DEBT RESTRUCTURING

is still possible in today's recession

BY DAVID HUEMPFNER AND JOHN SIMPSON

Many marina owners are facing increasing debt obligations and decreasing revenue stemming from a shaky economy. Making matters worse, financial institutions have drastically cut back on the supply of credit, which makes refinancing of debt a difficult, if not impossible, proposition for many facilities.

Over the past few years, many owners have entered the marina market, and some have overpaid for now underperforming facilities. Many were unfamiliar with the intricacies of marina management, and many of these owners leveraged themselves and their marina properties using bank loans amortized over 10 to 15 years with associated balloon payments due between years three and five. Those balloon payments are now coming due, and the due dates loom with little or no resources available for refinancing.

Everyday the number of marina owners who are in trouble or marina lenders with non-performing loans grows. The properties are close to foreclosure or very near a balloon payment that owners will not be able to pay or refinance. The owners are stuck in limbo. They know they need advice but don't want to spend the money even if they have it available. So they wait, and if they don't do something soon, it will be too late.

The good news is that there are solutions for all involved that are less painful than foreclosure, which is not always the best course for the lender. Owners can take action to minimize losses and even save their properties.

The problem

Currently, a large number of marina owners are looking for ways to improve cash flow and survive the recession in the short term. However, some U.S. economists are projecting that a potential recovery may take 12 to 18 months. Even if marina owners facing daunting debt obligations can increase short-term cash flow, they still face the prospect of a long-term balloon payment adjustment before a projected economic recovery. Loans must be reworked, renegotiated, or allowed to sell short of the loan amount, or defaults are inevitable.

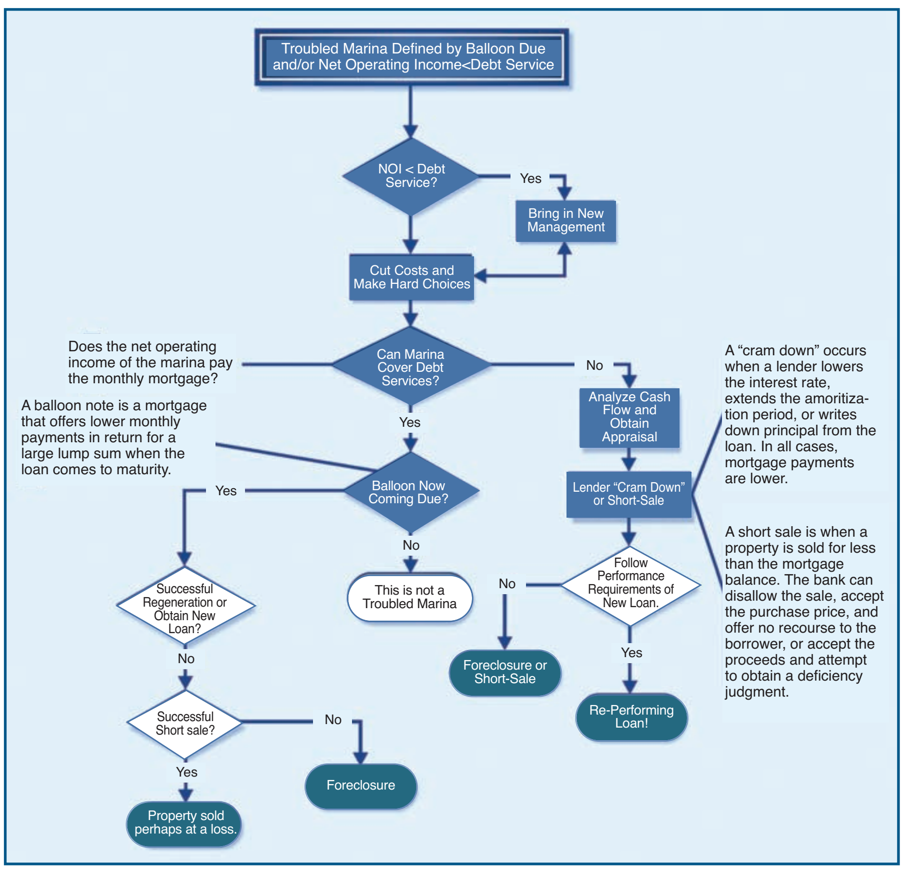
Having been involved in negotiations for both lenders and debtors, one thing is clear: the final outcome is much better when both sides communicate and don't bury their heads in the sand.

