



Fiscal policy and trade finance in emerging economies: Evidence from Africa

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Abstract

The paper examines how fiscal policy shapes trade finance in emerging economies with particular focus on Africa. In the past, the international trade finance market was thought to be liquid and efficient. However, it has recently gone through stressful times, most notably after the period following the 2008 Lehman crisis, necessitating quick structural adjustments. Given that trade finance makes up a growing portion of global trade, developing nations, especially those in emerging market economies in Africa, may be more concerned about its functioning. Nonetheless, a persistent trade finance gap across the continent, regulatory dissonance, exchange rate volatility and macroeconomic instability are just a few of the intricate structural limitations that African economies must contend with. The paper shows that fiscal policy can address trade finance gap through government spending that directly reduces risk for private lenders, and through tax policy that improves the cash flow and profitability of trading businesses, making them more creditworthy. It further reveals that fiscal policy can resolve trade finance constraints through macroeconomic stability and financial sector development.

Keywords

- fiscal policy
- government expenditure
- macroeconomic stability
- taxation
- trade finance

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Introduction

Historically, authorities paid little attention to the global trade finance market since it was thought to be liquid and well-functioning. However, the industry has lately gone through stressful times, most notably following the 2008–2009 Lehman collapse and in late 2011, when funding issues at European banks sparked worries about potential disruptions. Additionally, the industry seems to be undergoing early structural transformation, as seen by the entry of new market players and initiatives to create new modalities that minimise the use of bank resources and balance sheets. However, persistent data inadequacies have made it challenging to monitor and analyse the significance of current market dynamics as well as the magnitude and impact of recent dislocations (BIS, 2014).

The strategies and tools used to finance international trade have recently received more attention in the literature (Ahn, 2011; BIS, 2014; IMF, 2018; Niepmann & Schmidt-Eisenlohr, 2017). Scholars have emphasised the role that shocks to the supply of banks' trade finance services played in the "Great Trade Collapse" that followed the global financial crisis of 2008 (Accominotti & Ugolini, 2020; Ahn et al., 2011; Amiti & Weinstein, 2011; Del Prete & Federico, 2014; Niepmann & Schmidt-Eisenlohr, 2016; Paravisini et al., 2015).

Trade is unquestionably a significant driver of development, but for it to be successful, sufficient funding and support for capacity building are necessary. By bridging the gap between importers' and exporters' divergent expectations regarding when payment should be made, credit and credit insurance help to lubricate trade. For this reason, it is critical to find and fill any funding shortages that may arise. Because importers and exporters are supported by established banking sectors, trade finance is sometimes taken for granted in industrialised nations. Small and medium-sized businesses (SMEs) often have less collateral, guarantees and credit history than larger companies, which makes it difficult for them to obtain finance even in these countries (AfBC, 2025; Ntoya, 2025; World Bank, 2025; WTO, 2016).

Given that they make up an ever-growing portion of global trade, developing nations, especially those in emerging market economies, may be more concerned about trade finance. In addition to unique hurdles including smaller, more selective and sometimes less developed local financial industries, developing countries may have some of the same issues as their developed counterparts, such as creditworthiness recognition. Access to the information and abilities needed to handle trade finance instruments is a major problem in many developing nations. As developing economies look to take advantage of the trade opportunities presented by changing patterns of production, adequate trade finance is crucial (WTO, 2016).

This paper attempts to assess the extent to which fiscal policy shapes trade finance in emerging economies, with particular emphasis on Africa. Specifically, it examines how fiscal policy mechanisms in African countries are tailored to support trade finance. It also evaluates how fiscal policy and trade finance interventions are utilised by African countries to foster macroeconomic growth. Lastly, the paper identifies possible fiscal policy adjustments to restructure the trade finance trajectory in Africa.

1. Conceptual review

1.1. Fiscal policy

Fiscal policy is an instrument by which a government regulates its spending in order to control and influence the economy. Fiscal policy is widely perceived to be linked to growth; more specifically, it is believed that appropriate fiscal policies can be utilised in specific circumstances to boost economic growth and development (Khosravi & Karimi, 2010). Proponents of government intervention in economic activities argue that it can boost long-term growth. They cite the government's role in maintaining efficiency in resource allocation, market regulation, economic stabilisation and social dispute resolution as examples of how the government could use fiscal policy to stimulate economic growth (Mengistu, 2022).

1.2. Trade finance

Trade finance is the oldest form of international finance. Since the beginning of international business, merchants and firms have shown the need for working capital to finance their international commercial operations and have sought ways to lessen the risks associated with long-distance trade. International trade necessitates the immobilisation of significant quantities of cash in a relatively short (but substantial) period of time, as well as the acceptance of significant risks by both exporters and importers. Trade finance refers to all tools and procedures that allow businesses to get capital to fund their international activities and/or decrease the risks associated with international trade (Accominotti & Ugolini, 2020; Asmundson et al., 2011; BIS, 2014).

2. Review of related literature

2.1. Political economy of fiscal policy

The importance of fiscal policy as a policy instrument has fluctuated over time. Laissez-faire, or limited government, was the dominant philosophy prior to 1930. After the Great Depression and the stock market crash, policymakers pushed for governments to get more involved in the economy. Countries had lately reduced the size and influence of government, with markets playing a larger role in the distribution of goods and services. However, many countries reverted to a more active fiscal policy when the global financial crisis threatened to trigger a global recession. Governments can affect the economy through fiscal policy by altering the amount and kinds of taxes, the amount and nature of spending, and the amount and extent of borrowing (CFI, 2019; Horton & El-Ganainy, 2017).

The economy's usage of resources is influenced by governments both directly and indirectly. This is illustrated by the fundamental national income accounting formula, $GDP = C + I + G + NX$, which calculates an economy's production, or GDP, based on expenditures. GDP, or the total worth of all finished products and services generated in the economy, is shown on the left. Private consumption (C), private investment (I), government purchases of goods and services (G) as well as exports less imports (net exports, NX) are the sources of aggregate expenditure or demand on the right. It is clear from this equation that governments have an impact on GDP, controlling G directly and indirectly influencing C, I and NX through changes in taxes, transfers and spending. Fiscal policy that directly raises aggregate demand by increasing government spending is generally referred to as expansionary or "loose". Conversely, contractionary (or "tight") fiscal policy is frequently used if it lowers demand through lower spending (Horton & El-Ganainy, 2017).

Fiscal policy goals differ from one country to another though a major focus shows its objective of delivering goods and services such as basic education, transportation and public safety. Governments may prioritise macroeconomic stabilisation in the short term, which could involve reducing spending or raising taxes to counteract rising inflation or to lessen external vulnerabilities, or increasing spending or lowering taxes to boost a struggling economy. Longer-term goals could include promoting sustainable growth or lowering poverty through supply-side initiatives to enhance infrastructure or education. Even though these goals are generally the same across nations, their relative significance varies based on the specific conditions of each nation. Priorities may change in the short term in reaction to a natural disaster, the business cycle or an increase in the price of food or gasoline globally. Longer-term factors may include endowments of natural resources,

population or development levels. In an advanced economy, pension reforms may target the long-term expenditures associated with an aging population, while in a low-income country, the goal to decrease poverty may cause spending to shift toward primary health care. By reducing procyclical spending, both by avoiding painful cuts when oil prices fall and by limiting spending spikes when they rise, policymakers in an oil-producing nation may seek to better align fiscal policy with broader macroeconomic developments (CBN, 2017; Weil, n.d.).

