EXPORT FINANCE

SUBMITTED TO: -

UNIVERSITY OF MUMBAI OCTOBER 2006

Project Guide: Prof. Mr. Umesh

PREFACE

In the light of growing need & importance of exports for our country it is of utmost importance that everyone should have an insight in the field of exports.

In the course of last decade, the export scenario in India has undergone a tremendous change. The liberalization initiated by the government, the keen competition in the market place & the rapid increase in the export of services have all combined to change the picture completely

This project will be covering various aspects of export finance. Areas covered in this project are related to “concept and types of export finance, financial institutions” etc.

I hope that this project would provide one, some essential information that will be useful to in future.

TABLE OF CONTENTS

EXECUTIVE SUMMARY

FINANCE IS THE LIFE AND BLOOD OF ANY BUSINESS. Success or failure of any export order mainly depends upon the finance available to execute the order. Nowadays export finance is gaining great significance in the field of international finance.

Many Nationalized as well as Private Banks are taking measures to help the exporter by providing them pre-shipment and post- shipment finance at subsidized rate of interest. Some of the major financial institutions are EXIM Bank, RBI, and other financial institutions and banks. EXIM India is the major bank in the field of export and import of India. It has introduced various schemes like forfeiting, FREPEC Scheme, etc.

Even Government is taking measures to help the exporters to execute their export orders without any hassles. Government has introduced schemes like Duty Entitlement Pass Book Scheme, Duty free Materials, setting up of Export Promotion Zones and Export Oriented Units, and other scheme promoting export and import in India. Initially the Indian exporter had to face many hurdles for executing an export order, but over the period these hurdles have been removed by the government to smoothen the procedure of export and import in India.

CHAPTER 1 - INTRODUCTION OF EXPORTS

Export in simple words means selling goods abroad. International market being a very wide market, huge quantity of goods can be sold in the form of exports.
Export refers to outflow of goods and services and inflow of foreign exchange.

Export occupies a very prominent place in the list of priorities of the economic set up of developing countries because they contribute largely to foreign exchange pool.

Exports play a crucial role in the economy of the country. In order to maintain healthy balance of trade and foreign exchange reserve. It is necessary to have a sustained and high rate of growth of exports.

Exports are a vehicle of growth and development. They help not only in procuring the latest machinery, equipment and technology but also the goods and services, which are not available indigenously. Exports leads to national self-reliance and reduces dependence on external assistance which howsoever liberal, may not be available without strings.

Though India’s export compared to other countries is very small, but one of the most important aspects of our export is the strong linkages it is forging with the world economy which is a great boon for a developing nation like India.

CHAPTER 2 - EXPORT FINANCE

2.1 - INTRODUCTION

Credit and finance is the life and blood of any business whether domestic or international. It is more important in the case of export transactions due to the prevalence of novel non-price competitive techniques encountered by exporters in various nations to enlarge their share of world markets.

The selling techniques are no longer confined to mere quality; price or delivery schedules of the products but are extended to payment terms offered by exporters. Liberal payment terms usually score over the competitors not only of capital equipment but also of consumer goods.

The payment terms however depend upon the availability of finance to exporters in relation to its quantum, cost and the period at pre-shipment and post-shipment stage.

Production and manufacturing for substantial supplies for exports take time, in case finance is not available to exporter for production. They will not be in a position to book large export order if they don’t have sufficient financial funds. Even merchandise exporters require finance for obtaining products from their suppliers.

This project is an attempt to throw light on the various sources of export finance available to exporters, the schemes implemented by ECGC and EXIM for export promotion and the recent developments in the form of tie-EXIM tie-ups, credit policy announced by RBI in Oct 2001 and TRIMS.

2.2 - CONCEPT OF EXPORT FINANCE:

The exporter may require short term, medium term or long term finance depending upon the types of goods to be exported and the terms of statement offered to overseas buyer.

The short-term finance is required to meet **"working capital"** needs. The working capital is used to meet regular and recurring needs of a business firm. The regular and recurring needs of a business firm refer to purchase of raw material, payment of wages and salaries, expenses like payment of rent, advertising etc.

The exporter may also require **"term finance".** The term finance or term loans, which is required for medium and long term financial needs such as purchase of fixed assets and long term working capital.

Export finance is short-term working capital finance allowed to an exporter. Finance and credit are available not only to help export production but also to sell to overseas customers on credit.

2.3 - OBJECTIVES OF EXPORT FINANCE

- To cover commercial & Non-commercial or political risks attendant on granting credit to a foreign buyer.
- To cover natural risks like an earthquake, floods etc.

An exporter may avail financial assistance from any bank, which considers the ensuing factors:

a) Availability of the funds at the required time to the exporter.
b) Affordability of the cost of funds.

2.4 - APPRAISAL

Appraisal means an approval of an export credit proposal of an exporter. While appraising an export credit proposal as a commercial banker, obligation to the following institutions or regulations needs to be adhered to.

Obligations to the RBI under the Exchange Control Regulations are:

- Appraise to be the bank's customer.
- Appraise should have the Exim code number allotted by the Director General of Foreign Trade.
- Party's name should not appear under the caution list of the RBI.

Obligations to the Trade Control Authority under the EXIM policy are:

- Appraise should have IEC number allotted by the DGFT.
- Goods must be freely exportable i.e. not falling under the negative list. If it falls under the negative list, then a valid license should be there which allows the goods to be exported.
- Country with whom the Appraise wants to trade should not be under trade barrier.

Obligations to ECGC are:

- Verification that Appraise is not under the Specific Approval list (SAL).
- Sanction of Packing Credit Advances.

GUIDELINES FOR BANKS DEALING IN EXPORT FINANCE:

When a commercial bank deals in export finance it is bound by the ensuing guidelines: -

a) Exchange control regulations.
b) Trade control regulations.
c) Reserve Bank's directives issued through IECD.
d) Export Credit Guarantee Corporation guidelines.
e) Guidelines of Foreign Exchange Dealers Association of India.

CHAPTER 3 - TYPES OF EXPORT FINANCE

The export finance is being classified into two types viz.

- Pre-shipment finance.
- Post-shipment finance.

3.1 - PRE-SHIPMENT FINANCE

MEANING:

Pre-shipment is also referred as **"packing credit".** It is working capital finance provided by commercial banks to the exporter prior to shipment of goods. The finance required to meet various expenses before shipment of goods is called pre-shipment finance or packing credit.

DEFINITION:

Financial assistance extended to the exporter from the date of receipt of the export order till the date of shipment is known as pre-shipment credit. Such finance is extended to an exporter for the purpose of procuring raw materials, processing, packing, transporting, warehousing of goods meant for exports.

IMPORTANCE OF FINANCE AT PRE-SHIPMENT STAGE:

- To purchase raw material, and other inputs to manufacture goods.
- To assemble the goods in the case of merchant exporters.
- To store the goods in suitable warehouses till the goods are shipped.
- To pay for packing, marking and labelling of goods.
- To pay for pre-shipment inspection charges.
- To import or purchase from the domestic market heavy machinery and other capital goods to produce export goods.
- To pay for consultancy services.
- To pay for export documentation expenses.

FORMS OR METHODS OF PRE-SHIPMENT FINANCE:

1. **Cash Packing Credit Loan:**

   In this type of credit, the bank normally grants packing credit advantage initially on unsecured basis. Subsequently, the bank may ask for security.

2. **Advance Against Hypothecation:**

   Packing credit is given to process the goods for export. The advance is given against security and the security remains in the possession of the exporter. The exporter is required to execute the hypothecation deed in favour of the bank.

3. **Advance Against Pledge:**

   The bank provides packing credit against security. The security remains in the possession of the bank. On collection of export proceeds, the bank makes necessary entries in the packing credit account of the exporter.

4. **Advance Against Red L/C:**

   The Red L/C received from the importer authorizes the local bank to grant advances to exporter to meet working capital requirements relating to processing of goods for exports. The issuing bank stands as a guarantor for packing credit.

5. **Advance Against Back-To-Back L/C:**

   The merchant exporter who is in possession of the original L/C may request his bankers to issue Back-To-Back L/C against the security of original L/C in favour of the sub-supplier. The sub-supplier thus gets the Back-To-Bank L/C on the basis of which he can obtain packing credit.

6. **Advance Against Exports Through Export Houses:**

   Manufacturer, who exports through export houses or other agencies can obtain packing credit, provided such manufacturer submits an undertaking from the export houses that they have not or will not avail of packing credit against the same transaction.

7. **<u>Advance Against Duty Draw Back (DBK)</u>:**

DBK means refund of customs duties paid on the import of raw materials, components, parts and packing materials used in the export production. It also includes a refund of central excise duties paid on indigenous materials. Banks offer pre-shipment as well as post-shipment advance against claims for DBK.

8. **<u>Special Pre-Shipment Finance Schemes</u>:**

- Exim-Bank's scheme for grant for **Foreign Currency Pre-Shipment Credit (FCPC)** to exporters.
- Packing credit for **Deemed exports.**

SOME SCHEMES IN PRE-SHIPMENT STAGE OF FINANCE

1. PACKING CREDIT

SANCTION OF PACKING CREDIT ADVANCES:

There are certain factors, which should be considered while sanctioning the packing credit advances viz.

i. Banks may relax norms for debt-equity ratio, margins etc but no compromise in respect of viability of the proposal and integrity of the borrower.
ii. Satisfaction about the capacity of the execution of the orders within the stipulated time and the management of the export business.
iii. Quantum of finance.
iv. Standing of credit opening bank if the exports are covered under letters of credit.
v. Regulations, political and financial conditions of the buyer's country.

DISBURSEMENT OF PACKING CREDIT:

After proper sanctioning of credit limits, the disbursing branch should ensure:
To inform ECGC the details of limit sanctioned in the prescribed format within 30 days from the date of sanction.

a) To complete proper documentation and compliance of the terms of sanction i.e. creation of mortgage etc.
b) There should be an export order or a letter of credit produced by the exporter on the basis of which disbursements are normally allowed.

