

Developments in Structured Trade & Commodity Finance 2019 Update

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Simmons & Simmons

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Asia Warehouse Fraud

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Inventory Finance



Financing:

- Cargos on Ship
- Stocks in Warehouses
- Oil Storage Tanks

Two main structures:

- **Loans with Security**
- **Commodity Repos**

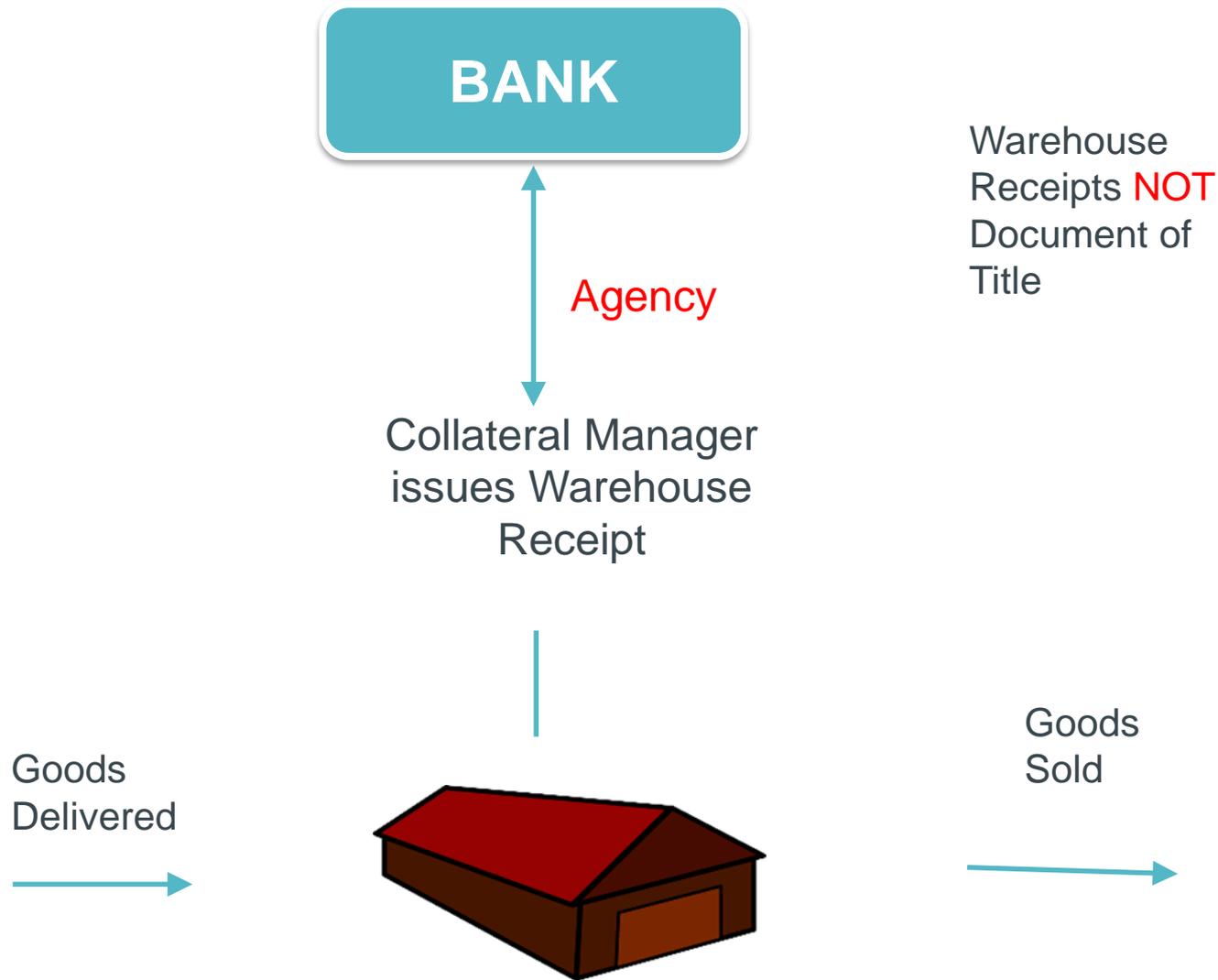
2014 – Qingdao Port Fraud in China



Late 2017 - Access World Press Release

- Warehouse Operator announced it had become aware of "forged warehouse receipts" and urged holders of its warehouse receipts to authenticate them
- Warehouse Operator said it would provide authentication for clients' warehouse receipts, after which it would honour "***duly authenticated original warehouse receipts***".
- Qingdao 2.0?

