



## Financial Institutions in Food Business

Day 3, Plenary Session I, 1000 Hrs-1115 Hrs, 19<sup>th</sup> Dec 2009, MSME DI, Guindy, Chennai

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**Tamil Nadu Technology Development & Promotion Center**

*An autonomous society of Government of Tamil Nadu and Confederation of Indian Industry*

# *Introduction to Indian Financial System*



# Before 1947

- Organised Financial Systems just begun
- Efforts to build our own system initiated
- Banks & financial systems were at infant stage
- No development Banks
- Motive of Colonial rule just to draw the wealth but NOT DEVELOPEMENT



# PRE 1991 ERA

- Gradual rise in the economy
- Emengence of independent banks & financial Institutions/ Development banks
- Thrust on providing finance to Industries & entrepreneurs
- Financial systems - Socialistic society based
- Public sector based economy
- Economic growth slow and financial systems had lot of hindrances and gaps



# POST 1991 ERA

- New Financial policies
- LPG- Liberalisation/Privatisation and Globalisation
- Reduced Govt Control on the economy growth
- Lead to faster economic growth
- Banks are development oriented
- Ensure funds –timely,adequate and cheap



# INCOTERMS



INTERNATIONAL COMMERCIAL TERMS

# INCOTERMS

- Abbreviation
- First used in 1936
- Formulated and published by international chamber of commerce
- ( ICC )
- Revised 1953, 1967, 1976, 1980, 1990, 2000
- Latest referred to as **incoterms 2000**.



# GROUPS



- 13 incoterms
- They fall in 4 groups
  - Departure (**E**)
  - Main carriage unpaid (**F**)
- Main carriage paid (**C**)
  - Arrival (**D**)
- Each gp. Letter make up the first letter of the incoterm

# 4 GROUPS OF INCOTERMS

**E GROUP - DEPARTURE**  
EXW

**D GROUP - ARRIVAL**  
DAF  
DES  
DEQ  
DDU  
DDP

**F GROUP – MAIN**  
**CARRIAGE**  
**NOT PAID BY**  
**SELLER**

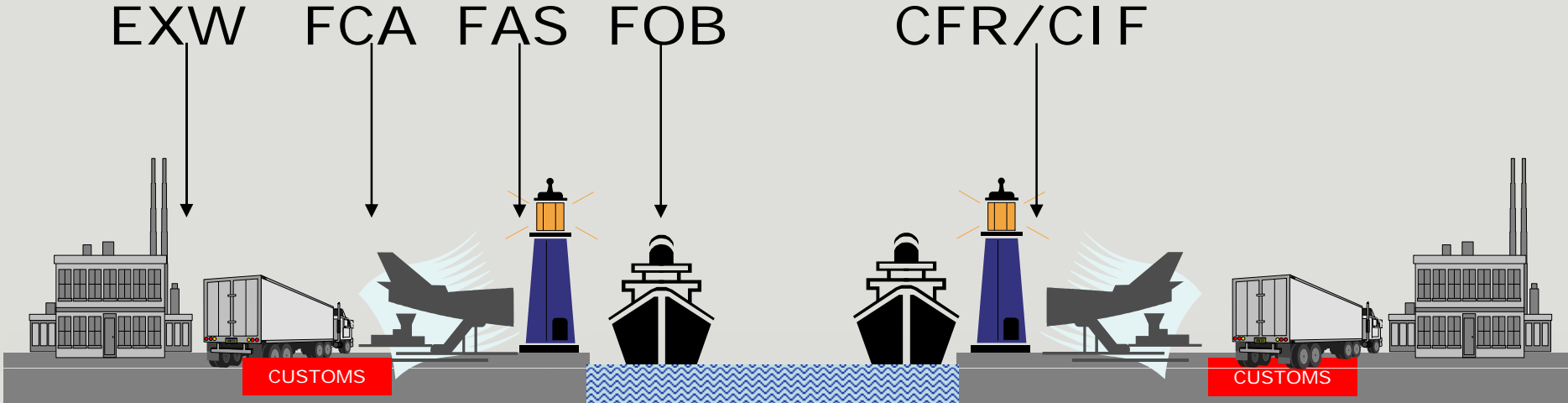
FCA  
FAS  
FOB

**C GROUP – MAIN**  
**CARRIAGE**  
**PAID BY**  
**SELLER**

CFR  
CIF  
CPT  
CIP



# DEPARTURE CONTRACTS



DES DEQ DDU DDP

# ARRIVAL CONTRACTS





- **EXW**
- Ex-works, named place where shipment is available to the buyer, not loaded.
- Seller will not contract for any transportation
- Minimum involvement of seller, maximum involvement of buyer.

# GROUP F

- **FOB** – Free on Board vessel, named ocean port of shipment
- Seller responsible for delivery at named port, custom clearance and loading on vessel
- Point of transfer of responsibility when goods pass ship's rail



# GROUP C

## MAIN CARRIAGE PAID BY SELLER



- **CFR** - Cost & Freight (...named port of destination)
- Seller responsible for custom clearance, delivery to named port of destination, unloading at destination and destination port charges
- It is a monomodal term and can only be used when main carriage is by sea
- **CIF** - Cost, Insurance & Freight (..named port)
- Similar to CFR with the addition of **insurance** as seller's responsibility.

