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A new dawn for trade finance

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How time flies: with the release of the first 2018 FI.News, we now find ourselves a full decade on from the global financial crisis. But if the years since 2008 have shown us anything, it is that the recovery in world trade growth has a long way to go yet.

I firmly believe that we, at Commerzbank, are well equipped to support this recovery, however – and help lead trade into a new dawn. Not only are we a bank with trade in our DNA and 150 years’ experience under our belt; our targeted approach to innovation is also vital for supporting our corporate and FI clients through challenging times, as Ludger Janssen and Ruediger Geis explain.

That is why this issue of FI.News is all about paving the way for the future. Angela Koll and Gerhard Schipp offer their views on how evolving technology can transform trade and supply chain finance. Ingrid Weisskopf explores the impact of new developments in the payments sector. Ruediger Geis tells us how updates at SWIFT will affect the industry. And Enno-Burghard Weitzel emphasises the need to invest in this future, in a video interview with The Banker.

It is not just the trade finance industry that is looking to the future. In our spotlight features on the world’s emerging markets, Alexander Mondorf explains how Pakistan is increasingly integrating into the global economy, Christian Toben navigates Southern Africa, while Hans Krohn reports from Uzbekistan on the country’s newfound optimism. Commerzbank will be closely supporting such positive developments through its facilitation of trade. Our activity worldwide, of course, is built on our strong, strategic partnerships with financial institutions. Take a look at how our close work with Kapitalbank helps our clients take advantage of new opportunities in Uzbekistan.

As usual, the newsletter provides a holistic overview of the news, events and updates in the Commerzbank world.

On a more personal note, it is a particular pleasure to welcome you to my very first FI.News as Divisional Board Member.

Enjoy the issue.

Nikolaus Giesbert
Divisional Board Member
Fixed Income, Currencies
& Commodities
Trade Finance &
Cash Management
Commerzbank
What's hot in trade?

FI News asks Commerzbank’s experts for their take on current developments

A decade on from the global financial crisis, trade is still to make a full recovery. According to the World Trade Organization (WTO), trade growth in 2018 is likely to be a modest 3.2%. In such an environment, commerce needs the full support of both banks and regulators.

Ruediger Geis, Head of Trade Affairs at Commerzbank, is confident that things are moving in the right direction. “An encouraging trend seems to be that regulatory authorities, as well as trying to ‘protect’ their countries against fraud, are now also increasingly trying to ‘promote’ them for trade – just look at the ongoing cooperation between Hong Kong and Singapore. It’s a positive message, and one that banks should support.”

Looking for innovation

Given the compliance demand, Geis believes banks have to innovate. “As authorities look to us as the first line of defence against criminal money flows, we have to explore the automation of KYC and other compliance processes. With it, we could process more checks with more efficiency; without it, there could be rises in costs or, worse, the risk of missing something important in a trade transaction.”

There are exciting proposals on the horizon. Research from McKinsey, for example, estimates that increased uptake of the Legal Entity Identifier (LEI) code alone could lead to cost savings of up to $500 million for the trade community in the KYC arena.

The holy trinity of facilitating trade

Yet innovation remains a work in progress. Ludger Janssen, Commerzbank’s Head of Product Management Trade, explains: “Our work in trade finance ultimately rests on three pillars: not only digitalisation, but also regulation and the wider economic impact. As a trade bank, we need to take each of these into account – all the while ensuring that we meet the needs of our clients. That means any innovative project should have a business case; it has to be able to tackle existing market and sector-specific challenges. It must also be able to satisfy the regulatory demands of the jurisdictions in which our clients work – in turn requiring a joint effort when it comes to agreeing and setting legal standards.”

Geis agrees. “When it comes to innovation in the trade industry, there is likely to be a certain hybrid model. Over the next few years, we need to prepare for some documents in an electronic format, and some remaining in paper.”

Innovation in trade will doubtless continue to be a major topic in the years to come. With a targeted and analytical approach, banks can help trade continue on its recovery.”
Uzbekistan is a newly shining light in Central Asia. At the end of 2016, President Shavkat Mirziyoyev’s new government took power. Under a wide-ranging programme of reforms, the government has sought to decentralise and deregulate the economy, make markets more efficient, and entice foreign investment – all designed to raise the country into the World Bank’s “upper-middle income country” bracket by 2030. Uzbekistan could be well on its way to achieving this: last year, GDP grew by an impressive 6%.

This has accompanied a significant improvement in relations with the outside world. President Mirziyoyev has just completed a state visit to neighbouring Tajikistan, while the country has seen the establishment of four new free economic zones (building on the existing three).

