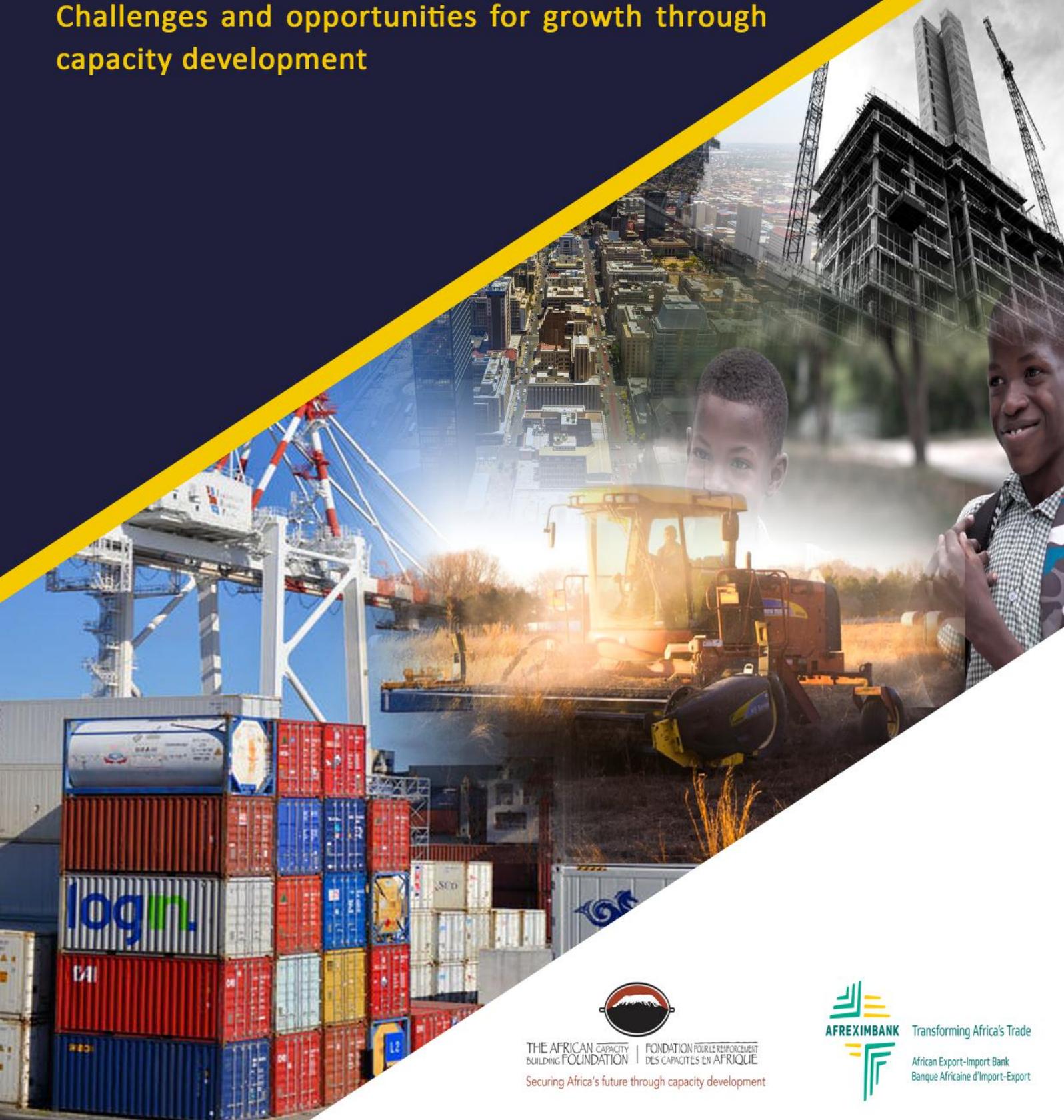


# Factoring in Africa to support trade development:

Challenges and opportunities for growth through capacity development



THE AFRICAN CAPACITY BUILDING FOUNDATION | FONDATION POUR LE RENFORCEMENT DES CAPACITES EN AFRIQUE

Securing Africa's future through capacity development



Transforming Africa's Trade

African Export-Import Bank  
Banque Africaine d'Import-Export



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## Foreword

African countries have engaged in various important initiatives aimed at boosting intra-Africa trade and Africa's global trade performance. As a key program of Agenda 2063, the African Continental Free Trade Area agreement (AfCFTA) launched on 7 July 2019 is the most significant. Trading under the AfCFTA started on 1 January 2021 with a market of 1.2 billion people and a Gross Domestic Product (GDP) of US\$2.5 trillion, making it the world's largest free trade area in terms of number of countries since the formation of the World Trade Organization (WTO).

The implementation of the AfCFTA depends crucially on the availability of trade finance to increase export capacity and to boost intra-African trade in Africa. Small and Medium Enterprises (SMEs) which account for around 80% of the Africa's businesses have a catalytic role in the AfCFTA as the engine of growth in Africa. Unlike large firms, the distinct financing needs of SMEs are not adequately catered for in the formal banking system as they are often considered as unattractive due to higher risks and transactions costs. As an important trade finance tool, factoring provides a solution for SMEs to expand trade by addressing short-term financing and cashflow problems caused by the significant time lag from ordering of goods, selling the goods, and receiving payments. While domestic factoring is still important, international factoring is increasingly recognized as critical in the implementation of the AfCFTA to increase intra-African trade. To be sure, it will enable the capturing of niche markets in other African countries through the development of a network of import and export factors to address cross-border financing needs and related administrative, cultural, language and other barriers. Reverse factoring also has the potential to revolutionize strategic supply chains as part of regional value chain development through partnerships among medium-large companies, SMEs as suppliers, and factoring companies—banks, non-bank financial institutions and fintech companies. In addition, reverse factoring can be catalyst for increasing value addition and diversification through supply chain management, which is critical for accelerating Africa's industrialization and the implementation of the AfCFTA.

However, the use of factoring as an alternative trade financing tool to support Africa's SMEs is still at its infancy stage. Africa's share of global factoring (domestic and international) market of EUR 3,000 billion a year is currently 0.84%, which is less than 1%. For Africa, the practice is relatively recent and not widely understood. Given the negative and disproportionate impact of COVID-19 on the finances of SMEs in Africa, there is an urgent need and an opportunity for factoring to be promoted to enable SMEs to grow their businesses, expand export capacity, increase intra-Africa trade as part of the post-COVID-19 recovery and resilience to build back better. It is against this background that ACBF in collaboration with Afreximbank developed this paper to examine the capacity imperatives for the development of factoring as an innovative trade financing tool for SMEs to accelerate the implementation of the AfCFTA.

Achieving a faster growth in the volume of factoring, particularly in international and reverse factoring which are the essential building blocks to accelerate the implementation of the AfCFTA, would require addressing the key constraints affecting the development of factoring in Africa. It is precisely these constraints that the study has identified. These constraints include limited understanding of the concept and its benefits, institutional gaps such as inadequate legal and regulatory framework, lack of policies to create an enabling environment for factoring and inadequate number of factoring companies and credit insurance companies. There is also lack of technical knowledge and transformative leadership skills as well as inadequate data to inform policies and to assess progress. The strong message that emerges from this publication is that factoring provides enormous potential for trade finance for SMEs in African countries and there is a need to build capacity and share knowledge to facilitate the development of factoring in Africa.

**Professor Emmanuel Nnadozie**  
*Executive Secretary*  
The African Capacity Building Foundation

## List of Acronyms

|             |   |
|-------------|---|
| ACBF        | African Capacity Building Foundation                        |
| AfCFTA      | African Continental Free Trade Agreement                    |
| Afreximbank | African Export-Import Bank                                  |
| BCR         | <i>Banca Comercială Română</i> (Commercial Bank of Romania) |
| COVID-19    | Coronavirus disease 2019                                    |
| EUR         | Euro (European Monetary Unit)                               |
| FCI         | Factors Chain International                                 |
| GDP         | Gross Domestic Product                                      |
| RECs        | Regional Economic Communities                               |
| SMEs        | Small and medium-sized enterprises                          |
| UNIDROIT    | International Institute for the Unification of Private Law  |
| WHO         | World Health Organization                                   |
| WTO         | World Trade Organization                                    |

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## Executive Summary

**Background:** Factoring known as the selling or transferring of accounts receivable to secure funds that are immediately available, provides a solution to address the financing gap for SMEs to support trade development as part of the AfCFTA and Africa's structural transformation agenda. However, the development and use of factoring as an alternative trade financing tool to support businesses, particularly Africa's SMEs is still at its infancy stage compared to other regions as the practice is relatively recent and the product and its potential benefits are not well understood.

**Aim and Study Approach:** The aim of the paper is to examine the capacity imperatives for the development and use of factoring as an innovative trade financing tool to advance the implementation of the African Continental Free Trade Agreement (AfCFTA). The study is based on an extensive review of the literature and an analysis of secondary data from Factor Chain International (FCI) database and other materials collected on factoring to identify key issues, trend, progress, drivers, and barriers affecting factoring in leading African countries.

**Key Findings are summarized below:**

### ***Benefits of factoring in trade development and industrialization.***

Factoring offers an alternative source of financing for African businesses to increase intra-African trade under the AfCFTA. Whilst domestic factoring is still important, international factoring will allow African businesses to increase intra-African trade by capturing niche markets in other African countries through the development of a network of import and export factors to facilitate trade financing. Reverse factoring as a relatively new product in Africa also has the potential to revolutionize value chain development through the support of strategic supply chains in key sectors to support Africa's industrialization.

### ***Africa's share in global factoring and growth rate in factoring.***

Africa's share of 0.84% in the global factoring market of EUR 3,000 billion a year in 2019 is extremely low with Europe leading with a market share of 67.7%, Asia Pacific (23.5%), South America (4.5%) and North America (2.9%). The continent also experienced the smallest growth rate of 6.22 % in factoring volume from 2013 to 2019 compared to other regions - 98.74% for Middle East; 45.98% for Europe; 30.19% for South America and 8.38% for Asia.

### ***Factoring GDP penetration in Africa compared to other regions.***

Factoring GDP penetration rates of leading African countries are well below other regions. South Africa is the best performing country by a huge margin in Africa with a 6 % GDP penetration-rate in 2019 compared to 2.37% in Morocco, Mauritius (1.83%), Tunisia (0.98%) and Egypt (0.22%). This is significantly below that of leading countries in Europe and Asia such as Spain with a GDP penetration of about 15%, Hong Kong (14%), United Kingdom (13%) Australia (9%), and Chile (12%).

### ***Number of companies in Africa compared to other regions.***

There are significant variations in the number of companies involved in the global factoring market ranging from over 2,200 in Asia Pacific to 23 (Middle East), 847 (South America), 688 (Europe), 323 (North America) and 154 companies in Africa. Within Africa, South Africa dominates with 110 companies, 25 (Morocco), 11 (Egypt), 5 (Tunisia) and 3 (Mauritius).

### ***Factoring volume/turnover per company in Africa compared to other regions.***

Apart from South America with a factoring volume/turnover of 155 million euros per company, Africa with 159 million euros per company lags well behind other regions with Europe significantly ahead at 2,872.4 million euros per company, Middle East (432 million euros), Asia (312.4 million euros) and North America (268.6 million euros). Within Africa there is also a significant disparity with average factoring volume/turnover per company of 190 million euros in South Africa, 101.3 million euros Morocco, 67.6 million euros Tunisia, 53.4 million euros Egypt and 53.5 million euros Mauritius.

### ***Share of leading countries in the factoring market in Africa.***

Although, factoring is gradually being developed in Africa, it is still dominated by a few countries. South Africa is the most advanced with 85% share, followed by Morocco (10%) and Egypt (3%) while Mauritius and Tunisia each had a share of 1% in 2019. Small sized factoring companies are emerging across the continent, particularly in Cameroon, Gabon, Ghana, Côte d'Ivoire, Kenya, Mauritania, Mozambique, Nigeria, Senegal, Tanzania, Zambia, and Zimbabwe but data is not available on the level of factoring activities.

### ***Share of international factoring compared to domestic factoring in Africa.***

The share of international factoring (compared to domestic factoring) in leading African countries is also very low with Egypt at 21.22%, South Africa (17.3%), Morocco (4.27%), Tunisia (3.85%), and Mauritius (1.3%).

### ***Key drivers stimulating the growth of factoring.***

Key drivers are the demand for funding for SMEs as engines of economic growth, innovation, and scope for expansion of factoring products including international and reverse factoring as well as digital transformation to automate and simplify functions including customer interfaces, documentation processes and analytics.

### ***Main barriers affecting the development of factoring.***

The main barriers are lack of familiarity with the concept and visibility, challenging domestic environment, including competition from banks and limited number of factoring companies, inadequate legal and regulatory framework, problems with taxation and high transaction costs, limited credit insurance, policy environment characterised by policy inconsistencies and lack of data on factoring activities for evidence-based policies and to track progress.

**Conclusion:** Factoring provides a sustainable solution to address the financing gap of SMEs and to facilitate trade development necessary to advance the implementation of AfCFTA. However, Africa's performance in the factoring market need to improve significantly based on number of key indicators - share in global factoring, including international factoring, innovation such as reverse factoring, number of factoring companies, turnover per factoring companies, and factoring GDP penetration. Factoring activities are projected to reach US\$50 billion by 2025 in Africa with a number of small-sized factoring companies emerging in other African countries. However, a coordinated approach to capacity development is needed to address the barriers identified.

### **Key recommendations include:**

- strengthening institutional capacity for developing legal and regulatory framework to adopt the model factoring law, improving the policy environment, building credit information systems, and fostering partnerships to modernize factoring using digital solutions, increase the number of factoring companies and factoring volume significantly;
- strengthening human capacity focusing on critical technical skills including trade economists, trade lawyers, digital specialists, supply chain specialist, logistics, credit risks and insurance experts and building transformative leadership skills such as the appointment of 'Factoring Champions' to promote factoring in African countries; and
- setting a research agenda to facilitate data collection for evidence-based policy-making and tracking progress, knowledge sharing, policy dialogues and advocacy to support the strengthening of institutions and skills building of key actors and increase awareness of the benefits to stakeholders.

