

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 lenders provide a means for small and medium-sized enterprises (SMEs) that lack sufficient internal liquidity to process and acquire goods and services to fulfill export orders and to extend open account terms to their foreign buyers. EWC funds are commonly used to finance three different areas: (a) materials, (b) labor, and (c) 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 place challenging demands on working capital. EWC financing, which is generally secured by personal guarantees, assets, or high-value accounts receivable, helps to ease and stabilize 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.
- A transaction-specific loan is generally up to one year, and a revolving line of credit may extend up to three years.
- Availability is generally limited to financially-stable large corporations or established SMEs with access to strong personal guarantees, assets, or high-value accounts receivable.
- A government guarantee may be needed to obtain a facility that can meet export needs.
- Exporters may need risk mitigation to offer open account terms confidently in the global market.

Where and How to Obtain an Export Working Capital Facility

Many commercial banks and lenders offer facilities for export activities. To qualify, exporters generally need (a) to be in business profitably for at least 12 months (not necessarily in exporting), (b) to demonstrate a need for transaction-based financing, and (c) to provide documents to demonstrate that a viable transaction exists. Note that personal guarantees, collateral assets, or high-value accounts receivable are generally required for SMEs to obtain commercial EWC facilities. The lender may place a lien on the exporter's assets,

CHARACTERISTICS OF AN EXPORT WORKING CAPITAL FACILITY

Applicability

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

Risk

Significant risk of non-payment for exporter unless proper risk mitigation measures are used.

Pros

- Allows fulfillment of export sales orders
- Allows exporter to offer open account terms to remain competitive

Cons

- Generally available only to SMEs with access to strong personal guarantees, assets, or high-value receivables
- Additional costs associated with risk mitigation measures

such as inventory and accounts receivable, to ensure repayment of a loan. In addition, all export sales proceeds will usually be collected by the lender 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

Basically, there are two types of EWC 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 if the outflows and inflows of funds are predictable over time. Short-term 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, however, are appropriate for a series of small export orders because they are designed to cover temporary funding needs that cannot always be anticipated. Revolving lines of credit have a very flexible structure so that exporters can draw funds against current account at any time and up to a specified limit.

Why a Government Guarantee May Be Needed

The U.S. Small Business Administration and the Export-Import Bank of the United States offer programs that guarantee EWC facilities to U.S. exporters. These programs allow U.S. exporters to obtain needed facilities from participating lenders when commercial 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 risks associated with export sales. More detailed information is provided in Chapter 7.

Why Risk Mitigation May Be Needed

Although EWC financing certainly makes it possible for exporters to offer open account terms in today's highly competitive global markets, the use of such financing does not necessarily eliminate the risk of non-payment by foreign customers. Some forms of risk mitigation may be needed in order to offer open account terms more confidently in the global market and to obtain EWC financing. For example, a lender may require an exporter to obtain export credit insurance as a condition of providing working capital and financing exports.