A chorus of approval

SEAN EDWARDS reflects on the best of what trade finance offered at the IFA conference in Vienna

It is, to borrow from Dickens, the best of times and the worst of times. For evidence of the latter one need only open a newspaper, look at the television or, too often, just listen to the office voices. And battered trade finance has its own share of particular woes with the cost of capital for unjustly unloved trade products to the fore. Asserting the former is a more delicate, even audacious, task. And yet it was the light from some of the best of what trade finance has to offer that pierced the gloom at the International Forfaiting Association's (IFA) 38th Annual Conference in Vienna.

A tale of two markets

Let us start with the markets without which no business can find a home. Beginning and ending the conference was an examination of two very different markets, the one furthest from home arguably no longer emerging and the other, closer, still evolving and finding its way.

Central and Eastern Europe (CEE)

Dr Herbert Stepic, the CEO of Raiffeisen Bank International, is a distinguished banker, de facto statesman, and, as we saw at the end of his presentation, a humanitarian. Central and Eastern Europe is a heterogeneous mix of countries. Some, such as Poland and the Czech Republic have had, over the recent past, among the best performing economies of any country in the EU. Others lag seriously behind. Tantalisingly, however, the CEE sub-region hardest hit by the 2008 crisis, the CIS, has the best current and medium-term numbers. Driven by commodity prices and sufficient volume in those products to weather at least some downturn in price levels, the virtuous combination of wealth generators and a need for capital goods and infrastructure provide an ideal market for forfaiters.

In contrast, Southern and Eastern Europe has more serious structural problems and will need to play catch-up for many years to come. But yet again, while the credit analysis is harder and state or parastatal support more important, this should be a natural stomping ground for forfaiting. As Dr Stepic pointed out, however, even this region benefits from the favourable factors that bless the CEE as a whole, among them low tax rates, increasing productivity and good educational standards. For Dr Stepic it all begins and ends with people, and not without some help from him, as he encouraged us to support his charity for deprived young people in the CEE (www.stepiccharity.org).

The offshore Remnimbi market

Asia mirrors in many ways the CEE. Equally heterogeneous, growth and trade are, however, far more solidly anchored, with the region a voracious consumer of just those commodities produced in the CIS. Lixin Guo, head of forfaiting at Bank of China, presented an impressive overview not just of the different countries that make up the region, but opened the window onto the offshore Remnimbi market which is growing rapidly around the Asian offshore centres of Hong Kong and Singapore. Currently focused around a need to provide liquidity and settlement facilities for Chinese exporters and importers, this is an area innovating at the Chinese speed of light and is an irresistible market for the IFA's members. Forfaiting volumes are huge, indeed daunting, but just resist the glare for a moment and it is clear that there is nothing here the forfaiter and the techniques he has evolved cannot get to grips with. They just need deeper pockets (or bigger internal lines, credit departments please note).

Just what some of those techniques are was given air-time in the presentations of two speakers, one an old friend and the other newer to conference shores.

Synthetic letters of credit

Geoffrey Wynne of SNR Denton (*see also* page 32 of this issue) set out his thoughts on structured or synthetic letters of credit (LCs). Anathema to some in the LC world, these instruments are used principally as a means of raising finance rather than effecting payment. Is this wrong Geoff asked? The answer was empathically no, so long as you are aware of what you are doing. A recent case in New York formed the centre piece of his presentation. In *Fortis Bank v ADIB*, a Middle East issuing bank refused to pay Fortis on grounds of fraud for a letter of credit where payment for the underlying supply of goods had already been satisfied outside of the letter of credit. The New York court disagreed as it was clear the defendant had not been deceived and there was nothing intrinsically impermissible in using letters of credit in this way.

The discussion did not end there. Wider questions of whether this was trade or, to use the buzzword, 'true trade', began a lively discussion with the audience. Touching on recent experiences in Kazakhstan (where the IFA lobbied for its members) and older ones in Latin America, Mr Wynne gave the only answer that it is possible to give in these circumstances (and the one you would expect from a lawyer): it all depends on the facts. Or, to put it more precisely, the perception that true trade always gets paid will depend on the decision of, and funds available to, the recalcitrant debtor.

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Supply chain financing

Supply chain financing is not a product invented by the forfaiting market, but much of what characterises it is already part of its stable. Anurag Chaudhary of Citibank runs one of the most successful platforms in the market for this kind of business. The platform itself is, as Anurag admitted, a very expensive black box to establish. IT resources are considerable, but, once operational, the very large number of individual transactions amortises the cost. What interested the audience principally was how they could invest in the assets made available by the platform. The undoubtedly complicated trust structure devised by Citibank has to be seen in context. First, against the alternatives (don't ask) and, second, in the faith placed by participants in Citi that they have got it right. Validating this may require some extra care and attention but a number of large institutions have blessed the offering. Go forth and conquer!

