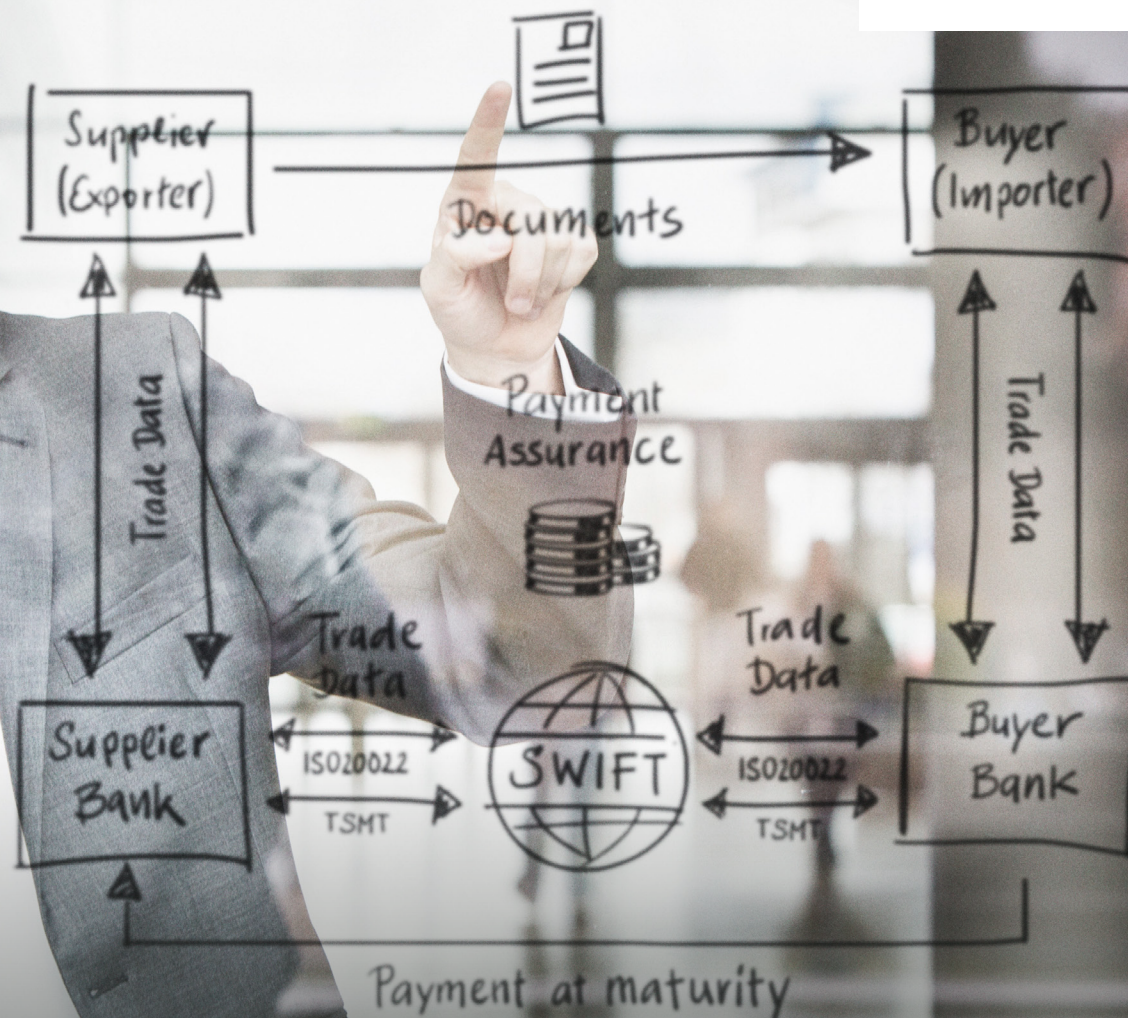


COMMERZBANK

The bank at your side



Trade Finance

The Bank Payment Obligation:

Leading the path of digital evolution

Start ►



Digital evolution of trade finance and the BPO 1/3 ▶

Introduction What is the BPO? Function Framework for SCF Hurdles and targets Benefits Future potential Summary

Trade finance is entering the digital age. The industry is witnessing the emergence of innovative, transformative and disruptive developments such as cryptotechnologies, in the form of distributed ledger technology (DLT) or blockchain. For a successful transition from paper-based to data-based processes, banks need to follow the path of their customers' digital evolution. They need to practically apply proven solutions that can improve the overall conduct of trade, to save time in offering digital solutions and meeting corporates' expectations, and to gain experience with the electronic handling of data in trade finance – a process which has only just begun.

One such solution is the Bank Payment Obligation (BPO) – a standardised irrevocable payment instrument for enhanced trade finance transaction settlement, based on the handling of digitised data of the physical supply chain. Yet the current state of the BPO's implementation in the global market shows that the progress of digitisation remains far from complete. In an industry that is slow to change and heavily reliant on paper-based activities, innovation in trade can be time-intensive and complex, and market adoption can be challenging. This means that the potentially transformative benefits of the BPO's underlying technology are not always easily realised.

Since 2010, when the first BPO transaction took place, bodies such as SWIFT and the International Chamber of Commerce (ICC) have championed the instrument as a means of harnessing the rapid



Digital evolution of trade finance and the BPO ◀ 2/3 ▶

Introduction What is the BPO? Function Framework for SCF Hurdles and targets Benefits Future potential Summary

growth of the “data economy”. In publications such as the 2013 [Uniform Rules for Bank Payment Obligations](#) (URBPO) – which provide the essential regulatory framework for how BPO transactions should be conducted on a global scale – the ICC and SWIFT have shown how the BPO can enable data to be used as an alternative to paper in trade finance transactions.

Together with other initiatives like eDocs and the multibank SWIFT standard MT798, the BPO pushes the evolution of trade towards digital handling. As industry players continue to struggle with illiquidity, security and efficiency, enhanced uptake of the BPO would yield high benefits across the trade finance landscape – improving the mitigation of payment risk, allowing faster and more flexible processing, and increasing capital availability. According to Michael Quinn, Managing Director at J P Morgan, “Many customer supply chains are already digital. But banks have not yet leveraged what our customers use daily into the financial settlement process”.

Crucially, the BPO can also serve to enhance the provision of supply chain finance (SCF) – utilising its four-corner transaction model (i.e. the mutually dependent relationship of two trading counterparties and two banks: buyer, seller, buyer’s bank and seller’s bank). In this respect, it benefits from the cooperative networks between banks, especially for onboarding involved corporates, KYC procedures, compliance checks and financing.

Banks have started to embrace the BPO as part of their own product portfolios and settle BPO transactions with their corporate clients – who, in turn, are keen to adopt innovative measures that can boost the efficiency of their physical supply chains.

