Capgemini Consulting

# Trade Finance

## Digitise your Trade Finance Processes

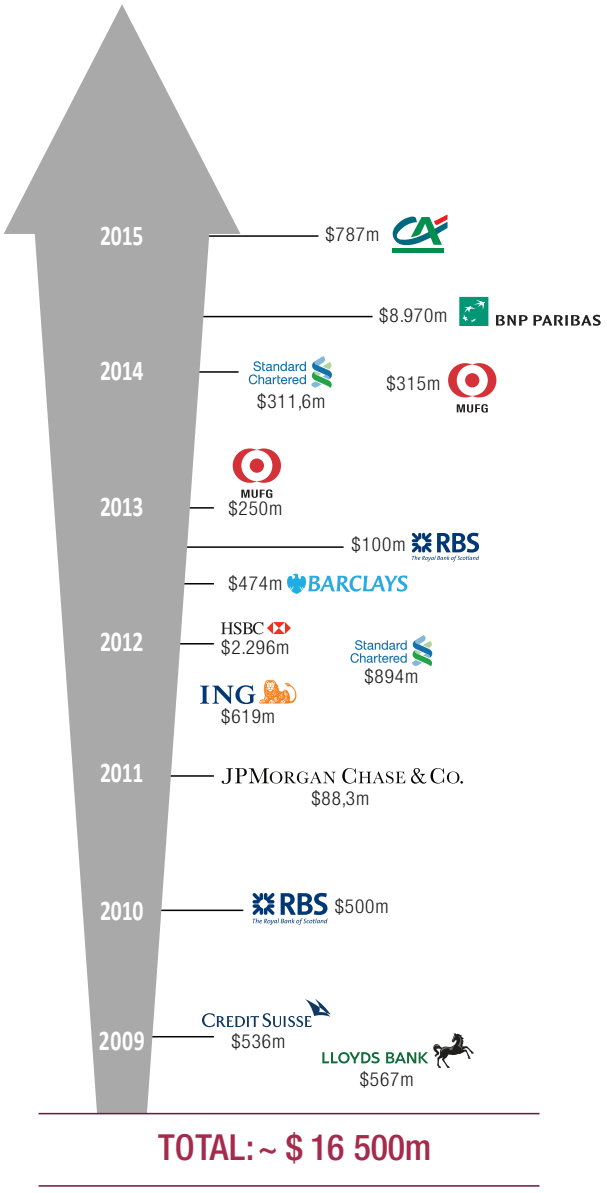
May 2016

# Digitise your Trade Finance Processes !

**All global banks involved in Trade Finance are now facing the same tremendous challenge: Cope with the stressing constraint to abide by the multiple, ever-evolving and more and more drastic compliance regulations, making Compliance risk mitigation a top priority among their other projects.**

- Within the Transaction Banking business, Trade Finance activities tend to strongly appear in the spotlight of Compliance, notably as they are closely tied to international, global commercial flows, and henceforth carrying many related risks (client, counterparty, country, goods, currency…). Considering only the breach of US Financial Rules, Banks have thus had to pay around 16.5 billion dollars fine for the past 6 years (as shown by the chart).
- Adding to that the wide extent of existing regulations, ranging from European Basel III rules, Ethics, to AML and Corporate and Social responsibility, Banks and financial institutions are now facing severe financial sanctions from different authorities, and are consequently exposed to high reputational risks in the event they fail to comply.
- Worse, Banks could potentially lose their Banking license. In that context, Banks need urgently to initiate operational and organizational transformation, by strengthening their internal Compliance control frameworks and implementing relevant remediation plans.

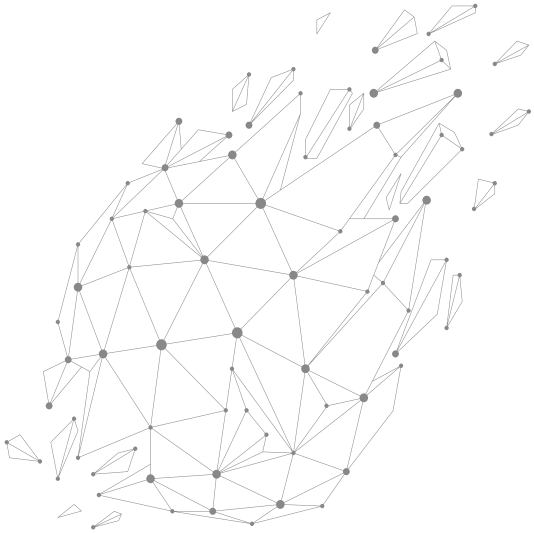
Figure 1 : Financial sanctions for embargoes violation



