DC-PRO

LC Market Intelligence Survey






2005

European Bank
for Reconstruction and Development

International Financial
IFSA
Services Association

ICC

Table of Contents

1. Introduction

This report outlines the results of the DC-PRO Letter of Credit Market Intelligence Survey carried out in April and May of 2005.

1.1 Background

This survey is a follow-up to the widely acclaimed 2003 LC Market Intelligence Survey. As with the original Survey, its purpose is to obtain information from the marketplace that reflects current commercial and operational practice within the international trade finance banking community.

The scope of this Survey has been extended beyond the DC-PRO member-base to include participants from the International Financial Services Association, USA, and members of the European Bank for Reconstruction and Development's Trade Facilitation Programme.

This broader participation allows more specific regional analysis and facilitates the more accurate capture of trends in global operations and practice.

1.2 Methodology

DC-PRO and the ICC developed a 30-item questionnaire to collect information from over 1500 trade finance professionals across 112 countries.

The survey was conducted on-line and was available to participants from 6 April 2005 to 13 May 2005.

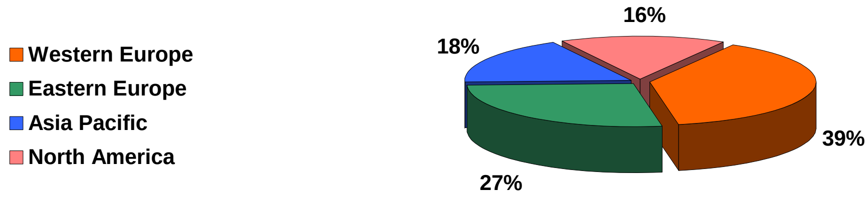
The broad goal of this survey was to obtain valid and reliable information from experienced trade finance professionals with "hands-on" knowledge of international trade finance work in a modern banking environment.

Specifically, this survey's questions addressed the following topics:

- the trade finance department structure and operation
- rules and practice in trade finance
- trade development and technology

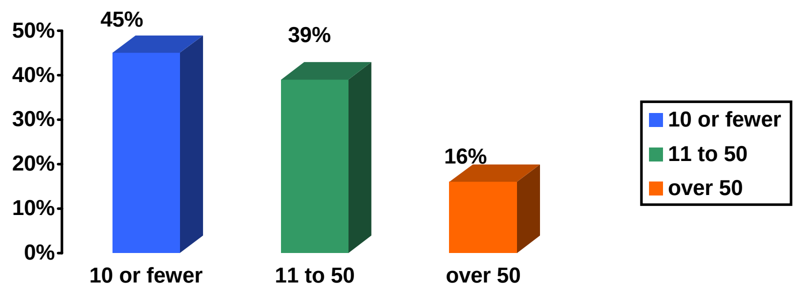
The survey received a 14% response rate. All respondents are guaranteed anonymity.

The representation by geographic region was as follows:

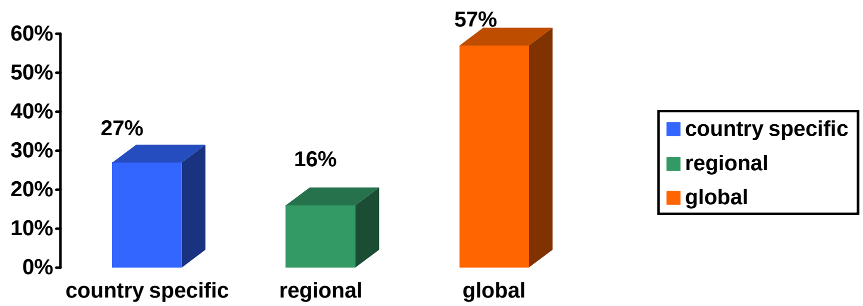


Western Europe – 39%
Eastern Europe and CIS States – 27%
Asia Pacific (including Middle East) – 18%
North America – 16%

The profile of respondents varied significantly:



45% represented LC departments of 10 or fewer staff
39% represented LC departments of between 11 and 50 staff
16% represented LC departments of over 50 staff



57% of banks' trade finance operations are distributed globally
27% of banks' trade finance operations are based in one country
16% of banks' trade finance operations are based within a number of countries in one geographic region

This report is an amalgamation of the feedback and opinions of this geographically and organisationally diverse section of the trade finance banking community.

1.3 Executive Summary

Trade Finance Department Structure and Operation

60% of trade finance departments report an increase in both the volume and value of import and export L/Cs over the past 5 years. Only 15% of respondents report a decrease. The greatest increases were in Eastern Europe and Asia Pacific at around 80% each.

More respondents report an increase in employee levels (43%) than those reporting a decrease (37%). 18% report no change in staffing levels over the past 5 years.

Discrepancy rates have fallen slightly since the 2003 survey, with average discrepancy rates now at 52% and 56% for import and export L/Cs respectively. 84% of departments indicate a constant or lower level of discrepancies than 5 years ago.

Rules and Practice

98% of respondents issue standby credits subject to UCP 500. 45% have also issued standbys subject to ISP98.

Almost half of the departments surveyed have issued Demand Guarantees subject to URDG 458.

There is no reported use of eUCP. The majority of respondents feel it will be over 4 years before credits will be issued subject to eUCP.

99% of departments have not issued a revocable credit in the past 5 years.

Trade Development and Technology

Most respondents see Asia as the market with the most potential for development of letter of credit activity.

Over 75% of departments offer some level of document pre-checking facilities to customers. However only 24% offer this service to all customers.

83% of trade finance departments do not offer any document preparation services to customers.

52% of respondents currently offer, or are developing, an online L/C application service.

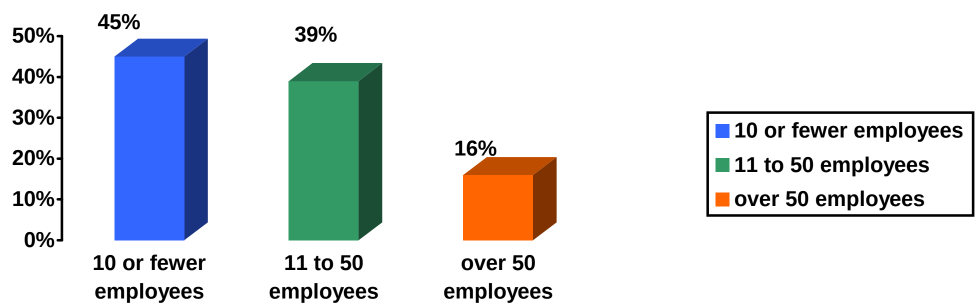
90% of departments have not outsourced or insourced any aspect of their trade finance services.

Trade Finance Department Structure and Operation

2.1 Employee levels

Department sizes range from single person operations to processing centres with 200+ employees. The average department size is 36 employees.

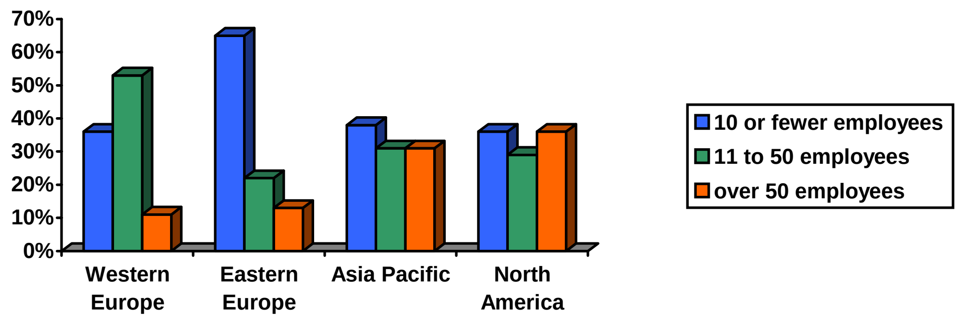
Department sizes



45% of international trade finance departments have 10 or fewer employees
39% have between 11 and 50 employees
16% have over 50 employees

Regional Comparisons

Employee levels in trade finance departments varied markedly between regions.

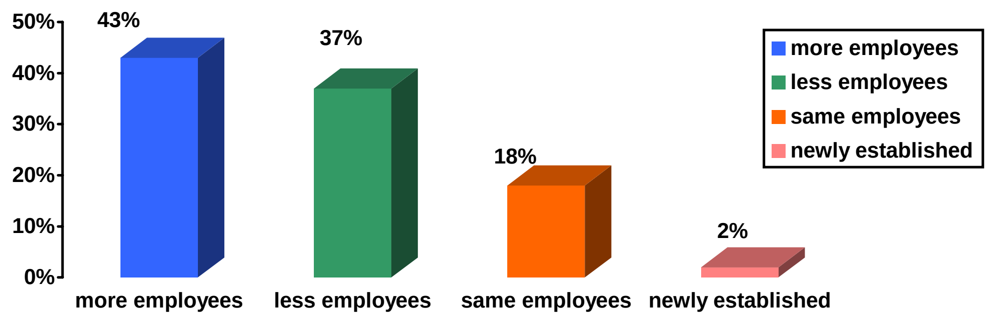


65% of Eastern European trade finance departments have 10 or fewer employees – almost double the figures indicated by the Western European (36%), Asia Pacific (38%) and North American (36%) trade finance departments.

Western Europe has the highest number of trade finance departments in the 11 to 50 employees bracket with 53%.

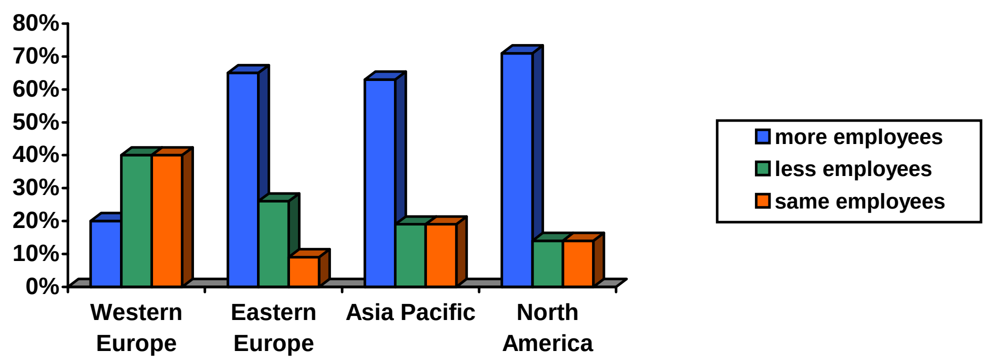
North America and Asia had the largest percentage of departments with over 50 employees – with 36% and 25% respectively.

Employee levels over the past 5 years



43% of departments have a greater number of employees than 5 years ago
37% of departments have a lesser number of employees than 5 years ago
18% of departments have the same number of employees as 5 years ago
2% of departments are newly established

Regional comparisons



The majority of departments in Eastern Europe, Asia Pacific and North America indicate an increase in the numbers of employees over the past 5 years.

Conversely, the majority of Western European departments indicate either a decreased or constant level of employees – with only 20% of departments indicating an increase in employee levels over the past 5 years.

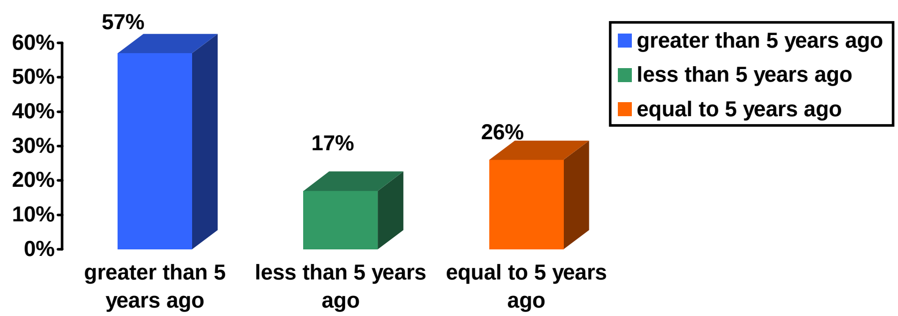
"The number of people involved in documentary business fell substantially (from 9 to 5)."

"Globally less in operations but quite a few more in sales."

