ICC BANKING COMMISSION | GUIDING INTERNATIONAL BANKING PRACTICE | DRIVING CHANGE IN TRADE FINANCE

2020 ICC GLOBAL SURVEY ON TRADE FINANCE

INTERNATIONAL CHAMBER OF COMMERCE
@100 years

IN THIS REPORT

ABOUT THE INTERNATIONAL CHAMBER OF COMMERCE

The International Chamber of Commerce (ICC) is the institutional representative of more than 45 million companies in over 100 countries. ICC's core mission is to make business work for everyone, every day, everywhere. Through a unique mix of advocacy, solutions and standard setting, we promote international trade, responsible business conduct and a global approach to regulation, in addition to providing market-leading dispute resolution services. Our members include many of the world's leading companies, SMEs, business associations and local chambers of commerce.

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ACKNOWLEDGEMENTS

This 11th edition of the ICC Global Survey on Trade Finance is the result of a dedicated collaboration between ICC, ICC Banking Commission experts and staff, and numerous organisations and individuals who have contributed with leading market intelligence content and timely production support. The report was enabled with outstanding guidance and backing from the Editorial Committee.

We express our sincere appreciation to the Editorial Committee for its commitment, engagement and invaluable contributions to shaping both the strategic direction and the content and analysis in this flagship ICC publication:

- Dominic Broom – ICC Banking Commission
- Mark Evans – ANZ
- Huny Garg – SWIFT
- Xu Jun – Bank of China
- Ana Kavtaradze – Bank of Georgia
- Alexander R. Malaket – Opus Advisory, Chair
- Dave Meynell – TradeLC Advisory
- Vincent O'Brien – ICC Banking Commission
- Olivier Paul – ICC Banking Commission

This report depended on the support and expertise of various specialists and partner organisations. We would like to thank our contributing authors for this edition and our colleagues in partner organisations who have also facilitated these contributions.

We extend our appreciation to the 346 respondents to the Global Survey located in 85 countries for their comprehensive, considered and insightful answers to the survey, which are at the heart of the consistently high value and quality of this report. Survey responses, complemented by expert insight, content and commentary, underpin a publication unlike any other in the market today, richly valuable for practitioners, policy professionals, international development practitioners, academics, multilateral entities and a wide range of members of the global ecosystem of trade and trade financing.

Boston Consulting Group is a critical partner to the ICC and the Banking Commission in the conception, development and publication of two flagship ICC reports, this one and the ICC Trade Register. Our multi-year association has progressed to encompass a wider scope of collaboration, and has been instrumental in raising the robustness, quality and authoritativeness of these reports. Our thanks to the BCG team for its tireless work, proactive leadership and skilled program management: Sukand Ramachandran, Ravi Hanspal and Noah Mayerson.

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INTRODUCTION

Foreword

John W.H. Denton AO,
Secretary General, International Chamber of Commerce

The year 2020 has not unfolded as anyone would have anticipated. The rapid spread of COVID-19 to nearly every country and territory in mere weeks has challenged assumptions about the resilience of the global economy and put tremendous strain on governments, businesses, healthcare systems and communities.

With supply lines and physical movement often curtailed in response, global trade as we knew it in 'pre-COVID-19' times has been significantly disrupted. The consequences have been severe, and the IMF predicts unsurprisingly the greatest drop in global growth since the Great Depression. Every day, the ongoing pandemic threatens the viability of businesses of all sizes and in nearly every sector. And as lockdowns in many countries remain in force, the devastating combination of labour constraints, travel restrictions and demand shocks continue to cripple business activity and escalate unemployment.

In such times, the role of ICC as the voice of global business is vital. Our work is animated by our clear priority to protect and preserve lives and livelihoods. As the only private sector organisation with a permanent seat at the United Nations, ICC has a crucial role to play in supporting the international response to this pandemic. And with an unparalleled reach across global business, we are uniquely placed to marshal key evidence to guide policymakers through their vital decisions.

This year's Global Survey indicates that banks are optimistic about the long-term future of trade finance and are looking to invest further to gain new clients, offer new products (such as supply chain finance), expand geographically and increase digital offerings. However, in the short term many banks anticipate a steep decline in trade flows due to COVID-19, with the majority expecting at least a 20–30% decline in 2020 from original forecasts. This broadly aligns with BCG's analysis in the Global Survey, forecasting a decline of between 11% and 30% in 2020 trade flows.

Enabling the shift to digitalised trade

ICC has already launched several initiatives to ensure that its global network can be put to best use in the fight against COVID-19. One aspect of our response to this crisis has incorporated key objectives to bring greater efficiency to the paper-based global trading system. Central to this is expediting the shift to digitalised trade, which the Global Survey shows is already underway but will need to accelerate in the wake of the crisis. Already this year, ICC has launched the Digital Trade Standards Initiative, a cross-industry effort to enable the standardisation of digital trade. This effort will bring greater economic inclusion, connect digital islands and ensure the all-important collective nature of formats and processes. We are also working with governments to implement broader legal

recognition of electronic documentation based on the uniform model law established by UNCITRAL. The far-reaching impacts of the pandemic have made plain that we must improve the outdated system of trade in operation at the outset of the crisis.

The fight to save SMEs and maintain open trade

One of the many benefits of a more digitalised trading system will be greater inclusion and increased opportunities for smaller businesses, which are the drivers of economic growth in most countries. The Global Survey reveals that financial inclusion was already a material concern for many trade banks even before the COVID-19 crisis, which is expected to have a disproportionate impact on SMEs. ICC has been vocal about the urgent need to support SMEs during and after the pandemic. In March, we launched an urgent call for decisive action to 'Save Our SMEs' and combat the economic repercussions of this pandemic. We are continuing to raise awareness of the challenges faced by SMEs with governments and international financial institutions and are providing concrete tools to help them stay in business.

Responding to a crisis for the benefit of all

Uniting our many efforts is ICC's guiding objective in these difficult times to preserve lives and livelihoods. We are committed to enabling effective response efforts to the public health and economic crisis created by COVID-19 as it is happening, and we are intent on shaping a recovery phase that leads to a more resilient global economy and trading system.

We will ensure that our unparalleled network of 45 million businesses worldwide is positioned to help policymakers take decisions based on the best evidence available. And we will ensure that the private sector plays its part in mitigating the global impact of this pandemic.

We do so in keeping with the spirit of ICC's creation more than 100 years ago, when the ravages of the First World War brought businesses together in support of peace, prosperity and opportunity for all. As we look ahead with hope to a 'post-COVID-19' future, that driving purpose remains as important as ever.

State of trade: tension, transition, and turning point

Alexander R. Malaket,
President, OPUS Advisory Services International Inc.;
Chair, ICC Finance for Development Market Intelligence

Trade has been a critically important part of the human experience for thousands of years. It has seen periods of tension, transition and tragedy – at the core of war and colonialism, at the heart of impressive progress in economic inclusion and international development, and recently at the centre of a political posturing and policy that can best be described as controversial.

Additionally, and with some justification, trade faces questions today that have never been levelled at this part of commerce before: questions related to its sustainability in its current form and to the carbon footprint of key components of the physical supply chain, such as the global shipping industry. Relatedly, questions about the importance of supply chain visibility and traceability have come to the forefront of commercial and regulatory dialogue, with increasing responsibility placed upon large global buyers, for the behaviours and actions of their suppliers and extended supply chains.

As we develop content for the 2020 edition of the ICC Global Survey on Trade Finance, the world – including global supply chains – grapples with the tragedy and as yet opaque impact of the COVID-19 crisis.

The Bloomberg New Economy newsletter of 7 March 2020 strikes a note of cautious optimism by noting that "Globalization faces a bend-but-won't-break crisis on coronavirus" – a statement that applies equally well to the state of globalisation linked to trade.

We have seen significant 'bending', and incurred material costs around the world from a spate of tariffs and 'trade wars' that no one can or will 'win', yet the fundamental character of the system remains resilient. Multilateral, rules-based trade continues to be central to the governing of trade flows around the world, despite a slowing of global growth to the range of 3% in 2019.

This temporary moment of tension in the dynamics of trade will normalise as a more thoughtful, strategic and informed approach to policy returns to shape the global discourse and the actions that follow.

In the meantime, the forced, now inevitable, search for alternatives – once it succeeds – will set a much more solid, inclusive and sustainable foundation for the global architecture for trade.

ICC participated in the annual Trade Finance Experts' Group Meeting hosted by the WTO in Geneva in March of this year. This meeting of senior trade leaders from around the world, chaired by WTO Counsellor Marc Auboin and hosted by Deputy Director General Yi, provides a unique forum for a far-reaching update on key initiatives and issues across the industry, as well as substantive dialogue on policy and advocacy priorities.

It was in this context that an underappreciated but important reality of trade today was highlighted: the level of zero-tariff trade concluded on the basis of the WTO's 'Most Favoured Nation' status has never been higher (Figure 1).

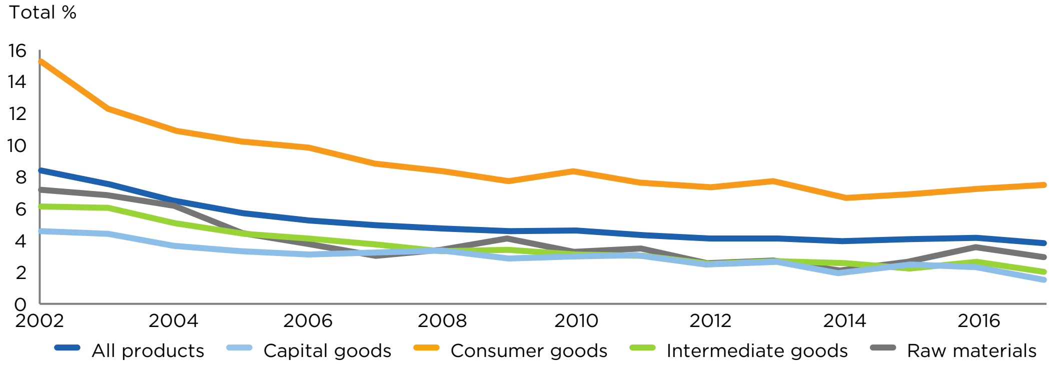
Put another way, despite active, misguided efforts to dismantle a system that has contributed to global growth and prosperity since the post-world war era, the reality is that the core purpose of the multilateral system continues to advance.

Trade works and is continuing to work despite an onslaught of poor decisions, poor policy and absent leadership from those best positioned to advance and magnify its positive effects for the world.

The prevailing geopolitical and policy environment forces a search for alternatives in leadership, in policy and in options for achieving a more balanced, inclusive reality, with trade making an important contribution.

Figure 1

Tariffs applied to the value of imports, by processing stage, world average (2002–2017)



Note: trade-weighted average for effectively applied tariffs.
Source: World Bank, WITS (World Integrated Trade Solution)

We will soon see a period of transition to a 'new normal' in international economics and trade. Just as the G20 occupies a growing position of influence globally as a direct result of its rightly more inclusive nature, this 'new normal' will be characterised by a growing appreciation for the interconnected nature of prosperity, inclusion and security, and will refocus on the necessary growth of multilateral engagement.

As the ICC starts its second century under new leadership, and as the Banking Commission finds its roots in the new Finance for Development Knowledge Centre, we will continue to advocate – clearly, unequivocally and consistently – in support of multilateral engagement, and inclusive, rules-based trade.

This means we will continue to focus on understanding and addressing the global gap in trade financing, while continuing to engage in advocacy through partners like the WTO, the B20/ G20, the United Nations, the Financial Stability Board, the Financial Action Task Force, and the Wolfsberg Group among others.

This includes our traditional areas of work, shaping industry practice, standards and guidance, as well as emerging areas of contribution such as digitisation of trade, supply chain finance (with important partners like BAFT, the ITFA, FCI and EBA among others) regulatory and compliance issues in financial crime, advancing the development of trade finance as an increasingly investable asset class, and a wide range of other important topics.

Business, and trade, can and should be powerful forces for good in the communities and societies in which we thrive. Even the most commercially disciplined, profit-oriented organisations in the world are beginning to recognise that the sands are shifting, with questions around sustainability increasingly at the core of commercial dialogue, and the emerging framework of Economic, Social and Governance (ESG) likewise is increasingly an imperative. Our work around enabling access to trade finance as an element of financial and economic inclusion progresses through critical partnerships with multilateral development banks, including ADB, EBRD and IFC among others, as well as with the Berne Union and its members around the world.

ICC, with our network of National Committees, our more than 45 million members worldwide, and our ecosystem of partners, is uniquely positioned to be a thoughtful voice and a constructive force as we shift from tension to transition to turning point.

Introduction to the Global Survey

The 11th edition of the ICC Global Survey on Trade Finance took place over eight weeks, from February to March 2020, gathering insights from 346 respondents in 85 countries. The Global Survey was conducted by the ICC Banking Commission, in partnership with Boston Consulting Group (BCG), TXF, SWIFT and the Asian Development Bank (ADB). BCG supported with the data collection, aggregation of results and analysis of the survey data. Given the rapidly advancing COVID-19 pandemic, a supplementary survey was conducted to begin to understand the impacts of the pandemic on global trade and trade finance.

The profile of the 346 respondents varies widely, from large multinational banks serving customers around the globe to small local banks with few customers and low trade flows. The diversity of respondents reflects the structure of the trade finance market. The most represented regions in the survey are Western Europe at 32% and Asia Pacific (APAC) at 30% (Figure 3).

Figure 2
What type of bank is your bank?

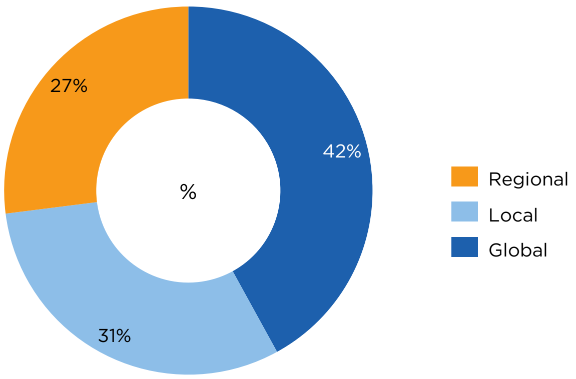
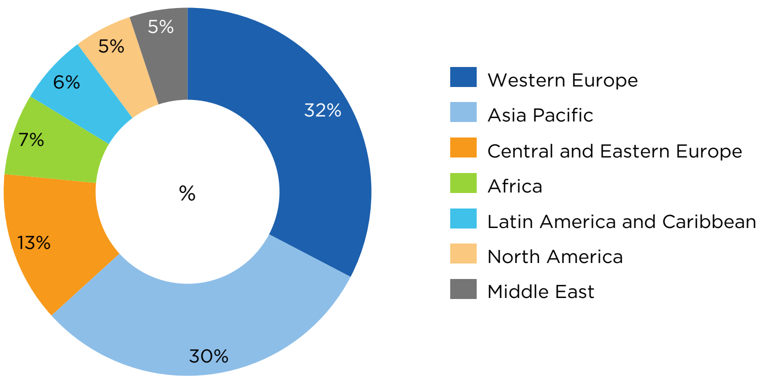
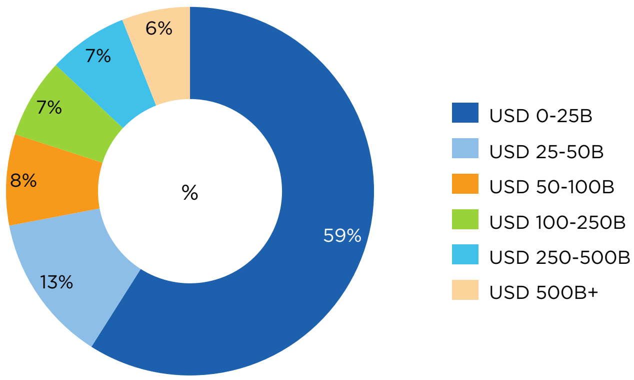


Figure 3
Where is your bank headquartered?



We asked participants to estimate the USD value of all trade finance applications that their banks received last year. The majority (59%) indicated a small-to-medium sized trade finance business of up to USD 25 billion (Figure 4), which is broadly reflective of the dispersed trade finance market around the world. However, respondents also included some large players, with 27% indicating they received at least USD 100 billion in trade finance applications in 2019. This diversity in size and scope provides a rich set of answers and data to draw upon, once again clearly illustrating the representativeness, importance, and reach of the Global Survey.

Figure 4
What was the total USD value of all trade finance applications your bank received in 2019?



Key findings of the Global Survey and the COVID-19 Survey

This year's Global Survey has again provided insights into the trends shaping trade finance, and a fact-based, data-driven view of some of the trade industry's hypotheses on trade. In addition, the short supplementary COVID-19 Survey has allowed us to understand some of the emerging challenges and responses arising from the crisis across the globe.

In summary, the two surveys have provided insights across the following themes:

1. Market outlook on trade finance

- Banks around the world are looking to expand their trade finance business – for our purposes this includes traditional trade finance (TTF) and the various techniques of supply chain finance (SCF) – through various means, including gaining new clients, offering new products, expanding geographically, and increasing digital offerings. In particular, 86% of respondents said that supply chain finance was either an immediate or near-future priority, while 84% answered the same for digital.

- However, concern persists about regulatory and compliance-related obstacles to growing trade finance businesses. These include anti-money laundering (AML) and Know Your Customer (KYC) requirements, and the challenges arising from requirements linked to countering the financing of terrorism (CFT), as well as those related to international sanction regulations.

- Industry practitioners and leaders fully support the policy and regulatory objectives, as well as the overarching need to protect the global financial system from abuse. The issues flagged, however, relate to consequences of regulation that are believed to be unintended, and that directly affect access to trade financing – thus inevitably curtailing trade and impacting economic inclusion and international development.

2. The impact of COVID-19 on trade and trade finance

- Banks from all geographies are already noticing the impact of COVID-19 on trade flows, with most reporting a 0-10% decrease in Q1 2020. Banks expect an even more significant decline in trade flows for the full year, with the majority expecting at least a 20–30% decline from original forecasts, which broadly aligns with both WTO and BCG scenarios.

- Encouragingly, the majority of banks are helping their customers who have been affected by COVID-19, using various measures including extending financing terms and providing more convenient digital (or partly digital) solutions. Some banks have also relaxed their internal policies on original documentation rules, which hopefully is a sign of things to come as the current crisis catalyses and accelerates a significant reduction (perhaps ultimately the elimination) of paper in trade and trade finance transactions. Leading trade banks have

What has ICC done...?

- Leading trade banks have come together under the auspices of the Banking Commission Digitalisation Working Group to **issue a paper** sharing practices adopted in order to enable trade to flow despite pandemic-related difficulties in accessing hard-copies of trade documentation
- The ICC has **issued a call** for governments to quickly enact legislation and measures aimed at advancing digital trade.

come together under the auspices of the Banking Commission Digitalisation Working Group to issue a paper sharing practices adopted in order to enable trade to flow despite pandemic-related difficulties in accessing hard-copies of trade documentation.

- Most banks have not yet seen meaningful support from local authorities to facilitate ongoing trade on digital terms. Requirements persist for original documentation in trade transactions, perhaps unsurprisingly given the speed with which COVID-19 has transformed the commercial landscape.

- The early part of the COVID-19 crisis did not have a systemic impact on the availability of trade financing which, by all reports, remained consistent. However, careful market monitoring by ICC, the WTO, and other key players now suggests emerging system-wide difficulties with USD liquidity, targeted deployment and far tighter controls on trade financing. Deteriorations in credit quality linked to coming bankruptcies are expected to generate a wave of adverse consequences for trade and trade financing. Encouragingly, according to the vast majority of reports, industry standards and practice around the financing of trade have been robust and respected through the crisis to date.

3. Supply chain finance

- Trade banks, particularly those serving global customers, are broadly adopting supply chain finance platforms and expect further growth in this space. However, there is an ongoing divide between global and non-global banks, with 64% of global banks offering SCF platforms, compared to just 13% of local banks and 38% of regional banks.

- This divide is set to continue: global banks expect significant growth in the next five years from SCF, with one-third expecting over 50% growth. In contrast, the majority of local banks expect only 0–15% growth over the same period, which is notable given clear market trends that continue to reflect growth in open account trade as well as in SCF techniques such as payables finance. This significant difference in expected growth rates may reflect differing views around the evolution of the market, or they may be an illustration of limited appetite, expertise or capacity among local banks to significantly advance their SCF propositions.

- Respondents indicate lingering concerns regarding regulation and the ability of smaller banks to enter SCF due to challenges with technology build (e.g. high costs and lack of internal capabilities), although smaller players have overcome these through partnerships and white labelling solutions.

4. Sustainability

- All banks are increasingly recognising the imperative to develop a sustainability strategy, with 67% of respondents stating that they have one. This urgency has primarily been fuelled by concerns related to reputational risk and by fast-growing client expectations.

- There is strong agreement that the environment and climate change should be priorities, with the majority of banks already integrating sustainability risks into credit risk management procedures for clients and conducting sustainability-related due diligence.

- There is a clear desire, however, for more formal guidelines for banks in this area, with 84% of respondents saying they would welcome ICC support in providing sustainability guidelines. The nascent state of these matters, coupled with the wide range of levels of progress on sustainability issues across jurisdictions, including among central banks, adds complexity and urgency to efforts to advance a sustainability agenda globally.

5. Regulation and compliance

- Survey respondents continue to express concern regarding the impacts of existing regulation and compliance policies, with

56% indicating 'significant concern' regarding regulatory requirements.

- The majority of banks expect customer risk due diligence (including sustainability risks) and increased minimum capital requirements to become areas of increased regulatory focus in the coming years.

- Industry stakeholders have reacted positively to the visibility of the BIS in terms of capital requirements as a short-term response to COVID-19; the imperative to balance regulatory efficacy with risk-aligned treatment of trade finance continues to be an area of focus.

6. Digitisation

- While digitisation is widely seen as one of the most important trends to shape trade and trade finance in the coming years, there is a clear divide: while 83% of global banks have a digital strategy, only 46% of local banks report having one.

- This divide exists not only in technology adoption, but also in whether digitisation is considered useful and can reduce costs. While 59% of global banks indicate that digitisation would provide a significant benefit to their operations, just 25% of local and 32% regional banks indicate the same. Furthermore, 90% of global banks expect a reduction in their cost base from the implementation of digital solutions, but only 55% of non-global banks say the same.

- The sharp contrast in expected benefits from digitisation between global banks and regional/ local institutions is instructive, as is the significant difference in benefits expected through cost reduction versus more general, positive business impact. The chasm between global banks and others in recognising a compelling business case tied to digitisation risks driving further consolidation and concentration in trade financing among banks.

7. Financial inclusion

- 73% of survey respondents feel that there is a shortage in servicing the needs of the global market, and the majority believe that there is a role for governments and export credit/ multilateral agencies to help close this gap.

- Most banks reject only a small percentage of trade finance applications, with 62% rejecting between 0–10% of applications in 2019. Micro, small and medium-sized enterprises (MSMEs), and those from Africa and Central/ Eastern Europe, are disproportionately rejected – consistent with the findings from the previous three editions of the Global Survey. The most common reasons cited for rejection are KYC concerns and low-quality applications.

- Digital trade is widely seen as a key enabler to help banks close the trade finance gap, with 55% of survey respondents positioning themselves to service more MSMEs using technology solutions. The challenge is to ensure enough local banks – that often serve these MSMEs – are sufficiently digitally enabled to make it commercially viable to serve the MSME client segment.

MARKET OUTLOOK ON TRADE FINANCE: COVID-19 AND BEYOND

Survey analysis

Since 2000, global trade flows have trebled from USD 6.2 trillion to USD 18.1 trillion in 2019 – growth now widely acknowledged as having been enabled by trade financing, which provides liquidity and risk mitigation solutions for importers and exporters, allowing them to transact with confidence across borders.

The strong growth in trade finance over the past two decades looks set to continue as we enter the 2020s. The 2020 Global Survey indicates that banks continue to see trade finance as a growth area. Across the board, respondents indicated their ambitions to expand their trade finance arrangements to new clients, products and geographies.

The importance of this activity was brought sharply into focus at the peak of the global financial crisis and in the intervening years, where 'real economy' activity like international trade moved to the forefront of the recovery. The priority assigned to transaction banking, including trade financing, within financial institutions was raised in consequence.

Respondents were asked to identify which options they are considering in growing their business (Figure 5). 77% included "transitioning to digital" in their selections (Figure 6). Encouragingly, 61% indicated that they were planning to "expand product offerings", whilst 54% indicated that they will be "expanding their market participation".

Only 3% of respondents answered that their banks were planning to either reduce their product offering or their market participation – demonstrating the optimism many banks have in their trade finance business.

These results are significant for the industry and reiterate the point that trade finance is continuing to evolve. Although the transition to digital has been slower than for other banking products for well-documented reasons, over the coming years this digitisation will materially shape how trade finance works and the types of solutions offered.

Financial Technology firms or Fintechs will continue to expand their involvement in trade financing – likely focused on SCF – over the medium term. This will likely evolve through a combination of direct funding to SMEs and/ or the formation of white-labelled technology partnerships. Continued growth in open account trade and SCF will encourage non-banks to enter the market. The growth trajectory and capacity of non-banks will bear watching over the coming years, particularly in terms of these entities' ability to bring balance sheet capacity to market.

54% of banks mentioned, pre-COVID-19, that they will be expanding their market

Figure 5
Is your bank reconsidering its trade finance business model?

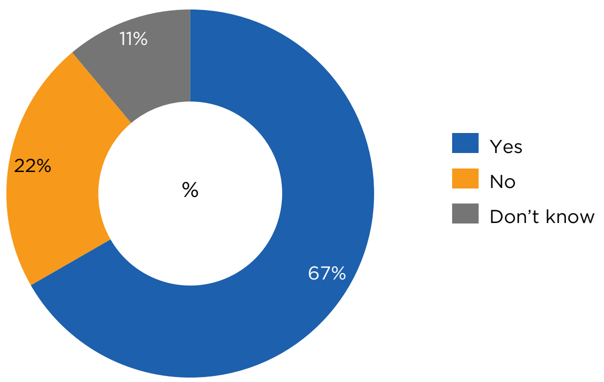
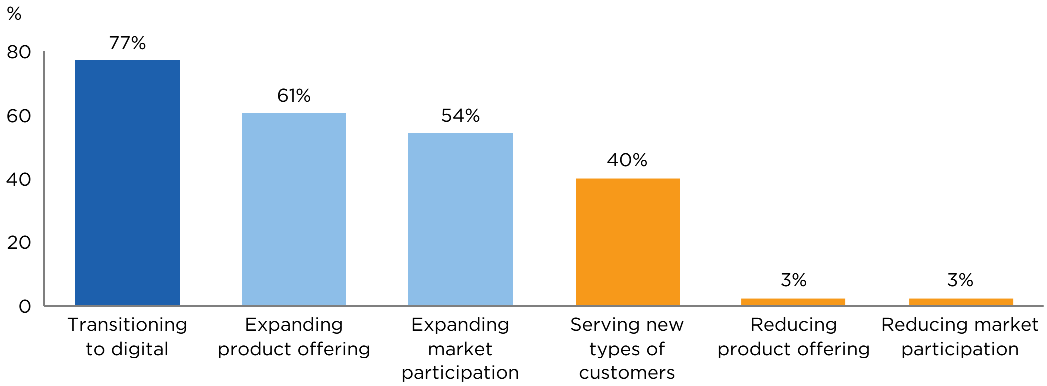


Figure 6
What options are your bank considering for its trade finance model?

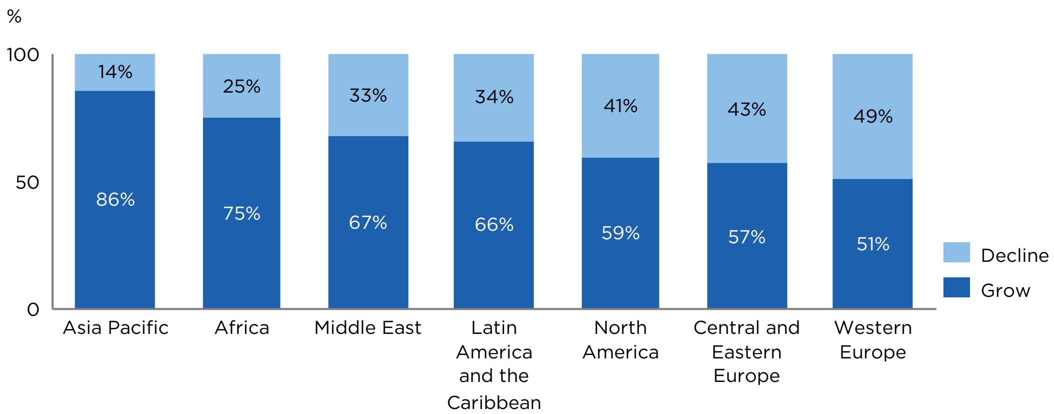


participation despite recent geographical retrenchment and the ongoing reconfiguration of trade corridors. Whether this speaks to a growing desire to target the MSME client segment, or the intention to create net new capacity to underwrite business by distributing trade assets to interested investors, remains to be seen.

When asked about the growth prospects for trade finance by geography, respondents overwhelmingly predicted growth over the coming two years. Growth expectations were positive across the board, with 86% indicating that the demand for trade finance will grow in Asia Pacific (Figure 7), while 75% said the same for Africa. Western Europe saw the biggest split in the survey, with 51% expecting trade finance to grow, and 49% expecting it to decline in the coming years.

Such expectations have been reported despite ongoing and arguably worsening geopolitical and 'trade war' dynamics, at a time when trade has finally, post the 2008 global financial crisis, regained its familiar position as an engine of economic growth. The exact nature and duration of the impact from COVID-19 remains unclear; in particular, the devastating human and economic impact of the virus on the most vulnerable but until now highest-growth markets will demand careful monitoring and has already required crisis-level response from authorities around the globe. There is serious risk that the USD 1.5 trillion annual trade finance gap will be exacerbated by the COVID-19

Figure 7
Will demand for trade financing grow or decline over the next two years (by region)?



crisis. Significant mitigation measures by multilateral development banks, export credit agencies and others are already in progress, but there is much work still to be done.

Asked what they consider to be the priority elements to develop in their trade finance businesses, the vast majority of respondents indicated that traditional trade finance was still an immediate priority for their bank (Figure 8).

While traditional trade finance is the largest source of revenue today, its lead is now only marginal versus open account trade: a shift that is expected to continue over the next few years, even if a short-term, COVID-induced return to traditional mechanisms does materialise.

Despite ongoing market shifts away from traditional trade and trade financing mechanisms, only 53% of respondents indicated that SCF is an immediate priority.

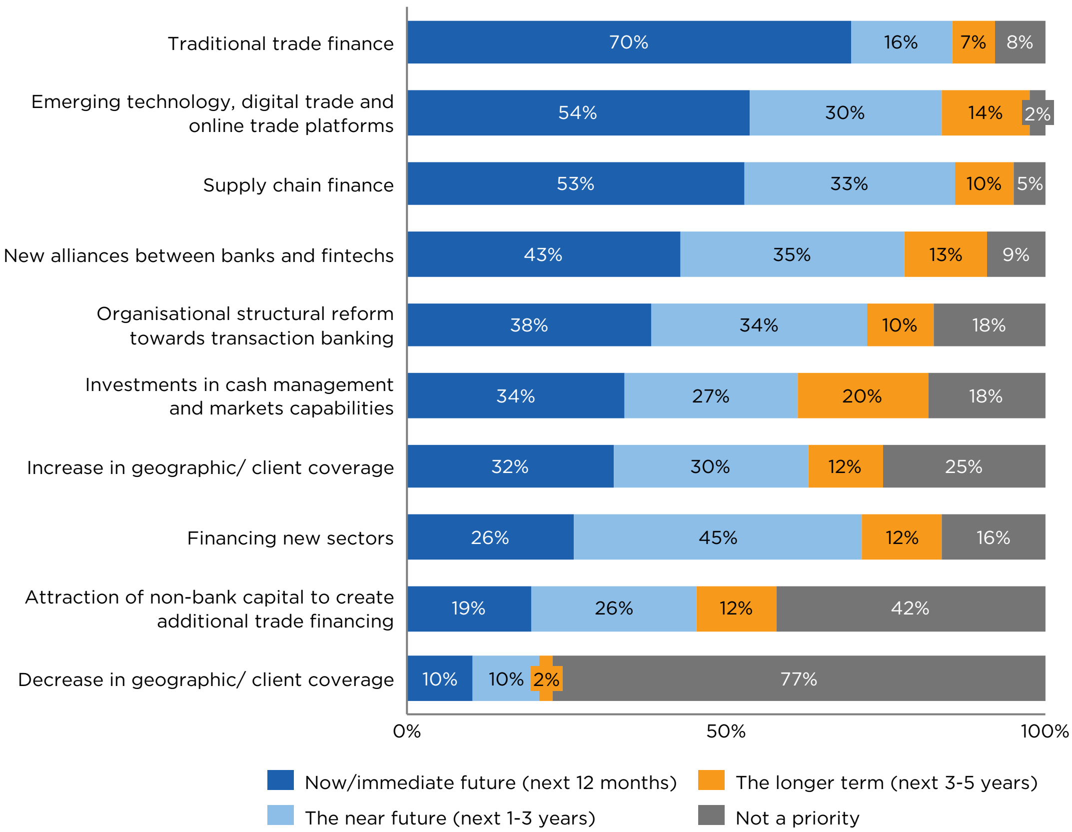
This suggests a disconnect between where banks are focusing and where the market is moving. Whether the gap is bridged by banks shifting their priorities to align with emerging client expectations, or by the entry of more non-banks into the trade financing market, remains to be seen.

84% of participants responded that digital solutions and platforms were either an immediate or near-future priority, confirming the widespread view that trade banks see digitisation as a key market force that will help drive further investment and participation in global trade.

Only 45% of respondents saw attraction of non-bank capital (i.e. asset distribution to third party investors) as a priority area for development. This is worth highlighting given the prevailing interest rate environment, the clear search among asset managers and other capital markets players for attractive investment alternatives, and the ongoing

Figure 8

Please indicate what you consider to be the priority areas of development and strategic focus for your bank



capital cost challenges faced by bank intermediated trade finance. The 'originate to hold' business model persists, as does the interbank asset distribution practice. However, indications are that there is an undercurrent of interest in exploring asset distribution alternatives, enabling technologies and the role of non-bank capital in increasing global trade financing capacity. The ICC has launched a Working Group – Institutional Investors in Trade Finance – to further explore and advance this aspect of the market.

A transition to digital is one of the most prominent themes seen in trade finance over the past few years and was a significant focus of this year's survey. Indeed, 36% of respondents expect either moderate or significant growth in the share of their trade finance business provided through digital ecosystems (Figure 10), rising to 55% for respondents from global banks.

While the vast majority of respondents (92%) indicated that only a minimal proportion of their trade finance business is conducted through Distributed Ledger Technology (DLT) or blockchain (Figure 9), there are indications that the market perceives opportunity in the application of DLT to trade and trade financing, as reflected in several DLT-based multibank consortia in the market. Other commentators, such as the World Economic Forum, have identified trade finance as an area where compelling DLT use cases can and should be developed.

This disparity in expectations and priorities linked to digital trade between global and other banks could be driven by the scale of investments that larger banks have been

Figure 9
What value of trade finance through DLT/ blockchain/ digital ecosystems has your bank provided in 2019?

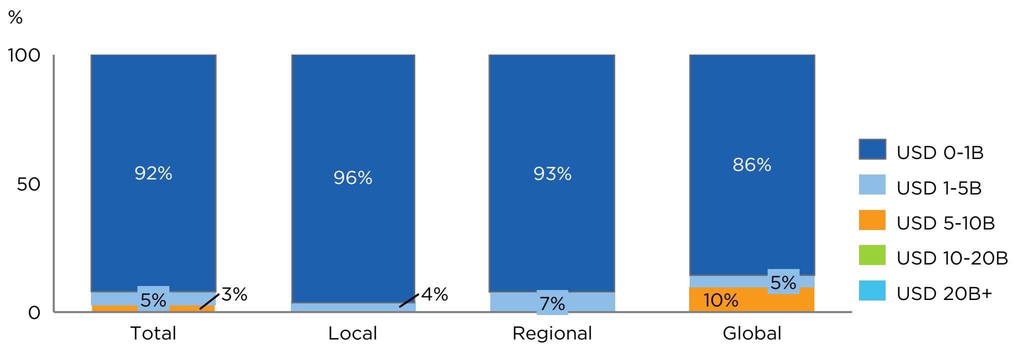
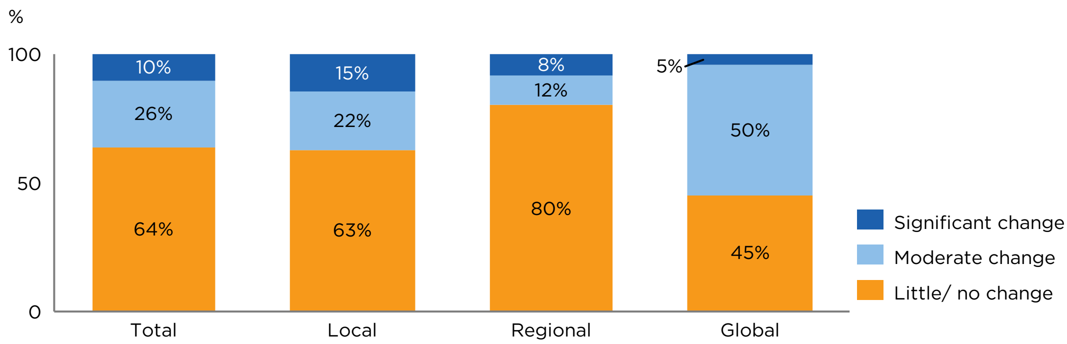


Figure 10
How do you expect this to change for 2020?



able to make in DLT, blockchain and digital ecosystems, and in turn the commitment to making these technologies a key part of the future of trade finance. The evolving imbalance in digital capabilities between global banks and others may lead to further consolidation and concentration in the trade finance market, unless regional and local institutions actively seek to retain their place in the financing of trade. It may also evolve that the rising tide of digitisation lifts all trade banks (and fintechs), as it combines with notions of open networks and complementary partnerships to reorient the landscape in trade financing.

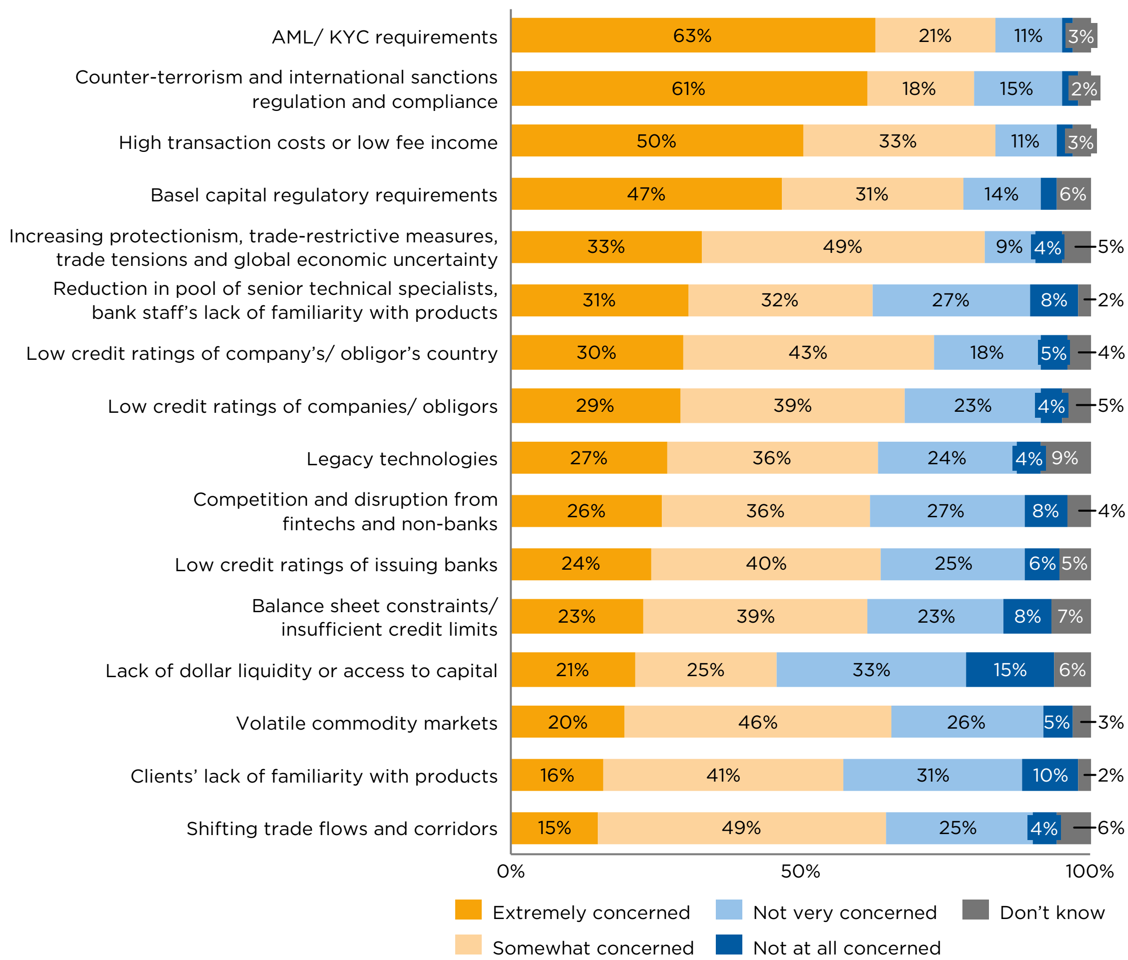
Despite the survey pointing towards future growth and investment in trade finance, concerns persist about ongoing obstacles to expanding the trade finance arrangements of financial institutions. Of particular concern to banks is an increasingly complex and burdensome regulatory regime.

When asked about potential barriers to the growth of trade finance, participating banks overwhelmingly indicated concern about AML/ KYC requirements (with 63% extremely concerned) (Figure 11) and countering the financing of terrorism/ international sanction regulations (with 61% extremely concerned). In past editions of the Global Survey, AML/ KYC requirements have similarly been cited as the top growth-impeding concern of trade banks.

Regulatory and compliance expectations continue to be an overwhelming concern of banks in terms of growth prospects and the ability to generate additional trade financing capacity. The concern is not driven by any fundamental disagreement around

Figure 11

How concerned is your bank about the following potential obstacles?



