DETAILS OF IMPLEMENTATION ARRANGEMENTS

1. **General**. Exposure of the Asian Development Bank (ADB) under the Trade Finance Program (TFP) will not exceed $2,150,000,000 at any point in time.[1] Guarantees, loans, and unfunded and funded participation and risk distribution arrangements will continue to be provided on a rolling basis.[2] To monitor this exposure, the program provides monthly exposure reports to the Office of Risk Management (ORM).

2. **Products and Risk Coverage.** The TFP will continue to offer the following transaction products covering trade and related services.[3]

(i) **Unfunded products**.

(a) **Credit guarantee**. The credit guarantee in the form of a standby letter of credit is the program's most commonly used product. It covers up to 100% of the risk of non-payment of a trade obligation issued by a developing member country (DMC) bank. During 2018−2020, 63% of the total value of transactions supported by the program was generated through the credit guarantee product.

(b) **Risk participation.** ADB, under risk participation agreements (RPAs), shares risk (up to 85%) with partner financial institutions (PFIs) that have regular flows of transactions into DMCs on a portfolio basis. PFIs like this product because it is efficient and requires little administration. During 2018–2020, the product has constituted 31% of the program's portfolio.

(ii) **Funded products.**

(a) **Revolving credit facility**. ADB provides revolving credit facility (RCF) loans directly to partner DMC banks to support pre- and post-shipment trade transactions. During 2018−2020, the product represented about 3% of the total transaction value supported by the program.

(b) **Funded risk participation.** Launched in 2017 on a pilot basis until 31 December 2021, ADB risk participates on a funded basis in up to 50% of the risk of funded trade transactions. Through funded risk participation agreements (FRPA) with PFIs, the product helps mobilize more private sector funds to support trade in DMCs and, during 2018–2020, constituted about 3% of the program's portfolio.

(iii) **Cofinancing.** The program developed an aggressive cofinancing strategy in 2010 through a risk distribution agreement (RDA). Use of the RDA has grown with the size of the program. Distribution, also known as risk transfer, was used only when internal risk bearing capacity was at its limit. Cofinance is important to the program because it leverages capital resources and credit limits by mobilizing private sector resources. This enables the TFP to support at any one time more than double the amount of trade than would otherwise be possible under its program limit, and it is therefore important to closing market gaps. The RDA enables the program to

[1] The program's exposure limit is net of amounts of risk distributed, and/or syndicated to non-developing member country counterparties.

[2] In the context of the TFP, a "guarantee" is a reference to a standby letter of credit issued by ADB under the TFP Credit Guarantee product. A standby letter of credit is not a guarantee as a matter of law but is referred to as such by the TFP for ease of understanding and marketing purposes.

[3] As with the trade finance programs of the European Bank for Reconstruction and Development and the International Finance Corporation, the TFP may support trade in services including in the form of bid, performance and advance payment guarantees.

distribute risk—mostly to private insurance—efficiently, enabling the program to transfer 50%–90% of ADB's exposure.

3. **Trade finance knowledge products and partnerships.** The program will continue to create knowledge products, services, and solutions. These initiatives will be focused on (i) gender equality; (ii) sustainability; (iii) capacity building and training; (iv) digitalization of trade; and (v) transparency, anti-money laundering (AML) and combatting the financing of terrorism (CFT). Partnerships with industry associations and non-governmental institutions will continue to be critical to implementing the program's knowledge initiatives.[4]

4. **Tenor.** The maximum tenor of guarantees, loans, and unfunded and funded risk participations covered by the program will remain at 3 years. While substantial trade finance market gaps exist for tenors of less than 1 year, even fewer financial institutions are able to support trade carrying longer tenors. Supporting transactions classified as Category B for environment under ADB's Safeguard Policy Statement (2009) will result in more transactions for capital equipment with longer tenors. Notwithstanding the maximum possible tenor, it is anticipated that the average tenor for the program will continue to be less than 180 days.

5. **Currencies**. The TFP offers unfunded and funded products in a number of currencies, in each case following required conditions of ADB's Treasury Department, Office of the General Counsel, Controller's Department (CTL) and Office of Risk Management (ORM).

6. **Domestic trade.** The TFP's RCF is eligible for domestic trade transactions during emergencies declared by national governments or officially recognized international bodies, such as the World Health Organization. Parameters of specific emergency facilities will be defined and approved by the ORM on case-by-case basis.

