HSBC Bank USA, N.A.
Trade and Supply Chain

ECIDA 2011 International Business Seminar

Financing Exports in 2011
And Beyond

HSBC
The world's local bank

MAJOR RISKS

Major Risks

- **Political Risk**
  - War, civil disturbance, or revolution
  - Expropriation
  - Inconvertibility of local currency into dollars or other hard currency. (Transfer Risk)
- **Commercial Risk/Business Risk**
  - Disputes between buyer and seller.
  - Controlling title to goods pending payment.
  - Customer illiquidity or insolvency
  - Inability to finance company “investment” in export accounts receivable
  - Control of quality of goods.
  - Working capital tied up
  - Increasing reliance on bank debt.
- **Documentary Risk**
- **Interest Rate Risk**
- **Foreign Exchange Risk**

Trade and Supply Chain & HSBC

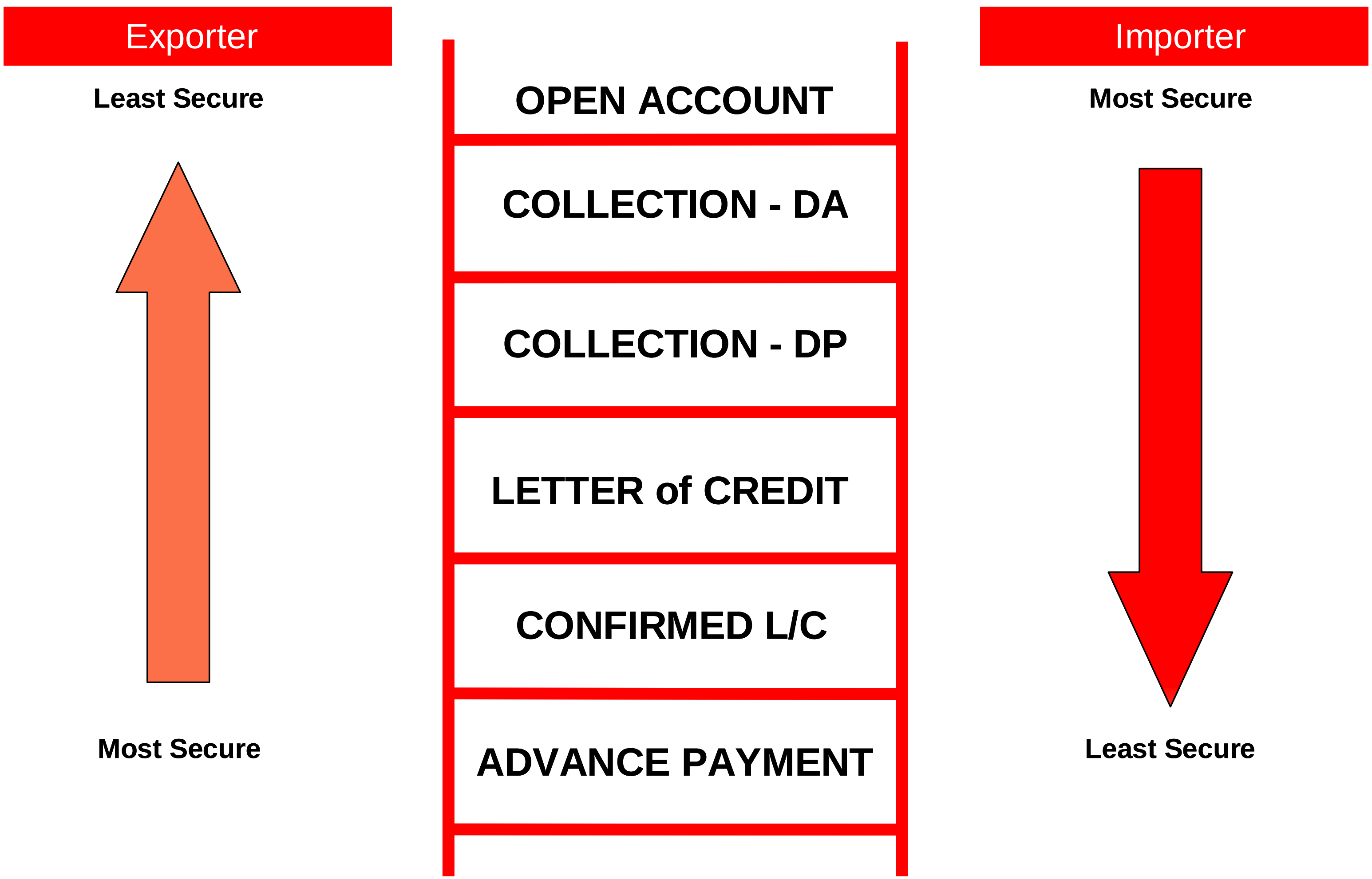
- **Banks major role in International Trade is to assist clients in**
  - Mitigating risk
  - Effecting Payment
  - Providing a level of trust and integrity to the transaction between two parties that are frequently not well known to each other
- **In any trade arrangement, a conflict of wants exists between:**
  - Supplier
    - Wants payment for the goods
    - Wants payment prior to shipment of the goods
  - Buyer
    - Wants to receive the correct goods
    - Wants goods at the right time
    - May want credit terms
- **Trade and Supply Chain assists in bridging the gap between these conflicting wants**

