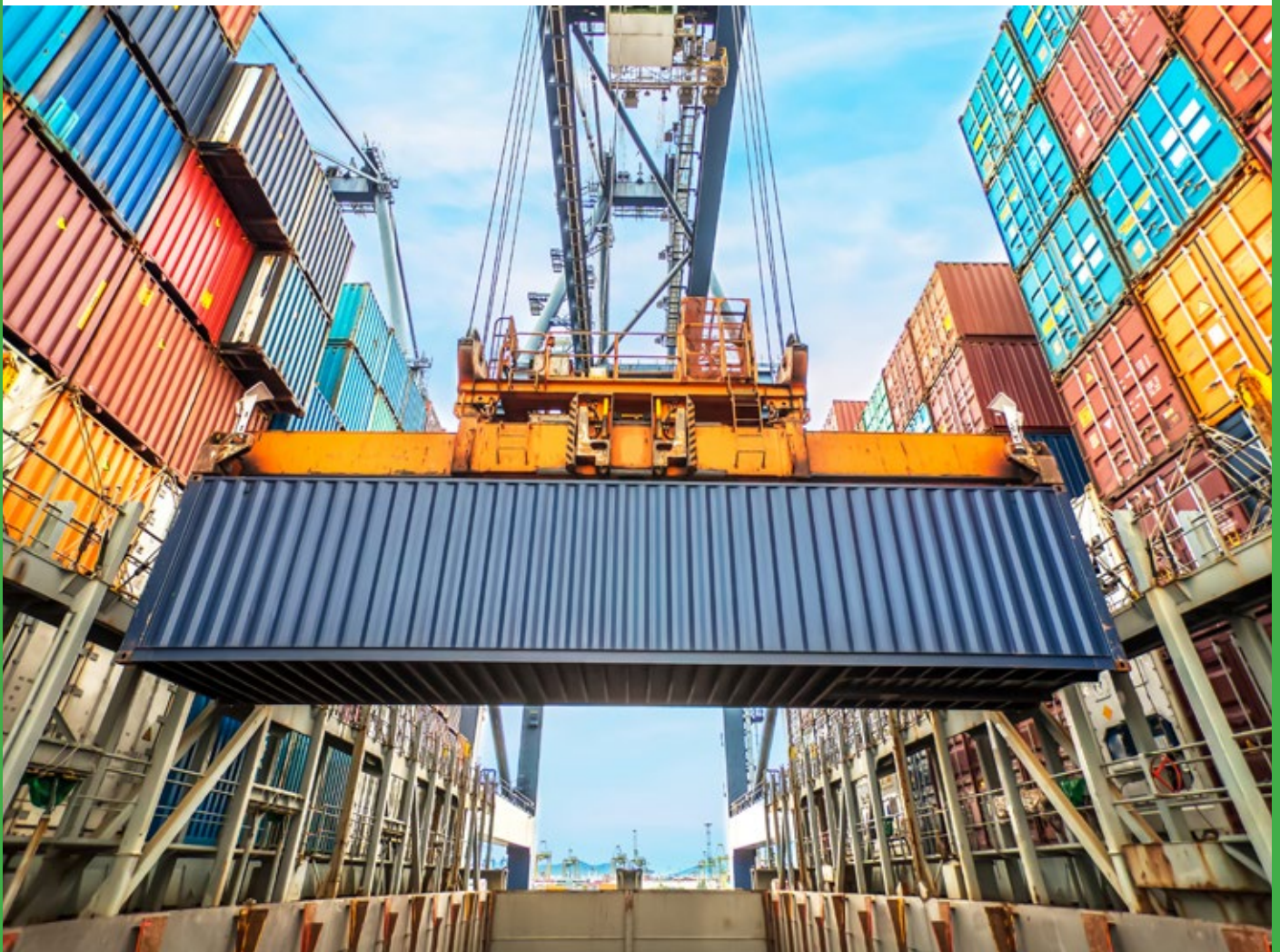


# FOSTERING DEVELOPMENT THROUGH TRADE FINANCE



AFRICAN DEVELOPMENT BANK GROUP



# TRADE FINANCE

In Support of Africa's Development

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*"Trade finance is an important instrument for influencing Africa's long-term economic development and structural transformation. It can play a cross sectoral role to facilitate delivery of the Bank's "High 5" strategic priorities to "power and light up Africa", "feed Africa", "industrialize Africa", "integrate Africa" and "improve the quality of life of the people of Africa."*

**AKINWUMI A. ADESINA,**  
**PRESIDENT OF THE AFRICAN DEVELOPMENT BANK**

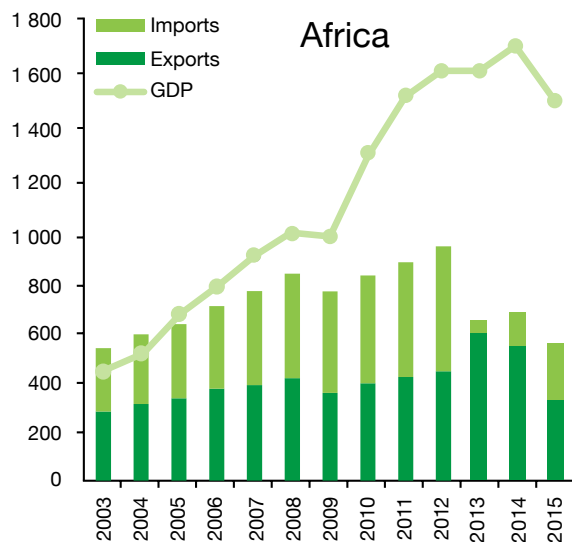


## African Development Bank INTRODUCTION

# AFRICA IN GLOBAL TRADE

Trade is the cornerstone of economic development by African countries. Botswana, Mauritius and Namibia have all transformed themselves from low income into middle income countries by improving their ability to trade in regional and global markets. Yet the continent as a whole can greatly strengthen its trading position in order to improve living standards and economic growth. Africa accounts for just 3 per cent of global trade and has a lower proportion of intra-regional trade than any other part of the world. The continent remains overly dependent on the export of raw materials, so that growth levels fluctuate in line with international commodity prices.

To demonstrate the power of trade to the economic transformation of the African continent, if Africa were to increase its share of world trade from 2 to 3 per cent, that 1 percentage point increase would in nominal terms generate about US\$70 billion of additional income, which is about three times the total amount of development assistance the continent receives from the rest of the world each year. Progress is being made on a piecemeal basis, with regional trade agreements and new transport infrastructure helping to promote trade between neighbouring states, but the continent is yet to experience the same kind of sustained growth levels as East Asia over the past 30 years.



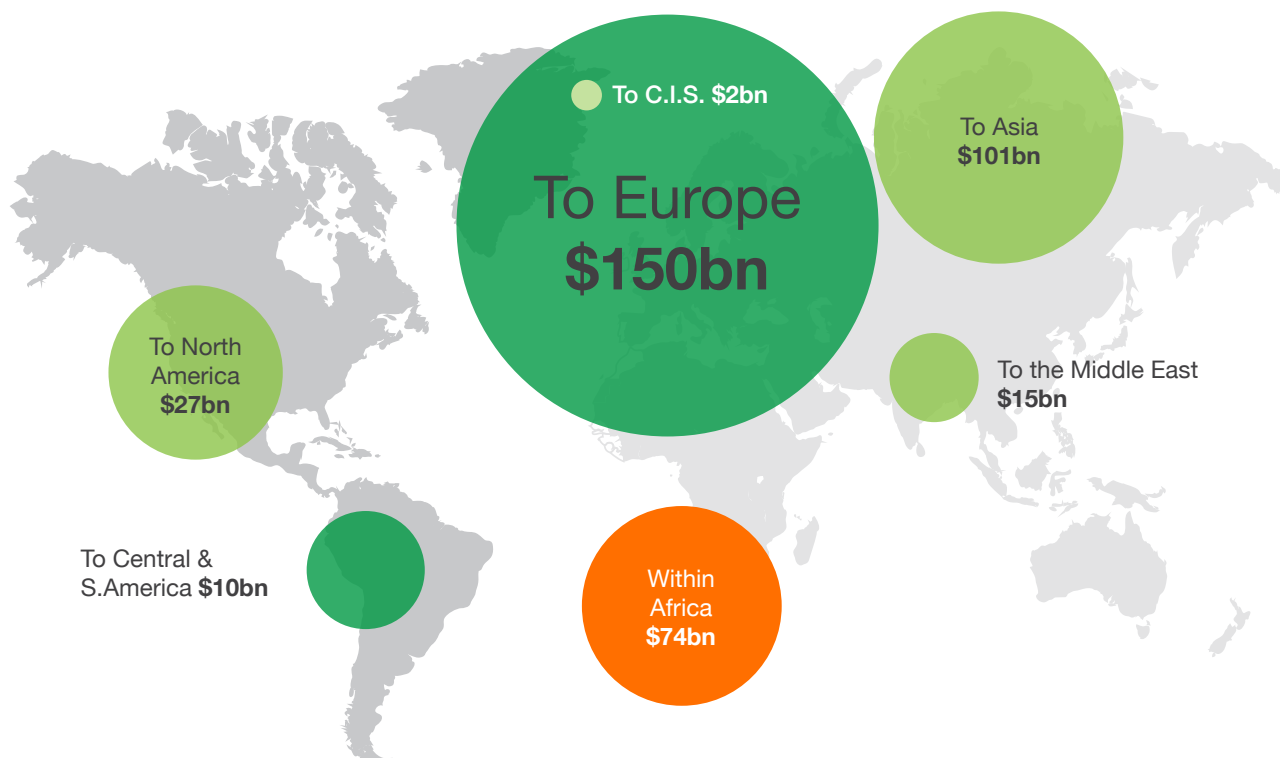
*African Trade (Exports and Imports) and GDP (in USD Billions - Constant 2000)*

