

6. Advancing Trade and Improving Lives through Private Sector Development: An ITFC Trade Finance Perspective

KASHIF J. IQBAL

Senior Strategy Manager, Strategy Management
Strategy & Organizational Performance Office,
International Islamic Trade Finance Corporation

ADVANCING TRADE & IMPROVING LIVES IN THE ERA OF THE SUSTAINABLE DEVELOPMENT GOALS

It is well known that growth through international trade builds regional economic cooperation¹⁷⁵ and raises collective development benefits in the form of job creation, poverty alleviation and improved livelihoods.¹⁷⁶ Sadly, accelerating income growth and sustainable employment is a challenge in the developing world, given prevailing demographic and economic trends. The 57 member countries of the Organisation of Islamic Cooperation (OIC) have a population in excess of 1.2 billion people, the majority of whom are less than 25 years of age and with an unemployment rate of 8.8 percent.¹⁷⁷ As the youth enter into the labour force, sustaining employment and economic growth will become a rising priority for governments.

The magnitude of this development challenge is significant—and it does raise a fundamental question: in the era of the Sustainable Development Goals (SDGs), how can development finance institutions play a role in addressing this challenge? The answer lies in the development of the private sector by providing access to finance. For most people living in poverty, a decent job is their best chance of escaping to a better future, and on average the private sector provides 90 percent of jobs in a country.¹⁷⁸ In poorer countries, the majority of these jobs are in the informal sector and are either “microenterprises” or small and medium-sized enterprises (SMEs).¹⁷⁹

175 OECD Publishing, ‘Aid for Trade and The Sustainable Development Agenda: Strengthening Synergies’, OECD Development Papers, No. 5, 2016.

176 Higgins, K. and S. Prowse, ‘Trade, Growth and Poverty: Making Aid for Trade Work for Inclusive Growth and Poverty Reduction’, Overseas Development Institute, 2010.

177 IDB Data Portal, 2015.

178 World Bank, ‘World Development Report 2013: Jobs’, Washington, DC, World Bank, 2012.

179 Stein, Peer, Oya Pinar Ardic and Martin Hommes, ‘Closing The Credit Gap for Formal and Informal Micro, Small, and Medium Enterprises’, Washington, DC, International Finance Corporation, 2013.

The International Islamic Trade Finance Corporation (ITFC),¹⁸⁰ a member of the Islamic Development Bank (IsDB) Group, is playing an important role in addressing this challenge. ITFC was established with the purpose of advancing trade among OIC member countries and to improve the socioeconomic conditions of the people across the world. ITFC has a mandate to contribute towards the economic development of its 57 member countries by advancing trade and improving lives. Promoting private sector development is one of the three ITFC strategic pillars and one of its core contributors towards the IsDB Group's strategic objectives and the attainment of the SDGs.

DEVELOPING THE PRIVATE SECTOR THROUGH TRADE FINANCING

Private sector development is more than just creating jobs. The benefits of a thriving private sector range from increasing the availability of goods and services for consumption to driving positive social change.¹⁸¹ A strong economy can re-engage marginalized sections of society, incentivize investments in education and improve political engagement.¹⁸² In short, it can act as a real catalyst for change.

The trigger for this catalyst lies in the provision of finance. Access to finance can stimulate growth within the private sector by enhancing the range of goods and services that an economy produces.¹⁸³ This economic diversity has shown to be a good predictor of growth and highlights a strong rationale for trade finance institutions to support the development of the private sector and contribute towards the attainment of the SDGs.¹⁸⁴

Over the past 10 years, ITFC has provided more than \$40.25 billion of trade financing to OIC member countries,¹⁸⁵ making the Corporation the leading provider of trade solutions for OIC member countries' needs. Within the private sector, ITFC has provided \$9.28 billion, of which \$3.62 billion went to SMEs through partner financial intermediaries.

