



DRIVING INCLUSIVE DIGITALIZATION IN TRADE AND TRADE FINANCE

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Driving Inclusive Digitalization in Trade and Trade Finance

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INTRODUCTION

Amid the ongoing coronavirus disease (COVID-19) pandemic, risks from the Russian invasion of Ukraine, rising inflation, and tighter financial conditions are raising economic uncertainty while global growth and trade have yet to recover to pre-pandemic levels.

Nonetheless, the pandemic has hastened forces toward digitalization around the world that can help overcome challenges as COVID-19 wanes, including in trade and trade finance. At the same time, digital technologies can help the trade sector adopt measures to economic growth that is more inclusive and environmentally sustainable.

Global economic growth (up 6.0%) and merchandise trade volume (up 9.7%) both recovered in 2021 but are expected to moderate in 2022 and 2023. Gross domestic product (GDP) growth is expected to ease to 3.2% and 2.7% in those years, and trade to 3.5% and 1% (IMF 2022, WTO 2022) (Figure 1).

Likewise in developing Asia, GDP growth accelerated to 7.0% while merchandise trade volume grew 13.1% in 2021 but are expected to slow growth to 4.3% in 2022 and 4.9% in 2023 and merchandise trade to 2.9% and 1.1% in the same period (ADB 2022a, WTO 2022).

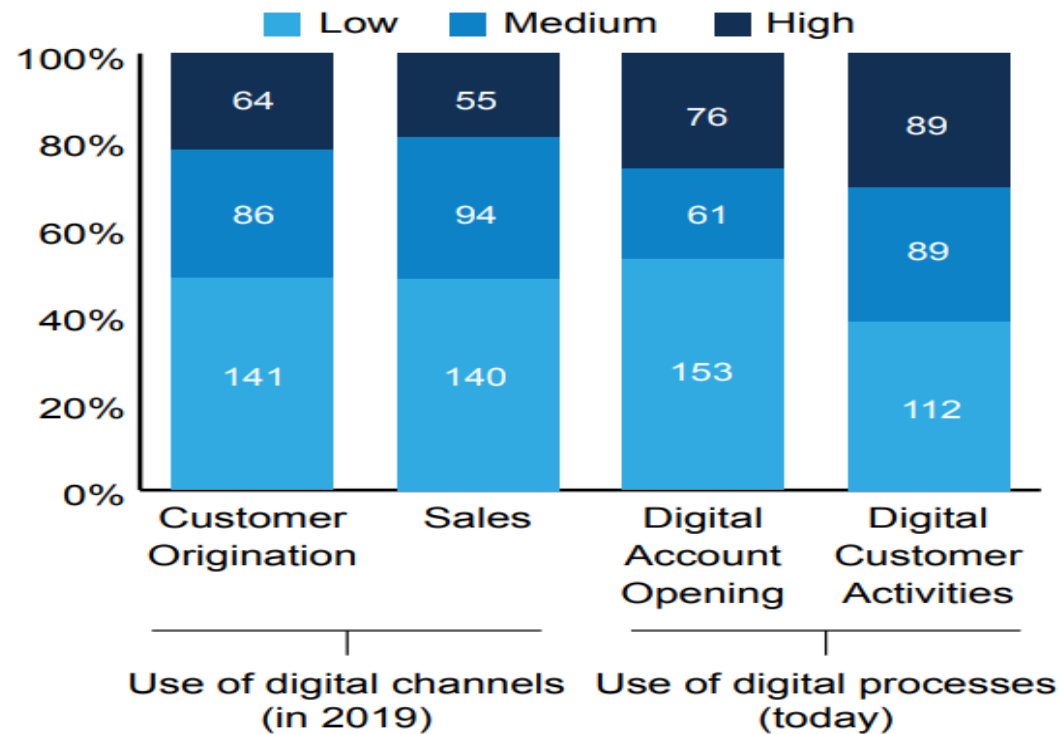
Notes:
1. This brief draws from the discussion during Parallel Session 2A, Driving Digitalization to Close Trade and Supply Chain Finance Gap at the Trade 20 (T20) Summit that took place in Bali, Indonesia on 4-5 September 2022; Toward Inclusive Access to Trade Finance: Lessons from the Trade Finance Gaps, Growth and Jobs Survey (ADB 2022a); and Asia-Pacific Trade Facilitation Report 2019: Bridging Trade Finance Through Technology (ADB and UNESCAP 2019).
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The pandemic accelerated digitalization, while an uncertain economic climate poses risks

Use of digital processes for sales and customer origination



Source: World Bank. 2022. World Bank Group Global Market Survey: Digital Technology and the Future of Finance. (2022).