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## 1. Introduction

The Africa Continental Free Trade Agreement (AfCFTA) is a flagship program of Agenda 2063 and one of the most recent initiatives aimed at overcoming trade constraints and boosting Africa's trade performance. Such continental Agreement aims to consolidate Africa into one major trading bloc and presents opportunities to boost export capacity and increase intra-African trade. Signed by 54 African countries and ratified by 34 (ECA, 2020), the operational phase of the AfCFTA was officially launched on 7 July 2019 with trading initially slated for 1st July 2020 but has been delayed by COVID-19 pandemic. COVID-19 threatened to reverse the gains made in strengthening trade and economic integration in Africa due to measures taken to fight the pandemic such as the restrictions on businesses and travels including the closure of borders to trade. COVID-19 measures significantly affected businesses across different sectors resulting in a disproportionate impact on SMEs with a critical role to play in trade development to implement the AfCFTA.

Trading under the AfCFTA started from 1 January 2021 but measures are needed to put the AfCFTA back on track. With the elimination of up to 90% of tariffs on African goods, the AfCFTA implementation will boost intra-African trade and promote the transfer of technology, industrial development, economic productivity, and diversification of economies. The AfCFTA will require financing to ensure that Africa's 1.2 billion people and its US\$2.5 trillion market benefit from its operationalization (Harare Receivables Exchange, 2020). SMEs are expected to play a catalytic role in the implementation of AfCFTA as the growth in African economies is largely driven by them, but they face greater financing obstacles in the formal banking systems with banks often considering SMEs as unattractive due to higher risks and transactions costs.

Factoring known as the selling or transferring of accounts receivable in order to gain funds that are immediately available, provides a solution to address the financing gap particularly for Small and Medium Enterprises (SMEs) to support trade development through the African Continental Free Trade Agreement (AfCFTA). The immediate access to cash for the supplier/seller makes factoring an essential financing instrument especially for a continent such as Africa with a large number of SMEs forming the "backbone" of African economies, often with limited access to formal bank loans (London Stock Exchange Group, 2018). Factoring offers an alternative source of financing that can contribute significantly to the long-standing challenge of financing Africa's development agenda and priorities (Oramah, 2014a) particularly the AfCFTA. To accelerate the implementation of AfCFTA, factoring is increasingly recognized as viable tool for trade development (Oramah, 2014a; Tomusange, 2017) that can address the financing gap for SMEs to boost export potential and increase intra-African trade under the AfCFTA. The growth of intra-African trade through the AfCFTA will result in the growing need for factors to address cross border trade financing across the continent (Awani, 2020). SMEs, which are bearing the brunt, in the face of severely constrained conventional sources of finance, could benefit the most. Factoring is an alternative cost-effective form of financing to enable businesses to unlock funding held in their yet to be paid invoices (Harare Receivables Exchange, 2020).

However, factoring as a funding option remains largely under-utilized in Africa given its potential to assist African SMEs and support the participation of SMEs as indirect exporters in supply chains or suppliers to larger businesses. The African continent is a relatively small player in the global factoring market (Oramah, 2014a; Oramah and Dzene, 2014; Tomusange, 2017). The development and use of factoring in the African continent is low due to various challenges, including the lack of a comprehensive facilitative legal and regulatory infrastructure governing factoring transactions in Africa, as well as lack of awareness on the continent about the product (Kameni, 2014).

There is therefore a need for a better understanding of the key drivers stimulating the growth of factoring and barriers affecting its development as an alternative and viable tool for trade finance and development in the African continent.

The objective of this paper is to examine the capacity imperatives for the development and use of factoring as an innovative financing tool to advance Africa's development agendas. To achieve the objective, the paper is based on desktop research of literature, and analysis of secondary data and materials. First,

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an extensive literature review was carried out which focused on the evolution of factoring and trend in Africa. Second, factoring volume data was collected from FCI (Factors Chain International) platforms, the global representative body for factoring and financing of open account domestic and international trade receivables. Data available on the leading African countries involved in factoring (Egypt, Mauritius, Morocco, South Africa, and Tunisia) were reviewed and analyzed to determine the trend and progress made by African countries, focusing on variables such as factoring turnover, growth rates, volume by country and drivers and barriers. The choice of countries was mainly due to the availability of data from the FCI database. The findings provided the basis to develop a better understanding of how to frame the capacity challenges using the African Capacity Building Foundation (ACBF) holistic capacity development framework to identify the gaps in factoring and to provide recommendations to address the capacity constraints affecting the development and use of factoring across the continent.

The paper is structured as follows. Following the introduction, Section 2 reviews the extant literature, including the definition, models, and evolution and benefits of factoring. Section 3 examines the potential role of factoring in financing Africa's trade development and advancing the implementation of AfCFTA. Section 4 examines the factoring trends in Africa compared to the rest of the world, progress in factoring in leading African countries to better understand the key development indicators, main drivers of factoring and barriers affecting the development of factoring in Africa. Section 5 analyzes the key capacity challenges and discusses the institutional and human capacity constraints affecting the development of factoring in Africa and Section 6 is the conclusion and the recommendations.

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## 2. Evolution of Factoring

### 2.1 Origin of factoring

From as early as the 1200s, variations of invoice factoring were used in countries and regions such as Italy, Turkey, Northern Africa, Spain, the Netherlands, France, and other countries (Factoring Directory, 2017). Some scholars trace the origins of factoring to the Roman Empire where rich manufacturers and merchants used a mercantile agent or factor to administer the sales of their merchandise (Rutberg, 1994; FCI, 2019a). Merchants who worked in the clothing, textiles, fabrics, and garment trade routinely used factoring companies to fund their operations. In general, whenever manufacturing and distribution businesses needed to ship or export their finished products, there is a strong probability that invoice factoring services were used. Domestic factoring emerged from the US in the mid-19th century with European countries considered as pacesetters for international factoring from the 1960s. Contemporary factoring, which originated from the United States' model is considered as an innovative finance tool, and an alternative to the traditional bank loan and other credit lines (FCI, 2019a). Factoring is therefore recognized as one of the oldest forms of commercial finance (Bakker, Klapper and Udell, 2004).

### 2.2 Concept of factoring

The term “factoring” has been defined in different ways due to the absence of a uniform codified law. The World Bank (2009) defined factoring as ‘a technique whereby, under the terms of a contract, a specialized credit institution (the factor) takes responsibility for collecting a company’s debts while opting to bear any losses incurred as a result of debtor insolvency’. Broadly, it is defined as a relationship created by an agreement, between the seller of goods or services and a financial institution called the factor, whereby the latter purchases the receivables of the former and also controls and administers the receivables of the former (Tomusange, 2017). Factoring based on the sale of accounts receivables (short term assets) is a useful financing tool for efficient and off-balance sheet access to working capital, especially for small and medium size companies (EBRD, 2018).

Factoring is popularly used to mean a financial transaction in which a supplier (business) sells its invoices (accounts receivables) to a third party (called a factor) at a discount in order to immediately receive cash for a payment for goods or services whose payment the supplier, ordinarily, would have had to wait a certain period to receive (Klapper, 2006; Malhotra, Chen, Criscuolo, Fan, Hamel, and Savchenko, 2007; Tomusange, 2015; 2017). By so doing, the supplier receives working capital immediately and transfers the ownership of the debt on the invoices to the factor (factoring company) as well as responsibility for collection of payment on the same (Obara, 2011).

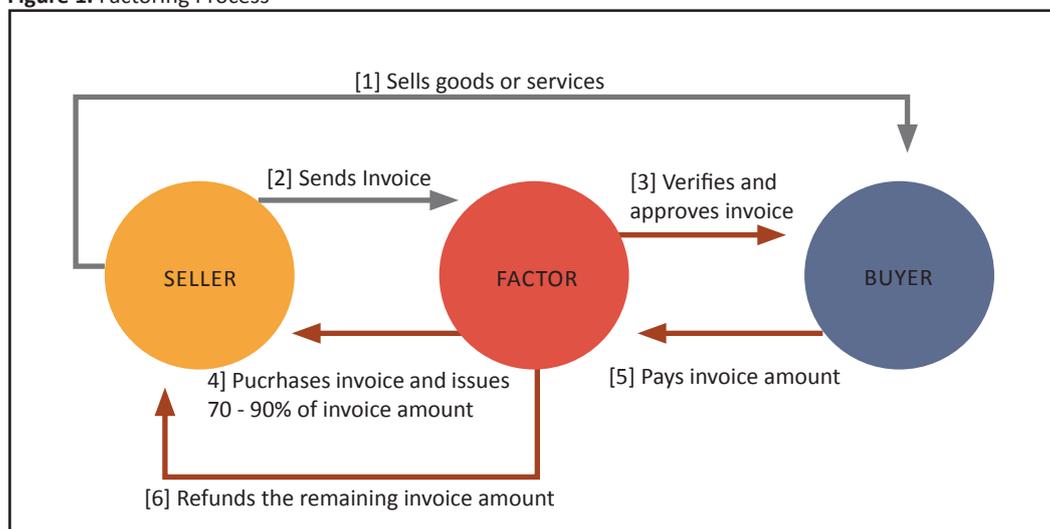
Factoring is carried out through the selling of invoices using a process known as assignment which involves an arrangement between a business concern or seller (sometimes known as client), a buyer (debtor) and financial institution (factor). A *factor* is essentially a “*funding source* that agrees to pay the company the value of an invoice less a discount for commission and fees” (Investopedia, 2020). The amount paid upfront will be a percentage of the value of the receivables purchased but will vary depending on the factor’s perception of the debtors’ creditworthiness (World Bank, 2009).

### 2.3 Types of factoring: key processes and actors

There are different types of factoring reflecting a variation in processes and roles by different actors. For example, in domestic factoring there are three parties involved, (1) the seller (client) – company which sells goods and services on credit, (2) the buyer (debtor) – customer who purchases goods from the client and the (3) Factor – financial institution which acts on behalf of the client to collect debts from the debtor - acting as an extension of the borrower’s back office for the collection processes and bookkeeping. However, in international factoring (cross border factoring), there are four parties namely: (1) the seller (client) – exporter or the company which sells goods and services on credit; (2) buyer – importer or customer who purchas-

es goods from the client; (3) export factor responsible for all factoring operation and selecting the counterparty (import factor) and (4) the import factor in the country where the goods will be shipped. Having an export factor and import factor reduces the risks in international, cross border transactions or trade. The import factor ensures that the local context is properly understood and facilitates communication in dealing with unfamiliar culture, foreign customs, and the local language (Factoringkb, 2020). Figure 1 shows the process of factoring with the key actors involved.

**Figure 1.** Factoring Process



**Note:** Suppliers (of good/services) are factoring users who sell to their customers known as buyers or debtors

**Source:** Adapted from FCI (2020d)

Domestic factoring relates to transactions carried out in the same country where there is a single factor. According to Egypt’s Factoring Law, factoring is considered domestic when both the client and the debtor are registered or are residents in Egypt (EBRD, 2018). In international factoring, there will be an international trade contract with two factors (the import and the export one) with the export factor buying the exporter’s debt. The main difference is that the debtors in international factoring are foreign companies. Factoring allow businesses to export or import between countries and be assured of payment from counter parties. For example, MCB Factors in Mauritius conducts international factoring via Factors chain international (FCI) using a network of factoring companies with more than 250 members in more than 70 countries (MCB Factors, 2020). Collection services are outsourced to factoring members within FCI thus removing the cultural and language barriers.

The International Institute for the Unification of Private Law (UNIDROIT) Convention considers four main functions of factoring which are (1) cash financing (through the factor’s advancing the supplier with immediate cash upon entering into factoring transaction); (2) accounts receivable administration (by taking over the administration of the seller’s buyer accounts); (3) collection of the accounts receivable from the seller’s buyer; and (4) credit insurance to cover the seller from buyer payment default (FCI, 2019a; Nure, 2018; EBRD, 2018). *Full-service factoring* includes all the factoring services from (1) to (4) – i.e., finance, accounts receivable administration, collection of accounts receivable, credit risk cover. However, factoring companies may choose not to subscribe to all the main functions, and some may provide other additional services such as consulting services, debt recovery litigation services, appraisal of customers’ creditworthiness and risk prevention, simplification of debt collection services (World Bank, 2009).

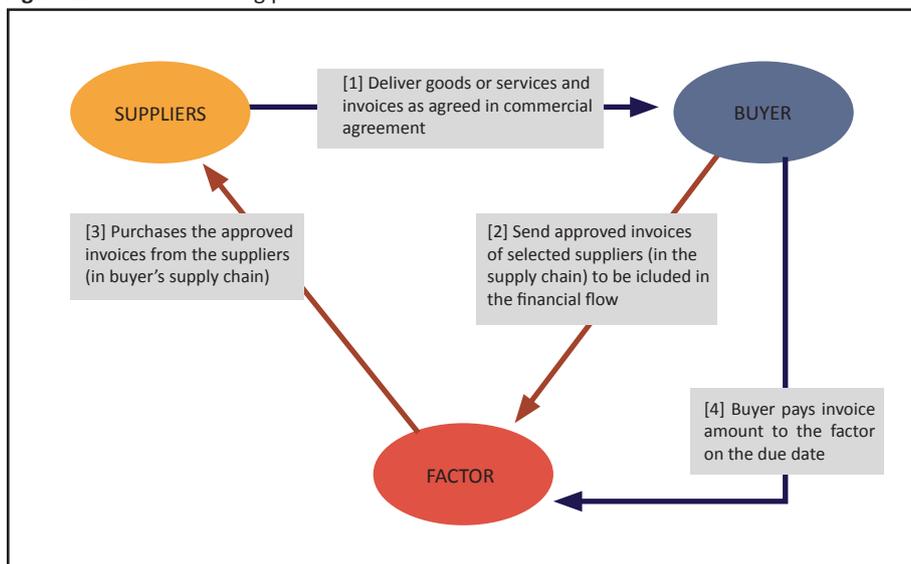
However, there are different types of factoring which relates to the way a transaction is made (Tomusange, 2017; FCI, 2019). For example, *factoring with recourse* is where the client (i.e., seller) is not protected against the risk of bad debt i.e., in the case of uncollectable debt, the client bears the loss (Alayemi, Oyeye and Adeoye, 2015). In this situation, the transaction changes from factoring to a loan (given that the supplier would have already received the cash at the time of the factoring transaction). In *factoring without recourse (known as non-recourse factoring)*, the factor bears the loss of a non-collectible payment (Green,

2014; Tomusange, 2017). *Non-recourse factoring* effectively means that if there is an issue with payment, an insurance claim is made against the buyer, and the client (seller) need not pay. The factor that purchases the receivables assumes the credit risk for the buyer’s ability which means that the financial service includes credit protection, amongst other services (Klapper 2005). In the case of buyer insolvency, the benefits of trade finance companies come into play as they will file an insurance claim against the buyer (Tradewind Intelligent Finance, 2020).

