TXF GLOBAL TRADE REPORT 2021

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Global trade system comes under greater scrutiny

With widespread disruptions in the trade supply chain and a growing trade finance gap, particularly impacting smaller businesses, a recently released report calls for systemic modernisation of global trade finance and lays down a roadmap for radical change.

The call to improve procedures within the global trade system, and in particular the financing mechanisms that are the engine of that, have been steadily ramped up for many years now. The global financial crisis of 2007-2008 was a harsh wake-up call, and now coming up to two years of the Covid-19 pandemic and the major disruptions that has had to global supply chains, there is intense scrutiny being placed on how the trade finance system can be fundamentally improved.

It is not as though nothing has been done this century to improve and modernise the system – plenty has. But it is blatantly obvious it is not enough. And advances in standardisation, transparency and digitalisation etc so far have not been fast enough to keep up with the growth in global trade and the technological advances available to help in the push for the greater efficiencies needed.

With continued sluggish and inefficient systems, the financing of global trade suffers. For years now we have talked about the global trade finance gap – where companies trying to access finance are unable to do so. That gap is simply getting bigger, and it is predominantly micro, small and medium-sized enterprises (MSMEs) that are losing out (see below).

The scrutiny that has been directed at the global trade system has led the International Chamber of Commerce (ICC) and the World Trade Organisation (WTO) to call on governments, development banks and multilateral banks to act. At the same time there is now real impetus with certain initiatives being put forward by these bodies. In addition, a recent research report suggests a fundamental overhaul of global trade finance.

Released by McKinsey, the ICC and Fung Business Intelligence in November, a 57-page report entitled: 'Reconceiving the global trade finance ecosystem' explores a way to reshape and modernise trade to make it not only more accessible to help smaller businesses, but also more sustainable in a variety of ways.

There is no question this is a landmark report, and that it will be discussed, considered and hopefully some of the measures ultimately taken up. I urge you to read the report. One thing that I continue to find odd though is how the use of the word 'ecosystem' has gradually crept into 'trade talk'. I've heard it numerous times at conferences and obviously seen it in print too – but I still find its use weird! For me, ecosystem means a biological community of interacting organisms and their physical environment. Now, it also has the meaning of 'a complex network or interconnected system'. Fair enough, but I won't be using it!

Trade finance gap grows

Up until last year many reports on the global trade finance gap had quoted the figure of $1.5 trillion as the size of the global trade finance gap – a figure which had been released by the Asian Development Bank (ADB) in relation to its Trade Finance Gaps, Growth, and Jobs Survey of 2018. The gap represents the difference between requests and approvals for financing to support imports and exports. In October 2021, the ADB revised this figure to $1.7 trillion for 2020, following its latest survey.

ADB trade and supply chain finance head Steven Beck, commented: "To close the gap, we need to bring trade fully into the digital world through greater coordination with the private sector as well as global agreement on common standards, practices, and legislation."

In a statement released by the WTO and ICC in July 2020 (also in a letter to the G20) it noted the following: "Trade finance is a critical element in re-igniting worldwide growth in imports and exports. Since the need for trade finance is estimated to be between $2 trillion and $5 trillion, meeting this demand and addressing the shortfall will be challenging. There is serious concern that the growing gap between demand and supply will particularly affect MSMEs and businesses in developing countries, with important implications for jobs and incomes."

WTO and ICC urged the private and public sectors to work together to bring about a rapid transition to paperless trading, including e-documents in the processing of trade finance transactions. In addition, the statement called for an exchange of views on how regulatory authorities can help ease constraints on the provision of trade finance. It also proposed increased risk sharing to support trade finance and the extension of development bank schemes to provide risk mitigation.

The report - 'Reconceiving the global trade finance ecosystem'

The McKinsey, ICC, Fung Business Intelligence report is based on a year-long effort by the ICC's advisory group on trade finance to raise awareness and address the challenges facing MSMEs, particularly in the emerging markets, in accessing the trade finance needed to support their growth and the global recovery. It is based on over 150 interviews with end-users and subject matter experts in 12 countries, and an ideation and review process covering leaders from trade, finance and technology.

According to McKinsey's Global Banking Pools, the global trade finance market covered a value of approximately $5.2 trillion in 2020, amounting to roughly 6% of global GDP. Of this $5.2 trillion, 55% is throughout Asia-Pacific, 30% EMEA and 15% Americas.

It ought to be noted here that in 2020 global merchandise trade volume stood at $17.5 trillion, down from $19 trillion in 2019, which was itself down 3% on 2018. It is generally accepted that approximately 80%-90% of global trade requires financing of one form or another. The bulk of global trade is financed on 'open account' financing terms.

Broadly, the scope of trade finance considered for the purpose of the report covered three types of products. First, documentary business including traditional on- and off-balance-sheet trade finance instruments. Documentary business accounts for roughly 85% of total trade finance volume the report notes. Second, buyer-led finance eg reverse factoring, and third, supplier-side finance eg factoring, forfaiting.

Within its introduction, the report stated: "Against a backdrop of increasing digitisation of financial and commercial services, trade finance has been relatively slow to modernise its decades-old processes. Multinational corporations have begun to leverage digital technologies that promise improved supply-chain efficiency and transparency, establishing new digital networks to facilitate trade and finance. But MSMEs, with their fragmented nature and limited scale, find it difficult to capitalise on such opportunities.

"Resolving this issue is critical for all participants in the global trade finance system. An improved global trade finance ecosystem could add many of the 600 million new jobs needed by 2030 to absorb the growing global workforce, as well as enable progress toward the goal of financial inclusion, which is particularly needed in developing economies."

The report also stated that technological innovations to date within trade finance had led to 'digital islands' or closed systems of trading partners which unintentionally could create longer-term disconnects. It suggested bridging these islands with an 'interoperability layer', enabling "ubiquitous access across networks and platforms".

This interoperability layer would have a three-part mission. First, to promote adoption at scale of existing trade finance standards for operational interaction. Second, to design and disseminate additional global trade finance standards and protocols to fill market gaps. And third, to develop blue books and identify guiding principles for improved collaboration among trade finance participants.

In a subsequent article by the report authors, it noted: "The interoperability layer would be a virtual construct that acts as an umbrella for existing and future standards, protocols, and guiding principles. To be clear, it is not a proposal for regulatory change, nor is it intended to be a hardware or software entity to which parties must connect. It would be a collaborative effort involving relevant organisations in the trade finance market. It would give all parties - particularly underrepresented segments like MSMEs and businesses in emerging markets - a fair opportunity to participate. The goal is an architecture of common standards and best practices enabling trade finance to become more inclusive, collaborative, and digitised."

The report lists a number of benefits of a revamped system for a range of players including: buyers and suppliers (who would see the greatest benefits, particularly with increased access to liquidity); logistics providers; financial institutions; trade organisations; technology providers; and, governments and regulators.

For financial institutions, some of the benefits are: "A full deployment of the interoperability layer would bring a substantial structural change to the financial industry as a whole, specifically benefiting existing providers (primarily banks) while also attracting much-needed new credit capacity to the industry (from entities such as institutional investors), drawn by added transparency, access to technology, and regulatory support. In addition, the ecosystem could bring additional revenue streams and value-added services while making the processes more efficient and cost effective."

The road map

The report stresses that the realisation of an interoperability layer would only be possible with the coordination and commitment of the broad community of trade finance participants. It noted: "Given the complexity of the market, this effort may require five to ten years to reach a level at which most participants will realise its full benefit. However, some of an interoperability layer's building blocks could be deployed on an accelerated path, leveraging work that has already been done by trade organisations."

This plan is structured over three phases. The first phase is over 12-18 months. This involves: mobilising the existing trade finance ecosystem. — Establishing a governance model for the interoperability layer. — Launching a detailed action plan to accelerate adoption of standards for digital trade enablement. — Finalising critical missing elements for trade finance interoperability foundations. — Building a road map to drive adoption of the key standard.

The second phase is over two to three years. This involves: Developing the reconceived ecosystem and starting scaling up adoption. — Finalising missing elements of the interoperability layer (eg, blue books, best practices). — Promotion of a broader adoption of the chosen standards applying a supply-side approach (starting with banks).

