How to access trade finance

James Sinclair, Trade Finance Global

info@tradefinanceglobal.com
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How to Access Trade Finance

An SME Finance Guide by Trade Finance Global

One of the biggest challenges any small or medium enterprise (SME) faces is access to finance. This guide aims to do the following:

➔ Define trade finance, the different types of financial instruments, and who/when they are accessible and most appropriate for

➔ Discuss the challenges and reasons why SMEs struggle to access trade finance

➔ Highlight the benefits of trade finance and how it can be used as a convenient facility to help with short to medium-term finance solutions

➔ Explain the trade finance credit process from pre-application to repaying the loan

➔ Sourcing the right lenders and banks and the negotiation process

Key terms: trade finance, stock finance, supply chain finance, import and export finance, Letters of Credit, factoring, forfaiting, insurance
What is trade finance?

Trade finance concerns international and national trade transactions - when a buyer purchases goods or services from a seller, the financial activities involved come under the umbrella term ‘trade finance’. This includes:

- Lending facilities
- Issuing Letters of Credit (LCs)
- Export factoring (banks secure finance based on invoices or accounts receivable)
- Forfaiting (purchasing the receivables or traded goods from an exporter)
- Export credits (to reduce risks to funders when providing export or trade finance)
- Insurance (during delivery and shipping, also covers currency risk and exposure)

Why is trade finance important?

Trade finance is a huge driver of economic development and helps maintain the flow of credit in supply chains. It is predicted that 80-90% of global trade is reliant on trade finance, and is estimated to be worth around USD $10 trillion a year.1

As a result of the global economic crisis in 2008, export markets reduced in size by around 40-50%, SMEs being the hardest hit. As a result, lending decreased as investor’s appetite for risk decreased, and banks had to reduce the sizes of their loan books.

Who benefits from trade finance?

Trade finance has many beneficiaries: developing countries, governments, small and medium enterprises. SMEs are engines for economic growth and development, accounting for around 99% of businesses, 50% of employment

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1 World Trade Organization
2 International Trade Centre
and driving around 30% of private sector revenue in the UK\textsuperscript{3}.

In relation to export finance and the supply chain, many SMEs play a large role in the running of multinational corporations and larger companies. SMEs require access to finance to fulfill larger contracts, import goods from overseas and create wealth, jobs and develop economies.

**Challenges for SMEs in accessing trade finance**

From the banks perspective, as they become more technology and efficiency driven, SMEs often don’t fulfil certain criteria for banks to justify lending to. As lending money has an associated transaction cost, it is more costly to assess and monitor loans to a smaller, riskier company where profit is less certain, relative to a larger, more profitable and stable business.

Banks will often ask for the following from any company when filling out an application for any type of business finance, trade finance included:

- Audited financial statements
- Full business plans
- Financial forecasts
- Credit reports
- Details and references of the directors
- Information on assets and liabilities

As well as the cost of lending to SMEs being less profitable for banks, there is a much higher default risk and chance of bankruptcies with SMEs in comparison to larger firms. The other challenge that banks have in lending to SMEs is the lack of security and collateral an SME can provide.

SMEs also face challenges in accessing finance from banks. In a recent survey by the British Business Bank, 46 percent of SMEs were looking to grow in the next 6 months, yet awareness of types of finance available and finding sources of finance (especially after being rejected from a bank) are major concerns amongst SMEs\textsuperscript{4}. The perceived high cost of borrowing, lengthy procedures for

\textsuperscript{3} **Department for Business, Innovation and Skills (BIS)**
\textsuperscript{4} **British Business Bank** survey
securing a loan and also the amount of paperwork and documentation required is often off-putting and cumbersome to SMEs.

**Benefits of trade finance**

Most businesses require financing at some stage, particularly those in the international export or global supply chain trade where capital costs are high and profitability is greater when order volumes are high.