Other examples include *maturity factoring*, *mixed factoring*, *invoice discounting* and *partial factoring*. *Maturity factoring*, also known as materiality factoring, is the full service without the finance function of the service. In this type of factoring, the supplier may already have other sources of capital but seeking to reduce administration overheads while having a guarantee of receiving payment by a stipulated period – at the maturity of the agreed payment period (provided there is credit cover – in the case of an insolvent buyer) (FCI, 2019a). *Mixed factoring* is one which combines payment in advance (85% or more) to the supplier, with the remainder being paid later (Alayemi, Oyeleye and Adeoye, 2015). *Invoice discounting* is the only type of factoring which differs from the others, as the buyer is not being notified of reassignment of an invoice to the factor. Confidentiality of this arrangement is kept by the fact that the collections from the buyer are made into a bank account in the name of the buyer but wholly controlled by the factor (FCI, 2019a). In *partial factoring* some invoices are selected as not all the invoices are accepted for buying (Alayemi, Oyeleye and Adeoye, 2015). *Reverse factoring (or supply chain financing)* is a financing method initiated by the buyer, usually a medium-sized to large company, to help suppliers in its supply chain to finance receivables easily and at a lower interest rate than what would normally be offered.

Suppliers benefit from better pricing of credit risks due to the creditworthiness of the buyer (i.e., medium-sized to large company). The buyer starts the process by choosing invoices of suppliers in their manufacturing and distribution supply chain to be paid earlier by the factor at an accelerated rate in exchange for a discount, typically at a lower interest cost (International Finance Corporation, 2014; Global Supply Chain Finance Forum, 2016; PwC, 2018). Figure 2 shows the process of reverse factoring.

Figure 2. Reverse factoring process



Source: Adapted from Danske Bank (2020)

Reverse factoring is a short-term financing solution tailored to fit the needs of suppliers that serve large customers. Through the intermediary of a “factor”, suppliers can obtain payment for their invoices before the contract deadline (BNP Paribas, 2016). The factor could be a Bank, non-bank financial institution and increasingly Fintech - technology companies delivering financial services. SMEs are increasingly attracted to reverse factoring services as it represents a win-win situation as buyers are able to secure their supply chains, improve supplier relations and approve suppliers’ invoices and suppliers are able to receive financing quickly at a highly competitive rate and enhance their cash flow management.

Factoring exists as source of financing, but other means of financing are still available. They include peer-to-peer lending (where funding is sourced from crowdfunding sites, friends, families, etc. with low capacity to mobilize large amounts); revenue-based finance loan system (where the borrower will repay a certain percentage of sales every month until the loan is fully repaid or settled with low probability of mobilizing required resources); and pension-led funding (where businesses can have the opportunities to leverage the value of their assets, which can be purchased or leased by the pension fund, with low coverage in Africa). Unlike alternative means of financing, factoring has significant benefits for SMEs (see in Table 1).

**Table 1.** Key Benefits of Factoring

|  |
|--|
| <p><b>Quick turnaround for cash and overcome rigid requirements associated with a bank loan.</b> Ability to access finances faster with up to 90% of the invoice value paid within 8 business hours (e.g., BNP Paribas Factor) or within 24 hours (e.g., MCB Factors in Mauritius). Factoring does not require the stringent review associated with bank loan applications with list of terms and conditions.</p>  |
| <p><b>Opportunities for maintaining market share and rapid growth.</b> Without factoring, a business will be out of stock and other companies will take their market share. Can take on new orders which would not have happened without the quick cash raised against unpaid invoices to have access to working capital and responding quicker to customers' needs and market opportunities for growth by boosting sales rapidly.</p>   |
| <p><b>Flexible and scalable to meet changing or evolving business needs.</b> Factor agreements can be adapted to fit the changing/evolving needs of an organization (e.g., a business can decide to factor all invoices or choose to factor no invoices. Quick cash required for a new opportunity/other business needs can be secured easily).</p>  |
| <p><b>Credit screening for company's customers to make better business decisions.</b> The factor conducts the assessment for creditworthiness and once customers are approved, the factor purchases invoices, advances cash to the company and collect the debt from the customers later. The funding is based on the creditworthiness of a company's customers rather than the borrower's own financials.</p>   |
| <p><b>Saving time and facilitating the collection procedures.</b> Without factoring businesses wait for a considerable period (e.g., up to 90 days to receive payments) or longer if the time from ordering, customs clearance etc. is considered. (e.g., Morocco has a law to limit payment periods to 60 days, but it is difficult to enforce and penalties are not defined for late payers. Factoring simplifies the collection of invoices by transferring it to the factoring company working with clients in a way that is not detrimental to customer relationship.</p> |
| <p><b>Building loyalty from suppliers with potential discounts and responding to customer needs.</b> Raising cash against unpaid invoices ensures that suppliers are paid earlier to build loyalty/trust and to secure generous discounts. It also addresses customers request for long term payments and those who pay late.</p>  |
| <p><b>Keeps balance sheet clean and retaining equity in company.</b> Unlike bank loans, factoring does not show up on a company's balance sheet as debt which will improve leverage with room to grow. Factoring provides control on company's finances by retaining equity rather than seeking capital investors for portions of equity.</p>  |
| <p><b>Debtor protection through the credit insurance cover.</b> Help companies to create more predictable cash flow; and allows for the conduct of business with approved credit for customers.</p>  |
| <p><b>No collaterals required.</b> Provides financing without securities which is good for SMES with smaller balance sheets. Many SMEs do not have access to bank borrowings, as banks are generally reluctant to provide funding to companies with smaller balance sheets.</p>  |

*Source: Author's compilation from different sources*

Key benefits include quick turnaround for cash, opportunities for rapid growth, flexibility and scalability and not requiring businesses to have a good credit score compared to many other financing options (Hamanyati, 2017). However, factoring if not properly managed can result in the loss of internal control of debt management and direct business-client relationship nexus as well as additional transaction costs depending on the receivables transferred, and/or a fee charged by the factoring company. The rewards and benefits clearly outweigh the associated risks (Tomusange, 2015).

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### 3. Using Factoring to address Africa's trade financing gap

Africa has made significant progress in its development process, and despite the slowdown in economic growth in recent years due to COVID-19, the continent remains among the fastest growing regions in the world. Africa has benefitted from strategic long-term planning anchored on the development priorities of the continent, with its vision and goals well-articulated in Agenda 2063. However, in the absence of finance, implementation of these noble plans and strategies for socio-economic transformation programs embedded in Agenda 2063 will not happen. Africa has a large financing gap and domestic resources are expected to contribute to about 80% to 90% to the financing of the Agenda 2063 (African Union Commission, 2017). Financing is also expected through other mechanisms including the international financial market, foreign investments, official development assistance to support African priorities (Nnadozie, Munthali, Nantchouang and Diawara, 2017; African Union Commission, 2017).

#### 3.1 Potential for supporting Africa's AfCFTA program

One of the flagship programs of Agenda 2063 is the African Continental Free Trade Area agreement (AfCFTA) signed by 54 African countries and ratified by 34 based on the Johannesburg Declaration of December 2020. The operational phase of the AfCFTA initially slated for 1st July 2020 has been delayed by COVID-19 pandemic. Trading under the AfCFTA started from 1 January 2021. The AfCFTA is expected to cover a market of 1.2 billion people with a Gross Domestic Product (GDP) of US\$2.5 trillion, making it the world's largest free trade area since the formation of the World Trade Organization (WTO). The AfCFTA aims to consolidate Africa into one major trading bloc and factoring can be a catalyst for unlocking working capital and an avenue for efficient and secure payments across the continent (Harare Receivables Exchange, 2020). Factoring offers an alternative source of financing that could enable African businesses to increase trade within the AfCFTA and, more importantly, trade competitively. However, factoring remains one of the potential sources of financing for the AfCFTA flagship program. Factoring is a cost-effective alternative form of financing where businesses can unlock funding held in their yet to be paid invoices (Harare Receivables Exchange, 2020) but this funding option which can assist African SMEs and private sector trade under the AfCFTA remains largely under-utilized in Africa.

#### 3.2 Factoring as alternative financing for SMEs to implement the AfCFTA

The factoring product has been recognized by governments and central banks as a safe and secure means to finance trade and to support SMEs (FCI, 2016). The growing interest of SMEs in factoring is 'largely based on the fact that the factoring company's decision is determined by the solvency and creditworthiness of the SME's customers and not of the SME itself' (World Bank, 2009). Factoring has become a growing source of external finance worldwide for SMEs (Alayemi, Oyeleye and Adeoye, 2015) as they face greater financing obstacles than larger firms in the formal financial and banking systems due to higher transactions costs and higher risk premiums (Awani, 2020) with banks often 'unwilling/unable to consider SMEs as an attractive and profitable market' (World Bank, 2009). Given the advent of the AfCFTA, there are opportunities for factoring to support the growth of African SMEs and private sector. Africa can learn from the experience of many countries in Europe, Asia, and Latin America where factoring as a trade finance tool was successfully used to provide the working capital needs of SMEs to increase their trading volumes and drive economic growth (Awani, 2020). SMEs have played, and will continue to play an increasingly critical role in cross-border trade which has long been recognized as key driver for African countries with the AfCFTA designed to overcome the disadvantages of relatively small, homogeneous and fragmented economies, deteriorating commodity prices and international terms of trade. Addressing these shortcomings through the implementation of the AfCFTA is a priority for the African continent to increase intra-African trade and to become a global player given its significant market size and natural resource endowments.

SMEs constitute the greatest proportion of Africa's industrial fiber, accounting for about 80% of businesses and employing not less than 70% of Africa's workforce. For example, recent data in Morocco, shows that the SMEs are important in the socioeconomic landscape accounting for 95% of active enterprises, generating

75% of GDP and employing 85% of the workforce (Khattab and Moudine 2016). If properly supported, SMEs can advance intra-African trade under the AfCFTA given that access to finance remains a key constraint to SME operations. Availability of sustainable trade finance through factoring will be a key lubricant to propel the AfCFTA (Afreximbank and FCI, 2020). Evidence from Kenya shows that increasing access to factoring can help fund SMEs but also benefits the community and the region as well (Nabawanda, 2019), supporting their participation as indirect exporters in supply chains and suppliers to larger businesses (Awani, 2016b).

In the context of the AfCFTA, international factoring will allow African businesses to trade in other African countries by overcoming a key constraint of intra-African trade and by extending credit terms to capture niche markets in other African countries. Reverse factoring can strengthen supply chain by ensuring that there are no hold-ups in production or manufacturing processes due to a constraint in any part or linkages in the supply chain, particularly SMEs. BNP Paribas, for example, has a supply chain financing agreement with a large Italian manufacturer of construction materials (buyer) which involves 25 suppliers with an assigned turnover of 90 million euros to speed up payment to suppliers, to ensure suppliers benefit from reasonable payment terms, improve working capital, and strengthen strategic relationships (BNP Paribas, 2020b). Indeed, reverse factoring creates liquidity across the whole supply chain by exploring various solutions with or without a facilitating technology which can be supplier-based finance and/or buyer-based finance (Gelsomino, Mangiaracina, Perego, and Tumino, 2016; Marchi, Zanoni, and Jaber 2020).

Reverse factoring represents an opportunity to support the AfCFTA implementation, by unlocking the possibilities for financing the supply chain with the potential to revolutionize strategic sectors in Africa. Weigert and El Dahshan (2019) noted that regional value chains will help Africa industrialize which is particularly crucial in the context of AfCFTA. Weigert and El Dahshan (2019) further noted that regional value chains, supporting gradual development and protecting against foreign competition, already thrive in Africa's tea industry and cassava markets. UNCTAD (2018) identified another sector such as leather and leather products industry as a tremendous opportunity for Africa to form regional value chains to add greater value to Africa's exports. Supporting regional value chain development seen as a primary model for Africa's industrialization can be enhanced through reverse factoring which will be essential to accelerate the implementation of the AfCFTA given the need for increasing value addition and diversification of Africa's products. UNCTAD (2018) further noted that well-established regional value chains in Africa can also provide an opportunity to be strategically linked into the global value chains to increase the bargaining power of the lead firms in Africa.

Factoring is therefore a vehicle that can easily boost trade immediately, enabling businesses to reach the wider continent and beyond (Harare Receivables Exchange, 2020). The importance of factoring in financing SMEs can be further justified given that the portfolio of available financial instruments is limited and does not always meet the requirements of all segments of potential customers, including SMEs (UNCTAD, 2020). Unlike large firms or high turnover businesses, the distinct needs of SMEs remain inadequately catered for and can be addressed through factoring. Through the development of factoring, SMEs which account for around 80% of the Africa's businesses will be able to access much-needed finance, payment waiting periods across supply chains will be minimized, increasing efficiency and stock turnover in trading under AfCFTA. This will directly benefit African businesses, thus allowing them to focus on productivity and long-term business growth. The factoring funding model assists stakeholders across transactions by providing confidence across the supply chains, whether they are trading companies interested in 'know-your-client process' or the regulators concerned with anti-money laundering activities in cross-border payments (Harare Receivables Exchange, 2020).