An excellent case study of fiscal policy is the global crisis that originated from the collapse of the US housing market in 2007. Global economies were impacted by the crisis, since private consumption, investment and foreign trade were all negatively impacted by financial sector issues and declining confidence (all of which affect output, GDP). In response, governments attempted to increase activity through two means: fiscal stimulus, which includes increased discretionary spending or tax breaks, and automatic stabilisers. Stabilisers are not dependent on particular government actions; rather, they take effect when tax income and expenditure levels fluctuate. The business cycle has an impact on how they function. For example, under progressive tax systems, where higher-income earners are placed in higher-tax-rate categories, the amount of taxes collected decreases as output slows or diminishes because company profits and taxpayer incomes decline. During a recession, unemployment compensation and other social expenditures are also intended to increase. Fiscal policy is inherently contractionary during upturns and expansionary during downturns due to these cyclical shifts (Horton & El-Ganainy, 2017; TPC, 2024a, 2024b).

The size of the government is correlated with automatic stabilisers, and advanced economies typically have larger governments. Since both strategies lessen the consequences of a downturn, there may be less need for stimulus in areas with larger stabilisers. Examples of these strategies include tax cuts, subsidies and public works initiatives. In fact, nations with bigger stabilisers tended to use fewer discretionary measures during the most recent crisis. Furthermore, automatic stabilisers are not impacted by implementation delays like discretionary measures are, even though the latter can be adjusted to stabilising requirements. (For instance, designing, obtaining approval and implementing new road projects can take time). Moreover, automatic stabilisers – and their effects – are automatically withdrawn as conditions improve. Designing and implementing stimuli successfully can be challenging, and when conditions improve, they can be challenging to reverse. But in many developing market and low-income nations, stabilisers are comparatively weak due to institutional constraints and limited revenue bases. Even in nations with bigger stabilisers, there might be an urgent need to make up for the lost economic activity and strong arguments for directing the government's crisis response toward the people who are most in need (TPC, 2024a, 2024b; Weil, n.d.).

2.2. How does fiscal policy shape trade and trade balances?

Fiscal policy's direct effect on the balance of payments makes it easy to understand how it influences trade. If fiscal policy refers to the relationship between government spending and tax revenues, and "balance of payments" refers to the current account balance (merchandise trade plus net services and investment income), then the following is true: increasing government spending will substantially increase the current account deficit while maintaining constant revenues and net private saving (private saving less private investment). It follows that unless net private saving increases, the current account deficit (capital inflows) cannot decrease without a commensurate (but causative) decrease in the budget deficit. If accommodating capital inflows are only accessible at a higher interest rate, the increase in net private saving could occur at the same time as a recession and the collapse of private investment (Linn & Wetzel, 1990; Makin, 1989).

Normally, a regime of fixed exchange rates would be used to explore the relationship between fiscal policy (tax and spending) and the balance of payments. Domestic interest rates would experience early upward pressure from more expansionary fiscal policy. At a given global interest rate, capital inflows support fiscal expansion in a Mundellian small-country world with indefinite capital mobility. In the absence of monetary accommodation by the central bank or an endlessly elastic (with regard to interest rates) money demand schedule, the "crowding-out" that leads to a closed-economy setup does not lessen the positive influence on aggregate demand. In the fixed exchange-rate scenario, fiscal expansion has no net effect on the balance of payments, but this conceals a shift in its constituent parts. Unless there is a shift in private net saving or government intervention in foreign exchange markets, the increased capital inflow will be matched by an increase in the current account deficit. In other words, a greater current account deficit is a result of a capital inflow from outside that supports an increase in national dissaving (Dean et al., 2020; Makin, 1989).

As long as the higher interest rate does not increase net private saving by precisely the same amount as the increase in government dissaving, a portion of the capital inflow may come from official intervention in the foreign exchange market intended to peg the exchange rate if private capital is not infinitely mobile. The demand for foreign currencies will be excessive if net private saving growth falls below that key threshold and private capital inflows are insufficient to offset the increase in national dissaving. According to Lane and Perotti (1998), in the event where the exchange rate is completely flexible, the currency depreciates until the sum of increased interest rates and currency depreciation raises net private saving by the same amount as the increase in government dissaving.

On the other hand, if the exchange rate is fixed, government support for the domestic currency will either decrease the amount of money in the country or increase the amount of money in other countries if it is not sterilised. This puts all of the adjustment pressure on the interest rate, which needs to rise domestically by enough to raise capital inflows and private net saving by the same amount as the increase in government dissaving. Capital inflows are improved when the foreign interest rate declines. By boosting imports and decreasing exports, higher domestic prices and lower foreign prices aid in the adjustment by increasing the amount of capital inflows that are needed. Reduced costs overseas may reduce net private saving overseas through the real balance effect on saving, while higher prices at home may also increase private net saving domestically. The adjustment process cannot function if the intervention used to fix the exchange rate is sterile. When the home country's excess demand for foreign exchange becomes chronic, intervention persists until the possibility of a drastic adjustment – typically a devaluation by the deficit country – is realised. At that point, a combination of higher interest rates and currency devaluation results in either the necessary reduction or net private dissaving (Dean et al., 2020; Makin, 1989).

2.3. Trade finance and macroeconomic growth

Prior to the 2008–2009 global financial crisis, politicians, scholars and economic analysts paid comparatively little attention to the function of trade finance in international trade. As a means of maintaining export and import capacity, trade finance did receive high priority in the coordinated restructurings during the debt crisis in the 1980s. Conversely, during the emerging market (EM) financial crises of the 1990s and early 2000s, trade finance was frequently treated with less involvement, which led to a steep decline in trade finance. The IMF came to the conclusion that these contractions made the economic effects of previous crises worse and that, should there be another crisis in the future, trade finance support measures should be explicitly taken into account as part of the broader stabilisation plan (IMF, 2003).

However, starting in 2008, anecdotal evidence indicated that the resulting decline in trade flows could be significantly influenced by disruptions in the supply of trade finance (Amiti & Weinstein, 2011), especially in the wake of the Lehman collapse. In fact, the G20 leaders called for coordinated public sector initiatives to increase the availability of trade finance after worries over a perceived lack of trade finance prompted business and the public sector to work together to better the statistics on trade finance markets. The World Bank Group and the regional development banks significantly increased their assistance to the industry as part

of this endeavour, mostly through guarantee programs. Additionally, the central banks of Brazil and Korea launched creative programs that directly targeted trade finance markets (BIS, 2014).

