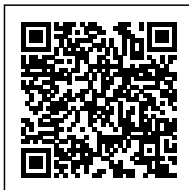


# DEVELOPMENTS IN FOREIGN MARKETS FINANCING

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**As is widely known, Spanish and Portuguese lending institutions are facing a severe liquidity crisis. Unfortunately, this is occurring at a time when an enormous amount of corporate debt is**

## maturing.

The result is a classic issue of supply and demand – the demand for finance by Iberian corporates is reaching a high point, right at a time when their traditional sources have no capacity to lend.

Economic uncertainty in Europe is causing banks to hoard cash; new financial regulations in Spain are drastically increasing provisioning requirements; and BASEL III will have additional provisioning requirements as well. This harsh fiscal environment also makes it unappetising, or simply impossible, for banks to entertain traditional forms of restructuring, such as a debt-for-equity exchange.

Non-performing loans have risen dramatically in Spain, from a low of 1% in 2008 to a high of nearly 8% in 2012, and will likely increase sharply, as the amount of leveraged loans in Spain is expected to almost double from 2012 to 2015. In most cases, the best scenario for a company with a non-performing loan is to refinance, by extending the maturity date and hopefully lowering the interest rate as well. This is often the best way for a company to avoid bankruptcy or an undesirable sale or merger.

Meanwhile, all indications are that the liquidity and capacity for loan making of Iberian lending institutions will be constrained for some time. Historically, most Iberian corporations did not stray beyond their peninsula in the search for financing. Circumstances will now require that they look abroad, many for the first time. Fortunately, and perhaps ironically, the economic crisis in the United States creates many opportunities for debt financing and other alternatives for Iberian corporations searching for debt or equity financing.

In the US, interest rates are at historic lows. The US Federal Reserve Bank has stated publicly that it will keep rates low until 2014, and perhaps beyond. Low commercial interest rates have led to a boom of refinancing for healthy US borrowers. Even borrowers that are experiencing some difficulty have been able to refinance their debt at rates lower than would be obtained in a normal lending environment. While many US financial institutions may still be wary of large exposures in Europe, a healthy Iberian company may yet prove to be an enticing credit.

Even more remarkable is the current high-yield debt market. The high-yield markets are generally available to non-investment grade companies and are frequented by foreign issuers of US debt. The extremely low commercial interest rates have placed downward pressure on high-yield interest rates. Furthermore, the lack of growth and investment opportunities in the US economy has driven a large number of investors into the high-yield markets in their search for a return on investment.

The result is an environment where there are Iberian corporates in search of debt financing, and an excess of investors entering the high-yield markets in the US. Already, in the past few years there have been a few Spanish corporates that have taken advantage of the high-yield markets. As Iberian corporates become more familiar with the US debt markets, the number will probably rise.

Finally, US-based private equity funds are also searching abroad for returns that are increasingly difficult to find in the US. Private equity funds can be much more nimble than institutional lenders in the manner that they provide debt and equity financing. Funds can provide debt (on a secured or unsecured basis) and equity investments for expansion projects, and can also participate in debt for equity exchanges, which is common where the fund acquired the pre-existing debt from an institutional lender.

In short, the public and private debt markets in the US are searching for borrowers, precisely at a time when Iberian corporates are looking for financing. It is probably only a matter of time before more trans-Atlantic matches are made.

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