> *"Less staff in Europe, more in Asia."*

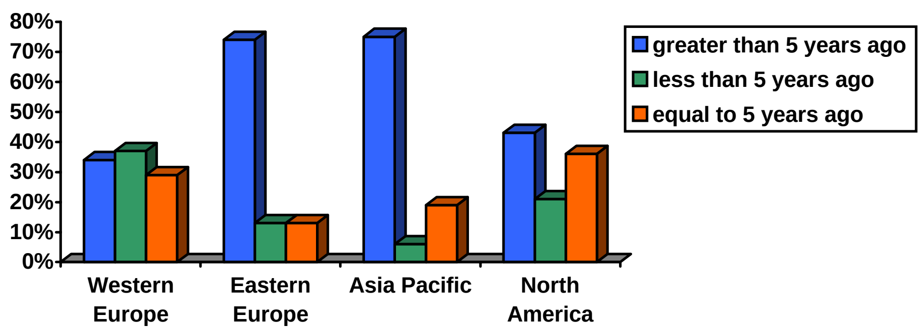
2.

The majority of LC departments indicate an increase in the volume and value of import LCs over the past 5 years.



57% of departments indicate a higher volume and value in import LCs than 5 years ago
17% of departments indicate a lower volume and value in the same period
26% of departments indicate a volume and value in import LCs equal to 5 years ago

Regional comparisons



75% of departments in both Eastern Europe and Asia Pacific indicated an increase in the volume and value of import LCs over the past 5 years.

43% of North American departments indicated an increase.

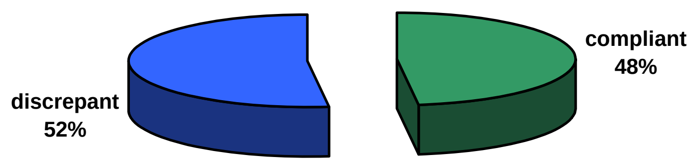
Western Europe is the only region where there were more departments indicating a decrease in volumes and values (37%) than the number reporting an increase (34%).

> *"Figures depend on our clients' growth in international trade, on the change of number of our clients and on migration of LC to documentary collections or direct payments, because of lower prices and despite higher risk."*

> *"Though the use of LCs is decreasing compared to other payment terms, the overall figures are higher as imports are increasing significantly."*

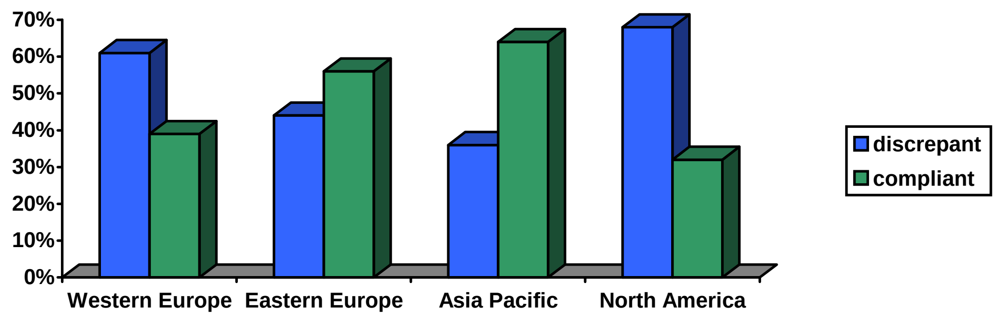
2.3 Discrepancy rates for import LCs

The average discrepancy rate on first time presentations under import LCs was 52%. Discrepancy rates on import LCs varied greatly from department to department. The lowest discrepancy rate experienced was 10% and the highest was 95%.



On average 52% of presentations under import LCs were discrepant on first presentation
On average 48% were compliant on first presentation

Regional comparisons



Discrepancy rates varied widely between regions.

North America indicated the highest average discrepancy rate of 68%.

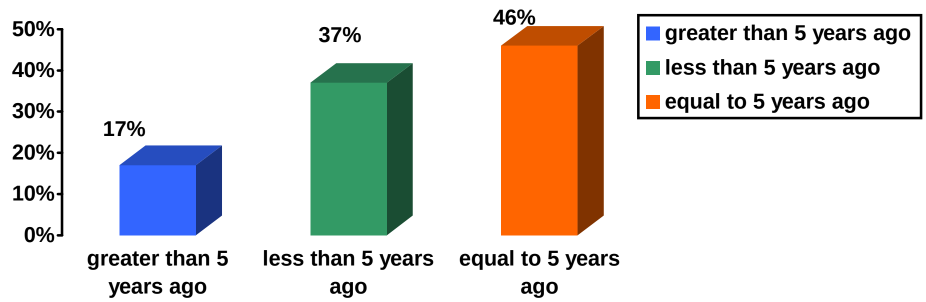
Asia Pacific indicated the lowest average discrepancy rate of 36%.

"The majority of discrepancies are found in transport documents, especially in CMR and B/L"

"The figures exclude those import bills that have delivered goods under shipping guarantee. The shipping guarantee accounts for 25% of our total transaction number."

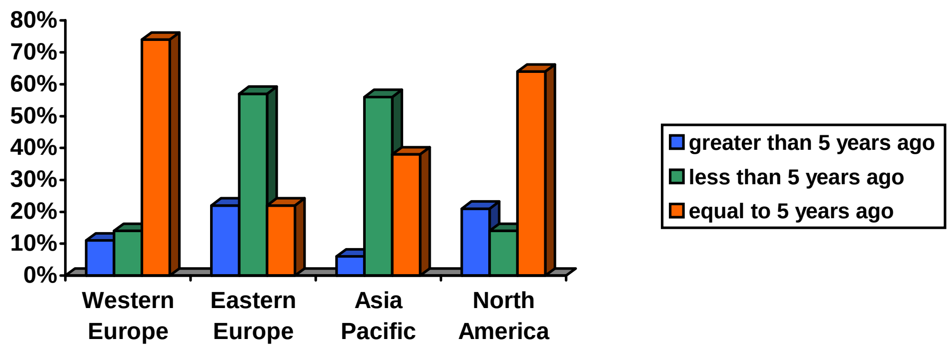
"It depends on the origin - European and Korean documents generally contain fewer discrepancies."

Discrepancy rates over the past 5 years



17% of departments report an increase in discrepancy rates in the past 5 years
37% report a decrease
46% report a constant rate of discrepancies

Regional comparisons



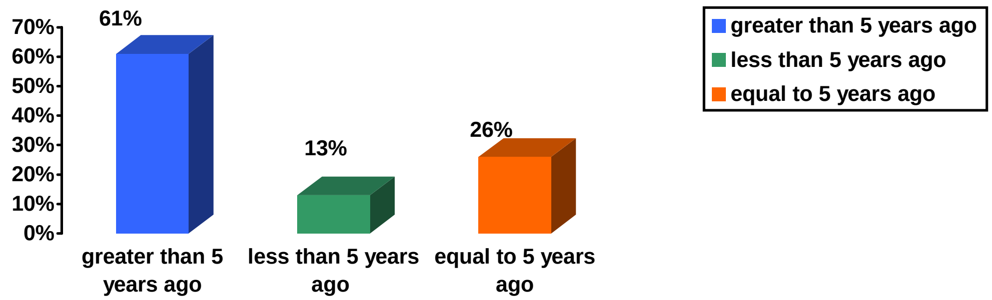
Over 80% of trade finance departments in each region indicate that discrepancy rates are less than or equal to those experienced 5 years ago.

74% of trade finance departments in Western Europe indicate that discrepancy rates have remained constant.

At the same time 50%+ of Eastern European and Asia Pacific departments indicate a decrease in discrepancy rates over this 5 year period.

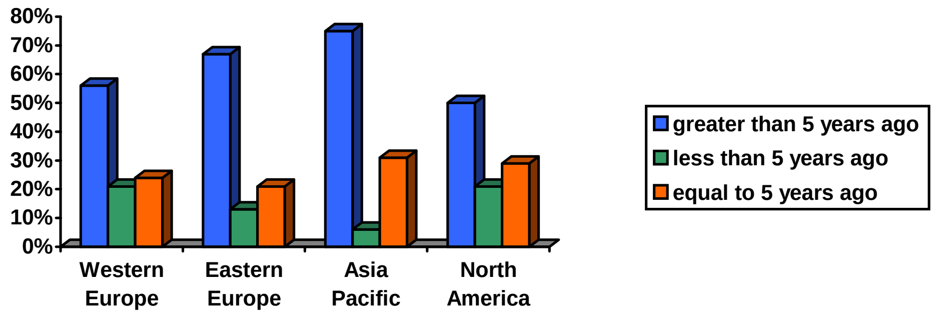
2.4 Export LC Processing

The majority of LC departments indicate an increase in the volume and value of export LCs over the past 5 years



61% of departments indicate a higher volume and value in export LCs than 5 years ago
13% indicate a lower volume and value
26% indicate a level of volume and value equal to 5 years ago

Regional Comparisons



Over 50% of departments in each region indicate an increase in the volume and value of export LCs over the past 5 years.

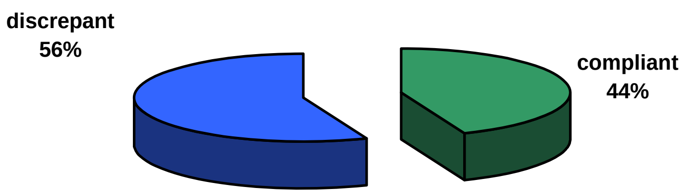
"Our bank has started to spend actively on international trade finance operations since 2001, so the quantity of sets of documents presented under export credits is greater than 5 years ago."

"Figure depends on growth of exports and new markets for our exporters."

"Transaction count is more or less the same, but the transaction amount is greater."

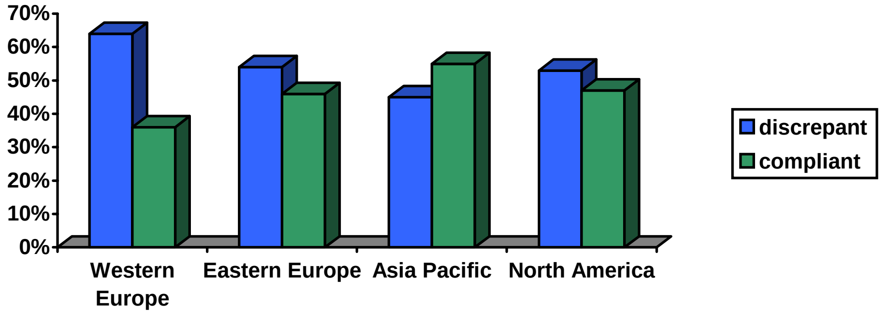
2.5 Discrepancy rates for export LCs

The average discrepancy rate on first time presentations under export LCs was 56%. Discrepancy rates on export LCs varied greatly from department to department. As with import LCs, the lowest discrepancy rate experienced was 10% and the highest was 95%.



On average 56% of presentations under export LCs were discrepant on first presentation
On average 44% were compliant on first presentation

Regional comparisons

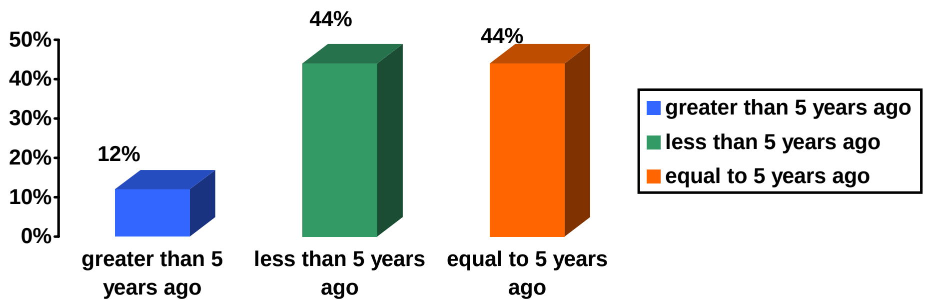


Western European trade finance departments indicated the highest average discrepancy rate of 65%.

Departments in Asia Pacific had the lowest discrepancy rate on first time presentations of 45%. This was the only region where the compliance rate was greater than the discrepancy rate.

