LONG: GLOBAL SHIP LEASE, INC. (NYSE: GSL)

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INVESTMENT THESIS

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Global Ship Lease, Inc., a small-cap containership leasing company, has a strong and stable business with reliable revenues and cash flows. Due to its business model, it has experienced very little financial distress due to COVID-19, but its current share price reflects a general market depression that has as yet failed to fully recover. Comparable companies analysis finds GSL to be trading at attractive multiples relative to its peers and discounted cash flow analysis suggests that the intrinsic value of the company exceeds its current market valuation.

Recommendation: **Long** position on Global Ship Lease, Inc.

COMPANY OVERVIEW

COMPANY OVERVIEW | INTRODUCTION

- Global Ship Lease, Inc. (NYSE: GSL)
- Market Cap: $128.62mm
- Headquartered in London and incorporated in Mauritius
- Has traded on NYSE since 8-15-08
- Revenue is USD-denominated and financials reported in USD (shipping industry standard)
- Merged (stock-for-stock) in 2018 with Poseidon Containers
- Containership leasing company with 43 vessels

GLOBAL SHIP LEASE

COMPANY OVERVIEW | POSITION WITHIN INDUSTRY

- **Container shipping:** temperature-controlled containers of standardized size that can be transferred between ships, trains, trucks, etc., in contrast to "bulk" shipping, which ships loose materials (e.g. grain, coal, gravel, etc.) to be containerized at docking
- **"Panamax"** (along with "neo-Panamax"): a size classification that refers to ability to fit within the Panama Canal's lock systems
  - GSL leases primarily mid-size Post-Panamax and smaller ships
- **"Reefer" capacity**: refrigerated shipping capacity, a fast-growing segment that is particularly important for shipping of foodstuffs
  - GSL benefits competitively from its high-reefer ships

COMPANY OVERVIEW | POSITION WITHIN INDUSTRY *CONT.*

- **Real-time lease**: contracts wherein lessor (GSL) covers crew/operation costs while lessee (customer) covers fuel expenses and pays to lease boat. This is GSL's model, in contrast with:
  - Periodic tenancy: consistent renewal of agreement until ended by the tenant
  - Bare boat charters: leasing of the ship without crew or operations managers
- **Non-mainlane** and **intra-regional** trade routes, which represent over 70% of global container trade volume
- **TEU:** Twenty-foot Equivalent Units, a measure of a ship's capacity
  - GSL ships range from about 2000 to 12000 TEUs

COMPANY OVERVIEW | OWNERSHIP

- 42% ownership by Kelso & Company, a multi-sector $11.2b private equity firm
  - Invested in 2010
  - GSL is one of 17 current portfolio companies
- 10% ownership by board and management
- 10% ownership by CMA CGM S.A., a French containership company
  - 9.94% of Class A common shares representing 11.13% of voting rights
  - CMA CGM is also GSL's largest customer, constituting 52.40% of GSL's revenues in the trailing twelve months ending 6-30
  - This relationship guarantees a stable revenue stream – CMA CGM is incentivized to stay with GSL lest its investment lose value
- 38% public float, including small ownership stakes (< 7% each) by various other institutions

COMPANY OVERVIEW | GOVERNANCE

- Board of 8 directors
- None of the chief executives sits on the board of directors
- CEO (Ian J. Webber) and Chief Commercial Officer (Thomas A. Lister) have held their roles since August 2008
- Most board members and executives have extensive prior experience in shipping sector
- A handful of board members and executives joined after 2018 merger with Poseidon Containers
- Only one director (Michael S. Gross) serves on the board of any other company, suggesting significant management focus
  - As a curiosity: Gross is a co-founder and former president/CEO/chairman of Apollo Management and a Kellogg alumnus
- $3mm in stock-based compensation reported in LTM ending 2020 Q2

