# Digitalization of Trade Finance

Opportunities for Banks and Corporates

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Tuesday, March 27th, 2018

2:00 PM EST

# Today’s Presenters

## Carol Chiu

*Head of Product Strategy*

Premium Technology

Carol has over 15 years of senior advisory experience within Wholesale Banking, with a specific focus on successfully launching innovative Trade Finance and Supply Chain Finance product and service offerings for large institutional clients, and streamlining operational processes and delivery models.

## Craig Jeffery, CCM, FLMI

*Founder & Managing Partner*

*Strategic Treasurer*

Craig Jeffery formed Strategic Treasurer LLC in 2004 to provide corporate, educational, and government entities direct access to comprehensive and current assistance with their treasury and financial process needs. His 20+ years of financial and treasury experience as a practitioner and as a consultant have uniquely qualified him to help organizations craft realistic goals and achieve significant benefits quickly.

## David Hennah

*Global Head of Trade & Supply Chain Finance Products*

Finastra

David Hennah leads the trade and supply chain finance product management team at Finastra having previously re-joined Misys from SWIFT, where he spent eight years driving the industry body’s financial supply chain strategy. David spent over twenty years in a variety of senior roles at Barclays, spanning all areas of the transaction banking business.

## Art Lorenz

*Former Treasurer & Senior Director*

*Hunter Douglas*

Art Lorenz, most recently Treasurer & Sr. Director of Finance at Hunter Douglas Inc., a global market leader in custom window coverings.  Mr. Lorenz had the dual role overseeing the treasury and FP&A functions for the organization. Lorenz was responsible for the treasury, credit, banking, risk management, planning, budgeting, forecasting, management reporting and analysis functions.

# Topics of Discussion



- **Introduction: Trade Finance**
  - Overview
  - What is it & Who is Involved
- **What Does Each Party Want Out of Trade Finance?**
  - Banks & Corporates
  - Globalization
- **Obstacles to Trade Finance**
  - Regulation & Compliance
  - Risk & Financing
  - Digitization
- **Owning Trade Finance: Banks vs. Fintechs**
  - Varying Strengths
  - A Competitive Yet Collaborative Environment
- **Digitalized Trade Finance: Advantages**
- **Key Considerations**

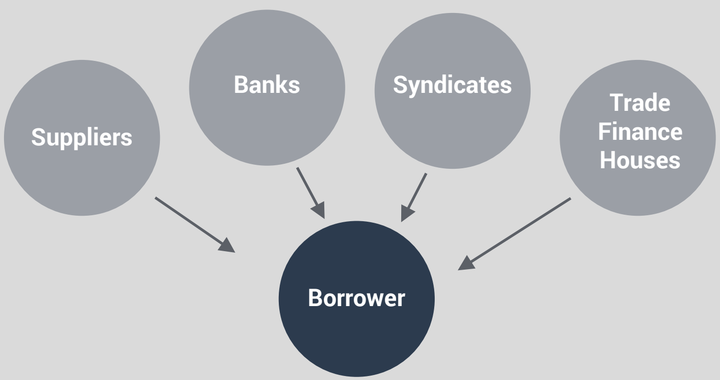
# Trade Finance: What is it?



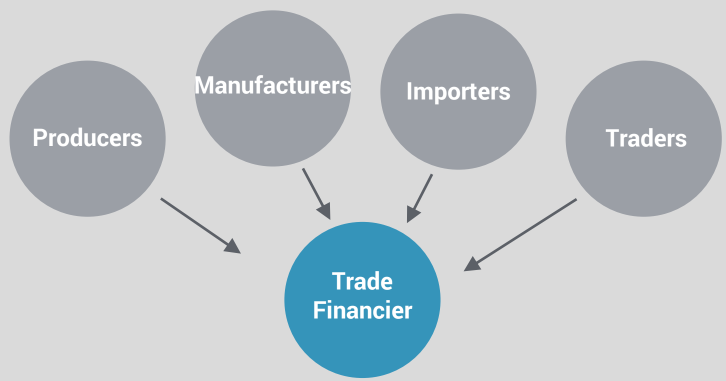
## What is Trade Finance?

