Semester VI

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17BAU602B DSE – 4: INTERNATIONAL TRADE POLICY AND STRATEGY	**6**	**2**	**-**	**6**

SCOPE

International Trade Policy and Strategy represents the basis of international trade, policy instrument, global institutional structure, regional trade blocks, industrialization strategy, IE Code, strategies of emerging economies and export control regulations.

OBJECTIVES

- To get the students acquainted with understanding of the basis for international trade and strategies.
- To enlighten the students knowledge in global institutional structure and trade strategies of developing countries and trade partners of India

UNIT I

Review of Economic Theory on International Trade - Basis for international trade - Gains from trade - Distributional issues - Policy instruments and their impact - Political economy - Trends in Global Trade and Balance of Payments with special reference to India - Historical roots of today's international trade – Composition - Origin and destination of global exports and imports - Trade in invisibles - Balance of payments - Current account and Capital account - Capital flows and foreign exchange revenues - External Debt.

UNIT II

The Global Institutional Structure - GATT (General Agreement on Trade and Tariffs) - WTO (World Trade Organization) - Regional Trade Blocks and Trade Agreements.

UNIT III

India's Industrialization Strategy and International Trade - Review of Economic planning strategies and issues - Early phase; the 1970s and 1980 - Policies since 1991 - Exim policy - Structure of tariffs and restrictions - Currency depreciation and convertibility - Export Promotion Zones, Special Economic Zones, Importer and Exporter Code (IE Code).

UNIT IV

Experience of Select Developing Countries - Analysis of the trade strategy and the policy framework in two select large countries and comparison with India - Impact of trade on growth - agriculture - inequality - poverty and other developmental indicators - Case Studies on Trade Strategies of Emerging Economies - China and ASEAN (Association of South East Asian Nations).

UNIT V

Exchange Control Regulations - RBI Guide Lines - Authorized Dealers - FEMA, Permitted Currencies - ACU - Export Realization - Procedure and Related documents - Trends in India's Exports and Imports.

SUGGESTED READINGS:

TEXT BOOKS

1. Balagopal, T.A.S .(2010). *Export Management.* Mumbai : Himalaya Publications.

REFERENCES

1. Srinivasan, T. N., & Suresh D Tendulkar. (2003). *Reintegrating India with the World Economy*. Washington: Institute for International Economics.
2. Connor & David, E. O. (2006). *Encyclopedia of the Global Economy*: *A guide for students and researchers*. New Delhi: Academic Foundation.
3. Bibek Debroy, & Debashis Chakraborty. (2007). *The Trade Game: Negotiation trends at WTO and concerns of developing countries*. New Delhi: Academic Foundation.
4. Paul R., Krugman, Maurice Obstfeld., & Marc Melitz. (2016). *International Economics: Theory and Policy* (10^{th} ed.). New Delhi: Pearson Education.
5. Rajiv Sikri. (2013). *Challenge and Strategy: Rethinking India's Foreign Policy*. New Delhi: SAGE Publication India Pvt., Ltd.
6. Francis Cherunilam. (2013*). International Trade and Export Management*. Mumbai: Himalaya Publications.
7. Varma & Agarwal. (2006). *Foreign Trade Management: Forward Book Depot.* New Delhi: Academic Foundation.
8. Manab Adhikary, (2011). *Global Business Management*. New Delhi: Macmillan India Limited.

INTERNATION TRADE STRATEGY AND POLICY (17BAU602B)

UNIT I

SYLLABUS

Review of Economic Theory on International Trade - Basis for international trade - Gains from trade - Distributional issues - Policy instruments and their impact - Political economy - Trends in Global Trade and Balance of Payments with special reference to India - Historical roots of today's international trade – Composition - Origin and destination of global exports and imports - Trade in invisibles - Balance of payments - Current account and Capital account - Capital flows and foreign exchange revenues - External Debt.

International trade is the exchange of capital, goods, and services across international borders or territories. In most countries, such trade represents a significant share of gross domestic product (GDP). While international trade has been present throughout much of history, its economic, social, and political importance has been on the rise in recent centuries. It is the presupposition of international trade that a sufficient level of geopolitical peace and stability are prevailing in order to allow for the peaceful exchange of trade and commerce to take place between nations.

. Thus international trade is mostly restricted to trade in goods and services, and only to a lesser extent to trade in capital, labor or other factors of production. Trade in goods and services can serve as a substitute for trade in factors of production. Instead of importing a factor of production, a country can import goods that make intensive use of that factor of production and thus embody it. An example is the import of labor-intensive goods by the United States from China. Instead of importing Chinese labor, the United States imports goods that were produced with Chinese labor. One report in 2010 suggested that international trade was increased when a country hosted a network of immigrants, but the trade effect was weakened when the immigrants became assimilated into their new country.

International trade is also a branch of economics, which, together with international finance, forms the larger branch called international economics. Trading is a value-added function: it is the economic process by which a product finds its market, in which specific risks are to be borne by the trader.

Scope: Scope of international business is quite wide. It includes not only merchandise exports, but also trade in services, licensing and franchising as well as foreign investments. Domestic business pertains to a limited territory. Though the firm has many business establishments in different locations all the trading activities are inside a single boundary.

Benefits: International business benefits both the nations and firms. Domestic business have lesser benefits when compared to the former.

To the nations: Through international business nations gain by way of earning foreign exchange, more efficient use of domestic resources, greater prospects of growth and creation of employment opportunities. Domestic business as it is conducted locally there would be no much involvement of foreign currency. It can create employment opportunities too and the most important part is business since carried locally and always dealt with local resources the perfection in utilization of the same resources would obviously reap the benefits.

To the firms: The advantages to the firms carrying business globally include prospects for higher profits, greater utilization of production capacities, way out to intense competition in domestic market and improved business vision. Profits in domestic trade are always lesser when compared to the profits of the firms dealing transactions globally.

Review of Economic theory on International:

The following are noted models of international trade.

Adam Smith's model

Adam Smith displays trade taking place on the basis of countries exercising absolute advantage over one another.

Ricardian model

The law of comparative advantage was first proposed by David Ricardo.

The Ricardian model focuses on comparative advantage, which arises due to differences in technology or natural resources. The Ricardian model does not directly consider factor endowments, such as the relative amounts of labor and capital within a country.

The Ricardian model is based on the following assumptions:

- Labor is the only primary input to production
- The relative ratios of labor at which the production of one good can be traded off for another differ between countries and governments

Heckscher–Ohlin model

In the early 1900s a theory of international trade was developed by two Swedish economists, Eli Heckscher and Bertil Ohlin. This theory has subsequently been known as the Heckscher–Ohlin model (H–O model). The results of the H–O model are that countries will produce and export goods that require resources (factors) which are relatively abundant and import goods that require resources which are in relative short supply.

In the Heckscher–Ohlin model the pattern of international trade is determined by differences in factor endowments. It predicts that countries will export those goods that make intensive use of locally abundant factors and will import goods that make intensive use of factors that are locally scarce. Empirical problems with the H–O model, such as the Leontief paradox, were noted in empirical tests by Wassily

Leontief who found that the United States tended to export labor-intensive goods despite having an abundance of capital.

The H–O model makes the following core assumptions:

- Labor and capital flow freely between sectors
- The amount of labor and capital in two countries differ (difference in endowments)
- Technology is the same among countries (a long-term assumption)
- Tastes are the same

Applicability

In 1953, Wassily Leontief published a study in which he tested the validity of the Heckscher-Ohlin theory. The study showed that the United States was more abundant in capital compared to other countries, therefore the United States would export capital-intensive goods and import labor-intensive goods. Leontief found out that the United States' exports were less capital intensive than its imports.

After the appearance of Leontief's paradox, many researchers tried to save the Heckscher-Ohlin theory, either by new methods of measurement, or by new interpretations. Leamer emphasized that Leontief did not interpret H-O theory properly and claimed that with a right interpretation, the paradox did not occur. Brecher and Choudri found that, if Leamer was right, the American workers' consumption per head should be lower than the workers' world average consumption Many textbook writers, including Krugman and Obstfeld and Bowen, Hollander and Viane, are negative about the validity of H-O model. After examining the long history of empirical research, Bowen, Hollander and Viane concluded: "Recent tests of the factor abundance theory [H-O theory and its developed form into many-commodity and many-factor case] that directly examine the H-O-V equations also indicate the rejection of the theory."

In the specific factors model, labor mobility among industries is possible while capital is assumed to be immobile in the short run. Thus, this model can be interpreted as a short-run version of the Heckscher-Ohlin model. The "specific factors" name refers to the assumption that in the short run, specific factors of production such as physical capital are not easily transferable between industries. The theory suggests that if there is an increase in the price of a good, the owners of the factor of production specific to that good will profit in real terms.

Additionally, owners of opposing specific factors of production (i.e., labor and capital) are likely to have opposing agendas when lobbying for controls over immigration of labor. Conversely, both owners of capital and labor profit in real terms from an increase in the capital endowment. This model is ideal for understanding income distribution but awkward for discussing the pattern of trade.

New Trade Theory

New Trade Theory tries to explain empirical elements of trade that comparative advantage-based models above have difficulty with. These include the fact that most trade is between countries with similar factor endowment and productivity levels, and the large amount of multinational production (i.e., foreign direct investment) that exists. New Trade theories are often based on assumptions such as monopolistic competition and increasing returns to scale. One result of these theories is the home-market effect, which asserts that, if an industry tends to cluster in one location because of returns to scale and if that industry faces high transportation costs, the industry will be located in the country with most of its demand, in order to minimize cost.

Although new trade theory can explain the growing trend of trade volumes of intermediate goods, Krugman's explanation depends too much on the strict assumption that all firms are symmetrical, meaning that they all have the same production coefficients. Shiozawa, based on much more general model, succeeded in giving a new explanation on why the traded volume increases for intermediate goods when the transport cost decreases.

Gravity model

The Gravity model of trade presents a more empirical analysis of trading patterns. The gravity model, in its basic form, predicts trade based on the distance between countries and the interaction of the countries' economic sizes. The model mimics the Newtonian law of gravity which also considers distance and physical size between two objects. The model has been proven to be empirically strong through econometric analysis.

Contemporary theories

Ricardo's idea was even expanded to the case of continuum of goods by Dornbusch, Fischer, and Samuelson This formulation is employed for example by Matsuyama and others. These theories use a special property that is applicable only for the two-country case.

Neo-Ricardian trade theory

Inspired by Piero Sraffa, a new strand of trade theory emerged and was named neo-Ricardian trade theory. The main contributors include Ian Steedman (1941–) and Stanley Metcalfe (1946–). They have criticized neoclassical international trade theory, namely the Heckscher-Ohlin model on the basis that the notion of capital as primary factor has no method of measuring it before the determination of profit rate (thus trapped in a logical vicious circle). This was a second round of the Cambridge capital controversy, this time in the field of international trade.

The merit of neo-Ricardian trade theory is that input goods are explicitly included. This is in accordance with Sraffa's idea that any commodity is a product made by means of commodities. The limitation of their theory is that the analysis is restricted to small-country cases.

Traded intermediate goods

Ricardian trade theory ordinarily assumes that the labor is the unique input. This is a great deficiency as trade theory, for intermediate goods occupy the major part of the world international trade.

Yeats found that 30% of world trade in manufacturing involves intermediate inputs. Bardhan and Jafee found that intermediate inputs occupy 37 to 38% of U.S. imports for the years 1992 and 1997, whereas the percentage of intra-firm trade grew from 43% in 1992 to 52% in 1997.

McKenzie and Jones emphasized the necessity to expand the Ricardian theory to the cases of traded inputs. In a famous comment McKenzie (1954, p. 179) pointed that "A moment's consideration will convince one that Lancashire would be unlikely to produce cotton cloth if the cotton had to be grown in England." Paul Samuelson coined a term Sraffa bonus to name the gains from trade of inputs.

Ricardo-Sraffa trade theory

Economist John S. Chipman observed in his survey that McKenzie stumbled upon the questions of intermediate products and postulated that "introduction of trade in intermediate product necessitates a fundamental alteration in classical analysis". It took many years until Shiozawa succeeded in removing this deficiency. The Ricardian trade theory was now constructed in a form to include intermediate input trade for the most general case of many countries and many goods. Chipman called this the Ricardo-Sraffa trade theory.

Based on an idea of Takahiro Fujimoto, who is a specialist in automobile industry and a philosopher of the international competitiveness, Fujimoto and Shiozawa developed a discussion in which how the factories of the same multi-national firms compete between them across borders. International intra-firm competition reflects a really new aspect of international competition in the age of so-called global competition.

International Production Fragmentation Trade Theory

Fragmentation and International Trade Theory widens the scope for "application of Ricardian comparative advantage". In his chapter entitled Li & Fung, Ltd.: An agent of global production (2001), Cheng used Li & Fung Ltd as a case study in the international production fragmentation trade theory through which producers in different countries are allocated a specialized slice or segment of the value chain of the global production. Allocations are determined based on "technical feasibility" and the ability to keep the lowest final price possible for each product.

Comparative Cost Theory

This theory is developed by a classical economist David Ricardo. According to this theory, the international trade between two countries is possible only if each of them has absolute or comparative cost advantage in the production of at least one commodity. This theory is based upon following assumption

- There are only two countries and two commodities
- There is no governmental intervention in export and import
- Only labor is factor of production. Quantity of labor used gives cost of production

- There is perfect mobility of labor within the country but not between the countries
- There is no cost of transportation between the countries
- The law of constant returns to scale operates in production.
- The units of labor is homogeneous
- The units of each commodity in both countries are homogeneous

According to comparative cost advantage theory of international trade, each country exports the commodity in which it has cost advantage and imports the commodity in which it has cost disadvantage. This theory can be explained as following:

Comparative cost advantage

If a country can produce both commodities with less cost than another country but in different ratio, the country is said to have comparative cost advantage

Country	**Labor required to produce clothe**	**Labor required to produce shoe**
Nepal	10	4
India	20	12
ratio	10/20=0.5	4/12=0.33

In the above table, the cost of production of clothe in Nepal is only 50% of cost of production of clothe in India. In case of shoes, the cost of production is only 1/3rd of cost in India. It shows that Nepal can produce both commodities with fewer cots than India. But in order to take advantage, it produces only shoes land let India produce clothe for it. Nepal produces shoes and exports to India. India produces clothe and exports to Nepal. If they do so, both of them can take benefits.

Absolute cost advantage:

If a country can produce a commodity with less cost but has to bear more cost in the production of another commodity than another country then the country is said to have absolute cost advantage. In this case, both of the countries produce and export the commodities in which they have absolute cost advantage.

Country	**Labor required to produce clothe**	**Labor required to produce shoe**
Nepal	10	8
India	20	4
ratio	10/20=0.5	8/4=2

In the above table, the cost of production of clothe in Nepal is less than in India. But cost of production of shoes is less in India than in Nepal. In this case, Nepal is said to have absolute cost advantage in production of clothe but absolute cost disadvantage in production of shoes. India is said to have absolute cost advantage in production of shoes but absolute cost disadvantage in production of clothe. Therefore, Nepal produces only clothe and exports to India. India produces only shoes and exports to Nepal. Doing it, both the countries can take benefit.

No cost advantage:

If a country can produce both commodities with less cost than another country but in equal ratio, the country is said to have no cost advantage.

Country	Labor required to produce clothe	Labor required to produce shoe
Nepal	10	4
India	20	8
ratio	10/20=0.5	4/8=0.5

In the above table, Nepal is shown able to produce both commodities with less cost than India in equal ratio. It means Nepal has no cost advantage. It is loss to the Nepal to import any commodity form India. That's why it decides to produce both goods for itself. Therefore, India too produces both goods for itself. Hew is no trade between them.

Criticisms

- This theory is not applicable if there are more than two countries and more than two commodities
- In every country there is more or les government intervention in international trade
- There is cost of transportation form one country to another country
- The units of labor are not homogeneous and the workers are paid more or less in different countries
- There may be increasing or decreasing returns to scale
- Labor is not perfectly mobile within the country too. In the modern era, there is mobility of labor form one country to another
- The commodities produced in the different countries differ in quality, taste, size, quantity etc.

Basis for International trade:

Market Fluctuations: Firms conducting trade internationally can withstand these situations and huge losses as their operations are wide spread. Though they face losses in one area they may get profits in other areas, this provides for stabilizing during seasonal market fluctuations. Firms carrying business locally have to face this situation which results in low profits and in some cases losses too.

Modes of entry: A firm desirous of entering into international business has several options available to it. These range from exporting/importing to contract manufacturing abroad, licensing and franchising, joint ventures and setting up wholly owned subsidiaries abroad. Each entry mode has its own advantages and disadvantages which the firm needs to take into account while deciding as to which mode of entry it should prefer. Firms going for domestic trade does have the options but not too many as the former one.

To establish business internationally firms initially have to complete many formalities which obviously is a tedious task. But to start a business locally the process is always an easy task. It doesn't require processing any difficult formalities.

Purvey: Providing goods and services as a business within a territory is much easier than doing the same globally. Restrictions such as custom procedures do not bother domestic entities but whereas globally operating firms need to follow complicated customs procedures and trade barriers like tariff etc.

Sharing of Technology: International business provides for sharing of the latest technology that is innovated in various firms across the globe which in consequence will improve the mode and quality of their production.

Political relations: International business obviously improves the political relations among the nations which gives rise to Cross-national cooperation and agreements. Nations co-operate more on transactional issues.

Gains from Trade

All of the economic theories of international trade suggest that it enhances efficiency. In this regard, international trade is like a new technology. It adds to the productive capacity of all countries that engage in trade. Some of the efficiency is due to comparative advantage, as in the Ricardo and Heckscher-Ohlin theories. In addition, some efficiency comes from taking advantage of increasing returns.

Trade based on comparative advantage should tend to benefit small countries more than large countries. That is because the benefits of comparative advantage are proportional to the difference between the relative prices in world markets and the relative prices that would prevail in home markets without trade. If that difference is large, then a country earns a large advantage from trade. If that difference is small, then there is only a small advantage from trade. Small countries are more likely than large countries to find that relative prices in the world market differ significantly from what would prevail in their home markets.

Another benefit from trade is that it promotes dynamism and innovation within an economy. Improvements in manufacturing quality and productivity in the United States in recent decades have been credited, in part, to the pressure of competition from Japan and elsewhere.

An economy that is closed to trade is one in which inefficient industries and laggard firms are well protected. In fact, studies suggest that barriers to trade are a major cause of extreme underdevelopment.

The countries that are most closed to trade tend to be the poorest in the world. Countries that have reduced trade barriers and increased the share of imports and exports in their economies tend to be among the fastest-growing nations.

According to a World Bank study, twenty-four developing countries that became more integrated into the world economy in the 1980s and 1990s had higher income growth, longer life expectancy, and better schooling. Per capita income in these countries, home to half the world's population, grew by an average of 5 percent in the 1990s compared with only 2 percent in rich countries. China, India, Hungary, and Mexico are among the countries that adopted policies that allowed their people to take advantage of global markets. As a result, they sharply increased the amount of their GDP accounted for by trade. Real wages in these countries rose and the number of poor people fell.

The study also points out that two billion people—particularly in sub-Saharan Africa, the Middle East, and the former Soviet Union—are in countries being left behind. These countries' integration into the world economy has not increased, and their ratio of trade to GDP has stagnated or fallen. Their economies have generally contracted, poverty has increased, and education levels have risen less rapidly than in the more globalized countries.3

Another report notes that exports plus imports as a share of output among the richest countries rose from 32.3 percent to 37.9 percent between 1990 and 2001. Moreover, among developing countries, that share rose from 33.8 percent to 48.9 percent over that period. The success of India and China recently, and Japan, Taiwan, South Korea, and other countries in the 1970s and 1980s, is due in large part to trade.4

The OECD countries, which together have more than $25 trillion in GDP, account for most of world trade. Poor countries account for less than $300 billion in GDP, which is less than one-tenth of world output, and thus account for only a miniscule fraction of world trade.

Distributional issues

At that time footwear was typical of a manufacturing sector in high income countries under pressure from imports from developing countries in East Asia for which policymakers granted additional protection beyond tariffs in the form of quantitative restrictions.

The particular non-tariff barrier analysed in these papers is voluntary export restraints (VER), a quantitative restriction imposed by a government to limit the quantity of goods that can be exported to another country during a specified period of time.

The reason governments impose VERs to limit their own exports is to appease the importing country and prevent the imposition of more draconian and less flexible trade barriers. VERs are typically implemented on a bilateral basis and became a popular form of protection during the 1980s, perhaps in part because they did not violate countries' agreements under the GATT at that time.

However, during the Uruguay Round of trade negotiations members of the newly created WTO agreed not to implement any new VERs and to phase out any existing VERs over a four-year period. It shows high economic costs for UK consumers of the quantitative trade barriers imposed on footwear imports.

The papers address a key technical challenge with regard to a quantitative restriction (QR) on trade — it necessarily induces rationing. If suppliers raise their price in response to the restriction so that there is no excess demand then they are rationed, since they would like to sell more than they are permitted to at the new higher price.

On the other hand, if prices do not rise fully to clear demand then it is consumers who are rationed, since at that price they would like to buy more than they are able to because of the restriction. Such rationing leads to additional welfare costs beyond those that will be normally estimated

Capital Flows and the Balance of Trade

In 2000, U.S. exports were $1.1 trillion and U.S. imports were close to $1.5 trillion. The excess of imports over exports is called a current account deficit. What caused this deficit? Modern economists believe that the trade surplus and capital flows are mutually determined. When a nation's domestic saving (personal saving plus retained earnings of corporations) exceeds the domestic uses of saving (financing its private investment and its government budget deficit), then that nation will run a trade surplus, and vice versa.

Imagine that all international trade took place in the form of barter of goods and services. If you wanted to buy a Japanese car, you would have to offer something of equivalent value in return. In that case, trade in goods and services would have to balance, and there would be no trade deficits.

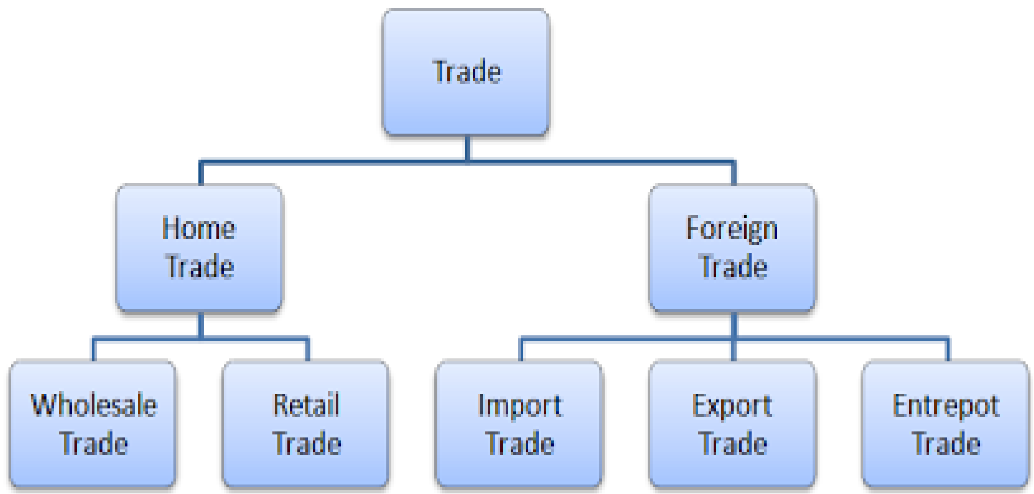
To obtain a Japanese car without trading goods and services, the Japanese have to accept financial assets in exchange for cars. These assets could be dollars, shares of U.S. companies, corporate bonds or other private debt instruments, or U.S. government debt. A country that is accumulating foreign assets will necessarily run a trade surplus. A country that is selling assets to foreigners will necessarily run a trade deficit. A country will accumulate assets when its domestic saving is greater than its domestic uses of saving. A country will sell assets when its national saving is insufficient for its domestic uses of saving.

Typically, one would expect wealthy countries to have excess saving and to invest in capital-poor countries. From this perspective, it is an anomaly that the United States is a capital importer and China is a capital exporter. However, the United States is a relatively attractive country in which to invest, and American policies tend to encourage consumption rather than saving.

Different Types of Trade

Internal Trade

Internal trade is also known as Home trade. It is conducted within the political and geographical boundaries of a country. It can be at local level, regional level or national level. Hence trade carried on among traders of Delhi, Mumbai, etc. is called home trade. Internal trade can be further sub-divided into two groups, viz.,



- **Wholesale Trade**

It involves buying in large quantities from producers or manufacturers and selling in lots to retailers for resale to consumers. The wholesaler is a link between manufacturer and retailer. A wholesaler occupies prominent position since manufacturers as well as retailers both are dependent upon him. Wholesaler act as a intermediary between producers and retailers.

- **Retail Trade**

It involves buying in smaller lots from the wholesalers and selling in very small quantities to the consumers for personal use. The retailer is the last link in the chain of distribution. He establishes a link between wholesalers and consumers. There are different types of retailers small as well as large. Small scale retailers includes hawkers, pedlars, general shops, etc.

External Trade

External trade also called as Foreign trade. It refers to buying and selling between two or more countries. For instance, If Mr.X who is a trader from Mumbai, sells his goods to Mr.Y another trader from New York then this is an example of foreign trade.

External trade can be further sub-divided into three groups, viz.,

- **Export Trade**

When a trader from home country sells his goods to a trader located in another country, it is called export trade. For e.g. a trader from India sells his goods to a trader located in China.

- **Import Trade**

When a trader in home country obtains or purchase goods from a trader located in another country, it is called import trade. For e.g. a trader from India purchase goods from a trader located in China.

Domestic Trade

Domestic trade, also known as internal trade or home trade, is the exchange of domestic goods within the boundaries of a country. This may be sub-divided into two categories, wholesale and retail. Wholesale trade is concerned with buying goods from manufacturers or dealers or producers in large quantities and selling them in smaller quantities to others who may be retailers or even consumers. Wholesale trade is undertaken by wholesale merchants or wholesale commission agents.

Retail trade is concerned with the sale of goods in small quantities to consumers. This type of trade is taken care of by retailers. In actual practice, however, manufacturers and wholesalers may also undertake retail distribution of goods to bypass the intermediary retailer, by which they earn higher profits.

Importance and Role

The importance of domestic trade in a country is that it facilitates exchange of goods within the country. By doing this it also makes sure that factors of production reach to the right places so that the economy of the country can grow. By allowing all different types of goods and services to reach to all parts of the country it improves the standard of living of the residents of the country as well as the employment rate of the country. And it helps the growth of an industry by ensuring the availability of raw materials.

It even facilitates foreign trade. Traders from outside the country will have to come in contact with internal traders, because it's not easy to come directly into another country and get the required products.

Major Differences between Domestic Trade and International Trade

The following are the major differences between domestic trade and international trade:-

Mobility in Factor of Production

- **Domestic Trade**: Free to move around factors of production like land, labor, capital and labor capital and entrepreneurship from one state to another within the same country
- **International Trade**: Quite restricted

Movement of Goods

- **Domestic trade**: easier to move goods without many restrictions. Maybe need to pay sales tax,etc
- **International Trade**: Restricted due to complicated custom procedures and trade barriers like tariff, quotas or embargo

Usage of different currencies

- **Domestic trade:** same type of currency used
- **International trade:** different countries used different currencies

Broader markets

- **Domestic trade**: limited market due to limits in population, etc
- **International trade**: Broader markets

Language and Cultural Barriers

- **Domestic trade**: speak same language and practice same culture
- **International trade**: Communication challenges due to language and cultural barriers

Cultures

No two cultures are the same and understanding both the social and business culture in another country is the first key to success. Culture defines everything a society does, from its business practices, to its response to advertising and marketing, to negotiating sales. It is important to include research on the culture of the country(s) that you intend to sell to prior to entering their market. Understanding these, often sensitive, areas will mean that you are better prepared when first entering the market. Although the people that you will deal with will not expect you to be completely in tune with the culture, respect and politeness will go a long way.

Level of Competition

The level of competition you will experience in foreign markets is likely to be more dynamic and complex than you experience in domestic markets.

A good strategic tool to use to determine if you are able to compete in a particular international market is the Porters 5 Forces analysis. This tool will assess your supplier power, buyer power, threat of competitor products and the threat of new entrants to the market.

Market Intelligence

The key points to determine when gathering market intelligence on the market you intend to enter are:

- Understanding how the market works
- Who your direct competition is, and
- The best market entry strategy.

It may be difficult to find reliable information and data for some markets, particularly less-developed economies as their statistical agencies may not be as sophisticated as developed market economies. However it is important to gather as much information as you can to successful enter the market.

International Law

Countries determine their laws based on the needs of their citizens not the concerns of foreign companies. By and large, international law is a gentlemen's agreement which is honored, but not always. For example in areas such as intellectual property, although there are many agreements in place, protecting intellectual property can be time consuming and costly.

Technology

The degree of technology can vary substantially in foreign markets. If your product or service requires a high degree of technology sophistication to use or implement, then markets with low levels of technology will not be suitable for your business.

Logistics

Like technology, business infrastructure in foreign markets will be at different levels of development. This may well have an impact on your ability to get your products to that market. It is important to research your new target market and understand how goods are moved within the country before you commit to that market.

Media

Advertising your product and service will of course be an important component of your marketing strategy. It is important to be aware of the types of media available and the kind of media your target market uses to gain information about products and services they wish to buy. Not everyone is connected to the internet nor is every customer able to read and write. This does not mean those markets should be ignored. It does mean that how you advertise and market your products will require an examination of the most appropriate media for your target market. Gains from trade

In economics, gains from trade refer to net benefits to agents from allowing an increase in voluntary trading with each other. In technical terms, it is the increase of consumer surplus plus producer surplus from lower tariffs or otherwise liberalizing trade.

Dynamics

Gains from trade are commonly described as resulting from:

- Specialization in production from division of labor, economies of scale, scope, and agglomeration and relative availability of factor resources in types of output by farms, businesses, location and economies
- A resulting increase in total output possibilities
- Trade through markets from sale of one type of output for other, more highly valued goods.

Market incentives, such as reflected in prices of outputs and inputs, are theorized to attract factors of production, including labor, into activities according to comparative advantage, that is, for which they each have a low opportunity cost. The factor owners then use their increased income from such specialization to buy more-valued goods of which they would otherwise be high-cost producers, hence their gains from trade. The concept may be applied to an entire economy for the alternatives of autarky (no trade) or trade. A measure of total gains from trade is the sum of consumer surplus and producer profits or, more roughly, the increased output from specialization in production with resulting trade. Gains from trade may also refer to net benefits to a country from lowering barriers to trade such as tariffs on imports.

David Ricardo in 1817 first clearly stated and proved the principle of comparative advantage, termed a "fundamental analytical explanation" for the source of gains from trad But from publication of Adam Smith's The Wealth of Nationsin 1776, it was widely argued, that, with competition and absent market distortions, such gains are positive in moving toward free trade and away from autarky or prohibitively high import tariffs. Rigorous early contemporary statements of the conditions under which this proposition holds are found in Samuelson in 1939 and 1962. For the analytically tractable general case of Arrow-Debreu goods, formal proofs came in 1972 for determining the condition of no losers in moving from autarky toward free trade.

It does not follow that no tariffs are the best an economy could do. Rather, a large economy might be able to set taxes and subsidies to its benefit at the expense of other economies. Later results of Kemp and others showed that in an Arrow-Debreu world with a system of lump-sum compensatory mechanisms, corresponding to a customs union for a given subset set of countries, there is a common set of world' tariffs such that no country would be worse off than in the smaller customs union. The suggestion is that if a customs union has advantages for an economy, there is a worldwide customs union that is at least as good for each country in the world.

Measurement of gains from trade

Classical Economist there are two methods to measure the gains from trade:

- International trade increases national income which helps us to get low priced imports;
- Gains are measured in terms of trade. To measure the gains from the trade comparison of cost of production between domestic and foreign countries something is required. But it is very difficult to acquire the knowledge of cost of production and cost of imports in a domestic country. Therefore terms of trade method is preferable to measure the gains from trade.

Factors affecting gains from trade

There are several factors which determine the gains from international trade:

Differences in cost ratio:

The gains from international trade depends upon the cost ratios of differences in comparative cost ratios in the two trading countries. The smaller the difference between exchange rate and cost of production the smaller the gains from trade and vice versa.

Demand and supply:

If a country has elastic demand and supply gains the gains from trade are higher than if demand and supply are inelastic.

Factor availability:

International trade is based on the specialization and a country specializes depending upon the availability of factors of production. It will increase the domestic cost ratios and thereby the gains from trade.

Size of country:

If a country is small in size it is relatively easy for them to specialize in the production of one commodity and export the surplus production to a large country and can get more gains from international trade. Whereas if a country is large in size then they have to specialize in more than one good because the excess production of only one commodity cannot be exported fully to a small sized country as the demand for good will reduce very frequently. So the smaller the size of the country, the larger the gain from trade.

Terms of Trade:

Gains from trade will depend upon the terms of trade. If the cost ratio and terms of trade are closer to each other more will be the gains from trade of the participating countries.

Productive Efficiency:

An increase in the productive efficiency of a country also determines its gains from trade as it lowers the cost of production and price of the goods. As a result the country importing gains by importing cheap goods.

Static and dynamic gains from trade

The gains from trade can be classified into static and dynamic gains from trades. Static Gains means the increase in social welfare as a result of maximized national output due to optimum utilization of country's factor endowments or resources. Dynamic gains from trade, are those benefits which accelerates economic growth of the participating countries.

Static gains are the result of the operation of the theory of comparative cost in the field of foreign trade. On this principle countries make the optimum use of their available resources so that their national output is greater which also raises the level of social welfare in the country. When there is an introduction of foreign trade in the economy the result is called the static gains from trade.

Dynamic gains from trade relate to economic development of the economy. Specialization of the country for the production of best suited commodities which result in a large volume of quality production which promotes growth. Thus the extension of domestic market to foreign market will accelerate economic growth.

Terms of trade (TOT) refers to the relative price of exports in terms of imports and is defined as the ratio of export prices to import prices. It can be interpreted as the amount of import goods an economy can purchase per unit of export goods.

An improvement of a nation's terms of trade benefits that country in the sense that it can buy more imports for any given level of exports. The terms of trade may be influenced by the exchange rate because a rise in the value of a country's currency lowers the domestic prices of its imports but may not directly affect the prices of the commodities it exports.

Terms of trade (TOT)

History

The term (barter) terms of trade was first coined by the US American economist Frank William Tausig in his 1927 book International Trade. However, an earlier version of the concept can be traced back to the English economist Robert Torrens and his book The Budget: On Commercial and Colonial Policy, published in 1844, as well as to John Stuart Mill's essay Of the Laws of Interchange between Nations; and the Distribution of Gains of Commerce among the Countries of the Commercial World, published in the same year, though allegedly already written in 1829/30.

Definition

Terms of trade (TOT) is a measure of how much imports an economy can get for a unit of export goods. For example, if an economy is only exporting apples and only importing oranges, then the terms of trade are simply the price of apples over the price of oranges. In other words, how many oranges can you get for a unit of apples. Since economies typically export and import many goods, measuring the TOT requires defining price indices for exported and imported goods and comparing the two.

A rise in the prices of exported goods in international markets would increase the TOT, while a rise in the prices of imported goods would decrease it. For example, countries that export oil will see an increase in their TOT when oil prices go up, while the TOT of countries that import oil would decrease.

Two country model CIE economics

In the simplified case of two countries and two commodities, terms of trade is defined as the ratio of the total export revenue a country receives for its export commodity to the total import revenue it pays for its import commodity. In this case the imports of one country are the exports of the other country.

In basic Microeconomics, the terms of trade are usually set in the interval between the opportunity costs for the production of a given good of two countries.

Terms of trade is the ratio of a country's export price index to its import price index, multiplied by 100. The terms of trade measures the rate of exchange of one good or service for another when two countries trade with each other.

Multi-commodity multi-country model

In the more realistic case of many products exchanged between many countries, terms of trade can be calculated using a Laspeyres index. In this case, a nation's terms of trade is the ratio of the Laspeyre price index of exports to the Laspeyre price index of imports. The Laspeyre export index is the current value of the base period exports divided by the base period value of the base period exports. Similarly, the

Laspeyres import index is the current value of the base period imports divided by the base period value of the base period imports.

Limitations

Terms of trade should not be used as synonymous with social welfare, or even Pareto economic welfare. Terms of trade calculations do not tell us about the volume of the countries' exports, only relative changes between countries. To understand how a country's social utility changes, it is necessary to consider changes in the volume of trade, changes in productivity and resource allocation, and changes in capital flows.

The price of exports from a country can be heavily influenced by the value of its currency, which can in turn be heavily influenced by the interest rate in that country. If the value of currency of a particular country is increased due to an increase in interest rate one can expect the terms of trade to improve. However, this may not necessarily mean an improved standard of living for the country since an increase in the price of exports perceived by other nations will result in a lower volume of exports. As a result, exporters in the country may actually be struggling to sell their goods in the international market even though they are enjoying a (supposedly) high price.

In the real world of over 200 nations trading hundreds of thousands of products, terms of trade calculations can get very complex. Thus, the possibility of errors is significant.

Trends in global trade

1) Forced Dynamism:

International trade is forced to succumb to trends that shape the global political, cultural, and economic environment. International trade is a complex topic, because the environment it operates in is constantly changing. First, businesses are constantly pushing the frontiers of economic growth, technology, culture, and politics which also change the surrounding global society and global economic context. Secondly, factors external to international trade (e.g., developments in science and information technology) are constantly forcing international trade to change how they operate.

2) Cooperation among Countries:

Countries cooperate with each other in thousands of ways through international organisations, treaties, and consultations. Such cooperation generally encourages the globalization of business by eliminating restrictions on it and by outlining frameworks that reduce uncertainties about what companies will and will not be allowed to do. Countries cooperate:

i) To gain reciprocal advantages,

ii) To attack problems they cannot solve alone, and

iii) To deal with concerns that lie outside anyone’s territory.

Agreements on a variety of commercially related activities, such as transportation and trade, allow nations to gain reciprocal advantages. For example, groups of countries have agreed to allow foreign airlines to land in and fly over their territories, such as Canada's and Russia's agreements commencing in 2001 to allow polar over flights that will save five hours between New York and Hong Kong.

Groups of countries have also agreed to protect the property of foreign-owned companies and to permit foreign-made goods and services to enter their territories with fewer restrictions. In addition, countries cooperate on problems they cannot solve alone, such as by coordinating national economic programs (including interest rates) so that global economic conditions are minimally disrupted, and by restricting imports of certain products to protect endangered species.

Finally, countries set agreements on how to commercially exploit areas outside any of their territories. These include outer space (such as on the transmission of television programs), non-coastal areas of oceans and seas (such as on exploitation of minerals), and Antarctica (for example, limits on fishing within its coastal waters).

3) Liberalization of Cross-border Movements:

Every country restricts the movement across its borders of goods and services as well as of the resources, such as workers and capital, to produce them. Such restrictions make international trade cumbersome; further, because the restrictions may change at any time, the ability to sustain international trade is always uncertain. However, governments today impose fewer restrictions on cross-border movements than they did a decade or two ago, allowing companies to better take advantage of international opportunities. Governments have decreased restrictions because they believe that:

i) So-called open economies (having very few international restrictions) will give consumers better access to a greater variety of goods and services at lower prices

ii) Producers will become more efficient by competing against foreign companies, and

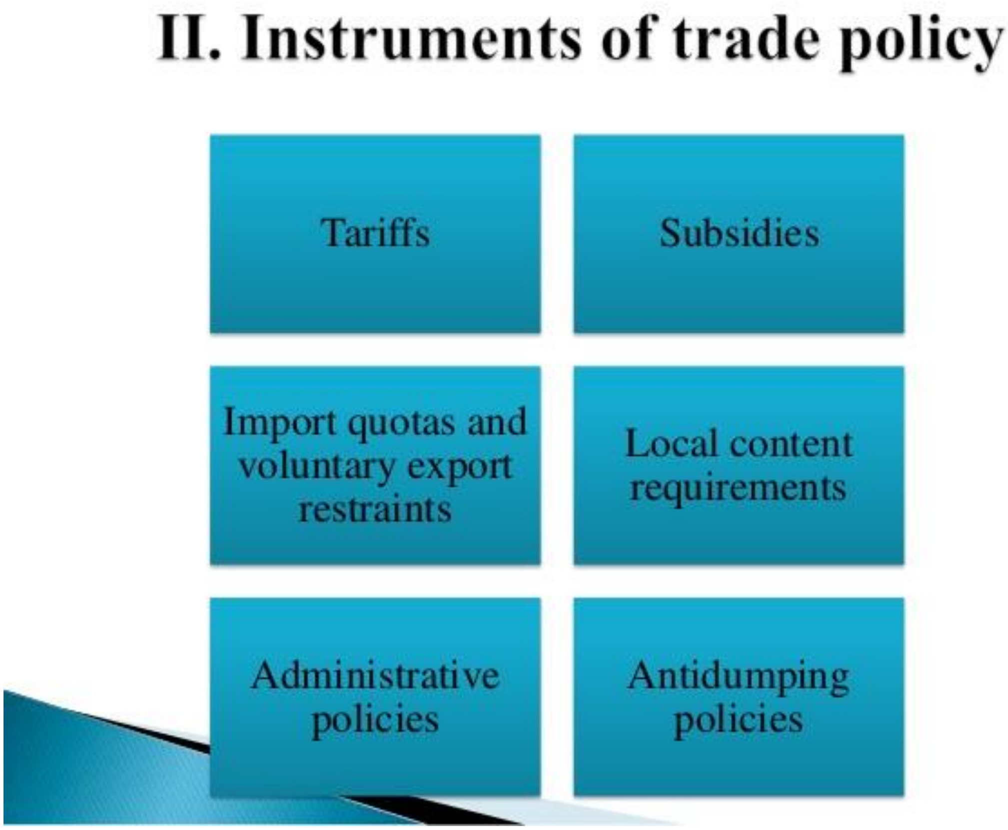
iii) If they reduce their own restrictions, other countries will do the same.

4) Transfer of Technology:

Technology transfer is the process by which commercial technology is disseminated. This will take the form of a technology transfer transaction, which may or may not be a legally binding contract, but which will involve the communication, by the transferor, of the relevant knowledge to the recipient. It also includes non-commercial technology transfers, such as those found in international cooperation agreements between developed and developing states. Such agreements may relate to infrastructure or agricultural development, or to international; cooperation in the fields of research, education, employment or transport.

5) Growth in Emerging Markets:

The growth of emerging markets (e.g., India, China, Brazil, and other parts of Asia and South America especially) has impacted international trade in every way. The emerging markets have simultaneously increased the potential size and worth of current major international trade while also facilitating the emergence of a whole new generation of innovative companies. According to “A special report on innovation in emerging markets” by The Economist magazine, “The emerging world, long a source of cheap la, now rivals the rich countries for business innovation”.



- **A tariff** is a tax levied on imports

There are two basic ways in which tariffs may be levied:

1. **Specific tariffs:**
   Are levied as a fixed charge for each unit of a good imported.
2. **Ad volorem Tariffs:**
   Are levied as a proportion of the value of the imported goods.

- A tariff raises the cost f imported products. In most causes, tariffs are put in place to protect domestic producers from foreign competition.

Ex: When goods are brought into the Netherlands from a country outside the European Union (EU), Customs charges tax on them. The amount of tax depends on the country of origin and the kind of product.

Subsidies

- A subsidy is a government payment to a domestic producer.
- Subsidies take many forms including cash grants, low-interest, tax breaks and government equity participation in domestic and government producers in two ways:

  1. They help producers compete against foreign imports and
  2. Subsidies help them gain export markets.

- The main gains from subsidies accrue to domestic producers, whose international competitiveness is increased as a result of them.

Import quotas

- An import quotas: Direct restriction on the quantity of some good that may be imported into a country.
- An import quotas: Limitations on the quantity of goods that can be imported into the country during a specified period of time.
- An import quota is typically set below the free trade level of imports - A binding quota.
- If a quota is set at or above the free trade level of imports – A non-binding quota.

Voluntary export restraints

- VER: quotas on trade imposed by the exporting country, typically at the request of the importing country's government.
- Typically VERs arise when the import-competing industries seek protection from a surge of imports from particular exporting countries.
- VERs are then offered by the exporter to appease the importing country and to avoid the effects of possible trade restraints on the part of the importer.
- Ex: one of the most famous examples is the limitation on auto exports to the United States enforced by Japanese automobile producer in 1981.

  Foreign producers agree to VERs because they fear for more damaging punitive tariffs or import quotas might follow if they do not.

Local content requirements

- **A local content requirement demands that some specific fraction of a good be produced domestically**
  - Physical terms (e.g., 75 percent of component parts for this product must be produced locally)
  - Value terms (e.g., 75 percent of this product must be produced locally)

Administrative policies

- **Bureaucratic rules designed to make it difficult for imports to enter a country.**

- In Japan, custom inspectors insisted on checking every tulip bulb by cutting it vertically down the middle =>Japanese 'masters' in imposing rules.

