

Lloyd's List

Containerisation International 6th Annual LINER SHIPPING CONFERENCE

April 9th & 10th 2003

Café Royal, Regent Street, London

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Title: How close is the market to paperless trading?

How close is the market to paperless trading?

Most bankers and carriers would agree with Mr. Kim Christensen, Product Consultant and Technical Advisor, Nordea Trade Finance, in Copenhagen who says that there is no shortage of grandiose predictions about the future of B2B e-commerce and the move from paper to paperless trade. Mr. Christensen argues that predictions about e-commerce are meaningless unless all parties in international-trade transactions are willing to make them come true. Aside from taking the risk of making yet another prediction may I start by saying that **having the right approach to the market is one of the key points to move from paper to paperless trade.** My paper explores solutions proposed to the market in the last few years, how they relate to the needs of importers, exporters, banks, and trade service providers such as ocean carriers, freight forwarders, insurers, surveyors and others, why have all solution providers failed so far to achieve critical mass and what could ultimately lead to making paperless trading a reality.

Why has the take-up been slow?

Urs Kern, managing consultant at Cap Gemini Ernst & Young points out six different reasons as to why the take-up of e-commerce has been slow. They are as follows:

1. The leap from paper to sophisticated straight-through processing is too drastic
2. Banks are frustrated because of the 'Bolero example'
3. The workflow of an international transaction is highly complex
4. The investment is high and the volume of trade-finance transactions is relatively small
5. The industry lacks an international communication standard
6. Bank's are waiting for customer demand, whereas customers are waiting for the banks' offerings¹

First, the leap from 99% paper based settlement to the highly sophisticated Straight Through Processing (STP) like BOLERO is probably too drastic. It is Cap Gemini Ernst & Young's opinion that @GlobalTrade could easily build the bridge between paper and e-paper.

Second there has been a big gap between BOLERO's vision when they first launched its platform in 1998 and the available technology. This resulted in high investment cost not only on the bank side but also on the customer side. Many banks have spent considerable amounts of money in BOLERO enabled technology and marketing efforts without achieving a break even on their investments. Now, with availability of BOLERO XML and other changes in their product offering it has become more customer friendly although not all agree. Most banks are still hesitating due to their own frustrations or frustrations of their fellow bankers with the BOLERO experience.

Third, the workflow of an international transaction is highly complex. STP could only be achieved if all participants are using the same Internet communication language. However, the e-commerce investment of banks and corporates were concentrated at the end of the nineties in the so-called e-shop solutions (purchasing portals). The use of the Internet to achieve workflow collaboration (C-Commerce) with other companies aiming for optimisation of the processes is rather new. C-Commerce, however, will be the great opportunity for solutions like BOLERO, @GlobalTrade and TradeCard. On the occasion of a feasibility study for building a collaborative virtual working space in the trade and structured commodity finance area for one of the major banks in Germany Cap Gemini Ernst & Young has calculated the efficiency potential to be between 25% and 40%.

Forth point, there are the relatively high investment cost versus the relatively small volume of trade finance transactions. About 2% of world-wide SWIFT message are letter of credit MT 700 based messages. This accounts for over five million LC messages per year. Trade Finance and Trade Services remain still in most banks a "Bank-in-Bank"- business that is hardly understood by other bank employees. Some banks have therefore decided not to invest in a final initiative but in its components as Document Management System, Workflow System and Security (Certification) considering also the requirements of other departments. The B2Bex portal of Standard Chartered and the All Trade platform of ABN AMRO are very good examples of this. However, customer acceptance of a single bank solution has to be awaited. Especially in Europe customers are looking for multi-banking solutions, a demand that cannot be supported by a single bank platform.

Fifth hurdle is the lack of an international communication standard for trade services operations. In the same manner as trading participants were demanding common international rules for trade finance operations at the beginning of the century, now in the new Internet age the same people are looking for world-wide accepted international communication formats and standards. The ICC has already created the base by launching the eUCP and ISBP last year. It will be very interesting to watch the different initiatives regarding standardization.