Sub-participation agreements

What distinguishes forfaiting from many other trade finance markets is the presence of a highly developed distribution channel in the form of the secondary market. One very popular way of selling risk is through the use of sub-participation agreements. Daniel Schär of Zurcher Kantonalbank, and an IFA board member, and Nicole Keller of KfW IPEX-Bank gave the audience a valuable class in the meaning and use of the 'BAFT' or, in other words, the model sub-participation agreement produced by BAFT-IFSA. Involved at the very start of the drafting process, Schär outlined the history of the document in Europe (a New York law version has been produced for use in America where different issues of true sale arise).

Keller and Schär then proceeded to an explanation of the architecture and objectives of the agreement itself. Some slides on the options provided by the agreement and how to choose between them should have set pens to paper as this is where nearly all negotiation (in relation to the fraud option sometimes quite bitterly fought) takes place. Happily, consideration is already being given to reducing or simplifying these for a possible future version. But for the moment, thank you Professors Keller and Schär for your enlightenment!

Uniform Rules for Forfaiting (URF)

Dealing with some current preoccupations was the purpose of a talk and workshop on the Uniform Rules for Forfaiting (URF), a project with the International Chamber of Commerce now nearing completion, and a presentation on Basel III by members of the IFA's newest committee the ITEC (International Technical Experts Committee).

My own presentation ran through essential components of the URF whose vocation is to become a global set of terms for originating and selling in the primary and secondary market respectively – to become a UCP for forfaiting. The URF will feature in a later article in *TFR* and changes are still being made, so it is useful to dwell only on the most interesting or controversial points here. Foremost among these is the issue of recourse or true sale. While the concept of the without recourse sale is at the heart of forfaiting, it is clear this is not literally true and that some recourse is often expected and maybe even desirable. The grounds for recourse and where the boundaries lie have raised the most discussion and resistance. I raised some possible solutions but no final decision has yet been taken.

As theory is often incomprehensible without a practical demonstration, my presentation was followed up by a workshop with case studies by Waltraud Raderschall of Commerzbank, Lucio Matassoni of OCBC and Bert Verkerk of Rabobank. By linking issues thrown up by the case studies with the solutions offered by the URF, this session helped to show the value of the new rules in a meaningful way.

Spectre of Basel

Basel III is the biggest sword hanging over not just the forfaiting market but trade finance in general. It is often hard for practitioners to follow the detail and the changes in the debate, so the presentation by Silja Calac of Unicredit and Paul Coles of Bank of America was very welcome and the comprehensive summary of the new rules was clear and invaluable. What is not yet clear is whether the Bank for International Settlements (BIS) will treat trade more favourably, as many have urged, given its central importance to the world economy and good track record.

A vibrant business

So closes Vienna 2011. The shared experience of this conference as with the others organised by the sure hand of Paolo Provera, the IFA chairman, undoubtedly strengthens the bonds between the existing members of this vibrant business. But, with increasing participation from Asia and Central and Eastern Europe, it is also proof of the growing size of what has sometimes been called a niche market. May the good times roll.

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CLARISSA DANN talks to some of the delegates at the recent IFA annual conference and finds out more about the glue that holds forfaiters together

Goodnight Vienna

When around 180 International Forfaiting Association (IFA) annual conference delegates descended into the bowels of Vienna's Piaristenkeller on 7 September, they were transported back in time to the days of Hapsburg rule and immediately got into the spirit of things.

Decked out with hats of the period, the worries about the implications of Basel III were put to one side as people got to know each other in the more relaxed surroundings of what was a former monastery and even managed to do a bit of business. Having only been at the *TFR* helm for one month, this opportunity to immerse myself in 'the art of forfaiting' for what ended up being four days (I am a 'graduate' of the educational seminar) was a huge privilege.

I was struck by how helpful everyone was – and how passionate they were about what they did. Work and leisure all melded together as people exchanged deal ideas and contact information at the same time as showing each other pictures of their families on their smartphones.

Vladimir Metelski of Belarusbank told *TFR*: "Although we are not a major player in the forfaiting business, it was really useful to meet people I already have dealings with and we did negotiate some new instruments."

New to forfaiting, Vernon Darko of Texan machinery exporter EquipXP had signed up to the event in a quest to learn more about how he could use forfaiting as a financing tool. "I enjoyed the conference a great deal and I got more than I'd actually expected – in terms of leads as far as the banks and understanding how the forfaiting process works", he said.

Earlier that first evening, the group had been treated to the angelic tones of the Vienna Boys Choir, whose performance for our benefit at St Peter's – the vast baroque church that once hosted Mozart, Haydn, Brahms and Brucker – provided an appropriate cultural diversion from the conference proceedings.

