Key Developments and Growth in Global Ship-Finance

September 2018

By Ted Petropoulos, Head, Petrofin Research ©.

We are pleased to present our Global ship finance research.

The bank loan portfolios to Global shipping presented here are as of 31st December 2017.

Petrofin Research © wish to thank all participating banks for their on-going support, without which, this research would not have been possible.

We also include the Petrofin Global Index, which monitors the global bank ship finance positions since 2008.

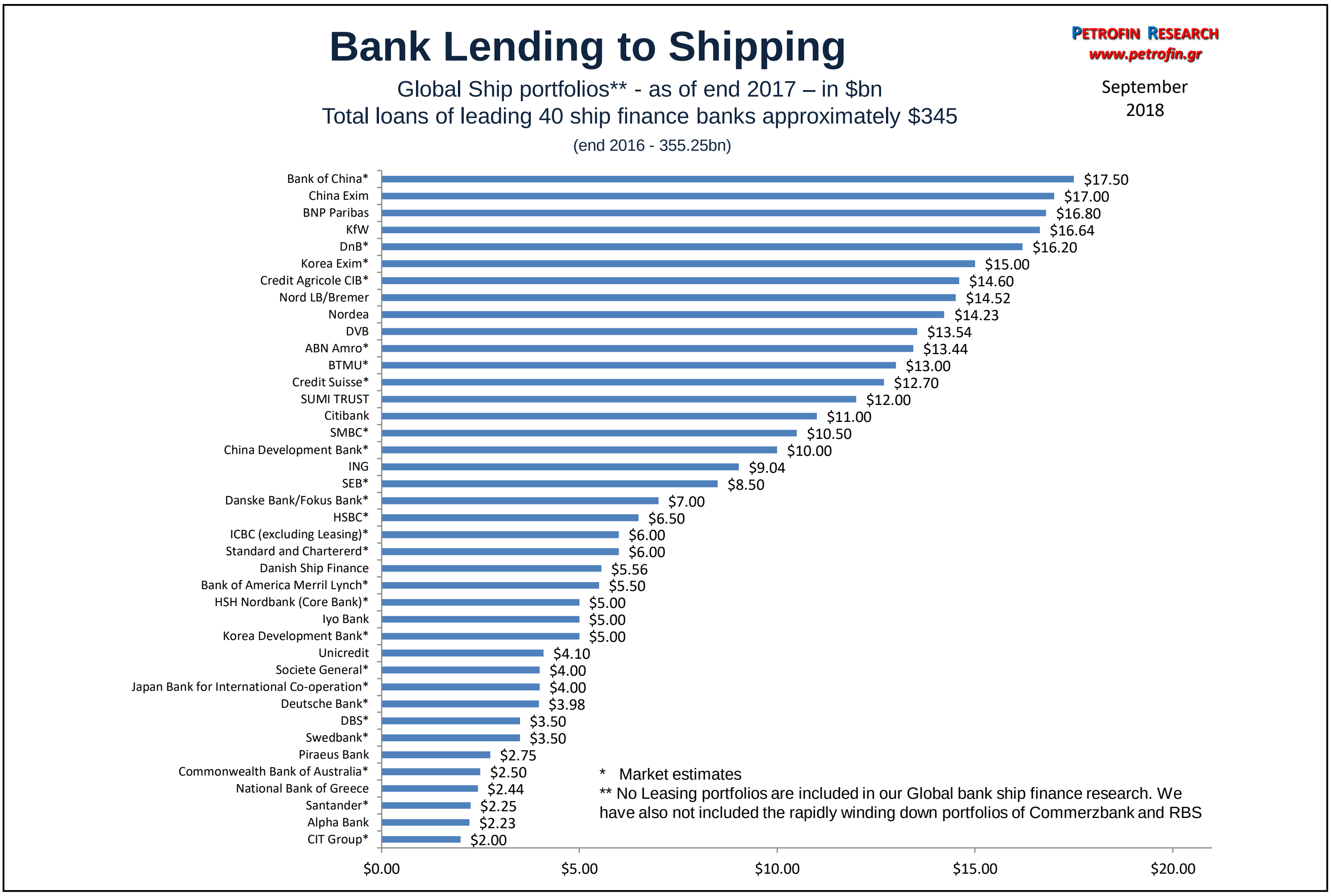
Contents

1.	**Top 40 banks**	**p. 2**
2.	**Petrofin Global Index ©**	**p. 4**
3.	**Nationality and commitment of banks**	**p. 6**
4.	**The outlook for 2019 and beyond**	**p. 9**

