# INTERNATIONAL POLL AND SURVEY

"Shipping Finance 2020 –

Trends and Prospects after the outbreak of COVID-19"


July 2020

**XRTC Business Consultants Ltd.** has been active since its establishment (1999) in Shipping Finance and in the provision of advisory services to maritime companies. XRTC has been a commercial representative of international banking groups in the Greek Shipping Market, such as the French banking institutions Credit Lyonnais and Natixis, as well as a consultant to National and International Organizations and international shipping companies.

The Company has secured and organized with great success a large number of shipping loan agreements under various forms, through cooperation with International Banking Groups since its establishment.

Since 2009, XRTC cooperates with Chinese banking groups that are interested in investing in Greek Shipping Market. The company managed for the first time ever to secure the financing of a Greek interest Shipping Company, directly from the Chinese banking group China Development Bank. Since then the company acts as ship-finance advisor to the institution.

XRTC's staff has knowledge and experience on a worldwide level, by offering high quality services throughout the duration of a transaction. The Company's Research and Development Department based on its knowhow, is able to analyze in depth all the matters of International Shipping. As a consultant in Ferry Markets the company has undertaken many projects in Greece and abroad for both ship financing and further market development. XRTC cooperates with the largest export credit agencies in the world.

XRTC has been honoured by International and Greek firms for its contribution to the development of Shipping and Ferry Market; such as Lloyds Greek Shipping Awards 2010 as the "Best Shipping Financier of the Year" and the award by Transport Finance as the "Best Deal of the Year for Export Credit".

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# *INTRODUCTION*

The financial aspects pertaining to commercial activities of the marine industry are covered entirely under maritime finance. Banks remain the backbone of shipping finance despite the financial crisis of 2008 and the slow-down of the world economy that have led them to limit their high-risk investments. Over the years, European banks which have been the leaders in shipping finance, have been affected the most. The Euro crisis, the stricter risk management policies put in place by the ECB, and the much more demanding disciplinary framework such as the Basel's Accord have put pressure on European banks to divest.

The decrease in the European banks' market share has been taken by the Far East Leasing companies, which are largely unregulated compared to banks. The paradox is that many Chinese leasing houses are funded by traditional ship finance banks.

The current COVID-19 pandemic has heightened uncertainty over the economy, while many things remain outside our control. As the virus spreads around the globe, concerns have shifted from supply-side manufacturing issues to decreased business in the services sector. The pandemic is estimated to be causing the largest global recession in history, with more than a third of the global population at the time being placed on lockdown and the rest being placed in the uncertainty of the restarting security measures that will limit the spread of the pandemic. This rapid spread has had a major impact on global shipping markets, with the slump in demand for goods from China having a ripple effect on everything from container ships to oil tankers. While China was the first country to be hit by Covid-19 is now the first and perhaps the only one with a recovering economy and re-emerging population. For the rest of the world, uncertainty is the only certainty.

In line with these changing trends, XRTC Business Consultants Ltd conducted a Poll concerning the prevailing conditions and parameters especially in the international Ship Finance Market, between the 10th and 20th of May 2020. The Poll has been designed to encompass the most important aspects of the Ship Finance industry and investigate the current trends globally. The transition to the new normal encapsulates challenges and opportunities for financiers and investors, which require clear answers before tackled.

The present survey was addressed to global Ship Finance market thought leaders aiming at drafting actions relevant to the new business normal. A private and confidential electronic tool to preserve the anonymity and confidentiality among the participants was used.

The poll's questions are divided in 3 sections. The first part consists of 10 questions of general information related to the institution. Starting from its nationality, its ship finance activities, and the number of its employees to the sale/purchase of NPLs. The second part consists of eight questions related to the institution's Ship Financing requirements. Among the requested information is the preferred sectors of finance, the desired leverage of each institution matched with the identification of the most important threats of international shipping markets.

In the 3rd part of the poll we tried to understand the Lenders' thoughts regarding the key impacts of Covid-19 on global shipping markets as well as the potential effects of this crises on the Ship Finance arena.

The answers received from the participants for each one of the questions are analyzed and presented next.

# *SURVEY FINDINGS AND ANALYSIS*

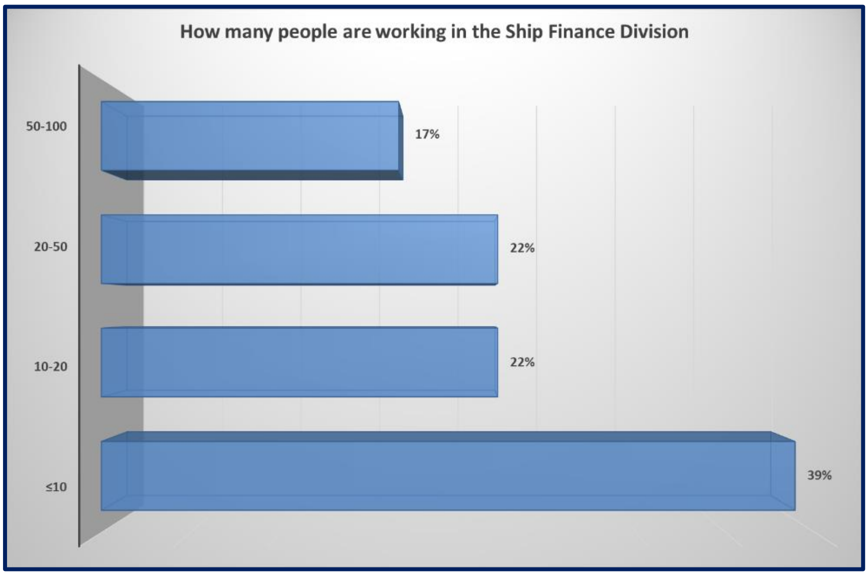
## *PART 1: GENERAL QUESTIONS*

| Questions |
|---|
| Institution's Nationality |
| How many years is your institution involved in Ship Finance? |
| How many people are working in the Ship Finance Division? |

All Greek and Cypriot institutions involved in Shipping finance have participated as well as Banks from Germany, France, Norway, Holland, U.K., U.S.A., China and Japan as follows:

Most of the participant institutions are long lasting shipping financiers. Almost 40% are involved in the sector for at least 50 years, while another 28% are present for the last 20-40 years and 33% for less than 20 years.