As well as economic benefits (job and wealth creation), individual companies benefit from export finance as it generally increases productivity, profitability and growth. Below is a summary of the benefits an SME can see from external financing, in particular, trade and export finance:

<table>
<thead>
<tr>
<th>Benefit</th>
<th>Reason</th>
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<tbody>
<tr>
<td>Allows growth of an SME</td>
<td>More working capital and better cash flow management allows business owners to keep in control of the day-to-day running costs of the business whilst growing and fulfilling larger orders that ordinarily wouldn't be possible.</td>
</tr>
<tr>
<td>Higher profit margins</td>
<td>A finance facility can allow an SME to buy in bulk or volume, up front (at reduced costs) and strengthens the relationship between buyers and sellers. This can be an opportunity to increase profit margins and EBITDA.</td>
</tr>
<tr>
<td>Greater efficiency and productivity</td>
<td>Working with other international players allows business owners to diversify their supplier network which increases competition and drives efficiency in markets and supply chains.</td>
</tr>
<tr>
<td>Reduces bankruptcy risks</td>
<td>Late payments from debtors, bad debts, excess stock and demanding creditors can quickly cause the crippling of an SME which is reliant on effective cash management in order to stay alive. External financing or revolving credit facilities can ease this pressure and prevent an SME from facing these risks.</td>
</tr>
</tbody>
</table>
What types of trade finance are there?

At Trade Finance Global, ‘trade finance’ is a catch-all term for the financing of international trade. Here are some of the types of trade finance that we have briefly summarised.

**Trade Credit**

Normally the seller requires payment of goods 30 or 60 days post shipment. Trade credit, which is probably the easiest and cheapest arrangement is based mainly on trust directly between the buyer and the seller. When the two parties are less well known to each other, or if the creditworthiness of the buyer is not known, a bank backed bill of exchange can be issued and guaranteed by the buyer’s bank.

**Cash Advances**

A cash advance is an injection of capital (unsecured) into the business. It’s often based on trust, and a cash advance can even be favourable and sought from the exporters themselves, given that timely delivery will help your business deliver and ensure their repayment.

**Receivables Discounting**

Invoices, post-dated checks or bills of exchange can be immediately sold on the market at a reduced rate, less 10-30% of the invoice value. Receivables are mainly commercial and financial documents, and new finance houses and marketplaces allow such documents to be sold at discounted prices in return for immediate payment. The discount rate, which is relatively high and can be costly for SMEs is calculated based on the risk of default, creditworthiness of the seller and whether the transaction is international or domestic. Find out more about [invoice discounting and invoice factoring](#) in our guide on our website.
**Term Loans**

Longer term debt (including loans, commercial mortgages and overdraft facilities) can be more sustainable sources of funding. They are often security or guarantee backed (your business would need to own assets up to the value of the loan being sought). Often in the world of international trade and finance, securing against assets owned by business owners in other countries is more tricky, especially due to different ownership regulations in other jurisdictions. Find out more about term loans and business loans on our website.

**Leasing and Asset Backed Finance**

Leasing involves the borrowing of expensive fixed assets such as machinery, vehicles and equipment. There are several finance mechanisms which allow SMEs to have access to assets which are repaid in smaller contractual, tax deductible repayments.

Asset finance allows SMEs to purchase equipment or assets over a period of time, worry less about the maintenance of it, and it is favourable for tax treatment in many markets.

There are different types of leasing / asset finance, including finance lease, hire purchase and operating leases. We’ve detailed these types of finance and written an asset finance guide which you can access here.

**Other types of business finance**

There are other types of trade finance which we think would be useful for SMEs to know about, which aren’t strictly ‘trade finance’ as we define, but it’s worth considering. Equity finance includes seed funding, angel investment, crowdfunding, venture capital (VC) funding and floatation. The principles however are the same. Generally a business owner will give a proportion of his or her shares to an investor (so that they own a share of the business) and if the company grows and shares become more valuable, they will sell their shares in the business (exit) and make a return on their initial investment. It’s a rather complicated type of finance with many different types - we’ve summarised them and written a more extensive guide to equity finance here.
Methods of Payment in Trade Finance

Importers and exporters normally require intermediaries such as banks or alternative financiers to guarantee payment and also the delivery of goods. Cash advances or trade credits on open accounts usually develop after the buyer and seller develop a trusted relationship; therefore trade finance requires financing mechanisms to help support these transactions.

