An Assessment of the Trade Finance for SME's in Tanzania—A Case Study of CRDB Bank Plc

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***Abstract*—This study examines trade financing at CRDB Bank, focusing on costs, awareness, and efficiency among Small and Midsize Enterprises (SME) customers. It evaluates the bank's provision of trade finance products like Letters of Credit, Guarantees, insurance, lines of credit, factoring, and supplier credit, both locally and internationally. Using a case study approach and descriptive research design, the study sampled 130 individuals, with 108 complete responses. Quantitative methods, including questionnaires and data analysis via Excel, chi-square tests, and SPSS for ANOVA, were employed. The researcher sought to understand the challenges customers face in accessing Tanzania's trade finance products and services. The researcher evaluated the relationship between trade finance utilization and SME's performance indicators, such as profitability, export capacity, and market access. According to the study, improving trade finance instruments such as letters of credit, trade credit, and export financing can significantly enable SMEs to engage in international trade. SMEs, that used trade finance, also reported reduced operational and overhead costs, more accessible reach into global markets, and improved cash flow and growth rates. Interest rates, collateral requirements, and little financial literacy are reasons most SMEs lack access to finance. Recommendations are for CRDB Bank to promote training sessions to boost SMEs' understanding of trade finance products and their advantages and introduce more flexible collateral or risk-sharing arrangements. As an important enabler, CRDB Bank contributes toward the growing individual and international competency of Tanzanian SMEs through trade finance. In conclusion, SMEs that do succeed in exploiting Trade Finance enjoy better operational capacity in the face of adversity. Working to overcome the obstacles identified in this study will help to improve accessibility to trade finance further also supporting the broader economic development of Tanzania's SME sector.**

***Keywords*—cost, awareness, efficiency**

I. Introduction

Trade finance refers to multiple financial intermediation arrangements between buyer and seller of goods and services encompassing different credit mechanisms such as Letters of Credit, Guarantees, Insurance, lines of credit, factoring, and Supplier credit (Nyarko, 2021; Hikelman, 2008). Trade financing plays an important role in shifting the risk from the exposure that a seller/an exporter creates on the buyer/importer for parting with goods and or services before receipt of payment through banks. To guarantee payments on the due date, the importer bank issues a Letter of Credit to shift the risk of non-payment by the importer to the importer bank (Nyarko, 2021). Banks also offer credit mechanisms such as international leasing, lines of credit to importers and exporters, project financing, and buyer credits (Abor, 2007). Other credit arrangements that equally expose banks to credit risks are insurance and Bank Guarantees.

According to Lwindiko *et al.*, (2014), numerous studies have shown that Micro, Small, and Medium Enterprises (MSMEs) employ a significant number of people in the low-income bracket hence, the need for reliable and cost-effective financing. MSME businesses play a significant role in poverty reduction through job creation and income generation. However, MSMEs from developing countries are exposed to several challenges in their business operations including financing.

A large portion of import and export trade in Tanzania is intermediated through banks and insurance SMEs (Asmundson *et al.*, 2010). In this arrangement, importers effectively transfer performance and payment default risks to intermediaries including parallel financiers. A significant portion of the world's trade in goods and services is financed through open accounts where the exporter assumes the risk of default in payment by the importer. In open account trading, payment by importers to exporters is effected directly without going through intermediaries like banks and insurance, usually after receiving goods or services. In such a trade arrangement, the exporter finances the importer. In the cash-in-advance trade agreement, exporters receive payment before delivery of goods or services. In this arrangement, the importer assumes the risk of non-delivery of goods or services at the opposite end of the spectrum from open accounts. In these, importers pay for goods before they are shipped, and this places both non-performance risk and the burden on working capital on the importer.

Gladson and Gideon (2020), underscored the important role of trade finance in international trade. Numerous studies conducted on trade fiancé in Tanzania have shown a significant positive impact on the country's economy.

