TRADE DIGITISATION

Eyes on the Prize

Intensifying the Focus on Trade Digitisation


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The challenging economic outlook and its potential impact on global trade were hot topics at Sibos 2022. But there were also highly encouraging indications that perennial themes, such as ESG and digitisation, are entering a decidedly pragmatic phase. Two experts from J.P. Morgan Payments share the inside track on the latest trade-related developments, including an exciting partnership with AI-driven fintech platform, Cleareye.

Having already endured three chaotic years for markets and economies, banks and corporates are bracing themselves for further turmoil as 2023 continues into its second half, with ongoing macro uncertainties, geopolitical tensions, and the war in Ukraine demanding they remain on the front foot, says Natasha Condon, Global Head of Trade Sales, J.P. Morgan Payments.

Indeed, the challenging outlook had been one of the main talking points at Sibos in Amsterdam back in October 2022. Speaking to TMI shortly after the conference Condon highlighted some of the key issues for banks and corporate treasurers that had been discussed animatedly, both on and off stage, at Sibos. These were notably the strong dollar, inflation, volatility, and the latest advances on the road to digitisation.

"For banks, the way the external operating environment is playing out is causing considerable pain in terms of dollar funding, cost of funds, credit, capacity, risk-weighted assets – all the kinds of issues you expect to test the banking market when times get hard," notes Condon.

Macro challenges ahead for emerging markets specifically were another major talking point, with concerns voiced about the impact of dollar FX rates and dollar strength, which, in effect, is leading to the US "exporting inflation" to countries, putting pressure on local central banks, and undermining trade flow.

And while energy and food remain topmost concerns when it comes to commodity price inflation, Condon says the outlook for global agricultural fertiliser supply has moved rapidly up banks' and corporates' list of concerns.

She notes: "We should all be paying a lot more attention to what is happening in the global fertiliser market. Due to the lack of supply of certain fertiliser components that used to come from Russia and Ukraine, low yields from agriculture

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globally next year are basically baked in, there's no getting away from it now."

Beyond theorising

Turning to the more operational concerns expressed in Amsterdam, Condon says these revolved around perennial themes, such as ESG and digitisation, but with a vital distinction versus previous Sibos gatherings. "Finally, there is a sense that we've gone beyond theorising and we are now into the practical aspects of implementing and executing ESG strategies."

How to define good standards for an ESG-compliant deal and managing instances where the 'E' element is in conflict with the 'S' were among key issues raised at Sibos, she says. Another was the thorny subject of collecting accurate, accessible data that is granular enough to support ESG programme proposals and transactions.

"How do you collect that ESG data? Because if the banks are going to police this, act as judges in some way as to whether a transaction is ESG compliant, then what metrics are we going to apply, and exactly what data will we need to collect? How are we going to get our corporate clients to provide that data since we don't ask for it today?"

Financial inclusion, an aspect of the 'S' element in ESG, was also much in mind at Sibos. Condon says its importance has been magnified by the turmoil of the past three years and the tough challenges for the global economy currently. "As a result, many corporates and banks are thinking hard about leveraging their activities to drive financial inclusion, support small suppliers, small businesses, and minority-owned counterparties in their supply chains."

Rethinking digitisation

As with ESG, Condon sensed at Sibos that digitisation is also undergoing transformation, with collaborations between fintechs and banks helping to drive the development of real-world solutions that are more practical than those that were out in the market a few years ago.

In the past, much of the effort on digitisation by banks and fintechs tended to focus on developing "utopian" universal platforms for the whole of global trade, she explains, with all the actors in the space, including buyers, sellers, banks, freight forwarders, shippers, and insurance agents, on one platform globally.

"That was how we were going to solve the fundamental problem of all the paper that flies around the world in global trade. Well, it's 2023 and my business still receives roughly four million pieces of paper per year. Can you believe it?

Natasha Condon
Global Head of Trade Sales, J.P. Morgan Payments

"Those previous platforms were extremely well meaning, and they were developed in many cases using very high-quality technology by very smart people, but fundamentally, they didn't get the traction because it's an impossible challenge they set for themselves."