Collateral Manager/ Warehouse Operator Simmons & Simmons



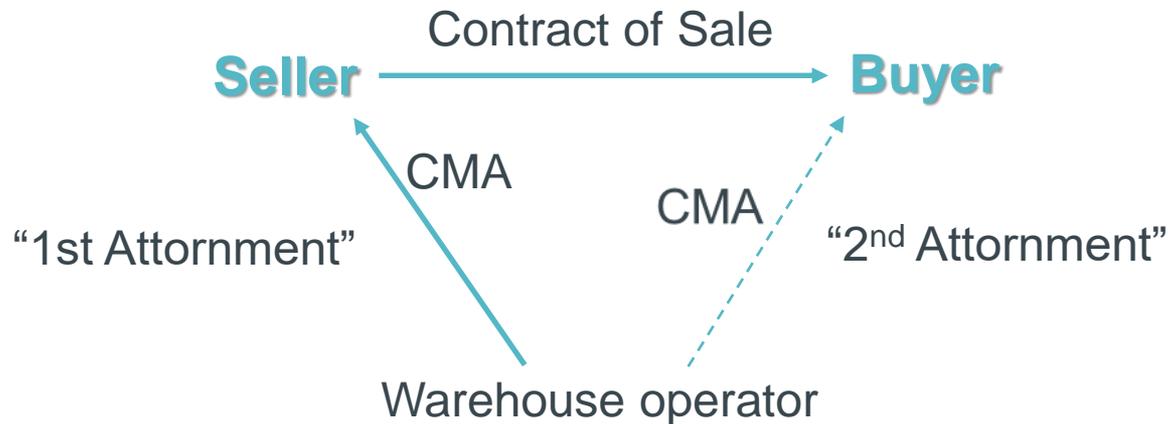
FAKE WAREHOUSE RECEIPTS



Who wins – Bank A or Bank B?

WAREHOUSE RECEIPTS & ATTORNMENT

Warehouse Receipts are **not** documents of title (some exceptions)



Attornment = warehouse operator undertaking to hold goods for buyer. Often they only do this they receive original warehouse receipt from Buyer

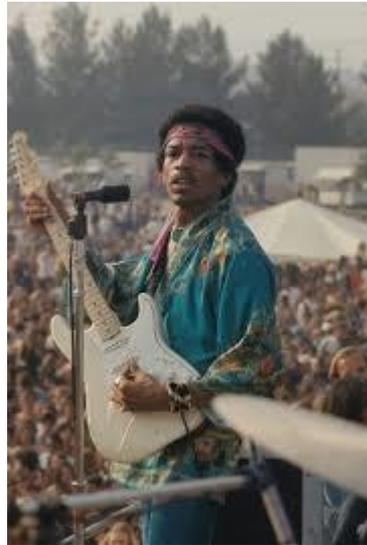
Watch out for “Provisional Attornment” based on copy WRs!

