KNOT Offshore Partners

First Quarter 2018 Earnings

June 6, 2018 at 12:00 p.m. Eastern

CORPORATE PARTICIPANTS

John Costain – *Chief Executive Officer, Chief Financial Officer*

PRESENTATION

Operator
Good day, and welcome to the KNOT Offshore Partners First Quarter 2018 Earnings conference call. All participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key followed by zero. After today's presentation there will be an opportunity to ask questions. If you'd like to ask a question, you may press star then one on your touchtone phone. To withdraw the question please press star then two. Please note, today's event is being recorded.

With that, I'd like to turn the conference over to John Costain. Please go ahead.

John Costain
Thank you. If any of you have not read the earnings release or slide presentation, they're both available on the investor section of our website. On today's call, our review will include non-US GAAP measures such as distributable cash flow and adjusted earnings before interest, taxation, depreciation, amortization, the EBITDA. The earnings release includes a reconciliation of these non-GAAP measures to the most directly comparable GAAP financial measures.

A quick reminder that any forward-looking statements made during today's call are subject to risks and uncertainties, and these are discussed at length in our annual and quarterly SEC filings. As you know, actual events and results can differ materially from those forward-looking statements. The partnership does not undertake a duty to update any forward-looking statements.

So, introduction.

KNOT Offshore Partners, KNOT, focuses on the shuttle tanker segment. The individual tanker is field specific and an integral component in the offshore oil production value chain.

Shuttle tankers operate in a niche space and under non-volume based contracts, transporting oil from the offshore production units to shore side. After being built to the Charterer's requirements the tankers are generally used on specific oil fields, enabling the partnership to yield both sustainable and stable revenue longer term.

Oil production continues to move further offshore, so shuttle tankers operate in a space which will see substantial growth in the coming years. Some of the largest discovered oil reserves in the southern hemisphere are in the pre-salt 130 kilometers off the coast of Brazil. The average annual production operates in the pre-salt layer, which includes portions of Petrobras and its partners, in 2017, were the largest in the company's history, reaching a mark of 1.29 million barrels per day.

Although our MLP is young, our sponsor is a very experienced operator, having been involved in the design and construction of this type of vessel, growing his fleet organically for more than 30 years.

In the last 18 months, the MLP has acquired *Raquel Knutsen* in Q4 '16, *Tordis* in Q1 '17, *Vigdis* in Q2, *Lena* in Q3, *Brasil* in Q4, and in Q1 '18, *Anna Knutsen*. We have achieved these acquisitions through a combination of common and preference issues, together with refinancing's and revolving credit facilities. This has enabled us to grow our distributable cash flow cover to the current level, and improve the long term outlook for the MLP.

Our sponsor, Knutsen NYK, is according to Clarkson Platou research, part of the largest shipping group in the world, and NYK is a major company in the Mitsubishi family. In a space of just under five years,

the fleet has grown 300%, to 16 vessels with an average age of about 4.75 years.

Now, turning to the presentation.

Looking at Slide 3, the Financial Highlights.

For the first quarter of 2018, the partnership generated its best set of results. All of the following are our highest figures on both an aggregate and a per unit basis.

Total revenue of $68 million, operating income of $31.9 million, net income of $30.7 million, and adjusted EBITDA of $53.4 million. The partnership generated distributable cash flow at $27.9 million, and after declaring a cash distribution of $0.52 per unit, this gives a coverage of 1.55 for the quarter. During the quarter, the fleet operated 99.6% utilization per scheduled operations.

Since our initial public offering in 2013, we've declared and paid common unit distributions of $9.78. So our initial investors have received a total return of $0.47. Our current distribution is stable at around 10%.

On the 30th of January, 2018, the partnership closed a $100 million senior secured credit term loan facility with a consortium of banks, in which Bank of Tokyo-Mitsubishi UFJ acted as agent. This was secured on the *Torill Knutsen* with a margin of 2.1% over LIBOR.

On the 1st of March, 2018, the partnership acquired the shuttle tanker *Anna Knutsen* from Knutsen NYK for a purchase price of $120 million. After acquisition, there was approximately $74.4 million of debt secured on the vessel.

Slide 4, the Income Statement.

The total revenues were $68 million for the three months ended 31 March, 2018, (Q1) and compares to $61.6 million for the three months ended December 31st, (Q4).

