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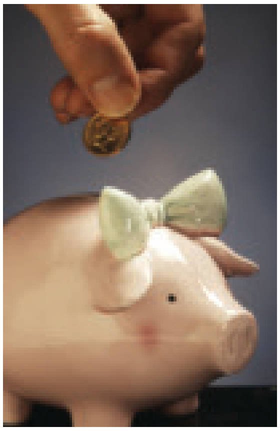
Filling the Funding Gap

Commodity financing offers an excellent alternative funding source for food companies

Whether you're looking at a brewer in Vancouver, a grain handler in the Prairies, or a coffee roaster in Ontario, Canadian food companies often have one thing in common. That is, they have unnecessarily tied-up their expensive capital – in using bank credit lines – to fund the purchase of much needed "soft" commodity inventory, such as barley, canola or coffee, that is eventually used in food production and processing. However, recent developments in financial markets have allowed some international banks to offer tailor-made commodity finance products that let food companies monetize their exchange tradable soft commodity inventories while remaining in possession of the inventory so that business is not disrupted.



The demand for such financing techniques is evident as they offer a clear and unique way for food companies to generate cash and save on financing costs.

International banks, with their financial structuring skills and insight into commodity markets, have already offered these types of commodity finance products in many international jurisdictions. In the U.S. and Europe, these commodity finance products, also known as Repurchase (Repo) or commodity sale and forward purchase products, have received regulatory approval. These products are increasingly assisting businesses – originally metals and mining and energy, but now also food companies – to generate short-term cash and reduce the cost of funding inventories by selling their commodities to banks while retaining the right to buy back the inventory at a later date, when needed, on maturity.

Food companies with seasonal build-up of inventory commodities, such as grain handlers or chocolate companies, have benefited greatly from the ability to utilize an alternative funding source to finance their commodity inventories before peak sales seasons. In the U.S., large agricultural companies with material amounts of agricultural commodity inventory have been able to generate significant cash from idle inventory located in warehouses simply by transferring warehouse receipts to banks in exchange for funds, and making repayment to the bank at a future date when the commodity is needed for sale or processing. Not only are such commodity finance products alleviating liquidity challenges for food and agricultural companies, but they have also helped manage commodity price volatility, something that has become a growing concern given rising soft commodity prices.

In Canada, government regulators and legal specialists on financial products are increasingly coming to the realization that banks should be allowed to help businesses finance inventory in non-traditional ways along with their existing practice of helping manage commodity price risk. A few international banks have been working on establishing a structure to offer commodity finance products in Canada, as it is available in other markets, and have received positive feedback from the marketplace. The demand for such financing techniques is evident as they offer a clear and unique way for food companies to generate cash and save on financing costs.

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