"Trade Financing & Bank Services"

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Attended Torquay Boys Grammar School graduating in 1958, following which studied at the Plymouth and Devonport Merchant Navy School of Navigation. On graduating as an Officer Cadet served with a major U.K. shipping company for three and a half years with extensive world travel. Commenced banking career in 1961 with Westminster Bank Ltd. which amalgamated with other banks to form National Westminer Bank. Occupied various levels within general banking prior to joining Royal Bank of Canada in Toronto in 1973 occupying various senior managerial positions both in domestic and commercial areas, concentrating on the corporate and commercial levels of business. Joined Barclays Bank of Canada on March 16th, 1987 to occupy the position currently held with concentration on international trade finance in the commercial and corporate sectors of the Bank's Ontario based business.

It would be very difficult to cover in great detail, all of the international trade services which are readily available to importers and exporters.

I will confine my remarks to the general aspects of trade financing, with a heavy emphasis to the exporter selling goods on a short term basis which would include the granting of trade credit up to 365 days. I will also touch upon medium size transactions in the 3 to 5 year range and the types of credit facility which could be tailored to fit a financing need.

The role of the banking system in the export financing process, let alone export credit agencies, does not always appear to have been widely understood by Canadian exporters and there has been an ongoing process in development of the full extent of chartered banks, export financing capabilities and the awareness among our exporters community over the past few years to rectify this. A greater effort has been made by the banking community in working with the Canadian Government and Export Development Corporation to undertake a larger role in the medium and long term financing process, which in recent years had been almost exclusively undertaken by the Crown Corporation.

New and innovative forms of trade financing will be key to market success for many companies vying for international business.

Short Term Trade Finance

As we move closer to a freer trade agreement with the United States of America, Canadian exporters will be presented with increasing opportunities to market their product south of the border. Key to success will be their ability to provide high quality product and service, at competitive costs and in providing better terms than the competition to suit their buyers needs.

Much of the trade undertaken with the U.S.A. is based on open account terms. Short term method e.g. net 30 days, with often discounts of 2% net 10 days being granted. Payment is usually effected by cheque, bank draft, or mail and wire transfers. Financing for this method has in the past been mainly undertaken through domestic bank credit lines. In January 1988, Barclays Bank of Canada launched its new short term trade finance product specifically geared to financing trade between Canada and U.S.A. and other markets of first class risk, for example, the various European, Asian and Australasian countries. The bank will purchase open account receivables for periods of up to 180 days, either on a transaction or a revolving basis. In the latter case, enabling exporters to ship on an ongoing basis during the currency of the credit to the maximum limit established. The limit would be predicated upon the size, frequency of shipment and collection period under each separate export sale. This method is particularly useful to an exporter in freeing up existing bank lines for other working capital needs.

Short term trade financing facilities can be granted on either a RECOURSE - which means that full responsibility of the Canadian exporter for the amount of the transaction will be retained the event of nonpayment for any reason or; on a NON-RECOURSE basis - which means the exporter having sold his receivable, will have passed the risk to the bank. Limited recourse will always be retained, however, in the event of nonpayment by the buyer for reasons of a contractual dispute and in some cases for post maturity interest in the event of late payment and where no predetermined compensatory amount was paid by the exporter to the bank.

What are the benefits of this programme? Certainly these can be demonstrated by:

1. Improves cash flow/working capital
   - credit sale becomes a cash transaction
   - receivable eliminated from the balance sheet
   - operating lines freed for day-to-day needs
2. Improves competitive edge
   - longer term offered to buyer
   - financing available in several currencies
3. Provides fixed rate financing to an exporter
4. Transfers credit risk, currency risk to the bank

Individual transaction amounts can range from a low of US $150M to $1MM or subject to prior agreement, larger amounts. Revolving credit lines can be established to suit and exporters need taking into consideration the amount of the sale contract, frequency of shipment and term. As you can see, this new product is flexible and highly attractive in assisting exporters tapping the lucrative USA market place by offering more extended terms. A point worthy of note, is that unlike margining receivables against normal domestic lines up to 100% financing of the face amount of each commercial invoice purchased under the scheme will enable exporters to take full advantage of increased credit capacity.

Letters Of Credit

Traditionally letters of credit have been used by buyers and sellers of all types of goods and services, including consumer goods, agricultural products and raw materials in financing 01international trade. The major exception, of course, has been the Canada/US trade which I have alluded to earlier.

A letter of credit is an instrument of payment or a written undertaking by a bank given to the seller at the request of the buyer to pay the seller an amount of money within a prescribed time limit, provided that the terms and conditions of the letter of credit are met. In international trade, letters of credit usually fall within the documentary credit nature which calls for a seller to present certain documents listed in the credit, together with the trade draft or bill of exchange in order to obtain payment from the advising bank. Letters of credit are usually used where a buyer and seller do not have a long standing relationship of trust where reliability of delivery and payment are yet to be proven or where the country risk is considered to be high for commercial dealings. In essence the letter of credit substitutes the risk of a buyer for that of a bank in the country of origin. It is usual when requesting a letter of credit in payment for exported goods that an irrevocable letter of credit be opened which means that the instrument cannot be cancelled without the express instructions of the beneficiary, whereas revocable letters of credit can be cancelled and are in effect of little value to an exporter requiring security of payment. In some cases, exporters can ask for the added confirmation of a Canadian bank to the letter of credit which has the effect of removing the risk of the foreign bank with drawings being paid immediately on presentation of documents to the Canadian advising bank.