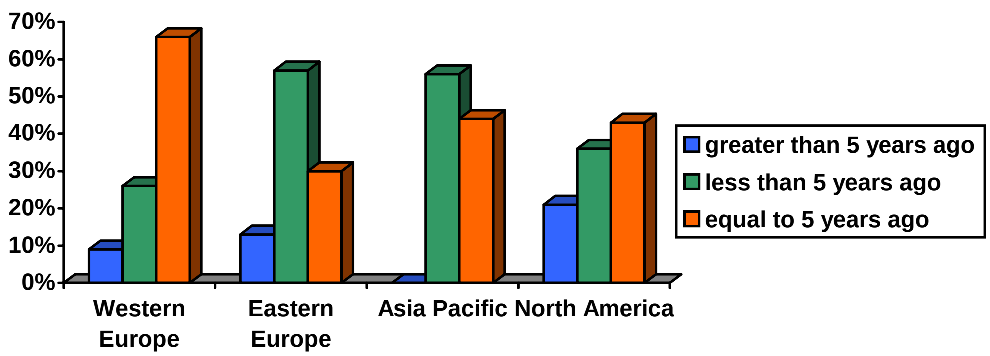
Eastern Europe and North America indicated discrepancy rates of 54% and 53% respectively.

Discrepancy rates over the past 5 years



12% of LC departments report an increase in discrepancy rates over the past 5 years
44% of LC departments report a decrease
44% of departments report a constant rate of discrepancies over this period

Regional Comparisons



The majority of banks in each region indicate that discrepancy rates for export LCs are equal to or less than those experienced 5 years ago.

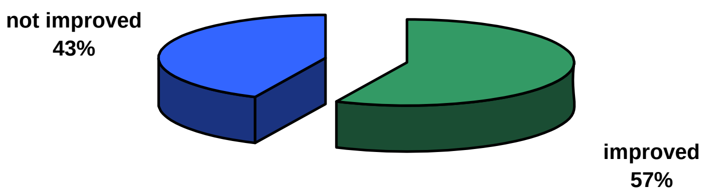
100% of Asia Pacific departments indicated discrepancy rates less than or equal to 5 years ago.

"Second presentations give a better picture of the situation. We have experienced that it is almost impossible to avoid rejections of documents from Western European Banks acting as Confirming Banks. We always have to fight to achieve compliance."

"These percentages decrease to less than 10% after first examination and corrections from the beneficiary."

2.6 ISBP and beneficiary presentation of documents

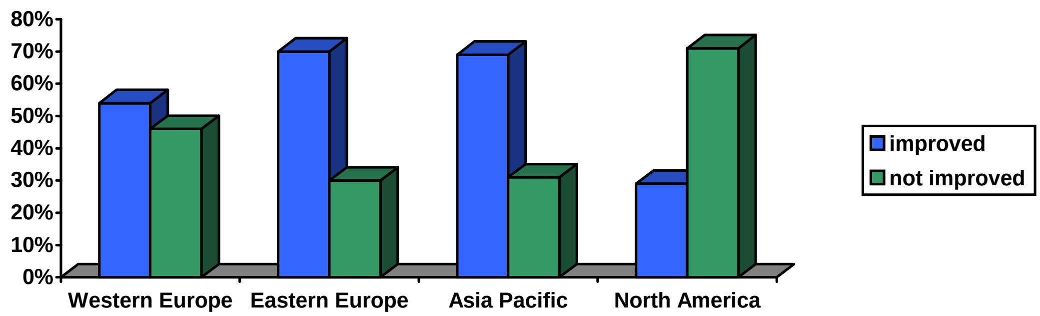
There is an almost even division between departments over whether the ISBP has resulted in improved beneficiary preparation of documents.



57% of LC departments indicate that the introduction of ISBP has improved beneficiary preparation of documents

43% indicate that it has not had an impact

Regional Comparisons



North America is the only region where less than half of the respondents felt that ISBP had improved beneficiary preparation of documents.

> *"Perhaps the best reference on interpreting the UCP. It has made life easier for bankers."*

> *"Neither beneficiaries nor applicants show a lot of interest in study or use of ISBP."*

> *"It depends on the effort of the banks - and if they extend the relevant training to their customers. We are just starting the external customer training and waiting to see the result."*

> *"A lot of customers don't bother to check ISBP and totally rely on the bank's advice."*

Commentary by Vincent Maulella

Vin Maulella is the principal of an international banking and trade consultancy. He has over 30 years experience in banking, specializing in operations, risk, product and project management of businesses dedicated to facilitating and financing international trade. Having retired from The Chase Manhattan Bank, he serves the market by working independently and through a number of organisations active in a policy role for letters of credit and related trade matters.

Vin serves as Associate Director of the Institute for International Banking Law & Practice, as International Banking Advisor for the United States Council for International Business, as a member of the FCIB Hotline Committee, and as a Contributing Editor for Documentary Credit World.

Vin is a DOCDEX Expert, ICC Centre for Expertise, an Accredited Arbitrator, International Centre for Letter of Credit Arbitration and holds the FCIB professional designation Certified International Credit Professional. He serves as an expert witness and litigation consultant in civil and criminal proceedings. Vin is also on the Advisory Board of several e-initiative companies. As part of his consultancy Vin offers review of tactical and strategic business plans as well as critique and recommendations of operational procedures and systems alternatives.

I would like to begin my commentary with a cautionary note; it is possible for a 6-foot tall statistician to drown in a stream that averages 3-foot in depth!

This caution resides in the same school of thought on statistics as the well-known sayings *“lies, damned lies and statistics” and “Figures don't lie, but liars figure”.*

Having carried out many Surveys with the Institute of International Banking Law and Practice in the global ‘L/C Annual Survey’ events, I have learned that statistics can be very useful but can be read, misread and manipulated to form and support different, even opposing viewpoints.

My comments on this Survey are based on my years of hands-on experience in the field, participation in global trade programs and discussion with market leaders and followers. Nevertheless, I urge readers to consider my views in light of their own experiences and insights. Keep in mind also that to many questions, there is more than one right answer and in fact, in many cases there may be no right answer.

Not working for a particular bank or industry group, I do not have specific point to prove or disprove. I accepted this invitation to offer commentary as just that, an invitation to comment. I do not have an agenda or thesis and my comments are offered in that spirit. I offer those who might disagree with me, the same invitation to share their views and insights.

I hope the insights that I provide are informative and of assistance to your L/C operations but remember they are not definitive and are not the last word.

Department Sizes and Employee Levels

The fact that some trade finance departments have a single person while others have over 200 makes it clear that there is no one size fits all for trade finance.

No doubt, departments of over 200 employees reflect the centralised operations for those large global banks, a number of which also offer processing for smaller banks, thus making big operations even bigger.

Those operations not only offer economies of scale, but should “raise the bar” of upgraded trade services to a broader user base of commercial and financial companies; the downside, if one chooses to view it as such, is the commoditisation of trade services.

A department of 10 or less could represent a centralised operation for a newly established trade finance bank, or, a small regional processing department, or a decentralised operation for a large national or global bank.

A department with 11 to 50 employees could represent a small centralised or regional operation, while a department with over 50 employees could represent a large regional processing centre for a global bank or a centralised operation for a national or global bank.

I for one am concerned with the report that there are a number of single person operations. We need to know more about these single person operations. If these single person operations represent the spoke of a hub and spoke strategy (the spoke does data entry not decision making) then I am less concerned than if a bank has a one person event where that one person does everything for everybody (issuance, document examination, all “dollar” values and all variations of complex transactions).

A final observation regarding the single person operations would be a word of warning and caution for management….. if this person is doing more than data entry it raises a number of concerns in relation to the depth of required knowledge involved, back up for that person (in the event of sickness, holidays(!), career change, retirement etc.) and on an operational level in relation to consistency, control, and compliance with banking and regulatory standards.

The regional comparisons are helpful in appreciating the distribution of these departments. For example, Eastern Europe is highest in percentage of smaller (10 or fewer) departments. This is understandable if we accept that these may be newly established departments with relatively low volumes.

Asia Pacific and North America department size is fairly evenly distributed among the three sizes. Given the geographical market size in North America and Asia Pacific, the number of key trade and financial centres in those markets, and number of banks operating in those markets, this is a reasonable size allocation.

Western Europe reports the highest percentage of 11-50 employee departments which seems to reflect the maturity of an established market of trade service providers and the centralisation or regionalisation of processing centres.

The employee levels over the past 5 years show a reversal of the figures reported in the 2003 Market Intelligence Survey. These levels must also be viewed in relation to import and export L/C volumes reported. Factoring in, or out as you please, the 20% of respondents with the same number of employees as two years ago, or who are newly established - those with more staff figure at approx 54% and those with less at approx 46%. In 2003 those numbers would have been 40% more and 60% less.
Now, factor in volume of import and export L/Cs. 26% of respondents report equal volume of imports and exports as 5 years ago but only 18% report the same number of staff as 5 years ago. What does that tell us? Could be that (1) some departments were overstaffed or to put it another way had excess capacity and did not need to be increased to meet new volume or (2) management is slow to increase staff in trade finance departments to meet increased volume. Yet, for the 17% and 13% of respondents reporting a decrease in volume of imports and exports from 5 years ago, a disproportionate number of respondents, 37% reported a decrease in staff -- figure that one!

It's no secret among trade service managers that senior bank management is quick to reduce trade service staff at the first sight of reduced volumes. An inescapable reality facing trade service managers is that trade is often viewed as a cost centre and so, can only contribute to the bank's bottom line by reducing expenses. In addition, trade does not yield the same return on expense or capital as other bank business lines. The pressure has been and continues to be on trade. Many Product Managers spend a good deal of their time trying to explain the relationship and interdependency of direct trade services revenues, like L/C and collection fees, to foreign currency commission, loan income and treasury revenues.

As might be expected, trade finance departments in Eastern Europe are growing, while those in Western Europe remain fairly stable. Surprisingly, a high percentage of respondents from Asia Pacific and North America report an increase in staff levels. Depending on who is replying for which banks, and considering some of the additional comments, that apparent distortion may be the result of relocation of work to lower cost environments, whether in region or country, (e.g. from New York City to Tampa, Florida) or out of country (e.g. North America and Western Europe to Asia Pacific).

The increase in value of L/Cs should be no surprise. Many importers and exporters - concerned about traditional discrepancy rates and the fact that banks charge minimum fees which make L/Cs disproportionately expensive for small dollar transactions - have established internal policies that call for open account or cash in advance for shipments under threshold dollar values. Makes sense! This is happening more and more. You will find that many banks are looking for new products to capture that market of low dollar trade settlements.

L/C Processing, Discrepancy Rates and ISBP

Import and Export L/C processing figures are also interesting. Fortunately, the numbers pretty much speak for themselves, in that one bank's import increase (57% report increase) is another bank's export increase (61% report increase). 26% report a volume of imports and exports equal to 5 years ago.

With the exception of Western Europe, each region reports a higher level of import and export L/C processing than 5 years ago. Consistent, but it would be good to know who is reporting especially as we have instances such as in the US market where the top five bank issuers of commercial L/Cs account for almost 80% of the dollar outstandings. *(DCW April 2005 Statistics US Banks 4Q 2004. JPMorganChase, Bank of America, CITIBANK, Wachovia, and Bank of New York report over $21 billion outstanding in commercial L/Cs; top 300 issuers report $27 billion outstanding.*)

This is a definite case of the 6-foot statistician drowning in a stream 3-foot deep. Curiously, those same five banks account for 60% of the standby dollar value outstanding. *(DCW April 2005 Statistics US Banks 4Q 2004. JPMorganChase, Bank of America, CITIBANK, Wachovia and Bank of New York report over $ 204 billion in standbys out of a total $331 billion.)*

In such situations, it is unfortunate that the respondents to the Survey must remain anonymous. I have not found similar reports which would allow a comparative market share size for Europe and Asia but my instinct tells me it is comparative. Parenthetically, we know that some major vendors must believe this market share argument as they have targeted their product for the ten to twelve global “market drivers.” We don’t want the tail wagging the dog, do we?