In both the cases following particulars are to be verified:

i. Name of the Buyer.
ii. Commodity to be exported.
iii. Quantity.
iv. Value.
v. Date of Shipment / Negotiation.
vi. Any other terms to be complied with.

2. FOREIGN CURRENCY PRE-SHIPMENT CREDIT (FCPC)

- The FCPC is available to exporting companies as well as commercial banks for lending to the former.
- It is an additional window to rupee packing credit scheme & available to cover both the domestic i.e. indigenous & imported inputs. The exporter has two options to avail him of export finance.
- To avail him of pre-shipment credit in rupees & then the post shipment credit either in rupees or in foreign currency denominated credit or discounting /rediscounting of export bills.
- To avail of pre-shipment credit in foreign currency & discounting/rediscounting of the export bills in foreign currency.
- FCPC will also be available both to the supplier EOU/EPZ unit and the receiver EOU/EPZ unit.

Pre-shipment credit in foreign currency shall also be available on exports to **ACU (Asian Clearing Union)** countries with effect **from 1.1.1996.**

Eligibility: PCFC is extended only on the basis of confirmed /firms export orders or confirmed L/C's. The "Running account facility will not be available under the scheme. However, the facility of the liquidation of packing credit under the first in first out method will be allowed.

Order or L/C : Banks should not insist on submission of export order or L/C for every disbursement of pre-shipment credit , from exporters with consistently good track record. Instead, a system of periodical submission of a statement of L/C's or export orders in hand, should be introduced.

Sharing of FCPC: Banks may extend FCPC to the manufacturer also on the basis of the disclaimer from the export order.

2.2 - POST-SHIPMENT FINANCE

MEANING:

Post shipment finance is provided to meet working capital requirements after the actual shipment of goods. It bridges the financial gap between the date of shipment and actual receipt of payment from overseas buyer thereof. Whereas the finance provided after shipment of goods is called post-shipment finance.

DEFENITION:

Credit facility extended to an exporter from the date of shipment of goods till the realization of the export proceeds is called Post-shipment Credit.

IMPORTANCE OF FINANCE AT POST-SHIPMENT STAGE:

- To pay to agents/distributors and others for their services.
- To pay for publicity and advertising in the over seas markets.
- To pay for port authorities, customs and shipping agents charges.
- To pay towards export duty or tax, if any.
- To pay towards ECGC premium.
- To pay for freight and other shipping expenses.
- To pay towards marine insurance premium, under CIF contracts.
- To meet expenses in respect of after sale service.
- To pay towards such expenses regarding participation in exhibitions and trade fairs in India and abroad.
- To pay for representatives abroad in connection with their stay board.

FORMS/METHODS OF POST SHIPMENT FINANCE

1. **Export bills negotiated under L/C:**
   The exporter can claim post-shipment finance by drawing bills or drafts under L/C. The bank insists on necessary documents as stated in the L/C. if all documents are in order, the bank negotiates the bill and advance is granted to the exporter.

2. **Purchase of export bills drawn under confirmed contracts:** The banks may sanction advance against purchase or discount of export bills drawn under confirmed contracts. If the L/C is not available as security, the bank is totally dependent upon the credit worthiness of the exporter.

3. **Advance against bills under collection:** In this case, the advance is granted against bills drawn under confirmed export order L/C and which are sent for collection. They are not purchased or discounted by the bank. However, this form is not as popular as compared to advance purchase or discounting of bills.

4. **Advance against claims of Duty Drawback (DBK):** DBK means refund of customs duties paid on the import of raw materials, components, parts and packing materials used in the export production. It also includes a refund of central excise duties paid on indigenous materials. Banks offer pre-shipment as well as post-shipment advance against claims for DBK.

5. **Advance against goods sent on Consignment basis:** The bank may grant post-shipment finance against goods sent on consignment basis.

6. **Advance against Undrawn Balance of Bills:** There are cases where bills are not drawn to the full invoice value of gods. Certain amount is undrawn balance which is due for payment after adjustments due to difference in rates, weight, quality etc. banks offer advance against such undrawn balances subject to a maximum of 5% of the value of export and an undertaking is obtained to surrender balance proceeds to the bank.

7. **Advance against Deemed Exports:** Specified sales or supplies in India are considered as exports and termed as **"deemed exports".** It includes sales to foreign tourists during their stay in India and supplies made in India to IBRD/ IDA/ ADB aided projects. Credit is offered for a maximum of 30 days.

8. **Advance against Retention Money:** In respect of certain export capital goods and project exports, the importer retains a part of cost goods/ services towards guarantee of performance or completion of project. Banks advance against retention money, which is payable within one year from date of shipment.

9. **Advance against Deferred payments:** In case of capital goods exports, the exporter receives the amount from the importer in installments spread over a period of time. The commercial bank together with EXIM bank do offer advances at concessional rate of interest for 180 days.

SOME SCHEMES UNDER OPERATION IN PRE-SHIPMENT FINANCE

1. DEFERRED CREDIT

Meaning:

Consumer goods are normally sold on short term credit, normally for a period upto 180 days. However, there are cases, especially, in the case of export of capital goods and technological services; the credit period may extend beyond 180 days. Such exports were longer credit terms (beyond 180 days) is allowed by the exporter is called as **"deferred credit"** or **"deferred payment terms".**

How the payment is received?

The payment of goods sold on **"deferred payment terms"** is received partly by way of advance or down payment, and the balance being payable in installments spread over a period of time.

Period of financial credit support:

Financial institutions extend credit for goods sold on "deferred payment terms" (subject to approval from RBI, if required). The credit extended for financing such deferred payment exports is known as Medium Term and Long Term Credit. The medium credit facilities are provided by the commercial banks together with EXIM Bank for a period upto 5 years. The long term credit is offered normally between 5 yrs to 12 yrs, and it is provided by EXIM Bank.

Amount of credit support:

Any loan upto Rs.10crore for financing export of capital goods on deferred payment terms is sanctioned by the commercial bank which can refinance itself from Exim bank. In case of contracts above Rs.10 Lakhs but not more than Rs50crore, the EXIM Bank has the authority to decide whether export finance could be provided. Contracts above Rs.50crore need the clearance from the working group on Export Finance.

2. REDISCOUNTING OF EXPORT BILLS ABROAD (EBRD) SCHEME:

The exporter has the option of availing of export credit at the post-shipment stage either in rupee or in foreign currency under the rediscounting of export bills abroad (EBRD) scheme at LIBOR linked interest rates.

This facility will be an additional window available to exporter along with the exiting rupee financing schemes to an exporter at post shipment stage. This facility will be available in all convertible currencies. This scheme will cover export bills upto 180 days from the date of shipment (inclusive of normal transit period and grace period) .

The scheme envisages ADs rediscounting the export bills in overseas markets by making arrangements with an overseas agency/ bank by way of a line of credit or banker's acceptance facility or any other similar facility at rates linked to **London Inter Bank Offered Rate** (LIBOR) for six months.

Prior permission of RBI will not be required for arranging the rediscounting facility abroad so long as the spread for rediscounting facility abroad does not exceed one percent over the six months LIBOR in the case of rediscounting 'with recourse' basis & 1.5% in the case of 'without recourse' facility. Spread, should be exclusive of any withholding tax. In all other cases, the RBI's permission will be needed.

3. FINANCE FOR RUPEE EXPENDITURE FOR PROJECT EXPORT CONTRACTS (FREPEC)

1. What is FREPEC Program?

This program seeks to Finance Rupee Expenditure for Project Export Contracts, incurred by Indian companies.

2. What is the purpose of this Credit?

To enable Indian project exporters to meet Rupee expenditure incurred/required to be incurred for execution of overseas project export contracts such as for acquisition/purchase/acquisition of materials and equipment, acquisition of personnel, payments to be made in India to staff, sub-contractors, consultants and to meet project related overheads in Indian Rupees.

3. Who are eligible for Assistance under FREPEC Program?

Indian project exporters who are to execute project export contracts overseas secure on cash payment terms or those funded by multilateral agencies will be eligible. The purpose of the new lending program is to give boost to project export efforts of companies with good track record and sound financials.

4. What is the quantum of credit extended under this program?

Up to 100% of the peak deficit as reflected in the Rupee cash flow statement prepared for the project. Exim Bank will not normally take up cases involving credit requirement below Rs. 50 lakhs. Although, no maximum amount of credit is being proposed, while approving overall credit limit, credit-worthiness of the exporter-borrower would be taken into account. Where feasible, credit may be extended in participation with sponsoring commercial banks.

5. How are Disbursements made under this Program?

Disbursements will made in Rupees through a bank account of the borrower-company against documentary evidence of expenditure incurred accompanied by a certificate of Chartered Accountants.

6. How is a FREPEC Loan to be extinguished?

Repayment of credit would normally be out of project receipts. Period of repayment would depend upon the project cash flow statements, but will not exceed 4 (four) years from the effective date of project export contract. The liability of the borrower to repay the credit and pay interest and other monies will be absolute and will not be dependent upon actual realization of project bills.

7. What is the security stipulated for FREPEC loan?

Hypothecation of project receivables and project movables.

Optional: where available

- Personal Guarantees of Directors of the Company.
- Available collateral security.

CHAPTER 4 - LETTER OF CREDIT

INTRODUCTION:

This is one of the most popular and more secured of method of payment in recent times as compared to other methods of payment. A L/C refers to the documents representing the goods and not the goods themselves. Banks are not in the business of examining the goods on behalf of the customers. Typical documents, which are required includes commercial invoice, transport document such as Bill of lading or Airway bill, an insurance documents etc. L/C deals in documents and not goods.