- France required all imported videotape recorders arrive through a small customs entry point => delayed Japanese VCRs

Balance of payments

The balance of payments (BOP) of a country is the record of all economic transactions between the residents of a country and the rest of the world in a particular period (over a quarter of a year or more commonly over a year). These transactions are made by individuals, firms and government bodies. Thus the balance of payments includes all external visible and non-visible transactions of a country during a given period, usually a year. It represents a summation of country's current demand and supply of the claims on foreign currencies and of foreign claims on its currency.

Balance of payments accounts are an accounting record of all monetary transactions between a country and the rest of the world. These transactions include payments for the country's exports and imports of goods, services, financial capital, and financial transfers. The BOP accounts summarize international transactions for a specific period, usually a year, and are prepared in a single currency, typically the domestic currency for the country concerned. Sources of funds for a nation, such as exports or the receipts of loans and investments, are recorded as positive or surplus items. Uses of funds, such as for imports or to invest in foreign countries, are recorded as negative or deficit items.

When all components of the BOP accounts are included they must sum to zero with no overall surplus or deficit. For example, if a country is importing more than it exports, its trade balance will be in deficit, but the shortfall will have to be counterbalanced in other ways – such as by funds earned from its foreign investments, by running down central bank reserves or by receiving loans from other countries.

While the overall BOP accounts will always balance when all types of payments are included, imbalances are possible on individual elements of the BOP, such as the current account, the capital account excluding the central bank's reserve account, or the sum of the two. Imbalances in the latter sum can result in surplus countries accumulating wealth, while deficit nations become increasingly indebted.

The term balance of payments often refers to this sum: a country's balance of payments is said to be in surplus (equivalently, the balance of payments is positive) by a specific amount if sources of funds (such as export goods sold and bonds sold) exceed uses of funds (such as paying for imported goods and paying for foreign bonds purchased) by that amount. There is said to be a balance of payments deficit (the balance of payments is said to be negative) if the former are less than the latter. A BOP surplus (or deficit) is accompanied by an accumulation (or dissimulation) of foreign exchange reserves by the central bank.

Under a fixed exchange rate system, the central bank accommodates those flows by buying up any net inflow of funds into the country or by providing foreign currency funds to the foreign exchange market to match any international outflow of funds, thus preventing the funds flows from affecting the exchange rate between the country's currency and other currencies.

Then the net change per year in the central bank's foreign exchange reserves is sometimes called the balance of payments surplus or deficit. Alternatives to a fixed exchange rate system include a managed float where some changes of exchange rates are allowed, or at the other extreme a purely floating exchange rate (also known as a purely flexible exchange rate). With a pure float the central bank does not intervene at all to protect or devalue its currency, allowing the rate to be set by the market, and the central bank's foreign exchange reserves do not change, and the balance of payments is always zero.

BALANCE OF TRADE

The commercial balance or net exports (sometimes symbolized as NX), is the difference between the monetary value of exports and imports of output in an economy over a certain period, measured in the currency of that economy. It is the relationship between a nation's imports and exports. A positive balance is known as a trade surplus if it consists of exporting more than is imported; a negative balance is referred to as a trade deficit or, informally, a trade gap. The balance of trade is sometimes divided into a goods and a services balance.

Definition

The balance of trade forms part of the current account, which includes other transactions such as income from the net international investment position as well as international aid. If the current account is in surplus, the country's net international asset position increases correspondingly. Equally, a deficit decreases the net international asset position.

The trade balance is identical to the difference between a country's output and its domestic demand (the difference between what goods a country produces and how many goods it buys from abroad; this does not include money re-spent on foreign stock, nor does it factor in the concept of importing goods to produce for the domestic market).

Measuring the balance of trade can be problematic because of problems with recording and collecting data. As an illustration of this problem, when official data for all the world's countries are added up, exports exceed imports by almost 1%; it appears the world is running a positive balance of trade with itself. This cannot be true, because all transactions involve an equal credit or debit in the account of each nation. The discrepancy is widely believed to be explained by transactions intended to launder money or evade taxes, smuggling and other visibility problems. However, especially for developed countries, accuracy is likely.

Factors that can affect the balance of trade include:

- The cost of production (land, labor, capital, taxes, incentives, etc.) in the exporting economy vis-à-vis those in the importing economy;
- The cost and availability of raw materials, intermediate goods and other inputs;
- Exchange rate movements;
- Multilateral, bilateral and unilateral taxes or restrictions on trade;
- Non-tariff barriers such as environmental, health or safety standards;
- The availability of adequate foreign exchange with which to pay for imports; and
- Prices of goods manufactured at home (influenced by the responsiveness of supply)

In addition, the trade balance is likely to differ across the business cycle. In export-led growth (such as oil and early industrial goods), the balance of trade will improve during an economic expansion. However, with domestic demand led growth (as in the United States and Australia) the trade balance will worsen at the same stage in the business cycle.

Monetary balance of trade is different from physical balance of trade (which is expressed in amount of raw materials, known also as Total Material Consumption). Developed countries usually import a lot of raw materials from developing countries. Typically, these imported materials are transformed into finished products, and might be exported after adding value. Financial trade balance statistics conceal material flow. Most developed countries have a large physical trade deficit, because they have a large ecological footprint.

Civil society organizations point out the predatory nature of this imbalance, and campaign for ecological debt repayment.

Since the mid-1980s, the United States has had a growing deficit in tradable goods, especially with Asian nations (China and Japan) which now hold large sums of U.S debt that has funded the consumption. The U.S. has a trade surplus with nations such as Australia. The issue of trade deficits can be complex. Trade deficits generated in tradable goods such as manufactured goods or software may impact domestic employment to different degrees than trade deficits in raw materials.

Economies such as Japan and Germany which have savings surpluses, typically run trade surpluses. China, a high-growth economy, has tended to run trade surpluses. A higher savings rate generally corresponds to a trade surplus. Correspondingly, the U.S. with its lower savings rate has tended to run high trade deficits, especially with Asian nations.

Components

The current account shows the net amount a country is earning if it is in surplus, or spending if it is in deficit. It is the sum of the balance of trade (net earnings on exports minus payments for imports), factor income (earnings on foreign investments minus payments made to foreign investors) and cash transfers. It is called the current account as it covers transactions in the "here and now" – those that don't give rise to future claims.

The Capital Account records the net change in ownership of foreign assets. It includes the reserve account (the foreign exchange market operations of a nation's central bank), along with loans and investments between the country and the rest of world (but not the future regular repayments/dividends that the loans and investments yield; those are earnings and will be recorded in the current account). The term "capital account" is also used in the narrower sense that excludes central bank foreign exchange market operations: Sometimes the reserve account is classified as "below the line" and so not reported as part of the capital account.

Expressed with the broader meaning for the capital account, the BOP identity states that any current account surplus will be balanced by a capital account deficit of equal size – or alternatively a current account deficit will be balanced by a corresponding capital account surplus:

Current account + broadly defined capital account + Balancing item = 0

The balancing item, which may be positive or negative, is simply an amount that accounts for any statistical errors and assures that the current and capital accounts sum to zero. By the principles of double entry accounting, an entry in the current account gives rise to an entry in the capital account, and in aggregate the two accounts automatically balance.

A balance isn't always reflected in reported figures for the current and capital accounts, which might, for example, report a surplus for both accounts, but when this happens it always means something has been missed – most commonly, the operations of the country's central bank – and what has been missed is recorded in the statistical discrepancy term (the balancing item).

An actual balance sheet will typically have numerous sub headings under the principal divisions. For example, entries under Current account might include:

Trade – buying and selling of goods and services

Exports – a credit entry

Imports – a debit entry

Trade balance – the sum of Exports and Imports

Factor income – repayments and dividends from loans and investments

Factor earnings – a credit entry

Factor payments – a debit entry

Factor income balance – the sum of earnings and payments.

Especially in older balance sheets, a common division was between visible and invisible entries. Visible trade recorded imports and exports of physical goods (entries for trade in physical goods excluding services is now often called the merchandise balance). Invisible trade would record international buying and selling of services, and sometimes would be grouped with transfer and factor income as invisible earnings.

The term "balance of payments surplus" (or deficit – a deficit is simply a negative surplus) refers to the sum of the surpluses in the current account and the narrowly defined capital account (excluding changes in central bank reserves). Denoting the balance of payments surplus as BOP surplus, the relevant identity is

BOP surplus = Current account surplus + narrowly defined capital account surplus

Variations in the use of term "balance of payments"

Economics writer J. Orlin Grabbe warns the term balance of payments can be a source of misunderstanding due to divergent expectations about what the term denotes. Grabbe says the term is sometimes misused by people who aren't aware of the accepted meaning, not only in general conversation but in financial publications and the economic literature.

A common source of confusion arises from whether or not the reserve account entry, part of the capital account, is included in the BOP accounts. The reserve account records the activity of the nation's central bank. If it is excluded, the BOP can be in surplus (which implies the central bank is building up foreign exchange reserves) or in deficit (which implies the central bank is running down its reserves or borrowing from abroad).

The term "balance of payments" is sometimes misused by non-economists to mean just relatively narrow parts of the BOP such as the trade deficit, which means excluding parts of the current account and the entire capital account.

Another cause of confusion is the different naming conventions in use. Before 1973 there was no standard way to break down the BOP sheet, with the separation into invisible and visible payments sometimes being the principal divisions. The IMF has their own standards for BOP accounting which is equivalent to the standard definition but uses different nomenclature, in particular with respect to the meaning given to the term capital account.

The IMF definition of Balance of Payment

The International Monetary Fund (IMF) use a particular set of definitions for the BOP accounts, which is also used by the Organisation for Economic Co-operation and Development (OECD), and the United Nations System of National Accounts (SNA).

The main difference in the IMF's terminology is that it uses the term "financial account" to capture transactions that would under alternative definitions be recorded in the capital account. The IMF uses the term capital account to designate a subset of transactions that, according to other usage, form a small part of the overall capital account. The IMF separates these transactions out to form an additional top level division of the BOP accounts. Expressed with the IMF definition, the BOP identity can be written:

Current account + financial account + capital account + balancing item = 0

The IMF uses the term current account with the same meaning as that used by other organizations, although it has its own names for its three leading sub-divisions, which are:

- The goods and services account (the overall trade balance)
- The primary income account (factor income such as from loans and investments)
- The secondary income account (transfer payments)

Imbalances

While the BOP has to balance overall, surpluses or deficits on its individual elements can lead to imbalances between countries. In general there is concern over deficits in the current account. Countries with deficits in their current accounts will build up increasing debt and/or see increased foreign ownership of their assets. The types of deficits that typically raise concern are

- A visible trade deficit where a nation is importing more physical goods than it exports (even if this is balanced by the other components of the current account.)
- An overall current account deficit.

- A basic deficit which is the current account plus foreign direct investment (but excluding other elements of the capital account like short terms loans and the reserve account.)

As discussed in the history section below, the Washington Consensus period saw a swing of opinion towards the view that there is no need to worry about imbalances. Opinion swung back in the opposite direction in the wake of financial crisis of 2007–2009. Mainstream opinion expressed by the leading financial press and economists, international bodies like the IMF – as well as leaders of surplus and deficit countries – has returned to the view that large current account imbalances do matter. Some economists do, however, remain relatively unconcerned about imbalances and there have been assertions, such as by Michael P. Dooley, David Folkerts-Landau and Peter Garber, that nations need to avoid temptation to switch to protectionism as a means to correct imbalances.

Causes of BOP imbalances

There are conflicting views as to the primary cause of BOP imbalances, with much attention on the US which currently has by far the biggest deficit. The conventional view is that current account factors are the primary cause – these include the exchange rate, the government's fiscal deficit, business competitiveness, and private behaviour such as the willingness of consumers to go into debt to finance extra consumption. An alternative view, argued at length in a 2005 paper by Ben Bernanke, is that the primary driver is the capital account, where a global savings glut caused by savers in surplus countries, runs ahead of the available investment opportunities, and is pushed into the US resulting in excess consumption and asset price inflation.

Reserve asset

The US dollar has been the leading reserve asset since the end of the gold standard. In the context of BOP and international monetary systems, the reserve asset is the currency or other store of value that is primarily used by nations for their foreign reserves. BOP imbalances tend to manifest as hoards of the reserve asset being amassed by surplus countries, with deficit countries building debts denominated in the reserve asset or at least depleting their supply. Under a gold standard, the reserve asset for all members of the standard is gold. In the Bretton Woods system, either gold or the U.S. dollar could serve as the reserve asset, though its smooth operation depended on countries apart from the US choosing to keep most of their holdings in dollars.

Following the ending of Bretton Woods, there has been no de jure reserve asset, but the US dollar has remained by far the principal de facto reserve. Global reserves rose sharply in the first decade of the 21st century, partly as a result of the 1997 Asian Financial Crisis, where several nations ran out of foreign currency needed for essential imports and thus had to accept deals on unfavourable terms.

The International Monetary Fund (IMF) estimates that between 2000 to mid-2009, official reserves rose from $1,900bn to $6,800bn. Global reserves had peaked at about $7,500bn in mid-2008, then declined by about $430bn as countries without their own reserve currency used them to shield themselves from the worst effects of the financial crisis. From Feb 2009 global reserves began increasing again to reach close to $9,200bn by the end of 2010.

While the current central role of the dollar does give the US some advantages, such as lower cost of borrowings, it also contributes to the pressure causing the U.S. to run a current account deficit, due to the Triffin dilemma. In a November 2009 article published in Foreign Affairs magazine, economist C. Fred Bergsten argued that Dr Zhou's suggestion or a similar change to the international monetary system would be in the United States' best interests as well as the rest of the world's. Since 2009 there has been a notable increase in the number of new bilateral agreements which enable international trades to be transacted using a currency that isn't a traditional reserve asset, such as the renminbi, as the Settlement currency.

Balance of payments crisis

A BOP crisis, also called a currency crisis, occurs when a nation is unable to pay for essential imports and/or service its debt repayments. Typically, this is accompanied by a rapid decline in the value of the affected nation's currency. Crises are generally preceded by large capital inflows, which are associated at first with rapid economic growth. However a point is reached where overseas investors become concerned about the level of debt their inbound capital is generating, and decide to pull out their funds.

The resulting outbound capital flows are associated with a rapid drop in the value of the affected nation's currency. This causes issues for firms of the affected nation who have received the inbound investments and loans, as the revenue of those firms is typically mostly derived domestically but their debts are often denominated in a reserve currency. Once the nation's government has exhausted its foreign reserves trying to support the value of the domestic currency, its policy options are very limited. It can raise its interest rates to try to prevent further declines in the value of its currency, but while this can help those with debts denominated in foreign currencies, it generally further depresses the local economy.

Balancing mechanisms

One of the three fundamental functions of an international monetary system is to provide mechanisms to correct imbalances.

Broadly speaking, there are three possible methods to correct BOP imbalances, though in practice a mixture including some degree of at least the first two methods tends to be used. These methods are adjustments of exchange rates; adjustment of a nations internal prices along with its levels of demand; and rules based adjustment. Improving productivity and hence competitiveness can also help, as can increasing the desirability of exports through other means, though it is generally assumed a nation is always trying to develop and sell its products to the best of its abilities.

Rebalancing by changing the exchange rate

An upwards shift in the value of a nation's currency relative to others will make a nation's exports less competitive and make imports cheaper and so will tend to correct a current account surplus. It also tends to make investment flows into the capital account less attractive so will help with a surplus there too. Conversely a downward shift in the value of a nation's currency makes it more expensive for its citizens to buy imports and increases the competitiveness of their exports, thus helping to correct a deficit (though the solution often doesn't have a positive impact immediately due to the Marshall–Lerner condition).

Exchange rates can be adjusted by government in a rules based or managed currency regime, and when left to float freely in the market they also tend to change in the direction that will restore balance. When a country is selling more than it imports, the demand for its currency will tend to increase as other countries ultimately need the selling country's currency to make payments for the exports.

The extra demand tends to cause a rise of the currency's price relative to others. When a country is importing more than it exports, the supply of its own currency on the international market tends to increase as it tries to exchange it for foreign currency to pay for its imports, and this extra supply tends to cause the price to fall. BOP effects are not the only market influence on exchange rates however, they are also influenced by differences in national interest rates and by speculation.

Rebalancing by adjusting internal prices and demand

When exchange rates are fixed by a rigid gold standard, or when imbalances exist between members of a currency union such as the Eurozone, the standard approach to correct imbalances is by making changes to the domestic economy. To a large degree, the change is optional for the surplus country, but compulsory for the deficit country. In the case of a gold standard, the mechanism is largely automatic. When a country has a favourable trade balance, as a consequence of selling more than it buys it will experience a net inflow of gold.

The natural effect of this will be to increase the money supply, which leads to inflation and an increase in prices, which then tends to make its goods less competitive and so will decrease its trade surplus. However the nation has the option of taking the gold out of economy thus building up a hoard of gold and retaining its favorable balance of payments.

On the other hand, if a country has an adverse BOP it will experience a net loss of gold, which will automatically have a deflationary effect, unless it chooses to leave the gold standard. Prices will be reduced, making its exports more competitive, and thus correcting the imbalance. While the gold standard is generally considered to have been successful up until 1914, correction by deflation to the degree required by the large imbalances that arose after WWI proved painful, with deflationary policies contributing to prolonged unemployment but not re-establishing balance. Apart from the US most former members had left the gold standard by the mid-1930s.

A possible method for surplus countries such as Germany to contribute to re-balancing efforts when exchange rate adjustment is not suitable, is to increase its level of internal demand (i.e. its spending on goods). While a current account surplus is commonly understood as the excess of earnings over spending, an alternative expression is that it is the excess of savings over investment. That is:

CA = NS - NI,

Where,

CA = current account,

NS = national savings (private plus government sector),

NI = national investment.

If a nation is earning more than it spends the net effect will be to build up savings, except to the extent that those savings are being used for investment. If consumers can be encouraged to spend more instead of saving; or if the government runs a fiscal deficit to offset private savings; or if the corporate sector divert more of their profits to investment, then any current account surplus will tend to be reduced.

However in 2009 Germany amended its constitution to prohibit running a deficit greater than 0.35% of its GDP and calls to reduce its surplus by increasing demand have not been welcome by officials, adding to fears that the 2010s will not be an easy decade for the euro zone. In their April 2010 world economic outlook report, the IMF presented a study showing how with the right choice of policy options governments can transition out of a sustained current account surplus with no negative effect on growth and with a positive impact on unemployment.

Rules based rebalancing mechanisms

Nations can agree to fix their exchange rates against each other, and then correct any imbalances that arise by rules based and negotiated exchange rate changes and other methods. The Bretton Woods system of fixed but adjustable exchange rates was an example of a rules based system. John Maynard Keynes, one of the architects of the Bretton Woods system had wanted additional rules to encourage surplus countries to share the burden of rebalancing, as he argued that they were in a stronger position to do so and as he regarded their surpluses as negative externalities imposed on the global economy.

Keynes suggested that traditional balancing mechanisms should be supplemented by the threat of confiscation of a portion of excess revenue if the surplus country did not choose to spend it on additional imports. However his ideas were not accepted by the Americans at the time. In 2008 and 2009, American economist Paul Davidson had been promoting his revamped form of Keynes's plan as a possible solution to global imbalances which in his opinion would expand growth all rounds without the downside risk of other rebalancing methods.

Historical roots of today's international trade:

Origin:

International trade has a rich history starting with barter system being replaced by Mercantilism in the 16th and 17th Centuries. The 18th Century saw the shift towards liberalism. It was in this period that Adam Smith, the father of Economics wrote the famous book 'The Wealth of Nations' in 1776 where in he defined the importance of specialization in production and brought International trade under the said scope. David Ricardo developed the Comparative advantage principle, which stands true even today.

All these economic thoughts and principles have influenced the international trade policies of each country. Though in the last few centuries, countries have entered into several pacts to move towards free trade where the countries do not impose tariffs in terms of import duties and allow trading of goods and services to go on freely.

Composition:

The 19th century beginning saw the move towards professionalism, which petered down by end of the century. Around 1913, the countries in the west say extensive move towards economic liberty where in quantitative restrictions were done away with and customs duties were reduced across countries. All currencies were freely convertible into Gold, which was the international monetary currency of exchange. Establishing business anywhere and finding employment was easy and one can say that trade was really free between countries around this period.

The First World War changed the entire course of the world trade and countries built walls around themselves with wartime controls. Post world war, as many as five years went into dismantling of the wartime measures and getting back trade to normalcy. But then the economic recession in 1920 changed the balance of world trade again and many countries saw change of fortunes due to fluctuation of their currencies and depreciation creating economic pressures on various Governments to adopt protective mechanisms by adopting to raise customs duties and tariffs.

The need to reduce the pressures of economic conditions and ease international trade between countries gave rise to the World Economic Conference in May 1927 organized by League of Nations where in the most important industrial countries participated and led to drawing up of Multilateral Trade Agreement. This was later followed with General Agreement of Tariffs and Trade (GATT) in 1947.

However once again depression struck in 1930s disrupting the economies in all countries leading to rise in import duties to be able to maintain favorable balance of payments and import quotas or quantity restrictions including import prohibitions and licensing.

Slowly the countries began to grow familiar to the fact that the old school of thoughts were no longer going to be practical and that they had to keep reviewing their international trade policies on continuous basis and this interns lead to all countries agreeing to be guided by the international organizations and trade agreements in terms of international trade.

Today the understanding of international trade and the factors influencing global trade is much better understood. The context of global markets have been guided by the understanding and theories developed by economists based on Natural resources available with various countries which give them the comparative advantage, Economies of Scale of large scale production, technology in terms of e commerce as well as product life cycle changes in tune with advancement of technology as well as the financial market structures.

What Is Invisible Trade?

An invisible trade is an international transaction that does not include an exchange of tangible goods. Customer service outsourcing, overseas banking transactions, and the medical tourism industry all are examples of invisible trade. In fact, any transaction that is associated with a value but not with physical goods could be called an invisible trade.

In modern times, any accounting of a nation's balance of trade must include a calculation of its invisible trade. This is often referred to as the invisible balance.

Features

- Invisible trade, or the exchange of non-tangible goods, represents an increasing percentage of the world's business.
- Global financial services and insurance companies, shipping services, and tourism all engage in invisible trade.
- Medical tourism is one of the modern businesses that has emerged in invisible trade.
- The concept of invisible trade is used to define business activities that involve monetary exchange but not an exchange of physical goods. The purchase of an insurance policy by a firm in one country from a company in another country is such a transaction.
- It also describes a bank's income from its overseas branch offices, income from foreign investments, shipping services, tourism revenues, and consultant fees from international contracts.
- **Examples of Invisible Trade**
- Education is a form of invisible trade. Students might travel to other nations to gain access to learning at institutions that are renowned for their expertise in particular academic fields. Once they graduate, they might stay on or go home. If they go home, they will transfer their knowledge and expertise across borders in another intangible exchange.

- Patients in need of specialized medical procedures, higher quality healthcare, or lower-cost services now often travel to other countries to get them. Medical tourism has become a significant factor in invisible trade.

What Are Capital Flows?

Capital flows refer to the movement of money for the purpose of investment, trade or business production, including the flow of capital within corporations in the form of investment capital, capital spending on operations and research and development (R&D).

In emerging economies, capital flows can be particularly volatile as the economy may experience periods of rapid growth and subsequent contraction. Increased capital inflows can lead to credit booms and the inflation of asset prices, which may be offset by losses due to depreciation of the currency based on exchange rates and declines in equity pricing.

External Debt

Definition: It refers to money borrowed from a source outside the country. External debt has to be paid back in the currency in which it is borrowed.

Description: External debt can be obtained from foreign commercial banks, international financial institutions like IMF, World Bank, ADB etc and from the government of foreign nations.

How External Debt Is Used by the Borrower

Sometimes referred to as foreign debt, corporations, as well as governments, can procure external debt. In many instances, external debt takes the form of a tied loan, which means the funds secured through the financing through must be spent back into the nation that is providing the financing. For instance, the loan might allow one nation to buy resources it needs from the country that provided the loan.

External debt, particularly tied loans, might be set for specific purposes that are defined by the borrower and lender. Such financial aid could be used to address humanitarian or disaster needs. For example, if a nation faces severe famine and cannot secure emergency food through its own resources, it might use external debt to procure food from the nation it received the tied loan from. If a country needs to build up its energy infrastructure, it might leverage external debt as part of an agreement to buy resources such as the material to construct power plants in underserved areas.

Important Questions:

Part-B (5×2=10 Marks)

1. What do you mean by International trade?
2. List out the theories for International trade
3. What do you mean by trade invisibles?
4. Write a short note on external debt.

5. Define balance of payment.
6. What are all the distributional issues in international trade?

Part C (3×8=24Marks)

1. Explain the economic theories on international trade.
2. Enumerate the basis for international trade.
3. List out the Advantages and Disadvantages of International trade
4. Explain the recent trends in international trade.
5. Write a short note on balance of payment and explain in detail.
6. Compare the historical and todays international trade.
7. Define capital flows and explain foreign exchange revenues
8. Explain in detail David recado’s comparative advantage theory.
9. Criticize the concept of Bertil Ohlin theory for international trade.
10. Explain origin and destination of global exports and imports of international trade.

International trade Policy and Strategy (17BAU602B)

Unit I - MCQ

SI. NO	Question	Option 1	Option 2	Option 3	Option 4	Option 5	Option 6	Answer
1	The Director General of Foreign trade is appointed by…………………	Central Government	State Government	Ministry of commerce	Chief justice of the Supreme Court			Ministry of commerce
2	The incentive available under Focus Market Scheme (FMS) is………………..	1.5 to 2 per cent	2 to 2.5 per cent	2.5 to 3 per cent	3 TO 3.5 per cent			2.5 to 3 per cent
3	To double India's percentage share of global merchandise trade is the objective of…………………	1992-97 policy	1997-02 policy	2002-07 policy	2009-14 policy			2009-14 policy
4	The foreign Trade (Regulation) Rules was passed in the year……………………	1991	1992	1993	1994			1993
5	The apex body of the Foreign Trade is………………	Central Government	State Government	Ministry of commerce	WTO			Ministry of commerce

6	The tenure of the Foreign Trade policy is……………….	3 years	5 years	1 year	7 years			5 years
7	How many chapters are there in The Foreign Trade (Development and Regulation) Act, 1992?	5	4	6	7			6
8	The legal settlement of international trade disputes is………………	Negotiation	Arbitration	Litigation	Conciliation			Litigation
9	The WTO Agreement related to investment measures is…………….…	TRIPS	TRIMS	GATT	TCA			TRIMS
10	In international business cheaper alternatives to litigation is/ are………………	Conciliation	Arbitration	Negotiations	Conciliation and arbitration			Arbitration
11	TRIMs stands for……………….	Trade Related Investment Measures	Trade Review Information Modules	Tripartite Review of Investment Means	Trade Related Intellectual Measures			Trade Related Investment Measures

12	Development in international law is process. What does this process promote?	Mainly human development	Mainly economic development	Mainly social development	Mainly political development			Mainly economic development
13	Why is sustainable development a principle of paramount importance in international law?	Because it promotes world peace	Because it is a principle which did not exist before	Because it is a principle recognised by the International Court of Justice as well as bumber of leading international organisations	Because non-governmental organisations support this principle			Because it is a principle recognised by the International Court of Justice as well as bumber of leading international organisations
14	Trade in services includes which of the following?	textiles	Computer hardware	Weapons	Insurance			Insurance
15	Which of the following is international trade…………….	Trade between provinces	Trade between countries	Trade between regions	Trade between states			Trade between countries
16	Which is NOT an advantage of international trade……………..	Export of surplus production	Import of defence material	Dependence on foreign countries	Availability of cheap raw materials			Dependence on foreign countries
17	If Japan and Pakistan start free trade, difference in wages in two	Increase	Decrease	No effect	Double			Decrease

	countries will……… ……….							
18	Trade between two countries can be useful if cost ratios of goods are………… ….	Equal	Different	Undetermined	Decreasing			Different
19	Foreign trade creates among countries… ……….	Conflicts	Cooperation	Hatred	Trade Increase			Cooperation
20	A tariff……… ……….	Increases the volume of trade	Reduces the volume of trade	Has no effect on volume of trade	help weak countries			Reduces the volume of trade
21	A tariff is………… ……	A restriction on the number of export firms	Limit on the amount of imported goods	Tax and imports	Increases the volume of trade			Tax and imports
22	All are advantages of foreign trade EXCEPT… …………..	People get foreign exchange	Nations compete	Cheaper goods	Optimum utilisation of country's resources			People get foreign exchange
23	Terms of trade of developing countries are generally unfavourable	They export primary goods	They import value added goods	They export few goods	(a) and (b) of above			(a) and (b) of above

	because…… ………							
24	Term of trade of a country show……… ….	Ratio of goods exported and imported	Ratio of import duties	Ratio of prices of exports and imports	(a) and (c) of above			Ratio of prices of exports and imports
25	In a free trade world in which no restrictions exist, international trade will lead to…………	Reduced real living standard	Decreased efficiency	Increased efficiency	Reduced real GDP			Increased efficiency
26	What would encourage trade between two countries… ………….	Different tax system	Frontier checks	National currencies	Reduced tariffs			Reduced tariffs
27	"Terms of trade" between two countries refer to a ratio of………….	Export prices to import prices	Currency values	Exports to imports	Balance of trade to balance of payments			Export prices to import prices
28	Terms of trade of a country…… …………	Mean the trade agreement between trading countries	Is another name of exchange ratio of two currencies	Show the ratio between total export earnings and import bill of a country	Are determined by the price index of export and import goods			Are determined by the price index of export and import goods

29	This is an advantage of foreign trade……….	We can preserve our natural resources	New technology comes to the country	People need not go abroad	We can get foreign currencies			New technology comes to the country
30	This is NOT an advantage of foreign trade…………….	We can get gold from abroad	New technology comes to the country	We can import goods which are in short supply in India	We can made best use of natural resources			We can get gold from abroad
31	How many countries are members of the Eurozone in 2011?	20	17	16	25			17
32	India is part of…………….	European Union	NAFTA	SAARC	CER			SAARC
33	Which of the following treaties marked the establishment of the European Union?	Maastricht Treaty	Treaty of Lisbon	Berlin Treaty	Treaty of London			Maastricht Treaty
34	The European Commission is headquartered in………………	London	Geneva	Paris	Brussels			Brussels
35	Which of the following is not a member of SAARC?	Afghanistan	Nepal	Mauritius	the Maldives			Mauritius

36	SAARC is headquartered in…………….	New Delhi	Kathmandu	Islamabad	Colombo			Kathmandu
37	NAFTA is an example of a(n)……………….	FTA	customs union	common market	economic union			FTA
38	The Multi-Fibre Arrangement was an agreement in the area of……………	coffee	textiles	Petroleum	bananas			textiles
39	Which of the following is not a founding member of the OPEC?	Venezuela	Brazil	Kuwait	Iran			Brazil
40	CARICOM was established under which of the following treaties?	Coal and Steel Treaty	Treaty of Venice	Treaty of Chaguaramas	Treaty of Rome			Treaty of Chaguaramas
41	MERCOSUR originated as free-trade pact between…………….	Brazil and Argentina	Brazil and Venezuela	Argentina and Chile	Uruguay and Peru			Brazil and Argentina
42	Which of the following is a trade agreement between countries of the developed and	NAFTA	MERCOSUR	LAFTA	ALADI			NAFTA

	developing world?							
43	The European Parliament meets at……………	Rome	Vienna	Berlin	Strasbourg			Strasbourg
44	The genesis of the European Union is in the……………	Treaty of Maastricht	Coal and Steel Treaty	Treaty of Rome	Schengen Agreement			Coal and Steel Treaty
45	The ANDEAN Pact is a(n)………………	common market	customs union	FTA	political union			customs union
46	Regional economic integration presents potentially significant threats to business outside the area, including…………….	long-term improvements in the competitive positions of firms inside the areas.	the end of a “fortress” mentality means other firms outside the area will be able to enter the areas more easily to compete with existing area firms	the end to efforts to rationalize production and reduce costs	the imposition of US standards, recognized as a pioneer in regional economic integration, which means US firms will not be able to get around the legal barriers			the end to efforts to rationalize production and reduce costs

47	Regional economic integration, for example, the EU, offers significant opportunities to US businesses including………………	non-EU companies no longer need to set up subsidiaries in EU countries	companies can realize significant cost economies by centralizing operations where factor costs and skills are optimal	it makes no difference where in the EU one locates an operation since the costs are the same throughout	cultural differences and national consumer preferences are now irrelevant			companies can realize significant cost economies by centralizing operations where factor costs and skills are optimal
48	In a(n)……………..similarities in the underlying structure of economic activity make it feasible to adopt a single currency and use a single exchange rate as an instrument of macroeconomic policy	optimal currency zone	free trade area	customs union	common market			optimal currency zone
49	Which institution is responsible for proposing EU legislation, implementing it, and monitoring compliance?	The European Council	The European Parliament	The Court of Justice	The European Commission			The European Commission

50	One of the main impediments to regional economic integration is the cost that individuals must bear even while the country as a whole might gain. The second major impediment is the…………………..	increased concern about monetary policy	loss of national sovereignty	loosening of control over fiscal issues	the increased costs of defending and monitoring borders			loss of national sovereignty
51	The North American Free Trade Agreement is an example of……………	western economic integration	regional economic integration	eastern economic integration	global economic integration			regional economic integration
52	An agreement between countries in a geographic region to reduce tariff and nontariffbarriers to the free flow of goods, services, and factors of production between each other isreferred to as…………	regional economic integration	cross-cultural economic integration	geographic economic-political integration	cross-cultural economic-political integration			regional economic integration

	……….							
53	By 2008, ……….. WTO members had notified the organization of participation in oneor more regional trade agreements.	one-third of	one half of	two-thirds of	almost all			almost all
54	Nowhere has the movement toward regional economic integration been more successfulthan in………….	Africa	South America	Asia	Europe			Europe
55	Which three countries implemented NAFTA?	Panama, Mexico, and the United States	Canada, Brazil, and the United States	United States, Argentina, and Mexico	Canada, Mexico, and the United States			Canada, Mexico, and the United States
56	NAFTA stands for………….	North Asian Free Trade Agreement	North African Free Trade Association	North Atlantic Free Trade Agreement	North American Free Trade Association			North American Free Trade Association

57	Which countries are members of the free trade area known as MERCOSUR?	Chile, Mexico, Columbia, and Paraguay	Argentina, Brazil, Paraguay, and Uruguay	Chile, Brazil, Uruguay, and Columbia	Mexico, Columbia, Paraguay, and Uruguay			Argentina, Brazil, Paraguay, and Uruguay
58	A country that does not trade with other countries is called………	Developed economy	Closed economy	Independent economy	Isolated economy			Closed economy
59	Policy of Protection in trade…………….	Facilitates trade	Protects foreign producers	Protects local producers	Protects exporters			Protects local producers
60	Which of the following is a Latin American regional institution?	SAARC	MERCOSUR	APEC	ASEAN			MERCOSUR

KARPAGAM ACADEMY OF HIGHER EDUCATION

DEPARTMENT OF MANAGEMENT (UG)

III BBA 92017-2020 BATCH)

INTERNATIONAL TRADE POLICY AND STRATEGY (17BAU602B)

UNIT-II -Syllabus

The Global Institutional Structure - GATT (General Agreement on Trade and Tariffs) - WTO (World Trade Organization) - Regional Trade Blocks and Trade Agreements.

Balance of payments

The balance of payments (BOP) of a country is the record of all economic transactions between the residents of a country and the rest of the world in a particular period (over a quarter of a year or more commonly over a year). These transactions are made by individuals, firms and government bodies. Thus the balance of payments includes all external visible and non-visible transactions of a country during a given period, usually a year. It represents a summation of country's current demand and supply of the claims on foreign currencies and of foreign claims on its currency.

Balance of payments accounts are an accounting record of all monetary transactions between a country and the rest of the world. These transactions include payments for the country's exports and imports of goods, services, financial capital, and financial transfers. The BOP accounts summarize international transactions for a specific period, usually a year, and are prepared in a single currency, typically the domestic currency for the country concerned. Sources of funds for a nation, such as exports or the receipts of loans and investments, are recorded as positive or surplus items. Uses of funds, such as for imports or to invest in foreign countries, are recorded as negative or deficit items.

When all components of the BOP accounts are included they must sum to zero with no overall surplus or deficit. For example, if a country is importing more than it exports, its trade balance will be in deficit, but the shortfall will have to be counterbalanced in other ways – such as by funds earned from its foreign investments, by running down central bank reserves or by receiving loans from other countries.

While the overall BOP accounts will always balance when all types of payments are included, imbalances are possible on individual elements of the BOP, such as the current account, the capital account excluding the central bank's reserve account, or the sum of the two. Imbalances in the latter sum can result in surplus countries accumulating wealth, while deficit nations become increasingly indebted.

The term balance of payments often refers to this sum: a country's balance of payments is said to be in surplus (equivalently, the balance of payments is positive) by a specific amount if sources of funds (such as export goods sold and bonds sold) exceed uses of funds (such as paying for imported goods and paying for foreign bonds purchased) by that amount. There is said to be a balance of payments deficit (the balance of payments is said to be negative) if the former are less than the latter. A BOP surplus (or deficit) is accompanied by an accumulation (or decumulation) of foreign exchange reserves by the central bank.

Under a fixed exchange rate system, the central bank accommodates those flows by buying up any net inflow of funds into the country or by providing foreign currency funds to the foreign exchange market to match any international outflow of funds, thus preventing the funds flows from affecting the exchange rate between the country's currency and other currencies.

Then the net change per year in the central bank's foreign exchange reserves is sometimes called the balance of payments surplus or deficit. Alternatives to a fixed exchange rate system include a managed float where some changes of exchange rates are allowed, or at the other extreme a purely floating exchange rate (also known as a purely flexible exchange rate). With a pure float the central bank does not intervene at all to protect or devalue its currency, allowing the rate to be set by the market, and the central bank's foreign exchange reserves do not change, and the balance of payments is always zero.

BALANCE OF TRADE

The commercial balance or net exports (sometimes symbolized as NX), is the difference between the monetary value of exports and imports of output in an economy over a certain period, measured in the currency of that economy. It is the relationship between a nation's imports and exports. A positive balance is known as a trade surplus if it consists of exporting more than is imported; a negative balance is referred to as a trade deficit or, informally, a trade gap. The balance of trade is sometimes divided into a goods and a services balance.

Definition

The balance of trade forms part of the current account, which includes other transactions such as income from the net international investment position as well as international aid. If the current account is in surplus, the country's net international asset position increases correspondingly. Equally, a deficit decreases the net international asset position.

The trade balance is identical to the difference between a country's output and its domestic demand (the difference between what goods a country produces and how many goods it buys from abroad; this does not include money re-spent on foreign stock, nor does it factor in the concept of importing goods to produce for the domestic market).

Measuring the balance of trade can be problematic because of problems with recording and collecting data. As an illustration of this problem, when official data for all the world's countries are added up, exports exceed imports by almost 1%; it appears the world is running a positive balance of trade with itself. This cannot be true, because all transactions involve an equal credit or debit in the account of each nation. The discrepancy is widely believed to be explained by transactions intended to launder money or evade taxes, smuggling and other visibility problems. However, especially for developed countries, accuracy is likely.

Factors that can affect the balance of trade include:

- The cost of production (land, labor, capital, taxes, incentives, etc.) in the exporting economy vis-à-vis those in the importing economy;
- The cost and availability of raw materials, intermediate goods and other inputs;
- Exchange rate movements;
- Multilateral, bilateral and unilateral taxes or restrictions on trade;
- Non-tariff barriers such as environmental, health or safety standards;
- The availability of adequate foreign exchange with which to pay for imports; and
- Prices of goods manufactured at home (influenced by the responsiveness of supply)

In addition, the trade balance is likely to differ across the business cycle. In export-led growth (such as oil and early industrial goods), the balance of trade will improve during an economic expansion. However, with domestic demand led growth (as in the United States and Australia) the trade balance will worsen at the same stage in the business cycle.

Monetary balance of trade is different from physical balance of trade (which is expressed in amount of raw materials, known also as Total Material Consumption). Developed countries usually import a lot of raw materials from developing countries. Typically, these imported materials are transformed into finished products, and might be exported after adding value. Financial trade balance statistics conceal material flow. Most developed countries have a large physical trade deficit, because they have a large ecological footprint. Civil society organizations point out the predatory nature of this imbalance, and campaign for ecological debt repayment.

Since the mid-1980s, the United States has had a growing deficit in tradable goods, especially with Asian nations (China and Japan) which now hold large sums of U.S debt that has funded the consumption. The U.S. has a trade surplus with nations such as Australia. The issue of trade deficits can be complex. Trade deficits generated in tradable goods such as manufactured goods or software may impact domestic employment to different degrees than trade deficits in raw materials.

Economies such as Japan and Germany which have savings surpluses, typically run trade surpluses. China, a high-growth economy, has tended to run trade surpluses. A higher savings rate generally corresponds to a trade surplus. Correspondingly, the U.S. with its lower savings rate has tended to run high trade deficits, especially with Asian nations.

Components

The current account shows the net amount a country is earning if it is in surplus, or spending if it is in deficit. It is the sum of the balance of trade (net earnings on exports minus payments for imports), factor income (earnings on foreign investments minus payments made to foreign investors) and cash transfers. It is called the current account as it covers transactions in the "here and now" – those that don't give rise to future claims.

The Capital Account records the net change in ownership of foreign assets. It includes the reserve account (the foreign exchange market operations of a nation's central bank), along with loans and investments between the country and the rest of world (but not the future regular repayments/dividends that the loans and investments yield; those are earnings and will be recorded in the current account). The term "capital account" is also used in the narrower sense that excludes central bank foreign exchange market operations: Sometimes the reserve account is classified as "below the line" and so not reported as part of the capital account.

Expressed with the broader meaning for the capital account, the BOP identity states that any current account surplus will be balanced by a capital account deficit of equal size – or alternatively a current account deficit will be balanced by a corresponding capital account surplus:

Current account + broadly defined capital account + Balancing item = 0

The balancing item, which may be positive or negative, is simply an amount that accounts for any statistical errors and assures that the current and capital accounts sum to zero. By the principles of double entry accounting, an entry in the current account gives rise to an entry in the capital account, and in aggregate the two accounts automatically balance.

A balance isn't always reflected in reported figures for the current and capital accounts, which might, for example, report a surplus for both accounts, but when this happens it always means something has been missed – most commonly, the operations of the country's central bank – and what has been missed is recorded in the statistical discrepancy term (the balancing item).

An actual balance sheet will typically have numerous sub headings under the principal divisions. For example, entries under Current account might include:

Trade – buying and selling of goods and services

Exports – a credit entry

Imports – a debit entry

Trade balance – the sum of Exports and Imports

Factor income – repayments and dividends from loans and investments

Factor earnings – a credit entry

Factor payments – a debit entry

Factor income balance – the sum of earnings and payments.

Especially in older balance sheets, a common division was between visible and invisible entries. Visible trade recorded imports and exports of physical goods (entries for trade in physical goods excluding services is now often called the merchandise balance). Invisible trade would record international buying and selling of services, and sometimes would be grouped with transfer and factor income as invisible earnings.

The term "balance of payments surplus" (or deficit – a deficit is simply a negative surplus) refers to the sum of the surpluses in the current account and the narrowly defined capital account (excluding changes in central bank reserves). Denoting the balance of payments surplus as BOP surplus, the relevant identity is

BOP surplus = Current account surplus + narrowly defined capital account surplus

Variations in the use of term "balance of payments"

Economics writer J. Orlin Grabbe warns the term balance of payments can be a source of misunderstanding due to divergent expectations about what the term denotes. Grabbe says the term is sometimes misused by people who aren't aware of the accepted meaning, not only in general conversation but in financial publications and the economic literature.

A common source of confusion arises from whether or not the reserve account entry, part of the capital account, is included in the BOP accounts. The reserve account records the activity of the nation's central bank. If it is excluded, the BOP can be in surplus (which implies the central bank is building up foreign exchange reserves) or in deficit (which implies the central bank is running down its reserves or borrowing from abroad).

The term "balance of payments" is sometimes misused by non-economists to mean just relatively narrow parts of the BOP such as the trade deficit, which means excluding parts of the current account and the entire capital account.

Another cause of confusion is the different naming conventions in use. Before 1973 there was no standard way to break down the BOP sheet, with the separation into invisible and visible payments sometimes being the principal divisions. The IMF has their own standards for BOP accounting which is equivalent to the standard definition but uses different nomenclature, in particular with respect to the meaning given to the term capital account.