- The mitigation of risks (counterparty, country, market)
- The facilitation of secure and timely payments
- The provision of financing for buyers, sellers and other members of the value chain
- The provision of information about a transaction and related financial flows

### Providers of Trade Finance




### Users of Trade Finance




*Source: Trade Finance Analytics*

# The Umbrella of Trade Finance



## THE TRADE & SUPPLY CHAIN UMBRELLA

### Traditional Trade Finance

- Letters of Credit
- Collections
- Standby letters of credit
- Guarantees
- Participations
- Shipping guarantees
- Reimbursements
- Bankers acceptances

### "Bank-assisted" Open Account

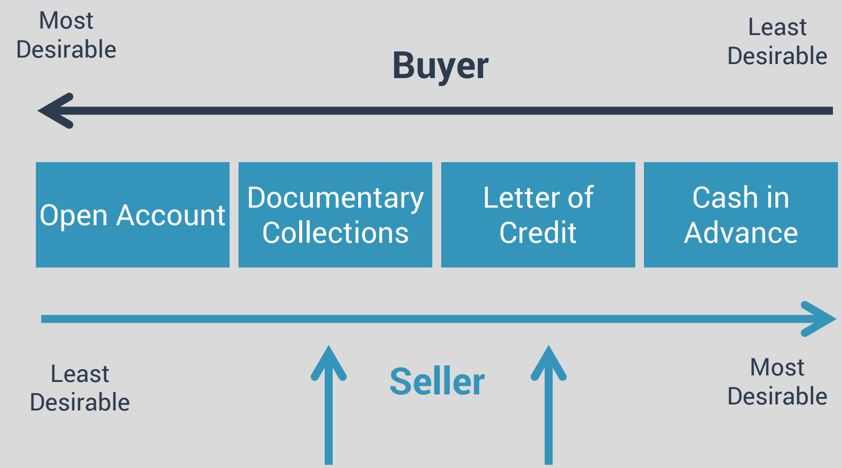
- Receivables Discounting
- Forfaiting
- Factoring
- Payables Finance
- Loan or Advance against receivables
- Distributor /dealer finance
- Loan or advance against inventory
- Pre-shipment finance
- Bank Payment Obligation

- In the vast majority of cases, traditional trade finance refers to letter of credit. In a majority of cases, supply chain finance similarly refers to approved payables finance.
- Just as letters of credit have become synonymous with trade finance, so approved payables have become synonymous with supply chain finance. The ICC and others have invested time and effort to dispel this misrepresentation.

# Trade Finance: Key Components

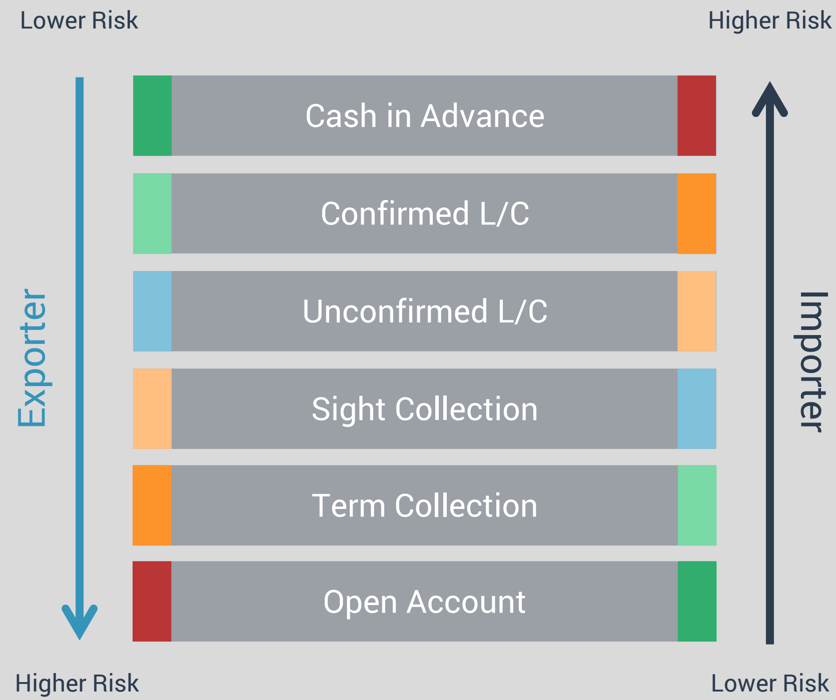


## Trade Finance Spectrum: Risk Profiles & Credit Terms




- In traditional trade finance banks have visibility into the underlying transaction which enables them to offer:
  - Risk mitigation
  - Payment assurance
  - Working capital finance

- Supply chain finance is normally applied to help banks provide assistance to buyers and sellers who choose to trade in an open account environment




- Generally speaking, the terms available to buyers/sellers in a trade finance agreement have inverse impacts on each party (i.e. what is best for the exporter is of great risk to the importer).