The increase in revenues was mainly due to increased earnings from the *Brasil Knutsen*, as she was included in the results of operations from the 15th of December, 2017, and one month of earnings on the *Anna Knutsen* included from the 1st of March, plus a full quarter of earnings from the *Carmen Knutsen*, which incurred offhire in the fourth quarter, due to both scheduled drydocking and subsequent propeller repairs. The increase was partly offset by reduced revenues from the *Raquel Knutsen* as a result of 4.5 days offhire, reduced revenues from *Brasil Knutsen*, as she started scheduled drydocking at the end of the quarter, and two additional calendar days in Q4, compared to Q1.

Vessel operating expenses for the first quarter 2018 of $13.2 million, a decrease of $1.9 million from the $15.2 in Q4 2017. The decrease is mainly due to the bunkers consumption in connection with the scheduled drydocking and propeller repairs of the *Carmen Knutsen* that was charged in the fourth quarter. This was partially offset by higher operating expenses due to the *Brasil Knutsen* and *Anna Knutsen* being included in the results from operations from December 15th and the 1st of March, 2018, respectively.

General administration expenses of $1.3 million for the first quarter were unchanged from the 4th quarter.

Depreciation of $21.6 million for Q1, an increase of $1.5 million. The increase is mainly due to the *Brasil Knutsen* and *Anna Knutsen* being included in operations from the 15th of December and the 1st of March. As a result, operating income from Q1 was $31.9 million, compared to $25 million in Q4.

Interest expense for Q1 was $10.6 million, compared to $9.2 million in Q4. The increase is mainly due to additional debt incurred in connection with the acquisitions.
Realized and unrealized derivative gains were $10 million in Q1, compared to $3 million in Q4. The unrealized non-cash elements of the mark-to-market gain was $9.2 million for Q1, compared to $3.8 million for Q4.

Of the unrealized gain for the first quarter 2018, an 8.9 related to mark-to-market gains on interest rate swaps, due to the swap rate during the quarter, the comparison for Q4 was a mark-to-market gain of $4.6 million, and an unrealized loss of $0.8 million related to the foreign exchange contracts due to the strength of the US dollar against the NOK. As a result, net income for the Q1 was $30.7 million compared to $18.6 million for Q4.

Slide 5, Adjusted EBITDA.

In Q1, the partnership generated EBITDA of $53.4 million, compared to $45.1 million for Q4. Adjusted EBITDA refers to earnings before interest, taxation, depreciation, and amortization, and other financial items that provides a proxy for cash flow.

Adjusted EBITDA, of course, is a non-US GAAP measure used by our investors to measure partnership performance. With a wasting asset like a vessel, younger fleets tend to produce lower EBITDAs for every dollar invested. The annuity effect reduces the annual loss in the early years, which is factored into the replacement CapEx calculation for the distributable cash flow.

At the end of Q1, KNOT fleets had 16 vessels with an average age of 4.7 years, compared to the rest of the industry average of shuttle tankers excluding KNOT, of around 12 years. Since the formation of KNOT we have very high levels of vessel utilization, on average around 99.6% of scheduled operations. Financially, this translates into a continually higher and increasing predictable revenue, adjusted EBITDA, and discounted cash flow as more vessels are added to the fleet.

Slide 6, Distributable Cash Flow.

Another non-US GAAP measure to measure estimated distribution sustainability.

Distributable cash flow (or DCF) represent the net income adjusted for depreciation, unrealized gains and losses from derivatives, and foreign exchange, distributions on a Series A Convertible Preferred Units, and other non-cash items, and estimated maintenance and capital for dry-docking and replacement capital expenditures, which are required to maintain long-term operating capacity of, and therefore, the revenue generated by the partnership capital assets.

DCF was $27.9 million in Q1, the comparison $21.5 million in Q4, but we maintained our distribution level for Q1 at $0.52 per unit, equivalent to an annual distribution of $2.08. The distribution coverage ratio is our highest ever recorded, at 1.55 for Q1.

Impacting the calculation for the full year, 2018, 1/3 of the time charter fleet will complete dry-dockings between May and November 2018. More specifically, the partnership's earnings for the second quarter of 2018 will be affected by the planned five-year special survey dry-docking of the *Brasil Knutsen*, which was off hire for 56 days, including mobilization back and forth to Brazil. The dry-docking of *Brasil Knutsen* was completed on time and within budgeted costs.

