Introduction

Trading Up is a global blended finance partnership between Global Affairs Canada, MEDA, Sarona Asset Management (Sarona), and The University of Waterloo (UW) for sustainable and economic development. The Project responds to the critical role played by Small and Medium-sized Enterprises (SMEs), supply chains, and investments to support women and men low-income employees and smallholder farmers, advance trade, and boost economic growth.1 Implemented in direct collaboration with its partners—Sarona and UW—MEDA’s Trading Up project is underpinned by three major components:

- **Sarona Trade Finance Fund (STFF):** Established by Sarona, the STFF injects capital into pooled investment vehicles (funds) of trade finance intermediaries (TFIs) and/or Alternative Financial Intermediaries (ATIs) that on-lend to SMEs in eligible Official-Development Assistance (ODA) countries.

- **Partner Capacity Building (PCB):** MEDA provides technical assistance (TA) to select STFF TFIs for the development and/or enhancement of their Gender Equality; Environmental, Social, and Governance (ESG); and/or Impact Measurement and Management (IMM) practices.

- **Farmer Impact Grants (FIG):** Trading Up offers grant incentives for select portfolio SMEs and farmer cooperatives and associations (i.e., grant recipients linked to STFF TFIs) to enable strengthened engagement of key actors with smallholder farmers (SHFs) to improve productivity, market linkages, and wellbeing.

- **Research:** Little, if any, research has been conducted on the significant impact trade financing has on local economic growth (e.g., job creation, increase in the supplier base and strengthening the tax base—little). Through a cross-cutting component, Trading Up identifies the socio-economic impacts that trade finance has on SME business performance, job creation, gender equality, and contribution to local economies, among other key indicators.

In a research publication commissioned by the Project, Mbuyu Capital—an investment advisory firm—recognizes that “non-bank provision of trade finance—particularly by funds—is a nascent area of financial markets” and that “[t]here is considerable scope for new entrants to develop the sector ensuring impactful investment is firmly on the agenda.”2 This is the role Trading Up has played over the last four (4) years since inception in 2017: building the capacity of TFIs to “ensuring impactful investment is firmly on [their] agenda.”

This article is part of a series of learning briefs on the implementation of the Project. In this article we will focus on the PCB component and discuss some of the lessons learned in developing and enhancing the capacity of TFIs keen to impact SME borrowers demonstrably and significantly and/or workers, suppliers, or customers in target countries.
Trading Up Partner Capacity Building

As part of Trading Up, MEDA offers qualifying TFIs, their investees (SMEs), as well as related associations and cooperatives, customized TA packages geared towards enhancing impact, while promoting improved business performance. These packages, enhanced with a 1:1 matching component of CAD 16,000, offer TFIs TA in a range of areas that aim at enhancing the awareness and adoption of strengthened Gender/ESG/IMM practices for the improvement of TFIs’ investment processes and the impact for clients—including prospective and current portfolio SMEs. The PCB process, that can last up to 12 months, follows a customer-centric approach divided in the following steps:

1. **Introductory calls**
   - MEDA conducts needs assessment
   - MEDA proposes recommendations
   - TFI develops action plan & enters contract

2. **MEDA & TFI implement action plan**
   - TFI measures impact

**Needs Assessment:**
MEDA conducts a thorough review of key documentation (e.g., impact policies, Gender/ESG/IMM strategies, and/or corporate recent performance); the TFI receives a close-ended questionnaire which is analyzed by MEDA’s team of technical experts; and follow up interviews with senior personnel aimed at gaining a richer picture of TFI goals, financial and impact performance, and main challenges. Following completion of submission of information and interviews, the PCB team reviews the data and summarizes trends and patterns observed, including, but not limited to the firm’s impact strategy, investment processes, portfolio monitoring, investors and investor reporting, etc.