The IMF definition of Balance of Payment

The International Monetary Fund (IMF) use a particular set of definitions for the BOP accounts, which is also used by the Organisation for Economic Co-operation and Development (OECD), and the United Nations System of National Accounts (SNA).

The main difference in the IMF's terminology is that it uses the term "financial account" to capture transactions that would under alternative definitions be recorded in the capital account. The IMF uses the term capital account to designate a subset of transactions that, according to other usage, form a small part of the overall capital account. The IMF separates these transactions out to form an additional top level division of the BOP accounts. Expressed with the IMF definition, the BOP identity can be written:

Current account + financial account + capital account + balancing item = 0

The IMF uses the term current account with the same meaning as that used by other organizations, although it has its own names for its three leading sub-divisions, which are:

- The goods and services account (the overall trade balance)
- The primary income account (factor income such as from loans and investments)
- The secondary income account (transfer payments)

Imbalances

While the BOP has to balance overall, surpluses or deficits on its individual elements can lead to imbalances between countries. In general there is concern over deficits in the current account. Countries with deficits in their current accounts will build up increasing debt and/or see increased foreign ownership of their assets. The types of deficits that typically raise concern are

- A visible trade deficit where a nation is importing more physical goods than it exports (even if this is balanced by the other components of the current account.)
- An overall current account deficit.
- A basic deficit which is the current account plus foreign direct investment (but excluding other elements of the capital account like short terms loans and the reserve account.)

As discussed in the history section below, the Washington Consensus period saw a swing of opinion towards the view that there is no need to worry about imbalances. Opinion swung back in the opposite direction in the wake of financial crisis of 2007–2009. Mainstream opinion expressed by the leading financial press and economists, international bodies like the IMF – as well as leaders of surplus and deficit countries – has returned to the view that large current account imbalances do matter. Some economists do, however, remain relatively unconcerned about imbalances and there have been assertions, such as by Michael P. Dooley, David Folkerts-Landau and Peter Garber, that nations need to avoid temptation to switch to protectionism as a means to correct imbalances.

Causes of BOP imbalances

There are conflicting views as to the primary cause of BOP imbalances, with much attention on the US which currently has by far the biggest deficit. The conventional view is that current account factors are the primary cause – these include the exchange rate, the government's fiscal deficit, business competitiveness, and private behaviour such as the willingness of consumers to go into debt to finance extra consumption. An alternative view, argued at length in a 2005 paper by Ben Bernanke, is that the primary driver is the capital account, where a global savings glut caused by savers in surplus countries, runs ahead of the available investment opportunities, and is pushed into the US resulting in excess consumption and asset price inflation.

Reserve asset

The US dollar has been the leading reserve asset since the end of the gold standard. In the context of BOP and international monetary systems, the reserve asset is the currency or other store of value that is primarily used by nations for their foreign reserves. BOP imbalances tend to manifest as hoards of the reserve asset being amassed by surplus countries, with deficit countries building debts denominated in the reserve asset or at least depleting their supply. Under a gold standard, the reserve asset for all members of the standard is gold. In the Bretton Woods system, either gold or the U.S. dollar could serve as the reserve asset, though its smooth operation depended on countries apart from the US choosing to keep most of their holdings in dollars.

Following the ending of Bretton Woods, there has been no de jure reserve asset, but the US dollar has remained by far the principal de facto reserve. Global reserves rose sharply in the first decade of the 21st century, partly as a result of the 1997 Asian Financial Crisis, where several nations ran out of foreign currency needed for essential imports and thus had to accept deals on unfavourable terms.

The International Monetary Fund (IMF) estimates that between 2000 to mid-2009, official reserves rose from $1,900bn to $6,800bn. Global reserves had peaked at about $7,500bn in mid-2008, then declined by about $430bn as countries without their own reserve currency used them to shield themselves from the worst effects of the financial crisis. From Feb 2009 global reserves began increasing again to reach close to $9,200bn by the end of 2010.

While the current central role of the dollar does give the US some advantages, such as lower cost of borrowings, it also contributes to the pressure causing the U.S. to run a current account deficit, due to the Triffin dilemma. In a November 2009 article published in Foreign Affairs magazine, economist C. Fred Bergsten argued that Dr Zhou's suggestion or a similar change to the international monetary system would be in the United States' best interests as well as the rest of the world's. Since 2009 there has been a notable increase in the number of new bilateral agreements which enable international trades to be transacted using a currency that isn't a traditional reserve asset, such as the renminbi, as the Settlement currency.

Balance of payments crisis

A BOP crisis, also called a currency crisis, occurs when a nation is unable to pay for essential imports and/or service its debt repayments. Typically, this is accompanied by a rapid decline in the value of the affected nation's currency. Crises are generally preceded by large capital inflows, which are associated at first with rapid economic growth. However a point is reached where overseas investors become concerned about the level of debt their inbound capital is generating, and decide to pull out their funds.

The resulting outbound capital flows are associated with a rapid drop in the value of the affected nation's currency. This causes issues for firms of the affected nation who have received the inbound investments and loans, as the revenue of those firms is typically mostly derived domestically but their debts are often denominated in a reserve currency. Once the nation's government has exhausted its foreign reserves trying to support the value of the domestic currency, its policy options are very limited. It can raise its interest rates to try to prevent further declines in the value of its currency, but while this can help those with debts denominated in foreign currencies, it generally further depresses the local economy.

Balancing mechanisms

One of the three fundamental functions of an international monetary system is to provide mechanisms to correct imbalances.

Broadly speaking, there are three possible methods to correct BOP imbalances, though in practice a mixture including some degree of at least the first two methods tends to be used. These methods are adjustments of exchange rates; adjustment of a nations internal prices along with its levels of demand; and rules based adjustment. Improving productivity and hence competitiveness can also help, as can increasing the desirability of exports through other means, though it is generally assumed a nation is always trying to develop and sell its products to the best of its abilities.

Rebalancing by changing the exchange rate

An upwards shift in the value of a nation's currency relative to others will make a nation's exports less competitive and make imports cheaper and so will tend to correct a current account surplus. It also tends to make investment flows into the capital account less attractive so will help with a surplus there too. Conversely a downward shift in the value of a nation's currency makes it more expensive for its citizens to buy imports and increases the competitiveness of their exports, thus helping to correct a deficit (though the solution often doesn't have a positive impact immediately due to the Marshall–Lerner condition).

Exchange rates can be adjusted by government in a rules based or managed currency regime, and when left to float freely in the market they also tend to change in the direction that will restore balance. When a country is selling more than it imports, the demand for its currency will tend to increase as other countries ultimately need the selling country's currency to make payments for the exports.

The extra demand tends to cause a rise of the currency's price relative to others. When a country is importing more than it exports, the supply of its own currency on the international market tends to increase as it tries to exchange it for foreign currency to pay for its imports, and this extra supply tends to cause the price to fall. BOP effects are not the only market influence on exchange rates however, they are also influenced by differences in national interest rates and by speculation.

Rebalancing by adjusting internal prices and demand

When exchange rates are fixed by a rigid gold standard, or when imbalances exist between members of a currency union such as the Eurozone, the standard approach to correct imbalances is by making changes to the domestic economy. To a large degree, the change is optional for the surplus country, but compulsory for the deficit country. In the case of a gold standard, the mechanism is largely automatic. When a country has a favourable trade balance, as a consequence of selling more than it buys it will experience a net inflow of gold.

The natural effect of this will be to increase the money supply, which leads to inflation and an increase in prices, which then tends to make its goods less competitive and so will decrease its trade surplus. However the nation has the option of taking the gold out of economy thus building up a hoard of gold and retaining its favorable balance of payments.

On the other hand, if a country has an adverse BOP it will experience a net loss of gold, which will automatically have a deflationary effect, unless it chooses to leave the gold standard. Prices will be reduced, making its exports more competitive, and thus correcting the imbalance. While the gold standard is generally considered to have been successful up until 1914, correction by deflation to the degree required by the large imbalances that arose after WWI proved painful, with deflationary policies contributing to prolonged unemployment but not re-establishing balance. Apart from the US most former members had left the gold standard by the mid-1930s.

A possible method for surplus countries such as Germany to contribute to re-balancing efforts when exchange rate adjustment is not suitable, is to increase its level of internal demand (i.e. its spending on goods). While a current account surplus is commonly understood as the excess of earnings over spending, an alternative expression is that it is the excess of savings over investment. That is:

$$CA = NS - NI,$$

Where,

CA = current account,

NS = national savings (private plus government sector),

NI = national investment.

If a nation is earning more than it spends the net effect will be to build up savings, except to the extent that those savings are being used for investment. If consumers can be encouraged to spend more instead of saving; or if the government runs a fiscal deficit to offset private savings; or if the corporate sector divert more of their profits to investment, then any current account surplus will tend to be reduced.

However in 2009 Germany amended its constitution to prohibit running a deficit greater than 0.35% of its GDP and calls to reduce its surplus by increasing demand have not been welcome by officials, adding to fears that the 2010s will not be an easy decade for the euro zone. In their April 2010 world economic outlook report, the IMF presented a study showing how with the right choice of policy options governments can transition out of a sustained current account surplus with no negative effect on growth and with a positive impact on unemployment.

Rules based rebalancing mechanisms

Nations can agree to fix their exchange rates against each other, and then correct any imbalances that arise by rules based and negotiated exchange rate changes and other methods. The Bretton Woods system of fixed but adjustable exchange rates was an example of a rules based system. John Maynard Keynes, one of the architects of the Bretton Woods system had wanted additional rules to encourage surplus countries to share the burden of rebalancing, as he argued that they were in a stronger position to do so and as he regarded their surpluses as negative externalities imposed on the global economy.

Keynes suggested that traditional balancing mechanisms should be supplemented by the threat of confiscation of a portion of excess revenue if the surplus country did not choose to spend it on additional imports. However his ideas were not accepted by the Americans at the time. In 2008 and 2009, American economist Paul Davidson had been promoting his revamped form of Keynes's plan as a possible solution to global imbalances which in his opinion would expand growth all rounds without the downside risk of other rebalancing methods.

History of balance of payments issues

Historically, accurate balance of payments figures were not generally available. However, this did not prevent a number of switches in opinion on questions relating to whether or not a nations government should use policy to encourage a favourable balance.

Pre-1820: mercantilism

Up until the early 19th century, international trade was generally very small in comparison with national output, and was often heavily regulated. In the middle Ages, European trade was typically regulated at municipal level in the interests of security for local industry and for established merchants.

From about the 16th century, mercantilism became the dominant economic theory influencing European rulers, which saw local regulation replaced by national rules aiming to harness the countries' economic output. Measures to promote a trade surplus such as tariffs were generally favored. Power was associated with wealth, and with low levels of growth, nations were best able to accumulate funds either by running trade surpluses or by forcefully confiscating the wealth of others. Rulers sometimes strove to have their countries outsell competitors and so build up a "war chest" of gold.

This era saw low levels of economic growth; average global per capital income is not considered to have significantly risen in the whole 800 years leading up to 1820, and is estimated to have increased on average by less than 0.1% per year between 1700 and 1820. With very low levels of financial integration between nations and with international trade generally making up a low proportion of individual nations' GDP, BOP crises were very rare.

1820–1914: free trade

Gold was the primary reserve asset during the gold standard era.

From the late 18th century, mercantilism was challenged by the ideas of Adam Smith and other economic thinkers favouring free trade. After victory in the Napoleonic wars Great Britain began promoting free trade, unilaterally reducing her trade tariffs. Hoarding of gold was no longer encouraged, and in fact Britain exported more capital as a percentage of her national income than any other creditor nation has since. Great Britain's capital exports further helped to correct global imbalances as they tended to be counter cyclical, rising when Britain's economy went into recession, thus compensating other states for income lost from export of goods.

According to historian Carroll Quigley, Great Britain could afford to act benevolently in the 19th century due to the advantages of her geographical location, its naval power and economic ascendancy as the first nation to enjoy an industrial revolution. A view advanced by economists such as Barry Eichengreen is that the first age of Globalization began with the laying of transatlantic cables in the 1860s, which facilitated a rapid increase in the already growing trade between Britain and America.

Though Current Account controls were still widely used (in fact all industrial nations apart from Great Britain and the Netherlands actually increased their tariffs and quotas in the decades leading up to 1914, though this was motivated more by a desire to protect "infant industries" than to encourage a trade surplus), capital controls were largely absent, and people were generally free to cross international borders without requiring passports.

A gold standard enjoyed wide international participation especially from 1870, further contributing to close economic integration between nations. The period saw substantial global growth, in particular for the volume of international trade which grew tenfold between 1820 and 1870 and then by about 4% annually from 1870 to 1914. BOP crises began to occur, though less frequently than was to be the case for the remainder of the 20th century. From 1880 to 1914, there were approximately 8 BOP crises and 8 twin crises – a twin crises being a BOP crises that coincides with a banking crises.

1914–1945: de-globalization

The favorable economic conditions that had prevailed up until 1914 were shattered by the first world war, and efforts to re-establish them in the 1920s were not successful. Several countries rejoined the gold standard around 1925. But surplus countries didn't "play by the rules", sterilising gold inflows to a much greater degree than had been the case in the pre-war period. Deficit nations such as Great Britain found it harder to adjust by deflation as workers were more enfranchised and unions in particular were able to resist downwards pressure on wages.

During the Great Depression most countries abandoned the gold standard, but imbalances remained an issue and international trade declined sharply. There was a return to mercantilist type "beggar thy neighbour" policies, with countries competitively devaluing their exchange rates, thus effectively competing to export unemployment. There were approximately 16 BOP crises and 15 twin crises (and a comparatively very high level of banking crises.)

1945–1971: Bretton Woods

Following World War II, the Bretton Woods institutions (the International Monetary Fund and World Bank) were set up to support an international monetary system designed to encourage free trade while also offering states options to correct imbalances without having to deflate their economies. Fixed but flexible exchange rates were established, with the system anchored by the dollar which alone remained convertible into gold. The Bretton Woods system ushered in a period of high global growth, known as the Golden Age of Capitalism, however it came under pressure due to the inability or unwillingness of governments to maintain effective capital controls and due to instabilities related to the central role of the dollar.

Imbalances caused gold to flow out of the US and a loss of confidence in the United States ability to supply gold for all future claims by dollar holders resulted in escalating demands to convert dollars, ultimately causing the US to end the convertibility of the dollar into gold, thus ending the Bretton Woods system. The 1945–71 era saw approximately 24 BOP crises and no twin crises for advanced economies, with emerging economies seeing 16 BOP crises and just one twin crises.

1971–2009: transition, Washington Consensus, Bretton Woods II

Manmohan Singh, Former PM of India, showed that the challenges caused by imbalances can be an opportunity when he led his country's successful economic reform programme after the 1991 crisis.

The Bretton Woods system came to an end between 1971 and 1973. There were attempts to repair the system of fixed exchange rates over the next few years, but these were soon abandoned, as were determined efforts for the U.S. to avoid BOP imbalances. Part of the reason was displacement of the previous dominant economic paradigm – Keynesianism – by the Washington Consensus, with economists and economics writers such as Murray Rothbard and Milton Friedman arguing that there was no great need to be concerned about BOP issues.

In the immediate aftermath of the Bretton Woods collapse, countries generally tried to retain some control over their exchange rate by independently managing it, or by intervening in the foreign exchange market as part of a regional bloc, such as the Snake which formed in 1971.

The Snake was a group of European countries who tried to retain stable rates at least with each other; the group eventually evolved into the European Exchange Rate Mechanism (ERM) by 1979. From the mid-1970s however, and especially in the 1980s and early 1990s, many other countries followed the US in liberalising controls on both their capital and current accounts, in adopting a somewhat relaxed attitude to their balance of payments and in allowing the value of their currency to float relatively freely with exchange rates determined mostly by the market.

Developing countries who chose to allow the market to determine their exchange rates would often develop sizeable current account deficits, financed by capital account inflows such as loans and investments, though this often ended in crises when investors lost confidence. The frequency of crises was especially high for developing economies in this era – from 1973 to 1997 emerging economies suffered 57 BOP crises and 21 twin crises. Typically but not always the panic among foreign creditors and investors that preceded the crises in this period was usually triggered by concerns over excess borrowing by the private sector, rather than by a government deficit. For advanced economies, there were 30 BOP crises and 6 banking crises.

A turning point was the 1997 Asian BOP Crisis, where unsympathetic responses by western powers caused policy makers in emerging economies to re-assess the wisdom of relying on the free market; by 1999 the developing world as a whole stopped running current account deficits while the U.S. current account deficit began to rise sharply. This new form of imbalance began to develop in part due to the increasing practice of emerging economies, principally China, in pegging their currency against the dollar, rather than allowing the value to freely float. The resulting state of affairs has been referred to as Bretton Woods II.

According to Alaistair Chan, "At the heart of the imbalance is China's desire to keep the value of the yuan stable against the dollar. Usually, a rising trade surplus leads to a rising value of the currency. A rising currency would make exports more expensive, imports less so, and push the trade surplus towards balance. China circumvents the process by intervening in exchange markets and keeping the value of the yuan depressed."

According to economics writer Martin Wolf, in the eight years leading up to 2007, "three-quarters of the foreign currency reserves accumulated since the beginning of time have been piled up". In contrast to the changed approach within the emerging economies, US policy makers and economists remained relatively unconcerned about BOP imbalances. In the early to mid-1990s, many free market economists and policy makers such as U.S.

Treasury secretary Paul O'Neill and Fed Chairman Alan Greenspan went on record suggesting the growing US deficit was not a major concern. While several emerging economies had intervening to boost their reserves and assist their exporters from the late 1980s, they only began running a net current account surplus after 1999. This was mirrored in the faster growth for the US current account deficit from the same year, with surpluses, deficits and the associated buildup of reserves by the surplus countries reaching record levels by the early 2000s and growing year by year. Some economists such as Kenneth Rogoff and Maurice Obstfeld began warning that the record imbalances would soon need to be addressed from as early as 2001, joined by Nouriel Roubini in 2004, but it was not until about 2007 that their concerns began to be accepted by the majority of economists.

2009 and later: post Washington Consensus

Speaking after the 2009 G-20 London summit, Gordon Brown announced "the Washington Consensus is over". There is now broad agreement that large imbalances between different countries do matter; for example mainstream U.S. economist C. Fred Bergsten has argued the U.S. deficit and the associated large inbound capital flows into the U.S. was one of the causes of the financial crisis of 2007–2010. Since the crisis, government intervention in BOP areas such as the imposition of capital controls or foreign exchange market intervention has become more common and in general attracts less disapproval from economists, international institutions like the IMF and other governments.

In 2007, when the crises began, the global total of yearly BOP imbalances was $1680 billion. On the credit side, the biggest current account surplus was China with approx. $362 billion, followed by Japan at $213bn and Germany at £185 billion, with oil producing countries such as Saudi Arabia also having large surpluses. On the debit side, the US had the biggest current account deficit at over $1100 billion, with the UK, Spain and Australia together accounting for close to a further $300 billion.

While there have been warnings of future cuts in public spending, deficit countries on the whole did not make these in 2009, in fact the opposite happened with increased public spending contributing to recovery as part of global efforts to increase demand. The emphases has instead been on the surplus countries, with the IMF, EU and nations such as the U.S., Brazil and Russia asking them to assist with the adjustments to correct the imbalances.

Economists such as Gregor Irwin and Philip R. Lane have suggested that increased use of pooled reserves could help emerging economies not to require such large reserves and thus have less need for current account surpluses. Writing for the FT in Jan 2009, Gillian Tett says she expects to see policy makers becoming increasingly concerned about exchange rates over the coming year. In June 2009, Olivier Blanchard the chief economist of the IMF wrote that rebalancing the world economy by reducing both sizeable surpluses and deficits will be a requirement for sustained recovery.

In 2008 and 2009, there was some reduction in imbalances, but early indications towards the end of 2009 were that major imbalances such as the U.S. current account deficit are set to begin increasing again.

Japan had allowed her currency to appreciate through 2009, but has only limited scope to contribute to the rebalancing efforts thanks in part to her aging population. The euro used by Germany is allowed to float fairly freely in value, however further appreciation would be problematic for other members of the currency union such as Spain, Greece and Ireland who run large deficits. Therefore Germany has instead been asked to contribute by further promoting internal demand, but this hasn't been welcomed by German officials.

China has been requested to allow the renminbi to appreciate but until 2010 had refused, the position expressed by her premier Wen Jiabao being that by keeping the value of the renmimbi stable against the dollar China has been helping the global recovery, and that calls to let her currency rise in value have been motivated by a desire to hold back China's development. After China reported favourable results for her December 2009 exports however, the Financial Times reported that analysts are optimistic that China will allow some appreciation of her currency around mid-2010.

In April 2010 a Chinese official signalled the government is considering allowing the renminbi to appreciate, but by May analysts were widely reporting the appreciation would likely be delayed due to the falling value of the Euro following the 2010 European sovereign debt crisis. China announced the end of the renminbi's peg to the dollar in June 2010; the move was widely welcomed by markets and helped defuse tension over imbalances prior to the 2010 G-20 Toronto summit. However the renminbi remains managed and the new flexibility means it can move down as well as up in value; two months after the peg ended the renminbi had only appreciated against the dollar by about 0.8%.

By January 2011, the renminbi had appreciated against the dollar by 3.7%, which means it's on track to appreciate in nominal terms by 6% per year. As this reflects a real appreciation of 10% when China's higher inflation is accounted for, the U.S. Treasury once again declined to label China a currency manipulator in their February 2011 report to Congress. However Treasury officials did advise the rate of appreciation was still too slow for the best interests of the global economy.

In February 2011, Moody's analyst Alaistair Chan has predicted that despite a strong case for an upward revaluation, an increased rate of appreciation against the dollar is unlikely in the short term. And as of February 2012, China's currency had been continuing to appreciate for a year and a half, while drawing remarkably little notice.

While some leading surplus countries including China have been taking steps to boost domestic demand, these have not yet been sufficient to rebalance out of their current account surpluses. By June 2010, the U.S. monthly current account deficit had risen back to $50 billion, a level not seen since mid-2008. With the US currently suffering from high unemployment and concerned about taking on additional debt, fears are rising that the US may resort to protectionist measures.

Competitive devaluation after 2009

By September 2010, international tensions relating to imbalances had further increased. Brazil's finance minister Guido Mantega declared that an "international currency war" has broken out, with countries competitively trying to devalue their currency so as to boost exports. Brazil has been one of the few major economies lacking a reserve currency to abstain from significant currency intervention, with the real rising by 25% against the dollar since January 2009.

Some economists such as Barry Eichengreen have argued that competitive devaluation may be a good thing as the net result will effectively be equivalent to expansionary global monetary policy. Others such as Martin Wolf saw risks of tensions further escalating and advocated that coordinated action for addressing imbalances should be agreed on at the November G20 summit.

Commentators largely agreed that little substantive progress was made on imbalances at the November 2010 G20. An IMF report released after the summit warned that without additional progress there is a risk of imbalances approximately doubling to reach pre-crises levels by 2014.

IMF Balance of Payments Manual

The Balance of Payments Manual published by the International Monetary Fund provides accounting standards for balance of payments reporting and analysis for many countries. The Bureau of Economic Analysis adheres to this standard.

The sixth edition was released in prepublication form in December 2008. Its title has been amended to Balance of Payments and International Investment Position Manual to reflect that it covers not only transactions, but also the stocks of the related financial assets and liabilities.

Tariff

A tariff is a tax on imports or exports (an international trade tariff), or a list of prices for such things as rail service, bus routes, and electrical usage (electrical tariff, etc.).

Etymology

The small Spanish town of Tarifa is sometimes credited with being the origin of the word "tariff", since it was the first port in history to charge merchants for the use of its docks The name "Tarifa" itself is derived from the name of the Berber warrior, Tarif ibn Malik. However, other sources assume that the origin of tariff is the Italian word tariffa translated as "list of prices, book of rates," which is derived from the Arabic ta'rif meaning "making known" or "to define".

Customs duty

A customs duty or due is the indirect tax levied on the import or export of goods in international trade. In economic sense, a duty is also a kind of consumption tax. A duty levied on goods being imported is referred to as an import duty. Similarly, a duty levied on exports is called an export duty. A tariff, which is actually a list of commodities along with the leviable rate (amount) of customs duty, is popularly referred to as a customs duty.

In the Kingdom of England, customs duties were typically part of the customary revenue of the king, and therefore did not need parliamentary consent to be levied, unlike excise duty, land tax, or other forms of taxes. This is no longer the case.

Calculation of customs duty

Customs duty is calculated on the determination of the assessable value in case of items for which the duty is levied ad valorem. This is often the transaction value unless a customs officers determines assessable value in accordance with the Harmonized System.

However, for certain items like petroleum and alcohol, customs duty is realized at a specific rate applied to the volume of the import or export consignments.

Harmonized System of Nomenclature

For the purpose of assessment of customs duty, products are given an identification code that has come to be known as the Harmonized System code. This code was developed by the World Customs Organization based in Brussels. A Harmonized System code may be from four to ten digits. For example 17.03 is the HS code for molasses from the extraction or refining of sugar. However, within 17.03, the number 17.03.90 stands for "Molasses (Excluding Cane Molasses)".

Introduction of Harmonized System code in 1990s has largely replaced the Standard International Trade Classification (SITC), though SITC remains in use for statistical purposes. In drawing up the national tariff, the revenue departments often specifies the rate of customs duty with reference to the HS code of the product. In some countries and customs unions, 6-digit HS codes are locally extended to 8 digits or 10 digits for further tariff discrimination: for example the European Union uses its 8-digit CN (Combined Nomenclature) and 10-digit TARIC codes.

Customs authority

A Customs authority in each country is responsible for collecting taxes on the import into or export of goods out of the country. Normally the Customs authority, operating under national law, is authorized to examine cargo in order to ascertain actual description, specification volume or quantity, so that the assessable value and the rate of duty may be correctly determined and applied.

Evasion of customs duty

Evasion of customs duties takes place mainly in two ways. In one, the trader under-declares the value so that the assessable value is lower than actual. In a similar vein, a trader can evade customs duty by understatement of quantity or volume of the product of trade. Evasion of customs duty may take place with or without the collaboration of customs officials. Evasion of customs duty does not necessarily constitute smuggling.

Duty-free goods

Many countries allow a traveller to bring goods into the country duty-free. These goods may be bought at ports and airports or sometimes within one country without attracting the usual government taxes and then brought into another country duty-free. Some countries impose allowances which limit the number or value of duty-free items that one person can bring into the country. These restrictions often apply to tobacco, wine, spirits, cosmetics, gifts and souvenirs. Often foreign diplomats and UN officials are entitled to duty-free goods. Duty-free goods are imported and stocked in what is called a bonded warehouse.

Duty calculation for companies in real life

With many methods and regulations, businesses at times struggle to manage the duties. In addition to difficulties in calculations, there are challenges in analyzing duties; and to opt for duty free options like using a bonded warehouse.

Companies use ERP software to calculate duties automatically to, on one hand, avoid error-prone manual work on duty regulations and formulas and on the other hand, manage and analyze the historically paid duties. Moreover, ERP software offers an option for customs warehouse, introduced to save duty and VAT payments. In addition, the duty deferment and suspension is also taken into consideration.

Economic analysis

Neoclassical economic theorists tend to view tariffs as distortions to the free market. Typical analyses find that tariffs tend to benefit domestic producers and government at the expense of consumers, and that the net welfare effects of a tariff on the importing country are negative. Normative judgments often follow from these findings, namely that it may be disadvantageous for a country to artificially shield an industry from world markets and that it might be better to allow a collapse to take place. Opposition to all tariff Organization aims to reduce tariffs and to avoid countries discriminating between differing countries when applying tariffs. The diagrams to the right show the costs and benefits of imposing a tariff on a good in the domestic economy, Home.

Political analysis

The tariff has been used as a political tool to establish an independent nation; for example, the United States Tariff Act of 1789, signed specifically on July 4, was called the "Second Declaration of Independence" by newspapers because it was intended to be the economic means to achieve the political goal of a sovereign and independent United States.

In modern times, the political impact of tariffs has been seen in a positive and negative sense. The 2002 United States steel tariff imposed a 30% tariff on a variety of imported steel products for a period of three years. American steel producers supported the tariff, but the move was criticised by the Cato Institute.

Unpopular tariffs are known to have ignited social unrest. Example of this are the 1905 Meat riots in Chile that evolved from protests against tariffs applied to the cattle imports from Argentina.

Tariffs within technology strategies

When tariffs are an integral element of a country's technology strategy, the tariffs can be highly effective in helping to increase and maintain the country's economic health. As an integral part of the technology strategy, tariffs are effective in supporting the technology strategy's function of enabling the country to outmaneuver the competition in the acquisition and utilization of technology in order to produce products and provide services that excel at satisfying the customer needs for a competitive advantage in domestic and foreign markets. This is related to the Infant industry argument.

In contrast, in economic theory tariffs are viewed as a primary element in international trade with the function of the tariff being to influence the flow of trade by lowering or raising the price of targeted goods to create what amounts to an artificial competitive advantage.

When tariffs are viewed and used in this fashion, they are addressing the countries and the competitors' respective economic health’s in terms of maximizing or minimizing revenue flow rather than in terms of the ability to generate and maintain a competitive advantage which is the source of the revenue. As a result, the impact of the tariffs on the economic health of the country are at best minimal but often are counter-productive.

A program within the US intelligence community, Project Socrates, that was tasked with addressing America's declining economic competitiveness, determined that countries like China and India were using tariffs as an integral element of their respective technology strategies to rapidly build their countries into economic superpowers. It was also determined that the US, in its early years, had also used tariffs as an integral part of amounted to technology strategies to transform the country into a superpower.

The Importance of Tariff Classification

For Government

For government, a tariff classification system enables "uniform identification of imported and exported goods for purposes of duty and tax collection, enforcement of national laws and international treaties, analysis for economic and business planning, and international trade negotiations."

For Companies

For users of the tariff (importers and exporters of all types and sizes), correct classification is a legal responsibility. Non-compliance can mean shipment delays, increased inspections, fines, and other administrative penalties.

Correct classification often saves money, both in the short and long term. When examining a company's past imports, customs consultants find that overall, too much duty has been paid, indicating that full advantage of provisions of the tariff were not taken. Making use of these provisions requires a precise knowledge of the product to be classified, something that the importer or exporter has, as well as knowledge of the Tariff and the principles of classification, something readily know-able.

Whether goods are eligible for any of the special provisions of the Tariff that allow for lower duty rates usually depends on the use or purpose for which they are being imported, or on the availability of certificates of origin. Again, the importer is in the best position to know these facts.

Verifying the classification decisions of customs brokers and professional classification suppliers is a good way of protecting both compliance records and revenue outlay in the form of duties and taxes. By understanding how the tariff classification process works, importers will be able to work together with their classification provider (usually a customs broker or consultant) to ensure that their goods are classified correctly.

An international "Harmonized System" for the description and classification of goods was created in 1988, and soon after adopted by nations around the world. The broad, core specifics and structure of Harmonized System classifications is universal, with each participating country eligible to add and define specific detail items, and to create and assign rates of duty in any required categories for all classifications.

Optimal tariff

The level of a tariff that maximizes a country's welfare. In a non-distorted small open economy, the optimal tariff is zero. In a large country it is positive, due to its effect on the terms of trade. A bird's eye view of the stock exchange where optimal tariffs are negotiated between countries. An optimum -- or optimal -- tariff is a tax designed for maximizing the welfare of a country. Optimum tariffs are found in international trade.

Purpose

Tariffs are taxes levied by a country and charged for sales internationally. They increase the country's overall income. Other countries often retaliate by also charging an optimum tariff.

Considerations

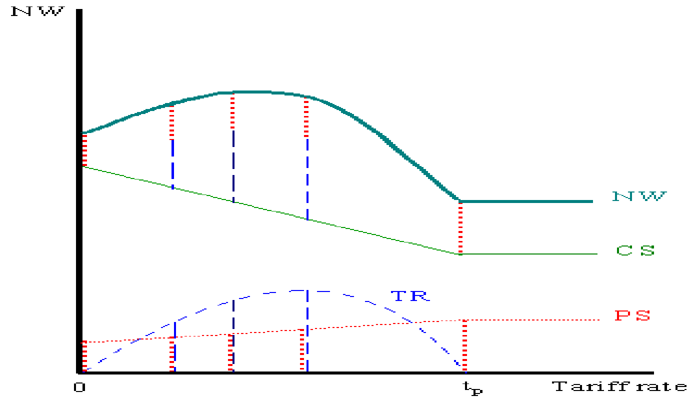
Only large countries use optimum tariffs and benefit from them. Small countries with small economies do not have optimum tariffs. The tariff in this case is considered zero. Large countries using optimum tariffs, however, are considered to have a positive tariff because of the effect on trade.

Effects

While these tariffs were designed to increase a country's wealth, a common effect is a decrease in demand for products offered by the country.

The possibility that a tariff could improve national welfare for a large country in international markets was first noted by Robert Torrens (1844). Since the welfare improvement occurs only if the terms of trade gain exceeds the total deadweight losses, the argument is commonly known as the Terms of Trade Argument for protection.

Economists have studied the conditions under which a tariff will be welfare improving in a variety of perfectly competitive models. This section describes the general results that come from that analysis.



Consider the adjoining diagram plotting the levels of consumer surplus (CS), producer surplus (PS), and tariff revenue (TR) at different tariff rates. The origin corresponds to a zero tariff rate, or free trade. As the tariff is increased from zero consumer surplus falls since the domestic price rises. This is shown by the solid declining (green) CS line. When the tariff becomes prohibitive at tp, the price settles at the autarky price and any further increases in the tariff have no effect upon consumer surplus. Hence the CS line becomes flat above tp.

Producer surplus (PS), the red dotted line, rises as the tariff is increased from 0, however it rises at a lower rate than consumer surplus falls. This occurs because, for an importing country, producer surplus increases are less than the change in consumer surplus for any increase in the tariff. When the prohibitive tariff is reached, again the price settles at the autarky price and any further increases in the tariff rate has no effect upon producer surplus.

Tariff revenue (TR), the blue dashed line, first increases with the increase in the tariff and then decreases for higher tariff rates. This occurs because tariff revenue equals the tariff rate time's imports. As the tariff in increased from zero, imports fall at a slower rate than the increase in the tariff rate, hence revenue rises. Eventually imports begin to fall faster than the tariff rate rises and tariff revenue declines.

Another way to see that tariff revenue must rise then fall with increasing tariffs is to note that when the tariff rate is zero, tariff revenue has to be zero for any level of imports. Also, when the tariff rate is at or above tp, the prohibitive tariff, imports are zero, thus whatever the tariff rate; tariff revenue again must be zero. Somewhere between a zero tariff and the prohibitive tariff, tariff revenue has to be positive. Thus, tariff revenue must rise from zero and then fall back to zero when it reaches tp.

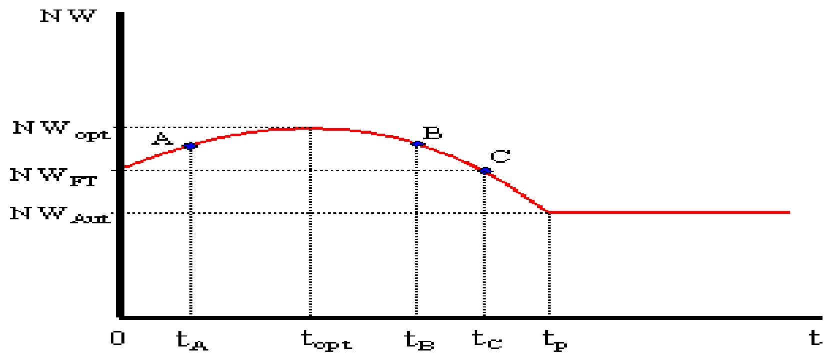
The national welfare level at each tariff rate is defined as the sum of consumer surplus, producer surplus and tariff revenue. The vertical summation of these three curves generates the national welfare curve (NW) given by the thick solid blue-green line. In the diagram, the vertical summation is displayed for five different levels of the tariff rate.

The basic shape of the national welfare line is redrawn in the next diagram. Note that national welfare first rises then falls as the tariff is increased from zero. For one tariff rate (topt), the country can realize the highest level of national welfare (NWopt), one that is higher than that achievable in free trade. We call that tariff rate the "optimal tariff."

If the tariff is raised above the optimal rate, as with an increase from topt to tB, then national welfare will fall. The terms of trade gain, which rises as low tariffs are increased, will begin to fall at a higher tariff rate. Since the deadweight losses continue to rise, both effects contribute to the decline in national welfare. Note, however, that at a tariff level like tB,national welfare still exceeds the free trade level.

Eventually, at even higher tariff rates, national welfare will fall below the free trade level. In the diagram this occurs at tariff rates greater than tC. The higher the tariff is raised, the lower will be the level of imports. At a sufficiently high tariff, imports will be eliminated entirely. The tariff will prohibit trade. At the prohibitive tariff, tp in the diagram, there is no tariff revenue, which implies that the previously positive terms of trade gain is now zero. The only effect of the tariff is the deadweight loss. The economy is effectively in autarky, at least with respect to this one market, hence national welfare is at NWAut. Note that any additional increases in the tariff above tp, will maintain national welfare at NWAut since the market remains at the autarky equilibrium.

The National Welfare Effects of Trade Liberalization for a Large Country. Trade liberalization can be represented by a decrease in the tariff rate on imports into a country. If the country is large in international markets, then the analysis above suggests that the effect on national welfare will depend on the values of the original tariff rate and the liberalized tariff rate.



For example, if the tariff is reduced from topt to tA, then national welfare will fall when the country liberalizes trade in this market. However, if the tariff is reduced from tB to topt, then national welfare will rise when trade liberalization occurs. This implies that trade liberalization is not necessarily welfare improving for a large importing country.

4 Main Types of Disequilibrium in the Balance of Payments | Foreign Trade

Main types of disequilibrium in the balance of payments are: i. Cyclical Disequilibrium ii. Structural Disequilibrium iii. Short-run Disequilibrium iv. Long-run Disequilibrium!

i. Cyclical Disequilibrium:

It occurs on account of trade cycles. Depending upon the different phases of trade cycles like prosperity and depression, demand and other forces vary, causing changes in the terms of trade as well as growth of trade and accordingly a surplus or deficit will result in the balance of payments.

Cyclical disequilibrium in the balance of payments may occur because:

i. Trade cycles follow different paths and patterns in different countries. There are no identical timings and periodicity of occurrence of cycles in different countries.

ii. No identical stabilisation programmes and measures are adopted by different countries.

iii. Income elasticities of demand for imports in different countries are not identical.

iv. Price elasticities of demand for imports differ in different countries.

In short, cyclical fluctuations cause disequilibrium in the balance of payments because of cyclical changes in income, employment, output and price variables. When prices rise during prosperity and fall during a depression, a country which has a highly elastic demand for imports experiences a decline in the value of imports and if it continues its exports further, it will show a surplus in the balance of payments.

Since deficit and surplus alternatively take place during the depression and prosperity phase of a cycle, the balance of payments equilibrium is automatically set forth over the complete cycle.

ii. Structural Disequilibrium:

It emerges on account of structural changes occurring in some sectors of the economy at home or abroad which may alter the demand or supply relations of exports or imports or both. Suppose the foreign demand for India’s jute products declines because of some substitutes, then the resources employed by India in the production of jute goods will have to be shifted to some other commodities of export.

If this is not easily possible, India's exports may decline whereas with imports remaining the same, disequilibrium in the balance of payments will arise. Similarly, if the supply condition of export items is changed, i.e., supply is reduced due to crop failure in prime commodities or shortage of raw materials or labour strikes, etc. in the case of manufactured goods, then also exports may decline to that extent and structural disequilibrium in the balance of payments will arise.

Moreover, a shift in demand occurs with the changes in tastes, fashions, habits, income, economic progress, etc. Propensity to import may change as a result. Demand for some imported goods may increase, while that for certain goods may decline leading to a structural change.

Furthermore, structural changes are also produced by variations in the rate of international capital movements. A rise in the inflow of international capital tends to have a direct impact on a country's balance of payments.

iii. Short-run Disequilibrium:

A short-run disequilibrium in a country's balance of payments will be a temporary one, 'lasting for a short period, which may occur once in a while. When a country borrows or lends internationally, it will have short-run disequilibrium in its balance of payments, as these loans are usually for a short period or even if they are for a long duration, they are repayable later on; hence the position will be automatically corrected and poses no serious problem.

As such, a disequilibrium arising from international lending and borrowing activities is perfectly justified. However, a short-run disequilibrium may also emerge if a country's imports exceed its exports in a given year.

This will be a temporary one if it occurs once in a way, because later on, the country will be in a position to correct it easily by creating the required credit surplus by exporting more to offset the deficit. But even this type of disequilibrium in the balance of payments is not justified, because it may pave the way for a long-term disequilibrium.

When such disequilibrium (arising from imports exceeding exports or even vice versa) occurs year after year over a long period, it becomes chronic and may seriously affect the country's economy and its international economic relations. A persistent deficit will tend to deplete its foreign exchange reserves and the country may not be able to raise any more loans from foreigners.

iv. Long-run Disequilibrium:

The long-term disequilibrium thus refers to a deep- rooted, persistent deficit or surplus in the balance of payments of a country. It is secular disequilibrium emerging on account of the chronologically accumulated short--term disequilibria — deficits or surpluses.

It endangers the exchange stability of the country concerned. Especially, a long-term deficit in the balance of payments of a country tends to deplete its foreign exchange reserves and the country may also not be able to raise any more loans from foreigners during such a period of persistent deficits.

In short, true disequilibrium is a long-term phenomenon. It is caused by persistent deep-rooted dynamic changes which slowly take place in the economy over a long period of time. It is caused by changes in dynamic forces/factors such as capital formation, population growth, territorial expansion, technological advancement, innovations, etc.

A newly developing economy, for instance, in its initial stages of growth needs huge investment exceeding its savings. In view of its low capital formation, it has also to import a large amount of its capital requirements from foreign countries and its imports thus tend to exceed its exports. These become a chronic phenomenon. And in the absence of a sufficient inflow of foreign capital in such countries, a secular deficit balance of payments may result.

Causes of Disequilibrium in Balance of Payment ↓

1. Population Growth

Most countries experience an increase in the population and in some like India and China the population is not only large but increases at a faster rate. To meet their needs, imports become essential and the quantity of imports may increase as population increases.

2. Development Programmes

Developing countries which have embarked upon planned development programmes require to import capital goods, some raw materials which are not available at home and highly skilled and specialized manpower. Since development is a continuous process, imports of these items continue for the long time landing these countries in a balance of payment deficit.

3. Demonstration Effect

When the people in the less developed countries imitate the consumption pattern of the people in the developed countries, their import will increase. Their export may remain constant or decline causing disequilibrium in the balance of payments.

4. Natural Factors

Natural calamities such as the failure of rains or the coming floods may easily cause disequilibrium in the balance of payments by adversely affecting agriculture and industrial production in the country. The exports may decline while the imports may go up causing a discrepancy in the country's balance of payments.

5. Cyclical Fluctuations

Business fluctuations introduced by the operations of the trade cycles may also cause disequilibrium in the country's balance of payments. For example, if there occurs a business recession in foreign countries, it may easily cause a fall in the exports and exchange earning of the country concerned, resulting in a disequilibrium in the balance of payments.

6. Inflation

An increase in income and price level owing to rapid economic development in developing countries, will increase imports and reduce exports causing a deficit in balance of payments.

7. Poor Marketing Strategies

The superior marketing of the developed countries have increased their surplus. The poor marketing facilities of the developing countries have pushed them into huge deficits.

8. Flight Of Capital

Due to speculative reasons, countries may lose foreign exchange or gold stocks People in developing countries may also shift their capital to developed countries to safeguard against political uncertainties. These capital movements adversely affect the balance of payments position.

9. Globalisation

Due to globalisation there has been more liberal and open atmosphere for international movement of goods, services and capital. Competition has beer increased due to the globalisation of international economic relations. The emerging new global economic order has brought in certain problems for some countries which have resulted in the balance of payments disequilibrium.

UNIT-III – Syllabus

India’s Industrialization Strategy and International Trade - Review of Economic planning strategies and issues - Early phase; the 1970s and 1980 - Policies since 1991 - Exim policy - Structure of tariffs and restrictions - Currency depreciation and convertibility - Export Promotion Zones, Special Economic Zones, Importer and Exporter Code (IE Code).

Export Procedures

- **Export Licence**

Majority of goods are allowed to be exported without obtaining a licence. Export licenses are only required for items listed in the Schedule 2 of ITC (HS) Classifications of Export and Import items. An application for grant of Export Licence for such items must be submitted to the Director General of Foreign Trade (DGFT). The Export Licensing Committee under the Chairmanship of Export Commissioner considers such applications on merits for issue of export licenses.

Export of Special Chemicals, Organisms, Materials, Equipment and Technologies (SCOMET) items are also permitted under a license or prohibited altogether. Guidelines for Export of SCOMET items can be viewed here.

