INITIAL PUBLIC OFFERS' IMPORTANCE IN FINANCING SHIPPING COMPANIES. CASA STUDY ON SCORPIO TANKERS INC

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ABSTRACT

In the shipping industry there is a dynamic business environment which determines shipping companies to get some other financial resources in order to maintain and develop on this market. Through this paper we want to establish the important role of the initial public offers on the stock market, from the different geographically regions; the probability that these offers might determine the success or failure of a company and the way of this financing process could be made by a company which needs resources for development and surviving on such unstable market, as the maritime market is. In order to show how the initial public offers work on the stock market we took an example of a maritime company, Scorpio Tankers Inc., whose shares are listed on New York Stock Exchange, from 2010.

Keywords: *Public offer, shares, transaction, underwriting spread, New York Stock Exchange.*

1. INTRODUCTION

Financing shipping companies has greatly expanded during the last years, moving from financing companies by dividing the value of the ship in 64 equal parts (each investor being able to buy parts of the ship), to finance through charter contracts (used as guarantees, especially time charter contracts), mortgaging ships, using credit (this is one of the most used methods of financing used in the last 30 years, especially because of the possibility of keeping the company's control, credits which can come either from commercial banks or from shipyards), through leasing (in maritime transport we have to do with financial leasing, due to the tax advantages offered so as accelerated depreciation) or attracting important investors, and in this case we refer manly at shipowners resources, different ways of association (the most significant being the Norwegian Association- K/S Companies), naval investment funds or public offers on stock exchange from different parts of the world.

As the business environment changes dynamically in the shipping industry, shipping companies turn to new financial instruments and markets to finance their investment plans. Shipping companies must develop strategies and procedural structures appropriate for companies able to participate on the capital markets (Figure 1).

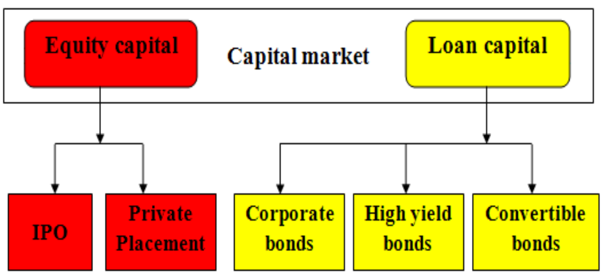

Figure 1 Financing source on the capital market
Sources: www.kpmg.com

2. GENERAL DISCRIPTION

Although financing companies through equity ownership might be the most profitable financing way, due to the capital intensive nature of shipping business, these could determine the low payment or no dividend to investors, who have to accept this reality because most of the times the retained earnings are channelled on fleet replacement and expansion.

An important problem for shipping companies interested in raising equity in the stock market is the pricing of the new issues. In is known that the majority of shipping IPOs refer to bulk shipping offerings, so it is expected that the issuer will set an IPO price at or near market-adjusted net asset value per share. This is reasonable in cases where company earnings and cash flows fully support net asset value (Stokes, 1997). In practice, however, ship prices in the second-hand market do not necessarily reflect operating cash flow and earnings generated by the ships. More frequently, ship prices represent a very high multiple of operating cash flow, whereas in certain bulk shipping segments operating earnings have been negative for a number of years. (Syriopoulos, 2007)

Shipping companies may obtain important financial resources within the public offers on the stock market from different parts of the world. In the maritime transportation's domain, shipping stocks are usually list in: New York, Oslo, Hong-Kong, Singapore or Stockholm (the US stock markets, NYSE and NASDAQ are on the first place in attracting most shipping IPOs, followed by Oslo; London loosed first place, which it has been gained during the last years).

Figure 2 shows the distribution of IPOs over the sectors of the economy.

