Perspectives

Opening the door to global markets

How and why smaller UK businesses should take a bigger slice of global trade

- The BRICs and other rapid-growth economies offer huge opportunities for SMEs, but currently UK businesses have a very low penetration of these increasingly important export markets.
- The UK's share of global exports has been shrinking over the past three decades. But with help and guidance, there is no reason why the UK can't compete and succeed in the new global growth markets.
- UK SMEs in particular are held back by a number of barriers, including the challenge of finding the right local partners and the ability to mitigate risks related to doing business in unfamiliar markets.
- More education is needed to inform UK businesses of the tools and support available.

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Glossary of terms

Bill of Exchange: A written unconditional order from one person (the drawer) to another (the drawee). The bill directs the drawee to pay a specified amount to a named drawer at a fixed or yet to be agreed future date.

Bonds / Guarantees: An irrevocable commitment by a bank to make a payment provided the terms of the bond or guarantee are met.

BRICs: An acronym referring to Brazil, Russia, India and China, all countries that have been recognised for their newly advanced economic development.

Collections: A secure, universally recognised method for routing trade documentation through the banking system.

Invoice Finance: Funding solutions that allow you to turn unpaid invoices, inventory or assets into cash.

Letters of Credit (L/C): A financial instrument meaning that the payment from the importer is guaranteed by the importer's bank.

Supply Chain Finance: Solutions that aim to ease payment pressures along the supply chain, each element of which is under pressure to receive payment as early as possible.

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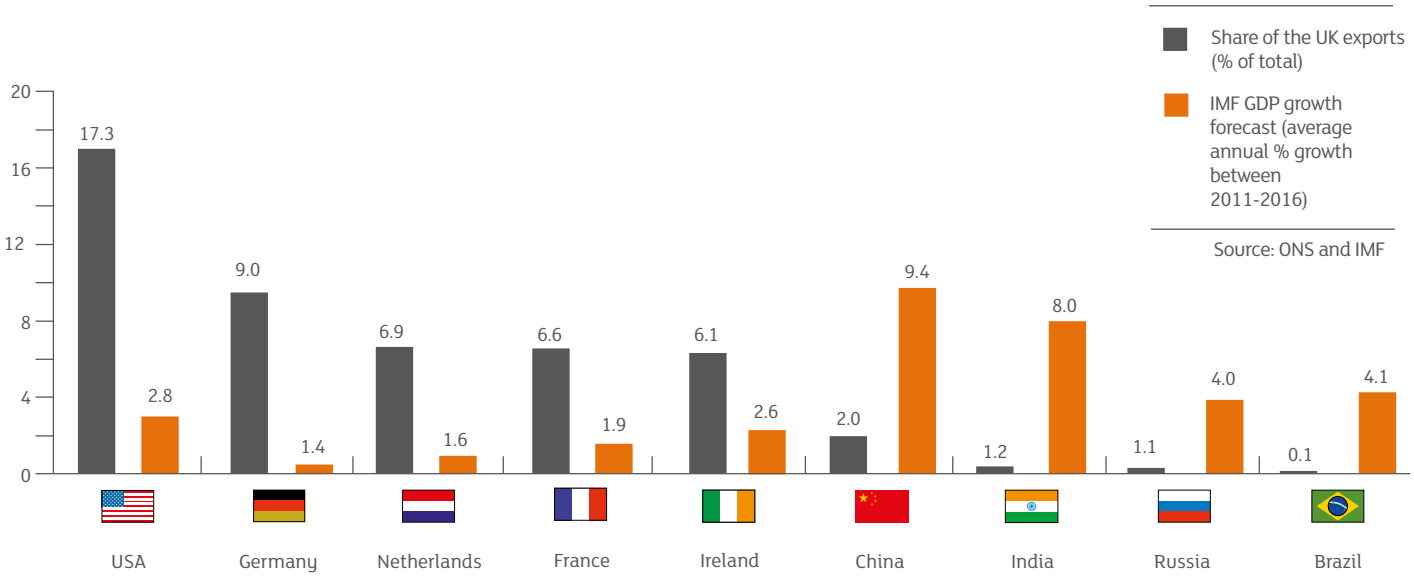
Your questions answered

Destination of UK exports compared with GDP growth forecasts



Where are the future growth markets for UK businesses?