## TRANSFORM or QUIT

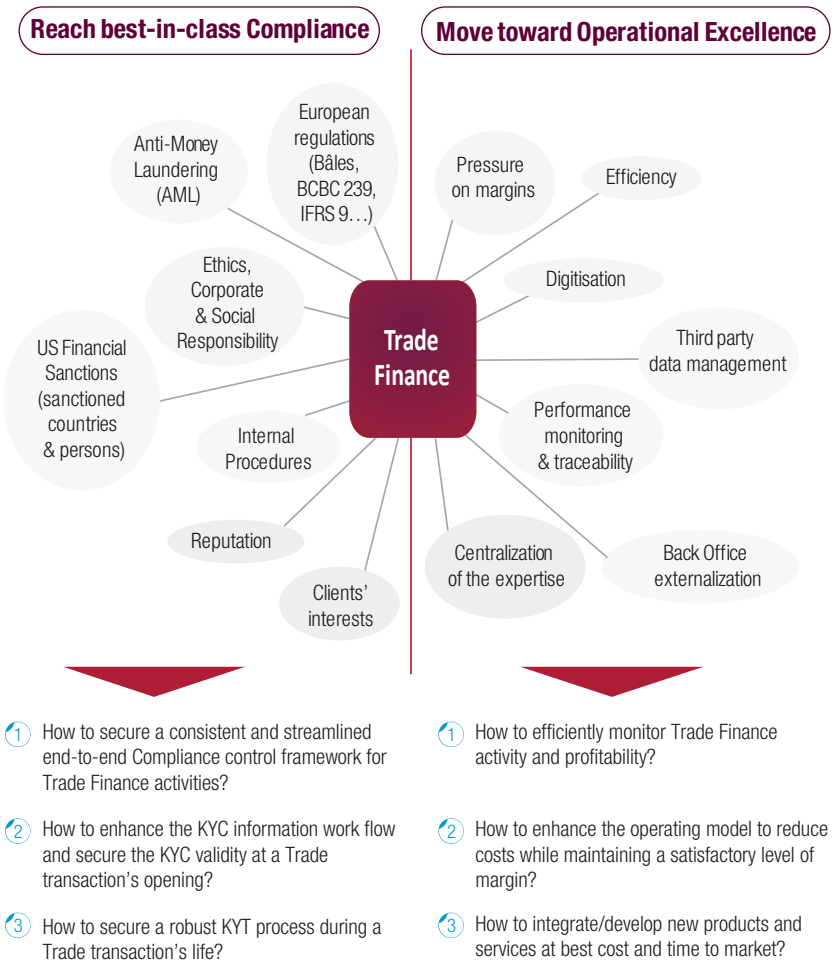
**Business-wise, the Trade Finance market is currently marked by a fierce competition and increasing commoditization.**

- Indeed, the higher pressure on prices, resulting from the downward trend on Traditional Trade products like Letter of Credits (lower commissions observed this last few years) and the progressive shift towards Open Account financing (~80/85% of transactions), directly undermine the margins and thus reduce Banks' profitability.
- Therefore, focus should be made on improving Operational Excellence on the entire value chain (from Front Office, to Middle and Back Offices), while searching for scalability to be in a position to grow and reach capacity to lower costs and keep pricing at par with competitors.
- Furthermore, Banks also cope with the strong necessity to propose innovative, value-added products and services to improve their visibility on the market and enhance their clients' experience. In that area, technology, more specifically Digitisation, would appear as a key enabler to meet clients' sophisticated needs (e.g. E-Banking, host-to-host connectivity, bundling).



## 2 major stakes for the banks, addressed by the **DIGITAL TRANSFORMATION** of the Trade business

Figure 2 : Financial sanctions for embargoes violation




**This paper mainly addresses the following scope of Trade Finance products:**

**Traditional Trade**

| Documentary Business | Guarantees | Working Capital |
|---|---|---|
| Import/ Export Letter of Credits<br>Import/ Export Collections | • Guarantee issuance<br>• Guarantee re-issuance | • Payables<br>• Receivables |

# Reach best-in-class Compliance

# Reach best-in-class Compliance

How to secure a consistent and streamlined end-to-end Compliance control framework for Trade Finance activities?