The third phase is over five to ten years. This involves: Scaling up global efforts, with solutions addressing the needs of all market participants. — Supporting development of shared utilities, based on blue books and standards. — Scaling up global adoption of the reconceived ecosystem by both the supply and demand sides.

In concluding, the report stresses the real need for all-party coordination and commitment: "The overarching goal of the proposal described in this report is to build on the collaboration already gaining momentum among participants in the trade ecosystem, to cover gaps in existing operating models, and, most importantly, to promote the wider adoption through further coordination. If cooperation and execution throughout the global trade finance community can be inspired, the joint objective - and an equitable distribution of benefits - are well within reach."

Taking ideas forward

The report is undoubtedly a document which is trying to drive the trade finance community to pull together to bring the range of trade financing products and services properly into the 21st century in an organised way for all. As it states, much has already been done. However, refinement of all these qualities and organisation will require considerable attention over a good period of time. And, where there is a will, there is always a way.

Inevitably, not everybody has been entirely impressed with the report however, one senior executive within a US-based capital market fund which invests in trade finance assets, observes: "I was impressed by the density of meaningless buzzwords." Possibly a bit harsh, but at times I could certainly see where he was coming from.

Expanding beyond this, the executive explains: "Within the report there seemed to be no recognition of the fact that banks have a finite amount of capital available for trade finance." Here, the executive seems to have a point

And specifically on the issue of non-bank investors in trade, coming more into trade finance to help fill some of the gap, he complains: "I detected little or no mention of the potential for financial investors to help fill the gap."

There is in fact a small section on institutional investors in the report, which skirts around involvement, but never properly looks at the growing involvement of private credit investors within trade finance, and the greater potential of such activity. The report noted: "institutional investors to date have not embraced at-scale trade finance as an investable asset. Indeed, the trade finance market tends to be illiquid and non-transparent for reasons including technology limitations - resulting in the lack of a transparent electronic market - and limited risk assessment expertise among institutional investors."

A comprehensive review of private credit within trade finance can of course be found in the recent report published by TXF: 'Private Credit & the Trade Finance Opportunity'.

Another market practitioner, Christoph Gugelmann, CEO of Tradeteq, a technology provider which set up the Trade Finance Distribution Initiative to drive standardisation for the distribution of trade finance assets had these insights to say about the McKin-

sey/ICC/Fung report: "The McKinsey/ICC report pulls out a number of key issues with global trade: supply chain issues creating fragility, the insurmountable barriers for SMEs attempting to access funding and lack of interoperability. At the heart of each of these problems is legacy infrastructure and the reliance on paper-processes such as faxes and spreadsheets which are slow and have no transparency or standardisation."

And in considering ways to improve the global trade system, Gugelmann remarked: "In my view, the way to reboot this $5 trillion [financing] engine that powers global trade is to adopt and utilise new technology and incorporate modern infrastructure which enables more automation, less friction and reduced costs. The technology and infrastructure needed to parcel trade finance instruments into investable assets which helps solve the trade finance gap already exist.

"Modern AI [artificial intelligence] tools can give firms early warning signs of supply chain issues before they're directly affected. These solutions have come about through banks, fintechs and investors working together and using innovative technology, and this is the formula required to truly revolutionise this centuries-old industry."

Sound words. We look forward to further developments and concerted progress on the restructuring of the global trade finance system.

Trade developments through the COVID-19 crisis

Marc Auboin, counsellor, economic research at WTO takes a step back and reflects on the impact of the pandemic on trade, and how the impact of the recovery is not uniform.

Marc Aubion

The outbreak of the COVID-19 pandemic affected the world economy through a combination of supply and demand shocks, affecting all parameters of the economy – output, investment, consumption, and trade. While in the first part of 2020 strict lockdowns led to factory closures and major disruptions in supply chains, consumption and investment patterns have also been affected by the succession of epidemic waves.

The trade impact of the recession was very strong in the first half of 2020 for both goods and services, but the recovery of merchandise trade started relatively early in the second half of 2020, with quarter-toquarter growth rates even stronger than GDP. Overall, good trade dropped by 5.3% in 2020, against a contraction of real GDP of 3.6%.

This is to be compared to a much larger drop of goods trade in 2009 (-12%), at the height of the global financial crisis, relative to GDP (-2%). Many observers highlighted the resilience of global supply chains, which quickly responded to rising demand for essential goods during and after lockdowns (personal protective equipment, food), despite all the obstacles and uncertainties encountered by producers and traders in the process of producing and shipping goods across-borders (disruptions of supply routes, modes of transportation, documentation, limitations in the supply of services which rely on the presence of individuals abroad, etc). In certain sectors, supply bottlenecks and transport disruption continue.

World merchandise trade volume and real GDP growth, 2014-2020

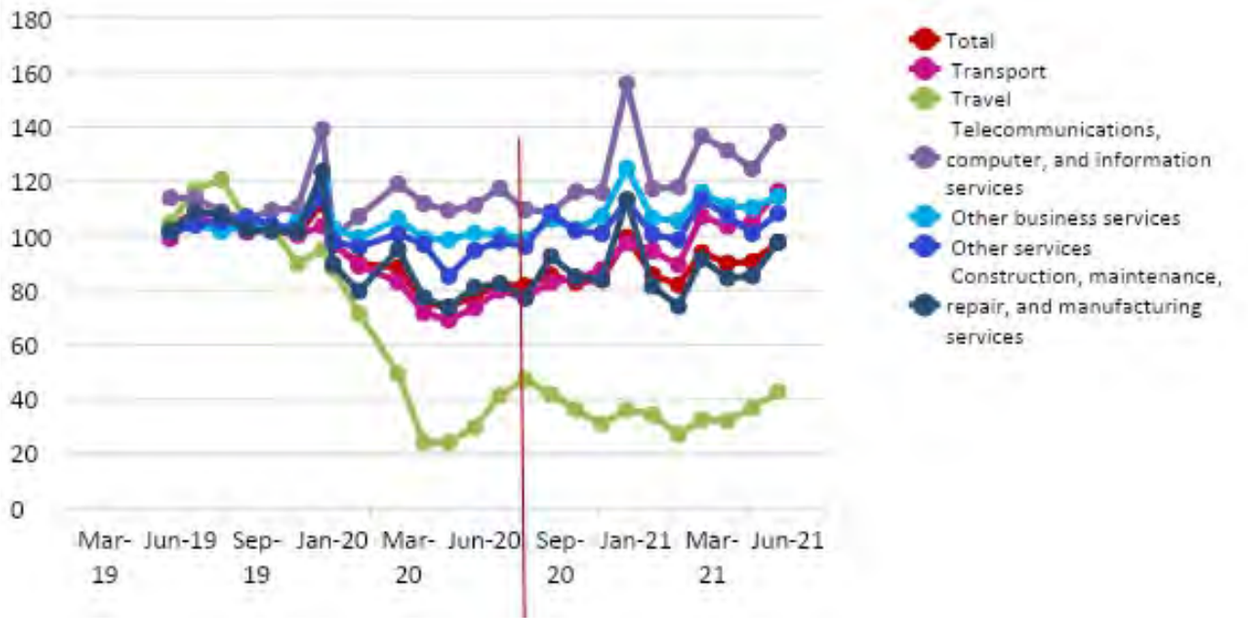
The crisis recovery has not been uniform, though. While trade volumes are expected to pick-up globally by 8% in 2021, the strength of the recovery depends on the size of the available fiscal stimulus, access to vaccination (hence the reopening of economic activity), specialization of countries, pre-existing trade linkages to those countries with fewer COVID-19 cases, and degree of digitization of trade.

Trade is certainly at the heart of economic recovery in many countries by providing sustained foreign demand for exports and ensuring the availability of imported intermediate products and services for those reopening gradually. However, trade and economic recovery has been lagging in less globally integrated regions (Latin America, South Asia, Sub-Sahara Africa), with goods imports in these regions still below their 2019 peak levels in the first quarter of 2021.