Offsetting this off-hire will be the *Anna Knutsen*, expected to operate for the entire second quarter.

The *Hilda* is due her first five-year special survey dry-docking in the third quarter of 2018, and the *Torill* and *Ingrid Knutsen* are due for their first five special survey dry-docking in the fourth quarter of 2018. These vessels are operating the North Sea and will undergo dry-docking in Europe and are expected to incur off-hire times of approximately 18 to 20 days per vessel, as well as off hire on these vessels with positional bunker costs are expensed, impacting the 2018 results. Nevertheless, whilst we have not guided financial results for 2018, we expect a coverage ratio of a little over 1.3 on average for the year.

The average coverage ratio was 1.26 for the full year in 2017.

End Q1, the partnership had interest rate swap agreements totaling $645 million, on which the partnership received interest based on LIBOR and pays an average interest rate of 1.73%. These have an average maturity of approximately 4.5 years. Whilst the partnership financial results are impacted by changes in the market priority swaps, the cash flow is stabilized, mitigating the interest rate impact on the DCF.

We also see rising interest rates in the US in 2018 and ’19, together with increasing replacement Capex provisions charged on our vessels as they get older; however, our coverage has increased from earlier years, and our full year estimates for 2018 and ’19 look solid.

KNOT has an elevated yield compared to most MLPs and is focused on building coverage and deleveraging, as today it is not making accretive investments. Given the quality and market position of the sponsor, together with the shuttle tanker outlook, this yield is elevated and a very attractive value proposition.

There is, therefore, little benefit to the MLP in the short term to increase the distribution when yield is close to 10%. We continue to see double digit distributions as a signal our investors will prefer, increased coverage through investments, and secondly, deleveraging, rather than increasing dividends. The growing coverage ratio gives the partnership more flexibility regarding both our capital base and distributions going forward.

Slide 7, the Balance Sheet.

At the end of Q1, the partnership had $57.1 million in available liquidity, which consisted of cash and cash equivalents of $44.1 million, and $13 million of capacity under its revolving credit facilities. The revolving credit facilities mature in June and August 2019. Given the increasing fleet size, we hope to expand these facilities. We have a predictable cash flow, a healthy liquidity position, and with the Torill refinancing, no significant balloon repayments until 2019.

The partnership’s total interest bearing debt outstanding as of the 31st of March 2018 was $1.133 billion, net of debt issuance costs. The average margin was approximately 2.1% over LIBOR for Q1.

On March 1, 2018, the partnership acquired the shuttle tanker *Anna Knutsen* from Knutsen NYK for a purchase price of $120 million, less $105 million of debt, net of capitalization fees. There were other purchase price adjustments totaling $5.3 million. On its closing, the partnership repaid $32 million of the indebtedness, leaving an aggregate of approximately $74 million. The debt is repayable in quarterly installments with a final balloon payment of $57.1 million due in March 2020. It has a margin of 2%. The purchase price of the *Anna* acquisition was settled in cash.

As well as the acquisition, other significant transactions affecting the balance sheet occurred in January 2018 when the partnership subsidiary that owns the vessel *Torill Knutsen* closed $100 million senior secured term facility with a consortium of banks, in which the Bank of Tokyo--Mitsubishi UFJ acted as

agent.

The new facility is repayable in 24 consecutive quarterly installments with a balloon payment of $60 million due on maturity. It has a margin of 2.1% maturing in January 2024. The facility refinanced a $73.1 million loan facility associated with the vessel, that bore interest at a margin of 2.5%, and was due to be repaid in full on November 2018, a much larger loan with a significantly lower margin.

Slide 8, Long-term Contracts by Leading Energy Companies.

The *Windsor Knutsen* has been on charter to a subsidiary of Royal Dutch Shell since October of 2015. After the initial two-year period, Shell lifted the first of six annual extension options. The next option is declarable in July, and the vessel has a competitive option rate fully reflecting the current market. So Shell, we believe, are likely to continue using this vessel for the long term.

Bodil Knutsen, our largest shuttle tanker operating in the North Sea, is ice class and on charter for Statoil AS until May 2019. Following the end of the charter, there are five annual extension options.