- **Export of Samples**

Export of samples upto specified limits are allowed free. The exporter is required to be registered with the appropriate Export Promotion Council to avail of this benefit. Samples with permanent marking as "sample not for sale" are allowed freely for export without any limit.

- **Processing of Shipping Bill**

In case of export by sea or air, the exporter must submit the 'Shipping Bill', and in case of export by road he must submit 'Bill of Export' in the prescribed form containing the prescribed details such as the name of the exporter, consignee, invoice number, details of packing, description of goods, quantity, FOB value, etc. Along with the Shipping Bill, other documents such as copy of packing list, invoices, export contract, letter of credit, etc. are also to be submitted. There are 5 types of shipping bills:-

- Shipping Bill for export of duty free goods. This shipping bill is white coloured.
- Shipping bill for export of goods under claim for duty drawback. This shipping bill is green coloured.
- Shipping bill for export of duty free goods ex-bond i.e. from bonded warehouse. This shipping bill is pink coloured.
- Shipping Bill for export of dutiable goods. This shipping bill is yellow coloured.

- Shipping bill for export under DEPB scheme. This shipping bill is blue in colour.

The Bills of Export are:-

- Bill of export for goods under claim for duty drawback
- Bill of export for dutiable goods
- Bill of export for duty free goods
- Bill of export for duty free goods ex-bond
- Exporters can check and track the status of Shipping Bills online.

Let Export Order

After the receipt of the goods in the dock, the exporter may contact the Customs Officer designated for the purpose and present the checklist with the endorsement of Port Authority and other declarations along with all original documents. Customs Officer may verify the quantity of the goods actually received and thereafter mark the Electronic Shipping Bill and also hand over all original documents to the Dock Appraiser, who may assign a customs officer for the examination of the goods. If the Dock Appraiser is satisfied that the particulars entered in the system conform to the description given in the original documents, he may proceed to allow "let export" for the shipment.

EXPORT DOCUMENTATION AND PROCEDURES

Exporters should seriously consider having the freight forwarder handle the formidable amount of documentation that exporting requires; freight forwarders are specialists in this process. The following documents are commonly used in exporting; which of them are actually used in each case depends on the requirements of both our government and the government of the importing country.

- Commercial invoice
- Bill of lading
- Consular invoice
- Certificate of origin
- Inspection certification
- Dock receipt and warehouse receipt
- Destination control statement
- Insurance certificate
- Export license
- Export packing list

Enquiry:

STEP1

The starting point for any Export Transaction is an enquiry. An enquiry for product should, inter alia, specify the following details or provide the following data

- Size details - Std. or oversize or undersize
- Drawing, if available
- Sample, if possible
- Quantity required
- Delivery schedule
- Is the price required on FOB or C& F or CIF basis
- Mode of Dispatch - Sea, air or Sea/air
- Mode of Packing
- Terms of Payment that would be acceptable to the Buyer - If the buyer proposes to open any Letter of Credit, any specific requirement to be complied with by the Exporter
- Is there any requirement of Pre-shipment inspection and if so, by which agency
- Any Certificate of Origin required - If so, from what agency.

STEP 2: - Proforma generation:

After studying the enquiry in detail, the exporter - be it Manufacturer Exporter or Merchant Exporter - will provide a Proforma Invoice to the Buyer.

STEP 3: Order placement:

If the offer is acceptable to the Buyer in terms of price, delivery and payment terms, the Buyer will then place an order on the Exporter, giving as much data as possible in terms of specifications, Part No. Quantity etc. (No standard format is required for such a purchase order)

STEP 4: Order acceptance:

It is advisable that the Exporter immediately acknowledges receipt of the order, giving a schedule for the delivery committed.

STEP 5: Goods readiness & documentation:

Once the goods are ready duly packed in Export worthy cases/cartons (depending upon the mode of despatch), the Invoice is prepared by the Exporter. If the number of packages is more than one, a packing list is a must.

Even If the goods to be exported are excisable, no excise duty need be charged at the time of Export, as export goods are exempt from Central Excise, but the AR4 procedure is to be followed for claiming such an exemption. Similarly, no Sales Tax also is payable for export of goods.

STEP 6: Goods removal from works:

There are different procedures for removing Export consignments to the Port, following the AR4 procedure, but it would be advisable to get the consignment sealed by the Central Excise authorities at the factory premises itself, so that open inspection by Customs authorities at the Port can be avoided.

If export consignments are removed from the factory of manufacture, following the AR4 procedure, claiming exemption of excise duty, there is an obligation cast on the exporter to provide proof of export to the Central Excise authorities

STEP 7: Documents for C & F agent:

The Exporter is expected to provide the following documents to the Clearing & Forwarding Agents, who are entrusted with the task of shipping the consignments, either by air or by sea.

- Invoice
- Packing List
- Declaration in Form SDF (to meet the requirements as per FERA) in duplicate.
- AR4 - first and the second copy
- Any other declarations, as required by Customs

On account of the introduction of Electronic Data Interchange (EDI) system for processing shipping bills electronically at most of the locations - both for air or sea consignments - the C&F Agents are required to file with Customs the shipping documents, through a particular format, which will vary depending on the nature of the shipment. Broad categories of export shipments are:

- Under claim of Drawback of duty
- Without claim of Drawback
- Export by a 100% EOU
- Under DEPB Scheme

STEP 8: Customs Clearance:

After assessment of the shipping bill and examination of the cargo by Customs (where required), the export consignments are permitted by Customs for ultimate Export. This is what the concerned Customs officials call the 'LET EXPORT' endorsement on the shipping bill.

STEP 9: Document Forwarding:

After completing the shipment formalities, the C & F Agents are expected to forward to the Exporter the following documents:

- Customs signed Export Invoice & Packing List
- Duplicate of Form SDF
- Exchange control copy of the Shipping Bill, processed electronically
- AR4 (original duplicate) duly endorsed by Customs for having effected the Export
- Bill of Lading or Airway bill, as the case may be.

STEP 10: Bills negotiation:

With these authenticated shipping documents, the Exporter will have to negotiate the relevant export bill through authorized dealers of Reserve Bank, viz., Banks.

Under the Generalized System of Preference, imports from developing countries enjoy certain duty concessions, for which the exporters in the developing countries are expected to furnish the GSP Certificate of Origin to the Bankers, along with other shipping documents.

Broadly, payment terms can be:

- DP Terms
- DA Terms
- Letter of Credit, payable at sight or payable at... days.

Step11: Bank to bank documents forwarding:

The negotiating Bank will scrutinize the shipping documents and forward those to the Banker of the importer, to enable him clear the consignment.

It is expected of such authorized dealers of Reserve Bank to ensure receipt of export proceeds, which factor has to be intimated to the Reserve Bank by means of periodical Returns.

STEP 12: Customs obligation discharge:

As indicated above, Exporters are also expected to provide proof of export to the Central Excise authorities, on the basis of the Customs endorsements made on the reverse of AR4s and get their obligation, on this score, discharged.

STEP 13: Receipt of Bank certificate:

Authorized dealers will issue Bank Certificates to the exporter, once the payment is received and only with the issuance of the Bank Certificate, the export transaction becomes complete.

It is mandatory on the part of the Exporters to negotiate the shipping documents only through authorized dealers of Reserve Bank, as only through such a system Reserve Bank can ensure receipt of export proceeds for goods shipped out of this country.

Documents Required

Export procedure describes the documents required for exporting from India. Special documents may be required depending on the type of product or destination. Certain export products may require a quality control inspection certificate from the Export Inspection Agency. Some food and pharmaceutical product may require a health or sanitary certificate for export.

Shipping Bill/ Bill of Export is the main document required by the Customs Authority for allowing shipment. Usually the Shipping Bill is of four types and the major distinction lies with regard to the goods being subject to certain conditions which are mentioned below:

- Export duty/ cess
- Free of duty/ cess
- Entitlement of duty drawback
- Entitlement of credit of duty under DEPB Scheme
- Re-export of imported goods

The following are the export documents required for the processing of the Shipping Bill:

- GR forms (in duplicate) for shipment to all the countries.
- 4 copies of the packing list mentioning the contents, quantity, gross and net weight of each package.
- 4 copies of invoices which contains all relevant particulars like number of packages, quantity, unit rate, total f.o.b./ c.i.f. value, correct & full description of goods etc.
- Contract, L/ C, Purchase Order of the overseas buyer.
- AR4 (both original and duplicate) and invoice.
- Inspection/ Examination Certificate. The formats presented for the Shipping Bill are as given below
- White Shipping Bill in triplicate for export of duty free of goods.
- Green Shipping Bill in quadruplicate for the export of goods which are under claim for duty drawback.
- Yellow Shipping Bill in triplicate for the export of dutiable goods.
- Blue Shipping Bill in 7 copies for exports under the DEPB scheme

Note: - For the goods which are cleared by Land Customs, Bill of Export (also of 4 types - white, green, yellow & pink) is required instead of Shipping Bill.

Documents Required for Post Parcel Customs Clearance

In case of Post Parcel, no Shipping Bill is required. The relevant documents are mentioned below:

- Customs Declaration Form - It is prescribed by the Universal Postal Union (UPU) and international apex body coordinating activities of national postal administration. It is known by the code number CP2/ CP3 and to be prepared in quadruplicate, signed by the sender.
- Dispatch Note, also known as CP2. It is filled by the sender to specify the action to be taken by the postal department at the destination in case the address is non-traceable or the parcel is refused to be accepted.
- Prescriptions regarding the minimum and maximum sizes of the parcel with its maximum weight : Minimum size: Total surface area not less than 140 mm X 90 mm.
- Maximum size: Lengthwise not over 1.05 m. Measurement of any other side of circumference 0.9 m./ 2.00 m.
- Maximum weight: 10 kg usually, 20 kg for some destinations.
- Commercial invoice - Issued by the seller for the full realizable amount of goods as per trade term.
- Consular Invoice - Mainly needed for the countries like Kenya, Uganda, Tanzania, Mauritius, New Zealand, Burma, Iraq, Ausatralia, Fiji, Cyprus, Nigeria, Ghana, Zanzibar etc. It is prepared in the prescribed format and is signed/ certified by the counsel of the importing country located in the country of export.
- Customs Invoice - Mainly needed for the countries like USA, Canada, etc. It is prepared on a special form being presented by the Customs authorities of the importing country. It facilitates entry of goods in the importing country at preferential tariff rate.
- Legalized/Visaed Invoice - This shows the seller's genuineness before the appropriate consulate/ chamber of commerce/ embassy. It do not have any prescribed form.
- Certified Invoice - It is required when the exporter needs to certify on the invoice that the goods are of a particular origin or manufactured/ packed at a particular place and in accordance with specific contract. Sight Draft and Usance Draft are available for this. Sight Draft is required when the exporter expects immediate payment and Usance Draft is required for credit delivery.
- Packing List - It shows the details of goods contained in each parcel/ shipment.
- Certificate of Inspection - It shows that goods have been inspected before shipment.
- Black List Certificate - It is required for countries which have strained political relation. It certifies that the ship or the aircraft carrying the goods has not touched those country(s).
- Weight Note - Required to confirm the packets or bales or other form are of a stipulated weight.
- Manufacturer's/ Supplier's Quality/ Inspection Certificate.
- Manufacturer's Certificate - It is required in addition to the Certificate of Origin for few countries to show that the goods shipped have actually been manufactured and are available.

- Certificate of Chemical Analysis - It is required to ensure the quality and grade of certain items such as metallic ores, pigments, etc.
- Certificate of Shipment - It signifies that a certain lot of goods have been shipped.
- Health/ Veterinary/ Sanitary Certification - Required for export of foodstuffs, marine products, hides, livestock etc.
- Certificate of Conditioning - It is issued by the competent office to certify compliance of humidity factor, dry weight, etc.
- Antiquity Measurement - Issued by Archaeological Survey of India in case of antiques.
- Tran-shipment Bill - It is used for goods imported into a customs port/ airport intended for Tran-shipment.
- Shipping Order - Issued by the Shipping (Conference) Line which intimates the exporter about the reservation of space of shipment of cargo through the specific vessel from a specified port and on a specified date.
- Cart/ Lorry Ticket - It is prepared for admittance of the cargo through the port gate and includes the shipper's name, cart/ lorry No., marks on packages, quantity, etc.
- Shut Out Advice - It is a statement of packages which are shut out by a ship and is prepared by the concerned shed and is sent to the exporter.
- Short Shipment Form - It is an application to the customs authorities at port which advises short shipment of goods and required for claiming the return.
- Shipping Advice - It is prepared in aligned document to be used to inform the overseas customer about the shipment of goods.

Order (business)

In business or commerce, an order is a stated intention, either spoken or written, to engage in a commercial transaction for specific products or services. From a buyer's point of view it expresses the intention to buy and is called a purchase order. From a seller's point of view it expresses the intention to sell and is referred to as a sales order. When the purchase order of the buyer and the sales order of the seller agree, the orders become a contract between the buyer and seller.

Within an organization, the term order may be used to refer to a work order for manufacturing, a preventive maintenance order, or an order to make repairs to a facility.

In many businesses, orders are used to collect and report costs and revenues according to well-defined purposes. Then it is possible to show for what purposes costs have been incurred. **Spoken orders**

Businesses such as retail stores, restaurants and filling stations conduct business with their customers by accepting orders that are spoken or implied by the buyer's actions. Taking a shopping cart of merchandise to a check-out counter is an implied intent to buy the merchandise. Placing a take-out or eat-in order at a restaurant is a spoken purchase order. Putting gasoline in one's tank at a filling station is an implied order. The seller usually expects immediate payment by cash, check or credit card for these purchases, and the seller provides the buyer with a receipt for the payment. In legal terms, this form of business order is an "implied in fact contract".

Steps in commercial orders

In commerce, various business documents are used to record the negotiation of an agreement to buy and sell, record the agreement itself, and record compliance with the agreement and closure of the contract. An agreement to buy and sell is a form of contract.

There are five basic requirements for a contract to exist between two parties: agreement, voluntary, consideration, capacity, and legality. A sixth requirement of "in writing" sometimes applies.

The main concern for commercial orders is that there must be agreement (offer and acceptance) for the order to be a contract. Prior to this, businesses often record the details of negotiations by using a request for quotation, request for bid, sales quotation, or sales bid. Quotations are non-binding and part of the negotiation process. A request for bid can be binding or non-binding, depending on the terms of the bid.

Once an agreement or contract is in place, businesses record these as confirmed purchase orders and confirmed sales orders.

Commerce	Buyer's Action	Seller's Action
Buyer wanting the product and seller selling the product	Search for vendors (sellers) of the product	Marketing and advertising
Check product pricing, availability, specifications, delivery costs	Request for Quotation or Request for Bid	Sales quote or bid created
Buyer and seller agree to transaction	Purchase order recorded	Sales order recorded

Product is shipped from seller to buyer		Packing slip, *pro forma* invoice for certain international shipments
Buyer receives product from seller	Packing slip and product is checked with purchase order; product is checked for good condition	
Seller sends invoice to buyer	Match packing slip with purchase order and invoice; record purchase in financial accounts under accounts payable	Record sales order in financial accounts under accounts receivable
Buyer pays seller	Pay by cash, check or electronic payment; record payment on purchase order	Receive cash, check or electronic payment; record payment on sales order

Uniform Commercial Code

In the US, Article 2 of the Uniform Commercial Code covers commercial contracts, and section 2-103 gives definitions of terms under this code. Section 2-106 describes the difference between a present sale (recorded as a sales order) and asale (recorded as a transfer of title to the buyer).

(1) In this Article unless the context otherwise requires "contract" and "agreement" are limited to those relating to the present or future sale of goods. "Contract for sale" includes both a present sale of goods and a contract to sell goods at a future time. A "sale" consists in the passing of title from the seller to the buyer for a price (Section 2-401). A "present sale" means a sale which is accomplished by the making of the contract.

Aggregate level of orders

In their "Advance Monthly Sales for Retail Trade and Food Services", the US Census Bureau publishes estimates of US retail and food services sales. These "sales" are orders that have been filled; payment has been made or is an account receivable. In their "Preliminary Report on Manufacturers' Shipments, Inventories and Orders", the US Census Bureau publishes statistics for "new orders", shipments, "unfilled orders" and inventories for manufactured durable goods. This gives an indication whether trade is increasing or decreasing for manufactured durable goods in the US.

Order Receipt

An order receipt is a document that provides information about the details of an order and confirms it has been received by the company responsible for fulfilling it. It may come by email or fax confirmation, and sometimes arrives in the mail when the lead time on an order is considerable. It offers notice to the buyer about the specifics of the order and usually has information on how to cancel or change it, if necessary, often by using a return slip included with the receipt for convenience.

A typical order receipt should list the name and contact information for the shipper and seller, and specify the items in the order. It will include an estimated ship and delivery date, if appropriate, and the amount of the order, including tax, shipping, handling charges, and any other expenses. If the buyer finds an error, she can correct it before the order is actually filled, eliminating the need for a costly returns process where the goods go back to the shipper because a mistake was made.

Example

Confirm Receipt of an Order from a Customer

Dr. Mel Luthy, Chief Editor

Sample Letter #1

As you requested in our phone conversation this morning, I have notified our truck driver to pick up your old refrigerator when he delivers the new one that you purchased on Friday.

We will make our delivery in the early afternoon on Tuesday, March 5. The driver will call to confirm that someone will be home at that time. There is no extra charge for this pickup service.

[Senders Name]
[Address line 1]
[Address line 2]
[State, ZIP Code]

Sample Letter #1: Confirm receipt of an order from a customer

[Letter Date]

[Recipients Name]
[Address line 1]
[Address line 2]
[State, ZIP Code]

[Subject: Normally bold, summarizes the intention of the letter] -Optional-

Dear [Recipients Name],

I would like to inform you to expect the delivery of the items you purchased from our store on Monday, between 2:00 pm and 4:00 pm. We will also help you dispose of your old air-conditioning unit when we make the delivery. Please ensure that someone is home during this time to meet our delivery personnel, so that there will not be any unnecessary delays. Rest assured that there will be no additional charges for the pick up of your old unit. Thank you.

Sincerely,

[Senders Name]

[Senders Title] -Optional-

Procedures for 'negotiation of export documents'

Once your goods moved out of your factory, the Customs House Agents appointed by you complete customs formalities on behalf of you and delivers you necessary export shipping documents. Once customs formalities completed and obtained 'let export order' shipping bill, you hand over cargo to shipping line to carry your goodsProcedures for negotiation of export documents to final destination at buyer's place. Once after handing over cargo to shipping line, Bill of Lading is issued.

What are the precautions to be taken while submitting documents for negotiation with bank?

While negotiating documents, you submit all required documents as per letter of credit terms and conditions to bank to send to your overseas buyer though LC opening bank.

When shipment is under Letter of Credit, documentation is a crucial part as the opening bank debits you against any discrepancy found on documents. So once you received Letter of Credit, make a copy of the same and read carefully twice. Mark each and every point where ever necessary. Whether any international inspection required, clean on board bill of lading, factory inspection certificate, certificate of origin, legalized documents, consulate attestation, SGS,BVQI inspection, Phyto sanitary certificate, chemical analysis certificate, shipped on board certificate, freight certificate, etc.etc. List out the documents required to submit while negotiating bills. Go through each document minimum twice, whether each document is as per LC requirements. Make sure, all documents are there as per LC terms and not found any discrepancy in each of document. This is very important while submitting documents with bank to send to overseas buyer through buyer's bank.

Once after receipt of export documents, your bank arranges to negotiate bill as per Letter of credit terms and conditions after proper verification of each and every clause. If your export order is in US Dollar currency, you can either convert the amount in your currency or you can open a dollar account and transfer the amount accordingly.

LETTER OF CREDIT

After a contract is concluded between a buyer and a seller, the buyer's bank supplies a letter of credit to the seller. Seller consigns the goods to a carrier in exchange for a bill of lading.

Seller provides the bill of lading to bank in exchange for payment. Seller's bank then provides the bill to buyer's bank, which provides the bill to buyer.

Buyer provides the bill of lading to carrier and takes delivery of the goods.

A letter of credit is a document from a bank guaranteeing that a seller will receive payment in full as long as certain delivery conditions have been met.

In the event that the buyer is unable to make payment on the purchase, the bank will cover the outstanding amount. They are often used in international transactions to ensure that payment will be received where the buyer and seller may not know each other and are operating in different countries. In this case the seller is exposed to a number of risks such credit risk, and legal risk caused by the distance, differing laws and difficulty in knowing each party personally. A letter of credit provides the seller with a guarantee that they will get paid as long as certain delivery conditions have been met. For this reason the use of letters of credit has become a very important aspect of international trade.

The bank that writes the letter of credit will act on behalf of the buyer and make sure that all delivery conditions have been met before making the payment to the seller. Most letters of credit are governed by rules promulgated by the International Chamber of Commerce known as Uniform Customs and Practice for Documentary Credits. Letters of credit are typically used by importing and exporting companies particularly for large purchases and will often negate the need by the buyer to pay a deposit before delivery is made.

They are also used in land development to ensure that approved public facilities (streets, sidewalks, storm water ponds, etc.) will be built. The parties to a letter of credit are the supplier, usually called the "beneficiary", "the issuing bank", of whom the buyer is a client, and sometimes an advising bank, of whom the beneficiary is a client. Almost all letters of credit are irrevocable, i.e., cannot be amended or canceled without mutual consent of all parties.

Terminology

Origin

The name "letter of credit" derives from the French word "accréditation", a power to do something, which derives from the Latin "accreditivus", meaning trust.[citation needed]

Related terms

- A sight LC causes payment to be made immediately to the beneficiary/seller/exporter upon presentation of the correct documents. A time or date LC specifies when payment is to be made at a future date and upon presentation of the required documents
- Negotiation means the giving of value for draft(s) or document(s) by the bank authorized to negotiate, with the nominated bank. Mere examination of the documents and forwarding the same to the LC issuing bank for reimbursement, without giving of value / agreed to give, does not constitute a negotiation.
- Advising Bank — advises the beneficiary at the request of the issuing bank.
- Applicant — the party on whose request the issuing bank issues a credit.
- Banking day—The day on which a bank is regularly open at the place at which an act to be performed.

- Beneficiary — the party who is to receive the benefit (payment) of the LC. The consignee of an LC and the beneficiary may not be the same. The credit is issued in the beneficiary's favor.
- Presentation — either delivery of documents against an LC or the document itself.
- Complying presentation — when the presentation of documents is in accordance with:
  - The terms and conditions of the credit
  - The applicable provisions of UCP
  - International standard banking practice
- Confirmation — a definite undertaking from the confirming bank to honor or negotiate a complying presentation in addition to that of the issuing bank.
- Confirming bank — adds confirmation to an LC. It does so at the request of the issuing bank and taking authorization from the issuing bank.
- Letter of credit/credit — an irrevocable commitment of the issuing bank to honor a complying presentation.
- Honour — to act according to commitment of the LC. Presentations are honored in different ways depending on the type of credit:
  - Making payment at sight for sight LC.
  - Incurring a deferred payment undertaking and paying at maturity for deferred payment LC.
  - Accepting a draft drawn by the beneficiary and paying at maturity for deferred acceptance LC.
- Issuing bank — issues the LC.
- Nominated Bank — the bank with which credit is available. If no bank is mentioned in the credit as nominated bank, all banks are "nominated".
- Negotiation — A nominated bank is said to negotiate a document if it purchases a draft or documents under a complying presentation either by making an advance or agreeing to advance funds to the beneficiary on or before the date on which reimbursement is due to the nominated bank. A draft drawn on a nominated bank cannot be purchased separately.

Documents that can be presented for payment

To receive payment, an exporter or shipper must present the documents required by the LC. Typically, the payee presents a document proving the goods were sent instead of showing the actual goods. The original bill of lading (BOL) is normally the document accepted by banks as proof that goods have been shipped. However, the list and form of documents is open to negotiation and might contain requirements to present documents issued by a neutral third party evidencing the quality of the goods shipped, or their place of origin or place. Typical types of documents in such contracts include:

- Financial Documents — Bill of Exchange, co-accepted draft
- Commercial Documents — Invoice, packing list
- Shipping Documents — Transport document, insurance certificate, commercial, official or legal documents

- Official Documents — License, embassy legalization, origin certificate, inspection certificate, phytosanitary certificate
- Transport Documents — Bill of lading (ocean or multi-modal or charter party), airway bill, lorry/truck receipt, railway receipt, CMC other than mate receipt, forwarder cargo receipt
- Insurance documents — Insurance policy or certificate, but not a cover note.

Legal principles governing documentary credits

One of the primary peculiarities of the documentary credit is that the payment obligation is independent from the underlying contract of sale or any other contract in the transaction. Thus the bank's obligation is defined by the terms of the LC alone, and the sale contract is irrelevant. The defenses available to the buyer arising out of the sale contract do not concern the bank and in no way affect its liability. Article 4(a) of the UCP states this principle clearly. Article 5 of the UCP further states that banks deal with documents only, they are not concerned with the goods (facts). Accordingly, if the documents tendered by the beneficiary, or his or her agent, are in order, then in general the bank is obliged to pay without further qualifications.

The policies behind adopting the abstraction principle are purely commercial and reflect a party's expectations: first, if the responsibility for the validity of documents was thrown onto banks, they would be burdened with investigating the underlying facts of each transaction, and less inclined to issue documentary credits because of the risk and inconvenience.

Second, documents required under the LC could in certain circumstances be different from those required under the sale transaction. This would place banks in a dilemma in deciding which terms to follow if required to look behind the credit agreement.

Third, the fact that the basic function of the credit is to provide a seller with the certainty of payment for documentary duties suggests that banks should honor their obligation notwithstanding allegations of buyer misfeasance. Courts have emphasized that buyers always have a remedy for an action upon the contract of sale and that it would be a calamity for the business world if a bank had to investigate every breach of contract.

The "principle of strict compliance" also aims to make the bank's duty of effecting payment against documents easy, efficient and quick. Hence, if the documents tendered under the credit deviate from the language of the credit the bank is entitled to withhold payment, even if the deviation is purely terminological. The general legal maxim de minimis non curat lex has no place in the field.

Types

- Import/export — The same credit can be termed an import or export LC[4] depending on whose perspective is considered. For the importer it is termed an Import LC and for the exporter of goods, an Export LC.
- Revocable — The buyer and the bank that established the LC are able to manipulate the LC or make corrections without informing or getting permissions from the seller. According to UCP 600, all LCs are irrevocable, hence this type of LC is obsolete.

- Irrevocable — Any changes (amendment) or cancellation of the LC (except it is expired) is done by the applicant through the issuing bank. It must be authenticated and approved by the beneficiary.
- Confirmed — An LC is said to be confirmed when a second bank adds its confirmation (or guarantee) to honor a complying presentation at the request or authorization of the issuing bank.
- Unconfirmed — This type does not acquire the other bank's confirmation.
- Transferrable — The exporter has the right to make the credit available to one or more subsequent beneficiaries. Credits are made transferable when the original beneficiary is a middleman and does not supply the merchandise, but procures goods from suppliers and arranges them to be sent to the buyer and does not want the buyer and supplier know each other.

The middleman is entitled to substitute his own invoice for the supplier's and acquire the difference as profit.

A letter of credit can be transferred to the second beneficiary at the request of the first beneficiary only if it expressly states that the letter of credit is "transferable". A bank is not obligated to transfer a credit.

A transferable letter of credit can be transferred to more than one alternate beneficiary as long as it allows partial shipments.

The terms and conditions of the original credit must be replicated exactly in the transferred credit. However, to keep the workability of the transferable letter of credit, some figures can be reduced or curtailed.

i. Amount
ii. Unit price of the merchandise (if stated)
iii. Expiry date
iv. Presentation period
v. Latest shipment date or given period for shipment.

The first beneficiary may demand from the transferring bank to substitute for the applicant. However, if a document other than the invoice must be issued in a way to show the applicant's name, in such a case that requirement must indicate that in the transferred credit it will be free.

Transferred credit cannot be transferred again to a third beneficiary at the request of the second beneficiary.

- Untransferable — A credit that the seller cannot assign all or part of to another party. In international commerce, all credits are untransferable.
- Deferred / Usance — A credit that is not paid/assigned immediately after presentation, but after an indicated period that is accepted by both buyer and seller. Typically, seller allows buyer to pay the required money after taking the related goods and selling them.
- At Sight — A credit that the announcer bank immediately pays after inspecting the carriage documents from the seller.
- Red Clause — Before sending the products, seller can take the pre-paid part of the money from the bank. The first part of the credit is to attract the attention of the accepting bank. The first time the credit

is established by the assigner bank, is to gain the attention of the offered bank. The terms and conditions were typically written in red ink, thus the name.

- Back to Back — A pair of LCs in which one is to the benefit of a seller who is not able to provide the corresponding goods for unspecified reasons. In that event, a second credit is opened for another seller to provide the desired goods. Back-to-back is issued to facilitate intermediary trade. Intermediate companies such as trading houses are sometimes required to open LCs for a supplier and receive Export LCs from buyer.

Pricing

Issuance charges, covering negotiation, reimbursements and other charges are paid by the applicant or as per the terms and conditions of the LC.

If the LC does not specify charges, they are paid by the Applicant. Charge-related terms are indicated in field 71B.

Legal basis

Legal writers have failed to satisfactorily reconcile the bank's undertaking with any contractual analysis. The theories include: the implied promise, assignment theory, the novation theory, reliance theory, agency theories, estoppels and trust theories, anticipatory theory and the guarantee theory.

Although documentary credits are enforceable once communicated to the beneficiary, it is difficult to show any consideration given by the beneficiary to the banker prior to the tender of documents. In such transactions the undertaking by the beneficiary to deliver the goods to the applicant is not sufficient consideration for the bank's promise because the contract of sale is made before the issuance of the credit, thus consideration in these circumstances is past. However, the performance of an existing duty under a contract may be a valid consideration for a new promise made by the bank, provided that there is some practical benefit to the bank A promise to perform owed to a third party may also constitute a valid consideration.

Another theory asserts that it is feasible to typify letter of credit as a collateral contract for a third-party beneficiary because three different entities participate in the transaction: the seller, the buyer, and the banker. Because letters of credit are prompted by the buyer's necessity and in application of the theory of Jean Domat the cause of a LC is to release the buyer of his obligation to pay directly to the seller. Therefore, a LC theoretically fits as a collateral contract accepted by conduct or in other words, an implied-in-fact contract under the framework for third party beneficiary where the buyer participates as the third party beneficiary with the bank acting as the stipulator and the seller as the promisor. The term "beneficiary" is not used properly in the scheme of an LC because a beneficiary (also, in trust law, cestui que use) in the broadest sense is a natural person or other legal entity who receives money or other benefits from a benefactor. Note that under the scheme of letters of credit, banks are neither benefactors of sellers nor benefactors of buyers and the seller receives no money in gratuity mode. Thus is possible that a "letter of credit" was one of those contracts that needed to be masked to disguise the "consideration or Privity requirement". As a result this kind of arrangement, would make letter of credit to be enforceable under the action assumpsit because of its promissory connotation.

A few countries, including the United States (Article 5 of the Uniform Commercial Code) have created statutes in relation to letters of credit. These statutes are designed to work with the rules of practice including UCP and ISP98. These rules of practice are incorporated into the transaction by agreement of the parties. The latest version of the UCP is the UCP600 effective July 1, 2007. Since the UCP are not laws, parties have to include them into their arrangements as normal contractual provisions.

International Trade Payment methods

International Trade Payment method can be done in the following ways.

- Advance payment (most secure for seller) — the buyer parts with money first and waits for the seller to forward the goods.
- Documentary Credit (more secure for seller as well as buyer) — Subject to ICC's UCP 600, the bank gives an undertaking (on behalf of buyer and at the request of applicant) to pay the beneficiary the value of the goods shipped if acceptable documents are submitted and if the stipulated terms and conditions are strictly complied with. The buyer can be confident that the goods he is expecting only will be received since it will be evidenced in the form of certain documents called for meeting the specified terms and conditions while the supplier can be confident that if he meets the stipulations his payment for the shipment is guaranteed by bank, who is independent of the parties to the contract.
- Documentary collection (more secure for buyer and to a certain extent to seller) — Also called "Cash Against Documents". Subject to ICC's URC 525, sight and usance, for delivery of shipping documents against payment or acceptances of draft, where shipment happens first, then the title documents are sent to the buyer's bank by seller's bank, for delivering documents against collection of payment/acceptance
- Direct payment (most secure for buyer) — The supplier ships the goods and waits for the buyer to remit the bill, on open account terms.

Risk situations

Fraud Risks

- The payment will be obtained for nonexistent or worthless merchandise against presentation by the beneficiary of forged or falsified documents.
- Credit itself may be funded.

Sovereign and Regulatory Risks

- Performance of the Documentary Credit may be prevented by government action outside the control of the parties.

Legal Risks

- Possibility that performance of a documentary credit may be disturbed by legal action relating directly to the parties and their rights and obligations under the documentary credit.

Force Majeure and Frustration of Contract

- Performance of a contract – including an obligation under a documentary credit relationship – is prevented by external factors such as natural disasters or armed conflicts.

Applicant

- Non-delivery of Goods
- Short shipment
- Inferior quality
- Early / late shipment
- Damaged in transit
- Foreign exchange
- Failure of bank viz issuing bank / collecting bank

Issuing Bank

- Insolvency of the applicant
- Fraud risk, sovereign and regulatory risk and legal risks

Reimbursing Bank

- No obligation to reimburse the claiming bank unless it has issued a reimbursement undertaking.

Beneficiary

- Failure to comply with credit conditions
- Failure of, or delays in payment from, the issuing bank

EXPORT DOCUMENTS

Documents required for an international sale can vary significantly from transaction to transaction, depending on the destination and the product being shipped. At a minimum, there will be two documents: the invoice and the transport document. The buyer will usually provide the seller with a list of documents needed to get the goods into his country as expeditiously and inexpensively as possible. Some documentary requirements are not open to negotiation, as they are needed by the importer to clear customs at the port of destination. This presentation discusses documentation in relation to export letters of credit.

When the letter of credit payment method is used for an export sale, each document presented under the terms and conditions of the letter of credit must:

1) Conform to all L/C terms and conditions.
2) Comply with the UCP 500.
3) Agree with the data content of every other document.

For the following documents listed, the number in parenthesis refers to the relevant UCP 500 article.

THE BILL OF EXCHANGE / DRAFT (UCP Article 9)

Almost every letter of credit presentation and documentary collection is accompanied by a draft. This demand for payment is drawn by the seller on the payee. The payee on a letter of credit draft is almost always a bank. For a documentary collection it would be the buyer.

COMMERCIAL INVOICE (UCP Article 37)

The accounting document claiming payment from the buyer, normally an export invoice would include:

- Seller’s name and address
- Buyer’s name and address
- Issue Date
- Invoice Number
- Shipping marks and numbers
- Term of Sale: e.g. FOB, etc.
- Shipping information
- Info required by L/C
- Country of Origin
- L/C number
- Merchandise description, P.O. number, unit price, and total price

CONSULAR INVOICE / VISAED INVOICE (UCP Articles 20, 21)

For exchange control and balance of payments reasons, some countries do not allow the import of merchandise unless accompanied by a certificate issued by one of its officials in the exporter’s country. These certificates evidence that the shipment meets certain statutory or other regulations of the importing country. A visaed invoice is an original or copy of an invoice, which has been originally signed and/or stamped by a consulate official.

INSURANCE POLICY OR CERTIFICATE (UCP Article 34, 35, 36)

Every export sale should be covered by insurance. Who provides the coverage depends on the INCOTERM used. Insurance coverage on exports is a complicated issue that we cannot fully cover on this site. For more information on export insurance, we suggest that you contact your business insurance agent or freight forwarder as to who can provide insurance on an as Needed Basis” Or “By Blanket Policy” On An Annual Basis.

Certificates

When a letter of credit calls for a document to be issued as a “certificate”, that document must be signed. Certificates come in a many different forms depending on the product and the country of destination. L/C’s often require that certificates be issued by reputable third party inspection surveyors such as the Societe Generale de Surveillance (SGS) or the US Department of Agriculture. It is important to remember that each certificate required by an L/C will increase the cost of goods sold. Some of the most common certificates are discussed below.

Certificates should always be issued before the goods are shipped. Certificates issued after the goods arrived in the country of import defeat the purpose of the letter of credit.

Certificate of Origin (UCP Articles 20, 21)

A Signed Statement Certifying the Country of origin of the goods being sold is sometimes required by regulation in the buyer’s country. This document may be as simple as a certificate signed by the seller. Certain countries may require it to be issued by a third party such a Chamber of Commerce, or be notarized, legalized, or visaed by their Embassy or Consulate.

Inspection Certificate (UCP Articles 20, 21)

An independent firm would usually conduct the inspection to ensure that the merchandise conforms to the buyer's criteria. Inspection certificates should be based on quantifiable criteria.

When an L/C is the method of payment, the criteria should be specifically spelled out in the letter of credit.

Weight List or Certificate (UCP Articles 38, 20, 21)

Not synonymous to a packing list. This document breaks down the shipment by weight. This is generally needed only if a "certificate" is required.

USDA Inspection Certificate (UCP Articles 20, 21)

This certificate is issued by the US Department of Agriculture and covers grade and condition for agricultural products. It provides evidence that the produce was in good condition at the date and time of inspection and can be useful in the event of a damage claim.

Phytosanitary Certificate (UCP Articles 20, 21)

Numerous foreign governments and buyers require a "phyto" for fresh plants and plant products. This certificate states that the product has been inspected and is free of harmful pests and plant diseases. They are issued by the USDA Animal and Plant Health Inspection Service.

Packing List (UCP Articles 20, 21)

A mirror of the merchandise covered by the invoice, the packing list omit prices, but itemizes the merchandise by number of cartons, packages, etc., and the contents of each. It generally does not have to be signed unless called for in the L/C.

Other Miscellaneous Documents (Ucp Articles 20, 21)

- Ucp 500 article 21: "when documents other than
- Transport documents, insurance documents and
- Commercial invoices are called for, the credit
- Should stipulate by whom such documents are to be
- Issued and their wording or data content. If the
- Credit does not so stipulate, banks will accept
- Such documents as presented, provided that their
- Data is not inconsistent with any other stipulated
- Document presented."

Selected references to documents in the UCP 500

Document topic UCP 500 articles

- Authentication requirements - UCP 20
- Copies of - UCP 20

- Conforming - UCP 14
- Content of - UCP 21
- Documents v. Goods/ Services/ Performance - UCP 4
- Dated prior to L/C issuance - UCP 22
- Discrepancies - UCP 14
- Examination - UCP 13
- Fraudulent Documents - UCP 15
- Issuer, ambiguity about - UCP 20
- Lost Documents - UCP 16
- Non-stipulated Documents - UCP 13
- Originals - UCP 20
- Required Documents - UCP 5
- Signature on - UCP 20
- Stale Documents - UCP 43

Export Incentives

The Government of India has framed several schemes to promote exports and to obtain foreign exchange. These schemes grants incentive and other benefits. The few important export incentives, from the point of view of indirect taxes are briefed below:

Free Trade Zones (FTZ)

Several FTZs have been established at various places in India like Kandla, Noida, Cochin, etc. No excise duties are payable on goods manufactured in these zones provided they are made for export purpose. Goods being brought in these zones from different parts of the country are brought without the payment of any excise duty. Moreover, no customs duties are payable on imported raw material and components used in the manufacture of such goods being exported. If entire production is not sold outside the country, the unit has the provision of selling 25% of their production in India. On such sale, the excise duty is payable at 50% of basic plus additional customs or normal excise duty payable if the goods were produced elsewhere in India, whichever is higher.

Electronic Hardware Technology Park / Software Technology Parks

This scheme is just like FTZ scheme, but it is restricted to units in the electronics and computer hardware and software sector.

Advance Licence / Duty Exemption Entitlement Scheme (DEEC)

In this scheme advance licence, either quantity based (Qbal) or value based (Vabal), is given to an exporter against which the raw materials and other components may be imported without payment of customs duty provided the manufactured goods are exported. These licences are transferable in the open market at a price.

Export Promotion Capital Goods Scheme (EPCG)

According to this scheme, a domestic manufacturer can import machinery and plant without paying customs duty or settling at a concessional rate of customs duty. But his undertakings should be as mentioned below:

Customs Duty Rate, Export Obligation and Time

- 10%, 4 times exports (on FOB basis) of CIF value of machinery and 5 years
- Nil in case CIF value is Rs200mn or more, 6 times exports (on FOB basis) of CIF value of machinery or 5 times exports on (NFE) basis of CIF value of machinery and 8 years
- Nil in case CIF value is Rs50mn or more for agriculture, aquaculture, animal husbandry, floriculture, horticulture, poultry and sericulture, 6 times exports (on FOB basis) of CIF value of machinery or 5 times exports on (NFE) basis of CIF value of machinery and 8 years

Note:-

- NFE stands for net foreign earnings.
- CIF stands for cost plus insurance plus freight cost of the machinery.
- FOB stands for Free on Board i.e. export value excluding cost of freight and insurance.

Deemed Exports

The Indian suppliers are entitled for the following benefits in respect of deemed exports:

- Refund of excise duty paid on final products
- Duty drawback
- Imports under DEEC scheme
- Special import licenses based on value of deemed exports
- The following categories are treated as deemed exports for seller if the goods are manufactured in India:
- Supply of goods against duty free licences under DEEC scheme
- Supply of goods to a 100 % EOU or a unit in a free trade zone or a unit in a software technology park or a unit in a hardware technology park
- Supply of goods to holders of licence under the EPCG scheme
- Supply of goods to projects financed by multilateral or bilateral agencies or funds notified by the Finance Ministry under international competitive bidding or under limited tender systems in accordance with the procedures of those agencies or funds where legal agreements provide for tender evaluation without including customs duty
- Supply of capital goods and spares upto 10% of the FOR value to fertilizer plants under international competitive bidding
- Supply of goods to any project or purpose in respect of which the Ministry of Finance permits by notification the import of goods at zero customs duty along with benefits of deemed exports to domestic supplies

- Supply of goods to power, oil and gas sectors in respect of which the Ministry of Finance permits by notification benefits of deemed exports to domestic supplies

Manufacture Under Bond

This scheme furnishes a bond with the manufacturer of adequate amount to undertake the export of his production. Against this the manufacturer is allowed to import goods without paying any customs duty, even if he obtain it from the domestic market without excise duty. The production is made under the supervision of customs or excise authority.

Duty Drawback

It means the rebate of duty chargeable on imported material or excisable material used in the manufacturing of goods in and is exported. The exporter may claim drawback or refund of excise and customs duties being paid by his suppliers. The final exporter can claim the drawback on material used for the manufacture of export products. In case of re-import of goods the drawback can be claimed.

The following are Drawbacks:

- Customs paid on imported inputs plus excise duty paid on indigenous imports.
- Duty paid on packing material.

Drawback is not allowed on inputs obtained without payment of customs or excise duty. In part payment of customs and excise duty, rebate or refund can be claimed only on the paid part.

In case of re-export of goods, it should be done within 2 years from the date of payment of duty when they were imported. 98% of the duty is allowable as drawback, only after inspection. If the goods imported are used before its re-export, the drawback will be allowed as at reduced percent.

India extends export benefits to rupee trade with Iran

"Export proceeds against exports to Iran realised in Indian rupees are permitted to avail exports benefits/ incentives under the Foreign Trade Policy, 2009-14, at par with export proceeds realised in freely convertible currency," the Director general of Foreign Trade (DGFT) has said in a notification.

Indian exporters mainly trade in freely convertible currencies including US dollar and euro. The government provides export incentives under different schemes, including Focus Market Scheme, to exporters realising their proceeds in such currencies.

Iran makes payment in rupees to Indian exporters after the Western countries imposed sanctions on it.

To increase bilateral trade, the government in April had also waived the value addition norms for exporters shipping imported items like food and pharmaceuticals to Iran.

Besides food products, India mainly exports to Iran pharmaceuticals, machinery, transport equipment, chemicals, man-made yarns and fabrics and steel. The bilateral trade between the two countries stood at $15.25 billion in 2013-14.

India is one of the biggest oil importers from Iran. Since February 2013, when the US blocked payment channels to Iran for its nuclear programme, India has been paying 45 per cent of its Iran oil bill in rupees through a UCO Bank branch in Kolkata.

India has steadily cut imports from Iran as the sanctions from US and other Western countries blocked payment channels and crippled shipping routes.

It imported 21.20 million tonnes of crude oil from Iran in 2009--10, which came down to 18.50 million tonnes in 2010--11 and 18.11 million tonnes in 2011--12.

Crude oil imports from Iran were reduced to 13.14 million tonnes in 2012--13, the year when the US had tightened screws on Iran.

