Finance for Australian Exporters

Five ways to manage your export cashflow

Contents

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Introduction

How to get on the path to positive cashflow

For small to medium businesses in the export market, having access to cash is critical. As an exporter, your working capital cycles can be very long, and you'll need cash to cover many costs. However, securing a source of cash when you start out in exporting isn't always easy.

This paper can help give you guidance on whether your business is in the best possible cashflow position to take on the export market.

It provides simple, step-by-step guides to some of the key cashflow challenges facing exporters – from preparing your business and handling new export contracts and payments, to managing growth. It also includes tips to help you follow up on new opportunities, so you can build on your success.

Achieving positive cashflow: the challenges

1. The challenge of accessing cash

For a new business, having enough cash to establish yourself in an export market can be a significant challenge. Finding customers is only one of the factors to establish your export business. You'll also need enough working capital at hand to keep the business moving while you're shipping or waiting for payments.

To minimise cashflow issues, you should consider protecting your business with strong contracts and favourable payment terms. For example, you may choose to ask for an upfront deposit, interim payments and shorter payment periods.

There may be times when you need to rely on external finance to ensure you have access to working capital to keep the business going in between payments.

If you're looking for a loan, the most obvious place to start is at your bank. However, your bank may not always be able to assist: you may not have the level of physical assets needed to use as security against a loan, or perhaps you're exporting to an emerging market with a high-risk profile.

What's more, as a relatively new business, your earnings profile could be variable. This could discourage banks, who may rely on your historical financial records to build a risk profile for your business.

2. Managing working capital while growing

A growing business is good news, but it can create significant working capital shortfalls.

For instance, an overseas customer may award you a much larger contract than the value of your domestic business. That's great news if you want to grow your company – but it could also mean that you'll need more money to hire extra staff or to order more stock from suppliers to meet increased demand.

What's more, if you're negotiating a contract with an international company, especially one that's larger or more experienced, the terms of payment may be weighted in their favour. So it may be difficult to get an advance payment from your buyer – or you may need to wait for a long time before you receive any payment at all.

To avoid a funding shortfall it's important to understand the financing options available. Bank guarantees and bonds can help to bridge the cashflow gap between paying your suppliers and receiving payment. Or you may need to seek out additional finance such as a line of credit or a short term loan.

3. Managing international payments

Even if you've got a successful track record of managing cashflow while doing business locally, managing international payments comes with its own risks. These may include country or political risks, currency risks, corruption, risk of non-payment and more.

How to get cashflow positive

A world of opportunities

Managing the cashflow challenges of exporting can be daunting. On the plus side, becoming an exporter can open your business up to a world of opportunities. These include:

- A significantly larger pool of customers to promote and sell your goods or services to.
- More diverse markets can help you increase your competitiveness and mitigate risk.
- Increased economies of scale.
- The potential to increase your profits.

The key to exporting successfully is to understand and manage your risks. That way, you'll be able to make the most of the opportunities, and be on the way to becoming cashflow positive.

Discover how Efic can help your business take on the world

Efic provides Australian export businesses with financial assistance to help them grow, when their bank may not be able to assist.

To find out more about how Efic could help your business, go to **efic.gov.au** or phone **1800 093 724.**

Challenge 1:

Preparing your business

Before you start exporting, get a clear understanding of where your domestic business stands. That way, you'll know what resources you have – and identify any funding gaps.

A key thing to consider when thinking of exporting is whether you have a viable export market. Your export strategy should align with your overall business plan, outlining your export objectives and action plan, and include your budget, operational model and any partners you may have. You should also create a cashflow forecast to help you identify potential cashflow gaps.

Create a cashflow forecast

A cashflow forecast helps you find out if your business can cover its running costs and identify any periods when you will have more cash going out than coming in. You can then decide if you need finance to cover funding gaps.

"Your forecast will help you understand if there's a long wait between paying your suppliers and getting paid yourself," explains Andrew Watson, Executive Director, Export Finance at Efic.

"If there is, you'll need to work out how long it will continue for, and how you will fund it. You'll also need a buffer if costs blow out or the buyer doesn't pay on time."

How to create a cashflow forecast

To create your cashflow forecast, you will need:

- Receipts for any business expenditure.
- Records of any other costs such as wages, paying suppliers, purchasing assets, bank and credit card fees and charges.
- Cash inflows such as income from sales, any loans or grants, personal equity from business owners or shareholders, the sale of assets, royalties and any tax refunds or GST rebates.
- An estimate of your company's peak cashflow deficits.
- If you are taking out more credit, what your potential repayments will be.
- If you already have an export contract, when you expect payment from customers.
- A list of any fixed overheads or existing debt repayments.

