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# Technology is key to closing the trade finance gap

**John W.H. Denton**

Secretary General, International Chamber of Commerce (ICC)

Trade finance is considered low risk, with a default rate of less than 1%, according to the International Chamber of Commerce's latest Trade Register Report. Yet there remains a significant and persistent gap between its demand and supply, currently estimated by the Asian Development Bank to be about $1.5 trillion.

A principal cause for this gap stems from regulatory and compliance requirements. Worryingly, 93% of bank respondents to ICC's 2018 Global Survey on Trade Finance viewed regulation and compliance as an obstacle to their growth prospects in the financing of international trade. Regulations aimed at countering the financing of terrorism and international sanctions were of particular concern, with more than 50% of respondents stating they were extremely concerned about the impact of such regulations and sanctions on their ability to provide adequate levels of financing to support cross-border trade.

## Heavy impact on MSMEs

*Persistent gaps in trade finance can lead to exclusion of MSMEs from the trading system.*

This gap especially affects micro, small and medium-sized enterprises (MSMEs). According to the survey, about 40% of rejected transactions involved MSMEs in 2017. MSMEs in Africa were the most likely to face rejection – with 46% of applications declined – while those in North America were the most successful, with about 70% of requests approved. Persistent gaps in trade finance can lead to exclusion from the trading system. As key players and major employers in many economies, the impact on MSMEs is therefore particularly concerning.

As a result, bridging the trade finance gap has been a long-standing objective for the finance sector. While digitalization will not happen overnight, it brings opportunities to address some key issues. Firstly, as the sector moves towards digital processes and paperless trade, new actors – such as fintechs, non-banks and alternative financiers – will enter the market. They are expected to help reduce the gap by decreasing the cost of delivering trade finance and providing greater market capacity, so that SMEs will no longer be solely reliant on banks for their financing needs.

Secondly, emerging technologies such as distributed ledger technology (DLT) also hold promise. Smart contracts, based on DLT, will be able to execute automatic money transfers as merchandise is shipped across international borders and predefined commercial and financial trigger events take place.

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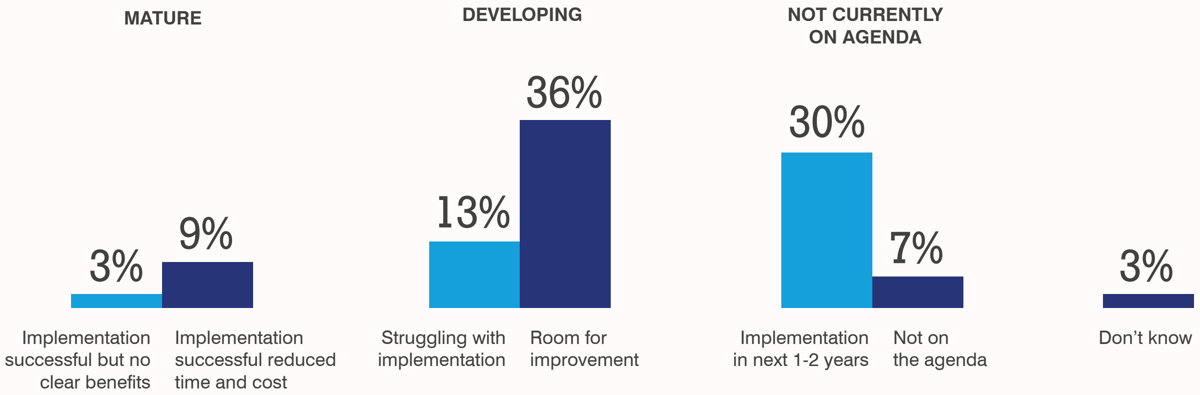
## Assistance needed on compliance

Technology, therefore, holds immense potential to transform the trade finance industry. Yet, significant advances remain necessary for it to close the trade finance gap entirely. While technology can help decrease costs and increase market capacity, MSMEs will require extensive help addressing compliance and regulatory obligations. These include assessing performance risks and determining compliance with requirements on money laundering, Know Your Customer and Know Your Customer's Customer, for example.

As a result, to end the financing gap, it is necessary to strive for standardized regulations and new rules for trade finance that are fit for a digitized industry. Large global market gaps for trade finance persist, and technology presents an opportunity to resolve these, but success depends on a concerted effort from all market participants.

### ICC GLOBAL SURVEY ON TRADE FINANCE

**How digitalized are your trade finance operations?**




# $700 billion

**Estimated unmet trade finance demand in developing Asia each year**

**Source:** International Chamber of Commerce.