

KARATZAS

MARINE ADVISORS & Co.

Shipping Finance Advisory, Ship-brokerage and Maritime Services Firm

Navigating The World of Modern Shipping Finance: Developments, Challenges & Opportunities

Grain & Maritime Days in Odessa, Ukraine

May 30th 2019
Maristella Marine Residence


'Safe Harbor' Statements

 'And seas but join the regions they divide'

Alexander Pope







 'In Sea affairs, nothing is impossible, and nothing is improbable'

*Admiral Lord Nelson, writing from
HMS Victory in 1804*

 'If you want to build a ship, don't drum up the men to gather wood, divide the work and give orders. Instead, teach them to yearn for the vast and endless sea'

Antoine de Saint-Exupéry

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-  **Agenda & Company Introduction**
-  **Shipping Industry Review**
-  **Shipping Finance Review**
-  **Parting Thoughts & Conclusions**
-  **Company Contact Details**
-  **Appendix**

Karatzas Marine Advisors: Company Introduction

- Client-focused, results-oriented shipping finance, ship-brokerage and services firm
 - Established in 2011, headquartered in Manhattan, NY, satellite office in Hamburg, Germany
- Active on behalf of institutional investors, shipping banks, leasing companies, alternative capital firms and capital providers in shipping industry
 - Originate transactions in the tanker, dry bulk, containership and offshore sectors of shipping industry
 - Equity and debt, preferred capital, mezz, leasing, joint-ventures
 - Disposition and sale of shipping assets, including auctions and judicial sales
 - Advisory services including due diligence, vessel valuations, business valuations
- Active on behalf of operating shipowners
 - Source financing for acquisition, expansion, growth, restructuring
 - Advisory services including due diligence, vessel valuations, business valuations
 - Vessel Sale & Purchase (S&P) services on exclusive mandates
- Management team bears decades of multi-faceted shipping industry expertise, and access to C-suite executives in the industry worldwide
- Well-representative existing clientele base with worldwide footprint
- Impeccable credentials & references