As far as the number of Ship Finance Divisions' employees is concerned 39% of the institutions have less than 10 persons dedicated to shipping.




| Questions |
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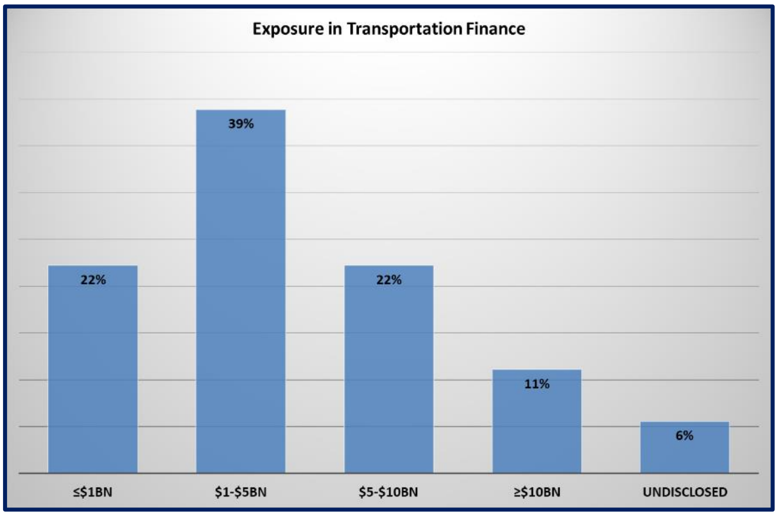
| Has your institution been active in Ship Finance in the last 2 years |
| Are you involved in Greek Ship Finance? |

Almost all participant institutions (95%) have been active in the field during the last two years as they are among the traditional Lenders, while they are all involved in Greek Ship Finance. It is a fact that it is difficult to find a shipping financier who does not support Greek Shipping.

| Question |
|---|
| Exposure in Transportation Finance |

The majority (39%) of the participants' claimed to have an exposure in Transportation Finance between $1bn and $5bn. Around 22% declare that their exposure is equal or less than $1bn while another 22% has an exposure between $5bn and $10bn. Fewer institutions (11%) appear to have an exposure of equal or more than $10bn.

Greek institutions' transportation exposure, with the exception of one, are dedicated to Shipping only without any exposure in off-shore, aviation and rail and road markets. Only one Greek bank is exposed to rail and road. Apart from the Greek institutions, many institutions' exposure is totally linked to shipping. Namely, 37% of the participants state that their transportation portfolio is 100% dedicated to shipping while 32% of the participants kept undisclosed such information. The remaining institutions claim that that more than 70% of their transportation portfolio is linked to shipping.




| Question |
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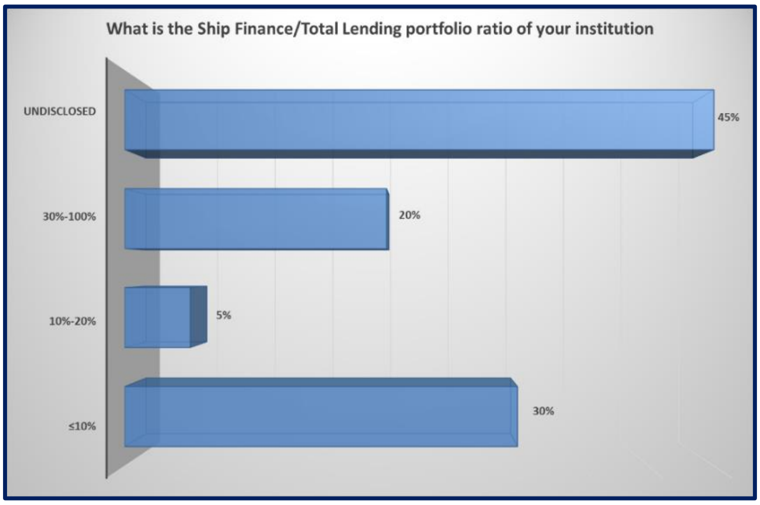
| What is the Ship Finance/Total Lending portfolio ratio of your institution? |

Although this question has not been answered by all participants, the answer provides an x-ray of the ship financing industry. Actually, 45% of the participants kept undisclosed their Ship Finance/Total Lending portfolio ratio.

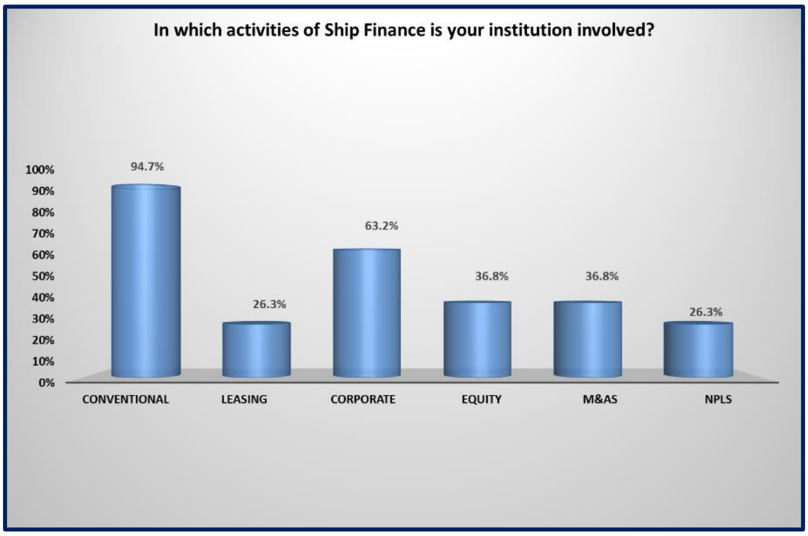


A portion of 30% of them have a Ship Finance proportion of less than 10% in their Total Lending portfolio while for 20% of the institutions this ratio stands between 30% and 100%. Another 5% of the participants have a ratio between 10% and 20%.

