BANKS JOIN THE MOVEMENT TO CLEAN UP THE SEAS

New forms of sustainable financing to move the green agenda in shipping

Photo: Sean Lee

Demand for green shipping loans are likely to grow, according to Mr Nicolas Parrot, Managing Director and Head of Transportation Sector, Investment Banking Asia Pacific at BNP Paribas Singapore.

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Global shipping is seeing the green shoots of financing with new, innovative products that have come up in recent years: green and sustainable loans.

This trend has been driven by stricter environmental regulations, such as the impending IMO2020 sulphur cap, ballast water management rules, and the global target for greenhouse gas emissions to be halved in 2050, compared with 2008.

"I think it's no secret that the shipping sector is a major contributor to CO2 emissions. Climate action is one of the European Investment Bank's (EIB) top priorities, and this type of financing should be seen as an incentive for ship owners to consider doing things differently," said EIB President Werner Hoyer in a press release in February last year.

He was referring to the deal the EIB inked with Dutch multinational bank ING back then to support green investments in the European shipping market for a total of €300 million.

"The facility... aims to help the shipping sector transition to a greener future."

Green financing tools

Green or sustainable shipping finance comprise mainly two products: green bonds and green loans, and sustainability-linked loans, explained Mr Nicolas Parrot, Managing Director and Head of Transportation Sector, Investment Banking Asia Pacific at BNP Paribas Singapore.

The key feature of green bonds and green loans, as opposed to traditional sources of financing, is that proceeds must be used to provide clear environmental benefits, he said.

Green loans are used to finance sustainable projects or assets, from ballast water treatment systems to liquefied natural gas engines and propellers, and scrubbers.

"(They) open the doors for more shipping companies to be certified green, taking them further on their sustainability journey," Mr Parrot said.

Sustainability-linked loans, on the other hand, are designed to incentivise the borrower to achieve ambitious, pre-determined sustainability performance objectives, he noted.

Put simply, when the borrower achieves a pre-determined target and shows a clear improvement in his sustainability performance, the margin or interest rate on his loan will then be reduced. But if he falls short of the target and clocks higher carbon emissions, for example, interest rates may go up.

Rising demand

In an industry that has its hands tied with limited access to finance – the result of massive overcapacity and piling debt levels in the last few years – such innovative loans have been welcome.

After all, for many companies, having the financial ability to retrofit their ships with scrubbers or access compliant fuels to meet the new rules is critical for their survival.

Within the Asia Pacific, Singapore-based shipowner Quantum Pacific Shipping in November entered into a US$40 million green loan with BNP Paribas for scrubbers – the first of its kind in the region.

Japanese shipping giant NYK Line has also closed a ¥2 billion loan to build its first methanol-fueled chemical tanker, and a ¥9 billion syndicated loan agreement for scrubbers.

Demand for such loans is only set to grow.

Mr Parrot said BNP Paribas is expecting higher interest for green financing from shipowners this year. "It provides funding source diversification, and the tightening of environmental regulations will promote the use of new technologies. These capex are ideal targets for green shipping products," he said.

"Going green is no longer an option today – it's becoming an industry standard." ▪

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>
> *Dr Werner Hoyer*
> *President*
> *European Investment Bank*

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ARE CHARTERERS READY TO REPORT HIGHER DEBT LEVELS THIS YEAR?

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As the year 2020 approaches, shipping players across the world are scrambling to prepare for the upcoming sulphur cap set by the International Maritime Organization.

But that is not the only change that is taking place in the maritime industry.

On Jan 1 this year, new lease accounting requirements kicked in, with Moody's Investors Service describing them as "one of the most transformative accounting changes in recent history".

The IFRS 16 Leases and the Singapore-equivalent pronouncements FRS 16 and SFRS(I) 16[1] now require charterers to capitalise or record future charter payments as a liability on their balance sheet. Previously, future charter payments were mostly off-balance sheet and expensed only as incurred, except for long charters stretching over most of the economic life of the ships.

