The Role and Prospects of Finance Consultants in Shipping

July - August 1999

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The 1990's have witnessed a huge rise in the number of financial consultants serving the shipping industry. The numbers have grown from a mere handful in the 1980's to **63** in 1999 in accordance with data drawn from the 1998 LSE Capital for Shipping directory and adjusted for entries/deletions known as of 4/5/1999.

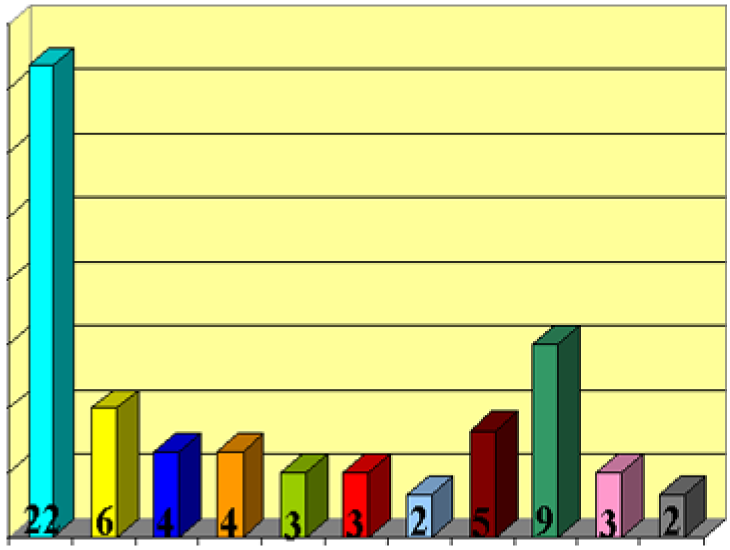
Although the directory cannot possibly contain information on every shipping financial consultant since some may have failed to provide their entries, it is, nevertheless, an authoritative source. Furthermore, the analysis of the composition of these financial consultants does produce certain interesting facts.

In the above analysis, commercial banks and US investment banks have been excluded, since the focus is on pure shipping financial consultants who do not ordinarily provide finance using their own capital. It does cover though specialist arms of banks when these are set up as financial consultant mode.

The analysis covers only dedicated financial consultants and not parties that may also provide selective or occasional financial advice and services. If these parties were also to be included, the number would have multiplied since "financial consultancy is also offered "on the side" by S&P brokers, lawyers and retired bankers who may operate out of their homes.

The geographical spread of financial consultants is shown on **Table I.**

TABLE I: Number of Financial Consultancy Firms per Geographical Position

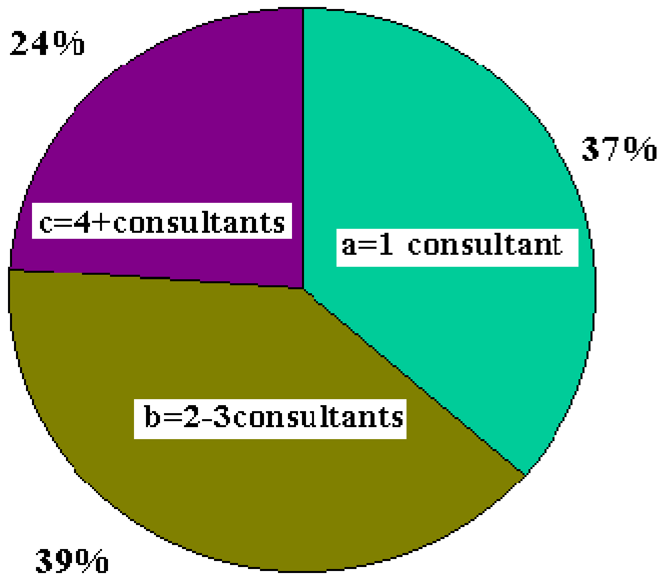


The "make up' of the Financial Consultant in shipping

Although European consultants predominate, the US financial consultancy representation has grown by leaps and bounds over the last 5 years in line with the renewed interest in shipping by the US capital markets.

Table II shows the size of each dedicated financial consulting firm based on the number of qualified consultants it employs.

TABLE II: Size of Consultancy Firms



As you will observe, 23 or 37% of all consultants is single "producer" firms. Furthermore, of the 63, in total 50 or 79% of all consultants were independent of a specific association or ownership by a bank or larger institution whereas 13 or 21% were dependent on a "big brother" **(Table III).**

Numbers are going up

What, however, is the reason for the growth in numbers? The main factor has been the development of "disintermediation" whereby consultants are the link between banks and clients offering "specialist" knowledge and services to the benefit of both.