What can we say about discrepancy rates? While discrepant presentations continue to exceed compliant presentations, the gap has narrowed significantly. This most recent Survey shows a clear improvement from the 2003 Survey. *(DC-PRO Market Intelligence Survey 2003. 62% export and 56% import versus 56% and 52% in 2005.)* When comparing these numbers on a regional basis and attempting to determine quality of presentation of a particular region, we must remember that import numbers reported by banks in North America, for example, reflect the quality of documents presented - not by North American importers or exporters but by their trading partners in other regions.

Conversely, reported export discrepancy rates are more likely to reflect the quality of documentary presentations in the reporting region, unless of course export documents are processed in another “Survey” region.

Respondents note the same phenomena; one comments: “It depends on the origin - European and Korean documents generally contain fewer discrepancies.”

Other interesting respondent comments:
(a). *“The figures exclude those import bills that have delivered goods under shipping guarantee. The shipping guarantee accounts for 25% of our total transaction number.”* Does this mean that the respondent bank does not examine documents presented after issuance of a shipping guarantee?

(b) *“These percentages decrease to less than 10% after first examination and corrections from the beneficiary.”* Wow! Does that mean that had beneficiaries paid more attention to document preparation they could have avoided the discrepancies and the discrepancy fees?

(c) *“The majority of discrepancies are found in transport documents, especially in CMR and B/L.”* There may be several reactions to this comment: (1) the L/C does not require the transport document which correctly reflects the shipment, (2) transport document issuers are not familiar with UCP 500, and or (3) bankers are not familiar with transport documents. Take your pick or propose another.

To what can we attribute this improvement in document presentation? Less than half the respondents credit ISBP. Polls taken at global venues of the Annual Survey of L/C Law & Practice support the respondent view that ISBP is used more within and between banks than with applicant and beneficiaries. In fact, very few banks have offered training or education to their customers in ISBP. Trying to put all this in perspective, can we conclude that many discrepancies were bank created by overly zealous or conservative applications of UCP 500 or as one respondent commented: “We have experienced that it is almost impossible to avoid rejections of documents from Western European banks acting as Confirming Bank. We always have to fight to achieve compliance.”

Bankers have always known that some of their brethren have used poor letter of credit decisions to compensate for poor credit decisions.

In addition to the respondent comments supporting the view of “bank causal and bank cure,” I would point to several other initiatives contributing to an improvement in document presentation: (a) the transfer of L/C staff to sales and “advisory” roles working with importers and exporters to review L/Cs and (b) as will be shown in Section 4 of this Survey, pre-examination of documents and use of document preparation services.

I think that every commentator in cases such as this likes to end their piece with something prophetic. In 2003, I ended my commentary with the following:

> Where does L/C go from here?
> There are those users who swear by L/C and those who swear
> at it! … Is L/C becoming or has it already become a commodity?
> How can you differentiate your L/C from your competitors’ L/C?
> Can your bank afford the investment in technology to keep up
> with the competition? Do your customers want technology and
> if so, are those demanding technology willing to pay for it?

Aside from a few updates on possible new solutions to replace L/C and or to keep banks intermediated in the process (SWIFT’s Trade Service Utility. See www.swift.com), respondents clearly recognise that the cost of L/C and the frustration with it as a payment mechanism are driving users to less expensive alternatives - even where those alternatives have greater risk attached. It has been reported that L/Cs now account for approximately 11% of world trade payments; ten years ago that figure was approximately 17%.

I believe that the trends identified in this Market Intelligence Survey regarding concentration, capacity and costs, people and technology, whether for banks to stay in the trade business or for the commercial parties seeking to mitigate risk, will force banks to reconsider their role: will banks own the customer or the delivery system or will some banks own both?

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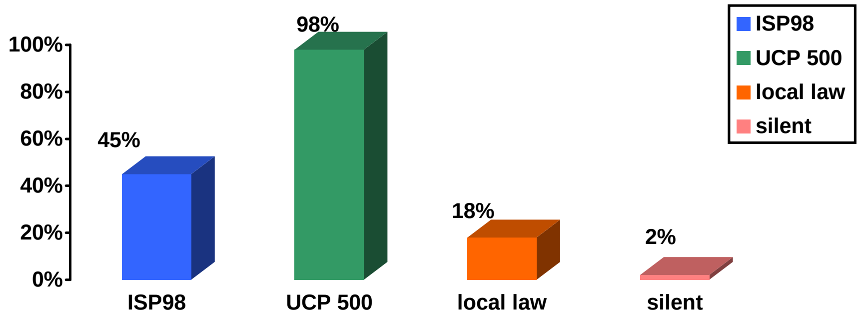
3. Rules and Practice

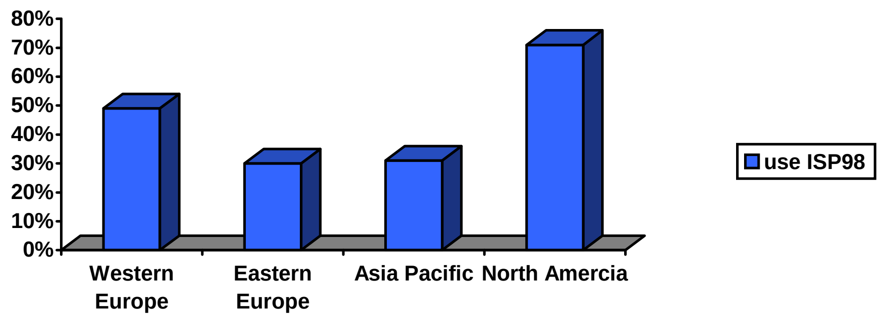
3.1 Standby letters of credit

The vast majority of departments issue standby credits subject to UCP 500. Almost half also issue standbys subject to ISP98.



45% of departments issue standbys subject to ISP98
98% of departments issue standbys subject to UCP 500
18% of departments issue standbys subject to local law
2% of departments issue standbys that are silent as to governing rules/law

Regional comparisons



71% of departments in North America issue standby credits subject to ISP98
49% of departments in Western Europe issue standby credits subject to ISP98
31% of departments in Asia Pacific issue standby credits subject to ISP98
30% of departments in Eastern Europe issue standby credits subject to ISP98

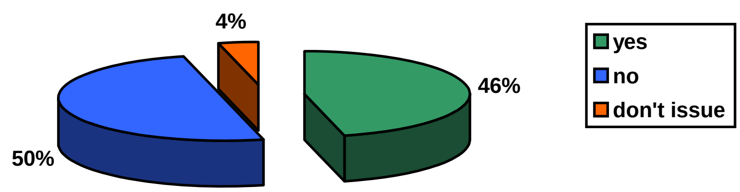
“It's still not the practice in Asia to issue Standbys subject to ISP98.”

“ It is our policy to issue Standby LCs subject to UCP500 rather than ISP98.”

“In many cases subject to ISP98 or UCP 500 and to local law for matters not cover by I.C.C. rules.”

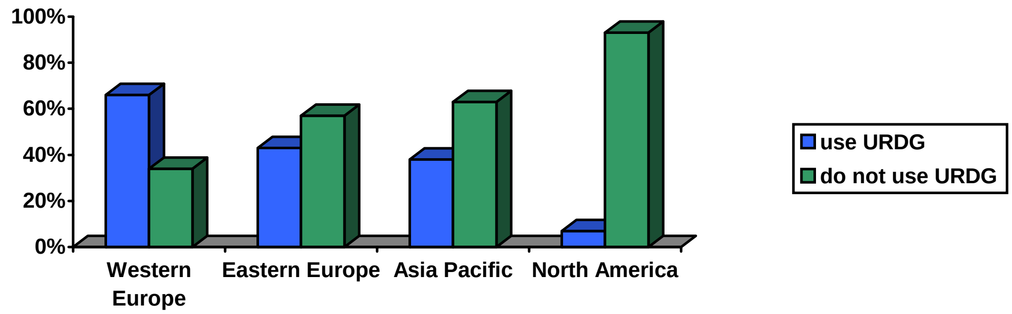
3.2 Uniform Rules for Demand Guarantees

Almost half of the departments surveyed indicate that they issue guarantees subject to URDG 458.



46% of departments issue demand guarantees subject to URDG 458
50% of departments do not issue demand guarantees subject to URDG 458
4% of the departments surveyed do not issue demand guarantees

Regional comparisons



66% of Western European departments issue guarantees subject to URDG
43% of Eastern European departments issue guarantees subject to URDG
38% of Asia Pacific departments issue guarantees subject to URDG
7% of North American departments issue guarantees subject to URDG

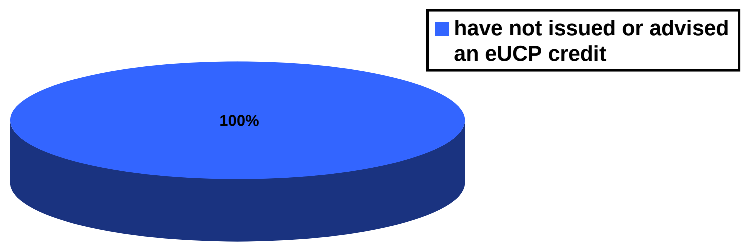
> *“URDG are used when a "straight" guarantee is issued i.e. not using another bank to intervene in any manner. Most of our guarantees are counter-guarantees.”*

> *“Our bank issue guarantees for local beneficiaries more than for foreign beneficiaries.”*

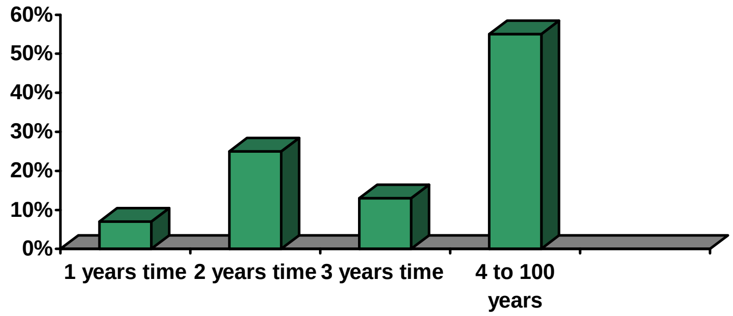
> *“Many still prefer issuance of guarantees subject to local law.”*

3.3 eUCP

None of the respondents have issued or advised an eUCP credit.



Expected timing of the use of eUCP



The majority of respondents feel that it will be over 4 years before they issue an eUCP credit.

"It depends on too many factors outside of the bank's control."

"We don't think it will be the practice in the market in near future unless the environment matures and the demand from customers is great enough."

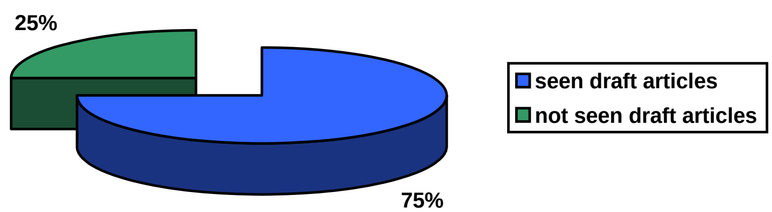
"Our bank is already equipped for processing eUCP credit. However clients and correspondents are not yet willing to use eUCP."

"I do not know, but I will most likely have retired when they start."

"Local Law does not allow it."

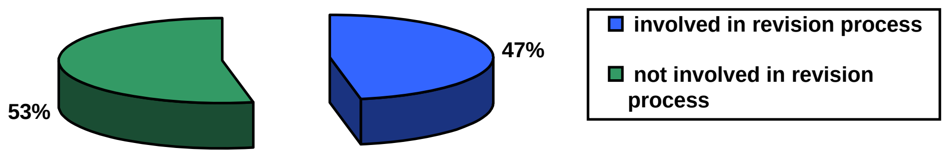
3.4 UCP revision

A large majority of respondents indicated that they have seen draft articles relating to the revision of UCP.



