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Is Your Trade Finance Firing On All Cylinders?

Amey Prabhu, 17-May-2019

Introduction

A study[1] published by Asian Development Bank shows that the businesses world over struggle to get credit from the banks and this has resulted in a trade finance gap of $1.5 Trillion in the year 2016 alone. The same study cites that the cost, low returns and complexity of the due diligence were the prominent reasons for the banks' reluctance to finance small businesses. It is interesting to note that, in the year 2016, the volume of the world merchandise and commercial services trade saw a decline of three[2] percentage points over the 2015 numbers.

Thus, in a market, which saw a decrease in the trade activity, the banks declined or let go the opportunity worth $1.5 Trillion due to the cost and complexity of trade finance. The trade finance in its current avatar involves multiple parties, needs navigation through a maze of regulations, and manually processes plethora of, mostly physical, documents. This, combined with low technology adoption, brings in the inefficiencies and escalates the cost of processing and compliance.

Over the last decade, technology has had a disproportionate and profound impact on every sphere of human life. Today, every sector of the world economy – finance, healthcare, education, communication, real estate, manufacturing, retail, entertainment, agriculture and others – is either watching with keen interest or is already a part of the digital revolution.

The banking sector saw the retail banking businesses consume technological innovations at a pace much greater than their corporate banking siblings did. Corporate banking, especially trade finance, has been around for long and has seen very few changes technologically.

The trade finance banks are now taking brisk steps in the direction of superior customer experience, improved operational efficiency and innovations in the business model, the cornerstones for digital transformation of any organization.

The competition to improve the topline and the bottom line is intense and the delay to take timely and effective action can lead to annihilation.

What plagues Trade Finance?

Inefficient Processes

For long, trade finance has been the proverbial problem child for the banks. By nature, financing a trade is a paper intensive process. Multiple cross-border parties have a role to play and absence of correct, complete, instant, compliant and reliable communication can impede critical decisions. Trade finance also requires deft navigation through the maze of regulations within the country of origin as well as the country of destination.

In the age of scanning apps and PDFs, paper documents find a place of prominence in the world of trade finance. In addition to being impediments to efficiency of processing, the paper documents are prone to slow and/or delayed delivery, tampering, damage, theft and loss. Document examination - for correctness, completeness and compliance - is largely manual and is open to human error. The back office personnel are humans and incorrect data entry is a reality.

Thirty plus documents running up to hundred pages in total, close to hundred unique data fields and ten plus parties involved in multiple interactions with the data at multiple stages of the trade transaction makes it a tedious, costly, error prone, risky and complex process for the bank as well as the customers.

<u>Inferior Customer Experience</u>

Customers today are smarter and have higher expectations than ever before. They have a low threshold for tolerance and personalized experience on all the customer touchpoints is the new normal. The new age brands have set the bar and the digitally aware customer has experienced instant gratification in every interaction they have. They abhor visiting the bank and expect the bank to be available on their smartphones.

The current arrangement requires multiple visits to the bank for KYC and submission of trade documents for credit sanction and disbursal of funds. Then another trip to claim the ownership of the goods.

Corporates do not have on-the-go access to the status of the documents, credit limits or the goods. The information is fragmented and distributed across systems.

<u>Rudimentary Business models</u>

Maersk, running the cargo business for a century, is now offering trade finance with the containers as collateral.

Peer to peer lending is a reality and it is easy for individuals running small businesses to borrow without collateral. For the lender, it offers an opportunity to earn higher interest rate than the bank deposits.

Wallets have made it easy to hold funds and make small purchases

However, the corporate banks continue to offer the decade old trade financing products. The business model has not changed much and the focus continues to be on earning revenues through interest and fees. With the advent of digital technologies, there is an opportunity to create new and more profitable revenue streams.

The Technology Story

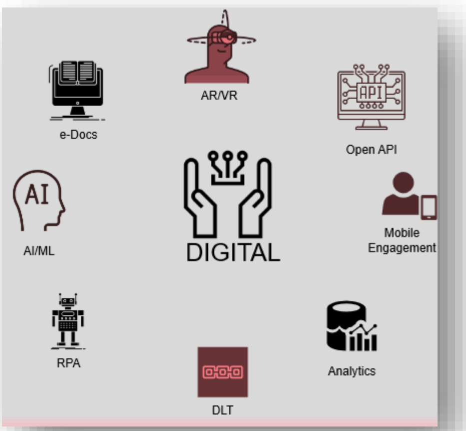
As per the survey[3] undertaken by Ovum, the digital transformation budgets are set to increase by 31% in the year 2019. This and multiple other studies have repeatedly state that the organizations that adopt digital transformation report revenue and margins significantly higher than their peer group.

Banks in the business of trade finance are warming up to the digital reality and are taking a long-term strategic view. The erstwhile “scratch-the-surface” moves like addition and/or integration to corporate internet banking are giving way to replacement of ageing systems with platforms designed for the new digital world.