**Recommendations:**
The PCB team drafts a report that includes an analysis of the findings and the top five recommendations a TFI can follow to develop and/or enhance existing practices. These recommendations are discussed with TFI key individuals—including senior management—to discuss the TFI’s response/reaction to the report’s findings and recommendations (e.g., what surprised them, what do they agree or disagree with, what excites them, etc.); explore if there is an appetite by the firm to implement any of the recommendations, or if there are other strategies the TFI would like to adopt; and whether the firm agrees to co-develop an Action Plan for the implementation of recommended strategies within the following 6 – 12 months.

**Action Plan:**
After MEDA disseminates the recommendations report to the TFI, the TFI can select recommendations of their choosing, which will be implemented immediately and supported by MEDA. As part of this step, TFIs develop an action plan which MEDA reviews and integrates into an agreement with the TFI. For the subsequent 6-12 months, the TFI implements the action plan with support from MEDA, drawing upon local and international consultants as required. After implementation, the TFI agrees to measure and report impact data for the length of the investment relationship with the STFF.

As of the date of this brief, four (4) TFIs have completed all stages of the PCB process up to the Recommendation step, and three (3) are completing the co-development of their Action Plans.
Lessons Learned

Trading Up is partnering with extraordinary organizations (e.g., Sarona is both a certified BCorp and has regularly been featured in the ImpactAsset 50 list), including STFF investees that are very keen to take the leadership in the sector by becoming 2X Challenge eligible and also being featured in the IA 50 list. That being said, building and strengthening the capacity of TFIs has been challenging, and has been compounded by the ongoing COVID-19 pandemic. Partnering TFIs are at different stages of their Gender/ESG/IMM capabilities: some have well defined impact strategies but lack implementation goals for measuring progress; others recognize an opportunity to integrating ESG risk management systems into their investment and monitoring processes to significantly increase their assets under management by raising future funds from impact investors, responding to the changing and more rigorous ESG and impact requirements of this investment group. Others are refining their impact strategies to become impact investment leaders in the trade financing and private credit spaces. These challenges can be categorized as follows:

- **In-house capacity:** Few TFIs have in-house capacity and/or dedicated teams focusing on ESG and/or IMM. ESG/IMM is added to staff tasks rather than a critical component of their main responsibilities;

- **Technical Assistance:** TFIs interested in integrating ESG/IMM considerations into their business processes have a limited understanding on how to do so, making technical assistance and support ever more relevant;

- **International Standards:** Whereas some TFIs understand the importance of aligning their impact practices with industry standards (e.g., IFC Exclusion List; UNPRI Principles; or the UN Global Compact), fewer TFIs have the capacity to counting beyond numbers, capturing the “impact” of their investment on Gender and ESG issues, and/or setting impact targets that they would like to see as a result of their investments.

When originally designed, the PCB component was envisioned to generate for participating TFIs including: reducing portfolio risk through the identification and management of material GESG factors; enhancing their understanding of the relationship between financial performance and impact/Gender/ESG; and strengthening their relationships with SME clients through the provision of value-added services. This would ultimately improve deal sourcing through better integration of Gender/ESG factors and improve TFIs’ investor reporting on impact performance, helping them to attract additional limited partners, especially those with an impact focus. However, the completion of the PCB process, as reported in the previous section, has been delayed primarily by the competing priorities these financial intermediaries face.

For example, while private and institutional investors provide capital to these firms and validate their professionalism and authority as intermediaries—therefore, enabling their actions in the sector—, investors also demand both accountability (e.g., justification of decisions and explanation of failures) and good financial results—therefore, constraining their actions in the sector. The financial performance of these intermediaries ultimately influences the flow of money into or out of their funds. Gaining momentum on the implementation of the PCB has experienced some friction and COVID-19 has further delayed the prioritization of this component when compared to other competing priorities of these funds.