PROCEDURES AND DOCUMENTATION FOR AVAILING EXPORT INCENTIVES

Exports are given priority in India and enjoy lot of incentives. However, the major problem lies in the process of realizing them. Unfortunately, exporters have to approach multiple organizations for seeking sanction. Each organization prescribes its own exclusive method of documentation as well as procedure form the stage of submission of claim till sanction. The documentation and procedures are diverse with each incentive provided. This is not the end of their problems. Incentives are available at post-shipment stage but they are connected with the documents generated at the time of shipment. If exporter does not pay adequate care and attention at the time and stage of export shipment in providing complete and adequate information in the documents in a proper way, their claims for export incentives are adversely affected. It is essential to the exporters to plan carefully in respect of incentives, even at the time of shipment, though their benefits are available only after completion of the shipment.

In the absence of adequate planning, it will upset their fund flow and equally the total realization may not be remunerative for effecting exports. Exporters have to draw a suitable plan of action for claiming incentives in a timely manner to avoid delays and cuts in realization. Exporters have to understand the different procedural formalities, connected with multiple and diverse agencies. This would ensure proper compliance for availing of full benefit of incentives. In this area, Government has to rationalize the incentives by opening a single window approach for sanction of multiple claims.

TYPES OF INCENTIVES

Government of India has been endeavoring to develop exports through various financial and non-financial assistance and fiscal incentives to the exporters. They are divided in two categories. They are:

- Incentive Linked to Export performance
    - (a) Duty Drawback (DBK)
    - (b) Excise Duty – Refund/Exemption
    - (c) Duty Free Replenishment Certificate
    - (d) Duty Entitlement Pass Book Scheme
- Duty Exemption Scheme

Advance License

- Fiscal Incentives

  (a) Sales Tax Exemption

  (b) Income Tax Exemption

- Claim for Rail Freight Rebate
- Claim for Air Freight Assistance

DOCUMENTATION AND PROCEDURE FOR CLAIMING INCENTIVES

- The procedure for claiming these incentives is different for different incentives.
- Duty Drawback (DBK)

PROCEDURES AND DOCUMENTATION FOR AVAILING EXPORT INCENTIVES

The duty drawback refers to the refund in respect of Central Excise and Customs Duties paid in respect of raw materials and other inputs used in the manufacture of the product, prior to export.

Whom to Apply: The customs house in whose jurisdiction the exporter's factory or warehouse is situated.

When to Apply: An exporters is entitled to claim the duty drawback as soon as the export of goods is completed. Delivery of goods at the port of destination is not essential. Export' for the purpose of claiming duty drawback is evidenced by "Let Export Order". Claim application is to be submitted with in a period of three months from the date of "Let Export Order", issued by the Customs Officer. The exporter can seek extension of period for submission of claim. The Assistant Commissioner can grant extension for a period of three months, if he is satisfied that the exporter is prevented from submitting the application.

When Samples are Drawn: In case, any sample has been drawn from the shipment of goods to determine the contents of the basic materials for fixation of drawback, the sample report is be given to the exporter within a period of one month from the date of taking the sample. This report is to be submitted along with other relevant documents for submitting the claim. Delay in giving the report will be added to the period allowed for submission i.e. three months period. For example, if the sample report is given after one month and twenty-five days, the exporter can submit the claim within three months and twenty-five days, in addition to the discretionary extension period of three months.

Drawback Rates:

The Government of India announces the rates of duty drawback every year on 31st May, product wise in the drawback schedule. Generally, the rates are expressed as a percentage of the FOB value of the goods exported. All such rates are called All Industry Rates. The rates are made effective from 1st June of every year. In case, duty drawback rate is not announced for a particular product, the manufacturer/exporter is known as Brand Rate. In case, the rate of duty drawback is less than 80% of the duties paid, the exporter can submit an application for suitable upward revision. This is known as Special Brand Rate. The application is to be submitted to Directorate of Duty Drawback Ministry of Finance.

When Duty Drawback not Admissible: Duty drawback is admissible for the export of all the notified products. However, in the following cases, it is not admissible:

(a) No excise/customs duty is paid for the manufacture of export product
(b) Amount of drawback is less than 1% of the FOB value of the goods. However, if the amount of drawback is more than Rs.500, it can be claimed
(c) If the export proceeds are not realized within six months
(d) If the amount of foreign exchange spent on the inputs used for the export is more than the foreign exchange value of the exports. In other words, value addition is negative
(e) Cenvat Credit is availed of

How to File Claim:

The procedure for claiming duty drawback depends upon whether the processing of shipping documents has been computerized or not. The exporter is not required to file any separate application for claiming duty drawback, if the processing of documents has been computerized at the jurisdiction customs station. Where processing has not been computerized, separate application is to be submitted for claiming duty drawback. Triplicate copy of the shipping bill becomes the application only after the Export General Manifest is filed.

Documents to be submitted: The following documents are to be submitted to the Directorate of Duty Drawback:

(a) Triplicate copy of the Shipping Bill
(b) Copy of bank attested invoice
(c) Copy of Packing List
(d) Copy of Bill of Lading/ Airway Bill
(e) Copy of ARE-1 form, where applicable
(f) Insurance Certificate, where necessary
(g) Copy of the Test Report, where required
(h) Copy of communication regarding Special Brand Rate fixation
(i) Copy of the export contract or letter of credit as the case may be
(j) Pre-receipt for drawback claim

How Claim Amount is paid:

The Customs House that has the jurisdiction over the port or airport through which exports are affected makes the payment.

How Delay in Payment of Claim is avoided:

When the claim application along with complete set of documents is submitted, an acknowledgement in the prescribed form is issued to the exporter within 15 days from the date of filing the claim. The duty drawback is to be paid to the exporter within a period of two months from the date of acknowledgment. In case of delay, interest @15% per annum is paid for the period of default. Due to compulsory interest provision, normally, claims are settled in time.

PRE-SHIPMENT INSPECTION

This article needs additional citations for verification. Please help improve this article by adding citations to reliable sources. Unsourced material may be challenged and removed. (September 2011)

Pre-shipment inspection, also called preshipment inspection or PSI, is a part of supply chain management and an important and reliable quality control method for checking goods' quality while clients buy from the suppliers.

It ensures that the production complies with your specifications and/or the terms of your purchase order or letter of credit. The Final Random Inspection (FRI), or Pre Shipment Inspection (PSI), checks finished products when at least 80% of your order has been produced and export-packed. Samples are selected at random, according to standards and procedures. This way the buyer makes sure, he gets the goods he paid for.

Although increasing numbers of clients would like to collect suppliers' information from the Internet, this contains high risks because it is not a face-to-face transaction, and Internet phishing and fraud can corrupt it. Pre-shipment inspection can greatly avoid this risk and ensure clients get quality products from suppliers.

Process

The pre-shipment inspection is normally agreed between a buyer, a supplier, and a bank, and it can be used to initiate payment for a letter of credit. A PSI can be performed at different stages:

- Checking the total amount of goods and packing
- Controlling the quality and/or consistency of goods
- Checking of all documentation, including test reports and packaging list
- Verifying compliance with the standards of the destination country (e.g. ASME or CE mark)

The first stage is often performed by the transport company, but for the latter two stages a proper inspection company is needed. Similarly, if between the buyer and seller money transfer via a letter of credit is agreed upon, it is necessary to assign a reputable inspection company. In case of the letter of credit, after inspection of the goods, an inspection certificate is sent to the bank issuing the letter of credit and the buyer, initiating the money transfer.

46.A is a clause in the Letter of Credit (LC), that expresses the required documents that shall be provided to the bank by the seller. It is mandatory for any fund transfer. So, one of the subjects that can be expressed in 46.A clause is: "The original inspection certificate shall be issued by independent third party pre-shipment inspection company not sooner than the bill of lading date and the inspection shall be done by "the name of inspection agency" and certifying that: "The quality, quantity, and the packing of the goods dispatched are strongly conforming with provisions of the goods stated in the associated proforma invoice (PI), the terms of Letter of Credit and any attachments built thereto as submitted to "name of third party pre-shipment inspection agency" by the buyer".

The clause 46.A expresses lots of documents that shall be provided to the bank to initiate payment. The certificate of inspection is simply one of them. The statement quoted above must be written exactly like this within the certificate of Inspection. Even if the original document (Letter of Credit) contains a spelling error, it shall be written in the same form. Any change in this wording will be disapproved by the bank and the funds will not be transferred to the seller.

The inspection agency will submit an inspection certificate once the manufacturer/seller submit them with the following documents: Certificate of Origin (COO) and Packing List (PL). Based on above listed documents; altogether, they will issue a certificate and submit it to the manufacturer/seller. Finally, the manufacturer/seller will collect all mentioned documents and present them to the bank in order to initiate the payment.

Inspection companies are classified in two classes:

- **Free-market companies:** These are privately owned companies, which sell their services to the market. Danger with these might be, especially if it is a smaller company that they might be paid as well by the manufacturer, thus working in his interest.
- **State owned inspection companies**: Only very few companies operating on the market are state-owned or partly state-owned. The shareholding of governmental institutions guarantees the independence and objectivity.

A higher form of the PSI is called expediting; in this the dates of delivery and the production are controlled as well. Some countries, like Botswana, require PSIs for all goods entering the country in order to fight corruption. In these cases the PSI must be performed by the company designated by the country.

PSI and corruption charges

The World Bank recommends pre-shipment inspections (PSI) as a means to fight corruption especially in developing countries. Most known is the payment to the then husband of Pakistani president Benazir Bhutto, Asif Ali Zardari. Further irregularities were published about the contracts with Paraguay and the Philippines.

1. INTRODUCTION

1.1

INTRODUCTION TO THE INDUSTRY

The Indian Textile Industry is one of the largest in the world with a massive raw material andtextile manufacturing base. Our economy is largely dependent on the textile manufacturing and tradein addition to other major industries. About 27% of the foreign exchange earnings are on account of export of textiles and clothing alone. The textiles and clothing sector contributes about 14% to theindustrial production and 3% to the gross domestic product [GDP] of the country Around 8% of the total excise revenue collection is contributed by the textile industry. So muchso, the textile industry accounts for as large as 21% of the total employment generated in theeconomy. Around 35million people are directly employed in the textile manufacturing activities.Indirect employment including the manpower engaged in agricultural based raw-material productionlike cotton and related trade and handling could be stated to be around another 60million.Indian textile industry is constituted of the following segments: Readymade Garments, CottonTextiles including Handlooms, Man-made Textiles, Silk Textiles, Woollens Textiles, Handicrafts,Coir, and Jute. The Apparel Export Promotion Council [AEPC] represents over 8000 small, medium,and large exporters. The country ranks sixth among the top garment exporting countries globally. Nearly 78% of garments are exported from India are cotton-based. The main products are ladies garments, blouses, skirts, T-Shirts and trousers.

INDIAN EXPORT AND IMPORT SCENARIO (2009)

Indian textile trade has undergone massive restructuring following the 1991 liberalization policies. Indian textile exports fell from $200.9 billion in 2008 to $165 billion in 2009. India wasranked 22nd in the world in terms of textile export volume. The graph below shows the countries whohave contributed to the total volume of textile exports;

Figure 1.1.1 Indian Textile Export Partners, 2009

During this period, the growth rate was recorded as 18.11% and the bigger surprise was that theimport sector had experienced a growth rate of 34.30%. India was ranked 15

th

in the world in terms of import volume. The graph below shows the countries who have contributed to the total volume of textile imports;

Figure 1.1.2 Indian Textile Import Partners, 2009

OUTLOOK FOR INDIAN TEXTILE INDUSTRY

The outlook for textile industry in India is very optimistic. It is expected that Indian textileindustry would continue to grow at an impressive rate. Textile industry is being modernized by anexclusive scheme, which has set aside $5bn for investment in improvisation of machinery. India canalso grab opportunities in the export market. The textile industry is anticipated to generate 12mn new jobs in various sectors.

TECHNOLOGY IN TEXTILE INDUSTRY

Textile technology, once considered a handicraft, has become a highly sophisticated,scientific and engineering activity of new types of fibres and technologies. The field encompassesdifferent areas of engineering such as mechanical, electrical, computer, chemical, instrumentation,electronic and structural engineering. Apparel and fashion technology, a part of textile technology has become an important activity for the designing, fashioning and marketing of garments. All thisrequires knowledge of latest technology and the present day textile-design students are poised to takeup the challenge

VISION OF INDIA 2010 FOR TEXTILES

•

Textile economy to grow to $85billion by 2010

•

Creation of 12 million new jobs in textile sector.

•

To increase India’s share in world trade to six per cent by 2010.

•

Achieve export value of $40 billion by 2010.

•

Modernization and consolidation for creating a globally competitive industry.

1.1

INTRODUCTION TO THE COMPANY 1.1.1About the company

•

Set up as an SSI unit in the year 1992 with a minimum investment of Rs.1 Cr.Currently having a net worth of Rs.7 Cr

•

Purely an Export Oriented Unit [EOU]

•

It is a Partnership firm promoted by Mrs. & Mr.Duraisamy with an equal share in thecompany

•

Located 13kms from the knit city Tirupur and 35kms away from the airport.

•

Well equipped with modern machines occupying an area of 25,000 sq. feet

•

Manufacturer and Exporter of knitted garments to top end customers in theInternational Market.

•

Produces styles for kid's, children, ladies' and men's outer wears, night wears andsports wears

•

Specialized in mercerized knitted fabric garments

•

It employs about 120 people including contract labour

•

Equipped with modern high-speed sewing machines, picoting & zig zag machines, button hole & button stitch machines, Vacuum Steam Iron Tables, Stain removers andFusing machines and others which serve the purpose of completion of an order

Lead Time of 1,25,000 pieces in a month of the basic styles

•

It has a separate in-house stitching unit under the name of Sree Jayram Exports whichis now concentrating on the domestic sale of knitted garments

•

Imports raw material, knitted processed fabric from overseas, adds value to it andexports the same

1.1.1

Vision

"The vision of the Company is to become a leading manufacturer and exporter of apparel

bycontinuously excelling in Quality, Service and Customer Satisfaction using the best technology, processes and people".

1.1.2Mission

“To become the most preferred one-stop source for ready-made garments & ready to cutfabrics”“To constantly update the technology and skill sets t`o cater to the ever changing needs of theapparel & textile industry”.

1.1.3Quality Policy

The company is committed to achieve total customer satisfaction by producing superior products at competitive price and timely delivery with total involvement and excellence.

1.1.4Details of PON SANGER EXPORTS

4

•

IEC Code Number : 3293006876

(See Annexure 1)

•

AEPC Registration Number : 202640

(See Annexure 2)

1.1.1ORGANISATION CHART

Figure 1.2.1 Organisation Structure of PON SANGER EXPORTS

5PONN SANGERGeneral ManagerFactory Manager

Merchandiser

Manager(Rawmaterials &StoresDepartmentFinishedWarehouse InIn-houseQuality

ManagingPartneCommunicationMarketingDevelopmentExport ManagerAccounts

Production Manager

1.1.1

Ponn Sanger Overseas Buyers and Suppliers’ share

Their high profile customers are not only happy but also satisfied whichhas earned them recognition and unflattering loyalty from prominent buyersoverseas.

Fig.1.2.2 Overseas Buyers of the firm

Overseas Buyers:

•

SWC , USA

•

Design In Motion , USA

•

Henrich Opermayer , Germany

•

GMBH , Germany

Fig.1.2.3 Overseas Suppliers of the firm

Overseas Suppliers:

•

Taiwan and China are the mainPlayers of imports here

6

•

Sampling incharge

•

PatternMaster

•

Cutting Incharge

•

Time Officer

•

LineInspector

•

Supervisorscheckin

•

Upon the request of the specificBuyer, Ponn Sanger imports theRaw material, the fabric

•

Kind not manufactured in home Country

•

Disclosure of certain sensitive information, e.g. the commissions for the Post-Shipmentformalities

•

Formalities at both the stages of shipment are subject to change by the home or foreignCountry’s norms

2. REVIEW OF LITERATURE

Review of literature shows the previous studies carried out by the researcher in this field inorder to gain insight into extent of research. The research problem can be more understood and madespecific referring to theories, reports, records and other information made in similar studies. This will

provide the researcher with the knowledge on what lines the study should proceed and serves tonarrow the problem.

Thomas A. Cook (1994)

1

says, “One of the major pitfalls in an international sale is the quality of thedocumentation supporting the transaction. A mistake in spelling, execution, language or number of copies will cause substantial delays in obtaining clearance and require additional expenditures tocomplete the process.”Many potential exporters shy away from exporting due to the fear of the potential headachescaused by export documentation. In reality, while the process is complicated and has a steep learningcurve, with the right approach and support from several resources the process can be simplified andthe inherent obstacles lifted.Most of the necessary documents required for an export transaction are the invoice, packinglist, export declaration and the bill of lading. Other documents that may be required include: paymentinstruments (letters of credit, sight drafts), health/sanitary certificates, certificates of origin,export/import licenses, SGS inspection certificates, carnets (customs passes), certificates of insuranceand required import documents.In addition to knowing the specific documents, the exporter will need to know language, thenumber of copies, required signatories, format, notarization, consularization, and the shippinginstructions.”

Laurel Delaney(2006)

,

describesAES Direct,a free online process for filing Shipper's ExportDeclarations. AES stands for Automated Export System. Here are some highlights:

1.

Ensures export compliance

- It returns a confirmation number to verify that you successfullyfiled your export documentation.

2.

Corrects errors

- Get immediate feedback when data is omitted or incorrect, and correct errorsat any time.

3.

Eliminates paper review

- Eliminates time delays of handling paper.

4.

Stays up-to-date with trade agreements

- AES conforms to NAFTA and GATT, making iteasier to do business in multiple countries.

5.

Evaluates and measures potential markets

- Provides accurate and timely export statistics.

Koch and John (2007)

say the subsequent need is to reduce the risk of loss to the small businessexporter if and when their foreign customer does not pay the exporter's sales invoice. Again, there aresolutions to mitigate these risks of loss, which result from two sets of risk of loss event perils:1.Foreign "Commercial" Risk of Loss EventsThis event occurs in the foreign client's inability or failure to pay invoices due toBankruptcy/Insolvency, Slow-Pay Behavior (Protracted Default) , Devaluation of Foreign Currency2.Foreign 'Political' Risk of Loss EventsThis event occurs when a foreign country's regulations and statutes allow Confiscation of Goods, Suspension of Import Licenses, War, Civil Strife, Rebellion, Currency InconvertibilitySales made under irrevocable letters of credit (LCs) are a traditional tool used to mitigate risk of loss. An LC places the U.S. exporter's bank and their foreign customer's bank inside the tradetransaction, reducing the risk of loss to both parties for failure of either one to live up to the exportsales/purchase contract. The exporter's commercial bank will assist with the LCs if the bank providesinternational banking services, or if the bank uses another correspondent bank that maintains aninternational banking department. There are some drawbacks to LCs. Not all foreign buyers can payunder an LC because of the high fees, often 2-3% of shipment value. An LC requires a creditrelationship between the foreign importer and its bank, which might divert precious working capitalfrom the foreign buyer's other local credit needs.

Post-Shipment Finance (สินเชื่อหลังการส่งออก)

Get money right away without waiting for collection - increase liquidity for your business at KBank

Exporters can get money instantly when they submit the Export Bill for Collection (B/C) or Export Bills under L/C. Increase liquidity to pay for raw materials or goods, or use the money as working capital to run your business before getting payment from your trade partner in a foreign country or the L/C-issuing bank. KBank is ready to meet your needs with our Post-Shipment Finance, a credit line that frees you from a potential liquidity crunch … for your boundless business.

Key Features

The credit line per Export Bills is approved in either Baht or 10 other foreign currencies as you require. The Bank gives 100 percent credit per the value shown in Export Bills … to increase convenience and adroitness of your business.

With KBank's service that sends the receipt of account crediting through e-mail, you can save the time and expense of traveling to collect the receipt at International Trade Service Center.

With the Trade e-Report service summarizing your outstanding with the Bank – which you can receive as often as you choose – you can manage the funds more efficiently.

Product Details

Type of Service

1. Purchased or Discounted under Export L/C or B/C

A short-term post-shipment credit that the Bank gives to exporters to pay for raw materials or use as working capital in business operations before the exporters receive payment from the L/C-issuing bank or the B/C-Collecting Bank. The maximum repayment period is not more than 180 days in the forms of export bill purchase or discounted purchase under L/C or B/C.

2. Discounted under Export L/C without Recourse

A short-term post-shipment credit on without recourse basis gives exporter liquidity and reduces risk of non-payment from L/C issuing bank.

3. Packing Credit under Usance Bill

A short-Term post-shipment credit that the Bank gives to exporters in the forms of packing credit under B/C or L/C usance bill. Exporters can pay for raw materials or use as working capital in business operations before the exporters receive payment from the L/C-issuing bank or the B/C-Collecting bank on due date. The Bank gives 90 percent credit of the value in L/C or B/C.

Required Documents

For Purchase/Discount under L/C

1. Application for Negotiation/Discount of Export Bills Drawn under Letter of Credit for the purchase or discounted purchase of export bills drawn under L/C.

2. Original L/C

3. Original export documents under L/C

4. An Application Form for Foreign Currency Transaction (for the amount of USD50,000 or equivalent, or greater)

For Puchase/Discount under B/C

1. Application for Collection/Instruction for Negotiation/Discount of Export Bills for the purchase or discounted purchase of export bills under B/C
2. Original export documents
3. An Application form for Foreign Curency Transaction (for the amount of USD50,000 or equivalent, or greater)

For Post-Shipment Finance:Packing Credit under Usance Bill

1. Promissary note
2. Original L/C
3. Bill of Exchange
4. Export document
5. An Application Form for Foreign Currency Transaction (for the amount of USD50,000 or equivalent, or greater)

Terms & Conditions

Export must have post-shipment finance credit line approved by the bank.

*In case of Discounted under Export L/C without Recourse

L/C issuing bank's credit line is used for discount and the bank will discount the bill under L/C term only after the

bank receives authenticated SWIFT due date acceptance from issuing bank. However, the bank's consideration is

subject to issuing bank's credit rating and credit line available.

Procedure of Post-Shipment Finance

1. Exporter requests to set up the Purchased/Discounted under Export L/C, B/C with the Bank.
2. After the Purchased/Discounted under Export L/C or B/C is set up, the exporter can prepare documents specified in the L/C and related documents to submit to the Bank to request a credit line.
3. The Bank verifies the documents according to the L/C and transfers the money to the exporter's account.
4. The Bank sends document to collect payment from buyer via the L/C-issuing bank, and waits for collection result.

International trade Policy and Strategy (17BAU602B)

Unit III - MCQ

SI.NO	Question	Option 1	Option 2	Option 3	Option 4	Answer
1	How can the structure of the international society be displayed?	The structure of the international society follows the vertical model of the domestic legal orders	International society consists of a constellation of sovereign States and other international organizations, which are dispersed in a rather horizontal order of authority	International society is so anarchical that there is no order of authority, neither vertical nor horizontal	The structure of the international society resembles the structure of the most powerful nations in the world	International society consists of a constellation of sovereign States and other international organizations, which are dispersed in a rather horizontal order of authority
2	Is there any hierarchy or priority among States under international law?	Yes, the States that were the founding members of the United Nations are vested with more powers and authority	Yes, the Permanent Five Members of the UN Security Council (UK, USA, France, Russia, China) are in a superior position than the other States	No, all States are considered equal as sovereign States (the principle of sovereign equality	Whether there will be any hierarchy among States is a matter of each international organization to decide	No, all States are considered equal as sovereign States (the principle of sovereign equality
3	What is the problem of 'fragmentation' of international law?	Fragmentation of international law concerns the possibility of different legal regimes apply the same rules of international	It is possible for several legal regimes (ie foreign investment law and human rights law) to exist and develop	Fragmentation is when States assume different interpretations of the same rule of international law	Fragmentation is when States disagree to abide by a certain rule of international law	It is possible for several legal regimes (ie foreign investment law and human

		law	in isolation of each other, ultimately culminating in the production of divergent rules of international law			rights law) to exist and develop in isolation of each other, ultimately culminating in the production of divergent rules of international law
4	Is there any priority among international courts and tribunals?	According to the lis pendens rule, the court or the tribunal that seizes first the dispute has exclusive jurisdiction to adjudicate it	The International Court of Justice has by definition priority over any other court or tribunal	Since there is no lis pendens rule in international law and all depends on the consent of the parties to a dispute, there is no priority or hierarchy among international courts and tribunals	Regional or special courts have priority over all others in line of the principle of lex specialis	Since there is no lis pendens rule in international law and all depends on the consent of the parties to a dispute, there is no priority or hierarchy among international courts and tribunals
5	What is the major difference between naturalism and positivism?	On the one hand, naturalism is based on a set of rules that are of universal and objective scope and on the other hand, positivism is based on a structured and coherent legal system that is created by States in light of their	While naturalism serves only the theory human rights law, positivism has a wider and more general scope	Naturalism concerns the underpinning values of the international society, while positivism the international rules	Naturalism is a school of thought advocated outside of Europe, while positivism is Euro-centric theory	On the one hand, naturalism is based on a set of rules that are of universal and objective scope and on the other hand, positivism is based on a structured and

		interests and desires				coherent legal system that is created by States in light of their interests and desires
6	Are there any limits to the application of article 103 of the UN Charter	No, there are no limits to article 103	Yes, Article 103 cannot trump multilateral treaties	Yes, article 103 of the UN Charter cannot trump jus cogens norms	Yes, when a case is submitted to the ICJ, article 103 ceases to have any effect	Yes, article 103 of the UN Charter cannot trump jus cogens norms
7	Which are the formal sources of international law?	Custom, treaties and judicial decisions	Custom, general principles of law and theory	Treaties, custom and general principles of law	Treaties, custom and General Assembly Resolutions	Treaties, custom and general principles of law
8	Which treaties are considered as 'source of international law' under article 38 ICJ Statute?	All treaties that are in force at the time of the dispute	Only the treaties that are in force and binding upon the parties to the dispute	All treaties that have been concluded between the parties to the dispute, regardless whether they are in force	Only treaties that are multilateral and of paramount significance	Only the treaties that are in force and binding upon the parties to the dispute
9	What is required for a general rule of customary law to be formed?	Only general, widespread and consistent practice on the part of States is required	The consistent practice of few States is sufficient	The legal conviction that a certain practice of a State is in accordance with international law is the most significant	Both the elements of widespread and consistent State practice and of the opinio jurisare required	Both the elements of widespread and consistent State practice and of the opinio jurisare required

				requirement		
10	What kind of State practice is required?	Widespread, consistent and uniform practice, consisting both of acts and omissions	Only widespread, consistent and uniform acts and not omissions of States	Widespread acts and omissions of States but not necessarily consistent or uniform	Consistent practice of few States, including both acts and omissions, which is met with protestation by the other States	Widespread, consistent and uniform practice, consisting both of acts and omissions
11	Who is a 'persistent objector'?	The State which persistently objects to the rule in question after its formation	The State which denies to be bound by the rule in question for a short period	The State which persistently and publicly objects to the formation of a rule of customary law from its outset	The State which accepts the formation of a rule of customary law but it retains objections as to its content	The State which persistently and publicly objects to the formation of a rule of customary law from its outset
12	Where do we find the 'general principles of law recognized by civilized nations' (article 38 ICJ Statute)?	We look for established principles of law recognized only among the most civilised nations	We look for established principles of law, which are common to all major legal systems	We look for general principles of international law recognized by international courts and tribunals	We look for general principles of law recognized by all nations	We look for established principles of law, which are common to all major legal systems
13	What is the relationship between the formal sources of international law?	There is no hierarchy between the formal sources of international law	Treaties supersede custom	Custom supersedes treaties	General Principles of Law supersede both custom and treaties	There is no hierarchy between the formal sources of international law

14	What is the value of the Resolutions of the UN General Assembly in terms as a 'source' of international law?	GA Resolutions are considered as additional sources of international law	GA Resolutions are equivalent to treaties	GA Resolutions reflect always customary law	GA Resolutions are considered as material source	GA Resolutions are considered as material source
15	How can customary law be related to treaty provisions?	Treaties may only codify customary law	Customary law is a different source of international and it cannot be embodied in treaties	Treaties may 1) codify customary law, 2) 'crystallise' customary law, 3) lead to the emergence of customary law	Customary law can emerge only from few multilateral treaties	Treaties may 1) codify customary law, 2) 'crystallise' customary law, 3) lead to the emergence of customary law
16	What is 'unilateral acts'?	They are acts that States perform as practice in the context of custom	They are acts creating unilateral legal obligations to the acting State	Unilateral acts are simply political acts of State devoid of any legal effect	Unilateral acts are those that State perform in order to be bound by a treaty	They are acts creating unilateral legal obligations to the acting State
17	What is a 'treaty' according to the Vienna Convention on the Law of Treaties (VCLT)?	Treaties are all agreements concluded between States, international organizations and non-State entities	Treaties are agreements concluded between States in written form and governed by international law	Treaties are both the written and oral agreements between States	Treaties are agreements concluded between States in written form governed either by international or domestic law	Treaties are agreements concluded between States in written form and governed by international law
18	Should treaties assume a particular form?	Treaties should always be designated as such and assume a particular form	Treaties should always assume a particular form, no matter how they are designated	Treaties do not have to assume a particular form or designated	Treaties have to be designated as such, no matter what form they assume	Treaties do not have to assume a particular form or designated

19	Who has the authority to conclude a treaty on the part of States?	Treaties are concluded by the competent representatives of States.	Treaties may only negotiated and concluded by the heads of State and ministers of foreign affairs	Treaties are negotiated and signed only by the persons that bear the necessary 'full powers' and no person is presumed to hold such authority	Treaties are concluded only by members of the diplomatic missions of States	Treaties are concluded by the competent representatives of States.
20	How the consent to be bound of a State may be expressed?	The consent of a State to be bound is expressed only by ratification	The consent of a state to be bound by a treaty may be expressed by signature, ratification, acceptance, approval or accession	The consent of a State to be bound is expressed by signature	The consent of a State to be bound is expressed by whatever means they choose	The consent of a state to be bound by a treaty may be expressed by signature, ratification, acceptance, approval or accession
21	Do treaties bind third States, ie non-State parties?	Treaties may create only rights for third States	Treaties create both obligations and rights for third States	Treaties do no create obligations or rights for third States without their consent	Treaties do not create any obligations or rights for third States, even when the latter consent	Treaties do no create obligations or rights for third States without their consent
22	How treaties are to be interpreted?	Treaties are to be interpreted in good faith	Treaties are to be interpreted only in accordance with the ordinary meaning of their terms	Treaties are to be interpreted in accordance with the intention of the parties, as evidenced in the preparatory works of the treaty	Treaties are to be interpreted only in light of its object and purpose	Treaties are to be interpreted in good faith

23	When a reservation is considered as invalid under the law of treaties?	A reservation is invalid when the majority of the State parties objects to it	A reservation is invalid only when an international tribunal	A reservation is invalid only when is incompatible with a peremptory norm of international law	A reservation is invalid when it is incompatible with the object and purpose of the treaty	A reservation is invalid when it is incompatible with the object and purpose of the treaty
24	What is 'material breach' of the treaty?	'Material breach' is a ground for the invalidation of a treaty	'Material breach' is the repudiation or a significant violation of the treaty and serves as a ground for the unilateral termination of the treaty	'Material breach' is an insignificant violation of a treaty	Material breach' is a significant violation of the treaty which can never lead to the termination of the treaty	'Material breach' is the repudiation or a significant violation of the treaty and serves as a ground for the unilateral termination of the treaty
25	What does the 'fundamental change of circumstances' entail for the treaty?	A fundamental change of circumstances concerns the object and purpose of the treaty and it leads to its amendment	A fundamental change of circumstances has no bearing on the life of treaties	A fundamental change of the circumstances which constituted an essential basis of the consent of the parties to be bound by the treaty and which was not foreseen by the parties, may be invoked as a ground for terminating or withdrawing from the treaty	A fundamental change of circumstances leads to the automatic termination of the treaty	A fundamental change of the circumstances which constituted an essential basis of the consent of the parties to be bound by the treaty and which was not foreseen by the parties, may be invoked as a ground for terminating or withdrawing from the treaty

26	Can countries rely on their domestic law as an excuse to violate their obligations under international law?	Domestic law always prevails over international law	Only customary international law prevails over domestic law	Obligations under international law prevail over domestic law	Constitutional obligations always prevail over obligations under international law	Obligations under international law prevail over domestic law
27	What is the fundamental premise of monist theory?	Monism posits that international law is superior to domestic laws	Monism posits that international and domestic law are part of the same legal order	Monism posits that domestic laws are superior to international law	Monism posits that domestic and international law never clash	Monism posits that international and domestic law are part of the same legal order
28	What is dualism?	Dualism suggests that international and domestic law are part of a unified legal system	Under dualism, international and domestic laws comprise distinct legal Systems	Dualism suggests that international and domestic law are distinct but equal in hierarchy	Dualism suggests that international and domestic law are distinct legal systems whereby domestic law always prevails	Under dualism, international and domestic laws comprise distinct legal Systems
29	What does the doctrine of incorporation suggest in respect of treaties?	The doctrine of incorporation requires that all treaties undergo legislative transformation before they become domestic law	The doctrine of incorporation does not require any further action at the domestic level	The doctrine of incorporation treats treaties as inferior to domestic law	The doctrine of incorporation suggests that ratified treaties automatically pass into the sphere of domestic law	The doctrine of incorporation suggests that ratified treaties automatically pass into the sphere of domestic law
30	What are self-executing treaties?	Self-executing treaties are adopted only by the executive	Self-executive treaties are clear and precise enough so as not to require any further implementing	Self-executing rely on implementing measures stipulated in the treaty Itself	Self-executing treaties follow the doctrine of transformation	Self-executive treaties are clear and precise enough so as not to require any further

			measures			implementing measures
31	What is the fundamental prerequisite for the incorporation of custom under English law?	Custom is incorporated if it is not in conflict with existing legislation	Custom is superior to English law and is always incorporated	Custom must first be recognised by Parliament before the courts can bring it into the domestic sphere	Custom is incorporated with the passing of implementing legislation	Custom is incorporated if it is not in conflict with existing legislation
32	What dimension did the Kadi judgment introduce with respect to the incorporation of UN Security Council resolutions?	The Kadi judgment demanded that UNSC resolutions are construed in accordance with human rights	The Kadi judgment demanded that all UNSC resolutions be incorporated without any further implementing legislation	The Kadi judgment required that important UNSC resolutions be transformed and not merely incorporated	The Kadi judgment claimed that UNSC resolutions are not binding if they violate human rights	The Kadi judgment demanded that UNSC resolutions are construed in accordance with human rights
33	What was the consequence from the absence of implementing legislation in the Tin Council case?	The International Tin Council was headquartered in London and hence the absence of implementing legislation was inconsequential	The constitutive treaties of international organisations are subject to the doctrine of incorporation	The absence of implementing legislation with respect to the Council's founding treaty meant that individuals did not derive rights and duties from it in the English legal system	The absence of implementing legislation in England in respect of an international organisation is inconsequential under international law	The absence of implementing legislation with respect to the Council's founding treaty meant that individuals did not derive rights and duties from it in the English legal system

34	Are there any limitations to the incorporation of customary crimes under English law?	There are no limitations to the incorporation of customary crimes	Customary crimes must be contained in a multilateral treaty in order to be automatically incorporated	The courts may freely incorporate customary crimes into the domestic sphere	The situation is not clear-cut but an act of parliament would most probably be required	The situation is not clear-cut but an act of parliament would most probably be required
35	Is the recognition of foreign judgments subject to the same rules as those applicable to the incorporation and transformation of treaties?	Foreign judgments are enforced on the basis of the doctrine of incorporation	Foreign judgments are enforced on the basis of the doctrine of transformation	The recognition of foreign judgments is dependent on the existence of appropriate bilateral or multilateral treaties	The courts exercise discretion as to the enforcement of foreign judgments on the basis of the rule of comity	The recognition of foreign judgments is dependent on the existence of appropriate bilateral or multilateral treaties
36	Incoterms has been issued in …………	1990	1995	1997	2000	1990
37	In which I.C.J Article the sources of International Law are explained?	Article 15	Article 38	Article 50	Article 48	Article 38
38	The UN membership as at December 31,2011 was…….	190	193	200	210	193

39	Principle of " Pacta sunt servanda" means……	Treaties are binding	Treaties have no force	Agreements are sacred	Treaties are to be interpreted in good faith	Agreements are sacred
40	What was the exact number of member states when the UN was founded in 1945?	41	51	61	71	51
41	The British Sales of Goods Act……………… ………	1979	1989	1999	2009	1979
42	The unification of the substantive rules occurs…………	resolution of Conflict	settlement	negotiation	govern international sales of goods transactions	govern international sales of goods transactions
43	ULF means……….	Uniform Law on the Formation	Unity legal formation	Uniform law function	United nation law frame	Uniform Law on the Formation
44	The purpose for ULF is…….	negotiation	dispute settlement	Formation of Contracts	Legal frame	Formation of Contracts

45	The purpose for ULIS is…….	negotiation	International Sales of Goods	Formation of Contracts	Legal frame	International Sales of Goods
46	International mercant usages law is ………	Formation of Contracts	sales contracts	International Sales of Goods	negotiation	sales contracts
47	CPT means ______________.	carrier posted to.	carrier paid to.	carriage paid to.	carriage posted to.	carriage paid to.
48	CFR means _______________.	container and freight.	cost and freight.	carriage and freight.	carrier and freight.	cost and freight.
49	FOB means…..	Freight on Board	Free on Board	Free of business	freight rate	Free on Board
50	Foreign Trade Development & Regulation Act…..	1990	1991	1992	1993	1992

51	Foreign Exchange Management Act…….	1990	1991	1992	1999	1999
52	Pre Shipment Inspection and Quality Control Act…..	1990	1991	1963	1999	1963
53	Customs Act…..	1963	1999	1972	1962	1962
54	"Treaties are the supreme law of the land". Where is it laid down?	Constitution of USA	UN Charter	Statute of the ICJ	British Constitution	Statute of the ICJ
55	"International Law is not true Law but positive international morality only". Who said it?	Pufendof	Austin	Bentham	Pollock	Austin
56	The permanent court of arbitration was established by………..	The Hague Conferences of 1899 and 1907	The Washington Naval Conference of 1922	The Vienna Conference of 1968-69	The Geneva Convention of April 29, 1958.	The Hague Conferences of 1899 and 1907

57	A Condominium is……..	A State of Chaos	A State enjoying Dominion status	A particular territory over which joint dominion is exercised by two or more external powers.	A State with a Federal form of Constitution	A particular territory over which joint dominion is exercised by two or more external powers.
58	Arbitration is a method of ……	negotiation	International Sales of Goods	settlement of disputes	Legal frame	settlement of disputes
59	American Arbitration Association (AAA) was founded in ……	1926	1936	1946	1956	1926
60	International Centre for Dispute Resolution (ICDR), established in…..	1986	1996	1997	1998	1996

INTERNATIONAL TRADE POLICY AND STRTEGY (17BAU602B)

UNIT IV SYLLABUS

Experience of Select Developing Countries - Analysis of the trade strategy and the policy framework in two select large countries and comparison with India - Impact of trade on growth - agriculture - inequality - poverty and other developmental indicators - Case Studies on Trade Strategies of Emerging Economies - China and ASEAN (Association of South East Asian Nations).

Export Finance

Export finance refers to financial assistance extended by banks and other financial institutions to businesses for the shipping of products outside a country or region. Export financing enables MSMEs to expand its reach to a global audience.

An exporter should first gain understanding of some documents commonly required by export finance institutions. These documents are mandatory requirements for most types of export finance assistance.

Export finance assistance is extended at various stages of exports. Loans or advances are granted by financial institutions to exporters for financing the purchase, processing, manufacturing or packing of goods prior to shipment which is known as pre-shipment credit .

Loans or advances are granted by financial institutions to exporters from the date of extending credit after shipment of goods to the date of realization of export proceeds which is known as post shipment credit.

Banks and financial institutions extends factoring services to exporters where-in it buys the accounts receivable of the exporter at a discount in exchange for immediate money.

PAYMENT TERMS AND EXPORT FINANCE RESOURCES

Payment Terms- A list of things to consider when determining the best price for your product overseas.

Terms of Sale

Terms in international business transactions often sound similar to those used in domestic business, but they frequently have very different meanings. For this reason, the exporter must know the terms before preparing a quotation or a pro forma invoice.

Preparing Quotes for International Buyers

While a sales contract that spells out the details of a transaction is warranted for larger, more complex deals, a quotation in the form of a Pro Forma Invoice may be sufficient for smaller transactions.

Learn how to prepare Pro forma invoices and the information they should contain and more about how to prepare quotes.

METHODS OF PAYMENTS

A successful export transaction starts with the negotiation of a sales contract and ends with a timely payment. The buyer/importer gets the product they want and pays the seller/exporter a profitable amount as soon as possible. Depending on the parties' comfort with the degree of risk, there are four methods of payment and other issues to consider, as explained below.

Cash In Advance

With Cash In Advance, the buyer pays the exporter before the shipment/export is made. This method benefits the seller, provided all costs were taken into consideration and calculated correctly. See VEDP Fast Facts on terms Ignoring actual cash and the barter system, there are three forms of payment that qualify as cash in advance:

- A wire transfer is the best method of paying, although banks charge ($25-$35) for this service.
- Paying by check is another good option, but payment could be delayed for up to six weeks waiting for clearance from a foreign account. A bank draft is more appropriate for trade.
- A credit card is a viable choice for low dollar amounts, mostly for the convenience of speed and the automatic currency conversion, but the decision will depend on the exporter's product and in-house collections process.

Cash In Advance payment terms may be considered the most "credit-risky" for the importer/buyer, however the terms may allow for a "savings" to the importer if offered with a discount. Often, Cash In Advance payment terms can be less expensive for the importer when viewing the overall process of the sale and compared to the costs for opening a Letter of Credit at their bank. Depending on a product's lead time and the investment required to produce goods for a specific buyer, Cash In Advance terms by "progress payments" can be an attractive payment method.

Letters Of Credit / Documentary Credits

Letters of Credit (L/C) are often called Documentary Credits by some banks to avoid confusion with "Stand-by" L/C, which are used as a "back up" when services are not provided per a sales agreement. Documentary Credits help to remind the parties involved that banks deal strictly in documents; they do not see or handle the actual goods, so attention to detail on the shipping documents is a must. This method of payment involves strict adherence to bank instructions on the types of documents, terms, conditions, and specific wording required. See flow chart page 5.

- Letters of Credit are produced by commercial banks. The importer's bank "opens" a L/C in favor of the exporter, which is based on the importer's credit and the export sale involved.
- The format for Letters of Credit has been standardized by the International Chamber of Commerce (ICC). For instance, uniform codes are used for each line item so that, as an example, line item 45A will always be where the description of goods will be found, and line item code 44C will always be where the latest shipment date is designated.

- The best type of L/C for the seller is one that is based on their proforma invoice and is non-transferable and irrevocable. All L/Cs, unless specified, are considered irrevocable – meaning the buyer/seller cannot back out of the deal after the L/C has been opened and accepted.
- A "confirmed" L/C ensures the exporter will be paid by his or her own bank, even if the importer's bank fails to pay, provided all of the L/C instructions and document requirements are followed. Although additional fees apply, exporters should request importers to open a confirmed, irrevocable and non-transferable commercial L/C. The importer's bank must have a corresponding relationship with a U.S. bank or be creditworthy since the exporter's bank will not confirm the L/C of an unknown bank. Note that in some countries, a confirmed L/C is not always available due to risk factors.
- A disadvantage to an importer (relative to the size of their business) is that their bank charges fees to open a L/C and usually will hold a percentage of collateral during the "validity" of the L/C (it "ties up" their cash).

There are several variations of Letters of Credit, including Export, Sight, Time, Performance, and Stand-By. Before the exporter accepts the Letter of Credit from the importer, it is extremely important for them to review every detail of the L/C. For example, the exporter should consider if the latest ship date referenced in the L/C is acceptable, or if the amount/value of the L/C is correct (a "+" or "–" prefix to the value on the amount stated can actually help prevent delays when the total ends up being different than the exact amount indicated on the L/C).

Documentary Draft

Documentary drafts are a standardized document available to the exporter by their bank and used to execute the payment terms for a sale. Drafts are filled out by the exporter/seller and sent with the shipping documents to the presenting bank – the bank in the buyer's country. Copies are sent to the exporter's bank and the two banks become "witnesses" to the transaction.

The original shipping documents are released by the presenting bank as the importer/buyer "accepts" the draft with a payment schedule of 30/60/90 days "tenor" or pays the draft "at sight." Then, the presenting/buyer's bank sends the payment to the seller's bank.