Building your business' creditworthiness

All businesses are likely to need credit at some time – especially when exporting for the first time. A cornerstone of building your business' credit profile is to establish strong financial systems, so it is simpler to get finance when the time comes.

Efficient accounting systems that help you understand your financial position, good relationships with reputable accounting and financial advisers, and a clear, accurate business case will help.

If you're borrowing for export, you will also need to be able to identify cashflow issues that relate specifically to the export part of the business – keeping them separate from your domestic business.

Establish strong financial systems for your export business from the start

- Ensure you have a robust export strategy that outlines your financial resources, including the sustainability of your export budget.
- Use a good accounting system.
- Build a strong relationship with your business banker by keeping them informed of any developments in your business.
- Choose an accounting firm that has experience working with small businesses – especially with exporters.
- If you have a financial adviser, ask them to review your export strategy regularly.

Challenge 2:

How to manage a new export contract

Opportunity versus risk

You have your export strategy and cashflow forecast in place, and you've received interest from overseas customers.

Congratulations! By expanding into new markets, you'll have the chance to grow your business and customer base. But as with every opportunity, there are also risks that you'll need to identify and manage.

What are the risks?

Key risks for new exporters include:

- **Non-payment (credit or non-performance risk):** Your buyer may be unable to pay, or refuses to pay. This risk is greater with a new customer.
- **Currency risk:** The exchange rate could move against you between the time you negotiate the contract and the time your customer pays you in a foreign currency.
- **Country and transfer risk:** A change of government policy could change trade laws or restrict the amount of cash leaving the country, impacting your ability to do business.

Other risks for your business can include:

- operating in a new jurisdiction with laws you don't understand or know about
- dealing with overseas banks that may be unstable
- having your business disrupted by unreliable shipping or delivery schedules – for example, overseas customs holding up your goods or refusing to let them into the country.

Non-payment (credit or non-performance risk)

The biggest risk for a new export contract is that you won't get paid – and the bigger the transaction, the greater the risk can be. If you're starting a contract with a new buyer, it's wise to go slowly at first.

"If possible, start with a small delivery – then if everything goes smoothly, you can increase delivery sizes," says Andrew Watson, Executive Director, Export Finance at Efic. "Once you're confident that your overseas customer will pay regularly and on time, then you can decide how much credit you'll extend to them."

Don't be afraid to go back and forth to negotiate more favourable terms where you feel there might be scope to do so, such as receiving a deposit before you send goods or perform services. Remember that you've received the contract because your business has something special to offer the buyer. So try and negotiate – your buyer may be happy to meet your requests.

Tips for securing payment

- Be very clear what the payment terms are, and how your customer will guarantee payment.
- Ensure your contract clearly outlines what you need to deliver and where. Make sure your lawyer reviews the contract – especially if it's complex or if there's anything you don't fully understand.
- Secure a deposit before your goods are shipped.
- Avoid giving credit to new customers.

Currency risk

If your cost base is in Australian dollars but your customer receipts are in another currency, you're exposed to currency risk. While a depreciating Australian dollar can benefit you, a stronger Aussie dollar can erode your profitability.

Depending on the size of your contract, you may wish to hedge your currency. For instance, you might stipulate that the contract is in Australian dollars. Or you might put a forward contract in place, where you and your trading partner agree to exchange a specified amount of each other's currency.

It's not always necessary or even beneficial to hedge. If you're not sure, talk to your accountant, financial adviser or bank to help you decide what's best for your situation.

Country and transfer risk

Do your homework about the country to which you're exporting and try to understand its business culture.

Make sure you understand government regulations, and whether you will need certain licences or approvals before your goods or services can be received. Remember to check the relevant customs regulations, both here in Australia as well as at your export destination, to avoid unnecessary delivery delays.

Where possible, it can be helpful to have people on the ground who understand the market, including how to manage negotiations and payments.

Austrade or your local chamber of commerce can also be a great place to start. Or speak to other businesses who know this market's advantages and pitfalls.

Receiving legal advice on your contracts

It's important to get legal advice on your contracts – even when they seem quite straightforward. A professional perspective can help identify hidden issues you may not be aware of – and help you avoid any costly mistakes.

