MOORE STEPHENS LLP
CHARTERED ACCOUNTANTS OF SINGAPORE

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Adding Value to Your Business

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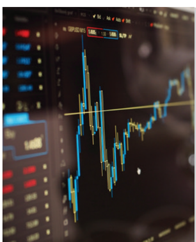

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Key Economic Developments

OCTOBER - DECEMBER 2016

1. By October 2016, about US$10.5 billion worth of assets had been repatriated to Indonesia under its tax amnesty programme, according to Indonesian tax authorities. Approximately 57% of the assets were from Singapore. The Monetary Authority of Singapore (MAS) had earlier advised Singapore banks to encourage Indonesian clients to ensure tax affairs are in order, where necessary, via the amnesty.

2. In October 2016, the International Monetary Fund included the Chinese Renminbi as the fifth currency in the Special Drawing Rights basket, with weightings exceeding both the Sterling Pound and Japanese Yen.

3. In October 2016, Vietnam's TTC Group revealed plans to raise US$600 million on the Singapore equity bourse by listing one of its sugar units within 5 years. Ahead of the listing, TTC will become Vietnam's biggest sugar producer with a worth of US$200 million upon completion of its proposed merger with another sugar company.

4. In November 2016, Trans-Pacific Partnership (TPP) member countries sought to press on with TPP in spite of possible US withdrawal. Japan's parliament has ratified the TPP subsequently in December 2016, while Singapore agreed to amend its laws to ratify TPP by 2017.

5. In November 2016, Donald Trump was elected as the 45th president of the United States, beating Democrat and former Secretary of State Hillary Clinton. Trump will succeed President Barack Obama upon his inauguration on 20 January 2017.

6. In December 2016, Cheung Kong Infrastructure Holdings Ltd., owned by Hong Kong billionaire Li Ka-shing, offered to buy Australia's Duet Group for A$7.3 billion in cash at a 28% premium. The deal would be Li's biggest acquisition in Australia.

7. In December 2016, the Ministry of Finance and the Accounting and Corporate Regulatory Authority launched a public consultation exercise to gather views on the proposed changes to the Companies Act, Limited Liability Partnerships (LLP) Act and Accountants Act. The changes include aligning timelines for holding annual general meetings and filing annual returns, requiring liquidators to retain records of wound-up companies and LLPs for five years instead of two, and requiring companies and LLPs incorporated or registered in Singapore to maintain registers of beneficial owners, among other changes.

8. In December 2016, TPG Telecom became Singapore's fourth telecommunications company with a bid of S$105 million. TPG Telecom will be allocated 60MHz of spectrum band, with operations set to start in 2018.

9. In December 2016, brokerage firm OCBC Investment Research reported that SembCorp Marine has axed 8,000 workers since 2015 as part of its cost cutting measures to deal with a declining order-book.

Key Economic Developments (Cont.)

10. In December 2016, the Singapore branches of Standard Chartered Bank and Coutts & Co were fined S$5.2 million and S$2.4 million respectively by MAS for lapses in money laundering controls in the handling of 1MDB-related fund flows. MAS has also shut down two private banks – BSI and Falcon – and jailed two former BSI bankers for their links to the Malaysian state investment fund. In November 2016, EFG International acquired BSI for 1.06 billion Swiss francs (US$1.07 billion), lower than the originally announced purchase price of 1.33 billion Swiss Francs.

11. In December 2016, Goldman Sachs was ordered to pay US$120 million for attempts to manipulate interest rates. According to the United States' Commodity Futures Trading Commission, Goldman Sachs traders had deliberately timed and priced trades between 2007 and 2012 to influence published interest rates. Separately, the Swiss Competition Commission also imposed nearly US$100 million of fines on several banks including Barclays, Citigroup, Credit Suisse, Deutsche Bank, JP Morgan, Royal Bank of Scotland, Societe Generale and UBS, for rigging interest rates between 2005 and 2010.

12. In December 2016, Deutsche Bank and Credit Suisse paid penalties of US$7.2 billion and US$5.3 billion respectively to settle claims of toxic mortgage bonds that contributed to the 2008 financial crisis.

Key Shipping Developments

OCTOBER - DECEMBER 2016

1. In September 2016, Lonsdale Consortium comprising the Future Fund, QIC, Global Infrastructure Partners and the Ontario Municipal Employees Retirement System acquired, for AUD9.7 billion, a 50-year commercial lease on the Port of Melbourne, which is Australia's biggest container and cargo port and is visited by more than 3,000 ships each year.

2. In September 2016, the Ballast Water Management Convention came into force after ratification by Finland. The convention will take effect on 8 September 2017 and requires ships to manage ballast water to remove, render harmless, or avoid discharge of aquatic organisms and pathogens.

3. Tankers, bulkers and containerships generally benefitted from declining operating costs in 2015, according to an OpCost benchmarking study conducted by Moore Stephens in October 2016. It is the fourth consecutive year-on-year reduction.