In fact, trade volumes shrank by a factor of four in the 12 months that ended in March 2009, which was far quicker than the global GDP in 2008–2009. Some have interpreted the significant relative decline in trade as proof that the so-called “Great Trade Collapse” was caused by factors other than a worldwide recession. However, one of the main challenges in assessing the impact of changes in trade finance on global trade flows is the lack of reliable data. Furthermore, the slow-down in trade that was seen in 2008–2009 and 2011 was caused by a number of other factors, including the price and demand for traded commodities; these factors may have had a much greater impact on trade flows than shifts in the availability of trade finance. Naturally, they may have played a role in any reported decline in trade finance to the degree that they decreased demand for trade finance (Baldwin, 2009).

Analysts from the public and private sectors have tackled these issues in a number of ways, such as by conducting surveys, extrapolating from case studies where more comprehensive firm-specific export and financial data are available, or estimating the impact of fluctuations in the availability and use of trade finance using proxy data. They have also made an effort to measure the degree to which the reported decline in international trade flows within a specific timeframe may have been explained by other causes. According to literature, the primary cause of the dramatic decline in global trade volumes in the quarters after Lehman’s bankruptcy was the decline in demand for consumer durables and capital goods worldwide, with trade finance disruptions playing a secondary but economically significant role. Similar findings were reached by the Group’s statistical investigations. Even a secondary contributory role, however, suggests an economically substantial impact on trade and economic activity given the size of the decline in trade volumes (BIS, 2014, 2016).

3. Methodology

A mixed-methods approach was employed as the research design for the study. To obtain a more thorough grasp of a research subject, mixed methodology combines the collection and analysis of both quantitative and qualitative data in a single study. In order to capitalise on the advantages of both quantitative and qualitative data, it integrates both to provide a more comprehensive picture than either approach could accomplish independently. The intentional integration of findings

during collection, analysis or reporting is a component of this method, which goes beyond merely collecting both kinds of data (Creswell & Plano Clark, 2023; Niglas, 2023; Plano Clark & Ivankova, 2016).

Documentary sources were used for data collection. Payne and Payne (2004) as well as Mogalakwe (2006) describe these sources as written documents in the private or public domain containing relevant information that can be utilised by researchers. Thus, data was derived from reports of international organisations such as the African Export-Import Bank (Afreximbank), African Development Bank (AfDB), Financial Sector Deepening (FSD) Africa, Bank of International Settlements, International Monetary Fund (IMF), World Trade Organization (WTO), International Trade Centre (ITC) and International Chamber of Commerce (ICC).

Data analysis was done using content analysis. Content analysis is a research technique that methodically examines and detects communication patterns. It entails categorising the data into easily understood categories, or “codes”, in order to quantify the occurrence of specific phrases, themes or concepts, allowing for conclusions about the message, its sources and context. The procedure is frequently systematic and replicable, incorporating qualitative and quantitative methods (Bailey, 2008; Bengtsson, 2016; Berg, 2001; Burnard, 1991, 1995).

4. Data presentation and analysis

4.1. State of fiscal policy indicators in Africa

Despite the challenges posed by the global economic slowdown, African growth has persevered. Due to supply chain difficulties and geopolitical tensions, global consumption was muted in 2024, which had a detrimental impact on African exports, particularly in primary commodities. Africa’s internal growth has been hindered by political instability in Sudan, terrorism in the Sahel and conflicts in the Democratic Republic of the Congo. Significant droughts in Somalia and the Sahel as well as cyclones in Comoros, Madagascar and Mozambique are examples of climate-related problems that have further hampered economic prospects (Afreximbank, 2025a). In spite of these obstacles, the continent’s growth has risen (although marginally) increasing from 3.3% in 2023 to 3.4% in 2024. While this growth rate is still below 2022 estimates, it is higher than pre-pandemic 2019 numbers, suggesting some recovery despite persistent challenges (Figure 1).

Although net exports have a negative impact on overall performance, strong household spending is what drives Africa’s resilience on the demand side. Resilient

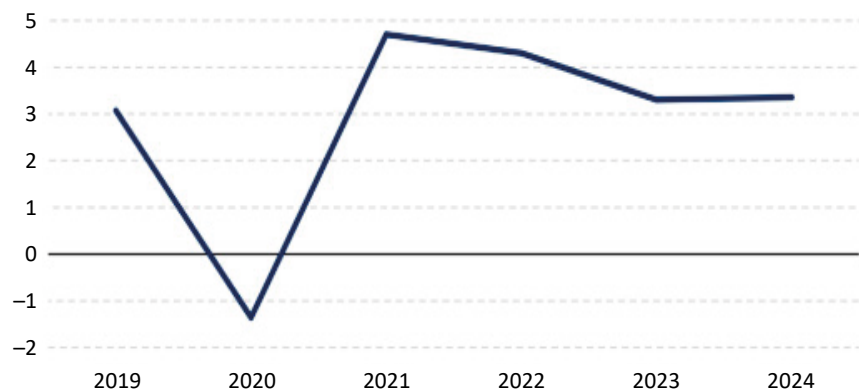


Figure 1. Africa’s real GDP growth, 2019–2024 (in %)

Source: (IMF, 2024; Afreximbank, 2025a).

household consumption increased its GDP growth contribution from 1.8 percentage points in 2023 to 2.7 percentage points in 2024. Investment contributions decreased from 2.0 percentage points to 1.8 percentage points. After declining by –0.1 percentage point in 2023, public spending increased by 0.2 percentage points. Nonetheless, net export stagnation remains a major obstacle, accounting for –0.8 percentage points of growth in 2024, up from –0.2 percentage points the year before (Figure 2).

The supply-side resilience of African economies was supported by a strong services sector. Between 2023 and 2024, the services sector made up about 2.3% of the total. On the other hand, the industrial sector saw a minor contraction, reduc-

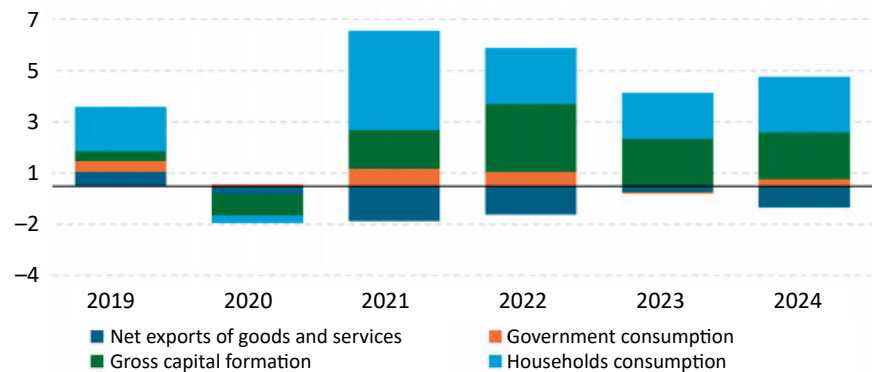


Figure 2. Demand-side decomposition of Africa’s GDP growth, 2019–2024 (in %)

Source: (World Bank, 2024; IMF, 2024; Afreximbank, 2025a).

ing its share of economic growth by 0.1 percentage point from 2023 to a revised 0.5 percentage point contribution. Although the agricultural sector still faces difficulties as a result of climate disruptions, its growth contribution has improved slightly, rising from 0.27 percentage points in 2023 to 0.33 percentage points in 2024 (Figure 3).