COMPANY OVERVIEW | CUSTOMERS AND REVENUE

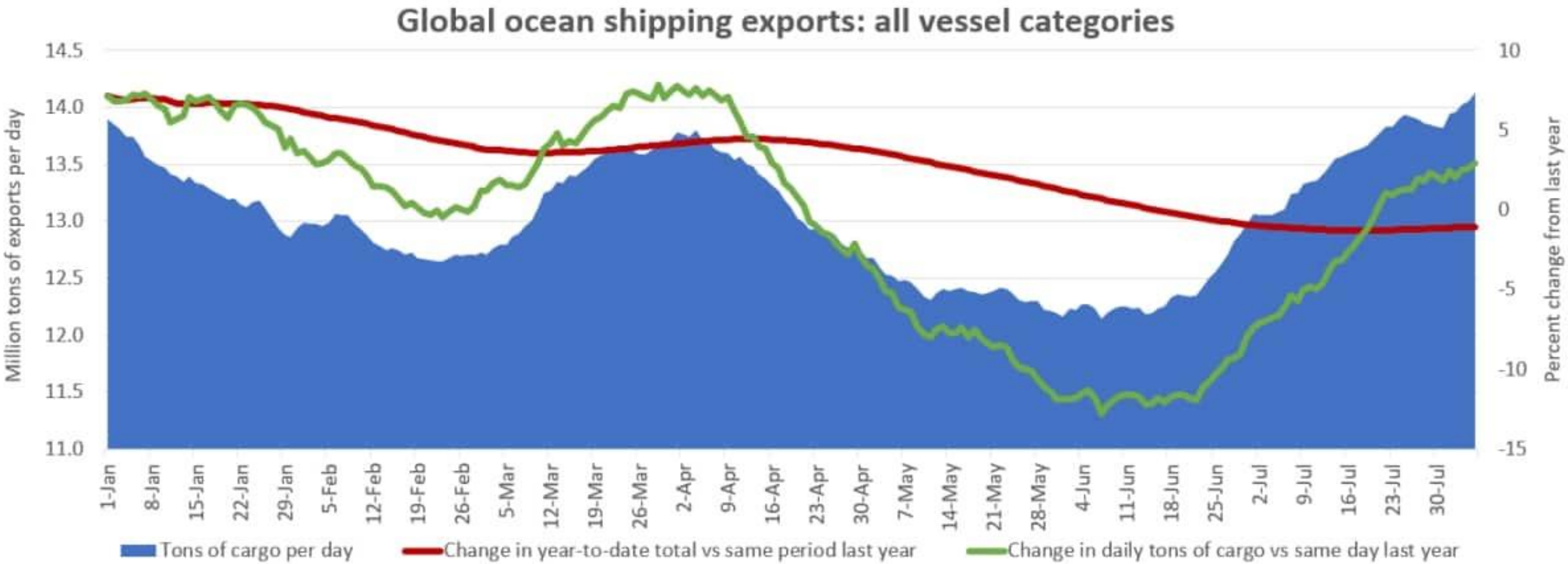
- Much of GSL's revenue is guaranteed by contracts that extend for several years into the future
  - Contract coverage as far into the future as end of 2023 (39% of annualized adj. EBITDA covered by contracts through 2023)
  - Many contracts come with option periods for future extensions
  - Contracted revenue of $659mm and 2.3 years TEU-weighted forward cover
- Many leases are signed at the time of purchase, which makes the investments in additional ships low-risk for GSL
- Signed or extended contracts for eleven ships in 2020 Q2
- Switching costs---easier for customers to renew contracts than find new lessors, negotiate new contracts, and get new boats
- Largest customer: CMA CGM S.A., accounting for15/43 ships and 52.40% of revenues (see previous slide)
  - Notice that more than half of revenues come from less than half of ships, suggesting GSL is able to negotiate attractive lease rates even with a major shareholder
- Other major customers: Maersk (7 ships) and MSC Industrial Direct (10 ships)
  - Many contracts confidential

COMPANY OVERVIEW | COMPETITORS

- Other major ship leasing companies include:
  - Hamburg Commercial Bank
  - Maersk
  - First Ship Lease Hoiding
  - Bank of Communications Financial Leasing
  - ICBC Leasing
  - Galbraith's
  - CCB Financial Leasing
  - Minsheng Financial Leasing
  - CMB Financial Leasing

- High barriers to entry: establishing a ship leasing company requires the purchase of several dozen containerships
  - Average price for a gearless 12000-TEU ship is over $100mm
- Stickiness of customer relationships: renewing contracts for the same ship is easier than contracting a new ship

