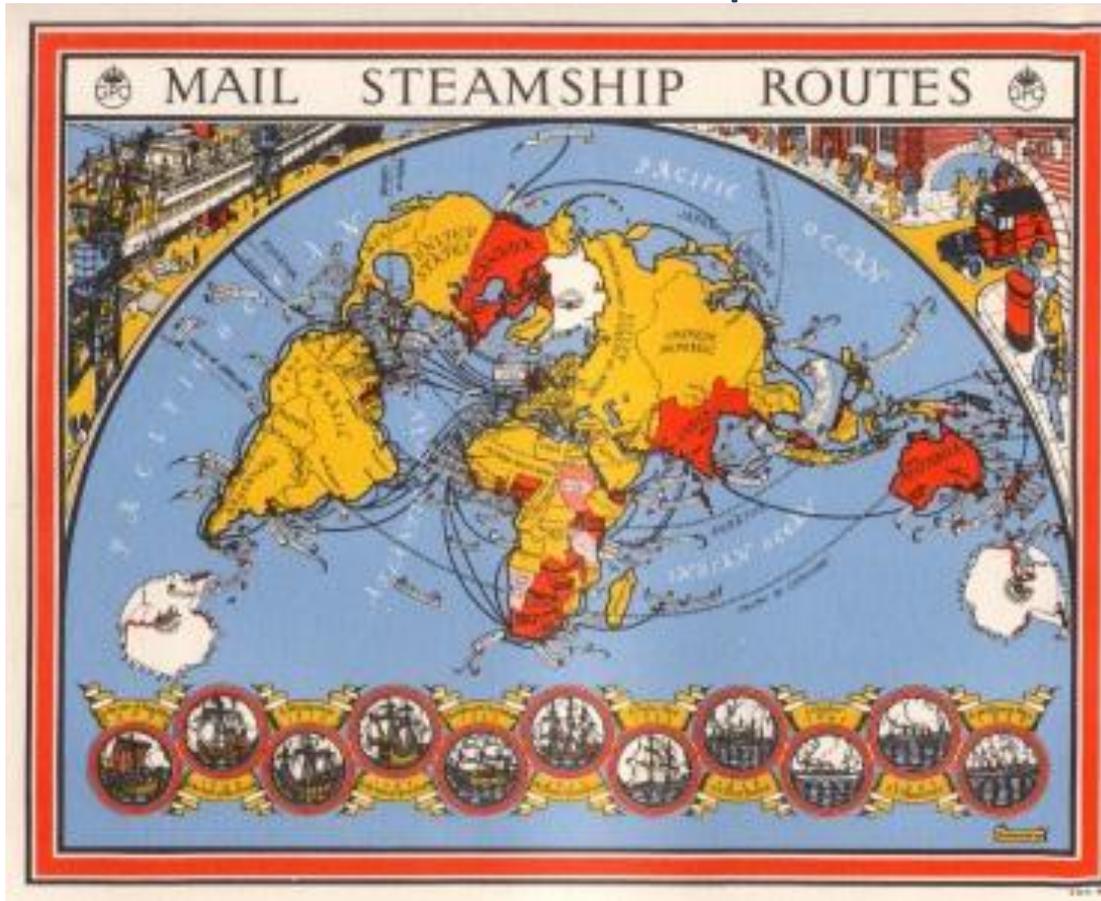


Transacting global business

The role of finance in export success



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Key Allies for Success in Exporting

- **Local international trade partners**
 - US Export Assistance Center (US Dept of Commerce + SBA + ExIm)
 - Center for International Trade Development (CITD)
 - California Dept. of Food & Agriculture/Western US Ag Trade Assn (WUSATA)
- **Federal trade finance program providers** – SBA, Ex-Im Bank
- **Freight Forwarder** – “travel agent” for your export products
- **Export Credit Insurance provider** – export A/R insurance
- **Lender!** – and its international trade department

See handout: [Take Your Exporting to the Next Level](#)