Services trade is, at last, showing signs of recovery, but it continues to be disproportionately impacted by COVID-19, in particular travel. In 2020, global services trade was substantially lower (some 20%) overall than in 2019 due to the pandemic. Travel was the type of service most negatively affected, but other services requiring the movement of persons or face-to-face interactions (such as business services) were affected too. Increases in information and communication technology services can be explained by more activities being conducted remotely over the internet due to social distancing measures and the closure of borders implemented during the pandemic. As of June 2021, though, global services exports had yet to recover to their pre-pandemic levels (see chart).

World services trade

Source: Estimates based on WTO and UNCTAD data



Certain categories of traders had been, and are still, facing notable challenges during this pandemic. This is the case for small-scale cross-border traders, a majority of whom are women. They often rely on ease of cross-border movement and on gathering at local marketplaces where maintaining social distance is difficult.

While immediate national health policies have focused on limiting the health and human costs of COVID-19, small-scale traders have been forced to make fundamental changes and adapt their business and market behaviour to the new environment of the global pandemic. The most direct impacts have resulted from the closing of border crossings for pedestrian traffic, as well as the closure of border markets. These impacts have had adverse consequences for regional trade, the income of the small-scale trader population and the generally low-income consumers they serve.

Diverging recovery

The picture of a diverging recovery may well fit trade finance markets as well, although the existence of partial data on trade finance makes it difficult to properly compare trade and trade finance developments. Financial institutions which are specialized in mitigating cross-border trade finance risks, such as banks, export credit agencies (ECAs) and multilateral development banks (MDBs), have had a challenging 18 months in responding to demands from their customers, with, in some cases and countries, support being vital to keeping the channels of trade open at the height of the pandemic.

At the height of the pandemic it was quickly realized that one-off extensions of the terms of payments by creditors would be insufficient to deal with a much longer period of strain, and that anticipated payment difficulties and failures would go beyond the sectors initially impacted by the pandemic (airlines, aeronautics, tourism etc). With extra liquidity provided by the authorities and healthier balance sheets than during the global financial crisis, banks have been able to support core customers (importers and exporters) in the main markets.

Many developing countries, though, faced deteriorating sovereign and private credit risk, translating into a reduced access to trade confirmation lines available from international banks and shortfalls in foreign exchange liquidity. [See in particular: African Export Import Bank (Afreximbank) and the United Nations Economic Commission for Africa (UNECA) (2021), Survey of the Impact of COVID-19 on African Trade Finance; and IFC's Bank Surveys.]

In order to avoid the 'scissors' effect of recovering demand and hesitant supply of funding related to an increased risk aversion, governments, ECAs and international financial institutions, including MDBs, have provided support to trade finance markets. MDBs have provided record amounts of trade finance guarantees and liquidity in developing countries, in particular the poorest, while governments implemented payment deferral schemes, in addition to directing domestic lending support to corporates. Large central banks have supplied foreign exchange resources to other central banks through swap agreements.

Overall, the situation seemed to have eased globally, but the demand for MDBs' facilities remains very high in countries in which deteriorated sovereign and other risk have had a significant knock-on effect on their ability to secure private credit and confirmation lines.

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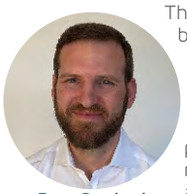
Narrowing the trade finance gap with Trade-Finance-as-a-Service

While trade finance has an essential role to play in supporting the global economy through the post-COVID recovery, many firms are still unable to access the finance they need. Fortunately, technology can help banks meet their customers' trade finance needs – and with cloud-based solutions, the cost of a specialist system is no longer prohibitive for small and mid-sized banks, as Surecomp's Enno-Burghard Weitzel and Andrew Coles explain.



Enno-Burghard Weitzel

The last 18 months have brought exceptional challenges – and when it comes to supporting companies and economies through the post-COVID-19 recovery, trade finance has a vital role to play. But while demand for trade finance continues to outweigh availability by a considerable margin, high transaction costs mean it is simply not viable for many smaller banks to provide customers with the trade finance they need. So why is trade finance technology so critical when it comes to narrowing the trade finance gap? And how can cloud-based solutions help small and mid-sized banks support their customers more effectively?

Trade finance and recovery

The impact of the pandemic on global trade has been substantial. Travel restrictions, factory shutdowns and lockdowns had a major impact on the supply of goods and services, with global trade falling by 8.9% in 2020. At the same time, shipping costs have increased significantly since the beginning of the pandemic – and a plethora of other issues, ranging from shortages of semiconductors and shipping containers to the infamous grounding of the Ever Given in the Suez Canal, have brought further disruption. While challenges remain, this year has brought something of a recovery: trade volumes reached a record high in the first quarter of 2021, while Moody's has predicted that global trade will grow by 7-9% in 2021. And with trade volumes bouncing back – albeit tentatively – trade finance is seen as a vital tool for supporting economic growth. In reality, however, not every company that needs trade finance is able to access it.

Before the pandemic, a report by the Asian Development Bank estimated the global trade finance gap to be $1.5 trillion, with small and medium sized enterprises (SMEs) particularly struggling to access trade finance. According to the report, 45% of trade finance applications by SMEs were rejected, compared to 17% for multinational corporations. Even without knowledge of the impending pandemic, 60% of responding banks said they expected the trade finance gap to increase in the following two years.

Many different measures have been adopted to address this shortfall, including regulatory reform, policies and technical initiatives. But while the global trade landscape may be complex, one of the major reasons for the trade finance gap is simple: in some cases, the cost of a trade finance transaction is larger than the value of the transaction itself. As a result, most of the world's trade finance is provided by a small number of banks that have been able to achieve economies of scale and reduce their processing costs by harnessing technology. Smaller banks, in contrast, have struggled to achieve profitability in this area.

Falling behind

Andrew Coles

As we move through the crisis and beyond, it's clear that trade finance has an important role to play in supporting economic recovery – and in order to close up the gap, banks need to embrace trade finance digitisation. With the right solutions in place, banks can offer a more streamlined digital experience, improve their workflows and reduce the cost of trade finance transactions. This, in turn, can help to increase trade activity and provide companies with the finance they need to do business.

For larger banks, and for dedicated trade finance banks, getting budgetary approval for purchasing a specialist solution is likely to be more straightforward. But for smaller and mid-sized banks with fewer financial and IT resources available to them, accessing the technology they need can be more difficult.

Trade finance margins are already under pressure, and growing compliance costs driven by the greater focus on AML and KYC mean that the cost of doing business is continuing to rise. As such, banks that have smaller volumes are likely to find it more challenging to build the business case needed to invest in a dedicated trade finance system. Purchasing such systems has

historically meant spending millions of dollars on an on-premise solution, and implementing this type of solution tends to be very time consuming. The ongoing maintenance can also be very expensive for these heavy-duty deployments, which typically require a dedicated IT team to run both the software and the hardware.

All of this has tended to make specialist trade finance solutions out of reach for smaller banks that are often constrained by shrinking budgets, scarce IT resources and regulatory pressure. As a result, many of these smaller banks are using inefficient, manual tools such as spreadsheets and emails to handle their trade finance business – thereby reducing the profitability of their trade finance business.

Without access to technology that can reduce costs and increase efficiencies, banks may find it difficult to offer trade finance in a way that is economical. They may also struggle to scale up effectively, retain and attract customers, and provide the expected level of service needed in this competitive market.

These smaller banks may feel left behind if they are unable to act while their competitors go live with sophisticated new trade finance solutions – and the gap has become all the more significant during the pandemic. As the handling of digital documents became increasingly difficult during lockdowns, the adoption of digital alternatives has sped up considerably. As a result, smaller banks that continue to rely on manual processes and have not invested in a suitable digital platform may already be falling behind their more digitally enabled peers.

The way forward

Fortunately, technology is opening up new opportunities for smaller banks to access sophisticated trade finance solutions. Software-as-a-Service (SaaS) and cloud-based solutions have much to offer in this respect as they can free banks up from the burden of having to implement and maintain on-premise systems.