Source: World Bank



## AFRICA'S MERCHANDISE EXPORTS

by region (2015)



The balance of African trade has changed in recent years, as Asia has begun to rival Europe as a destination for African exports. The two regions account for 65% of African merchandise exports, as trading ties with the rest of the world remain weak, including perhaps surprisingly North America. The biggest weakness in the composition of the continent's trade, however, is the fact that intra-African trade comprises just 19% of total African exports.

### AFRICA'S TRADING PARTNERS

	AFRICAN MERCHANDISE EXPORTS BY REGION (2015)	
	US\$bn	%
AFRICA	74	19%
EUROPE	150	39%
ASIA	101	26%
NORTH AMERICA	27	7%
MIDDLE EAST	15	4%
CENTRAL & SOUTH AMERICA	10	3%
COMMONWEALTH OF INDEPENDENT STATES	2	0.5%
<b>TOTAL WORLD EXPORTS</b>	<b>379</b>	

Source: WTO

# African Development Bank

## AFRICA & WORLD TRADE

The United Nations Conference on Trade and Development (UNCTAD) Trade and Development Report (TDR) 2016 indicates that global economic growth has remained weak, growing at a rate below 2.5% in 2016, and global trade slowed down dramatically to around 1.5% in 2015-2016, compared to 7% before the global economic crisis. The decline in world commodity prices in 2015 had a significant impact on the value of merchandise trade.

The global ratio of merchandise trade to GDP that fell sharply in 2009 following the global economic crisis and bounced back quickly in 2010-2011 started to show signs of gradual decline in 2012-2014 it declined gradually, before falling significantly in 2015 -2016. This is attributed to the loss of dynamism in advanced economies, combined with low commodity prices and global financial instability which has had a knock-on effect on most developing countries. The global slowdown in trade has impacted the growth of developing economies significantly. UNCTAD projects an average growth of less than 4% in developing economies this year, but with considerable variation across countries and regions. Whereas Latin America is in recession, growth in Africa and West Asia is slowing down to around 2%, East, South-East and South Asia is still growing at a rate close to 5%.

Export growth has continued to play a vital role in Africa's economic growth performance and it has the

### WORLD TRADE GROWTH

Growth in world merchandise exports (in %)



potential to create a multiplier effect through promotion trade induced industrialization. Although exports from Africa in 2015 were worth US\$373.1 billion, this was a big decline by -39.8% since 2011 and down by -34.9% from 2014. African exports represent an estimated 2.3% of total world exports which were \$16.239 trillion during 2015.

Based on statistics from the International Monetary Fund's World Economic Outlook Database, the total Gross Domestic Product (GDP) for African countries amounted to roughly \$5.809 trillion in 2015. Exports account for about 6.4% of Africa's total economic output. Given Africa's population of about 1.153 billion people, the total \$373.1 billion in 2015 African exports translates to roughly \$323 for every person on the continent.



## GLOBAL EXPORTS BY REGION (IN %) Percentage of world merchandise exports by region, 1953-2015

	1953	1963	1973	1983	1993	2003	2013	2015
NORTH AMERICA	24.8	19.9	17.3	16.8	18	15.8	13.2	19
SOUTH & CENTRAL AMERICA	9.7	6.4	4.3	4.4	3	3	4	4
EUROPE	39.4	47.8	50.9	43.5	45.4	45.9	36.3	37
COMMONWEALTH OF INDEPENDENT STATES	3.5	4.6	3.7	5	1.5	2.6	4.3	2
MIDDLE EAST	2.7	3.2	4.1	6.8	3.5	4.1	7.4	4
ASIA	13.4	12.5	14.9	19.1	26.1	26.2	31.5	29
AFRICA	6.5	5.7	4.8	4.5	2.5	2.4	3.3	3
VALUE OF WORLD TRADE (IN BILLIONS)	84	157	579	1,838	3,676	7,377	18,301	15,984

Source: WTO

## AFRICA'S SHRINKING SHARE OF WORLD TRADE

Africa has not, in the modern era, been a major source of exports to the rest of the world. Indeed, since the 1950s, the continent has seen its share of global trade shrink to half its post-war totals.

## INTRA-AFRICAN TRADE REMAINS LIMITED

Among all the regions of the world, intra-regional trade is lowest in Africa, accounting for approximately 19 per cent of the total value of African trade in 2015, although this is a big increase on the 11 per cent recorded in 2012 and even the 15.4 per cent recorded in 2014. This rise is partly a function of the fall in the value of African commodities to the rest of the world but is also the result of rising trade volumes between African states. Cross-border transport links are improving, with new investment in both road and rail projects. In addition, regional trade groups, such as the Southern African Development Community and East African Community are eroding trade barriers.

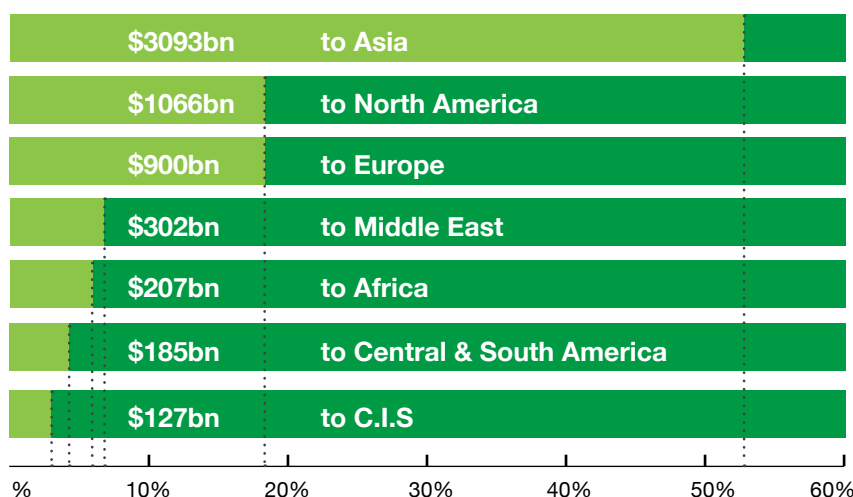
The top 10 African exporting countries South Africa US\$81.5 billion (21.9%), Nigeria \$49.5 billion (13.3%), Algeria \$34.6 billion (9.3%), Angola \$34.1 billion (9.1%), Morocco \$22.2 billion (6%) Egypt \$20.1 billion (5.4%), Tunisia \$12.9 billion (3.5%), Ghana \$10.3 billion (2.8%), Libya \$9.5 billion (2.6%), Côte d'Ivoire \$8.4 billion (2.2%), accounted for 75.9% of African exports in 2015. Among the top 20 African exporters, the only countries to increase the value of their exports were diversified economies that were not impacted by oil price slump which included Ethiopia (up 92.3% from 2011 to 2015), Cameroon (up 83.6%) and Morocco (up 2.7%). It is important to note that, with the decline in global oil prices, Africa's exports of intermediate goods are dominated by mining products and resource-based manufactures such as basic metals or chemicals and fuels; this is consistent with a forward integration into global value chains, but merely as exporter of raw materials and other intermediates embodying limited value addition. Despite its limited size, intra-African trade in intermediates is significantly more diversified than the corresponding trade with the rest of the world. The scope for incipient emergence of regional value chains,

particularly in the manufacturing sector, is however still largely untapped due to an array of structural and policy constraints. The shallowness of regional supply chains can be gauged by the fact that Africa sources 88 per cent of its imported inputs from outside the region. Consistent with global trends, intermediate products accounted for the bulk of Africa's merchandise trade, accounting for about 60 per cent of Africa's total merchandise imports and over 80 per cent of its exports. In addition, intermediates represent the most dynamic component of Africa's merchandise trade, increasing fourfold over the last decade; yet Africa only accounts for 2-3 per cent of the global figure. Imports of manufacturing intermediates have expanded remarkably, yet this has largely failed to reverse Africa's premature deindustrialization, and spur the emergence of viable regional supply chains.

