# What are the prospects and opportunities for the small owner

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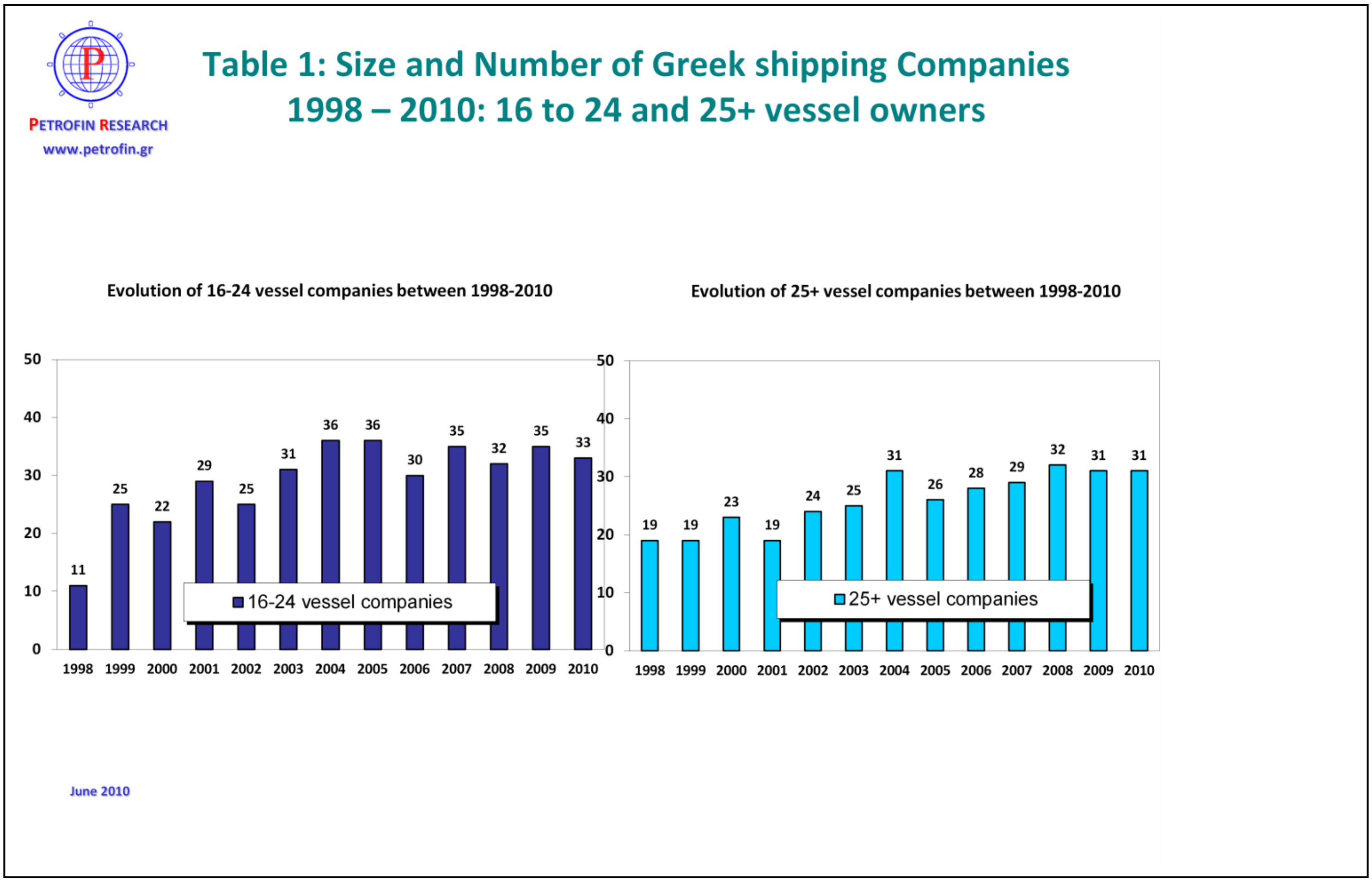
In all industries, the size of the competing firm does matter. Hence, we observe that, over time, the industry becomes concentrated in the hands of a few large firms. The main factors behind this process are invariably two: a) economies of scale and b) barriers to entry for newcomers.

It would be interesting, thus, if we could see whether the above factors also apply to the Greek shipping industry and to what extent. At Petrofin, we have been conducting research into the composition of the Greek shipping industry since 1998, with the results being published annually. The research (Petrofin Research ©) can be viewed in its entirety at our website (www.petrofin.gr).

In order to assess changes in the size of Greek owners over time, we have segmented the market into six categories. Small owners with 1 – 2 vessels and 3 – 4 vessels, medium owners with 5 – 8 and 9 – 15 vessels and large owners with 16 – 24 and over 25 vessel fleets.

