

The end-to-end approach to large ticket transactions



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Consolidating trade finance requirements might be more complex than aggregating other transaction banking needs, but, as Ravi Saxena, Managing Director, EMEA Trade Services Head, Citigroup, points out, it is far from impossible.

In today's market, where supplier consolidation is a key business priority, more and more organisations want the convenience of dealing with a single relationship bank for all their transaction banking needs. The process of compressing trade finance requirements into a few dominant relationships has often proved prohibitively complex for the corporate and its banking partners, but banks are responding, and even the largest and most complex deals can now be handled by a single partner.

The demand for large financing transactions is booming. Rising oil prices, for example, are causing the requirement for trade facilities to spike, with liquidity-flushed companies in oil-generating countries seeking to finance facility upgrades and expensive acquisitions. The syndicated loan market, where banks pool their resources to cover a large loan, has seen a spectacular increase in volumes and transaction sizes in recent years. However, when it comes to large trade finance transactions involving non-funded borrowing, i.e. letters of credit (LCs), matters become more complex.

Banks are required to 'front' large ticket transactions because beneficiaries favour a single instrument. In contrast with the traditional, syndicated loan arrangement, where one bank can take on the role of agent while the syndicate shares the risk of the loan, using the 'fronting' method, the bank taking on the role of issuer of LCs is still left with much of the risk. Essentially, the bank becomes guarantor for both its share and that of its partner banks – exposing itself to a potential risk that is effectively the value of the credit being issued despite the participation of the banks. For example, a bank providing \$10 million of a \$100 million letter of credit as part of a syndicate of ten banks and issuing the letter of credit on behalf of its customer, would, in effect, be taking on an additional \$90 million of bank risk. This capital inefficient method places a severe limit on the size and number of 'fronting' deals that can be taken on by any one bank, making it more difficult for businesses to obtain the service they require.

A package deal

Despite this capital inefficiency, fronting structures for standby LCs have grown rapidly in recent years (owing to the aggregation benefits of syndicated deals). However, these structures are impractical for commercial documentary LCs because of the underlying transactional complexities, i.e. complex payment and delivery schedules that often involve multiple instalments over period of up to three years as well as the country and credit risk inherent in long-term projects.

Fortunately, help is at hand. With today's credit market flooded with liquidity and investors' appetite for credit instruments at an all-time high, there is significant opportunity for global trade finance banks to provide bilateral agreements with sell-downs; i.e. the relationship bank takes on the full risk of a trade finance deal and subsequently packages the risk and sells it on the secondary market. This enables corporates to deal with their preferred banking partner on even the largest trade finance transactions and facilities, whilst other parties shoulder some of the risk. This method also benefits the purchasing financial institutions by allowing them to diversify their trade risk portfolio to include countries where they do not have a physical presence.

Structured trade transactions

There is an emerging requirement of large corporates to find a 'one-stop' bank to meet their growing trade finance needs and handhold structured trade transactions on an end-to-end basis. As a global bank, Citigroup is well positioned to lead the challenge in the market place to meet our customers' requirements.

As an example, Citigroup's partnership with a corporate client, whose subsidiary was purchasing capital equipment and wanted to avoid the lengthy process of arranging a syndicated facility or handling multiple bilateral documentation decided to find a single issuing bank that would underwrite the entire transaction and issue LCs immediately.

Citigroup developed a tailored solution to help its corporate client meet contract terms requiring the issue of import LCs totalling \$120 million favouring suppliers who were also Citigroup's clients. By acting on behalf of both its importer and exporter clients, Citigroup was also able to ensure that the solution was end-to-end, enabling the importer to raise the facilities through a single bank, and have the entire process coordinated and facilitated by its preferred partner. Citigroup agreed with the importer that it would take the whole amount onto its books and distribute it on the market to 'tier one' investors. Citigroup also took responsibility for maximizing the deal's investor appeal by establishing a structure which meant that the LCs were issued directly by Citibank International Plc (CIP) London rather than Citigroup's emerging market branch thus mitigating cross-border risk for the exporter.

Heightened demand for large, unfunded single ticket deals means that there is a clear market need for banks that can structure end-to-end bilateral agreements that deliver benefits to issuers, beneficiaries and financial institutions. Such solutions require global infrastructure, a deep understanding of trade finance requirements and a wide-reaching distribution network. As a bank with a proven investment track record in trade finance, we believe that Citigroup has the answers. ■