NON-TRADITIONAL INVESTORS HELP TORM EXIT ROUGH WATERS

The emergence of new participants in shipping finance should be viewed as a silver lining. Recent transactions, such as the restructuring of Torm, demonstrate the flexibility and creativity that the newfound diversity brings to the industry writes Peter Newman*

Peter Newman (Milbank): A renewed and recapitalised Torm had positive earnings

The financial crisis wreaked havoc for the shipping industry and its banks. Shipping companies struggled to service their increasing debt burden, and a flurry of restructuring activity followed. Familiar names grappled with the need to recapitalise their debt-laden balance sheets.

Shipping banks felt the pressures doubly. They suffered from the woes of their shipping-industry clients as well as the well-reported pressures faced by commercial banks across industries and jurisdictions. Falling vessel values and increasing loan defaults caused capital impairment and liquidity issues. Bank regulators began to pressure banks to hold more capital and reduce risk. Banks were faced with an inability to lend and, in some cases, were forced to sell off loans and loan portfolios. Some banks were subject to bailouts and nationalisations.

As banks began to shed shipping loans into the secondary markets, alternative types of investors, including mutual funds, private-equity funds, hedge funds and other return-driven investment funds, became lenders to shipping companies. The new lenders generally lacked the historical ties to the shipping industry of the legacy shipping banks. They sometimes purchased loans and assets at discounts and, as different types of institutions from the banks, sometimes had different financial motivations and institutional goals. At times, the introduction of secondary purchasers into the formerly insular shipping world led to wariness and even mistrust between the old guard and the perceived interlopers.

While this dynamic is understandable given the difficult circumstances in which it unfolded, recent experience shows that the presence of different types of institutions in the markets can be highly beneficial to shipping companies and their historical lenders. The introduction of alternative lenders has facilitated dynamic transactions to facilitate growth and corporate renewal that may never have been possible in the pre-financial crisis environment.

Take Torm, for example. Following a first restructuring in 2012 and sales of ships to pay down debt, Torm remained saddled with loans of US$1.4 billion against assets worth roughly half that amount. Torm's historical lenders that could afford to take capital provisions began to sell their loans. Torm's remaining legacy lenders firmly resisted taking further write-downs. By late 2014, Torm was unable to continue to service its debt, had no prospect of refinancing, could not reach agreement with its lenders on a consensual debt restructuring, and appeared headed for insolvency.

Oaktree Capital Management, an investment manager that owned a fleet of product tankers managed by Torm, sought to merge its fleet with Torm's. The combined fleet would create a stronger operating platform. The proposal was embraced by Torm's management, but the transaction could not be delivered without significant concessions from Torm's lenders to reduce leverage to sustainable levels. After months of intense negotiations, a group of lenders that acquired Torm's debt in the secondary market agreed to exchange their debt for equity in the post-combination Torm, thereby facilitating the transaction and enhancing value for all parties.

Ultimately, each of Torm's stakeholder groups contributed to the success of the restructuring: Oaktree contributed vessels to make Torm one of the largest owner-operators of product tankers globally, the 'new lenders' agreed to take equity risk in the reorganised company, and Torm's historical bank lenders continue to offer Torm loan financing. After emerging from over half a decade of over-leverage and financial distress, Torm issued its 2015 second-quarter report: a renewed and recapitalised Torm had positive earnings and cash flows – and US$890 million in equity – and adjusted upward its expectations for the rest of the year. *TST*

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*Peter Newman is a partner in the London office of global law firm Milbank, Tweed, Hadley & McCloy. The views expressed are the author's own. Milbank Associates Kelly McDonald and Ed Rance also contributed to this piece.