Digitising trade finance – a work in progress

The trade arena is increasingly warming to digitisation, yet a number of barriers to adoption persist. Mauro Bonacina examines the current state of play and how banks and fintech companies together can drive real progression in the trade finance landscape

Technology is driving change within trade finance. While this change is not occurring with the same velocity as that in some areas of the financial industry, substantial advancements have been made during the past decade (take Bolero, for example).

Furthermore, the rate of progress could be set to gain momentum. This is because new capabilities are allowing the sector to evolve not just in terms of solutions and practices but also in terms of mindset.

The trade sector's traditional approach and values can result in a reluctance to alter embedded processes; meaning it is often slow to embrace new concepts. Yet the rapid pace at which technology innovations are being developed is, to a degree, desensitising the industry and allowing it to become more used to change. Subsequently, developments are being increasingly welcomed, with all parties in the supply chain accepting and agreeing that digitisation is not only needed but desirable.

Certainly, demand is growing for solutions that offer streamlined processes, enhanced processing speed and efficiency, and reduced working capital costs. Fuelled by technology that enables real-time access to data, improved transparency of information and flows, and document traceability, the value of 'going digital' and automating the supply chain is increasingly being realised.

A challenging environment: the complexity of trade

While members of the supply chain may be warming to digitisation, there are a number of other hurdles to overcome before real progressive change can take place.

It can be easy to become frustrated at the slower rate of change in the trade finance space than, say, the payments space, but it must be remembered that trade is far more involved and complex. The entire payments process is very often entirely paperless, with many of today's transactions now initiated via portable, electronic devices. Trade, however, requires an exchange of documents (physical or otherwise) – as opposed to simply an exchange of data.

Despite moves to encourage dematerialisation of the trade process, there are still many port authorities that strictly stipulate the requirement for original bills of lading (b/ls), for example – without which goods cannot clear customs. Therefore, for steps to be taken towards trade becoming an effective digital industry, a universal set of standards is required, with all port authorities approving digital shipping documentation. Unfortunately, there is still a way to go before such harmonisation is established.

Certainly, the industry is not making things easy – for instance, more than 400 different formats and providers of e-invoices currently exist in Europe alone. There are also concerns regarding the potential for digitisation to increase the risk of fraud. While fraud risk will be reduced due to less manual intervention, it is feared that it could create the opportunity for new 'techno-fraudsters' to enter the arena to, for example, electronically forge documents, change beneficiary names and duplicate b/ls for double negotiations. In order to overcome such threats, a constant process of enhancing security and encryption will be required.

A further barrier to digital growth is the significant level of investment needed. A huge portion of the trade business worldwide is originated by micro businesses or SMEs, many of which, understandably, are not financially positioned (or sufficiently tech-savvy) to commit to substantial, costly revamps.

Without doubt, the trade environment can be challenging in terms of progression, and a number of barriers to digitisation persist. Even new tools launched by key industry figure SWIFT have received a lacklustre reception. Adoption of the bank payment obligation (BPO) solution, based on the proprietary Trade Services Utility (TSU), has been extremely slow so far due to the aforementioned reasons – as well as other factors affecting its growth.

The potential of OCR

Digital progress is yet to build significant momentum in the trade arena, with products that have been introduced so far addressing 'niche' opportunities, rather than being significant game changers. But a key development bearing enormous potential to disrupt the trade business is optical character recognition (OCR) – the electronic conversion of images of typed, handwritten or printed text into machine-encoded text. OCR enables scanned documents to become electronically readable, allowing them to be examined by dedicated software, with very limited manual intervention – the trade equivalent of straight-through processing for payments. The adoption of this solution in the processing segment would play a pivotal role in the advancement of document processing.

While such capabilities are technically already available, OCR is not yet reliable enough to become mainstream; there are too many variables and the error margin is still too high. Indeed, it is one thing to acquire the (usable) phone number and an email address from a scanned business card, but another altogether to check for compliance of documents presented against a letter of credit (LC). Therefore, further development of the product is ongoing. But it is expected that once these issues have been addressed, OCR will become a widely adopted trade processing method.

Driving digitisation through collaboration

Banks have a huge role to play in advancing the trade industry into the digital era, and must be committed to investing in the future of trade processing and facilitating the growth and development of the world's trading opportunities; positioning clients with the tools they need to flourish in this transforming space.

That is why many banks, rather than investing in new platforms and training staff for products that end-clients are not demanding (for example, solutions such as BPO), are focusing on engaging with fintech companies to leverage the benefits arising from the digital space. Through these relationships, banks are not merely offering investment to help bring concepts to fruition, but are providing invaluable guidance regarding how creative ideas could be developed into viable real-world applications; a vital requirement if new digital solutions are to successfully penetrate the industry.

When it comes to the digitisation of trade finance, the blockchain is creating by far the most noise, as it could hold the key to transforming the entire industry. Certainly, its distributed ledger concept could significantly enhance settlement and reconciliation; offering full, immediate visibility of all entries, and transparency of the whole process. BNY Mellon has established a number of innovation centres across the globe, collaborating with professionals and clients to explore the possibilities and be positioned to adopt a clear blockchain strategy if and when the time comes. Whether blockchain will become best practice or a missed opportunity remains to be seen, but one thing is clear: until regulators officially buy in to the blockchain and facilitate its adoption, it is likely to remain little more than hype.

In the meantime, collaboration is paramount for progressing trade and encouraging dematerialisation; local–global bank collaboration as well as bank–fintech collaboration. Indeed, in this technology-fuelled era, investment into sophisticated platforms and capabilities can be a challenge beyond the reach of many local banks, and local–global bank partnerships can be an ideal solution. Such non-compete relationships enable local banks to benefit from enhanced product offerings without committing to substantial investment, while knowledge and experience can be shared to help both parties add significant value to client service and the overall transaction experience.

Digitisation of the supply chain is an ongoing process, but the migration from paper to paperless is well underway, and the potential to transform even perhaps the most change-averse industry in finance is very much there to see. It is through reciprocal, supportive partnerships that real progress can be made – leveraging opportunities that technology can unleash and enabling clients to grasp the future of trade with both hands.

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