

# EXTREME SPORT

It was a year of highs and lows, opening in the aftermath of the post-Lehman Brothers crash in world trade, but ending much, much busier. *TFR* talks to five trade finance professionals for their opinions of the year in review.

## THE PANEL



**John MacNamara**  
Global Head of Structured Commodity Trade Finance, Deutsche Bank



**David Sullivan**  
CEO, Trade Finance Corporation



**Peter Sargent**  
Head of Transaction Banking, Europe, ANZ



**Pierre Veyres**  
Global Head of Global Transaction Banking, BNP Paribas



**Toshio Ishizuka**,  
Global Head of Trade Finance, SMBCE

## 1. SO, HOW WAS 2009 FOR YOU?

**John MacNamara, Deutsche Bank:**

Overall, I can't complain. We managed to lead a number of the best commodity-backed deals available for some outright top-tier clients, and we managed to avoid most of the restructurings, which seem to have occupied the time of so many of our colleagues out there.

**David Sullivan, TFC:**

Quite frankly, it was the worst year in the life of TFC. The debt market and sources of funding just dried up and banks were, for most of the year, unable even to entertain new trade finance lines. For our investment banking business, non-leverage investors were waiting and waiting for the bottom of the market before they would invest.

**Peter Sargent, ANZ:**

I guess this is an answer in two distinct parts split by geography. Our business in Europe weathered the most difficult market conditions in living memory and, at a time when a number of banks took the option of 'going home' (or, indeed, did not survive at all), it is a tribute to our team that we emerged from 2009 in a robust, if somewhat bruised, state.

We completed less business, but made more from each item that we did complete. Overall, the bank had an excellent year. Indeed, its conservative approach to risk meant that its business in Australia and Asia not only survived, but benefited from the recession. We continue to expand in Asia both by acquisition and through organic growth, while maintaining the risk management ethos that enabled us to keep our 'AA' credit rating.

**Pierre Veyres, BNP Paribas:**

2009 was a year of strong developments in all regions, leveraging on our comprehensive product offer and our appetite for business, while taking opportunity of a bumpy environment.

**Toshio Ishizuka, SMBCE:**

There is plenty of demand for trade instruments and a vigorous volume of cross-border flows. Although overall global trade volumes have decreased, much of that is due to reduced demand from the US and other major economies, which are not our primary focus.

Our business comes mainly from exports of industrial goods, vehicles and manufactures from developed markets to emerging markets, transactions between emerging markets themselves such as food or fuels, and transactions from commodity trading companies. We also support trade-related transactions between firms in developed markets, such as supply chain finance, an area of growth as major corporations leverage their relative credit worthiness to extend payment periods or reduce supplier costs.

For every market that is difficult, there is a market somewhere else that is thriving, or one which offers very attractive risk-adjusted pricing. As always in emerging markets, there are sudden events. The challenge is not just to foresee them and take timely mitigating action, but also to have sufficient local knowledge to correctly

evaluate market events and not overreact to them. Many of our markets have shown resilience during this past year.

## 2. THE STIMULUS PACKAGE IN CHINA SEEMS TO HAVE BOOSTED CHINA'S ECONOMY, BUT CAN THIS LAST IF DEMAND IN THE WORLD'S NUMBER ONE IMPORTER – THE US – REMAINS DEPRESSED?

**John MacNamara, Deutsche Bank:**

I think you may get a different answer per commodity because the dynamics vary between, say, soybean imports to china compared to, say, copper imports. Also, if we look at the US, President Obama seems to have waved his magic wand over the car industry, which on its own is a large buyer of various commodities (once the things get on the road...). So it's not a *fait accompli* that either the US will remain depressed, or that China will have to reduce commodity imports.

**David Sullivan, TFC:**

The second stimulus package certainly worked after the non-event of the first one. Now, the Chinese government is more concerned about excessive lending, particularly because many manufacturers and producers have had, and continue to have, very poor order books. Also, like banks outside China, banks inside the country are diverting more funds to bigger clients only.

## **"A lot of the 'fall in trade' was precisely because of the massive drop in commodity prices from July 2008."**

JOHN MACNAMARA, DEUTSCHE BANK

**Peter Sargent, ANZ:**

The theory of de-coupling is all well and good, but China needs the US as a trading partner, both on the import and the export side. Increasingly, the relationship between the two countries is changing and the US needs Chinese investment dollars to help drive its own economic recovery.