## DIGITAL TRANSFORMATION
impacts on **COMPLIANCE** risks mitigation

To reach a consistent and streamlined end-to-end Compliance control framework for Trade Finance activities, Banks should focus on achieving the following objectives :

A. Implement a standard framework at Group level to ensure homogeneity of Compliance controls,

B. Ensure a full coverage of Compliance risks at each event of a transaction.

**A.**

THE CHALLENGES

**Implement a standard framework at Group level to ensure homogeneity of Compliance controls**

- Although Trade finance products have existed for centuries, the management of their processes by Global Bank remains complex, due to specific characteristics of this business – a global business, following several process steps requiring different capabilities (e.g. commercial capabilities, transportation expertise, client business understanding, credit risk analysis capabilities,…) and involving a significant mass of documents to analyse in a limited time frame.
- As already mentioned, Trade Finance operations are global – usually involving buyers and sellers from different countries. Then, several entities within a Banking Group should be able to process these products. Consistency of Trade Finance practices among entities is key for different reasons, but especially regarding Compliance controls. A first level of consistency among Banking Group entities is related to Banking fees. This alignment should prevent the client from potential arbitrations for cheaper entities within the same Group. Back to Compliance control, alignment among entities is required for the same reasons : a corporate should not be « tempted » to route its deals to a specific entity because controls might be «easier».

OUR ANSWERS

- To ensure this consistency, the following elements could be considered as key success factors:
  - A global alignment on the “rules” (e.g. Embargo and Financial sanctions rules, AML regulation, local law, bank internal rules) by documenting and providing Group Procedures.
  - A global alignment on the Control Practices, by setting up an unique Control Framework at Global Level, for each process step.
  - A clear view on the full « End-to-end » processes, as exchange of information might be required between Front, Middle and Back Offices.
  - A common Governance, to secure the continuity of the set up.

## DIGITAL OPPORTUNITY

Use a workflow management tool, such as BPM solution, to enhance efficiency and productivity, and to secure the communication between Front, Middle and Back Office

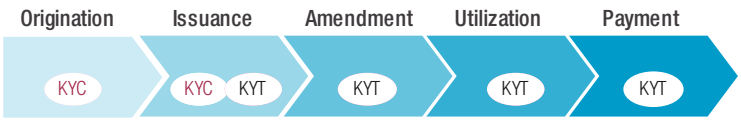
THE CONTEXT

B.

**Ensure a full coverage of Compliance risks at each event of a transaction**

- A Trade finance transaction could last months (even years in the Guarantees business). During this "Transaction life", the transactions are going through several steps, from the facility set up (i.e. origination) to the payment phase. As described in the following scheme, different types of control should be performed at different steps. Some of these controls might be repeated during the Transaction life, due to frequent changes in the Compliance Procedures and in the « Lists » (e.g. Specially Designed Nationals [SDN] List)

Figure 3 : Compliance controls on a Letter of Credit life cycle




- Each event of a transaction is presenting different characteristics: for example, the "opening" of the Transaction, when the Letter of Credit is issued, will be a key step as the Bank will commit itself. But later on, during the "utilisation" step, the full pack of documentation will be received and a detailed analysis of the deal might be possible only at this stage.

- Two types of controls apply during the product life cycle :
- Know Your Customer [KYC] validity control : focusing on the client's KYC validity which could be characterised by (i) a status (e.g. updated or overdue), (ii) a client's sensitivity (e.g. high risk or low risk), and (iii) by specific restrictions (e.g. not to perform business with this client under certain conditions such as specific products, currencies or amounts).
  Actually, the KYC integrates several other components (e.g. ownership, countries of incorporation and of residence, rating, business sector, geographical analysis of the business activity, major clients) and is comparable to a client "profile".
- Know Your Transaction [KYT] controls : focusing on the information related to each transaction, such as the client(s) counterparties, the countries involved (i.e. country of origin of the goods, country of departure and of destination), information on the transportation (e.g. ports, vessels), and the nature of the transported goods.

THE STAKES

- These controls are facing two major stakes :
- The freshness of the control. Regulations are updated frequently. KYC validity control and KYT controls should be performed, and re-performed in regular bases.
- The materialisation of the controls : record the result of the control (e.g. KYC status at a given moment). An adapted materialisation should ensure the audit trail to secure the traceability of these controls, and the possibility to link with related documentation (e.g. a potential waiver from Compliance to process a sensitive transaction).

