Sustainable trade finance and African trade

Giving an African voice to the evolving standards on sustainable finance and trade

by Kleos Advisory and ITFA,

10 November 2022

itfa.org

Prioritising sustainability in African trade: Giving an African voice to evolving global standards for sustainable trade finance.

ITFA White Paper on sustainability, trade finance and African trade

by Kleos Advisory and ITFA,

10 November 2022

itfa.org

Executive Summary

Africa's trade finance gap, estimated to be between USD 80bn to USD 120bn, has widened further over the past decade, exacerbated by the disruption to global supply chains caused by the Covid-19 pandemic. The lack of access to trade finance especially impacts Africa's SMEs, which make up around 80% of African traders, and whose banks struggle with regulatory costs to profitably finance their merchant activities. Against this background, growing ESG requirements (mainly related to climate impact) have added a further challenge for African traders.

The Sustainable Development Goals (SDGs) and the Paris Climate Agreement have been broadly adopted as benchmarks by all businesses, sectors and governments, shaping the ESG standards and regulations that are emerging. But to date the focus has been on climate action and decarbonisation of the economy. Given that Africa accounts for just 3% of world Greenhouse Gas (GHG) emissions (versus 25% for the G7 countries), this focus is misaligned with the sustainability objectives of Africa, which embrace broader environmental and social impacts, such as deforestation and the treatment of workers in the supply chain. The climate-centric approach also fails to recognise the positive role played by trade in the economy. According to World Bank data, trade makes up 50% of Africa's real GDP and employs around 80% of the population. This makes trade finance hugely impactful in terms of boosting economic growth and opportunities. In addition, African trade is directly linked to nearly all of the SDGs, notably poverty reduction, economic growth and gender inclusion.

Given the current focus of the global sustainability agenda, there is a risk that the standards being developed for sustainable trade finance could prove unworkable for African trade. These standards have been designed for multinational manufacturers and merchants in developed markets, rather than SMEs in emerging markets, and African traders will struggle to meet the data and reporting requirements being proposed. ESG is not just about decarbonisation, it is also about the need for a 'just transition', which recognises that "one size does not fit all" and which compensates for the wider social impacts of moving to a more sustainable economic model. This is especially the case in Africa, where the population is among the most vulnerable in the world to the impacts of climate change, and where most Africans work in industries that are now excluded from trade finance.

This is why we need to reframe the argument around African trade finance, recognising that African trade's high exposure to sustainability risks and impacts is an opportunity to unlock financing for African traders. Banks, regulators, international DFIs and investors need to recognise that trade finance is remarkably low risk and comes with a high level of governance embedded in its structure. This includes mediating bank regulation, detailed credit analysis, setting KYC and documentation requirements and implementing robust monitoring processes. African trade finance is therefore the perfect tool for achieving the SDGs, as trade is linked to all parts of the economy and the supply chain. This gets to the core of the UNEP-FI's Principles for Responsible Banking (PRB), which call on financial institutions to embrace the concept of 'double materiality', assessing both their financial and ESG impacts and doing everything in their power to minimise the negative impacts and maximise the positive ones.

African banks will need to play a leading role in this process, providing the essential bridge between international liquidity providers and African SME traders. Working together, African banks can break the logjam, aggregating revolving trade portfolios which can then be financed by international banks, DFIs and investors. But if African banks are to play this role, international lenders need to put more trust in them, especially in their ability to judge the sustainability impacts of their lending. The key to unlocking this opportunity is building capacity in African banks, and this is where regulators and governments can provide support, training staff on the ESG / sustainability impacts of trade, helping them to develop meaningful metrics to measure their performance and reap the full benefits of digitalisation. There is also a large opportunity to develop a new generation of sustainable trade finance products.