# GROUP D

- **DDP**- Delivered duty paid ( named destination)
- Seller responsible for all costs and risks of delivery until destination.
- Seller responsible for import custom clearance  
and other payment of domestic duties in the buyer's country  
Door to Door service , seller bear entire risk until delivery

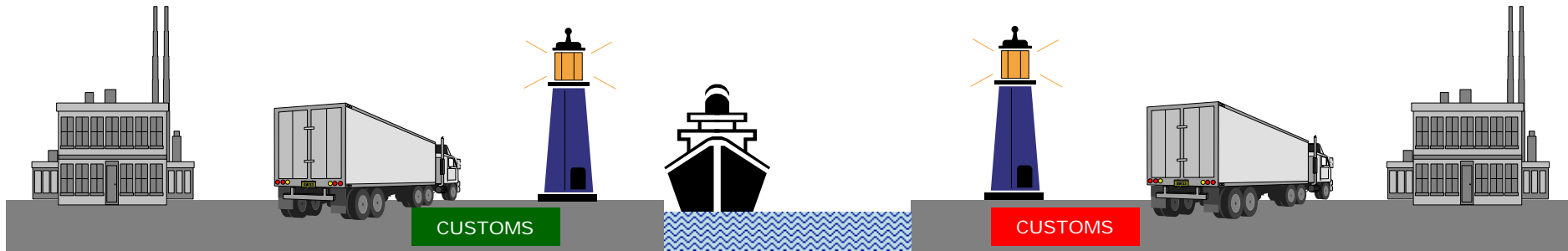


# TRANSFER OF RISKS

- EXW when goods are at the disposal of buyer
- FOB when goods pass the ship's rail
- CFR when the goods pass ship's rail
- CIF when the goods pass ship's rail
- DDP when goods are placed at the disposal of buyer



# FOB — free on board



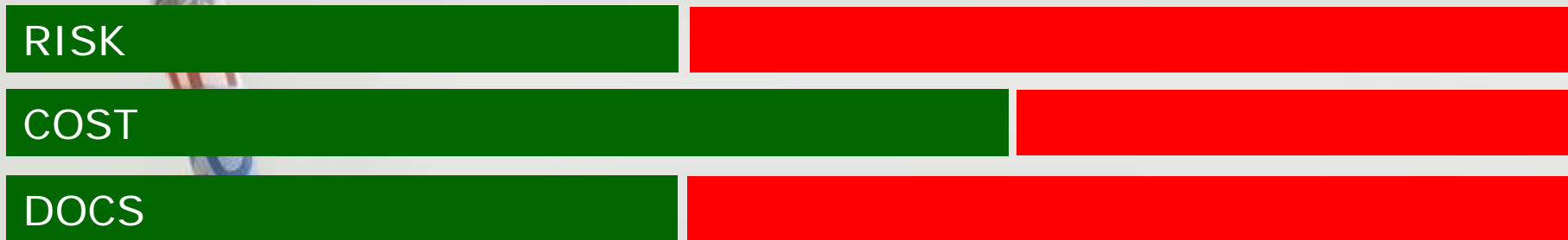
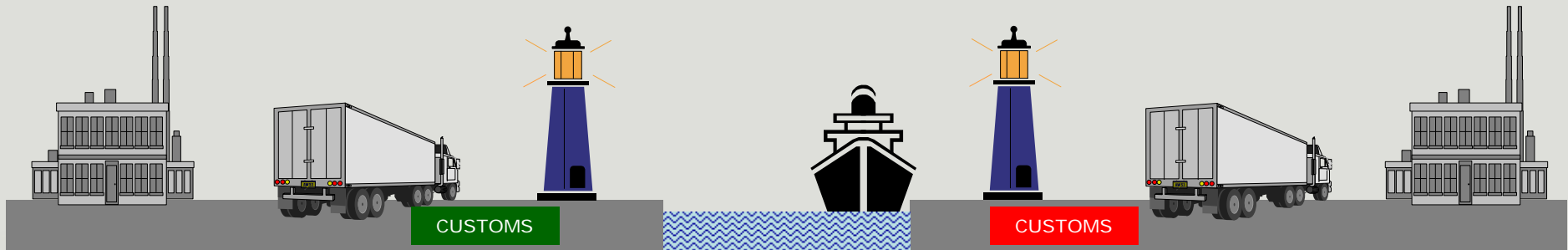
RISK

COST

DOCS

Loading costs of ship for account of **seller**

# CFR – cost, insurance, freight



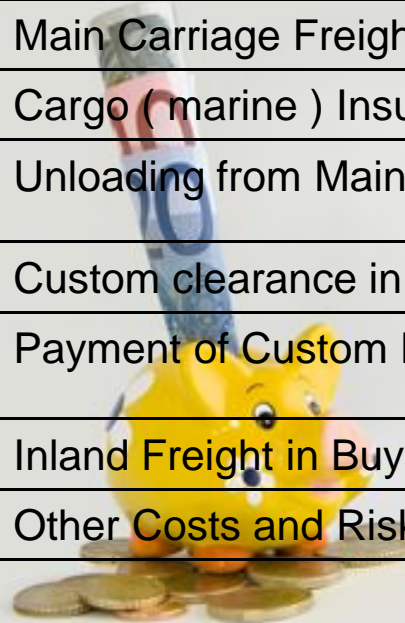
Loading costs of ship for account of **seller**

Unloading costs ship for account of **buyer**

CFR for countries where local insurance is mandatory

## **OBLIGATION UNDER EXW TERMS ( B - BUYER )**

Inland freight in India; delivery to carrier or frontier	Buyer
Export Custom clearance	Buyer
Payment of Custom Charges in India and Taxes	Buyer
Loading to the Main Carrier and Port Charges	Buyer
Main Carriage Freight	Buyer
Cargo ( marine ) Insurance	Buyer
Unloading from Main Carrier and Port Charges	Buyer
Custom clearance in Buyer's country	Buyer
Payment of Custom Duties and Taxes in Buyer's country	Buyer
Inland Freight in Buyer's country	Buyer
Other Costs and Risks in Buyer's country	Buyer