Torill and *Hilda Knutsen* operate on the Goliat, the first field to be developed in the Barents Sea, and it currently represents the world's most northerly offshore development. It is estimated that the Barents Sea contains nearly half of the discovered oil reserves in the Norwegian shelf. Starting production in 2016, the estimated lifetime of the field is 15 years. It has an estimated recoverable reserves equivalent to about 178 million barrels of oil.

And *Hilda* and *Torill* are two of three specially designed shuttle tankers built to operate in this arctic environment. Never have shuttle tankers had to meet such strict requirements. Our vessels are heavily winterized allowing the crew, and, hence, the vessels to operate safely in temperatures down to -30 degrees Celsius.

After the initial five-year term on both vessels, there are five annual extension options. We expect ENI trading and shipping SPA, (ENI), to lift the first of these annual extension options for *Hilda* in July, and *Torill* in October. Our bankers are certainly relaxed. We have recently completed refinancing on both vessels on significantly better terms than our previous deals.

Today, many Charterers like this annual option type of agreement, both for the commercial flexibility and because of the imposition of more onerous financial disclosure requirements. There is a much lower impact in the accounts of the Charterer. For the MLP, this mix of short and long Charterers in the portfolio is useful, because as well as tailoring solutions for the Charterers wishes, we believe asset prices could firm, and the market will tighten in the coming years. And given the size of our fleet and therefore commercial footprint, some measure of contract flexibility is desirable.

Four of our vessels are on long-term [indiscernible] chartered through 2023 with Petrobras Transpetro. These vessels are amongst the youngest in the Petrobras fleet, delivering between 2011 and 2012 and are heavily utilized. *Dan Sabia* and *Dan Cisne* are a unique size, and *Fortaleza* and *Recife Knutsen* have shallow drafts with lots of thruster capacity.

Delivered in 2013, the *Carmen* is on charter direct to Repsol Sinopec until 2023.

The *Ingrid* was delivered in December 2013, and is operating in the North Sea on a time charter for Standard Marine Tonsberg, a Norwegian subsidiary of ExxonMobil. This will expire in the first quarter of 2024. The charter has options to extend the charter up to five one-year periods.

The *Raquel Knutsen* was delivered in March 2015 and operates under a charter that expires in the first quarter of 2025 to Repsol Sinopec in Brazil. There are options to extend until 2030.
The *Tordis, Vigdis*, and *Lena Knutsen* are on five-year charters to Brazil Shipping One, a subsidiary of Shell. These will expire in 2022, and the Charterer has options to extend with two additional five-year options totaling fifteen years.

The *Brasil* and *Anna Knutsen* are on charter for Galp Energia until 2022, with options to extend until 2028.

The KNOP fleet have an average remaining fixed-contract duration just under four years, and an additional 4.7 years on average in Charterers option. Whilst we currently have no further dropdown candidates, which means no near term equity requirement, given the market outlook, we will expect to be able to grow the MLP significant in the coming years.

Slide 9, Refinancing our Fleet.

We have a significant refinancing due in 2019, with the current debt secured on *Fortaleza, Recife, Windsor, Bodil*, and *Carmen* requiring renewal, and a smaller commercial tranche due on the *Ingrid* toward the end of 2018.

We're starting the process, and we'll look to finalize a new facility around September 2018. This will be secured against all of the above vessels. Compared to our current leases, the average margin on our new facility remains in line. With the package as currently presented, we anticipate that we will be able to increase the overall size of the attached credit line by around $20 million. At draw down, the structured debt element will match the borrowing at the end of June, giving a small advantage.

In summary, Slide 10,

KNOT Offshore Partners should be considered as a mobile pipeline business with fully contracted revenue streams, and, therefore, a great fit with the MLP market.

Since being awarded its first year contract in 1984, Knutsen has grown organically for over 30 years as the business has been able to build into a sizable fleet of these tankers, currently 29 units.

This quarter we report, the partnership's highest ever quarterly performance, both in absolute and per unit terms for revenue, profit, EBITDA, and distributable cash flow. Yet, another quarter with stronger financial performance and substantial increase in all financial measures.

