

# Debt Financing



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**DnBNOR**

# Agenda

**Perspective of Shipping**

**Who is DnB NOR?**

**Financing Alternatives**

**How do we do it?**



# The Shipping Industry



- **Unpredictable earnings**
  - Volatility due to quick changes in the supply/demand balance
    - Demand: Transport volumes determined by world economy and world trade, changes in foreign exchange rates, shifts in supply/demand for natural resources, and even weather
    - Supply: Determined by a finely tuned balance of newbuildings, demolition activity (a function of vessel age, newbuilding prices, scrap steel prices, and, in some cases, regulation), and charter rates
- **Competitive Factors**
  - Barriers to entry/exit, long lived assets, high fragmentation
- **High operating leverage**
  - A large portion of costs are fixed, capital intensity
- **Complex company structures**
  - Holding companies with various legislation involved, transparency / disclosure, private companies
- **Regulatory environment**
  - The U.S. Oil Pollution Act of 1990, IMO

## Rating Agency summing up...

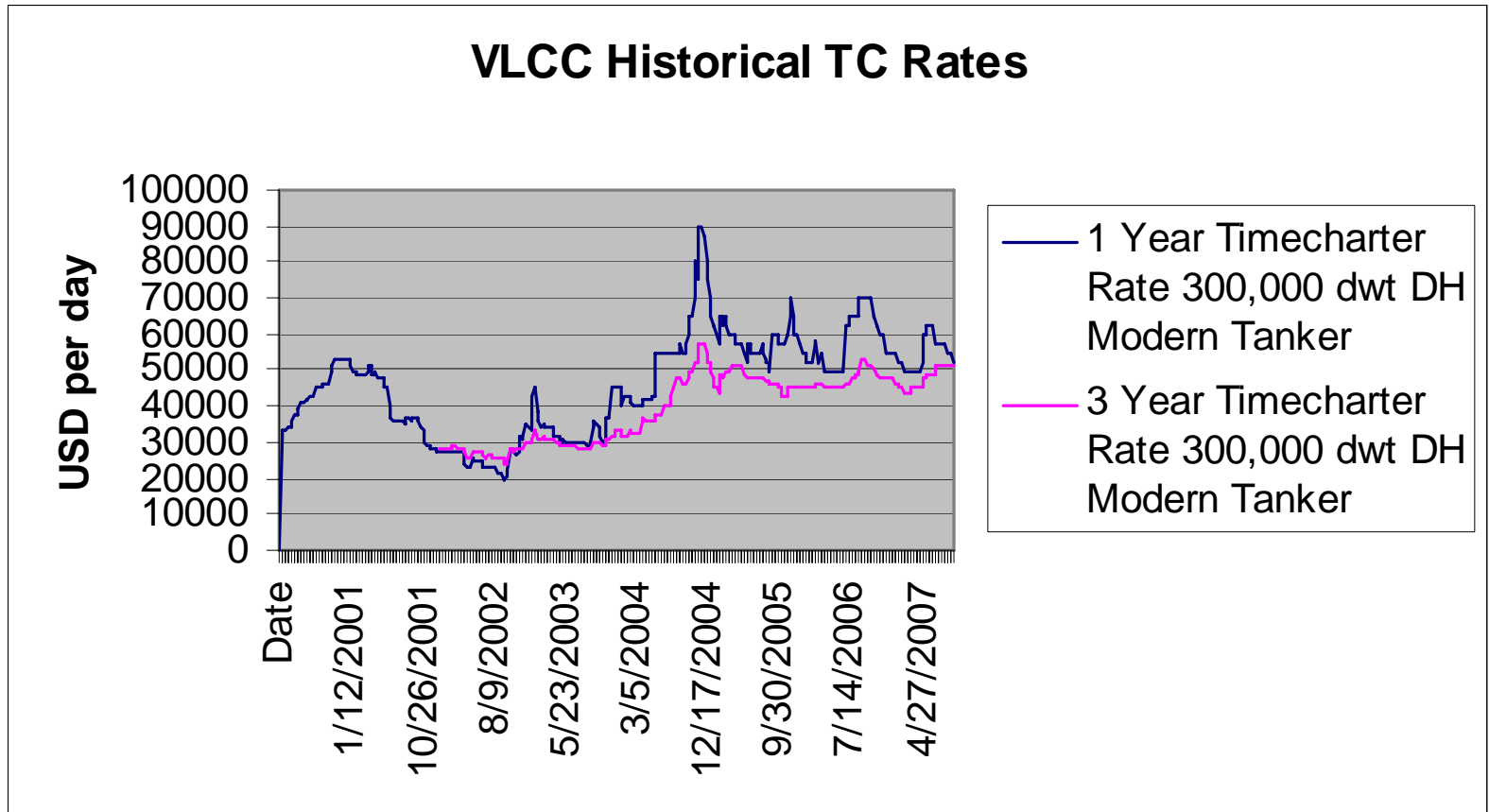


**“Generally, the shipping industry's risk profile may be characterized as speculative-grade because of its:**

**Economic sensitivity, capital intensity, and competitive factors, all of which lead to extremely volatile pricing swings in both freight rates and asset values”.**

