Improvements in export finance

A comprehensive range of facilities is now available to the U.K. exporter for the finance of export credit. Earlier measures to stimulate exports by improving the facilities available to finance them had concentrated on capital goods, for which long credit terms are increasingly demanded by overseas buyers; and these facilities have been further improved in the last year, as is described later in this note.(1) But little had been done until recently to encourage those exporters who sell on short-term credit; yet something like one-quarter of all U.K. exports are sold on credit terms of up to six months. Admittedly, the cost of finance for such a short period is a far less important element in the final price of the goods—except where margins are very narrow—than it is in the case of long-term credit. Nevertheless, it is in general unsatisfactory that, when short-term rates are high, the facilities for financing exports should produce a rate structure which is more favourable to longer-term credit. This disparity has now been reduced by a new scheme, first mentioned by the Chancellor of the Exchequer in July last year. Details have been worked out with the banks, and were announced by the President of the Board of Trade on 8th March.

New scheme for short-term finance

Under the scheme, the London clearing banks and the Scottish and Northern Ireland banks have agreed to provide finance at Bank rate against eligible export instruments which have been unconditionally guaranteed by the Export Credits Guarantee Department. To be eligible, instruments must be either trade bills drawn on a foreign buyer, or promissory notes issued by him, and must have a tenor of between thirty days and two years. The interest rate will be the current Bank rate, with a minimum of $4\frac{1}{2}\%$, but it will vary as Bank rate varies, and will not be fixed for the whole term for which finance is provided, as it is in the case of longer-term export finance.(2) Previously, the average cost of short-term export finance was about 1% above Bank rate. The general benefit from the new scheme will therefore be a reduction of around 1% per annum in short-term financing costs. Equally important, however, it will enable an exporter to obtain finance immediately the goods have been shipped for the full amount of the bill without the bank having recourse against him.

The scheme will be open only to exporters who have held a standard E.C.G.D. comprehensive guarantee policy for at least a year.(3) For each exporter, the E.C.G.D. will set a limit to the amount of credit outstanding at any one time for which they are prepared to give an unconditional guarantee direct to his bank. This guarantee will cover 100% of the finance provided by the bank, plus the interest due on it. The premium payable by the exporter will be 2*s*. 6*d*. per annum for each £100 of the limit. Apart from interest on outstanding advances, the bank will make no charge for the facility.

The scheme will work as follows. As soon as the bill or promissory note is handed to the exporter's bank, the bank will provide finance

(1) Earlier improvements in finance for exports on medium and long-term credit were described in the *Bulletins* for March and June 1961, March 1962 and March 1965.

(2) March 1965 *Bulletin*, page 30.

(3) This facility was outlined in the June 1961 *Bulletin*.

(subject to the limit) for its full face value, and the E.C.G.D. guarantee will come into force. The guarantee may thus operate before the bill has been accepted. In addition to handing over the bill or promissory note, the exporter will have to provide his bank with evidence of shipment, and will have to warrant that the transaction is fully covered within the terms of his credit insurance policy with the E.C.G.D. If a buyer defaults on an accepted bill or promissory note the bank will claim on the E.C.G.D. If a buyer refuses to accept a bill, the bank will first ask the exporter for reimbursement, although the bank's effective rights of recourse will in fact be against the E.C.G.D., and not against the exporter. This means that if the exporter does not reimburse the bank, the latter will then claim from the E.C.G.D. On the other hand, the E.C.G.D. will have a counter-claim against the exporter for any payments they make to the bank in advance of claims on the credit insurance policy or for losses not covered by the policy.[1]

The new arrangement is not intended to affect the banks' liquidity position. Bills of six months' tenor or less covered by the scheme, or advances secured by such bills, may be counted as liquid assets for the purpose of calculating the banks' liquidity ratios; but a refinancing facility similar to that provided by the Bank of England for medium-term export credit[2] will not be extended to this short-term finance. The bills will not be regarded as marketable, though they will be transferable among the participating banks.

For the present, at least, the scheme will apply only to transactions where a negotiable instrument is available as evidence of the debt, on which action can be taken if payment is not made on the due date. Many short-term credit sales which are conducted on ' open account ' with overseas importers, with periodic settlements of balances due and without a bill of exchange or promissory note being drawn, will thus be excluded from the new arrangements; but it is hoped eventually to include them. The problems involved in extending the E.C.G.D. unconditional guarantee to transactions of this kind are now being examined.

Medium-term finance

Since the publication of the article in the March 1965 *Bulletin*, there have also been some improvements in the arrangements for medium-term export finance. E.C.G.D. unconditional bank guarantees, against which the banks provide medium-term finance at a fixed rate (currently $5\frac{1}{2}$%), were at that time available only for contracts worth at least £50,000 on credit terms of three years or more, and covered only 90% of the finance provided by the banks. In April 1965 the minimum credit period was reduced to two years and the cover was increased to 100%. In August the minimum value was reduced to £25,000. On 8th March 1966, at the same time as he gave details of the new short-term facility, the President of the Board of Trade announced that the E.C.G.D. would now be prepared to issue bank guarantees, in cases where the banks were agreeable, for contracts worth less than £25,000. Other improvements in E.C.G.D. facilities have been an increase in April 1965 from 85% to 90% in the cover given by comprehensive guarantees against buyer risks and successive reductions in premium rates. The additional premium for the unconditional guarantee to banks was halved in April 1965 and further reduced in May 1966. Virtually all other premiums were cut by 10% in June 1965 and also further reduced in May 1966, the size of the reductions varying according to the market and the type of cover. The effect of the latest cuts will be to reduce the E.C.G.D.'s charges by an average of 15%.

These changes in finance, for which thanks are due to the co-operation of the banks, mean that it will now be possible for post-shipment finance to be made available for exports at any term from thirty days upwards, without recourse by the bank to the exporter. For credit periods up to two years the interest rate will be the current Bank rate, but with a minimum of $4\frac{1}{2}$%; for periods over two years it will be a fixed rate of $5\frac{1}{2}$%.

(1) Claims on the policy are payable only after a specified waiting period; and the policy does not cover, for example, 100% of the loss or such contingencies as rejection of the goods by the buyer.

(2) Described in the *Bulletins* for March and June 1961 and March 1965.