



20 October 2023
Volume 1203

Unlocking The Power of Structured Trade Finance

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In global commerce, every agricultural or primary commodity has an inherent need — to find a buyer or off-taker. This concept forms the foundation of structured trade finance.

The Basics of Structured Trade Finance

Whether used for South African or foreign trade, this financial tool plays a vital role in assisting with working capital for importing or exporting. It's more than just financing; it's the engine that propels commodities from soil to shelf.

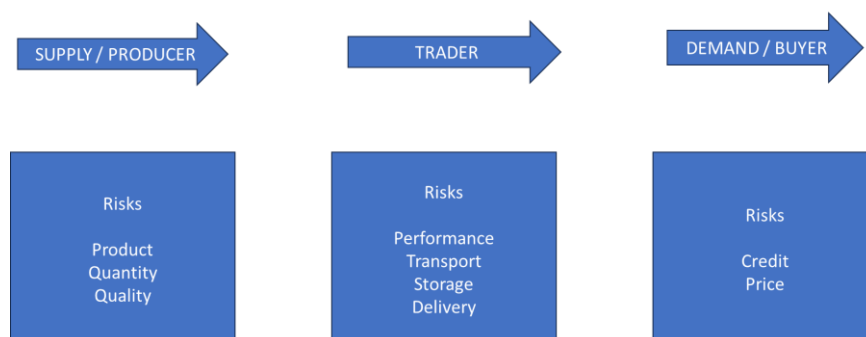
Structured Trade Finance assists stakeholders such as Producers, Traders, and Manufacturers. Its primary function is to provide short-term working capital, propelling the movement of goods along the supply chain to reach the end consumers.

The beauty of this approach lies in its off-balance sheet nature. It's not about the size of a company's balance sheet but rather about understanding the dynamics of the specific commodity and its flow within the supply chain. The risk is, therefore, taken against the commodity and its price.

Fundamentally, the most important philosophy and risks that must be taken into consideration in this respect are:

OFF BALANCE SHEET / COMMODITY FINANCING

1. Understand the business of your client
2. Understand the commodity being traded
3. Understand the risks of the above
4. Shift or mitigate the risks



Distinguishing Between Worlds

When analysing the entire supply chain of commodities, we must distinguish between first-world/developed and third-world/developing countries.

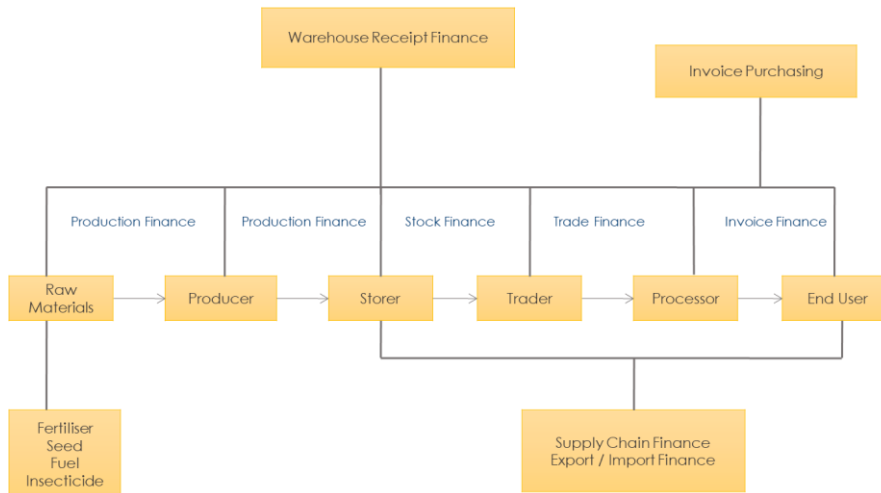
In the developed world, commodity trade financing has a long history. Financial institutions have tried and tested methods in how they want to finance various stages of the supply chain and the risks associated. Often, these factors are the size and strength of the commodity trader's balance sheet, operational capacity and trading history, trading volumes, and other available security securities unrelated to the trade.

Not all businesses fit this mould. Therefore, other financing methods must be applied, especially in developing countries and Small and Medium Enterprises (SMEs).

These typically lack the substantial balance sheets and additional security that established entities in developed countries do. SMEs are, therefore, often prejudiced and need help to secure much-needed working capital to grow their businesses, even though they have access to the commodity and off-takers.

It is in this area that actual structure commodity finance can be of assistance to the SME market. Here investors can finance various stages of the supply chain via generic financing methods, achieving above-average risk-return ratios. This allows the SMEs to gain access to funding and therefore increase their income streams and profitability.

STRUCTURED FINANCE THROUGHOUT THE COMMODITY SUPPLY CHAIN



The Path to Successful Investment

To effectively invest in structured trade finance, financiers and investors must follow a well-defined roadmap:

- Understand the market and business sector linked to the commodity.
- Gain comprehensive insights into the commodity or asset being financed.
- Evaluate, understand, and address the associated risks.
- Possess the capability to shift or mitigate identified risks.
- Establish a robust network within the market.
- Efficient administration with a "hands-on" approach.