Not surprising when set against the acquisition program, one vessel, *Raquel,* was added into the fleet in Q4 2016. Four vessels were added to the fleet during 2017: the *Tordis*, first quarter; the *Vigdis*, second quarter; *Lena*, third quarter; and *Brasil*, fourth quarter. A sixth vessel in a sixteen-month period, the *Anna* was added on the 1st of March, 2018.

KNOT has very good access to financing, in the last year to finance the growth acquisitions, we have raised both $211 million worth of new equity, and $200 million worth of long-term debt, with $25 million of credit facilities, all on attractive terms.

KNOT is well placed to complete in future tenders. We have a solid and profitable contract base, generated by our modern fleet, which, by the end of December, has an average age of around 4.75 years.

Since the formation of KNOP, we have had very high levels of vessel utilization, on average around 99.6%. Financially, this translates into high and increasingly predictable revenue, adjusted EBITDA, and a discounted cash flow as more vessels are added to the fleet.

No one has more expertise in operating the sophisticated shuttle tanker of this nature than KNOT Offshore Partners, and we operate these vessels with real expertise. Today's supply is tightening, and the market is expanding. And with tenders back, the sponsor expects to build a further drop down inventory.

We have a large and financially strong and supportive sponsor who knows this market as well as anyone.

We remain a very attractive value proposition with a core for distribution of $0.52, equating to around 10% as an annual distribution.

Thank you, and that concludes the narrative for the slides. If anybody has any questions, I'll be happy to take them.

QUESTIONS AND ANSWERS

Operator
We will now begin the question and answer session. To ask a question, you may press star then one on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw the question, please press star then two. Once again, if you'd like to ask a question today, please press star then one.

And our first question today comes from Hillary Cacanando with Wells Fargo. Please go ahead.

Hillary Cacanando
Hi, thanks for taking my question. So, I'm sorry, I missed part of the presentation. Did you talk about the recontracting opportunity for *Windsor, Hilda*, and *Torill*, by any chance, or? I'm sorry if you've already—

John Costain
Well, yes, I mentioned it, Hillary. I just briefly said that we have a structure on the older ships which is one option one, option one, for five or six-year periods. *Windsor* has already had one of those option periods exercised. In July, *Hilda* and *Windsor*, their Charterers have to declare whether they're going to exercise those options, and we've not received an indication that they're not. And given the late stage now, I think it's highly likely we can assume that they will lift those options, or alternatively, the vessels will get redelivered, which is unlikely in the current market environment.

As I said in the presentation, we feel it's good to have a mix between long and short contracts because the market is tightening and the asset prices are starting to come back. So it's good to have a mix, and it's also good for the Charterers to have a bit of flexibility as well. So it cuts both ways really. Well, yes, today we have quite a lot of ships with these structures. Given also the financial constraints of the Charterer having short contracts, it works on a financial disclosure basis for them, as there's much lower impact on their accounts. And we see more of these types of agreements coming into play.

Hillary Cacanando
I'm sorry. So you said you think these options will be exercised?

John Costain
Yes, definitely. There's no reason why they wouldn't be. They haven't really ordered the new ship any,

for instance on the *Hilda*, so they either redeliver the ship, and don't move the oil from the platform, or they carry on with the charter. Normally, it would take probably three years to build a vessel like that, so it's only a month away from exercise, so I think it; unlikely they will do anything other than exercise at this point, as they haven't come back and told us anything other than—.

Hillary Cacanando
Okay. And then I know there's no more assets in the dropdown pipeline. Is it because the assets at the parent level have not enough, the contract length is not long enough, or it just they—?

John Costain
We tend to put our new ships on longer contracts, all the better-quality contracts, really. The sponsor has quite a lot of the older tankers. I think looking at the MLP today, it's not going to stand still in the long run. It is a nicely formed shipping company, effectively they're a mobile pipeline company with 16 very well-positioned tankers which are specialized in and very good at revenue on contracts.

I just look at it as an investment. It's very attractive for the sponsor to use the vehicle for carrying on growing. But, we're obviously having internal discussions as to the best way forward. What we're not going to do is go out into the market and just press and win contracts at numbers that are not realistic.