Especially SWIFT has to be observed in this context. SWIFT is planning to develop new XML based message types (SWIFT Next Generation). Due to Cap Gemini Ernst & Young's information the focus will be also on trade finance transaction.

The Sixth hurdle is the question of marketing responsibility. Financial institutions in general are waiting for the customer demand, whereas the customers are waiting for the banks' offering. The selling offices of the different initiatives have been in some cases too small to cover the whole market. Now a rethinking can be watched. In Germany for example a certain group of corporates and banks has started to discuss the collaborative workflow optimization.ⁱⁱ

In my opinion one of the main reasons why the take up of new electronic trade platforms has been slow is due to the practices that people are used to. It is difficult to change right away from the reliance on paper documents to not having the legal backing that paper provides.

Another reason is that if you want to achieve straight through processing of electronic documents all parties would need to use the same system, meaning that you have to have importers, exporters, banks and all other trade service providers registered on one platform. Be it a neutral multi-bank platform like @GlobalTrade or Bolero or a single bank solution, they have to be registered and they have to be authenticated. If system access is protected by digital certificates, the software is fairly new and to manage it properly takes quite a bit of resources. There are parts of the world where there is no legal infrastructure to deal with digital certificates. There are other parts of the world where digital certificates cannot be used because of export restrictions. Such restrictions pose challenges to adoption and building critical mass. Taking this into account, if you think about any platform that would need the importer and exporter registered and authenticated on it plus parties in their respective trade chains on board before any transaction could start, that becomes a very challenging task.ⁱⁱⁱ

Kim Christensen agrees with Kern that one of the real obstacles is that *the leap from 99% paper-based settlement to highly sophisticated STP is too drastic*. "If you cannot see or feel a benefit – a reason – for something, you are not into it 100%," says Christensen. He argues that if all of the parties within the trade-chain really wanted this, then all these obstacles would not be real obstacles. I agree with his statement, but must qualify with two points that are crucial in my opinion to the adoption of paperless trade:

1. There must be a system available that can serve as a transition between the paper and paperless document environment;
2. Corporate customers must ask all their banks and trade service providers to participate in such a system.

Corporate customers are importers and exporters. Do both importers and exporters want to benefit from the efficiencies that an electronic trade platform would provide?

Do not rush to say Yes!

Just ask yourself a question: Does the importer want to pay faster?

If importers do not want to pay faster and by joining an electronic trade platform they will be forced to pay faster due to the fact that the exporters would be able to present compliant documents on an average eight days sooner; will they join such a platform?

Should they want to have the goods just in time for Christmas sale or be afraid that the perishable goods will spoil if they are held up in the discharge port due to the fact that the commercial set of documents is held up at the counters of a negotiating bank, then they may want to join an electronic trade platform that will make the transaction move faster. In other cases it may not be in their best interest to join such a platform unless they are forced to do so.

Who will drive change towards paperless trade?

Exporters will lead the change from paper to paperless trade since they have the most to gain from the efficiencies created as the result of speeding up the transaction flow. Exporters want to improve the existing paper process leading to discrepancy free documentation, faster payment and cost savings.

Exporters that sell on letter of credit terms deal with many advising, negotiating and confirming banks. Most large exporters say that in order for them to change their existing paper based process the service provider of the electronic trade platform must offer a multi-bank solution for trade services.

This is the main reason why our company has developed @GlobalTrade Export, a Multi-bank Solution for Trade Services. It is a fully open web-based system for completing cross border trade transactions over the Internet that adheres to ICC (UCP 500 and eUCP) rules and international standard banking practices. The system offers straight through processing by merging banks' systems with the ASP based document management system, while allowing users to leverage their existing IT infrastructure.

@GlobalTrade Export makes it possible for a letter of credit to be advised over the Internet from anywhere in the world; to virtually eliminate delays caused by discrepancies in paper-based processing; and to track the entire transaction process on-line in real time. It allows for faster payment processing, preparation of export documentation, centralized printing of documents, improved efficiency through information reuse, global collaboration, savings in courier costs, faster

document delivery, real-time multi bank global reporting on documentary business, and secure Internet connectivity of exporters to their banks and trade service providers.