4. In November 2016, Norddeutsche Landesbank (NORD LB) reported consolidated losses after tax of EUR 0.7 billion for the first 9 months of 2016 due to losses on ship financing, and expected full year losses of over EUR 1 billion (US$1.06 billion).

5. In November 2016, average shipping confidence levels rose to its highest levels since August 2015, according to a shipping confidence survey conducted by Moore Stephens.

6. In November 2016, members of the Organization of Petroleum Exporting Countries (OPEC) agreed to reduce crude oil production by 1.2 million barrels per day. Certain non-OPEC oil producers, including Russia, also agreed to reduce production by 0.6 million barrels per day. Among those most likely to be impacted will be Very Large Crude Carrier owners due to potentially lower demand for oil transportation.

7. In December 2016, A.P. Møller-Mærsk A/S acquired German rival Hamburg Süd, the world's seventh largest container shipping company, after Maersk announced plans to split operations into separate divisions focused on transport and energy.

8. In December 2016, Korea Development Bank and Mirae Asset Securities launched a KRW 500bn (US$418 m) shipping fund to finance new investments by Korean shipowners.

9. In December 2016, bondholders of Rickmers Trust Management (RTM) voted against a financial restructuring proposal, leaving RTM with no option but to raise capital by reducing the vessel fleet.

Key Shipping Developments (Cont.)

10. Confidence in the Singapore bond market was shaken by defaults from Offshore & Marine (O&M) issuers in the second half of 2016. One issuer, Swiber had filed for liquidation in July 2016, but was subsequently placed in judicial management instead. O&M issuers that successfully restructured debt included Marco Polo Marine, AusGroup, and Ezra Holdings. Others, including Rickmers Maritime, Swissco and Perisai Petroleum Teknologi, were less successful.

11. In December 2016, the Federal Maritime Commission (FMC) approved THE Alliance for trade lanes traveling to and from the United States. THE Alliance is a vessel-sharing arrangement that combines the shipping capabilities of Hapag-Lloyd, Yang Ming and the recently-merged Japanese container lines (K Line, MOL and NYK).

12. As at December 2016, containerships sent for scrapping in 2016 amounted to 699,000 TEUs, according to statistics from shipbroker Braemar ACM. Demolition looks set to exceed 700,000 TEUs by end-2016, a nearly four-fold increase from the 187,500 TEUs scrapped in 2015.

Shipping Confidence hits 15-month high

The latest Shipping Confidence Survey from Moore Stephens shows an improved shipping confidence for the third successive quarter in the three months to end-November 2016.

The average shipping confidence level went up from 5.4 in August 2016 to 5.6 out of 10.0 in November 2016 – the highest rating since August 2015. All main categories of respondent were more confident than in August 2016, with the charterers attaining a notable increase of 2.0 points to 6.8. This marks the highest figure in the life of the survey for such respondents.

Business performance factors

27% Competition

25% Demand trends

15% Finance costs

Competition is expected to influence performance most significantly over the next 12 months, just ahead of demand trends, followed by finance costs and tonnage supply.

A number of survey respondents believe that the bottom of the cycle had been reached and that the only way was up. Respondents are primarily concerned about overtonnaging, insufficient recycling, and increased cost for regulatory compliance.

Respondents also felt that competition is likely to influence shipping performance the most over the next 12 months, just ahead of demand trends, followed by finance costs and tonnage supply.

The likelihood of respondents making a major investment or significant development over the next 12 months was unchanged, at 4.9 out of 10. Charterers' and owners' confidence in this regard were up, but those of managers and brokers were down. The number of respondents expecting finance costs to increase over the coming year rose from 35% to 53%, the highest level for five years.

Most important funding sources

- 21% Shipowner equity
- 19% Bank finance
- 15% BWM system manufacturers
- 12% Shipyards
- 10% Other non-bank finance

When asked what they considered to be the most important source of funding for compliance with Ballast Water Management (BWM) regulation by shipowners, 21 percent of respondents felt that shipowner equity would provide the source of funding, 19 percent said bank finance, 15 percent said BWM system manufacturers, 12 percent said shipyards, and 10 percent said other non-bank finance.

This is the third successive increase in shipping confidence recorded by the survey despite the adverse general climate, according to Richard Greiner, Partner of Shipping & Transport at Moore Stephens, which says much for the tenacity and resilience of the shipping industry.

Country-by-Country Reporting (CbC Reporting): A new paradigm in Singapore

Background

In October 2015, the Organisation for Economic Cooperation and Development (OECD) rolled out the final reports on Base Erosion and Profit Shifting (BEPS). This marked the culmination of about three years of intensive deliberations involving the OECD member countries and some other members of the G20. One of the significant achievements of the BEPS initiative is the consensus on greater transparency regarding global supply chain profits for transfer pricing risk assessment by tax authorities. Action 13 of BEPS introduces a framework for CbC Reporting, with the objective of enhancing transparency for tax administrations.