Not surprisingly, as recent as April 2019, one of the world top three banks by transaction banking revenue signed up to replace its time tested and stable but monolithic, aged and inflexible mainframe based trade finance system. The replacement is a modern, agile, open and flexible trade finance platform.

September 2018 saw the third largest bank in Singapore take a similar step. It kick started the program to replace its homegrown, mainframe trade finance system with a modern, web based, digital trade finance platform.

The replacement would enable the banks to respond faster and cheaper to the market needs, leverage the emerging technologies, enhance customer experience through higher levels of digital engagement and foster innovations on the open architecture. These platform changes improve the banks preparedness to seamlessly adopt and assimilate the technological advancements.



Year 2018 saw 52.2% of all website traffic worldwide generated through mobile devices, up from 50.3% the previous year. By the end of 2019, 67% of the world population would own a mobile phone. The world is on the threshold of transition to 5G, which will increase the network speed from the current 300 MBPS to 10 GBPS. The data is cheaper than ever.

Faster network, cheaper data, cheaper devices and the comfort of doing things on the go has driven the explosive growth in the percolation and adoption of mobile apps. Banks are not far behind and the year 2018 saw a Y-o-Y increase of 3.8% in the mobile banking users.

Robots have taken over the labor intensive and repetitive work. Artificial intelligence is revolutionizing decision-making, contextual conversations and risk mitigation. Machines are becoming adept at tasks through continuous learning. Analytics is helping businesses to make targeted offers and increase the hit rates while offering personalized experience to their customers. Networked non-living objects have started sensing and generating actionable data. API ecosystem is helping developers, FinTechs and the banks to collaborate and build new applications. Consortiums like R3 and Marco Polo are funding and leading the innovations on use cases for Blockchain in BFSI.

Investments in digital technologies and proof of concepts have started finding audience in the boardrooms.

Historic Opportunity to transform Trade Finance

The corporate customer purchasing any trade finance product has to face the dual challenge of time and cost. The banks are not too happy with the revenue and profitability from the trade finance business.

The previous sections focus on the inefficiencies embedded in every stage of the trade finance process from application to disbursement and repayment.

This section focusses on the options available to solve the time and cost problem for both the banks and the bank's customers while making the trade finance process a delightful customer experience.

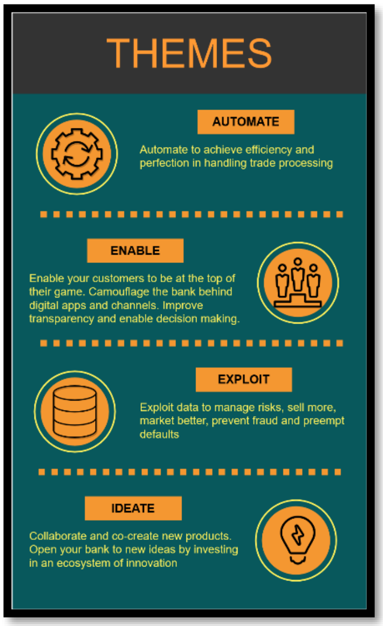
Advent of modern technologies and the ecosystem of collaborative innovation offers an historic opportunity to unravel the troubles afflicting trade.

Digitally reimagining the business of trade finance leads us to multiple themes for refinement, dominant among them being

A) Automating the document handling and trade processing
B) Minimizing the customer visits to the bank by enabling self-service and increasing transparency through intuitive dashboards

C) Exploiting internal and external data to the advantage of the customers, bank staff and the bank

D) Creating or participating in the API ecosystem to innovate by creating new product/service lines or renewing existing products/services



Automate

KYC:

Scandinavian banks and financial institutions leave their first time customers spellbound when the customer enters his SSN (Social Security Number) to onboard and in some cases, get instant credit. The KYC, AML, PEP/Sanctions List checks and the credit assessment is paperless and automatic.

While that is for the retail customers, for corporate customers too, there are solutions that look through the electronic company registry to validate the business and fetches the information on the individuals running the business. The KYC for these individuals then happens through their social security numbers. Digital or e-KYC is quick and easy due to the availability of verified customer information linked to social security numbers.

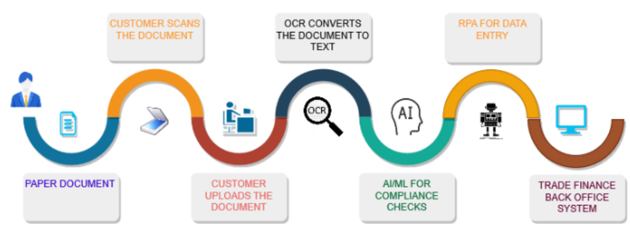
Another option is to centralize the KYC and Blockchain offers a formidable alternative. Banks come together to form consortiums and agree on the terms and conditions of the KYC. Once verified, the documents in electronic form are stored securely on the Blockchain. Customer has control on the documents stored and can share the information on need to know basis. Smart contract renders the KYC documents invalid once the validity period of the KYC is over.

