Along a turbulent path

SIZING THE SWISS HUB
A diverse trading community

PRIORITY TO FOOD SECURITY
Trade’s role in the quest for safe supply

THE ROLE OF SOEs IN TRADING
The State in the current landscape

DRIVING THE NEXT SUPERCYCLE
Is the current upbeat trend a glitch?

GUIDANCE & REGULATIONS
Conducting an ethical business

TECHNOLOGY & RESEARCH
Disrupting commodity trading
Financing solutions for commodity traders and producers

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The political context delivers greater uncertainty than usual, and we are witnessing structural changes that will greatly influence the commodities markets. Though the shift from globalisation to global protectionism may be grounds for concern, commodity prices are picking up and the evidence suggests that we may be in the early stages of a new bull market. Rising supply risks can be expected to underpin higher prices with the prospect of accelerated infrastructure building in the US and surprise demand growth in China.

Changing weather and demographics, combined with geopolitical uncertainty, may have a negative impact on food security threatening the livelihood of millions. The world’s population is expected to reach nine billion by 2050, and the food supply chain will have to respond to the growth in demand without compromising sustainability, and despite rising temperature. Commodity traders must remain adaptable, if they are to negotiate this difficult path. Extraordinary times call for an extraordinary response, in this case new collaborations and innovative solutions. State-owned enterprises (SOEs) have become influential in the global economy in the past decade, and with their declared intent to increase control over supply, they are gaining ground in commodity trading. Over the years, SOEs considered several strategies for entering the sector, from direct purchase to minority or majority equity participation in existing trading houses. They have often become direct competitors of existing players, but recently exposed vulnerabilities in the sector suggest that partnership rather than competition may be a better way to make their mark.

Theory indicates that supercycles recur every 20 to 40 years, and as the last one peaked in April 2011, we shouldn’t see another until 2030 at the earliest. Yet, following a significant drop between April 2011 and February 2016, the average commodity index has increased by nearly 40% over the last year. Are there potential drivers for the deep shift in the supply/demand balance that could trigger a new supercycle? The question is open to debate. Trump’s $1 trillion plan for the renewal of US infrastructure has raised some people’s expectations of commodity price increases, while others believe that the demand resulting from an increase in infrastructure spending in the US is likely to be limited.

Some drivers impact the supply/demand equilibrium in smaller markets too. With the energy transition, lithium is expected to experience the fastest increase in demand of any significant commodity over the past century. Demographic growth in India, and associated food habits, are curbing the supply/demand ratio for pulses, which are no longer considered a niche market. Many agricultural commodities are under severe threat from global warming. As an example, coffee production is likely to drop by 20 to 25% by 2050. The Swiss commodity hub continues to function efficiently, sailing through price movements, evolving political agendas and continuous innovation.

Traders redefine their business strategies in order to thrive in a world that is changing at breakneck speeds, delivering political agendas and continuous innovation. The Swiss commodity hub continues to function efficiently, sailing through price movements, evolving political agendas and continuous innovation. Traders redefine their business strategies in order to thrive in a world that is changing at breakneck speeds, delivering political agendas and continuous innovation.
Working together through challenging times

In an environment full of uncertainty, constructive collaboration across all stakeholder groups is critical.

David Fransen, President, STSA

 эффективность стал важным элементом в любой области деятельности. Финансовые рынки также требуют того, чтобы участники понимали, как их действия влияют на общество. Нельзя недооценивать значение информационной прозрачности и открытости в современном мире, где информация играет ключевую роль в принятии решений.

С точки зренияأنواع продуктов, важным является понимание их происхождения. Банк NESTLE, например, активно занимается этническим происхождением продуктов и стремится обеспечить их прозрачность по всему циклу производства.

В свете этих изменений, участники рынка должны быть готовы к новым вызовам и готовы к сотрудничеству с целью объединения усилий и решения общих проблем. Это может быть достигнуто через открытость, прозрачность и доверие, которые стимулируют социальную ответственность и устойчивое развитие.

В заключение, можно констатировать, что работа вместе, несмотря на разные мнения и интересы, является путь к решению сложных проблем и обеспечению благополучия всех участников. Это требует наличия открытой и искренней коммуникации, понимания и уважения различных взглядов, а также готовности к совместной работе.

Switzerland: a 150-year trade leader only recently awakening public curiosity!

Stéphane Graber, Secretary General, STSA

id you know that Switzerland was already a trade leader 150 years ago? And that in the 16th century Geneva was one of the “loftiest” places for trading goods between northern and southern Europe, leading the Medicis to develop the first banking activities in Switzerland to support such trade? Later in the 18th century, returning Swiss expatriates brought with them the unique value of an international network, and trade went on to enrich Swiss families such as the Stockalpers, silk merchants of Brug. Did you also know that after World War II, the only freely convertible currency in the US dollar? Was the Swiss franc then? Finally, in today’s increasingly protectionist environment, who remembers that Switzerland’s wealth is partly a product of immigration, being a safe haven for foreigners and refugees who contributed to the development of important industries for the Swiss economy such as watchmaking, Egyptian cotton, and even Nestle’s iconic powdered milk?

With increased importance and visibility comes heightened responsibility. It was evidenced in the 2016 federal referendum spurred by the Young Socialists’ initiative against speculation on foods, tuffs, and the successful campaign of STSA and its members at the national level (leading to almost 60% voting against the initiative). These events are still relevant in 2017, as the broad NGO coalition behind the Responsible Multinationals Initiative seeks to make up for the lack of transparency and to promote its initiative, aided by the lack of public understanding of commodity trading activities.

This should be viewed as an extraordinary opportunity – a threat to engage with the public on the economic significance of commodity trading which is indispensable to our everyday lifestyles. Five years ago, who cared about the origin of their Nescafe coffee, its cultivation, transportation and processing? It is precisely this new-found curiosity that represents a unique opportunity for our industry to inform the public about our complex value chains, as well as the issues facing our companies in the fight against corruption and money laundering. Since last year, this has resulted in STSA proactively embracing the opportunity to communicate to the general public and private sector actors, activities, and corporate governance. Notable milestones have included the creation and publication of an animation movie and the enforcement of a Code of Conduct endorsed by all of the Association’s members. This has taken shape through a multi-channel approach to reach interested members and the public at large in order to better inform their understanding of the commodity trading sector. In addition to the use of LinkedIn and Twitter, this has also taken form through the launch of a new YouTube channel and a brand new website.

STSA together with its members are testament to the ability of the industry to adapt to the changing environment and to prepare the industry to successfully overcome future challenges. The importance of our industry cannot be understated, as it can play an influential role in global issues such as food security. The landscape is changing, with the emergence of new actors and the evolution of technology (perhaps leading to the next supercycle). Moreover, increased regulation has brought higher financial costs linked to its implementation, and has highlighted the persistent lack of regulatory harmonization. The ability of STSA to bring together the industry around these important issues as demonstrated in this magazine and to work together despite the diversity of industry members in transatlantic, transnational and in multi-stakeholder initiatives including the Swiss multi-stakeholder dialogue on the UN guiding principles on business and human rights and commodity trading corporate responsibility. In parallel, the Swiss based energy sector continues to work with stakeholders in the EITI commodity trading working group to establish an appropriate framework for transparency and accountability. The participation of the National Oil Companies from some producing countries has been critical. They are our customers and without their participation and support, this process is simply not possible. These initiatives are relevant and important and, we hope, will result in meaningful positive outcomes.

Paperwork takes time and costs resources, which is particularly difficult for some of our smaller member companies. There were no real benefit it would be a waste indeed. Our industry, Switzerland and indeed the world faces uncertain times at present. Many of the challenges we face transcend borders and they are all complex. Switzerland has long benefited from a large and prosperous trading community, attracted by its stability and collaborative approach. In a world where confrontation is driving schemes through our society and our politics, collaboration is a rare and valuable behaviour. Only by working together, as an industry, will our stakeholders in Switzerland and beyond, will we be able to drive progress and the positive benefits that global trade can bring.
Entrepreneurs shouldn’t have to be their own wealth managers.
Business environment for Swiss based commodity trading companies: insights from the 2016 survey

The survey conducted by the University of Geneva between March and July 2016 provides a first static picture of the interplay between commodity trading companies and their environment in Switzerland. These companies are characterised by their international outlook and activities. In the 20th century they have increasingly made Switzerland their home to the point that over the decades they have grown to represent a significant share of the national economy. Considering the high mobility of the activities of such companies, it is imperative to understand how they perceive the business environment in Switzerland and how it determines their continued presence in the country.

Overall, the commodity trading companies appear to be satisfied with the general business environment in Switzerland, with over 70% of the respondents considering it good to very good. It is also considered as one of the most important factors for three quarters (75%) of the companies surveyed. The regulatory environment ranks as the most important factor with 80% describing it as being very important. However, this factor is only ranked 4th when it comes to the level of satisfaction since 70% consider it as good or very good. While it remains an excellent result, we might assume that it reflects the increasing regulatory burden on the industry since 2006, with for example the recent new rules on the use of derivatives as part of a larger financial regulatory body introduced after the 2008 financial crisis, the REMIT regulation of wholesale energy markets, as well as other rules such as the REACH regulation on hazardous chemical substances. In a context where new regulatory proposals are flourishing every day, the relevance and international consistency of such regulatory projects should be dealt with caution and clearly assessed before moving forward.

Political and economic stability is clearly considered by the surveyed companies as the most positive element in Switzerland, since around 90% perceive it as good to very good. Not only is it considered as very important, it ranks as one of the three most important factors. The results also show some interesting insights into companies’ perception of corporate tax. 70% of the responding companies consider corporate tax as a very high priority, however the level of satisfaction is in comparison with other factors rather low, as 40% of the surveyed companies consider it very bad or bad. It is even worse when it comes to individual tax, where Switzerland seems to underperform compared to other factors. This clearly reflects the fierce fiscal competition from other trading hubs.

A last important finding is the quality of the workforce and the ease to recruit staff. While it is not the most important priority for companies (65% consider it very important), around 60% consider it as good or very good. This finding highlights the importance of training and education in the area of commodity trading and the quality of the expertise available in the country.

Thus, in addition to a favourable tax policy, these figures suggest that what is central to commodity trading companies is the general quality of the business environment, combining knowledge, competence, and expertise. However, the economic and political stability that characterises Switzerland has undergone some changes. The Minder Initiative against excessive corporate pay that was accepted in 2013, the Initiative Against Mass Immigration accepted in 2014, and more recently the rejection of the Corporate Tax Reform III on 12 February 2017 contribute to give the perception of a less stable and foreseeable business environment in Switzerland. While the Swiss population tended in the past to always support the business community in referendums and initiatives on economic issues, the global financial crisis also affected the trust of the Swiss population in its companies, which are more challenged than ever before in public votes. These findings underline the importance for economic actors to better address public concerns in order to ensure a stable and foreseeable legal outlook for companies. This also holds for an industry such as the commodity trading sector that represents an important part of the Swiss economy.
Commodities – The Swiss sector analysis

Publication of the first scientific study on commodity trading in Switzerland

The Swiss Research Institute on Commodities (SRIC) recently published the first scientific study on the commodity trading industry in Switzerland. While commodity trading is an important economic sector representing 3.8% of the Swiss GDP, it is still largely unknown to the public. The publication of the results of a unique representative survey on commodity trading companies provides a first preliminary overview of the sector and offers important insights that are of particular relevance in the current debate and that have important policy implications. The SRIC study thus informs the discussion on commodity trading in Switzerland that often relies on widespread public perceptions of the industry supported by limited empirical evidence and draws a very different picture from these.

The study was conducted by the Institut de recherche appliquée en économie et gestion (IRG) from the University of Geneva and the Haute École de Gestion. The Swiss Trading and Shipping Association contributed to the study by providing a list of about 500 companies active in the sector which constituted the population from which the representative sample was drawn (the Federal authorities estimated the number of commodity trading companies at 550 in 2013). Thanks to the definition of the population of commodity trading companies in Switzerland, one of the major outcomes of the survey is the update of the so far under-estimated number of direct jobs provided by the industry. As of 2016 it provides over 35,000 direct jobs, bringing the commodity trading sector more in line with the typical employment to output ratios that are observed in other comparable sectors. In addition it informs about the distribution of these jobs across companies and shows that the commodity trading sector in Switzerland is dominated by small and medium enterprises. Indeed, over 80% of the entities performing commodity trading activities in Switzerland have less than 100 employees (see Graph 1). This goes against the commonly held view that the commodity trading industry in Switzerland is mainly comprised of large multinational enterprises. Of those surveyed, 44% have less than 50 employees and 65% have less than 1,000 worldwide. It also depicts a very diverse sector in terms of origination and destination of commodities, but with Europe dominating in both cases. Indeed, almost 40% of the traded commodities originate from Europe, and close to 40% are destined to Europe. Switzerland’s position at the heart of the continent clearly provides trading companies with a strategic location. Therefore, whilst common perceptions suggest that the sector is operating from Switzerland mainly in order to benefit from favourable regulations, the importance of commercial factors such as customer proximity and geographic advantages should not be overlooked. A commodity trading company needs a presence in Europe, and Switzerland is a well-suited option, offering a stable business climate which plays an important role in explaining their presence in Switzerland (see article on the general business environment in Switzerland on page 6).

The study also addresses financial aspects of the sector in Switzerland. An important finding is that trading companies have been subject to strong national and international financial regulations. Consequently, being under the direct supervision of banks, commodity traders are regulated through banks. This offers support to and is consistent with the Federal Council’s practice according to which a direct FINMA supervision is of no additional use (Federal Council 2013).

Some insights on the turnover figures of commodity trading companies can also be found in the study, which underlines the strong dependence of the turnover on the type of commodities traded. It shows considerable differences across families of commodities given the price differences across commodities. This finding illustrates the fact that turnover figures are not the best indicators of the size of the industry since they strongly depend on the commodity traded.

In sum, the findings depict an industry in Switzerland dominated by SME structures that are mainly privately owned (91.5% are privately owned). The surveyed companies are strongly rooted in Europe since their main geographical markets are located in this region, focusing their activities on trading and trade finance, and concentrated in the three historical areas of this activity in Switzerland (Lake Geneva Region, Lugano and Zug). It also shows that, for Switzerland at least, the sector’s companies cannot be assimilated to large multinational enterprises. Commodity trading companies’ strong links to Switzerland have much to do with the overall business environment, expertise in the field, in particular the availability of highly skilled workers, and proximity to their markets (Europe).

This publication is thus a first step towards the systematisation of information on the sector, helping to overcome some common misunderstandings about the industry in Switzerland. It calls for a regular monitoring under the auspices of the Swiss Research Institute on Commodities. The monitoring should also be completed by the development of a code for commodity trading in the Swiss classification of industries (3-digit NOGA code), so that data does not capture commodity trading specifically but incorporates the activities within different categories. This would significantly improve our knowledge of the sector and overall grasp of a heterogeneous industry sector that is largely unknown from the general public, and ally misconstrued notions of opacity.

(1) The complete report of the study is available at https://goo.gl/VwBZMRP
ENSURING FOOD SECURITY

We must give greater attention to the sustainability of our value chains if we are to meet the objective of global food security.

