THE EDGE SINGAPORE
BUSINESS & INVESTMENT WEEKLY

HD **Corporate: Otto Marine repositioned as ship charterer amid rising demand and competition**

BY stories By Kang Wan Chern
WC 2,318 words
PD 21 April 2014
SN The Edge Singapore
SC EDGESI
LA English

LP

As the business of vessel building becomes more competitive and risky, Otto Marine has repositioned itself as a charterer of deepwater offshore support vessels (OSVs). “We are seeing an increase in demand for bigger OSVs as work moves deeper offshore. Since the 2009 crash, things have been very flat and everyone struggled. Now, the market is at the start of an upswing,” Garrick Stanley, CEO of Otto Marine, tells The Edge Singapore.

Otto Marine started out mainly as a builder of OSVs that specialised in complex, deepwater vessels such as anchor handling tug supply (AHTS) vessels, platform supply vessels (PSVs) and multi-purpose vessels (MPVs). It owns and operates one of the largest shipyards in Batam, Indonesia and has built and delivered more than 50 OSVs, mainly AHTS vessels between 5,000bhp and 21,000bhp in size, since listing in 2008. It also runs a smaller chartering business through joint ventures with other vessel operators in the industry.

TD

However, it is to this chartering arm that Otto Marine has been channelling more resources in recent years. In 2011, as new orders ground to a halt and existing ones faced the threat of cancellation, Otto Marine expanded its chartering business through the **acquisition** of a controlling **stake** in Go Marine Group, an experienced Australian OSV charterer. Immediately, the move gave it access to Go Marine’s OSV fleet and customer base in offshore hotspots such as the North Sea, Africa and the Gulf of Mexico. Today, Otto Marine operates a fleet of 64 owned and chartered-in OSVs between 3,600bhp and 24,000bhp in size and is now in the process of upgrading that fleet to target complex work in the world’s deepest waters.

“We are now building larger vessels so that we can upgrade and replace our existing fleet to become a full-fledged shipping **company** over the long term. We also plan to have more owned vessels in our fleet for better long-term returns and margins. We have repositioned our yard to mainly build larger vessels to replace the smaller vessels in our charter fleet, which will be sold off,” Stanley says. In January this year, Otto Marine sold seven small-sized OSVs for a total of US$10 **million** ($12.5 **million**) and has identified seven more vessels for **sale** this year. Meanwhile, the yard will continue to take on third-party repairs and fabrication jobs and build smaller vessels for customers in Indonesia and Malaysia.

On Feb 28, Otto Marine announced the completion of the Norshore Atlantic at its yard. Capable of performing complex offshore drilling work, well completion and intervention work and subsea construction work in ocean depths of up to 3,000m, the Norshore Atlantic is also the first vessel of its kind to be completed by an Asian yard. Indeed, the vessel has already been engaged for work in Asian waters and has been booked by an **oil** major for a period of three years after it completes its current contract.

“Over the long term, we are aiming to have a fleet of 50 to 60 vessels of 12,000bhp and above for AHTS vessels and a minimum of 5,000 tonnes for PSVs in our fleet to support subsea contractors like Subsea 7 and Technip as well as the **oil** majors,” says Stanley. “We want to compete in this deepwater segment of the market because we struggle to compete in the smaller vessel segment, where there is a lot of competition. We are in the large vessel market and want to compete alongside charterers like Swire Pacific Offshore and Tidewater. In addition, larger vessels fetch higher margins, which will improve our bottom lines.”

Tough competition

Still, Otto Marine is entering the chartering business at a time when competition is heating up. Already, half a dozen experienced OSV operators are listed on the Singapore Exchange and fighting for a slice of the charter market as well as funds from investors and banks. These include operators such as Pacific Radiance, which listed last November with a fleet of over 120 vessels, as well as experienced OSV charterers such as Ezra Holdings, Swiber Holdings and Mermaid Maritime.

Ezra, in particular, has had a tough time establishing itself in the deepwater subsea charter market after its **acquisition** of Aker Marine Contractors in 2011, and only recently managed to turn profitable in the subsea space. Another charterer — Jaya Holdings — was taken private by Australian offshore **company**Mermaid Marine Australia for $625 **million** in February.

