QUO VADIS, NAVICULARIE?[i]

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Greek owners have always had the reputation of being vindicated in their decisions. They have also been able to position themselves well ahead of market developments, in term of buying / selling vessels or in chartering. Often, their decisions have been counter-cyclical. The cumulative results of their attitude to risk and abilities in shipping are evident for all to see.

It is for the above reasons that the shipping market has been watching the recent rush of orders by Greeks with great interest.

According to Clarkson's, the current Greek order book stands at approximately 800 vessels, of which 500 are dry bulk vessels. The total capacity of the above orders is 74 million DWT, which, if delivered, would represent approximately 31.6% of the current Greek fleet.

Despite a continuing newbuilding delivery slippage of approximately 40%, the rate of deliveries has grown and the newbuilding order book growth continues unabated.

This continuous commitment by Greek owners for newbuilding orders (in the light of the bulging worldwide order book and the uncertainties over the global economic prospects and fears of a double dip recession) has been puzzling. Admittedly, China and the Far East region still represent high growth areas.

However, even their frenetic growth rates have recently been curbed and more importantly the slowdown in activity in the rest of the world has resulted in an international growth rate not exceeding approximately 3% p.a. Even if this translates itself into a greater demand in international trade of approximately 5%p.a., these rates of international rate growth cannot be compared with fleet growth rates in capacity well in excess of 10% per annum and in the case of drybulk over 16% per annum in accordance with 2010 to date statistics (SSY).

Consequently, we have what appears to be a disequilibrium in the demand / supply equation made worse by the very limited scrapping and this imbalance appears to be growing all the time.

Many owners and analysts have correctly identified port congestion and longer voyages to justify the relative recovery of the market. However, are these factors going to continue in the years to come? More importantly, are these factors alone able to cover the ever rising demand / supply imbalance?

The arguments between the analysts using facts and figures and the owners is raging. Whilst many owners are adopting a cautious approach, many others are placing order after order.

The main question is who will be proved right? Will it be the prudent owner, who cannot ignore the worryingly large capacity and overhanging order book or the intuitive owner, who has an unnerving and uncanny ability of reading the market well, despite all the facts pointing to the contrary?

The story will, undoubtedly, unfold in your computer screens and will make or break fortunes.

Having presented the wider picture, my article, today, shall focus on another issue, one that may have a pronounced bearing on owners’ performance. The issue I wish to analyse is that of ship finance, or to put it rather crudely, the lack of ship finance.

Coming off a global banking and economic crisis, ship finance has also been affected. For many banks elected to downsize their shipping portfolios during the crisis and conditions are not clear yet for a massive return of confidence.

Admittedly, shipping has not resulted in numerous defaults and / or losses for banks. However, this may have had more to do with the banks' forbearance towards loan defaulters rather than a pronounced recovery to full health by the shipping industry.

The jury is still out in terms of the prospects for the three main shipping markets, dry, wet and container. As such, banks have yet to be tested decisively by a 2-3 year pronounced bad market. In addition, banks are still trying to recover their liquidity and capital ratios, as well as, meet the more stringent capital adequacy terms imposed by central banks.

In this rather uncertain and potentially dangerous climate, it is not surprising that banks are still reluctant to expand their shipping portfolios.

More importantly, many banks are using the run off in their loan books via repayments, sales etc. to reduce their shipping exposures, conserve capital and build up liquidity.

In order to assist in highlighting the above forces at play, we wish to present to you our latest Petrofin Bank Research © analysis of the global and Greek ship finance markets.

Last year, we did research, whereby we took the top 42 shipfinancing banks in the global market and their loan portfolios and split them between "banks with lending capacity", "banks with a reduced capacity" and "banks with neutral / unclear policy towards shipping".

We conducted the same research this year and the results are shown in table 1.

