

MC SHIPPING INC  
Form 10-Q  
November 12, 2004

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**SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549**

**FORM 10-Q**

**QUARTERLY REPORT UNDER SECTION 13 OR 15 (d)  
OF THE SECURITIES EXCHANGE ACT OF 1934**

**Quarter ended September 30, 2004**

**Commission File Number:  
1-10231**

**MC SHIPPING INC.**

(Exact name of the registrant as specified in its charter)

**LIBERIA**

(State or other jurisdiction  
of incorporation or organization)

**98-0101881**

(I.R.S. Employer  
Identification No.)

**Richmond House, 12 Par-la-ville Road, Hamilton HM CX, Bermuda**

(Address of principal executive offices)

**441-295-7933**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES  NO

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

**Class**

**Shares outstanding at  
September 30, 2004**

**Common stock,  
par value \$.01**

**8,765,974**



**MC SHIPPING INC. AND SUBSIDIARIES**

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**PART I: FINANCIAL INFORMATION****ITEM 1: FINANCIAL STATEMENTS**

**MC SHIPPING INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(UNAUDITED)

|  | <b>ASSETS</b>        |                      |
|--|----------------------|----------------------|
|  | SEPTEMBER 30<br>2004 | DECEMBER 31<br>2003  |
| <b>CURRENT ASSETS</b>  |                      |                      |
| Cash and cash equivalents  | \$ 10,957,780        | \$ 16,446,582        |
| Restricted cash  | 148,597              | 615,455              |
| Hire receivables   | 7,426                | 13,111               |
| Recoverable from insurers  | 609,821              | 807,530              |
| Inventories  | 623,487              | 582,388              |
| Receivables from affiliates  | 61,659               | 76,094               |
| Prepaid expenses and other current assets  | 1,139,966            | 1,186,015            |
| <b>TOTAL CURRENT ASSETS</b>  | <b>13,548,736</b>    | <b>19,727,175</b>    |
| <b>VESELS, AT COST</b>   |                      |                      |
| Less - Accumulated depreciation  | 109,303,246          | 109,303,246          |
|  | (50,639,413)         | (47,114,005)         |
|  | 58,663,833           | 62,189,241           |
| <b>FURNITURE &amp; EQUIPMENT, AT COST</b>  |                      |                      |
| Less - Accumulated depreciation  | 27,793               | 24,304               |
|  | (27,685)             | (21,737)             |
|  | 108                  | 2,567                |
| <b>OTHER ASSETS</b>  |                      |                      |
| Dry-docking costs (net of accumulated amortisation of \$3,050,966 at September 30, 2004 and \$2,006,533 at December 31, 2003)  | 3,934,656            | 4,894,163            |
| Debt issuance cost (net of accumulated amortisation of \$1,580,048 at September 30, 2004 and \$1,472,654 at December 31, 2003) | 326,495              | 502,870              |
| <b>TOTAL ASSETS</b>  | <b>\$ 76,473,828</b> | <b>\$ 87,316,016</b> |

THE ACCOMPANYING NOTES ARE AN INTEGRAL  
PART OF THESE CONSOLIDATED FINANCIAL STATEMENTS.



**MC SHIPPING INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
(UNAUDITED)

**LIABILITIES AND SHAREHOLDERS' EQUITY**

|   | SEPTEMBER 30<br>2004 | DECEMBER 31<br>2003  |
|---|----------------------|----------------------|
| <b>CURRENT LIABILITIES</b>  |                      |                      |
| Accounts payable  | 251,365              | \$ 612,759           |
| Hire received in advance  | 584,843              | 584,843              |
| Accrued expenses  | 2,608,539            | 4,435,166            |
| Accrued interest  | 254,649              | 1,193,420            |
| Current portion of long term debt   | 4,179,553            | 4,179,553            |
| 11.25% Senior Notes called as of Nov 1, 2004  | 21,100,000           | -                    |
| <b>TOTAL CURRENT LIABILITIES</b>  | <b>28,978,949</b>    | <b>11,005,741</b>    |
| <b>LONG TERM DEBT</b>   |                      |                      |
| 11.25% Senior Notes due 2008  | -                    | 27,640,000           |
| Secured Loans   | 15,935,262           | 19,441,690           |
| <b>TOTAL LONG TERM DEBT</b>   | <b>15,935,262</b>    | <b>47,081,690</b>    |
| <b>TOTAL LIABILITIES</b>  | <b>44,914,211</b>    | <b>58,087,431</b>    |
| <b>SHAREHOLDERS' EQUITY</b>   |                      |                      |
| Common stock, \$.01 par value - 20,000,000 shares authorised<br>8,765,974 shares issued at September 30, 2004 (8,530,238 at<br>December 31, 2003) | 87,660               | 85,302               |
| Additional paid-in capital  | 51,280,010           | 52,135,576           |
| Less : Treasury stock, at cost - None at September 30, 2004 (221,730<br>shares at December 31, 2003)  | -                    | (891,806)            |
| Accumulated deficit   | (19,880,775)         | (21,905,096)         |
| Accumulated comprehensive income  | 72,722               | (195,391)            |
|   | <b>31,559,617</b>    | <b>29,228,585</b>    |
| <b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>   | <b>\$ 76,473,828</b> | <b>\$ 87,316,016</b> |

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**MC SHIPPING INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**