Against the backdrop of OECD's inclusive framework for the global implementation of measures against BEPS, Singapore is committed to implement four minimum standards under the BEPS project, of which CbC Reporting is one. To align with its commitments as a BEPS associate, the Singapore Ministry of Finance (MOF) has incorporated CbC Reporting in the draft Income Tax (Amendment) (No. 3) Bill for introduction in Parliament. On 10 October 2016, the Inland Revenue Authority of Singapore (IRAS) released an e-Tax Guide to provide taxpayers with administrative guidance on the implementation of CbC Reporting from financial year 2017 onwards. CbC Reporting requires Multinational Corporation (MNC) groups with a Singapore-based ultimate parent to compile information on the group's profits from operations worldwide.

Key highlights of CbC Reporting in Singapore are underlying as below:

CbC Reporting Applicability and Filing

The CbC Reporting requirements are applicable to a Singapore-based MNC group if:

- The ultimate parent entity of the MNC group is tax resident in Singapore;
- The consolidated group revenue in the preceding financial year is at least S$1,125 million (approximate to the EURO 750 million recommended by the OECD); and
- The MNC group has a presence in at least one foreign jurisdiction.

Where the Singapore entity is not the ultimate parent entity, it will not be required to prepare a Country by-Country Report (CbC Report). This is because the foreign ultimate parent entity may be responsible for filing the CbC Report in its home country. However, the Singapore entity may need to provide the necessary information for its ultimate parent entity to report.

CbC Report Contents

The CbC Report is a document that collates information on an MNC's international related-party dealings, revenues, profits, and taxes paid by each jurisdiction. Essentially, it enables the tax authority to draw inferences on the substance and scale of operations in a particular country and the taxes paid there. The CbC Report format set out by IRAS is identical to that proposed by the OECD under BEPS Action 13 and comprises of three tables:

Country-by-Country Reporting (CbC Reporting): A new paradigm in Singapore (Cont.)

Table 1 – Overview of income, taxes, employees and assets of the MNC group allocated to the different tax jurisdictions that the MNC group operates in.

Table 2 – Overview of the entities (including permanent establishments) of the MNC group organised according to the tax jurisdictions that the entities are tax resident in.

Table 3 – Any additional information that the MNC group believe it would be relevant and useful to interpret or understand the data provided in the CbC Report.

Details and guidance on the information required to complete the above is provided within the IRAS e-Tax Guide. IRAS has also provided useful clarifications and examples on how to interpret the definitions and guidance on the CbCR template.

Submission and penalties

Affected Singapore MNC groups will need to submit the CbC Report within 12 months from the end of any financial year which begins on or after 1 January 2017. Details on the mode of submission of the CbC Report will be released at a later date. Failure to submit the CbC Report may be penalised under Section 105M (Part XXB: International Agreements to Improve Tax Compliance – Offences) of the Singapore Income Tax Act – which could be a fine not exceeding S$10,000 or imprisonment for a term not exceeding two years or both.

Use of CbC Report

The IRAS will use information in the CbC Report for:

- High-level transfer pricing risk assessment purposes;
- Evaluation of other BEPS related risks; and
- Any economic and statistical analyses.

Others key points covered in the e-Tax Guide are:

- IRAS will share information in the CbC Report with jurisdictions with whom they have agreements for automatic CbC Reporting information exchange, on a confidential basis;
- IRAS has emphasized that the CbC Report is intended to supplement a taxpayer's transfer pricing documentation and cannot be used as a substitute for transfer pricing documentation;
- IRAS has clarified that non-Singapore headquartered MNC groups will not be required to submit a CbC Report to IRAS; and
- IRAS has also provided clarification that IRAS does not intend to implement secondary mechanisms (i.e. whereby the filing obligation would fall on any 'constituent entity' of the MNC group operating in a country adopting the OECD's recommended approach) on non-Singapore headquartered MNC groups.

Country-by-Country Reporting (CbC Reporting): A new paradigm in Singapore (Cont.)

Conclusion

This latest development underlines a stronger push for greater transparency and information exchange that demands increased compliance efforts by taxpayers to provide more information to tax authorities. Taxpayers need to plan strategies in advance and create bandwidth for more intensive information requests from tax authorities. Other than CbC Reporting, IRAS has also introduced other measures to enhance tax reporting, e.g. the new Form for Reporting Related Party Transactions.

CbC reporting will require taxpayers to relook at global value chains and ensure parity in profits/income from each country vis-à- vis the level of operations in that country. Taxpayers need to critically examine the data in the CbC Report and identify potential issues. Although the first CbC Report is only due on 31 December 2018, early assessment will provide companies with more time to ensure compliance and avoid unnecessary taxation penalties.

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Singapore Introduces New Tax Form for Reporting Related Party Transactions

In a bid to enhance Transfer Pricing ("TP") risk assessment, enforcement, administration and compliance, the Inland Revenue Authority of Singapore ("IRAS") has imposed new requirements for taxpayers to report details of related party transactions ("RPT").

