

MODULE 2.11

Forfaiting

Forfaiting is a form of trade financing undertaken to facilitate export transactions. The process of forfaiting thus has a lot of significance as it undertakes to solve the cash flow problems of the party taking the benefit of factoring. In a forfaiting transaction, the exporter surrenders his right for claiming the payment for services rendered or goods supplied to the importer in favor of the forfaiter. A deed is prepared stating the same and the exporter receives cash payment from the facilitator. All the transactions of forfaiting are performed with the support of a bank, which assumes the default risk possessed by the importer. The exporter before extending finance for a forfaiting transaction looks into several critical aspects of the underlying goods or commodity.

For example, the bank would pay special attention towards the durability/perishability nature of the goods, authentication of the product (date of manufacturing, product code, etc.), packaging arrangements and other precautions adopted during the stage of shipment etc. After these checks and verifications, the banker provides the exporter with the funds. In other words, the forfaiting transaction helps an exporter with instant cash and eliminates his cash flow problems. Forfaiting is a relatively new concept. It is a specialized form of factoring, which is undertaken on export transactions on a non-recourse basis.

Characteristics of Forfaiting

Forfaiting is an international trade finance tool.

It helps exporters or international manufacturing companies to reach cash flow by selling their debts, which are mostly supported by a bank guarantee, or trade-related receivables secured with trade finance instruments such as bills of exchange, promissory notes or deferred payment letter of credit proceeds with a discounted price to the forfaiting companies.

Exporters sell their debts under a forfaiting agreement without recourse basis, which means that once the debt is sold the non-payment risk passes to the forfaiter.

What would be happening to the original payment obligation will not be concerning the sellers after that point.

- Forfaiting can be applied to a wide range of trade related and purely financial receivables typically have maturities from 3 months to 10 years.
- Forfaiting can be applied to both international and domestic transactions.

- 100% financing without recourse to the seller of the debt
- The payment obligation is often but not always supported by a bank guarantee
- The debt is usually evidenced a legally enforceable and transferable payment obligation such as a bill of exchange, promissory note or letter of credit.
- Transaction values can range from US\$100,000 to US\$200 million
- Debt instruments are typically denominated in one of the world's major currencies, with Euro and US Dollars being most common.
- Finance can be arranged on a fixed or floating interest rate bas

The term forfaiting owes its origin to a French term 'forfait' which means to forfeit (or surrender) ones' rights on something to someone else.

Forfaiting is a mechanism of financing exports:

- (a) By discounting export receivables
- (b) Evidenced by bills of exchanges or promissory notes
- (c) Without recourse to the seller (viz; exporter)
- (d) Carrying medium to long-term maturities
- (e) On a fixed rate basis up to 100% of the contract value.

In other words, it is trade finance extended by a forfaiter to an exporter seller for an export/sale transaction involving deferred payment terms over a long period at a firm rate of discount. Forfaiting is generally extended for export of capital goods, commodities and services where the importer insists on supplies on credit terms. Recourse to forfaiting usually takes place where the credit is for long date maturities and there is no prohibition for extending the facility where the credits are maturing in periods less than one year.

Parties to forfaiting

There are five parties in a transaction of forfaiting.

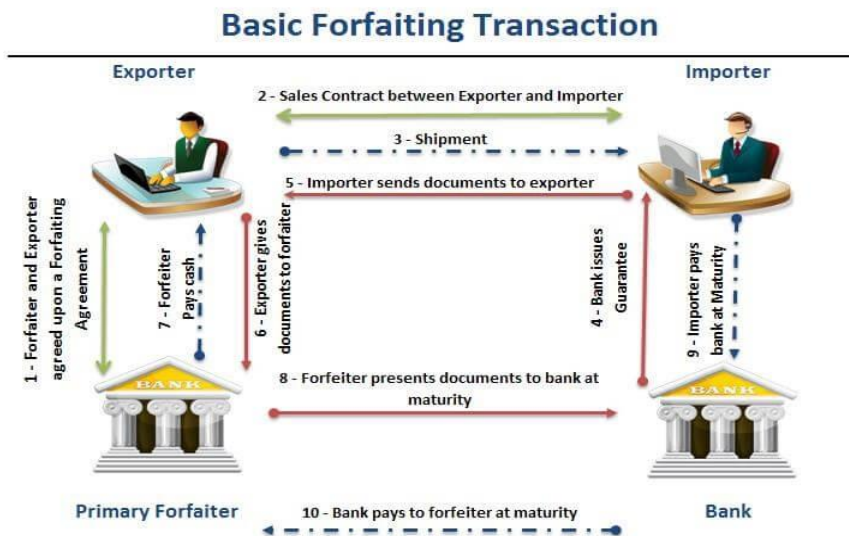
These are (i) Exporter (ii) Importer (iii) Exporter's bank (iv) Importer's bank (v) the forfaiter.

