Capital Link Shipping
Weekly Markets Report

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Golden Age of Gas glitters again

Contributed by

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A few years ago, a report from the International Energy Agency (IEA) talked about "The Golden Age of Gas". Admittedly, the real market penetration for gas, when it overtakes coal, as climate change concerns reign supreme is decades out, but it's a journey. Last week, the importance of natural gas was highlighted with the announcement that Shell would be acquiring BG in a stock and cash deal valued at roughly $70 billion. This is comparable to the price tag on Exxon's purchase of Mobil, in the late 1990's. Many analysts and observers of the energy space had expected the sector-wide plunge in prices for barrels and molecules to create buying opportunities for well-capitalized acquirers. The big and mighty will get bigger and mightier- at least that's the case with natural gas reserves. For Shell, where valuation of reserves has been an issue, proven gas reserves will grow by 25%. Among gas producers, it vaults ahead of Exxon Mobil in the league tables.

For investors, suddenly a new group of smaller and mid level E & P companies will gain exposure, because of their potential as targets, as the energy giants (or financial investors) swoop down. Names like Tullow and Ophir (which very recently acquired Salamander Energy) have been mentioned in the U.K. In the States, might another oil super-major (hint- Shell is tapped out now, and BP faces potential liabilities re events of 2010, so check out the previous paragraph) try to swallow Anadarko. Such take-over suggestions are hardly new, but I would point out that Anadarko is well positioned in the emerging gas plays of East Africa, and, no doubt, merger-mavens can find Mozambique on their maps.

For shipping, what do we make of the big gas deal- and the copy-cats and replications that follow? For the maritime side, the implications of Shell/ BG (and the others that may follow) are all good. The LNG shipping shares have taken their lumps recently (with their partnerships also battered). As we near the end of the Spring term at university, some economics majors might view the merger as increasing the clout of a big buyer of shipping services- which I would not dispute. Its worth highlighting that LNG shipping requires the highest standards of quality and safety; the reputational risks to a big oil company are far too high for them to be bullying shipowners, market-clout notwithstanding. This is the diametric opposite of drybulk (more later)- often called the "last bastion of pure supply and demand" in those university courses. Most talk in shipping about "paying for quality" is fatuous- but in LNG, it's actually true.

The writers in The Economist, a highly respected business magazine, said it better than I could: "One of BG's strengths, for example, is in the liquefaction, transport and storage of gas. Its fleet of giant tankers will boost Shell's clout in the world gas market." The Wall Street Journal also picked up on this theme, with a headline stating that the Shell acquisition of BG would create a giant fleet of LNG ships. It highlights GasLog (GLOG), noting that the entity has 15 ships on to BG and two more with Shell (representing vessels in GLOG and its partnership-GLOP where two vessels with Shell charters have not yet been dropped down). The WSJ has a cordial relationship with GLOG/ GLOP- having done a very complimentary write-up on the partnership entity just two days before the parent's issue of roughly $111 million (net) of 8.75% Series A Cumulative Redeemable Perpetual Preference shares (somewhere between debt and equity)- a day or two prior to the Shell/ BG announcement. The article and also mentions that privately-held giant- Maran (Angelicoussis) as being a beneficiary of the growth trend in LNG shipping. As far as traded issues, LNG shipping is a small club; just from memory, Shell has taken charters of ships from Teekay LNG, Golar, and soon to be listed (maybe) SCF. Though stock picking is not really appropriate here, it's pretty obvious that GLOG (nearly 3% yield)/ GLOP (nearly 8% yield) are obvious beneficiaries of the mega-merger. Intuitively, with some fuel burn-off provided by the mainstream media, these and other names in the space should probably also get a boost as LNG transportation begins to get back in the limelight. And if the underwriters for the putative SCF listing are reading this, my advice is "go for it." With the tanker market on the move again, and equity markets on an uptrend, the stars are aligning.

And then there's drybulk. I love the mainstream financial press- always because of its barometer-effects, and sometimes (not always) because of the content of shipping articles. Another useful source of information and views can be Linked-In discussions. The Capital Link Shipping discussion group has been rolling at full steam. In particular, a dialogue (temporarily suspended due to Greek Easter) regarding investments in the dry bulk sector has offered an "online dialogue out in the virtual lobby" following up on Capital Link's shipping conference of several weeks ago. OK, the virtual lobby is not as grand as the elegant and cavernous atrium in the Metropolitan Club (where the event was held), but the discussions have been opinionated and informative. A very blunt discussion challenging participants to offer their views on drybulk investment timings has generated considerable controversy- with one group noting that shipping's big fortunes have come from true asset plays, while another set of commentators pointed out that the drybulk market's strength of 2006- early 2008 was not likely to be repeated. One commentator from the latter camp, running a large (and highly successful) investment fund, offered the bearish view that: "This sector has been promising a recovery for over 5 years. Don't hold your breath. The next few months will not be smooth sailing, and will test investors' patience for sure." The same fund manager added later that: "At some point, investors will learn...show me the money. And they will also learn to be distrustful of shipowners who run around with investment pitches that show "10 year average earnings" that are ENTIRELY skewed by 2007 and 2008 which are clearly a black swan event."

Other topics including a discussion in its early stages regarding the possible impacts of the Iran deal on the tanker market (which came up briefly in my article last week). A panoply of views is expected as participants return from gardening, Easter celebrations, and watching the improbable result in the Masters golf tourney, on TV.