INDUSTRY OVERVIEW

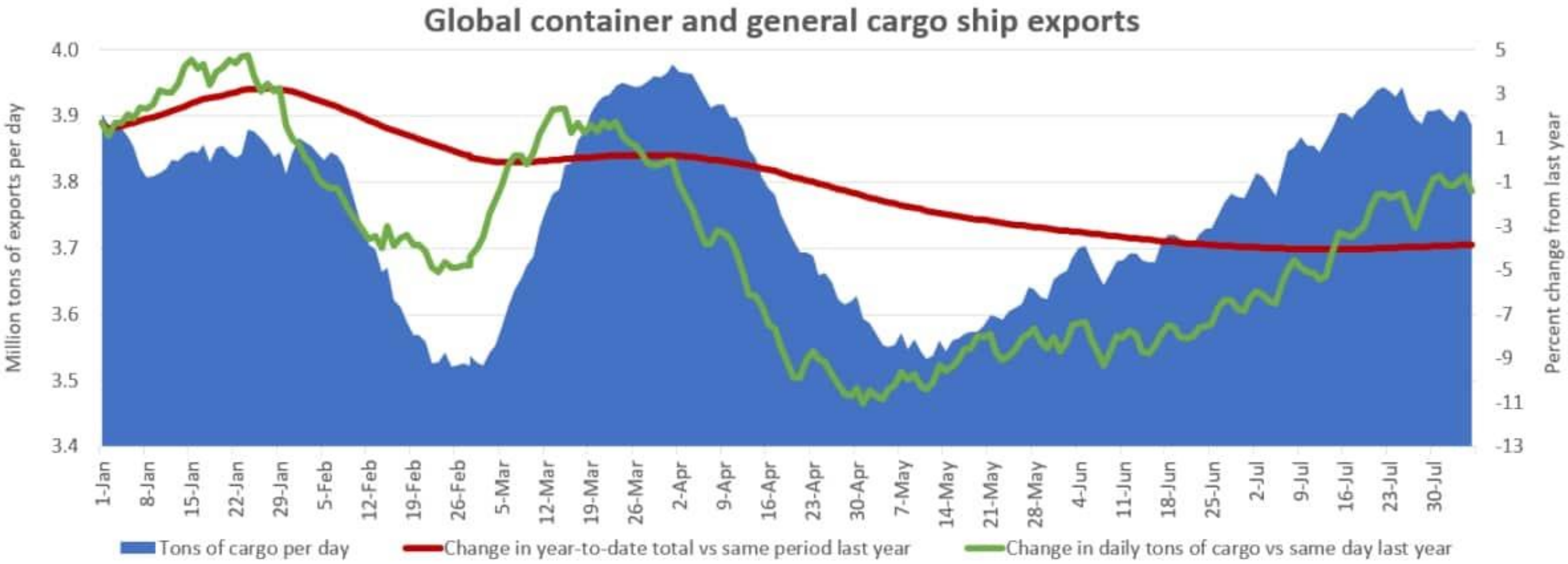


Daily volume estimates are 30-day averages. Data credit: Cerdeiro, Komaromi, Liu and Saeed (2020); AIS data collected by MarineTraffic. Year-on-year and YTD data calculated by FreightWaves based on data from Cerdeiro, Komaromi, Liu and Saeed (2020).

OCEAN SHIPPING VOLUMES

The graph demonstrates a general depression resulting from COVID-19 followed by a swift recovery.

The first "valley" represents a supply-side depression from the initial outbreak in Wuhan, while the second represents a demand-side shock from consumer lockdowns in the West.



