

Sailing the high seas of the stock market

Tanker stocks, like those of other industries, have taken a beating in recent months

Fickle investors have learned that the laws of gravity and cyclicity apply, often simultaneously. In a market that has tossed all the boats around with nobody emerging unscathed, conservative shares have done better weathering the storm. The darlings of early 2001 are this year's wallflowers, as shares generally have taken a battering on slumping stock markets all over the world. In the bellwether US markets, major stock indices are back to pre-Internet boom values, after a dismal performance in the 3Q at a time of softness throughout the tanker sector.

The strategy at many of the big tanker players has been to prepare for the next leg upward, whenever that may come. OPEC production, a major impetus behind tanker rates, is down by some 4m to 5m barrels per day from its heady levels of two years ago, amid a long elusive quota discipline that is incentivised by a weak economic outlook. Did anyone say "double-dip recession?" Oil stockpiling, amid bellicose war talk, has bolstered demand, as evidenced by some upward blips on the rate graphs. Unfortunately, the blips cannot yet be connected to a rising trendline.

Financial news and strategic alliances or decouplings, rather than exciting operating results, have dominated the actions of the big players as they reposition for the next market upturn. All of the big stocks are underwater when market value is compared to book - the conservative plays less so in this down cycle.

Rainy day strategies, i.e. what to do until recovery time, have been all over the map. Some listed companies tried to prop up their prices with company buybacks, while others have seen insiders adding to their private holdings, reminding analysts of that maritime conundrum - that very fine, sometimes indiscernible, line between public and private companies. Operating measures have included acquisition of cheap assets (not necessarily conservative financially) and/or scrapping older tonnage to bring in cash. Tanker companies are also experimenting or bolstering their presence in diverse market sectors - perhaps trying to look at value-adds rather than mainline moves. For example, two recent OMI Suezmax newbuilds were reported trading spot in the clean products sector, at the same time that shipping giant Maersk was targeting orders for large clean trading Aframaxes.

Life on the stock market

As the bloom has come off the rose, the wilting has been noticeable at stalwarts such as Overseas Shipholding Group (OSG). A major player in the tanker sector, OSG's market capitalisation has slumped from over \$1 billion, when shares were at less year's zenith, to less than \$600m with its share price below \$16 (versus book value of nearly \$24 per share). OSG, still paying a dividend, has recently authorised a buyback plan for up to 3 million shares (nearly 10 per cent of those outstanding). On the plus side, a possible sale of older Panamax tankers may bring in some cash. Investors view OSG as a stalwart, as evidenced by investors pricing its shares in excess of five times the cash flow.

Meanwhile, at battered Frontline (FRO) - which has now pulled its VLCC's out of the Tankers International pool (which includes OSG and others) - the private company controlled by insider John Frederiksen has been fattening up his holdings with continued buys. No company has been more expansive than Frontline over the past few years and its latest reports sounded a cautionary note on the use of its shares as currency for further acquisitions, at least for now. Frontline, listed in New York, London and Oslo had shed 70 per cent of its value from 1Q 2002 to 3Q 2002 as both stock markets and tanker markets spiraled downward. Unlike OSG, Frontline, with a massive debt in excess of \$1 billion to support its modern fleet, has now omitted its

dividend. Frontline had synthetically sold shares (which the buyer can put back) using a highly imaginative swap, only to continue marking market exposure all the way down as its share price moved down to around \$4. The current price, less than half the book value, now represents a market cap under \$400m. Some wags noted that under the Norwegian law, Hemen (the private company), with 46 per cent of the outstanding shares, was approaching the point where it would be required to tender for the entire company. Others wondered whether its expensive but growing involvement with British Petroleum signals a new reinvention as an industrial logistics provider, albeit with a high price tag to sit at this table.

OMI Corporation (OMM), is heavily concentrated in crude hauling Suezmaxes (mainly spot) and smaller Panamax and Handy units in the products trades (with some charter cover). OMM, with a stock price that has been stagnant below \$4 (equating to a market cap below \$250m, some 40 per cent below book value), has been working to pay down short term debt and fine tune its credit arrangements to fund growth. Reserves are ample, but total debt is above \$400m. In this soft market, OMI has been acquisitive, and still has a six ship newbuild program.