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However, there is limited awareness of trade fiancé products and services at local and national levels necessitating the urgent need for a public awareness campaign by the government through the Bank of Tanzania. According to Danielson and Scott (2004), because of the difficulties in accessing trade finance, customers have opted for credit cards and supplier credit to circumvent restraints that banks and financial institutions impose on SMEs. Consequently, customers use the most expensive cost of funds by providers of credit cards and supplier credit.

A. General Objective of the Research

An assessment of trade finance in Tanzanian SME market a case of CRDB Bank Plc.

B. Specific Research Objectives

The research objectives to guide this project were: (i) An assessment of SMEs' awareness of trade finance products. (ii) An Assessment of the costs, and (iii) An assessment of the operational efficiency of commercial banks in the rendition of trade finance products and services to SMEs.

C. Research Questions

What challenges do customers face in accessing Tanzania's trade finance products and services?

Respondents were asked to rate the accessibility of trade finance, obstacles to offering trade finance products and services, lending institutions' ability, borrowers' ability, and benefits of trade finance to SMEs at CRDB Bank Plc on a scale of 1 to 5, where 5 is the highest and 1 is the lowest.

D. Conceptual Framework

Trade finance represents the financial instruments and products associated with trade in international commerce. It also includes services such as lending, Letters of Credit (LCs), factoring, export credit, and insurance. Trade finance essentially exists to help mitigate the risks around international trade, for importers and exporters by ensuring liquidity while promoting cross-border trading of goods and services.

Trade finance is a financial service that enables trade between exporters and importers that involves interaction between three agents namely; exporting firms, centers engaged in manufacturing goods to be exported, arms-length buyers overseas, or foreign affiliates within multinational company institutions such as banks.

Trade finance navigates a track of payment instruments to keep the importer and exporter from risk of default. These can be Letters of Credit (LCs), a formal guarantee by the bank to pay the exporter on behalf of an importer, assuming that export goods or services will be delivered according to contract terms. Bills of Exchange, a bill is a written order by the exporter telling his representative to pay some amount on a certain future date, and the open account, wherein the goods are shipped and delivered before payment is due to the exporter, thus offering credit terms from the importer's perspective. These are important functions of trade finance that help to mitigate the risk on a large scale.

Trade credit insurance or export-credit insurance protects exporters on receivables from the political, economic, and commercial risks of non-payment by importers. Factoring is also an important source of financing that encompasses financial institutions buying the exporter´s accounts receivables at a discount so that it receives some working capital, and in turn, gets into risk of collection with either the end buyer or prospective customer. Another feature of trade finance is working capital financing which helps SME customers with their cash flow management. SMEs doing export and import trade depend on working capital financing to fund activities before revenue collection. Some important financing tools are pre-shipment financing where the exporter gets the funds before his goods are delivered, and post-shipment finance where exporters can receive payment after delivery based on the value of goods or services received.

Banks, suppliers, and other non-bank financial institutions provide credit facilities, issue LCs, and offer risk mitigation services. International entities like the International Chamber of Commerce (ICC) published rules, such as the Uniform Customs and Practice for Documentary Credits (UCP 600), which harmonize trade finance practices across all institutions worldwide. The presence of financial technology SMEs (FinTechs) is rapidly revolutionizing innovations in the trade finance sector. For instance, the deployment of block-chain technology in trade finance, and paper-intensive processes could be reduced considerably to improve transparency, reduce fraud, and help speed up transactions.

II. A Review of the Professional and Academic Literature

Trade credit is essential for enabling and financing commerce for those who may not have the cash to purchase goods outright. Trade credit also protects the parties against local and international trade risks. SMEs are the backbone of Tanzania's economic activity and employment, representing over 90% of businesses in the country (Olewale & Smit, 2010). However, the availability of trade finance for these businesses is difficult and limits them from trading in local and international markets.

