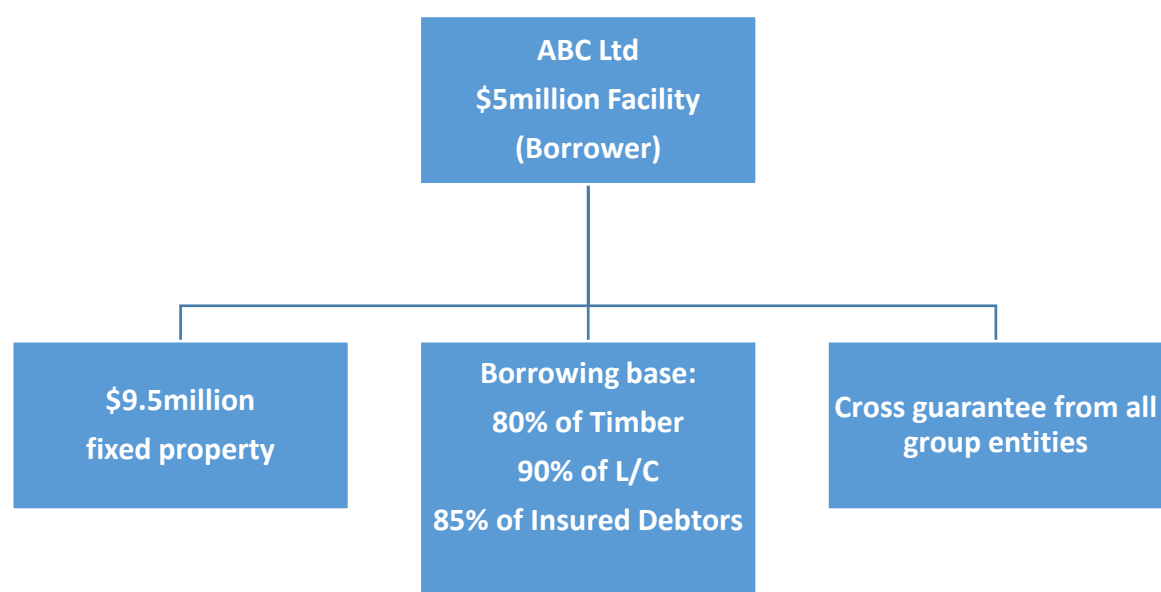


# ABC LIMITED

## CREDIT APPLICATION

### TRANSACTION AT A GLANCE

ABC Ltd is an AIM-listed company with award-winning social impact credentials<sup>1</sup>. They require \$5million in fully-collateralized trade finance to fund working capital emanating from a sharp growth curve due demand in their African sustainable timber business.



### BASIC TERMS

**Facility amount:** USD5,000,000

**Security:** Sawn Timber, backed by offtake contract

**Upfront fees:** 2% (USD100,000)

**Interest:** 11.5% per annum

**Term:** 12 month revolving facility

### FACILITY DETAIL

**Amount:** USD5,000,000

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<sup>1</sup> Appendix 1b – September 2017 Social Stock Exchange Impact Report (page 2 Impact Company of the Year sub \$150m capitalisation category)

**Security will comprise of a borrowing base**, such that the amount disbursed under the facility amount equals the aggregate of:

- i) 80% of the cost of timber, cut to standard sizes, attached to a legally binding off-take contract
- ii) 85% of insured receivables insured at 90% of invoice value
- iii) 90% of amounts due under Letters of Credit once all conditions are met

**Additional security (Fixed Property):**

- i) First mortgage over Mozambique saw mill valued at \$1,500,000
- ii) First mortgage over Tanzanian farm valued at \$500,000
- iii) First mortgage over 2 Gabon factories valued at \$7,500,000

Note: Legal description of properties to be verified by counsel, and an acceptable independent valuation report to be supplied.