## 4. An overview of factoring in Africa

### 4.1 Factoring trends in Africa compared to the Rest of the World

The global factoring market is about EUR 3,000 billion a year and the industry has experienced a compound annual growth rate of more than 10% for the last 20 years (FCI, 2020c). Factoring volumes increased globally by 5.4% from EUR 2,767,067 million in 2018 to 2,917,105 million in 2019 (FCI, 2020c). Table 2 presents the 2019 estimates of factoring volume per region.

**Table 2.** Factoring Turnover by Region (and leading African countries) in 2019 (in euro millions)

| Region              | Domestic EUR     | International EUR | Total EUR        | Companies    |
|---------------------|------------------|-------------------|------------------|--------------|
| Total Africa        | 20,702           | 3,860             | 24,562           | 154          |
| Total Asia-Pacific  | 546,428          | 141,166           | 687,594          | 2,201        |
| Total Europe        | 1,592,792        | 383,446           | 1,976,239        | 688          |
| Total Middle East   | 7,118            | 2,819             | 9,937            | 23           |
| Total North America | 80,311           | 6,431             | 86,742           | 323          |
| Total South America | 128,055          | 3,976             | 132,031          | 847          |
| <b>Total</b>        | <b>2,375,406</b> | <b>541,699</b>    | <b>2,917,105</b> | <b>4,236</b> |

Source: FCI (2020c)

Based on 2019 data from FCI, Europe is the largest factoring market (both domestic and international combined) in the world with a market share of two-thirds (67.7%). The recent growth in Europe is driven mainly by the strategic emphasis towards the commercial banking sector which controls approximately 90% of Europe's factoring volume. Asia Pacific has the second largest with a market share of slightly under a quarter (23.5%), followed by South America (4.5%), North America (2.9%), Africa (0.84%) and Middle East (0.34%)

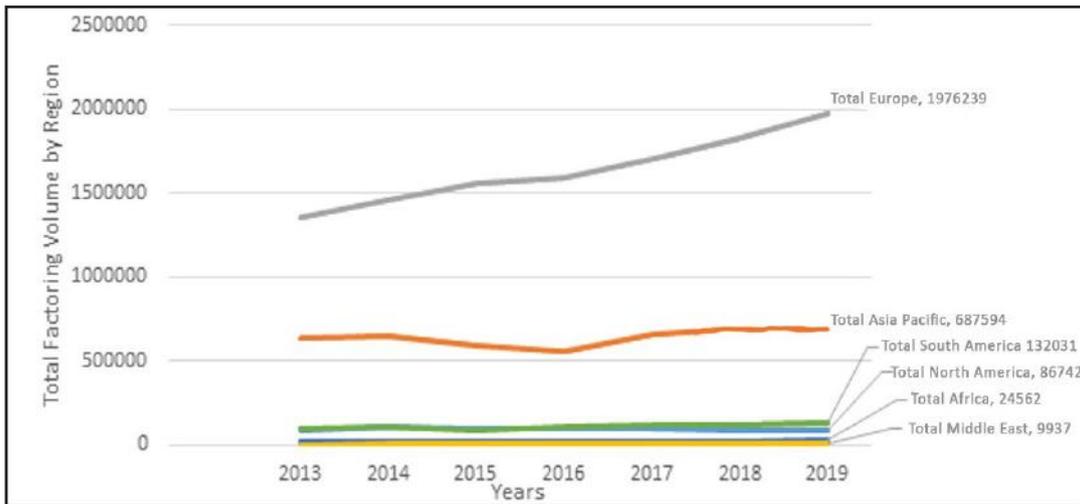
In 2010, Africa's share of global volume of factoring was 1.01% which represents a decline in market share with the continent significantly trailing behind Europe, Asia Pacific, North America, and South America in terms of global factoring (both domestic and international combined).

In terms of international factoring, the European region with 383,446 million euros accounts for more than two-thirds (70.8%) of the total cross-border factoring volumes of 541,699 million euros, followed by Asia Pacific (26.06%), North America (1.19%) and South America (0.73%). Africa's share in international factoring of 0.71% is only ahead of Middle East at 0.52%.

In terms of the number of companies involved in global factoring, there are significant variations ranging from over 2,200 in Asia Pacific to 23 companies in Middle East as shown in Table 2. Apart from South America with a factoring volume/turnover of 155 million euros per company, Africa with 159 million euros per company lags well behind other regions with Europe significantly ahead at 2,872.4 million euros per company. Middle East has a factoring volume/turnover of 432 million euros per company, Asia (312.4 million euros per company) and North America (268.6 million euros per company).

Figure 2a and Figure 2b show the growth of factoring volume in Africa and other regions. The growth of total factoring volume from 2013 to 2019 is 6.22% for Africa compared to 98.74% for Middle East; 45.98% for Europe; 30.19% for South America and 8.38% for Asia.

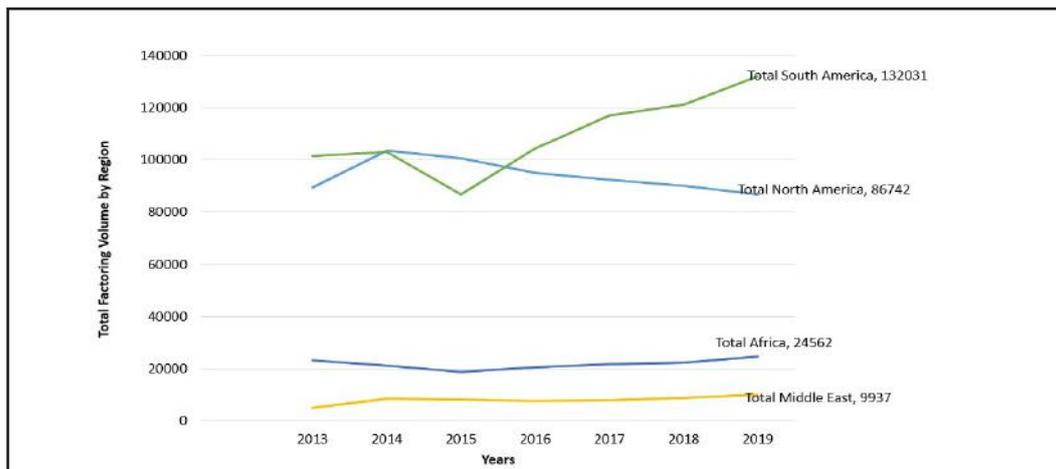
**Figure 2a.** Evolution of Factoring Volume by Region in the Last 7 Years (in Millions of EUR)



Source: FCI (2020c)

Africa is expected to experience a growth of 10% from its current volume of 24 billion euro largely due to the contribution of South Africa (+11%) and Egypt (13%) (FCI, 2020b).

**Figure 2b.** Evolution of Factoring Volume in Africa against other Regions (excluding Europe and Asia) in the Last 7 Years (in Millions of EUR)



Source: FCI (2020c)

There are expectations of a significant increase in Africa’s factoring activities with volume projected to reach US\$50 billion in 2025 (FCI, 2016). However, such opportunities for further development and expansion which offers significant benefits to SMEs in Africa can only be realized if the barriers are identified and addressed to render factoring services.

COVID-19 affected the growth of global factoring volume. Monitoring of factoring data by FCI in 2020 shows that business volumes are largely impacted from the second quarter of the year given that new invoices/ contracts were minimal as a result of declining global economic activities due to the pandemic (Mulroy, 2020). It is predicted that there will be a drop in global factoring volumes in 2020, more than the 3% decline during the credit crunch in 2009 (Mulroy, 2020). In the context of African countries, AfDB and Afreximbank 2020 Report shows that COVID-19 has added to the burden of risks facing African trade and trade finance, including factoring solutions. The COVID-19 pandemic caused a decline in the prices of most of Africa’s top export commodities, which could reduce access to foreign exchange liquidity and therefore affect the willingness of factoring companies to engage in trade finance transactions (AfDB and Afreximbank, 2020).

## 4.2 Factoring Trends in Leading African Countries

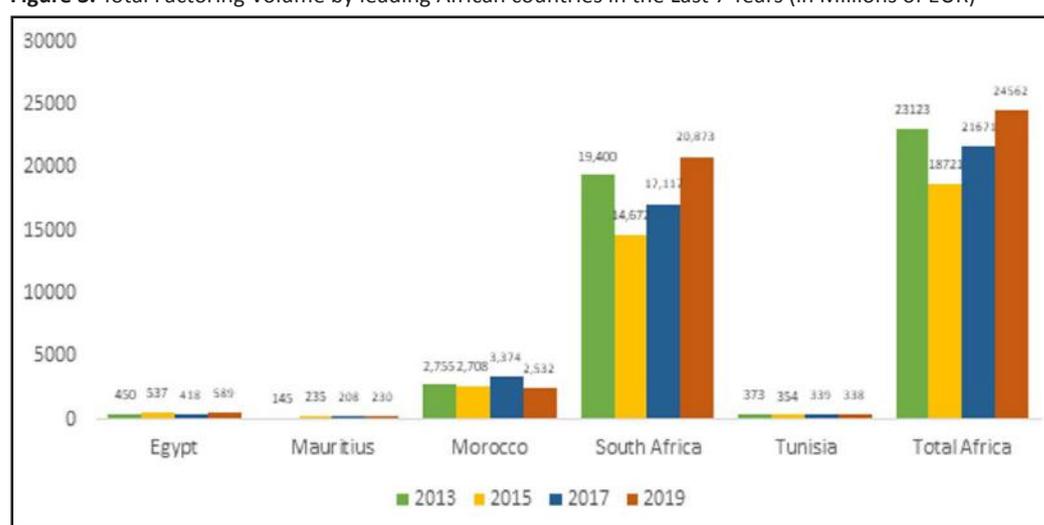
Many African countries are still in the early stages of development as the continent is a relatively small player in the global factoring market (Oramah, 2014a; Oramah and Dzene, 2014; Tomusange, 2017). For example, no African country is represented among the top 10 domestic factoring and the top 10 in international factoring countries (FCI, 2019b; 2020c).

According to the FCI database, factoring is still dominated by Egypt, Mauritius, Morocco, South Africa, and Tunisia. In Africa, South Africa is the most advanced dominating with an 85% share, followed by Morocco (10%) and Egypt (3%) while Mauritius and Tunisia each had a share of 1% in 2019. As of 2019, only 14 African countries have businesses which offer factoring services and are members of the FCI (FCI, 2020a). There is a growing market in Sub-Saharan African countries with a number of small sized factoring companies emerging across the continent, particularly in Cameroon, Gabon, Ghana, Côte d'Ivoire, Kenya, Mauritania, Mozambique, Nigeria, Senegal, Tanzania, Zambia and Zimbabwe that are receiving support from their governments and the central banks (Ivanovic, Baresa, and Bogdan, 2011). Egypt, Morocco, Nigeria, Mauritius, Cameroon, Zimbabwe, Botswana, and the Republic of Congo, joined FCI in 2018 (Awani, 2019) but data is not readily available on all the countries.

Although factoring companies or factoring departments of banks can be found in most parts of the world (FCI, 2019a), factoring product was introduced much more recently in Africa (Kameni, 2014; Oramah, 2014a; Korankye-Sakyi, 2019). Currently, FCI has members from around 75 countries and serves more than 80% of the world's international factoring volume. World Bank, European Bank for Reconstruction and Development (EBRD), Afreximbank, IDB Invest for the Americas, Asia Development Bank (ADB), the ICC Banking Commission, and other national factoring associations are instrumental in promoting financing services across the world (Grand View Research, 2020). A key feature of factoring in Africa is that the services are mainly offered by banks and bank subsidiaries and independent factoring companies are inadequate in the continent (Oramah, 2014a).

Figure 3 shows the total volume of factoring in Africa from 2013 to 2019. Africa witnessed a growth of 2% in 2018 resulting in a total volume of EUR 22.1 billion (Awani, 2019). There was a drop in volume in 2015 to about EUR 19 billion, followed by a steady increase from EUR 22 billion in 2018 to over EUR 24 billion in 2019 representing a 10% growth. Countries that led this growth included Egypt, South Africa, Tunisia, and Mauritius with 13.9%, 12.3%, 7%, and 1.3% growth, respectively between 2018 and 2019.

**Figure 3.** Total Factoring Volume by leading African countries in the Last 7 Years (in Millions of EUR)



Source: FCI (2020c)

Total domestic factoring volume surpassed the international factoring volume in 2019 in the leading African countries. The Egyptian domestic factoring accounts for 79% of the country's total factoring business while the figures are 99% for Mauritius, 96% for Morocco, 83% for South African and 96% for Tunisia (Table 3).