Support for trade finance includes facilitating payment in a secure and timely manner (e.g. SWIFT), mitigating possible risks through credit insurance, and tracking the shipment of goods when they are in transit.

Payments have varying types of risk: for the importer and the exporter. Here we cover 4 types of payment methods: cash advances, letters of credit, documentary collections and open accounts. As a business owner, it is important to understand the different risks for each type of payment method, to see which one is most favourable and suitable for your business requirements.

Cash Advance

All the risk lies with the importer; a cash advance requires full payment before the goods have been shipped. Cash advances are common with Internet businesses, due to low value orders.

As an exporter, a cash advance is by far the least risky payment method; it provides them with up front working capital to produce and/or ship the goods, and security (no risk of no or late payments). Conversely, as an importer, a cash advance can cause cash flow problems for the business, and can be problematic if the goods aren’t up to standard, faulty, or not delivered on time.

Letters of Credit (LCs)

Letters of credit (LCs), also known as documentary credits are financial legally bound instruments, issued by banks or specialist trade finance institutions, which pay the exporter on behalf of the buyer, if the terms specified in the LC are fulfilled.
A LC requires an importer and an exporter, with an issuing bank and a confirming (or advising) bank respectively. The financiers and their creditworthiness are crucial for this type of trade finance: it is called credit enhancement – the issuing and confirming bank replace the guarantee of payment from the importer and exporter. In this section, and in most cases, we consider the importer as the buyer and the exporter as the seller.

A LC transaction generally happens as follows (Fig 1):

1. An importer agrees to buy goods off an exporter – a purchase order (PO) is issued
2. The importer will approach an issuing bank (trade financier) who will issue an LC if it fulfils their criteria (e.g. they are creditworthy)
3. The exporter will work with a confirming bank who will request the LC documents to be shipped from the issuing bank of the importer
4. The confirming bank will then check the LC and if the terms are correct, the exporter can then ship the goods
5. The exporter then sends the relevant shipping documents to the confirming bank, who will then process the payment
6. Once the confirming bank has examined the shipping documents in strict compliance against the LC terms from the issuing bank, they will forward these documents on to the issuing bank
7. The importer pays the issuing bank
8. The issuing bank then releases the shipping documents so that the importer can claim the goods that were shipped
9. The issuing bank then transfers money to the confirming bank who will then transfer this money to the exporter

LCs are flexible and versatile instruments (we will talk about the different types of LC below). The LC is universally governed by a set of guidelines known as the Uniform Customs and Practice (UCP 600), which was first produced in the 1930s by the International Chamber of Commerce (ICC).

Demystifying the Letter of Credit

The beauty of a LC is that it can meet a variety of needs that benefit both the buyer and the seller. For this reason the terms in a LC are important to
understand, we’ve put together a quick summary of terms that are common in LCs:

<table>
<thead>
<tr>
<th>Revocable</th>
<th>Irrevocable</th>
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<tbody>
<tr>
<td>The LC can be cancelled or changed at any time by the buyer or the issuing bank without notification. It is important to note that in the latest version of the UCP 600, revocable LCs have been removed for any transaction undertaken under their jurisdiction.</td>
<td>The LC cannot be unilaterally reversed, unless all parties (the issuing bank, confirming bank, buyer and seller agree).</td>
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<table>
<thead>
<tr>
<th>Confirmed</th>
<th>Unconfirmed</th>
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<tbody>
<tr>
<td>The status of a LC is ‘confirmed’ once the confirming bank (of the exporter) has added its obligation to the issuing bank. The obligation could be a guarantee or assurance of payment.</td>
<td>An unconfirmed LC is guaranteed only by the issuing bank (i.e., there is no confirmation by the advising bank). This type of confirmation is the most common in LCs, although where a jurisdiction has economic instability or political unrest, payment could be at risk.</td>
</tr>
</tbody>
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<table>
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<tr>
<th>Transferrable</th>
<th>Un-transferrable</th>
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<tbody>
<tr>
<td>If the beneficiary is an intermediary for the real suppliers of goods or services, the payment will need to be transferred to the actual suppliers.</td>
<td>An un-transferrable LC prevents payments from being transferred to third parties.</td>
</tr>
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<table>
<thead>
<tr>
<th>Straight</th>
<th>Negotiable</th>
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<tbody>
<tr>
<td>Here, the issuing bank has to pay the beneficiary.</td>
<td>The issuing bank is obligated to pay the beneficiary or any bank nominated</td>
</tr>
<tr>
<td><strong>Restricted</strong></td>
<td><strong>Unrestricted</strong></td>
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<tr>
<td>----------------</td>
<td>------------------</td>
</tr>
<tr>
<td>Only one advising bank can purchase a bill of exchange from the seller in the case of a restricted LC.</td>
<td>The confirmation bank is not specified, which means that the exporter can show the bill of exchange to any bank and receive a payment on an unrestricted LC.</td>
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<tr>
<th><strong>Term (Usance)</strong></th>
<th><strong>Sight</strong></th>
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<tbody>
<tr>
<td>Payment can be deferred in the case of a usance LC which gives time for the buyer to inspect or even sell the goods.</td>
<td>If a LC is at sight, it is payable as soon as the documents have been verified and presented.</td>
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</table>
Documentary collection