For the Quarters ended September 30, 2004 and September 30, 2003  
(UNAUDITED)

|  | SEPTEMBER 30<br>2004 | SEPTEMBER 30<br>2003 |
|--|----------------------|----------------------|
| CHARTERHIRE AND OTHER INCOME               | \$ 8,127,173         | \$ 7,911,048         |
| <b>COSTS AND EXPENSES</b>                  |                      |                      |
| Commission on Charterhire                  | (186,890)            | (210,544)            |
| Vessel Operating Expenses                  | (4,129,633)          | (4,899,586)          |
| Amortisation of Dry-docking Costs          | (334,111)            | (359,701)            |
| Depreciation                               | (1,150,659)          | (1,549,717)          |
| General and Administrative Expenses        | (857,011)            | (253,775)            |
| OPERATING INCOME                           | 1,468,869            | (637,725)            |
| <b>OTHER INCOME/(EXPENSES)</b>             |                      |                      |
| Interest Expense                           | (965,152)            | (1,096,591)          |
| Interest Income                            | 30,241               | 38,065               |
| Loss on Repurchases of Notes               | (40,121)             | -                    |
| Gain on sale of vessels                    | -                    | 1,785,253            |
| NET INCOME                                 | \$ 493,837           | \$ 1,364,452         |
| <b>BASIC AND DILUTED PER SHARE AMOUNTS</b> |                      |                      |
| Net Income                                 | \$ 0.06              | \$ 0.17              |
| <b>WEIGHTED AVERAGE NUMBER OF</b>          |                      |                      |
| SHARES OUTSTANDING                         | 8,736,197            | 8,250,526            |

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**MC SHIPPING INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**

For the nine months ended September 30, 2004 and September 30, 2003  
(UNAUDITED)

|  | SEPTEMBER 30<br>2004 | SEPTEMBER 30<br>2003 |
|--|----------------------|----------------------|
| CHARTERHIRE AND OTHER INCOME                             | \$ 23,904,609        | \$ 28,109,416        |
| <b>COSTS AND EXPENSES</b>                                |                      |                      |
| Commission on Charterhire                                | (574,020)            | (728,064)            |
| Vessel Operating Expenses                                | (12,381,627)         | (14,085,796)         |
| Amortisation of Dry-docking Costs                        | (1,044,431)          | (826,747)            |
| Depreciation   | (3,527,808)          | (6,942,054)          |
| General and Administrative Expenses                      | (1,924,164)          | (925,948)            |
| OPERATING INCOME   | 4,452,559            | 4,600,807            |
| <b>OTHER INCOME/(EXPENSES)</b>                           |                      |                      |
| Interest Expense   | (2,883,643)          | (3,816,466)          |
| Interest Income  | 92,286               | 76,990               |
| Provision for impairment loss on vessels                 | -                    | (2,918,650)          |
| Gains on Repurchases of Notes                            | 363,119              | 2,620,477            |
| Gain on sale of vessels                                  | -                    | 1,785,253            |
| NET INCOME   | \$ 2,024,321         | \$ 2,348,411         |
| <b>BASIC AND DILUTED PER SHARE AMOUNTS</b>               |                      |                      |
| Net Income   | \$ 0.24              | \$ 0.28              |
| <b>WEIGHTED AVERAGE NUMBER OF<br/>SHARES OUTSTANDING</b> |                      |                      |
|  | 8,544,616            | 8,243,665            |

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**MC SHIPPING INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**

For the nine months ended September 30, 2004 and September 30, 2003  
(UNAUDITED)

|  | SEPTEMBER 30<br>2004 | SEPTEMBER 30<br>2003 |
|--|----------------------|----------------------|
| <b>OPERATING ACTIVITIES:</b>   |                      |                      |
| NET INCOME   | \$ 2,024,321         | \$ 2,348,411         |
| Adjustments to reconcile Net Income to net cash provided from operating Activities |                      |                      |
| Depreciation   | 3,527,808            | 6,942,054            |
| Amortisation of Dry-docking costs  | 1,044,431            | 826,747              |
| Amortisation of issuance costs   | 107,394              | 195,701              |
| Dry-docking Costs Capitalised  | (84,926)             | (4,917,566)          |
| Provision for impairment loss  | -                    | 2,918,650            |
| Gains on repurchases of Senior Notes   | (363,119)            | (2,620,477)          |
| Gain on disposal of vessels  | -                    | (1,785,253)          |
| Comprehensive income   | 268,113              | 184,246              |
| Changes in Operating Assets and Liabilities:                                       |                      |                      |
| Hire receivables   | 5,685                | (60,056)             |
| Recoverable from insurers  | 197,709              | 89,719               |
| Inventories  | (41,099)             | (31,283)             |
| Receivables from affiliates  | 14,435               | 80,518               |
| Prepaid expenses and other current assets  | 46,049               | (2,418,857)          |
| Accounts payable   | (361,394)            | 338,829              |
| Accrued expenses   | (1,497,891)          | 3,902,210            |
| Hire received in advance   | -                    | (599,895)            |
| Accrued interest   | (938,771)            | (1,358,870)          |
| <b>NET CASH PROVIDED FROM OPERATING ACTIVITIES</b>                                 | <b>\$ 3,620,009</b>  | <b>\$ 4,054,828</b>  |
| <b>INVESTING ACTIVITIES:</b>   |                      |                      |
| Variation in office equipment  | 61                   | (974)                |
| Sale of vessels  | -                    | 20,335,693           |
| Change in restricted cash  | 466,858              | 1,858,250            |
| <b>NET CASH PROVIDED FROM INVESTING ACTIVITIES</b>                                 | <b>466,919</b>       | <b>22,192,969</b>    |
| <b>FINANCING ACTIVITIES:</b>   |                      |                      |
| Repayments of long-term debt   | (3,506,428)          | (19,495,491)         |
| Repurchases of Senior Notes  | (6,107,900)          | (4,283,050)          |
| Debt issuance costs  | -                    | -                    |
| Issuance of stock  | 38,598               | 12,400               |
| <b>NET CASH USED BY FINANCING ACTIVITIES</b>                                       | <b>(9,575,730)</b>   | <b>(23,766,141)</b>  |
| DECREASE/INCREASE IN CASH  | (5,488,802)          | 2,481,656            |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD                                   | 16,543,107           | 14,061,451           |
| CASH AND CASH EQUIVALENTS AT END OF PERIOD   | \$ 10,957,780        | \$ 16,543,107        |

THE ACCOMPANYING NOTES ARE AN INTEGRAL

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PART OF THESE CONSOLIDATED FINANCIAL STATEMENTS.