The statistics, facts and figures clearly suggest that a renewed efforts has to be put in place to reinforced recognition that export trade and wider access to trade finance is critical for sustainable economic development of Africa.



## ASIAN EXPORTS (IN \$BN AND %)



Asian economies' trade has developed not only with the rest of the world, but within their own region

**AFRICA ACCOUNTS FOR LESS THAN ONE PER CENT OF MANUFACTURING VALUE ADDED AND IMPORTS MANY OF THE MANUFACTURED GOODS THAT IT USES**



Perhaps the most striking feature of Asian international trade is that more than half of it takes place with other Asian countries. Likewise, integration in post-war Europe drove helped drive economic growth; so that 68.5% of the continent's international trade now takes place between different European countries. Intra-regional trade was also the key to more equitable, sustainable growth in Europe. Even the three North American countries trade more with each other than with the rest of the world put together.

Africa accounts for less than 1 per cent of global manufacturing by value and imports most of the manufactured goods that it consumes. Exports of mining, oil and gas commodities, which represent the bulk of the continent's trade, do not lead to the creation of many productive jobs. Of equal value, given the current external

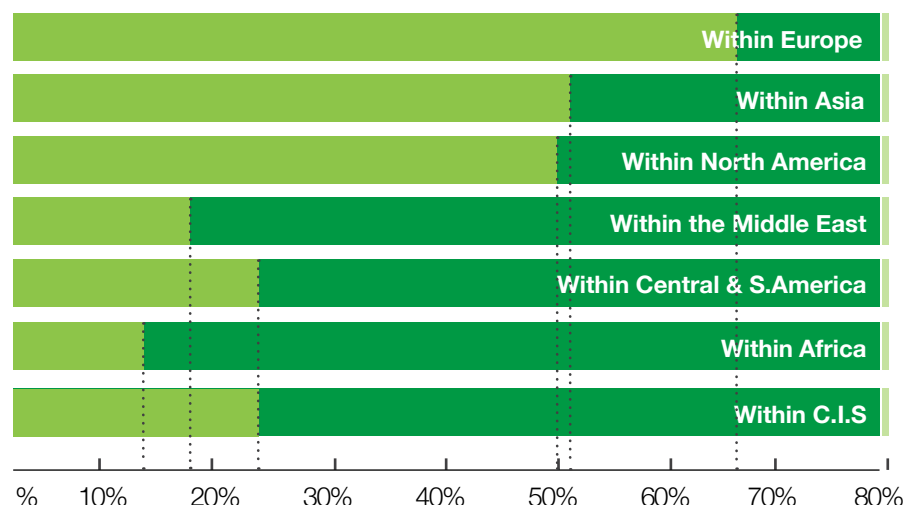
### TRADING WITH ASIA

Growing trade with Asia has often been heralded as a sign of Africa's growing importance on the world stage. Certainly the increase in African exports to and imports from Asia has had an impact on growth, but the Asian economies' emergence was in large part due to improved links between countries in Asia.

SOURCE: WTO



## GLOBAL INTRA-REGIONAL TRADE (IN %)



## REGIONAL TRADE

While global trade has been responsible for generating growth and employment in many developing markets, progress has, in most cases, ultimately been secured by improving links with regional neighbours.

SOURCE: WTO

**THERE IS AN ADDITIONAL BARRIER THAT IS CURRENTLY PREVENTING COMPANIES, PARTICULARLY SMALLER COMPANIES, FROM PARTICIPATING IN THE CROSS-BORDER GROWTH IN TRADE: LIQUIDITY**

environment, is the way that building strong regional markets insulates developing countries from external shocks that emanate from the industrialised world. The infrastructure deficits that have contributed to this ongoing problem are well known, and despite concerted efforts in the political sphere to improve the links within and between the continent's major trading blocs, policy and regulatory hurdles remain.

However, there is an additional barrier that is currently preventing companies, particularly small and medium sized enterprises (SMEs), from participating in the cross-border growth in trade: liquidity. With the cost of trade still high in the developing world – far higher than in industrialized economies – SMEs face significant challenges in accessing the credit they need to get

their goods to market. The international financial crisis saw many financiers pull back liquidity from emerging markets and from trade finance more generally in order to cover positions in their home jurisdictions. Local financial institutions found it hard to access credit in international markets, with considerable knock-on effects for SMEs, while international banks have sought to reduce their exposure to emerging markets to protect their core interests. This withdrawal has reduced the already limited access to credit in most of Africa.



## African Development Bank

# DEVELOPMENT OUTCOMES

### TRADE FINANCE IN GLOBAL TRADE

If the role of development financiers is to deploy resources where both the need and potential impact is greatest, the financial crisis and ensuing economic downturn around the world created whole new areas for them to intervene in. One of these was the sudden requirement to put money into the global system of trade.

Multilateral Development Banks (MDBs) have been working to fill the gaps in trade for many years. Trade finance is a commercially viable business as long as the risks for commercial banks are managed and mitigated. MDBs, with their strong financial backing and credit ratings, are able to create facilities that can de-risk transactions for commercial banks and help to promote trade. The European Bank for Reconstruction and Development began its Trade Facilitation Programme in 1999 in order to promote foreign trade in its countries of operation in Eastern Europe, the Middle East and the Mediterranean. The success of the model has been adopted by other international financial institutions, including the Asian Development Bank and Inter-American Development Bank.

Development finance institutions (DFIs) also reacted to the drop in trade resulting from the global financial crisis by supporting trade finance through the Global Trade Liquidity Programme, among other initiatives. For DFIs, there are clear benefits to supporting trade finance. Low income countries and fragile states, which are considered high risk by commercial banks, are often the first to suffer in times of tightening credit supply. This is equally true of SMEs in developing markets. Small businesses are very often the largest source of job creation and supporting their success has immediate and obvious development outcomes.

Yet trade finance has most easily been accessed by large corporations and it is still difficult to target SMEs. Global commercial banks are often reluctant to support trade in developing countries because of perceived high levels of risk, relatively weak banking systems and limited transaction data. According to research by the Asian Development Bank, the highest rejection rates for trade finance were recorded by clients in Russia, Middle East

# \$1.6TN



The Global trade Finance Gap by 2014 was estimated to be at about US\$ 1.6TN. Africa's trade Finance Gap in 2013 and 2014 was estimated at US\$ 94 billion respectively with, while the comparative estimated gap was US\$ 120 billion in 2011 and 105 billion in 2012. Although this trend suggests a gradual narrowing of the gap in Africa over time, it is important to note that the gap is still significant.

and North Africa, and Sub-Saharan Africa. It is clear that the cost and complexity of compliance with regulatory requirements, including Basel III and anti-financial crime regulation, is a substantial obstacle to the provision of trade finance.