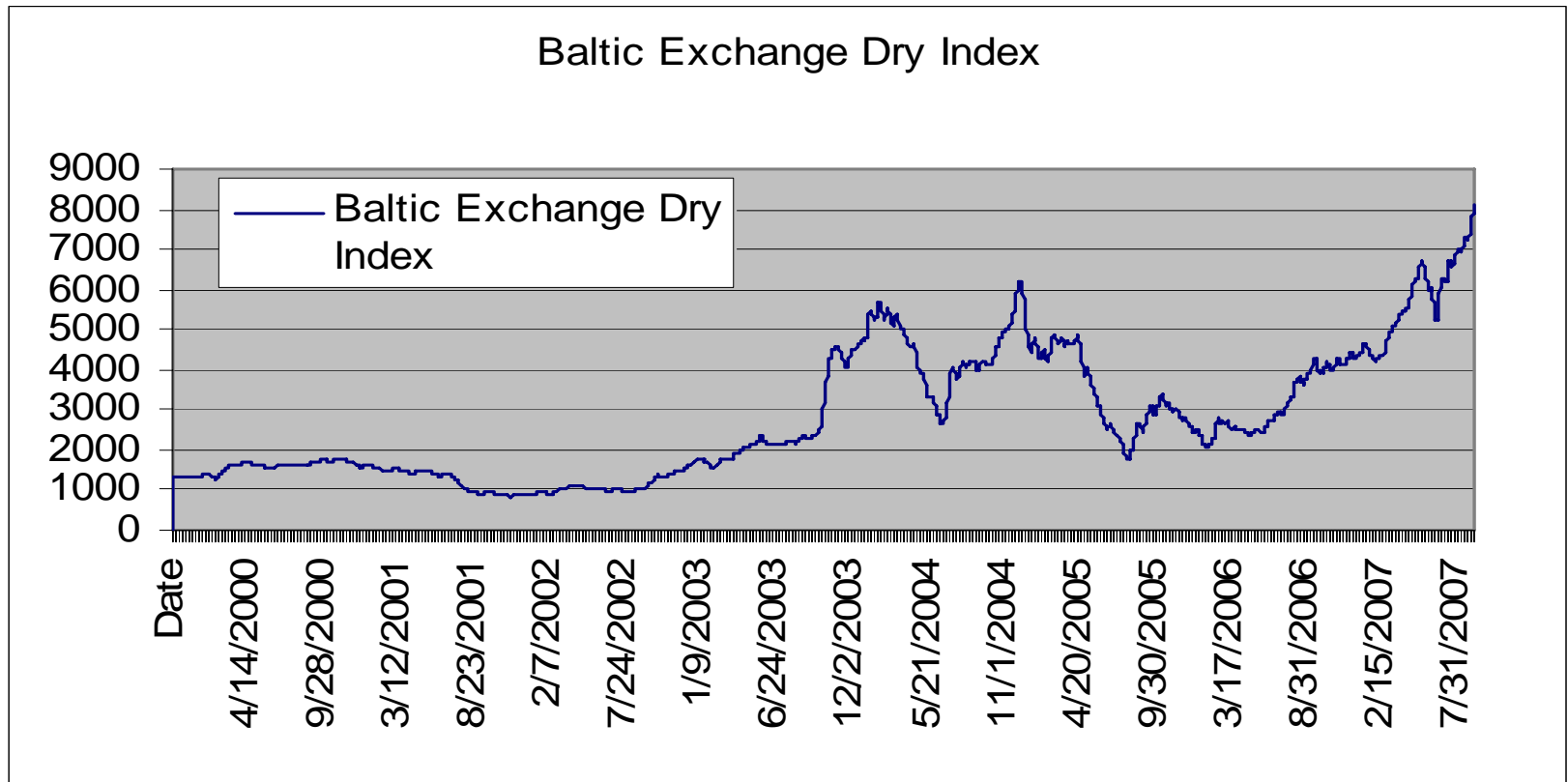


# VLCC – Historical TC Rate Volatility



Source : Clarksons

# Baltic Dry Index



Source : Clarksons

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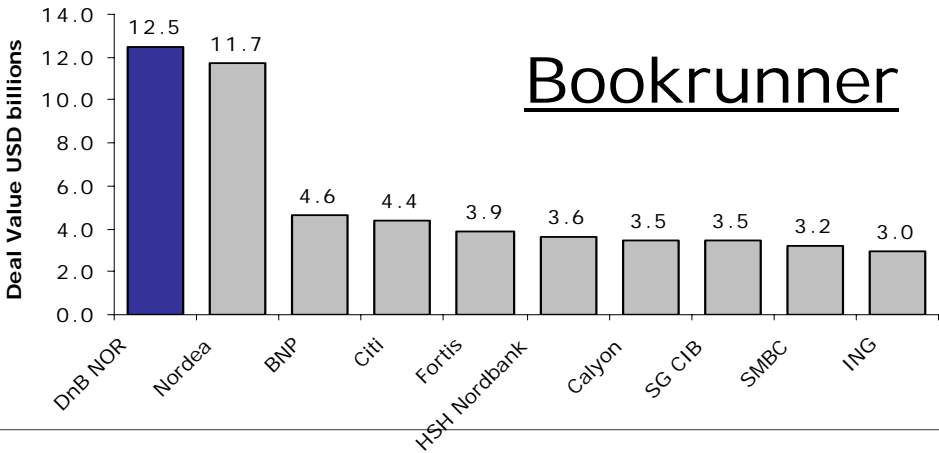
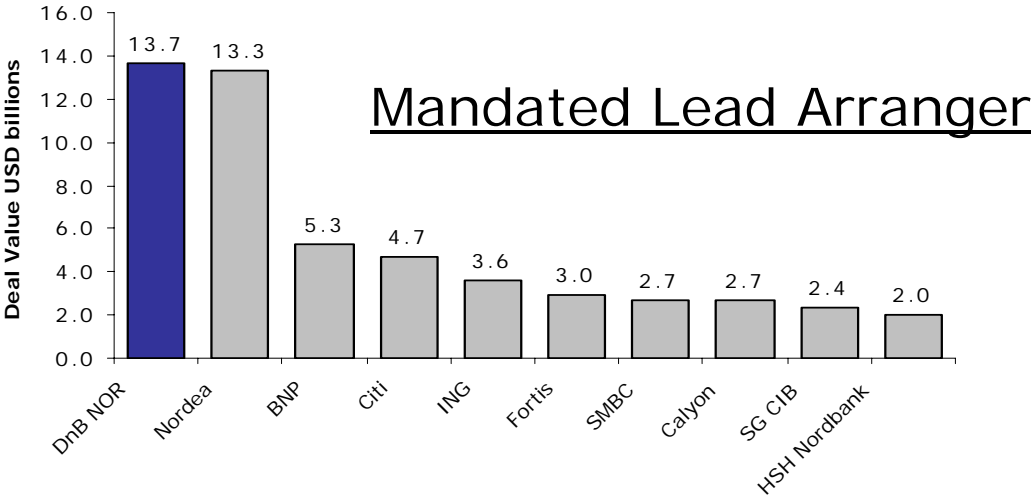
# DnB NOR Shipping at a glance



- **Among the world's leading shipping/offshore banks**
- **Total shipping commitments approx. USD 25 billion.**
- **Approx. 50 % of portfolio consists of exposure to non-Norwegian clients and is growing**
- **No. 1 Mandated Lead Arranger and Bookrunner of Syndicated Shipping Loans in 2006**
- **More than 25 years of specific focus on shipping/offshore**
- **Nearly 80 professionals with long and varied shipping/offshore experience**
- **Presence in the major shipping locations:**
  - Oslo and Bergen
  - London
  - New York
  - Singapore
  - Shanghai



