

The Shipping Man

Adventures in Ship Finance



Matthew McCleery

MARINE
M O N E Y
INTERNATIONAL

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The painting on the cover of this book is "Sea of Green" by Suzy Barnard, 2010, oil on wood, 32"x38"; Collection of Alistair & Jaqueline Sawers; Photo credit: Donald Felton

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A portion of the proceeds from the sale of this book will be donated to the Prader Willi Syndrome Association.

About the Author

Matt McCleery is the President of Marine Money International. He is also Managing Director of Blue Sea Capital, Inc., an advisory firm specializing in the arrangement of debt and equity financing for vessels. He can be contacted at mmcleery@marinemoney.com.

Acknowledgments

In delivering one of his well-known pre-conference dinner toasts, I once heard my partner Jim Lawrence remark, “Your friends and your family probably don’t understand what you do for a living, but we at Marine Money *celebrate it!*”

He was right. Over the past 25 years, it has been an honor and a privilege to report on, analyze, explain and support the largely private business of capital formation for ships - and applaud the individuals who make the industry so fascinating and fun. The goal of this book is to capture the unique spirit of the shipping and ship finance business in a way that is, hopefully, both entertaining and educational.

Like everything we do at Marine Money, this book would not exist without the ideas, energy and enthusiasm of our industry friends around the world. I would like to thank Jeff for reading the initial drafts, George for including a few early chapters in Marine Money, Bob for insight into U.S. Coast Guard inspections, Jill and Maren for editing, Mike for his usual sound advice, Eric for helping me figure out what to do with the book, Suzy for allowing me to use her painting on the cover and Cari and Elaine for making it shipshape.

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Above all, I want to thank my wife, Buffy, for supporting this project (and its many, many predecessors).

For my friend Jim Lawrence,

Whose enthusiasm is among the shipping industry's most
valuable assets

Chapter One

Serendipity

Robert Fairchild gazed deeply into the amber numbers illuminated on his Bloomberg terminal, staring in disbelief that something called the “BDI” had fallen by 97%. The three letters, which he quickly learned were shorthand for the Baltic Dry Cargo Index and measured the daily time charter rates paid for cargo ships, had plunged from an all-time high to a 25-year low in just *three months*. As a New York City hedge fund manager who valued volatility, Robert Fairchild was immediately intrigued by what he saw.

The funny thing was he had stumbled on the ocean shipping industry purely by mistake when he typed the letters “BDI” into Google instead of the stock quotation box on his Bloomberg. And although he couldn’t realize it that late morning in early May, his chance encounter with the international shipping industry would forever change his life.

Without the benefit of any analysis whatsoever, Robert Fairchild decided that he had happened upon a historic contrarian investment opportunity— and he made a promise to himself that he wasn’t going to miss it.

Since founding Eureka! Capital ten years earlier, he had come up with plenty of good reasons not to participate in some of the most monumental money making moments in the history of mankind; the inflation and deflation of the dot.com bubble, the rise and fall of the housing market, and the bull-run in agricultural commodities, crude oil and gold. He had missed

them all and his investors, especially Luther Livingston, would never let him forget it.

But the international ocean shipping industry was sure to change his luck, he concluded as he stared at the chart of the BDI, a downward slope steeper than any double black diamond he had traversed during his semiannual vacations in Aspen. After all, he reasoned, the shipping industry carried 98% of international trade and had been around for tens of thousands of years – it couldn't just disappear...*could it?*

No more than sixty minutes had passed before Robert Fairchild's Blackberry vibrated on his belt as he was sitting alone over his daily ration of spicy popcorn shrimp from the midtown outpost of Nobu. He normally would have screened the call, but he was intrigued by the exotic incoming telephone number starting with +30 944...

He slowly stepped out of the conference room and into the window lined hallway as he answered the phone and said hello. Watching the procession of vehicles inching their way up and down a rain-soaked Park Avenue, he listened carefully to the courtly cadence of a British accent overlaid on top of another mysterious foreign tongue.

