

Financing Working Capital in uncertain times

The challenge: How to finance working capital after securing a large international order with long payment terms.

The solution: NZEC guaranteed payment of a letter of credit issued by the international buyer's bank. NZEC's guarantee helped the exporter's bank to provide the working capital it needed to fulfil the order.



The benefit: The timber manufacturer was able to accept a sizeable export order that had a 360-day repayment term, with the confidence that it would receive full payment from its New Zealand bank upon fulfilling the terms of the LC.

During the COVID-19 pandemic, international trade slowed in many sectors. So when an Auckland timber exporter secured a \$1.3 million sale to a Maldives resort, it was keen to get the deal across the line.

But there was a problem: the contract with the resort had repayment terms of 360 days. The first challenge for the exporter was how to mitigate the risk of their buyer, operating in the international tourism sector during a global pandemic, not defaulting on its payments.

The exporter's second challenge was how to fund this contract if payment was not going to be until one year after delivering their goods. This was a significant hit to the exporter's working capital particularly during the uncertainties of the pandemic when they needed cash to keep their operation afloat.

The exporter's solution was to first require payment via a letter of credit (LC) issued by the buyer's bank. In effect, this meant that the buyer's bank was guaranteeing that payments would be made to the exporter, regardless if the buyer subsequently went out of business.

To assist with the financing of this sale, the exporter then requested its bank, ASB, to advance the payment of this letter of credit when they fulfilled the terms of the LC.

ASB's payment to the exporter would be conditional on two factors:

Firstly, the exporter presenting all compliant documents required by the LC. The typical documents required by the LC are invoice, packing list, bill of lading, quality certificate issued by an independent organisation and etc.

Secondly, ASB having the risk appetite on buyer's bank.

ASB's Trade Finance Manager Liam Tressler says the bank was keen to help a thriving, proven exporter secure a substantial deal during COVID-19. However ASB

didn't have the risk appetite to accept the long payment terms from the buyer's Maldives bank.

"This deal was important to our customer – and the Maldives is an important market for them. But we were not sufficiently comfortable with risk profile of the Maldives bank. For a time there it looked like the window was closing to find a way to make this deal happen", explains Liam.

ASB has had a long association with New Zealand Export Credit (NZEC), so together the organisations nussed out a way forward.

NZEC undertook due diligence on the Maldives bank and satisfied itself with its risk profile. NZEC offered ASB its Letter of Credit Guarantee which covers losses in the event the Maldives bank defaults on its repayment. With this in place, ASB was happy to support the lending to the exporter required to make the deal happen.

The exporter effectively received the payment upfront instead of waiting for a year to get paid which allowed them to proceed without cashflow issues.

NZEC Senior Business Originator, Thomas Sheng, says that this deal has helped the exporter to understand how Letters of Credit can be a valuable tool in the current climate of uncertainty.

"There is a bit of a process involved to transact a Letter of Credit but, in times like these, some businesses are moving back towards this as an effective way to manage payment risk as well as access finance."

www.asb.co.nz

If you want to understand more about how our letter of credit guarantee may help an exporter mitigate payment risk, please get in touch:

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