A break from the past
This is not the Uzbekistan of old. Until two years ago, the country had one of the world’s most closed and tightly controlled economies. A major trigger for change was the liberalisation of Uzbekistan’s exchange rate. With the restrictive currency regime now lifted, the Uzbek som is floating freely. Needless to say, a controlled currency can foster the development of a black market and a grey market, resulting in huge differences between official and unofficial exchange rates. Any sudden liberalisation, therefore, can be a shock to the financial system.

According to Hans Krohn, Regional Head, Financial Institutions Russia & CIS at Commerzbank, however, the Uzbek government worked hard for a smooth transition: “The liberalisation of the som was played out in stages, in order to mitigate disruption. The government first announced its plans to move in a liberalising direction. Then they did a ‘field test’ – nominating a number of banks that were allowed to trade hard currencies. This meant they were able to check how the market reacted and how the banks would cope.”

The financial system has since proven resilient. The central bank increased the reference rate to discourage lending, in order to help banks build a liquidity cushion for any possible economic shocks. “I was in Uzbekistan when all this was being talked about,” recalls Krohn. “Many in the market felt this was long overdue. At the time, there was a mixture of nervousness and great expectation.”

Moving on up
Half a year later, Krohn identifies positive trends: “Now that the overvaluation of the currency is a thing of the past, we are seeing a definite increase in both economic activity and international trade. Exports are up and imports into the country are on the rise. We’re also seeing a growing demand for trade financing – be that short- or long-term.”

At a glance: Uzbekistan

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<th>Capital: Tashkent</th>
<th>Population: 32.2 million</th>
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<td>Currency: Som</td>
<td>GDP growth, 2017: 6%</td>
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<td>GDP composition:</td>
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<td>Agriculture: 18.5%</td>
<td>Industry: 34.4%</td>
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<td>Industry: 34.4%</td>
<td>Services: 47%</td>
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<td>Major exports</td>
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<td>Cotton</td>
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Export partners
- China
- Russia
- Kazakhstan
- Turkey
- Bangladesh
- Afghanistan
- Switzerland

Import partners
- China
- Russia
- South Korea
- Kazakhstan
- Turkey
- Germany
Trade, in fact, is a top priority of the government, which seeks to increase the country’s ability to export and move it up the value creation chain. Uzbekistan is highly dependent on commodity exports. As the world’s seventh-largest cotton producer, for example, and its fifth-biggest exporter, it relies on its “white gold” for a considerable share of revenues and foreign exchange. But pressure is building to export more in the form of textiles or finished garments, instead of the raw material, in order to better weather price fluctuations on international markets.

The new-found exporting potential also extends to higher-value industries. “Uzbekistan is actually a car producer,” notes Krohn. “Originally, its cars were mainly destined for other Central Asian countries, as well as the domestic market (Uzbekistan has the most densely populated market in the region). But the economic crisis in Russia over the past few years has had the effect of making Uzbek cars more attractive in this much larger market – so where there’s already expertise, there is also greater potential for this industry.”

Engaging with Uzbekistan

Of course, weaknesses remain. There is still high state influence in business, persistent (though improving) regulatory uncertainty, and bureaucratic obstacles. Transparency is, as yet, rather insufficient, and there remains the threat of corruption. Yet Krohn is impressed with the positive steps the country is taking: “For many years, development was below the country’s potential. Now, for the first time in living memory, we see a chance that this potential can actually be realised.”

This seems to be a view shared by many in the Western banking industry. “At Commerzbank, we’ve been doing business in Uzbekistan for many years, supported by our representative office on the ground in Tashkent. But now, we’re seeing new delegations of foreign bankers coming to the country every couple of weeks!” says Krohn.

Importantly for commerce, the European Bank for Reconstruction and Development (EBRD) is in the process of setting up shop again in Tashkent. After a hiatus of several years, establishing its operations in the country means a return of the important Trade Facilitation Programme (TFP). Though foreign trading companies may be keen to do business with the country, they could be unfamiliar with local counterparties. Banks’ credit lines, meanwhile, can be a limiting factor; increasing line capacities is a gradual process and must account for risk. This is where the TFP steps in – undertaking part of the risk of trade finance operations.

“Commerzbank has a very long history of working as a close partner of the EBRD,” comments Krohn. “While we benefit from the EBRD’s guarantees, we in turn bring to the table our large network of correspondent banks. For many years, we’ve been the most active confirming bank under the TFP. It’s a fruitful partnership: we facilitate more trade, the EBRD fulfils its mandate, and – of course - it’s good for Uzbekistan’s prosperity.”

Uzbekistan seems at last to be opening up to the world – and its foreign partners have high hopes for success.
A reliable partnership for changing times

Fl. News sees strong partnership between Commerzbank and Kapitalbank

Uzbekistan’s economy is undergoing a period of important evolution (read the report from Hans Krohn on page 4). Witnessing the changes at first hand has been Sherzod Karimbaev, Deputy Chairman of the Board of JSCB Kapitalbank: “Since the President’s reforms to liberalise the country’s foreign exchange policy, the investment attractiveness of our economy has increased. Systematic work is now underway to make the transition from an import substitution model to one of export-oriented development.”

