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EXPORT FINANCING

*Gary W. Collins**

INTRODUCTION

In any discussion of Caribbean Basin trade or trade with any world area, there must invariably be considered the role of the bank. While there are in excess of 10,000 commercial banks in the United States, less than 300 are significantly involved in any international activities. Of this group, less than half make a significant contribution in the area of trade development, the remainder being essentially concerned with travel services and local customer needs. The majority of "international banks" develop in major trade areas with significant port facilities such as those of Baltimore.

No bank becomes involved in this business with initial intentions of solving the world's financial problems. Instead, it is out of a need to satisfy local customer demands for personal services; buying and selling currency, travellers checks, money transfers, and so forth. Simultaneously, the bank fulfills the need to handle some very basic transaction services with regard to exports or imports. A bank may choose to resign itself to this level of involvement (and many do) or it may actively solicit and develop the export-import business of its area. Consequently, the bank will offer a broader range of services including letters of credit, collections and foreign exchange trading.

Banks, not being charitable organizations, must eventually look to the profitability of all their endeavors. Such goals prompt going beyond the above services (generally necessary but not excessively profitable) to that which banking is all about, *i.e.,* lending money. In international banking this begins with the safest risk possible — financing to governments and banks in economically and politically stable countries. If successful, the banker will move on to more risky loans to LDCs, foreign corporations, and the subject of our meeting, export financing. After eighteen years, this is the point to which the Maryland National Bank has progressed.

ASPECTS OF EXPORT FINANCING

When an exporter approaches his local bank, he will generally have need of several of the services offered by its international department, not the least of which will be advisory discussions. If the company has just

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begun exporting, the need for marketing assistance and trade lead information will be paramount. Potential buyers or agents of a particular product can be located through worldwide relationships with other banks. Other country or regional information such as trading environment, future outlook, history, normal credit terms and payment experience will be of importance and can be provided by the bank from the personal travel experience of its area representatives. Through its network of correspondents, the local bank can obtain credit information on an exporter's potential customers and can provide input so that a rational credit decision can be reached. The bank will make an exporter aware of the alternative payment mechanisms available to him (cash in advance, letter of credit, collection, open account), suggest the necessary protections and discuss details of the services as necessary.

It would appear that the above involves early developmental stages for an exporter and, once in the business, experience eliminates the need for such personal assistance. In point-of-fact the more knowledgeable an exporter becomes the more he realizes there is to learn. The only change is in the increased complexity of the needs and their increased frequency.

No matter the size of a company or its degree of international involvement, financing of one sort or another will amost certainly be a necessity. The needs may be short-term for normal working capital needs (*i.e.,* to buy raw materials, manufacturing cost, etc.) to cover normal buyer credit terms, or for extended periods to cover a buyer's inability to pay within a reasonable period (*i.e.,* sale of capital goods). In providing export financing, a bank has a number of tools at its disposal and many variations to the basic process of lending money. Each is best suited to a particular situation or type of exporter and must be "custom-fit" to the situation. These have varying degrees of safety for the bank and the exporter with various levels of exporter risk retention.

THE EXPORT-IMPORT BANK

Perhaps the most secure transactions available are those involving U.S. government affiliates such as Eximbank. This organization was chartered by Congress to develop methods of promoting U.S. exports. It has done this through programs of credit insurance, guarantees and direct loans. Transactions handled by Eximbank are, for the most part, medium-term in nature and for amounts in excess of $500,000. This generally limits their involvement to sales of "big ticket" capital items such as construction equipment and cranes, and most often only to developing nations. Eximbank has a variety of programs which promote exports each of which is briefly set forth:

1. *Medium-term guarantee programs.* Eximbank will provide to financial institutions, such as banks, a guarantee covering political and commercial risks for the purchase, without recourse, of notes for a supplier's sale in a foreign market of a U.S. product. Such guarantee will provide coverage for up to ninety percent of the amount being financed and can range from 181 days to five years. A bank can then finance the transaction at its lending rate with little risk.

2. *Direct loans, participation credits and financial guarantees.* Eximbank joins with financial institutions on an equal basis to provide loans to a foreign buyer to purchase U.S. goods or services. They also can provide a financial guarantee to the participating bank covering its loan. This type of financing is generally long-term (over five years).

3. *Cooperative finance facilities.* With respect to financing, Eximbank participates with non-U.S. financial institutions by lending them fifty percent of a qualified sale to be used in connection with an equal lending participation by the financial institution.