A. Working Capital Finance for the SME Sector in Tanzania

Trade finance consists of financial instruments like letters of credit, bank guarantees, lines of credit, trade credit insurance, and factors that help businesses mitigate risks associated with international trade to overcome cash flow constraints (World Trade Organization [WTO], 2016). Most SMEs in Tanzania are found to be involved mainly in the agriculture, manufacturing, and retail trade sectors (Ngowi, 2019), which all need financing to capture both imports and exports. Yet, low financial diffusion and costly transactions concerning trade finance ensured that it remained out of reach for most SMEs.

B. Challenges to Trade Finance for Smaller Businesses

Many barriers prevent SMEs from obtaining trade finance in Tanzania. The leading challenge that SMEs encounter is the lack of security/collateral. Lending to Tanzanian SMEs are conducted on an informal basis because there are no collaterals (Ndunguru, 2018). Consequently, banks are extremely reluctant to offer trade finance products for SMEs due to the substantial default risk. Furthermore, SMEs pay high interest and fees for trade finance products, rendering them unaffordable (Kira, 2021).

The inability of SMEs to trade locally and internationally for whatever reason is a barrier, and so is the lack of financial literacy (Marwa, 2014). Salum (2020) stated that some entrepreneurs do not know the available trade finance options and have no financial literacy to understand complex financial products. A lack of knowledge of traders contributes to the low-level use of formal financial products and massive dependence on informal lenders such as shortcut banks borrowing from family or friends, and unlicensed lenders.

C. Role of Financial Institutions in Trade Finance

Trade finance is provided through financial institutions with banks being the most important participants. For example, in Tanzania CRDB Bank, the National Microfinance Banks (NMB), and other commercial banks issue Letters of Credit and other export facilities like export credit guarantee schemes (CRDB Bank, 2020). However, there is poor uptake among SMEs. Banks do not provide loans easily due to strict eligibility criteria and high transaction costs. Additionally, SMEs find the application process for trade finance products too bureaucratic and lengthy (Mungaya *et al.*, 2020).

With the Fintech sector gaining momentum, several new funding methods have cropped up for SMEs. One such example relates to services provided by a mobile banking platform like M-Pesa which has enabled access to microloans for SMEs that can, in turn, be utilized for financing trade activities (Jack & Suri, 2016). The transaction costs are relatively low, making it possible for rural businesses to use digital financial services that do not require physical collateral.

D. Measures Taken by the Government of Tanzania to Increase Credit in Trade Finance

According to Lwindiko *et al.*, (2014), the Tanzanian government has taken several measures to broaden trade finance opportunities for SMEs. Several initiatives are outlined in the National Financial Inclusion Framework (NFIF) 2018–2022 which targets improving SMEs' accessibility to financial services, and trade finance inclusive (Bank of Tanzania, 2018). For example, credit guarantee schemes that provide either total or partial guarantees on loans to SMEs from banks significantly reduce risks for financial institutions (Lotto, 2019). While these schemes have been moderately successful in encouraging banks to lend to SMEs, they are severely limited by insufficient funding and implementation bottlenecks.

According to International Finance Corporation (2020), the government has collaborated with global institutions like the International Finance Corporation (IFC) through its Global Trade Finance Program (GTFP)., and the Africa Import and Export Bank (AFREXIM) to facilitate SMEs' access to trade finance. IFC and AFREXIM issue guarantees to banks on trade-related transactions according to a Cost, Insurance, and Freight (CIF) publication allowing the market in general and SMEs in particular access to facilitate credit services. However, in other parts of the country, these programs are still nascent and more work is necessary to make them appropriate for addressing characteristic systemic issues SMEs face.

E. COVID-19 and the Trade Finance for SMEs

Tanzanian SMEs struggle with trade finance access and the COVID-19 pandemic has worsened the predicament. Other factors, like disruptions in global supply chains and declining demand for goods, have further challenged the cash flow of SMEs, increasing the need to finance (World Bank, 2021). Consequently, the economic uncertainty prompted by the pandemic has seen banks become even more risk-averse, limiting trade finance elsewhere (Gagnon, Kamin, & Kearns, 2023). The Tanzanian government responded by introducing stimulus packages to support SMEs, but these have had limited effects in improving access to trade finance (UNCTAD 2021).