Similarly as with discounting trade acceptances, commercial invoices, the bank will be quite happy to discount drawings under letters of credit on presentation of shipping documents and subject to the bank being satisfied as to the credit-worthiness of the opening bank and the country of risk.

Medium Term Finance

There are basically three methods under which an exporter can arrange financing through the bank to cover its medium term export sales. These can be defined as follows:

1. Purchase or discount with or without recourse of a series of promissory notes/bills of exchange.
2. Aforfait.
3. Buyer credit.

Export Development Corporation will usually consider providing up to 85% of the Canadian content portion in the medium and longer term via either direct loans and/or guarantees and insuring against commercial and political risks in the buyer's country. I will highlight methods under which the three forms of medium term financing can be undertaken by banks and the Crown Corporation.

Purchase Of Promissory Notes/Rates Of Exchange

The bank will be prepared to purchase on either a recourse or non-recourse basis to the exporter a series of promissory notes which the exporter takes back from the buyer as payment for goods 01and services exported. The notes will usually be expressed in either Canadian or US dollars and will bear a rate of interest. Once purchased or discounted the exporter receives funds and the bank will be reimbursed on payment at maturity of each separate instrument.

Aforfait

This form of financing has been a popular method, particularly in European countries and over the last few years, in North America. Financing ranges from 1 - 5 years which can certainly fit the bill where exporters are looking for fixed rates on a non- recourse basis. It is available in various marketable currencies for example, Deutsche Mark, Swiss Francs, US Dollars, Sterling, Canadian Dollars. What is special about forfaiting is the limited documentation that is required. A quick response/turnaround and indeed the transfer by the exporter to the forfaiter of all the risks as well as the administration and collection concerns. It is a cash for credit trade financing service which has been growing rapidly over the past decade. As with the supplier/credit outline above, the banks will purchase a series of promissory notes which will usually bear the "Aval" or guarantee of an acceptable international bank or government guarantee. In some instances where the name of a highly reputable world-class multi- national corporation is concerned, its name alone can often be considered acceptable. A secondary market exists in Europe for trading of aforfait paper which means that many institutions providing the actual financing can change their portfolios of investments through sale of the paper.

Buyer Credit

While we stipulate that buyer credit falls within the medium term category, long-term financing transactions are also usually concluded under this method. It simply means that a buyer will execute a direct lending agreement with the lending bank and/export credit agencies where appropriate, supported by disbursement, pre-disbursement agreements and a series of promissory notes payable at various maturities. The international lending group agreements are by their very nature, comprehensive recognizing the various legal jurisdictions involved in the separate countries, and costly to the buyers. Forfaiting as opposed to buyer credit has the distinct advantage of being cheaper.

For those of you that are contemplating the export market for the first time, I can only add that your persistence, patience and perseverance in developing your foreign markets will prove in the long term to be most rewarding and beneficial. Many changes have taken place over the last number of years with regard to the growing need for cost competitive and innovative financing methods. The heavy debt crises in the early 1980's lead to many countries having great difficulties in servicing interest on existing debt let alone pay back the principal to the commercial banking sectors and export credit agencies.

Many countries in seeking alternatives opted for counter trade as a continuing method of obtaining goods from the western world. The existence of this trade form has been in being in the Eastern European Block countries for many years with a growing emergence 01to the Far East and South American markets. How would one define counter trade? Well we see it as the potential purchase made conditional upon reciprocal purchase by prospective exporters for third parties acting on their behalf. Counter trade can form a competitive marketing tool in seeking business in untapped markets and enhancing an exporter's opportunity in those more traditional markets which are exploring counter trade in a serious manner, for example, Indonesia. Normally, when we think of counter trade we think of barter transactions. Well, under the auspices of the world counter trade, switch trading, swap trading, counter purchase, compensation deals are undertaken. Let us examine each separately. Barter is a direct exchange of goods with no cash payment, usually in the short term with one contract. Switch Trading comprises the transfer of all or part of a clearing account to third party. The third party uses credit to purchase goods. A Swap Transaction can be exchange of trade commitments between countries to save freight and transportation costs. Counter Purchase usually includes parallel contracts having cash value with a percentage of the contract trading goods. There is usually a reciprocal purchase obligation and contracts are linked with a protocol of intent. Usually the transaction falls within a one to three year term. Compensation, sale of technology or equipment with a commitment to buy back output as in Hydro-Electric projects with take and pay arrangements for electricity output, are contracts in the larger dollar value with medium to long term financing of a project nature being involved. Compensation represents the fastest growing form of counter trade. Industrial Offset - this has been a popular form of countertrade particularly where the award of defence related contracts has been made to foreign suppliers. Often a proviso that manufacturing and supply contracts and transfer of technology coupled with job creation programmes have been key to the purchasing country as part of the agreement, Viz Canada CF18 Programme, McDonnell Douglas Canada, Canadian Patrol Frigate Programme, and the Llad Europe Award.

As stated earlier, there are many reasons why counter trade has become popular in some countries. These can be listed as follows:

- To balance trade deficits
- Minimize usage of hard currency
- Stabilization of production and prices
- Access to new markets for exporters
- Decrease external indebtedness
- Secure long term investment in country

and,

- To accelerate economic development