Forfaiting is a means of financing that enables exporters to receive immediate cash by selling their medium and long-term receivables—the amount an importer owes the exporter—at a discount through an intermediary. The exporter eliminates risk by making the sale without recourse. It has no liability regarding the importer's possible default on the receivables.

The forfaiter is an individual or entity that purchases the receivables, and the importer then pays the receivables amount to the forfaiter. A forfaiter is typically a bank or a financial firm that specializes in export financing.

Mechanism

1. The exporter and importer negotiate the proposed export sale contract. Then the exporter approach es the forfaiter to ascertain the terms of forfaiting.
2. The forfaiter collects details about the importer, supply and credit terms, documentation etc.
3. Forfaiter ascertains the country risk and credit risk involved.
4. The forfaiter quotes the discount rate.
5. The exporter then quotes a contract price to the overseas buyer by loading the discount rate, commitment fee etc. on the sale price of the goods to be exported.
6. The exporter and forfaiter sign a contract.
7. Export takes place against documents guaranteed by the importer's bank.
8. The exporter discounts the bill with the forfaiter and the latter presents the same to the importer for payment on due date or even sell it in secondary market.



- Step 1 : Forfaiter and Exporter agreed upon a Forfaiting Agreement.

- Step 2 : Sales Contract has been signed between Exporter and Importer.
- Step 3 : Shipment is initiated by the exporter.
- Step 4 : The importer obtains a guarantee from his bank.
- Step 5 : The importer obtains a guarantee from his bank.
- Step 6 : Exporter gives documents to forfaiter.
- Step 7 : Forfaiter controls the documents pays for them as indicated on the Forfaiting Agreement.
- Step 8 : Forfaiter presents documents to bank at maturity date.
- Step 9 : Importer pays to bank at maturity date.
- Step 10 : Bank pays to forfaiter at maturity date.

Documentation

1. Forfaiting transaction is usually covered either by a promissory note or bills of exchange.
2. Transactions are guaranteed by a bank.
3. Bills of exchange may be 'availed by' the importer's bank. 'Aval' is an endorsement made on bills of exchange or promissory note by the guaranteeing bank by writing 'per aval' on these documents under proper authentication.

Costs of forfaiting

The forfaiting transaction has typically three cost elements:

1. Commitment fee, payable by the exporter to the forfaiter 'for latter's' commitment to execute a specific forfaiting transaction at a firm discount rate within a specified time.
2. Discount fee, interest payable by the exporter for the entire period of credit involved and deducted by the forfaiter from the amount paid to the exporter against the availed promissory notes or bills of exchange.
3. Documentation fee.

Benefits of forfaiting

Forfaiting helps the exporter in the following ways:

1. It frees the exporter from political or commercial risks from abroad.
2. Forfaiting offers 'without recourse' finance to an exporter. It does not effect the exporter's borrowing limits/capacity.

3. Forfaiting relieves the exporter from botheration of credit administration and collection problems.
4. Forfaiting is specific to a transaction. It does not require long term banking relationship with forfaiter.
5. Exporter saves money on insurance costs because forfaiting eliminates the need for export credit insurance.

However there are certain disadvantages of forfaiting -

1. From bank purpose of view there is no legal framework to guard the banker or financial institution doing forfeiture and thus they face the danger within the kind of political, rate of exchange risk and different risk go together with foreign transactions.
2. It is very expensive from exporter point of view because banks take high fees for forfeiture thanks to high risks concerned in it.
3. There is no secondary marketplace for these kinds of instruments thus there is lack of liquidity for these instruments.

