The Changing Business of Trust: *Revisiting Letters of Credit's Role in Global Trade*

The Underlying Forces Shaping Global Trade

The Covid-19 pandemic was cause for companies to become reacquainted with the global reach of their supply chains. Since then, the evolving landscape of global trade is being continually reshaped by a complex interplay of drivers, such as supply chain disruptions, inflation, the commercialization of new technologies, and latest developments in trade policies. As global trade continues to take on new catalysts, treasurers and procurement leaders face an increasing need for financial security and flexibility.

In Citi's annual GPS Supply Chain Financing report, the Large Corporate Survey found that, on average, respondents reported maintaining 395 buyer relationships and 346 seller (supplier) relationships. Many established businesses are able to depend on relatively consistent working capital cycles and are closely aligned with the unique characteristics of their working capital cycles. While common factors like seasonality and customer demand are often predictable, unforeseen risks still remain as buyers weigh the reliability of existing suppliers against activating potential new suppliers.

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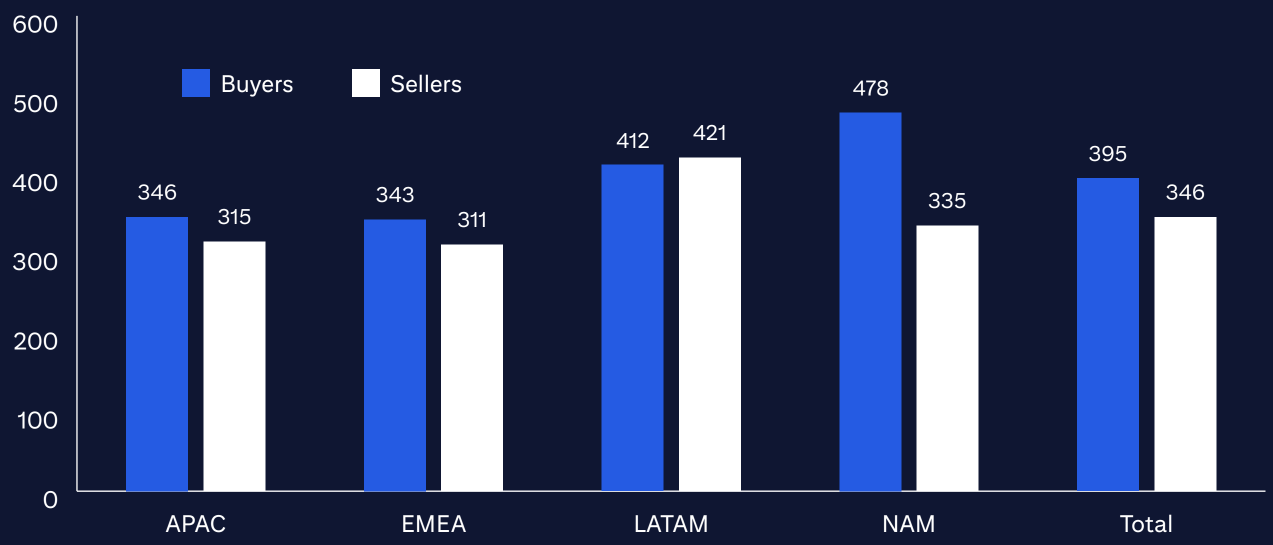
Figure 1. How many supply chain partners do you currently manage in your network? – Averages Per Region



Source: East & Partners Large Corporate Survey 2024, Citi Treasury and Trade Solutions

Despite the challenges of maintaining global trade operations, companies remain focused on strengthening future growth to drive shareholder value, especially for companies with high valuation multiples.[1] Companies that are able to demonstrate a clear strategic path to both short-term and long-term growth, are more often rewarded by investors accordingly.[2] Corporates are directing investments toward high-potential areas, with five defining themes driving significant capital expenditures across diverse industries and regions.

The Five Capex Super Cycles Driving Global Trade

Throughout history, corporates have deployed capital to fund the expenditures that in turn would secure their next generation of growth. In 2025, there are five major capital expenditure trends ("capex super cycles") that are driving global investment.

Race for Superior Technology

Just as cloud computing became an integral part of business operations in the mid-2000s, driven by increasing corporate adoption and interconnectedness, 2023 marked a similar turning point for artificial intelligence (AI). As corporates rapidly embed AI into everyday workflows, AI technologies are now forecasted to reach and annual spend of USD 650 billion in 2028.[3]

The technology underpinning businesses' daily activities relies on vast networks of data centers, powered by servers and semiconductors. These components have a finite operational lifespan, driving continuous corporate investment to meet growing demand.