**Table 3.** Factoring turnover by leading African countries in 2019 (in euro millions)

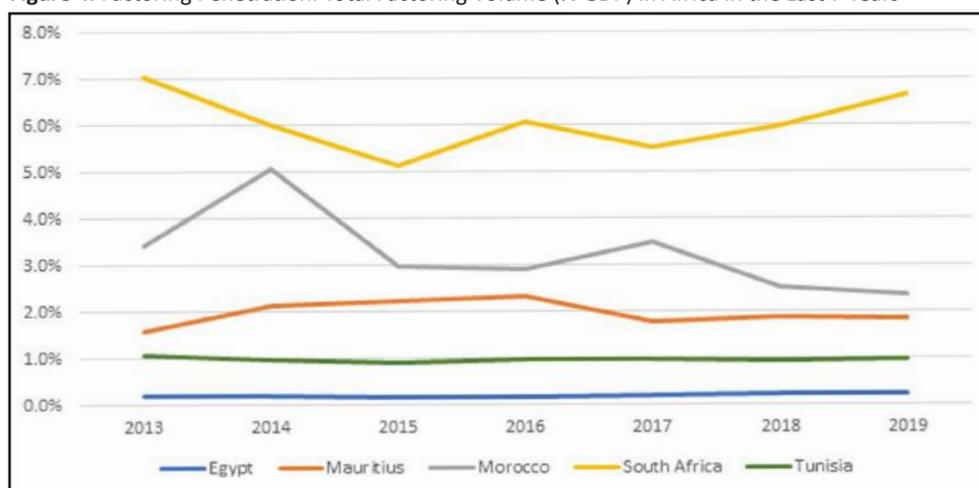
| Region       | Domestic EUR | International EUR | Total EUR | # Companies |
|--------------|--------------|-------------------|-----------|-------------|
| Total Africa | 20,702       | 3,860             | 24,562    | 154         |
| Egypt        | 464          | 125               | 589       | 11          |
| Mauritius    | 227          | 3                 | 230       | 3           |
| Morocco      | 2,424        | 108               | 2,532     | 25          |
| South Africa | 17,262       | 3,611             | 20,873    | 110         |
| Tunisia      | 325          | 13                | 338       | 5           |

*Source: FCI (2020c)*

About 80% of factoring in Africa focuses on domestic factoring (Oramah, 2014b) with recent data from FCI for 2019 showing that domestic factoring is currently at 84% (FCI, 2020c). While domestic factoring is still dominant in Africa, there are opportunities to enhance international factoring (Tomusange, 2015) as a trade finance instrument given the export-oriented nature of Africa and the potential it offers in increasing intra-African trade through the operationalization of the AfCFTA.

Figure 4 shows considerable variation in factoring market penetration rates, measured as factoring volume/ GDP from 2013-2019 in the leading African countries with South Africa significantly in the lead with 6.65% of GDP followed by Morocco (2.37%), Mauritius (1.83%), Tunisia (0.98%) and Egypt (0.22%) as in 2019. However, a recent report by the World Bank indicated a Market penetration of 3.6 percent for Morocco compared to 7.6% for South Africa and 1.1% for the Middle East and North Africa (MENA) region (World Bank, 2016).

**Figure 4.** Factoring Penetration: Total Factoring Volume (% GDP) in Africa in the Last 7 Years

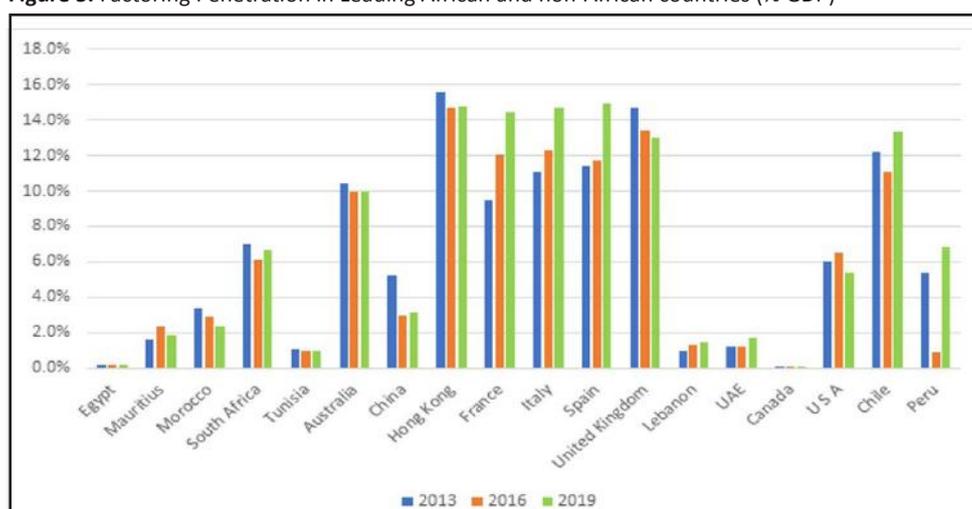


*Source: FCI (2020c)*

Figure 5 compares the factoring market GDP penetration rates in leading African countries against selected leading countries in Asia Pacific (Australia, China, and Hong Kong), Europe (France, Italy, Spain, and UK), Middle East (Lebanon and UAE), North America (Canada and USA) and Latin America (Chile and Peru) for 2013-2019.

The data shows that considerable efforts are needed by African countries given that the GDP penetration rates of leading African countries are well below those of leading European countries. For instance, while the best country by a huge margin in Africa (South Africa) has a 6% penetration-rate in 2019 compared to 2.37% in Morocco, Mauritius (1.83%), Tunisia (0.98%) and Egypt (0.22%), South Africa's performance is significantly below that of leading countries in Europe and Asia such as Spain with a GDP penetration of about 15%, Hong Kong (14%), United Kingdom (13%) Australia (9%), and Chile (12%).

**Figure 5. Factoring Penetration in Leading African and non-African countries (% GDP)**



Source: Analyzed from FCI data (2020c)

### 4.3 Case Studies of Leading African Countries

For each case study, the information captured from a variety of secondary sources and data analyzed from FCI database focused on the regulatory and legal framework, development and trend in factoring activities, nature and number of factoring companies, role of SMEs, type of factoring products in the market, challenges or key changes, and market share of leading companies.

#### South Africa

South Africa is a hybrid of Roman Dutch and English Law which is the basis of its legal structure. However, there are no specific laws governing domestic and international factoring (Hamanyati, 2017). The FCI reported total factoring volume of 20,873 million euros in 2019, up from 19,400 million euros in 2013 (FCI, 2020b), representing an increase of 7.59%.

**Table 4.** Factoring volume in South Africa compared to total factoring volume in Africa (in Millions of EUR)

| Year                 | 2013   | 2014   | 2015   | 2016   | 2017   | 2018   | 2019   |
|----------------------|--------|--------|--------|--------|--------|--------|--------|
| South Africa         | 19,400 | 15,898 | 14,672 | 16,291 | 17,117 | 18,582 | 20,873 |
| Total Africa         | 23,123 | 21,094 | 18,506 | 20,178 | 21,456 | 22,174 | 24,562 |
| *Share in Africa (%) | 83.90  | 75.38  | 79.28  | 80.74  | 79.78  | 83.80  | 84.98  |

Source: \*Analyzed from FCI data (2020c)

South Africa continues to dominate the factoring activities in Africa with a market share of 85% in total volume of factoring activities (both domestic and international) in 2019, marginally higher than the figure of 83.90% in 2013. South Africa has a share of 83.38% in domestic factoring and a significantly higher market share of 93.55% in international factoring. However, as a country only 17.30% of its activities are in international factoring.

**Table 5.** Factoring turnover in 2019 (in euro millions) by domestic and international share (%) in South Africa

| Region               | Domestic EUR | International EUR | Total EUR | *Share of international factoring (%) | # Companies |
|----------------------|--------------|-------------------|-----------|---------------------------------------|-------------|
| South Africa         | 17,262       | 3,611             | 20,873    | 17.30                                 | 110         |
| Total Africa         | 20,702       | 3,860             | 24,562    | 15.72                                 | 154         |
| *Share in Africa (%) | 83.38        | 93.55             | -         | -                                     | -           |

Source: \*Analyzed from FCI data (2020c)

South Africa is also well ahead of the other leading African countries with over 100 factoring companies out of over 150 companies operating in Africa, with an average factoring volume per company of 190 million euros and GDP penetration rates that are consistently above 5% from 2013-2019 decreasing marginally from 7.02% in 2013 to 6.65% in 2019.

**Table 6.** Factoring Penetration: Total Factoring Volume (% GDP) in South Africa (2013-2019)

| Year         | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|--------------|------|------|------|------|------|------|------|
| South Africa | 7.02 | 6.02 | 5.13 | 6.08 | 5.53 | 5.96 | 6.65 |

*Source: Analyzed from FCI data (2020c)*

Majority of businesses in South Africa are made up of SMEs (98.5%) which represent a critical force driving the country's economy. But the SMEs are historically faced with challenges of accessing the capital they need to grow to further support the development of South Africa. Evidence shows that only 6% of SMEs indicated that they have received government funding while 9% reported having been funded through private sources (SME South Africa, 2020). The factoring industry is therefore providing an excellent source of funding to emerging SMEs and represents a convenient financial means suited to the nature of businesses run by SMEs. The South African factoring industry experienced good growth over the past four decades. During this period, there have been relatively few issues affecting the factoring industry such as the global financial crisis in 2008-2009, prevailing economic conditions in 2013, conversion problems relating to information technology system experienced in 2013 by one of the major local factors, a fall-off in local demand and a sluggish South African economy in 2016 (BCR, 2019).

Invoice discounting is more popular product with other forms including supply chain finance or reverse factoring (Cory, 2020). The South African factoring industry is well established approximately 50 years old with eight (8) members making up the Debtor Financing Committee. These are Standard Bank, ABSA, Nedbank, FNB, Sasfin, Merchant Factors, Reichmann and Grinrod. Of these, Sasfin, Standard Bank and Nedbank are FCI members. Data in 2018, shows that the South African factoring market was dominated by the following factoring service providers: Nedbank (38%), FNB (24%), ABSA (13%), Standard Bank (14%), Merchant Factors (4%), Sasfin (4%) with other service providers with a combined share 3% (BCR, 2019). Clients using factoring product offerings are found in all sectors of the South African economy, including logistics, manufacturing, transport, footwear, food, clothing/textile, wholesaling, steel, pharmaceutical, and automotive equipment.

According to Cory (2020), Head Debtor of Management/Business Banking at Nedbank in South Africa, the key changes in the sector includes the increased use of automation, customers demanding quicker decisions, need to verify debt purchased electronically, licenses developed for big buyers who can secure funds and offer to their suppliers, banking sector developing business intelligence to provide higher overdraft facilities to certain suppliers to stifle competition from factoring companies and the need to employ people to innovate to cope with changes.

## Egypt

Egyptian Financial Supervision Authority is the supervisory body and regulator, and Non-banking factoring companies are required to obtain a license before starting factoring operations (EBRD, 2018). The factoring industry in Egypt started official operations in 2007. The industry covered domestic and international factoring, with the latter divided into export factoring and import factoring (BCR, 2019). The FCI reported total factoring industry volume of 589 million euros in 2019, up from 450 million euros in 2013 (FCI, 2020b), representing an increase of 30.89%

**Table 7.** Factoring volume in Egypt compared to total factoring volume in Africa (in Millions of EUR)

| Year                        | 2013          | 2014          | 2015          | 2016          | 2017          | 2018          | 2019          |
|-----------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Egypt                       | 450           | 435           | 537           | 550           | 418           | 517           | 589           |
| <b>Total Africa</b>         | <b>23,123</b> | <b>21,094</b> | <b>18,506</b> | <b>20,178</b> | <b>21,456</b> | <b>22,174</b> | <b>24,562</b> |
| <b>*Share in Africa (%)</b> | <b>1.95</b>   | <b>2.06</b>   | <b>2.90</b>   | <b>2.72</b>   | <b>1.95</b>   | <b>2.33</b>   | <b>2.40</b>   |

*Source: \*Analyzed from FCI data (2020c)*

Egypt's share of factoring is still focused on domestic activities with a share of 21.22% in international factoring, higher than the average of 15.72% for Africa.

**Table 8.** Factoring turnover in 2019 (in euro millions) by domestic and international share (%) in Egypt

| Region               | Domestic EUR | International EUR | Total EUR | *Share of international factoring (%) | # Companies |
|----------------------|--------------|-------------------|-----------|---------------------------------------|-------------|
| Egypt                | 464          | 125               | 589       | 21.22                                 | 11          |
| Total Africa         | 20,702       | 3,860             | 24,562    | 15.72                                 | 154         |
| *Share in Africa (%) | 2.24         | 3.24              | -         | -                                     | -           |

Source: \*Analyzed from FCI data (2020c)

Data from FCI in 2019 shows that 11 companies are involved in factoring activities in Egypt with an average factoring volume per company of 53.4 million euros and GDP penetration rates that varied slightly around an average of 0.2%. The GDP penetration increased marginally from 0.21% in 2013 to 0.22% in 2019.

**Table 9.** Factoring Penetration: Total Factoring Volume (% GDP) in Egypt (2013-2019)

| Year  | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|-------|------|------|------|------|------|------|------|
| Egypt | 0.21 | 0.19 | 0.18 | 0.18 | 0.20 | 0.24 | 0.22 |

Source: Analyzed from FCI data (2020c)

The Egyptian economy is heavily dependent on SMEs, which on aggregate account for 80% of the country's GDP. About 75% of the nation's labor force are also employed by SMEs. The preponderance of SMEs therefore necessitates the growing need for factoring as a tool for trade finance for SMEs (Hamanyati, 2017). According to Shaheen (2020), CEO, Egypt Factors, although factoring started more than a decade ago, there was a significant growth during the last three years from two (2) to twelve (12) factoring companies following the passage of the Model Law in Factoring. Several new institutions are now offering factoring services as the law is designed to regulate businesses, solve legal disputes, and tackle taxation issues.

Factoring as a non-banking financial service is conducted by seven companies, namely Coface Egypt, Cairo Factors, Export Credit Guarantee Company of Egypt, QNB Alahli Factoring, Egypt Factors, Tamweel Mortgage and Drive Finance. Egypt Factors was the first to enter the market and holds the largest share of factoring transactions. It is jointly owned by FIMBank Plc and the International Commercial Bank and offers the full range of factoring products to the market including domestic factoring with and without recourse, export factoring with and without recourse, import factoring and reverse factoring, both domestic and cross border (Hamanyati, 2017). Data in 2018 shows that the Egyptian factoring industry was mainly dominated by QNB Factoring which has more than a 47% share, followed by Egypt Factors with 28.4% and Drive Factoring with 18.8%. These three firms control over 94 per cent of the market (BCR, 2019).

## Mauritius

Factoring is regulated by the Financial Services Commission and the compliance process is rigid (Rambacussing, 2020). The FCI reported total factoring industry volume of 230 million euros in 2019, up from 145 million euros in 2013 (FCI, 2020b) representing an increase of 58.62%.