And then when we've looked at the last contract, the Petrobras one in Brazil, we were quoted, from the yard that we went to, they wanted a 10% increase in the price; and rates that are being bandied about are quite significantly lower than what the normal market rate has been in recent years, so I was quite surprised. Anyone dealing with Petrobras today has to make a really attractive offer to get a deal; that's where we read it. I don't know what else, but I think you can guarantee that we are in talks with other Charterers. There is an appetite toward the ships, and I think we're comfortable with the present situation.

Hillary Cacanando
Okay. All right, that's it for me, thanks John.

John Costain
Okay. Thanks, Hillary.

Operator
The next question comes from Robert Silvera, with RE Silvera and Associates Marine Surveyors. Please go ahead.

Robert Silvera
Thank you, gentlemen, looks like a very nice job that you've done. My first question has to do with your Series A convertible preferred units. They were no change in the number from last quarter to this quarter. Are you still in the market to want to purchase some of those to reduce the number?

John Costain
No, not today. My own view on it is, it's not necessarily the sponsor's, but we don't want to load too many prefs into the market if we don't have to, because obviously it creates a problem for the common units.

Our competitor, at 20% common—sorry, 20% prefs, which I think is a little bit high--I think I like the amount we have today. I don't particularly want to put more in; we're not in the market for that sort of capital. But obviously, we never say never because the preference market might be open when the common unit market's closed. As of today, we've finished our business, and I think the answer's probably no.

On those preference units, the strike price has drifted up to $24.50 because we've been reporting good results on the companies, so that's very positive and they are working very well for the MLP, because they're definitely very accretive, but we have to balance that against the fact the equity yield strip is on top of the common unit holder.

Robert Silvera
Right. My general concern is because of world-wide interest rates are starting to climb a little bit. My second question has to do with what your average debt per vessel is, and whether you see yourselves reducing that average debt per vessel.

John Costain
Well, inevitably our debt is structured debt first, mortgage priority debt, which is relatively cheap compared to equity. We have a very good quality sponsor, and we have very good quality end user contracts that support that sort of level of debt. We obviously will take the opportunity if we're not doing accretive acquisitions to reduce the debt level, so we will reduce the debt. Basically we have 1.1 Billion on 16 ships.

Robert Silvera
Yes, you are doing that. Good, you are doing that average debt per vessel. I realize taking on new vessels increases the total debt, but the average across all the vessels is what I'm concerned about, that it's going down in a healthy manner.

John Costain
Well, just--Yes, it goes down on the normal repayment schedule—

Robert Silvera
Let me ask you another question. It goes down by program, I realize that, but you're not taking any extra cash to alleviate a debt level on a faster basis then?

John Costain
No, we're paying—these are very, very good contracts. We're going to use the—

Robert Silvera
Right

John Costain
We contract directly with the oil majors for oil delivery so we can leverage quite well against that because obviously there's no intermediary here. The vessel is actually acting as a pipeline, so the cash flows are very secure, so you can leverage accordingly, and if you have a long contract like we have, it's quite straightforward to do that. It's always operated with a decent amount of leverage. And basically, with these contracts, they are competitive, and therefore you have to have leverage. We're paying 10% yield today in our MLP, so this is necessary]—

Robert Silvera
Right, I know. I'm—that's one of the main reasons we're stockholders in it, because of the nice yield, and the soundness of your balance sheet, and the way you're running the business; we're very pleased. Do you have any feeling for the average resale value of the vessels that you had? If you had to say, "Okay, here's the whole fleet, here's what the average price of the whole fleet would be per vessel."

John Costain

On a break up, charter-free basis, you mean? So basically, you're discounting the whole contracts that are in place, and plugging them into the market as a shuttle tanker?

Robert Silvera
Right.

John Costain
Probably—

Robert Silvera
Yes, I'm just trying to look at the assets by the assets themselves. Not as a business, because obviously the business is doing very well, paying the nice dividends, etc., but I'm just looking at it from the standpoint of you have value in every ship. And of course, each ship is different value if it was going to be resold. So, taking an average across all the ships, where would you place a reasonable market value as an average number? And then also, what would the average scrap value of those vessels be?

John Costain
Well, the average price point is about $16/$17 a unit I would say, and then the premium is basically for the Charters and the position of sponsor in markets.

Robert Silvera
Right.