1. Top 40 Banks

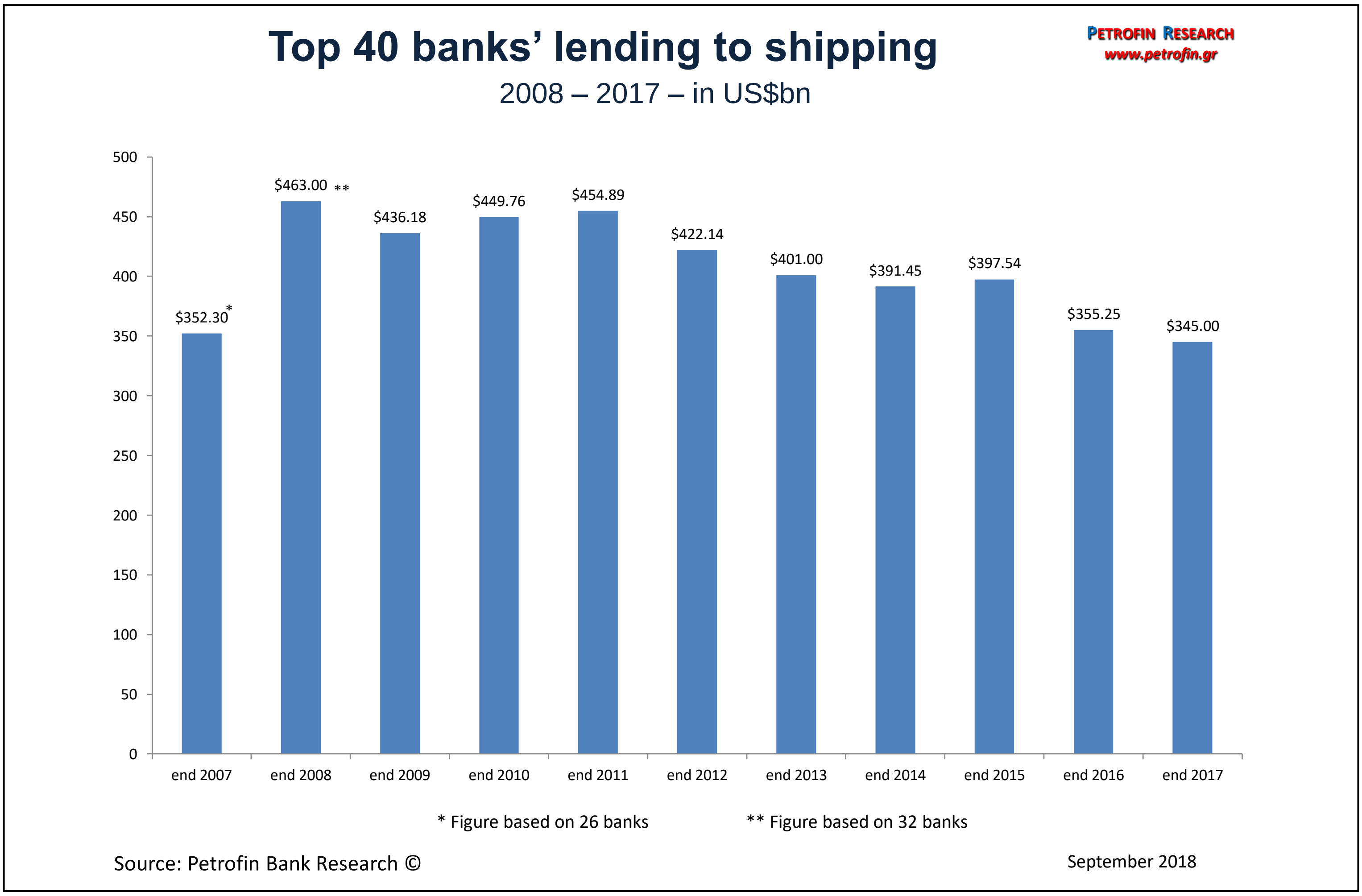
We are pleased to present the latest Top 40 Global banks' lending as of December 2017, amounting to $345bn (see Graph 1).

Graph 1: The Top 40 banks have a total of $345bn exposure to shipping.



Another $10bn has been knocked off the portfolios of the top 40 banks over the last year. Bearing in mind the previous year's reduction of 42.5bn, it would appear that the rate of decline is slowing down. It is yet early days to conclude if banks will continue reducing their exposure in the sector and a great deal will depend on the overall available lending resources of banks and their commercial strategy. Also, for the first time, 2 Chinese banks top the market underlying the fundamental geographical shift taking place.