Like its predecessor, the liquidity, capital and leverage requirements of Basel III are designed to encourage banks to incorporate trade finance into their leverage calculations, by factoring in short term contingent liabilities relating to trade finance. This could push banks with capital constraints out of the market. Limited support from international banks for African trade finance means that African banks must take the lead. Trade finance default rates are higher in Africa than in the rest of the world, averaging 4 per cent in comparison with a global average of less than 1 per cent. This varies from an average of 1.1 per cent in Southern Africa to 6.3 per cent in West Africa. There is an obvious correlation between stability and access to trade finance. However, trade finance default rates are significantly lower than banks' overall non-performing lending ratios. Average default rates for

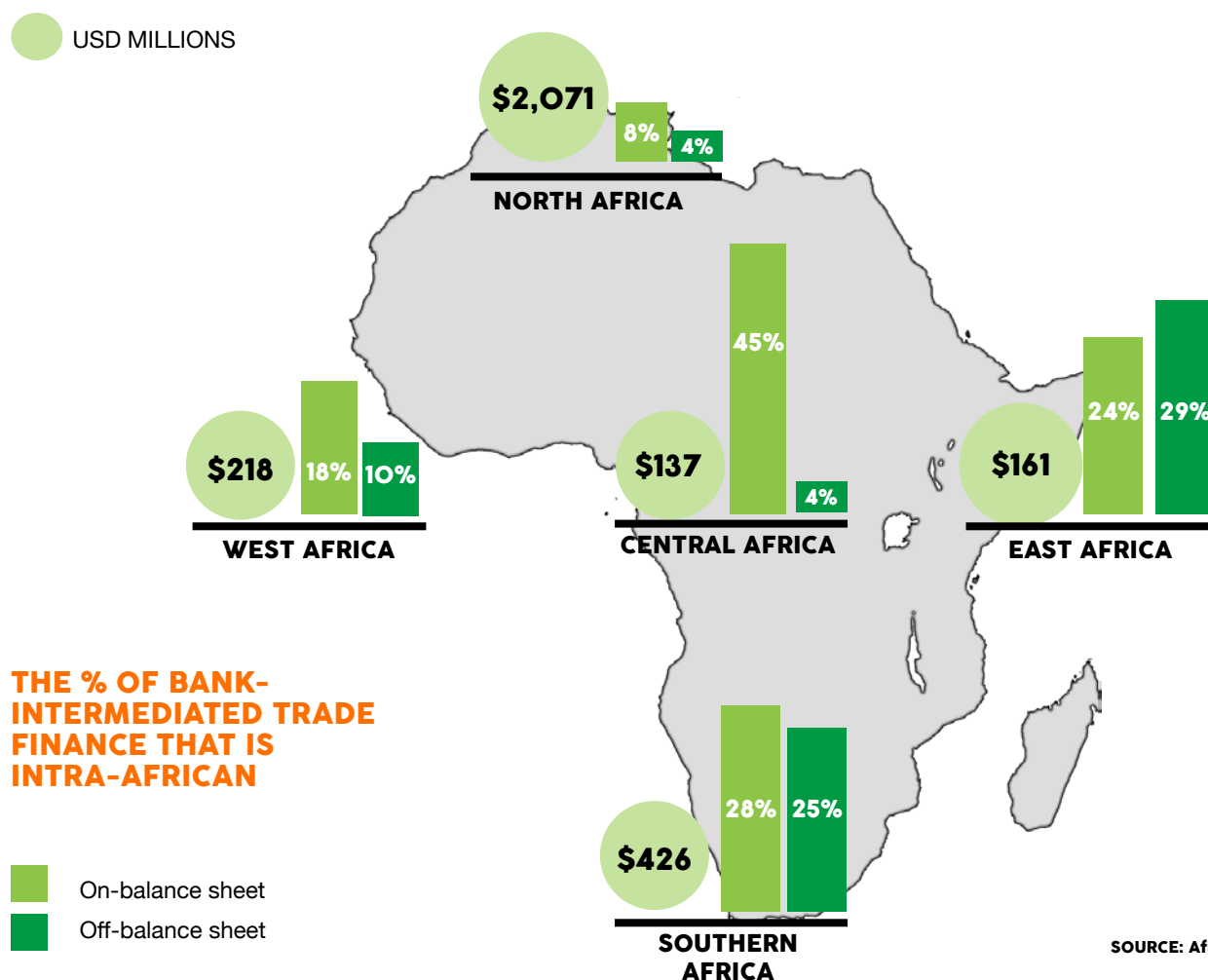
all assets are 4 per cent in Southern Africa, ranging up to 12 per cent in West Africa. Commercial African banks already generate 17 per cent of their earnings from trade finance and only one out of every 14 African banks is yet to enter the trade finance market revealing substantial appetite for the sector.

Many African banks expect to increase their trade finance activities but there are still many obstacles to overcome. These include low US dollar liquidity, regulation compliance, slow economic growth, and the inability to assess the credit-worthiness of potential borrowers. The requirement of confirmation of letters of credit (LCs) remains a major challenge for African banks as virtually all LCs issued by banks on the continent require confirmation when the counterparty is located outside the region. Given the limits on risk headroom by confirming banks for African issuing banks, a large number of the latter are highly constrained in providing needed trade finance. Given these obstacles, governments and DFIs must continue to play a big role. In particular, trade facil-

itation programmes that address US dollar liquidity and relax constraints from binding risk are needed to meet the increasing demand of African firms for trade finance.

Given this reality, the AfDB's trade finance programme - backed by the AfDB's AAA credit rating - is a welcome addition to on-going trade facilitation programmes instituted by a number of DFIs. An estimated US\$340 billion - or a third of all African trade - is backed by bank-intermediated trade finance, although this proportion is higher in North Africa than in the rest of the continent. Just 18% of this US\$340 billion comprises intra-African trade. Intra-African trade accounts for 19 per cent of the total value of African trade. A great deal of the demand for trade finance comes from labour intensive industries, such as agriculture and agribusiness. Interventions in these sectors, which in African countries are typically the largest employers and contributors to GDP, are broad-based.

## AVERAGE ANNUAL VALUE OF LETTERS OF CREDIT ISSUED BY BANKS IN 2014 & 2015





# INTERVIEW

## INTERVIEW WITH YAW ADU KUFFOR

Manager, Trade Finance Division

### Can you set the scene in terms of the current position and challenges facing Africa in terms of global trade and finance?

The markets of Africa are emerging developing markets with a huge dependence on open access to international markets where to a large degree primary commodities are the mainstay. Africa has been in a challenging position for quite some time, since the financial crisis but the challenges were becoming to a large degree manageable.

Recent international events have compounded these challenges: Brexit creates uncertainty and uncertainty slows investment decisions and hinders signing off on trade market access agreements. We are also seeing a return to trade protectionist posturing by some leaders and potential leaders across the globe, the immigration problem in Europe can also be expected to have negative consequence for remittances as a source of funds for the poorer developing countries in Africa. Europe which included the UK as part thereof, provided tariff free access to the least developed countries on the African continent. This is now all up in the air. Simply put, trade is important everywhere but nowhere is trade development more critical today than in Africa, which we know has the world's highest proportion of low-income countries and yet accounts for only 3.3 per cent of global trade. Let's be frank: slow export growth in most African economies is being exasperated by a rebalancing of the global economy. Just look at the changing the face of African trade as we speak. Possible recession in some of the key traditional export markets of Africa, low levels of growth, high unemployment and economic uncertainty persist across the European Union, China continues to grow but at a slower pace – and as just mentioned – Brexit! Even the simple fact of the weakening of the Sterling has had an immediate negative impact on African exports.

### If the expectation of global trade growth is subdued, then can you elaborate on then what Africa can do to counter these challenges?

We need to focus on intra-African and trade diversification while not losing sight of the supply chain connectivity Africa has already developed over the years with traditional markets. Stronger intra-African trade can act as a driver for growth. It is widely known that Africa's exports are 80% based on raw unprocessed commodities and 20% processed goods, intra-African trade accounts for 40% of the former and 60% of the latter. For instance, looking back in time we can see that international trade was at the heart of the economic boom and internationalization that came from Asia. This trade expansion in Asia drove the creation

of productive value added employment, in particular in manufactured goods, as developed markets, rightly in my view took advantage first of labour arbitrage and then benefitted further from the increasing sophistication of the production capacity that evolved in Asia. While success in transforming an economy depends on your starting position it is clearly evident that larger numbers of higher quality jobs moved millions of South Korean and Chinese people out of poverty. The current dynamic in Africa can provide a similar opportunity – we have the natural resource, we have the people, we have the talent – that is the opportunity!

### I am not so sure I agree with you 100% on that point. For instance, when you look at the collapse in commodity prices which were and still are an African mainstay does the proposition of expanding trade really hold out that opportunity?

History has shown us that some of the best innovations have been borne, not from creative thinking but through necessity. In Africa we have necessity – but we also have the creative human resources to innovate. Trade within the continent of Africa can be a driver of growth. More importantly, intra African trade can also be the key to more equitable and sustainable growth right across the continent. But for that to happen we need to improve the physical infrastructure and work toward reducing the non-tariff barriers as well. Think about it: Africa accounts for less than one per cent of manufacturing value added and imports a huge proportion of the manufactured goods that Africa consumes. Exports of primary commodities, which represent the bulk of the continent's trade, do not lead to the creation of so many productive jobs. Challenge and opportunity!