## DIGITAL OPPORTUNITY

- Use a tool to keep a snapshot and an audit trail of the control, and to archive it
- Use a scanning tool to perform frequent automated control of the client and counterparties database

# Reach best-in-class Compliance

How to enhance the KYC information workflow and secure the KYC validity at a Trade transaction's opening?

## THE CHALLENGES

- Major Regulators (e.g. OFAC, ICC) consider the control on the Bank's clients as the main Compliance control. The Bank has to know which corporate and which activities are supported by its direct funding. Therefore, this control is rather a cross-Business Lines control than a control especially related to Trade Finance activity.
- A difference must be made between (a) the "KYC process" and (b) the "KYC validity control" :
  - (a) The KYC process relies on a client's due diligence at client's on-boarding and a periodical review of its KYC information (e.g. ownership, countries of incorporation and of residence, business sector, geographical analysis of the business activity, major clients, client's rating regarding credit risk, and other criteria), performed by the Coverage team (or / potentially supported by an equivalent Front Office team).
  - (b) The KYC validity control, as described on the previous page, is performed by the Front Office team(s), at deal set up (usually in preparation for the Credit Committee), based on the latest KYC information (e.g. status, sensitivity and restrictions).
- Even though both the KYC process and the KYC validity control are performed by Front Office teams, by contracting deals with their clients, the Business Lines (such as the Trade Finance team) are responsible of the Compliance of these deals, especially the KYC.

## OUR ANSWERS

- Focusing on the Trade Finance activity, and considering the significant Compliance risk factor related to this business, the Business Line needs to secure this control during the whole life of the transaction, and not only at the client's on-boarding. According to ICC rules, at a transaction's opening, the Bank commits to payment or confirmation, which makes the opening an important event in the transaction life cycle. Therefore, it is key for the Bank to secure that no new transaction is opened for a client with an invalid KYC, otherwise, the Bank could be exposed to a Compliance risk.
- In other words, secure the client's KYC validity at the opening of a transaction is key to fulfill Compliance requirements. However, as a common practice, Banks do not perform the KYC validity control at a Transaction opening: It is a challenge as it might generate operational constraints.
- To enable this control, we suggest 2 possible approaches :
  - Automated solutions : set up of an automated upfront process implemented from Coverage (or the concerned Front Office team) to the Business and Operations, to stop adequately a transaction opening when the client's KYC is invalid (incl. audit trail).
  - Example : connect Front Office and Operations IT systems, and perform a regular screening of clients database.
  - Semi-automated solutions : set up of an automated workflow for KYC information from Front Office to Operations, providing updated KYC information, to Back Office Team. Based on this information, Back Office will perform a manual control on the KYC validity for every transaction.

## DIGITAL OPPORTUNITY

- Connect tools used by different teams (FO vs. Operations) to preserve information consistency between systems and increase efficiency
- Use automated tool able to block a transaction opening in the systems
- Use a tool to communicate the relevant KYC information from Front Office (origination stage) to Operations (from issuance to payment events)

# Reach best-in-class Compliance

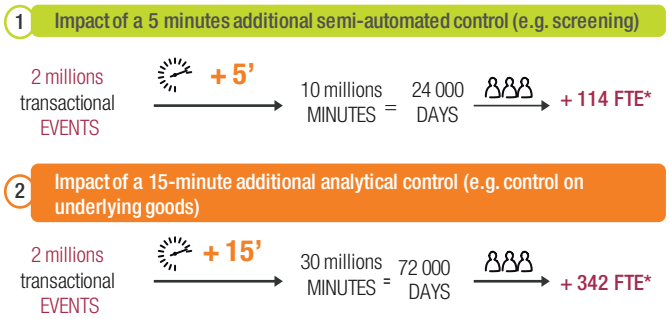
How to secure a robust KYT process during a Trade transaction's life?

- The KYT (Know Your Transaction) controls objectives are to assess the information related to a transaction, from Compliance, Corporate Social Responsibility [CSR] and Anti-Money Laundering [AML] perspectives.
- The Bank should be able to control, at each event of a transaction, the counterparties names, the countries and goods (nature & origin) involved, and the transportation information (e.g. vessel, ports).
- For Working Capital Solutions products (i.e. payables and receivables programs), documentation received during the transaction life might be limited. In these case, KYT control might be compensated by reinforced control at program set up. These controls will be especially focused on the Supplier ("Know Your Supplier" [KYS] in case of payable deal) and the Debtor ("Know Your Debtor" [KYD] in case of receivable deal).

