

Sang Man Kim

Payment Methods and Finance for International Trade

 Springer

Payment Methods and Finance for International Trade

Sang Man Kim

Payment Methods and Finance for International Trade

 Springer

Sang Man Kim
International Trade
Duksung Women's University
Seoul, Korea (Republic of)

ISBN 978-981-15-7038-4 ISBN 978-981-15-7039-1 (eBook)
<https://doi.org/10.1007/978-981-15-7039-1>

© The Editor(s) (if applicable) and The Author(s), under exclusive license to Springer Nature Singapore Pte Ltd. 2021

This work is subject to copyright. All rights are solely and exclusively licensed by the Publisher, whether the whole or part of the material is concerned, specifically the rights of translation, reprinting, reuse of illustrations, recitation, broadcasting, reproduction on microfilms or in any other physical way, and transmission or information storage and retrieval, electronic adaptation, computer software, or by similar or dissimilar methodology now known or hereafter developed.

The use of general descriptive names, registered names, trademarks, service marks, etc. in this publication does not imply, even in the absence of a specific statement, that such names are exempt from the relevant protective laws and regulations and therefore free for general use.

The publisher, the authors and the editors are safe to assume that the advice and information in this book are believed to be true and accurate at the date of publication. Neither the publisher nor the authors or the editors give a warranty, expressed or implied, with respect to the material contained herein or for any errors or omissions that may have been made. The publisher remains neutral with regard to jurisdictional claims in published maps and institutional affiliations.

This Springer imprint is published by the registered company Springer Nature Singapore Pte Ltd. The registered company address is: 152 Beach Road, #21-01/04 Gateway East, Singapore 189721, Singapore

Preface

This book covers various methods of payment in international trade and trade finance schemes for international trade. In addition, this book also overviews the concepts, purposes, features, and risks of international trade.

Companies engage in international trade transactions for various purposes. Maximizing corporate value by increasing revenues and profits will be the ultimate goal for most companies. Companies engaging in international trade transactions are likely to gain more revenue and profits.

International trade transactions, however, bring various risks that originate from the features of international trade transactions. Exporters may not get paid even after the performance of a contract. The risk of non-payment is largely dependent on the method of payment.

In international trade, the number of documents required will vary depending on the individual transaction. Documents come in two types: financial documents and commercial documents. Financial documents mean bills of exchange, promissory notes, checks, or other similar instruments used for obtaining the payment of money, while commercial documents mean invoices, transport documents, documents of title, or other similar documents.

The basic methods of payment in international trade are “payment in advance” (cash in advance), “open account”, “documentary collection”, and “documentary credit” (letter of credit). Other types of method of payment, such as “consignment”, “netting”, and “bank payment obligation”, are also used. Each of the methods of payment has advantages and disadvantages to the respective parties.

Some methods of payment might bring detrimental losses rather than profits, and also cause cash flow problems. In negotiating methods of payment, companies need to consider trade finance as well as non-payment risk. There are various types of trade finance normally used in international trade: pre-shipment finance, post-shipment finance, export working capital financing, negotiation of bills of exchange (or discounting invoices), export factoring, international forfaiting, export credit insurance (export credit guarantee), etc.

The understanding of various methods of payment in international trade together with the relevant trade finance scheme is a key factor for a successful international trade transaction. The understanding of the features and risks of international trade will help to understand the various methods of payment.

For the successful completion of an international trade transaction, depending on the terms of the transaction, both parties need access to funds. Small and Medium-Sized Enterprises (SMEs), compared to large companies, often face difficulties in raising capital or funds. Financing an international trade transaction is often key to successful completion. There are various financing mechanisms available for international trade transactions. Besides financing ability, the choice of a proper financing mechanism is also important for the successful completion of an international trade transaction.

For successful completion of an international trade in goods or services, depending on the payment terms and other conditions of a particular transaction, both exporters and importers need access to funds. Thus, it is important to understand the trade finance mechanisms for the successful completion of an international trade. The ability to allow longer payment terms has become a competitive factor in international trade. However, long payment terms bring cash flow shortage to an exporter. Thus, an exporter needs to obtain trade finance in order to make up the cash flow shortage arising out of an international trade transaction with long payment terms.

Exporters preparing the performance of export transactions are frequently in need of finance for the performance of the transactions (or for delivery of the goods). Such finance is called pre-shipment finance. Exporters are also in need of finance after the performance of the transactions (or after delivery of the goods) because they get paid long after transactions are completed. Such finance is called post-shipment finance. Post-shipment finance includes negotiation of bills of exchange and/or documents, forfaiting, and factoring.

Export credit insurance (or export credit guarantee) is very useful for the facilitation of pre-shipment finance and of post-shipment finance. Therefore, it is considered one of the financing mechanisms available in international trades.

Many countries have established export credit agencies to promote exports through various support mechanisms, including export credit insurance (or export credit guarantee). Its main aim is to promote exports by protecting exporters from commercial and political risks.

Export credit insurance (or export credit guarantee) promotes a country's exports by giving a variety of advantages to its exporters. The key functions of export credit insurance include reducing non-payment risks, offering competitive payment terms, increasing exports with reduced non-payment risk and competitive payment terms, creating easy and accessible trade financing solutions, etc. When an export credit insurance (or export credit guarantee) backs an exporter's foreign receivables, commercial banks are often willing to lend to an exporter with favorable terms against foreign receivables, otherwise excluded from the borrowing base.