Market adoption of the BPO has been lower than expected, however. This is because it depends on acceptance of the instrument by a “critical mass” of banks, which – to date – has not yet been reached. According to Alexander R. Malaket, CITP, CTFP, President OPUS Advisory Services International Inc.: “When it was first launched, the BPO was probably one of the most substantive and promising innovations in the business of financing international trade. Subsequent efforts to commercialise and to motivate adoption, including its market positioning and the limited awareness among corporates provide some important lessons to inform a go-forward strategy. The viability of the BPO requires a reset – both around market awareness and perception, and around the practicalities of value proposition and implementation. At its core, the BPO framework offers clear potential in advancing the financing of global commerce, and can complement broader digitisation initiatives in the industry.”

Digital evolution of trade finance and the BPO ◀ 3/3

Introduction What is the BPO? Function Framework for SCF Hurdles and targets Benefits Future potential Summary

Therefore, this paper will consider the challenges facing market adoption of the BPO today and the steps needed to boost it. It will outline the benefits the BPO can bring to banks and their corporate customers if widely adopted – including the significant opportunities to enable and enhance SCF – as well as the future potential applications of the instrument. It will also stress that, given commercialising new products with DLT will take time, there is a need to invest in the BPO for practical solutions in parallel with continued experimentation in DLT or blockchain.

As Enno-Burghard Weitzel, Head of Product Management Trade Services at Commerzbank, notes: “We see the BPO as a substantial milestone in the evolution of trade finance towards digitisation. The BPO is the first trade finance instrument based on an automatic matching of digital trade data. As an instrument to undertake payments, it also provides a framework for financing along the supply chain of our corporates and thus brings together the business areas of trade finance and supply chain finance. We are already seeing that the concept of the BPO will be used in the DLT solutions that are yet to come. Therefore, we actively support a revision and extension of the URBPO to include DLT technologies – both in order to allow an evolution of the BPO itself, and to make the market increasingly aware that it is profitable to get BPO-ready now.”



What exactly is the BPO?

Introduction **What is the BPO?** Function Framework for SCF Hurdles and targets Benefits Future potential Summary

The BPO serves as a legally binding promise to execute payment for goods or services, based on the successful matching of agreed electronic trade data. According to Article 3 of the URBPO, the instrument is “an irrevocable and independent undertaking of an obligor bank [that is, the buyer’s bank] to pay or incur a deferred payment obligation and pay at maturity a specified amount to a recipient bank [the seller’s bank] following Submission of all Data Sets required by an Established Baseline and resulting in a Data Match or an acceptance of a Data Mismatch”.

The trade data of the purchase order, invoice and the delivery/shipment of goods and services are provided by the buyer and seller, respectively, before being converted into an electronic standard format (ISO 20022TSMT). This format is an XML standard designed exclusively for exchanging and matching data between involved banks and Trade Matching Applications (TMA). SWIFT’s TSU is the primary TMA used for matching data on BPO transactions, but any TMA platform can process the data required. If the matching is successful, the obligor bank undertakes payment to the recipient bank at a given date. Unhindered by discrepancies in jurisdictional regulation or counterparty size, the BPO creates a legally binding and enforceable international payment obligation.

With the successful matching of purchase order, invoice and shipment data, the BPO can also serve as an enabling framework for SCF – optimising liquidity and working capital, and minimising payment risk. As defined in the [Standard Definitions for the Techniques of Supply Chain Finance](#), issued and published by the Global Supply Chain Forum in March 2016: “The BPO[’s].. data-driven enabling framework has significant potential for facilitating SCF solutions based on open account trade flows.. especially those with deferred payment periods”. The BPO’s irrevocability and given maturity date can help to assist the provision of SCF both before and after shipment. The successful match of data within the physical supply chain provides solutions along the financial supply chain and therefore enables a convergence of both supply chains in a digital environment.

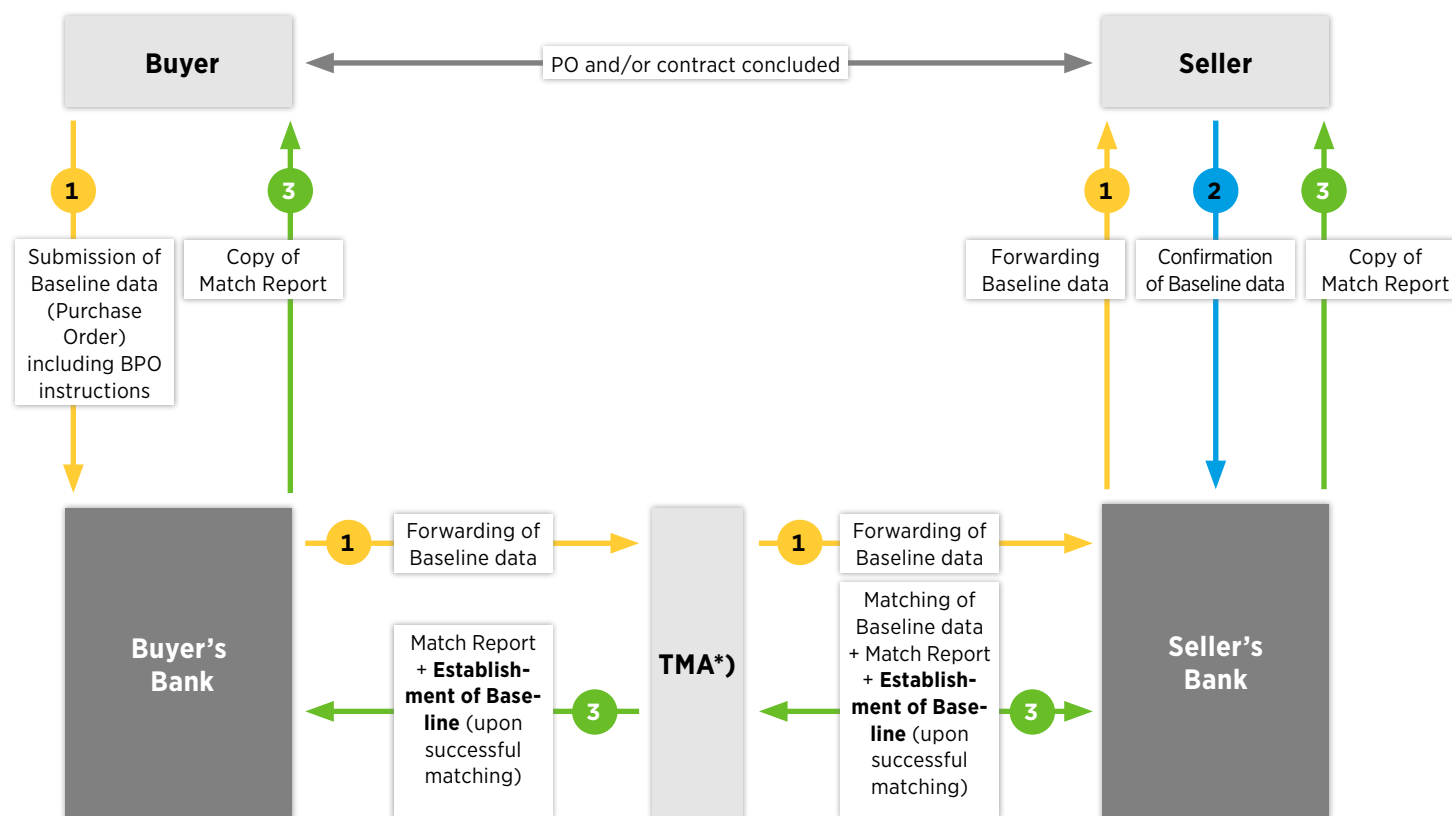


How does the BPO work? 1/2 ▶

Introduction What is the BPO? **Function** Framework for SCF Hurdles and targets Benefits Future potential Summary