The moves are a step in the right direction, bringing higher levels of transparency to the balance sheet.

But this also means that many charterers are likely to report higher liabilities and gearing (debt-to-equity ratio) this year. Previously, most charterers would have reported low or even no liabilities associated with their charter contracts.

Since a higher debt level inevitably affects a company's financial metrics, with possible consequences on bank agreements and key performance indicators, it will benefit charterers to have prepared for it in advance.

It is important to note that the new rules differ for various ship charters. For example, ship charters of less than one year are not capitalised or recorded.

Most voyage charters do not need to be capitalised either because the new requirements target only charter-parties, where control of the ship – in terms of decisions such as ship route, cargo, voyage speed and so on – is passed to the charterer. For voyage charters, these decisions are usually not dictated by the charterers.

In addition, not all charter payments are capitalised. For example, charter payments that vary based on a charterer's revenues or profits do not need to be capitalised.

Further, charter-parties may comprise different streams of revenue. Take, for instance, a time charter-party that comprises revenue from both the underlying bareboat charter and services, such as the provision of crew. In such a contract, the charterer might choose to capitalise only the bareboat charter revenue, subject to certain criteria.

The new leasing requirements will have less impact on shipowners who charter out their ships, as the accounting by lessors is largely unchanged. For lessors, the distinction between finance and operating leases remains, based on whether the charter-party transfers all the substantial risks and rewards incidental to the owners of the ship.

With a significant number of charterers likely to be affected by the new rules, it is important that they make the relevant preparations in advance. Negotiation and the proper structuring of charter-party clauses, with a clear understanding of their financial implications under the new leasing requirements, will be crucial to minimising any unintended financial consequences. ▪

[1] IFRS, FRS and SFRS(I) are abbreviations for International Financial Reporting Standards, Singapore Financial Reporting Standards and Singapore Financial Reporting Standards (International) respectively.

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POWERING FORWARD WITH LNG

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Mr Thomas Hansen, Commercial Director of Eastern Pacific Shipping, believes in taking the lead in green shipping with LNG.

Photo: Sean Lee

In its push for a more sustainable future, the shipping industry has found itself awash with uncertainties.

But Mr Thomas Hansen, Commercial Director of ship management company Eastern Pacific Shipping, believes that "future-proof" liquefied natural gas (LNG) is the way to go – at least for now.

Last month, the Singapore-based firm exercised an option from a 2017 order and requested for another six 15,000 standard-sized boxships. The new dual-fuel ships will run on LNG.

Shipping, which has been reliant on dirty heavy fuel oil, is under mounting pressure to clean up its act. The International Maritime Organization has set a target for the industry's annual greenhouse gas emissions to be halved by 2050.

Speaking at the Moore Stephens Singapore Shipping Forum yesterday, Mr Hansen cited the merits of the firm's upcoming LNG dual-fuel ships.

They will reduce carbon emissions by half compared to its first-generation vessels, slash sulphur oxides by 95 per cent, cut nitrogen oxides by 80 per cent, and eliminate particulate emissions.

"Are we meeting the IMO2050 target? We don't know yet. But we're ready to see how far (we can go) before that comes out. That's very meaningful reduction," he said.

LNG is the cleanest burning fossil fuel, although observers have noted its inherent drawbacks, such as the risk of methane slips in the supply chain.

At the sides of the event, Mr Hansen noted there are many ship fuel options available, but "very few of them actually viable to be introduced, implemented and adapted today".

Pointing to how the oil majors have invested heavily in LNG, he said the gas will set the course for shipowners until the next best fuel becomes available – "but that's unlikely to happen in the next 10, 15 years".

"So is LNG a temporary fuel? Maybe. But is it temporary for 10 years, or 30, 40 years?" he said.

"Our ships are unlikely to last beyond 20, 25 years, which doesn't even bring us to 2050. If we don't take a lead now, and we just rely on fuel oil, we're not going to get anywhere." ▪