DEFINITION:

A Letter of Credit can be defined as **"an undertaking by importer's bank stating that payment will be made to the exporter if the required documents are presented to the bank within the validity of the L/C".**

PARTIES INVOLVED IN LETTER OF CREDIT:

Applicant:	The buyer or importer of goods__
Issuing bank:	Importer's bank, who issues the L/C
Beneficiary:	The party to whom the L/C is addressed. The Seller or supplier of goods.
Advising bank:	Issuing bank's branch or correspondent bank in The exporter's country to whom the L/C is send for Onward transmission to the beneficiary.
Confirming bank:	The bank in beneficiary's country, which Guarantees the credit on the request of the issuing Bank.
Negotiating bank:	The bank to whom the beneficiary presents his Documents for payment under L/C

A Letter of Credit contains these elements:

- A payment undertaking given by the bank (issuing bank) on behalf of the buyer (applicant)
- To pay a seller (beneficiary) a given amount of money on presentation of specified documents representing the supply of goods within specific time limits
- These documents conforming to terms and conditions set out in the letter of credit
- Documents to be presented at a specified place.

In simple words, the Issuing Bank's role is twofold:

- To guarantee to the seller that if complete documents are presented, the bank will pay the seller the amount due. This offers security to the seller – the bank says in effect "We will pay you if you present documents (XYZ)"
- To examine the documents and only pay if these comply with the terms and conditions set out in the letter of credit. This protects the buyer's interests - the bank says "We will only pay your supplier on your behalf if they present documents (XYZ) that you have asked for"

ADVANTAGES OF LETTER OF CREDIT

ADVANTAGES TO THE EXPORTER:

- No blocking of funds.
- Clearance of import regulations.
- Free from liability.
- Pre- shipment finance.
- Non-refusal by importer.
- Reduction in bad-debts.

ADVANTAGES TO THE IMPORTER:

- Better terms of trade.
- Assurance of shipment of goods.
- Overdraft facility.
- No blocking of funds.
- Delivery on time.
- Better relations.

DISADVANTAGES OF LETTER OF CREDIT:

- Lacks flexibility.
- Complex method
- Expensive for importer
- Problem of revocable L/C

Sample Document: Letter of Credit (Documentary Credit)

THE MOON BANK
INTERNATIONAL OPERATIONS
5 MOONLIGHT BLVD.,
EXPORT-CITY AND POSTAL CODE
EXPORT-COUNTRY

OUR ADVICE NO.	**ISSUING BANK REF. NO. & DATE**
MB-5432	SBRE-777 January 26, 2005

To,
UVW Exports
88 Prosperity Street East, Suite 707
Export-City and Postal Code
Dear Sirs:

We have been requested by The Sun Bank, Sunlight City, Import-Country to advise that they have opened with us their irrevocable documentary credit number SB-87654
For account of DEF Imports, 7 Sunshine Street, Sunlight City, Import-Country in your favor for the amount of not exceeding Twenty Five Thousand U.S. Dollars (US$25,000.00) available by your draft(s) drawn on us at sight for full invoice value

Accompanied by the following documents:

1. Signed commercial invoice in five (5) copies indicating the buyer's Purchase Order No. DEF-101 dated January 10, 2005

2. Packing list in five (5) copies.

3. . Full set 3/3 clean on board ocean bill of lading, plus two (2) non-negotiable copies, issued to order of The Sun Bank, Sunlight City, Import-Country, notify the above accountee, marked "freight Prepaid", dated latest March 19, 2005, and showing documentary credit number.

4. Insurance policy in duplicate for 110% CIF value covering Institute Cargo Clauses (A), Institute War and Strike Clauses, evidencing that claims are payable in Import-Country.

Covering: 100 Sets 'ABC' Brand Pneumatic Tools, 1/2" drive, complete with hose and quick couplings, CIF Sunny Port

Shipment from:	Moonbeam Port, Export-Country to Sunny Port, Import-Country
Partial shipment	Prohibited
Tran-shipment	Permitted

Special conditions:

1. All documents indicating the Import License No. IP/123456 dated January 18, 2005.
2. All charges outside the Import-Country are on beneficiary's account

Documents must be presented for payment within 15 days after the date of shipment.
Draft(s) drawn under this credit must be marked

Drawn under documentary credit No. SB-87654 of The Sun Bank,
Sunlight City, Import-Country, dated January 26, 2005

We confirm this credit and hereby undertake that all drafts drawn under and in conformity with the terms of this credit will be duly honored upon delivery of documents as specified, if presented at this office on or before March 26, 2005

Very truly yours,

Authorized Signature

Unless otherwise expressly stated, this Credit is subject to the Uniform Customs and Practice for Documentary Credits, 1993 Revision, International Chamber of Commerce Publication No. 500.

CHAPTER 5 - SOME IMPORTANT CONCEPTS IN EXPORT FINANCE

5.1 - FORFEITING

Forfeiting is a mechanism of financing exports.

- By discounting export receivables
- Evidenced by bills of exchange or promissory notes
- Without recourse to the seller (viz. exporter)
- Carrying medium to long term maturities
- On a fixed rate basis (discount)
- Upto 100 percent of the contract value.

The word `forfeit' is derived from the French word `a forfeit' which means the surrender of rights.

Simply put, Forfeiting is the non-recourse discounting of export receivables. In a forfeiting transaction, the exporter surrenders, without recourse to him, his rights to claim for payment on goods delivered to an importer, in return for immediate cash payment from a forfeiter. As a result, an exporter in India can convert a credit sale into a cash sale, with no recourse to the exporter or his banker.

CONCEPT OF FORFEITING

1. **What exports are eligible for forfeiting?**

   All exports of capital goods and other goods made on medium to long term credit are eligible to be financed through forfeiting.

2. **How does forfeiting work?**

   Receivables under a deferred payment contract for export of goods, evidenced by bills of exchange or promissory notes, can be forfaited.

   Bills of exchange or promissory notes, backed by co-acceptance from a bank (which would generally be the buyer's bank), are endorsed by the exporter, without recourse, in favour of the forfeiting agency in exchange for discounted cash proceeds. The co-accepting bank must be acceptable to the forfeiting agency.

3. **Is there a prescribed format for the bills of exchange or promissory notes?**

   Yes. The bills of exchange or promissory notes should be in the prescribed format.

4. **What role will Exim Bank play in forfeiting transactions?**

   The role of Exim Bank will be that of a facilitator between the Indian exporter and the overseas forfeiting agency.

5. **How will Exim Bank facilitate a forfeiting transaction?**

   On a request from an exporter, for an export transaction which is eligible to be forfaited, Exim Bank will obtain indicative and firm forfeiting quotes - discount rate, commitment and other fees - from overseas agencies.

   Exim Bank will receive availed bills of exchange or promissory notes, as the case may be, and send them to the forfeiter for discounting and will arrange for the discounted proceeds to be remitted to the Indian exporter.

Exim Bank will issue appropriate certificates to enable Indian exporters to remit commitment fees and other charges.

6. **What does forfeiting cost include?**

A forfeiting transaction has typically three cost elements:

- Commitment fee
- Discount fee
- Documentation fee

7. **What benefits accrue to an exporter from forfeiting?**

Converts a deferred payment export into a cash transaction, improving liquidity and cash flow

Frees the exporter from cross-border political or commercial risks associated with export receivables

Finance up to 100 percent of the export value is possible as compared to 80-85 percent financing available from conventional export credit program

As forfeiting offers without recourse finance to an exporter, it does not impact the exporter's borrowing limits. Thus, forfeiting represents an additional source of funding, contributing to improved liquidity and cash flow

Provides fixed rate finance; hedges against interest and exchange risks arising from deferred export credit

Exporter is freed from credit administration and collection problems

Forfaiting is transaction specific. Consequently, a long term banking relationship with the forfeiter is not necessary to arrange a forfeiting transaction

Exporter saves on insurance costs as forfeiting obviates the need for export credit insurance

5.2 - FACTORING

Factoring may be defined as **"A contract by which the factor is to provide at least two of the services, (finance, the maintenance of accounts, the collection of receivables and protection against credit risks) and the supplier is to assigned to the factor on a continuing basis by way of sale or security, receivables arising from the sale of goods or supply of services".**

Factoring offers smaller companies the instant cash advantage that was once available only to large companies with high sales volumes. With Factoring, there's no need for credit or collection departments, and no need to spend your profits on maintaining accounts receivables.

In simple words...Factoring turns your **receivable into cash today,** instead of waiting to be paid at a future date.

International export Factoring Scheme:

RBI has approved the above scheme evolved by SBI Factors and Commercial Services Pvt. Ltd Mumbai for providing **"International Export Factoring Services"** on **"with recourse"** basis. The salient features of the scheme are as follows:

- An exporter should submit to **SBI Factors & Commercial Services Pvt.Ltd** i.e. the **Export Factor(EF)** a list of Buyers(customers) indicating their names & street addresses and his credit line needs .

- The **Import Factor (IF)** located in the importer's country selected by **EF**, will rate the buyer's list and the results will be reported to the exporter through **EF**. The exporter will apply for a credit limit in respect of overseas importer. **IF** will grant credit line based on the assessment of credit-worthiness of the overseas importer.

- The exporter will thereafter enter into an export factoring agreement with **EF**. All export receivable will be assigned to the **EF**, who in turn will assign them to **IF**.

- The exporter will ship merchandise to approved foreign buyers. Each invoice is made payable to a specific factor in the buyer's (importer) country. Copies of invoices & shipping documents should be sent to **IF** through **EF**. **EF** will make prepayment to the exporter against approved export receivables.

- **EF** will report the transaction in relevant ENC statement detailing full particulars, such as Exporter's Code Number, GR Form Number, Custom Number, Currency, Invoice value etc.

- On receipt of payments from buyers on the due date of invoice, **IF** will remit funds to **EF** who will convert foreign currency remittances into rupees and will transfer proceeds to the exporter after deducting the amount of prepayments, if made. Simultaneously, **EF** will report the transaction in the relative 'R' returns enclosing duplicate copy of the respective GR form duly certified. The payment received will be the net payment after deduction of a service fee, which ranges from 0.5 % to 2% of the value of the invoices.

