

Lemmings and the pressure to consolidate

In 2016, the maritime industry is facing a year of consolidation, and some market shifts could occur. This is the conclusion of this year's HANSA-Forum »Shipping | Financing«. Scrapping is up for discussion. A review by Michael Meyer

For years, there has been speculation about the great wave of consolidation in the container shipping industry. The freight and charter rates are forcing carriers to alternative solutions beyond austerity programmes or lay-up measures.

As for the shipping companies an imminent takeover of NOL including the container shipping company APL is to be expected, the number three in the world CMA CGM is holding talks at an advanced stage. Being state-arranged, the merger of CSCL and COSCO in China is only a matter of time. There is further speculation about a merger of Hyundai Merchant Marine (HMM) and Hanjin Shipping in Korea.

Germany's largest shipping line Hapag-Lloyd has recently managed the long planned IPO (initial public offer) after the merger with the Chilean CSAV and thus embarked on their own course towards consolidation. Thanks to the synergy effects a positive result was achieved for the first nine months. COO Anthony J. Firmin considers it likely the industry will see similar projects, but he also expects problems. »From 2007 to 2013 there were no major acquisitions. It is also becoming increasingly difficult,« he said at the 19th HANSA Forum »Shipping | Financing« in Hamburg. Thus larger consolidation projects often conflict with national or family interests. »Founders often regard shipping companies their family jewels which they tend to overvalue,« he said.

Otto Schacht, who is responsible for the ocean freight business of the world's biggest logistics provider Kuehne + Nagel as a board member and thus one of the major customers of shipping lines, observes an industry which is under high pressure. »Similar to 2005, the coming year will be dominated by consolidation. For the first two quarters of 2016 the carriers will be facing bad times again,« he said at the top-class traditional event in front of 450 attendees in Hamburg's Grand Elysée Hotel. Therefore, further mergers or acquisitions would be on the agenda.

Some experts believe the obligation of the top lines to alliances is an obstacle. Mergers between partners thus were considered to make little sense, because a great degree of the synergy effects had already been generated by the formation of alliances, says the Hapag Lloyd COO. His shipping company is cooperating within »G6« including APL, HMM, MOL, NYK and OOCL. In addition, there are »M2« by Maersk and MSC, »Ocean Three« (CMA CGM, UASC, CSCL) and »CKYHE« (COSCO, »K« Line, Yang Ming, Hanjin, Evergreen).

The regional impact of alliances is also considered important. Thus mergers are most beneficial if shipping routes with diverging operating areas complement one another, but less so for two shipping companies, both of which mainly operate on the highly competitive Asia-Europe routes. After the mergers of Hapag-Lloyd with CSAV and Hamburg Süd with Chilean CCNI there is no major player left for an alliance in South American trade.

According to Schacht the problems of shipping lines are also a consequence of too optimistic cargo forecasts in recent years. He expects growth particularly in US traffic. The unsatisfactory imports from Asia thus came as a big surprise. »Too much was imported into this country. Correspondingly the margins decreased in 2015, because at first the stock levels were reduced,« says Schacht. The revaluation of the Chinese currency Renminbi also had an influence, because the decision made products from the People's Republic more expensive. »I

just wonder when Beijing will devalue the currency again,« says the K+N-Manager. Following discussions with customers, however, he assumes imports will increase as of the second quarter 2016.

At K+N as well as in the liner shipping companies the freight rate levels are considered to be too low. From Shanghai to Santos 50 \$ have to be paid for a 40-foot container (FEU). »This is much too low, the rate would have to be at 1,500 \$,« says Schacht. Between Asia and Europe prices are thus fluctuating from 1,500 \$ to 200 \$ per FEU. »We do not understand this, neither do our customers. But we have to live with it.«

There is always a carrier willing to transport cargo even at the lowest rates, Firmin says. This was a reason why it is such a hard job at the market right now. In case of doubt, everything would be done to fill a ship's cargo hold.

On the other hand, the tramp shipowners are under enormous pressure. After a small interim high in summer charter rates again fell enormously. The oversupply of tonnage is only one reason. Another could be a power imbalance, market players involved agree. The powerful alliances deal with a fragmented tramp shipping sphere. About 50% of the capacity is provided by 142 commercial managers or pools. These are backed by no less than 272 tramp shipping companies.

Despite the existence of overcapacity and the low rate levels new vessels are constantly being ordered, principally ULCV (13.000+ TEU). At least for his shipping company Firmin denied the theory liner shipping companies for some time have behaved like lemmings jumping off the cliff against their better knowledge to even further expand their fleets, and jostling for the front position at the cliff. »Hapag-Lloyd does not jump off this cliff. While we want to buy large newbuildings, we are not in a great hurry,« said the COO.

Kurt Klemme, Managing Director of Reederei Nord, demanded a widespread scrapping by the industry. His credo: »Stop the unrealistic restructuring plans! Instead, scrap, scrap, scrap«. Firmin agrees to this claim in principle. However, there was a problem: »We wanted to scrap 16 units. Ultimately, however, only four ships were sent to die, because there are still buyers who purchase the old freighter and continue operation«. For this year, König & Cie was among such players.

