Trade Safe: Episode 2

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SANJEEV GANJOO: I can only foresee that this might be a key differentiator as a key financing source for the corporates in the next decade. And also, many small and medium-sized enterprises may follow a similar path as well.

SPEAKER 2: Welcome to Trade Safe, a podcast series for trade credit professionals where WTW experts talk with industry colleagues on how organizations across all industry sectors can manage trade credit risks safely.

SCOTT PALES: A warm welcome to our listeners, as we embark on our second podcast topic in our Trade Safe. Series I'm your host, Scott Pales. I'm a trade credit specialist broker with WTW. And with me is my partner, Sanjeev Ganjoo, who's the global head of AR financing with Citibank. Welcome, Sanjeev.

SANJEEV GANJOO: Hello, Scott. It's my pleasure to be participating in this series of podcasts. And once again, thank you so much for inviting me.

SCOTT PALES: You're very welcome. So Sanjeev, for today's discussion, I'd like to dig a bit deeper into what we're seeing with regard to changing client behaviors on a pre versus post-pandemic basis. So let's kick off by looking back five years ago. What are the biggest structural differences that you see with today's portfolios being submitted for bank consideration?

SANJEEV GANJOO: Now, as comparison to five years back, I do think that there are a lot of differences which have emerged in the current environment. And the key differences we are seeing in today's portfolio structures are mainly the cross-border portfolio-- now, this cross-border data which earlier used to be only domestic based, mainly because it appears clients have started exploring growth in the wallet internationally just to align themselves with the shifting of supply chains.

SCOTT PALES: Well, that's an interesting shift. Does this then open the bank to FX issues? And as this is a pretty significant benefit, I'd have to assume bank clients are willing to pay incrementally higher costs to achieve this solution.

SANJEEV GANJOO: It does. It does involve FX because obviously when you start moving from local to regional to global, it does involve the FX piece. And I think insurers do factor in pricing accordingly. Next point on that specific topic is, again, we are seeing the diversified portfolio, which used to be initially a concentrated one. So now, it has become-- just because we are talking of a global scale, we are seeing a diversified portfolio nowadays.

SCOTT PALES: It seems to me that historic concentrated portfolios-- and bear with me because I'm using my air quotes-- were cherry picked to facilitate funding versus risk transference. So do you see this current push to increase available funding, to secure risk transference, or is it maybe a bit of both?

SANJEEV GANJOO: I think it's a bit of both. I would say that. And obviously, since the portfolios are becoming more diversified, more cross-border, so I would turn this as a mix of both. On the mix of the portfolio, in terms of the rating of the portfolio, I've seen that there is a mixture of investment grade and non-investment grade debtors, and a reason for this being clients appear to be looking more from a balance sheet perspective besides purely risk mitigation.

SCOTT PALES: So you are seeing the balance sheet tune-up versus risk mitigation due to this investment grade component? Or as we just previously discussed, is this more of, let's call it, a hybrid approach?

SANJEEV GANJOO: Yeah, again, this is my favorite word. I would say that this is still a hybrid approach, which corporates are adopting in the current environment. And next is on the securitization structures. These structures seem to be getting more common nowadays, and also a broader base of investors coming into the participants to cover in restructuring in securitization structures in anticipation of better yields.

SCOTT PALES: So this is interesting to me because historically, years and years ago, when we saw-- when we saw the securitization-based structures, it involved naming as the insured a bankrupt remote special purpose vehicle or special purpose entity. What you're saying now is effectively these securitizations transactions are being created with tranching versus the use of SPV, correct?

SANJEEV GANJOO: That's right, Scott. And there is a very clear risk-tranching being done to achieve the securitization framework. And last but not the least, we have seen tenors going beyond traditional one year into medium-term financings.

SCOTT PALES: Wow, so I'm curious on this one. If you're looking at medium-term financings for these transactions, what's the average obligor rating for these guys?

