



CREDIT SUISSE 

## Commodities and Trade Finance Risks and solutions



Guy Barras, Head of Trade Finance Services, Geneva  
October 5, 2015

---

---

---

---

---

---

---

---

---


---

## Commodity Trade Finance (CTF)

**Overview**

The exchange of goods is one of the oldest forms of trade in the world and has been practiced for as long as mankind has been on the planet. Initially, surplus goods were traded for essential items, arms or luxury goods. Only with the introduction of money did trading become more artificial. Trading houses were founded with the aim of obtaining excess goods or raw materials of all kinds. Such goods were often produced in extremely remote, dangerous and exotic places. As early as the 17th century, banks in Italy started lending money to trading houses who specialized in importing silk and spices from the Far East. These items were marketed to European royalty, industrialists or other wealthy individuals.

Over the years, banks have developed trade finance into a common but more sophisticated instrument. Its purpose is to give financial support to specialized trading companies which do not have sufficient working capital to purchase and ship unprocessed raw materials (commodities) from overseas colonies to Europe. Nowadays, commodity finance has a firm place in the banking world. The basic principle remains to grant loans to raw materials traders. The traders employ this working capital to purchase crude oil, metals, minerals or agricultural goods from producers and repay the loan using the proceeds from reselling the goods. Pre-export finance, crop finance, inventory finance and receivables finance are all types of commodity finance.

CREDIT SUISSE  Guy Barras, Head of Trade Finance Services, Geneva October 5, 2015 2

---

---

---

---

---

---

---


---

---

---

## Definitions and questions

<p><input type="checkbox"/> Commodity :</p> <p>"Any usefull thing" "Anything bought and sold"</p>	<p>➤ <i>Is this commodity known ? Is this commodity regularly traded ? Is the price of this commodity fixed on a regular (even daily) basis ? Is the quality of this commodity standardized ?</i></p>
<p><input type="checkbox"/> International Trade :</p> <p>"The exchange of goods and services across international boundaries or territories"</p>	<p>➤ <i>From which country through/to which country(ies) goods will transit, be transported ? By which means of transport ?</i></p>
<p><input type="checkbox"/> Trade financing :</p> <p>"To supply or get money" (for purchasing and selling goods)</p>	<p>➤ <i>Do we (bank) lend to reputable and professional trader ? Does this trader dispose at least of minimum financial ressources for absorbing payment delay, additional expenses in case of "Force Majeur" or other incident ?</i></p>

CREDIT SUISSE  Guy Barras, Head of Trade Finance Services, Geneva October 5, 2015 3

---

---

---

---

---

---

---

---

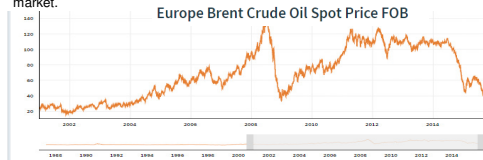
---

---



### Challenges of Global Economy & Global Institutions

- Global economic outlook remains deeply uncertain.
- Weak sovereign balance sheets of certain countries.
- Measures of reforms of the financial sector → Basel III.
- Acceleration of cyclical phenomenon of increase/decrease of prices and volatility of the market.



- Preserving the reputation and standing of the firm and competitiveness.
- Protecting the firm of possible fines (e.g. accusations of violations of applicable sanctions)

---

---

---

---

---

---

---

---

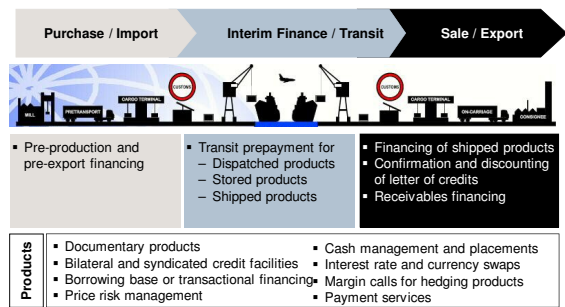
---

---

---

---

### CTF business offers different financing types during the value chain of the physical trade of the commodities




---

---

---

---

---

---

---

---

---

---

---

---

### Other factors

- Emotional, affective
  -
- Economical pressure
  -
- Emergency
  -
- Past paradigm
  -
- Remedies : Independent re-assessment through :
  - Colleagues, manager,
  - Credit unit,
  - Credit committee,
  - IMB,
  - Commodity specialist,
  - Carriers,
  - Inspectors,
  - Legal & compliance
  - ...