Trade’s essential role in the quest for food security and safety

Trade and food security concerns can be better articulated within the multilateral trading system through improvements to the World Trade Organization’s (WTO) Agreement on Agriculture. However, the right balance must be struck between the benefits of growing awareness by regulators and consumers on matters such as health and environment, particularly in developing countries, and the policy space required by developing countries according to their specific country-level needs.

The linkages between trade and food security have been subject to intense debate. A key challenge that pervades these discussions is the compatibility between measures intended to address national food security concerns on one hand, and their effect on the food security of trading partners on the other. It is argued that the food security of one country ought not to be at the cost of food insecurity in another. Trade will increasingly influence the extent and nature of food security across the globe. The challenge, therefore, is how to ensure that the expansion of agriculture trade works for, and not against, the elimination of hunger and malnutrition. Greater participation in global trade is an inevitable part of most countries’ national trade strategies. However, the process of opening up to trade, and its consequences, will need to be appropriately managed if trade is to work in favour of improved food security outcomes.

Trade, though not sufficient, is an essential tool for ensuring food security as it affects many of the economic and social variables that ultimately determine a population’s food security and nutritional status. This includes growth, incomes, poverty levels, food and trade flows. The likelihood of spikes, even if episodic, needs to be factored into longer-term decisions related to the management of trade in food and agricultural products.

Trade, through its potential to detrimentally impact those most in need of access to affordable food staples, has the potential to be exploited pose severe obstacles for traders. Measures should not detract from their public health or environmental protection objectives, but rather should be designed to ensure that those most vulnerable in society are not at a disadvantage. The linkages between trade and food security have been subject to intense debate. A key challenge that pervades these discussions is the compatibility between measures intended to address national food security concerns on one hand, and their effect on the food security of trading partners on the other. It is argued that the food security of one country ought not to be at the cost of food insecurity in another. Trade will increasingly influence the extent and nature of food security across the globe. The challenge, therefore, is how to ensure that the expansion of agriculture trade works for, and not against, the elimination of hunger and malnutrition. Greater participation in global trade is an inevitable part of most countries’ national trade strategies. However, the process of opening up to trade, and its consequences, will need to be appropriately managed if trade is to work in favour of improved food security outcomes.

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Reshaping the agricultural supply chains

It’s been said that “the pace of change will never be slower than it is today.” At Cargill, we are seeing rapid industrial and geopolitical shifts—from rising protectionism and rejection of international trade agreements-deals that have immediate impacts on our business, our communities and our ability to build a resilient food system.

In the midst of all this change, the world’s population is growing. This has resulted in a complex global food system that has sustained us for thousands of years, the amount of food traded is rising, and will continue to provide high quality, nutritious food to millions of people.

The lack of harmonised regulation is crucial that policies focus on sustainable agricultural practices, improving market access and productivity for farmers, and supporting childhood nutrition and education around the world. Companies have invested heavily in systems applying broad, comprehensive, science- and risk-based approaches to food and feed safety to ensure the safety and integrity of products worldwide. However, the industry must do more to raise awareness on the impact of inconsistent regulation and the lack of coordination across governments, NGOs, policy-makers and consumers.

Social and environmental goals need to be taken seriously, but food and feed safety challenges are at the forefront given their impact on food security. Issues around the lack of import tolerances for pests and diseases on data submission on active substances or residues, and slow renewals of active substances cause uncertainty and increasingly disrupt trade. Trading houses internationally have mapped nearly 2,000 Cargill sourcing points for cocoa, palm and soy to establish a baseline for tree cover loss and gives us a way to concretely and transparently measure our progress. These early results signal an important path forward to make serious and long lasting changes in global supply chains and new—and sometimes unlikely—alliances need to become a critical part of the equation. Thirdly, as the world is changing, we all need to be looking forward. We need to anticipate disruption. This means envisioning what finance structure and regulations need to address reality where new uncertainties, more volatility and more risk are the new normal. And at a time when the signs of protectionism are re-emerging we need to establish the benefits of global trade. Open trade means farmers can continue to ensure that crops are grown in the right places at the right time. It means an industry can continue to move food from areas of surplus to areas of deficit without facing more barriers. It means governments can adequately respond to the challenges of food security, sustainability and nutrition, a new, complex layer of challenges is emerging as food security, climate and political stability become inextricably linked. We need to be cognisant of these dependencies, and what anticipated, unexpected or unintended consequences they may create. How well we prepare to deal with these changes will be in part small determine the resilience of our food system to cope with this pace of change in the months and years to come.

The lack of harmonised regulation on food safety and security

The Grain and Feed Trade Association (GAFTA) has been addressing the intersection between food security, sustainability and nutrition, a new, complex layer of challenges is emerging as food security, climate and political stability become inextricably linked. We need to be cognisant of these dependencies, and what anticipated, unexpected or unintended consequences they may create. How well we prepare to deal with these changes will be in part small determine the resilience of our food system to cope with this pace of change in the months and years to come.

Increasingly non-scientific arguments in regulatory decisions create compliance difficulties.

Tackling the approval process in their relevant jurisdiction. Again, this is not a safety issue, but one of compliance for a period of time until all government safety authorities have tackled the approval process in their relevant jurisdiction. A low level presence solution (LLP) is needed on a global level to provide the industry with a commercially feasible level of certainty. We are also seeing a lack of harmonisation globally in how to deal with new plant breeding innovations, as well as techniques which hamper innovation and investment. A recent example is the proposed EU rules on comitology to approve GMOs or MRLs, which are expected to impact trade and create further delays in adoption. These rules must be based on sound science.

Trading companies hold themselves accountable to fully implement global food safety approaches and continuously seek ways to improve the food safety system in our supply chains. This is not something that can be done in isolation. New alliances will lead to creative solutions to tackle these issues in the agriculture and food supply chains and the private sector has a critical role to play in helping scale up solutions. Collaboration will power investments across the entire supply chain, including with governments, farmers and their communities.

There are examples where action is already being taken. As an example, earlier this year the Cargill Report on Forests set out our progress against a series of commitments to eliminate deforestation in all of our supply chains. One of these efforts will not enable us achieving these commitments and we have established new alliances with NGOs and other private sector partners to advance long-term solutions to end deforestation. These partnerships are helping us reach more than 140,000 farmers and suppliers to protect forest regions in Brazil, Indonesia, Paraguay, Zambia, Côte d’Ivoire and Ghana. They have provided invaluable expertise to help monitor and manage deforestation risk in our supply chains. Partnering with the World Resources Institute’s Global Forest Watch we have mapped nearly 2,000 Cargill sourcing points for cocoa, palm and soy to establish a

INCREASINGLY NON-SCIENTIFIC ARGUMENTS IN REGULATORY DECISIONS CREATE COMPLIANCE DIFFICULTIES.
Soil biology plays a big role in crop production, whether managed directly or not. Green Tech is ushering in agriculture’s biological Era.

Climatic change is often discussed in abstract terms, but it was recently made a reality for banana growers in the Dominican Republic. The island nation suffered through a prolonged drought in 2015 followed immediately by torrential rains and flooding the following year. Unfortunately, bananas require large amounts of soil moisture but cannot tolerate flooded soils, making them especially sensitive to the increased variability caused by climate change. The two years of extreme weather in Dominican Republic were devastating for the country’s banana industry. Bananas are not the only crop feeling the impact of climate change: coffee and cacao, for example, are also under threat, and some estimate that suitable coffee production area will be cut in half by 2050.

The Physical Era began in the mid-20th century, when an explosion of scientific innovation allowed farmers to manage the crop’s chemical environment in ways they never dreamed of. While the tillage and seeding practices of the Physical Era continued, the use of chemical fertilizers allowed massive yield increases. Of course, these increases came with their own challenges: poor management could lead to nutrient leaching, runoff, and other environmental problems. Solutions to these challenges have included technologies like slow-release fertilizer coatings, and increasingly strict regulatory restrictions on fertilizer use.

Now, in the face of increased climate variability and shifting climate “normals” around the world, agricultural innovation has been exploring and developing tools that use biological processes to improve crop production. Physical and Chemical Age technologies and practices have always been affecting these biological processes indirectly — but in the Biological Era of agriculture, new technological and agronomic developments have made it possible for farmers to manage soil biology directly through integrated soil fertility management, and with technologies like biofertilizers, inoculants, and biostimulants.

Soil biology is still largely a mystery, and scientists have only identified somewhere between 5-10% of the microbial species living in soil. However, we know enough by now to see that “good” biology is crucial for agricultural productivity. Soil biology has been identified as a key factor within the Climate-Smart Agriculture framework for climate change mitigation and adaptation. For example, soil biology builds soil organic matter to store carbon, and breaks organic matter down to release carbon back into the atmosphere. The balance between these two processes determines whether a soil is a carbon source or a carbon sink, and the goal is to tip the scale in favour of building soil organic matter. Soil biology can also be managed to help farms adapt to climate change. Building soil organic matter not only sequesters greenhouse gases from the atmosphere, but also makes soils more resilient in the face of changing temperature and moisture regimes.

Ag tech developments have been increasingly focused on biological solutions — as evidenced in the growth of biological agricultural products sold on the market today (see figure). In 2016, marketandmarkets.com estimated the size of the global agri-cultural microbial market at US$2.2 billion, with projected growth to $5.0 billion by 2021. Similarly, biofertilizers were estimated at US$1.8 billion, with expected growth to $2.9 billion by 2021. Back in the Dominican Republic, some banana growers had been using biological technologies — including Earth Alive’s Soil Activator biofertilizer — at the beginning of the drought in 2015.

We learned that while the plantations in their region had seen yields drop by 50% or more during the drought, their yields had been similar to previous years. The successful management of the biology of their soils had a profound effect on their farm’s climate resilience. The results we saw in the Dominican Republic led us to establish our Mocha Initiative, a collaborative research program in the cacao and cacao sectors that seeks to develop new sustainable production methods built on healthy soil biology. The biological approach will surely bring significant value to all members in the agricultural sector as we move into a future increasingly defined by the challenges posed by climate change.
Biodiversity is of existential meaning for food security protocol

Biodiversity needs agriculture and agriculture needs biodiversity. This may sound like a paradox but it isn’t. It is the message of the International Year of Biodiversity in 2010. What is clear is that biodiversity needs agriculture and agriculture needs biodiversity. Amid growing environmental concerns around agricultural activities (for example, animal and plant species), this symbiotic relationship will be instrumental in fostering the right environment for food security. Biodiversity is not a static state. It continuously evolves and adapts within our changing environments. Until the end of the 19th century, the development of various farming activities led to a multitude of different habitats. These new habitats formed to provide a living space for new or evolving species, which in turn adapted over time to changing conditions within these habitats. Later, industrial advances led to the use of machinery and production inputs which demanded more uniform units. This shaped agriculture and its structures in different ways, leading to monotonous landscapes, a loss of diverse habitats and a loss of biodiversity. Despite these changes, agriculture nevertheless continues to rely heavily on biodiversity. Indeed, we still have a diversity of land-use types and environments that would not exist without farming, providing habitats for various wild and domesticated plant and animal species. This vast reservoir equips us with a myriad of possibilities for adapting to future changes in the environment, such as the looming threat of climate change for plant and animal production. Genetic diversity for example enables us to select the variety most suitable in any given change. Take apples. In fact, our domesticated apple varieties are highly susceptible, there being fire blight, a severe pathogen in apple production. On the other hand, some wild apple varieties are resistant to this bacterium. Using various breeding technologies, researchers are working to transfer resistance from the wild variety to our domesticated varieties. Biodiversity can also support the regulation of pests and plant diseases. Whilst diversity in any ecosystem develops even without any action from farmers, beneficial organisms can be maintained and fostered in order to control pests and diseases. In Switzerland, an intensive study is currently taking place in order to support the diversity of beneficial organisms. To that end, research is being conducted on strips of crop fields which are used to grow plants and provide living spaces for these beneficial organisms. Through the abundance of these species, also called functional biodiversity, the pressure from insects and other pests on crops is reduced, allowing for lower pesticide use. Biodiversity can also help to ensure food security in different ways. It provides a basis for stable yields both today and in the future. Whilst mankind has relied mainly on a limited selection of crops (rice, wheat and corn) and meat (stemming from only one parental line), biodiversity can ensure a diverse diet, thereby supporting nutritionally-sensitive agriculture. However, there are many trade-offs in the relationship between attaining biodiversity and food security. In the short term, it may make sense for a farmer to reduce diversity in his fields and rely only on those varieties that are best adapted to our current natural, economic and social environment in order to use the resources more efficiently. Thus, the important task of fostering wild and functional biodiversity lies with our policy makers and agricultural research and development.

Phytosanitary regulations: the need for a better middle-ground

Phytosanitary activities in agricultural products often revolve around balance sheets, quality specifications and futures markets, in addition to the more practical elements concerning the products themselves, such as transportation and shipping. Within the confines of this area of the business, phytosanitary organisations and their specific requirements can sometimes be overlooked. People in our business, especially traders, could benefit from taking a closer look at such requirements. Any harmful pest or plant disease could lead a trade to fall through, or goods to be refused at the port, causing unnecessary waste and inefficiencies. At a time when the world is facing the challenge of feeding a growing population, the loss of 0.85% of agricultural products (equivalent to US$ 4 billion) due to rejection at import borders is not insignificant. Phytosanitary organisations have their roots in two important events. The first was the phylloxera crisis, commonly known as the Great French Wine Blight. The outbreak of a severe parasite destined for vineyards of the French wine industry and nearly obliterated the local wine industry in the mid-19th century, which highlighted the need for more careful use of certain practices and products. This led to the adoption in 1881 of the International Convention Respecting Measures to be Taken Against the Phylloxera Vastatrix. The second was the Berne Convention, a binding international legal instrument in the field of nature conservation which came into force in 1982. The former became a part of the International Plant Protection Convention (IPPC), which was adopted in 1952. The IPPC aims to ensure coordinated, effective prevention of the spread of plant blights, and to control the introduction of plant products. It also aims to facilitate trade through international standards that regulate the safe movement of plants and plant products. Nevertheless, this aims to be a market trend towards adopting international standards, almost blindly, in order to facilitate trade. This may not necessarily have a positive impact on the market. While it is easy to acknowledge that proper regulation could protect the industry and ultimately the consumer, there is some room for improvement where the enforcement of international phytosanitary standards is concerned. Over time, the market has experienced some challenges as between phytosanitary organisations and trade actors. This is illustrated by outdated or unrealistic rules, both of which can lead to inefficiencies. For instance, phytosanitary organisations require that products be fumigated with methyl bromide, a fumigant that has been forbidden in several countries around the world. Further examples include stringent regulations on products that are intended to ensure they are disease-free. While it would be foolish to disagree with this principle, the reality is more complex. The standards outlined in these regulations bring our products nearly to the same level as pharmaceuticals. But because of the conditions in which our products are shipped (in bulk, in the belly of Panamanian vessels), these standards are practically impossible to meet in full. In addition to these restrictions, even at a time when communication is easy and instantaneous, some phytosanitary organisations do not always provide sufficient information to merchants. Only a few organisations inform the industry appropriately when a product’s destination or origin is not accepted for certification. As a result, we may discover too late that we are unable to distribute our goods. This causes products to be quarantined at the border. Due to the number of pending phytosanitary regulations in relation to quarantines, ensuring their release can be a difficult, lengthy and costly process. Finally, a further challenge includes the occasional lack of flexibility encountered at some of the organisations, as well as a complex bureaucratic process that is the practice in some of the certified countries. Undoubtedly, the current situation is, to a certain extent, a reflection of a wider lack of industry cooperation internationally. Phytosanitary organisations are, however, essential to the international trade of agricultural protection products. With such improvement, they could be very beneficial to the industry and consumers around the world. In order to get there, the communication flow by means of an electronic phytosanitary certification system (such as ePhyto), as well as to clearly defined, realistic requirements, could be a good place to start. *(1) Leffler and Spence, “Standards and agro-food exports from developing countries: rebalancing the debate”, World Bank p. 21*
Trade policy can help governments achieve the targets of the 2030 Agenda for Sustainable Development to end hunger and malnutrition.