UK businesses are adjusting to a new world, in which the biggest growth opportunities for the future are often to be found in distant and less familiar markets.

Today the UK conducts most of its trade with Europe. For example, Germany, France, the Netherlands and Ireland alone account for 29% of UK exports, versus 17% for the US and a mere 2% for China (see chart). But with growth in Europe constrained, and likely to remain so for the foreseeable future, a number of booming emerging markets are set to assume much greater importance as trading partners in the coming years.

Tapping into these fast-growth markets offers UK SMEs a huge opportunity to accelerate growth. For example, the CBI estimates that if Britain could achieve its export potential, it would inject £20 billion into the economy by 2020, equivalent to 1.5% of GDP[1].

There are signs that firms are beginning to exploit these opportunities: exports to the BRIC markets (Brazil, Russia, India and China) are growing strongly, with the total value of UK exports to the BRICs rising 42% between 2008 and 2011. However, that growth has been achieved from a very low base and exports to BRICs account for only around 5% of total exports[2]. Stepping up the pace of exports to emerging markets is a key priority for the UK government, which wants to double UK exports to £1 trillion by 2020[3].

How easy is it for UK SMEs to access these markets?

It's easy to talk about exports, but for smaller business in particular, the move into new and unfamiliar markets can be quite daunting.

There's the need to research and understand destination markets thoroughly. The selection of key local partners is also an area where companies need to take care. On top of this, one of the biggest concerns is uncertainty and risk around assuring payment when trading with less known markets.

Not surprisingly, these issues have deterred many UK SMEs from taking more of a lead on exports. But the rewards of taking your business into global export markets are substantial. Germany, for example, has maintained a reasonably constant share of world exports of between 8-10% over the last two decades. This has provided an invaluable economic boost during and since the financial crisis.

The UK government is keen to emulate this export success, and is making additional funding available to support SMEs as they target overseas markets. There are also many sources of practical and financial support available to SMEs. These range from banks, to trade associations, to government-supported export agencies. Many have regional offices in the UK to support new exporters, as well as people on the ground in around 100 economies, who can offer practical advice and help.
(See 'More information' on page 4.)

[1] Winning overseas: boosting business export performance, CBI, 2011

[2] Winning Overseas: Export destination graph, CBI, 2011

[3] http://news.bis.gov.uk/Press-Releases/Additional-funding-to-help-UK-SMEs-export-680cd.aspx

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So what's holding UK businesses back?

There certainly doesn't seem to be any doubt among business leaders about the opportunities for global trade. For example, the British Chambers of Commerce's Trade Confidence Index recently hit its highest level since 2007[4]. However, given that only one-fifth of UK SMEs currently export, well below the European average, it would seem that there are still significant barriers that prevent UK businesses from getting on the trade trail[5]. Some of those barriers include:

Difficulty in identifying the right markets and tailoring a strategy to suit a potentially very different business and economic environment.

Understanding the cultural norms for doing business.

The absence of trusted local partners in new markets.

Managing the risks and uncertainty surrounding doing business with new trading partners, particularly ensuring that contracts and payment terms are watertight.

The complexity of dealing with a different legal and regulatory environment, including protecting intellectual property.

Minimising currency risks such as volatile exchange rates and high inflation.

These are all issues that deserve careful consideration, but none are insurmountable.

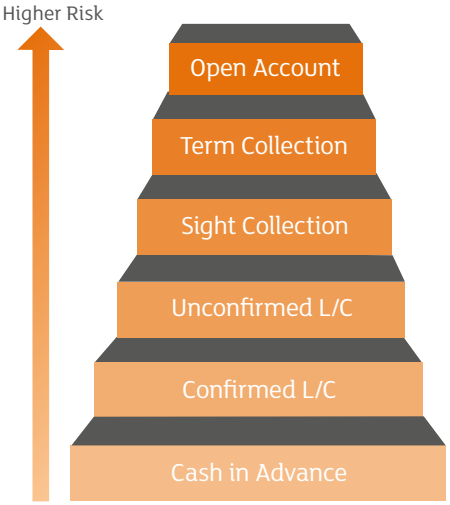
[4] http://www.britishchambers.org.uk/policy-maker/policy-reports-and-publications/dhl-/-bcc-trade-confidence-index-q2-13.html

[5] http://www.cbi.org.uk/business-issues/smes/exporting/

How can I reduce the risks while accelerating my business in these markets?