It is important to notice that most of the «big» Banks have small Ship Finance portfolio ratio as they may be heavily exposed in other cyclical industries such as Industry, Sales, Real Estate, Energy, Aviation etc.

| Question |
| --- |
| In which activities of Ship Finance is your institution involved? |

Almost all (95%) participant institutions are involved in Conventional/Mortgage Ship finance, while a great number of them (63%) are also involved in Corporate financing. Equally 36,8% are involved in Equity and M&As while 26.3% are involved in Leasing and in NPLs.



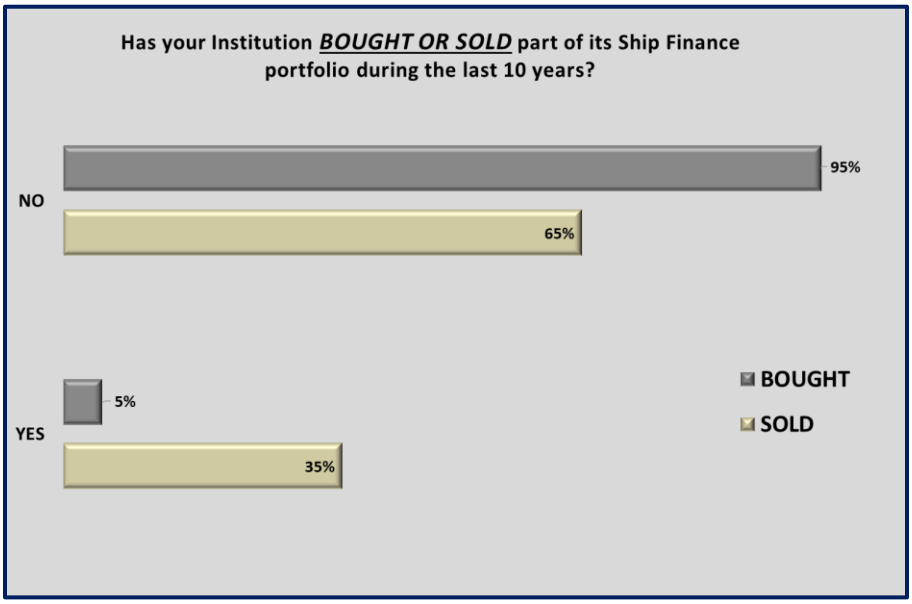

| Questions |
| --- |
| Has your Institution sold part of its Ship Finance portfolio during the last 10 years? |
| Has your Institution bought part of its Ship Finance portfolio during the last 10 years? |

While only 5% of the participant institutions have bought Non Performing Loans ("NPL"s) from other institutions, 35% have sold part of their Ship Finance portfolio during the last 10 years. The amounts or the percentage of the NPLs transactions on their total Ship Finance portfolio were not disclosed.

According to a 3Q18 deleveraging report published by Deloitte, some EUR 16.8bn and USD 3.3bn in shipping deals have come to the market since 2012 from the UK, France, Germany, Italy, and Greece. Those shipping NPL deals have included non-performing loans, performing loans as well as mixed performing and non-performing loan packages, according to the report.

Since then, an additional amount close to EUR 13bn of non-performing shipping-related loans have come to the market as German and Greek banks attempted to clean up their balance sheets due to continuing pressure from European Commission and European Central Bank requirements.

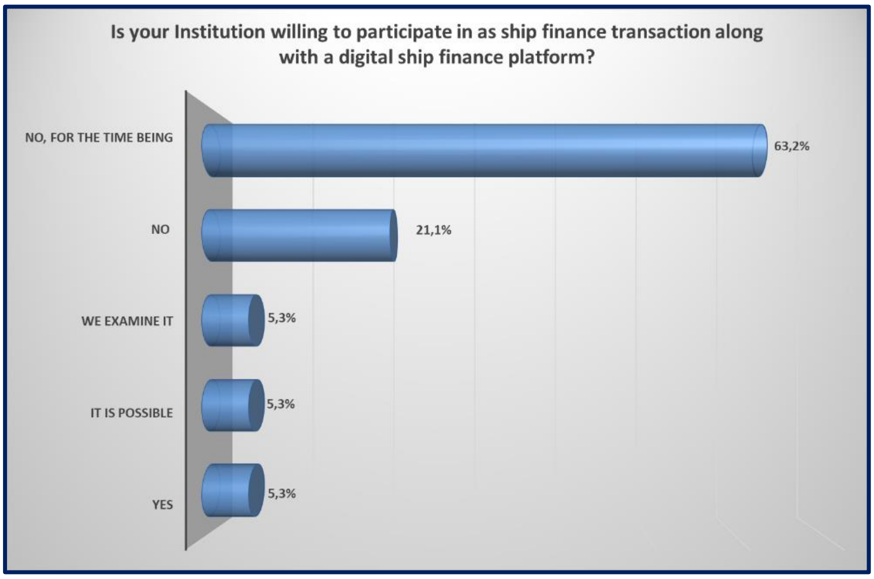
As analysts claim, the hedge funds are more interested in shipping debt rather than in equity since the upside potential in equities is limited. The truth is that as long as bank lenders reduce their exposure in shipping or have decided their exit, more hedge funds will enter the market.




| Question |
|---|
| Is your institution willing to participate in a ship finance transaction along with a digital ship finance platform? |

One of the new tools in the financial market is the emergence of new forms of financing through digital platforms where investors have the right to choose among the borrowers and the characteristic of the projects, presented in the platform, they wish to invest while borrowers enter in order to attract investors / financiers.