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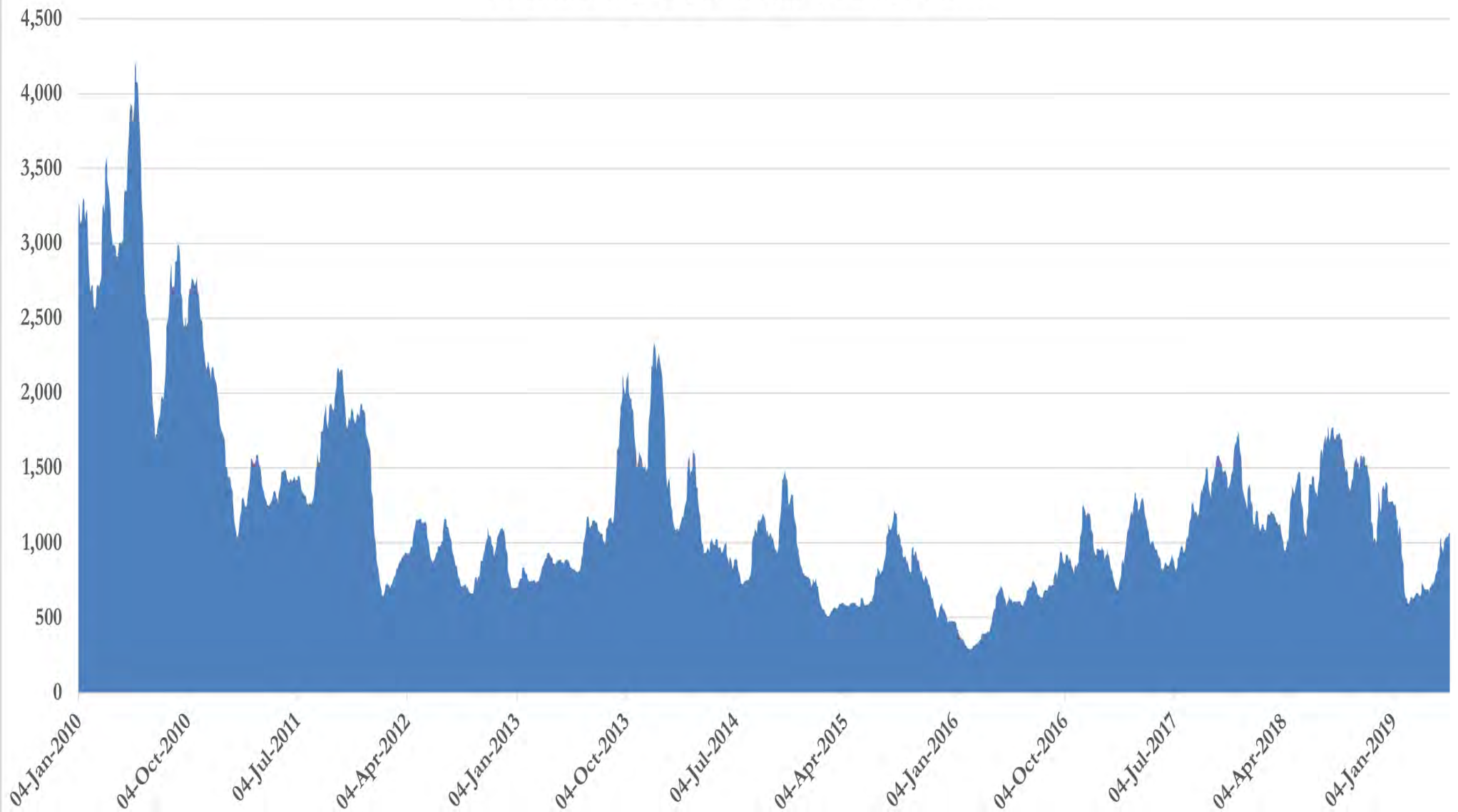
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The Shipping Industry in the Last Decade: The Course of the Baltic Dry Index (BDI), the Industry Proxy

Baltic Exchange Dry Index (BDI), since JAN 2010





Characteristics of the Shipping Industry




Extremely Volatile

-  Although volatility has declined in last decade, still high by many standards



Capital Intensive

-  Always it has been so, and although presently ships are priced in the lower-end of price range in last decade, today's fleets have to have many vessels to be cost efficient
-  Industry highly dependent on interest rates, cost of capital and availability of credit



Diverse Market

-  By asset class (type of vessels, and also trading pattern)
-  By employment type and revenue stream (spot market vs time-charter, etc)
-  By cargo and region

Geo-politics




-  Talk of “trade wars” affects trade volumes both negatively (tariffs) and positively (disruption of established supply chain and trading routes)
-  Trend for “onshoring” and “near-shoring” (vs “offshoring”) / anti-globalization

Regulations & Technology




-  **Environmental regulations (IMO2020) are getting heightened**
-  Disruptive technologies, Automation, Digitization, etc necessitate larger fleets in order to maintain cost/vessel low

“Drivers” of the Shipping Industry




Fiscal & Monetary Policy

-  Governments worldwide try to stimulate anemic growth
-  Major central banks maintain historically low interest rates and likely to do so in the near future
-  Higher banking regulation


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-  China can be a “frenemy” (friend and/or enemy) to any commodity or trade

Macro-economics

-  Economic growth likely to decrease due to tariffs / trade wars, when uncertainty rises and firms are hesitant to invest / trade

Shipping Finance, the way it was

FINANCING A SHIP ACQUISITION

CAPITAL STRUCTURE

DEBT (~70%)

FIRST PREFERRED SHIP MORTGAGE

- * SHIPPING BANKS
- * PRIVATE, BI-LATERAL DEBT
- * CHARACTER, CREDIT, COLLATERAL, CAPITAL (4 'Cs' OF LENDING)
- * NAME LENDING
- * 60-90% LEVERAGE
- * RELATIVE SMALL PUBLIC DEBT MARKETS (SHIPPING BONDS, "JUNK BONDS")

