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Korea's Mega-Merger of Shipyards Set to Dominate Global Shipbuilding

Combined group would control 20% of the global market, and hold more than half the lucrative orders for liquefied natural gas carriers

A liquefied natural gas carrier at Daewoo Shipbuilding & Marine Engineering Co.'s shipyard in Geoje, South Korea, in 2016. Building ships to carry LNG can be more lucrative than building other kinds of big vessel. PHOTO: HANDOUT/REUTERS

By Costas Paris

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Shipyards in South Korea are trying to forge a new shape for the industrial sector that underpins global shipping.

The merger of Hyundai Heavy Industries Co. and Daewoo Shipbuilding & Marine Engineering Co. being engineered in Seoul promises to create a behemoth controlling 20% of the global market for new ships, and an even bigger share of the market for the liquefied natural gas carriers that are reconfiguring global energy markets.

The combination also would leave rival yards in China and Japan struggling to compete, raising questions about those countries' commitment to supporting their own ship builders.

Shipbuilding is a vital part of the economies of Asian countries such as South Korea and China, employing hundreds of thousands of people. Seoul and Beijing repeatedly bailed out or subsidized money-losing shipyards during a long slump in maritime trade as vessel operators trimmed their fleets and new orders plummeted.

But the industry is now regaining its bearings, boosted by big trends in energy markets and new regulations. Stricter marine pollution rules that take effect next year, as well as rising demand for advanced ships such as LNG carriers, have triggered a wave of new orders to replace aging fleets.

The merged Korean superyard may benefit the most. Between them, HHI and DSME have 52% of existing orders for LNG carriers, and they control a fifth of the broader ship building market, according to marine data provider VesselsValue.

The total combined Korean order-book now is worth $31.4 billion, compared with $15.2 billion for China's top two shipyards—China State Shipbuilding Corp. and China Shipbuilding Industry Corp.—which also plan to merge.

Japan's two biggest facilities, Imabari Shipbuilding Co. and Oshima Shipbuilding Co., are separate companies with a combined order-book of $12.6 billion.

"Our efforts over the past five years was to keep HHI and DSME from sinking," said a senior Korean official involved in the merger. "The target now is to create a yard facility that will dominate ship orders, especially high-margin vessels like LNG carriers, for years to come."

LNG ships cost on average $175 million apiece and the profit margin for the companies that build them is almost double that of other vessels, according to shipbuilding executives. Bulk carriers typically cost around $25 million each.

Korean yards are also the favorites to win one of the biggest ship orders ever—a deal for some 60 LNG carriers set to be signed by Qatar to ship gas from 2023. The order is estimated to be worth more than $10 billion, according to shipping services provider Clarkson PLC.

The new ships will roughly double Qatar's existing fleet, which was mostly built by Korean yards. Some of the ships will be used to move gas from the Golden Pass LNG facility in Sabine, Texas, which is 70% owned by Qatar Petroleum, 17.6% by Exxon Mobil and 12.4% by ConocoPhillips.

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"If you want LNG ships, you go to DSME or HHI," said a Greek shipowner whose company operates around two dozen such vessels. "LNG will become a pivotal fuel over the next decade and the Korean yards will be the biggest beneficiaries."

Rising demand from countries including Japan, China, Korea and India has tripled seaborne LNG cargoes since 2000 to 308 million metric tons last year, according to Bloomberg New Energy Finance. Capacity for another 170 million metric tons is due to be added by 2030, if planned projects go onstream.

Big shipowners like those in Greece are so confident of future demand that they are buying LNG carriers speculatively, rather than on the back of long-term contracts with energy majors as they usually would.

Ships sit under construction at DSME's Geoje shipyard this month. **PHOTO:** SEONGJOON CHO/BLOOMBERG NEWS

"You need at least four ships to have a critical mass, so it's a big gamble," said Basil Karatzas of New-York-based Karatzas Marine Advisors and Co. "Years ago the Greeks put their bets on crude tankers and it paid off. Now they are doing the same with LNG ships, and history shows that they are pretty good in reading the market."

The windfall for the merged HHI-DSME would be difficult for competitors to match. The $2 billion all-share deal, which is expected to be completed by the end of this year, comes with $2.25 billion in state liquidity support on top of a $2.6 billion bailout for DSME in 2017.

Chinese shipping officials hate the deal, but won't be able to stop it, shipping regulation experts say. Beijing will now be pressed to complete the approved merger between CSSC and CSIC, but it will likely take time to see it through. The two companies have complicated ownership structures, and pressure to preserve jobs as China's economy slows could make it harder for the combined company to cut costs.

"The shipbuilding consolidation is part of a wider plan to restructure strategic sectors like shipping, telecoms, airlines and energy," said a senior executive at a state-run Chinese shipping and logistics business. "We are inching ahead, but at a snail's pace."

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