**Table 10.** Factoring volume in Mauritius compared to total factoring volume in Africa (in Millions of EUR)

| Year                 | 2013   | 2014   | 2015   | 2016   | 2017   | 2018   | 2019   |
|----------------------|--------|--------|--------|--------|--------|--------|--------|
| Mauritius            | 145    | 206    | 235    | 256    | 208    | 227    | 230    |
| Total Africa         | 23,123 | 21,094 | 18,506 | 20,178 | 21,456 | 22,174 | 24,562 |
| *Share in Africa (%) | 0.63   | 0.98   | 1.27   | 1.27   | 0.97   | 1.02   | 0.94   |

Source: \*Analyzed from FCI data (2020c)

Mauritius' market share in the factoring market in Africa has increased from 0.63% in 2013 to 0.94% in 2019 and was over 1% for 2015, 2016 and 2018. Mauritius's share of factoring is still focused on domestic activities with a share of 1.3 % in international factoring, significantly lower than the average of 15.72% for Africa.

**Table 11.** Factoring turnover in 2019 (in euro millions) by domestic and international share (%) in Mauritius

| Region               | Domestic EUR | International EUR | Total EUR | *Share of international factoring (%) | # Companies |
|----------------------|--------------|-------------------|-----------|---------------------------------------|-------------|
| Mauritius            | 227          | 3                 | 230       | 1.3                                   | 3           |
| Total Africa         | 20,702       | 3,860             | 24,562    | 15.72                                 | 154         |
| *Share in Africa (%) | 1.10         | 0.08              | -         | -                                     | -           |

Source: Analyzed from FCI data (2020c)

Mauritius has 3 companies registered on the FCI database with an average factoring volume per company of 53.5 million euros. Factoring GDP penetration rates in Mauritius varied from 1.59% to 2.32% with an increase from 1.59% to 1.83% from the period 2013 to 2019.

**Table 12.** Factoring Penetration: Total Factoring Volume (% GDP) in Mauritius (2013-2019)

| Year      | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|-----------|------|------|------|------|------|------|------|
| Mauritius | 1.59 | 2.14 | 2.23 | 2.32 | 1.77 | 1.89 | 1.83 |

Source: Analyzed from FCI data (2020c)

The Government of Mauritius launched the SME Factoring Scheme (Investment Support Programme) with the objective to provide financing to SMEs by easing up their cash flow by factoring their invoices which is implemented through Non-Bank-Financial- Institutions (NBFIs) that provide factoring services with CIM Finance as the sole NBFi participant in the scheme (Awani, 2019). Factoring companies must source funds and are trying to work with the government and the capital market but need a strong asset base for authorities to trust factoring companies.

The factoring offerings currently available in the Mauritius are as follows: domestic recourse, domestic non-recourse, international (import and export) factoring. However, with the issue of excess liquidity in the market, customers have a much easier access to alternative money market lines. The other forms of business finance available on the market and provided by banks are, bank overdraft, invoice discounting, trade finance, import and export loans (BCR, 2019).

According to (Rambaccussing, 2020), new products are being launched such as reverse factoring (supply chain finance) with credit insurance companies playing a major role as non-recourse factoring is now mandatory with COVID-19. However, the market is dominated by one insurer with 75% market share. There is a bright future with the launching of new products such as reverse factoring which is mainly a product for strong creditworthy companies and considered more suitable for medium to large companies as it allows them to manage payables to thousands of suppliers. Rambaccussing (2020) noted that as a factoring company registered by FCI, there are benefits from training and educating people which is the key and FCI also provides valuable network for business development.

Based on 2019 data, there are three registered factoring companies with FCI - MCB Factors (with more than 10 years' experience in factoring and performing collection on more than 7,000 debtors in the domestic market), SBM Factors (a subsidiary of SBM (NBFC) Holdings Ltd which is a non-bank financial institution) and CIM Finance but data on market share is not readily available.

There is no specific law on factoring in Morocco although the Banking Law and its implementing circulars provide only the definition of factoring and classify factoring operations under 'credit operations'. Factoring operations are regulated by the Central Bank (*Bank al Maghrib*), which issues licenses for factoring activities and its supervision (EBRD, 2018). Under Moroccan law, factoring companies must be licensed as banks or financing companies. The license will vary with the activity that is applied for and can be limited to specific

banking transactions, such as factoring operations. The Central Bank has the power to grant and revoke banking licenses.

The FCI reported total factoring industry volume of 2,532 million euros in 2019, down from 2,755 million euros in 2013 (FCI, 2020b) representing a decrease of 8.09%.

**Table 13.** Factoring volume in Morocco compared to total factoring volume in Africa (in Millions of EUR)

| Year                       | 2013          | 2014          | 2015          | 2016          | 2017          | 2018          | 2019          |
|----------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Morocco                    | 2,755         | 4,200         | 2,708         | 2,708         | 3,374         | 2,532         | 2,532         |
| <b>Total Africa</b>        | <b>23,123</b> | <b>21,094</b> | <b>18,506</b> | <b>20,178</b> | <b>21,456</b> | <b>22,174</b> | <b>24,562</b> |
| <b>Share in Africa (%)</b> | <b>11.91</b>  | <b>19.91</b>  | <b>14.63</b>  | <b>13.40</b>  | <b>15.73</b>  | <b>11.42</b>  | <b>10.31</b>  |

*Source: Analyzed from FCI data (2020c)*

Morocco's market share in the factoring market in Africa has been consistently over 10% from 2013 to 2019. It decreased significantly from 19.91% in 2014 to 10.31% in 2019. Morocco's factoring is still focused on domestic activities with a share of 4.27% in international factoring, significantly lower than the average of 15.72% for Africa.

**Table 14.** Factoring turnover in 2019 (in euro millions) by domestic and international share (%) in Morocco

| Region                     | Domestic EUR  | International EUR | Total EUR     | Share of international factoring (%) | # Companies |
|----------------------------|---------------|-------------------|---------------|--------------------------------------|-------------|
| Morocco                    | 2,424         | 108               | 2,532         | 4.27                                 | 25          |
| <b>Total Africa</b>        | <b>20,702</b> | <b>3,860</b>      | <b>24,562</b> | <b>15.72</b>                         | <b>154</b>  |
| <b>Share in Africa (%)</b> | <b>11.7</b>   | <b>2.80</b>       |               |                                      |             |

*Source: Analyzed from FCI data (2020c)*

Morocco currently has 25 companies operating in factoring with an average factoring volume per company of 101.3 million euros. Factoring GDP penetration rates varied considerably from 2.53% to 5.07% but decreased during the period from 3.43 % in 2013 to 2.37% in 2019.

**Table 15.** Factoring Penetration: Total Factoring Volume (% GDP) in Morocco (2013-2019)

| Year    | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|---------|------|------|------|------|------|------|------|
| Morocco | 3.43 | 5.07 | 2.97 | 2.90 | 3.48 | 2.53 | 2.37 |

*Source: Analyzed from FCI data (2020c)*

SMEs represent 95% of all businesses in Morocco (Hachimi, Salahddine and Housni, 2017) and face financing gap estimated to be \$37 billion. SMEs have limited access to the short-term working capital financing needed to develop and grow as 84 percent of bank loans require collateral (IFC, 2020). Factoring is therefore an important source of working capital financing for SMEs. There has been a ten-fold increase in domestic factoring from 2007 to 2014. The difficult domestic economic environment and the increase in payment delays raised the working capital financing needs for SMEs which led to increased demand for factoring (World Bank, 2016).

Morocco registered 25 companies that actively participated in factoring activities generating 2,424 million euro in domestic factoring and 108 million euro in international factoring (FCI, 2020b). Some of the factoring companies include Attijari Factoring Maroc, Maroc Factoring, Rci Finance Maroc, Jean Busnot Maroc, J.b.m. (Kompas, 2020) but data on market share is not readily available.

## Tunisia

The Ministry of Finance and the Central Bank of Tunisia both acts as supervisory bodies and regulators for factoring companies. Non-banking factoring companies are required to obtain a license from the Ministry of Finance before starting factoring operations (EBRD, 2018).

The FCI reported total factoring industry volume of 338 million euros in 2019, down from 373 million euros in 2013 (FCI, 2020b) representing a decrease of 9.38%.

**Table 16.** Factoring volume in Tunisia compared to total factoring volume in Africa (in Millions of EUR)

| Year                        | 2013   | 2014   | 2015   | 2016   | 2017   | 2018   | 2019   |
|-----------------------------|--------|--------|--------|--------|--------|--------|--------|
| Tunisia                     | 373    | 355    | 354    | 373    | 339    | 316    | 338    |
| <b>Total Africa</b>         | 23,123 | 21,094 | 18,506 | 20,178 | 21,456 | 22,174 | 24,562 |
| <b>*Share in Africa (%)</b> | 1.61   | 1.68   | 1.91   | 1.85   | 1.58   | 1.43   | 1.38   |

**Source:** \*Analyzed from FCI data (2020c)

Tunisia's share in the factoring market in Africa has been consistently below 2% from 2013 to 2019. Over the review period, it decreased from 1.61% in 2013 to 1.38% in 2019. Tunisia's share of factoring is still focused on domestic activities with a share of 3.85% in international factoring, significantly lower than the average of 15.72% for Africa.

**Table 17.** Factoring turnover in 2019 (in euro millions) by domestic and international share (%) in Tunisia

| Region                      | Domestic EUR | International EUR | Total EUR | *Share of international factoring (%) | # Companies |
|-----------------------------|--------------|-------------------|-----------|---------------------------------------|-------------|
| Tunisia                     | 325          | 13                | 338       | 3.85                                  | 5           |
| <b>Total Africa</b>         | 20,702       | 3,860             | 24,562    | 15.72                                 | 154         |
| <b>*Share in Africa (%)</b> | 1.57         | 0.33              | -         | -                                     | -           |

**Source:** \*Analyzed from FCI data (2020c)

Tunisia has 5 companies operating in the factoring industry with an average factoring volume per company of 67.6 million euros and the GDP penetration is consistently under 1% except for 2013 when it was 1.07. It is now 0.98% as at 2019.

**Table 18.** Factoring Penetration: Total Factoring Volume (% GDP) in Tunisia (2013-2019)

| Year    | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|---------|------|------|------|------|------|------|------|
| Tunisia | 1.07 | 0.99 | 0.91 | 0.99 | 0.96 | 0.94 | 0.98 |

**Source:** Analyzed from FCI data (2020c)

There are over 80,000 SMEs employing more than half the population with 40 per cent contribution to GDP. Tunisia's economy relies heavily on SMEs as key drivers for growth but access to funding and liquidity remains a serious constraint (Zgheib, 2019). Access to finance for SMEs has therefore been identified as a strategic priority by both the government of Tunisia and the EBRD recently provided a €24 million loan to *Tunisie Leasing and Factoring*, the country's first and largest leasing company (Zgheib, 2019). Factoring is therefore an important source of finance for SMEs.

Two companies (*Tunisie Factoring* and Unifactor) control the market in Tunisia which was a total of TND 451.1 million (352 USD million) at end 2008 with 83.2 percent domestic factoring (World Bank, 2009). Today, a total of 5 participating companies generated an industry volume of 338 million euros. The leading factoring companies are *Tunisie Factoring*, *Union de factoring (UNIFACTOR)*, *Med Factor*, and *Attijariwafa bank Factoring* but data on their market share is not readily available.

The level of awareness and acceptance of factoring is considered as 'medium' and the level of demand is positive (FCI, 2020b). The World Bank in 2008 noted several challenges including contract enforcement difficulties, difficulty of obtaining information on credit histories and payment records of companies, and the absence of a specific legal framework (World Bank, 2009). These challenges remain as demonstrated by the recent World Bank Doing Business reports (World Bank, 2020).

## Other Countries

There is evidence from various literature that small sized factoring companies are emerging across the continent. Egypt, Morocco, Nigeria, Mauritius, Cameroon, Zimbabwe, Botswana, and the Republic of Congo, joined FCI in 2018 (Awani, 2019) but data is not readily available on all the countries. Only data on Egypt, Mauritius, Morocco, South Africa, and Tunisia are available (see FCI, 2020c), hence, factoring activities in Africa is likely to be slightly different from what is reported in the FCI database. The lack of statistics in many African countries<sup>1</sup> where factoring is at its infancy stage is a major challenge in tracking the progress and development of factoring. Some information captured on factoring activities in Zimbabwe and Senegal from recent panel interviews/discussions on the growth of factoring are shown in Boxes 1 and 2.

**Box 1: Some information about factoring in Zimbabwe**

According to Tamba (2020), CEO, Harare Receivables Exchange in Zimbabwe, factoring was introduced in 1990's in Zimbabwe with two companies which subsequently closed down due to hyperinflation. Factoring is gradually emerging again but there is a negative perception or skepticism in approaching buyers. Education of buyers and dealing with third parties remains a problem as buyers do not recognize third parties. Buyer education through focus groups is therefore considered very important to access larger multinationals/companies. Policy inconsistencies is cited as another major challenge as government monetary review affected hard currency facilities. There are other challenges relating to competition from the banks and transaction cost of 2-4% incurred by factoring companies who are not exempted from certain tax that banks are exempted from. The future of factoring is digital and there is a need to leverage that. There is also a need to look at innovation and guarantees to be given to import factors. A platform has been launched for the receivables market which all banks and factors can participate in with central register and centralized payment for buyers.

**Box 2: Some information about factoring in Senegal**

According to Ba (2020), CEO, Locafrique in Senegal, factoring services are offered by all banks to support businesses. Factoring is good to support SMEs by providing funding through buying invoices from government to address issues of late payment. There are challenges with taxation based on common law but there are ongoing discussions with the central bank to have a uniform law. If taxation is high, factoring as a product cannot move forward. There is a problem with double taxation as using the common law results in high taxation as selling your debt will involve paying VAT and an additional 1% tax. Recent measures by Government includes initiatives aimed at facilitating consultation between factoring companies and the central bank on how to deal with the issue of taxation. The Factoring law is not yet in place but there is a law passed in the National Assembly to facilitate factoring. However, problems of taxation affected the price of the product which is currently too high.