Given the potential negative impacts that emerging Western-focused ESG standards could have on African trade, and the huge potential of African trade finance to deliver on the SDGs, African banks and institutions must make their voices heard.
This White Paper proposes five priorities for action:

i. Build ESG capacity in African banks, corporates and SMEs;

ii. Develop appropriate metrics to measure sustainability for African trade finance;

iii. Allow sufficient time for African banks, corporates and SMEs to gradually shift towards sustainable finance standards;

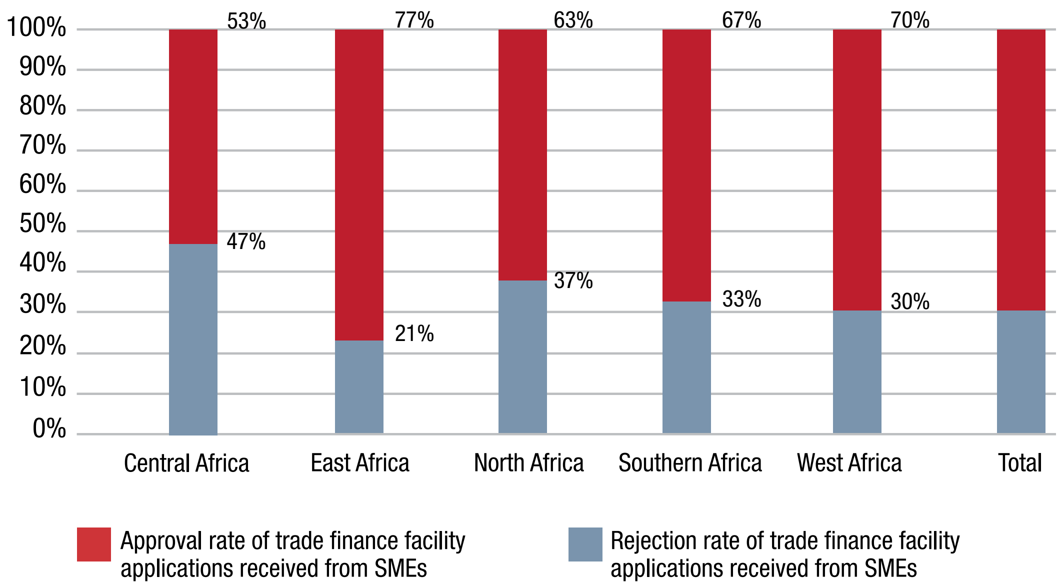
iv. Develop sustainable financial products for African SME traders; and

v. Secure the support of the key stakeholders in African trade to ensure that Africa's voice is heard in the debate over sustainability standards.

1. What is driving Africa's trade finance gap, and why is it so persistent?

Despite concerted efforts by multilateral agencies, banks and African governments, Africa's trade finance gap has continued to widen over the past decade, worsened by the disruption caused to the global economy and supply chains by the pandemic and geopolitical events. Africa's trade finance gap especially impacts SMEs, which make up around 80% of African traders. In the ICC's 2016 Trade Survey, the AfDB identified the inability of SMEs to obtain trade finance facilities from their financing institutions as the root cause of the trade gap. A subsequent report in 2020 by the AfDB and Afreximbank found that over the period 2011-19 SME trade finance rejections ranged from 23% in East Africa to 47% in Central Africa.[1] This situation has been exacerbated by the recent USD liquidity squeeze which has increased African countries' debt-servicing costs and as a consequence has further reduced the availability of USD for African traders.

Chart 1: Average rejection and approval rates of trade finance facility applications received from SMEs, by African region, 2011-19



Source: AfDB & Afreximbank

So why is Africa's trade finance gap so persistent? In part, the trade finance gap reflects structural factors. Most African countries rely on commodity exports to build up their foreign currency reserves, but as most commodities are exported raw (e.g. cocoa beans, metal ores, crude oil, uncut timber), the majority of their value is captured in external markets and not in Africa itself. This puts huge pressure on the current account to pay for imports of food, fuel and consumer goods, limiting

1 AfDB & Afreximbank, Trade Finance in Africa: Trends Over the Past Decade and Opportunities Ahead, September 2020, https://www.afdb.org/en/documents/trade-finance-africa-trends-over-past-decade-and-opportunities-ahead

African traders' access to USD, especially in the current climate of record high food and energy prices and rising interest rates.

But the primary factor driving the trade finance gap is international regulation on investment banking capital and liquidity which greatly reduces the profitability of trade finance for international and African banks. Despite all the empirical data in the ICC Trade Register, which clearly demonstrates that African trade finance has a remarkably low product default rate (which at a regional level is often better than 'developed' markets), banks must hold large 'risk weighted' capital costs. The short-term liquidity ratio requirements of Basel III increase treasuries' costs, as they are required to match short-term liquidity with short-term trade finance tenors.

