Financing and Payments

Introduction to Financing and Payments

Understanding trade finance and payments helps exporters turn opportunities into sales and get paid for those sales in full and on time. A successful international transaction starts with the negotiation of a sales contract and ends with a timely payment. The buyer, or importer, gets the product or service they want and pays the seller, or exporter, a profitable amount in an agreed-upon timeframe.

Methods of Payment

There are four methods of payment in international trade:

Exporter	Methods of Payment	Importer
High Risk	Open Account	Low Risk
↑	Documentary Collection	↓
	Letters of Credit	
Low Risk	Cash-in-Advance	High Risk

Each payment method contains a varying level of risk for the importer and exporter. For exporters, a shipment is a gift to the buyer until payment is received. For importers, a payment is a donation to the exporter until goods or services are received. Therefore, exporters want to receive payment as soon as possible while importers want to delay payment as long as possible.

An appropriate payment method must be chosen carefully to minimize the payment risk to the exporter while accommodating the needs of the importer. To learn more about each payment method, see the following page.

(Source: U.S. Department of Commerce, International Trade Administration)

Financing and Payments Topics

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Cash-in-Advance

With cash-in-advance, the buyer pays the exporter before the shipment is made. This method is most beneficial for the exporter because it eliminates the risk of non-payment. Alternatively, cash-in-advance is the least attractive option for the buyer because it can create cash-flow problems and buyers will be concerned that the goods may not be sent if payment is made in advance.

Insisting on cash-in-advance can cause exporters to lose sales to competitors that offer more flexible payment terms. Partial or progress payments can also be used as cash-in-advance methods. The two most common payment methods for cash-in-advance are international wire transfers or credit cards. Exporters with internet-based businesses often use cash-in-advance by accepting credit card payments.

When to Use:

- The buyer is a new customer with unsatisfactory creditworthiness or operating history
- The political and commercial risks of the buyer's country are very high

Letters of Credit

A letter of credit (LC), also referred to as a documentary credit, is a commitment by the buyer's bank that payment will be made to the exporter, provided that the terms and conditions stated in the LC have been met. The buyer pays his or her bank to perform this service. Depending on the terms in the LC, payment can occur when the bank receives evidence that the goods have been shipped or delivered as promised, protecting both the buyer and seller.

LCs are one of the most secure payment methods available in international trade. An LC is a contract that should always be prepared by a well-trained professional. Banks deal strictly in documents and do not see or handle the actual goods, so the seller must strictly adhere to the terms and conditions in the LC and correctly prepare the necessary documents. Even the smallest discrepancy on a document can result in additional fees or prevent payment.

There are several variations of LCs, including Export, Sight, Time, Performance, and Stand-By. Confirmed LCs and transferrable LCs are also available. Exporters should always consult with their bank before an importer applies for a letter of credit.

(Source: U.S. Department of Commerce, International Trade Administration)

When to Use:

- The trade relationship is new or less-established
- Reliable credit information about a foreign buyer can't be found
- The exporter is satisfied with the creditworthiness of the buyer's foreign bank

For more information, refer to the International Trade Administration's Trade Finance Guide.

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Documentary Collections

A documentary collection (D/C), also referred to as a documentary draft, is a transaction in which the exporter's bank and the importer's bank act as payment facilitators and certain documents are used to transfer the title to the goods from the exporter to the importer. The importer pays the face amount of the draft either at sight (referred to as document against payment [D/P] or cash against documents) or on a specified date (referred to as document against acceptance [D/A] or cash against acceptance). The banks receive funds from the importer and transfer funds to the exporter in exchange for the documents.

D/Cs involve a slight risk for the exporter because there is no guarantee of payment. D/Cs are generally less expensive than letters of credit (LCs) and are filled out by the exporter. Using the documentary drafts process requires coordination and proper due diligence as to the customer's ability to pay, the country's economic conditions and international transaction laws, as well as communication with the freight forwarder. The documentary draft process signals more trust in the trade relationship between the exporter and importer.