Why policies on trade and markets matter

Recent international commitments on food and nutrition security could have significant implications for trade and markets between now and 2030, if governments follow through on the Sustainable Development Goals (SDGs) they agreed at the UN General Assembly in September 2015. However, doing so will require them to work together towards shared objectives. The 2030 Agenda for Sustainable Development sets a ground-breaking new commitment for all countries: to end hunger and all forms of malnutrition by 2030. The new goals will require governments to address the “triple burden of malnutrition”: under-nourishment, micronutrient deficiencies and over-nutrition. However, achieving this will require closer collaboration in policy areas ranging from trade to climate change, all of which could affect food and agriculture markets in the years ahead.

Trade policy and rules can help governments to achieve the 2030 Agenda targets, such as doubling productivity and incomes for small producers by improving access to markets and opportunities for value addition, and creating rural jobs. Governments also committed to promoting “a universal, rules-based, open, non-discriminatory and equitable multilateral trading system” under the World Trade Organization (WTO). Governments have made rapid if uneven progress in fighting global hunger, with 200 million fewer people undernourished since the 1990s according to FAO data. Reductions in under-nourishment have been driven primarily by progress in Asia, especially China, while in Africa the number of undernourished people increased by almost 49 million over the same period – despite a drop in the overall share (due to rapid population growth). Meanwhile, recent success in reducing micronutrient deficiency has still been too slow to hope to end malnutrition by 2030, while overweight and obesity have worsened. Despite falling food prices in recent years, many poor countries also remain vulnerable to sudden market shocks, given the evidence that climate-related extreme weather events will become more frequent and intense. Changing climatic conditions are also causing fish stocks to migrate, with potential consequences for nutritional outcomes in low-latitude countries. At the same time, OECD and FAO estimates suggest that in the medium term both production and consumption are due to grow, in line with the requirements of a growing global population with higher average incomes. However, Africa’s consumption of rice, wheat, vegetable oils, and sugar is expected to grow much faster than production, while Latin America is set to continue producing more oilseeds, meat, fruit and vegetables than the region is set to consume. Similarly, fish production and trade is also projected to expand in coming decades, with the volume of trade in fish products growing by some 40% towards 2030. While Africa is expected to export more, Asia is due to become a larger importer.

Agriculture and trade policies have also changed significantly in recent decades. Some developed countries which previously provided heavy subsidies to their farm sectors have now reduced the levels of trade-distorting support they provide. Meanwhile, several large developing countries have moved towards providing increased domestic support for the sector. Tariffs on farm goods have also fallen in all world regions due to unilateral liberalization and preferential trade deals. Tariffs and non-tariff barriers nonetheless remain significant on “sensitive” farm goods such as beef, dairy, rice, and sugar. Current WTO rules provide considerable scope for governments to boost farm productivity and raise rural incomes. For example, by allowing unlimited support for “public goods” such as pest control, research, rural infrastructure, sustainable irrigation schemes or farm advisory services. Governments will nonetheless also need to fast-track multilateral talks on meaningful new rules in areas such as agricultural domestic support, fisheries subsidies and access to markets for farm goods. Governments could also usefully prioritize trade policy initiatives that aim to create jobs and raise rural incomes among food-insecure groups, including through steps to improve the functioning of non-agricultural markets. They will need to expand domestic food aid for poor consumers, perhaps financed through international collaborative action. Effective trade policy measures to mitigate volatility in global markets are also likely to become more important – such as better global rules on export restrictions to prevent price spikes from harming consumers in poor food-importing countries. However, governments must not shy away from the difficult questions. If ‘business as usual’ continues, the FAO and OECD estimate that over 600 million people will be undernourished by 2024, a number which is far short of the 2030 zero hunger target. At the same time, the world is facing a nutritional transition leading to serious problems of obesity and related health problems that need to be addressed. Negotiators will therefore need to demonstrate they are willing to tackle thorny subjects such as the issue of agricultural domestic support: many hope that the WTO’s 2017 ministerial conference in Buenos Aires can achieve progress in this area, despite the historical difficulties in doing so. While policy-makers may feel daunted by the scale of the task ahead, steps forward on agricultural export subsidies at the WTO’s Nairobi ministerial conference in 2015 suggest that incremental progress is both feasible and realistic, so long as governments are willing to work together to achieve shared goals. If they can agree to do so, government officials now have an opportunity to take concrete measures towards ensuring that more equitable and sustainable markets actually contribute to the goals of ending hunger and malnutrition.

* This piece is based on the report Trade, Food Security, and the 2030 Agenda, published on 10 October 2016 by the International Centre for Trade and Sustainable Development.

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**Trade**

**Policy**

**Can help governments achieve the targets of the 2030 Agenda for Sustainable Development to end hunger and malnutrition.**

**Why policies on trade and markets matter**

**Recommendations**

**Steps forward on agricultural export subsidies suggest that incremental progress is both feasible and realistic.**
Who will disrupt the disrupters?

Digital technologies challenge commodity markets and force you to transform your business model. We can help you evolve your trading operations and provide new approaches to work toward boosting your success.

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The better the question.
The better the answer. The better the world works.
State-owned enterprises are increasingly present in trading. As commercial operators and as government entities.

STATE-OWNED ENTERPRISES (SOEs) ARE RESILIENT TRADING FORCES

In recent years, a growing focus on commercialisation has swept SOEs within the commodity trading industry. In the past, the state or SOEs (operating outright or in joint ventures) would simply sell the physical resources, often to private trading companies. However, Soca’s takeover of a commodity trading house in 2015 is just one example of SOE commercialisation efforts as countries such as Azerbaijan, Saudi Arabia, China and Russia are increasingly building on their activities to both procure and market commodities directly, investing in downstream consumer markets. Indeed, government-owned Chinoil is one of the biggest traders of Middle Eastern crude today, handling some 2.6 million barrels in 2014. Governments may also use SOEs (and so-called ‘state-trading enterprises’ under WTO terminology) to pursue particular strategic objectives. For example, the trade policies of the Chinese Ocean Group (a regulatory marketing board) has restructured its national cocoa and coffee value-chains with the stated overriding aims of increasing farmer livelihoods, and the Ocean Group’s market participation since the 1990s has led to spot contracts involving a variety of different actors. Nevertheless, governmental influence remains significant. And justifiably, SOEs are now seen as powerful tools for public value creation.

In this context, SOEs have become direct competitors rather than competitors? New entrants with considerable firepower

Focus on the energy sector in China (but recognising that the same is true in India where the energy sector is currently being reorganised), big national groups are initial producers or refiners who are implicitly responsible for supplying and implementing the country’s energy policy. Over time, simple supply needs have been outgrown and SOEs have become key market players, keeping in the hands of a few the access to large amounts of oil, coal, metals and oil products. Pressure to reinforce security of supply has led SOEs to diversify their commodity access, from bilateral negotiations and sourcing control to more regular participation in markets, including peer transactions. It is not without causing real stability problems for markets whose price-fixing principles are based on reference price systems (benchmarks) and whose representativeness is based on the diversity of stakeholders and a fair balance of negotiated volumes. Unlike trading companies buying and selling on the market on a daily basis, SOEs naturally turn only in one direction, like buying for example. On several occasions, record volumes have been negotiated by some lead actors in the so-called ‘Platts Windows’, the reference period that sets product prices when the market closes each day. SOE trading subsidiaries are obviously on both sides of the market but the trading volumes are so important that there are benchmark bias risks (see August 2015 incident on Dubai’s market). SOEs are looking for a new way to participate in global commodity markets by announcing agreements with existing trading companies.

SOEs: competitors who become partners

SOEs are looking for a new way to participate in global commodity markets by announcing agreements with existing trading companies.

**A model reaching its limits**

However, vulnerabilities are emerging and SOEs have become commodity mastodons, giants who have become important competitors of existing companies, even threatening the stability of market-based mechanisms. However, vulnerabilities are emerging and SOEs are looking for a new way to actively participate in global commodity markets. By announcing agreements with existing trading companies, will SOEs become partners rather than competitors?

Several options have been tested: direct purchase, minority and majority equity participations. Mixed success and management issues have demonstrated a need for new forms of cooperation. Over the years, the economic and financial environment has progressed, and access to resources is more complicated. Chinese authorities want to increase their impact on pricing, but it is obvious that credible Asian benchmarks implementation will take more time than expected. An effective and controlled participation to existing mechanisms would probably be more efficient.

At the same time, the entire trading sector has become more professional, and advanced expertise is now needed to implement more complex and structured supply chain strategies. It is now time to combine logistics, financial, legal, and risk management expertise. Debt financing also has limited avenues, and we need to find more proactive funding tools suitable for market realities.

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**SOEs: a new breed of trading partners**

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From the 1960s to the 1980s, gas supply chains were rigid, so too will contracts and pricing. As the geography and dramatis personae of world gas markets changed, so too have competitive strategies and business models. As the integrated majors and national utilities. As the SOEs are known by many names – government corporations, government-linked companies, public sector enterprises and so on. While the varying forms of SOEs may provide national states with a means to play an active role in gas markets, so too will complex and pricing. The increased SOE presence in the Global 500 has been driven primarily by Chinese SOEs. In fact, three Chinese SOEs (Sinopac Group, China National Petroleum and State Grid) have consistently made the top 50 largest SOEs since 2010. This underscores the growing revenue share of Chinese-owned SOEs (and from the rest of Asia) among the biggest companies in the world.

For some time SOEs have been increasing presence in the trading space, initially through National Oil Companies, such as SONACOR in Geneva, along with other well know examples such as Saudi Aramco and Gazprom Marketing, moving into a space previously occupied by independent trading houses. This has been a driving force for traders to move more into assets, upstream and towards origination in search of added value in the supply chain. A more recent trend shows SOEs expanding through acquisitions. China’s Cnooc Corp obtained full ownership of Noble Agri and Nidera last year. At the time of writing Noble Group is in early discussions with China’s Sinochem about a possible investment. State-owned China National Chemical Corporation acquired a 12 percent stake in Mercuria, the largest international gas trader, last year and is currently in the process of obtaining regulatory approvals for its acquisition of Syngenta. Driving factors in many of these acquisitions are threefold. Firstly, there is an interest from SOEs in increased control over supply. This is particularly the case for agricultural commodities, due to changes in global food consumption patterns. A second reason is to gain access to marketing capabilities. As shown in some recent headline SOE-trading joint ventures in the energy sector, synergies are emerging. In the case of LNG, the potential for lowing increased trading volumes with access to supply and distribution. Lastly, the access to funding that may be provided, again shows an area of synergy between traders and SOEs. The aforementioned is also visible in global statistics, with petroleum refining a dominant sector and insulate SOEs from the legal framework applied to other companies, including competition laws, bankruptcy provisions or securities laws.

The US shale revolution has driven changes domestically and globally. US dry gas production, stuck below 20 tcf (560 bcm) from the 1970s to 2000s, leapt 50% during 2005-2015. The US today remains a net importer of 20 bcm, albeit well below 2005’s 105 bcm. Natural gas prices of 100 bcm are now expected by 2020, a reversal of expectations even five years ago. LNG import facilities have morphed into low cost liquefaction plant, opening a Pandora’s box, exporting not only US gas, but also gas-on-gas pricing to an international market accustomed to oil indexed contracts. The US and Australia will add 115 million tons of LNG capacity by 2021, contributing to a near-50% global LNG fleet expansion. Australian projects confront cost and project over-runs, so peak new supply may arrive nearer 2020 than trading executives had predicted in 2017/2018. Nonetheless, additional supply will outstrip incremental demand through the early 2020s, even though 2016 demand recovered sharply amid double-digit growth from China and India.

East of Suez demand remains key. Asia takes 75% of today’s LNG and will remain predominant in future. China and India are to the fore, though growth is also taking off in Egypt, Pakistan, Malaysia, Indonesia and Thailand. Asian LNG imports could increase to 250-300 million tons by 2030 from 125 million today. Calls for gas contract flexibility accelerated after the 2011 Fukushima disaster, when Japan’s buyers sought emergent access to diversified supply, and insulated LNG flexibility and high quality spot, hub and oil linkage, all with an eye on sub-$8/mmbtu US Henry Hub prices. Lower post 2014 crude prices gave oil-indexation a reprieve, leaving US LNG less attractive to Asian buyers. Now, with crude prices rising faster than gas, and with power mix uncertainties, Asian buyers will again prioritise flexibly-contracted gas from diversified suppliers.

New business models have emerged to help deal with an LNG surplus that may stretch to the early 2020s:

• traders deploying infrastructure to arbitrage from diverse LNG portfolios to disparate buyers;
• supplier/traders investing downstream in regasification (including flexible, floating capacity and power generation);
• buyers forming collectives to seek supply contract concessions;
• spot and short term deals, now 30% of LNG trade from below 10% in 2005;
• producers, long-winded to oil-indexed, taking on long-term contracts increasingly accepting hub linkage.

Oil indexation and long term contracts will linger (especially for new supplies needed post-2020) but a precedent for diverse, flexible sourcing has been set. A prolonged buyers’ market may ultimately kill designation clauses. Asian price benchmarks and hubs may eventually emerge, around which liquid futures contracts can develop. It won’t happen overnight (European markets took a decade to liberalise), but nor should we dismiss Asia’s ability to progress more quickly.

From a standing start in 2009, Gunvor’s pipe-line gas and LNG business now accounts for 20% of US Henry Hub prices. Lower post 2014 crude prices gave oil-indexation a reprieve, leaving US

in the Fortune Global 500 SOEs as shown in the figure. While SOE involvement in this sector is not surprising, it is interesting to observe emerging sectors in the SOEs’ category, where metals and trading stand out.

SOEs are now a global force. Many, if not most, large SOEs are internationally and engaged in trade, with some emerging country governments pursuing explicit policies of SOE internationalisation. Increased global competition for financing, talent, and resources are seeing some countries turn to SOEs as tools to better position themselves for the future in the global economy.