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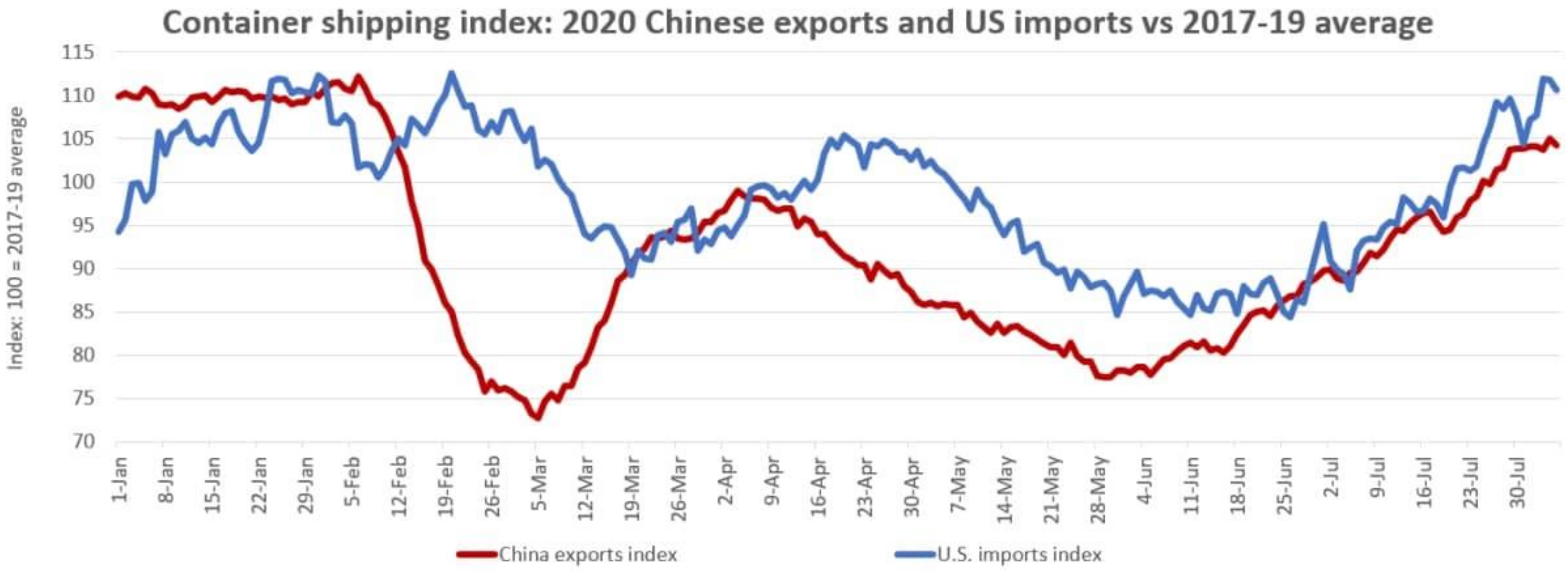
CONTAINER SHIPPING VOLUMES

The graph demonstrates a general depression resulting from COVID-19 followed by a swift recovery.

The first "valley" represents a supply-side depression from the initial outbreak in Wuhan, while the second represents a demand-side shock from consumer lockdowns in the West.



Daily volume indices adjusted for timing of Lunar New Year and based on 30-day averages. Data credit: Cerdeiro, Komaromi, Liu and Saeed (2020); AIS data collected by MarineTraffic.