With a sophisticated cloud-based solution, the hefty upfront costs associated with traditional systems are replaced with a manageable monthly subscription fee. Cloud-based solutions also eliminate the need for internal IT support, and can significantly reduce the total cost of ownership (TCO) for specialist trade finance solutions. As such, cloud solutions have an important role to play in helping bank access the technology they need to support trade growth for their customers.

This approach can offer particular value to smaller banks that might otherwise be unable to access trade finance technology. Surecomp, for example, has recently expanded its Trade Finance-as-a-Service (TFaaS) offering to allow smaller and mid-sized banks to improve their trade finance processing efficiencies and customer service. Banks can now access our leading DOKANG™ trade finance solution as a fully cloud-based service for as little as $50,000 per year, meaning smaller banks can now harness the benefits of the world's most widely adopted back-office solution.

Speed of deployment

While there are other SaaS-based solutions available, one of the most compelling differentiators of Surecomp's offering is the speed at which banks can be up and running with the new solution. Integrating a back-office trade finance system with internal systems can take months, or even years. But by drawing upon decades of experience in the trade finance market, we are able to offer a much more streamlined deployment. In fact, we've made a commitment that banks will be able to start using the solution within just 10 weeks of starting the project – an implementation speed that is a game changer for smaller and mid-sized banks.

Once up and running, banks can use the TFaaS solution to streamline their workflows, speed up transaction processing, and increase their volume handling. Banks can use the solution to access everything from letters of credit, collections and loans to supply chain finance and syndications. They can also use the solution to connect to Surecomp's API fintech marketplace, meaning they are able to access solutions and capabilities from over 30 different providers.

Last but not least, our TFaaS offering gives banks the agility they need to evolve and grow. For one thing, the solution enables banks to scale up as their transaction volumes increase by accessing additional modules, such as documentary collections or our front-office corporate facing solution. It also provides future-proof compliance with upcoming regulatory and market changes, such as SWIFT's transition to ISO 20022 messaging. And banks can ensure they are fully up-to-date with the latest developments by taking advantage of monthly feature releases, without having to spend time on inconvenient upgrades.

What this means is that by using our TFaaS solution, small and mid-sized banks can reduce their IT reliance and cost of ownership by as much as 30-50%. As a result, many players in the industry can now access a system that allows them to embark on their digitisation journeys and better serve their corporate customers. As Santiago Cano, trade finance manager at Banco Pichincha at Ecuador, commented: "Moving to a cloud-based solution aligns with our digital-first strategic direction."

Supporting the recovery

In conclusion, trade finance has a vitally important role to play in supporting the global economic recovery in the wake of the COVID-19 crisis. And while smaller and mid-sized banks have historically struggled to access the technology they need to make trade finance a viable option, the rise of streamlined cloud-based solutions means this is no longer the case. By taking advantage of a rapid implementation time, light infrastructure and subscription-based pricing model, smaller banks can operate more efficiently, reduce transaction costs – and ultimately offer customers access to the trade finance they need.

Enno-Burghard Weitzel is senior vice president strategy, business development, digitisation and Andrew Coles is global head of solutions consulting at Surecomp.

Sponsored article

Lowering the toll: The next step in the digital trade evolution

Why are there still so few bridges between digital islands? And no 'cars' on the bridges that have been built? Michael Vrontamitis, advisor at Kountable and Subra Shankhar, founder and principal at TOTTA look at why digital islands persist, and how they can be bridged. Do not ignore smaller businesses.

Michael Vrontamitis

As digital trade nerds, the last few years have been exhilarating. Back in 2017 there was no plan, no common understanding of what was actually required to digitise trade, and everyone was trying to understand the 'B' word [blockchain]. At that time the International Chamber of Commerce (ICC) Trade Finance Digitisation working group published the ICC Digital Trade Roadmap[1] laying out what was required for some of the key actors to solve for the digital island problem that is exponentially growing in trade and trade finance.

The roadmap created this common understanding and laid out three pillars.

1. Government focused on updating legal infrastructure through implementing commitments, reviewing laws, identifying, and removing barriers and aligning to international best practice.
2. The ICC focused on rules and standards through building consensus, aligning resources, and connecting initiatives.
3. Industry focused on digital transformation through upskilling teams, digitising processes, integrating systems and piloting innovative technology solutions.

In July 2021 BAFT and ITFA published a paper[2] prepared by the ICC Trade Finance Digitisation working group that demonstrated tremendous progress being made. For example, the need for harmonisation of country's domestic legal frameworks with UNCITRAL's MLETR[3] is now on the G7 agenda with progress being made in numerous jurisdictions. The ICC launched the ICC Digital Standards Initiative [DSI]. New eRules were released – eUCP2.0, eURC1.0, URDTT1.0. There were also BAFT's Distributed Ledger Payment Commitment (DLPC) and ITFA's 'Manual of Digital Negotiable Instruments,' among others at a speed more reflective of the digital era versus the multi-year processes that had been followed in the past for new rule sets.

In 2017 the only people who understood MLETR and its potential impact were sitting in the back of the room in their proverbial white coats. Today, even politicians understand the importance of having it on their agenda. That's how far we've come. There are dedicated people all over the globe, lobbying, reviewing, and implementing many of the recommendations in the first two pillars of the roadmap.

The question therefore is why after all this effort are those increasing number of digital islands still not connected? When the islands are connected, why is the use of them still so low?

Still early days

Subra Shankhar

The simple answer here is that it is still early days. We are still at the starting line. Early versions of rules have been written, standards published and connected, while laws to enable the digitisation of trade are newly published, in flight or being discussed.

As with every big transformation project once you are sure that you have the rules, laws and standards in place you need to design and build solutions. And this is where we are.

Pillar three of the ICC Digital Trade roadmap calls for industry to undergo a digital transformation. To prepare systems, integrate them, upskill workers. All great words, but what does it mean in practice.

Typically, when a large enterprise digitises a process well, they review their own workflow, identify process improvements, and develop the requirements for an automation solution. It is rare for any large enterprise to look beyond the process within their own company for example their suppliers' or (business) buyers' processes. Once the requirements are finalised the large enterprise will issue an RFP, select a technology vendor, and then implement.

To ensure success of the solution, their partners will need to adopt it. Large enterprises generally use their market power to force

[1]https://iccwbo.org/content/uploads/sites/3/2020/05/2020-icc-digital-roadmap.pdf

[2]Progress on Trade Digitization 2021 (URL: https://bit.ly/3um8Zzm or https://bit.ly/3mc82ps)

[3]UNCITRAL Model Law on Electronic Transferable Records (2017) (URL: rb.gy/n3qlq4)

adoption. Small businesses may not have a choice if they want to continue to do business with their large buyer or supplier.

In implementing the large enterprises' solution, the small business will usually need to update and receive data through a web portal if they don't have the ability to integrate into their own workflow digitally.

Equal sized counterparties or co-dependent ones to the large enterprise may agree a direct integration via API, EDIFACT or some other standard communication and messaging protocol in order to fit into their own workflow and while there are costs involved in this integration it is necessary for success.

The large enterprise here has digitised its process, but its ecosystem is far from digital. In a connected system you can't just digitise part of the system for it to be digital. Each of these solutions therefore becomes its own digital island.

So how does this feel as the small business who is being asked by its big suppliers and buyers to connect to them in their preferred manner, let alone a myriad of service providers and government agencies with multiple 'Single Window' programmes that have their own connection preferences?

How it feels to be the small business

The complexity of this is the toll that is required to digitise each bridge. Given the resource constraints and prioritisation on income generation most small businesses don't generally have the capacity to solve

this problem irrespective of the scaling benefits solving it will give them because the cost and understanding required to solve it in the first place.