A BPO transaction flow consists of 2 data-matching processes:

1. Matching of Baseline Data (Establishment of Baseline)



i

1st Matching:

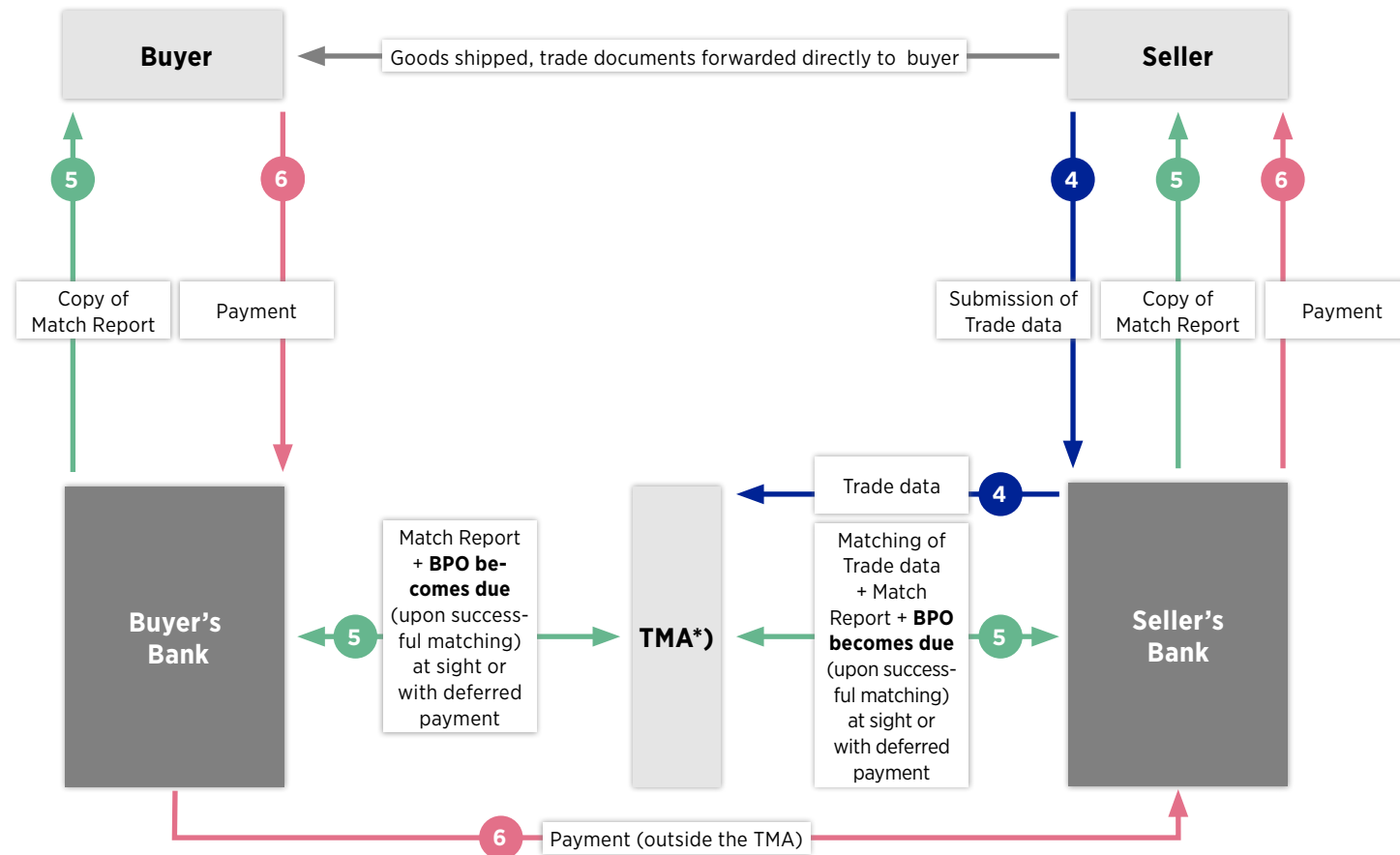
The buyer and seller agree on the purchase order data as the basis for triggering the payment obligation after shipment. This data protocol is called the “established baseline”. Now the seller already has the assurance to receive payment at maturity if shipment is effected according to the agreed terms and the data presented in compliance with the baseline. The data flow is channelled through the involved banks and processed on the SWIFT TSU.

*) Trade Matching Application, e.g. SWIFT TSU

How does the BPO work? ◀ 2/2

Introduction What is the BPO? **Function** Framework for SCF Hurdles and targets Benefits Future potential Summary

2. Matching of Trade Data (BPO becoming due)



*) Trade Matching Application, e.g. SWIFT TSU

2nd Matching:
After shipment, the seller provides the invoice and shipment data for matching against the baseline on the SWIFT TSU and sends the trade documents directly to the buyer. Upon successful matching of the data, the BPO becomes due and the obligor bank is automatically obliged to pay the BPO amount at maturity.



