ICC BANKING COMMISSION | GUIDING INTERNATIONAL BANKING PRACTICE | DRIVING CHANGE IN TRADE FINANCE

# 2015 RETHINKING TRADE & FINANCE

AN ICC PRIVATE SECTOR DEVELOPMENT PERSPECTIVE


World Economic Outlook ›

Global and Regional Trends in Trade Finance ›

Highlight: Trade Finance in Latin America and the Caribbean ›

Business Trends in Factoring, Export Finance and Export Credit Insurance ›

Business Trends in Trade Facilitation Programmes ›

Analysis of Trade Finance Gaps ›

Looking Ahead – Expert Observations and Analysis for the Future ›



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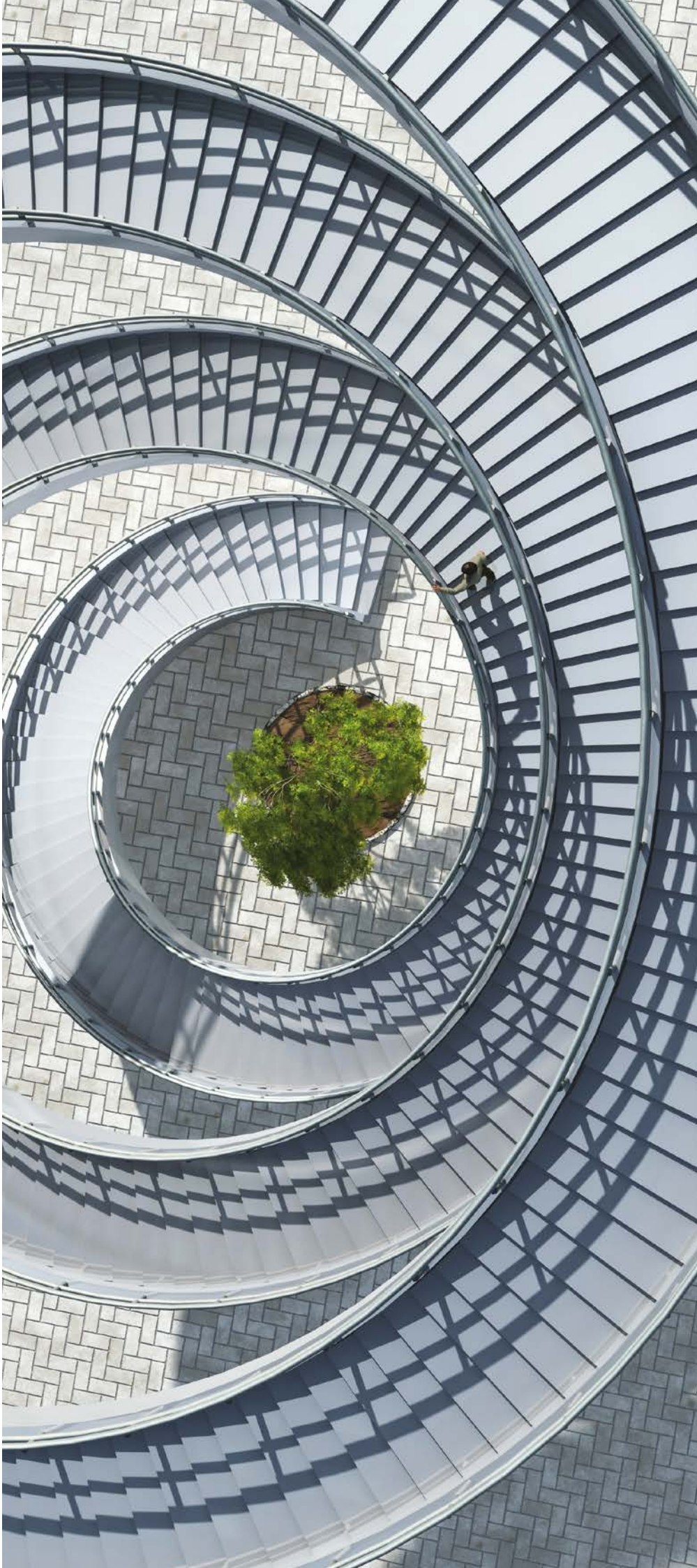

# ACKNOWLEDGEMENTS

**We are very pleased to release the 2015 edition of the annual series Rethinking Trade & Finance, a flagship private sector initiative of the International Chamber of Commerce (ICC). Leading international institutions and foremost experts in banking collaborated in its completion.**

The ICC Global Survey on Trade Finance uncovers patterns in business and trade, helping ICC Banking Commission members and various industry players make sense of these changes and their implications. An accurate snapshot of market trends, the survey enables bankers, traders and government officials to gauge global trade expectations.

We would like to thank all 482 respondents located in 112 countries for their timely, accurate and insightful answers to the survey, thus enabling us to generate the findings of the market intelligence product at hand. We would like to express our gratitude to all our ICC Banking Commission members and to ICC's network of 88 national committees for their valuable involvement in the continuing effectiveness of our shared efforts.

The ICC Global Survey on Trade Finance was established and pursued its remarkable progress over the past eight years in particular thanks to Thierry Sénéchal to whom we address our most sincere gratitude.

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ICC thanks its members and sponsors for their support in the preparation of this Survey.

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ICC is the world business organization, whose mission is to promote open trade and investment and help business meet the challenges and opportunities of an increasingly integrated world economy.

With interests spanning every sector of private enterprise, ICC's global network comprises over 6 million companies, chambers of commerce and business associations in more than 130 countries. ICC members work through national committees in their countries to address business concerns and convey ICC views to their respective governments.

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Key findings


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# ACRONYMS

**ADB** Asian Development Bank
**AfDB** African Development Bank
**BAFT** Bankers Association for Finance and Trade
**BCBS** Basel Committee on Banking Supervision
**BIS** Bank of International Settlement
**Bp** Basis point
**BRIC** Fast-growing developing economies of Brazil, Russia, India, and China
**CCF** Credit Conversion Factor
**DDA** Doha Development Agenda
**EBRD** European Bank for Reconstruction and Development
**ECA** Export Credit Agency
**ECA** Europe and Central Asia
**GTA** Global Trade Alert
**GDP** Gross Domestic Product
**ICC** International Chamber of Commerce
**IDB** Inter-American Development Bank
**IFC** International Finance Corporation
**IFSA** International Financial Services Association
**ILO** International Labor Organization
**IMF** International Monetary Fund
**LAC** Latin America and the Caribbean
**LCs** Letters of credit
**LGD** Loss Given Default
**MDB** Multilateral Development Bank
**MDGs** Millennium Development Goals
**MENA** Middle East and North Africa
**MIC** Middle-Income Countries
**NTM** Non Tariff Measure
**PO** Procedural Obstacles
**PRC** People's Republic of China
**SAR** South Asia
**SME** Small and Medium-sized Enterprise
**SSA** Sub-Saharan Africa
**SWIFT** Society for Worldwide Interbank Financial Telecommunication
**UCP** Uniform Customs and Practices for Documentary Credits (ICC Rules)
**US$** United States Dollar
**WTO** World Trade Organization

# FOREWORD

## Access to trade finance ever more important as economic woes persist.

Many congratulations to the International Chamber of Commerce for producing this comprehensive survey of the development of trade and trade finance across the world.

This report is an immensely useful tool that allows policymakers, regulators and international financial institutions to identify gaps in the availability of trade finance for local banks and their clients.

With its worldwide network of national committees and the high number of members using ICC rules in international trade and trade finance agreements all over the world, ICC is in a unique position to gather first-hand information from market participants. This sort of information is simply not available elsewhere.

2014 was a difficult year for the international trade finance community and continuing economic fragility and growing political tensions suggest that those challenges are likely to persist.

The EBRD's own most recent economic forecasts do not point to a broad-based recovery any time soon. Important emerging economies are caught between the conflicting pressures of monetary easing in the Eurozone and the prospect of a monetary tightening in the United States.

The very sharp recession in Russia is casting a shadow well beyond its borders, putting pressure on economies in the Caucasus and in Central Asia. Even those energy-importing countries that should be benefitting from the relatively low oil price are suffering because of their trade or financial links to Russia.

Ukraine remains under acute economic pressure and most recently Turkish markets have reacted nervously to rising political and security tensions.

Against this backdrop of economic uncertainty, many foreign providers of trade finance have reduced their exposure to business partners in these regions, leading to a shortfall in trade finance for banks, importers and exporters just at a time when they most need it.

At the same time, capital requirements and cost saving programmes have made it more difficult for foreign commercial banks to establish and maintain trade finance facilities also for smaller banks and corporates in emerging markets.

Access to trade finance is particularly important for small- and medium-sized enterprises (SMEs) in early transition countries.

Since foreign importers and exporters and foreign financial institutions are often unable to meet their trade finance needs, smaller and medium-sized importers and exporters in less advanced countries are strongly dependent on trade finance facilities provided by local banks.

Organizations like the EBRD are very happy to help bridge this trade finance gap, in the case of the EBRD by using its Trade Facilitation Programme that works with over 800 partner banks in 26 countries.

The EBRD is particularly grateful to ICC for this report which provides important support for the EBRD's work in trade finance.

I am convinced that it will also help shape the business and development strategies of other developmental financial institutions and trade policymakers all over the world.

**Sir Suma Chakrabarti**
President, European Bank for Reconstruction and Development (EBRD)

# MESSAGE FROM THE CHAIR

## The ICC survey: Driving better information, communication and regulation.

Knowledge is power, and the visibility of that knowledge is essential to trade. Every year the Banking Commission of the International Chamber of Commerce (ICC) and this annual Global Survey on Trade & Finance provide us with knowledge that helps visibly quantify the trade environment and inform crucial industry debate. Whether for factors facilitating trade, obstacles hindering trade, or the changes required to ensure trade growth, the ICC annual Global Survey has become essential reading.

Regulatory changes affecting banks and businesses are well known, but direct and indirect consequences of compliance are harder to specify. Of these, Basel III casts the largest shadow. However, thanks partly to ICC efforts, progress on this front is underway regarding leverage ratios and the treatment of export credits and contingent funding liabilities. Anti-money laundering/know-your-client legislation can also prove challenging, and there is work to be done to provide information and clear channels of communication with regulators in order to prevent knock-on effects – particularly on small- and medium-sized enterprises and high-growth markets.

As the Survey highlights, regulation is only one of several constraints on banks increasing both their cost and caution around entering new relationships. Although cheaper finance is possible, the cost of business is increasing – also likely to hit emerging market and start-up businesses the hardest. A lack of available funding can impede trade for those sectors, although there is no shortage of liquidity in the market overall – only a disconnect between source and opportunity caused by imperfect knowledge. New players can prove their worth by addressing this shortfall; new or alternative financiers may support trade in areas where banks are restricted by risk appetites, regulatory burdens or stakeholder concerns. As such, I welcome new market entrants as complementary additions to existing players, and fresh thinkers in a sector that has always embraced innovation.

The unknown poses the biggest risk to trade, namely geopolitical risks, which further raise barriers to trade and globalization, predominantly for emerging markets and their counterparties. While they are experiencing significant challenges, these markets constitute the greatest opportunities and most significant growth in trade finance. Freedom from cumbersome legacy systems and established infrastructures allows them to innovate and respond faster than developed counterparts, offering potential for those willing to invest.

Trade finance should continue to support and lubricate trade and globalization, helping alleviate geopolitical risk by broadening the stakeholders in society. ICC can play its part by continuing to push for cross-border standardization and facilitation through initiatives such as the ICC Academy, which has created a “common language” for education and understanding of trade finance.

Combined with the ICC Trade Register, the Global Survey helps quantify trade finance as a notably low-risk form of financing. This is abundantly clear to all players. Yet there are risks for trade finance as a discipline – particularly in the reputational damage banks suffered post-crisis. As new Chair of ICC’s Banking Commission, I want to work towards repairing banks’ contract with businesses and society. Like all relationships, it can be healed and strengthened by clear communication and commitment to transparency and honesty. Equally important is the ICC’s role in informing, and working with regulators to help smooth the path for trade. This Survey is illustrative of ICC’s continuing efforts to better inform all sides about global trade and trade finance. Yet it is only one part of the work that will continue in years ahead.

**Daniel Schmand**
Chair, ICC Banking Commission

# SUMMARY REVIEW

With the purpose of identifying the highlights of this report, the following section outlines the key patterns, challenges and opportunities determined in trade and finance.


Introduction ›

Key Findings and Expert Insights ›

# INTRODUCTION

We are pleased to release the ICC's 7th edition of Rethinking Trade & Finance, the annual survey on global trade and finance. Consistent with ICC's mission of promoting open trade and investment and helping business meet the challenges and opportunities of an increasingly integrated world economy, this report provides readers with independent, accurate and in-depth analysis of trends in trade finance. It will thereby enhance the readers' understanding of the trade finance industry and help them discern the causes of trade finance shortage, in order to make informed decisions.

The ICC Global Survey assesses patterns of trade finance in markets worldwide. ICC believes that a multi-stakeholder approach is essential in addressing issues of global impact. Thus, the creation of this ICC Survey, which has its origins in the midst of the financial crisis, involves extensive outreach and dialogue with the financial services community, policymakers and government agencies. Industry actors from around the world pooled their knowledge to develop a valuable global view on current pressing issues in trade finance and beyond. This Survey series is therefore a genuine blueprint for international collaboration in global trade.

This year's edition examines patterns of recent developments in world trade – including structural factors in the global trade slowdown – and explores the insights into global and regional trends in trade finance gathered thanks to the ICC global trade finance questionnaire. The Survey has been expanding year by year in worldwide representation and relevance: 482 respondents across 112 countries contributed to the survey data that the report objectively analyzes to provide high quality foresight.

With ICC's strong focus on extending its reach into emerging markets, this year's highlight section on "Trade Finance in Latin America and the Caribbean" forms an important component of this report. Prepared together with the Inter-American Development Bank (IDB), this section outlines the preponderant trends shaping the current state of trade finance in this region.

We would like to extend our sincerest thanks to the industry leaders who contributed their unique insights on the challenges that may have a critical and defining impact on trade finance over the coming years.

We hope this global survey will serve as a foundation and starting point for an ongoing dialogue on the role of Trade Finance. We invite feedback and comments as we continue to support the trade finance industry with key market intelligence products and look forward to a robust debate.

**David Bischof**
Policy Manager, ICC Banking Commission

# KEY FINDINGS AND EXPERT INSIGHTS

With 482 respondents from 112 countries across the world, the record response rate to this year's 2015 Global Survey on Trade Finance shows that developments and trends in international trade and finance are now centre stage in the minds of stakeholders and policymakers.

In last year's Survey, we pointed towards a slowdown in Asian market led growth, increased geo-political risks and forthcoming structural changes in international trade and finance. These forecasts are now coming to pass and while later than we anticipated, will most likely also impact economic growth and development more significantly than originally anticipated.

In the last quarter of 2013 and as we reported in the 2014 Survey, the tide was turning with a slowdown in China and other emerging markets. In recent years we can see that trade growth has averaged about 3% a year, compared with 6% a year from 1983 to 2008. It will be major challenge to reach the 3% level for 2015 due to unfolding global developments.

It is entirely credible that the recent devaluation of the yuan is predominantly directed towards a market-oriented Chinese currency and inclusion in the IMF's Special Drawing Rights basket. However, when China, the second largest world economy accounts for 15% of Global GDP and 50% of growth and perhaps more acutely, close to 45% of Asian GDP, the fallout in terms of trade impact can be expected to be significant.

The trade-related impact is obvious, for example, the currencies of previously high performing emerging markets of Russia, Colombia, Brazil, Turkey, Mexico and Chile have fallen between 20 and 50% against the US$. The Indonesian rupiah and Malaysian ringgit are at their lowest level since the Asian financial crisis of 1998. Even Australia, one of the 10 largest advanced economies has been impacted with the Australian dollar at its weakest level since April 2009.

### Trade finance demand is still growing: good news amongst the turmoil

Given this slowing pattern of trade growth, is it curious to see that 63.3% of survey respondents reported an overall increase in trade finance activity? It transpires that, given the turbulence in the international trade markets, there is a clear rise in demand for trade finance instruments to cover potential default risk under cross-border commercial contracts.

Increasing demand for trade risk coverage products means increased business and fee income for trade finance banks, but the underlying key message is that there is an increased perception of commercial, bank, and country risks in global trade markets.

At first sight it may appear positive to see that 71.9% of the survey respondents experienced an increase in trade finance net income during 2014. Interestingly, the majority of respondents expect fees and fee income to increase going forward in 2015 and beyond. The ICC Surveys of 2013 and 2014 reported flat trends in relation to fees, so why are increasing fees now being anticipated? It has become clear from the 2015 Survey that with the increased costs of operations, and in particular increased compliance charges, fees charged by trade banks to customers must now be moving into an upward cycle.

### Trade finance demand for factoring and export credit insurance moves forward

It is encouraging to see positive news from both the factoring and export credit insurance sectors. Overall, factoring grew by 6.3% in 2014 to EUR2.34 trillion. Domestic factoring grew marginally at a rate of 1.6% whereas cross-border factoring grew at an impressive 22%, generating over EUR490 billion in cross border factoring business. Export credit insurance also saw positive growth rates with Berne Union members reporting a 4% increase in new cover during 2014 to reach a total amount of US$1.875 trillion. Claims paid out by Berne Union members amounted to US$4.432 billion, which represents an increase from the previous year.

With the lapse in US EXIM Bank's authority, as of July 1, 2015, the US EXIM Bank is unable to take on new trade-facilitating business for US exporters. This is a practical concern going forward when we see that US exports dropped 5.6% to $895.7 billion in the first seven months of 2015.

Without the US EXIM Bank in the market, thousands of US export oriented SMEs will not be able to access export credit insurance or working capital loan guarantees. The withdrawal of these important trade finance tools will hamper US SMEs in their efforts to expand into international markets where risks are on the rise.

### Multilateral development banks continue to keep supply chains open during challenging times

The positive work of the multilateral development banks continues to keep supply chains open in what can be considered high risk emerging markets. At the time of writing this report, collectively the EBRD, IFC, IDB and the ADB have facilitated trade finance transactions in challenging markets to an impressive level of US$70 Billion.

The International Islamic Trade Finance Corporation (ITFC), part of the Islamic Development Bank (IDB), was established in 2008. However, in its short period of operation, the ITFC has achieved more than US$34 Billion of targeted financing.

We have also seen newly formed institutions focused on infrastructure and cross-border cooperation projects. The Asian Infrastructure Investment Bank (AIIB) and the New Silk Road Fund were established in Beijing. The New Development Bank (NDB) and the Contingent Reserve Arrangement (CRA) have been set up in Shanghai. These institutions will no doubt have trade facilitation as part of their strategy for development.

### The ICC Trade Register continues to expand its role with enhanced granular data to facilitate trade

The work initiated in 2009 by the Asian Development Bank at the peak of the global crisis through ICC partners has provided stakeholders and policy makers with focused data on credit-related risks and default data in respect of international trade finance transactions.

The 2015 ICC Trade Register Report covers a total exposure of over US$7.6 trillion. This report makes for interesting reading when considering the risk profile of trade finance banking. For example, data in the register illustrates a customer default rate of 0.72% for loans (import and export) involving bank and corporate risk. Furthermore, the ICC Trade Register Report also provides an obligor view of default rates with export letters of credit coming in with a very low default rate of 0.04% and import letters of credit coming in at 0.29%.

### Commodity Prices Deterioration brings new issues on the trade finance radar

When commodity prices fell after the 2008-2009 financial crisis, we encountered a spike in damaging trade finance issues such as court injunctions, allegations of fraud and an increase in contractual disputes and resultant claims under guarantees and standby letters of credit.

We are again seeing these issues being highlighted by survey respondents.

In this year's survey, 18.5% of respondents reported experiencing an increase in allegations of fraud, 16.1% reported an increase in court injunctions barring payment of bank undertakings. It is also of concern that 23.9% of respondents reported an increase in claims under bank guarantees.

### Trends in SWIFT messaging are consistent with respondents' insights

Overall SWIFT trade traffic volumes showed a decrease of 1.79% in 2014, which was more than double the decrease of 0.65% reported in 2013. The importance of changes in trade patterns in Asia are also underscored by the fact that Asia Pacific continues to register far greater volume of MT 700 traffic (issue of documentary credit), namely 70% import and 76% export.

Perhaps most fascinating of all the trends in SWIFT trade messaging in this report is the rise of the renminbi, which is the second most used currency on the SWIFT platform, accounting for 10.17% of total value in 2014, up 9% from 2013. Of course, the United States Dollar remains the dominant currency for trade messaging being used for 82.51% of the MT 700's (issue of documentary credit).

### SMEs hardest hit by the trade finance gap and compliance challenges

The perception of a shortfall of trade finance globally has become evident and an increase in rejection of trade finance proposals or applications has hit SME applicants.

Overall it was reported that 45.75% of proposed trade finance applications had been submitted by SMEs, 39.63% by large corporates and 14.62% by multinational companies. Many of these trade finance proposals were declined by banks. Of all the declined trade finance proposals, over half of them (53%) were submitted by SMEs. By way of contrast, 79% of large corporates had their trade finance proposals approved.

It is of concern to see that 70% of this year's respondents report declined transactions due to Know Your Customer (KYC)/ Anti-money-laundering (AML) regulations, with 46% of respondents reporting experiencing termination of correspondent relationships due to related costs and complexities. Going forward, it is worrying to observe that 91% of respondents expect compliance requirements to increase over the next year, up from the 81% in 2014.

Furthermore, the International Trade Centre reports that a lack of financing for SMEs impedes their ability to access information, skilled labour and technology, all of which are vital for innovation to create new exporters around the world.

Compliance is now part of the global financial system but difficulties remain due to differing standards being applied: 53% of respondents consider that the lack of compliance harmonization between jurisdictions is a great challenge to the trade finance industry.

### Latin America and the Caribbean (LAC) focus: the trends of the rest of the world are borne out in the Americas

Through research interviews with key regional trade finance professionals, we found that many of the emerging global trends are also evident in LAC. Regulatory issues are challenging, with many senior trade bankers concerned about the possible negative impact on costs and liquidity in the region.

"De-risking and regulatory changes are adversely affecting trade finance flows and financial inclusion, particularly in higher risk emerging economies in Latin America," says Mauri Cavalcanti de Albuquerque, Head of Global Transaction Banking of Santander Brazil, adding that Basel III reforms have "created some unintended consequences in Latin America, where a risk weight of up to 150% may be required on short term loans related to trade finance".

Reported research from the Florida International Bankers Association (FIBA) correlates the 2015 Survey's findings on the cost of regulation. FIBA maintains that the risk weighting rules around Basel III will unfairly penalise trade in LATAM, where a risk weighting of up to 150% on short-term loans related to trade finance may be required, compared with a figure of 20% weighting in some developed markets.

Equally, macroeconomic issues are a deep concern in LAC. The Inter American Development Bank (IDB) revealed that LAC exports fell by 9.1% over the first three months of 2015, with Mercosur exports falling by 41.3% in 2014.

Further concerns regarding the financing of SMEs are also apparent in the region, where 80% of companies are small-sized, but just 15% of trade finance is financing these actors of the market.

### International trade and finance is predominantly short-term business with long-term benefits

We are now at a mission critical point in the evolution of an inclusive world of international trade and finance, which is inherently linked to economic development in both the advanced and poor countries. Without trade finance, there will be no expansion of trade; without trade, there is no need for trade finance.

Recent global events such as the devaluation of the yuan and structural changes in China were not unexpected. The negative consequences have brought the importance of advancing trade and trade finance in this globally connected world into sharp focus. Remember, before the yuan devaluation, the pressure on Asian currencies was already in play and driven by the expectation of a pending upward movement in US interest rates.

No doubt, emerging market nations, including the BRICS - Brazil, Russia, India, China and South Africa – who met at the G20 finance chiefs' meeting in Turkey earlier this month, encouraged a moderate approach to raising US interest rates.

Holding off on raising interest rates is for now the correct approach. Despite the current pressures in international trade markets, the creeping upward trend in protectionist trade barriers must be resisted. Countries must also show unity in resisting competitive currency devaluations and the ongoing positive dialogue, facilitating open secure trade enhancing the world trading system, must be continued.

**Vincent O'Brien**
Member of the Executive Committee,
ICC Banking Commission Chair,
ICC Banking Commission Market
Intelligence Task Force

# THE FULL REPORT

A detailed statistical analysis of the regional and global trends in trade finance followed by a digest of the latest trends in factoring, export insurance, as well as activities of multilateral development banks and export credit agencies in trade finance that charts their growing presence.


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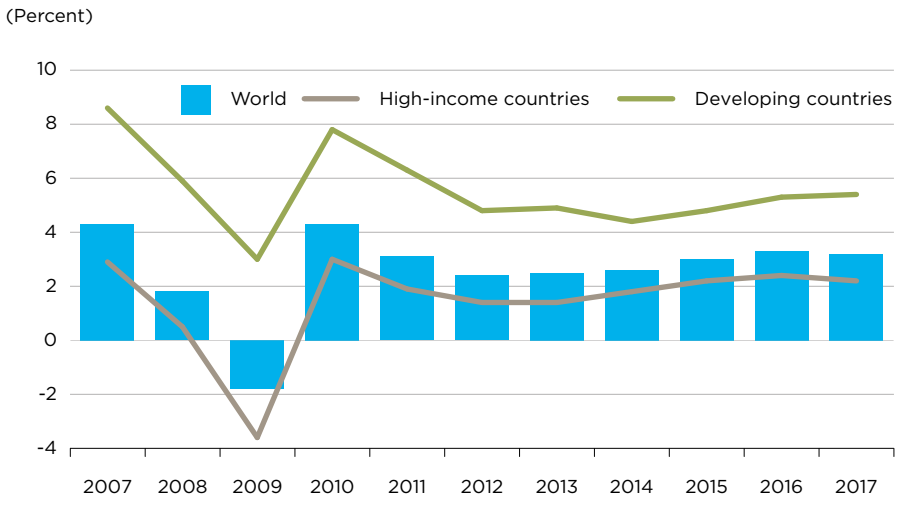
# WORLD ECONOMIC OUTLOOK

### Global Trade Developments and Prospects

The global economy struggled to gain fresh momentum in 2014, as the pattern of low economic growth compared to historical levels continued. Growth picked up only marginally from 2.5% in 2013 to 2.6% in 2014. Concerns have arisen over whether or not the weak recovery in high-income economies and the slowdowns in several large emerging markets signal deeper structural weaknesses. High-income countries are still dealing with the fallout of the global financial crisis. Emerging economies are showing less dynamism than in years past. With such a fragile global outlook, implementing growth-enhancing policies and structural reforms is imperative. There is a window of opportunity for reforms, as well as significant downside risks to inaction. The challenge will be for policymakers to take action while this window remains open.

**Figure 1: GDP Growth, Actual and Projected**




Sources: World Bank and Bloomberg

**Footnote**

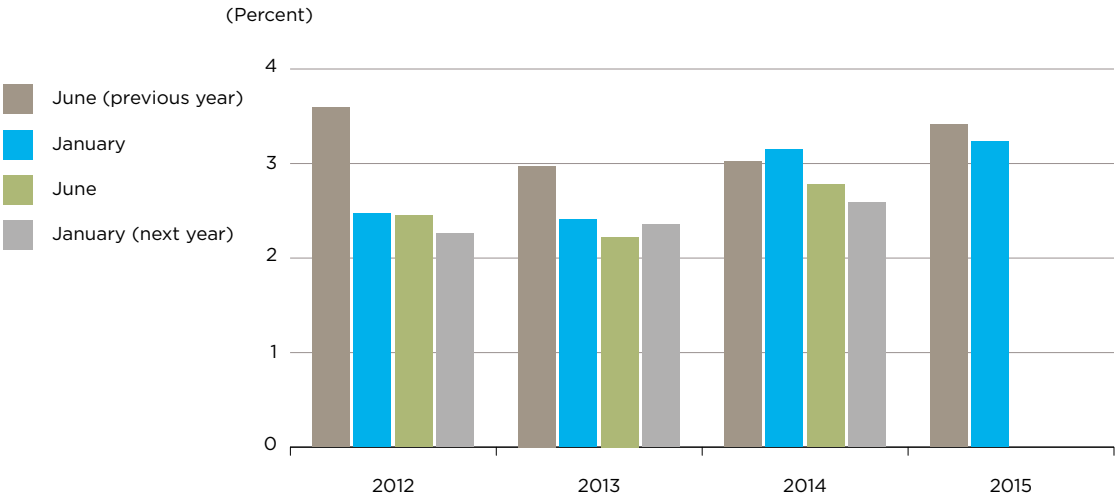
The following data and analysis are current and updated as of June 2015.

## Global Trade Trends

Increasingly divergent trends headlined the performance of developed economies in 2014. In the United States (US) and the United Kingdom (UK), the recovery now appears robust. Stronger labour markets and loose monetary policy helped the two economies gain momentum, with both countries exceeding pre-crisis peaks in 2014. Activity stalled in the US in the first half of 2015, partly due to another cold winter, disruptions in port activity, and cutbacks in capital expenditures in the oil and gas sector. Driven by private consumption and an uptick in household purchasing power due to sharply lower oil prices, growth is expected to pick up again later in the year. In the UK, robust housing markets and expanding credit helped support the recovery. Growth reached 2.8% in 2014 and is expected to continue to be above expectations in 2015. The fall in oil prices, along with strong job creation and rising wages, has helped consumer spending.

The Euro Area and Japan showed stronger signs of recovery in early 2015, despite lagging activity in 2014. Lingering effects of the financial crisis, coupled with serious structural bottlenecks, had hampered their recovery last year. Overall, the Euro Area and Japan accounted for nearly half of all downward revisions to global growth in 2014. Some of the factors that led to these revisions showed signs of abating as the year wore on, and in early 2015, their recovery actually began to pick up steam. Japan is now expected to grow a modest 1.1% in 2015, accelerating to 1.7% in 2016, due in part to a series of new fiscal stimulus measures and declining energy prices. The European Union (EU)'s landmark quantitative easing programme has also done much to improve its outlook. The policy has helped weaken the euro against the dollar and strengthened competitiveness thanks to the dip in oil prices. And while the situation in Greece has had wide-ranging repercussions for its national economy, knock-on effects in the wider Euro Area have thus far been limited. Any further deterioration, however, could affect broader confidence in the European economy.

**Figure 2: Global GDP Growth Forecasts (and Downward Revisions)**




Sources: World Bank and Bloomberg

As of June 2015, the Chinese government has continued to manage its economy's slowdown. Policy measures aimed at containing financial vulnerabilities and unwinding excess capacity in construction, shipping, and renewable energy, especially, have tempered growth. A number of targeted stimulus packages throughout 2014 and early 2015 have helped to partially offset policy tightening. This approach is in line with the objectives of the government's current five-year plan, and a "new normal" of slower but more sustainable growth. Still, excess capacity concerns and weak domestic demand have been considered enough to cool the country's medium-term growth outlook. After growing 7.3% in 2014, growth is expected to fall below 7% by 2016.

Together, these five major economies dominate global activity and international trade. In 2014, they accounted for 63% of global Gross Domestic Product (GDP) and 54% of imports. They also continued to play the most prominent role in financial markets, holding 60% of international banking assets and 72% of global stock market capitalization. Exactly how well these major economies manage to steer the ongoing recovery will continue to shape the outlook for developing countries.

Growth in middle-income countries has also been modest. Forecasts were repeatedly revised downwards in many emerging economies throughout 2014. Productivity growth has slowed due to both cyclical and structural factors. Political tensions and uncertainty set back confidence in Argentina, Brazil, Ghana, South Africa, Thailand, and Venezuela. Similar uncertainties slowed growth in India and Mexico early in the

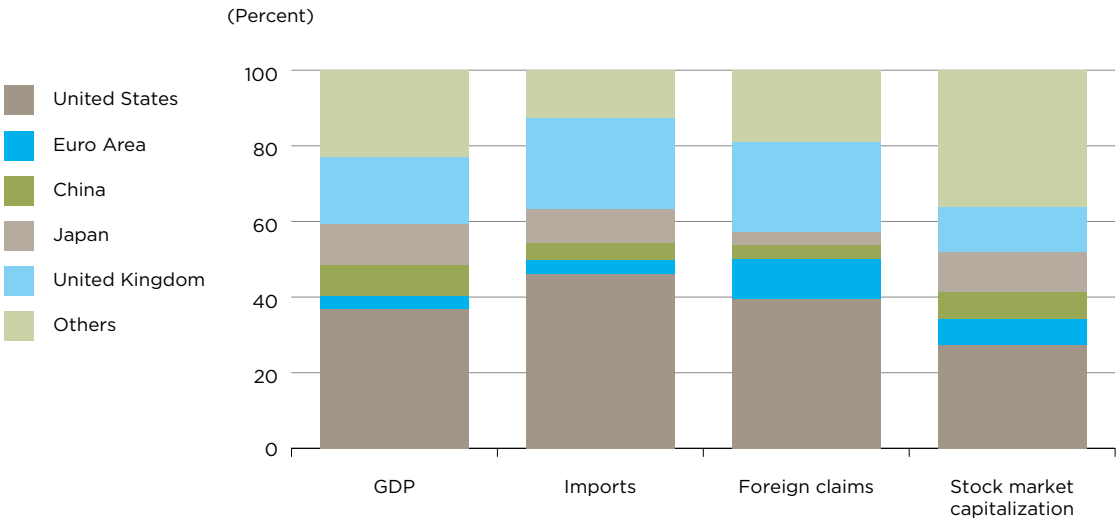
**63%**

**US, UK, Euro Area, Japan and China accounted for 63% of the global GDP in 2014**

**60%**

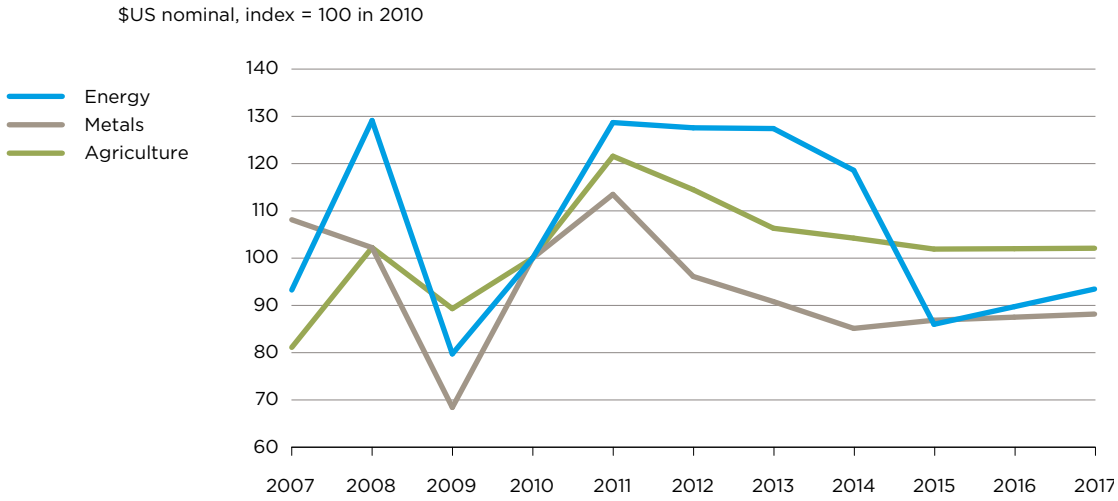
**The same major economies held 60% of international banking assets**

**Figure 3: Major Economies' Importance in the World: Distribution of Global GDP, Trade, and Financial Assets**




Note: Foreign claims refer to claims of Bank for International Settlements (BIS) reporting banks on foreign banks and nonbanks. Stock market capitalization is the market value of all publically traded shares.
Sources: World Bank, BIS, and World Federation of Exchanges (2013).

**Figure 4: Commodity Prices Remain Soft**




Note: Energy consists of oil, natural gas, and coal. Agriculture consists of grains, edible oils, oil seeds, and tropical commodities. Metals include the six base metals (aluminium, copper, lead, nickel, tin, and zinc) and iron ore. Sources: World Bank and Bloomberg.

**6%**

**Average growth of low-income countries in 2014**

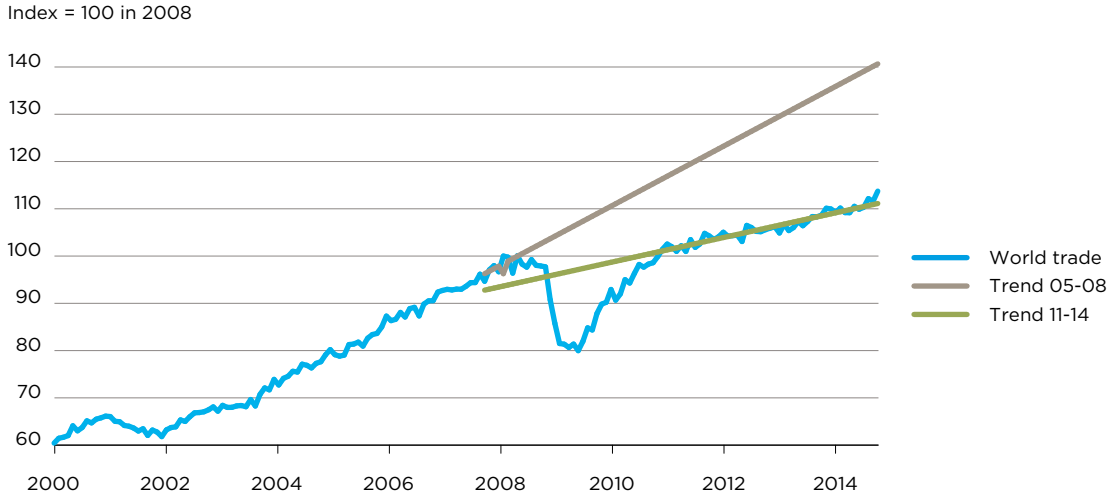
2014, before investment eventually picked back up. Domestic policy tightening in Brazil, Mexico, the Philippines, and Turkey also weighed on activity. Inflation generally slowed, along with credit growth. Fiscal balances widened and debt rose. Employment mostly grew at a sufficient rate to absorb the demographic upswing in working age population and labour force participation, although unemployment remained high and increased for some countries in the Middle East, North Africa, South Asia, and Eastern and Central Europe.

Low-income countries have continued to grow at a robust pace, though the rapid expansion of the pre-crisis years has slowed since 2010. Growth averaged roughly 6% in 2014. Rising public investment and substantial capital inflows helped. In Ethiopia and Rwanda, strong harvests were especially beneficial. Meanwhile, improved security in Myanmar, Central African Republic, and Mali led to stronger activity. Many low-income countries remained heavily reliant on remittances, which helped support consumption growth particularly in South Asia and Sub-Saharan Africa.

Looking forward, several major forces that came into play in 2014 will continue to impact the global economic outlook. Divergent monetary policies across major economies (including persistently low interest rates), softening commodity prices, and weak world trade will remain drivers in performance across countries. The sharp fall in oil prices since mid-2014, in particular, will continue to have far-reaching impacts. These may be positive for global activity, especially in oil-importing developing countries, but it is likely to have significant negative impacts on growth in oil-exporting countries. These may also lead to further regional ramifications.

Unfortunately, significant downside risks to recovery remain. Financial markets remain volatile, spiking again in late 2014. Any sudden deterioration in liquidity conditions could drive up developing countries' borrowing costs. Geopolitical tensions also remain high on a number of fronts, keeping the risk of intensified conflict a serious concern. If commodity markets prove volatile or if a major emerging market shows new signs of financial stress, risk assets will need to be reassessed. Global trade could weaken even further if the Eurozone or Japan slip into prolonged stagnation or even deflation. The broad-based dollar appreciation could slow the US economy more than expected, and if the policy buffers put in place in China fail to maintain stability, the potential implications for the global economy would be considerable.

**Figure 5: Global Trade Volumes**




Note: Blue line: trend during 2005Q1-2008Q1; green line: trend since 2011Q1.
Sources: World Bank, CPB Netherlands Bureau for Economic Policy Analysis - World Trade Monitor.

Yet, despite these risks, global growth is expected to rise moderately to 2.8% in 2015 and strengthen to 3.2% through 2017. Much of this will be driven by developing countries as some of the headwinds holding back growth in 2014 ease and demand picks back up in high-income countries. Growth in developing countries is projected to gradually accelerate from 4.4% in 2014 to 5.3% by 2017. Oil prices could change this outlook, and thus merit particular attention. For their part, high-income countries are expected to see growth of 2% in 2015 and 2.3% over 2016- 2017, a not insignificant bump from 1.8% in 2014. The gradual recovery of labour markets in combination with low financing costs should help.

In terms of external drivers of growth, countries with tighter trade linkages with the US should gain momentum. Those relying more on the Euro Area—mainly Eastern Europe, Northern and Sub-Saharan Africa—will likely face persistent

**2.8% => 3.2%**

**Global growth is expected to rise moderately to 2.8% in 2015 and strengthen to 3.2% through 2017**

headwinds. Metal and coal prices are expected to remain soft, meaning producers like Chile, Columbia, Indonesia, Mongolia, South Africa, and Zambia may struggle to maintain their previous high growth rates. Activity should weaken in oil exporting countries, more broadly, with spillovers to trade partners and recipient countries of remittances. The current recession in Russia, in particular, will dampen growth in Central Asia.

Easing political uncertainty, defused tensions, and the implementation of proposed structural reforms will likely act as domestic drivers of growth in several countries. Uncertainty and tensions are expected to recede in Brazil, Indonesia, South Africa, and Thailand. Meanwhile, reforms are expected to move forward in India, Kenya, Malaysia, Mexico, Nigeria, and Senegal that should help to raise investor confidence and domestic consumption. Capacity constraints are also expected to ease in several Sub-Saharan countries.

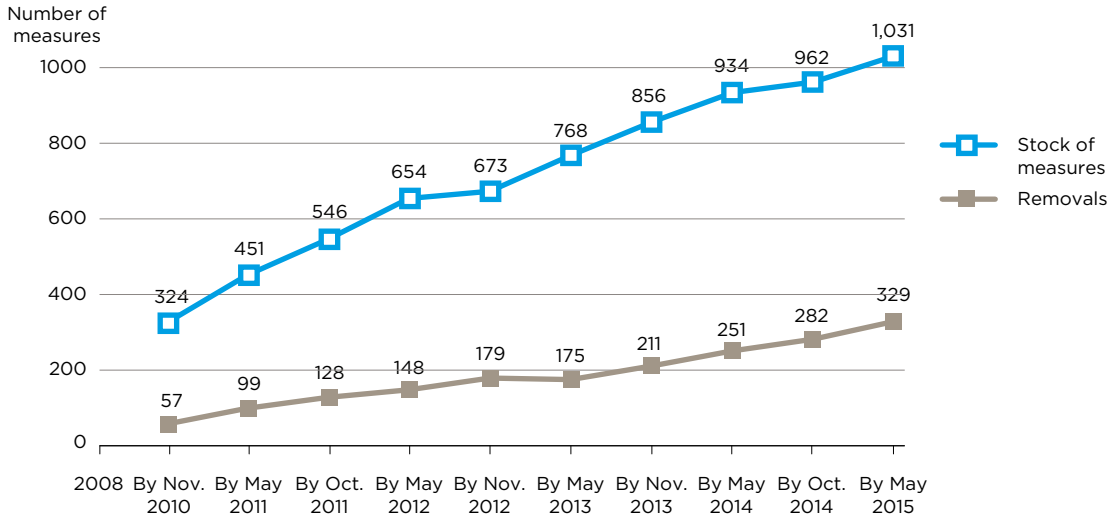
If these expectations are to be met, the forces driving growth and the associated risks involved will require substantive policy responses. Both high-income and developing countries will need to continue to address structural issues, improve institutions, and invest in the necessary modern infrastructure to promote growth and job creation. For high-income countries, a continuation of an accommodative monetary policy will be especially important if the economic recovery is to stand on its legs. This will need to be met with a flexible approach to fiscal policy, one which fosters growth in the near-term but sets in place the concrete medium-term consolidation plans necessary for long-term structural reform.

Developing countries face a different set of challenges, especially in light of global financial tightening. Reduced capital flows could trigger currency depreciation, which, although this may strengthen exports and help current account balances, could weaken balance sheets. Soft commodity prices will also come into play, with depreciation likely to dampen any potential disinflationary effects. To hedge against these risks, central banks will need to balance monetary policies designed to support growth with those needed to stabilize currencies and inflation. Fiscal stimulus may need to be considered if an unexpected sharp cyclical downturn threatens financial stability. However, in all likelihood, the possibility of employing any countercyclical policy tool may be limited by a lack of fiscal capacity.

### Restrictive Trade Measures in G20 Economies

A slight deceleration in the application of new trade-restrictive measures by G20 economies has cut the average number of such measures applied each month to levels not seen since 2013, according to the World Trade Organization. However, with trade growth slowing significantly from the trends of the 1990s and early 2000s and the global economic recovery still very much in the balance, concerns remain over the continued introduction of trade-restrictive measures. The WTO has called for G20 economies to take decisive action to reduce trade restrictions and to show restraint in the imposition of new measures.

**Figure 6: Types of G20-imposed Non-Tariff Measures from 2011-2014**




Note: The monitoring of the accumulation of restrictions and the removals started at end-2010. Information on trade restrictions and distortions in place before October 2008 is not available.
Source: WTO.

Since the onset of the global financial crisis in 2008, the WTO has recorded 1,360 restrictions. Only 329 of these were later removed. The total number was up 7% since the last WTO report. The number of product lines subject to import restrictions has more than doubled since 2007, according to World Bank Group analysis. The pace of continual additions and the low removal rate stands in sharp contradiction to G20 pledges to reduce protectionist measures. However, the WTO believes this number to be low enough to determine that the global reaction to the financial crisis was not as extreme as could have been predicted, an indication that the multilateral trading system has been an effective backstop against protectionism.