Documentary collections differ from a Letter of Credit.

In the case of DC, the exporter will request payment by presenting its shipping and collection documents to their remitting bank. The remitting bank then forwards these documents on to the bank of the importer. The importers bank will then pay the exporters bank, which will credit those funds to the exporter.

The role of banks in a documentary collection is limited, they do not verify the documents, take risks, nor do they guarantee payment; banks just control the flow of the documents.

With documentary collections, the bank does not cover credit and country risk, however, they are more convenient and more cost-effective than Letters of Credit and can be useful if the exporter and importer have a good relationship, and if the importer is situated in a politically and economically stable market.

Open Accounts

An open account is a transaction whereby the importer pays the exporter 30 – 90 days after the goods have arrived from the exporter. This is obviously advantageous to the importer and carries substantial risk for the exporter – it often occurs if the relationship and trust between the two parties is strong.

Open accounts help increase competitiveness in export markets, and buyers often push for exporters and sellers to trade on open account terms. As a result, exporters may seek export finance to fund working capital whilst waiting for the payment.

Often export credit insurance is taken out to reduce the risk of commercial losses such as bankruptcies, defaulting and insolvencies from the buyer.
Options for Trade Finance

What does a small business actually use trade finance for? We can categorize trade-financing options into: pre-shipment finance, post-shipment finance and supply chain finance (SCF).

Pre-shipment finance

Pre-shipment finance includes any finance that an exporter needs before they send goods to a buyer. Once the business has a confirmed order from a buyer, which is sometimes backed by a Letter of Credit, working capital finance is often required to fund wages, production costs and buying raw materials. Exporters can access receivables backed financing, inventory/warehouse financing and pre-payment financing.

Receivables-backed financing is essentially a loan where the goods exported are the security, so in the case of defaulting, the lender can seize the goods. Lenders will often fund up to 80% of the total value of the goods, but this can vary depending on the risk of exporting the goods and the lender. The goods being exported are also an important consideration for receivables-backed export lenders: if there is little demand for the goods (e.g., bespoke furniture or specialist circuits), a lender may not be able to resell in the case of commercial losses, therefore the risk is higher and they may be unwilling to finance the transaction.

Often lenders wish for goods to be kept in a trusted location or public warehouse (or in the borrower's premise but controlled by a third party). Warehouse or inventory financing is often favourable to borrowers for short term working capital or loans (especially if they have used up existing credit lines or bank overdraft facilities), and the inventory can be used as collateral or more flexible terms.

Pre-payment financing is subtly different to receivables-backed financing – in this case, the buyer will take out a loan specifically for the purpose of paying the seller in advance of shipping the goods, and the export contract states that the buyer pays the loan back to the bank once the seller fulfils the terms agreed. This process ensures speedy payment and the risks are shared with the
buyer and the bank.

**Post-shipment finance**

Once an exporter has shipped goods, a financier can advance the payment so they have sufficient liquidity between shipping the goods and receiving the payment. Post-shipment finance can operate in a number of ways: through a Letter of Credit, a loan via an accounts receivables document, or via invoice factoring or Receivables Discounting (selling the invoice or receivables document - see our report on invoice finance here).