The forfaiter is a financial intermediary that provides assistance in international trade. It is evidenced by negotiable instruments i.e. bills of exchange and promissory notes. It is a financial transaction, helps to finance contracts of medium to long term for the sale of receivables on capital goods. However, at present forfaiting involves receivables of short maturities and large amounts.

Different Type of Forfaiting

Promissory Note / bill of exchange

The great majority of forfaitable obligations take the shape of either note of hand issued by the human in favor of the beneficiary or bills of exchange drawn by the beneficiary on and accepted by the human. The primary reason for the predominance of those kinds of certificate of indebtedness may be a matter of familiarity. Long expertise in addressing such paper has led to wide easy handling by all parties and customarily facilitates a fast and uncomplicated group action.

“Without Recourse” Clause

By transferring the drafts, the importer additionally transfers his claim to the forfaiter. This can be done by an endorsement on the back of the draft, the importer being the endorser and also the Forfaiter being the endorsee. A sample endorsement would scan “Please pay to the order of forfaiter while not recourse - signed exporter”. This clause excludes the endorsee’s right of recourse against the previous holder of the draft - the most characteristic of Factoring.

“Effective / internet of Deduction” Clause

All drafts should to bear this clause that ensures that payment might solely be accomplished within the currency approved and not in any native currency. The clause can scan “effective payment to be created in alternative country currency solely, while not deduction for and freed from any tax, impost, levy or duty gift or way forward for any nature.” A draft bearing this clause is issued “in international format”.

Book Receivables / Letters of Credit

Letters of credit with credit clause are often Forfaiting moreover. However, transactions tend to be a lot of complicated, since all maturities are proved by one document, created go in favor of the beneficiary. The duty is commonly not transferable while not specific permission from the obligor.

How Forfaiting Works

The exporter approaches a forfaiter before finalizing the transaction’s structure. Once the forfaiter commits to the deal and sets the discount rate, the exporter can incorporate the discount into the selling price. The exporter then accepts a commitment issued by the forfaiter, signs the contract with the importer, and obtains, if required, a guarantee from the importer’s bank that provides the documents required to complete the forfaiting. The exporter delivers the goods to the importer and delivers the documents to the forfaiter who verifies them and pays for them as agreed in the commitment. Since this payment is without recourse, the exporter has no further interest in the financial aspects of the transaction and it is the forfaiter who must collect the future payments due from the importer.

Which Indian Bank provides Forfaiting Services?

Exim Bank, Export-Import Bank of India established by an act of parliament in 1982, is India's premier export finance institution. The bank facilitates, promotes and finances exports from India responding to exporters needs on a continuous and proactive basis. It was the first to introduce forfaiting into India in 1992.

Forfaiting in India

For a long time, Forfaiting was unknown to India. Export Credit Guarantee Corporation was guaranteeing commercial banks against their export finance. However, with the setting up of export-import banks, since 1994 forfaiting is available on liberalized basis.

The exim bank undertakes forfaiting for a minimum value of Rs. 5 lakhs. For this purpose, the exporter has to execute a special Pronote in favor of the exim bank. The exporter will first enter into an agreement with the importer as per the quotation given to him by the exim bank. The exim bank on its part, gets quotation from the forfaiting agency abroad. Thus, the entire forfaiting process is completed by exporter agreeing to the terms of the exim bank and signing the Pronote.

Forfaiting business in India will pick up only when there is trading of foreign bills in international currencies in India for which the value of domestic currency has to be strengthened. This would be possible only with increasing exports. At present, India's share stands at 1.7 percent in the world exports. Perhaps, this will bring a push to the forfaiting market.

Problem areas in forfaiting and factoring where legislation is required.

1. There is, presently, no legal framework to protect the banker or forfaiter except the existing covers for the risks involved in any foreign transactions.
2. Data available on credit rating agencies or importer or foreign country is not sufficient. Even Exim bank does not cover high-risk countries like Nigeria.
3. High country and political risks dissuade the services of factoring and banking to many clients.
4. Government agencies and public sector undertakings (PSUs) neither promptly make payments nor pay interest on delayed payments.
5. The assignment of book debts attracts heavy stamp duty and this has to be waived.
6. Legislation is required to make assignment under factoring have priority over other assignments.
7. There should be some provisions in law to exempt factoring organization from the provisions of money lending legislations.
8. The order 37 of Civil Procedure Code should be amended to clarify that factor debts can be recovered by resorting to summary procedures. Thus, the existing legal framework governing the transactions of factoring business is not adequate to make the functioning simple, inexpensive and attractive in the market.