The 1st component of international finance

1. Financing for **the foreign buyer**

- the terms extended to the buyer
- ... while assuring that everyone gets paid

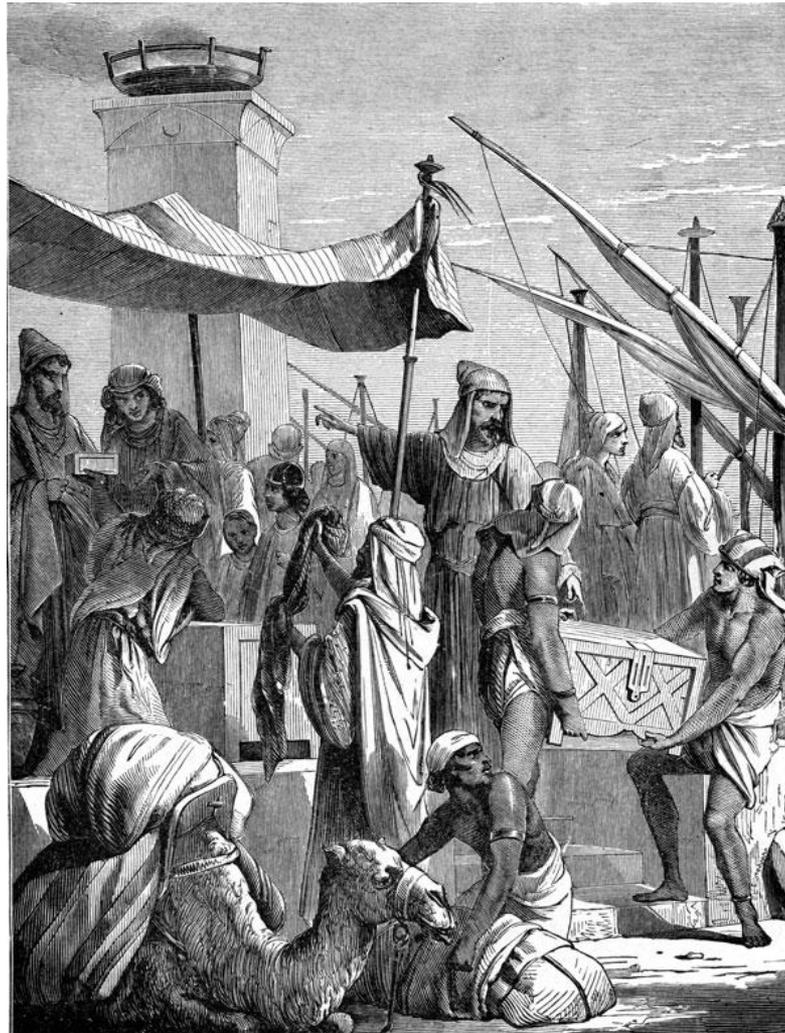
2. Financing for **the exporter's business**

- Positioning the firm for export success
- Fulfilling export orders



Financing for **the foreign buyer**

What will it take to get the deal done?



3 issues in financing the foreign buyer

1. **INCOTERMS** – International Commercial Terms

- EXW; FCA; FOB; FAS; CPT; CIP; CFR; CIF; DAP; DAT; DDP
- How much responsibility will you have for:
 - Transit
 - Insurance
 - Customs clearance

2. **Payment terms**

- How much time will you give the buyer to pay
- How much protection will you require to assure payment

3. **Currency**

- Selling in USD\$ is a solid starting point
- With a strong FX partner, you can use other currencies safely



Terms of Sale? It's a negotiation

There is no “one right way” to structure sales.

- **Exporter is concerned about:**
 - Getting paid at the highest price (in their own currency) as soon as possible
 - BUYER risk
 - BUYER's BANK risk
 - BUYER's COUNTRY risk
- **Foreign buyer is concerned about**
 - Getting the goods at the least price (in their own currency) and postponing payment as long as possible
 - SELLER risk
 - Getting what is ordered
 - Delivery risk



The financing you offer is part of your value proposition

- The **quality** of your product
- + The **cost** of your product
- + The **profit** you need
- + The **delivery** responsibilities you agree to undertake (**INCOTERMS**)
- + The **payment terms** you offer (**Terms of Sale**)
- + The **currency terms** you offer (**Currency**)
- + The **risk mitigation measures** you need
- = The **total cost** of the product to the buyer

... and the competitiveness of your product vs. another

Every exporter should have a range of well-thought-through
export pricing options to negotiate from



