Capital Link Shipping
Weekly Markets Report

"It's the Pipe, stupid", and why costs matter

Contributed by

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The Capital Link International Shipping and Offshore event, last week, which has been held for 9 years, was off-the-charts good. A few weeks ago, I used the term "Recency bias" (which one analyst has now dubbed as the "R" word), talking about how investor views of future oil prices, going several years out, are swayed by very recent spot market activity. A presentation that I would highlight offered the same concept, as applied to public market offerings by shipping companies, in the light of contemporaneous freight rates. Robert Lustrin, a Partner at law firm Seward & Kissel (which blends maritime with securities law) offered an excellent exposition of the preponderance of investor offerings (with both public and institutional uptake) at times when spot hires are hopping in the underlying sector. He noted that around 2005, after years of only tanker offerings, "…all of a sudden, the drybulk owners were really having their day." Mr. Lustrin added that, "Clearly, for drybulk, 2005 to 2007 were the years for the most public deals." He stressed the "Windows of Opportunity" (in drybulk, but also in tankers or containerships) involve a convergence of healthy conditions on Wall Street (ie strong equity markets) at the same time as investor predilections for "…a perceived upward move in freight rates."- a more eloquent way of invoking the "R" word.

So where are we now? On the Capital Markets panel, well known shipping banker Jeff Pribor, from Jefferies, described the current environment as "fragile", noting that "…the current shipping recovery, which began in 2013, has not played out the way that many people had hoped." On the same panel, Wells Fargo Securities' Managing Director Mr. Eric Schless opined that the dichotomy between positive operational results (certainly in the tanker sector) and mainly lackluster stock market performance has frustrated some investors.

Since many readers were actually in attendance at Capital Link's event, my write-up will emphasize a different conference, held about 30 miles away from midtown- in Stamford, Connecticut. The Connecticut Maritime Association (CMA) was also meeting last week- holding their annual conference, a fantastic networking event drawing shipping folks from all over the world. The three days of programming (with some time slots overlapping, unfortunately, with Capital Link's event) provided perspectives on shipping markets, commodity markets, and a host of other issues facing the industry. One noteworthy session, moderated by analyst Arlie Sterling (from Marsoft- a well known consultancy) offered observations from a handful of deal-makers at the center of the markets. One interesting question concerned industry consolidation- a popular topic, to be sure, at conferences and whether pricing power would result from drybulk and tanker companies' urges to merge. The answer, voiced by noteworthies such as panel participant Basil Mavrolean, Projects specialist at CR Weber, was along the lines of "No, the shipping companies will still be price-takers, however a consolidated company may see lower costs, when amortized across a larger fleet." To Mr. Schless's point (from the Capital Link conference), sell-side analysts trying to discern which names may truly benefit from consolidation might study cost issues more closely.

One of the best CMA conversations happened somewhat serendipitously, when I got chatting with a friend from Inmarsat- a big communications powerhouse listed in the UK. At one time, the hedge fund Harbinger owned a large stake, with UK based Apax Partners also involved some years after Inmarsat had privatized in the late 1990's.

The conversation, with a rep attending the CMA event, started with me asking why, exactly, Big Data has so much hype (almost de rigueur these days at shipping conferences- right up there with "consolidation", including at least two CMA sessions) but so little maritime uptake? Big data depends on having actionable inputs; legitimate applications will include vessel maintenance and ultimately the monitoring of emissions (another hot topic at the CMA). In these cases, more availability of more data will actually add value to the whatever analytics need to be done. So, to sum up, the answer I got (paraphrasing) was "It's the pipe, stupid."

With the observations of Mr. Mavrolean and his co-panelists still fresh in my head, I got to thinking about which players, exactly, might see lower costs than their peers? Also on mind were visions of technical exhibits, showing engines and the like, that I'd seen the previous week at a big shipping industry exposition (where several stalwarts from San Jose and Palo Alto were hosting booths- which I found puzzling at the time).

My Inmarsat buddies, also loving the CMA, spent quite a while educating me about Globe Xpress- rolling out later in the year, and the collaboration with follks from Silicon Valley. The tech design will enable the cost of the comms from ship to the "vendor" (which might be monitoring an onboard function) to be shifted over to the service, who can then package that cost as part of a bigger package. Yes, a shipowner pays, but the smarter pipe, from Inmarsat and its value added re-sellers, enables costs to be parcelled out- the vendor pays for the communications related to its service package (which likely will be bundled and then rebilled to the owner). But the breakthrough comes from acknowledging that not all communications are alike, and that there are multiple budgets aboard ships. Maintenance budgets (that would be the remote monitoring) are distinct from communications budgets (emphasizing crewing welfare or even downloads of electronic charts).

Big Data, which should be about cost reduction, is INTERTWINED with communications. Thus, CMA panelists who talk about the virtues of data (or conversely, who lament the lack of shipowner uptake in certain maintenance regimes) need to keep this in mind. Positive impacts of Big Data will be about operational efficiencies; engineers (some of whom are from Silicon Valley, we discover) love this stuff. Did someone say "If you can measure it, you can manage it?"

So, yes, back to Mssrs. Lustrin, Schless and the folks at Capital Link- there will be big winners among companies who time the market better than others. But, in a commoditized market, prone to overbuilding (with CMA panelist Ed Koll, from Pangaea Shipping noting that even the winners often get caught out by overbuilding), the cost side should not be forgotten.