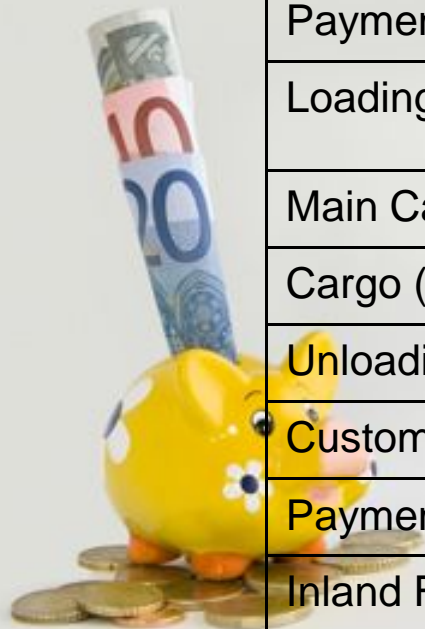
## OBLIGATION UNDER F TERMS ( B - BUYER ) ( S - SELLER)

	FOB
Inland freight in India; delivery to carrier or frontier	<b>S</b>
Export Custom clearance	<b>S</b>
Payment of Custom Charges & Taxes in India	<b>S</b>
Loading to the Main Carrier and Port Charges	<b>S</b>
Main Carriage Freight	<b>B</b>
Cargo ( marine ) Insurance	<b>B</b>
Unloading from Main Carrier and Port Charges	<b>B</b>
Custom clearance in Buyer's country	<b>B</b>
Payment of Custom Duties and Taxes in Buyer's country	<b>B</b>
Inland Freight in Buyer's country	<b>B</b>
Other Costs and Risks in Buyer's country	<b>B</b>



## OBLIGATION UNDER C TERMS ( B - BUYER ) ( S - SELLER )

	CFR	CIF
Inland freight in India; delivery to carrier or frontier	S	S
Export Custom clearance	S	S
Payment of Custom Charges & Taxes in India	S	S
Loading to the Main Carrier and Port Charges	S	S
Main Carriage Freight	S	S
Cargo ( marine ) Insurance	B	S
Unloading from Main Carrier and Port Charges	S	S
Custom clearance in Buyer's country	B	B
Payment of Custom Duties and Taxes in Buyer's country	B	B
Inland Freight in Buyer's country	B	B
Other Costs and Risks in Buyer's country	B	B



## OBLIGATION UNDER **D** TERMS (B - BUYER) (S - SELLER)



	DDP
Inland freight in India; delivery to carrier or frontier	<b>S</b>
Export Custom clearance	<b>S</b>
Payment of Custom Charges & Taxes in India	<b>S</b>
Loading to the Main Carrier and Port Charges	<b>S</b>
Main Carriage Freight	<b>S</b>
Cargo ( marine ) Insurance	<b>S</b>
Unloading from Main Carrier and Port Charges	<b>S</b>
Custom clearance in Buyer's country	<b>S</b>
Payment of Custom Duties and Taxes in Buyer's country	<b>B</b>
Inland Freight in Buyer's country	<b>S</b>
Other Costs and Risks in Buyer's country	<b>S</b>

# CONSOLIDATED CHART OF RESPONSIBILITY ( B - BUYER), ( S - SELLER )



	EXW	FOB	CFR	CIF	DDP
WH STORAGE	S	S	S	S	S
WH LABOUR	S	S	S	S	S
EXP PKG	S	S	S	S	S
LOADING CHARGES	B	S	S	S	S
INLAND FRT.	B	S	S	S	S
TERMINAL CHARGES	B	S	S	S	S
FORWARDING COST	B	B	S	S	S
LOADING ON VESSEL	B	S	S	S	S
SEA/ AIR FREIGHT	B	B	S	S	S
DESTINATION CHARGES	B	B	B	B	S
DUTIES./TAXES, CUSTOMS AT DEST	B	B	B	B	S
DELIVERY TO DEST.	B	B	B	B	

# PURPOSE

- Reduce confusions over interpretations
- To outline the obligations of buyers and sellers
- To state precisely when the shipper relinquish his obligation and when the buyer takes over



# Financial issues in export

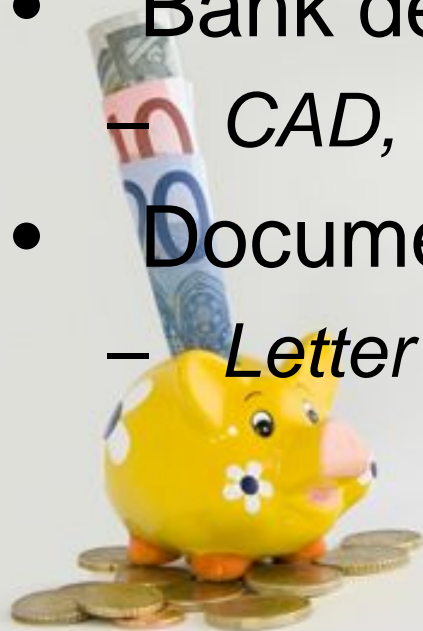
## Payment terms



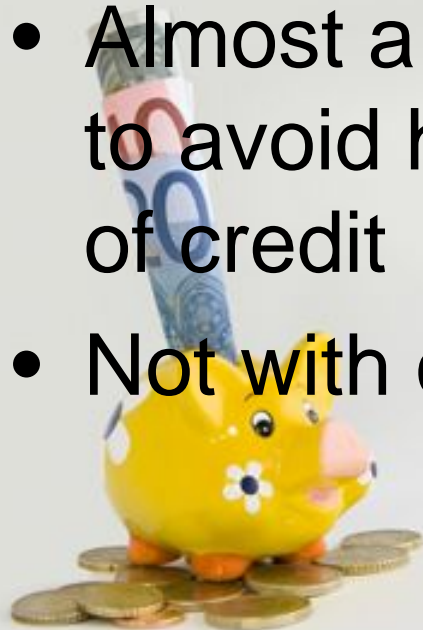
- Credit management
- Payment terms



- Direct payments
  - *Prepayment*
  - *Open account*
- Bank deliveries
  - *CAD, D/P, D/A*
- Documentary credits
  - *Letter of credit*