Of equal value, given the current external environment, building strong regional markets can help insulate developing countries within Africa from external shocks that are more frequently tending to emanate from the advanced economies. Strong and accessible regional markets also offer scope and opportunities for SMEs to expand their activities in these markets and benefit from economies of scale. We can see that in terms of trade Africa has an open door policy with the rest of the World – now we need to be more effective in opening doors and connecting countries for trade within the African continent itself.

### OK – point taken, but what can the African Development Bank do to advance this proposition: where does your Trade Facilitation Programme fit in, and what exactly can you hope to achieve?

We are not just hoping to achieve – we are demonstrably achieving. First, the objective of the Bank is to promote sustainable economic growth in our member countries and by extension that means poverty reduction. As a trade specialist Vincent, you know that growth derives from trade and investment, so by facilitating trade we are targeting the essential first element of the growth equation. Facilitating trade as you know has a pretty much immediate and positive impact.

Second, the perception used to be that the trade finance market in Africa was sufficiently served by the commercial players. We now know from various studies, some of them articulated at your annual meeting in Johannesburg, that this is not the case and that there is a sizeable funding gap. I am not going to blame everything on the 2008-09 financial crisis, but it was a negative tipping point. What can we do at the AfDB you ask: Well It is part of our mandate to address market failure, and that implies that the TFP will go where the commercial market, which in reality means where commercial trade finance banks are unable or unwilling to go.

**Right, so you have outlined where the AfDB is going but can you be more specific about how you are going to get there – I mean can you concisely explain how the trade facilitation measures actually work?**

I am happy to do so. The TFP offers 3 complementary products core products: the Risk Participation Agreement which we call the RPA; the Trade Finance Line of Credit-the TFLOC; and The Soft Commodity Finance Facility-the SCFF. Similar to the model developed by the other multilaterals such as the EBRD, the RPA is an unfunded facility. This is targeted at confirming banks that require capital relief to provide more support in confirming letters of credit coming from issuing banks in Africa. Alternatively, the TFLOC allows AfDB to extend direct financing by way of advances to local banks specifically for trade finance. The local banks then extend finance to viable trade finance projects brought forward by their export and import customers.

The Soft Commodity Finance Facility-the SCFF is targeted at supporting export marketing entities and similar institutions engaged in providing agricultural inputs to local farmers. This one gets right down to the lowest level in the agricultural commodity supply chain and in doing so puts previously unavailable financial resources in the hands of the baseline mainstay commodity producers, the farmers. This in turn supports the marketing of soft commodities such as coffee, cocoa and tea. As the bank is continually updating and innovating in the trade finance support structures I suggest that you visit: <http://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/trade-in-anceprogram/>

**Thanks - that is now concise and clear. I can see how these targeted trade finance measures can help bridge the trade finance gap you mentioned. Can you elaborate on the size of this trade finance gap in Africa or is this just subjective guesswork?**

At the AfDB we have been far from subjective in determining the trade finance gap in Africa. Let me elaborate; The AfDB commissioned an African continent-wide trade finance survey, the results were published in December in 2014 and discussed with stakeholders in early 2015 and on an ongoing basis since then. This objective study provided some insightful findings: First, the survey revealed that the estimated value of bank-intermediated trade finance in Africa is between USD 330 billion and USD 350 billion. This represents roughly only one third of Africa's total merchandise trade which our friends at the WTO estimated at USD 1.29 trillion in 2014.

It is no surprise that most of this bank intermediated trade finance is made up of documentary trade credit, no-

tably confirmed letters of credit. Second, it was also observed that the share of bank-intermediated trade finance devoted to intra-African trade represented only 18% (USD 68 billion) of the total trade finance assets of banks in Africa and quite surprisingly, that most of this financing was made up of trade loans rather than documentary trade facilities such as letters of credit. Third, quite alarmingly the AfDB survey report revealed that the unmet demand for bank intermediated trade finance is as high as USD 120 billion. This is significantly higher than previous estimates which were as low as USD 25 billion. The gap is also bigger in fragile states and low-income countries than in middle-income countries.

**Alarming indeed. Sitting here today doing this interview, can you spell out in**

a few words what you see as the primary headwinds holding back the advancement of trade expansion across Africa?

The external risk perception about Africa is still not very positive, and added to this is the growing cost of regulatory compliance to financial institutions. Basel III capital requirements and the ardent desire of global banks to avoid falling foul of various regulatory compliance regimes, whether in respect of capital adequacy or anti-money laundering, are constraining the availability of adequate trade finance support in Africa.

In advanced economies the bigger players 'derisking' policies are having a negative impact. The negative consequences of these de-risking policies will be felt more severely over the medium term. It was good to see the IMF lead by Christine Lagarde in her address to the New York Fed on 18 July 2016 set out the challenges 'de-risking' and closure of correspondent relationship accounts are creating particularly in developing markets. The initiatives of the Financial Stability Board, the World Bank and other stakeholders such as the ICC must be commended in bringing together policymakers and the private sector to develop a shared understanding and possible solutions to these challenges. Furthermore, it is no secret that the recent fall in the price of oil and other primary commodities is proving to be a significant challenge especially for oil-dependent export economies such as Nigeria, Angola, Congo and Gabon. With such commodities predominantly priced in dollars and the price of the commodity at low levels then clearly dollar liquidity becomes a challenge.

**You paint a challenging picture. Do you have specific figures on the actual impact of the fall in commodity prices?**

Yes, off the top of my head I can provide you with headline figures. The World Trade Organization, by way of their International Trade Statistics 2015 indicated that Africa's total merchandise export fell by 8% in 2014 compared to 2013 – imports grew by a paltry 1%. As a result of the fall in Africa's key export commodity prices and other fiscal slippages, major African economies such as Nigeria, Angola, Ghana and South Africa are experiencing currency challenges. This has left many local banks in these countries struggling to fulfil their trade finance commitments to international confirming banks. Despite the challenges the feedback from international commercial banks in terms of cooperation and final reimbursements are predominantly good news stories. Within this context, our Trade Finance Program has provided counter-cyclical support to local banks in Africa to help cushion the effects of foreign currency shortages.

## African Development Bank

# DEVELOPMENT OUTCOMES



## THE AfDB IN TRADE FINANCE

Currently, there is a funding gap in African trade finance that is measured in the billions of dollars. Around a third of African countries have interest rates in excess of 10% on trade loans offered on a non-sovereign basis and cash collateral requirements of up to 50 per cent of the value of the loans. These prohibitive terms are serious hurdles to the development of Africa's trade. Additionally, the external economic environment has reduced the need for African goods and commodities, while structural problems, including non-convertible currencies, weak regulatory and policy frameworks and inefficient institutions have affected the development of import and export industries.

The African Development Bank's ten year strategy (2013 –2022) which focuses on the High 5" strategic priorities to 'power and light up Africa'; "feed Africa"; "industrialize Africa" "integrate Africa"; and "improve the quality of life of the people of Africa" and its Financial Sector Development Strategy (2014-2019) place a strong emphasis on private sector development, which it sees as vital to economic and social progress. To achieve this, the bank believes that the continent needs more open economies and increased trade, both within Africa and between African countries and the rest of the world. Trade facilitation is an essential part of private sector development.

Trade finance improves the macroeconomic resilience of countries by protecting their important export industries against external failures in liquidity and confidence. This is particularly important where the commodity

being exported is a major or primary source of earnings for a country, or where overseas equipment is needed for industrial expansion and job creation. Trade gives Regional Member Countries (RMCs) access to technology and critical inputs that are essential to move up the value chain.

Where the primary sources of the exports being facilitated are in fragile states or low income countries, interventions in trade finance directly impact poverty reduction, while trade in medication, energy and food has significant influence on development outcomes. Sub-Saharan Africa food imports are estimated at more than US\$30 billion annually, and the entire region now generates less income from agricultural exports than Thailand. To guarantee food security, trade finance is available for imports of fertilizers, seeds and crop protection inputs. Agricultural export industries, such as West African cocoa, are crucial to rural development.

Trade finance also supports private sector development by allowing enterprises to meet their investment and working capital needs and to prevent supply shortages. By giving security of operation to companies in Africa, interventions in trade finance help to convince enterprises to invest in their operations and their workforces, thereby sustaining and creating jobs.

Existing MDBs and other agencies have supported trade finance in Africa, but have been unable to keep up with the large and growing demand.