What is the requirement? Effective from YA 2018, each company must complete and submit a Form for Reporting RPT ("RPT Form") to IRAS together with its tax return ("Form C"), if the value of RPT disclosed in audited accounts exceed S$15 million. The value of RPT is the aggregate of:

- All RPT amounts reported in the Income Statement excluding compensation paid to key management personnel and dividend.
- Year-end balances of loans and non-trade amounts due to/from all related parties.

What will the Form contain? The RPT Form requires companies to disclose detailed information on the type and value of RPT with both domestic and overseas related entities, and, in respect of the latter, further details such as the countries of incorporation of the foreign related entities and their exact relationships with the reporting companies.

What should taxpayers do now? Companies should ensure that robust and contemporaneous TP documentation are available to provide evidence that the RPT disclosed are in line with the arm's-length principle, as IRAS will likely request for such documentation when reviewing the RPT Form. Penalties may be imposed for failure to submit as well as incorrect submission of the RPT Form.

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Moore Stephens Financial Reporting Seminar 2016

> *"Of the financial reporting changes that become effective after 2016, the new framework for revenue recognition....which takes effect in 2018, may have the most wide-ranging impact..."*

Extensive changes in financial reporting for revenue, financial instruments and leases will take effect in 2018 and 2019, and companies need to start preparing for these changes now.

That was the key message at the Moore Stephens Financial Reporting Seminar 2016, held at M Hotel on 18 November 2016 and attended by more than 150 participants including directors, CFOs and finance executives. The seminar provided participants with effective and practical tools to assess the impact from new reporting regulations.

Financial Reporting Changes in 2016

One of the most significant changes in 2016 will be the enhanced auditor's report, according to Mr. Wong Koon Min, Partner and Head of Professional Standards at Moore Stephens LLP, who kicked off the seminar by highlighting the most immediate changes that take effect in the 2016 financial year. The enhanced reports are likely to increase the value of the audit, but may also create challenges including potentially increased scrutiny on the tone and language of the more discursive reports.

Other amendments to financial reporting rules in 2016 include changes to accounting rules for biological assets, depreciation and amortisation of long-term assets, pension plans, investment entities, acquisition of unincorporated joint ventures, presentation issues, etc.

Financial Reporting Changes after 2016

Of the financial reporting changes that become effective after 2016, the new framework for revenue recognition specified in FRS 115 Revenue from Contracts with Customers, which takes effect in 2018, may have the most wide-ranging impact.

According to Mr. Wong, while FRS 115 provides a seemingly straightforward, principle-based and 5-step approach to assessing revenue, it also includes much more prescriptive guidance on how that approach applies in a wide range of situations. This has led to the creation of new rules in situations where, prior to FRS 115, companies largely had the flexibility to exercise judgment.

Accounting for financial instruments also faces an overhaul in 2018, when FRS 109 Financial Instruments becomes effective. Mr. Wong highlighted that among the key challenges associated with FRS 109 implementation are the requirements to fair value unquoted equity investments, continuous estimation of impairment provisions, and implementation of the new hedge accounting rules. However, the new hedge accounting rules are generally more permissive than existing ones.

From 2019, lessees will have to capitalise most leases under the new accounting framework in FRS 116 Leases, according to Associate Professor Ng Eng Juan, UniSIM School of Business. As some of these leases may have been classified as "operating leases" which were off-balance sheet under pre-FRS 116 rules, many lessees will report higher gearing ratios. Further, FRS 116 will accelerate lease expenditure,

Moore Stephens Financial Reporting Seminar 2016 (Cont.)

because it front-loads the lease liability amortisation expense, whereas, prior to FRS 116, operating leases were amortised evenly throughout the lease period.

Other Corporate Reporting Developments

Thereafter, Mr. Winston Seow, Head of Corporate & Securities at Withers KhattarWong LLP went on stage to explain the latest developments in corporate regulations. Mr. Seow highlighted that recent events have led to increasing Anti-Money Laundering (AML) enforcement which have increased companies' compliance obligations. In addition, there are expectations that the Code of Corporate Governance may be reviewed soon as the last review was carried out in 2012.

Technological issues were also discussed at the seminar. According to Mr. Choo Kwong Chee, Director of IT Consulting and Solutions at Moore Stephens LLP, the traditional reliance on generic spreadsheet software for reporting purposes is increasingly inadequate to deal with today's sophisticated and increasingly-regulated reporting environment, where seemingly-trivial errors can result in huge losses. Fortunately, cost-effective, tested, and flexible cloud solutions are readily available to support budgeting, planning and reporting.

The seminar concluded with a panel session in which views were shared between the speakers and two additional panellists, Mr. Phil Cowan and Mr. Nick King. Mr. Cowan is Head of Corporate Finance at Moore Stephens LLP, London while Mr. King is a Director in the forensic accounting services team of Moore Stephens LLP, London. The panel discussion was hosted by Mr. Chris Johnson and Mr. Neo Keng Jin, who lead the Risk Management and Initial Public Offerings divisions, respectively, at Moore Stephens LLP, Singapore. The seminar ended at 4.30pm.