In Table 1, we show the number of owners per fleet size. Kindly observe the increase of the large owners (16-24 vessels and 25+ vessels) from 30 (11 and 19 respectively) in 1998 to 64 in 2010 (33 and 31 respectively). This supports the economies of scale hypothesis.

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Over the same period, the small owners (1-2 and 3- 4 vessels), tally fell from 679 (483 and 196 respectively) in 1998 to 511 (340 and 171 respectively) in 2010 (Table 2).

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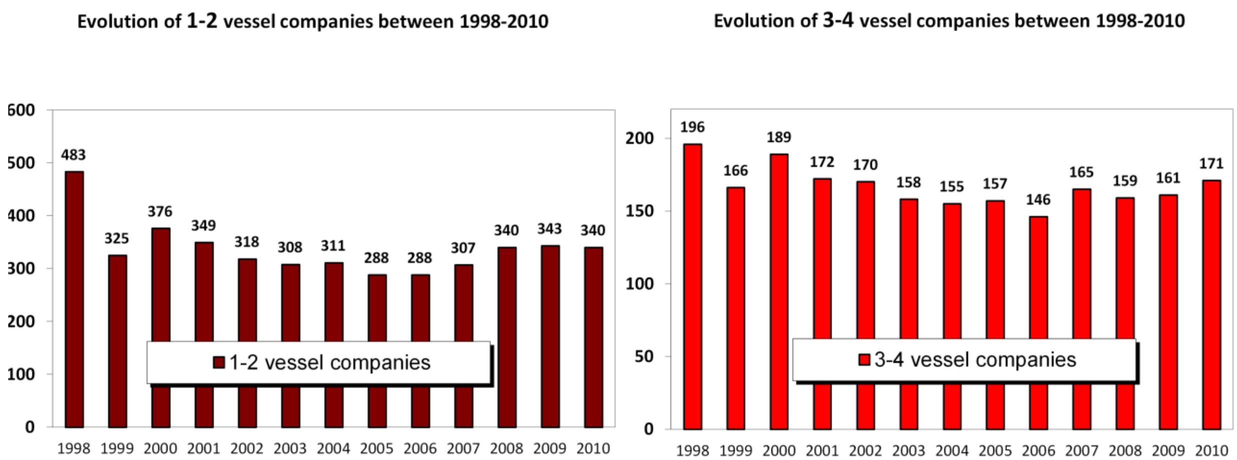
## Table 2: Size and Number of Greek shipping Companies 1998 – 2010: 1-2 and 3-4 vessel owners

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Economies of scale can cover a large number of advantages, related to size. These can be explained by means of a reduction of cost i.e. lower operating costs, as a result of spreading overheads over a larger fleet, lower purchasing costs, lower insurance costs, large volume discounts etc. There are, also,

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higher efficiency factors, when applying information costs across a larger fleet. There are, also, competitive advantage costs, related to the relative power of a large firm, in relation to its counterparts in the market place in the market place.

Lastly, it can, also, relate to higher opportunity benefits, whereby some market opportunities i.e. chartering, hedging, contracting, are more readily available to the large owner.

As firms become very large, there are, also, diseconomies of scale that begin to offset the above economies, as very large firms can become too bureaucratic, have multiple layers of management, unwieldy, slow to respond to challenges and opportunities and be impersonal. Owners running very large firms, by necessity, must rely on a large number of senior managers, managing departments, the whole process being run, often, by a board of directors that can be a formal arrangement, in the case of public companies, or informal, in the case of large private companies.

There are no hard and fast results about the cross over point i.e. at which point the diseconomies outweigh the economies. It would appear, however, that 25-vessel fleets and over require additional layers of management, which distances owners from day-to-day management tasks. This calls for more coordination and cross-departmental informational communications that are sometimes found wanting.

Large public companies, in particular, can suffer more than large private companies, as to all the usual diseconomies must be added the increased reporting and regulatory requirements, legal considerations and often the absence of a single person being the driving and power source, as ownership is dissipated and the company's affairs are being run by boards and committees.

It is important, however, to stress that despite the above diseconomies, evident in very large firms, the economies of scale benefits still represent powerful locomotives, often outweighing the diseconomies.

One size related advantage I have left for last, relates to finance. Large companies have always been able to attract the attention of more banks and to enjoy the benefits of such competition by means of lower margin fees, better terms, easier approvals etc. Moreover, larger firms tend to be more attractive to banks, for reasons associated with higher transparency, better financial information systems, diversification of risk, a more professional approach, better market presence, greater management depth and knowhow, better access to information, more developed links with charterers etc. Often, large firms have a more secure chartering policy and higher liquidity, which can provide greater security to banks.