Goods Trade and Real GDP, yoy%, World



Source: IMF WEO 2022; WTO 2022

Various international initiatives are gaining ground in driving digitalization

- All **ASEAN** member states are part of ASEAN Single Window
- **Singapore** has signed digital economy agreements with **Chile, New Zealand, Australia, Republic of Korea, and UK**
- **G7** economies have approved declaration on Digital Trade Principles
- **ROK** adopted the Framework Agreement on Facilitation of Cross-border Paperless Trade in Asia and the Pacific
- **UK** has proposed an Electronic Trade Documents Bill
- **US** has enacted amendments to Uniform Commercial Code

Three major challenges in cross-border trade and trade finance transactions



Paper-based transactions

- Inefficient, expensive, prone to error
- Processing L/C involve 20 parties and over 100 pages of documentation



Regulatory requirements

- High costs of KYC/AML compliance for banks
- Regarded as biggest hindrance to trade finance provision

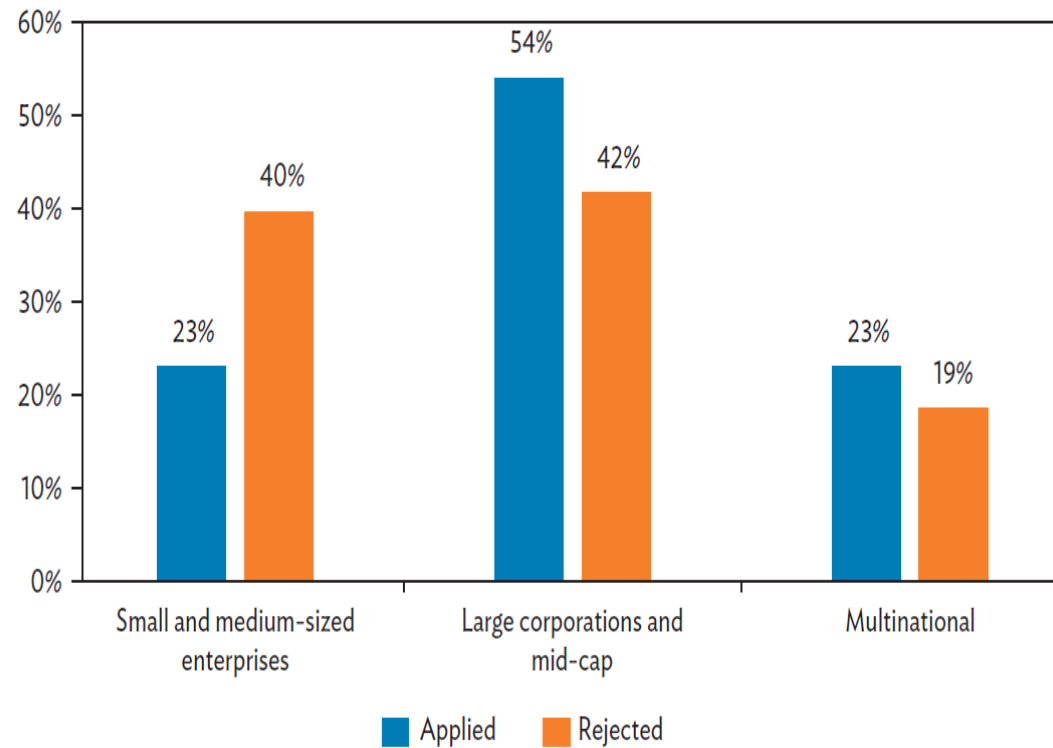


Information asymmetry

- High risk premiums charged to small firms
- Difficult for SMEs to meet collateral, guarantee requirements

