Stock Finance / Collateralised resp. Secured Lending

Most (metal) trading companies obtain stock finance at terms between 80 – 100% depending upon such factors as those enumerated below, in addition to balance sheet considerations, the quality of the MIS, risk control measures, stock levels vs speed and means of repayment etc. Location plays a role, OECD countries might go at 100%, well rated countries at 90% and developing ones at ca. 80%. I do not know of a formulaic basis for deciding the lending rate, the method is more of a matrix application (in theory if not in practice) where the undernoted elements are weighted to give an overall credit risk analysis. Some countries are avoided for political reasons e.g. Iran, Libya, Algeria, some ex-east bloc countries, some Latin American e.g. Bolivia, Peru or perhaps American restrictions.

- the lender must (be allowed to) treat such credit as secured lending in order to limit the risks of recourse on the counterpart / intermediary. Alternatively one can seek funds on a "repo" basis (sale and repurchase agreement) which moves property in the goods in line with the flow of funds (e.g. Standard Bank does this for larger deals.)

- ***the lending ratio is (should be) subject to an objective test considering:***

i. the type of goods involved (commodity or specific / manufactured goods)
ii. market liquidity for the goods taken as collateral (speed of disposal)
iii. mitigating measures to minimise market / price risks (hedging)
iv. the tenor of the transaction, rationale for unduly long financing period
v. how much has been paid for the goods e.g. 80-100% of the purchase invoice value (it is unlikely that full value would be given if only 80% had been paid as it creates an unsecured payment risk)

- ***location of the goods, quality of the warehouse, warehousekeeper's track record / independence***

i. location is important for obvious reasons such as political risk
ii. is the warehouse truly independent or is it part of a group controlled by the seller (often the case with large suppliers especially Chile)
iii. does the seller have any residual rights in the goods to complicate moving / liquidating same
iv. is the warehouse well situated (within or close to a port) or inland/inaccessible
v. are the goods stored inside or outside (deterioration and security risks)
vi. who has access to the goods and can this be restricted
vii. can goods be exported easily re. vessel availability / rail connections / customs procedures / is the port inaccessible at certain times (strikes / freezing / low water levels e.g. Danube transport etc.)
viii. is the warehouse LME / Comex registered or belong to a recognised group
ix. do the goods need to be registered locally to perfect the pledge

- ***security given / residual rights / nature of the pledge instrument / applicable law and legal forum***

i. are there legal differences locally between warehouse receipts and holding certificates
ii. do the goods have to be registered locally to perfect the pledge, do restrictions apply to goods allowed
iii. how is the HC worded, does it cover the min. risks and elements required by the lender
iv. has it been countersigned by an independent inspection co. / is a separate certificate issued
v. is free access given to the goods / can this in practice be guaranteed
vi. how often are the goods checked for quality / quantity / segregation
vii. is the issuer legally authorised to issue and sign the document provided
viii. are the signatures thereon legally binding upon the issuing company / verification procedures
ix. the original document must be sent direct to the lending entity (photocopies not acceptable)
x. has unauthorised release happened before thus destroying the pledgee's collateral security (it does happen and can prompt a bank to withdraw facilities!)
xi. are all conditions met as imposed by insurance co. to ensure cover is given and maintained
xii. is the HC subject to an acceptable law and neutral forum e.g. English law and London courts

- ***payback period / quality of off-taker / sales method / EXW, FOB or CIF sale / mitigants***

i. how long is the total finance period, the impact of interest accruals, can any unforeseen delays be accommodated to avoid unwinding the deal
ii. to whom are the goods being sold, do they have an acceptable credit rating, can del credere cover be obtained and if so for what amount, are there restrictions on origin (especially relevant for USA)
iii. how are the goods sold, by (un)confirmed LC / CAD (via bank or not) / draft acceptance / PN / unsecured sale (see above), is there a binding contract in place, what are the terms and conditions
iv. are freight / insurance costs incurred in the sale and who bears these
v. have the goods been hedged, who bears the VM settlement risk, how are margin payments secured
vi. what other market or price fluctuation risk mitigants are available, are these practical and acceptable to the financier.