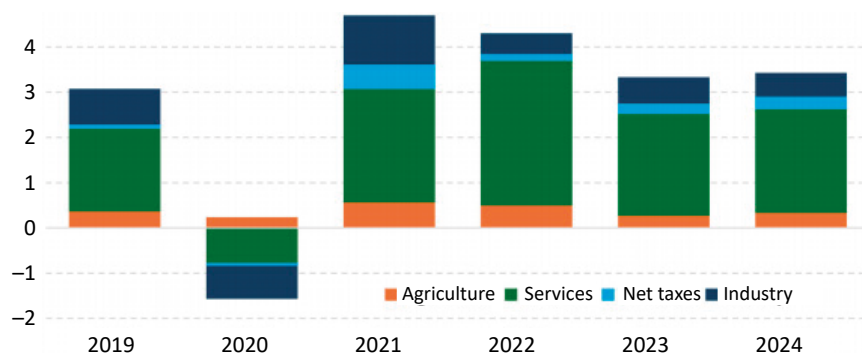


Figure 3. Sectoral decomposition of Africa's GDP growth, 2019–2024 (in %)

Source: (World Bank, 2024; IMF, 2024; Afreximbank, 2025a).

Although the current account deficit has been growing, it is still less than it was before the pandemic. It dropped to less than 2% of GDP between 2021 and 2023 as a result of increased commodity costs. But in 2024, it increased to 2.4% of GDP as import prices remained high and global commodity prices declined (Afreximbank, 2025a). African nations' dependence on imports, lack of export diversification as well as volatility in commodity prices are the main causes of the continent's structural imbalance.

Current account analysis demonstrates that fiscal deficits have a major impact on the evolution of the continent's net external position. While net private savings have stayed almost unchanged, Africa's current account deficit has increased in 2023 and 2024 as a result of a growing budget deficit. This increase implies that government expenditure raises domestic demand, which is met by imports rather than domestically produced goods and services, thus adding to budget deficits (Figure 4).

Furthermore, chronic budget deficits that have persisted for several decades are to blame for the rise in sovereign debt throughout Africa. This position is made worse by low national savings mobilisation and underdeveloped domestic financial markets, which lead to long-term account deficits. The average fiscal balance of the continent has continuously been in deficit during the last 20 years. The one exception, which occurred from 2005 to 2008, was brought on by an oil boom that greatly increased government revenue. The year 2006 saw the largest fiscal surplus, amounting to almost 4% of GDP. The worst public deficit-to-GDP

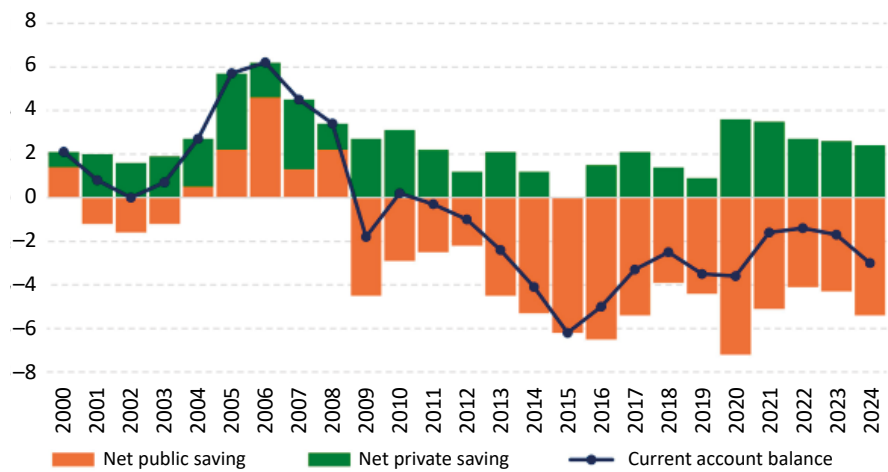


Figure 4. Current account decomposition, 2000–2024 (% of GDP)

Source: (IMF, 2024; Afreximbank, 2025a).

ratio, however, occurred in 2020 as a result of fiscal measures to the COVID-19 pandemic, rising to 5.37%. Over the past 20 years, the current account balance has continued to be negative. Given the increasing oil prices, the current account deficit was at its lowest in 2007 (0.19% of GDP). The current account deficit, on the other hand, peaked in 2015 at 7.27% of GDP during the decline in oil prices from 2014 to 2016 (Figure 5).

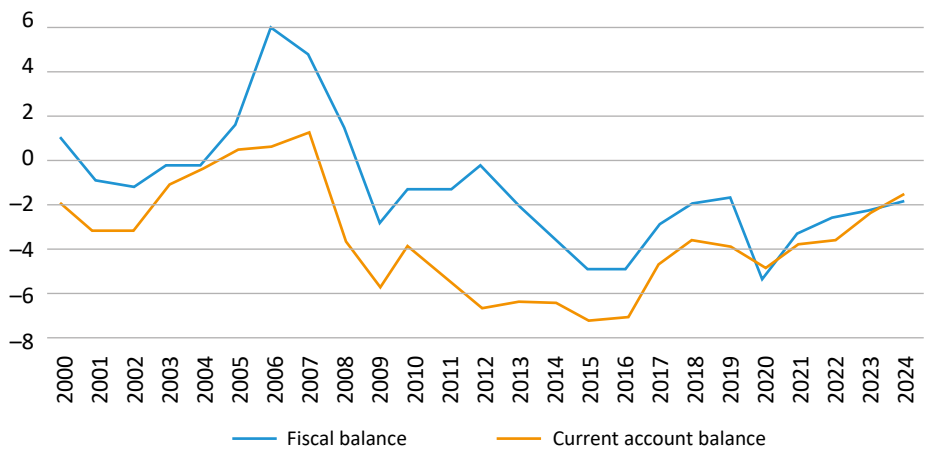


Figure 5. Fiscal balance and current account balance, 2000–2024 (% of GDP)

Note: Data are averages over African countries for each year.

Source: (IMF, 2024; Afreximbank, 2025a).

The twin deficit hypothesis – a positive causal relationship between the fiscal balance and the current account balance – is supported by empirical studies conducted in Africa between 2000 and 2023. The data indicates that the current account deteriorates by 0.27% of GDP in the year of the shock and by 0.28% in the subsequent year when there is an exogenous fiscal deficit equal to 1% of GDP (Afreximbank, 2025a). Short-term negative effects are not always associated with the twin deficits. The importation of investment goods required for public infrastructure projects is likely to worsen the external balance in the short term if these investments cause fiscal deficits in African nations. But over time, the productivity benefits brought about by these expenditures ought to boost growth rates and improve the current account balance.

