Commoditization, competitive strategy, and consolidation

Contributed by

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Looking in at shipping companies from the outside has its challenges. Businesses that are industrial don't really reveal much about their inner workings- social media blasts of blue containerships (or FPSOs with good safety records) don't really count. Indeed, the old adage "loose lips sink ships" , originally applied when shipyards were cranking out T2s and Liberty ships (circa 1940's) applies just as well in commercial contexts of the business, 70 years later. Sell-side equity analysts have high levels of frustration in dealing with structures that were not built with transparency in mind. Independent analysts (including tanker nerds and those who dabble in writing) can occasionally gain good insights into what companies might do, or why they are doing it. But, such endeavors-whatever the affiliation of the analyst, involve much guesswork, complementing all hard work and financial modeling that goes into pronouncements.

It was extraordinarily refreshing to hear from a company that has no intention of launching an IPO, and is already the biggest in its niche- so therefore, it will not be going on about "consolidation" and similar things. The "general arrangement" diagram, or simply "GA" for maritime types, of a self unloading bulk carrier provided the starting point for a highly informative presentation at the Connecticut Maritime Association (CMA) monthly luncheon. The meeting, quite well attended, was something of a home-coming. The presenter, Rod Jones, President of the privately held CSL Group (based in Montreal) , actually the world's largest owner and operator of such vessels, worked in Connecticut back in the 1980s with Van Ommeren and Navios. . Mr. Jones, who opened CSL's U.S. office (in the Boston area) in the early 1990s, is well schooled in the business end of shipping, having earned an MBA is from the Tuck School, at Dartmouth (more on that later).

Mr. Jones offered a combination of practical business insights tied together with an interesting personal view. Importantly, the speech revealed a very principled shipping company. CSL (founded more than 100 years ago) is a member of Green Marine, a voluntary coalition of maritime companies in North America whose members strive to improve their environmental performance (with attendant economic benefits) way beyond the minimum levels outlined in regulations. Mr. Jones also proudly mentioned his firm's membership in the Maritime Anti-Corruption Network (MACN), alongside a number of leading shipowners who seek to promote a strong posture against bribery and similar practices.

Beyond the traditional self-unloaders, CSL fleet includes cement carriers and specialist trans-shipment vessels. CSL, once dubbed Canada Steamship Lines, has its roots in the Great Lakes trades, but is now a big international company- with a network of worldwide offices that stretches to Singapore and Australia. Europe is also important- CSL operates vessels in pools with established owners including Egon Oldendorff and Jebsens. After noting the lack of asset trading (more common in other parts of shipping) he told the audience: "….we are not trying to position for an IPO…" Throughout his talk, he stressed the importance of a long term approach to industrial transportation, based on deep knowledge and customer relationships and without position lists of open spot vessels.

Mr. Jones' discussion of strategy was the opening for the more personal side of his remarks and slides. In contrast with the more common Powerpoint affairs typically seen at roadshows or industry conferences, it was clear that Mr. Jones (rather than a junior number cruncher) had actually crafted the presentation. He explained that he was born into a "shipping family". His father started his career started with Great Lakes ore shipping, and later went on to become one of the founders of Navios Corporation- which was originally part of U.S. Steel, in the 1950s. However, after getting the shipping bug, Rod Jones used his MBA lessons on strategy (one slide showed that Michael Porter book that some 1980's vintage B-School grads might remember) to seek out a less commoditized part of the maritime business for himself. Self-unloaders (similarly with chemical tankers and gas carriers) allow a particular company to stand out from another ostensibly in the same business. Indeed, in one notable quote, Mr. Jones pointed out that, in commoditized shipping- like oil tankers, for example,: "…the freight rate for cargo on a brand new ship is the same as it would be on an old clunker."

The differentiation within drybulk (to bespoke versus homogenous) is critical to the CSL story, and to that of Mr. Jones personally. In the audience was a mentor of sorts to Mr. Jones, C. Sean Day- the CMA's Commodore in 2005, who had much to do with shaping the modern-day Navios, still around, 60 years on. Mr. Day also has played an important role in shaping the Teekay group of companies- which received a round-about mention when the luncheon speaker sung the praises of being private. The Porter book, "Competitive Strategy," once required reading at MBA programs, is no doubt worth a dusting off.

Then we have a fresh dose of consolidation within the commoditized sector. Last week saw the new face of such consolidation. It was revealed that General Maritime and crude tanker entity within Navig8 would be joining forces in a stock for stock deal described variously as a "merger", an "acquisition", and a "business combination"- we will just stick with the latter. The General Maritime team, led by Darmouth B-School grad Peter G, will be taking the helm - but Navig8's commercial team will be booking the vessels through its well established pools. Though the business combination, dubbed Gener8, has been long anticipated, the non transparent nature of both entities leaves observers with many questions. Oaktree, a long time investor at General Maritime (even back to its pre-IPO days in the 1990s), seems to be firmly in the consolidation driver's seat. Navig8's crude tanker business may have other investors, Avenue Capital and Monarch Alternative Capital, in the catbird's seat, but the transaction is clearly a Private Equity driven tie-up, anyway you slice it. Oaktree has co-operated in various business ventures with each of these two PE players previously. Indeed, Monarch Alternative Capital has been a big investor in Star Bulk Carriers (on the dry side)- where, let's say, Oaktree exerts a great deal of influence. An explicit Oaktree connection has been denied in the "business combination (with one media account famously suggesting that the deal stemmed from the good vibes resulting from the guys having had a nice meal together- though omitting the all-important detail of who paid). However- would an all-stock deal really happen, if the investors- even from different pools of PE money, were not all very comfortable with each other? With financial guys running the show, if the markets cooperate, we can surmise that a listing in New York might be generated.

The consolidation trend is indeed a real one, though economists can debate exactly how much "pricing power" merged shipping companies might have (compared to more concentrated industries like utilities and the like). When the often mysterious providers of alternative capital decide to talk about their shipping investments- they do mention the importance of building bigger companies. The strong tanker market lately has put such deals in the air, as Tankers International (dominated by the now listed Euronav, clearly a darling of sell side analysts and financial investors) has gotten together with Frontline on a chartering arrangement. Frontline itself, now flush and able to meet its coming obligations thanks to the healthy tanker markets, is now looking at merging with Frontline 2012. The latter is looking to move its drybulk and gas tanker investments out. Thus, Gener8, with the 46 large tankers it would control, would be joining an elite peer group. And, back to Michael Porter and all that, there are commodity industries where a smallish number of players do exert pricing power. The tanker nerds will all be watching.