Trade Finance: Overcoming Obstacles to Strengthen Inclusive and Sustainable Growth

A "Thought-Starter" Contribution on Trade Finance to the 2020 G20 Process

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LIST OF ACRONYMS

AML	Anti-Money Laundering
BAFT	Bankers' Association for Finance and Trade
CCF	Credit Conversion Factor
CFT	Combating the Financing of Terrorism
DLs	Distributed ledgers
DLT	Distributed Ledger Technology
EBIDA	Earnings Before Interest, Depreciation and Amortization
EU	European Union
FSB	Financial Stability Board
GDP	Gross Domestic Product
GPFI	Global Partnership for Financial Inclusion
GVCs	Global Value Chains
IFC	International Finance Corporation
IFSA	International Financial Services Association
IRB	Internal ratings-based
KYC	Know Your Customer
MDBs	Multilateral development banks
MPIA	Multi-Party Implementation Agreement
OECD	Organisation for Economic Co-operation and Development
SDGs	Sustainable Development Goals
SME	Small and medium-sized enterprise
WEF	World Economic Forum
WTO	World Trade Organisation

FOREWORD

Sustainable economic growth has been at the core of the joint work between the B20 and *Business at OECD* since 2015, culminating in a series of B20-*Business at OECD* annual events on Finance and Sustainable Growth and related publications. Each year, the conclusions of the roundtables have helped pave the way for action by G20 leaders. Contributions for our publications came from representatives of SME associations and large corporates, as well as governments, financial institutions, and international organizations.

Our annual contributions to the G20 process aimed at "joining the dots" and illustrating how finance links to other policy areas given that policies are often run in silos. In a globalised world, this generates the dispersion of efforts, which may end up magnifying adverse consequences. Policies are more effective if they are complementary to each other and adequately coordinated. For example, under the 2018 **Argentinian Presidency** work focused on **productivity**, with us underlining the critical importance of harmonising policies aimed at combining economic growth with those aimed at stability and productivity.

Against this background, business believes that the 2019 Japanese Presidency rightly highlighted the **critical importance of stronger cooperation** ten years after the global financial crisis, in which the G20 and the OECD both play a key strategic role. Emphasis was also placed on the need to provide tax certainty for cross-border trade and investment. As the global economy continues to perform below potential, it is evident that poor policy coordination creates costly fragmentation, while uncertainty holds back trade and business investment. We now look towards **Saudi Arabia's Presidency** to draw on past efforts and promote this global vision aimed at balancing (i) Economic Growth, (ii) Financial Stability and (iii) Productivity, key to generating Sustainable and Inclusive Growth.

In this context, we continue and further develop our past work in this years' contribution by focusing on **Trade Finance as an all-round example of inclusive and sustainable growth**. In particular, we highlight the importance of developing "trade ecosystems" which help to facilitate payments and enable trade financing, and become more accessible to both SMEs and large corporates. Leveraging both traditional and emerging digital technologies and data will be a key enabler in this regard. More generally, governments need to look critically at how trade, investment and tax agreements interact and whether they are sending a consistent message to the private sector.

In our contribution, we encourage the OECD to create dedicated work streams and analysis on enhancing trade finance.

INTRODUCTION – TRADE FINANCE, AN ALL-ROUND EXAMPLE OF THE INCLUSIVE SUSTAINABLE GROWTH G20 AGENDA

The G20 has made commitments towards achieving sustainable economic growth since the first Leaders' Summit in 2008 in Washington. In line with this, the 2019 Japanese Presidency's core vision included the need for continued and steady progress towards achieving the Sustainable Development Goals (SDGs) across all countries, supporting global growth and its adequate distribution to ensure that all people enjoy peace and prosperity.

Industry and finance have made great progress in responding to new and growing requirements of societies and households. Examples include the development of new products and more effective production processes, the provision and application of new technologies, the financing of innovative sectors and protection from old age, health and natural disasters, and the construction and maintenance of infrastructure. Business stands ready to actively participate and contribute to sustainable development, responsible investment, ESG initiatives, international dialogue and cooperation. However, national governments and intergovernmental institutions need to cooperate more closely and effectively in enabling markets to operate smoothly. It is key to correct market imperfections, eliminate bureaucratic regulatory and policy obstacles to cross-border financing of investment and provide opportunities for all in accessing such finance and sharing its benefits. This concerns in particular vulnerable groups, such as SMEs, but also applies to credit and capital markets whose development and cross border integration are essential pre-requisites for sustainable growth and innovation.