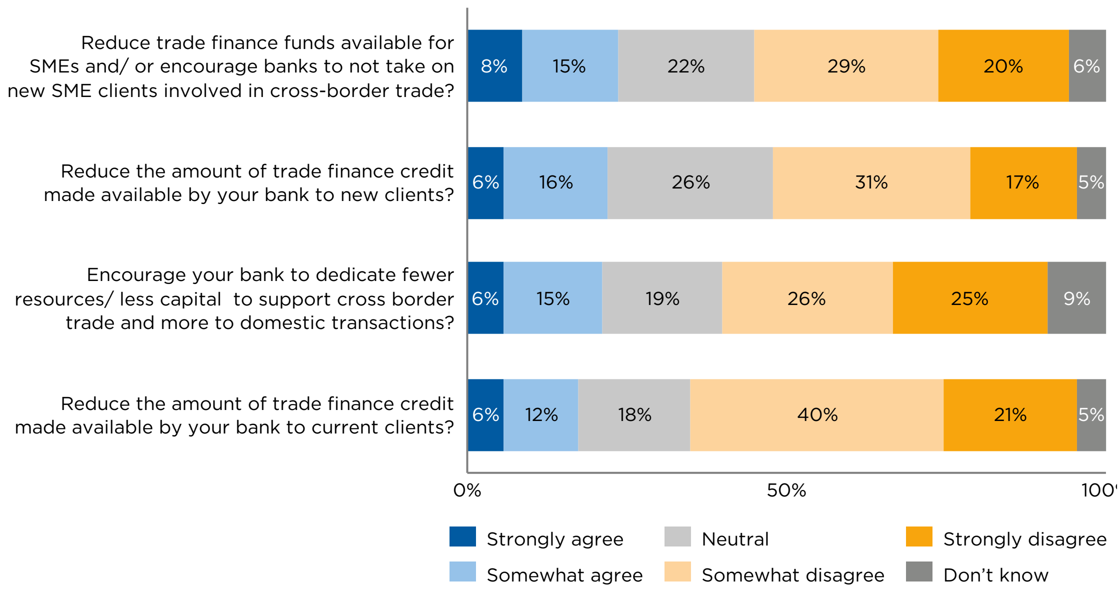
the objectives of regulatory and compliance expectations, but rather around the nature and scope of the role of banks in areas like AML/ CFT and around issues like cross-border inconsistency in regulation, as well as what are believed to be unintended adverse consequences on trade finance through regulation and compliance.

A combination of factors, such as increased feedback from financial intelligence units (FIUs) to industry, the use of enabling technology (Regulatory Technology or RegTech) and, where feasible, greater collaboration between industry and regulatory bodies can help achieve the shared objective of balancing effective regulation with access to trade finance.

Industry collaboration and government support, such as introducing shared KYC libraries and using Legal Entity Identifiers (LEIs) in AML, KYC, and other types of screening, can further help banks manage regulatory requirements. These solutions reduce duplication of effort and the degree of subjectivity in decision making, and they bring validated, verified data into the equation. In addition, projects such as the ADB's Trade Finance Scorecard: Regulation and Market Feedback can help stakeholders better navigate regulatory requirements in different jurisdictions, which have been shown to be a barrier contributing to the trade finance gap.

Looking beyond risk and regulation, 82% of respondents indicated that they were at least somewhat concerned by trade tensions and protectionism (Figure 11), likely driven by an escalation in trade tensions between the US and several jurisdictions, including China. Respondents appeared less concerned by the specific impacts this would have on trade finance (Figure 12). While this may appear counterintuitive given the adverse impact trade tensions have had on actual flows, the view of practitioners may be that tensions will lead to a restructuring of the architecture for trade – including global supply chains and trade corridors – but that trade will ultimately continue and will need to be financed.

Figure 12
To what extent do you agree/ disagree that existing or anticipated trade tensions will:



Talent Management

Over 50% of banks are finding it more challenging to attract trade finance talent in 2019 than in 2018 (Figure 13). The vast majority of banks are recruiting internally (Figure 14), with external sponsorships and initiatives proving less popular.

Attracting and developing the next generation of trade finance practitioners is a challenge that has been the subject of industry discussion for a decade or longer; while consolidation of the trade finance business helped redistribute capacity for a time, the issue is now systemic, it has spawned several industry initiatives including by BAFT, ITFA and the ICC through the Successors in Trade program to attract, train and retain transaction banking and trade finance specialists.

The changing nature of trade finance, and the availability of increasingly robust technology to effect compliance checks, document verification and other operational activities, will inevitably change the skill profile, demographic and character of human resources required to sustain trade financing capabilities in banks and in the wider market. It is also increasingly clear that long-term, incremental 'learn by doing' approaches favoured in trade operations units will not keep pace with the needs of the market, or with the career aspirations and expectations of the next generation of the global labour force.

Figure 13
Compared to 2018, how easy does your bank find it to attract trade finance talent?

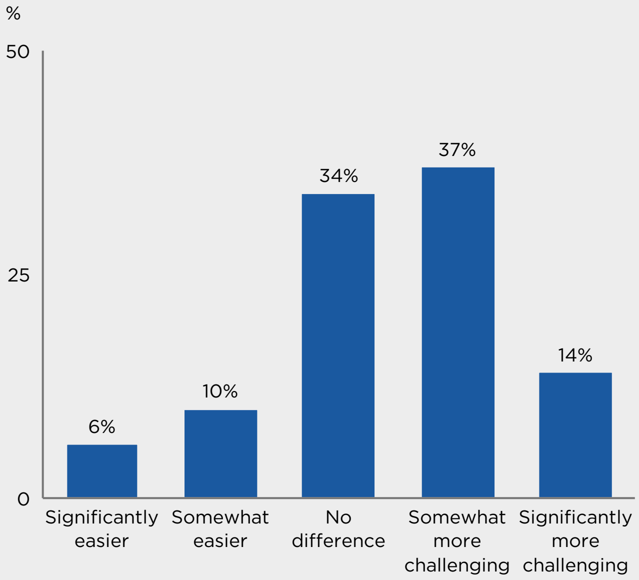
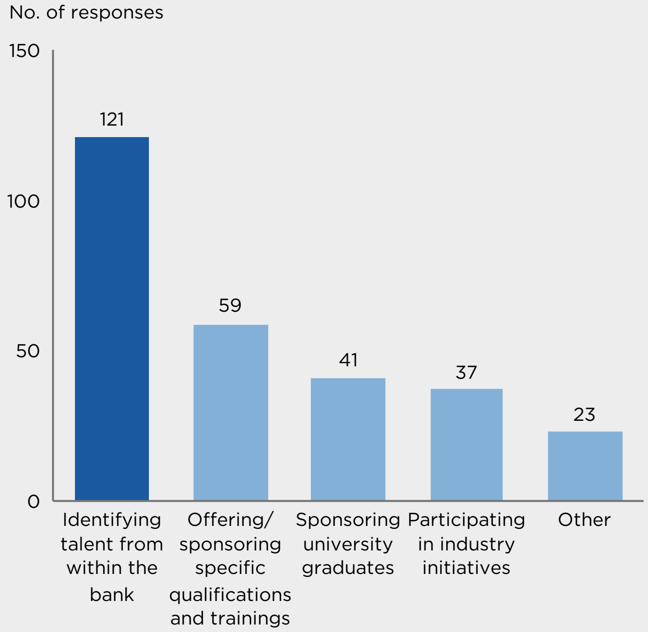


Figure 14
How is your bank attracting a new generation of trade finance staff?



FEATURE

Scenario analysis on the impact of COVID-19 on trade finance

Sukand Ramachandran, Managing Director and Senior Partner, Boston Consulting Group
Ravi Hanspal, Principal, Boston Consulting Group
Noah Mayerson, Associate, Boston Consulting Group

What does COVID-19 mean for international trade and trade finance?

While global trade remained at a near-record high of USD 18.1 trillion in 2019, the onset of the COVID-19 crisis is expected to dramatically impact both the world economy and global trade in the short-to-medium term. The headline-grabbing developments in recent weeks and months – tens of millions unemployed, record falls in stock indices, and unprecedented government intervention – speak to both how profoundly and quickly the virus has challenged the presumed strength of the global economy. And indeed, the positive growth trajectory in global trade over the past decade will doubtlessly be disrupted, as well.

The ultimate impact of COVID-19 on international trade will depend on the scale and duration of the pandemic itself and on the various governmental and policy interventions intended to mitigate the economic crisis. While difficult to predict the precise economic impact of the pandemic, we believe that three scenarios for economic output are plausible, each with different implications for international trade (Figure 15) and trade finance revenues (Figure 16).

Scenario 1: We assume a moderate 3-to-6-month downturn, with a V-shaped recovery into 2021 that sees the global economy quickly return to its pre-crisis growth path. This more optimistic scenario would only likely have been achieved if COVID-19 were brought under control by most major economies by the middle of 2020; given the progress of the pandemic at the time of publishing, this unfortunately no longer seems to be a realistic outcome. In this scenario, we estimate that the fall in global trade for 2020 will be around 11%, and that it will return to its 2019 value by 2021, going on to reach nearly USD 27 trillion by 2028. We would also expect trade finance revenues to drop from USD 46 billion in 2019 to USD 40 billion in 2020 – growing on average at 4.1% per year until 2028.

Scenario 2: We assume a deeper 6-to-9-month downturn with a slower V-shaped recovery (approaching a U shape) into 2021. This implies that by end of Q4 2020, most major economies will have reopened and some form of economic business-as-usual will have returned. We consider this scenario the most likely. In this scenario, we estimate that global trade will decline by 21% in 2020 and only return to its pre-crisis levels in 2024. Given this less bullish scenario, we would expect trade finance revenues to decrease to USD 36 billion – the lowest level in over a decade – subsequently growing by 1.5% per year until 2028.

Scenario 3: In this scenario, we assume a deep widespread shock lasting more than a year with an L-shaped recovery that leaves economic growth at a lower trajectory over the long run. This would become a distinct possibility if COVID-19 (and the associated lockdowns and declines in economic output) persist throughout 2020 and/ or if the virus returns in the winter of 2020/ 2021. If this were the case, we project that international trade will decline by 30% in 2020, rising to just USD 15 trillion by 2028 – far below its pre-crisis value, and approaching levels comparable to those seen at the peak of the 2008 global financial crisis, which was arguably less severe than COVID-19 yet still required over a decade of recovery time.

At the time of publication, the likelihood of second and third waves of COVID-19 is increasingly part of the medical and economic discourse, as is the probability of additional mutations, linked directly to the loosening of restrictions, even controlled degrees of return to work, and the gradual return of travel across local and international borders. The behaviour of pockets of population flaunting physical distancing and limitations on large-group gatherings presents a serious concern. Taken together, these factors present a significant risk that may increase the likelihood of Scenario 3 developing.

This independent analysis largely mirrors the April 2020 projections of the World Trade Organization, which estimated global trade to decline by anywhere from 13% to 32% in 2020.

Implications for trade finance

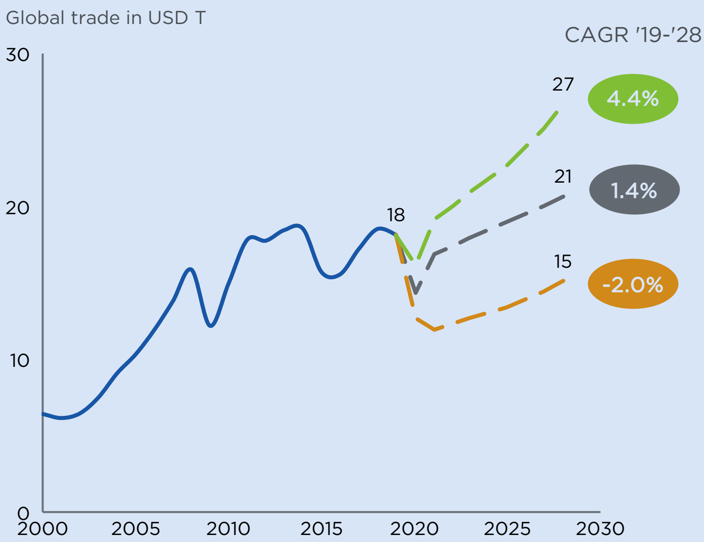
The declines in trade finance revenues projected across the three scenarios are clearly driven in part by a wider slowdown in global trade, which will consequently reduce the demand for trade finance products. However, declines in trade finance revenues will not necessarily directly correlate to declines in the world economy or global trade. Trade finance earnings, particularly from the usage of documentary trade products, have a small element of counter-cyclicality that soften the impact of economic and financial downturns.

As credit quality declines and the global risk environment worsens, it is normal to find that the cost of risk mitigation solutions rises; this will in part counter the anticipated reduction in transaction volumes and will contribute to offsetting declines in trade finance-related revenue.

Products like letters of credit and bank guarantees, which

Figure 15

BCG Trade Finance Model, estimated global trade flows, 2000-2028



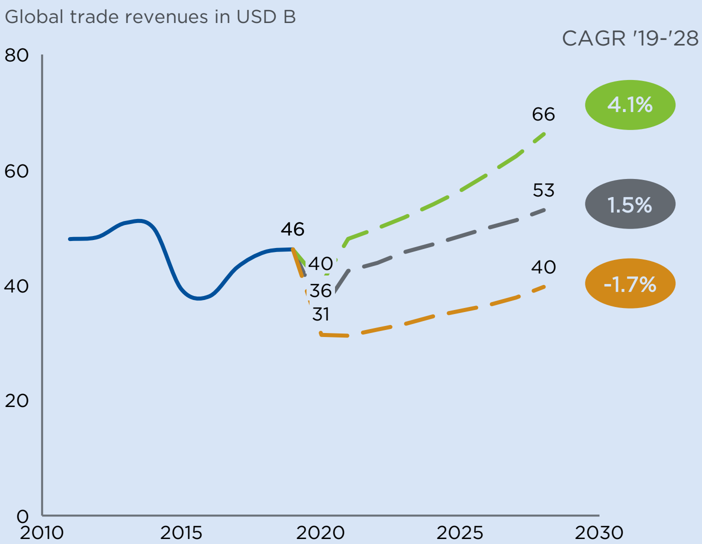
Source: BCG Omnia Global Trade Finance Model 2020

These analyses represent only potential scenarios based on discrete data from one point in time (06 April 2020).

They are not intended as a prediction or forecast, and the situation is changing daily.

Figure 16

BCG Trade Finance Model, estimated global trade finance revenues, 2011-2028

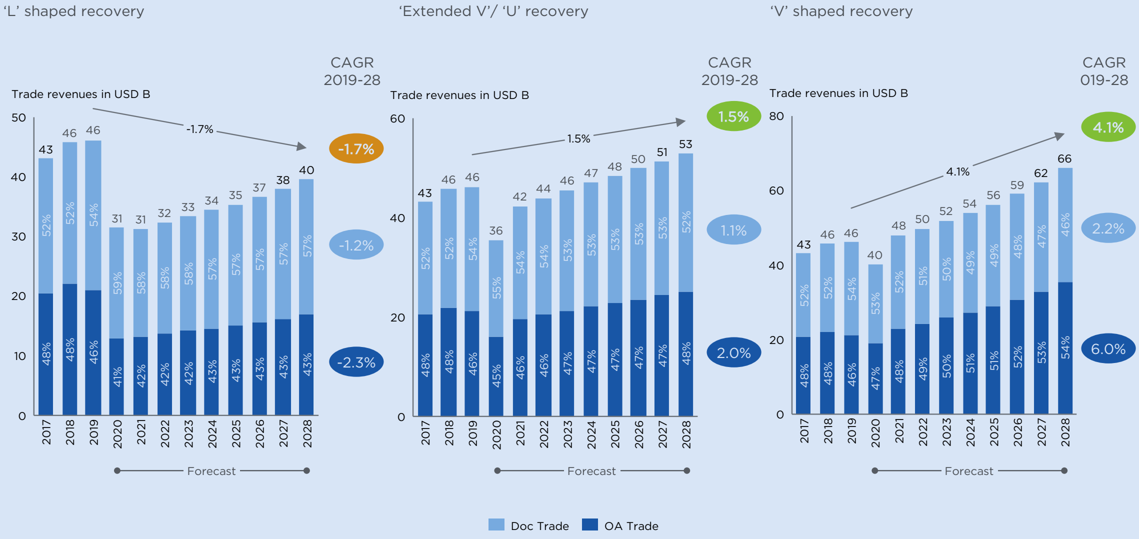


Source: BCG Omnia Global Trade Finance Model 2020

These analyses represent only potential scenarios based on discrete data from one point in time (06 April 2020).

They are not intended as a prediction or forecast, and the situation is changing daily.

Figure 17
BCG Trade Finance Model, estimated share of documentary trade vs. open account, 2011-2028



Source: BCG Omnia Global Trade Finance Model 2020

These analyses represent only potential scenarios based on discrete data from one point in time (06 April 2020). They are not intended as a prediction or forecast, and the situation is changing daily.

command higher margins than open account trade products, will likely grow in popularity given their reputation for risk mitigation. As such, we expect a temporary shift toward documentary trade across the three scenarios, with the shift increasing as the scenarios worsen (Figure 17).

A decline in trade finance revenues and the reduced usage of open account trade products are not the only expected impacts of the pandemic on trade finance. Given the widescale economic disruption we expect a sharp rise in trade finance defaults, especially among SMEs (though we also anticipate that despite this rise, relative to other banking products, trade finance will still be seen as low risk).

Optimistically, the crisis may also help to hasten the shift toward digital solutions in trade. As discussed later in the survey, banks have struggled to navigate a system reliant in part on paper-based documentation in a world under lockdown. Industry and regulators may emerge from the crisis determined to do away with the anachronistic and inefficient system of paper-based trade.

For more information, please see the extended article 'State of the Market' in the ICC Trade Register.

The COVID-19 situation is rapidly evolving, on a daily basis. This article represents a number of scenarios based on discrete data from one point in time (early April 2020). It is not intended as a prediction or forecast about the duration of lockdown, peak of viral infections, efficacy of government or health care responses to the virus, or other health or societal impacts, and it does not represent an 'official' BCG view. It also does not constitute medical, legal or safety advice, and is not a critique, endorsement or recommendation of a particular response. As such, you are advised to use this document as general guidance only in making your own continued assessments as to the appropriate course of action, taking into account local laws, rules, regulations, and orders.

FEATURE

The economic impact of COVID-19 on supply chains

Krishnan Ramadurai, Chair, ICC Trade Register
Ravi Hanspal, Principal, Boston Consulting Group

We would like to acknowledge Zoltan Pozsar and James Sweeney for their original publication 'Covid-19 and Global Dollar Funding', that introduced some of the concepts discussed in this article in the context of COVID-19

As COVID-19 spreads globally and we begin to manage the immediate-term health crisis (ventilator supply, ICU capacity, access to PPE and the like), our attention has increasingly shifted to the economic crisis at hand. Given the global reach of the pandemic, a common topic for thoughtful commercial and policy consideration is the impact on global supply chains, pressured from both 'supply' and 'demand' side challenges.

What will the shutdown of industrial production and services mean for output? What will billions being placed into self-isolation and banned from working, socialising, travelling and, in many ways, spending, do to demand? And, what impact will such shocks have on financial markets, bank lending and global liquidity?

What do we mean by supply chain?

A supply chain is the interconnected transfer of value from one party to another as part of an end-to-end manufacturing process, often across multiple geographical borders, and commonly involving an ecosystem of hundreds, perhaps multiple thousands, of commercial enterprises – domestic or international. At each stage of the supply chain, there is an input, a 'value add', and an output, with the distribution of these varying materials across stages. A prime example is in the electronics industry: the supply chain may start in Asia with intermediate producers in South Korea and Chinese Taipei supplying goods to China, where the final assemblers add their value to the goods and ship them to various destinations such as the US, Europe, South America, or elsewhere in Asia.

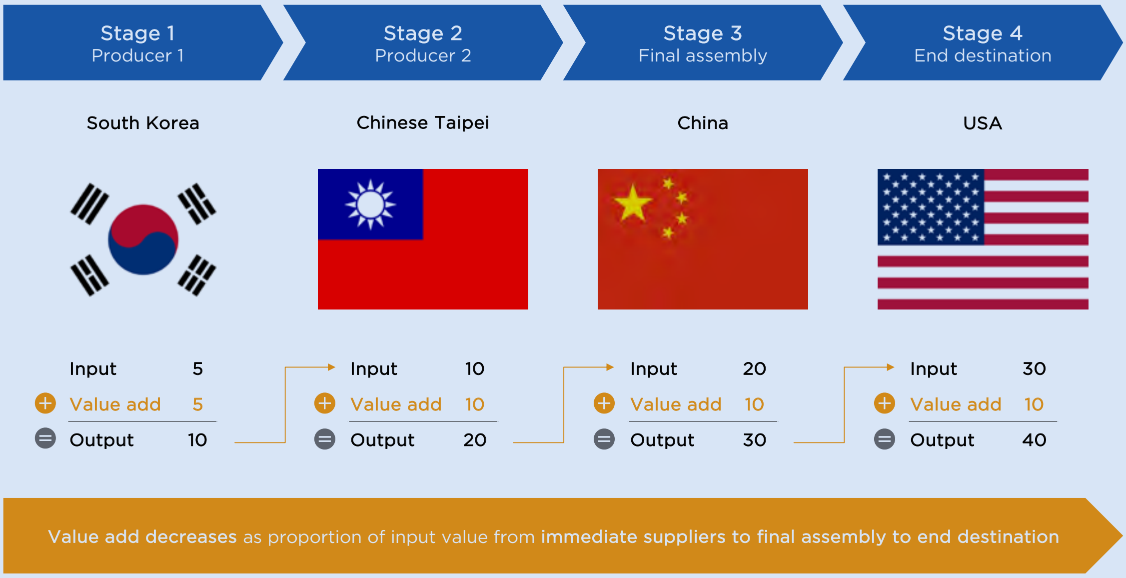
Supply chains are increasingly viewed as being composed of at least three concurrent and complementary layers:

- A physical supply chain, involving the production and movement of goods and services
- A financial supply chain, involving the movement of money, financing and risk mitigation as well as related transfers of ownership, plus the aforementioned value-add
- A data and information supply chain, increasingly powered by technology, such as remote sensors, complex financial and logistics systems and others that can provide extensive, near real-time insight into the state of a transaction and a shipment

To help visualise the transfer of value – which relates directly to payment flows – along the electronics supply chain, we have used a sequential chain (Figure 18), but supply chains can be highly complex in reality, with components commonly crossing the same borders multiple times over the course of a production process.

Fundamentally, goods move from seller to buyer and payments from buyer to seller. If one link 'breaks' – through a stall in output or a stall in payment – the supply chain no longer works, and all players face consequences. As value is added at each stage of the production process, the health of the financial supply chain becomes increasingly critical to completion and delivery, driving demand for a range of trade financing solutions aimed at mitigating risk and ensuring adequate cash flow and working capital in the supply chain. Trade finance is, in this way, the oil in the engine of global commerce.

Figure 18
Sample electronics supply chain



What is the impact of COVID-19 on supply?

On the supply side, COVID-19 first truly hit supply chains by the mandated shutdown of production capacity in China, which was soon replicated across the world.

As production shuts down and disables critical components of the supply chain, gaps turn into problems. Inventories of raw materials and finished goods build up, and staff are laid off. Transport and logistics start to seize-up, compounding the problem by slowing down any limited remaining production and delivery capacity.

Soon, with no goods coming in or out, payments are delayed and missed along the supply chain. Delayed or missed payments will mean that intermediate suppliers will need to meet wages, fixed overheads such as rent, and debt servicing costs from either internal cash reserves or by drawing-down on bank credit lines. Alternatively, they may be able to extend payment terms to their suppliers, but this effectively means transferring the risks down the supply chain. The ability to extend payment terms is a function of the bargaining power the buyer can exercise over the seller. Suppliers down the supply chain will typically be squeezed the most. The impact will be disproportionate, as small and medium enterprises far down the supply chain will have the least bargaining power or external funding options and will also feel the cash flow strains quicker than large corporates.

Although trade finance practitioners are increasingly working to solve the 'last mile' financing challenge in international supply chains, and although payables finance programs can offset some of the adverse cash flow impact of extended payment terms, such programs are most commonly available to larger suppliers collectively representing the most significant 'spend' by the buyer. Small suppliers that are considered strategic to the smooth functioning of a supply chain may be the exception, as well those with unique product characteristics or intellectual property that cannot be easily replaced. This dynamic contributes to the reasons why payables finance programs must be appropriately structured, managed and reported upon, and must be thoughtfully deployed across international supply chains. The COVID-19 crisis has provided stark illustrations of supply chain vulnerability in medical equipment and agri-food, among others, with multilateral institutions having to step in quickly and decisively to shore up critical supply chains.

The susceptibility of a specific supply chain will vary depending on five key factors:

- **Industry:** The complexity of supply chains varies materially by industry. The automotive, electronics and telecommunication industries rely on many different component manufacturers, and their end production is dependent on all of these coming together seamlessly. In addition, these industries often are geographically concentrated, with a large proportion of manufacturing in China. The combination of China as an anchor to many global supply chains, and the same country being the source (though no longer the epicentre) of the pandemic outbreak, has directly shaped the impact of COVID-19 on trade flows, and has amplified calls for more agile (and in some cases, reconfigured) supply chains that had been loudly heard in the context of pre-COVID-19 trade war rhetoric. Certain firms are known to actively counter the trend in automotive supply chains: fewer but more intelligent parts, and fewer suppliers, mean that the overall supply chain is simpler and easier to manage.

- **Terms of trade:** The greater the disparity in bargaining power between buyers and sellers, and the smaller the concentration of buyers to suppliers (or vice versa), the less resilient the supply chain will be. The Japanese earthquake and tsunami in 2011 exposed the dependence of Japanese car manufacturers on OEM suppliers to their factories located in the US, as well as the critical importance of a particular Japanese supplier to a US technology giant's supply chain and production capability.

- **Value addition:** Supply chains characterised by higher value addition at each stage will be impacted more than supply chains where value addition is modest or incremental, as the risk is less concentrated in the latter scenario. The garment sector will typically experience a more muted impact than sectors such as electronics and automotive. This is because intermediates depend more heavily on payments flowing through these high value-added supply chains, and therefore experience more immediate and adverse impact in the event of a disruption in payment flows.

- **Supply chain strategy:** As supply chains have become leaner and leaner, there has been less and less slack in the system: fewer resources on standby, less contingency stock, no more buffers in delivery timelines. While this can cut costs, it also means that at times of disruption, impacts are seen immediately and may become more difficult to address, as has been observed during the COVID-19 crisis. As a result, some of the most tightly operated supply chains may be the first to face trouble.

- **Leverage:** As supply chain finance (specifically payables finance) has grown in popularity, supply chains have become increasingly leveraged. As a result, individual firms within the ecosystem have become less disciplined in maintaining their own healthy working capital, resulting in potentially smaller cash reserves at a time of crisis.

What will happen to demand?

Inevitably, supply-side shocks are being accompanied by demand-side shocks caused by widespread production and service sector shutdowns, coupled with lockdowns restricting the movement – and ability to work – of billions of people, goods, and services. Consequently, discretionary consumer spending is likely to collapse.

This will be further exacerbated by the fall in financial markets and the 'dash for cash' as reflected in the indiscriminate selling of financial assets, which results in declining household wealth and falling consumption. Even households not directly impacted will become cautious – with growing uncertainty over jobs, investments, and pensions – translating into less spending.

Understandably, the decline in demand will be felt most acutely in sectors such as travel, and in some areas of the services sector, due to the direct impact of forced shutdowns and border closures. Given the increasing importance of the services sector and its contribution to country GDPs, the fall in demand will have an adverse knock-on impact on reported GDP numbers.

This will no doubt be accompanied by a decrease in demand for goods as the drop in the service and travel sectors ripple across supply chains such as those for food and beverages for bars, restaurants, and hotels, fuel for aviation, and many others. This will be amplified as consumers delay major purchases and travel, local commutes reduce drastically due to lockdown, and businesses – even entire sectors – face a difficult recovery post-lockdown.

At an institutional level, this decline in demand can quickly translate into falling revenues and forced extension of payment terms for suppliers. When coupled with the need to meet fixed costs, pay wages, and service debt, internal cash flows can come under strain, resulting in drawdowns of credit lines at banks – just as we are seeing from the shutdown in supply.

The devastating demand-side and supply-side impacts of COVID-19 build upon each other and reinforce a cycle of crisis as each side of the market wrestles with existential risk in an environment with perhaps no parallel from which to draw helpful lessons and insight.

What does this mean for businesses financially?

As discussed, at an institutional level a shock in supply and demand will translate into missed and delayed payments. If these missed and delayed payments accumulate, and are overlaid with a need to meet salaries, fixed costs and debt payments, then internal cash flows are likely to come under substantial strain. Institutions will have two choices: either they extend payment terms to their suppliers, or draw down available credit lines from banks.

While drawdown of bank credit lines is essentially a function of a bank's assessment of an institution's ability and willingness to repay loans and the bank's appetite to take on more risk exposure, the ability to extend payment terms is a function of the terms of trade and the bargaining power the corporate has over its suppliers.

Looking back at our example from the electronics industry, intermediate suppliers in Korea, Chinese Taipei and final assemblers in China could lean on big technology companies with large cash surpluses for early payment or direct cash funding. We are already seeing some firms accelerating payments to European suppliers, paying them within 15 days. While this will provide some back-stop relief for suppliers, this is not a permanent solution.

With capital markets in a swoon, accessing the commercial paper, bond and equity markets would no longer be a viable option for large and medium-sized corporates under normal circumstances. In addition, SMEs that are typically wholly reliant on banks would also find themselves in a 'no win' situation, assuming banks would want to limit exposures. As such, the crisis calls for extraordinary measures and government intervention to ensure that credit continues to flow and support real economic activity – which is exactly what is happening.

Indeed, in the US the Treasury Department and Federal Reserve have launched a series of financing programmes under the new CARES Act (Coronavirus Aid, Relief, and Economic Security Act), including the Primary Market Corporate Credit Facility and Main Street Business Lending Program. Similar programmes are seen elsewhere, including CBILS (Coronavirus Interruption Business Loans Scheme) in the UK to provide government-backed lending to small businesses.

What does this mean for the banking system?

A key obvious risk for the banking system in such a crisis is the likelihood of increased defaults, as the health of corporates and small businesses starts to deteriorate, and they can no longer service their debt. While this may be, in part, softened by government intervention, the majority of government programmes are focused around providing and backing new lending – but not necessarily preventing default on existing facilities.

However, an additional key risk to consider – particularly around the theme of supply chains – is liquidity. As USD is the major invoicing currency for global trade in goods and services, the risks at a bank level are essentially related to USD funding and the ability for banks to provide this funding.

As supply-side shocks intertwine with demand-side shocks, corporates will draw down internal cash surpluses in the first instance, and credit lines in local currency (LCY) and foreign currency (FCY). While LCY funding should not be a major issue (central banks can print local currency to meet any sharp increase in demand), banks will need to fund USD loans from their stock of USD deposits. For banks that are structurally short on USD, they will need to borrow in the inter-bank market from USD surplus banks which often tend to be the US banks. In addition, countries under US sanctions will face amplified issues due to restricted access to USD funding.

As corporate USD cash surpluses in banks gets drawn down there is a knock-on impact for banks, which puts pressure on their Liquidity Coverage Ratios (LCR), as these withdrawals raise the denominator of the LCR ratio, forcing banks to increase their stock of high-quality liquid assets (HQLA), the numerator of the LCR ratio. The ability to reduce outflows for banks in this situation is limited.

The inter-bank market is a source of liquidity in good times. However, as liquidity is fragile in a crisis, it can act only as a temporary backstop, and banks needing USD funding on a continuous basis will need to get their funding from alternative sources. These alternatives, using our stylised example of the electronics industry, will be the local Taiwanese and South Korean banks, that will fill the gap left by the Japanese banks, which are the traditional lenders of USD in the electronics supply chain.

This switch in funding sources has the potential to redistribute cross-currency funding pressures from a USD/ Yen basis, USD/ Korean Won basis or USD/ Taiwanese Dollar basis. The knock-on impact of these pressures will flow through in the earnings of these banks, as banks in South Korea and Chinese Taipei cannot raise USD as cheaply as the Japanese banks.

Given that Japan, South Korea and Chinese Taipei dominate the 'value add' share of the electronics supply chain that runs through China, USD liquidity will be more at risk in these geographies than in China. If the cascade of requests to draw down credit lines and in particular USD loans becomes a systemic issue, then it can translate into a depletion of USD reserves at local central banks and in turn drain excess reserves at the US Federal Reserve.

Using China as an example, in the case that local banks are swamped with a drawdown of USD deposits their natural port of call will be the People's Bank of China. In turn, the Chinese central bank – as it keeps a part of its FX reserves in FX swaps where they lend USD in exchange for Euros and Yen – will now need to flip this around and unwind these swaps, effectively becoming USD borrowers rather than lenders. This means dealers in London and Hong Kong will need to find alternative sources of USD to match their books. As in normal times most of these dollars were used to fund carry trades, this switch has the potential to transmit local imbalances globally.

In the unlikely event the Chinese central bank exhausts its dollar liquidity in cash markets like the FX market described above, then the bank will either repo or sell its treasury portfolio to fund the dollars required. The central bank will, however, not approach the US Federal Reserve to tap swap lines as, unlike several other central banks (e.g. Japan, UK, Europe and Switzerland), the Chinese central bank does not have swap lines with them.

In essence, a cascade of USD drawdowns has the potential to create stress in USD liquidity:

- In peripheral cross-currency markets (e.g. TWD/ USD) as missed payments grow
- In EUR/ USD and USD/ Yen currency markets as reserve managers stop lending in the FX swap market to help their local banks and the banking system deal with USD outflows in their jurisdictions
- Insofar as USD Libor-OIS spreads grow, as banks start to remedy their LCR ratios to counter the outflow of operational deposits and the drawdown of credit lines

Concluding thoughts – selected policy considerations

This brings to mind a number of considerations for potential policy interventions:

- Expand USD swap lines to countries currently with no access to these swap lines. This effectively means going beyond the 14 countries that currently have access to these swap lines.
- Multilateral Banks raise USD funding from Global Capital Markets which can then be used as a source of liquidity to fund Trade Transactions through targeted lending programmes.
- Relax LCR and Net Stable Funding Ratio (NSFR) with a view toward channelling USD liquidity to where it is needed most.

COVID-19 Survey analysis

The optimistic results from the Global Survey demonstrate a clear desire by banks to grow their trade finance businesses, reflecting an underlying confidence in commercial prospects, trade flows, and general geopolitical stability. However, many respondents completed the survey before COVID-19 moved from a localised threat in China and South East Asia to a global pandemic. As a result, we expect sentiment toward trade finance to be more cautious in the short-to-medium term.

To supplement the Global Survey, the ICC Banking Commission launched a short additional survey specifically aimed at understanding the initial impact of COVID-19 on trade finance. The findings reflect market views as at early April 2020.

The COVID-19 Survey had 233 respondents, and the participating bank profile was somewhat different from that of the Global Survey, with 49% from local, 28% from regional, and 23% from global banks (Figure 19). The largest number of responses were received from banks headquartered in Central and Eastern Europe (39%), Western Europe (20%) and Asia Pacific (17%) (Figure 20).

Responses across geographies and bank types were broadly similar, except where highlighted otherwise.

Overall, banks from all geographies are already noticing the impact of COVID-19 on trade flows, with 34% suffering a 0-10% drop in trade flows versus expectations in Q1 (Figure 21). A further 37% indicated that their trade flows declined from 10-30% in Q1. Only 16% of banks suffered greater than a 30%

Figure 19
What type of bank is your bank?

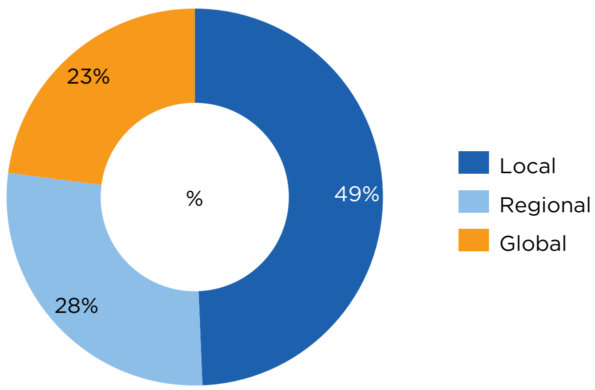
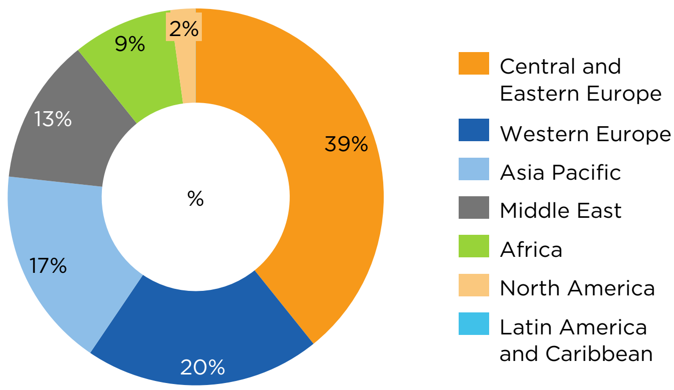


Figure 20
Where is your bank headquartered?

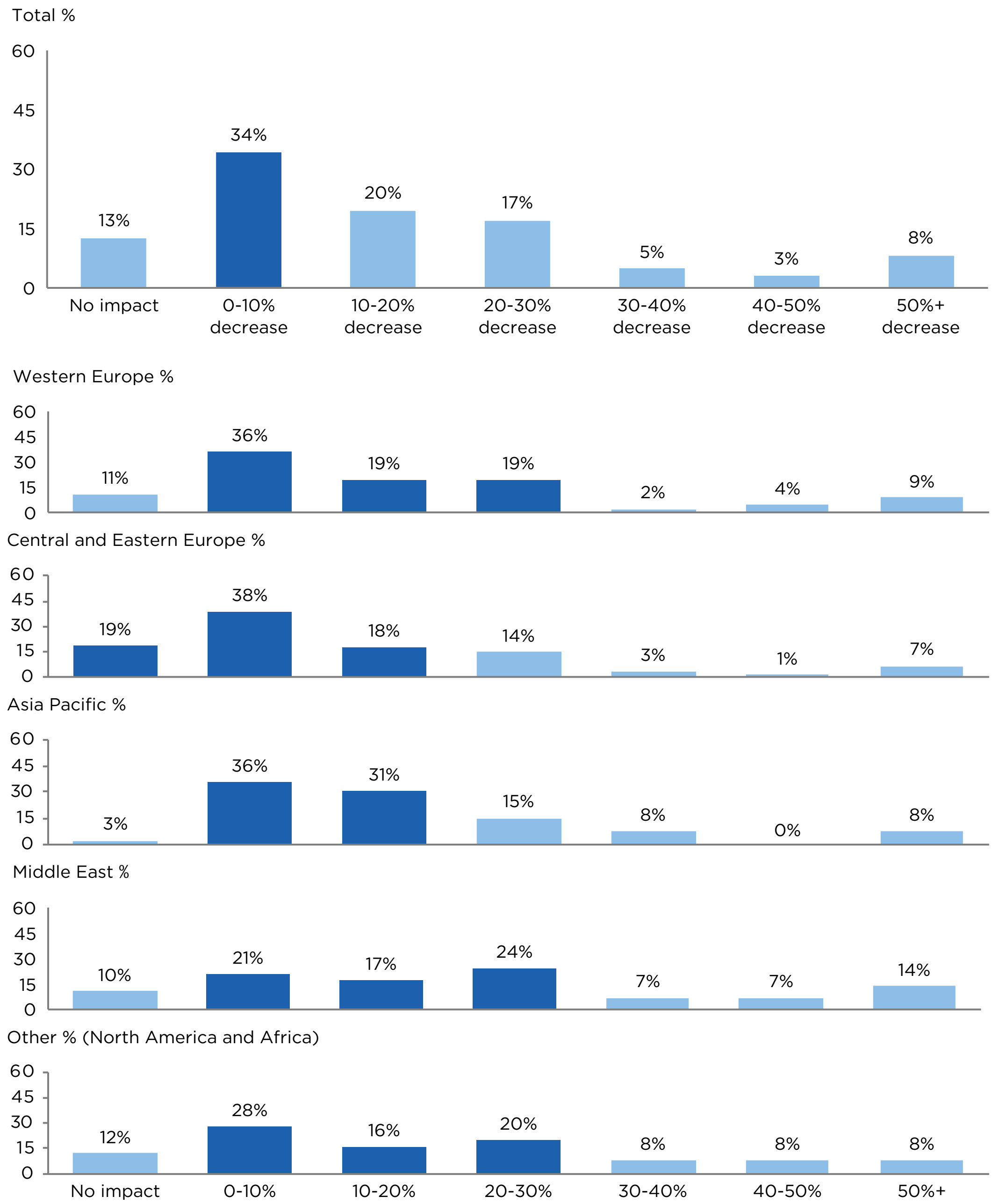


decrease, although this may be because the impact on trade in most markets was more subtle towards the beginning of the quarter.

Results did not diverge materially across markets or categories of banks responding to the survey. Even in APAC, where the impact on trade flows might reasonably have been expected to be worse given proximity to China, 36% reported only a 0-10% decrease in Q1 trade flows.

Looking ahead to the rest of 2020, banks expect a more significant impact on trade flows as COVID-19 continues to shut down economies, reduce consumer spending, and bring businesses of all sizes to the brink. In 2020, 28% of banks expect a 20-30% hit to the trade flows they support (Figure 22), a further 25% anticipate a 10-20% reduction, and 15% expect a 30-40% decrease. This largely dovetails with the projected impact on global trade flows outlined above (Figure

Figure 21
How has COVID-19 impacted your Q1 trade flows versus expectations?



15) from BCG's Trade Finance Model, which estimated an 11-30% decrease in global trade flows as a result of COVID-19 across three different scenarios. Assessment from the WTO (April 2020) suggests a COVID-related reduction of trade flows in the range of 13-32%.

Across regions, the results are largely similar, except for the Middle East where 24% of respondents expect a decrease of 50% or more in 2020 trade flows (and a further 20% expect a 30-50% reduction). The view from the Middle East is likely influenced by the state of oil prices and petroleum exports, as a region heavily dependent on oil exports is seeing oil prices and volumes drop to some of the lowest levels in recent memory, for reasons only partly related to COVID-19.

Respondents indicated that a range of geographies and commodities are expected

Figure 22

What does your bank anticipate to be the COVID-19 impact on 2020 trade flows?

