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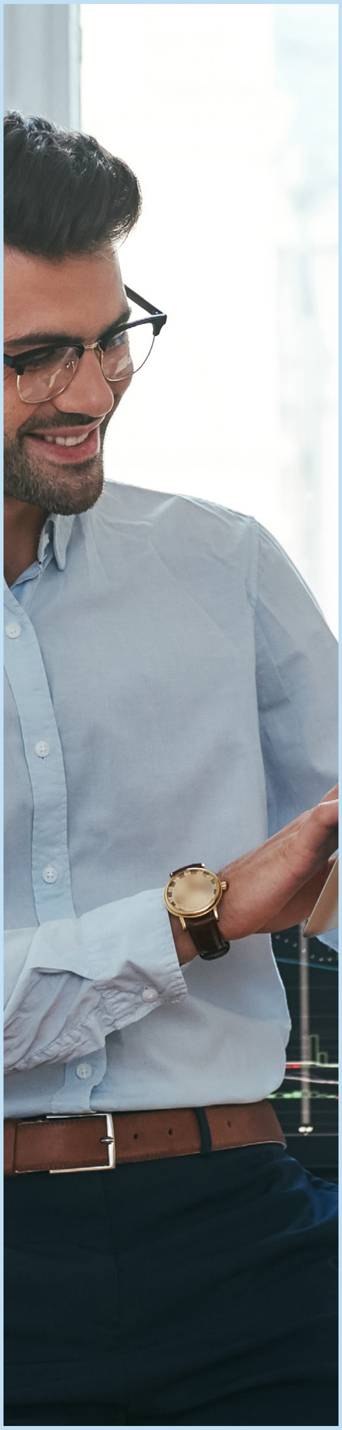

TRADE FINANCE IN THE DIGITAL ERA: WILL BANKS RISE OR FALL TO FINTECH DISRUPTION?

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Trade finance and supply chain management are the lifeblood of businesses and represent a significant revenue stream for large banks. The top three U.S. banks serve just about 35% of large American companies, and the global trade finance market is projected to grow at a CAGR of 7.5% through 2030 – representing a significant opportunity for growth. Banks that fail to act quickly risk forgoing billions in untapped market potential.

Despite their importance, trade finance and supply chain management often lag in digital transformation compared to other banking services like payments and lending. The sector faces significant challenges, including heavy reliance on paper, a lack of standardization and outdated legacy systems. Limited digitalization in supply chain finance further intensifies these issues. Large corporate clients are increasingly adopting integrated systems to manage invoices and payments, but many U.S. banks have struggled to keep pace, leading to a fragmented and incomplete experience. The absence of automation has resulted in greater inefficiencies, heightened operational risks, and reduced profitability. This has created a fertile ground for fintechs to not only develop modern technology solutions, but to shift business away from traditional banks, paving the way for innovative working models.

Why is trade and supply chain still predominantly manual and riddled with legacy?

Despite being one of the pillars of the overall working capital solutions banks offer to clients, this sector remains one of the most encumbered by outdated practices and technologies. In some cases, transaction origination alone consumes up to 60% of total processing time, making it one of the least automated functions in wholesale banking. This burden directly impacts service levels, leaving small and medium-sized enterprises (SMEs) particularly dissatisfied. The low service levels and overall lack of sophistication have forced businesses to consider moving relationships either to other banks or the new emerging class of fintechs, a trend we are seeing distinctly in the market.

On the other hand, banks face considerable challenges in their modernization efforts:

Legacy technology:

Antiquated systems, limited standardization and a lack of seamless integration lead to operational inefficiencies. Processes remain heavily reliant on manual documentation, customized code on old technology and limited knowhow thereof. All these factors have hindered speed and agility of transformation.

Shifting trade patterns:

In North America, open accounts dominate most of international trade transactions, causing a huge shift from earlier days. This has somewhat weakened the business case for transformational investments in trade solutions.

High-risk environment:

Trade finance in particular is inherently exposed to risks around local regulations, foreign exchange exposure, trade complexities, sanctions, KYC and money laundering. The need for stringent compliance adds to the operational burden and caution. A United Nations report found that trade-based money laundering accounts for 87% of all illicit financial flow worldwide. Risk monitoring and compliance systems built around trade products are expensive and difficult to re-engineer. This is one reason why banks worldwide have shied away from changing what was established and working, albeit inefficiently.

COTS product limitations:

Many banks rely on inflexible commercial-off-the-shelf (COTS) products which restrict their ability to keep pace with technological advancements.

AI mirage:

While AI offers immense potential for automating processes and mitigating risks, its implementation in trade finance is heavily dependent on COTS product vendors, slowing down innovation. Much of this implementation depends on third-party software vendors, limiting banks' capacity for independent innovation

Opportunity for fintechs

Despite these challenges, the need for "financing of trade" is not going away. The global trade finance gap reached an estimated $2.5 trillion in 2022, up from $1.7 trillion in 2020. The rising demand highlights a growing gap in accessible financing, including local supply chain. Hence, banks have a strong case to invest in modernizing these systems. But this has created a lucrative opportunity for fintechs, both on the technology side as well as on the financing side. With seamless connectivity and microservices-based product architecture that makes modular or piecemeal replacement of legacy products easy, fintechs are enabling banks to modernize their legacy technology environment one small step at a time. Additionally, through offering innovative financing models and streamlined agile financing processes, fintechs are steering business away from banks.

