

# Punching above their weight class?

*Alexander Malaket examines the state of trade finance and transaction banking in Canada, as Toronto welcomes leaders in the world of finance for Sibos 2011.*

Much has been made of the resilience of the Canadian financial sector in the face of the worst global economic crisis in decades, and indeed, the praise and positive messaging around the Canadian regulatory and financial environment was, it appears, well-founded.

Canadian banks are among the healthiest and best-capitalised in the world today, and while most Canadian-headquartered institutions remain regionally focused in terms of their activities and presence, there is a decided optimism and cautious pride among transaction bankers here.

#### **Opportunity in crisis**

At the risk of overusing an already abused idea – the notion of a seed of opportunity residing at the core of

crisis, the match-up between this concept and the experience in Canada practically demands that this be an element of the discussion around trade and transaction banking.

Canadian banks had, as a group, limited exposure to toxic assets linked to sub-prime lending, and, in part because of robust regulation, were then, and remain today, very robust from a balance sheet and capital adequacy perspective.

Equally important for the long-run, the crisis helped to reduce tension between the trade banking groups and Export Development Canada (EDC), the national ECA. Historical tensions about complementary versus competitive positioning of EDC vis à vis the banks have given way to a recognition that EDC's interventions during the crisis were invaluable in supporting trade finance and the conduct of international commerce.

Finally, Canadian institutions have enjoyed an enhanced profile in the marketplace, both for their commitment to existing clients through rough waters, and for their ability – and willingness – to step in a respond to the needs of businesses left reeling by crisis in the US and European financial sectors,

Canada as a nation has earned and enjoyed a level of quiet but effective influence in international affairs – including business – that has been, arguably, disproportionate to the size and economic power of the nation. That remains broadly true today despite some recent changes in direction that have diluted this historical positioning, and much in the same way, Canadian banks are also 'punching above their weight class' particularly in trade finance and some aspects of transaction banking today.

The experience of CIBC is perhaps illustrative.

"Trade finance is enjoying a renaissance period despite a strong Canadian dollar and volatility in commodity prices," notes Silvia Brudar, head of trade finance and financial institutions at CIBC. "CIBC's enhanced focus on transactional services fits in very ➤



Sara Joyce at BMO in Toronto

## Trade Finance in Canada

► well with the direction of our customers: we see treasurers taking on a much more strategic role in managing working capital flows and counterparty risks. Our strong value proposition in trade and transaction banking continues to evolve through strategic alliances and an ongoing focus on helping our clients succeed.”

The resilience of the Canadian market – forced or not, by circumstances, is further illustrated by the ability of Canadian businesses, exporters in particular, to respond to a crushing appreciation of the Canadian dollar against the US currency. Exporters accustomed for decades to operating in an environment where exchange rates facilitated a price-competitive posture and sales strategy, have been forced to respond to a new reality where the Canadian dollar is now well above par, and a currency-based margin of thirty percent or more, no longer exists. Relatedly, Canadian businesses have been forced to look beyond the familiar and favoured US market, shifting trade to Asia and elsewhere in light of the reduced demand from the world’s largest consumer economy.

The shift, which has seen 10%–15% of Canadian exports shift away from the United States, has forced Canadian trade and transaction bankers to follow their customers to new markets, and therefore to ensure that product and solution mixes are adjusted to respond to perhaps more complex transactions, with a more significant element of risk mitigation.

Benoit Daignault, senior vice president at Export Development Canada (EDC) in Ottawa, observes: “We are bullish on the Canadian market and on the successful engagement of Canadian businesses in international markets. A core group of companies are increasing the scope of their international activities, and EDC is there in partnership with the banks and other providers, to support the success of Canadian businesses. We perceive that the need for financial intermediation will increase; the importance of partnership has been clearly demon-

strated, as has the importance of maintaining such partnerships across trade and business cycles.”

### Market highlights

Canada is certainly benefiting from the commodity boom, including significant demand from China, which in part sustains the nation’s economic health, and contributes to positive-trending trade figures. At the same time, efforts continue to revitalize the critical automotive and manufacturing sectors, while concurrently advancing value propositions in the service sector and areas like bio-technology, geomatics, green energy and other sectors.

