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Lloyd's List

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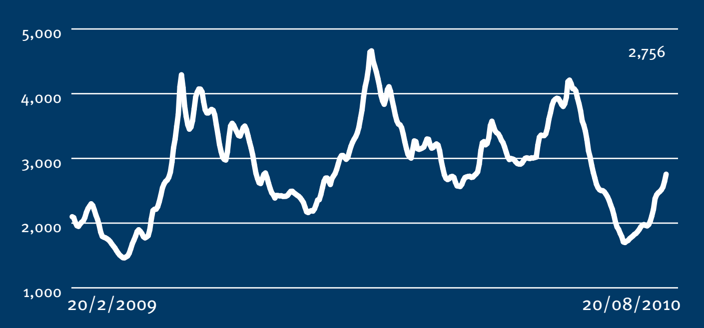

Source: Baltic Exchange

Distressed asset deals get real

Private equity has shown a keen appetite for realistically priced 'value acquisitions'

RICHARD MEADE

A FURTHER influx of private equity finance is expected to enter the shipping markets as investors who failed to land heavily discounted distressed assets look for opportunistic deals at more realistic rates.

Close to $2bn of private equity deals are estimated to have been concluded in the past 12 months alone, and finance experts suggest that more are on the way.

While distressed asset funds, hastily established in the wake of the economic downturn, have failed to make any significant purchases, the private equity interests behind many of the funds have not lost their appetite for "value acquisitions" in shipping.

Banking insiders suggest there has simply been a change in mindset after the initial slew of "pie in the sky" offers were rejected and distressed asset funds realised that banks were not prepared to concede the 25%-30% discounts that some investors had imagined.

"We have seen well over $1.5bn of private equity deals in shipping, probably closer to $2bn, and private equity has never been more active in commercial shipping. But they are certainly not seeing what they were originally looking for," said AMA Capital Partners managing director Peter Shaerf.

"I would hesitate to describe any of these deals as distressed, but they are all being done by people who originally wanted to get into that space."

Distressed asset sales have been few and far between in the shipping industry, despite the fact that the vast majority of shipowners are understood to have breached loan covenants last year.

Flexibility on the part of the banks, largely borne out of their own financial problems, limited the availability of distressed sale opportunities. And those that were considered failed in most cases due to the overwhelming gap between buyers' and sellers' expectations on price.

"The buyers were expecting the banks to take a beating, but in the end their expectations were just too much," said Eurofin chief executive Anthony Zolotas.

"Some were trying to take on distressed loans for a song, but it was pie in the sky what they were offering, and 25%-30% discounts were always going to be impossible from the bank's point of view."

Consequently there were very few truly distressed deals. According to several bankers approached by Lloyd's List, the only deals that were concluded involved owners who were sitting on liquidity and were more prepared than the funds to look beyond the numbers and take a long-term proposition, largely because of the loans that were attached.

Distressed asset funds, however, have not disappeared. A recent research note issued by consultants Mercer quoted distressed shipping investment managers who insist that internal rates of return of 15%-25% can be achieved in the current environment. "The return drivers are income and capital appreciation… as such, shipping investments chart return profiles similar to private equity but can throw off significant yields," read the research note.

"We have seen well over $1.5bn of private equity deals in shipping, probably closer to $2bn, and private equity has never been more active in commercial shipping"

Peter Shaerf, AMA Capital Partners

But despite the apparent renewed optimism from investors, shipping financiers argue that expectations are now more realistic. Whereas funds were previously given euphemistic names, such as "opportunistic" (for "distressed"), the current focus is from investors looking for workable opportunities in a market where asset prices are still attractive in terms of the long-term shipping cycle.

"Six months ago [distressed asset funds] were everywhere," said Keith McRae, DVB Bank's head of shipping asset management. "But there has been a change of mindset, and those that were looking at shipping as a distressed asset buy opportunity are now looking at it as a true market opportunity in the sense that values are still way off their peaks.

"Don't get me wrong, there is still distress out there and we are by no means out of the woods yet. But this is opportunistic buys they are looking for, not distressed assets per se." ■

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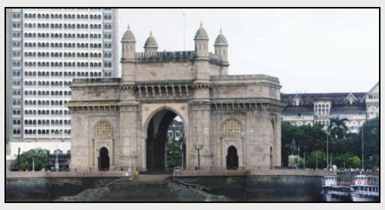

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Chinese yards set for major slowdown over next three years

HUI CHING-HOO — HONG KONG

CHINA Shipbuilding Industry Corp, that nation's largest shipbuilder, has warned that China's yards will face a major slowdown in two to three years, burdened by its recent expansion in shipbuilding capacity.

"The worst is yet to come," said CSIC deputy manager Qian Jianping, speaking at a press conference to announced CSIC's figures for the first half of 2010.

Although analysts have long discussed the likelihood that China's yards have expanded too fast, this is the first time a yard has gone public with the concern.

China recently surpassed South Korea as the world's largest shipbuilder in terms of the volume of tonnage completed. According to Clarksons, China delivered 22.7m dwt in the first six months of the year, while South Korea delivered only 18.3m dwt. China's government has had a long-stated goal of becoming the world's largest shipbuilder, and the recent expansion has been fuelled by soft lending from state-owned banks to shipowners that opt to have vessels built in them.

Too big, too fast? Rapid expansion has been fuelled by soft lending from the state. *Bloomberg*

In one example disclosed by Lloyd's List recently, China's Exim bank extended a loan to the NITC, the Iranian tanker giant, on favourable terms of 90% credit and 10% in a $1.2bn deal last August. The deal was to build 12 very large crude carriers at two Chinese yards, Dalian Shipbuilding Industry and Shanghai Waigaoqiao Shipyard, for delivery in 2013.

Mr Qian's caveat came as CSIC announced an 18% rise in operating income of Yuan63.2bn ($929m) for the first half this year, compared with Yuan53.5bn in the same period in the previous year.

Meanwhile, the total value of the ships it completed in the first half grew 21% to Yuan81.6bn from Yuan67.4bn in the first half of 2009.

Between January and June, CSIC secured new shipbuilding contracts with total value of Yuan71.4bn, up 10.8% compared with Yuan64.4bn in the same period last year.

The shipbuilder's orderbook now includes 61 very large crude carriers and 58 180,000 dwt bulk carriers.

Mr Qian noted that the majority of Chinese shipyards' existing orders were placed during the shipping boom, between 2007 and 2008. However, the volume of new orders secured by Chinese shipyards has seen a significant shrinkage since 2009, affected, as in all the world's yards, by the impact of the global economic crisis. That shortfall will take its biggest toll on China's yards in two or three years, Mr Qian said.

"This is the fact. The shipbuilders have to accept it," said Bao Zhangjin, an analyst at China State Shipbuilding Corp's research centre.

The number of new orders secured by Chinese shipyards fell 34.9% to 23.8m dwt for the first half of 2010, compared to 36.6m dwt for the first half of 2008, according to the China Association of the National Shipbuilding Industry.

Mr Bao also said that smaller yards may be forced to close as the situation worsens, but that larger yards such as CSIC could benefit by the acquisition of smaller, struggling yards.

"Shipbuilders were aggressive to receive long-term contracts in the upward cycle in 2008," said a broker based in Shanghai, "as the ship price was high enough to cover the fluctuation of production cost."

The broker added: "The situation is different now that the shipyards become more prudent as the ship and steel price trend is highly uncertain over the next two to three years."

Mr Qian said CSIC would strive to snatch more new orders in an effort to offset the waning profitability, even if ship prices declined. The company would also increase involvement in non-shipping areas so as to mitigate the plight of the shipping downturn, he said. ■