DEVELOPMENTS IN TRADE FINANCE

MARINE MONEY
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Olivier Bazin, Partner
T: +41 (0)22 322 4814
Olivier.Bazin@hfw.com
The trade finance gap

- According to the WTO demand for trade finance exceeds supply by around $1.4 trillion

1. Regulatory
2. Compliance
3. Sanctions
4. Protectionism / trade barriers
5. Human rights / sustainability
Regulatory

- Basel III
- Banks - regulatory cost of capital
- Net Stable Funding Ratio (LT)
- Leverage Ratio
- Security (legal opinions)
Alternative trade financiers

- Traders
- Alternative financiers including funds
- Securitisations
- Investors – yield in low interest environment

Trade facilitation programmes (IFC, EBRD, IDB, WTO (Feb 2017)
[https://www.wto.org/english/news_e/news17_e/fac_31jan17_e.htm](https://www.wto.org/english/news_e/news17_e/fac_31jan17_e.htm)

- Islamic Trade Finance has grown +20% (approx. 15% of world trade according to ICC)

International Islamic Trade Finance Corporation (part of Islamic Development Bank) [http://www.itfc-idb.org/en](http://www.itfc-idb.org/en)

- ECAs
- De-risking and secondary loan market (including insurance)
Compliance - AML

- KYC / KYCC
- Due diligence
- Financial crime / AML
- 4\textsuperscript{TH} anti-money laundering directive
- Before 26 June 2017
- Central register of beneficial ownership – “\textit{persons with significant control}”
- Virtual currency exchange platforms and virtual wallet providers
- Correspondent banking / emerging market access to finance SWIFT keys ➔ impact on trade and trade finance
What makes trade finance a target for financial crime?

- Global nature of business – cross-border flow of goods and money
- Contractual chains
- Volume of transactions
- Ad hoc controls – lack of systematic checks with financial institutions
- Lack of automation – i.e. need for digitalisation
- Prevalence of “dual-use goods”
Compliance - AML – Due Diligence

- Take the vessel as an example ....
  - Owning company (SPV) global sanctions list check
  - Ultimate beneficial owner (UBO) global sanctions check list
  - Port State Control history check
  - Ship global sanction list check
  - Ship movement history check

- What is required?
  - Screening
  - Monitoring
  - Audit trail
Compliance: Transmar case – was it fraud?

- Credit Facility dated 26 February 2016 – New York law
- Amendment and Restatement since 2011
- Tenor **2 years**
- Amount **USD 360m**
- First-priority liens the Debtor's current assets
- Borrowing base composed of eligible cash and
  - eligible net liquidity in brokerage accounts
  - eligible accounts receivable and letters of credit
  - eligible inventory (cocoa powder and butter)
  - eligible net unrealized forward gains and losses
  - eligible prepayments to suppliers
  - eligible origin foreign inventory
Transmar – timeline of financing events

- **15 January 2016** – Itochu acquires a minority stake in Transmar Group and lends money to the trader – Transmar (US) turns to a syndicate of banks for trade loans.

- **4 May 2016** – Transmar (US) borrows $360 million from banks – ABN AMRO is the arranger, collateral agent and admin. agent

- **14 November 2016** – Transmar (US) subsidiary defaults on its commodity contracts and files for bankruptcy in Germany.

- **28 December 2016** – Transmar (US) files for Chapter 11 bankruptcy protection in the United States - $313 million missing Collateral – reportedly transferred to European subsidiary.

- **18 January 2017** – It is reported that the trader’s biggest offtaker is its own indirect subsidiary in Europe.
Status of Transmar case today

- Proceedings taking place in the U.S. Bankruptcy Court for the Southern District of New York
- $400 million owed in total to creditors
- Including $360 million claim by ABN AMRO and $4.7 million in interest
- ABN AMRO representing syndicate including Société Générale, BNP Paribas, Natixis, Macquarie and the Bank of Tokyo-Mitsubishi
- 7 April 2017 – ABN AMRO given permission by court to issue subpoenas on two former Transmar Group senior staff accountants responsible for the preparation of borrowing base reports that Transmar had previously refused to make available for depositions
- Examination of “record-keeping processes”

ABN AMRO – application to Court 29 March 2017
“...borrowing base reports provided to Lenders... were inaccurate, at best, and perhaps fraudulent.”
Fallout of the Transmar case

- Increased scrutiny on borrowing base facilities
- Trust / Fraud risk yes but:
  1. Due Diligence and Understand the customer’s business – don’t neglect corporate credit DD
  2. Structuring
  3. Security and perfection
  4. Conservative advance rates now and for duration
  5. Frequency of reports and audits