While some of the external conditions that led to the original shortages in trade finance have now moderated, most of the development banks active in the space have found that demand for their services has remained high in developing countries. Many of the banks that, pre-crisis, were active in trade finance are still facing serious problems in their home markets and may struggle to



## MAJOR ACHIEVEMENTS

- » The Bank has supported more than 1,000 trade transactions involving 85 financial institutions in more than 20 Countries for a cumulative trade value of USD 3 billion.
- » Intra-Africa trade accounted for approximately USD 600 million, representing at least 20% of total trade supported.
- » From 2013 to 2015, the Bank approved 21 trade finance facilities comprising 13 Risk Participation Agreements (RPAs), 11 Trade Finance Line of Credits (TFLOCs), 1 Soft Commodity Finance Facility (SCFF) and 2 Equity investments.
- » Four of the RPAs have been signed with Standard Chartered Bank, Commerzbank, Ecobank and Afreximbank.
- » In just 3 years, the Bank approved RPAs for 11 confirming banks and more than USD 3 billion of trade has been supported.

return to funding African trade for years.

Encouraged by the success of the response to the trade finance initiative and recognising Africa's rapidly increasing finance needs, the AfDB aims to consolidate its role as a provider of trade finance through its Trade Finance Programme (TFP). The Programme was set up in 2013 for an initial period of four years with a limit of US\$1 billion. The TFP offers a wholesale approach to trade finance through the provision of risk mitigation facilities and liquidity support. The bulk of the operations are targeted at low income countries, African local banks, small and medium enterprises in critical sectors such

as agriculture/agribusiness, light manufacturing and intermediate/capital goods in regional member countries.

The Bank deploys a number of instruments as it increases its participation in trade finance: Trade Finance Lines of Credit; Risk Participation Agreements; and Soft Commodity Finance Facilities. Alongside these, the Bank seeks to add trade finance components to other regional infrastructure or trade facilitation operations and to build the capacity of institutions participating in trade finance or using trade finance facilities.

The Bank also participates in joint initiatives with other MDBs and development financial institutions, where the development impact is strong and compelling. While these programmes have been effective, they have left gaps which the Bank is well positioned to address. The AfDB hopes to have RPAs in place with at least 15 of the most active confirming banks in Africa within 4 years of the programme's inception, creating ongoing additional risk capacity in trade finance of around US\$20 billion. The aim is to have comprehensive geographical coverage across Africa, with an emphasis on underserved markets, in particular the low income countries and fragile states that are typically viewed as high risk by commercial banks, as well as sectors that have an impact on poverty reduction, in particular agribusiness and small and medium enterprises. A number of commercial banks continue to express interest in using the Bank's RPA products to expand.

The Bank intends to rely on a wholesale approach to trade finance in order to meet the needs of SMEs. This means focusing on programmes and products that assist financial intermediaries, who can then use their market presence and institutional capacity to reach companies in need of finance.

### Approved and signed projects as at 31 December 2015

Project	Country	Amount (USD m)			
		RPA	TLOC	SCFF	Equity
Standard Chartered Bank	Regional	300	-	-	-
FirstRand Bank	Regional	100	-	-	-
Sumitomo Mitsui Banking Corporation Europe	Regional	100	-	-	-
Ecobank Transactional Inc	Regional	100	100	-	-
Afreximbank	Regional	100	150	-	30
UT Bank	Ghana	-	20	-	-
Shelter Afrique	Regional	-	20	-	-
Unibank	Ghana	-	15	-	-
FBN	Nigeria	-	300	-	-
FSDH	Nigeria	-	50	-	-
BCI	Mauritania	-	10	-	-
ATI	Regional	-	-	-	-
ATI	Zimbabwe	-	-	-	30
ETI	Regional	-	310	-	2.08
Banque de l'Habitat	Tunisia	-	66.90	-	-
Standard Chartered Bank	Regional	200	-	-	-
Meridian	Regional	0	0	20	0
CBA	Kenya	0	40	0	0
<b>Total</b>		<b>900</b>	<b>1,081.90</b>	<b>20</b>	<b>62.08</b>

## African Development Bank

# PRODUCT PORTFOLIO

## RISK PARTICIPATION AGREEMENT (RPA)

This is an arrangement under which a commercial bank and the African Development Bank share the default risk on a portfolio of trade finance transactions. The RPA is designed to give regional and international commercial banks partial cover for their trade finance operations in Africa, with the AfDB typically taking a 50 per cent share of the risk. The commercial bank performs the credit risk analysis on the issuing banks and originates, processes and monitors the transactions. The AfDB will select its commercial partners based on the size of their African trade portfolio, the breadth of their African market coverage, support for intra-African trade and the quality of the credit approval process.



### BENEFITS

- » Provides the partnering bank with cover for a broad range of trade finance instruments; with capital relief and the confidence to enter new markets; and with capacity enhancement in terms of increased limits and tenors.
- » Helps issuing banks to form relationships with new correspondent banks and enhances their risk profile.
- » Gives regional financial institutions the support to become acceptable confirming banks.
- » Offers a stimulus to SME sector financing.

**TENOR** Maximum of 3 years.  
Underlying transactions are limited to 2 years.

**COVERAGE** Up to 50% credit risk.

**PRICING** The fees charged to issuing banks are market-based.

**CURRENCY** Mainly in US dollars and euros

The trade finance gap in Africa amounts to several billion dollars, a gap which has to be bridged if African exporters are to take advantage of the seismic shifts occurring in world trade.

**STEFAN NALLETAMBY,**  
Director, Financial Sector Development  
Department, AfDB

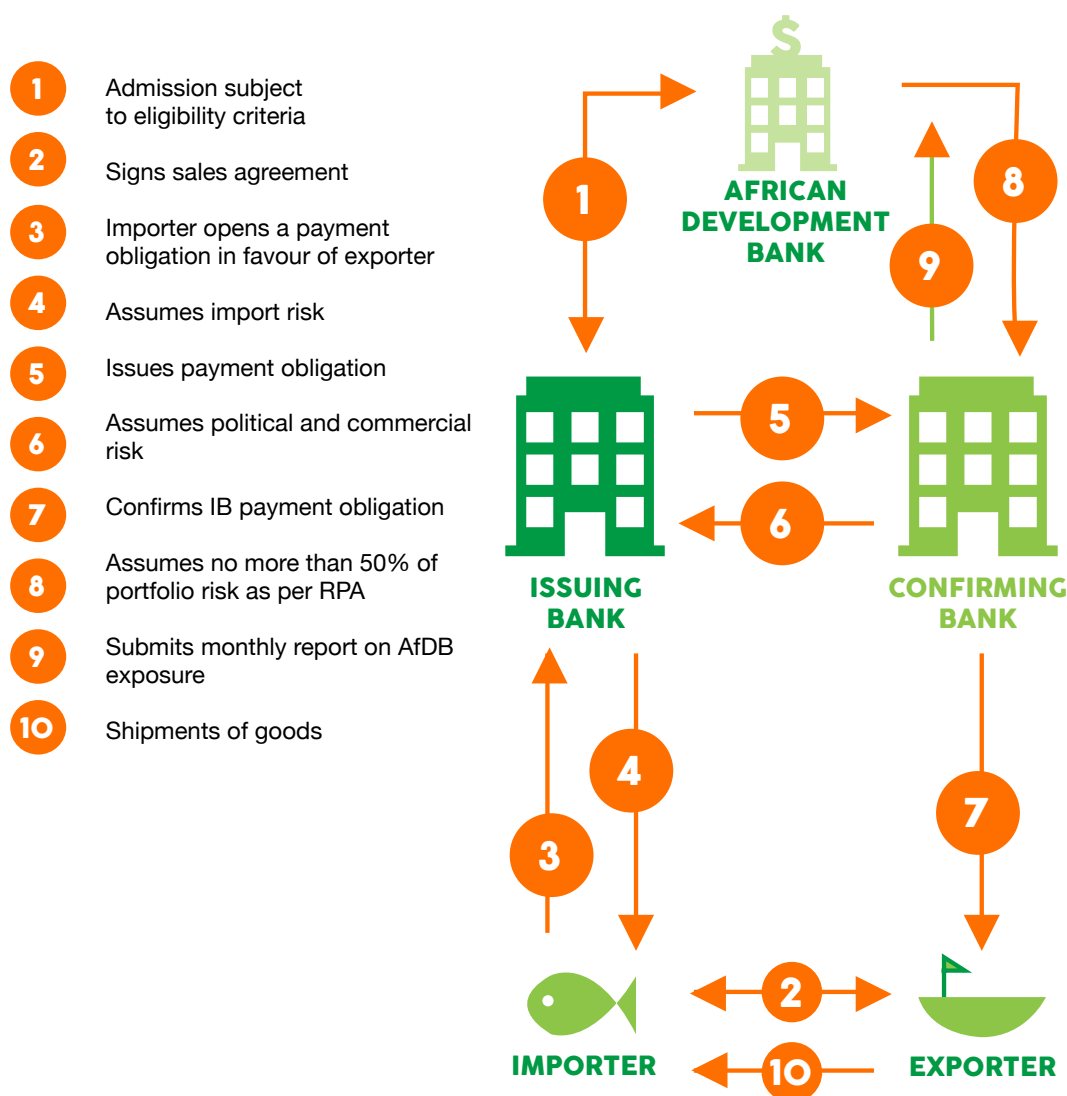
# ELIGIBILITY

The RPA bank must be an established confirming bank that has:

