

BANKING ON BEEF

The complex world of beef finance is not one many readers would be familiar with. **David Murray**, of Blackrock

There has been much media speculation about the "recklessness" of many continental Banks who provided £460 million pounds of "unsecured loans" to the Goodman International Group. This has focused attention on a much unloved source of finance by Irish banks namely trade finance. While Irish banks are familiar with the instruments of trade finance such as Letters of Credit, Bills of Exchange etc. there is a clear reluctance to provide actual trade finance facilities to Irish importers and exporters. However, banks based in long established trading nations such as U.K., Continental Europe and Arab Countries have no such reluctance.

The export of beef to the Middle East is a particularly complex area of financing. A typical contract would be for the supply of 5000 tonnes of boneless beef to the appropriate trading company in the Middle East. The new season of negotiations have not yet been completed where the terms of such contracts are finalised. However, let us assume a contract price of

US\$1,800 per tonne has been agreed. The terms of payment are normally by way of Letter of Credit drawn at sight (immediately), 90 days, 180 days, or 360 days. The last number of contracts for the supply of beef to Iraq were paid by sight Letter of Credit whereas formerly they were paid by way of 360 day Letter of Credit. The contracts for the supply of beef to the Islamic Republic of Iran are currently paid by way of sight Letter of Credit.

A Performance Bond of 10% of the contract value is normally required by the purchasing authority from the Beef Exporters Bank before they will open the Letter of Credit. The Performance Bond is effectively a guarantee from a bank that the beef exporter will honour delivery of the contract. The bank is consequently exposed for this amount and will have to make a credit decision on the exporter and also charge a fee for such a Performance Bond (typical 0.5% of its value). The value of the Performance Bond would amount to US\$900,000 being 5000 tonnes @ US\$1,800 x 10%.

The Performance Bond is normally released by the purchasing authority three months after delivery of goods under the contract.

The Exporter must then finance the contract value of the beef. A

bank would tend not to lend more than 90% of this contracted value - making allowance for the exporter's contribution. The amount advanced by the bank will be drawdown by the exporter in instalments against Warehouse Warrants issued by the coldstores storing the beef before shipment. The amount of finance provided by the bank would therefore be 5,000 tonnes @ 1,800 x 90% = US\$8,100,000. The bank would normally have security of such stocks. This is a very competitive finance market and the banks would normally receive a margin of less than 1% on such transactions.

There are E.E.C. grants to companies exporting beef to certain markets outside the E.E.C. The level of these supports is broadly determined by the difference between world prices and the intervention floor price and is administered on behalf of the E.E.C. by the Department of Agriculture. The value of such export refunds would amount to approximately IR£1,500 per tonne. Usually there exists a time difference of up to 2 months between the period beef is produced and paid for and receipt of the export refund. Consequently, bridging finance is required from a bank for such export refunds. Arrangements can be made to make payments direct to the bank from the Department of Agriculture. However, while this bridging facility is repaid within a matter of weeks - prior to the payment of these export refunds a financial guarantee equal to 120% of the refund amount must

be lodged with the Department of Agriculture and Food from a top 500 bank. The guarantees are released upon proof of export. However, this can take up to 3 months after shipment.

The bank guarantee required would amount as follows:

5,000 tonnes x IR£1,500 x 120% = IR£9,000,000

US\$/IR£ exchange rate 1.7 US\$ value of guarantee = US\$15,300,000.

This guarantee is assessed and charged by the bank in a similar manner to the Performance Bond already detailed.

The maximum financing requirements of this beef export contract may be summarised as follows:

Finance US\$	Guarantees US\$
	Performance Bond
	900,000
Contract Finance	
8,100,000	
E.E.C. Export Refunds	
	15,300,000
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8,100,000	16,200,000
Total Facilities	US£24,300,000
Contract Value	US£9,000,000

As one can see the financing requirements of such exports greatly exceed the value of such contracts and partly explain the reason for such large borrowings by beef exporters such as Goodman International.

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