An enabling framework for Supply Chain Finance 1/2 ▶

Introduction What is the BPO? Function **Framework for SCF** Hurdles and targets Benefits Future potential Summary

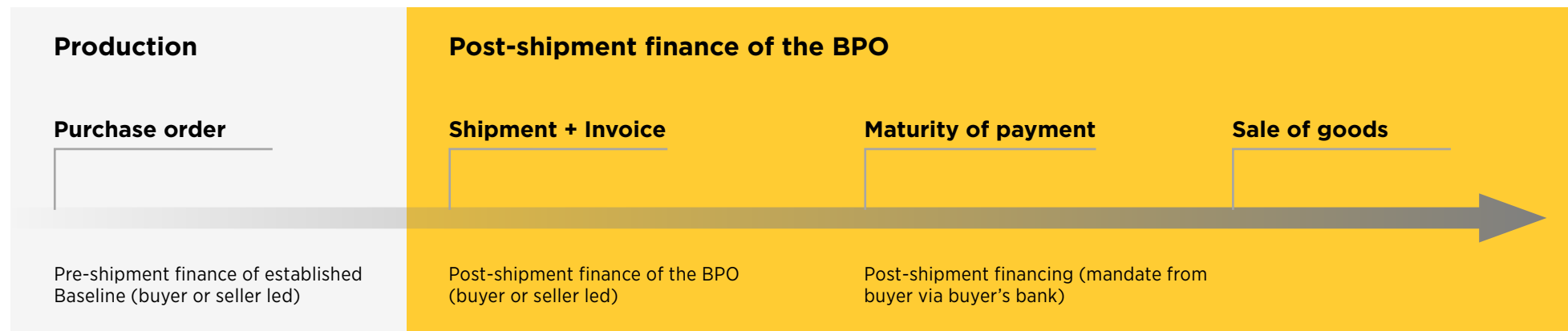
The Standard Definitions for the Techniques of Supply Chain Finance, issued and published by the Global Supply Chain Forum – in turn represented by a number of industry associations with members around the world – identified the BPO as a beneficial instrument for SCF in various countries and markets due to its use of the four-corner model.

The obligor bank relies on the buyer's creditworthiness when entering into the irrevocable payment undertaking of a BPO – which not only secures the payment itself, but also provides security for financing against the payment, offered by the recipient bank, or the obligor bank, allowing a deferment of payment terms and maturity date. The extension of payment terms is key: if the payment is able

to be deferred, the buyer is given more autonomy over their working capital and can optimise their capital cycle and the supply chain network within which they work. At the same time, the supplier does not suffer illiquidity because financing is offered against the BPO-assured payment, without touching their own credit facilities.

The BPO could also be used to augment a buyer-led/payables SCF programme. Financing an import BPO by order of the buyer, processed as an early fulfilment of the payment obligation, follows the construction of buyer-led payables finance; here, the buyer approves payment of the invoice and offers financing of the invoice amount to the supplier.

BPO as an enabling framework for Supply Chain Finance:



An enabling framework for Supply Chain Finance ◀ 2/2

Introduction What is the BPO? Function **Framework for SCF** Hurdles and targets Benefits Future potential Summary

Financing of the BPO is transactional based and refers to larger, rather than smaller, payment amounts. Contrary to payables finance programmes in the three-corner model of buyer-to-bank-to-supplier, the four-corner model of the BPO (i.e. buyer-to-buyer's bank-to supplier's bank-to supplier) enables the issuing obligor bank to take advantage of its network of correspondence banks to provide finance in a jurisdiction where it has no presence or risk appetite and – by involving the supplier's bank – facilitates a smooth supplier onboarding.

To provide solutions in Supply Chain Finance it is important to understand the relationship between the physical supply chain and the financial supply chain and its dependencies. At different points along the physical supply chain (for example, production, shipment and payment), trade partners have a need for mitigating risk and obtaining liquidity. Banks are asked to provide solutions to meet these requirements. The BPO follows this concept and provides a payment undertaking with possible financing (on the financial supply chain) against electronic matching of data of the physical supply chain (PO data, invoice data, shipment data) at different points of the supply chain.



Market adoption: hurdles and targets 1/5 ▶

Introduction What is the BPO? Function Framework for SCF **Hurdles and targets** Benefits Future potential Summary

2010 was a milestone for the BPO: it was then that it moved beyond the “proof of concept” stage and reached its “pilot”, as Standard Chartered Bank’s internal branch network facilitated a transaction between BP and Octal. The first cross-border transaction, between Bank of China and Bank of Montreal, took place the same year.

The BPO has since matured to its “commercialisation” stage. More corporates have used the instrument, and the number of “BPO-active” and “BPO-ready” banks is now about 40, situated primarily in Asia and Europe. Such BPO-active banks are citing growing BPO business and reporting that – slowly, but steadily – more corporates are being onboarded for the purpose of completing new BPO transactions.

Market adoption is crucial to the success of any given product; the BPO itself continues to be adopted because it both fills existing gaps in the market and satisfies the demand for value-added, client-centric digitisation. Yet market adoption of the BPO has been relatively slow.

▶ How to become “BPO-live”

Hurdles

Adoption has been slow because: 1) the trade industry, steeped in tradition, faces a complex ecosystem; 2) there remains a scarcity of banks available to transact with the BPO; 3) corporates and 4) banks still need to be made aware of the instrument’s appeal; 5) intensive sales and marketing activities remain key to increase the BPO business; and 6) the URBPO still largely position the BPO as a tool for banks, rather than for corporates as well.

1) Trade comprises a complex landscape

International trade instruments – like the letter of credit, the guarantee and documentary collection – have been used between trading counterparties for centuries. While the trade ecosystem today continues to use traditional methodologies, it has grown into a billion-dollar global industry with a multiplicity of players and different cross-border regulatory frameworks and requirements. Such complexity means complete digitisation will require taking a long-term approach to adopting new technologies and innovative solutions.

2) A banking bottleneck

While some banks are BPO-ready and BPO-active, market adoption has been held back by those that have not embraced the instrument. Ultimately, further corporate demand for the BPO will not be met until more banking partners are able to transact with it.

Market adoption: hurdles and targets 1/5

Introduction What is the BPO? Function Framework for SCF **Hurdles and targets** Benefits Future potential Summary

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The BPO has since corporates have “active” and “BPO-ready” Asia and Europe business and reports are being onboarded actions.

Market adoption BPO itself continues gaps in the market centric digital relatively slow.

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How to become “BPO-live”

- 1) **Registration** on the SWIFT TSU matching platform and completion of internal training
- 2) **Implementation** of the BPO in internal processes and infrastructure
- 3) **Piloting** with other banks
- 4) **Communication** (internal and external) for sales roll-out
- 5) **Onboarding** of buyers, sellers and identifying BPO partner banks for piloting first BPO transactions
- 6) **Execution** first in a test environment; then, if successful, in a live environment

dit, the guaran- between trad- system today own into a bil- rs and different ts. Such com- g a long-term ve solutions.

market adoption of the instru- PO will not be ransact with it.

► How to become “BPO-live”

Hurdles

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Banks still need to overcome the hurdle of transacting with digital data instead of verified documents. This might lead to the perception of higher fraud risk. Yet following the approach in which the BPO serves as an alternative to open account transactions and re

Market adoption: hurdles and targets ◀ 2/5 ▶

Introduction What is the BPO? Function Framework for SCF **Hurdles and targets** Benefits Future potential Summary

Banks still need to overcome the hurdle of transacting with digital data instead of verified documents. This might lead to the perception of higher fraud risk. Yet following the approach in which the BPO serves as an alternative to open account transactions and recurring simple letters of credit in an established, trusted trade partnership, the risk of fraud is relatively low. Furthermore, strict KYC procedures force banks to maintain relationships with only trusted customers – and they still have the chance to request additional information, should any concerns be raised for the trade transactions concerned.