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**MC SHIPPING INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 2004  
(UNAUDITED)**

**NOTE 1. BASIS OF PRESENTATION**

The accompanying unaudited consolidated financial statements of MC Shipping Inc. and subsidiaries (the "Company") have been prepared in accordance with United States generally accepted accounting principles for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of Management, adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the quarter ended September 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004. These consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K.

**NOTE 2. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES**

**ORGANIZATION:** The Company is incorporated in the Republic of Liberia and, through its subsidiaries, currently owns and operates thirteen second-hand vessels comprising seven liquid petroleum gas ("LPG") carriers, four containerships and two multipurpose seariver vessels.

**PRINCIPLES OF CONSOLIDATION:** The consolidated financial statements include the accounts of MC Shipping Inc. and its wholly-owned subsidiaries. All inter-company accounts and transactions have been eliminated.

**REVENUE RECOGNITION:** Charter revenues are derived from timecharters, voyage charters and bareboat charters. Timecharter and bareboat charter revenue is recognised on an accrual basis. Voyage charter revenue and related expenses are accounted for on the percentage of completion method.

**VESSEL REPAIR AND OVERHAUL:** Normal vessel repair and maintenance costs are charged to income when incurred. Costs incurred during dry-dockings and periodic inspections for regulatory and insurance purposes are deferred and charged to income rateably over the period of five years to the next intermediate or special survey dry-docking. For the vessels, which are earmarked for sale, dry-docking expenses are charged to expenses when incurred.

**VESSELS AND DEPRECIATION:** Vessels are stated at cost, which includes contract price and other direct costs relating to acquiring and placing the vessels in service. Depreciation is calculated, based on cost, less estimated salvage value, using the straight-line method, over the remaining economic life of each vessel. The economic life of LPG carriers is assumed to extend from the date of their construction to the date of the final special survey which is closest to thirty years from the date of their construction. The economic life of other vessels is assumed to extend from the date of their construction to the date of the final special survey, which is closest to twenty-five years from the date of their construction. If a vessel is used beyond its fifth special survey, its economic life is assumed to extend to the end of its current charter.

**IMPAIRMENT OF LONG LIVED ASSETS:** In accordance with Statement of Financial Accounting Standards No. 144, "Accounting for Impairment of long-lived Assets and for long-lived Assets to be Disposed of", the Company writes down the value of vessels to fair value when information, typically in the form of appraisals and cash flow forecasts, indicates that the carrying value of such vessels is not recoverable. Assets to be disposed of are valued at the lower of carrying amount or fair value less cost to sell. Depreciation is not recorded on the vessels that are earmarked for sale, as such vessels are included in the financial statements at their market value, and such value is reviewed at the end of each quarter.

**SEGMENT REPORTING:** The Company operates as a single segment, as Management internally evaluates the performance of the enterprise as a whole and not on the basis of separate business units.

**COMPREHENSIVE INCOME:** Comprehensive income consists of foreign currency translation adjustment and unrealised losses on cash flow hedges.

**DEBT ISSUANCE COSTS:** Debt issuance costs are being amortised, using the interest method, over the terms of the long-term credit facilities. The write-offs of debt issuance costs associated with the Company's repurchases and retirements of Notes and the prepayment and refinancing of debt are recorded as losses on debt extinguishment (or a reduction of Gains on repurchases of Notes). The write-offs of debt issuance costs associated with the Company's prepayment of secured debt at the time of the sale of vessels are recorded as a reduction of gains on disposals of vessels.

**INTEREST RATE SWAPS:** From time to time, the Company enters into interest-rate swap agreements to fix the variable interest rate of some of its outstanding debt (See Note 6). As such interest rate swaps are designated and qualifying as a cash flow hedge (i.e. hedging the exposure to variability in expected future cash flows that are attributable to a particular risk), the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income and reclassified into earnings in the same line item associated with the forecasted transaction in the same period during which the hedged transaction affects earnings. If a swap is cancelled, the cancellation cost is recorded as interest expense.

**INVENTORIES:** Inventories consist principally of lubricating oil and victualling and are stated at cost, determined by the first-in, first-out method.

**CASH AND CASH EQUIVALENTS:** Cash and cash equivalents consist primarily of deposits with banks.

**RESTRICTED CASH:** Restricted cash consists primarily of deposits with banks that are restricted to guarantee the Company's performance under various loan agreements.

**EARNINGS PER SHARE:** Basic and diluted earnings per share are calculated in accordance with FASB Statement No. 128, Earnings per Share. Basic earnings per share exclude dilution and are computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution that could occur if outstanding options were exercised or converted into common stock.

**TAXATION:** The Company is not subject to corporate income taxes in Liberia because its income is derived from non-Liberian sources. Additionally, the Company believes that it is not subject to corporate income taxes in other jurisdictions, including the United States.

### **NOTE 3. RELATED COMPANY TRANSACTIONS**

Until May 2004, the Vlasov Group was the main shareholder of the Company. On May 13, 2004, Vlasov Investment Corporation sold the 4,168,000 shares of Common Stock of MC Shipping that it owned (approximately 47.78%).