A further constraint of Basel III concerns Loss Given Defaults (LGDs). In order for trade transactions to be approved by banks and qualify for lower LGDs, which lowers the cost of capital, traders must provide detailed information about the transaction, including the importer/exporter, goods, origin, tenor, shipping, ports and other documentation. For major trading houses this kind of information is easily obtainable, but for most African SME traders – which deal in multiple small transactions with short tenors and which lack efficient data management systems – this can prove impossible, forcing them to fund their transactions at uneconomic rates out of their African banks' treasuries. These reporting requirements make it impossible to refinance the banks' SME trade portfolio, which is one of the few tools EM banks' treasuries can use to manage the bumpy reality and timing of trade cash flows.

Given these factors, financing Africa's SME traders is just not profitable for banks which prefer to divert their scarce FX and capital towards other products that offer better returns. Even when international banks do have appetite for African trade finance risk, any deal worth less than USD 5mn is not worth the time and resources needed to assess the risk and structure the lending. At a stroke, this excludes the majority of African traders, who might be looking for financing from as little as USD 10,000 (for new machinery or equipment) to around USD 100,000 (for larger trades and business expansion). At the same time, African banks are incentivised to park their funds in government bonds and T-bills, where they are guaranteed near zero risk and high returns. This means banks are not playing the critical role of intermediation for African SME traders, locking them out of both USD liquidity and local currency capital and liquidity.

Africa's banks and regulators have long been aware of this problem and have developed a number of initiatives to support Africa's SME traders. For example, Afreximbank's Pan-African Payment and Settlement System (PAPSS) could provide a major boost for cross-border trade, enabling African traders to settle payments in their own currency without having to use USD. Similarly, the African Continental Free Trade Area (AfCFTA) holds great promise for opening up tariff-free and borderless trade for African SMEs. Although both initiatives are critically important to the growth of African intra-regional trade flows and payments, they do little to address the core problem for African SME traders: how to get the financing in the first place. And with most cross-border trade, both within and outside Africa, continuing to be transacted in USD, SME traders are faced with the same barrier.

Useful tools are being developed to unlock trade finance for SME traders, for example structured LCs about which ITFA produced a guide in April 2021 (ITFA, 2021). Structured LCs are a prime example of home-grown, trade-tenor, hard currency liquidity which can be used to fund African banks' SME trade portfolios, as they require no detailed underlying substantiation. African regional banks can use these as a source of trade liquidity to support trade flows in other countries without using up precious foreign exchange reserves. However, the purpose and mechanics of structured LCs are poorly understood by the market and they have earned an undeservedly poor reputation. As a result, they are difficult to sell into the secondary market and some DFIs and insurers won't risk share in them, forcing their discounting banks to hold onto them until maturity, which stunts their beneficial scale.

Africa's SME traders have also yet to reap the full benefits of the digitalisation of trade, from easier KYC and client onboarding to quicker and cheaper digital payments and capturing the intricate characteristics of each individual transaction. Instead, most of them continue to operate with paper, cash and manual records. This means that a new model is needed that moves away from large, lumpy, long-tenor trade assets to one which can deliver trade finance for multiple small, high-velocity short-tenor trades and working capital facilities.

> **Florian Wicht, Regional Head for Trade & Supply Chain Finance - Africa, IFC**
> ***"We need more emerging market voices in the global ESG debate so that the standards that emerge do not penalise traders in these markets."***