METHODS OF PAYMENT REVIEW

Payment Methods Review

- **The choice of payment is determined by:**
  - Buyer's Credit Standing
  - Supplier's Financial Condition
  - Competition for the Sale
  - Industry Practice
  - Amount of the Transaction
  - Regulatory Environment
- **Primary Payment Methods:**
  - Payment in Advance
  - Open Account
  - Documentary Collections
  - Documentary Letter of Credit

What is Trade Finance About? Risk Management



Relying on Counterparty risk

PAYMENT IN ADVANCE

OPEN ACCOUNT

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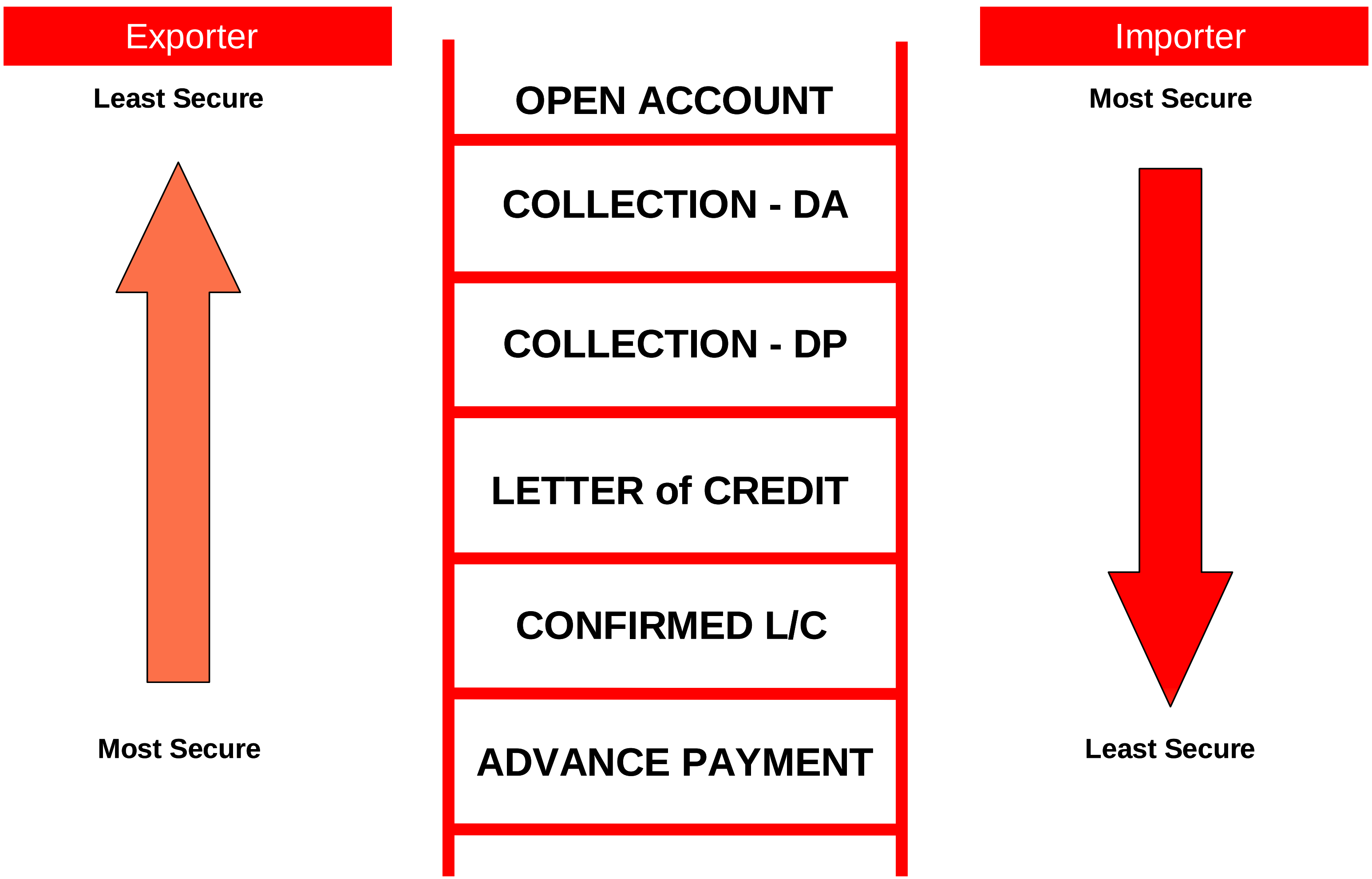
Payment In Advance/ Open Account