Graph 2: Top 40 banks lending to shipping from end 2007 till end 2017

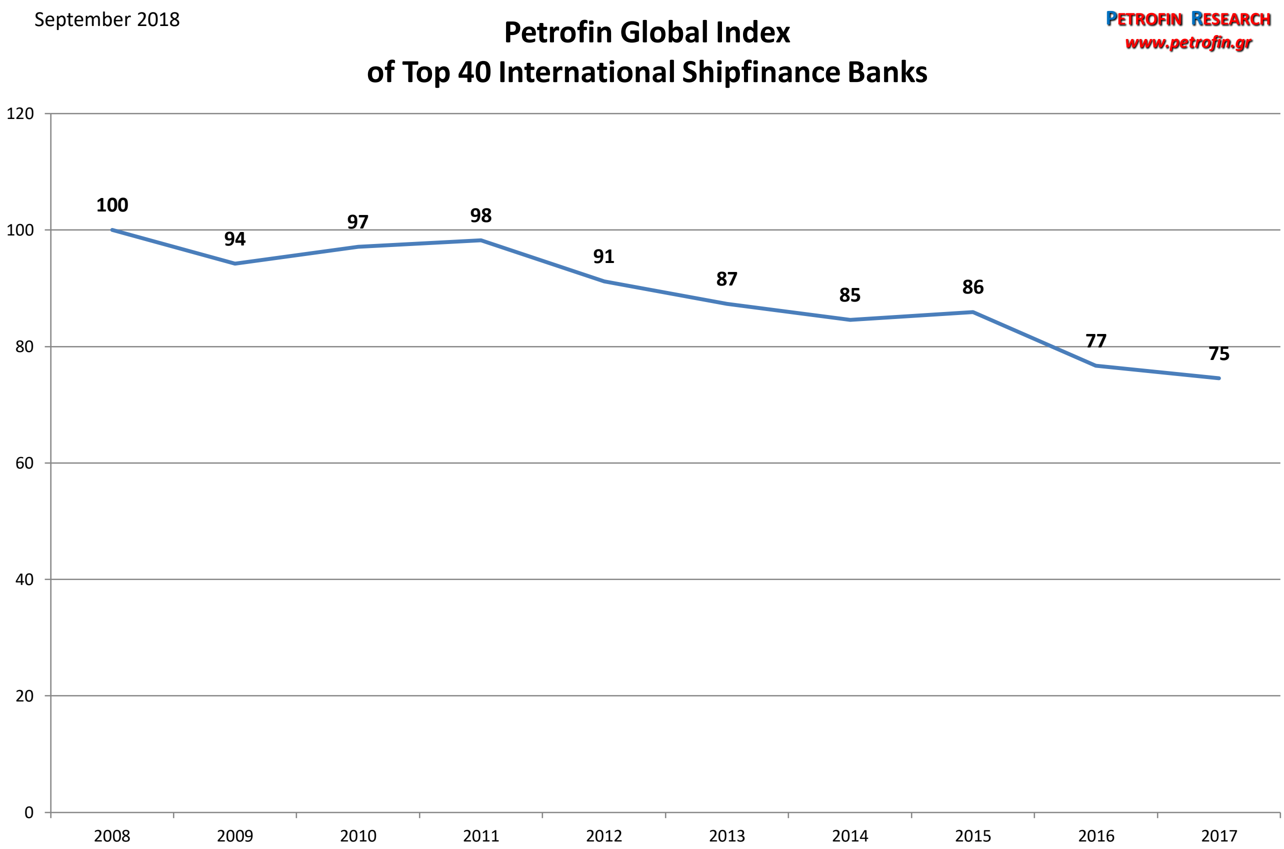


Global bank finance stands at the lowest level of the last 11 years. Banks are well underway in addressing their non performing loanportfolios and are also beginning to alter their departmental structures in relation to shipping. For example, both Nordea and ABN Amro, the first being a bank reducing its exposure and the second one that is expanding, have included shipping into other existing departments, such as corporate lending and the logistics unit, respectively. This does not necessarily denote that shipping is of lesser importance. Nevertheless, it takes away the independent status of shipping It should be noted that recent statements by Western banks indicate a reversal in loan provisions and increased shipping profits, which is a positive sign for the future.