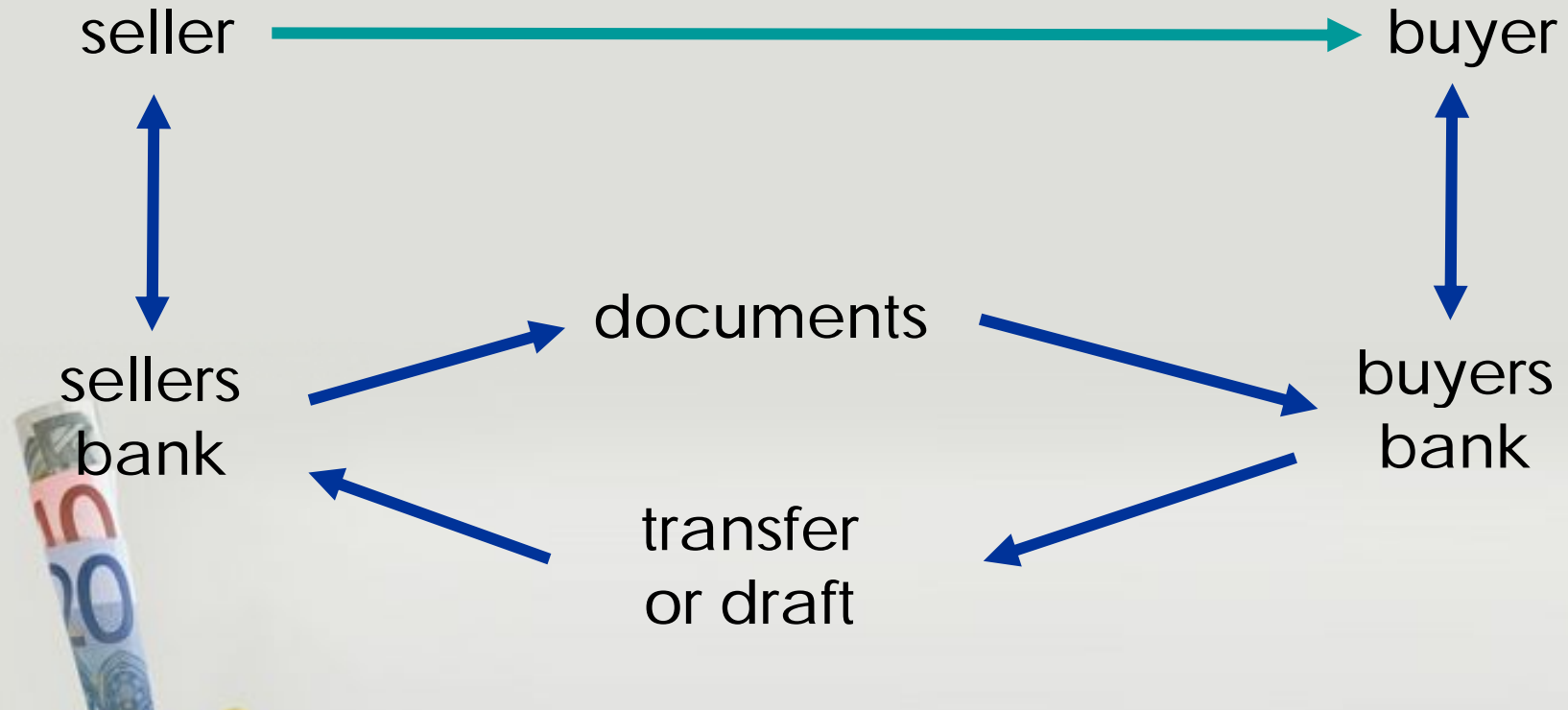
- *“You pay – I ship”*
- Most times not accepted
- Partly payments can be a solution
- Almost a must with new clients who want to avoid hassle with documents or letters of credit
- Not with consignment deliveries



- *“I ship - you pay”*
- Not with new customers
- Beware of the second and third order
- No risk management at all
- “The” way of doing business on the long run