Fortunately there is a wide range of tools available to mitigate the risks faced by new exporters, particularly financial risks such as getting paid, managing cashflow and managing currency risk.

The exporters' risk ladder



1 Getting paid

Understandably, getting paid and getting paid on time are among the most common concerns for new exporters.

Most transactions whether within the UK, or across international borders, are carried out via **'Open Account'**. The exporter ships the goods with an invoice and awaits the payment from the importer. The importer has the advantage as there is no guarantee of payment on time or even payment at all. This has led to the development of more secure payment methods.

One of the most common is a **Letter of Credit (L/C)**. Internationally recognised, L/Cs provide a secure method of settlement, as they guarantee payment. This is important if you are dealing with a new market, country or trading partner.

Documentary collections also provide a secure, universally-recognised way of sending and receiving payments overseas. The banks for each party act as agents in the transaction, handling and coordinating the payment and exchange of documents. Collections can be 'term' (paid at a specified later date) or 'sight' (paid immediately on receipt of goods).

Bonds, guarantees and standby letters of credit provide peace of mind that your buyer has the ability to pay for your goods. Bonds and guarantees are a commitment by your bank to make payment, providing the terms of the bond or guarantee are met. Standby L/Cs can be put in place for a specified period to support your normal open account trading.

Cash in advance means the exporter receives the payment for goods before they have been shipped. The importer trusts the exporter to honour the contract and deliver the goods on time and as specified.

2 Managing cashflow

From the moment you take an order, through manufacturing, shipping and receipt of goods, there are many times where your business may need funding. Principal among these are:

Pre-export finance - This can cover a range of uses; for example, to cover the cost of raw materials or extra labour you need to fulfil a new contract. Pre-export loans are short-term loans tailored to a specific transaction and are repaid when your customer pays you.

Post-export finance - This allows you to offer your clients payment flexibility, such as extended payment terms, that you might not otherwise be able to fund from existing cashflow. By offering flexible payment terms you may be able to secure more contracts.

Invoice Finance – This includes a number of funding solutions that allow you to turn unpaid invoices, inventory or assets into cash.

Supply Chain Finance – These solutions aim to ease payment pressures along the supply chain, each element of which is under pressure to receive payment as early as possible. Leveraging the buyer's financial strength and approval of a supplier's invoices enables working capital to be released sooner.

3 Managing currency risks

Exchange rates can be volatile. If they move in an unfavourable direction, they can have a negative impact on your finances, the cost of imports and the value gained from exporting goods and services, with knock-on effects on your profitability and cash flow. FX hedging allows you to identify, qualify and manage your FX risks.

RBS perspective

"The UK has an extraordinary history as a trading nation that goes back centuries. Even today, Britain is still known for its open economy and international outlook, which is why so many multinationals are headquartered in Britain.

Against this backdrop, it's surprising that Britain punches so far below its weight as an exporting nation. But it does. Its share of global exports has been in decline for decades.

It is critical for the UK's long-term economic health and competitiveness that companies focus on the opportunities offered by export markets. And it's also clear that the fastest growing markets will be concentrated in the developing world. The rise of the BRICs has been well charted, but we are now seeing the emergence of large numbers of affluent consumers in these countries – a shift that makes them increasingly attractive export destinations for UK companies of all sizes.

UK SMEs should position themselves to benefit from global growth markets. Unfortunately, many businesses we talk to are held back by a range of barriers, including practical concerns about some of the risks and uncertainties, through to not knowing where to get started.

Fortunately, there is a range of proven solutions to many of these issues, and businesses will be pleasantly surprised to see how much support there is out there for companies who want to start exporting. Government agencies, trade bodies and banks can all provide guidance, research and contacts to new exporters.

Importantly, there is also help in managing the risks, including addressing that key question when contracting with unfamiliar partners: will I get paid, and in a timely fashion?"

Where do I go for more information?

RBS: www.rbs.com/perspectives

Find our country profiles of key export markets here: www.rbs.co.uk/corporate/international/g0/country-trade-insight.ashx

UK Trade & Investment, the government's trade promotion body: www.ukti.gov.uk

UK Export Finance supports exports to, and investments in, markets across the world: www.gov.uk/government/organisations/uk-export-finance

www.opentoexport.com/

The British Chambers of Commerce offers export readiness training and access to market information: www.britishchambers.org.uk/business/international-trade