#### 4.4 Understanding the drivers and barriers affecting factoring in Africa

**Key drivers stimulating growth of factoring.** There are several drivers stimulating the growth of factoring in Africa which includes demand for funding for SMEs, innovation, and digital transformation.

##### *Demand and major source of funding for SMEs as drivers of economic growth*

Key drivers in South Africa are the positive attitudes toward factoring, with the industry continuously providing an excellent source of funding to emerging SMEs. In Egypt, the key drivers identified as fostering the growth of factoring industry are support from policy makers who are committed to develop factoring to stimulate the country's SMEs as growth engine; and the expected growth of exports, with the increased prevalence of the small supplier that has a large buyer (BCR, 2019). FCI also indicated the level of demand as positive in Mauritius and Tunisia. In Morocco, the growth of SMEs was cited as a key driver (Medias24, 2015; World Bank, 2019) and in Tunisia, it is also mainly driven by SMEs given the structure of the economy and their needs for financing; as well as the need for Tunisian companies to be supported in the international development agenda, particularly in non-traditional markets (Finance & Vous, 2012).

##### *Innovation and scope for expanding domestic, international, and reverse factoring which can be enhanced through automation, simplification of functions/processes and involvement of fintech companies*

There are significant opportunities in international factoring given the need for exports and imports to increase intra-African trade as part of the AfCFTA. The share of international factoring (compared to domestic factoring) is currently very low in leading African countries with Egypt at 21.22%, South Africa (17.3%), Morocco (4.27%), Tunisia (3.85%), and Mauritius (1.3%). New forms of factoring products are emerging particularly reverse factoring (supply chain finance) in South Africa (Cory, 2020), but are considered more suitable for medium to large strong creditworthy companies as it allows them to manage payables to thousands of suppliers (Rambaccussing, 2020). Innovation in factoring products can be enhanced by technology. Given

<sup>1</sup> Examples of countries include Cameroon, Côte d'Ivoire, Gabon, Ghana, Kenya, Mauritania, Mozambique, Nigeria, Senegal, Tanzania, Botswana, Zambia, and Zimbabwe.

the increasing use of technology new factoring products such as reverse factoring can be delivered 100% on-line through a secure portal or a Mobile App to manage and track all transactions, including viewing of approved invoices (BNP Paribas, 2020a). Cross-border trade will be a key driver for growth in international factoring and reverse factoring will revolutionize regional supply/value chains and stimulate industrialization, adding value and diversifying Africa's products to accelerate the implementation of the AfCFTA.

### *Digital solutions to automate and simplify functions including customer interfaces, documentation processes and analytics*

In South Africa, key drivers cited are the availability and use of internationally supplied software, robotics, and artificial intelligence (AI) to automate and simplify functions where appropriate (BCR, 2019). For Mauritius, the main drivers for the development of factoring industry include innovativeness and offering of digital solutions, supporting customer interfaces, documentation processes and analytics (BCR, 2019). In Morocco, some of the drivers supporting the growth of factoring market are the availability and easy accessibility of internet and digital solutions (Medias24, 2015; World Bank, 2019). Although technology is recognized as a key driver in South Africa, Mauritius, and Morocco, significant investment in digital capacity building is required in Africa as most African countries lag behind other regions in terms of e-capabilities due to constraints in internet access and enabling infrastructure, computer insecurity, and logistical inefficiencies. Africa is home to 55 countries, 1.25 billion people and GDP of US\$2.5 trillion with the AfCFTA, making it the world's largest free trade area in terms of number of countries, but internet penetration is only 35 percent according to Emergent Payments, a payment platform provider (Kaplan, 2018). Africa therefore has the potential for significant growth in factoring if digital capacity can be built rapidly with new opportunities created for trading and the increased use of digital payment systems expected under the AfCFTA. The Pan-African Payment and Settlement System (PAPSS) launched by Afreximbank to allow payments for goods and services is a key driver for AfCFTA as it intends to be the first digital payment system across the entire continent (Afreximbank, 2019). The developments in technology, particularly the implementation of blockchain technology offer potential for the growth of the factoring market. For instance, the China Construction Bank launched a blockchain-based refactoring platform, focusing on commercial factoring businesses to support their operations, by offering new features in factoring, improvements in efficiency, and cross-chain connectivity. Moreover, BNP Paribas also launched *Mediana*, an e-factoring platform to help create and provide a better digital client experience in handling portfolios safely (Grand View Research, 2020).

**Barriers affecting the development of factoring.** There are significant barriers affecting the development of factoring which includes the following.

### *Lack of familiarity with the concept, visibility, and limited understanding of product range*

Limited understanding, problems with visibility and sensitization to ensure familiarity of the concept, and its benefits are all barriers affecting the development of factoring in Africa. For example, barriers identified in South Africa are the lack of focus and visibility of factoring as very few meetings are arranged by the Debtor Financing Committee. The lack of familiarity with the concept was also identified in Egypt. Limited visibility and understanding of the concept require initiatives for educating more clients (EBRD, 2018; Bourse & Finances, 2018). The need for the education of buyers and dealing with third parties was also highlighted by Tamba (2020) as a problem that persist as buyers do not recognize third parties. Buyer education through focus groups is therefore considered very important to access larger multinationals/companies (Tamba, 2020).

### *Challenging domestic environment, including competition from banks and limited number of factoring companies impacting negatively on factoring volume and factoring GDP penetration*

In Mauritius, the barriers identified relating to the challenging domestic operating environment includes competitive landscape, particularly the strong competition from banks with high liquidity and access to a variety of alternative trade finance solutions (BCR, 2019). Apart from South Africa with over 100 factoring companies, the number of factoring companies are significantly less in the other leading African countries. This ranges from 25 companies in Morocco, 11 in Egypt, 5 in Tunisia and 3 in Mauritius with significantly less factoring volume per company (53.4 million euros per company in Egypt, 53.5 million euros (Mauritius), 67.6 million euros (Tunisia) and 101.3 million euros (Morocco) compared to factoring volume of 190 million euros per company in South Africa. Increasing the number of factoring companies and size of factoring ac-

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tivities focusing on existing gaps in international factoring and emerging products such as reverse factoring to support AfCFTA will therefore have a significant positive impact on factoring volumes and factoring GDP penetration rates in Africa.

*Inadequate legal and regulatory framework such as the absence of factoring law and non-assignment clauses in Government, provincial and municipality as well as mining company contracts.*

The barriers identified in Morocco includes the lack of specific law on factoring, the Banking Law and its implementing circulars providing only the definition of factoring and classifying factoring operations under the category of credit operations (Kameni, 2014). In Tunisia, barriers include the lack of law on factoring or contract law provisions for factoring in the Tunisian Code of Obligations and Contracts (Kameni, 2014). In South Africa, barriers identified includes non-assignment clauses in Government, provincial and municipality as well as mining company contracts, creating obstacles to sellers securing debt finance (BCR, 2019). Recent research carried out in Ghana shows that the enactment of good factoring law will give impetus to convenient access to finance and broaden the scope of facilitation of SMEs and their activities within the factoring enterprise (Korankye-Sakyi, 2019). Similarly, research conducted on factoring as an international trade finance product also advocated for Zambia to enact its own Factoring Act drawing lessons from the Afreximbank Model Law to ensure that SMEs can have enhanced access to financing through factoring to operate at their cutting edge (Hamanyati, 2017). Klapper (2006) noted that the ‘factoring experience in Eastern Europe suggests that factoring business increases as a proportion of GDP following the enactment of laws’ as a legal framework would stipulate what is required in the event of payment default.

*Problems with various taxes levied on factoring companies but not on banks and high cost of transactions relating to interest rates and factoring commissions*

Issues of taxation are critical to the development of factoring. The FCI 2020 Africa Chapter Workshop held on 3 December 2020 shows that other factors impeding the development of factoring include the tax implications as in Senegal and Zimbabwe. For example, in Senegal, there is a problem of double taxation whilst in Zimbabwe, factoring companies are not exempted from certain taxes which banks are exempted from (Ba, 2020 and Tamba, 2020). Other barriers included the high transaction costs, cost of factoring commissions given the lack of competition, value added taxes on the activities and interest rates (Finance & Vous, 2012; EBRD, 2018).

*Inadequate insurance schemes to support factoring due to limited number of credit insurers and lack of adequate credit information system*

Factoring requires good quality information on credit and payment history of the beneficiary enterprises and a lack of such information significantly increase the credit risks to factoring companies (World Bank, 2009). Factoring is a useful vehicle to provide credit protection services to African SMEs (Awani, 2020) but limited access to creditworthiness information of potential clients is key constraint (Oramah and Dzene, 2014; BCR, 2019). Lack of adequate financial information, and information asymmetry between SMEs and financial institutions, is the most cited reason for the existence and development of factoring. SMEs are considered opaque which explains the credit rationing behavior of classical banks in financing them (cited in Hachimi, Salahddine and Housni, 2017). The extent of credit risk borne by banks is closely linked to the quality of the information available to make lending decisions. The exclusion of risky borrowers is done through credit rationing rather than by rising borrowing rates (Stiglitz and Weiss, 1981) which therefore limits access to credit for SMEs. There is a lack of adequate credit insurance schemes to deal with factoring and to provide solutions (Afreximbank and FCI, 2020). The availability of credit insurance remains a major obstacle to factoring due to inadequate insurance companies. For example, there is only one major insurance provider in Mauritius with 75% market share (Rambaccussing, 2020).

*Policy environment characterised by policy inconsistencies and lack of data on factoring activities for evidence-based policy-making and tracking progress*

The policy environment is a key barrier affecting the development and use of factoring in Africa. Although bills on Movable Property Security interests enacted in 2017 impacted positively in factoring business during 2018 in Zimbabwe (Awani, 2019), policy inconsistency was cited as a major challenge as the Government of Zimbabwe Monetary Reviews affect hard currency facilities (Tamba, 2020). In the case of Nigeria, Afrex-



imbank and Nigeria Export and Import Bank (NEXIM) engaged the Central Bank of Nigeria (CBN) to advocate for a favorable regulatory environment including regulatory guidelines for factors as well as foreign exchange guidelines for open account mode of payment (Awani, 2019). The literature also shows that there is a lack of data on other countries apart from five countries - Egypt, Mauritius, Morocco, South African and Tunisia as most data is provided by FCI, which is an industry group with only members reporting on factoring transactions (FCI, 2020c). Support from regulatory bodies such as central banks and Ministries of Finance to provide activity/research reports on factoring and increasing country memberships in factoring international bodies or associations will facilitate the collection of data to inform progress, and the development of appropriate policies to support the uptake of factoring.

## 5. Key Capacity Challenges in the Development of Factoring in Africa

The drivers and barriers of factoring discussed in the previous section can also be classified based on environmental, organizational, and technological contexts (Gopal, Patil, Shibin and Prakash, 2018) as summarized in Table 19.

**Table 19.** Drivers (+) and Barriers (-) of factoring in Africa

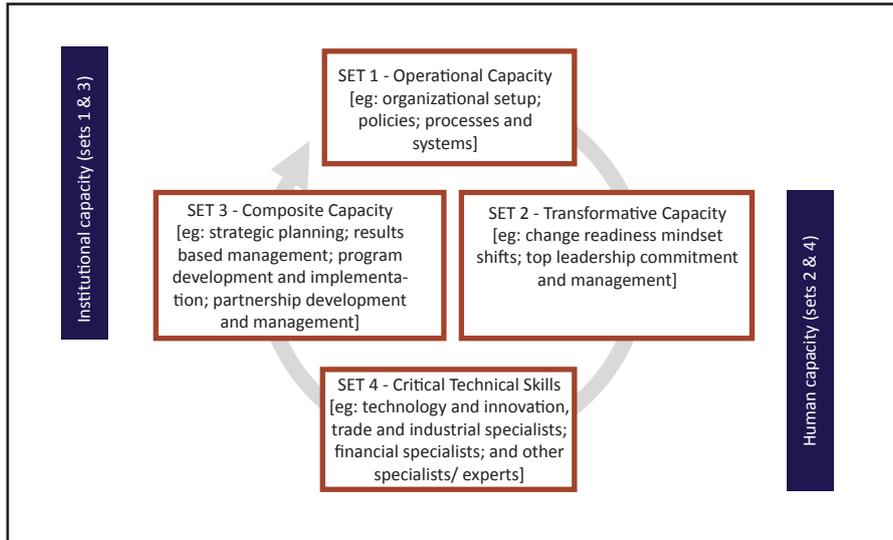
|                               |   |
|-------------------------------|---|
| <b>Environmental context</b>  | <p>(-) inadequate legal and regulatory framework such as the absence of factoring law and non-assignment clauses in Government, provincial and municipality as well as mining contracts.</p> <p>(-) the policy environment characterised by policy inconsistencies, lack of data on factoring activities for evidence-based policy-making and to track progress</p> <p>(-) problems with various taxes levied on factoring companies but not on banks and high cost of transactions relating to interest rates and factoring commissions</p> <p>(+) demand and source of funding for SMEs as drivers of economic growth</p> |
| <b>Organisational context</b> | <p>(-) lack of familiarity with the concept and visibility, limited understanding of product range</p> <p>(-) challenging domestic environment in certain regions due to competition from banks with limited factoring companies impacting negatively on factoring volume and GDP penetration</p> <p>(-) inadequate coverage from insurance schemes to support factoring due to lack of adequate credit information systems and limited credit insurers</p>   |
| <b>Technological context</b>  | <p>(+) innovation and scope for expanding domestic, international, and reverse factoring which can be enhanced through automation, simplification of functions/processes and involvement of fintech companies</p> <p>(+) digital solutions to automate and simplify functions including customer interfaces, documentation processes and analytics</p>  |

*Source: Authors' compilation based on literature*

### 5.1 Framework for analyzing capacity issues and gaps

To better understand the capacity issues and gaps in developing factoring in Africa, the ACBF holistic framework (Figure 6) clustered into four main categories is a useful starting point (ACBF and AUC, 2016). There are two dimensions with sets of capacities to consider – institutional (relating to operational and composite capacities) and human capital (relating to critical technical skills and transformative leadership skills). Each barrier/driver identified in Table 19 has an institutional and/or human capacity dimension. For example, *inadequate legal and regulatory framework* at the environmental level means that there is a need for systems review focusing on institutional capacity development, whether they are organisational set-up, policies, processes, strategic planning, and partnerships to support factoring. Responding to the barrier, *limited factoring companies impacting negatively on factoring volume and GDP penetration* at organisational level will require human capacity development interventions focusing on business development, entrepreneurship, and product and process innovation to support existing, new, and emerging factoring companies.

