INSTITUTE OF CHARTERED SHIPBROKERS

MONDAY 8TH MAY - MORNING

SHIPPING FINANCE

Time allowed – three hours

Answer any FIVE questions – all questions carry equal marks

Please read the questions carefully before answering

1. Felix Shipping is a company which has a significant amount of debt in its capital structure, raised through bond issues several years ago which are due to mature within the next couple of years. Interest on these bonds must be serviced before any other distributions are made. The company wants to expand its fleet through purchases in the second hand market, raising the capital required through equity. The Chief Executive Officer (CEO) informs you that he has concerns about such an issue. First, although Felix is a large company in terms of the number of vessels under its control, it is a family-owned business. He does not want dilution of control, and does not want a new group of shareholders 'sticking their noses into his business'.

   He has informed you that the company has oil transportation contracts with certain conflict-torn countries which would be embarrassing if they were to be disclosed. If the company goes for an initial public offering on the New York Stock Exchange, details of these contracts must be 'kept off the books' and should not be disclosed in any marketing material or prospectus.

   The CEO is also concerned that recently the market entered a period of declining freight rates; the company's earnings are anticipated to fall as a consequence. Accordingly, an issue of ordinary shares may not be sufficiently attractive to investors. He has asked you to make suggestions as to alternative types of equity which may be offered to potential investors. As an alternative, the CEO has asked you to advise on the advantages and disadvantages of a private placement as a way of raising the required equity.

   Advise the CEO with regard to each of the matters which he has raised with you.

2. Answer **<u>ALL</u>** parts of the question.
   Explain each of the following loan facilities, including risks to each party, identifying at which stage of the shipping cycle they are suitable.
   a) Front end loan
   b) Back end loan.
   c) Moratorium loan
   d) Bullet repayment loan.

PLEASE TURN OVER

3. Discuss the financial reasons, as opposed to operational reasons, why shipping companies fail, and what steps may be taken to avoid these before corporate failure occurs.

4. You are the loan application appraisal officer at a ship finance bank. Pegasus Shipping owns several oil tankers and recently purchased two high tech reefers. The tankers are over twenty years old and have been worked hard during a recent boom. They are 'dirty ships' in terms of their sulphurous emissions. The reefers are registered in Panama and the tankers in a politically unstable country. Your research indicates that one of the reefers was recently involved in a collision at sea but details regarding the outcome of court proceedings have been impossible to find. It is intended that the tankers will be redeployed from African waters to be traded in waters around the European Union. One of the reefers is employed under a time charter with a strong international agricultural company, but the other has been employed on very short term voyage charters. Two of the tankers have been paying ever increasing insurance premiums because of their badly maintained condition, and yet the company has not as yet done anything to remedy the faults which have led to this increase.

   Discuss the factors which you would take into account as a lender to Pegasus when making an analysis of its vessels from a collateral or security perspective.

5. Answer **BOTH** parts of the question.
   a) Discuss the factors which are taken into account when making a customer analysis for a loan application.
   b) Describe the importance of character, capacity and capital when making a loan application evaluation, and to what extent each of these may be affected by the different phases of the shipping cycle.

6. Answer **ALL** parts of the question.
   In the context of a typical shipping finance loan agreement, discuss the contents and purposes of all of the following:
   a) Negative pledge
   b) Events of default
   c) Security cover
   d) Provision of information
   e) Ship's name and registration

7. Identify and discuss the main provisions found in a typical registered ship finance mortgage.

8. 'Shipping finance is not a static concept. The debt-equity structure must be kept under constant review to ensure the balance between the two reflects changes in the cycle and ever-changing investor sentiment'. Discuss.