The finance related economies of scale have in the past been a very significant factor, favouring large firms. This factor has become even bigger in the last two years, as a result of the banking and economic crises. The restrictions towards new lending, as a result for capital and liquidity considerations for western banks has resulted in a shortage of loanable funds, for the global ship finance industry in general, and the Greek ship finance sector, in particular. This has been exacerbated by the Greek economic crisis, which has effectively taken out 25% of the Greek ship finance capacity, represented by Greek banks.

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In these days of tight finance, it is very natural for banks to concentrate their limited resources into their larger, safer and higher quality clients. In this context, quality refers, primarily, to the age of the client's fleet.

Consequently, small owners have found it exceedingly difficult to obtain finance. Newcomers have found it impossible to obtain any finance and this has raised the barriers to entry in Greek shipping. I wish to remind readers that everyone of today's large Greek Groups begun by buying its first ship(s) using some form of finance that was more readily available in the past e.g. Nedship, small Greek banks, niche banks specializing in the smaller owners' sector etc.

Even where finance could be found today, this is often linked to very high margins of 4% - 5% over LIBOR, or higher, as well as a lower loan to asset percentage and harsh terms. Hence, finance economies of scale have been increasingly important and dominant in Greek shipping.

By now, readers would have started to believe that the small owner was doomed to extinction. Far from it, as is evident in the still very large number of small owners existing today. So, what is supporting small owners and allowing them to overcome such adverse odds?

The answer lies in the nature of shipping itself. Shipping operations, often, require instant decisions that small owners can take, not needing to obtain approval from large boards or see how it relates to public company reporting requirements or strategy. Small owners are thus by their very nature very quick, flexible, imaginative, daring and committed. It is very much a “hands on” approach, where an experienced, capable and astute owner can achieve a better performance and address risks before they are allowed to develop.

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The close private nature of small firms leaves all employees in no doubt about who makes the decisions and the closeness of the firm can invariably generate close personal links between owners and their staff. Whereas, in terms of decision making, the small firm has some distinct advantages, in terms of finance there are no compensating factors. As long as, therefore, ship finance conditions shall be tight, the small owners shall find it difficult to attract finance to increase or upgrade his / her fleet.

The success of shipping has, however, generated a significant flow of private equity from private individuals and this has assisted small owners in covering some of their capital requirements. Despite the disadvantages of the small owner, it is interesting to see that every year some 20 – 30 new names emerge. How can this be explained?

Often, as firms become larger, there are differences in the strategy to be followed by the original partners or their heirs. Often, the new generation has fresh ideas about the future of the company. Some wish it to expand, via borrowing or by going public or by becoming a multi-shareholder corporate style company, whereas others in the same firm wish to stay put awaiting for a better opportunity to trade vessels for younger ones and in continuing to adopt the traditional style of ownership / operation. Conflicts can also account for the creation of new companies.

Lately, large Greek industrialists have decided to invest into shipping for investment, tax and other reasons. Hence, every year there are some new names that do possess, however, substantial financial strength and are thus able to obtain bank support.