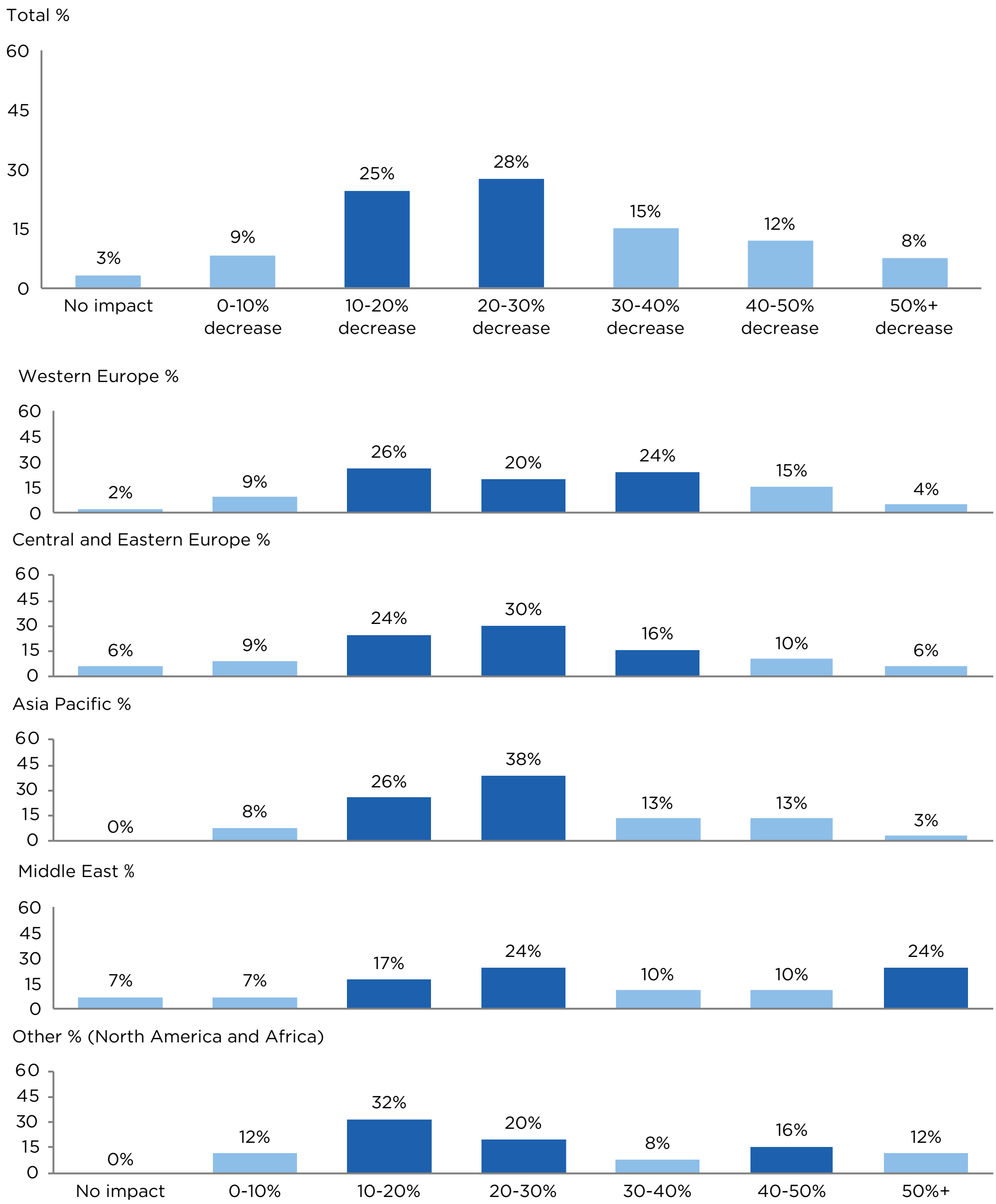
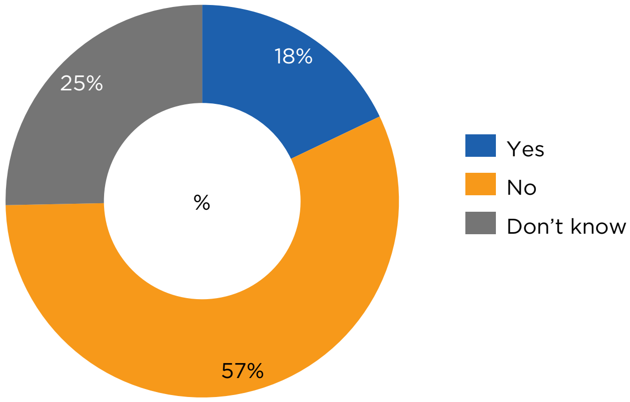


Figure 23
Have you seen any noticeable rise in trade finance defaults owing to COVID-19?



to be impacted by COVID-19. However, retail, travel and tourism (including airlines and hotels), automotive, and, in particular, oil, were cited by many respondents as the most likely sectors to see significant disruption.

We also asked banks if they have seen any noticeable rise in trade finance defaults as a result of COVID-19. As of early April, 57% of respondents had not witnessed an increase in defaults, while only 18% reported that they had observed an increase in defaults (Figure 23).

It is, however, too early in the crisis to properly assess the resulting default situation. Several factors must be taken into account:

- The tenor of traditional trade finance, as well as the maturity timeframes for techniques like payables finance, often exceed 90 days; instances of default, if they arise, would not yet have been discovered.
- Default status may be reached by crossing a timeframe defined by regulatory standards and may therefore be reached as a 'technical' default without reflecting commercial or transactional reality.
- Measures aimed at mitigating the adverse effects of the COVID-19 crisis are under assessment and consideration, and may include, as a matter of government and public policy, the creation of temporary loan extension or forgiveness measures.
- Trade obligations, particularly those related to strategically important flows like agri-food, commodities, defence spending and others, have tended to be given priority in settlement. Such action may prevent technical or even probable defaults from occurring in the end.

Industry leaders and ICC will carefully monitor the evolving state of trade obligations as a critical element of managing the COVID-19 crisis and will work to proactively devise mitigation strategies with authorities where appropriate. It will be difficult to avoid a global, systemic liquidity crisis. The key will be the nature, decisiveness and speed of a coordinated response across jurisdictions, and in this context, multilateralism will again demonstrate its value despite its acknowledged imperfections. Further, the ICC Trade Register will play an important role in providing robust data, analysis and advocacy as the default picture takes shape.

Given the sharp decline in trade flows anticipated by the responding banks, it is more important than ever that both financial institutions and public bodies think creatively to help facilitate global trade and mitigate any barriers created by COVID-19. However, the Survey reveals mixed perceptions in this area, with individual banks taking the lead on implementing new measures and solutions to support their customers, while other key players in the trade ecosystem may need to accelerate their response to the crisis.

As with the global financial crisis of 2008, international bodies, multilateral development banks, and some export credit agencies have responded quickly. Equally encouragingly, the Basel Committee promptly provided direction aimed at reducing capital pressure. Other agencies of public and international policy are understandably preoccupied with urgent health and public safety priorities; the ICC and industry partners are working judiciously to ensure that messages related to the importance of trade and trade finance, the imperative to support SMEs, and the urgent need to safely reopen the global economy are thoughtfully communicated.

When we asked responding banks if they have implemented any measures to support their customers through the COVID-19 crisis, 72% – across the various bank profiles – indicated that their banks have done so (Figure 24). Dozens of respondents indicated that they were extending financing terms such as loan maturity dates and repayment schedules.

Many also indicated that their banks had stopped collecting interest on their trade finance facilities for periods extending out to nine months and had stopped charging customers bank fees. A few respondents credited their central banks with the deployment of new policies and programs aimed at supporting business, with such measures seen as providing important additional impetus to the initiatives taken by the banking sector.

In terms of customer uptake of these measures, many respondents noted that, while early, customers have responded quite positively. One respondent noted that the "demand to structure loans was high," while another said that "customers have responded very favourably and with appreciation" to the new measures. However, one bank respondent mentioned that they had seen "more requests for Confirmation of L/Cs from exporters who normally didn't [request them] before the crisis". This is not unexpected, and reflects the reality that risk is a function of both objective fact and perception. Such an observation also highlights why trade finance techniques and mechanisms have proven their mettle over hundreds of years, enabling trade to flow securely even under the most challenging conditions.

A key question, however, is to what extent will these measures suffice in the medium term? Trade banks are accustomed to trade finance being a low-risk product. However, should the risk dynamics of trade be completely overturned as importers' and exporters' cash reserves are depleted amid the COVID-19 crisis, more substantial intervention will be required, including government grants and growth in government-backed export credit agency funding. Should a worse-case crisis scenario develop, concerns will reach across jurisdictions and the global financial and economic system and will demand coordinated mitigation measures. In such an eventuality, the advocacy dimension of ICC's work, and ICC's unique, trusted, and authoritative position with organisations like

Figure 24
Has your bank put in place any measures to support customers impacted by COVID-19?

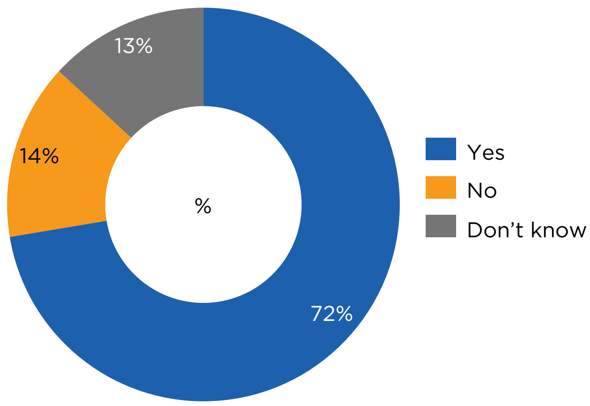


Figure 25

Has your bank rolled out any new digital solutions specifically to mitigate the disruption caused by COVID-19?

the UN, the WTO, the G20 and others will be brought sharply into focus.

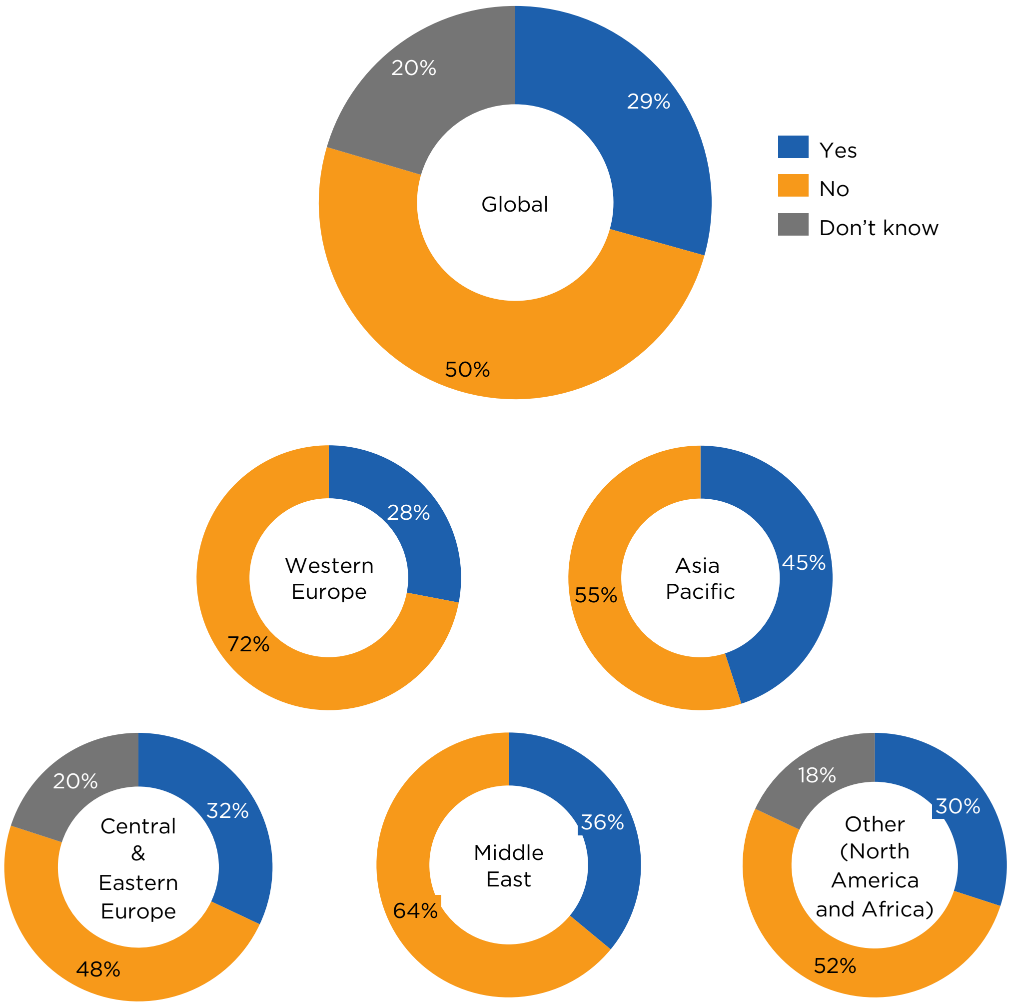
ICC has already responded with unprecedented speed in developing communications, tools and program recommendations in the context of COVID-19 and continues to work on such initiatives, including in support of trade and trade financing.

Concerns around the impact of COVID-19 on trade finance are not limited to credit risk, but also operational feasibility, for example the transfer of critical legal documents. To this point, we are aware of various cases where goods are ready to export but securing a letter of credit has not been possible due to 'lockdown' restrictions impacting carriers, bank branches, and the like.

In light of this, 54% of respondents said that their banks had introduced new digital solutions to mitigate any disruption caused by COVID-19 (Figure 25). Notably, in Asia Pacific, the original epicentre for COVID-19, 62% of respondents indicated that their banks have not introduced any digital solutions, the lowest of all regions surveyed.

Taken holistically, the cases where operational and transactional challenges in trade finance have impeded the flow of trade have been limited in number, again illustrating the

Figure 26
Has your local authority/ government provided any regulatory support to your bank to facilitate ongoing trade?



ability of trade finance providers to respond relatively well in times of crisis. Whether this remains the case as COVID-19 evolves is to be determined. Technology and digitisation will play a crucial part in ensuring access to timely and sufficient trade finance at this time.

In addition to more general usage of online platforms and services for day-to-day tasks, many respondents indicated that their banks have relaxed existing rules on the need for original documentation, for example by allowing scanned documents and other e-documents, and have rolled out new rules and platforms to enable the use of e-signatures for legal documents. The importance of global correspondent networks and interbank relationships in trade financing is clearly illustrated under current conditions; concretely, one survey respondent shared that their bank was launching "agreements with [other] banks that in case they are unable to send original documents, they can instead send scanned documents via email as a temporary solution".

29% of respondents said that their local authority has provided regulatory support to help facilitate ongoing trade (Figure 26). In contrast, Asia Pacific seems to be leading the way in the public sector response to COVID-19, with 45% of respondents indicating at least some public action to support trade (the highest of any region in the survey). As observed earlier, this is likely a function of life and death priorities faced by authorities around the globe, coupled with resource and capacity constraints: it will be important to ensure that trade and trade finance are prominent in the economic and commercial policy dialogue that is developing in parallel to the public health priorities.

Specific measures introduced by governments cited by respondents included stimulus packages and support for many small businesses that have been introduced by parliaments and central banks around the world. But they also included more trade-specific measures. Many respondents indicated that regulators had relaxed the need for physical documentation. Other respondents also indicated that a reduction in capital requirements and a relaxation of KYC have been introduced to help support the ongoing flow of global trade.

Notably, 50% of respondents indicated they did not know whether their governments had provided regulatory support to help facilitate trade flows. This finding surely reflects in part the urgency of focusing on other matters, but also hints at the need for improved communication flows and enhanced understanding of available support options.

The redefinition of the commercial, legal, and policy landscape around trade may prove to be a powerful force in advancing long-delayed aspirations to digitise trade and trade finance. The ICC Digital Trade Roadmap will be an important contribution to the development of new modes of digital trade.

The impact of COVID-19 on trade comes not only from supply and demand shocks, but also from logistical challenges. Quarantines and closed borders, coupled with reduced global capacity to move cargo, will naturally reduce global trade flows. In unprecedented and unpredictable moments like these, new and creative solutions emerge – first as temporary fixes and ultimately as new industry norms. The difficulty many banks have found in respect of original documentation serves to highlight the urgency of digitisation in trade finance.

One respondent wrote that in the short term “the ICC should push banks to agree on amending pending L/Cs where original documents cannot be produced anymore or delivered”. However, with an eye on the longer term, one respondent said, “The fact that original documents have to be examined and delivered is a significant problem. Technical issues become credit risks. I hope that based on the experience with COVID-19 we can continue to move toward digitisation [in trade]”.

FEATURE

SWIFT Trade Traffic: the year in review

Huny Garg, Head of Trade – EMEA, Business Development, SWIFT

This section of the report provides a data-driven commentary on global trade finance traffic, based on data from SWIFT. While SWIFT trade finance traffic represents only a modest portion of global trade by volume, it is a good barometer of trends for L/C use, since about 90% of L/C transactions go via SWIFT.

SWIFT Terms Explained

Traffic: Live messages sent over SWIFT

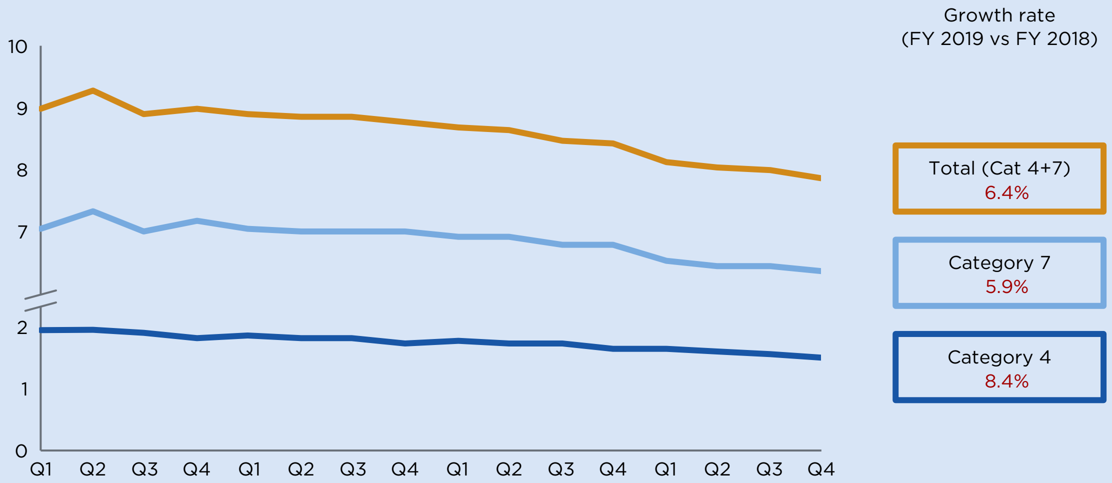
Category 4 messages/ MT400s: Flows for documentary collections, except the three least used cash letter messages

Category 7 messages/ MT700s: Flows for commercial and standby L/Cs and guarantees

Analysis of SWIFT Trade Traffic: Highlights in 2019

- SWIFT trade finance volume fell 6.4% in 2019 from the year before, in large part due to a 5.9% drop in category 7 and a 8.4% drop in category 4 traffic. The decline for MT700 traffic at 3.9% was less pronounced than the overall decline that was driven by an 8.4% decline in MT799 messages.
- Asia-Pacific continued to register much higher volumes of MT 700, garnering a 76.0% share for imports and a 78.1% share for exports. Countries using SWIFT L/Cs the most for imports were: Bangladesh, South Korea, China, India and Pakistan.
- Country/ region using SWIFT L/Cs the most for exports were: China, Bangladesh, India, Hong Kong and Singapore.
- Imports rose sharpest in Ethiopia and Nepal, up 10.4%, and exports rose fastest in Portugal, up 9.6%.
- Imports fell the most steeply in Sri Lanka, down 15.8%, and exports fell sharpest from Saudi Arabia, down 18.6%.

Figure 27
SWIFT global trade finance traffic, FY2016-FY2019



Trade finance traffic continues to slide

SWIFT trade finance volumes in 2019 were down 6.4%, falling more sharply than last year's drop of 2.35%, pushed down by the decline in category 7 documentary credits and guarantees of 5.9%, and an 8.4% fall in category 4 documentary collections.

L/C volumes and values – the slump continues

The volume of L/Cs on SWIFT fell again last year, off 3.9%. Interestingly, Q4 2019 showed an upward trend after many quarters of decline. There was a decline of 8.13% in MT799 (the free format message type that accounts for the largest portion of category 7 volumes) possibly due to improvements in structured messages during standards release in 2018 by SWIFT.

Figure 28
Import traffic vs. average value in FY2019, split by region, based on SWIFT MT700 traffic

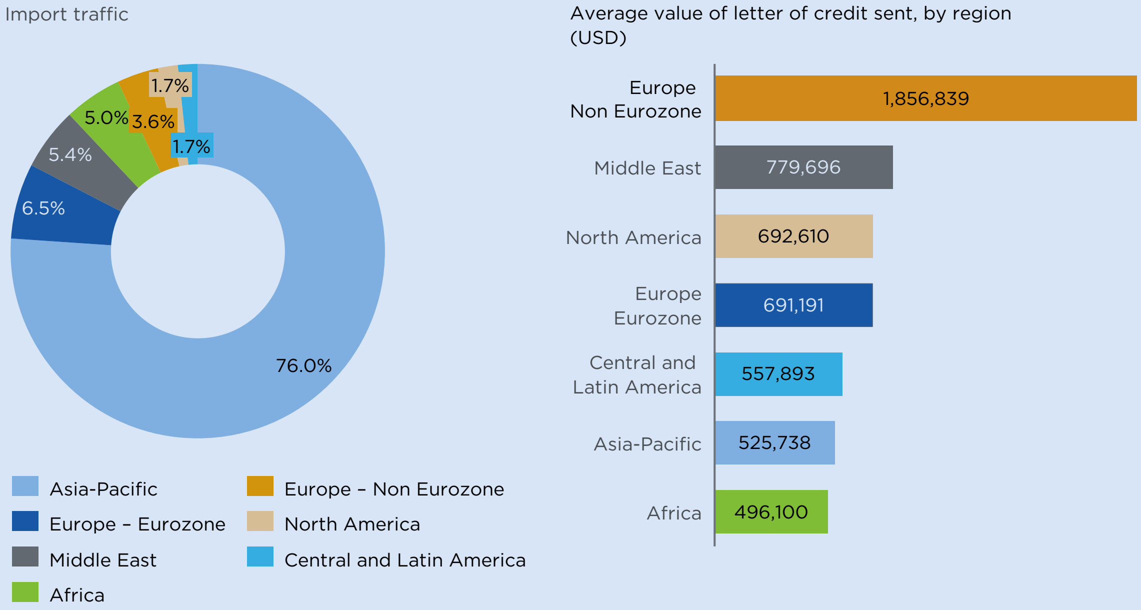
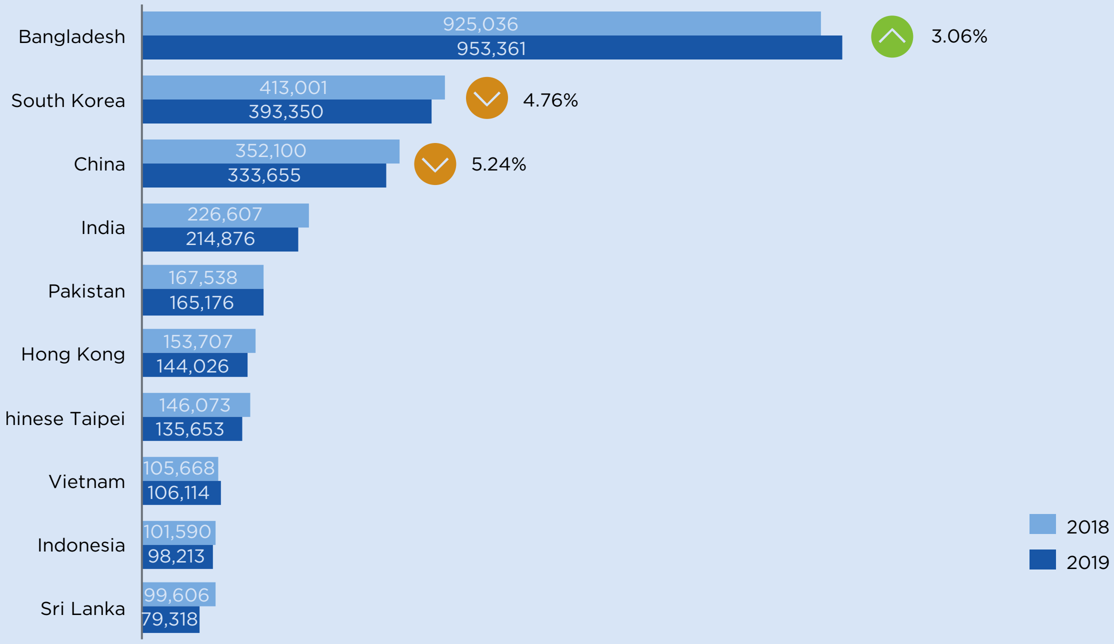


Figure 29

SWIFT MT700 import L/C volumes by country/ region (# messages)



Asia-Pacific received the most L/Cs, around 3.1 million MT700s, much more than any region. But the average value of an L/C received in Asia-Pacific was lowest at USD 430Kv.

Regional analysis: Import L/Cs[1]

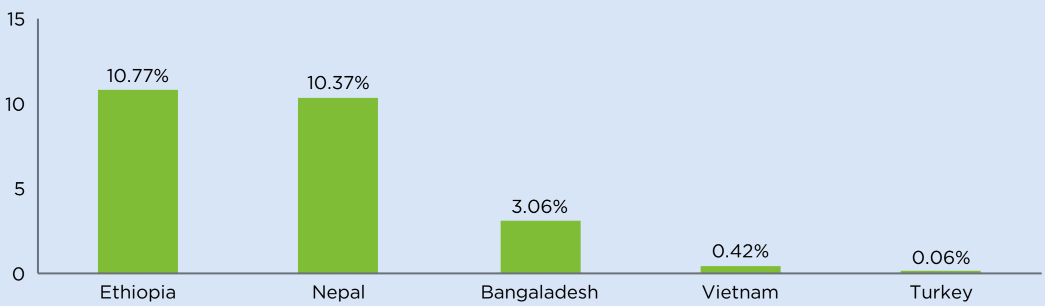
Asia-Pacific continued to register the largest volume for import L/Cs sent using MT 700s, making up 76.0% of world traffic in 2019, followed by the Eurozone 6.5% and the Middle East 5.4%.

The average value of import L/Cs was the highest in non-Eurozone European countries, whereas Africa had the lowest value import L/Cs.

Looking at the cross-border volume of MT700 traffic, excluding domestic flows, the countries importing the most using L/Cs are shown in Figure 29.

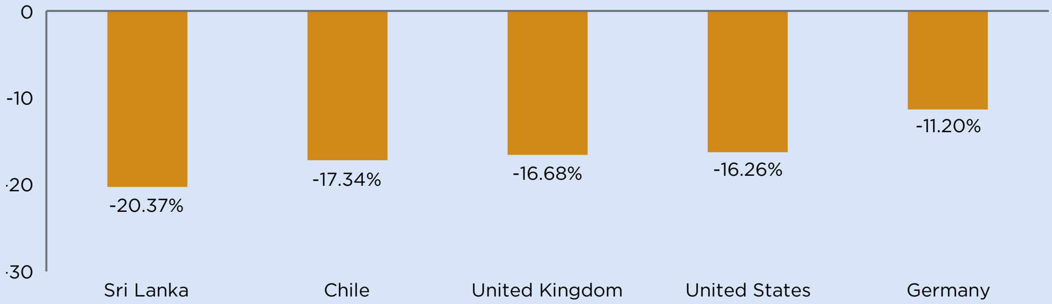
Figure 30

Fastest-growing importers, based on SWIFT MT700 traffic



1 Data includes both domestic and international traffic, as commercial letters of credit can be utilised in domestic transactions

Figure 31
Importers with the sharpest declines in imports, based on SWIFT MT700 traffic



Bangladesh was the only country among the top 5 that experienced growth in import L/C volumes. Countries like South Korea and China saw a decline of 4.76% and 5.24% respectively.

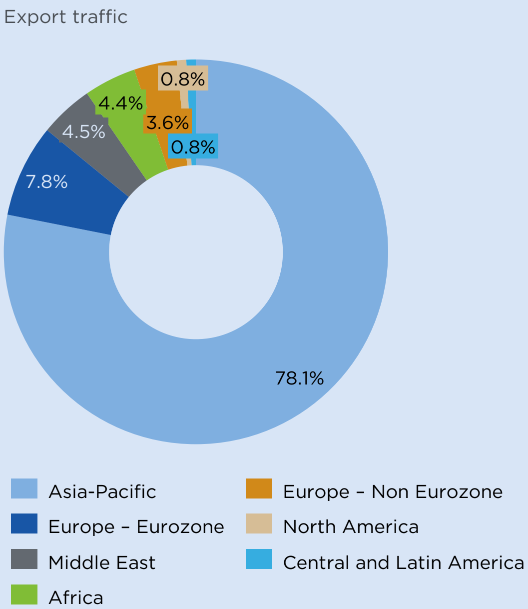
Looking at annual volume over 20,000 MT700s sent internationally, the countries with the highest year-on-year growth in this category in 2019 are shown in Figure 30 above.

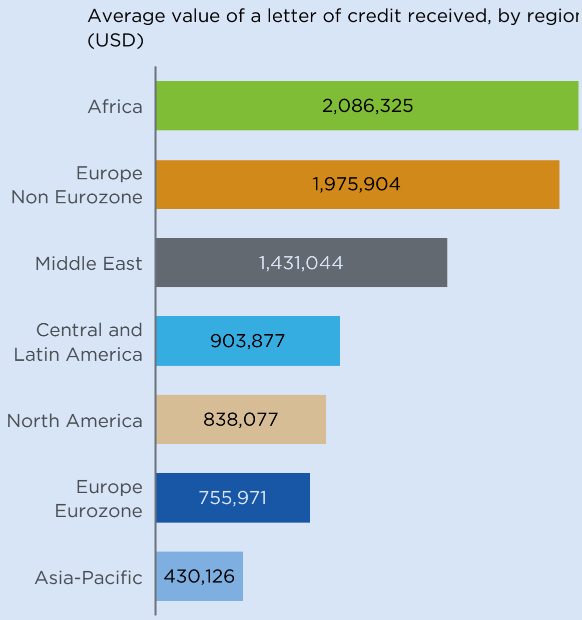
With a yearly volume higher than 20,000 MT700s sent internationally as a gauge, the countries showing the largest declines in imports using L/Cs are shown in Figure 31.

Regional analysis: Export L/Cs[1]

Asia-Pacific continued to register much higher volume for received MT 700s, (exports) accounting for 78.1% of world traffic in 2019, followed by the eurozone (7.8%) and non-eurozone Europe (4.5%).

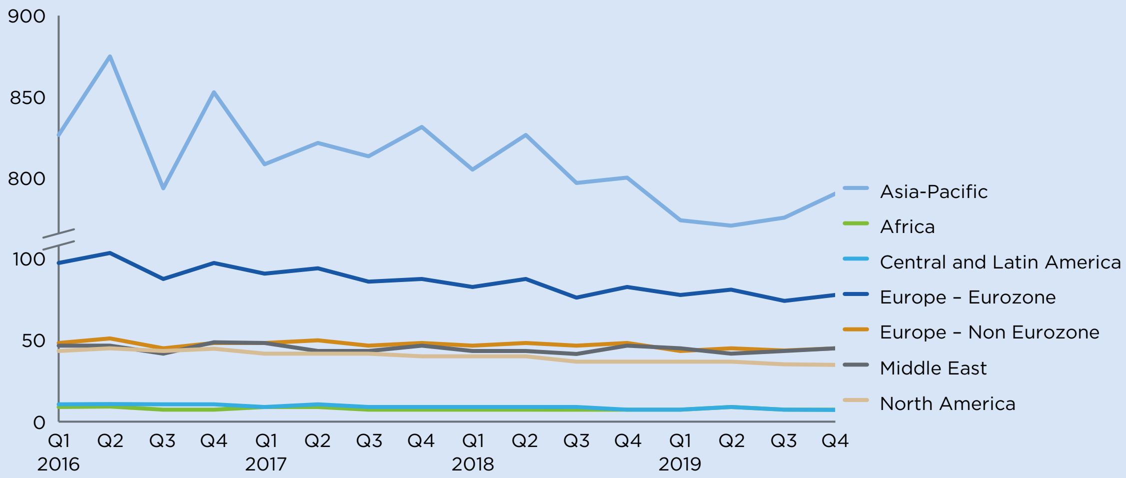
Figure 32
Export traffic vs. average value in FY2019, split by region, based on SWIFT MT700 traffic





1 Data includes both domestic and international traffic, as commercial letters of credit can be utilised in domestic transactions

Figure 33
SWIFT MT700 messages received to non-Eurozone Europe



Export-related message traffic was down across the board in 2019 compared with the previous year. The region that showed the steepest drop was the Eurozone, where export traffic trailed off 6.92%, followed by North America, where traffic contracted 6.54% and Africa, where traffic fell 5.80%.

Looking at the cross border (excluding domestic flows) volume of MT700s received, the countries that exported the most using L/Cs are shown in Figure 34.

Figure 34
SWIFT MT700 export L/C volumes by country/ region (# messages)

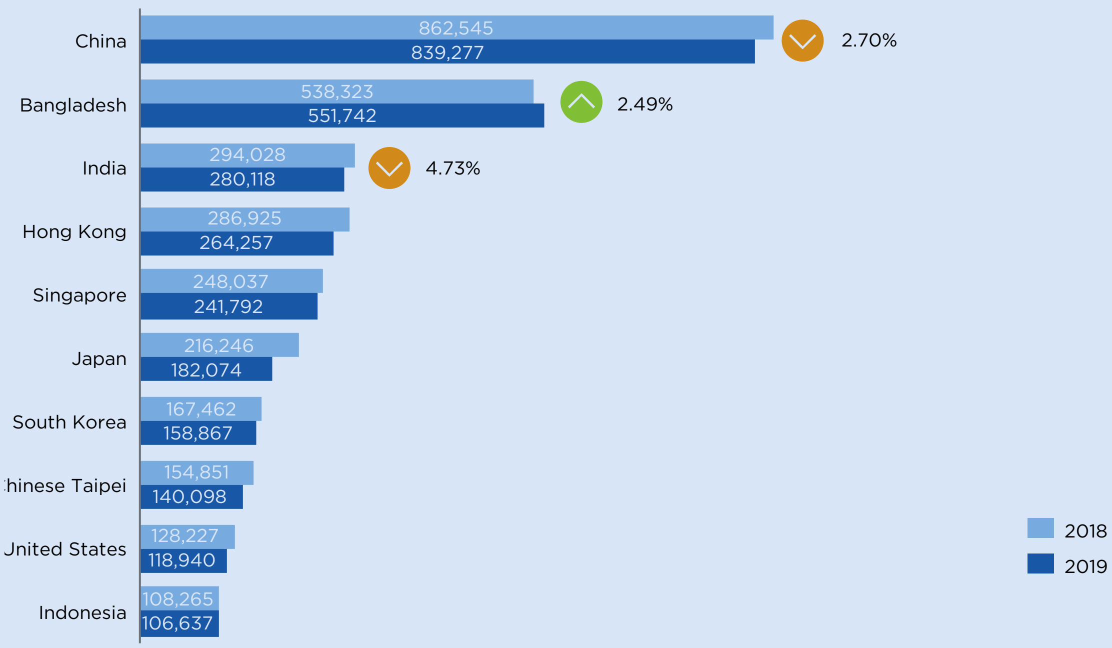
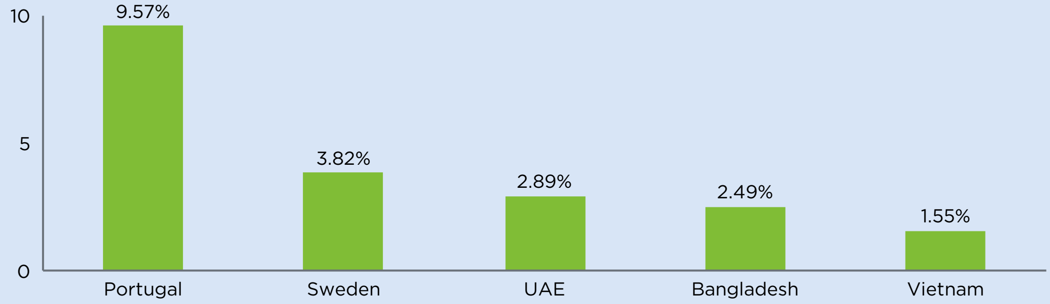


Figure 35
Fastest-growing exporters in 2019, based on SWIFT MT700 traffic

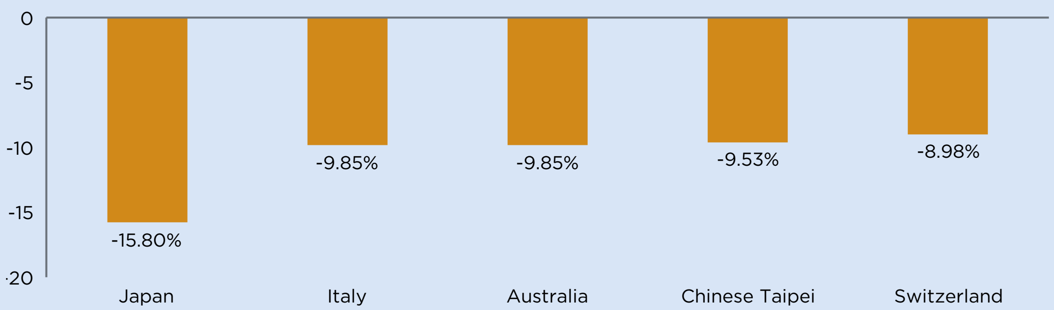


It was noted that Bangladesh continues to see growth in L/C volumes despite most top markets seeing a decline in 2019.

Using a yearly volume of more than 20,000 MT 700s received internationally as a gauge, the countries with the fastest growth in 2019 compared to 2018 and shown in Figure 35

The countries registering the largest drop in annual volumes in 2019, in the category over 20,000 MT 700s sent internationally, are shown in Figure 36.

Figure 36
Exporters with the sharpest declines in exports, based on SWIFT MT700 traffic



Deep-dive on confirmed L/Cs

The share of confirmed L/Cs rose slightly, up 0.3% in 2019 from the previous year. Africa continued to receive the highest percent of confirmed L/Cs, and Asia-Pacific the lowest.

Figure 37
Confirmed export L/C volume, based on SWIFT MT700 traffic in 2019 vs. 2018

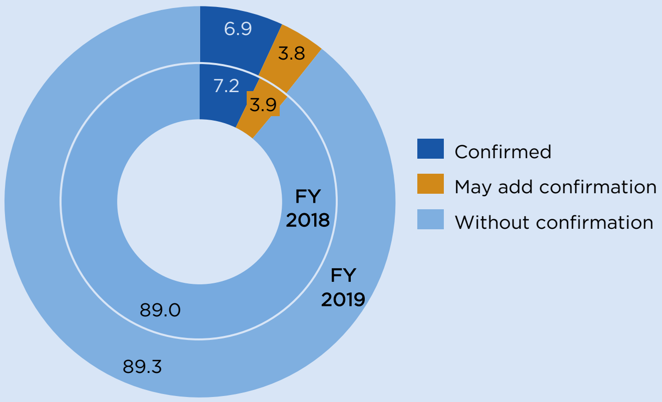
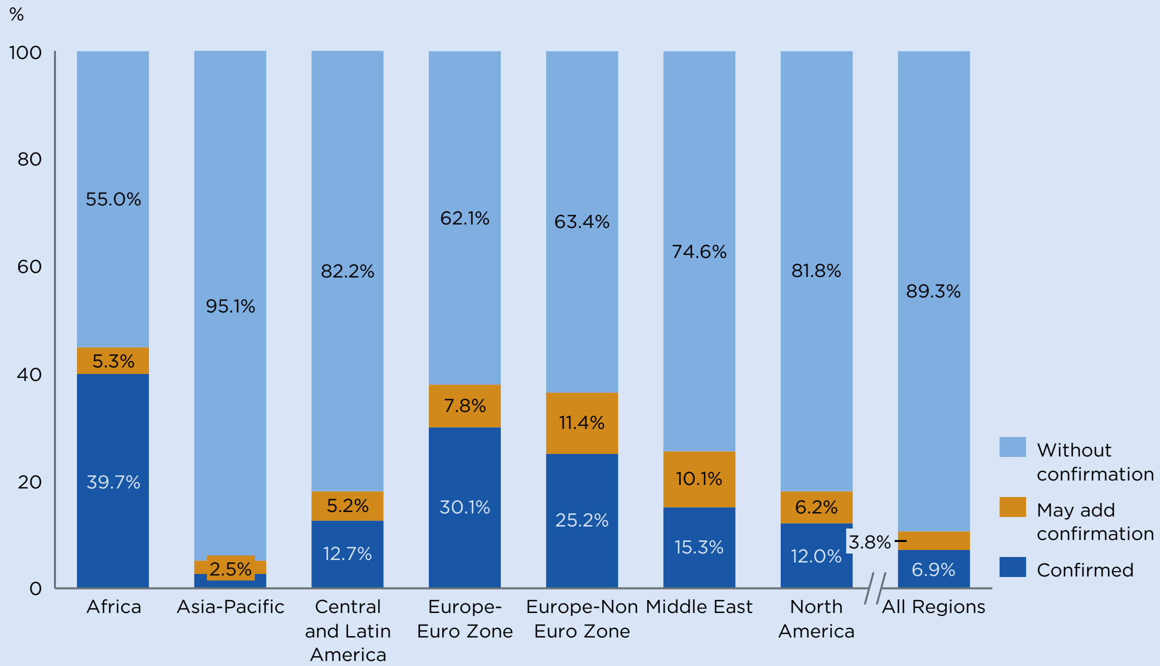


Figure 38
Distribution of confirmed export LC volumes by region in 2019, based on SWIFT MT700 traffic



Deep-dive on L/Cs available by negotiation

The broad preference for using L/Cs available by negotiation as defined under ICC UCP rules continues to be in evidence in SWIFT message data.

In most cases, L/Cs available by negotiation are issued. Based on SWIFT traffic, the share was slightly higher at 74.1% in 2019 with the previous year at 73.6%. Regionally, L/Cs available by negotiation accounted for 80.9% of L/Cs in North America and 78.6% in Asia Pacific. All other regions except Africa (where Payment is most common) mostly used L/Cs available by Negotiation.

For purposes of this section and the graphics that follow, SWIFT has used the term 'Credit Rule' to identify the ways in which an L/C may be made available, as reflected in the ICC's Uniform Customs and Practice (UCP) for Documentary Credits. L/Cs available by Negotiation represent one among multiple credit rule options, but by far the most common and preferred globally.