- If an approved buyer (importer) is unable to pay the proceeds of exports, **IF** will pay the receivables to **EF**, 100 days after the due date. The transactions of this nature will be reported by **EF** in the half yearly statements which are to be submitted to RBI, indicating therein the reasons for delay /non payment.

5.3 - Supplier's Credit for deferred payment exports

Definition of Deferred Payment Exports:

In terms of Regulation 9 of the Foreign Exchange Management Act 1999, the amount representing the full export value of goods exported must be realized and repadriated to India within 6 months of date of export.

Exports where more than 10% of the value is realized beyond the prescribed period, i.e. 6 months from date of shipment, are treated as Deferred Payment Exports

1. **What is an offer?**

⇒ Exim Bank offers Supplier's Credit in Rupees or in Foreign Currency at post-shipment stage to finance export of eligible goods and services on deferred payment terms.

⇒ Supplier's Credit is available both for supply contracts as well as project exports; the latter includes construction, turnkey or consultancy contracts undertaken overseas.

2. **Who can seek finance?**

⇒ Exporters can seek Supplier's Credit in Rupees/ Foreign Currency from Exim Bank in respect of export contracts on deferred payment terms irrespective of value of export contracts.

3. **What are the general terms of Supplier's Credit?**

⇒ **Extent of Supplier's Credit:**
100% of post-shipment credit extended by exporter to overseas buyer.

⇒ **Currency of Credit:**
Supplier's Credit from Exim Bank is available in Indian Rupees or in Foreign Currency.

⇒ **Rate of Interest:**
The rate of interest for Supplier's Credit in Rupees is a fixed rate and is available on request. Supplier's Credit in Foreign Currency is offered by Exim Bank on a floating rate basis at a margin over LIBOR dependent upon cost of funds.

⇒ **Security:** Adequate security by way of acceptable letter of credit and/or guarantee from a bank in the country of import or any third country is necessary, as per RBI guidelines.

⇒ **Period of Credit and Repayment:** Period of credit is determined for each proposal having regard to the value of contract, nature of goods covered, security, competition. Repayment period for Supplier's Credit facility is fixed coinciding with the repayment of post-shipment credit extended by Indian exporter to overseas buyer. However, the Indian exporter will repay the credit to Exim Bank as per agreed repayment schedule, irrespective of whether or not the overseas buyer has paid the Indian exporter.

⇒ **Overseas Buyer's Credit:** Credit is offered directly to overseas buyer for a specific project/ contract.

CHAPTER 6 - MAJOR FINANCIAL AND OTHER INSTITUTIONS

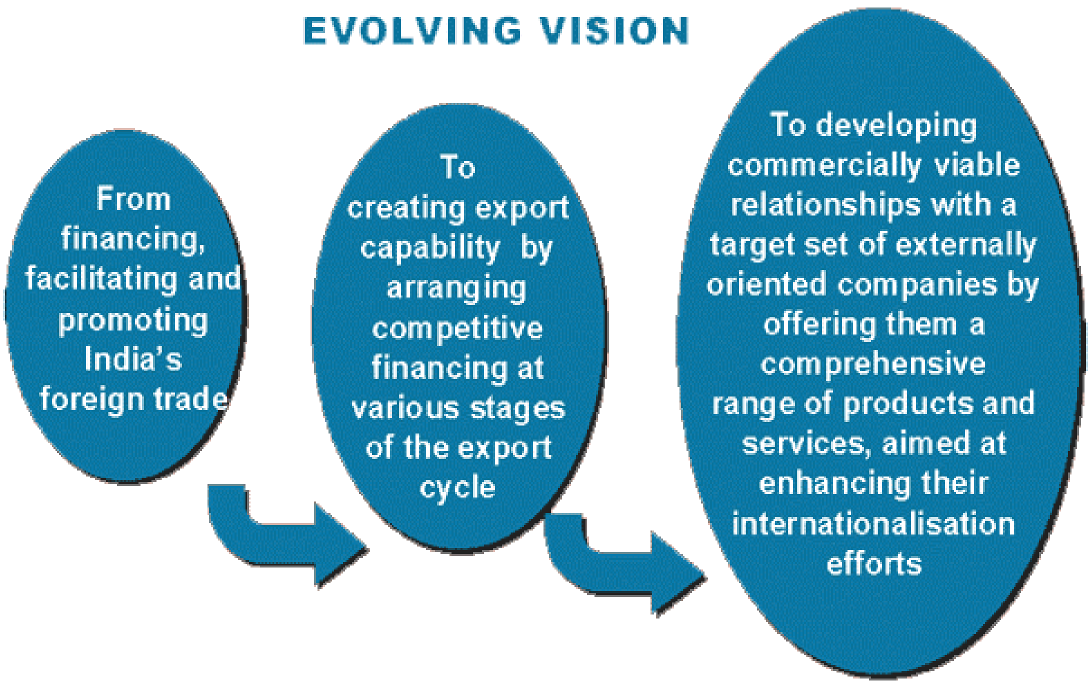
For providing credit and finance and insuring export credit risk, there are 2 primary institutions i.e. EXIM Bank and ECGC.

Although there are other commercial banks, nationalized institutions and private institutions such as IFCI, IDBI, engaged in providing finance to exporter. The major institutions are EXIM Bank, ECGC, and RBI.

6.1 - EXIM BANK

Exim Bank Act-Completed 20 years of operations.

- Set up by an Act of Parliament in September 1981.
- Commenced operations in March 1982.
- Wholly owned by the Government of India.
- Export-Import Bank of India was set up for the purpose of financing, facilitating and promoting foreign trade in India.
- Exim is the principal financial institution in the country for co-ordinating working of institutions engaged in financing exports and imports.



INTRODUCTION

The Export-Import bank of India is the apex institution for project finance, which provides direct finance and coordinates the working of the institution, which is engaged in financing export or import of goods and services. It has taken over the operations of international finance wing of the industrial development bank of India (IDBI). The EXIM bank of India came into existence on 1st January 1982, and started functioning from 1st march 1982. It has it's headquarter in Mumbai and its branches and offices in important cities in India and abroad.

Offices

Head office – Mumbai.

A network of 13 offices in India and Overseas.

Domestic Offices - Ahmedabad, Bangalore, Chennai, Hyderabad, Kolkata, Mumbai, New Delhi, Pune.

Overseas Offices - Budapest, Johannesburg, Milan, Singapore, Washington DC.

PURPOSE

The EXIM bank was established for the purpose of financing medium and long term loan to the exporters thereby promoting foreign trade of India.

MAIN OBJECTIVES

To provide financial assistance (medium and long term) to exporters and importers.

To function as the principal financial institution for coordinating the working of institutions engaged in providing export finance.

To promote Foreign Trade of India.

To deal with all matters that may be considered to be incidental or conducive to the attainment of above objectives.

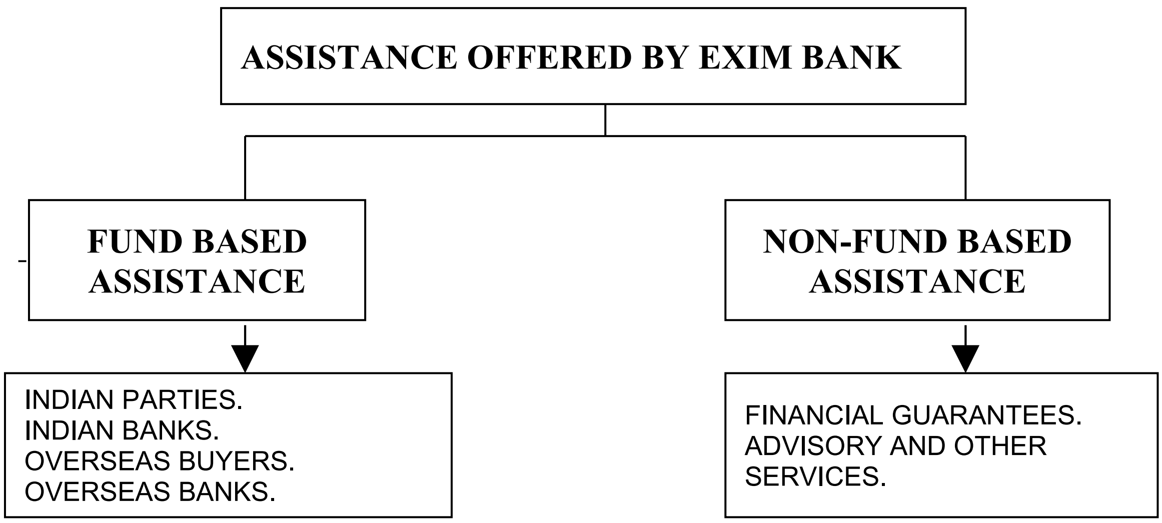
FUNCTIONS

The assistance provided by EXIM Bank to the exporters can be grouped under two heads:

Fund Based Assistance.

Non-Fund based Assistance.

The various assistance provided by EXIM Bank can be charted as follows:



A. FUND BASED ASSISTANCE:

- **Assistance to Indian Exporters:**
  - (a) It provides financial assistance to **"Deferred credit exports".**
  - (b) It offers credit facilities to **"Deemed Exports".**
  - (c) It finances ***"Indian Joint Ventures in Foreign countries".***
  - (d) Finances units in***"EPZ/ SEZ and 100% EOU's".***
  - (e) It provides Pre-shipment finance to exporters for procuring raw materials and other inputs.
  - (f) It finances export/import of machinery and equipment on lease basis.
  - (g) It provides Computer Software exporters foreign exchange loan subject to RBI clearance.
  - (h) It provides finance facility against deferred credit to exporters of consultancy, technology and other services.

(i) It provides finance to Indian exporters to undertake various export marketing activities in India and abroad through Export Marketing Fund (EMF).

(j) It also operates Export Development Fund (EDF) to finance techno-economic survey/research or any other study for the development of Indian Exports.

