Metal Bulletin

INTERVIEW: Kimura Capital seeks to fill commodity trade finance gap

A liquidity gap is developing in commodity trade finance which is especially impacting small to medium-size companies and could severely constrict global growth going forward, according to a senior executive at Kimura Capital LLP.

Kristofer Tremaine, founder and chief investment officer at the London-based asset management firm, said that the situation could worsen further if commodity prices begin to pick up.

"We are already at capacity in terms of a lot of banking lines, or lines that banks are willing to provide, so in an upwardly mobile commodity price environment, we could see a liquidity crisis," he told Metal Bulletin in an interview.

"This would especially affect the smaller players - before it impacts the bigger ones," he said. Citing data from the International Chamber of Commerce, Tremaine said that by number, small to medium-size enterprises (SMEs) constitute over 95% of all firms and account for approximately 60% of employment globally.

"Financing these smaller companies is absolutely critical to maintaining global growth," he added.

A recent report issued by the Asia Development Bank showed that the global trade finance gap for 2015 is estimated to have been $1.6 trillion, with the deficit especially felt in Asia and mostly among SMEs.

Tremaine noted that the withdrawal of many banks from commodities generally has particularly added to this gap. He cited capital adequacy requirements that have made it more expensive for banks to service borrowers, while anti-money laundering and know your customer (KYC) regulations have acted as an impediment to the expansion of trade finance as the cost of compliance and stringency of credit criteria has increased.

"The knock-on effect of these factors is the internal upscaling criteria within an investment bank, which in turn makes it very difficult for a small client to be interesting - or in fact onboarded in the first place - just for its trade finance needs alone," Tremaine said.

Kimura Master Fund
It’s a gap that Kimura, whose main fund is in its initial offer period before moving to transacting from October, is confident it can fill.

The Kimura Master Fund is focused on strategic commodities - energy, metals and agriculture - with a global mandate; its remit is not to finance traders looking to make a speculative return, or one-off transactions, but to work with companies that fulfil a role in the commodities supply chain. Kimura is also looking to provide funding that will ultimately be job creative and socially responsible, Tremaine noted.

In metals this could mean financing the movement, storage or refinancing needs of a company processing copper concentrates, for instance; the company has been actively reviewing base metals and related transactions in Chile, Peru and South Africa, Tremaine said.

"We are keen on metal concentrates, which historically is a less attractive platform for a bank to finance, as they prefer metal in LME-grade finished form. We're comfortable with the risks of funding concentrates, and see it as quite a liquid part of the portfolio," he said.

"We're trying to build something that is a gold standard and has scalability. We have a global, pan-commodity mandate that we have not seen in any of the other alternation funding solutions yet," he added.

The company is happy lending into deals originating from emerging economies where there is an associated jurisdiction of legal recourse (borrower being domiciled in a developed economy), but won't deal with nations that are sanctioned or have sanctions pending.

Tremaine founded Kimura after two decades of working across various banking and physical commodity industry businesses, including at BNP Paribas, ABN AMRO, UBS, Société Générale, Hetco, and PPG.

The company's chairman is Neil West, an energy market veteran with over 40 years' experience beginning at BP within physical oil risk management and trading and continuing at Goldman Sachs, where he headed up and developed the bank's energy division in London. Having also held senior roles with Phibro and Tosco, Neil latterly was head of crude oil trading at Hetco until 2012.

Kimura also lists as partners Alan Gordon, Morgan Metters and Warren Kirrane, who have worked in various roles across commodity trade finance and structuring, sales, physical trading and derivatives at various banks and merchants. The portfolio is managed by Michael Fitzgerald, who has over 10 years of experience working within trade finance at Noble, Armajaro and Trafigura.

Banks out

In some places, the big commodity trading houses have stepped in to fulfil the gap within commodity trade finance, but Tremaine said it can be non-optimal for a borrower to have its financing needs provided by what is essentially a competitor to its trade flows.

"The big commodity houses are borrowing from a consortium of banks that syndicate to issue their revolving credit facilities, and then they finance these smaller companies at market rates, but with the addition in many cases of requiring to be the off-taker of the financed commodity. This is a very attractive situation for the big commodity companies, but not so much for the SMEs they are financing," he said.

"In other words, banks are assuming the same risks on their balance sheets by proxy that they were meant to be avoiding," he added.

Kimura does collaboratively work with merchant banks, however; the fund is designed to step in and finance collateral issues that arise and allow banks to continue working with SMEs that they have cultivated relationships with.

"We certainly see ourselves as collaborative with the banks, we're not here to be disruptive," Tremaine said.

"Kimura will not typically go after investment grade business because the individual transaction sizes cause concentration issues in the portfolio. Given where our position is within the market, the rates are not attractive to our investors - when you're operating as a fund, you are constantly balancing the need to provide competitive rates to the client with returning rates that are attractive enough for new investors to invest," he added.

Tremaine said that some banks may eventually return to commodity trade finance as they work on building their internal capital, but that this situation is probably several years away.

"Commodity trade finance represents one of the lowest default rates of any form of debt – it's typically all short-term asset-backed paper, and in our opinion it's a very safe haven to be in, if managed properly with the right skills and resources," Tremaine told Metal Bulletin.

"There will come a point when the combination of the legislator and central banks realise it is a safe haven and a long-term solid business line, and we may see them return. But the trend for now over the next three to five years is certainly more of banks stepping away," he said.

Kimura intends to build the business out like a merchant finance company, and will add different products over time that allow it to participate in different structures within the trade finance ecosystem, such as pre export and supply chain finance, he noted.

"Any investor that wants an uncorrelated product which targets higher yield returns and low volatility, then this is something they should seriously consider," he added.