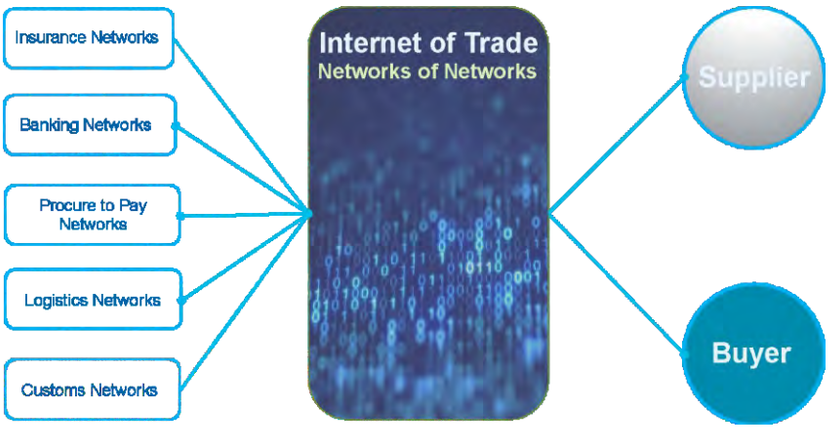
While protocols to interface two systems are readily available, the real cost of connecting is in defining datasets, agreeing liability clauses and legal negotiation. As a result, most small businesses involved in international trade naturally default to paper in their core processes with haphazard digitisation depending on what their trading partners demand.

This complexity is the toll that is stopping cars from using the bridges.

What is needed to lower the toll?

This is not an easy question to answer. It is less about the toll and more about redesigning the bridges. Very few people are actively solving this problem for small businesses. The focus is on solving the automation challenge for large companies and government.

Small businesses need a gateway, a connector to many platforms that enables them to scale. Building the connections to each procure to pay network, each government single window, every ERP (Enterprise Resource Planning) platform, each bank, each logistics company, insurance company and customs network.



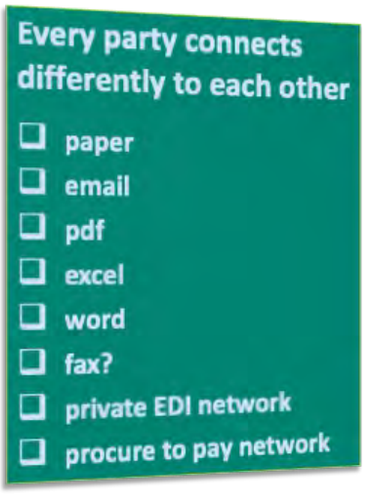
Is the solution a network of networks?

The network of networks is about creating this interconnectivity. Is it a neutral entity providing this service? Is it a series of networks in each trade vertical connecting via a host of applications creating an 'Internet of Trade'? Time will tell. Given the fragmentation of the counterparties in trade and its inherent complexity we don't believe there will be one network to rule them all and collaboration is the only real viable path.

Irrespective of how the market develops, companies will hopefully see the problem that is there due to the digital islands they have helped create. New laws, rules and standards will provide a framework to enable this to be solved more holistically for small businesses.

There is an opportunity here for technology companies and industry players to leverage this evolving framework and for large enterprises to think beyond their own island and more actively engage in building bridges with no tolls.

Meanwhile, small businesses will need access to unbiased information and advice on how to best to streamline their own processes and connect to their ecosystem in a way that allows them to scale in simple costeffective ways.



CGI: The path to trade Nirvana is undergirded by tactical APIs

APIs may not be flashy or high tech, but they could be a critical and tactical route for banks to take on the way to full end-end-digitisation in trade. Patrick DeVilbiss, Offering Manager, Trade and Supply Chain Solutions and Colin Zeglen, Product Manager for Trade and Supply Chain Solutions at CGI explain that evolution and why it's important right now

Patrick DeVilbiss

End to end digitisation is the Nirvana state for efficiently financing trade. But there are steps along that road that will ease that path to the ultimate destination, and one such is a more API (Application Programming Interface)-centric approach. "APIs are the undergirding to what the future of trade will look like," says Patrick DeVilbiss, Offering Manager, Trade and Supply Chain Solutions at CGI. "It may be low-tech, but it is critical. That is what bank and corporate strategy needs to be built around."

Where are we now in the process of end-to-end digitization of trade and creation of new networks? "At CGI we have retooled our back office systems to be very much API centric. It's certainly something we're talking with our customers about in terms of their strategy. We know that it's really critical to the market going forward," DeVilbiss, says. Why so and why now?

"Our rationale is twofold. One element of the criticality is that the ecosystem is changing and there are many consortia and network platforms developing to connect the spiderweb of trade together. That multitude of networks may reduce down at a certain point, but no matter what, it's critical to be able to connect to them in some way, both flexibly and quickly. APIs are a way to enable that connectivity in a relatively short timeframe using modern design patterns."

And when DeVilbiss talks about APIs, he is typically referring to RESTful APIs [where REST stands for REpresentational State Transfer, an architectural style for distributed hypermedia systems] as the backdrop for enabling connectivity.

Trade spiderweb: Interconnectivity with different ecosystems and Fintechs

What should banks be thinking about in terms of how to provide value to their customers through multiple channel partners? "If you look back 15 years, banks got to be the centre of business," says DeVilbiss. "Now they are realizing that their corporate customers are using some of these new platforms, perhaps tying in through an existing treasury management system, or through a B2B platform where they interact with a supplier, or a channel where a Fintech has some funding for supply chain finance (SCF), or one of the bank consortia. Banks need to be able to deliver their own value through that ecosystem on any of those networks."

And the way that they can achieve that is through API capabilities, particularly using real time transactions that provide both visibility into what is happening at any time and also allow users to transact on those networks. "We view that as core and critical to what banks will be doing in the future, because some of these new networks haven't yet reached high volume," DeVilbiss says. "There are banks sitting on the outside waiting to see the [networks deliver the] value promised in press releases, etc. But in reality, once that value hits, they need to be able to move quickly. And in order to do that, they can't be reliant on legacy architecture."

Colin Zeglen

That means those banks may not yet be able to meet modern standards or to achieve the API connectivity they need. "Strategically, banks may be in a 'wait and see' mode, but even then, they should still be planning for future architecting and to be able to meet the needs of the marketplace for tomorrow, and that's just on the trade ecosystem side," DeVilbiss says.

The multichannel future

More widely, banks need to decide how they will engage with corporate customers and this comes down to their perspective and strategy with respect not only to trade, but also more broadly connecting clients and delivering value to them. In many cases, strategy has shifted to more of an omnichannel approach.

Corporate portals are taking in data from other systems, and companies want a seamless user experience through APIs or other integration. The future is certainly one of multiple layers that also need to connect to any trade portal. Those layers include centralized corporate portals, treasury, cash

management, trade and data, mobile channels and transaction banking core actions. "In order to really drive that further or to deliver a more holistic view, banks can utilize things like web services, which are, in effect, APIs that allow abstraction of some of trade data up a layer and present it back to customers and potentially transact through it as well," DeVilbiss says.

They will need a broader strategy in place for how they interact with customers and what kind of information and customer user experience they want. "Things like ERP connectivity are going become more important. That's going to all be API driven. Some of that exists today in terms of basic flows, but you could see that broadening out. You can provide services and API functionality such as generalized financial services or directly through an ERP for your corporate customer. We're only touching the surface of what this could look like in the future. There is a mountain of opportunity."

The key is delivering what trade and transaction banking customers want and need on their own terms. An omnichannel approach does not mean that trade portals will disappear, but rather than banks saying, 'this corporate customer needs to come on to my trade platform', that corporate customer may already be on a platform that then connects back to multiple different banks. "We're seeing this this kind of shift in the marketplace and also new opportunities. This is where I get fired up because we do not fully know how your corporate customers will want to interact with you," DeVilbiss enthuses.

A call to action for banks in trade

The big message for banks is they cannot simply develop or plan for trade as a standalone. "There's a much bigger mindset that you would have at a bank. And in order to deliver seamlessly to your corporate customers, from a UX perspective, you need to understand where your bank is headed directionally both in terms of its technology and in terms of its experience for corporate customers. That is where trade can sometimes get left behind. But understanding that will help you in terms of not getting kind of sideswiped by a project that gets started at a central level that bleeds down to [trade] much later than it should." At the moment the impact is mainly focused on commercial banking, and it and it is still early days, but that change is afoot.