[1] Citi GPS, Supply Chain Financing: Resilience, Opportunity and the Shifting Winds of Trade, 2025
[2] Citi GPS, Supply Chain Financing: Resilience, Opportunity and the Shifting Winds of Trade, 2025
[3] S&P, Great Cap Expectations: Tech, Utility Spending Power Capital Goods Revenue Growth In 2025, 2025

Energy Transition and Alternative Energy

While "energy transition" have occurred for more than 200 years[4] with emerging new sources, the current period is distinctly marked by shift towards seeking alternatives to fossil fuels. Climate change concerns are a primary driver of this shift, but the sheer unrenewable nature of fossils fuels also represents a significant vulnerability to global energy security.

Increased Power Needs

The converging trends of technological advancements and energy transition are driving a surge in global power demands. Things that once relied on fossil fuels, such as automobiles, garden tools, and stoves, increasingly now have electricity powered alternatives. Separately, technology continues to evolve at an ever-increasing pace, however with that comes greater power needs. Data centers consume massive amounts of electricity and likely figure to do so for the foreseeable future.

This increased demand is straining existing power grids, many of which were already fragile. Natural disasters such as Hurricane Maria, which left some without power for 11 months, underscore the pressing need for investments in grid infrastructure.[5]

Public Spending

Public spending – simply spending at all levels of government to provide goods and services to the public – often operate at a scale only sovereign governments are capable of funding. In the U.S. for example, many likely don't remember a time before highways existed. It was President Eisenhower's Interstate Highway System initiative that brought the U. S.'s highway system to fruition, marking the transformative potential of public investment. Public spending is not just limited to infrastructure; the European Chips Act legislated EUR 43 billion to strengthen Europe's chips industry, while its global military expenditure reached USD 2.4 trillion in 2023.[6]

Reshoring Capex

"Reshoring" of supply chains and manufacturing first started gaining traction during the first Trump Administration and strengthened during the Covid-19 pandemic as corporates became increasingly aware of global supply chain vulnerabilities and the risks posed by over-reliance on specific countries. Today, reshoring is primarily the result of two factors: increased manufacturing efficiency and a rise in protectionism.

Previously, much of foreign direct investment was in pursuit of lower manufacturing costs. Advancements in technology, collectively known as Industry 4.0, haven't completely eliminated the relative cost benefit of overseas production but is cause for some to consider whether it make sense to produce closer to the end users. In an analysis of Bloomberg supply chain data, Citi's data scientists have found strong evidence suggesting onshoring may be occurring in critical industries like computer and semiconductor manufacturing, as supply chains show signs of becoming increasingly domestic.[7]

Plotting a Way Forward

Corporate investment decisions, whether driven by shifting trade policies or pursing new technologies, carry significant risk and reward for the company. In today's constantly evolving global trade landscape, business face the challenge of balancing these two competing forces. Pragmatic applications of legacy trade finance solutions, namely letters of credit, can be a powerful enabler for business' future aspirations and ambitions.

[4] World Economic Forum, The 200-year history of mankind's energy transitions, 2022

[5] ABC News, Puerto Rico's power grid is struggling 5 years after Hurricane Maria. Here's why., 2022

[6] Stockholm International Peace Research Institute, Trends in World Military Expenditure, 2023, 2024

[7] Citi GPS, Supply Chain Financing: Resilience, Opportunity and the Shifting Winds of Trade, 2025

Using Letters of Credit to Solve for Current Challenges

Trade finance exists to facilitate global trade. Letters of credit are some of the oldest trade finance tools in existence however, they remain relevant as ever in today's global trade landscape. Letters of credit can be broadly categorized into two types:

Figure 2. Summary of Letters of Credit

	Standby Letter of Credit	Documentary Letter of Credit
Overview	A legal instrument issued by Citi providing a guarantee of a commitment to pay the beneficiary if the applicant defaults on their agreement.	A contractual commitment by a buyer's bank to pay once a seller (or exporter) ships goods and presents the required documentation to the exporter's bank as proof.
Recommended Purpose	Provides assurance payment will be made for goods/services if the applicant fails to adhere to the stipulations defined in the contract.	To protect both sellers (exporters) and buyers (importers).
Variations of Instrument	Bid, Performance, Advance Payment Guarantee, Protective, Retention, Warranty, Procurement	Import and Export Letters of Credit, Usance Payable at Sight, Red Clause
Benefits	• Strengthens buyer/supplier relationship as obligations are guaranteed by Citi • Utilize Citi's footprint to grow/establish a global network of customers • Enhanced convenience for buyers as the guarantee issued by Citi can be issued in the beneficiary's country • Guarantees can be monitored using Citi's trade finance platform	• The seller (exporter) gets a guarantee of payment while offering the buyer (importer) reasonable payment terms • Optionality to enhance Cash Conversion Cycle by financing the letter of credit • Can finance a deferred payment Letter of Credit with Citi decreasing DSO or can provide the option to customers to finance deferred payment option and they can finance with Citi thus increasing your DPO

Applying Letters of Credit to Solve for Today's Challenges

While some suppliers or goods are easily substituted with one another, others may be more specialized and thus may require a more nuanced approach when incorporating them into supply chains and corresponding supply chain financing strategies. Letters of credit are highly structured, negotiated instruments. The optionality of letters of credit enables their users to create unique solutions that allows for them to curate the way buyers and sellers transact with one another.