The support of MEDA’s investment partner, Sarona, has played a significant role in reactivating the conversations when STFF investees become non-responsive to Trading Up’s communications. By following a customer-centric and flexible approach to the implementation of the PCB (e.g., co-creating TA plans that are flexible and driven by business imperative, recognizing that TFIs possess the deepest understanding of their needs and opportunities); closely communicating with Sarona and co-creating smart solutions for troubleshooting and risk management (e.g., including PCB-linked clauses in the side letters investees adhere to); and by gathering customer feedback through multiple avenues—including pre and post client satisfaction surveys and monthly check ins—, Trading Up continues making progress in the implementation of PCB activities with existing and upcoming partners.

In a recent op-ed piece at The Globe and Mail, Tariq Fancy, former Chief Investment Officer for Sustainable Investing of BlackRock Inc.—the world’s largest asset manager—, recognizes that investment professionals “are trained to chase yield and profits” and that “for many investments and strategies, such as highly liquid ones with short holding periods [e.g., TFIs]” fiduciary obligations and short-term incentives invite them to focus on monetary outcomes, rather than environmental and social ones. When TFIs raise capital to serve more clients and/or expand their services, they usually
do so by responding to the requirements of investors who constantly demand good financial performance rather than social and/or environmental results. Through Trading Up, MEDA aims at demonstrating that STFF TFIs that have built their Gender/ESG/IMM capabilities through the Project’s PCB have greater capacity to clearly benefit SMEs in their portfolio.

Conclusion

Partnering TFIs face internal and external pressures to generate above-market returns, first, and social/environmental outcomes, second. Whereas the COVID-19 crisis increased the economic and social vulnerability of already vulnerable communities, the pandemic also created opportunities for the impact investing sector to demonstrate its resiliency and commitment to its raison d’être: impact first, returns, second. However, partnering TFIs continued experiencing pre-COVID-19 expectations primarily driven by short-term results, pressuring them to implement stricter underwriting standards and shifting to sectors less vulnerable to COVID-19 lockdown waves. Nevertheless, STFF investees are keen to integrate impact considerations in their operations and processes. This could explain why, during the height of the COVID-19 crisis, these TFIs actively worked with their borrowers to restructure some of the loans to longer repayment schedules. These firms worked with their clients to reschedule their loans onto longer-dated repayment plans, ranging from 1-month rescheduling to 24-month amortizing loans.

With the PCB support of Trading Up these partnering organizations are building the case for future iterations of similar blended finance partnerships. While the impact journey of STFF TFIs can better be represented in a spectrum (i.e., some TFIs are only starting this process and others are well advanced and widely recognized), all partnering financial intermediaries have a commitment to enhancing their Gender/ESG/IMM processes and considerations to clearly benefit portfolio SMEs.

In December 2020, the STFF completed its first commercial closing. Since inception, the Fund has invested approximately CAD 18.5M, providing loans to more than 86,000 SMEs; contributed to the creation of approximately 7,000 jobs; and supported almost 60,000 jobs.

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Endnotes

1. For more information on Trading Up, please visit: https://www.meda.org/investment-projects/585-trading-up.


3. These steps are illustrative and the timeframe might vary depending on the specific context of the TFI.

4. This questionnaire builds on MEDA’s Gender Equality Mainstreaming (GEM) Framework, a practical manual and toolkit for assessing gender equality, and identifying, implementing and measuring gender equality mainstreaming strategies within companies. For more information on the GEM Framework, please visit: https://www.meda.org/gem.

5. Certified B Corporations (or B Corps) are businesses “that meet the highest standards of verified social and environmental performance, public transparency, and legal accountability to balance profit and purpose.” For more information on certified B Corps, please visit: https://bcorporation.net/about-b-corps.

6. ImpacAssets 50 (IA 50) annually features a list of asset management firms and funds that “demonstrate significant commitment to social impact and track clear measures of social and/or environmental impact.” For the latest IA 50 list, please visit: https://www.impactassets.org/publications_insights/impact50.

7. For a comprehensive analysis of “Enabling and constraining” actions in investment relationships, please refer to Arjaliès et. al in “Chains of Finance: How Investment Management is Shaped” (Oxford, 2017).