Energy sector

Commodity trade costs surge as industry seeks up to $500bn in extra finance

Rising rates, market volatility and the war in Ukraine are making it more expensive to move goods around the world

The price for shipping coal has nearly tripled over the past year. © David Gray/Bloomberg

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High interest rates, volatile prices and the war in Ukraine have made it significantly more expensive to finance commodity trade, forcing the industry to hunt for an extra $300bn to $500bn in working capital to keep raw materials moving around the world.

Changing trade patterns have made the global flow of raw materials less efficient and more costly to finance and are also likely to push up the price of commodities for consumers, according to a new study by consultancy McKinsey.

"Since the end of 2020, we have seen a doubling of the working capital requirements in the commodity trading sector," said Roland Rechtsteiner, McKinsey partner and lead author of the report. "We could see a similar increase by the end of next year, if [further] changes in trade flows materialise."

The commodity trading sector, which moves raw materials like oil, gas, sugar and gold around the world, is the engine of the global economy. However the cost of the financing required to move these cargoes has risen significantly because of volatility in prices and rising interest rates.

On top of this, Russia's invasion of Ukraine has trigged a profound shift in global trade flows — often resulting in longer, less efficient shipping routes.

One example is coal, where prices have nearly tripled over the past year. Europe is importing from Colombia, South Africa, Australia and other places, replacing coal that was previously brought from Russia. As cargoes have to travel further, financing costs rise.

“This year the traditional trade directions changed,” said Rechtsteiner. “That puts us in a suboptimal system in terms of efficiency, and increases costs.”

The McKinsey report predicts average shipping times will increase 8 per cent, energy prices rise three-fold, and interest costs will rise seven-fold, between the end of 2020 and 2024 and that working capital requirements for commodity trading globally will increase between $300bn and $500bn as a result.

Over the past year, even the world’s biggest trading houses have had to increase their lines of credit and seek new sources of finance. Trafigura increased its credit lines by $7bn to around $73bn by the end of last year.

Meanwhile Glencore disclosed that, during the first half of 2022, it had to post an additional $2bn to meet margin requirements on commodities exchanges, contributing to a “significant” increase in working capital during the period.

Governments have also had to provide emergency support for credit lines to utilities, particularly in Europe, where power and gas prices have been highly volatile over the past year.

From Germany to Austria and Finland, governments have stepped in to back credit lines for power producers and suppliers that have had to meet higher margin calls because of price swings.

The transition from oil and gas to electricity and renewables could further exacerbate the “regionalisation” of commodity trade flows, according to Rechtsteiner.