Considering current economic conditions, more can be done to drive economic growth and the global recovery through the international trading system. World trade remains weak and growing more slowly than expected. The removal of trade-restrictive measures and the continuation of multilateral trade liberalization can be an effective policy response. In the most recent five-month period for which there are statistics, 119 new trade-restrictive measures were enacted by G20 economies. Trade-remedy measures accounted for more than half of these, followed by other restrictions on imports and exports. These applied to roughly 0.9% of G20 merchandise imports and 0.7% of total global merchandise imports' value, around US$135.1 billion. When considering the total impact of all import-restrictive measures introduced since 2008, that number skyrockets to US$839.5 billion, about 4.6% of the value of world merchandise imports.

**839.5**

**US$Billion**

**The total impact of all import-restrictive measures introduced since 2008, 4.6% of the value of world merchandise imports assets**

**Figure 7: Trade Restrictive Measures**

| Type of measure | Mid-Oct 10 to Apr 11 (6 mths) | May to mid-Oct 11 (6 mths) | Mid-Oct 11 to mid-May 12 (7 mths) | Mid-May to mid-Oct 12 (5 mths) | Mid-Oct 12 to mid-May 13 (7 mths) | Mid-May to mid-Nov 13 (6 mths) | Mid-Nov 13 to mid-May 14 (6 mths) | Mid-May to mid-Oct 14 (5 mths) | Mid-Oct 14 to mid-May 15 (7 months) |
|---|---|---|---|---|---|---|---|---|---|
| Trade remedy | 53 | 44 | 66 | 46 | 67 | 70 | 66 | 54 | 71 |
| Imports | 52 | 36 | 39 | 20 | 29 | 36 | 25 | 25 | 32 |
| Exports | 11 | 19 | 11 | 4 | 7 | 8 | 17 | 9 | 10 |
| Other regions | 6 | 9 | 8 | 1 | 6 | 2 | 4 | 5 | 6 |
| Total | 122 | 108 | 124 | 71 | 109 | 116 | 112 | 93 | 119 |
| Average per month | 20 | 18 | 18 | 14 | 16 | 19 | 19 | 19 | 17 |

Source: WTO

## Definition

**Non-tariff measures (NTMs)** are policy measures other than ordinary custom tariffs that have the potential to affect the international trade in goods.

While these are significant figures, there is further concern that the method of protectionism have shifted towards non-tariff measures (NTMs) in recent years. These behind-the-border measures include policies defining regulation, subsidies, and other distortionary effects. Information to adequately capture their impact is still lacking. There is a strong need to better qualify their operation and quantify their impact. Greater transparency from G20 economies could be a critical starting point, establishing a new paradigm of openness and accounting when it comes to NTMs.

Of course, liberalizing trade policies is another positive step for international trade flows. G20 economies adopted 112 measures aimed at trade facilitation between October 2014 and May 2015. This trend remains stable, averaging 16 measures per month. Not counting trade remedy actions, G20 economies have actually adopted more liberalizing import measures than restrictive measures since the end of 2013. However, it is unclear whether these trends will continue. Considering the slow pace of removal of previous restrictions, the overall stock of restrictive measures has continued to increase. Further liberalization of merchandise and services trade should be combined with a reduction in NTMs and improvements in border management processes. In several low-income countries, restrictions on services trade remain particularly distortionary.

### The Significance of an Environmental Goods Agreement

One area where the international trade community may see significant liberalization in 2015 is in the area of environmental goods. Consumer demand for more environmentally friendly products in markets around the globe has incentivized leaders in politics and in business to rethink production processes along their supply chains. The increasingly fragmented nature of production means that trade policy can play a

critical role in either facilitating or constraining the trade of environmental goods and services. Expectations of significant political progress on a global climate agreement at the 21st Session of the Conference of the Parties to the United Nations Framework Convention on Climate Change (COP21) in Paris in December have breathed life into negotiations for a WTO Environmental Goods Agreement (EGA).

The WTO's Doha Ministerial Declaration instructed Member States to negotiate the reduction and possible elimination of tariff and non-tariff barriers to trade in environmental goods and services back in 2001. It has taken over a decade for this call to shift into formal negotiations, but in July, 2014, a group of 14 WTO Member States began working towards a plurilateral agreement. The negotiations have since expanded, and now include Australia, Canada, China, Chinese Taipei, Costa Rica, the EU, Hong Kong, Iceland, Israel, Japan, the Republic of Korea, New Zealand, Norway, Switzerland, Singapore, the US, and Turkey.

These participants began by building on an initial list of 54 environmental goods identified by the Asia-Pacific Economic Cooperation (APEC) forum in 2012. APEC members had agreed to reduce import tariffs on these goods to 5% or less by the end of 2015. The WTO group has now expanded that list to include roughly 650 tariff lines—more than 2,000 products—based on submissions from each party to the negotiations, though the final number is expected to fall to around 150-200 total products. These fall into 10 categories: air pollution control, solid and hazardous waste management, wastewater management and water treatment, environmental remediation and clean-up, noise and vibration abatement, cleaner renewable energy, energy efficiency, environment monitoring assessment and analysis, resource efficiency, and environmentally preferable goods. The group has been meeting at regular intervals to go through this list line-by-line to determine the credibility of each proposed product with the objective of having a final list and agreement in place by December, in time for the Paris COP21 or the WTO's tenth ministerial conference, also scheduled for that month.

Negotiations have been complex. Concerns over mercantilism in the proposed tariff reductions tabled by each party have been a substantial challenge to overcome. Many tariffs on environmental goods are already low, and failing to eliminate them completely may have only very minor implications for trade. There is also the issue of ensuring the Member States reach the 'critical mass' threshold criteria for a plurilateral agreement to come into effect for all WTO Member States. Generally, this threshold has been when all parties account for 90% of global goods trade for the products under negotiation. This was the case for the critical mass in the Information Technology Agreement. But perhaps most notable is the fact that the negotiations do not currently target reducing barriers to trade in environmental services, a key piece of the puzzle yet to be properly put in place.

**Currently, negotiations to reduce and possibly eliminate tariff and non-tariff barriers to trade in environmental goods do not include environmental services**

# 1 US$Trillion

**Total global trade in environmental goods annually**

Total global trade in environmental goods is estimated at roughly US$1 trillion annually, with an increasingly large percentage of that now coming in the form of South-South trade flows. The global market for low-carbon and energy-efficient technologies is projected to almost double within the next five years. This offers an unprecedented opportunity for developing countries to transition towards cleaner, more sustainable growth, while also boosting competitiveness in the global economy. The fact that the WTO EGA negotiations began with the APEC list as their foundation and the central role of APEC nations in the EGA also strengthens the oft-criticized value proposition of the WTO for developing countries on the world stage moving forward.

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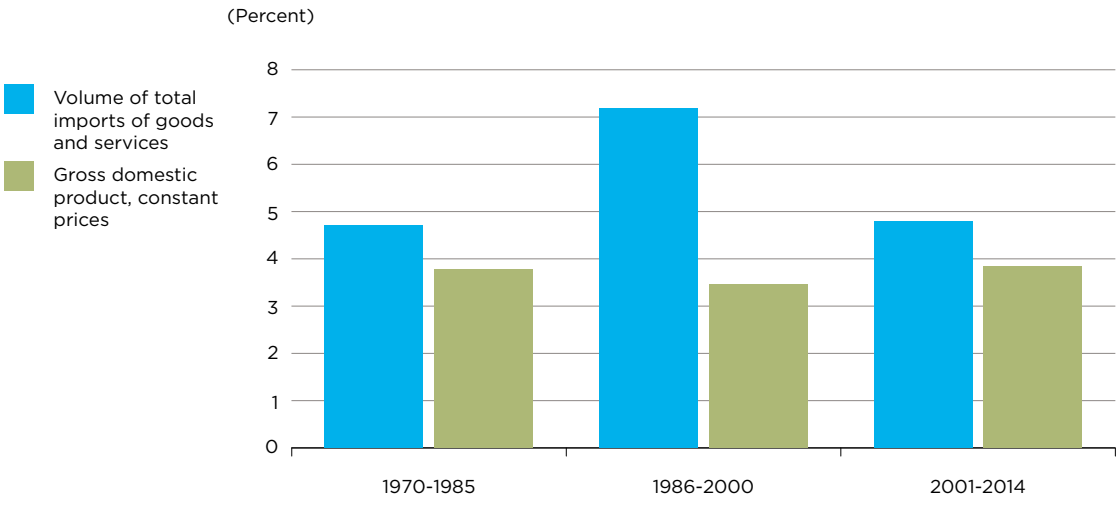
# STRUCTURAL FACTORS IN THE GLOBAL TRADE SLOWDOWN

After an initial rebound, global trade growth has been sluggish since the global financial crisis. Weak economic growth during this period, especially in advanced economies, is widely seen as a key explanatory factor. However, a deeper reason may be the changing long-run relationship between world trade and GDP. The growth rate of world trade volumes was roughly double that of real income growth in the period 1986-2000. This period, dubbed the "long 1990s", appears to have been exceptional compared to the preceding and subsequent periods, when trade volumes grew only slightly faster than real GDP (Figure 8).

To examine the relationship between trade and income in greater detail, Constantinescu, Mattoo and Ruta (2015)[1] (henceforth, CMR) estimate the long-run trade elasticity (the association between trade and GDP). They find that during the long 1990s, a 1% increase in world real GDP was associated with a 2.2% increase in the volume of world trade. This elasticity is substantially higher than in either the preceding period (1970-1985) or subsequent period (2001-2013), when the trade elasticity was 1.3.

**A deeper reason may be the changing long-run relationship between world trade and GDP, aside weak economic growth in advanced economies**

**Figure 8: Average Growth Rates Across Selected Periods**

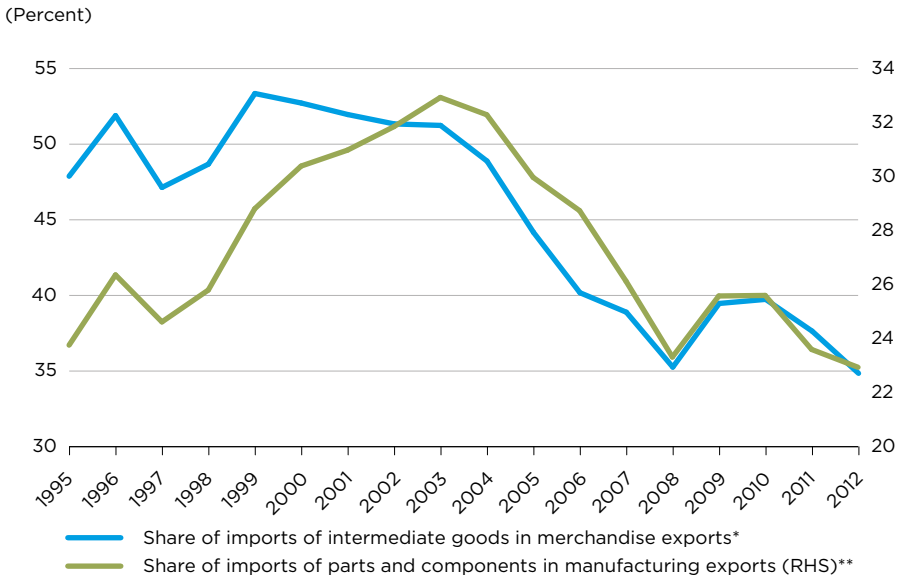



Source: IMF World Economic Outlook

The main force underlying the decline of the world trade elasticity appears to have been the fall of the trade elasticity for manufactured goods in the 2000s. While factors behind the decline in elasticity could range from protectionism to the changing structure of trade or aggregate demand, the evidence analyzed in CMR suggests that at least part of the explanation lies in changes in international vertical specialization. The long-run trade elasticity increased during the long 1990s as production fragmented internationally into global supply chains and decreased in the 2000s as the pace of this process decelerated.

China offers an illustrative example of these changing international production relations. The manufacturing supply chain between China and the group of advanced economies took to a large extent the form of parts and components being imported by the former and then being assembled into final goods which were exported to the latter. The share of imports of parts and components in China's merchandise exports declined from a peak of close to 60% in the mid-1990s to the current share of approximately 35% (Figure 9). The falling share of imports of parts and components reflects the substitution of domestic inputs for foreign inputs by Chinese firms.

**Figure 9: China's Imports of Intermediates and Parts and Components as a Share of Exports, 1995-2012**



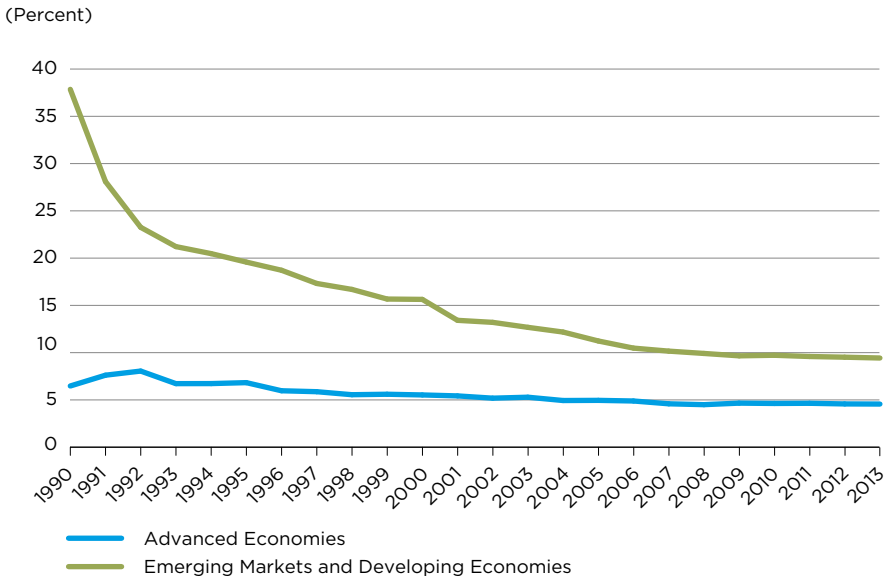

Source: UN Comtrade and WITS
* Intermediate goods linked to global value chains are defined as categories 22, 42 and 53 in UN Comtrade's BEC Classification. **Parts and components are defined as categories 42 and 53 in BEC plus 651 through 657 in SITC Rev. Manufacturing is defined as categories 5 through 8, minus 68 and 891 in SITC3 Rev3.

In order to analyze the impact of global supply chains more systematically, CMR compare the long-run income elasticities of value-added trade and gross trade, both calculated on a seven-year rolling basis due to constraints in value-added data. Results indicate that the gap between the gross and value-added trade elasticities tends to close over time, suggesting the slower pace of expansion of global supply chains is a contributing factor of the trade slowdown.

An additional long-term factor that could have contributed to the global trade slowdown is the deceleration in trade liberalization since late 2000s. Due to reforms implemented by countries in anticipation or as a result of WTO membership, applied tariffs fell in the 1990s and early 2000s from averages of nearly 40% to less than 10% in emerging and developing economies and from 8% to less than 5% in advanced economies (Figure 10). The liberalization led to a significant increase in the ratio of imports to GDP in all countries, with the ratio significantly higher for emerging and developing economies through most of the 1990s and early 2000s (Figure 10). The process of unilateral liberalization slowed down after this period and multilateral negotiations have stalled. New regional trade initiatives are yet to equate the impact of, say, the North American Free Trade Agreement (NAFTA) and the conclusion of the Uruguay Round in 1994, or the reforms in Eastern European countries before joining the EU.

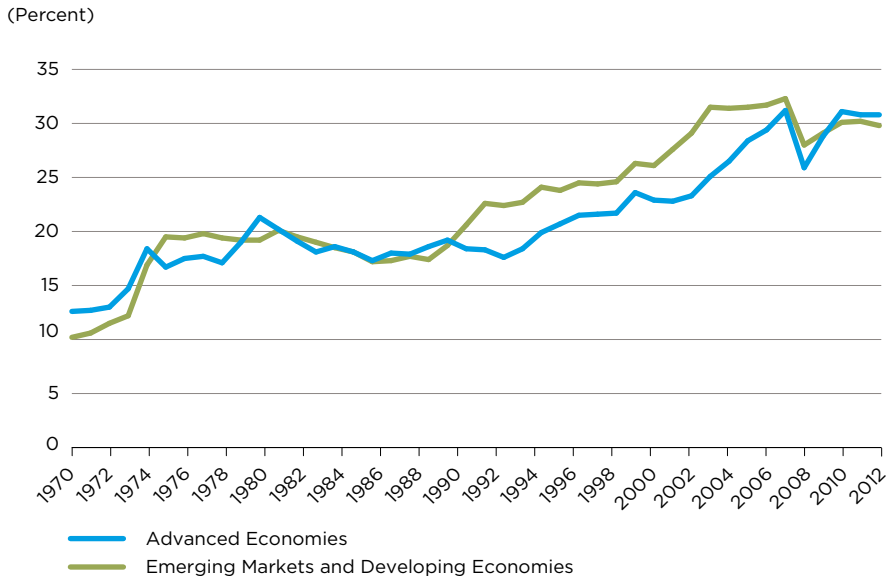
**Deceleration in trade liberalization since late 2000s contributed to the global trade slowdown**

**Figure 10: Average Applied Tariffs*, 1990-2013**




Source: UNCTAD TRAINS.
*Simple averages of MFN Applied and Preferential tariffs.

**Figure 11: Imports of Goods and Services, 1970-2013 (in percent of GDP in US$)**




Source: IMF World Economic Outlook

A trade slowdown triggered by structural (hence, more durable) causes is likely to persist for the coming years. Having said that, there is still scope for increasing international division of labour in Europe and for regions that have been at the margins of global supply chains, such as South Asia, South America, Sub-Saharan Africa, and Middle East and North Africa. In addition, there are potentially important gains to be made from further trade integration in traditional and new areas. These trade liberalization initiatives can move forward at different speeds and depths, but should seek to avoid fragmenting trade and eventually be multilateralized.

## Footnote

1 Constantinescu, Cristina, Aaditya Mattoo and Michele Ruta (2015), 'The Global Trade Slowdown: Cyclical or Structural?' IMF Working Paper, WP/15/6.

# GLOBAL AND REGIONAL TRENDS IN TRADE FINANCE

This ICC Banking Commission 2015 Global Trade Finance Survey comes at a pivotal time in the history of the development of trade finance and the insights from close to 500 banks across the globe will provide guidance and direction to policymakers, business decision makers and the stakeholder in the facilitation of international trade.

Trade finance is the mission critical element for the expansion of trade – without trade finance expansion, trade remains constrained. Constrained trade means constrained economic development and in turn increased instability across all sectors, countries and populations.

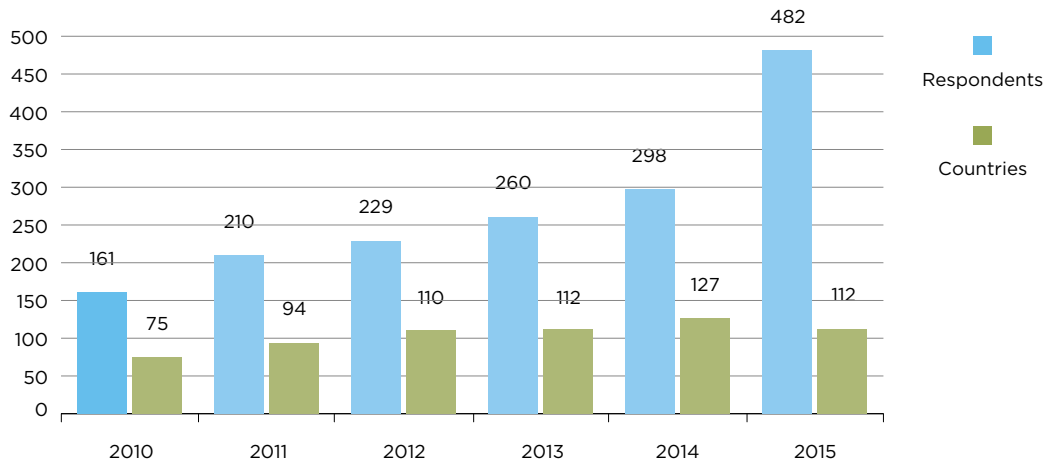
The information gleaned from the previous 2014 Survey highlighted that trade finance gaps in poorer emerging markets, especially affecting SMEs, were expanding faster than anticipated. Consequently, the 2015 survey was expanded to gain more granular data into the elements behind the trade finance gaps. The importance of business analysis and operational challenges for the trade finance market retain their prominence within this 2015 report.

The ICC Global Trade Finance Survey 2015 received 482 responses from 112 countries around the globe. This is a tangible increase in the number of responses from previous years.

**N.B.**

The Asian Development Bank has carried out extensive work in examination of the Analysis of Global Trade Finance Gaps with the key factors having impact on the gaps reported from page 102 in this report.

**Figure 12: ICC Global Survey Population (2010-2015)**



## Global Business and Operational Issues

- 63.3% report an increase in overall trade finance activity
- 61.2 % of banks increased their capacity to satisfy their customers' demand for trade finance
- 71.9% of the survey respondent banks experienced an increase in trade finance fee income
- 30.9% report an increase in standard trade finance fees over the past year
- 26.2% expect standard fees to continue to increase through 2015
- 58.9% reported increased demand for confirmations
- 60.8% expect demand for confirmations to continue
- 53.3% expect cost of confirmations to increase in 2015
- 18.5% report an increase in allegations of fraud
- 65.6% didn't experience an increase in refusal rates in LC documents presented
- 67.8% expect downward trend in refusal rates to continue
- 16.1% saw an increase in incidence of court injunctions
- 23.9 % experienced an increase in claims under guarantees and standbys
- 21.5% reported an increased interest in the BPO
- 40.7% reported an increased interest in supply chain finance
- 34% of respondents adopted the Equator Principles
- 66.1% adopted or will adopt more stringent environmental and social criteria in respect of trade finance transactions

**25%**

**Survey respondents from Asia**

### Geographical Spread of Respondents

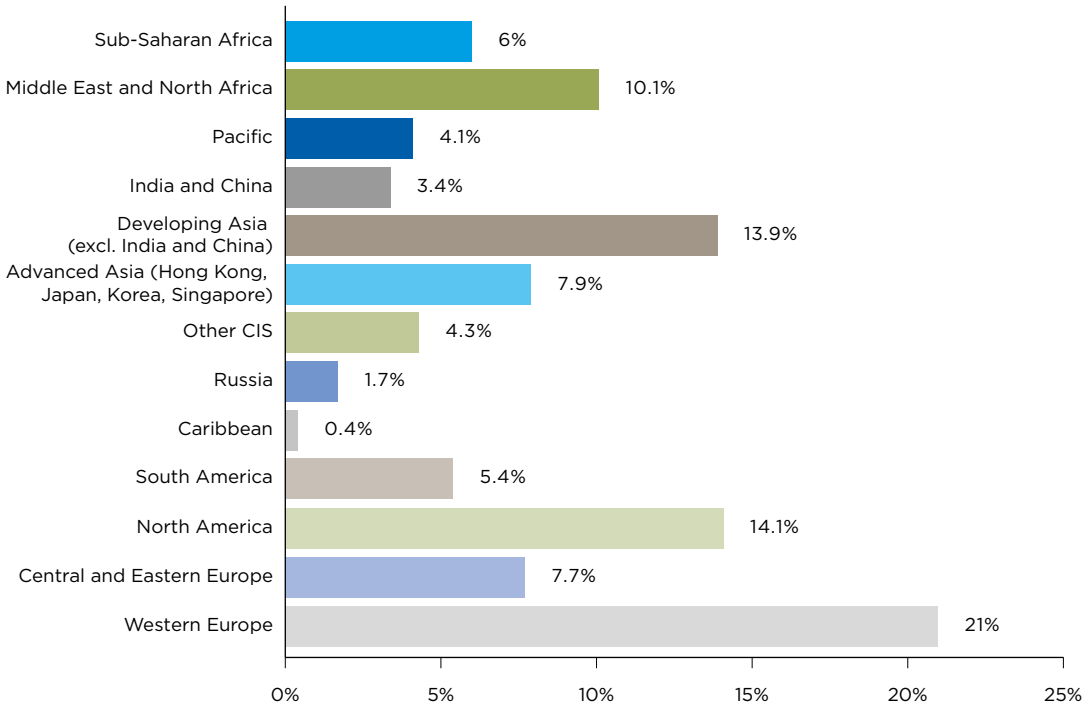
Given the current volatility in global trade and the fact that many global supply chains are anchored in key markets in Asia, the increasing visibility of the Asian markets in the participation in trade finance policy and dialogue is encouraging. Asian markets accounted for more than 25% of survey respondents.

The increased responses from the Middle East and North Africa (MENA region) were also encouraging with 10% of overall responses.

Clearly, the realisation of the importance and need for market-driven data to plan for sound economic development can be seen, now more than ever in the history of ICC Global Trade Finance Surveys.

The broad geographical reach of the survey and increased regional participation enhances the richness of the data collected for use as a resource by stakeholders and policymakers in international trade and finance.

**Figure 13: Respondent Geographical Spread**




### Employee Level of Respondents within Trade Finance Banks

Apart from the increased geographic spread, the 2015 survey reached across banks of all sizes. It was encouraging to see an active participation from smaller regional banks: 44.9% of responses came from smaller banks with less than 50 trade finance employees. At the other end of the spectrum, large international banks with in excess of 50 trade finance-related employees accounted for a shade under 20% of responses.

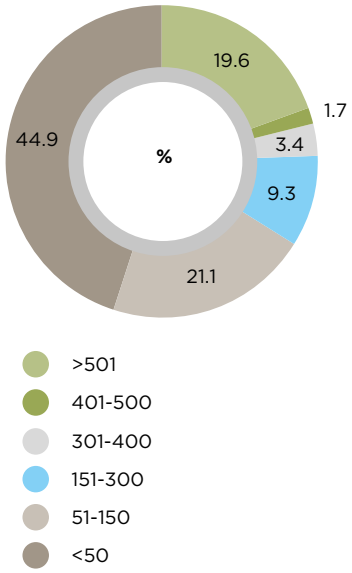
The survey is undertaken in partnership with the major development banks who distribute the survey questionnaire to issuing banks within the MDB's trade programmes. The proactive support of the development banks in actively distributing the survey and encouraging participation greatly enhances the value of the findings for policymakers and stakeholders.

The larger global trade finance banks responded well as has become the norm with 19.6% of respondents coming from banks with more than 500 trade finance-related staff, which naturally would be operating in different countries and regions.

### Regional Market Focus for Trade Finance

As can be anticipated the centre of gravity for trade processing activity continues to have an eastwards orientation, with 39.3% of respondents indicating that their main centres for trade processing were in Asia Pacific, this followed by Europe with 24% and then North America with 9.52%.

**Figure 14: Respondent Staff Numbers in Banks Surveyed**

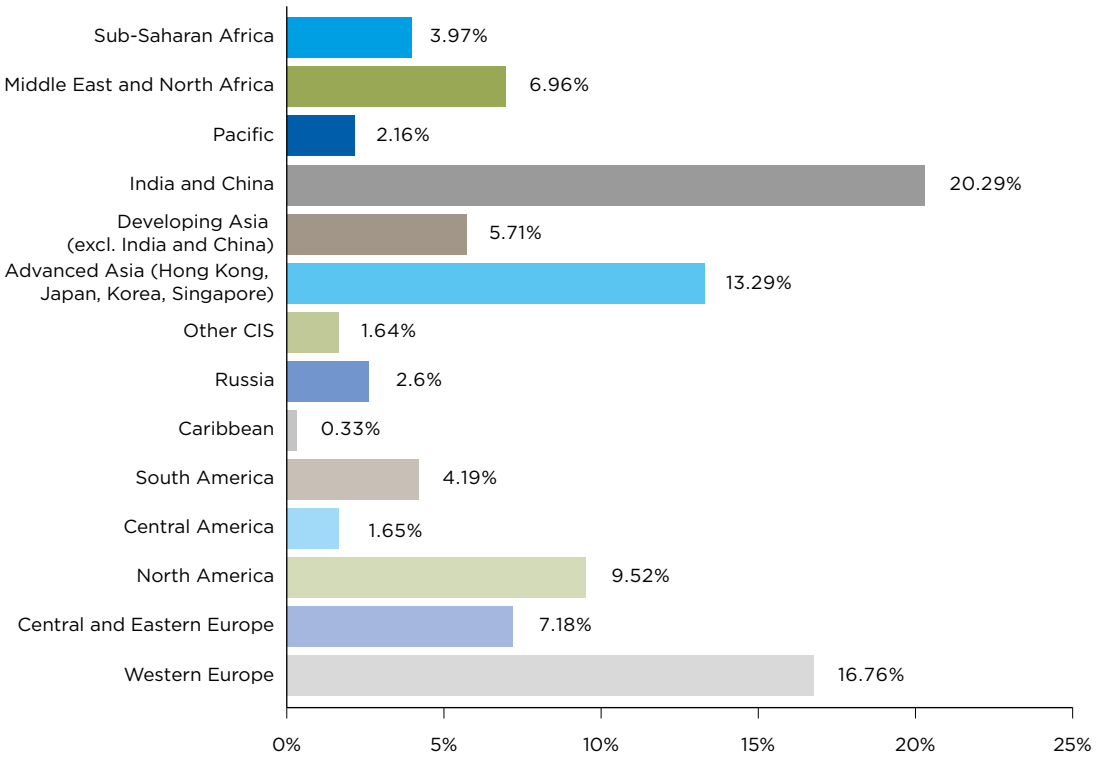


The importance of the Middle East becoming a hub for international and interregional trade and as a gateway to the African markets appears to be supported by the level of responses to the survey which showed that almost 7% of respondents had their main trade finance centre operating in the Middle East.

These trends are corroborated from SWIFT data within this report which shows Asia Pacific accounting for 70% of MT 700 import traffic and 76% of MT 700 traffic for exports. The SWIFT data also reports that while trade finance messaging traffic decreased overall by 1.79%, the Middle East was the single region to register an increase (1.59%) in 2014.

Even with trade growth slowing down in Asia, these markets remain core markets for trade finance in comparison to the advanced economies. It is important to remember that the significant fall in commodity prices and other structural imbalances have bitten hard into the overall value of global trade transaction, but perhaps not so hard into volumes of goods and services traded.

**Figure 15: Regional Trade Focus**



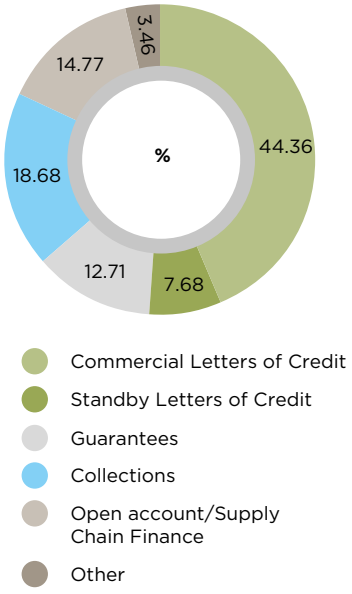
## Export Trade Finance Product Mix

When we examine the overall makeup of the export trade finance product mix handled by respondent banks we see that in the context of export transactions, commercial letters of credit as a proportion of overall trade finance products are now in a slow but steady growth phase as part of the product mix. Commercial letters of credit made up 44.36% in the 2015 survey increasing from 41% in the 2014 survey. Without doubt, recent instability in some the top global trade markets combined with the current perception of increased risk of default for goods and services exported is shaping this development.

With many currencies currently tending toward decline the feature of commercial letter of credits when issued irrevocably fixing the payment and currency amount to be paid, before the goods are actually shipped, (regardless of tenor) is a feature attracting beneficiaries back towards export L/Cs. As can be seen in the reported SWIFT messaging data, letters of credit are predominantly issued in US$. Once issued the amount and currency to be paid is irrevocably fixed for the beneficiary. Should the currency of the importer decline in the interim period before maturity the beneficiary must be paid by the bank in the currency and amount available under the credit as originally issued.

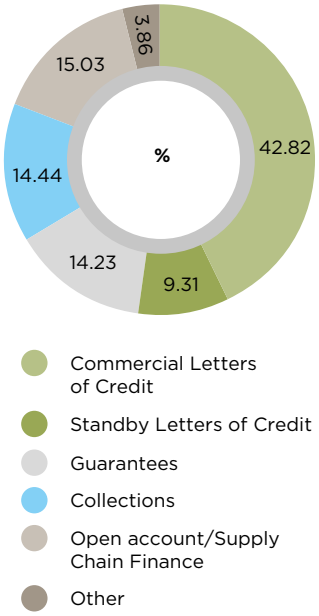
The logic supporting the use of trade instruments to cover the risk of default is also underwritten in the 2015 survey, where it is reported that for export transactions Standby Letters of Credit make up 7.7% of the mix, which is an increase from 5% in the 2014 survey. The figure for guarantees came in at 12.71% of the overall export trade finance product mix.

### Figure 16: Export Trade Product Mix




### Figure 17: Reported Increase or Decrease in Export Trade Product Volumes

**Figure 18: Import Trade Product Mix**




The figure of 14.77% for open account transactions needs to be considered within the particular context: respondents to this survey generally originate from traditional trade finance departments and often open account transactions are handled in different departments of their banks. At the same time, it can be seen that banks are investing in supply chain solutions which focus on this open account business.

However, as you will read in the section of this report on Factoring, we are experiencing significant increases in cross-border factoring which is targeted specifically at this open account and supply chain business. Total cross border factoring between 2009 and end 2014 has experienced an exponential growth rate of 24%. The growth rate in cross border factoring focusing predominantly on this open account pace slowed modestly in 2014 but yet remained at an impressive 22%.

It is interesting to observe that in all export trade risk coverage product areas more respondents are reporting increased volumes of transactions as a proportion of the mix which again is a direct reflection from participants active in the market. Clearly, banks that have exited or are de-risking are experiencing declining volumes and in some extreme situations cessation of trade finance activity or trade product throughput.

### Import Trade Finance Product Mix

On the Import side we are seeing a similar trend evolving in the trade finance product mix usage.

Commercial letters of credit on the import side comprised 42.82% of the import finance product mix, up from 36% in 2014. Standby L/Cs remained constant coming in at 9.31%, just a shade above the figure of 9% in 2014.

**Figure 19: 2014 Reported Increase or Decrease in Import Trade Product Volumes**

An interesting observation from the reported figures is that bank guarantees, as part of the import trade finance product mix fell quite sharply to 14.23%, down from 20% reported in the 2014 Survey.

The key proposition to this reported decline in demand for guarantees as part of the overall product mix is that due to the economic slowdown in some major emerging markets there is related decline in infrastructure and construction and shipbuilding contracts, all sectors which have major impact on the use of bank guarantees and bonds.

Interestingly, consistent with trends on the export side, respondents active in the import side of the market have reported an increase in the demand for traditional trade finance instruments across the board.

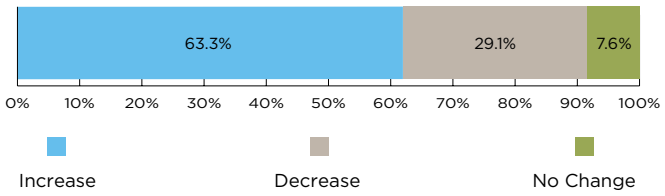
The reported increase in the use of the commercial letter of credit in this 2015 survey may be short-lived, given the progress being made in electronic trade payment platforms, the expansion of factoring, short term export credit insurance and other supply chain products.

However, as has been proven countless times, the demise of the commercial letter of credit is not imminent by any means, as has been proven repeatedly over a period of several decades.

### Overall Trade Finance Activity

In the context of overall trade finance activity the reported figures are, at first glance encouraging: 63.3% of respondents reported an increase in overall trade finance activity, up from 57.59% in the 2014 survey.

**Figure 20: Overall Trade Finance Activity**




The automatic and natural assumption is that this may be driven by increased underlying trade. This may be part of the story, but the primary driver for increased activity in terms of trade risk products is driven by increased risks, or increased perception of risks being faced by trading counterparties. The drop in commodity prices has an immediate negative effect on banks outstanding trade finance obligations when securing such transactions. The currency and amount to be paid will remain as stated in the instrument as issued but the value of the goods, often the primary collateral may have diminished considerably. There is also the creeping consequence of the viability of parties' business models when global commodity prices collapse. Combining this with fast declines experienced

**63.3%**

**Report an increase in overall trade finance activity, compared to 57.59% previously**

## Definition

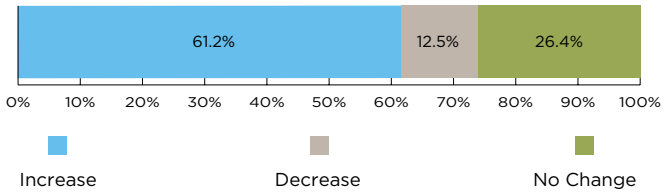
**Bank Payment Obligation (BPO)** is an irrevocable and independent undertaking of an Obligor Bank to pay or incur a deferred payment obligation and pay at maturity a specified amount to a Recipient Bank following Submission of all Data Sets required by an Established Baseline.

in local currency values in commodity-focused business increases the risk of default or at a minimum involves trading parties endeavouring to re-negotiate commercial contracts. In simple terms, when the currency of the importer depreciates and the value of the underlying commodity goods also decline, the importer faces the potential of significant losses as in local currency terms it will be difficult to sell the imported commodity in local markets denominated at a local currency price which will gain enough local sales revenue to meet original pending hard currency obligations.

The calendar year of 2014 brought an increase of these challenges for banks active in trade finance but without doubt these challenges have grown and become more complex at the time writing this report at end third quarter of 2015.

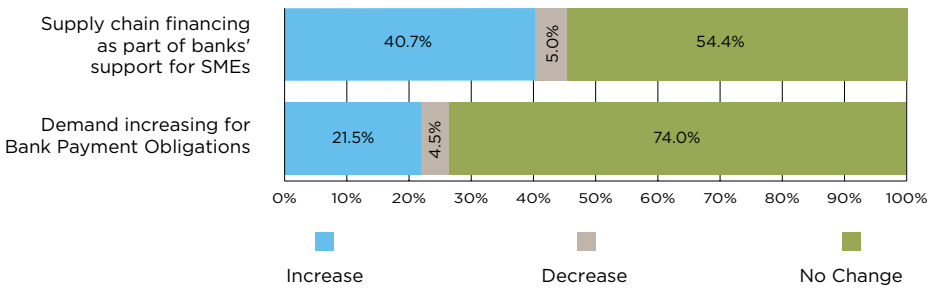
Notwithstanding the challenges, it can be observed that 61.2% of respondents felt that their banks' capacity to satisfy their customers' demand for trade finance increased. This figure is slightly down compared to the figure reported of 62.35 in the 2014 survey.

**Figure 21: Respondent Banks' Capacity to Satisfy Customers Trade Finance Needs**




Interest in innovative trade finance solutions is clearly growing with 40.7% of respondents reporting an increase in interest from their customer base in supply chain finance solutions with 21.5% reporting increased interest in the Bank Payment Obligation (BPO).

**Figure 22: Increased Interest in Innovative Trade Finance Solutions – Supply Chain and BPO**



## Requests for Confirmation

Many commentators on the international trade finance markets have not only observed increases in bank and country risks in various regions of the world and also at global level, but are pointing towards an escalation of such risks going forward.

In terms of demand for confirmations this year's survey appears to support this increased risk proposition with the survey finding that 59.9% of respondents reported increased demand for confirmation of letters of credit.

The facts that demand for confirmations is increasing also supports the contention that customers are actively taking steps to cover bank and country risks and consequently are prepared to pay for the benefits and comfort the confirmation of a letter of credit provides.

It is also important to take on board that this demand is driven by the increased perception of risk by international traders active in the global markets and is not in any way an indicator of underlying increases in cross border international trade activity.

This trend in increased perception of risk is further supported by the fact that 60.8% of respondents expect the demand for confirmation of letters of credit to continue to increase through 2015.

The increase in demand for confirmations of letters of credit is anticipated to go hand in hand with increased pricing in terms of cost of banks adding their confirmation to letters of credit. 53.3% of the respondents to the 2015 survey expect the cost of confirmations to be on an increasing trajectory.

Given recent developments in some large trade-oriented emerging markets, the crash in commodity prices, shrinking trade margins, compounded by currency declines, it is possible that we will see commercial bank lines and indeed multilateral banks credit lines used to facilitate confirmations tested to an extent to which they have not been tested before.

## Trends in Refusal of Documents Under Letters of Credit

The challenging situation concerning documentary compliance reported in earlier surveys appears to be abating in that in this year's survey 65.6% of respondents reported no increase in refusal rates of documents on first presentation.

This is a welcome and positive development as it has often been the case during past challenging times that reported document discrepancy rates increased.

A further positive trend reported in the context of refusal of documents is reflected in the fact that 67.8% of respondents expect this downward trend in refusal rates on documents to continue to decrease through the remainder of 2015.

Some parties contend that this improvement is due to the evolution of the International Standard Banking Practices (ISBP) of the ICC, whereas others contend that the main driver is that export beneficiaries are becoming more professional,

**Figure 23: Demand for Confirmation of L/Cs**

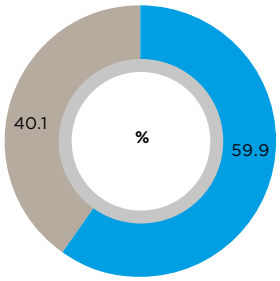



**Figure 24: Expectations of demand for confirmation of L/Cs**

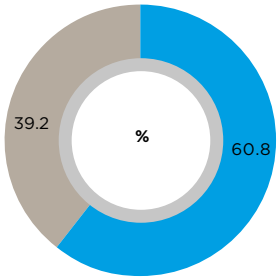



**Figure 25: Expectations of Cost of Confirmation fees for L/Cs**

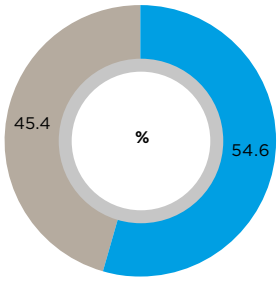



**Figure 26: Trend in Refusal Rates of Documents Under L/Cs**

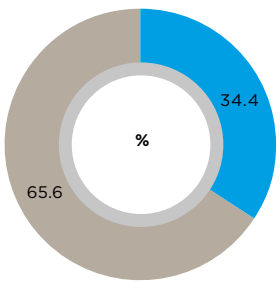
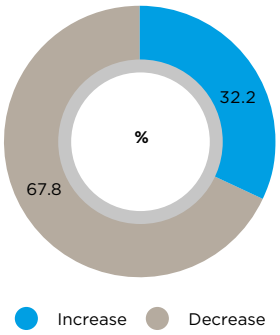


**Figure 27: Expectations on Trends in Refusal of Documents under L/Cs**




striving to avoid risks and making sure they get value for confirmation fees paid to cover international trade finance risks when using commercial letters of credit.

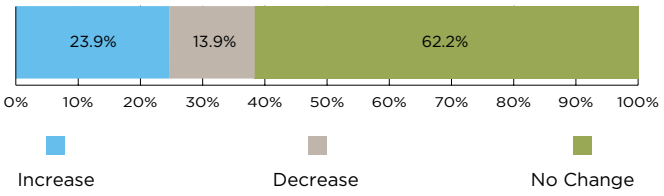
In recent years, corporate exporters understand that risk mitigation fees paid with the intention of irrevocably covering bank and country risks may well be costs incurred without any added value when documents are not presented in compliance under letters of credit.

### Claims Under Guarantees, Court Injunctions and Allegations of Fraud

The reported increase in the use of the mix of traditional trade finance instruments to cover non-payment or default risk appears to be driven by significant events currently unfolding in the international trade and finance markets.

No doubt, the collapse in commodity prices has had an impact, especially where an importer has locked into a contract at a higher commodity price and the value of the goods on receipt or on payment date deteriorates. When the payment instrument was a letter of credit, the undertaking of a bank to pay is irrevocably fixed not only in terms of timing but also in terms currency and value.

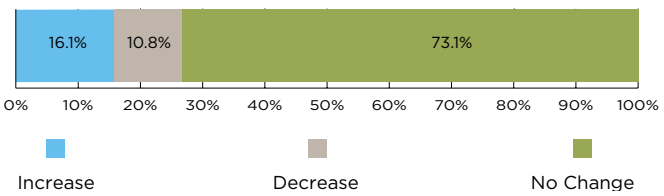
**Figure 28: Trends in Claims Made under Guarantees or Standby L/Cs**




Furthermore, in this year's survey, 23.9% of respondents reported an increase in claims under bank guarantees, (13.9% reported a decrease). Typically claims are made due to a default or non performance in the underlying contract or relationship. Incidents of default or non performance increase in challenging economic time and during downturns in commodity markets and traded goods or service markets.

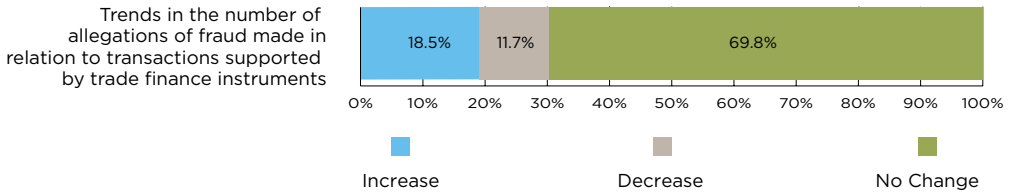
**Figure 29: Trends in Court Injunctions Seeking to Prevent Banks Honouring Bank Undertakings**

Trends in the number of court injunctions seeking to prevent payment under commercial letters of credit, standby letters of credit and guarantees



A further negative trend due to market conditions is reflected in the survey responses, in that 16.1% reported an increase of court injunctions barring payment under bank independent undertakings. Again, as was the case in the early months of 2009 we are seeing an increase in the reported incidence of court injunctions or stay orders temporarily or in some reported incidences permanently stopping payment or reimbursement.

**Figure 30: Trends in Allegations of Fraud in Connection with Trade Finance Instruments**




This conflicted market status is also verified in that 18.5% of respondents reported a worrying increase in allegations of fraud. This trend is troublesome for the international trade finance markets.