2. Petrofin Global Index of Shipfinance

In Graph 3, the Petrofin Global Index from 2008 till 2017 continues its sharp decline for 2017. The index is standing at its lowest point since first published in 2008.

Graph 3: Petrofin Global Index of shipfinance between 2008 - 2017



Source: Petrofin Bank Research ©

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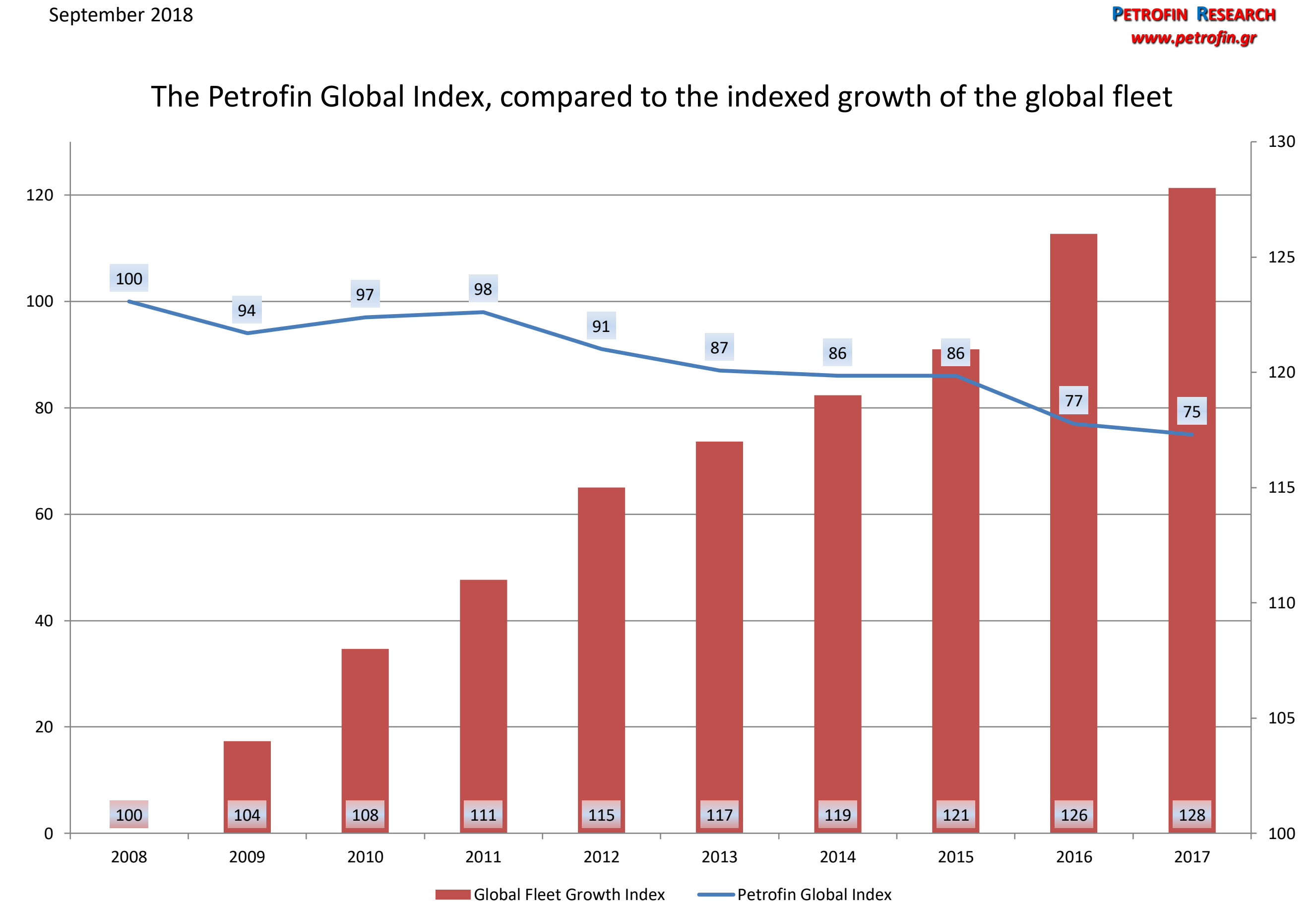
Graph 4: The Petrofin Global Index, compared to the indexed growth of the global fleet (fleet data from Clarkson's (World Fleet Register)