Warehouse operators will only treat holder of original WR as their customer

IBORs and Commodities

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LIBOR

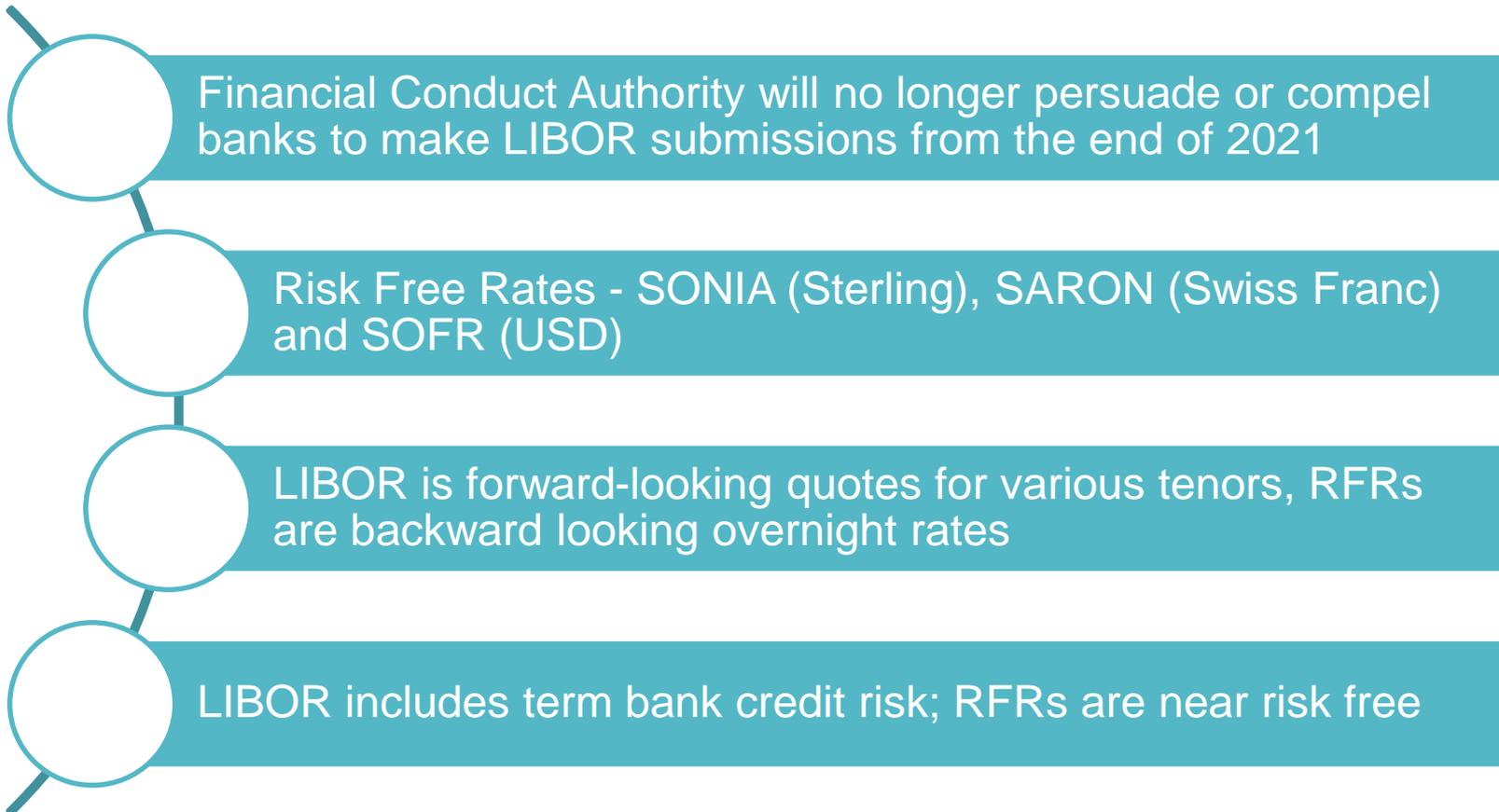
“I was, more or less, if you excuse the lack of modesty, the one who started the whole thing”

“We started something which was practical and convenient. We never had in mind that this rate would spread to mortgages and things like that”



- **Minos Zombanakis**

Finding alternatives to LIBOR



IBOR rates and Commodity Traders

- **Traders are Borrowers:** lots of credit lines ! (Trafigura – circa 130 bank relationships)
- **Traders are Lenders:** Bundle trading with financing services (eg Advance Payment structures)
- **Sophisticated hedging positions** (commodity prices, FX and interest rates)

Transition to “Risk Free Rates”

2022 : Central Banks & Regulators to stop supporting IBORs

OLD “IBOR Rates”

GBP LIBOR
JPY LIBOR/ TIBOR/ Euroyen
EUR LIBOR/EURIBOR/ EONIA
USD LIBOR
CHF LIBOR

NEW “Risk Free Rates”

Unsecured overnight rate
SONIA GBP
TONAR JPY
ESTER EUR

Secured overnight rate
SOFR USD
SARON CHF

Existing LMA fallbacks



- Interpolated Screen Rate



- Reference Bank Rate



- Cost of funds

Transition to Risk Free Rates – Not Simple!

- By 2022 every document must be amended to either:

- (i) Provide fallback if IBOR ceases OR

- (ii) Change IBOR to RFR

- Fallbacks do not ensure orderly transition to RFR as IBORs may continue!

- Switching IBOR to RFR is not just CTL+ALT+REPLACE

- Each organisation's documents & trade require separate legal amendment

- You cant control the timetable

Prudential Regulation Authority Paper – Good News for Banks?

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UK PRA Policy Statement

- **February 2018** – PRA issues consultation paper suggesting “guarantee” must pay out “within days” to be eligible as unfunded credit risk mitigation for CRR
- Impacts all firms bound by the Capital Requirements Regulation (575/2013) (CRR)
- **Early 2019** - PRA published a policy statement on the eligibility of guarantees as unfunded credit protection. Rows back on previous proposal
- Expectation on firms to consider the risks arising out of eligible guarantees. The PRA draws firms’ attention to Article 194(8) of the CRR (which requires firms to have adequate risk management processes to control risks arising out of credit risk mitigation) and Article 213(3) of the CRR (which requires firms to fulfil any contractual and statutory requirements in respect of, and take all necessary steps to ensure, the enforceability of its unfunded credit protection)

Watch this Space!

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