Many of the countries with the highest SOE shares of gross domestic production are also important traders. For instance, the top eight countries with the highest SOE shares (China, United Arab Emirates, Russia, Indonesia, Malaysia, Saudi Arabia, India and Brazil) collectively accounted for more than 50% of global gas trading.

This could be a result of one of the top five megatrends we have observed i.e. a shift in economic power: (the other four megatrends being rapid urbanisation, demographic and social change, technological breakthroughs, and climate change and resource scarcity).

In our report World in 2050, we indicate that the aggregate purchasing power of the E7 emerging economies – Brazil, China, India, Indonesia, Mexico, Russia and Turkey – will overtake that of the G7 by 2030. China will clearly be the largest economy by 2030, while India could challenge the US for second place by 2050. This shows us the future of where global trading is moving.

It is important to note that the driving forces behind SOEs are different to profit-driven trading houses. SOEs are now a global force. Many, if not most, large SOEs are internationally and engaged in trade, with some emerging country governments pursuing explicit policies of SOE internationalisation. Increased global competition for financing, talent, and resources are seeing some countries turn to SOEs as tools to better position themselves for the future in the global economy.

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Structuring the coffee-cocoa sector in the Ivory Coast

The coffee and cocoa sectors make up an important share of the Ivory Coast’s economy, with cocoa alone accounting for 14% of GDP over the past 5 years. Moreover, the Ivory Coast plays a decisive role on international cocoa markets with its 40% share of global production. In order to rationalise the industry and improve the livelihoods of producers, the government reorganised the national cocoa and coffee value chains with a sweeping reform introduced in November 2011. Inspired by the President of the Republic, its stated objective aims at strengthening good governance and transparency in resource management, developing a sustainable cocoa and coffee economy, safeguarding farmers’ incomes and establishing strong inter-professional bodies. The Commission for the Regulation, Stabilisation and Development of the Coffee-Cocoa Sector, known as the Coffee-Cocoa Board, was created in December 2011, laying down the rules for the marketing of coffee and of cocoa in the Ivory Coast.

A joint undertaking by the State and sector representatives

The Cocoa Coffee Board is responsible for implementing the sector reform, whose main objective is to secure income for producers by setting up a guaranteed minimum price (at least 60% of the CIF price). The Coffee-Cocoa Board acts as a civic enterprise, also working for the well-being of coffee-cocoa producers and their communities through the activities of the Rural Investment Fund (FIMR). Administered on a joint basis by the State and the inter-professional trade body, the Council falls under the supervision of several ministries, notably the Ministry for Agriculture and Rural Development, the State Budget and Planning Ministry and the Ministry of the Economy and Finance, while its Board of Directors is evenly composed of twelve members, with six representatives of the State and six representatives of the industry and of the banking and insurance trade associations.

Three main mission areas with the ultimate goal of benefiting producers

The Coffee-Cocoa Board has three main mission areas: regulation of the coffee-cocoa sector, market stabilisation missions and development missions. Since 2011, the efforts of the Coffee-Cocoa Board have led to an improvement of the overall quality of the coffee thanks to common standards and enhanced controls, besides a strengthened compliance framework, in keeping with the Council’s regulatory missions. The role of the Coffee-Cocoa Board in organising the domestic and export marketing of national production is also key to creating stable buying prices for coffee and cocoa producers. The mission of the Coffee-Cocoa Board however goes far beyond simple market management and supervision. The central policy of ensuring a stable income for producers by providing them with a guaranteed minimum price of at least 60% of the CIF price is supplemented by a number of initiatives aimed at improving the sector’s productivity and improving the wellbeing of local populations. With the financial backing of the Rural Investment Fund (FIMR in French), the Coffee-Cocoa Board has been investing in a number of basic socio-economic infrastructures such as health centres, schools, rural trails, water points and solar energy. Hence its slogan: “the Coffee-Cocoa Board at the service of producers”. The Coffee-Cocoa Board thus regularly publishes tenders for equipment that will directly benefit the populations of the growing areas, such as school kits, water pumps or even housing units. In general, significant investments have been made in the areas of health, education, safety, agricultural access roads, village water supply and solar power. The Coffee-Cocoa Board has also actively engaged with many public and private sector stakeholders both domestically and abroad and has entered into a number of agreements in the framework of the Ivory Coast’s Public-Private Partnership Platform (PPPPP) for sustainable coffee and cocoa value chains. In addition, it works closely with the Agricultural Council and other sector partners on spreading technical skills. Finally, the Coffee-Cocoa Board organises the strategic and sanitary monitoring of the coffee-cocoa sector with a view to anticipating the issues and challenges of the sector.

Conclusion

The new organisation of the coffee-cocoa sector in the Ivory Coast under the Coffee-Cocoa Board is an example of how the State can look to address the challenges of market fragmentation, productivity and farmer income. An improved market governance framework built around a strong public-private partnership can deliver the sustainable development called for in the President of the Republic’s government programme.
**Interview with Arzu Azimov, CEO of SOCAR Trading Group of Companies**

**Do State-Owned Enterprises have a competitive advantage in trading?**

SOCAR Trading is fully owned by SOCAR, the national oil company in Azerbaijan. As the trading arm of SOCAR, the company’s mission since 2008 has been the marketing of the oil and gas products owned by SOCAR. Additionally, SOTC Trading has been developing third-party trading activity since 2013. Today, the gross trading profit on third party barrels represents over 90 percent of its revenues. According to Arzu Azimov, CEO of SOTC Trading, having a state-owned enterprise (SOE) as a unique shareholder does not affect SOTC Trading’s modus operandi, being more pertinent to issues related to compliance and Know Your Customer. “We simply operate as a commodity trading house established on the foundation of a state-owned oil and gas producing company.”

What is the general role of an SOE in trading?

The majority of SOEs in the energy sector are represented by national oil and gas producing companies, operating on the international market alongside private trading companies. However, their interests are not always aligned. Where energy or fuel markets grow constantly, the revenues of producing countries increase proportionally. But for traders, this makes no sense as they need volatility. In competitive markets, following the model of IOCs such as BP or Shell, many national energy companies have established their own trading arms. Some trading arms of SOEs even step into alternative markets unrelated to the business profile of their “mothership.” To give an example, SOTC does not produce steel, nor does it generate coal burning power, so it has no footprint in the coal market. On the other hand, SOTC Trading trades coal and develops LNG projects. In the strongly competitive trading market where nothing is stagnant, we are constantly learning and expanding our role.

Does SOTC Trading own exclusive rights to Azerbaijani oil?

There is no “exclusivity,” at least de jure. In de-facto however, SOTC Trading – as the trading arm of the national oil company of Azerbaijan – has a mandate from SOCAR to effectively market the so-called “system production” of the state oil company. As you may know, a major part of the oil and gas exported from Azerbaijan is produced by international consortia. The state-owned share of this production is also marketed by our company. Regarding volumes allocated to contracting parties in return for investments, we trade those cargos on a competitive basis. As a market leader since 2008, we have managed to build quite an efficient marketing system of Azerbaijani oil.

How much of a competitive advantage does SOTC Trading have compared to private companies?

Having an SOE as a unique shareholder does not affect our modus operandi. Rather, the differences relate more to compliance. Of course, the status may affect our Know Your Customer (KYC) qualification. However in certain projects, having the status of a state-owned entity may help us to participate in government programs or projects.

Because of the nature of its relationship with the authorities, does SOTC Trading trade differently than it would were it private?

The sole difference is based on reputation. The reputation and rating of the SOE would impact SOTC Trading. I would see it more as a virtual factor than a material one, except when we talk about access to credit facilities.

**Interview Elsa Floret**
The current upbeat trend in commodity prices may be a temporary glitch... or a sign of structural change.

After a significant drop of 60% between April 2011 and February 2016, commodity prices are picking up. Over the last year, the average index has increased by nearly 40% with the bulk of the rise attributable to fuel (+54%) and metals (+31%). We are still below the levels of the last peak but the evidence suggests that we are in the early stages of a new bull market. Is this just a bull episode in a bear market or the beginning of another supercycle?

Following the great commodity depression of the 1980s, the last rally began in 2000 (largely fueled by the emergence of the Chinese economy and its seemingly insatiable appetite for industrial commodities. As the theory states, that supercycles recur every 20 to 40 years, and as the last one reached its peak in April 2011, we shouldn’t be seeing another one until 2030 at the earliest.

So what are the potential drivers for the deep shift in the demand/supply balance that could trigger a new supercycle? One of these is Trump’s $1 trillion plan for the renewal of US disoral infrastructure, set to cost trillions of dollars. A lost output and possibly countless lives (as recently seen with the advertised disaster at the Oroville dam). Similarly, after decades of underinvestment and mismanagement, India’s infrastructure is posing a significant threat to its economic growth. According to Finance Minister Arun Jaitley quoted by the Economic Times last summer, India needs over $1.5 trillion in investment in the next 10 years to bridge its gap. Last but not least, according to the Africa Infrastructure Country Diagnostic (AICD), the infrastructure needs of Sub-Saharan Africa alone exceed US $93 billion annually over the next 10 years. Beyond these, some Southeast Asian countries could also start to invest more heavily in their infrastructure and fill part of the growth void created by a slowing China. On the topic of China, it may also be useful to remember that it still represents half of the demand for industrial metals (46%) — with $1.7 trillion spent in 2016 alone — and that its needs are still increasing (+15% for copper and +11% for nickel last year).

On the offer side, low prices have discouraged investment and capacity cuts in the resources and energy sectors. As an example, fundamentals are favourable to copper where, from a peak of circa $71 billion in 2012, diversified total capex shrank to an estimated $25 billion in 2016. Old mines are closing and new ones won’t cover the loss in output. Social and political tensions — in Indonesia, in Chile, in the Philippines — are rising. Rising supply risks can be expected to underpin higher prices.

The prospect of accelerated building in the U.S. has helped to extend a metals rally that began in early 2016 with surprise demand growth in China and copper posted its biggest price gain last year since 2010. How large producers - such as Russia - will respond is yet unknown. Other aspects of the offer/demand equilibrium are also changing. Although, according to BP’s recent outlook, “...oil and gas, together with coal, remain the main source of energy to 2035”, fossil fuels may eventually become “legacy”. The energy transition impacts a whole range of new products from lithium to graphite and from cobalt to neodymium. As an example, lithium demand is expected to rise 16 percent a year from 175,000 tonnes in 2015 to 775,000 tonnes by 2025, “an increase that would be the fastest of any significant commodity over the past century”.

Beyond innovation, demographic growth and associated food habits also curb the offer/demand ratio. The India Pulses and Grains Association states that global trade in pulses has increased almost six fold over the past three decades. With the value of global exports increasing more than 11 times and the unit value of exports nearly four times. Some agricultural products are also severely impacted by global warming. Coffee production is under threat and may drop by 25% to 25% by 2050 at a time when demand is growing by 2.5% p.a.

Supercycles are about timing. If unexpected increases in demand — say in the US and in India — converge and offer cannot respond in time, we may be at the dawn of another supercycle.

Will there be another supercycle in metals?

Although paper markets for steel and iron ore recently reflected optimism, the supercycle is not obvious all at once for these products

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Will there be another supercycle in metals?
I n spite of the anticipated fiscal stimulus in the United States, the outlook for metals continues to be dominated by developments in the Chinese economy. Base metals such as iron ore, copper, aluminum and nickel — are the lifeblood of global industrial production and construction. Shaped by shifts in supply and demand, they are a valuable weather-vane of change in the world economy. While metals prices have been on the decline since 2011 reflecting the growth slowdown in emerging markets, they have rebounded more recently (see Chart 1).

The rally is on account of the anticipated possibility of a fiscal stimulus in the United States and Chinese authorities’ policies in support of credit growth including a fiscal stimulus in the United States and Chinese authorities’ policies in support of credit growth. Indeed, following the U.S. election by the then President-elect Trump a $1 trillion infrastructure plan (over 10 years) was announced. Notwithstanding the limited amount of details available about the stimulus plan in the U.S. there are several reasons to believe it will have a moderated impact on metals prices. First, the United States account for a small share of global metals consumption (see Chart 2). In 2016, the U.S. accounted for less than 8 percent of global refined copper demand and 3 percent of iron ore demand according to the World Bureau of Metal Statistics and the World Steel Association. In contrast, China accounted for about 50 percent of global copper demand and 60 percent of global iron ore demand. That said, China’s intended rebalancing, aimed at shifting away from investment and toward consumption, is likely to lead to a significant reduction in its demand in metals in the medium run. Second, the increase in infrastructure spending in the U.S. will likely be directed mostly toward brownfield as opposed to greenfield projects. In other words, U.S. infrastructure spending will likely be directed mostly toward maintaining and rehabilitating existing infrastructure as opposed to building new infrastructure projects as is the case of China. The service component involved in the infrastructure spending is likely to be much bigger per dollar spent in the U.S. than in China. The increase in metals demand and hence in prices from an infrastructure spending in the U.S. is thus typically much smaller than from a dollar equivalent infrastructure spending in China.

Lastly, the U.S. and China differ markedly in the amount of recycled metals used in their domestic consumption. That difference again suggests that the demand increase resulting from a potential U.S. increase in infrastructure will be limited while any increase in China infrastructure spending will have a strong impact on metals prices. In 2015, 9 percent of China’s steel production came from scrap compared to 65 percent in the U.S. according to the World Steel Association. That is however likely to change. China’s scrap ratio is expected to rise to around 20 percent by 2020, and 30-39 percent by 2030 according to BHP Billiton.

All in all, the demand for metals resulting from an increase in infrastructure spending in the U.S. is likely to be limited. In contrast, policy developments in China which focus not just on managing the demand side but also on the supply side would have dramatic effect on metals prices. Indeed, the Chinese authorities are actively curtailing excess capacity in the steel sector by reducing production of outdated factories, among other things to reduce pollution. Steel mills in mainland China have increased the volume of imported higher grade iron ore, which has helped increase iron ore prices. Markets suggest that metals prices will continue to stay “low for long”. Futures markets indeed point to most metal prices staying around the current level except for iron ore prices, which are expected to decline sharply. The downside risks for metal prices could result from waning of policies in support of credit growth in China or from an economic upset in China.
India: a commodity trading powerhouse

India offers an attractive long-term future for the commodity industry powered largely by its economic growth, a consumer class expected to more than triple, and a business friendly environment.

