Chapter 14 - Export Risks Management

Introduction
Export pricing is the most important factor in for promoting export and facing international trade competition. It is important for the exporter to keep the prices down keeping in mind all export benefits and expenses. However, there is no fixed formula for successful export pricing and is differ from exporter to exporter depending upon whether the exporter is a merchant exporter or a manufacturer exporter or exporting through a canalising agency.

Like any business transaction, risk is also associated with good to be exported in an overseas market. Export is risk in international trade is quite different from risks involve in domestic trade. So, it becomes important to all the risks related to export in international trade with an extra measure and with a proper risk management.
The various types of export risks involve in an international trade are as follow:

Credit Risk
Sometimes because of large distance, it becomes difficult for an exporter to verify the creditworthiness and reputation of an importer or buyer. Any false buyer can increase the risk of non-payment, late payment or even straightforward fraud. So, it is necessary for an exporter to determine the creditworthiness of the foreign buyer. An exporter can seek the help of commercial firms that can provide assistance in credit-checking of foreign companies.

Poor Quality Risk
Exported goods can be rejected by an importer on the basis of poor quality. So it is always recommended to properly check the goods to be exported. Sometimes buyer or importer raises the quality issue just to put pressure on an exporter in order to try and negotiate a lower price. So, it is better to allow an inspection procedure by an independent inspection company before shipment. Such an inspection protects both the importer and the exporter. Inspection is normally done at the request of importer and the costs for the inspection are borne by the importer or it may be negotiated that they be included in the contract price.
Alternatively, it may be a good idea to ship one or two samples of the goods being produced to the importer by an international courier company. The final product produced to the same standards is always difficult to reduce.

Transportation Risk
With the movement of goods from one continent to another, or even within the same continent, goods face many hazards. There is the risk of theft, damage and possibly the goods not even arriving at all.

Logistic Risk
The exporter must understand all aspects of international logistics, in particular the contract of carriage. This contract is drawn up between a shipper and a carrier (transport operator). For this an exporter may refer to Incoterms 2000, ICC publication.

Legal Risk
International laws and regulations change frequently. Therefore, it is important for an exporter to drafts

a contract in conjunction with a legal firm, thereby ensuring that the exporter's interests are taken care of.

Political Risk
Political risk arises due to the changes in the government policies or instability in the government sector. So it is important for an exporter to be constantly aware of the policies of foreign governments so that they can change their marketing tactics accordingly and take the necessary steps to prevent loss of business and investment.

Unforeseen Risk
Unforeseen risk such as terrorist attack or a natural disaster like an earthquake may cause damage to exported products. It is therefore important that an exporter ensures a force majeure clause in the export contract.

Exchange Rate Risk
Exchange rate risk is occurs due to the uncertainty in the future value of a currency. Exchange risk can be avoided by adopting Hedging scheme.

Export Risk Management Plan
Risk management is a process of thinking analytically about all potential undesirable outcomes before they happen and setting up measures that will avoid them. There are six basic elements of the risk management process:
- 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

A risk management plan helps an exporter to broaden the risk profile for foreign market. For a small export business, an exporter must keep his risk management analysis clear and simple.
Export Risk Mitigation

Export risk mitigation are the various strategies that can be adopted by an exporter to avoid the risks associated with the export of goods.

- Direct Credit: Export Credit Agencies support exports through the provision of direct credits to either the importer or the exporter.

Importer: a buyer credit is provided to the importer to purchase goods.
Exporter: makes a deferred payment sale; insurance is used to protect the seller or bank.
- Guarantees
- Bid bond (tender guarantee): protects against exporter's unrealistic bid or failure to execute the contract after winning the bid.
- Performance bond: guarantees exporter's performance after a contract is signed.
- Advance payment guarantee (letter of indemnity): in the case where an importer advances funds, guarantees a refund if exporter does not perform.
- Standby letter of credit: issuing bank promises to pay exporter on behalf of importer.

- Insurance

Transportation insurance: Covers goods during transport; degree of coverage varies.
Credit Insurance: Protects against buyer insolvency or protracted defaults and/or political risks.

Seller non-compliance (credit insurance): Covers advance payment risk.
Foreign exchange risk insurance: Provides a hedge against foreign exchange risk.

● Hedging

Instruments used to Hedge Price Risk

- Stabilization programs and funds.
- Timing of purchase/sale.
- Fixed price long-term contracts.
- Forward contracts.
- Swaps