



Significance of export credit system in India

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Abstract

Export credit system provides three basic functions. First, they help exporters meet officially supported foreign credit competition. (When foreign governments subsidize their companies' exports by offering buyers below-market, fixed-rate financings, exporters often find it difficult to offer financing that matches those subsidized rates.) Secondly, Export credit system provides financing to foreign buyers when private lenders cannot or will not finance those export sales, even with the risks removed. Third, and perhaps their most important function, Export credit system assume risks beyond those that can be assumed by private lenders.

Export credit system does not compete with private financial institutions. To the contrary, they enhance the ability of their country's lenders to compete internationally. It should also be noted that they do not offer development assistance to other countries; other agencies typically fulfill this role.

Keywords: credit, export, bank

Introduction

Export credit system address two fundamental risks involved in an export transaction. The first is political risks, which refers to those events that occur due to political actions taken by the government that impact payment by the buyer. These may include transfer risk (inability to exchange the local deposit to that of the Export credit system country), expropriation, war risks, cancellation of an existing import and export license, and/or political violence. The risks of countries are usually evaluated by OECD and classified into seven categories depending on their risk profile.

Working capital support from Export credit system significantly reduces a lender's risk on the goods or services for export. This support may also assist in posting standby letters of credit needed to secure down payments, post bid bonds, or other activities required in anticipation of an export sale. An Export credit system's primary function is to shield the exporter from the commercial and political risks of selling overseas.

This can be done as a supplier credit, where the Export credit system guarantees the obligation of the importer on terms extended by the exporter; or it can take the form of a buyer credit where the Export credit system supports the obligation of the importer directly. Finally, Export credit system have recognized the need to support turn-key solutions with project financing support, as well as tailoring their support to work with the special financing needs of specific industries.

Export credit system offer a variety of export credit insurance policies to exporters and financial institutions to reduce repayment risks on foreign receivables due to political and commercial events. Policies may cover single or repetitive sales, to single or multiple buyers. As determined by the product, repayment terms are available for short-term sales (up to 180 days, exceptionally 360 days) and medium-term sales (up to five years). Loans are made directly by some

Export credit system to overcome financing gaps and compete against foreign subsidized competition with the lowest interest rates allowed under international guidelines. Typically this is on a limited basis, since their goal is not to compete with the private sector. By reducing repayment risks, guarantees from Export credit system allow lenders to offer financing to exporters and/or their foreign customers with fixed or floating competitive rates.

According to statistics, one out of every eight dollars of world trade is now financed by Export credit system. Much of the remaining seven dollars is influenced by what the Export credit system do: whether they advocate a restrictive or expansive policy of selling goods to other nations affects exporters' willingness to trade with particular countries and buyers and influences the terms and conditions on which trade is conducted. There are only about 200 Export credit system in the world – domiciled in 100 countries- but their contribution to trade and development has been massive and intensive in the success of globalization and a healthy economy.

Export credit system activity far exceeds that of all multilateral development banks (MDBs), such as the World Bank, International Development Bank – IDB and KfW. By the way, these institutions represent a constant source of funding for Eletrobras' funding activities. Eletrobras has recently developed a loan agreement with World Bank, whose resources will be channeled to a project from the Eletrobras' System distribution companies.

Export credit system financing takes the form of loans, guarantees, insurance, and related technical assistance which are used to support export sales. In order to fund these operations, the world's Export credit system obtain monies from both domestic and international capital markets that are then lent to their nations' exporters. Most importantly of all, perhaps, the Export credit system are a repository of information and technical skill, which are used to show

exporters and banks how to extend credit to foreign buyers in a sound fashion. The Export credit system excels in the techniques of intelligent risk management, which they apply in their own extensions of short-, medium-, or long-term credit. These techniques are picked up, and carried on, by a nation's exporters and banks, regardless of whether the Export credit system provides financing or other assistance for a particular sale.

Research Study

Lenders use these programs for several reasons. By limiting the risk inherent in international lending, Export credit system programs enable lenders to assist their current customers with international sales they otherwise would be unable to finance. These programs also help lenders develop new relationships with exporters and foreign buyers that may grow into long-term, profitable lending relationships.

These programs help exporters meet two critical financial needs. First, Export credit system help obtain the working capital financing they need to produce or buy their goods and services for export. Creditworthy exporters sometimes have difficulty securing such financing for a number of reasons: they have reached their borrowing limit with the lending institution; the lender has no relationship with the exporter; or the lender will only provide a low percentage loan against the exporter's collateral, thereby constraining the firm's cash resources.

Second, Export credit system help exporters secure credit for foreign buyers. Often the exporter cannot complete the sale unless competitive financing can be provided. In some cases, the exporter could expand business with current customers if credit is extended.

Most industrial country Export credit system have now been in operation for more than fifty years. More than half of the developing country Export credit system have been in business for at least a decade and thus can be considered fully experienced in the appraisal and administration of export credit, guarantees, and insurance. The differences between industrial and developing countries in this field, which were tremendous in earlier years, are gradually narrowing and approaching common ground. The industrial countries have pulled back from overexpansion of credit to marginal markets, while the developing countries have sought to take more risk on credit sales with jeopardizing their financial soundness.

Export credit system around the world share a number of constraints, imposed by such factors as their total authority and yearly budgetary ceilings, by requirements that they supplement and complement and not compete with private finance, by the need to seek reasonable likelihood of repayment on transactions, by other limits imposed to ensure prudent financial management, by the need to conform to the terms and conditions of international understandings, and by a number of other restrictions imposed by their authorizing legislation, guardian authorities in government, or private shareholders.