Figure 39
Export volume by credit rule combination, based on SWIFT MT700 traffic

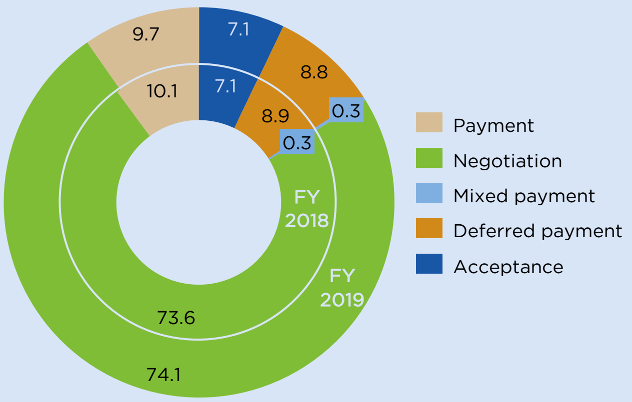
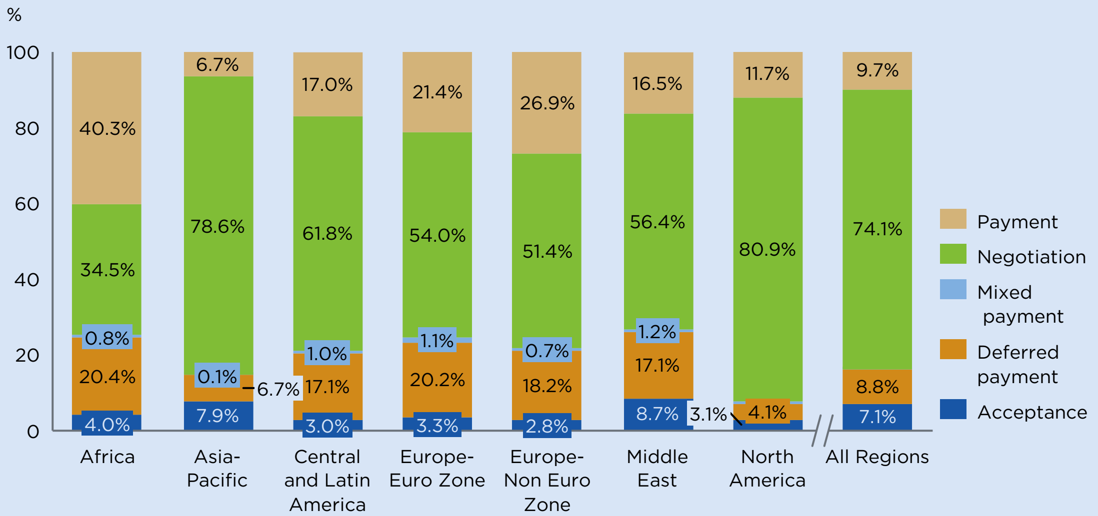


Figure 40
Distribution of confirmed export LC volumes by negotiation in 2019, based on SWIFT MT700 traffic



Deep-dive on L/C validity

L/C validity – or the time between the issuance of the L/C and its expiry – remains short. A total of 38.9% of L/Cs were extended from 31 to 60 days, and 35.4% from 61 to 90 days in line with the short-term nature of a significant portion of global trade.

Validity of L/Cs are generally longer in the Eurozone (33% up to 60 days) and Africa (34.3% up to 60 days) compared to Asia-Pacific where validity is shorter on average (52.9% up to 60 days).

Figure 41:
Volume of L/Cs split by validity, 2019, based on SWIFT MT700 traffic

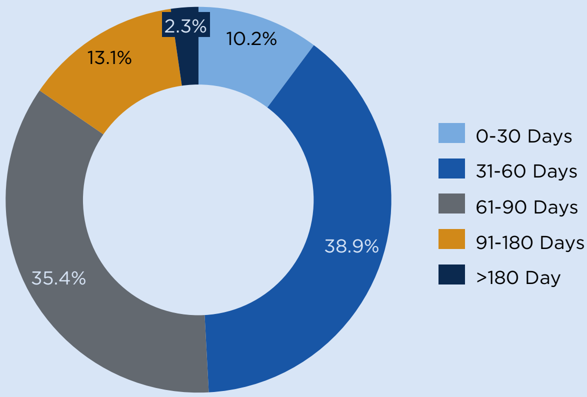
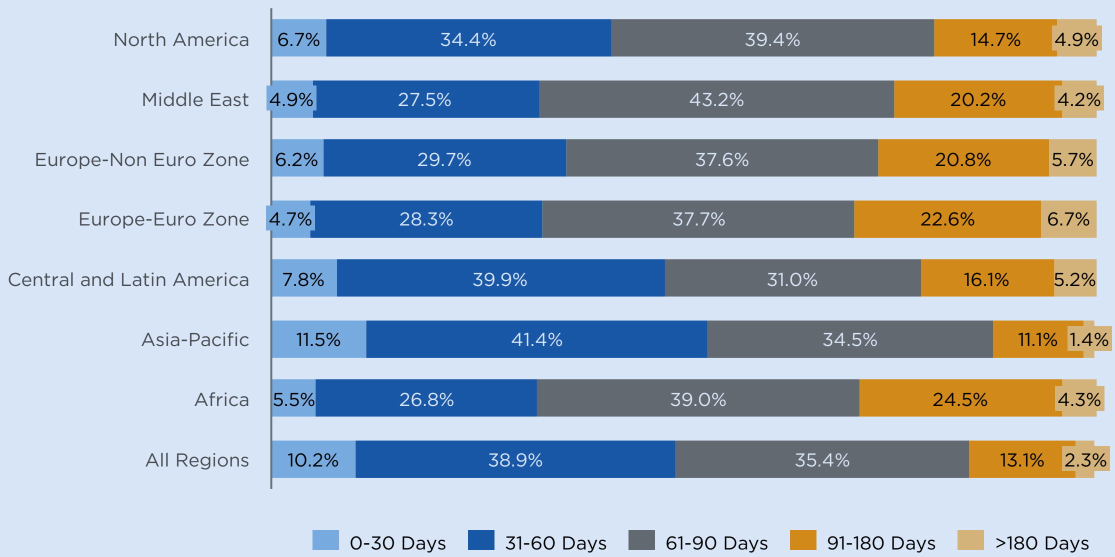
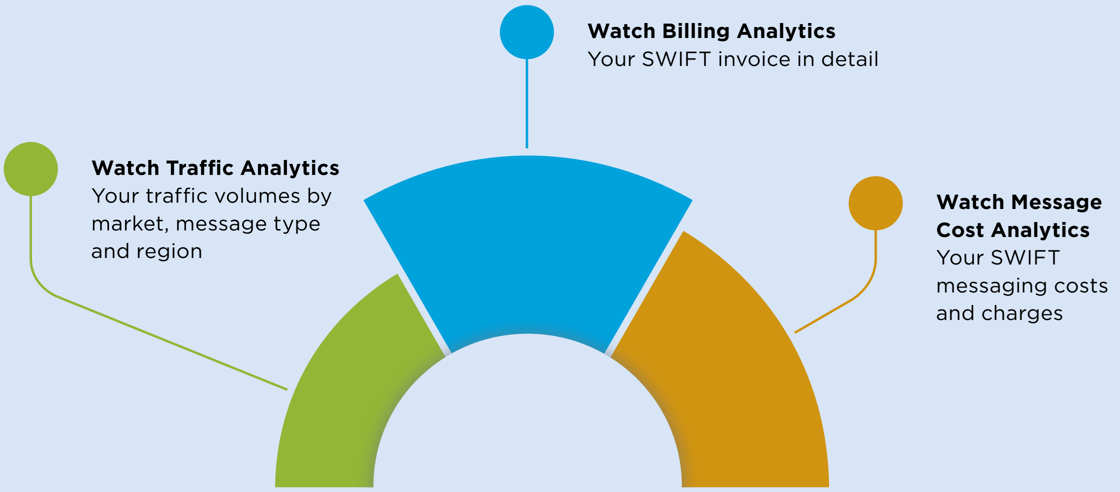


Figure 42
Region-by-region export volume by validity, based on SWIFT MT700 traffic



Watch Traffic

Comprehensive and dynamic analysis of global financial message volumes, message costs and billing data sent and received over SWIFT.



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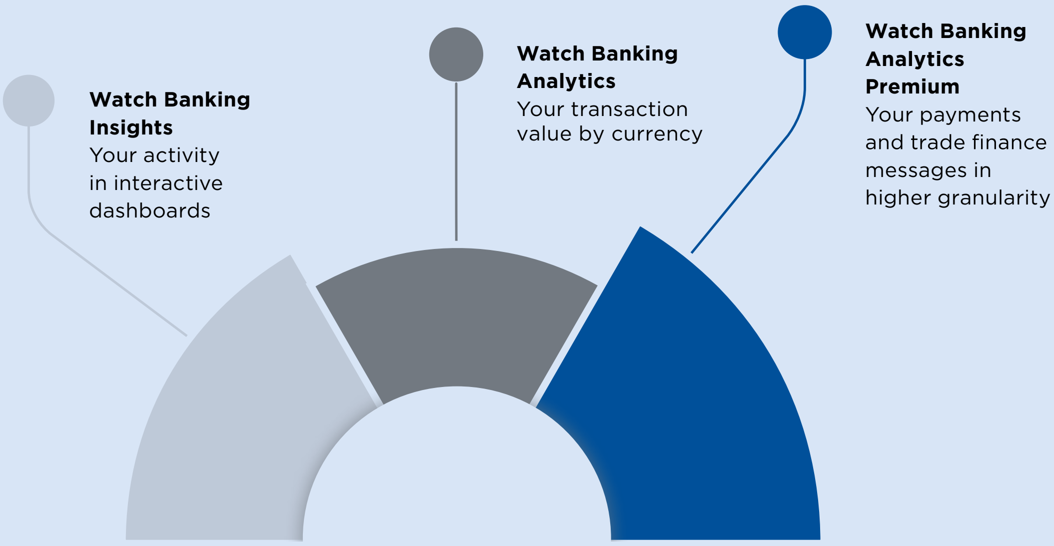

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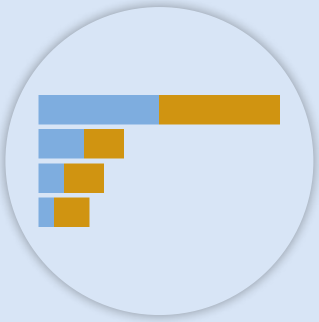
Develop footprint and portfolio for Payments and Cash Management



Your top cash management reporting messages sent and received YTD

Manage correspondent network for Payments and Trade finance

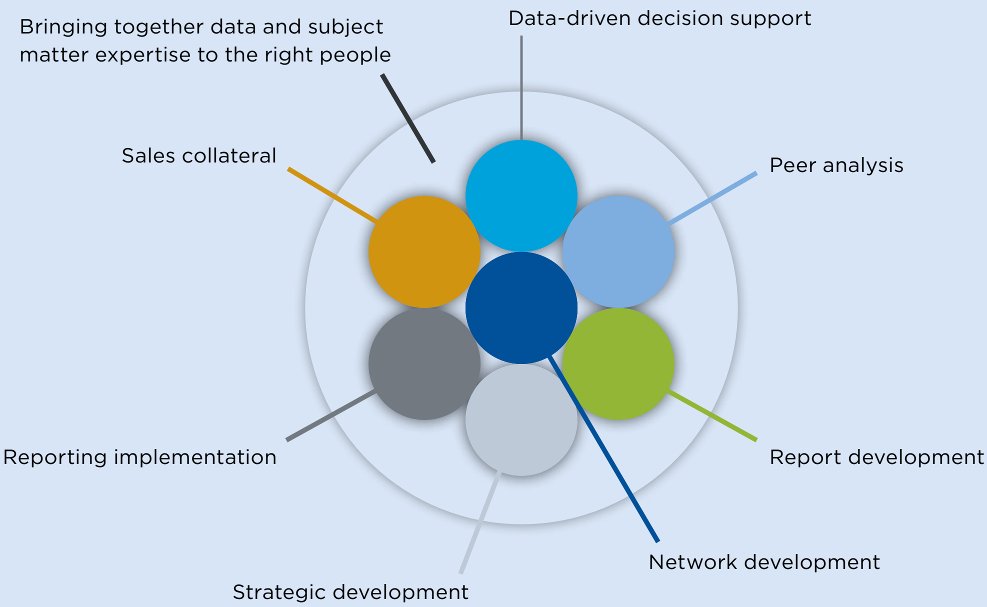
The evolution of the number of counterparties and countries you have activities with

Develop footprint and portfolio for Trade finance

Your activity share in MT 700 YTD and its variations compared to last year

BI services

Our consultants bring subject matter expertise and more granular data, serving your transaction business teams with tailor-made market and anonymous competitive information.



FEATURE

TXF on Export Finance

Dr Tom Parkman, Head of Research, TXF

This feature is based on market sentiment data collected from TXF Research's global Export Finance Industry Report 2020, scheduled for release at TXF Global in 2020, and closed deal data from TXF Data. The primary aim of this feature is to provide a comprehensive overview of the state of the export finance market in 2019.

It is important to note that this feature was produced prior to the COVID-19 outbreak. While it is discussed in some detail, the data in this feature highlights the state of the export finance industry before the outbreak.

Methodology

TXF Research

TXF Research's Export Finance Industry Report 2020 uses a mixed methodology that combines quantitative and a qualitative component. The quantitative data was collected using an online survey platform (SurveyMonkey) with banks, export credit agencies (ECAs), exporters, importers (borrowers), law firms and private insurers (brokers and underwriters) all taking part. The qualitative data was collected via telephone interviews with consenting individuals. This mixed methods approach enables the report to identify the latest trends in the market with in-depth and thought-provoking commentary to understand how and why these market trends are occurring.

At the time of writing (March 2020), the data collection was still ongoing, meaning that the data presented in this feature is based on a cross section of the final dataset. A total of 246 individual respondents from the above-mentioned institutions make up the survey data.

TXF Data

TXF Data is the leading source of transaction data in the export finance market, used as the main reference by all the market leaders. The information is collected through three sources:

(i) Deal information submitted through Tagmydeals and directly to TXF

(ii) News articles obtained through TXF's editorial team

(iii) Corporate press releases found online using machine learning.

Findings

Before this feature delves into the state of the export finance market, it would be remiss to not start by mentioning COVID-19. In financial parlance, a black swan event is an extremely rare and damaging event that is almost impossible to predict. It is safe to say that the global COVID-19 pandemic is a 'black swan' event.

To supplement TXF Research's Export Finance Industry Report 2020, an addendum survey looking specifically at the impact of COVID-19 on the industry was conducted. One area the survey explored was force majeure.

Our survey data found that nearly 35% of the sample do not know, or do not have, a force majeure clause built into the legal part of their export finance loans. Further, of those that did have a force majeure clause built into their legal work, a combined 75% of the sample did not know, or do not have, a global pandemic scenario inbuilt, and, finally, **just 15% of the sample with a force majeure clause that covers global pandemics have invoked it**. It remains to be seen how damaging COVID-19 is to the export finance industry but the uncertainty surrounding force majeure could have serious financial, operational and reputational repercussions for institutions.

The ICC has been tracking whether force majeur clauses have been (disproportionately or inappropriately) triggered in the context of the COVID-19 pandemic and has found no systemic evidence of abuse – highlighting that trade continued to be conduced on a good faith basis and in line with industry standards and practice. It has also issued a Guidance Paper on force majeur which builds upon past ICC publications and industry practice.

The market at a glance

In 2019, total deal volume reached USD 108 billion across 341 deals, down USD 30 billion from 2018's USD 138 billion total volume across 412 deals. Looking in more detail at 2019, it was a fairly turbulent year with three clear peaks in export finance activity in February, May and December corresponding to deals closed by Australia Pacific LNG for USD 6.9 billion, the Bahrain Petroleum Company (BAPCO) for USD 4.1 billion, and Gazprom's massive Amur gas processing plant for USD 12.8 billion, heavily backed by a number of European ECAs, respectively (Figure 43).

Interestingly, if these three deals are removed, the export finance landscape looks quite different. The total deal volume drops to USD 84 billion with an average deal size across the year of USD 7 billion (compared to USD 9 billion in Figure 44). Figure 44 also shows that the largest deal volume in the top performing month drops to just over USD 12 billion (down from USD 25 billion in the same month in Figure 44) which suggests that 2019 was a fairly flat year for export finance. This is particularly true when compared to 2018.

TXF Research supports this finding with the level of activity being rated as three out of five over the past 12 months. One lawyer explained why: "Export finance activity seems to be a little bit less busy than in recent times. I think this is probably driven by the China-US trade war. There has just been a general softening of things. I also think Brexit has had a detrimental effect too. I also think the Coronavirus will have a very damaging effect on activity."

At the time of the interview, the COVID-19 pandemic had not taken full hold of the global economy, but it is clear now that that was an accurate prediction. When survey respondents were asked about the impact of the pandemic on the global economy, nearly 80% posited that it will lead to a global recession comparable with the 2008 financial crash.

Figure 43
An overview of the export finance market in 2019

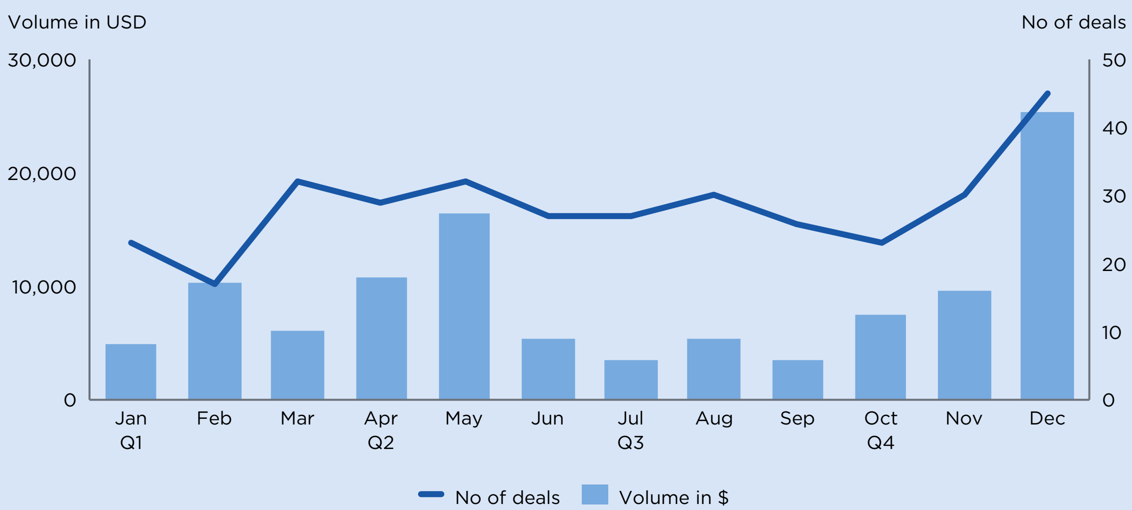
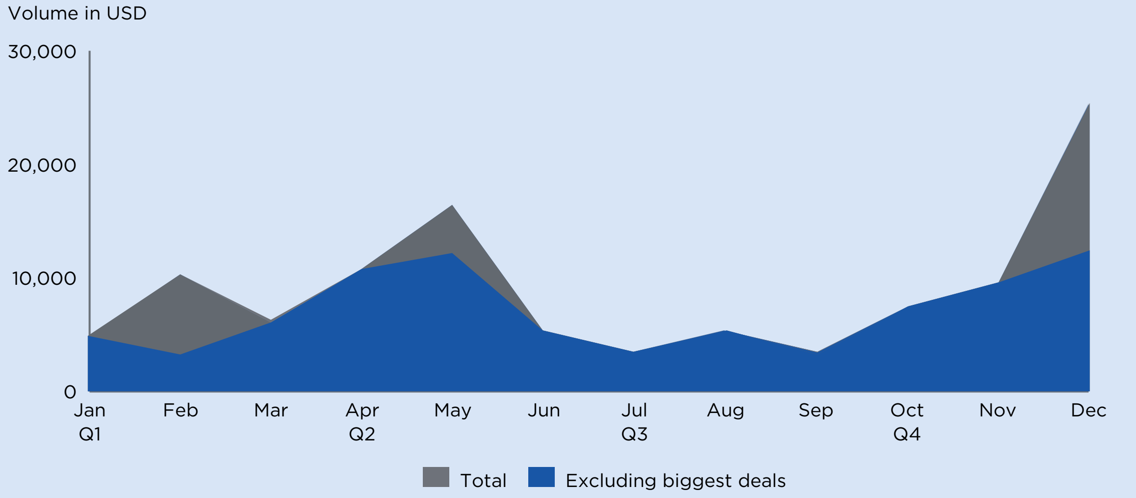


Figure 44
An overview of the export finance market in 2019, without the three largest deals included



A regional view

Looking at closed deal data, Figure 45 shows that Asia Pacific was the most active region for export finance in 2019, with deal volume totalling USD 17.4 billion across 51 deals, followed by the Middle East (USD 6.9 billion across 27 deals) and Russia (USD 16 billion across 40 deals). However, the Middle East had an average deal size of USD 629 million, nearly double that of Asia Pacific (USD 341 million). Europe had the smallest average deal size of USD 201 million, a finding driven by a smaller total volume (USD 14 billion), but it did have the greatest number of closed deals (n=71).

TXF Research suggests that this trend will continue over the next 12 months, with 49% of respondents suggesting that they will do more export finance business in Asia Pacific, followed by the Middle East (31%) and Europe (30%). One exporter currently active in Asia Pacific, and looking to do more, explains why Asia Pacific is attractive: "China is not just the only place to do business with anymore [in Asia Pacific]. We are doing more in Bangladesh, Vietnam, Myanmar, Chinese Taipei and many others. We are looking to cover as many markets as possible not just in terms of quantity, but quality also."

Figure 45
2019 regional breakdown

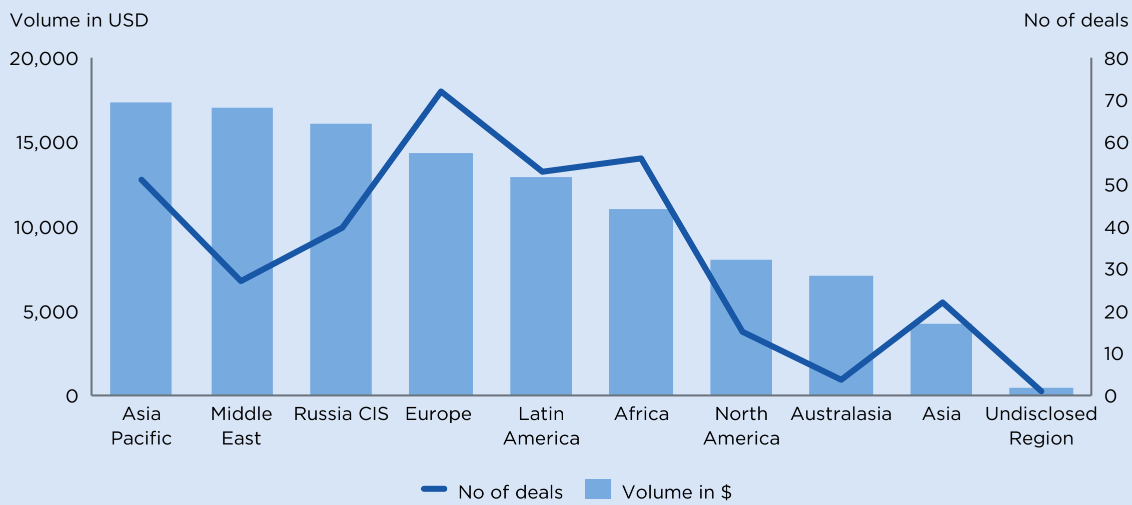


Figure 46
Respondents' level of activity over the past 12 months

	More active	About the same	Less active
Asia-Pacific	49%	45%	6%
Central and South America	27%	62%	10%
Europe (including Russia and Turkey)	30%	65%	5%
Middle East	31%	58%	11%
North America	19%	68%	13%

A deeper look at sector breakdown

Figure 47 shows that oil and gas continued to dominate the export finance market in terms of volume with USD 36.7 billion being closed across 21 deals in 2019, followed by power (USD 22.4 billion across 51 deals) and transport (USD 15.9 billion across 62 deals). With the average deal size of oil and gas standing at a sizeable USD 1.7 billion, it is more than four times larger than the average deal size in power (USD 438 million) and nearly seven times larger than transport (USD 257 million). This closed deal data shows why oil and gas remains the dominant sector to invest in. Figure 48 too suggests that oil and gas may continue to dominate, as it has grown year-on-year since TXF Data started collecting closed deal data.

Figure 47
A breakdown of export finance activity, by sector in 2019

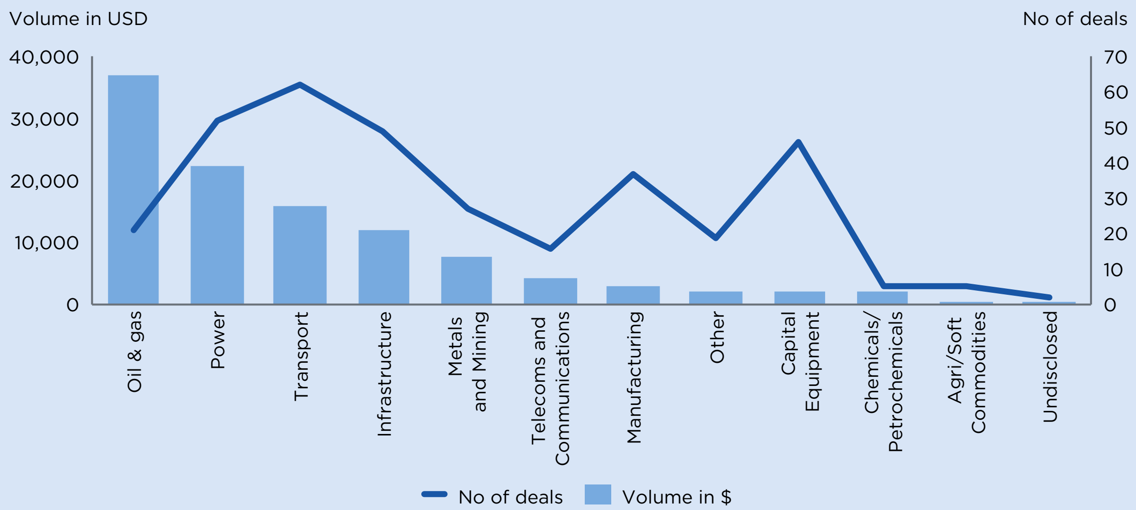


Figure 48
Activity levels across the sectors, 2017-2019

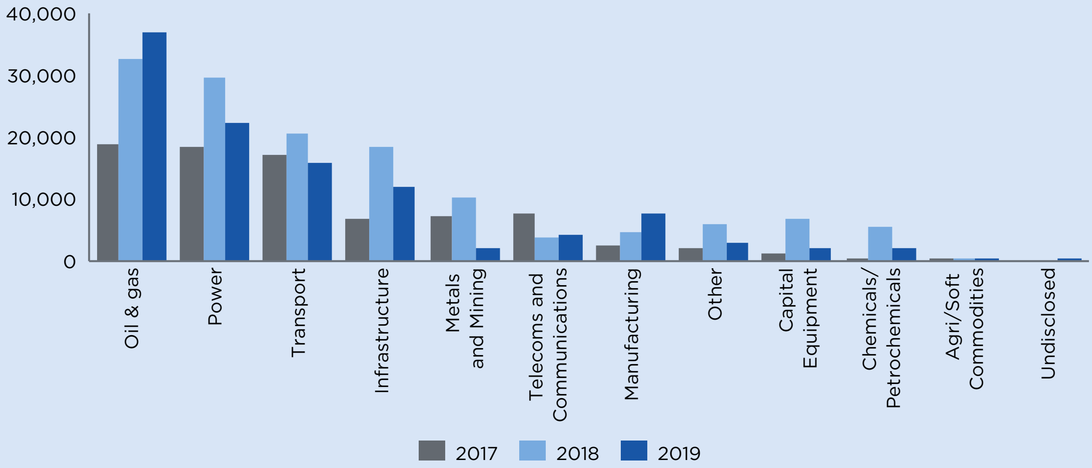


Figure 49
Export finance activity over the next 12 months, by sector

	More active	About the same	Less active
Defence	22%	70%	8%
Infrastructure	46%	50%	4%
Manufacturing	17%	74%	8%
Metals and mining	15%	71%	14%
Oil and gas	25%	64%	12%
Petrochemicals	19%	73%	8%
Power	26%	71%	3%
Renewable energy	53%	47%	0%
Telecommunications	19%	73%	8%
Transport	36%	60%	4%

However, preliminary projections in TXF Research's Export Finance Industry Report 2020 provide some optimism for the renewable energy sector, with 53% of the survey sample stating that they plan to become more active in this space, double that of those looking to do more in oil and gas (25%) (Figure 49).

Perhaps encouragingly for the export finance industry too is that 59% of the survey sample believe that sustainability is a way of life that must be adopted by every institution involved in export finance. Given the strong relationship between sustainability and renewable energy, there is cautious optimism to be had for the future, as one banker pointed out: "We don't finance anything in coal, defence or petrochemicals anymore. We are also reviewing nuclear and our involvement in mining. It will take time as many of these deals have long tenors, but I see a positive future for export finance."

Figure 50
ECA involvement over the past three years

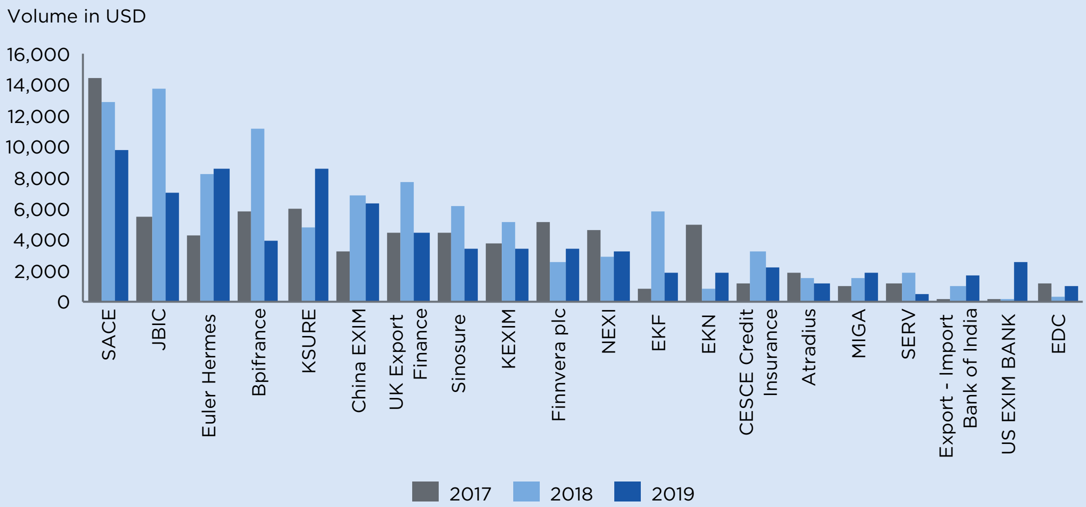
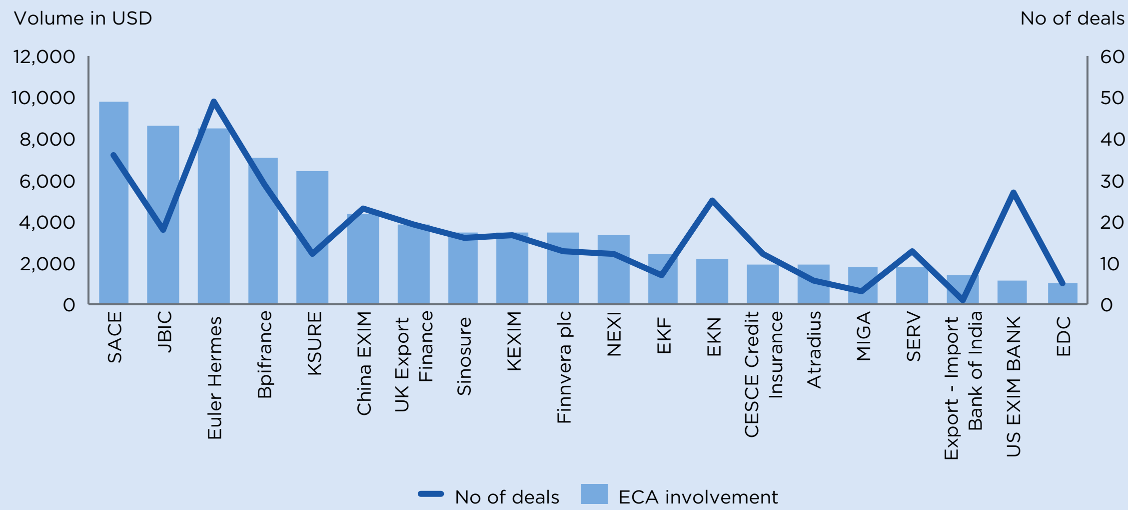


Figure 51
ECA involvement over the past 12 months



ECA involvement

Figure 50 shows that compared to 2017 and 2018, ECA involvement in 2019 has been significantly lower. Looking more closely at the past 12 months, SACE has led the way, guaranteeing USD 9.8 billion worth of deals, followed by KSURE (USD 8.6 billion) and Euler Hermes (USD 8.5 billion) (Figure 51), all of which were involved in the two largest export finance deals in 2019 the Amur gas power processing plant (SACE and Euler Hermes) and the Bahrain Petroleum Company deal (KSURE).

The future of export finance

When the survey respondents were asked about how optimistic they were about the future of export finance, it was a fairly muted response, with an average overall score of two out of five. The main reason for this, as Figure 52 shows, is because of a global recession. It is important to note that respondents noted a global recession as the greatest threat prior to the COVID-19 pandemic.

Since the outbreak, an addendum survey asking the export finance industry about the impact of COVID-19 has been released to the market to better understand its impact. Of a separate sample of 72 respondents (at the time of writing), the reported likelihood of a global recession, comparable to that of 2008, is four out of five. While it is unclear what the final cost of the outbreak will be, it is safe to say that the future of the export finance industry is very uncertain.

Conclusion

2019 proved to be a fairly flat year for export finance, with oil and gas continuing to dominate above any other sector. While Asia Pacific did look set for a fairly optimistic future, the COVID-19 outbreak will almost certainly curtail that optimism. While TXF Data suggested that 2020 might see a resurgence in export finance activity, the black swan event that is COVID-19 looks set to have serious and long-lasting consequences for trade finance.

Figure 52
Greatest disrupters to the export finance industry

Global recession	53%
Geopolitical tensions in borrowing countries	48%
Increasing regulation and compliance	42%
The ongoing US-China trade war	38%
Climate change/ rising environmental problems	30%
Increasingly stringent KYC (‘know your customer) requirements	26%
Involvement of development banks	23%
Increased direct lending from ECAs	16%
Lower funding/ fees from new entrants into the export market	15%

SUPPLY CHAIN FINANCE

Survey analysis

Supply chain finance is one of the fastest growing trade finance products and is responsible for the majority of market growth. Incumbents and disruptors who have succeeded in this market have done so with material technology investment that has allowed the product to work at scale with some of the world's largest supply chains. The Global Survey, however, reveals a stark divide in how trade banks are planning to engage with SCF – if at all. Global banks are adopting SCF platforms broadly and expect further growth in the coming years.

The survey found that 64% of global banks already offer an SCF platform (Figure 53), largely in the form of proprietary systems (Figure 54). This is compared to just 38% of regional banks, and 13% of local banks. Given that open account trade and SCF are responsible for the vast majority of growth in trade and trade finance, the disparity between global, regional, and local banks here is concerning: the lack of SCF capabilities may marginalise smaller players, potentially driving further consolidation in a strategically important market that is already highly concentrated.

Notably, while 65% of respondents report having built a proprietary SCF platform, over a third of respondents purchased an open network platform, use a hybrid platform, or insource their SCF platform from a provider. This highlights a potential strategy for smaller players to stand their ground in the market without the need for capital-intensive technology builds, and hence effectively compete in their markets. Indeed, even some of the world's largest banks offering SCF solutions are today leveraging third-party platforms to accelerate bringing leading solutions to customers.

This is the case for payables finance programs, and increasingly for the next wave of evolving SCF techniques, as described in the Standard Definitions for Techniques of Supply Chain Finance, co-authored by the ICC and several industry associations.

Figure 53
Does your bank currently offer a supply chain finance platform?

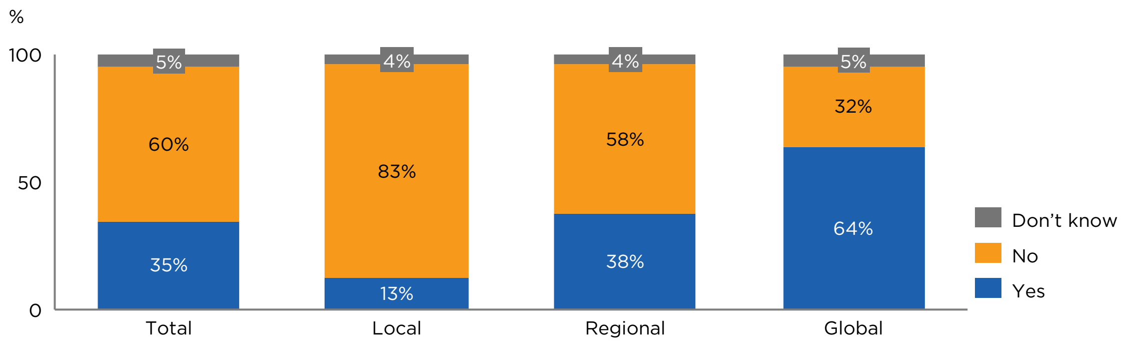
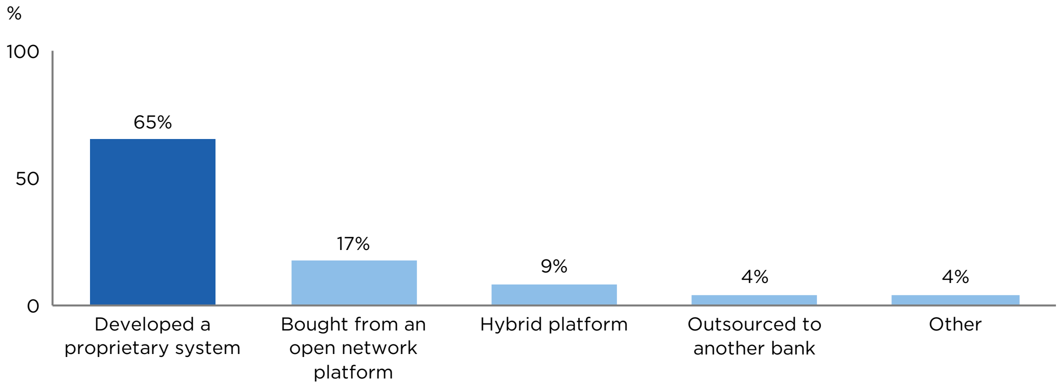


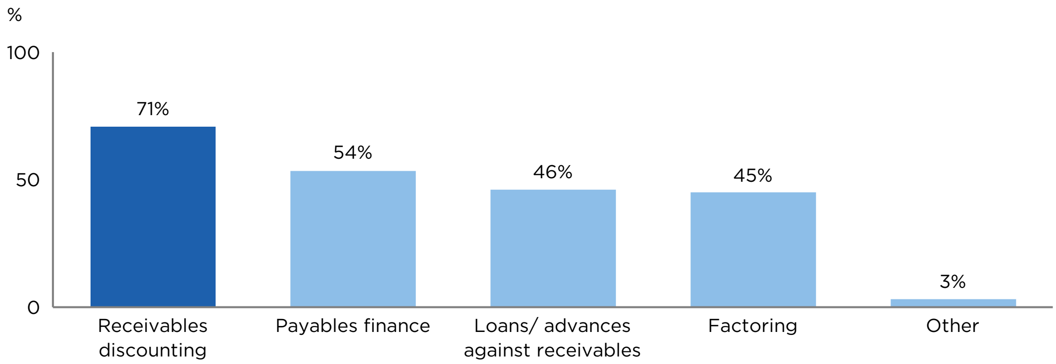
Figure 54
Which of the below best describes your bank's SCF platform(s)?



In terms of the different SCF products, receivables discounting is seen as the most in-demand SCF technique from a client perspective (Figure 55), followed closely by payables finance, loans/ advances against receivables, and factoring. While not necessarily evident from the survey data, there is substantial variation in the customer profiles of these different products. Historically, receivables financing and factoring have been skewed to the micro, small, and medium enterprises (MSME) market, with payables financing more commonly used by larger corporates. Such programs typically involve large buyers extending payment terms to their suppliers, while concurrently inviting suppliers to access funds early on the basis of a discount.

Current market patterns are starting to change with increased demand for receivables finance among lower-margin but high-revenue large corporates, as a means to manage cash flow and liquidity. On the other end, as technology has developed and become more scalable, and non-bank players and third-party investors have grown their presence in the market, we are beginning to see more and more mid-market SCF programs.

Figure 55
What, if any, of the following SCF techniques are most frequently cited as a priority for your bank's clients?

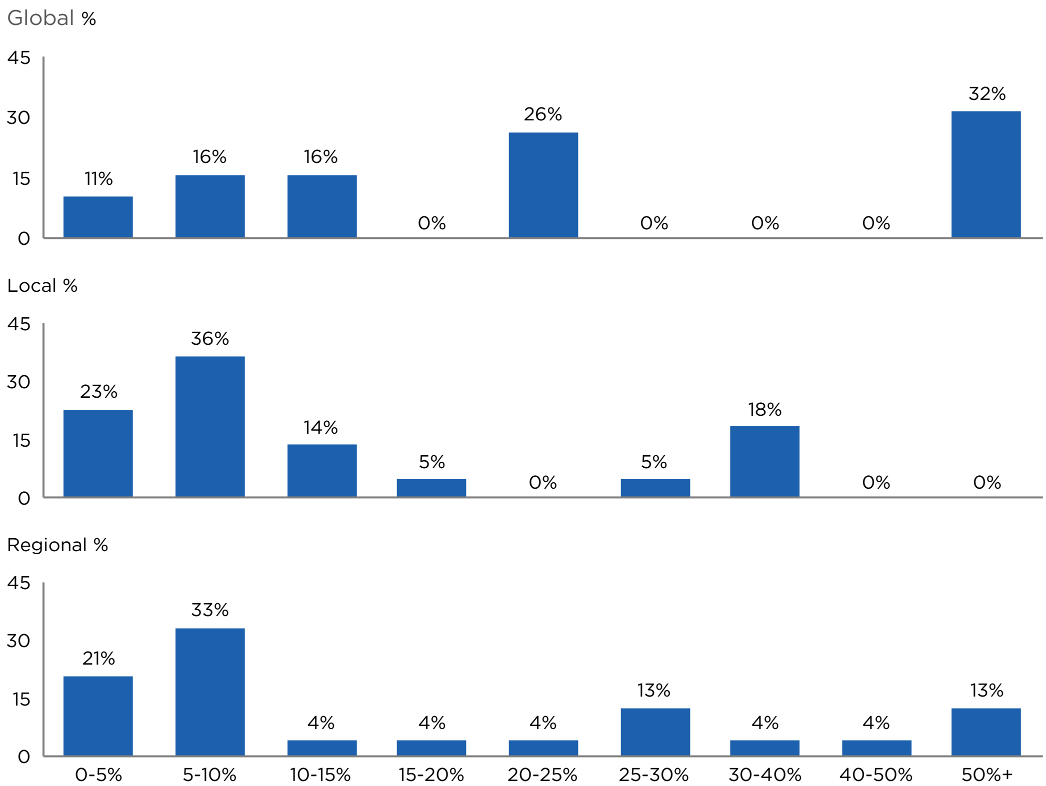


In line with market forecasts, global banks reported that they expect to see a significant increase in the usage of SCF over the next five years – with one-third expecting over 50% growth (Figure 56). By contrast, the majority of local banks expect only 0–15% growth over the same time period, again highlighting the divergence in perspectives between different types of banks. This raises strategic concerns for smaller regional and local banks. If their growth will not come from SCF and open account trade, where will it come from in a market where traditional trade is flat to downward-tending, as reflected in the analysis of SWIFT data earlier in this report?