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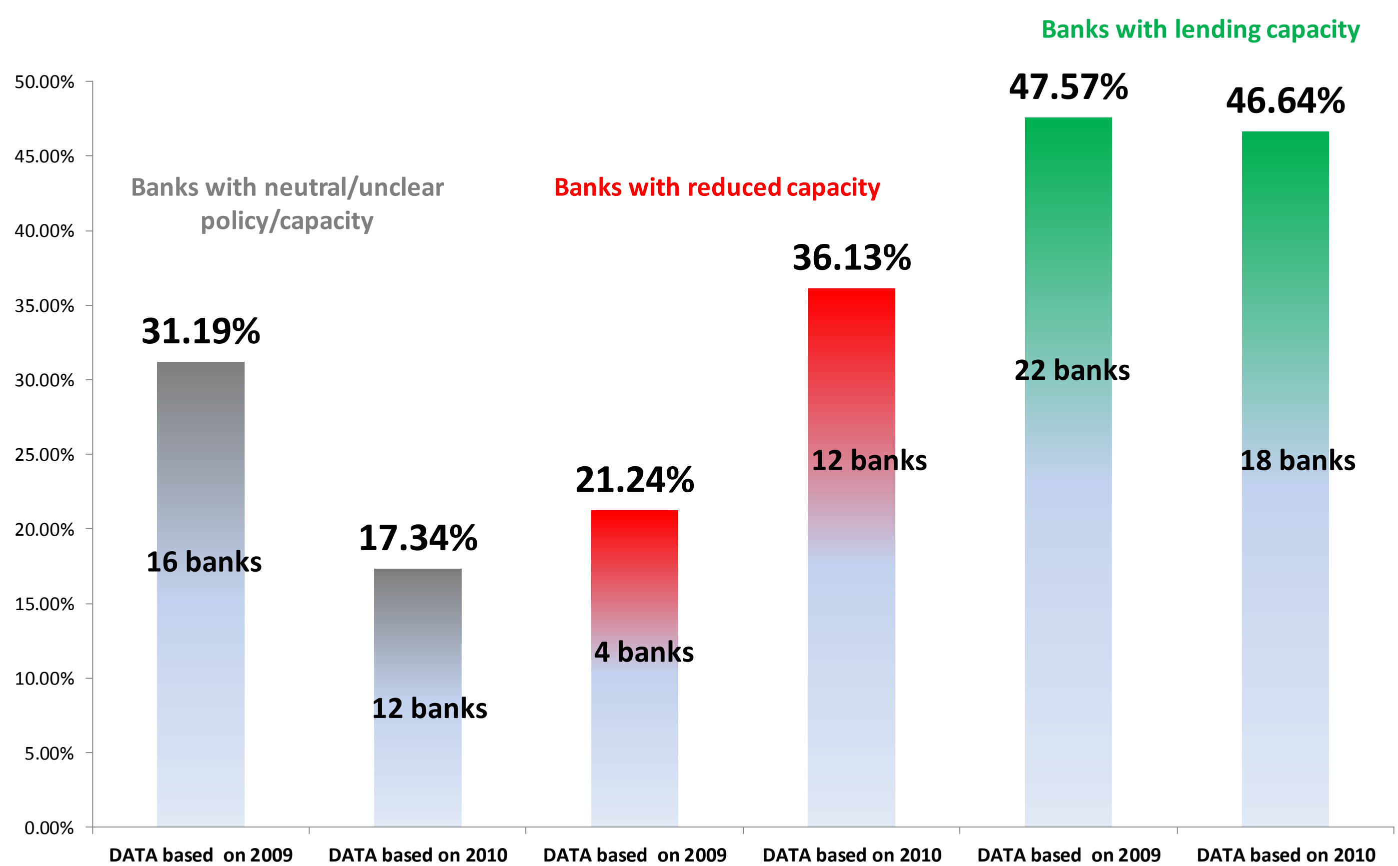
Ship finance banks capacity

2009 Global portfolio, top 42 banks: $463.75bn
2010 Global portfolio, top 42 banks: $436.93bn

Table 1



As you will see, there are the following main trends:

a) The Global shipping portfolios of these 42 banks reduced from $463.75 bn in 2009 to $436.93 bn in 2010, i.e. a 9.4% reduction.