Businesses, both small and large, see this change as a breath of fresh air. It creates a sense of urgency within banks and, more importantly, moves the conversation to the forefront. Fintechs have delivered personalized financing solutions that surpass traditional banks, offering lower costs through reduced overheads and technology-driven efficiencies while ensuring a smooth customer experience from onboarding to funding and servicing.

Platforms like Traydstream simplify international trade by enabling digital customs submissions. Several startups now offer banks a solution to integrate with business platforms, giving direct access to accounts payables and receivables data. More advanced solutions enable buyers to offer their suppliers early payment options, and fintechs facilitate this payment by providing the necessary liquidity.

There are more examples from some fintechs focusing on improving the supplier onboarding process, with others helping banks distribute assets, as in the example above, or managing KYC and sanctions in a more simplified way. All of this has reduced risk for banks and accelerates processing, providing businesses with a smoother trade experience and better working capital solutions. The emergence of crowdfunding is further challenging traditional banking models. While crowdfunding is not directly mentioned in the context of supply chain finance yet, some fintechs are experimenting, using similar principles to democratize access to working capital, offering greater flexibility and leveraging data for smart decision-making.

Ravi Akula, Co-founder and CEO of Digiwins, an early stage fintech start-up in this space, states: "In a complementary role to banks' own technology, platforms like ours provide AI-powered tools to simplify trade finance by digitizing and automating traditional (manual) processes, minimizing manual intervention, accelerating transaction processing, and enhancing accuracy.

We have created a modern AI-driven, multi-banking exchange for supporting supply chain finance transactions, almost like an ecosystem with pre-defined rules that enables distribution of assets to participating financial institutions. It's a win-win for all, buyers and suppliers are able to manage their working capital with more efficiency, banks participate depending on their risk appetite for each transaction."

– Ravi Akula,
Co-founder & CEO, DigiWins Technologies Inc.

What does this mean for banks?

Do banks risk delegating the majority of the supply chain finance process to fintechs? It's unlikely.

Firstly, trade finance transactions, such as letters of credit and bank guarantees, serve the critical function of providing "surety," which relies heavily on banks' established credit standing — something that's challenging for fintechs to replicate. Additionally, in supply chain finance, while fintechs have successfully partnered with banks to deliver technological advancements, banks still remain a crucial part of the broader ecosystem which fintechs help create in most cases through participations.

But it's clear that a new type of player has emerged in this space — a small, agile, tech-savvy outfit with deep domain expertise and the flexibility banks often lack. Meanwhile, corporate treasury technology is advancing rapidly, driving banks to modernize under increasing pressure from clients. Failure to adapt could result in banks losing control of the supply chain finance ecosystem.


Dice Roll Probability Lab

The path forward: embracing collaboration and innovation

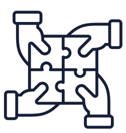
The future of trade finance supply chain hangs in the balance. To seize the digital opportunity and retain their position in the ecosystem, banks must:

Prioritize digital transformation:

Elevate trade finance to a strategic priority – at least for products that matter e.g. open accounts, letters of credit. Explore a piecemeal approach to modernization. Allocate sufficient resources and investment.

Enhance supply chain integration:

Develop solutions that seamlessly integrate with corporate clients' existing software systems, facilitating efficient and transparent supply chain financing.



Embrace collaboration:

Forge partnerships with fintechs and technology providers to access innovative solutions and expertise. Join the ecosystem, but only after a careful evaluation of risks such as cyber threats and after ensuring the solutions meet the needs of the clients you are trying to service.

Focus on AI and automation:

New AI use cases emerge every day. Leverage AI to reduce manual workloads, enhance fraud detection, and simplify compliance, enabling faster and more efficient transactions.

Data-driven insights:

Leverage data analytics to offer businesses valuable insights into their supply chains, leading to better decision-making. Supply chains ecosystems are rife with data that mostly goes unutilized. Find a way to use that to your advantage.

Enhanced user experience:

With a focus on user-friendliness, create intuitive interfaces that greatly enhance the supply chain financing experience for businesses of all sizes.

Conclusion

The potential benefits of digitizing trade finance are substantial. According to McKinsey, such efforts could yield annual cost savings of $8-10 billion. A report by the Boston Consulting Group (BCG) for the International Chamber of Commerce (ICC) suggests that integrating digital solutions could save global trade banks between $2.5 billion and $6 billion annually, based on a cost base of $12 billion to $16 billion. Moreover, a full digital transformation could potentially increase trade revenues by up to 20% while cutting processing times by 60%. In one instance, over 50% of DBS's documentary trade transactions are now digitally initiated.

The advantages of digitized trade finance extend beyond individual banks. A transition to paperless trade could drive $267 billion in additional exports for G7 economies, showcasing the global economic impact of modernization. These figures underscore the transformative potential of digitalization in trade finance and highlight the urgency for banks to modernize their operations to remain competitive.

The future of trade finance is at a crossroads. By prioritizing innovation and fostering fintech partnerships, banks can reclaim their competitive edge and thrive in an evolving global trade ecosystem. The time for action is now—those who adapt will lead the way into a new era of opportunity.

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Ajay Bhandari is Senior Vice President and Regional Head of Financial Services for North America at Infosys, with over 30 years of experience driving innovation and transformation in the financial services industry. Over the past decade, he has delivered impactful solutions that enhance customer experiences and create value for clients.

A trusted leader, Ajay collaborates across ecosystems to champion innovative strategies that optimize business models, operations, and technology, shaping the future of financial services.

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