

The outlook and prospects for the small Greek owner

By
Ted Petropoulos

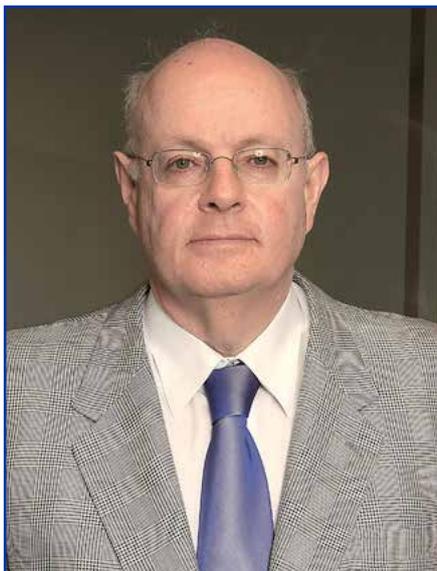
Head, Petrofin Research

A notable feature of Greek shipping has been the plethora of small owners, defined as operating fleets of 1 to 4 vessels.

Petrofin Research © has been closely following the evolution of small owners over the years. In Graph 1, you will observe that compared with 10 years ago, the number of small owners has remained relatively steady at about the 450 mark. Admittedly, following the mid 2000's dry bulk boom, many new owners emerged increasing numbers to 515 in 2011, before returning to the 450 base over the last 3 years. In the same Graph, you will observe that whilst small owners' shares of Greek shipping has declined from the 11.96% peak in 2007 to 9.46% last year, the sector's total deadweight rose from 11.3m dwt to 28.7m dwt, over the last 10 years.

The demise of small Greek owners has often been prophesied in the past but the sector has shown remarkable resiliency over the years, despite the usual shipping cycles and other pressures facing this sector. The arguments of those who foresee the decline of the small owner have been centered primarily on the economies of scale argument. Larger fleets command better insurance, purchasing and attention by all shipping providers, from insurers to suppliers to shipyards and the banks. Whereas it is not possible to determine precisely the extent of the economies of scale cost advantage enjoyed by large owners, the benefit is thought to be significant. In addition, the complexity of regulations and compliance has impacted more severely on the small owner, who has a smaller operation and staff. In the age of near perfect information, though, small owners too, can adequately tackle the field of compliance. Banks have for a long time shown their support for the large corporate structured owners and for quoted public companies. Small owners have, though, been able to continue financing their requirements with Greek banks, as well as a number of non-Greek banks.

Small owners, have some comparative advantages of their own. Owners and managers are often the same persons and who are very 'hands on' and committed to their companies. Lines of communication are shorter and decisions are made swifter. There is a stronger



team spirit and a model closer bonding among the managers and their staff. The attention given to vessels is higher and often they can be more proactive and quicker to respond to emergencies. They enjoy personal relationships across the whole spectrum of shipping services' providers, built over decades. Family ownership provides the committed evolution of small owners, which remain tightly owned and controlled.

We fear, though, that we stand at a watershed for small owners. Recent banking developments may put this sector at risk and drive many Greek small owners out of business. Small owners may be less financially sophisticated and may obtain less attractive ship finance terms and loans per vessel than their bigger brothers but they have always been able to secure some financing from a small number of banks that support Greek shipping.

In Graph 2, you will observe the evolution of the number of banks that have provided loans to Greek shipping since 1992 (Petrofin Bank Research ©). As you will observe, the numbers are supportive of Greek shipping with non-Greek banks without a Greek presence expanding noticeably over the last decade. In Graph 3, you will observe the same evolution but adjusted for the loan portfolios of each bank. As you can readily see, the non-Greek banks with a Greek presence have been declining from 2008. The same applies to the

main supporters of the small Greek owner, the Greek banks, whilst non-Greek banks without a Greek presence have shown a consistent rise.

Our concerns, however, lie over the following factors that affect the Greek ship finance and the small owners, in particular:

1. A number of the non-Greek banks that have enjoyed long and substantial support to Greek owners, such as RBS, HSH, Commerzbank and others have been declining, as a result of their own decision to reduce their overall shipping exposure and / or Greek shipping.
2. All banks have been increasingly focusing on the large Greek owners with modern eco ships and either strong corporate owning structures or being publicly quoted, primarily in the US markets.
3. The banks' risk departments and their credit risk models have long favoured large owners, who tend to be more liquid and their financial position more transparent. This has affected mostly the small owners, who are often outside a bank's target list and who are thought to be inherently more risky to the banks.
4. Small owners are perceived as having reduced options, when facing a market trough, as they cannot raise additional public equity or other means to support their companies.
5. Newcomers to the industry (often operating from outside Greece) have also favoured the large Greek owners, as they lacked the local knowledge and presence, to handle small owners.
6. Chinese and other Far Eastern owners have also favoured the large Greek owners, as they concentrate on ship finance for vessels constructed at local shipyards.
7. Greek banks, in particular, have been adversely affected by the "continuous" Greek crisis. Despite receiving substantial fresh capital from the EU, as well as from private and corporate investors via the Greek Stock Exchange, their liquidity and capital adequacy has fallen. The recent flight of deposits and capital controls has hit Greek banks very hard

and has prevented them from supporting Greek shipping in general and small owners, in particular.

8. All banks have been adjusting their loan exposures and appetite across all sectors, including shipping as a result of compliance with the Basle III capital adequacy targets, as well as those imposed by the ECB, who assumed supervisory authority for all EU banks. With limited loan capacity and facing the lingering effects of the 2008 financial and banking crisis, it is no wonder that banks are aiming on their lending strategies. Often, lending has been refocused, in accordance with National criteria, whilst at all times shipping would compete with loans to other sectors, offering similar risk / rewards.

The above facts have been increasingly felt by all small owners, when looking for fresh finance. The adverse development has affected most the small owners with modern fleets (0-9 years old), who constitute 17% of small owners. These owners are keenest to grow into medium size and will be even more frustrated by the banks' reduced appetite. Consequently, small owners, who could benefit from buying inexpensive vessels at cyclical lows will increasingly rely on their own liquidity, to support their acquisition program or turn towards joint ventures with private equity funds. As small owners are fiercely independent, such joint ventures are not their priority.

The reason that we believe that we are at a watershed for Greek small owners is the virtual lack of finance available at present. Small owners are struggling to secure finance for their new purchases in this market and face very tough and expensive terms. Often, they need to resort to buying vessels for cash, which cannot continue for long. At the same time, the shipping crisis has affected a number of small owners, who may well not be able to survive the crisis. Unless, therefore, bank appetite for Greek small owners returns somewhat, we fear that small owners leaving the industry will not be fully replenished by fresh ones. Consequently, we foresee the small Greek owner segment contracting most severely over the next years.

There is an additional de-stabilizing factor, though. There is considerable concern over the tax status and position of Greek shipping, as the country desperately needs more taxes and as Greece has committed itself as part of their 3rd austerity package to gradually remove the favourable constitutionally guaranteed tax status of Greek shipping. Many large owners have developed plans for leaving Greece, although few have actually done so, as they are awaiting for developments. A number of large owners have already set up an operating basis outside Greece e.g. Cyprus, which they can utilise at short notice, to switch all their operations out of Greece. Small owners, though, are less able to uproot their family business from Greece and set up afresh abroad. A number may choose to stay and face the increasingly less favourable conditions for Greek owners, with many of them biding their time until the next market peak, when they might sell their fleets and disband their companies.

Small Greek owners are currently facing numerous challenges that are more pronounced than bigger owners. Their ability to survive, despite their fierce commitment, will depend on their ingenuity and flexibility.