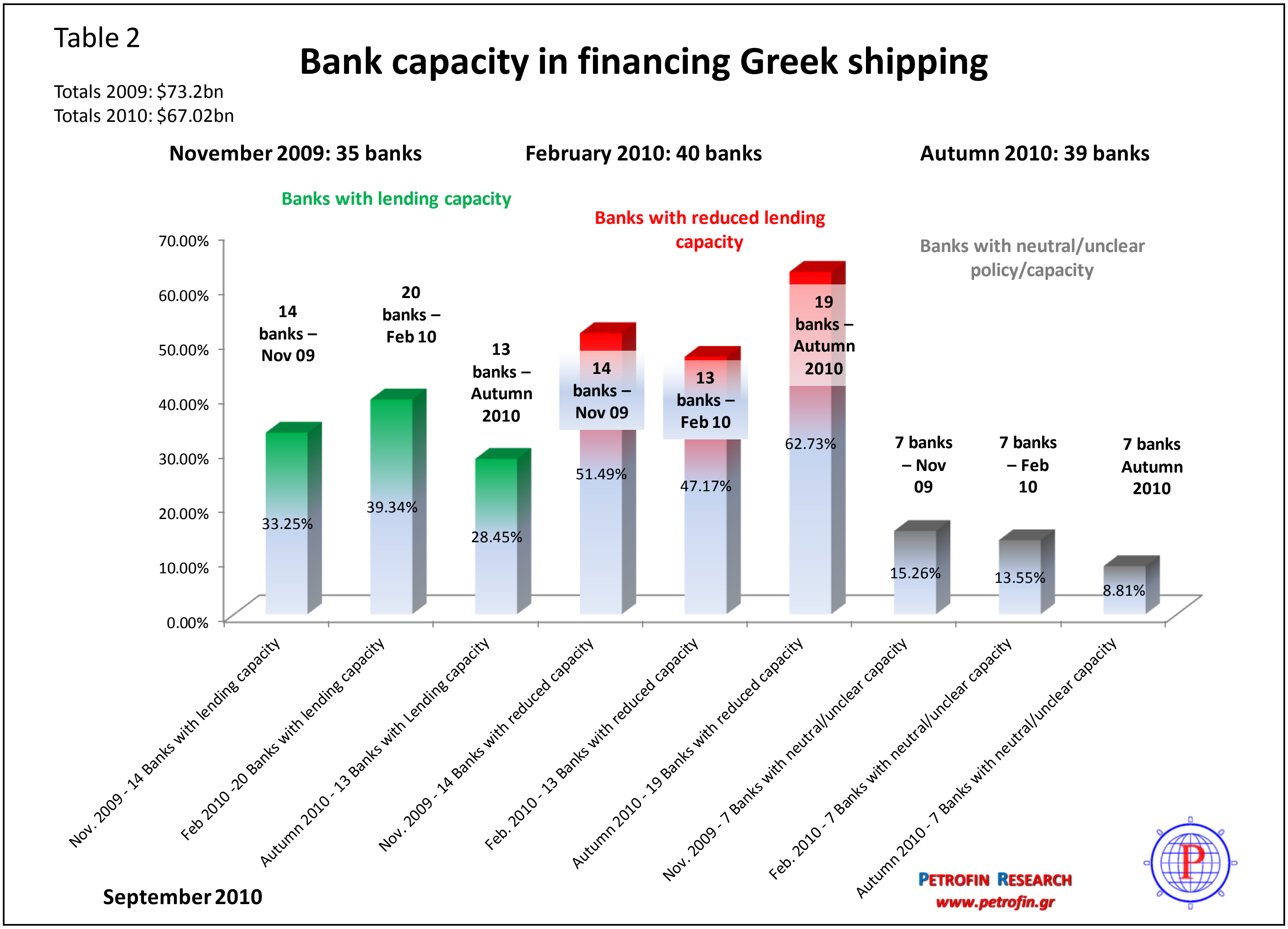
b) The number of banks with reduced capacity rose from 4 to 12 banks and these now represent 36.13% of the Global loan portfolio, as opposed to 21.24%, last year. This clearly signifies an international reduction of interest in ship finance, at this point of time.