This month, the local bourse will see the IPO of PACC Offshore Services Holdings (POSH), which could raise between $1 **billion** and $2 **billion**, reports say. POSH is the offshore and marine services arm of Malaysia's richest man Robert Kuok and operates a fleet of more than 50 OSVs that include 16,000bhp AHTS vessels; another 50 OSVs will be delivered over the coming three years.

Can Otto Marine find its feet amid the fierce rivalry? Stanley is not too worried. The way he sees it, to operate successfully in the offshore industry, charterers need to establish a track record for being able to meet the vessel requirements of **oil** majors and deliver the vessels on time. "A delayed AHTS can hold up a multi-**million**-dollar offshore operation, so we always make sure we deliver," he says. In addition, Otto Marine is also setting itself apart from its rivals with its move into the large OSV sector with AHTS vessels of up to 24,000bhp. In comparison, the other charterers mostly operate vessels of up to 16,000bhp. "We consider our competition to be the likes of Farstad Shipping in Norway, Swire in **Hong Kong** and Tidewater from the US."

Furthermore, Otto Marine can leverage on its building expertise. "We are building boats according to what the market needs and building them based on Norwegian-class standards and higher fuel efficiency. Vessel requirements are becoming more complicated, so you need to be able to build them at the right quality and price. [In that regard], we are leveraging on our knowledge as a shipyard to build for ourselves more efficiently. If you can build cheaper than your competitors, you can make more money and pay down more debt," he adds.

Rising demand

So far, Otto Marine's push into the chartering business appears to have made a good start. On March 19, it clinched a US$21 **million** charter contract for a multi-purpose offshore supply vessel for an unstated period in Australia and Vietnam. This came just a week after Otto Marine secured a charter contract worth US$24.9 **million** for three of its AHTS vessels. Two will be deployed on long-term charter contracts in Mexico while a third vessel was contracted for a short-term towage project from Singapore to West Africa.

In February, Otto Marine won contracts totalling almost U$60 **million** for the charter of three of its vessels, including its largest AHTS vessel — the 24,000bhp Go Pegasus — which will be deployed for work under a term contract in the North Sea. The contract also includes an option to extend the charter for an undisclosed period. Meanwhile, Otto Marine will also charter out a small-sized AHTS vessel under a long-term charter for work in Western Australia for US$11.3 **million**, while a third vessel — a 8,600 tonne PSV — will be deployed to support drilling work in Australia for a period of 152 days.

Indeed, there has been no shortage of demand for Otto Marine's fleet of OSVs, with utilisation levels at 90% and 75% for larger and smaller vessels respectively. "Everything is moving deeper offshore. The industry is now expecting some 134 new harsh-environment jack-ups to come onstream this year that will require double- or single-boat towage with more power. Bigger AHTS vessels are in demand, and that's the big shift for our **company**," says Stanley.

The tide looks to be turning for Otto Marine. For the 12 months to Dec 31, 2013, the **company** reported earnings of US$15.9 **million**, reversing the US$113.7 **million** in losses in FY2012. Revenue was 37% higher at US$512 **million**, owing to higher contributions from the vessel chartering business. It also managed to improve operating cash flows and lower its debt during the year. "We have spent the past few years cleaning up former chartering joint ventures that did not work out. We also have no intention of raising more cash through debt or **equity** because, by selling our smaller vessels, we can generate the **equity** needed to fund the building of our new vessels," says Stanley.

Still, shares in Otto Marine have fallen a long way from their peak in 2010, when they traded for as much as 47 cents each. Since then, Otto Marine shares have been on a downward spiral as the **company** struggled with order cancellations and failed investments. On April 16, shares in Otto Marine closed at eight cents apiece, down 16% since the start of the year. At current levels, the **company** has a market value of $330 **million**, and trades at 11 times price-to-earnings.

For his part, Stanley knows more work needs to be done to establish Otto Marine as a serious charterer and improve its earnings. “We need to produce results. The work we have done in the last few years to clean up our JVs and strengthen the balance sheet has put us in the position to expand in the right way. And, the volume of contracts coming in is quite strong. We see a better year for Otto Marine,” he says.