2. Emerging sustainability standards could hurt African trade

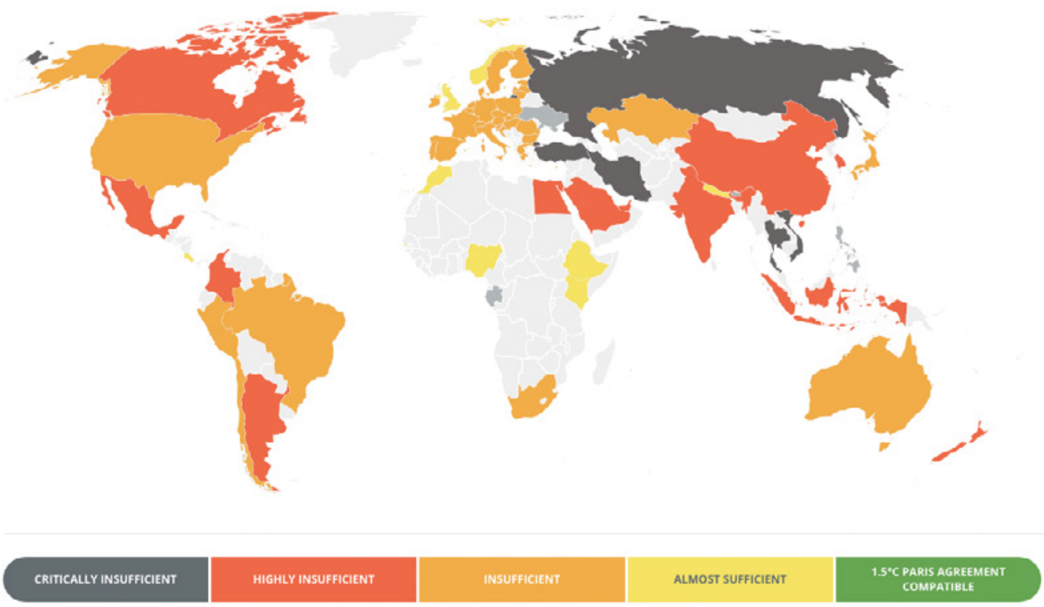
Against this backdrop, sustainability poses an additional challenge to African traders. The global sustainability agenda is currently defined by two guiding frameworks, the Sustainable Development Goals (SDGs) and the Paris Climate Agreement. These provide the benchmark against which all government, regulatory and corporate sustainability strategies are aligned. While the Paris Agreement is focused on decarbonisation – with a target to limit global warming to no more than 2 degrees Celsius and reach Net Zero by 2050 or earlier – the seventeen SDGs are more wide-ranging, covering all the issues that must be addressed to ensure a sustainable economy, a stable climate and ecosystem, and a just society.

These two frameworks have been interpreted through various other frameworks, the most commonly used being ESG, which divides sustainability factors and impacts into three components that can be tracked: Environmental, Social and Governance. The ESG approach was first developed for the investor sector but it has been widely adopted by all businesses, sectors and governments, shaping the sustainability standards and regulations that are emerging.

However, the SDGs were designed to be high-level, global goals which each country can interpret in its own way when designing transactional frameworks and taxonomies. This has spawned a spectrum of ESG definitions and standards, most of which betray the confirmation bias of their authors, who tend to be developed market policy makers. As a result, to date the focus has been on climate action and efforts to decarbonise the economy, for example with the creation of the Taskforce on Climate-related Financial Disclosures (TCFD), which is now becoming mandatory in G7 markets. This has pushed broader environmental issues (other than climate) as well as social issues into the background, which is detrimental to Africa, and African trade, for several reasons.

First and foremost, Africa accounts for just 3% of global Green House Gas (GHG) emissions. In comparison, the G7 countries together account for 25% of global emissions.[2] This imbalance is reflected in the country assessments carried out by Climate Action Tracker, which lists five African countries (Ethiopia, Kenya, Morocco, Nigeria & The Gambia) in the seven best performing countries, ranked as ‘Almost Sufficient’ for meeting the Paris Agreement targets, while major economies such as the USA, Germany and Japan are ranked as ‘Insufficient’.[3] Moreover, Africa’s 3% share of global emissions is concentrated in just a handful of carbon-intensive economies, namely South Africa, Nigeria and in North Africa.

Chart 2: Greenhouse Gas (GHG) emissions by region, 2022



Source: Climate Action Tracker

2 Science Based Targets, 4 charts reveal G7 countries need enhanced corporate climate action, June 2021, https://sciencebasedtargets.org/blog/4-charts-reveal-g7-countries-need-enhanced-action.

3 Climate Action Tracker, https://climateactiontracker.org/countries/.

The current global focus on decarbonisation is therefore misaligned with the sustainability objectives of Africa, which embrace broader and equally important impacts. These include environmental impacts other than climate change, such as deforestation, biodiversity loss and plastic pollution of the oceans, and social impacts, which range from worker pay and conditions and gender equality to the infringement of indigenous land rights. Where these broader impacts have been identified in Africa's supply chains the focus has tended to be on the negative, for example highlighting child labour in West Africa's cocoa sector or the contamination of the environment and water sources caused by artisanal mining.