### Trends in Trade Finance Income and Trends in Fees

In the 2015 survey we are seeing traditional trade finance products taking a larger share of the trade finance product mix than seen in recent years. We are also seeing increased demand for confirmations and other related products to reduce trade payment related risks. All of these product-related developments have an impact on the fee income generated by banks active within trade finance.

Given the aforementioned, it is not surprising that 71.9% of respondents reported an increase in trade finance fee income for trade finance activity during the calendar year of 2014 compared to 2013.

Trade finance fees are determined to a significant degree on the evaluation of the associated risks in line with an institution's capacity and appetite for that risk. In the 2015 survey 30.9% of respondents reported an increase in their standard fees for traditional trade finance instruments.

With the unfolding of a challenging environment for players active in the trade finance markets it is not surprising that 26.2% of respondents to the 2015 survey expect standard trade finance fees to continue to accelerate through 2015 and beyond.

In reality, these increases in fees will ultimately have to be borne to a large scale by banks' trading customers, many of whom are already challenged due to commodity price collapses, political and economic issues and tighter market conditions for the exchange of goods and services across international borders.

**Figure 31: Net Income from Trade Finance Activities**

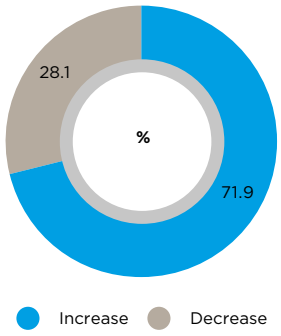



**Figure 32: Increase in Standard Trade Finance Fees Compared to the Previous Year**

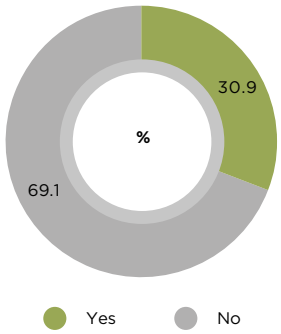


**Figure 33: Expectations of Trade Finance Fees to Increase in 2015**

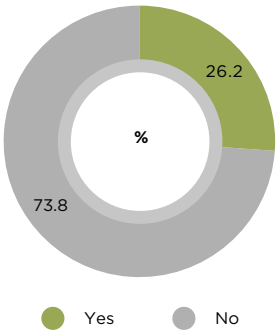



**Figure 34: Sustainability – Is your bank a signatory to the Equator Principles?**

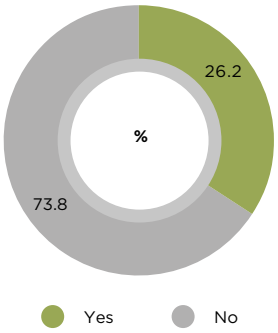
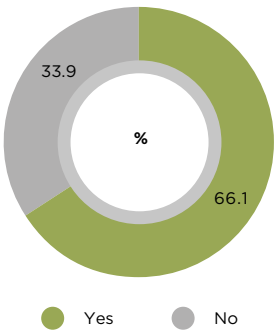



**Figure 35: Sustainability - Environmental and Social Criteria in Respect of Trade Finance Transactions**




In summary, there is widespread expectation for increases in trade finance fees reported by respondents to the ICC 2015 Global Trade Finance Survey. Some of the variables driving this acceleration of costs to banks customers vary across banks and regions but a narrow spectrum of key issues repeatedly surfacing are:

- increasing burdens on banks in terms of risk capital
- the increasing risk profile of many markets based on geo-political and economic variables
- increasing costs of compliance and Know Your Customer unfolding right across the globe.

However, despite the above, in terms of comparison of conventional financing alternatives to finance trade, it is clearly demonstrated from responses to the 2015 survey that respondents consider trade finance activity to be of significantly lower risk than conventional financing such as overdrafts and loans. 25% of respondents considered trade finance instruments supporting trade as involving more than 75% less inherent risk than conventional lending.

In the context of risk management and corporate social responsibility, it was interesting to see that only 34% of respondents reported having adopted the Equator Principles. However, 66.1% of respondents reported that their banks have implemented or are planning to implement more stringent environmental and social criteria in respect of trade finance transactions.

Having examined the Business and Operational Issues responded to in the 2015 ICC Global Trade Finance Survey the responses from respondents to the 2015 survey in respect of Global Trade Finance Gaps are presented and commented further in the report at hand.

## Definition

**The Equator Principles (EPs)** is a risk management framework, adopted by financial institutions, for determining, assessing and managing environmental and social risk in projects and is primarily intended to provide a minimum standard for due diligence to support responsible risk decision-making.

HIGHLIGHT

# ICC TRADE REGISTER: EVOLUTION CONTINUES

The ICC Banking Commission continues the work of seeking to expand the understanding of the credit-related risk profile of the trade finance business. The work initiated in 2009 at the peak of the global crisis, based on the initiative of the Asian Development Bank, remains important to the industry and to the wider audience of stakeholders interested in the financing of international commerce.

The Trade Register covers a clearly identified subset of products and is, thus far, focused on credit-related risk and default data. It remains the objective of the project team to extend the scope of the Trade Register to cover a wider range of products, with specific options to be determined in consultation with participating member banks. Similarly, the Register will extend to cover other categories of risk, as well as other metrics and data elements that will enhance market understanding of the characteristics of trade finance.

The project execution processes have been enhanced materially in the last year, as member bank feedback has clearly acknowledged; a clearer set of product definitions serving as a data dictionary has contributed to a more effective data collection process, and a tighter communication protocol has contributed to a material improvement in data quality. Raw data collected from member banks is put through a filtering and quality process. The 2015 ICC Trade Register Report is underpinned by a larger data set than past versions of the report, for two broad reasons:

- The report covers data from two additional years 2013 and 2014, in both the Short Term and MLT side of the Register
- The raw data set and the post-filtration data pool is larger even when compared on a single-year basis with prior exercises

Process and data issues aside, a major takeaway is that the core findings of the Trade Register have been supported once again by the data and the Basel-aligned approach to analytics. The core conclusions of the Trade Register around the favourable (credit) risk profile of trade finance are again supported by objective data and by a disciplined approach to analysis and advocacy.

The data that informs the 2015 ICC Trade Register Report:

- Is contributed by 23 participating banks
- Covers the majority of global market share in the products covered by the Register
- Includes over 13 million transactions from 2013 and 2014, following a rigorous data filtration and quality assurance process
- Represents a total exposure of over US$7.6 trillion

The 2015 Trade Register reflects numerous findings that provide a view of the risk and default characteristics of trade finance. The customer default rate is relatively low across all products, for example 0.72% for loans (import and export) involving bank and corporate risk.

The 2015 edition of the ICC Trade Register Report provides an obligor view of default rates across in-scope products, further reinforcing the fundamental message about the favourable risk profile of this form of financing.

A transaction level default view is provided as well, again confirming through a different lens, the negligible default rates attributable to common trade finance products.

There are issues of definition and decisions made about how to interpret certain scenarios that arise in the context of trade finance transactions, and the details of these decisions on methodology are well explained in the comprehensive Trade Register Report.

Commercial realities, such as the option for a letter of credit to allow for partial shipment, can have a material impact on the way a 'default' is calculated or reported: the importer

**Figure 36: Obligor Default Rates**

| PRODUCT | TOTAL # OBLIGORS | TOTAL # DEFAULTED OBLIGORS | OBLIGOR DEFAULT RATE | MOODY'S RATING FOR COMPARABLE DEFAULT RATE |
|---|---|---|---|---|
| 1. Export L/C | 92,881 | 36 | 0.04% | Aaa-Aa |
| 2. Import L/C | 113,026 | 333 | 0.29% | Baa |
| 3. Performance Guarantees | 181,626 | 773 | 0.43% | Baa-Ba |
| 4. Loans for Import/Export | 145,021 | 1,050 | 0.72% | Ba |

**Figure 37: Transaction Default Rates**

| PRODUCT | TOTAL # TRANSACTIONS | TOTAL # DEFAULTED TRANSACTIONS | DEFAULT RATE |
|---|---|---|---|
| 1. Export L/C | 1,847,734 | 121 | 0.01% |
| 2. Import L/C | 3,164,200 | 2,509 | 0.08% |
| 3. Performance Guarantees | 1,615,351 | 2,736 | 0.17% |
| 4. Loans for Import/Export | 6,816,742 | 15,176 | 0.22% |

**Figure 38: Estimated Expected Loss for MLT Trade Finance**

| | EXPOSURE-WEIGHTED CUSTOMER DEFAULT RATE | EAD | LGD | EL |
|---|---|---|---|---|
| Observed 2007-2014 | 0.26% | 100% | 5.21% | 0.01% |

may be in default after the first shipment under a large documentary credit, for example, yet the financial impact is far below the value of the L/C, as an exporter might not ship additional product to an insolvent buyer. The impact of discrepancies in documentation, which determine whether a bank must make payment (an L/C is a contingent obligation) can also be material to the way defaults are defined, reported and interpreted.

The quality of the Export Credits covered by ECAs of high-income OECD Countries was also confirmed.

The observed Expected Loss figures appear lower than one would anticipate for "vanilla" corporate lending, due to the benefits of the ECA guarantee. In fact, due to the low Loss Given Default, the annual loss rate from 2007 to 2014 is lower than that reported by Moody's for the same period for Aa rated bonds (which experienced an average annual loss rate between 2007 and 2014 of approximately 0.08%).

In the end, the primary objective of the ICC Trade Register to date has been to enable and underpin a data-based, objective dialogue and advocacy process with regulatory authorities in Basel and at the national level in numerous jurisdictions. There have been notable successes, achieved through the ICC Banking Commission but also on the basis of wider industry and international institution engagement, including important support and progress with the World Trade Organization, among others. The ICC Trade Register has been quoted and referenced as an authoritative source – the only one currently available – by various regulatory bodies, academic entities and others around the world.

A core group of financial institutions continue to contribute time, resources, financial support and proprietary data to the Trade Register Project, and 2015 saw new members initiate discussion about participating in the initiative, and longer-term members getting closer to the ability to access and submit data in the required format. While certain advocacy objectives (such as the removal of the 360-day maturity floor) have been advanced or achieved, it is clear that the data, analytics and advocacy linked to the ICC Trade Register can still add significant value in support of financing international commerce, even while maintaining the current scope and parameters of the project.

The ICC Trade Register will be a useful reference point when the European Union (EU) ultimately completes its calibration exercise of the Net Stable Funding Ratio (NSFR), and the Basel committee finalises the rules for the "Revised Standardised Approach" and the capital floors for the "Internal Ratings-Based" (IRB) approaches.

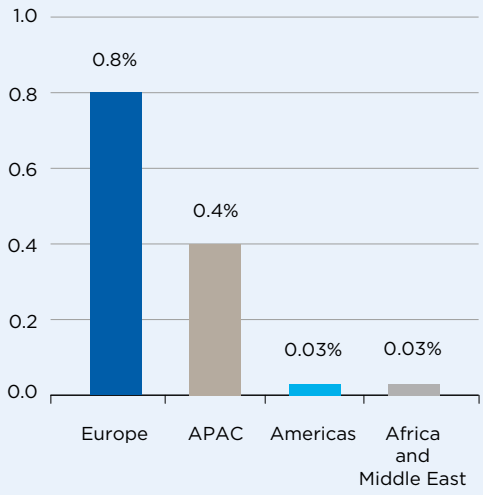
Once we begin to extend product coverage, collect data or effect analysis that provides additional views of the characteristics of the business of financing trade, and/or extend data collection beyond risk-related default and loss data, the value and impact of the Trade Register will increase materially.

The 2015 Trade Register Report takes a step forward in providing a geographic view of default experience, in this edition focusing on presenting a regional perspective. More granular market-level views have been identified as important to trade finance banks for benchmarking and internal risk modeling related dialogue, and as the size and reach of the post-filtration dataset grows, it will be feasible to provide greater visibility on this dimension of the Report.

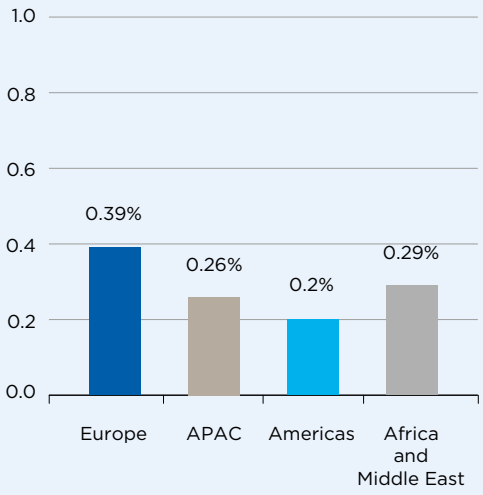
The 2015 edition of the ICC Trade Register Report provides a solid foundation, building upon the work in prior years, to take the Project and the annual Report to the next level in quality, robustness and scope, ensuring that the ICC Banking Commission will continue to be at the centre of advocacy efforts and efforts to bring trade finance increasingly into sharp focus, for the benefit of international commerce and the economic value, growth and prosperity to which it contributes around the world.

**Figure 39: Customer Default Rates Across Regions and Products, 2008–2014**

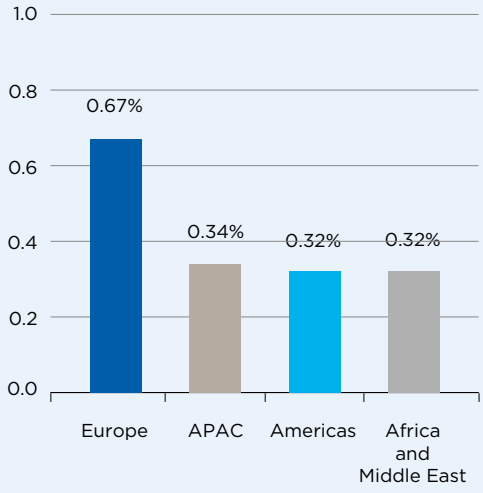
### Export L/Cs



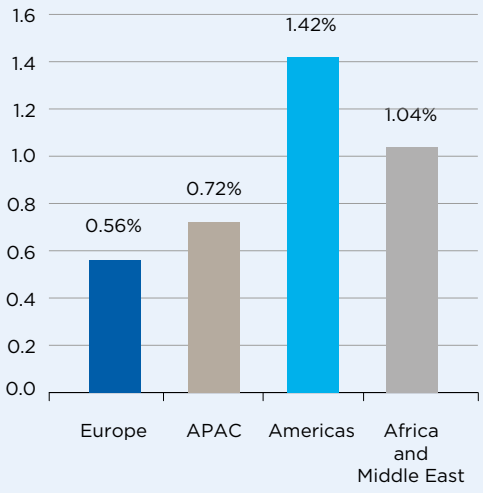

### Import L/Cs




### Performance Guarantees




### Loans




## Find more online

A full version of the Trade Register Report is accessible on the ICC Banking Commission website, and may be downloaded at: www.iccwbo.org/Products-and-Services/Trade-facilitation/ICCTrade-Register

# SWIFT TRADE MESSAGING TRENDS

The following section has been provided exclusively to ICC by SWIFT and provides background information and contemporaneous data on trade finance messaging volumes worldwide.

## Global Trends

Before considering the SWIFT trade volume statistics and related comments, their context should be understood. SWIFT trade traffic is only one part of the overall trade picture, but it can be considered as a good indication of the overall usage trends for the L/C instrument, as around 90% of all L/C transactions go via SWIFT.

"Traffic" refers to live transaction messages sent over the SWIFT network. When global figures are recorded, messages sent are equal to messages received. This report refers to "Category 4" and "Category 7" traffic. Category 4 messages are flows for documentary collections, with the exception of three little used "cash letter" messages. Category 7 messages are flows for commercial and standby letters of credit and guarantees.

### Trade Traffic Falls for a Fourth Year

In 2014, SWIFT trade volume fell by 1.79%, a bigger drop than the 0.65% decline in 2013. This is evident in 3.09% and 1.41% drops in Categories 4 and 7, respectively. It reflects the wider picture of slowing global trade, due in part to low commodity prices and low demand in important industrial and consumer markets.

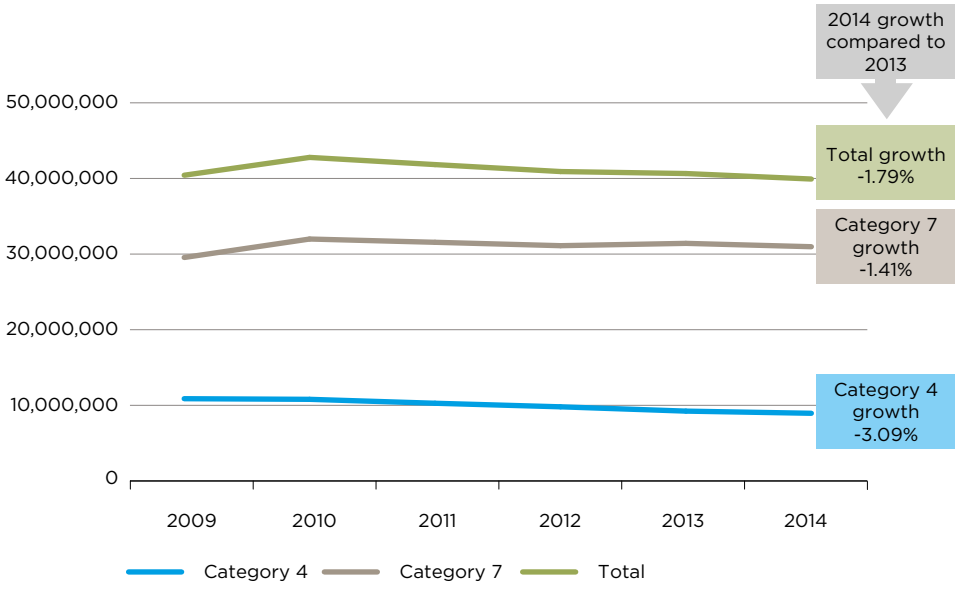
### Regions' Preferences for L/Cs and Collections Through SWIFT

Also striking is the disparity between usage of L/Cs (MT 700) and collections (MT 400) in different regions. L/Cs are used more commonly in Asia-Pacific, with collections more prevalent in Europe and North America. This suggests contrasting risk appetites, with exporters keen to use the more secure L/C option in less developed markets, while those trading within Europe arguably require fewer assurances from their trading partners.

## Key findings

- SWIFT's trade volume for 2014 showed a decrease of 1.79%, higher than the 0.65% drop in 2013. This trend is underlined by the decrease in Category 4 (flows for documentary collections) and Category 7 (flows for letters of credit) of 3.09% and 1.41%, respectively.
- Asia-Pacific continues to register far greater volume of MT 700 (letter of credit or L/C trade) with 70% (import) and 76% (export) of the world traffic in 2014.
- The countries that imported the most using the L/C instrument on SWIFT are: Bangladesh, China, South Korea, India and Hong Kong.
- The countries that exported the most using the L/C instrument on SWIFT are: China, Hong Kong, Bangladesh, India and Japan.
- The region that shows the highest annual decrease in trade is Africa, with a decline of more than 18%.
- The average value of an L/C in 2013 was US$653,000. In 2014, it has decreased by US$10,000 to US$643,000.
- The renminbi is the second most used currency, representing 10.17% of total SWIFT trade volume in 2014, an increase on the 9% reported in 2013.

**Figure 40: SWIFT Trade Traffic Worldwide in Number of Messages, 2009-2014**



### Volume of L/Cs on SWIFT

The volume of MT 700 (issue of a documentary credit) decreased by 2.5% in 2014, but still remains above the recorded volumes in 2011 and 2012. The slump in commodity prices over the past year is likely to have played a part in this. Energy and mineral prices have plummeted, caused falling exports in resource-rich countries such as Australia, Brazil and Indonesia.

Meanwhile Figure 41 shows that the volume of MT 103 has risen each year since 2009. This shows that the use of open account transactions is growing, with many banks pushing more sophisticated trade finance offerings in developing markets. Based on the results of the ICC survey, we expect this trend to continue.

**Figure 41: SWIFT Trade Traffic Worldwide in Volume of MT 103 2009-2014**

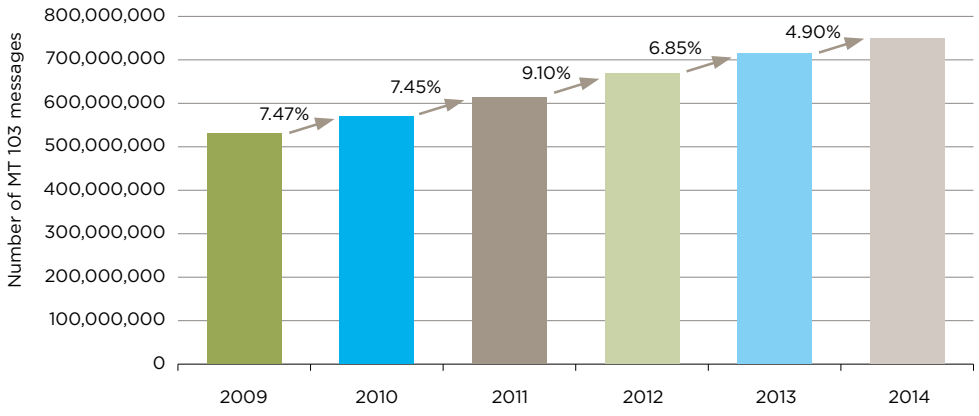



**Figure 42: SWIFT Trade Traffic Worldwide in Volume of MT 700, 2009-2014**

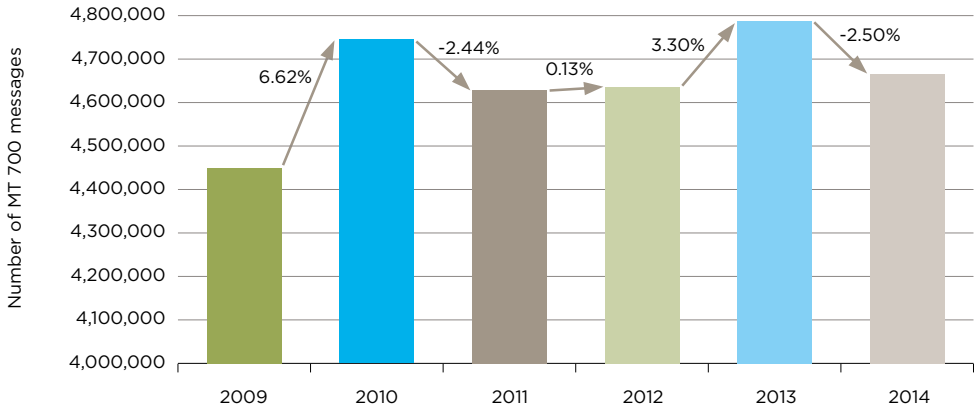


**Figure 43: SWIFT Trade Traffic by Region in Volume of Sent (Import) MT 700, 2009-2014**

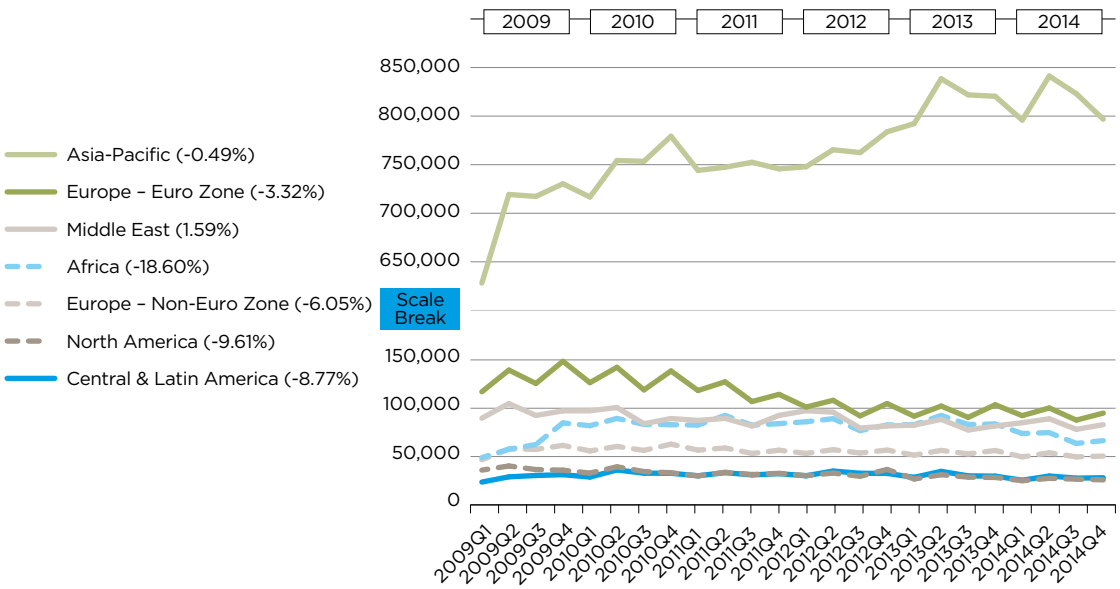
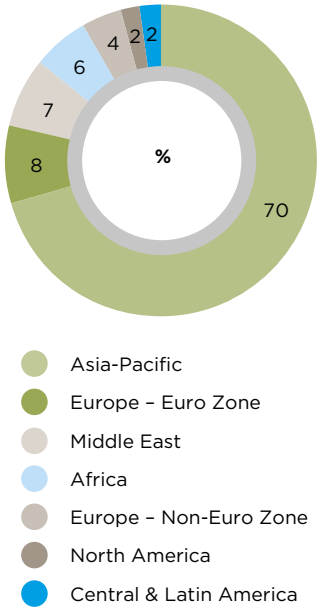



**Figure 44: Import Traffic**




### SWIFT Regional Analysis – Import Using L/C

Asia-Pacific accounted for 70% of SWIFT's global import traffic in 2014. Long considered to be the production line of the world, the data shows that Asian consumption is increasingly important, while intra-regional commodity trade is also a huge driver. Africa showed an 18.6% decrease in imports in 2014. An interesting footnote to this is the fact that South Africa has been running a trade surplus throughout 2015, largely driven by falling energy import costs. Energy importers around the world have experienced similar trends.

### Top Importing Countries

The countries importing most using L/Cs in 2014 were:

- Bangladesh (+5.82% compared to 2013)
- China (-5.77%)
- Korea (+1.6%)
- India (+1.24%)
- Hong Kong (-7.32%)

Bangladesh, with its booming population and thriving textiles sector, is commonly referred to as a "frontier market" by trade financiers. The country's main imports are energy and raw cotton materials. The yearly rise in import volumes of 5.82% occurred when energy prices were lower, suggesting that the country's textiles sector continues to expand, fuelled by raw material imports.

Indeed, along with Bangladesh, Sri Lanka and Vietnam – three of Asia's growing manufacturing hubs – reported the highest annual growth in import traffic in 2014. At the other end of the scale, Japan, Hong Kong, Thailand and China – four of the more advanced Asian economies in relative terms – suffered the biggest declines. In the case of China, it suggests that the government's plan to restructure the economy to a consumption-based model is still a work in progress.

**Figure 45: Highest Growth Between 2013 and 2014 for Countries with >10,000 Sent (Import) MT 700**

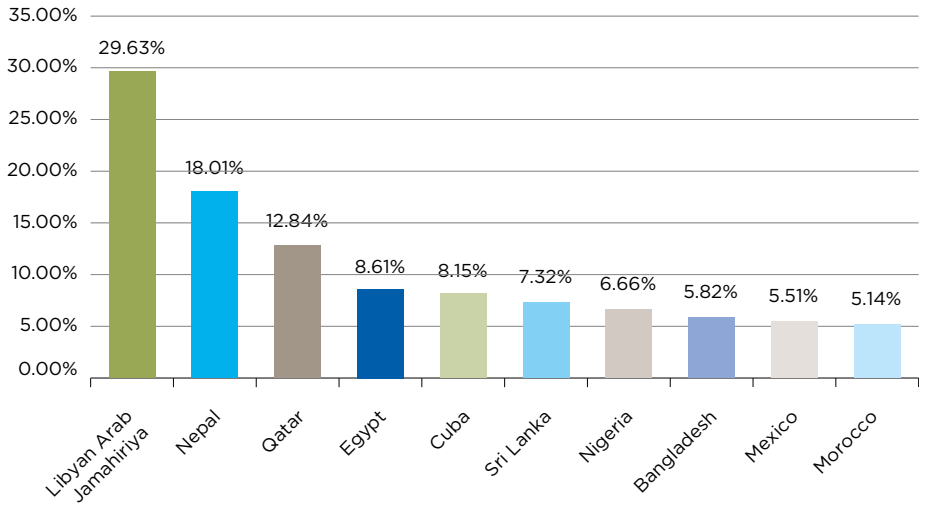



**Figure 46: Highest Decrease Between 2013 and 2014 for Countries with >10,000 Sent (Import) MT 700**

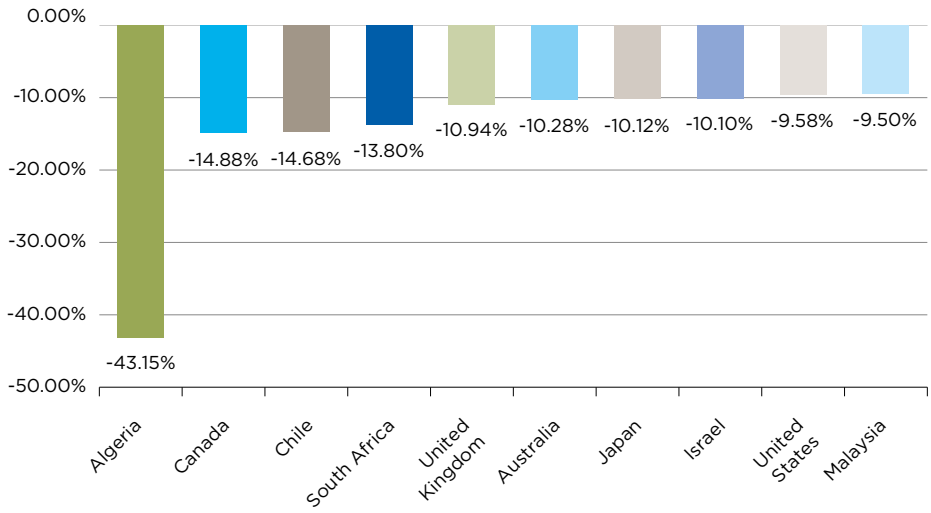


**Figure 47: SWIFT Trade Traffic by Region in Volume of Received (Export) MT 700, 2009-2014**

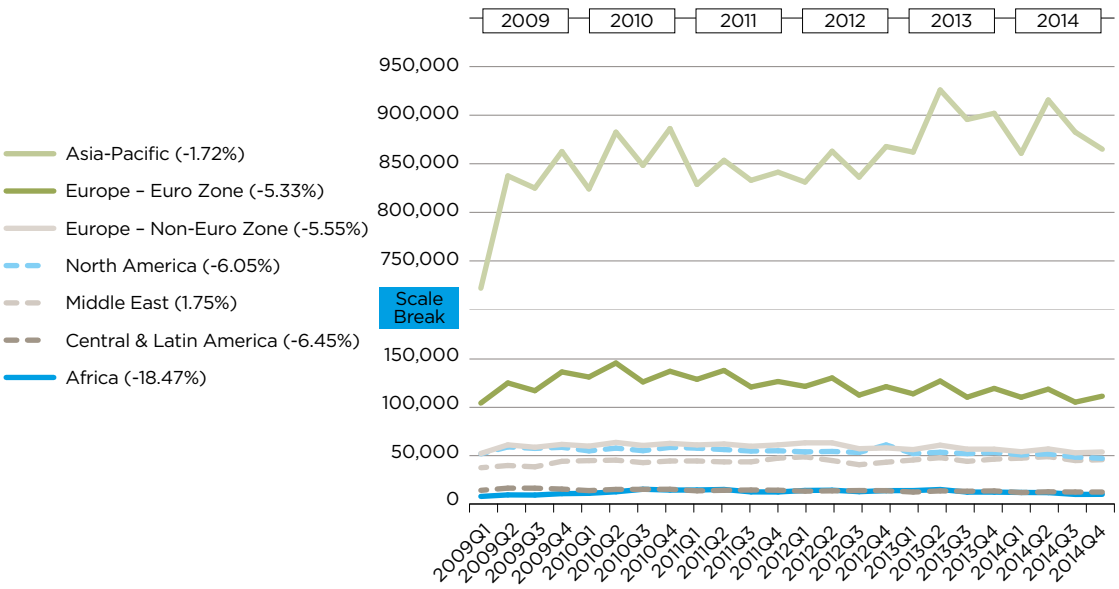
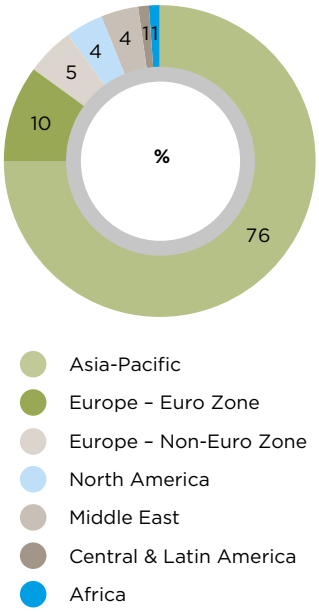



**Figure 48: Export Traffic**




From countries with a yearly volume higher than 10,000 import trade messages sent, Libya reported by far the biggest growth in 2014, but given the economic destruction of the civil war, this is coming from a very low base.

Of the countries with a yearly volume higher than 10,000 import messages sent, Algeria showed the biggest decline in 2014. Official government data shows that Algeria's imports bill has continued to fall into 2015, with huge reductions in the amount paid for building materials and pharmaceuticals.

### SWIFT Regional Analysis – Export Using L/C

Asia-Pacific also registers far greater export messaging volumes than anywhere else in the world, with 76% of the global total in 2014, ahead of Europe – Eurozone (10%) and Europe – non-Eurozone (5%). Despite this, only the Middle East showed an annual increase in 2014, of 1.75%. This runs counter to the general trend of commodity rich nations and regions experiencing exports decline. GCC nations in particular have far lower breakeven margins on oil exports than other countries, such as Russia. Their capacity to weather the price slump is therefore greater.

### Top Exporting Countries

Breaking it down on a country-by-country basis, those that exported the most using the L/C in 2014 were:

- China (-1.26% compared to 2013)
- Hong Kong (-7.38%)
- Bangladesh (+1.87%)
- India (+1.11%)
- Japan (-0.82%)

Those with the highest export traffic growth in 2014 were Germany (+6%), Indonesia (+4%), Bangladesh (+2%) and United Arab Emirates (+2%). The presence of Germany may surprise some, given the concerns over its exposure to sanctioned Russia, to which it sold high volumes of engineering equipment and machinery. Germany's Eurozone peer Italy is the country with the highest decrease in export volumes in 2014 (8%). This is arguably down to Italy's failure to diversify its exports markets as well as Germany. China now accounts for 6.6% of Germany's total exports, while taking only 2.2% of Italy's.

**Figure 49: Highest Growth Between 2013 and 2014 for Countries with >10,000 Received (Export) MT 700**

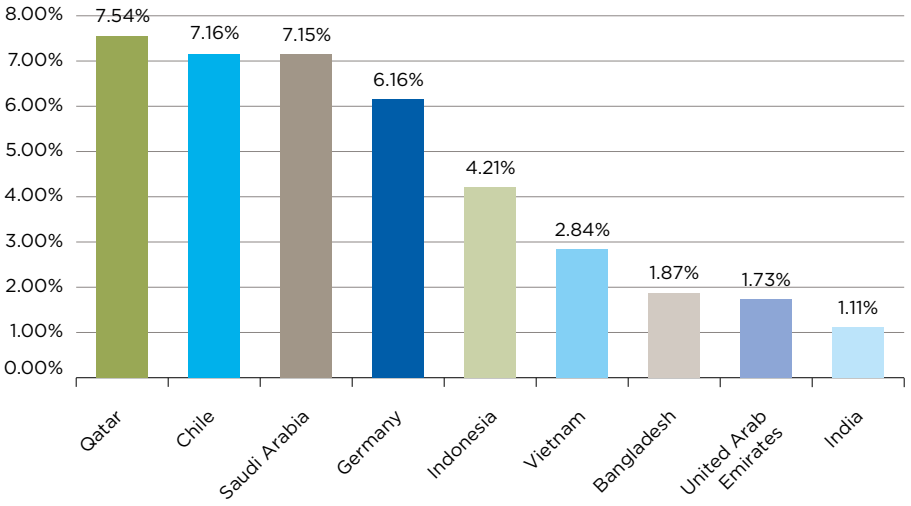



**Figure 50: Highest Decrease Between 2013 and 2014 for Countries with >10,000 Received (Export) MT 700**

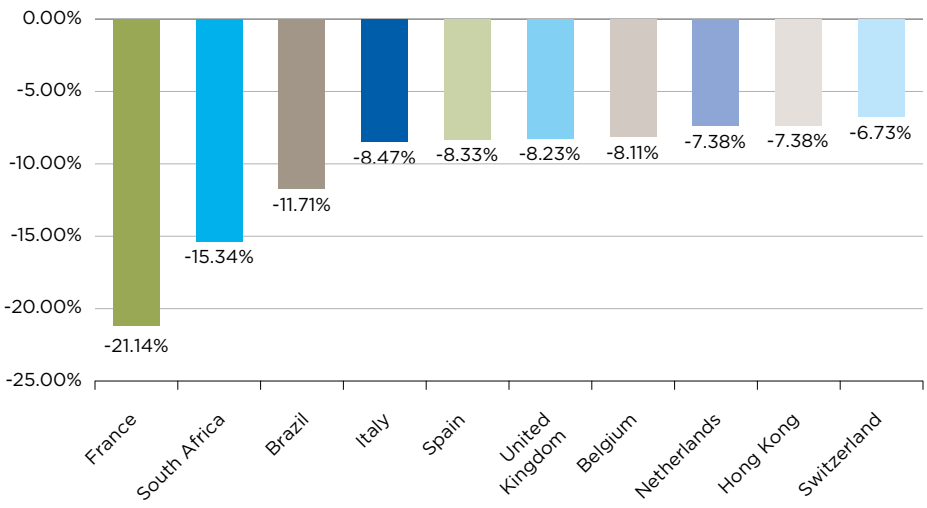


**Figure 51: Volume of L/Cs in CNY, 2011-2014**

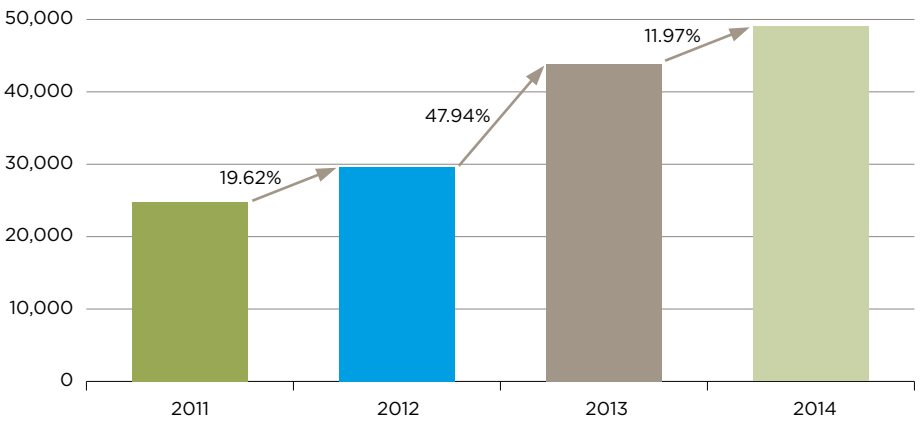
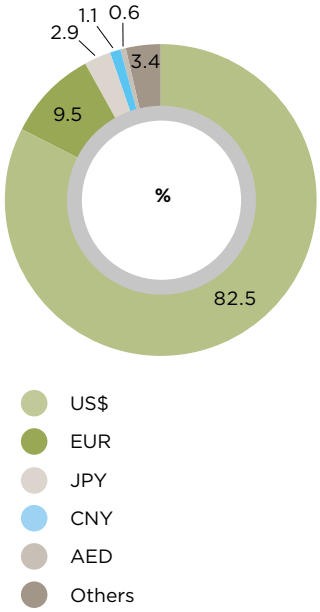



**Figure 52: Volume of L/C (MT700) by Currency, 2014**




From countries receiving with a more than 10,000 export messages per year, Figure 49 shows the countries with the highest growth in 2014 compared to 2013.

Meanwhile, those higher volume countries experiencing the biggest exports decline are led by France. The presence of Italy, Spain, the UK, Belgium and the Netherlands in the top 10 suggests that concerns over EU trade are well-grounded.

### Average value of an L/C

The average value of an L/C (MT 700 only, amount converted to US$) fell by US$10,000 in 2014. This could be, once again, partially attributed to the decline in the price of many imports, mainly commodities, while the role of the strengthening US dollar must also not be discounted.

Meanwhile, in currency stakes, the dollar continues its global primacy, being used in 82.51% of MT 700.

Most striking, perhaps, is the continued rise of the renminbi (CNY or RMB), which is now the second most used currency, at 10.17%, up by 9% year-on-year. The Chinese government has been actively pursuing an internationalization programme for the RMB, while foreign companies are often offered discounts for settling in RMB by their local counterparts.

**Figure 53: Amount of L/Cs in CNY, Converted to US$, 2011-2014**

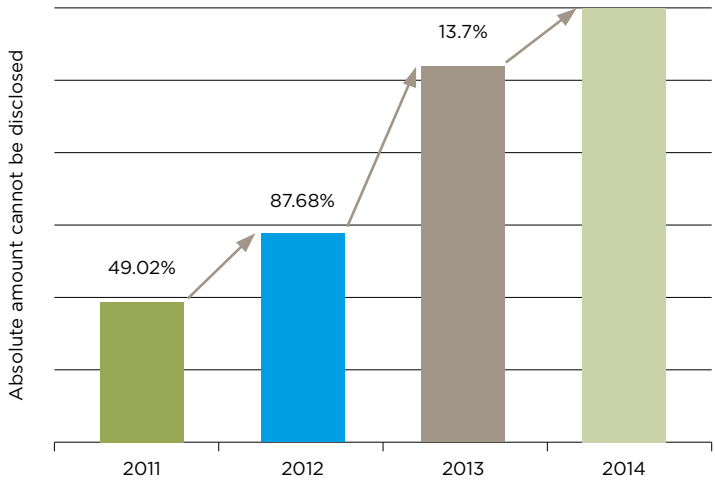
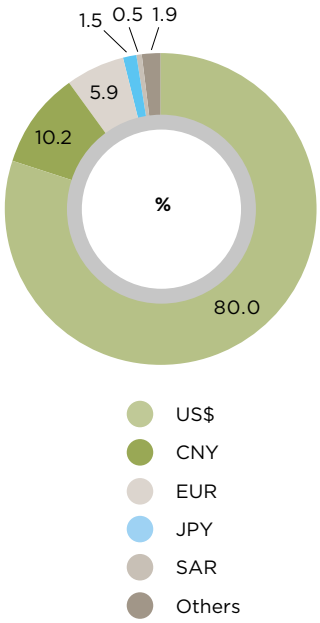



**Figure 54: Amount of L/ Cs by Currency Converted to US$, 2014**




### Asia-Pacific Tops the Chart in Import L/Cs

By far the highest number of L/Cs are issued in Asia-Pacific. Most of this traffic is intra-regional, suggesting once again a desire to mitigate risk in trade. The average value of an import L/C in Asia-Pacific is well below average, which also suggests exporters erring on the side of security.highest (US$ 605,479 for imports).

**Figure 55: SWIFT Trade Traffic in Volume and Average Values of L/Cs Sent (Import) by Regions, 2014**

**Volume of L/Cs Sent by Regions, 2014**

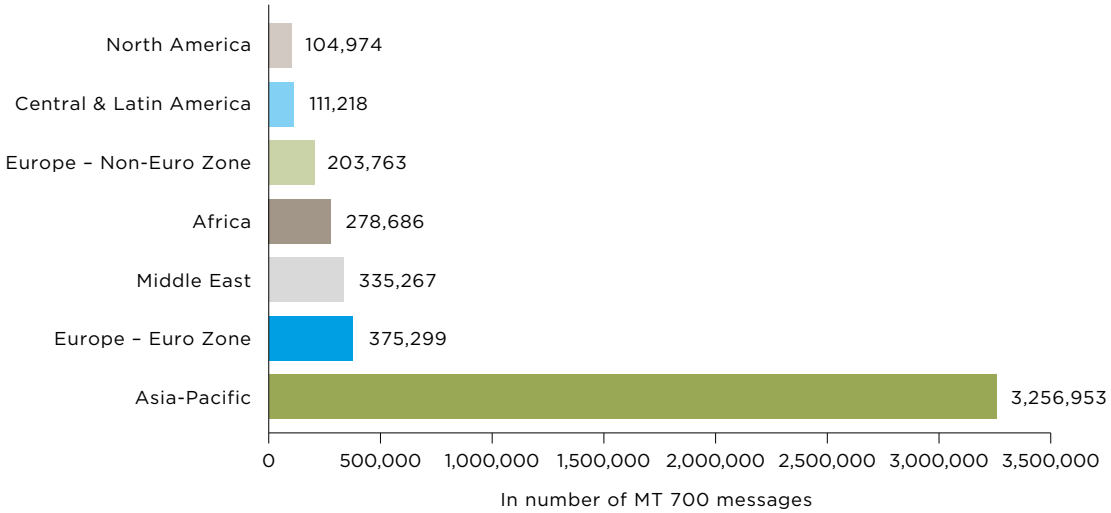
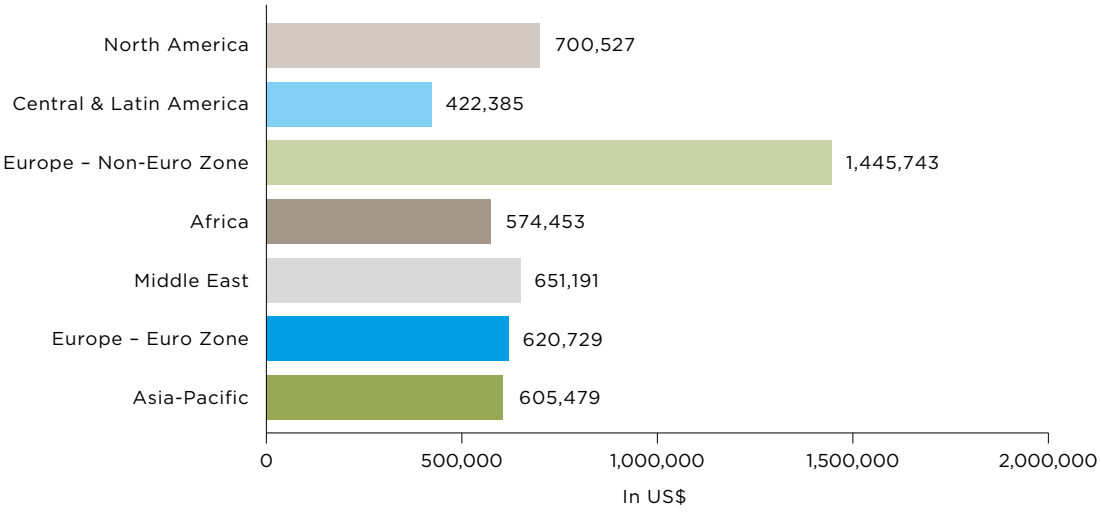


**Figure 56: Average Value of L/Cs Sent by Regions, 2014**




**Asia-Pacific Leads L/C for Exports**

Asia-Pacific receives the highest number of L/Cs by some distance, most of which are for intra-regional trade. The average L/C value is also lower in the region than elsewhere (US$509,312 for exports), suggesting that exporters are keen to limit their exposure in higher-risk markets, even when the deal value is lower.

