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"RESTRUCTURING AND FUNDING SOLUTIONS IN A CHALLENGING BANKING ENVIRONMENT"

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ABSTRACT

Distress in the shipping sector continues to highlight the fundamental disconnect between what drives shipping businesses and their financiers in the current environment.

Lenders avoid taking action for fear of incurring enforcement and holding costs, because of uncertain market conditions, and a reluctance to crystallise losses. Lenders are increasingly unlikely to provide desperately needed additional funding.

Shipowners face the loss of their equity, they have run out of funding options to help them manage their fleet efficiently, and have no incentive (or alternative) other than to adopt delay tactics with financiers in the hope that the market improves.

In short, there remains a large part of the sector where the lack of available funding is preventing shipowners from optimising earnings, and banks from maximising recoveries.

This article explores the characteristics and risks that arise from not addressing problematic debt and vessels, and suggests some solutions for both shipowners and banks.

Common challenges faced by distressed shipping companies/financiers…and practical solutions.

Managing distressed shipping and drilling situations is complex for shipping companies and financiers alike. The exposures and potential losses are significant, the legal framework is difficult, funding solutions are often limited (or non-existent) and management time and costs are significant.

Set out below are common challenges faced by distressed shipowners and financiers and some effective and practical solutions:

Challenges	Shipowners	Lenders	Practical solutions
1. Poor information and deteriorating relationships	• Owners are focussed on running the business - often at the expense of properly managing and reporting to lenders • Distressed shipowners often struggle to effectively manage working capital and trade creditors – paying the most aggressive rather than most important creditors	• Relationship fatigue - loss of trust in the borrower • Concerns over accuracy or lack of borrower information	• Early engagement is key for both shipping companies and financiers - eliminate inaction and drive solutions before equity (or security) value is wasted • Financiers should utilise 'soft' defaults as an opportunity to obtain more information and challenge uncommercial decisions • Appointing a Chief Restructuring Officer ("CRO") to manage lenders and trade creditors and improve communication ➢ a CRO demonstrates a strong commitment to restructuring and is an effective circuit breaker to move past legacy issues ➢ the CRO also improves transparency and access to information

Challenges	Shipowners	Lenders	Practical solutions
			• A key strength of any experienced CRO is managing trade creditors and creating breathing space through strong working capital management
2. Restructuring inertia	• Delays caused by unrealistic equity raising activities – owners reluctant to acknowledge 'true' equity value or give up control • Equity is rarely a solution on its own – it typically provides limited deleveraging and liquidity through to where the borrower expects (or hopes) the market to turn	• Lenders fall prey to borrower delays - avoiding repayments and dragging out any restructuring in the hope that the market improves • Absentenforcement (or other solutions), there is little incentive for borrowers to accelerate solutions	• The earlier restructuring negotiations commence, the better. The best options are usually all available early, and start to fall away with time. Restructuring inertia is short sighted and is not in the interests of shipowners or lenders • Formal restructuring tools such as Schemes of Arrangement (Singapore, UK, Australian, HK), PKPU (Indonesia) and Chapter 11 (US) warrant consideration – a payment moratorium provides breathing space to formulate a comprehensive and equitable restructuring proposal; conversely a court timeline can be effective in forcing resolutions
3. Enforcement complexities and costs	• Poor vessel/group ownership structure increasing susceptibility of wrongful arrest or sister arrest and requiring ransom payments	• Enforcement is complex - maritime law, insolvency law, flag state regulations and the (often changing) location of the vessel all play a role • Practically difficult where the owner or crew is resistant/hostile • Unknown maritime claims and liens rank ahead of financiers. Priority of claims can differ between jurisdictions • Financiers reluctant to incur enforcement costs and be liable for future holding costs in uncertain market conditions without an obvious solution	• Impediments to enforcement are best managed by restructuring professionals who can deliver practical and innovative solutions and the necessary funding and ownership structures (e.g. protecting vessels from sister arrest)
4. Funding	• Highly capital intensive sector-maintenance/ preservati on costs are substantial. A lack of funding generally limits options • Financiers pushing shipowners to restructure, but not providing the further funding to achieve the best results • Working capital constraints lead to continuous crisis management rather than optimal fleet performance	• Institutional global lending freeze • W orking capital funding is largely non-existent • Re cover y of enforcement and asset preservation costs takes time • Enforce/take control-then what? • Lack of available resources, funding, expertise or even legal capacity to operate vessels and/or rigs effectively	• Identify an experienced restructuring advisor or partner to provide funding to maximise vessel earnings and restructuring or sale recoveries • Incentive based fee structures rewarding working capital management and cost savings