Marina owners are seeking to avoid a potential loan default by refinancing loans with their original lending institution or seeking alternative sources of capital. Consequently, lenders are now faced with determining which underperforming marina properties they are willing to refinance with a "cram down" (reducing the loan amount or loan terms or extending the amortization of a loan) and which to place into receivership.

The choices

There are some options available in this scenario to solve problems for clients. Each choice, however, has advantages and disadvantages for both sides.

Renegotiating is less of a loss for both sides. Foreclosure in these painful economic times will result in larger losses for lenders than renegotiating. Logically, lenders should be willing to accept solutions that allow marinas to remain in business with a reasonable adjustment to their loans, rather than



face the prospect of managing marinas and then auctioning them off during a severe recession. Overall, placing numerous marinas in receivership will not maximize the profit of the lender and will only continue to push the industry down.

Possible Solutions

Lenders and owners work to resolve troubled loans using the decision tree (page 42). Different solutions include:

- A group of hard-money lenders is willing to provide bridge financing.
- A group of permanent lenders is willing to come into a project, once stabilized, with new underwriting criteria and reserve requirements.
- Experienced managers take over operations and stabilize the asset.
- An industry standard market study is performed for benchmarking.
- Underwriting that lends on the value-in-use (using current income stream and not "upside potential") until the market recovers.
- Reversal of troubled dockominiums back to rentals.
- Tax assessment relief from local jurisdictions based on value-in-use.

If current management is not performing well, the lender should insist on professional management for the property during the stabilization period. Owners and lenders should also embrace having a professional management company provide consulting services. For example, Island Global Yachting (IGY) Vice President of Business Development Tom Mukamal has seen an increasing number of financial stakeholders request IGY's marina management and auditing expertise for distressed marinas to help stabilize assets, develop strategic options, and gain the support of a credible industry partner in the current economic cycle.

Results

Faced with limited funds and mounting losses, some lenders are reluctantly refinancing troubled marinas. However, lenders have adjusted underwriting criteria to reflect larger equity investments from the borrower and are charging higher interest rates. Furthermore, it is not unusual for lenders to now require additional documentation from borrowers that validates the marina's value (e.g., marina appraisal) and projected performance (e.g., independent market validation report and/or action plan assessment). Although many of these items were always required, they are being scrutinized.

There are some lenders today that are starting to finance new loans at 50 to 60 percent loan-to-value for very strong borrowers with credit scores above 700 and who have other assets that can be attached. The interest rates on these loans are higher, however, and reserves are starting to be required and escrowed.

So where are these lenders? Unfortunately, none of them wanted to broadcast their willingness to lend because they are just determining how to underwrite marinas and are only interested in working with current clients, at least for now.

Going out to the financial market is hard for marinas, and the current lien holder needs to acknowledge this and try to work with their current loans. Hard-money lenders are out there but for a steep price. It is important to note that few in the banking industry understand marinas as assets. However, an experienced marina consultant can greatly assist these lenders.

Conclusions

Given the scarcity of available funds, refinancing an existing marina in the face of a recession can be especially difficult but not impossible. Therefore, marina owners in trouble should determine if an alternative form of capital (e.g., partners) makes the most fiscal sense when compared to refinancing with a traditional lender at a higher interest rate and putting greater equity at stake.

Renegotiating terms with the current lender is another possible course of action. If the renegotiation option is chosen, it is imperative that the marina owner/developer substantiate why the lender should approve a restructuring of the current loan. The owner must be prepared with an action plan for remaining solvent in both the short term and long term, and have a demonstrated commitment to repaying the loan.

One way to demonstrate this commitment would be to retain third-party professionals recognized by the lender that are qualified to validate the marina property's value and projected performance based on their specialized marina industry experience. Independent market validation reports and action plan assessments are necessary to confirm the presence of a viable marina market while validating that management has properly positioned the facility to maximize revenues and the potential partners'/lenders' return on investment (ROI).

Property condition reports showing capital improvement needs are also important, along with allocating enough reserves for replacement. No longer can a marina owner expect to refinance for capital expenditures. Higher reserves and updated underwriting criteria will be the keys to debt restructuring.

Competition for financing among marina owners/developers has increased significantly due to the limited availability of funds. Given the current financial environment, wary lenders or speculative potential partners are apt to lend/refinance only to marina owners who can support their facility's validity, sustainability, and performance by an independent marine industry expert's professional evaluation.

In short, this is perhaps the worst environment for marina lending and refinancing in memory, but there are still opportunities to turn a dire financial situation around. ⚓

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