4.2. Landscape of trade finance in Africa

An era of structural readjustment has begun in the global economy. Rising economic nationalism, supply chain disruptions and rapid digitalisation have all started to reshape trade and investment since the global financial crisis of 2008. According to a Deutsche Bank (DB) study (cited in Afreximbank, 2025b), semiconductor chips already made up around 15% of the value of global goods trade in 2020, while crude oil, the barometer of merchandise commerce, has been surpassed by semiconductors. Since the 2008 financial crisis, services have grown from 20 to 25% of global trade, with their true size still being underrepresented in official figures. This growth has been fuelled by the growing usage of digital platforms as necessary to enable remote personal, corporate and professional transactions. Additionally, the geography of trade has changed. As shown in Table 1, Europe, North America as well as East and Southeast Asia collectively accounted for 75% of global exports in 2023, demonstrating that these three regions – dubbed “global factories” (Baldwin & Lopez-Gonzalez, 2015) – continue to have a dominant position.

Due to a global financial and trade environment that is experiencing significant change, Africa finds itself at a critical juncture in its economic development. Global value chains have been more frequently disrupted in the last ten years, international trade governance has been more fragmented, and the trend toward digital and green finance has accelerated. With major ramifications for Africa’s capacity to obtain finance, expand its economies and engage in competitive international trade, these developments are rewriting the norms of investment and commerce.

The round-tripping model, which has caused massive foreign exchange reserve leaks and ongoing balance of payments pressures, has continued even as Africa’s trade direction has shifted eastward (Asia), demonstrating the stickiness of the colonial development model of resource extraction, where African countries sys-

Table 1. Share of regions in global exports

Regions	Services		Goods		Goods and Services	
	2009	2023	2009	2023	2009	2023
Africa	2.2	1.8	3.5	3.2	2.9	2.3
European Union	38.4	38.2	33.9	30.4	34.9	32.3
United Kingdom	8.0	7.4	2.8	2.2	4.0	3.5
Total Europe	46.3	45.6	36.7	32.5	38.9	35.8
China	4.0	4.9	9.5	14.2	8.3	11.9
Hong Kong	1.8	1.2	2.6	2.4	2.4	2.1
South Korea	2.0	1.6	2.9	2.7	2.7	2.4
Taiwan	0.6	0.7	1.6	1.8	1.4	1.5
Japan	3.3	2.6	4.6	3.0	4.3	2.9
ASEAN nations	4.9	6.8	6.5	7.6	6.1	7.4
Total East and Southeast Asia	16.4	17.8	27.8	31.7	25.2	28.3
India	2.6	4.3	1.3	1.8	1.6	2.4
United Arab Emirates	0.3	2.1	1.5	2.0	1.2	2.1
Qatar	0.1	0.4	0.4	0.4	0.3	0.4
Total Other Asia	2.9	6.8	3.2	4.3	3.1	4.9
United States	13.9	12.7	8.4	8.5	9.6	9.5
Mexico	0.6	0.7	1.8	2.5	1.5	2.0
Canada	1.9	1.7	0.5	0.6	0.8	0.9
Total North America	16.4	15.1	10.8	11.5	12.0	12.4
Total (trillion)	3,603	7,822	12,585	23,813	16,188	31,635

Source: (Afreximbank, 2025b).

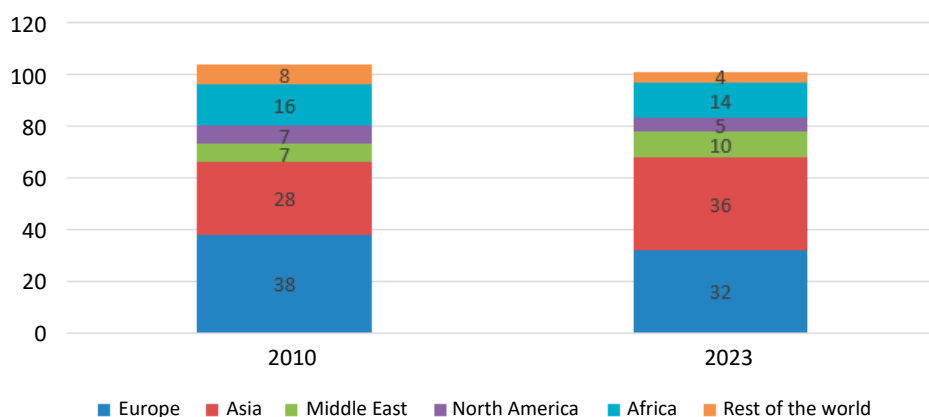


Figure 6. African origin of imports, 2010 and 2023 (in USD billion)

Source: (Afreximbank, 2025b).

tematically exported raw materials and natural resources to European powers and imported value-added manufactured goods at higher prices (Figure 6). The most recent projections indicate that hydrocarbons account for the majority of Africa's trade, with refined petroleum and allied products accounting for the largest share of the continent's overall imports (ITC, 2023).

Beyond the massive leaks of foreign exchange reserves, the colonial growth model exposes nations to frequent negative commodity terms of trade shocks, which are substantially to blame for the high frequency of balance of payments crises and the unstoppable increase in external obligations. Additionally, in a world of global value chains, where manufactured and intermediate commodities with rising technology content dominate trade, African trade has steadily declined in comparison (Fofack, 2024; Luke, 2023; Wellisz, 2022). Although its proportion of the world's population has continuously climbed to 17%, the region today makes up less than 3% of global trade, down from roughly 5% in the years following independence (Figure 7). Additionally, intra-regional trade has remained a paltry 15% of overall African trade, compared to 60% in Asia and 70% in Europe, causing the distribution of African trade to be biased towards extra-African trade (Figure 8).

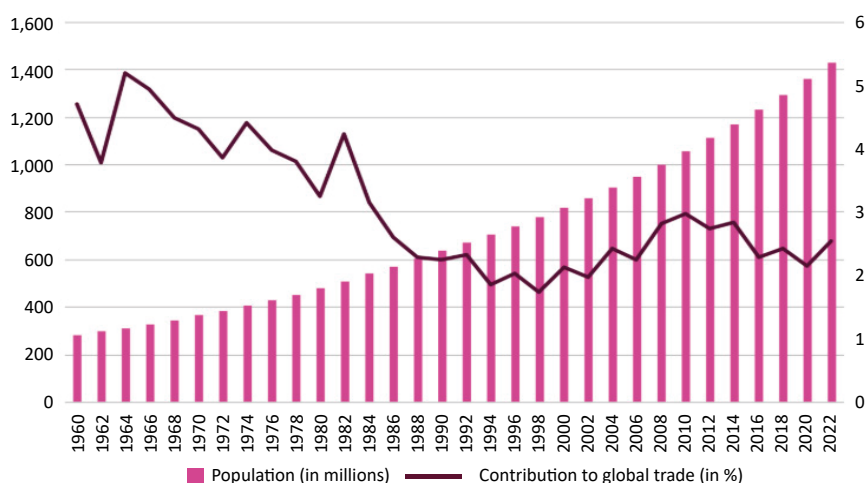


Figure 7. Africa's population (left axis) and contribution to global trade (right axis), 1960–2022

Source: (UNDESA, 2022; UNCTAD, 2023; Fofack, 2024).