This book provides a comprehensive treatment of methods of payment in international trade accessible to those less familiar with the subject matter. This book provides various examples and figures for trade documents, each method of payment, trade finance scheme, etc.

This book will be a valuable reference for experienced managers and bankers in international trade. This book can be used as a guide book or a manual for new employees in trading companies. It can also be used as a college textbook for a one-semester course for upper-level undergraduate or graduate students.

This book is based on the author's practices as a legal consultant and underwriter for export trades, and researches as a professor of international trade. The figures were created or modified by the author.

Seoul, Korea (Republic of)

Sang Man Kim

Contents

- 1 Introduction to International Trade 1**
 - 1.1 Concept of International Trade 1
 - 1.2 Purposes of Engaging in International Trade. 2
 - 1.2.1 To Increase Revenues and Profits: The Exporter’s Perspective. 2
 - 1.2.2 To Use Production Capability Fully and Sell Excess Products: The Exporter’s Perspective. 3
 - 1.2.3 To Learn or Acquire Advanced Technology: The Importer’s Perspective 3
 - 1.2.4 To Meet Domestic Demand: The Importer’s Perspective. 3
 - 1.3 Features of International Trade 4
 - 1.3.1 Different Laws and Standards 4
 - 1.3.2 Government Control and Intervention 4
 - 1.3.3 Complex Documents 5
 - 1.3.4 Different Customs and Cultures. 5
 - 1.3.5 Different Languages 6
 - 1.3.6 Different Currencies 6
 - 1.3.7 Long Distance 6
 - 1.4 Risks in International Trade. 6
 - 1.4.1 Introduction 6
 - 1.4.2 Risk Factors 8
 - 1.4.3 Commercial Risk and Country Risk 12
 - References 14
- 2 International Trade Contracts 15**
 - 2.1 Concept of a Contract 15
 - 2.2 Formation of a Contract 17

2.2.1	Requirements for the Formation of a Valid Contract	17
2.2.2	The Process of Offer and Acceptance	19
2.2.3	Information Included in an International Sale Contract	20
2.2.4	Ordering Process	22
2.3	Performance of a Contract	22
2.3.1	Obligations	22
2.3.2	Breach of Contract	22
2.3.3	Various Examples of Contract	23
	References	28
3	Documents for International Trade	29
3.1	Introduction	29
3.2	Commercial Documents	30
3.2.1	Transport Documents	30
3.2.2	Commercial Invoices and Other Documents	32
3.2.3	Specimen and Examples	34
3.3	Financial Documents	42
3.3.1	Bill of Exchange (Documentary Draft)	42
3.3.2	Promissory Note	47
3.3.3	Payment of Bill of Exchange and Promissory Note	48
	References	49
4	Overview of Payment Methods	51
4.1	Introduction	51
4.2	Basic Types of Payment Method	53
4.3	Case Study for Respective Methods of Payment	57
4.3.1	Payment in Advance (Cash in Advance)	57
4.3.2	Open Account	57
4.3.3	Documentary Collection	58
4.3.4	Documentary Credit	59
	References	61
5	Payment in Advance (Cash in Advance)	63
5.1	Introduction	63
5.2	Operation of a Payment in Advance	64
5.2.1	Telegraphic Transfer (Bank Transfer, Wire Transfer)	64
5.2.2	Credit Card	65
5.2.3	Payment by Check	65
5.2.4	Electronic Payment	65
5.3	Advantages/Disadvantages	66

5.3.1	Advantages/Disadvantages	66
5.3.2	When to Use Payment in Advance	66
	References	67
6	Open Account	69
6.1	Introduction	69
6.2	Operation of an Open Account	70
6.3	Features and Advantages/Disadvantages	72
6.3.1	Features (Comparison with a Documentary Collection)	72
6.3.2	Advantages and Disadvantages	72
	Reference	73
7	Documentary Collection	75
7.1	Introduction	75
7.2	Operation of a Documentary Collection	77
7.2.1	Overview	77
7.2.2	Parties to a Documentary Collection	77
7.2.3	Documents Against Payment	79
7.2.4	Documents Against Acceptance	81
7.2.5	Collection Instruction	83
7.3	Features and Advantages/Disadvantages	84
7.3.1	Features	84
7.3.2	Advantage/Disadvantage	85
7.4	The Uniform Rules for Collections	86
	References	89
8	Documentary Credit	91
8.1	Introduction	91
8.1.1	The Background	91
8.1.2	History	92
8.1.3	Concept	93
8.2	Operation of a Documentary Credit	94
8.2.1	Flow of a Documentary Credit Transaction	94
8.2.2	Application and Issuance of a Documentary Credit	94
8.2.3	Responsibilities of the Advising Bank	97
8.2.4	Presentation of Documents	98
8.2.5	Advantages/Disadvantages	100
8.3	Various Types of Credits	101
8.3.1	Basic Types of Credit Under UCP	101
8.3.2	Other Forms of Credit	102
8.4	Independence Principle and the Fraud Exception	105
8.4.1	Independence Principle	105
8.4.2	Complying Presentation and Strict Compliance	105
8.4.3	Fraud Exception	106