Klemme expects those in charge of rescue efforts for distressed vessels to reconsider: »We do not need unrealistic scenarios with banks extending life-cycles. Take a look at HSH Nordbank and it becomes obvious that in such cases we face an even bigger problem which will cost the taxpayer dearly in the end«. The Commerzbank, which had decided to phase out ship financing three years ago and since then consistently decreased the portfolio, is seen as a positive example by Klemme.

Like Simon Aust, Executive Director of the brokerage firm Harper Peterson & Co, the Managing Director of Reederei Nord sees a problem with the market power of alliances and shipping lines. »A major problem is the behaviour of the competition authorities. They very generously approve line shipping collaborations. For us tramp ship operators such approval is far more difficult to get,« criticized Klemme.

Industry speculation has it that indirect or »soft« price-fixing would be practiced which would be highly problematic under competition law. Hapag-Lloyd COO Firmin rejects this: »There are no agreements, even within alliances. The shipping companies negotiate prices with their customers separately«. This also applies to charter. Although talks on cascading measures exist, »but only for a company's own ships, not for charter tonnage«.

As for tramp shipowners both Aust and Klemme have not such a negative vision of the future as others. »When the new Panama Canal is opened, I expect a recovery. In the medium term I see reasonable markets for the container shipping industry,« said the broker. Aust justified this with the situation in North America, where many ports are not designed for large ships. »This creates inefficiencies in fleet operation, which in turn binds tonnage«.

Nevertheless, another, at least temporary consolidation in the tramp sector is necessary, he believes. For years now it is said that a large part of many small and medium-sized charter shipowners who have shaped the industry in Germany cannot survive at such low rates and concentration will be indispensable. There have been diverse pool developments or cooperations in charter, recently Hanseatic Unity Chartering emerged, where Borealis Maritime by Christoph Toepfer is pooling its own chartering activities with those of O&S Chartering which was founded in 2013 as a cooperation of Reederei Nord and the Schulte Group. Previously, other actors have taken a similar step.

The main arguments in favour of pools are size, better geographical coverage of available tonnage and their effective use. »Along the way« this supports the banks' demand for larger units. Otherwise such projects also involve pitfalls such as conflicts whose ship will get a specific job. One possible solution to this is the pooling of revenues, which continue to remain insurance tax free in the future pursuant to a decision of the German Federal Ministry of Finance. However, the silver bullet was not found yet. According to Aust, this could help to stop the fall in charter rates and to ensure more balanced power relations in the competition with shipping lines. As for Klemme pools are also of great importance: »Mergers are difficult, simply because of the existing vanities in shipping. When pools are discussed, the antitrust authorities are more generous«.

Broad portfolio

In multipurpose shipping which is also subject to overcapacity, BBC Chartering from Leer and competitor Intermarine showcase »performance« as operators to acquire customers. New and efficient ship designs are hugely important, attendees agreed on the HANSA-Forum. A further option is to optimize the on-board operation. Albrecht Grell of classification society DNV GL explained the application and advantages of »Big Data« in shipping. Corresponding projects would increase the efficiency of the fleet and lead to more transparency. An important aspect for charterers and partners, Grell said.

Among those issues not only intensively discussed in Hamburg ship financing or the procurement of capital was high on the agenda. Lars Solbakken, CEO of Norwegian provider Ocean Yield, presented strategies how German players may realize new business in project partnerships with international investors with reference to the example of Reederei Hartmann from Leer. Also IPOs or private equity are still considered apt instruments of raising capital, as speakers from Norway and the US pointed out.

The German KG-industry has to prepare for more difficult years ahead. KG financing was a model which had grown enormously during the boom years of the local shipping industry. David Landgrebe Board at HCI Capital, disclosed that new ship funds are probably not to be expected prior to 2018 since the mood among investors is currently too bad. During the crisis, the number of HCI funds previously dropped from 340 to 190. Like Jens Mahnke, Managing Director at competing König & Cie, he believes that it will be quite possible to raise capital at the retail market with KG-projects in the future. »It will be important that the management will be much less complicated and more transparent, for example, a switch from analogue to digital processing for the customer.

Currently there is considerable uncertainty about the future of HSH Nordbank. After the EU Commission decision to reduce the shipping portfolio by a total of 8.2 billion € to be followed by privatization it is currently not clear yet where the bank will be heading – even in-house. In which framework HSH could persist is thus uncertain. Details have to be worked out by the parliaments of the owner states of Hamburg and Schleswig-Holstein. »Until then, any further considerations are nothing but speculation,« Ingmar Loges, Head of Shipping Finance at the HSH Nordbank, said. He added the bank, however, wanted to continue as an active market player. Consequences for the rest of the banking sector cannot be ruled out, added Oliver Faak, Global Head of Ship Finance at Nord / LB.

The traditional HANSA-Forum »Shipping | Financing« at Hamburg's Hotel Grand Elysée was held for the 19th time while some 450 attendees met to discuss new business models, threats to the industry and models to counter the tremendous challenges. Under the motto »New Horizons« three panels dealt with the pressure for consolidation in container business, recent trends in charter in multi-purpose but also ship operation as well as national and international aspects of financing.