Better economic and social performance have always gone hand-in-hand with trade and market openness in countries at all levels of development - creating new opportunities for workers, consumers and firms around the globe and helping to lift millions out of poverty. As societies can only support economic openness, when it is also accompanied by appropriate domestic policies to prepare people for change, international cooperation is essential to bridge public sector, private sector and civil society. This triangular open-collaboration approach, emphasised[1] at the 2019 B20 Tokyo Summit, is crucial to support change, strengthen local adaptation and guarantee resilience and sustainability for the new business cycles reshaping the way we produce and consume.

Yet, **fragmentation and frictions continue to impede the free flow of people, capital, goods and services**, as the global economy remains divided into separate jurisdictions, and markets develop due to the introduction of new technologies and market segments. Policy initiatives, including regulation and compliance regimes, frequently find cross-border consistency challenges, generating at best the dispersion of effort and at worst, negative unintended consequences. Worryingly, research indicates that 90% of cross-border trade declarations involve a broker and 75% of traders use third-party logistics providers (Accenture, 2018a). Escalating trade conflicts and protectionist rhetoric are taking an increasing toll on business confidence adding to uncertainty.[2]

In this context, the **role and further development of trade finance is central to business trust** in global trade activities with four-fifths of those activities – worth USD 15trn a year – underpinned

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[1] Defined informally as "three to tango" by the intervention of Dr. Marcella Panucci, Director General of Confindustria.
[2] OECD, "*Economic Outlook, November 2019*".

by specialized loans or guarantees (The Economist, 2019). Yet, services supporting trade transactions, especially financing and risk mitigation, are more easily and affordably accessible to larger companies and their Tier 1 suppliers/distributors. This results in unmet demand for trade finance, with many challenges experienced by small and medium-sized enterprises (SMEs). The importance of ensuring broader access to trade financing, both traditional mechanisms and those linked to supply chain finance, underpins the discourse in this paper.

Further developing "trade ecosystems" can support payments and enable trade financing, accessible to both SMEs and large corporates, leveraging both the existing data from traditional sources and new data arising from these digital platforms and blockchain technologies. We stress that the development of trade ecosystems will benefit all players, paving the road to enhancing SME participation with local and national authorities, banks, etc., thereby creating new jobs. It can also support financial crime prevention, such as money laundering or terrorist financing, which are ever growing risks in trade whereby criminals use a legitimate trade to disguise criminal proceeds.[3]

This thought starter proposes trade finance to serve as an all-round example of the inclusive sustainable growth agenda. Continuing on previous years' recommendations to G20 Leaders, we encourage the OECD to create dedicated work streams and analysis on enhancing the role played by inclusive global value chains (GVCs) in trade finance.

This **aligns to the long-term strategic vision delineated in previous years**, with the need for policies and regulations that support investments towards these strategies and suffer less from fragmentation in their implementation. For instance, under the 2018 Argentinian Presidency, work focused on Productivity. This reflected the broader efficiency and efficacy needed for longer-term investments in infrastructure, digital, health, climate and energy supporting the wider Economy. We highlighted the critical importance of harmonising policies aimed at (i) Economic Growth and those aimed at (ii) Financial Stability with those targeting (ii) Productivity to generate Sustainable and Inclusive Growth. Such harmonisation is achieved by integrating (a) strategic growth activities, owned by governments and the business community alike, which should target longer-term strategic vision; and (b) implementation of such policies; an example of failing implementation is given by the cumulative burden caused to the ultimate receiver.

Finally, it is also worth noting the efforts under way through the **United Nations** (UN, 2019), and in particular the UN Centre for Trade Facilitation and Electronic Business (UN/CEFACT) project to propose and motivate closer linkage between the techniques and practices of trade financing and the disciplines of trade facilitation.[4] The premise of this initiative is that the role of financing is so critical to the ability of businesses to conduct trade that efforts aimed at the traditional areas of focus of trade facilitation (such as enhanced customs and logistics, improved regulatory context and others) will fail to maximize benefits if the financing element is not more closely and directly integrated into facilitation practices (Malaket, 2015).