Standards needed to underpin the opportunity

As the landscape evolves and it becomes more clear what APIs may need to be constructed, standards need to be considered. Lessons can be learned on the consumer banking side and through the Open API movement. Corporate customers today might see multiple different banks constructing an API for the same service. "That's where we're going to see frustration," says DeVilbiss. "Hopefully initiatives like the ICC's Digital Standards Initiative (DSI) and others will be able to create a common API framework to use. Ultimately it will be a question of what can you expose through those API channels from either your back office or trade portal to be able to continue to meet the customer where they are now and create that seamless user experience."

The responsibility for API standards should be an industry one, not simply the banks. "Everyone's got a little skin in the game," DeVilbiss notes. "The more collaboration you see creating a standard, the better. We're in an ecosystem and many of those partners are important to that ecosystem. Corporate input and insight can also be helpful."

Evolution in this area is fast, the development of a plethora of APIs is happening rapidly and as standards are developed, banks and Fintechs are going to have to adjust to reach them at pace. "On standards, the market isn't going to wait".

Tactical solutions for end-to-end digitization

How can a bank ensure that they are digitizing end-to-end wherever possible?
- Artificial Intelligence projects – data capture, OCR, etc
- Digital signatures
- Email and electronic presentations

CGI continues to encourage tactical solutions along the route to end-to-end digitization. "Taking anything where there is a manual process, an offline spreadsheet for instance, and shifting to more of an end-to-end digital process offline where you own it is important," DeVilbiss says. "There are certain components in the trade world, physical documentation, that has not that has not gone away and we don't expect that to go away anytime soon, even if we're seeking that Nirvana state.

Nonetheless, incorporation of digital signatures into your platform and intelligent data capture, intelligent automation, artificial intelligence projects are really important to so that you can start to decrease the low value work that you may have to do and increase the high value work that your trade employees can deliver back."

SWIFT changes should be embraced

- New Guarantee/Standby Letters of Credit (SBLC) changes are happening and are impacting operational changes
- New messages and impacts – automatic extension, claims, local undertakings
- ISO 20022 standards coming – benefits for data and compliance
- GPI (global payments innovation) service that allows for near real time payment tracking

Tactically, banks need to be on top of the modifications to SWIFT messaging types on trade in November – particularly as the digital trade envelope messages in Standby LCs and guarantees are moving from unstructured to a much more structured set of methods and messages. "Operationally this has been a nightmare in the short term for some banks, but it will be good thing in the long term and people need to embrace that change," says DeVilbiss. "It's difficult because it feels like we haven't had much breathing room between the changes on the commercial LC side and then the pandemic and now this. Fundamentally, it's going to create opportunities to standardize some of your approach internally. It leads to more automation and more seamless transactions."

Risk reduction benefits

Colin Zeglen, Product Manager for Trade and Supply Chain Solutions, adds that these changes will also help to reduce risk. "You can reduce risk through more standardization. You're not going to have free forms that are essentially an email. Also, there will be better tracking of these items. For instance, you will be able to extract structured data in a SWIFT message more easily than from a free form. Overall, better tracking and better ability to pull out data is a recurring theme."

That, combined with changes with ISO 20022, which is also about creating better structured data, will have important implications for compliance screening in the future, Zeglen says, and will create a worldwide standard for payments. "In some countries the standard is not there yet exactly, but the potential is there for much greater standardization. All of this blends together as the better you're able to track things, the better standards there will be and it creates a much more seamless experience." That will impact operations in a positive way and then in turn, reduce costs and make resolutions faster. "It's just better for everyone in the long term. But there will be more near term pain with all of this operational changes, system changes, etc."

Nobody said the road to trade digitization Nirvana was going to be easy.

No more Libor: trade finance users unprepared for transition

There's less than one month to go until the first cessation of certain Libor rates. So why do corporate users of trade finance still have a long way to go in transitioning all of their Libor-linked instruments to a suitable alternative?

After years of preparation for its cessation there is now a clear timeframe for transition from Libor – the longstanding default benchmark rate for trade finance. After 31 December 2021, Libor rates for sterling, euro, swiss franc and yen, as well as one-week and two-month US dollar Libor, will no longer be published – with cessation of US dollar one-day, one-month, six-month and one-year rates to follow in 2023.

As a result, financial markets across the world have just three months to transition their Libor-linked exposures to a suitable alternative rate. However, a recent TXF report – 'No more Libor: What next for trade finance?' – undertaken in collaboration with Baker McKenzie and BAFT (Bankers Association for Finance and Trade), finds that many corporates within the trade finance sector are still underprepared for the 2021 transition, and more surprisingly, even the 2023 transition.

Libor's significance

Libor is an average rate based on a small number of banks' daily estimates of their cost to borrow unsecured funds from each other and has a critical role in global markets as the world's most widely used benchmark for short-term rates. At almost 40 years old, it is widely used as a reference rate for financial contracts and as a benchmark to gauge funding costs and investment returns for a broad range of financial products, including adjustable-rate mortgages, credit cards, floating-rate bank loans and interest rate swaps.

It is estimated that across these markets Libor underpins approximately $300 trillion of financial contracts worldwide, according to the Bank of England Working Group. Consequently, the cessation of Libor is going to have huge ramifications for every Libor-linked exposure.

Why move away from Libor?

While global markets have grown in complexity and size, the methodology for calculating Libor rates has remained unchanged. The main argument for moving away from Libor – apart from the 2012 Libor rates manipulation scandal – is because it is no longer based on sufficient volume of actual transactions. Following the 2008 Global Financial Crisis, banks were unwilling to lend to each other, eliminating observable financial transactions and consequently, the ability for the Intercontinental Exchange (ICE), the exchange tasked with collecting and publishing the data, to generate an empirically robust Libor rate.

As real transactional data dried up that referenced Libor, it became increasingly reliant on 'expert judgement' from the 20 Libor panel banks, a position that was ultimately deemed untenable by many. Indeed, in 2012 many of these banks (Deutsche, Barclays, Citigroup, JP Morgan Chase, and Royal Bank of Scotland) were found to have abused their position by manipulating Libor rates.

As a result of the rate fixing scandal, and concerns over the volume of transactions, in 2017, the UK Financial Conduct Authority (FCA) announced it would not support the production of Libor after the end of 2021, paving the way for its discontinuation.

What will replace Libor?

Risk Free reference rates (RFRs) are the alternative rates which have been identified as the favoured Libor replacement. RFRs are deemed risk free, or as near as makes little difference, because they are based on real, short term (overnight) transactions, removing the risk associated with 'expert judgements', as well as credit and term risk.

The Bank of England, which convenes and hosts the UK industries Working Group on Sterling Risk Free Reference Rates (RFRWG), has marked RFR as the preferred alternative to Libor. This is a broad industry group and includes representation from corporates and relevant trade associations (such as the Association of Corporate Treasures).

One RFR is set to replace each Libor-quoted currency. SOFR for the US dollar, SONIA for sterling, ESTER for the euro, TONAR for the yen, and SARON for the swiss franc. Each of these RFRs will be based on live data from their corresponding underlying, and importantly, liquid market.

It is estimated by the Federal Reserve Bank of New York that the transaction volumes underlying SOFR are approximately $1 trillion in daily volumes. According to the Bank of England, in Q2 2202 Sonia was underpinned by £60 billion of daily transactions.

While US dollar Libor is the most widely used benchmark across the trade finance industry globally, the transition of sterling and other Libor currencies will have a marked impact on the trade finance sector.

"There are now deep and liquid markets across the SONIA product set," says Alastair Hughes, head of division in the Bank of England's Markets Directorate, and responsible for work on risk-free rate transition. "In len-

ding we have seen a wide range of borrowers access SONIA facilities. We are not just talking about large multinationals like Shell here, but also businesses such as National Express and housing associations. We're seeing tens of billions worth of SONIA-linked sterling facilities being put in place and this number is growing all the time."

Both RFRs and Libor reflect short-term borrowing costs, however Libor can't simply be swapped out with an RFR in existing contracts that reference Libor – at least not without appropriate adjustments.