**Supply chain finance (SCF)**

**What is supply chain finance?**

Both large corporations and small businesses need to import or export goods as part of their end-to-end supply chain. As a result of globalisation, supply chains are constantly being lengthened as a result of competition, increased efficiency and productivity from markets, and to diversify risk (i.e., purchasing one product from many suppliers). The catch all term ‘receivables management’ which covers GSCF and asset-based lending is predicted to be worth over USD $1.3tn per year.

Global supply chain finance, (also known as GSCF or supplier finance,) is a cash flow solution which helps businesses free up working capital which is trapped in global supply chains. It is a solution designed to benefit both suppliers and buyers; suppliers get paid early and buyers can extend their payment terms. This solution allows businesses which import goods to unlock working capital as well as reduce the risk associated with buying goods in bulk and/or transporting them globally (read more about risks of supply chain finance here).

**How does supply chain finance work?**

1. Normally a buyer will want to purchase goods from a supplier, who will invoice the buyer on standard credit terms (normally 1 month).
2. A supply chain finance institution, or a GSCF platform acting on behalf
of the buyer will remit the invoiced amount to the supplier, often paying early so that a discounted price (or early payment discount) can be applied.

3. The supply chain financier will then extend the payment from the buyer to a further 30-90 days, meaning the buyer has ultimately extended the payment period.

4. The financing rates are based on the buyer’s risk, the supplier will normally get paid instantly, and the rates are typically 10 times lower than using a traditional factoring agency.

Supply chain finance rates are 10 times lower than using traditional factoring facilities.

**Who can use supply chain finance?**

Currently, supply chain finance programmes exist predominantly in Western European and US markets, but Asian markets are quickly following suite, particularly India and China. Chief Financial Officers are beginning to include supply chain finance as part of their working capital and treasury agendas. Despite being around for over 70 years, supply chain finance is now being transformed by digital innovation. Proprietary software and technology platforms work with banks to automate and provide instant rates and terms which suit both parties. Payables data will typically get uploaded to a supplier platform and suppliers can immediately approve invoices and see invoices before they mature.

Supply chain finance is great for large corporations or SME suppliers/ buyers. Whether you’re looking to import automotives and vehicles or retail stock such as clothing, supply chain finance is an innovative solution which the UK government fully supports and encourages.

**What are the benefits of supply chain finance?**

<table>
<thead>
<tr>
<th>Benefits to buyers/ importers</th>
<th>Benefits to suppliers/ exporters</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buyers can maintain a healthy balance sheet</td>
<td>Suppliers can get paid earlier than their usual 30-day credit terms</td>
</tr>
<tr>
<td>Buyers maintain a good relationship</td>
<td>Little financial risk – insurance is sorted</td>
</tr>
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Trade Finance Global
<table>
<thead>
<tr>
<th>with suppliers</th>
<th>through a supply chain financier</th>
</tr>
</thead>
<tbody>
<tr>
<td>Promotes competition/diversity in suppliers</td>
<td>Doesn’t cost the supplier any extra</td>
</tr>
<tr>
<td>Allows buyers to make purchases in bulk to save costs</td>
<td>Allows supplier to have the cashflow to work on numerous deals simultaneously</td>
</tr>
<tr>
<td>Buyers can work with complex end-to-end supply chains</td>
<td>Helps with the provision of liquidity and reduces financing costs</td>
</tr>
<tr>
<td>SCF doesn’t disturb existing bank relationships or overdrafts</td>
<td></td>
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</tbody>
</table>
The risks of trade finance

What are the risks of Trade Finance?

In comparison, international trade carries substantially more risk than domestic trade. Due to differences in language, culture, politics, legislation and currency, understanding the dynamics and complexities of an international trade are important for buyers, sellers and lenders. Mitigating risk via the type and method of trade finance is crucial in ensuring successful trade. Below we have summarized the different types of risk under product, manufacturing, transport and currency risks.

**Product risks**

Product related risks are those which the seller automatically has to accept as an integral part of their commitment, for example, specified performance warranties, agreed maintenance or service obligations. The buyer must consider how external factors such as how negligence during production, or extreme weather during shipping could affect their product.

