Chapter 6
Export Working Capital Financing

Export working capital (EWC) financing allows exporters to purchase the goods and services they need to support their export sales. More specifically, EWC facilities extended by commercial banks can provide a means for exporters who lack sufficient internal liquidity to process and acquire goods and services to fulfill export orders and extend open account terms to their foreign buyers. EWC funds are commonly used to finance three different areas: (1) materials, (2) labor, and (3) inventory, but they can also be used to finance receivables generated from export sales and/or standby letters of credit used as performance bonds or payment guarantees to foreign buyers. An unexpected large export order or many incremental export orders can often place challenging demands on working capital. EWC financing helps to ease and stabilize the cash flow problems of exporters while they fulfill export sales and grow competitively in the global market.

Key Points

- Funds may be used to acquire materials, labor, inventory, goods and services for export.
- A facility can support a single export transaction (transaction specific short-term loan) or multiple export transactions (revolving line of credit) on open account terms.
- The term of a transaction specific loan is generally up to one year and a revolving line of credit may extend up to three years.
- A government guarantee may be needed to obtain a facility that can meet your export needs.
- Risk mitigation may be needed to offer open account terms confidently in the global market.

CHARACTERISTICS OF AN EXPORT WORKING CAPITAL FACILITY

Applicability

To purchase raw materials, supplies, and equipment to fulfill a large export sales order or many small export sales orders.

Risk

Without the use of proper risk mitigation measures, the exporter is exposed to significant risk of nonpayment.

Pros

- Can fulfill export sales orders
- Can offer open account terms to remain competitive

Cons

- Cost of financing a facility
- Risk mitigation may be needed, incurring additional costs

Where and How to Obtain an Export Working Capital Facility

Commercial banks offer facilities for export activities. To qualify, exporters generally need to (1) be in business profitably for at least 12 months (not necessarily in exporting), (2) demonstrate a need for transaction-based financing, and (3) provide documents to demonstrate that a viable transaction exists. To ensure repayment of a loan, the lending bank may place a lien on the assets of the exporter, such as inventory and accounts receivable. In addition, all export sale proceeds will usually be collected by the lending bank before the balance is passed on to the exporter. Fees and interest rates are usually negotiable between the lender and the exporter.

Short-term Loans or Revolving Lines of Credit

There are basically two types of export working capital facilities: transaction specific short-term loans and revolving lines of credit. Short-term loans, which are appropriate for large and periodic export orders, are typically used in situations where the outflows and inflows of funds are accurately predictable in time. These loans can be contracted for 3, 6, 9, or 12 months and the interest rates are usually fixed over the requested tenors. Revolving lines of credit, on the other hand, are appropriate for a series of small fractional export orders as they are designed to cover the temporary funding needs that cannot always be predictable. These revolving lines of credit have a very flexible structure so that you can draw funds against your current account at any time and up to a specified limit.

Why a Government Guarantee May Be Needed

The Export-Import Bank of the United States and the U.S. Small Business Administration offer programs that guarantee export working capital facilities to U.S. exporters. With these programs, U.S. exporters are able to obtain needed facilities from commercial lenders when financing is otherwise not available or when their borrowing capacity needs to be increased. Advance rates offered by commercial banks on export inventory and foreign accounts receivables are not always sufficient to meet the needs of exporters. In addition, some lenders do not lend to exporters without a government guarantee due to repayment risk associated with export sales. More detailed information is provided in Chapter 7.

Why Risk Mitigation May Be Needed

While export working capital financing will certainly make it possible for exporters to offer open account terms in today's highly competitive global markets, the use of such financing itself does not necessarily eliminate the risk of nonpayment by foreign customers. In order to offer open credit terms more confidently in the global market, the use of some forms of risk mitigation may be needed. In addition, the use of risk mitigation may be necessary for exporters to obtain export working capital financing. For example, the bank may require the exporter to obtain export credit insurance as a condition of providing working capital and financing exports. Forms of risk mitigation will be discussed in other chapters of the *Trade Finance Guide*.