

Chapter 2

Cash-in-Advance

With the cash-in-advance payment method, the exporter can avoid credit risk or the risk of nonpayment, since payment is received prior to the transfer of ownership of the goods. Wire transfers and credit cards are the most commonly used cash-in-advance options available to exporters. However, requiring payment in advance is the least attractive option for the buyer, as this method tends to create cash flow problems, and unless the seller sees no other option or the buyer has other vendors to choose from, it often is not a competitive option. In addition, foreign buyers are often concerned that the goods may not be sent if payment is made in advance. Exporters that insist on this method of payment as their sole method of doing business may find themselves losing out to competitors who may be willing to offer more attractive payment terms.

Key Points

- Full or significant partial payment is required, usually via credit card or bank/wire transfer, prior to the transfer of ownership of the goods.
- Cash-in-advance, especially a wire transfer, is the most secure and favorable method of international trading for exporters and, consequently, the least secure and attractive option for importers. However, both the credit risk and the competitive landscape must be considered.
- Insisting on these terms ultimately could cause exporters to lose customers to competitors who are willing offer more favorable payment terms to foreign buyers in the global market.
- Creditworthy foreign buyers, who prefer greater security and better cash utilization, may find cash-in-advance terms unacceptable and may simply walk away from the deal.

CHARACTERISTICS OF A CASH-IN-ADVANCE PAYMENT METHOD

Applicability

Recommended for use in high-risk trade relationships or export markets, and ideal for Internet-based businesses.

Risk

Exporter is exposed to virtually no risk as the burden of risk is placed nearly completely on the importer.

Pros

- Payment before shipment
- Eliminates risk of nonpayment

Cons

- May lose customers to competitors over payment terms
- No additional earnings through financing operations

Wire Transfer—Most Secure and Preferred Cash-in-Advance Method

An international wire transfer is commonly used and has the advantage of being almost immediate. Exporters should provide clear routing instructions to the importer when using this method, including the name and address of the receiving bank, the bank's SWIFT, Telex, and ABA numbers, and the seller's name and address, bank account title, and account number. This option is more costly to the importer than other options of cash-in-advance method, as the fee for an international wire transfer is usually paid by the sender.

Credit Card—A Viable Cash-in-Advance Method

Exporters who sell directly to the importer may select credit cards as a viable method of cash-in-advance payment, especially for consumer goods or small transactions. Exporters should check with their credit card company(s) for specific rules on international use of credit cards as the rules governing international credit card transactions differ from those for domestic use. As international credit card transactions are typically placed via online, telephone, or fax methods that facilitate fraudulent transactions, proper precautions should be taken to determine the validity of transactions before the goods are shipped. Although exporters must endure the fees charged by credit card companies, this option may help the business grow because of its convenience.

Payment by Check—A Less-Attractive Cash-in-Advance Method

Advance payment using an international check may result in a lengthy collection delay of several weeks to months. Therefore, this method may defeat the original intention of receiving payment before shipment. If the check is in U.S. dollars or drawn on a U.S. bank, the collection process is the same as any U.S. check. However, funds deposited by non-local check may not become available for withdrawal for up to 11 business days due to Regulation CC of the Federal Reserve. In addition, if the check is in a foreign currency or drawn on a foreign bank, the collection process is likely to become more complicated and can significantly delay the availability of funds. Moreover, there is always a risk that a check may be returned due to insufficient funds in the buyer's account.

When to Use Cash-in-Advance Terms

- The importer is a new customer and/or has a less-established operating history.
- The importer's creditworthiness is doubtful, unsatisfactory, or unverifiable.
- The political and commercial risks of the importer's home country are very high.
- The exporter's product is unique, not available elsewhere, or in heavy demand.
- The exporter operates an Internet-based business where the use of convenient payment methods is a must to remain competitive.