1. INCOTERMS

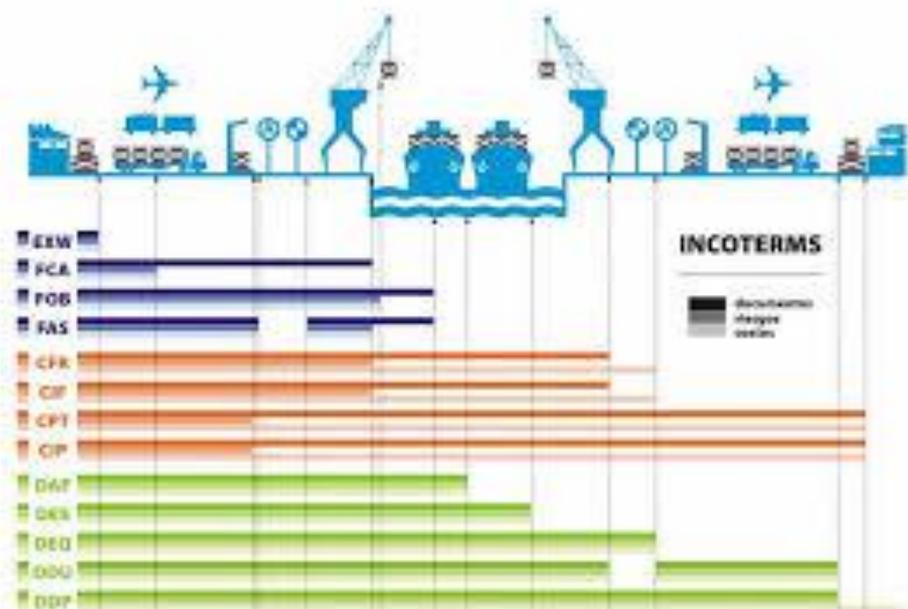
- **INCOTERMS (International Commercial Terms)**

- Globally accepted shorthand for who is responsible for:

- Making arrangements for and paying for **transportation**
- Bearing the risk of damage during transit – **insurance**

- EXW; FCA; FOB; FAS; CPT; CIP; CFR; CIF; DAP; DAT; DDP

- EXW Sacramento, California vs. DDP Casablanca, Morocco



2. Payment Terms

Spectrum of Credit Terms for International Sales

- From lowest risk to highest risk for the exporter;
 - From highest risk to lowest risk for the foreign buyer:
1. **CASH IN ADVANCE**
 2. * **LETTER OF CREDIT** – about 8% of transactions
 3. * **DOCUMENTARY COLLECTION** – about 3% of transactions
 4. **OPEN ACCOUNT** – majority of transactions

* Techniques that rely on **banks** as intermediaries!

A great, FREE resource: **Trade Finance Guide**
(export.gov/tradefinanceguide)



1. Cash in Advance

- **CASH IN ADVANCE** – get full (or partial) prepayment
 - Lowest risk for seller, but not very competitive
 - A good place to start an exporting relationship
 - Typically only sustainable when exporter has a uniquely desirable product
 - ...or when foreign buyer repayment ability is questionable
 - Places entire cash flow burden on foreign buyer
 - **Wire transfers** (via your bank's SWIFT account) - ideal
 - **Credit cards** – more risk, but can be okay for small transactions; work with bank to understand risk



2. Letter of Credit

1 of 4

- **LETTER OF CREDIT** – get the foreign buyer’s bank (instead of the buyer) to agree to pay you:
 - Have your buyer arrange for their bank to commit to pay you once you present specific shipping documents that prove you’ve fulfilled the order – i.e., the bank issues a Letter of Credit (“L/C”).
- If are concerned about the ability of buyer’s bank (or country) to pay, you can also have your own bank commit to pay you. This is called a “Confirmed L/C”.



- **From the foreign buyer's perspective**
 - Note that an L/C requires the buyer to obtain credit from their bank.
 - Buyer must pay a fee to their bank for the L/C
 - Buyer's Bank will typically require buyer to keep sufficient funds to cover the L/C on deposit in their bank, thus tying up buyer cash
 - Even so, an L/C allows buyer to delay actual payment till exporter has shipped, allaying many seller concerns.



- From the **exporter's** perspective
 - Buyer's bank's willingness to issue L/C is like getting a strong credit report from a savvy local financial player
 - L/C from buyer's bank doesn't protect exporter from "country risk" or risk associated with the buyer's bank.
 - To address this concern, exporter may seek a Confirmed L/C from its own bank. This adds costs for seller, as they must apply to their own bank to secure a confirmation.
 - Small processing fee is charged to seller for the L/C service, and amending any errors in documentation will add to these fees - \$100-\$1,000.