Source: Petrofin Bank Research © and Clarksons' World Fleet Register

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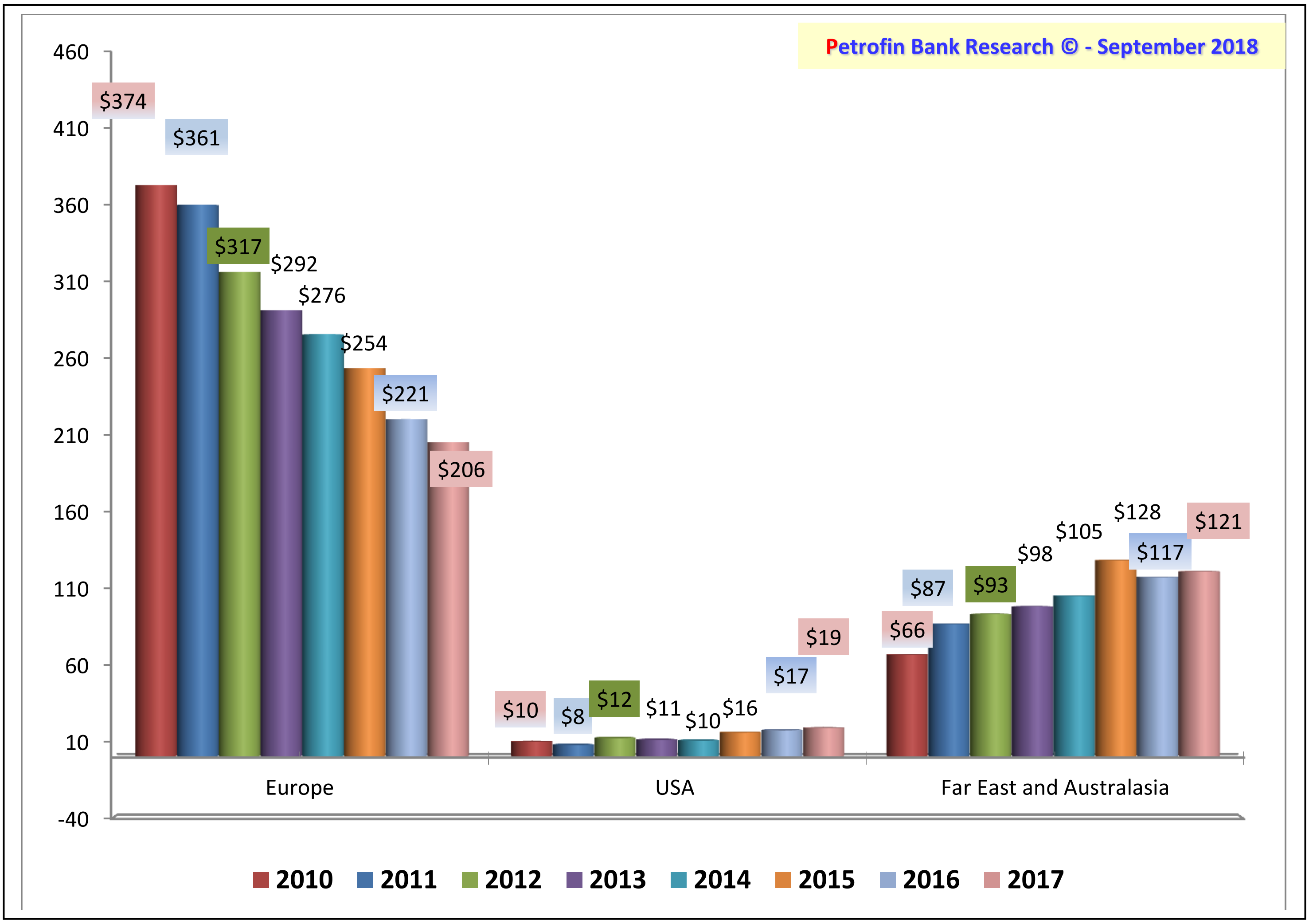
The growth of the global fleet is increasingly funded from non-banking sources. During 2017, Chinese Leasing to shipping stood at $47bn.

Petrofin Index has fallen by 25% whereas the global fleet is up by 28%.