## THE CHALLENGES

- The Bank's ability to perform these controls is challenged by :
  - The significant amount of documents received for each transaction (assuming that all the elements available to the Bank should be controlled),
  - The multiplicity of events in a transaction life,
  - The large volume of transactions that the Bank needs to process (and on which the Trade business profitability relies).
- Therefore, the principal stake for the Bank is to achieve the maximum level of Compliance controls with the minimum business impacts. In fact, additional controls could increase the processing time, leading to a reduced volume of transactions processed; and additional resources to perform such controls could increase costs and reduce margins. However, the perspective of breaching Compliance rules – especially the US Financial Sanctions / Embargoes – is likely to be more difficult to bear, and drawbacks more difficult to overcome.

Figure 4 : Impacts on resources for a back-office processing 2 millions transactional events per year




*1 FTE (Full Time Employee) = 210 days

## OUR ANSWERS

- Taking into account these challenges, the Bank should be equipped with :
  - A filtering tool for Swift messages which :
    - Secures the exhaustiveness of information contained the message,
    - Enables a fluid and auditable workflow for "hits" processing,
  - A regular scanning of non-client corporate counterparties whose information is not contained in the Swift messages (incl. PEP for bribery control),
  - A tool to facilitate the control on documentation, Example : the Optical Character Recognition [OCR] tool brings together the scanning and the screening parts into one task.
  - A tool to enhance the controls on goods which are the most challenging since :
    - The control on nature of goods requires an analytical treatment,
    - Controls on goods need to be performed from Compliance, CSR and AML perspectives

    Note: Filtering and scanning tools enable to comply mainly with Financial Sanctions and Embargoes, names are screened against a set of lists for sensitive / sanctioned names and countries.

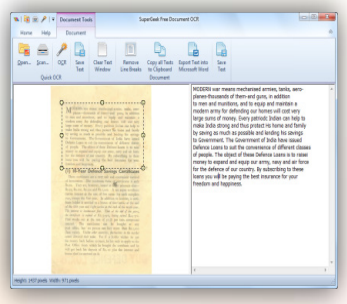

# Move toward Operational Excellence

# Reach best-in-class Compliance

How to secure a robust KYT process during a Trade transaction's life?

## DIGITAL OPPORTUNITY

- Enhance Swift messages data quality and relevancy
- BPM solution for F2B process orchestration
- E-Document management system, e-Signature, RAD/LAD to extract data from documents, etc.
- Robotic Process Automation to automate low value human steps (e.g. compliance checks, document filling, reporting)
- **Implement an OCR tool to enable optical recognition of handwritten or paper scanned documents**



- Application of "Internet of Things" [IoT] technology for Trade Finance.

  Provide a connectivity set up to « things » will be a driver to improve Compliance and operational processes. For instance :

  - **Connected vessel** to enable a real-time tracking and vetting control, and might provide an automated alert process in case of transshipment within a sensitive country
  - **Connected goods** to (1) secure the tracking between different storage locations, especially for Inventory Management financing, and (2) measure the storage environment quality (e.g. hydrometrics) for sanity purpose

# Move toward Operational Excellence

## **DIGITAL TRANSFORMATION** impacts on **OPERATIONS** excellence

### Possible actionable levers

Achieving operational excellence is a must-have for Banks willing to mitigate high pressure on its margins. Three categories of levers can be engaged:

1. **Operational efficiency**

The major axis to consider here is to what extent *alignment and standardisation of processes* can be pushed across sites and across products, and what level of task segregation can be achieved at each step of the processes.

Complementary to this, reflection around the *organisation* would be necessary to answer some key questions: e.g. Do we aim at a local, regional or global structure, do we need our operations to be delivered internally or externally, what is the level of specialization of staff required? Furthermore, *tools industrialisation and rationalisation* appear as a must have, as this will often be the prerequisite of the processes and organisation efficiency. This will mainly imply to promote core and standard solutions, with the intent to face systems obsolescence, to absorb increased volumes and to provide enhanced flexibility to both adapt to clients needs and fit security/compliance requirements.