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Areas of Regulatory Focus for 2016 Financial Statements

In December 2016, the Accounting and Corporate Regulatory Authority (ACRA) issued Financial Reporting Practice Guidance No. 1 of 2016, which highlighted key areas of focus in upcoming regulatory reviews of FY 2016 financial statements. These areas may require more attention from company directors and finance teams prior to approval of the 2016 financial statements.

1. Adequacy of going concern assumption

    - Assumptions should consider all information relating to a period at least 12 months beyond the financial year-end.
    - Financial support from a parent company to otherwise-insolvent subsidiaries is effective only when the parent company itself is financially viable.
    - Financial statements should include adequate disclosures on significant management judgments on going concern.

2. Adequacy of impairment reviews of long-lived assets

    - Annual impairment testing is compulsory for goodwill and indefinite-lived intangible assets.
    - Impairment reviews on other long-lived assets are required when indicators of impairment occur.
    - Key impairment projection assumptions must be realistic and supported by historical or benchmark data.
    - Cash inflows from assumptions should be consistent with assumptions on related cash outflows.
    - Discount rates used should reflect risks specific to each asset or cash generating unit.
    - Financial statements must contain adequate disclosures, including sensitivity analyses relating to impairment of goodwill or indefinite-lived intangible assets where applicable.

3. Appropriateness of significant one-off gains or losses

    - Significant one-off gains or losses should be critically evaluated in the context of all relevant facts and circumstances to ensure that they accord with the economic reality of such facts and circumstances.
    - Engagement of external financial reporting specialists can facilitate the assessment of such accounting treatments.

4. Appropriate identification of intangible assets in business acquisition accounting

    - Business acquisition premiums paid should be closely analyzed to assess whether such premiums are paid for intangible rights/ resources that need to be separately recorded at fair value (i.e. excluded from goodwill), even if such intangible assets have not been previously recorded in the books of the acquisition target. The financial reporting literature provides precise guidelines on intangible rights/ resources that need to be separately recorded as opposed to those that should be incorporated into goodwill.

Areas of Regulatory Focus for 2016 Financial Statements (Cont.)

5. Appropriate assessment of whether to consolidate or equity account for investees

- Contractual terms that may accord or limit decision powers of specific investors should be properly considered, over and above typical equity voting rights.
- Investor agreements may set out reserved matters that require specific forms of approval (e.g. approval required from certain or all investors), which can impact the assessment of whether investors have control, joint control or significant influence over investees. Investor rights via equity options and side contracts can also influence such assessments.
- Financial statements must contain adequate disclosures relating to significant judgements made in such assessments.

6. Appropriate classification of cash flows in the Statement of Cash Flows

- One common pitfall is to present cash flows relating to business acquisitions or disposals as operating cash flows.
- Another common pitfall is to present foreign currency translation differences arising from the consolidation of foreign subsidiaries as an adjustment to profit when determining operating cash flows using the indirect method.

7. Appropriate disclosure of significant judgements and critical estimates

- Financial statements should contain adequate, meaningful disclosures on significant, subjective or complex judgements.

The full report is available at:
https://www.acra.gov.sg/uploadedfiles/Content/Publications/Practice_Guidance/FRSP%20PG%201%20of%202016.pdf

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GST Treatment on Fringe Benefits

On 16 May 2016, the Inland Revenue Authority of Singapore (IRAS) released an e-Tax guide "GST: Fringe Benefits", which took effect immediately to clarify IRAS's position on when are fringe benefits regarded as being "for the purpose of business" such that the related GST input tax will be claimable by GST-registered businesses. A 2nd edition of the guide, published on 6 January 2017, provided further operative guidance and clarifications.

Previous rule

Prior to 16 May 2016, goods and services acquired and provided by the business entity as fringe benefits (e.g. mobile phone plans, memberships with a professional body and educational course) to its employees were generally considered to be for business purposes, and the related GST input tax was largely recoverable with limited exceptions (as specified in regulations 26 and 27 of the GST (General) Regulations).

New rule

With effect from 16 May 2016, fringe benefits are being regarded as being "for the purpose of business" **only if** there is a close nexus to business activities ("Close Nexus Test"). Mere capability to provide business benefits (e.g. improved staff morale) is insufficient justification to meet the Close Nexus Test.

To meet the Close Nexus Test, IRAS must be satisfied that the fringe benefits:-
1) Are necessary for the proper operation of the business;
2) Directly maintain or promote the efficiency of business operations;
3) Primarily promote staff interaction;
4) Encourage upgrading of employees' skills and knowledge that is relevant to the business;
5) Recognise employees' contribution towards the business; or
6) Promote corporate identity.