**Facility fee:** 2%

**Interest rate:** 11.5%

**Term:** 12 months, renewable annually

**Collection Account:** All offtake payments to be paid into a collection account.

**Additional conditions:**

- i) Assignment of supply and offtake contracts.
- ii) Assignment of debtors.
- iii) Assignment of all proceeds under Letters of Credit.
- iv) Assignment of cash account operated for purpose of receivables.
- v) Single trade is limited to \$250,000 per shipment.
- vi) **Guarantee by all group entities, joint and several for full debt.**

**Tenor:** 150 days maximum

## TRADING & FINANCE CYCLE

- a) The trading cycle commences with a sales contract with an off-taker,
- b) Stock is then sourced from supply within the group or from external suppliers,
- c) Our first and only disbursement for **80% of the purchase contract with a supplier** occurs once the stock is containerized and under the control of the logistics agent who acknowledges our claim over the stock.
- d) The disbursement will only occur if the stock is tied to a specific off-take contract with evidence that it complies with the quantity and quality specifications. Verification of specification will be proved via a third party inspection certificate e.g. Government agency or SGS. The stock may also be purchased from an ABC group entity.
- e) The stock may require kiln drying after purchase. The kiln drying process and site in Abidjan has been inspected and has been proven to be relatively risk free since it speeds up the natural process of drying wood via the circulation of warm dry air in

an enclosed space. The company reports no losses since inception in 2004 using this process.

- f) The borrower will supply proof of marine and cargo insurance for each draw, with the Lender nominated as loss payee.
- g) All offtake contracts are to be made payable to a collection account under the control of the Lender in the event of default.
- h) Over and above product costs, the borrower has to pay duties, fumigation and stuffing costs, which are approximately 10-15% of cargo value, varying per region.
- i) Note we have suggested a limit on the size of a single trade being \$250,000, which same limit is applied by the insurers as their maximum conveyance limit.

## **EXIT STRATEGY IN THE EVENT OF DEFAULT**

The primary risk of default on a singular trade would be a consequence of an individual off-taker failing to make payment due to financial reasons. As discussed above, the risk of dispute due to quantity or quality is eliminated by obtaining a third-party inspection certificate prior to shipment.

In the unlikely event of non-payment, the cost of diverting the container is approximate \$2000-\$4000, depending upon the destination. A number of alternative off-takers can be chosen considering that we are not funding any custom cuts, only timber cut to standard sizes. See list of off-takers below showing that the Borrower is not dependent upon any single off-taker

## **COMMODITY OVERVIEW**

- Global demand drivers (population, housing, and middle income growth) create a robust outlook for timber demand growth led by emerging markets (China and India)<sup>2</sup>
- ABC is one of the few funded timber operators in Sub-Saharan Africa committed to both sustainable forestry management and moving up the value chain.
- ABC is currently producing sawn timber through subsidiaries in Mozambique, Ivory Coast and Gabon, with plans to complete a veneer factory in Gabon in late 2017.
- Global timber trading platform, acquired through the acquisition of ACME, provides access to a global customer base and an opportunity to drive profitable revenue growth by expanding the division's access to trade finance.

## **FEATURES OF TIMBER SECURITY**

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<sup>2</sup> ABC Investor Presentation 2017

Timber is a robust commodity that is considered relatively low risk in terms of transport, care and storage. Although timber is an organic product, it is not easily subject to damage or theft. The commodity is bulky in nature and theft is generally not reported as a major risk. The product is however fully insured against all risks, including theft, water damage, and fire.

We have thoroughly investigated the drying process that the wood undergoes prior to sale. The product is transported to a kiln drying facility where it is subjected to mild heat and air flow to speed up the drying process that would occur naturally. The kiln drying process is akin to a controlled storage space, rather than anything that can be said to transform the product. Damage during this process is unheard of as it would require negligence to the extent that product is “forgotten” in the storage facility for more than 10 days. In the unlikely event that this occurred, the product can still be sold at a slightly reduced value.

We have insisted that any commodity financed by us is cut to standard international sizes in order to ensure that the product remains sale-able to multiple off-takers, or on the open market.

(Declined veneer product as security for now. Concerned about the fragility of the product despite insurance. Solid timber is fairly robust and forgiving in terms of moisture and spoilage of any kind. We can reconsider on renewal).

## ADDITIONAL SECURITY

ABC’s fixed assets are unencumbered. We have therefore seen the opportunity to take their fixed assets as additional security. This is motivated by the fact that we shall be ABC’s largest lender; albeit fully secured by commodities. This approach also makes it more difficult for them to raise other debt. The primary assets are:

- \$1,500,000 Saw Mill in Mozambique
- \$500,000 Farm in Tanzania
- \$7,500,000 Factories in Gabon

Note we have requested an independent valuation report as a Condition Precedent.

