Oiling the wheels

As Middle Eastern consumer markets develop, countries look to increase trade ties and infrastructure investment into MENA. Yet with payment risk and cultural differences remaining barriers to trade for both parties, corporates will rely on their banks to help them grasp the opportunities, explains **Ralph Nitzgen**, Senior Executive Officer and General Manager, Commerzbank Dubai Branch. And, in this respect, the best solution is a correspondent banking network

The Middle East's economic resurgence following the financial crisis in 2008 has opened doors to extensive trading opportunities - for local corporates, and those based in Asia, Africa and the US which are deepening import and export ties with the region.

Yet trade with Europe should not be disregarded. Indeed, World Trade Organisation statistics highlight nearly 30 per cent of Middle East imports in 2011 were from Europe, equating to $194 billion of trade – making Europe second only to Asia in terms of an import source for the region. And Europe continues to be an exporter of manufactured goods that are then re-exported from the UAE – which is well-established as the region's trading hub – to Asia and Africa. What's more, as the Middle East's economy continues maturing, it is likely local corporates will increasingly turn to Europe for products and expertise; especially with regards to infrastructure and consumer goods.

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Certainly, the Middle East needs an estimated $4.3 trillion over the next 15 years to develop infrastructure in order to accelerate economic growth. Qatar, in particular, is looking to enhance global trade ties as it ramps up investment ahead of the 2022 FIFA World Cup, with up to $100 billion expected to be allocated to infrastructure projects including the Doha Metro System, the Doha Bay crossing and a major new airport development.

HIGH-END EQUIPMENT

Of course, the lion's share of these contracts is expected to go to Asian contractors, which have a cost advantage in terms of labour and raw materials. Yet European corporates will still have a significant role to play. Indeed, specialist European knowledge has long been utilised to provide high-end equipment on major projects, which is especially pertinent in the Middle East where innovation is being pushed to the limit. One recent example is the completion of Dubai's Burj Khalifa, the world's tallest skyscraper, which used specialised concrete pumps and specific expertise provided by Putzmeister Holding, a German concrete-pump maker.

Away from construction, the Middle East boasts some of the fastest-growing consumer goods markets in the world. Indeed, the luxury goods market is set to grow by 15 per cent this year, with the long-established

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reputations for quality built up by European companies resulting in them being major beneficiaries.

However, cultural and language differences, restrictions on certain investments, physical distance and high transportation costs are issues for corporates on both sides of the Middle Eastern-European trade corridor. The biggest barrier, however, is payment risk; also linked to political or economic risk. In this respect, trade may therefore be best served by banks on both sides of the trade collaborating via a correspondent banking network. And such a partnership may also have advantages for banks themselves.

POLITICAL CIRCUMSTANCES

Correspondent banking relationships, therefore, can help ease corporate concerns regarding counterparty creditworthiness. Yet counterparty risk is not the only concern. What is often neglected by corporates is how differences in political circumstances or economic situations may affect companies' ability to either supply goods or pay on time and in full, as contractually obliged. Construction projects may be halted in the Middle East by political turmoil, or economic turmoil could scupper production in Europe, for instance. In this respect, the experience and expertise of local banks in the Middle East – garnered from liaising with the local political players, local businessmen and local opinion leaders – is vital in helping particularly European corporates understand the scale of the risks and how they may affect trading contracts.

Indeed, correspondent banking relationships are beneficial not only to corporates looking to take advantage of this expanding trade corridor, but also for the banks on each side of the trade. Such arrangements can even provide local banks with liquidity and capital assistance, enabling them to reduce their borrowing requirements and continue lending. Additionally, global banks can also provide expertise to help in the management of loan books and risk management. Such relationships can also lower costs for banks, and help share risks – especially in new markets. Significantly, a correspondent relationship also means that participating global banks, such as Commerzbank, are not competing with local banks for corporate business in their local markets.

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THE BANKING CHAIN COMES UNDER THE SPOTLIGHT

With regards to understanding and then mitigating risk, corporate clients may favour a correspondent banking relationship between a Middle Eastern and global bank – combining their respective local knowledge, on-the-ground presence and transaction expertise. Such networks of banks can generate risk mitigation structures such as the use of letters of credit (LCs), issued and confirmed by the banks of the trading parties. Certainly, while other regions are moving towards open-account trading, LCs remain the most used tool for corporates trading with the Middle East, with their use being further boosted since the global financial crisis in 2008.

COMMITMENT AND FINANCIAL VIABILITY

Evidently, the strength of such a network – and its usefulness in supporting international trade – is dependent on the commitment and financial viability of the banks involved. For our part, we have been developing relationships in the Middle East for over 30 years. This means that, while many European banks responded to the crisis in the Euro zone by calling in loans, reducing credit and retrenching to core markets, Commerzbank did not; not a single credit line was removed during that period. And given that trading contracts can only be built on strong foundations, this commitment is vital if corporates are to seize the opportunities available.

Ralph Nitzgen is SEO and GM, Commerzbank, Dubai. He joined the bank in 1989 and, after working as a representative for Commerzbank in Germany, moved to the Middle East in 1996, where he became chief representative for the GCC countries and Yemen. He has worked with the region ever since, holding the position of regional manager, Middle East, as well as his current position, which he assumed in 2007. Nitzgen is also a member of the board and treasurer of the German-Emirati Joint Council for Industry & Trade (AHK), Abu Dhabi, and is a member of the board of the German-Arab Chamber of Commerce, Berlin.