"The biggest legal risk for exporters is if you didn't understand your contract or got into it too quickly and didn't take any legal advice," says Andrew Watson, Executive Director, Export Finance at Efic. "There can also be issues in certain countries where taking legal action from Australia and trying to enforce a judgment of an Australian Court overseas can range from very difficult to almost impossible."

Managing your contract

- Understand your company's financial position, and make sure you have the resources to deliver on your new contract and your existing business contracts.
- Understand the options you have for getting the finance you need.
- Make sure your finances are up to date and your documentation is ready so you can move quickly if you need to apply for credit.
- Don't accept a contract you won't be able to fulfil, and have a plan B in place in case you reach capacity in your own production. For instance, consider teaming up with another business to help you produce the extra goods or services if you're unable to produce them yourself.

Case study: PowerfulPoints covers cashflow gap with new export client

Since 2003, **PowerfulPoints** has been producing high quality presentations for blue-chip companies – from traditional slide shows to full-scale video productions. They moved into the overseas market in 2007 after securing a large blue-chip account in the Asia-Pacific, the Middle East and Africa. The company now regularly deals with overseas clients and has offices in Singapore and China.

PowerfulPoints founder and CEO, Lee Featherby, said that it's critical for businesses entering new international markets to have a stable domestic business.

"Whenever you go into any market it's going to cost more than you predict and take longer than you think," Featherby said. "Your Australian enterprise must be able to fund that or you could end up in trouble."

According to Featherby, the major risk of exporting as a service provider is default on payment. Because PowerfulPoints deals mainly with blue-chip companies, non-payment is usually not a risk for them. But if they work with smaller, new companies, they manage the additional risk by asking for a 50% payment upfront.

PowerfulPoints also faces currency risk when trading with countries with protected currencies. To mitigate this risk, they ask for payments to be made in US or Australian dollars – with an exchange rate that is fixed at the time of signing the contract.

For projects with long completion times, Featherby generally asks for a progress payment – but this isn't always possible.

"We had a large project that was going to take nine weeks to complete, and we wouldn't receive payment until 60 days after the end of the month of that project," he explained. "The client then changed their mind on what they wanted us to deliver after the contract was signed, so the project ended up taking 780 hours instead of 350."

To help cover the cashflow gap, Featherby approached Efic for funding – securing finance for 80 per cent of the contract's value.

"The process was so easy," said Featherby. "We provided a copy of the contract and some other paperwork and filled in a form which took about an hour to complete."

Challenge 3:

How to manage the payment process

Late payments can deprive a business of the working capital it needs to operate – so having a strong payment system in place is vital.

This is particularly important for exporters, as overseas payment terms can be much longer than Australian cycles – which can be especially challenging for businesses that already have long working capital cycles.

Help while you're waiting for payment

If there's a long gap between producing products and services, and receiving payment, you may need to consider a loan to cover your working capital requirements.

Efic can help with loans or short-term guarantees. See **Challenge Four: How to manage growth** to find out more.

Agree payment terms

Start by clearly outlining your payment process with your customers.

For instance, will you require a part payment before sending any goods – and if so how much? If the contract you're working on will take place over time, do you want a progress payment? How long are your terms from the time your customer receives the goods or services to the time you get paid?

Remember to negotiate your payment terms with your suppliers too. For instance, you can ask them to extend terms of payment, or start the payment terms from once you've received your goods.

Agree payment methods

Find out how the buyer intends to make their payment. For instance, will they use a credit card, a bank transfer or another type of transfer system, such as Western Union?

Two common methods of collecting overseas payments include:

- **Letter of Credit.** This is essentially a guarantee from your buyer's bank that they will pay you when the buyer has received your goods, and you have met all the terms and conditions listed in the letter of credit.
- **Documentary Collection.** The bank collects payment for you, by sending the shipping documents and payment instructions to your buyer's bank.

A Letter of Credit is more expensive, but is also more secure than a Documentary Collection. So, it may be best to use it for a new buyer, if you're confident that their bank is creditworthy.

Your bank can advise you on the most appropriate payment system for your situation. You should also understand the regulations governing each payment method, and any additional costs they have, such as international transfer fees.

Keep in control of your payments

- Before you sign a contract, have a payment process in place.
- Take your time at the beginning of the contract to establish a good relationship with your customer.
- Make sure you understand the cashflow position of your business – and that you have cash forecasts in place, which you can adjust over time as you understand your business better.
- Don't forget to seasonally adjust your projections to ensure your cashflow will remain stable.
- Consider a loan to help cover any gaps in your working capital cycle.

