

Promise of a paperless future for trade finance

The internet is dead, long live the internet. No-one gets excited about business to consumer websites anymore, but you will find plenty of money — and investors proclaiming the benefits of business to business websites — in the trade finance sector.

Jamie Ivey discovers that many corporates are realizing the internet is going to change the way that business is done.

The next decade is going to be about driving out inefficiencies from corporates' external supply chains. Historically trade has been a paper and time intensive business. Arranging the necessary cover to offset the risk of international trade through mechanisms such as letters of credit and performance guarantees is a laborious business. Up until now there has been little or no alternative but new systems have been developed, targeted mainly at the large number of so-called vanilla trade finance transactions carried out by corporates every day.

There are many different products in the market place (see page 31 for a selection of those available) and each addresses a different part of the trade chain. Their roles vary from offering a market place for trade finance instruments, or providing a tendering system facilitating access to trade finance from banks, to establishing the infrastructure to process trade orders from supplier to purchaser in a paperless fashion. The basic proposition, of course, is

that if corporates choose to use these systems they will be saving time and money.

The figures given by those involved are impressive, particularly in terms of the growth that they display. Looking back at 2001 Kurt Cavano, the CEO of TradeCard, says: "By the end of the third quarter of this year, we had processed a total of \$60 million – consisting of \$10 million last year and \$50 million this year. We will probably do \$50 million in the fourth quarter this year, and \$50 million in the first month of next year (2002). It is ramping like crazy, we will do several billion next year based on the customers who have signed up and what they have committed."

There are also some significant corporate names that are beginning to explore these alternative methods of conducting trade and sourcing their trade finance requirements. Thomas Ross, the managing director of bfinance.co.uk, cites the example of a leading French car manufacturer which confirmed a Eu1.5 million (\$1.34) letter of credit through bfinance and says: "You would have thought that the company had such buying power that they would be getting the best price in the market. They improved their price by 6% [by using bfinance]." Cavano counts companies such as Wolverine and RadioShack amongst his customers and says: "We have two of the top five retailers in the US who are using TradeCard, which we have not announced yet."

Arguably though, it is not the bottom line cost of accessing trade finance through on-line exchanges which is the most interesting financial development. Rather it is the ability of some of these systems to get into the financial supply chain and provide a mirror image of the physical supply chain. As Cavano argues: "The last ten years has been about just-in-time inventory management, and what TradeCard is doing is bringing those same concepts to money." The idea is that in the future corporates will be able to allocate their working capital at precisely the moment required to fulfil a purchase order.



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It is also topical at the moment because after the big corporate collapses of last year, CFOs and corporate treasurers are under increased pressure to apply their working capital to their core business and not to financing a trade client.

Luigi Laferla, the managing director of LTP Trade, gives the example of Enron saying: "What captured my attention most was that among the names, sometimes I found that it was corporates who had been losing money. A corporate is not supposed to have a credit exposure to Enron."

Peter Scott, the commercial director of Bolero, supports these arguments and says: "It is all about cash. What people are realising is that there is a huge amount of cash tied up in the inventory supply chain and they are trying to look to squeeze that cash out of the business. Not only by reducing their costs, but also looking at the transaction cycle and the inventory carry cost that they have as a consequence of the inefficient trade process." The argument is that systems such as Bolero and TradeCard are going to do for corporates' external processes what enterprise resource planning systems did for internal processes in the 1980s and 1990s.

Rio Tinto's subsidiary Hammersley Iron joined Bolero in December 2000. Rio Tinto, BHP Billiton, Nippon Steel, POSCO and associated banks and shipping companies began a trial test of Bolero's messaging program on September 1 2001. Nick Stephens of Rio Tinto says that it is too early to quantify the advantages that Bolero will bring to the company, although its main benefits are seen in terms of process improvement, reduced transaction costs, reductions in technical risk and increases in functional capacity. He argues: "Using Bolero will result in closer integration with our customers and a greater understanding of each other's business needs, which will



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enable Rio Tinto to better service customer requirements.”

Rio Tinto's promotional material illustrates the efficiency savings that are in the process of being introduced into world trade. The company used to have 10 different bill of lading formats, different invoice formats, different sea-way bill formats, different draft survey formats, and different statement of facts formats. They now aim to have just one standard format for all.

The arguments seem convincing, but following the bursting of the internet bubble it would be logical to assume that investors have become much more cautious when it comes to ploughing money into dot.com companies on the basis of future performance. Either they have not, or there is some substance to the claims being advanced by the companies involved. LTP Trade completed a fund raising in July 2001 which capitalized it to fund the next two years of development.