These matters could well lead to disputes between the parties, even after contracts are signed. It is important for the seller that the contract is worded correctly, such that any changes that could affect the product will by default include compensation or corresponding changes in the seller’s commitments.

**Manufacturing risks**

Manufacturing risks are particularly common for products which are tailor-made or have unique specifications. Often the seller would be required to cover costs of any readjustments of the product until the buyer sees fit, because the product can’t be resold to other buyers. Such risks can be addressed as early as the product planning phase, which often means the buyer has to enter payment obligations at a much earlier stage of the transaction.

To mitigate the risks for both the buyer and the seller, the terms of payment are often delivered into part-payments and separate guarantees throughout
the design, production and delivery of the product.

Transport risks

Aside from risks associated with the product itself, lies the movement of the goods from the seller to the buyer. Cargo and transport risks are reduced through cargo insurance, which is usually defined by standard international policy wordings (issued by the Institute of London Underwriters or the American Institute of Marine Underwriters).

One area of cargo insurance that a seller should be aware of is who should arrange the insurance – this is often determined by the agreed terms of delivery. Another area of cargo insurance is the risk of the buyer arranging insurance according to some terms of delivery. If the buyer fails to insure the cargo shipment in a proper way, the insurance could be invalid if, for example, the port or transport route changes and the items arrive in damaged condition.

Currency risks

In recent years markets have been difficult and foreign exchange levels have remained uncertain; more so than any time in history. All of these factors mean that the currency risk management strategy of a company needs to be strong. There is further pressure to reduce risk due to greater regulatory and governmental scrutiny involved in the financing markets and ever tightening margins.

Currency risk policies have historically taken a back seat and been relatively basic. There are a range of financial instruments available today and all need the correct risk management policies in place. Due to the increasing volatility seen in the market and the need to operate in various currencies, policies need to be flexible and cater accordingly.

Exchange rate volatility can affect all sizes of business, this is important when there are changes to the value of assets, liabilities and cash flows; this is certainly the case when denominated in a foreign currency. Volatility will also affect contracts where you have agreed to sell products at a future point internationally, or where such items are liable to exchange rate fluctuations.
These moves will have an effect on your profit margin.

Prior to developing a strategy, a company should look at what proportion of a business relates to imports or exports, the currencies that are being used, when payments are to be made, and what currency is used when payments and invoices are made.

Various strategies are used to manage currency risk and these usually involve using limit orders, options, forwards, stop-losses, and other risk management tools.
Trade finance providers

There are many service providers of trade finance; it is crucial that business owners choose the correct lending institution to access credit. Providers can generally be split into commercial banks and alternative finance institutions.

**What are commercial banks?**

Some commercial banks have specialised trade finance divisions, which offer facilities to businesses. Commercial banks represent the majority share of financial institutions globally, although they range in size from small and niche banks to large multinational banks.

The banking services offered by trade finance commercial banks include: issuing letters of credit, accepting drafts and negotiating notes, bills of exchange and documentary collections. The advantage over larger commercial banks over smaller niche banks is twofold: their global presence (they may have foreign subsidiaries which makes L/C confirmation cost effective), and their credibility.

Smaller domestic banks can however be advantageous to SMEs too – being niche, it can be easier to accommodate the specific (albeit riskier) needs of SMEs.

**Development Finance Institutions**

Development finance institutions (DFIs), also known as development banks, help provide trade finance to promote economic development. They are often country specific, and target specific types of mid- to long-term trade finance in the agricultural, mining and projects sector. Development finance institutions can provide standby letters of credit, discounting facilities, project financing and are often directly or indirectly funded by governments. DFIs often operate as joint ventures in emerging markets which means that they can provide insurance and guarantees given that the countries may face political and socio-economic risks.
**Alternative Finance and Non-Bank Funders**

There are many types of financial institutions that do not use public deposits as a funding resource. Funding sources include crowd-funded (pooled) investment, private investment and market brokering.