Most institutions (63,2%) are not willing to participate in a ship finance transaction along with a digital ship finance platform for the time being, while 21% clearly states that they are completely negative. Only 16% considers this issue as a possibility.



# PART 2: SHIP FINANCING REQUIREMENTS

| Questions |
|---|
| Do you prefer financing new building vessels, second hand or both? |
| Regarding newbuilding financings is your institution advancing pre-delivery finance only? |

Concerning the financing only of the pre-delivery stage, just 5% of the participants replied positively, and 39% negative. It seems that institutions have realized that the oversupply of vessels experienced in the past, remains a threat for the market. The rest of the participants equally prefer to finance either secondhand tonnage (47,5%) or both secondhand and new building tonnage (47,5%).

| | |
|---|---|
| Second Hand | 47% |
| Both | 5% |
| New Building | 47% |

| | |
|---|---|
| Pre-and Post Delivery is available | 56% |
| No | 39% |
| Yes | 5% |

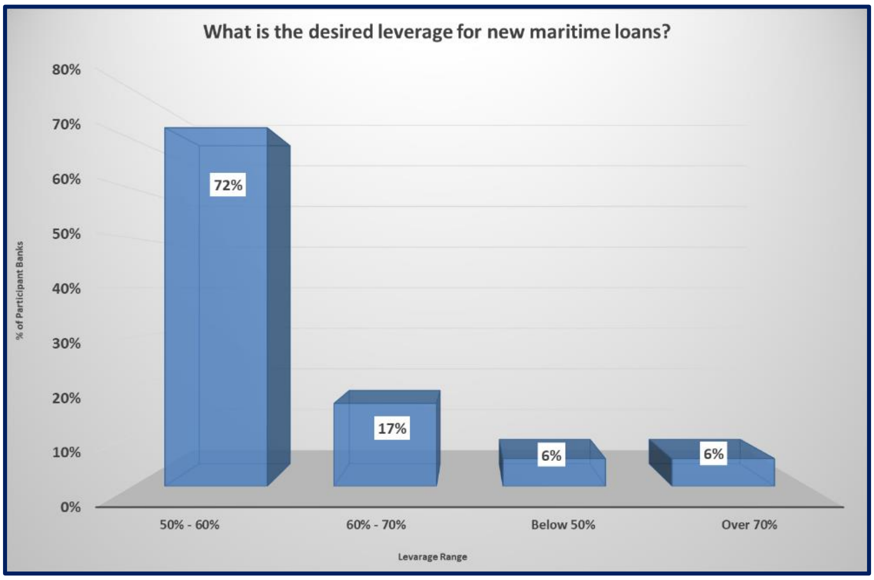
| Question |
|---|
| Which sector/s do you prefer to finance? |

The specific question addresses the issue of lenders' preference in sector activity. Tanker and Dry Bulk sector share almost the same percentage (27% and 26% respectively) with Container sector following with 22%, while 14% of the institutions are willing to finance LNG/LPG. The most specialized sectors were left out of lenders' preferences.

| | |
|---|---|
| **Tankers** | **28%** |
| **Dry bulk** | **26%** |
| **Containers** | **22%** |
| **LNG/LPG** | **14%** |
| **Specific project's characteristics more important compared to sector** | **5%** |
| **Offshore** | **2%** |
| **Cruise** | **2%** |
| **Ferry** | **2%** |

| Question |
|---|
| What is the desired leverage for new maritime loans? |

This is another question which reflects institutions' desired exposure to new maritime loans and has been also answered from all participants. The vast majority of the lenders i.e. 72%, prefer an exposure between 50% and 60% while another 16.7% prefers an exposure between 60% and 70%. About 11% of the respondents are equally split in two groups of 5.6% each, with the first group preferring financings of less than 50% and the other group financings of over 70%. Undoubtedly, the participants' desired leverage depicts their willingness to see more equity in place for each project and a cautious stance in the development of their shipping loan portfolios. We also note that the desired loan leverage does not depend neither on the institutions' country of origin nor on their size.