In order to ensure that the functioning of a factor is with ease and confidence the legal framework should:

- (a) Define the rights, liabilities, duties and obligations of the parties involved, in a clear and comprehensive manner, so that the parties can plan their affairs with certainty, and
- (b) Be supportive of the transactions and procedures involved, so that they may be undertaken and completed simply and inexpensively.

In short, areas like 'assignment', 'stamp duty', 'priorities of factoring assignment', 'liabilities of the debtor', 'obligations of banks', realisation of debts through simple legal process etc. require focused attention. A draft bill on the factoring of debts due to industrial and commercial undertakings has been prepared which awaits clearance by the Government of India. Once this bill is passed majority of the constraints will be eliminated

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exchange and promissory notes. It is a financial transaction, helps to finance contracts of medium to long term for the sale of receivables on capital goods. However, at present forfaiting involves receivables of short maturities and large amounts.

Key Differences between Factoring and Forfaiting

The major differences between factoring and forfaiting are described below:

1. Factoring refers to a financial arrangement whereby the business sells its trade receivables to the factor (bank) and receives the cash payment. Forfaiting is a form of export financing in which the exporter sells the claim of trade receivables to the forfaiter and gets an immediate cash payment.
2. Factoring deals in the receivable that falls due within 90 days. On the other hand, Forfaiting deals in the accounts receivables whose maturity ranges from medium to long term.
3. Factoring involves the sale of receivables on ordinary goods. Conversely, the sale of receivables on capital goods are made in forfaiting.
4. Factoring provides 80-90% finance while forfaiting provides 100% financing of the value of export.
5. Factoring can be recourse or non-recourse. On the other hand, forfaiting is always non-recourse.
6. Factoring cost is incurred by the seller or client. Forfaiting cost is incurred by the overseas buyer.
7. Factoring does not deal with negotiable instrument while Forfaiting involves dealing with negotiable instruments like bills of exchange and promissory note
8. In factoring, there is no secondary market, whereas in the forfaiting secondary market exists, which increases the liquidity in forfaiting.

Managing a Forfait Transactions-Risks to Exporters,

Importers and Guarantors

The exporter's risks

1. An exporter who has sold an amount receivable to a forfaiter has virtually no outstanding risk arising from the transaction. His only risks may arise during the period between the acceptance of his tender or bid for the importer's customer and the delivery of the goods or services, that is, during a period when he is committed to taking a forfait finance at an agreed discount rate even though the contract with the importer has yet to be completed. Any interest rate risk during this period should not, however, be overemphasised as it only represents an 'opportunity' risk.

There is the risk, of course, that the importer will arbitrarily cancel the contract during the commitment period or that, for some other reason, the contract will not be completed. In this event, the exporter is obliged to recompense the forfaiter for any cost or loss he suffers. In practice, a forfaiter will generally look upon the problem sympathetically, if only because he wants to maintain his relationship with the exporter. In addition, it is probably fair to say that any question of compensation for the forfaiter is usually trivial compared with the problems which caused the cancellation in the first place and with any sum which the aggrieved party, importer or exporter, is seeking from the other as a consequence. Finally, there is no control which can be instituted by the exporter to protect himself against this risk.

2. The one true risk that the exporter may run during the commitment period arises when the promissory notes or bills of exchange which he has agreed to sell are denominated in a currency other than his own reporting currency. He will have the risk that currency movements will be unfavourable to him.

Controlling the exporter's risks

3. The exporter should maintain a list of his forfaiting commitments by currency so that he can monitor his exposure to currency parity movements and enter into forward currency contracts if appropriate. As in the case the importer and explained below, an exporter with large numbers of commitments exporting at different dates may need to list them by maturity tranche net of any forward currency contracts.