This is exacerbated by the fact that as larger banks continue to invest in technology to drive automation in trade, it will be increasingly difficult for smaller players to compete on cost-to-serve, putting them in a challenging position in the market. As such, now is an important time for regional and local players to understand how they can access technology in a cost-effective way in order to build a resilient, future-ready trade and supply chain business. The increased availability of banking-as-a-service, software-as-a-service, and infrastructure-as-a-service (including cloud) solutions are likely to play a key role.

Perhaps equally important, the lessons learned by large global banks – and fintechs – around supplier onboarding and payables finance program design and deployment can prove invaluable to regional and local banks in charting a way forward. Industry practitioners in leading SCF banks will likely acknowledge that the core challenge is not necessarily a technology challenge. Multi-bank, consortium-based initiatives may offer a compelling path for non-global banks to participate in the open account market through SCF solutions targeted at their unique client base. Relatedly, finance executives in mid-cap and smaller enterprises may not be as conversant with SCF techniques and may not therefore express a demand for such support from their financial institutions.

Figure 56
What are your growth expectations for SCF within your bank for the next five years?



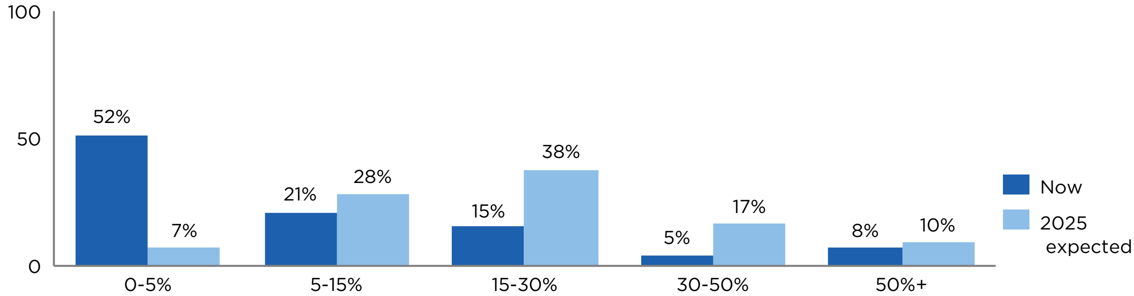
While a majority of respondents indicate that SCF represents only 0–5% of the trade financing made available today, only 7% think that this will be the same in 2025 – highlighting the expectation in the market of the growth in popularity of SCF relative to documentary trade and TTF (Figure 57).

It is worth noting that the findings of this survey will likely understate bank activity levels in SCF, since certain techniques – such as factoring – reside and are delivered in areas outside of a typical trade finance business, in some cases even outside a bank through a related affiliate entity.

However, despite the enthusiasm that global banks have for SCF, the survey reveals a number of challenges in delivering SCF solutions to customers.

Figure 57

What is the proportion today of SCF against TTF provided by your bank? By 2025, what do you expect to be the proportion of SCF against TTF provided by your bank?

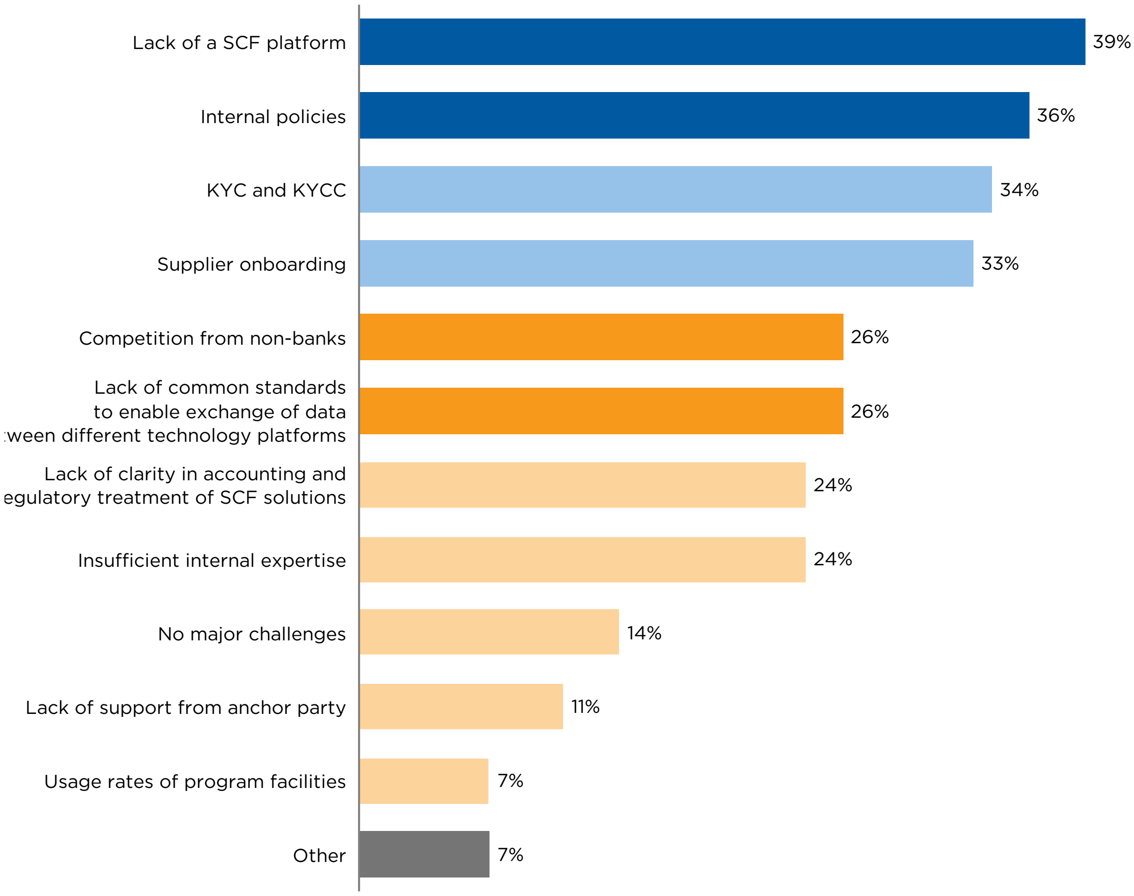


Lack of an SCF platform and aligning internal policies to SCF are the primary concerns of respondents (Figure 58). As referenced above in Figure 55, the majority of respondents who offer an SCF platform have developed their own system; it seems the development of a system is highly prohibitive to banks not yet offering SCF solutions.

KYC and supplier onboarding are concerns, with one in three respondents citing these as major challenges. Further, a quarter of banks surveyed were concerned about competition from non-banks and lack of common standards to enable the exchange of data.

Ensuring that banks of all types are provided with guidelines and support to understand and implement SCF solutions should be an industry priority in the coming years. Indeed, the barriers to the adoption of SCF solutions cited by many banks in our survey are highly solvable – with the right tools. Fortunately, as SCF has grown in popularity, it has also grown in maturity; industry bodies such as the ICC, BAFT, the ITFA, FCI and the EBA, through the Global Supply Chain Finance Forum (GSCFF), work to drive the evolution of SCF and to advocate for its appropriate, transparent, and properly reported use in support of domestic and international commerce. Industry leaders and practitioners have a responsibility and an opportunity to advance thoughtful, informed dialogue with corporates, banks, governments and regulators to maximise a common understanding of SCF techniques and to begin setting the necessary standards globally.

Figure 58
What are the major challenges, if any, your bank faces in delivering SCF solutions to your customers?



FEATURE

Supply chain finance: evolution or implosion?

ICC Global Survey Editorial Committee

Supply chain finance is increasingly recognised as an important and growing solution set in the financing of international trade – high-value, strategically important economic activity worth about USD 25 trillion per year if we count merchandise and service sector trade. Up to 80%, or about USD 16 trillion, of merchandise trade is said to depend upon some form of trade finance, with the fast-growing service sector inexorably developing an increasing need for trade finance.

SCF, an umbrella term that covers multiple techniques, aims to address the vast majority of trade today that takes place on open account terms, with the remaining 10% or so on the merchandise trade side enabled through more traditional trade finance mechanisms such as documentary letters of credit and documentary collections.

SCF has been showing promising signs of growth and wider adoption, with one of its variations or techniques, payables finance, providing a viable mechanism for enhancing the cash flow of both the buyer and the seller in a cross-border supply chain. Such programs, where a buyer extends terms to improve its own financial health while simultaneously offering discount options to suppliers, are even encouraged in a couple of key jurisdictions as a means of addressing systemic liquidity issues and SME finance challenges.

A nascent proposition in the market, SCF as a whole (though not all techniques under that umbrella term) is beset by a lack of common understanding and clarity around what is deemed ‘appropriate practice’, and by the absence of definitive guidance on accounting treatment and reporting requirements.

This reality creates a context in which innovation can thrive. However, it also indirectly enables boundary-pushing practices, some of which should be welcomed and supported, and others which are questionable at best, or even outright abuses aimed at obscuring commercial and financial realities.

The evolving nature and thus far limted development of of clear and agreed industry standards and accepted practice, to say nothing of the absence of ICC rules, opinions, and guidance which have provided critical parameters in traditional trade finance since 1933, amplifies the situation. Though this is natural given the early stage in which SCF exists at the moment, those very same characteristics, coupled with the entry of unregulated fintechs and non-bank financiers into SCF, create a perfect storm of innovation plus potential abuse.

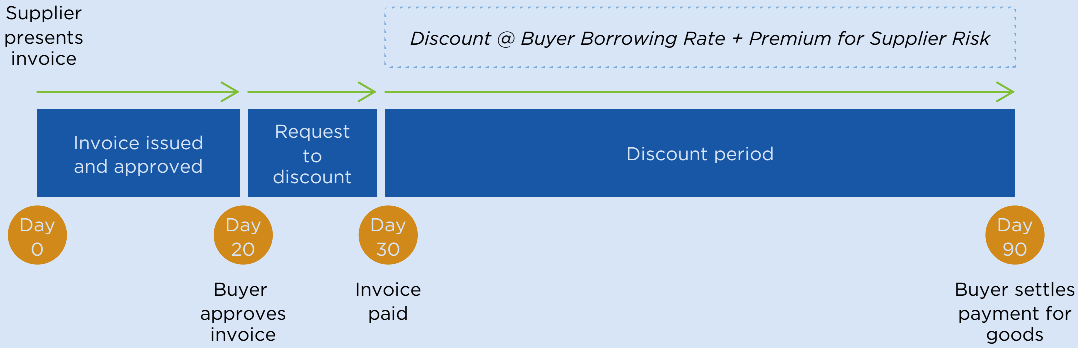
Trade finance and more specifically SCF have been the subject of unaccustomed levels of attention from the press, ratings agencies and regulatory authorities, partly off the back of a very few, but highly visible commercial failures linked to payables finance and partly as a result of market activities that trigger reactions across a range of stakeholders.

Thoughtful and well-informed questions are important and welcome, as are genuine efforts to shine the light of truth on SCF practices around the globe. Sensationalist postures by writers or by others seeking to earn political points are less constructive and should be countered by more rigorous discourse.

Unbalanced postures pose an existential threat to a set of financing solutions that could prove powerfully effective in advancing economic inclusion and trade-based growth.

Contrary to some of the coverage, which highlights the extension of terms as an abuse of SMEs through payables finance, the complete picture on this technique is

Figure 59
Payables finance in action



that terms are extended to benefit the large buyers, while participating SMEs have the option to secure immediate payment at a discount to the face value of invoices, at rates linked to the credit quality and (often lower) borrowing cost of the large buyer.

Are there alternatives, like mandated accelerated payment standards? Possibly, but these could arguably represent a market-distorting policy option as opposed to a commercial practice. Their use becomes a matter of political choice. Could the cashflow situation of MSME suppliers be improved by reducing transaction timeframes through technology or enhanced processes? Probably.

The specific characteristics of a payables finance program can vary – from the scope of coverage of suppliers, to the cost of discount and the degree of extension of terms. It is in the detail of program structure that definitions of accepted practice and the value of industry guidance plus regulatory and standards body direction can be critically important.

Should the option to extend payment terms through payables finance be open-ended, for example? In the absence of guidance and direction, some very credible and legitimate practitioners are happy to structure programs that extend out beyond 24 months, whereas others are developing an argument that term extensions ought to be guided by the typical working capital cycle of an industry sector. Other questions arise around the types of invoicing (and therefore underlying commercial or trade activity) that should be considered in-scope for payables finance.

In the end, payables finance presents a significant opportunity to enable the flow of liquidity across domestic and international supply chains, down into the so-called ‘long tail’ where MSMEs occupy an important space. Its appropriate use and structuring ought to be determined through a thoughtful, coordinated, and decisive set of steps involving press and ratings agencies, accountancy bodies and firms, regulators, trade industry bodies, finance providers, and corporates as well as MSMEs.

Whether or not boundary-testing practices (including financial and regulatory reporting) or structures will be tolerated by authorities, it is clear at this moment that some form of accepted framing of payables finance is necessary and important. Anything outside of those agreed boundaries may well be a valuable addition but should be clearly distinguished from SCF and payables finance.

SUSTAINABILITY

Survey analysis

Global trade has no way of hiding from the climate change challenge: its business-as-usual operations have long been susceptible to disruption from extreme weather events, and it is increasingly being forced to adapt to new regulations targeting carbon-heavy industries that directly impact their viability. It is imperative for banks to not only nominally support sustainable trade, but to integrate sustainability into their trade finance policies and day-to-day activities (such as supply chain finance). At the same time, sustainability should not just be viewed solely or exclusively through the lens of climate change, but rather, by reference to the widest definitions of sustainability which include environmental, social and governance (ESG) issues among others.

In the survey, 66% of respondents say that they have a sustainability strategy that applies to trade finance and SCF (Figure 60); we would expect – and hope – for this to climb to much closer to 100% in the future editions of the Global Survey, perhaps emulating the rapid shift in focus on ESG which has now become central to investment management and strategy, physical supply chain management, public procurement and a host of other areas. Indeed, as enablers of international trade, trade banks have a critical role and influential opportunity to drive changes in business practices and behaviours globally for the better.

Western European banks are leading the way in this area, with three-quarters having a sustainability strategy. More broadly, these strategies were primarily adopted due to credit and reputational risk (38%), as well as client expectations (35%) (Figure 61). These are likely also influenced by banks' group-wide policies and initiatives towards sustainability. Regulatory requirements are less of a driver across all geographies. However, this is likely to change in the coming years as new regulations come into force.

Figure 60
Does your bank have a sustainability strategy that applies to trade finance and supply chain finance?

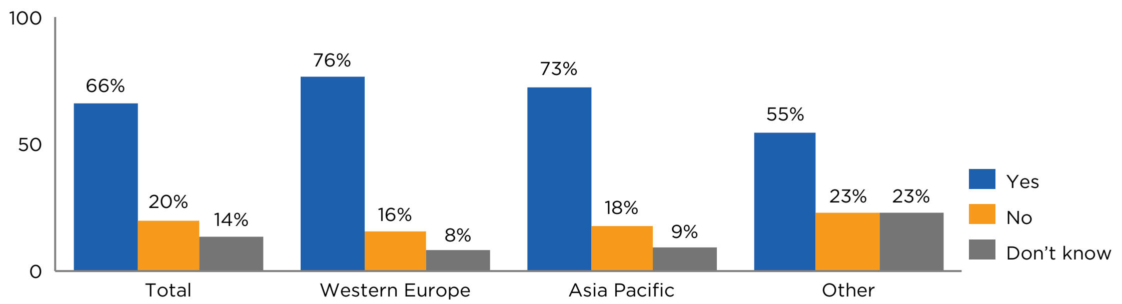
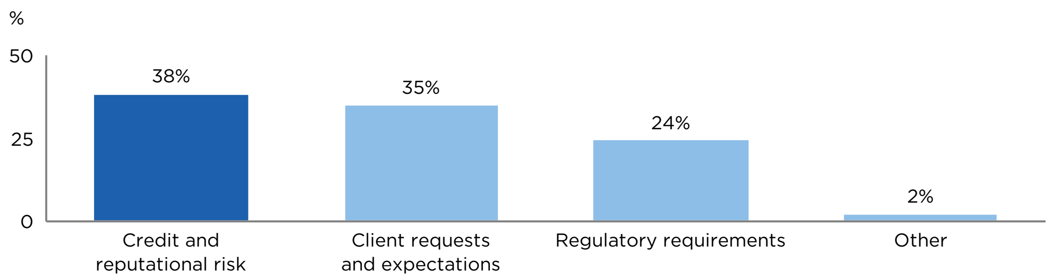


Figure 61
What, if any of the following, is the primary reason your bank has adopted a sustainability strategy?



The survey demonstrates that banks of all types are increasingly coming to terms with the need for a sustainability strategy in trade. The available evidence points to the integration of sustainability policies now – not just as a longer-term goal. Indeed, 76% of respondents indicated that they are already integrating sustainability-related due diligence in respect of KYC and other credit risk adjudication and management policies (Figure 62 and Figure 63). Further, 61% of respondents said that their bank has rejected trade finance applications in the past year as they didn't meet their bank's internal policies on ESG risks (Figure 63).

Figure 62
Is your bank integrating sustainability risks into credit risk management procedures for clients using trade finance/ supply chain finance instruments?

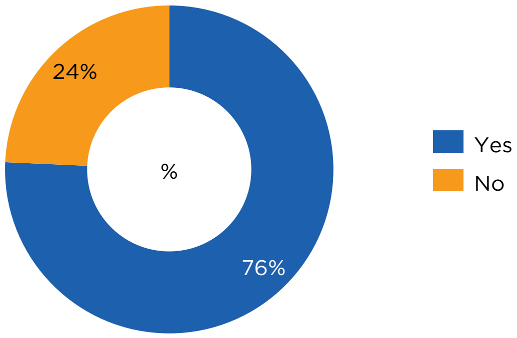


Figure 63
Is your bank conducting sustainability-related due diligence in its trade finance operations as part of KYC procedures?

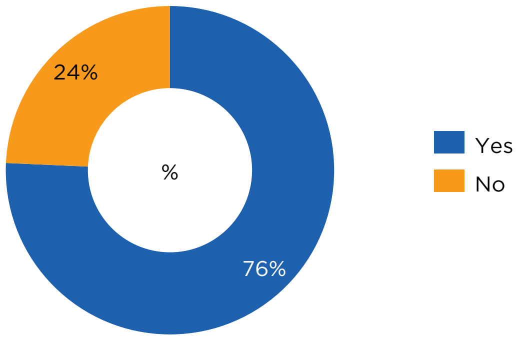
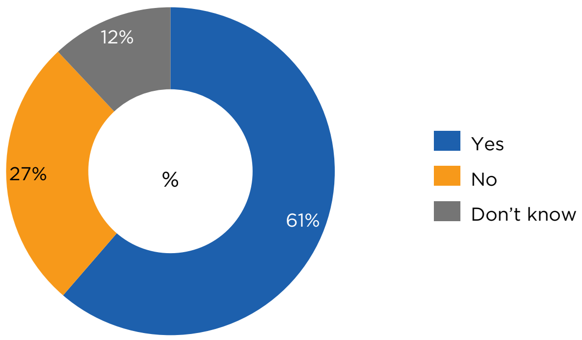


Figure 64
Did your bank reject any trade finance applications due to ESG risks with clients?



From a demand perspective, almost half of banks feel their clients are requesting innovative finance mechanisms to help them implement more sustainable strategies and operations (Figure 65), highlighting a clear expectation for trade banks to play their part in driving sustainability and advancing ESG considerations in trade. Customers want their banks to be proactive, and not just reactive.

There is strong agreement that climate change and the environment should be priorities for banks, with survey respondents ranking these areas as their key sustainability priorities (Figure 66). Banks continue to interpret sustainability as climate-related. At the same time, there is opportunity for banks to recognise the critical role that trade and trade finance provision play in other pressing social issues, such as the eradication of forced child labour, promoting financial inclusion of women, and the broader fight for gender equality, among numerous others. This fast-emerging reality mirrors the increasing responsibility faced by buyers for the actions and behaviours of members of their supply chain – no matter how small or how remotely located they may be. The human cost, and increasingly the regulatory expectations and reputational impact – good or bad – are transforming the way these issues are prioritised and addressed around the globe.

Figure 65

Are your trade finance clients requesting innovative finance mechanisms for implementing more sustainable strategies and operations?

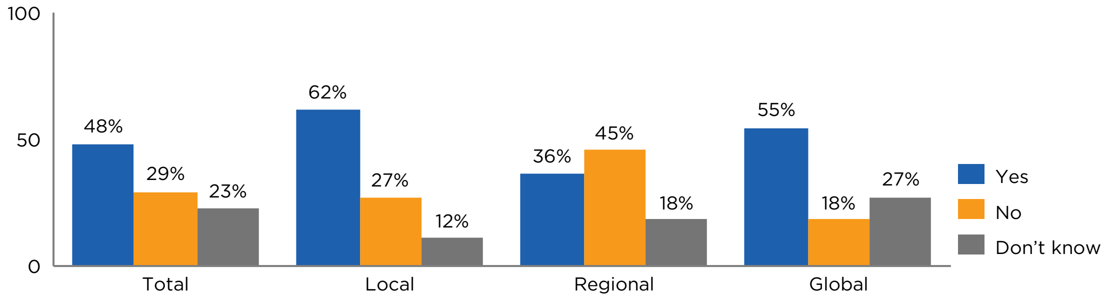
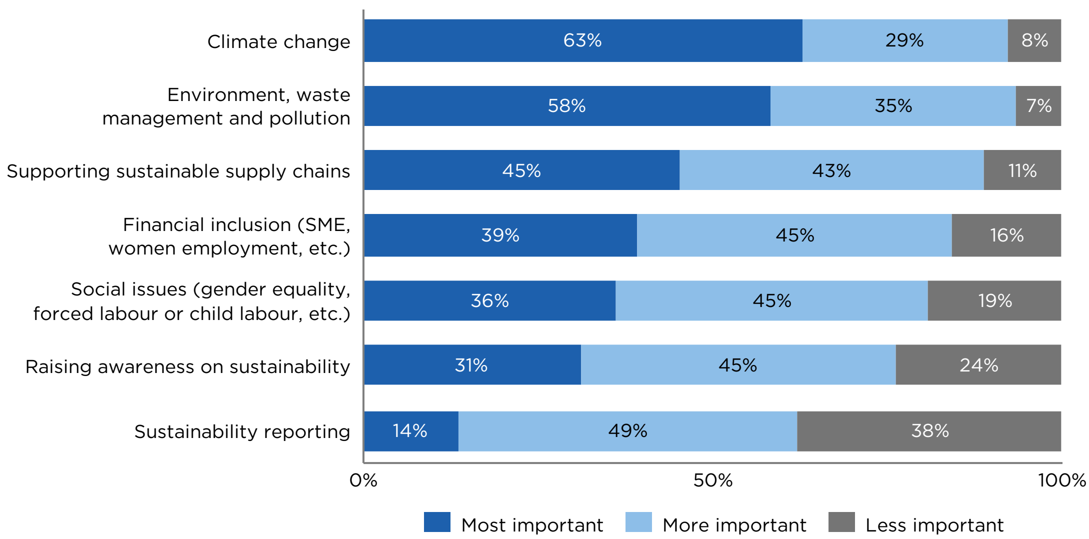


Figure 66

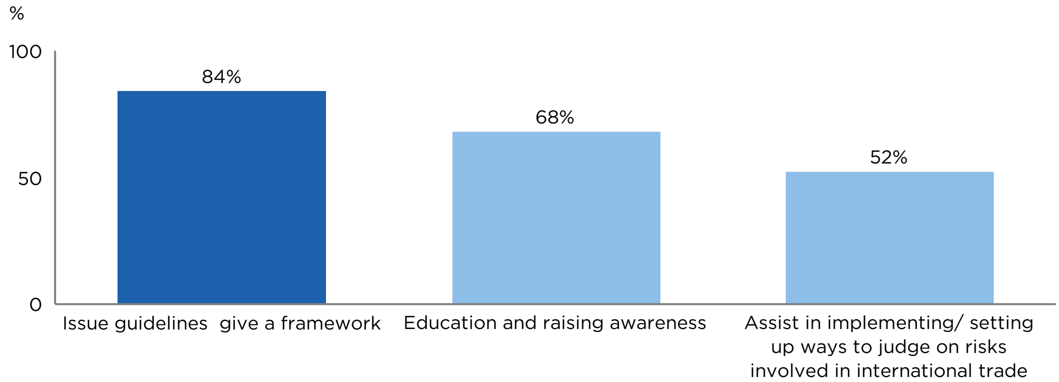
What should be the sustainability priorities for banks in trade finance over the next five years?



While banks indicate sustainability as a core business priority, there is a clear desire for structured support and formal guidelines to support them in this transition. 84% of survey respondents indicate that the ICC Banking Commission could add value by providing these tools (Figure 67).

The ICC is active at the highest levels of advocacy around climate change and sustainability, and the ICC Banking Commission has a well-established Working Group on Sustainable Trade Finance. In 2019, for example, ICC organised a series of consultations bringing together high-level business leaders, policy makers, academic experts, economists, and thought leaders to discuss the nexus between international trade and climate change. However, there is clearly room to continue and expand our contributions in this area: an opportunity that will rise in priority as more of our members adopt sustainability as a key part of their business.

Figure 67
Where/ how can the ICC Banking Commission add value to sustainability in trade finance?



FEATURE

ICC: accelerating progress on sustainable trade finance

Roberto Leva, Trade & Supply Chain Finance Relationship Manager Asian Development Bank; Co-Chair, ICC Sustainability Working Group
Harriette Resnick, Co-Chair, ICC Sustainability Working Group

Introduction

It is no longer a question whether banks that provide trade finance should allocate their capital in a way that promotes sustainable ESG practices by their customers. The question now is how to get it done at scale within the critical next decade.

The reasons why are evident to anyone following world events; major fires, sea-level rise and coastal erosion, flooding, heat waves and droughts, deforestation and biodiversity loss are all occurring with alarming frequency across the globe. Regulatory authorities, as well as customers, investors, and employees, are focusing on whether these global threats pose prudential risks to banks and the extent to which their portfolios are aligned, or out of sync, with sustainable development goals.

In response to these challenges, the ICC Banking Commission's Working Group on Sustainable Trade Finance has developed database tools and guidance that can help banks identify and mitigate their exposure to risks arising from adverse environmental and social effects of customers' operations and supply chains. Through four work streams, members from commercial banks, multilateral development institutions, and other trade experts are exploring how to accelerate the use of trade finance to encourage sustainable business practices.[1] The objectives and achievements of the working group to date, which are consistent with ICC's, ADB's and many member organisations' commitment to climate action and promotion of green and inclusive growth, are described below.

Process and principles

This work stream has created tools and guidelines that enable trade bankers to identify sustainability risks arising from trade finance transactions and to speak to their customers about them. Its objective is to drive integration of these tools and guidelines into operational processes, in line with individual banks' risk management strategies and ESG, reputational, and credit risk policies.

To facilitate trade bankers' access to key ESG information, work stream leaders Nigel Beck and Lindokuhle Ndlangamandla of Standard Bank have collaborated on International Finance Corporation's development of a new version of its Global Map of Environmental and Social Risks in Agro-Commodity Production (GMAP) database.[2] In addition to highlighting such risks arising in over 250 country/ commodity scenarios, GMAP now integrates information from the International Trade Centre's (ITC) Standards Map that specifies which voluntary certification authorities are available for those scenarios and whether their requirements address the high risks identified by GMAP. Targeted next steps are to improve ease of access to GMAP/ ITC data, potentially through developing an interface for an automated feed into user systems, and to cover other country/ soft commodity risk scenarios.

1 The working group, led by Harriette Resnick, independent advisor, and Roberto Leva, Trade and Supply Chain finance specialist at the Asian Development Bank, has also benefitted from the input of talented young professionals participating in the Banking Commission's Successors in Trade program
2 GMAP was created by IFC with the assistance of World Wildlife Fund, drawing on the IFC 2012 Performance Standards on Environmental and Social Sustainability. To get access to the full GMAP data, register without charge through this link: gmaptool.org/register. A webinar on the integrated GMAP tool is available at: youtube.com/watch?v=0HLXlexzJN4&feature=youtu.be)

In addition, inspired by the due diligence process used by banks to comply with KYC requirements, working group co-head Roberto Leva of the Asian Development Bank spearheaded the development of sustainable trade finance Customer Due Diligence Guidelines. The guidelines include a questionnaire that can form part of a client-level review, designed to help relationship bankers identify whether a customer's operations or supply chain pose ESG risks. They also aid them in evaluating customer responses to determine whether the client is taking appropriate steps to mitigate those risks. To minimise customer workload from duplicative information requests, SWIFT is currently working to incorporate the questionnaire as an optional feature of its new Corporate KYC Registry.[1]

We are soliciting feedback on these tools, both from banks and corporates, to validate their utility and highlight potential areas for improvement.

Training

This work stream, with Roberto Leva as its leader, aims to develop training materials to raise awareness of the risks faced by banks if they finance customers who fail to manage adverse ESG impacts. In addition to case studies that provide examples of these risks, we aim to spotlight business opportunities that encourage sustainable practices. Training resources will also highlight the tools and guidelines described above. The first step will be the creation of a podcast sponsored by the Asian Development Bank, in collaboration with the ICC Academy, to be widely available to the industry in 2020, to assess further interest in additional content. Following the podcast, the working group, the Asian Development Bank, and the ICC Academy will evaluate the need for the creation of online training to be accessed via the ICC Academy platform.

Regulation, policy and green finance: definitions and taxonomies

The regulatory landscape relating to 'sustainable finance' is evolving quickly. Taxonomies to define that term have been developed by the EU and other jurisdictions for a range of economic activities.[2] Central banks and supervisory authorities recognise, and are taking steps to address, the prudential risk to financial institutions created by climate change and other ESG challenges, and the need to promote sustainable transactions.[3] Banks may soon be required to conduct stress testing through portfolio reviews that assess exposure to climate change impacts.[4] They may also be asked to disclose the extent to which they have financed 'green' transactions, or have exposure to customers whose business results in climate-related physical or transition risks or other adverse environmental or social impacts.[5]

In response to these developments, the working group has initiated two new work streams. The first, led by Merisa Lee Gimpel of Lloyds Bank, will seek to develop support for the proposition that sustainable operations and supply chains reduce default rates for customers' trade finance transactions. As part of this inquiry, they will consider what data is needed to make this case. This stream will also examine the policy ramifications, i.e. whether sustainable trade finance merits capital relief, or should improve a company's credit rating, as well as what other incentives are needed to encourage the funding of 'green' trade transactions.

1 swift.com/news-events/news/enabling-smoother-know-your-customer-kyc_processes-for-corporates
2 See, for example, ec.europa.eu/info/files/200309-sustainable-finance-teg-final-report-taxonomy_en ("Final TEG Report)
3 or information about the Network for Greening the Financial System, see ngfs.net/en; centralbanking.com/awards/4662326/green-initiative-network-for-greening-the-financial-system
4 See, for example, bankofengland.co.uk/paper/2019/biennial-exploratory-scenario-climate-change-discussion-paper
5 See, for example, fsb-tcfd.org/; Final TEG Report at 9

Under the leadership of Simon Connell of Standard Chartered Bank, the other new work stream aims to define 'sustainable trade finance' with greater specificity[1] and in line with regulatory developments. The objective is to help identify which trade transactions will meet the growing demand for sustainable assets that is being encouraged by public policy measures. Focusing initially on the traditional trade and supply chain finance products covered in the ICC Trade Register, work stream participants will review whether current definitions of sustainable investments from ongoing taxonomy initiatives can be leveraged to apply to these trade structures, starting with a few sample business sectors and their related taxonomy criteria.

Conclusion

Throughout its history, the ICC Banking Commission has developed rules and best practice standards that have helped trade finance to flourish, both as critical, trade-enabling commercial activity, and more recently as an asset class. The Sustainable Trade Finance Working Group's ongoing efforts to define the pathway for sustainable trade and expand its positive impact continues that important tradition.

1 To date, our working definition has been the provision of traditional trade and supply chain finance products to support "the business and activities of buying and selling commodities, goods and services that meet environmental, social and economic criteria capable of benefitting all actors involved and minimizing adverse impact while fostering sustainable global development." iccwbo.org/publication/global-survey-2018-securing-future-growth/

REGULATION AND COMPLIANCE

Survey analysis

Over the past few years, the growing use of digital solutions by banks has enhanced their ability to assess risk and combat criminal activity. However, the increasing sophistication of criminal and terrorist organisations has been accompanied by a growing regulatory regime aimed at stamping out criminal activity from the financial system and from global trade. This trend, along with new capital requirements from the Basel Committee, presents significant concern to banks across the world – particularly in respect of the resources needed to meet the increasing complexity of regulation and compliance policies.

56% of survey respondents indicated that their banks were significantly concerned both by understanding and implementing compliance procedures, and with capital and regulatory requirements (Figure 68 and Figure 69).

However, while there was widespread similarity across banks on capital and regulatory requirements, there was a more pronounced divide between different types of banks in respect of compliance. While 74% of global banks and 68% of regional banks indicated that they were extremely concerned by the need to implement compliance procedures, only 35% of local banks said the same. This, unsurprisingly, suggests that navigating the complexity of compliance rules and regulations may have the most pronounced impact on trade banks that operate across multiple countries and jurisdictions.

Figure 68
How concerned is your bank with understanding and implementing compliance procedures?

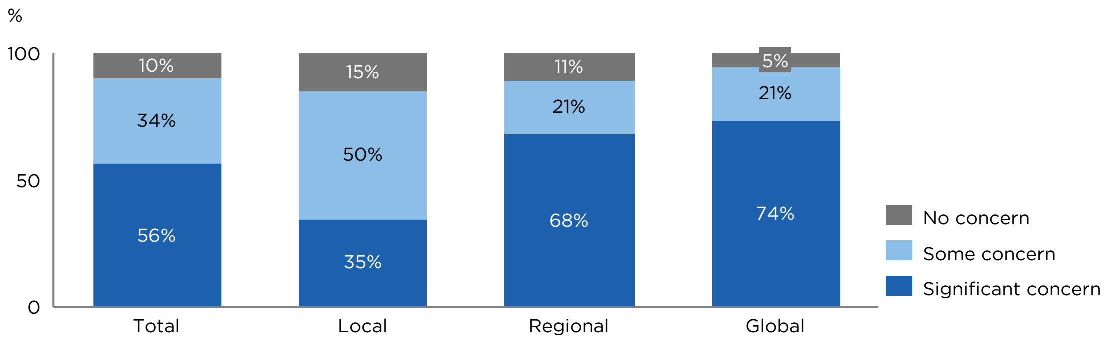
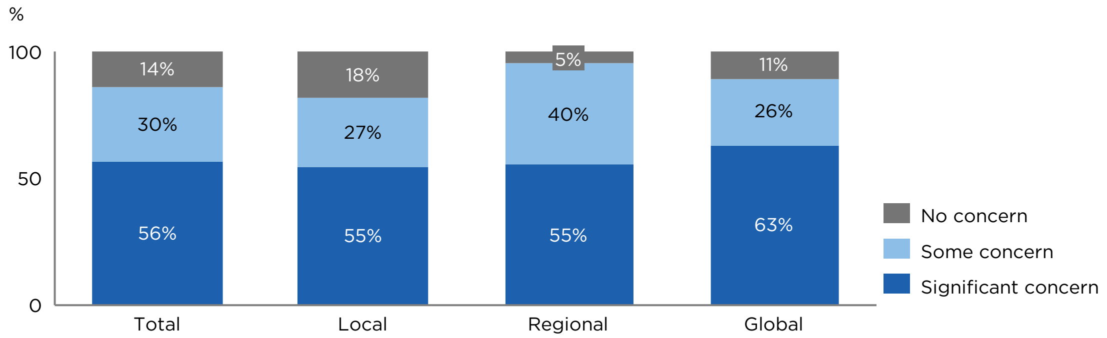


Figure 69
How concerned is your bank with capital and regulatory requirements?



The impact of an increasingly complex regulatory regime has been felt by banks across geographies. We asked banks to give a sense of the FTE increase needed over the past decade to understand and implement new financial crime policies. 40% of respondents said that they have been required to increase their staff by 20% or more (Figure 70); among banks based in Western Europe this number rises to 55%. Furthermore, when asked how due diligence transaction and client monitoring capabilities have evolved in the past year alone, many respondents cited an increase in staff numbers. This clearly has a material impact on operational costs for trade banks – which is likely to be passed on to customers in the form of higher prices or may have the unintended adverse consequence of reducing overall industry capacity to provide trade finance.

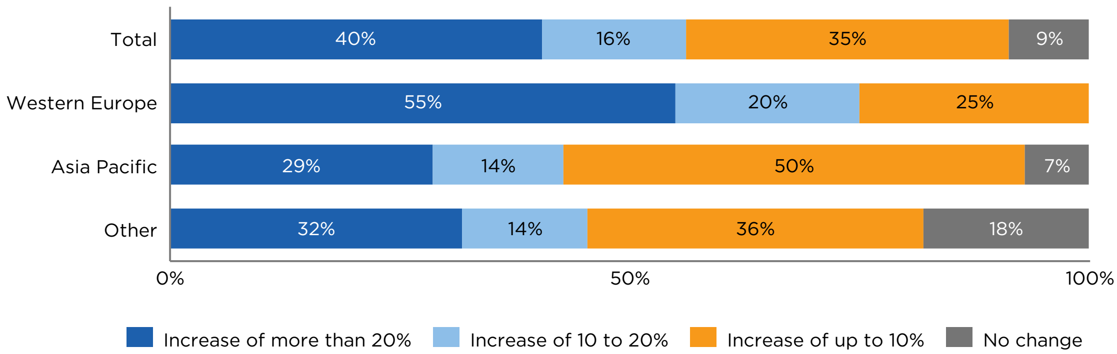
The unintended impact of regulation arising, for example, from cross-border inconsistency or material variations in standards of compliance, can be profound: the complexity and/ or cost of compliance may result in banks being less able to cost-effectively support trade. This is most relevant for MSMEs, who are often seen to be the highest risk and therefore need the most onerous checks but bring in the lowest revenue per transaction.

As such, AML, KYC, and other regulations are alleged to be a key contributor to many banks underserving the SME market. However, at the same time, very few banks would argue against the need for such regulation, and therefore the key question remains: how can regulatory authorities and banks together achieve an optimal balance between regulatory efficacy and assured access to timely and affordable trade finance?

Banks may debate the expectations – implicit and explicit – from authorities that the financial sector ought to become more central to investigative, intelligence, and prosecutorial activity, and regulators may indicate that the commercial impact of compliance costs is irrelevant. In reality, the path forward is one that leverages technology but is built on a foundation of effective collaboration between banks, governments, regulators, and industry bodies.

Figure 70

Compared to ten years ago, can you give an estimation of the increase of FTEs that has been needed to implement financial crime policies in your bank?



Operationally, since 2018, most banks have seen either an increase or no change in the number of alerts of suspicious activity, false positives and trade finance red flags, with only a small minority reporting a decline (Figure 71). For the significant number of respondents who indicated an increase in 2019 across the three measures, it is challenging to ascertain whether this trend is good news (i.e. the numbers are increasing due to improved bank operations and digital solutions to detect criminal activity) or a sign of increasing criminal sophistication and usage of trade channels.

For the trade banks implementing machine learning-based controls, reducing the number of false positives is a critical Key Performance Indicator (KPI) in the cost effectiveness of this technology, and many are pushing to bring false positives to well below 15%.

Financial intelligence units report anecdotally that 'defensive' filings of Suspicious Activity Reports (SARs, also called Suspicious Transaction Reports and Suspicious Matter Reports) generate material volumes of content for authorities to review, with little actionable intelligence arising when such reports are filed based on an overabundance of caution – 'just in case' – by banks. Efforts are underway by the Asian Development Bank, following publication of the ADB's Trade Finance Scorecard: Regulation and Market Feedback, to advance collaboration and to advocate for the inclusion of selected common (and

Figure 71
Please indicate for each of the following if the number has increased, decreased, or remained the same when compared to 2018

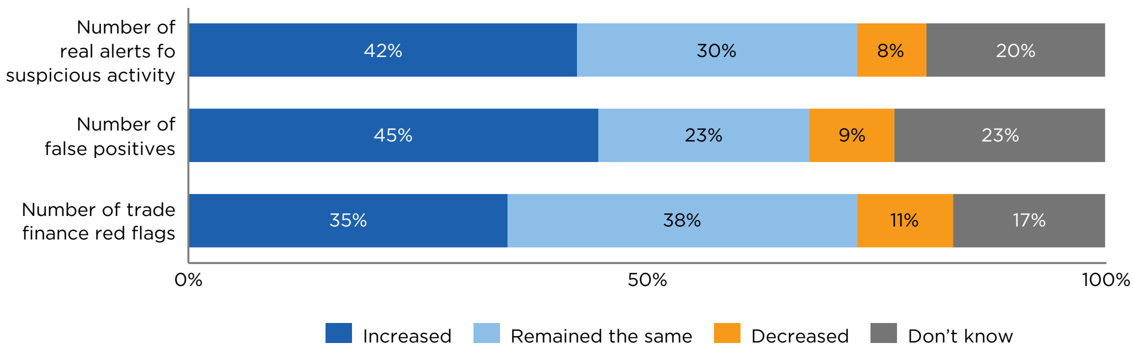
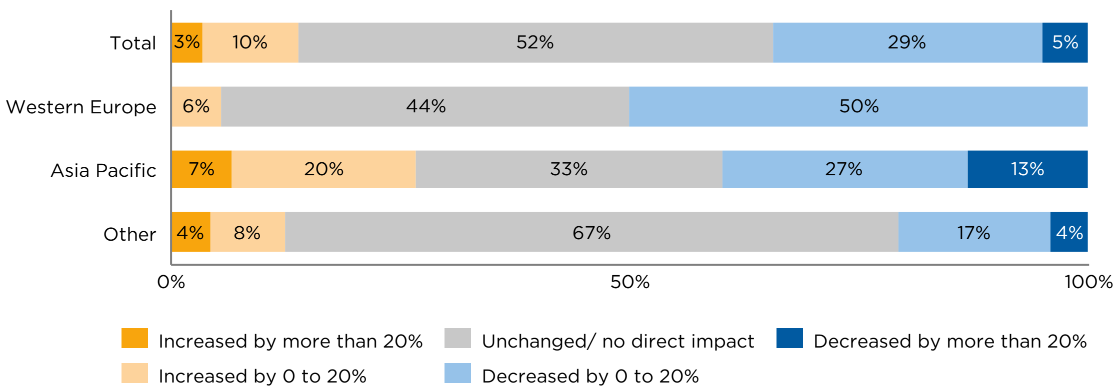


Figure 72
To what extent has the regulation implementation measures relating to financial crime and AML impacted your trade finance business (in transaction volumes)?



structured) data elements in SARs, and to enable cross-jurisdiction investigations and follow-ups between intelligence and investigative agencies and others. This is with the direct intent of reducing the adverse impact on trade finance while concurrently helping to improve the value of SARs in generating actionable intelligence.