Enhanced Surety

The need for enhanced surety for participants active in global trade is two-fold. First, while inflationary pressures have eased in many parts of the world, prices remain elevated comparatively and a result, the underlying notional values of global trade are higher than they were years ago. Second, broadly speaking, geopolitical tensions throughout the world remain present. Geneva Academy currently tracks 110 different armed conflicts through its Rule of Law in Armed Conflict Online Portal[8] while import restrictions in force as of October 2024 affected an estimated USD 2,942 billion or 11.8% of world imports, a 1.9% increase from the year prior.[9]

Historically, trade finance has served as a risk mitigant in global trade as parties have used letters of credit to limit the potential risks inherent when transacting on a global scale. For added assurance, sellers may choose to use silent confirmations, in which the advising bank provides a confidential commitment to pay the seller that is independent of the buyer's and issuing bank's performance. Negotiating commercial terms often creates a conflict of interest as suppliers want to be paid as soon as possible while buyers prefer longer terms. This challenge is magnified when transacting with new or unfamiliar counterparties. Buyers may wish to employ a red clause letter of credit, which enables them to extend partial payment to suppler in advance of the seller presenting any shipping documentation to the advising bank.

Managing Cash Deployment

Red clause letters of credit are an important tool for buyers as not only do they limit buyers' risk, but they also help buyers be more strategic about the cash they deploy. They provide buyers the ability to advance only a portion of the total payment, rather than the full amount. Maximizing cash and working capital is an essential component of a resilient treasury management strategy at any period during the economic cycle.

Many corporates utilize supply chain finance structures to help maximize working capital, which have the dual benefit of helping a buyer harmonize payment terms while providing suppliers access to efficiently provided liquidity.

Supply chain finance is not the only tool buyers have at their disposal to manage payment terms with; buyers may elect to issue Usance Payable at Sight (UPAS) letters of credit as a way to help secure extended payment terms without disrupting supplier's cash flow. Under a UPAS LC, the issuing bank pays suppliers on an "at sight" basis, while buyers have a "usance" period before having to repay the issuing bank at the agreed upon maturity date.

Modern Advancements

Much of the capital being deployed as part of the capex super cycles in play today is across investments with longer time horizons, well in excess of the 180-day tenor common in many traditional letters of credit. Applicants today increasingly require longer tenors, with some banks now issuing letters of credit with tenors of up to three years. Despite this, there still exists a need for even longer tenors and additional parties may step in to help meet this need.

Like other financial products, a secondary market for letters of credit exists, enabling banks to issue letters of credit with longer tenors by then being able to syndicate the risk to interested investors. The prevalence of private capital enables non-bank lenders to step in to help facilitate more exotic letter of credit structures when the risk is greater than a bank's appetite. Development finance institutions (DFIs) and export credit agencies (ECAs) with their unique risk appetite can also step in to help enable letter of credit structures when risk extends beyond a bank's appetite.

[8] Geneva Academy, Today's Armed Conflicts, 2025

[9] WTO, WTO report shows increase in trade restrictions against backdrop of unilateral policies, 2024

Conclusion

Many global corporates may likely find themselves trying to navigate a rapidly evolving global trade landscape while also still trying capitalizing on opportunities to cement future growth. Letters of credit remain an indispensable tool for facilitating both trade and capital expenditures; corporates should consider a few key points when it comes to how letters of credit can support their needs:

- **Tailoring letters of credit to meet specific needs:** No two commercial agreements are the same and letters of credit may be structured accordingly, in order to meet the needs of both buyers and sellers.
- **Limit risk while maximizing working capital:** In addition to being an important risk mitigant, letters of credit can also help corporates preserve cash and manage advance payments required by suppliers for future production.

Citi's trade finance experts and Working Capital Advisory team can help interested firms assess how letters of credit can help facilitate both trade and capital expenditures in a manner that is supportive of a holistic working capital management framework.

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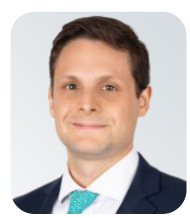

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