**Figure 57: SWIFT Trade Traffic in Volume and Average Values of L/Cs Received (Export) by Regions, 2014**

**Volume of L/Cs Received by Region, 2014**

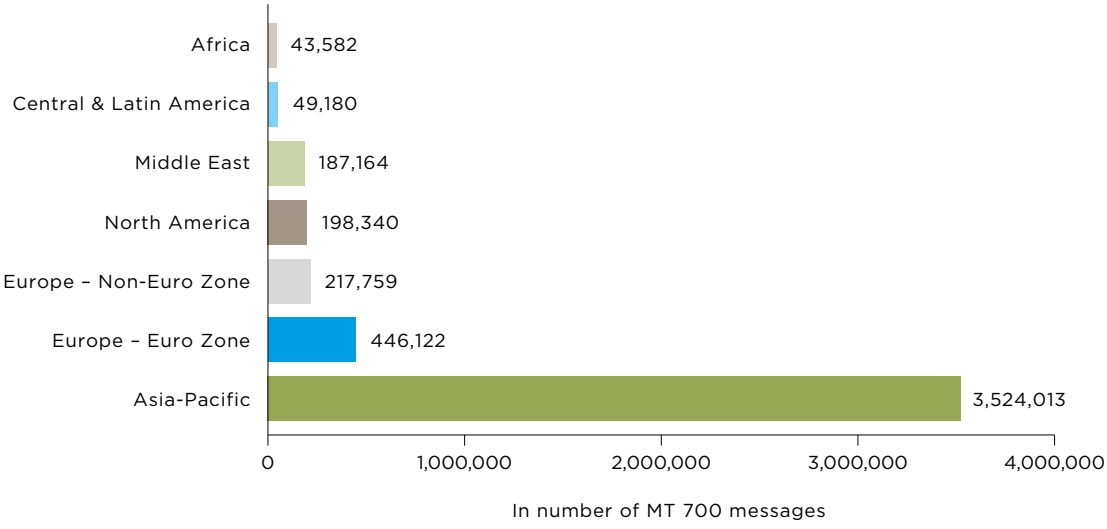
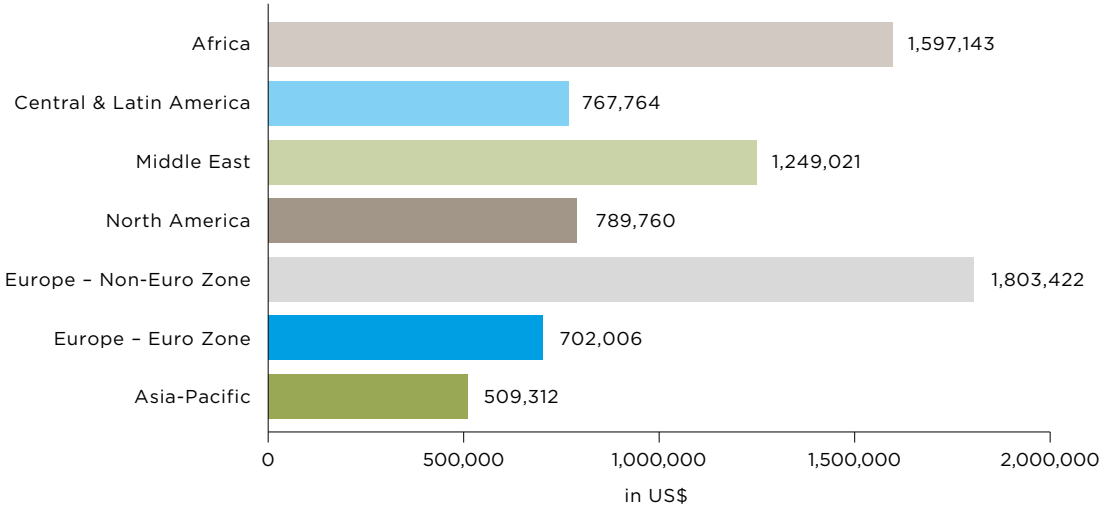


**Figure 58: Average Value of L/Cs Received by Region, 2014**




### 10% of L/Cs are Confirmed

The share of L/Cs confirmed fell by 0.4% in 2014 compared to 2013. Africa received the highest number of confirmations, largely due to the higher perceived trading risk there. Asia-Pacific had a lower level of confirmations, due to differing market practices: firms are keen to cut costs, but it may also suggest mature trading relationships.

**Figure 59: Percent Distribution of L/C Received by Confirmation per Region, 2014**

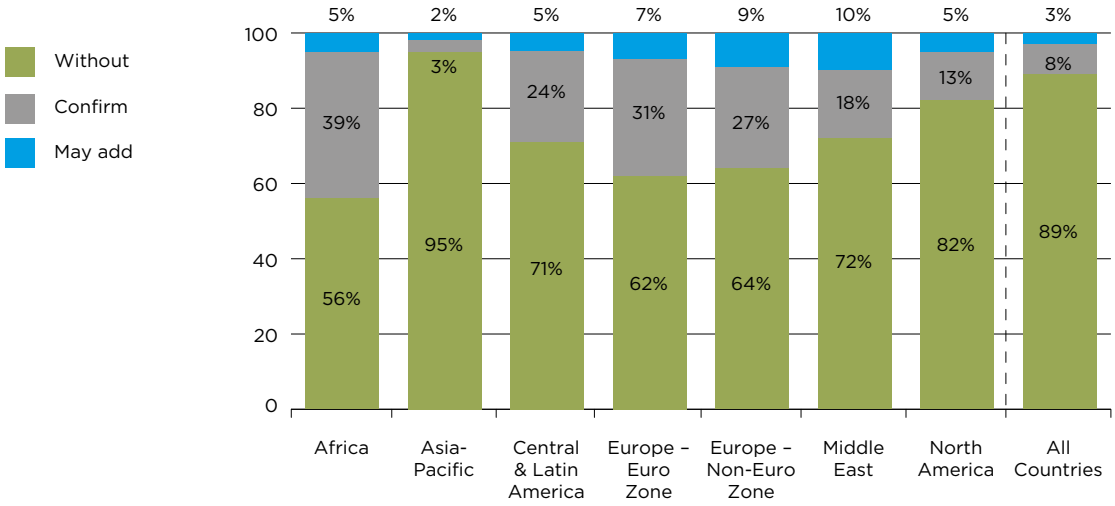


**Figure 60: Volume of L/C Received by Confirmation, 2013 vs 2014**

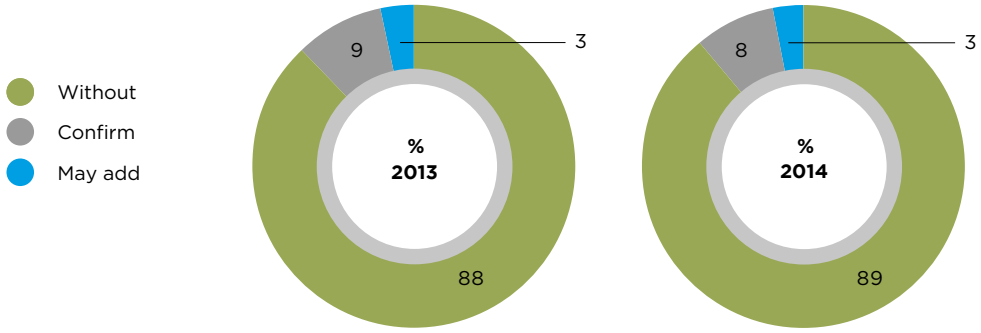



**Figure 61: Percent Distribution on L/Cs Received by Credit Availability Combination, 2014**

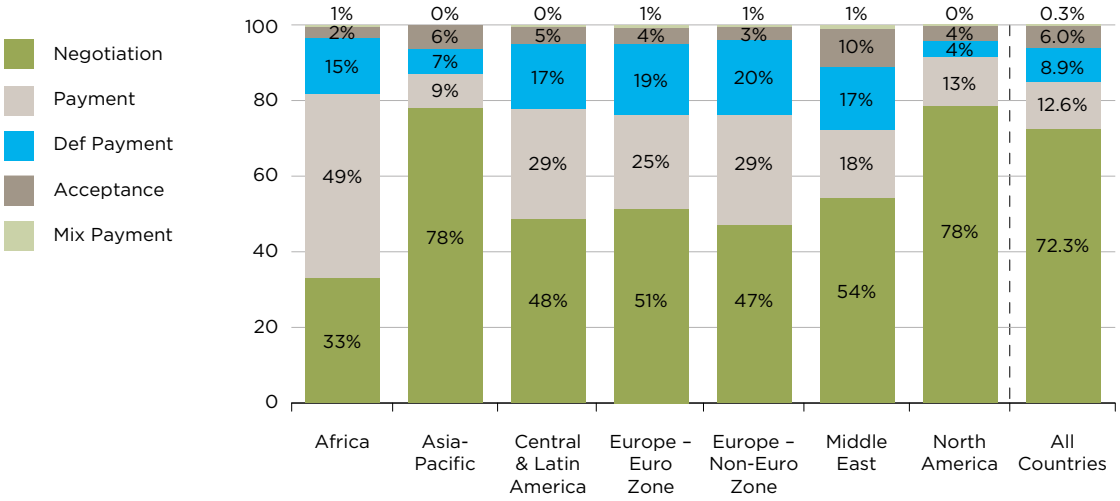
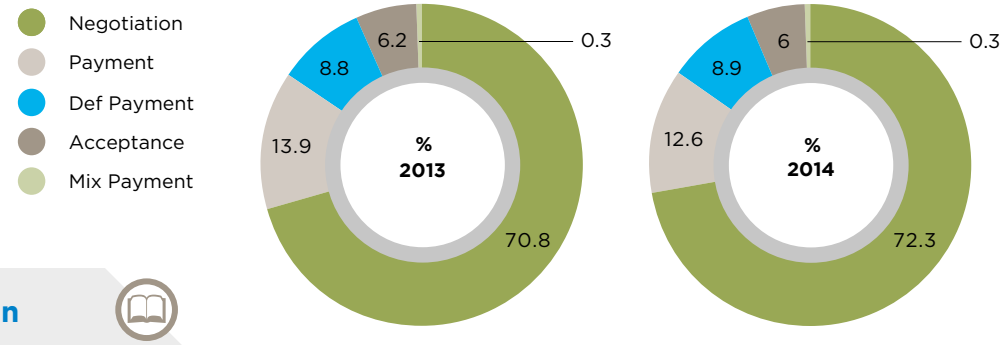



**Figure 62: Percent Distribution on L/Cs Received by Credit Availability Combination, 2014**

Source:
SWIFT Watch



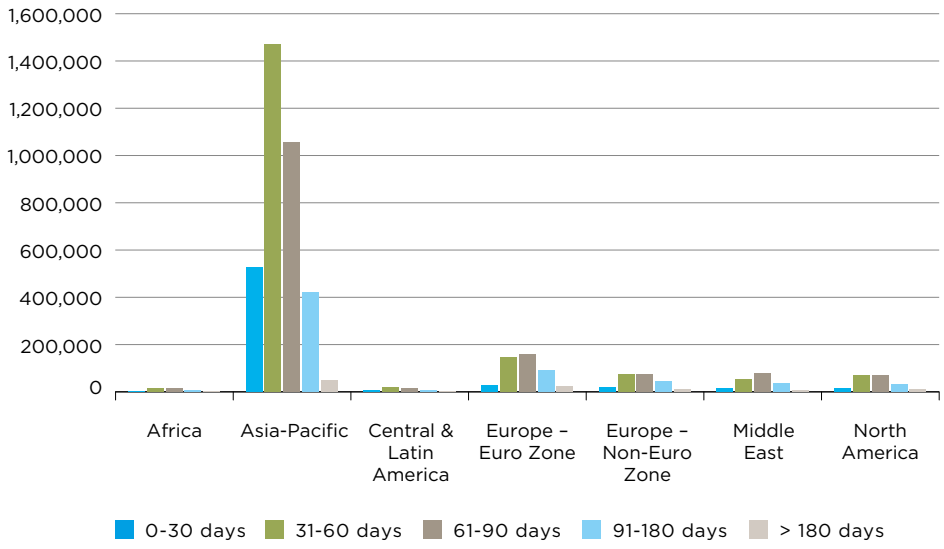

## Definition

**Credit availability:** an indication of how the credit is available. It identifies the bank with which the credit is available (the place for presentation). It is represented by the filed 41a in MT 700

### Negotiation is Preferred in Most Regions

The vast majority of trade (72.3%) is done by negotiation, followed by payment, deferred payment and acceptance. Regionally, negotiation credit accounts for 78% of trade in Asia-Pacific and North America, while in Africa payment credit is preferred. The discrepancies are also likely due to risk perception: while negotiation credit is arguably the cheapest, simplest and most efficient of the L/C instruments, exporters prefer to err on the side of caution in some markets.

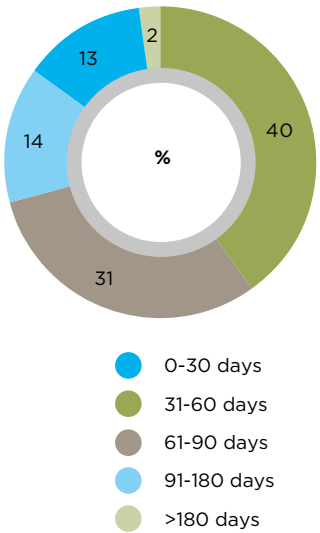
**Figure 63: Volume of L/C Received per Tenor Length by Region, 2014**




### Average Tenor is About 60 days

40% of L/Cs have tenors of between 31 and 60 days, followed by 31% with 61-90 days. The overwhelming preference for shorter-term tenors suggests that exporters are actively trying to maximize their working capital and minimize any potential risk.

**Figure 64: L/C by Tenor Length, 2014**




## Footnote

### SWIFT Business Intelligence

- SWIFT and its customers can monitor the SWIFT trade traffic with the SWIFT Business Intelligence (BI) portfolio. The SWIFT Business Intelligence portfolio continues to expand and now encompasses an entire suite of intuitive tools including analytics, insights and economic indicators designed to grow with a customer's business needs.

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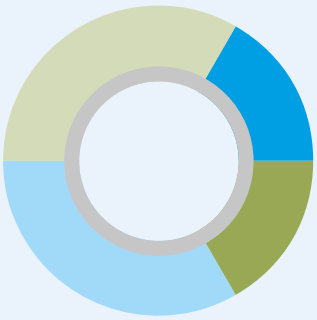

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- **Watch Billing Analyser:** Your SWIFT invoice in detail
- **Watch Value Analyser:** Your transaction value by currency
- **Watch Traffic Analyser:** Your traffic volumes by market, message type and region

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- Manage correspondent network for Payments and Trade Finance
- Develop footprint and portfolio for Trade Finance

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HIGHLIGHT

# TRADE FINANCE IN LATIN AMERICA AND THE CARIBBEAN

Mandated by the Inter-American Development Bank, the following section outlines the preponderant trends shaping the current state of trade finance in Latin America and the Caribbean, as well as the challenges and opportunities for the region's industry actors.

FIBA View on the status of trade finance in Latin America and the Caribbean 74

Interviews: Expert views on the status of trade finance in Latin America and the Caribbean 77

# TRADE FINANCE IN LATIN AMERICA AND THE CARIBBEAN

### The Big Picture

The year 2015 to date has been a challenging one for trade. The statistics for Latin America and the Caribbean (LAC) broadly reflect those of much of the rest of the world. According to a study by the Inter-American Development Bank (IDB), LAC exports experienced a 9.1% drop from January through March in 2015.[2] This is a continuation of the trend of the past few years, after a stagnation of trade volumes in 2012 was replaced by a 2.7% contraction in 2013.[3]

The scale of the relative decline varies across the region. IDB data shows that the biggest drops were felt in Mercosur, where exports dropped by 41.3% in 2014 compared to the previous year, followed by the Andean countries (-6.6%). Central American and Dominican Republic exports grew by a meager 1%, while Mexico was the top performer, with a 17.5% increase.[4]

The relative downturn has come in tandem with a region-wide slump in economic growth. According to the IDB, from 2004 to 2011, Latin America experienced uninterrupted growth with the exception of the post-Lehman crisis year, 2009. The seven largest member states (Argentina, Brazil, Chile, Colombia, Mexico, Peru and Venezuela) experienced growth averaging 6.1% over this period – well up on the 3.7% average over the 1990s. Since then, however, the rate has fallen sharply with a disappointing 2% GDP expansion anticipated for 2015.

This pattern of expansion and deceleration was present in every country in the region, with Venezuela, Argentina and Brazil experiencing the largest growth decreases and Mexico, the smallest. Overall, LAC reported a trade deficit for the second consecutive year in 2014. This was mainly due to the fall in the trade surplus in Argentina, Chile and Venezuela, and the widening of the trade deficits in Brazil, Colombia and Peru.

### Frisking the Issues

When exploring the reasons for the downturn, it again becomes clear that many of them feed into the general global picture. A slowdown in some of the region's key export markets has resulted in weak demand for the key goods which Latin America produces. The managed restructuring of China's economy continues to be an issue for much of the world, while the Eurozone continues to stagnate, with weak demand and concerns over Greece playing on investor confidence and contributing to poor economic growth and sluggish demand. Although the US recovery has been more marked, it still lags pre-2008 levels of growth.

It is no surprise, then, to learn that imports of Latin American goods by the region's three main trading partners have declined: by 28% for China, 6% for the United States, and 3% for the European Union during the first trimester of 2015.[5] The appreciation of the dollar has only served to compound issues.

Another major factor at play is the weakening of commodity prices. This has been most severely felt in the minerals markets. Indeed, between January and October 2014, iron ore prices decreased by 24.6%, and those of gold and copper fell by 11.7% and 6.1%, respectively. Soybean prices, a commodity very important to the export basket of Argentina, Brazil, Paraguay and Uruguay, decreased by 9.6% through October. Regarding oil, its price remained high throughout 2013, but dropped drastically in mid-2014: between June and October it fell 20%.[6]

These figures make the relative slump in certain LAC economies more easily understood. Ecuador, for instance, relies on crude petroleum for around half of its entire export portfolio. This helps to explain the 26.3% drop in overseas sales reported by the IDB for the first quarter of 2015. The only commodity that had a positive price performance was coffee, with its price increasing by 40% through October, mainly because supply was affected by a drought in Brazil, the world´s largest coffee producer.

### Banking Health

Despite the issues facing regional trade, research by the ICC Guatemala in conjunction with Citibank remains positive over the overall health of the banking sector. As a result of institutional regulation and supervision of the banking systems in the region, adverse economic conditions such as rising interest rates, lower commodity prices and depreciating currencies are not expected to result in a banking crisis in any of the major countries in the regions. Hence, from a macroeconomic perspective, the banking system remains strong.

Recent woes aside, cross-border trade out of Latin America and within it has increased markedly over the past few decades. The Florida International Bankers Association (FIBA)[7], for instance, is quick to highlight the astronomical rise in trade between the region's two largest economies (Brazil and Mexico) and the US. It is a pattern repeated throughout much of the region, on a smaller scale. This has brought new opportunities for financiers.

That is not to say, however, that the trade finance community is not faced with its own raft of challenges. Issues over compliance and regulation loom large, technology presents both opportunities and threats to trade financiers' business, while gaps in infrastructure and connectivity act as an effective handbrake on the amount of regional trade that can be done, particularly in Central America and the Caribbean.

Banks working in Latin America are now faced with the unprecedented task of operating under all of these constraints. A region long known for political revolutions is facing one of a different kind: financial.

### Compliance Issues

From changing anti-money laundering (AML) rules, to stricter implementation of Know Your Customer (KYC) and the impending introduction of Basel III regulations, the banking sector has rarely been under so much regulatory scrutiny. It means that tools that would have previously been channeled into financing trade have been instead set aside for the ticking of regulatory boxes: be that

investing in technology or specialized people, or retrenching from markets which have been deemed too risky in which to operate.

According to KPMG's 2014 Global AML Survey, the average rate of AML investment globally was 53%, 13% higher than what was expected.[8] This feeds into a wider story on de-risking, in which banks, fearing regulatory pressure, fines, reputational risk and criminal prosecution, are scaling back operations in certain areas. In total, US and European banks have been hit with fines totaling US$65bn for failing to comply with regulatory measures. It has been argued that one of the main victims of the fears created in this environment is the correspondent banking network which has become crucial in financing trade in less developed parts of the world.

Some global banks have reportedly shut down correspondent banking relationships with partners in regions including Latin America for fear of financial penalization in the US. In 2014, the *Financial Times* cited a British Bankers' Association survey of global clearing banks, which showed that thousands of correspondent banking relationships have been severed since

2011, with an average decline of 7.5% per bank interviewed.[9] Hit by such actions were banks in Mexico, Colombia and other parts of LAC which rely on access to the US banking network to settle trade transactions.

In the era of KYC, it is easy to see why some banks feel the need to take tighter controls over where their money goes, and which partner disburses it. The growing regulatory environment and complexity of programmes force banks to act conservatively in terms of segments to which they provide services. Without relationships with international banks, accessing finance for importing and exporting goods and transferring money abroad becomes prohibitively expensive for regions like Latin America.

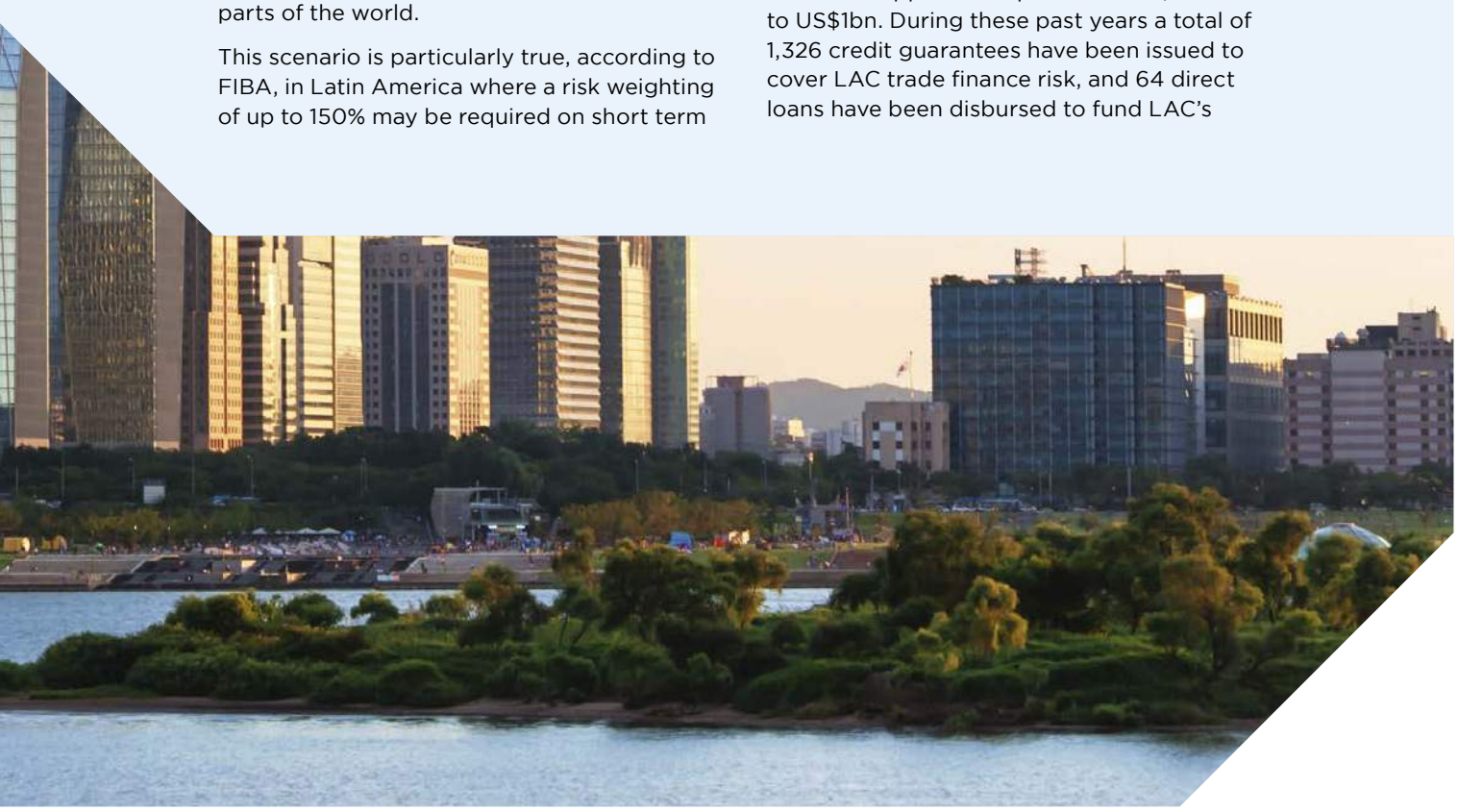
Simultaneously, banks operating in Latin America – as they do elsewhere in the world – continue to prepare for incoming Basel III regulations, which are aimed at increasing financial institutions' resilience to systemic stress through tighter capital controls. The rules were designed to limit the potential of a repeat of the 2008 financial crisis, but many have argued that they will result in a dearth in the supply of trade finance to less developed parts of the world.

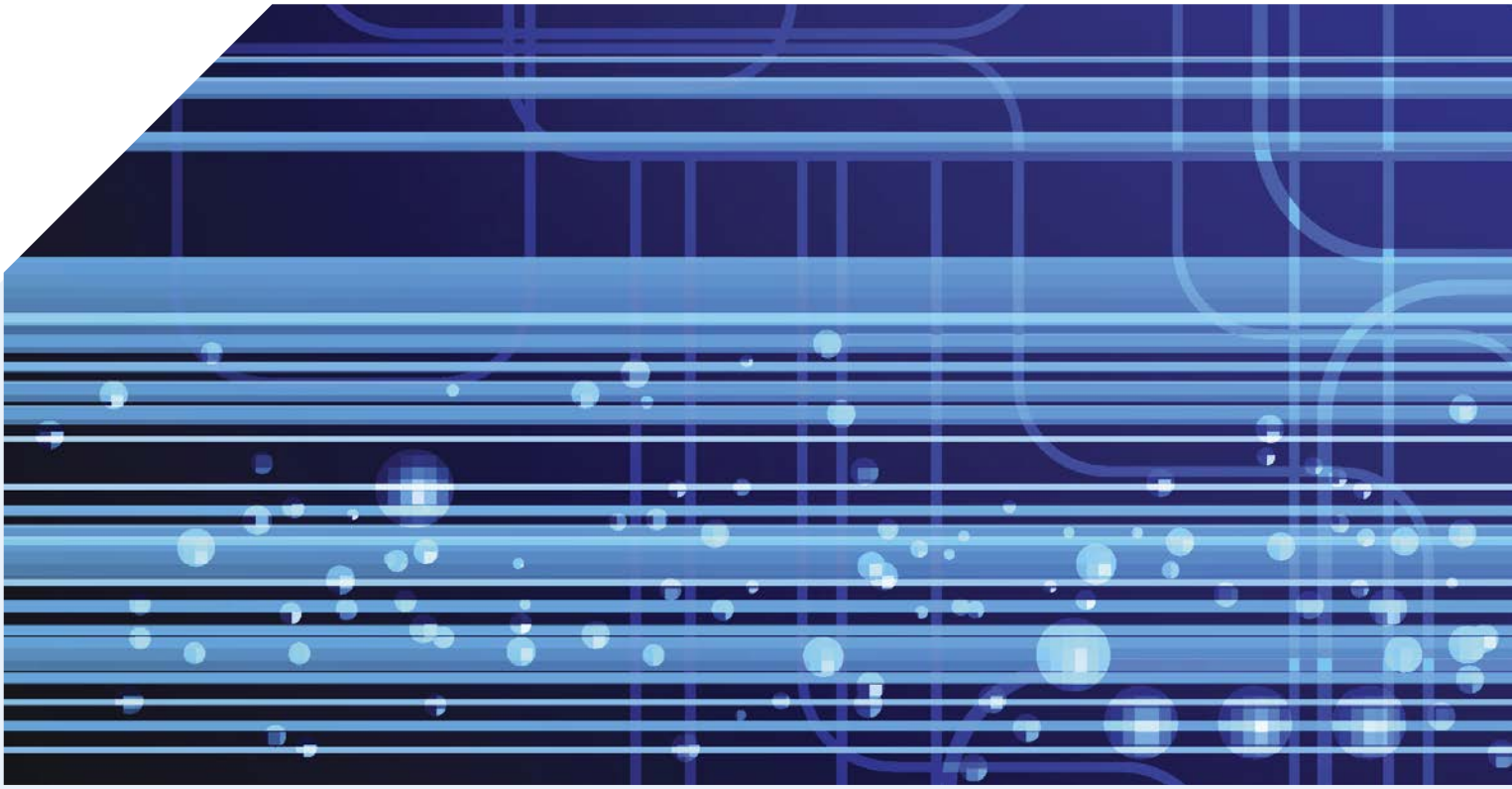
This scenario is particularly true, according to FIBA, in Latin America where a risk weighting of up to 150% may be required on short term loans related to trade finance. By comparison, the weight for developed nations runs closer to 20%. The fear is that smaller, local banks may find themselves on the sidelines of trade finance markets, with the net effect being that customers in these markets will find access to finance harder to come by. It is important for institutions such as FIBA and ICC to work closely with government to collectively attempt to ensure trade finance – historically, one of the least risky areas of banking – does not find itself overly penalized by these measures.

The question is not whether or not we need Basel III, but how we can work to collectively improve upon it.

### Help is at Hand

There is assistance available for those providing trade finance in Latin America, and this year the IDB's Trade Finance Facilitation Program (TFFP) celebrates its tenth anniversary. The IDB launched its TFFP to support Latin American and the Caribbean banks' access to international trade finance markets. Since then, the programme has grown from 30 participating banks (both local and international) to over 300, and from a maximum approved exposure of US$400mn to US$1bn. During these past years a total of 1,326 credit guarantees have been issued to cover LAC trade finance risk, and 64 direct loans have been disbursed to fund LAC's





international trade. In total, 5,271 individual trade transactions have been supported for US$5.03bn.

The volumes supported by the programme have grown exponentially over the years. In 2008-2010, the programme's annual volumes ranged from US$200-300 million, while an all-time record was reached in 2013, with US$1.26 billion in transactions processed under the programme. In 2014, US$952.9 million trade transactions were supported. The data presented by the IDB in the 10th year of the programme support the bank's findings that less developed economies are finding it more difficult to gain access to commercial trade finance. Up to 60% of all transactions since the programme's inception have involved small and vulnerable economies, with 61% of all lending going to SMEs. Furthermore, the fact that US$2.5 billion has been directed towards South-South trade involving LAC economies emphasizes this seismic shift in the direction of global trade.

Despite persistent liquidity, the overall demand for TFFP products in the last year has been high. Expected increases in prices due to expected tightening liquidity, increasing banking costs and worsening market conditions have not materialized yet, as spreads continued to be generally low across the region. With turbulence throughout the LAC region predicted, in trade terms, it is likely that the TFFP will continue to be an important support for these economies.

### The Technology Question

While a powerful trade accelerator, the ubiquitous and rapidly changing technology has altered the financial landscape and those institutions and countries without the resources to compete are at greater risk of falling behind. This is as much the case in Latin America as it is in other parts of the world. In the meantime ongoing issues such as IT, cyber security and evolving global communication continue to present challenges of universal integration. There exists a continued need to protect sensitive data and secure information and while this is excellent news for cyber security firms, which are flourishing thanks to the business of financial services clients, banks without the resources to spend in this area will quickly atrophy.

The news is not all bad. Technological innovation also has a democratizing effect when it comes to participation in global trade. The mobile wallet is a good example, as its use increases overall security for customers and merchants, speeds up payment processing and

essentially eliminates the risk of handling cash. Individuals who may not live in large cities now have varied options for interconnectedness and communication with their financial institutions that may not have been possible prior to technologies such as Apple Pay and YellowPepper. This is excellent news for commerce in more remote parts of LATAM.

A by-product of this technological development is an increase in the trade of mobile technology. Brazil, for instance, exported a massive US$300 million worth of cell phone equipment in the first quarter of 2015. For some smaller economies, the technology is even more important. Peru, for instance, with just 15% of the population of Brazil, exported more than US$160 million of cell equipment over the same period. So while investing in technology may prove arduous and costly for the banking system of Latin America, there are certainly gains to be made here for exporters, particularly with the prospect of further inter- and intra-regional free trade agreements on the horizon.

## References

2 IDB: Latin American Trade Trends 2014 – Update 1Q 2015.

3 Ibid

4 Ibid

5 Boletín estadístico: Comercio Exterior de Bienes en América Latina y el Caribe, Primer Trimestre de 2015, CEPAL.

6 IDB Integration and Trade Sector based on official national sources.

7 FIBA is a non-profit trade association, based in Florida whose members include the largest financial institutions from Europe, the United States, Latin America and the Caribbean and aims to influence regulation and legislation affecting the industry.

8 Source: World City & US Trade Numbers.

9 Source: Financial Times, November 13, 2014

# FIBA VIEW ON THE STATUS OF TRADE FINANCE IN LATIN AMERICA

### Latin America's Rapidly Evolving Trade Finance Landscape – The Revolution is Happening

By the Florida International Bankers Association (FIBA) [10]

### Overview

Headwinds in the form of the macroeconomic climate and tighter regulatory requirements, along with the ever accelerating pace of technological innovation, pose obstacles to some of international trade finance's longstanding pillars. Since 2008, the Latin American trade balance has seen a significant uptick in exports (US$1049.1 billion exported last year)[11]. According to World City's 2015 Trade Numbers report, the United States has achieved a record US$3.97 trillion in trade with the world. Mexico and Brazil actively serve as two of the US' top trade partners, contributing nearly US$192.0 billion – of which $171.56 billion comes from Mexico alone – of the total US$3.9 trillion.

Within this increased trade flow, the banking system is now tasked more than ever with striking the right balance between regulatory compliance and expanding cross-border trade activity. Trade finance offers a practical approach for banks to meet buyer and supplier liquidity needs within a shifting regulatory framework.

### Compliance Costs

Increased trade volume between countries means greater stress on the correspondent banking system specifically in terms of upholding a key compliance requirement — transactional transparency. Vital resources and tools like specialized executives and increased operational budgets are either in short supply or just plain absent. According to KPMG's 2014 Global Anti-Money Laundering Survey, the average rate of AML investment globally was 53%, 13% higher than what was expected.[11]

The increased cost and volume of anti-money laundering (AML) scrutiny required has to an extent constrained the growth of trade finance, reaffirming the importance for organisations like the ICC globally and FIBA regionally to provide the needed resources and educational information to the community.

### De-Risking Portfolios

Current AML and anti-terrorist enforcement actions have led some financial institutions to actively "de-risk" their portfolios, with some large global banks ridding themselves of all accounts from second and third tier banks to comply with Know Your Customer (KYC) regulations. According to KPMG's 2014 Global AML Survey, KYC regulations were ranked the second largest AML investment by respondents. The action of de-risking is inadvertently forcing financial institutions to look for alternative methods of lending and payment methods, which poses ancillary risks.

Simultaneously, fines, reputational risk and criminal prosecution are on the rise, fraying the network of relationships that tie the global financial system together, and driving up costs of finance for underdeveloped countries. This is arguably leading to a retrenchment from the correspondent banking system that is so vital in ensuring trade finance is provided to less-developed regions.

Without relationships with international banks, accessing finance for importing and exporting goods and transferring money abroad becomes prohibitively expensive for regions like Latin America.

### Unintended Consequences of Basel III

While clearly needed after the global crisis that began in 2008, Basel III reforms have also unfortunately created a few unintended consequences in Latin America, where a risk weight of up to 150% may be required on short term loans related to trade finance. By comparison, the weight for developed nations runs closer to 20%. This makes it more difficult for smaller banks to service clients. However, initiatives such as the ICC's Trade Register should help lessen the risk of this.

## References

10 FIBA is a non-profit trade association and international centre for financial excellence. The Florida-based organisation's membership includes the largest financial institutions from Europe, the US, Latin America and the Caribbean.

11 Source: Inter-American Development Bank

CUERNAVACA
VIADUCTO TLALPAN
AV MEX
SANTA TERES

# EXPERT VIEWS ON THE STATUS OF TRADE FINANCE IN LATIN AMERICA AND THE CARIBBEAN

The ICC Banking Commission spoke with some of the most senior and respected figures in LAC trade finance to get their views on the burning issues affecting the sector now and in the future.

**MEXICO**

GERARDO GUTIERREZ-OLVERA CABRALES
Managing Director, Head of Trade Finance & Intl Treasury Services BANORTE; President of Trade Finance Committee, ICC Mexico

LUIS FERNANDO MENDOZA
Trade Finance and Correspondent Banking Director, Grupo Financiero Intercam

**ECUADOR**

SANTIAGO PROAÑO ENDARA
Comercio Exterior – Banca Empresas, Banco Pichincha

**BRAZIL**

MAURO CAVALCANTI DE ALBUQUERQUE
Head of Global Transaction Banking, Santander Brazil

**HONDURAS**

ILDOIRA BONILLA
Vice President of International Business, Banco Atlántida

**PARAGUAY**

RAÚL VERA BOGADO
President, Banco Regional

**BOLIVIA**

CHRISTIAN HAUSHERR ARÍÑEZ
Chief Financial Officer, Banco de Crédito de Bolivia

**ARGENTINA**

ALBERTO LLAMBÍ CAMPBELL
Director – Member of the Board, Banco CMF

# What are, according to you, the preponderant trends shaping the current state of trade finance in Latin America?

**GERARDO GUTIERREZ-OLVERA CABRALES:** In the two decades of NAFTA and the incorporation of commodity-hungry China into the global economic equation, international trade has been one of the major growth engines of Latin America. The maturity and stability of US-Mexico commercial ties, as well as the "energy revolution" taking place in North America will keep strengthening the NAFTA region.

Because of this new reality, huge Latin American commodity exporters will no longer be the flavour of the month and banks active in LATAM will have to become more creative to provide the adequate trade and supply chain financing and services to support traditional trade flows as well as unbundled foreign trade to old and new players.

---

**LUIS FERNANDO MENDOZA:** Both intra-regional and international trade agreements are helping to push Latin America into the trade world every day by boosting access to their economies and allowing these countries to look for new horizons, creating inbound and outbound trade with new partners. Together with the increasing purchasing power of the growing middle class in Asia and Latin America, and its demand of consumer goods, this is what's driving trade development these days.

---

**MAURO CAVALCANTI DE ALBUQUERQUE:** While there is still consistent demand for traditional trade instruments, such as commercial letters of credit and collections, there is growing demand from clients for sophisticated solutions, upon which we have focused in recent years. Supply chain finance is a growing area. Working capital solutions have become a very favourable way for corporates to manage their liquidity.

---

**CHRISTIAN HAUSHERR ARÍÑEZ:** For a number of years now, the traditional trading partners of all major economies have been losing ground to Asian countries, primarily China. Specifically, in Bolivia we see significant opportunities in trade finance with China as our commercial relations continue to deepen with that country.

---

**RAÚL VERA BOGADO:** The impact of lower commodity prices is pressing an increase in pre-financing by traders, which are coming from commodity trading houses, who are better suited to providing such facilities than global banks with decreasing appetites. Other trends include the looming effect of the slowdown in the Chinese economy and trade, the somewhat protracted recovery of the United States and its impact on access to US dollar financing, and the approaching implementation of Basel III standards might induce banks to be even more cautious in capital allocation decisions.

---

# On a regional scale, do you see any improvement in terms of access to trade finance for SMEs?

**GERARDO GUTIERREZ-OLVERA CABRALES:** Lending to SMEs has been steadily growing in Mexico and local commercial banks are very interested in this segment and best positioned to cover them. Although domestic banks are more familiar with the SME client and business environment, sometimes, purely local financial institutions lack of the global specialized capabilities and expertise, which may result in a less competitive trade finance offering. This again represents a very clear opportunity for the creation of banking partnerships between local and international banks active in trade finance.

---

**LUIS FERNANDO MENDOZA:** The current legislation and policies discussion around Basel III and compliance are mainly affecting small businesses, since large corporates can always access other means of financing. It is also a slow road for these companies when it comes to tools such as BPO or factoring and supply chain finance. Banks have a lot to worry about in terms of the new regulatory framework and most of their focus is not really in trying to support the SMEs trade efforts, even though it is something they'd like to do.

---

**MAURO CAVALCANTI DE ALBUQUERQUE:** SMEs represent approximately 80% of companies trading in LATAM, but account for less than 15% of total trade financing. Because of their limited credit history and lack of technical expertise, working with smaller companies requires a deeper knowledge of the clients, which can be achieved only by local banks. We do not necessarily see an improvement in terms of access to trade finance for SMEs. The challenge is to ensure that SMEs know where to find alternative sources of financing and that they understand how products work.

---

**ALBERTO LLAMBÍ CAMPBELL:** We think that there will be an improvement in this area and change seems to be happening. For example, in Argentina, banks such as Banco Santander Rio, Banco Galicia and others have developed commercial platforms specialized in trade finance for SMEs, offering courses and support to such businesses.

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# How are the evolving political, environmental, economic, regulatory and technological contexts challenging the established model in the industry?

**GERARDO GUTIERREZ-OLVERA CABRALES:** Companies in Latin America have been utilizing high quality trade finance assets for many years to finance trade in a low risk way. Unfortunately, for many years, trade bankers did not gather enough statistical evidence to support this statement. Thanks to the ICC's Trade Finance Register, this situation is now being addressed, but the industry must keep on collecting data in order to push more appropriate regulatory capital treatment. Banks need to work even more closely with regulators to resolve any remaining doubts about the excellent credit risk track record of trade finance and to promote its benefits to the economy.

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**MAURO CAVALCANTI DE ALBUQUERQUE:** From Basel III to the Dodd-Frank Act, to FATCA and AML, the new regulatory framework has required banks to invest heavily in systems and procedures to operate in the new trade finance environment. There are also a number of new risk dimensions in the market. Sovereign and credit risks have been joined by environmental, reputational and compliance risks when financing complex projects and trade flows in emerging markets. This could potentially limit business activities to only the markets and companies that banks are truly comfortable with.

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**CHRISTIAN HAUSHERR ARÍÑEZ:** There are several factors affecting the established model. The number of companies with cross-border operations continues to grow, and that creates a need for new ways of doing business. Access to information has also had a significant impact on the way companies in the region are managing their value chains. However, significant challenges remain in the establishment of cross-border regulations and in the institutional weaknesses found in many countries within the region.

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**ILDOIRA BONILLA:** New technology is required to satisfy our customers' needs. They demand quicker, cheaper, "anytime and anywhere" payments. As well as this, customers are taking more control of their financial relationships, making them more personal and demanding greater trust. Among companies with lower and, in some cases, non-existent risk ratings, the lack of credit information and tougher regulations and AML policies that must be implemented are some of the challenges that need to be faced, and this will probably be at a greater cost to banks.

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# In your opinion, what key forces will drive trade finance in the near future?

**GERARDO GUTIERREZ-OLVERA CABRALES:** New regulatory requirements are here for good and will only keep growing. This new reality is something that trade financers in LATAM have to learn to live with. These increase the cost of conducting trade finance, and not all banks can be good at everything. Financial institutions will have to focus on their most profitable, well-known markets and familiar trade finance business lines, and therefore cross-border partnerships between banks will grow stronger in order to support their clients abroad.

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**MAURO CAVALCANTI DE ALBUQUERQUE:** Working capital management will be the key force that will drive trade finance in the near future: giving the customer more value from their solutions. However, traditional finance will still exert an important role in trade finance: financing exports and imports and forcing closer relationships between parties through guarantees, L/Cs and early payment programmes (EPPs).

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**CHRISTIAN HAUSHERR ARÍÑEZ:** The fall in the prices of many commodities and the depreciation of almost all currencies in the region will have a significant impact in the short and medium term in Latin America as most of the countries continue to have economies that rely heavily on the export of commodities.