In response to those past unsuccessful attempts to create universal platforms, J.P. Morgan Payments, along with others in the industry, is adopting a different strategy. "The emphasis now is more on digitising bits we can control, approach it like a jigsaw, one piece at a time, with a focus on areas where we can actually get traction with clients. Such an approach means we stand a much better chance of making tangible progress. The idea is to create a network of high-quality solutions for these areas that will eventually all talk to each other, the magic word for that particular ambition of course being interoperability."

Condon points to J.P. Morgan's strategic alliance with Cleareye to digitise trade finance operations as a successful example of this enlightened approach to digitisation. Explaining the rationale for the Cleareye alliance, Condon says J.P. Morgan Payments boasts a significant trade business and an associated documentary business which, as at every other bank, has traditionally relatively high fixed costs because of the manual effort involved in handling paper. She says digitising the business, in general, is one way of moving the needle on cost of business for the banks.

"The more global a business is, the more trade business it can do. And every country that it operates in has a regulator, and every regulator has a view on what the business should be doing, and those views change over time. The standards on anti-money laundering, for example, are tightening everywhere, as they should, but it lays more work upon the banks; there's an expectation that banks 'police' adherence to standards."

Notable examples of such regulatory challenges for banks include India's Legal Entity Identifier initiative to prevent fraudulent duplicate financing from different bank lenders for the same trade inventory, and moves by UK authorities to tighten up trade-based money-laundering requirements.

"All of this is good progress, and it's positive that some of the regulators are paying attention to how we can all do business better over time, however it also adds to the cost of doing business, in every market we work in," says Condon.

Tackling skills shortages

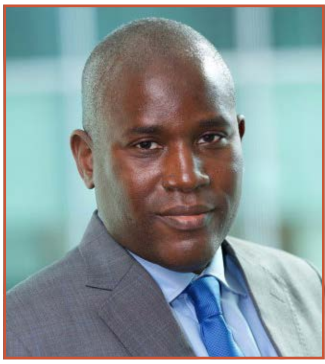
Another major challenge developing for banks is a "very worrying" projected shortage of skilled trade document checkers. Condon says that her operations team at J.P. Morgan Payments boasts "some enormously knowledgeable, skilled, and expert people" with 20 to 30 years' experience in document checking. But a considerable number will be retiring over the next 10 years.

"There's a demographic cliff edge with document checkers that we all know about in the industry," she says. "As it stands, I won't be able to replace them because there are few young people who really, really want to be document checkers on letters of credit [LCs].

"There is, therefore, a risk that in five to 10 years there will be severe shortages of skilled document checkers. It has already resulted in a massive talent war within the trade industry. I'm competing with my valued peers all the time for high-quality operations staff."

Condon believes the ClearTrade solution developed in partnership between J.P. Morgan and Cleareye will help address the issue. Key features of ClearTrade include an optical character recognition (OCR) module for scanning and digitising documents, and a compliance module that watches out for trade-based money laundering.

ClearTrade also offers a module that checks documents under letters of credit and spots discrepancies. "That is a really impressive element because it is something that has been incredibly difficult to achieve, and only a few have tried to develop something like it."



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The solution, which took three years to develop, is currently live in Hong Kong, one of the key processing hubs for J.P. Morgan's trade finance business, and she hopes that by the end of the current year it will be live in all of its processing hubs around the world.

Condon is keen to stress that the data used by ClearTrade is not shared, that there is no co-mingling of one bank's data with another's. All the data used, however, will help the solution internally to learn and become better over time, benefitting all users.

"The whole thing becomes a virtuous circle over time, and I am genuinely quite excited about that. Members of our operations team love ClearTrade. It saves them the less interesting work associated with the initial checks, and it's proving more intellectually stimulating for them too. It's also great to see the solution out in the real world and available to everybody."

