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What the pandemic means for future access to trade finance

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From a data revolution to fairer access to finance. COVID-19 has changed everything

Trade financing – whether in its traditional, mature form or in the nascent but fast-growing supply chain finance space, has a history of relative resilience and robustness in times of crisis. It is designed with a view to facilitate trade under the most challenging of conditions, whether in terms of commercial complexity, political risk, macro-level shocks, and even in extreme cases of civil unrest.

The early days of the COVID-19 pandemic demonstrated this resilience. Long-established, broadly accepted, and respected rule sets such as the various International Chamber of Commerce (ICC) rules governing trade finance proved to be well-functioning, with negligible levels of pandemic-induced abuse of process. Banks, insurers, and trading parties have continued to respect their obligations, honour their commitments and have generally "stayed in lane" as far as accepted industry practice.

The evolution of the COVID-19 crisis, unprecedented in its dual public health and global economic character, has created an urgent imperative to digitalise trade financing as well as trade itself, and in this respect, the trade finance industry has responded decisively, quickly, and effectively in enabling the critical flow of trade.

Trade financiers have clearly been part of the solution in enabling trade, as we all work our way through the crisis.

The COVID-19 pandemic has, alongside its devastating human cost, forced a shift in the spectrum of social, economic, and environmental priorities around the world. This shift includes a heightened awareness of the critical importance and vulnerability of small businesses – including ecommerce ventures and digital channels – as a clear result of the COVID-19 pandemic and its ancillary consequences.

Additionally, the evolving linkages between trade, environment, social, and governance issues as well as sustainability, are brought sharply into focus by the crisis, not least because of supply disruptions in a range of the critical products.

Trade finance is rightly increasing its engagement in, and alignment with, these issues, partly through the work of the ICC but also at the level of individual market players, and in the context of the increased visibility among senior leaders in business, government, academic, and international institutions.

Access to finance (A2F) remains a perennial challenge for SMEs in particular, with indications of widening gaps in SME

finance, finance of women-led enterprises, and trade finance to some degree. Thus far, with the critical support of international organisations, multilateral development banks, development finance institutions, and export credit entities, we have not experienced anything remotely resembling the complete engine seize-up in trade, we saw in the 2008 crisis when trade finance all but evaporated due to the interbank lending freeze linked to concerns about exposures to toxic mortgage assets.

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The significantly higher level of visibility of trade finance in gatherings and working groups such as the B20/G20, OECD, and elsewhere, including through a new C-level advisory group initiated under the auspices of the ICC, combine to help maintain senior-level policy visibility for trade finance, and to ensure access to adequate levels of trade-enabling liquidity.

The unprecedented attention around supply chain resilience, sourcing concentration risk, and related considerations that first surfaced in the context of US/China trade tensions continue to grow as we consider these issues through the lens of the COVID crisis. Financing will be linked to supply chain resilience, and will be critical to enabling any meaningful diversification of concentration risk.

These issues are particularly urgent in the context of vaccines, PPE, and other medical and security products and their related supply chains. The work of the Asian Development Bank and others around PPE supply chain mapping, as well as assuring access to adequate levels of liquidity in critical supply chains, is illustrative of how quickly energy and resources have been deployed to address COVID-19 related challenges. Public/private partnerships on the logistics side are equally illustrative.

It must be noted, however, that there is broad expectation of a wave of general business defaults, especially but not exclusively among SMEs off the back of the COVID-19 lockdowns. The degree to which this default wave flows into trade finance, or is somehow offset through government support programmes and/or temporary changes in the way debt is managed across the globe, remains to be seen. The default wave, coupled with supply chain reconfigurations motivated by the need to offset concentration risk, may complicate the commercial and competitive landscape for SME suppliers. With some evidence of interest in near-shoring, emerging market-based SMEs may find their already difficult circumstances amplified by the COVID-19 crisis.

The search among investment and asset managers for attractive alternative investments has been amplified and made significantly more urgent by the persistent crisis. As banks consider how best to create additional balance sheet and risk capacity in order to underwrite more trade finance business, the notion of distribution of assets to non-bank players shows signs of gaining, or regaining, traction, with a growing community of investors looking to trade finance as a compelling and uncorrelated asset class.

This development, coupled with work by the ITFA, ICC and past work by BAFT on widely-used enabling documentation, promises to create significant additional trade financing capacity "in the system" by bringing net new capital to the financing of trade. This development may require some time to achieve scale and critical mass, but with the right combination of initiatives it has the potential to be a significant, positive reshaping of the trade financing landscape.

The positive potential includes increased deployment of capital to underserved markets and client segments. Trade finance involving SMEs and emerging markets tends to be different in risk/return profile for example, when compared to financing intra-OECD trade flows. These variations will attract different investors and different types of capital, some of which are significantly more risk-tolerant than banks. COVID-19 can potentially lead to an increase in capacity for trade financing, as policymakers and business leaders recognise the critical role that robust trade will play in the global recovery. It is one of very few truly global levers available to enable far-reaching economic recovery, and trade financing must be available for trade to play its role. Any significant and sustained ambition to build back better requires a solid foundation of recovery, including the reinvigoration of multilateral, rules-based sustainable trade. Access to timely and affordable trade financing is vital to the equation of global economic recovery.