But viewing African trade through this lens ignores the positive role trade plays as a driver of the economy, financial inclusion and business generation. According to World Bank data, trade makes up 50% of Africa's real GDP and employs around 80% of the population. This makes trade finance hugely impactful in terms of boosting economic growth and opportunities. In addition, African trade is directly linked to nearly all the SDGs, in particular SDGs 1 (No Poverty) and 2 (Zero Hunger) by providing employment and livelihoods to millions of Africans, as well as broader sustainability objectives such as the fair treatment of workers (SDG 8), reduced inequalities (SDG 10) and sustainable consumption and production (SDG 12). Gender equality (SDG 5) has particular relevance in the African context as African SMEs are predominantly owned and run by women, especially micro-SMEs of 1-6 employees. In this way trade finance directly impacts the parts of the supply chain that desperately need financing, and in the process it provides livelihoods for millions of African farmers, processors and traders, and their families and communities.

GIven this imbalance in the global sustainability agenda, there is a growing risk that the global standards being developed for sustainable trade finance could prove unworkable for African trade. This is because these standards have been designed for multinational manufacturers, rather than SMEs in emerging markets, and African traders will struggle to meet the data and reporting requirements being proposed.

A case in point is the initiative being developed by the ICC, which published a positioning paper with proposed sustainable trade finance standards for industry consultation in November 2021.[4] Recognising that global frameworks for sustainable finance are not well-suited to deal with the complexities of trade, where a single trade transaction can involve 20 different parties and numerous kinds of goods, services and raw materials, the ICC divides trade into five components. These measure sustainability of the good/service, the seller/origin, the buyer/destination, the transition/transportation and the purpose of the trade.

While this approach simplifies current procedures and could provide the basis for the standardisation of sustainability metrics for global trade finance, it could prove unworkable for most African SME traders. Few of them have the data required to quantify the sustainability of the goods they trade in millions of tiny transactions

---

4 ICC, ICC Standards for Sustainable Trade and Sustainable Trade Finance, November 2021, https://iccwbo.org/publication/icc-standards-for-sustainable-trade-and-sustainable-trade-finance/

each year, and most have no idea who the final buyer is or the ultimate purpose of the trade. Adopting this approach could shut African traders out of obtaining financing for future trade transactions as the world transitions to a fully sustainable supply chain.

> **Benedict Oramah, President and Chairman of the Board of Directors, the African Export-Import Bank (Afreximbank)**
> ***"One size doesn't fit all. We need African voices in this debate so that the sustainable trade finance standards that emerge actually work in Africa."***

This is why it is essential that the debate on sustainable trade finance includes an African voice and perspective. If standards are developed and adopted that do not take into account the reality of African trade and SMEs, they could worsen rather than improve the continent's trade finance gap. At the global level, the trade finance sector has already been through this experience during the roll-out of the Basel III regulations which unduly (and unintentionally) penalised trade finance, notably through the Liquidity Coverage Ratio (LCR) requirement. This prompted industry-wide engagement with the Basel Committee, led by the WTO's Trade Finance Expert Group, which eventually resulted in an easing of LCR requirements for trade finance. However further regulatory changes are on the horizon, when Basel IV is implemented, including the ending of the LGD attenuation for trade finance, which will further increase the capital cost to trade financiers.

While this process of regulatory change is underway, it is essential that the industry does not repeat previous mistakes and introduce standards that are unworkable in Africa and that end up penalising SME traders. There must be a 'just transition' for Africa, which recognises and compensates for the wider social impacts of moving to a more sustainable model. Africa's population is among the most vulnerable in the world to the impacts of climate change, and if there is an aggressive shift towards decarbonisation without provision for the potential negative social impacts, it could make a difficult situation even worse. For example, many banks are withdrawing from coal financing, which could devastate the communities in South Africa that depend on the coal mines for their livelihoods. These broader social impacts, which often fall under the radar, must be considered if the transition towards a climate-neutral economy does not unjustly impact those least able to manage the impacts of climate change.