# Trade Finance: Standard Workflow



## Trade Finance Workflow


### Trade Finance Workflow

The standard trade finance workflow typically begins with a buyer initiating a purchase of goods, and then entering into negotiations for a trade financing agreement. The parties involved in this process include a buyer/supplier and each party's respective bank(s).

**1. Goods Purchased.**

A buyer initiates a purchase of goods from a supplier and notifies the supplier of their intent to establish trade finance terms. In some circumstances, the supplier may look to establish terms.

**2. Gather Documentation.**

Each party in the arrangement must review the other party's financials to determine if they are an acceptable credit risk.

**3. Risk / Credit Analysis & KYC.**

If each party is in good financial standing, then all standard KYC and credit documentation must be completed. This includes the drafting of a letter of credit.

**4. Negotiations.**

The buyer and supplier, as well as the banks of each party, are involved in negotiating the trade finance terms and have a chance to review and make adjustments before a final agreement is established.

**5. Trade Execution.**

Once both parties are satisfied with the terms of the agreement, goods are shipped and funds may be provided to the supplier early and at a discount.

**6. Monitor & Manage.**

Because goods are purchased on credit, both the buyer and supplier must monitor the relationship to ensure the other party delivers on their obligations.

# Trade Finance: Who Wants What?



## Bank & Corporate Needs in a Trade Finance Arrangement

- Each party in a trade finance arrangement has a unique set of objectives and goals
- Chiefly, bank (lender) and corporate (borrower) participants must align their needs before terms can be agreed upon.

### Corporate Borrowers

- Line of Credit – Extended Payment Terms
- Letter of Credit & Supporting Documentation
- Solution for Managing Activity & Visibility
- Timely & Regular Communication and Feedback

### Lenders (Banks)

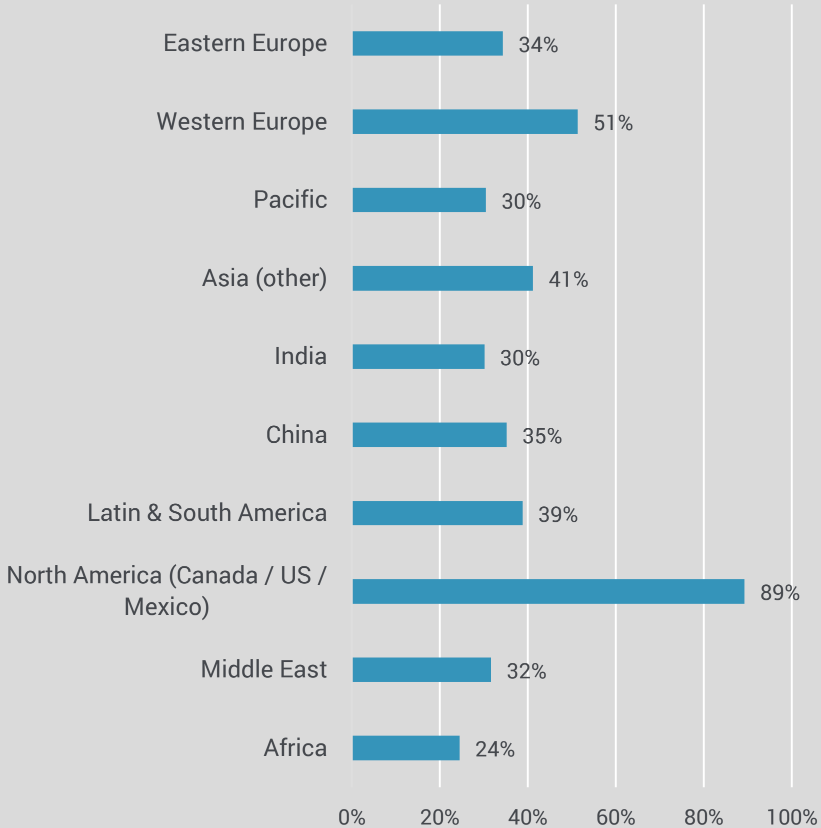
- Streamlined documentation
- Low Risk
- Interest Earned
- Market/Margin Growth