The need for trade finance

In such an environment, the outlook for Uzbekistan’s trade finance sector is positive. “Trade finance is a huge driver of economic development and a key factor in assuring the competitiveness and efficiency of world trade,” notes Karimbaev. “Providing financial support, we can help small businesses create new jobs, as well as increase firms’ productivity, profitability and growth. Significantly, with longer maturities, we can help our corporate clients rise up the value chain. This will be vital for importing the higher-quality machinery and capital goods that an expanding Uzbek economy needs.”

The “Made in Germany” label has a powerful appeal here. As Dr Bodo Thoens, Commerzbank’s Senior Representative in Tashkent explains: “Germany is already one of Uzbekistan’s most reliable trade partners; bilateral relations benefit from close economic and investment cooperation. Uzbekistan is home to world-class German companies, and fruitful and constructive investment has seen cooperation on large-scale projects in the country.”

The roots of successful partnership

Cross-border trade, of course, is where partnership with global banks can help. “As interest to conduct business in Uzbekistan grows, cooperation with international financial institutions is actively developing,” Karimbaev says.

Kapitalbank, however, can already count on a history of successful partnership with Commerzbank, stretching back to 2004. According to Karimbaev: “Commerzbank’s euro clearing services give us a real competitive advantage; we especially value their prompt execution of orders through their wide branch and correspondent network, which simplifies the flow of payments. Commerzbank is also our main partner for trade finance operations. With its help – and in an economy moving in a positive direction - we can look forward to larger transactions and longer tenors. We know their team in Tashkent well, and can always count on them to deal swiftly with any problem.

In brief: Kapitalbank

Originally established in 2001, JSCB Kapitalbank is a private joint-stock commercial bank, and among the 10 largest financial institutions in Uzbekistan.

With more than 10,000 corporate clients and over 2 million retail customers, the Bank offers a wide range of products and services, including interbank transactions, corporate and retail lending, savings and account servicing, foreign exchange transactions, and investment banking.

Headquartered in Tashkent, Kapitalbank maintains 14 branches and 17 mini-banks around the country.
no matter the size. So it’s a partnership built on reliability and trust.”

Thoens, too, is optimistic for the relationship. “Kapitalbank is a market leader among Uzbekistan’s private banks – and we’re very pleased to accompany its success. Their broad customer base aligns very well with our own business: entrepreneurial SMEs in the country, for instance, depend on the international trade finance we can facilitate. While our local market expertise has already allowed us to build a close relationship with Kapitalbank, as the business environment becomes friendlier, we look forward to enhancing this cooperation. We know it will remain a reliable partner.”

Navigating an evolving financial sector

Such strong partnership will be of great importance to Kapitalbank in a rapidly changing financial sector. Karimbaev comments: “Digitalisation is fast changing our customers’ preferences and decision-making. They depend on round-the-clock access to technology-driven banking services from anywhere in the world, and demand more integration of these services into their day-to-day operations.”

Karimbaev continues: “The development of insurance, securities and non-banking financial players is accelerating. As non-bank organisations enter the market – making serious investment in technology and with a lower regulatory burden than banks – competition is intensifying. The banking system is also busy making the transition to the Basel III standard. As regulatory requirements become tougher, banks will need to account for higher costs for compliance control, personal data protection, and the prevention of questionable transactions.”

Uzbekistan’s banks must work to meet changing customer needs and maintain market share. Reliable partnerships could give them the competitive advantages they need to adapt to new conditions.

“...strong partnership will be of great importance in a rapidly changing financial sector...”

Sherzod Karimbaev
Deputy Chairman of the Board
JSCB Kapitalbank

with

Dr Bodo Thoens
Senior Representative
Financial Institutions
Commerzbank
Marco Polo charts a new course for trade finance

Commerzbank forms part of a core group of banks to pilot the blockchain project

Marco Polo is a new trade finance project developing a global platform based on distributed ledger technology (DLT). Having successfully demonstrated a proof of concept, Commerzbank – along with other leading global banks, trade finance technology specialist TradeIX and enterprise software firm R3 – embarked on the pilot phase of the initiative in February 2018.

Powered by TradeIX’s TiX platform and R3’s Corda blockchain technology, Marco Polo enables end-to-end, real-time, seamless connectivity between trade participants, eliminating the data silos which prevent the free flow of information and cause inefficiencies and discrepancies.

Since launching in September 2017, Marco Polo has attracted significant interest from the global banking community. The core banks are BNP Paribas, Commerzbank and ING, with additional banks including Standard Chartered, DNB, and OP Financial Group having joined in recent months.