The market for trade finance and transaction banking is described as robust and competitive, with some evidence of entry by US banks. The Canadian market is adequately liquid, and price-competitive, and the banks suggest that their risk appetite today is sufficient to meet the requirements of the market. Says one senior banker: “I am not aware of any deals that are not getting done at the moment.”

“Canada continues to do well under challenging economic and business conditions, and through the integration of our transaction businesses we are even better able to respond to the growing and evolving needs of our business and financial institution clients,” says Phil Griffiths, head of global transaction banking at CIBC. “By combining the product, sales and service functions for all of our global transaction businesses, we are able to provide integrated solutions with speed and flexibility.”

Although Canadian banks have climbed the ranking of financial institutions by asset size over the last couple of years, the businesses they serve are, as a result of the size of the Canadian market, largely in the mid-market, with some notable exceptions. Trade and transaction bankers are referring to a new focus on servicing a ‘mid-market sweet spot’ in the commercial banking segment. In addition to a degree of concentration of businesses in this segment, part of the motivation for this shift likely relates to the attractive pricing and margins available to trade and transaction bankers in this segment – some suggest two or three times what can be earned from large corporate clients.

Akhil Lamba, managing director, TD Securities, notes: “At TD, the strength of our balance sheet, coupled with our market position and credibility as an institution, allows us to provide a world-class product, very effective and competitive solutions in the trade and transaction banking space, and a compelling value proposition overall, to the clients and markets we serve. We perceive the emergence of a certain equilibrium in the global market for trade finance, and our view is that the Canadian marketplace is currently well-served, exhibiting a healthy competitive energy, sound liquidity and adequate pricing. We are monitoring developments particularly in the area of supply chain finance solutions, which to date do not appear to be generating the levels of interest among Canadian corporates which are in evidence in certain other markets around the world.”

While some trade financiers are fully engaged in the development of solutions around supply chain finance,



Ben Arber at HSBC Bank Canada in Toronto



**Dyanne Carezza**  
at Scotiabank  
in Toronto



**Silvia Brudar** at CIBC  
in Toronto

particularly the few international/global banks with meaningful presence in the Canadian market, the tendency overall seems to be to observe and await developments. As one banker noted, anchor-based supply chain programmes are gaining traction in international markets, typically developed around the supply chains of large buyer entities. The challenge for Canadian businesses (and therefore their bankers) in this model, is that the Canadian buyer can often find itself facing significantly larger suppliers, and therefore lacking leverage to 'onboard' a supplier to such programmes, when the supplier may have a stronger balance sheet and the ability to finance its requirements at more attractive rates.

Others perceive and describe a rather more robust dialogue around transaction banking and supply chain finance in particular. John Stockton, director, working capital and structured solutions sales at Bank of Montreal, comments: "We see significant interest among our clients – across all segments, from large corporate to SME – in the subject of supply chain finance, including those clients accustomed to conducting trade on the basis of traditional instruments. All our customers are looking at, or have developed, working capital management initiatives, though there is still a degree of caution around the concept and mechanics of supply chain finance."

CGI, a Canadian-headquartered, internationally active technology provider and consultancy with a specialist practice in the trade and transaction banking space, brings a unique perspective to the state of the

Canadian market in the context of trends in North America and globally. Frank Tezzi, director, trade and supply chain group, notes: "The banks we are privileged to work with are clearly doing their homework, and are very aware of, and linked into, the evolving needs of their end-clients in trade and transaction banking. Customer focus is a consistent theme, and certain banks are looking for a technology platform such as Trade360, which supports global capabilities."

Canadian banks have demonstrably 'stepped in' to fill certain gaps in capacity left by US or European institutions retrenching domestically, or scaling back international activities in the wake of the global crisis. The collective strength of bank balance sheets, and the relatively liquid position of the leading institutions in Canada motivate, at a minimum, a continental outlook on business growth and opportunity, and in some cases, a significantly more international view than might have otherwise been the case.