## CASE STUDY - BANK A

**Objective***:* Achieve enhanced efficiency of Traditional Trade processes along with optimised organisation

**Context:**

- No standard tool able to manage guarantees worldwide: heterogeneous systems and processes preventing further industrialization and limiting reactivity to market shifts and regulatory constraints
- Obsolete, poorly featured set-up generating operational risk and preventing from absorbing strong volume growth
- Local sourcing and skills issue existing in a context of volume growth in the major region

**Achievements & Results:**

- Build and implementation of standard Guarantees tool to mitigate operational risk and improve service quality (eg. Syndication of Pan European Guarantees)
  - Reduce lack of interfaces
  - Automation of manual tasks (calculation of commissions)
  - New fronting capabilities
- Centralisation of Guarantees operations in Europe to absorb volume growth and face lack of resources. Dedicated pool able to handle administrative and expertise tasks
- Optimisation of Guarantees processes on main site and deployment in other regions in a second step
- Implementation of 2 platforms for processing 60% of global scope of documentary products, while maintaining local processes in smaller sites. Alignment of processes by product category for the main sites

## Possible actionable levers

### 2. Promotion of Digitisation: Towards an enhanced client experience

Digitisation stands out as a key driver towards operational excellence. It will mainly foster *automation of processes or tasks* through automatic matching / electronic document management (OCR, BPO) and improve Front to Back straight through processing capabilities through a complete digital workflow and enhanced functionalities, resulting in improved interfacing rates between applications, better turn around times and fewer mistakes.

As a second benefit, Digitisation can also help developing significant *business differentiation* through value added services, ranging from the scope of features delivered in eBanking (e.g.. extent and quality of user interfaces and portals, analytics an reporting modules) to the multi connectivity and offer customisation possibilities proposed by the Bank.

## CASE STUDY - BANK B

**Objective**: Push Digital capabilities to optimise operations and promote business differentiation

**Context:**

- Sustain mature and stable business in main countries and enhance commercial capabilities by offering an eBanking tool with new functionalities

**Achievements & Results:** Build and deployment of new fully featured eBanking tool

- Enhancement of user interface based on extended Digital platform
  - Administration and workflow capabilities with transaction status reporting
  - Widgets enabling quick overview of FX Rates, past deals, link to other platforms, sales message)
- Offering of new functionalities to clients
  - Enhanced reporting features: Possibility to send requests and raise advanced queries, customisable visual reports, for client or internal, compliance or regulatory purposes
  - Multi-connectivity: Interface with Corporates ERP (host to host), SWIFNET
  - Syndication capabilities
- Promotion of cross-selling via a single portal (FX and Trade bundles, potentially extendable to Cash and Deposits)
- Improvement of operational efficiency with FO to BO Straight Trough Processing with new interfaces between tools

## Possible actionable levers

### 3. Enhanced activity and performance monitoring

Beyond the efficiency of the processes, Trade Finance businesses have still room for improving its activity and performance monitoring. Indeed, manual or local reporting combined with multiple processes and systems make it difficult to produce a common aggregated vision of the business. In terms of *activity monitoring levers*, we can envisage to develop the level of granularity (by product, geography, client) and to improve the frequency and quality of the reporting in alignment with the decision-making processes. Here, the silver bullet would be to the ability to retrieve the full profitability per client for instance.

As for *performance monitoring,* improvement levers can cover following topics: Existence of a global operations SLA with defined indicators of service quality, KPIs to measure productivity of operations and sales as well as operating or credit risks…

## CASE STUDY - BANK C

**Objective***:* Ensure consolidated activity monitoring of for both Documentary Trade and Supply Chain Management products in order to feed governance and support decision-making process

**Context:**

- Activity monitoring performed at local level only, based on partial KPIs and using specific tools
- Absence of global consolidation of business activity figures, preventing any arbitration at global business line level

**Achievements & Results:**

- Build of consolidated activity report on activities, providing insights on business evolution with breakdown per product and regions
  - Number of transactions and principal amounts for Documentary Trade
  - Number of payable/receivable programs, entities and counterparties with associated principal amounts and margins for Supply Chain
- Ability to compare regional trends per category of product and prioritise investments at Trade Finance business line level
- Ability to better challenge need for developing or maintaining operating platforms / Back offices and to feed cost allocation process

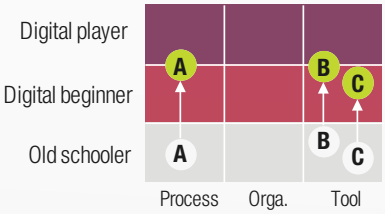
# How can Capgemini Consulting help you digitise your Trade Finance ?