7. **Category A and B transactions.** Program support for transactions involving goods in projects classified as Category B for environment and involuntary resettlement under ADB's Safeguard Policy Statement will only be available for partner banks that have ADB-endorsed environmental and social management systems (ESMSs) and demonstrated capacity to implement these. TFP support can also be used for transactions classified Category A for environment or involuntary resettlement and A or B for indigenous peoples impacts if the transactions support goods and equipment for ADB financed projects, and for which ADB compliance is confirmed.[5]

8. **Pricing**. Program pricing is based on market rates. By applying market pricing, the program demonstrates to private sector financial institutions that it is possible to operate in challenging markets, assume reasonable risks, and earn adequate compensation. The program conducts monthly pricing surveys to ensure it is within market. In addition, the program holds monthly calls with the International Finance Corporation for coordination purposes, including on pricing alignment. Market-based pricing also helps ensure that international banks have natural incentives to use lower percentages of ADB risk cover. As pricing fluctuates significantly with changing market conditions, it is important that the program has maximum flexibility to quickly decide on pricing in line with the market. This is especially important given the short period of time within which the program must respond to clients.

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[4] The TFP's knowledge products and partners are further addressed in Program Results, Business Strategy and Plan (accessible from linked document 7 in Appendix 2).

[5] The TFP's safeguards and social requirements implementation are further developed in Environmental and Social Management System Arrangements (accessible from linked document 5 in Appendix 2).

9. **Onboarding of developing member country banks.** The program will conduct due diligence, financial analysis, and integrity due diligence (IDD), and (where appropriate) will propose limits. DMC bank limit approvals are delegated to the Head of ORM, with limits subject to annual review.[6]

10. **Single obligor or developing member country bank limit.** After ORM has endorsed an obligor limit on the amount and tenor for a particular DMC bank risk, the program can apply those limits to whichever unfunded product—credit guarantee or RPA—is most in demand without seeking further approvals. With respect to the program's funded products—the RCF and FRPA—the program will have to secure a specific limit from ORM. While the program can take from funded limits to support either RPAs or credit guarantees without ORM approval, the reverse is not true.

11. **Program guarantees will provide cover up to 100% of transactions**.[7] There are strong developmental and business reasons for the program to provide this much risk cover. Financial institutions cannot assume country risk and/or bank risk in some DMCs. By availing of 100% guarantees, international banks can develop credit histories, business contacts, and knowledge of DMCs. The program thus builds partnerships between international and DMC banks even in the most challenging markets.

12. **Collective exposure limit.** Program limits for DMC banks that are owned by the same group will generally not exceed 25% of the aggregate equity of all DMC banks in the program that belong to the same group.

13. **Accreditation of partner financial institutions.** Onboarding of PFIs will be approved by the Investment Committee. Risk participation products—RPA and FRPA—are offered to international banks that have a significant presence in DMCs where the program operates. As such, it is likely that PFIs for an RPA will be the same banks to be offered the FRPA.

14. **Information technology.** The program is in the process of acquiring new information technology (IT) systems to help manage its business. Operational risk is heightened due to weakness in the program's IT system, which is incapable of supporting a business of this scale and size. ADB's Office of the Auditor General audited the program in 2020.[8] While the audit recommended improvement in controls and efficiency within Trade Finance Program Management System, it also states that the Trade Finance Unit has adequate manual controls in place to compensate the system's shortcomings.[9]

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[6] In line with ADB. 2016. Nonsovereign Operations. *Operations Manual*. OM D10. Manila.

[7] The program's provision of 100% guarantees is in line with what the International Finance Corporation, the European Bank for Reconstruction and Development, the Inter-American Development Bank, and commercial banks provide in trade finance products.

[8] ADB. 2020. Audit of Trade Finance Program and Supply Chain Finance Program. Audit Report Number: 20-007. Manila.

[9] The TFP operating guidelines serves as a manual setting forth the program's operating processes. It is updated every 18−24 months, with the last update in July 2020 to include process improvement initiatives and new procedures following integration with Controller's Department's system and SWIFT, and the coronavirus disease response, among others. ADB. 2020.*Trade Finance Program Operating Guidelines*. Manila.