c) The number of banks with neutral / unclear policy fell from 16 banks, representing 31.39% of Global loan totals in 2009, to 12 banks, representing 17.34% of such totals in 2010. This, strongly indicates that a number of banks shifted their policy from neutral to negative.

d) It is of comfort to the shipping industry that 18 banks compared with 22 last year, continue to report ship lending capacity and that this represents 46.64% of Global loan totals. These banks represent the best hope for ship finance and hold nearly 50% of the market.

We conducted the same analysis, based on our 2009 and 2010 annual Greek ship finance bank research in November 2009, February 2010 and August 2010, in order to identify the attitude to Greek ship finance among banks involved in Greek ship finance and to compare our findings with that of the Global ship finance market.

The results are shown in table 2 and are as follows:



a) The total Greek ship finance totals fell from $.73.2 bn in 2009 to $.67.02bn in 2010 (see Petrofin Bank Research ©), i.e. a fall of 8.4%.

b) The gradual recovery in confidence evidenced between November 2009 and February 2010 has evaporated.

c) The number of banks with lending capacity fell from 20 in February 2010, representing 39.34% of Greek ship finance totals, to 13 banks, representing 28.45% of such totals.

d) Worryingly, the total number of banks with reduced lending capacity grew from 13 banks in February 2010, representing 47.17% of Greek loan totals, to 19 banks, representing 62.73% of such totals.

e) Comparing the Global and Greek ship finance positions, it is clear that conditions in Greek ship finance are much tighter. This is mainly due to the reduction in lending capacity by HSH and RBS (very prominent banks in the Greek sector), as well as, the liquidity problems of Greek banks, which collectively account for approx. 25% of the loan totals.

What the above research has clearly highlighted is that shipfinance conditions for the Greek shipfinance market are particularly difficult.

The question, therefore, is “Quo vadis, navicularie”? Very few owners can finance newbuilding orders out of their own liquidity and without ship finance. Invariably, the vast majority of orders are therefore “speculative” i.e. there is neither finance nor a time charter in place.

Owners may well argue that ship finance activities may improve over the next 2-3 years, until their vessels shall be delivered and that they are expecting greater bank competition and an improved ability to raise finance. Are they right, though? Will banks currently reducing their exposures do an “about change” shift? Will there be new and committed large players into Greek ship finance to replace the lost capacity?

The more one focuses on the above questions, the more concerned one becomes, for the outlook over the next 1 – 2 years.

My own thoughts are that in addition to the usual risks facing an owner about to place a new order, such as the state of the market at delivery and absence of long-term employment, owners have an added risk of non-available, inadequate or expensive ship finance.

Moreover, should the shipping market weaken, as a result of overcapacity, the attitude of banks is likely to turn even more negative towards ship finance. Consequently, owners may find themselves unable to obtain finance and may be forced to abandon their orders and risk losing their down payments.

A lot of positive changes have to take place between today and 2012 – 2013, when these new orders shall be delivered.

Once again, it may well be that everything will slot into place and current vessel newbuilding prices shall turn out to be a “bargain”. Greek owners’ decisions may well be vindicated once more. However, the obstacles have never been higher and the prospects are so unclear, so that owners have to realize that, placing orders today, represents gambling bets of the highest order.

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[i] Quo vadis, navicularie? = Where are you heading, ship owner?