> **Albert Rweyemamu, Senior Underwriter, African Trade Insurance Agency (ATI/ACA)**
> ***"If we are to have a just transition, we need to prepare, adapt and mitigate."***

3. Africa's exposure to sustainability risks could be a benefit, not a liability

If we are to address these challenges and ensure that African trade finance is both sustainable and accessible to all traders, especially the SMEs, we need to reframe the argument. This means recognising that African trade's high exposure to sustainability risks and impacts is actually a huge opportunity to unlock financing for traders and to develop sustainable trade as an asset class in its own right.

First, banks, regulators and international DFIs need to recognise that trade finance is remarkably low risk. According to the ICC Trade Register, which aggregates data on over 38 million global trade finance and export finance transactions worth over USD 19 trillion, the transaction default rate for export LCs is just 0.01%.[5] This compares with a historical corporate default rate of 2-3%, i.e. 200-300 times higher. The low default rate of trade finance partly reflects the fact that trade finance is not dependent on the underlying SME or corporate performance. But it is also the result of banks' ability to roll outstanding facilities into new ones, thus avoiding a default. This gets to the very nature of trade finance which is flexible and dynamic.

However, banks' economic models, which are based on debt and credit, fail to account for this intrinsic strength of trade finance and the lower risk of default that it involves. This affects trade in all markets, both industrial and developing, but impacts especially hard in Africa. For example, under Basel III banks must use theoretical obligor ratings which are capped at the sovereign grade. This means that a USD 10 million LC issued by a Ghanaian bank, which in reality should have a AAA rating or better (as the likely default rate is practically zero), is rated CCC with a probability of default of 14.48%, and a confirming bank would need to hold more than USD 26 million of capital costs.

Second, governments, regulators and banks need to recognise that trade finance is the perfect tool for achieving the SDGs. As trade is linked to all parts of the economy and the supply chain, it can be used to deliver positive sustainability impacts that go well beyond climate, embracing all elements of E, S and G. This approach has already been trialled in initiatives such as Aid for Trade by the WTO, which aims to build trade capacity and infrastructure for developing countries so that they can benefit from trade opening. But if the focus is switched to deploying trade finance directly to the supply chain, rather than capital investment to improve the infrastructure, the positive sustainability impacts can far outweigh the economic impacts of large-scale projects.

Compare, for example, the sustainability impacts of a 10-year USD 500m financing for a new mine, railway and port infrastructure with an equal amount in short-term trade finance for thousands of SME traders. While the new mine, railway and port

---

5 ICC, Letters of credit (LCs): recognizing the value of simple trade instruments, July 2016, https://iccwbo.org/media-wall/news-speeches/letters-of-credit-lcs-recognizing-the-value-of-simple-trade-instruments/

will over time increase the foreign exchange earnings of the country, supporting real GDP growth and the currency, relatively little value from this enclave project will be transferred to the general population. In comparison, USD 500m in trade finance offered to thousands of SMEs will have a multiplier effect, delivering funding throughout the value chain and down to the elusive 'Last Mile', directly supporting the livelihoods of millions of Africans who depend on trade. This is not to say that project finance for developing Africa's industry and infrastructure is not beneficial to Africans, but rather that deploying funding for trade finance can a have much greater positive social and economic impact, and more quickly too.

And third, governments and regulators need to recognise that trade finance, by its very nature, comes with governance embedded in it. The high level of KYC and documentation requires sound governance and this is reflected in the extremely low level of default of trade finance. This makes trade finance an ideal tool for driving sustainability goals, such as preventing deforestation or ensuring farmers' children are fed and are in school, as well as for monitoring impacts and progress with meeting ESG targets.

Viewed from this perspective, African trade's exposure to sustainability risks and impacts is not a liability, but rather an opportunity to drive the sustainability agenda and ensure positive impacts for both the environment and society. This approach is aligned with the UNEP-FI's Principles for Responsible Banking (PRB), which call on financial institutions to embrace the concept of 'double materiality'. This requires banks to take a different approach to assessing their impacts, focusing not just on financial impacts (profits or losses) but also on sustainability impacts. These include impacts on the bank itself, from climate events (e.g. flooding of branches) and regulatory changes, to the impacts caused by the activities of the companies they lend to. The PRB calls on all banks to understand these impacts, minimise the negatives ones and maximise the positive ones. Trade finance could be the perfect tool for delivering on the PRB's objectives, which are aligned with the SDGs and Paris Agreement, for example by helping reduce biodiversity loss (by linking finance to progress on ending deforestation) or by improving farmers' incomes (by requiring clients to pay farmers a living income and provide evidence for it).