We also asked banks to estimate the impact on their trade finance volumes as a result of AML and financial crime policies. Over half of respondents said that these regulations had no direct impact on transaction volumes (Figure 72), and a further 34% indicated a decrease. However, there are relatively sharp divergences across different geographies.

In Western Europe, 50% of respondents said such policies had a negative impact on transaction volumes, with 44% indicating no direct impact. While we may have expected a greater proportion of respondents to indicate a reduction in flows as a result of financial crime regulation, it is encouraging to see how banks have been able to adapt.

KYC regulation and AML policies have increased the regulatory imperatives faced by trade banks in recent years. Manual data provision by customers and slow verification processes can delay or even prevent banks from supporting transactions in a commercially timely manner, impeding the building of new customer relationships.

Figure 73
Please indicate which, if any, of the following KYC utilities your bank is using?

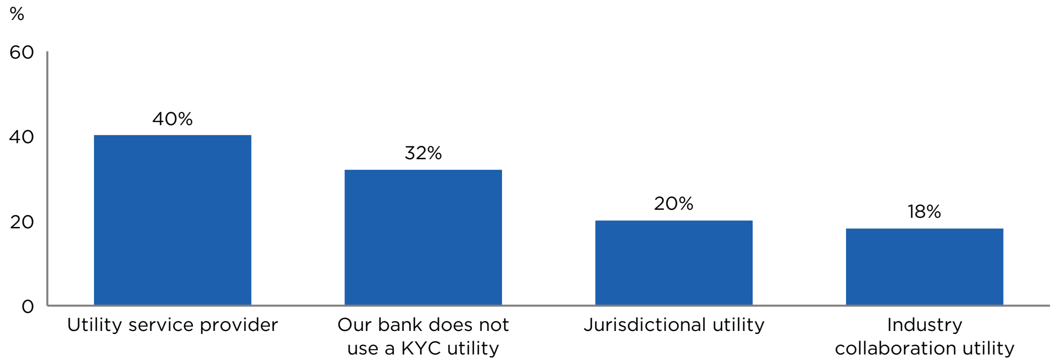
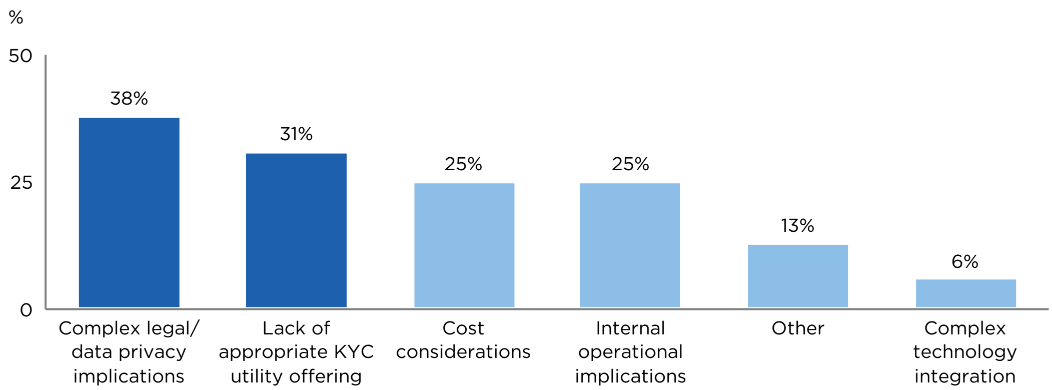


Figure 74
For what reasons does your bank not use a KYC utility?

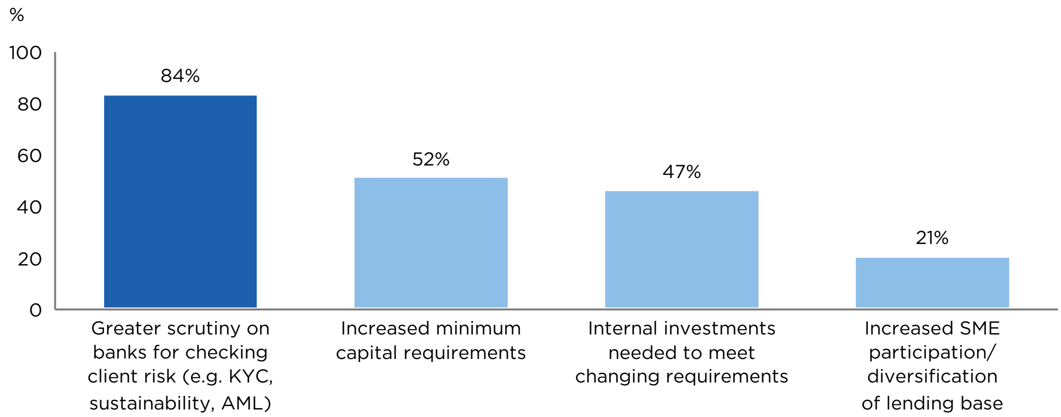


KYC utilities aim to ease this process for trade banks by standardising data and risk operations and enabling industry collaboration. However, when asked which KYC utilities banks were using, 32% indicated that they were not using one at all (Figure 73). Of the remaining respondents, 40% indicated that they were using a utility service provider to manage their KYC risk monitoring and operations, 20% were using a jurisdictional utility, and 18% were using an industry collaboration utility. Of the one-third of respondents not using a KYC utility, 38% indicated legal and privacy implications as the main reason (Figure 74) A further 31% said that there was no satisfactory utility offering available. Only 6% were discouraged by the cost and complexity of technology integration.

Looking ahead, the survey indicates that banks do not expect regulatory scrutiny to abate. 84% of respondents anticipate added pressure to check client risks (Figure 75) from KYC and AML policies to sustainability requirements. In line with this, digitised KYC and AML processes were the most frequent single change that respondents believe would improve efficacy in compliance activities. Other respondents would like to see increased guidance from regulators. One respondent voicing a common view across the industry stated that they would like to see “clearer and more consistent direction from regulators on compliance requirements”.

52% of respondents anticipate an increase in minimum capital requirements, while 47% expect that their banks will need to

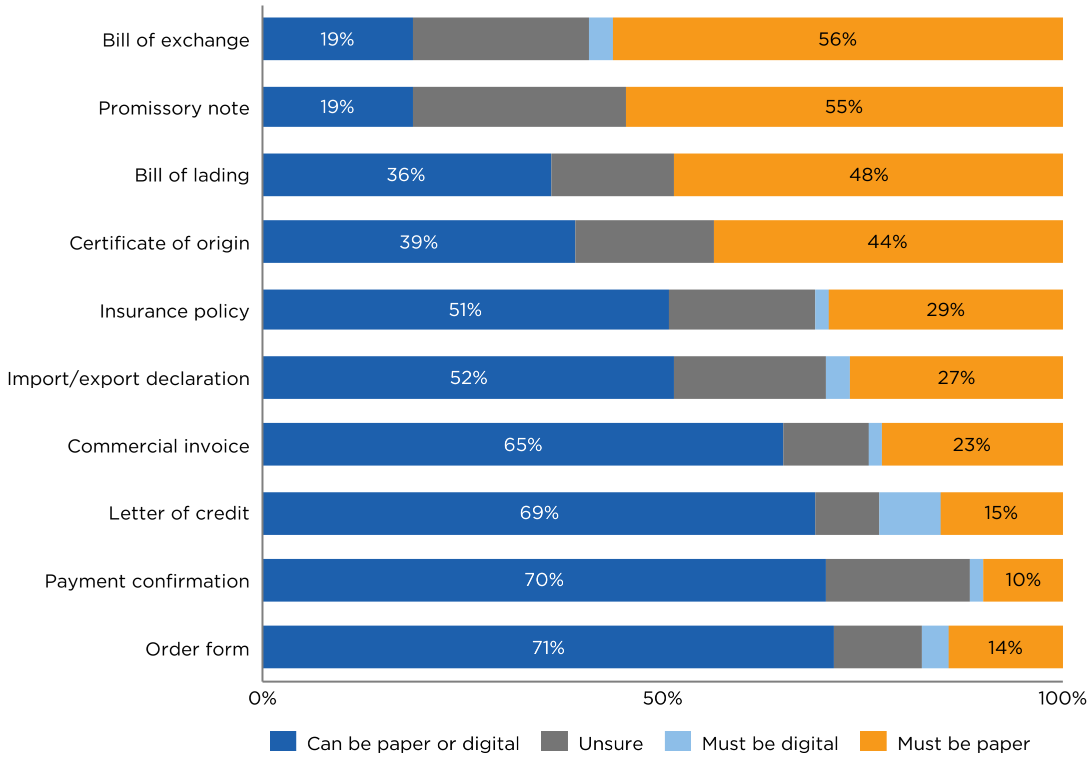
Figure 75
As regulation becomes stricter, what challenges/ requirements do you see being imposed on banks going forward?



make further investments in their internal operations to meet this expectation. There is a strong sense that knowledge sharing and collaboration across the industry would improve the ability to adhere to regulatory and compliance requirements, suggesting a wider adoption of KYC utilities in the future. The growing receptiveness of regulatory authorities to engage with industry through public-private partnerships such as the UK's Joint Money Laundering Intelligence Task Force or AUSTRAC's Fintel Alliance is a constructive development with promising potential. Progress on compliance-related data-sharing across borders would be an important complement, and should be achievable while respecting local and regional privacy law.

While regulation has become more complex in some areas, it appears to be starting to modernise to enable more digitised trade. For most trade documentation, over 50% of respondents mentioned that documentation was no longer mandated to be paper-based in the context of trade financing (Figure 76). The challenge, however, is that for trade to truly digitise, all end-to-end documentation – including bills of lading and certificates of origin, which in many markets still need to be physical – must be able to be digitised. Digital documents or digital data extracts must be more widely recognised as having legal standing. Digital documentation would also be required in both the importer's and exporter's jurisdictions. This makes it clear that local regulations and requirements remain a barrier to paperless trade. Digital trade is explored in more detail in the next section.

Figure 76
Which of these documents are legally required to be paper in your home jurisdiction?



FEATURE

Regulations in a digital world

Felix Prevost, Senior Capital Manager, GTRF, HSBC

When horse-drawn carts became prevalent and streets crowded, France introduced rules mandating that they stay on the right to reduce accidents and improve traffic flow. The UK chose the left. Whatever their reasons, be it to free coach drivers to manipulate whip or sword, a system of codified rules emerged to support ever faster and larger coaches. When the first motorised vehicles appeared, some states required a footman to precede the automobile to announce its presence and ensure clear passage. The rules of the road continued to evolve, and today self-driving cars are on the streets of multiple cities around the world.

Over the past two centuries, international trade has rocketed. Innovations in technology support ever more goods to move around the world in complex global supply chains. The advent of steam-powered ships allowed bigger and faster ships. Containerised shipping allowed faster loading and unloading of ships with fewer breakages. Finance of international trade, though, has barely changed since the invention of paper money: a letter of credit is a commercial bank's promise to pay, just like currency notes today are simply a note issuer's promise to pay the bearer on demand.

Digital innovations in the space of communication, computing and banking promise to change trade finance. The question we ask is whether regulations can evolve to support these digital innovations? To answer this, we must turn to the risks that the current regulatory regimes seek to address.

Communication

The world communicates electronically. We send emails, text, call, and videoconference around the world. Why do we still sign and mail physical contracts? Regulations around physical documents assume that physical presence ensures uniqueness (there is only one contract and no other false copy), acceptance (the signature proves that the counterparty has seen and accepted the terms of the contract), and legality (how else can I show this is legal unless I have a physical record?).

Until distributed ledger encryption (Blockchain) provides a suitably acceptable ecosystem for record-keeping of contracts (fix the terms in perpetuity for future record review, record who viewed and accepted the terms, etc.), electronic signatures and digital contracts provide an intermediate step which can achieve similar purposes as those of a physical contract. The European Union Electronic Identification, Authentication and Trust Services (eIDAS) regulation goes a long way in showing how regulation can support this digital solution to physical records.

In international trade, documents have multiple uses; however, at its core trade finance intermediated by banks helps build trust between buyers and sellers by ensuring, for example, that bills of lading, which enable the holder to claim and collect goods, are only released by the seller to the buyer once payment is ensured. As of now, most of these documents remain paper-based as they are not yet widely accepted electronically. Paper documents require manual processing and time-consuming and costly air freight delivery from the seller to their bank to the buyer's bank and onwards to the buyer. Digitising the paperwork could save on operating costs for each party in the chain (e.g. no postage), reduce operational risk (e.g. lost documents, incorrectly read documents), improve carbon footprint (e.g. no post by air), enable governments to enhance and accelerate their customs controls (e.g. automated submission of documents for customs pre-checks while goods are in transit) and ensure no tax evasion (e.g. one electronic submission to both exporting and importing customs offices preventing mislabelling or mis-valuing of shipment).

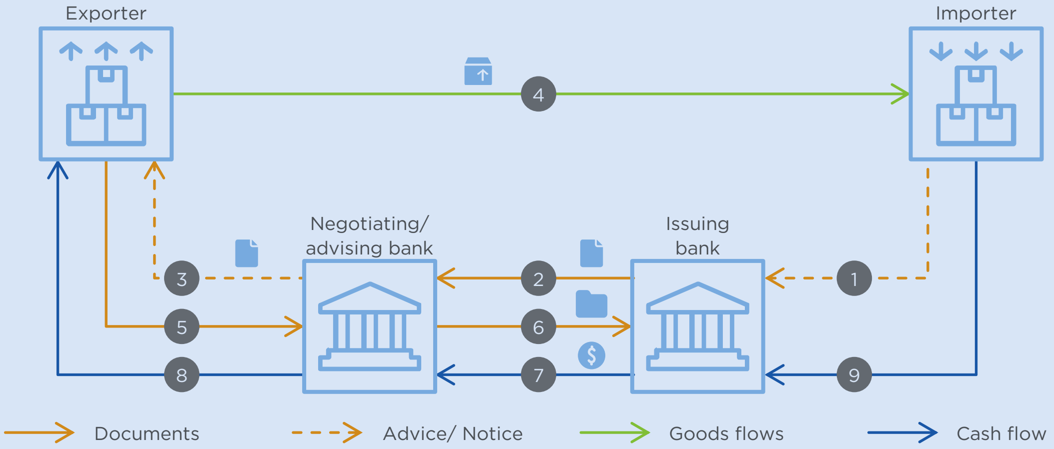
Evidently, all interested parties will need to move jointly together to support digitisation of trade documentation. If any one party, such as a customs officer or a freight forwarder, still requires a paper document by law or practice, then that document will need to be created and posted between the other actors. According to the World Economic Forum and the United Nations, a supportive regulatory framework covering banking, insurance, contract law, and customs as set out by the UN Economic and Social Commission for the Asia-Pacific (UNESCAP) could reduce annual trading costs by up to USD 7 billion and increase exports by USD 257 billion in Asia alone.

Computing

In the second half of the twentieth century, banks were among the first to adopt computers widely. Notwithstanding the tens of billions of dollars spent on bank IT each year, their core systems remain stuck in the days of green screens. As banks worldwide wrestle with creaking mainframes, two computing developments offer potential solutions.

Cloud computing could ensure that banks have access to enough computing capacity to run and grow their operations and optimise their vast pools of data to manage risks arising from intermediating such things as international trade. Many regulators around the world, however, remain hesitant as to the prospect of banks uploading their data stores into the cloud. Although borne of an understandable desire to protect individual consumer data, newly enacted data protection laws can act as a brake on banks upgrading their IT infrastructure. Outsourcing and operational resilience rules set by regulators such as the United Kingdom's Financial Conduct Authority (FCA) and the European Banking Authority (EBA) codify some of the expectations on banks in this regard. Regulatory sandboxes worldwide provide a useful mechanism for banks and cloud service providers to demonstrate the viability of their proposed operating model, and we can expect regulators to more fully embrace the use of cloud computing

Figure 77[1]
Typical documentary credit transaction



1 DC application
2 DC issued
3 DC advised
4 Goods are shipped
5 Documents presented. If any discrepancy exists the Exporter is notified
6 Document sent to issuing bank
7 Issuing bank will effect payment or accept for a future payment
8 Payment to Exporter
9 Documents received and import bill settled

Note the separate flow of documents on top of payments and goods

1 Step 8 can also take place before Step 9

in the banking industry. In the context of international trade finance, regulators may wish to consider balancing privacy and data sovereignty considerations against the positive impact of data-sharing and data storage across borders, with appropriate safeguards in place.

Cloud computing could unlock great value through its potential to power artificial intelligence (AI) and machine learning. Such tools could simplify and automate documentary processing for trade loans, credit approvals and risk management, including anti-money laundering and sanctions controls. A comprehensive regulatory framework for AI is still outstanding, with the European Union spearheading efforts to codify expectations that AI rules be auditable and explainable at the forefront.

Banking

Regulators are leading the charge on at least one area: around the world, they are beginning to force banks to open their doors to new financial technology providers (fintechs) through Open Banking Application Programme Interfaces (APIs). In the United Kingdom the FCA and the competition authority are mandating banks to allow their clients to share their data with other providers. Open Banking offers the promise of financial innovation with the aim of providing enhanced solution to clients. If they do not adapt and evolve, banks risk disintermediation as fintechs encroach on their business, or they risk being left to run the plumbing as utilities while fintechs reap the benefit of higher value-add service relationships with clients.

Open Banking can also help with building the infrastructure for a truly integrated framework to fight financial crime. Today banks are mostly left to their own devices to identify and report suspicious transactions based on their limited view of the end-to-end transaction and payment flow. In 2020 the UK government announced a new bank and financial services levy to tackle money laundering. Through Open Banking tools the Financial Intelligence Unit (FIU) or another authority could tap into a wider dataset to run its own anti-money laundering and sanctions screening. This could even be further enhanced by implementing the recommended rollout of Legal Entity Identifiers (LEI) and public company registries.

While most regulators are still exploring the relative risks and merits of Blockchain technology, some are taking the lead and establishing supportive frameworks to develop useful Blockchain solutions to trade finance. The Bank of Thailand has spearheaded the development of the Thailand Blockchain Community Initiative within its regulatory sandbox. This initiative aims to digitise and eliminate paper guarantees from the Thai government procurement system. Such digitisation promises to simplify the guarantee amendment and cancellation process. With governments in South Asia and the Middle East still often requiring the issuance of de jure or de facto open-ended guarantees, such simplification through a central repository of guarantees could see banks improve their capital allocation by more easily engaging with beneficiaries to cancel dud guarantees. Elsewhere in Asia, the Hong Kong Monetary Authority is partnering with banks to find a way to digitise trade documents. These are clear examples of a well-defined problem being road-tested to develop a solution in partnership with industry.

Regulators from Mexico to India have supported the development electronic platforms allowing companies to auction off their receivables in a bid to simplify access to working capital. Whereas certain jurisdictions make it prohibitive for companies to assign receivables, here is an example of regulators trying to bring together industry participants to create an arm's-length market for receivables. Likewise, recent progress in the ratification of the UN Convention on the Assignment of Receivables in International Trade suggests further potential in this area.[1]

1 www.mayerbrown.com/-/media/files/perspectives-events/publications/2020/05/the-un-convention-on-the-assignment-of-receivables.pdf

Developing rules

Laypersons can easily identify producers as suppliers and consumers as buyers, and most also understand that buyers can in turn be producers themselves. Practitioners also know that surrounding this supply chain there lies a complex ecosystem of freight forwarders, shipping agents, insurers, financiers, quality inspectors, customs agents, and regulators. Digitisation of trade finance has been a long time coming, but roadblocks remain on this transformation. Some jurisdictions still do not accept electronic bills of lading, while others require paper documents to support cross-border payments as part of capital controls. Change can only happen if all parties in the trade ecosystem move together in line with regulation.

Pax Romana gave the world one of the first systems of long-distance international trade. Over centuries, the Silk Road facilitated exchanges between China and Europe. European empires thrived from trade with the New World. The Industrial Revolution gave rise to specialisation of production on a global scale, with cotton from British colonies feeding mills in Northern England. Along the way, how legislators regulate market activity has evolved to reflect changing legal, cultural and technological realities. Like cars learning to drive themselves, trade finance is subject to digitisation and will require a supportive regulatory framework to ensure it can fulfil its potential, and the Digital Trade Roadmap set by the ICC establishes a helpful guide for regulators and industry to develop this framework.

FEATURE

Stronger together: combatting trade-based money laundering

Richard Bunting, Principal Specialist, Intelligence Partnerships, AUSTRAC
(Australian Transaction Reports and Analysis Centre)

International trade has increasingly become a target for criminal exploitation, and government and industry must join forces to combat trade-based money laundering.

In simpler times, a business front would suffice to make illegally acquired money appear legitimate. A chain of laundromats did the job for Al Capone and is the origin of the term 'money laundering'. Over time, criminals have turned to increasingly sophisticated methods to disguise the origins of dirty money and integrate it into the mainstream economy.

In trade-based money laundering (TBML), criminals take advantage of the size and complexity of international trade to transfer money between parties and evade authorities. Techniques include mismatching the value of the goods and payment (over- or under-pricing relative to market value, quantity or quality), issuing multiple invoices for a single shipment, or sending no goods at all. Money launderers may also seek to obscure their crime through constructing a network of highly complex trade processes that mingle legitimately with illicit funds and take advantage of governance gaps across jurisdictions.

TBML is big business. The profits of international organised crime have been estimated as 1.5% of global GDP, with more than half of these profits laundered through the global financial system.[1] Developing countries are particularly vulnerable, where value gaps in reported international trade have been estimated as USD 8.7 trillion over 2008-17, and USD 817.6 billion in 2017 alone.[2] The human consequences are grave, including 40.3 million people forced into slavery worldwide, a quarter of whom are children[3].

For authorities and the trade financing industry, TBML can be difficult to detect amid the many processes, parties, transactions and jurisdictions. As with any disruption approach, anti-TBML efforts need to be constantly refined to keep up with new and emerging risks posed by criminals seeking to harm the community and profit from their crimes.

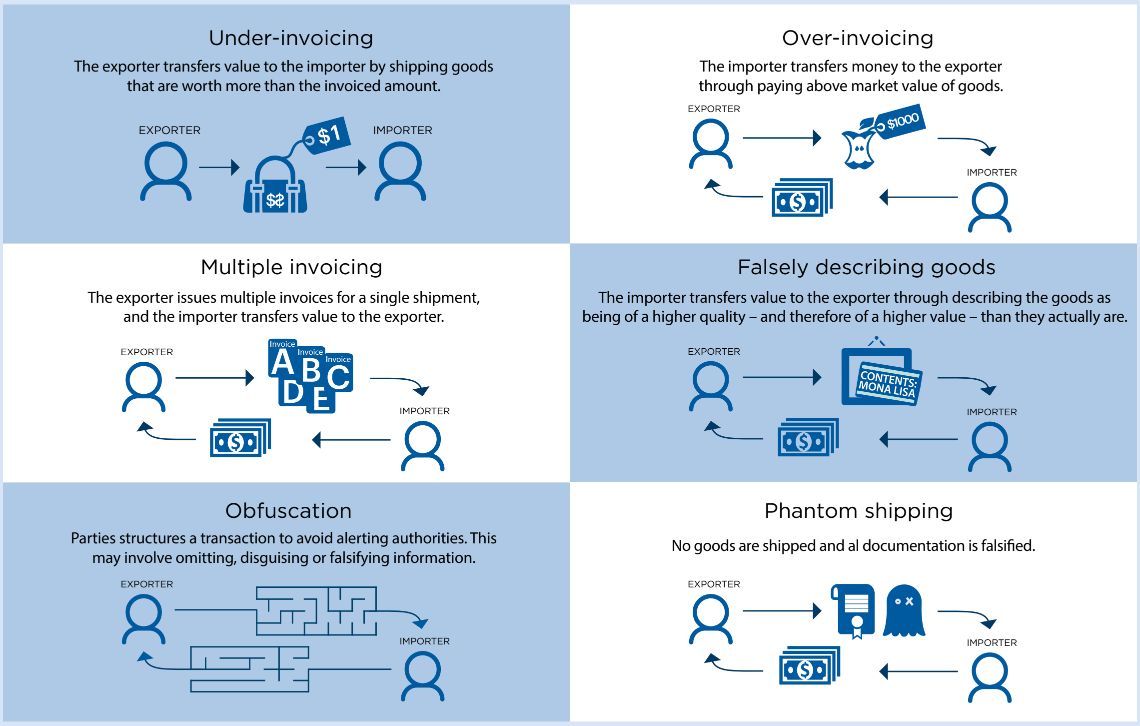
Collaboration is key

Acknowledging that no single body can tackle such challenges, the Australian Government's anti-money laundering/ counter-terrorism financing regulator and financial intelligence unit, AUSTRAC, takes a collaborative approach.

AUSTRAC is the Australian government agency responsible for preventing, detecting, and responding to criminal abuse of the financial system to protect the community from serious and organised crime. AUSTRAC regulates more than 15,000 businesses to protect them, and the financial sector, from criminal abuse. These regulated or 'reporting' entities are at the front line in combating financial crime. They submit reports about financial transactions and suspicious matters to AUSTRAC which become the building blocks of actionable intelligence. Each report contributes a piece of the jigsaw puzzle that, when put together, allows a more detailed picture to emerge.

1 OECD (2016), Illicit Trade: Converging Criminal Networks, OECD Reviews of Risk Management Policies, OECD Publishing, Paris. dx.doi.org/10.1787/9789264251847-en
2 GFI (2020), Trade-Related Illicit Financial Flows in 135 Developing Countries: 2008-2017, Global Financial Integrity, Washington DC. gfintegrity.org/report/trade-related-illicit-financial-flows-in-135-developing-countries-2008-2017/
3 ILO (2017), Global Estimates of Modern Slavery, International Labour Organization and Walk Free Foundation, Geneva. ilo.org/global/topics/forced-labour/statistics/lang--en/index.htm

Figure 78
Trade-based money laundering techniques



Such information realises its greatest potential when understood within a larger context. Suspicious matter reports and financial information received by AUSTRAC are available to more than 5,000 designated users within partner agencies to support national security and law enforcement investigations. AUSTRAC's analysts also use this information to identify new and emerging risks and to develop sophisticated in-depth intelligence reports on priority law enforcement and national security matters. AUSTRAC then provides indicators and trends back to the businesses it regulates to help them further mitigate risks and respond to emerging threats. As the quality of reports increases, so does the intelligence that leads to the detection and apprehension of criminals.

To further boost the benefits of collaboration, AUSTRAC established the Fintel Alliance in 2017, the world's first private-public partnership of its kind. Fintel Alliance's 28 members include experts from financial industry, intelligence agencies, law enforcement, and academic and research institutions. Along with improved operational outcomes, members' capability increases as partners learn from one another and synthesise knowledge. Fintel Alliance has now formed a TBML working group that includes front-line experts from industry and law enforcement to develop indicators and typologies that can be broadened to other jurisdictions and trade types.

The value of this interconnected approach is becoming clear. Better intelligence and information-sharing regarding child sexual exploitation resulted in a 643% increase in suspicious matter reports to AUSTRAC. This supported the detention or arrest of 73 persons and the protection or rescue of 35 victims in 2018-2019.

To combat TBML, as with other serious and organised crimes, we need to continue to monitor and prepare for shifts in the risks that criminals may pose to the financial system and community. Timely and quality contributions from industry are crucial for success. As financial crime becomes more complex across the globe, collaboration is a critical foundation to overcome criminal exploitation of our interconnected trade, financial systems and global communities.

FEATURE

Combating money laundering: improving systems, enabling trade

Can Sutken, Relationship Manager, Asian Development Bank, Trade Finance Program
Catherine Daza Estrada, Workshop Secretariat, Asian Development Bank, Trade Finance Program

Increased trade helps bring developing countries into the global financial system. But financing that trade can be difficult when the process is sometimes stymied by systems aimed to combat money laundering.

Trade helps build inclusive growth and reduces poverty. Trade finance helps facilitate international trade and commerce by making it easier for importers and exporters to transact business using financial instruments and products.

Greater access to the global financial system would narrow the gaps between developed and developing countries. Without proper financing, developing countries cannot benefit from trade because they do not have the money to build supply-side capacity and trade-related infrastructure. Greater financial inclusion is key to achieving the UN's Sustainable Development Goals (SDGs).

In the latest study by the Asian Development Bank, the global trade finance gap was estimated to be USD 1.5 trillion. This persistently large market gap impedes the full potential of trade to deliver growth, jobs, and poverty reduction. The ADB study identified AML and KYC requirements as one of the key reasons why trade finance proposals get rejected.

The United Nations Office on Drugs and Crime estimates only about 1% of crime proceeds laundered via the global financial system are seized and frozen. Around 80–90% of the reports of suspicious financing are of no immediate value to active law enforcement investigations, based on a poll conducted by the Royal United Services Institute.

To be clear, this isn't a choice between fighting financial crimes and improving financial access. Illicit money transfers cannot be allowed to compromise the integrity and security of the global financial system.

It is worth studying, however, whether the regulatory regimes designed for KYC, AML, and countering the financing of terrorism (CFT) could be streamlined so that the bad guys get caught but the good guys still get financed.

In terms of trade and trade finance, 'following the money' is thought to be more challenging given that trade finance involves complex transactions involving multiple parties, including correspondent banking relationships that are thought to be of higher risk from an AML perspective.

To address trade-based money laundering (TBML), the Asia/Pacific Group on Money Laundering Trade Based Money Laundering Typologies Report 2012 recommended the adoption of common formatting to record and maintain trade-relevant statistics. That way, data could be analysed to identify trends related to trade-based money laundering, instead of that data being lumped in with other forms of money laundering, as they are now.

For its part, the ADB Trade Finance Program has convened multiple stakeholders from international organisations, regulators, and major global banks to brainstorm on these issues and present practical solutions.

ADB is encouraging standard setters to consider adopting common trade data points in suspicious transaction reports to produce higher quality, actionable intelligence from those submissions. It has highlighted the need for a feedback loop between and among regulated banks, financial intelligence units, law enforcement, and other relevant agencies such as customs authorities.

To help address issues relating to non-customer due diligence in trade finance, and a perceived misalignment in trade finance examinations by bank examiners, the ADB has published “Trade and the Legal Entity Identifier”, a paper discussing the Legal Entity Identifier as a unique and secure system to facilitate business transactions, risk evaluation, and money lending; and “Effective Practices in Trade Finance Examinations”, which provides bank examiners and regulators a better understanding of trade finance, how departments involved work, and how to align expectations on appropriate compliance related to trade and trade finance.

Actively engaging the private sector in creating solutions to address money laundering, not just in trade and trade finance, could be the missing piece in the fight against financial crimes. The ADB is leveraging its neutral position to enable the parties involved to discuss and move forward with more clever solutions that are effective and support clean business.

This doesn’t need to be a choice between fighting financial crimes or improving financial access. Systems can be designed to be better at spotting illicit transactions while streamlining the process so that the developing economies are not left behind.

DIGITISATION

Survey analysis

The Global Survey has already touched on several aspects of digitisation, from supply chain finance to SME inclusion to regulation. Digitisation is not simply a trend in trade finance, but a singularly disrupting change to the way trade finance operates. Given the difficulty that many banks have had in accessing original documentation during COVID-19 (due to lockdowns and quarantines), we expect the push to fully digitise global trade and trade finance to gather further momentum. While digitisation is widely seen as one of the most important – and promising – developments to shape trade finance in the coming years, the survey shows a clear divide between banks that have the vision, capacity and commitment to advance digital capabilities and those that currently do not.

Of the banks surveyed, 64% indicated that they have a digital strategy for trade finance (Figure 79). However, this number differs significantly by bank type. While 83% of global banks have a digital strategy, only 46% of local banks have one – a stark reminder of the challenges many banks face in integrating digital solutions into their existing offerings. Indeed, only 17% of respondents have successfully implemented digital solutions (Figure 80), with a surprising one in five not yet seeing any tangible benefits. 22% of banks said that they have tried to implement technology solutions but that it has been

Figure 79
Does your bank have a digital strategy for trade finance?

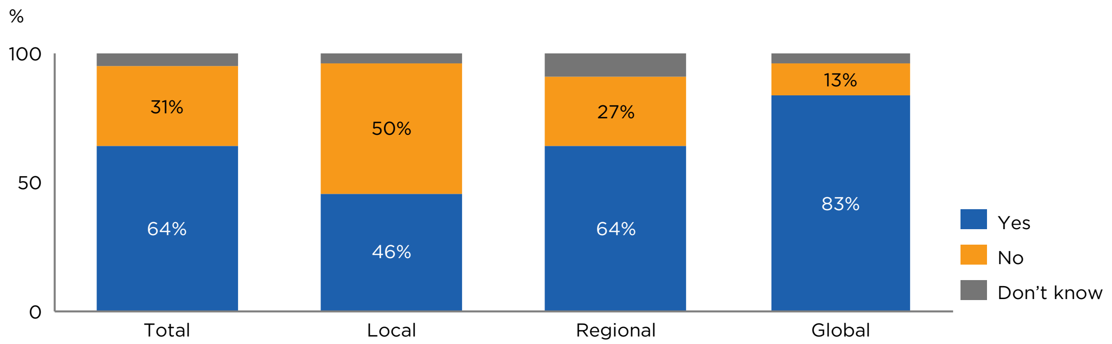
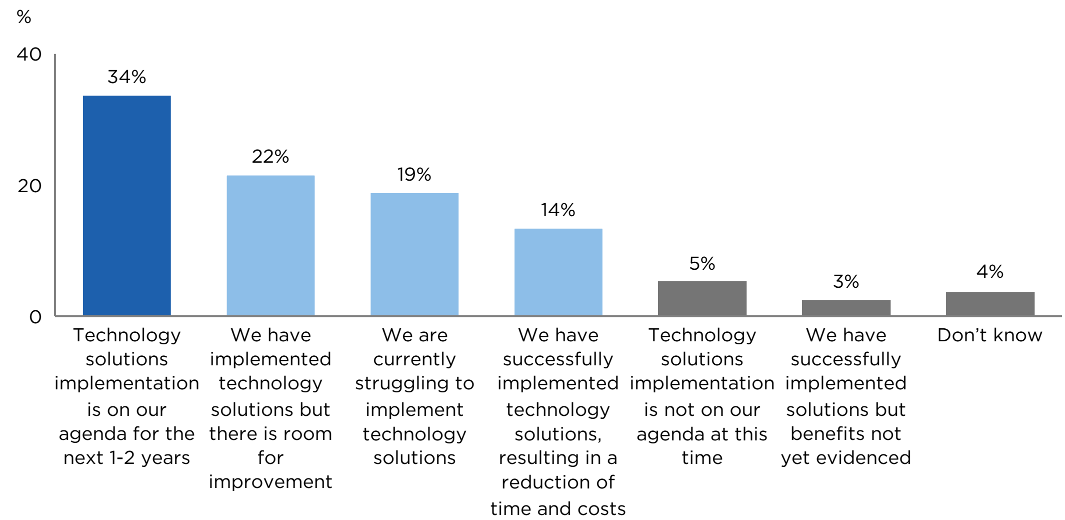


Figure 80
Please indicate the maturity of your bank in using technology solutions



imperfect, while a further 19% are currently struggling to even match that. This clearly highlights that the effort and expense of upgrading bank technology continues to be a key hurdle in digitising trade, and indeed for some organisations runs into hundreds of millions USD when calculated in US Dollars..

Of the various digital trade technologies looked at in the survey, the most common implemented by banks is an online platform for trade finance (55%) (Figure 81). This is unsurprising, and largely considered to be 'table stakes', given that channels represent the 'customer gateway' to digital trade. High-quality

Figure 81
What instruments and solutions are your bank using for digitised trade finance?

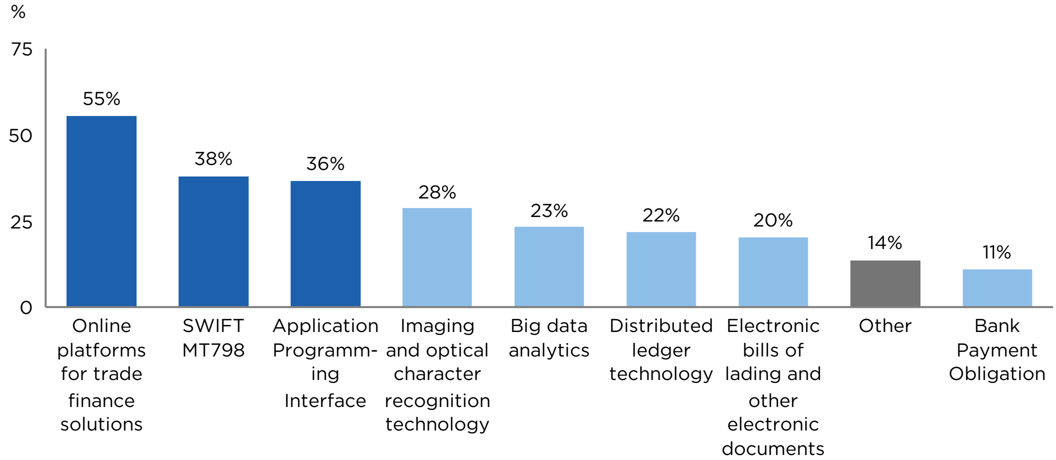
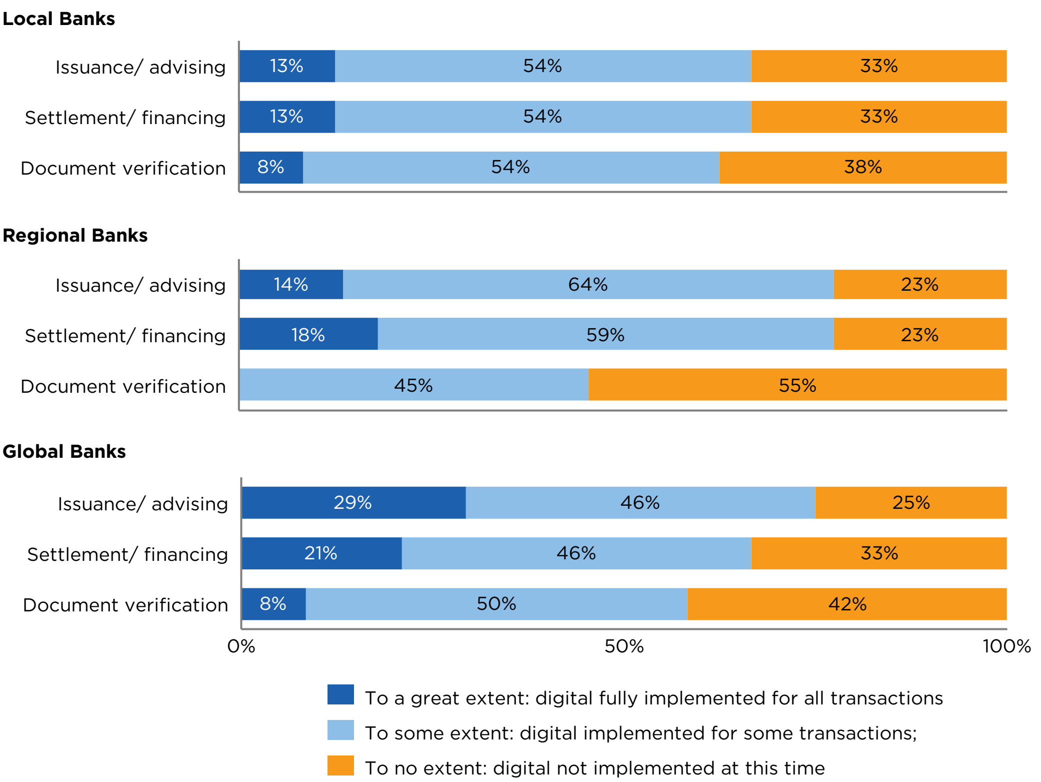


Figure 82
To what extent has your bank removed the use of physical paper for documentary transactions?



digital channels are often a substantial value differentiator, particularly in the MSME space where host-to-host connectivity is largely non-existent.

SWIFT MT798 (38%) and APIs (36%) were also frequently cited by respondents as digital solutions offered by their banks. Only 22% of respondents indicated that their banks were integrating DLT-based solutions in their trade finance operations; while this may be surprising given the attention DLT continues to receive, it likely represents the fact that DLT is still often applied largely to pilot transactions and proofs of concept, with practitioners seeking to better understand the scalability of DLT-based solutions and the differentiated proposition around DLT-based technical architectures versus other options.

Digital is clearly an important topic for banks, and particularly for global banks, but there is limited end-to-end adoption of digital solutions in trade finance. This is consistent

Figure 83
What is the level of client usage of digital channels in each of the following areas?