This disintermediation is a development of the last decades and can be found in all industries. Indeed, the services sector is the fastest growing sector in every developed or developing country.

Financial consultants claim that despite the development of information technology, the capital markets are far from perfect. As such, they help clients become aware and take advantage of different products and services offered by the financial community.

These may be either in the procurement of loans and / or the provision of structuring and other financial advice or in assisting companies grow via the capital markets (equity or bonds) or in advice on mergers and acquisitions (M and As) or simply in putting across professionally financial presentations to lenders that are well prepared, analysed and presented.

As clients themselves have become more sophisticated so too have consultants developed their services in order to promote "value added" advice and expertise and thus make themselves useful and, at times, indispensable.

Often, financial consultants have largely dropped out of the mainstream consultancy sector and have begun to offer very specific products that go hand in hand with the development of the capital markets. For a while during the heyday of the high yield frenzy, there were 30 potential issues that were being pursued in conjunction with the financial consultancy sector.

Whereas most have been "put on the shelf", nevertheless the experience has been useful and will facilitate swifter progress when market conditions shall once again become more favourable.

What do Consultants have to offer?

Shipping clients themselves have become very demanding in what service they wish to receive from their consultants as well as what terms they insist in obtaining from banks and the market through the use of consultancy.

Consultants often complain that they have to prove in tangible form that their services produce better terms and that the yardsticks are being raised even higher. They argue (with good reason) that their involvement augments the whole process with other benefits, such as greater speed, smoother negotiations, reduced errors, avoidance of bank imposed "onerous" terms, more reasonable financial covenants, better debt repayment profiles and so on.

As competition among consultants intensifies, client pressure can become intolerable. Clients expect that the use of a financial consultant at an infinitesimal fraction of transaction costs or a relatively low fee should "automatically" guarantee very high levels of finance.

Consultants have started to turn away such speculative or at times "impossible to realise" business and this has been to the benefit of both the industry and to the credibility of such consultants over time.

Since the number of potential financial sources has grown over the last decade and since the range of products and services offered has also increased, it would be virtually impossible for the hard pressed finance director or manager of a shipping company to keep track of every source or product that would be available at a specific point in time.

In addition, consultants have the benefit of negotiating with each financial institution across a large number of clients and transactions, thereby bringing to bear all their directly relevant experience.

Whereas the benefits of the use of consultants by shipping clients is not in doubt, there is an element of controversy and mixed feelings from financial institutions themselves.

Banks' reactions to Consultants

Banks have been making increasing progress in overcoming the problem of "disintermediation" which they feel may be denying them of useful profits. Although they would be the first to admit that client business supported by a professional financial consultant is invariably better presented, analysed and does reduce the amount of time spent by the bank in considering and finalising each transaction, they prefer to have a "one-to-one" relationship with the client.

The "conflict of interest" in being both a provider and an "adviser" does not seem to perturb them. Bankers also often feel pressured or at times intimidated by the presence of another "expert" who may point to terms and clauses that may have been missed or incorrectly assessed by the client or are not in line with what is available in the market.

As such, once a finacial transaction is done, banks often seem to push away consultants and develop their own direct relationship. This is often couched in such soft terms as "you don't need a consultant now", "you are financially sophisticated enough not to need a consultant" or in even harsher manner by saying that "the bank would prefer if you avoided the use of consultants". Whereas the motivation and benefits to the financial institution are self evident, clients are often swayed by such remarks often to their detriment.

It is fair to say that not all banks have the same attitude, since a number do respect the source of introduction and the long-term contribution of permanent consultants. We at Petrofin have sought to develop permanent long-term bank-client relationships, as well as seek to satisfy our clients' requirements primarily via the clients' existing range of banks, if at all possible. This loyalty has paid dividends to all parties and has promoted greater stability and enhanced long-term bank-client relationships.

Can Consultants be useful to Banks?

Banks remember consultants when their loan portfolios get in trouble during a shipping slump. At that time, pressure from the market and from within the bank becomes intolerable and the use of consultants becomes a useful safety valve.

Financial consultants that specialise in providing advise to banks have a deep knowledge of when to foreclose and realise a bank's collateral or when it may be possible to work a problem out over time seeking a recovery via closer co-operation and control of the situation.