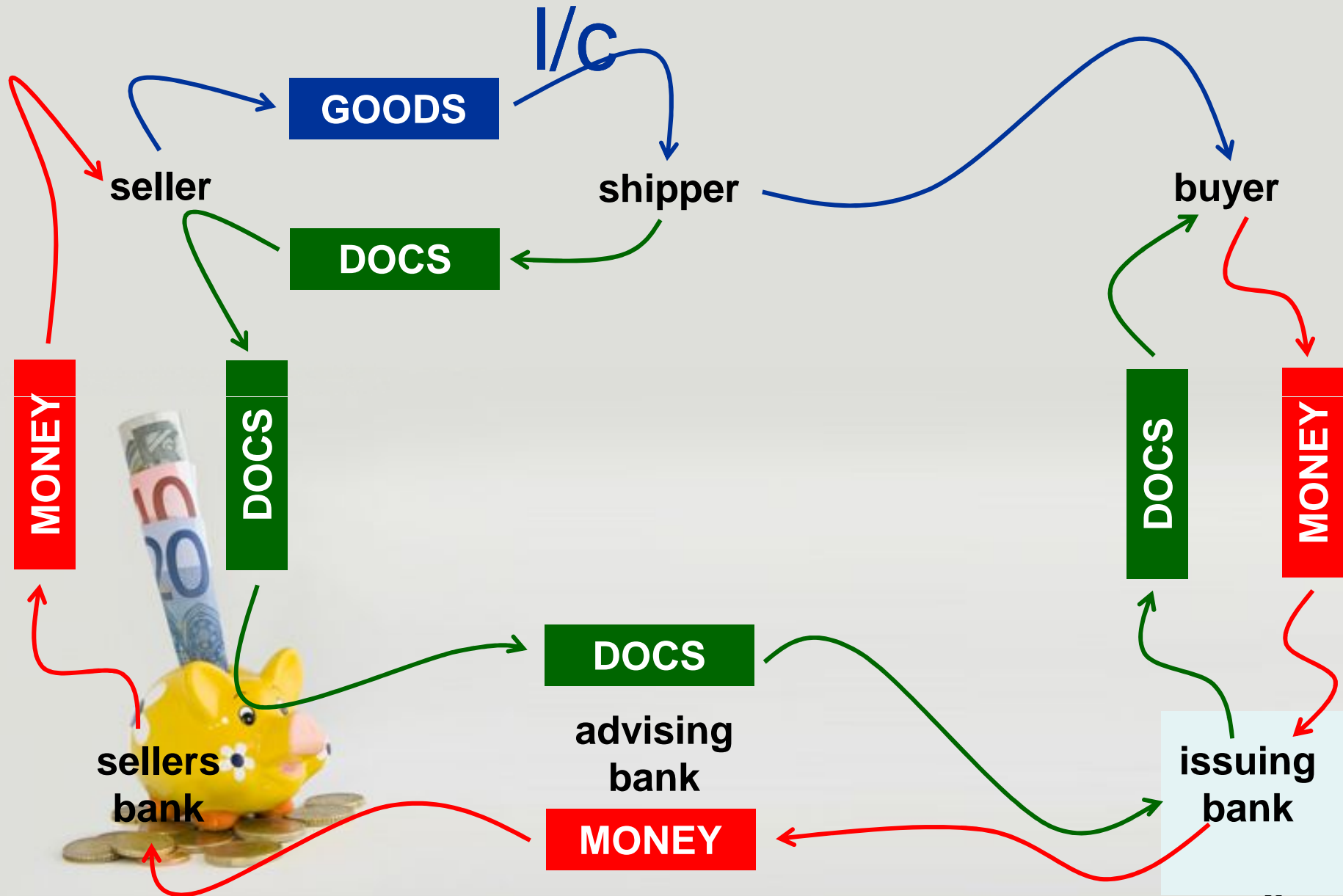


# 3. Bank deliveries

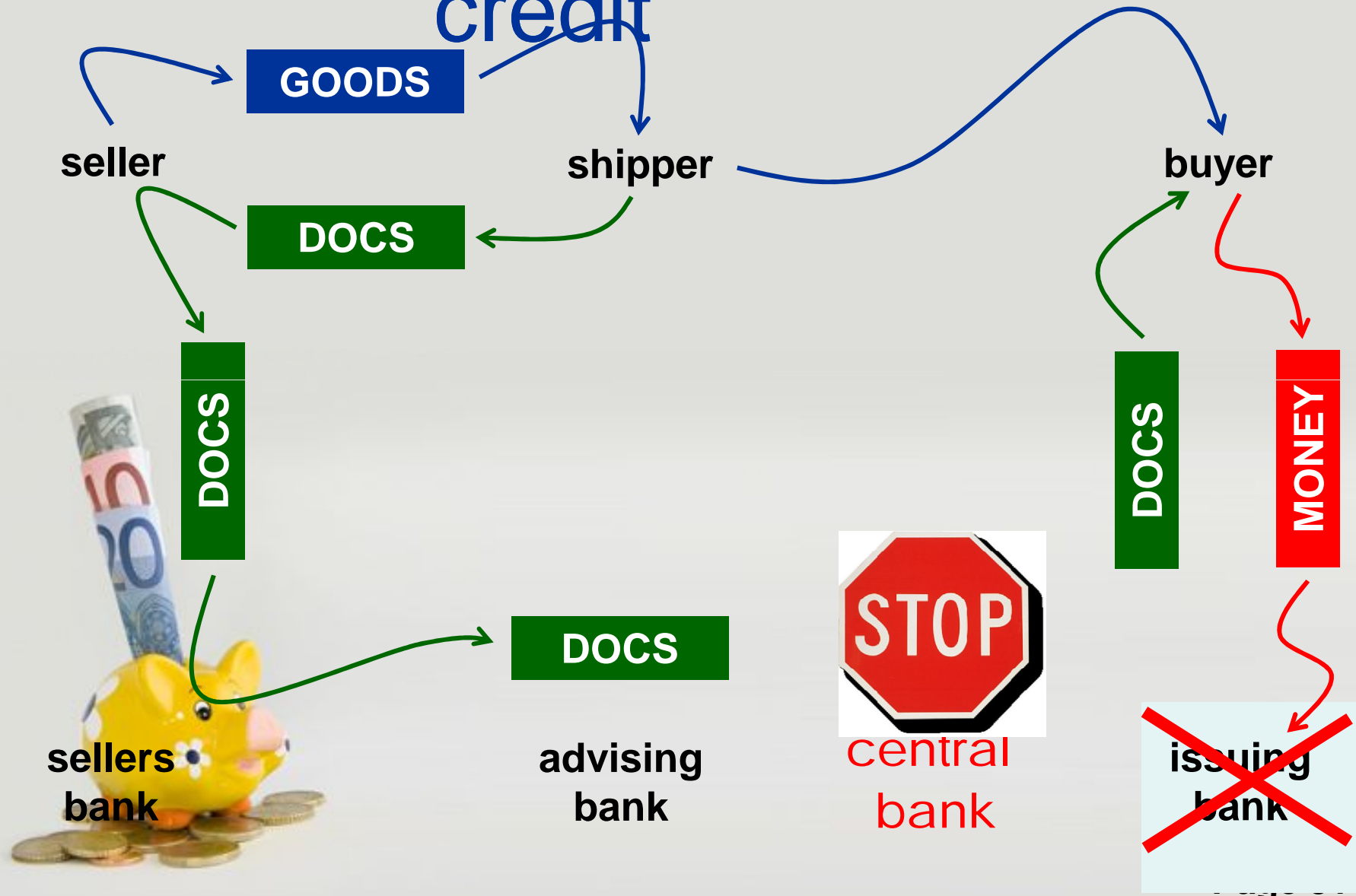


- ✦ CAD cash against documents
- ✦ D/P documents against payment
- ✦ D/A documents against acceptance (of draft)