Amit Sreedharan, Director Client Services, Energy Resources, Infosys, Geneva
Vassant Sekaria, Manager Client Services, Energy and Resources, Infosys, London

ranked as the seventh most valued “nation brand” in the world, India recently became the sixth largest economy by nominal GDP and the third largest in PPP terms, at US$2.3 trillion and $8.6 trillion respectively. With a future growth rate projected by the World Bank at 7.6% for 2017, far ahead of other nations and global business and political headwinds, India is poised to lead the future of global change and is undergoing a transition in terms of investor perceptions of its market potential. India’s story in commodity trading started way back in 1875. Its futures market was vibrant until 1960, when it was closed due to war and political changes. The era of economic liberalisation since 2002 re-introduced commodity futures in India and the market has grown at a staggering pace since. In 2014-15 the Indian futures market had an aggregate turnover of approximately US$92 billion. The various exchange-based domestic commodity derivatives segment. With a population base around 1.3 billion, continuous migration to urban centres, per capita income, and climate change, there is immense diversity nurturing growth and creation of diverse commodities. India is one of the biggest consumers and producers of most commodities worldwide. The government’s move to transfer the supervision of the commodity derivatives market to SEBI and Exchange Board under the Securities Contract Regulation Act, a stronger law than the former framework, ensures better regulation and increased confidence. SEBI has shown greater inclination to listen to market players with the introduction of new commodities and options trading. Also, with the expected entry of new companies with India’s own markets such as mutual funds, insurance companies, and domestic and foreign banks; volumes are expected to increase and so will better price discovery. These changes will also bring out improved risk management opportunities for the trading houses and the investors. The government’s strategic initiatives around Make in India, Digital India, ENAM Agri platform, and MCX have led to an explosion in the commodity markets. Vedanta has committed $3 billion to 3 years. Trafigura has set up India’s first online refined metal platform Lyxos, while Bosch and GE have been expanding their manufacturing base and GM has just rolled out the first “Made in India” Mercedes E class. One of the biggest challenges faced by organisations in India is infrastructure whose improvement is a major focus area for the government. India plans to spend north of $59 billion to modernise its railways, airports and roads, in order to improve flows, reduce transportation costs and boost goods trade. There is an action plan to revolve 160 airports and airstrips, as well as modernising the 125 already in existence. More significantly, India plans to be a global leader in the country, allowing ventures with logistic companies which will provide enhanced connectivity to the South-east Asia and Southern China. There will also be 21,000 km of economic corridors and 14,000 km of feeder routes. India’s infrastructure build-up will also drive metals and mining demand in the coming years. While the Indian commodity industry has been growing due to suitable conditions across the board, there is a high probability that the rise in demand may outpace output growth given that supply response will be constrained by several resources, including financial and human ones. By leveraging the current and new investment in innovation, many commodity firms can reduce their cost per trade, reduce leakages in their supply chain, increase yield, productivity and profitability. They can also use machine learning, robotic process automation and artificial intelligence to perform some of the common tasks across support functions like human resources, finance, and procurement, thus enabling the up-skilling of existing personnel. Commodity firms have the chance to be the flag bearers that is sweeping India and harness the country’s existing technology foundation. With the right using harnessing, vast natural resource, participants, and technology in place, India is emerging from a sub-prime price taker to a dominant “price maker” of global commodities. The influence of India on the global commodity markets is both at the greatest it has ever been and the smallest it will ever be. And maybe, India can fire the next commodity super-cycle.

Africa: delivering energy to the people

Africa, a resource rich continent, suffers from a lack of energy. How can the trading community help?

Punit Bakhri
Head of Africa, Vitol

In many ways the countries in Africa are in an invidious position. Whilst Europe ages, Africa remains young – 60 percent of its population is under the age of 25. At the same time it faces significant development challenges, particularly in the energy sector. If Africa is to capitalise on its young and growing population, these are challenges which need to be addressed. The most important source of energy that Africa needs is power. Only 42% of the population has access to electricity, compared with 75% in the developing world. In sub-Saharan Africa it is 30% overall and only 14% in rural areas. Even those with electricity face interrupted supply and the African Development Bank reckons that the opportunity cost of an unreliable power supply is as much as 2% of GDP.

The solution to this is complex and multi-faceted, encompassing all points along the chain from generation, through distribution and delivery to the end consumer. Yet Africa has extensive natural resources which could be harnessed for its benefit. One example of such a project is our development, with ENI of the Sankofa Gye Nyame gas fields in Ghana. This project will power Ghana’s thermal power sector to 2016 and beyond. It has taken ten years from the awarding of the license to date, with first gas not anticipated until next year. In addition to producing the gas, the project requires an overhaul of Ghana’s infrastructure, from gas compressor plants to power stations and would simply not have been achieved without the support of the World Bank and IFC, as well as the Ghanaian authorities. We hope this project will serve as a “proof of concept” and that other countries with natural gas resources look to develop them for domestic use. Other countries have seen the benefit of natural gas will look to a range of power solutions; from renewables including hydro, solar, wind and geothermal to more traditional fuels such as coal. Many African power stations still burn fuel oil, current day). We anticipate that, over the next decade, transport driven demand will increase by 27% or 650,000 bpd. Today, Africa’s refineries operate at 65% of capacity with an output of 2.21 million bpd. This is much less than the current demand which is 1.1 million bpd. Without significant investment refinery output will not increase sufficiently, and the gap will have to be filled by imports. As has been highlighted, with varying degrees of accuracy, in the Swiss press, the specifications for fuels sold in Africa is equivalent to European specs from the 1990s. We are pleased to be part of the stakeholder groups which are working to improve local specifications, but the challenge should not be underestimated. To oversimplify the issue may be, but we cannot be complacent in our efforts to make a material difference to the problem. There is no doubt that Africa faces many challenges. At the same time, it also presents a unique opportunity to harness new technologies and to forge its own path of development, leapfrogging the challenges to a new and modern infrastructure.

From a trader’s perspective, the largest opportunity in Africa remains the transport sector. Many as those affected by ambient air pollution. Traders are ideally placed to facilitate the trade in LPG and also contribute to the underlying energy infrastructure through the investment in the handling and storage facilities. For example our investment in the Navgas terminal in Nigeria which, at 16,000 cubic meters, is among Africa’s largest LPG storage facilities.

Notwithstanding the above, from a trader’s perspective the largest opportunity in Africa remains the transport sector. We are pleased to be part of the stakeholder groups which are working to improve local specifications, but the challenge should not be underestimated. To oversimplify the issue may be, but we cannot be complacent in our efforts to make a material difference to the problem. There is no doubt that Africa faces many challenges. At the same time, it also presents a unique opportunity to harness new technologies and to forge its own path of development, leapfrogging the challenges to a new and modern infrastructure.

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Can Europe find its green energy in trees?

Wood pellets have emerged as a significant substitute fuel, in Europe but also increasingly in other regions.

The legend has it that Rothschild made a fortune by spotting von Blücher early at the battle of Waterloo and buying government bonds just before the news broke in London. But market traders, trying to position itself general nor a duty bound imperial French army are expected to come out the woods behind Brussels these days. However, wood pellets have emerged as a significant substitute fuel across the world and particularly in Europe. There is also a growing following in other regions, especially among insular communities. Its use by converted coal fired power stations or district heating networks has suddenly broken the forest gates that the pulp and paper industry once kept to themselves as “their” resource. Wood is coming back with a vengeance in the fuel market, all the more because basic refining and better furnaces deliver massive efficiency gains. This is not going unnoticed by policy makers who identified renewable heat as a pillar of support for industry (almost every production process has a heat treatment of some sort). Zero marginal cost prices may one day be the outcome of the renewable or nuclear power rollout, but in the meantime, on-demand energy generation remains the order of the day, and fuels do meet that demand. As for wood, it comes as a close second after waste on the merit curve. As forests in temperate climates need to be managed, diseases and insects from spreading, the amount of fibre that has to come out of the wood is reaching many millions of tonnes per year, while the current volume of wood pellets consumed in the world is still far off the 100 million tonne mark. The value chain linking the tree to the power plant is worth £25-£30/MWh LCV (or $275/tonne of heating oil equivalent). This eye catching spread with current energy market prices reads well, but the 68% to £20/ MWh LCV additional cost for heating plants is a major hurdle, currently keeping wood pellets out of the power market... for the time being.

Supply side elasticity

The good news is that the time to market of a new forest resource is relatively short. It takes the best part of 5 years, mostly spent on negotiation, planning and construction to deliver the first shipment of industrial grade wood pellets. Most of the “exploration” has been done in the form of long-standing negotiations with NGOs and governments on understanding “sustainability”. This needs translates into a never depleting reservoir! That story does not real well as well with the timber jack or with the oil man. The former does not have a ready market for his fuel when the few major off-takers are weened off their subsidy scheme... and there is little on the horizon. Consequently only medium-scale schemes are taking advantage of the relative oversupply which allows for the low-hanging fruits to be picked on the cheap. The British Renewable Heat Incentive, the European continental VAT spread and fossil fuels levies are leveraging this situation to the benefits of residential customers: “There is a new season to the next trading cycle is likely to underperform now that investors are looking at weather related risk arbitrage. Investment opportunities will abound around relative value trades and weather related risk arbitrage. Investment opportunities will also emerge, either with the few listed names (Envi- ra LLP, DRAX PLC...) or in private equity looking at port infrastructure or distributors consolidation.

Trading houses

The cost of reporting a losing position from one season to the next still represents about a quarter of the notional value of the trade. This paves the way for diversified trading houses to underwrite that risk - too heavy to bear by many distributors - or at least for those interested in better understanding that market, with a view to acting on that information to make private equity investment upstream or downstream. Vertical integration is the key to the game, which plays in favour of energy service companies with a captive downstream portfolio.Bio-sourcing of materials is also gaining in the market, this would increase the amount of wood available for energy or other traditional applications. As this trend favours agriculture and light industry resources overall and plesus public opinion, one may want to take a downstream position early on.

Towards a policy-driven green supercycle

The SDGs and climate policies are creating the conditions for a new take on trading

Commerce has always been the first factor of development. A trading company is first and foremost a link to the market. Adjusting to position itself where it has a competitive advantage, thereby creating economic growth, for a company, a region, a country. This requires international exposure, finance, transportability, energy, trade, and distribution channels.

New policy drivers creating new risks and opportunities

Risks and constraints are the way to opportunities. And while policy makers tend to be risk adverse and look to regulate these risks, from a trading perspective regulations are constraints, but equally risks. Despite seeming part of a far-fetched future not applicable to traders, international agreements and policies increasingly shape market outlooks.

A fragmented outlook: countries in multiple policy-gears

Each country will have its own targets to simultaneously address climate change and development goals. A reliance on “bottom-up” principles means that there is not one way single rule but each single country can decide on which aspect to prioritise. This should be perceived as a renewed opportunity to revive trading and differentiate one company from the other. Even spurred by politicians, economics remain the dominant force in opening up new markets and selling “developed” services and consumer goods. Moreover, there is a need to fill in the various gaps across the globe and foster exchanges of natural resources worldwide.

No, we are not cynical or not, in both cases trading companies must identify which specific risks they are willing to trigger to keep on playing with volatility and arbitrage.

The imperative of adapting business practices

One cannot price in a new market, in Africa, with its major growth potential and reserves of natural resources, without ever going there. Or be unwilling to deal under the local law or with a local bank while simultaneously asking a local partner to take all these risks and fill in a KYC (why require a utility bill when power is produced from a generator?). Capacities to address and reconsider risk appetite and management at the individual level, for specific countries, and a willingness to be part of a specific market will be key to reviving a commodity trading cycle. As the Paris treaty/SDGs call for local financial services enforcement, trading houses and financial institutions need to work on this to improve local practices, without systematically striking out the option to use local institutions. For example “International First Class banks” are not defined anywhere but the term used in all contracts. When published, lists of accepted banks prove tremendously concentrated.

Green funds ushering in a new era?

How would the commodity trading community react if a coastal and commodity rich country would impose to have only LNG bunker fuelled vessels calling at their port? One should not assume that stricter regulations will always come from the “developed side”. While economically risky, this might be vital to protect their communities and be linked to a major loan from a green fund, just as banks are seeking to develop their green portfolio. One major trading agency has already started to include sustainable elements in its rating. However, this was done hardly out of conviction, but because the risk was high that their index would underperform now that investors are looking at these very factors.

Trading houses have the knowledge and abilities to revive a trading cycle without waiting on regulators. It is about day-to-day business, the ability to identify risks and trigger constraints, it is about partnership: SDG number 17!

In this respect the next trading cycle is likely to be green!

(1) https://sustainabledevelopment.un.org/sdgs
(2) Country and counterparty risk and even the way of rating these risks
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Critical metals: how is the supply chain evolving?

LAURENT KOLLER
Director, Espoir SA

Critical metals represent about 70% of the critical raw materials identified by the EU Commission. These metals are of economic importance, but face a supply risk with a lack of substitution. According to the EU Commission, these materials are “linked to all industries across all supply chain stages.” Over the last two decades, these metals have gradually and almost insistently invaded our lives. This has taken place not only at the private and professional level, but also in relation to their essential roles in reducing greenhouse gas emissions. At the dawn of Industry 4.0, we are in the age of efficient materials that help improve on how we meet the needs of a modern world in search of miniaturisation, speed, mobility and sustainable energy.

The supply chain of critical metals has evolved due to technological advances and related innovations. In order to deliver the quality and purity required by manufacturers for integration in their processes, precise ore concentrate specifications have been developed. This has led to the rapid evolution of the automotive, telephone, internet and even energy. Miniaturisation in high speed computing represented a major technological advancement, making us more interconnected than ever and able to work from anywhere through a “cloud.” Our cars have drastically shed weight and are full of electronics and serve more than just transport. Autonomous cars will be the most safer than with us as the driver! Our bridges and buildings have also replaced cast iron and traditional steel components with lighter materials such as high-strength steel. Going forward, smart automation through robotics will also significantly impact the supply chain.

In this context, and in view of the still limited progress in substitution and recycling means, critical metals continue to be indispensable for the design of these new materials. Moreover, they can provide a decisive competitive advantage for end-user products.

The global supply chain will evolve around new players outside of China who will ensure a continuous and high-quality supply upstream. As there are no Tesla cars without lithium, graphite and cobalt, nor offshore wind turbines without neodymium, vertical integration for original equipment manufacturers (OEMs) can mitigate the risk of security of supply within the supply chain.

Before 2010, supply chains were not concerned with dependency. China fulfilled its primary role in a globalised world, increased its market share and became the essential supplier of critical metals. This came at the expense of preserving its environment and of respect for its mining laws (30% to 40% of Rare Earth Elements (REE) came from the black market). Western industrialised countries relied on this supplier and relocated production units to China.

In 2010, China sent a strong signal to the rest of the world with a sharp reduction in its rare earth export quotas. However, efforts to revitalise supply chains outside China were thwarted by slower economic growth and the effects of the debt crisis. Additionally, China maintained its low prices by subsidising its industry to promote the attractiveness and development of its products, whilst consolidating its own value chain.

Today, the sole producer outside China is Lynas Corp. In China, six major groups control REE production. All are Chinese state-owned companies, and five of them are listed. The REE industry consolidation effort has been supported by massive subsidies which are disappearing progressively. The Chinese REE industry faces profitability challenges, and the environmental cost will be integrated into the production cost. The successive five-year plans have always aimed to reinforce the Chinese REE domestic market and Chinese market share. However, the COP 21 and the “Made in China 2025” policy will have new impacts on supply and demand, and on reaching a sustainable price for rare earth raw materials.

The COP 21 Paris Agreement might be a catalyst on how we meet the needs of a modern world in search of miniaturisation, speed, mobility and sustainable energy. China fulfilled its primary role in a globalised world, increased its market share and became the essential supplier of critical metals.

The near future may see a pivotal point in the development of critical metals supply chains outside of China amid security of supply concerns and increased demand for consumer goods. This would better equip supply chains to keep up with global demand. However this will require collaborative efforts, including the support of OEMs, governments, and possible new trade alliances.