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[3] Trade based money laundering, or the deliberate falsification of the value or volume of an international commercial transaction, is the largest component of illicit financial flows, measuring up to US$1 trillion for developing countries, according to Global Financial Integrity (GFI). It estimates that on average over 80% of such illicit financial flows were due to fraudulent mis-invoicing of trade. See: GFI, GF Trade, "*Trade Misinvoicing Risk Assessment*".
[4] See: UN/CEFACT, "*Integrating Trade Finance and Supply Chain Finance into Trade Facilitation*".

CHAPTER 1 – TRADE FINANCE: KEY OBSTACLES

Trade finance and financing throughout the GVCs are important enablers of international trade. By ensuring secure and timely payment across borders, they significantly support the optimization of working capital on the buyer side, and generate additional operating cash flow on the supplier side, whilst also offering highly effective risk mitigation solutions that enable trade in the most challenging conditions and markets; which results in enabling domestic commercial activity and in providing working capital to local SMEs as well.

Volumes are significant with four-fifth of global trade transactions – accounting for about USD 15trn a year – rely on specialized loans or guarantees.

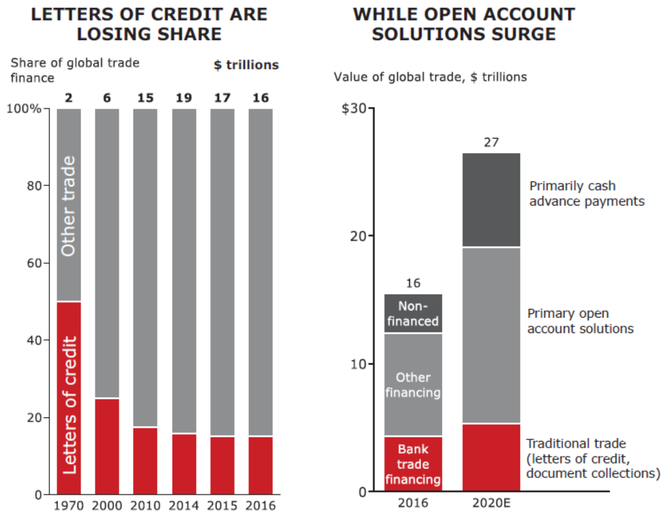
However, financial instruments, such as **letters of credit and guarantees**, can be unattractive for small-ticket transactions due to the relatively high operational costs. The typical cost-to-income ratio in traditional trade finance is 50-60%, meaning that more than half of the price charged to clients for trade finance needs to cover operational expenses, even before covering the costs of risk, liquidity and capital. Key challenges include:

- **Inefficient documentation processes** including manual contract creation, multiple checks or duplicate bills lead to complexities and delays. From banks and insurers to warehouses and customs, processing trade credit requires the exchange of 36 original documents and 240 copies on average. This introduces errors and risks, jeopardising reliable real-time information gathering and tracking required for credible financing decisions. A recurring issue with the paper-intensive transactions involved in traditional trade finance is that the shipment can arrive at port of destination ahead of completing the paper processing – i.e. the physical supply chain moving more efficiently than the financial supply chain.
- **Multiple platforms** may lead to increased risk of miscommunication and fraud.
- The trade arena and the **rules that govern it are geared towards paper-based manual processing**. Implementing streamlined digital processes where there is shared control and liability for intangible digital objects into the current paradigm will result in trust issues across the network. Financial institutions today are looking to new ways to improve their trade finance processes.
- In addition, **trade finance may not be sufficiently visible to users, especially to SMEs**. This mainly comes from lack of public understanding (and often times lack of "advertisement" from the supply side) as to what kind of trade finance is available, as well as how to access it. It is worth noting that this issue is intertwined with the high-cost structure and inefficiency mentioned above: since provision of trade finance is not attractive to its suppliers, they are reluctant to offer trade finance products to their customers, leading to less visibility and availability. These are frequently coupled with **skillset gaps of SMEs in communicating their financing needs**.