“We are one of the first three banks to successfully perform the proof-of-concept acceptance tests, which is a major achievement for us,” commented Nikolaus Giesbert, Divisional Board Member, Fixed Income, Currencies & Commodities and Trade Finance & Cash Management. “We are pleased with how far the development has come in such a short time span. Together, we have proven that blockchain technology will make trade finance faster and more transparent for all participants.”

Marco Polo’s participants aim to expand the initiative in 2018 to include additional banks and third-party service providers, such as ERP and logistics providers and credit insurers, leveraging the collaborative nature of the platform to create a fully interoperable open-sourced trade finance network.

Leading euro services provider

2018 is six years on the trot with FImetrix

FImetrix, the market research firm for financial institutions, has identified Commerzbank as a “Distinguished Provider” of transaction services denominated in euros. One of only four global designees, the Bank has consistently won the accolade for the past six years. FImetrix conducted interviews with senior-level executives at 563 of the largest banks in 85 countries across five global regions active in cross-border cash and trade. Respondents were surveyed on providers’ operational efficiency, customer service, technology, product range, and staff skills.

SWIFT updates

Are you prepared for the standards release?

SWIFT is updating its trade finance messaging system, replacing older message formats with more modern, structured standards. November 2018 and November 2019 will see a raft of changes to the interface and messages for letters of credit and guarantees.

Don’t get caught out: speak to your relationship manager, and find out more here from Ruediger Geis.
Commerzbank releases major new BPO white paper

Publication assesses the outlook for the trade instrument

In Commerzbank’s new white paper, *Leading the path of digital evolution*, Angela Koll, Specialist Trade & Supply Chain Finance, describes how the Bank Payment Obligation (BPO) works, sets out the benefits the instrument offers to both banks and corporates, and argues that increased market adoption could help spur the digitisation of trade.

The white paper is published with the approval of SWIFT, and includes insights from the International Chamber of Commerce (ICC) Banking Commission, OPUS Advisory Services International and JP Morgan Chase.

Continued cash and trade success

*Global Finance* magazine picks out Commerzbank for its leading services

For the second year running, leading magazine *Global Finance* has given Commerzbank the title of “Best Bank for Trade Finance in Germany”, as well as the award for “Best Treasury & Cash Management Provider” for the third time in a row.

Enno-Burghard Weitzel, Head of Product Management Trade Services, remarks: “We are naturally honoured to be recognised – yet again – for our commitment to the home market. It’s true that no bank opens more letters of credit in favour of German exporters than Commerzbank. But this award does not just reflect our market-leading position in the country. It also builds on the hard work of our trade teams that serve day in, day out as close partners of our clients – whether that is through optimising their supply chains worldwide, navigating global risk on their behalf, or driving forward the digital evolution of the trade finance industry.”

Klaus-Josef Mueller, Head of Product Management, Trade Finance & Cash Management, adds: “This reflects our dedication to helping our growing corporate customers in Germany to reach their operational potential. Clients now expect high-end products and services from their banks to be cloud-based, driven by apps, and digitally secure – and we’re the ones raising the bar.”

*Global Finance’s* awards have picked out the best providers in global cash and trade services for nearly two decades.
In a nutshell, what’s going on?

Ruediger Geis: SWIFT is updating the format of its trade finance messages. The series of updates is called the “Standards MT Release” and it is taking place in two steps in November 2018 and November 2019. Affecting the messages known as “Category 7”, it represents the most significant set of changes to the trade finance messaging interface in 30 years.

What systems will be affected?

RG: Not only will the new standards release mean IT systems have to account for technical changes, but it will also have an impact on the business side of the trade industry, as both banks and corporates will have to make adjustments to their operational processes.

This means that at Commerzbank, for example, all our digital trade finance offerings – including our web-based trade services – will be directly affected. With new characters coming up we also have to make sure that these can be recognised and processed in our compliance tools and payment systems. Otherwise we might have a significant increase in false positives or non STP. We are currently hard at work to ensure the smooth-running for our clients of other, related systems that may be indirectly affected too.

Guide us through some of the changes – what advantages will they bring?

RG: The changes are truly significant – and many are highly complex. In some areas, they will mean completely new messages types, such as the

more structured MT 759 (which should reduce the use of MT 799). In other areas, we will see a considerable enhancement of the maximum size for messages that determine trade finance issuance, amendments and advice. The format MT700/701, for instance, currently has space for three extension messages – but the new system will allow nine.

Another major update governs the use of free text within fields. Traditionally, instructions to amend an order – for example, to change the goods description, alter the documents required or inform of partial shipments – have had to be written in free text form. But in the new interface, the use of free text will be replaced by short, efficient new command codes, such as “ADD”, “DELETE”, and “REPLACE”.