---

---

---

---

---

---

---

---

---

---

---

---

### Business case – Oil financing

- ❑ Financing the FOB purchase/ CIF sale of 1.0 mio. u.s. bbls of REBC (Russian Export Blend Crude Oil) payable 120 days after shipment date.
- ❑ Company to be financed : Trade Oil SA, Geneva (a newly formed registered company with USD 3.0 mio. equity. Management well known to the bank and past performance proven).
- ❑ Buyer : BP Oil Int'l Ltd, London 
- ❑ Suppliers : JSC Oil Company "Rosneft", Mosc 
- ❑ Purchase Incoterms : **FOB Baku, Azerbaijan.**  
Price : Platt's published quotation on b/l date, less USD 2.00 per bbl. (clause shortened for sake of simple example).
- ❑ Selling Incoterms : **CIF Rotterdam.**  
Price : Platt's published quotation on b/l date, plus a premium of USD 3.00 per bbl. (clause shortened for sake of simple example).

→ **Question** : How to assess this transaction if, in the bank's shoes, you are asked to finance this trade (purchase/sale of a/m oil cargo flow) with a current market value of approx. USD 45.0 mio. ?

---

---

---

---

---

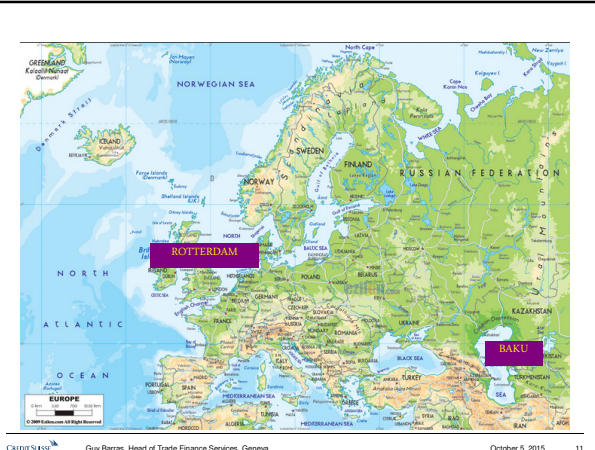
---

---

---

---

---



---

---

---

---

---

---

---

---

---

---

### An explosive cocktail !



---

---

---

---

---

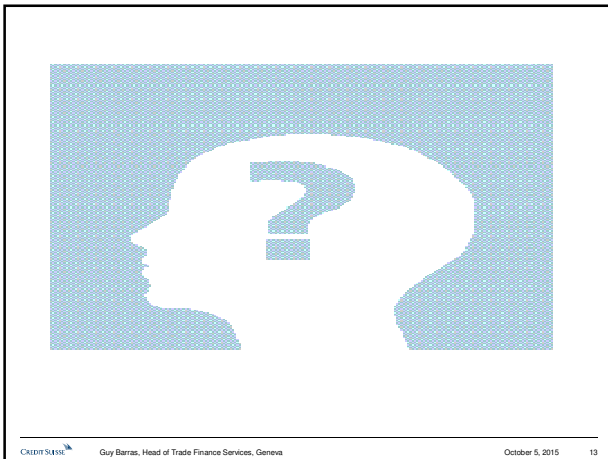
---

---

---

---

---



CREDIT SUISSE Guy Barras, Head of Trade Finance Services, Geneva October 5, 2015 13

---

---

---

---

---

---

---

---

**«Red Flags» when processing Trade Finance transactions**

- The customer engages in transactions that are inconsistent with the customer's business strategy (or profile), or make no economic sense
  - *E.g. : A steel company that starts dealing in precious metals.*
- A customer deviates significantly from their historical pattern of trade activity
  - *E.g. : Goods totally out of line with customer's known business.*
- Transacting parties appear to be affiliated, conduct business out of a residential address, or provide only a registered agent's address.
  - *E.g. : L/c counterparties : Connected applicant/beneficiary.*

CREDIT SUISSE Guy Barras, Head of Trade Finance Services, Geneva October 5, 2015 14

---

---

---

---

---

---

---

---

**«Red Flags» when processing Trade Finance transactions**

- Customer conducts business in jurisdictions that are at higher risk for money laundering, terrorist financing or other financial crime.
  - *E.g. : The commodity is shipped to (or from) a jurisdiction designated as «high risk» for money laundering activities.*
- Obvious over or under pricing of goods and/or misrepresentation of quantity of goods shipped.
  - *E.g. : Significant discrepancies appear when comparing known market value and/or abnormal weights for shipped goods are suspected.*
- The payment terms or tenor are inconsistent with the type of goods.
  - *E.g. : Unusal favorable payment terms, with beneficiary's insistence to obtain the discounting (advance) of the deferred payment.*