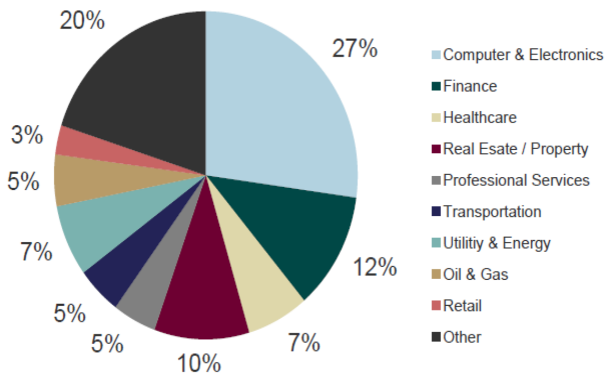

Figure 2 IPOs By Industry
Sources: www.marinemoney.com

A public offer is a type of public offering in which the stock or bonds of a company are sold to the public. Through this process, a private company becomes a public one. Initial public offerings are used by companies to expand their capital and to become tradable companies. A company that sells shares is never required to repay capital to public investors. After the initial public offer, when shares are freely traded on the open market, the money is divided between public investors.

A company can consider an IPO as an alternative only if it is a leading player in the growing and profitable segments of the market, driven by motivation of the personnel and commitment of the key managers to the success of the business (human factor is very important) or it is demonstrating sustainable growth rates and capability to win in a competitive environment.

There are many factors that influence the success of an initial public offering, both in terms of controlling a shipping company within and outside it. Those factors can include:
- overall public capital markets;
- investor perception about the shipping company and about the segment of which it forms part;
- the results of the company;
- experience, quality and commitment of the company's management and Board of Directors.

Shipping IPOs are distinct from those of ordinary industrial or service companies. The market value of a shipping company is often closely associated to the underlying value of the physical assets (vessels). In this respect, shipping IPOs bear similarities with the respective IPOs of closed end funds and property companies. Furthermore, due to extensive information flows in international vessel sales and purchase markets, shipping IPOs tend to exhibit lower information asymmetry. Figure 2 shows transportation IPOs, from which one can easily see that the maritime transport has a large share compared to road transport.

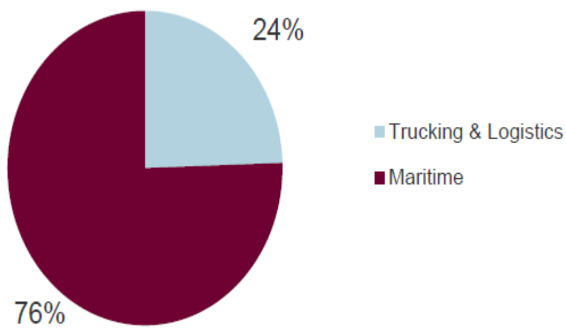

Figure 3 Transportation IPOs
Sources: www.marinemoney.com

On IPO stock market performance, the following important factors were considered: size of the company, gross proceeds of the IPO issue, proportion of equity offered, gearing level, age of the company and age of the fleet.

3. ADVANTAGES AND DISADVANTAGES

It is true that going public in shipping and not only, is not always an attractive alternative for many companies, this source of financing brings with it many advantages such as:
1. The company will raise a large amount of cash, that can be used for its expansion plans, its growth, its competitiveness or establish an improved financial structure, but also for further research and development or to expand its products and services.
2. After becoming public the company will have access to the public capital markets, which generally enables it to raise money more quickly with less cost and more flexibility than in the private markets
3. The company will receive worldwide media coverage through the financial markets. Listed companies are thought of as financially healthy and having high standards of transparency and information disclosure; it increases the company’s credibility and it will reflect positively on is services and products.
4. Becoming public, brings benefits for current employees, who can see the results of their efforts in the share price more immediately. It is sure that allowing employees to benefit alongside the company’s financial success will increase productivity and loyalty to the company, which will attract for sure top talent.

Becoming a public company has significant disadvantages as well, some of which include:
1. An IPO is a costly undertaking. Public offerings involve many costs like investment bankers' commissions, lawyers and accountants’ fees, ancillary costs, such as public relations, printing, corporate advertising and others, including the costs of maintaining a quote on the stock exchange (stock exchange fees, management time, more extensive audits and reporting, etc.).

2. In order to become public a company needs to disclose information on a regular basis so that investors and potential investors can make buy, sell or hold decisions. This costs money and discloses information to competitors.
3. After becoming public the outsiders often could take control and even fire the entrepreneur which will lead to a big loss of control.
4. The IPO entrepreneurs are allowed to cash out only many months after the initial public offer, due to various restrictions.

