

KG firms turn to new model 'opportunity' funds

Patrick Hagen - Tuesday 28 July 2009

GERMANY's ship financing companies, that took the front seat during the containership ordering spree, are facing serious problems, writes Patrick Hagen.

As the economic crisis has deepened so the renowned KG financing scheme has come under concerted attack as the once reliable retail investor customer base has become increasingly insecure.

Feri Rating & Research's KG market survey reveals that German KG houses raised €2.9bn (\$4.1bn) in equity financing for ships last year compared to €3.58bn in 2007. The amount this year is expected to be significantly lower after top companies MPC and Lloyd Fonds reported a huge drop in the amount of capital raised from investors in the first quarter. MPC Capital collected €11.1m against €123m a year earlier and Lloyd Fonds raised €5.5m compared with €78.8m.

However, market leader HCI Capital topped the list of firms who have to publish their results by collecting €21.5m in the first quarter compared with €81.2m a year earlier.

Those KG firms who have given guarantees to banks that they will raise sufficient equity for their fund projects could face major problems. As a rule, a ship is ordered at a yard before the necessary equity has been collected from retail investors. Accordingly, KG houses have to arrange a bridging loan and should a KG company fail to collect sufficient money it has to step in with its own capital. Some KG houses have guaranteed a volume of placements that exceeds their own equity.

KG companies and their investors played a focal role in creating the large orderbook that is now a burden. According to investment house Maritim Equity, German owners have 1,400 vessels on order with a combined value of €50bn, to be delivered by 2013. Many were meant to be financed through the KG market. While some orders have been delayed or cancelled, even if a quarter of the vessels are never delivered a huge volume of new tonnage would still come on the market. Existing shipping funds are also in dire straits. Those of large and well-regarded companies including HCI or Gebab are now asking investors for more money to stave off bankruptcy. One call for investor capital came in April from a Gebab KG fund which financed the 1997-built, 2,900 teu containership *Champion*: the vessel had been idle since November 2008 and the fund's bank had refused to grant a further loan. The bank's action was watched closely by the industry as the *Champion* had not been a problem in the past.

A critical Dirk Schildwächter, Gebab's chief executive, complained that some banks were not interested in helping a debt-free vessel — in contrast to helping ships where they were still involved with a loan.

KG-financed ships have been badly hit by the crisis. The ratio of idle vessels owned by non-operating owners is growing as lines continue to hand back vessels when the charter expires and, in the event that a relatively new and highly indebted KG vessel were to become idle, the fund would soon be on the verge of bankruptcy. Last November, the 1,687 teu, 1994-built *MarCatania*, financed by a HCI KG fund, was hit by the insolvency of South Korean operator C & Line. It was subsequently employed in March for a 40-day voyage by Singaporean operator SE Shipping. The banks granted several additional loans totalling \$1.8m and accepted deferred payments before running out of patience in July and leaving it to investors to decide on the future of the fund.

The risk of a charterer defaulting was often ignored in boom years. Alarm bells only started ringing when Chinese carrier SYMS cut its services in August 2008 and a number of German owners and KG houses had to fix new charter contracts in rapidly worsening market conditions.

This was only the prelude to what was demanded by Chilean carrier CSAV. A group of German owners and KG houses including Peter Döhle, F. Laeisz and HCI had to bail out the carrier with a \$360m rescue package in which they accepted reduced charter payments in exchange for CSAV shares. The compromise took two months to negotiate though it had become clear early in the process that owners would participate in the rescue of the stricken carrier as CSAV is one of the most important customers for tramp owners. The carrier owns only seven of its fleet of 84 boxships. The remainder are chartered in from owners who considered a CSAV collapse to be a worst-case scenario as many of their ships would have headed into lay-up.

Despite this, the German KG system is again proving its adaptability. As investors shy away from buying shares in shipping funds, KG firms are now counting on 'opportunity' funds and a raft of newly established funds to take over distressed ships and sell them at a profit at a later stage. The countercyclical funds give investors a chance to earn money during the crisis while investors in ordinary shipping funds are set to lose money.

The industry never tires of pointing out that investment in ships, aircrafts or real estate projects will sooner or later benefit from the crisis and the decline in the stock markets. Hopes are rising for the second half. But if this upturn does not materialise, some KG companies will be in real trouble.

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