MARINE TECHNOLOGY NEWS

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Marine Finance for Brown Water Operators

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A primer for navigating the 'ups and downs' of marine money for domestic

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stakeholders.

Vessel financiers are resourceful and adaptable to changing markets. On the domestic side, financiers of Jones Act and "brown water" assets have continued to serve their customers through shifting shoals in both broader capital markets and in the marine markets – both known for their ups and downs. Marine finance can take many forms. In the broadest sense, funding can be done through loans, where the vessel is owned by the borrower, or through leases, where an institution owns the equipment and charters out it out to the customer (sometimes for the life of the equipment).

Marine Money & its Origins

Companies with larger balance sheets, approaching $1 billion of asset values, and more, are able to tap into money center bank credit markets through syndicated loans (which might be term loans or revolving credit), from syndicates of major banks, or, more recently from institutional investors (these are called "Term Loan B").

For example, Kirby Corporation, a public company, reveals in a 2017 regulatory filing: "The Company has a $550,000,000 unsecured revolving credit facility ("Revolving Credit Facility") with a syndicate of banks, with JPMorgan Chase Bank, N.A. as the administrative agent bank, with a

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maturity date of April 30, 2020 … As of March 31, 2017, the Company … had $177,535,000 of debt outstanding under the Revolving Credit Facility." Kirby has also been able to tap debt capital markets, and its filing notes that: "The Company has $500,000,000 of unsecured senior notes ("Senior Notes Series A" and "Senior Notes Series B") with a group of institutional investors, consisting of $150,000,000 of 2.72 percent Senior Notes Series A due February 27, 2020 and $350,000,000 of 3.29 percent Senior Notes Series B due February 27, 2023. No principal payments are required until maturity."

Another well publicized loan deal in recent years, this one with equipment providing security, was Moran Towing & Transportation's senior secured revolving credit facility, which closed in mid 2014. Investment bank Merrill Lynch Pierce Fenner & Smith was the lead arranger in $450 million syndicate with Bank of America, N.A. acting as administrative agent for the group that participated in the deal.

Most recently, in mid June 2017, Hornbeck Offshore announced that it had refinanced a $200 million senior secured revolving credit facility set to expire in February 2020 with a new "first lien" credit (described as providing up to $300 million of term loans) maturing in June, 2023.

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Term Loan B deals have characteristics of loans (with some repayment of principal along the way) but may also exhibit bond-style "bullet" amortization (where much of the principal is repaid at maturity). During a 2013 expansion phase, Harvey Gulf International Marine refinanced existing loans and raised approximately $1 billion of credit- that included $600 million of Term Loan B debt.

Larger (balance sheets of $1billion+) non-listed outfits may also seek capital from Private Equity (PE) investors. Harvey Gulf went this route in 2008, when a "middle market" PE house Jordan Company (packager of the "Resolute" private funds), took a majority position in Harvey Gulf to help fuel its transition from a towing outfit to an offshore service provider. Paducah-based Marquette Towing has benefited from multiple investors from the PE sector. In early 2015, KRG Capital Partners, a middle market specialist with a liking for "platform" companies, sold its interest in Marquette, onward to another investor – in this case, BDT Capital Partners, LLC, a private equity arm of Chicago-based BDT & Company, LLC. At the time of the deal, BDT pointed to a long term horizon to fund growth, alongside the Eckstein family, for Marquette Towing. In a theme which runs throughout this article; industry expertise really matters, and it is here where the Richmond, VA office of Harris Williams & Co. (a boutique investment ba

nk with a specialty in transportation, logistics and distribution companies) was instrumental in structuring this deal.

Smaller Companies

Key Equipment Finance, part of Cleveland based KeyBank NA, has been in business since the early 1970s. Paolo de Alessandrini, Senior Vice President at KeyBank, based in the Great Lakes region, told *Marine News* that his team: “knows the industry and the equipment, we are experts.” Asked about the longevity of the equipment finance business – Key Equipment Finance (KEF), he said: “We are very careful about our client selection. Credit metrics are critical; they drive the risk profiles.” KEF’s Director of Commercial Marine Finance, Ronnie Evans, based near Baton Rouge, emphasized this point, saying “Credit is the driver behind today’s market, and amortization [the length of time in which a loan is paid back] drives many credit decisions.”

Separately, Walter Rabin, President and CEO of Signature Financial (wholly owned by Signature Bank), a veteran of the business, explained the trade-offs between the asset and the corporate side of lending. Active in the finance of inland, coastal and equipment used in harbors, Signature Financial provides both loan and lease finance. They are “… guided by what our customers want,” according to Mr. Rabin. Five years after moving over with a team from another bank,

his group now numbers more than 100 people.

In a practical rather than legal sense, the lines between leases and loans may blur; for example, a term loan for an asset's entire value (or nearly), over a lengthy time period, may have similar impacts as a lease transaction. KEF's Evans emphasized the point, saying, "Most clients would like to finance for as long as they can; on new assets, we typically see tenors of 7 to 10 years. But the amortization profile, which determines the balloon to be repaid at the end, is also important. It's a big part of the credit underwriting."

Signature Financial's Rabin offered some insights into the considerations that go into lending decisions. He explained, "Similar to other types of equipment finance, we need to think about the financial profile of the client," with the latter touching on issues of corporate credit. Cautioning that each deal has its own wrinkles, he continued, "We start by looking at the value of the asset, considering the structure, the term, amortization profiles, and of course, we look at exits; asking ourselves what steps we might take if something goes wrong." But banking is all about relationships – knowing the customer and its business, as well as the industries they serve. Rabin adds, "We look at borrower, how long they've been in business, and, if there's a charter, we look at

the relationship with the client's customer."