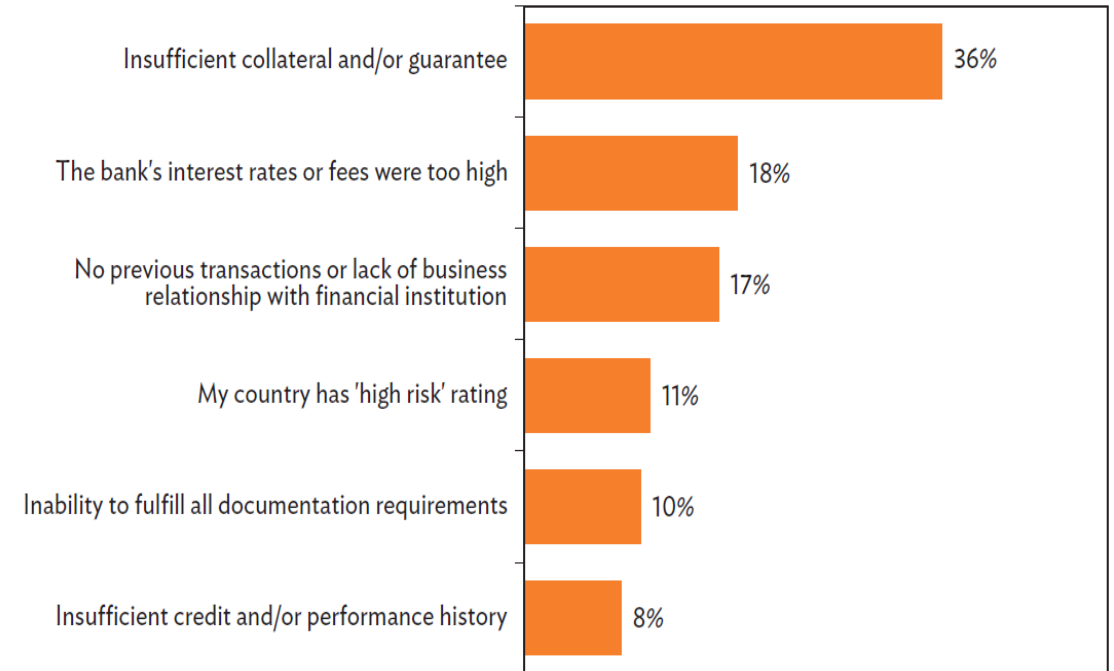
SMEs continue to face high trade financing costs relative to large firms

Share of Rejections in Trade Finance, by Firm Size



Source: ADB. 2021. Trade Finance Gaps, Growth and Jobs Survey. ADB Briefs No. 192.

Firm's Perception of Reasons for Rejection



Source: ADB. 2022. Toward Inclusive Access to Trade Finance: Lessons from the Trade Finance Gaps, Growths, and Jobs Survey. Manila.

Current economic climate is compelling businesses to adopt digitalization due to large benefits

Benefits of Trade Digitalization and Technology

Technology	Addressing Challenges of Trade Finance				
	Challenge 1: Process inefficiency		Challenge 2: Regulatory requirements		Challenge 3: Information asymmetry
	Decreased human errors	Improved speed of transactions	Improved flexibility to changes in market and/or regulatory requirements	Improved AML and KYC efforts	Improved credit scoring tools
Cloud-based invoicing solutions	✓	✓			✓
Optical character recognition	✓	✓		✓	
Electronic bills of lading	✓	✓			
Distributed ledger technology such as blockchain-based platforms	✓		✓	✓	✓
Artificial intelligence and big data	✓	✓	✓	✓	✓
Single window	✓	✓	✓		
Internet-of-Things and GPS	✓	✓			
Application programming interfaces	✓	✓	✓		

AML = anti-money laundering, GPS = global positioning system, KYC = know-your-customer.