3) A lack of awareness of the benefits to corporates

If banks are too reticent to talk to their customers of the BPO's benefits, they cannot expect demand for – or indeed knowledge of – the BPO to grow among corporates. Without sufficient demand from corporates, there is a risk that other banks will see little incentive to invest in the BPO – thus exacerbating the issue of the banking bottleneck.

4) A lack of awareness of the benefits to banks

With the BPO, banks can take advantage of offering a digital solution for payment assurance and finance by targeting growing open account business. As corporates demand faster and cost-saving processing of their trade transactions, banks can also use the BPO to recapture LC business which will be lost to open account handling. Business cases to justify the implementation of the BPO as

a new product should therefore not only reflect the potential for new revenues but also the estimated business losses as mentioned above.

5) Intensive and ongoing sales activities is key

Even if banks have managed to become BPO-ready, a new instrument cannot sell itself. It needs marketing and presentation to corporates. The necessary onboarding of involved parties when finding potential BPO transactions takes effort, time and patience. Data mining for business with BPO banks is useful for finding “matching couples” of corporates, but implementing a new trade finance solution within the existing processes on the corporates' side also takes time and effort.

6) The URBPO are in need of an update

Currently, the URBPO only address regulation and protocol for the obligor bank and the recipient bank – not the corporates between which the transaction is taking place. This positions the BPO as an instrument for banks, rather than as a tool for trade transactions more broadly, which – despite the benefits – could diminish its appeal to corporates.

7) Involving and informing local regulators or central banks

For cross-border trade transactions in certain countries, local regulators or central banks require established trade finance instruments, such as the letter of credit, for establishing and settling the trade.

Market adoption: hurdles and targets ◀ 3/5 ▶

Introduction What is the BPO? Function Framework for SCF **Hurdles and targets** Benefits Future potential Summary

These institutions need to be informed of the BPO, so that it can be included as a new trade finance instrument in local regulatory frameworks.

Targets

Digitisation of the trade finance industry depends on banks hitting the following targets: 1) identifying customer challenges and priorities and then applying the right solutions; 2) ensuring that these products reach commercialisation; and 3) developing adequate levels of standardisation and legal frameworks to support them.

1) Raising awareness of challenges and solutions

Making adoption of the BPO more widespread among both banks and corporates and boosting commercialisation first depends on educating the market. As well as investing in their own capability to transact with the BPO, BPO-active banks themselves need to take a strategic approach to promoting the BPO as a product, both to their corporate customers and – critically – to other banks in the trade finance industry, in order to reach an industry-wide tipping point.

This is the goal that the BPO Commercialisation Group is striving to achieve. The Group is composed of representatives of ANZ, Bank of Tokyo Mitsubishi, BNP, Commerzbank, J. P. Morgan, Standard Chartered Bank and UniCredit, and will be part of the ICC Working Groups on Digitization in Trade, which has recently been established. Particularly, the group has proposed an update to the UR-BPO, extending them to better reflect the direct benefit the BPO

offers to corporates and to enable risk mitigation in other emerging technologies. It is hoped that, with this measure, more corporates will seek BPO transactions – in turn placing more pressure on their banks to adopt the instrument.

2) Actual commercialisation

Banks' primary target remains to develop a proof of concept, then commercialise it – and so realise the potential benefits. The shift from proof of concept to commercial implementation is both a crucial and an intricate process. Unlike with blockchain, which – having just passed through the first gates of proof of concept – still has some way to go towards commercialisation, the BPO has already entered the market.

3) Timeframes, standardisation and legalisation

While the trade finance community will pursue DLT advancements in the coming years, the BPO concept is available now – and has also already been demonstrated to be both commercially viable and valuable. What is more, unlike BPO's home within SWIFT, blockchain technology is being developed by a plethora of fintechs and banks in accelerator and incubator programmes across the world. Due to the diversity of blockchain offerings, and the complexity of the ecosystem within which they aim to operate, it will take time to develop substantial standardisation and legalisation to move towards successful piloting and production – something the BPO has already achieved.

Market adoption: hurdles and targets ◀ 4/5 ▶

Introduction What is the BPO? Function Framework for SCF **Hurdles and targets** Benefits Future potential Summary

Applying the McKinsey model

Industry 4.0 – that is, moving beyond simple automation and towards implementing artificial intelligence (AI) and robotics, the Internet of Things (IoT) and cloud-computing across corporate supply chains – has increased demand within the trade industry for similarly innovative offerings. Banks are thus under growing pressure from their corporate customers to embrace value-added, data-driven offerings. But widespread discussion of DLT, in particular, has prompted a misconception that the BPO is somehow a lesser rival to blockchain. Instead, the BPO represents a vital stage of trade finance’s digital evolution, because becoming familiar with the BPO’s data-handling and matching is important to understanding the data-heavy processes of blockchain.

Of course, the trade finance industry needs to pursue a seamless, efficient digital transition. So while banks must doubtless continue to pursue commercialisation of blockchain, they must also utilise – and raise awareness – of the tools already currently available to them. This means investing in their BPO capabilities in parallel to their work on DLT. In fact, efforts are being undertaken to leverage the framework of the BPO for DLT applications. This will support the transition to emerging technologies that are not dependent on the SWIFT TSU but rather rely on smart contracts and the definition of conditions which constitute a commitment to pay.