One Size Does Not Fit All

Cookie cutters don't have a place in marine financing. Evans told *Marine News*, "Each deal is a little different." Paolo de Alessandrini chimes in, "As we look at deals, we see increasing opportunities for structured transactions which may go beyond regular credits. These transactions are more complicated than plain vanilla loans between a borrower and one bank and there could be an asset finance component. That's where you need knowledgeable people."

Citing deals where a Signature Financial client's newly constructed equipment might be on a lengthy charter to a utility (or similar), Mr. Rabin said, "We may look through to the credit of the end-user customer, and ultimately get an assignment of the contract. Sometimes we are able to work with a client to create a sounder transaction structure, which may include being paid monthly first through an intercept payment … not always, and it's not a hard request, but sometimes it makes sense." He reminded *Marine News*, "Of course, this won't work on a three-year contract on an asset with 10-year life."

Signature Financial's Walter Rabin continued on: "On newly constructed equipment for a good borrower, we might lend with a 10-year term, with up to 20-year amortization,"

which would leave a balloon payment at the end of the loan term. On advance rates, he said, “For the strong borrower, we could typically lend up to 100 percent on new asset. If the credit is not so good – we may ask for 10 percent down.” Asked about financing second-hand equipment, he mused that, “There is art mixed in with science here; while we are much more cautious on used equipment, we have plenty of industry knowledge that we have leveraged to make appropriate decisions on these types of deals. We may finance based on a 20-year amortization profile for very long-lived assets, and we’d rarely advance more than the orderly liquidation value, which would likely be less than the fair market value (FMV) from a recorded sale.”

As far as trends in the marketplace, the KeyBank team pointed to caution related to vessels serving the oil industry. Evans said that banks were closely monitoring deals that had been inked in that sector. He also said that leasing is not as common as it used to be but he noted that customers were increasingly showing a preference for lease deals in situations where their business was in the red. “If they are experiencing losses, they can’t really use the depreciation. So they can pass the tax benefits of depreciation off to a lessor, and benefit from a lower interest rate in the form of lower lease payments.”

KeyBank’s Paolo de Alessandrini highlighted

an additional advantage of leasing, telling *Marine News*, “Leasing may also be advantageous for compliance with covenants on existing loans.”

Signature Financial’s Rabin stressed the need to be prepared for the unexpected, citing unanticipated turning points in market cycles which could influence asset values.” He pointed out that estimates from expert surveyors who provide estimates of future asset values always include the caveat of being “subject to market conditions.”

Ship finance lawyer Mark Lowe, currently counsel at New York based Hill, Betts & Nash, has seen the business from all angles, with stints on the owning side earlier in his career. He told *Marine News*, “Where U.S. finance transactions are concerned, the documentation is similar to that of foreign deals. The one exception is where U.S. government guaranteed financing, the Title XI program, is involved. There, the documents are totally different and considerably more complex and voluminous.”

Amy Kyle is a partner in the Boston office of Morgan, Lewis & Bockius. The firm represents financial institutions with a specialty in transportation deals. She told *Marine News*:, “The corporate structures favored by shipping companies (individual vessel owning subsidiaries) impacts lending structure, calling for a co-borrower or

guarantor structure, since the lenders will want to have claims over the asset owning entities (and related collateral). Jones Act citizenship rules continue to have an impact on lending. While a lender can mortgage Jones Act vessels without proving citizenship, restrictions on Non-citizen equity ownership of Jones Act companies can add to complexity."

Who is Active? Where to Look

Where non-listed companies (unlike Kirby, OSG and Hornbeck) are involved, all parties are tight-lipped. A recent deal is the exception. Privately held VanEnkevort Tug & Barge, an operator on the Great Lakes, used $53 million of funding from Key Equipment Finance, plus additional funding from Key Bank's capital markets and syndications group, to acquire a tug/barge combination that had been built by DonJon in 2011, for DonJon's joint venture with Seabulk. The ATB hauls bulk steelmaking commodities around the Lakes, including into Cleveland (where Key Bank is headquartered).

Who else has been active in the market? The United States Surface Transportation Board (which deals primarily with rail transportation) requires that certain debt obligations be recorded. A sampling of recent "recordations" provides a very unscientific window into who is doing what in the world of equipment finance. The database is online at https://www.stb.gov/recordations.nsf

Eyes on the Oil Patch

All eyes are on vessels serving the oil patch, particularly in the Gulf of Mexico. Earlier this summer, Hornbeck Offshore Services announced that it had "... refinanced its existing $200 million senior secured revolving credit facility (the "Old Credit Facility") with a new first-lien delayed-draw credit facility providing for up to $300 million of term loans (the "New Credit Facility"). The six-year term of the New Credit Facility extends the maturity of the Old Credit Facility from February 2020 to June 2023." These deals are complicated, but, in essence, Hornbeck – in the grip of a terrible market – has gained more liquidity, and (if you read the fine print) must no longer comply with certain financial ratios that were crafted in better times. Interestingly, the fine print also hints at an intention to use the financing (not cheap, at interest rates of ranging from Libor plus 600 in year 1 to Libor plus 750 in year 5 and beyond, if not prepaid) to pick up downtrodden competitors' distressed assets. The lenders are part of a syndicate administered by Wilmington Trust, NA. One hint of possible participants can be found in the Collateral Agreement, Hornbeck maintains deposits at Capital One, DNB, and Whitney Bank.

https://www.sec.gov/Archives/edgar/data/.

101_06152017.htm
http://hornbeckoffshore.com/company/new...offshore-announces-new-credit-facility-2017

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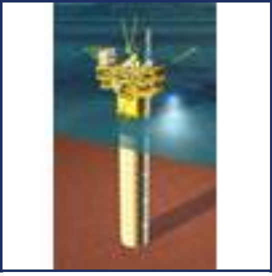

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