CHAPTER 2 – NEED TO REMOVE UNINTENDED OBSTACLES FROM FINANCIAL REGULATION AND THE CUMULATIVE BURDEN OF REGULATIONS

Trade finance has been negatively affected as a result of rise in cost of capital under the key ratios segment of the Basel III measures, leading banks to shrink their balance sheets. In short, a consequence of the post financial crisis regulatory regime is that banks are offloading some of their safest assets towards multiple riskier directions. Banks' capital costs in trade finance are expected to increase by 18% to 40% due to tighter regulation according to BAFT.[5]

Figure 2: Trade Finance losing out to alternative finance solutions



Source: World Bank; ICC Global Survey Rethinking Trade and Finance (annual reports 2010-2015); MISYS Financing Future Supply Chains.

Credit Conversion Factors (CCFs), being low given the nature of trade finance, are being increased and banks cannot use either receivables or physical collateral as eligible credit risk mitigants (as these are expressly reserved for banks operating under the internal ratings-based (IRB) approach, benefit that that may be removed through the "output floor" under the finalisation of Basel III).

Additionally, minimum capital requirements based on a minimum one-year tenor is a burden to trade finance activity as its turnover rate is considerably faster. As trade finance is considered low risk, returns are smaller and the margins thinner, compared with other business lines. Similarly, trade finance typically relies on interbank transactions and exposures to banks are severely penalized by the finalization of Basel III.

As a result, this may have led to an **increase in systemic risks**, with **banks being crowded out** in different directions:

- **Within banks' business models,** if the capital that is being applied to the activity of trade is the same as for any other type of lending that generates a higher return on the same capital, then banks will choose to deploy their capital for those types of assets.
- **Across trade finance**, we see an evolution from traditional products in support of trade and GVCs towards other forms, e.g. Bank-to-Bank or Subsidiary-to-Subsidiary trade finance that may support the working capital of individual entities, rather than directly benefiting the trade ecosystem as a whole.
- **Multilateral development banks** (MDBs), such as the International Finance Corporation

[5] BAFT is a global financial services association formed by the merger of the Bankers' Association for Finance and Trade (BAFT).

(IFC), have historically supported banks in emerging economies requiring financing for their corporate clients' trading activity and lenders who want the deals to be backed by the security that IFC offers or via dedicated trade facilitation programmes[6]. However, the capacity of MDBs is limited by the capacity and willingness of member states to inject capital. This has led to a trend toward "blended finance", which makes the regulatory treatment for private sector financial institutions all the more critical. Critical is to avoid a crowding out of MDBs at the expense of commercial banks, and rather strengthen the complementary position of MDBs.

- The shrinking bank balance sheets have given rise to increased activity of alternative service providers that are keen to step in, including **shadow banks**.[7] These are attracted to trade finance as an asset class because of its low default rates, and **benefit in terms of compliance costs** by not having to adhere to the same **compliance requirements** that are applied to banks, such as the very Basel capital and liquidity requirements or Know Your Customer (KYC) and Anti-Money Laundering (AML) standards. Some insurance companies provide trade insurance products to help smooth out the international business transactions, but less known to the public. They can be a viable complement, but the risks to the stability of the financial system are significant and need to be addressed by increased compliance regulations that are up to speed with the current digital capabilities, which would have the **unintended adverse consequences of containing access to trade finance.**

[6] e.g. the European Bank for Reconstruction and Development (EBRD), and the Export-Import Bank of the United States

[7] Shadow banks are a group of financial intermediaries that facilitate the creation of credit across the global financial system but whose members are not subject to regulatory oversight. Examples include hedge funds, unlisted derivatives, and other unlisted instruments.

CHAPTER 3 – A STRATEGIC VISION: EXPLOITING THE POTENTIAL OF EMERGING TECHNOLOGY FOR TRADE FINANCE

Policy-making has clearly a key role to play in setting the right framework conditions for trade and investment in general, and to support SME integration in GVCs. **However, it is not just a question of policies, commercial decisions also affect the evolution of the international trade's global architecture**. For instance, many corporate participants have opted not to integrate aspects of transaction processing with freight forwarders, government bodies and document preparers, and many banks have been reluctant to invest, as long as corporate adoption of digital solutions remains low.