EQUITY (~30%)

OWN EQUITY / "SWEAT EQUITY"

- * SHIPOWNERS' OWN EQUITY
- * POSSIBLY SOME JVs / PRIVATE EQUITY (SELECTIVELY)
- * MOSTLY PRIVATE MARKETS, SELECTIVELY PUBLIC MARKETS (IPOs)

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Shipping Finance Developments since 2008

- Shipping freight market collapse in 2008 caused massive losses for shipping banks
- When political considerations came to play (including state bailouts), several major shipping banks were forced to exit the industry
- “Bad” shipping loans still provide an overhang over the industry (as these portfolios of ships can be sold in the secondary market, still; some of such portfolios are now owned by U.S. private equity funds, which have been aggressive toward shipowners-in-default)
- A decade after the crisis of 2008, the market has never reached a structural recovery, resulting in:
 - More losses for shipping banks and institutional investors that entered the market 2010-2015
 - Most operating shipowners barely generating an operating profit while several have burned through their cash reserves
- Banks start becoming heavily regulated, causing further loss in the shipping industry
- New players in the shipping market
 - China no longer a passive commodity importer; besides and active shipbuilder, now, a major shipowning nation with great shipping finance ambitions (export credit, Chinese leasing)

State of Shipping Finance Today: Shipping Banks

- Shipping banks' declining interest in the shipping industry
 - Past losses have brought to focus “riskiness” of the shipping industry
 - Sale of shipping loan portfolios, shipping assets, exiting shipping altogether
- New banking regulatory environment makes shipping a costly industry
 - Ship mortgages as “asset backed financing” are costly
 - Preference for corporate finance / “balance sheet” finance
 - “Green finance” is the next frontier of bank regulation and loan availability
- As a result, focus on shipowners that “check the boxes”
 - Consolidated financials & large and strong balance sheets
 - Cash flows, charter coverage, COAs, etc
 - Trading ships on “spot market” is risky business
 - Bi-furcated shipping lending market:
 - Certain, and very few, shipowners have access to extremely competitively priced shipping loans
 - Majority of traditional shipowners are “un-bankable”

Accounting at corporate level, and fleet size are important!

State of Shipping Finance Today: Private Equity

- Early “golden era” of PE investing more than \$5 bln in newbuildings in 2011-2013 has resulted in substantial losses in shipping due to ill-timing and over-optimism
 - Some private equity funds have not “realized” their losses yet, a market unknown
 - Private equity funds having invested in distressed debt anecdotally have had a better performance
- Private Equity funds, in general, lost interest in further investing in shipping, due to
 - Previous bad performance
 - No clear “catalyst” for a market recovery
 - “Buy low, sell high” or “buy cheap ships” has gotten tired
 - Most of the new investment projects offer no differentiation
- Private Equity funds selectively keep an eye on shipping for
 - Projects that have a “unique story”
 - Access to captive cargo or competitive advantage
 - Industrial shipping

Solid business plans, distinctive competitive advantage, and fleet scale are preferred!

State of Shipping Finance Today: Public Markets

- Many of the hopeful publicly listed shipping stocks and IPOs of last decade have become “penny stocks”
- Fair reputation of shipping companies on Wall Street
- Limited appetite for shipping IPOs due to risk, lack of clear “market driver”, but also overall market conditions
- Selectively, limited appetite for yield / dividend stocks (at least while interest rates stay low) and selectively secondary public offerings / “follow-ons”
- “Four ship” shipping company IPO is as dead as a doornail; companies seeking to access the public markets have to have excess \$1 BILLION in market capitalization and solid business record
- Bottom line:
 - Shipping companies with big fleets only matter
 - Solid business model and track-record
 - “Never say never”, but for now and the foreseeable future, public markets can only consider large shipping companies; shipowners of fewer than 20 ships no need to apply

Large shipping companies with long records are important!