The most important feature of the @GlobalTrade Export system is that it allows users at any time in the transaction to convert electronic documents to paper.

Unlike other electronic trade platforms that must have the importer, exporter, banks and trade service providers registered and authenticated with the platform before a transaction can start, @GlobalTrade Export can start with the exporter and its advising bank only and then connect the exporter's trade services providers and other parties. Should the importer and its issuing bank want to register with @GlobalTrade Export they would be also be able to receive documents and exchange messages with other registered parties electronically and securely through the @GlobalTrade system. This will ultimately lead to eUCP credits and electronic presentation since a system would already be in place and users would gradually be able to make the transition from paper, to paper and electronic, to electronic documents.

The role of electronic trade platforms and one-bank eTrade solutions

We have all heard about Bolero, TradeCard and @GlobalTrade as the three main trade platforms positioned to improve the efficiency in cross border trade transactions. Large trade banks such as ABN AMRO, Deutsche Bank, JP Morgan and Standard Chartered have developed their proprietary electronic trade solutions. Other trade banks have invested in web based front-end systems for import and export LCs and some have updated their back office systems to handle centralization of multi-branch processing, document imaging and other services. If you take the best features from the above-mentioned solutions and put them together you will probably have a super system. The question to ask is: super for whom? The bank, importer, exporter or trade service provider?

Super for the **bank** would be a system that would drive more business to the bank.

Super for the **importer** would be a system that would allow the importer to see and print commercial documents as soon as they are uploaded onto the system.

Super for the **exporter** would be a system that would help prepare documents compliant with LC terms and would lead to faster payment and better monitoring and control of its trade operations.

Super for the **trade service provider** would be a system that it would not have to pay for and that would help it provide better customer service.

If you agree that the exporter will lead the industry to change from paper to paperless trade a solution that will be successful must adhere to the needs and wants of the exporter. Such a solution must be multi-bank and must allow all trade service providers and other parties to the trade transaction hassle free participation.

The market needs improvement in the handling of trade transactions. Too much time and money is spent today in handling paper documents. In some markets the paper will not go away for a long time and this is why the right approach is needed in order to achieve market penetration. The company or companies that will find this correct approach will change the face of the trade services industry and will make the work of all participants in a trade transaction easier, safer and more efficient.

How to bring all parties to a trade transaction onto the same electronic page?

'The eUCP articles coming into force on April 1, 2002 have given a signal to the market at the right time,' said Wolfgang Friedinger, Head of Product Management, Clean Payments/Documentary Business at HVB Corporates & Markets Bayerische Hypo-und Vereinsbank AG. 'The ICC has created new international rules available for the electronic sector that are accepted as common standard in the same way as the normal UCP 500. But corporations worldwide are just beginning to re-organize the settlement of international trade and to move towards electronic documents. Therefore, the demand for information regarding eTrade Services is very high and a lot of awareness training has to be done.'^{iv}

Friedinger added that his corporate customers are expecting HVB to inform them and provide training in these new areas. 'Having talks and workshops with corporations to keep them informed and make them feel comfortable with this future are issues that will be on our agenda for this year. If they want to move forward we are prepared to pilot systems with them that assist in handling electronic documents or in making workflow processes for settlement of international trade more efficient,'" stated Friedinger.^v

Mizuho Corporate Bank Ltd., which is one of Japan's leading banks and serves seven of the ten Japanese corporations, hosted the International Trade Services e-Commerce Seminar last year. Invited to the seminar were three hundred companies that conduct a significant volume of international-trade-related financial transactions through the bank. Following the successful seminar, Mizuho invited interested corporate customers to participate in pilot projects. 'All our trade finance customers want to find an easier way to present trade documents - at low cost and in a secure environment,' said Ms. Makoto

Hasegawa, Assistant Vice President of International Trade Services Division No.1 (e-Trade), Mizuho Corporate Bank, Ltd.^{vi}

According to Hasegawa, Mizuho is still looking into the implications of eUCP and expects big changes in this area in the near future. Friedinger agrees. 'The eUCP has been published at the right time and has given an important signal to the market as to where the future will be. We think for easy L/C structures electronic documents and consequently the eUCP will prevail in the market within the next two to three years.'^{vii}