This suggests that there is much to be gained by reforms that **make it easier for productive firms to invest in the resources required to underpin their growth.** As outlined in 2018 by the B20 and *Business at OECD*, a strategic view on productivity is required which needs to be based on (i) fostering innovation; (ii) creating a market environment where productive firms are allowed to thrive, thereby facilitating the more widespread penetration of available technologies; and (iii) reduce resource misallocation, particularly skill mismatches.

Specifically related to supporting trade financing, **digital technology offers solid opportunities to increase efficiency and transparency,** for example through dynamically capturing and validating the big data exchanged among all GVCs' participants, which was also highlighted by the World Economic Forum (WEF) (the future of infrastructure finance, WEF-2018).

In particular, **Distributed Ledger Technology (DLT),** including **blockchain** or equally Robotic Process Automation (RPA) and Artificial Intelligence (AI), are cornerstones of efficiency gains, and are therefore increasingly seen as **a potential driver of savings in infrastructure and back-office processes,** and receive significant interest especially among financial services firms. Blockchain has the potential to make a major contribution to trade facilitations by speeding up customs procedures and trade financing and thereby taking forward the Bali Fintech agenda.[8]

Fintechs have become important players in the trade finance market (IMF, 2019): they provide some services similar to traditional banking (e.g. financial support to SMEs), but are currently not subject to banks' regulations, transparency, consumer protection or capital requirements. Fintechs operating in trade finance focus on cost-reduction initiatives such as automation, and concentrate on mid-tier, and non-listed companies. According to a recent survey (Accenture, 2018b), Fintechs increasingly see themselves as partners to financial institutions, opening new channels for SME financing and facilitate greater SME financial inclusion.

Blockchains are built on a series of innovations in organising and sharing data, and has the potential to eliminate data silos and enable existing innovations to scale. The objective is to create **trusted sources of standardised information**, used by all participants, containing a much richer dataset than that existing in any one system today. Being mindful of the data ledger's current data

[8] The International Monetary Fund (IMF) and the World Bank Group launched the Bali Fintech Agenda in October 2018. It is a set of 12 policy elements aimed at supporting member countries to harness the benefits and opportunities of rapid advances in financial technology, while managing the inherent risks. For further information see: IMF, "*Policy Paper the Bali Fintech Agenda*", October 2018.

capacity constraints, DLTs have the potential to introduce a range of benefits for participants, offering a faster, cheaper and safer alternative to manual systems by operating on secure and shared databases, where all participants have a copy of the stored data, vs. loosely connected participants of traditional processes.

This means that when a transfer of funds or, in the context of trade, information concerning a shipment would be recorded, validated and immediately available to all relevant parties, this would sharply reduce processing times; creating one and **only one verifiable**, shared version of the transaction. Crucially, in **permissioned distributed ledgers** (DLs) (different from general DLs which are open for contribution by anyone who can access the network) such as CORDA, D3-ledger or Marco Polo, only certified parties can initiate and verify transactions by using data verification, validated information and unique encrypted digital signatures, thus strengthening transparency and security against fraud, and therefore support unleashing greater infrastructure, enriched by risk insurance and hence SMEs' participation to trade finance globally.

Primarily, **distributed ledgers may thus provide efficiencies in reconciling records both within organizations and across firms**, while wider benefits of distributed ledgers may also be leveraged through developing applications that interface with DLs such as digital currency or smart contracts.

Over recent years we have seen the creation of several **trade finance blockchain consortia** (e.g. Marco Polo, we-Trade, Hong Kong Trade Finance Platform, Voltron) and increased participation in them by many renowned financial institutions. Despite indications that such digital architectures can contribute to improved access to trade finance, especially for SMEs, industry leaders are cautious about the practical impact and outcomes related to DLT-based solutions, mostly in relation to financing and data sharing, as well as possible challenges in the domain of competition.

On a smaller scale, platforms for trade and supply chain management have existed for years, and **more recently financing has been integrated into their capabilities.** These make use of digital to accelerate services such as for example Taulia (AI-powered platform delivering payment processing and working capital solutions to free up cash and connect supply chains), GTNexus (cloud-based platform connecting and optimizing supply chains) or SAP (service providers of multiple business intelligence tools and management software).