| Question |
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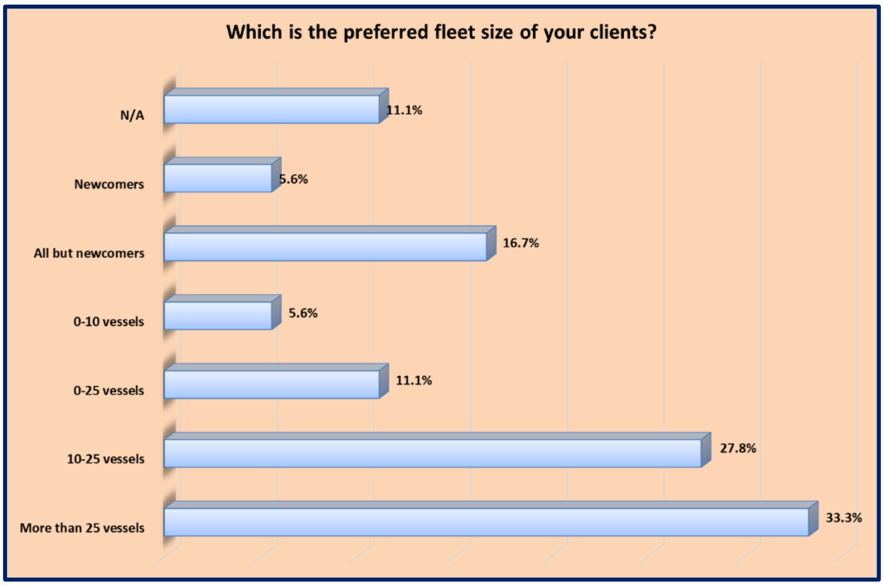
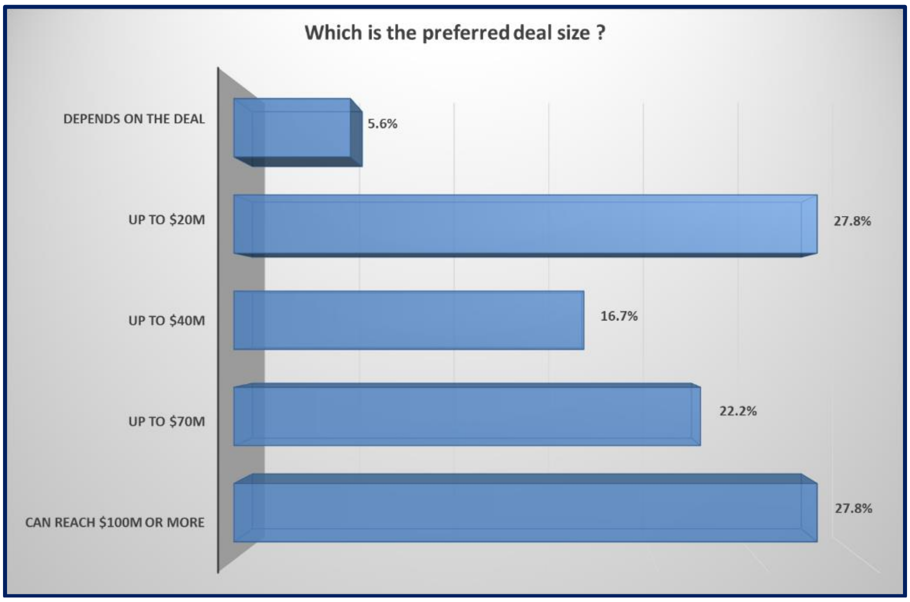
| What is the preferred fleet size of your clients? |

The fleet size of the potential borrower, matters. The preferred fleet size for the institutions' clients is clear, since 60% of the financiers prefer a fleet size of more than 10 vessels and 33% prefer a fleet size of more than 25 vessels. To the contrary less than 10% of the institutions are ready to finance newcomers and/or shipowners with less than 10 vessels.




| Question |
|---|
| What is your preferred deal size ? |

As seen institutions vary in their willingness to provide different loan amounts. It is worth noting that there are two groups of 27.8% each with one preferring to lend amounts of up to \$20m and the other one reaching the amount of \$100m or more. On another note, 22.2% of the participants prefer loan amounts of up to \$70m and another 16.7% prefer loan amounts of up to \$40m.




| Question |
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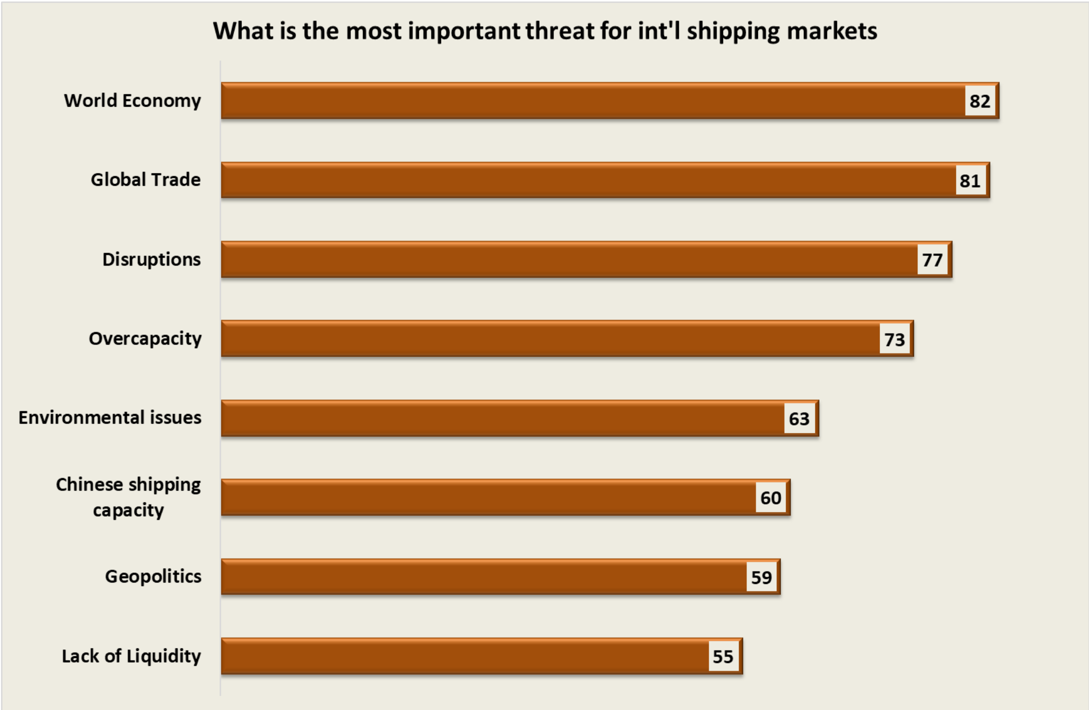
| What is the most important threat for int'l shipping markets? |

This question wishes to depict which is the most important threat for international shipping markets. As seen, the major threat with a score of 82 is the World Economy closely followed by Global Trade with a score of 81. Disruptions is ranked third (score 77) for reasons we all understand following the Covid-19 issue, while Overcapacity, which scores 73 reaffirms that it creates a major obstacle for a healthy upturn at least in the core shipping sectors. The option of Environmental Issues scored 63 followed by Chinese Shipping Capacity (60), Geopolitics (59) and Lack of Liquidity (55).