4. CASE STUDY

Going over the past we will find an eloquent example which will show the benefits of an IPO. In 1993, Bona Shipholding Ltd, issued on 17 December 1993 on the Oslo Stock Exchange a prospectus offering 11 million shares at 9$ per share. It is known that the price is determined by market supply and demand, so by 1996 the Stock in Bona Shipholding Ltd was trading at 11.79 $, allowing investors willing to sell to get a profit of 2.79 $ per share.

In order to show how this work we took an example of a maritime company, Scorpio Tankers Inc., whose shares are listed on New York Stock Exchange, from 2010 under the symbol "STING".

Scorpio Tankers Inc. is an important company which provide seaborne transportation of refined petroleum products and crude oil worldwide. In October 2009 they began their operations with only three vessels and operating subsidiary companies. Scorpio Tankers Inc. is incorporated in the Republic of The Marshall Islands and has principal executive offices in Monaco and New York. In April 2010, they completed their initial public offering of 12,500,000 shares of common stock at a public offering price of $13.00 per share. Since then they expanded their fleet and in 2013 their fleet consists of 14 wholly owned tankers (one LR2 tanker, four LR1 tankers, one Handymax tanker, seven MR tankers, and one post-Panamax tanker), with a weighted average age of approximately 4.4 years and they have also contracts for the construction of 33 additional new building vessels. It is important to notice that since their initial public offering closed on April 6, 2010, they haven’t paid a dividend.

At December 31, 2010, they had 24,634,913 registered shares authorized and issued with a par value of $0.01 per share. These shares provide the holders with rights to dividends and voting rights. Due to their annual report presented on New York Stock Exchange, we can notice how many shares were sold and at what price:

- In May 2011, they closed on a follow-on public offering of 6,000,000 shares of common stock at $10.50 per share.
- In December 2011, they closed on the sale 7,000,000 shares of common stock in an underwritten public offering at an offering price of $5.50 per share.
- In April 2012, they closed on the sale of 4,000,000 shares common stock in a registered direct placement of common shares at an offering price of $6.75 per share.
- In December 2012, they closed on the sale of 21,639,774 shares of common stock in a registered direct placement of common shares at an offering price of $6.10 per share.
- In February 2013, they closed on the sale 30,672,000 shares of common stock in a registered direct placement of common shares at an offering price of $7.50 per share.
- In March 2013, they closed on the sale 29,012,000 shares of common stock in a registered direct placement of common shares at an offering price of $8.10 per share.

In the table below we can see the highest and lowest market price for their shares of common stock on the New York Stock Exchange.

Table 1. The highest and lowest market price for Scorpio Tankers Inc. shares of common stock

For the year ended	High	Low
December 31, 2010	$13.01	$ 9.50
December 31, 2011	$12.18	$ 4.28
December 31, 2012	$ 7.50	$ 4.93

Sources: www.nasdaq.com

As you can see since their initial public offering in April 2010, when the price per share was of $13.00, they have never had a price bigger that, so we can say that their “paper” profit was not big, but we can also see the big number of shares that were sold, which brought millions of dollars to the company. It is true that they also used other financing sources, but considering the economic crisis and its impacts regarding the maritime and port sector, we can easily say that for Scorpio Tankers Inc. becoming public was a good choice.

The market price has fluctuated widely since Scorpio Tankers Inc. become public as a result of many factors, including the prospects of their competition and of the shipping industry in general and in particular the tankers sector, differences between their actual financial and operating results and those expected by investors and analysts, changes in analysts' recommendations or projections, changes in general valuations for companies in the shipping industry, changes in general economic or market conditions and broad market fluctuations.

5. CONCLUSIONS

The financing process within public offers lead to important capital resources, but it can also be not the best source of capital resources.

The listing also open many financial doors such us:

- Due to the financial controlling process, public companies could obtain better prices when they have debt.
- As there is an important demand on the market, a public company could always obtain much more financial resources which allows mergers and purchases, the resources are translate as a part of the negotiation process.
- Agreements on the open market stocks within liquidities.

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