Key Client Criteria

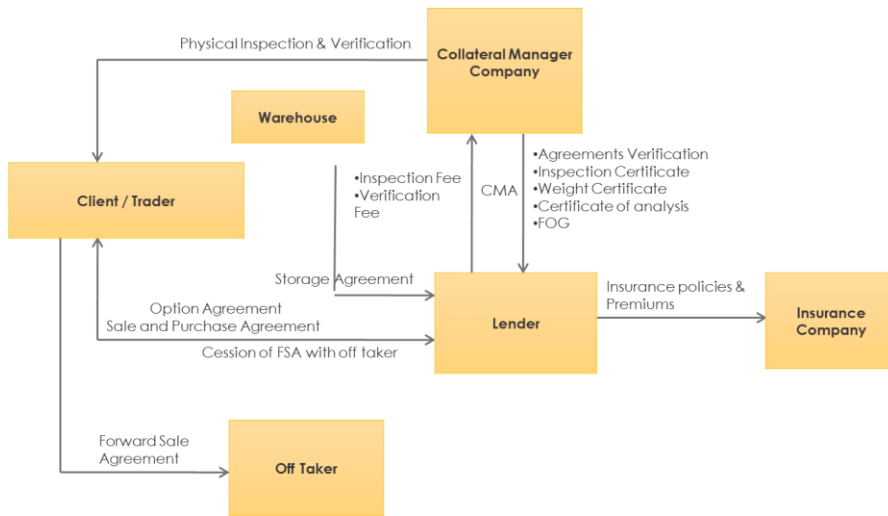
When financing a particular segment of the supply chain, financiers or investors should seek clients who meet the following criteria:

- A reputable entity in terms of financial stability, operational excellence, quality, and supplier relationships.
- A profitable trade history track record, as demonstrated by interest cover.
- A stock and trade turnover not exceeding 180 days.
- A solid, liquid asset base, as indicated by the current ratio.
- Commercial solvency.
- A strong, creditworthy off-taker or a readily tradable commodity.
- Operational and administrative efficiency.

Below, we've provided two illustrative scenarios to showcase how structured trade finance can work:

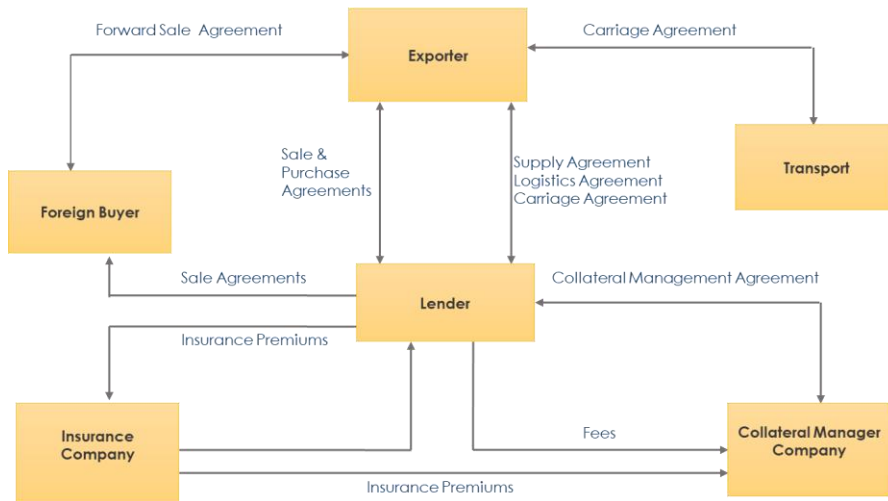
1. Imagine a scenario where a Trader or Producer needs financing while their commodity is in storage before the sale to its client — structured trade finance make it happen seamlessly.

WAREHOUSE RECEIPT FINANCING



2. In this example, we explore how structured trade finance supports a Trader needing funds to export commodities on a Free on Board (FOB) basis.

EXPORT FINANCE FOB



Conclusion

Structured trade finance is more than just finance. With the right partner, it's the key to unlocking potential in global commodity markets.

Glacier Research would like to thank Peter Martin for his contribution to this week's *Funds on Friday*.



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Having commenced a career in banking in 1981 with Barclays Bank, Peter joined ABSA in 1988 within the corporate and merchant banking division. By 1994, in response to the South African Grain and Agricultural Boards' disbanding, he started developing off-balance-sheet financing structures to fund the commodity supply chain in South Africa. Such was the success hereof that ABSA soon formed a specialised division which Peter headed up and expanded across the African continent and internationally. He later joined Barclays Bank Plc (2003) and Standard Chartered Bank (2007) at their request to form similar divisions specialising in global trade and agricultural finance. In 2011, Peter retired from Standard Chartered Bank as Global Managing Director: Structured Agricultural Finance to create similar solutions to benefit SMMEs worldwide and train banking professionals and funds in local and international structured trade and commodity finance.