Sara Joyce, executive managing director, head of international financial institutions and trade finance at BMO, reflects this evolution, observing: "At Bank of Montreal, we are committed to being a full-service trade bank, providing a full range of working capital solutions, from technology and automation solutions, to traditional trade products, to supply chain finance. We are working closely with our customers – and with partners such as EDC in Canada, and Exim Bank in the United States – to develop and deliver the solutions required by our clients."

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## Trade Finance in Canada

### Looking ahead

As has been the case in many markets, there has been a concerted effort among several of the Canadian banks to integrate capabilities, and service offerings, under a transaction banking 'umbrella' organisation, commonly covering trade, supply chain, cash management, payments and foreign exchange, as well as financial institution (correspondent) relationships.

Progress is evident, but the work continues. Kitt Carswell, senior offering manager, trade and supply chain group at CGI, observes: "The GTB 'umbrella' has been truly developed among some of the top-tier global financial institutions. Currently, and this is true in the Canadian market, we observe that the integration is most advanced in terms of client-facing aspects of the business, such as sales and business development in cash management and trade finance. The overlap at the back-end in terms of technology platforms and integrated processing, is limited and still in development. This reality, and the costs associated with back-office integration, is one reason why the CGI 'software as a service', or SaaS model, has resonated with our clients. Cost, speed-to-market, and the ability to implement global platforms allowing banks to follow the setting sun: each factor has been important to our customers."

Tezzi concurs, noting: "Market consolidation will continue, and as the cost of deploying complex, integrated technology platforms increases, the second, and even more critically, third tier of providers in transaction banking, will be compelled to seek cost-effective solutions in this space. The Canadian market, even with such robust balance sheets and a relative abundance of financial resources, has recognised these new realities."

The changing commercial and trade landscape in which Canadian businesses – and their bankers – must now pursue opportunities will test the long-held view of Canada as a 'trading nation', given the forced diversification away from the US market, the evaporation of currency arbitrage which provided a significant and comfortable cushion of margin.

Businesses of all sizes are looking to extend activities beyond familiar markets, and the pull to Asia is, as in many parts of the world, nearly gravitational in force. Likewise, relatively greater focus on opportunities in the Middle East, and in emerging markets in Africa, as well as India, and South Asia, are complemented by a conscious policy in the Federal Government, of engaging more vigorously 'in our own neighbourhood' in the Americas.

Banks and other providers of trade finance, including EDC, will – and have begun to – need to respond to these changing dynamics. The crisis has engendered a significantly more positive dynamic between the various actors in the Canadian trade finance market, by nearly all reports – in particular, a much more partnership-oriented approach between the banks and the national export credit agency.

The evolution of Canadian trade, and the likelihood that greater international engagement will characterise the Canadian business landscape for some years to come, is perhaps one reason why HSBC is pursuing an



Akhil Lamba at TD Securities in Toronto

expanding remit in the Canadian trade market.

Ben Arber, head of trade and supply chain, HSBC Bank Canada, in Toronto, notes that senior leadership at the bank has mandated strong growth in trade banking and related services in Canada: "Canada exhibits an impressive size and array of trade activity, both by sector, and increasingly, by market. We will be assisting clients with the growth of their businesses in ways that HSBC, with our global footprint, is uniquely positioned to do. We consider Canada to be a market of high strategic importance. Our products and services are comprehensive and we will actively seek to respond to the needs of clients transacting on open account terms, in addition to remaining in the traditional trade finance space. We will provide solutions across markets and client segments – in developed and emerging markets, and in support of businesses of all sizes."

Opportunity in crisis, indeed, when a market such as Canada generates the kind of visioning and dialogue around trade and trade finance, which that has been observed particularly in the post-crisis environment.

While some jurisdictions debate whether banks should lead their clients in product/solution integration (the removal of organisational and product/process silos), the approach in Canada seems decidedly to be shaped by the needs and demands of customers – in particular, finance executives. Trade and transaction bankers will gladly engage in dialogue and even activities to educate customers where desired and necessary, but for several, it appears that the development of solutions will follow, not lead, commercial and corporate clients.

