EXIM TRADE: SOURCES OF SHORT -TERM BORROWED FUNDS

***Dr. Anil Soni**

Abstract

There are 5 Ms of production i.e. Men, Materials, Machines, Methods and Money. Money is considered as one of the most important factor of production. In commercial terms money is known as finance. Someone has rightly said that finance is the life blood of business. The other factors of production can be procured only if one is having money. The policy of liberalization and globalization introduced in the early 1990s by Pamulaparti Venkata Narasimha Rao Government in India has led to a astonishing growth in the export and import business of India. The Indian economy is flooded with the Multinational Corporations and there is hardly any top brand of the world which is not available in India. Similarly, there are a large number of Indian companies which have started operating in many countries of the world. There has been terrific growth in exports from India. There is hardly any country of the world where Indian products are not being exported.

With the increase in the volume of exports during the last 25 years, there has been a sizable increase in the demand for export credit facilities. The Indian banks and other financial institutions are extending a large number of credit facilities to the exporters. These facilities are broadly classified under the two heads viz. Pre-shipment finance and Post-shipment finance.

Keywords: Pre-shipment finance, Post-shipment finance, Packing Credit, IEC, DGFT

Introduction:

The finance is required at every step for various purposes. The organization needs finance to purchase raw materials, to meet day to day expenditures, to extend credit to the customers etc. The finance is equally importance irrespective of the nature, size, location or type of business. The exporters also need finance to their various needs. The export financing in India is broadly classified into two categories viz. Pre-Shipment finance and Post-Shipment finance. We shall be discussing various forms of these types of finance in the following paragraphs.

*Associate Professor, Department of Business Management,

DAV Institute of Engineering & Technology, Jalandhar.

Pre-Shipment Finance

Pre-Shipment finance as the name suggests is required before the goods are shipped/dispatched. This means that Pre-Shipment finance is required to manufacture/procure the goods for export. Pre-Shipment finance is generally called Packing Credit The pre-shipment credit facility is extended by the banks to exporters for the following purposes:

1. Purchasing raw materials to be used in the manufacture of goods to be exported.
2. To meets packing expenses of the goods.
3. To meet the routine expenses of exporters.
4. Meeting the processing expenses.
5. To meet other financial costs.
6. To pay for consultancy expenses.
7. For storage of the goods in the warehouse till the time they are shipped

Types of Packing Credit

Packing credit is of two types:

A. Packing Credit in Indian rupees

B. Pre-Shipment Credit in Foreign Currency (PCFC)

Packing Credit in Indian Currency:

The facility of Packing Credit can be availed by every exporter. The packing credit is extended to the exporters again the confirmed purchase orders received from the overseas buyers or against the confirmed letter of credit. Banks usually sanction a limit to the exporter for packing credit. This limit is of revolving nature. Once the limit is sanctioned by the bank, the exporter can avail the facility of packing credit. As and when exporter receives an order or a confirmed letter of credit, they have to approach to the bank for disbursement of packing credit.

Requirement of Getting Packing Credit Facility:

The packing credit facility can be extended to the exporter who fulfills the following conditions:

- The exporter is having a valid 10 digit Importer-Exporter Code (IEC) issued by Director General of Foreign Trade (DGFT)
- The exporter is not in the caution list of Reserve Bank of India.
- The items to be exported fall under Open General License (OGL) category, if it is not so, the exporter must have the license issued by DGFT

Disbursement of Packing Credit

As an exporter approaches to the bank for disbursement of packing credit the banker has to ensure the followings:

1. That the documentation is complete and all the formalities of sanction are complete including creation of mortgage.
2. That exporter has got the confirmed order or irrevocable letter of credit which has the following details:
    - Name and complete address of the buyer
    - Complete description of the items to be exported.
    - Quantity
    - Price of the item
    - Port of Loading
    - Port of Discharge
    - Last date of shipment
    - Payment terms
3. Profile of the importer
4. Political and Economic Conditions in the country of import
5. The exporter is having the valid license or quota if the goods to be exported do not fall in the Open General License Category
6. Whether the country of import is in the list of Restricted Cover Countries (RCC) or not

Quantum of Finance:

The quantum of finance depends upon the amount of the order or the value of the letter of credit received by the exporter. Banks usually grant a credit ranging from 75% to 90% of the value of order/letter of credit. The bank also wants some margin money from the exporter. The amount of margin money to be contributed by the exporter depends upon the following factors:

- The nature of the order
- The nature of the item to be exported
- The capability of the exporter to bring in the requisite contribution.