# Top MLA and Bookrunner for Arranging Syndicated Shipping Loans in 2006



# DnB NOR Shipping Asia

## Background

- Base of major shipping clients with long history & high quality asset base
- Loan commitment of USD4 billion to Asian shipping
- Operates in the Far East (north to Japan, south to Indonesia & west to India)
- Singapore branch established for over 35 years
- Shanghai branch set up in 2006

## Products & Services

- Capital (Debt & Equity)
- Advisory Services
- Structured Finance
- Treasury Products
- Cash Management
- Guarantees / Bonds

**Perspective of Shipping**

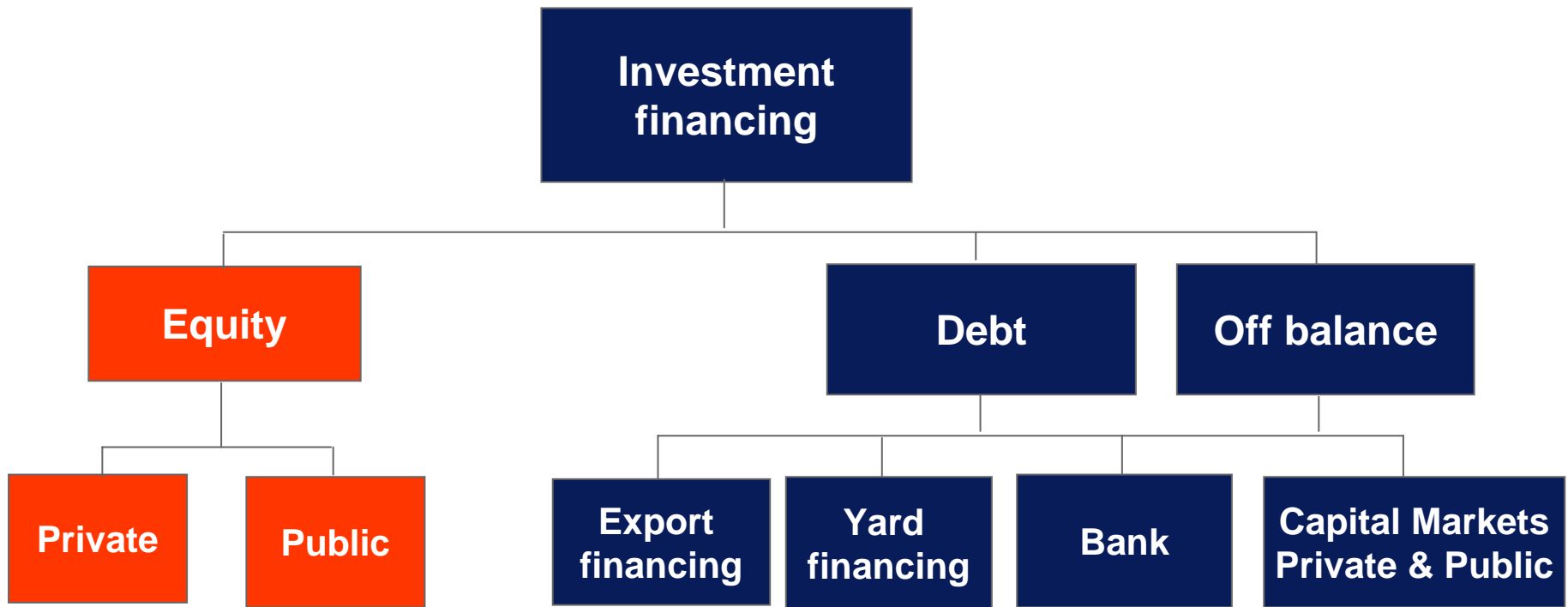
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# Ship Finance in general



**Investors optimal capital structure will combine flexibility with the lowest total cost of capital**

... but different split of risk & reward



### **Equity investor**

- **Full upside**
- **Full downside**

### **Bank / Lender**

- **No share of upside  
(principle + interest only)**
- **Protection on the  
downside**

**Ship financing is all about reflecting the risk and reward sharing between the equity investors and the bank**

# Capital Sources



## Export financing

- Government credit schemes
- Repayment to zero over 12 years (OECD terms)
- Yards co-operate with governmental credit agencies