> **George Wilson, Head Institutional Trade Finance, Investec:**
> ***"We need to ensure that the sustainable trade finance standards that emerge take into account the context of African trade; if not, they could make the trade finance gap worse."***

4. African banks will play a key role in unlocking the potential for sustainable African trade finance

Given its potential to drive the implementation of the SDGs, sustainable African trade finance could become an alternative asset class in its own right. There are currently trillions of USD in assets being held by pensions funds, asset managers and investors that are looking for sustainability investments. To date, only a trickle of these funds have made their way into Africa's trade value chain, reflecting the widespread but misguided view that African trade is high risk and has sustainability impacts that are overwhelmingly negative. But if the narrative on African trade finance can be changed, and investors can view African trade finance as a gateway to achieving the SDGs, it could unlock a potentially bottomless pool of liquidity to fund African trade transactions.

African banks will need to play a leading role in this process, providing the essential bridge between international liquidity providers (e.g. banks and impact and alternative fund investors) and African SME traders. African financial institutions are, after all, the only institutions that know the traders and that can originate transactions on the ground. An international bank simply wouldn't know where to start and the various NBFIs, microfinance and factoring companies and DFI-sponsored programmes that are seeking to inject financing directly into the supply chain are a drop in the ocean. Working together, African banks can break the logjam, aggregating revolving trade portfolios which can then be financed by international banks, DFIs and other liquidity providers.

> **Emeka Uzomba, Representative of the AfCFTA in charge of financial services**
> ***"African banks and other financial institutions are the key pieces in the puzzle. They know the Afican SMEs and can provide a bridge between them and the international banks, investors and DFIs."***

But if African banks are to play this role, international lenders need to put more trust in them, especially in their ability to judge the sustainability impacts of their lending. This is the classic 'chicken and egg' problem: if international banks don't have sufficient trust in African banks to support their African SME trade transactions, African banks will have little incentive to seek out these SMEs and structure deals for them. But to build this trust, banks and investors need evidence that their money is being used for sustainable trade transactions, and today the focus is on environmental issues such as carbon emissions and deforestation. This puts a huge evidential burden on SMEs and is unworkable for millions of small trade transactions.

The key to unlocking this opportunity is capacity building. Every bank in the world, not just in Africa, is grappling with the challenge of training staff on ESG issues and developing risk and credit management systems that measure and track ESG impacts. Some of the largest banks, such as Barclays, HSBC and Citi, are well advanced in this process, but most banks are in the early stages, and in developing markets many have barely started. This requires a major drive to build capacity in African banks, train staff on the ESG impacts of trade (both positive and negative) and develop metrics to measure and interpret ESG performance.

This is where regulators, DFIs and intra-African institutions such as the AfCFTA can play a key role, building on their existing work to train bank and corporate staff in ESG issues, share best practice and knowledge, and develop standards and metrics that are appropriate and workable. This process should be supported by the automation of data collection and analysis, ensuring Africa's Banks, corporates and SME traders reap the full benefits of digitalisation. There is also a huge opportunity to develop a new generation of sustainable trade finance products. These can include ‘push factors’ such as lower interest rates or better payment terms if ESG targets are met.

Once there is progress on building capacity, African banks can be trusted to play the role of intermediary between international liquidity providers and African SME traders, bridging the gap between the vast unmet demand for trade finance from African traders and the appetite of investors for sustainable investments.

> **Lamin Drammeh, Head of Trade Finance Division, African Development Bank**
> ***“African regulators will play a key role in creating the conducive regulatory environment and together with other stakeholders in building capacity in African banks on ESG issues.”***

5. Calls to action and recommendations

Given the potential negative impacts that developing Western-focused ESG standards could have on African trade, and the huge potential to develop sustainable trade finance as an investment class, African banks and institutions must make their voices heard.