"Hello, my friend," the man intoned ominously. Perhaps because the voice reminded him of Count Dracula, Robert was physically unable to respond. "They call me Spyrolaki and I am in the process of meeting investors to buy sheeps which have fallen in value by more than 50% in recent months." The caller was speaking slowly and carefully, as if to a young child.

"I'm sorry pal," Robert said dismissively, "but I don't invest in livestock, not anymore, not since I was long pork bellies when the Swine Flu hit a few years ago."

The caller emitted an impossibly slow laugh, almost a moan, before responding. "I am speaking of the vessels," he said in a

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voice that had the unmistakable patina that can only come from smoking cigarettes for a long period of time.

“Vessels? Wait a minute, do you mean *ships*?” Robert asked with sudden interest.

“Does this surprise you, my friend?”

“No, it doesn’t surprise me pal, but how did you get my *name*?” Robert asked suspiciously.

Robert Fairchild, who always tried to keep a low profile, was astonished that he was being solicited to make a shipping investment so soon after his chance encounter with the little known shipping industry. He had only stumbled on the BDI less than an hour beforehand and since that time he hadn’t spoken to another human being other than Katie, his personal assistant.

“Brilliant question, my friend,” the cold caller laughed without offering an answer. “If I told you that a Greek ship owner recently paid \$40 million for a brand new 6500 TEU container ship that had been ordered for over \$100 million at a Korean shipyard, would you be interested?”

“Well, let’s see, I don’t know what a TEU is,” Robert admitted as he watched traffic below, “but that does sound like a pretty attractive buy price. How’s the cash flow?” he asked.

“The cash flow?” the Greek laughed. “Listen to me my friend, and listen carefully; when it comes to buying ships the best deals have the worst cash flow.”

“What? But that makes no sense,” Robert said.

“Nevermind,” Spyrolaki said, knowing that the American would need to learn shipping’s most valuable lesson the hard way: *you generally don’t get a good price and good cash flow at the same time*. “My friend, it is a very good price,” the caller stressed before Robert heard him dramatically exhale what he

presumed were two lungs loaded with cigarette smoke. “And for your information, a TEU is the acronym for twenty-foot equivalent unit,” he added. “That is the unit measurement of the metal boxes that are loaded onto container vessels.”

Between the “BDI” and the “TEU”, Robert was quickly getting the impression there were going to be a lot of acronyms in his future.

“Oh,” Robert said, “You mean like the boxes I am afraid are going to kill me and my family when we drive on the Cross Bronx Expressway?”

“Bravo!” The Greek proclaimed. “These are the ones.”

“Did you just say *bravo*?” Robert inquired.

“Yes, bravo, you are correct, my friend. These boxes can also be loaded onto trucks and trains which is why they are called *intermodal*. And did you know that this type of transportation system was invented by an American truck driver named Mr. Malcolm McLean?”

“Smart guy; what’s the name of *his* company?” Robert quipped. “Is it publicly traded?”

Spyrolaki laughed again and then made a clicking sound with his tongue. “His company is bankrupt.”

“You mean to tell me that the guy who invented modern transportation went *bankrupt*?” Robert asked with disbelief. “That is just not fair.”

“There is no justice in shipping,” Spyrolaki said sadly and sighed. “There is only the market. If your timing is not correct, you will never make money even if you are very smart, which is why I am calling you.”

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Robert paused as he considered the Greek's last statement. "So why *are* you calling me?" Robert finally asked. "Is it because I am not smart or because I will lose money in shipping?"

"No," he said sternly. "I am calling you because everyone has a chance to be successful in the shipping business. It is like America in this way. Fifty ships are bought and sold each week and there is a shipping man on each side of the transaction that believes he is doing the right thing."

"Fifty ships are sold *every week*?" Robert asked, aroused by the amount of liquidity in the market for used vessels.