The importer's risks

Once he is committed to pay a promissory note or bill of exchange, the importer is bound, as an obligator, to make payment at a specific time in the future. The amount involved and the currency in which it is denoted are fixed. He has no risk from fluctuating interest rates, since interest on his debt is already calculated and included in the value of the bill or note itself. Provided that the currency of the bill or note is the same as that in which his accounts are reported, usually his home currency, he has no risk from currency parity movements.

The only risk to the importer is the possibility that he will have insufficient funds available to effect repayment on the due dates. This risk can be minimized by careful monitoring of his cash and debt positions.

Controlling the importer's risk

1. Currency risk

The importer should maintain an up-to-date list in each currency of outstanding debt commitments and obligations. Any hedging foreign currency transactions should be offset against the currency totals so that the true currency exposures is shown.

2. Risk Repayment or liquidity

This is, in essence, the same as any other cash-flow risk that an importer or, indeed, any trader has. All business need to manage and monitor their cash flow. The only slight additional problem in the case of a forfait finance is that debts are due in the future rather than immediately, so that there is a greater possibility that they will be overlooked.

3. The guarantor's risks

In any a forfait transaction, the guarantor has a commitment to pay off the promissory notes or bills of exchange at their maturity dates and the right to demand simultaneous payments by the importer. It follows that he has contingent liability and a contingent asset. Provided that both are disposed of simultaneously, he has no risk. To the extent that the importer pays late, he will demand interest for late payment and will thus be unlikely to have a significant exposure to interest charges. However, he has an absolute risk of default by the importer and an absolute sovereign risk if the importer's country is different from his own (though it is unusual for this to be the case). In the event of either late payment or non-payment, he has a liquidity risk in that he must be sure that he has adequate funds available to pay the bills or notes.

Controlling the guarantor's risk

1. Risk of default by the importer

Any guarantor must have clear procedures set out in writing which must be followed, that levels of personnel who can approve limits of a particular size must also be specified, and that any breach of limits must be reported at an appropriate level very quickly.

2. Sovereign risk

Sovereign limits will be much larger and often subject to more frequent reconsideration than those for individual customers or particular industry.

3. Liquidity risk

Since most guarantors are major banks, this is seldom a matter for great concern. None the less, any guarantor will wish to maintain an up-to-date list of his contingent assets and liabilities with immediate exception reporting of any repayments that are overdue. Responsibility for reviewing

exception reports and taking appropriate action must be clearly established at an appropriate level of authority.

The forfaiter's risks

From the moment he grants an option for a forfait finance to the moment the forfeited assets are repaid, the forfaiter is exposed to risk. The various stages giving rise to risk can be charted as followed.

1. Option period

During the option period, the forfaiter runs the risk that interest rates will move against him. Since the exporter is not committed to the transaction at this point, the forfaiter will hardly ever entered into any funding arrangements in respect of it. His exposure is thus absolute.

By the same token, the forfaiter has accepted the credit-worthiness of the guarantor as soon as he grants the option. He is exposed to risk in this respect and to sovereign risk until he is repaid or until the exporter refuses the option.

The only thing that changes, in terms of risk, between the option period and the commitment period is that the forfaiter can assume in the commitment period is that the forfaiter can assume in the commitment period that the a forfait transaction will take place. He can therefore commit himself to funding arrangements and, assuming he can obtain fixed-rate funding, thereby eliminate any interest-rate risk. The most significant reason for not matching funding too closely to the maturities of forfeited assets is the flexibility it enables the forfaiter to retain. If he sees an attractive opportunity to sell some of his assets on the secondary market. the forfaiter does not wish to be drawn into difficult and potentially expensive negotiations to free himself of any related funding.

2. Date of purchase

Until this date is reached, the forfaiter can always back out of the a forfait transaction if he finds irregularities in the asset he is buying or in its guarantee or, indeed, if he is dissatisfied as to the completion of formalities in respect of the particular transaction, for example failure by the importer to obtain the permission of the relevant authorities for the commitment to transfer the relevant foreign currency at the maturity dates of the bills or notes forfeited.

3. Period during which paper is held

The one very obvious danger that the forfaiter faces while he has the asset is that he will fail to send maturing assets for collection. An oversight in this respect is seldom tragic but any delay in receiving repayment costs the forfaiter money. The other side of the coin is that the forfaiter needs to keep a careful watch on his borrowings to ensure that he has funds available to pay them when they become due, since, as stated earlier, he is unlikely to have matched the repayment of his borrowings to the maturity dates of his assets.