Fringe benefits that are given **only** to sole proprietors, partners of a partnership, company directors, or connected persons, would not satisfy the Close Nexus Test, unless the fringe benefits pertain to fees for courses that are relevant to the business. Further, businesses making supplies that are partly exempt and partly taxable can only claim the apportioned GST input tax in respect of the latter.

Accounting for deemed GST output tax

The requirement to account for GST output tax on fringe benefits remains unchanged, i.e. businesses may be required to account for GST output tax on fringe benefits provided to employees if they have claimed the corresponding GST input taxes, with limited exceptions (e.g. goods costing below $200 and free services provided by the business to its employees).

Conclusion

With the new GST rules on fringe benefits, businesses need to review employee fringe benefits to effectively integrate the changes when preparing GST returns.

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Moore Stephens in the News

The Straits Times | Thursday, December 22, 2016

vice portfolio, up from 13 per cent in the previous quarter.

Moody's also expects OCBC and UOB to see more NPLs next year. It has downgraded the baseline credit assessments for all three lenders from "aa3" to "a1" to reflect weakening asset quality and profitability.

Besides the banks, companies from other industries servicing the sector have also been affected.

"Offshore and marine firms are tightening their belts in general due to the downturn. We therefore run longer and further for every dollar earned," said Mr Jonathan Oon, director of the shipping department at law firm TSMP Law Corporation.

He noted that TSMP deals with more dispute resolution and restructuring work these days, compared with financing work previously.

"We certainly expect to see more disputes between companies next year, as is common in a down market. Amid challenging operating conditions, companies tend to worry about solvency issues with their business counterparts and are less likely to extend credit or allow deferment of payments," he said.

Traders at the New York Stock Exchange. Opec's decision in November to cut output sent oil prices higher, although production cuts could also have implications for the offshore and marine industry in Singapore and elsewhere in the world. PHOTO: BLOOMBERG

Once an industry darling, Swiber faced mounting debt obligations it was unable to fulfil amid a dearth of new orders and work. Its troubles – never mind that poor management might also have been at play – are but symptomatic of the distress that has gripped the wider sector.

HOW LONG MORE TO GO?

The question remains – will the recent developments in oil spell a new chapter for the beaten-down offshore marine sector here?

Analysts agree that the oil market could see recovery, though only if global oil producers adhere to the production cuts, which could help lift offshore and marine companies.

If the production cuts are carried out as promised, oil prices could average at US$60 to US$65 a barrel next year, Mr Audun Martinsen, vice-president of oilfield service analysis at Rystad Energy, wrote in a recent report. Exploration and production spending, too, will react accordingly.

He said: "Opec production cuts will turn the needle on the FID (final investment decision) for many projects in shale and offshore, which will generate more transparency on activity and revenue."

That said, it will require time for any positive uptick in crude prices to trickle down the supply chain.

Mr Ang Ding Li, IHS Markit's Asia Pacific head of upstream cost research, believes the market will remain weak next year, as the issue of oversupply has yet to be resolved.

New orders for oil rigs, for example, which have come to a standstill amid excess supply, are set to be extremely low for the next five to 10 years, while the markets for offshore support vessels and platform supply vessels continue to be massively oversupplied.

"Although we may begin to see some projects being awarded in 2017, it will not be sufficient to propel the industry towards recovery. A recovery is likely to begin only sometime in 2018 or 2019," said Mr Ang.

Mr Mick Aw, senior partner at shipping advisory firm Moore Stephens, expects more job cuts across the sector, which accounts for up to 11 per cent of manufacturing's contribution to Singapore's economy, and 20 per cent of manufacturing jobs.

Citing SembMarine as an example, Mr Aw noted that the group has retrenched more people since the start of the year, to 8,000. "Even after these cuts, it was still in the red. It is not impossible that further cost reduction may be carried out to return the group to profitability."

Other companies may similarly attempt to return to profitability through more efforts to streamline operations and reduce costs.

With a slew of uncertainties clouding the near-term outlook for the local offshore and marine sector, it remains to be seen whether the flow-on effects of the oil price troubles will let up any time soon.

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• Additional reporting by Wong Wei Han

> "Even after these cuts, [SembMarine] was still in the red. It is not impossible that further cost reduction may be carried out to return the group to profitability..."
>
> **Mick Aw**
> Senior Partner,
> Moore Stephens LLP,
> Singapore

Moore Stephens in the News (Cont.)

The Edge | Monday, October 24, 2016

6 • THE EDGE SINGAPORE | OCTOBER 24, 2016

CORPORATE

Shipping's new threat

Experts predicted the comeback of container shipping in 2016/17, when the vessel glut causing the slump was expected to abate. Yet, companies such as Hanjin Shipping and Rickmers Maritime are going under, and more are in danger of sinking. What is still ailing the sector?

| BY KANG WAN CHERN |

It has been five years since the world's largest shipping company, Maersk Line, ordered its first ten 18,000 TEU (twenty-foot equivalent unit) container ships, and over a year since the first of the vessels were delivered. The largest of their kind at the time, the vessels are able to move a maximum of 18,000 twenty-foot containers — equivalent to more than 180 million iPads or 111 million pairs of shoes — across the world at a much lower cost than smaller vessels.