Official export credit, guarantee, and insurance agencies also share many features with regard to the mechanics of their operations. They have similar eligibility criteria, term differentiation, Risk classification, degree of coverage, underwriting techniques, premium and interest rate systems,

policy administration, risk-sharing methods, and reinsurance. This is not by chance. The techniques, terms, and conditions of export credit insurance and guarantees have been largely "internationalized" by regular exchanges of information and agreements reached through the International Union of Credit and Investment Insurers (Berne Union) and the Organization for Economic Cooperation and Development (OECD), and there is a growing level of comparability among individual national schemes.

Normally, export credit agencies provide assistance that does not exceed 90 percent of postshipment financing, with the exporter or bank taking the balance of the risk for its own account. Pre-shipment assistance is also usually limited to a maximum of 90 percent of required credit. On medium- and long-term transactions, official schemes require the foreign buyer to make an advance payment of at least 15 percent. On short-term coverage, no advance payment is required from the foreign buyer.

Governments play many roles in support of Export credit system. They can be insurers or reinsurers of risks; they can provide finance to exporters or to their customers; or they can intervene in the cost of financing. It is important to note that government's role in most Export credit system is now diminishing, as the private sector in most countries is more willing and able to take risks and assist them in their activities.

Discussion

Growing private extensions of export credit have reduced the need for official export finance in many countries, and decreases in the volume of mixed credits (a combination of trade and aid financing) have further limited the necessity for government loans to support exports. However, governments are still actively involved in risk-sharing with Export credit system in all countries. Even though international private reinsurance of export credit risks continues to grow, governments are still the major insurers or reinsurers of risk, particularly political risks, for their national Export credit system.

Export contracts are transactions that involve the cross-border sale (or sometimes the lease) of equipment or services. The OECD Arrangement defines export contract value to include the entire value of imported goods and services contracted between the buyer and the supplier. Export credits are financial obligations that arise from particular export contracts and are directly and explicitly "tied" to such contracts. Financings that simply make funds available to buyers for general foreign purchases are "untied".

Official fixed-rate support is and Export credit system offer of protection against increases in interest rates during the life of an export credit. Official fixed-rate support is delivered by different means by different Export credit system. Indian Bank provides official fixed-rate support by means of direct fixed rate loans, where Indian Bank itself serves as the financial intermediary on behalf of the supplier. Other countries (usually not the Export credit system) guarantee banks for a fixed margin over a floating rate cost of funds when they provide fixed rate financing at arrangement interest rates.

It is customary in export sales and in export credit financing, as in domestic lines of business and their financing, for suppliers and their financiers to require a significant good-

faith cash payment from prospective buyers. The OECD Arrangement codifies this practice by requiring, at a minimum, a cash payment equal to 15 percent of the export contract value for all export credits.

The OECD Arrangement requires the first payment of principal and interest on an officially supported export credit no later than six months after the proper “starting point”, a date which reflects the nature of the underlying export contract. Many exported goods and services are delivered to buyers. For these goods, the proper starting point is delivery. Many exported capital goods are installed. Some are installed in broader projects that must be constructed. For export credits involving such capital goods, the proper starting point is the conclusion of physical installation or construction. As for projects involving the installation of multiple units of imported capital goods, the arrangement requires either the use of multiple starting points or of an average one.

As export credit’s disbursement period is the period between the export credit’s first disbursement and the starting point for repayment. For delivered products, the disbursement period is usually very short; in some cases, there may be a single disbursement. For projects under construction, the disbursement period can be as long as four or five years, or perhaps even longer. In such cases, partial disbursements are made as various construction milestones are achieved.

For lease, the OECD Arrangement permits mortgage-style level total payments of principal and interest. This payment pattern has the cash flow advantage of lower payments during the first few years of a term credit. However, there are larger payments during the last few years, and export credit principal is paid down at a much slower pace.

For loans under an Indian Bank comprehensive guarantee covering 100 percent of principal and interest with no risk deductible, the spreads usually are rather small, as there is no residual credit risk taken by the lender.

The remaining spreads represent compensation for administrative expenses in making the loan and an element of lender’s profit. For loans guaranteed by those Export credit system that cover only 98 percent, 95 percent, 90 percent, or lesser amounts of principal and interest, the lending spreads can be substantially larger, as they seek to compensate for residual credit risk.

“Concessional” is a measure of the financial stability of the recipient government. The concessional of tied aid credits is typically underwritten by development assistance (aid) agency budgets rather than export credit agency budgets. A standalone grant offers 100 percent concessional, a standalone export credit offers zero percent concessional, and a mixed credit with a 35 percent grant portion offers 35 percent concessional. For a soft loan, concessional depends on the present value of such financing, discounted at a market-related rate in the currency of the financing offered. The lower the present value, the higher the concessional. The lower the interest rate, relative to market rates in the currency of the financing offered, or the longer the repayment term, the more concessional is the soft loan.

Conclusion

The Export credit system have performed the invaluable function of making credit available to many countries where

commercial banks and other private lenders are not willing to make trans-border loans, and of making credit available to most developing countries at interest rates and repayment periods that are more favorable than alternative private sources of funds. This has enabled the developing world to purchase much more of the equipment, goods, and services that the industrial countries have to offer, with a resulting dramatic improvement in social welfare, the standard of living, and investment in new infrastructure and the productive sector.

The level of export credit agency activity grew rapidly in the early 1990s as international trade increased at a rate approximately three times that of domestic growth. Export trade is now widely acknowledged as the primary engine of economic growth and development and, as such, notorious of special financial institutions to help with the proper structuring of credit sales, the necessary extension of appropriate loans, the sharing of related risks, and the encouragement of other institutions to participate in this business. In recent years, industrial capacity has expanded, consumer tastes have changed, trade barriers have fallen, and competition among supplier nations has intensified. As a consequence, all countries face growing pressures to adapt their financing systems to new trading requirements.

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