For Scotiabank, which styles itself as Canada's 'most international bank', the trade and cash convergence process is very much client-driven. Dyanne Carenza, vice president, trade business and product management at Scotiabank notes: "While there will always be a place for traditional solutions and products, we are

very open to and active in the exploration of emerging solutions and new products in trade and transaction banking. At the moment, we are reviewing options based on market developments, such as the evolution of global supply chains, increasingly common 'multi-sourcing' patterns and a clear desire among treasury and finance executives for greater transparency around supply chain finance. At Scotiabank, we are looking at global trade flows and trade corridors, and at ways to mirror financial flows with the physical flow of goods."

"Global transactional banks," observes Carena, "are focused on providing buyer-based supply chain financing for corporate and commercial clients. They focus on providing attractive funding to suppliers, as well as optimising buyers' working capital by increasing payment terms. Innovative thinking can be applied at each step in the financial supply chain to address evolving trade conditions. Some banks, such as Scotiabank, have been able to leverage their global footprint, specifically their retail banking operations in local markets, to successfully approach their suppliers."

### Mid-tier providers and boutique firms also thriving

The health and robustness of the Canadian trade finance market, and the vigorous engagement of various providers in this area of activity, can perhaps be further illustrated by the reality that mid-tier providers – and specialist boutique firms – are succeeding where global players in other markets have been forced to exit the business of financing international commerce.

National Bank of Canada, a financial institution with activities relatively concentrated in the Province of Quebec, with complementary activities in other parts of the country, has developed a vibrant, niche-based trade financing and factoring capability, and is said recently to have successfully challenged some of the larger institutions in certain segments.

Jean-Bernard Ruggieri, senior manager, head of



Jean-Bernard Ruggieri at National Bank in Montreal

trade finance, at National Bank in Montreal, observes: "There have been significant changes in the global trade finance market, and concurrently, in trade flows across the map. The former present opportunities for Canadian financial institutions to respond to needs no longer met by European and American banks in particular, and the latter, as our clients fully appreciate, provide opportunities for Canadian businesses, either

**"Trade finance is enjoying a renaissance period despite a strong Canadian dollar and volatility in commodity prices."**

to engage in new markets directly, or to act as trusted intermediaries, for example between India and China, to the benefit of all. Just as we work to facilitate complementary partnerships and alliances for our clients, National Bank is actively seeking new partnerships and alliances in the business of trade finance."

As with many markets across the globe, pre-crisis circumstances in Canada reflected an under-served SME segment, for the same reasons as was the case elsewhere: low margins and high demands in terms of the involvement of bank staff in 'hand-holding' small businesses through international transactions. Even EDC, a public sector entity with a policy-driven (though significantly commercially oriented) mandate, was seen to be more responsive to larger clients.

This persistent historical gap allowed for the development and growth of a SME-focused trade finance provider, Northstar Trade Finance, in a unique partnership model with bank and public sector shareholders, in 1994. Northstar has since replicated the success of its partnership model in various markets including the United States, the UK, Europe and Australia.

For Northstar CEO Scott Shepherd, the situation is changing: "Banks have focused attention on the mid-market and on SME-lending, including in the trade finance space, as a direct result of favourable margins. Our activities in Germany are instructive: German exporters, like their Canadian counterparts, are faced with the significant appreciation of the euro in relation to the US dollar, yet the role of the German SME and mid-market segment – the Mittelstand – in the impressive export-led recovery is undisputed. Trade finance has been critically important in mitigating the damage and driving recovery post-crisis, and our partnership model at Northstar has proven its mettle under tough conditions. Going forward, we will be actively extending our international footprint through carefully selected relationships and partnerships, both with providers and among client end-users of trade finance solutions."

Punching, successfully, above their weight class: Canadian trade financiers take a bow, as SWIFT holds the annual Sibos conference in Toronto. ■