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INFOCUS

Extending Export Credit Overseas

by **BRIAN GAULER**

Doing due diligence prior to shipping can eliminate much of the risk.

Most discussions about export credit involve a banker. However, marketing managers should have a basic understanding of methods of payment for international orders so they can use export credit as a sales tool.

Methods of Payment

There are four standard methods of payment that all exporters might use at one time or another in their international sales. These include:

- *Cash.* Some form of payment is required upfront. Cash can include wire transfer, credit cards or prepayment by check. This is the most secure payment method for the exporter.
- *Letter of credit.* Banks make the payment to the seller on behalf of the buyer. This is the second most secure type payment for the exporter.
- *Documents against payment.* The buyer is allowed to pay the invoice sometime after shipment of the goods. Banks are involved, but only in the flow of the documents. This method has more risk for the exporter.
- *Open account.* Payment on terms that is often used in the U.S. This carries high risk, even more so than domestic transactions, because the buyer is less accessible.

All of these payment methods can be useful to an exporter. In fact, not only will the exporter often use each of these in different circumstances, in many cases all these methods of payment might be used as part of a payment "evolution" process for each new overseas account. For example, you may start with a new distributor overseas by using letters of credit for the initial orders, then move to less secure documents against payment when you have a working history. Eventually this may lead to open account terms, the same as generally used in the U.S., but with some extension of the due date because of additional shipping time.

Credit Factors

Where does "credit" fit into this picture? And, how can credit be used as a sales tool while minimizing the risk for the seller? U.S. exporters must consider a number of factors when thinking about offering credit.

Two major factors are the cost of money (both for the seller and the buyer) and transit time. Because the distances for international sales are greater than domestic and transit times are extended, whatever the company norm is for domestic sales is generally extended for international sales—usually an additional 30 to 60 days credit.

The cost of money is a definite advantage for U.S. exporters. It's not uncommon for foreign buyers to have finance charges in excess of 20 percent. If a U.S. exporter can provide credit at a lesser rate using the U.S. rates they pay as a base, both parties win. But what about the risk?

One way to provide credit for the buyer while reducing the risk to the seller is for the exporter to use a less secure method of payment, such as a letter of credit, but use a time draft instead of a sight draft for payment. In this way, the exporter reduces the risk of the letter of credit because the time draft is paid at a specific point in time rather than on demand.

This arrangement can be advantageous to the foreign buyer, and result in potential increased sales for the seller. Most overseas accounts will evolve over time, and the foreign buyer will eventually want to eliminate the costs and administrative problems associated with a letter of credit, so exporters should always look for ways to better support foreign transactions.

Credit Information Form

A simple way to get started in the right direction is to use a credit information form when starting with a new account. The form doesn't provide any assurance of payment, but the information can be very helpful in determining what, if any, credit the exporter might consider providing.

A credit information form can be very simple. Often it is just a standard single sheet that requests basic financial information such as bank and credit references. You also can ask for a financial statement, although usually companies are reluctant to provide that information. However, it can't hurt to ask, and financial statements give you valuable information for assessing creditworthiness.

Perhaps the most valuable information you can receive is also generally the easiest to get. Ask the foreign buyer for U.S. companies with whom they have already worked and established a credit history. With that information, you can contact the U.S. companies and learn firsthand about your potential credit customer.

A helpful hint: When you contact the U.S. references, also have your marketing manager talk with the company's marketing manager. You may pick up insight that you can't glean from the credit department. Information doesn't assure creditworthiness, but it goes a long way in helping you sort out those companies you do not want to risk offering credit to.

Extending credit for export orders usually isn't all that clear-cut, unless you are selling to a well-known international firm. But, by doing some due diligence prior to shipping your order, you can eliminate much of the risk. A commonsense approach to offering export credit can provide increased sales benefits to the exporter as well as a restful night's sleep.

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