Another important factor is the continued emergence of Asian countries, which have been stealing ground on those countries that consider themselves to be the traditional trading partners of all major economies. Specifically, in Bolivia we see significant opportunities in trade finance with China as our commercial relations continue to deepen with that country.

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**RAÚL VERA BOGADO:** Commodity trading houses will keep their influence in commodity trading, so long as banks continue to be hit by new regulation that prevents them from increasing pre-export financing volumes. For SMEs, accounts receivables financing might be an opportunity to grow. We can see more SMEs using open account solutions, replacing the traditional letter of credit transaction.

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**ALBERTO LLAMBÍ CAMPBELL:** Latin America is basically the same commodity exporting region it was 40 years ago. As it was then, these exports accounted for nearly 10% of GDP in 2010. But in Mexico and Central America commodity dependence has fallen sharply. Look at the example of Asia, which in the 1970s was a net commodity exporter, evolving to a net importer in 2010. There is a long way to go. While LATAM as a whole is more diversified than four decades ago, a lot of commodity-dependent counties are suffering with the slump in prices – especially countries that have no strong economic fundamentals and which are not fully integrated into the global financial system.

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**SANTIAGO PROAÑO ENDARA:** Trade finance has been emerging in the Latin American market as a key part of the banking offering, and will continue to do so. We see this continuing in an environment dominated by trade agreements, legal security and foreign investments. The economies of LATAM will be and will have access to bigger markets. The main trends over the coming years will be related to the political stability that we hope the region will achieve over the next period of time. The growth of trade finance depends so much on these regional political factors, as well as macroeconomic issues such as the recovery of the global economy and the extent of the slowdown in China.

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# Looking ahead and in realistic terms, how would you describe the state of trade finance in Latin America in 2020?

**GERARDO GUTIERREZ-OLVERA CABRALES:** There are two FTAs underway that will have a very significant impact on LATAM trade flows. The Trans-Pacific Partnership (TPP) and the Pacific Alliance – a comprehensive second generation South-South deal that includes Mexico, Colombia, Peru and Chile – both provide great opportunities. The TPP is being negotiated with nine other countries which will give the three LATAM countries involved (Mexico, Chile and Peru) greater access to the Asia-Pacific Rim (we could call this "Tigers and Dragons meet the Three Amigos"). It represents a huge and fast-growing potential market which will also remove the dependency of the region on the US economy.

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**LUIS FERNANDO MENDOZA:** Certainly, we'll feel the increased presence of some of the economies that have benefitted from a somewhat steady economic cycle and haven't stopped their efforts at penetrating other markets, a clear example being China investing in Latin America. Another example is the growth in Mexico's automobile and telecommunication sectors. All these, together with the very marginal growth in economies like the US and Europe, will result in south-south trade that is more visible than ever.

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**MAURO CAVALCANTI DE ALBUQUERQUE:** We will see a mix of sophisticated clients looking for structures with added value, such working capital solutions, ECA and supply chain financing, and other clients still working with traditional trade finance instruments such as L/Cs and EPPs. Banks will be pushing to optimize their capital remuneration, looking for structures that mitigate risk, such as the collateralization of inventory and receivables, accounts receivable discount insurance, L/Cs discounting, and ECA financing.

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**CHRISTIAN HAUSHERR ARÍÑEZ:** Trade finance should continue to experience high growth rates in the region. In the short and medium term, the commodities slump and the depreciation of almost all currencies in the region will have a significant impact, as most countries continue to have economies that rely heavily on the export of commodities. Countries that are more reliant on commodity exports will experience slower growth, as their terms of trade will be put under significant pressure.

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**ILDOIRA BONILLA:** Political and environmental factors, combined with new technology, will require new financial products tailored for companies of all sizes. All of these transactions must be controlled by new regulations, based around AML laws and risk reduction. New business models will be developed, with Institutions being able to provide ideas, capital and operational skills

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# How is the use of non-traditional trade finance products and practices evolving in Latin America (in particular with supply chain finance and its other related techniques: trading on open account, forfaiting, factoring, BPO)?

**GERARDO GUTIERREZ-OLVERA CABRALES:** A growing portion of the Mexico-US trade flow has moved away from import L/Cs into open account territory and cross-border supply chain financial solutions (buyer-centric SCF, factoring, forfaiting, etc.) that will keep on growing in importance.

The BPO is still under construction and local regulations will have to be adapted before it is widely accepted (as is the case in Mexico). It still has a long way to go in the region. However, I firmly believe that technology will change the trade finance industry very soon. The convergence of paper-based payments with more efficient electronic initiatives is inevitable and desirable.

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**LUIS FERNANDO MENDOZA:** Although these products are perceived to be the natural, simplest and least invasive way for trade finance banks to evolve, the reality is that their penetration has been too slow in the international trade arena. Only a small bunch of large global corporates are seriously interested and investing in it. There is a genuine effort from some government-owned banks, sometimes supported by official agencies such as the IFC and IDB, to spread the benefits of this type of financing, but their reach is limited.

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**MAURO CAVALCANTI DE ALBUQUERQUE:** The BPO still does not have demand among customers, although it would increase efficiency for both sides. In our view, banks must invest in technology infrastructure system in order to be compliant with the messaging requirements of the BPO, and update physical trade documents required under local legislation to release the delivery of goods from customs.

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**ALBERTO LLAMBÍ CAMPBELL:** We find that across all of LATAM, each country finds itself in a different scenario. For example, Chile or Brazil have more sources – through their correspondent banking network – of trade finance than Argentina or Venezuela. Generally speaking, classic trade instruments such as L/Cs, and standby L/Cs remain very important in LATAM. Nevertheless, and it again depends on the country, other products are showing important growth. For example, we are seeing the growing use of open account transactions in trade finance.

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# Are you familiar with the ICC Banking Commission and its work? If yes, how do you think its role should develop in the next five years? On what key areas and issues should it focus?

**GERARDO GUTIERREZ-OLVERA CABRALES:** I am an active member of the ICC Banking Commission in Mexico and I believe that it should focus on gathering global qualitative historical data and market intelligence that supports a better regulatory treatment for trade finance information, analysing and writing the global rules, standards and best practices for international trade, linking the different ICC Banking Commissions to develop a homogeneous approach to common issues.

**LUIS FERNANDO MENDOZA:** I think its work has been instrumental in emphasizing the importance of trade finance amidst regulatory flux. We are seeing its results cascading from the main discussion panels in Europe and the US to second tier economies. It should, however, be more aggressive in lobbying local decision-makers and high-level banking organizations in developing countries with a view to supporting importers and exporters in Latin America more quickly. Convincing local banking regulators to focus on trade finance must be a priority.

**MAURO CAVALCANTI DE ALBUQUERQUE:** We are very close to the ICC Banking Commission, and have already seen significant advances in terms of regulatory flexibility for trade finance, proving its capacity as a safer and liquid asset.

We think ICC should keep gathering information and proposing capital and liquidity treatment and KYC/AML requirements that take into account trade finance's idiosyncrasies. ICC should also work with banks on structures that could be used for liquidity relief purposes.

**ILDOIRA BONILLA:** The ICC Banking Commission should continue providing rules and guidelines to the different actors of the trade sector such as importers, exporters, and the financial institutions that provide funding. It is also very important that it continues to expand its support through its educational programmes and market surveys which outline the major risks and AML trends.

# BUSINESS TRENDS IN FACTORING

2014 was another impressive year of performance for the global factoring industry. Even as international trade softened due to the uneven economic recovery and as we witnessed the plummeting of commodity prices, along with quite a volatile foreign exchange environment, the factoring industry grew by 6.3% in 2014, surpassing EUR2.35 trillion in global annual volume, a rate faster than the 4.6% recorded in 2013. This growth was led predominantly in Europe and the Americas at 8% each, which together account for over 71% of the global factoring volumes, as reported by Factors Chain International (FCI) in Figure 65.

**Figure 65: FCI Global Factoring Statistics by Region, (in millions of EUR) 2014**

| | 2013 | 2014 | Group rate % change |
|---|---|---|---|
| Europe | 1,354 | 1,463 | +8% |
| Asia | 599 | 615 | +3% |
| Americas | 192 | 207 | +8% |
| Africa | 23 | 21 | -9% |
| Australasia | 40 | 42 | +5% |
| Total | 2,208 | 2,348 | +6% |

In 2014, domestic factoring only grew by 1.6% over 2013, indicative of the general slowdown in global GDP. However, cross border international factoring grew at a much faster pace, generating over EUR490 billion in volume last year, and an increase of 22% over the same period.

Since the start of the financial crisis in 2009, factoring has been growing at a rate of 14% per annum, doubling in size, adding over 1 trillion euros in factoring volume, a substantial feat achieved in such a short period of time, considering the modern era of factoring began over a century ago in the US. During this same period, domestic factoring grew 11% on average, however international cross border factoring grew even faster, at a rate of 24%, as can be seen in Figure 68.

**Figure 66: FCI Global Factoring Statistics by Region, 2014**

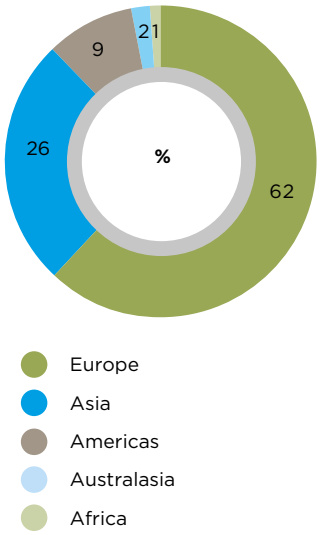


**Figure 67: Total Domestic Factoring Volume (in millions of EUR), 2009-2014**

| 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | CAGR |
|---|---|---|---|---|---|---|
| 1,118,100 | 1,402,331 | 1,750,899 | 1,779,785 | 1,827,680 | 1,857,410 | 11% |

**Figure 68: Total International Cross-border Factoring Volumes 2009-2014 (in millions of EUR)**

| 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | CAGR |
|---|---|---|---|---|---|---|
| 165,459 | 245,370 | 264,108 | 354,840 | 402,753 | 490,114 | 24% |

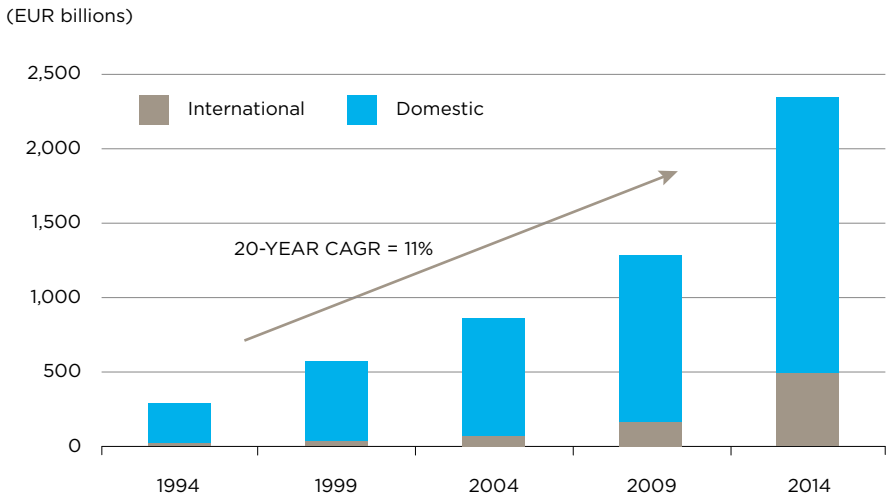
## Definition

**The Compound Annual Growth Rate (CAGR)** is the mean annual growth rate of an investment over a specified period of time longer than one year.

Domestic factoring amounted to EUR1,857 billion in 2014, accounting for 79% of total global factoring volume, compared to international factoring, which amounted to EUR403 billion, accounting for 21% of global volume. This growth in cross border factoring has again been driven by an increase in open account trade, especially from suppliers in the developing world, pushed by the major retailers/importers in the developed world, and the acceptance of factoring as a suitable alternative to traditional letters of credit. The greater China region has played the most important role in this impressive growth story, adding a staggering increase in cross border factoring volume over the past decade.

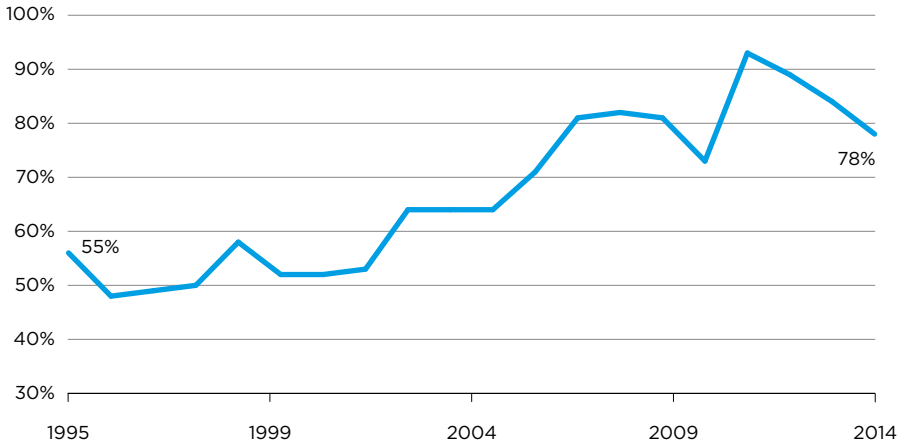
Since 1993, the global factoring industry has been growing at a relatively fast pace, increasing on average nearly 11% per annum, as can be seen below in Figure 69 below.

**Figure 69: Global Factoring Volume 1994-2014**



Founded in 1968, FCI is a global network of leading factoring companies, whose common aim is to facilitate international trade through factoring and related financial services. FCI has 280 members located in 75 countries, and is the world's largest factoring network, with member transactions representing approximately 78% of the world's international cross-border correspondent factoring business conducted in 2014, as can be seen in Figure 70.

**Figure 70: FCI's Share of World International Factoring Volumes (in %), 1995-2014**




Factoring is considered to be a product designed to offer financing to SMEs. Funding is offered based upon the accounts receivables created by the client: with a factoring solution, the factor agrees to pay an agreed percentage of approved debts as soon as the receivables are assigned to the factor. The factor will often also undertake all credit management and collections work. There will normally be a charge for the collections service and, if it is required, for bad debt protection as well as a discount charge for finance provided in advance of collections. Not only is most of the business conducted within the framework and membership of FCI, but FCI also provides a legal foundation to conduct cross-border correspondent factoring. The General Rules of International Factoring (GRIF) form the legal basis under which nearly all cross-border correspondent factoring business transactions are conducted, and this legal framework has been accepted by nearly every international factoring company around the world. FCI members also use a proprietary communication system called edifactoring.com. Like the SWIFT messaging system, edifactoring.com provides a sound and secure means by which members can issue factor guarantees, send invoice data, issue dispute notices, and send payment messages.

The factoring industry continues to evolve and grow, entering new markets and bringing in many new players. However, alternative forms of factoring, like reverse factoring/confirming have evolved to complement this unique form of financing open account trade. The significant increase in world factoring volume has been driven by a systematic growth in open account trade, which has been led by commercial bank run factoring businesses, especially in Europe and Asia. In Europe alone, over 90% of the factoring industry is generated by bank owned factoring subsidiaries and in most of Asia, trade finance units of commercial banks control the vast majority of the factoring activities there. In fact, only until recently, banks in China were the only parties permitted to operate a factoring activity. However, a change in policy there has recently allowed the service to be operated by non-bank financial institutions, resulting in over 1,000 new factoring businesses established over the past few years. In many markets, like the US and Brazil, factoring is unregulated, and therefore most players operate as non-bank financial institutions. Nonetheless, the explosive growth of the industry, especially since the start of the financial crisis, is in large part inspired by an enhanced perception of risk globally, but also stems from the shift from overdraft/ unsecured credit facilities to receivables-based factoring/ invoice-discounting portfolios. This shift is also enhanced by the introduction of Basel II/III rules and the favorable treatment they impart on banks from a capital treatment standpoint but also based on the understanding that factoring is simply a more prudent form of financing. Governments, development banks and regulators have come to understand and appreciate that factoring is a secure and reliable method of financing trade and an invaluable means of providing liquidity to SMEs, the engine of growth in most economies.

The ICC Global Survey 2015 is an excellent vehicle to promote factoring, as many of the traditional trade finance players are also members of FCI, and have factoring activities within their respective organizations. It is also valuable to potential new companies interested in developing cross border factoring as an alternative to traditional letters of credit and documentary collections. As a contributor, it is our hope that this fine publication will contribute to a better understanding of our industry.

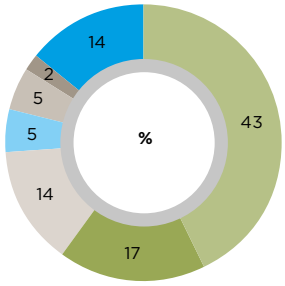
# BUSINESS TRENDS IN EXPORT FINANCE

The following section outlines the findings of the *ICC Export Finance Global Survey 2015*, conducted by Trade and Export Finance (TXF), to identify the most relevant and recent market trends within export finance.

## Key findings

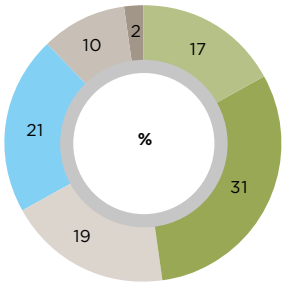
- Only 10% of export financiers report an increase in fees over the past year
- Only 12% report an increase in pricing over the past year
- Legal and regulatory hurdles are the biggest obstacle to doing export finance business in new markets
- 70% of export financiers have successfully concluded business with institutional investors
- 42% believe a lack of understanding of the product and associated risks is holding back more institutional investors from entering export finance
- 35% are currently pricing Basel III into their export finance transactions
- Most financiers do not believe Basel III will have an impact on their competitiveness
- The majority of respondents believe the export finance market will grow by 1%-10% in 2015
- 58% report that export finance is being used more within project financings
- Russia was the leading borrower destination in 2014, while oil & gas was the top sector
- Euler Hermes ranked the most efficient ECA, and UKEF the most improved
- Export finance remains a profitable business for the vast majority of those in the industry (79%)

**Figure 71: Profile of Export Finance Professional**




- Bank
- Export Credit Agency (ECA)
- Corporate (Exporter)
- Corporate (Borrower)
- Law firm
- Private insurance underwriter/ Broker
- Other (please specify)

**Figure 72: How Has Pricing in Export Finance Changed Over the Last Year?**




- Decreased by more than 20%
- Decreased by more 11%-20%
- Decreased by 1%-10%
- Stayed the same
- Increased by 1%-10%
- Increased by 11%-20%
- Increased by more than 20%

## Overview: Pricing and Fees Decrease as Capital Markets Expectations Rise

The export finance industry suffered a significant decrease in pricing and – even more so – fees in 2014, and is anticipating a rise in the interest of capital markets in 2015 as institutional investors become more knowledgeable about the export finance product.

These are some of the key findings of the ICC Export Finance Global Survey 2015, conducted by TXF, which polled a range of export finance professionals from across the world.

Those polled included global heads of export finance at banks and CEOs of Export Credit Agencies (ECAs), as well as senior professionals at both exporting and borrowing companies. The survey was conducted anonymously, to ensure participants felt confident in being open and honest about their views.

## Pricing and Fees Head South

Two-thirds of those questioned reported that pricing had gone down in 2014, with one in six placing this decrease at greater than 20%. By contrast, only 12% reported an increase in pricing and the vast majority put that increase at 10% or less.

The gloomy 2014 pricing picture for bankers is expected to trickle into 2015. Twice as many survey respondents (38%) anticipate pricing will decrease further in the next 12 months as those that believe it will increase (19%). The majority, the remaining 43%, expect pricing will stay at the same level.

There is a similar pattern for bank fees, where 54% report a decrease in 2014 as compared with just 9% who have experienced an increase. The low pricing and fees are reflective of a competitive marketplace with diversified liquidity options for borrowers.

One factor identified that could drive pricing upwards is regulatory requirements, and particularly Basel III. Only a third of the professionals surveyed indicated that they were already pricing Basel III into their transactions. A larger proportion, 55%, stated it would lead to an increase in their pricing nearer to 2019, although the vast majority of these believed that increase would be "moderate".

In terms of the impact Basel III is currently having, nearly 70% of respondents believe that it has not made a difference to their competitiveness in the market. Of the 30% who did feel it was having an impact, a slight majority (18%) believed it was making them less competitive – presumably linked to the increase in pricing and resources the compliance requirements entail.

This reflects the uneven implementation of Basel III, whereby both within specific regions and across regions as a whole, financial institutions are integrating and pricing Basel III into their operations at varying paces. While some have been fully Basel III compliant for a number of years now, on the opposite end of the spectrum others are waiting until closer to the 2019 deadline before reaching full implementation. This underlines how institutions competing with each other for the same business might be at an advantage or disadvantage relative to their counterparts - both in terms of pricing but also in terms of the speed and flexibility with which they can carry out transactions.

**Figure 73: Export Finance Profitability**

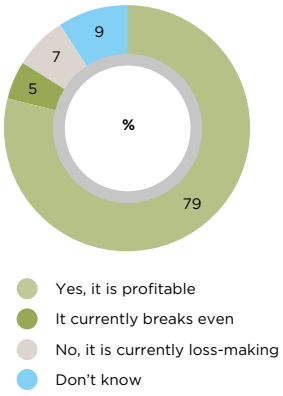



**Figure 74: Expectations on Pricing Over the Next 12 Months**

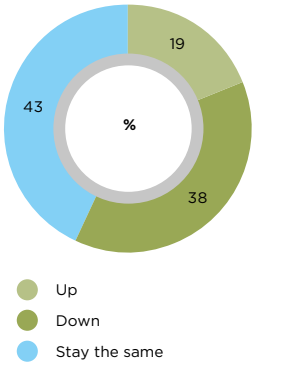



**Figure 75: Trends in Export Finance Bank Fees Over the Past Year**

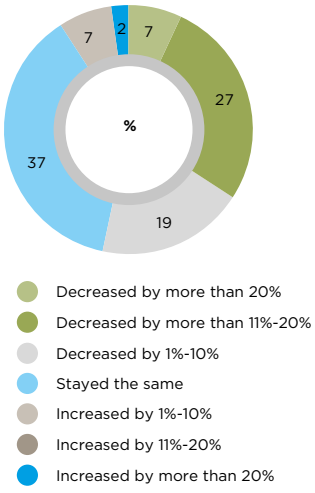
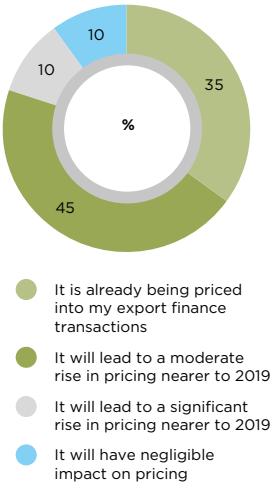


**Figure 76: Impact of Basel III on Export Finance Pricing**




## More Sophisticated Capital Markets

The export finance product continues to arouse the interest of the capital markets and this is reflected in the survey. Six in 10 of those surveyed expect to see more capital markets solutions in the near future, while the remaining four in 10 are evenly split among those who are unsure and those that do not believe there will be further capital markets solutions in 2015.

As with last year's survey, 36% of respondents felt that investors' understanding of the export finance product today, as compared with previous years, had increased.

Where there has been a greater change is in the perception of barriers to more institutional investors entering export finance. While 49% of respondents cited a lack of understanding of product and associated risks among investors last year, this number fell to 42% this year. Conversely, while pricing was identified as a barrier by 9% of respondents last year, it now stands at 16%, illustrating the knock-on effect that low pricing in the industry is having.

**Figure 77: Most Prohibitive Factors to Doing Export Finance Business in New Markets**

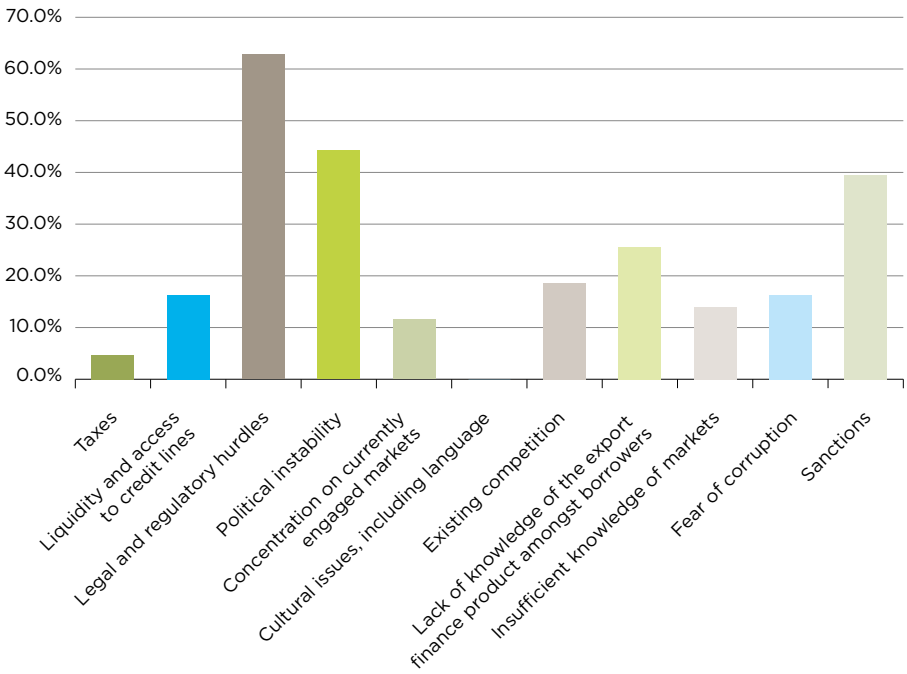
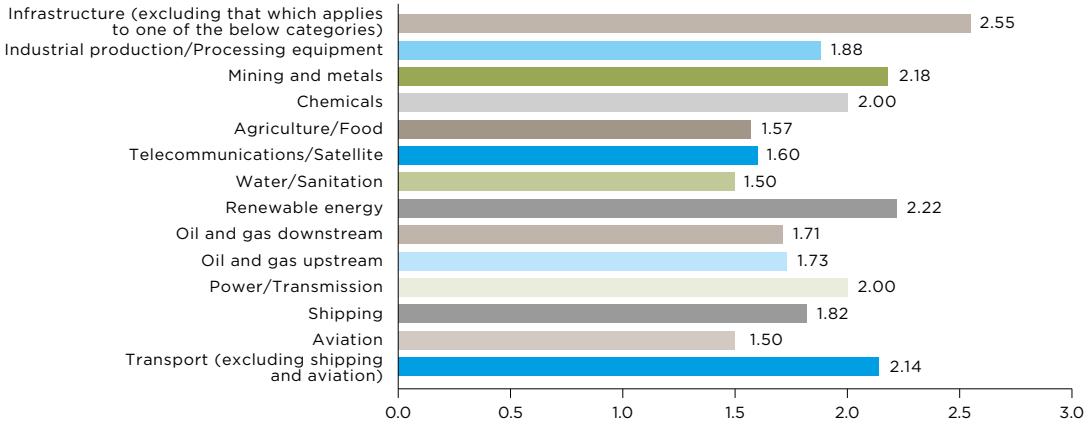


**Figure 78: Top Sectors for Export Finance**




*Participants were asked to list their top three sectors and each sector was then given an average weighting.*

### To Lend or Not to Lend

Since the global financial crisis, the role of export credit agencies (ECAs) as direct lenders within export finance transactions has been consolidated. TXF's Export Finance Market Status report 2014 found that ECA direct lending accounted for just over a third of all ECA-backed financings at nearly US$21 billion last year.

In this survey, respondents largely felt that direct lending was only necessary in specific circumstances (40%). More than one third felt it either provided unhealthy competition or was no longer necessary, while a quarter deemed it to be a necessary intervention overall.

These figures show a divergence in opinion among stakeholders on the role of ECAs and direct lending that is much in line with last year's findings – and a debate that shows no sign of abating.

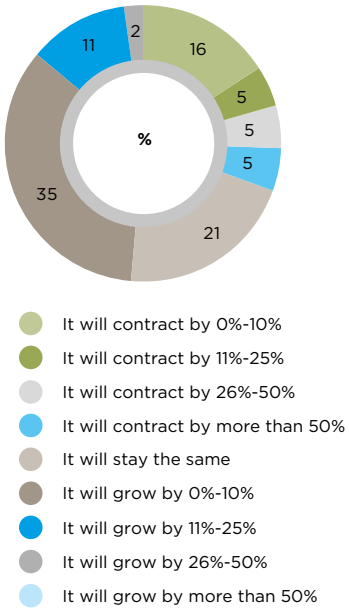
### Renewables Rise but Oil & Gas Still Leads the Way

There has been a distinct rise in the number of export finance professionals who deem renewable energy to be one of their top three sectors. It was identified as a top three sector by a quarter of respondents – up from just 9% last year.

The most dominant sector was still oil and gas, when combining upstream and downstream, with the sector figuring in 42% of respondents' top three sectors. The other standout sectors were as follows: industrial production/processing equipment (37%) and shipping, power/transmission, mining, metals and infrastructure (all 26%).

Following on from that, Russia leads the way in terms of regions, as 49% of respondents ranked it their number one borrower market. Brazil was second, although some way behind at 12%. Turkey was the third most popular; slightly behind Brazil with 10% of professionals confirming it was their top borrower destination.

**Figure 79: Export Finance Market Predictions for 2015**




### Sanctions Continue to Bite

In spite of Russia's prominence in the export finance market, one of the key findings of this year's survey was the impact that sanctions, and the fear of sanctions, were having on financiers. When asked for their top three most prohibitive factors to doing export finance in new markets, 40% identified sanctions, making it the third most cited barrier, behind legal and regulatory hurdles (63%) and political instability (42%).

These findings underscore the close relationship between geopolitics and export finance, particularly at a time when appetite for new-markets business is high. Only 12% identified a concentration on currently engaged markets as being one of the primary reasons for not doing business in new markets this year, down from 21% in last year's survey.

Also down on last year's survey is the number of respondents who identified cultural issues, including language, as being a barrier (0% this year versus 10% last year), reflecting a continuing expansion of banks' and export credit agencies' overseas divisions and international personnel.

Another key factor in terms of the provision of export finance in new markets is the capacity of ECAs. In light of this, TXF asked respondents to identify the ECA they worked with that they felt was most efficient, and that which was the most improved.

Euler Hermes was voted top in terms of efficiency in 2014. This efficiency was put to strong use, moreover, according to figures from TXF Data – which show that the German ECA guaranteed just over US$7 billion worth of financings in 2014.

UK Export Finance (UKEF) was deemed to be the most improved ECA last year, a reflection of the agency's much increased product offering and more streamlined approach since the takeover of David Godfrey as new chief executive officer.

### Cautiously Optimistic, but Displaying Signs of Nerves

The export finance industry continues to be in a state of flux, with new entrants and new regulations still to make their full mark. Given this, there is an understandable uncertainty as far as forecasting goes for what will happen to the market in the next 12 months.

The most common sentiment is that the market will grow in 2015, with nearly half of the respondents predicting this. Of those, most feel it will grow by 10% or less.

However, there is a substantial amount of people who feel the market will either contract (30%) or stagnate (21%).

These signs of nerves reflect the key role other factors already identified, such as Basel III pricing and the role of institutional investors, are likely to play in shaping the export finance landscape over the next few years.

# BUSINESS TRENDS IN EXPORT INSURANCE

**Export Credit Insurance Resilient, Showing Steady Growth in 2014**

Volumes of export credit insurance reported for 2014 by Members of the Berne Union, the International Union of Credit and Investment Insurers, increased by 4% to reach a total amount of US$1.875 trillion.

Out of this total business volume, more than US$1.7 trillion represented short-term (ST) export credit insurance, while medium and long-term (MLT) cover provided by official export credit agencies amounted to just over US$166 billion.

Against a background of volatile economic developments globally, considerably weakening energy and commodity price levels and increasing geo-political risk hot spots, export credit insurers have impressively demonstrated the resilience of their commitment.

This business evolution accentuates the growing awareness of exporters and importers about enhancement effects and the trade facilitating role as delivered by the export credit industry over the past years, with Berne Union members supporting about 10% of international trade in 2014.

Total claims paid by Berne Union members during 2014 amounted to US$4.432 billion, a slight increase compared to the previous year. While ST claims modestly decreased, MLT claims moderately increased.

Since the beginning of the global financial crisis in 2008, Berne Union members have paid approximately US$28 billion to exporters to compensate them for losses suffered due to defaults by buyers or other obligors.

Thus Berne Union members have provided ample and flexible risk capacity to support international trade transactions and to foster sustainable economic growth.

**4.432**

**US$Billion**

**Claims paid by Berne Union members during 2014**

### Short-term Business – Solid Growth, Still in a Good Shape but Growing Price Pressure

Short-term business represents insurance of exports with repayment terms of less than one year – often 30, 60 or 90 days. These transactions are typically shipments of consumer goods, with the movements of ST export credit insurance closely linked with the ups and downs of the broader global economic environment.

The volume of ST export turnover insured by Berne Union members grew by 4.1% in 2014 and reached US$1.709 trillion. This is significantly higher than the average growth rate for international trade during the past year. The rising demand may indicate a spreading awareness of the benefits resulting from the use of risk mitigation products to protect international sales transactions.

To support these exports, the insurance capacity provided by Berne Union members, measured by the amount of credit limits approved and granted to exporters at a given point in time, stood at over one trillion US$ throughout 2014. At the end of the year, the capacity reached US$1.051 trillion, 4% below the highest levels ever recorded in 2013. Achieving turnover growth while reducing risk limits demonstrates a greater efficiency and focus the short term credit insurance industry.

ST claims paid by Berne Union members to indemnify exporters for defaults on their trade receivables rose from US$1.913 billion in 2013 to US$2.019 billion in 2014. While this 5.5% increase is slightly higher than the 4.1% turnover growth rate of the business the overall default to turnover ratio of 0.118% continues to reflect sound underwriting practices. For most of the membership, ST claims paid have actually remained relatively stable. The total claims figure certainly includes a number of larger defaults that mainly occurred in some of the current risk hot spots.

The strong competition among Berne Union members and from alternative providers for export risk protection such as trade finance banks and multilateral institutions resulted in a more favourable pricing environment for exporters. While not all members report premium data, the trend is pretty compelling: the ST loss ratio (i.e. claims paid as a share of the premiums earned) for Berne Union members continues to increase, now standing at about 56%, after 49% in 2013 and 48% in 2012.

When comparing the loss ratios of private commercial export credit insurers to that of ECAs, as in previous years, also in 2014 the ECAs recorded higher ST loss ratios than their private peers. A credible cause is that, by mandate, the ECAs operate in a special niche to support their national exporters, in particular where commercial insurance cover might otherwise be difficult to obtain.

The highest volumes of ST claims paid per country in 2014 resulted from defaults in Venezuela (US$173 million), USA (US$165 million), Italy (US$110 million), Brazil (US$90 million), and Russia (US$76 million).

Many Berne Union members paid claims due to commercial buyer defaults in the United States and Western European countries, representing the largest international trade volume countries and the largest exposures for Berne Union members. Supported trade and thus exposure of members to Brazil has also remained on a relatively high level in recent years.

In 2014 only a few Berne Union members provided ST protection for exports to Iran, whereas a significant amount of claims paid earlier could be recovered from Iran. The impact of the declining energy price level has impacted the risk capacity for Venezuela which was severely restricted in 2014. Due to the tightening of the sanctions imposed respectively the impact of the ongoing conflict, preparedness to underwrite risk in Russia and Ukraine were also curbed.

**Preparedness to underwrite risk in Russia and Ukraine were also curbed, due to tightening sanctions imposed**

**Figure 80: Short-Term Export Credit Insurance**

| MILLION US$ | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|---|---|---|---|---|
| Export turnover covered | 843,719 | 975,262 | 1,126,721 | 1,296,878 | 1,122,608 | 1,257,794 | 1,495,227 | 1,538,609 | 1,641,823 | 1,709,246 |
| Claims paid | 702 | 783 | 1,007 | 1,128 | 2,418 | 1,508 | 1,323 | 1,827 | 1,913 | 2,007 |

### Medium and Long-Term Business – Demand for ECA Cover Still Above Pre-Crisis Levels

The MLT statistics of the Berne Union capture export insurance coverage provided by official state-backed ECAs only. Alongside insurance business, some ECAs in the Berne Union also provide direct financing, which is also reflected in the data and represents approximately 7.7% of the total business reported, after 8.75% in 2013 and 12.87% in 2012.

MLT export credit insurance covers exports of capital goods. These are transactions with longer repayment terms of typically 5-7 years, and up to 10 years or even 15 years for renewable energy and certain infrastructure investments in some cases. Most of the business is conducted with banks as the insured.

## No new cover for Iran has been issued in 2013 and 2014

The total portfolio of MLT transactions insured by Berne Union ECAs reached US$ 651 billion at the end of 2014, representing a slight decrease of 0.9% versus 2013 when the highest ever exposure was recorded.

New export credits covered in 2014 increased by 3.1% to US$166 billion. This is still higher than the volume of new MLT business before the global financial crisis, yet lower than the record years 2009 and 2011 (US$191 billion in both years), indicating that financial markets have stabilized.

The slight decline of the overall portfolio size indicates that orderly repayments from the early financial crisis years have commenced to flow. Thus MLT ECA business is expected to return to a more normal level. Whether there will be a new normal at higher levels than before 2008 remains the big question; an increasing share of non-OECD ECAs, especially by China, however, can already be observed.

In 2014 new business for the large ECAs in OECD countries, with very few exceptions, has decreased or remained flat. This is less a result of a change in cover policy by the ECAs but reflects the underlying deal flow which appeared somewhat suppressed, at least partially as an impact of the sanctions in Russia where new business declined by 20% when compared to 2013.

Claims paid to customers by ECAs under MLT transactions amounted to US$2.427 billion in 2014, a minimal reduction of 0.5% when compared to 2013 defaults. The highest amounts of claims paid per country were due to defaults in Iran (US$916 million), Russia (US$296 million), Ukraine (US$187 million), USA (US$172 million), and Kazakhstan (US$97 million).

The background to the various claims situations is specific and differs significantly from country to country and case to case. A number of Berne Union ECAs have been affected by the Iranian sanctions situation, with obligors experiencing severe difficulties to effect payments abroad. While claims payments for exposure in Iran are almost exclusively linked to long term transactions entered into prior to the imposition of the sanctions, almost no new cover for Iran was issued in 2013 and 2014.

In Russia, although the environment and the cause for defaults are largely different, a number of ECAs have been affected by increasing losses; here the claims payments appear to be closely linked to the weak price levels for energy and mining resources. Whereas the relatively high number of claims in Ukraine seems to be directly linked to the unresolved conflict and as a result Ukraine's shrinking national economy.

However, the diversity of causes triggering claims in multiple countries illustrates the necessity for official support in gap areas that may affect exports across the globe. The support of ECAs appears to be more than ever crucial to help banks and exporters trade internationally.

**Figure 81: Medium Long Term Export Credit Insurance**

| MILLION US$ | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|---|---|---|---|---|
| New business covered | 104,241 | 126,891 | 142,120 | 153,591 | 190,589 | 173,393 | 191,428 | 181,808 | 160,901 | 165,795 |
| – of which insurance | 100,433 | 119,321 | 132,522 | 142,225 | 164,038 | 161,529 | 177,238 | 158,411 | 146,822 | 153,831 |
| – of which lending | 3,808 | 7,570 | 9,599 | 11,366 | 26,552 | 11,864 | 14,190 | 23,397 | 14,079 | 11,964 |
| Claims paid | 2,115 | 1,913 | 1,245 | 1,128 | 3,004 | 1,836 | 2,457 | 2,608 | 2,440 | 2,427 |

### Outlook – the Export Credit Insurance Industry Remains Resilient

Export credit insurance has proven to be very robust during the past years, both from a private risk capital as well as from a public ECA mandate perspective. With 2014 certainly a year of growing geo-political risk and great uncertainty for natural resources producers, the industry did deliver and appears to be covering a higher share of international trade than before.

Yet the rather continued pressure on pricing is a warning signal. While part of the cause lies in the low claims ratios, in part it is also the market's ample capacity of insurer's and bank's capital seeking investment. The judges are still out as to whether this situation is sustainable.

Past loss events serve as a reminder that pricing of risk mitigation products needs to be covering for expected as well as unexpected losses, which may well rise given the current global situation where more erratic claims trends in markets like Russia or the now stagnating Brazil should not come as a surprise.

Nevertheless, a part of the demand is also driven by growing awareness of the inherent enabling and facilitating features provided by export credit insurance for international trade flows. A lot of work remains to be done with regulators to ensure regulatory discrepancies and incoherencies will be addressed. While in particular banks would benefit from fairer treatment when using trade credit insurance products, this will also contribute to preserve the robust operating models of many Berne Union members and their exporting clients.

The trade credit industry is intrinsically a global industry due to the nature of its risk. Members of the Berne Union are ready to contribute to a sustainable global economic development.

**Erratic claims trends in markets like Russia or the now stagnating Brazil should not come as a surprise**

# ANALYSIS OF GLOBAL TRADE FINANCE GAPS

The Asian Development Bank (ADB) has kindly provided the Analysis of the Global Trade Finance Gaps, based on the ICC Global Survey on Trade Finance 2015 statistics collected.

## Key findings

- 53% of respondents perceive a shortfall of trade finance globally
- Rejection rates of trade finance proposals highest in Asia (31%), Africa (18%) and Russia/CIS (15%)
- SMEs trade proposals rejected 53% of occasions whereas large corporates accepted 79% of occasions
- 80% of respondent banks maintained or increased overall trade credit lines
- 75% agreed MDBs help narrow the trade finance gaps
- 72% of respondents felt ECAs help narrow the trade finance gap
- 80.32% of respondents felt that a lack of harmonization between jurisdictions is a problem
- 70% of respondents reported declining transactions due to AML/KYC issues
- 45.8% reported terminating correspondent relationships due to AML/KYC issues
- 27% of reported terminated relationships had no evidence of suspicion or non-compliance with anti-financial crimes regulations
- Sanctions on Russia resulted in terminated correspondent relations, fewer proposals and higher rejection rates
- 93.1% of respondents expect compliance requirements to increase in 2015

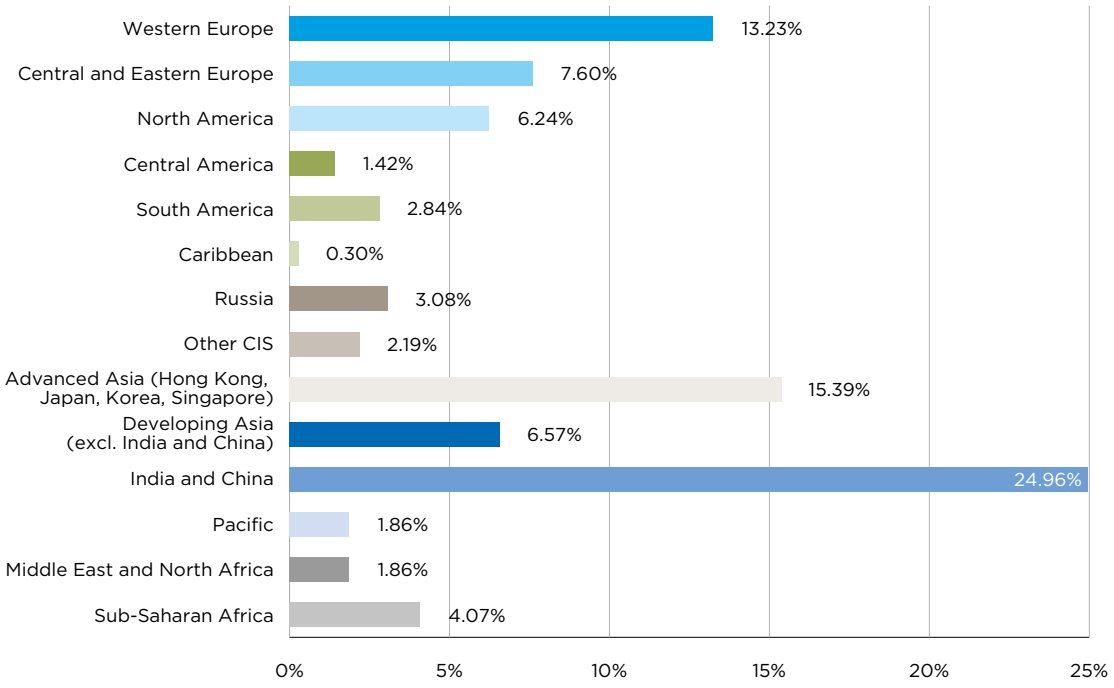
## Overview

Emerging economies are depending on trade as an engine of growth. Where trade finance shortfalls exist, export growth is constrained. The trade finance gap questions in the ICC Global Survey are intended to help understand where gaps exist, both geographically and in terms of client types, and why.

This year, questions were adjusted to add more depth on the issue of financial crimes compliance measures. Last year's survey had identified compliance as the primary constraint to trade finance for emerging markets and SMEs. The new questions sought to provide more detail. In addition, a geographical selection for the Pacific region was included.

Since the surveyed population is different from year to year, it is difficult to make comparisons with previous years' results. In general, trends identified last year continue to move in the same direction. This suggests that the international trading system continues to operate smoothly, but also that regulatory requirements and lack of harmonization between jurisdictions continues to produce pockets of underserved populations.

**Figure 82: Proposed Transactions by Regions**



## Trade Finance Availability

Of surveyed banks, 53% reported that they perceive a shortfall of trade finance globally. This is roughly in line with last year's survey results. The data reflects some variation in regional gaps, in particular due to sanctions on Russia.