EXPORTS AND IMPORTS VS. 2017-19 AVERAGE

100 = 2017-19 average

STOCK PERFORMANCE

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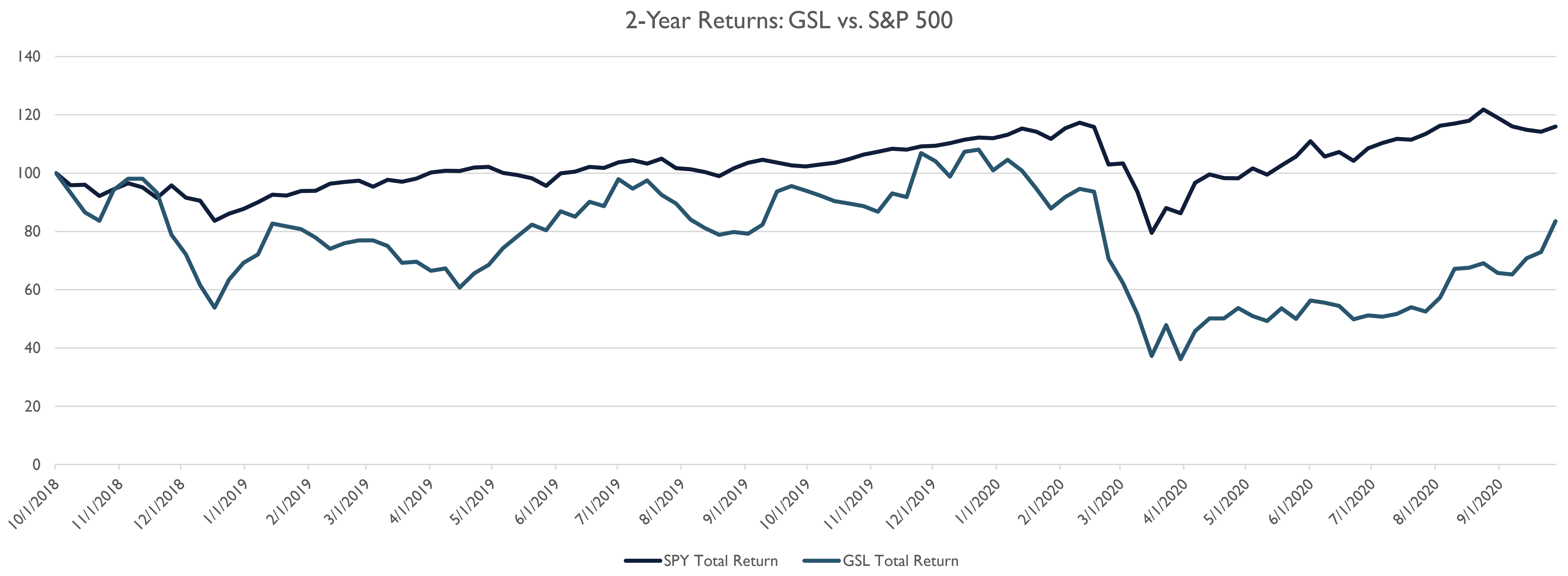
Current share price: $6.92 [10-6] | 52-week high: $9.25 | 52-week low: $2.61

Stock was discovered at $5.54 and bought at $5.60 (23.5% upside to date).

2 years of data were graphed, to remove share price response to 2018 Merger.



STOCK PERFORMANCE VS. S&P 500

GSL has underperformed the S&P 500, but a bull run is currently underway, demonstrating catalysts for growth to be realized.

2 years of data were graphed, to remove share price response to 2018 Merger.

VALUATION | COMPARABLE COMPANIES ANALYSIS

VALUATION | COMPARABLE COMPANIES ANALYSIS

- Universe of comparable companies: 20 marine shipping companies with market capitalizations below $300mm
  - Median and mean market caps of $71.7mm and $46.8mm, respectively
- Many peers did not report meaningful P/E multiples (suggesting negative net income)
  - This makes it even more of a positive sign that GSL does report positive net income, since many companies in the same industry fail to do so
  - GSL's P/E multiple was below the mean and the market-cap-weighted mean of its peers
- GSL had Price/Sales, Price/Book, Price/Cash, and Price/FCF multiples below both the median and the mean of its peers
  - P/S, P/B, and P/C multiples were also below the cap-weighted and trading-volume-weighted averages of its peers; P/FCF was below cap-weighted average but above volume-weighted average

VALUATION | COMPARABLE COMPANIES ANALYSIS *CONT.*

- GSL's 2019 and current EV/EBITDA multiple was below the mean 2019 and current EV/EBITDA multiples of its peers
- GSL had EPS growth this year of 120.8% and compounded EPS growth over the past 5 years of 15.4%
  - Peers on average showed declines in EPS this year and mixed EPS growth over the past 5 years
- GSL had compounded sales growth over the past 5 years of 13.50%
  - Peers had positive but more modest sales growth

VALUATION | DISCOUNTED CASH FLOW ANALYSIS

VALUATION | DCF | ASSUMPTIONS: TOP LEVEL

- Projected unlevered free cash flow because GSL is not a financial company
- Used historical period extending back five quarters ending Q2 2020
  - A historical period of several years would be poorly representative, as it would combine data from before and after the Poseidon merger
  - The Poseidon merger added economies of scale by doubling the size of the company, and significantly changed the composition of its management
- Used a five-year explicit projection period, as the company is not young