The new standards releases are a sign of changing times. The “@” “%” and “&” characters, for instance, will now be able to be used in certain designated fields. It used to be impossible to include these specific characters in messages. But with the new standards release, SWIFT is recognising that these characters now form an important part of international electronic communication.

The release in 2019 will have even more significant consequences for the structure of guarantees and should not at all be underestimated.

When exactly can we expect these changes to happen?

RG: SWIFT has actually been working on these changes for the past five years, but the changes will take effect for users in two stages. The first,
The two new standards will go live in a “Big Bang” style. Implementation will be mandatory for all SWIFT participants – and there’s no going back after these dates.

**So preparation is the key?**

RG: Absolutely. Both trade banks and corporates need to realise how important the upcoming standards release is, and get ready for it. Otherwise, they run the risk of not being able to completely execute transactions via SWIFT and having to do a lot of manual work – or worse, not being able to carry them out at all. But to those institutions that are prepared, the standards releases offer many opportunities. The revised methods of processing financial messages give banks such as Commerzbank the chance to provide their customers with a higher-quality digital trade offering. That’s why we’re ensuring that both our back-office infrastructure and our foreign branches are well-prepared for our clients in November and next year.

Click here to read more about the Standards MT Release 2018 and 2019 and other updates at SWIFT.

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**In brief: SWIFT**

The Society for Worldwide Interbank Financial Telecommunication – better known as SWIFT – is a cooperative network of more than 11,000 financial institutions in over 200 countries and territories across the world.

Since 1977, its infrastructure has enabled the worldwide communication of standardised financial messages for trade, as well as payments, securities, and treasury.

“...the standards releases offer many opportunities...”
Pakistan forges new links with the world

Chinese investment, ambitious infrastructure development and new trading opportunities will help the economy on its growth path.

“Pakistan’s banks are looking forward to a good 2018.”

Alexander Mondorf, Commerzbank’s Regional Head Indian Subcontinent & ASEAN and Country Relationship Manager, comments: “This is encouraging, and we don’t see any reason why the positive trend shouldn’t continue. We should also remember that the country has elections coming up this year. This will be a landmark, as it will make only the second consecutive time in Pakistan’s history that a democratically elected government has seen out its term.”

Things are looking up for Pakistan. Data from the IMF reveal its economy expanded by 5.3% last year; it is now setting its sights on 5.6% in 2018, and almost 6% through to 2020. Such rates place Pakistan’s growth firmly above the average for emerging-market economies – not to mention the world as a whole.

Against the backdrop of such progress, the country’s financial sector is particularly confident. “Pakistan’s banks had a very good 2017,” notes Mondorf. “Despite the low-interest rate environment, they were able to make profits and are looking forward to a good 2018.”

Enter the dragon

Optimism is growing, thanks to ongoing development of the China-Pakistan Economic Corridor (CPEC). Having gained traction in recent years, this Chinese initiative is channelling into the country investments worth tens of billions of dollars in order to modernise Pakistan’s infrastructure.

A crux of CPEC has been the redevelopment of a major deep-water port at Gwadar, just west of Karachi. Pakistan is looking forward to several road developments, too. These include the building of a motorway from Lahore to Karachi and an upgrade of the Karakoram Highway, which links the Punjab to the Chinese border.

Railways will also be improved under CPEC, such as the Karachi-Peshawar line (a vital north-south artery) and in places extended to connect with China’s own networks. The last piece in the puzzle is an upgrade of the country’s power infrastructure, as the final quarter of 2017 saw Chinese energy companies beginning to invest in Pakistan’s power grids.

There are high hopes for the long-term boon that CPEC will generate. It is estimated that, over the next two to three years, all this new development could add around 2% growth to GDP, and create some 2 million jobs. “This is a great opportunity for Pakistan,” argues Mondorf. “It’s really giving the Pakistani people a sense that something’s happening – that things are moving forward.”

Nevertheless, in the short term, there are some challenges that the country will have to overcome, such as dwindling foreign currency reserves and a pending downgrade of the

At a glance: Pakistan

Capital: Islamabad
Largest city: Karachi
Population: 209.9 million
Currency: Rupee
GDP growth, 2017: 5.3%
GDP composition:
- Agriculture: 24.7%
- Industry: 19%
- Services: 56.3%
Major exports:
- Textiles
- Rice
- Leather goods
- Sporting goods
- Chemicals
- Surgical instruments
- Carpets and rugs

Export partners:
- United States
- China
- United Kingdom
- Afghanistan
- Germany

Import partners:
- China
- United Arab Emirates
- Indonesia
- United States
- Japan
country by the Financial Action Task Force. Both, however, are challenges that are not new to Pakistan and that have successfully been dealt with in the past.