TradeCard has attracted \$70 million of funding and is owned 74% by New York private equity firm Warburg Pincus.

And yet those involved in this new dynamic area of business, such as Scott, freely except that in terms of market share, the progress of companies such as Bolero is negligible. If the logic of cost savings and just-in-time working capital management is so persuasive why are more corporates not using these systems?

The common denominator between the systems mentioned in this article is that they are relatively new attempts to offer financing and trade solutions to corporates. As such, they have to overcome a degree of initial inertia in the management of corporates, who are either ill-informed about the potential benefits of the systems, or sceptical about the benefits of on-line services.

Scott also argues that some corporates may not yet be ready to focus on the pos-

sible advantages of the systems on offer. Many corporates have yet to realise the benefits of streamlining their internal processes and so are not ready for the next wave of examining their external processes to drive further efficiencies.

As with all new ideas it can be difficult to distinguish the hype from the reality and the initial success of products can be based on excessive marketing claims. There is undoubtedly an unusually high degree of inefficiency in the traditional ways of carrying out and financing international trade, but the question is whether the timing is right for all these new products and ultimately whether they can deliver on their promises. Scott at least is convinced: “As far as we are concerned, the timing is pretty good for us, the fact that there is more risk in the market place, that people are looking to introduce efficiencies and cost savings into their companies, might make it a good time for us to actually increase our penetration.” ■

Some of the systems on offer and their applications

Bolero.net – The system promotes itself as a standard international platform that allows importers, exporters, banks, customs and shippers to talk to each other seamlessly. It claims to be able to cut the amount of time spent processing trade documents from up to 25 days to under 24 hours. The key benefit that Bolero offers is the standardization of trade documents. Whereas importers and exporters traditionally relied on a wide variety of documents to cover the various stages of the trade process, through Bolero they can aim to rely on one standard for the whole process.

The service that Bolero provides can best be visualized as an electronic infrastructure that facilitates international trade. It does not in itself provide trade finance, but instead a secure basis against which banks can provide the necessary trade finance guarantees. Peter Scott, commercial director at Bolero, says: “Most of the banking processes are built around reconciliation and compliance. Bolero being able to do this in an automated fashion means that banks will be able to scale their business more effectively, maybe also into areas of trade that they could not previously offer risk intermediation and credit services in a competitive way.”

TradeCard – TradeCard claims that it automates the financial supply chain. Kurt Cavano, CEO of TradeCard, explains: “We are automating the whole process end to end, with people like RadioShack and Wolverine.” Through using the TradeCard system, corporates can access trade finance at competitive prices – payment guarantees are available through the system, replacing the need to get the more traditional letter of credit.

Cavano says: “What we are doing is not only giving them [corporates] access to cheap trade finance but also eliminating the paper in the process.” TradeCard consulted on the Bolero standards and is able to map its system to Bolero. Approximately 275 corporates are using the system at the moment.

LTP Trade – LTP describes itself as the world's first electronic market place, specifically designed for trade finance assets. It is able to accommodate virtually all forms of trade finance assets – such as without recourse sale of transferable instruments, participations in letters of credit – and offers can be made using a variety of methods including auctions, fixed and range prices, first-come first-served and syndication. Sellers can select their audience so that they choose which member banks are approached.

Luigi Laferla, the CEO of LTP Trade, says: “The model that we follow is that of a market place – we try to get together the major suppliers of trade finance risk capital and allow transparent and immediate access from the corporate. We are rolling the application out now to institutions and corporates. It is quite early to say what the take-up will be.”

bfinance – bfinance aims to bring together corporates and banks to arrange commercial borrowing. It has signed up over three hundred financial institutions across Europe to provide the finance. As part of its suite of products it offers corporates the ability to tender banks for their trade finance needs. As with LTP trade it is possible to exclude specific banks from the tendering process, should the client so require. A fee on any transaction organized through the website is payable by the successful bank.

Thomas Ross, managing director of bfinance.co.uk argues that the system has put transparency into a market place which has traditionally been opaque. He considers the system akin to a dating agency – uniting interested parties. He says that bfinance is, “almost more useful for the more complicated transactions. We are able to provide a lot of information that the banks would need to do their due diligence review and to provide direct contacts into the business. We have a certain level of expertise within bfinance so that we can help facilitate the process and that is very much an important part of our service for the less sophisticated corporates”.