VALUATION | DCF | ASSUMPTIONS: REVENUE AND EXPENSES

- Revenue: Primary revenue driver is the size of GSL's fleet. Assumed a consistent proportion of revenue to book value of fleet based on average over historical period.
- COGS: Assumed consistent proportion of revenue based on historical period.
- Depreciation: Assumed a consistent ratio to the prior quarter's fleet size based on the most recent quarter (higher figure than average)
- SG&A: Consistent proportion of revenue
- EBITDA and EBIT calculated using the figures above
- GSL pays a very low tax rate and reported tax expenses every other quarter; a consistent average tax rate was assumed and applied to alternating quarters to find NOPAT
- Interest expense: assumed a consistent proportion of debt (see below for debt projections)

GLOBAL SHIP LEASE

VALUATION | DCF | ASSUMPTIONS: CAPITAL EXPENDITURES

- Assumed capital expenditures were in proportion to but greater than depreciation (otherwise, fleet book value would decrease with time), which is true in the historical period
- Assumed this proportion to linearly taper down to just over 1:1 over the course of the explicit projection period
- Found each quarter's fleet value by subtracting that quarter's depreciation and adding the previous quarter's capital expenditures

VALUATION | DCF | ASSUMPTIONS: COST OF EQUITY

- Unlevered beta was the more conservative (highest) of:
  - Median unlevered beta of 12 public peer companies (small-cap marine shipping companies) (0.49)
    - Assumed 20% tax rate for US companies and 1.0% tax rates for non-US companies
  - Damodaran's industry unlevered beta for the European shipbuilding & marine industry, with a sample size of 62 companies (0.90)
- Unlevered beta was re-levered at GSL's current capital structure (by book value)
- Equity risk premium was Damodaran's for the UK as of July 2020, based on an assumption of a base ERP for mature economies of 5.23%.
  - Used the most conservative of two methods to estimate country risk:
    - Default spread based on Moody's credit rating of country's 10-year government bonds
    - Default spread based on the current interest rates on credit default swaps (CDSs) on the country's 10-year government bonds, less the current interest rates on the corresponding US Treasury bond CDSs
  - Spreads were scaled up by factors of 1.25x and added to base ERP
- "Small-cap premium" of 4.0% was added to cost of equity

VALUATION | DCF | ASSUMPTIONS: COST OF DEBT & PREFERRED

- Cost of debt used was the more conservative of:
  - Interest expense over total debt (8.73%)
  - Interest rate on most recent debt issuance ($9.00mm Chailease facility, 2/26/20), LIBOR + 4.20%. Used 1-year average on 3-month LIBOR (1.07%) for cost of debt of 5.27%
- Cost of preferred: coupon rate on preferred (8.75%)
- WACC found using current capital structure (by book value)
- Model contains optionality to set "Zero" to 0 or -0.125 for mid-period or end-of-period discounting. End-of-period discounting is more conservative, so that was used for the final calculations.

VALUATION | DCF | ASSUMPTIONS: SHARE COUNT

- Began with most recent quarter's diluted weighted average shares outstanding (WASO)
  - Had seen 1.7% growth in share count over previous quarter---projected growth at this rate that linearly decreases to quarterly growth of 0% over the course of the projection period
  - BUT, in the interest of conservatism, did not use the proceeds from these sales of stock to supplant any projected debt issuances
  - Used share count at end of the projection period to calculate implied share price

VALUATION | DCF | ASSUMPTIONS: CAPITAL STRUCTURE

- Projected discretionary debt repayments (to revolvers) as a consistent proportion of (EBITDA less CapEx) based on most recent quarter
- GSL debt covenants require that it maintain a cash balance of at least $20mm, so no repayments were projected that would reduce its cash balance below this threshold
- Projected mandatory repayments based on the maturities of its notes outstanding (due 2022 and 2024)
- Projected issuances of debt based on needs for cash incurred by mandatory debt repayments
- Projected issuance/financing costs based on consistent (historical average) proportion of issuance costs to debt issuances
- Projected quarterly change in cash using CFFO, CapEx, preferred dividends, debt repayments & issuances, and common stock issuances, and used this change to project quarterly cash balance
  - Projected restricted cash based on historical proportion of restricted cash over total cash balance