- Documentary drafts are also standardized by Uniform Customs and Practices (UPC 600).
- Documentary drafts involve a slight risk for the exporter compared to a confirmed L/C since there is no guarantee of a payment.
- Payments by documentary drafts are less costly than documentary drafts to process for the importer. For the exporter, they have the advantage of allowing the shipment to be without the stipulations of a L/C. For example, a L/C may have a "latest ship date" that is impossible to meet because of product availability or production delay requiring an amendment to the L/C which, if accepted, will add a fee to the cost of the sale.

- With this payment term, the exporter need not wait for a L/C to be opened from the importer's bank - if the goods are ready to ship, the exporter just needs the buyer's bank information to send the Documentary Draft.
- Using Documentary Drafts for collections is a good step in building a long-term relationship with a client. The documentary draft process signals more trust, less costs to the importer, and may be used as a gauge for the exporter to decide when to offer Open Account terms.

Open Account

Open account means the exporter is extending credit to the buyer as a contractual relationship.

- The importer agrees to pay at a later time. Terms offered by the exporter may be 30/60/90 and sometimes 120 days after the date of the Commercial Invoice or Bill of Lading.
- The exporter's credit and collections/finance department monitors the customer's account in their billing/accounting system designating the transaction involved and payment due date.
- Open Account payment terms may be considered the most "credit-risky" for the exporter and should not be offered until they have determined that the importer has a good reputation for making payments.

Credit Insurance

EX-IM also provides credit insurance at very reasonable prices which protects U.S. exporters against the risks of non-payment by foreign buyers for political or commercial reasons. EX-IM assumes the risks banks will not accept—as long as there is reasonable assurance of repayment.

Pre-Export Financing

EX-IM's working capital financing can help U.S. exporters obtain loans to produce or buy goods or services for export. These working capital loans are made by commercial lenders and backed by an EX-IM guarantee. Exporters may use the guaranteed financing to:

- Purchase finished products for export;
- Pay for raw materials, equipment, supplies, labor and overhead to produce goods and/or provide services for export;
- Cover Standby L/C serving as bid bonds, performance bonds, or payment guarantees;
- Finance foreign receivables.

To be eligible for working capital loans:

- Exporters must be located in the U.S., have at least a one-year operating history, and a positive net worth;
- Exports must be shipped from the U.S.;
- Products must have at least 50% U.S. content. If less than 50%, then Ex-Im can only support the export up to the percent of the U.S. content;
- Services must be performed by U.S.-based personnel;

- Military or defense items are generally not eligible, nor are sales to military buyers (with certain exceptions).

Payment terms as a means of financing your exports

Your financing requirements begin at the time you decide to enter the export market, but the serious financing requirements start once you get the order. The contract that you negotiate with the importer dictates:

- How you will be paid
- When you will be paid
- For what you will be paid

These are referred to as your 'payment terms'. All of these factors impact on your post-contract financing requirements. Take, for example, if you agree to be paid in 90 days. This will mean that you will not see any money from the buyer for 90 day.

Negotiating payment terms

It is highly likely as you become increasingly involved in exporting, that a point will come where you have to negotiate an export sale. During these negotiations, the importer is most likely going to ask you what payment terms you offer. A payment term refers to the way payment will be made as well as the period over which you will allow the importer to pay for the goods. Such payment/credit terms are important in international trade as they can be used to competitive tool to attract business for your firm, but they can also be used by the importer against you.

Risk to the importer

If your goods are not up to standard and the importer has already paid you, they will have lost out. Once you have received your money, it is very difficult for the importer to exert any influence over you. You may argue that you are a reputable company and that you would never renege on a contract or that you will always provide after-sales service, but the importer may not be willing to take a chance with a company that they do not know and that is also very far away.

If the importer is in a stronger position, then you may be obliged to offer payment terms. What is more, if payment terms are being offered by your competitor or if payment terms are normal in the industry or country that you are competing in, then may again be obliged to offer such terms.

Know the market before negotiating payment terms

It is important, therefore, before you begin negotiating with the importer, to know exactly what circumstances prevail in the industry or country that you are competing in. Payment terms ranging from 30 to 90 days are quite common in export markets. Be very careful when extending longer payment terms, as longer credit periods may increase the risk of default.

Always undertake a credit check on the importer

Also you need to be aware of your own importance that you attach to this sale. It would also be worthwhile having undertaken a credit check on the company you plan to do business with. With this knowledge you will be in a better position to decide whether to offer credit or not. Bear the cost of financing and method of payment in mind.

Pricing as a financing mechanism

Clearly, the export price that you agree to with the foreign buyer impacts on the income you generate and your ability to pay for your export endeavors. If you price too low, there may be little or no profits with which to finance your exports. Price too high, then you can pay back any export-related costs more quickly, but you stand to lose the order because your price is too high.

Absorbing the credit costs into your export price

In the instance where you decide to offer relatively short-term credit (say between 30-60 days) to the foreign buyer, and your firm has the capacity to do so, it may be worthwhile to absorb the credit costs into your export price. You would include these credit costs as part of your costing exercise.

Converting export receivables into cash

There are several ways to turn export receivables (the monies owned to you by the importer) into cash. They are as follows:

- Confirming
- Factoring
- Forfaiting

Confirming

Confirming is a financial service in which an independent company confirms an export order in the seller's country and makes payment for the goods in the currency of that country. Among the items eligible for confirmation (and thereby eligible for credit terms) are the goods themselves; inland, air, and ocean transportation costs; forwarding fees; custom brokerage fees; and duties. For the exporter, confirming means that the entire export transaction from plant to end user can be fully coordinated and paid for over time.

Factoring

Factoring (also known as debit financing) involves the discounting of your foreign account receivable to a specialist factoring house - an organisation that specialises in this form of financing. A factoring house will probably be prepared to offer you more (up to 80%) for the value of your accounts receivables than a bank, but will only provide financing for work already done and for which you have invoiced the importer. Once the final payment is received from the importer, you will receive the remainder of your outstanding monies, less the factoring house's financing charges (which will probably be a few percent higher than the standard rate for an overdraft). Essentially you would transfer your title to your foreign accounts receivable to the factoring house for cash at a discount on the face value. Although factoring is sometimes done without recourse to the exporter, the specific arrangements may vary and need be verified by the exporter. Factoring is usually not available where a draft is involved.

Forfaiting

Forfaiting is a form of bill discounting, yet it is usually provided without recourse to exporter in the event of non-payment at the maturity of the bill (but this may differ from forfeiting agency to forfeiting agency and so it is important that you confirm this with the agency concerned). Forfaiting enables exporters to convert a credit sale into a cash sale. The reason for this is that forfeiting involves selling your longer-term accounts receivable or promissory notes from a foreign buyer to a specialist agency such as a bank that does forfeiting (not all banks are involved in forfeiting). The forfeiting agency would pay you for the value of the accounts receivable, less a discount, which represents their fee. The difference between factoring and forfeiting is that while factoring is essentially a loan based on your accounts receivables, forfeiting is the outright sale of your accounts receivable. Forfaiting is often used in instances where you will be paid in stages and is used for financing high-value goods, such as construction projects.

Alternative sources of financing

There are several alternative sources of financing. For example, the Industrial Development Corporation provides financing for capital and other types of exports. The Small Enterprise Development Agency (seda) assists in finding financing for small businesses and there is no reason why this should not include small exporters. Various regional development agencies provide financing for local firms and you might want to consider these.

Getting buyers and suppliers to help

Do not loose site of the possibility of the buyer helping to finance the sale. To begin with the buyer may be prepared to put down a deposit to help finance the deal. In addition, they may be prepared to make periodic progress payments based on a third-party report or some other confirmation that certain agreed-upon percentages of the project have been completed.

Using export intermediaries to help finance your exports

If you are a small exporter and simply cannot find the money to finance your export project, you could turn to an export agent or an export trading house to help you. In this instance, they would probably take over the deal completely and may simply pay you for the goods which they would then sell to the importer making whatever mark-up they choose. If financing is required, they may be in a better position to obtain the financing required to cover the export sale, but they would expect a substantial reward for their involvement and your profits are likely to be cut quite substantially.

Managing your export risk

Introduction

There are many risks involved in exporting and in this section we briefly cover the main risks you are likely to encounter. Follow the links below to learn more about the risks in question:

- Credit risk
- Poor quality risk
- Transportation and logistics risks
- Legal risks
- Political risks
- Unforeseen risks
- Exchange rate risks
- Cultural and language risks
- Managing your risks

Companies need to develop a professional approach when entering the field of exporting. The company's management will have to be extremely committed and will need to devote time and money to starting up their export campaign. Companies will also face greater competition and more stringent rules and regulations pertaining to products and packaging. There are a number of risks facing exporters, while there is an element of risk in all commercial transactions, the complexity of the environments that exporters must operate in, multiplies these risks.

Credit risk

In most instances - mainly because of the large distances and alien environments involved - it is generally difficult for the exporter to verify the creditworthiness and reputation of an importer. If the creditworthiness of a foreign buyer is unknown there is the increased risk of non-payment, late payment or even straightforward fraud.

It is essential, therefore, that the exporter should strive to determine the creditworthiness of the foreign buyer. There are many commercial firms that can provide assistance in credit-checking foreign companies. In addition, the exporter should insist (particularly if the foreign buyer is unknown) for a secure method of payment such as an irrevocable documentary credit. The exporter could approach his bank in South Africa for assistance regarding international payment procedures.

Poor quality risk

If the goods to be exported are not inspected before they are shipped by an independent third-party, the exporter may find his entire shipment being rejected on arrival at the importer's premises due to the poor quality of the goods. Some unscrupulous importers may do this just to put pressure on an exporter and to try and negotiate a lower price. Experienced importers may request a pre-shipment inspection, to be conducted by an independent inspection company. If they don't, then it may be worth suggesting to the importer during the negotiation stage that such an inspection be carried out as part of the contract. Such an inspection protects both the importer and the exporter.

Transportation and logistics risks

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.

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). Exporters and importers must understand their legal rights to claim against carriers. The "shipper", would be the party that pays the main carrier of freight and this could be either the exporter or the importer, dependent upon the Incoterm (see section on Incoterms 2000, ICC publication) under which that particular transaction was effected.

Legal risks

International laws and regulations change frequently and/or may be applied differently from that of the exporter's own country. It is therefore important that the exporter drafts a contract in conjunction with a legal firm, thereby ensuring that the exporter's interests are taken care of. The exporter should draw up a checklist of basic legal questions aimed at the imported prior to signing any formal contract.

In particular the exporter should be clear as to which law and dispute-settlement procedure will apply to the contract (known as the jurisdiction of the contract). The exporter may wish to impose choice of law and choice of forum clauses, which state that disputes will be settled under the exporter's own national law and courts.

Political risk

The political stability of a foreign country into which a company is exporting is of the utmost importance. Exporters must be constantly aware of the policies of foreign governments in order that they can change their marketing tactics accordingly and take the necessary steps to prevent loss of business and investment.

Instability in the target market could lead to losses resulting from war, civil strife and political instability. It is essential to warn exporters to be aware of government intervention in the target market. Most countries world-wide operate under a capitalist system within which the volumes and values of goods and services whether provided locally or by way of imports, are set by the forces of supply and demand.

Unforseen risks

A natural disaster or terrorist action in a particular country could completely destroy an export market for a company. Unexpected occurrences may also increase the cost of transport causing great loss to the exporter. It is therefore important that the exporter ensures that a force majeure clause be included in any international contract the exporter concludes.

Exchange rate risks

All South African exporters face this risk on a daily basis, as our South African Rand strengthens or falls against other major currencies, it is difficult for South African exporters to predict the movement of the Rand, thus resulting in speculation on the part of the exporter on the likely direction of movement of the currency (i.e. up or down). Ultimately one party will benefit over the other. The easiest way to overcome this is to quote in one's own currency namely the SA Rand. A strategy that the exporter could follow in order to protect against the influence of exchange rate movements is to hedge against such movements through the purchase of forward exchange rate contracts.

Culture and language risk

Misunderstandings in communication and in international trade transactions arise because in most instances the importer and exporter come from different cultures and express themselves with different languages. In most instances business practices, tax systems, rules and regulations, accounting methods, currency controls and customs systems all differ from that of the exporter's own country.

The exporter must ensure that he fully understands these differences and often an in-market visit to the intended country of export will greatly assist the seller in having a better understanding of his intended market place and the culture differences (s)he may encounter.

Managing your risks

The task of managing your export-related risks begins with known what the risks. Your first step is therefore to identify the risks that you are likely to encounter and to give some 'weighting' to the seriousness of the risk. The more serious it is, the more attention you will need to give to addressing the risk in question. With some of the risks outlined above, you can obtain insurance to cover the risk. Three main types of risk cover include credit risk cover, country risk cover and transit risk cover - these are discussed below.

Negotiating and quoting in exports

Introduction

Once you have done all of your planning and preparation and put together an export strategy and plan, you need to begin implementing this plan. The plan has many facets to it and one of these is to approach your customers, convince them to buy from you, negotiate a deal and price that that they find acceptable, and present them with a quote which hopefully they will accept. This represents the start to the actual export transaction and represents the selling process, involving negotiating with and quoting to customers.

The selling process

It sounds easy, but the negotiating and quoting process is the key to the success of your export endeavours. As with any business, success is based on closing sales. Without sales, there is no business. All of the market research done, advertising undertaken, e-mails sent, and buyers approached, or trade fairs attended is worth nothing if you cannot close the sale. There is much theory written and models proposed about the selling process, but in this section we try to put forward as practical an approach as possible.

In the selling approach we propose, there are eight steps. These are:

- Deciding who will do the selling?
- Prospecting for buyers

- Doing a preapproach
- Approaching the buyer
- Making the presentation
- Overcoming objections
- Closing the sale
- Following up

The process outlined above is not strictly linear. It is more like a spiral, each step feeding back and influencing the others as the process overall moves forward toward the close (assuming you do it right). The salesperson knows that selling is a process of evaluation and reevaluation - both for the salesperson and for the prospective customer.

- **Deciding who will do the selling?**

The first step in the selling process is deciding on who will do the selling. For smaller export companies, it will probably be the owner, managing director, or marketing/sales manager (where one exists) that will do the actual selling. In bigger companies that have an export department, it will probably be the export manager, but in very large companies with extensive export operations, they may employ a professional sales force in one or more countries that undertake the selling process in the countries they are responsible for.

Consider a sales team

Even if you are a relatively small firm, you may still want to consider forming a small export sales team, perhaps with your marketing/sales manager and/or a company technical expert (an engineer, for example). For those owners that are determined to be part of the export sales process, doing it as a team is a good option. Firstly, you can select staff to support you that are good in areas that you are no. For example, they may be technically more knowledgeable than you, or they may be better at selling than you, or they be able to speak a language (such as German) that you could put to use in your selling efforts, or they may have a more suitable personality for selling in foreign cultures.

Secondly, working as a team is often a good sales strategy, as it allows you the opportunity to share the selling duties, concentrate on different aspects of the selling process, or allow yourselves a chance to discuss and confirm your feelings about a new development or aspect of the sales proposition.

For larger companies, approaching the export sales task as a team is strongly recommended. Contracts are often large and complex enough to justify a team approach.

- **Prospecting the buyers**

Prospecting is the process of gathering a list of potential customers or buyers. After all, before you can approach a particular buyer, you need to know who the buyer is. Generally you will identify your list of buyers at the same time as undertaking your export marketing research. Indeed, one of the objectives of your research effort should be to come up with a list of potential buyers.

But compiling a list of buyers is not enough. You still need 'qualified' these buyers, which means that they need to be assessed to see if there is business potential, otherwise you could be wasting your time. In order to qualify your foreign prospects, you need to:

Focus on the needs of the customer

- Determine which products or services you produce best meet their needs
- In order to save time, rank the prospects and leave out those that are least likely to buy from you (and obviously start with those with the most potential)

Buyers versus end-users

It is worth considering that your buyer may not be the end user of your product. For example, if you sell children's toys, the end user may be the child that uses your product and the parent that buys the toy, but your customer may be an import agent or wholesaler of toys in the target market you have selected.

- **Doing your preapproach**

At this point you now have compiled a list of qualified buyers (perhaps five to ten firms or even more) that you think are likely buyers of your firm's products. The next step is to prepare your approach to these companies. To do this, you will attempt to identify possible problems in the customer's firm where your product could provide a solution. At this stage you would also consider various selling objectives which take into account the marketing environment and the specific situation of the customer's firm.

Approaching the buyer

This step can be further divided into two parts:

a) Making the appointment

The first is to make an appointment with the buyer. Most foreign buyers will be interested in meeting with foreign suppliers, even if only out of curiosity's sake, but you still need to take care as to how you phrase your introduction. Your introduction will also depend on what medium you use (fax, e-mail, letter or telephone).

b) The appointment itself

The second part of the approach is actually calling on the buyer. This is perhaps the toughest part of the selling process. It involves introducing yourself and making a "connection" with the buyer. Here you need to be very careful, as different cultures deal with business introductions differently. Read up on how the business etiquette in the country you are visiting. Make sure that you are on time - this is very important in many cultures (even if the buyer arrives late, this does not matter).

A good firm handshake is always a good start and bow if this is appropriate in the country you are visiting. Greeting the buyer in his home language is also a sign of respect (at which point you would of course switch back to English). Thank the buyer for giving you the time to meet with him/her. A business card is essential and this will usually be swapped early on in the meeting. Dress appropriately. Be circumspect about giving gifts and get advice about gifts beforehand. Also be careful about using humour.

During this stage you would also try and learn more about the buyer him/herself in order to establish a bond with him/her. Unfortunately, there is often very little time to do this in, while many factors may interfere with the process. Make sure that you've done some homework before meeting your prospect. This will show that you are committed in the eyes of your customer. Keep a set of samples at hand (where appropriate), and make sure that they are in very good condition.

Evaluating the customer's needs and buying situation

At this point, you will want to obtain some facts and figures related to the needs of the buyer, so that you can determine whether you can satisfy these needs. You will also want to inform your buyer about your products and deal with any concerns the buyer may have about your firm and its products. With some products you may not be able to present a final proposition to the buyer because you still need to make some calculations back at your office. In these instances, tell the buyer what you plan to do and stick to this schedule.

- **Making a presentation**

In the selling process, there will be a time when you present your company and its products to the buyer - this is what the meeting is all about. Be careful about leaving before having done this presentation. Sometimes you may have only a few minutes to do this and you will only be able to do this verbally; on other occasions you may have an hour or more to deliver your presentation and you will be able to support your verbal presentation with slides, graphics, photographs and even videos.

Presentation tips

Some additional tips for your presentation:

- Be enthusiastic about your product or service. If you are not excited about it, do not expect your prospect to get excited.
- Focus on the real benefits of the product or service to the specific needs of your client, rather than listing endless lists of features.
- Try to be relaxed during the meeting, and put your client at ease.
- Let the client do at least 80% of the talking. This will give you invaluable information on your client's needs.
- Remember to ask plenty of questions. Use both open-ended questions and 'yes' or 'no' questions. This way you can dictate the direction of the conversation.
- Never be too afraid to ask for the business straight off, but do so with respect.
- Stages of presentation
- Your presentation (whether a short five minute one or a longer hour presentation or even a digital or hardcopy presentation) should strive to achieve five things:

- Attention: Get the buyer's attention
- Interest: Get the buyer interested in what you have to
- Desire: Get the buyer to want what you have to offer
- Conviction: Get the buyer to believe that your offer is a good one for his firm
- Action: Get the buyer to sign an agreement/contract
- The first two steps will in most cases be easy to achieve. The fact that you have travelled far afield to visit the buyer will probably ensure his/her attention and interest. If, however, you are selling something that the buyer does not believe that you or your country is a recognised seller of (such as selling brandy to France), then you may still have to focus on these two steps.

The last three steps will possibly more difficult to achieve in foreign markets because of the distance involved and the question mark on matters such as reliability and complexity of supply, the costs involved, the uncertainty about service, etc.

- **Overcoming objections**

In almost all sales presentations, local and foreign, the buyer will have certain reservations about the company, the products and entering into an agreement with your company. In the foreign sales environment, overcoming these objections is even more difficult because of the complexity of the foreign communications and cultures involved. Some objections may prove too difficult to handle, and sometimes the buyer may just take a dislike to you (also known as "the hidden objection").

Approaches for handling objections

Objection handling is the way in which salespeople tackle obstacles put in their way by clients. Here are some approaches for overcoming objections:

- Firstly, try to anticipate objections before they arise.
- Do not allow objections to grow into an argument.
- Objections often have merit, especially from the buyer's point of view. If necessary, acknowledge the objections, provide some simply counter arguments in an amicable and friendly way and then move on. Do not simply ignore or wave the objections away.
- Do not follow a confrontational approach and try and be more superior than the buyer - show respect.
- The 'yes but' technique allows you to accept the objection and then to divert it. For example, a client may say that they do not like a particular colour, to which you may counter 'Yes but the product is also available in many other colours.'
- Ask 'why' the client feels the way that they do.
- 'Restate' the objection and put it back into the client's lap. For example, the client may say, 'I don't think the product will work in this country,' to which you could respond, "Is it that you don't think the product will work in this country because of the different power supplies being used?', generating the response

"No, we have different national standards compared with South Africa; and we have tried it before". You may be able to counter with the comment that you have no adapted the product to meet their national standards authority and that you have received national certification for the product.

The sales person could also tactfully and respectfully contradict the client, but you need to be very careful how you do this.

- **Closing the sale**

This the most important stage of the selling process and often salespeople leave without ever successfully closing a deal. It is at this point where you need to employ an affective means of bringing the buyer to a decision. In the foreign environment where you are not familiar with the culture and language, it may be very difficult for you to gauge when to try and close the sale. If you do it too soon, the buyer may feel that you are being too 'pushy' and may withdraw from the discussion. Leave it too long and the buyer may get bored and frustrated with your presentation with the same ultimate effect.

Some tips for closing the deal:

- Just ask for the business! - 'Please may I take an order?' This often works well.
- Look for buying signals (i.e. body language or comments made by the client that they want to place an order). For example, asking about availability, asking for details such as discounts, or asking for you to go over something again to clarify.
- Just stop talking, and let the client say 'yes.' Again, this again works well.
- The 'summary close' allows the salesperson to summarise everything that the client needs, based upon the discussions during the call. For example, 'You need 12 000 items of product X in blue, packaged as we discussed, and delivered in Hamburg by the end of February' Then ask for the order.
- The 'alternative close' does not give the client the opportunity to say no, but forces them towards a yes. For example 'Do you want product X in blue or red?' Cheeky, but effective.
- It is important to realise that closing the sale is really about getting the buyer to agree to buy from you. The first step is really simply a verbal agreement to the parameters of the order that the two of you have discussed the past hour or so.

To begin with, in most instances it is unlikely that the buyer will agree to the order immediately. The buyer more likely will want

(a) Specifications both in terms of capacity and price that you may still need to confirm back home,

(b) Some time to think about the order (in some countries such as Japan, it may take many, many visits and several years of interaction, negotiation and discussion before you ever receive an order),

(c) A formal quotation on which to make the decision.

A few flamboyant exporters may tell you that you should not walk out of the buyer's office without a signed order form, but it is seldom as easy as this. Because of the many cultural and language differences, a single order form is unlikely to suffice in all instances. The requirements between buyers may also vary drastically especially as you move from country to country. Finally, most export orders are confirmed on the basis of a quotation, which usually takes the form of a proforma invoice.

In many instances, the actual closing of the sale often takes place away from the original meeting and forms part of the follow-up process that is key in the export selling process.

- **Following up the sale**

As we said above, the follow-up is an important part of selling process especially in export markets. Depending on whether the agreement was signed at the time of the sales presentation, you will either want to (a) thank the buyer for his time and custom, and assure him of your attention to the supply of the goods sold, or (b) thank him for the meeting and provide a proforma invoice that covers all of the issues that the buyer asked you to address (these may have had to do with quality, quantity, price, colour, specifications, delivery dates, insurance, freight, etc.). We deal with the preparation of the proforma invoice in the section on quoting for exports.

Export-Import Bank of India

Export-Import Bank of India is the premier export finance institution in India, established in 1982 under the Export-Import Bank of India Act 1981. Since its inception, Exim Bank of India has been both a catalyst and a key player in the promotion of cross border trade and investment. Commencing operations as a purveyor of export credit, like other Export Credit Agencies in the world, Exim Bank of India has, over the period, evolved into an institution that plays a major role in partnering Indian industries, particularly the Small and Medium Enterprises, in their globalisation efforts, through a wide range of products and services offered at all stages of the business cycle, starting from import of technology and export product development to export production, export marketing, pre-shipment and post-shipment and overseas investment.

Export-Import Bank of India: Objectives and Functions

The Export-Import Bank of India was set up by the Government of India on January 1, 1982. Its main objects are:

- To ensure and integrated and co-ordinated approach in solving the allied problems encountered by exporters in India.
- To pay specific attention to the exports of capital goods;
- Export projection;
- To facilitate and encourage joint ventures and export of technical services and international and merchant banking;
- To extend buyers’ credit and lines of credit;

- To tap domestic and foreign markets for resources for undertaking development and financial activities in the export sector.

The functions of Exim Bank include:

- Planning, promoting and developing exports and imports;
- Providing technical, administrative and managerial assistance for promotion, management and expansion of export sector.
- Undertaking market and investment surveys and techno-economic studies related to development of exports of goods and services.

The EXIM Bank has a 17-member Board of Directors, with Chairman and Managing Director as the chief executive and full-time director. The Board of Directors consists of the representative of the Government of India, RBI, IDBI, ECGC, commercial banks and the exporting community.

The authorised capital of EXIM Bank is Rs. 200 crores, of which Rs. 75 crores is paid up. The banks have secured a long-term loan of Rs. 20 crores from the Government of India. It can also borrow from the RBI. It is empowered to raise resources in domestic and international markets.

The Bank began its lending operations from March, 1982. Till June, 1982, it has extended assistance up to Rs. 133 crores to the export sector in various ways.

The establishment of Exim Bank may be regarded as a right step in the export promotion policy and programmme of the Government.

During 1984, the Exim Bank sanctioned various programmes of funded assistance of Rs. 430 crores. It also launched a new programme to provide term finance for export-oriented units, under which assistance was provided through a consortium for establishing a 100 per cent export unit in the ceramics industry.

The EXIM Bank also extended its financial assistance to Indian exports through letters of credit, re-lending facility, export bills rediscounting, overseas investment finance, facilities for deemed exports and assistance to hundred per cent export units and units in free trade zone.

At the end of December 1984, the Exim Bank’s outstanding underfunded and non-funded assistance amounted to Rs. 415 crores and Rs. 510 crores, respectively.

In 1984, the Exim Bank signed a loan agreement to borrow one billion yen from the Japanese commercial yen market.

In June 1986, the Exim Bank introduced a new programme called the Export Marketing Fund (EMF), under which finance is made available to Indian companies for undertaking export marketing activities. The programme also covers activities like desk research, minor product adaptation, overseas operations and travel to India by buyers overseas. During 1986, Rs. 78 lakhs were sanctioned, while Rs. 3.4 lakhs have been utilised under the EMF.

On whole, the Exim Bank concluded an agency credit line of US $ 15 million with the International Finance Corporation (IFC).

During 1994-95, Exim Bank sanctioned Rs. 2,466 crore and disbursed Rs. 2,130 crore of financial assistance under various lending project.

Activities of Exim Bank:

The bank can raise additional resources through borrowing from Government of India, from RBI and from the market through the issue of bonds and debentures. Exam bank also provides refinance facilities to the commercial bank and financial institutions against their export-import financing activities.

During the Year ending on 31 March, 2003, Exim Bank sanctioned loans of Rs. 7,828 crores while disbursements amounted to Rs. 5,320 crores, Net Profit (before tax) of the bank for the period 2002-03 on account of General Fund amounted to Rs. 268 crore.

Organization

EXIM Bank is managed by a Board of Directors, which has representatives from the Government, Reserve Bank of India, Export Credit Guarantee Corporation of India, a financial institution, public sector banks, and the business community.

The Bank's functions are segmented into several operating groups including:

- Corporate Banking Group which handles a variety of financing programmes for Export Oriented Units (EOUs), Importers, and overseas investment by Indian companies.
- Project Finance / Trade Finance Group handles the entire range of export credit services such as supplier's credit, pre-shipment Agriculture Business Group, to spearhead the initiative to promote and support Agricultural exports. The Group handles projects and export transactions in the agricultural sector for financing.
- Small and Medium Enterprise: The group handles credit proposals from SMEs under various lending programmes of the Bank.
- Export Services Group offers variety of advisory and value-added information services aimed at investment promotion.
- Export Marketing Services Bank offers assistance to Indian companies, to enable them establish their products in overseas markets. The idea behind this service is to promote Indian export. Export Marketing Services covers wide range of export oriented companies and organizations. EMS group also covers Project exports and Export of Services.

Besides these, the Support Services groups include:

- Research & Planning,
- Treasury and Accounts,
- Loan Administration,

- Internal Audit,
- Management Information Services,
- Information Technology,
- Legal,
- Human Resources Management and
- Corporate Communications.

Pre-shipment and Post-Shipment Finance

The term ‘export finance’ refers to credit facilities and techniques of payments at the pre-shipment and post-shipment stages. Export finance whether short-term or medium term, is provided exclusively by the Indian and foreign commercial banks which are the members of the Foreign Exchange Dealers Association.

The Reserve Bank of India (RBI) and the Industrial Development Bank of India (IDBI) provide refinance facilities to the commercial banks. Export-Import Bank of India (commonly known as EXIM Bank) also extends finance to exporters and to overseas projects abroad joint ventures and construction projects abroad.

Pre-shipment Finance:

Pre-shipment finance refers to the financial assistance provided to the exporters before actual shipment of goods. Pre-shipment finance is provided to the exporters for the purposes like purchase of raw materials, their processing and converting into finished goods and packaging them.

For these purposes, the following pre-shipment finance is made available:

- Packaging credit
- Advance against Incentives
- Advance against Duty Drawback.

Pre-shipment credits are granted by the banks under concessional rates of interest at 7.5 per cent. Credit can be extended up to a maximum period of 6 months.

Post-Shipment Finance:

Post-shipment finance may be as “any loan or advance granted or any other credit provided by a bank to an exporter of goods from India from the date of extending the credit after shipment of goods to the date of realization of export proceeds.”

Thus, post-shipment finance serves as bridge loan for the period between shipment of goods and the realization of proceeds. Such loan is usually provided for a maximum period of 6 months. Interest is charged at the rate of 8.65 per cent.

Business involves risk but export business is more prone to risks. With a view to reduce risk element in export business, the government has set up the Export Credit and Guarantee Corporation (ECGC) which provides export assistance in the form of insurance cover and guarantees. There is also an Export Inspection Council of India (EICI) which extends financial assistance to the exporters for the quality control purposes.

Types of Pre Shipment Finance

- **Packing Credit**

Advance against Cheques/Draft etc. representing Advance Payments. Pre shipment finance is extended in the following forms :

- Packing Credit in Indian Rupee
- Packing Credit in Foreign Currency (PCFC)
- Requirment for Getting Packing Credit
- This facility is provided to an exporter who satisfies the following criteria
- A ten digit importer exporter code number allotted by DGFT
- Exporter should not be in the caution list of RBI.
- If the goods to be exported are not under OGL (Open General Licence), the exporter should have the required license /quota permit to export the goods.

Packing credit facility can be provided to an exporter on production of the following evidences to the bank:

Formal application for release the packing credit with undertaking to the effect that the exporter would be ship the goods within stipulated due date and submit the relevant shipping documents to the banks within prescribed time limit.

Firm order or irrevocable L/C or original cable / fax / telex message exchange between the exporter and the buyer.

Licence issued by DGFT if the goods to be exported fall under the restricted or canalized category. If the item falls under quota system, proper quota allotment proof needs to be submitted.

The confirmed order received from the overseas buyer should reveal the information about the full name and address of the overseas buyer, description quantity and value of goods (FOB or CIF), destination port and the last date of payment.

Eligibility

Pre shipment credit is only issued to that exporter who has the export order in his own name. However, as an exception, financial institution can also grant credit to a third party manufacturer or supplier of goods who does not have export orders in their own name.

In this case some of the responsibilities of meeting the export requirements have been out sourced to them by the main exporter. In other cases where the export order is divided between two more than two exporters, pre shipment credit can be shared between them

Quantum of Finance

The Quantum of Finance is granted to an exporter against the LC or an expected order. The only guideline principle is the concept of NeedBased Finance. Banks determine the percentage of margin, depending on factors such as:

- The nature of Order.
- The nature of the commodity.
- The capability of exporter to bring in the requisite contribution.
- Different Stages of Pre Shipment Finance

Appraisal and Sanction of Limits

1. Before making any an allowance for Credit facilities banks need to check the different aspects like product profile, political and economic details about country. Apart from these things, the bank also looks in to the status report of the prospective buyer, with whom the exporter proposes to do the business. To check all these information, banks can seek the help of institution like ECGC or International consulting agencies like Dun and Brad street etc.

- The Bank extended the packing credit facilities after ensuring the following"

- The exporter is a regular customer, a bona fide exporter and has a goods standing in the market.
- Whether the exporter has the necessary license and quota permit (as mentioned earlier) or not.
- Whether the country with which the exporter wants to deal is under the list of Restricted Cover Countries(RCC) or not.
- Disbursement of Packing Credit Advance

2. Once the proper sanctioning of the documents is done, bank ensures whether exporter has executed the list of documents mentioned earlier or not. Disbursement is normally allowed when all the documents are properly executed.

Sometimes an exporter is not able to produce the export order at time of availing packing credit. So, in these cases, the bank provide a special packing credit facility and is known as Running Account Packing. Before disbursing the bank specifically check for the following particulars in the submitted documents"

- Name of buyer
- Commodity to be exported
- Quantity
- Value (either CIF or FOB)

- Last date of shipment / negotiation.

Any other terms to be complied with

- The quantum of finance is fixed depending on the FOB value of contract /LC or the domestic values of goods, whichever is found to be lower. Normally insurance and freight charged are considered at a later stage, when the goods are ready to be shipped.
- In this case disbursals are made only in stages and if possible not in cash. The payments are made directly to the supplier by drafts/bankers/cheques.
- The bank decides the duration of packing credit depending upon the time required by the exporter for processing of goods.
- The maximum duration of packing credit period is 180 days, however bank may provide a further 90 days extension on its own discretion, without referring to RBI.
- Follow up of Packing Credit Advance

3. Exporter needs to submit stock statement giving all the necessary information about the stocks. It is then used by the banks as a guarantee for securing the packing credit in advance. Bank also decides the rate of submission of these stocks.

- Apart from this, authorized dealers (banks) also physically inspect the stock at regular intervals.
- Liquidation of Packing Credit Advance

4. Packing Credit Advance needs be liquidated out of as the export proceeds of the relevant shipment, thereby converting preshipment credit into postshipment credit.

- This liquidation can also be done by the payment receivable from the Government of India and includes the duty drawback, payment from the Market Development Fund (MDF) of the Central Government or from any other relevant source.
- In case if the export does not take place then the entire advance can also be recovered at a certain interest rate. RBI has allowed some flexibility in to this regulation under which substitution of commodity or buyer can be allowed by a bank without any reference to RBI. Hence in effect the packing credit advance may be repaid by proceeds from export of the same or another commodity to the same or another buyer. However, bank need to ensure that the substitution is commercially necessary and unavoidable.
- Overdue Packing

5. Bank considers a packing credit as an overdue, if the borrower fails to liquidate the packing credit on the due date. And, if the condition persists then the bank takes the necessary step to recover its dues as per normal recovery procedure.

- Special Cases
- Packing Credit to Sub Supplier

1. Packing Credit can only be shared on the basis of disclaimer between the Export Order Holder (EOH) and the manufacturer of the goods. This disclaimer is normally issued by the EOH in order to indicate that he is not availing any credit facility against the portion of the order transferred in the name of the manufacturer.

- This disclaimer is also signed by the bankers of EOH after which they have an option to open an inland L/C specifying the goods to be supplied to the EOH as a part of the export transaction. On basis of such an L/C, the subsupplier bank may grant a packing credit to the subsupplier to manufacture the components required for exports.
- On supply of goods, the L/C opening bank will pay to the sub supplier's bank against the inland documents received on the basis of the inland L/C opened by them.
- The final responsibility of EOH is to export the goods as per guidelines. Any delay in export order can bring EOH to penal provisions that can be issued anytime.
- The main objective of this method is to cover only the first stage of production cycles, and is not to be extended to cover supplies of raw material etc. Running account facility is not granted to subsuppliers.
- In case the EOH is a trading house, the facility is available commencing from the manufacturer to whom the order has been passed by the trading house.
- Banks however, ensure that there is no double financing and the total period of packing credit does not exceed the actual cycle of production of the commodity.
- Running Account facility

2. It is a special facility under which a bank has right to grant preshipment advance for export to the exporter of any origin. Sometimes banks also extent these facilities depending upon the good track record of the exporter.

- In return the exporter needs to produce the letter of credit / firms export order within a given period of time.
- Preshipment Credit in Foreign Currency (PCFC)

3. Authorised dealers are permitted to extend Preshipment Credit in Foreign Currency (PCFC) with an objective of making the credit available to the exporters at internationally competitive price. This is considered as an added advantage under which credit is provided in foreign currency in order to facilitate the purchase of raw material after fulfilling the basic export orders.

- The rate of interest on PCFC is linked to London Interbank Offered Rate (LIBOR). According to guidelines, the final cost of exporter must not exceed 0.75% over 6 month LIBOR, excluding the tax.
- The exporter has freedom to avail PCFC in convertible currencies like USD, Pound, Sterling, Euro, Yen etc. However, the risk associated with the cross currency truncation is that of the exporter.
- The sources of funds for the banks for extending PCFC facility include the Foreign Currency balances available with the Bank in Exchange, Earner Foreign Currency Account (EEFC), Resident Foreign Currency Accounts RFC(D) and Foreign Currency(NonResident) Accounts.

- Banks are also permitted to utilize the foreign currency balances available under Escrow account and Exporters Foreign Currency accounts. It ensures that the requirement of funds by the account holders for permissible transactions is met. But the limit prescribed for maintaining maximum balance in the account is not exceeded. In addition, Banks may arrange for borrowings from abroad. Banks may negotiate terms of credit with overseas bank for the purpose of grant of PCFC to exporters, without the prior approval of RBI, provided the rate of interest on borrowing does not exceed 0.75% over 6 month LIBOR.
- Packing Credit Facilities to Deemed Exports

4. Deemed exports made to multilateral funds aided projects and programmes, under orders secured through global tenders for which payments will be made in free foreign exchange, are eligible for concessional rate of interest facility both at pre and post supply stages.

- Packing Credit facilities for Consulting Services

5. In case of consultancy services, exports do not involve physical movement of goods out of Indian Customs Territory. In such cases, Preshipment finance can be provided by the bank to allow the exporter to mobilize resources like technical personnel and training them.

- Advance against Cheque/Drafts received as advance payment

6. Where exporters receive direct payments from abroad by means of cheques/drafts etc. the bank may grant export credit at concessional rate to the exporters of goods track record, till the time of realization of the proceeds of the cheques or draft etc. The Banks however, must satisfy themselves that the proceeds are against an export order.

PRE-SHIPMENT EXPORT CREDIT

Pre-shipment Credit in Foreign Currency (PCFC)

Definition

'Pre-shipment' means any loan or advance granted or any other credit provided by a bank to an exporter for financing the purchase, processing, manufacturing or packing of goods prior to shipment, on the basis of letter of credit opened in his favour or in favour of some other person, by an overseas buyer or a confirmed and irrevocable order for the export of goods from India or any other evidence of an order for export from India having been placed on the exporter or some other person, unless lodgement of export orders or letter of credit with the bank has been waived.

General

With a view to making credit available to exporters at internationally competitive rates, authorised dealers have been permitted to extend Pre-shipment Credit in Foreign Currency (PCFC) to exporters for domestic and imported inputs of exported goods at LIBOR/EURO LIBOR/EURIBOR related rates of interest as detailed below.

Scheme

(i) The scheme is an additional window for providing pre-shipment credit to Indian exporters at internationally competitive rates of interest. It will be applicable to only cash exports.

(ii) The exporter will have the following two options to avail of export finance:

(a) to avail of pre-shipment credit in rupees and then the postshipment credit either in rupees or discounting/ rediscounting of export bills under EBR Scheme mentioned in paragraph 2.2.

(b) to avail of pre-shipment credit in foreign currency and discount/rediscounting of the export bills in foreign currency under EBR Scheme.

(iii) Choice of currency

(a) The facility may be extended in one of the convertible currencies viz. US Dollars, Pound Sterling, Japanese Yen, Euro, etc.

(b) To enable the exporters to have operational flexibility, it will be in order for banks to extend PCFC in one convertible currency in respect of an export order invoiced in another convertible currency. For example, an exporter can avail of PCFC in US Dollar against an export order invoiced in Euro. The risk and cost of cross currency transaction will be that of the exporter.2

(iv) Banks are permitted to extend PCFC for exports to ACU countries.

(v) The applicable benefit to the exporters will accrue only after the realisation of the export bills or when the resultant export bills are rediscounted 'without recourse' basis.

Source of Funds for Banks

(i) The foreign currency balances available with the bank in Exchange Earners Foreign Currency (EEFC) Accounts, Resident Foreign Currency Accounts (RFC) and Foreign currency (Non-Resident) Accounts (Banks) Scheme could be utilised for financing the pre-shipment credit in foreign currency.

(ii) Banks are also permitted to utilise the foreign currency balances available under Escrow Accounts and Exporters Foreign Currency Accounts for the purpose, subject to ensuring that the requirements of funds by the account holders for permissible transactions are met and the limit prescribed for maintaining maximum balance in the account under broad based facility is not exceeded.

(iii) Foreign currency lines of credit

(a) In addition, banks may arrange for 'lines of credit' from abroad. Banks may negotiate lines of credit with overseas banks for the purpose of grant of PCFC to exporters without the prior approval of the RBI, provided the rate of interest on the line of credit does not exceed 1 percent over six months LIBOR/EURO LIBOR/EURIBOR. Cases where the rate of interest exceeds this ceiling should be referred to RBI, Exchange Control Department, Central Office, Mumbai giving full details of the facility such as names of foreign banks/institutions, amount of foreign currency, eligibility criteria, period of facility, spread, etc. for prior approval.

(b) As soon as the terms and conditions of the lines of credit to be availed of by the bank from overseas banks have been finalised, these may be advised to the Exchange Control Department, RBI, Central Office, Mumbai.

(c) Banks should draw on the line of credit arranged only to the extent of loans granted by them to the exporters under the PCFC. However, where the overseas bank making available the line of credit stipulates a minimum amount for drawals which should not be very large, the small unutilised portion may be managed by the bank within its foreign exchange position and Aggregate Gap Limit (AGL) limit. Similarly, any pre-payment by the exporter may also be taken within the foreign exchange position and AGL limits.3

(iv) In case, the exporters have arranged for the suppliers' credit for procuring imported inputs, the PCFC facility may be extended by the banks only for the purpose of financing domestic inputs for exports.

Period of Credit

(i) The PCFC will be available as in the case of rupee credit initially for a maximum period of 180 days; any extension of the credit will be subject to the same terms and conditions as applicable for extension of rupee packing credit and it will also have additional interest cost of 2 percent above the rate for the initial period of 180 days prevailing at the time of extension.

(ii) Further extension will be subject to the terms and conditions fixed by the bank concerned and if no export takes place within 360 days, the PCFC will be adjusted at T.T. selling rate for the currency concerned. In such cases, banks can arrange to remit foreign exchange to repay the loan or line of credit raised abroad and interest without prior permission of RBI.4

Disbursement of PCFC

(i) In case, full amount of PCFC or part thereof is utilised to finance domestic input, banks may apply appropriate spot rate for the transaction.

(ii) As regards the minimum lots of transactions, it is left to the operational convenience of banks to stipulate the minimum lots taking into account the availability of their own resources. However, while fixing the minimum lot, banks may take into account the needs of their small customers also.

(iii) Banks should take steps to streamline their procedures so that no separate sanction is needed for PCFC once the packing credit limit has been authorised and the disbursement is not delayed at the branches.

Liquidation of PCFC Account

(i) General

(a) The facility of PCFC will be self-liquidating in nature. Accordingly, the PCFC should be liquidated out of proceeds of export documents on their submission for discounting/rediscounting under the EBR Scheme.

(b) The export bills will have to be discounted or covered by grant of foreign currency loans (DP bills) to liquidate the outstanding PCFC. The question of sending export bills for collection does not arise.

(c) The PCFC should not be liquidated with foreign exchange acquired from other sources.

(d) PCFC cannot be treated as a loan to be repaid in order to avail of post-shipment credit separately.

(ii) Packing credit in excess of F.O.B. value In certain cases, (viz. agro based products like HPS Groundnut, defatted & deoiled cakes, tobacco, pepper, cardamom, cashew nuts, etc.) where packing credit required is in excess of FOB value, PCFC would be available only for exportable portion of the produce.