"Yes, and there are 50 winners and 50 losers. I want *you*, Robert Harrison Fairchild, to be a winner which I why I want you to invest your capital in my fund."

"Nice segue," Robert remarked. "And how do you know my middle name?"

"I do my research, my friend. You see the way the fund works is that we will co-invest with you and buy vessels at today's attractive prices. We are targeting the containership industry which is the most financially distressed today, but we will also buy tanker and dry cargo ships if we can find deals that meet our investment parameters."

"Wait a minute; did you just say *fund*?" Robert asked grimly.

"Correct. The fund will be registered in the Marshall Islands and comprised of..."

"Hold your horses..." Robert said, as if physically pulling back on the reins. "I can't invest in a fund, Spyrolaki," he said sadly, "which is too bad because I really do want to make a shipping investment."

"But *why* can you not invest in a fund?" Spyrolaki protested.

“Because *I* am a fund; my mandate is to make direct investments in operating companies. That’s what my investors pay me to do. If I just invest in another fund, they will wonder why they need me around. You don’t, by any chance, own a shipping company, do you Spyrolaki?” Robert asked hopefully.

“A shipping company? Just what do you mean by *that*?” he asked defensively.

“It’s not a trick question, pal. Do you have proprietary cargo? Do you have operations to run ships?”

“I have just one ship. I am just a small Greek shipowner looking for a way to grow. Besides, most ship owners do not need cargo because they simply provide their vessels into the market.”

“But if you are just putting your ship into the market, how can you possibly gain an advantage over your competitors?”

The Greek laughed. “There are only three ways to get an advantage over your competitors in this business.”

“What are they?” Robert asked.

“Pay less for your ships, pay less to operate them or pay less for your capital. In a commodity business like shipping, the only thing that really matters is price. Even the grain houses and oil companies will charter out the ships they own to other people if they think they can charter in ships cheaper from someone else.”

“Oh,” Robert sighed and decided to move on. “Well do you have incentive fees?” Robert asked, hoping he would hear another “No” and he could dress-up Spyrolaki as having a bona fide, albeit small, shipping company.

“Oh yes, my friend,” he said, his smoky voice lifting with optimism. “We have many fees. We have acquisition fees, we have chartering fees and we even have fees to oversee our own

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acquisitions and chartering. Not only that, we have six tiers of incentive fees and profit splits that are based on..."

"Then I *definitely* can't invest with you," Robert cut off Spyrolaki's rambling litany of fees.

"But why not?" Spyrolaki pleaded emotionally. "We *have* the fees."

"It's like I told you before; I cannot pay you management fees and incentive fees because I am already charging my investors management and incentive fees. Don't you get it, Spyrolaki? That's too many fees."

"This is nonsense my friend, a good shipping investment can *easily* carry the fees of two funds," the Greek countered. "In fact, a good shipping investment can support an entire island in the Mediterranean!"

"What about a bad shipping investment?" Robert asked dully.

"A bad shipping investment cannot carry the fees of even a single fund, so what difference does it really make how many fees there are?" Spyrolaki questioned. "The most important thing is to do good deals and doing good deals means buying cheap ships."

Robert paused as he considered Spyrolaki's analysis.

"Look, Spyrolaki, I am sure you are a great guy and very good at what you do, and I could definitely use your help, but this just isn't going to happen," the American said. "So you may as well find someone else to invest in your fund."

"But you *do* want to invest in shipping?" his suitor asked again. "Is that correct?"

"Oh yes," Robert confirmed, "definitely."

“Then we will find a way to make a shipping man out of you, Robert Fairchild,” Spyrolaki declared. “That is my promise to you, my friend.”

“A shipping man?” Robert asked with a wry smile on his face. He immediately liked the sound of it. “How can you be so sure?”

The Greek laughed knowingly. “Because when capital has the desire to go into the shipping industry it will always find a way.”