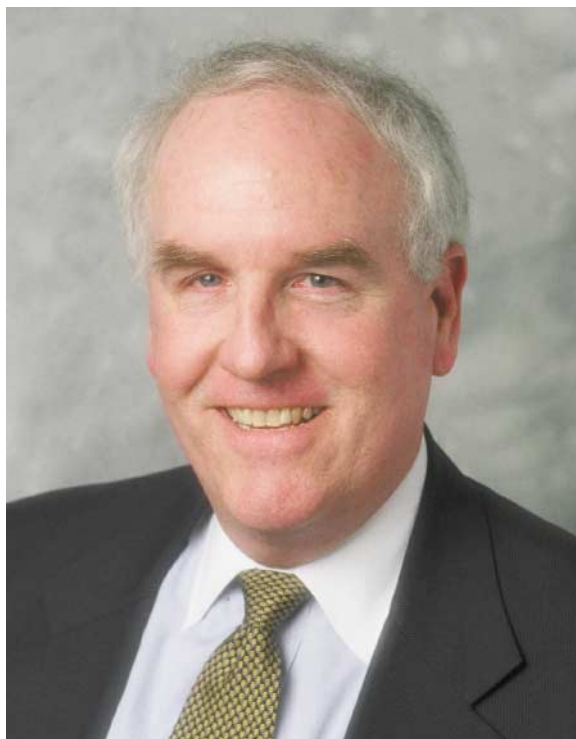


Re-discovering trade finance in North America

The action in trade finance these days is in Asia, the Middle East, Eastern Europe and Russia where financial action, offers profitability and compelling returns, but also endorphin flow for trade bankers. The excitement of being in hot markets and doing challenging deals keeps risk managers awake at night, and also makes for great ‘war stories’. But is this really the trade finance landscape today? The global engine of export trade may well be China, but the other half of that equation is still the United States, as the leading importer, and economic superpower. Alexander Malaket assesses the action.

The allure outside of North America

There is much potential, and significant interest in international trade and trade finance in various parts of the world, including China, India and Brazil. The growth of trade finance programmes supported by multilaterals such as the European Bank for Reconstruction and Development (EBRD), Inter-American Development Bank (IADB) and others is indicative of cautious interest in certain higher-risk markets; Dubai’s



Bruce Proctor at JPMorgan Chase in New York

active efforts to position as a regional trading hub have resulted in several high-profile initiatives in the UAE, and the hardiest of trade financiers continue to look to parts of Africa for high-risk, high-margin business.

The view from North America

The crisis in the Chinese capital markets earlier this year, as well as some recent concerns about product quality and safety may bear out certain investment advisors who have been claiming that the market is overheated, or, the market may prove so resilient and rooted in waves of positive expectation, that such ‘blips’ will be a passing memory.

Peu importe – it matters little: bankers are re-discovering North America as an appealing, if less exotic, market for trade finance. In part, that is because the region provides the ‘second half’ of trade relations with India, China and others, and in part, because the trade dynamics under NAFTA (North American Free trade Agreement) create leading-edge needs and expectations among importers and exporters in Mexico, Canada and the United States.

Even with the crisis linked to the US sub-prime market – a ‘crisis of exotic instruments’, and an acknowledged ‘liquidity crunch’, despite near-parity between two currencies on the continent, and even with growing business relations between Mexico and China, the potential for trade finance in North America merits attention.

North America, which comprises three trading partners at varying levels of power, development and financial stability, provides an interesting context for the development and delivery of trade finance solutions. Proximity to Brazil and other markets in Central and ▶

► South America, adds to the interest and potential.

Export Development Canada (EDC) has been communicating the concept of ‘integrative trade’ – the evolution of trade beyond traditional import/export silos, to a situation where global sourcing sees exporters often importing elements or components for inclusion into a final product, and where direct investment is closely connected to international trade. The implications of integrative trade are significant for an export credit agency, its mandate and scope of activities, just as they are significant for global supply chains and trade financiers.