GLOBAL SHIP LEASE

VALUATION | DCF | ASSUMPTIONS: TERMINAL VALUE

- Exit Multiple Method
  - Used first quartile (mre conservative than median) EV/EBITDA multiple of peer companies
  - Implied share price: $8.91
  - More conservative implied share price will be used for calculations of returns and investment horizon
- Gordon/Perpetuity Growth Method
  - Assumed a conservative terminal FCF growth rate of 1.0%
  - Implied share price: 11.96
- Subtracted net debt/preferred based on preferred, debt, and unrestricted cash in final quarter of projection period
- Median implied share price: 10.44

GLOBAL SHIP LEASE

VALUATION | DCF | RESULTS AND SENSITIZATION: EXIT MULTIPLE

		Exit Multiple								
		6.51	6.56	6.61	6.66	6.71	6.76	6.81	6.86	6.91
	12.10%	$ 9.02	$ 9.20	$ 9.38	$ 9.57	$ 9.75	$ 9.93	$ 10.12	$ 10.30	$ 10.49
	12.20%	$ 8.85	$ 9.03	$ 9.22	$ 9.40	$ 9.58	$ 9.76	$ 9.95	$ 10.13	$ 10.31
	12.30%	$ 8.69	$ 8.87	$ 9.05	$ 9.23	$ 9.41	$ 9.59	$ 9.77	$ 9.96	$ 10.14
	12.40%	$ 8.52	$ 8.70	$ 8.88	$ 9.06	$ 9.24	$ 9.42	$ 9.60	$ 9.78	$ 9.97
	12.50%	$ 8.36	$ 8.54	$ 8.72	$ 8.90	$ 9.08	$ 9.26	$ 9.43	$ 9.61	$ 9.79
WACC	12.60%	$ 8.20	$ 8.37	$ 8.55	$ 8.73	$ 8.91	$ 9.09	$ 9.27	$ 9.44	$ 9.62
	12.70%	$ 8.03	$ 8.21	$ 8.39	$ 8.57	$ 8.74	$ 8.92	$ 9.10	$ 9.27	$ 9.45
	12.80%	$ 7.87	$ 8.05	$ 8.22	$ 8.40	$ 8.58	$ 8.75	$ 8.93	$ 9.11	$ 9.28
	12.90%	$ 7.71	$ 7.89	$ 8.06	$ 8.24	$ 8.41	$ 8.59	$ 8.76	$ 8.94	$ 9.11
	13.00%	$ 7.55	$ 7.72	$ 7.90	$ 8.07	$ 8.25	$ 8.42	$ 8.60	$ 8.77	$ 8.95
	13.10%	$ 7.39	$ 7.56	$ 7.74	$ 7.91	$ 8.08	$ 8.26	$ 8.43	$ 8.60	$ 8.78

VALUATION | DCF | RESULTS AND SENSITIZATION: GORDON

		FCF Growth Rate								
		0.60%	0.70%	0.80%	0.90%	1.00%	1.10%	1.20%	1.30%	1.40%
	12.10%	$ 12.09	$ 12.35	$ 12.62	$ 12.90	$ 13.18	$ 13.46	$ 13.75	$ 14.05	$ 14.35
	12.20%	$ 11.86	$ 12.12	$ 12.38	$ 12.65	$ 12.93	$ 13.21	$ 13.49	$ 13.78	$ 14.08
	12.30%	$ 11.63	$ 11.88	$ 12.14	$ 12.41	$ 12.68	$ 12.95	$ 13.23	$ 13.52	$ 13.81
	12.40%	$ 11.40	$ 11.65	$ 11.91	$ 12.17	$ 12.44	$ 12.71	$ 12.98	$ 13.26	$ 13.55
	12.50%	$ 11.18	$ 11.43	$ 11.68	$ 11.94	$ 12.20	$ 12.46	$ 12.73	$ 13.01	$ 13.29
WACC	12.60%	$ 10.96	$ 11.20	$ 11.45	$ 11.71	$ 11.96	$ 12.22	$ 12.49	$ 12.76	$ 13.04
	12.70%	$ 10.74	$ 10.99	$ 11.23	$ 11.48	$ 11.73	$ 11.99	$ 12.25	$ 12.52	$ 12.79
	12.80%	$ 10.53	$ 10.77	$ 11.01	$ 11.26	$ 11.51	$ 11.76	$ 12.02	$ 12.28	$ 12.55
	12.90%	$ 10.33	$ 10.56	$ 10.80	$ 11.04	$ 11.28	$ 11.53	$ 11.79	$ 12.04	$ 12.31
	13.00%	$ 10.12	$ 10.35	$ 10.58	$ 10.82	$ 11.06	$ 11.31	$ 11.56	$ 11.81	$ 12.07
	13.10%	$ 9.92	$ 10.15	$ 10.38	$ 10.61	$ 10.85	$ 11.09	$ 11.33	$ 11.58	$ 11.84