## Leasing

- Financial leases are a financing source
- Lease is an alternative to buying – a rental scheme
- Tax benefits through use of depreciations by lessor

## Bank Financing

- Most commonly used
- Known to be flexible & cheap

## Capital Markets (Bonds)

- Long-term financing, up to 10-20 years
- One drawdown, one repayment
- Few, but tough financial covenants
- Often unsecured
- Limited flexibility, prepayment penalties

# Bank Financing



## Senior Term Loan

- Primarily one drawdown of the loan
- Repayment through instalment
- Instalments paid can not be redrawn

## Revolving Credit Facilities

- Several drawdowns under the loan
- Repayment through reduced availability
- Amounts paid are available for new drawdowns

## Bridge Facilities

- Shorter term financing to bridge a time gap
- Both 'legs' of the bridge to be solid

## Acquisition Financing

- Not allowed to finance against assets in target comp.
- Often high profile transactions

## Mezzanine Financing

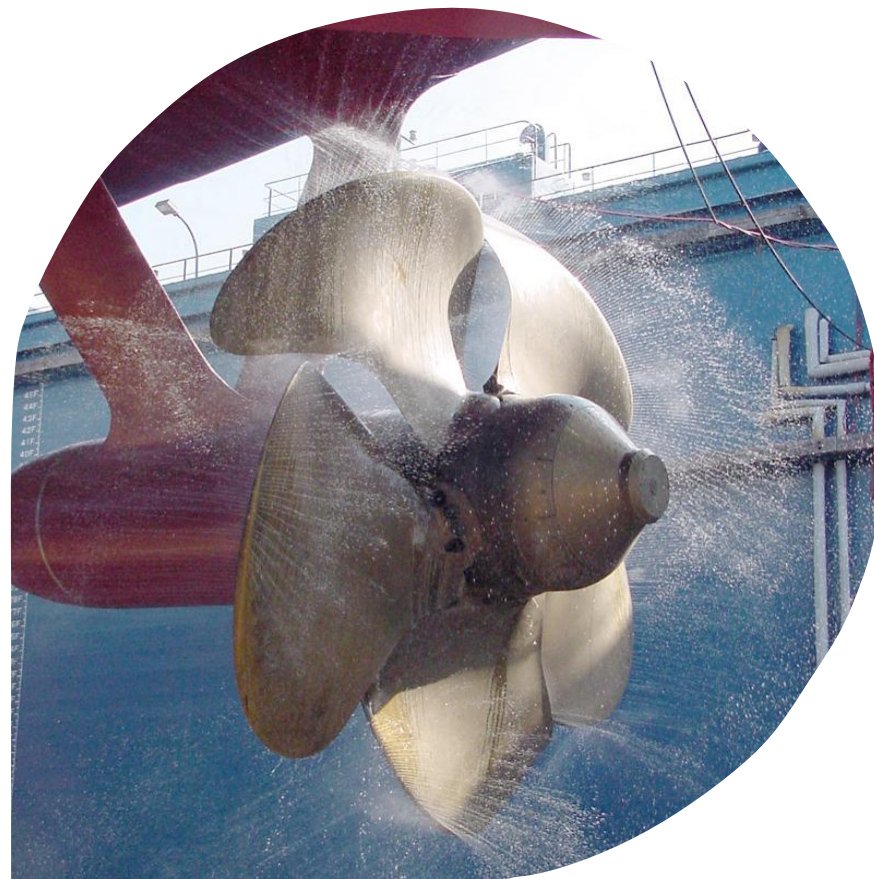
- Normal bank debt with lower security coverage
- Higher cost due to higher risk
- Quasi equity, right to convert or 'equity kicker'