China has used its centralised economic model to drive its own economic recovery quickly and has established its ascendancy in the 'new world order' that has emerged from the crisis. Although China makes up half of the region's GDP, Asia generally is well on the road to recovery. The trick for banks in 2010 will be to spot the countries that are producing demand momentum in their domestic economies and follow the export led flows around these economies. Recovery in Asia will be by no means uniform.

**Pierre Veyres, BNP Paribas:**

This is a key question. There is some correlation here, but one may distinguish between domestic and infrastructure projects in China compared to demand for consumer goods in China's main markets.

## 3. HOW DO YOU ACCOUNT FOR THE RECOVERY IN COMMODITY PRICES OVER THE PAST YEAR, GIVEN THE FALL IN TRADE, AND RECESSION IN MANY MAJOR ECONOMIES?

**John MacNamara, Deutsche Bank:**

Don't forget that a lot of the 'fall in trade' was precisely because of the massive drop in commodity prices from July 2008. The two largest shipped commodities in the world by value (oil and steel) both dropped about 80%, so even had tonnages remained flat (which, to be fair, they didn't), this would have hit dollar-based statistics. There was a lot of de-stocking over the winter months as people let stocks bought at higher prices run off and refrained from buying fresh inventories, which was also a component in reducing shipping volumes. But you can only de-stock once.

If you stay in business, eventually you have to start buying again. Also, you have to say that all financial exchanges, including the commodity ones, are subject to a lot of speculative interest, much of which follows very 'pro-cyclical' trading strategies: the price goes down and everyone wants to exit, so the sell-off was clearly over-done.

Interestingly, aluminium was one of the slower ones to recover, with a lot of speculative short-positioning by hedge funds in the first half of 2009, who assumed that prices wouldn't recover until the Chinese cut their relatively high-priced production, which they showed little sign of doing.

**"For every market that is difficult, there is a market somewhere else that is thriving, or one which offers very attractive risk-adjusted pricing."**

TOSHIO ISHIZUKA, SMBC

Eventually, as other non-ferrous metals, such as nickel and especially copper, steadily climbed back up. The alu price also got dragged up by association until, one by one, the hedge funds hit their 'stop loss' trigger prices and then alu leapt the last \$300 per metric tonne to current levels.

You might say copper was over-bought, but the bottom line is that commodities never go to zero. There isn't a country in the world that doesn't rely on commodities, one way or another, so while the prices go up or down there will always be some level of activity. And if production is cut back when prices are too low, the inevitable result will be price recovery. The hard part is getting the timing right.

**David Sullivan, TFC:**

Fund speculation, weak dollar. All driven by the Wall Street/London investment 'gamblers'.

**Peter Sargent, ANZ:**

We believe that many people have underestimated the level of de-stocking that took place in early 2009 and part of the surprising strength in many markets has been driven by re-stocking. The government stimulus in China helped commodity prices in the second half of the year, but there is a risk that some of the goods bought have not been used and we expect to see a choppy outlook in 2010. Having said that, as the world recovers we remain cautiously optimistic about the price of oil and, of course, gold as a safe haven.

**Pierre Veyres, BNP Paribas:**

The recovery in commodity prices has played a positive role in some regions. However, overall it remains a challenging market due to the ongoing financial crisis and the reduced demand as a result.

**Toshio Ishizuka, SMBC:**

Amongst the commodity trading companies, energy markets, are doing very well, with oil prices at moderate levels and sufficiently volatile to generate good returns. Some metals traders had to cut both inventories and costs during the past year, but have shown robust management in tackling such issues and should emerge stronger as a result.

Oil commodity exporters are beginning to tap the pre-export finance markets again, and the restructuring of a number of major metals facilities gives quiet confidence that those markets are beginning to recover, and that finance packages backed by direct legal rights to underlying goods flows can provide an effective solution.