Growth from Asia

The 38th International Forfaiting Conference held in Vienna was an interesting barometer of how the IFA is becoming a much more global association – having started out in 1999 as something very European. In his opening remarks IFA's chair, Paolo Provera (ABC International Bank), did admit that that consolidation among banks and forfaiting houses had briefly set numbers back a little, but was pleased to report that membership is now at 122, spanning 26 countries. Charles Brough (UniCredit), the IFA's membership secretary based in Singapore, confirmed that the take-up from Asia had been increasing. The interest was there for all to see – 18 delegates from that region, along with Bank of China's Lixin Guo's welcome as a non-executive board member to chair the North Eastern Asia Regional Committee was an indicator of where much of the new forfaiting activity is coming from.

Although the event was conducted in English, when I heard bits of conversations in various pockets of the exhibition hall and at dinner at the end of the day, there was more German spoken than any other language. While I would have expected third in the pecking order to be French, it was in fact Mandarin – to the extent that I jokingly suggested to Guo over a glass of wine that perhaps I should start taking lessons. He kindly took this at face value and offered to put me in touch with his colleagues at the Bank of China in London (I'm still thinking about whether I have the aptitude). Guo's talk on the offshore Remnimbi (RMB) was something of an eye-opener to many, not least because of the significant market to forfaiters provided by the Chinese currency (*see* page 14) .

Networking

The opportunity to set up and conduct meetings with delegates that would otherwise require a very long plane journey was something Simon Lay (London Forfaiting) found "very useful". He told TFR: "I did have a lot of meetings with people it would normally cost a lot of money to reach. The conference works very well, it is fairly short – not a long drawn-out affair, it is very much people from our industry so the networking is very focused and relevant and the presentations they do are concentrated on the issues in our industry."

Veron Darko agreed that the networking was invaluable and that he had set up "a number of transactions". Newcomers and regulars alike were helped by the mix of organised yet relaxed entertainment in the evenings. This did much to break down any reservations people might have had about striking up fruitful conversations with delegates they had never met before in what was often a second language for both parties.

Education

The general heightened interest in supply chain financing throughout the trade finance market was evident not only at the IFA event but even more so at Sibos (19 to 24 September) in Toronto, and because of this, forfaiting is enjoying something of a new growth spurt. More newcomers are now joining the sector and they, like me, find it helpful to go back to basics and understand how the transactions actually work.

So it was hardly surprising that the excellent educational seminar, run by Richard Willsher (a *TFR* contributor) over two days was full up at 23 delegates – representing 16 different financial institutions.

The course was structured around three main modules: risk assessment, discount calculations and documentation. He reminded delegates that in forfaiting, "there are very few extremely poor risks and most are in the middle ground, so it is difficult for us to make money. Consequently we have to be careful about how we structure transactions." He went on to explain that emerging market deals can often be attractive, but timing and "getting the maths right" were vital.

1. *TFR*'s new editor, Clarissa Dann gets involved. **2.** Winetasting at the traditional Piaristenkeller. **3.**The Vienna boys choir performing for IFA delegates at St Peter's. **4.**The IFA board and the conference sponsors, from left to right: Daniel Schär, Sean Edwards, Demetris Zouzoukis, Shanan Zamir (sponsor), Paul Langford, Charles Brough, Paolo Provera, and Sema Zeyneloglu

He then proceeded to walk delegates through the construction of a deal for an exporter looking for US$5m for his goods over a five-year credit term. By the time all the numbers had been plugged into the software (Willsher advised delegates to equip themselves with this rather than battle in MS Excel[1]), he was able to demonstrate that the discounting mechanism meant that the original contact value had to be uplifted so that the exporter received the US$5m he was looking for after it had been discounted back.

Other parts of the course included a risk assessment case study and some forfaiting case studies where 'students' assessed whether the deal presented was attractive or not, using the learning points from earlier in the course. One of these was a theoretical deal that financed a Paris-based coffee trader, looking to purchase international grade coffee from an African producer.

Going forward

Sema Zeyneloglu of Rabobank, who heads up the Education Committee at IFA, makes the point that with all the work being done on the up and coming Uniform Rules for Forfaiting (URF) and BAFT Master Risk Participation Agreement (*see* page 14), education is something the board will be ramping up. Ideas for seminars (likely to be held in Western Europe for the time being, but events in Asia and the Balkans are being planned) should be emailed to her at info@forfaiters.org.

The last day came all too soon, and although I managed to hop on the Metro and visit some of the sights in the old city, it was with some sadness that I boarded the bus to the airport after what had been an enjoyable and instructive four days. I must have had forfaiting vibes coming off me because the chap in plus fours behind me in the check-in queue told me that although he had long since retired from his trade finance job at HSBC in Hong Kong, he'd had, (to borrow Dickens again) the best of times.

Reference

1. He gave examples of CMG Rohirst, GML Trade Finance Analytics and Forfaiting Manager by ZP Software