Kevin O’Brien, SVP, financing products group at EDC notes: “Globalization and the advent of integrative trade are reshaping the reality of international business and trade: EDC is working to identify innovative solutions to the changing needs of our clients. We are a commercially-oriented ECA, and as such, we are responding to new sourcing patterns, the increasing importance of investment, and other shifts in the nature of global trade.”

Trade market trends

Trade and trade finance continues to exhibit consolidation across the industry, from banks to technology solution providers, to freight forwarders, brokerage houses and others. There is an ongoing aggregation of trade-related capabilities into increasingly larger organizations, serving customers that value a ‘one-stop shop’ approach.

Investments in technology and integration of capabilities, including product/service offerings such as trade and cash management constitute an additional key trend, which, successfully executed, is seen as a powerful differentiator among trade banks.

Leading trade players – including banks – are working to broaden the definition of trade and the elements of trade they support. For one major bank at least, the conclusion is clear: help clients to buy and sell effectively in international markets, allowing those clients to focus on their core business.

Bruce Proctor, head of global trade services at JPMorgan Chase notes: “Corporate and mid-market clients are looking for a solutions discussion – they are far less interested in a conversation around processing efficiency and letters of credit: car buyers do not concern themselves with the factory in which the car is produced, and much in that way, trade is shifting away from a commodity, factory-based transaction product, to an integrated solution for international business. We need complete solutions, and the time is ideal to seek partnerships across functions and across geographies, in the development and delivery of such capabilities.”

Refining the value proposition

Within that context, there is a clear move among certain banks to shift from a credit or product-driven approach to a client-centric approach to the business of trade finance.

Observes Sanjiv Sanghvi, CEO of the Wells Fargo HSBC Trade Bank: “We are taking a customer-centric approach to trade, responding to client needs in our chosen markets. In a business that has been traditionally

very transaction-driven, we are looking holistically at the relationship between trade finance and our customers’ global supply chains, and offering comprehensive solutions which include asset-based lending, international factoring and in-market financing.”

Trade finance providers in North America continue to work on an effective offering to respond to the continuing shift to open account trade. The emphasis on open account is problematic for suppliers with limited access to capital, which is creating a need for a larger numbers of transactional loans, including pre and post export lending in emerging markets. Larger players are looking to match payment terms to inventory carrying terms.

Small and medium-sized businesses continue, despite much rhetoric to the contrary, to be short-changed in terms of trade finance services from traditional sources – a simple matter of scale and economics.

Scott Shepherd, president and CEO, Northstar Trade Finance, observes: “Northstar Trade Finance, and our affiliate companies continue to partner with export credit agencies and banks, to ensure that small and medium-sized businesses engaged in international trade, are provided with support and services to enable success in the global marketplace – support which surpasses the poor standard of attention generally accorded to this undervalued segment of the market”

An increasing focus on business solutions across all segments and transaction types has driven a number of banks to develop highly customized information technology solutions; some now wonder whether that approach was optimal, observing that the market is currently shaped by strategic acquisitions, technology-based partnerships and joint ventures, and variations thereof. Large customers – global players and increasingly, companies that would be qualified as “second-tier” in terms of international business, are in need of highly custom solutions, even as both groups continue the shift towards open account on a global basis.

Every trade bank, from regional and mid-tier, to global, is working on the value proposition best seen to fit current (and emerging) requirements and expectations.

Dan Fisher, senior vice president, global transaction banking, national trade business and product development, HSBC in New York, notes: “Trade is alive and well; although the decline in the use of traditional trade instruments is widely acknowledged, trade itself is growing – we need to think about trade differently, to develop new processes around trade finance...we are actively looking at systemic solutions, and are committed to significant levels of technology-related investment in response to developments in the market”.

The process of sourcing and procurement among corporate/commercial clients is increasingly global, and showing signs of accelerating, as well as innovating. One challenge identified by a senior US trade financier, is to ensure that the costs of maintaining a global supply chain infrastructure (administrative costs, inventory build-up, delayed payments, overall balance sheet impact) do not exceed the benefits. Such assessments require a high level of visibility into the client supply chain.