Geographically, rejection rates of trade finance proposals (declined transactions) remain highest in emerging markets: Asia (31%), Africa (18%) and Russia/CIS (15%) registered higher rejection rates than more established markets in Europe and North America. Within developing country regions, the highest sub-regional rejection rates are in the more developed markets. For example, within Africa, Middle East and North Africa record higher rejection rates than Sub-Saharan Africa.

Sanctions on Russia were reflected in both fewer proposals (3.2% of the total) and a moderately higher rejection rate (10%) than last year.

India and China again reflected both the highest number of trade finance proposals (26% of the total) and the highest rejection rate (16%). Rejections are slightly lower than those reported last year. SMEs continue to be disadvantaged in trade finance transactions. Banks report that 45% of proposed trade finance transactions are submitted by SMEs, 39% by large corporates and 14% by multinationals. However, in contrast to large corporates which have 79% of their proposals accepted, SMEs are rejected 53% of the time. To compound problems, 68% of banks report that, among firms, SMEs are the most negatively impacted by more stringent regulatory compliance requirements. Since compliance requirements are expected to increase in 2015, we can expect SMEs to remain underserved.

Continuing the positive trend of last year, more than 80% of responding banks either maintained or increased their credit lines in 2014. The majority of banks reported increasing the number of credit lines to both corporate clients (62%) and financial institutions (57%). About 60% of banks reported that the level of the increase in credit lines offered was in the range of 25%, while 15% of banks reported more substantial increases of 25-50% to corporate clients.

Banks were positive about the role of multilateral development banks in addressing trade finance shortfalls. 75% of respondents agreed that MDBs help narrow trade finance gaps at least to some extent. Export credit agencies were also narrowing gaps according to 72% of respondents.

**Figure 83: Proposed Transactions by Client Segment**

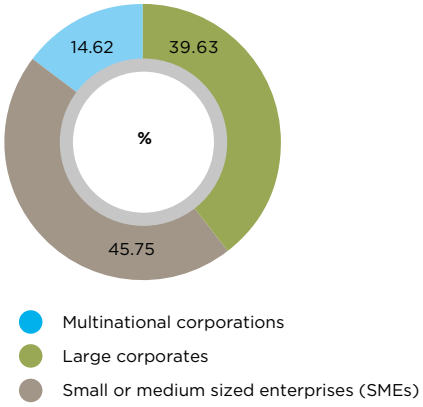


**Figure 84: Rejected Transactions by Regions**

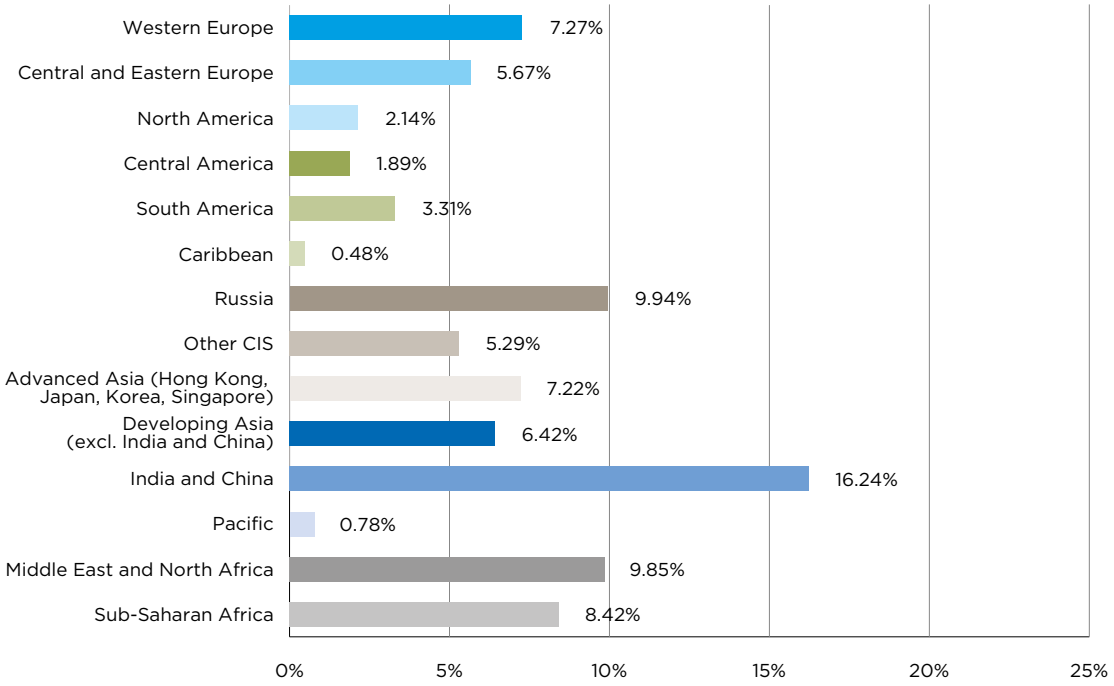



**Figure 85: Rejected Transactions by Client Segment**

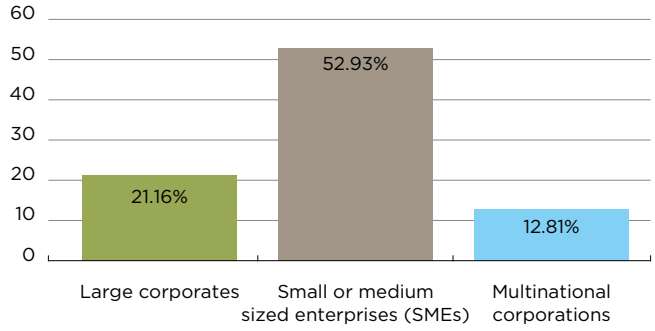



**Figure 86: Percieved Shortfall of Trade Finance Globally?**

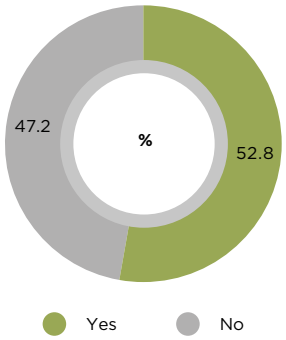


**Figure 87: Extent to Which Trade Finance Programmes of Multilateral Development Banks Narrow Market Gaps for Trade Finance**

"0" means "not at all" and "4" means "to a very great extent".

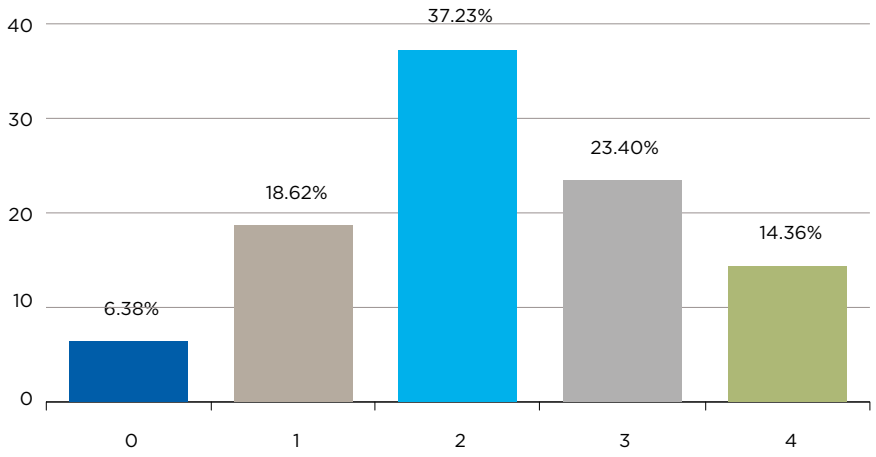



**Figure 88: Extent to Which ECAs Narrow Market Gaps for Trade Finance**

"0" means "not at all" and "4" means "to a very great extent".

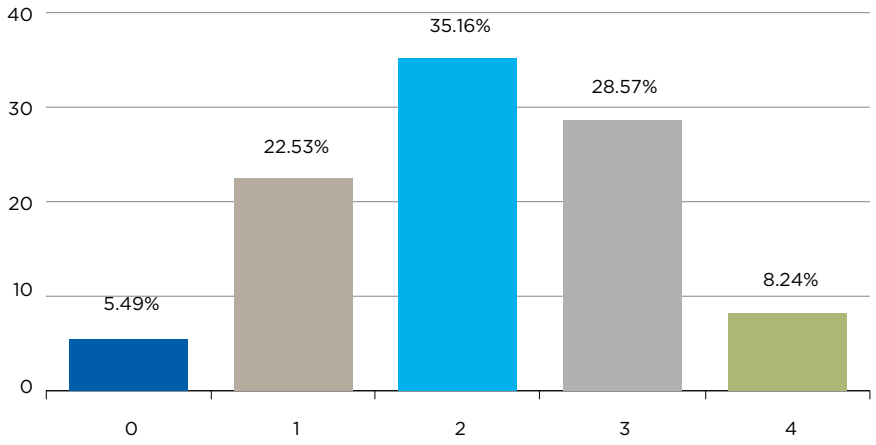
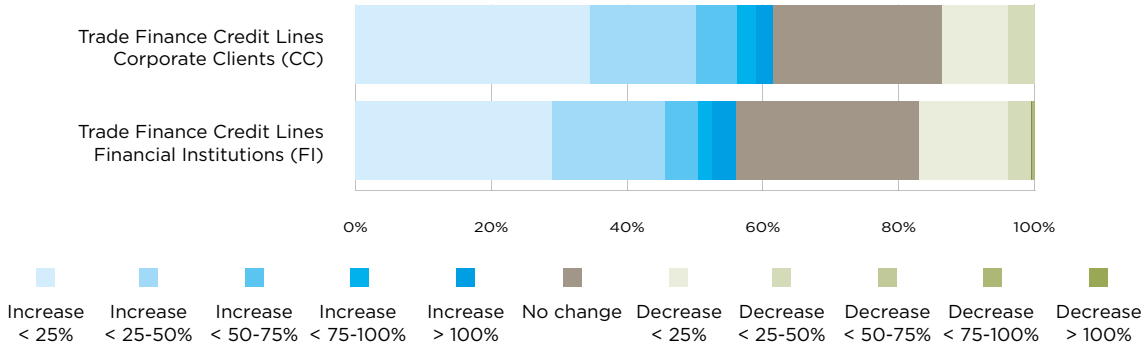



**Figure 89: Trends in the Level of Increase or Decrease in Trade Finance Credit Lines Offered by Banks**



### Impediments to Trade Finance

Impediments to trade finance reflected the same key constraints as last year, but with a higher percentage of respondents (81%) citing anti-financial crimes compliance requirements as a significant impediment. Other constraints reported as significant by more than 60% of respondents were related to the more traditional credit risk issues, including low ratings of countries (75%), issuing banks (71%) and companies (62%). Frequent write-in responses also mentioned lack of bank staff experienced in trade finance as a hindrance.

In addition, 53% of respondents felt that the lack of harmonization between jurisdictions is a 'great' challenge to the trade finance industry. If we include those who felt it was also 'to some extent' a challenge, this captures 80% of respondents. This reflects the widespread difficulties posed by differing legal and regulatory requirements, which multiplies both the cost and complexity of compliance.

Of those banks which reported decreasing credit lines to corporate clients (14% of respondents) and financial institutions (17% of respondents), the most prominent reason given (41% of respondents) was 'more stringent criteria being applied'. Only 11% reported that this was due to 'exiting markets'.

**Figure 90: Impediments to Trade Finance**

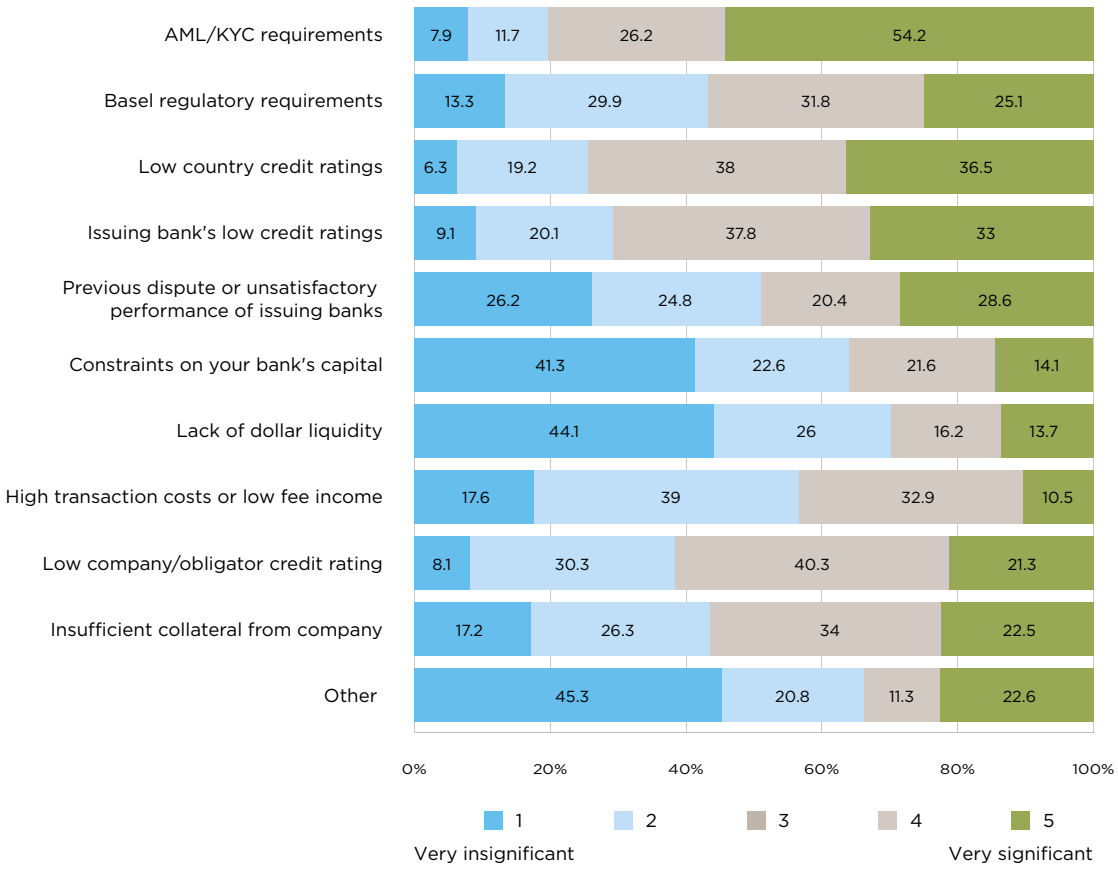
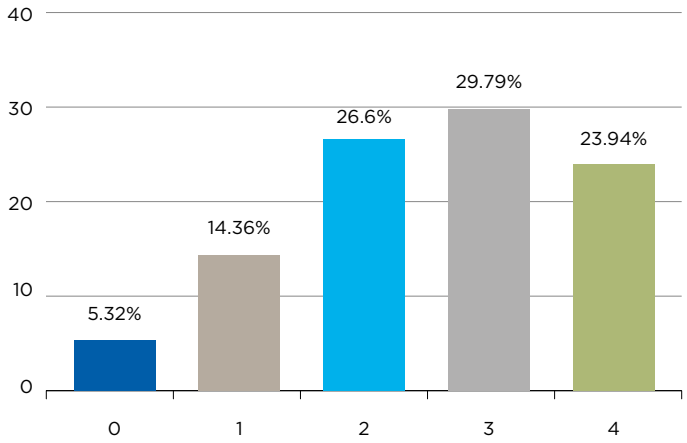


**Figure 91: Lack of Harmonization of Compliance Requirements between Jurisdictions a Challenge to the Trade Finance Industry**

"0" means "not at all" and "4" means "to a very great extent".




## The impact of compliance requirements

Questions on this topic were intended to build some context into the indication that anti-financial crimes compliance requirements, including AML/KYC, was a 'significant' impediment to trade finance.

In this year's survey, 70% of respondents reported declining transactions due to AML/KYC, while 46% reported terminating correspondent relationships for the same reason. Correspondent banking is particularly important for trade in emerging markets. Thus, the proportion of terminated correspondent relationships, which has increased over last year's responses, may indicate a broader chilling effect on the country and customer segments in which this is occurring.

The regions where increasing compliance costs have had the greatest impact on terminating correspondent relationships include Africa and Russia/CIS. In both cases, about one third of respondents reported that these regions had been impacted to 'a great extent'. 37% reported that India and China had been impacted at least 'to some extent'.

For both banks which had terminated relationships and those which had experienced termination of relationships, more than a quarter (26% and 27% respectively) claimed there was no evidence or suspicion of 'non-compliance' with anti-financial crimes regulation.

Finally, even with increasing attention to the challenges of balancing compliance requirements with policy objectives such as promoting trade in emerging markets, compliance requirements are increasing. 93% of respondents expect compliance requirements to increase in 2015. Responses suggest that this is likely to further affect those markets which are already negatively impacted by existing requirements.

**Figure 92: Termination of Correspondent Relationships (2011 to Present) due to the Increasing Cost or Complexity of Compliance (Including More Stringent AML and KYC)**

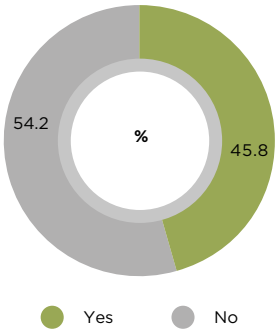



**Figure 93: Termination of Correspondent Relationships by Other Banks (2011 to Present) due to the Increasing Cost or Complexity of Compliance (Including More Stringent AML and KYC)**

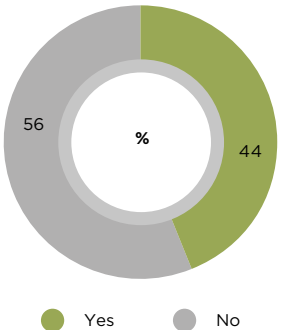



**Figure 94: Declined Trade Finance Transactions due to KYC/ AML Issues from 2011 to resent**

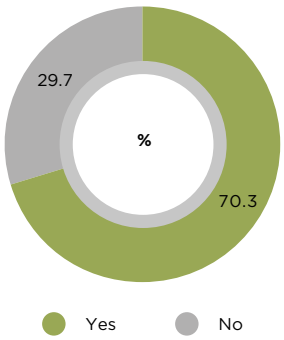


**Figure 95: Regions and Level of Impact in Which Correspondent Relationships Were Terminated from 2011 to present due to the Increasing Cost or Complexity of Compliance (Including More Stringent AML and KYC)**

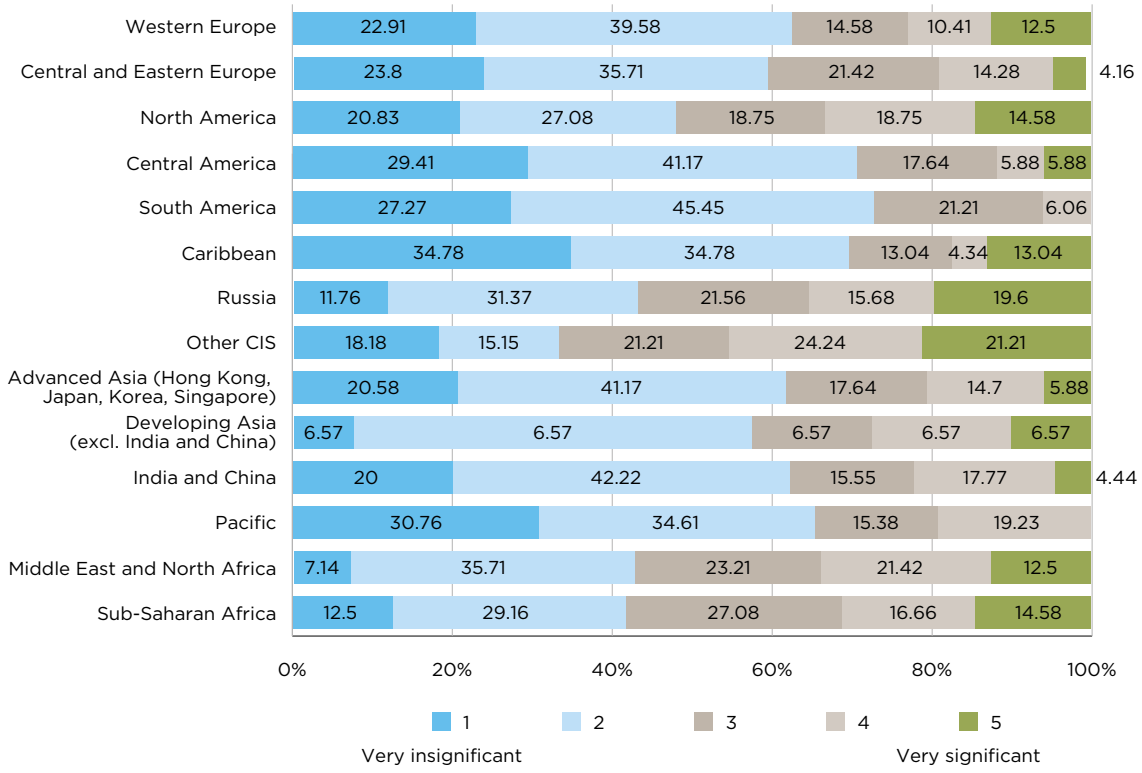



**Figure 96: Customers Most Impacted by More Stringent Compliance (AML and KYC) Requirements**

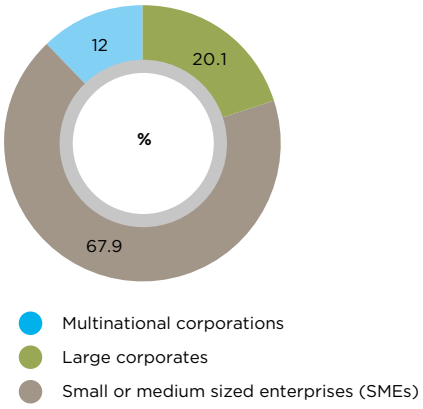
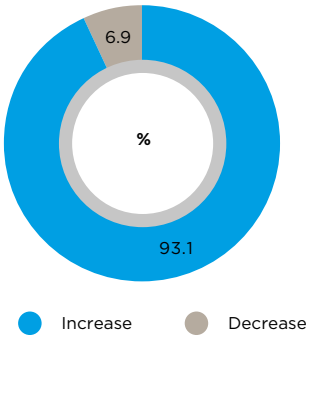



**Figure 97: Expectations for 2015 in Terms of Compliance Requirements for Banks in Trade Finance**



HIGHLIGHT

# ENABLING INCLUSIVE AND SUSTAINABLE GROWTH THROUGH SME COMPETITIVENESS

The interventions at this year's Financing For Development conference and the ongoing intergovernmental discussions on the post-2015 Sustainable Development Goals (SDGs) mirror what policymakers have been arguing for years – small and medium enterprises (SMEs) are not only the backbone of the economy but also an integral element to sustainable economic development. But what exactly is an SME and how do they contribute to inclusive growth?

## SMEs and Their Contribution to Development

By number, SMEs constitute over 95% of all firms and account for approximately 60% of employment globally. The term SME encompasses a broad spectrum of definitions which vary across countries and regions as well as across international organisations and financial institutions. The definitions generally have in common that small firms (i.e. businesses which employ twenty or less individuals) serve the local economy, use basic technologies in the production of their goods and services, and have a turnover and assets of the order of US$100,000. Medium-sized companies may employ between twenty to fifty people, and are likely to be focused on serving the national economy. Turnover and assets are usually in the region of millions of dollars. These companies are most likely to use rather competitive production methods and be relatively well equipped to join existing international value chains either by direct exports or by serving large/foreign firms in the domestic market.

## The Missing Middle

Unfortunately, these trade-ready medium-sized firms account only for a small share of total SMEs while micro and small enterprises, often operating in informal labour-intensive sectors, present the overwhelming bulk. Studies suggest that this may open the door to inefficiencies and non-competitive behaviour as it splits the private sector into two segments: A large number of small, often micro enterprises on the one hand; and a handful of very large enterprises on the other hand - a phenomenon often referred to as the "missing middle". Recent research points out that this missing middle is likely to be caused by structural issues in taxation and policies around access to finance which adversely affect medium-sized firms and creates disincentives for small firms to grow. Indeed, medium-sized firms are often just large enough to be taxed but too large to be eligible for micro finance schemes. Small enterprises, in contrast, often chose to stay small to avoid regulations and taxes while being eligible for micro finance schemes. Large firms, on the

other hand, have the capacities to develop sophisticated business models that maximise their access to capital and minimise their fiscal obligations.

Such structural challenges perpetuate the existence of the productivity gap across firm sizes which is found to be particularly large in developing countries. While small firms in Germany, for instance, achieve around 70% of the productivity of large firms, their Brazilian counterparts realise less than 30%. In order to assist firms and countries in boosting competitiveness and closing this gap, the International Trade Centre's (ITC) forthcoming "SME Competitiveness Outlook" has developed a conceptual and empirical framework that captures firms' capacity to compete, to connect and to change at the firm level, the immediate business environment and the national economy. Analysing the findings confirms that access to finance continues to present a major challenge to SMEs' business operations. In particular, the lack of financing contributes to impeding firms' ability to access information, skilled labour and technology – all three being prerequisites for the successful integration into international value chains (IVCs) and realising new market potentials.

## Improving the Business Environment for SMEs and Enhancing Their Competitiveness

The International Trade Centre tackles this issue from three different angles: First, ITC provides practical and comprehensive guides for SMEs, such as for instance, "How to Access Trade Finance" and "Islamic Finance". Second, rather than providing direct access to finance, ITC assists SMEs in strengthening their competitiveness which in turn increases their attractiveness to financing institutions and consequently eases SMEs' access to finance.

Third, ITC and its extensive network of partner Trade and Investment Support Institutions (TISIs) and Trade Promotion Organizations (TPOs) continue implementing programmes that minimise trade costs at the immediate business as well as national economy level. One area of work is the logistic efficiency which is as important as production efficiency. ITC Trade Facilitation Programme's mission is to increase the competitiveness of the private sector, especially small and medium-sized enterprises (SMEs), by building their capacity to comply with cross border procedures. ITC also supports businesses to effectively participate in the policy design and implementation through public-private dialogue and supports policymakers to ensure that policy reforms factor in the needs and priorities of business. ITC is working with developing and least developed countries enabling them to implement obligations ensuing from Trade Facilitation Agreement in a business friendly manner. Such support helps in reducing direct and indirect trade transaction costs and improving competitiveness. More specifically, it provides solutions for bridging the soft trade infrastructure with actual situation, and facilitating SMEs' ability to connect to global value chains.

As part of the monitoring and evaluation exercise conducted under the WTO and OECD's Fifth Global Review of Aid for Trade 2015, private companies were asked about their experience with trade costs and about their priorities for future trade cost reductions. The top priority for SMEs is access to information about export opportunities – an area in which ITC has a longstanding history of success. Building upon Trade Map (http://www.trademap.org/) and Market Access Map (http://www.macmap.org/), the International Trade Centre is currently developing Export Potential Map – a user-friendly online application that will not only allow stakeholders to match strongly performing export products with accessible high demand markets but also to diversify the existing export basket and explore new opportunities. This is complemented by ITC's Standard Map (http://www.standardsmap.org/), which currently covers 170 standards initiatives, applicable to more than 80 sectors and 180 countries, and ITC's Non-Tariff Measures Survey (http://ntmsurvey.intracen.org/) which covers more than 14,000 companies in 30 developing countries. The combination of these ITC market analysis tools allows SMEs to reduce market access and trade costs at the firm level. Another example is assistance to SMEs in the area of quality management and sustainability standards, including building the capacity of SMEs to comply with standards and regulations.

ITC's work goes beyond SME-level activities to the immediate business and national environment. Over the last 50 years, the International Trade Centre has developed a far reaching network of partner TISIs and TPOs which act as intermediaries between the private sector, especially SMEs, and the government. Through SME-focused technical assistance and capacity building initiatives, ITC assists its partners in the field to reduce direct and indirect trade transaction costs, pass on the benefits to the private sector and deepen regional integration.

The International Trade Centre will continue working in this direction, to strengthen SMEs' export activities, boost their competitiveness and facilitate an immediate business environment in which they can flourish, with the overall goal of promoting sustainable and inclusive economic growth.

# MULTILATERAL DEVELOPMENT BANKS (MDBS)

## Innovation in Action!

2014 was a challenging year for trade finance in emerging and developing markets. Many international commercial banks continue to pull back, de-risk and consolidate their exposures. With country risks in a state of flux across the globe, the role of the multilateral development banks in keeping supply chains financed is more important than ever. The innovative trade finance models of the MDBs have been a lifeline for emerging markets and second- and third-tier banks, to support their growing base of small- and medium-sized customers during this time of economic turmoil.

There is no doubt that with the increased pressure for higher risk capital, confirming banks' demand for MDB support will accelerate further.

An interesting phenomenon is that there had not been any write-offs or losses at the time of writing this report, although the MDBs`focus is on high-risk markets.

Furthermore, with the global acceptance that fostering international trade right down to grassroots SME level is mission critical for economic development, we can expect more innovation from the MDBs.

In fact, it is now clear that we will soon have newly established MDBs, active in the trade development, supply chain and infrastructure development space.

**The innovative trade finance models of the MDBs have been a lifeline for emerging markets and second-and third-tier banks**

**Figure 98: MDB Trade Facilitation – Summary of Coverage 2014**

| | EBRD | IFC | IDB | ADB |
|---|---|---|---|---|
| Number of Countries of Operation | 26 | 90 | 21 | 17 |
| Programme Commencement | 1999 | 2005 | 2005 | 2004 |
| Number of Trade Transactions since Commencement | 17,300 | 40,000 | 5,271 | 11,308 |
| Value of Transactions since Commencement | EUR11.8 billion | US$38.6 billion | US$5.03 billion | US$21.7 billion |
| Number of Confirming Banks | 800+ | 1,100 | 300+ | 139 |
| Claims to Date | 2 – no write-offs | zero | zero | zero |

## European Bank for Reconstruction and Development (EBRD)

### Background and Markets

The significant price decrease of oil since mid-2014 as well as other commodity prices had a double-edged sword effect for the EBRD region and overall driving the region's growth down. Commodity exporters are impacted negatively; particularly the largest country in the region, Russia, where the oil price collapse is compounding the impact of already poor investor confidence, long-run structural problems and increasingly biting economic sanctions. The ensuing negative spillovers are already affecting the economies in Eastern Europe, the Caucasus and Central Asia that have strong economic ties with Russia as well as other commodity exporters. In countries such as Armenia and Belarus currencies came under pressure as the rouble tumbled further contributing to already weak import volumes and Ukraine is experiencing a deep recession because of its geopolitical tensions and subsequent effects on the economy.

Other commodity exporting countries such as Kazakhstan and, to some extent, Azerbaijan and Turkmenistan, have also been adversely impacted by the drop of oil prices. At the same time, lower export demand and remittances from Russia and the decline in consumer and investor confidence weighed on the growth rates of many commodity importers. Georgia, whose economy relies to lesser extend on either Russia or commodities, was the only country in the Caucasus and Central Asia region where growth actually accelerated.

In South Eastern Europe, Serbia entered a recession in 2014 as widespread damage from floods in May 2014 compounded existing economic weaknesses, and growth slowed down significantly in Montenegro towards the end of the year partly on account of delayed investment agenda. In contrast, sustained export expansion supported further growth in FYR Macedonia and a better than expected performance in Bosnia and Herzegovina, which also suffered major flood damage in May 2014.

The economic situation looks better in Central Europe and the Baltic countries which are starting to benefit from the nascent recovery in the Eurozone supported by the ECB's quantitative easing. Particularly in Poland, the regions' largest economy, household consumption has been supported by a further fall in unemployment rate to a level last seen in 2009, accompanied by a rise in real disposable incomes. The situation is also brighter for countries in the southern and eastern Mediterranean region on the back of terms of trade gains linked to lower oil prices, some reforms and improving confidence in the region's largest economy, Egypt.

### Summary of Activity (Volumes and Values 2014)

Generally, the availability of trade finance limits from foreign commercial banks remains a significant impediment. Increased cost of compliance and higher capital charges on trade exposures have prompted commercial banks to reduce their presence in many of the EBRD's countries of operation. Therefore, particularly smaller and regional private banks request support under the EBRD Trade Facilitation Programme (TFP).

The TFP aims to promote foreign trade to, from and within Central and Eastern Europe and the CIS as well as in Cyprus, Egypt, Jordan, Morocco, Tunisia and Turkey. Through the programme, the EBRD provides guarantees to international confirming banks and factoring companies, taking the political and commercial payment risk of international trade transactions undertaken by banks in the countries of operations and the recipient countries (the issuing banks). The programme can guarantee any genuine trade transaction to, from and within these countries of operations. 106 issuing banks in the region participate in the programme with limits exceeding EUR 1 billion. In addition, the TFP includes over 800 confirming banks throughout the world.

In 2014 the programme facilitated 1,756 trade transactions for a record total amount of EUR1.3 billion.

### Summary of Developmental Impact

TFP cover was particularly important for trade finance transactions with larger amounts and longer tenors in Belarus and Ukraine while in smaller countries such as Armenia, Azerbaijan, Georgia and Moldova the TFP supported a higher number of small transactions with very short tenors, underlining particular support through the Programme for SME-sized exporters and importers. In Armenia, for example,

**The availability of trade finance limits from foreign commercial banks remains a significant impediment**

**Banks often lack not only the necessary technical skills to execute documentary and structured trade-finance transactions but also have difficulty in promoting trade-finance solutions to their customers**

the average transaction amount was only EUR175,000 and the average tenor less than 180 days.

Intra-regional transactions within EBRD's countries of operation have long been a major focus of the TFP; and recent examples include the export of leather goods from Ukraine to Belarus, machinery from Bulgaria to Georgia and food products from Turkey to Azerbaijan. In 2014 the programme facilitated more than 400 such intra-regional trade transactions.

In addition to risk cover, the TFP provides technical assistance to banks with very limited or no trade finance experience. These banks often lack not only the necessary technical skills to execute documentary and structured trade-finance transactions but also have difficulty in promoting trade-finance solutions to their customers. Technical assistance is provided in the form of consultancy service and classroom-style training courses on topics such as UCP 600 rules, URDG rules or correspondent banking and legal issues concerning trade finance.

### Innovations in International Trade and Finance

In addition to classical types of technical assistance the EBRD has developed an online training course in cooperation with ICC covering all of the ICC international trade-finance products and Incoterm rules. The study programme is flexible and can be accessed for 12 months from the date of subscription. On completion of a training module, a student can request an ICC certificate of achievement for each module indicating the highest score achieved in each course assessment. Since the launch more than 700 trade specialists from over 170 banks across EBRD region have taken part in such an e-Learning Programme.

**Since the launch, more than 700 trade specialists from over 170 banks across EBRD region have taken part in such e-Learning Programme**

This partnership model using best practices in blended learning has been highly acclaimed across the trade finance industry with leading international banks providing scholarships and prizes to best performing graduates.

### Default or Claims Experience

Economies and subsequently banks in EBRD's countries of operation were affected by the financial crises of 2008/2009. During this period, the EBRD's TFP was confronted with two claims under the programme from confirming banks for guarantees which covered trade from issuing banks in Kazakhstan and Ukraine. Both claims were settled immediately, and the EBRD is in the process of restructuring and recovering outstanding amounts.

### Trade Outlook for the Future

The EBRD's TFP will continue in 2015 to assist partner banks and exporters and importers in their trade finance activities. While the economic outlook for 2015 has strengthened in central eastern and south eastern Europe, the situation looks more gloomy in many of the CIS countries, particularly in Ukraine, which is experiencing a deep recession which is expected to continue for the rest of the year.

Taking into account that many foreign commercial banks and their subsidiaries in Eastern Europe and the CIS will have to further increase their capital or reduce their lending also in the light of new Basel III regulations, it is expected that the overall volume of available trade finance facilities will not increase significantly in 2015 as the cost of trade finance continues to increase.

Clearly, the important role played by the EBRD in supporting trade in its countries of operation will continue to play an essential role due to the ongoing challenging environment.

## International Finance Corporation (IFC)

### Background and Markets

This year, IFC celebrates the 10th anniversary of the launch of its first programmatic effort to support emerging market trade. Since the Global Trade Finance Programme (GTFP) began in 2005, IFC's support for emerging market trade flows has grown exponentially and its global network has expanded to include financial institutions and their customers in more than 150 countries in every region. IFC now offers a full suite of products that provide essential working capital to emerging market firms and propel goods through the economic value chain: from input financing for farmers to inventory and warehouse financing; from supply chain financing to pre-export and post-import financing for international shipments. Training is also available to banks and their customers through IFC's Trade Advisory Services programme.

### Summary of Activity

In the first year of the GTFP, the initiative supported global trade of nearly US$300 million. At present, IFC enables that amount through all of its trade and commodity finance programmes every five days, and the GTFP network has grown to include over 280 participating banks. Over the last two years, through its various programmes, IFC has backed emerging market exports and imports in excess of US$22 billion annually. In 2014, the largest share, US$14 billion, came from Portfolio Solutions products, which include risk-sharing facilities in banks' trade portfolios aimed at increasing trade finance and working capital for clients based in developing countries. Many facilities are targeted to facilitate the flows of critical commodities, such as agricultural goods and refined fuel imports, to promote food and energy security particularly in the world's poorest countries.

After 10 years, the GTFP continues to serve as IFC's flagship trade facilitation product. The programme, which offers up to 100 % cover on country and counterparty risk for transactions in 90 emerging markets, provided over US$6 billion in guarantees in 2014. Sub-Saharan Africa, where a record US$1.8 billion in transactions were financed, continued to represent the largest share, followed by Asia and the Pacific and Latin

**IFC now offers a full suite of products that provide essential working capital to emerging market firms and propel goods through the economic value chain**

America and the Caribbean (both with US$1.4 billion). The additions of issuing banks in the Democratic Republic of Congo, Myanmar, and Nepal broadened the network's footprint in fragile and conflict-affected countries. Further network expansions came through new relationships with financial institutions in Bolivia, Honduras, Lebanon, Romania, and Tanzania.

### Climate Change Mitigation and Equipment Finance

Through its trade facilitation efforts, IFC has taken a lead in helping the private sector confront the global challenge of climate change. As severe weather events and resource constraints disproportionately affect the poor, climate change threatens to reverse recent development gains, hampering economic growth and plunging people back into poverty. The Climate Smart Trade initiative works with IFC's bank partners to support trade of goods and services that enable their corporate clients to adopt energy-efficient technologies, cut carbon emissions, and ensure the sustainability of their operations and their supply chains. IFC can offer more favorable terms, including longer tenors, for guarantees covering equipment and projects that have clearly defined climate change benefits.

In the past year, IFC has provided crucial backing to emerging market countries to aid them in accessing cutting-edge renewable technologies. An IFC guarantee allowed Yunus Energy to import a wind power turbine from Nordex Germany, helping increase the supply of clean energy generated through wind farms in Pakistan. To assist the government of Honduras in keeping on track to meet an ambitious target – to generate 60% of domestic energy from renewable sources by 2022 – IFC supported the import and installation of solar panels that have already helped reduce carbon emissions by 79,000 tons. Other guarantees under GTFP enabled the import of equipment to expand a hydroelectric plant in Nepal, helping modernize the country's economic infrastructure and reducing a power supply gap that severely inhibits the productivity of local firms.

IFC has also moved to fill a market gap in trade finance for equipment and capital goods, which often require medium-term guarantees, through its launch last year of its Capital Equipment Programme. The initiative offers GTFP guarantees to select partner banks for tenors of up to five years. As it is rolled out across the global network of existing GTFP customers, the programme will support deliveries of equipment and machinery into emerging markets to enhance productivity, promote technology transfer, and improve efficiency in using raw materials and resources, thereby spurring economic growth.

**Through its trade facilitation efforts, IFC has taken a lead in helping the private sector confront the global challenge of climate change**

### Development Impact and Innovations

IFC has leveraged the success of its GTFP and Portfolio Solutions to design a broad, holistic set of products to cover the trade and commodities finance needs of its clients and partners. These products build on IFC's existing knowledge – gleaned from short-term, multi-transactional facilities – to create structured and focused solutions that address longer-term trade and working capital needs in emerging markets. Structured commodity finance, warehouse finance, supplier finance, and working capital solutions combine expertise and specific industry knowledge to enable financial institutions to offer greater support to their real-sector clients.

For these extended offerings, 2014 was marked by several groundbreaking deals. In Africa, IFC joined Natixis and Standard Bank Group in a facility to finance more than half of Ethiopia's annual refined petroleum product imports. Modeled after similar structures used by IFC previously to support oil flows into Cote d'Ivoire and Mauritania, the fully secured, US$450 million facility ensured a stable energy supply – a key driver of economic growth – in a country in which more than a quarter of the population lives in extreme poverty. In Eastern Europe, IFC extended its first structured commodity facility for soft commodities to Trans-Oil, the largest trader of grains and processor of vegetable oil in Moldova. Arranged by Societe Generale Corporate & Investment Banking, the US$155 million facility allowed Trans-Oil to perform its obligations while opening new opportunities for Moldova's farmers to participate in the global agricultural value chain. Also last year, IFC's Critical Commodities Finance Program, which provides targeted risk-sharing facilities to promote crucial commodity flows, surpassed US$30 billion in total trade support since its 2012 launch during the European financial crisis.

Meanwhile, through its working capital solutions, IFC was able to quickly respond to the outbreak of Ebola in West Africa. Food shortages, depletion of government resources, inflation, and significant drops in economic activity and cross-border trade resulted in rapidly falling incomes that most notably impacted the poor and vulnerable. In answer, IFC set up the Ebola Emergency Liquidity Facility, which combined funded working capital and unfunded trade support, to channel much-needed US$ liquidity and trade finance to local banks in Ebola-affected countries and provide continued financing for the imports of basic goods. The facility was part of IFC's US$450 million commercial financing package to support trade, investment, and employment in Guinea, Liberia, and Sierra Leone.

### Default or Claims Experience

There have been no defaults since the IFC commenced activity in 2005.

**Food shortages, depletion of government resources, inflation, and significant drops in economic activity and cross-border trade resulted in rapidly falling incomes**

**There have been no defaults since the IFC commenced activity in 2005**

**Emerging markets are playing a steadily growing role in the global economy**

**GTFP guarantees have enabled much-needed medical supplies to get to hospitals in the central Brazilian state of Goias**

### Market Outlook

As many high-income countries continue to grapple with legacies of the global financial crisis and emerging economies are less dynamic than in the past, the global economy is still struggling to gain momentum. Over the short term, we are unlikely to see again the rapid growth in trade that propelled globalization before the 2008 financial crisis. Global trade grew less than 4% a year during 2012-14, well below the pre-crisis average annual growth of about 7%. However, the WTO's recent trade facilitation agreement, which includes measures to remove trade barriers, and the potential completion of the Trans-Pacific Partnership, the Transatlantic Trade and Investment Partnership, and other free trade agreements could cut trading costs and hasten new growth opportunities.

While global trade growth has slowed, emerging market trade is still growing and remains above pre-crisis levels. Emerging market trade will likely pick up in 2015-16 to about 8%, but will not regain the rapid growth of 20% annually seen before the financial crisis. Emerging markets continue to take on an increasingly larger share of global trade, and now account for 42% of global exports, up from 19% in 1990. South-South trade makes up 24% of global trade, up from 8% in 1990, and is expected to overtake North-North trade by 2030. Moreover, these markets are moving up the global value chain as trade becomes ever more "unbundled" and countries trade less in goods and more in "tasks" that occur during the assembly process.

As emerging markets are playing a steadily growing role in the global economy, there remains high demand for multilaterals to provide critical working capital and trade facilitation in these economies. As global banks continue to be more selective in maintaining relationships with counterparties to extend their lines in developing countries, significant trade finance gaps are emerging, with firms in every region, especially small and medium enterprises, experiencing credit constraints.

In response to these market conditions, IFC will continue growing its global network to reach new financial institutions and developing innovative structures to work with partners to support the flows of critical commodities in some of the world's poorest countries. In the first six months of 2015, IFC has concluded a US$600 million risk-sharing facility with Citibank to assist the bank in extending more support to emerging market customers. Together with Societe Generale, IFC is helping finance the purchase, processing, storage, and export of cotton seeds for the current harvest season in Burkina Faso. And GTFP guarantees have enabled much-needed medical supplies to get to hospitals in the central Brazilian state of Goias; provided smallholder farmers in Benin with fertilizer needed to begin planting; and put desks for more than 4,000 students, along with other furniture, in classrooms in Angola.

## The Inter-American Development Bank (IDB)

### Background and Markets

The Trade Finance Facilitation Program (TFFP) was created in 2005 to support Latin America and the Caribbean (LAC) banks' access to international trade finance markets. As a part of the beyondBanking strategy, the TFFP supports its customers through technical cooperation, knowledge creation and the access2Markets financial product line. Such financial products include (i) TFFP trade guarantees and loans to LAC financial intermediaries, and (ii) loans to trade finance funds, which mobilize equity investors to directly finance LAC importing/exporting companies.

Since its inception, the Program has grown from 30 participating banks (both local and international) to over 300, and from US$400 million to a US$1 billion maximum approved exposure. Between 2005-2014, 1,326 credit guarantees have been issued to cover LAC trade finance risk, and 64 direct loans have been disbursed to fund LAC's international trade. In total, 5,271 individual trade transactions have been supported for US$5.03 billion.

The volumes supported by the Program have grown exponentially over the years. In 2008-2010, the Program's annual volumes ranged US$200-300 million. In 2011-2012, the volumes increased threefold to the US$600-800 million range. An all-time record was reached in 2013, with US$1.26 billion transactions processed under the Program. In 2014, US$952.9 million trade transactions were supported, setting a second historic highest.

2014 also set a historic record in terms of mobilization. Mobilized funds into the region through the TFFP syndicated loans programme reached US$302 million, a sevenfold increase with respect to 2013. This is aligned with the Program's orientation towards increasingly leveraging IDB's resources into the region using private sector funds.