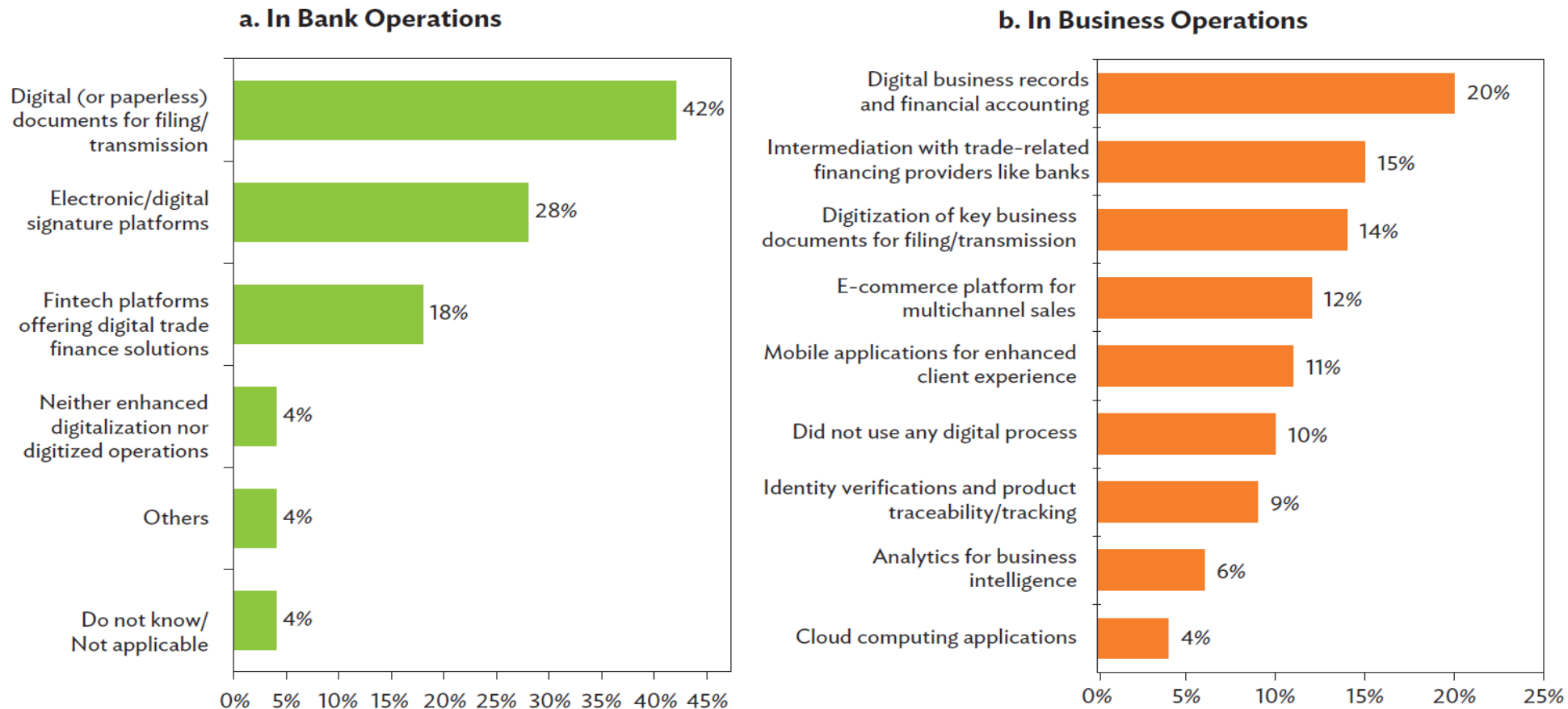
Source: ADB and UNESCAP. 2019. Asia-Pacific Trade Facilitation Report 2019: Bridging Trade Finance Gaps Through Technology. Manila.

- Reduces human error
- Enhances traceability in complex supply chains, enables ESG compliance
- Helps verify business identity and financial capacity
- Facilitates SME participation in trade

Despite benefits, the scope of digitalization remains limited

- Businesses use technology mainly for digital filing and transmission, record-keeping, and accounting