- **Payment in Advance:**
  - Buyer remits funds before the goods are shipped
  - Supplier ships after the funds are received
  - Buyer at risk:
    - Non-shipment by the seller
    - Quality of goods shipped
    - Exchange controls frustrating payment
    - Negative impact on cash flow
- **Open Account**
  - Goods dispatched directly to Buyer
  - Buyer pays on receipt/ after a specified period
  - Supplier at risk:
    - Non-payment by Buyer
    - Exchange controls may frustrate payment
    - Negative impact on Supplier's cash flow

DOCUMENTARY COLLECTIONS

What is Trade Finance About? Risk Management



Documentary Collections

Definition

- A payment mechanism initiated by the Exporter, using the services of a bank, to collect payment from the Importer
- This is done by forwarding documents, most importantly title documents, through agreed banking channels

Types of Payment

- D/P: Release of Documents against Payment- Documents are not released until payment is made by the Importer
- D/A: Release of Documents against Acceptance- Documents released upon the promise of payment at a future date as evidenced by a draft drawn on and accepted by the Buyer

Documentary Collections- Risk Profile

Benefits:

1) Supplier cr
required

2) If D/A term
before paymen

3) Cheaper th

Key Risks:

1) Shipment sc
be controlled.

2) If payment

Benefits:

1) Under D/P l
of the goods th

2) Under D/P, c
payment is ma

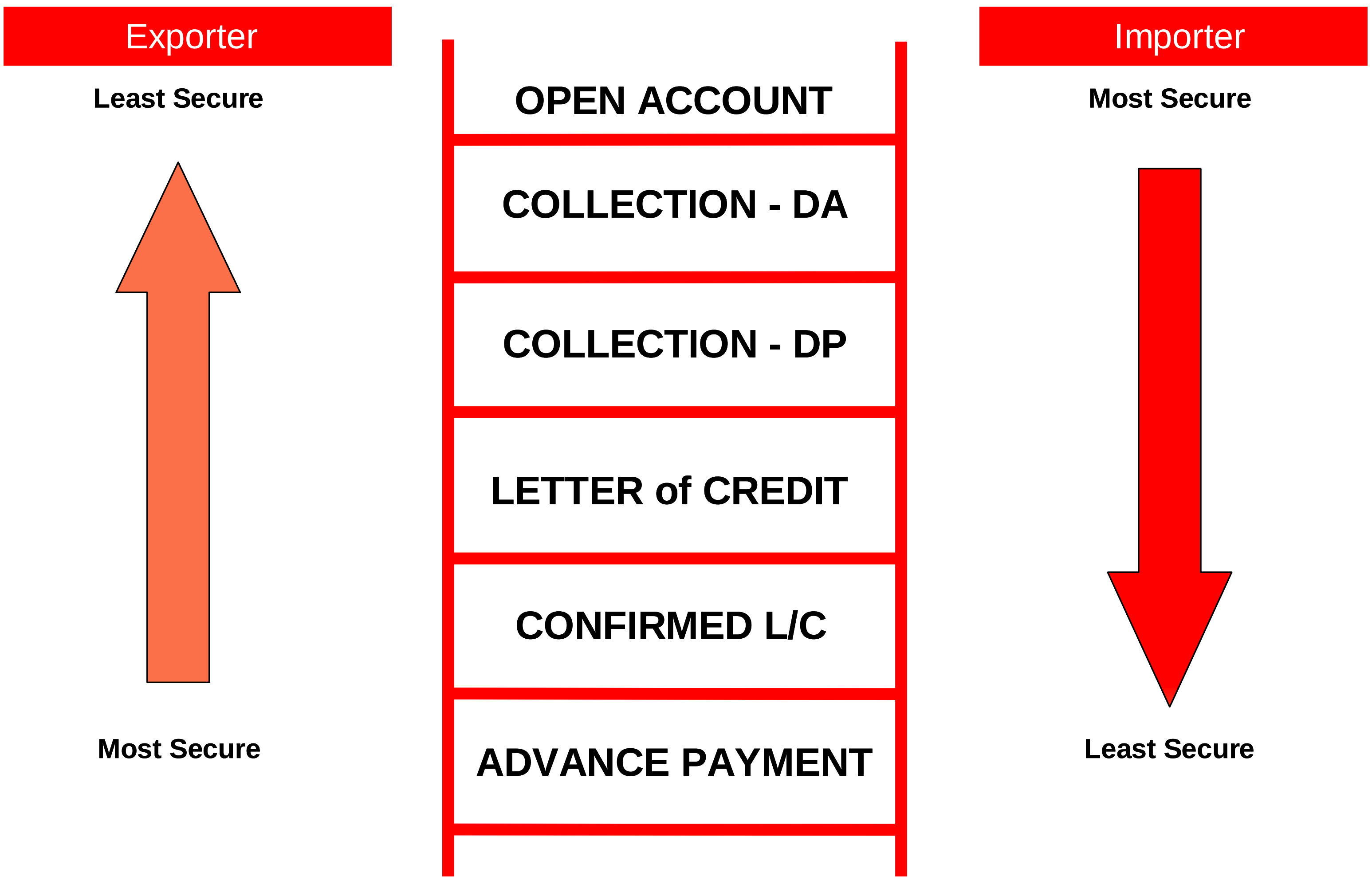
3) Under D/A
legal recourse

Key Risks:

1) Since there is
to effect payme
making payme

LETTERS OF CREDIT

What is Trade Finance About? Risk Management



Documentary Letters of Credit

Definition

- A written undertaking by a bank
- Given to the Supplier at the Buyer's request
- Promising to effect payment of a stated amount at a stated time
- Against presentation of documents in compliance with the terms and conditions stated in the Credit

Types of Payment

- Sight LC
- Usance LC

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Letters of Credit- Risk Profile

Benefits:

1) Only oblige
evidence tha
and present

2) Control ov
timing.