As of December 31, 2014, the TFFP included 100 Latin American and the Caribbean Financial Intermediaries (LACFIs, formerly Issuing Banks) enrolled with approved lines of over US$2.78 billion, and a network of over 300 Global Financial Intermediaries (GFIs, formerly Confirming Banks) present in 64 countries. During 2014, 56 guarantees were issued and 27 loans were disbursed under the Program, to support a total of 817 underlying transactions. As of that date, the TFFP had an accumulated exposure of US$848 million in trade transactions.

**5,271**

**individual trade transactions have been supported for**

**5.03**

**US$Billion**

**30.2%**

**Brazilian banks accounted for 30.2% of the total Program supported volume in 2014**

### Regional Highlights 2014

By volume, Brazilian banks were the most active under the Program in 2014, accounting for 30.2% of the total supported volume. Bahamas followed with 21%, then Mexico (10.5%), Dominican Republic (9%), Honduras (6.8%) and Argentina (6%).

Also by volume, 49.5% of the transactions supported were LAC exports, versus 50.5% imports. On the export side, Brazil, Chile, Honduras and Mexico were our most active countries, in this order. 34.4% of LAC exports under the Program consisted in agriproducts, followed by 15.3% of processed food. On the import side, 31.15% of LAC import transactions supported came from USA and 12.9% from China. Main imported products were oil and gas (34.6%), manufactured goods (16.6%) and vehicles (10.9%). 21.31% of the total deals supported were LAC intra-regional trade.

Looking at the region's trade flows, exports from LAC continued the general stagnation trend observed in previous years. According to IDB's Latin American Trade Trend Estimates 2014 – Update 1Q 2015, in 2014 exports of goods fell -2.7% compared to 2013 levels, and ended the year at US$1.04 trillion. The region's foreign sales have gone from a stage of stagnation that began in mid-2012 to one of contraction. Per sub regions, the biggest drops were felt in Mercosur, where exports dropped -41.3% in 2014 compared to the previous year, followed by the Andean countries (-6.6%). Central America and Dominican Republic exports grew by a meager 1%. Mexico was the top performer, with a 17.5% increase.

The weak performance of the export sector is the result of a combination of several variables affecting the global economy. The appreciation of the dollar and the drop in commodity prices, mainly petroleum, drove this downward trend, in the general context of weakening global trade flows. Meager global imports, besides weakening demand for Latin American products, have put on pressure on prices of the goods that predominate in the regional export basket. Imports of Latin American goods by the region's three main trading partners fell by 28% for China, 6% for the United States, and 3% for the European Union during this period. In 2014, LAC scored a trade deficit for the second consecutive year. This was mainly due to the fall in the trade surplus in Argentina, Chile and Venezuela, and the widening of the trade deficits in Brazil, Colombia and Peru.

We continue monitoring closely the evolution of the south-south flows. In 2014, LAC exports to and imports from Asia under the Program totaled US$116.5 million. China was LAC's main importing partner (53% of that volume was imports from China), followed by South Korea (13.2%).

Lastly, looking at the activity of GFIs under the TFFP, 51% of the trade volume supported during 2014 was provided by US correspondent banks, followed by European banks (36%) and LAC banks (12.1%). The big majority of the TFFP deals have been traditionally conducted through US banks, whose role has gained increasing importance in the last years. The participation of European banks was still modest, although we saw a slight recovery from post-crisis levels. High levels of liquidity in the past years have allowed new LAC intraregional players to participate as counterparties to LAC's trades, increasing and diversifying the sources of funding available for banks in the region.

### Development Impact

Our commitment to developmental impact is proven by: (i) the percentage of individual trade transactions supported for small and vulnerable economies (50-60% since the programme's inception), (ii) the number of trade transactions processed for small and medium enterprises (61% of the total since the programme's inception), and (iii) the volume of "south-to-south" trade supported (c. US$2.50 billion since the programme's inception, including LAC intra-regional trade).

In an effort to strengthen our outreach to LAC's small and medium sized importers and exporters, in 2007 the IDB launched the Small Banks Initiative, aimed at integrating into the TFFP a group of smaller financial institutions, predominantly catering to micro, small, and medium enterprises (MSMEs). The ultimate goal of the initiative is to effectively increase the access of these companies to trade finance. Together with the integration component, the initiative also envisages a capacity building component, offering technical support to these smaller financial institutions to improve and strengthen their trade finance departments. To date, 16 small financial institutions from LAC have been incorporated in the Program under this initiative.

Also in pursuit of a greater developmental impact, the TFFP has signed a number of bilateral agreements with partner financial institutions that share our commitment towards improving and expanding the trade finance resources available in the region. The first trade co-lending partnership was signed in 2010 with Standard Chartered Bank, as a collaborative effort to provide up to US$200 million in financing to LAC banks in support of import and export transactions. A second co-lending partnership was signed in 2011 with China's Export Import Bank (China Eximbank), with the aim of enhancing south-south trade between LAC and Asia. A series of additional alliances are being negotiated at the moment. Such alliances are a priority in supporting interregional trade.

**51%**

**The trade volume supported during 2014 was provided by US correspondent banks**

### Default or Claims Experience

There have been no defaults since the IDB programme's inception in 2005.

### Regulatory Impact on Scale and Scope of Business Activity

As discussion goes on around the higher costs derived from new leverage, capital and liquidity ratios in the framework of Basel III, a growing concern is shifting towards the costs of regulatory compliance. Rising costs of KYC and regulatory requirements are negatively affecting the ability of international lenders to continue serving long-standing correspondent bank relationships that are no longer profitable. Higher cost pressures are forcing many banks to reduce and exit these relationships. This represents an important risk, especially for smaller banks and smaller countries, which will need to be monitored closely by multilateral institutions.

### Innovations in International Trade and Finance

The IDB continues to expand the scope of its support to LAC trade each year through a number of innovative products and structures, within the TFFP and parallel to it.

In the last years, the Bank has participated in two trade finance funds, one managed by Crecera and the other one by the International Investment Group (IIG), that are meant to complement traditional trade finance banking services available for LAC exporters and importers. This represents for the Bank an effective and cost efficient way to directly finance the importing and exporting companies in the region. In the capital markets arena, the Bank continues providing long-term funding to the companies in the region through several Diversified Payment Rights Programs (DPRs). Under these structures IDB's financing is secured by payment obligations, which are often trade-related flows. In addition to providing liquidity to the market, these kinds of structures allow the borrowing financial institution to improve its credit rating before creditors and investors, and in this way to obtain better funding conditions in terms of amount, tenor and pricing. These benefits are then passed on to its clients.

In March 2014, the IDB launched ConnectAmericas, the first social network for businesses in the Americas, which aims to help companies in the region to expand market access abroad. The platform is primarily designed to help companies overcome obstacles that prevent them from exporting and investing abroad, such as lack of access to reliable technical information and business contacts. Since its launch, the website has received more than 10,500 visits and more than 3,000 people have registered. Users have access to the three types of services which allow companies to: CONNECT, LEARN and FINANCE. ConnectAmericas is supported by Google, DHL, Visa and Alibaba.com, who have partnered with the IDB to support the creation of this innovative platform.

**Rising costs of KYC and regulatory requirements are negatively affecting the ability of international lenders to continue serving long**

To further close gaps in trade finance knowledge in the region, the TFFP re-launched at the end of 2014 a set of new face-to-face and online courses oriented at increasing the technical trade finance capacities of the TFFP banks in the region. The courses include a wide array of knowledge content that range from basic, plain-vanilla trade finance and to more complex structured trade finance schemes. The first course was taught in Paraguay at the end of the year. Courses will continue throughout 2015 in other countries of the region.

Lastly, as part of the efforts to promote LAC-Asia ties, the IDB organized in March 2014 the first China Insights Program, an immersion programme to help TFFP banks from LAC improve the commercial and financial relations between their client firms and companies from China. Participating bankers were invited to Beijing to meet with Asian counterparts and immerse on the economic, financial and cultural reality of China. Similar initiatives will repeat in the coming years.

### Snapshot Comment for First Half 2015 and Outlook for the Future

We have not observed a significant change in demand from 2014 levels. Pricewise, last year's spreads continued to be generally low across the region, which is still enjoying a comfortable liquidity position. Recent upheaval in some of our markets did have an observable effect on prices during the first half of 2015 for those markets. The region is expected to grow in 2015 slightly over 2%, though the recovery is expected to show uneven patterns across the different markets.

**Recent upheaval in some markets had an observable effect on prices during the first half of 2015**

**22**

**US$Billion**

**Current value of transactions since inception**

## Asian Development Bank (ADB)

### Background and Markets

The ADB's Trade Finance Programme fills market gaps for trade finance by providing guarantees and loans through over 200 banks. The ADB TFP is now at an interesting phase in its history with continuing expansion, innovation and diversification. From 2008 to 2012 the programme was in an aggressive 'ramp up' phase. The ADB TFP team was running from country to country, establishing relationships, conducting due diligence, securing internal approvals, developing internal operational procedures, designing an IT system to manage growth, in addition to building its business portfolio.

Back in 2008 ADB's TFP supported a modest US$18 million in trade through 458 transactions.

### Volumes and Values 2014

As the TFP evolved the trade support figures also increased significantly. By 2013 the figure was US$4 billion through 2,000 transactions, and now it seems to be hovering in this general range. Given the current flux in the commodity markets and slower trade growth in emerging markets we may see some downward impact on this outcome going forward in 2015. With the current value of transactions since inception currently pushing towards US$22 billion the volumes and values and in turn demand figures for the TFP speaks for itself.

The ADB TFP has expanded in most of its core markets – Bangladesh, Pakistan, Sri Lanka, Uzbekistan, Mongolia, Viet Nam and 12 others. The ADB TFP does not currently have plans for TFP to start assuming risk in relatively developed markets such as China, India and Thailand

### Summary of Development Impact

The ADB's TFP fills market gaps for trade finance by providing guarantees and loans, but more importantly by mobilizing private sector resources to fill the trade finance gaps. Co-financing and risk-sharing with private sector entities remain a priority. The ADB TFP is working hard to shrink the market gap in trade finance in the most challenging markets, both through its direct support and by mobilizing private resources into challenging markets. This approach helps create long-term relationships (credit lines) between banks in developed and developing countries. With these new relationships come greater financial links to support trade, job creation and more prosperity in emerging Asia.

ADB's TFP supports the development of the banking sector in its developing countries of operations. With rigorous due diligence and ongoing risk monitoring processes, and related feedback to bank we instill an appreciation for best international banking practices in bank management.

ADB's TFP also believes in empowering trade bankers in our countries of operation. In partnership with ICC experts the ADB has provided customized trade related training solutions to participating banks.

Within ADB countries of operation SMEs are a major source of job creation which in turn keeps the wheels of economic development turning right down to grass roots level. By training the trade bankers this international trade and finance knowledge can in turn be passed on to their customers, many of whom are new to the concepts of international trade and finance.

### Default or Claims Experience

There have been no defaults since the ADB programme's inception in 2004.

### Regulatory Impact on Scale and Scope of Business

Increasing levels of regulatory requirements for trade finance have increased the challenges for the trade finance industry right across the globe. This in turn has increased the trade finance gap in developing countries, and therefore have increased the demand for multilateral development banks such as the ADB to fill the gap.

ADB initiated the creation of a default and loss data base, in conjunction with ICC. The core statistics created from this research are available on ICC's website. This information was presented to regulators in an effort to ensure regulatory requirements reflect the relatively low-risk profile of trade finance. Some progress has been made to treat trade finance appropriately for regulatory purposes and this valuable process of dialogue between the stakeholders must be continued.

In addition to establishing the Register, ADB's TFP is continuing its work in quantifying market gaps for trade finance and their impact on growth and jobs. These studies, among other things, seek to emphasize the importance of the link between trade finance and economic growth and to underscore the importance of removing regulatory and other impediments that restrict the financing of trade.

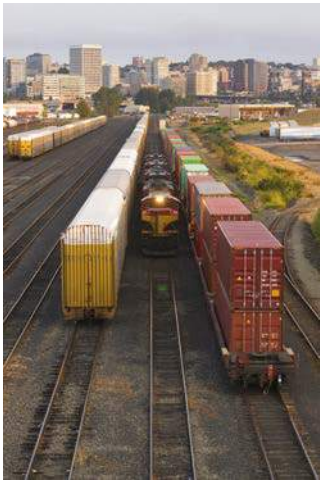
### Trade Outlook for the Future

The ADB's TFP will continue supporting trade in emerging Asia and with the apparent challenges in the markets we can expect the demand remains robust.

Looking ahead, the ADB TFP will be expanding to Myanmar and Pacific islands over the course of 2015/16. TFP will be rationalizing the banks it works with: ending relationships, but without exiting countries, where there has been no business. We will also be increasing the number of partner banks in core markets such as Bangladesh, Pakistan and Viet Nam, where we anticipate adding possibly 4-5 more banks.

Our research has highlighted that environmental safeguard policies in financial institutions are typically not well attuned to the trade finance business. The ADB TFP aims to have a closer look at this difficult question and explore the possibility of designing guidelines that are more specific to trade finance business.

**ADB's TFP is continuing its work in quantifying market gaps for trade finance environmental safeguard policies in financial institutions are typically not well attuned to the trade finance business**



## TFP can to act as an information gateway fostering the establishment of trade related relationships in emerging markets

In response to market demand, TFP is designing a new innovative funded risk participation product, which is designed to help our partner client banks respond to the changing regulatory landscape.

Furthermore we see closing information gaps as the precursor to closing market gaps. The ADB TFP continues to innovate and distinguish itself through 'knowledge products'.

In simple terms, this means that well informed TFP relationship managers will actively provide information to partner client banks and insurers about opportunities and risks in TFP's countries of operation. This is a proven strategy to help partner banks and insurers take informed decisions. We have seen banks and insurers take first steps into new markets, supported by the information which TFP's relationship managers provided. This means that the ADB TFP can to some degree act as an information gateway fostering the establishment of trade related relationships in emerging markets.

### Conclusion – MDBs and Trade Facilitation

Multilateral development banks continue to play an important lynchpin role in keeping supply chains open. They facilitate the development of relationships for smaller issuing banks in emerging markets with the international trade finance markets

We can now see the expansion of the existing MDBs trade facilitation programmes and the creation of new development banks which will also have a strong focus on trade and investment. The innovative trade finance models of the MDBs continue to provide trade risk coverage and access to finance which even penetrates down to SME trade activity even in the poorest countries.

The ICC Banking Commission has forged strong relationships with the development banks who have a common shared goal, which is to facilitate, support and advance trade, which now more than ever provides the primary opportunity to uplift economic development and poverty reduction.

No access to trade finance means no access to trade.

# INTERVIEW

## The International Islamic Trade Finance Corporation (ITFC)

**Eng. Hani S. Sonbol**
Deputy CEO, International Islamic Trade Finance Corporation

# REGIONAL FOCUS: MIDDLE EAST AND NORTH AFRICA

With the ICC's strong focus on extending its reach into emerging markets and the establishment of the ICC Regional Banking Commission MENA in Dubai (ICCRBC MENA), Vincent O'Brien is delighted to have had the opportunity to talk with Eng. Hani S. Sonbol, the Deputy CEO of the International Islamic Trade Finance Corporation.

**The ICC Banking Commission has been working in partnership with the global development banks for many years and with the establishment of the ICC Regional Banking Commission MENA, there is now a sharp focus on expanding the reach into the Middle East and North Africa region. Can you provide some background on the establishment of ITFC in the context of supporting trade with a particular focus on the MENA countries?**
ITFC is an autonomous entity within the Islamic Development Bank (IDB) Group. Its establishment came as a consolidation of all IDB Group trade finance activities under a single umbrella.

Our parent institution, the Islamic Development Bank; from its inception in 1975, had recognized the value of trade to economic development and started trade financing as an integral component in its socio economic development activities in its member countries since inception.

With the establishment of the ITFC in 2008, the initiative was to facilitate and financially support international trade and finance. Basically, the mission for the ITFC was to act as a catalyst for the development of trade among the Organization of Islamic Cooperation (OIC) member countries and in doing so, help the countries engage through trade with the rest of the World.

As you indicated the MENA region is of great importance but it is also worth highlighting that the IDB has 56 member countries across Asia, Europe, MENA, Sub-Saharan Africa and even South America.

In the context of the MENA region, the ITFC has a long and successful track record with more than US$8.0 billion of financing since 2008. The ITFC in total however has achieved more than US$34.0 billion of financing since 2008.

**We have seen lacklustre expansion of trade and growth in recent years in many markets compared to growth rates seen before the financial crisis. Can you provide an insight into trade and growth rates of OIC Member Countries?**
The numbers speak for themselves and we see some similar developments. The OIC member countries experienced sharp downturn in economic activity in 2013 when their growth rate fell from 4.6% to 3.9%. However, they managed to regain a “hint’ of recover in 2014 with a growth rate just a shade above 4%. While there are disparities between member countries growth rates it was somewhat encouraging that the average growth rate of

the real per capita GDP in OIC countries has remained positive during the period 2009-2014, for example it increased by 1.8% in 2013 and reached just above 2% in 2014.

**The importance of guarantees issued by way of Standby Letters of Credit under Multilateral Development Bank taking risk on smaller banks in emerging banks has clearly played an important role in facilitating trade with countries that otherwise may have been outside international commercial banks risk appetite. What are the primary financing tools used by the ITFC in supporting and expanding the provision of finance to support international trade?**

It must be acknowledged the guarantee programmes of our colleagues in development banks have been successful and have played a role in keeping supply chains open, especially during challenging times. Our model at the ITFC is more focused on providing direct financing to partner banks, institutions, governments and the private sector through Shari'ah-compliant structures designed and customized for specific client needs.

Simply put, our model is a targeted one where we work in partnership with stakeholders devising specific trade solutions for specific trade related needs. Moreover, our model primarily focuses on the end of the supply chain considering mainly the end beneficiary to provide the funded elements of the Trade Finance cycle.

**If I may push you to provide more specific examples – can you provide current cases of how some structured solutions of the ITFC were actually implemented?**

I am happy to do so; various Structured Trade Finance (STF) schemes have been devised as solutions in member countries. This is where we at the ITFC get close to the actual business, partnering with collateral managers, agent banks and top-rated insurance companies. This results in innovative tailored trade finance solutions being provided.

One example has been the partnership with a bonded warehouse operator in Turkey to provide collateral management services for ITFC trade financed operations. Last year, ITFC also concluded the first Structured Trade Deal with a bank in the CIS.

By way of a further practical example, in September 2014, the ITFC and Aktifbank Turkey signed a 2-Step Murabaha Agreement for US$45 M and in June 2015 we signed a similar line with Turk EximBank for US$350 M. These structures are basically a trade finance line for Turkish Exporters. By working in partnership, this facility was implemented very quickly. Due to the innovative features the deal with AktifBank won the 2014 Trade Finance Magazine Deal of the Year.

A hallmark transaction for the ITFC was the Trade Finance Line for Egypt to support their energy requirements. This was in the form of a group of transactions under a Framework Agreement with the Government that enabled ITFC to continuously meet the needs of the Egyptian General Petroleum Corporation for Petroleum Products. So far ITFC has financed approximately US$3.6 B for Egypt under this structure. In addition, ITFC is able to support the private sector by extending multi-country facilities to our clients that supports their operations in all the countries. As an example, ITFC extended such a facility to a major Food Manufacturing company in Saudi Arabia to cover their financing needs across all of their companies in region.

Finally, a transaction which I particularly liked due to its development impact was a creative financing transaction based on government subsidy receivables in Morocco. This Moroccan deal led to implementation of an LPG transaction for a company that serves rural communities in the country.

**That is significant on the financing side, but can you provide some insights into the importance of the ITFC's development role?**

This is a good question. As a member of IDB Group, the ITFC was created with the purpose of advancing trade which would ultimately contribute to the overarching goal of improving socioeconomic condition of the people in our member countries. ITFC has a mandate to provide financing in countries where the interventions have strong potential to make a positive difference in the lives of the common people, particularly, in rural communities. A clear example is to provide financing and technical support to create value for agricultural output in early stages of production which is mission critical for food security in many less developed countries going forward.

This type of financing is often avoided by commercial banks but at the ITFC this 'grass roots financing' is central to our developmental role. To be more specific, the developmental role of ITFC can be categorized in 4 main areas for which I will also give you specific examples:

**1 Supporting Strategic Exports: Gambia & Senegal (Groundnuts)**

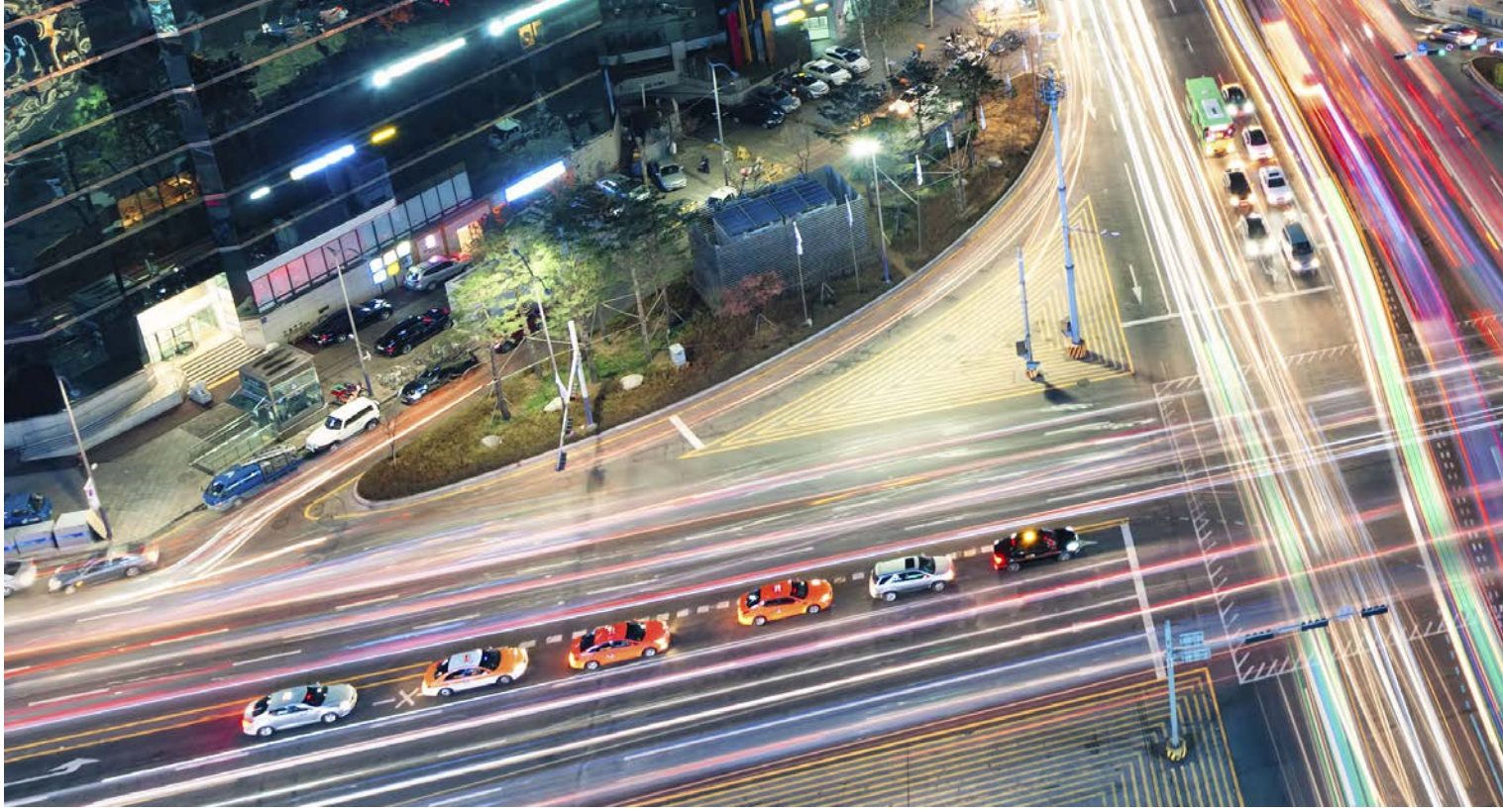
- Several pre-export financing operations were granted to help farmers promote their Agri-Products to the world, the financing was implemented in a structure that helps farmers secure the required agriculture inputs such as quality seeds & fertilizers at reasonable costs, whilst at the same time allowing the relevant government agency procure harvests from farmers at good prices and with payment on a timely basis;
- These facilities have a great development impact on the farmers as they provide direct access to quality inputs and give them the assurance of receipt of value for their produce in time. In Gambia for example, we are very pleased that our intervention benefits over 300,000 local farmers, 70% of whom are in the rural areas whose livelihood depend on this crop;
- In addition, this development financing also supports the mentioned countries export expansion plans, as purchased produce are partially processed and then exported to earn much needed foreign exchange;
- In other countries in the region such as Benin, Burkina Faso and Cameroon, ITFC is lending vital support to the cotton industry and thus helping these member countries enhance the export of this strategic commodity.

**2 Alleviating Poverty: Niger & Mali Food Security Financing**

- Niger and Mali are both landlocked countries with each economy based on subsistence crops. The agriculture sector is a major contributor to GDP and provides livelihoods for significant part of the population;
- ITFC financing in synergy with IDB was approved to support the food security programme of the governments and help fight malnutrition and alleviate poverty, while contributing to the overall social wellbeing of the population. This is a success story that provides a model going forward.

**3 Ensuring economic activity stability: Comoros, Djibouti, Egypt, Mali, Mauritania, Morocco and others for refined petroleum products**

- ITFC financing in these instances is used to supply fuel oil leading to stability in supplying this commodity for electricity generation reaching large number of cities/villages in the countries;
- Stability in Electricity generation has a positive impact on the economy in terms of continued operation of social services (Hospitals, schools), infrastructure, agriculture, main Industries as well as individual homes;



- For example, ITFC helped increase the strategic stock of fuel oil of the electricity company to 12 days from 2 days in Mauritania. This importance of this type of facility cannot be overstated.
- Another good example is Comoros, where ITFC is successfully helping to secure and rationalize the cost of its energy supplies, improving at the same time the country's macro-economic situation. The intervention helped reduce costs directly by over US$1 million. In addition, the financing led to increased competition between suppliers resulting in competitive pricing. The decrease of premiums is estimated to generate US$4 million in savings in comparison to the year before (excluding oil prices drop impact).
- In Morocco, ITFC is supporting private sector initiatives in the oil and gas industry for the provision of crude oil, refined petroleum products as well as liquefied petroleum gas for local consumption.

**4 Supporting the private sector and regional financial institutions**

- In countries like Nigeria and Togo, ITFC is intervening the financial sector by providing the Two-Step Murabaha to local and regional banks. This allows these financial institutions to provide more cost effective financing to their SME customers and thus adding development to this otherwise marginalized sector of the economy.

**Development Banks have historically placed significant importance on the provision of technical assistance and training to facilitate the expansion of international trade and finance. Is there an important role for trade related technical assistance at the ITFC?**
Within the ITFC, the Trade Cooperation and Promotion Programme (TCPP) is the trade development arm, complementing the ITFC overall vision of being a trade solutions provider for our member countries. We achieve positive development impact by pooling of technical and financial resources from a network of development partners. The benefits from these initiatives filter right down through governments, financial institutions, corporations and even to SME enterprises availing of their services.

Building strong human and institutional capacities in trade is essential to foster trade, development, to improve the lives of the common people and in turn, most importantly, to alleviate poverty.

The ITFC has a common goal with ICC in enhancing trade knowledge and expertise. As the ITFC network and regional presence expands we also expect to see an expansion in the role and importance of trade related technical assistance and training.

**Alliances and partnerships with other development organizations are very important to achieve better and wider developmental results. Does the ITFC have innovative initiatives with other development organizations?**
Yes, indeed. ITFC is working with several international and regional organizations to achieve economic integration and employment through trade such as the Aid for Trade Initiative for Arab States (AfTIAS). This is a multi-donor, multi-country and multi-agency programme, aiming to foster Arab trade through enhancing enterprise competitiveness and facilitating ongoing trade.

Let me demonstrate how this works: The AfTIAS is organized to help Arab countries to expand trade beyond current levels, boost economic growth and employment, reverse deindustrialization and ultimately achieve higher human development outcomes. Through this initiative it is planned to provide a major platform to assist the Arab Region to mobilize resources, to accelerate the pace of trade reforms and enhance competitiveness in global and regional markets. Basically, the objective is to head-on address the challenges of unemployment, particularly youth unemployment, support economic diversification and provide momentum for the full realization of the Pan-Arab Free Trade Area (PAFTA).

The AfTIAS has a clear target to enhance regional competitiveness through trade reforms, strengthen trade supply side and value chain integration and also strengthen regional and sub-regional organizations' capacity to foster trade integration.

**Finally, Eng. Sonbol – thank you for your valuable time in conducting this interview. As a parting remark can you suggest how the ICC Banking Commission can take further steps to enhance its position in facilitating trade with emerging markets, particularly in the MENA region?**
You are most welcome – the establishment of the ICC Regional Banking Commission MENA was a positive step in reaching out to trade professional in the expanding MENA markets.

Furthermore, I see a significant opportunity for partnership with the ICC Banking Commission in terms of the sharing of knowledge and expertise and perhaps also in the development of international trade facilitating standards.

At the ITFC we look forward to continuing the cooperation with the ICC Banking Commission.

HIGHLIGHT:

# ICC ACADEMY

The ICC Academy offers world-class certifications and recognition, online training programmes, international seminars, specialized publications and a number of networking opportunities.

The ICC Academy promotes the highest global standards of excellence in professional education—providing a wide range of specialized certification programmes that are recognised worldwide. In line with the ICC's mission to promote international trade and investment, the Academy helps professionals develop the skills required to address today's business challenges. The ICC Academy started operations in the field of trade finance, one of the International Chamber of Commerce's (ICC) strongest domains of expertise.

### Our Mission

The ICC Academy aims to provide rigorous, relevant and applicable business education – encouraging individuals to reach their highest potential with respect to professional competency and ethical conduct. Additionally, we want to offer those in developing or remote regions equal access to world-class professional educational opportunities, therefore helping develop skills even in the most challenging environments.

### ICC Academy's Curriculum and Membership

ICC has a worldwide reputation for drafting international business standards and first-rate policy in many industries. The ICC Academy's curriculum is developed by ICC's unrivalled roster of experts and practitioners—incorporating insights from external senior business leaders and policy-makers.

The ICC Academy will be leveraging decades of expertise in standard-setting and policy making. The ICC Academy credentials denote proven expertise in trade finance. Certified members will have a unique set of skills that are not found in any other career field or discipline; they will combine knowledge of complex financial transactions with an understanding of methods, international practice, and how to resolve allegations of fraud and/or disputes.

ICC Academy members get access to a wealth of information and training, as well as to exclusive publications and savings. You will also become part of an international network of thousands of like-minded professionals, providing each other with guidance and support.

### MEMBERSHIP

Individual professionals join the ICC Academy as members; but to attain the highest level of membership in the ICC Academy, members needs to demonstrate competence through the completion of a series of certification programmes and mandatory continuing professional education. The Academy also offers valuable networking opportunities to its members.

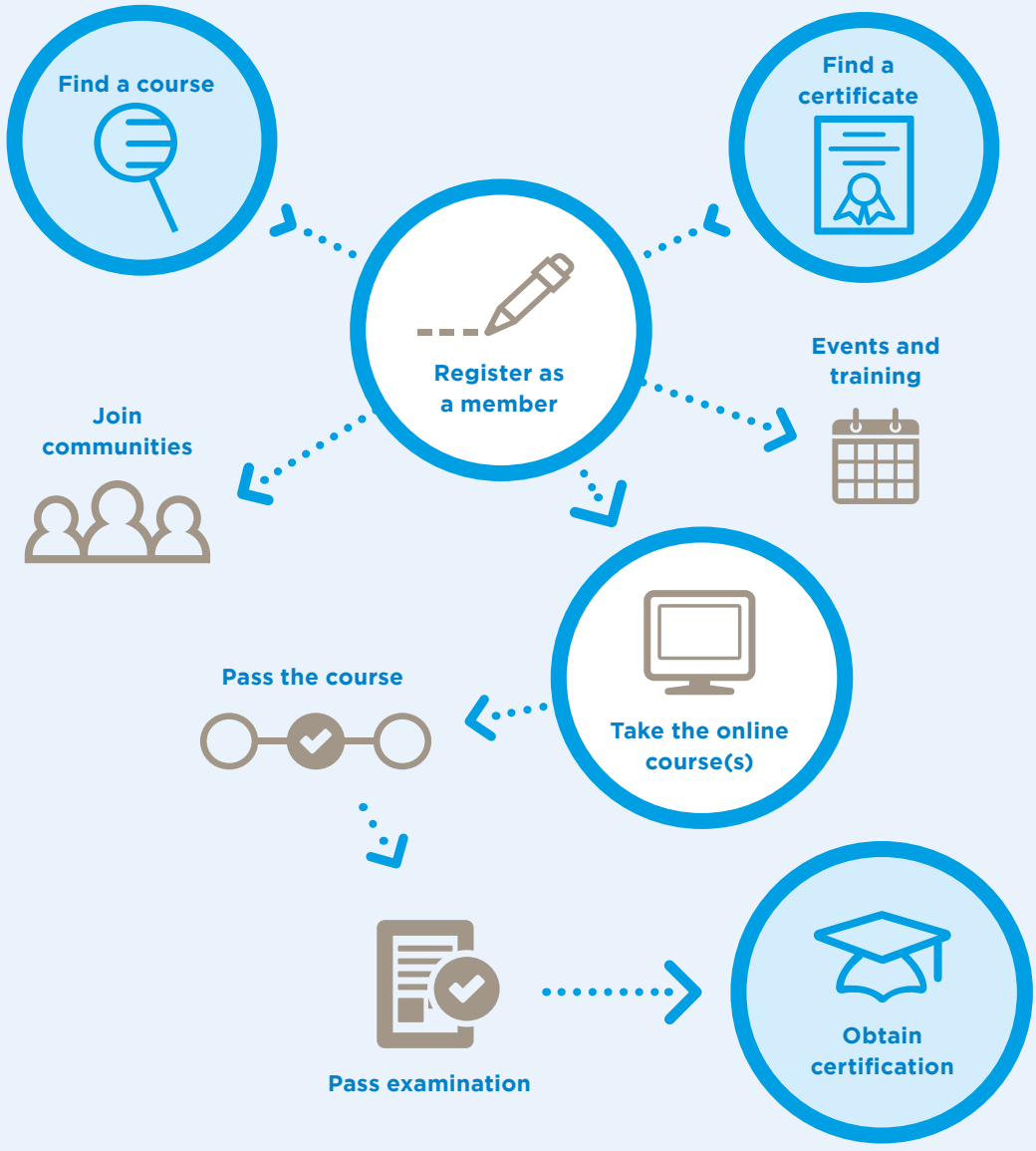
### EDUCATION & TRAINING

The ICC Academy sets an international standard for testing the knowledge of those entrusted with the financing of cross-border trade. A wide range of products and services will be provided to support the ICC Academy certification programmes, including: E-Learning; specialized publications, webinars, trainings, etc. Through ICC's global network, the ICC Academy provides specialized trainings and seminars around the world.

www.icc.academy

# How to get started?

An interactive classroom that's open all hours.



# LOOKING AHEAD

A panel of industry experts share their views on the drivers and solutions to a more robust and resilient market, with a few retrospective observations on the Survey and a call to take part in the next edition.


The Interviews › 138

Closing Remarks › 166

# EXPERT VIRTUAL ROUNDTABLE DISCUSSION

In the form of a virtual roundtable discussion, the ICC liaised with key figures of the Banking Commission to discuss the ways in which they are keeping their business moving in this, the most challenging of times for the industry. The results below demonstrate a realization of the need for trade financiers to be nimble and forward-thinking. In order to survive and to thrive, banks must be alert to and prepared for the unprecedented multitude of challenges they're faced with today, or face being left behind.

In the Looking Ahead section that follows, we discuss the risks and opportunities for trade presented by this constantly changing world, with some of the most experienced and dynamic practitioners in the business.

## ALBERTO AMO MENA

Global Head of Trade Asset Solutions in Santander Global Banking and Markets; member of the Advisory Board of the ICC Banking Commission

Alberto Amo is responsible for Trade Finance for Corporates and solutions which require counsel on regulatory, capital and liquidity matters. Moreover, he is in charge of the development and extension of all Global Transaction Banking assets to mobilization, distribution and syndication strategies, with innovative products such as Trade MAPS or ECA Backed Covered Bonds. During more than 20 years in the industry, he has mainly developed his career in Corporate Banking as Relationship Manager.

## MARC AUBOIN

Counselor in the Economic Research and Statistics Division of the WTO

Marc Auboin is responsible in particular for trade and finance issues, including trade finance, and for coherence in economic policy-making with other institutions. Previously he held several positions at the International Monetary Fund (IMF), worked for the French Treasury. Marc holds a PhD in Economics and lectures as an adjunct Professor at the World Trade Institute in Switzerland. He published many pieces of research on trade finance issues.

## SABRINA M. BORLINI

Global Manager, Global Trade and Commodity Finance, International Finance Corporation

Sabrina M. Borlini leads a global team responsible for business origination for IFC's suite of trade and commodity finance products such as the Global Trade Finance Programme (GTFP), the Critical Commodities Finance Programme (CCFP), the Global Warehouse Finance Programme (GWFP), the Global Trade Supplier Finance (GTSF), the Global Trade Liquidity Programme (GTLP) as well as Structured Trade Finance solutions. Prior to her current position, Sabrina covered a number of positions in the Trade and Commodity Finance Department, based in Sarajevo (Bosnia), Johannesburg (South Africa) and Brussels (Belgium).

## OLIVIER PAUL

Head of Trade Finance Competence Centre, BNP Paribas; member of the Advisory Board of the ICC Banking Commission

Olivier Paul started his career in the bank 30 years ago, taking several positions in the Corporate Banking: from the management of mid cap portfolios up to the position of head of the network branches in Paris of Banque Paribas. Since 1st January 2014 Olivier has been appointed Head of Trade and Banking Flow (TBF). He is currently 'Conseiller du Commerce Exterieur de la France' and member of the Business Finance Committee of the European Banking Federation.

## ERIC DE JONGE

Managing Director, Global Head Structured Export Finance, ING Bank; member of the Advisory Board of the ICC Banking Commission

Eric de Jonge is an ING banker with over 20 years of experience in financing assets, companies and projects. His current responsibilities include implementation of strategies and policies as well as client coverage, origination, business development and portfolio maintenance related to export financing transactions for ING globally. Eric leads a global team of up to 40 professionals in various locations. As such he is involved in the commercial and credit approval processes.

## DANIEL SCHMAND

Head of Trade Finance & Cash Management Corporates EMEA, Deutsche Bank, Chair of the ICC Banking Commission

In addition to his responsibility for the EMEA region, Daniel Schmand heads the Global Trade Finance Committee, which drives the Trade Finance strategy, encompassing Financial Supply Chain and Structured Trade and Commodity Finance products. Daniel joined Deutsche Bank in 1987 as a trainee. He holds a Bachelor's degree of Business Administration as well as executive education at INSEAD and the International Leadership Programme at Ashridge, IMD and Duke.

## STUART TAIT

Global Head of Trade and Receivables Finance, HSBC; member of the Advisory Board of the ICC Banking Commission

Stuart Tait is the Global Head of Trade and Receivables Finance which provides financing and risk mitigation solutions to meet clients' international and domestic trade requirements. These encompass products that finance the supply chain end-to-end, from raw materials to manufacturing and shipment, to discounting and collecting receivables across more than 60 countries. Stuart joined HSBC in 1984 and has held various positions in Commercial Banking, Global Banking and Markets, Retail Banking and Wealth Management, Risk and HR. His assignments have been in Asia, Europe, North America and the Middle East.

## MARKUS WOHLGESCHAFFEN

Managing Director Global Head of Trade Products, Global Transaction Banking, Corporate & Investment Banking UniCredit; member of the Advisory Board of the ICC Banking Commission

Markus Wohlgeschaffen is responsible for all commercial Trade Finance Products & Services as well as all Supply Chain Finance Products of UniCredit. His area of responsibility comprises the management, innovation, development and implementation of all (traditional) Commercial Trade Finance and Service products (Letters of Credit, Letters of Guarantee, Documentary Collections, Forfaiting) offered by UniCredit worldwide. Markus is the Chairman of BAFT's Global Trade Industry Council (GTIC), member of the Board of Trustees of the Fraunhofer-Institute for Material Flow and Logistics, Dortmund and member of the SWIFT Corporate Advisory Group (CAG).

## MICHAEL VRONTAMITIS

Head of Trade, Product Management, Transaction Banking, Standard Chartered Bank; member of the Advisory Board of the ICC Banking Commission

Michael Vrontamitis is responsible for the P&L and delivery of the Bank's Trade Finance capabilities globally in Documentary Trade, Receivables Finance, Supply Chain Finance, and working capital solutions, to all of the Bank's clients across Corporate & Institutional, Commercial and Business clients, as well as for the Bank's Trade Finance distribution. He joined Standard Chartered Bank in 1995 and has worked in Hong Kong, London and Singapore across a number of business areas. Michael is on the board and the honorary treasurer of KELY support group, a Hong Kong-based Charity.

# Generally speaking, what are the primary trends you are noticing specifically relating to trade finance and how it is being conducted?

**STUART TAIT:** In terms of trade finance trends, we forecast a continued movement towards open account solutions with a focus on both receivables financing and supply chain products. Some companies have responded to economic and political stress by reconfiguring their supply chains, either sourcing from geographically nearer trade partners, reshoring, or nearshoring their manufacturing base. Others have looked to new markets for their products. These present a changing pattern of trade, but the constant is that firms are looking to optimize working capital beyond traditional trade products and mitigate risk.

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**MICHAEL VRONTAMITIS:** In the recent past, while volumes have increased, the value of trade (and trade finance) in the traditional merchandising space has not grown with the same multiples to GDP as we have seen in the last couple of decades. This, coupled with the recent significant reduction in commodity prices, has seen an overall reduction in the demand for trade financing.

On the supply side, we've had quite a lot of liquidity in the market place in a number of jurisdictions, particularly in Europe, China and Japan. In other jurisdictions, we're even seeing supply come down a little, particularly around de-risking, as well as capital management, as banks increasingly focus on conserving capital and improving their returns whilst minimizing risks.

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**MARKUS WOHLGESCHAFFEN:** One strong trend is the growth of cross-border trade alongside an over-proportional increase of open account transactions. This is especially the case as trade expands with counterparties in emerging markets such as Africa and Central and Eastern Europe, a result of modern and efficient multi-dimensional supply chain networks. Such developments promise increases in process complexity for corporates, coupled with the need to manage exposures to operational and financial risks.

> "The constant is that firms are looking to optimize working capital beyond traditional trade products and mitigate risk."
>
> **Stuart Tait**

**ALBERTO AMO MENA:** On the demand side, the major trend remains the shifting of global supply chain flows. This is diversifying corporate needs and forcing domestic and cross-border solutions to converge. On top of this, there is a higher demand for trade as a working capital and risk solution than before, when it was 'mainly' a way for a commercial transaction to occur and be bankable. These factors are driving an increase in the use of trade finance solutions.

**OLIVIER PAUL:** The cost of implementation of trade finance activities is increasing, and since profitability is decreasing, you have a 'scissors effect' with revenues that are decreasing and expenses attached to this transaction which are increasing. As a result, you could obtain a difficult situation in terms of global, overall, profitability for the banking industry in terms of trade finance activities.

> **"The shifting of global supply chain flows is diversifying corporate needs."**
>
> **Alberto Amo Mena**

# How are these factors influencing the amount of liquidity in the market?

**ALBERTO AMO MENA:** On the banks' supply side, trade finance faces its own tests within the current financial industry situation. Quantitative easing policies, causing excess liquidity and low interest rates in major currencies, are severely reducing spreads in some markets. However, there are other regions where the rise of regulatory pressure still poses a threat due to its unintended consequences on the provision of trade finance.

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**MARC AUBOIN:** The WTO Expert Group on Trade Finance indicates that while there is enough liquidity for trade finance in the main trade routes, due in particular to the relatively favourable environment created by monetary policy, this liquidity is not available everywhere and not to all players. Markets have become more selective, and the aftertaste of the financial crisis manifests itself in the form of continued deleveraging by global banks. While market shares are taken up by local and regional players, this leaves a gap at the low end of the market (small players in poorer countries), which already faces the weight of structural challenges.

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**ERIC DE JONGE:** I agree, liquidity is available in abundance, putting pressure on structures – loosening covenants and conditions – and pricing. Interest rates are around an all-time low, providing for an environment to borrow as cheap as never seen before. Traditional products face competition from alternative products fuelled by liquidity and appetite for risk or risks on earn higher yields. For example crowd funding and disintermediation via private and capital markets are putting pressure on the banks' involvement and their business models.

> **"Traditional products face competition from alternative products fuelled by liquidity and appetite for risk."**
>
> **Eric de Jonge**

# We are living in a time of unprecedented numbers of macroeconomic issues being played out: commodity prices slumping, geopolitical crises, trade and financial sanctions: what are you noticing here, and what impacts are they having on trade finance?

**SABRINA M. BORLINI:** Lower commodity prices, particularly in the energy sector, combined with concurrent economic slowing of several emerging market trade powerhouses, such as China, Brazil, and Nigeria, have contributed to a reduction of dollar volume trade finance flows in emerging markets. Sanctions on Russia and the uncertainty in the region have also contributes to a general slowdown. Accompanying this is wider variance in market liquidity – with some having an excess while others find the need for forex greater than in recent years. Oil prices are predicted to recover slowly in FY15 and FY16, although they will not reach prior levels during that time. Aggregate demand for commodities will remain muted until economic growth picks back up in some of our larger economies. On the positive side, we see some signs of recovery in certain markets, for instance, with Nigerian elections successfully completed, there is a promise of renewed trade finance for Africa.