And, despite a ballooning glut of container ships and sinking freight rates across the world's trade routes, Maersk has ordered 10 more 18,000 TEU and eleven 19,630 TEU ships, in anticipation of continued expansion in global trade and economic growth. Its peers, including **Orient Overseas International**, Mediterranean Shipping Co and CMA CGM, have ordered vessels of similar or greater size. Shipping, the industry insiders have argued, is a cyclical business, and would eventually turn around when demand for vessels to ship goods improved and balanced out supply. To prepare for that upturn, liners have been building big, hoping to snatch market share and raise margins when demand returns. Between 2005 and 2016, the global supply of container ships grew 147%, according to consultancy Moore Stephens.

Yet, shipping remains in the doldrums after years of industry consolidation and a slew of innovative strategies such as shipping alliances and the implementation of peak season surcharges to keep freight rates profitable. Transpacific service contracts for the largest retailers have dropped below US$750 per forty-foot equivalent unit to the US West Coast, and US$1,500 per FEU to the US East Coast between May 1, 2016 and April 30, 2017. Historically, contract rates on the Transpacific ranged between US$1,800 and US$3,000 per FEU.

After months of trying unsuccessfully to negotiate for lower charter rates from ship owners and missing several payments to suppliers, South Korea's **Hanjin Shipping**, the world's seventh largest shipping line, finally buckled in August. A month later, Singapore-listed shipping trust **Rickmers Maritime** announced a restructuring plan requiring bond holders to swap $100 million of 8.45% notes due May 2017 for $40 million due November 2023 and around 1.32 billion new units in the trust. Failure to restructure will result in Rickmers Maritime winding up.

"Two years ago, the industry predicted shipping was nearing the bottom of the cycle and that the oversupply of vessels would clear out by 2016/17. But here we are again, at the same place. Things have not gotten better and no one knows just how long this downturn will last," says Kim Ji Woon, a shareholder in the Singapore office of law firm Vedder Price, which specialises in shipping.

Maersk has ordered more container ships in anticipation of continued expansion in global trade and economic growth, but shipping remains in the doldrums despite years of industry consolidation

Changing demand

Why isn't the container oversupply abating? What is holding up the recovery? One reason could be a shift in consumer demand. "The fall in demand for shipping can be linked to changing spending patterns. These days, people are not buying physical products such as CDs or PlayStations anymore. They are buying music on iTunes and games on the App Store," says Rahul Kapoor, a director at maritime consultancy Drewry Financial Research Services. "There is also less demand and less of an incentive to invest in cars, or in furnishing new hotels, with more awareness of the environment and adoption of models like Airbnb."

Worldwide shipments of devices such as PCs and mobile phones have also been declining since 2015. This year, the market for PCs is expected to drop 8% y-o-y as demand shifts to laptop computers and tablets, and businesses delay replacing existing machines, says tech research firm Gartner. Meanwhile, total mobile phone shipments are expected to decline by 1.6% y-o-y this year. "The smartphone market is maturing with phones that remain good enough for longer," Gartner research director Roberta Cozza says in a press statement.

Kapoor adds that the industry will probably continue to flounder, given the way businesses are investing these days. "Over the past 18 to 24 months, global trade has been growing at a fraction of GDP because the manufacturing sector is stagnating and investors are channelling capital into growing the services sector. That has a negative impact on the shipping of physical goods," he says. At the start of 2016, the Baltic and International Maritime Council reported lower shipping demand from China and disappointing European demand for containerised goods.

The changing dynamics of the international political economy pose new threats to shipping. "Since the start of the year, we have seen Brexit and the de facto failure of the Transatlantic Trade and Investment Partnership. In addition, there is opposition to the Trans-Pacific Partnership within the US, which may impact future Transpacific trade and shipping demand. Innovations such as 3D printing could also potentially threaten international shipping demand," says Mick Aw, senior partner and head, corporate finance and restructuring at Moore Stephens.

Closer to home

Another reason for the protracted shipping slump is a growing preference among retailers for nearshoring, that is, outsourcing production to countries closer to home as wages rise in traditional offshore manufacturing hubs such China and India. That has raised demand for smaller and more versatile vessels to deliver goods on shorter-haul routes, such as intra-Asia routes. "The vessels that are able to operate within Asia are usually just a few thousand TEUs, as some ports in the region are shallow-river ports," says Jason Chiang, director at Ocean Shipping Consultants, part of **Royal HaskoningDHV**.

To speed up delivery time, many more ships on the Transpacific route now bypass the Suez Canal and are moving through the newly expanded Panama Canal, a shortcut connecting the Atlantic and Pacific oceans. "The number of vessels sailing between China and the US through the Suez Canal has declined as liners now favour passing through Panama Canal to save time and costs. However, Panama is only equipped to handle vessels of up to 13,000 TEU in size."