- **Assistance to Indian Commercial Banks:**

(a) It provides Refinance Facilities so as to Indian exporters who extend term credit to importers.

(b) It offers Export Bills Rediscounting Facility to commercial banks in India who have earlier discounted bills of exporters.

- **Assistance to Overseas Buyers:**

(a) It offers "Overseas Buyer's Credit" facility to foreign importers for import of Indian capital goods and related services with repayment spread over a period of years.

- **Assistance to Overseas Banks:**

(a) Long term finance is also provided under "Lines of Credit" to finance financial institutions abroad, who in turn, extend finance to importers of their country to buy Indian Capital goods.

(b) It provides Relending Facility to overseas Banks to make available term finance to their clients for import of Indian goods.

2. NON-FUND BASED ASSISTANCE

- **Guarantees and Bonds:**

EXIM Bank provides non-fund base assistance in the form of guarantees in the nature of Bid Bonds, Performance Guarantee etc. These guarantees are provided together with Commercial Banks.

- **Advisory and Other Services:**
  - (a) It advises Indian companies, in ***Executing Contracts Abroad***, and on sources of overseas financing.
  - (b) It advises Indian exporters on global exchange control practices.
  - (c) The EXIM Bank offers Financial and ***Advisory Services to Indian construction projects abroad.***
  - (d) It advises ***small-scale manufacturers*** on export markets and product areas.
  - (e) It provides ***Euro Financing*** sources and ***Global Credit*** sources to Indian exporters.
  - (f) It assists the exporters under **Forfeiting scheme**.

FREQUENTLY ASKED QUESTIONS (FAQ's) IN EXIM BANK

1. What is Export-Import Bank of India? What are its objectives?

✓ The Export-Import Bank of India (Exim Bank) is a public sector financial institution created by an Act of Parliament, the Export-import Bank of India Act, 1981. The business of Exim Bank is to finance Indian exports that lead to continuity of foreign exchange for India. The Bank's primary objective is to develop commercially viable relationships with a target set of externally oriented companies by offering them a comprehensive range of products and services, aimed at enhancing their internationalization efforts.

2. What is the place of Exim Bank in the institutional structure for financing developmental needs?

- ✓ There are apex institutions in the country, which deal with major economic activities, viz. industry, agriculture and foreign trade. The Industrial Development Bank of India extends term industrial loans; the National Bank for Agricultural loans; and the Exim Bank extends term loans for foreign trade. All these institutions are wholesale banks. They, therefore work closely with commercial banks and other state level financial institutions that operate the retail banking system in the country.

3. <u>What are the types of services provided by Exim Bank</u>?

- ✓ Exim Bank provides a range of analytical information and export related services. The Bank's fee based services help identify new business propositions, source trade and investment related information, create and enhance presence through joint network of institutional linkages across the globe, and assists externally oriented companies in their quest for excellence and globalization. Services include search for overseas partners, identification of technology suppliers, negotiating alliances, and development of joint ventures in India and abroad. The Bank also supports Indian project exporters and consultants to participate in projects funded by multilateral funding agencies.

4. <u>How does Exim Bank support Indian consultants to secure assignments overseas</u>?

- ✓ Exim Bank encourages Indian consultants to gain and enhance their international exposure by assisting them in securing assignments overseas.
- ✓ Assignments are awarded under programme sponsored by International Finance Corporation (IFC) in Washington to promote private sector development in select countries and regions. Arrangements set in place cover:
  - Africa Project Development Facility
  - African Management Services Company
  - Africa Enterprise Fund
  - South-east Europe Enterprise Development Facility

- Mekong Project Development Facility
- Business Advisory and Technical Assistance Services (BATAS)
- Other Technical Assistance & Trust Funds

Exim Bank assists these agencies in the recruitment of Indian consultants and meets the professional fees of the consultant selected by IFC.

Consultancy assignments undertaken comprise pre-feasibility studies, project and investment related services, management information systems, operations and maintenance support mainly for SMEs in a variety of sectors like agriculture, agro-industry, consumer goods, light engineering, telecom.

5. <u>What are the various types of financial facilities provided by Exim Bank to Indian Companies for export of turnkey/ construction projects, export of services and export of capital/ engineering goods & consumer durables</u>?

✓ Exim Bank provides financial assistance to Indian Companies by way of a variety of lending **Programmes, viz.**

Non-Funded

- Bid Bond
- Advance Payment Guarantee
- Performance Guarantee
- Guarantee for release of Retention Money
- Guarantee for raising Borrowings Overseas
- Other guarantees

Funded

- Pre-shipment Rupee Credit
- Post-shipment Rupee Credit
- Foreign Currency Loan
- Overseas Buyer's Credit
- Lines of Credit
- Loan under FREPEC programme
- Refinance of Export Loans

6. **<u>How is Forfeiting useful as an export financing option? What role does Exim Bank play in a Forfeiting transaction</u>?**

- ✓ Forfeiting is a mechanism of financing exports by discounting export receivables evidenced by bills of exchange/ promissory notes without recourse to the exporter.
- ✓ Exim Bank plays the role of an intermediary for facilitating the forfaiting transaction between the Indian exporter and the overseas forfeiting agency.

7. **<u>What are the various types of financial facilities provided by Exim Bank to Indian Companies for export capability creation</u>?**

- ✓ Exim Bank provides financial assistance to Indian Companies for export capability creation by way of a variety of lending programmes, viz.,
  - Lending Programme for Export Oriented Units
  - Production Equipment Finance Programme
  - Import Finance
  - Export Marketing Finance Programme
  - Lending Programme for Software Training Institutes
  - Programme for Financing Research & Development
  - Programme for Export Facilitation: Port Development
  - Export Vendor Development Lending Programme
  - Foreign Currency Pre-Shipment Credit
  - Working Capital Term Loan Programme for Export Oriented units

8. **<u>What type of financial assistance is extended by Exim Bank in setting up joint ventures</u>?**

- ✓ Assistance is extended to Indian Promoter Companies by way of programmes that address to different requirements of the promoter company in setting up of the joint venture.
  - <u>Overseas Investment Finance Programme</u> for setting up joint ventures and wholly owned subsidiaries abroad.

- Asian Countries Investment Partners (ACIP) Programme for creation of a joint venture in India with East Asian countries, through four facilities that address different stages of a project cycle.

EXPORT FINANCING PROGRAMMES PROVIDED BY EXIM BANK

EXIM INDIA offers a range of financing programs that match the menu of Exim Banks of the industrialized countries. However, the Bank is atypical in the universe of Exim Banks in that it has over the years evolved, so as to anticipate and meet the special needs of a developing country. The Bank provides competitive finance at various stages of the export cycle covering:

EXIM INDIA operates a wide range of financing and promotional programs. The Bank finances exports of Indian machinery, manufactured goods, and consultancy and technology services on deferred payment terms. EXIM INDIA also seeks to co finance projects with global and regional development agencies to assist Indian exporters in their efforts to participate in such overseas projects.

The Bank is involved in promotion of two-way technology transfer through the outward flow of investment in Indian joint ventures overseas and foreign direct investment flow into India. **EXIM INDIA** is also a Partner Institution with European Union and operates European Community Investment Partners' Program (ECIP) for facilitating promotion of joint ventures in India through technical and financial collaboration with medium sized firms of the European Union.

The Export- Import Bank of India (Exim Bank) provides financial assistance to promote Indian exports through direct financial assistance, overseas investment finance, term finance for export production and export development, pre-shipping credit, buyer's credit, lines of credit, relending facility, export bills rediscounting, refinance to commercial banks.

Loans to Indian Entities

- **Deferred payment exports:** Term finance is provided to Indian exporters of eligible goods and services, which enables them to offer deferred credit to overseas buyers. Deferred credit can also cover Indian consultancy, technology and other services. Commercial banks participate in this program directly or under risk syndication arrangements.

- **Pre-shipment credit:** finance is available form Exim Bank for companies executing export contracts involving cycle time exceeding six months. The facility also enables provision of rupee mobilization expenses for construction/turnkey project exporters.

- **Term loans for export production:** Exim Bank provides term loans/deferred payment guarantees to 100% export-oriented units, units in free trade zones and computer software exporters. In collaboration with International Finance Corporation. Washington, Exim Bank provides loans to enable small and medium enterprises upgrade export production capability. Facilities for deeded exports; Deemed exports are eligible for funded and non- funded facilities from Exim Bank.

- **Overseas Investment finance:** Indian companies establishing joint ventures overseas are provided finance towards their equity contribution in the joint venture.

- **Finance for export marketing:** This program, which is a component of a World Bank loan, helps exporters implement their export market development plans.

Loans to Commercial Banks in India

- **Export Bills Rediscounting:** Commercial Banks in India who are authorized to deal in foreign exchange can rediscount their short term export bills with Exim Banks, for an unexpired usance period of not more than 90 days.

- **Refinance of Export Credit:** Authorized dealers in foreign exchange can obtain from Exim Bank 100% refinance of deferred payment loans extended for export of eligible Indian goods.

- **Guaranteeing of Obligations:**
  Exim Bank participates with commercial banks in India in the issue of guarantees required by Indian companies for the export contracts and for execution of overseas construction and turnkey projects.

Loans to Overseas Entities

- **Overseas Buyer's Credit:** Credit is directly offered to foreign entities for import of eligible goods and related services, on deferred payment.

- **Lines of Credit:** Besides foreign governments, finance is available to foreign financial institutions and government agencies to on-lend in the respective country for import of goods and services from India.