On a systemic scale, following successful examples experienced in creating a digital payment ecosystem, e.g. in China, the **same approach is increasingly being used to support trade, *de facto* creating the GVCs global payment ecosystems.** However, further development requires scaling across multiple networks and entities around the globe; and as outlined by DiCaprio-Malaket (2018), centralized solutions in a decentralized ecosystem do not scale: trade is about collaboration within and between networks.

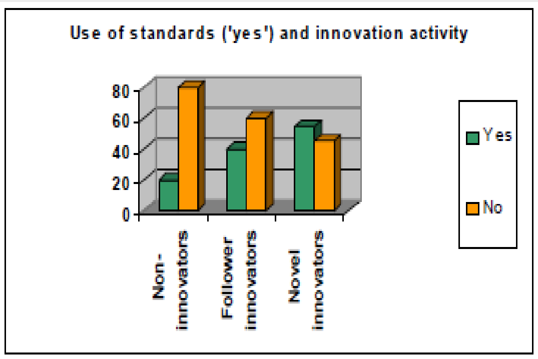
To initiate and support this evolution towards global multiple networks' "trade ecosystems", there is a need **to collaborate on standards** of factors across the trade chain and the capability to seamlessly integrate viable cross-border financing options, customs and logistic movements (see box 1).

Box 1: The importance of Standardisation

Tackling inefficiencies – *asserting that operational costs in trade simply relate to tariffs is short-sighted; inefficiency and diversity of procedures also lead to unsatisfactory revenue collection, poor export competitiveness and make the country involved less attractive to investment. This reduces the ability of traders, carriers, agents, ports and airports in developing countries to fully participate in global trade expansion, and by the same token make SMEs' participation extremely expensive.*

A lesson from containers – *Malcolm McLean brought to life the concept of intermodal transportation, based on the shipping container – i.e. uploading and offloading freight from different vectors (ship, train, truck) in a seamless way (standard dimensions and corner fittings). He once said: "I talked to an old London dockhand some time back. He remembered how in 1970 it took 108 guys about five days to unload a timber ship. Then came containerisation. The comparable task today takes eight folks one day. That is, a 98.5% reduction in man-days, from 540 total to just eight". As noted in the ISO TC 104 business plan "today, the vast majority, in excess of 90%, of world trade in non-bulk goods, moves in ISO freight containers".*

The simplification and harmonisation *of international trade procedures can be achieved by leveraging the GVCs as delineated above, maximising the use of DLTs. By making GVCs online marketplaces with standardised processes and data requirements, will by default (i) accelerate the procedures' time requirements, hence (ii) improving timeliness of payments (a long-standing low hanging fruit), and in turn (iii) reduce the operational costs and the trade finance requirements, which will further shorten in tenor and increase in credit quality, benefiting firms, suppliers and administrations.*



Source: CIS Innovation survey, DTI, UK

A misconception is also to consider standardization and innovation on opposing positions. Hard evidence exists of a positive link between the two; innovation frequently needs standardization. However, timing is critical: wrong timing, or in the wrong way, can harm innovation.

As standardization conveys legitimacy and continuity for a new product to the market, aiding companies and reassuring customers, standardisation of processes brings efficiency to the GVCs. Similarly to the experience with containers, thanks to today's interconnected word, the more GVCs use standardised information within their own processes, the wider will be the cross-fertilisation across GVCs.

Standardisation of factors does not mean and should not lead to a situation where one party has full control of the system and technology. Currently there are different large companies dominating each aspect of the ecosystem. There is a need for co-ordinated action by both private and public stakeholders to create the necessary supporting infrastructure, but with regulation to avoid domination of a single network. Such a transition is likely to help **reduce fragmentation, scale up innovation, facilitate technology spill-overs and managerial know-how, broadenand deepen skillsets, and enhance productivity.** There are increasing initiatives globally in this direction from various players, including Governments and business associations.

In the future, **GVCs could themselves form "ecosystems" which facilitate trade financing and supporting payments,** accessible to both SMEs and large corporates. They would be able to leverage traditional data and new data which would arise from the use of different online platforms. Similarly, today's digitalisation, opportunities offered by data verification technologies together with government support (at local, regional, sectorial and nationwide levels) would allow the creation of "Data Hubs" dedicated to SMEs (***"SME Hubs"***; B20-*Business at OECD*, 2018). These would be service platforms bringing SMEs together with local and national authorities, banks, etc.; thereby benefiting all players, and favour ***GVC Passports*** (B20-*Business at OECD*, 2018), in order to raise access to finance. The key is that all parties must be involved in the deployment of technology in an effective and coordinated way.