Traditional ‘receivables-backed finance’ has been disrupted by smaller finance platforms since the economic crisis. This has been driven by a decrease in appetite for risk by larger banks, which has opened the doors to risk averse smaller finance lenders, who can fill the gap. Private investment funds and larger banks back alternative trade financiers. Crowd-lending (peer to peer) finance have also entered the trade finance sector. In addition to this, new technologies to disrupt the somewhat lengthy application process for certain types of trade finance make it easier to assess risk, supply credit and documentation to importers and exporters have crept onto the scene.
Securing finance: the credit process

It is important to consider that every lender has specific requirements and criteria when lending. Some banks are very conservative in terms of risk appetite, others less so, and this also determines interest and repayment rates. There are often several requirements and a lengthy process when applying for a loan, and we’ve outlined the main stages of a loan credit process.

How to apply for a loan

1. Application

The initial ‘credit’ application drives the process when applying for credit. When a business goes to a bank of financial institution applying for trade finance, they will require you to provide truthful information about why you are seeking that specific type of loan, about yourself, and about your business.

Generally a business plan with financial forecasts is essential to show to a banker that your business idea is sound and realistic, you can implement it successfully, and that you know what the finance will be used for. Business plans vary in formats, but usually include the following:

- Thorough introduction to the business, including a future vision and the goals of the business and any significant business accomplishments to date.
- Information on the key stakeholders/ directors including past experience and stake in the company
- Introduction and an analysis of the product or service offered
- Overview of the sector/ competitor landscape
- Summary of anticipated results, including financial forecasts

Often lenders will ask for additional information that can help give an overview of the company or directors. This includes curriculum vitae/ resumes of the directors, articles of association and memorandum, the last 3-5 years of profit and loss accounts, references from banks, budgets and yearly forecasts, current invoices from suppliers or clients.
Lenders will often ask for information on current assets or collateral that the business owns, including debt and overdrafts, assets that the company or directors own (property, equipment, invoices).

2. Evaluating the Application

The lender will undertake a full credit risk assessment documents have been received. The credit analysis will usually involve inputting figures from the applicant’s income statement, balance sheet and cash flow documents. It will also take into consideration the collateral the SME can provide, and the quality of this.

The evaluation process will normally involve some kind of credit scoring process, taking into account any vulnerabilities such as the market the business is entering, probability of default and even the integrity and quality of management. A credit score is normally ranked from AAA (very low risk of default) to D (likely to result in the denial of a loan application).

What does a lender look at to determine an applicant’s credit?

- Key financial information
- Management / directors’ credentials
- Operating market / sector
- Risk of the transaction
- Analysis of the collateral

3. Negotiation

Eligible SMEs applying for trade finance can negotiate terms with lenders. An SME’s aim with a lender is to secure trade finance on the most favourable terms and price. Some of the terms that can be negotiated can include non-interest costs, fees and fixed charges, as well as interest rates.

If you’re prepared and understand the structure of fees and charges, it can help you negotiate terms that are in your favour. Sometimes it may be a good idea to seek advice from your local trade body to avoid any risks, understand the charges and the structure of the loan and insurance.
4. The Approval Process and Documentation of a Loan

Typically, the account officer who initially deals with the applicant and collects all of the documentation will do an initial credit and risk analysis. This then goes to a specific committee or the next level of credit authority for approval. If the loan is agreed (on a preliminary basis) it goes to the legal team to ensure that collateral can be secured/protected and to mitigate any risks in the case of default. Signatures will also be required from a senior director at the bank for the loan documents.

The loan document is a legal signed contract from both parties that consists of definitions, a full description of the trade finance facility that has been agreed (amount, duration, interest rates, currency and payment terms – both interest and non-interest charges). The conditions of a loan will also be included, which will state any obligations of the buyer and the lender, as well as what would happen in the case of any disputes or a default.

**Repaying the loans once approved**

In order to maintain a good relationship with the lender, repayment of an approved loan in a timely manner is essential (it also ensures the business has a good credit rating). Reputation as a borrower is crucial when growing a business – finance facilities and trade finance may not be a one time occurrence, and it can become easier and faster to get funding again once you establish a good reputation with your lender.

It is also important to remember the contractual and legal obligations that you have, as per the loan agreement.
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