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**Commodity Trading, its value chain  
and specificities to consider in the transparency debates**

By

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# Commodity Trading, its value chain and specificities to consider in the transparency debates



Dr Stéphane Graber, Secretary General



# GTSA in brief

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## GTSA is the main professional commodity trading association in Switzerland

- Created in 2006
- **More than 80 Members**, small, medium and large size entities
  - More than 60 companies involved in **commodity trading, shipping and certification**
  - 10 banks specialised in commodity trade finance
  - Associate Members such as large law firms and majors auditing companies
  - Institutional Partners such as the University of Geneva, CCIG
- Its **mandate** is to represent its members and their interests through various projects
  - Training young people in the various commodity trading professions
  - Explaining the different commodity trading professions and their economic significance
  - Supervision of working groups on sectorial and regulatory topics (i.e. Tax, ACT)
  - Maintaining a dialogue with the authorities and civil society



# Specificities of commodity trading

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## Commodity trading consists of buying raw materials to producers for delivery to consumers

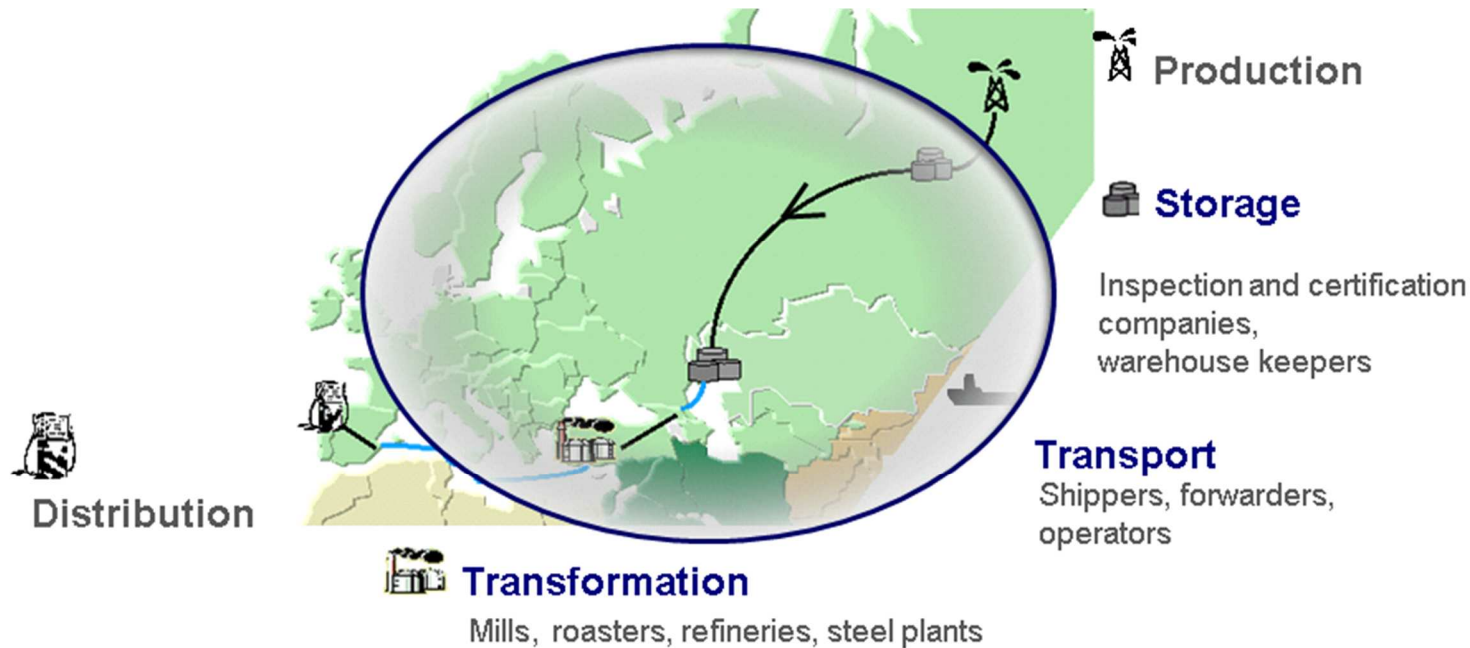
- It aims to buy at the highest price to producers and to sell at the lowest price to buyers through the optimisation of the logistic chain
- It evolves in globalised and increasingly complex markets