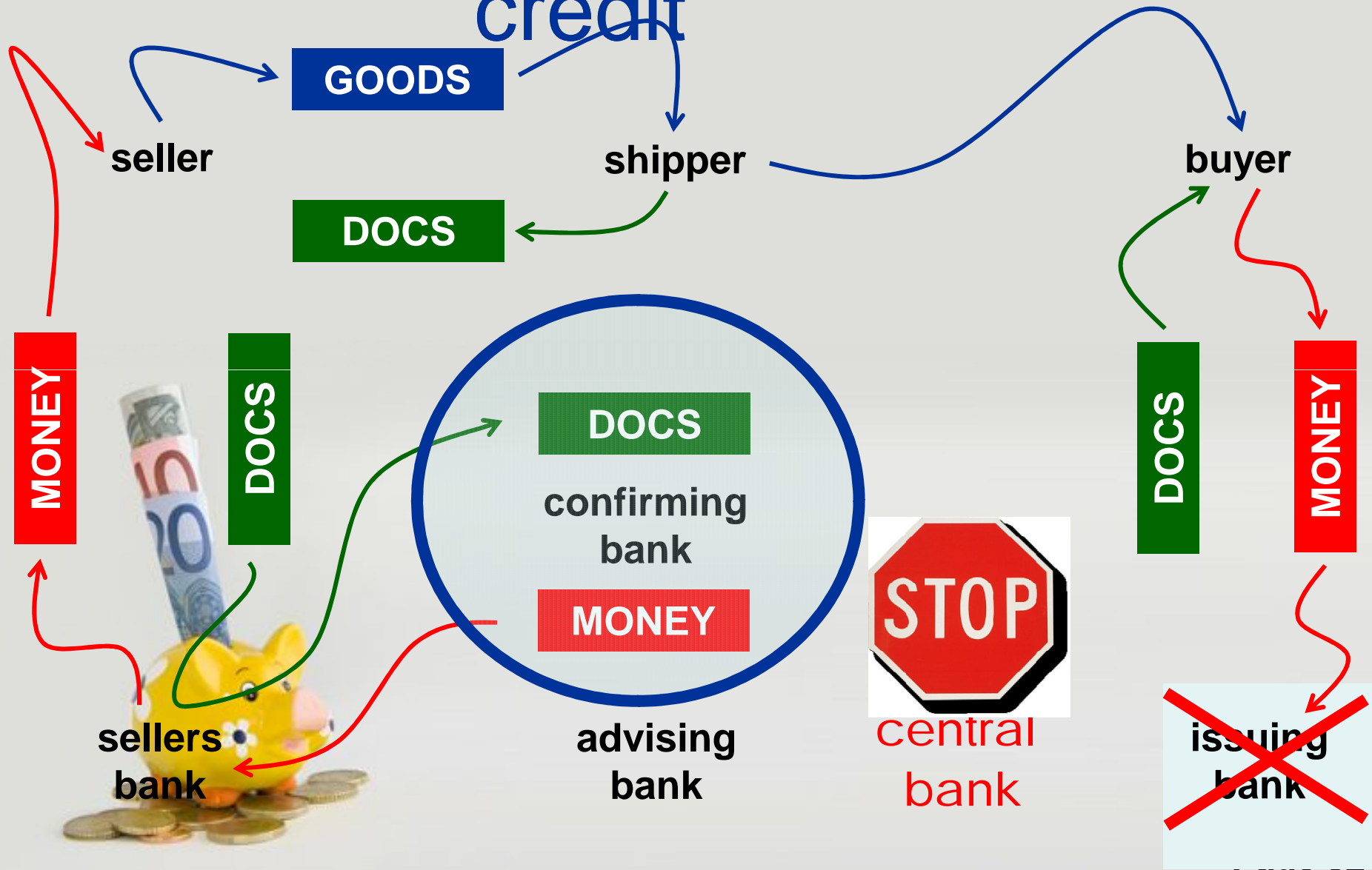
# 4. Documentary credit –



# Confirmation of letter of credit



# Confirmation of letter of credit



# “THE” letter of credit

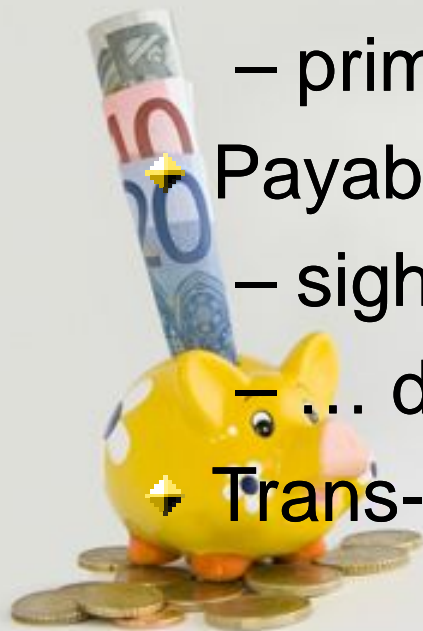
- ✦ Irrevocable
- ✦ Negotiable
- ✦ Confirmed by
  - prime US / EU bank