« We can observe that, today, Compliance topics are acting as an accelerator for the digital transformation of banks »
**Global Trade Finance Director of a Major Global Bank, 2015**

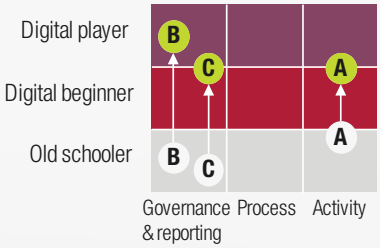
- Capgemini Consulting experts have built three matrices to assess your digital maturity, position you against your competitors, and identify the areas of improvement to achieve a significant digital shift.

The matrices are based on the 3 actionable levers identified previously :

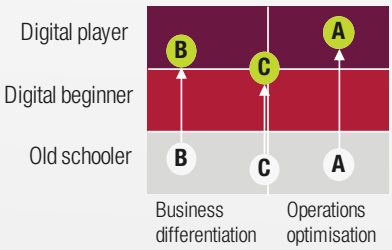
## Improvement of operational efficiency




## Enforcement of activity and performance monitoring




## Promotion of Digitisation




### Digital player

- High level of digitisation, automation, no manual treatments
- Alignment of systems and processes to business needs, systems equipped with intelligence layers
- Homogeneous practices on a large scope (organisation and geography)

### Digital beginner

- Processes partly digitised
- Homogeneous processes across a significant scope (organisation and geography) but remaining areas improvements

### Old schooler

- Lack of digital processes, significant manual inputs / re-treatments and paper-based communication
- Heterogeneous processes across the organisation

**Banks case studies**

- Target
- Initial situation


2.95%
4.78
4.82
1.54%
+0.60
+3.77%
4.94%
15.90
+0.20
+3.42%
4.15%
-0.10
-0.51%
1.03%
19.50
+0.05
+0.85%
1.68%
1.00%
2.02
-0.50
-1.43%
2.18%
-2.04%
1.39%

# Authors


**Yves C Bettan**

Vice President
CSS, United States
yves.bettan@capgemini.com

**Cécile André**

Vice President
Capgemini Consulting France
cecile.andre@capgemini.com

**Frederic Abecassis**

Vice President - Head of CC Hong Kong & Singapore, CC France
frederic.abecassis@capgemini.com

**Alain Swolfs**

Principal,
Capgemini Consulting Brussels
alain.swolfs@capgemini.com

**Gerrit Jan Haitsma Mulier**

Principal,
Capgemini Consulting Utrecht
gerritjan.haitsmamulier@capgemini.com

**Geoffroy Charpentier**

Principal
Capgemini Consulting France
geoffroy.charpentier@capgemini.com

**Lars Boeing**

Senior Manager
Capgemini Consulting Germany
lars.boeing@capgemini.com

**Edouard Mouton-Digard**

Manager
Capgemini Consulting France
edouard.mouton-digard@capgemini.com

**Gautier Durand**

Manager
Capgemini Consulting France
gautier.durand@capgemini.com

**Robert Ord**

Senior Consultant,
Consulting Services UK
robert.ord@capgemini.com

**Wassane Elhsissen**

Consultant
Capgemini Consulting France
wassane.el-hsissen@capgemini.com


Capgemini Consulting

**Capgemini Consulting is the global strategy and transformationconsulting organization of the Capgemini Group, specializing in advising and supporting enterprises in significant transformation, from innovative strategy to execution and with an unstinting focus on results. With the new digital economy creating significant disruptions and opportunities, our global team of over 3,600 talented individuals work with leading companies and governments to master Digital Transformation, drawing on our understanding of the digital economy and our leadership in business transformation and organizational change**

Find out more at: www.capgemini consulting.com

*Rightshore® is a trademark belonging to Capgemini*

**About Capgemini**

Now with 180,000 people in over 40 countries, Capgemini is one of the world's foremost providers of consulting, technology and outsourcing services. The Group reported 2014 global revenues of EUR 10.573 billion. Together with its clients, Capgemini creates and delivers business, technology and digital solutions that fit their needs, enabling them to achieve innovation and competitiveness. A deeply multicultural organization, Capgemini has developed its own way of working, the Collaborative Business ExperienceTM, and draws on Rightshore®, its worldwide delivery model.

Learn more about us at www.capgemini.com.

*Rightshore® is a trademark belonging to Capgemini*