# *PART 3: THE PANDEMIC NORMAL*

| Question |
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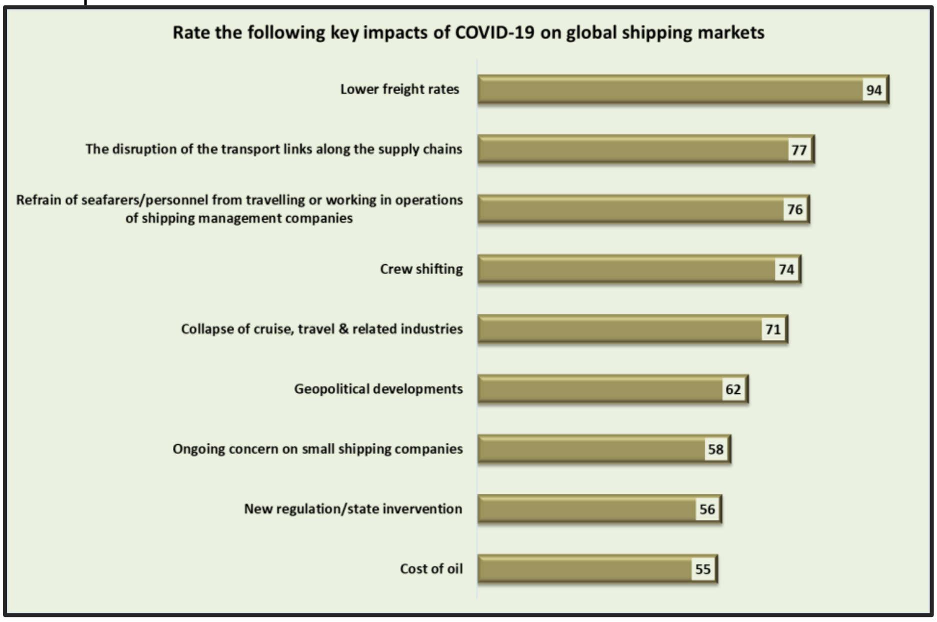
| Rate the key impacts of COVID-19 on global shipping markets |

The third part of the Survey tackles the Pandemic Normal as international shipping and trade have been hit hard by the spread of the Covid-19 pandemic. Significant key impacts are evident in shipping such as the physical delivery of cargoes, the chartering and purchase of ships, the physical delivery of ships, the change of crew and even the inspection of ships. Transportation to and from China has been hit, freight rates have fallen to low levels, and oversupply is making the whole market difficult. Likewise, all trading partners were disrupted irrespective the geographical location and commercial activities in the maritime sector were interrupted.

In the first question respondents were asked to rate some key impacts on global shipping markets. Lower Freight Rates was considered to have the highest impact (score 94). Lenders show interest on the payback tool of loans, which is the freight rates. The tankers that have not experienced the same disruption from the pandemic, have witnessed the crude oil price crash that offered them business opportunities in the storage and trading activities.

The disruption of the transport links along the supply chains has been ranked second (score 77). As emerging market economies have steadily come to account for a greater proportion of global GDP, goods often must go through more stages before reaching the end consumer. From national lockdowns to closed airspace and borders, Covid-19 has resulted in unprecedented disruption of the mechanics for most economies, regardless their size or stage of development.



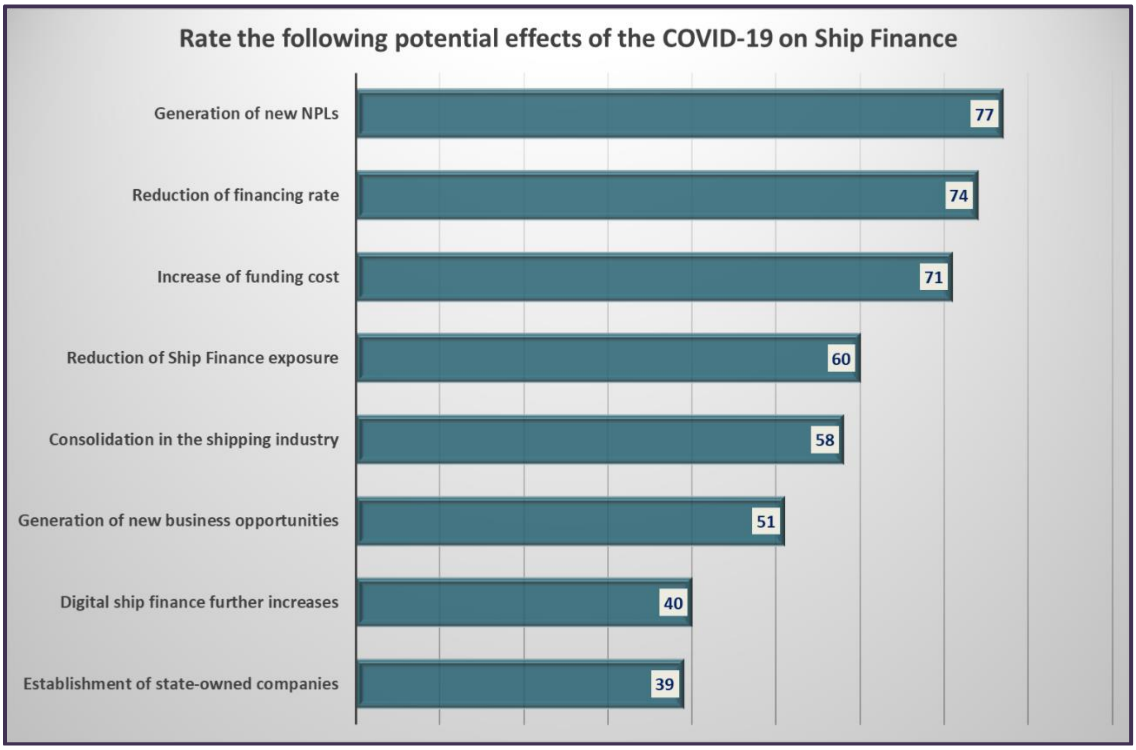

Another interesting factor, with a score of 76, is the refrain of seafarers/personnel from traveling or working on maintenance or other operations of shipping management companies and related industries. The imposed restrictions intended to keep the virus at bay, have proven to disturb crew mobility and operations. Crew shifting (score 74) confirms the case.

