Opening Up Access to Finance through Warehouse Receipt Systems

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Presented by:
Michael Andrade
Sr Vice President – Agri Business
HDFC Bank, India
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- HDFC Bank was incorporated in August 1994

- Promoted by the Housing Development Finance Corporation

- Balance sheet size of US$55 billion (Rs 2,773 billion) and Net Profit of US$0.785 billion (Rs 39 billion) for the 9 months ended Dec 31, 2011

- Distribution of 2201 branches, 7110 ATM's across 1174 locations

- Key strengths include Cash Management, Trade Finance and Consumer Banking

- A pioneer and a dominant player in the Warehouse Receipt Market in India
Pillars of HDFC Bank’s Agricultural Business
• Retail Agri (farmer Services)
• Commodity Finance (post harvest services)
• Rural Initiative Group (supply chain)
• Co-operatives

Commodity Finance
• Agri Business Credit & Cash management
• Warehouse Receipt Loans

Structure
• Relationship Managers
• Product Control Group (surveillance team)
• Central Product Team

Partners
• Collateral Managers
• Service Providers
• Buy back agency’s
Characteristics of Warehouse Receipts in India

- The Formal Warehouse Receipt Market in India evolved only 5-6 years ago
- The market is hovering at US$2BN (Rs 100 billion)
- This is a fraction of the US$6.6BN (Rs 3,300 billion) lent to agriculture
- The market has remained limited in size and scale due to:
  - Lack of quality warehouses
  - Govt. intervention in order to control inflation
  - Collateral management losses to banks
  - Wholesale in nature
- The Warehouse Development & Regulation a/c 2006 addresses all these issues once implemented
Warehouse Receipt – Dominated by Large Players

- Farmers
- Intermediary
- Agro processor
- Traders
- Govt Agencies

- Very limited stocking by farmers
- Purchase agents may take small positions

- Most of the stocking happens at the wholesale end of the supply chain
- Stocks under hypothecation form the bulk of bank finance
- Govt. Agencies take up a significant portion of warehouses capacity

To open access we have to take the product downstream.
The current product features are designed for Wholesale customers.

It’s a Short Term loan given as an add on to normal working capital.

Due to inefficiencies in the Warehousing system it is not a pure commodity risk but also based on individual borrower assessment.

Key features:

- Tenor – One crop season (11 mths)
- Applied Prices and Margins set based on volatility on a monthly basis
- Mark to market done on a weekly basis
- Delinquency > 30 days are auctioned in the market.
- Stock insurance
- Pre-disbursement – warehouse approval
- Quality & quantity certified by the collateral manager pre-disbursement
Key Statistics

• Warehouse Receipt book has been in the range of Rs 15 billion.

• Covering 2,300 customers.

• 3,300 warehouses across the country ranging from 1,000 MT to 10,000 MT.

• Cost to income ratio of 65-75%.

• Collateral management fee is around 0.65% of a loan.

• Distribution:
  • 50% is Wholesale
  • 40% is Small & Medium Enterprises (Agro processors)
  • 10% Large Farmers
Challenges

- Farmers require much shorter tenors
- The loan sizes are smaller in comparison
- Given the high Collateral management cost this becomes unviable

Enablers

- Establishment of grading standards for commodities
- Shift from identity preserved stocking to co-mingled stocks
- Warehousing regulation
- Negotiable warehouse receipt that can be dematerialized
- Simplification and uniformity of state taxes

The Govt. has taken the initiative

- Warehousing Development and Regulation Act 2006
- General Sales Tax is expected to be resolved soon

Implementation of these initiatives by the Govt. are challenging

- Large number of low capacity warehouses (1,000Mt - 2,500MT)
- Shifting to comingled stocks is a huge challenge
Warehouse Receipt as Supply Chain Tool

- Set up the Terminal Market in warehouses attached to large agro-processors
- Bank manages the warehouse through a Collateral Manager
- Bank provides other banking services at the warehouse through a BC
- Price discovery provided from various sources
- Processor may out-bid the market due to savings on transaction cost & transportation

The Supply Chain Route to Farmer Warehouse Receipt is an intermediate step that can be taken up by the industry which will go a long way in the Govt.’s objective on WHR being achieved

Negotiable WH receipt gets transferred by Endorsement
In the interim the warehouse receipt will be part of the total supply chain rather than a stand-alone product.

An alternate to Contract Farming

Warehouse owners / Agro processors are the primary partners.
Key Challenges & Success Criteria

Challenges:
• Weaning farmers away from existing markets and intermediaries
• Warehouse rental costs (storage in the field is free)
• Farmers are politically sensitive (can create a law & order situation)
• Current Market does not reward quality
• Getting corporates to take the business risk (disturbing part of their existing supply chains)

Success Criteria:
• Gaining farmer confidence on availability of storage at an affordable price
• Providing buyers at all times
• Providing Settlement services and banking services at the warehouse
• Transparency in price discovery, mark to market and liquidation of stocks in case of defaults
• Access to Futures market at the warehouse
Trends indicate that stocking by farmers is on the rise this give rise to new challenges:

- Farmers do not have adequate access to organised storage facilities
- Agro processors are unable to plan their production schedules
- Creates volatility in prices

Benefits:

- The immediate benefits are that it addresses the above pain area’s
- Quality of produce will improve with scientific storage
- The combined offering of Warehouse Receipt, Terminal Market and Banking correspondent at a warehouse, increases the viability of investment in Warehousing
- Can easily be extended to Govt. procurements, improving efficiency
In conclusion

• Opening up the warehouse market to farmers downstream is an investment in the future warehousing market in India

• Banks richer by the experience of such pilots will be able to leverage and take part in the implementation of the Warehousing development regulations

• It is not only about providing a warehouse receipt loan to the farmer but providing complete services at the warehouse

• These developments will see a migration from traditional markets to warehouse receipt based Terminal and Futures markets

Thank you!