III. Findings and Discussions

The analysis shows that a large percentage of the questionnaires were completed by CRDB Bank clients (57%) and bank employees (28%). Demographically, men constituted 58% of the clientele, with women making up 42%. The predominant age group among CRDB Bank's customers was 35 to 45 years, accounting for 49%, followed by 34% in the 18–35 age bracket, and a mere 6% over 45 years. Notably, 90% of the clients held college or university degrees, while 10% had completed high school, with no primary school graduates reported. This demographic suggests a client base that is well-educated and informed. Besides trade finance, CRDB Bank provides a diverse portfolio of services to its customers including; lending, deposit-taking, and payments services.

Client preferences on banking products and services leaned towards current and savings accounts (28%), loans (36%), and trade financing (32%), with a smaller percentage (5%) utilizing other services like fixed deposits, overdrafts, and electronic money transfers. Trade finance, current, savings accounts, and loan services emerged as strategic offerings in the higher consumption bracket. The client base comprised 24% individual/personal clients, with corporate clients at 4%, and SMEs forming the majority at 64%, a distribution that underscores the bank's strategic focus on the SME market.

A. The Attainability of Trade Finance Products and Services

Concerning the survey results on the accessibility of trade finance products and services, the general tendency is towards optimism as a great proportion is satisfied with the scale and level of accessibility. In particular, 75% of respondents viewed the accessibility level of the trade and export finance services as excellent. In comparison, only 20% regarded this as good; merely 5% felt it was bad and gave a poor rating. These results are useful for understanding the level of accessibility in trade finance and the objective of the financial institutions and business entities. There were very few people who viewed the trade finance products and services accessibility level as poor, nonetheless, these few are indicative that there is a challenge that SMEs would like to see resolved. There is a structure with networks that facilitates access to financial support in every organization. This could be attributed to several factors such as:

i) CRDB Bank has integrated its systems with customers to enhance the delivery of trade finance products such as letters of credit, export financing, and guarantees. This high rating could be attributed to online platforms and mobile banking systems.
ii) Trade finance services are likely becoming more customized to the size and nature of businesses. The degree to which loan approval times are drastically reduced, terms and conditions are highly flexible, and the level of risk involved is well managed.
iii) In terms of enhancing accessibility, CRDB Bank has extended geographical outreach and cross-border trade finance solutions to places like Burundi and The Democratic Republic of Congo (DRC) which could have also been an added advantage. With increased international trading by businesses, the trend in the financial sector has been to seek to make more of their products and services accessible across the board.

Of the respondents, 20% rated trade finance accessibility as good rather than excellent indicating that while there are positive aspects, some may be lacking. For instance, trade finance is often seen as a multi-actor crossing through banks, export credit agencies, insurers, and other stakeholders. Some respondents may have thought that while access was generally adequate, examining numerous alternatives was complicated or tedious. SMEs operating in remote locations or banking with banks with few branches still have challenges accessing trade finance products and services as easily as their more mature market colleagues. The 5% of respondents who rated trade finance services accessibility as poor are expressing that for a limited number of businesses, there are still exceedingly high galactic barriers:

One possible reason for poor ratings is their poor understanding of the mechanics of trade finance products. SMEs new to foreign trade may have scarce chances to get such information or recommendations from banks. Small and Medium-sized Enterprises (SMEs) may not pay the cost of trade finance products tailored to them, which may be why they tend to complain about the services offered.

From the findings of this research, it is clear and quite evident that SMEs have positive attitudes towards the availability of trade finance products and services as can be expected from the market development efforts in the industry. Nevertheless, some still struggle with issues that need to be dealt with, such as those with small SMEs or those located in less developed regions in Tanzania. This shows, the financial institutions, that there is still a need for more creativity, streamlining of processes, and provision of personalized services so that all types of businesses can harness the benefits that are offered by trade finance products and services.