As of May 14, 2004, V. Investments Limited, V Ships Group LTD., V Holdings Limited, Greysea Limited, Close Securities Limited, Close Investment Partners Limited, Navalmar (UK) Limited, Bogazzi Fimpar SpA, and Enrico Bogazzi filed a joint Form 13D to report that they might be deemed to have shared beneficial ownership of 4,308,790 common shares, which represented approximately 49.39% of the common stock outstanding. Following the purchase of an additional 133,200 shares in the open market by Navalmar, V Investments and Navalmar control, since

September 3, 2004, over 50% of the outstanding stock of the Company.

Prior to March 28, 2003, V.Ships had been an affiliate of the Company, as it was 39% owned by the Vlasov Group, the main shareholder of the Company at that time. V.Ships was also owned 31% by Greysea Limited ("Greysea"), a Guernsey corporation controlled by certain senior officers and former officers of V.Ships, 19% by General Electric Capital Corporation and 11% by some officers of V.Ships. Following a change in the shareholding structure of V.Ships, V.Ships is now controlled 50% by Greysea and management and 50% by a third party independent investor group (4% warrants are held by lending banks).

Certain of the directors and executive officers of the Company are involved in outside business activities similar to those conducted by the Company. Mr Antony Crawford (Chief Executive officer, Chief Operating Officer, President and Director) is also the Chief Executive Officer of V Ships financial and commercial services division; he is a Director and minority shareholder of V Holdings Limited. Mr Bogazzi (Director) is involved in the business of purchasing, owning and selling cargo vessels through the Bogazzi Group of shipping companies. Mr Guy Morel (Director) is a Director and minority shareholder of Greysea, which indirectly owns a participation in V Ships. As a result of these affiliations, such persons may experience conflicts of interest in connection with the selection, purchase, operation and sale of the Company's vessels and those of other entities affiliated with such persons.

The By-Laws of the Company provide that many of the transactions giving rise to potential conflicts of interest are subject to review by the Audit Committee of the Company's Board of Directors which is also charged with the responsibility of monitoring and reviewing transactions to be entered into with affiliates.

The Company, via its wholly owned subsidiaries, has entered into Management Agreements with V.Ships for the technical operation of all the Company's fleet, excluding the seariver vessels which are managed by an independent vessel manager because of the specialised nature of the trade. The Agreements are "cost-plus" contracts under which the Company reimburses all costs incurred by V. Ships for the operation of the Company's vessels and V.Ships is paid a fixed management fee. For 2004, the management fees are fixed at the rate of \$8,855 per vessel/per month for the container ships and the Laforge and at the rate of \$8,753 per vessel/per month for the other LPG carriers managed by V.Ships (in 2003, \$8,600 and \$8,500 respectively). In the quarter and in the nine months period ended September 30, 2004, \$290,379 and \$871,137 respectively were paid by the Company to V.Ships for services provided to the Company pursuant to the Management Agreements (in 2003, \$282,000 and \$846,000 respectively).

If the Company deems it necessary to employ the services of V.Ships in the chartering or commercial operation of any of the Company's vessels, V.Ships is entitled to a commercial chartering commission determined in light of current industry practice. This commission can vary between 0.5% and 1.25% of such vessels' gross charter revenue and demurrage. In the quarter and in the nine months period ended September 30, 2004, no commercial chartering commissions were paid by the Company to affiliates of V Ships (in 2003, none and \$4,500 respectively).

If the Company deems it necessary to employ the services of V.Ships in the acquisition or disposal of vessels, the Company will pay commissions and legal fees determined in light of current industry practice. In the quarter and in the nine months period ended September 30, 2004, no commissions or legal fees were paid by the Company to affiliates of V.Ships (in 2003 - \$17,942 and \$17,942 respectively).

The Company leases office space from an affiliate of V.Ships. The rental cost paid to the affiliate of V.Ships in the quarter and in the nine month period ended September 30, 2004 was approximately \$21,288 and \$64,081 respectively (in 2003, \$18,652 and \$55,955 respectively).

In the quarter and in the nine month period ended September 30, 2004, the Company paid for accounting services to an affiliate of V. Ships approximately \$7,750 and \$23,250 respectively (in 2003, \$7,750 and \$23,250, respectively).

In August 2004, the Company entered into a service agreement with V. Investments Limited whereby, the Company pays a fee of £10,000 per month in consideration of V Ships permitting the Chief Executive Officer to provide his services to the Company. V Ships is also entitled to reimbursement of all business expenses incurred by the CEO in the provision of his services. As of September 30, 2004, approximately \$40,000 were due to V Ships under this agreement.

In addition, on a case by case basis, as technical manager of the Company's fleet, V.Ships may use on behalf of the Company the services of other service providers for insurance, crew and staff travelling, port agency services,

manning, safety and training services, and miscellaneous services. Some of the service providers may be affiliates of V Ships.



At September 30, 2004, the Company had intercompany balances of trade account receivable due from affiliates of \$61,659 (\$76,094 at December 31, 2003).

#### **NOTE 4. PROVISION FOR IMPAIRMENT LOSS**

In accordance with Statement of Financial Accounting Standards No. 144, "Accounting for Impairment of long-lived Assets and for long-lived Assets to be Disposed of", the Company writes down the value of vessels to fair value when information, typically in the form of appraisals and cash flow forecasts, indicates that the carrying value of such vessels is not recoverable.

At September 30, 2004, the Company evaluated the recoverability of its vessels in accordance with FAS 144 and determined that no provision for loss was required as the carrying values of vessels were deemed to be recoverable. (see "Item 2. Management discussion and analysis", for further comments).