I personally see the eUCP as a useful road map to follow. Having participated in the building of @GlobalTrade Export in compliance with eUCP rules I can say that it will take many years for adoption of eUCP for the same main reason as stated earlier in the paper. That reason being that the importer has to initiate the issuance of a eUCP credit. If it will not be in the importer's best interest to issue a letter of credit subject to eUCP obviously adoption will be slow. Once banks will have systems in place that could handle electronic documents exporters could start asking their importers to issue credits in their favour subject to eUCP. The state of the market today is that most banks are not moving until their 'important' customers ask them for a system that will help them improve their trade services, and customers are not moving, waiting for their banks to offer them a comprehensive solution. A comprehensive solution means a multi-bank open platform allowing participation of all parties to a trade transaction.

Although multi-bank solutions are not necessarily in the best interest of large banks, Bolero and @GlobalTrade Export are pioneers in the market. Banks and corporations around the world are currently piloting both systems. Bolero aims to set standards and achieve straight-through processing in moving data and documents. @GlobalTrade is taking a simpler approach starting first with improvement of the process of handing paper documents via the Internet. Large exporters are asking for a multi-bank solution for trade services as it would not only save them cost and time but would also give them far greater control over their entire export operation. Despite the fact that most large exporters run sophisticated ERP systems letters of credit, guarantees and documentary collections are handled manually and recorded on spreadsheets at best. Internal approvals and amendments are requested by phone, e-mail, or fax and are stored in master files.

'Our customers want to handle their international trade business as easily as possible and increase efficiency within the trade chain,' said Friedinger. 'They are looking for easy, cost-saving solutions that also hold the possibility of moving to paperless trade step-by-step.'^{viii}

What does this mean for Liner Shipping?

Ocean carriers are very important participants in the trade transaction. The negotiable bill of lading is still called for in the majority of letters of credit subject to UCP 500. Although the push is towards Sea Waybills and electronic alternatives to transfer title, the negotiable bill of lading remains an essential tool of trade finance.

Ocean carriers have made investments in Intra, GT Nexus and CargoSmart as well as their own web sites as far as electronic booking, shipping instruction, remote BL print and track and trace. The next step is to develop blank paper BL solutions and to integrate with banks and neutral multi-bank platforms in order to give their customer greater efficiency and cost saving.

Since many letters of credit still call for bill of lading to be manually signed there must be work around solutions created in order to comply with the terms of the credit and still offer a more efficient way to handle paper documents. Our company is positioned as the bridge between ocean carriers and financial institutions. We have a game plan for the next seven years in terms of moving from paper to paperless trade and are in the final stages of launching @GlobalTrade Export commercially. @GlobalTrade Export will start by solving the needs of the exporter and gradually moving to eUCP credit and paperless trade. Once large exporters start using any system their bankers, carriers and other trade service providers should join in as well providing the barrier to entry is not too costly and the software is simple to use.

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 - ^{iv} *L/C Monitor*, Volume 5, Issue 1, January/February 2003. p. 1.
 - ^v *L/C Monitor*, Volume 5, Issue 1, January/February 2003. p. 1.
 - ^{vi} *L/C Monitor*, Volume 5, Issue 1, January/February 2003 p. 2.
 - ^{vii} *L/C Monitor*, Volume 5, Issue 1, January/February 2003 p. 2.
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Prior to founding GlobalTrade Corporation, Jacob Katsman was the Director of Finance of a multinational steel trading company. He also managed trading companies in Asia, Europe and North America. Katsman is a recognized expert on international trade. His book [How To Make Money Without Money. The Art of Transferable Letters of Credit and Assignments of Proceeds](#), is regarded by the international banking community as a standard guide to the practical use of letters of credit in trade finance. He is the Managing Editor of *L/C Monitor* www.lcmonitor.com, a legal financial journal covering practical aspects of payment instruments in international trade and the Founder of the International Trade & Banking Institute www.itbi.net. For the past three years Katsman has been involved in the development of @GlobalTrade, a Multi-bank Solution for Trade Services that aims to bring all parties in a trade transaction onto the same electronic page.