# Trade Finance Today: Globalization



## Regions Operating In

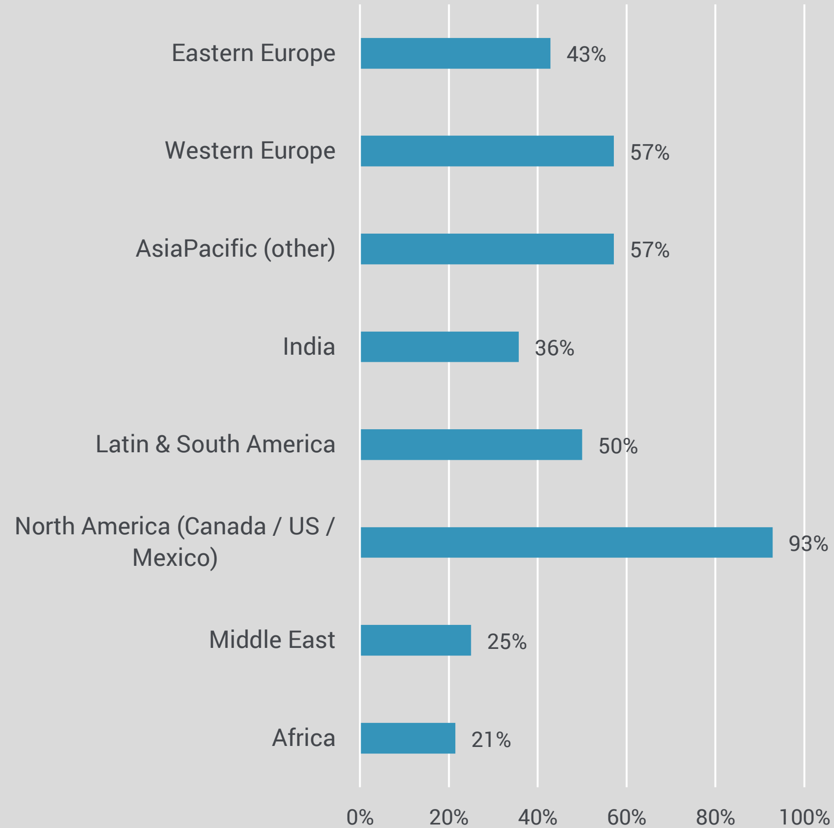
Which regions does your company operate in? (Select all that apply)




*2017 Strategic Treasurer, Bottomline Technologies, & Bank of America Merrill Lynch B2B Payments & WCM Strategies Survey*

## Supplier Locations

Buyers: In what regions are your suppliers located? (Select all that apply)




*2017 Strategic Treasurer Supply Chain Finance Survey*

## Obstacles to Trade Finance

### Globalization

- Globalization can result in a complex spread of bank relationships and supplier networks.

### Regulation & Compliance

- Regulations can differ by region
- Business practices vary by region
- North America compared to China

### Digitization

- Process Automation
- System Integration
- Decentralization of Information

### Risk & Financing

- Risk Analysis
- KYC & AML Documentation
- Terms negotiation, covenant compliance, etc.