While Libor is a forward-looking rate, giving the cost of borrowing for the future period starting on the day it is published, an RFR is backward looking. This means that borrowers with debt linked to an RFR will not know the floating rate for each interest period until the end of the period.

Furthermore, as an RFR does not include a credit premium for the banking sector, it typically fixes lower than Libor. As a result, amending loan agreements for Libor transition to incorporate appropriate transition language will be key. As such, the main objective during transition will be to minimise the transfer of economic value between the parties as the transition is made to the relevant RFR plus a Credit Adjustment Spread.

Corporates need to catch up

Despite the progress by the Bank of England and FCA in establishing SONIA, it is apparent many corporates are dragging their feet on Libor transition. Survey results from TXF's report indicate nearly 70% of corporates are not prepared to successfully transition from Libor by 31 December 2021, or even the 30 June 2023 deadlines.

"I don't think understanding the new index is a problem for the financial community. I think the problem is leaving Libor," says Justo García, at Homt Infrastructures, an engineering, procurement and construction contractor. "We're accustomed to Libor, it's difficult to get rid of it."

That perception of the market is evident in the data. Across all the corporates surveyed, just 13% of all their Libor-linked exposures have been successfully transitioned to an RFR. And if any of these Libor-linked exposures are backstop facilities that are yet to be drawn, it is likely that the percentage of exposures that have been successfully transitioned is lower than 13%.

A combined 88% of those surveyed stated that transitioning Libor-linked trade finance exposures to an alternative RFR was difficult. This was reported as a reason why 'very little progress' (1.6 out of five) has been made. "There's some quite complex economics around moving from one rate to the other," says Hughes. "But I think the important thing here is that there is clear guidance to make sure financial providers know and understand they have programmes and governance in place to monitor and help people move across.

"We're very aware corporates sometimes feel there's a knowledge gap between them and the financial service provider. And obviously, historically there have been some unfortunate cases, which may mean, they're not as trusting of financial service providers as perhaps they once were."

Digging into the data further, corporates offering derivatives, swaps, and futures have made the most progress in transitioning away from Libor – 36% of corporates reported that they had made a great deal of progress in this space. Less progress has been made with bank-to-bank loans (18%), traditional trade (11%), supply chain finance (8%), and structured trade/export finance (4%). Trade/export finance is by far the least prepared with 38% reporting none or minimal progress in transitioning.

Some of the slow progress is down to lack of prioritisation. Dealing with fallout from Covid-19 (48%) and Brexit (25%) were both cited by corporates as more important than transitioning all Libor-linked exposures to an alternative RFR (just 3% of corporates stated that Libor transition was their top priority). To compound matters, there was a reported lack of understanding of what Libor cessation means and how to go about successfully transitioning their Libor-linked exposures to a RFR.

Responses also highlighted a disparity between the perceived level of support corporates get from the banks and banks' perception of their own support. This was made worse by a lack of clarity on which RFRs should be used, with delays in the development of a forward-looking RFR being one of the biggest hurdles.

This sentiment was echoed by García. "Right now, we are working on our project in the Maldives and are still using Libor as reference rate.

"We are not receiving enough information from the banks in order to know what is going to happen in the coming months. I think that they [the banks] are praying for an extension of Libor. My perception is that there is a kind of reluctance to proceed."

A forward-looking rate for trade finance

The construct of RFRs might work for some in the export finance market – but not for all. Sovereigns, state-owned enterprises and borrowers in emerging markets in particular might struggle with the backward-looking nature of RFRs.

"To substitute Libor exactly would be to replicate its weaknesses '' says Hughes. "The underlying market that Libor seeks to measure – the market for unsecured wholesale term lending between banks – is no longer sufficiently active to support such a widely used reference rate. This has not changed in the last four years, and it makes Libor a less reliable and more volatile rate – not good characteristics for users of the rate, such as corporates."

Compounded SONIA, to give it its full title, is the preferred replacement for sterling Libor recommended by the Working Group. And for the majority of products that currently use Libor, SONIA is the recommended alternative. However, the Working Group acknowledged in its use case paper that a limited proportion of the cash market would likely require alternative rates. Trade and working capital products such as supply chain finance and receivable facilities require a term rate or equivalent to calculate forward discounted cash flows to price the value of assets into the future.

The result has been the development of two forward looking Term SONIA reference rates (TSRR), produced by the ICE Benchmark Administration (IBA) and Refinitiv, both respected and regulated benchmark providers in the UK.

TSRR are forward-looking rates, similar to Libor, in that the rate is fixed at the outset of the given interest period. Term SONIA reflects the expected average Compounded SONIA rate over a given period, but unlike SONIA, it is not necessarily based on actual transactions.

Dealing with legacy

Standard and forward-looking SONIA rates will not ease everyone's concerns. There will be a significant pool of 'tough legacy contracts' referencing sterling Libor that will mature beyond the end of this year. Many of these contracts cannot be amended or don't have robust contractual fallback language that will automatically transition those contracts to robust alternative rates.

As a result, the Bank of England, in collaboration with the FCA, has created a 'safety net' for corporates that are unable to transfer to the SONIA rates with the creation of a synthetic Libor rate. The FCA was given those powers by the UK government through legislation which was passed earlier this year (Financial Services Act 2021).

Hughes stresses that it should be seen as a 'bridge' that is there to aid a smooth transition, and not a permanent solution. "The FCAs new powers will help ensure there is safety net in place, but this does not remove the need for borrowers to act and we continue to encourage market participants to amend their contracts where they can," said Hughes. "Any safety net the FCA provides in the form of a synthetic Libor rate would be for a time limited period. The FCA have proposed these synthetic rates would be based on forward-looking risk-free rates, so SONIA for sterling, plus the relevant credit adjustment spread."

The FCA still needs to confirm which legacy contracts will be permitted to use synthetic Libor and that decision will not be confirmed until the end of this year. TXF understands that It is expected to run for a maximum of 10 years.

The TXF perspective

It has long been understood that there are more hurdles to Libor transition in trade finance than in other sectors. With greater clarification on forward looking SONIA rates and incoming legislation on synthetic Libor, it's important that corporates and banks engage with each other to come to mutually acceptable solutions.

The example of two forward looking rates in the UK has shown that it is possible to develop usable forward-looking term risk-free rates. All the pieces are now in place for a Term SOFR (US dollars) to be developed. For export finance and project finance, this is particularly significant as 88% of deals across 2020 were financed in US dollars. However, for this to take place the underlying SOFR derivatives markets, which underpins the creation of a robust Term SOFR, must increase in volume and liquidity. With new use of US dollar Libor discouraged after the end of 2021, this liquidity needs to develop quickly.

Trade digitisation: Secret sauce update

It's been an interesting year for trade digitisation. Time will tell whether the secret sauce to trade digitisation been discovered in MLETR and is it something that will get over a decade of industry fatigue on the subject? Will the trade industry be able to get the sauce out of the bottle, will everyone like the same sauce, will they need to? Interoperabilty layers are the latest addition. The story continues.

A regulation that is not a regulation, G7 endorsement, a platform that is not a platform, another boost for electronic bills of lading in shipping with WAVE BL and MSC, the UK Law Commission giving recommendations to the UK government to change English law to help support digital trade, and more. Trade digitisation has had a dizzying year, but it certainly feels like something is coming out of the bottle. The secret in the secret sauce? There is no secret, and there may be more than one sauce.

Starting with the regulation that's not a regulation, the Model Law on Electronic Transferable Records (MLETR). In April, G7 digital and technology ministers endorsed a framework for collaboration on electronic transferable records, which, among other things, supports the adoption of UNCITRAL's MLETR.

UNCITRAL, the United Nations Commission on International Trade Law is the body whose conventions, model laws and explanatory texts are part of what makes us comfortable to buy stuff on the internet globally, among other things (from the 2005 UN Convention on the Use of Electronic Communications in International Contracts). UNCITRAL texts on electronic transactions have been incorporated in more than 100 states, more than half of the world, according to Luca Castellani, legal officer at UNCITRAL. That familiarity is what is underpinning hopes that the MLETR will form some of the spine of attempts to digitise international trade. And the MLETR itself is not a regulation, it is an enabling text to be used as a 'source of inspiration' for national legislators. Its secret sauce is that it is a source (apologies for the pun).

