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Corporates Look to Digital Solutions as COVID Disrupts Trade Finance in India

Q4 2020

Covid-19, a tragic event that has upended our lives and caused unprecedented and perhaps irreversible damage to the global economy, continues to shape the narrative for the future of trade and commerce. The World Trade Organization (WTO) estimates that world merchandise trade could decline by between 13% and 32% in 2020, a much steeper drop than the 9% contraction observed at the height of the 2008–2009 global financial crisis. This, in turn, has affected the trade finance sector, with banks having to contend with not only operational continuity challenges but also newer risks relating to letters of credit and invoice-discounting transactions.

The Depth of Disruption

Now that two quarters have passed since the pandemic began, corporates are better positioned to assess its impact on current and future operations. Certain sectors, especially those that rely heavily on global supply chains, have been deeply impacted.

As a pharmaceutical company, we are seeing an increase in the number of contracts we are getting. Coupled with the fact that we are well stocked, the impact on us has been fairly positive. However, this might not be long lasting, as we [expect] the prices of raw materials will increase.

- India pharmaceuticals company

Since the lockdown, there is no movement and, thus, no demand for transport. Demand for our crude oil has fallen. In addition, our supply chain has been drastically affected due to a decrease in manpower.

- India oil & gas company

Overall, exports year-to-date have seen a decline, albeit, growth in recent months has improved substantially, with both September and October showing increases. CRISIL tracks exports in a number of sectors, including nearly 20 key segments that account for 45–50% of total merchandise exports. Merchandise exports make up nearly 65% of India's total exports, while services exports that account for 30–35% are dominated by the IT and ITES sector. Indian services industries have clearly been resilient, registering flattish growth in the first half of fiscal 2021. However, merchandise exports have been hit substantially, but recovery trends have been varied.

Specific sectors like pharmaceuticals, specialty chemicals and agro chemicals have been resilient, growing at 14%, 5–7% and 4%, respectively. On the other hand, ready-made garment (RMG) exports have seen a year-to-date decline in H1 of up to 30%, while cotton yarn has seen a sharp uptick in exports from countries like Vietnam and Bangladesh, in anticipation of a pick-up in orders for RMG during the festive season.

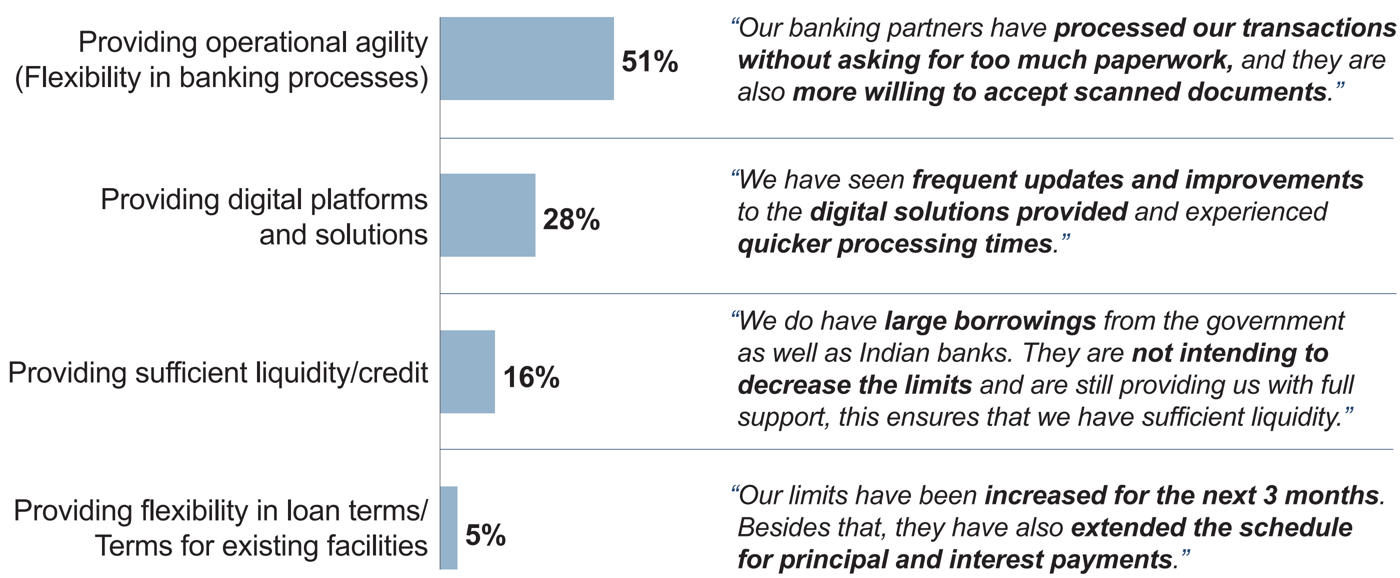
A second wave of COVID cases in the U.S. and Europe are fading hopes of an early recovery, however, and the sustainability of cotton yarn exports is a concern. Agriculture-linked sectors like sugar and rice, and non-agricultural commodities like steel and aluminum have also seen a unique pick-up in exports in the second quarter of the year. Diversification from China is supporting non-agri commodity exports, while shortages of food products in many ASEAN countries along with favorable government policies are supporting agri commodities exports. But other value-added segments like autos and engineering products continue to remain a drag for exports.