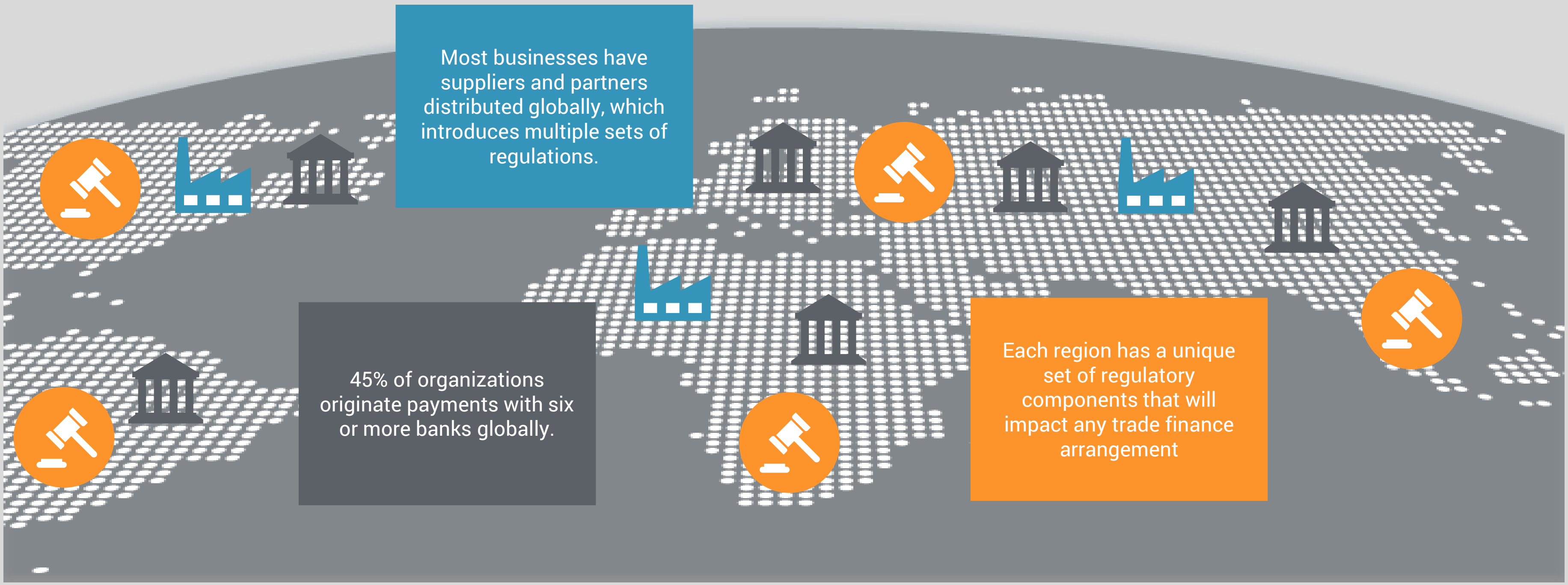
- While there are an array of challenges associated with trade finance, additional complexities are added to the mix due to:
  - Legacy technology (both bank and corporate)
  - Inefficient documentation processes
  - A confusing regulatory and compliance landscape
  - Difficulties with determining risk profiles and establishing payment terms

# Trade Finance Challenge: Regulation & Compliance



## Regulatory Landscape

- The compliance landscape of today involves multiple regulatory bodies that shift across regional and jurisdictional lines.
- Some regulations may be industry or region-specific, while others are global in scope.
- Any cross-border trade finance arrangement may be subject to one or more of these regulations, and differences in regional practices can cause confusion when structuring payment terms, accounting treatment, etc.



# Trade Finance Challenge: Risk & Financing



**Documentation Required**
Banks must perform due diligence on any new customer or party that they perform business with, for each area of service.

**Risk Analysis.** One of the first steps for a bank is determining whether a firm fits into their risk profile for lending/financial services.

**Financial Scrutiny.** Banks take a close look at the financials of the company, location, and other factors to determine risk involved.

**Sanctions Screening.** Banks also run queries on staff and other partners of the business to ensure there are no known criminals/sanctioned parties.

**37 Days**

**Client Approved.** If a firm passes all these checks, the bank can begin servicing the client.

## Bank Documentation & KYC Requirements

**Primary Responsibility:** Banks shoulder the majority of KYC and documentation responsibilities, due to heightened regulatory pressure and requirements.

**Added Steps:** This responsibility means that banks must gather more background information and documentation from clients up-front, and often must request information regarding the clients of their clients (KYCC).

**Issues Compounded:** Added costs for time spent verifying details, delays to business operations, ensuring compliance, etc. is often compounded due to inflexible or legacy technology that cannot handle frequently changing regulatory requirements/updates.

**Significant Delays:** it takes ~37 days for retail banks to complete KYC documentation for a corporate client.*

*Stratum

# Trade Finance Challenge: Digitization



**Corporates Need Access.** Corporates regularly need access to bank details (statements, limits, transaction activity, documentation, etc.).

**Connectivity is Key.** The ability for bank solutions to integrate with corporate technology has become a major component and expectation for commercial banking services.

**Legacy & Outdated Tech**

**APIs & Open Architecture**

## Bank Interfaces in the Spotlight

### Outdated & Insufficient

Despite leading corporates in most areas of development, some banks lag behind their clients when it comes to having a flexible, open architecture.