1. European Commission website
2. (1) European face aux défis de la substitution des métaux stratégiques
3. Supply Chain Evolution beyond the paradox, Feb 2017
4. (4) Metaux critiques et Industrie 4.0 Dec 2016
5. (5) S5: Made in China 2025

The unstoppable rise of pulses

ROBIN PACKE
Managing Director, Alliance Grain Traders (Switzerland) SA

Pulses have been part of human diet from the beginning of civilization. Fossilised chickpeas and split lentils, preserved by Mount Vesuvius ashes some 2000 years ago, can still be seen at Pompeii today.

Although the global production and consumption of pulses has only grown moderately over time, the world market has deeply changed. The total production of pulses has increased by just around 69% over the last half century, from 40.35 million tonnes to 68.2 million tonnes, but global trade increased almost six fold over the past three decades, from 1.7 million tonnes in 1981 to 12.4 million in 2011. With the value of global exports increasing more than 11 times over the same period and the unit value of exports almost four times from $133.8 in 1961 to $654.6 in 2011 (an annual average increase of 7.6%), demand for pulses is running ahead of supply and prices traded in the international markets are rising swiftly.

Until the 1960s the world market remained balkanised, with a multitude of small players. Drastic changes started in the 1990s, due to several factors including growing demand in line with demographic growth, the liberalisation of Indian pulses import policies and the imposition of export curbs, disintermediation through the internet and globalisation. Traditional exporters such as Turkey turned to importers. New origins took the lead in production and export. Canada emerged as the largest world exporter followed by the US, Myanmar and Australia. Still, global trading houses would not invest in a sector then considered as a small niche market. Many small industrial processors had the know-how but not the finance or the international network to go global. Changes accelerated from 2001, through vertical integration from the fields down to the shelves, largely under the impulse of a handful of players who for the first time, managed to consolidate and scale up the supply chain, putting together origins, industrial know how and assets, finance and destinations, one of them capturing today a 30% market share.

Demand is destined to grow with anticipated population growth and increasing incomes in developing economies, not only in India but also across the MENA region, Southeast Asia and Western and South Africa. With 1.3 billion people (of which 80% vegetarian), India is the biggest consumer and its population increases at the rate of 30 million people p.a. But consumption picks up all over the world, due to agricultural, ecological and health concerns, in a general trend to substitute animal with vegetable proteins. Pulses currently constitute around 11% of consumed protein worldwide. For farmers, pulses not only represent an opportunity to increase their revenues with valuable crops, but to save on fertilisers through crop rotation as pulses regenerate the soil naturally with nitrogen.

The next decades looks bright for the pulse industry: acreage and exchanges will keep increasing. While containers remain the main portion of the traffic, some raw pulses are transported today in bulk vessels of up to 15000 MT. Tomorrow’s challenges will be on quality, which can vary significantly depending on weather, and in logistics in order to cope with growing volumes and optimise the cost to end users.

1. (1) FAO
2. (2) India Pulses and Grains Association

• Hull and P&I
• War Risks / YC P&I
• Political & War Risks
• Charterers’ Liability / FDD
• Marine Cargo
• Storage
• Cargo Owners’ Liability / FDD
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Marcus Cooper

“A new super cycle is inevitable”

Russia is the second largest world exporter of crude and oil products with Rosneft a major market stakeholder. The country has diversified its exports, in particular towards the East and China. Rosneft recently extended its agreement with CNPC on oil supplies to China and has signed an agreement setting out the framework of the Far-Eastern Petrochemical Company (FEPCO) with ChemChina. Russia is also turning towards India and Rosneft has invested in the Essar oil project in India that includes the country’s second private refinery at Vadinar (Gujarat). Although Russia has increased production last year, it has agreed to limit output alongside OPEC. We met Marcus Cooper, General Director of Rosneft Trading, on the outlook for oil, infrastructure build-up, price trends, capital expenditure, joint ventures and the role of the Swiss hub.

Rosneft recently extended its agreement with CNPC on oil supplies to China. What is your view on the Chinese market?

Chinese oil consumption per capita remains significantly lower than in other parts of the world, 4 times lower than the US, 4.5 times lower than the UK. Despite this, Russia has sold oil to China because it is economically sensible. In the long run, however, the Chinese will need to import oil from other sources to meet their demand growth for some time to come. The Chinese economy continues to grow despite technological advances in the efficiency of how resources are consumed. In terms of diversification, China and Russia share a border of 4,200 kilometers, 12 times the length of Switzerland, presenting a logical geographic opportunity for Russian exports overland via rail and pipeline into China.

Rosneft has also invested in the Essar oil project in India. Do you believe that India will be one of the major players of tomorrow?

The Indian population is now similar in size to China’s, together making up 36% of the world’s population despite combined oil demand in both countries being 5-6 times lower than in the developed world. As these economies further integrate into the world economy demand for resources will increase rapidly – Indian oil demand grew 500kb/d year on year last year. India and China are already major players and will be the major centres for demand growth for some time to come.

Russian production has significantly increased last year. Do you believe that this trend will last?

Russia and Rosneft have one of the lowest cost centres of production in the world meaning that they are well poised to be able to address the considerable challenges of the future as demand continues to grow over time, even after taking into account agreements to re-balance markets over the short term.

Do you think that a new supercycle with high demand driving high prices as well as investments is likely over the next few years?

If everyone in the world consumed oil at the rate being consumed in the developed world oil production would need to increase 3-4 times. Despite this context investments in exploration capexes have fallen by 40% over the last two years in response to the recent downturn in oil prices suggesting that a rebound in price and the beginning of a new super cycle is inevitable over the next few years.

With substantial expenditure planned over the next 15 years, Russia’s infrastructure development programme is ambitious. Are the investment levels realistic?

Russia’s infrastructure development plans are carefully thought through to calibrate with the demands of a growing and ever more affluent world population. When seen in context these investment levels are realistic and necessary to ensure security of supply and reliable price stability in the commodities markets.

Infrastructure programmes are one of the main buzz throughout the world. How do you believe that the major Chinese, South East Asian and Indian programmes will impact the demand for commodities?

We consider that Chinese, South East Asian and Indian commodity demand will remain vibrant over the coming years putting upwards pressure on prices and volatility in the event that supply is not able to adequately satisfy demand.

As a major oil producer and trader, are there any concerns that technological innovation could significantly displace demand for oil?

Based on the massive underlying potential for oil demand growth globally over time a variety of technologies will inevitably enter into the market place at the margin to help satisfy energy demand as prices trend higher over time.

Rosneft is working with Chinese entities but also with European companies (Rosneft sold BP a 20% of the Taas-Yuryakh Project). How important are JV’s for Russian energy companies in the future?

Joint ventures are very important for Russian energy companies as a means towards addressing the considerable energy challenges of the future via sharing of skills, technologies and best practices for mutual benefit.

Rosneft Trading was established in Geneva in 2011. How do you value your partnership with Swiss trading companies?

Geneva and Zug are key trading hubs in the global energy markets alongside London, Houston, Dubai and Singapore. Being physically located in one of the major hubs enables Rosneft to interact more readily in the global market place, including with co-located Swiss based trading companies.

How important is it for a State-owned enterprise to own a separate trading company?

Rosneft has been substantially expanding its international activities over the recent past, including in India, Indonesia, Egypt, Iran, Ethiopia and Libya as well as via long term supply contracts into CNPC in China. An internationally based trading company is key to optimising this expansion of the asset base, particularly in the event that resources are more efficiently sourced from the market vs from Russia.

What is your view of Switzerland as a trading hub as we enter a new era of global dynamics with Brexit, the election of Trump and the rise of populism and protectionism?

Switzerland has always been a beacon of stability in an ever changing world. Markets perform most efficiently when the rules of the game are clear and understood by all participants; Switzerland’s stability lends itself as an anchor to Switzerland’s future as a key trading hub.

Interview: Thomas Esdaile-Bouquet, STSA
SUSTAINABILITY & THE SWISS HUB

With success comes accountability. STSA is working on developing guidance in a multiple stakeholders process.

Rapid economic change has presented our industry with a multitude of opportunities to conduct activities in a range of jurisdictions. However, with success comes accountability. More and more, our industry with its complex value chain faces change in competitive dialogue on practical ways forward.

Ethical Challenges

Ethical questions have and will continue to be raised to the complex global business environment which drives companies to make critical choices in order to fulfill the expectations of their shareholders and stakeholders. Shareholder interests, however, may differ widely from those of stakeholders. But once companies enter markets with different legal structures and ethical frameworks, they can no longer ignore the interests of their stakeholders.

All companies, not just trading and shipping companies, need to be a part of the corporate commitment to develop some form of guidance with the Institute for Human Rights and Business. It is clear that we as an industry have a vital part to play in continuing to undertake due diligence and risk assessments throughout our entire value chains, and communicating our efforts internally and externally. The commodity trading sector in Switzerland is at the forefront in designing sector-specific guidelines based on the UNGPs as part of a multistakeholder process, aided by the Swiss Federal Department of Foreign Affairs which is committed to assisting with their implementation.

In recent months these issues of corporate responsibility have played out in the media, centring on the supply of high sulphur fuels to Africa. Trading companies play a crucial role in supplying markets with the desired products while mitigating price distortions. However, wide variations of fuel specifications across the globe create problems, together with outdated national legislations on fuel standards in a number of developing countries, has led to concerns over public health implications. With countries in some cases lagging decades behind in terms of regulations and traders responding to predefined fuel specifications through tenders, it is therefore governments – not just NGOs and corporations – that have a decisive role to play.

Similar concerns regarding SOx emissions exist in the shipping industry and the introduction of global IMO sulphur content limits are leading to a rapid transition towards cleaner fuels. Challenges abound however, as the lower costs of environmental externalities come at a high cost for shippers and traders as low-sulphur marine fuels cost 60-70% more. These costs will ultimately have to be passed on. Financial regulations are also being tightened. In Switzerland, the Financial Markets Infrastructure Act (Finmira) entered into effect on 1 January 2016, imposing a number of reporting obligations on all open derivative products itself in the public eye. Its future depends on how it meets these concerns to ensure a more sustainable and transparent business environment. To help facilitate this, STSA and its members have been a part of a Code of Conduct for complex automation in Switzerland to increase corporate responsibility come just as new frameworks tighten in a number of areas, leading to a complete overhaul of standards across the industry, as seen with the fuel products market.

A growing number of international initiatives have shaped the development of soft law, with a particular focus on corporate responsibility and sustainability including the OECD Guidelines for Multinational Enterprises. Notably, the UN Guiding Principles on Business and Human Rights (UNguids) have been a global game-changer in the development of regulation and soft law. In Switzerland, the Responsible Business Initiative is the top political priority in a number of countries which they must solve in accordance with the ethical business standards defined by international actors. These include corruption, the respect for human rights, and environmental issues.

Growing international pressure

In the last decades, globalization has brought increased public and political attention upon the role of international companies. This has prompted the launch of various initiatives across the international spectrum. 40 years ago the OECD formulated guidelines for international companies. Since then, the UN Global Compact initiative was launched which, in 2011, approved the Ruggie Principles (2011) and the 2030 Agenda for Sustainable Development Goals (2015). Persistent failures to meet relevant standards undermine efforts to promote growth in developing and emerging countries given the far-reaching impacts of the corporate behaviour of international companies. For example, child labour undermines the development of decent education systems. Tax avoidance schemes deprive countries of the funds necessary to develop their infrastructure. Corruption cheats countries out of a fair price for their goods. These issues have become of global concern. This has led to growing pressure from international and national agencies, as well as non-governmental organisations (NGOs) to increase the regulatory burden for businesses.

Nowadays, companies must align their strategies and operations in order to comply with international ethical standards. In the face of current economic and environmental problems worldwide, companies can no longer ignore the externalities that create costs for the whole society. They must endure a new role.

Defining business strategies

The role of commodity trading companies in Switzerland has put them firmly and regularly into the headlines. Despite recent commitments made by these companies, civil society and political actors remain suspicious. As noted by the Swiss Federal Council, the most imminent risk for our country is the reputation attributed to the commodity companies directly involved in the mining and processing of raw materials. This represents a growing foreign policy challenge.

These potential dangers must be anticipated by adapting working practices where necessary in order to avoid, on the one hand, further criticism and on the other, a stream of regulations in the years ahead. Nowadays, international companies are required to play an active role in promoting development. Companies who recognise that they can play an important role in societal and environmental terms extra to work together with local or national governments and NGOs. In doing so, they redefine their business strategy and combine the sustainability of the business with good for society, we are saying the opposite, what is good for society is good for business.” It is the current role to redefine their players change on this new role as it they who have the potential to make a positive and long lasting difference.

NGOs challenging companies and governments

In the last decades, NGOs have become high-profile actors in the form of international development. Despite possessing few formal powers, they have many accomplishments to their credit. Their challenge companies to be sustainability-minded on a global level. The attention they receive from the media and public requires business leaders to listen and engage in dialogue and ultimately search for new forms of collaboration with both NGOs and political actors.

The obstacles of doing business in developing and emerging countries are known. Business leaders must often overcome local regulatory and institutional barriers that inhibit the development of a sustainable business in those countries. But they cannot attribute these practices to local “culture”. They must do everything they can to eradicate them, with or without the help of local politicians. The alternative is not only continuing misery in the countries involved, but also seeing millions of people continuing to look for a better place to live. It is a challenge, but management must address these critical ethical business issues.

Sustainability as a strategic priority

Some companies have subscribed to the guidelines of the UN Global Compact, the EITI (Extractive Industries Transparency Initiative) or the Ruggie Principles. Some are members of the Plenary of the Voluntary Principles on Security and Human Rights Initiative, which promotes responsible practices in the extractive sector. Some have adopted the concept of Creating Shared Value (CSV) and developed strategic initiatives in this direction. Some have adopted the concept of Creating Shared Value (CSV) and developed strategic initiatives in this direction. Some have adopted the concept of Creating Shared Value (CSV) and developed strategic initiatives in this direction.

The integration of sustainability throughout their business must be strategic for all international companies in this century. This includes publishing sustainability reports in order to respect the political requirements for greater transparency. Accepting responsibility in the prevention of human rights violations and environmental impacts is an important role in societal and environmental impact of their activities, including by debt default, poor performance and reporting on core aspects.

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BUSINESS LEADERS CAN NO LONGER ATTRIBUTE MALPRACTICES TO LOCAL “CULTURE”.

