MINING APPETITE FOR YIELD
CONTRIBUTION TO SHIP FINANCE

Winner: Peter Evensen

In our estimation, everyone who successfully runs a shipping company deserves an award. The simplicity of the business, moving cargo from one point to another, belies its sheer complexity. Of course, to be successful, a CEO not only needs a deep understanding of the business itself, but also a working knowledge of psychology, group behavior, anthropology, and economics among other specialties to have a picture of the broader factors which drive the business.

Given the cyclicality of the shipping business and its high cost assets, what really matters, at the end of the day, is having the lowest cost ships or from the liner companies’ perspective view, the lowest slot cost. This starts with the ship purchase. Long-term shipyard relationships, strong negotiating skills, perfect timing (ordering when the shipyards have no orders) and getting options are critical because once acquired, the cost is fixed. But it has to be paid for and that requires highly competitive financing to manage the numbers game of limited equity, a growing fleet of expensive ships (one is never enough) and increasing leverage to bridge the gap. Here careful negotiation of coupon, tenor and amortization can reduce the impact of leverage in calculating the all-important cash breakeven cost.

With his banking background, Peter Evensen was born for this role. As Peter rose through the ranks at JP Morgan and then Teekay, ships were mainly financed with cheap bank debt and equity. The possibilities of the capital markets were just becoming apparent, as shipping companies started to go public. Already a public company, Teekay understood the capital markets and enjoyed all of its benefits. Strategically, the company was growing and expanding its business beyond tankers into the marine midstream value chain focusing on shuttle tankers and LNG. It was a happy confluence of a financial need, an experienced public company, and a uniquely open and creative mind.

At some point, Peter and Citi sat down and the subject of master limited partnerships (“MLP”) must have come up. In the late 1980s, the tax code created the tax-free, publicly traded partnerships, which were required to generate at least 90% of their income from “qualified sources,” such as real estate or natural resources.

Sponsors form MLPs to achieve higher valuations and due to this cost of capital efficiency and the resulting valuation premium, MLP projects and acquisitions can be more accretive, thereby providing motivation for a corporation to drop-down MLP-qualifying assets. And lastly, the sponsor retains control of the assets through its ownership of the general MLPs pay out the bulk of operating cash flows as distributions to their unitholders. The stability and predictability of its cash flow is prized by all and that is why most MLPs use a “toll-road” business model, where the partnership receives a fee or “toll” for handling a customer’s product on their infrastructure system. As it does not own the commodity, it has little commodity price risk. From a defensive perspective, the MLP’s assets typically operate under long-term contracts which mitigate the downside risk of a volatile economy.

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In more prosaic terms, the MLP accesses appropriately priced capital from investors who can appropriately value the long-term contracts and their underlying cash flows to meet their desire for yield with less risk.

A look back at Peter’s career shows a multitude of accomplishments too numerous to mention. In addition to successfully managing a complex corporate structure, Peter was a consummate dealmaker. But what has characterized his career and made it incredibly successful in our mind was his championing of “financial fracking”, a concept which refers to his ability to find discrete/bespoke pockets of capital for financing Teekay’s MLP model to shipping that stands as a game changer and a major contribution to the industry. It brought highly competitive equity funding to the industry and introduced the retail investor, previously an untapped source, to shipping. Later, these investors would learn to love preferred stock and baby bonds as well. Peter and Citi were the architects and first movers but a wave soon followed as they saw its many advantages. And, while it has had its problems as of late, the operating model remains intact; it is the MLP market, which broke down but is now in the process of recovery showing the resilience of the model.

Thank you Peter. It was a great run.