Elsewhere in the States, Seabulk International (SBLK), operating Jones Act Tankers as well as offshore service vessels, has shown that the marketplace will respond vigorously and positively to an improving story, albeit one of recovery from bankruptcy of the predecessor company. Now recapitalised with a fresh investment from DLJ/ Carlyle, Seabulk reported stronger renewals on charters of its Jones Act product carriers.

Teekay (TK), one of the best capitalised pure shipping plays, along with OSG, gets more respect than most of its peers, as noted by a price/cash flow ratio above 4x. While its price, now around \$27, has been pushed down, this represents a mere 20 per cent discount below its book value, and its market cap is still above \$1 billion. There was growing talk in the market that TK was about to take the plunge on Aframax newbuildings in Far Eastern yards, which it can easily afford given that debt comprises only 40 per cent of its huge \$2.4 billion balance sheet.

New York's three IPO amigos, Peter G (Genmar), Stelios (Stelmar) and Nick (Tsakos Energy) have had mixed fortunes in their first year or so of public life, and clearly illustrate that investors are preferring the conservative approach. After a rally earlier in the year, Genmar (GMR), with the most exposure to the spot trades, has faded back down to a price of \$6, actually half of book value (and way below its IPO price), equating to approximately 3x cash flow. Meanwhile, Genmar has been mentioned as one potential acquirer for big lightering player American Eagle Tankers, as AET's parent Neptune Orient Lines investigates sales possibilities. Stelmar (SJH), with almost complete forward cover for its fleet, has remained in a trading channel above its IPO price, with highs at \$16 and lows of \$14 - about 20 per cent below book value. Investors appear to emphasise Stelmar's almost full forward cover, rather than its 60 per cent debt. Tsakos (TNP), the middle brother in terms of risk perception, has come down to \$11.50/ \$12 (versus its debut at \$15 in 1Q 2002), and has announced its first dividend, \$0.50 per share, with Nick Tsakos pointing to TNP's "current strong financial position".

These Greek boys have a second cousin from the North: Torm, long traded in Copenhagen with ADR's now traded in the US under the symbol TRMD. Torm is emerging as a drybulk/tanker play, having hived off its Liner Division, and unsuccessfully launching a hostile tender offer for Norden. Torm, with a price above \$6, giving a market cap of \$100m, trades for about 2/3 of book value.

Concordia Maritime, traded in Stockholm, has been taking its lumps having sold its ULCCs, and is still trading its 1970s 2m barrel vessels and its two V-Max vessels on T/C to Sun Oil. Concordia booked a loss of \$9m in the first half of 2002, and like others, was waiting for a recovery.

Bergesen (BEA), diversified among dry bulkers, gas and oil carriers, saw 2002 results way down from those of a year earlier. The soft market, perhaps, was

inspiring major investments by the company towards propping up the Oslo share price, part of an ongoing buyback program. With the disappointing rates in the large tanker sizes, around WS 30, the Berge Chief (for a storage project) and the Berge Odel (for scrap) had each been sold, each bringing in around \$7m to \$8m. Gas tankers provide the majority of revenues and cash contribution, but even the gas sector was caught by the double edge sword of the world economic slump and OPEC quotas.

Among other Scandinavian issues, a quick scan of the technical charts of issues such as Odfjell (ODF), Golar LNG (GOL) - still not listed in New York - Stolt (SNI) and Awilco (AWS) all show nearby peaks on the hopefulness of this past March/April. As recession and quotas set in, the result was weaker earnings and six months of downward chart channels through the beginning of the 4Q. At Stolt, ironically, the chemical tanker sector was a better performer than its other holdings.

As this article is being written, war talk continues but without the large inventory stockpiling that would be expected. After all the battering and bruising, analysts in New York have now been downgrading shipping stocks, perhaps the clearest buy signal amidst all the market noise.