CHALLENGES IN CONDUCTING AN ETHICAL BUSINESS

The integration of sustainability must be a strategic priority for all international companies. This represents a growing foreign policy challenge. These potential dangers must be anticipated by adapting working practices where necessary in order to avoid, on the one hand, further criticism and on the other, a stream of regulations in the years ahead.
Cleaner fuels for Africa

Rox de Jong
Head of the Transport Unit
UN Environment

Reducing global emissions from vehicles is essential to reduce urban air pollution and to meet global climate change targets. Introducing cleaner fuels and vehicles is the key to achieving this. The oil industry, including oil traders, plays an important role in this. Every year, about 7 million people die prematurely due to air pollution, with outdoor air pollution accounting for around half of them. Air pollution is partly caused, in the transportation sector and it is a major contributor to the overall global emissions. The challenge of dirty fuels and vehicles in developing regions remains real. In Africa, only 7 of the 54 countries have achieved low sulphur fuels. In fact, not one of the 15 West African countries has achieved low sulphur fuels. In Africa, only 7 of the 54 countries have achieved low sulphur fuels. In fact, not one of the 15 West African countries has achieved low sulphur fuels. In 2016, 7 of the 54 countries have achieved low sulphur fuels. In fact, not one of the 15 West African countries has achieved low sulphur fuels.

Low sulphur fuels are mixed with low-spec components before shipment to African countries that have lax and outdated standards. African citizens have been bearing the brunt of this problem. Particulate matter pollution in Africa is a major issue and its impact on human health and the environment is significant. In 2016, 7 of the 54 countries have achieved low sulphur fuels.

Exporting and importing countries, together with the UN, are working together to stop the practice of dumping high sulphur fuels in Africa. Last year, the Governments of The Netherlands and Nigeria, together with UN Environment, organised a meeting in The Hague with all stakeholders including governments, the oil industry, civil society, media and the UN to identify ways to stop the export of low spec fuels to Africa. Importing West African countries have decided to introduce new harmonised low sulphur standards. Ghana has announced that it will implement new standards which will come into effect before mid-2017. The countries together with UN Environment are also reviewing if the trade in polluted petroleum products is illegal under the Basel and Bamako Conventions that regulate the trade in hazardous substances. The Bamako Convention states that export of substances that are not allowed in exporting countries for health and environment reasons should not be exported to African countries. A recent review by an environmental law think tank concluded that the trade in high sulphur fuels is illegal.

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For more information: www.sttaswiss.ch
Switzerland is one of the world’s most important hubs in the global trade of commodities. The Swiss commodity sector is under continuous scrutiny for human rights as calls for social responsibility question its governance. Ethics and human rights are important to Switzerland, which has adopted the United Nations Guiding Principles on Business and Human Rights as set by John Ruggie (ex-UN Special Representative for Business and Human Rights) and endorsed by the UN Human Rights Council in 2011 in Geneva. Michael Posner, Co-Director for the Center of Business and Human Rights at New York University Stern School of Business, was recently the guest of the Swiss Research Institute on Commodities.

How well does Switzerland fare in terms of human rights?

The Swiss government is ahead of many other European countries, in terms of advancing human rights principles. I would even say it is a pioneer, with clear leadership in this matter. To cite one example, following the killing of 21 people in Iraq by the private security contractor, Blackwater, the Swiss government has led a multi-stakeholder initiative to develop a code of conduct for security companies which is evolving into a global standard. Over a hundred countries have joined The International Code of Conduct for Private Security Providers’ Association (ICoCA), a multi-stakeholder initiative established as a Swiss non-profit association, largely funded by the Swiss government.

What is the role of companies in ensuring that human rights are respected?

The concept of human rights is quite recent and dates back to the first years of the United Nations and its commission on Human Rights which was created in 1946. The Universal Declaration of Human Rights was adopted by the United Nations General Assembly at the end of 1948 largely in response to the Holocaust and the experience of the Second World War. Had it existed before, countries would have had grounds to intervene against the Nazis in Poland. The Declaration grants civil and political rights, free press, fair trial, and economic rights for example relating to health work and education. It was initially the business of States to ensure these rights were respected, but many States have not lived up to these expectations. There is a growing public awareness of this failure which has increased with social media.

So the rising trend is to expect global companies, which have grown larger and more powerful, to protect populations where States fail to do so. On the other hand, there is increasing distrust for the global trade system, with a feeling that it is not serving the public interest, that there is a growing gap between rich and poor. Some are advocating restrictions on trade as a way to address this gap. The expectations of companies to correct the failures of States are high, sometimes unreasonably so. What can companies do? This is where the UN came in by setting up a broad framework for a discussion of these issues with the creation of the Global Compact Network and later developing the UN Guiding Principles on Business and Human Rights (Ruggie principles). These are only first steps because States are not meeting their duties. While it is now clear that companies have some role to play, companies’ responsibilities are not clearly set out.

What does it mean for the industry to take on such responsibility?

Each industry faces different challenges. Human rights challenges are different for coffee trading, energy, textile, fishing or security. Therefore, industry-specific standards and metrics through some form of a multistakeholder process. There are issues related to security, land or labour for which standards exist but need to be applied at the industry level. The challenge is to think about these questions in practical ways to actually measure performance. There also is a need for metrics to help companies, but also investors and consumers evaluate company performance.

What type of metrics?

Whether it is in measuring profitability, products or services quality, or business priorities most aspects of company performance are subject to metrics. So should human rights. Measuring all laws for reputational risk to be used as leverage for better behaviour. Sustainability costs are real and require long-term investments. Unfortunately, most companies cannot afford them because of the short-term pressures they face from investors. Only the stronger ones can.

To take one example, Unilever scrapped quarterly earnings guidance for investors to avoid compromising long-term missions such as improving working conditions and the environment. This also applies to Apple. Today there are some strong measures around companies’ governance and some metrics on companies’ environmental footprint but social metrics are very weak and assessments of performance practically non-existent. However, investors are beginning to recognize that companies with strong ESG performance make sustainable long-term investments.

What would it require to build and implement such metrics?

It would require setting concrete industry standards, for example relating to labour practices in coffee, or for the security industry. The next step is to develop metrics based on these broader standards. This process starts by examining the central business model for companies in a particular industry that is how they make money. Usually the application of these metrics will reveal the need for money to be invested to correct problems. For this to be possible more investors will need to be supportive and move from short-term to longer-term investment horizons and thinking. The results could be measured in terms of fewer hours worked, better pay, avoidance of forced or child labour or fewer incidents of discrimination or harassment. Implementing some of these standards and remedying gaps often involve extra costs and we need to acknowledge that and find ways to allocate those costs fairly. One reason I am hopeful about this is that we can already observe a generational change that will make these measures feasible. You are seeing increasingly uncomfortable with using products or services which are improperly made. These will be the next generation of investors and consumers, so there are attitudes really matter. In addition there are more NGOs everywhere working on these issues and more enlightened industry leaders are tackling them in ways they would not have 25 years ago.

Isn’t it easier for large companies than for SMEs?

It is much harder for SMEs as they are younger and have smaller margins. This is why we are looking at the largest global companies first because they have the means to move forward. The solutions for SMEs may need to be different and we do not have an answer in the short term. On the other hand, SMEs often work on a personal relationship basis and know their partners, which allow them to have better control over their environment.

Commodity traders change suppliers often so it is hard for them to influence their partners on a long-term basis.

Long-term partnerships allow trust and reliability to be built so they are a better way forward. Traders may get a better deal from the next guy, but he may also bring greater risks. Faster and cheaper is not always the most efficient solution.

Swiss trading houses have been criticised for selling fuel below European standards to African countries. Although these fuels were way within the standards set by the countries themselves, should they do more?

Trading houses should ask themselves whether there are global standards that need to be set. Companies have an obligation to take on such challenges as an industry. Following local laws is not likely to be sufficient especially if local laws below international standards. We need to recognize differences, but we also need companies to take a more global view. Simply implementing the International Code of Conduct for Private Security Service Providers’ Association (ICoC)
When commodities such as iron ore, grain and other goods are moved around the world, they are largely carried by ships. So it is in the interests of everyone to ensure that shipping continues to become safer, greener and cleaner, as well as more efficient.

The International Maritime Organisation (IMO) is the United Nations agency charged with regulating international shipping. For nearly 70 years, IMO has developed and adopted stringent global shipping standards. This has been achieved through collaboration between the IMO’s 172 Member States (and their Associate Members), with welcome input from interested international non-governmental and intergovernmental organisations. Of critical importance is the concept of global regulation for shipping. It is crucial for regulations to apply worldwide and to all global shipping. Regulations do not allow anyone to gain an advantage – either by cutting corners or by imposing unilateral requirements. And they ensure that ships have to comply with the same rules and technical standards anywhere in the world they operate and regardless of how ships fly across the seas. The countries that came together to create IMO’s conventions in 1948 to draft the IMO Convention recognised these principles and embodied them in its first two articles. As IMO prepares to celebrate the 70th anniversary in 2018, those principles remain just as important today.

And IMO has been successful in living up to those principles to date. Against a background of more trade and more ships – responding to the ever-increasing desire for consumer goods and the basic need for raw materials and commodities that support economic growth and sustainable development – margins rules have been developed and regulations to prevent pollution from ships have been strengthened. Shipping has never been safer, cleaner or more efficient. IMO’s work continues. January 2017 saw the entry into force of a mandatory code for ships using gas or other low-flashpoint fuels, as well as the Polar Code, which introduces additional safety and pollution prevention rules for ships in Arctic and Antarctic waters.

Further key measures are set to be implemented soon. First, IMO has set 1 January 2020 for the 0.50 mass by mass (m/m) sulphur limit for fuel oil used by ships. This represents a reduction by a factor of 80% m/m limit and will impact significantly on ships operating outside ECAs, but in turn will bring significant health and environmental benefits. Greenhouse gas emissions from ships also remain under the spotlight. IMO Member States, meeting in the MEPC in October 2016, collectively and by consensus agreed a “roadmap” for developing a comprehensive strategy on the reduction of GHG emissions from shipping. The roadmap focuses on setting a 40% reduction target by linking physical markets behaviour to derivatives markets as optimisation strategies become clearer and there is only so much that a regulator can do in terms of anti-avoidance rules before losing the argument, either legally or practically.

The main grievance with the scope of these new regulations is that the commodity derivatives markets exist to serve the needs of the physicals market, but that the impact of new regulations has been to impose rules on derivatives markets that negatively impact the efficiency of the physicals market. This is particularly concerning as there is no evidence that commodity derivatives pose a systemic risk to the global financial system. The clearest example of this mission creep is the EU’s market abuse regime where derivatives regulation steps into the physical commodity market by linking physical markets behaviour to deriv¬atives markets behaviour in a way that prioritises control over efficiency, both over the very real needs of the physical commodity market – a case of the tail wagging the dog. Therefore, the current commodity regulations are largely limited to the core aspects of the G20 commitments.

The G20 commitments that directly affect commodity derivatives are the clearing requirement, pre- and post-trade transparency and regimes for risk mitigation techniques, including margining. The Dodd-Frank, EMIR and Finfra’s regulatory regimes are the key ones for Swiss commodity companies. In addition, the EU wants to update the Markets in Financial Instruments Directive and remove the transitional commodity exemption that was reluctantly granted back in 2004. On MiFID II, the G20 raised issues about the scope and purpose of regulation, the impact of regulation on commodities, and the political dimension of regulation. In particular, at what level of derivatives activity should a commodity company be treated as a financial services company, and whether there is specification in futures markets that needs to be dam¬pened and if position limits could or should be used to do this? Both apply to key new rules being settled in a way that should not adversely impact commodity companies, but it has been a long time coming.

An unresolved issue is whether non-EU derivatives activity can or should be used to determine market-making when doing calculations under RTS 20. In principle, it makes sense for regulators to do this, but in practice, where are they going to get accurate accurate actually is not easy for participants going to know when they are at risk of exceeding a threshold? Similarly, there are practi¬cally difficulties in implementing the EU’s anti-avoidance rules. We have seen the consequences of a pro¬cess, the second step being the analysis of the data collected, leading to an informed decision on whether further measures are needed. If so, policy options would then be considered. The aim is to deliver realistic and pragmatic solutions which work from a technical and a political perspective; and are acceptable to all parties. The discussions on GHG emissions from ships will take place in a dedicated working group, which will meeting before, and report to, the MEPC. Meanwhile, IMO is supporting capacity-building work to create global, regional and national partnerships to address maritime energy efficiency and for countries to bring this issue into the main¬stream within their own development policies, programmes and dialogues.

Another key challenge for shipping is the current flood of financial services regulations, including on clearing and margining requirements, capital adequacy and market abuse. To add to this, the focus on anti-bribery and cor¬ruption, business and human rights, and trade sanctions and this regulatory package has posed a serious challenge. As IMO prepare to celebrate their 70th anniversary in 2018, those principles remain just as important today.

THE NEW SWISS REGULATIONS ARE LARGELY LIMITED TO THE CORE ASPECTS OF THE G20 COMMITMENTS.
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The unintended products of innovation

Innovation and technology will make commodity markets more efficient, transparent and safe.

We are on the cusp of a new era in trading, driven by innovation.

Adapting to changes is part of the commodity traders’ DNA. However, the industry is facing its next major challenge in technological advances, which are set to fundamentally disrupt the way commodities are traded.

The amount of information available on commodity trading floors has reached levels that have never been seen before. So much so, in fact, that arbitrage opportunities are becoming increasingly rare and margins are melting away like snow in the sun. Extracting the predictive power from such a vast amount of data has become a key element in remaining competitive and finding alternative trading paths. One typical example includes the analysis of market prices combined with weather and shipping data or even satellite imagery to identify new trading patterns or optimised flows. Advanced predictive analytic techniques, such as artificial intelligence and machine learning, applied to unstructured data will provide the companies that use them with a clear competitive advantage in the not too distant future. While it is highly unlikely that robots will replace traders, the latter are already benefiting from new analytical tools. We expect that it will soon become part and parcel for traders to be supported by dedicated data scientists, who will turn data into actionable insights.

New technologies also make it possible for commodity trading firms to implement streamlined and more cost-efficient processes. For instance, the whole trade finance documentation chain can be made more efficient by replacing manual steps with automated robotics processes. Cost savings are even more remarkable when we take a look at blockchain technology: trading companies can virtually eliminate paperwork expense by using distributed ledger technologies. Indeed, some major companies have already taken stock of this strategic challenge. The same applies to trade reconciliation and other finance processes that have already taken stock of this strategic challenge. The same applies to trade reconciliation and other finance processes that improve HSE, as well as enhancing reliability and optimising operations. So long as the cybersecurity risks are appropriately managed, it will benefit both the industry and stakeholders.

In short, we are on the cusp of a new era in trading, driven by innovation. It is well known that today we can do business faster and in more locations. But what we have to realise is that technology is set to bring new levels of transparency. As with all technologies, the associated risks have to be carefully managed. Nonetheless, there is no holding back this change and we should all prepare for the new future.

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How can a multi-stakeholder platform like the SRIC promote research?

The Swiss Research Institute for Commodities (SRIC) was created in December 2014 to promote research in the complex field of commodity trading and its related environment. It involves stakeholders from the professional sector, governmental agencies, civil society and academic institutions.

Commodity trading companies must invariably generate revenues, both for their survival and to contribute to the distribution of commodities around the world. They are hence faced with a continuous optimisation problem with a set of constraints that evolve with time. These constraints include technical aspects bound to the type of commodities (energy, agriculture, and natural resources), to business practice (regulations, financial markets) as well as civil and environmental interests.