State of Shipping Finance Today: Leasing

- Chinese and Japanese financial institutions getting more active in shipping, mostly as yield investors, in the form of leasing
- They can offer up to 100% “financing” and at a competitive cost of capital (even below 5%)
- While originally intended for strategic clients (ordering newbuildings in captive shipyards or group companies), or for strategic purposes (affiliated cargo owners and commodity importers), Chinese and Japanese leasing have been growing to encompass non-strategic clients and projects, and smaller players, but still
 - Will only consider companies with big balance sheets (at least several hundred million of dollars)
 - Consolidated financials
 - Although it can be arranged as off-balance sheet finance, for Chinese and Japanese leasing, size and quality of balance sheet matter tremendously
 - Still, a form of financing for sizeable companies (of more than 20 ships)

Rather large companies, preference for balance sheet finance and large fleets are strongly preferred!

State of Shipping Finance Today: Credit Funds

- It seems that a “credit fund” or “alternative capital fund” has been getting established every quarter in the last couple of years: a tangible sign that shipping debt (lending) is dysfunctional
- Can consider “project finance” and single-vessel acquisitions, but
 - Cost of capital is high (usually in 8-12% range, and “double digits” are not unheard of, depending on circumstances)
 - Moderate leverage (typically 60-80%, but there are minor exceptions)
 - Tight covenants and terms
 - Not indiscriminate lending / financing
 - Often require proper accounting and corporate governance
 - Be prepared to pay less or more as level of risk decreases / increases
 - Be prepared to actively deal with breaches of terms and covenants; unlike shipping banks, do not expect a passive, patient approach

Can really be the way for long-term financing for the shipping industry?

At 8 - 12% interest?

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Parting Thoughts

■ **Access to Capital is the new “name of the game” in shipping**

■ **The next generation of Shipowner will look different from the Shipowner of the past**

- De-emphasis of the tramp trade / spot market
- Cash flow visibility via time-charter employment or COAs
- Consolidated financials
- Critical mass of fleet (25+ vessels)
- Comprehensive business plan in place

■ **Banks to still be the “lowest cost of capital” provider; but**

- Fewer banks
- Likely regional banks more active to regional (non-international shipowner)
- Higher competition for shipping projects

■ **There always be capital available to shipping, but**

- At a higher cost
- Opportunistic (for distress or growth opportunities)
- Dependent on the employment prospects of the vessels

Positioning

“Cargo is King!”

- An old saying in shipping, but always wise!
- Cash flow visibility is critical in today’s finance - whether for equity, debt, mess or leasing
- Time charters are great, but quality of the charter-party is critical
 - Focus on end-users and cargo owners
- Become a “transport need” solution provider, become part of the supply chain
 - Provide transport solutions, even if it requires custom solutions
 - Become indispensable to the supply chain
 - Consider industrial shipping projects too!
- Shipping is considered a “commodity” business; unless a shipowner has a sustainable competitive advantage in such, “commodity” shipping will become obsolete!

Focus on cargoes, Contracts, Transport Solutions!

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Karatzas Marine Advisors & Co.

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What Separates KMA from the competition?

Dedication, focus, hard-work and a solid track-record of delivering value for the Clients time and again

- More than \$500 million in sale & purchase transactions
- More than \$500 million in financial transactions in shipping
- Extensively published / mentioned / quoted on maritime maritime in the international business press and trade publications
- Have repeatedly consummated value-added transactions with ‘Fortune 10’ companies
- Have solid record of ‘repeat customers’ and strong customer referrals
- Have done business with national oil companies and other state-own companies
- Solid record of results-driven performance with integrity and professionalism
- No ‘legacy issues’ or ‘hidden agendas’ of ‘conflicts of interest’ / Transparent structure

Above all, simple business strategy: **We Sail the Extra Mile for the Client!**

Core Competencies & Business Philosophy

Core Competencies

- In-depth knowledge of the shipping markets and access to decision makers worldwide
- Access to institutional investors, private equity, fund managers
- Timely access to market information**
- Management's diverse business & professional background encompassing entrepreneurship and venture capital, finance & leasing, advisory, vessel operations and managements, ship brokerage, project & term chartering

Business Philosophy







- Integrity, Accountability, Confidentiality, Loyalty
- Adamant belief in that only 'win-win' structures are long-term successful and profitable
- Due diligence, and knowing intimately the client, their needs and goals
- 'At all times the idea of doing only first-class business, and that in a first-class way, has been before our minds.' **J.P. Morgan, Jr;** May 23, 1933; Excerpt from statement made before the Sub-Committee of the Committee on Banking and Currency of the U.S. Senate.