Adopting a trade ecosystem along the lines of a "GVC ecosystem" may thus help to overcome some of abovementioned obstacles. For example, Bain & Company estimates (Bain&Co, 2018b) that trade finance operating costs (e.g. wait times for documents) could be reduced by 50-70% and improve turnaround times three- to four-fold, depending on the trade finance product involved. For example, Banco Bilbao Vizcaya Argentaria (BBVA) has applied a distributed ledger system to reduce the time for submitting, verifying and authorizing an international trade transaction from over a week to just 2.5 hours.

Progress in developing such systems depends on all **stakeholders working together so that private and public sector leaders can align on common interests**, as emphasised by the Global Partnership for Financial Inclusion (GPFI) report on digital payments ecosystems.[9] In 2016, the G20 published the "High-Level Principles for Digital Financial Inclusion", designed to inform national policies to leverage digital financial services. These principles aim to sustainably increase financial inclusion while fostering sustainable growth and protecting users of digital payments.

However, none of that can be achieved, or at least cannot deliver growth to its full potential, if unintended regulatory obstacles are not overcome. **Ultimately, a stable, consistent and competitive regulatory environment is needed.**

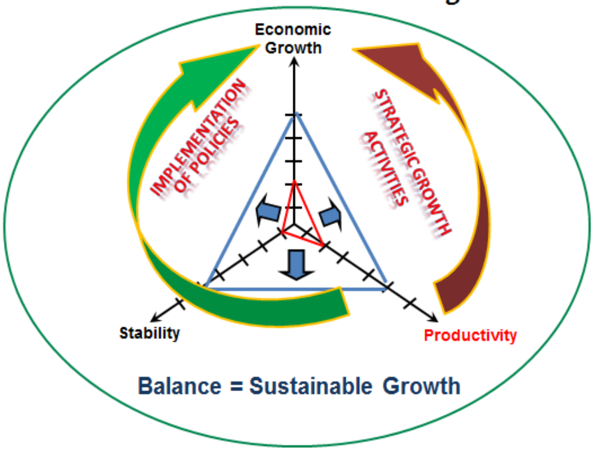
In implementing new technologies it is equally important to obtain buy-in from the participants who may benefit from it. While it may be easier for large corporates to digest what those innovations mean to them, **SMEs may not simply have enough resource to interpret the implications** (some are even "allergic" to implementing new technology). Therefore, policymakers, as well as other participants involved in creating a digital ecosystem to streamline trade finance, need to be mindful of the fact that **the majority of businesses may not be able to fully understand its benefit and that the technology itself needs to be user-friendly.**

[9] GPFI 2017b – Global Partnership for Financial Inclusion (GPFI), Financing SMEs in Sustainable Global Value Chains; Washington, D.C., May 2017.

RECOMMENDATIONS AND NEXT STEPS FOR THE 2020 G20 AGENDA

The importance of continuity between G20 Presidencies is critical in ensuring adequate review of progress made and ensuring forward momentum. The *Business at OECD* work with the B20 over the years has helped pave the way for action by G20 leaders and strengthened our holistic view, best represented via the *Sustainable Growth Triangle,* aimed at assessing policy balance across three pillars: economic growth, stability and productivity. Each year since 2015, we have focused in turn on one of these three pillars. In 2020, **it is recommended to put some focus on Trade Finance, highlighting the importance of harmonising a strategic vision around GVCs and leveraging digitalisation through blockchains, with a consistent implementation of policies and regulations** that remove barriers and support the complementarity of financing providers rather than crowding out regulated players in favour of unregulated ones.

The Sustainable Growth Triangle



We believe that G20 Leaders and the financial industry should embrace the creation of inclusive online multiple networks' marketplaces, deploying free cost online platforms to end users through a sustainable business model, offsetting monopolistic, geopolitical and data privacy concerns. Such platforms shall seamlessly integrate financial institutions to the commerce, insurance and logistics industries within the global value chains.