**Supporting Pakistan’s trade**

China is already Pakistan’s largest trading partner, and CPEC is likely to build considerably on existing trading volumes. Mondorf explains: “Beijing’s own objective, of course, is to help develop China’s northwest by opening up new regional trade routes. CPEC will give it crucial access to the Indian Ocean, the Persian Gulf and East Africa; not having to sail through the South China Sea will cut days off shipping times.”

Yet Pakistan itself will also be able to pursue more trade with partners across Asia – and according to Mondorf, Commerzbank is ready. “We have a strong track record of supporting Pakistan’s cross-border commerce since independence, and healthy relationships with 20 local banks. For regional Asian banks, Pakistan – along with other emerging countries like Nepal and Bangladesh – tends to be rather ‘off the map.’ But thanks to our branches in Singapore, Hong Kong, Beijing and Shanghai, we can form a bridge to Pakistan for those institutions that may lack substantial links with the country. That is why we can facilitate the commodity trade between Pakistan and Singapore, for example, which regional banks cannot handle.” As Pakistan finds greater prosperity, meanwhile, demand for Europe’s exports will doubtless rise.

Here, too, Mondorf is confident. “Our work goes beyond facilitating exports of machinery from Germany. We’re unique in that our correspondent network can work in tandem with our local European branches. Our presence in Czechia, for instance – combined with our links to financial institutions in the Subcontinent – facilitates the flow of Czech exports to Pakistan. And just last year, we processed a letter of credit for a Scandinavian exporter sending capital goods to a plant in Pakistan; we were able to connect unfamiliar counterparties, and handle the size of the deal.”

New regulatory measures may help. Until recently, Pakistani law stipulated that the import of capital goods and machinery for projects must be 100% financed in rupees. But as a result of dwindling foreign exchange reserves, the central bank has determined that, now, there must be a 50/50 mix of local and foreign currency. “We’re used to handling letters of credit and short tenors,” says Mondorf. “But as Pakistan’s infrastructure development really kicks off, we’re expecting more demand for longer-term, ECA-covered finance denominated in foreign currencies. The financing opportunities in Pakistan’s market could be significant.”

With the help of Chinese infrastructure investment and banking partners with global reach, Pakistan’s trade can look towards bright horizons.
Building bridges in Southern Africa

In a region marked by economic disparities and political shifts, Christian Toben argues the financial sector can help form close trade and investment links.

The countries of Southern Africa – Angola, Botswana, Lesotho, Malawi, Mozambique, Namibia, South Africa, Swaziland, Zambia and Zimbabwe – have made significant efforts to regionalise, integrating through transport, energy and common customs infrastructure. The region is home to the world’s oldest-existing customs union. With roots dating back to 1889, today the Southern Africa Customs Union (SACU) – of South Africa, Botswana, Lesotho, Namibia and Swaziland – benefits the smaller members with tariff revenues generated by South Africa’s imports; while the Common Monetary Area (CMA) offers free capital flows and access to South Africa’s financial markets. The CMA comprises South Africa, Lesotho, Namibia and Swaziland. The currency pegs to the South African rand in Lesotho, Namibia and Swaziland reduce inflation and provide predictability in exchange markets.

Such regionalisation is key to building trade relations and attracting foreign investment to larger markets. We are even seeing infrastructure initiatives venture further to improve links with East Africa.

Trading companies are keen to tap Southern Africa’s potential: agribusiness companies, for example, see the region as a great cornfield. Interest from Asia continues: Japanese and Indian business grows, supplementing European investment, and offering alternatives to China. Keen to foster strong Asian trading relationships, at Commerzbank we have recently encouraged greater flows of expertise between Southern Africa and our Asian branches.

Even if we see improvement, several risks persist: weak legal systems, political instability and corruption threaten to some extent to hold back interest among foreign investors and economic development.

...partnership enables us to focus on cooperation with local banks in a very competitive market...

Banking bridges

The banking sector can help. On the one hand, global banks can mitigate the risk of unfamiliar markets and offer companies the cross-continental reach they need. With the support of our representative office in Johannesburg, for example, we gain a better understanding of local markets; Commerzbank thus serves as a bridge between our corporate customers – for instance in Europe and Asia – and local banks to facilitate trade business. This partnership model enables us to focus on cooperation with local banks in a very competitive market.

On the other hand, supranational development banks can provide the all-important cover in the region’s more challenging markets. At Commerzbank, we value opportunities to work closely with these institutions and bring them into contact with our corporate customers – inviting them to conferences and workshops in Europe. This allows African financiers to provide crucial insights into the Southern African market, and first-hand experience of how they evaluate local risks.