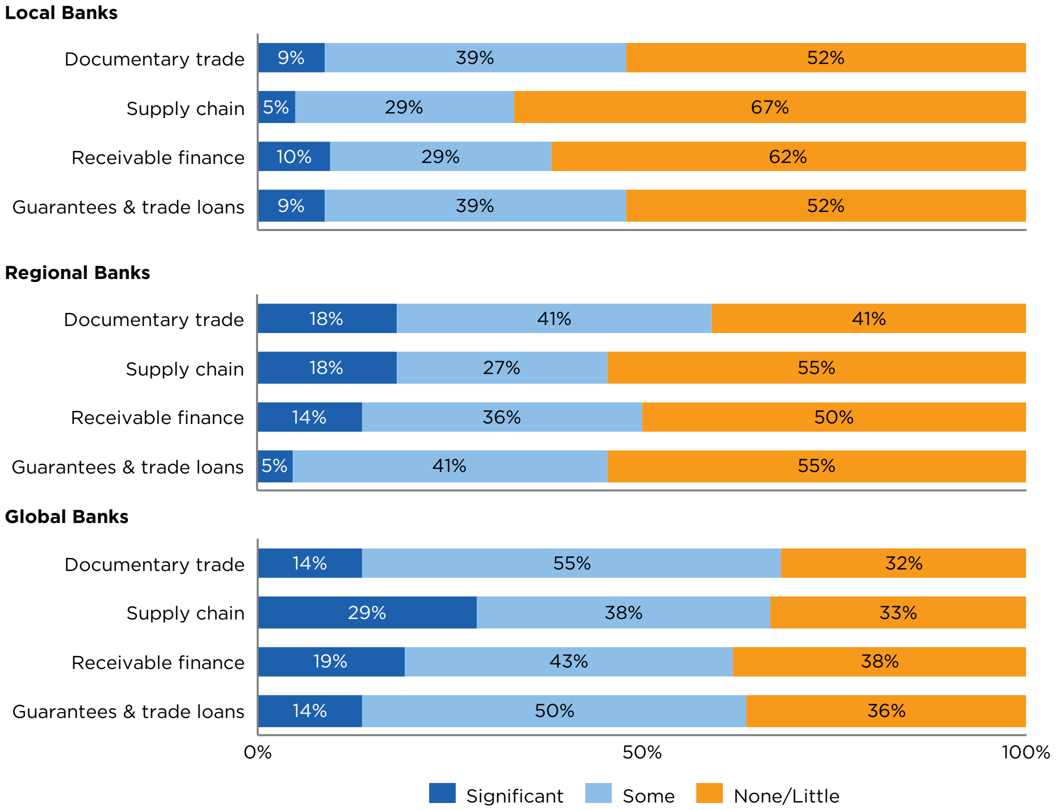
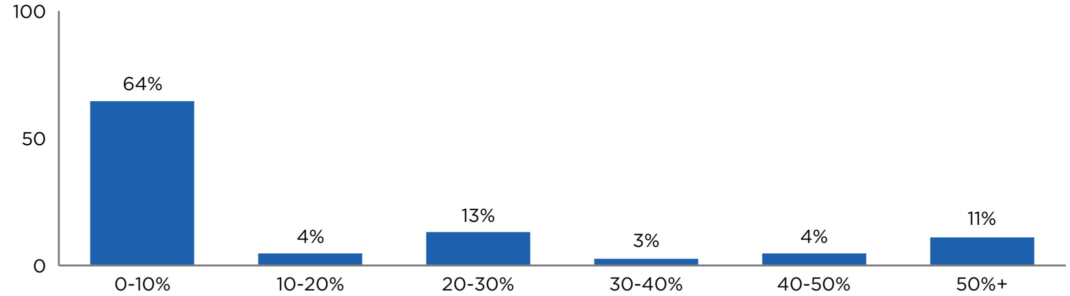


Figure 84
What percentage of documentary trade transactions do you receive digitally?



across bank types, although adoption is more limited among local and regional banks than global banks. While most banks have removed the use of physical paper for documentary transactions to some extent (Figure 82), it is more common among global banks. However, between half and two-thirds of local banks indicated that client usage of digital channels across trade finance products is either minimal or non-existent (Figure 83). For global banks the number is closer to one-third.

Further, most banks receive only a small amount (0–10%) of documentary trade (Figure 84) and open account trade (Figure 85) transactions digitally. This is rather surprising given the prevalence of digital channels for transaction origination.

The same trend emerges for zero-touch processing transactions (i.e. no human intervention from start to finish), with an average of only 6–9% across the four products surveyed (Figure 86). This is less surprising and a known challenge for banks – while many components of trade finance operations are being digitised (e.g. data capture, sanctions screening), very few players, if any, have managed to create a fully digital 'zero touch' end-to-end process (e.g. to include document checking).

In terms of achieved benefits of digitisation, 83% of respondents indicated only a minimal reduction in costs over the past five years due to digitisation (Figure 87). Given the prominent focus that digitisation has had in

Figure 85
What percentage of open account trade transactions do you receive digitally?

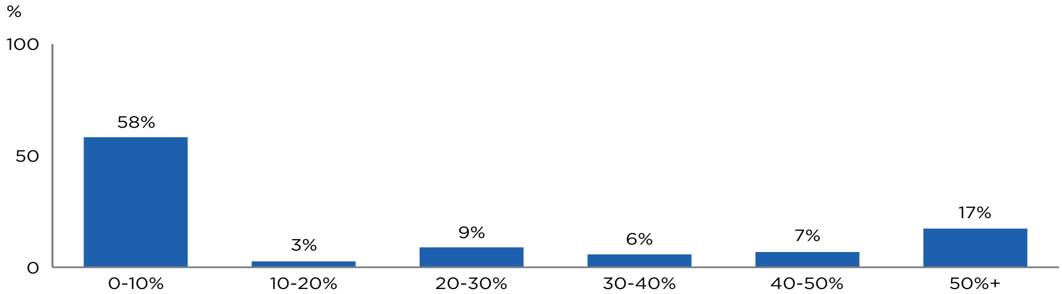
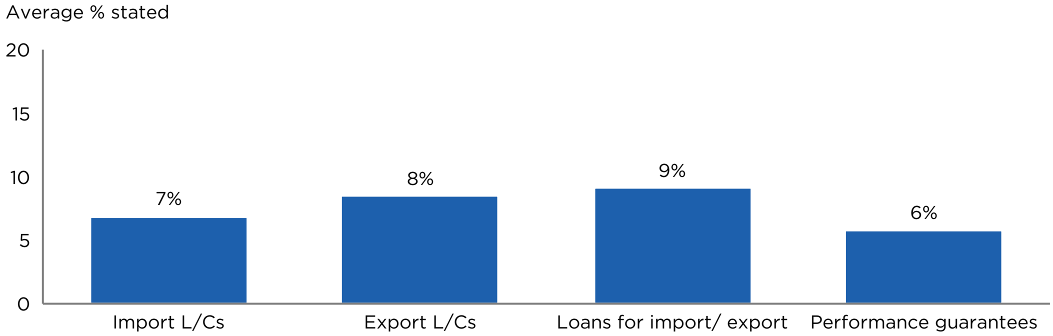


Figure 86
What percentage of your transactions have zero-touch processing for the following products?



the industry over the past decade, it may be surprising that so few banks report much benefit (at least from a cost perspective). This may be due to the fact that we are still far off from system-wide paperless trade, and hence there is still a long way to go in terms of cost reduction from digitisation. Alternatively, these findings may speak to the challenge and cost of implementing technological solutions – reducing returns on investment.

Looking ahead, 66% of respondents expect at least 10% in cost savings from digitisation over the next five years. However, again this differs by bank type, with 91% of global banks expecting a meaningful reduction to their cost base from digital solutions (Figure 88), but only 55% of non-global banks expecting the same.

Of banks surveyed, 80% spent only USD 0–10 million in 2019 on developing or acquiring digital solutions for trade finance (Figure 89). This may be because the limited reduction in costs that most banks have experienced over the past five years has reduced their appetite for investment, or conversely the lack of adequate investment may be limiting cost reductions.

The differences between bank types in the survey go beyond technology adoption to how they view the fundamental utility of digitisation. Looking beyond cost savings, digitisation can bring improved product propositions, more advanced channels, enhanced customer experience and retention, and superior risk mitigation - amongst other benefits. This could shape the future of trade finance, with banks that can build and implement digital solutions taking greater market share, and banks that are unable to do so entering partnerships or withdrawing from the market.

Respondents from banks with successful digital trade finance solutions said that the solutions with the most benefits were online

Figure 87
Over the past five years what % cost savings has digitisation of trade provided?

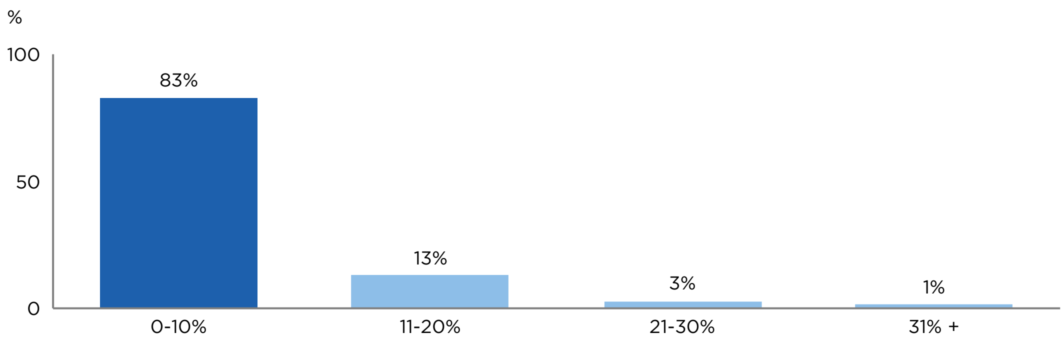
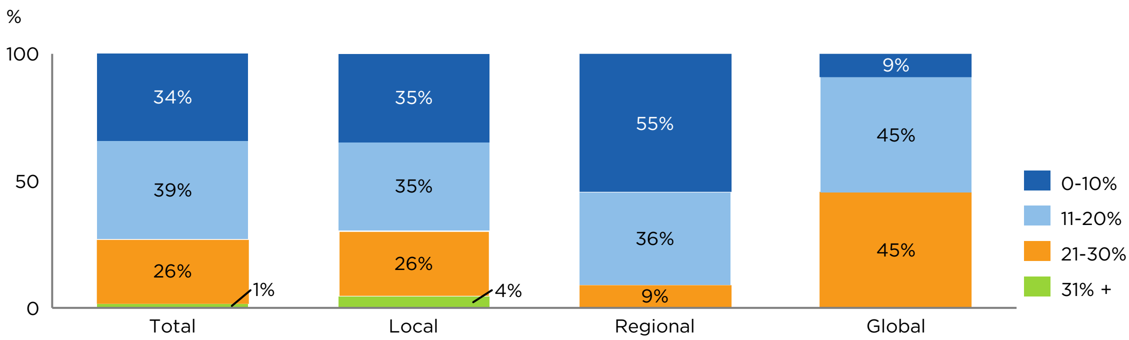


Figure 88
Over the next five years what % cost savings do you expect digitisation of trade to provide?



platform offerings to customers, digital processing and approval processes, and automation of operations. One respondent cited "use of machine learning/ artificial intelligence to automate processing in operations" as an example of how their bank has integrated digital solutions into their offerings. Another respondent noted that "[digital products] do not replace people, but help people operate more efficiently".

The cost reduction impact of digital solutions suggests strongly that the case for investing in these technologies must be built upon a wider foundation – a combination of factors such as client expectation and satisfaction, reductions in operational and fraud risk, and the ability to refocus trade finance specialists from mundane, lower-value tasks that can be addressed through technology to activities that generate business or client relationship value.

For banks that are finding it hard to implement technological and digital solutions, 61% cite the challenges (financial, logistical, and technical) of building internal capabilities (Figure 90). A further 51% answered that both regulation and client needs were hampering wide-scale adoption of digital solutions.

When asked to evaluate the benefits of digitisation, answers vary again across bank types. While 57% of global bank respondents agreed that digitisation will enable banks to serve their customers significantly better (Figure 91), only 42% of local bank respondents felt the same way. The divide was even starker when respondents were asked if digitisation would benefit their trade finance operations – 59% of global banks agreed, while only 32% of regional banks and 25% of local banks agreed (Figure 92).

Despite these responses, global banks expect that it will take longer for digital trade finance to replace current models and practices

Figure 89
How much has your bank spent in 2019 on developing/ acquiring digital solutions for trade finance, including future spends (3-5 years ahead)?

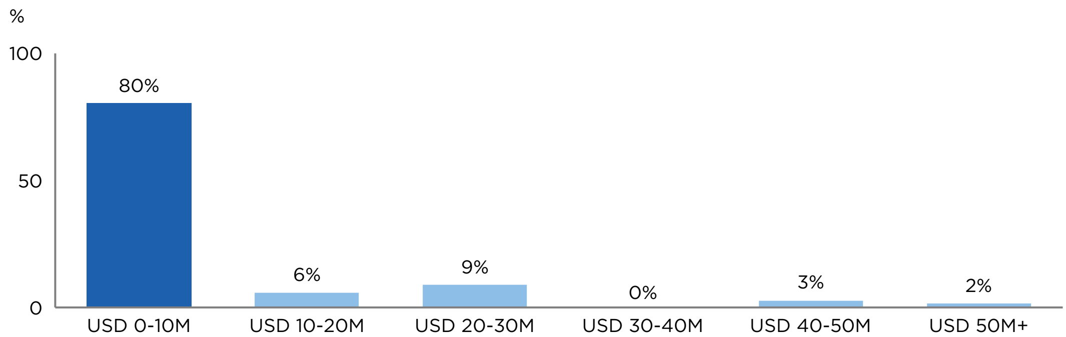
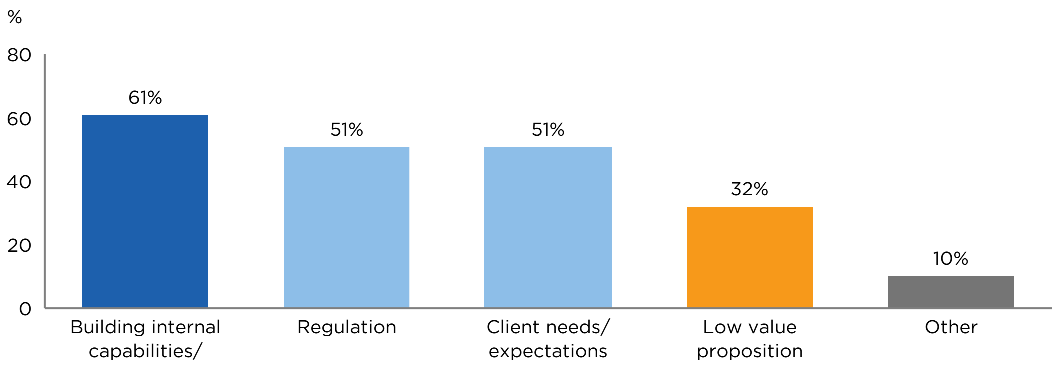


Figure 90
What are the main barriers that are preventing a wider adoption of digital solutions?



than do other banks. Only 43% of global banks expect this to happen before 2030, compared to 59% of local banks (Figure 93). Further, 13% of global banks expect that pure digital trade finance will never fully supplant traditional trade finance. This could be driven by global banks' first-hand knowledge of how challenging, expensive, and time-consuming it is to modernise legacy systems and associated processes across multiple jurisdictions.

The disparity in sentiment towards digitisation between global, regional, and local banks is somewhat concerning. It is clear that smaller banks have had less success in reaping the benefits of digital solutions, particularly when we consider the reality that benefits of digital solutions must be understood to encompass more than cost reduction.

Limited investment capacity, local regulations, a small customer base, and the inherent scale challenges of technology are all particularly acute for smaller trade banks. If these smaller banks fail to capture the advantages of technology, there is a material risk of their being disadvantaged in a two-speed market. However, in today's market there are emerging alternatives to the prohibitive costs of technology solutions, from forming partnerships with non-bank players to adopting white-label digital platforms that will give smaller banks the opportunity to keep up with the changing world of trade finance.

Figure 91
To what extent, if any, do you think that digitisation will enable your bank to better serve its existing clients and attract new clients?

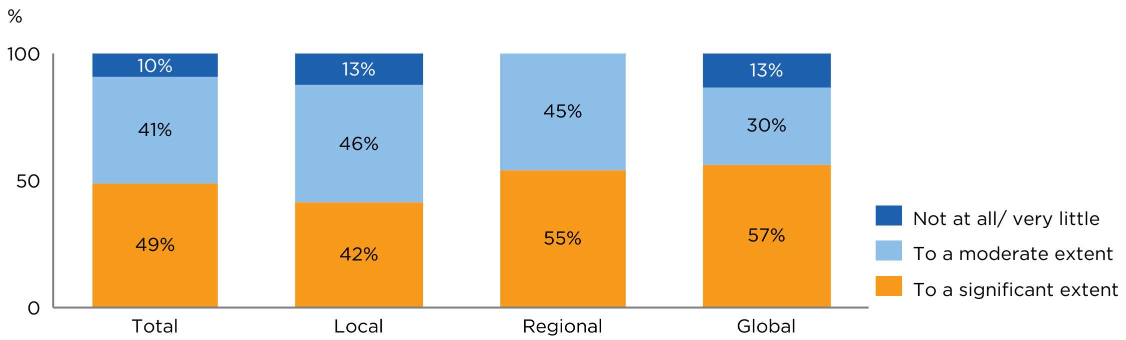


Figure 92
How would you rate the benefits of digitisation to your bank's trade finance operations?

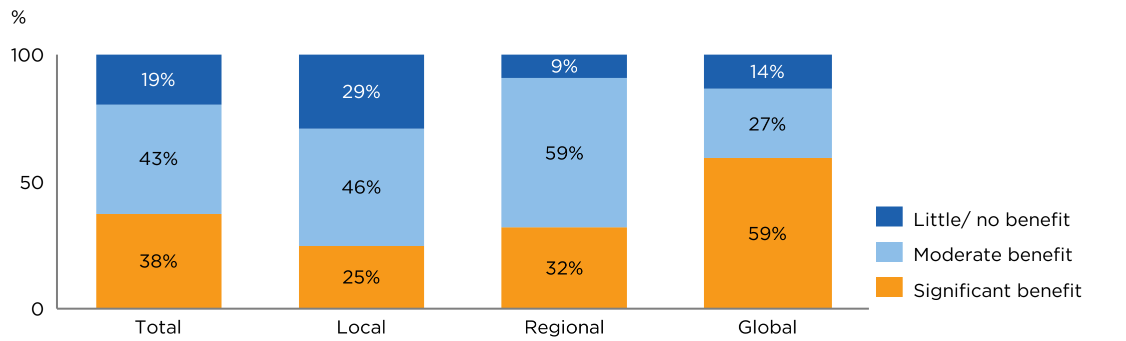
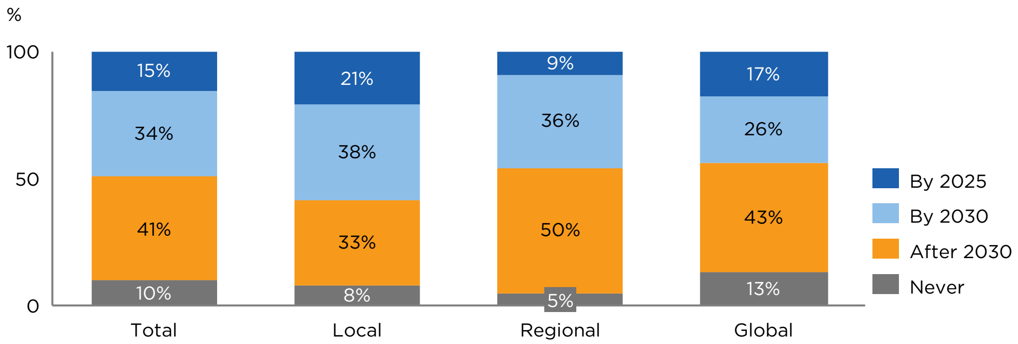


Figure 93
When would you predict pure digital trade finance to completely replace traditional trade finance as known today?



FEATURE

Digital trade and COVID-19: maintaining the crisis-driven momentum

Alisa DiCaprio, Head of Trade and Supply Chain, R3
Chris Southworth, Secretary General, ICC UK

Introduction

By April 2020, most banks across the globe had implemented Business Continuity Plans (BCPs) in response to local quarantines and lockdowns. Common to many of these BCPs was the scaling up of existing digital solutions. Indeed, 55% of respondents to the supplementary ICC COVID-19 Survey report rolling out new digital solutions during the pandemic. None of this was easy or without significant adjustment challenges. But many are asking what is going to happen to this progress when we return to business as usual?

This is where the ICC can play a role. The ICC Digital Trade Roadmap is a tool to continue the digital gains made during COVID-19. We need this because we can expect the digital strides we have made to regress back to paper when the crisis eases. The reason why is the same reason that digitisation hadn't progressed this far earlier: the stubborn persistence of paper-pushing norms and regulations.

What is the roadmap?

The ICC Digital Trade Roadmap is a simple framework for governments, institutions and industry. It presents a list of specific policies and actions that would progress the digital agenda over time. It does this by advocating action in three pillars:

1. Modernising outdated laws and regulations,
2. Supporting standards that enable interoperability of digital platforms, and
3. Changing industry behaviours and norms around paper

Harmonisation of action across digital advocates will be key in 2020. Few believe that we should be using paper originals and handwritten signatures in 2020. But moving to digital is an enormous task that requires coordination from the private sector and government. It isn't that no one wants to do it, it's that there is so much to do, no obvious way to prioritise, and no single global institution tasked with coordinating the agenda. The roadmap can provide this coordination on both a local and global level.

What does the roadmap tell us about digitisation in different jurisdictions?

In addition to guiding actions, the roadmap also gives us a way to estimate national level digital trade progress.

Digitisation is a global challenge that requires patient and persistent cooperation. At the inter-governmental level, we have a good understanding of what needs to be done to make a difference. But at the national level, the picture is more nuanced because of the different legal frameworks and different makeups of economies. Figure 94 offers a view into 12 ICC member economies. They include a mix of developed and developing economies.

Figure 94 tells us three important things. First, that most countries are doing relatively well in implementing the WTO Trade Facilitation Agreement. Second, that progress on Electronic Single Window initiatives is in evidence, albeit slowly. And third, we learn that the WTO E-commerce negotiations, while broadly inclusive, could benefit from more markets participating. These insights can be used for greater advocacy on these topics.

The roadmap also allows us to see that progress on digitisation isn't only about modernising regulations or establishing standards. Equally important is systems change within the industry. This points to the need for more focus on pillar three in the roadmap: helping industry upskill and modernise systems and processes.

Before we can change practices around paper, we need to understand why paper is used in the first place. We asked ICC respondents to tell us – for their region – which documents were required to be paper and which could be submitted digitally. Figure 95 shows these results.

Of the ten document types included in the survey, there were four where more than 50% of respondents reported that they must be issued in paper form. These are Bills of Exchange, Promissory Notes, Bills of Lading and Certificates of Origin. Ideally, governments need to create the conditions where all documents operate by digital means to prevent a return to paper, but these results are helpful in identifying a specific area of law where governments can make a tangible difference to digitising trade, similar to what is happening in the UK.

Most positively, documents that could be paper or digital with more than 50% of respondents included: Insurance policies (51%), import/ export declarations (52%), commercial invoices (65%), Letters of Credit (69%), payment confirmations (70%) and order forms (71%).

Figure 95 also reveals the inconsistency across different legal jurisdictions. Smaller countries, without legacy systems like Georgia and Singapore, can often act as hotbeds of innovative new practices and be a useful bridge between developed and less developed countries. If mobilised, this group could be a powerful force for change in institutions like the World Trade Organization, in the same way the Friends for Ecommerce for Development were in the lead up to the WTO Ministerial Conference in Buenos Aires in 2018 and the consequent start of ecommerce negotiations.

Figure 94
Digital progress in three areas

	Implementation of the WTO Trade Facilitation Agreement (%)	**Use of Electronic Single Window**	**Participation in WTO Ecommerce negotiations**
Brazil	95.8	operational	yes
China	96.2	in progress	yes
Germany	100	operational	yes
India	72.3	in progress	no
Netherlands	100	in progress	yes
Nigeria	15.1	in progress	yes
Russia	100	in progress	yes
South Africa	100	operational	yes
UAE	90.3	no	no
UK	97.1	operational	yes
US	100	in progress	yes

Sources: TFA database, World Bank, EC database

Figure 95

Which documents are legally required to be paper (by region)

Country	Letter of Credit	Bill of Exchange	Commer-cial Invoice	Order Form	Insurance Policy	Promis-sory Note	Bill of Lading	Certificate of Origin	Payment Confirmation	Import/ Export Declar-ation
APAC										
Australia	Paper or digital	Must be paper	Paper or digital	Paper or digital	Paper or digital	Must be paper	Paper or digital	Paper or digital	Paper or digital	Paper or digital
Bangladesh	Must be paper	Unsure	Unsure	Must be paper	Unsure	Unsure	Must be paper	Must be paper	Must be paper	Must be paper
China	Paper or digital	Must be paper	Paper or digital	Paper or digital	Paper or digital	Must be paper	Paper or digital	Must be paper	Paper or digital	Must be paper
Hong Kong	Paper or digital	Must be paper	Paper or digital	Paper or digital	Unsure	Must be paper	Paper or digital	Paper or digital	Unsure	Paper or digital
India	Paper or digital	Must be paper	Paper or digital	Paper or digital	Paper or digital	Must be paper	Paper or digital	Paper or digital	Paper or digital	Paper or digital
Singapore	Unsure	Paper or digital	Must be paper	Paper or digital	Paper or digital	Paper or digital	Must be paper	Paper or digital	Paper or digital	Paper or digital
Sri Lanka	Paper or digital	Must be paper	Must be paper	Paper or digital	Must be paper	Must be paper	Must be paper	Must be paper	Paper or digital	Paper or digital
Vietnam	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital
Middle East										
Afghanistan	Paper or digital	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Paper or digital	Unsure
Qatar	Paper or digital	Must be paper	Must be paper	Paper or digital	Paper or digital	Must be paper	Must be paper	Must be paper	Paper or digital	Paper or digital
Saudi Arabia	Paper or digital	Must be paper	Paper or digital	Paper or digital	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper
UAE	Paper or digital	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Paper or digital	Must be paper
LATAM										
Argentina	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital
Brazil	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Must be paper	Must be paper	Must be paper	Paper or digital	Paper or digital
Ecuador	Must be paper	Must be paper	Paper or digital	Paper or digital	Must be paper	Must be paper	Must be paper	Must be paper	Paper or digital	Paper or digital
Mexico	Must be paper	Must be paper	Paper or digital	Paper or digital	Must be paper	Must be paper	Must be paper	Paper or digital	Paper or digital	Paper or digital
Panama	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital
Central & Eastern Europe										
Armenia	Must be paper	Unsure	Paper or digital	Paper or digital	Paper or digital	Unsure	Must be paper	Must be paper	Paper or digital	Must be paper
Belarus	Paper or digital	Must be paper	Unsure	Unsure	Unsure	Must be paper	Unsure	Unsure	Unsure	Unsure
N Macedonia	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Unsure
Russia	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper
Turkey	Paper or digital	Must be paper	Must be paper	Paper or digital	Must be paper	Must be paper	Unsure	Must be paper	Paper or digital	Must be paper
Ukraine	Paper or digital	Must be paper	Paper or digital	Paper or digital	Unsure	Must be paper	Must be paper	Unsure	Unsure	Paper or digital
Uzbekistan	Paper or digital	Unsure	Paper or digital	Must be paper	Must be paper	Unsure	Must be paper	Unsure	Paper or digital	Paper or digital
Western Europe										
Belgium	Paper or digital	Must be paper	Paper or digital	Paper or digital	Paper or digital	Must be paper	Must be paper	Must be paper	Unsure	Paper or digital
France	Paper or digital	Must be paper	Paper or digital	Paper or digital	Must be paper	Must be paper	Unsure	Must be paper	Paper or digital	Must be paper
Germany	Must be paper	Must be paper	Must be paper	Paper or digital	Must be paper	Must be paper	Must be paper	Must be paper	Paper or digital	Must be paper
Italy	Paper or digital	Must be paper	Paper or digital	Paper or digital	Paper or digital	Must be paper	Must be paper	Must be paper	Paper or digital	Must be paper
Serbia	Paper or digital	Must be paper	Paper or digital	Paper or digital	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper	Must be paper
Spain	Paper or digital	Must be paper	Paper or digital	Paper or digital	Paper or digital	Must be paper	Must be paper	Must be paper	Paper or digital	Paper or digital
Sweden	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Unsure	Must be paper	Paper or digital	Paper or digital	Paper or digital
UK	Paper or digital	Unsure	Paper or digital	Paper or digital	Paper or digital	Unsure	Paper or digital	Paper or digital	Paper or digital	Paper or digital
Africa										
Egypt	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital
South Africa	Paper or digital	Must be paper	Paper or digital	Must be paper	Paper or digital	Must be paper	Must be paper	Must be paper	Paper or digital	Must be paper
Tunisia	Paper or digital	Must be paper	Must be paper	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital	Paper or digital

Must be paper · Paper or digital · Unsure

Note: The above chart has been developed directly – unedited - from Global Survey responses, and does not represent an official ICC view. Please treat as an indication that requires further validation

How COVID-19 reinforced the need for a roadmap

COVID-19 accelerated the digitisation agenda in ways that were unimaginable a year ago. Companies, governments, and institutions all scrambled to implement ad hoc practices in order to keep trade flowing and teams working while isolated at home. This reinforced the applications for the ICC Digital Trade Roadmap in two important ways.

First, it made it clear that guidance is needed even for temporary measures. Business Continuity Plans (BCPs) were rolled out before most government or regulators had a chance to offer any guidance. And even then, fewer than 30% of ICC's COVID-19 Survey respondents report receiving support from their governments in relaxing requirements for paper (although anecdotally, this appears to have improved over the course of the crisis). However, there are clearly authorities that have issued direct guidance. As an example, both the Indian Bankers Association and the Bank of Algeria suggested that electronic or scanned documentation was acceptable where presentation or transmission was not feasible.

Today's environment – as we saw in Figure 92 and Figure 93 – isn't yet conducive to fully digital trade flows. To have the confidence to try untested solutions, banks need regulators and governments to show their support. The roadmap can be used to identify where guidance is most needed.

Second, emergency response measures made it clearer than ever before what is achievable. In some cases, they also illustrated what it will take to get there. The ad hoc digital practices implemented by banks aimed to address five challenges: deal origination and distribution, negotiable instruments, document transmission, authorised signatures, and shipping delays. Banks managed to keep trade flowing despite these hurdles. Now that we know it is possible to go digital, the direct actions promoted by the roadmap can help introduce greater collaboration among trade participants.

Conclusion

We have a framework available in the roadmap, a better grasp of where we need to act to move the agenda forward to digitise trade documentation, and a global crisis on which minds are focused. There is a clear case for action in order to set the conditions for economic recovery – digitisation is a solution.

For the first time in living memory, we have all the tools available at the same time to capture the opportunity if, as industry, we mobilise and cooperate across jurisdictions. ICC has a central role to play as the neutral rallying point but so does the finance industry as a facilitator to help bring all the stakeholders to the table.

USING THE ROADMAP TO MAKE PROGRESS: THE UK EXPERIENCE

The UK is the second-largest services exporter, third-largest ecommerce market, and a global centre for finance, innovation, and international business. It is thus surprising the UK hasn't already taken the opportunity to position itself as a global leader in the digital business environment.

The answer lies in the complexity and age of the UK legal system, coupled with the fact that there is no single point of leadership in government and no trade body singularly focused on making the case for change.

We have identified three specific pieces of legislation that act as a brake on progress.

- The Bills of Exchange Act 1882,
- Carriage of Goods by Sea Act 2002 and,
- The Statute of Frauds Act 1695 (Northern Ireland).

The need to modernise underscores a deeper issue in UK law: how title of ownership is recognised. In trade, title refers to goods. But the legal definition goes much further and covers everything from ownership of assets to pensions and power of attorney. Several attempts have been made to review the UK situation, but all have failed to make significant progress.

The good news is there is genuine alignment and a real appetite to address the issues from across industry and government. ICC has stepped in to act as the neutral convener using the roadmap to rally the different stakeholders. They have included the UK Law Commission, Ministry of Justice, Department for Digital Trade, the Commonwealth, and a host of experts from finance, law, academia, shipping, insurance and trade. All agree the time is right and there is a real opportunity to move the agenda forward.

As the home of English law and the Commonwealth, the general consensus is that if the UK can fully digitise trade documentation, it sets an important precedent across all 54 Commonwealth countries and all contracts that use English law. The UK could also become the first G7 country and lead the way for others to follow.

Multilateral and bilateral trade dialogues are another place that the UK can show leadership. The UK is also an active participant in the WTO Ecommerce negotiations and is in the midst of trade negotiations with the EU and US. Brexit and now COVID-19 have accelerated the agenda and opened up a window of opportunity that has remain unchanged for hundreds of years. It's an enormous opportunity that the UK must take.

Using the roadmap, the ICC can act as a neutral convener for industry, to bring all the parties to the table and to step in as the body that makes the case for change. If we can do this across the ICC network, we will be able to accelerate the digitisation of global trade.

FINANCIAL INCLUSION

Survey analysis

One of the most pressing and challenging issues facing the trade industry today is financial inclusion broadly defined, as well as more specifically in making sure, that trade finance products are available to businesses of all sizes and across geographies, and that by extension, the benefits of trade in terms of enhanced standards of living can be more equitably distributed. Survey respondents overwhelmingly believe there is a shortage in servicing the needs of the global market (Figure 96), and that multilaterals, governments, and export credit agencies have a role in helping to close this gap. Additionally, while public–private partnerships can help banks close the trade finance gap, there is a wider set of tools available, and the onus of expanding access to trade finance is shared by both industry and public bodies.

The majority of banks only rejected a small percentage (0–10%) of trade finance transactions in 2019 (Figure 97), primarily due to KYC concerns, suitability, and low-quality applications (Figure 98). While this rejection rate is low on the whole, there is a discrepancy across geographies, with applications from Africa, and Central and Eastern Europe, receiving a disproportionately high number of rejections relative to their representation in trade finance applications (Figure 99), contributing to the well-documented trade finance gap, which persists at about USD 1.5 trillion annually according to ongoing analysis by the Asian Development Bank.

In addition to these geographical discrepancies, MSMEs are more likely than other customer segments to be rejected for trade finance support (Figure 100). These businesses represent 29% of total trade finance applications and make up 36% of rejections, again highlighting the extent of unmet demand (i.e. the trade finance gap) that exists in the market, and the degree

Figure 96
Do you believe there is a shortage in servicing the trade finance needs of the global market?

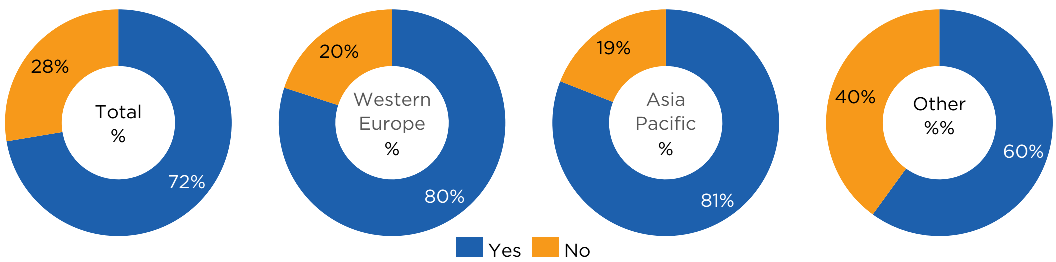


Figure 97
Of the total value of trade finance transactions your bank received in 2019, what percentage did your bank reject/ not support?

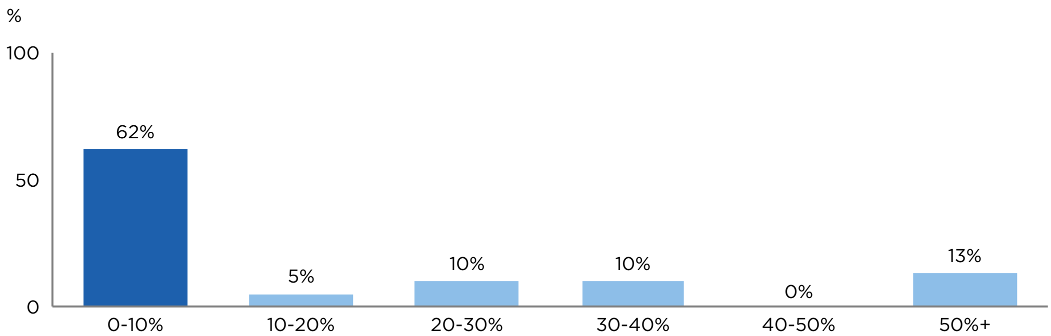
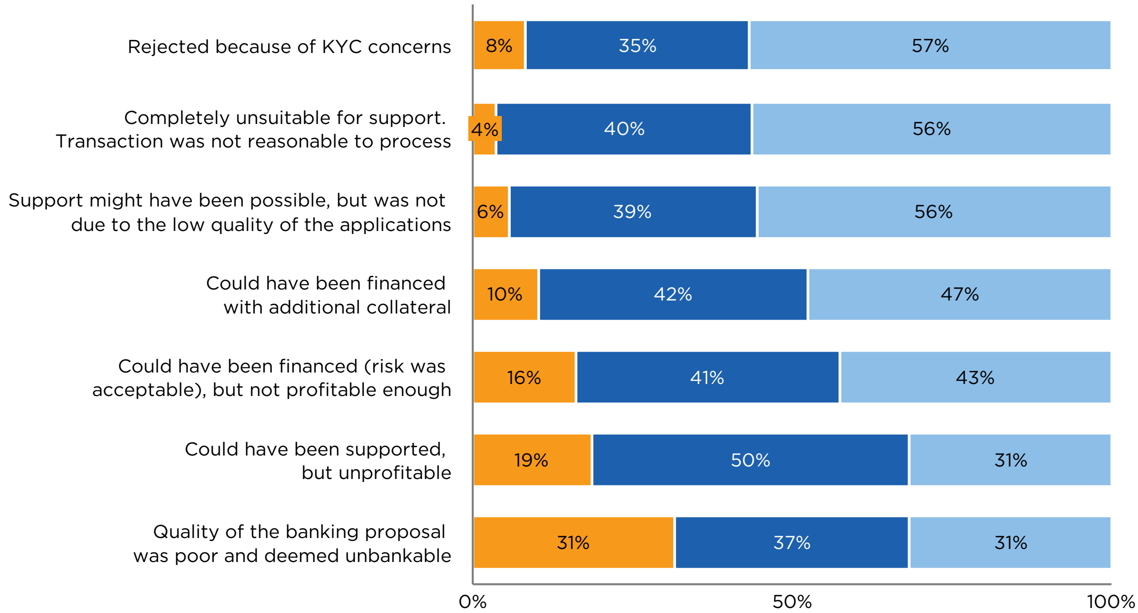


Figure 98

Of the rejected/ not supported transaction applications, please rank the most common reasons that your bank did not support applications in 2019

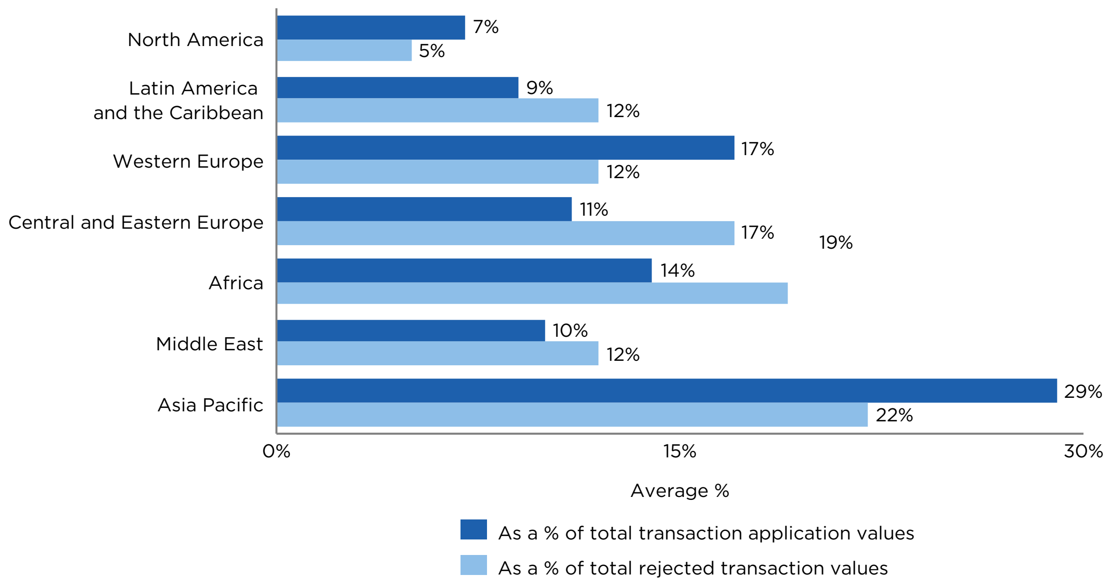


Note: 'Rejected because of KYC concerns' – not that the (potential) client was suspicious, but that the KYC regulatory requirements were too costly and onerous

'Could have been supported, but unprofitable' –regulatory capital on trade finance made supporting the transaction unprofitable

Figure 99

In 2019 what was the percentage breakdown of trade finance applications and rejections per region?



to which MSMEs face a disproportionate challenge in accessing trade financing.

Further, there is little variation in the rejection rate of various trade finance products relative to their share of overall applications (Figure 101), although there are small spikes in rejections for loans or advances against both inventory and receivables.

Banks generally do not receive trade finance support from government or other public institutions to help provide financing to MSMEs (Figure 102). However, Asia Pacific is an exception, with 62% of respondents indicating they receive some public support for MSME financing. In light of this, it is interesting to note that Asia has the lowest rejection rate of all regions relative to the

Figure 100

In 2019 what was the percentage breakdown of trade finance applications and rejections per client segment?

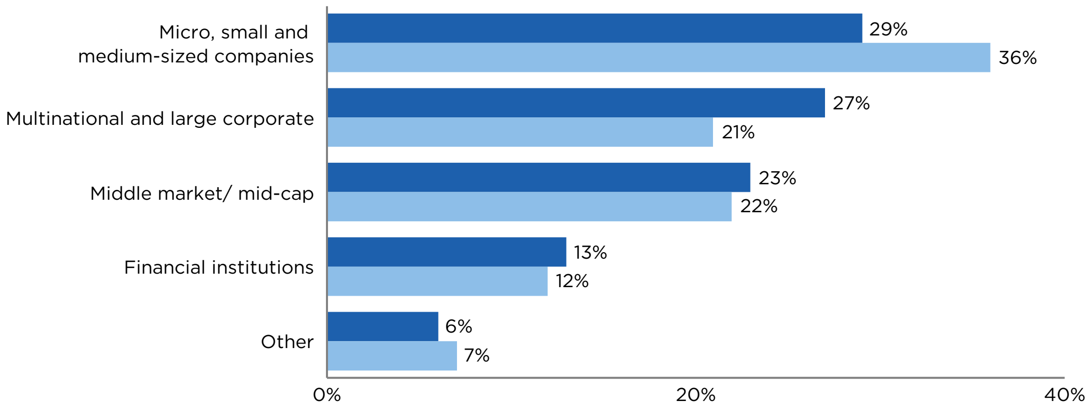
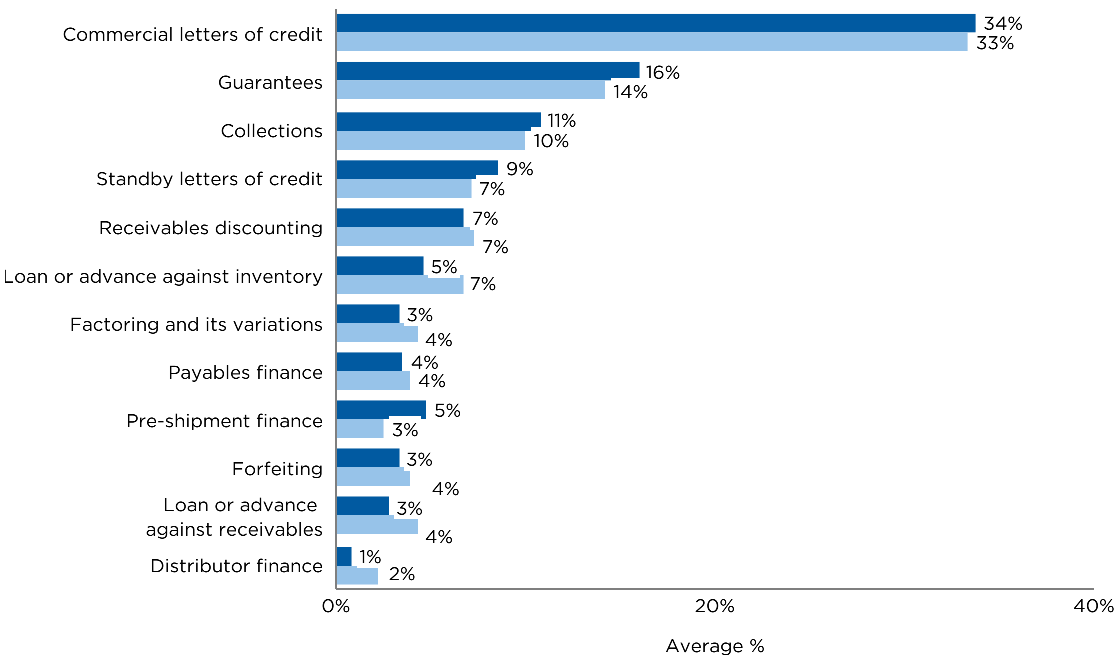


Figure 101

In 2019 what was the percentage breakdown of traditional trade finance applications and rejections per transaction type?



values of their trade finance applications (Figure 100). This may be due in part to the public support offered to MSME financing.