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**DANIEL SCHMAND:** Geopolitical risks, which have been thrown into the spotlight again this year, will influence both bank and corporate behaviour in the years to come. Unfortunately, low risk appetites coupled with the ongoing burden of compliance can mean that banks and corporates are reluctant to undertake new markets – despite the wealth of opportunities to be exploited in many of them.

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**ERIC DE JONGE:** Major uncertainties are sanctions and changes thereof, in Russia, Iran etc., wars or threats thereof, such as ISIS, local conflicts in Africa, and some territorial tensions between countries in Asia. The number one issue is how will the sanctions and political issues develop and influence trade financing opportunities going forward?

"Low risk appetites coupled with the ongoing burden of compliance can mean that banks and corporates are reluctant to undertake new markets."

Daniel Schmand

# And what does the panel feel are the consequences of these sorts of risks and trends? In what ways can authorities work towards alleviating such risks in order to ensure the free flow of trade?

**MARC AUBOIN:** Trade finance is primarily demand-driven, so any major uncertainty relates primarily to global economic activity and trade expansion. Trade finance will expand if global economic activity and global trade expands. The slowdown in trade growth relative to the past and the fall in prices of certain goods (commodities) could create a challenge to the industry if they were to be lasting phenomena.

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**SABRINA M. BORLINI:** Beyond the cyclical nature of commodity prices and thus trade finance volumes, potential retrenchment of banks that have historically extended into a wide array of markets creates a need for new players. The speed and extent to which current banks will retrench and others will rise to fill the gap remains to be seen.

**DANIEL SCHMAND:** One consequence of these anxieties is a distinct movement towards a more holistic approach to trade; focusing beyond the corporate body to look at the supply chain environment as a whole – leading in part to a soaring interest in supply chain financing. Through awareness of the interest rates, funding costs, and potential vulnerabilities of counterparties, and counterparties' counterparties, corporates can mitigate risks – whether environmental, financial or political – and strengthen trade relationships.

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**STUART TAIT:** The G7 summit showed the continued political will from global leaders for the liberalization of trade. Intermediate inputs account for more than half of global trade. This means goods move multiple times, through multiple firms, across multiple borders, bringing smaller companies together with regional and global players. Businesses need global trade policies which reflect this reality. We look to policymakers to bring the various plurilateral and multilateral trade agreements under negotiation to fruition.

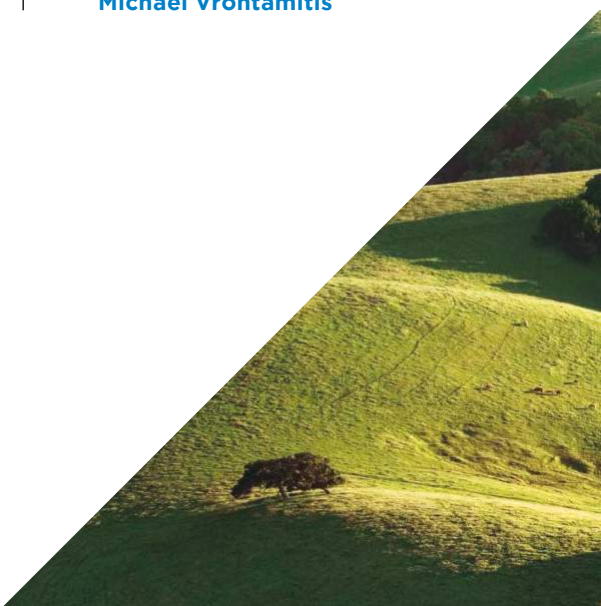
> "Trade finance will expand if global economic activity and global trade expands."
>
> **Marc Auboin**

**There is a lot of talk at the moment about de-globalization: borne out of the raft of bilateral and plurilateral agreements being negotiated around the regions of the world. In terms of trade flows and regional trade blocs, what are you seeing emerging strongly at the moment?**

**MICHAEL VRONTAMITIS:** One key trend is really this whole East-to-West story of economic power shift to the East, with emerging markets growing faster than the West. We're seeing China as the mega-trader of the future – it is already a mega-trader – but on global scale, China will increasingly become more and more critical to global trade, particularly as its consumption grows. That's a critical trend.

Increasingly, we'll see more of the South-South corridors, rather than the traditional Asia-to-Europe or intra-Europe type of corridors. I'm not saying that those corridors won't continue to grow, but on a relative basis, they'll grow less quickly and so these will be driven by urbanization and by the development of the emerging markets. China and India particularly, are growing at a faster rate and will essentially be taking up a larger percentage of the global economy in the next five to ten years. I think in five years we expect China to be almost the same size as the US in terms of absolute GDP – it will be relatively close.

> "Increasingly, we'll see more of the South-South corridors."
>
> **Michael Vrontamitis**



> "Many are leapfrogging developed market technologies."
>
> **Daniel Schmand**

**DANIEL SCHMAND:** I would concur with that. The major shifts in trade flow patterns continue – we will likely see global trade divided up in more diverse ways as emerging markets continue to increase their share. And as they do so, we see not only new trade flows between different regions, but also a rise in two-way trade flows that have traditionally had a buyer-supplier relationship.

As many emerging markets have younger populations, and the new powerhouses such as India and China experience a rapidly expanding middle class, huge new consumer markets are opening up. This new demand is stimulating both South-South trade corridors and inverse developed-developing trade relationships – as well as encouraging developed corporates and banks to consider their locations.

The liberalization of the renminbi, which started off this year by breaking into the top five global payment currencies, also supports South-South growth. Yet while emerging market growth is undeniable, a failure to differentiate between different regions or countries in terms of emerging market opportunities, risks and growth rates is a pitfall that should be carefully avoided.

Emerging markets can offer greenfield opportunities to banks and corporates looking to expand in new regions; without the burden of legacy systems and with different pressures to innovate, many are leapfrogging developed market technologies and implementation.

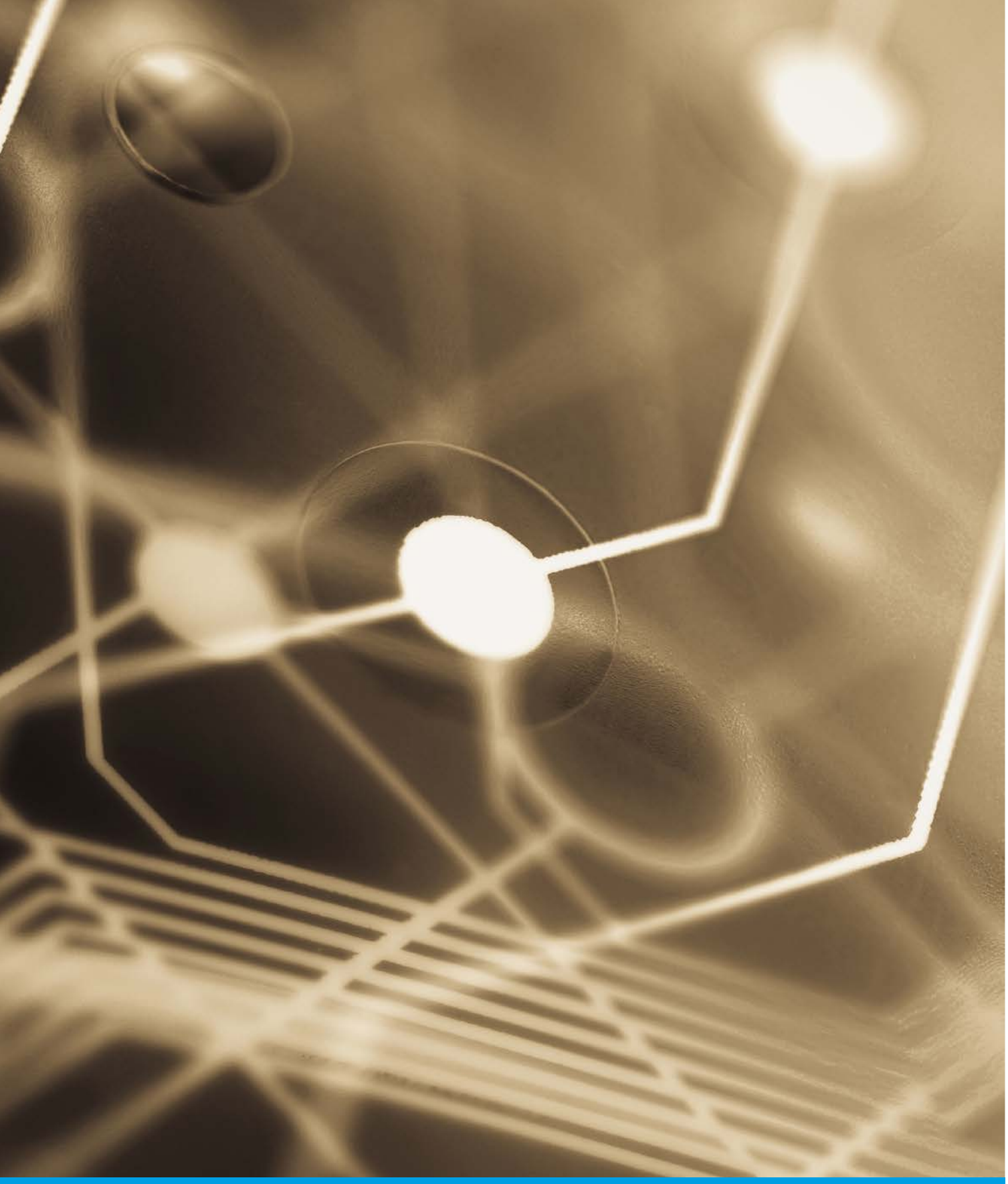
**This 'reshaping' of trade, so to speak, will obviously nurture serious change in supply chains. What are you seeing on this front, and how can financiers work to optimize supply chains in the face of such change?**

**MICHAEL VRONTAMITIS:** We are seeing what we call the 'unbundling of trade' – and this is essentially that supply chains are becoming more broken up into tasks – things are no longer Made in China or Made in Taiwan, for example. Specific parts of the process or parts of the manufacturing process are now built in different areas and different parts of the world, so we see that in the way that the percentages of imports and the percentages of exports continue to increase, and we expect that trend to continue.

What that means is that there'll be more SME involvement in supply chains and more inter-company flows within the supply chain; the supply chain will be more dispersed; and increasingly, moving closer to the point of consumption. And this will require increased financing in the SME segments, but will also have a more negative impact from a trade finance perspective, in reducing or improving the working capital flow of cycle of companies, therefore reducing the amount of trade finance that companies need.

**ALBERTO AMO MENA:** The shift in the origins of supply chains have increased risk assessment and compliance costs, which is an important challenge for trade financiers. Industry leaders must now combine business knowledge with a deep understanding of the regulatory impact when defining their strategy.

> "Unbundling of trade – supply chains are becoming more broken up into tasks."
>
> **Michael Vrontamitis**



"The shift in the origins of supply chains have increased risk assessment and compliance costs, which is an important challenge for trade financiers."

**Alberto Amo Mena**

## It is almost impossible to have the discussion on supply chains without talking about the underlying technology and the much-vaunted digitization of trade finance. What major innovations have you seen, or are you expecting?

**STUART TAIT:** One trend is that the industry is investing in technology to meet regulatory changes through automated processes such as Financial Crime Compliance screening. As customers move towards open account solutions, this increases opportunities for technology firms to enter the trade finance market. How this trend plays out, in terms of regulation and customer requirements, remains to be seen.

Over the medium term, new payment technologies such as mobile will replace standard trade finance tools for settling simple trade flows for smaller companies. New ways of managing supply chains will also drive technological changes in the industry.

A dematerialization of trade will continue as the cost and ease of digital trade increases, augmented by 3D printing and robotics, which could shorten supply chains. This, combined with increased global consumer appetite and income to pay for services such as healthcare, education, tourism and banking, will drive an increase in trade in services.

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**MICHAEL VRONTAMITIS:** Digitalization is beyond just digitalizing trade finance, but actually digitalization of trade; we're seeing increasing moves by large companies at this stage, and I think we're heading to a tipping point sometime over the next couple of years, where more and more trade will be done digitally, and this will have an impact on trade finance.

One effect is that it'll open up and continue to open up a whole host of post-shipment and post-acceptance financing, for non-traditional non-banks players. If we say that 30% of

> "Industry is investing in technology to meet regulatory changes through automated processes."
>
> **Stuart Tait**

**"There will be a continued desire to develop new sustainable supply and sales opportunities through automation and digitalization."**

**Markus Wohlgeschaffen**

the working capital of the finance cycle is in that space, you'll have far more competition in this space emerging, and I think what the difficulty will be, is that pre-shipment, pre-acceptance financing will become more and more challenging. In my view, there are very few solutions at the moment in the marketplace that will solve that part of the supply chain. BPO is a potential solution for that, but at this point, it is not something that's taking off in a big way.

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**DANIEL SCHMAND:** Regarding digitization and its impact on our industry, the individual involved in trade finance has come to expect the same capabilities in business as they enjoy in their personal life, meaning that technological developments will continue to drive financing capabilities towards real-time, integrated, multi-device and multi-channel accessible and intuitive tools. While technology will solve many problems and can lubricate trade, it will also continue to throw up new topics of debate around regulation, standardization and risk.

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**MARKUS WOHLGESCHAFFEN:** I agree that despite the trend of political uncertainty, there will be a continued desire to develop new sustainable supply and sales opportunities through automation and digitalization – as well as the synchronization of the physical and financial supply chains. Traditional financial risk assessment techniques, such as balance sheet analysis, will be complemented by transactional financial and operational risk assessments based on big data analysis through sophisticated algorithms.

This will not only allow financial service providers to offer new products and services, but it will also further illuminate the disproportionately low default rates and risk of trade finance transactions. Of equal importance will be the ability to comply with prevailing and future compliance rules which aim to strengthen the financial system and counter financial crime. Here, too, digital processes and big data will be useful tools.

## To what extent does the digitization era bring opportunities or threats for traditional financiers? Does it open the door to further competition – and in that respect, what threat do such non-bank players carry for the traditional institutions?

**OLIVIER PAUL:** We can expect to have very fierce competition. The winners will be the ones able to deliver significant levels of investments in IT systems, innovation and new products. The optimistic scenario would be that the external impact will become more stabilized in terms of regulations and compliance, and we come back to the real world, which is competition with other banks, and we focus on quality of services, products, innovations, etc. Of course competition on pricing will remain, but in that case the cost evolution will be slightly different, because if we are able to provide a better quality of service, maybe the pricing can be adapted in accordance with this.

The very pessimistic scenario is that there is an emergence of new actors, which are not regulated as banks are, and who will take some market share from the banking industry, stemming primarily from the uncertainty facing the banking sector. It's a circling effect: if banks start to lose too much market share, it means that profitability around those products will continue to decrease, because the competition will be more and more aggressive to keep at least a piece of market share. If the profitability continues to decrease, the general management of the banks will raise the big question of whether it is worth continuing in this activity.

At the end of the day, the industry itself will be the big loser in such a case, because there will be a lot of traditional banking actors that will drastically reduce their presence in this market, letting non-banking actors to penetrate the space, but perhaps for a limited period of time. Very pessimistic and very unlikely, but it's difficult to be sure that this won't happen.

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**SABRINA M. BORLINI:** Trade drives growth via exports, and also imports which provide necessary capital equipment, technology and know-how. Trade also provides goods that are absolutely critical to many countries' economic function and lives of citizens, such as energy, food, and health supplies. However, embedded with every challenge is a significant opportunity.

> "Embedded with every challenge is a significant opportunity."
>
> **Sabrina M. Borlini**

The potential material KYC-driven cross-border retrenchment from many emerging market banks opens the door for other players to grow. We see opportunities for regional players to emerge to take a greater role in cross-border confirmations and other trade finance activity. We also see significant opportunities in capital markets as existing market investors such as institutional investors and sovereign funds recognize the value of the trade finance asset class to their portfolio allocation strategies.

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**MICHAEL VRONTAMITIS:** FinTech companies have sprung up, offering solutions across the supply chain and in particular, in post-shipment post-acceptance in the open account space. I believe, to be successful, many of these companies will likely require banks to be part of the solution. I'm not aware of a FinTech company coming in and doing direct lending with the regulatory environment that would enable it but there is definitely a disruption play there. The market is still very fragmented and while it is not clear who the winners or losers will be, banks will need to disrupt their own business models to compete, and this ultimately benefits the customer.

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**DANIEL SCHMAND:** New industry players and alternative financiers are not going away and should be taken seriously. While it is important both for the protection of corporates and banks that they are fairly and cautiously regulated, they provide new blood that will drive innovation and forward-thinking, as well as offering liquidity in areas – whether regions, industries or to SMEs – that banks may find themselves unable to cater for and that could otherwise be neglected.

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**MARKUS WOHLGESCHAFFEN:** These new and versatile non-bank entrants into the finance industry will challenge the existing business models of banks, including factoring companies, and insurers. Closer collaboration between these two financial service providers is necessary to generate new value-added products and services – for instance to develop a more efficient way liquidate risk-insured receivables – and to avoid disintermediation. Another very big challenge for trade banks is to find worthy substitutes for its ageing population of trade practitioners over the next five to ten years. Greater investment in scouting and training will be necessary.

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**ALBERTO AMO MENA:** We will certainly arrive at the point where these new players will be subject to the same regulation and compliance obligations, as they will acquire significant volumes. At this point, due diligence requirements in terms of cost and operating systems, will create such a huge entry barrier that it might end up favouring the 'traditional' players' business models rather than the new participants.

> **"A big challenge for trade banks is to find worthy substitutes for its ageing population of trade practitioners over the next five to ten years."**
>
> **Markus Wohlgeschaffen**

**The elephant in the room – and one which has been touched on several times by panelists, is the issue of regulation, coupled with compliance. I think a straw poll would tell us that this is the greatest challenge facing trade financiers in 2015. What are the main regulatory challenges you are facing? What impact are these constraints having on banks' ability to provide finance?**

**SABRINA M. BORLINI:** Commercial banks are facing two converging challenges that could put the supply of trade finance lines at risk, particularly to smaller banks and economies. First, changes in capital requirements and other regulatory requests have reduced the capital that each bank has to invest, requiring a higher return on that now more scarce capital. Second, the cost of KYC compliance has skyrocketed as requirements have increased along with scrutiny and accountability for banking clients' activity.

Thus, just as the need for return on capital is increasing, higher costs make that a challenge, particularly for smaller customers and markets, where the revenue generated may no longer clear the hurdle required to maintain the relationship or where the regulatory environment is perceived as weaker. Compliance costs and scrutiny are not expected to ease in the near term, hence the pressure will continue to build, particularly in emerging markets.

> "Compliance costs and scrutiny are not expected to ease in the near term."
>
> **Sabrina M. Borlini**

> **MICHAEL VRONTAMITIS:** Regulatory uncertainty due to the different speeds of implementation between the west and the east is the primary one for me. Global banks are currently disadvantaged relative to local and regional banks on the regulation side. This is already disrupting the business model in the short run.

The expectations on banks with respect to capital and AML regulations will continue to become tighter and more constraining for financial institutions, making it more challenging for them to be able to deliver financing at low costs, particularly to the smaller domestic corporates. It will become increasingly more difficult to provide cost-effective financing across the supply chain. This trend will need to be addressed, probably through product innovation around supply chain finance and regulators increasingly recognizing the unintended consequences of current regulations.

> **ERIC DE JONGE:** Regulatory requirements (Basel III), along with the increasing attention for environmental and social responsibilities related to financiers´ policies, will all influence trade flows and its financing. Threats of fraud, terrorism and financial crime, making use of all kinds of technologies, will also continue to put pressure on the financiers having to deal with higher costs of security and innovation to deal with these. Efficiencies, safety, compliance and service will be key elements for banks and other parties in order to continue to be active and successful in financing trade.

> **DANIEL SCHMAND:** While the dangers that regulatory changes seek to address are key and cannot be ignored – from capital to anti-money laundering, anti-fraud and reporting requirements – we must continue in our efforts to ensure

**“The expectations on banks with respect to capital and AML regulations will continue to become tighter and more constraining for financial institutions.”**

**Daniel Schmand**

that it does not obstruct the flow of trade. Banks' reputations have understandably been damaged in recent years, but their crucial central role as facilitators and supporters of trade and economic growth must be understood and encouraged. Constraints on banks may have potential unintended consequences, from raising the cost of entering into new relationships and markets to retrenching in certain directions.

**OLIVIER PAUL:** Compliance is absolutely the key trigger for banks' capacity to do business. It could go up to disruption of the business model – if it happens that compliance guidance are increasing more and more in the years to come, due to political environment and regulatory difficulties – environmental as well.

Another uncertainty may be regulation on the balance sheet of the banks, i.e. all the evolution of Basel III and Basel IV in the years to come – which could create regulatory capital requirements for the trade finance activity, which would create difficulties because of the profitability of trade finance activities, decreasing from year to year.

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**ALBERTO AMO MENA:** International trade has traditionally relied on 'bank-to-bank' relationships and sovereign states support to enable transactions, especially those connected to low-income countries, to take place. Reducing systemic risk and bank interconnectivity is one of the current goals to be achieved by regulation, though this fails to consider the particular idiosyncrasies of trade finance.

The regulatory wave is forcing banks to refocus on domestic operations. Politicians tend to ring fence domestic deposits from international exposure – affecting offshore booking – and there are incentives to refrain from extensive foreign branch networks. Minority stakes and interests in other banks' equity are penalized; reducing the transfer of technology and practices.

We are currently seeing the retreat of global banks, which is not bad news per se, but some of the new local counterparties providing customer service do not necessarily have the required product sophistication or credit and compliance standards.

> **"The regulation on the of the banks' balance sheet is another uncertainty."**
>
> **Olivier Paul**

# How can governing institutions– such as the ICC's Banking Commission – work towards making regulatory issues less obtrusive for banks, and by default, for global trade flows?

> **MICHAEL VRONTAMITIS:** Something we've been working on for a number of years – and it needs to continue – is around the understanding of the risks within trade finance, and ensuring that trade is conducted under international rules, that it gets the appropriate regulatory treatment so that we don't starve global trade from being financed. Given the low risk, self-liquidating nature of trade finance, regulation of trade finance products and facilities need to be risk-based and proportionate. Otherwise, this would be to the detriment of global GDP. We also need to figure out a way to finance trade so as to enable GDP to grow at a faster rate – particularly for smaller companies and economies, as this also helps further financial inclusion.

> **MARKUS WOHLGESCHAFFEN:** For the financial industry, one of the most significant challenges and cost drivers is the need to meet existing and future regulatory requirements. An ongoing, open and coordinated dialogue between regulators and banks is needed in order to avoid unintended negative consequences for international trade, and maintain the ability of financial service providers to support it.

> **ALBERTO AMO MENA:** The industry should harmonies AML, KYC and DD requirements, reducing its cost without affecting the quality and effectiveness of crime fighting. There must be recognition of country risk mitigation. The G20 should recommend a formal procedure to determine how to preserve trade flows in case of country events.

"The need to meet existing and future regulatory requirements is one of the most significant challenges and cost drivers in the industry."

**Markus Wohlgeschaffen**

There must also be improvement of rating agencies' understanding of trade and development of new methodologies. We have to follow the Bank for International Settlement Committee on the Global Financial System's recommendation for readiness, with central banks building safety nets and trade facilitation programmes globally, ready to be immediately effective in the event of a crisis. Banks should also do their homework: standardization of rules and instruments, knowledge exchange and development of a secondary market for trade assets.

**OLIVIER PAUL:** ICC has a great role to play in many respects, by trying to harmonize the approach of the banking industry related to trade finance. ICC is a key actor in determining what the rules that ensure the governance of trade finance products are. It's absolutely essential for ICC to continue to have and even enforce this role, giving the regulators a kind of comfort that there are big players around the table who are discussing the best way to manage trade finance transactions in a very professional way.

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**MARK AUBOIN:** We need stability. Trade finance needs a stable global financial system to expand – trade finance being inherently safe, in a global financial sector which is not always. From this standpoint, while there may be grumbles at times about the cost of prudential regulation, in the end trade finance benefits from the stability of other segments of the financial system. Let us not forget that trade finance has been hit hard by contagion of crises in other areas of finance.

**"Banks should also do their homework: standardization of rules and instruments, knowledge exchange and development of a secondary market for trade assets."**

**Alberto Amo Mena**

# What other issues would you like to see the ICC's Banking Commission address in the coming years, or any additional roles you would like to see it take on?

> "Volatility is the big enemy of the lending activity."
>
> **Olivier Paul**

**ALBERTO AMO MENA:** I would like to see the development of internationally accepted rules around factoring and forfaiting, for example, official legal opinions, harmonization of terminology and dispute resolution, and dissemination of conclusions, are also welcome initiatives in helping to achieve a level playing field in the industry.

This exercise will be also very valuable in increasing investors' demand for trade finance. Whilst on the other side, measures to transform trade assets characteristics are also needed. The export finance group and investors project should be drivers in enhancing Banking Commission activities in the coming years.

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**OLIVIER PAUL:** I think that to mitigate the external environment, the more we can demonstrate that the profession itself is organized with different entities that are able to put around the table the main actors and that are able to deliver the main solutions, good and consistent solutions in order to manage the business correctly in the frame of what is requested by the regulators in terms of supervision, levels of controls, and level of reporting, I think it will significantly contribute to the stabilization we require. As long as we talk about financing trade, volatility is the big enemy of the lending activity.

ICC can obviously play a very big role in order to give stability to the market. It acts as insurance vis-à-vis all our partners that there is an entity creating good rules, advice and guidance to the banking industry to conduct the business.

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**DANIEL SCHMAND:** I agree that the role of ICC is to support digitization, to enhance standardization and global harmonization of regulations and formats in order to level the playing field and encourage cross-border trade, to disseminate knowledge and awareness of the importance of trade finance and banks to global prosperity, and to work with regulators to ensure that effective regulations are implemented without restricting growth.

Among these issues, I think we must particularly work towards repairing and reasserting banks contract with society. It is the connection between banks and corporates that will foster this growth, and that requires trust and communication. Also, we must resist penalizing banks for their inherent role and nature and instead ensure that their resources are freely and optimally used to generate trade and economic growth.

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**STUART TAIT:** ICC should drive agreement between stakeholders on technological progress such as customs, port authorities, shipping companies, banks, because documentary trade is still too reliant on paper in the 21st century. This could be done through existing frameworks (eUCP); by greater participation in the UNeDocs project to help in the transition of the industry; or in conjunction with the WTO.

Financial crime risks should be added to the ICC's rule setting, dispute resolution, and policy advocacy activities. Documentary trade enables banks and regulators greater insight into transactions, this needs to be better understood. ICC advocacy with politicians, policymakers and regulators could support a deeper understanding of the trade finance sector and support agreement on coherence on the controls and capital requirements needed. The ICC's voice should also be heard in the debate on how barriers to trade are reduced and how greater standardisation can be introduced. As trade finance products develop, there is a case for revisiting definitions beyond documentary credits.

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**SABRINA M. BORLINI:** The availability of trade finance data remains critical, particularly now as the industry is shifting. Being able to quantify actual country to country trade finance volumes, the true cost of compliance across all cross border confirming banks, as well as the implication on available trade lines and liquidity will be essential as other financial service providers formulate their own strategies on how to address the increasing gap.

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**MICHAEL VRONTAMITIS:** What I've seen over the past five years with the Banking Commission is really this acknowledgement that there is this open account trade finance and the fact that we need to be much more stretched in the way that we address it from a rules perspective and enable it to flourish and grow. Obviously, we've had organizations like FCI and some others dealing with the part of open account financing space, and I understand that's also coming within the boundaries of ICC. My view is that we need to continue that down that path, and continue to enable financing to be much simpler for corporates in this space, particularly in the pre-shipment space. This is particularly how we enable SMEs and smaller corporates to have access to trade financing. That would be one key aspect.

**"ICC's voice should also be heard in the debate on how barriers to trade are reduced and how greater standardisation can be introduced."**

**Stuart Tait**

"I encourage a continuation of the open dialogue through the policy consultation on trade finance with the B20 and G20."

**Eric de Jonge**

**MARK AUBOIN:** As was indicated during the 2015 Banking Commission Meeting in Singapore, in addition to its important rule-making role, ICC is an important body contributing to information gathering such as its annual survey and the trade finance register, education regarding trade finance – hence the importance of the new ICC Academy – and integrating its developing countries members into trade finance markets.

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**ERIC DE JONGE:** I would also like to see involvement in discussions regarding Basel III and its capital requirements based on the data delivered for publication of the ICC Trade Register. I concur that ICC could further play a role in discussions regarding harmonization and standardization in trade documentation etc., all with the aim of fostering efficiencies and lower costs.

I encourage a continuation of the open dialogue through the policy consultation on trade finance with the B20 and G20 to exert some influence based on concerns in the industry over the development of trade and its facilitation. It would be good to continue to put more emphasis on the medium to long term trade business, and on the appetite of capital markets investors in trade assets. Furthermore I think continuing and expanding surveys and gathering of market intelligence will definitely serve the industry well.

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**MARKUS WOHLGESCHAFFEN:** The key issues are the regulatory requirements, the avoidance of any negative impact on international trade due to de-risking tendencies and safeguarding the proper provisioning and training of all participants in the trade value chain. For the first and second points,ICC should orchestrate the industry dialogue with governmental bodies and regulators. Moreover, it should continue to enlarge the set of uniform customs and practices for financial crime prevention and common nomenclature in trade, for example.

# It's crystal ball time. What is your primary outlook or scenario for trade finance over the next five years, taking us to the year 2020?

**SABRINA M. BORLINI:** Over the next several years, the trade finance gaps in emerging markets will expand, even in some of the larger emerging markets. Without significant intervention and growth of coverage among multilaterals such as the IFC and other players, there is a very real potential that some markets could see a debilitating downturn of trade finance – and that can have significant impact on their ability to trade.

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**ERIC DE JONGE:** Surely an increase of global growth in coming years will facilitate trade and financing thereof. Trade Finance more specifically would certainly also benefit from an abolishment of Russian sanctions, facilitating an increase of trade with this important and sizeable market. Easing of tensions in many African countries would open up more trade opportunities as well. At the same time it would be regarded positive if the Basel III committee would decide on a fairly low percentage of the leverage ratio, say less than 3%, which would ultimately have an effect on pricing and capacity to do Trade Finance on balance sheet.

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**STUART TAIT:** A gradual acceleration of world growth, leading to increased trade between nations. The big trade agreements on the table are concluded and implemented, bringing down barriers. Lesser developed countries continue to move up the value chain, increasing demand for trade, which supports economic development. Asia continues to develop its role in international trade, with the creation of an ASEAN network, the emergence of India and Indonesia as trade superpowers and further connectivity thanks to infrastructure investment.

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**MICHAEL VRONTAMITIS:** I'm positive on the outlook for trade finance as we expect global trade to expand. For example, there has been a lot of commentary around the possible death of documentary trade, but quite frankly, I think that it is evolving and will continue to do so in a very positive way. There will definitely be more digitization, through electronic bills of lading and all that good progress happening in documentary trade.

The real shift will be in the open account space, particularly in receivables financing and supply chain financing. And I think that's where we'll see an increase in innovation and risk appetite, in order to support the unbundling of supply chains which will continue to grow, albeit differently from the past, and in the process stimulate global trade growth. So, supply chain finance and how we finance

> "Without significant intervention and growth of coverage, there is a very real potential that some markets could see a debilitating downturn of trade finance."
>
> **Sabrina M. Borlini**

> "The most desirable next steps for the industry are quite clear, but not so easily executed."
>
> **Daniel Schmand**

> "Trade Finance has proven to be a resilient business and will continue to grow if we all, together do our homework."
>
> **Alberto Amo Mena**

those open account flows will become more critical. When I look out to 2020, I see the open account financing business continuing to grow and innovate, and the documentary trade business becoming more efficient.

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**DANIEL SCHMAND:** The most desirable next steps for the industry are quite clear, but not so easily executed. A key objective is still achieving higher levels of streamlining, integration and compatibility through standardised formats and automated processes. We may see SEPA-like initiatives spreading as globally accepted and data-rich formats improve and enhance the payables and receivables processes. Another is to ensure that regulation is protective but not restrictive, and levels the playing field rather than heightening imbalances.

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**MARK AUBOIN:** There is no serious scenario supporting a de-globalization process. Trade may not grow as fast as pre-crisis level, but trade finance should continue to benefit from a moderate expansion of trade.

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**MARKUS WOHLGESCHAFFEN:** As an optimist I will focus on the best case scenario, which is that banks will find the right answer to the challenges and opportunities posed by digitization, automation and an aging population of trade finance practitioners. Banks will be easy to deal with because they offer easy to integrate IT-platforms for their products and services. They will safeguard 100% straight-through-processing and the integration of the prevailing physical value chains of their corporate clients. I hope the BPO will be recognized as a powerful tool to reduce financial and operational risk in connection with cross-border trade transactions and to unleash trapped liquidity.

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**OLIVIER PAUL:** I hope we reach a kind of stabilization in terms of regulatory and compliance requirements, so that the banking industry is able to build a new business model, taking into account all those stabilized requirements. Then I hope we develop the capacity to provide services and financing to business in a more stabilized environment. At that time, what will become very important for the market will be the capacity of innovation and technical aspects, as well as the capacity of creating new products for the industry.

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**ALBERTO AMO MENA:** Trade Finance has proven to be a resilient business and will continue to grow if we all, together with WTO and ICC, do our homework. The retreat of some players from certain markets will cause temporal gaps, to be filled by regional or domestic entities. All open account and receivables related business will continue to increase, creating new challenges in processes, structures, legal framework and AML. Finally, still wonder for how long this high level of US$ liquidity will remain and the quest to repackage trade assets to institutional investors will expand.

# CLOSING REMARKS

**"The Survey is a blueprint for international collaboration – industry actors from around the world pool their knowledge to develop a valuable global view on the pressing issues of today in trade finance and beyond."**

**EMILY O'CONNOR**

2015 marks the 7th anniversary of the founding of the Rethinking Trade & Finance series. This ICC Survey, which had its origins in the midst of the financial crisis, is now a well-established market intelligence tool for the whole trade and finance industry. This year, with the help from our colleagues at the IDB and FIBA, we were able to shine more light on trade finance in Latin America. In 2016, the ICC Banking Commission will hold its annual meeting for the first time in Africa. It is therefore our wish is to focus in next year's issue edition on trade and trade finance in Africa – and to bring knowledge, vision and calls for action to support banks and their clients in the region to grow.

The Survey has already become increasingly inclusive of areas outside traditional trade finance instruments. Our institutional partners enabled us this year to provide the whole industry with the most relevant trends in factoring, export finance and export insurance, trade facilitation programmes from MDBs, SMEs competitiveness enhancement programmes and challenges posed by compliance developments. Looking towards the future of trade finance, next year's Survey will address key topics such as the digitalization of trade and finance, sustainable financing and the ineluctable regulatory agenda.

We take this opportunity to show the highest appreciation to our partners, survey respondent banks, sponsors and staff who contributed to the creation of this report. We also invite you to join your colleagues around the world to take part in the ICC Global Survey on Trade Finance 2016 and thus ensure the effectiveness of our shared efforts.

Thank you.

The ICC Banking Commission.

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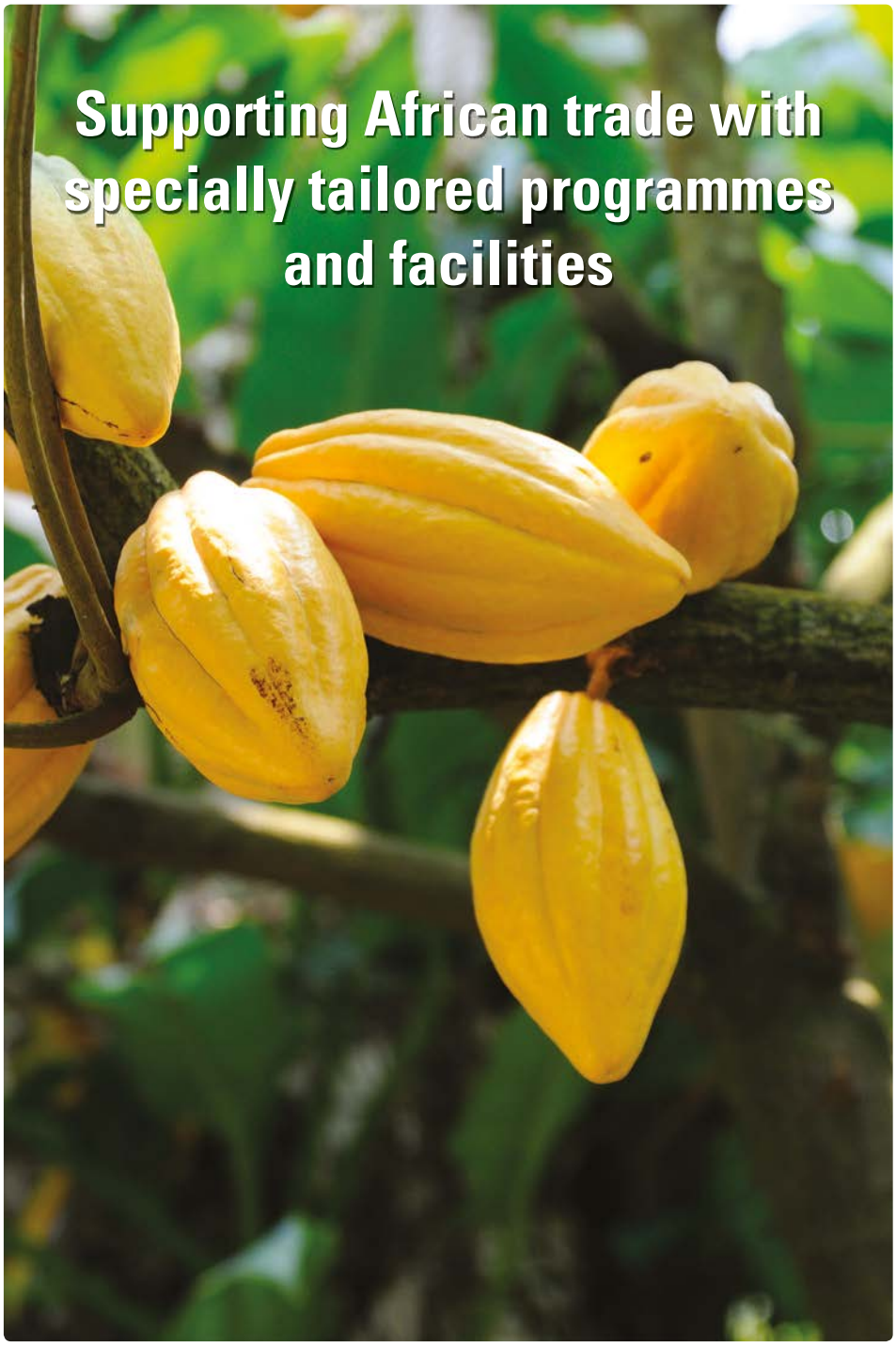


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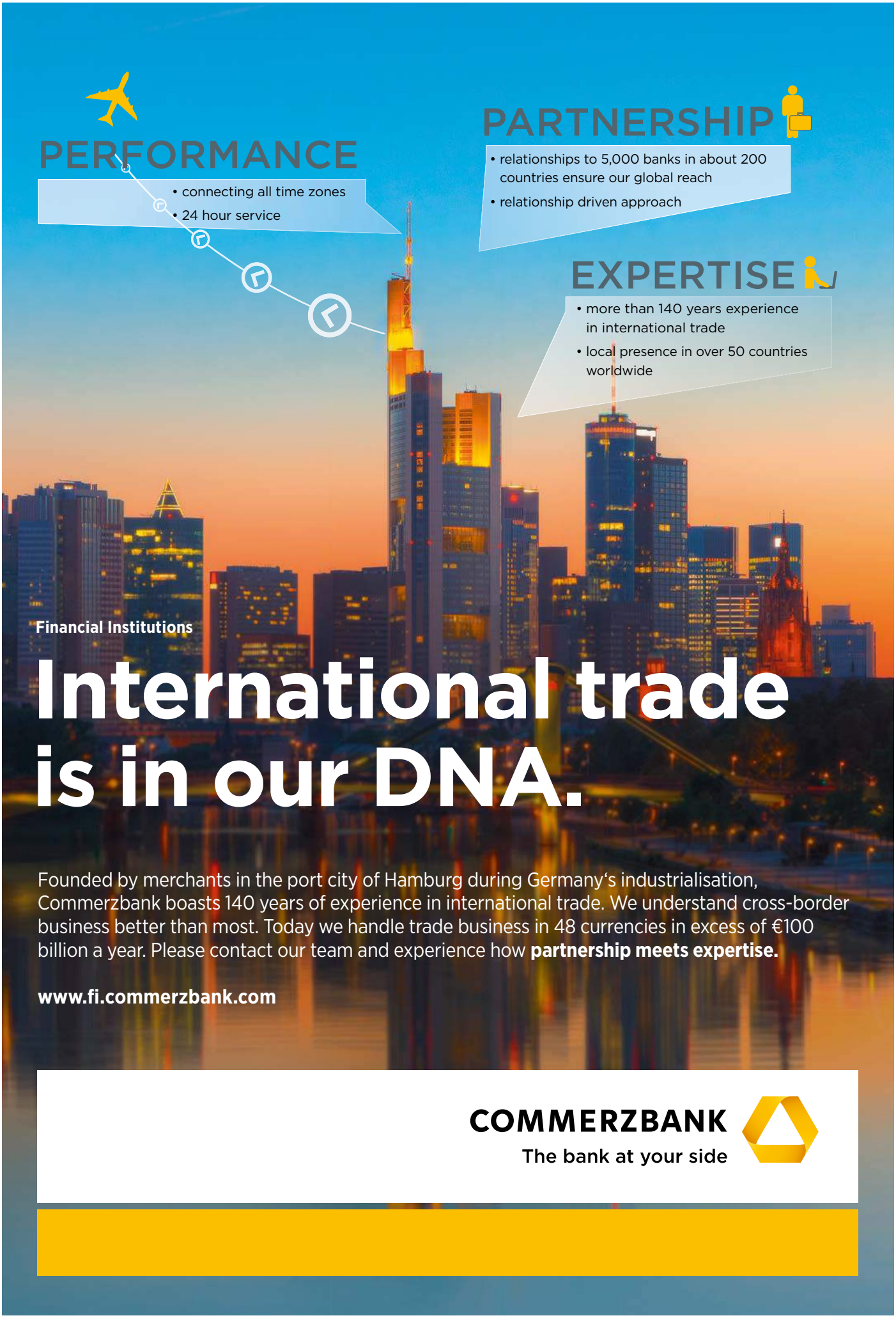
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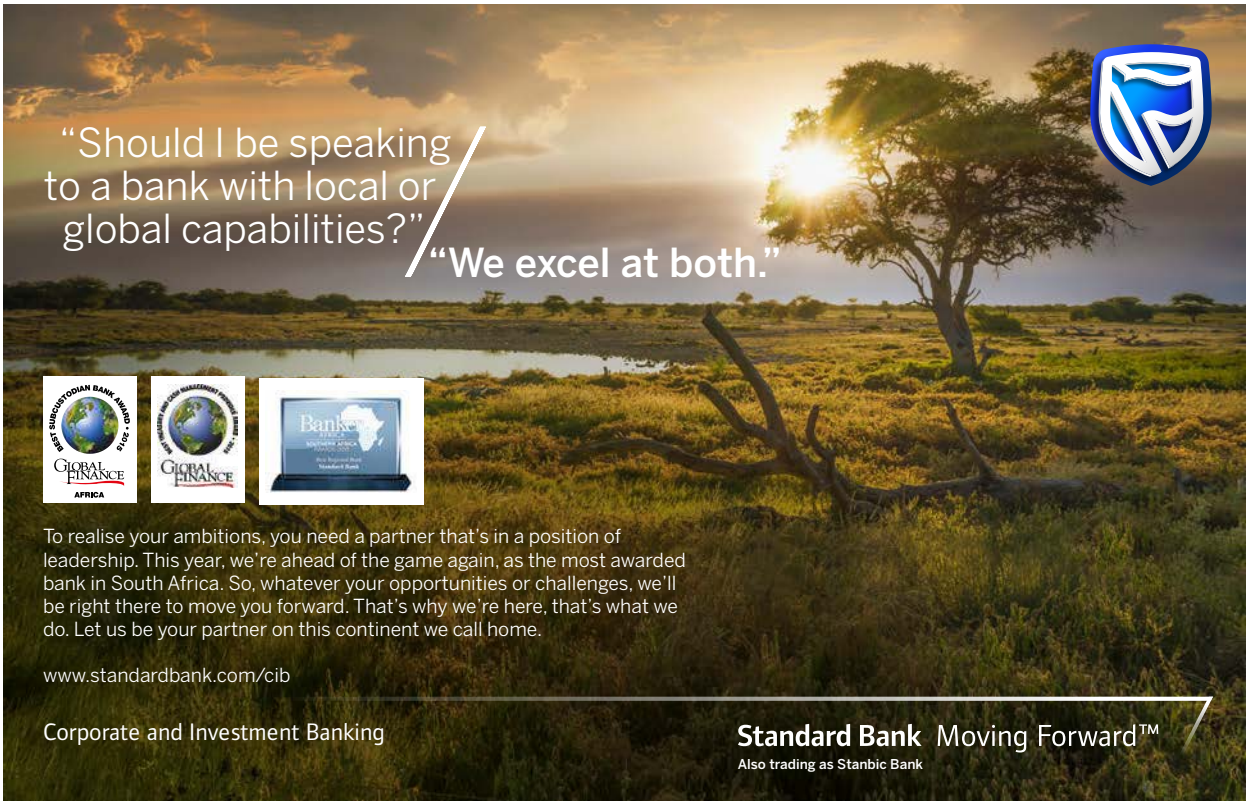


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*Third International Conference on Financing for Development – Addis Ababa: Opening session, Roberto Azevedo, Director General, World Trade Organization, July 13, 2015*

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