180 The ITFC is a member of the Islamic Development Bank Group. It was established with the purpose of advancing trade among the OIC member countries, which would ultimately contribute to the overarching goal of improving socio-economic conditions of the people across the world. Since inception in 2008, ITFC has provided more than \$40.25 billion of trade financing to OIC member countries, making it the leading provider of trade solutions for OIC member countries' needs. With a mission of being a catalyst for trade development among OIC member countries and beyond, the ITFC helps companies and institutions in member countries gain better access to trade finance and provides them with the necessary trade-related capacity-building tools, which enables them to successfully compete in the global market. Earning the A1 rating by Moody's reflects the Corporation's efficiency in service delivery by responding swiftly to customer needs in a market-driven business environment.

181 IFC, 'International Finance Institutions and Development Through the Private Sector – A joint report of 31 multilateral and bilateral development finance institutions', 2013.

182 Heath, R. and A.M. Mobarak, 'Manufacturing Growth and The Lives of Bangladeshi Women', *Journal of Development Economics*, 115, 1-15, 2015.

183 Kharas, H., 'The Emerging Middle Class in Developing Countries', Paris, OECD Development Centre (Working Paper 285), 2010.

184 Hidalgo, C. A. and R. Hausmann, 'The Building Blocks of Economic Complexity', *Proceedings of The National Academy of Sciences*, 106(26), 10570-10575, 2009.

185 ITFC Internal Analysis, Approvals US\$40.25 billion between 2008 – 2017 (end of year).

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Advancing trade and improving lives are the founding values of ITFC. These twin values are at the core of the ITFC strategy, which is designed to deliver financial growth through the provision of trade finance solutions and create development impact across the 57 member countries.

It is this balancing mandate which inspired ITFC to launch its Development Impact Framework in 2017, organized around six themes which contribute towards the SDGs. This framework allows ITFC to join an international community working towards addressing global challenges and united towards the achievement of global goals.



ENCOURAGING GROWTH AND INNOVATION IN SMEs

Alleviating the financing restrictions affecting SMEs has been shown to drive job creation in developing countries, encourage innovation and entrepreneurship and facilitate growth.¹⁸⁶ In the long run, the transition from a developing to a modern economy is achieved as the formal sector (including SMEs) begins to grow and displaces informal sector microenterprises.¹⁸⁷ It is this transitional role which multilateral financial institutions can facilitate as a catalyst for change.

The ITFC aspires to contribute towards this positive change by using innovative trade solutions such as structured trade finance tailored for private sector corporations, in addition to lines of financing given to banks for onward financing of trade operations of SMEs. This enables private sector participants to overcome barriers in accessing trade finance, boost private sector activities and contribute to economic growth and the socioeconomic condition of people across the 57 IFTC member countries. To this end, ITFC has provided more than \$9.28 billion of trade finance to the private sector, of which \$3.62 billion went to SMEs through the line of financing structure.

The ITFC partnership with Turk Eximbank is a perfect illustration of the successful cooperation between ITFC and the partner banks for SME development. Turkey's growth strategy relies on developing the export-oriented, private sector-led market by increasing productivity and accelerating industrialization. Supporting SMEs especially for their export financing requirements is a key component and ITFC has given priority for partnership with local banks in Turkey. The latest line of financing extended in 2017 in the amount of \$436 million illustrates the strong capacity of ITFC to mobilize funds from partner financial intermediaries for financing trade operations in the member countries.

HARNESSING THE POWER OF PARTNERSHIPS

It is important to recognize the power of partnerships "to mobilize additional financial resources for developing countries from multiple sources", as defined by the United Nations Partnership for the Goals.¹⁸⁸ Trade finance institutions like ITFC are able to negotiate with multiple sources to raise the amount of financing needed to meet the requirements of private sector enterprises. This creates a level of value-addition that would otherwise not be available.

The ITFC has significantly contributed towards this SDG by arranging over \$3.56 billion in additional resources mobilized from partners to support private sector development over the last 10 years. This has been delivered through the ITFC co-financing and syndication arrangements to help bridge the trade finance market gap and meet the financing needs of private sector enterprises.

186 Beck, T., 'Bank Financing for SMEs – Lessons from the Literature', 2013.

187 La Porta, R. and A. Shleifer, 'Informality and Development', *The Journal of Economic Perspectives*, 28(3), 109-126, 2014.