3) Ability to wo

Key Risks:

1) Issuing Bank
based purely o
appear on their
terms of the LC

SELLER

Benefits:

1) **The exporter has the Issuing Bank's undertaking to pay against compliant documents regardless of the financial capacity of the Buyer.**

2) **Ability to Confirm and/or Discount drafts.**

Key Risks:

1) A high percentage of presentations made under LCs are discrepant therefore making the payment obligation of the issuing entity null and void.

2) Depending on the country the goods are being shipped to, Country & Bank Risk can negate a major protective factor of LC's.

**Two key factors for discrepancies are poor documentation and late shipment/presentation.

Documentary Letters of Credit

- **Remember- Banks deal in Documents, not goods!**
  - Importer must still pay if exporter’s documents comply with letter of credit.
- **Governed by the following regulations:**
  - Uniform Customs & Practice for documentary credits ICC No. 600 (2007 revision)
  - International Chamber of Commerce- Publication Number 600 (1JUL07)

TERMINOLOGY

Terminology

- **Applicant**
  - Buyer/ Importer/ Account Party
- **Beneficiary**
  - Seller/ Exporter/ Drawer
- **Issuing Bank**
  - Importer's bank
  - Guarantees payment against correct documents
- **Advising Bank**
  - Correspondent Bank- close to seller, but not always seller's bank
- **Confirming Bank**
  - Located in beneficiary's country
  - Adds "guarantee" of payment
- **Negotiating Bank**
  - Correspondent Bank
  - Close to Seller
  - Often advising bank
  - Always the confirming bank (if any)
  - Sometimes the paying bank
  - Checks and processes documents

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Terminology

- **Paying Bank**
  - May be the negotiating bank
  - May be the advising bank
  - May be the issuing bank
- **Accepting Bank**
  - Usance Letter of credit
  - Drawee of draft

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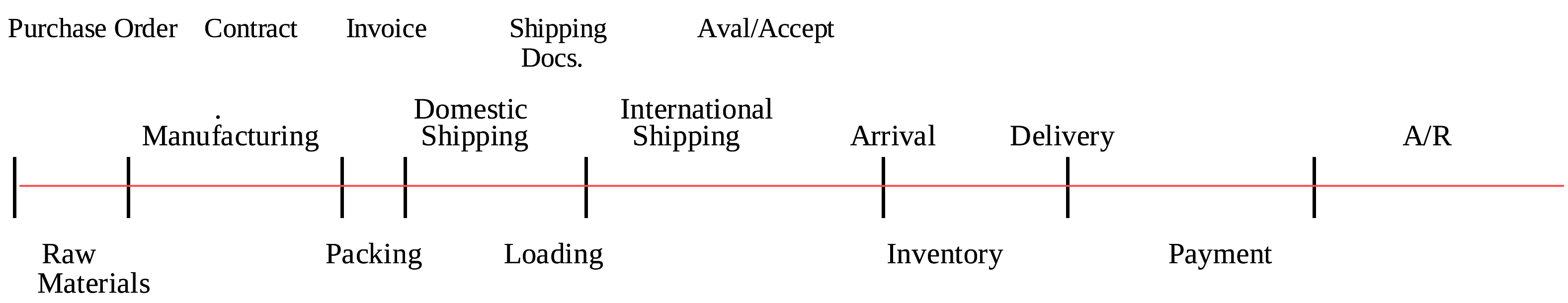
MOVING BEYOND THE BASICS

Trade Cycle

Exporter **Importer**



Confirmed Letter of Credit

- **When a bank, other than the Issuing Bank, adds its undertaking to pay under the Letter of Credit**
  - Usually the exporter's own bank is the Confirming Bank
- **Why is a Confirmation necessary?**
  - Beneficiary doubts the Issuing Bank's ability to pay (e.g. bank risk, country risk, or exchange controls)
  - Beneficiary needs payment on presentation of documents
  - Beneficiary wants "without recourse" financing

Confirmed Letters of Credit (cont'd)