### PSD2 & the Era of "Open Banking".

With the introduction of PSD2 in Europe, the use of APIs are looking to play an immense role in linking bank systems with outside parties and other Fintech providers to provide streamlined automation, integration, and STP.

### APIs Grab Corporate Treasury's Focus.

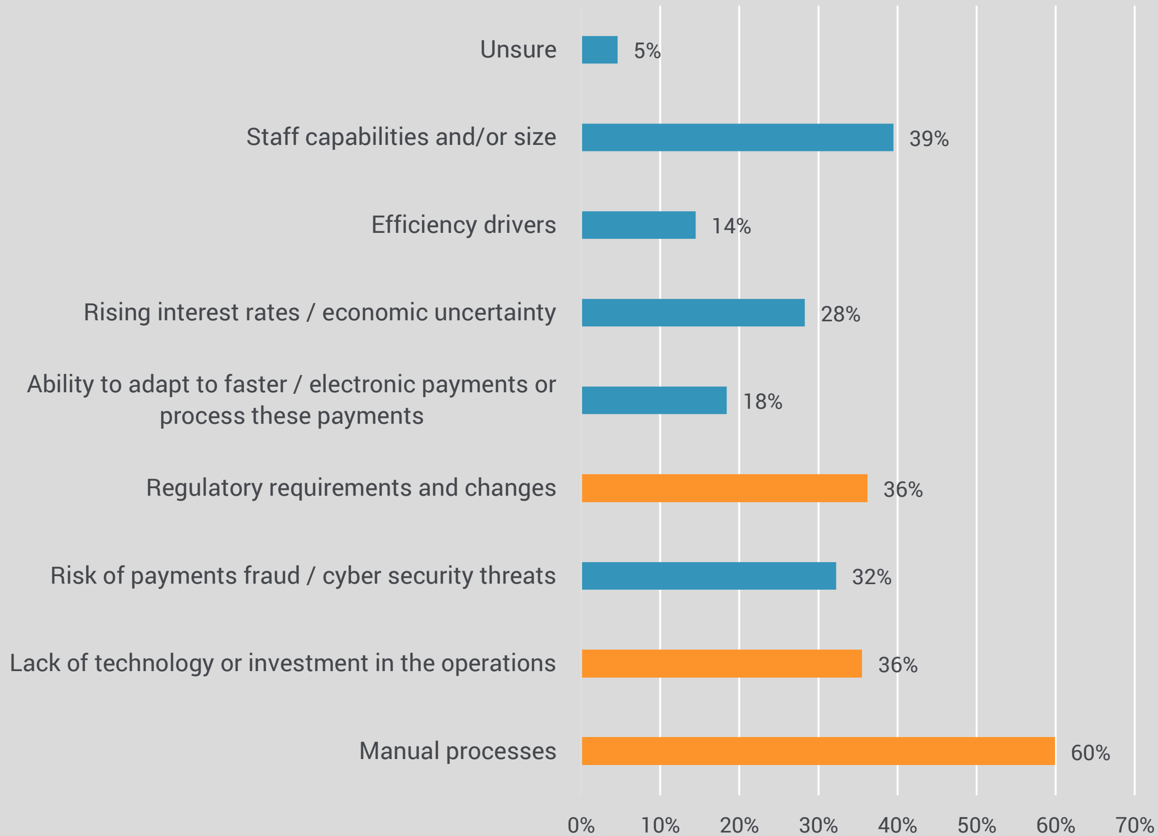
Over 4x as many respondents to a recent survey saw APIs as more important than blockchain for payments over the next 1-3 years.

# Need for Digitalization

## Rising Above Manual Labor

- Corporates regularly indicate that manual processes and lack of automation are a large obstacle
- Regarding trade finance, corporates commonly rely on their bank to manage documentation & provide credit.
- They also use bank's system, or partially rely on bank system, to monitor activity.
- Strength of the platform is just as important as the extension of credit.

