Official Opening Address at the Afreximbank 2016 Annual Structured Trade Finance Seminar/Workshop

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Labourdonnais Hotel, Port Louis, Mauritius

November 21, 2016

The President and Chairman of the Board of Afreximbank

Chairman of the SBM Group

Dr Fofack

Ladies and Gentlemen

Good Morning

Thank you Dr Oramah for the invitation extended to me for the opening of the 2016 Annual Structured Trade Finance Seminar. At a time when trade openings among African countries have gathered momentum and trade relations between countries at the global level have again become a topical issue, the organisation of this seminar is a welcome initiative. I take this opportunity to express my appreciation to the organisers.

I understand that Afreximbank has been organising this flagship seminar since 1999. It's the first time that the Seminar is being held in Mauritius. I am delighted to welcome you all to Mauritius.

The seminar is part of an endeavour to promote trade finance in African countries. Over the next four days you will have the opportunity to get acquainted with the technicalities and to explore the underlying complexities of structured trade finance under the guidance of very able and proficient speakers. I am sure you will be better equipped to handle the various aspects and intricacies of trade finance by the end of this seminar.

Trade financing gaps, according to the World Trade Organisation, is quite pronounced in Africa, notably among the poorest countries. The underdevelopment of the financial sector constitutes a significant barrier to trade. Closing the trade finance deficit in the SME sector, especially in Africa, is a neglected area. SMEs have increasingly become the most dynamic sector in terms of job creations, value-added and even innovation, but sadly it is also the sector facing major constraints in securing trade finance. I have no doubt this issue will trigger lively discussions.

Trade finance fell sharply across the world during the global financial crisis. The growth rate of international trade has been very weak. The scarcity of trade finance exerted significant drag on world trade during the critical phase of the crisis, with adverse implications for economic growth. We are still not fully out of the woods. Though economic prospects around the world have generally improved, it remains plagued with lingering uncertainty and volatile financial markets. The flow of finance to export sectors in most countries have taken quite a few years to recover after the 2007-08 global crisis. Conditions in trade finance markets have normalised gradually.

Financial institutions still remain cautious and are selective in risk-taking, partly due to new regulatory demands. In the aftermath of the financial crisis, regulatory scrutiny tightened up, causing many financial institutions to lower their risk-appetites. More concerned with quality, they focus increasingly on established customers. As a result, SMEs servicing the lower end of the market, are struggling to obtain affordable finance. While the instrumentation of trade finance is going through a period of innovation like the ‘bank payment obligation’ and ‘supply chain finance’, it is crucially important that suitable trade finance products be constructed for SMEs in sub-Saharan Africa.

In 2013, the African Development Bank estimated that the value of the credit gap for formal SMEs in Africa is over USD100 billion, out of which USD70 to 90 billion applies to SMEs in Sub-Saharan Africa. To close this credit gap, Sub-Saharan Africa would need to increase the provision of credit, including loans, overdraft, leasing, factoring and trade finance, to the neglected formal SME market by 270-320 per cent.

Surveys conducted independently by the WTO and the Asian Development Bank reveal some disturbing trends. The trend in trade finance gap is growing steadily, adversely affecting as high as one third of existing markets in developing countries. The main reasons for the rejection of requests for financing are said to be:

- the lack of creditworthiness or poor credit history,
- the insufficient limits granted by endorsing banks to local African issuing banks,
- the small size of the balance sheets of African banks, and
- insufficient US dollar liquidity.

Traditionally, credit risks associated with trade finance is considered low, given that the facilities are self-liquidating, short term and secured by the underlying goods. But when a trade finance fraud occurs, losses can run into millions of dollars. Standard Chartered reportedly lost almost $193 million from trade fraud in 2014. Nor is it sensible to underestimate the impact of reputational risks associated with AML/CFT. It can adversely impinge on a country’s reputation and, hence, on financial stability.

Fortunately, we have not seen any material loss or adverse trends in the banking sector in Mauritius. It would, however, be unwise to disregard the incidents reported internationally, given the openness of the Mauritian economy. From an AML/CFT perspective, banks should be alert to transactions involving higher-risk goods. Goods may be over- or under-valued in an effort to evade anti-money laundering or customs regulations, or to move funds or value across national borders. The need for banks to have a sound understanding of their customers, their business and underlying transactions can hardly be overlooked. Conducting background checks on the concerned buyers and suppliers, with a view to independently ascertaining their existence and involvement in the trade cycle, is an essential step in risk-minimisation.

Banks must also be wary of the risk of external frauds. One type of trade fraud is double financing. Importers and exporters collude to either create false turnover and/or invoice with the intention of obtaining credit facilities before disappearing. Trade financing requirements for complex group structures should be therefore carefully analysed to detect double financing. It is imperative that banks implement appropriate policies and procedures to spot collusion between customers and their alleged buyers or suppliers. Some banks are proactively implementing systems which cross-reference data to easily identify linkages between counterparts, U-turn transactions and, hence, detect collusion. Less sophisticated banks may opt to implement manual processes with the same objective. Banks have to make sure that inventories and manufacturing plants are regularly visited and reconciled with trade financing requirements to detect fictitious goods and accounting frauds.

Country risk is also an important factor in trade financing. The political and economic stability of a country determines whether the country can and will honour its payment commitments in time. Having specialised team for assessment of country risk and to control level of exposure at a countrywide level can strengthen banks financial position and avoid unpleasant surprises.

Bank risk is yet another relevant factor, given that all banks do not have the same of degree of financial strength. Again specialized units to assess bank risk as well as limits by banks could assist in mitigating the risks. Risk management is not merely compliance with regulatory guidelines but also represents a shield from unforeseen losses, and therefore should be developed as a second habit. It is the surest road to stability, profitability and success. Banks must be at the forefront of risk management. Reviewing constantly the control framework equips banks to harness current and emerging risk issues. An adequately capitalised bank is more resilient to adverse shocks.

Lately, there has been a retreat of correspondent banking services from banks domiciled in advanced economies. International commercial banks that historically provided confirmation lines for trade instruments have started to reduce their exposures gradually. Banks in Sub-Saharan Africa can use this as an opportunity to grow their share of business in trade finance. However, the proper mechanism would need to be in place to ensure that only genuine transactions are being financed.

In a low interest rate environment, trade finance represents an avenue through which banks can grow their income. Acceptances and documentary credit extended by banks in Mauritius increased from Rs10.1 billion to Rs18.9 billion between June 2006 and June 2016. Fees generated from trade finance has been on the rise for most of our banks.

At the Bank of Mauritius, we follow quite closely the evolution of the Basel Committee on Banking Supervision to establish fair and reasonable prudential treatment for trade finance. Overtime Mauritius has carved a strong image of a well-regulated banking sector living to the expectations of best international practice.

I wish you, particularly those of you who are visiting us, a pleasant stay in Mauritius. I wish you all the best for the days ahead.

Thank you.