Private Equity Looks Towards Shipping

The Private Equity (PE) boom, usually taking the form of investment funds buying out entire companies or divisions of larger entities, has touched every major industry- including the shipping business. Closely related has been a wave of investments, by specially purposed “infrastructure” funds, in port and terminal assets. Investment banks and PE firms are raising staggering amounts of money. Goldman Sachs just completed a $20 Billion raise (GS Capital Partners VI), rivaling a $15 Billion inflow to TPG (was Texas Pacific Group- an investor in the maritime dotcom “Levelseas”). TPG’s latest fund mirrors similar sized raises by PE players Blackstone Group and Kohlberg Kravis and Roberts (KKR)- the subject of the book “Barbarians at the Gate”. Meantime Blackstone and TPG are selling shares in themselves.

Deal templates vary but the PE funds’ objective of “buying low and selling high” transcends differences in financial structuring. Frequently, a central management company, serving multiple holdings, reaps fees. After some period of private ownership, the payday for investors in a fund comes with a “liquidity event”, which could be a public offering, or possibly a sale to another fund. Typically, original investors and company management will retain a major shareholding, even after an offering.

U.S. Shipping Partners L.P. , a partnership now traded on the New York Stock Exchange, (“USS”) is an example of a successful leveraged buyout, sponsored by a Sterling Partners LP, a Connecticut PE fund shop. In late 2002, a large oil company, Amerada Hess Corporation, seeking to raise cash for investment in refineries, sold its fleet of six U.S. Flag Integrated Tug Barges (ITBs) to a Sterling investment fund, for a price in the region of $200 Million- much of which was financed with new debt, or “leverage”. Two years later, in 2004, the original investors, mainly insurance/ pension companies such as Aetna and Travelers, were amply rewarded as the debt was repaid and the company completed its Initial Public Offering of partnership units. Last Summer, Blackstone Group announced that it would be investing jointly with USS and building new tankers for the US Flag trades.

Horizon Lines offers a similar example of financial legerdemain. The US Flag arm of what was once SeaLand Corporation was jettisoned by CSX Corporation in early 2003, and picked up by funds within the influential Carlyle Group for around $300 Million. In mid 2004, after investing in the Horizon brand, Carlyle flipped the company to another private equity shop, Castle Harlan Partners (CHP), for $650 Million (including debt of nearly $400 Million). CHP, no stranger to shipping with previous investments in Statia Terminals, has since achieved its payday through an offering of Horizon shares owned by a CHP fund.

In late 2006, PE shop Madison Dearborn Partners floated the IPO of Great Lakes Dredge & Dock- involved in towing and infrastructure repair. Apollo Partners, where famed financier Michael Milken's son works, made news this past February, 2007 with its purchase of Oceania, valued at $850 Million (including around $375 Million of debt). Its efforts to use financial muscle to build the brand, for possible re-sale, were evident with its announcement of a two vessel order from Fincantieri, shortly after announcing the Apollo deal.

Going forward, continued buoyant economies will fill the coffers of investment funds, who will seek business with a baseline of predictable cash flows and some growth prospects. Port officials and corporate strategists will carefully consider offers to unload non-core assets to PE investors at a time of plentiful debt finance available at low interest rates.

The booming dry market may presently be too hot to touch, but tanker companies, who have experienced a market down from its highs (and could therefore turn higher), have already been on the PE radar screen- an offer from one PE investor (believed to be Fortress Investment, itself listed on the NYSE, the same group that management had brought into the Stelmar fray in 2004, at a lowball $25.00/share) was the actual catalyst that triggered OMI Corporation's selling process during March 2007. Bankers eventually shopped OMI to 13 PE funds; and five subsequently signed confidentiality agreements, an expression of serious interest.

UPDATE: an article all about OMI is posted elsewhere on the site. Strategic buyers, ie buyers from the industry (Teekay and Torm) sailed a course around the financial buyers (ie the PE funds). So, a big question is whether shipping people can see value, or can see synergies that are worth money, that will enable them to bid above non-shipping players. This question does not have an answer- we should keep a weather eye on shipping deals and also port / infrastructure deals for the answer to this question.