AML/PEP/Sanctions List & Credit Assessment:

Numerous AML service providers that flag the appearance of the business or individuals have rendered the AML and Sanctions List information just an API call away. So is Credit assessment. Post onboarding, regular fetch of data can ensure monitoring the customer for appearance on AML/Sanctions List or change in the Credit Rating.

Trade Documents:

Availability of a legal framework for e-documents is making it possible for the trade finance parties to exchange document in electronic format. Solutions provided by electronic document platforms like Bolero® and essDocs® has the potential to disrupt the way documents are shared today. Subscription based models minimizes the infrastructure and the installation cost and makes it an attractive proposition for the banks, cargo carriers, corporates and other parties. These solutions also accept the scanned documents and so the parties that do not have the infrastructure to produce electronic documents can rest assured.



Document Scrutiny:

Artificial Intelligence (AI) and Machine Learning (ML) are moving closer to take up the job of scrutinizing the documents for compliance to the terms and conditions of trade.

Data Entry:

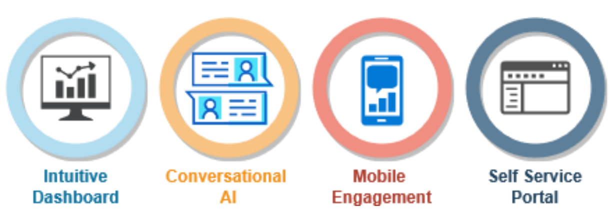
Optical Character Recognition (OCR) combined with Robotic Process Automation (RPA) provides a cost effective, almost error free and faster alternative to manual document reading and data entry into the trade processing systems.

Enable

Assisted Onboarding:

Conversational AI is proving to be an effective tool to help the customer to complete his onboarding without hassles by responding to any queries the customer might have during the onboarding workflow.

Onboarding is an opportunity for the bank to cast a good first impression about the brand. If speed and convenience are the hallmarks of gratifying customer onboarding then unobtrusive data capture, minimal or no visits to the bank, electronic documents, digital compliance checks and intelligent sanction of credit limit are the means to achieve it. Efficient onboarding leaves behind a happy, loyal customer and a bank that reaps rich dividends by reduction in cost.



Self-Service & Intuitive Dashboards:

Modern Corporate Internet Banking solutions are comprehensive tools for the corporates to request for products, submit the documents necessary, check the status of the products purchased and pay for the products as necessary. Mobile versions of these solutions makes it possible for the corporates to inquire and act at a place and time of their choice.

Exploit

Predict Delinquency:

Predictive Analytics makes it possible to gauge the probability of the asset going delinquent. There is enough data available internally and externally to arrive at a reasonably accurate conclusion.

Sell More:

Another effective use of the data is to cross sell products based on the history of the customer transactions and predicting his need for either trade finance or other products.

Preempt Risks

Monitoring the health of customer's business and that of customer's customer through the data on industry outlook, quarterly profits, deals won or lost, political situation in the country of trade and currency fluctuations helps the bank take preemptive steps to manage risks.

Improve Customer Service

Analysis of customer call records, emails and social media posts helps fine tune the customer service and take the steps necessary to improve customer advocacy.

Ideate

Open Banking:

Embracing the open banking API ecosystem helps the banks to enhance the existing services and offer new services to their existing customers whereas a bank with innovative services attracts prospective customers.

Trade Finance on Blockchain:

Blockchain is crawling into our lives. Multiple investments, collaborations and experiments are trying to bring to life the use cases relevant to the humankind. Trade Finance, due to its complexities and inefficiencies, is subject of multiple proof of concepts on Blockchain. Secure and tamper proof storage of documents, controlled visibility of status of the trade transactions to every party involved and actions triggered on encoded logic is a huge advantage that the Blockchain network provides over the traditional methods. FY 2020 might see some of the banks go live with Trade finance on the Blockchain.

Conclusion:

Technologically untouched for the past decade, the banks across the globe look at trade finance as a lever to generate higher revenues and profits. Customer demands for transparency and smooth user experience are pushing the envelope further.

Plethora of options backed by multiple technologies makes trade transformation an intriguing proposition. One size does not fit all and choosing the right technology & technology partner to solve the problem at hand is the key to success.

Tech Mahindra understands your trade finance business and facilitates your journey to improved efficiency and superior customer experience by providing gainful insights, designing the roadmap and implementing the digital agenda.

Footnotes :

1- ADB Survey 2017
2- WTO Statistics
3- Ovum Survey on Digital Transformation

About The Author

Amey Prabhu is a Principal Consultant with Tech Mahindra who leads the Trade Finance Domain Competency Practice. In this role, he is engaged in designing innovative solutions in the Trade Finance space leveraging internal capabilities as well as partnerships with FinTechs. Amey has extensive experience in consulting, business analysis, project management and product development with deep understanding of technology as well as the domain landscape. Amey brings with him 16+ years of rich experience in the Banking domain and has been part of trade finance initiatives at multiple domestic and international banks.

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