## Commodity merchants are market, logistic and transport professionals

- Their profit is made thanks to their capacity of
  - developing long term commercial **relationships** with producers
  - addressing the quantity and quality requests of long terms **relationship** buyers
  - optimising the logistic chain
  - managing price risks related to physical trade (i.e. volatility, exchanges)
  - managing operational risks  
(i.e. climate, counterparty, quality, legal, piracy, unstable environment)
- Their margin remains limited compared to the risks taken
- They have to protect themselves from price volatility to secure their commercial margin thanks to appropriate hedging transactions

# Role of commodity merchants in the logistic chain

Commodity traders operates **between the production and the distribution** along **with other actors from the supply chain**



**Producers and distributors use commodity traders because they need their market and logistic knowledge**

# Characteristics of commodity trading vs. mining industries

## Physical trading of commodities is often confused with extraction of commodities

Both activities have no comparable professional requirements and constraints in matter of know how, financing and societal or environmental impact

<b>Commodity trading</b>	<b>Extraction</b>
<ul style="list-style-type: none"><li>▪ profit independent from price level and made from margins on arbitrages (i.e. commodity quality, location, storage, transport)</li><li>▪ Contracts mostly secured through public tenders and market places</li><li>▪ Financed on risk capital (short term)</li><li>▪ Mostly private to preserve the flexibility required by the inherent volatile nature of commodity trading</li></ul>	<ul style="list-style-type: none"><li>▪ profit are related to the price of the extracted commodity</li><li>▪ Margins 10 to 15 times higher than in commodity trading</li><li>▪ Financed on investment capital (capital-intensive and long term)</li><li>▪ Mostly public with shareholders expecting steady quarterly earnings and tight management of debt</li></ul>

**The different characteristics between commodity trading and extractive activities must be considered in the regulatory approach**





# Towards mastering “optionality” vs. vertical integration

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“Optionality” means **diversifying supply sources to answer market demands, while the core business remains responding efficiently to costumers**

- Because, buyers are more demanding (i.e. ethic standards, short term worldwide delivery), commodity traders corporate value and reactive global services make the difference in a very competitive market
  - commodity merchants need to be flexible and secure quick access of requested standard and quality
  - i.e. they may open new ports to increase efficiency of infrastructure and delivery or they may invest in production or storage to insure flexibility of resource access
- **Specific asset diversifications** ≠ vertical integration, which is running at the same time production, logistic and downstream activities in the same proportion, capturing margin all along the value chain
- We also observe a **horizontal diversification** linked to the interconnectivity of markets

## Risks:

- Enter capital-intensive operations with long term financing needs + limited experience

**In taking the best decisions across the supply chain, commodity merchants are able to**

- **provide the best services** to the market
- **react swiftly to disturbance** in the commodity’s market equilibrium

**The best asset of commodity traders remains human resources!**

# Best approach to transparency

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## Experience shows that the right approach lies not necessarily on more regulations

- Swiss companies are already **well regulated** with national and internationally recognised legal standards and auditing obligations
- The implementing costs of new procedures, the potential impact of certain directives on market liquidity and the **risks** to sink companies under paperwork should not be underestimated
- Most commodity trading deals are done on public tenders or through market places
- Economically and commercially sensitive data must be **protected**
- More regulation does not mean better regulation, there will still be ways to escape as transparency regulations are difficult to implement
- The market regulates itself thanks to the ethical requirements of the consumers (i.e. coffee)

**Commodities merchants are looking for settlements that are adapted to their activity and applied internationally and multilaterally to all actors involved in the market**

**A multi-stakeholders approach on voluntary standards seems to produce better and more efficient results than a compulsory regulatory approach**

- Switzerland has been very successful in promoting voluntary initiatives such as the International Code of Conduct for Private Security Service Providers (ICoC)
- The Kimberley Process, DDII, ITIE have shown better ways to address complex issues in developing countries



## Message

The need to evolve in a stable and well regulated environment is a challenge shared by commodity merchants who are looking for prediction and risk mitigation

**GTSA** 

Dr Stéphane Graber, Secretary General