4. Date of maturity of the paper

The only additional risk at this point in the life of an a forfait transaction arises from its late payment because of tardiness or incompetence on the part of the guarantor or his paying agent. It is true that, if this happens, the forfaiter has grounds to make a claim for interest on the offending party, but it is also true that he may have great difficulty in actually obtaining the interest.

Controlling the forfaiter risks

The forfaiter needs to maintain up-to-date list by currency of all items in his portfolio and those for which he has extended an option or to which he is committed.

Because of his general tendency not to match borrowings specifically to the maturity of assets, a forfaiter may well have some assets, purchased at a time of relatively low interest rates, which are earning less than the prevailing cost of borrowing as a result of an increase in interest rates. Since a forfaiter in this position will probably be looking upon his portfolio as a pool of assets, this will not disturb him greatly, provided that, overall, his portfolio is profitable.

1. Guarantor credit risk

Just as the guarantor should have set credit limits for individual customers and industries, so the forfaiter should set credit limits for individual guarantors. The forfaiter should have clear procedures set out in writing for establishing these limits, levels of personnel who can approve limits of a particular size must be specified, and any breach of those limits must be reported at an appropriate level very quickly.

2. Risk of inadequate documentation

This risk can best be controlled by the use of a check-list covering such matters as evidence to support the genuineness and legality of the trade underlying the forfaiting transaction, checks which need to be made on the form and connect stipulated by the guarantor's local law of any letter of guarantee or aval, and checks ascertaining local requirements which are needed to gain permission for the remittance of foreign currency.

3. Exporter and importer risk

A forfaiter will generally examine the competence, credibility and credit-worthiness of these parties to a forfaiting transaction only very superficially, since he will very seldom have need to revert to them because of a problem. To the extent that the exporter or importer is known to him from previous dealings, or from general reputation, any specific steps that he need take to check them out will be further reduced.

4. *Currency risk*

The forfaiter needs to maintain an up-to-date list by currency of all his forward currency contracts by maturity period.

5. Collection risk

The interest-rate risk report and the foreign currency contract list together provide the forfaiter with most of the cash-flow information he requires to minimize the risk of lack of liquidity.

Market Growth

During the period 1970-1980, both the primary and secondary markets in and for nonrecourse trade paper increased considerably. Specialist banks in addition to traditional deposit and clearing banks developed Forfaiting departments, usually within their trade finance departments.

Later, specialist Forfait Houses were set up and there was a perceptible geographic growth and shift of the market from Switzerland/Northern Italy to Western Germany and more markedly to London. In 1984 London Forfaiting Company PLC, the only publicly owned and U.K. Stock market quoted specialist Forfaiting Company, was set up. The primary forfait market has developed alongside state backed credit export schemes, sometimes as a competition and sometimes as an adjunct to the state credit export schemes. Between market professionals a secondary market also evolved in forfait paper, which in effect securities these exporter receivables. During the period 1980-90 an increasing awareness of the forfait market was developed in many developed countries among business community.

Forfaiting Services in India

Recognising the utility of Forfaiting services to Indian exporters, the RBI decided to make available such services to the exporters. At the beginning the RBI authorised EXIM Bank in 1992 to offer Forfaiting services. The role of the EXIM Bank has been that of a facilitator between the Indian exporter and the overseas Forfaiting agency.

Scheduled commercial banks have also been permitted to offer Forfaiting services by acting as an agent or a facilitator between Indian exporter and the Forfaiting agency operating in some other country. That means in other words, scheduled commercial banks can undertake Forfaiting services as a part of fee based financial services. A subsidiary of EXIM bank namely; Global Trade Financial Services Private Ltd. has been engaged in providing Forfaiting services to the exporters in India. As per the RBI's A D Circular No. 3 Dated February 13, 1992, discount fee, documentation fee and any other costs levied by a forfaiter must be transferred to the overseas buyer.