✦ Payable at

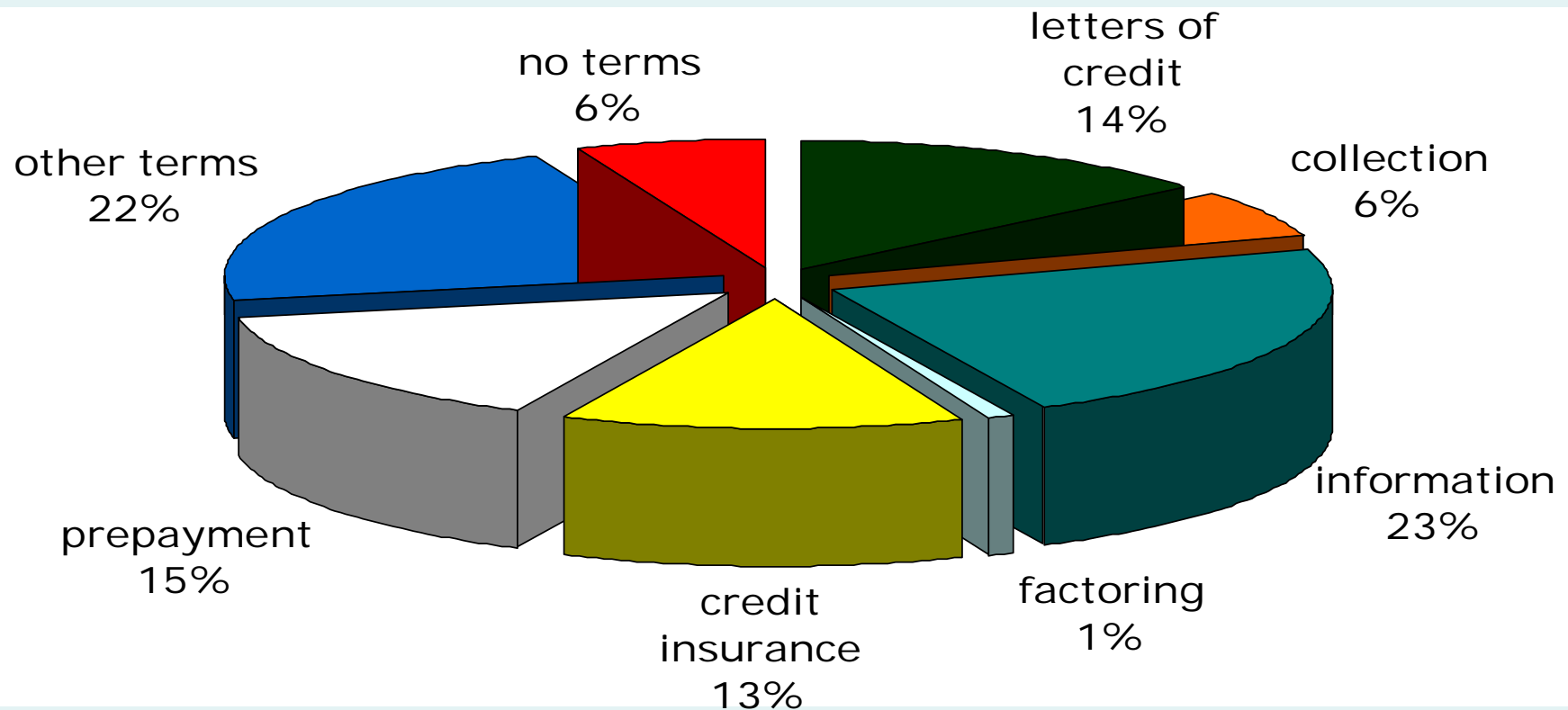
– sight

– ... days after date bill of lading

✦ Trans-shipments allowed

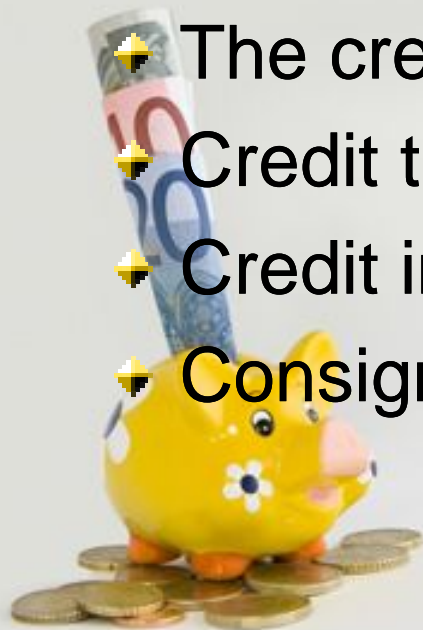


# credit instruments general level



# “The money” in a nutshell

- ✦ Only prepayment and I/c give guarantees
- ✦ Whom are you asking for a I/c ?
- ✦ The credit merry-go-around
- ✦ Credit terms : who has lowest financing ?
- ✦ Credit insurance limits
- ✦ Consignment and pre/post inspections



## Financial Issues in Exports

(preparing the company for exports)



\*Export Financing

\*Export Risks

Sources:

*\*Commercial banks (CB)*

- *All members of FEDA*
- *Provide loans at concessional rate*
- *Refinanced by RBI/EXIM Bank*

*\*Exim Bank of India*

- *Participate with CBs in providing medium term loans to exporters*

Other Related Institutions:

*\*Reserve Bank of India(RBI)*

- *Laydown Policy frame work & guidelines*
- *Refinances short & Medium*

*\*Export credit guarante corporation (ECGC)*

- *Guarantes cover for commercial political risks in export trade thro various policies*



## Export Financing- Forms

### Forms of Export Credit

Pre-shipment credit  
Post-shipment credit  
Forfaiting  
Factoring



# A. Pre-shipment Credit

## \* Pre Shipment Finance

- provided by financial institutions to Exporters before shipment.