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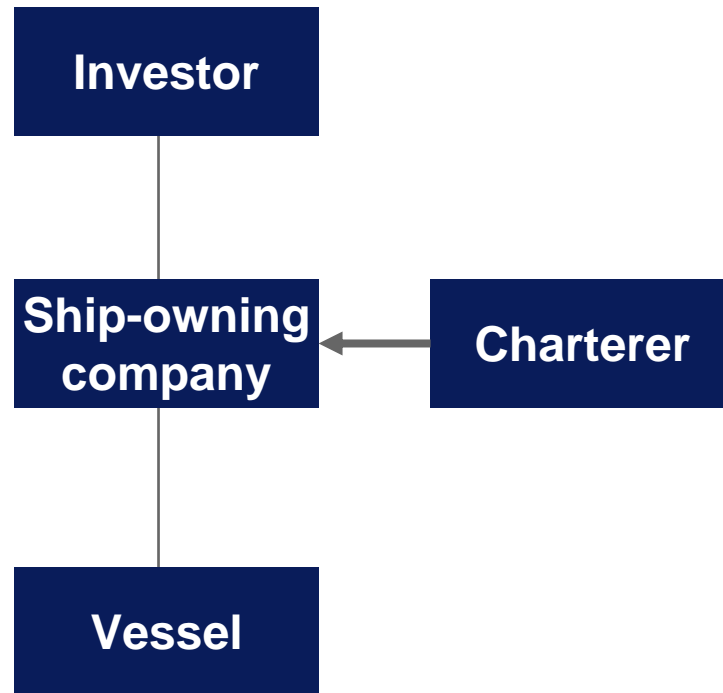




# Main Considerations



- Client
- Cash flow
- Collateral



# Management track record

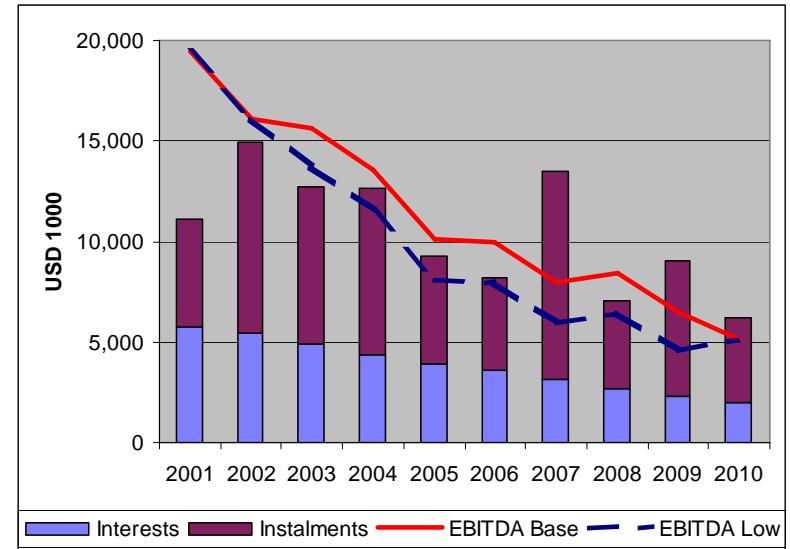


- **Operational skills and financial track record**
- **Historical performance versus that of the industry peer group**
- **Innovation and flexibility in reacting to changing market conditions**
- **Timing of equipment acquisitions and divestitures in relation to industry cycles and availability of attractive prices**
  - Certain companies, particularly in the tanker trade, buy and sell assets or newbuilding contracts primarily to profit from industry price swing. Not all do well..
- **Line of succession and management strength and depth**
  - Management is extremely important in the volatile and fiercely competitive ocean shipping industry. The depth and breadth of a company's management must be evaluated, especially for private companies or companies that are controlled by their founders or immediate family members (Corporate Governance)

# Cash Flow



**Will cash flow (EBITDA) cover interest and instalments in a Low Case scenario?**



## Cash Flow Stability

- The length of charters
- Time for renewal (all at the same time?)
- The charterer's financial position
- How firm is the contract (charter party)?

# Collateral

- Secured lending still most common though, unsecured lending to first class names has increased
- The most common securities
  - Mortgage
  - assignment of earnings/charter party
  - assignment of insurances incl. MII/AP
  - Parent company/personal guarantees
- Collateral should be the "second way out", and not justify an otherwise bad credit

# Loan Covenants

- Covenants assist Lenders to reach an understanding with a borrower regarding how the borrower will conduct its business and financial affairs
- The stronger the covenant package is, the greater the degree of control the lender can exercise over the investment/borrower
- Borrowers typically seek the least restrictive covenant package they can negotiate and maximum flexibility to conduct their business in the way they see fit
- Covenants do not play a significant enhancing role in determining *credit quality* of a company

## Summing up ..... – so far



- **Client – who is behind and what may they do with the money?**
- **Cash flow – are you comfortable with the debt service?**
- **Collateral – do you have a second way out?**

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