Wong Koon Min, a partner at Moore Stephens, says: "Nearshoring has established itself as an emerging trend owing to the significant advantages it offers." For one, product quality is usually better compared to that from far-flung offshore locations, and customer responsiveness and satisfaction are greater because of faster delivery times. Inventories, transportation costs and the risk of loss from piracy are also

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Mick Aw
Senior Partner,
Moore Stephens LLP,
Singapore

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STRAIT TALK

BY DAVID HUGHES

Looking up?

There are grounds for cautious optimism as shipping enters the new year, but the markets remain challenging

AS 2016 drew to a close, two press releases arrived on my desk that gave some seasonal cheer. After a year that has seen terrible markets across almost the whole shipping sector, and the failure of a huge liner shipping company, they provided welcome reading.

International accountant and shipping adviser Moore Stephens ended the year by telling us that shipping confidence improved for the third successive quarter in the three months to end-November 2016.

According to the firm's latest Shipping Confidence Survey, carried in the three months to the end of November, the average confidence level expressed by respondents was 5.6 out of 10.0, equalling the highest rating since August 2015. All main categories of respondent were more confident than in August 2016, when the overall rating was 5.4.

However, when the survey was launched in May 2008 the overall confidence rating for the shipping industry was 6.8. Since then we have more or less experienced an eight-year downturn. Moore Stephens says that "a number of respondents" felt that the bottom of the cycle had been reached and that the only way was up. That optimistic view seems to be based on the belief that the long-term problem of too many ships chasing too few cargoes may be about to ease. One respondent to the survey noted: "The oversupply of tonnage will cease when the banks write down bad loans and force owners to sell for scrap."

Another said: "The weak or unlucky will fold or be gobbled up, while the strong or the lucky will grow and succeed."

So what could trigger this rush to the scrapyard. Possibly the answer comes from the answer to a stand-alone question included in the survey: "They considered it would be the most important source of funding for the installation of Ballast Water Management (BWM) systems by shipowners. Overall, on a weighted average basis, 21 per cent of respondents felt that shipowner equity (shareholder funds) would provide the source of funding. Next came bank finance, at 19 per cent, BWM system manufacturers (15 per cent), shipyards (12 per cent) and other non-bank finance (10 percent)."

Tellingly however, one respondent said, "Financing BWM is almost impossible. Owners have no money for it."

That may be an exaggeration if applied to the whole industry but it is quite possible that the cost of fitting BWM to an elderly vessel will tip the balance towards a one-way trip to Alang.

More generally, an industry insider commented: "It is hard to see how major investment to meet environmental regulations can be justified in the current climate."

Another said: "Major investment will be required over the next few years to meet increasingly stringent environmental regulations at a time when earnings are on the floor and bank finance is hard to come by."

So perhaps it is realistic to see an exodus of older tonnage. The trouble is some shipyards are desperate to keep building new ships, stimulating excessive demand for newbuildings. Nevertheless, Moore Stephens partner, Shipping & Transport, Richard Greiner says, "This is the third successive increase in shipping confidence recorded by our survey. So despite overtonnaging, weak freight rates, declining demand, insufficient recycling, Brexit, Syria, Donald Trump, despite everything, shipping is still looking up, rather than down. This is not to deny the reality of today's difficult market, or the sluggish economic climate. But it does say much for the strength of shipping's backbone and the quality of its mettle.

Oil and tanker markets

He concludes: "Many of our respondents felt that things can only get better. They are probably right. But for that to happen, freight rates will have to go up. Perhaps it is safer to say for the moment that, if we want things to stay as they are, things will have to change." Make of that what you will.

However, research and consultancy firm Maritime Strategies International (MSI) says that both the oil and tanker markets, "after a year of tumultuous political and policy upheaval", are undergoing a process of rebalancing.

Its latest *MSI Quarterly Tanker Market* analysis finds that, despite the cuts having a limited negative near-term impact, there are reasons to be positive on prospects for the longer term.

"Oversupply of productive capacity in the oil market has been mirrored by excess tonnage capacity in the tanker market. Both are now rebalancing and although fleet growth is expected to remain high in 2017, low earnings and the ratification of ballast water treatment regulations support MSI's expectations that tanker scrapping will move sharply higher in 2017," says MSI senior analyst Tim Smith.

He added: "This will help construct a market recovery in 2018 and beyond, built on much lower fleet growth rates than being seen currently, both in the large crude and product tanker sectors. The tanker market, like the oil market, is in a clearing phase, removing over-supply and rebalancing. That process could take another year or so before returning to a position where sustained gains can be made, but we remain positive on the long-term outlook."

Nobody appears to be singing *Happy Days Are Here Again* quite yet, but perhaps there is a small glimmer of light at the end of the tunnel, for the shipowners who manage to make it that far.

> "This is the third successive increase in shipping confidence recorded by our survey..."

Richard Greiner
Partner,
Moore Stephens LLP,
UK

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