**4. HOW WILL SUCH ISSUES AS THE AVAILABILITY OF INSURANCE AND THE IMPACT OF BASEL II ON BANKS' WILLINGNESS TO FINANCE TRADE AFFECT EXPORTERS IN 2010? WHAT OTHER DANGERS DO YOU FORESEE?**

**John MacNamara, Deutsche Bank:**

Actually, the insurance market remained reasonably open throughout the crisis, so there was no particular problem from the supply side. Rather, the problem is on the demand side because the whole world is discovering it and many are dumping assets, so offer higher prices to underwriters to get the capacity.

It will be interesting to see what happens if anything goes wrong, because insurers rely on insureds to know what they are doing (especially in recovery) just as much as insureds rely on insurers to pay out in case of loss.

**David Sullivan, TFC:**

Insurance capacity has dried up since the Summer of 2009, but who can blame the insurers, with banks not lending, banks wanting to share less of the risk and, in some cases, more easily resorting to claims.

**Peter Sargent, ANZ:**

While the lack of availability of insurance remains a problem, the real issues for me in 2010 are much more around the lack of a secondary market, the issue around capital allocation for trade deals (ie. Basel II) and the lack of an industry wide body to lobby for change (although BAFT has done a good job in that respect). I also remain concerned that too many people are deluding themselves that the end of 2009 brings an end to the recession and that we can just go back to the good old days. Equally and conversely some of the risk professionals in the market need to understand that just saying 'no' is not risk management. 2010 will need focus and all banks should implement a very clear trade strategy that links closely into the overall strategic approach of individual banks.



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DAVID SULLIVAN, TRADE FINANCE CORPORATION

**Pierre Veyres, BNP Paribas:**

The way trade finance is handled under Basel II requires some fine tuning so that the resilience of that business in difficult environments, especially in tough times, is fully recognised – not penalised. In the meantime, some consistency at the global level is expected so that major international banks and local players can compete with each other on an equal footing.

**5. WHERE WILL THE NEW OPPORTUNITIES BE FOUND IN 2010?**

**John MacNamara, Deutsche Bank:**

Well, I'm hopeful that pre-export finance and borrowing base still has a role for clients before capital markets fully recover. The Dubai affair is probably good news because, hopefully, it will discourage people from being too aggressive to take unsecured risks, or risk secured on collateral other than commodities. We also anticipate much greater coagulation of risk mitigation in deals – so collateral, insurance, hedging and so on all coming together in deals to provide solutions robust enough to survive multiple changes in the overall business environment.

**David Sullivan, TFC:**

Trade finance will be on the up and, for an intermediary like us, the ability to recover business volume with simple products. At some point, we are meant to come out of this ‘fish tank’ bottomed recession, correct? So there should be lots of things cooking again. One thing is for sure, another year of the same Hong Kong housing market and I wonder whether parking spaces will break the \$1m barrier...

**Peter Sargent, ANZ:**

2010 will see the continued rise of Asia. Banks looking for growth have to be prepared to follow the flows of their clients into and out of the region. From a product point of view, cash and trade (and

transactional services generally) are seen as a core offering for most of the surviving banks. But offerings have to be closely aligned to the banks' geographic client base, accelerating the growth of partnerships between regional specialists – such as ANZ.

**Pierre Veyres, BNP Paribas:**

2010 will be very attractive in all regions, and Asia will be on the front line. From a product perspective, supply chain financing has become a key priority for large corporates, including the ones unaffected by the crisis. All players have realised that disciplined management of capital is one of the key metrics that they must get right.

**Toshio Ishizuka, SMBCE:**

We have expanded our cooperation with the major export credit agencies (ECAs), multilateral institutions (such as International Finance Corporation and the Asian Development Bank) and private insurance firms, as well as our presence in the secondary market. So long as the underlying transaction itself is sound, the contribution of ECAs and other support can be very positive. This has helped us provide support to a wider range of clients than we could otherwise have done.

There is lots of scope to automate the trade finance process, especially invoice discounting and supply chain finance, through the use of web-based technology solutions and so on. In times of scarce capital, we constantly refine our internal models to most closely reflect the risks.

The market is huge and very varied. To decide where to focus we look at fundamentals, we stay close to our clients, and we seek to expand the envelope of our services along the length of the trade flow. Markets are very dynamic and we constantly adjust our strategy accordingly.

I am quietly confident that trade finance will be seen to have been resilient and flexible in today's turbulent and dynamic markets. □