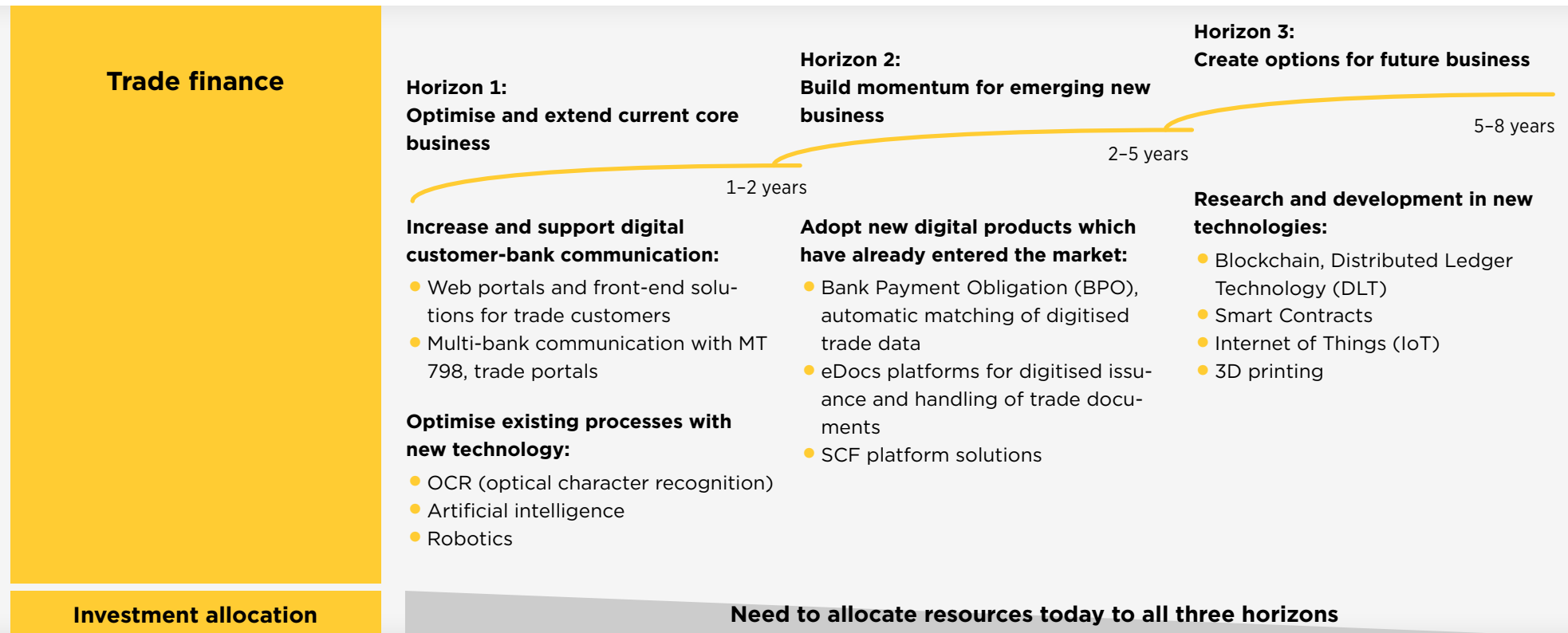
McKinsey’s “Three Horizons of Growth” model suitably illustrates the steps needed to be taken in the digitisation of the trade finance industry:

- **Horizon 1:** the improvement of core traditional trade finance by digital communication channels and the use of optical character recognition (OCR) software and AI to optimise existing manual processes.
- **Horizon 2:** the adoption of readily available, innovative solutions such as the BPO and eDocs.
- **Horizon 3:** pursuing a new technological mindset across the trade finance landscape by investing in disruptive technology (such as blockchain or DLT).

Market adoption: hurdles and targets ◀ 5/5

Introduction What is the BPO? Function Framework for SCF **Hurdles and targets** Benefits Future potential Summary

Digitisation in trade finance happens in different horizons based on “The Three Horizons of Growth” from McKinsey&Company



Horizon 1, naturally, deals with the most pressing, short-term issues; Horizon 3 looks to the longer term. The allocation of a bank's resources to all three horizons is vital to the digital evolution of the trade finance landscape.

▶ [Case Study: Commerzbank and the BPO](#)

Market adoption: hurdles and targets ◀ 5/5

Introduction What is the BPO? Function Framework for SCF **Hurdles and targets** Benefits Future potential Summary

Digitisation in Trade Finance happens in different Horizons

based on “The Three Horizons of Growth” from Mc Kinsey&Co

Case Study: Commerzbank and the BPO

Commerzbank first started to implement the BPO in 2013, and went live in October 2014 – with one transaction for a German SME for its trade business with Thailand, and another for a Belgian-based corporate trading with Turkey. The Bank has since increased its BPO business, settling transactions with partner banks for multinational companies, large corporates and SMEs, both within Europe and overseas. Notable recent transactions include the first BPO in London in August 2016, processed together with UniCredit and covering the export of chemicals from Ireland to Italy; the first BPO between Germany and China in September 2016; and the first in Austria in August 2017 (for details of the case studies see the “Benefits” section).

Commerzbank has sought to raise awareness and boost commercialisation of the instrument, and in recent months has seen an increase in BPO business as knowledge, interest and readiness grows amongst customers.

✕ close

Future business

5–8 years

Development in new

Digitized Ledger

(IoT)

Investment allocation

Need to allocate resources today all three horizons

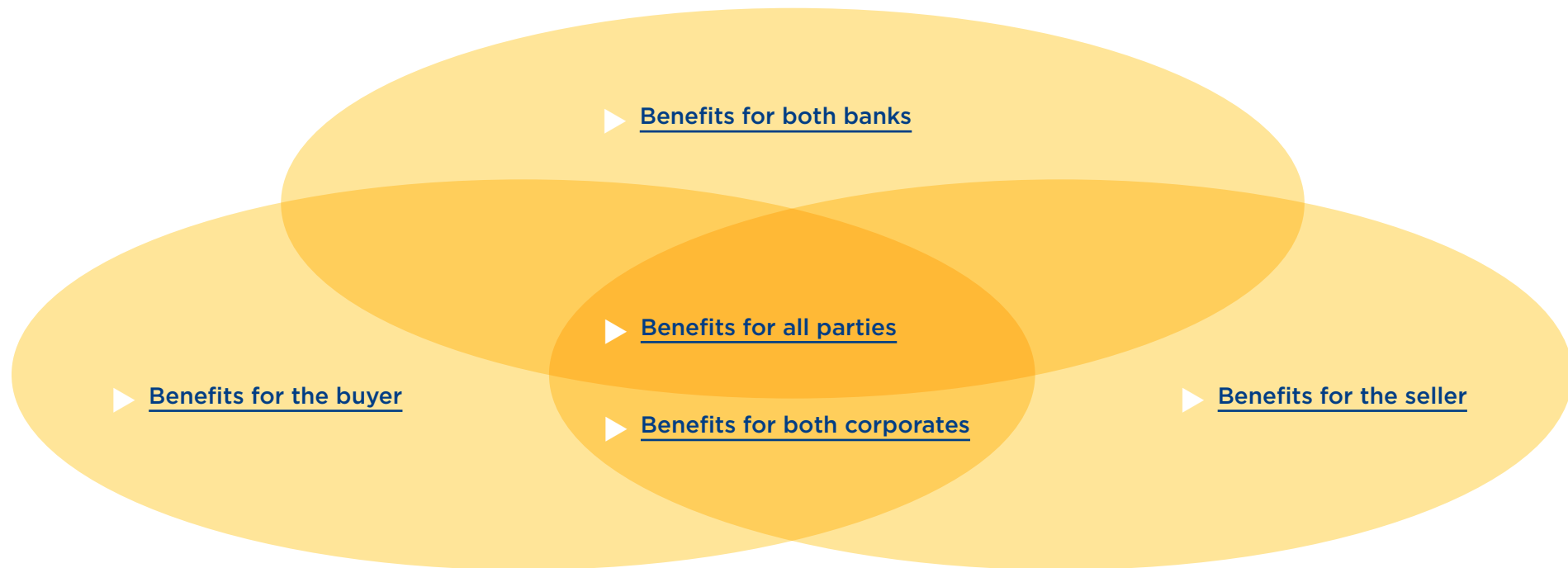
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► [Case Study: Commerzbank and the BPO](#)

The benefits of processing a BPO transaction are numerous, with those banks and corporates that have completed BPO transactions having lauded its simplicity, time-efficiency, and potential to enhance long-term relationships between trading counterparties.