Case study: Zonte's Footstep manages long cashflow cycles

Anna Fisher is Director and Chairperson of **Zonte's Footstep**, a South Australian winemaker making inroads in the international market. Having built a strong domestic business, the company looked to export, starting a relationship with a foreign liquor board in 2011.

Like most wine brands, Fisher says the company faces the challenge of a very long working capital cycle.

"For our current vintage, we started pruning in June 2015, with the harvest taking place between February and April 2016," Fisher said. "We won't bottle this wine until July 2017, then we sell it over a period of up to 12 months."

Even once it's sold, Fisher says payment for the wine is slow to arrive.

"The [Liquor Board's] payment terms are 90 days from receipt of shipment," says Fisher. "That means it can take up to two years from incurring our first costs to receiving any revenue. If something goes wrong it can make it even longer, and cashflow becomes critical."

Fisher stresses that negotiating payment terms with new export clients and checking their references is critical, especially in jurisdictions where it may be hard to legally enforce a contract.

"With new markets and customers, you go in cautiously, but as you see consistency in payment, their risk profile reduces."

"Once we know our clients better we can negotiate extended terms if needed, to build long-term relationships. We don't think it's worth getting into one-off contracts here and there – we're in it for the long haul."

To manage cashflow, Fisher forecasts on a weekly basis, for three months in advance.

"We use a plug-in online tool called Cash Flow Story, which gives our cashflow results to date. It helps forecast trends so we know what we're likely to borrow if needed to cover any gaps."

But, given the long cashflow cycle, Fisher says it would have been very difficult to fulfil their export orders without the assistance of a Small Business Export Loan from Efic.

"If you've done all your homework you can apply online in two hours, and have the funds in your bank account within nine business days."

Challenge 4:

How to manage growth

Your export business is up and running – and now there are opportunities to take on larger contracts. That's exciting – but before you commit to new clients, be sure that you have a growth plan for your export business.

Planning for growth

While it may be tempting to take on a large contract, without the time or money to ramp up your resources and equipment you could end up unable to meet your orders.

Andrew Watson, Executive Director, Export Finance at Efic, explains: "One of our customers had a win for a contract, but it required a rapid ramp-up and a very short time to deliver, which they didn't anticipate. They now realise they don't have the resources and experience available to deal with the big customer that they've landed."

To ensure you can take advantage of the opportunity without over-extending, make sure you plan to have enough people and equipment to deliver on the contract, and work out what your additional working capital requirements may be – and how you intend to fund them.

Getting ready to grow

- Plan your growth and the resources you will need.
- Talk to your adviser or accountant about the steps you need to take to ensure you're financially ready for growth.
- If you need help with finance, talk to your bank first.
- Consider alternative sources of finance, such as Efic, if your bank can't help.

Sourcing export finance

So where should you go to finance the growth of your export business?

"It's an age-old question as to whether to use debt versus equity to grow," says Watson. "Some business owners choose to use equity from their home as security, and re-mortgage in the early stage of growing their business."

If you decide to borrow money to grow your export business, your first port of call should be your bank. However, if your business can't meet your bank's lending terms, Efic may be able to help.

In addition to considering the level of security offered for the loan when you apply, Efic will also assess your company's potential capability as part of your application. Efic will also examine your export contract, and understand how your company can deliver on it.

How Efic can help

Here are some ways that Efic can help if your bank is not able to assist:

Loans and guarantees

You might not have the level of security that your bank requires to approve finance for your export-related contract, or your bank may be reluctant to approve such finance if it doesn't have the risk appetite.

If you're an established or first-time exporter, Efic may be able to help you with a direct loan, or by providing a guarantee to your bank so they can lend you the finance you need. Efic may also be able to help you if you're part of an export supply chain.

Export Line of Credit

If you're a small to medium enterprise (SME) with several export contracts with different buyers, or you're part of an export supply chain, Efic's Export Line of Credit may be suitable for your needs.

With an Export Line of Credit, you can access working capital finance before your goods or services are exported overseas. The loan allows you to draw down and repay funds multiple times, so you can access extra working capital when you need it. You can also arrange to link your payments, so that the proceeds can be redrawn when you're paid by your overseas buyers.

Export Venture Debt

If you're experiencing high growth and have received at least one round of venture capital financing, Efic may be able to provide a loan to help provide working capital between investment rounds, for costs related to a secured export contract.