Other key impacts rated of medium importance, are the Collapse of Cruise, Travel and related industries, Geopolitical developments, Ongoing concern on small shipping companies and New regulations/state intervention. The Cost of Oil has the lowest impact and is ranked last. In fact, the low price of oil has been a sustainable factor to shipping industry during the pandemic.

| Question |
|---|
| Rate the potential effects of COVID-19 on Ship Finance |

The next question is more specialized to the Lenders, as they were asked to rate the potential effects of the Covid-19 crises on Ship Finance. The worse effect on Ship Finance according to the participants of the Poll is the Generation of new NPLs (score 77) which continue to pose risks to economic growth and financial stability. By the end of 2019 Shipping finance was still attracting investors' interest, with German banks reducing their non-performing exposures (NPE) in the category. Although this was expected to continue, given the significant volumes of shipping loans also held by Nordic, Dutch, and Greek banks, the new pandemic normal is changing the plans.

Second potential effect on Ship Finance is ranked the Reduction of the financing rate (score 74), which as mentioned in previous questions is between 50%-60%, followed by the Increase of Funding Cost (score 71). These two effects provide sufficient evidence that the growth of the global fleet continues to be funded from non-banking sources. As the vast majority of vessels are financed from different sources, the shift from banking to non-banking sources is quite prominent. This explains Lenders' response on ranking the Reduction of Ship finance exposure 4th (score 60).
The rest of the factors are ranked by Lenders as follows; Consolidation in the shipping industry (score 58), Generation of new business opportunities (score 51), Increase of the Digital ship finance (score 40) and Establishment of State-owned companies (score 39).



| Question |
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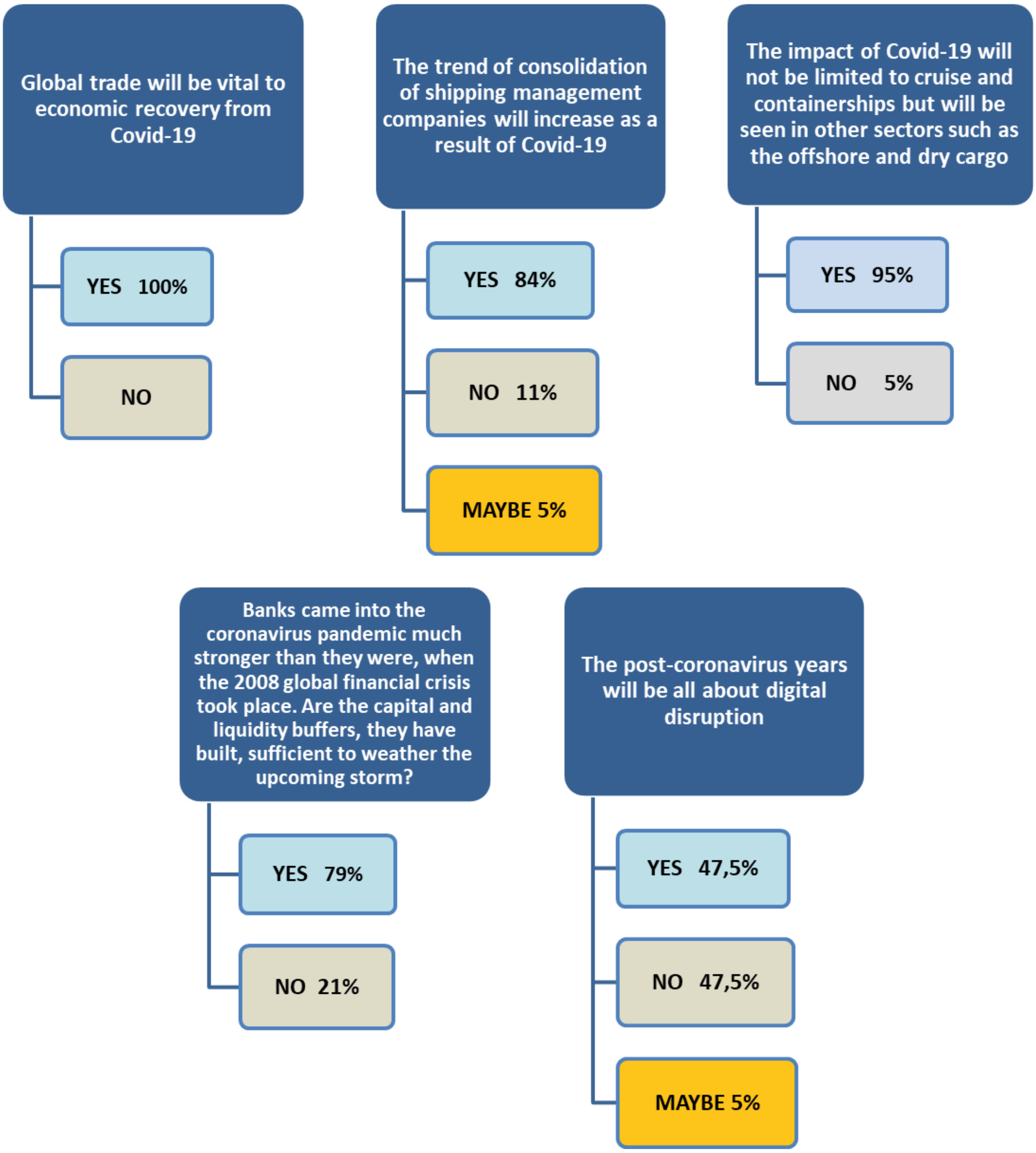
| Do you agree with the following public statements? |

The third part of the Poll concludes with some public statements Lenders were asked to agree or disagree.