Debt Restructuring Case Study (Representing Debtor): PT Berlian Laju Tanker / Chembulk (BLT Group)

Borrelli Walsh representatives were appointed CRO and Directors of the BLT Group, a dual-listed (Singapore and Jakarta) Indonesian company with debt in excess of USD2 billion, and a chemical and gas tanker fleet of more than 100 vessels operating from Jakarta, Hong Kong and US. BLT had announced a unilateral moratorium on interest and principal repayments to all creditors, as well as recent investment in some non-shipping Indonesian based assets. As a result, creditors were hostile to current management, and the future of the company as a going concern was in severe jeopardy.

Upon our appointment, measures taken included:

- taking actions to stabilise the crisis through implementation of vessel protection measures;
- engaging with senior bank lenders, international and local bondholders, as well as sale and leaseback creditors;
- through our appointment as CRO and, more importantly, as Directors, we were able to bring a degree of confidence to creditors that the company would be managed appropriately with a high degree of control, and with clear information to creditors;
- short and mid term cashflow forecasting and robust cash management;
- restructuring an underperforming fleet by changing ship management, removing (through lay up or sale) unprofitable vessels and contracts including realigning trade lanes for the core fleet;
- protection of vessels through engagement with hostile creditors, and utilising protective court measures such as PKPU and Ch.15 protective moratoriums;
- disposal of various non-core assets/vessels in a willing buyer/willing seller manner to reduce debt;
- formulating a restructuring proposal that accommodated the diverse lender and stakeholder groups (Asia, New York, London and Netherlands) including preparation of financial forecasts to establish new money requirements for working capital, cash sweep mechanisms, and raising new equity capital;
- having gained the confidence of Lenders, raised additional loans of approximately USD20 million, negotiating terms and security structure, to provide much needed working capital to maximise operational efficiencies within the core fleet; and
- negotiating terms and implementation of the restructuring in the framework of a PKPU process in Indonesia, Scheme in Singapore and Chapter 15 in New York.

Following three years of our appointment, Borrelli Walsh had obtained majority approval from secured and unsecured creditors in respect of a restructuring that involved, amongst others, the conversion of USD1.5 billion unsecured debt into half of the company's equity and senior debt holders obtained vessel fleet security and were paid in full. In parallel, the company deleveraged completely and continues to operate with a smaller but profitable fleet. Enforcement Case Study (Representing Bank): Singapore Based Shipping Group

Borrelli Walsh was appointed receivers and directors of a shipping and dry bulk trading shipping group by an international bank following a prolonged period of non-payment of both interest and principal. The debtor initially refused to hand over its books and records to receivers, and denied access to the shipping group's office premises.

Upon our appointment, measures taken included:

- secured control and stabilised the businesses, managing the operations of 14 vessels (5 owned and 9 chartered) and more than 30 ongoing cargo voyages;
- worked with local counsel to promptly secure control (including through our appointment as directors) of more than 10 companies with company registries and flag state authorities in Singapore, United States, Cayman Islands, Marshall Islands, United Kingdom, and Mauritius;
- developed short and long-term cash flow forecasts and established funding requirements, and subsequently secured additional working capital loan totalling USD6 million;
  proactive stakeholder management and stabilisation including regular meetings and discussions with employees, suppliers and managers; ship owners, charterers, ship managers, banks, financiers and insurers;
- managed the day-to-day operations of the shipping group including, amongst others, completion of the sale of 2 chemical tankers, re-negotiation of insurance renewal, renegotiation of charter hire rates and ship management fees; and
- successfully completed an international sale process for the shipping group.

Borrelli Walsh effectively took control of the shipping group by taking enforcement action in multiple jurisdictions simultaneously, removing incumbent management, and subsequently stabilised the shipping group's operations through constant communications with key stakeholders – that is, maintaining (and emphasising) "business as usual."

Importantly, within a relatively short period (around six months), Borrelli Walsh stabilised operations and secured a buyer for the shipping group - this facilitated a substantial recovery for the international bank in circumstances where they had already provided for the loan in full.

Borrelli Walsh has a strong track record of providing effective end to end solutions (including the provision of funding) to distressed shipping companies and financiers – this includes a full suite of restructuring, enforcement, funding and operational support services. For more information, please contact Mark O'Reilly at mo@borrelliwalsh.com, David Reeve Tucker at drt@borrelliwalsh.com or Jason Kardachi at jk@borrelliwalsh.com.