Evaluating recoverability in accordance with FAS 144 requires Management to make estimates and assumptions regarding future cash flows. Actual results could differ from those estimates, which could have a material effect on the recoverability of vessels.

#### **NOTE 5. SHAREHOLDERS' EQUITY**

The net income of \$2,024,321 for the nine months ended September 30, 2004 has been recorded as a reduction in the accumulated deficit.

The summary of changes in shareholders' equity during the nine months ended September 30, 2004 is as follows:

|   | Common<br>Stock<br>Par<br>Value | Treasury<br>Stock<br>at cost | Additional<br>Paid-in<br>Capital | Accumulated<br>Deficit | Foreign<br>Currency<br>Translation<br>Adjustment | Unrealised<br>Losses on<br>Cash flow<br>Hedges | Total<br>Shareholders<br>Equity |
|---|---------------------------------|------------------------------|----------------------------------|------------------------|--|--|---------------------------------|
| December 31, 2003                               | \$ 85,302                       | \$ (891,806)                 | \$ 52,135,576                    | \$ (21,905,096)        | \$ 91,503  | \$ (286,894)                                   | \$ 29,228,585                   |
| Net Income                                      | -                               | -                            | -                                | 2,024,321              | -  | -  | 2,024,321                       |
| Issuance of<br>Stock as dividend                | 1,938                           | 891,806                      | (893,744)                        | -                      | -  | -  | -                               |
| Issuance of<br>Stock to Directors               | 121                             | -                            | 19,879                           | -                      | -  | -  | 20,000                          |
| Issuance of stock<br>Under stock option<br>Plan | 299                             | -                            | 18,299                           | -                      | -  | -  | 18,598                          |
| Foreign currency<br>translation<br>adjustment   | -                               | -                            | -                                | -                      | (18,781)   | -  | (18,781)                        |

|  |           |                 |                 |           |         |               |
|--|-----------|-----------------|-----------------|-----------|---------|---------------|
| Unrealised gains<br>on cash flow<br>hedges | -         | -               | -               | -         | 286,894 | 286,894       |
| September 30, 2004                         | \$ 87,660 | - \$ 51,280,010 | \$ (19,880,775) | \$ 72,722 | \$ -    | \$ 31,559,617 |

With effect from April 1, 1998, directors who are not officers of the Company or of an affiliated company, receive \$5,000 out of their total annual compensation by allotment of shares of the Company's common stock of equivalent value.

In March 2004, the Company's Board of Directors decided to distribute a stock dividend of 1 share for every 20 shares owned, rounded up to the nearest multiple of 20. The date of record was April 16, 2004 and the date of distribution April 30, 2004. 415,513 shares were issued to that effect.

#### **NOTE 6. LONG TERM DEBT**

In March 1998, the Company completed an issue of \$100,000,000 of 10-year Senior Notes (the "Notes"). These Notes were issued pursuant to an indenture (the "Indenture") between the Company and Bankers Trust Company as trustee. Interest on the Notes was payable semi-annually in arrears on March 1 and September 1 in each year at a rate of 11.25% per annum. The Notes were senior unsecured obligations of the Company and ranked senior in right of payment to all subordinated indebtedness of the Company and pari passu in right of payment with all other senior unsecured indebtedness of the Company. The Notes effectively ranked junior to all secured indebtedness and to any indebtedness of the Company's subsidiaries. The Company's obligations under the Indenture were guaranteed on a senior unsecured basis as of the date of the Indenture by substantially all of the Company's then existing vessel-owning.

The Board of Directors had authorised Management to repurchase Notes at times and prices and in volumes, which Management deemed appropriate. During the nine months ended September 30, 2004, the Company repurchased Notes having a total face value of \$6,540,000 for a cash outlay of approximately \$6,107,900 and recorded a net gain of \$363,119 on the transactions (during the nine months ended September 30, 2003, the Company repurchased Notes having a total face value of \$7,000,000 for a cash outlay of approximately \$4,283,000 and recorded a net gain of \$2,620,477 on the transactions). The repurchased Notes have been retired.

On September 30, 2004 the Company called the remaining \$21.1 million of Notes outstanding. The date fixed for redemption was November 1, 2004 and the redemption price 103.75% in accordance with the terms of the Indenture. As a result, the Company reclassified the \$21.1 million of Notes due 2008 from Long Term Debt to Current Liabilities as of September 30, 2004. Upon recommendation of its auditors, the Company did not record in the 3<sup>rd</sup> quarter the net loss of \$979,874, corresponding to the call premium for \$791,250 and the write off of the Notes issuance costs for \$188,624. Such losses were recorded in the 4<sup>th</sup> quarter (see Note 8. Subsequent Events).

The Company has a long-term debt agreement with Fortis Bank and Banque Nationale de Paris ("BNP") obtained in September 1998. Pursuant to this credit facility, certain of the Company's subsidiaries could borrow up to total of \$40,000,000 to finance the acquisition of vessels. The facility bore interest at LIBOR plus 1.25% and the final repayment date under the facility was fixed at June 30, 2006. The vessel-owning subsidiaries had granted ship mortgages over their vessels as security for the advances and the Company had issued a guarantee in relation to the facility. Repayment schedules (consisting of semi-annual instalments plus a balloon) were made by reference to the ages and to the types of vessels acquired. Since December 31, 2003, drawings were no longer permitted under this facility. At September 30, 2004, the total amount outstanding under this facility was \$14,729,815. This loan was fully repaid on October 27, 2004 (see subsequent events).