3. Nationality and Commitment of Banks

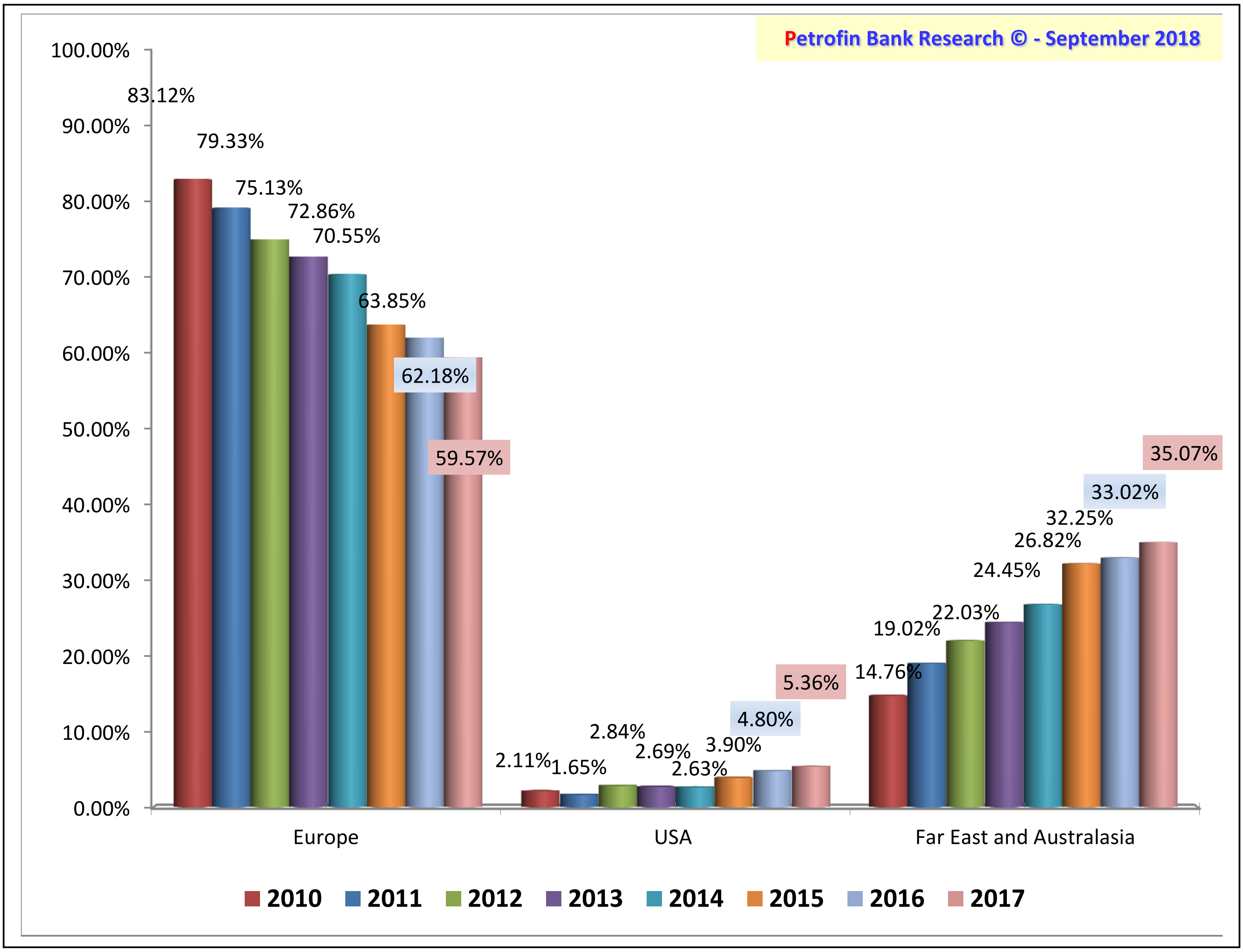
Over the last year, the consistent downward trend of European banks has continued, whilst Far Eastern shiplending has taken up some of the slack, with the US posting an increase of 12% to their modest portfolio.

Graph 5: Breakdown of Global shipfinance portfolios according to geographical area, in US$bn



In the Graph below (Graph 6), it is important to observe that the fall in Far Eastern ship finance did not affect its share of the global portfolio. On the contrary, Far Eastern share has increased (from 32% to 33%) as European banks are declining faster. It should be noted that, although the Royal Bank of Scotland and Commerzbank may still have some residual shipping portfolio, we have not included them this year, as they are selling these loans or the vessels at a fast pace.