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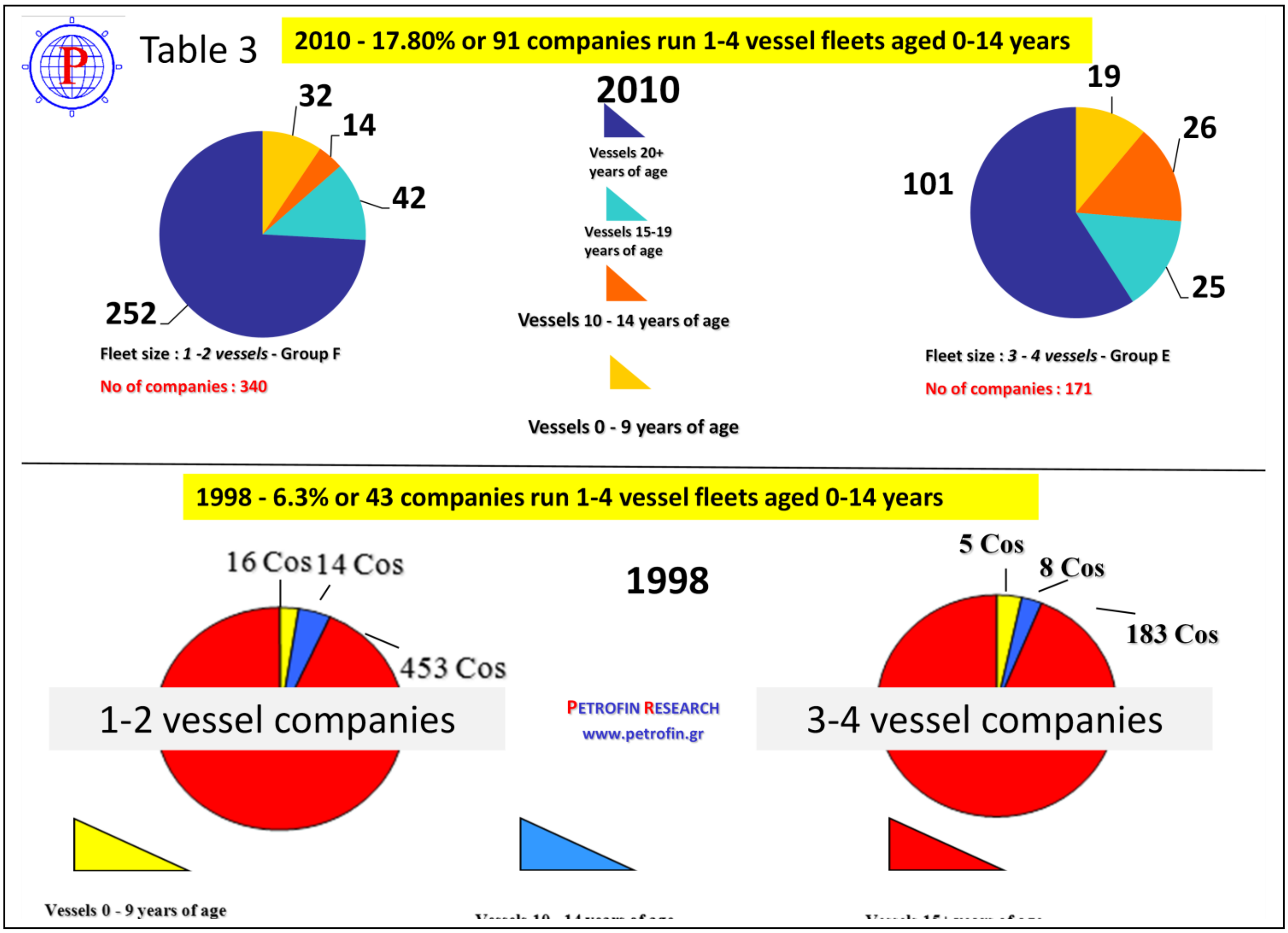
In Table 3, we present over time the age profile of the small (1-2 and 3–4) vessels) owners' fleets. As you can observe, the "quality" segment, consisting of fleets with ages of 0 to 9 years old and 10 – 14 years old, has risen from 6.3% to almost 18%% in 2010. It can be assumed, therefore, that the 91 modern fleet small owners, represent the more dynamic part of the small owners' total. They can be seen as owners who intend to grow larger, invest in modern assets and attract bank finance. As such, they may well cross over to the medium owner categories, later.

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The owners, who own fleets of over 15 years old, represent the “trapped” sector today. They are both too small and have old vessels and as such, cannot grow via bank finance, unless bank finance conditions shall improve or they have the ability and / or wish to invest large amounts of their private liquidity to secure opportunities.

The prospects for this large contingent of small owners are, therefore, bleak. Moreover, to the extent that such overage vessels are not preferred by charterers, insurers and banks, they, also, face increasingly the attention of Port State Control at various ports, as well as flag, class and insurer scrutiny.

The present state of the drybulk market that constitutes the majority of such small owners may well lead a number of them to sell or scrap their vessels, as the costs of maintaining and operating such vessels has risen. Many small owners will invariably prefer to hold on and await for better times to dispose of their last remaining vessels. However, the attractiveness of scrap prices, at about $500 per lightweight ton, may tip the balance in favour of scrapping.

For many small owners, vessel ownership and operation represents their way of life. It is what they know and if they should dispose of their vessels, it would be difficult to return to shipowning. Hence, they remain obstinate players, putting their faith into a better future market.

In current market conditions, are there any opportunities for small owners? We believe that there are. Many medium and large owners have by now developed their fleets towards younger and larger vessels. They would view buying old and often smaller vessels as a backward step. Sellers of older tonnage are increasingly finding that the levels they attract are closely linked to the scrap value of the vessels. Here lies an opportunity for a small owner paying cash for an old vessel. Should he / she be able to detect an upward change in the market or a period charter opportunity for an old vessel candidate, they may be able to secure her inexpensively and obtain both profits from operations as well as from resale. Buying an old vessel close to scrapping levels, represents a relatively low risk investment to an experienced owner/ manager.

To conclude, therefore, small owners do face many adverse factors that restrict their ability to survive and / or expand. However, Greek small owners do represent a committed large band of experienced owners / managers, who remain loyal to their small size and in non-reliance in ship finance. Although, their overall number is expected to continue to decline over time, especially at times of poor market conditions, new entrants and the re-entry of previous owners shall continue to keep the sector buoyant at times of market prosperity.

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