The ramifications of the pandemic on international trade have been fairly diverse. Inarguably, the pandemic has led to severe supply-chain disruptions due to lockdown measures, industrial shutdowns and the resulting delays in shipping and transport. The vast and diverse world of international trade and finance largely relies on the physical exchange of paper documents to function seamlessly. However, due to the constraints on physical mobility and the consequent logistical issues, the disruption felt in this segment of international finance has been acute.

The Changing Landscape of Global Trade Finance

In the backdrop of a challenging business and trade environment, corporates turned to their banking providers for critical support. Their "ask" has significantly changed, with requirements related to operational agility and digital solutions now taking precedence over liquidity needs or flexibility in lending terms. According to the Greenwich Associates 2020 Global Large Corporate Trade Finance Study, 51% of the respondents prioritized "providing operational agility" (flexibility in banking processes), while 28% valued access to digital platforms and solutions.

How Banks Have Helped Mitigate the Impact of COVID-19



Note: Based on 123 responses from March to June 2020.
Source: Greenwich Associates 2020 Global Large Corporate Trade Finance Study

Banks that Were Distinctive in Helping Mitigate the Impact of COVID-19

TOP 3 LOCAL BANKS	TOP 3 FOREIGN BANKS
Axis Bank HDFC Bank State Bank of India	Citi HSBC Standard Chartered Bank

Note: Based on 123 respondents.
Source: Greenwich Associates 2020 Global Large Corporate Trade Finance Study

The future of trade finance will hinge on how corporates orchestrate their global supply chains in an attempt to achieve operational resilience. To successfully implement long-term improvements and build more robust supply chains, corporates are likely to focus on the following:

- Ensure the end-to-end digitization of their supply chains
- Demand better visibility through real-time data on inventory, supply and demand
- Reduce the turnaround time in fulfilling financing/operational needs across the supply chains

To achieve this, corporates are again likely to turn to their banking partners to fulfill their needs for innovative and agile trade finance solutions that can adapt and connect to such new digital approaches. Thus, the current environment presents a unique opportunity for banks to embrace digitization and help their clients navigate the new normal. Our data shows that significant ROI can accrue to those banks that support their clients during periods of crisis.