SANJEEV GANJOO: Typically, when corporates move into an investment-grade-- sorry, medium-term financing, typically the rating is in the investment grade category. I have not seen in a single B or a BB category portfolio. So traditionally, they try to stick within the investment grade portfolio because that gives some comfort to the banking industry as well.

SCOTT PALES: Yeah, that makes sense for medium term. So moving away from that specifically, what do you see the benefits of a client utilizing a bank purchase policy versus a policy that they might purchase directly from an insurer and then name the bank as a loss payee?

SANJEEV GANJOO: Sure, so I think there are a few benefits of a bank purchase policy. Some of them may be-- like, let me start with, first of all, is that banks do have a wider association with insurers globally through a broker network, which Scott you're very well aware of that.

SCOTT PALES: Yes, indeed.

SANJEEV GANJOO: And as a bank, they may be able to leverage greater policy limit of liability and indemnity coverages as well.

SCOTT PALES: No, I completely agree with that, as opposed to a seller who might be working with one particular global insurer. So the bank will have a multiple of insurer relationships for sure.

SANJEEV GANJOO: Yeah. Secondly, bank assumes operational risk of its management of the policy, which can provide more comfort to the corporates.

SCOTT PALES: True. But at the same time, the warrants under the RPA-- and I look at these warrants and I say that this still will make the insurers quite comfortable as well.

SANJEEV GANJOO: True. Mixes, banks may be able to get a broader coverage besides the buyer insolvency in terms of protractor defaults, political risk, cross-border coverages. And banks always ensure that they do get risk-attaching policies.

SCOTT PALES: I have to say that I think the market's already there for seller-owned policies as well. But I'm going to say that due to the volume of business that the banks are placing with insurers, my thought is that the banks can actually see stronger rates. And it's going to be due to the volume, as well as-- again, I come back to that underlying RPA, and then also policy structures. I know that many of these structures have pretty significant levels of first loss retention. So I think a combination of all those will bring better pricing.

SANJEEV GANJOO: Absolutely. And next is even in case of canceled policies, banks can ensure that notice period is sufficiently long to allow a switch to another insurer without hampering utilization of programs for these corporates.

SCOTT PALES: Or maybe just have the requisite time to transition that buyer out of the facility altogether. As we typically don't see a huge divergence in how insurers will see credit risk, it could simply mean that the buyer's just no longer eligible for coverage due to their deteriorated financial performance.

SANJEEV GANJOO: Correct. Next is even for the concentrated portfolios, banks are able to get a required coverages because, as I mentioned earlier, even though market is moving to a diversified portfolio, but we do get several deals where we do have a concentration. And because of our relationship or a wide network association with the insurers, we are able to get the required coverages for those portfolio as well.

SCOTT PALES: And I'm going to sound like a broken record, but I'm going back to that underlying RPA and policy structure. Those two things will also come through and allow for that concentrated portfolio to be insured.

SANJEEV GANJOO: Sure. Lastly, banks may be able to offer better pricing, as in case of seller-owned policies, the performance and operational risk on the seller increases, which banks have to factor in through increased pricing or enhanced governance.

SCOTT PALES: Yeah, I agree. And we touched on this earlier, but you just mentioned another dynamic. And that is the seller performance risk. So all things being equal, are you alluding that a bank-owned policy could potentially lower the all-in cost of funding versus a seller-owned policy?

SANJEEV GANJOO: I would say that it may. I won't say that it will, but I would say it may because of the other factor which I mentioned. The next is, again, a very interesting topic here is on the RTR, which is the receivables turnover ratio, and how are the treasurers and the CFOs nowadays being measured. Now, RTR, which is mainly the receivables turnover ratio, appears to be emerging as a new benchmark in the industry.

We have seen it become one of the key performance indicators for the CFOs, treasurers, and CEOs. Chruing receivables or monetizing receivables, has become a way of raising working capital without impacting the overall debt of the companies. The shorter the RTR, the better it may work in the favor of the companies.