Gunvor CFO Jaques Enri

“I’m not sure if it’s due to Transmar, but we’ve seen a real increase in direct meetings with banks coming to meet with our risk people, our credit risk people and our compliance people.” – March 2017, Lausanne
Sanctions

- Economic weapon
- Cautious financiers
- Russia – new normal
  - SDNs
  - SSIs
    - Rosneft
    - Transneft
    - GazpromNeft
    - Novatek (US only)
    - Banks
- Iran
- Venezuela
EU Sanctions

EU Council Regulation No 833/2014, as amended

- “It shall be prohibited to directly or indirectly make or be part of any arrangement to make new loans or credit with a maturity exceeding 30 days...”

- Shall not apply to “financing for non-prohibited imports or exports of goods and non-financial services between the European Union and any third State”

- "the exemption applies where the goods for which financing is being provided are: (a) consigned from the EU to a third country, or (b) received into the EU from a third country (i.e. the EU is the destination). The mere transit of goods through the EU would be insufficient: there must be a meaningful nexus with the EU, in order for this exemption to apply". (page 4, FAQ 6)
Rosneft / Qatar / Glencore deal – December 2016

- Russia state holding company sells 19.5% stake in Rosneft to Qatar Investment Authority and Glencore – US law firms involved.
- Russian budget received $11.37 billion from the sale
- Italian bank Intesa Sanpaolo a major creditor for the deal
- Syndicate of 4 – 5 banks provided €7 billion in financing (Intesa provided €5.2 billion)
- Glencore to hedge the bulk of its stake in Rosneft
- January 2017 – Rosneft deal with company linked to Qatar and Glencore to supply 55 million tonnes of crude over 5 years

$11.37 billion
Planned IPO of EN+ Group

- Billionaire Oleg Deripaska hoping to raise $2.7 billion in IPO of EN+ holding company in 2017
- EN+ owns assets in metals and mining as well as energy and coal sectors - including a 48% stake in UC Rusal, a HK-listed Russian aluminium producer
- Two major US banks (along with Russia’s Sberbank and VTB Capital) are among arrangers according to Reuters

$2.7 billion (?)
EuroChem Group $800m pre-export facility

- Agrochemical company headquartered in Zug
- Owned by Andrey Melnichenko and Dmitri Strezhnev
- Five-year pre-export facility to refinance debt on club basis
- Arranged by **ING** (co-ordinator and documentation agent) and Citibank (facility agent and security trustee)
- Other banks – Bank of China, Commerzbank, Crédit Agricole, Industrial and Commercial Bank of China, Mizuho Bank, Natixis, Nordea, Raiffeisenbank, Société Générale, Rosbank, UniCredit
- Possible IPO in London 2017/18 according to CFO

$800 million
Yamal LNG financing – 3rd largest in Russian history

- $12 billion external financing by Chinese banks of Yamal liquefied natural gas (LNG) project deep in the Russian Arctic
- $27 billion JV between Novatek (50.1%), Total (20%), CNPC (20%) and Silk Road Fund (9.9%) – three phases 2017, 2018 and 2019
- Other external financing from Russian state ($2.3bn) and Sberbank and Gazprombank (€3.6bn)
Notable recent prepayment transactions

- E.g. Oil and Precious Metals – 30 or 90 days
- $165 million prepayment financing for SUEK AG by Sberbank (Switzerland) AG to be repaid by coal deliveries
- $100 million prepayment financing for Russian Copper Company Group (RCC) arranged by SIB (Cyprus) Limited to be repaid by copper deliveries
First-half 2017 Russian pre-export (PXF) deals

- **Acron** $750 million five-year loan – mineral fertilizers
- **SUEK** $1 billion loan – coal
- **Metalloinvest** $1.05 billion loan – steel
- **Metalloinvest** $200 million two-year revolver (ING) – steel
- **Rusal** $2 billion plus loan – aluminium

Oversubscription from banks means covenants are loosening and margins are hovering at a low rate of 3%
Protectionism / Trade Barriers

- Consistent rules and regulations
- Mega-regionals
  - TTIP
  - TPP
  - RCEP
- Focus on bilaterals, jobs and national security?
China – One Belt, One Road
Human rights and sustainability

- Corporate Social Responsibility (CSR)
- UNHR Council (Geneva)
- UN Guiding Principles for Business and Human Rights (June 2011)
  - State duty to **protect**
  - Corporate responsibility to **respect**
  - Access to **remedy**
- Expectations of business behaviour
- National Contact Point - OECD
- “Transnational Corporation (TNC)” – UNHRC working on binding instrument on human rights and TNC
Climate Change

Converting forest into agricultural land accounts for more emissions than the entire global transportation sector.