In September 2001, the Company was granted a \$17,700,000 credit facility by The Bank of Nova Scotia ("Scotiabank"). The facility consisted of two advances, bore interest at LIBOR plus 2% and was non-recourse to the Company:

- A first advance of \$13,462,500 was drawn by one of the Company's wholly owned subsidiaries in order to finance the acquisition of a second-hand LPG vessel. This first advance was repayable over five years in equal quarterly instalments. A swap agreement was concurrently entered into with Scotiabank, as a result of which the variable rate on the loan, exclusive of margin, has been effectively fixed at 4.595%. The swap's notional amount and duration followed the scheduled repayments of the underlying loan. On September 30, 2004, the swap was cancelled at a cost of \$124,500 and the cancellation cost was recorded as interest expense. At September 30, 2004, the total amount outstanding under the first advance was \$5,385,000. This advance was fully repaid on October 27, 2004 (see subsequent events).

- A second advance of \$4,237,500 had been drawn by two of the Company's wholly owned subsidiaries, each of refinanced a second-hand containership acquired in 1998. The outstanding amount of this second advance \$1,059,375 was fully prepaid on March 24, 2003 and the corresponding swap cancelled.

The Company's long-term debt is secured by certain of its vessels.

**NOTE 7: STOCK OPTION PLAN**

On June 20, 2001, the shareholders authorised the creation of a Stock Option Plan for the Company's employees. A maximum of 407,871 shares or 5% of the Company's outstanding shares were authorised for issuance under this stock option plan. Under the terms of the plan, the options give the right to purchase one share per option and vest 25% per annum, commencing one year after the grant date of the respective option. Options expire 10 years after the grant date.

On June 20, 2001, the Company's Board of Directors approved the issuance of 163,148 options to employees at an exercise price of \$0.622 per share.

Since the beginning of the plan, 78,515 stock options have been exercised and 42,182 options were cancelled following the departure of two employees at a cost of \$64,726. At September 30, 2004, 19,350 stock options were exercisable. As of September 30, 2004, the stock price of the Company was \$3.66.

On September 17, 2004, the Company's Board of Directors approved the issuance of 100,000 options to the Chief Executive Officer at an exercise price of \$2.80 per share.

**NOTE 8: SUBSEQUENT EVENTS**

On October 11, 2004, the Company entered a \$45,000,000 long-term debt agreement with Fortis Bank in order to refinance all of its outstanding debt. The facility bears interest at LIBOR plus 1.25% and is repayable over six years in equal quarterly instalments. The borrowers are the existing vessel-owning subsidiaries (except for the sea river subsidiaries) and have granted ship mortgages over their vessels as security. The Company has issued a guarantee in relation to the facility. The Company used the proceeds of this facility as follows: \$14,729,815 and \$5,385,000 to repay the amounts outstanding respectively under the Fortis/BNP and Scotia loans, \$21,891,250 to buyback the outstanding Notes bonds at a premium of 103.75% and the balance for general corporate purposes. Following the prepayment of its debt, the Company recorded a net loss of \$1,117,745 in the 4<sup>th</sup> quarter 2004, corresponding the 3.75% call premium of the \$21.1 million of Notes for \$791,250, to the write off of the Notes issuance costs for \$188,624 and to the write off of the existing bank debt issuance costs for \$137,871.

On November 9, 2004, a number of management changes were decided by the Board of Directors of the Company. Graham Pimblett, Vice President Operations, was promoted to the position of Chief Operating Officer and Alex Gorchakov was designated a Corporate Secretary upon the resignation of Ian Livesey.

**ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

**Results of Operations for the quarter ended on September 30, 2004.**

***Revenue***

The Company had revenue from charterhire and other sources amounting to \$8,127,173 for the quarter and \$23,904,609 for the nine month period ended September 30, 2004 (\$7,911,048 for the quarter and \$28,109,416 for the nine month period ended September 30, 2003). The reduction on the 9 months amount is due to the sale of four vessels on July 15, 2004.

In the first nine months of 2004, the Company's on-hire performance of the vessels on time charter was 99.2% on a potential 3,014 days (for the first nine months of 2003, it was 93.63% on a potential of 3,003 days). The increase in the on-hire performance is due to the fact that one ship underwent dry-docking during the first nine months of 2004 as opposed to eight ships in the same period of 2003. The on-hire performance of the vessels on bareboat charter in 2003 was 100%.

***Costs and Expenses***

Commission on charterhire was \$186,890 for the quarter and \$574,020 for the nine months ended September 30, 2004. It was \$210,544 for the quarter and \$728,064 for the nine months ended September 30, 2003.

Vessel operating expenses plus amortisation of dry-docking costs totalled \$4,463,744 for the quarter and \$13,426,058 for the nine months ended September 30, 2004. They were \$5,259,287 for the quarter and \$14,912,543 for the nine months ended September 30, 2003. Vessel operating expenses comprise vessel running costs, direct costs (such as fuel costs, port charges and canal dues incurred directly while vessels are unemployed or are employed on voyage charters) and management fees. As a percentage of revenue, vessel operating expenses plus amortisation of dry-docking costs increased from 53.0% in the first nine months of 2003 to 56.2% in the first nine months of 2004. The increase in vessel operating expenses as a percentage of revenues is mainly due to the fact that the four vessels sold on July 15, 2003 were employed on bareboat charter and such sale resulted in a reduction of revenues without a corresponding reduction of operating expenses (see Item 1: Business General). Daily operating expenses per vessel averaged \$3,706 in the first nine months of 2004 as compared to \$4,257 in the first nine months of 2003. This decrease is due partially to a general tightening of operating expenses and partially to the cancellation of some insurance write-offs in the second quarter of 2004.