Research is a powerful means to create knowledge. Proper knowledge is essential to understand the constraints that one has to consider in decision-making processes. The SRIC aims to promote research that will ultimately improve commodity trading practices. The SRIC is not a new type of platform. However, it is innovative in that it offers the opportunity to bring important stakeholders around the same table, with the clear motivation to understand each other's positions and collect comprehensive and transversal knowledge. The University of Zurich, for example, has created a Centre for Child Wellbeing and Development with internationally renowned Professor of Economics Ernst Fehr. It is co-financed by the Excellence Foundation, with notable partners such as UNICEF and the Development and Cooperation Department of the Swiss Government.

A platform like the SRIC enables the transfer of knowledge in a suitable manner so that it can be understood as widely as possible. The organisation of the Geneva Trading Forum is a notable example of such knowledge transfer. Taking advantage of its geographical position in Switzerland, where most of the commodity trading companies are established, the SRIC can also serve as the reference institution for the production of state of the art reports on the commodity trading sector.

Research, or the proper creation and transfer of knowledge, obeys a sustainable cycle. In short, the most complex yet fundamental questions are embeded in long-term projects, and nourish the short-term needs for knowledge. For example, the question of “How can innovation, business practices and regulations enable commodities supply to structuralize?”, the question of “How can we understand the impacts of climate change on production and demand of agricultural commodities and how can we mitigate these impacts?”, and “Which are the main factors that contribute to reaching a dynamic and sustainable equilibrium in a specific market?”. In addition, the question of proper knowledge is essential, at least in order to avoid the global unproductive “war of statistics”. Academic institutions such as the University of Geneva, and more specifically the Geneva School of Economics and Management, are at the core of independent knowledge building through research and actively participate in its transfer. The Master in Commodity Trading, created in 2008, is currently undergoing a reform that will allow its students to be exposed to broader academic questions and methodologies so that they can provide sustainable added value to businesses and institutions.

Supervised by professors, their Master theses can be either theory oriented or more focused on the trading market, and are used as a basis for executive papers that are distributed through the SRIC platform to interested stakeholders.

Additionally, long-term research projects are also required, involving experienced researchers (professors) connected to an interdisciplinary academic community, possibly together with Ph.D students. Supporting and helping to develop long-term research projects constitutes the next main objective to be reached by the SRIC foundation.

Finally, there is no free lunch. Research, knowledge creation and transfer, all require means. These means are not just financial, but also in-kind, such as information sharing, data collection, and available human resources that can freely contribute to the research network. It is now time to invest in serious assets so that we can enter a dynamic and virtuous knowledge creation and sharing cycle for highly valuable long-term returns for all stakeholders.

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Will your pension plan leave you with a sweet or fishy taste?

Don’t lick your lips only to end up staring at an empty bone.

Comparing your pension plan with a dish is perhaps a little far-fetched but the truth remains that we still do not know what ingredients the Swiss federal chambers will use to come up with their final “prévoyance 2020” recipe.

Negative long-term bond rates are unlikely to provide meaty opportunities for an ageing population and voracious centenarians. Unfortunately while we can expect a nice wrapping with a mouthwatering conversion factor, chances are the project cooked up by decision makers will not be quite as palatable when its long-term end date turns out to have been overstated.

It is hard to find the right recipe based on the Swiss 3-pillar system but by incorporating a few extra ingredients such as diversification it can become a rather sweet offering.

Companies with two or more plans have to offer an individual pension plan. Above a certain income level, pension plans called “Bel étage” allow you to tailor your investment profile while benefiting from the fiscal advantages linked to the 2nd pillar. Given the amounts that can contribute to savings and buybacks, this recipe is an appetising option to generate higher yields and long term income streams.

Make sure to check the Bel étage menu

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– Philippe Schiavon, PFS Conseils SA

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Customised, extra-mandatory Pension Plans made available exclusively to managerial employees of STSA member companies.

Smart Pension+ offers:

- A customised, flexible Pension Plan named “Bel Étage”
- Accrued fiscal optimisation of managed assets (insurance redemption)
- Increased capacity to build up employers contribution reserves, entirely tax deductible
- Free choice of investment strategies
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MARCO DUNAND | MERCURIA ENERGY TRADING

“All our jobs are influenced by technology”

The pace of innovation may have seemed slower in physical markets than in financial markets. Yet the energy markets have been deeply affected by innovation: from the introduction of tracking as a drilling technique to the spread of wind and solar energy and distributed energy. Faced with the necessity of dealing with massive amounts of data – ranging from vessel tracking to climate prediction –, trading houses are introducing new analytical tools. Technology has also reached the core of traders’ daily business. Earlier this year when shipping an oil cargo to China, Mercuria’s induced blockchain to energy trade. We met Marco Dunand, co-founder with Daniel Jaeggi of Mercuria Energy Trading.

Uncertainty is shaping the economy. How difficult is it to read the current context? The political context delivers more uncertainty and risk than usual. We are seeing structural changes that will greatly influence the energy markets. The latest OPEC agreement with countries outside the cartel has brought about a situation closer to Russia in a most unusual move, an unexpected reconciliation between the two countries’ interests. President Trump’s threat to penalise imports would have significant implications for the crude industry. His sharp criticism of President Obama’s nuclear deal and the possibility of new sanctions against Iran would also have a major impact on oil flows. So would his push for better US-Russia ties free US investment in Russian projects? The future is extremely difficult to predict. Uncertainty is at its highest level in years and as you know, uncertainty boosts volatility. At the moment, the volatility range is narrow but we may be on the brink of brutal disruption.

How will you manage such disruption? Our structures are built to deal with volatility and shifts in the forward price curve. Our fundamental role is to reduce imbalances. If markets were stable and well-adjusted, we would bring little added value.

Isn’t volatility precisely what scares investors off? We take charge of the volatility. From an investor’s viewpoint, commodity trading has proven to offer extremely stable results, a bit like coupons on a bond. Generally speaking, when trading houses have experienced losses, these losses came from the asset part of the company.

Does innovation disrupt or support your strategy? Innovation may have a disruptive effect and create imbalances on energy markets as we have seen with shale technology. Other types of technologies help us manage the information overload. The vast amounts of data from oil, gas, and power markets are often subsidised which favours the energy mix but triggers huge cost overruns. Innovation may have a disruptive effect and create imbalances on energy markets. The latest OPEC agreement with countries outside the cartel has brought about a situation closer to Russia in a most unusual move, an unexpected reconciliation between the two countries’ interests. President Trump’s threat to penalise imports would have significant implications for the crude industry. His sharp criticism of President Obama’s nuclear deal and the possibility of new sanctions against Iran would also have a major impact on oil flows. So would his push for better US-Russia ties free US investment in Russian projects? The future is extremely difficult to predict. Uncertainty is at its highest level in years and as you know, uncertainty boosts volatility. At the moment, the volatility range is narrow but we may be on the brink of brutal disruption.

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Does innovation disrupt or support your strategy? Innovation may have a disruptive effect and create imbalances on energy markets as we have seen with shale technology. Other types of technologies help us manage the information overload. The vast amounts of data from oil, gas, and power markets are often subsidised which favours the energy mix but triggers enormous cost overruns. This creates uncertainty around investment in power units as ultimately no one really knows what the price of electricity is. Another aspect is the impact of environmental concern over existing capacities. For example, one third of French nuclear plants were stopped between October and December for maintenance due to varying weather conditions. For example, one third of French nuclear plants were stopped between October and December for maintenance due to varying weather conditions. These losses came from the asset part of the company.

Can you see other applications of blockchain in the trading environment? It could definitely be adapted to warehouse receipts as for example commodity -storage receipts are an increasing concern.

Renewable energies also stem from innovation and have introduced further disruption. How do they affect the energy market? Renewable energies are indispensable to reach the COP21 objectives. They are often subsidised which favours the energy mix but triggers enormous price volatility. At times of high offer (high winds or sunshine) and low demand, electricity prices may even become negative. Furthermore, decentralised production means that the volumes available on the grids are hard to predict. This creates uncertainty around investment in power units as ultimately no one really knows what the price of electricity is. Another aspect is the impact of environmental concern over existing capacities. For example, one third of French nuclear plants were stopped between October and December for check up and maintenance with great loss in production. Extreme volatility and environmental concerns discourage investment in renewables but also in other sources of power such as fossil fuels or nuclear plants. This means that, with time, prices may soar. It may also mean that newcomers - information providers such as Google for example – could enter the electricity market because they own information about end users’ behaviour.

In January 2016, ChemChina completed a strategic investment in Mercuria. A year on, what is your assessment? Are you looking for other investments? Over the past year, we have found numerous examples of synergies between the two companies and are considering re-enforcing our cooperation further. As we are already overcapitalised, we are looking for other partnerships rather than for investors.

(1) According to NICE & C, it is common practice for traders, usually when they are the sellers of the goods and the charterers of a vessel, to instruct the carrier to discharge cargoes without production of the original bills of lading and to agree in indemnity the carrier against the consequences of doing so. This is done by providing a Letter of Indemnity (“LOI”).
The past year has seen a common culture of research slowly but steadily taking root within the commodity trading industry.

In addition to the promotion of research work, the SRIC has successfully brought together academics and industry members under one roof, as well as NGOs, authorities and the public at large. Under its auspices, these direct encounters crucially provide a vital voice to all types of stakeholders to ensure to engage in informed dialogue and find common ground. For example, the annual Trading Forum brings together this wide audience to examine some of the hot topics and challenges in the commodity trading industry, such as technology and trends in business ethics. Many students are in attendance, meeting with industry members and engaging in a continuous culture of learning with different perspectives being heard from all sides. Additionally, other public multi-stakeholder dialogues have been taking place, focused on important issues such as human rights in climate change. The outcomes have been impressive, providing solid grounding for researchers and industry members to further develop fundamental and practical knowledge and identifying innovative solutions.

An example is the discussion on ‘Measuring Human Rights Performance: Metrics that Drive Change‘ provided food for thought in the context of turbulence and mounting anxiety over the trade system. Professor Ponser highlighted the need for industries to take greater steps to meet public expectations by defining metrics to concretely measure the human rights performance of companies. More recently, in a dialogue on ‘Climate Change and the Post-COP21 Dynamic‘, Professors Beniston (co-recipient of the Nobel Peace Prize of 2007) and Di Falco examined climate change developments in the current political and economic context. More is set to take place over the course of 2017. Following the next Trading Forum on 21 March 2017 on innovation and business ethics, new seminars are planned for 2017-2018, with several keynote speeches under preparation. These snippets from the past year are only the tip of the iceberg. Though in their early stages, these bridges have already proven to be solid and effective ways to expand upon knowledge and research across the spectrum. Time and time again we have heard of the major challenges that lie ahead for the commodity trading industry. But by crossing these bridges to engage in knowledge sharing, we can transform these challenges into exciting new opportunities for a joint future.

THE STUDENTS OF THE MASTER IN TRADING ARE AN EXAMPLE OF THE SUCCESSFUL BRIDGING OF PROFESSIONAL AND ACADEMIC WORLDS. OUTSTANDING RESEARCH IS ACCESSIBLE ON THE SRIC’S WEBSITE.

Bridging the gap to greater knowledge

THE ECONOMICS OF CHOCOLATE

Written by researchers from KU Leuven, this book covers the history of cocoa and chocolate from its origins in Central America to the recent consumption boom in emerging markets, as well as the growing importance of sustainability. Written by researchers from KU Leuven, this book covers the history of cocoa and chocolate from its origins in Central America to the recent consumption boom in emerging markets, as well as the growing importance of sustainability. Written by researchers from KU Leuven, this book covers the history of cocoa and chocolate from its origins in Central America to the recent consumption boom in emerging markets, as well as the growing importance of sustainability. Written by researchers from KU Leuven, this book covers the history of cocoa and chocolate from its origins in Central America to the recent consumption boom in emerging markets, as well as the growing importance of sustainability. 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Transfers aim to better use talents and to offset shortages in some countries. This is particularly true for the commodity trading industry.

How to boost talents in a mobile world

Employees are now being transferred to another country or continent for a period of time, and may not return to their initial working location for years, while managers are often called to share their working time between different business units located in Europe or elsewhere. In parallel, the increasing diversification of businesses and the rapid development of new technologies require professional versatility. Employees are regularly requested to change position or to switch from one business unit to another and to quickly adapt.

This trend of internal transfers aims to better utilise employee talents within the company and to compensate talent shortages in certain countries. This situation is particularly true for the specific set of professions that are central to the commodity trading industry. Switzerland plays a leading role in preparing young talents for these demands through internationally-renowned training programmes designed specifically for the industry. Following completion of their studies, they will often be sent immediately to another country within the company group. These international assignments are no doubt a great career development opportunity.

Rising in the ranks of today’s globalised workforce are Generation Y or Millennials (defined as born between 1980 and 1995), who tend to seek a work/life balance that is both interesting and meaningful, and are generally keen to be mobile. They grew up travelling abroad (being the first generation growing with low-cost travel) and they enjoy a far greater degree of international exposure than previous generations. Millennials often do not consider international assignments as a “big deal”. Universities prepare students to meet today’s challenges and to thrive in a global economy by offering exchange programmes around the world and opening their classes to a vibrant mix of international students. As experienced with the Commodity Trading Master of Geneva University run in partnership with STSA, Master degree candidates do not hesitate to cross oceans to find more suitable programmes for their career aspirations, giving them a first taste of expatriation.

In this highly competitive professional environment, training is more than ever a prerequisite. Switzerland, with its high concentration of actors and experts, has become a centre of excellence producing a major talent pool brimming with training and employment opportunities (see the Swiss sector analysis by STSA/UNIGE on pages 6-7). Switzerland has become a springboard for new talents to enter the industry, STSA continues to address this need for mobility and versatility to better serve the interests of its members and reinforce the Swiss commodity trading hub. Not only does STSA offer in partnership with the University of Geneva two internationally recognised academic programmes (a Master of Arts and a Diploma of Advanced Studies), but on the request of its members STSA has developed its own competence centre providing a full range of professional trainings that evolve constantly, in line with new trends and industry needs.

Recognising the increasingly diversified activities of commodity trading companies and the fact that no company today trades only in one type of commodity, all educational programmes organised by STSA cover the three main families of commodity (agri, energy and metals). This equips young professionals with the specific set of professions that are central to the commodity trading industry and to cross international bridges, both locally and internationally.

These programmes continue to yield proven results. Many of our graduates have successfully entered the commodity trading industry, and many have benefited from mobility, working both on the banks of Lake Geneva and much further afield.

The challenge for STSA is to continue to create value and keep up with the pace of new trends and technologies. Ultimately, we must maintain the Swiss commodity trading hub’s competitive advantage of unique and local expertise to be transmitted to next generations of physical commodity trading specialists.

For more information, or to register, please email: stephanie.harper@euromoneyplc.com

Global Commodities Finance Conference

8th & 9th June 2017 | Hotel President Wilson, Geneva

Featuring: FINTECH TRADE FINANCE BRIEFING DAY® 7th June 2017

Connecting with traders, producers and insurers to optimise working capital across the supply chain

For more information, or to register, please email: stephanie.harper@euromoneyplc.com
This special edition has been produced with contributions from STSA, industry professionals and the support of the following organisations