Responsible for around 50% of these emissions:

- palm oil
- soy
- beef
- timber products
Sustainability – reputation vs. compliance

- HFW’s research into the market shows that, whereas a couple of years ago, sustainability was viewed as a reputational issue, it has since become a compliance-related matter.

- Changes such as the Banking Environment Initiative (BEI) have been key.

Example – **sustainable shipment letter of credit**

- a financial solution developed by the Banking Environment Initiative that gives banks the opportunity to incentivise the trade of sustainable palm oil

- Backed by IFC, which offers preferential terms for this type of shipment to its partner banks in the form of reductions in the cost of capital

- An example of new business opportunities that are, by definition, sustainable – and there is no compliance risk in lending with the instrument.
Sustainability

- Reputation – business impact

- e.g. palm oil producer suspended from the Roundtable of Sustainable Palm Oil which led to a very public withdrawal of support from a number of its main counterparties.

- Whether it is agricultural supply chains or energy sources, increasing momentum behind sustainability as it rises up the trade and commodity agenda.

- Legal risks
Digitalisation of trade finance

- The future is digital
- E-bills of lading
- Smart contracts – provides greater level of contractual certainty by setting up code to automatically trigger contractual events based on independently verified data sources
- Blockchain – general consensus that it will revolutionise main aspects of the legal industry
- Digitisation should be sweeping across the trade finance community but HFW’s research shows three-quarters (73%) of trade financiers use no digital solutions (not yet)
E-bills of lading

- Transaction growth – up to $85 trillion flow of goods and finance by 2025 – 3x the value of 2012 (McKinsey Global Institute)
- Cargill and Bunge are spearheading eDocs across key trade lanes
- LDC ramping up use of eDocs – recently executed first ever juice shipment via CargoDocs (Brazil – Netherlands)
- ICC has launched Digitization Workgroup to evaluate ICC rules / guidelines for eCompliance (i.e. Enabling banks to accept data vs. Documents)
- ICC conducting legal review of enforceability of digital vs. Paper B/Ls when used as security for trade finance transactions
Blockchain – applications in trade finance

- Bills of Lading and Letters of Credit are well established methods of managing the shipping and financing of goods and services.
- Processes are time and labour intensive, involving multiple documents and checks to reduce risk and provide assurance to sellers, buyers and their banks.
- These processes will be made more efficient.
- Fraud reduction.
- Cut days of paper / documentation cycle (15 days?)
Question 1:
What do you think will be the main challenge to growth in 2017 in developing market jurisdictions?

- Economic slowdown: 26.2%
- Geopolitical risk: 42.1%
- Security risk and terrorism: 7.9%
- Currency volatility: 7.9%
- Low commodity prices: 15.9%
Question 2:
What do you think is the most important factor for growth in the syndicated loan market in developing markets in 2017?

- Greater uptake of standardised documentation: 7.1%
- Global macro-economic and political stability: 41.3%
- Increased supply of "bankable" transactions: 39.7%
- Development of a secondary market: 6.3%
- More regulatory certainty: 5.6%
Question 9:
Which area holds the best opportunities for lenders in CEE (including Russia)?

- Project finance: 34.5%
- Leveraged finance: 13.6%
- Acquisition finance: 11%
- Pre-export finance: 37.3%
- Real estate finance: 3.6%
Next year, where do you think the best opportunities will lie in the loan market?

Remains largely as last year, with only Emerging Markets rising from 7.6% (2015) to 12.3% making any noticeable gain.

44.9% of respondents believe political uncertainty/instability will be the principal barrier to improving growth in developing market lending at the present time.
Question 10:
Which country has the greatest likelihood for economic growth out of the CEE countries (including Turkey)?

- Russia: 31.8%
- Turkey: 12.7%
- Romania: 9.2%
- Hungary: 4.5%
- Czech Republic: 10%
- Poland: 31.8%
Question 3:
What is the most important tool in mitigating risk for lenders in developing markets?

- Thorough due diligence: 24.8%
- Effective and enforceable contractual protections: 32.8%
- Involvement of ECAs/DFIs: 23.2%
- Standardised legal documentation: 3.2%
- Insurance: 8%
- Involvement of local stakeholders: 8%
THANK YOU