- **Risk?** Cost and complexity.
 - L/C's are safe, but they can get expensive and complicated
 - Requires attention to detail and strict adherence to that detail. You need clear instructions and good systems.
 - **60-80% of L/C transactions have discrepancies!**
 - Though nearly all end up paying, this may require amendments (which adds fees and delays)



3. Documentary Collections

- **DOCUMENTARY COLLECTION** – use the foreign buyer’s bank like an escrow agent:
 - Arrange the shipment so that the buyer’s bank gets the documents necessary to pick up the goods, and the bank only delivers the documents upon payment
- **Risk?** Foreign buyer won’t/can’t pay. Exporter’s recourse is to recover the documents from the buyer’s bank and retrieve the already-shipped goods and look for another buyer
- Works well with ocean-shipped exports where delivery documents provide greatest control over shipment’s release



4. Open Account

1 of 2

- **OPEN ACCOUNT**

- Ship now; get paid later
- Payment in 30, 60, 90, ... days
- Simple and very competitive
- Highest risk for exporter
 - Nevertheless, **70% international sales use this approach**
 - But according to one study, **only 15% of US firms export use it**



- **OPEN ACCOUNT**
 - **Risk?** Foreign buyer can't/won't pay, and the shipment is long gone.
 - **Mitigation?** Underwrite and establish a credit limit based on foreign buyer's strength, conditions, and relationship
 - **Mitigation?** **Export Credit Insurance**



The power of offering Open Account terms

- **Open Account?**

- Low US interest rates vs. high foreign interest rates can mean competitive advantage

<http://www.global-rates.com/interest-rates/central-banks/central-banks.aspx>

- The base interest rate in the **US = 0.25%** vs.

China = 5.35%

Brazil = 13.25%

Mexico = 3.0%

Turkey = 7.5%



3. Currency

- Happily, selling in US\$'s is widely accepted
- But when your price is in US\$'s, recognize that you are shifting currency risk to the foreign buyer and affecting your competitiveness
- You want to remain competitive as US\$ value moves against foreign currency
- Techniques – [see pp. 29-30 in Trade Finance Guide](#)
 - **Netting**
 - **Forward contract (hedge)**
 - **Futures contract**
 - **Currency options**



A few thoughts on the strengthening US Dollar

- **A strong dollar means US exports are more expensive now – how to stay competitive?**
- **Short-term volatility** – Use FX services to mitigate short-term risk in currency movement by pricing in the foreign currency and locking in the exchange rate by buying a forward contract
- **Longer-term trends** – it's important to be committed for the long run – consider price reduction strategies:
 - **Market quality and brand over price** - You lose in a race to the bottom
 - **Add follow-on services, warranties, etc.** – low cost ways to enhance value
 - **Offer open account terms** - remember interest rate differentials!
 - **Price in foreign currency** and lock in the rate with a forward contract (above)
 - **Shift INCOTERMS** – let foreign buyer handle transit & insurance in their currency
 - **Leverage lower energy costs** – will this permit re-pricing?
 - **Negotiate with suppliers** too, especially if any inputs are coming from countries with a devalued currency.
 - Use Treasury services to match any overseas expenses with overseas receipts
 - **Consult with freight forwarder** – are lower shipping costs available? (lower energy costs, extra capacity on certain routes)



So... what terms will you offer to your foreign buyer?

- **It's a negotiation**
 - There is no “one right way” to structure sales.
- **Recognize differences between your customers**
 - Distributors
 - Dealers
 - Retailers
 - First-time buyers
 - One-time buyers



Next... Financing for the Exporter



The 2nd component of international finance

1. Financing for **the foreign buyer**

- the terms extended to the buyer
- ... while assuring that everyone gets paid

2. Financing for **the exporter's business**

- Positioning the firm for export success
- Fulfilling export orders



As US exporters move toward Open Account terms...

Cash in advance...

- means using the foreign buyers funds for your working capital

Open account...

- The exporter needs export working capital financing
- **... an opportunity for business lending!**
- ... backed by SBA and ExIm 90% loan guarantees



Export Finance Assistance



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