Experienced consultants always advise banks that to foreclose is a last resort since invariably losses follow recently, however, some "advisors" have advocated more radical action, since they believe that the situation will get worse over time. They appeal to a banker's deeply held belief that the "first loss is the smallest loss".

However, shipping is a cyclical industry and when a bank-client relationship is sound and problems are exogenous (i.e. market related), consultants can often assist in keeping parties talking and co-operating until the market recovers.

The use by banks of financial consultants helps reduce the pressure and responsibility of account officers who are desperate to shift such responsibility away from them. In these situations, a financial consultant can be used as the "fall guy".

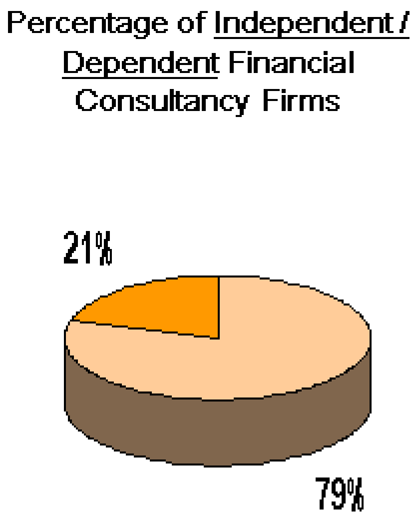
Bankers will counter that consultants have nothing to lose in offering advice for which they are well paid since the results of their advice is felt in the banks' pockets. No doubt the answer lies in the middle and the use of consultants to reach amicable compromise agreement in default loan situations by both sides has become a common place practice.

Does size matter?

Independent financial consultants have often felt the need to join forces with others similarly minded consultants in other geographical locations. Through reciprocity and non-competition agreements this has been a positive development in expanding the geographical coverage by both parties. These associations are loosely structured and not formally declared or known by the market.

As the earlier analysis has shown, there are very few large shipping consultancy Groups and even fewer with an international branch network. The reasons may lie in the sheer "independentness" of consultants and / or the lack of sufficient strong capital base **(see Table III).**

TABLE III: Percentage of Independent/Dependent Financial Consultancy Firms



Since the shipping cycle largely determines the futures of financial consultants and since the increased speculation has brought about greater risks of prolonged periods of inactivity, many shipping financial consultants have sought to diversify.

This diversification has take place in different ways. A number has sought to create an ability to take equity positions in projects in which they are involved. Others have sought to create investment deals in order to take advantage of investment opportunities that they identify. A smaller number are looking to diversify away from shipping by offering similar services to toher asset based industries.

Safety has been sought by some by becoming largely dependent on a simple introduction. This provides a steady stream of introductions and an ability to place business. However, the financial consultants' ability to offer "better advice" or have access to other financial institutions may be jeopardised.

The recent shipping slump has adversely affected financial consultants. However, there has not been any exodus from the industry as most consultants have shown geat flexibility and adaptability and are simply marking time.

What of the long-term future of financial consultants?

In view of the banks response to "disintermediation" by promoting "reintermediation", consultants will undoubtedly come under pressure to perform and to justify their existence, fees and ability to offer "value added services". However, whereas banks are largely inflexible and slow moving, consultants are quick to exploit other opportunities and develop "niche" products and services.

In our opinion, the services of a shipping financial consultant shall become more sophisticated and specialised over time, as consultants try and differentiate themselves from the inroads by financial institutions into the world of consultancy and advice. Whereas the pressure to become larger is also present in the world of financial consultancy, such development often restricts the flexibility of consultants and increases dramatically their costs.

The sector, therefore, shall continue to be dominated by relatively small practices. However, the need to develop more specialised services, will require the presence of a team and as such the days of the "lone consultant" may be numbered as their traditional role of loan procurement declines in importance over time. Banks are actively marketing clients, whatever they may be and this drive is ultimately working against the "bread and butter" work of many traditional consultants.

Whereas inevitably financial consultants were primarily based either in financial centres or in areas of shipping prominence, increasingly new practices are being set up in developed regions. This is a trend that will continue and accelerate.

In conclusion, therefore, the shipping financial consultancy sector is facing keen competition and needs to continuously develop new products and services to stay one step ahead.

The enormous variety, cyclicality and complexity of the shipping industry, coupled with the flexibility, ability and specialisation of shipping finance consultants will keep both their number and importance growing well into the new millennium.

From Economic Outlook July – August 1999 Issue