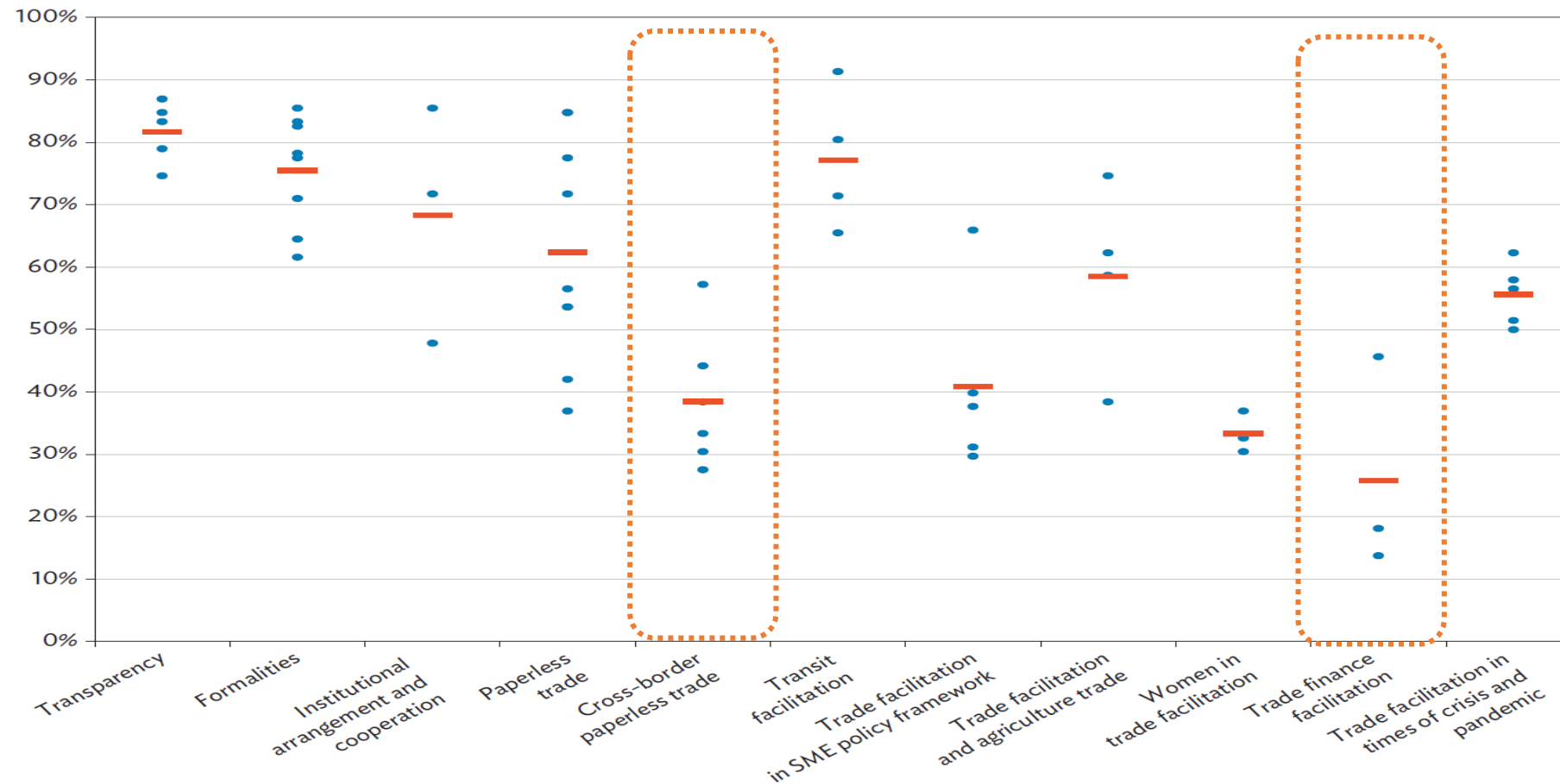
Areas of Operations Where Digital Solutions Are Utilized



Source: ADB. 2021. Trade Finance Gaps, Growth and Jobs Survey. ADB Briefs No. 192.

Asia has made significant progress in trade facilitation, but cross-border paperless trade lags behind

Implementation of Trade Facilitation Measures, Asia and the Pacific



SME = small and medium-sized enterprise.