Depreciation totalled \$1,150,659 in the quarter and \$3,527,808 for the first nine months of 2004 (\$1,549,717 for the quarter and \$6,942,054 for the nine months ended September 30 2003). The reduction is due to the sale of four vessels in July 2003 and to the fact that some vessels were fully depreciated at the end of 2003.

General and administrative expenses amounted to \$857,011 for the quarter and \$1,924,164 for the nine months ended September 30, 2004. They were \$253,775 for the quarter and \$925,948 for the nine months ended September 30, 2003. The doubling of general and administrative expenses in the first nine months of 2004 is due to non-recurring expenses incurred in relation with the change of ownership of the Company, the offer for additional equity received by the Company and severance payments. In addition, approximately 35 to 40% of the Company's normal overhead expenses are expressed in euros and the current appreciation of the euro has a negative impact on such expenses.

***Other Income and Expenses***

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Interest expense amounted to \$965,152 for the quarter and \$2,883,643 for the nine months ended September 30, 2004 (\$1,096,591 for the quarter and \$3,816,466 for the nine months ended September 30, 2003). The reduction is due to the debt repayments.

Interest income totalled \$30,241 for the quarter and \$92,286 for the nine months ended September 30, 2004 as compared with \$38,065 for the quarter and \$76,990 for the nine months ended September 30, 2003.

The Company realised a net loss on repurchases of Notes of \$40,121 the quarter and a net profit of \$363,119 for the nine months ended September 30, 2004.

### ***Impairment loss***

At September 30, 2004, the Company evaluated the recoverability of its vessels in accordance with FAS 144 and determined that no provision for loss was required as the carrying values of vessels were deemed to be recoverable at this time. Evaluating recoverability requires Management to make estimates and assumptions regarding future cash flows. Actual results could differ from those estimates, which could have a material effect on the recoverability of vessels.

### ***Net Income***

The net income was \$493,837 for the quarter and \$2,024,321 for the nine months ended September 30, 2004, as compared to \$1,364,452 for the quarter and \$2,348,411 for the nine months ended September 30, 2003.

### **Market Conditions**

In the third quarter of 2004, the market recovery accelerated in the small pressurised LPG segment. Charter rates have increased substantially since December 31, 2003 and the Company is slowly being able to take advantage of such better rates as the existing charters come for renewal. Vessel values of the small LPG ships have also increased a great deal and are currently in excess of book value. Management feels that increased import requirements in the Far East and the lack of new building orders for LPG carriers will help this trend to maintain itself. Management is therefore optimistic that market strength will sustain for the next twelve months. The Company owns six small LPG carriers of the fully pressurised type. In addition, the Company owns a very large LPG carrier, which is fixed on a long-term charter ending in September 2006.

In the third quarter of 2004, the market for containerships remained very strong. The Company is not taking advantage of this market, since its four container vessels are on fixed charters until September 2005 to Maersk Sealand. However, because of the strong market, the new owners of the Tampa did not exercise their option (see Contingencies). Market values of the container vessels have increased a great deal in the past months and management is investigating the possibility to sell and leaseback these vessels.

Certain of the information contained in this Form 10-Q may constitute "forward-looking statements" as that term is defined under United States federal securities laws. "Forward-looking statements" are subject to risks, uncertainties and other factors which could cause actual events to differ materially from those stated in such statements, including the identification of suitable vessels for purchase, the availability of additional financing for the Company, if needed, the cyclical nature of the shipping industry, competition, general economic conditions and other risk factors detailed in the Company's filings with the SEC.

### **Liquidity and Sources of Capital**

#### ***Liquidity***

The Company had \$10,957,780 in Cash and cash equivalents at September 30, 2004 (December 31, 2003 - \$16,446,582). Restricted cash amounted to \$148,597 (December 31, 2003 - \$615,455). In addition, it should be noted that \$1,221,815 were deposited in vessels operating accounts which are directly operated by the vessel technical



managers (December 31, 2003 - \$2,005,913). The ratio of current assets to current liabilities decreased from 1.79 at December 31, 2003 to 0.46 at September 30, 2004, because the 11.25% Notes due 2008 were reclassified from Long Term Debt to Current Liabilities following their call on September 30, 2004. However, the Company had secured the refinancing of such Notes (see Subsequent events).

### ***Operating activities***

The Company generated cash flows from operations of \$3,620,009 in the nine months ended September 30, 2004 in comparison to \$4,054,828 in the nine months ended September 30, 2003. The reduction is due to the sale of four vessels in July 2003, which were employed on a bareboat basis. Since they had no operating expenses, the resulting reduction in cash flow from operations is equal to approximately 90% of the reduction in revenues.

In the first nine months of 2004, the Company dry-docked one vessel, against eight vessels in the same period of 2003. There is no other dry-dock planned in 2004 (in total, the Company dry-docked eight vessels in 2003).

### ***Financing activities***

In the first nine months of 2004, the Company repaid net borrowings of \$10,046,428. These repayments consisted of: (i) \$3,506,428 for normal scheduled repayments, (ii) \$6,107,900 for the retirement of \$6,540,000 of Notes (see Note 6. Long Term Debt). As a result, the Company's long term debt (including the current portion) decreased from \$51,261,243 as of December 31, 2003 to \$41,214,815 as of September 30, 2004.

On September 30, 2004 the Company called the \$21,100,000 Notes still outstanding. The date fixed for redemption was November 1, 2004 and the redemption price 103.75% in accordance with the terms of the Indenture.