## INSURANCE

Our collateral remains fully insured by the client. The policy is underwritten by Hollard, one of South Africa’s major insurers. Hollard carries a domestic AA rating by GCR in South Africa. Salient terms are listed below:

Exports:	US\$250,000 any one vessel
Inland Transit:	US\$50,000 any one vehicle
Storage Abidjan:	US\$ 3,000,000
Storage San Pedro	US\$ 3,000,000

Storage Gabon	US\$ 1,500,000
Storage Mozambique	US\$ 850,000

The borrower has also obtained a quotation for insurance of stock within the kiln drying process. We see the kiln process as a relatively risk free process but we take comfort in the insurer's backing.

## BACKGROUND

ABC Ltd is a public company founded 15 years ago and listed on the Frankfurt Stock Exchange. The company has 300m shares in issue, with a market cap of \$67m. Since 2016, the new chairman and CEO have overhauled the board and management team. The company has disinvested from non-core assets and remains focused on sustainable timber trading, and also the expansion of its agricultural arm.

## MISSION STATEMENT

*"To be the leading provider of sustainable commercial enterprise on the African continent by respecting the world's most demanded and diminishing natural resources. We want to contribute to sustainable community development wherever we operate."*

They have a particular focus on vertical integration as demonstrated by their purchase of ACME.

## SUSTAINABILITY

Paramount to ABC's vision is the preservation of its already-impressive track record of responsible management of human and natural resources. ABC has an outstanding track record in managing its social and environmental impact. Some of the highlights are listed below but more detail is to be found under Appendices 1a and 1b.

- In 2013 ABC was awarded received a prestigious award for its social impact work **and investment in local communities where they operate.**
- Letter of Intent to Invest Africa, pledging to invest \$10m over 5 years in Tanzanian agriculture and its workforce through new infrastructure, training and extending its Outgrower (contract farming) programme.
- Partnership with A and B University of Agriculture in Morogoro.
- ABC supports and adheres to the World Bank's Forest Investment Plan and Climate Smart Agriculture (CSA) initiatives, which aim to increase productivity, improve food safety and boost farmers' incomes, while enhancing resistance to negative

environmental shocks such as droughts and, not least, reduce greenhouse gas emissions.

- Advanced talks with the African Development Bank to collaborate on agricultural projects, public private partnerships and facilitating the regional and global export of produce.

## SHAREHOLDING

Note to course members: A detailed discussion of all shareholders (more than 5%), the board, and the management team was included. This section has been removed for the sake of confidentiality.

## FINANCIALS

Overall the financials show a solid, conservatively managed balance sheet, but trading has nevertheless been unimpressive. The following report was obtained from the FD regarding their lackluster performance for the current financial year:

1. *“H1 is normally very quiet for us as:
  - a. It is the rainy season in Tanzania where nothing can be planted (for about 3 months) and then we can only harvest anything planted after the rainy season in about month 5.
  - b. There is a cutting ban in Mozambique (normally 3 months annually);*
2. *This year, the cutting ban was extended (normally 3 months of the year, but in 2016 it was nearly the entire 6 months);*
3. *Even though we cannot plant and cannot cut, we have to maintain our camps (both in Tz and Mz) and this means continuing to feed the group of workers who are on site (also providing electricity etc.). This cost was all expensed as cost of sales (when it can probably be capitalized into the value of closing stock);*
4. *H1 2017 was the first year that we exported containers to Dubai (and ABC is the first company to do so out of Tanzania). In order to ensure that the whole export process would run smoothly (once we scale up), we exported a few test containers (with fruit) and followed it every step of the way to ensure that we knew e.g. what paper work was required at what stage and also to correct the cold chain. This resulted in the write off of about 3 containers of stock as waste.*
5. *ACME was only acquired on 30 June 2017 and so our H1 results does not include ANY wood trading revenue.*
6. *Admin/operational costs in H1 had an element of duplication in that we were hiring new people to bring expertise internally, but kept on the various consultants during*

*the 'hand-over process' to ensure that the new people were sufficiently trained and the work properly handed over.*

7. *XYZ, the Zambia business that was sold off in 2016: We were liable to pay \$148,000 in rent for various sites during H1 where we could not otherwise dispose of the leases. This has now come to an end."*

## CURRENT & NEW DEBT

The group currently operates entirely out of its own cash resources without using bank or other credit facilities. The only debt being used is a EUR5million facility housed in ACME a recent acquisition. The company is perfectly positioned to take advantage of consistent demand for timber globally. Having invested substantial capital in infrastructure and a solid management team, the priority of the business is to ramp up sales.