INVESTMENT HORIZON

- GSL has closed at higher values for each of the past four weeks, suggesting a bull run in progress
- To find the investment horizon, I took the correlation coefficient (for daily increase in share price) over the past four weeks and assumed the share price would increase linearly at this rate until GSL reached its target price (see below)
  - Daily increase: $0.067, implying 28.9 days or 0.96 months to reach target price
- To be more conservative, I used the same method but with the slope over the past three months
  - Daily increase: $0.027, implying 73.7 days or 2.5 months to reach target price
- To be even more conservative, I used the same method with the slope since GSL's minimum in mid-March
  - Daily increase: $0.012, implying 153.0 days or 5.1 months to reach target price

GLOBAL SHIP LEASE

RISKS AND MITIGATION

- Loss of CMA CGM or other customers
  - Many CMA CGM contracts are in place until 2024 or 2025
  - CMA CGM's shares of GSL incentivize it to stay with GSL to preserve the value of their investment
  - GSL signed or extended charters for eleven ships in 2020 Q2, suggesting a customer base resilient to general economic distress
  - Switching-costs and strong customer relationships make existing customer base "sticky"
- Increase in prices of ships
  - Would result in industry standard of higher lease rates, especially since many leases are signed at the time of purchase
  - Temporary increases wouldn't be significant---GSL's existing boats have long useful lives and has a significant enough fleet to not need purchases in every quarter

RISKS AND MITIGATION *CONT.*

- Sale of two ships by GSL in 2020 Q2 could reduce future revenues
  - Priced into DCF---revenues are a function of fleet size
  - Ships were built in 1999---much older than the rest of GSL's fleet, suggesting lower rates
  - Ships were sold above book value and cash can be used to purchase additional ships
- High leverage
  - Priced into DCF---interest payments accounted for when finding cash balances and debt projected to find implied equity value

HEDGING OPTIONALITY

Various options exist to hedge this position:

- Short positions or put options on GSL's largest publicly-traded customers, Maersk (OTCMKTS: AMKBY) and MSC Industrial Direct (NYSE: MSM)
  - MSC is optionable and shortable; as Maersk trades over-the-counter (OTC), it is not clear whether it is shortable or optionable
- Long positions on containership manufacturers, to hedge the risk of sharp increases in the prices of ships
- To hedge industry risk, there are no ETFs that track containerized shipping, only bulk shipping or general transportation, so short positions or put options on these would be possible but imperfect hedges. Small short positions or put options on a large number of containerized marine shipping and/or leasing companies could accomplish this same goal, though this would warrant more diligence since it incurs a greater amount of risk associated with the specificities of each company.
- LIBOR floating-rate debt or interest rate derivatives that bet on an increase in the LIBOR, to hedge the risk in GSL's floating-rate LIBOR-plus debt
- GSL is not optionable, so options hedging strategies with GSL as the underlying security may not be feasible.

RECOMMENDATION AND IMPLIED RETURNS

Recommendation: Long position on Global Ship Lease, Inc. (NYSE: GSL)

Current price: $6.92

Target price: $8.91

Investment horizon: 5.1 months

Implied return: 28.75%

Annualized return: 81.23%

GLOBAL SHIP LEASE

FURTHER RESEARCH

- Model individual debt facilities
  - Difficult since GSL has debt in varying amounts with sixteen different creditors
  - Future revolver drawdowns or other issuances would be difficult to forecast with the same degree of precision
- Model revenue by individual ships
  - GSL has 43 ships at present, so this would involve a great degree of granularity
  - Predicting future ships would be difficult
- Examine turnover time between contracts per ship and look for patterns across different variables (size, age, etc.)

GLOBAL SHIP LEASE

OPEN TO QUESTIONS AND COMMENTS