75% had seen the draft articles relating to the revision of UCP
25% had not seen the draft articles relating to the revision of UCP

Involved in the UCP revision



47% are involved in the revision process
53% are involved in the revision process

Selection of comments on the UCP revision

> *“Amongst many important changes that we have proposed, the most important is the one referring to "negotiation". In our opinion it is obvious that "Negotiation" is clearly defined as an act taking place outside the credit and without protection of UCP.”*

> *“ With numerous court cases relating to "Negotiation", UCP needs to elaborate and define in detail what constitutes a negotiation of documents/drafts.”*

> *“I would prefer negotiation to be more clearly defined/explained to avoid having discrepancies.”*

> *“Try to delete "Negotiation".”*

“Delete Negotiation.”

“The clear definition and understanding by the bank community of "negotiation".

“I would welcome a clearer definition of negotiation and a solution to the dilemma of discounting deferred payment LCs.”

“More precise wording for 'negotiation', 'original documents' and 'on their face'.”

“More accuracy and conciseness would be nice so that any confusion would be avoided.”

“Inclusion by reference to the ISBP. Greater mandatory rules. Less "should", "may" etc. and more "must".”

“Avoid the use of double negatives - state the articles in positive words.”

“On board notation requirements need to be simplified - Date and notation of "on board" irrespective of place on the face of the bill of lading should be sufficient.”

“I would add instruction about the language of documents. "The documents must be made out in English language, if it is not otherwise requested or accepted by the credit'. It is always a matter of discussion in what language the documents may be presented. Some banks say that they can examine documents made out in Russian and some banks refuse documents in Russian. So adding this clarification would help banks to avoid any misunderstanding.”

The clause that causes regular problems is the one under art 13 of UCP i.e. "Documents which appear on their face to be inconsistent with one another will be considered as not appearing on their face to be in compliance with the terms and conditions of the credit”

“Discrepant documents and waiver.”

"UCP as it stands is fine. Any changes should be made to simplify as much as possible the use of LCs in order to make them more competitive/attractive compared to other means of payments (open accounts for example)."

"I would not change anything. I don't think it needs to be revised."

"I am OK with current version of UCP."

"Better representation of exporters and importers views."

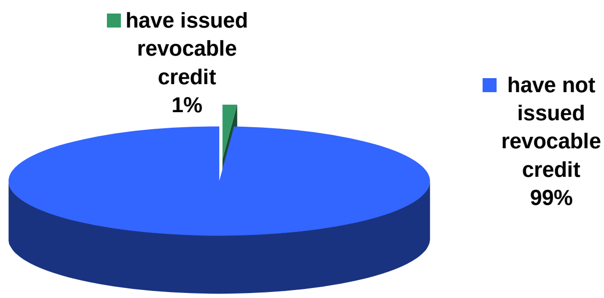
"Bring clarity to article 48."

"Remove reference to Standby LCs."

"Clarification of negotiation and pre-financing!"

3.5 Revocable credits

The vast majority of departments have not issued a revocable credit in the past 5 years.



99% of LC departments have not issued a revocable credit in the past 5 years
1% of LC departments have issued a revocable credit in the past 5 years

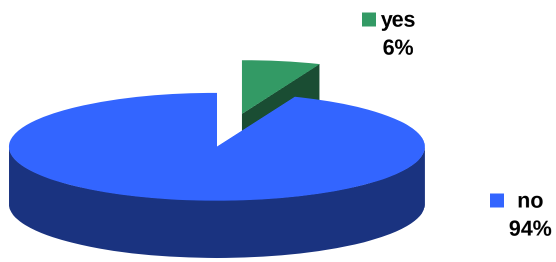
> *"Our customers and beneficiaries refuse to accept Revocable LCs.".*

> *"Revocable and LC are a contradiction. No wonder it is not popular."*

> *"I may say that I didn't see one in the last 15 years."*

3.6 Non-bank issued letters of credit

The majority of departments have not facilitated the issuing or advising of a non-bank LC.



6% of LC departments have facilitated the issuance or advice of a non-bank LC
94% of LC departments have not done so

Facilitation of the issuance/advising of non-bank LCs was reported in North America and Asia Pacific but not in Western or Eastern Europe.

> *"Advising only. Some of these issuers are subsidiaries of the banks in fact. The reasons of setting up such independent companies may be for regulatory or tax purposes."*

Commentary by Kim Christensen

Kim Christensen is Trade Finance Business & Product Specialist with Nordea - the leading financial services group in the Nordic and Baltic Sea region with approximately EUR 284,2 billion in total assets and a world-leading Internet banking and e-commerce operation with 4.1 million customers.

On behalf of the bank he holds seminars and presentations on various subjects within international trade. He is a member of the ICC Commission on Banking Technique and Practice, and serves as a contributing editor to LC Monitor (a legal/ financial journal covering the use of payment instruments in international trade) and is part of the editorial board for LC Views, an international learning magazine for and by LC specialists.

Introduction

Throughout the L/C community there is constant discussion concerning every conceivable L/C issue. You do not have to look further than to the DC-PRO Focus Discussion Forum to confirm this. The word "discussion" is one we are fond of. It gives us the feeling that we are indeed open to other people's views. I have seen "discussion" defined as "*…an exchange of views on some topic...*" Without wishing to start a new "discussion" I believe that we are in fact rather bad at discussing things - in the sense that we do not really "exchange" views. We "fire" our own (standard) opinions out as hard as we can and very often do not take other peoples views into account or adjust our own views based on discussion. If at some point we are caught in our own arguments, we will simply close the discussion with a statement like *"I accept your arguments, but I reserve the right to my own opinion".*

The latest – and very interesting – Survey from DC-PRO, hits right in the middle of some of the major "discussion areas" within the L/C community. The huge advantage here though is that the results are impartial and based on facts. No "gut feeling" or "experience" can alter these findings.

I have been given the privilege of providing commentary on the "Rules and Practice" section and so run the risk of initiating even more "discussions" by providing my own views on the findings. If that is the result, I sincerely hope that it initiates discussion in the true sense of the word - "an exchange of words that will bring all parties forward" – and helps towards improving the L/C as an instrument worldwide.

Standby Letters of Credit / Uniform Rules for Demand Guarantees

The first issue on my list from the Survey is Guarantees, including where it is "wrapped" in the L/C format: the Standby L/C.

Basically three sets of standardised rules "fight" to win the favour of the user: UCP 500, ISP98 and URDG. In addition to these come the deals subject to local law and the ones silent to governing rules/law.

The result – a bit sad, but hardly surprising – tells us that even though the rules specifically designed to cover these transactions are in fact being used, they do not seem to be “first choice”.

This becomes very obvious when viewing the results for standby letters of credit. Almost all respondents (98%) indicate that they issue standbys subject to UCP 500; while less than half (45%) issue standbys subject to ISP98, and 20% issue standbys subject to local law – or are silent as to governing rules/law.

To me this indicates that roughly half of respondents use only UCP 500, while the other half use UCP 500 and “something else” e.g. ISP98. This means that in most cases UCP 500, designed for commercial credits, is being used as first choice for standby credits.

The picture is more or less the same with Guarantees – except that there are no “UCP 500 like” rules to steal the picture. URDG “fights” local law – and the result is almost even (46/54).

The regional differences here are very interesting: ISP98 is very popular in North America (71% issue standbys subject to ISP98), but have gained limited success in Asia Pacific and Eastern Europe (31% and 30%).

When it comes to guarantees the regional differences are even more distinct: they are hardly used in North America (7%). This is not so surprising considering the history in North America of issuing standbys rather than guarantees. However, 66% of the Western European respondents show that things are moving in the “right direction” and have issued guarantees subject to URDG 458. At this point it is appropriate to mention the ICC Task Force on URDG, who are doing a huge job in widening the usage of URDG.

It seems very clear to me here that old habits die hard. If you are used to using a specific set of rules, you do not change to another easily. My advice for banks is to evaluate their own “strategy” in this area, and ask the question… is this “reasonable”? Which sets of rules are most appropriate for Standbys and for Guarantees?

I suggest that banks reach the conclusion that ISP98 and URDG should be first choice, and consequently assume the responsibility of driving this: e.g. on their internal applications and when advising their customers.

eUCP

The pie chart showing the usage of the eUCP is perhaps better than any comment I can give: a large round zero :-)

In any case, the status is very clear: none have been issued by any of the respondents.

In the previous LC Market Intelligence Survey, carried out in February and March 2003, 41% of respondents indicated the intent to issue an eUCP credit in 2 years. These 2 years have now passed, but none have been issued. It seems that respondents were far more optimistic regarding the eUCP 2 years ago.

Indeed, I believe that the L/C Community has been caught by the urge to predict when eUCP/electronic documents will be introduced. Basically every prediction that I have seen on the subject has been wrong (although hindsight is 20/20 vision). In that perspective there is nothing surprising or for that matter embarrassing about the result from 2003.In the present Survey you will notice that "only" 32% now indicate that eUCP credits will be issued in 2 years. The majority (55%) indicate that this will take 4 years or more.

The question of timing has been posed many times since the eUCP was launched in 2002. It seems to me that this is the wrong question! There is no doubt in my mind, that at some point in time documents will be available in an electronic format. It is equally clear to me that this will happen - when it happens! Therefore the right way to go about this may not be to ask the question "*when will eUCP happen*", but rather analyse "*how is the L/C area to be innovated*". One place to start is at the "Trade Development and Technology" section of this Survey where some interesting trends can be identified. However, this is outside the scope of this commentary.

Many of the comments given by the respondents in relation to the eUCP sound like excuses – for example…"*It depends on too many factors outside of the bank's control*" and "*We don't think it will be the practice in the market in near future unless the environment matures and the demand from customers is great enough*". Although I am sure that the drafters of the eUCP regret this result, they need not feel sorry - as long as the L/C Community takes responsible steps to innovate the L/C area and to address the challenges facing us.

UCP Revision

The UCP revision is upon us. It seems that a huge part of the L/C community has been mobilised to adjust these universal rules: 75% have seen the drafts, and 47% are involved at some level in the revision process.

More or less every discussion and article relating to L/C issues somehow turns to the UCP revision; with advice and/or comments on what should be dealt with, and what direction it should take. Interestingly enough the questions asked here in relation to the UCP revision have generated the largest number of comments of any of the questions in the Survey. Clearly indicating that the interest in the Revision is significant.

Within the comments on the UCP revision, there are a lot of "bad discussions" (in reference to my introduction). The worst – as I see it – is the one on "negotiation". About one third of the comments relate to "negotiation". It is however, a perfect example of a topic where argumentation seems to have lost all meaning.

Too many have said too much, too loudly. So, instead of a fruitful discussion based on debate, we now seem to have a battle of principle, a battle of right and wrong. And it seems that "right" or "wrong" will be determined by national votes within the ICC Banking Commission. I would most certainly have preferred a "solution" based on argumentation.

Other topics are mentioned in the comments and all in a fine line from the topics discussed within the L/C Community: refusal of documents, clarity of wording and definition, examination of documents, transferable credits etc.

Funnily enough, there is one topic that is NOT mentioned in the comments on UCP but was included as a question in this Survey: Revocable credits. I have heard L/C professionals argue that revocable credits should remain in UCP in order to keep issuers form inventing their own rules. However, no matter which view you hold in

relation to revocable credits, it is an undeniable fact that this type of credit is simply not being used anymore. This survey says that 1% of the respondents have seen one in the last 5 years! While I am sure that there were good reasons for revocable credits being covered in UCP 500 (e.g. for international intra-company/group deals where one country would require the usage of a L/C for exchange control purposes), the results of this Survey will surely make it more difficult to argue strongly for their retention in the revised UCP.

Non-bank issued letters of credit

From an L/C perspective this is a rather new phenomenon. The issue was raised in the Banking Commission in 2002, and a resulting ICC Opinion was made available on the ICC website. The conclusion of which is quite clear: there is nothing in the UCP 500 that prevents the issue or advice of Non-bank L/Cs. This does however raise some interesting issues e.g. whether or not it is sufficiently clear who is obligated under such credit.

The fact remains, that these credits exist…though apparently not in very large numbers. Only 6% of the respondents report that they have issued/advised such credits and their use would seem to be predominantly within North America and Asia Pacific for the time being.