## COMPETITOR ANALYSIS

The following represents ABC's primary competitors as seen from management's point of view on the market. Brief comment is included re each.

Company Name	Website	Description
JAF Global	<a href="https://www.jaf-group.com/en/markets/jaf-global">https://www.jaf-group.com/en/markets/jaf-global</a>	Global timber trader. Private company with ~1bn euro turnover. JAF have a longstanding relationship with ACME and had attempted to buy the company before ABC made an acquisition in 2017. JAF's primary interest in the acquisition was access to ACME' African supplier relationships.
Rougier	<a href="http://www.rougier.fr/en">http://www.rougier.fr/en</a>	Listed in France, with ~90 year family operating history in Africa as a producer of timber in Gabon, Cameroon, and Congo. They produce plywood and veneer which they export to France through their distribution network.
Timtrade	<a href="http://www.timtradewood.com/">http://www.timtradewood.com/</a>	Privately owned timber trader based in France sourcing from Europe and Africa. No production assets.
IHC	<a href="http://www.interholco.com/">http://www.interholco.com/</a>	Privately owned timber trader founded in 1962 with Production assets in Congo (1.16 million hectares), 7 regional sales offices in Europe and Asia.
Barths	<a href="http://www.barths-hamburg.de/startE.php">http://www.barths-hamburg.de/startE.php</a>	German based timber trading company founded in 1873. Exporting veneer and hardwoods from Africa, South America, and Asia.
Olam International	<a href="http://olamgroup.com/">http://olamgroup.com/</a>	Global agribusiness. Olam operates the Gabon SEZ outside Libreville inside of which our third party kiln operator is located.

PVS International (Dubai)	<a href="http://www.pvsinternational.com/">http://www.pvsinternational.com/</a>	Global timber supply chain player operating in 8 countries. Partner with and finance timber producers around the world.
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## BUDGETS/PROJECTIONS

Note to course members: financial date removed from this presentation.

Below are some of ABC's major off-takers.

Customer	Description
Assawaed Assamraa Company	Biggest timber and steel importer in Libya.
Inter-Continental Hardwoods LLC	One of the largest importers/exporters in USA.
B.F.T (Bois Fer Trading) – BFT	3rd largest importer of wood products in Senegal.
CP Timber Ltd	Importer / distributor, privately owned.
Elof Hansson USA Inc. Timber Division	Swedish paper pulp and wood company, operating worldwide.
Chabros International Group FZCO	Leading importer/distributor in the Middle East.
Woodland Lebanon S.a.r.l. Timber and Veneer	Top 10 importer in Lebanon.
Great Atlantic International, Inc.	US hardwood importer based in North Carolina.
North American Wood Products, LLC	Global distributor of hardwoods and softwoods.
JAF Global GmbH	Biggest distributor in Central Europe, one of the biggest buyers in Africa.
Northwest Hardwoods Inc.	Leading US importer of plywoods.
South Florida Lumber Co.	Privately owned distributor in Florida and Caribbean.
Evergreen Hardwoods Inc.	Dominant importer of veneer - supplying US plywood industry.
Hawat Trading Co.	Lebanese importer.
TWM TransWorld Maderas	Danish broker specialized in selling to Caribbean and Mexico.

## CONCLUDING REMARKS

ABC, as a listed entity, seems to have a solid management team who are personally invested in seeing the company's growth curve come to fruition. The commodity is easily trade-able, fully insurable, and has little risk of spoilage. Upon investigating the kiln drying process, it was found that the process has almost zero chance of destroying product as the drying



process is slow and merely aims to speed up the process that naturally occurs when wood is air-dried. The process is in any event insured.

However, the largest risk we foresee in any one trade is the counter-party risk that a new off-taker might pose as the company grows its client based. With the trade fully secured by stock, we see this risk as manage-able. Furthermore, the value of a single shipment (<\$250,000) is such that a very small amount of the facility is exposed to this risk. The fixed property taken as security acts as a further mitigating factor.

The business has a stellar Social Impact track record.