John Costain
But there is a subjectivity in the hard value, but it's pretty decent in relation to the unit. Obviously, it gets even more interesting as the dollar weakens more because it has weakened in the last two years, and I think that's probably why you see it in the marine space. You're looking at the marine investment now, which is probably a bit unfair, but there you go. In the marine space, generally in the last few weeks you've seen quite a lift in the prices of a lot of these companies, basis the fact that the oil prices are starting to creep up.

Bear in mind in the US in the last two years, if you look at the benchmark of the US dollar against say the SDR, the special drawing rights currency of the IMF, it's lost about 10% of its value. And also, you'll see the dollar interest rates are going up relative to the rest of the world. So, the dollar's actually losing ground. It is the go-to currency of the world still, but actually in positional terms it's losing a bit of value, and that makes shipping investments interesting, and that's why they've lifted. But we're a bit more stable than that. We're somewhere between that, and a pipeline, because obviously—

Robert Silvera
Right.

John Costain
Where it impacts is obviously, and where your question is interesting is obviously the re-contracting activity when we build a new ship, and we go unfixed. And that obviously impacts the level at which the pricing is determined for the whole contract. So, the Charterer will generally look for a point in the market where the asset prices are starting to climb, and we are there today, and we see a tick up in activity because of it. They're not stupid either, they realize when they look at the market they see if the price is bottoming out, it's both advantageous for them, but it's also advantageous for the owner, because obviously if you're at the bottom, and the market is starting to climb, and you order a ship, and you have a five-year contract, the residual risk at the end of the contract for the owner is lower, because the starting price was lower.

And for the Charterer, he gets a double benefit because he'll know going into the market at a lower figure the weighted average cost of capital is lower on that basis, as the residual risk is lower. And also the starting price, the asset price is lower, so that's what the game is with the market a little bit.

I can't say that we're not linked to the ship prices, but we're a bit distant from what they cost. We're not always facing the market. We do a contract, and generally it's on the life of the field. But you can never say never, and it depends on who moves into the market and what actually happens with it. So, your question's very valid. But yes, today, it's lower obviously than the unit price, but I think over time—

I think what's also interesting, as interest rates go up, relatively speaking a four- or five-year-old vessel is cheaper than a new build because it's actually been paid down a bit, so it actually makes it mildly more competitive because you're getting the annuity effect, and if interest rates do go up significantly, it's not necessarily a bad thing for a company with a lot of slightly older tonnage.

Robert Silvera
Interesting

John Costain
These things happen, but it's just maths really, when you start to think about it. With all the US capital market stuff there's always a circular argument for everything, you can always just divide everything if you're looking at from the other point of view. But the impressions are interesting, yes.

Robert Silvera
Okay. The other thing is in the VLCC market you see the average value—roughly speaking—of VLCCs around $16 million from scrap value point of view. If you were to look at your ships, now your ships are obviously much more specialized. Would the scrap value on our ships be considerably different than that, or would that same steel pricing be equivalent?

John Costain
No, because these are half the size, they're half the size. They're about 25,000, 27,000 tons-worth of steel, where a VLCC has about 45,000 to 50,000 tons in.

Robert Silvera
Okay, so they'd be about eight—

John Costain
The current scrap prices are—I think the current scrap price is about $400 a ton, so it's a little bit more than that.

Robert Silvera
Okay. My last question is—

John Costain
[Indiscernible].

Robert Silvera
I realize we're not in the market to scrap any of our vessels, I understand that [indiscernible]. But, I'm just trying to get a hard number in my mind what the steel is worth there in all versus our vessels, etc. Now, the last question I have is what percent of our debt is fixed?

John Costain
Well, we have derivative instruments basically, so $645 million out of the $1.1 billion is fixed, so that reflects the contracts bit you could say as well, because obviously we have about four, four or five ships with one-year contracts, so you'd probably match the long-term contracts up with the fixed portion.

Robert Silvera
Okay. Well, good. Thank you very much. I am very, very pleased with the job you've done. Keep up the good work.

John Costain
Thank you.

CONCLUSION

Operator
At this time, this will conclude today's question and answer session. I'd like to turn the conference back over to John Costain for any closing remarks.

John Costain
Now, thank you very much. I appreciate everybody who's taken the time and interest in coming on the call, and hopefully we'll continue with the good quarters going forward. Thank you.

Operator
The conference is now concluded. Thank you for attending today's presentation. You may now disconnect your lines.