Weak quarter for offshore support services offsets gains in Ezra’s subsea business

Ezra Holdings’ big bet on growth in the deepwater subsea space is finally beginning to pay off — three years after its US$250 **million acquisition** of Aker Marine Contractors (AMC) in 2011.

From little exposure to subsea work just three years ago, the subsea business — which operates under the EMAS AMC brand — now represents about two-thirds of Ezra’s revenues and recently began turning in profits as the **company** gradually establishes itself in the global subsea space.

For the six months ended Feb 28, 2014, Ezra reported revenues amounting to US$525.8 **million** ($658 **million**), up 22% from a year ago. Earnings fell 25% to US$59.5 **million**, owing to higher-than-expected operational and maintenance costs in its offshore support services division — EMAS Marine — which operates a fleet of offshore support vessels (OSVs) in Asia-Pacific.

However, with the delivery of two new subsea pipelay construction vessels to its fleet during the period, Ezra was not only able to take on a higher volume of subsea work, but it was able to win more complex and higher-value contracts in the subsea space. While subsea revenues were down 16% y-o-y to US$190 **million**, EMAS AMC managed to improve its vessel utilisation despite the winter period.

Ezra’s managing director Lionel Lee expects demand in the global subsea sector to continue to rise as spending for the exploration and production of **oil** and gas continues. Subsea work involves laying and installing pipelines to transport **oil** and gas from offshore wells to floating production platforms or onshore refining facilities. Over the next four years, investments to set up proper offshore infrastructure by the **oil** and gas sector are expected to total some US$140 **billion**, while spending on exploration and production activities in the global deepwater and ultra-deepwater space is expected to exceed US$250 **billion** over the same period, according to professional reports.

That bodes well for EMAS AMC, which recently began turning in profits after several years of losses. More importantly, it has managed to amass a fleet of 11 highly sophisticated subsea vessels over the years, enabling it to bid for large-scale, higher-value subsea engineering work and further establish its track record as a global subsea engineer. Meanwhile, the group is also expecting to take delivery of its most advanced subsea construction vessel — the Lewek Constellation — next year. “We expect to see further earnings growth in 2014 and an increase in our profitability as we leverage economies of scale. The Lewek Constellation is a game-changing vessel and we believe it will further drive growth and profitability in future,” says Lee.

So far this year, Ezra has already secured more than US$300 **million** worth of subsea contracts, taking its total subsea order book to US$1.4 **billion**. This includes the latest contract inked on April 11, involving the installation of pipelines, umbilicals and ancillary equipment in water depths exceeding 2,000m for Noble **Energy**. The contract is estimated to be worth US$150 **million**, according to CIMB. The brokerage believes Ezra could win up to US$1.5 **billion** in subsea contracts in FY2014.

Still, CIMB advises investors to wait for things to turn around in its offshore support services business and for the subsea division to bring in bigger contracts. “The unexpected disappointment in the offshore division — supposedly Ezra’s core division — has hindered the group from delivering consistent quarterly earnings once again. We advise investors to wait until the dust has settled,” it writes in an April 12 report.

Shares in Ezra closed April 16 at $1.075 apiece, down from a high of $1.35 in January. At current levels, it has a market capitalisation of $1.05 **billion** and trades at 19.5 times earnings. Of the 13 analysts who cover the stock, only one has a “buy” call, seven have “hold” calls and five are recommending a “sell”. As a whole, the analysts have a consensus price target of $1.13, implying an upside of 5% for the stock.

CO oicpl : Otto Marine Limited

IN iship : Water Transport/Shipping | itsp : Transportation/Shipping

NS gtacc : Transport Accidents | gcat : Political/General News | gdis : Disasters/Accidents | gmmdis : Accidents/Man-made Disasters | grisk : Risk News

RE singp : Singapore | austr : Australia | apacz : Asia Pacific | asiaz : Asia | ausnz : Australia/Oceania | seasiaz : Southeast Asia

PUB The Edge Publishing Pte Ltd

AN Document EDGESI0020140423ea4l00009