B. Obstacles in Offering Trade Finance Products and Services

As for the research findings about the perceived constraints in offering products and services in trade finance, there are encouraging views. In particular, 14 % regarded the constraints as excellent, 6% good, and 80% poor. In general, these findings, for example, suggest that businesses and institutions consider the challenges related to offering trade finance facilities to be insignificant. The fact that only 6% of the respondents rated the obstacles as significant means most of them over 80% feel that the potential markets for trade finance products and services have very well-controlled risks. Several factors could explain this strong positive assessment:

Trade finance incorporates significant exposure to counterparty, currency, and political risk. Therefore, the high percentage of people rating the Obstacles as insignificant is because most of the obstacles especially counterparty risk have been watched closely through the adoption of modern-day credit protection measures such as credit insurance and other hedging tools as well as proper due diligence measures that have become routine. Automation, Blockchain, and Artificial Intelligence (AI) tools for risk assessment and transaction processing have likely made operations more efficient, helping to provide trade finance solutions effectively and on a larger scale.

In many regions, trade finance regulatory frameworks are well-defined and stable. This reduces compliance and operational risks, contributing to the overall positive outlook. Moderate Perception (14% Rated Good). The 14% of respondents who rated the obstacles as good instead of excellent may recognize challenges that, while manageable, still disrupt the trade finance product delivery process. Trade finance products require customization to meet client needs, the type of goods traded, and the regions involved. This complexity can create operational hurdles, even though they are not overly burdensome.

Six percent of the participants rated the hurdles unfavorable, implying that a few businesses or financial institutions still face obstacles in providing trade finance products and services. Areas where regulations are not as reliable or stricter than others may face challenges when it comes to providing trade finance services. For financial institutions to navigate smoothly through complexities, more government intervention is needed in this area of business operations.

Trade finance demands resources, for management encompassing risk evaluation and due diligence to transaction oversight and reporting. Smaller organizations or those operating in developing markets may encounter challenges, with the operational expenses linked to providing such services, which could account for the unfavorable rating. Some trade finance providers might be unable to utilize the technologies and systems that have made trade finance more efficient.

Most financial institutions seem to consider the challenges in providing trade finance products and services either a thing of the past or successfully overcome as reflected by research findings, signaling risk management, technology adoption, and regulatory compliance initiatives have paid off. The survey also showed a small group struggling to overcome regulatory constraints, resource issues, operational challenges, and technology shortcomings. These may profit well with more investments in digital infrastructure, compliance capabilities, and personalized risk management strategies to overcome the challenges faced in their trajectory to digitalization.

C. Lending Institutions Capability in Trade Finance

Trade finance research found that the general perception of lending institutions in trade finance is quite good with 70% scoring their capabilities as excellent,18% as good, and only 12% as poor. The 70% of respondents that awarded lending institutions in trade finance the highest rating possible is a strong affirmation of their satisfaction with trade finance offered by CRDB Bank. There could be reasons such as; the bank having considerable experience in navigating all of trade finance’s impediments and intricacies in structured products such as letters of credit, guarantees, and export financing. This high rating is attributed to its capability to customize financial solutions according to the requirements of businesses and their understanding of international trade practices.

The 18% of respondents who rated the capabilities of lending institutions as "good" rather than "excellent" know that institutions are doing well but can still improve. Factors that can be attributed to this moderate rating include; some SMEs may think that even though banks are generally skilled in offering loans, the number of loan products or the flexibility of the terms is not as personalized as it should be. Even though most people gave a positive rating, some still go through time delays in approval processes or bureaucratic red tape when dealing with lending institutions.

The research results speak very clearly with a massive 55% of SMEs rating the cost in trade finance as poor because it is simply too costly or worse, these costs are hard to see. Several SMEs have seen value in trade finance, despite charges that may be imposed above and beyond what they can afford to pay. There is still great demand from another section too which wants more transparency, ease of cost structures, and tailor-made solutions to make it affordable from their hard-earned money. This, in turn, would help to make trade finance for SMEs fairer and more inclusive, enabling a larger share of SMEs that could benefit from global trading opportunities.