Due to protectionist policies, geopolitical tensions and unfavourable commodity terms of trade shocks, Africa's share of global exports has decreased from 3.5% in 2009 to 3.2% in 2023, highlighting its marginal position in global value chains. Africa's involvement in high-value industries is restricted by the disruption of supply chains caused by the competition between the US and China for semiconduc-

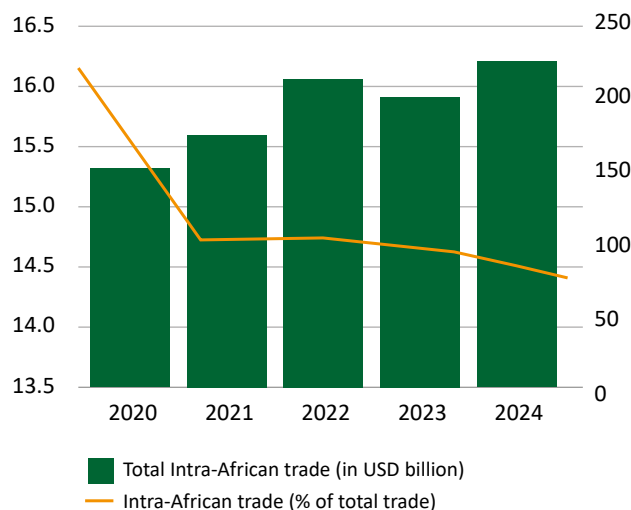


Figure 8. Total African trade (right axis) versus total intra-African trade (left axis), 2020–2024

Source: (IMF, 2025; Afreximbank, 2025b).

tors and vital minerals. African exports are under potential threat due to global protectionism, which includes US tariffs and the European Union’s Carbon Border Adjustment Mechanism. Global attention is drawn to Africa’s abundant reserves of vital minerals like cobalt and lithium, but collaborations run the risk of sustaining exploitative paradigms with little local value addition (Afreximbank, 2025b). To improve resilience and lessen dependency on unstable international markets, it is crucial to invest in infrastructure and digital finance as well as to strengthen African-led value chains through the creation of the African Continental Free Trade Area (AfCFTA).

The AfCFTA has the potential to drastically alter the continent’s trade and economic environment. It creates one of the world’s largest free trade areas, with 1.4 billion people and a combined GDP of USD 3.4 trillion (Fofack, 2021; 2024; Signé, 2023). It has been hailed as a game-changer because it has the potential to boost investment flows, which would then shift their composition and direction from natural resources to labour-intensive manufacturing as businesses benefit from economies of scale, competitiveness and productivity gains brought about by the sharp decline in the risk of investing in smaller markets. The AfCFTA is predicted by the World Bank to increase Africa’s exports to the rest of the world by 32% by 2035 and stimulate foreign direct investment, which is projected to rise by 111% to 159% (World Bank, 2020). Leveraging its enormous potential to go beyond the resource-extraction-based colonial development model will help to speed up the

diversification of growth and export sources, launching the region into a positive feedback loop of strong economic growth and a wider tax base that will fortify Africa's fiscal and debt sustainability foundation.

4.3. Trade finance gap in Africa

Africa has an annual trade finance gap of approximately \$100 billion. As 80 to 90% of businesses on the continent are small and medium-sized, this significantly restricts their capacity to participate in regional trade. Due to a predisposition towards external markets, just 18% of African banks' trade finance portfolios facilitate intra-African commerce. Small and medium-sized businesses are unable to expand their operations and incorporate themselves into local value chains due to this deficiency, which is made worse by high borrowing rates and tight international banking regulations like Basel IV. Closing this gap is critical to the success of the AfCFTA, which was intended to increase intra-African trade. To fully realise the potential of the continental accord, measures like Pan-African Payment and Settlement System (PAPSS) as well as Afreximbank's \$17.5 billion trade finance disbursements are important first steps, but expanding access to reasonably priced credit and harmonising financial laws are also top goals (Afreximbank, 2025b).

Trade finance accounts for over 80% of global trade, however the distribution is not uniform. One of the top three export hurdles cited by businesses in low-income regions is the inability to obtain finance. A report from the African Development Bank and Africa Import-Export Bank used exclusive data from over 600 banks across 49 African countries between 2011 and 2019 to illustrate this constraint. The report titled "Trade finance in Africa: Trends over the past decade and opportunities ahead" provides an overview of the trade finance gap in Africa during the last ten years, along with the variables that have influenced its development (AfDB-Afreximbank, 2020).

The trade finance gap shrank gradually but consistently from an estimated US\$120 billion in 2011 to US\$70 billion in 2016. However, in 2016, the downward trend in unmet demand was reversed, and since then, there have been some little variations. The predicted trade finance gap for 2018–2019 was still large compared to what the region's proportion of global trade would indicate, even though it was less than the nine-year average of US\$91 billion. A conservative estimate of the unmet demand for trade credit in 2019 was around US\$82 billion (Figure 9). Unmet trade financing demand in Africa accounted for over 8% of the region's total trade value and 5.5% of the global trade finance gap in 2019, with the continent's merchandise trade and global trade finance gap estimated at US\$1 trillion and US\$1.5 trillion, respectively. Africa's contribution of the global trade finance

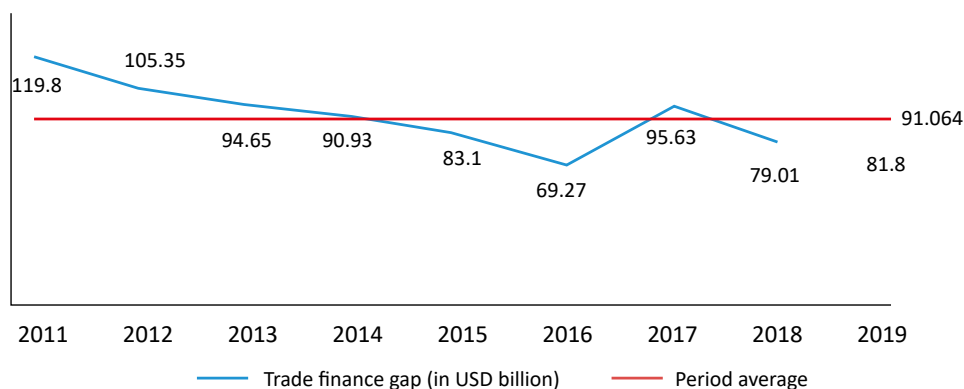


Figure 9. Trade finance gap in Africa, 2011–2019

Source: (Nyantakyi et al., 2021).

gap is disproportionately bigger than the region's share of worldwide trade, despite the fact that 5.5% may seem low at first (Nyantakyi et al., 2021). This is because Africa's trade only makes up 3% of global trade.

An examination of the global policy framework that has influenced the trade finance environment in Africa and beyond since the global financial crisis is necessary to comprehend the development of the trade finance gap in the region. It is possible that the global policy reaction to the Great Trade Collapse contributed to the reduction of the trade finance gap in Africa between 2011 and 2016. First, the gradual but consistent decline in the trade finance gap from 2011 to 2016 was a result of increased awareness of unmet demand after the 2008 global financial crisis. The global financial crisis of 2008–2009 saw a sharp and coordinated decline in global trade. Evidence suggests that trade credit issues were the second most important factor in the Great Trade Collapse, behind the decline in demand. However, whereas North America and Europe recovered swiftly, Africa and, to a lesser extent, Eastern Europe continued to face credit difficulties. In fact, in mid-2009, the only continent still facing dwindling trade finance supplies was Africa.

