FINANCING INTERNATIONAL EXPORT TRADE

BY
CHARLES KEREEKS
Central Fidelity Bank, Richmond, Virginia

Many businesses find financing a critical element in their day to day operation, and it is essential for the growth of the business. Frequently, we in the banking industry see that businesses have excellent ideas but no financial means to support their day to day activities. It is more true for businesses involved in international trade, particularly in the export business. A number of different elements have to be considered in the decision-making process to finance an export trading business.

However, even with these additional elements which increases the risk factor in international trade, there are a number of ways available for businesses to finance export transactions. I would like to direct my comments to businesses with annual sales of $100,000 or less. Two elements will be referred to throughout my presentation: pre-export and post-export financing.

In pre-export financing, we are talking about the time period between when the business receives an order from overseas and the merchandise is delivered for shipment to its overseas destination. To finance a pre-export transaction, the resources available to the company can be either internal or external. Internal resources are generated from the day to day activities of the business as cash flow. Most businesses are in the position to generate sufficient cash flow from operations in order to purchase the materials necessary for their manufacturing process and will not require outside sources for working capital purposes.

Business can look outside of its entity for financial resources to provide the necessary cash for the manufacturing process. The borrowing can take two major forms: direct borrowing or induced borrowing.

Under direct borrowing the business receives the necessary working capital from a financial institution in the form of a working capital credit or a one time loan for a specific transaction. All borrowing is based on the financial strength of the company, and if the financial institution is satisfied that the borrower is credit worthy, money will be provided to support the pre-export activity.

In those cases where the borrower is not strong financially, we can find federal and state agencies which can provide some sort of inducement to the financial institutions to make financial resources available to the borrower. Within the international arena, there are three government agencies that will guarantee a loan. The Small Business Administration (SBA) can provide a revolving export line of credit to businesses which can qualify under the criteria as a small business. The Export-Import Bank has a working capital guarantee program which will guarantee the lending institution the credit and provide an inducement for the extension of an export related credit facility. A number of states also have programs to encourage exportation of goods manufactured locally and guaranteed through a state guarantee program which will perform a similar function as the federal agency programs.

In post-export financing, we primarily deal with the situation where the exporter was able to purchase the goods or services and shipment was made to its overseas destination. The U.S. exporter might look to the financial industry for resources in order to shorten their business payments cycle since the international transaction normally takes longer to complete than domestic trade.

Within the element of risk we have to consider two important features: commercial risk and political risk. Commercial risk on the international scene has to consider foreign business practices and the long distance to the overseas buyer. Political risk will entail the economic and political condition created by foreign governments. It is very possible that a foreign buyer is a very strong business entity. However, due to economic policies, the importer's country is unable to generate foreign exchange for its economy. The result is the foreign business has no means to pay for U.S. goods imported into the country. A good example is Mexico and Latin American countries in late 1982.

To get paid in the international market, four alternatives are available: cash payment, open account transactions, documentary collections, and letters of credit transaction. The most significant and commonly used vehicle in international trade is letters of credit. A letter of credit is a guarantee issued by a bank to a beneficiary stating that if the beneficiary will meet all terms and conditions of the letter of credit, the bank will guarantee payment. In most cases, a commercial letter of credit is the only way a U.S. exporter is willing to sell his products overseas.

There are three ways post-export financing can be handled. In direct borrowing, financial resources will be made available to a company based on their financial strength. Considering the lag time, from the time a shipment is made and payment is received, it is foreseeable that the manufacturer will need to borrow money from a financial institution. Receivable financing is another way a financial institution will make monetary resources available to the borrower. This is a factoring arrangement, and the foreign receivables will support the transaction.

Sometimes an inducement will be necessary to encourage a financial institution to lend money to an exporter for post-export financing. The inducement can take various forms, but the most commonly used vehicles are private insurance companies, foreign credit insurance associations such as the FCIA, Export-Import Bank, and the U.S. Department of Agriculture.

THE ROLE OF THE EXPORT-IMPORT BANK IN EXPORT FINANCING

By
Harold W. Sundstrom
Export-Import Bank of the U.S.

The Export-Import Bank of the United States is a U.S. government agency. It is an independent agency, with five Presidentially appointed directors Eximbank has one mission -- to aid in financing and to facilitate U.S. exports. It was founded in 1934 to stimulate trade during the depression.