



MARITIME INSTITUTE OF MALAYSIA

# “SHOW ME THE MONEY!” THE MALAYSIAN SHIP FINANCING SCENE



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## PRESENTATION OUTLINE

- ➡ Features of shipping industry
- ➡ Global trends in ship financing (SF).
- ➡ State of play in SF in Malaysia.
- ➡ Lenders' perspectives.
- ➡ Borrowers' perspectives.
- ➡ Bridging the gap between borrowers and lenders
- ➡ Towards a more dynamic SF scenario in Malaysia

# FEATURES OF SHIPPING INDUSTRY

- ➡ Capital intensive
- ➡ High risk – low return
- ➡ Competitive
- ➡ Globalized
- ➡ Conflicting time horizons
- ➡ Volatile, cyclical markets
- ➡ Subject to stringent regulations
- ➡ Increasing public profile

# MALAYSIAN SHIPPING INDUSTRY

- ➔ Huge demand for shipping services
- ➔ Ships carry 95% of nation's trade.
- ➔ MISC dominates energy carriage.
- ➔ Cabotage Policy protects local players.
- ➔ Few local players in int'l liner trade.
- ➔ 90% of maritime trade carried by foreign shipping lines.
- ➔ Shipping lines slowly upgrading fleet from single-hull to double-hull vessels.

## MALAYSIAN SHIPPING INDUSTRY

- ➡ More than 100 shipping lines (foreign and local) calling at local ports.
- ➡ Local ports are linked to around 200 ports worldwide.
- ➡ Foreign lines are represented by locally incorporated ship agencies and owner's representatives.
- ➡ Most local lines are MASA members.
- ➡ Most foreign lines are ISOA members.

## GLOBAL TRENDS IN SF

- ➡ Increasing demand for SF worldwide.
- ➡ Pressure to replace old tonnage.
- ➡ Shift away from debt financing to leasing structures and equity.
- ➡ Impacts of developments i.e. Basel II, MARPOL, double-hull ruling on SF.
- ➡ Rise in ship prices / freight rates driving owners to seek alternative financing.
- ➡ German KG – biggest source of leasing capital to global shipping.

## STATE OF PLAY OF MALAYSIAN SF

- ➡ SF scene not very vibrant. Few local financial institutions (FIs) are involved.
- ➡ Government financing via Shipping Fund.
- ➡ Asian financial crisis impact looms large.
- ➡ Shipping companies say banks aren't supportive of the industry.
- ➡ Banks say internal / external controls, lack of exposure to shipping hamper lending.
- ➡ Rising demand for alternative financing.

# SOURCES OF FINANCING

- ➡ Commercial / merchant bank lending
- ➡ Leasing
- ➡ Government funding
- ➡ Equity financing
- ➡ Bond financing
- ➡ Venture capital
- ➡ Offshore financing
- ➡ Regional financial institutions



## BANK LENDING

- ➡ Single tranche term loans by commercial banks most common.
- ➡ Loans either syndicated or bilateral.
- ➡ Tenure rarely exceeds 7 years for newbuilds, 15 years for secondhand vessels, shorter terms for ships with limited useful lives.
- ➡ Secondhand ships easier to finance.
- ➡ Usually secured by a mix of mortgage, covenants, guarantees & assignments.

## LEASING

- ➡ Not widely used but gaining popularity in corporate finance structures.
- ➡ Emergence of Islamic SF leasing structures based on Al-Ijarah concept.
- ➡ Advantages : Off-balance sheet treatment, capital cost reduction.
- ➡ Disadvantages : long tenures, complex structures, tax liabilities.

## GOVERNMENT FUNDING

- ➡ RM1.3 bil. Shipping Fund launched in 1992, plus another RM1 bil. in 2000.
- ➡ Development financial institutions i.e. Bank Pembangunan, Bank Rakyat, BSN, MECIB, Exim Bank.
- ➡ Operating, construction, scrap-and-build subsidies
- ➡ Tax and depreciation allowances
- ➡ Customs duties and levies.

## EQUITY FINANCING

- ➡ The biggest shipping companies listed on Bursa Malaysia i.e. MISC, Halim Mazmin, PDZ, MMM, Maybulk, Global Carriers, Nepline, Alam Maritim, Coastal Contracts.
- ➡ Advantages : high profile, easy to raise financing from shareholders once listed.
- ➡ Disadvantages : high listing fees, subject to takeover, strict disclosure.

## BOND FINANCING

- ➡ Conventional and Islamic bonds being raised to repay borrowings, finance vessel purchase etc.
- ➡ Advantages : Allow companies which cannot get loans from banks to raise financing, improve cashflow, ease of covenants compared to bank loans.
- ➡ Disadvantages : Coupon rates higher than interest rates of bank loans.

## VENTURE CAPITAL

- ➡ Global Maritime Venture set up in 1994 to provide venture capital fund to local shipping companies.
- ➡ Government provided RM500 mil. Shipping Venture Fund from the RM1.3 bil. Shipping Fund.
- ➡ Private venture capital firms also give out small amount of SF loans.