**Figure 6.** Capacity framework for the development of factoring in Africa



Source: Adapted from ACBF and AUC (2016)

## 5.2 Key capacity development challenges

Building strong institutions (institutional capacity) and skilled people (human capacity) will facilitate the development and use of factoring in Africa.

### Institutional dimension

The study shows that some of the key barriers have an institutional dimension which focuses on operational and composite capacities as shown in Figure 6. Unfortunately, many African countries have weak public institutions which continues to hamper development (Nnadozie, 2016).

#### *Building operational capacity*

Building operational capacity to address gaps in factoring, includes, for example, putting in place legal and regulatory framework such as adopting specific factoring law to regulate the practice, organizational set-up to modernize factoring companies to ensure adequate administrative rules, regulations, and standards, digital policies, and infrastructure to facilitate cross-border trade. Building institutional capacity is also required to ensure uniform policies and processes to deal with tax issues and high transaction costs disproportionately affecting factoring companies and creating an enabling operating environment to support the growth of factoring. Building operational capacity is also critical to address other barriers such as improving the policy environment, domestic operating environment through effective coordination and participation of all actors – legislators, regulators including Ministries of Finance and Central Banks, Commercial Banks, Non-Bank-Financial- Institutions (NBFIs), Fintech companies, factoring associations, buyers including large companies and multinationals. Engaging central banks, other regulators, factoring companies, and SMEs is essential in developing effective policies and streamlining compliance processes. Fostering partnerships between Commercial Banks, Non-Bank-Financial- Institutions (NBFIs), Fintech companies and factoring associations will strengthen institutional arrangements relating to mandate, responsibilities, and coordination to increase the availability of trade finance – as a source of funding for SMEs to build the export capacity of SMEs and to stimulate economic growth.

#### *Building composite capacity*

Strategic planning, program development and partnerships are critical in building composite capacity. African Export-Import Bank (Afreximbank) continues to put emphasis on making factoring a strategic priority by developing and supporting various initiatives (Awani, 2020). For example, Afreximbank is working with FCI to enable the promotion and effective use of factoring across Africa. The African Export-Import Bank (Afreximbank) Model Law on Factoring provides a benchmark for African national legislatures in enacting arrange-

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ments aimed at fostering the growth of factoring activities across the continent (Afreximbank, 2016; BCR, 2017; TRALAC, 2018). The adoption of the Model Factoring Law in Egypt increased awareness in the private sector which led to a noticeable growth from two (2) to twelve (12) factoring companies in the last three years (Shaheen, 2020). To increase the use of factoring as an alternative system for financing SMEs, African countries need to adopt the Model Law of Factoring to regulate the practice and application of the activity. Besides the lack of adequate legal frameworks in some countries, there is need to update existing regulations that are obsolete and contract clauses likely to adversely impact on factoring – such as the continued use of stamp duty tax, foreign currency restrictions and laws impacting the rights of assignment. Countries such as Nigeria have already taken steps in passing legislation using the Model Law as guide (BCR, 2019). There is a need to build different type of partnerships for the growth of international factoring (import factors, export factors), domestic factoring and reverse factoring through cooperation rather than competition from banks to support the growth of SMEs. Building supporting networks for business development at the organizational level through FCI, local factoring associations, SMEs, and engagement with larger companies and multinationals is also important to increase understanding of the concept of factoring and its visibility, and product range. This will address significant gaps in the market by expanding domestic and international factoring as well as reverse factoring. Similar measures at the organizational level will be required to develop credit information systems and to increase the availability credit insurers working with key stakeholder to expand the provision of insurance schemes.

### **Human capacity dimension**

The human capacity dimension of the ACBF framework comprises the critical technical and transformative leadership skills.

#### *Building critical technical skills*

Critical technical skills focus on the required number and quality of technical expertise in the public sector as well as for non-state actors (factoring associations, private sector, SMEs) in areas such as trade law, finance, and related areas to support the development of factoring, particularly in responding to gaps in international factoring and reverse factoring. Significant training including skills development is required to address gaps in factoring companies to boost trade finance and the export capacity of SMEs to increase intra-African trade central to the objectives of AfCFTA. Equally important is the need for skills development programs for other stakeholders such as regulatory bodies, legislators, buyers, private sector, and civil society on specific areas for supply chain specialists, trade economists, trade law specialists, financial advisors/experts, risk assessors (including credit risks and insurance experts) to support the development of credit information systems, increase the number of credit insurers and expand the availability of insurance schemes. Building critical technical skills in the technological context to support factoring companies, SMEs, the growth of fintech companies will speed up digital solutions. Digital skills will be required to automate and simplify functions including customer interfaces, documentation processes and analytics which will be a key driver for the growth of factoring under the AfCFTA. Enhancing skills for exploiting innovations and strengthening entrepreneurship to support the growth of SMEs and factoring companies is necessary to stimulate intra-African trade and contribute to creating jobs particularly for youths and women entrepreneurs.

#### *Building transformative leadership skills*

Transformative leadership remains critical in harnessing the opportunities involved in supporting the promotion and application of the factoring. There is therefore a need for African countries to address the leadership capacity gaps to promote factoring. While the Afreximbank with support from FCI and the FCI's African Chapter, is playing a key leadership role in promoting factoring, there is need for top level commitment from the African Union Commission (AUC), and Regional Economic Communities (RECs) and in all countries and across all sectors (political, businesses, civil society, traditional, community groups, etc.) to take on the responsibility to act as champions to promote factoring in their respective countries. Transformative leadership is required for a better understanding of the factoring concept and visibility, knowledge of the product range (e.g., domestic, international, and reverse factoring) through 'buyer education' to transform the mindsets of larger companies and multinationals to support SMEs and to achieve the objectives of intra-African trade. Appointing champions in factoring will assist in translating the needs and aspirations into prudent and implementable policies and instruments to support service delivery (Ayee 2017; ACBF 2019). Factoring champions should be well informed about how factoring can contribute to the objectives of AfCFTA as an integral component of Agenda 2063 and UN SDG 2030. Such an approach will ensure that

factoring is embedded in national, regional, and continental agenda to support the socio-economic transformation of Africa.

### **Issues of data, research, knowledge sharing and policy advocacy**

Data availability, a research agenda, knowledge sharing, policy dialogues and advocacy are critical building blocks to support institution building and skills development, to engage policy-makers and other stakeholders on the benefits of factoring to increase uptake of factoring as an alternative trade finance solution to accelerate the implementation of AfCFTA.

#### *Addressing data issues*

Data remains a major challenge in tracking the progress in factoring as well as to inform the development of evidence-based policies to support the growth of factoring. Encouraging countries to take up membership with the international factoring bodies such as FCI that regularly publish factoring volume data will be an important step to address the lack of data in Africa. Given that factoring is a US\$3 trillion industry, there is a need to for coordinated efforts by African Governments to engage stakeholders including regulators such as central banks, commercial banks, Non-Bank-Financial-Institutions (NBFIs), statistical agencies, factoring associations so that adequate data is captured and published to inform the development of the factoring market.

#### *Setting a research agenda*

Factoring is an under-researched subject in the African context (Tomusange, 2015) which is reflected in the limited data available only on certain countries. This has implications on the level of awareness, acceptance, and attitudes towards factoring as well as its utilization, in most African countries. Research evidence is needed to inform policy makers, legislators, and other stakeholders on the current state of factoring in various countries and the potential benefits that will accrue from the widespread application or greater use of factoring as a tool for trade finance to support the AfCFTA. Knowledge and analysis of data on Africa is critical to assist countries in coming up with country-specific strategies and home-grown solutions on factoring to promote its application to accelerate the implementation of AfCFTA. A research agenda is essential to develop a critical mass of researchers to engage with policy-makers and other stakeholders to ensure that relevant research is carried out with buy-in and commitment from continental and national leadership. Africa is short of an estimated 1,170,000 researchers, which is projected to be about 1,405,300 by 2023 (ACBF and AUC, 2016). To ensure that a research agenda is driven by Africa, the capacity of African research institutions and think tanks should be strengthened to be able to engage with policy-makers to influence public policies on all aspects of factoring as a trade finance tool for SMEs for the implementation of AfCFTA.

#### *Knowledge sharing, policy dialogues and advocacy*

The knowledge sharing themes should focus on interventions to help raise awareness of the benefits of factoring to all stakeholders, addressing pressing challenges that are preventing factoring from being widely applied to support the AfCFTA, such as gaps in institutional, critical technical and transformative leadership skills as well as technological innovations that will support the development of factoring in Africa. For instance, knowledge sharing can focus on priority areas such as (1) barriers affecting the adoption of the Model Law in Factoring, (for example, ACBF, in the framework of its partnership with Afreximbank, is working on the advocacy on the Model Law on Factoring in various African countries through the Pan African Parliament), (2) capacity gaps to increase uptake of factoring, particularly in areas of growing importance such as digital skills for trade, reverse factoring to support supply chain/value chain development in Africa; (2) regular survey of factoring operations with indicators to measure the development and use of domestic, international and reverse factoring in Africa; (3) construction of database to inform stakeholders on progress and policy-making on factoring in Africa; (4) potential impact of factoring on AfCFTA and economic growth in African countries; (5) international factoring as a driver for intra-African trade; (6) opportunities of factoring in Africa in particular sectors; and (7) lessons learnt from other regions and best practices on the applications of factoring in Africa. The knowledge sharing platform should provoke discussions from a wide range of stakeholders about factoring in Africa and should be properly funded through the creation of scholarships, research grant and strengthening of policy dialogue platforms such as the Africa Think Tank Network.

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## 6. Conclusion

Factoring provides a solution to address the SME financing gap and would help innovative enterprises to grow and support Africa's structural transformation and facilitate the implementation of AfCFTA. However, Africa's share of the global factoring market which is EUR 3,000 billion a year is extremely low at 0.84% in 2019. The practice of factoring is gradually being developed in Africa, but it is still dominated by a few countries notably Egypt, Mauritius, Morocco, South Africa, and Tunisia. Although factoring is dominated by few countries in Africa it is slowly being adopted in other countries in Africa with several small-sized factoring companies emerging. It is projected that there will be a significant increase in Africa's factoring activities but to realize a faster growth in factoring volume, African countries need a coordinated approach to a capacity development informed by a comprehensive needs assessment with mapping of existing initiatives and gaps. Specific measures to support the development and promotion of factoring should focus on institution building, human capital development to increase both critical technical and transformative leadership skills to change mind-sets and sensitize stakeholders. Data remains a major challenge and must be addressed to track progress and to inform policies for the development of factoring. A research agenda, knowledge sharing, policy dialogues and advocacy is critical to support institution building and skills development, to engage policy-makers and other stakeholders on the benefits of factoring to increase uptake of factoring to accelerate the implementation of AfCFTA.

## 7. Recommendations

The following measures are recommended to increase the development and use of factoring, including international factoring and reverse factoring critical for increasing intra-African trade and supporting the AfCFTA.

**Building strong institutions including the development of adequate regulatory framework to adopt the Afreximbank Model Law on Factoring to promote its wider use and to support African countries to regulate the practice and application of factoring. Priority actions include:**

- Conducting comprehensive needs assessment with mapping of existing initiatives and identifying gaps with specific measures focusing on institution building and coordination to support the development and promotion of factoring.
- Addressing the gaps by building capacity and strengthening key institutions (regulatory bodies, and frontline organizations) dealing with factoring to ensure strong and adequate administrative rules, regulations, and standards, modernization of systems, and the development of a conducive institutional environment to promote factoring.

**Building critical technical and leadership skills by scaling-up existing training, proposing new skills development programs, and establishing 'Factoring Champions' to promote factoring in African countries to stimulate intra-African trade. Priority actions include:**

- Conducting comprehensive needs assessment with mapping of existing initiatives and identifying gaps with specific measures focusing on critical technical and transformative leadership skills to support the development and promotion of factoring.
- Addressing the gaps by building capacity of key actors dealing with factoring – factoring companies, regulatory bodies, legislators, buyers, private sector, and civil society etc. – to ensure that core technical and leadership skills are developed on priority areas to promote factoring.
- Setting up a system led by Afreximbank and its partners for key stakeholders to act as champions

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to promote factoring at the African Union Commission (AUC), and Regional Economic Communities (RECs). On a rotating basis, African governments, businesspeople, and civil society representatives should take on the responsibility to act as champions to promote factoring in their respective countries. Such an approach will ensure that factoring is embedded in national, regional, and continental agenda such as AfCFTA.

**Strengthening data collection systems to inform evidence-based policy-making and track progress developing a research and knowledge sharing agenda to support institution building and skills building to demonstrate the benefits of factoring and to sensitize all stakeholders. Priority actions include:**

- Reviewing and strengthening existing systems for coordinating the collection of data and reporting by institutions/countries involved in factoring to support the development of all aspects of the factoring market.
- Allocating funding to support research institutions, think tanks, communities of practices, to develop a critical mass of researchers and to strengthen Africa Think Tank Network with buy-in and commitment from continental and national leadership.
- Strengthening knowledge network to promote knowledge sharing, policy dialogue and advocacy events focusing on thematic areas to address gaps in institutional, and human capacity including technological innovations, to raise awareness and to demonstrate the benefits of factoring to stakeholders.

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