Period of Finance:

The period of packing credit finance depends on the production cycle, but in any case it can not go beyond the date of shipment. As per the normal banking practices, the packing facility can be granted up to 180 days, if this is beyond 180 days the permission of Reserve Bank of India is required.

Follow up of Packing Credit

Exporter needs to submit regular stock statements giving all the necessary information about the stocks. It is then used by the banks as a guarantee for securing the packing credit in advance. Bank also decides the dates of submission of these stocks. The banks should note due dates in due date registers and should periodically follow up with the exporters to ascertain the status of manufacturing the goods and probable date of shipment. In case it is observed that shipment can not be made in the prescribed period the reasons for delay are investigated. If the reasons are un avoidable such as labor problems, power shortage then the exporter should be advised to seek extension of shipment date from purchaser .Apart from this, authorized dealers (banks) also physically inspect the stock at regular intervals.

Liquidation of Packing Credit Advance

Packing Credit Advance needs be liquidated out of the export proceeds of the relevant shipment, thereby converting pre-shipment credit into post shipment credit. This liquidation can also be done by the payment receivable from the Government of India and includes the duty drawback, payment from the Market Development Fund (MDF) of the Central Government or from any other relevant source. In case if the export does not take place then the entire advance can also be recovered at a certain interest rate. RBI has allowed some flexibility in to this regulation under which substitution of commodity or buyer can be allowed by a bank without any reference to RBI. Hence in effect the packing credit advance may be repaid by proceeds from export of the same or another commodity to the same or another buyer. However, bank need to ensure that the substitution is commercially necessary and unavoidable

Overdue Packing Credit

Bank considers a packing credit as an overdue, if the borrower fails to liquidate the packing credit on the due date. And, if the condition persists then the bank takes the necessary step to recover its dues as per normal recovery procedure

Pre-Shipment Credit in Foreign Currency (PCFC)

The objective of extending packing credit facility in foreign currency is to make credit available to the exporters at competitive rates. When the credit is extended in foreign currency the exporter get an advantage of making foreign currency payments of raw materials and other items without getting the Indian Currency exchanged into foreign currency. The exporter can avail the PCFC in any freely convertible currency like US$, Pound Sterling, Euro, Yen etc.

Rate of Interest on PCFC

The rate of interest on PCFC is linked to London Interbank Offered Rate (LIBOR). According to guidelines, the final cost of exporter must not exceed 1.00% over 6 month LIBOR, excluding the tax.

Eligibility

The only criterion for extending PCFC in foreign currency is either confirmed order or confirmed letter of credit.

Period of Credit

(i) The PCFC will be available as in the case of rupee credit initially for a maximum period of 180 days; any extension of the credit will be subject to the same terms and conditions as applicable for extension of rupee packing credit and it will also have additional interest cost of 2 percent above the rate for the initial period of 180 days prevailing at the time of extension.

(ii) Further extension will be subject to the terms and conditions fixed by the bank concerned and if no export takes place within360 days, the PCFC will be adjusted at T.T. selling rate for the currency concerned. In such cases, banks can arrange to remit foreign exchange to repay the loan or line of credit raised abroad and interest without prior permission of RBI.

(iii) For extension of PCFC within 180 days, banks are permitted to extend on a fixed roll over basis of the principal amount at the applicable LIBOR/EURO LIBOR/EURIBOR rate for extended period plus permitted margin (1.0 percent over LIBOR/EUROLIBOR/EURIBOR).

Liquidation of PCFC

(a) The facility of PCFC will be self-liquidating in nature .Accordingly, the PCFC should be liquidated out of proceeds of export documents on their submission for discounting/rediscounting under the EBR Scheme

(b) The export bills will have to be discounted or covered by grant of foreign currency loans (DP bills) to liquidate the outstanding PCFC. The question of sending export bills for collection does not arise.

(c) The PCFC should not be liquidated with foreign exchange acquired from other sources.

(d) PCFC cannot be treated as a loan to be repaid in order to avail of post-shipment credit separately.