188 Global Partnerships – United Nations Sustainable Development [<http://www.globalgoals.org/global-goals/partnerships-for-the-goals/>], access date 15-01-2018.

ALLEVIATING POVERTY THROUGH JOB CREATION

In the era of the SDGs, there is a commitment towards ensuring decent work for all women and men by 2030. To this end, one of the most noted outcomes of private sector development is the creation of new jobs, which is the primary measure of development impact evaluated by development institutions. This is because the provision of finance to SMEs and larger private sector enterprises has considerable impact on job creation and poverty alleviation, leading towards the betterment of livelihoods.¹⁸⁹

According to the Asian Development Bank, firms which reported receiving an increase in finance also reported that their workforce grew by an average of 8 percent. Firms were also asked how they might allocate a hypothetical increase in trade finance of 25 percent. The average response stated they would increase their workforce by 20 percent; responses were higher in the Middle East and North Africa and sub-Saharan Africa, where firms responded 31 percent on average.¹⁹⁰

EVALUATING DEVELOPMENT IMPACT ACROSS THE PRIVATE SECTOR

Measuring the development impact of trade financing is an extremely challenging task. This is principally due to the short-term nature of trade financing and the long-time period until impacts (such as job creation and poverty alleviation) are observed. To overcome this challenge, development institutions must work more closely with private sector enterprises (particularly in less developed countries) to gather development data on a consistent periodic basis over the long term. Development institutions can provide initial support to help shape policies and processes to improve the governance within private sector enterprises and provide tools such as questionnaires and surveys to lay the foundation for data collection and impact analysis.

Another challenge involves the accessibility of data, even though it may be available in abundance. Development institutions are reliant upon private sector enterprises to share confidential data, such as the geographic and sectoral breakdown of their trade flows or the distribution of finance to SMEs through financial intermediaries. Many enterprises view this data as strictly confidential and may be unwilling to share. Furthermore, in-depth trade data may not be collected in certain developing countries at all. This is where building trust and reliable partnerships can help ease the journey of impact evaluation and allow all parties to identify areas where development impact can be maximized and lessons for improvement learned.

With an ever-increasing emphasis on building partnerships to achieve the SDGs, it is important to recognize the involvement of multiple players with information passing through multiple networks across a trade-related supply chain. Outcome mapping helps assess the determining factors which can either encourage or inhibit paths of development

189 Donor Committee for Enterprise Development, Private Sector Development Synthesis Note, 2017.

190 Asian Development Bank, 'Trade Finance Gaps, Growth, and Jobs Survey', 2016.

impact, and the paths through which impact can be most effective. This is particularly useful in strategic development planning.¹⁹¹

In addition to evaluating the impact attributable to an amount of private sector financing, counterfactual analysis creates an understanding of what would have happened in a community in the absence of financing. Comparison groups can be used to recreate scenarios where finance was not provided and allow in-depth exploration of an “intervention-free” environment. This can be compared directly with the actual evaluation to determine the scale of impact that is attributable to a set of financing. However, careful thought should be given when selecting the comparison group to ensure it is relevant, in order to avoid misrepresentation and invalidation of the evaluation results.¹⁹²

NEXT STEPS: MOVING TOWARDS THE SUSTAINABLE DEVELOPMENT GOALS

The SDGs represent a road map for solving the most pressing issues facing the people, the planet and ensuring progress in today’s challenging global environment. It is a path towards transformation and sustainable development. In the era of the SDGs, financial institutions have a leading role to play in accelerating income growth, alleviating poverty and supporting the betterment of livelihoods across the world. By financing private sector enterprises, financial institutions can act as a catalyst for change, contributing towards economic growth and youth employment and drive positive social transformation.

191 Davidson, E. J., ‘Ascertaining Causality in Theory-Based Evaluation’, *New Directions for Evaluation* 87(1): 17–26, 2004.

192 African Development Bank, *eVALUation Matters*, 2000, see https://www.afdb.org/fileadmin/uploads/opev/Documents/IEM_-_Impact_Evaluation_of_Development_Programs-_Challenges_and_Rationale.pdf.