A prompt and comprehensive policy response was implemented to support trade credit for developing economies. Over US\$80 billion was made available to assist international trade through the establishment of US\$9 billion in trade finance facilities by major multilateral development banks (MDBs). In order to ensure that trade transactions between Western firms and their African counterparts had the financial resources required to make trade contracts viable, large commercial banks like Sumitomo Mitsui Banking Corporation (SMBC) of Japan also implemented measures to help close the gap by using “follow your firm” strategies, in which foreign banks followed their domestic firms (Mora & Powers, 2009; Nyantakyi et al., 2021). The International Finance Corporation, African Development Bank and

Asian Development Bank all have trade finance support facility programs that continue to this day, demonstrating that MDB interventions have continued long after the global trade collapse. These initiatives, which have supported the region's trade finance supply, have primarily benefited African banks.

Between 2011 and 2016, the drop in commodity prices contributed to an exogenous downturn in the demand for trade finance. African trade fell by an average of 6% a year between 2012 and 2016, and the trade finance gap shrank by almost 10% throughout that time. In fact, due primarily to the drop in commodity prices that started in mid-2015, the entire value of African trade in 2016 was at its lowest point, at almost US\$848 billion. Not unexpectedly, the trade finance gap was at its lowest that year, at US\$69.3 billion (Figure 9). The decline in African trade value led to an exogenous reduction in the continent's total demand for trade finance, hence narrowing the imbalance between supply and demand.

Nonetheless, the trade finance gap may have increased recently due to shifts in the regulatory environment. In 2017, the downward trend in the global trade finance gap reversed. This reversal was certainly not unique to Africa; rather, it was symptomatic of the worsening global trade finance environment. According to recent data released by BNY Mellon and ADB, trade finance rejection rates are rising globally, which explains the gap. Three out of four banks cite KYC and compliance issues as the main reasons for rejection (BNY Mellon, 2019). The trade finance gap naturally widens with a larger rejection rate. In this case, the 2016 increase in the gap can be a result of the shifting global banking regulatory landscape. Banks are avoiding the trade finance industry, and international correspondent banks that are vital to African trade are pulling out of the continent as African nations embrace the new Basel III banking regulations that have gone into effect, particularly the way that Basel III treats trade finance as a riskier asset class (Table 2 and Figure 10).

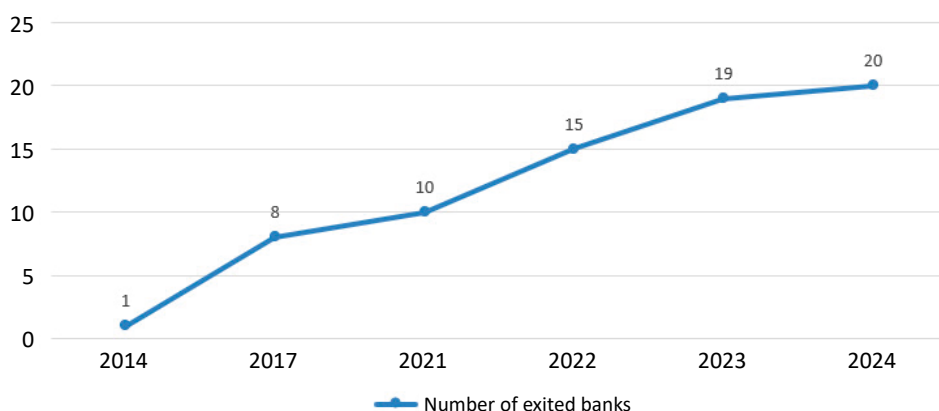


Figure 10. The exit of international banks from Africa, 2014–2024

Source: (Afreximbank, 2025c).

Table 2. Cumulative increase in the number African countries affected by international bank withdrawal announcements

Year	Banks	Newly affected African countries	Cumulative total (African countries)
2014	Citi Bank	Egypt	Egypt
2017	Barclays Plc	Botswana, Ghana, Kenya, Mauritius, Seychelles, Tanzania, Zambia	Egypt, Botswana, Ghana, Kenya, Mauritius, Seychelles, Tanzania, Zambia
2021	Atlas Mara	Mozambique, Rwanda, Tanzania, Botswana, Zambia	Egypt, Botswana, Ghana, Kenya, Mauritius, Seychelles, Tanzania, Zambia, Mozambique, Rwanda
2022	Credit Suisse & Standard Chartered	Angola, Cameroon, Gambia, Sierra Leone, Zimbabwe	Egypt, Botswana, Ghana, Kenya, Mauritius, Seychelles, Tanzania, Zambia, Mozambique, Rwanda, Angola, Cameroon, Gambia, Sierra Leone, Zimbabwe
2023	Societe Generale	Congo, Equatorial Guinea, Mauritania, Chad	Egypt, Botswana, Ghana, Kenya, Mauritius, Seychelles, Tanzania, Zambia, Mozambique, Rwanda, Angola, Cameroon, Gambia, Sierra Leone, Zimbabwe, Congo, Equatorial Guinea, Mauritania, Chad
2024	HSBC & BNP Paribas	South Africa	Egypt, Botswana, Ghana, Kenya, Mauritius, Seychelles, Tanzania, Zambia, Mozambique, Rwanda, Angola, Cameroon, Gambia, Sierra Leone, Zimbabwe, Congo, Equatorial Guinea, Mauritania, Chad, South Africa

Source: (Afreximbank, 2025c).

The number of banks involved in trade finance activities has decreased in Africa as a result of stricter Basel III capital requirements on trade finance assets and new anti-money-laundering/know-your-client (AML/KYC) compliance measures that have led to lower margins and higher due diligence costs. Table 2 and Figure 10 show that the percentage of African banks that provided trade finance dropped from 92% in 2014 to 71% in 2019 – a 21% drop – and then continued to decline in 2024. Higher costs and lower margins have reduced the profitability of minor transactions for banks that have stayed in the trade finance industry, particularly for small banks with higher average expenses. As a result, the supply of trade finance has decreased and rejection rates have increased, especially for SMEs.

It was once believed that SMEs' weak creditworthiness was the cause of their higher-than-normal trade finance rejection rate. However, a peculiar aspect of recent SME trade finance activity is that, although the risk profile for SME trade finance in Africa has improved, with the default rate dropping from 14% in 2014 to 10% in 2019, the rejection rate for SME trade finance applications has increased from 21% to 40% during the same period, indicating that there is more to the

SME trade finance rejection rate than just low creditworthiness. Correspondent banking connections are also affected by regulatory challenges. Due to increasingly strict AML/KYC rules and capital requirements, banks that provide the liquidity and risk-mitigation facilities that support international trade are steadily reducing their operations from riskier areas, especially in Africa, as part of a process known as “de-risking”. In 2016, Barclays PLC’s withdrawal from the area was widely reported. In fact, according to Afreximbank (2025c) and Nyantakyi et al. (2021), 20% of African issuing banks see correspondent banking ties as the main barrier to the supply of trade finance.