As the region’s countries continue to develop, export credit agencies (ECAs) are vital for providing cover for their high-value, capital goods imports. Banks can help “triangulate” support for key infrastructure projects – working closely with those private and public partners responsible for a project’s development.
In focus:
South Africa

Politics
Jacob Zuma resigned from his nearly decade-long presidency in February, following numerous motions of no-confidence in his leadership and major corruption scandal. Former deputy president Cyril Ramaphosa, the new leader of the African National Congress (ANC), the dominant political party since apartheid’s fall in 1994, has inherited a divided ANC and an economy in poor shape.

Economy
Africa’s most industrialised economy enjoys copious natural resources, well-developed communications, energy, and transport sectors, and the largest stock exchange on the continent.

Growth was a moderate 1.3% in 2017. Poverty, inequality, unreliable power infrastructure, currency volatility and unemployment – at a rate of almost 27% – persist. More than two decades after the end of white-minority rule, some 95% of the country’s wealth remains in the hands of 10% of the population.

The country’s long-term fiscal instability has posed challenges for international investors; by last year, two major international credit ratings agencies had downgraded South Africa’s international debt to junk bond status. Moody’s, however, has recently confirmed its investment-grade rating, citing Ramaphosa’s promises of fiscal reform, job creation and economic stimulus under his “New Deal” plan. This represents a crucial step toward allowing the country to finance its budget and current account deficits.

In focus:
Spill-over effects of the SACU on member countries

As the largest and most developed economy of the region, and the source of 85% of total SACU imports, South Africa is the main contributor to the SACU’s customs and excise revenue pool, which is shared across its other member countries Botswana, Lesotho, Namibia and Swaziland. The distribution system is based on their share of total intra-SACU trade and their development grade, measured by per-capita income.

In Botswana – for years boasting one of the best risk assessments in Africa, with low public and external debt, small budget and current account deficits, and a Sovereign Wealth Fund still benefiting the social needs of its citizens since independence – SACU revenues have been on a declining path, given high GDP growth between 4-5% of GDP in recent years.

The picture in Namibia is a slightly different one: here, SACU receipts contribute 32% of government revenues. After years of strong growth – of between 5-6% of GDP – since 2016 the economy has entered an adjustment phase, with large construction in the predominant mining sector having been completed. This year a recovery of 2.2% is expected, supported by higher commodity prices and new mining projects (for lithium) coming online.

The picture is slightly worse for Lesotho and Swaziland. To these two tiny landlocked countries, with a total population of 1.25 million people, SACU receipts contribute a remarkable 36-40% share of government revenues. Despite the urgently needed SACU contributions, both countries have very weak fundamentals with high budget deficits. South Africa also acts as a political stabiliser here, given the fact that the countries – both monarchies – are extremely politically divided.
The transformation of trade finance continues

Angela Koll and Gerhard Schipp offer FI.News their take on the latest trends in the evolution of trade finance

What areas of innovation are you exploring right now?

Angela Koll: We’re actively engaged in exploring new business models with those new technologies that can offer us greater transparency into the trade transactions of our customers. This transparency is key: it will help us to focus on more closely aligning the physical supply chain with the financial supply chain. It’s why the trade finance industry is so interested in unlocking the potential of distributed ledger technology (DLT), smart contracts, and the Internet of Things (IoT).

Gerhard Schipp: These are definitely exciting proposals. Blockchain could help clamp down on fraud and provide more integrated, efficient trade financing networks. Smart contracts could allow financing to trigger automatically at certain crucial points of a supply chain. And the IoT could bring us exciting things such as the “track and trace” of shipped goods, which would allow us important insights straight from the source. For instance, in addition to real-time assurance from exporters that a soft commodity has left port, banks and other counterparties could obtain temperature readings from inside the shipping container, or notifications from logistics companies that the goods were received by the importer. Our work with the Fraunhofer Institute for Material Flow and Logistics has been important as we explore a world in which the IoT interacts much more with the supply chains of the future.

Is momentum for innovation building in the industry?

GS: Just as in the rest of the financial sector, digitisation is certainly a hot topic, and driven by our corporate customers. But unlike other areas – such as payments – it’s still early days for the trade finance industry. Our sector has to account for a complex array of different counterparty: not only banks and corporates, but also regulatory and legal bodies, and logistics and insurance companies. Innovation will take time, engagement and investment from all those stakeholders; they will need to adopt new infrastructure to preserve interoperability, adjust their legacy (back-office) systems, and adapt to new rules and standards. We need to get to a “tipping point” at which investment begins to match rising demand for innovation.

AK: As major players in the trading landscape, we as banks also support the industry to reach this tipping point. This means investing in all of McKinsey’s “three horizons of growth”. The first horizon targets optimising and extending established trade finance solutions by digitising customer-to-bank communication, i.e. by implementing frontend solutions and offering portals. The second includes supporting market adoption of fairly new solutions like the Bank Payment Obligation (BPO), eDocs, and SWIFT’s MT798 “trade envelope” message, which have already entered the market. Encouragingly, the International Chamber of Commerce (ICC) has started to establish working groups to support the digital transformation by revising existing rules and guidelines which have an impact on the LC (eUCP) and BPO business (URBPO). In parallel, we are engaged in Horizon 3 - joining blockchain consortia and projects and investing in blockchain research initiatives.
What is progress like with banks’ blockchain projects?