These credits cover a need that exists in the market, and it is therefore likely that they will be issued whether or not the banks and/or SWIFT endorse them. From that perspective, it would seem to me that it is better that they are handled by professionals and using standard rules. In addition to that…. it is business! I just wonder when/if they will be seen in significant numbers within Western Europe.

Conclusion

It seems that there are great differences as to the “acceptance” and use of the various rules. It is hard to find logic behind some of the choices – other than the logic of habit. I am sure that most L/C professionals would agree that it is preferable to issue standbys subject to ISP98 rather than UCP 500 – or for that matter local law.

With this survey, we hold in our hands the figures that show the current picture. So the question now is what we want to do about this? One course of action is to examine why the results are as they are. More interestingly perhaps is to discuss how to change practice in a direction that is best for the L/C community.

There is also a major lesson to be learned from the results of the Survey in relation to the UCP revision. The mission is not complete on drafting the revision. The new rules must then be “sold” to the entire L/C community to ensure their widespread acceptance and use. That is the real task.

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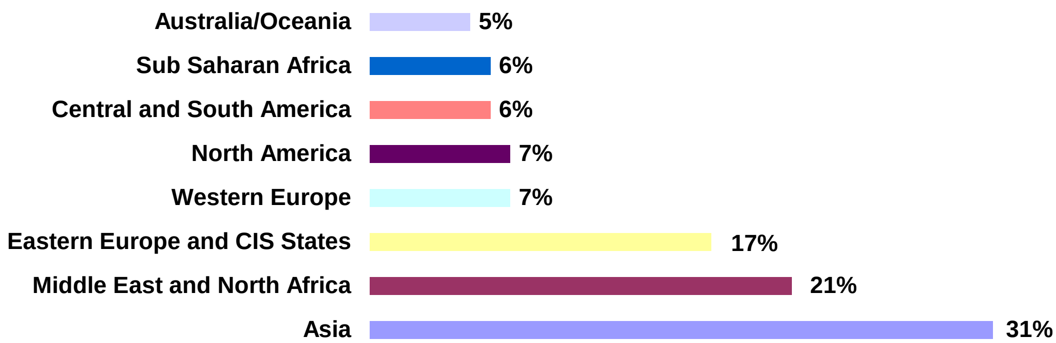
4. Trade Development and Technology

4.1 Markets with most potential

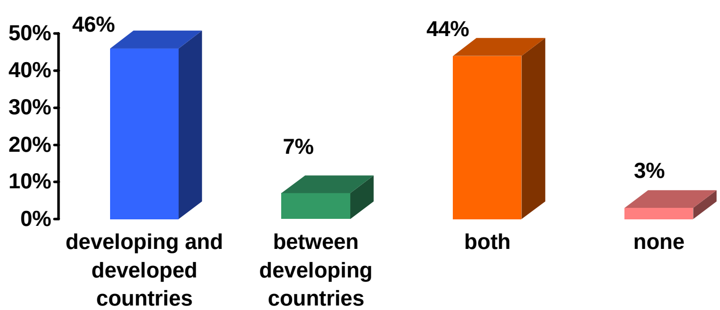
The top 3 markets with most potential for the development of letter of credit activity as indicated by respondents are 'Asia', 'Middle East and North Africa' and 'Eastern Europe and the CIS states'.



31% of respondents indicated Asia as the market with the most potential for the development of Letter of Credit business
21% indicated the Middle East and North Africa
17% of respondents indicated Eastern Europe

Growth areas

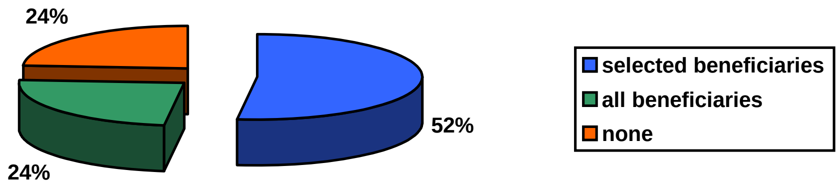
The majority of respondents see the greatest growth potential for letter of credit activity between developing and developed countries.



46% saw trade between developing and developed countries as the area of greatest growth potential
7% of respondents saw trade between developing countries as the area of greatest growth potential
44% of respondents saw both categories as having equal growth potential
3% of respondents did not see any growth potential in these areas

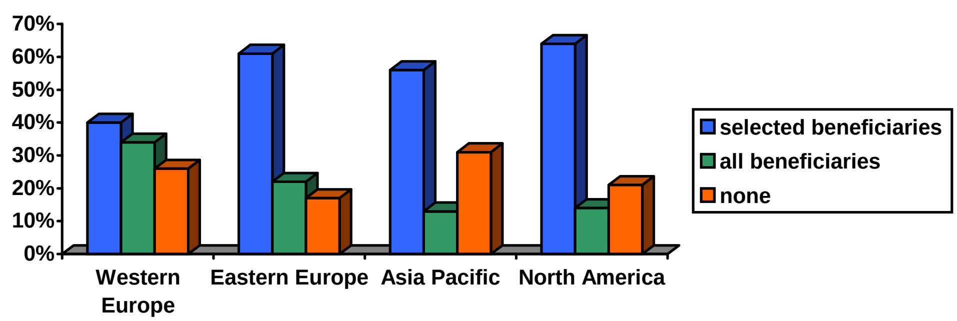
4.2 Document pre-checking services

Over 75% of departments offer some level of document pre-checking facility to their customers.



52% of departments offer document pre-checking services to selected beneficiaries
24% of departments offer document pre-checking services to all beneficiaries
24% of departments do not offer any document pre-checking services

Regional comparisons



"Only for some cases and often special agreements."

"We normally do it for an extra fee."

"We help and give consultations to all our customers under commercial LCs for correct preparation of documents."

"We don't say it in so many words, but informally we do it as part of the service."

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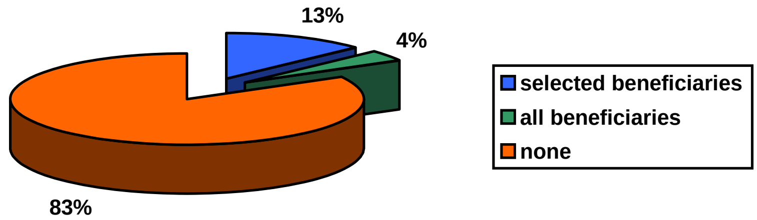
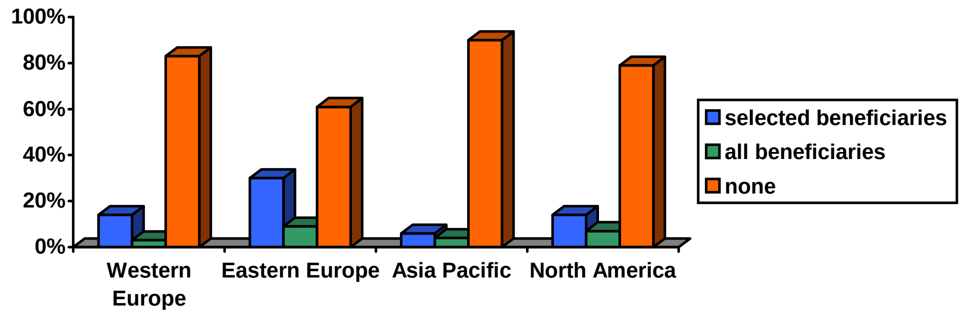
4.3 Document preparation services

The majority of banks do not offer any document preparation services to their customers.



4% offer document preparation services to all beneficiaries
13% offer document preparation services to selected beneficiaries
83% do not offer any document preparation services

Regional comparisons



> *"We refer to a document preparation service company we work with. We are investigating other options."*

> *"We will offer that service after implementation of our new software."*

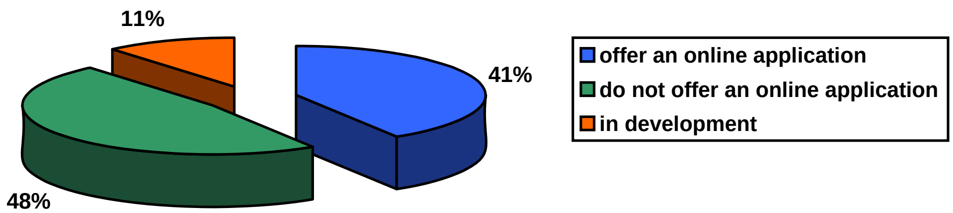
> *"It is the beneficiary's responsibility to prepare the compliant documents under LC. Meanwhile our bank can prepare the drafts for the beneficiaries."*

> *"No, but we propose it in a defensive way through a logistical company.."*

> *"Though we have no such service at this moment, we are evaluating the possibility."*

4.4 Online LC application

Less than half of departments offer customers on online LC facility. However, a number of banks are in the process of developing a solution.



41% offer customers an online LC application form
48% do not offer customers an online LC application form
11% are developing/evaluating an online LC application form/service

Of the departments who offer an online LC application form:

- an average of 39% of their customers use the online form for applying for their LCs
- an average of 49% of the total number of LCs issued are handled through the online application

> *"Though no such service exists at this moment, we are evaluating the possibility."*

> *"We began in 2004 and focused on the heavy users. More or less all import LCs are received electronically; if they are not then there better be a good reason."*

> *"We expect to have an online application within the next six months."*

> *"We are going to implement a new online system within two months."*

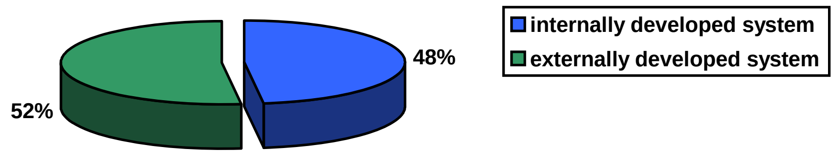
> *"We are in the process of making one available to customers."*

> *"We expect to start with an online application from the 4th quarter 2005."*

> *"We are implementing such an application during 2005."*

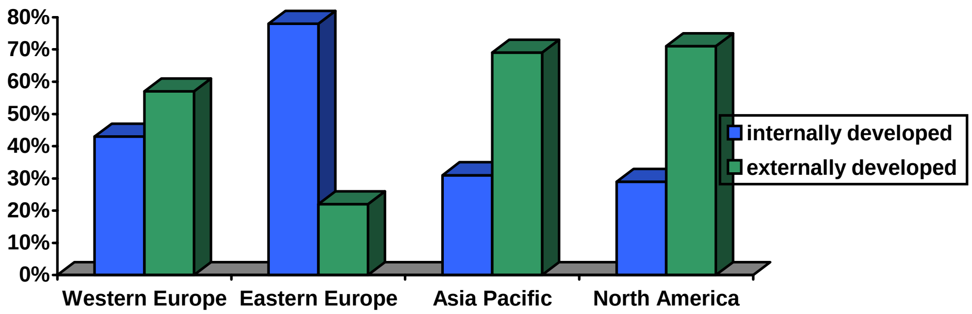
4.5 Trade processing systems

There is an almost even divide between departments that use an internally developed trade processing system and departments that use an externally developed system.



48% use an internally developed trade processing system
52% use an externally developed trade processing system

Regional Comparisons



North American departments indicate the highest usage of externally developed systems.

Eastern European departments indicate the highest usage of internally developed systems.