16. **Integrity due diligence**. The TFP undertakes an array of transactions through its on-boarded issuing banks, confirming banks, and PFIs.[10] Issuing banks, confirming banks, and PFIs are commercial banks that comply with the Board-approved eligibility criteria; onboarding involves a rigorous approval process that comprises financial due diligence and IDD. The TFP's IDD process fully complies with the 2015 Integrity Due Diligence Guidelines for Nonsovereign Operations (IDD Guidelines).[11] The process is in line with the relevant staff instruction.[12]

17. The program has implemented end-to-end sanctions screening of all proposed deals, committed transactions, and all outgoing trade-related financial messages that run on the SWIFT platform. For proposed deals, around 80 to 100 names are screened daily (including names of banks, exporters and/or importers, ports, vessels, and insurance companies) to help determine if each proposed transaction is eligible for ADB support. Over 13,000 names (from past and current transactions) are run on an ongoing basis on SWIFT batch screening and over 250 hits are investigated daily on SWIFT sanctions screening (i.e., automated transactions screening) to confirm that they are false positives. To ensure adequate and timely support to the trade finance business, the program has three dedicated team members to support its sanctions screening and IDD work.

18. The TFP follows the IDD process outlined below, categorized basis the type of counterparty engagement (or type of financial product) in compliance with the ADB's Program Integrity Due Diligence Guidelines for Nonsovereign Operations (footnote 11) and the IDD Requirement Per Product Matrix for Special Programs.[13]

(i) **Issuing banks**. The TFP conducts a full IDD review for its new and existing issuing banks, which includes completing the TFP AML and IDD checklists.[14] The IDD review is also inclusive of the client due diligence questionnaire that encompasses a comprehensive review of all possible risk areas related to the issuing bank and the ADB facility.[15].

(ii) **Confirming Banks.** The majority of the confirming banks in the program are rated BBB+ or higher by any of the three major international credit rating agencies. For rated confirming banks, only sanctions screening is required. For not rated confirming banks, TFP undertakes a desk review that includes identifying the shareholding structure, and conducting desktop research on integrity, AML/CFT, and sanction compliance issues of the bank and its key shareholders. The sanctions check and desk review report are submitted to AIPD for further review and assessment. This process is repeated annually as part of IDD monitoring.[16]

(iii) **Partner financial institutions.** The level of IDD review depends on whether the transaction supported with these counterparties are funded or not. For FRPA counterparties, an IDD checklist review is completed similar to the process for

[10] For purposes of this document, the term "issuing bank" shall refer to partner DMC banks that are Issuing Banks under CG arrangement, and Borrowers under revolving credit facility. Confirming Banks, often international banks, are banks to which TFP provides its guarantees—in the form of a standby letter of credit—against the risk of non-payment from DMC Issuing banks.

[11] ADB. 2015. *Integrity Due Diligence Guidelines for Nonsovereign Operations* (internal).

[12] ADB. 2019. *Nonsovereign* Operations. *Operations Manual.* OM D10. Manila (internal).

[13] ADB. Matrix of Products for purpose of Integrity Due Diligence Requirements (internal).

[14] ADB. *Trade Finance Program AML and IDD Checklist* (internal).

[15] ADB. *TFP Due Diligence Questionnaire for banks* (internal).

[16] Data related to the IDD review processing dates and status are encoded on TFPMS Compliance tab and used as part of daily transaction eligibility criteria—i.e., only transactions with partner banks and financial institutions that have "valid IDD" data may be processed.

issuing banks. For RPA counterparties, a desk review is completed similar to the process described for "Not Rated" confirming banks.

(iv) **Risk distribution partners**. Only sanctions screening is completed, because all risk distribution partners are either (i) "Rated", i.e., rated BBB+ or higher (in fact, all are rated A or better); or are (ii) an international financial institution or an agency owned by a government of an ADB member country.[17] In the case of international financial institutions and government-owned entities, TFP additionally secures confirmation from the AIPD of exemption from IDD review. The AIPD team conducts its own review and provides an assessment for each entity. This IDD review is refreshed annually.

19. **Monitoring and oversight**. The program's procedures contain checks and balances, monitoring, and oversight that involve multiple ADB departments. Beyond controls and the oversight of transactions and limits, the program requires ongoing reporting from and maintains close contact with DMC banks, typically visiting each bank at least once per year and conducting quarterly conference calls. This degree of contact helps monitor risks and quickly resolve problems as they arise or are foreseen.[18] Reviews of DMC banks, PFIs, and risk distribution partners will be undertaken in accordance with bank policy. The TFP and CTL monitor and reconcile exposures and statistics monthly. The TFP Operating Guidelines detail operational procedures (footnote 9). These guidelines are reviewed and updated about every 18 to 24 months, as required. The program updated its operating Guidelines in 2020.

[17] BBB+ (S&P rating) is equivalent to NSO3 in ADB's Non-Sovereign Operations internal credit rating scale.
[18] Subject to change if needed as deemed appropriate by ADB Management.