The 12% of respondents who rated the ability of lending institutions as poor, was the case of a subset of businesses that have been affected by a significant number of difficulties. Among others, this could be from lending institutions that have not yet fully embraced or remained up-to-date with the technological developments in trade finance. Banks that still prefer to use manual processes or outdated technologies, may attract inefficiencies and higher transaction costs, which will frustrate the clients who need quick financing.

The research findings show that many respondents perceive lending institutions as highly skilled in trade finance. This is because of the sector’s risk management skills, expertise, and other factors. Product personalization, process optimization, and increased risk appetite enable lending institutions to meet these needs. Trade finance is critical for Small and Medium-sized Enterprises (SMEs) that wish to scale up globally.

D. Advantages of Trade Finance for SMEs

Working capital is one of the leading benefits SMEs get from trade finance. Businesses can increase liquidity through trade finance solutions like letters of credit, invoice factoring, and trade credit insurance that expedite the release of capital tied up in receivables or reduce exposure to non-payment from international buyers. The overseas market can lead SMEs to multiple risks from payment defaults, currency changes, and geopolitical instability. These trade finance instruments act as a cushion, where payments are guaranteed and SMEs can avoid such losses.

With the help of trade finance, SMEs can also explore new marketplaces and expand their core business by mitigating global-reaching transaction risks. SMEs that may not have adequate capital, can enter global trade with confidence when they have access to trade finance. The main problem with the foreign market is that it exposes SMEs to multiple risks including default on payments, fluctuations in currency value, and sometimes even physical as well as war and other acts of God. These trade finance tools are an interesting intermediary in which payments are sure and SMEs can avoid losses.

Trade finance also helps SMEs discover new marketplaces and grow their core business by reducing transaction risks wherever they go in this global-reaching marketplace. For SMEs with no capital to handle the risk, trade finance allows such entities greater confidence in entering global trade. Trade finance can have an even larger impact on SMEs globally if we increase awareness, simplify processes, and enhance accessibility.

E. Implication for SMEs

The cost of trade finance is high for SMEs and continues to be one major challenge. The same research shows that only 25% of SMEs rated it as excellent while 20% considered the cost of trade finance to be good with a large majority (55%) rating it as poor. The distribution indicates that most SMEs see trade finance as having major benefits to their business with no major concern about cost. This may restrict SMEs’ ability to expand their businesses to international markets.

F. Proposal for Subsequent Research

This study assessed SMEs' awareness of trade finance products and the cost and operational efficiency of trade finance providers, with CRDB Bank as the case study. Future research should explore the advantages and disadvantages of the worldwide adoption of Artificial Intelligence and Block-chain in trade finance to assess the impact of technology and innovation on trade finance.

IV. Conclusion

Trade finance is vital for Tanzanian SMEs to participate in local and international trade. However, many are shut out by the restrictions on trade finance because they have no collateral or cannot pay the high costs of transactions, including a lack of financial literacy. Financial institutions and government programs have made some effort to widen access but are generally not directed enough at the specific needs of SMEs in Tanzania. Fintech and Digital Financial Services can widen access and affordability. However, as Tanzania continues to broaden its financial infrastructure it needs to take a collective stance for SMEs and allow them to contribute to economic growth.

For Tanzania's economy to prosper in trade, high costs and other impediments such as the availability of requisite trade finance instruments must be tackled to enhance accessibility. Cost of accessibility, increased branch network, and less expensive trade finance instruments have improved efficiency, brought significant savings to SMEs due to the low transactional costs, and influenced more clients to use trade finance instruments. Findings also show a general lack of awareness in the market regarding CRDB Bank's trade finance products and services.

Conflict of Interest

The author declares that there are no conflicts of interest concerning the publication of my research. I did not receive financial aid during my study, and no financial support or personal connections have influenced the study's outcome.

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