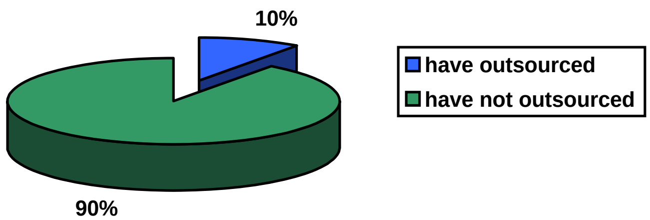
The system providers indicated were:

AMS
China Systems
Cibar
CSI
Eximbills Technologies Ltd
i-flex solutions

Misys plc
SmartStream Technologies
Surecomp
Temenos Systems
TD Commercial Banking

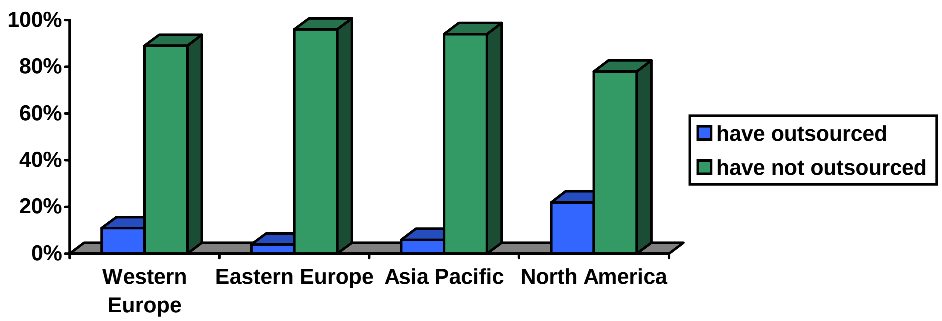
4.6 Outsourcing/Insourcing

The majority of banks have not outsourced or insourced any aspect of their trade finance services.



10% have outsourced
90% have not outsourced

Regional Comparisons



North American departments indicate the highest levels of outsourcing with 22%.

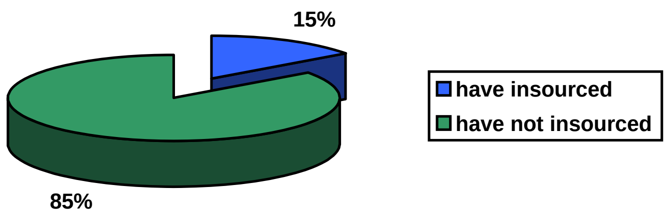
"Some aspects of LC trade processing is done through our affiliates in Asia"

"Centralisation but no outsourcing"

"We have outsourced the issuance and checking of documents."

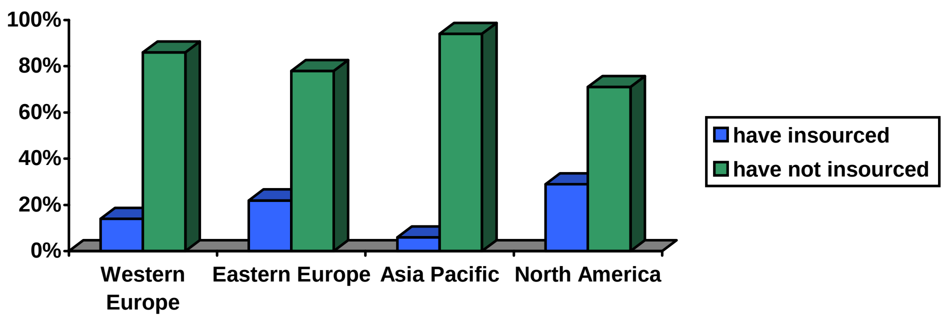
"Our Import LC business has been completely outsourced"

Insourcing



15% have insourced
85% have not insourced

Regional Comparisons



"We insource processing from our own bank (other branches) and plan to extend to other banks."

"We provide trade processing for smaller downstream correspondent banks including the issuance of commercial (import) letters of credit."

"A small number of LCs received from smaller local banks."

"We will do that after implementation of our new software."

4.7 Key challenges to the industry

The Survey received a very large number of responses in relation to the question: what is the key challenge facing the letter of credit industry?

The responses addressed varied issues but the vast majority could be categorised into three broad headings:

1. Competition (from inside and outside the banking industry)
2. Application and revision of UCP
3. Advances in technology

The following are a sample of the responses received:

Competition

“The fact that more companies are using open account terms ahead of L/Cs is having a big impact on the L/C industry.”

“Pricing competition from other financial institutions (including non-banks) is the key challenge to the industry.”

“The movement to other payment mechanisms as relationships between buyers and sellers mature is the greatest challenge.”

“As there is keen competition amongst all banks for L/C business, every bank is trying to lower pricing in order to attract more business in spite of whether the fees earned from the transactions justify operational costs.”

“While cost is a factor in L/C operations, the "KYC" principal is also an important factor. With the speedy evolution in technology - especially in communication channels - trading partners are better able to build stronger relationships and assess each other’s credit-worthiness and integrity. This reduces the need for third party participation in a transaction such as opening L/Cs to facilitate trade.”

“Businesses are now flourishing on open account basis. Somehow, traders increasingly believe that L/C is not the mechanism to use for settlement of international trade transactions. The outright rejection of documents on the basis of perceived discrepancies and the inherent delays in eventual settlements dissuades traders from going for L/C solutions. That's still the biggest challenge.”

“Cost is one of the major considerations for businesses when deciding to use (or not to use) L/Cs as their payment instrument.”

"Non-bank L/C clones are gaining more market share (electronic solutions similar to L/Cs in structure but not including obligation of a bank)."

"The popularity and trend towards settling trade on open account terms seems to be gathering pace. The L/C mechanism should be simple and practical enough to retain its primacy as the international trade finance settlement tool."

"The key challenge is the general move toward open account business."

"It is a great instrument but it needs to be "modernised" in order to combat the competition from other payment methods (open account)."

Application and revision of UCP

"The instrument (LC) must be made less cumbersome and easier to understand and use."

"Some banks use the grey areas of UCP to rejected documents. This must be addressed in the new UCP."

"The revision of UCP 500 is crucial and must include today's customs and practice instead of a theoretical approach based on anticipated ideas. Clear definitions, and the straightforward wording of articles should contribute to a more attractive set of rules that will help to promote L/C business. We must learn from experience to avoid situations where we need publications like ISBP and (so many) opinions and decisions from the ICC."

"We must standardise the interpretation of UCP."

"The high rate of non-compliant documents has to be addressed."

"In my opinion the key challenge facing the development of the Letter of Credit industry is improvement of the Rules and Practices. The ICC Opinions are too numerous so the rules can now be double-edged. Objectivity in interpretation is a big problem of L/C business. ISBP is helping with this."

"The UCP rules must be revised so that exporters and importers can more easily use them. At present they are designed for use by bankers - almost to the exclusion of exporters and importers."

"Letters of Credit have to be simplified and standardised."

"We need to standardise the issuance of L/Cs and eliminate non-payment on the grounds of frivolous "discrepancies" whenever the applicant decides not to pay."

Advances in technology

"The key challenge for our industry is the battle between the paper-based traditional L/C (which will exist for many years) and the growing demand for fully electronic solutions."

"In my opinion, the key challenge for the next decade will be the processing of eUCP credits and e-documentation, specifically between developing and developed countries."

"I think that the development of simpler and cheaper alternative payment instruments - pushed by electronic trade - is the key challenge to the industry. Though eUCP is an attempt to catch up with developments in technology, I think it is not enough to meet the requirements of changing market conditions."

"Technology continues to evolve faster than financial institutions are able to alter their systems."

"The development of a new electronic "light" L/C is the key challenge facing our industry."

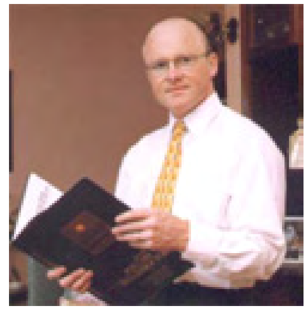
"Technology must be embraced - online applications and tools (such as the eUCP) have to be developed and the dematerialisation of documents has to be promoted."

"The key challenge facing the industry is the movement toward e-commerce."

"The presentation of paper and electronic documents must be standardised."

"Technology, which efficiently combines the management of client materials, control of credit lines, L/C issuance, document checking and communication with the relevant institutions (such as insurance companies, shipping companies and customs, etc.) must be developed and available for use universally."

Commentary by Vincent O' Brien



Vincent O'Brien is an experienced International Trade Banking Specialist with over 20 years international experience with banks in Europe and the United States as well as significant consulting and training experience in more than 30 countries worldwide. Vincent works with leading banks and development agencies in the establishment of trade finance operations in emerging markets as well as the development of technology driven trade finance training structures.

During the calendar year of 2004 Mr. O'Brien delivered technical training workshops in 21 countries that were attended by more than 1000 participants from approximately 400 banks.

Vincent is the examiner in the Finance of International Trade with the Institute of International Trade of Ireland. He is a regular contributor to international trade and payment publications such as 'Documentary Credit Insight' of the International Chamber of Commerce (ICC).

Vincent provides the Documentary Clinic in the International Payment Journal 'Letter of Credit Monitor'. In 2004 Vincent was presented with the award as Best Trade Finance Consultant by the European Bank for Reconstruction and Development in recognition of the results achieved in developing interregional and international trade under the EBRD Trade Facilitation Programme.

This final section of the Letter of Credit Market Intelligence Survey 2005 examined trends in trade development and looked for feedback on the application of technology in trade processing.

Trade Development and Technology may at first appear as strange "bedfellows" but these two elements are now more than ever intrinsically linked in the evolution and facilitation of world trade.

The advent of the internet and advances in technology have greatly enhanced the ability of traders to communicate in a cost effective manner. Traders from all corners of the world have grasped the opportunities provided by improved communications and we are now seeing positive trends in world trade. We can see this correlation by just looking at what is happening with reported Global trade flows.

Figures from the World Trade Organisation (WTO) show that nominal world merchandise trade growth reached 21% in 2004, which was the highest growth rate in 25 years. On more detailed examination we see that this surprisingly positive figure was due to a combination of a strong real trade growth figure of 9% and the sharp increase in dollar prices of 11% in 2004. Nevertheless, they represent impressive growth figures by any standards.

Market Potential

It is no great surprise that respondents to this 2005 LC Market Intelligence Survey see Asia as the market offering most opportunity for the development of letter of credit activity. The Asian markets have been and will remain key LC markets despite challenges from other methods of settlement. According to WTO figures, the Asian region recorded the highest volume of real merchandise export growth in 2004, at

14.5%. China, the Republic of Korea and Singapore recorded rates in excess of 20%. These three markets are strong LC users with the dominant activity of China in

trade related and trade finance activity becoming ever more transparent. Moreover, in 2004, China advanced to be the third largest exporter in world merchandise trade having already become the third largest importer in 2003.

The letter of credit may be losing ground to other methods of payment in securing and financing a proportion of the growing global trade market but what we are experiencing is more of a natural shift in market focus. Make no mistake LC volumes are on the increase, perhaps a more moderate increase than actual trade growth but nevertheless, are on the increase.

The recent progress of developing countries in expanding their merchandise trade is not only impressive but bodes well for the survival and evolution of the LC. We must look to the developing countries for this important trade business. Developing countries saw their share in world merchandise trade rise sharply in 2004 to 31%, the highest since 1950 (WTO figures released 14 April 2005).

I was a little surprised that respondents put the 'Middle East and North Africa' ahead of the 'Eastern European/CIS States' and 'Central and South America' as markets for LC potential.

From my experience with Trade Facilitation Programmes in 'Eastern Europe and CIS States', 'Asia' and 'Central and South America' I know that significant resources are being made available to emerging banks interested in developing trade finance activity in those regions. I am convinced that similar resources must be made available to all developing regions for trade to continue to grow.

Document pre-checking and preparation

With consolidation in the banking markets and margins under pressure, banks are looking to value added services to gain or retain the larger corporate customers. With the consistently high level of discrepancies in documents, an obvious target for banks is to provide some form of pre-checking or document preparation service to the exporting beneficiary.

In fact, some banks have strategically targeted 'doc-prep' and integrated this service into their international trade services business plan. With other banks the pre-checking of documents for selected beneficiaries has evolved into a full document preparation service.

Is this a wise move? Only time will tell.

Interestingly, 75% of respondents reported the provision of pre-checking facilities for their corporate customers but only 17% reported the provision of any form of hands-on document preparation services. This has a hint of 'look but don't touch'. Nevertheless, the trend towards 'doc-prep' services is continuing to gain momentum.

One point that I would like to emphasize to participants in the document preparation cycle is that there is a potential conflict of interest that arises when a bank acts out the role of document producer and confirming bank under the same credit. An imbalance of responsibilities can arise when the bank (confirming) that is providing its definite undertaking against complying documents is at the same time producing the documents prior to deciding on compliance.