- » Passed the AfDB's due diligence process for trade finance
- » Significant trade finance presence in Africa, or the potential to achieve scale in trade finance in Africa
- » The strategic intent to expand its trade finance business in low income countries
- » A satisfactory AfDB credit rating

The issuing banks under the RPA must:

- » Be located and registered in a Regional Member Country of the AfDB
- » Have passed the RPA bank's due diligence process and received a "no objection" approval from the AfDB
- » Remain in good standing with the AfDB and the confirming bank throughout the lifetime of the RPA
- » Have a strong SME focus





## African Development Bank

# PRODUCT PORTFOLIO

### TRADE FINANCE LINE OF CREDIT

This is a short-term loan, offered to African financial institutions to facilitate their trade finance operations. The AfDB seeks to support financial institutions with a strong focus on SMEs and trade finance, and that have acceptable and satisfactory corporate governance and risk management systems.

The proceeds from a Trade Finance Line of Credit (TFLOC) enable a financial institution to extend credit support to SMEs operating in either the import or export sectors of the economy. Facilities include pre- and post-shipment finance, factoring and import loans, among others.



### BENEFITS

- » Caters for a broad range of trade instruments.
- » Provides vital liquidity in the form of short-term loans to select local banks for on-lending to SME exporters and importers.
- » Could be used to support value chain activities linked to the import and export sectors and as a result help RMCs move up the value chain.

As part of scaling up its trade finance operations, the AfDB will support a number of flagship capacity-building initiatives that address the needs of African financial institutions to better serve the trade finance needs of SMEs in their respective markets.

**BLEMING NEKATI,**  
Chief Trade Finance Officer, Trade Finance  
Division, AfDB

#### TENOR

Maximum of 3.5 years.  
Proceeds can be rolled over  
several times during the tenor  
of the facility.

#### PRICING

Pricing is risk based. The rates  
can be floating or fixed.  
Front-end and commitment  
fees apply.

#### REPAYMENT

Bullet, balloon or straight line  
amortisation. Interest is paid  
semi-annually. The rates can  
be floating or fixed.

#### CURRENCY

Any of the AfDB's major  
lending currencies - the US  
dollar, euro, rand and yen.

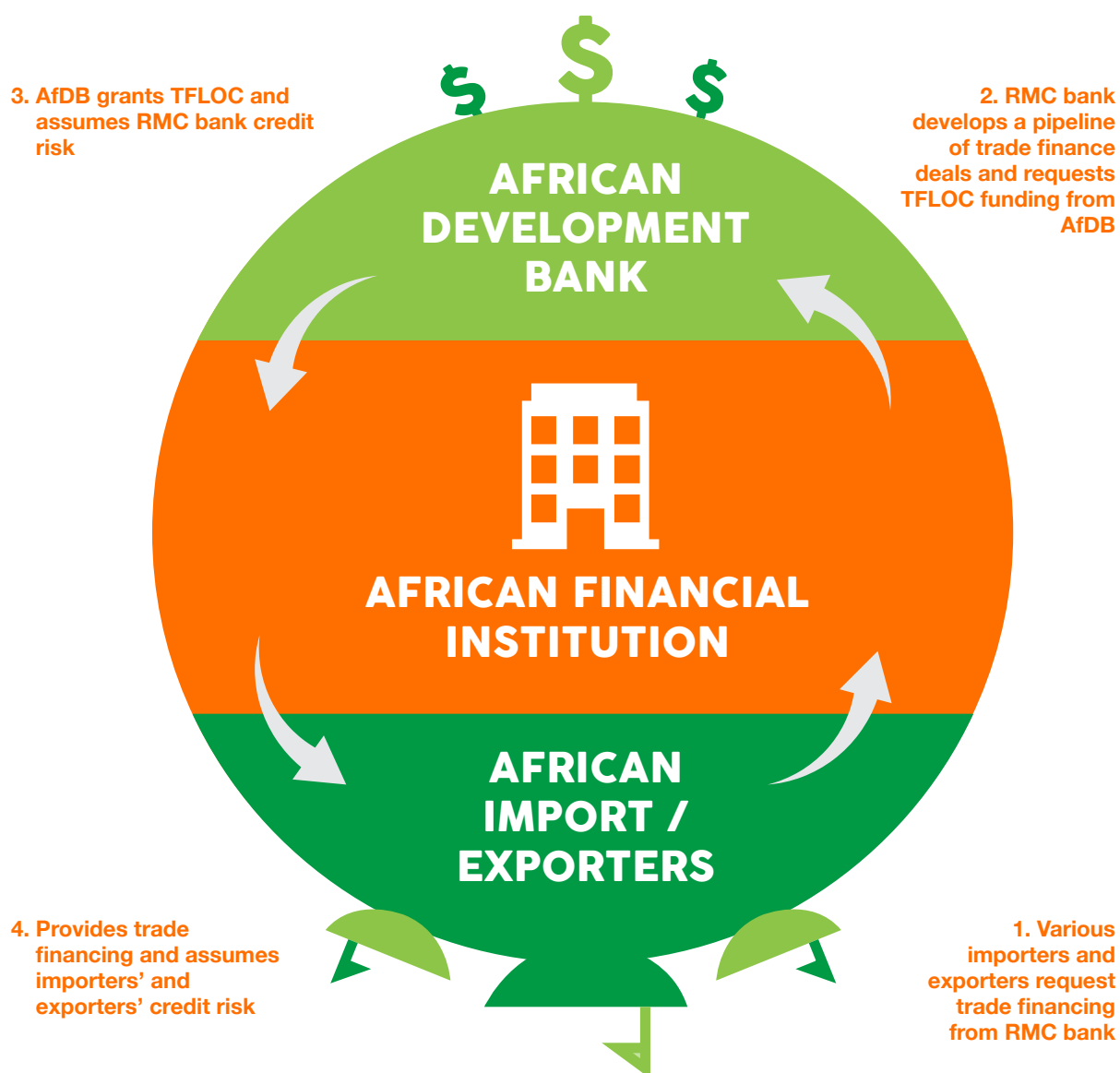
#### SECURITY & COLLATERAL

Unsecured, senior debt

## ELIGIBILITY

The qualifying bank must meet the following key considerations:

- » Passed the AfDB's due diligence process for trade finance and received a "no objection" approval from the AfDB
- » Significant trade finance presence or the potential to achieve scale in their respective market.
- » Attained a satisfactory AfDB credit rating
- » Be located and registered in a Regional Member Country of the AfDB
- » Have a strong SME focus or potential to achieve such potential



## African Development Bank

# PRODUCT PORTFOLIO

### SOFT COMMODITY FINANCE FACILITY (SCFF)

The SCFF is a funded trade finance product targeted at commodity aggregators and export marketing agencies for agri-based products, such as cocoa and coffee. These organisations, which deal directly with farmers, use SCFF loans to support the agri-commodity supply chain at the grassroots level.



### BENEFITS

- » Enables aggregators to purchase greater volumes from farmers, thus reducing post-harvest losses.
- » Allows for presale agreements and advance payments, therefore helping to finance pre-harvest activities.
- » Enables farmers to obtain guaranteed and better pricing and relieves them of the burden of warehousing and post-harvest storage.
- » Supports exports which represent the main source of foreign exchange receipts and liquidity for RMCs.

#### TENOR

Maximum of 2 years. Generally, the facility is structured to align with the cash conversion cycle.

#### PRICING

Pricing is risk based, according to an assessment of the underlying transaction. The rates can be floating or fixed.

#### REPAYMENT

Repayment is tailored to the underlying transactions and could take the form of bullet, balloon, or straight line amortisation.

Interest is paid semi-annually. The rates can be floating or fixed.