### ***Subsequent events***

On October 11, 2004, the Company entered a \$45,000,000 long-term debt agreement with Fortis Bank in order to refinance all of its outstanding debt. The facility bears interest at LIBOR plus 1.25% and is repayable over six years in equal quarterly instalments. The borrowers are the existing vessel-owning subsidiaries (except for the sea river subsidiaries) and have granted ship mortgages over their vessels as security. The Company has issued a guarantee in relation to the facility. The Company used the proceeds of this facility as follows: on October 27, \$14,729,815 and \$5,385,000 to repay the amounts outstanding respectively under the Fortis/BNP and Scotia loans, on November 1<sup>st</sup>, \$21,891,250 to buyback the outstanding Notes bonds at a premium of 103.75% and the balance for general corporate purposes.

As a result of the prepayment of its debt, the Company recorded a net loss of \$1,117,745 in the 4<sup>th</sup> quarter 2004, corresponding to the 3.75% call premium of the \$21.1 million of Notes for \$791,250, to the write off of the Notes issuance costs for \$188,624 and to the write off of the existing bank debt issuance costs for \$137,871.

The refinancing is expected to provide substantial interest expenses savings in the next few years. In 2005, the interest saving will be approximately \$1,545,615.

On November 9, 2004, a number of management changes were decided by the Board of Directors of the Company. Graham Pimblett, Vice President Operations, was promoted to the position of Chief Operating Officer and Alex Gorchakov was designated a Corporate Secretary upon the resignation of Ian Livesey.

### ***Contingencies***

In June 2001, the Company sold the 1984-built container vessel Maersk Tampa to a non-affiliated Company with the Maersk charter attached. In September 2004, Maersk extended the original charter for twelve months until November 2005 and the new owners did not exercise their option. In the event Maersk does not extend again the charter at its expiry in November 2005, the new owners have the option to give the vessel back on charter to the Company for a

period of six months at a charter rate of \$17,500 per day. The aggregate amount of the commitment under this agreement is approximately \$3,150,000. This amount does not take into consideration any revenues the Company will earn from chartering out the vessel to another party.

***Guarantees***

The Company's obligations under the Note Indenture are guaranteed on a senior unsecured basis by substantially all of the Company's vessel-owning subsidiaries except for the unrestricted subsidiaries (See Note 6 to the consolidated financial statements).

***Off-Balance sheet Arrangements***

The Company had no off-balance sheet financial arrangements as of September 30, 2004.

***Future cash requirements***

Management believes that the net cash provided by operating activities will provide sufficient funds to enable the Company to meet its liquidity requirements throughout 2004, based on current levels of charter rates. The Company does not currently have any significant commitments for capital expenditures.

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**ITEM 3: Market Risk**

***Long term Debt***

The Company is subject to interest rate risk associated with certain variable rate long-term debt as described herein. As of September 30, 2004 the bank debt outstanding \$20,114,815 was not hedged by interest rate swaps. However, all of this debt was subsequently repaid on October 27, 2004.

The new \$45 million loan facility was partially hedged for two third of its amount. A swap agreement was entered into with Fortis, concurrently with the loan agreement, as a result of which the variable rate, exclusive of margin, has been effectively fixed at 3.075% until October 2007 on 2/3<sup>rd</sup> of the loan amount. The swap's notional amount and duration follow the scheduled repayments of the underlying loan.

***Impact of Currency Fluctuations***

The Company's functional currency is the US dollar; however, a significant number of transactions are performed in other currencies.

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**ITEM 4: Controls and Procedures**

***Evaluation of disclosure controls and procedures.***

The Company's Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the Company's "disclosure controls and procedures" (as defined in the Securities and Exchange Act of 1934 Rules 13a-14(c) and 15d-14(c)) as of September 30, 2004, (the "Evaluation Date"). Based on such review, they have

concluded that, as of the Evaluation Date, the Company's disclosure controls and procedures were effective to ensure that material information relating to the Company and its consolidated subsidiaries would be made known to them by others within those entities.

*Changes in internal controls.*

There were no significant changes in the Company's internal controls or, to the knowledge of the Company's Chief Executive Officer and Chief Financial Officer, in other factors that could significantly affect the Company's internal disclosure controls and procedures subsequent to the Evaluation Date.

**PART II: OTHER INFORMATION**

Item 1 - Legal Proceedings

None

Item 2 - Changes in Securities

None

Item 3 - Defaults upon Senior Securities

None

Item 4 - Submission of Matters to a Vote of Security Holders

None

Item 5 - Other Information

None

Item 6 - Exhibits and Reports on Form 8-K

- a) Exhibit 31.1  
Certifications provided by the Chief Executive Officer of the Company pursuant to Section 302 of the Sarbanes-Oxley Act of 2003.
- b) Exhibit 31.2  
Certifications provided by the Chief Financial Officer of the Company pursuant to Section 302 of the Sarbanes-Oxley Act of 2003.
- c) Exhibit 32.1  
Certifications provided by the Chief Executive Officer of the Company pursuant to Section 906 of the Sarbanes-Oxley Act of 2003.
- d) Exhibit 32.2  
Certifications provided by the Chief Financial Officer of the Company pursuant to Section 906 of the Sarbanes- Oxley Act of 2003.
- e) Reports on Form 8-K

The Company filed reports on form 8-K on July 23, September 17, October 4 and November 5, 2004.

**SIGNATURES**

Pursuant to the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorised.

MC SHIPPING INC.

Registrant

Date : November 12, 2004

/S/ ANTONY CRAWFORD

Antony Crawford

President  
Chief Executive Officer  
(Principal Executive Officer)

Date : November 12, 2004

/S/ DOMINIQUE SERGENT

Dominique Sergent

Vice President  
Chief Financial Officer and Treasure  
(Principal Financial and Accounting  
Officer)



