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Euronav/Gener8 deal, the C-word, and getting to the 'magic number'

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The announcement of Euronav's all-share acquisition of Gener8 Maritime came after years of pounding the virtues of the C-word – consolidation - by Euronav's ceo Paddy Rodgers.

When this deal closes, presumably in Q2 2018, Euronav will boast a fleet of 75 crude oil tankers, including 44 VLCCs and 28 Suezmaxes. According to a report from brokers Evercore ISI shipping analyst Jon Chappell, the market capitalization of the combined company will be on the order of $1.8bn based on current prices.

Though the word "consolidation" is thrown around frequently at ship finance conferences, and the drinks parties afterwards, it comes in multiple flavours - much like the beverages being swilled. The three most frequently mentioned aspects of combining shipping companies are: market power (ability to influence prices), economies of scale (administration/ operation), and heft in the capital markets (ability to raise money).

Looking at market power, it's hard to make an argument for a movement of the combined entity toward true "pricing power". A back of the envelope calculation, using data derived from Clarksons, implies a year-end 2017 fleet of approximately 745 VLCCs and 515 suezmaxes with aggregate deadweights of 230m dwt and 81m dwt, respectively. The tanker market is, if anything, "fragmented"; by the measures of vessel count and aggregate deadweight tons, the business combination represents perhaps the morphing of two minnows into a respectively-sized but still smallish fish.

It's useful to contrast the tanker market with its more concentrated cousin- the liner shipping market, where the top dog Maersk Line with 4.1m teu of owned+chartered capacity following its absorbing Hamburg Sud, controls roughly 19.3% of the market, based on Alphaliner computations. In 2017, the liner sector has shown a strengthening, which the experts attribute to its numerous mergers and sharing arrangements through alliances- where the top 10 players are thought to control more than 65% of the market.

For Euronav, on the VLCC front, the combined entity would control 6% of the vessel count; in a reckoning of million-barrel suezmaxes, the calculation yields a share closer to 5%. When the overall dwt is considered, the number-crunching exercise yields a result of roughly 6% portion of the market's capacity- large (for tanker watchers) but unable to influence the market on a sustained basis.

In the Euronav deal, there will likely be a benefit as economies of greater scale are achieved- with management and operating costs spread over more units. Indeed, there combined entity may be approaching a n optimal size in this regard. Deutsche Bank shipping analyst Amit Mehrotra, interviewed in a recent Capital Link podcast, identified the "sweet spot" as being companies operating between 50 and 100 vessels.

And then there are the capital markets, where listed shipping entities struggle to break out and rise above the $1bn capitalization ceiling typically defines a "micro-cap" listing. In this regard, size begets strength, and, according to the panelists at numerous Marine Money and Capital Link confabs, an ability to gain attention from institutional investors- and, in turn, raise more money for fleet growth,which might come through additional business combinations.

On the same Capital Link podcast, Mehrotra, who had theorized about the Euronav/Gener8 transaction in May, 2017), "…there is a significant advantage to being larger…and investors like to throw around the $1bn mark…as the magic number."

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