1) **Payment assurance and increased flexibility**

By definition, the BPO is an irrevocable payment undertaking by a bank. This means it provides payment security at the outset – when purchase order data is agreed and the established baseline is set. BPO provides risk mitigation not only through guaranteeing payment, but also through the specification of an irrevocable payment date.





The benefits of processing a BPO transaction are numerous, with those banks and corporates that have completed BPO transactions having lauded its benefits. It enhances long-term

1) Payment assurance and increased flexibility

By definition, the BPO is an irrevocable payment undertaking by a bank on behalf of its client. The bank's obligation is set against the client's obligation to the counterparty when the payment baseline is set. The bank is then guaranteeing payment to the counterparty, ensuring a reliable payment.

Benefits for both banks

- Less effort and lower cost of onboarding clients (thanks to there being no additional KYC demands)
- Enhanced bank-to-bank international relations
- Fast, automated and seamless transaction processing
- Risk mitigation – and therefore lower costs – involved with trade finance
- Standardisation with other banks through the URBPO and ISO 20022TSMT
- Improved speed of handling mismatches on behalf of the client
- The ability to “mine” the data that support transactions for future business development

✕ close

Benefits of the BPO 1/3 ▶

Introduction What is the BPO? Function Framework for SCF Hurdles and targets **Benefits** Future potential Summary

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By definition, the BPO is an irrevocable payment undertaking by a bank on behalf of the buyer. The bank undertakes to pay the seller on the due date of the payment, even if the buyer has not yet paid the bank. The bank undertakes to pay the seller on the due date of the payment, even if the buyer has not yet paid the bank. The bank undertakes to pay the seller on the due date of the payment, even if the buyer has not yet paid the bank.

Benefits for all parties

- Improved visibility and transparency on the trade transaction
- Enhanced trading relationship
- Enhanced trade opportunities and processing and use of the four-corner model

▶ Benefits for the buyer

▶ Benefits for all parties

▶ Benefits for both corporates

▶ Benefits for the seller

Benefits of the BPO 1/3 ▶

Introduction What is the BPO? Function Framework for SCF Hurdles and targets **Benefits** Future potential Summary

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1) Payment assurance and increased flexibility

By definition, the BPO is an irrevocable payment undertaking by a bank on behalf of the buyer. The bank's obligation is set when the payment baseline is set. The bank is then guaranteeing payable payment.

Benefits for both corporates

- Fast, automated and seamless transaction settlement processing
- Improvement to the efficiency of the working capital cycle
- Risk mitigation and financing for open account transactions
- Reduction of complexity involved with paper-based processes

▶ Benefits for the buyer

▶ Benefits for all parties

▶ Benefits for both corporates

▶ Benefits for the seller

Benefits of the BPO 1/3 ▶

Introduction What is the BPO? Function Framework for SCF Hurdles and targets **Benefits** Future potential Summary

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Benefits for the buyer

- Guarantee of goods received as expected
- Flexible financing options at several stages of the supply chain
- Controlled input into the specifics of the payment conditions, as facilitated by data-matching on TMA/SWIFT TSU
- Early receipt of documents to avoid storage charges at the port of discharge

▶ Benefits for the buyer

▶ Benefits for all parties

▶ Benefits for both corporates

▶ Benefits for the seller

Benefits of the BPO 1/3 ▶

Introduction What is the BPO? Function Framework for SCF Hurdles and targets **Benefits** Future potential Summary

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Benefits for the seller

- Guarantee of payment in full on a specific due date
- Ability to raise finance on a BPO with deferred payment terms
- Lower implied cost of funding than would have been incurred under other financing structures

▶ Benefits for the buyer

▶ Benefits for all parties

▶ Benefits for both corporates

▶ Benefits for the seller

Benefits of the BPO ◀ 2/3 ▶

Introduction What is the BPO? Function Framework for SCF Hurdles and targets **Benefits** Future potential Summary

A BPO also provides a degree of flexibility to the counterparties, as the established baseline of data allows the conditions – including the shipment and payment date – of the payment to be specified by both the seller and the buyer. Amendments can be agreed within a short period of time. In this way, both parties are afforded more transparency over the trade and their cash management, and the capital cycle can therefore be improved upon.

Moreover, when using and matching data on the SWIFT TSU platform, trade documents are sent directly by the supplier to the buyer. This means the buyer can receive the documents prior to arrival of goods and thus avoid storage charges at the port of destination.

▶ From open account to the BPO: first transactions in Austria

2) Enhanced handling and cooperation with partner banks due to the four-corner model

The BPO uses a “four-corner” model for completing a trade transaction. The four corners are: the buyer, the obligor bank (buyer’s bank), the seller, and the recipient bank (seller’s bank). This brings a number of benefits – especially for onboarding involved corporates, KYC procedures, compliance checks and financing.

The four-corner model allows the trade counterparties’ respective banks to orchestrate the transaction together. This requires no extra

onboarding of clients, improves understanding of the clients’ needs, and entails no extra KYC effort and costs. Moreover, the buyer’s and seller’s own banks each have the motivation to apply the necessary credit facilities in order to fulfil the BPO’s specific obligations and can take advantage of networks of partner banks to provide global reach.

▶ The four-corner model in action: from Brussels to Istanbul

3) Working capital optimisation

The BPO’s combination of assured payment, a fixed maturity and possibilities to extend payment terms with provision of finance has the potential to transform the working capital cycle, both in terms of efficiency and liquidity.

A more-efficient working capital system can also help to offset some of the demands laid out by heightened regulatory measures since the financial crash of 2008. Conditions such as minimum capital allowance, for example, put a strain on liquidity and hinder the availability of capital to be offered as trade finance. By having a fixed and reliable payment assurance mechanism in place, both corporates and banks are able to adjust other payments accordingly and ensure that capital flow remains at the optimum level.

Benefits of the BPO ◀ 2/3 ▶

Introduction What is the BPO? Function Framework for SCF Hurdles and targets **Benefits** Future potential Summary

A BPO also provides a degree of flexibility to the counterparties, as the established baseline of data allows the conditions – including the shipment and both the seller and a short period of transparency over capital cycle can

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2) Enhanced handling of the four-corner

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From open account to the BPO: first transactions in Austria

In August 2017, Commerzbank processed the first BPO transactions in Austria, covering the import of bus components from Germany and Italy. The buyer, a customer of Commerzbank AG Austria, was TAM-Europe d.o.o., located in Maribor, Slovenia, one of Europe's largest bus and commercial vehicle manufacturers. The suppliers were MAN Truck & Bus AG, a commercial vehicle manufacturer headquartered in Munich (another customer of Commerzbank), and ISAF Bus Components srl, an Italy-based supplier and customer of UniCredit.