## *Conclusions*

The recent pandemic has alarmed the global business community with the maritime industry being among the first industries to experience the side effects, since it always acts as a barometer of the economy at any level, whether local or global. Increased volatility levels on the lower side of the spectrum for trade and freight rates has shifted the attention of all stakeholders on rethinking their strategies at operating and tactical levels with financing being at the core of the attention.

Over the course of the last few months, with the dramatic plunge in oil prices and increased concern on the impact of COVID-19, the need for shipping financiers and owners to consider its implications on the financing agreements has become even more demanding. Before the virus took place, we had witnessed challenges faced by the industry with IMO 2020 and the upcoming maturities on facilities standing out. To add further to these challenges, COVID-19 and the oil price deterioration means we are expecting to see real challenges for the shipping sector in the next few months.

The present survey focuses on the understanding financial institutions, and more specifically banks, have on the current developments and how they perceive the future will be for their operations. Among the key takeaways are:

- Shipping as a predominantly global industry, is not considered a key economic activity for most European countries, thus it is not core business for most banks. In addition, the most active banks in shipping, which are mainly European, suffer from the cost of financing which is entirely dependent on the USD and not on the currencies of the countries of operation (Euro, GBP, SF). Central banks and various regulators request high collateral levels in credit assets, forcing banks to prefer exposure to sectors of the economy where risk is manageable.
- Shipping industry is too «small» for Financiers, compared to other industries, and necessitates heavy specialization. Certainly, for those who do not have a specialized unit or a medium/long term presence, the specific industry is considered to be very demanding and of high-risk, which is significantly «penalized» by Basel's regulations.
- The tax-free investment schemes of the KGs have heavily affected the global maritime financing market. This financing policy of the German shipping companies, blessed by the German state, have put in danger the traditional shipping financing imposing noncompetitive bailout processes without precedent.
- The market has been equally affected by the inflated opportunistic and promising investment or exposure to the off-shore industry and suffered unbearable losses since the collapse of oil prices in the last decade.
- The resulting increase in NPLs prompted the European Central Bank (ECB) to carry out an in-depth review of European banks' shipping loan portfolios, leading many of the banks to strategically reassess their exposure and commence deleveraging. This has been met by an increasing appetite for increasing shipping finance presence from Chinese banks and leasing companies and the simultaneous exit of many European and British institutions.
- Greek banks continue their support in shipping proving their resilient performance despite continuing domestic problems, underlining their commitment to shipping. The fact is that the accumulated experience, the conservative strategy, and the effective control by the Central Bank of Greece prevented the expansion of losses in the Greek shipping banks financing market. Instead, shipping finance proved to be a secure business sector creating safe profitability.
- Lenders prefer to finance clients with big fleets. This fact condemns smaller companies to deal with the deficiency of financing, obliging them to face new challenges in order

to confront their high cost structure. In order for these companies to leverage new technology capabilities and achieve cost optimization as well as a new competitive advantage, are required to introduce digital-oriented leadership in combination with a technology-oriented company culture, as key determinants to their survival and success. Thus, two main questions arise; Can they cope with the industry transformation? Do they have the financial ability to shift their philosophy and business mindset?

- Many Banks have sold their Shipping NPLs to funds and it seems that a new wave of bad loans is on the way. Lenders' main concern according to the Survey, is the generation of new NPLs. Most of them are expected to originate from recently restructured loans which will turn nonperforming again. This means that the main job of banks and services in the coming months, will be to contain the spread of bad credit.
- It is more than certain that financial institutions and especially banks need experienced personnel capable of handling difficult cases in order to avoid the creation of new Non-Performing Loans. On the other hand, shipowners should be able to understand the current trends carefully and take appropriate actions.
- The participants in the Survey foresee further consolidation in the shipping industry across sectors. It is obvious that Lenders are not available to discuss new projects with newcomers. This can apply in the local markets such as Greece and Scandinavia where a significant number of banks continue to finance new names.
- Financiers involved in sectors related to tourism and public interest such as Cruise and Ferries as well as Ports will also confront difficulties. Chinese banks and Leasing companies having high exposures in these sectors of the maritime industry will have to set new emerging landscapes. The absolute collapse of Chinese leasing companies and banks' new financing foreign companies, after the pandemic, on the one hand jeopardizes the smooth running of the shipping finance industry but on the other hand it is an opportunity for alternative financing products.

Financial institutions and especially banks need to look into their digital transformation strategies especially since they foresee further consolidation in the shipping industry across sectors. If they do not act now, the dinosaur effect will hunt them trimming their profit margins to levels where they will strangle with competition. Now is the time to re-adjust the existing business models since there is a consensus on the healthy state bank institutions are at present. They can take advance on their current privileged stage and invest in new solutions. Moreover, the process of identification of European banks with the respective banking organizations of the West is a one-way street. We must expect developments towards this direction in the industry, which will then affect other organizations in Asia that may play a major role in ship financing.

In these unprecedented times, the ability of maritime transport to continue undisrupted the transport of food, energy and medical supplies across the continents will play a critical role in overcoming the pandemic. To this extent governments and central banks have realized that they must support maritime transport that has an essential role to play in growth and sustainable development. At the same time both shipping companies and their Lenders will need to become agile and adaptable to this changing situation and focus on building effective and responsive strategies and plans.

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