Castellani acknowledges the widespread 'trade digitisation fatigue' that has come from many false dawns. After all, digital negotiable instruments have been in the public domain for more than a decade and have had narrow uptake. What's different now? Underpinning the MLETR are two notions, of control and singularity. "The MLETR's fundamental issue, first of all, this is not a regulation, it is purely enabling. It is both technology-neutral and it allows underlying laws on transferable documents and instruments based on the notion of possession, and national differences to persist," Castellani says. "It is a keystone of the new vision that implements the concept of a data pipeline in paperless trade."

Hold onto the idea of possession. The early adopters of MLETR include Bahrain (in 2019), Singapore (2021) and Abu Dhabi Global Market (ADGM, also 2021). Is MLETR the secret sauce that is going to unlock trade digitisation? Yes, but. "The MLETR establishes control and singularity as the requirements to reproduce possession online. How those can be achieved depends largely on technical solutions," says Castellani.

And therein lies the rub and is the challenge being faced in a variety of different ways. "Different trade platforms have different definitions of dealing with singularity and control," says Oswald Kuyler, managing director DSI (Digital Standards Initiative) at International Chamber of Commerce (ICC). "While this fragmentation doesn't impact less complex supply chains or the ability to execute POCs [proofs of concept], more complex landscapes like retail require a modern approach that decentralises the title ownership – and enables transfer of ownership. Frameworks like IMDA TradeTrust simplifies, standardises and decentralises definitions for singularity and control for various documentation types across multiple industries and regions. ITFA DNI Specification does the same using a slightly different approach. These are exciting times and it will be wonderful watching these frameworks come to life over the next 12-24 months," says Kuyler.

Back to possession: The key ingredient in any secret sauce

There are many countries poised to take advantage of the MLETR framework. The recent G7 announcement had the UK as one of the champions of digitisation. And the ICC UK and Coriolis have spelt out some of the commercial benefits for MLETR adoption and digitisation of trade for the UK economy in an report in April, which argues that digitisation could boost UK trade by £25 billion.

National regulation will be key in delivering any change. A large chunk of international trade and finance is governed by common law structures (the main two being English Law and New York Law). The UK Law Commission, a government body, provides a useful summary of applicable international trade law. The Law Commission's consultation paper was published on 30 April and the consultation period for legal recognition of trade documents such as bills of lading and bills of exchange ended in July 2021. ITFA and the Law Commission have been working on the draft extensively.

For example, Appendix 4 of its draft bill

proposes a bewitchingly simple addition to the current legislation. "In section 89B(2) of the Bills of Exchange Act 1882 (instruments to which section 89A applies), at the end insert "or to a bill or note that is an electronic trade document for the purposes of the Electronic Trade Documents Act 2021 (see section 1 of that Act)."

The proof of any of the 'possession' pudding will be in the testing in court over the next few hundred years.

Platform that is not a platform

Turning to the matter of a platform that is not a platform: TradeTrust, which launched in January 2020. If it's not a platform, what is it? "We refer to TradeTrust as a framework," says Kay Ren Yuh, senior manage, trade, sectoral transformation group at Infocomm Media Development Authority (IMDA), a statutory board in the Singapore government which helps enable TradeTrust.

As a framework, "a particular set of rules, ideas or beliefs which you use in order to deal with problems or decide what to do," explains Kay. He went a long way to describe the recipe of TradeTrust's 'secret sauce' which is not to be a secret. TradeTrust is a multilateral, open legal and technical framework, that enables inter-operability for governments and companies across different trade platforms and formats for the exchange of digital trade documents on the back of a public blockchain.

Importantly, what TradeTrust does is to show a way to help disconnect title management from document management. That means, for instance, TradeTrust enables the carrier, when it is preparing a physical bill of lading, to register the title of that document on the public blockchain as part of the same process. Carriers, banks (even including SWIFT via FileAct), governments, importers and exporters can then go ahead with their own business processes in their own way, but there's one registered version of title.

"Our methods for solving this 'teensy-weensy problem' of paper trade documentation is [publicly available on Github via Architectural Design Records] and we could have just stopped there but we decided to take it one step further and bake those methods into software components that operate at the services layer that are designed to be easily integrated into platforms and systems," Kay says. "These software components are released as open-source so are free-for-use and anyone can look at the code to assure themselves of what it does." He adds: "The trade team at IMDA has worked very hard on this project for the past few years and we look forward to the international trade community benefiting from our efforts."

The concept of a public blockchain (in TradeTrust's example Ethereum), being used so one version of 'the truth' (ie a record of title) is one potentially good use of distributed ledger technology. "I would argue that having a trusted-reliable mechanism to verify and validate possession and control is a principal use case of distributed ledger technology. Embracing public blockchain to truly decentralise who holds title, while still enabling the PDF or data to be used in various different systems is required for simplified change management. Couple this with standards like the Digital Container Shipping Association (DCSA) electronic bill of lading standard ((eB/Ls) that helps democratise the process for preparation and issuance of bills of lading and we can see ourselves moving closer to a interoperable world," says Kuyler at DSI, which is an advocate of TradeTrust.

Progress on digitisation of eB/Ls continues elsewhere. MSC Mediterranean Shipping Company (a founder member of DCSA) announced that its customers can now exchange eB/Ls on the WAVE blockchain network. How close are we to scalability of the 'rails' supporting trade digitisation? Gadi Ruschin, CEO of Wave BL tells TXF, "Scalability is not an obstacle to digitisation today. WAVE BL's technological infrastructure scales to every type of organisation, from the smallest importer to the biggest bank."

WAVE BL is aligning to UN standards. "We welcome every initiative that supports digitisation – whether it's regulatory or commercial standardisation, or a drive to increase awareness in the industry. Standardisation certainly plays an important role in making it easier for companies to adopt digitization, which is vital for sustainability in global trade today," Ruschin says.

Another flavour to use MLETR

Meanwhile, ADGM is aligning with UN standards with its Electronic Transactions Regulations 2021 which confirm the legal enforceability of electronic negotiable instruments such as digital promissory notes and bills of exchange that are equivalent to physical paper documents. It has adopted MLETR with inputs on its electronic transactions framework from International Trade and Forfaiting Association (ITFA)'s Digital Negotiable Instruments (DNI) Initiative and Technology Experts for Regulatory Action (TERA) taskforce (which includes Enigio, a Swedish Fintech).

There is more news on its way, more standards for electronic title documentation, more to cover on the data pipeline in paperless trade, particularly as it will affect SME finance. 'Interoperability' is a word that many of the service providers following MLETR say is vital. How interoperable they will prove to be is untested. It will be interesting, however, to see whether users will have to choose what meal goes under their secret sauce.

On 18 November the ICC published an update on its trade digitisation progress – a roadmap "Reconceiving the global trade finance ecosystem" which sets great stall in building what it calls an interoperability layer into structures – meaning digital trade enablers – trade finance interoperability foundations and thirdly guiding principles for interoperability.

In the ICC report there was mention of the range of different technology platforms used Komgo, Bolero and essDOCS the most used for documentary trade, open account trade, and shipping and freight. The report says: "data suggests that use of digital technology in the sector is patchy with little certainty on when this may become commonplace across different trade finance activities."

This should be digitisation's moment. The pandemic has certainly been a driver for it, and it will continue to be. Says WAVE BL's Ruschin of his solution. "In the COVID-19 pandemic, reliance on paper has become a barrier and has caused severe disruptions to trade. The pandemic has been a turning point where everyone in the trade industry now sees digitisation as essential to business sustainability. Carriers, freight forwarders, exporters and importers have reacted quickly and adopted WAVE BL's digitised documentation solution. At the moment not all banks have caught up, which means there is an undigitised link in the chain. I'm sure this will evolve quickly, with more banks enabling buyers and sellers to use end-to-end digitised document workflows that support LCs."

This is an updated version of an article appearing in May 2021

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