Continuing on previous years' recommendations[10] to G20 Leaders, in 2020 **we recommend to the OECD and to the G20 Presidency to better analyse Trade Finance, and relevant policies in the following directions:**

- **Leverage on what digitalisation** can offer and work on policies targeted at promoting skills, digital technologies, access to finance and simplify tax compliance which increases the opportunities, especially for SMEs, to engage in supplier relationships with global buyers.
- Develop **infrastructure and common standards** with both public and private input which could help new digital initiatives to be tested and scaled-up faster, not confined to just DLTs, but also related to smart contracts, digital payment systems, lowering transaction costs, etc.
- Support harmonization in **data governance**, enhancing use of data and data portability for market development and economic growth, while also drawing appropriate policies on cyber security and privacy protection. In particular, we recommend work towards **data verification and data reliability incentives** to overcome the data privacy challenges.
- The use of **data analytics** is no longer just an opportunity, but a "requirement" in today's

[10] Recommendations consistent with the World Bank's "Maximizing Finance for Development" agenda as well as the October 2018 Eminent Persons Group's report that includes proposals to better coordinate international finance institutions in promoting financialisation.

world and we **must turn the digital divide into a digital dividend.** The results can be a massive expansion of the electronic footprint of SMEs.

- Enhance and better coordinate the dissemination of relevant and easily serviceable **information on how SMEs can access trade finance**, for example as part of government's capacity building via trade promotion agencies.
- Explore the opportunities offered by **Islamic Finance** to e-commerce in blockchain networks.

Box 2: Islamic Finance

Amongst many forms of alternative financing, Islamic Finance may be able to complement current bank offerings, while not posing systemic risks. A core feature of Islamic finance is to integrate finance with real economic activity. With e-commerce and digital trade systems, the process of trade becomes fully transparent from end-to-end, helping finance to seamlessly integrate in it. Islamic finance's contribution to trade financing can be easily identified in these two instruments:

- ***Murabaha*** *(cost-plus credit sale) is a financing arrangement in which a financing institution or a bank will purchase the commodity on a cash basis from the supplier and then sell it on credit to the buyer with a mark-up. This process becomes easily implementable and efficient in a digital system (preferably on a blockchain network). Since Murabaha requires on-time repayment of full outstanding debt, debt should be amortized, which reduces the financing cost for buyers, especially SMEs, enhancing their access to credit. Amortized debt on the other hand, will make funds available for financing other trade transactions, thus increasing turnover and return to financiers (investors or sellers).*
- ***Sukuk****, are financial certificates for mobilizing resources through capital markets. They can be used to mobilize funds for the Murabaha financing. Sukuk will represent ownership in the vehicle or the fund managing the Murabaha transactions. Sukuk holders share the profits and losses arising from financing trade through Murabaha. The risks associated with Murabaha are primarily credit-risks, which means that Sukuk holders are exposed to usually low levels of risk. Since these Sukuk are profit-and-loss sharing instruments, they can be funded off-balance sheet for the financial institution, posing minimal constraints on its balance sheet.*

Finally, many of those challenges mentioned in this paper **extend well beyond the financial sector**, but it is imperative for all policy-makers and standard-setting bodies to have an overarching view across regulations. Notably, we appreciate that the Financial Stability Board (FSB) has now been examining with all participants the effects of the financial reforms (FSB, 2019a and 2019b).

- In this regard, we recommend carefully considering the **cumulative regulatory burden** and the potential unintended consequences of the proposed regulation so that a balanced set of rules can be published which foster trade across borders while maintaining stability. To this effect, stronger coordination among FSB, OECD, European Union (EU), etc. is key.
- We also urge a look at reforms with **small players in mind** as they are key catalysts of trade, while also being the first to struggle in a challenging environment.
- It is critical to have a **holistic view across players**, not limited to the finance elements only, but **targeting a sustainable growth balance as depicted by the Sustainable Growth Triangle**. In the energy sector for instance, "**Energy GVCs**" are being reshaped by the vertiginous pace of technology, science, climate change, policy and consumer preferences, which cannot progress without a "plural" approach that respects national specificities which acknowledge region-centred roadmaps, according to distinct resource availability and capabilities.

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