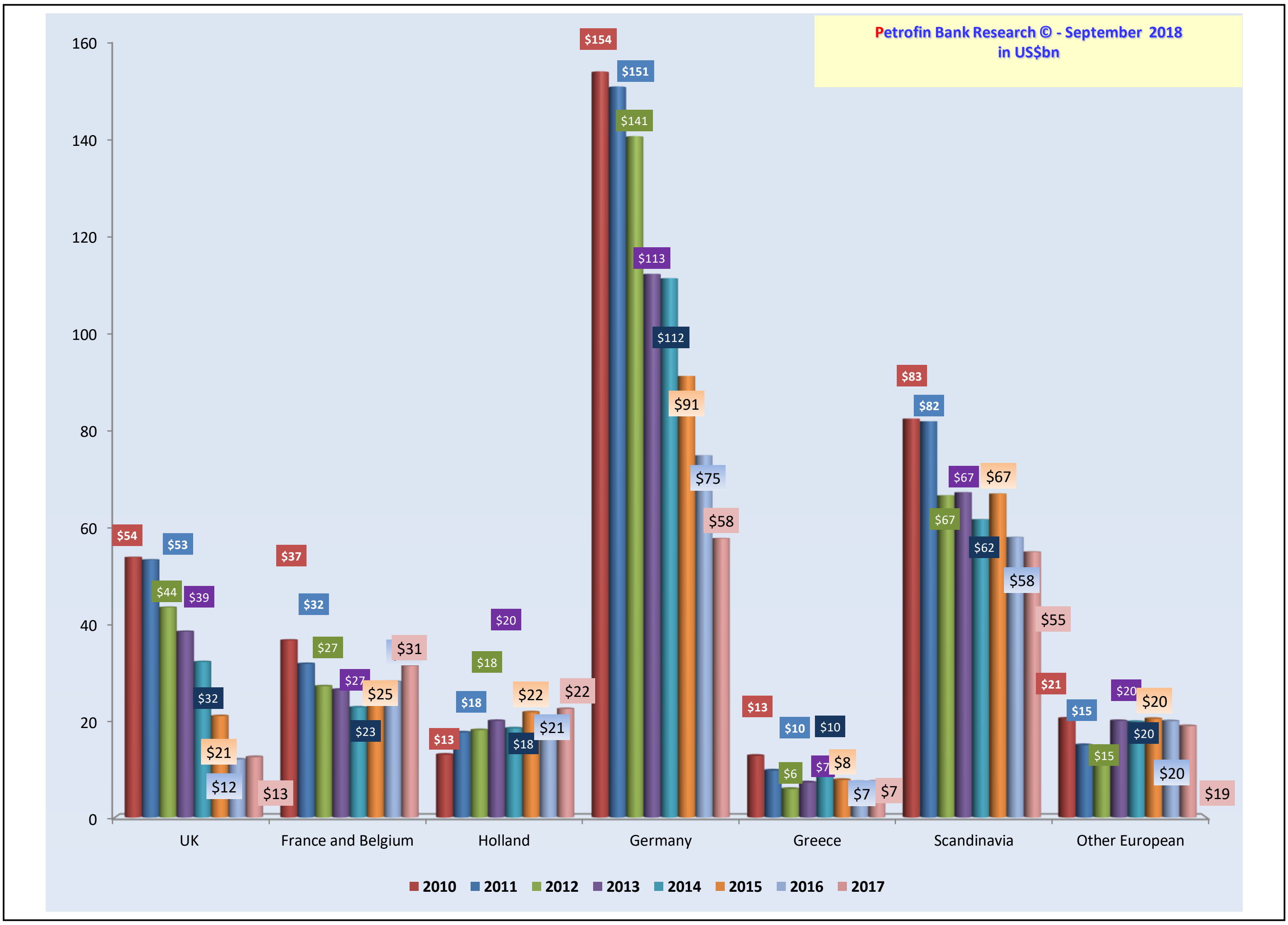
Graph 6: Breakdown of Global shipfinance portfolios development according to geographical area, in % share of total



Compared to 2010, the European share of the global ship finance market has dropped from 83% tp 59.6%, whilst the Far Eastern share has grown from 14.8% to 35%.

Putting the European bank global shipfinance portfolios under the microscope we observe that Scandinavian banks are now showing a slowdown and German banks continue to fall (Graph 7). France shows a modest increase, whilst Holland is now steady in a tight range between US$21-22bn.

Graph 7: European banks' global shipfinance development



4. The outlook for 2019 and beyond

The outlook for the dry bulk market appears positive with vessel values holding their gains and charter rates showing robustness. Demand for dry seaborne trade is rising at 3% and the yoy increase in the size of the bulk carrier fleet is also rising at approximately 3% p.a. Thus, it appears that an equilibrium has been reached between demand and supply. Any surplus or shortfall is likely to depend on other factors such as, slow steaming and port congestion, as well as geographical peculiarities. With an orderbook of 9.8% it would seem that future supply has been contained for now as well.