The counterparties were impressed with the BPO. MAN cited the ability of the BPO to simplify trade transactions as well as to save processing costs and times. TAM-Europe, meanwhile, saw the instrument as a successful supplement to open account and letters of credit. The transactions were particularly notable in that they marked the importer's first steps toward using the BPO for all its trade business.

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The four-corner model in action: from Brussels to Istanbul

In October 2014, BP Aromatics Ltd NV, a manufacturer and wholesaler of chemicals in Geel, Belgium, agreed to use the BPO for their trade with Köksan Pet Ve Plastik Ambalaj San. Tic.A.S. in Gaziantep, Turkey. The buyer’s bank – Commerzbank’s Brussels branch – and the supplier’s bank – İşbank in Istanbul – together processed and cleared the transaction.

Thanks to the four-corner model, the BPO enabled compliance requirements for each customer to be dealt with separately; in effect, this allowed the importer to convert bank debt to trade debt, which may be regarded as a positive from a credit ratings perspective.

[to Istanbul](#)

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Benefits of the BPO ◀ 3/3

Introduction What is the BPO? Function Framework for SCF Hurdles and targets **Benefits** Future potential Summary

4) Pricing

Because of its fast and efficient automated services, the handling fee for BPO transaction remains relatively low. Charges for mitigating the payment or financing a deferred payment period for a supplier are the same as they would be under a letter of credit. What is more, the supplier can benefit from the recipient bank taking the obligor bank's risk at a typically lower cost than corporate risk. For a more detailed account of the charges for BPO handling, see the ICC's publication,

[Bank Payment Obligation: Capital and Accounting Treatment.](#)

5) Security

The trade industry has always had to mitigate the threat of fraud, but the BPO could boost security. Given that over 80% of global trade is transacted with open account business, the risk of fraud could be considerably reduced if some of this share could be shifted to the BPO. More trade data can be submitted to automated matching and banks use contract agreements for BPO handling to oblige their corporates to provide the correct data - thus securing stable relationships among trading partners.

▶ [Going global: from Germany to China](#)

For further details on the benefits and potential of the Bank Payment Obligation and how it works, please watch this explanatory film.



5) Security

Going global: from Germany to China

In September 2016, Commerzbank and Industrial and Commercial Bank of China (ICBC) successfully processed the first cross-border BPO between Germany and China. The transaction covered the export of chemicals from ICBC's customer in Beijing to TRIGON Chemie GmbH, based in Schlüchtern, Germany.

Aside from crossing continents, the BPO was notable in that trade business between the two companies had previously been handled by documentary collection. TRIGON had shown an early interest in using BPO settlement – noting its ability to provide assurance of payment at the due date, faster handling of goods, earlier receipt of trade documents, and optimised processes. The challenge for Commerzbank was to find a bank on the seller's side able to handle a BPO transaction, and saw it as marking a significant step forward for BPO settlement between the two countries.

Future potential of the BPO

Introduction What is the BPO? Function Framework for SCF Hurdles and targets Benefits **Future potential** Summary

The BPO offers considerable future potential, both as a transformative innovation itself, and as a gateway to further trade finance technologies. Three particular developments appear forthcoming. First is the enhancement of the digital communication between corporates and the SWIFT TSU/banks by implementing a BPO frontend. Second is the merging of the data-matching of the BPO with the provisions of an electronic Bill of Lading (eB/L) and other electronic documents. Third is updating the URBPO to include rules and recommendations for corporates and to incorporate emerging technologies.

1) A corporate BPO frontend

A pillar of the digital age is the automation of data-entry processes. Just as the BPO enables banks to transfer trade data rather than documents, it could, arguably, also allow corporates to benefit from an automated system. In this respect, various banks are working on developing front-end software through which corporates can upload their trade data to the TSU via their banks – thereby saving time and resources by removing the need for manual entry.

2) BPO and an electronic Bill of Lading (eB/L)

Combining the electronic data matching of the BPO with the issuance and provision of an eB/L would improve the authentication and digital handling of data. The same data for the eB/L would be provided for the BPO, and by the time of successful data matching, the eB/L would become available for the buyer immediately.

This innovative model was piloted by essDocs in April 2015 through a CargoDocs Bank Payment Obligation Plus (BPO+) transaction.

The trade was an iron ore shipment from Australia to China, and the transacting parties comprised ANZ (the obligor bank), Westpac (the recipient bank), BHP Billiton (the seller), and Cargill (the buyer). As a result, there was zero data re-entry required.

3) Update of the URBPO

At present the ICC's 2013 URBPO only detail rules applicable to the banks carrying out the trade finance transaction. The ICC's 2015 [Guidelines for the Creation of BPO Customer Agreements](#) recommend bank-corporate clause contracts.

However, the ICC is being called upon to address recommendations in the corporate-corporate space. Trade relations between the two corporate trading parties are crucial to the success of any trade transaction; a BPO transaction is no different. By addressing this and standardising rules and recommendations governing the trading companies' interactions, the BPO will appeal more to banks' corporate customers and thereby stimulate demand, which will have a positive effect on market adoption.

As the evolution of digitisation progresses and continues to incorporate emerging technologies, the URBPO might also be extended to include these technologies for the matching of trade data. This would allow the BPO to provide risk mitigation and enable financing not only on Horizon 2, but also in new trade and supply chain finance models to come on Horizon 3 (see the "Hurdles and targets" section for the McKinsey model).

Summary and outlook

Introduction What is the BPO? Function Framework for SCF Hurdles and targets Benefits Future potential **Summary**

The BPO is a milestone in the digitisation of trade finance. It provides irrevocable payment assurance, meets the needs of open account trade financing, mitigates risk, optimises the working capital cycle, and ensures a fast, transparent, successful transaction settlement. It offers yet greater potential in the Supply Chain Finance space.

Despite its clear benefits and many applications, the BPO has experienced slow market adoption. “BPO-live” banks must make the case for the instrument – conveying the benefits to their corporates in order to stimulate demand, as well as to other banks in order to reach the “critical mass” of financial institutions that will drive industry-wide uptake. And while blockchain may well be heralded as the new wave of digitisation in trade finance, banks must take the time to consider all their investment horizons, embracing DLT in parallel with adoption of the BPO.

Success with the BPO would be a marked achievement for an industry traditionally resistant to change. It would set the trade finance landscape on course for further transactional optimisation and increasingly efficient processes, and, ultimately, would offer banks the chance to better meet the growing demands of trading corporates.



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