## What areas represent the top operational challenges for your organization in 2018? (Select all that apply)




*2018 Strategic Treasurer & TD Bank Treasury Perspectives Survey*

# Digitalizing Trade Finance: Banks & Fintechs



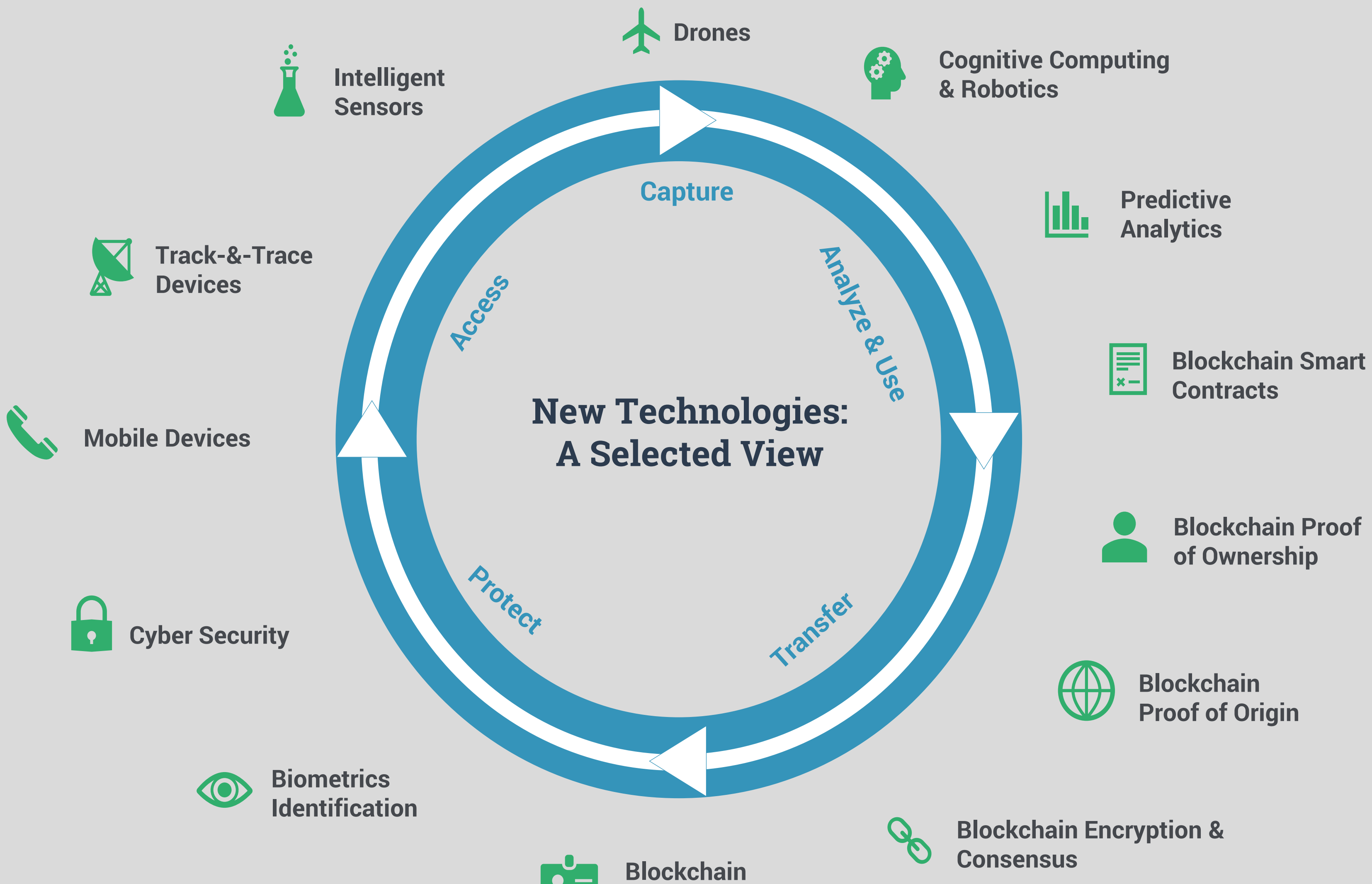
## Banks and Fintechs Vie for the Space

- In recent years, the innovation introduced by Fintech providers of trade and supply chain finance has led to a growing demand for Fintech (non-bank) services and solutions to facilitate such arrangements.
- There are pros and cons for both banks and fintechs from this standpoint.