(iii) Substitution of order/commodity Repayment/liquidation of PCFC could be with export documents relating to any other order covering the same or any other commodity exported by the exporter. While allowing substitution of contract in this way, banks should ensure that it is commercially necessary and unavoidable.

Cancellation/Non-execution of Export Order

(i) In case of cancellation of the export order for which the PCFC was availed of by the exporter from the bank, or if the exporter is unable to execute the export order for any reason, it will be in order for the exporter to repay the loan together with accrued interest thereon, by purchasing foreign exchange (principal + interest) from domestic market through the bank. In such cases, interest will be payable on the rupee equivalent of principal amount at the rate applicable to 'Export Credit Not Otherwise Specified' (ECNOS) at pre-shipment stage plus a penal rate of interest to be decided by the bank from the date of advance after adjustment of interest of PCFC already recovered. Banks are free to decide the rate of interest for ECNOS at pre-shipment stage, subject to PLR and spread guidelines.

(ii) It will also be in order for the banks to remit the amount to the overseas bank, provided the PCFC was made available to exporter from the line of credit obtained from that bank.

(iii) Banks may extend PCFC to such exporters subsequently, after ensuring that the earlier cancellation of PCFC was due to genuine reasons.

Running Account Facility for All Commodities

(i) Banks are permitted to extend the ‘Running Account’ facility under the PCFC Scheme to exporters for all commodities, on the lines of the facility available under rupee credit, subject to the following conditions:

(a) The facility may be extended provided the need for ‘Running Account’ facility has been established by the exporters to the satisfaction of the bank.

(b) Banks may extend the facility only to those exporters whose track record has been good.

(c) In all cases, where Pre-shipment Credit ‘Running Account’ facility has been extended, the L/Cs or firm orders should be produced within a reasonable period of time.

(d) The drawals made under Rupee ‘Running Account’ facility should not be converted into PCFC advances.6

(e) The PCFC will be marked-off on the ‘First-in-First-out’ basis.

(f) PCFC can also be marked-off with proceeds of export documents against which no PCFC has been drawn by the exporter.

(ii) Banks should closely monitor the production of firm order or L/C subsequently by exporters and also the end-use of funds. It has to be ensured that no diversion of funds is made for domestic use. In case of non-utilisation of PCFC drawals for export purposes, the penal provisions stated above should be made applicable and the 'Running Account' facility should be withdrawn for the concerned exporter.

(iii) Banks are required to take any prepayment by the exporter under PCFC scheme within their foreign exchange position and Aggregate Gap Limit (AGL) as indicated.

(c) above With the extension of 'Running Account' facility, mismatches are likely to occur for a longer period involving cost to the banks. Banks may charge the exporters the funding cost, if any, involved in absorbing mismatches in respect of the prepayment beyond one month period.

Forward Contracts

(i) In terms of paragraph 1.1.3 (iii) above, PCFC can be extended in any of the convertible currencies in respect of an export order invoiced in another convertible currency. Banks are also permitted to allow an exporter to book forward contract on the basis of confirmed export order prior to availing of PCFC and cancel the contract (for portion of drawal used for imported inputs) at prevailing market rates on availing of PCFC.

(ii) Banks are permitted to allow customers to seek cover in any permitted currency of their choice which is actively traded in the market, subject to ensuring that the customer is exposed to exchange risk in a permitted currency in the underlying transaction.

(iii) While allowing forward contracts under the scheme, banks may ensure compliance of the basic Exchange Control requirement that the customer is exposed to an exchange risk in the underlying transaction at different stages of the export finance.

Sharing of EPC under PCFC

(i) The rupee export packing credit is allowed to be shared between an export order holder and the manufacturer of the goods to be exported.7

(ii) Similarly, banks may extend PCFC also to the manufacturer on the basis of the disclaimer from the export order holder through his bank. PCFC granted to the manufacturer can be repaid by transfer of foreign currency from the export order holder by availing of PCFC or by discounting of bills. Banks should ensure that no double financing is involved in the transaction and the total period of packing credit is limited to the actual cycle of production of the exported goods.

(iii) The facility may be extended where the banker or the leader of consortium of banks is the same for both the export order holder and the manufacturer or, the banks concerned agree to such an arrangement where the bankers are different for export order holder and manufacturer. The sharing of export benefits will be left to the mutual agreement between the export order holder and the manufacturer.

Refinance

Banks will not be eligible for any refinance from RBI against export credit under the PCFC scheme and, as such, the quantum of PCFC should be shown separately from the export credit figures reported for the purpose of drawing export credit refinance.

Other Aspects

(i) The applicable benefits such as credit of eligible percent of export proceeds to EEFC Account etc. to the exporters will accrue only after realisation of the export bills and not at the stage of conversion of pre-shipment credit to post-shipment credit (except when bills are discounted/ rediscounted 'without recourse'). Surplus of export proceeds available after adjusting relative export finance and credit to EEFC account should not be allowed for setting-off of import bills.

(ii) ECGC cover will be available in rupees only, whereas, PCFC is in foreign currency.

(iii) For the purpose of reckoning banks' performance in extending export credit, the rupee equivalent of the PCFC may be taken into account.

Post-Shipment Export Credit - Definition

'Post-shipment Credit' means any loan or advance granted or any other credit provided by an institution to an exporter of goods from India from the date of extending credit after shipment of goods to the date of realization of export proceeds.

Rediscounting of Export Bills Abroad Scheme (EBR)

General

Banks are also allowed to rediscount export bills abroad at rates linked to international interest rates at post-shipment stage.

Exporters' Choice

The exporters have the option to avail of pre-shipment credit and postshipment credit either in rupee or in foreign currency. However, if the pre-shipment credit has been availed in foreign currency, the postshipment credit has necessarily to be under the EBR scheme since foreign currency pre-shipment credit has to be liquidated in foreign currency.

Scheme

(i) It will be comparatively easier to have a facility against bills portfolio (covering all eligible bills) than to have rediscounting facility abroad on bill by bill basis. There will, however, be no bar if rediscounting facility on bill to bill basis is arranged by an bank in case of any particular exporter, especially for large value transactions.

(ii) Banks may arrange a "Bankers Acceptance Facility" (BAF) for rediscounting the export bills without any margin and duly covered by collateralised documents.

(iii) Each bank can have its own BAF limit(s) fixed with an overseas bank or a rediscounting agency or an arrangement with any other agency such as factoring agency (in case of factoring arrangement, it should be on "without recourse" basis only).

(iv) The exporters, on their own, can arrange for themselves a line of credit with an overseas bank or any other agency (including a factoring agency) for discounting their export bills direct subject to the following conditions:

(a) Direct discounting of export bills by exporters with overseas bank and/or any other agency will be done only through the branch of a bank designated by him for this purpose.

(b) Discounting of export bills will be routed through designated bank from whom the packing credit facility has been availed of. In case, these are routed through any other bank, the latter will first arrange to adjust the amount outstanding under packing credit with the concerned bank out of the proceeds of the rediscounted bills.

(v) As soon as terms and conditions of BAF/lines of credit or similar facility with overseas bank/discounting agency or any other agency have been finalised, these may be advised by the bank or by the designated branch in the case of lines of credit negotiated directly by the exporter to the ECD, RBI, Central Office, Mumbai10 together with a copy of the agreement entered into by the bank/exporter with overseas bank/discounting agency/any other agency, as the case may be.

(vi) The limits granted to banks by overseas banks/discounting agencies under BAF will not be reckoned for the purpose of borrowing limits fixed by RBI (ECD) for them.

Eligibility Criteria

(i) The Scheme will cover mainly export bills with usance period upto 180 days from the date of shipment (inclusive of normal transit period and grace period, if any). There is, however, no bar to include demand bills if overseas institution has no objection to it.

(ii) For rediscounting export bills having payment terms beyond 180 days from date of shipment, proposals will have to be submitted to the RBI (ECD), Mumbai, furnishing all relevant details, for prior approval.

(iii) The facility under the Scheme of Rediscounting may be offered in any convertible currency.

(iv) Banks are permitted to extend the EBR facility for exports to ACU countries.

(v) For operational convenience, the BAF Scheme may be centralised at a branch designated by the bank. There will, however, be no bar for other branches of the bank to operate the scheme as per their internal guidelines/instructions.

Source of On-shore Funds

(i) There will be no bar on banks to utilise the foreign exchange resources available with them in Exchange Earners Foreign Currency Accounts (EEFC), Resident Foreign Currency Accounts (RFC), Foreign Currency (Non-Resident) Accounts (Banks) Scheme, to discount usance bills and retain them in their portfolio without resorting to rediscounting. In the case of demand bills, these may have to be routed through the existing post-shipment credit facility or by way of foreign exchange loans to the exporters out of the foreign currency balances available with banks in the Schemes ibid.

(ii) To facilitate the growth of local market for rediscounting export bills, establishment and development of an active inter-bank market is desirable. It is possible that banks hold bills in their own portfolio without rediscounting. However, in case of need, the banks should also have access to the local market, which will enable the country to save foreign exchange to the extent of the cost of rediscounting. Further, as different banks may be having BAF for varying amounts, it will be possible for a bank11 which has balance available in its limit to offer rediscounting facility to another bank which may have exhausted its limit or could not arrange for such a facility.

(iii) Banks may avail of lines of credit from other banks in India if they are not in a position to raise loans from abroad on their own or they do not have branches abroad, subject to the condition that ultimate cost to the exporter should not exceed 1percent above LIBOR/EURO LIBOR/EURIBOR excluding withholding tax. The spread between the borrowing and lending bank is left to the discretion of the banks concerned.

Accounting Aspects

(i) The Rupee equivalent of the discounted value of the export bills will be payable to the exporter and the same should be utilized to liquidate the outstanding export packing credit.

(ii) As the discounting of bills/extension of foreign exchange loans (DP bills) will be in actual foreign exchange, banks may apply appropriate spot rate for the transactions.

(iii) The Rupee equivalents of discounted amounts/foreign exchange loan may be held in the bank's books distinct from the existing post-shipment credit accounts.

(iv) In case of overdue bills banks may charge 2 percent above the rate of rediscounting of foreign exchange loan from the due date to the date of crystallization.

(v) Interest rate as per RBI interest rate directive for post-shipment credit in Rupees will be applicable from the date of crystallization.

(vi) In the event of export bill not being paid, it will be in order for the bank to remit the amount equivalent to the value of the bill earlier discounted, to the overseas bank/agency which had discounted the bill, without the prior approval of the RBI.

Restoration of Limits and Availability of Export Benefits such as

EEFC Account

As stated in paragraph 2.2.6 above, "Without Recourse" facility may not generally be available. Thus, the restoration of exporter's limits and the availability of export benefits, such as credit to EEFC accounts, in case of "with recourse" facility, will be effected only on realisation of export proceeds and not on the date of discounting/ rediscounting of the bills, However, if the bills are rediscounted12 "without recourse", the restoration of exporter's limits and availability of export benefits may be given effect immediately on rediscounting.

ECGC Cover

In the case of export bills rediscounted 'with recourse', there will not be any change in the existing system of coverage provided by Export Credit Guarantee Corporation (ECGC) as the liability of the exporter continues till the relative bill is retired/paid. In other cases, where the bills are rediscounted 'without recourse', the liability of ECGC ceases as soon as the relative bills are rediscounted.

Refinance

Banks will not be eligible for refinance from the RBI against export bills discounted/rediscounted under the Scheme and as such, the bills discounted/rediscounted in foreign currency should be shown separately from the export credit figures reported for purposes of drawing export credit refinance.

Export Credit Performance

(i) Only the bills rediscounted abroad ‘with recourse’ basis and outstanding will be taken into account for the purpose of export credit performance. The bills rediscounted abroad ‘without recourse’ will not count for the export credit performance.

(ii) Bills rediscounted ‘with recourse’ in the domestic market could get reflected only in the case of the first bank discounting the bills as that bank alone will have recourse to the exporter and the bank rediscounting will not reckon the amount as export credit.

Letter of credit

After a contract is concluded between a buyer and a seller, the buyer's bank supplies a letter of credit to the seller.

Seller consigns the goods to a carrier in exchange for a bill of lading.

Seller provides the bill of lading to bank in exchange for payment. Seller's bank then provides the bill to buyer's bank, who provides the bill to buyer.

Buyer provides the bill of lading to carrier and takes delivery of the goods.

A letter of credit is a document from a bank guaranteeing that a seller will receive payment in full as long as certain delivery conditions have been met.

In the event that the buyer is unable to make payment on the purchase, the bank will cover the outstanding amount. They are often used in international transactions to ensure that payment will be received where the buyer and seller may not know each other and are operating in different countries. In this case the seller is exposed to a number of risks such credit risk, and legal risk caused by the distance, differing laws and difficulty in knowing each party personally. A letter of credit provides the seller with a guarantee that they will get paid as long as certain delivery conditions have been met. For this reason the use of letters of credit has become a very important aspect of international trade.

The bank that writes the letter of credit will act on behalf of the buyer and make sure that all delivery conditions have been met before making the payment to the seller. Most letters of credit are governed by rules promulgated by the International Chamber of Commerce known as Uniform Customs and Practice for Documentary Credits. Letters of credit are typically used by importing and exporting companies particularly for large purchases and will often negate the need by the buyer to pay a deposit before delivery is made.

They are also used in land development to ensure that approved public facilities (streets, sidewalks, storm water ponds, etc.) will be built. The parties to a letter of credit are the supplier, usually called the "beneficiary", "the issuing bank", of whom the buyer is a client, and sometimes an advising bank, of whom the beneficiary is a client. Almost all letters of credit are irrevocable, i.e., cannot be amended or canceled without mutual consent of all parties.

Terminology

Origin

The name "letter of credit" derives from the French word "accréditation", a power to do something, which derives from the Latin "accreditivus", meaning trust.[citation needed]

Related terms

A sight LC causes payment to be made immediately to the beneficiary/seller/exporter upon presentation of the correct documents. A time or date LC specifies when payment is to be made at a future date and upon presentation of the required documents.

Negotiation means the giving of value for draft(s) or document(s) by the bank authorized to negotiate, with the nominated bank. Mere examination of the documents and forwarding the same to the LC issuing bank for reimbursement, without giving of value / agreed to give, does not constitute a negotiation.

- Advising Bank — advises the beneficiary at the request of the issuing bank.
- Applicant — the party on whose request the issuing bank issues a credit .
- Banking day—The day on which a bank is regularly open at the place at which an act to be performed.
- Beneficiary — the party who is to receive the benefit (payment) of the LC. The consignee of an LC and the beneficiary may not be the same. The credit is issued in the beneficiary's favor.
- Presentation — either delivery of documents against an LC or the document itself.
- Complying presentation — when the presentation of documents is in accordance with:

  (1) The terms and conditions of the credit

  (2) The applicable provisions of UCP

  (3) International standard banking practice
- Confirmation — a definite undertaking from the confirming bank to honor or negotiate a complying presentation in addition to that of the issuing bank.
- Confirming bank — adds confirmation to an LC. It does so at the request of the issuing bank and taking authorization from the issuing bank.
- Letter of credit/credit — an irrevocable commitment of the issuing bank to honor a complying presentation.
- Honour — to act according to commitment of the LC. Presentations are honored in different ways depending on the type of credit:

  (1) Making payment at sight for sight LC.

  (2) Incurring a deferred payment undertaking and paying at maturity for deferred payment LC.

(3) Accepting a draft drawn by the beneficiary and paying at maturity for deferred acceptance LC.

- Issuing bank — issues the LC.
- Nominated Bank — the bank with which credit is available. If no bank is mentioned in the credit as nominated bank, all banks are "nominated".
- Negotiation — A nominated bank is said to negotiate a document if it purchases a draft or documents under a complying presentation either by making an advance or agreeing to advance funds to the beneficiary on or before the date on which reimbursement is due to the nominated bank. A draft drawn on a nominated bank cannot be purchased separately.

Documents that can be presented for payment

To receive payment, an exporter or shipper must present the documents required by the LC. Typically, the payee presents a document proving the goods were sent instead of showing the actual goods. The original bill of lading (BOL) is normally the document accepted by banks as proof that goods have been shipped. However, the list and form of documents is open to negotiation and might contain requirements to present documents issued by a neutral third party evidencing the quality of the goods shipped, or their place of origin or place. Typical types of documents in such contracts include:

- Financial Documents — Bill of Exchange, co-accepted draft
- Commercial Documents — Invoice, packing list
- Shipping Documents — Transport document, insurance certificate, commercial, official or legal documents
- Official Documents — License, embassy legalization, origin certificate, inspection certificate, phytosanitary certificate
- Transport Documents — Bill of lading (ocean or multi-modal or charter party), airway bill, lorry/truck receipt, railway receipt, CMC other than mate receipt, forwarder cargo receipt
- Insurance documents — Insurance policy or certificate, but not a cover note.

Legal principles governing documentary credits

One of the primary peculiarities of the documentary credit is that the payment obligation is independent from the underlying contract of sale or any other contract in the transaction. Thus the bank's obligation is defined by the terms of the LC alone, and the sale contract is irrelevant. The defenses available to the buyer arising out of the sale contract do not concern the bank and in no way affect its liability. Article 4(a) of the UCP states this principle clearly. Article 5 of the UCP further states that banks deal with documents only, they are not concerned with the goods (facts). Accordingly, if the documents tendered by the beneficiary, or his or her agent, are in order, then in general the bank is obliged to pay without further qualifications.

The policies behind adopting the abstraction principle are purely commercial and reflect a party's expectations: first, if the responsibility for the validity of documents was thrown onto banks, they would be burdened with investigating the underlying facts of each transaction, and less inclined to issue documentary credits because of the risk and inconvenience. Second, documents required under the LC could in certain circumstances be different from those required under the sale transaction. This would place banks in a dilemma in deciding which terms to follow if required to look behind the credit agreement. Third, the fact that the basic function of the credit is to provide a seller with the certainty of payment for documentary duties suggests that banks should honor their obligation notwithstanding allegations of buyer misfeasance. Courts have emphasized that buyers always have a remedy for an action upon the contract of sale and that it would be a calamity for the business world if a bank had to investigate every breach of contract.

The “principle of strict compliance” also aims to make the bank’s duty of effecting payment against documents easy, efficient and quick. Hence, if the documents tendered under the credit deviate from the language of the credit the bank is entitled to withhold payment, even if the deviation is purely terminological. The general legal maxim de minimis non curat lex has no place in the field.

Types

- Import/export — The same credit can be termed an import or export LC depending on whose perspective is considered. For the importer it is termed an Import LC and for the exporter of goods, an Export LC.
- Revocable — the buyer and the bank that established the LC are able to manipulate the LC or make corrections without informing or getting permissions from the seller. According to UCP 600, all LCs are irrevocable, hence this type of LC is obsolete.
- Irrevocable — any changes (amendment) or cancellation of the LC (except it is expired) is done by the applicant through the issuing bank. It must be authenticated and approved by the beneficiary.
- Confirmed — An LC is said to be confirmed when a second bank adds its confirmation (or guarantee) to honor a complying presentation at the request or authorization of the issuing bank.
- Unconfirmed — this type does not acquire the other bank's confirmation.
- Transferrable — the exporter has the right to make the credit available to one or more subsequent beneficiaries. Credits are made transferable when the original beneficiary is a middleman and does not supply the merchandise, but procures goods from suppliers and arranges them to be sent to the buyer and does not want the buyer and supplier knows each other.
- The middleman is entitled to substitute his own invoice for the supplier's and acquire the difference as profit.
- A letter of credit can be transferred to the second beneficiary at the request of the first beneficiary only if it expressly states that the letter of credit is "transferable". A bank is not obligated to transfer a credit.
- A transferable letter of credit can be transferred to more than one alternate beneficiary as long as it allows partial shipments.

- The terms and conditions of the original credit must be replicated exactly in the transferred credit. However, to keep the workability of the transferable letter of credit, some figures can be reduced or curtailed.

Amount

- Unit price of the merchandise (if stated)
- Expiry date
- Presentation period
- Latest shipment date or given period for shipment.
- The first beneficiary may demand from the transferring bank to substitute for the applicant. However, if a document other than the invoice must be issued in a way to show the applicant's name, in such a case that requirement must indicate that in the transferred credit it will be free.
- Transferred credit cannot be transferred again to a third beneficiary at the request of the second beneficiary.
- Untransferable — A credit that the seller cannot assign all or part of to another party. In international commerce, all credits are untransferable.
- Deferred / Usance — A credit that is not paid/assigned immediately after presentation, but after an indicated period that is accepted by both buyer and seller. Typically, seller allows buyer to pay the required money after taking the related goods and selling them.
- At Sight — A credit that the announcer bank immediately pays after inspecting the carriage documents from the seller.
- Red Clause — Before sending the products, seller can take the pre-paid part of the money from the bank. The first part of the credit is to attract the attention of the accepting bank. The first time the credit is established by the assigner bank, is to gain the attention of the offered bank. The terms and conditions were typically written in red ink, thus the name.
- Back to Back — A pair of LCs in which one is to the benefit of a seller who is not able to provide the corresponding goods for unspecified reasons. In that event, a second credit is opened for another seller to provide the desired goods. Back-to-back is issued to facilitate intermediary trade. Intermediate companies such as trading houses are sometimes required to open LCs for a supplier and receive Export LCs from buyer.

Pricing

Issuance charges, covering negotiation, reimbursements and other charges are paid by the applicant or as per the terms and conditions of the LC. If the LC does not specify charges, they are paid by the Applicant.

Legal basis

Legal writers have failed to satisfactorily reconcile the bank's undertaking with any contractual analysis. The theories include: the implied promise, assignment theory, the novation theory, reliance theory, agency theories, estoppels and trust theories, anticipatory theory and the guarantee theory.

Although documentary credits are enforceable once communicated to the beneficiary, it is difficult to show any consideration given by the beneficiary to the banker prior to the tender of documents. In such transactions the undertaking by the beneficiary to deliver the goods to the applicant is not sufficient consideration for the bank's promise because the contract of sale is made before the issuance of the credit, thus consideration in these circumstances is past.

International Trade Payment methods

International Trade Payment method can be done in the following ways.

- Advance payment (most secure for seller) — The buyer parts with money first and waits for the seller to forward the goods.
- Documentary Credit (more secure for seller as well as buyer) — Subject to ICC's UCP 600, the bank gives an undertaking (on behalf of buyer and at the request of applicant) to pay the beneficiary the value of the goods shipped if acceptable documents are submitted and if the stipulated terms and conditions are strictly complied with. The buyer can be confident that the goods he is expecting only will be received since it will be evidenced in the form of certain documents called for meeting the specified terms and conditions while the supplier can be confident that if he meets the stipulations his payment for the shipment is guaranteed by bank, who is independent of the parties to the contract.
- Documentary collection (more secure for buyer and to a certain extent to seller) — Also called "Cash against Documents". Subject to ICC's URC 525, sight and usance, for delivery of shipping documents against payment or acceptances of draft, where shipment happens first, then the title documents are sent to the buyer's bank by seller's bank, for delivering documents against collection of payment/acceptance
- Direct payment (most secure for buyer) — The supplier ships the goods and waits for the buyer to remit the bill, on open account terms.

Risk situations

Fraud Risks

- The payment will be obtained for nonexistent or worthless merchandise against presentation by the beneficiary of forged or falsified documents.
- Credit itself may be funded.
- Sovereign and Regulatory Risks
- Performance of the Documentary Credit may be prevented by government action outside the control of the parties.

Legal Risks

Possibility that performance of a documentary credit may be disturbed by legal action relating directly to the parties and their rights and obligations under the documentary credit.

Force Majeure and Frustration of Contract

Performance of a contract – including an obligation under a documentary credit relationship – is prevented by external factors such as natural disasters or armed conflicts.

Applicant

- Non-delivery of Goods
- Short shipment
- Inferior quality
- Early / late shipment
- Damaged in transit
- Foreign exchange
- Failure of bank viz issuing bank / collecting bank

Issuing Bank

- Insolvency of the applicant
- Fraud risk, sovereign and regulatory risk and legal risks

Reimbursing Bank

- No obligation to reimburse the claiming bank unless it has issued a reimbursement undertaking.

Beneficiary

- Failure to comply with credit conditions
- Failure of, or delays in payment from, the issuing bank

Export-Import Bank of India – Role, Functions and Facilities

Export-Import Bank of India (Exim Bank) was set up by an Act of the Parliament "THE EXPORT-IMPORT BANK OF INDIA ACT, 1981" for providing financial assistance to exporters and importers, and for functioning as the principal financial institution for co-ordinating the working of institutions engaged in financing export and import of goods and services with a view to promoting the country's international trade and for matters connected therewith or incidental thereto.

EXIM Bank has two broad business streams: one, the traditional export finance typical of export credit agencies around the world and two, financing of export oriented units (export capability creation), which are non-traditional for export credit agencies. Since inception, Exim Bank has been the principal financial institution in the country for financing project exports and exports on deferred credit terms. As per

Memorandum PEM (MEMORANDUM OF INSTRUCTIONS ON PROJECT EXPORTS AND SERVICE EXPORTS) of Reserve Bank of India, the following constitute project exports:

i. Supply of goods / equipment on deferred payment terms
ii. Civil construction contracts
iii. Industrial turnkey projects
iv. Consultancy / services contracts

Exim Bank extends funded and non-funded facilities for overseas turnkey projects, civil construction contracts, technical and consultancy service contracts as well as supplies.

- Turnkey Projects are those which involve supply of equipment along with related services, like design, detailed engineering, civil construction, erection and commissioning of plants and power transmission & distribution
- Construction Projects involve civil works, steel structural works, as well as associated supply of construction material and equipment for various infrastructure projects.
- Technical and Consultancy Service contracts, involving provision of know-how, skills, personnel and training are categorised as consultancy projects. Typical examples of services contracts are: project implementation services, management contracts, and supervision of erection of plants, CAD / CAM solutions in software exports, finance and accounting systems.
- Supplies: Supply contracts involve primarily export of capital goods and industrial manufactures. Typical examples of supply contracts are: supply of stainless steel slabs and ferro-chrome manufacturing equipments, diesel generators, pumps and compressors.

EXIM Bank, under powers delegated vide the PEM, provides post-award clearance for project export contracts valued up to USD 100 million. Project export contracts valued above USD 100 million need to be provided post-award clearance by the inter-institutional Working Group. The Working Group is a single-window clearance mechanism, comprising Exim Bank as the convener and nodal agency, RBI – Foreign Exchange Department and Export Credit Guarantee Corporation of India Ltd. [ECGC]. In the case of very large value projects, officials of Ministry of Finance, Ministry of Commerce and Industry and Ministry of External Affairs, Government of India, are invited to participate in the Working Group Meetings. In order to obtain immediate clarifications for speedy clearance of proposals by the Working Group, the exporters concerned and their bankers are also associated with the meetings. With the same objective, participation of the main sub-suppliers, sub-contractors or other associates and their bankers in such meetings is also encouraged, particularly in respect of proposals for high value contracts. Exim Bank also plays the role of a financier and provides funded and non-funded support for project export contracts of Indian Entities.

In addition to project exports, Exim Bank also extends fund-based and non-fund-based facilities to deemed export contracts as defined in Foreign Trade Policy of GOI, e.g.,

- secured under funding from Multilateral Funding Agencies like the World Bank, Asian Development Bank, etc.;
- contracts secured under International Competitive Bidding;
- contracts under which payments are received in foreign currency.

EXIM Bank offers the following Export Credit facilities, which can be availed of by Indian companies, commercial banks and overseas entities.

For Indian Companies executing contracts overseas

- **Pre-shipment credit**

EXIM Bank's Pre-shipment Credit facility, in Indian Rupees and foreign currency, provides access to finance at the manufacturing stage - enabling exporters to purchase raw materials and other inputs.

Pre-shipment credits are usually extended by exporters' commercial banks for period upto 180 days. Exim Bank extends pre-shipment / post-shipment credit either directly or in participation with commercial banks. In order to offer one-stop banking products to export clients, the Bank has also been offering short-term pre / post shipment credit either directly or through exporter's bankers. Exim Bank may consider extending pre-shipment credit and post-shipment credit for periods exceeding 180 days, on case-to-case basis and subject to the merits of the case.

- **Supplier's Credit**

This facility enables Indian exporters to extend term credit to importers (overseas) of eligible goods at the post-shipment stage.

Post-shipment Supplier's Credit can be extended to Indian exporters upto the extent of the deferred credit portion of the export contract, either in Rupees or in Foreign currency. The period of deferred credit and moratorium will generally depend on the nature of goods [List A and List B of Memorandum PEM] or nature of projects, as per guidelines contained in the Memorandum PEM of RBI.

For Project Exporters

- **Export Project Cash-Flow Deficit Financing Programme [EPCDF]**

Indian project exporters (including those under Deemed Exports category) incur expenditure in rupee or foreign currency while executing contracts i.e. costs of mobilisation/acquisition of materials, personnel and equipment etc. Exim Bank's facility helps them meet these expenses for -

a) Project Export Contracts;
b) contracts in India categorized as Deemed Exports in the Foreign Trade Policy of India.

- **Capital Equipment Finance Programme (CEFP)**

Capital Equipment Finance Programme [CEFP] has been conceived to cater to capital expenditure for procurement of capital equipment to be utilized across multiple contracts. CEFP provides direct access to Exim

Bank's finance for eligible Indian companies for procurement of indigenous and imported capital equipment for executing overseas projects / deemed export projects.

For Exporters of Consultancy and Technological Services

EXIM Bank offers a special credit facility to Indian exporters of consultancy and technology services, so that they can, in turn, extend term credit to overseas importers.

Guarantee Facilities

Indian companies can avail of guarantee facilities of different types to furnish requisite guarantees to facilitate execution of export contracts (including deemed export contracts) and import transactions.

- **Advance Payment Guarantee (APG)**: Issued to project exporters to secure a project mobilization advance as a percentage (10-20%) of the contract value, which is generally recovered on a pro-rata basis from the progress payment during project execution.
- **Performance Guarantee (PG)**: PG for up to 5-10% of contract value is issued valid until completion of maintenance period and/or grant of Final Acceptance Certificate (FAC) by the overseas employer/client.
- **Retention Money Guarantee (RMG)**: This enables the exporter to obtain the release of retained payments from the client prior to issuance of Project Acceptance Certificate (PAC)/ Final Acceptance Certificate (FAC).
- **Other Guarantees**: e.g. in lieu of customs duty or security deposit for expatriate

labour, equipment etc.

- **Eligibility**: Indian project exporters securing overseas or deemed export contracts.

For Overseas Entities

- **Buyer's Credit**

Overseas buyers can avail of Buyer's Credit from Exim Bank, for import of eligible goods from India on deferred payment terms. As per Memorandum PEM guidelines, RBI has authorised Exim Bank to extend overseas buyer's credits upto USD 20 mn for project exports without seeking approval of RBI.

The facility enables exporters/contractors to expand abroad and into non-traditional markets. It also enables exporters/contractors to be competitive when bidding or negotiating for overseas jobs.

Benefits to Foreign Customers

- Enables overseas buyers to obtain medium-and long-term financing
- Competitive interest rate against host country's high cost of borrowing.
- **Eligibility:**

Buyer's Credit is extended to a foreign project company that intends to award the project execution to an Indian project exporter. The financing will be available to all kinds of projects and service exports from India. Facility is available for development, upgrading or expansion of infrastructure facilities; financing of public or private projects such as plants and buildings; professional services such as surveyors, architecture, consultations, etc.

- **Buyer's Credit under NEIA**

Buyer's Credit – NEIA is a unique financing mechanism that provides a safe mode of non-recourse financing option to Indian exporters and serves as an effective market entry tool to traditional as well as new markets in developing countries, which need deferred credit on medium or long-term basis.

Under this facility, Exim Bank facilitates project exports from India by way of extending credit to overseas sovereign governments and government owned entities for import of Indian goods and services from India on deferred credit terms. Exim Bank will obtain credit insurance cover under NEIA through ECGC. NEIA is a trust set up by the Ministry of Commerce and administered by Export Credit & Guarantee Corporation of India (ECGC).Facility is available for project exports requiring medium or long term deferred credit.

- **Eligibility:**

Exim Bank extends the credit directly to overseas buyer of projects from India without recourse to Indian exporter. Borrower should be overseas sovereign governments or government owned entities. Amount of Loan should generally not be more than 85% of the contract value. Sovereign guarantee is needed where the borrower is other than the foreign government. Any other security may be stipulated on a case-to-case basis.

Project Finance menu of funded and non-funded facilities to Indian exporters

The Project Finance menu of funded and non-funded facilities to Indian exporters, commercial banks in India and overseas entities is given below:

<table>
<tr><td>For Indian Exporters</td><td>For Commercial Banks in India</td></tr>
<tr><td rowspan="3">❖ Post-shipment Supplier's Credit
❖ Export Project Cash flow Deficit Financing Program
❖ Pre-shipment Credit in Rupee and Foreign Currency
❖ Finance for Export of Consultancy and Technology Services
❖ Finance for Deemed Export contracts
❖ Capital Equipment Finance
❖ Financing Deemed Export contracts secured via structures including but not restricted to BOT / BOO / BOOT / BOLT
❖ Letters of Credit / Guarantees</td><td>❖ Risk participation in funded / non-funded facilities extended to Indian exporters.
❖ Refinance of Export Credit</td></tr>
<tr><td>For Overseas Entities</td></tr>
<tr><td>❖ Buyer's Credit
❖ Buyer's Credit under NEIA</td></tr>
</table>

RBI’s Memorandum PEM has to be referred for Project and Service Exports.

Export Capability Creation loans extended by the Bank may be classified into three broad categories viz. finance for overseas investment, finance for export oriented units and finance for financial intermediaries. Besides loans, the Bank also extends non-fund based assistance by way of guarantees and Letters of Credit (L/Cs). The three categories are discussed as under:

<table>
<tr><td>1. Overseas Investment</td><td>✓ Term Financing – to overseas Joint Ventures/ Wholly Owned Subsidiaries as well as to Indian companies towards part financing their equity investment in overseas JV/ WOS.
✓ Equity Investment – Participation in equity of overseas ventures of Indian companies.
✓ Working Capital Loans to JVs/WOSs
✓ Guarantees to JVs/WOSs</td></tr>
<tr><td>2. Export- Oriented Units</td><td>✓ Asset Creation
o Equipment Finance
o Project Finance
✓ Working Capital
o Medium Term (LTWC, WCTL)
o Short Term Finance
✓ Special Products
o Export Marketing Finance
o Export Product Development Finance
o Export Vendor Development Finance
o Research & Development (R&D) Finance
o Finance for Indian Educational Institutions and setting up institutions abroad
o Finance for Software Technology Parks
o Finance for Development of Minor Ports / Jetties
o Creative Industry Financing
o Project-related non-fund based guarantees
o Guarantees and stand-by LCs (SBLCs)
o Letters of Credit (LCs)</td></tr>
<tr><td>3. Financial</td><td>✓ Refinance to Commercial Banks</td></tr>
</table>

Intermediaries (banks)	✓ Export Bills Rediscounting for commercial banks.

The primary objective of providing Export Capability Creation loans is to facilitate export production and international competitiveness of borrower companies. Exim Bank provides a comprehensive range of products and services covering financial needs of the borrower companies at all stages of their business cycle. The Bank’s vision is to develop commercially viable relationships with a target set of externally oriented companies by offering them a comprehensive range of products and services aimed at enhancing their internationalisation efforts.

Overseas Investment Finance Programme

EXIM Bank encourages Indian companies to invest abroad for, inter alia, setting up manufacturing units and for acquiring overseas companies to get access to the foreign market, technology, raw materal, brand, IPR etc. For financing such overseas investments, Exim Bank provides:

a) Term loans to Indian companies upto 80% of their equity investment in overseas JV/ WOS.

b) Term loans to Indian companies towards upto 80% of loan extended by them to the overseas JV/ WOS.

c) Term loans to overseas JV/ WOS towards part financing

- Capital expenditure towards acquisition of assets,
- Working capital,
- Equity investment in another company,
- Acquisition of brands/ patents/ rights/ other IPR,
- Acquisition of another company,
- Any other activity that would otherwise be eligible for finance from Exim Bank had it been an Indian entity.

d) Guarantee facility to the overseas JV/ WOS for raising term loan/ working capital.

Eligibility to avail finance or services:

EXIM Bank's funded/ non-funded assistance is generally with recourse to the Indian promoter Company. Exim Bank financing is available in Indian Rupees (to the Indian borrower) and in foreign currency [as per extant RBI guidelines]. The tenor range is usually 5-7 years with a suitable moratorium, and repayments in suitable monthly/ quarterly installments. Promoter margin is minimum 20% and security will include inter alia appropriate charge on the assets of the overseas entity, Corporate Guarantee of the Indian promoter backed by appropriate charge on its assets, Political and/ or commercial risk cover, Pledge of shares held by the Indian promoter in the overseas venture etc.

Export- Oriented Units, Corporate Banking

The Bank offers a number of financing programmes for Export Oriented Units (EOUs), importers and for companies making overseas investments. The financing programmes cater to the term loan requirements of Indian exporters for financing their new project, expansion, modernization, purchase of equipment, R&D, overseas investments and also the working capital requirements.

Finance for Corporate

Research & Development Finance for Export Oriented Units:

EXIM Bank encourages Indian exporters to invest more in their R&D spending in order to develop new products/processes/ IPRs for enhancing export capabilities. Considering the need to bridge the funding gap of Indian exporters in R&D space, the Bank has a dedicated R&D Financing Programme. Under the said Programme, financing for R&D can be extended to any export oriented company/ SPV promoted by companies, irrespective of the nature of industry. The financing covers both capital and revenue expenditure including inter alia:

- Land and building, civil works for housing eligible R&D activities;
- Equipments, tools, computer hardware/ software, miscellaneous fixed assets used in eligible R&D activities;
- Acquisition of technology from India or overseas at the "proof of concept" or design stage, which will be used to develop new product/ process.
- Salaries of R&D personnel, support staff during the R&D project phase including training costs;
- Cost of regulatory approvals, filing and maintenance of patent registration;
- Product documentation and allied costs during the R&D project phase.
- Costs of materials, surveys, technology demonstration studies and field trial
- Any other costs to enhance R&D capability.

Eligibility:

- Export oriented firms with exports (actual/projected) of at least 5 crores or 10% of annual turnover.
- R&D finance is generally extended upto 7 years. However, longer tenors with suitable interest resets would be permissible. Structured repayment can be considered to match the cash flow.
- Upto 80% of the total project cost can be funded.
- Security to include, inter alia, appropriate charge on the assets, Corporate Guarantee, charge/ assignment on the regulatory approval/ IPR, personal guarantee etc.

Pre-shipment/Post-shipment Credit Programme:

EXIM Bank extends export credit to Indian exporters to meet a wide range of trade financing requirements for execution of an export transaction. The Bank provides working capital finance by way pre-shipment credit and post-shipment credit. Bank also extends as part of export credit assistance, non-fund based limits inter alia including issuance of Letters of Credit (both Foreign & inland) and Bank Guarantees (both Foreign & inland) for its clients. The credit limits are generally extended as part of Borrower's consortium limit and are operated as a running account facility. The limits may be renewed for further period subject to satisfactory review of account and depending on the Borrower's export credit requirement. The facilities can be drawn in either Indian Rupee or Foreign Currency.

Eligibility:

- Indian exporters with a track record.
- The limit should be within the MPBF of Borrower's assessed bank finance.
- Margin of 15-20% under pre-shipment and 0-10% under post-shipment.
- Adequate security to be provided. Typical security includes appropriate charge on the current assets including export receivables, ECGC cover etc.

Lending Programme for Export Oriented Units:

EXIM Bank provides term loans to export oriented Indian companies to finance various capital expenditures including certain soft expenditures in order to improve their export capability and to enhance their international competitiveness. Loans/Guarantees are extended for the following purposes: Expansion, modernization, up gradation or diversification projects including acquisition of equipment, technology etc.; export marketing; export product development; setting up of Software Technology Parks;

Eligibility:

Manufacturing/trading/services companies with a minimum export orientation (actual/projected) of 10% of their annual turnover, or exports of 5 crore p.a., whichever is lower [inclusive of exports through Export/Trading Houses], are eligible to avail finance from Exim Bank. Exim Bank financing is available in Indian Rupees and in foreign currency [as per extant RBI guidelines]. The tenor range is usually 7-10 years with a suitable moratorium, and repayments in suitable monthly/ quarterly installments. Promoter margin is minimum 20% and appropriate charge on the fixed assets of the company/project plus any other acceptable security including personal guarantees may be stipulated.

Finance for MSMEs

Apart from the Corporate Banking facilities, there are additional services that Exim Bank offers to support Small and Medium Enterprises.

SME-ADB Line:

EXIM Bank has arranged for a credit line from the Asian Development Bank (ADB) for providing foreign currency term loans to the MSME borrowers in certain specific lagging states of India, viz. Assam, Madhya Pradesh, Orissa, Uttar Pradesh, Chhattisgarh, Jharkhand, Rajasthan and Uttarakhand. These foreign currency term loans can also finance domestic capital expenditure of the borrowers in Indian Rupees, besides meeting their foreign currency capital expenditure requirements. The assistance to these MSMEs will help in increasing competitiveness in the relatively backward states and help in integrating them into the mainstream economy.

Eligibility:

Export oriented MSMEs (as defined in MSMED Act, 2006) incorporated in the above mentioned lagging states

Purpose: To meet long term foreign currency loan requirements of Indian exporting entities in the MSME sector for financing their eligible capital expenditure. pertaining to inter alia setting up of new facilities, expansion/modernization of existing facilities, acquisition of equipment and plant & machinery, setting up of testing/R&D facilities, setting up of captive power plants/co-generation plant, setting up of infrastructure facilities like effluent treatment plants, storages/warehouses, etc. The Tenor of the loan will be upto 7 years including suitable moratorium.

For cluster of Indian MSME EOUs

EXIM Bank, besides providing financial assistance to individual MSME EOUs, also provides financial assistance to Special Purpose Vehicles (SPVs) of a cluster of MSMEs. Term loans are provided to such clusters of MSME units for the following activities:

- Development of new geographically contiguous cluster/industrial park, involving creation & maintenance of common infrastructure and common facilities, including inter alia construction of buildings and civil works, acquisition of assets/technology, for the benefit of industrial units within the cluster/industrial park.
- Development of an industrial estate, by industrial users, industry associations and/or Government bodies.
- Up-gradation of an existing industrial cluster or industrial estate.
- Development of specific infrastructure, including common effluent treatment plant, captive power plant, transportation linkages, hazardous waste disposal.
- Development of Common Facilities Centers like testing centers, cold storages, for industrial clusters, industrial estates, or a group of industries with common interests.

Technology & Innovation Enhancement and Infrastructure Development Fund (TIEID):

With a view to facilitate credit flow to the MSME sector at competitive rates, Exim Bank has set up a Technology and Innovation Enhancement and Infrastructure Development (TIEID) fund of USD 500 mn exclusively for MSMEs, to augment their export competitiveness and internationalisation efforts, by partnering with banks / FIs. TIEID seeks to meet long term foreign currency loan requirements of Indian exporting entities in the MSME sector for meeting capital expenditure, through refinancing of Banks / FIs against their eligible SME financing portfolio.

Eligibility:

Scheduled Commercial Banks / Financial institutions in India having acceptable credit risk for on-lending to MSME units.

Eligible Beneficiary:

Ultimate Beneficiary of the Foreign Currency funds provided to eligible Banks/FIs shall be MSME units in India having a minimum export orientation of 10% of annual turnover or exports of ` 5 crores p.a in absolute terms, whichever is lower. The loan should be used to meet long term foreign currency loan requirements of Indian exporting entities in the MSME sector for meeting eligible capital expenditure. Eligible capital expenditure include technology up gradation, capacity creation, common infrastructure development like captive power plant, common effluent treatment plant, hazardous waste disposal facility, testing facilities etc.

Lending Programme for Financing Creative Economy:

The Creative Industries are those industries which have their origin in individual creativity, skill and talent and which have a potential for wealth and Job creation through the generation and exploitation of intellectual property viz., Advertising, Architecture, Art and Antiques Market, Crafts, Design, Designer Fashion, Film and Video, Interactive Leisure Software, Music, Performing Arts, Publishing, Software and Computer Services, Television and Radio etc. In view of the large untapped potential for increasing exports by the creative industries and in order to provide a strategic focus to this sector and enhance Exim Bank's presence in the creative economy space, and as a corollary, in the MSME segment, Exim Bank has introduced a Programme specifically for financing the Creative Economy.