It is still challenging to forecast how the trade finance gap would develop in the future given the current uncertainty brought up by COVID-19. However, there are concerns that the epidemic would undo some of the gains, if not all of them, and push the trade finance gap above its typical long-term average of US\$91 billion. (Note: The trade finance gap in Africa was estimated at US\$80–US\$120 billion between 2021–2024) (Afreximbank, 2025a, 2025b, 2025c). Banks are hesitant to lend to African businesses as their balance sheets deteriorate as a result of COVID-19-related issues. Even in cases where banks are able to provide trade finance to businesses, the steps implemented to address the pandemic might occasionally make it challenging to conduct these transactions quickly (Afreximbank, 2021, 2025c). Consequently, it is imperative that policymakers keep pooling resources to guarantee that the trade finance imbalance does not rise, at the very least.

4.4. Building a sustainable trade finance ecosystem via robust fiscal policy

A complex network of structural barriers affects African economies, such as regulatory dissonance, currency rate volatility, macroeconomic instability and a persistent trade finance gap that is estimated to be over US\$100 billion yearly. Sovereign debt vulnerabilities, infrastructure deficiencies and systemic biases ingrained in international financial systems – such as biased credit rating practices, restricted access to concessional finance and underrepresentation in international decision-making bodies – complement these limitations (Afreximbank, 2025b). These difficulties do not require retreat. They call for coordination, leadership and fiscal reform.

The World Bank Group claims that liberal trade policies have helped more than a billion people in various nations escape poverty. Although there could have been more, the trade finance gap has consistently slowed down the productivity of international trade. This is especially true for African nations and companies. The difference between unmet and satisfied demand for trade funding is known as

the “trade finance gap”. Working capital is necessary for trade, whether it takes the form of products or services. The trade finance gap is caused by this capital’s unavailability to all types of firms. The trade finance gap is estimated to be \$2.5 trillion worldwide, with Africa accounting for about \$120 billion of that total (De Rose, 2025; Mwaba et al., 2025).

Professionals and trade specialists have discussed how to bridge the trade finance gap during the past ten years. Trade finance gaps can be addressed by fiscal policy, which is the use of taxes and spending by the government to control the economy. Government expenditures that directly lower risk for private lenders and tax laws that increase trading companies’ cash flow and profitability, as well as increase their creditworthiness, are the main ways it might accomplish this. Fiscal policy can also resolve trade finance constraints through macroeconomic stability and financial sector development (AfBC, 2025; De Rose, 2025; Ntoya, 2025).

1. Direct government spending and risk-sharing: By providing liquidity, reducing risks that the private sector is unable or unwilling to take on, as well as fostering a stable climate for private lending and investment in trade-related industries, direct government expenditure and risk-sharing can improve trade finance. Programs that crowd in private sector funding and absorb high-risk parts of trade transactions can also be funded by governments. These can be accomplished by:
 - A. Export Credit Agencies (ECAs) Funding: Increasing the financial capacity and mission of government-backed ECAs is the most straightforward strategy. ECAs make guarantees using public cash, supplying commercial banks with sovereign guarantees to mitigate the risk of trade loan or credit letter default. This encourages banks to offer trade finance by drastically reducing their risk weight. In addition to providing guarantees, ECAs also employ government funds to offer direct lending and reinsurance, acting as a direct lender or reinsurer for high-value or high-risk transactions that the private sector avoids.
 - B. Establishing and funding trade finance facilitation initiatives: Governments can put money into the trade finance initiatives of regional banks and multilateral development banks (MDBs). Banks in underdeveloped nations receive guarantees from this money, enabling them to validate letters of credit and gain access to the international trade network.
 - C. Investing in regulatory and digital infrastructure: Expenditure on modernising customs procedures, creating a Single Window for trade, and digitising trade documents (such as electronic bills of lading) all cut down on trade time and operational risk, which in turn lowers costs and expands access to finance (AfDB, 2017; Auboin & Meier-Ewert, 2003).

2. Targeted tax incentives: Tax policy can be modified to instantly boost the financial stability and liquidity of businesses that import and export.
 - A. Accelerated Value Added Tax (VAT) reimbursements: A lot of exporters are experiencing cash flow problems while they wait for their inputs' VAT refunds. The exporter's working capital and overall liquidity can be enhanced by a fiscal policy that prioritises the quick processing and payment of VAT refunds, which lessens the need for expensive bank financing right away.
 - B. Tax credits/deductions for trade costs: Allowing for immediate tax deductions for export-related spending or providing tax incentives, such as specific tax credits for R&D or investment in export-related capacity, improves a company's internal cash flow and long-term competitiveness.
 - C. Reducing financial transaction taxes: Businesses' total cost of financing can be directly decreased by lowering or doing away with taxes on particular cross-border financial transactions or trade finance instruments (Owens & Zhan, 2018; Redonda et al., 2020).
3. Macroeconomic stability and financial sector development: Good fiscal management reduces the general impression of risk that fuels the gap by fostering a stable environment in which private finance can flourish.
 - A. Fiscal prudence to stabilise the exchange rate: The danger of inflation and currency instability is decreased by limiting the budget deficit and avoiding excessive public debt. For trade finance, a stable exchange rate is essential because it reduces currency risk, which lowers transaction costs and makes pricing simpler for banks.
 - B. Supporting funding for financial literacy and capacity building: Government investments in initiatives to enhance the financial reporting and governance of SMEs – the group most impacted by the gap – make them appear to commercial banks to be less risky and more transparent borrowers.
 - C. Regulatory alignment (via fiscal budget): Allocating funds to ensure that domestic financial regulations are in line with international standards (such as Basel III) while also providing favourable treatment for short-term trade finance assets can help prevent banks from facing fiscal penalties from their own regulatory body for extending trade credit.
 - D. Public investment in infrastructure: Government expenditure on trade-critical infrastructure, such as ports, new customs procedures and digital trading platforms, reduces the time and non-financial expenses related to trade. This increases the efficiency of the supply chain as a whole, which speeds up and lowers the risk of trade transactions and incentivises banks to offer better conditions for finance (OECD, 2021).

Conclusions

The shifting global and regional financial landscape has the potential to change African trade. Global financial turbulence, trade disputes and evolving patterns of foreign direct investment all pose significant difficulties that could stifle development and create vulnerabilities. However, with fiscal policy reforms that prioritise expedited regional financial integration, combined with transformative initiatives and increased infrastructure expenditures, Africa can create new opportunities for intra-African trade and value chain development. By prioritising fiscal policy reforms and coordinated investments, African countries can drive long-term industrialisation, diversify their economies and eventually boost their competitiveness in an increasingly interconnected global market. This multilayered reorganisation, however complex, provides hope for African states to not only stabilise their trade networks, but also to emerge as an increasingly significant actor in the global economy.

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