Case study: BroadSource uses line of credit to expand globally

Australian company **BroadSource** provides IT solutions and platforms for global telecommunications companies. After establishing itself in the Australian market, BroadSource won its first overseas contract around two years ago – and the company hasn't looked back.

From the start, founders Jason Thals and Haydn Faltyn say they wanted a business that they could operate anywhere and easily scale up, driving their decision to put their systems in the cloud.

"The cloud-based nature of the business has meant that it is able to operate anywhere there is an internet connection. It also allows us to expand very easily. There are no major decisions and costs to expand to cope with additional needs – which means that growth can be very incremental," said Faltyn.

Thals says that one of the key decisions in the company's global success was its corporate structure.

"We made the decision early on to go with a corporate structure rather than a small business structure. We created a holding company located in Australia, then created BroadSource Europe and BroadSource US."

"This has enabled our business to expand and globalise – and as we grow, we can easily add more resources and entities."

He said that the structure also helps to simplify tax compliance and currency exchange.

"We learned early on why Europe wanted to create the EU and a single currency – when you go between currencies, GST, VAT, different taxes and currency exchanges!"

"We had to create the different structures to not leak too much of our precious revenue into foreign trading. Our structure helps us to retain the same currency, and minimise the number of times we convert. If we don't, we can lose 3+ percentage points in converting currencies around the world."

One of the biggest challenges for the company early on was achieving the finance it needed to set up and grow.

"Because we don't have physical assets, banks weren't really an option for us. And we didn't want venture capital, as we didn't want to hand over equity in the business we were working to build," says Thals.

Instead, he says that Efic's support was an important factor in the company's success.

Challenge 5:

How to keep the opportunity alive

You've succeeded – now what?

Once you've entered the export market, you need to ensure that you can turn short-term success into a sustainable and regular revenue stream. To do this, you may need to invest even more capital to find and deliver on new opportunities.

This could include setting up a permanent presence in your target markets. It may also mean building a network of distributors to ensure greater penetration of the market. Having a local network of trusted business partners – such as accountants and lawyers – can help ensure you can manage your tax liabilities appropriately and comply with local regulations.

As you grow, you may also need to consider whether your business structure is well-suited to an international business. Having the right corporate structure can not only streamline your business processes, it can make it easier to expand to new locations and grow.

Managing new opportunities

Once you have a foothold in your target market, you're in a good position to build a growth strategy. Depending on your business, you may find that word of mouth can deliver new opportunities. The better you understand your new market, the easier it is to know who to talk to and deliver solutions to meet their needs.

If you plan to expand into multiple markets, it's important to work out how easily your current business model can be scaled for growth. Also consider the impact of rapid growth on the domestic business and ensure that you manage for success on both fronts.

How you set up your corporate structure and employee network can have a big impact on your ongoing success. For example, you may choose to set up independent subsidiaries to operate overseas to try and simplify tax and currency impacts on each part of the business, while ensuring they remain separate enough to operate independently.

If your business relies on information systems or manufacturing processes, are they flexible enough to be scaled up and adapted to meet international demand? Will you be able to simply ramp up existing systems and processes – or will you need to replicate them in your target markets?

The right solution will depend on the type of business you have – but the earlier you consider how you will effectively manage growth, the better it will be for the business overall.

Build strong relationships

To help build a sustainable business overseas, you will also need reliable relationships in place. With your clients – who can spread the word and act as advocates for your business – and with your employees, who represent you around the world.

Importantly, you should consider working with legal, accounting and foreign exchange professionals who have experience in the markets you deal with. They can help you to identify and manage potential issues and help you to streamline the business' regulatory and taxation compliance, while making the most of currency conversions.

Business advisers who specialise in export businesses can also help to open doors overseas, and help make you aware of new opportunities. And of course, government agencies such as Efic and Austrade may be able to provide advice and potential financial support for when you need it.

Staying ahead

- Have processes in place to help you cover costs when business is slow.
- Keep on top of your finances and know your financial position at all times.
- Work closely with your bank, which can help you secure finance to cover gaps in working capital (and remember, Efic could also help you if your bank can't).
- Stay in close touch with your accountant and financial adviser (if you have one) to make sure your domestic and export business plans evolve with your business.

Resources for Australian exporters

Efic: **efic.gov.au**

Austrade: **austrade.gov.au**

Export Council of Australia (ECA): **export.org.au**

Your local chamber of commerce

Australian Government

Efic Finance for Australian Exporters

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