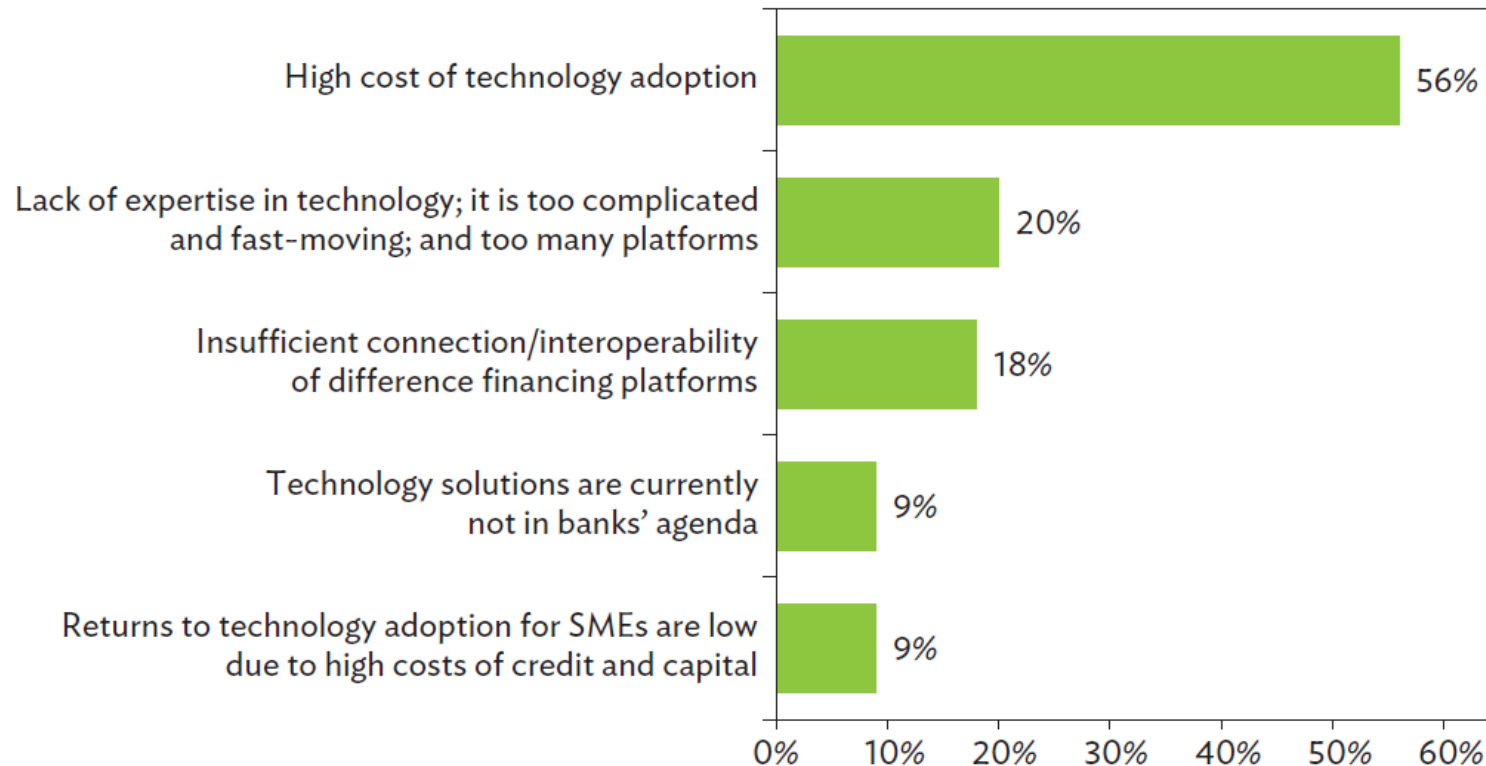
Note: Blue dots represent country scores (100% = full implementation); red lines are group averages.

Source: UN Global Survey on Digital and Sustainable Trade Facilitation. 2021.



Limited uptake arises from high cost of technology, lack of common standards and interoperability

Banks' Major Areas of Concern on Technology



- Only 7 jurisdictions have adopted UN Model Law on Electronic Transfer of Records
- Developing economies and SMEs lack digital infrastructure and knowhow

SME = small and medium-sized enterprise.

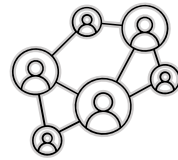
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POLICY CONSIDERATIONS



Legislation

- Adopt Model Law on Electronic Transferable Records or equivalent legislation



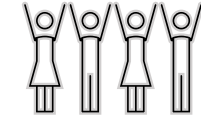
Interoperability

- Address digital island problem by adopting international standards
- Digital Standards Initiative (DSI)



Green and inclusive trade

- Create accessible incentives and sustainable financing tools
- ESG implementation



Digital divide

- Support developing economies to acquire skills, technology, hardware

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KEY POINTS

- Digitalization can help address structural issues that increase the cost of trade and trade finance such as paper-based process inefficiency, costly regulatory compliance for anti-money laundering/ know-your-customer, and high-risk premiums on small borrowers.
- The use of digital technology in trade and trade finance has been constrained by a lack of legal frameworks, limited technical interoperability, and a digital divide.
- A globally concerted effort is needed to address such constraints by adopting the United Nations Model Law on Electronic Transferable Records or equivalent legislation and promoting common digital standards across the trade ecosystem.
- Small businesses lag behind in digitalization given their limited capacity and access to finance, which requires special attention to their skills development and accessible sustainable financing tools.

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