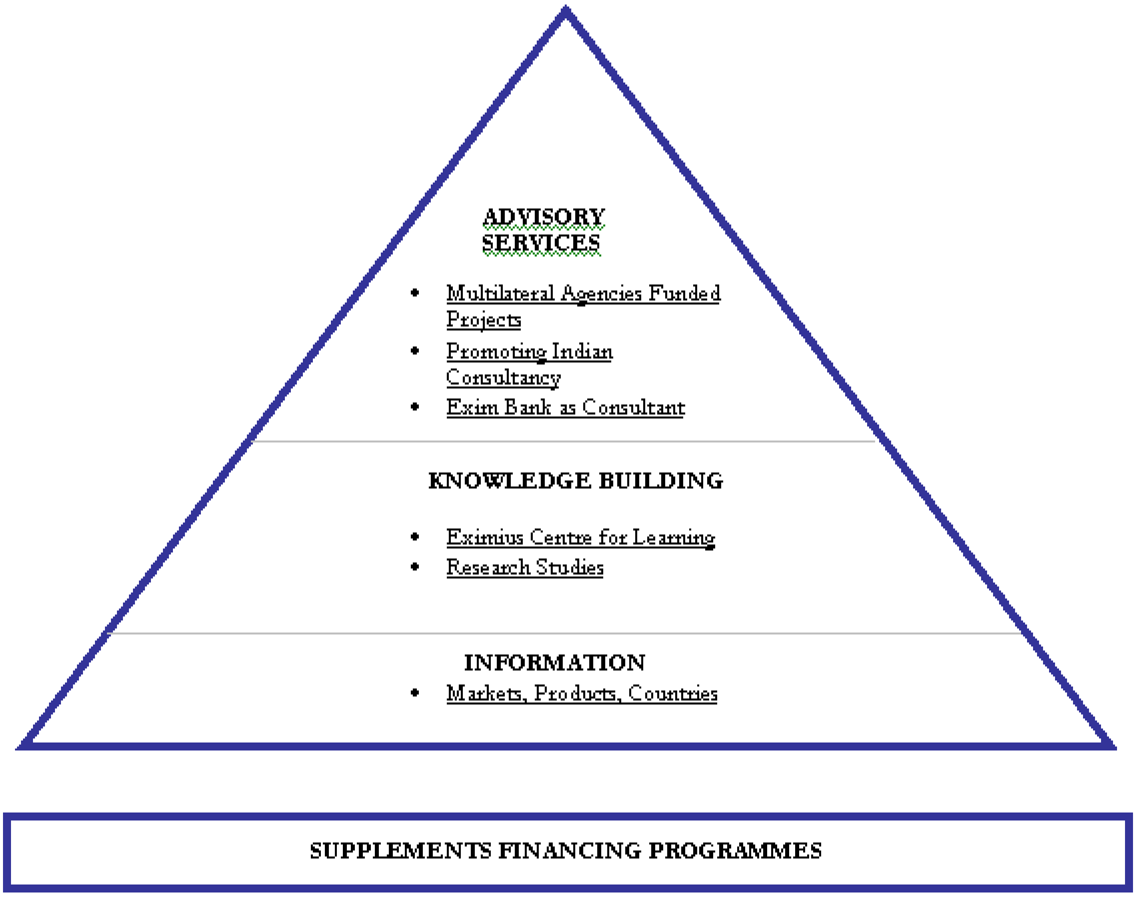
- **Relending Facility to Banks Overseas:** Relending facility is extended to banks overseas to enable them to provide term finance to their client’s worldwide for imports from India.

A RANGE OF EXPORT SERVICES PROVIDED BY EXIM BANK

EXIM INDIA provides a range of analytical information and export related services necessary for globalization of Indian companies. EXIM INDIA through its wide network of alliances with financial institutions, trade promotion agencies, information providers across the globe assists externally oriented Indian companies in their quest for excellence and globalization. Services include search for overseas partners, identification of technology suppliers, negotiating alliances, and development of joint ventures in India and abroad.

EXIM BANK : PARTNERS IN GLOBALISATION

SERVICES



A. ADVISORY SERVICES

I. MULTILATERAL AGENCIES FUNDED PROJECTS OVERSEAS (MFPO)

Services

- ➔ Information and support services to Indian companies to help improve their prospects for securing business in multilateral agencies funded projects.
- ➔ Dissemination of business opportunities in funded projects
- ➔ Providing detailed information on projects of interest

- ➔ Information on Procurement Guidelines, Policies, Practices of
- ➔ Multilateral Agencies
- ➔ Assistance for Registration with Multilateral Agencies
- ➔ Advising Indian companies on preparation of Expression of Interest, Capability Profile.
- ➔ Bid Intervention

II. PROMOTING INDIAN CONSULTANCY

TIE-UP WITH:

- ➔ International Finance Corporation, Washington D.C.
    - Africa Project Development Facility
    - Africa Enterprise Fund
    - Technical Assistance & Trust Funds
    - Mekong Project Development Facility
- ➔ Eastern & Southern African Trade & Development Bank (PTA Bank)
- ➔ African Management Services Company (AMSCO), Netherlands

EXAMPLES

- Gems & Jewellery Study - Zambia
- Financial Training Mission - Kenya
- Cement Project - Cameroon
- Software - Madagascar
- Wool Knitting - Vietnam
- Textile - Nigeria
- Refrigeration - Ghana

- Financial Training - Poland

III. EXIM BANK AS A CONSULTANT

- ➔ Feasibility study for establishment of an export credit and guarantee facility for Gulf Cooperation Council countries.
- ➔ Regional cooperation in export finance and export credit guarantees for ESCAP.
- ➔ Study on promotion of international competitiveness and exports of manufactured goods for ESCAP.
- ➔ Setting up the AFRICAN-EXIM Bank.
- ➔ Designing of Export Financing Programmes - Turkey
- ➔ Setting up an Exim Bank in Malaysia
- ➔ Design of Export Marketing Seminars for SMEs in Vietnam
- ➔ Export Development Project : Ukraine
- ➔ Enterprise Support Fund : Armenia
- ➔ Establishing an Export Credit Guarantee Company in Zimbabwe
- ➔ Advisory services to Industrial Development Corporation of South Africa for international finance products

B. KNOWLEDGE BUILDING

I. EXIMIUS CENTRE FOR LEARNING, BANGALORE

- ➔ Set up, in October 1994, to organize seminars and workshops in areas such as international trade & investment, export marketing, quality, packaging, business opportunities in multilateral agencies funded projects, sector and country specific programmes

- Guest faculty from network partners such as IFC, World Bank, EBRD, UNIDO.
- Number of Programmes Conducted: 53

II. RESEARCH STUDIES

- Research Studies on products, sectors, countries, macro economic issues relevant to international trade and investment
- Number of research studies published as Occasional Papers: 85

INFORMATION

- Exporters/Importers
- Industry/Market Reports
- Trade Regulations & Laws
- Country Reports
- International Quality Standards
- Partner Identification
- Product Display

Examples of Information Services

- Hungarian Pharmaceutical Sector
- Importers of Sanitary ware, Castings in North America
- Importers of Agro-chemicals in Eastern Europe
- Study for ear buds market in Hungary
- Study of the Indian Wine market for a Hungarian Company
- Partner identification for an Italian Sanitary ware manufacturer
- Study of the Indian Crane Industry for a Finnish company
- Regulatory Framework for setting up a Pharma Project in China
- Market report for Computer Monitors in India for a Singaporean firm
- Study on Bicycle market in Eastern Europe for Indian Cycle exporter

- Market Potential for Denim in South East Asia

6.2 - EXPORT CREDIT GUARANTEE CORPORATION OF INDIA LTD.

In order to provide export credit and insurance support to Indian exporters, the GOI set up the Export Risks Insurance Corporation (ERIC) in July, 1957. It was transformed into export credit guarantee corporation limited (ECGC) in 1964. Since 1983, it is now know as ECGC of India Ltd.

ECGC is a company wholly owned by the GOI. It functions under the administrative control of the Ministry of Commerce and is managed by a Board of Directors representing government, Banking, Insurance, Trade and Industry. The ECGC with its headquarters in Bombay and several regional offices is the **only** institution providing insurance cover to Indian exporters against the risk of non-realization of export payments due to occurrence of the commercial and political risks involved in exports on credit terms and by offering guarantees to commercial banks against losses that the bank may suffer in granting advances to exports, in connection with their export transactions.

OBJECTIVES OF ECGC:

➔ To protect the exporters against credit risks, i.e. non-repayment by buyers

➔ To protect the banks against losses due to non-repayment of loans by exporters

COVERS ISSUED BY ECGC:

The covers issued by ECGC can be divided broadly into four groups:

1. **STANDARD POLICIES** – issued to exporters to protect then against payment risks involved in exports on short-term credit.
2. **SPECIFIC POLICIES** – designed to protect Indian firms against payment risk involved in (i) exports on deferred terms of payment (ii) service rendered to foreign parties, and (iii) construction works and turnkey projects undertaken abroad.
3. **FINANCIAL GUARANTEES** – issued to banks in India to protect them from risk of loss involved in their extending financial support to exporters at pre-shipment and post-shipment stages; and

4. **SPECIAL SCHEMES** such as Transfer Guarantee meant to protect banks which add confirmation to letters of credit opened by foreign banks, Insurance cover for Buyer's credit, etc.

(A) <u>STANDARD POLICIES:</u>

ECGC has designed 4 types of standard policies to provide cover for shipments made on short term credit:

1. Shipments (comprehensive risks) Policy – to cover both political and commercial risks from the date of shipment
2. Shipments (political risks) Policy – to cover only political risks from the date of shipment
3. Contracts (comprehensive risks) Policy – to cover both commercial and political risk from the date of contract
4. Contracts (Political risks) Policy – to cover only political risks from the date of contract

RISKS COVERED UNDER THE STANDARD POLICIES:

1. Commercial Risks

➔ Insolvency of the buyer

➔ Buyer's protracted default to pay for goods accepted by him

➔ Buyer's failure to accept goods subject to certain conditions

2. Political risks

➔ Imposition of restrictions on remittances by the government in the buyer's country or any government action which may block or delay payment to exporter.

➔ War, revolution or civil disturbances in the buyer's country. Cancellation of a valid import license or new import licensing restrictions in the buyer's country after the date of shipment or contract, as applicable.