The same cannot be said for world crude oil and oil products seaborne trade, which is growing at a much lesser rate of 2% and 1% respectively. However, the increase of the tanker fleet is growing at only 0.5%, although the order book is at the same percentage levels as that of dry bulk at 9.8%. The main difference lies with low average tanker rates, which renders most types of tankers less cash flow positive and attractive than bulkers.

Tanker prices though, have largely held their own except for older Aframaxes and MRs, which have been weak.

The rest of the shipping sectors have been rather lackluster with the exception of the LNG sector, which is attracting a lot of interest by owners.

The above rather supporting shipping environment and the somewhat restored cash flows have assisted banks in managing, firstly, to contain fresh loan loss provisions and, recently, to show some recoveries.

Although the shipping climate has been helpful to banks, the international banking environment remains challenging, especially for western banks, which are struggling to meet capital ratio criteria and other central bank regulatory requirements. In addition, the availability of loanable funds by western banks remains restricted and this is not supportive for a capital intensive industry, such as shipping.

All western banks have conducted reviews, as to their future shipping exposure and whether ship finance should remain a separately run activity. Some banks have concluded that their continued presence in shipping would benefit by their shipping departments becoming part of a bigger internal corporate structure e.g. DNB, ABN AMRO, BNP and others.

Increasingly, banks have sought to emphasise fees, non-risk assets and services and deemphasise loan volumes to a level they deem strictly necessary to satisfy their core clients.

This process of re-orientation and restructuring is still ongoing and, as such, may well adversely impact on western banks' loan exposures, in the next few years.

Whilst some of the slack is being taken up by Far Eastern banks and, to some extent, North American banks, last year saw an overall decline in the top 40 shipping banks loan exposures by $10bn. This indicates that global loan exposures may be bottoming out.

This year's research shows that since 2008, global ship finance (top 40 banks) has fallen by 25%, whilst the global fleet grew by 28%. This large differential has been taken up primarily by leasing firms, mainly in the Far East. These consist of Chinese, Japanese, as well as Korean leasing companies, often linked to international Far Eastern banks. The leasing or bareboat hire purchase model is especially attractive to leasing companies, which have developed the know how to compete, whilst enjoying satisfactory profitability.

Both leasing companies, as well as banks have developed a targeted appetite for the biggest clients and transactions, with small and medium size clients facing the worst both in terms of availability and terms. Leasing companies whose ship finance total reached last year 47bn, tend to be more flexible, as to the client they are prepared to finance, although the approval process is often quite lengthy.

Some newer banks, M&M, Berenberg, Warburg, ATB and others, have also increased their lending, enjoying both low LTVs and satisfactory loan yields. However, their overall contribution to ship finance remains relatively modest.

Export finance has also grown in support of local ship builders, especially as their terms often offer longer maturities and lower margins. It could be argued though, that such attractive terms often counterbalance higher newbuilding costs.

Looking into the future, we anticipate continued growth by leasing companies. The same should be said of investment and equity funds, which have grown enormously over the last decade, most of which, however, focus primarily on the equity side of the business. Where lending is offered, their target yields are often very high (in excess of 12% p.a.), that only few owners can accept, despite the presence of grace periods and longer loan profiles.

The US equity and bond markets have been relatively quiet, with few IPOs. Recently, the 'LNG story' and the 'anticipated recovery of tankers' have added some IPO candidates with better potential. Overall, an increase, though not dynamic, in IPO activity is expected in the US.

The market that has evolved into a primary centre for shipping investment, loans and bonds has been the Norwegian market, which has shown to be a credible alternative to the US. The Norwegian market is growing in both size and depth and it has become easier to anticipate and rely upon. The recent Alafouzos fleet public listing, as well as the developments of Songa bulk, have brought the Norwegian market in the limelight. Supported by the presence of shipping specialists and an increasing number of placement brokers, as well as a knowledgeable investor base, the Norwegian market is expected to continue to grow strongly.

Returning to the banking ship finance market, it is essential for western banks to be able to attract fresh capital at a low cost, in order to compete with their Far Eastern competitors. It is anticipated that western banks will regain some of their lost competitiveness and appetite over the next years, but a great deal would depend on their overall lending capabilities and to the extent that shipping is attractive compared to other industries.

Lastly, the stability of the global financial economy as it addresses the extremely high levels of global debt, will also have a bearing on the ability of all banks to lend substantial funds to the shipping industry.