Even investors are nowadays reviewing the RTR of the company. And it's also an indicator of clients' cash flows. A few years back, clients would have happily borrowed for working capital, which would have added to their debt. And we had an adverse impact on ratios. But many clients nowadays appear to be looking for off balance sheet items. And by monetizing receivables on wholesale basis, it really helps in getting their RTR in a much better shape.

SCOTT PALES: So we discussed RTR briefly in our first podcast. And now, we're mentioning it here again. So we see AR purchasing and off balance sheet funding. It's been out there for decades. How specifically is RTR changing client behavior? Or how is it changing the behavior in any way?

SANJEEV GANJOO: Yes. In fact, these are part of KPIs nowadays. When you talk of the annual performance of the CFOs, treasurers, finance managers, everybody do get analyzed at the year end in terms of their KPIs. And everybody is focusing to have a better RTR and uses it as an effective monetization tool for working capital benefits.

SCOTT PALES: Got it, got it.

SANJEEV GANJOO: And that brings us to a very interesting point is on digitization, Scott. You know this is, again, a very, very buzzword nowadays in the industry. How digitization has affected the way these funding programs are serviced? I personally believe the difference in growth in receivables between the last decade and next decade will be digitization, which seems to be the buzzword in the receivable finance industry. I love this word, the buzzword.
SCOTT PALES: Yeah
SANJEEV GANJOO: Not only banks, but the emergence of fintechs in this space is in itself a testimony how digitization is leading growth in volumes. For example, during last year only, we managed approximately $100 billion of throughput just because there were digitized receivable finance offerings available in the market. Not only it helps in volume growth, but with direct integration to clients' ERP. The two-way reportings are done on a real-time basis, which can automatically update clients' financial systems for further in-house reportings. Plus, with the innovative platform, it's become quite an interactive and very powerful data analytics tool, which guides CFOs, treasurers about their receivables position, debtors performance in repayments, and over dues, country-wide open position, et cetera, and a lot of other features available, right? And I think, as an industry, we need to rely on data analytics big time in coming years, which not only helps internally, but also externally for our clients.
SCOTT PALES: Yeah, as you're talking, I'm actually seeing this large dashboard in front of me. And there's various aspects of this dashboard open positions, as you mentioned, maybe perhaps country-based concentrations. And at any given time, one of the bank's clients can click on this and access really strong management information at their fingertips. Am I imagining this correctly?
SANJEEV GANJOO: That's correct. That's correct, Scott. In a simple way, it's like bringing enhanced data analytics at the fingertips of our decision makers in the company for effective balance sheet management. It's simple as that.
SCOTT PALES: Yeah, fantastic.
SANJEEV GANJOO: Now, while most of the banks have-- are really putting a substantial tech investments-- but at the same time, clients also need to digitize their internal systems to make it work. While few years back the host to host connectivity was mainly box for cash management services, but now I'm seeing it has spread its wings to bring receivable finance business under its umbrella as well. And lastly, from the numbers perspective, while the global receivables finance volumes are approximately $3 trillion, but with digitization being the key focus area, we might see these numbers doubling in the next decade.
SCOTT PALES: Oh, fantastic. So clearly, exciting times ahead for the receivable finance industry.
SANJEEV GANJOO: Yeah.
SCOTT PALES: Sanjeev, you provided our listeners with great information on changing behaviors as you're seeing from clients on a post versus pre-pandemic basis. Any closing comments from you?
SANJEEV GANJOO: Sure, Scott. I can only foresee that this might be a key differentiator as a key financing source for the corporates in the next decade. And also, many small and medium sized enterprises may follow a similar path as well, in terms of their vision of transformation from being a local to regional or to a global player.
SCOTT PALES: Well, thank you, as always, for your valuable insights, Sanjeev.
SANJEEV GANJOO: Thank you, Scott.

SCOTT PALES: And thanks to our listeners for tuning in, which reminds me to invite all of you to listen to our next podcast where Sanjeev and I will be discussing best practices and innovation in establishing accounts receivable purchase program structures. So until then, Trade Safe and be well.
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