In view of this, the exporter, who intends to avail Forfaiting facility, should finalise the export contract in a manner which ensures that the amount received in foreign exchange by him after payment of Forfaiting discount and other fees is equivalent to the price which he would obtain if goods were sold on cash payment terms. If the banks are able to act as an agent to structure Forfaiting deals keeping in view the requirements of our Indian exporters, then there will be demand for such product. For this, commercial banks and others may have to introduce a lot of flexibility while acting as an agent or a facilitator in this regard. For example, the minimum value of the Forfaiting transaction may be required to be kept at a reasonable level. Instead of acting simply as an agent, with the permission from the RBI, banks and financial institutions in India must explore the possibility of taking up Forfaiting activity as a fund based activity. With the dissemination of knowledge about Forfaiting among Indian exporters, it may be possible to create awareness about it and subsequently demand for the same.

Conclusion

In India, in respect of deferred payment exports, post-shipment credit is available from banks on subsidised terms. Further, EXIM Bank also has its own finance schemes for medium/long term project exports. Export Credit Guarantee Corporation of India Ltd(ECGC) cover is also available for such finance. However, in tune with national policy of export promotion, export projects especially for capital goods, turnkey projects etc. are showing an increasing trend. Therefore, forfaiting if introduced in India, may open up an alternate window for availing finance as well as debt protection especially for export protects from small and medium enterprises. The working group on introduction of factoring services (Kalyansundaram Committee) has rightly made observation that as the volume of such exports 'i.e. export protects for capital goods) from India is growing, it 'i.e. Export projects for capital goods) from India is growing, it 'i.e. forfaiting) merits consideration as an additional method for financing, particularly as it also involves provision of credit protection.

While comparing the firm's average cost of fund and that of forfaiting and when it is revealed that cost of forfaiting is higher, it may be noted that forfaiting eliminates country/political risk, currency/ transfer risk and financial/commercial risk.

It is suggested that exporters should be convinced to convert their partnership firm into private limited/public limited company in order to muster a better MSME confidence of the forfaiter. Further, units also be encouraged to go for credit ratings to manage better confidence of forfaiter. Forfaiting provides a flexible, simple and creative alternative to traditional trade finance and would be of great benefit to buyers in developing nations. Further, it is 100% without recourse financing and so more useful to small units. They are free from the hassles of credit management and the collection of receivables. It also eliminates the need for export credit insurance by the exporter. The great benefit also lies in protection against risk of interest rate and exchange rate fluctuations. This services after considering the reforms in better institutional framework will provide a great deal of comfort to SME units as they do not have easy accessibility and availability of funds compared to large corporates. It also provides relief to SME sector in terms of collateral security not being required under this arrangement.

Hence Forfaiting is a form of trade financing undertaken to facilitate export transactions. · It is a relatively new concept in India. · The major parties involved are: exporter, importer, domestic bank, foreign bank and the forfaiter, which could be primary or secondary forfaiter. · The costs involved in a forfaiting transaction are: Commitment fees, discount fees and documentation fees. · The main reason for forfaiting not developing in India is the lack of awareness among the exporting community. Both the banks and the government have not taken any major steps to popularize forfaiting.

In today's discussion, we have covered the concept of forfaiting, its meaning, characteristics, its mechanism, Documentation. Cost, benefits, types, how forfaiting

works, which Indian banks provides factoring services, Problem areas in forfaiting and factoring where legislation is required. Key Differences between Factoring and Forfaiting, Managing a Forfait Transactions-Risks to Exporters, Importers and Guarantors.

In this unit we have discussed the financial services namely Factoring, Forfaiting and bill discounting. Factoring involves financing and collection of accounts receivables in domestic as well as international trade. This service is rendered by the factor who provides finance against book debts, collects cash against receivables, undertakes sales ledger administration, provides protection against bad debts, etc. There are three parties to a factoring contract: buyer of goods, who has to pay for goods bought on credit terms, seller of goods, who has to realize credit sales from buyer and the factor, who acts as an agent and realizes the sales from the buyer. Forfaiting is a source of trade finance which enables exporters to get funds from the forfaiter on transferring the right to recover the debts from the importer. It denotes the purchase of trade bills or promissory notes by a bank or financial institution, without recourse to seller. Bill discounting is a source of short-term trade finance. It is known as acceptance credit, where on party accepts liability of trade towards third Party.

THANK YOU