#### CURRENCY

Available in all AfDB's major lending currencies - the US dollar, euro, rand and yen.

#### SECURITY & COLLATERAL

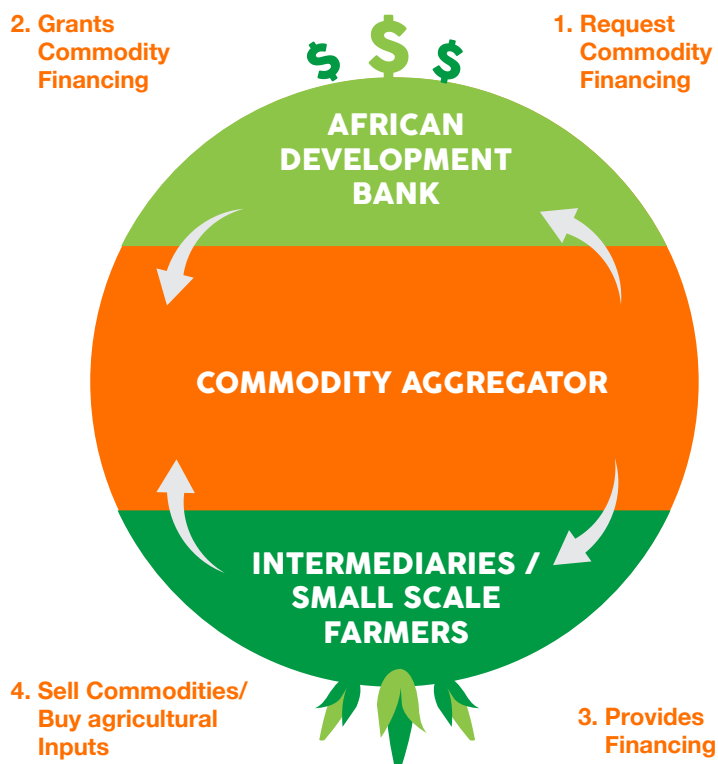
A senior debt obligation, backed by appropriate collateral arrangements.

## ELIGIBILITY

Eligible institutions will mainly be commodity aggregators engaged in the marketing, financing and exporting of soft commodities in Africa.

These institutions:

- » Must be registered and be operating in a Regional Member Country of the AfDB
- » Should be commercially viable on a standalone basis
- » Must have an acceptable level of operational autonomy
- » Must have a strong risk management culture and satisfactory corporate governance practices





## African Development Bank

# CASE STUDIES

## 1 | FOOD COMPANY IN GHANA

<b>AfDB Partner</b>	UT Bank Ghana
<b>Facility</b>	USD 20m TF Line of Credit UT Bank is a leader in SME financing.
<b>UT Bank Client</b>	Food/milling company
<b>Facility</b>	USD 7m (AfDB portion USD 3m)
<b>Purpose</b>	Purchase of machinery/wheat
<b>Client profile</b>	Wholly-owned Ghanaian milling company that produces wheat flour, maize grifts and fish and poultry feed.

One of the only 4 milling companies in Ghana, the company employs 129 staff. Although Ghanians like their yams and plantain, break and pastry are popular with the middle class. In addition, by providing fish and chicken feed to the local fish farming and poultry industries, the facility is contributing to Ghana's food self-sufficiency. AfDB's support also strengthened UT Bank's TF capacity.

## 2 | AGRIC INPUTS CO. IN ETHIOPIA

<b>AfDB partner</b>	Commerzbank
<b>Facility</b>	Confirmation of L/C
<b>Issuing Bank</b>	Commercial Bank of Ethiopia (CBE)
<b>Importer</b>	An agriculture inputs supply company in Ethiopia
<b>Commodity</b>	Compound fertilizer
<b>Amount</b>	USD 13.8 million
<b>Origin of goods</b>	Morocco

By guaranteeing 50% of the transaction against payment risk, AfDB helped increase Commerzbank's risk appetite for Ethiopia and CBE and facilitated the importation of fertilizer to Ethiopia from Morocco increase agricultural production. As an intra-African trade transaction, the facility helped to promote regional integration

## 3 | OIL IMPORTING CO. IN GAMBIA

<b>AfDB partner</b>	Ecobank (Paris subsidiary - EBI SA)
<b>Facility</b>	Confirmation of L/C
<b>Issuing Bank</b>	Ecobank Gambia
<b>Importer</b>	An oil importing company in Gambia
<b>Commodity</b>	Gasoline
<b>Amount</b>	USD 1.5 million
<b>Country of ex- porting company</b>	Switzerland

Until very recently, the importer was the sole fuel importing company in Gambia - a country that relies entirely on oil imports for electricity generation and transportation. AfDB guaranteed 50% of the transaction against payment risk of Ecobank Gambia and helped ensure the continued availability of a critical commodity for Gambia. AfDB's partnership with Ecobank is also contributing to the transformation of this pan-African financial institution into an internationally credible and acceptable confirming bank.

## 4 | ECOBANK TRANSNATIONAL INC

Since 2013, African Development Bank has availed trade finance facilities totalling to US\$ 510 million to support Ecobank Transnational Incorporated with the expansion of its trade finance operations. Ecobank, a banking group with headquarters in Togo and operations in 32 African countries and several others in international financial centres, has been one of the most ambitious of the continent's financial services businesses. The AfDB deal is designed to allow it to enhance its trade finance confirmation capabilities and give medium-term liquidity support to its subsidiary banks at national level, which can then pass on the capital through trade finance to small and medium enterprises around the continent, as well as to larger local corporates.

The first component of the original loan facility was a three-year, unfunded Risk Participation Agreement, to the value of US\$100 million. Under this instrument, the AfDB signed up to share the default risk of a portfolio of qualifying trade finance transactions with EBI SA (Ecobank Paris). The two parties shared equally the risk of transactions originated by issuing banks in Africa, with Ecobank matching each undertaking by the AfDB. This means that the total size of the portfolio is US\$200 million. The second part of the facility was a three and a half year, US\$100 million trade facilitation loan. This will be used by Ecobank's local subsidiaries to support transactions by local corporates and small and medium enterprises in Africa. In 2016, the Bank approved an additional US\$ 310 million trade facilitation loan to EcoBank, this brought the total figure AfDB's support to EcoBank to US\$ 510 Million.

**Trade finance is short-term, and financing of this type can be "rolled over" several times a year.**

**This package will facilitate around US\$1.8 billion in trade of intermediate and finished goods, raw materials and equipment, driving economic growth, employment and poverty reduction.**

### US \$200M

**SUPPORT TO TRADE FINANCE OPERATIONS**

### US \$1.8BN

**OF TRADE FINANCE TO DRIVE ECONOMIC GROWTH**

## 5 | THE AFRICAN TRADE INSURANCE AGENCY

Since 2015, the AfDB has supported at least 4 RMCs (namely Ethiopia, Benin, Cote d'Ivoire and Zimbabwe) with financial resources amounting to USD35 million to become members of ATI.

The ATI, which is the only cross-border African export credit agency, is a multilateral political risk and credit insurer established by international treaty by African member states at the initiative of Common Market for Eastern and Southern Africa (COMESA) in 2000. Due to the systemic significance of the Agency, its Charter underscores the importance of retaining the organization as an African entity.

Its membership comprises: Benin, Burundi, Democratic Republic of Congo, Kenya, Madagascar, Malawi, Rwanda, Tanzania, Uganda and Zambia as well as the following "special category" RMCs, Djibouti, Eritrea, Ghana, Liberia and Sudan.

A specific aspect of ATI's operations is that member states directly assume financial liability for the political risk losses that could affect trade within their own countries. For the past decade, it has offered cover against terrorist-related physical damage risks and now works alongside the Multilateral Investment Guarantee Agency (MIGA) to promote investment in Africa, including via risk sharing agreements on reinsurance and coinsurance projects.

Since December 2013, the AfDB has been a shareholder in ATI, following the approval of its US\$15 million equity investment. ATI provides medium-long term credit and political risk insurance as well as other risk mitigation products to the Bank's RMCs and related public and private sector actors, such as foreign and local investors, exporters, and commercial operators. These products directly encourage and facilitate foreign direct investment and trade both regionally and internationally. Furthermore, ATI also facilitates trade in Africa through underwriting trade credit, which is in line with the AfDB's Trade Finance Programme as well as catalysing private sector investment in infrastructure projects.



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AFRICAN DEVELOPMENT BANK GROUP

<http://www.afdb.org/trade-finance-program>