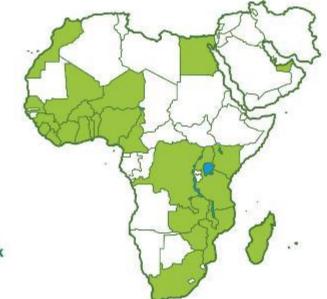
### **DRUM COMMODITIES LIMITED**

#### AFREXIMBANK

#### LUSAKA 4<sup>th</sup> – 6<sup>th</sup> NOVEMBER 2014

*"Mitigating Commodity Financing Risks Through Collateral Management Structures: Opportunities and Challenges"* 







# Contents

#### INTRODUCTION

- Challenges to traditional financiers in Africa
- Seismic event in February 2014 SGS withdraws from Collateral Management (CM) market place

#### BACKGROUND

- What are CM services and their benefits
- Compare to Stock Monitoring (SM)

#### CHALLENGES

- Tick Box mentality and short cuts by banks
- Conflicts of interests

#### **OPPORTUNITIES**

- Broadening of CM services
- Movement to SIP
- Financing needed by local banks



# Introduction

CHALLENGE TO TRADITIONAL FINANCIERS IN AFRICA

- EU based bank lending lower
- Weakness of EU economy
- Combined with Basel 3 regulations and capital adequacy requirements
- Resizing by BNPP following losses in Russia
- Litany of losses continues
- SCB and Standard Bank rumoured losses in China
- Development of new or expanding entrants e.g. ITFC, IFC
- Local banks taking up the reins



# Introduction

#### SEISMIC EVENT – SGS WITHDRAWS FROM CM MARKET

- February 2014
- Petroleum loss in Albania
- Rumour \$60 million
- Lloyds of London Underwriter withdraws from commodity & CM policies
- Forced CM's to Lloyds of London Professional Indemnity market
- Only Tier One CM departs
- Reduces credibility of CM as a risk management tool
- Basel 3 official risk mitigant continues to be crucial
- Diversification of CM role



#### **Background: Collateral Manager - Services**

Range of services

- Surveys: site, warehouse, factory, route, mine
- Standard: collateral management, stock monitoring, etc
- Logistics' studies
- Quality & Quantity certificates
- Project Management

Testing the viability of projects

Small cog in range of risk mitigants – Basel 3



#### **BACKGROUND: COLLATERAL MANAGER - SERVICES**

"Eyes & Ears" for bank or trader on the ground

- weighing, sampling, quality analysis
- fundamental stock control for the duration of the finance facility
- point organisation for stopping fraud e.g. movement trucks from the port to inland warehouse; release mechanisms



# Weighing





# Sampling





# Drying

















#### **Background: Collateral Manager - Services**

- Collateral Management services for more than one bank's financing of a specific customer's stock
- Structures in place for larger syndicated loans to a specific customer
- Audit function
- Dispute resolution
- Non-invasive monitoring during warehouse or factory operations
- Multi-commodity / Pan Africa



#### **Background: Collateral Manager - Services**

- Multi-commodity / Pan Africa
- Banks lending to a smaller range of borrowers
- And borrowers often have Pan-African destinations and requirements



### **Cement - Durban**





### **Cement – Durban**





### Tank Farm – Dar Es Salaam





### Tank Farm – Dar Es Salaam





### **Frozen Fish - Cameroon**





# Sugar - Ghana





### **Rice - Dakar**





### Wheat - Mali





### Wheat - Mali





#### Background Collateral Manager Services – Supply Chain Management

EXAMPLE: fertiliser Nigeria

- Ship to Port Warehouse; by truck & inland to warehouse / to blending plant; to finished product warehouse; to final release against sales
- Total control of the supply chain and visibility for the bank



























#### Background Collateral Manager Services – Supply Chain Management

#### SUPPLY CHAIN / PIPELINE CONTROLS

 Six receipts / warehouse warrants & six releases during the whole pipeline process



#### COLLATERAL MANAGEMENT AGREEMENT (CMA)

Security of product for bank: physical goods / collateral

- Port to warehouse supervision of movement of goods
- Provision of Warehouse Receipts to initiate the drawdown against the facility
- The release mechanisms fundamental to the repayment of the facility
- Warehouses locked & sealed
- Financial status of bank's client monitored for bank (payment of fees)



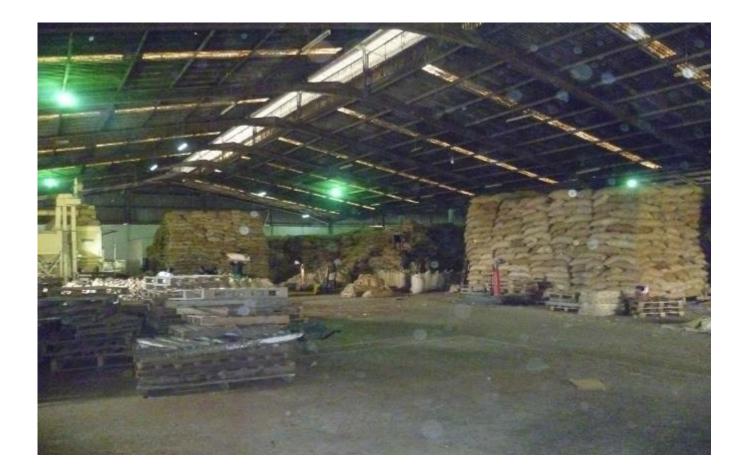
#### Background Collateral Manager – CMA versus SMA

#### STOCK MONITORING AGREEMENT (SMA)

- No security of product for bank
- Report to bank after the event
- Visual only no liability on CM
- No warehouse receipts or release procedures
- Limited comfort to bank
- Suitable for small ticket size
- SMA does not include key-holder status, therefore out of hours activity is not monitored.



#### **SMA - Monitoring & Inspection Audit – Cocoa - Lagos**





#### **SMA - Monitoring & Inspection Audit – Cocoa - Lagos**





Background Collateral Manager – CMA versus SMA

#### STOCK MONITORING AGREEMENT (SMA)

• Ultimately 'you get what you pay for'



# Challenges

#### TICK BOX EXERCISE

- Requirement from Credit Committees
- Last item for Relationship Manager (RM) to conclude with Borrower
- Who does the RM really work for?
- Plea from Bank & Borrower: "I ( = we!) will lose money if you don't reduce your fees". CMA fees are a SMALL cog in overall structure



# **Challenges**

#### PAYMENT OF FEES

- Conflict of interest: CM works for Bank but paid by the borrower"
- Patchy support from Bank if Borrower stops paying of fees
- Suddenly CM can become the Bank's "partner" in the problem as Borrower moves into recovery



#### BROADENING OF CM SERVICES

- Supply chain management from factory to port or port to inland warehouse = enhance visibility for banks
- Great control (management) of warehouse operations e.g. fumigation, sampling
- Control of documentation e.g. B/L's



#### MOVEMENT TO SIP

- Banks act as merchant repo basis
- Port focused
- Futures hedging



#### GREATER DEMAND FROM LOCAL BANKS

- Local financing rates challenged to be competitive with international banks – require greater controls
- Learning and understanding of CMA / SMA systems



#### IMMENSE VALUE OF CM AND CMA'S

- Head of Risk for Geneva based bank: "Many industries depend on the effectiveness of Collateral Management as a risk mitigant. Please continue to apply the same rigour you are known for."
- CMA structures turn a possible into a probable into a business



#### **DRUM COMMODITIES LIMITED**