## \* Objectives of pre shipment finance :

- Procure raw materials.
- Carry out manufacturing process.
- Provide a secure warehouse for goods and raw materials.
- Process and pack the goods.
- Ship the goods to the buyers.
- Meet other financial cost of the business.

## • Types

- Packing Credit
- Advance against Cheques /Draft etc. representing Advance Payments.

## • Forms :

- Packing Credit in Indian Rupee
- Packing Credit in Foreign Currency (PCFC)



# A. Pre-shipment Credit- Eligibility

- \*Exporter order in his own name
- \*Third party manufactures who don't have order in their own name
- \*Ten digit Import Export code (IEC) allotted by DGFT.
- \*Exporter not in the caution list of RBI
- \*Goods coming under the OGL or allotted under a license/quota
- \*Request for preshipment credit is writing & agree to submit documents in time.
- \*Firm order/irrevocable/fax from importer
- \*All details like buyer & address,product,quantity,value,goods,destination and last date of shipment.



# A. Pre-shipment Credit- Stages

- **Appraisal and Sanction of Limits**
  - Check Exporter profile, Product profile, political and economic details about country, and the exporters license/ permit
  -
- **Disbursement of Packing Credit Advance**
  - All the documents are properly executed.
  - Quantum of finance depend on the FOB value or the domestic values of goods, whichever is lower.
  - Insurance and freight charged are eligible
- **Follow up of Packing Credit Advance**
  - Exporter to submit stock statement
  -
- **Liquidation of Packing Credit Advance**
  - Liquidated out of the export proceeds of the relevant shipment, thereby converting PC to Post Shipment Credit
  - If No export. entire advance recoverable with interest
  -
- **Overdue Packing**
  - Packing credit as an overdue, if the borrower fails to liquidate the packing credit on the due date.
  - If the condition persists then the bank takes steps to recover



## A. Pre-shipment Credit –Other issues

- **Packing Credit Facilities to Deemed Exports**

Deemed exports are eligible for concessional rate of interest both at pre and post supply stages.

- **Packing Credit facilities for Consulting Services**

No physical movement of goods out of Indian Customs territory.

Pre-shipment finance can be provided to mobilize resources like technical personnel and training them.

- **Advance against Cheque/Drafts received as advance payment**

Direct payments from abroad by cheques/drafts eligible for credit till realization of the proceeds

Banks to satisfy proceeds are against an export order.



# B. Post-shipment Credit

## \* Purpose :

- Finance export sales receivables from date of shipment to dt of realization
- In Deemed exports, receivable against supplies made to designated agencies.

## • Basis :

- Against evidence of shipment of goods/supplies

## • Nature:

- Can be secured or unsecured.

## • Quantum :

- Up to 100% of the invoice value

## • Period :

- Short terms or long term as per Export Contract

## • Type of Exports covered:

- Physical exports, Deemed export ,Capital goods & Project exports.



## **B. Post-shipment Credit- Types**

- 1. Export Bills purchased/discounted.**
- 2. Export Bills negotiated**
- 3. Advance against export bills sent on collection basis.**
- 4. Advance against export on consignment basis**
- 5. Advance against un-drawn balance on exports**
- 6. Advance against claims of Duty Drawback.**



# Post-shipment Credit-types

## 1. **Export Bills Purchased/ Discounted : (DP & DA bills)**

Export bills (Non L/C Bills) discounted or purchased by the banks.

Indisputable export transactions within sanction limits

## 2. **Export Bills Negotiated (Bill under L/C):**

Banks prefer to extend the finance against bills under LC.

Two major risk factors for the banks:

- ✓ The risk of nonperformance by the exporter
- ✓ Documentary risk - issuing bank refuses to pay due to faulty documentation



# Post-shipment Credit-Types

**3. Advance Against Export Bills Sent on Collection Basis**

**4. Advance Against Export on Consignments Basis**

**5. Advance Against Undrawn Balance**

**6. Advance Against Duty Draw Back**



# Forfaiting

- ❑ Forfaiting refers to **non-recourse** discounting of export receivables.
- ❑ The exporter surrenders his rights to claim for payment
- ❑ Forfeiter pays exporter in cash & undertakes risk associated
- ❑ EXIM bank plays intermediary role
- ❑ Bank pays discounted proceeds to exporter.
- ❑ ADs to undertake forfaiting
- ❑ Involves two cost elements:  
Commitment fee to forfeiter and  
Discount fee to Bank



# Factoring

- A factor is an agent –offers services like coverage of credit risk, collection of export proceeds, maintenance of receivables & advance of funds.
- The Factor handle collection of export receivables and import collection services
- **Steps:**
  1. The exporter ships the goods to importer.
  2. The exporter assigns his invoices through the export factor to the import factor who assumes the credit risk
  3. The Export factor prepays invoices
  4. The importer pays the proceeds to Import factor
  5. The export factor deducts prepayment already made, other charges and pays the balance proceeds to the exporter.
- Factoring may be disclosed or undisclosed. Disclosed factoring is of two types: *Recourse factoring & Non-recourse factoring*



# Export Risks

- ***Risks in exports are quite different from risks involved in domestic trade. It is important to assess all the risks related to exports with an extra measure.***

- 1. Credit Risks***
- 2. Quality Risks***
- 3. Logistical Risks***
- 4. Country Risks***
- 5. Political Risks***
- 6. Currency Risks***
- 7. Unforeseen Risks***



# Export - Risks Management

## Six basic elements of risk management

- ✓ *Establishing the context*
- ✓ *Identifying the risks*
- ✓ *Assessing probability and possible consequences of risks*
- ✓ *Developing strategies to mitigate these risks*
- ✓ *Monitoring and reviewing the outcomes*
- ✓ *Communicating and consulting with the parties involved*

## Risks Mitigation methods

- ✓ **Direct Credit**
- ✓ **Guarantees**
- ✓ **Insurance**
- ✓ **Hedging**





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