8 finance

Finance

Securing payment is a vital consideration in any international trade transaction. Remember that an export is a gift until it is paid for.

The risks

It is important to identify the risks that may be faced when trading internationally and to be aware of some of the methods available to reduce these risks. In international trade generally, there are different risks for the seller of goods than for the buyer of goods.

Many of these risks can be insured against or mitigated through the payment mechanism. However, if the exporter reduces his risk then this has the effect of increasing the importer's risk.

Some of the main risks in international trade are:

Country risk

- Political and economic stability.
- Transfer risk/currency controls.
- War and civil disturbance.
- Import/export regulations.

Commercial risk (importer)

- Non-payment of invoices.
- Delayed payment of invoices.
- Insolvency of buyer.

Industry risk

- Demands for particular products.
- Recession in particular industry.
- Competitive products/pricing.
- Fashionable or seasonal goods.

Foreign exchange risk

- Fluctuating exchange rates affect pricing and profit.

Performance risk (exporter)

- Problems in producing correct documentation.
- Failure to supply goods in accordance with the sales contract.

Transportation risk

- Risks associated with the mode of transport, e.g. marine risks.
- Storage facilities in ports.
- Delayed shipment.

The solutions

Four ways to settle international trade debts are: Open Account; Bills for Collection; Documentary Credit; and Advance Payment.

The method of payment that trading partners choose to adopt depends on a number of factors:

- The level of trust.
- Creditworthiness.
- Respective bargaining power.
- Conditions imposed by a third party, e.g. a credit insurer.
- Import/export regulations (in certain countries).
- Financing requirements.
- Custom and practice in the particular country.

Open Account

The Open Account method of payment is probably the most widely used. It saves costs and procedural difficulties, although the risks to the exporter are greater. Conversely, it represents the highest degree of security for an importer.

Trading on Open Account terms implies that the exporter trusts the overseas buyer's business integrity and ability to pay. This could be by having established a long-term relationship with the buyer, through obtaining favourable status reports or credit assessments on the buyer, or it may be that credit insurance provides the confidence to trade on these terms.

Alternatively, market forces may simply dictate that Open Account terms are the only viable option to conduct business.

With Open Account trade, the goods and relevant documents are sent by the exporter directly to the overseas buyer who will have agreed to pay the exporter upon arrival of the documents or within a certain period after the invoice or shipment date. The exporter loses all control of the goods, trusting that payment will be made by the importer in accordance with the original sales contract.

However, an Open Account arrangement is not entirely without risk to the importer. For example, if the importer is committed to producing goods dependent upon receipt of imported materials, or has already 'on-sold' the goods to a third party, losses could occur if the goods or materials fail to arrive on time or are faulty.

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