➔ Cancellation of export license or imposition of new export licensing restrictions in India after the date of contract (under contract policy).

➔ Payment of additional handling, transport or insurance charges occasioned by interruption or diversion of voyage that cannot be recovered from the buyer.

➔ Any other cause of loss occurring outside India, not normally insured by commercial insurers and beyond the control of the exporter and / or buyer.

RISKS NOT COVERED UNDER STANDARD POLICIES:

The losses due to the following risks are not covered:

1. Commercial disputes including quality disputes raised by the buyer, unless the exporter obtains a decree from a competent court of law in the buyer's country in his favour, unless the exporter obtains a decree from a competent court of law in the buyers' country in his favour
2. Causes inherent in the nature of the goods.
3. Buyer's failure to obtain import or exchange authorization from authorities in his county
4. Insolvency or default of any agent of the exporter or of the collecting bank.
5. loss or damage to goods which can be covered by commerci8al insurers
6. Exchange fluctuation
7. Discrepancy in documents.

(B). SPECIFIC POLICIES

The standard policy is a whole turnover policy designed to provide a continuing insurance for the regular flow of exporter's shipment of raw materials, consumable durable for which credit period does not normally exceed 180 days.

Contracts for export of capital goods or turnkey projects or construction works or rendering services abroad are not of a repetitive nature. Such transactions are, therefore, insured by ECGC on a case-to-case basis under specific policies.

Specific policies are issued in respect of Supply Contracts (on deferred payment terms), Services Abroad and Construction Work Abroad.

1) **Specific policy for Supply Contracts:**

Specific policy for Supply contracts is issued in case of export of Capital goods sold on deferred credit. It can be of any of the four forms:

- **Specific Shipments (Comprehensive Risks) Policy** to cover both commercial and political risks at the Post-shipment stage.
- **Specific Shipments (Political Risks) Policy** to cover only political risks after shipment stage.
- **Specific Contracts (Comprehensive Risks) Policy** to cover political and commercial risks after contract date.
- **Specific Contracts (Political Risks) Policy** to cover only political risks after contract date.

2) **Service policy:**

Indian firms provide a wide range of services like technical or professional services, hiring or leasing to foreign parties (private or government). Where Indian firms render such services they would be exposed to payment risks similar to those involved in export of goods. Such risks are covered by ECGC under this policy.

If the service contract is with overseas government, then Specific Services (political risks) Policy can be obtained and if the services contract is with overseas private parties then specific services (comprehensive risks) policy can be obtained, especially those contracts not supported by bank guarantees.

Normally, cover is issued on case-to-case basis. The policy **covers 90%of the loss** suffered.

3) **Construction Works Policy:**

This policy covers civil construction jobs as well as turnkey projects involving supplies and services. This policy covers construction contracts both with private and foreign government. This policy covers 85% of loss suffered on account of contracts with government agencies and 75% of loss suffered on account of construction contracts with private parties.

(C). FINANCIAL GUARANTEES

Exporters require adequate financial support from banks to carry out their export contracts. ECGC backs the lending programmes of banks by issuing financial guarantees. The guarantees protect the banks from losses on account of their lending to exporters. Six guarantees have been evolved for this purpose:-

(i). Packing Credit Guarantee

(ii). Export Production Finance Guarantee
(iii). Export Finance Guarantee
(iv). Post Shipment Export Credit Guarantee
(v). Export Performance Guarantee
(vi). Export Finance (Overseas Lending) Guarantee.

These guarantees give protection to banks against losses due to non-payment by exporters on account of their insolvency or default. The ECGC charges a premium for its services that may vary from 5 paise to 7.5 paise per month for Rs. 100/-. The premium charged depends upon the type of guarantee and it is subject to change, if ECGC so desires.

(i) Packing Credit Guarantee: Any loan given to exporter for the manufacture, processing, purchasing or packing of goods meant for export against a firm order of L/C qualifies for this guarantee.

Pre-shipment advances given by banks to firms who enters contracts for export of services or for construction works abroad to meet preliminary expenses are also eligible for cover under this guarantee. ECGC pays two thirds of the loss.

(ii) Export Production Finance Guarantee: this is guarantee enables banks to provide finance at pre-shipment stage to the full extent of the of the domestic cost of production and subject to certain guidelines.

The guarantee under this scheme covers some specified products such a textiles, woolen carpets, ready-made garments, etc and the loss covered is two third.

(iii) Export Finance Guarantee: this guarantee over post-shipment advances granted by banks to exporters against export incentives receivable such as DBK. In case, the exporter Does not repay the loan, then the banks suffer loss? The loss insured is up to three fourths or 75%.

(iv) Post-Shipment Export Credit Guarantee: post shipment finance given to exporters by the banks purchase or discounting of export bills qualifies for this guarantee. Before extending such guarantee, the ECGC makes sure that the exporter has obtained Shipment or Contract Risk Policy. The loss covered under this guarantee is 75%.

(v) Export Performance Guarantee: exporters are often called upon to execute bid bonds supported by a bank guarantee and it the contract is secured by the exporter than he has to

furnish a bank guarantee to foreign parties to ensure due performance or against advance payment or in lieu of or retention money. An export proposition may be frustrated if the exporter's bank is unwilling to issue the guarantee.
This guarantee protects the bank against 75% of the losses that it may suffer on account of guarantee given by it on behalf of exporters.

(vi) Export Finance (Overseas Lending) Guarantee: if a bank financing overseas projects provides a foreign currency loan to the contractor, it can protect itself from risk of non-payment by the con tractor by obtaining this guarantee. The loss covered under this policy is to extent of three fourths (75%).

(D) SPECIAL SCHEMES

A part from providing policies (Standards and Specific) and guarantees, ECGC provides special schemes. These schemes are provided o the banks and to the exporters. The schemes are:

I. **Transfer Guarantee**: the transfer guarantee is provided to safeguard banks in India against losses arising out of risk of confirmation of L/C. the risks can be either political or commercial or both. Loss due to political risks is covered up to 90 % and that due to commercial risks up to 75%.

II. **Insurance Cover for Buyer's Credit and Lines of Credit:** Financial Institutions in India have started direct lending to buyers or financial institutions in developing countries for importing machinery and equipment from India. This sort of financing facilitates immediate payment to exporters and frees them from the problem of credit management.

ECGC has evolved this scheme to protect financial institutions in India which extent export credit to overseas buyers or institutions.

III. **Overseas Investment Insurance:** with the increasing exports of capital goods and turnkey projects from India, the involvement of exporters in capital anticipation in overseas projects has assumed importance. ECGC has evolved this scheme to provide protection for such investment. Normally the insurance cover is for 15 years.

6.3 - RESERVE BANK OF INDIA

INTRODUCTION:

The RBI with its head quarters in Mumbai and several regional offices is the central banks of our country to authorize extend and regulate export credit and transaction including foreign exchange affairs. RBI does not directly provide export finance to the exporters, but it adopts policies and initiates measures to encourage commercial banks and other financial institutions to provide liberal export finance.

The Two Departments of RBI are:

- ✓ Industrial and credit department and
- ✓ Exchange control department

These Departments administers various policies related to export finance/credit and foreign exchange.

SCHEMES OFFERED BY RBI TO ENCOURAGE COMMERCIAL BANKS TO PROVIDE EXPORT CREDIT TO THE EXPORTERS:

- **EXPORT BILLS CREDIT SCHEME, 1963:** Under this scheme, RBI used to grant advance to scheduled banks against export bills maturing within 180 days. Now this scheme is not in operation.

- **PRE-SHIPMENT CREDIT SCHEME, 1969:** Under this scheme, RBI provides re-finance facilities to scheduled banks that provide pre-shipment loans to bonafide customers.

- **EXPORT CREDIT INTEREST SUBSIDIES SCHEME, 1968:** Under this scheme, RBI provides interest subsidies of minimum 1.5 % p.a. to banks, which provide export finance to exporters, provided that the banks charge interest to exporter within the ceiling prescribed by RBI. The subsidies are given both against **packing credit** and **post-shipment.**

- **DUTY DRAW BACK CREDIT SCHEME, 1976:** Under this scheme, the exporters can avail an interest free advances from the bank up to 90 days against shipping bill provisionally certified by the customs authority towards a refund of customs duty. The advances made by commercial banks under this scheme are eligible for re-finance, free of interest from RBI for **maximum period of 90 days** form the date of advance.

Other approves or sanctions of application made by the exporters with RBI

- Extension of time limit for realization of export proceeds.
- Deduction in invoice price of exports goods.
- Fixation of commission to overseas consignee or agents.
- Provision of blanket permit where a lump sum exchange is released for a number of purposes.
- Remittance abroad in respect of advertising, legal expenses etc.
- Any other matters relating to foreign trade that require clearance form the exchange Control department of RBI.
- Clearance in respect of joint venture abroad.

GUIDELINES ISSUED BY RBI under section 47 of THE FEMA, 1999.

Issued by RBI under Sec. 47 of Foreign Exchange Management Act, 1999.

Types of Exports covered:

- Export of Goods on Deferred Payment Terms (e.g. Export of machinery, equipment, manufactured products)
- Turnkey Projects (e.g. Setting up of Sugar Plant, Cement Plant)
- Construction Projects (e.g. Construction of Roads, Dams, Bridges)
- Consultancy & Technical Services (e.g. Operation & Maintenance Contracts) collectively referred to as 'PROJECT & SERVICES EXPORTS'.

TURNKEY, CONSTRUCTION & SUPPLY BIDS / CONTRACTS

- **Upto Rs. 50 crores:** Scheduled Commercial Banks.
- **Upto Rs. 200 crores:** Exim Bank.
- **Above Rs. 200 crores:** Working Group.

SERVICES BIDS / CONTRACTS

On Cash Terms

- **Upto Rs. 5 crores:** Scheduled Commercial Banks.
- **Upto Rs. 10 crores:** Exim Bank.
- **Above Rs. 10 crores:** Working Group.

