Lonnie Frisby: Welcome back to Navigating Business. I'm Lonnie Frisby, and today I'm joined by Ajay Sharma, our Regional Head of Global Trade and Receivables Finance in Asia Pacific. Global trade has been hit on an extraordinary scale with the pandemic bringing the latest challenge to supply chains. For the moment, production from sourcing countries is slowly returning to normal levels.

However European and American retailers are still canceling orders and financial distress is a real risk facing many companies. So how can businesses respond and make decisions with this prevailing uncertainty? And what are the liquidity considerations facing suppliers? How can they minimize exposure to supply chain risk? Thankfully we have an expert with us here today to talk about the future of trade. Welcome, Ajay.

Ajay Sharma: Thank you, Lonnie.

Lonnie Frisby: So Ajay, COVID-19 is responsible for much of the collapse in trade activity. So I want to start by asking you, what are the implications that firms are dealing with as a result of COVID-19?

Ajay Sharma: So when we started in late Jan, early Feb, this really was a supply shock. Will we be able to actually get production out of China for a start? And the first thing that suffered was transport and logistics, and really there wasn't enough material that you could ship out in the short run because the clamp-downs were quite rapid in most countries.

And as we went along two, three months into this crisis, I think we've seen demand disappear or become much more muted, and this just shows up in all the numbers that you are currently seeing from The Economist. Whether you look at China exports first quarter, exports imports down 7%. Did pick up a bit in April, the China exports did. The US consumption went down 15%. The savings rate went up 30% against normal of 10%. That was quite a bit.

The question really is, is there pent up demand? There is money on the sidelines people are willing to spend. And will it come back? We did see early signs of it coming back, but the key question facing all of us is, is this going to be sustainable? How long will this demand last? And will we go back to pre-COVID levels of demand?

Lonnie Frisby: You make a good point, Ajay. So I'm quite interested to hear how has this extreme level of disruption, how has it affected businesses, but also banks.

Ajay Sharma: So everyone has had to really dust off or make sure that they had really strong contingency plans because this was an ultimate test of resilience. So a lot of our customers had them in place. I think the challenge was the speed at which the lockdowns when enforced in many countries, Bangladesh, India, Sri Lanka, Malaysia.

In Malaysia, we got notice at 8:00 PM and we had to scramble and get everything up and running next day morning. The benefit of which was that we were probably the only bank ready to transact at 9:00 AM. And that's really the ultimate test of our resilience.

Lonnie Frisby: I'm interested to ask, what kind of data are you seeing that can help illustrate the types of stress and strain that businesses are experiencing?

Ajay Sharma: Quite a bit of data. We have a fairly large book. And in terms of days receivables, if I give an example say China, we're seeing the receivable tenor extend from 74 to 86 days. That's 15%, 16%. The days past use that is, are you getting money in a timely manner, has increased from 1% to 4%. Getting better now.

Things are opening up but still a big jump. Typically the buyers will always adjust the money that they send or receivables, so for every 100 dollars, typically the adjustments with 3% or 4%. We've seen that jump to 6% to 8%. And all these three things really have an implication for our treasures in terms of cash flows and predictability of cash flows and the need to really spend more time managing day to day liquidity. But equally I think on the trade credit insurance front, the amounts that are available have come down and pricing against that insurance has gone up.

Lonnie: And Ajay thinking of some of those strains you just mentioned, what should companies consider as they formulate supply chain risk management strategies in response to the Pandemic?

Ajay: I think 3 points. Firstly, companies do need to look at the supply chains at a more holistic basis. Not the first layer. You need to look at it end to end so who are your suppliers' suppliers in a sense? So, 3- 4 levels down. And some people and some of our customers found out that while they have the full visibility of the first couple of layers, it wasn't all the way through and the disruptions can come at unexpected levels.

Secondly around inventory management, we all moved to a very tight turnaround just in time in terms of production. And I think this is just a wakeup call in terms of do you really want to be so skimpy in terms of inventory that the slightest disruption can create dislocations which you can't handle.

And finally, I think people are just going to fundamentally look at the supply chains in terms of, do you need to have multiple supply chains in different countries near-shoring, re-shoring and all of those. And from a banking perspective, I guess, how do you make sure that every level of your supply chain has access to liquidity.

Lonnie Frisby: Ajay, you mentioned near-shoring and re-shoring. Can you explain what you mean by those terms, and perhaps how you see supply chains will shift over time?

Ajay Sharma: It's quite simple. I think one, it's really getting your production where your customers are, and that from a logistics perspective makes it simpler. So you manufacturer where the demand is. It could be anywhere and on any of the large markets.

The other way to do it is really find the low-cost locations and or markets which have very attractive, free trade agreements. Markets like Bangladesh and ASEAN markets and especially Vietnam come to mind. Those often give additional benefits, which make it attractive to relocate into a new market.

Lonnie Frisby: Okay so let's get practical. What are some of the tools that you see that businesses can be using to help mitigate risk?

Ajay Sharma: So first of all, I think just to get some perspective here. We are now in a very different environment, even compared to late 2019. For the last six, seven years, the banking system has been flush with liquidity and the credit risk has been relatively benign, so that's changed. The best companies we deal with already have very formal risk management policies around the suppliers and supply chains that understand the multiple levels that they operate in, and therefore they understand every layer and the access to liquidity for each of that layer because that is becoming even more critical in this environment.

What role do banks play in this? Banks know how to manage counterparty risk, and therefore can be big partners. Equally there's insurance available in the market to mitigate risk. And when you put the entire capacity together, sometimes if that's not enough, there's a lot of work taking place in the market around distribution of trade assets and trade as an investible asset class.

Lonnie Frisby: Thank you, Ajay. Thanks for sharing your insights today.

Ajay Sharma: Thank you. My pleasure.

Lonnie Frisby: In the next episode, we'll discuss the emerging technologies and sectors that are shaping global trade. In the meantime, for more insights from HSBC or to listen to this series, please visit us at business.hsbc.com. Thank you for listening.