VenmynDeloitte.

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Breach of Covenants

The possibility is increasing

It is understood that banks are aware that some mining companies may default on the debt covenants that accompanied loans that they have taken in the past.

Debt covenants ask the borrower to fulfil certain conditions or forbid the borrower from other actions.

For mining companies, debt covenants may include requirements that they not enter into any more debt, miss a payment, maintain a maximum ratio of net debt to earnings before interest, tax, depreciation and amortisation (EBITDA) or a minimum EBITDA to net interest ratio.

Promoters of debt covenants suggest that they are intended to facilitate communication between borrowers and lenders, and that when mining companies are facing challenging times they should approach their banks to have frank discussions about the situation that they are in.

However, all too often, and especially in the current downturn, mining companies are concerned that open discussions will lead to banks initiating action that will trigger business rescue proceedings.

"In the current economic climate, many mining companies may be close to defaulting on these covenants," says Venmyn Deloitte MD Andy Clay.

Some of them are playing open cards with their banks while, in some instances, banks are actively trying to identify clients who may default, on the basis that some companies are reticent about disclosing the true state that their businesses are in.

Clay suggests that it is important for mining companies to be open with their banks or the consequences could be precipitous.

To comment on this issue, go to Venmyn Deloitte's Facebook and Twitter pages.

Kind regards,
Deborah Spicer

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