Post Shipment Finance

The credit which is extended to the exporter after the shipment of the goods till the realization of export proceeds is known post shipment finance. The objective of post shipment finance is allowing the exporter to meet the working capital needs of the exporter after shipping the goods. The post shipment finance is granted to meet the following expenses:

- To pay freight to the shipping
- To pay port charges
- To pay ECGC premium
- To pay insurance premium.
- To pay commission to overseas agents
- To pay custom duties and other government levies.

Types of Post –Shipment Finance

i. Export bills purchased/discounted /
ii. Advances against export bills sent on collection basis.
iii. Export bills negotiated under Letter of Credit (L/C)
iv. Advances against duty drawbacks receivables from government.
v. Advances against exports on consignment basis.
vi. Deferred payment exports

Export Bills Purchased/ Discounted. (DP & DA Bills)

Export bills are used in terms of sale contract/ order may be discounted or purchased by the banks. Proper limit should be sanctioned to the exporter for the purchase or discount of export bills. Risk of nonpayment may arise as the export is not covered under Letters of credits. The risk is more pronounced in case of documents under acceptance. In order to safeguard the interests of the bank and also of exporter, ECGC offers coverage of credit risk through their guarantees to the banker and policies to the exporters at the post shipment stage.

Advance Against Export Bills Sent on Collection Basis

Post shipment finance can also be granted against export bills sent for collection . It can be availed at the time of sending or after sending the bills for collection. Bills can only be sent on collection basis, if the bills drawn under LC have some discrepancies. Sometimes exporter requests the bill to be sent on the collection basis, anticipating the strengthening of foreign currency. Banks may allow advance against these collection bills to an exporter with a concessional rates of interest depending upon the transit period in case of DP Bills and transit period plus usance period in case of usance bill. The transit period is from the date of acceptance of the export documents at the bank's branch for collection and not from the date of advance.

Export Bills Negotiated (Bill under L/C)

Negotiation of export bills usually refers to the documents presented under freely negotiable letter of credit providing for negotiation of the bill. The documents drawn should be strictly in conformity with terms of LC and should be scrutinized carefully .The issuing bank can refuse the payments to the negotiating bank even if there will be a slightest variation in terms and conditions from those specified in LC. For example : LC expired before shipment or negotiation, drawing in excess of LC amount ,incomplete or incorrect invoice ,full set of documents not submitted as called for in LC. The risk of payment is less under the LC, as the issuing bank makes sure the payment. The risk is further reduced, if a bank guarantees the payments by confirming the LC. Because of the inborn security available in this method, banks often become ready to extend the finance against bills under LC.

Advance Against Export on Consignments Basis

Goods may be exported on consignment basis at the risk of exporter for sale abroad and the actual remittance of sale proceeds is made by an agent or consignee. This facility is granted to good customers only. Bank may choose to finance when the goods are exported on consignment basis at the risk of the exporter for sale and eventual payment of sale proceeds to him by the consignee.

However, in this case bank instructs the overseas bank to deliver the document only against trust receipt /undertaking to deliver the sale proceeds by specified date, which should be within the prescribed date even if according to the practice in certain trades a bill for part of the estimated value is drawn in advance against the exports. In case of export through approved Indian owned warehouses abroad the times limit for realization is 15 months. The advances granted should be liquidated from the remittance of sales proceeds within 180 days from the date of shipment. Concessional rate will apply for a maximum period of Notional Due Date , in case of all cash exports whether consignment or exports on outright sales basis even if RBI extends the time limit for realization of export proceeds beyond 180 days.

Advance against Claims of Duty Drawback

The government of India provides export incentives under export promotion scheme in the form of refund of excise and custom duty known as duty drawbacks. Banks grant advances to exporters at lower rate of interest for a maximum period of 90 days from the date of advance. These are granted only if other types of export finance are also extended to the exporter by the same bank. After the shipment, the exporters lodge their claims, supported by the relevant documents to the customs authorities. These claims are processed and eligible amount is disbursed after making sure that the bank is authorized to receive the claim amount directly from the concerned government authorities.

Conclusion

Even though government of India is providing financial assistance to the Indian exporters in export financing in the form of packing credit facilities, running account facilities, advances against export bills and deferred payments etc, even then India is lagging behind other countries. In today's competitive world, due to cost and period gap involved in export transaction, the availability of own finance & large and reasonable sources of credit facilities become a necessity. So the development of this sector is very much essential for India as foreign exchange can be earned through this sector which will help to maintain exchange rate stability in the country.

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