<u>On Deferred Payment Terms</u>

- **For any amount:** Working Group.

<u>How to apply for loan</u>?

The proposal is to be submitted in the prescribed application form (Ref: Memorandum PEM) along with implementation schedule, currency-wise cash flows and write-up with regard to site and infra-structural condition, and sub-contracting arrangements envisaged. In case of a non-Government buyer, status report on the client/prime contractor would first need to be obtained.

The completed applications are to be submitted to the sponsoring bank, for consideration, within fifteen days of entering into contract.

It would also be necessary to consult ECGC in advance in cases where corporation's insurance cover and/or counter guarantees are required. The applications are forwarded by the sponsoring banks with their comments, to the following agencies which constitute the Working Group:

- Exim Bank, Mumbai.
- Reserve Bank of India,
- Exchange Control Department,
- Mumbai.
- Export Credit Guarantee
- Corporation of India Limited, Mumbai.
- Ministry of Finance,
- Department of Economic Affairs,
- Banking Division, New Delhi.
- Ministry of Finance,
- Department of Economic Affairs (FT),
- New Delhi.
- Ministry of Commerce, New Delhi.
- Other participating banks
- Export Capability Creation Programmes:
  - Lending Programme for Export Oriented Units
  - Production Equipment Finance Programme
  - Technology Up gradation Fund Scheme for Textile and Jute Industries
  - Overseas Investment Finance Programme
  - Equity Investment in Indian Ventures Abroad
  - Asian Countries Investment Partners Programme
  - Export Marketing Finance Programme
  - Export Product Development Programme
  - Export Vendor Development Programme
- Programme for Export Facilitation:
  - Port Development
  - Software Training Institutes

- Foreign Currency Pre-shipment Credit
- Working Capital Term Loan Programme for Export Oriented Units
- Bulk Import Finance
- Finance for Research & Development for Export Oriented Units
- Long Term Working Capital
- Import Finance

Post-Award Clearance of Export Contracts

- Exporter submits application in prescribed from along with copies of contract through his commercial bank for Post Award Clearance.
- Exporter can directly approach Exim Bank for proposals of value limits upto Rs.200 crores.
- On receipt of application and contract copies from the commercial bank, EXIM Bank approves the proposal if the same falls within its delegated powers or convenes Working Group meeting.
- In approved cases, Exim Bank/Working Group accords clearance to the final terms and conditions of the contract including various fund based and non-fund based facilities and requisite exchange control approvals.
- On the basis of package post award clearance granted by Exim Bank/Working Group, final approvals for fund based and non-fund based facilities and requisite exchange control approvals are issued by the concerned institutions and export's banks.

Criteria for Consideration for Clearance of Export Proposals

- Exporter's financial position, track record.
- Status of overseas client - Government/ Private.
- Break-up of contract value - Indian / Third Country / Local.
- Risk Assessment of Buyer's Country.
- Estimates of Cost and Profitability.
- Currency of Payment - Convertible Currency / Local Currency
- Security - Letter of Credit, Bank Guarantee, Government Guarantee, Externalization undertaking of Central Bank.

- Foreign Exchange Outgo.
- Facilities required by the exporter.
- Salient Parameters of Appraisal for Clearance of Export Proposals
- Payment Terms : Advance Payment, Progress / Down Payment, Deferred Payment, Retention Money
- Availability of ECGC Cover, where necessary
- Important Contractual Clauses :
- Preshipment Inspection
- Arbitration
- Force Majeure
- Status of Exporter : Prime Contractor/Sub-contractor/ Consortium Member
- Penalty / Liquidated Damages for delay in Contract Execution
- Price Escalation
- Source of Funding : Multilateral / Local
- Foreign Exchange Outgo
- Facilities required by the exporter

CHAPTER 7 - MARKETING DEVELOPMENT ASSISTANCE (MDA)

INTRODUCTION:

Market developing assistance is provided for meeting the expenditure on export promotion scheme and projects for the development of market abroad for Indian products. It is available for sponsoring trade delegation abroad, market studies, publicity, setting of warehouse/showroom, research and development, quality control, etc. it is available to an individual/organization engaged in/concerned with export marketing.

BENEFICIARIES:

It is available largely to;

- ➔ **Export houses.**
- ➔ **Trading houses.**
- ➔ **Star trading houses.**
- ➔ **Super Star trading houses.**
- ➔ **Individual exporter or other persons sponsored or drafted by the approved organization such as EPC, IIFT, IIP, FIEO, MOC etc.**

The MDA grants disbursed by two agencies namely:

I. Federation of Indian export organization (FIEO)
II. Ministry of Commerce (MOC).

BENEFITS AVAILABLE UNDER MARKET DEVELPOMENT ASSISTANCE SCHEME

The consultancy firms may be provided assistances from the MDA for the following type of activities and at the specified rate.

I. Export Publicity Assistance- for publicity campaign at 60% of the net expenditure after taking into account the revenue from sales and advertisement for publishing magazines including journals, directories, brochure, pamphlets, etc. for use abroad.

II. For organization of trade fairs and exhibition.
III. Overseas market surveys/studies- for undertaking market studies abroad at 80%.
IV. MDA for opening foreign offices and other export activities- for opening an operating foreign office at 60% of the approved expenditure for the first two years, 40% for the next two years and 25% for the fifth year.
V. 40% of the expenditure on brand publicity.
VI. 60% of the approved expenditure to consultancy firms undertaking feasibility studies abroad on their own initiative. Cost of such studies includes cost on international travel, boarding etc. the firms having a minimum annual turnover of Rs. 10 lacs are entitled for this benefits.
VII. 50% reimbursement of the cost of preparation and submission of bids for turnkey/construction projects/ operational and maintenance of services contracts/consultancy contracts subject to standard cost ceilings on different bids.
VIII. 2.5% of bid value upto Rs. 50 lacs relating to consultancy projects. The assistance will go upto to2.5% of Rs. 50 lacs plus 1% of the incremental cost of project beyond Rs. 50 lacs subject a maximum of Rs. 6 lacs.
IX. 50% of the financing cost of bid bond.
X. Sponsoring trade delegations and study-cum-sales teams.
XI. Foreign exchange for specified purposes.
XII. Exemption/rebate in income tax on exports or foreign exchange earnings.
XIII. Reimbursement of central sale tax is exemption form sales tax.

CHAPTER 8 - ` HIGH COURT RULING: EXPORT LOSSES NOT ENTITLED TO TAX CONCESSIONS

In a landmark judgement , the Mumbai High court ruled that only profit from exports is entitled to tax concessions under Section 80HHC of the Income Tax Act. Losses are not to be considered for deduction under Section 80 HHC, the court ruled. The division bench comprising of Justice S.H. Kapadia & Justice V C Daga, gave this ruling on 2.7.2001, in an appeal filed by Ipca Labs against and order by the Income Tax Appellate Tribunal.

Case Details: The HC had to decide whether the loss incurred in export of goods was to be ignored while determining the appellant's entitlement to deduction u/sec 80 HHC (3) c of I-T Act. In this case, Ipca's export income contained 2 parts: One that resulted in Profit and the other that resulted in losses. Ipca claimed deductions for the profit it had made in the export of goods manufactured by it, even though it made a loss in the export of goods made by other manufacturers.

The company claimed that the loss it had incurred should be ignored because the loss was in export of goods made by others, the benefits of which had been surrendered by the company in favour of the supporting manufacturers.

The IT dept on the other hand, took a stand that profit & loss should be aggregated & only the balance is entitled for deductions. As per the department, the result was a net loss from the export of goods, in the case of Ipca. As a result the company did not get any benefit under Section 80 HHC.

Ipca's return indicated a net loss from the export of goods - loss from goods manufactured by supporting manufacturing at Rs.6.86 crore and profits from export of goods manufactured by it at Rs.3.78 crore. In its ruling the high court said:

However, the argument is that because of the disclaimer, the loss on the export of trading goods amounting to Rs.6.86 crore be ignored and only the profits from the self manufactured goods at Rs.3.78 crore alone should be taken into account. This is an ingenious method because if this argument is accepted then the supporting manufacturers as well as the exporting house would both be entitled to the benefits of tax concessions or deductions under Section 80 HHC.

CHAPTER 9 - CONCLUSION

Learning's/Suggestions through this project:

- Export Finance is a very important branch to study & understand the overall gamut of the international finance market.
- Availability of favorable Export finance schemes directly impacts the local trade, encourages exporters, enlarges markets abroad, improves quality of domestic goods and overall helps the nation boost its exchange earnings.
- The Government of any nation plays a very vital role in boosting export turnover. The credit policy of the Indian Government is also changed depending upon the needs of the exporters, global trade environment etc. The credit policy of Oct 2001 is a pointer in this direction.
- ECGC and EXIM Bank take a lot of efforts for Export promotion. The strategies of these 2 agencies in India should be flexible & their finance schemes should be constantly synchronized with the changing scene of world trade. This alone can help Indian exporters to stand competition in world markets effectively and more gain-fully.
- Finally, a very essential question needs to be answered by the International Trade gurus with reference to "Relevance of EXIM Policy in the current times". Exim policies had emerged when the state decided to limit imports and encourage

exports in order to maintain currency reserves. However, such ideas backfired: consumers were hurt and producers turned lazy.

Hence its time the experts/gurus answer the following queries:

a) Should the state get out of the way of trade?

b) Is the protection inherent in the new EXIM policy good for the country?

c) Would India be a major exporter if only she was equipped with a working infrastructure

An appropriate, rational and feasible reply to the above three questions matched with devoted & sincere implementation by the governments will go a long way in making India a powerhouse for international trade in the years to come…

BIBLIOGRAPHY

Books Referred:

Export –What Where & How by Paras Ram

Export Marketing by Michael Vaz

Export Management by T. A .S. Balagopal

Newspapers and Magazines Ref erred:

Business India

Economic Times

Internet Websites:

www.google.com

www.economictimes.com

www.rediff.com