## OFFSHORE FINANCING

- ➡ Labuan IOFC growing in popularity.
- ➡ Offshore banks provide mostly debt financing i.e. term loan, syndicated loan, bridging loan, project loan, letter of credit, working capital.
- ➡ They also provide equity financing (in US\$), sponsor / underwrite debt and equity instruments.
- ➡ Cheaper, less stringent compared to banks.

# REGIONAL FINANCIAL INSTITUTIONS

- ➡ Islamic Development Bank (IDB).
- ➡ Asian Development Bank (ADB)
- ➡ Japanese Bank for International Cooperation (JBIC).
- ➡ Overseas Economic Cooperation Fund (OECF) of Japan.



## LENDERS' PERSPECTIVES

- ➡ Many FIs are still cautious about the shipping sector despite its purple patch.
- ➡ Shipping is not a priority sector for most FIs.
- ➡ Some FIs are stigmatized by past experience in SF.
- ➡ To FIs, clients' creditworthiness, earnings potential and repayment ability are paramount in determining financing of shipping deals.

## LENDERS' PERSPECTIVES

- ➡ Strong cashflow, balance sheet & track record of applicants are paramount.
- ➡ Challenges for FIs : cost control, revenue diversification, improvement of asset quality, high earnings margins.
- ➡ Internal and external regulations restrict participation of local FIs in SF.
- ➡ Some FIs feel certain booming shipping sectors like O&G worth a serious look.

# LENDING CONSIDERATIONS

- ➡ Financial standing and track record
- ➡ Ability to service debt
- ➡ Single customer limit
- ➡ Flag of convenience
- ➡ Collateral / guarantees
- ➡ Type of registry
- ➡ Industry development
- ➡ Risks involved

## RISKS INVOLVED

- ➔ Credit / financial risk
- ➔ Market / business risk
- ➔ Timing risk
- ➔ Sovereign risk
- ➔ Security risk
- ➔ Residual value risk
- ➔ Legal risk
- ➔ Operating risk

# RISK MITIGATION

- ➡ Ship mortgage
- ➡ Assignments – earnings / insurances / contracts / proceeds
- ➡ Guarantee / indemnity
- ➡ Pledging of assets, deposits, shares
- ➡ Debenture
- ➡ Covenants

## METHODS OF APPRAISAL

- ➔ Net present value (NPV)
- ➔ Internal rate of return (IRR)
- ➔ Cashflow / discounted cashflow
- ➔ Discounting methods :
  - Annual capital charge
  - Growth rate of return
  - Discounted profit ratio
- ➔ Payback period
- ➔ Asset valuation

## BORROWERS' PERSPECTIVES

- ➡ Shipping companies perceive local FIs as lukewarm towards SF.
- ➡ Small shipping companies say local banks' demands are too stringent.
- ➡ A chicken-egg situation persists as banks will only lend money to solid companies.
- ➡ Shipping companies feel the current 'it takes money to borrow money' situation is not helpful to boost SF.

# BORROWING CONSIDERATIONS

- ➡ Demand and supply elasticity
- ➡ Fleet upgrading / expansion
- ➡ Maritime trade pattern
- ➡ Opportunity cost of investments
- ➡ Shared ownership of vessels
- ➡ Rate of scrapping of vessels
- ➡ Legal framework
- ➡ Availability of competitive financing



# WHAT BORROWERS WANT FROM FIs

- ➔ Greater focus on customer needs
- ➔ Long, flexible tenure
- ➔ Competitive interest rates
- ➔ Speedy processing of applications
- ➔ Greater financing flexibility
- ➔ In-house shipping industry experts
- ➔ More diversified financing structures

## SUMMARY OF MALAYSIAN SF SCENE

- ➡ Shipping companies want greater support from FIs and want them to improve knowledge on shipping.
- ➡ Malaysia's SF scene needs to go beyond 'plain vanilla' financing.
- ➡ Some FIs are cautious but feel the sector currently warrants attention.
- ➡ Past experience counts!
- ➡ Banks will lend to deserving applicants.

## BRIDGING THE GAP BETWEEN BORROWERS AND LENDERS

- Understanding b/w shipping companies and FIs is vital to boost local SF.
- FIs need to evaluate shipping fairly.
- Shipping companies must strive to put up strong case to qualify for financing.
- There must be a balance between financial and shipping markets.
- Vibrant SF generates multiplier effects to maritime sector, trade & economy.

## TOWARDS A MORE DYNAMIC SF SCENARIO IN MALAYSIA

- ➡ Consolidate shipping companies.
- ➡ FIs must change views about SF.
- ➡ Make available alternative financing
- ➡ Emulate best practices of leading SF nations.
- ➡ Enhance ancillary services i.e legal, insurance, consultancy.
- ➡ Put in place strategy to boost local SF.

*“NO FUNDS, NO FUN!”*





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# THANK YOU

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