A number of trade banks are looking to provide tools

and utilities – mostly technology-driven – to allow clients to better managed their business on a global basis.

At Bank of America, the view according to Paul Johnson, SVP, trade and supply chain product manager is that: “Over the last 4-5 years in particular, trade banks have been expanding the definition of the business we are in. At Bank of America, we are working to provide an end-to-end solution, including the management of information around the shipment of goods, to an increasingly globalized client base – fully 87% of our mid-market clients are involved in cross-border trade.”

A view that links closely to the pursuit of end-to-end solutions is the idea of ‘self-financing’ global supply chains. According to Erik Wanberg, managing director and trade head, North America, Citi Markets and Banking, the bank sees: “Continuing evolution in supply chain platforms, covering the full procure-to-pay cycle, linking customers and suppliers across the globe, and doing so with a view to optimizing global supply chains, ensuring efficiency in working capital and reducing the need to secure financing from the market.”

Well-designed, highly integrated global supply chains can be insulated from external shocks. Once a customer and its suppliers are on a platform, and parties have adequate visibility relative to transaction status (invoice dispatch and acceptance, inventory flow-through), a trade bank can finance a flow of goods, rather than addressing transactions on a one-off basis, enhancing the quality of the transaction, and presumably providing some pricing advantage to customers.

Trade, FI's and outsourcing

Changes in the trade business, as well as in the various markets globally, continue to support the case for outsourcing of trade operations by smaller and mid-tier trade banks. Technology enables these relationships in economically viable ways; the traditional case of the mid-level bank offering trade as a loss-leader to main-

tain a full suite of commercial/corporate banking solutions remains, yet there are other dynamics evolving in the FI-to-FI space (aka Correspondent Banking): partnerships that are enhancing trade delivery capabilities.

John McFadden and Michael Schmittlein within global trade services at Wachovia indicate: “The trend of consolidation of trade finance providers continues – partly through outsourcing of operations due to unsustainably expensive technology investments. Outsourcing is becoming a strategic choice rather than merely a cost-cutting exercise, and we see the potential for this business increasing, in North America and elsewhere. Outsourcing of operations has gained a degree of acceptance that allows full disclosure to the market, and has resulted in Wachovia becoming a value-added partner to our client banks, providing the necessary processing capability as well as shared thought-leadership.”

Certain banks are re-defining the nature of correspondent relationships in trade finance – or at least, shifting the emphasis from reciprocal letter of credit (LC) referrals to a business development and maintenance effort, that allows these institutions to replicate the ‘global footprint’ model to some degree, through correspondent banks. Wells Fargo refers to this as ‘Virtual Global Banking’.

Steve Bash, EVP, international division manager, global correspondent banking, at Wells Fargo HSBC in San Francisco notes: “Technology will continue to revolutionize the way we do business, but we must focus on our client. Without that focus and commitment, the value of the IT investment falls away. We also work with our correspondents to understand their client.”

North America: the frontier is back?

Is it possible to argue that North America represents a sort of a trade finance ‘frontier’, in the world we know today?

Certainly not in terms of the risk elements of trade finance. We know that certain trade risk insurers view Canada and the US as one ‘domestic’ market, and will not issue political risk cover on transactions crossing the longest undefended border in the world.

Surely not in terms of the complexities related to protectionist trade, financial instability, or even a demand for interesting project finance solutions.

There is one sense, however, in which this market is indeed a frontier of trade finance, and that is in relation to the increasing focus on open account trade, and the emerging value propositions around supply chain finance.

With the great majority of trade under NAFTA conducted on an open account basis, and with the resources, wherewithal and capacity to develop expensive, IT-based custom solutions in response to evolutions in international trade, North America may indeed be the cradle of the evolution of trade finance. It is no accident that Mexico has succeeded in developing a trusted open account platform, and quite understandable that several ground-breaking steps in the evolution of trade finance originate in North America.

It is indeed, a good time to ‘rediscover’ North America in trade finance, for reasons which go beyond the next quarter’s financial results. ■



Michael Schmittlein at Wachovia in Philadelphia