If the risk profile of the issuing bank or its country deteriorates within the life of the LC, the bank may find itself charged with an over zealousness for discrepancies.

Many have argued that this can be managed through service level agreements. This may be true but I have a strong feeling that this hypothesis will be stringently tested in the courts in the not too distant future.

At a recent international conference in the United Kingdom, Ms. Danielle Austin, an international trade specialist who manages letter of credit presentations for a division of the Sikorsky Aircraft Company commented …"*Why would a serious beneficiary consider 'doc-prep' as it will involve duplication, loss of control of documents. It also adds an additional link in the logistics chain and we should not forget that commercial documents must fulfill compliance and regulatory requirements other than LC stipulations alone".*

However, from the results of this Survey it would seem that pre-checking and document preparation services are growing and making progress in the marketplace. Such services may also in time facilitate the use of electronic documents within the LC process as parties within the trade chain become familiar with the examination of electronic records that represent the physical pieces of paper that are produced for presentation under an LC.

Online Application – Trade Systems – Outsourcing and Insourcing

The Survey shows that 41% of respondents currently offer an online LC application to their customers with another 11% indicating that they are in the process of developing such a service. This is encouraging when compared to the previous Survey (2003) in which 33% of banks indicated that they offered an online application.

So now, more than 50% of the banks surveyed are acknowledging and/or experiencing the benefits that can be derived from online systems in terms of execution and management of trade services. Considering the relative ease in which such online services can be implemented - this is long overdue.

In relation to trade processing systems, it was interesting to see the relatively even balance between banks that use internally developed systems and banks that use externally developed systems. It appears that the external providers of trade processing systems are now taking the lead with 52% reporting trade processing through externally developed systems.

When it comes to the insourcing or outsourcing of bank trade processing then technological capability is always a key determinant. At first sight the reported figures for outsourcing of 10% and insourcing of 15% may not appear significant. However, the figures are significant because they point to an evolving trend in trade banking where the combination of advanced technology, skilled staff and re-engineered processes are yielding tangible benefits.

Banks with advanced technological capability are already providing 'white label' services to regional and local banks that wish to retain their core customer and credit relationship but that also wish to avoid further technology investment and benefit from outsourcing the labor and cost intensive trade processing functions.

Key Challenges to the Industry

This section of the 2005 LC Market Intelligence Survey gave respondents the opportunity to communicate what they see as the key challenges for the industry.

The number of responses and the obvious conviction of the respondents' views bode well for the future of the industry. We are a passionate lot.

Examining the responses a number of consistent points emerged:

Firstly, the importance of the current UCP revision process cannot be overstated. World trade is increasing and we have seen that the LC continues to play an important role in facilitating trade, especially for emerging/developing countries. However, while LC numbers remain positive it is clear that settlement by letter of credit is proportionately losing ground to open account and other less document and process intensive means of settlement.

Many respondents believe that this revision of UCP must transform the LC into a more streamlined and efficient trade settlement product. The rules must be express and unambiguous; the obligations of the parties must be clearly defined; and the language adopted in the rules must be clear for all practitioners in the trade chain regardless of their language or geographical location.

Without this progress the LC will lose credibility as a payment instrument and its equally important role in financing international trade will be diminished.

Secondly, respondents can see that all parties in the trade cycle are operating in a global environment. Traders operating in an increasingly competitive global market will not tolerate any rules or processes that impede trade flows, increase trade costs or are demonstrably unreliable.

Exporters, importers and their logistical service providers have made huge gains in terms of efficiency in the export-import cycle. This progress has in the main been driven by technology, shorter transport transit times and incredible increases in cargo capacity. However, despite many innovations within the banking sphere and ICC initiatives (such as the introduction of ISBP and the eUCP), the amount of work, the level of discrepancies and the delays and uncertainties reported in the industry have not been significantly reduced over the past thirty years.

It is time for change.

We will see fewer but larger players in the trade-banking sector. This is similar to developments in the transport sector. Many respondents see a medium term threat to the LC from the transport operators themselves who are close to the customer, close to the goods, close to the documents (paper or electronic) and have the capability to monitor delivery, documentation and settlement on a moment-by-moment basis. The level of intelligence available to the transport operators is incredibly valuable in the context of the assessment and control of payment related risk concerning the movement of goods across international borders.

Thirdly, many of our banking respondents already feel challenged by external competition within the marketplace in terms of pricing and cost management. A surprising number of respondents also gave indications of an emerging phenomenon of internal competition within their own financial organisation in respect of the value of the return on capital employed in the provision of trade services. A number of respondents indicated that Basle II remains unclear as to its implications for trade finance products - with some giving a negative impression as to its effects.

Finally, some respondents noted that developments in technology have not as of yet sufficiently impacted on trade work in terms of facilitating trade processing. They believe that technology is the way to simplify the LC process and that this is the number one challenge facing our industry.

It would seem to me from the comments provided, and from my own experience, that we are fast approaching a moment of truth for the letter of credit, with two possible outcomes:

One, the LC - driven by the current revision of the UCP rules and innovations in technology - will evolve into the reliable, efficient, cost effective, independent payment and finance instrument we all want it to be.

Two, the LC will demise as a payment instrument.

All our energy and resources must ensure that the LC not only survives but flourishes.

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IFSA – International Financial Services Association

The International Financial Services Association (IFSA) is a not-for-profit trade association whose members are international financial services organisations and suppliers to the industry. The IFSA's focus is on international financial services operations which include trade services products such as documentary credits, funds transfer, treasury operations, etc. In the 1920's, the IFSA created the first rules for the processing of letters of credit between banks. These rules were the model for the International Chamber of Commerce Uniform Customs and Practice for Documentary Credits.

The organisation was founded in 1924 and has been in continuous existence since that time. The IFSA provides a forum for members to meet and discuss the various issues related to their operations products. The IFSA's primary functions are education and representing the membership with international bodies as well as domestic US regulators. Much of the work of the organisation is carried out by volunteers who participate in technical committees. These committees are organized under the major product groups of Trade Services, Payments and Treasury and Regulatory and Compliance. Through these committees the organisation establishes operating rules and procedures for financial services institutions.

Each year over two thousand bankers attend IFSA programs. Over 350 financial services executives as well as about 250 vendors and suppliers attend the IFSA Annual Conference. The educational functions of the IFSA are provided by an affiliated organisation, the IFSA Foundation. The Foundation is an education and research organisation. In addition to the educational programs, the Foundation periodically does research projects for the industry. The IFSA in conjunction with the UK's Institute of Financial Services and the ICC offers a certification program for letter of credit professionals. Letter of credit practitioners are able to attain the credential of a Certified Documentary Credit Specialist (CDCS).

The IFSA actively participates in the International Chamber of Commerce Commission on Banking Technique and Practice working with them on the establishment and revision of international rules of practice for banks. Additionally, the organisation is active with the United Nations Commission on International Trade Law and participated in their creation of a Convention on Bank Guarantees and Standby Letter of Credit. The IFSA is involved on an ongoing basis with SWIFT, as well as other international organisations and banking associations throughout the world.

Website

For further information on the International Financial Services Association (IFSA), please see their website at: www.ifsaonline.org

EBRD - European Bank for Reconstruction and Development

The European Bank for Reconstruction and Development (EBRD) was established in 1991 to foster the transition towards open market-oriented economies and to promote private and entrepreneurial initiative in Central and Eastern Europe and the Commonwealth of Independent States (CIS). The Bank views international trade as a key part of the transition process.

The Trade Facilitation Programme

The EBRD's Trade Facilitation Programme (TFP) aims to promote foreign trade to, from and within Central and Eastern Europe and the CIS (the EBRD countries of operations).

Through the programme, the EBRD provides guarantees to international confirming banks, taking the political and commercial payment risk of international trade transactions undertaken by banks in the countries of operations (the issuing banks).
The programme can guarantee any genuine trade transaction to, from and within the countries of operations.

Over 79 issuing banks in the region participate in the programme with limits exceeding € 850 million. In addition, TFP includes over 475 confirming banks throughout the world.

The programme is an excellent business development tool. It provides:

- cover for a broad range of trade finance instruments;
- unconditional guarantees payable on first written demand;
- guarantees of up to 100 per cent of the face value of the underlying trade finance instruments;
- uncommitted trade finance lines and transaction approval on a case-by-case basis;
- attractive fee levels that are agreed separately for each transaction;
- a fast and simple approval procedure to issue guarantees; and
- short-term loans to selected local banks for on-lending to local exporters and importers.

Website

For further information on the European Bank for Reconstruction and Development and the Trade Facilitation Programme, please see their website at www.ebrd.com/tfp

ICC – International Chamber of Commerce

International Chamber of Commerce (ICC) serves world business by promoting trade and investment and open markets for goods and services, as well as the free flow of capital. It defends the private enterprise system and encourages self-regulation by business.

Founded in 1919, ICC is a non-governmental organisation of thousands of companies and business associations worldwide. ICC National Committees throughout the world present ICC views to their governments and alert Paris Headquarters to national business concerns.

ICC has top-level consultative status with the UN, where it puts forward the views of business in industrialised and developing countries. It also maintains close relations with the World Trade Organisation (WTO), the Organisation for Economic Cooperation and Development (OECD), the European Union, and other inter-governmental and non-governmental bodies. ICC permanent representatives at the UN in New York and Geneva monitor developments affecting business within the UN and its specialised agencies.

Specialist ICC Commissions meet regularly to review issues affecting business, among them banking, competition, the environment, financial services and insurance, intellectual property, marketing, air, maritime and surface transport, taxation, and trade and investment policy. Commission members include senior executives of major international companies, law firms, and academics.

ICC Commission on Banking Technique and Practice

The Commission on Banking Technique and Practice acts to prepare new uniform rules, to update existing uniform rules for documentary credits, collections and bank-to-bank reimbursements and to adapt international banking practices to automatic data processing techniques. It works in conjunction with the International Commercial Practice Commission and with other international bodies on demand guarantees.

Documentary credits, also called letters of credit, are one of the principal instruments for financing trade worldwide. Billions of dollars in products are traded internationally using documentary credits. Banks throughout the world benefit from ICC rules for international banking and trade finance, in particular regarding the use of documentary credits, demand guarantees and other trading instruments. ICC rules for letter of credit practice – the UCP 500 – have been cited as the most successful in the history of the harmonization of international trade practice.

Website

For further information on the International Chambers of Commerce and the Commission on Banking Technique and Practice, please see their website at:
www.iccwbo.org

DC-PRO

DC-PRO is the world's leading online Letter of Credit training and information resource. Launched in 2000, banks and companies in over 90 countries worldwide now use DC-PRO to meet their information and training needs.

DC-PRO makes understanding and keeping up to date with LC related issues easy by combining:

- essential letter of credit information provided by industry leading organisations (such as the International Chamber of Commerce and the Institute of International Banking Law and Practice)
- the expertise of the world's top letter of credit professionals

What services does DC-PRO provide?

DC-PRO Focus

DC-PRO Focus offers the most comprehensive store of on-line Letter of Credit information available. The information provided includes ICC Rules, Official ICC Opinions, News, ISBP, Legal Case Summaries, DCInsight, Case Studies, ICC Policy Statements, DOCDEX and more…

Focus is a one-stop-shop for trade finance practitioners to satisfy their Letter of Credit information requirements - both policy and operations related.

The service is aimed at senior letter of credit professionals. It is ideally suited to decision-makers within LC operations.

DC-PRO Mentor

DC-PRO is the only ICC approved online training on letters of credit and UCP 500.
Top Letter of Credit experts from the ICC developed DC-PRO Mentor to enable users to gain knowledge and skills that in the past have taken years of experience to acquire.

DC-PRO Mentor contains 3 Modules that represent over 12 hours of training in Letters of Credit and UCP 500.The training covers all key aspects of LC work – from basic definitions, to the issuance of an LC, to checking the compliance of documentary presentations under letters of credit.

The service is aimed at beginners to Letter of Credit work but can be of benefit to all levels of LC staff regardless of experience.

Website

For further information on DC-PRO and the online LC services that DC-PRO provide, please see our website at: www.dcprofessional.com