Facing working capital woes

Mulling over the challenges ahead of corporate treasurers specifically, Condon is especially concerned about the outlook for working capital. Like many others, she believes "a perfect storm" is developing on this front. She explains: "Supply chain disruption has led to many corporates building up inventory in order to protect themselves, but now they are looking at a possible global recession, and consumer demand has been dropping.

"As a result, lots of them are sitting on huge amounts of inventory, which they are now, frankly, finding it hard to shift. That is driving a deterioration in working capital performance. And then, as mentioned, we have commodity price inflation, which the vast majority of corporates are exposed to in some way, as are the consumers, so buying power is going down.

"The upshot is that right now there is huge demand for working capital support, but a shortage of supply, and that's causing challenges everywhere."

Condon also points out that on the payables side of working capital, many buyers are reluctant to reopen conversations about payment terms with their suppliers, as they too look to shield themselves from pain. There are, however, options buyers can consider, such as an SCF-type structure to support their supply chains. "The immediate challenge is for businesses to get their small suppliers through the crisis and just keep business flowing," says Condon.

Exploring all avenues

Bayo Osolake, Global Head of Financial Institutions Trade Sales, J.P. Morgan Payments, echoes Condon's call for all parties, not least the bank's clients, to be open to considering alternative, sometimes innovative options, such as the ClearTrade solution, for navigating around the many tough trading challenges they face.

J.P. Morgan Payments itself remains proactive in exploring all avenues to best support its clients globally. Osolake says: "The way we have been able to do that is through partnership and collaboration with multilateral organisations and other trade financial institutions."

He cites J.P. Morgan's engagement with the US Department of Agriculture (USDA) under its 'GSM-102' programme as an example of the bank's nimbleness in leveraging novel solutions for clients. The GSM programme provides credit guarantees to encourage financing of commercial exports of US wheats and other agricultural products. The idea is that by reducing financial risk to lenders, credit guarantees enable lenders to facilitate global trade.

"Over the course of 2022, many clients in many countries had been looking at pivoting from Russia and Ukraine to find other sources for their wheat imports. The GSM-102 programme has been very useful for supporting that. The advantage for us as a bank is that by collaborating with the USDA, we're able to offer competitive pricing and a longer tenor than normal. It's effectively a win-win for all parties," he says.

Another initiative, of which Osolake says J.P. Morgan is particularly proud, entailed the bank joining forces with the Asian Development Bank to support trade financing for the import of vaccines and other health equipment into some of the countries in South Asia during the pandemic.

The bullish scenario

Elsewhere, the global pandemic also helped to fast-track the development of digital trade. Electronic signatures, for example, are now being accepted on trade finance transactions, with lockdowns and the explosion in remote working during the pandemic being key drivers for their greater acceptance.

The bank is also engaging with industry bodies that are looking at how they themselves can support trade digitisation across the economy. "As a thought leader in digitisation, we believe we can make a valuable contribution to the work of these bodies by providing helpful guidance.

"One of the big hurdles to digitisation is that it lacks a unified legal framework globally. It needs to be harmonised, so actively engaging with various parties in different jurisdictions to promote that, and thereby to support trade flows, is important. And while we have now started on the practical phase of the journey to trade digitisation, there is clearly still quite a bit to do."

In considering the outlook for global trade volumes generally, Osolake is reminded of a client event in London last summer, with attendees hailing mainly from Western European financial institutions. To glean their view on the outlook for global trade volumes, participants were asked to predict from one of three possible scenarios for the next couple years: strong growth in trade volume; a significant recession in 2023 accompanied by a large drop in global trade; or little dramatic change, a "puttering along" in volume.

Perhaps surprisingly, the vast majority of the audience plumped for the first option and see strong growth ahead in global trade, with mobile platforms continuing to be a key driver. On balance, Osolake too is bullish on prospects, concluding: "We did see a significant dip in 2020 with the COVID-19 crisis. But then we saw strong growth, and the general trajectory now is that global trade volumes are on an upward trend. We may see some peaks and troughs going forward, but our overall expectation is that we will see continuing growth in global trade volumes."

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