

## No bridge yet for the funding gap

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- by [Steve Matthews](#)

The difference between what owners want to borrow and what they can remain unresolved

MOST of the recent attention on bank lending to shipping has been on the question of whether banks will pull the plug on non-performing shipping loans if efforts to restructure them are unsuccessful.

But the fact remains that whatever the fate of existing loans, most banks are likely to remain extremely restrictive in the amounts they lend to shipping, the deals they fund and their terms for doing so.

This means there is still a sizeable gap between the perceived requirement for new shipping finance by owners for newbuildings and secondhand acquisitions, which are picking up, and other corporate needs.

Even though some shipping banks have indicated they are prepared to agree new lending for suitable deals, there is little sign of any significant increase in overall lending capacity for shipping.

There is still some debate about how big this funding gap is, with estimates ranging from \$50m to \$200m. The biggest single component of the outstanding funding requirement is still the newbuilding orderbook, but the gap depends on what assumptions are made and, crucially, the estimated number of cancellations and how the orderbook is valued.

The latter varies according to the values assigned to newbuildings. Ship values and newbuilding prices appear to have reached a relatively stable level, but should newbuilding finance requirements be set according to the prevailing value believed to be contracted?

With so many orders being renegotiated, even if not cancelled, it is difficult to make an accurate calculation.

Recent reports suggest likely outright cancellations have been overstated and that even where owners have cancelled orders, the ships will be discounted prices.

The current best estimate for the value of the orderbook is about \$400m. This happens to be about the same size as the current aggregate capacity.

At the end of 2009 Petrofin Bank Research managing director Ted Petropoulos suggested cancellations and delays could reduce the total net requirement by 25%, although the latest estimates put the proportion at rather less than that. It can be further reduced by downward revaluations and reductions by banks.

Assuming about half the outstanding total is still to be funded, the total figure is reduced to about \$100m. Additional funding for secondhand requirements must be added. This increases the overall net requirement currently to somewhere in excess of \$150m to be raised in the next three years.

A large proportion of this can be met by run-offs of existing loans, still leaving a net additional lending requirement to be found in other circumstances.

But in the current situation facing banks even a conservative estimate of about \$50bn in extra net lending in the next three years could prove difficult.

Most leading shipping banks in Germany that are heavily committed to the struggling containership sector are not in a position to increase lending. New portfolios will contract.

The expected bank restructuring in Germany of a country that was the leading source of bank lending for shipping is likely to mean bank financing will be reduced.

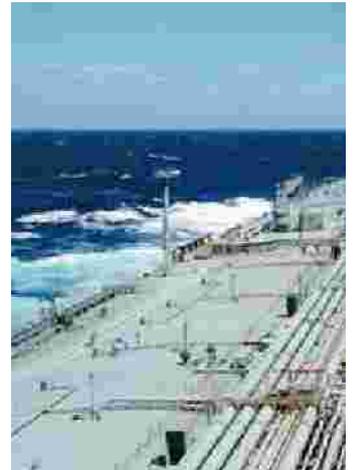
Most other shipping banks have indicated their portfolios will remain approximately at current levels, with lending capacity limited to replacing cancelled loans. Shipping banks say they are in a position to increase their loan books modestly this year.

Efforts by some funds to acquire shipping loan books from banks that are looking to use proceeds of sales to strengthen their capital base could be successful.

While banks' shipping departments are naturally resistant to such approaches, senior management may not be so committed to shipping at the moment and restructuring is taking a major effort.

Lloyd's List understands that several shipping banks have been approached by other parties, including funds and other banks, offering to take their hands. So far, most banks have been reluctant to sell shipping assets or loanbooks, but some deals could be done.

If shipping loan portfolios are not attractive for the banks, why should anyone else want to take them on? Most banks' shipping portfolios are not very attractive. Many loans are performing or near maturity. Others can be turned around through restructuring, while a few will have to be written off.



No bridge yet

Depending on the structure of individual portfolios, the prospects of making acceptable returns on reduced value assets may seem a distant one. Some loans are costing banks more to maintain than they are earning, because they were negotiated at low spreads, while the cost of finance

Banks that are willing to offload their shipping portfolios could be tempted to do so at a discount and use the proceeds for more profitable purposes.

Most banks are still seeking to boost their capital bases and reduce their exposure to risk. Those that have received state support are anxious to have funds available, banks are unlikely to increase lending to shipping until restructuring of existing non-performing loans has been complete and the valuation of the assets they are being asked to finance is satisfactory.

Dagfinn Lunde, head of ship finance at DVB Bank, which, as a dedicated transport finance bank, was untainted by the banking crisis, said he expects this year to be similar to 2009, but overall there was no sign of lending capacity coming back into the shipping market.

There is, therefore, little or no prospect of any overall increase in bank lending capacity to shipping at least this year and it will probably be some time before this situation changes, depending on wider economic and financial circumstances.

Even then banks are likely to remain cautious, while spreads and lending terms will not return to the liberal approach before the financial crisis. Spreads down to what were widely regarded as unsustainable levels.

This means that even if the loan finance gap is smaller than some estimates, the gap is still there and needs to be bridged somehow.

Some Asian banks, especially Chinese and export import banks, are providing some additional funding, especially to domestic shipbuilding in the Middle East, are also providing new funding to domestic and regional shipping companies.

Other sources of funding that are being tapped by shipowners in an attempt to fill the void include private equity funds, although the former market is in effect closed.

A number of funds have been created to seek out distressed ship sales, but there has been little business concluded so far. Banks have been reluctant to buy at prices as they would take a financial hit, but that could change.

There has also been an increase in capital market activity with a number of bond issues, while the public equity market is stirring, with several secondary issues under way or planned.

However, not all owners are able to use these alternative funding sources, as they often depend on favourable ratings. Moreover, while a few billion dollars in interest, even in aggregate they amount to only a few billion dollars and can make little impression on the overall finance gap for shipping.

How to fill this gap, whatever its size, in the next two to three years remains a vexing issue with no obvious answers, although the search goes on for innovative individual solutions.

One response is that the apparently insurmountable gap will be a good discipline for shipping, preventing a resurgence of overordering as markets improve and to secure finance for ship acquisitions at viable terms if they have a strong deal backed with firm employment and revenue streams, or if they are putting up a large ratio of equity finance. The gap would therefore gradually wither away naturally.

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