- **Used to mitigate issuing bank risk and country risk**
- **Structure the letter of credit to ensure that documents are presented correctly against the letter of credit.**
  - We typically work with our clients to secure a "sample" letter of credit from the foreign bank to review the terms before the letter of credit is issued.
- **Discounting of the drafts**
  - If the Buyer is asking for extended terms, and is located in an area with high interest rates (ex.- Latin/South America), may have the opportunity to offer them 30/60/90/180 day terms (in select countries we may have an opportunity to offer even longer terms)
  - HSBC would discount the drafts using US interest rates- extremely attractive to the Buyer
- **In a program such as this, the Exporter would be offering its customers a low interest rate loan while reducing Exporter letter of credit costs. By getting HSBC involved early enough in the process, we may have a relationship with either the Buyer in country, or a correspondent relationship with the Buyer's bank. In either case, we may have the opportunity to finance them directly. Commonly referred to as a Banker's Acceptance, this form of finance is a time draft drawn on and accepted by the exporter. The bank's acceptance of the draft is a formal acknowledgement of the bank's unconditional promise to pay at its maturity.**

Direct Documentary Collections

- **Service that facilitates payment for international shipments utilizing both HSBC as the collecting bank and the Buyer's bank as payment agents. Both banks act as intermediary collection agents. This is a low cost alternative to letters of credit.**
- **Under a Documentary Collection, the drafts and documents are forwarded to the bank for processing. Under a Direct Collection documents are sent out directly by the Supplier or Supplier's Freight Forwarder**
  - Supplier is sent a receipt to then track the payment.
- **Used when there is a high level of trust and confidence between the Buyer and the Supplier.**
- **Advantages to Exporter:**
  - Enhances competitive position because collections are low cost and there is no credit exposure to buyer.
  - Banks monitor the collection and automatically send out periodic tracers. Goods don't exchange hands until payment from buyer's bank is received.
  - More secure than open account. Documents are controlled by agent banks until payment or the draft is accepted
  - Governed by internationally accepted rules and regulations.
- **Disadvantage to Exporter:**
  - Less secure than a letter of credit or cash in advance terms
  - Documents are not reviewed for discrepancies.

Direct/Documentary Collections with an AVAL

- **Exporter may require that its customer's bank provide an "Aval"**
  - The "Aval" is the act of subscribing one's signature at the bottom of a promissory note or bill of exchange: this is an act of surety ship by the party signing, in favor of the party to whom the note or bill is given.
- **Advantages to the Exporter:**
  - More secure because supported by the availability under the customer's line of credit, at no additional cost to the Exporter. The cost to the customer is typically less than that of a letter of credit.
- **Disadvantage to the Exporter:**
  - Less secure than cash or a letter of credit from a highly rated bank.

Open Account-Enhanced By Export Insurance

- **Through our trade services team and our partnership with Euler Hermes, HSBC can help identify which of your customers in certain geographic regions qualify for open account terms secured by export insurance. At times this alternative can be a cost effective.**
- **Advantage to the Exporter:**
  - Ability to customize a program in which the country and level of coverage can be matched with your desired exposure levels.
- **Disadvantage to the Exporter:**
  - The cost of insurance is borne by Exporter, and must be passed on to the customer through some form of price increase.

Standby Letters of Credit

- **Any Letter of Credit, which represents an obligation to the beneficiary on the part of the issuer**
  - to make payment on default by A/C party
  - to repay money borrowed by A/C party
  - to make payment on buyers indebtedness
- **Aim is NOT to draw against the Standby**
- **Trade Uses:**
  - Bid Bond
  - Performance Bond
  - Overseas Bank Guarantees
  - Trade Credit Support

Shared Client

- In situations where we have a mutual customer relationship, HSBC may be able to leverage its global presence, either in country or through an affiliate/partner bank.
- In some cases we may be able to provide financing directly to the exporter's customer, either on a recourse, partial recourse, or non-recourse basis. As in all of our alternatives, your trade finances representative would work directly with your organization in the coordination of these types of programs.

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