When to Use:

- The exporter and importer have an established trade relationship
- The political and commercial risks of the buyer's country are low
- An open account is considered too risky and an LC is unacceptable to the buyer

Open Account

With an open account transaction, the goods are shipped and delivered to the buyer before payment is due. The exporter is extending credit to the buyer as a contractual relationship and the buyer agrees to pay at a later time, such as 30, 60, or 90 days after the date of the commercial invoice or bill of lading. The exporter's credit and collections or finance department monitors the buyer's account in their billing system and tracks when payment is due.

Open account payment terms are the most advantageous option for the buyer due to cash flow and cost. However, open account may also be considered the most risky payment term for the exporter and should not be offered until the importer has developed a good reputation for making payments.

Open account terms can be offered with the use of the trade finance techniques described on the following pages.

(Source: U.S. Department of Commerce, International Trade Administration)

When to Use:

- The exporter is fully confident that the buyer will accept shipment and pay in full and on time
- The political and commercial risks of the buyer's country are low
- The market is competitive and an attractive payment option must be offered to the buyer

For more information, refer to the [International Trade Administration's Trade Finance Guide](#).

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Export Financing Tools

Financing tools for U.S. exporters are offered by three key parties: (1) international banking institutions, (2) the U.S. Small Business Administration (SBA), and (3) the Export-Import Bank of the United States (Ex-Im Bank). Developing a relationship with an international banking institution is the best way to learn more about these tools and lessen the financial risks of international trade. As exporters discuss financing with their banks, it is important to have a basic understanding of the following export financing tools:

Export Working Capital Financing

Export working capital financing (EWC) provides funds for exporters to acquire materials, labor, inventory, and services to support export sales. This allows exporters to extend open account payment terms to buyers but does not eliminate the risk of non-payment. EWC is offered through commercial banks and is available to small and medium-sized businesses that have been profitable for at least one year. Export credit insurance and personal guarantees, receivables, or assets are often required to obtain EWC.

Government-Guaranteed Export Working Capital Loan Programs

The U.S. Small Business Administration and the Export-Import Bank of the United States offer loan guarantees to help U.S. businesses grow export sales. Government-guarantees for EWC loans are provided to commercial lenders so that they can provide financing to exporters. These programs are used when (a) financing is otherwise not available or (b) the exporter's borrowing needs are greater than the lenders' credit standards would allow.

Export Factoring

Export factoring allows exporters to transfer the title to short-term foreign receivables to a factoring house, or a factor, for cash at a discount from the face value. The factor assumes the risk of non-payment and handles collections. This allows the exporter to use open account payment terms and maximize cash flows. Export factoring is available to established small and medium-sized exporters with continuous sales of goods. Export factoring is offered by financial firms and is more expensive than export credit insurance.

Export Credit Insurance

Export credit insurance (ECI) protects U.S. exporters against the risks of non-payment by foreign buyers for political or commercial reasons. ECI is recommended when using open account terms and export working capital financing. ECI is offered through private insurance companies and the Export-Import Bank of the United States.

(Source: U.S. Department of Commerce, International Trade Administration)

Next Steps

- Review the SBA's loan programs and financing options for exporters: Visit SBA.gov
- Review Ex-Im Bank's services for commercial lenders and exporters: Visit ExIm.gov
- Discuss financing and payment options with your international banking institution

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Virginia Economic Development Partnership - International Trade offers a number of export-related services to Virginia businesses, including trade missions and market research by our Global Network of in-country consultants. These services are available to all Virginia exporters.

For more information, please visit our website: ExportVirginia.org

Additional Resources

Payment Terms & Financing Options	U.S. Commercial Service
International Trade Finance Guide	U.S. Commercial Service
Foreign Exchange Risk Management	U.S. Commercial Service
Guide to Export Finance	International Trade Administration
SBA Lenders by Zip Code	U.S. Small Business Administration
Ex-Im Lenders List	Export-Import Bank of the United States

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