CREDIT SUISSE Guy Barras, Head of Trade Finance Services, Geneva October 5, 2015 15

---

---

---

---

---

---

---

---

**«Red Flags» when processing Trade Finance transactions**

- Transaction structure and/or shipment terms appear unnecessarily complex or unusual and designed to obscure the true nature of the transaction.
  - *E.g. : The commodity is transshipped through one or more jurisdictions for no apparent economic reason.*
- The l/c contains non-standard clauses or phrases or has unusual characteristics.
  - *E.g. : Contracts or l/c contains clauses such as : «Ready, willing and able», «divisible and assignable», «proof of product», «funds are good, clean, cleared of non-criminal original». → A «competent» Trade Finance bank issuing a letter of credit subject to UCP600 shall not use those words.*

---

---

---

---

---

---

---

---

---

---

**«Red Flags» when processing Trade Finance transactions**

- The l/c is frequently significantly amended for extensions, changes to the beneficiaries and/or changes to payment locations.
  - *E.g. : Payment to be made to beneficiary's account held in a country other than beneficiary's rational location. Advanced waiver of discrepancies.*
- The transaction appears to involve the use of front or shell companies for the purpose of hiding the true parties involved.
  - *E.g. : Unexplained third parties, payment instructions are illogical or changed at the last minute. Customer is reluctant to provide clear answer. Excessive, aggressive pressure by the client.*
- Trade related documentation altered or certain documentation is absent.
  - *E.g. : L/c purportedly covers the movement of goods but fails to call for presentation of transport doc.*

---

---

---

---

---

---

---

---

---

---

**Recommendations**

International trade offers a lot of opportunities, unfortunately however, it is also a popular target for **fraudsters**. In order to prevent parties from any risks and/or losses, it is of utmost importance to assume due care when transactions are presented.

**Possible remedies**

- Compliance standards have to be fulfilled. Trading with commodities is a specialized business and all parties should be able to assess and judge the inherent risks. Actors in this business field must have a knowledge of the market and can show some past experience.
- It is advisable to immediately establish links to specialists for commodity trade finance. Specialist's experience will allow to determine the feasibility of a transaction at an early stage already.
- The key stone to secure payments in international trade remains the documentary credit (letter of credit) as the most popular and best compromise for banks, buyers and sellers.

---

---

---

---

---

---

---

---

---

---

## Questions and Input ?



---

---

---

---

---

---

---

---

This document was produced by Credit Suisse AG and/or its affiliates (hereafter "CS") with the greatest of care and to the best of its knowledge and belief. However, CS provides no guarantee with regard to its content and completeness and does not accept any liability for losses which might arise from making use of this information. The opinions expressed in this document are those of CS at the time of writing and are subject to change at any time without notice. If nothing is indicated to the contrary, all figures are unaudited. This document is provided for information purposes only and is for the exclusive use of the recipient. It does not constitute an offer or a recommendation to buy or sell financial instruments or banking services and does not release the recipient from exercising his/her own judgment. The recipient is in particular recommended to check that the information provided is in line with his/her own circumstances with regard to any legal, regulatory, tax or other consequences, if necessary with the help of a professional advisor. This document may not be reproduced either in part or in full without the written permission of CS. It is expressly not intended for persons who, due to their nationality or place of residence, are not permitted access to such information under local law. Neither this document nor any copy thereof may be sent, taken into or distributed in the United States or to any U. S. person (within the meaning of Regulation S under the US Securities Act of 1933, as amended). Every investment involves risk, especially with regard to fluctuations in value and return. Investments in foreign currencies involve the additional risk that the foreign currency might lose value against the investor's reference currency. It should be noted that historical returns and financial market scenarios are no guarantee of future performance. Emerging Markets are located in countries that possess one or more of the following characteristics: A certain degree of political instability, relatively unpredictable financial markets and economic growth patterns, a financial market that is still at the development stage or a weak economy. Emerging markets investments usually result in higher risks such as political risks, economical risks, credit risks, exchange rate risks, market liquidity risks, legal risks, settlement risks, market risks, shareholder risk and creditor risk. Investors should be willing and financially able to accept the risk characteristics of the investments described in this documentation. Copyright © 2015 Credit Suisse Group AG and/or its affiliates. All rights reserved.

---

---

---

---

---

---

---

---