| Banks | Fintech Providers |
|---|---|
| ✓ Large amounts of available capital | × Lack significant capital reserves in many cases |
| ✓ Plentiful cross-sell opportunities for existing clients | × Lack any large pool of existing clients in many cases |
| × Lack flexibility and scalability with their tech infrastructure | ✓ Highly flexible and configurable technology options. |
| × Subject to complex documentation requirements | ✓ Add-on functionality such as e-invoicing provides further value-add and opportunities for cost-savings. |
| | ✓ Fully automated process, end-to-end |

# The Future of Digital Trade Finance






*Source: Misys World Trade Symposium Exec Summary*

# Trade Finance as a Service

## Fintech Innovations in Trade Finance Services

| | | | | | |
|---|---|---|---|---|---|
| **Use Case** | • Ability to screen documents for consistency and compliance (NLP) | • Ability to analyse patterns, trends and changes in the trade landscape | • Ability to guarantee the provenance of goods (track & trace / smart contracts | • Ability to distribute trade risk to third party investors in capital markets | • Ability to connect with the<br>• e-commerce ecosystem |
| **Business Benefit** | • Reduced cost / reduced risk | • Intelligent insights into risk mitigation | • Ability to support ethical finance | • Ability to re-risk and optimise lifecycle management | • Increased speed / increased efficiency |

API

**Open APIs**

| | | | | | |
|---|---|---|---|---|---|
| LETTERS OF CREDIT | COLLECTIONS | GUARANTEES | PAYABLES FINANCE | INVOICE DISCOUNTING | PO FINANCE |

**Trade / SCF Back Office**

# Advantages of Digitalization



## Legacy Applications Approaching End of Lifecycle

| Legacy Architectures | Target Architecture |
|---|---|
| ❑ Monolithic & Siloed | ❑ Open APIs |
| ❑ Lack of Interoperability | ❑ Micro Services |
| ❑ Lack of Client Centricity | ❑ Rapid Deployment Model |
| ❑ Lack of Operational Excellence | ❑ Agility & Resilience |
| ❑ High Maintenance Costs | ❑ Process Automation |
| | ❑ Reduced TCO |
| | ❑ Value Efficiency |
| | ❑ Customer Centricity |
| | ❑ Interoperability |
| | ❑ Reduced Turnaround Times |
| | ❑ Scalability |
| | ❑ Digitised Data Consumption |
| | ❑ Predictive Analytics |

# Digitized Trade Finance: Corporate Value Proposition



| | Exporter | Importer |
|---|---|---|
| **Shorter Working Capital Cycle**<br>▪ Reduced time for documents in transit, improved turnaround on pmts. | ✓ | |
| **Increased Protection Against Fraud**<br>▪ Electronic docs can only be produced by registered parties in the platform<br>▪ All endorsements/transfers are tracked through the system registry | ✓ | ✓ |
| **Reduced transaction costs**<br>▪ Elimination of courier costs in case of a full ePresentations<br>▪ Avoids document transit delays and associated costs<br>▪ Reduced demurrage costs as documents arrive before shipment | ✓ | ✓ |
| **Enhanced Operational Efficiency**<br>▪ Significant time reduction when amending eDocs, such as splitting, switching, etc.<br>▪ Risk of documents being lost in transit is eliminated<br>▪ Increased visibility over shipments | ✓ | ✓ |
| **Improved Risk Management**<br>▪ The use of Letters of Indemnity (LoI) is eliminated, which reduces counterparty risk for recipients<br>▪ Security Provision – Insurance available per shipment | | ✓ |

# Final Thoughts



## Key Considerations for Corporates

### Examine your technology infrastructure and that of your bank

How does your internal technology infrastructure interact and integrate with bank and external solutions?

### Identify the largest inefficiencies

Are there any major compatibility issues? Are manual workarounds necessary for any workflows? Are there clear opportunities to streamline these processes?

### Meet with your banks to discuss the results

If there are opportunities to streamline or gain efficiencies in the process, meet with your banks to discuss what this would look like. With PSD2 on the horizon, it could be that banks are already working on upgrading their platforms to fix these issues.

## Key Considerations for Banks

### Don’t Underestimate the Importance of Technology

A growing number of corporates are basing their bank relationships off the strength of their financial and payment solutions and services, and are not just focusing on the relationship itself or on traditional lines of credit.

### The go-to source for all things treasury

Corporates have indicated that they rely on their banks for guidance and advice in a broad number of areas, including technology. Given the trajectory that financial technology is taking, banks need to ensure the state of their technology matches the pace of development in the industry.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