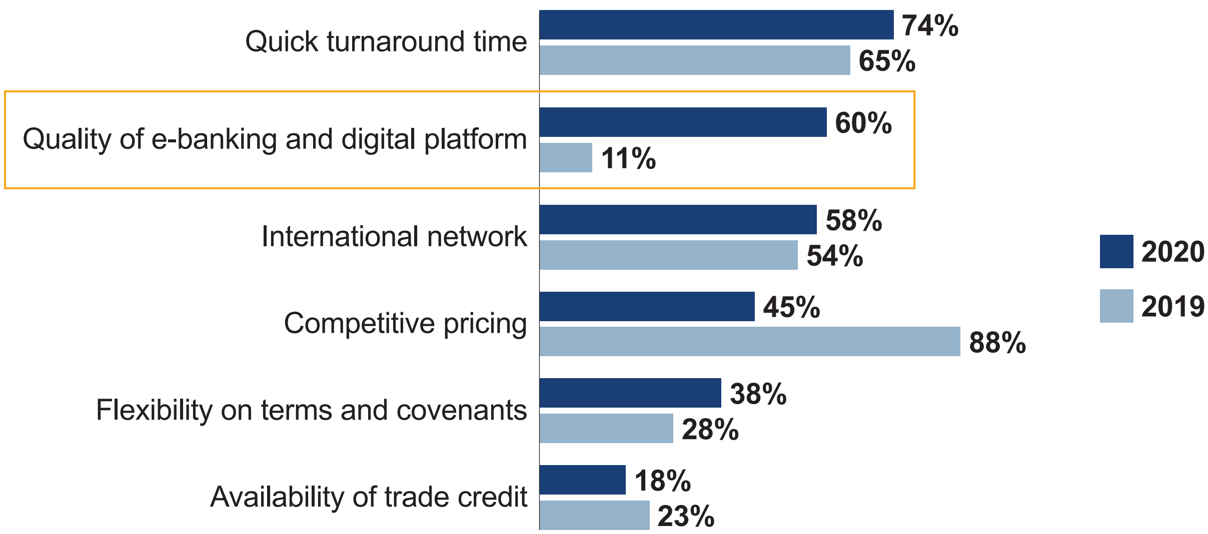
Banks to Provide a Digital Antidote

Digital capabilities are now taking center stage, as corporates accelerate their use of electronic channels. In the trade finance business, physical transactions, i.e., the actual exchange of paper, can potentially become less prevalent, as providers gravitate toward digitization. While this shift is certainly in response to the current crisis, it is likely to extend beyond the crisis as well. Once the threat of the pandemic begins to dwindle, end-to-end supply chain visibility and digital interoperability will become much higher priorities for corporates.

This, in turn, will compel banks to evaluate their digitization strategy and accelerate the digital transformation of trade finance. International trade finance is currently on the cusp of a digital transformation—one that can be proactively led by both regulators and corporates, along with their banking partners.

With corporates increasingly adopting digital solutions to interact with their customers and seamlessly deliver services, they will inevitably demand a similar level of digitization from their banks and other service providers. In addition to competitive pricing, the quality of e-banking and digital platform is becoming a relevant assessment metric for corporates. The results of our recent study clearly exemplify this shift. In 2019, 88% of respondents ranked “competitive pricing” as a key criterion for trade provider selection, while only 11% considered quality of e-banking and digital platform a relevant metric. However, in 2020, we observed a sharp shift toward digital solutions, with 60% of the respondents ranking digitization as a critical metric for evaluating a trade provider.

Key Selection Criteria for Trade Finance Providers



Note: Based on 123 respondents.
Source: Greenwich Associates 2020 Global Large Corporate Trade Finance Study

As corporates increasingly gravitate toward building digital supply chains, there are certain factors that can help banks build a distinctive digital supply chain solution. These include:

- **End-to-end solution:** The aim should be to provide a holistic experience to the corporate and offer a suite of services and products that can meet their myriad needs. Further, it would be beneficial to create multi-way channels and collaborate with fintech/techfin players in the ecosystem in order to deliver a seamless experience to the client.
- **Automated processing:** The two attributes above should be augmented by automation in payment settlements, financing applications, etc. Automation will help reduce the financing cycles and enable faster and more efficient delivery of services.
- **Ease of use:** Banks should focus on creating intuitive and user-friendly solutions that are easily accessible. User experience really has come to the fore in terms of driving engagement.

Looking Ahead

The global supply chain landscape is changing, with corporates across the world reassessing their supply chains and repositioning for the "new normal." In tandem, trade finance is shifting shape, aided by digital interventions and the changing needs of the corporates. The deep transformation in global trade and commerce that is currently underway will require banks to increase their digitalization efforts and make end-to-end connectivity a reality. The prevailing environment affords banks the opportunity to assess their current digitization drive, identify the gaps, and rethink and redesign for the future.

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