Our vessel valuation pedigree: well proven and solidly qualified

- Assisted in the preparation of two case studies on vessel valuations with *Harvard Business School* in 2010
- Have performed more than 5,000 valuations
- Valuations have been utilized in the Initial Public Offering Prospectuses (IPO) with companies on the New York Stock Exchange (NYSE), Singapore Stock Exchange (SGX) and Hong Kong Exchange (HKEx)
- Valuations have been utilized for the Annual Report and quarterly financial statements of publicly traded companies in the US and overseas
- Valuations for asset-backed securitization, including valuations or expert opinion ("SLV Expert Opinion", "Schiffsbeleihungswertgutachten") under the German Pfandbrief Act
- Approved valuator for numerous banks worldwide

(references gladly provided upon request)

Scope of Services: 'Turn key' services & services complimentary to Ship Brokerage (S&P)

-  Custodial services for vessels, including crewing and crew repatriation and addressing regulatory and statutory issues (in strategic alliance with one of the most reputable technical managers worldwide; details gladly provided upon request)
-  Commercial and technical management of vessels for short / long-term periods, or until a more opportune time for sale of asset can be strategized upon (in strategic alliance with one of the most reputable technical managers worldwide; details gladly provided upon request)
-  Creditor representation at auction sales
-  Anonymously credit-bid on behalf of creditors / 'sellers'
-  Provide and/ or work with off-balance-sheet SPV companies / 'warehousing platforms' to manage vessel
-  Combine 'warehousing platform' solutions in conjunction with equity injections / structured finance, and/or in conjunction of providing competitive vessel employment through spot or period charter, and possibly through COAs

Worldwide Expertise & Credibility

The
Economist

“Still at Sea”, Basil Karatzas quoted in The Economist, March 4th, 2017

“Ruling the Waves”, article written by Basil Karatzas in Week in China (Hong Kong), March 3rd, 2017

“Shipping Crisis Hits German Banks”, Basil Karatzas quoted in The Wall Street Journal, February 10th, 2017

THE WALL STREET JOURNAL.
WSJ

“Trade and Shipping: The World is not Flat Anymore”, article published by Basil Karatzas in the Cayman Financial Review, January 2017

“Perfect Storm Looms over Shipping Lenders”, The Financial Times, September 21st, 2016

FT

“Container Ships Stranded At Sea After South Korean Company Goes Bankrupt”, Basil Karatzas interviewed on National Public Radio (NPR), September 6th, 2016

FINANCIAL
TIMES

npr

“Stranded at Sea”, Basil Karatzas interviewed by the Canadian Broadcasting Corporation (CBC), The Exchange, September 3rd, 2016



“Fender Benders on Water; See Expanded Panama Canal”, Basil Karatzas quoted in The New York Times, July 31st, 2016

The New York Times

Professional Memberships & Credentials

- American Society of Appraisers, Accredited Senior Appraiser (ASA) accreditation
- Institute of Chartered Shipbrokers (ICS), Fellow
- The Baltic Exchange, Member
- BIMCO, Member
- Propeller Club, New York / New Jersey Chapter (past Board Member)
- Society of Naval Architects & Marine Engineers (SNAME), Associate Member
- Royal Institution of Naval Architects (RINA), Associate Member
- Royal Institute of International Affairs (RIIA), Member
- Piraeus Marine Club (Greece), Member
- American Bureau of Shipping (ABS), past Member
- Harvard Business School (HBS) alumni
- Rice University, Jones Graduate School of Management alumni



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