Any or all of these programs may fit a particular company's needs but this can only be determined in joint discussions by an exporter with Eximbank and the local international bank. Because of the nature and variety of transactions, rules for Eximbank's involvement are often difficult to define. They do, however, emphasize developing nations such as many of those in the topic of discussion and are usually receptive to all reasonable possibilities. While the minimum amount requirements may, at first, seem prohibitive, they usually present little problem. It must be remembered that countries in early development are generally restrictive on imports except in the area of large capital items necessary to the growth of a country. Such purchases generally fall within the Eximbank range. Smaller transactions can be dealt with by one of the other financing methods.

THE OVERSEAS PRIVATE INVESTMENT CORPORATION AND FOREIGN INVESTMENT

In the foreign investment area, OPIC was established as a wholly-owned U.S. government corporation to assume responsibility for private investment incentive programs. OPIC's interpretation of its basic statutory mandate is the encouragement of viable, private U.S. investment plans which are mutually beneficial for the host developing country and the United States. To accomplish these purposes, Congress provided them with several program tools in many ways similar to those of Eximbank:[1]

1. Information can be obtained from the author, International Operations, Maryland National Bank, Baltimore, Maryland.

(1) Insurance of private U.S. investments in LDCs against the risks of inconvertibility, expropriation, war, revolution or insurrection;

(2) Guarantees of private U.S. loans to projects in LDCs (usually from institutional lenders such as insurance companies, pension funds and commercial banks) against commercial and political risks;

(3) Direct dollar loans from the corporation's capital, repayable in dollars or foreign currency loans, to assist in financing private projects in these countries; and

(4) Financing of investment surveys and feasibility studies to develop projects in selected fields and countries, especially small business and agribusiness opportunities.

In either the direct loan or loan guarantee program, lending is transacted at normal commercial interest rates and on commercial terms. Such loans range from five to fifteen years. Financing of this sort is attractive to banks since normal credit terms are applied and a U.S. government guaranty is providing the security. The insurance program will not make financing automatically available but it can be the "added attraction" necessary to convince a bank to finance a particular transaction.

In the normal course of events, banks make accounts receivable financing available domestically and internationally to cover short-term needs. This is very difficult financing to accomplish unless a company is well-known to the bank. This includes not only its own reputation but also that of its foreign buyers. Such lending is short-term, for an agreed upon percentage of receivables (usually fifty to seventy percent) and involves a rate most often two percent or more over prime. Because this type of lending involves a substantial risk for the bank, FCIA (Foreign Credit Insurance Association) insurance is often required as an added protection. The FCIA consists of a group of insurance companies working as the quasi-private arm of Eximbank to protect U.S. exporter insurance against commercial and political risks. Exporters often wrongly assume that such insurance automatically provides financing without risk. While it does protect the bank against essentially all buyer-risks, there are certain instances of exporter fraud or negligence which negate the coverage. Bank error in the handling of documentation and reporting can do likewise. A bank must therefore be very concerned with an exporter's reputation and ability to perform; consequently, the normal corporate credit decision is primary, with FCIA providing only the added incentive.

Some banks have taken an extra step in the process of advancing on receivables by establishing factoring organizations to actually buy an exporter's receivables. While this provides a vehicle to companies whose financial situation does not allow for normal bank financing, it is a rather costly service to obtain.

The last method, I will describe involves the use of banker's acceptances. A bankers acceptance is simply a draft issued by an exporter demanding payment from his importer for merchandise sold on which is placed a bank's guarantee of payment at some designated future date (normally less than 180 days). In most situations, this will take place as a result of an exporter having received a letter of credit under which a claim is being made. An active market exists in these instruments, considered to be "prime bank paper," and thus their salability. Banks will buy such obligations from the holder, deducting interest at a market rate applicable for the day. In many cases, this rate is less than prime and almost always less than any other method available to a borrower.

There are also many additional approaches a bank can take to lending for such purposes. For the most part, all must be tailored programs and are therefore resolved on an individual basis. It is up to the banker to be familiar with the methods which have been described, as well as the exporter's product field and the prevailing environment in other world areas.

A bank's business is the lending of money and in the international area this invariably represents some types of trade financing. Banks such as ours are very much committed to development of their export incentive programs. It is necessary for them, because of the variety of market areas, to be flexible enough to offer programs which fit changing needs.