

The trading house as lender: a model in question

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The transformation of trading houses into lenders to states, which this chapter has described, raises a question of business model. A trading house is not a bank: it is subject neither to prudential supervision, nor to capital requirements, nor to the banking rules on sovereign credit. It funds its loans through its own bank lines and through the markets, thereby transferring to the banks, Geneva banks among them, a sovereign risk that they would not have taken on directly.¹ In return, it obtains long-term purchase contracts that secure its volumes and its position in the market, a commercial advantage that explains its willingness to lend.

This model has produced mixed results: liquidity for states in difficulty, volumes for the trading houses, debt crises for some countries and legal proceedings for some traders. Its regulation is indirect, through the banks that finance the trading houses, through the international institutions that demand transparency and through the criminal authorities that prosecute corruption. No authority supervises resource-backed loans as such. Chapter VI proposes good practices. One question remains open, namely whether the Geneva financial centre, which is home to the principal lending trading houses, should promote standards of transparency and sustainability for these loans, as it has done in other fields, or leave that task to the international institutions.

Worked example. A Geneva trading house grants a national oil company in Central Africa a prepayment of USD 500 million, repayable through deliveries of crude over three years, with a discount of USD 3 per barrel on the market price and an escrow account in London. At USD 70 a barrel, repayment requires around 7.5 million barrels, or 20 per cent of the company's annual production. At USD 40, it requires 13.5 million barrels, or 36 per cent. The trading house funds the transaction through a syndicated line from Geneva and European banks, which require covenants on country exposure. At the trader's insistence, the contract is published in

the country's report under the Extractive Industries Transparency Initiative, and the use of the funds, allocated to identified infrastructure, is verified by an auditor. The transaction illustrates both the usefulness of prepayment for a state without market access and its sensitivity to price, which transparency does not remove.

1 Notes

1. TXF, "The Rosneft prepayment: Deal of the Year 2013": a prepayment of USD 8.32 billion signed in March 2013 by twelve lead banks (including BNP Paribas, Credit Suisse, ING, Société Générale) in favour of Glencore and Vitol, secured by crude offtake contracts; Trafigura, press release of 8 December 2022 (credit lines of USD 73 billion from around 140 banks); International Crisis Group, 6 October 2021: "a handful of trading firms purchased most of South Sudan's oil from 2013 onward and then started lending the government money through 'prepayment arrangements'", for a total approaching or exceeding one billion dollars. ↩

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