In order to achieve this, this White Paper proposes five priorities for action:

i. **Capacity building for African banks, corporates and SMEs,** to help them understand and quantify the sustainability risks and impacts of trade and to guide them in integrating these risks into their business planning and risk management. Major institutions such as the IFC, the AfDB, Afreximbank and the AfCFTA can play a key role in supporting this priority, through offering training, expert advice and financing;

ii. **Develop appropriate ESG metrics** to measure African trade finance, both to facilitate finance and risk taking and also to build the case that African trade is the most effective tool for delivering on the broad SDG objectives;

iii. **Give African banks, corporates and SMEs sufficient time to work through this process** and embed sustainability in their business models. This should involve securing Africa a longer timeframe for adopting sustainable trade finance standards than in Western markets, and the development of a homegrown roadmap that is phased, realistic and aligned with Africa's broader sustainability objectives (i.e. not purely focused on climate action). This addresses the need for an appropriate just transition, given Africa's low share of global GHG emissions and the vulnerability of its population and economies to the impacts of climate change;

iv. **Develop sustainable financial products for African SME traders,** which could involve the next generation of structured LCs and financial instruments linked to ESG metrics and targets; and

v. **Secure the support of the key stakeholders in African trade,** including the regulators, financial institutions, corporates & traders, to ensure that Africa's voice is heard in the debate over sustainability and that the standards that emerge for trade finance do not inadvertently impact African trade negatively.

We call on all regulators and institutions involved in developing standards for sustainable trade to respond to these calls to action and we welcome cooperation with our partners, both international and in Africa, to drive forward this agenda.

Bibliography & sources

- AfDB & Afreximbank, *Trade Finance in Africa: Trends Over the Past Decade and Opportunities Ahead*, September 2020, https://www.afdb.org/ en/documents/trade-finance-africa-trends-over-past-decade-and-opportunities-ahead

- ICC, *ICC Standards for Sustainable Trade and Sustainable Trade Finance*, November 2021, https://iccwbo.org/publication/icc-standards-for-sustainable-trade-and-sustainable-trade-finance/

- ICC, *Letters of Credit (LCs): recognizing the value of simple trade instruments*, July 2016, https://iccwbo.org/media-wall/news-speeches/letters-of-credit-lcs-recognizing-the-value-of-simple-trade-instruments/

- ITFA, *The African SME trade gap, COVID-19 and practical solutions*, November 2020, https://itfa.org/the-african-sme-trade-gap-covid-19-and-practical-solutions-nov-2020/

- ITFA (2021), *The ITFA Guide to Structured Letters of Credit* (online). Available at: https://itfa.org/wp-content/uploads/2021/05/ITFA-Structured-Letters-of-Credit-Guide%5EJ-May-2021.pdf

- Science Based Targets, *4 charts reveal G7 countries need enhanced corporate climate action*, June 2021, https://sciencebasedtargets.org/ blog/4-charts-reveal-g7-countries-need-enhanced-action

- Wilson, George & Faure, Derryn, *African trade finance and sustainability – a question of systemic liquidity and ESG standardisation*, TFG, July 2022

- Wilson, George & Faure, Derryn, *African ESG trade finance realities – the wood and the trees*, GTR, April 2022, https://www.gtreview.com/magazine/esg-trade-issue-2022/african-esg-trade-finance-realities-wood-trees/

- Wilson, George & Faure, Derryn, *Qualifying sustainability for African trade finance*, GTR, January 2022, https://www.gtreview.com/magazine/commodities-issue-2022/qualifying-sustainability-african-trade-finance/

- Wilson, George & Faure, Derryn, *African FI Trade Finance – Probably the best alternative investment product in the World, GTR, 2022* (not yet published)

Interviewees

- Makiko Toyoda, Global Head of GTFP (Global Trade Finance Program), IFC
- Florian Wicht, Regional Head for Trade & Supply Chain Finance - Africa, IFC
- Gwen Mwaba, Director & Global Head of Trade Finance, Afreximbank
- Edmund Bala-Gbogbo, Head of ESG, Afreximbank
- Emeka Uzomba, Senior advisor to Afreximbank and representative of the AfCFTA in charge of financial services
- Albert Rweyemamu, Senior Underwriter, African Trade Insurance Agency (ATI/ACA)
- George Wilson, Head Institutional Trade Finance, Investec
- Lamin Drammeh, Head of Trafe Fiannce Division, African Development Bank

This report was produced in collaboration with the ITFA team and Dr Tedd George, Chief Narrative Officer of Kleos Advisory Ltd.