AK: Progress is very encouraging! For instance, thanks to good cooperation with several other financial institutions, R3 and Trade IX as part of the Marco Polo initiative, we have carried out the first proof-of-concept for using blockchain in a trade and supply chain finance environment. Along with our involvement with the Batavia platform, this has given us vital experience and the chance to see exactly where and how we can make the ecosystem of trade finance to become more transparent and visible.

We will start to process the first pilot transactions in 2018. It’s particularly exciting, because – just as with the BPO and the underlying smart contract concept – DLT will enable us to increasingly combine trade finance with supply chain finance solutions.

GS: Ultimately, we see great opportunities arising from new technologies and we will definitely find our role in future trade ecosystems. The management and mitigation of different risks in international trade finance, as well as the provision of finance to support liquidity along supply chains, will remain the major needs of our clients. In close collaboration with our clients and with other relevant stakeholders in existing and future trade ecosystems, we will identify exactly where new technologies offer new solutions and where they can help us to provide trade and supply chain finance in a much more sophisticated way.
“...banks are striving even harder to become more competitive and innovative for their corporate customers.”

With the entry of new fintech players into the market – not least encouraged by regulation such as the Second Payment Services Directive (PSD2) – and the availability and growing experience of new technologies, banks are striving even harder to become more competitive and innovative for their corporate customers.

**Reconciling with new projects**

When it comes to digitalisation, it is blockchain and distributed ledger technology (DLT) that tend to make the headlines. For instance, Commerzbank, together with SWIFT and other industry members, has been looking into a proof of concept for the reconciliation of payments over DLT. Since banks’ global correspondent networks and nostro accounts tie up large sums of liquidity, the idea is to use one centralised account platform from which both parties in a transaction can handle and gather information across a distributed ledger.

However, we must approach the new technology with a big question mark. The whole payment community needs time to establish a new common structure – so it remains a step-by-step process with plenty of opportunities.

**Progress continues with SWIFT gpi**

That is why, at least for the time being, payments will likely move more in the direction of SWIFT’s global payments innovation (gpi) initiative. With SWIFT, we have established structures, decision-making boards, contacts and working groups – all with a common understanding, built up over decades, of how the international payments system works and should work. SWIFT gpi is intended to build on this and revolutionise the payments industry – helping banks stay competitive by making payments faster, trackable, more transparent, and more easily cancellable.

The data we have are encouraging: just a year on from its launch, SWIFT has reported that over $100 billion worth of international payments is now facilitated under gpi every day – nearly 10% of its payment traffic – within minutes or even seconds.

At Commerzbank, we have achieved a number of steps vital to being able to offer gpi payments. For example, we have been hard at work installing the “unique end-to-end transaction reference number” functionality needed to track payments in real time. The pressure is on to embed many of gpi’s new features, since a number are required by SWIFT’s upcoming releases in November. The next major step for all banks will be to provide payment information directly to the corporate customer. There are certainly exciting times ahead.
A View from Sibos: Commerzbank’s video interview with The Banker

Enno-Burghard Weitzel updates the magazine on high-level trends in trade finance

As the financial community came together for the Sibos 2017 conference in Toronto, Enno-Burghard Weitzel, Head of CTS & Fi Product Management Trade Services, met Joy Macknight, Technology and Transaction Banking editor of The Banker, to discuss the most pressing issues in the trade finance industry today.

First up was innovation. Weitzel explained that the trade finance industry needs to “dramatically increase its efficiency and effectiveness” by using technologies already on the market, such as optical character recognition, machine learning and AI. Highlighting the value of the Bank Payment Obligation (BPO) to financial institutions and companies, Weitzel explained that “at Commerzbank, we are at the forefront of progress with the BPO, and seek to help more corporates to realise its benefits.”

While recent years have seen much hype over blockchain, Weitzel noted that significant progress with DLT has since been made: “We are now further down the road – working out where we can actually use blockchain, and investigating proofs of concept. Rather than replacing the letter of credit, I’d see blockchain of more value to the open account space, where we can bring more security to deals and find new solutions that meet the evolving needs of our corporate clients.”

Another key trend Weitzel identified was sustainability: “Wider society is demanding a sustainable economy – and banks must be the driving force behind it. But sustainability doesn’t just mean conserving our own resources. It also means taking a thorough look at our client relationships – intensifying our work with those that are looking to the future.”

Watch the interview here.
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