

# 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”*



**African Export-Import Bank**

*The Trade Finance Bank for Africa*

# Contents

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## 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

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## 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

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## 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

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## 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

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“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

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# Sampling

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# Drying

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# Quality

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# Storing

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## Background: Collateral Manager - Services

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- 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

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- 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

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# Tank Farm – Dar Es Salaam

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# Tank Farm – Dar Es Salaam



# Frozen Fish - Cameroon

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# Sugar - Ghana

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# Rice - Dakar

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# Wheat - Mali

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# Wheat - Mali

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## 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

# Supply Chain Management

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# Supply Chain Management

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# Supply Chain Management

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# Supply Chain Management

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# Supply Chain Management

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# Supply Chain Management

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## Background

# Collateral Manager Services – Supply Chain Management

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### SUPPLY CHAIN / PIPELINE CONTROLS

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

# Background

## Collateral Manager – CMA versus SMA

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### 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

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### 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

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# SMA - Monitoring & Inspection Audit – Cocoa - Lagos

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## Background Collateral Manager – CMA versus SMA

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### STOCK MONITORING AGREEMENT (SMA)

- Ultimately ‘you get what you pay for’

# Challenges

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## 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

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## 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

# Opportunities

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## 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

# Opportunities

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## MOVEMENT TO SIP

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

# Opportunities

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## 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



# Opportunities

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## 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

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*Questions and Answers*