Unsurprisingly, respondents overwhelmingly indicated that government support for MSME financing would help close the trade finance gap (Figure 103), even with multilateral development banks and export credit agencies providing important resources to help banks reduce unmet demand in the trade finance market (Figure 104). The positive reception of these public-private partnerships is encouraging and evidence for further public support to work with industries to close the trade finance gap.

Figure 102
Does your bank receive any type of support for MSME trade financing from the government or other public institutions?

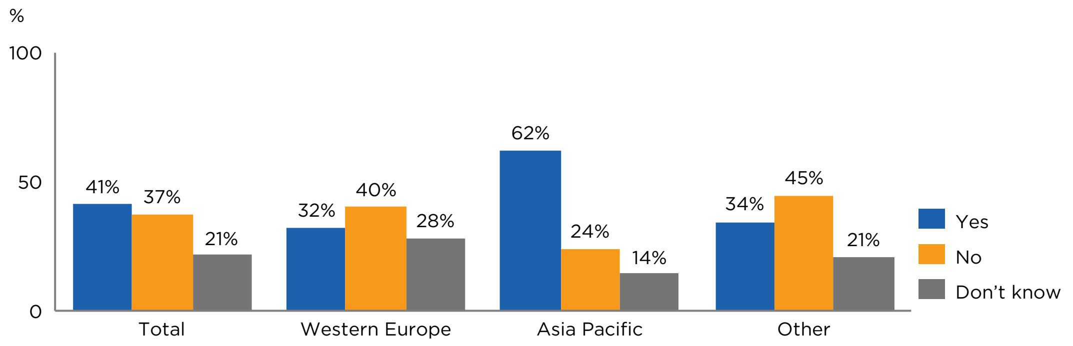
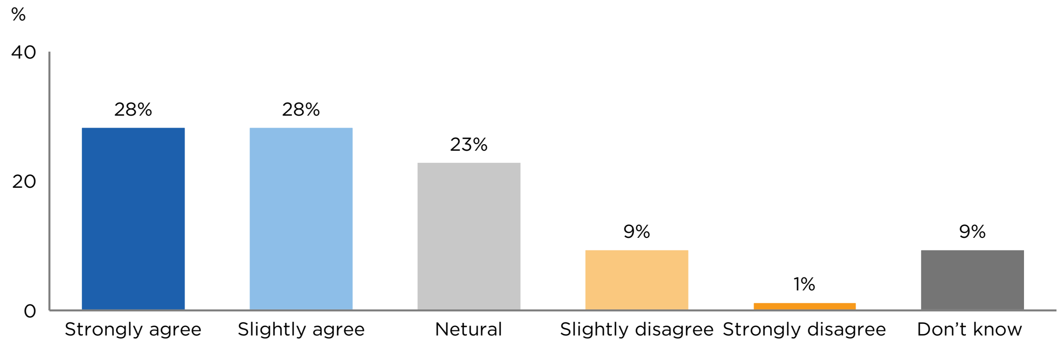


Figure 103
To what extent do you agree that government funding assistance/ partnerships for MSMEs would help in fulfilling demand for their trade finance?



Indeed, amid the COVID-19 crisis, we expect both the need for MSME trade finance and the scale of the trade finance gap to grow, adding to the urgency of government support – both to keep businesses viable today, and to help them recover in a more uncertain future. The ICC has issued an urgent call for decisive action to 'Save Our SMEs', and the Banking Commission has contributed with a specific call for governments to keep trade finance in mind, as they design support programs and mechanisms aimed at dampening the damaging effects of COVID-19.

The digitisation of trade finance and technology solutions are seen as major tools to help banks close the trade finance gap. A significant challenge for trade banks is serving MSMEs profitably. A small ticket letter of credit typically carries a fraction of the fees of a higher value corporate letter of credit, but often has the same – if not higher – operational cost given less publicly available information for KYC, credit assessment,

Figure 104
To what extent do you agree that multilateral development banks and export credit agencies help banks like yours to close market gaps (unmet demand) for trade finance?

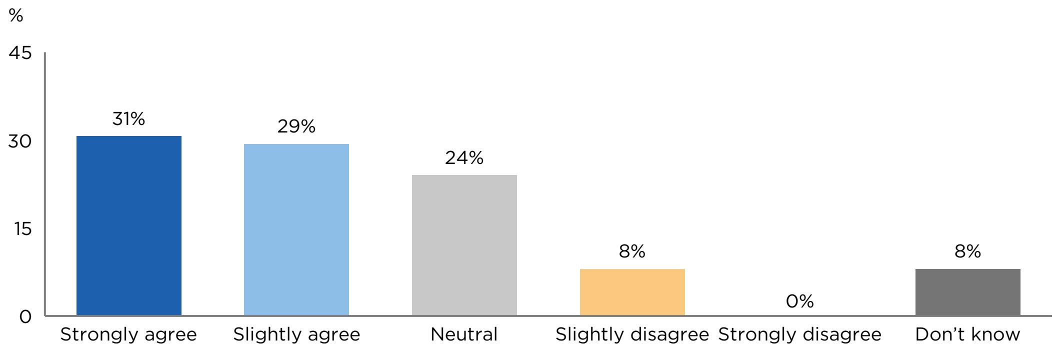
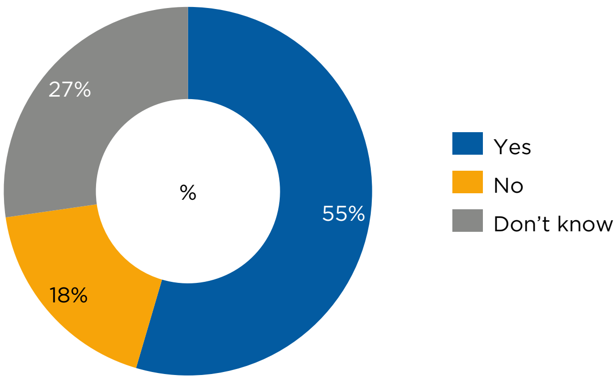


Figure 105
Is your bank positioning itself to maximise the potential to service more MSMEs and close market gaps (unmet demand) through technology?

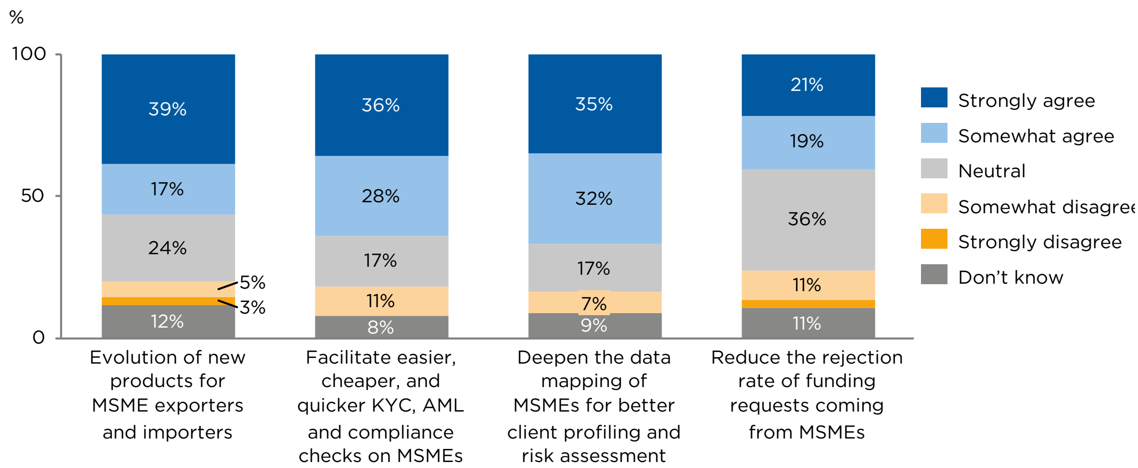


and other due diligence or regulatory requirements.As result, digital trade with self-service sales channels and straight-through-processing operations could open material opportunities.

Survey respondents are positioning themselves to service more MSMEs, with 55% using technology solutions to do so (Figures 105–106). Regional and local banks disproportionality indicated that they are not positioning themselves to do so. This is worrying because it is precisely these types of banks that could have the best reach into the MSME market. This is a further example of how digital trade is not yet sufficiently widespread, and many of the local and regional banks that could serve these MSMEs are behind the curve in its adoption.

Figure 106

To what extent do you agree that technology will enhance your bank's engagement with MSMEs in the following ways?



FEATURE

SMEs and the trade finance gap: it's a data problem...

Catherine Nomura, President and Founder, Kountable

The lack of inclusion of SMEs in global trade is often referenced by the SME trade finance gap, and much has been done to study and try to improve access of SMEs to finance, especially loans, to try to address this gap. Through Kountable's five years of partnering with SMEs in East Africa who struggle to finance trade deals, it has become clear that there is a much larger underlying problem, one which also points the way to practical solutions if we address it head-on. Inclusion shows up and is measured globally as a finance problem, but at its heart, it is a data problem.

The lack of digitisation of SME-involved trade, the lack of access to ERP (Enterprise Resource Planning) capabilities and a system of record capable of capturing the trading activities of sub-enterprise scale businesses, makes trade involving SMEs more difficult to transact and fund on many fronts. Exclusion extends beyond finance to difficulty accessing the best global suppliers and competitive pricing for trade services such as insurance and logistics.

Put simply, capital flows based on the assessment by its owners of risk and return.

The completion of due diligence on trade transactions involving SMEs, and on SMEs themselves, has been notoriously difficult. However, this failure to measure, this lack of reliable data on which to assess the merits of a trade, disguises the fact that much of this business is very investible on commercial terms, especially with data not just for due diligence, but also to manage projects to further mitigate execution and performance risk.

Lack of access to finance is one result of this absence of data and affects even the best SMEs (with outstanding demonstrated execution capabilities) in the presence of high-quality, enforceable contracts with reliable suppliers and investment-grade end payers.

What data is missing in trade involving SMEs?

1. Who the best SMEs are. We need a reliable source of data on which SMEs can execute, not just pay bills. Execution ability is different from and not always correlated with credit-worthiness. KYC data and measures of execution ability are key risk-mitigating data points.

2. Who the end-payers are. KYCC (Know Your Client's Client) is also needed but is often obscured by contract terms set up in tendering processes that require goods to be purchased onshore from SMEs who must first procure them abroad.

3. Is the trade transaction properly constructed to mitigate predictable risks, like those associated with currency fluctuations, contract terms mismatches, inspections, KYC/ KYCC related issues for all parties to the trade, and vetting and verification of contracts and key documents?

4. Real-time project management data, including tracking of milestones and financial flows comparable to what an ERP system integrated with enterprise-grade accounting and treasury management systems provides for larger entities.

With reliable data on all these aspects of an SME-involved trade transaction, capital can flow to this activity at scale because trustable risk profiles can be built and monitored.
On the flip side, failing to address the data problems will hobble any attempt to solve financial inclusion at scale. Unmitigated risk will continue to lead to casualties that sink programs. Guarantees can be part of the solution but are not a substitute for de-risking transactions at an operational level through better business practices, validation of data

integrity, transparency, and timely and secure data flows between the various stakeholders.

With regard to exclusion from quality supplier relationships, which we have seen have national and even global implications in the face of the current pandemic and governments' reliance on SMEs to procure medical products, data also helps. With data, SME buying activities can be aggregated to increase purchasing power to competitive levels, influence policy and take advantage of economies of scale as the cost of servicing trades skyrockets. Their inclusion at this time is critical to the pandemic response of any country that tenders out healthcare procurement.

Fortunately, the basic technological ability to gather this data now exists through smartphone proliferation and fairly widespread internet connectivity. The trade activity that SMEs are involved in, properly recorded and supported through the use of currently available data collection and management systems and tools, makes for an attractive investment option. It is usually short-duration, often supportive of the UN SDGs and ESG goals, high-margin, and offers tremendous diversity across geographies and sectors to fit the goals of a wide range of investment objectives and mandates. If we can solve the data problem, there is every reason to believe the market will respond at scale to the financial opportunity that is currently hidden.

FEATURE

How to increase the professionalisation of trade finance

Dominic Broom, Member, ICC Banking Commission Executive Committee;
Executive Consultant, The London Institute of Banking and Finance

Training and trust

At some point in the process of international trade, one of the parties involved will have to be trusted to handle someone else's money. But who should be trusted? Even in open account financing, making sure that the paperwork is correct and enforceable requires an objective and expert third party.

It is not always easy for companies that export and import goods and materials to know which third party really brings objectivity and expertise to the table. And companies are not the only stakeholders with an interest in ensuring honest, fair and efficient global trade. Governments, financial regulators, investors and, increasingly, NGOs also pay close attention to how trade is conducted. They want to reach a number of critical goals including: preventing money laundering and the financing of terrorism; ensuring that business is carried out in a fit and proper manner; boosting fair and sustainable trade; and closing the trade finance gap. Those are only a few important goals from a much longer list.

The banks engaged in trade finance have a long-standing tradition of upholding the sector's professional standards. They required their staff to undertake ongoing training and to sit rigorous exams that demonstrated their expertise. The Certificate for Documentary Credit Specialists (CDCS) set by The London Institute of Banking & Finance, for example, is a globally recognised benchmark. Banks and their clients can be confident that someone who has passed the exam knows what they are doing. Qualifications like the CDCS were part of the reason why banks were trusted over many decades to support and advise firms in global trade.

No more easy money

So, what's the problem? Financial services firms were able to make a lot of money in the 1990s and early 2000s with a 'good enough' approach to trade finance. Outsourcing was in full swing and supply chains were lengthening. With plenty of demand, banks did not necessarily seek out, or train, as many technical specialists as in the past. Instead, they outsourced many of their own functions to third parties. Graduate recruits, too, focused on more high-profile jobs in banking. That meant that, as trade finance bankers who had been trained under the old system started to retire, an expertise gap opened up. Arguably, a trust gap also appeared.

Then came the financial crisis and, as a trade finance gap opened up around the world, regulators started to look more closely at how banks were being run. What they saw was sobering. Today, they want to see solid evidence of up-to-date professional standards across the industry.

Those standards can be hard to meet. In trade finance, in particular, there are technical rulebooks – the Uniform Customs & Practice for Documentary Credits (UCP 600) and the Uniform Rules for Demand Guarantees (URDG), agreed by the ICC – that practitioners need to understand and apply in detail.

Trade finance bankers also need sound business judgement. They need to know their customers, their customers' customers, and to be able to gauge whether what is being proposed makes 'good honest sense'. That goes beyond having a level head and personal integrity – important though they are. Trade is multipolar, so assessing trade deals takes experience and expertise, a knowledge of the world economy, and ongoing professional development.

The real costs

What regulators want to see at trade finance banks is good governance, operational stability, environmental sustainability, and excellent compliance. None of those are feasible over any period without professionally trained staff.

Training staff, of course, comes with a cost, which is why it has often been neglected. However, loss of client trust, poor regulatory compliance, increased regulatory oversight, and high staff turnover are ultimately even more expensive. Outsourcing certain functions is not the solution. Regulators now want banks to be able to demonstrate that their systems are fit for purpose and sustainable. For most that means more trade finance professionals in-house.

Staff are your business

Finding those professionals will not be easy in the short term. A generation of bankers largely turned its back on training for a career in trade finance, despite the ever-growing need for trade and supply chain financing. That means expert advisors and mentors can be thin on the ground, which has arguably exacerbated the trade finance gap. However, specialist educators, like The London Institute of Banking & Finance and the ICC Academy in Singapore, can help. Their qualifications are recognised industry benchmarks and their staff and examiners are all longstanding industry practitioners. Both offer online qualifications and classroom-based training programmes that support banks and their employees with flexible ways of studying.

What may help even more is the value that younger employees place on access to training and expert qualifications. They know that they need to demonstrate professional excellence and to constantly update their skills and knowledge. They know that automation will transform banking. Blockchain and smart contracts, for example, are often cited as the future of trade finance.

It is certainly true that, over time, many routine tasks in trade finance will be automated – as they have been in other industries. However, what cannot be automated is trust in expert support and advice. Focusing on that will be imperative in banking – particularly when net interest margins are low.

Professionally trained staff will remain vital to the bottom line for two main reasons. One, regulators are much less intrusive when they know that a bank is carefully and appropriately staffed. That cuts compliance costs. Two, and just as importantly, customers appreciate access to trusted expertise. After all, people will shop around if they are buying a commodity product like broadband access. They quibble about the bill much less if they are having their kidney taken out. All they really want to know then is that they are going to be alright.

FEATURE

Successors in Trade: “Is it time to isolate or time to reach out?”

The Successors in Trade (SIT) programme was established by the Executive Committee of the ICC Banking Commission following a recommendation by Mr. Ruediger Geis of Commerzbank in Frankfurt, a long-serving member of the ExCo. The Program was launched in 2018 as a strategic programme to identify and develop the next generation of specialists to support trade finance and SCF practitioners.

An exciting sub-stream of the SIT programme is the Outreach Initiative. Young, talented trade finance professionals are challenged to devise and implement strategies to attract a new wave of trade professionals as members of the ICC Banking Commission and to reach into countries where the ICC Banking Commission is not represented or connected.

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The Outreach Initiative is guided and mentored by a panel of experienced trade finance professionals, who are either members of the ICC Banking Commission Executive Committee or the Advisory Board. They include Dr. Rudolf Putz of the EBRD, Mr. Vincent O’Brien of the Executive Committee, Ms. Ana Kavtaradze from Bank of Georgia, and Mr. Huny Garg from SWIFT.

In this section, SIT team members currently active in the Outreach Initiative share their experiences and insights and how they can bring new members from new countries into the ICC Banking Commission and the ICC itself.

The team is composed of Ms. Irina Chuvakhina (Priorbank Belarus), Ms. Innesa Amirbekyan (ID Bank Armenia), Ms. Antonija Koceva (Komercijalna Banka, North Macedonia), and Mr. Samuel Ansah (Ecobank, Africa).

Ms. Irina Chuvakhina, Priorbank, Belarus

Like many trade finance professionals around the world, I experience ICC every single day of my working life as so many trade banking transactions are based on the application of ICC rules. However, the possibility of playing a part within the ICC Banking Commission would not be something that I would have considered a real possibility. But with the support of my bank and the EBRD Trade Facilitation Programme (TFP), I was invited to participate as a guest at the ICC Banking Commission Meeting in Jakarta, Indonesia in April 2017. My participation was a small but historic step; this was the first time that a trade finance professional from Belarus was included as a delegate in the history of the ICC Banking Commission.

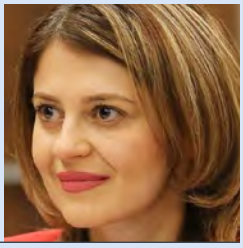
This amazing event and my knowledge about the keen interest of my colleagues from other Belarusian banks in ICC activity whet my appetite for the engagement. I returned home to Belarus inspired to do something to help trade finance professionals contribute to and benefit from participating in ICC Banking Commission.

Unfortunately, there was no immediate path to help the trade finance professionals in Belarus engage with ICC. We had the idea to establish an informal Trade Finance Club in Belarus among the participants of EBRD TFP, and with the assistance of one of our mentors, it was agreed with ICC Paris that if this informal trade finance club evolved into a more formal association, we could join as direct members of ICC.

With this progress in hand, we had a delegation of five trade finance professionals in attendance at the ICC Banking Commission Meeting in Tbilisi, Georgia in October 2018.

I am pleased to advise that with the guidance of our mentors, the key steps have already been taken to form the Trade Finance Association of Belarus with direct membership in ICC. A well-attended meeting of trade finance professionals from commercial banks and the National Bank of the Republic of Belarus endorsed this approach on 18 February 2020 in Minsk, Belarus.

It is fair to say that COVID-19 has slowed our advance but it will not stop us moving forward, and I hope that we will join the ICC family sooner or later and our delegation will attend the Dubai meeting in Spring 2021 as an ICC member.



Ms. Inessa Amirbekyan, ID Bank, Armeni

The SIT Outreach Initiative has empowered me to do what I have always wanted: to build a local and international network of trade finance professionals so that Armenia can prosper in international trade. For me, having good relations with other technically competent trade finance professionals makes business easier and a lot more rewarding.

ICC Armenia was formed in June 2018 and our Banking Commission took its first steps in October 2018. In fact, I was the first formal representative of ICC Banking Commission Armenia to join Banking Commission Meetings, with the first one in Tbilisi in October 2018, followed by the Annual Meeting in Beijing in 2019, and finally the Paris meeting in October 2019. I was all set and registered to participate fully at the Dubai meeting in April 2020 with a young delegation from Armenia, but COVID-19 put an end to that. This was a disappointment as the Dubai meeting had an amazing agenda and the theme reflected what the SIT Outreach Initiative is all about: Connecting the Trade World – shaping the future!

The challenge in Armenia is probably typical of the challenges facing the ICC Banking Commission all over the world in bringing in young talent. Without a doubt there are lots of interested young trade finance professionals wishing to interact with and be part of the ICC Banking Commission. However, decisions for membership are generally made by senior executives who are not familiar with the workings of the ICC Banking Commission and, in many instances, not familiar with the work of the ICC itself.

This situation creates a barrier for the younger and keenly interested trade finance professionals in Armenia to engage with ICC. However, this challenge was turned into an opportunity and a step towards full membership for young trade professionals as I established the first Trade Finance Club in Armenia. We recently held our first oversubscribed meeting in Yerevan, Armenia at the offices of ICC Armenia.

Given our love of trade finance I felt it appropriate to hold the meeting on 14 February 2020. This 'Valentine's Day' meeting was very successful and led to a delegation being formed to attend the April 2020 meeting in Dubai. While the Dubai meeting may now be temporarily postponed, our activity locally and with the other SIT team members continues by digital means. I can honestly say that being part of the SIT outreach team provides a tremendous opportunity to make positive change and we have already come up with a range of new ideas.

Trade finance professionals in Armenia, as in many countries in the region, are familiar with working with the development banks such as the EBRD, IFC, and the ADB. These development banks are partners of ICC in Market Intelligence and in many other areas of trade development and facilitation. These multilateral development banks can provide a bridge to bring in new young talent to the ICC Banking Commission, and this is one core area of activity on which we intend to focus.

Mr. Samuel Ansah, Ecobank, Africa

Given that I am a trade finance professional working at Ecobank, and responsible for smooth operations and trade technology across 32 countries, I have a keen interest in the integration of a new wave of tech-savvy trade finance professionals into the important work for trade development of the ICC Banking Commission.

However, based on my initial research, the catchy slogan of the ICC, "We make business work for everyone, every day, everywhere", may not yet be an accurate reflection of the reality on the ground in Africa.

However, with the support of my Outreach Initiative team members and mentors I intend to change that. Given that Africa is a continent of 54 countries, all eager for trade expansion, the fact that there are fewer than 10 ICC National Committees on the continent is considered by some to be a major disappointment. However, I see it as a great opportunity for the outreach team and the ICC itself.

The time to act is now. In March 2019, African leaders took a major step forward and now all 54 African nations signed the African Continental Free Trade Area (AfCFTA), the biggest trade agreement signed since the World Trade Organization was established.

With the AfCTFA in place, this challenge has become an opportunity for the SIT outreach team, and even amid the COVID-19 pandemic this is the time to think outside the box. My recommendation is simple but effective. When there is no ICC National Committee within a country, trade finance professionals should be able to join through the multilateral development banks that have been working in partnership with the ICC for many years. Should an ICC National Committee be established in a particular country, the membership would revert back through the more natural channel of the typical local ICC National Committee route.

Just think about what can be achieved if we integrate young trade talent from the African continent into the ICC Banking Commission. The raw numbers speak for themselves.

AfCFTA can create a market with GDP of USD 2.5 trillion and a population of over 1 billion, 60% of whom are below the age of 25. Surely, these figures in themselves are a call to action for the ICC Banking Commission and our SIT outreach team.

I have not yet had the honour of attending an ICC Banking Commission Meeting like my other SIT outreach team members, although I was all set with flights booked for Dubai 2020. However, it is always good to see and hear my team members in the virtual world, which is now becoming our norm and it is working well.

Ms. Antonija Koceva, Komercijalna Bank, North Macedonia

The leading trade finance banks in North Macedonia are members of the EBRD's TFP. Many of these banks have won international recognition for their services by international financial institutions and many of the trade finance professionals themselves have achieved exceptional results under the electronic learning programme of the EBRD. I have also graduated and hold my EBRD trade finance certificates with pride.

In North Macedonia there is an ICC National Committee but until now there has been no active Banking Commission within its framework. Recently there has been tangible progress in forming this commission and we are looking forward to the launch and active participation of the highly motivated trade finance professionals in North Macedonia.

By being part of the SIT Outreach Initiative and actively participating at ICC Banking Commission Meetings in Beijing and Paris, I have learned about the essential activities of the ICC Banking Commission. I have been inspired to mobilise local trade finance talents for an active ICC Banking Commission in North Macedonia.

Through special arrangements facilitated by our mentors and the ICC UAE I had put together a small but highly interested delegation to attend the Dubai 2020 meeting. With the Dubai meeting postponed, I urgently needed an event to maintain the momentum and interest in the ICC Banking Commission within the trade finance community in North Macedonia.

Thankfully the EBRD TFP took the initiative of agreeing to host a trade finance training and information event in our capital city Skopje on 17 March 2020. I am glad to advise that this event was highly successful with the participation of commercial banks, the central bank, and a highlight being a presentation by ICC North Macedonia on the benefits of being part of ICC.

The Dubai meeting being postponed was a major disappointment for my SIT outreach team members and me, and the COVID-19 lockdown and distancing temporarily derailed our momentum in the SIT programme and the Outreach Initiative.

However, we are now re-energised, re-focused and making maximum use of videoconferencing and other communications technology to achieve our objectives.

The next substantive step of the SIT Outreach Initiative will be to host an Outreach Initiative Webinar with participation of the respective ICC National Committees and the soon-to-be-formed Trade Finance Association of Belarus.

With our dynamic mindset and drive to be real Successors in Trade we will take every opportunity to turn the challenges of evolving global isolation into a reality of a dynamic and inclusive ICC Banking Commission global outreach initiative

The mentors for the SIT Outreach Initiative commend the team for their commitment and innovation in the pursuit of their team objectives and believe these young trade finance professionals are showing the way forward for the expansion of the important work of the ICC Banking Commission.

Successors in Trade Outreach Initiative Team

Ms. Irina Chuvakhina, Priorbank Belarus
Ms. Ana Kavtaradze, Bank of Georgia
Ms. Innesa Amirbekyan, ID Bank Armenia
Ms. Antonija Koceva, Komercijalna Banka
Vincent O'Brien, ICC Banking Commission

Final Successors in Trade Outreach Initiative before COVID-19

On 17 March 2020, the Successors in Trade Outreach Initiative with the support of the EBRD held an educational and informational event in Skopje, North Macedonia where ICC presented the benefits of ICC membership.

FEATURE

Mind the gap: why we need to think about small exporters

Dr. Rebecca Harding, CEO, Coriolis Technologies

The World Trade Organization's latest outlook for global trade makes grim reading. The COVID-19 pandemic could cause a drop in world trade of between 13% and 32% in 2020; this largely mirrors BCG's own analysis presented earlier in this report. The trade community has been watching inventory stock plummet since February, and while at the outset of the crisis this was simply a supply chain disruption, the complete global lockdown of our daily lives has caused a drop in global demand for goods and services like no other in recent memory. Even the IMF, which has been one of the more optimistic global forecasters over the last decade, is predicting a drop in global growth of up to 3%.

Within all this mayhem, spare a thought for the smaller businesses that form part of the global supply chains that define the way in which global trade works. These businesses are at the end of the supply chains and reliant on payment of invoices for their finance. They may well have contracts to supply goods or services to players further along the chain, but if the whole trade system grinds to a halt, then these invoices are not paid, and the contracts are not honoured – very simply because the goods at the end are not delivered to the client.

Here is the problem: if I am a small exporting business with a turnover below, say, GBP 5 million, then I probably do not know about export credit agencies, and I almost certainly fall outside of the banks' commercial banking reach. I therefore rely on the contracts I have and the swift payment of invoices to fund my business through cashflow. Even if I am supplying an essential good or service, I will find it difficult to access support schemes because I am too small and reliant on my invoices, not working capital loans or turnover. If the invoices against a contract stop being paid because the goods at the end of the chain aren't being delivered or even demanded any more, then my business runs out of cash very quickly. Because I am looking to have an invoice financed rather than a loan, I may fall outside many of the support structures currently on offer globally.

So, is the solution a digital one? The sector has been talking about the need for big data and artificial intelligence to create compliance and onboarding solutions; blockchain is regarded as one of the most effective ways of moving from manual trade finance processes to secure digital transactions. As a result, there are many fintech solutions out there in the market that have sought to digitise trade finance from the supply side. They streamline transactions and payments securely and generally save banks time and money, making them more efficient and effective.

The COVID-19 pandemic has revealed the importance of the demand side – in other words, the need for trade finance among a group of very small businesses who are currently excluded from existing, largely corporate, solutions. The legacy of the global financial crisis was to push trade finance providers away from these smaller companies because, in an environment where unorthodox monetary policy was keeping yields low, the due diligence and onboarding costs relative to deal size for the smallest businesses were simply unsustainable. Many of the digital solutions that have evolved since then have either directly or indirectly sought to close the SME trade finance gap by offering quicker onboarding and compliance tools to banks so that they can provide money to these businesses more readily.

There is limited evidence that digital solutions are substantially closing the gap, however, and COVID-19 is likely to widen it again. This is because these solutions do not address the demand side. That is, many of the SMEs, according to the OECD , are micro businesses that contribute to value added trade – that is, to critical value-adding parts of supply chains. So, while these businesses may be tiny, they add to global trade in terms of innovation and supplying a very specific part of the supply chain, but do not necessarily even know that trade finance solutions are available to them.

The technology challenge for the sector that emerges from this crisis is to develop digital technologies that are almost akin to trade finance marketplaces – where demand and supply can meet securely and where the SMEs drive the type of finance that they need with full transparency of how they appear to the banks in terms of risk. There are indeed marketplace solutions that are beginning to emerge, but the urgent pressure now is for the SMEs themselves to understand that trade finance is a viable solution in the current global lockdown if they have invoices or contracts. Rather than a supply-side digital marketplace, this is a demand-led Open Trade Finance solution – much as Open Banking has been in the retail sector. Unless this type of solution can be found, the supply in the market will always outstrip the demand.

OUR PARTNERS

We thank our valued partners for their ongoing contributions

Boston Consulting Group

Boston Consulting Group (BCG) plays a central role in the Global Survey by supporting the day-to-day project and the development of the survey and overall report, and by contributing a strategic, value-focused perspective to the core topics.

BCG is a global management consulting firm and the world's leading advisor on business strategy. BCG partners with clients from the private, public and not-for-profit sectors in all regions to identify their highest-value opportunities, address their most critical challenges, and transform their enterprises.

BCG's expertise in the Financial Institutions sector spans all major topic areas to give global, regional and local banks detailed insight, knowledge and analysis across markets. Trade finance is an established and growing topic area for BCG's Wholesale and Transaction Banking practices. BCG has worked on more than 25 recent trade finance-related projects globally on industry questions and challenges such as market entry and growth, pricing, cost reduction, operations, and digital change and transformation.

By partnering with ICC on the Global Survey, BCG aims to bring additional strategic insight, commercial, and technical industry perspectives to the table for maximum value for the reader base.

Beyond the ICC Global Survey, BCG continues to actively support the trade finance community with thought leadership, including releasing a publication with SWIFT ahead of SIBOS last year: Digital Ecosystems in Trade Finance. In addition, BCG once again supported the ICC and its editorial board in co-authoring the 2019 ICC Trade Register.

BCG was founded in 1963. It is a private company with more than 90 offices in 50 countries. For more information, please visit bcg.com.

TXF

We would also like to thank TXF for their continued contributions, including a feature in this year's report based on market sentiment data collected from TXF Research's global Export Finance Industry Report 2020, scheduled for release at TXF Global in 2020, and closed deal data from TXF Data. Along with TXF Essentials, the market leading platform for in-depth news and stories in the export, trade and commodity industries, these three strands make up TXF Intelligence, TXF'S new business intelligence platform

For more information on the TXF's data used in this feature, please contact:
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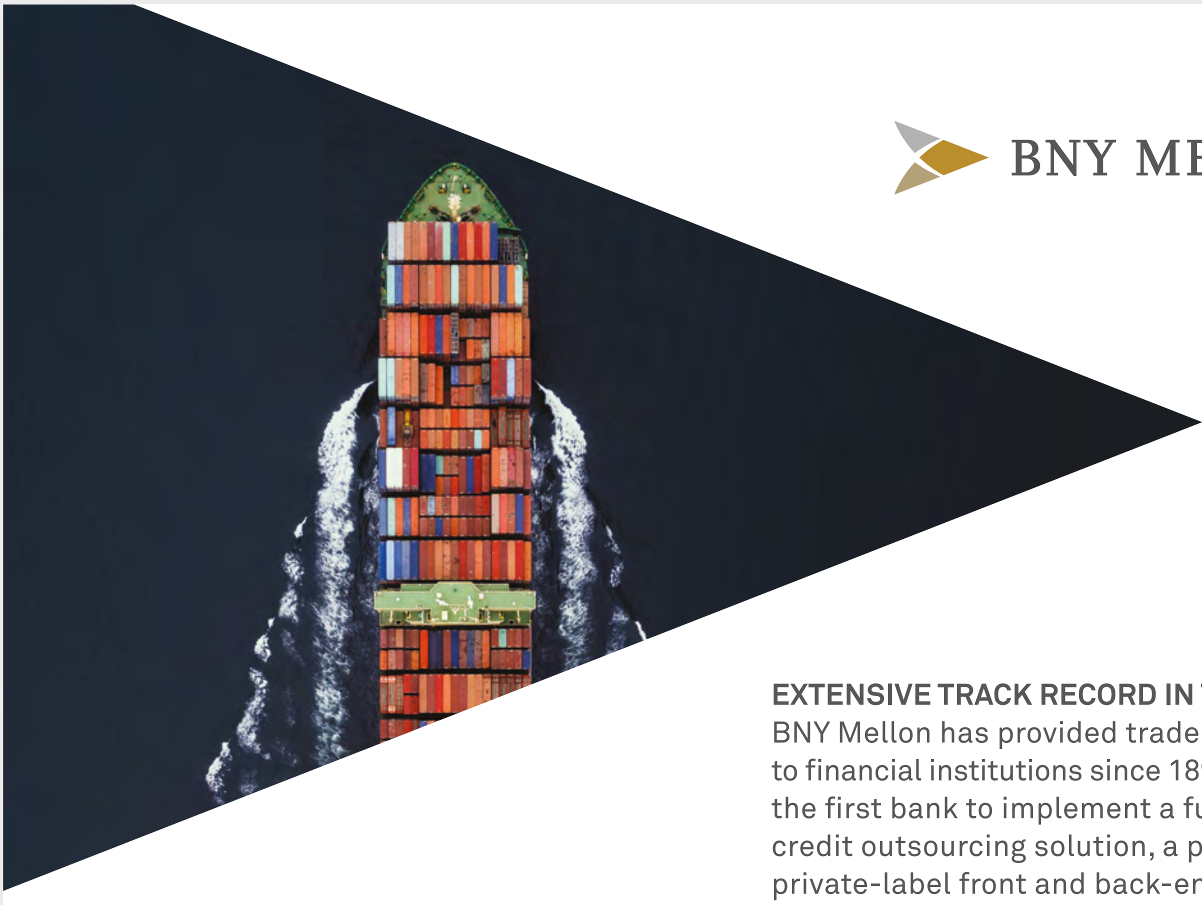

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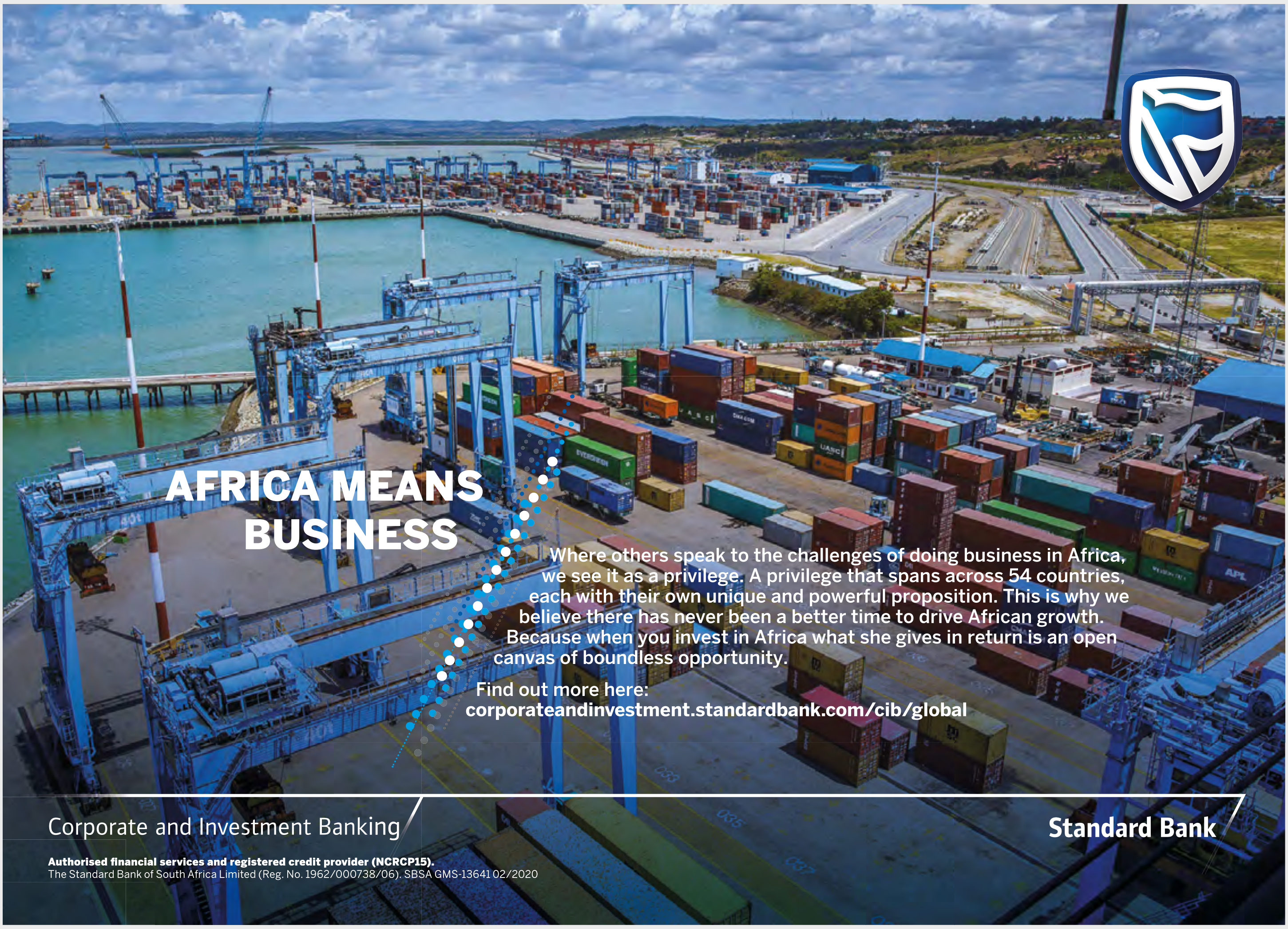
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ICC BANKING COMMISSION

The world's essential rule-making body for the banking industry

The International Chamber of Commerce (ICC) is the institutional representative of more than 45 million companies in over 100 countries. ICC's core mission is to make business work for everyone, every day, everywhere. Through a unique mix of advocacy, solutions and standard setting, we promote international trade, responsible business conduct and a global approach to regulation, in addition to providing market-leading dispute resolution services. Our members include many of the world's leading companies, SMEs, business associations and local chambers of commerce.

Rules

The ICC Banking Commission produces universally accepted rules and guidelines for international banking practice. ICC rules on documentary credits, UCP 600, are the most successful privately drafted rules for trade ever developed, serving as the basis of USD 2 trillion trade transactions a year.

Policymaking

The ICC Banking Commission is helping policymakers and standard setters to translate their vision into concrete programs and regulations to enhance business practices throughout the world.

Publications and market intelligence

Used by banking professionals and trade finance experts worldwide, ICC Banking Commission publications and market intelligence are the industry's most reputable and reliable sources of guidance to bankers and practitioners in a broad range of fields.

Dispute resolution

The ICC Banking Commission and ICC International Centre for Expertise administer the ICC Rules for Documentary Instruments Dispute Resolution Expertise (DOCDEX) to facilitate the rapid settlement of disputes arising in banking.

Education and certification

The ICC Academy is the world business organisation's ground-breaking e-learning platform. Its industry-relevant Global Trade Certificate (GTC) provides an extensive overview of trade finance products and techniques.

Specialised training and events

In addition to its bi-annual summit, gathering over 300 international delegates every six months, the ICC Banking Commission organises regular seminars and conferences around the world, in partnerships with ICC national committees and other sponsors.

Strategic partnerships

Well-established collaboration with leading policymakers and trade association, including WTO (World Trade Organization), ADB (Asian Development Bank), Berne Union, EBRD (European Bank for Reconstruction and Development), IDB (Inter-American Development Bank), IFC (International Finance Corporation), IMF (International Monetary Fund), SWIFT, the World Bank and others.

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