Eligibility:

The illustrative list of industry sectors include Heritage {Traditional Cultural Expressions (Art & Crafts, Festivals, Celebrations etc), Cultural Sites (Historical Monuments, Museums, Libraries, Archives etc)}; Arts {Visual Arts (Painting, Sculpture, Antique, Photography etc), Performing Arts (Live Music, Theatre, Dance, Opera, Puppetry etc)}; Media { Publishing & Printed Media (Books, Newspapers, Press & other Publications), Audio Visuals (Film, TV & Radio, Broadcasting etc), New Media (Digitised Content, Software, Video Games, Animations etc); Functional Creations { Design (Interior, Graphic, Fashion, Jewellery, Toys etc), Creative Services (Architecture, Advertising, Creative R & D, Cultural Services, Digital Services etc)}

Finance for Grassroots Enterprises

The Bank supports globalisation of enterprises based out of rural areas of the country through its GRID programme. Through this initiative, the Bank extends financial support to promote grassroots initiatives/technologies, particularly those having export potential. The objective of the programme is to help artisans/producer groups/clusters/small enterprises across the country realize remunerative return on their produce essentially through facilitating exports from these units. The group handles credit proposals from such organizations working at the rural /grassroots level and offers tailor-made financial products to cater to their needs. The group is mandated to work towards developing a robust, vibrant and holistic approach in its intervention by providing assistance at various stages of product development / business cycle including capacity building, export capability creation, expansion/diversification and finally exports. The broad areas of support extended by the Bank through its grassroots initiatives inter alia, include capacity building, development of common facility centres, construction of raw material bank, technology up-gradation and creation of export capability.

ELIGIBILITY:

The organisations eligible for support should meet various criteria including, but not limited to the following:

- Should be a legal entity registered under respective State/Central Govt. Act as a Society, Trust, Co-operative, Private Limited Company, Producer Company, or NGO etc;
- Should be working with communities at grassroots level for promoting income generating activities (IGAs) based on the traditional skills using indigenous or locally available materials in the areas of product development & design, capacity building, market development etc.;
- Should have proven track record of creating /adopting sustainable livelihood model which could be up-scaled and replicated across the geographies sharing similar characteristics (demographic, cultural, socio-economic similarities, etc
- Should be exporting, directly or indirectly

A **Line of Credit (LOC)** is a financing mechanism through which Exim Bank extends support for export of projects, equipment, goods and services from India. Exim Bank extends LOCs on its own and also at the behest and with the support of Government of India. Exim Bank extends Lines of Credit to:

a) Foreign Governments or their nominated agencies such as central banks, state owned commercial banks and organizations;

b) National or regional development banks;

c) Overseas financial institutions;

d) Commercial banks abroad;

e) Other suitable overseas entities.

The above mentioned recipients of LOCs act as intermediaries and on lend to overseas buyers for import of Indian equipment, goods and services. LOC is a financing mechanism that provides a safe mode of non-recourse financing option to Indian exporters to enter new export markets or expand business in existing export markets without any payment risk from the overseas importers.

BROAD GUIDELINES AND PROCEDURE FOR GOVERNMENT OF INDIA SUPPORTED LINES OF CREDIT

The Government of India (GOI), in 2003-04, formulated the Indian Development Initiative (IDI), now known as Indian Development and Economic Assistance Scheme [IDEAS] with the objective of sharing India's development experience through,

(a) Capacity building and skills transfer,

(b) Trade, and

(c) Infrastructure development,

by extending concessional Lines of Credit (LOCs) routed through Exim Bank, to developing partner countries, towards creating socio-economic benefits in the partner country. Recently, the Ministry of External Affairs (MEA) has set up the Development Partnership Administration (DPA) Division to deal with India's development assistance programmes abroad, including LOCs routed through Exim Bank. These LOCs are now increasingly being extended to partner countries for large-scale and complex projects (project exports from India).

Bilateral or multilateral assistance, through lines of credit, typically follows a sequence of standard procedures, viz.

a) Project identification and preparation,

b) Review and approval of the project proposal,

c) Offer of the loan, acceptance and execution of loan agreement,

d) Project implementation, monitoring and supervision, and

e) Socio-economic impact assessment after project completion.

The lessons learned from the impact assessment / evaluation act as a feedback to the preparation, review and implementation of future projects. This process forms the 'project cycle.'

Broad guidelines and procedure EXIM bank's own commercial lines of credit

EXIM Bank, since its inception, has been extending LOCs to various countries to promote export of Indian projects, products and services. Under the LOCs extended by Exim Bank to overseas financial institutions, foreign governments, regional and national development banks and commercial banks, Exim Bank finances all items eligible for being exported under the 'Foreign Trade Policy' of Government of India. The credit periods for these LOCs are generally up to 7 years and the LOCs typically carry LIBOR-linked interest rates.

Research & Analysis

EXIM Bank's Research & Analysis Group (RAG) offers a vast range of research products. The Bank's team of experienced economists and strategists provide insights on aspects of international economics, trade and investment through qualitative and quantitative research techniques. RAG monitors the global trends in the world and domestic economies and the impact of these trends, especially on India and other developing economies. RAG caters to the constituents within the Bank, as well as to those external to the Bank such as Government, RBI, exporters/importers, trade & industry associations, external credit agencies, academic institutions and researchers.

The research work carried out in the Group under the broad classification of regional, sectoral and policy related studies, are published in the form of Occasional Papers, Working Papers, Books, etc. These research studies primarily envisage identifying avenues for enhancing India's international engagement.

The group also undertakes country profiles, which assess the economic, political, currency and credit risks involved, along with the export opportunities in the country concerned. Further the profiles provide short-to-medium term economic outlook of a country, indicating the economic risk involved in doing business with country.

As a part of the support services and with an objective to provide contemporary information to Indian traders and investors, the group disseminates information on export opportunities and highlights developments that have a bearing on Indian exports, through its quarterly bulletin, Eximius: Export Advantage. The newsletter comprises of regional and industry outlooks, Bank's activities, opportunities in multilateral funded projects and contract awards, review on select traded currencies and countries, and a section on the happenings during the quarter. The newsletter is a free publication, effectively distributed to a wide network of scholars, economists, institutions, Government of India offices, and export promoting organisations.

The Bank also brings out a bi-monthly publication titled 'Agri Export Advantage' in English, Hindi and 10 regional languages (Assamese, Bengali, Gujarati, Kannada, Marathi, Malayalam, Oriya, Punjabi, Tamil, and Telugu). The newsletter provides stakeholders of Indian agribusiness with updates on global agri-environment and markets, research reports on agri-commodities, international issues related to agri-business, prospective areas of agribusiness, agricultural trade and trade policies, regulatory issues in international trade, WTO Government schemes and assistance, latest international news brief and Bank's activities to promote agri-export from India.

The Bank Brings out a bilingual 'Indo-China Newsletter' featuring areas of cooperation between India and China.

Marketing Advisory Services

EXIM Bank plays a promotional role and seeks to create and enhance export capabilities and international competitiveness of Indian companies. Exim Bank through its Marketing Advisory Services helps Indian exporting firms in their globalisation efforts by proactively assisting in locating overseas distributor(s)/buyer(s)/ partner(s) for their products and services. The Bank assists in identification of opportunities overseas for setting up plants or projects or for acquisition of companies overseas. MAS Group leverages the Bank's high international standing, in-depth knowledge and understanding of the international markets and well established institutional linkages, coupled with its physical presence, to support Indian companies in their overseas marketing initiatives on a success fee basis. Exim Bank has been able to successfully place a range of products in overseas as well as domestic markets.

Eligibility

Any company/firm wanting to export its quality products/services is eligible to avail this benefit as long as it does not fall in the negative list of India's Foreign Trade Policy and International Conventions. Marketing Advisory Services are provided across all the sectors. Information required from the company is as under:-

- Company profile

- Product Brochures
- Printed material
- Prices
- Existing export markets & target markets
- Minimum order quantity
- Quality certifications
- Samples, as and when required

EXPORT ADVISORY SERVICES GROUP (EAS)

The Export Advisory Services Group [EAS] offers a diverse range of information, advisory and support services, which enable exporters to evaluate international risks, exploit export opportunities and improve competitiveness. Value added information and support services are provided to Indian projects exporters on the projects funded by multilateral agencies.

The Group undertakes customised research on behalf of interested companies in the areas such as establishing market potential, defining marketing arrangements, and specifying market distribution channels. Developing export market entry plans, facilitating accomplishment of international quality certification and display of products in trade fairs and exhibitions are other services provided.

The Bank provides a wide range of information, advisory and support services, which complement its financing programmes. These services are provided on a fee basis to Indian companies and overseas entities. The scope of services includes market-related information, sector and feasibility studies, technology supplier identification, partner search, investment facilitation and development of joint ventures both in India and abroad.

Multilateral Funded Projects Overseas (MFPO)

The Bank provides a package of information and support services to Indian companies to help improve their prospects for securing business in projects funded by the World Bank, Asian Development Bank, African Development Bank, and European Bank for Reconstruction and Development.

EXIM Bank as a Consultant

The Bank’s experience in evolving as an institution supporting international trade and investment, in addition to functioning as an export credit agency in a developing country context, is of particular relevance in other developing countries. The Bank has been sharing its experience and expertise by undertaking consultancy assignments. Exim Bank also shares its experience and expertise through provision of on-site exchange of personnel programmes aimed at providing a first-hands experience to the employees of its institutional partners.

Institutional Linkages

The Bank has fostered a network of alliances and institutional linkages with multilateral agencies, export credit agencies, banks and financial institutions, trade promotion bodies, and investment promotion boards to help create an enabling environment for supporting trade and investment. The Global Network of Exim Banks and Development Finance Institutions (G-NEXID) was set up in Geneva in March 2006 through the Bank's initiative, under the auspices of UNCTAD. With the active support of a number of other Exim Banks and Development Finance Institutions from various developing countries, the network has endeavoured to foster enhanced South-South trade and investment cooperation. 'Observer Status' in UNCTAD underscores support for the Forum.

Award for Excellence

The Bank, in association with CII, has instituted an Annual Award for Business Excellence for best Total Quality Management (TQM) practices adopted by an Indian company. The Award is based on the European Foundation for Quality Management (EFQM) model.

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Unit IV - MCQ

SI. NO	Question	Option 1	Option 2	Option 3	Option 4	Option 5	Option 6	Answer
1	Intellectual Property Rights (IPR) protect the use of information and ideas that are of…..	Ethical value	Social value	Moral value	Commercial value			Commercial value
2	If Francesca invents a new process for recording music, she will likely apply for a…….	Patent	Trademark	Copyright	Industrial design			Patent
3	The rights of an author or artist with respect to his or her creation are governed by the law of……….	Patent	Trademark	Copyright	Industrial design			Copyright
4	A street vendor on Bloor Street is selling fake "TAGG" watches. Under which area of intellectual property would the TAG Company	Patent	Trademark	Copyright	Industrial design			Trademark

	likely seek a remedy?							
5	Which is false? Intellectual property rights may be protected by…………	Maintaining secrecy	Registration	Use of a confidentiality clause	Assignment			Assignment
6	Meena has designed a uniquely shaped walker for senior citizens, which can be collapsed and, with the aid of two levers, used as a chair. Reeti's design is in commercial production under the name of Supportive Stroller. Which types of intellectual property would most likely apply to Meena's creation?	Patent; copyright; trademark	Copyright; trademark; industrial design	Trademark; industrial design; trade secret	Patent; trademark; industrial design			Patent; trademark; industrial design
7	Which is not a remedy for infringement of intellectual property rights?	An accounting for profits	An injunction	Specific performance	Damages			Specific performance

8	Passing off is…….	Incitement to break the contractual obligations of another	Presenting another's goods and services as one's own	The public utterance of a false statement of fact or opinion that harms another's reputation	The utterance of a false statement about another's goods or services that is harmful to the reputation of those goods or services			Presenting another's goods and services as one's own
9	A trademark is………..	The ornamentation or shape of a functional object, such as a chair	The right to prevent others from copying or modifying certain works	A monopoly to make, use, or sell an invention	A mark used to distinguish the source of goods or services			A mark used to distinguish the source of goods or services
10	Under the Patent Act, the person entitled to receive a patent on a new invention is………	The one who invented it first	The who applied for a patent first	The one who commercialized it first	The one who first thought of it			The who applied for a patent first
11	The protection afforded by a Canadian patent lasts for a maximum of…………	10 years	20 years	The life of the patent holder	The life of the inventor plus 50 years			20 years

12	Use of a trademark that is the property of a competitor is………….	The tort of passing off	The tort of deceit	The tort of fraud	The tort of negligence			The tort of passing off
13	As a general rule……	Intellectual property rights are assignable	Moral rights can be assigned but not waived	Intellectual property rights are not assignable	Intellectual property rights are assignable and Moral rights can be assigned but not waived			Intellectual property rights are assignable and Moral rights can be assigned but not waived
14	Where does the Banaganapalle mango hail from?	TN	Andhra Pradesh	Kerala	Karnataka			Andhra Pradesh
15	Which of the following was awarded with GI tag? 1. Dharwad Pedha 2. Tirupathi Laddu 3. Hyderabadi Haleem 4. Bengal Rasagolla	1,2	1,2,4	2,3	1,2,3			1,2,3
16	Which of the following statement / s is / are correct? 1. Joha is an aromatic rice that is cultivated exclusively in Brahmaputra	Only 1	Only 2	1,2	None			Only 1

	Vally of Assam. 2. It has got the GI tag.							
17	The term 'Geographical Indications' could be used for……….	Agricultural goods	Natural goods	Manufactured goods	Agricultural, Natural and Manufactured goods,			Agricultural, Natural and Manufactured goods,
18	Geographical Indications are used to indicate……..	A geographical place	A link between some characteristic of the good and the particular region where it is produced	The place where the goods are manufactured/ produced	The origin of goods			A link between some characteristic of the good and the particular region where it is produced
19	The sign used for a Geographical Indication may be……………..	A name of a geographical place	A symbol	A map	A name of a geographical place, Symbol and map			A name of a geographical place, Symbol and map
20	Who can apply for registration of a Geographical Indication?	An association of persons	An organization of producers	An individual	Only 1 and 2			Only 1 and 2
21	Who can use a registered Geographical Indication?	A person having interest in goods to which the Geograp	A person residing in the area to which the Geograp	A producer of the goods in respect of which a Geographical Indication has been registered	An authorised user			An authorised user

		hical Indication relates	hical Indication relates						
22	Who can be considered a ‘producer’ in relation to goods under the Geographical Indications of Goods Act?	A person who produces, processes or packages agricultural goods	A person who uses natural goods in making or manufacturing products	A person who makes or manufactures handicrafts or industrial goods	All of the above				All of the above
23	Which one of the following is not a Geographical Indication?	Goa Feni	Nagpur orange	Indian Neem tree	Kolhapuri chappal				Indian Neem tree
24	Who can initiate an action for the infringement of a Geographical Indication?	The government	The registered proprietor	The authorized user	The registered proprietor and the authorized user				The registered proprietor and the authorized user
25	Intellectual property rights and …………..are two of the most important developing areas of law.	Cyber law	copyright infringement	patent law	trademark infringement				Cyber law
26	What action would a person bring against someone who steals a trade secret?	Economic Espionage Act	Infringement action	Misappropriation	Violation of trademark law				Misappropriation

27	To be patented, an invention must be…………	non-obvious	useful	novel	non-obvious, useful, novel			non-obvious,useful, novel
28	Who can challenge the issue of a patent?	Business competitors	The inventor's partners or employees	Anyone	Federal government			Anyone
29	Which of the following can a successful plaintiff in a patent infringement suit not recover?	Money damages	Royalties for the next ten years	Injunction preventing future infringements	Order requiring the destruction of the infringing article			Royalties for the next ten years
30	A patent may not be granted if the public used the invention for more than one year prior to the filing of the patent application pursuant to the………………….....	fair-use doctrine	public-use doctrine	World Trade organization treaty	American Inventors Protection Act			fair-use doctrine
31	Which of the following examples would not fall into the scope of the fair-use doctrine?	Brief quotation in a news report	Use in a parody	International reproduction in a broadcast of a reported event	Reproduction by a teacher to illustrate a lesson			International reproduction in a broadcast of a reported event
32	Which of the following statements is true?	Trademark registrations can be	Trademark law is intended to protect	To qualify for federal protection, a mark must be distinctive	Surnames alone can be trademarked.			Trademark registrations can be renewed

		renewed for an unlimited number of ten-year periods.	the owner's original work.	and have a "secondary meaning."				for an unlimited number of ten-year periods.
33	Which of the following would not qualify as a mark?	Toys "R" Us	Reebok	North	The Green Family Fun Experience			North
34	Which of following would not gain copyright protection?	A DVD	An unrecorded speech	Written lyrics of a song	A hand knitted jumper			An unrecorded speech
35	What is the duration of copyright protection for a novel?	A novel will not gain copyright protection	The day the author dies	The end of the calendar year in which the author died	70 years from the end of the calendar year in which the author died			70 years from the end of the calendar year in which the author died
36	Which one of the following actions is not a breach of copyright?	To import copied CDs	To make a copy of a CD and sell it	To borrow a CD from a friend and copy it to your laptop for your own private use	To purchase a CD and copy it to your laptop for your own private use			To purchase a CD and copy it to your laptop for your own private use
37	Which of the following is not one of the three essential elements for a	Be a product	Be new to the public	Involve an inventive step	Be capable of industrial application			Be a product

	patent to be granted for an invention?							
38	Which one of the following statements is true?	A patent must be registered in order to gain protection	Copyright must be registered in order to gain protection	The owner of a patent cannot sell it but can prevent others using his invention	The definition of an invention is set out in the Patents Act 1977			A patent must be registered in order to gain protection
39	The law governing registered trade marks can be found in which Act?	The Intellectual Property Act 1994	Copyright, Designs and Patents Act 1988	The Registered Trade Marks Act 1994	The Trade Marks Act 1994			The Trade Marks Act 1994
40	Which one of the following could not be registered as a trade mark?	The mark is an image	The mark is made up of letters and numbers	The mark is made up of a symbol with no words or letters	The mark represents the natural or technical shape of the goods			The mark represents the natural or technical shape of the goods
41	Which one of the following statements is false?	The maximum duration for an unregistered design right is 15 years	A registered design right may cover 2 dimensional and 3 dimensional objects	A registered design right only applies to 3 dimensional objects	The maximum duration for a registered design right is 25 years			A registered design right only applies to 3 dimensional objects

42	Unless a contract provides otherwise, who is the first owner of a design right created on or after 1 October 2014?	The person who commis sioned the design	The manufac turer of the design	The government	The designer			The designer
43	The tort of passing off is governed by which statute?	The Passing-off Act 1977	The Tort Act 1977	The Unfair Contract Terms Act 1977	There is no statute that governs the law of passing-off			There is no statute that governs the law of passing-off
44	The Intellectual Property Act ……..	1990	1991	1992	1994			1994
45	Copyright, Designs and Patents Act…….	1978	1988	1998	2001			1988
46	The Registered Trade Marks Act……	1974	1984	1994	1999			1994
47	The Trade Marks Act ……….	1994	1984	1995	1999			1994
48	The term of copyright for an author lasts how long?	the life of the author	the life of the author plus seventy years	ninety-five years	seventy years			the life of the author plus seventy years

49	Copyright protection begins when?	When the original work is fixed in a tangible medium of expression	Immediately when the author or creator comes up with the idea	When it is published	When it is registered			When the original work is fixed in a tangible medium of expression
50	International organization with objective to encourage creative activity and to promote intellectual propert throughout world is…………	WIPO	UPU	BIRD	WTO			WIPO
51	World Intellectual Property Organization was established in…….	14 March, 1959	14 July, 1967	14 August, 1965	14 October, 1960			14 July, 1967
52	World Intellectual Property Organization is specialized agency of……….	United Nations	United Nations Security Council	United nations Economic Council	United Nations Social Council			United Nations
53	First World Intellectual Property Organization on Changing Face of Innovation was	2005	2007	2011	2009			2011

	published in…………							
54	Headquarter of World Intellectual Property Organization is located in……….	Rome, Italy	Bern, Switzerland	Berlin, Germany	Geneva, Switzerland			Geneva, Switzerland
55	Which section of Design Act, 2000 defines the term 'Design'……….	2	3	4	1			2
56	What is encompassed in design as per Intellectual Property Law……….	Pattern	Configuration	features of shape	Pattern, Configuration and Features of shape			Pattern, Configuration and Features of shape
57	Which of the following can be considered as an article for purpose of registration of design………..	lable	token	card	Novel Industrial Product			Novel Industrial Product
58	What constitue article under the design act 2000………	Natural Article	Public domain article	Historical Article	Manufactured Article			Natural Article
59	What is the duration of a design registered under the design act, 2000?	5 years	depends upon the commercial value of infringement	2 years	10 years			10 years

60	The design Act……….	1990	1991	1999	2000			2000

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Unit V -Syllabus

Exchange Control Regulations - RBI Guide Lines - Authorized Dealers - FEMA, Permitted Currencies - ACU - Export Realization - Procedure and Related documents - Trends in India's Exports and Imports.

International Monetary Fund (IMF)

The International Monetary Fund (IMF) and the World Bank are institutions in the United Nations system. They share the same goal of raising living standards in their member countries. Their approaches to this goal are complementary, with the IMF focusing on macroeconomic issues and the World Bank concentrating on long-term economic development and poverty reduction.

History and Purpose

The architects of the Bretton Woods Agreement, John Maynard Keynes and Harry Dexter White, envisioned an institution that would oversee the international monetary system, exchange rates, and international payments to enable countries and their citizens to buy goods and services from each other. They expected that this new global entity would ensure exchange rate stability and encourage its member countries to eliminate the exchange restrictions that hindered trade. Officially, the IMF came into existence in December 1945 with twenty-nine member countries. (The Soviets, who were at Bretton Woods, refused to join the IMF.)

In 1947, the institution's first formal year of operations, the French became the first nation to borrow from the IMF. Over the next thirty years, more countries joined the IMF, including some African countries in the 1960s. The Soviet bloc nations remained the exception and were not part of the IMF until the fall of the Berlin Wall in 1989. The IMF experienced another large increase in members in the 1990s with the addition of Russia; Russia was also placed on the IMF's executive committee. Today, 187 countries are members of the IMF; twenty-four of those countries or groups of countries are represented on the executive board.

The purposes of the International Monetary Fund are as follows:

- To promote international monetary cooperation through a permanent institution which provides the machinery for consultation and collaboration on international monetary problems.
- To facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members as primary objectives of economic policy.
- To promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation.
- To assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of world trade.

- To give confidence to members by making the general resources of the Fund temporarily available to them under adequate safeguards, thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity.
- In accordance with the above, to shorten the duration and lessen the degree of disequilibrium in the international balances of payments of members.“Articles of Agreement: Article I—Purposes,” International Monetary Fund, accessed May 23, 2011,http://www.imf.org/external/pubs/ft/aa/aa01.htm.

In addition to financial assistance, the IMF also provides member countries with technical assistance to create and implement effective policies, particularly economic, monetary, and banking policy and regulations.

Special Drawing Rights (SDRs)

A Special Drawing Right (SDR) is basically an international monetary reserve asset. SDRs were created in 1969 by the IMF in response to the Triffin Paradox. The Triffin Paradox stated that the more US dollars were used as a base reserve currency, the less faith that countries had in the ability of the US government to convert those dollars to gold. The world was still using the Bretton Woods system, and the initial expectation was that SDRs would replace the US dollar as the global monetary reserve currency, thus solving the Triffin Paradox. Bretton Woods collapsed a few years later, but the concept of an SDR solidified. Today the value of an SDR consists of the value of four of the IMF’s biggest members’ currencies—the US dollar, the British pound, the Japanese yen, and the euro—but the currencies do not hold equal weight. SDRs are quoted in terms of US dollars. The basket, or group of currencies, is reviewed every five years by the IMF executive board and is based on the currency’s role in international trade and finance. The following chart shows the current valuation in percentages of the four currencies.

Currency	**Weighting**
US dollar	44 percent
Euro	34 percent
Japanese yen	11 percent
British pound	11 percent

The SDR is not a currency, but some refer to it as a form of IMF currency. It does not constitute a claim on the IMF, which only serves to provide a mechanism for buying, selling, and exchanging SDRs. Countries are allocated SDRs, which are included in the member country’s reserves. SDRs can be exchanged between countries along with currencies. The SDR serves as the unit of account of the IMF and some other international organizations, and countries borrow from the IMF in SDRs in times of economic need.

Key roles of IMF

The IMF is playing an expanding role in the global monetary system. The IMF's key roles are the following:

- To promote international monetary cooperation
- To facilitate the expansion and balanced growth of international trade
- To promote exchange stability
- To assist in the establishment of a multilateral system of payments
- To give confidence to members by making the IMF's general resources temporarily available to them under adequate safeguards
- To shorten the duration and lessen the degree of disequilibrium in the international balances of payments of members

The IMF's Current Role and Major Challenges and Opportunities

Criticism and Challenging Areas for the IMF

The IMF supports many developing nations by helping them overcome monetary challenges and to maintain a stable international financial system. Despite this clearly defined purpose, the execution of its work can be very complicated and can have wide repercussions for the recipient nations. As a result, the IMF has both its critics and its supporters. The challenges for organizations like the the IMF and the World Bank center not only on some of their operating deficiencies but also on the global political environment in which they operate. The IMF has been subject to a range of criticisms that are generally focused on the conditions of its loans, its lack of accountability, and its willingness to lend to countries with bad human rights records.David N. Balaam and Michael Veseth, Introduction to International Political Economy, 4th ed. (Upper Saddle River, NJ: Pearson Education International/Prentice Hall), 2005.

These criticisms include the following:

1. **Conditions for loans**

- The IMF makes the loan given to countries conditional on the implementation of certain economic policies, which typically include the following:
- Reducing government borrowing (higher taxes and lower spending)
- Higher interest rates to stabilize the currency
- Allowing failing firms to go bankrupt
- Structural adjustment (privatization, deregulation, reducing corruption and bureaucracy)"Criticism of IMF," Economics Help, accessed June 28, 2010,http://www.economicshelp.org/dictionary/i/imf-criticism.html.

The austere policies have worked at times but always extract a political toll as the impact on average citizens is usually quite harsh. The opening case in Chapter 2 "International Trade and Foreign Direct Investment" presents the current impact of IMF policies on Greece. Some suggest that the loan conditions are “based on what is termed the ‘Washington Consensus,’ focusing on liberalisation—of trade, investment and the financial sector—, deregulation and privatisation of nationalised industries. Often the conditionalities are attached without due regard for the borrower countries’ individual circumstances and the prescriptive recommendations by the World Bank and IMF fail to resolve the economic problems within the countries.

IMF conditionalities may additionally result in the loss of a state’s authority to govern its own economy as national economic policies are predetermined under IMF packages

2. **Exchange rate reforms.**

- “When the IMF intervened in Kenya in the 1990s, they made the Central bank remove controls over flows of capital. The consensus was that this decision made it easier for corrupt politicians to transfer money out of the economy (known as the Goldman scandal). Critics argue this is another example of how the IMF failed to understand the dynamics of the country that they were dealing with—insisting on blanket reforms.”“Criticism of IMF,” Economics Help, accessed June 28, 2010, http://www.economicshelp.org/dictionary/i/imf-criticism.html.

3. **Devaluations.**

- In the initial stages, the IMF has been criticized for allowing inflationary devaluations.“Criticism of IMF,” Economics Help, accessed June 28, 2010,http://www.economicshelp.org/dictionary/i/imf-criticism.html.

4. **Free-market criticisms of the IMF**

- “Believers in free markets argue that it is better to let capital markets operate without attempts at intervention. They argue attempts to influence exchange rates only make things worse—it is better to allow currencies to reach their market level.”

5. **Lack of transparency and involvement**

- The IMF has been criticized for “imposing policy with little or no consultation with affected countries.”“Criticism of IMF,” Economics Help, accessed June 28, 2010, http://www.economicshelp.org/dictionary/i/imf-criticism.html.

6. **Supporting military dictatorships**

- The IMF has been criticized over the decades for supporting military dictatorships.“Criticism of IMF,” Economics Help, accessed June 28, 2010,http://www.economicshelp.org/dictionary/i/imf-criticism.html.

Opportunities and Future Outlook for the IMF

The 2008 global economic crisis is one of the toughest situations that the IMF has had to contend with since the Great Depression.

For most of the first decade of the twenty-first century, global trade and finance fueled a global expansion that enabled many countries to repay any money they had borrowed from the IMF and other official creditors. These countries also used surpluses in trade to accumulate foreign exchange reserves. The global economic crisis that began with the 2007 collapse of mortgage lending in the United States and spread around the world in 2008 was preceded by large imbalances in global capital flows. Global capital flows fluctuated between 2 and 6 percent of world GDP between 1980 and 1995, but since then they have risen to 15 percent of GDP. The most rapid increase has been experienced by advanced economies, but emerging markets and developing countries have also become more financially integrated.

The founders of the Bretton Woods system had taken for granted that private capital flows would never again resume the prominent role they had in the nineteenth and early twentieth centuries, and the IMF had traditionally lent to members facing current account difficulties. The 2008 global crisis uncovered fragility in the advanced financial markets that soon led to the worst global downturn since the Great Depression. Suddenly, the IMF was inundated with requests for standby arrangements and other forms of financial and policy support.

The international community recognized that the IMF's financial resources were as important as ever and were likely to be stretched thin before the crisis was over. With broad support from creditor countries, the IMF's lending capacity tripled to around $750 billion. To use those funds effectively, the IMF overhauled its lending policies. It created a flexible credit line for countries with strong economic fundamentals and a track record of successful policy implementation. Other reforms targeted low-income countries. These factors enabled the IMF to disburse very large sums quickly; the disbursements were based on the needs of borrowing countries and were not as tightly constrained by quotas as in the past.

Many observers credit the IMF's quick responses and leadership role in helping avoid a potentially worse global financial crisis. As noted in the Chapter 5 "Global and Regional Economic Cooperation and Integration" opening case on Greece, the IMF has played a role in helping countries avert widespread financial disasters. The IMF's requirements are not always popular but are usually effective, which has led to its expanding influence. The IMF has sought to correct some of the criticisms; according to a Foreign Policy in Focus essay designed to stimulate dialogue on the IMF, the fund's strengths and opportunities include the following:

Flexibility and speed

"In March 2009, the IMF created the Flexible Credit Line (FCL), which is a fast-disbursing loan facility with low conditionality aimed at reassuring investors by injecting liquidity…Traditionally, IMF loan programs require the imposition of austerity measures such as raising interest rates that can reduce foreign investment…In the case of the FCL, countries qualify for it not on the basis of their promises, but on the basis of their history. Just as individual borrowers with good credit histories are eligible for loans at lower interest rates than their risky counterparts, similarly, countries with sound macroeconomic fundamentals are eligible for drawings under the FCL.

Cheerleading

"The Fund is positioning itself to be less of an adversary and more of a cheerleader to member countries. For some countries that need loans more for reassurance than reform, these changes to the Fund toolkit are welcome."Martin S. Edwards, "The IMF's New Toolkit: New Opportunities, Old Challenges," Foreign Policy in Focus, September 17, 2009, accessed June 28, 2010.

Adaptability

"Instead of providing the same medicine to all countries regardless of their particular problems, the new loan facilities are intended to aid reform-minded governments by providing short-term resources to reassure investors. In this manner, they help politicians in developing countries manage the downside costs of integration.

Transparency

The IMF has made efforts to improve its own transparency and continues to encourage its member countries to do so. Supporters note that this creates a barrier to any one or more countries that have more geopolitical influence in the organization. In reality, the major economies continue to exert influence on policy and implementation.

To underscore the global expectations for the IMF's role, China, Russia, and other global economies have renewed calls for the G20 to replace the US dollar as the international reserve currency with a new global system controlled by the IMF.

The Financial Times reported that Zhou Xiaochuan, the Chinese central bank's governor, said the goal would be to create a reserve currency that is disconnected from individual nations and is able to remain stable in the long run, thus removing the inherent deficiencies caused by using credit-based national currencies.

Although Mr. Zhou did not mention the US dollar, the essay gave a pointed critique of the current dollar-dominated monetary system:

"The outbreak of the crisis and its spillover to the entire world reflected the inherent vulnerabilities and systemic risks in the existing international monetary system," Mr Zhou wrote.

China has little choice but to hold the bulk of its $2,000bn of foreign exchange reserves in US dollars, and this is unlikely to change in the near future.

To replace the current system, Mr. Zhou suggested expanding the role of special drawing rights, which were introduced by the IMF in 1969 to support the Bretton Woods fixed exchange rate regime but became less relevant once that collapsed in the 1970s….

China is politically and economically motivated to recommend an alternative reserve currency. Politically, the country whose currency is the reserve currency is perceived as the dominant economic power, as Section 6.1 "What Is the International Monetary System?" discusses. Economically, China has come under increasing global pressure to increase the value of its currency, the renminbi, whichSection 6.3 "Understanding How International Monetary Policy, the IMF, and the World Bank Impact Business Practices" discusses in greater depth.

The IMF's mandate

The IMF promotes international monetary cooperation and provides policy advice and technical assistance to help countries build and maintain strong economies. The Fund also makes loans and helps countries design policy programs to solve balance of payments problems when sufficient financing on affordable terms cannot be obtained to meet net international payments. IMF loans are short and medium term and funded mainly by the pool of quota contributions that its members provide. IMF staffs are primarily economists with wide experience in macroeconomic and financial policies.

Framework for cooperation

The IMF and World Bank collaborate regularly and at many levels to assist member countries and work together on several initiatives. In 1989, the terms for their cooperation were set out in a concordat to ensure effective collaboration in areas of shared responsibility.

High-level coordination

During the Annual Meetings of the Boards of Governors of the IMF and the World Bank, Governors consult and present their countries' views on current issues in international economics and finance. The Boards of Governors decide how to address international economic and financial issues and set priorities for the organizations.

A group of IMF and World Bank Governors also meet as part of the Development Committee, whose meetings coincide with the Spring and Annual Meetings of the IMF and the World Bank. This committee was established in 1974 to advise the two institutions on critical development issues and on the financial resources required to promote economic development in low-income countries.

Management consultation

The Managing Director of the IMF and the President of the World Bank meet regularly to consult on major issues. They also issue joint statements and occasionally write joint articles, and have visited several regions and countries together.

Staff collaboration

The staffs of the IMF and the Bank collaborate closely on country assistance and policy issues that are relevant for both institutions. The two institutions also often conduct country missions in parallel and staff participate in each other's missions. IMF assessments of a country's general economic situation and policies provide input to the Bank's assessments of potential development projects or reforms. Similarly, Bank advice on structural and sectoral reforms is taken into account by the IMF in its policy advice. The staffs of the two institutions also cooperate on the conditionality involved in their respective lending programs.

The 2007 external review of Bank-Fund collaboration led to a Joint Management Action Plan on World Bank-IMF Collaboration (JMAP) to further enhance the way the two institutions work together. Under the plan, Fund and Bank country teams discuss their country-level work programs, which identify macro-critical sectoral issues, the division of labor, and the work needed from each institution in the coming year. A review of Bank-Fund Collaboration underscored the importance of these joint country team consultations in enhancing collaboration.

Reducing debt burdens. The IMF and World Bank also work together to reduce the external debt burdens of the most heavily indebted poor countries under theHeavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI). The objective is to help low-income countries achieve their development goals without creating future debt problems. IMF and Bank staff jointly prepare country debt sustainability analyses under the Debt Sustainability Framework (DSF) developed by the two institutions.

Reducing poverty

In 1999, the IMF and the World Bank launched the Poverty Reduction Strategy Paper (PRSP) approach as a key component in the process leading to debt relief under the HIPC Initiative and an important anchor inconcessional lending by the Fund and the Bank. While PRSPs continue to underpin the HIPC Initiative, the World Bank has adopted in July 2014 a new consultative approach to country engagement focused on supporting its members' policies to eliminate extreme poverty and promote shared prosperity. The Fund continues to rely on PRSPs to support the link between poverty reduction objectives and Fund engagement under the Extended Credit Facilityand the Policy Support Instrument.

Monitoring progress on the MDGs

Since 2004, the Fund and the Bank have worked together on the Global Monitoring Report (GMR), which assesses progress needed to achieve the UN Millennium Development Goals (MDGs). The report also considers how well developing countries, developed countries, and the international financial institutions are contributing to the development partnership and strategy to meet the MDGs.

Assessing financial stability

The IMF and the World Bank are also working together to make financial sectors in member countries resilient and well regulated. The Financial Sector Assessment Program (FSAP) was introduced in 1999 to identify the strengths and vulnerabilities of a country's financial system and recommend appropriate policy responses.

More detailed information can be found on the institutions' websites:www.imf.org and www.worldbank.org.

World Bank

The World Bank came into existence in 1944 at the Bretton Woods conference. Its formal name is the International Bank for Reconstruction and Development (IBRD), which clearly states its primary purpose of financing economic development. The World Bank's first loans were extended during the late 1940s to finance the reconstruction of the war-ravaged economies of Western Europe. When these nations recovered some measure of economic self-sufficiency, the World Bank turned its attention to assisting the world's poorer nations. The World Bank has one central purpose: to promote economic and social progress in developing countries by helping raise productivity so that their people may live a better and fuller life:

[In 2009,] the World Bank provided $46.9 billion for 303 projects in developing countries worldwide, with our financial and/or technical expertise aimed at helping those countries reduce poverty.

The Bank is currently involved in more than 1,800 projects in virtually every sector and developing country. The projects are as diverse as providing microcredit in Bosnia and Herzegovina, raising AIDS-prevention awareness in Guinea, supporting education of girls in Bangladesh, improving health care delivery in Mexico, and helping East Timor rebuild upon independence and India rebuild Gujarat after a devastating earthquake."Projects," The World Bank, accessed February 9, 2011,http://go.worldbank.org/M7ARDFNB60.

Today, The World Bank consists of two main bodies, the International Bank for Reconstruction and Development (IBRD) and the International Development Association (IDA), established in 1960. The World Bank is part of the broader World Bank Group, which consists of five interrelated institutions: the IBRD; the IDA; the International Finance Corporation (IFC), which was established in 1956; the Multilateral Investment Guarantee Agency (MIGA), which was established in 1988; and the International Centre for Settlement of Investment Disputes (ICSID), which was established in 1966. These additional members of the World Bank Group have specific purposes as well. The IDA typically provides interest-free loans to countries with sovereign guarantees. The IFC provides loans, equity, risk-management tools, and structured finance. Its goal is to facilitate sustainable development by improving investments in the private sector. The MIGA focuses on improving the foreign direct investment of developing countries. The ICSID provides a means for dispute resolution between governments and private investors with the end goal of enhancing the flow of capital.

The current primary focus of the World Bank centers on six strategic themes:

- The poorest countries: Poverty reduction and sustainable growth in the poorest countries, especially in Africa
- Post-conflict and fragile states: Solutions to the special challenges of post-conflict countries and fragile states
- Middle-income countries: Development solutions with customized services as well as financing for middle-income countries
- Global public goods: Addressing regional and global issues that cross national borders, such as climate change, infectious diseases, and trade
- The Arab world: Greater development and opportunity in the Arab world

- Knowledge and learning: Leveraging the best global knowledge to support development.“To Meet Global Challenges, Six Strategic Themes,” The World Bank, accessed February 9, 2011.

The World Bank provides low-interest loans, interest-free credits, and grants to developing countries. There’s always a government (or “sovereign”) guarantee of repayment subject to general conditions. The World Bank is directed to make loans for projects but never to fund a trade deficit. These loans must have a reasonable likelihood of being repaid. The IDA was created to offer an alternative loan option. IDA loans are free of interest and offered for several decades, with a ten-year grace period before the country receiving the loan needs to begin repayment. These loans are often called soft loans.

Since it issued its first bonds in 1947, the IBRD generates funds for its development work through the international capital markets (which Chapter 7 "Foreign Exchange and the Global Capital Markets"covers). The World Bank issues bonds, typically about $25 billion a year. These bonds are rated AAA (the highest possible rating) because they are backed by member states’ shared capital and by borrowers’ sovereign guarantees. Because of the AAA credit rating, the World Bank is able to borrow at relatively low interest rates. This provides a cheaper funding source for developing countries, as most developing countries have considerably low credit ratings. The World Bank charges a fee of about 1 percent to cover its administrative overheads.

Current Role and Major Challenges and Opportunities of World Bank

Like the IMF, the World Bank has both its critics and its supporters. The criticisms of the World Bank extend from the challenges that it faces in the global operating environment. Some of these challenges have complicated causes; some result from the conflict between nations and the global financial crisis. The following are four examples of the world’s difficult needs that the World Bank tries to address:

- Even in 2010, over 3 billion people lived on less than $2.50 a day.
- At the start of the twenty-first century, almost a billion people couldn’t read a book or sign their names.
- Less than 1 percent of what the world spends each year on weapons would have put every child into school by the year 2000, but it didn’t happen.
- Fragile states such as Afghanistan, Rwanda, and Sri Lanka face severe development challenges: weak institutional capacity, poor governance, political instability, and often ongoing violence or the legacy of past conflict. Anup Shah, “Causes of Poverty,” Global Issues, last modified April 25, 2010, accessed August 1, 2010, http://www.globalissues.org/issue/2/causes-of-poverty.

According to the Encyclopedia of the New American Nation and the New York Times, the World Bank is criticized primarily for the following reasons:

Administrative incompetence

The World Bank and its lending practices are increasingly scrutinized, with critics asserting that “the World Bank has shifted from being a ‘lender of last resort’ to an international welfare organization,” resulting in an institution that is “bloated, incompetent, and even corrupt.” Also incriminating is that “the bank’s lax lending standards have led to a rapidly deteriorating loan portfolio."Encyclopedia of the New American Nation, s.v., "International Monetary Fund and World Bank—World Bank Critics on the Right and Left," accessed June 29, 2010.

Rewarding or supporting inefficient or corrupt countries

The bank's lending policies often reward macroeconomic inefficiency in the underdeveloped world, allowing inefficient nations to avoid the types of fundamental reforms that would in the long run end poverty in their countries. Many analysts note that the best example is to compare the fantastic growth in East Asia to the deplorable economic conditions of Africa. In 1950 the regions were alike—South Korea had a lower per capita GDP than Nigeria. But by pursuing macroeconomic reforms, high savings, investing in education and basic social services, and opening their economies to the global trading order, the "Pacific Tigers" have been able to lift themselves out of poverty and into wealth with very little help from the World Bank. Many countries in Africa, however, have relied primarily on multilateral assistance from organizations like the World Bank while avoiding fundamental macroeconomic reforms, with deplorable but predictable results.

Conservatives point out that the World Bank has lent more than $350 billion over a half-century, mostly to the underdeveloped world, with little to show for it. One study argued that of the sixty-six countries that received funding from the bank from 1975 to 2000, well over half were no better off than before, and twenty were actually worse off. The study pointed out that Niger received $637 million between 1965 and 1995, yet its per capita GNP had fallen, in real terms, more than 50 percent during that time. In the same period Singapore, which received one-seventh as much World Bank aid, had seen its per capita GNP increase by more than 6 percent a year.

Focusing on large projects rather than local initiatives

Some critics claim that World Bank loans give preference to "large infrastructure projects like building dams and electric plants over projects that would benefit the poor, such as education and basic health care." The projects often destroy the local environment, including forests, rivers, and fisheries. Some estimates suggest "that more than two and a half million people have been displaced by projects made possible through World Bank loans." Failed projects, argue environmentalists and antiglobalization groups, are particularly illustrative: "The Sardar Sarovar dam on the Narmada River in India was expected to displace almost a quarter of a million people into squalid resettlement sites. The Polonoroeste Frontier Development scheme has led to large-scale deforestation in the Brazilian rain forest. In Thailand, the Pak Mun dam has destroyed the fisheries of the Mun River, impoverishing thousands who had made their living fishing and forever altering the diet of the region."Encyclopedia of the New American Nation, s.v., "International Monetary Fund and World Bank—World Bank Critics on the Right and Left," accessed June 29, 2010,http://www.americanforeignrelations.com/E-N/International-Monetary-Fund-and-World-Bank-Worldbank-critics-on-the-right-and-left.html. Further, the larger projects become targets for corruption by local government officials because there is so much money involved.

Negative influence on theory and practice

As one of the two Bretton Woods Institutions, the World Bank plays a large role in research, training, and policy formulation. Critics worry that because "the World Bank and the IMF are regarded as experts in the field of financial regulation and economic development, their views and prescriptions may undermine or eliminate alternative perspectives on development.""What Are the Main Concerns and Criticism about the World Bank and IMF?," Bretton Woods Project, January 25, 2007, accessed February 9, 2011,http://www.brettonwoodsproject.org/item.shtml?x=320869.

Dominance of G7 countries

The industrialized countries dominate the World Bank (and IMF) governance structures. Decisions are typically made and policies implemented by these leading countries—the G7—because they are the largest donors, some suggest without sufficient consultation with poor and developing countries.

Opportunities and Future Outlook for the World Bank

As vocal as the World Bank's critics are, so too are its supporters. The World Bank is praised by many for engaging in development projects in remote locations around the globe to improve living standards and reduce poverty. The World Bank's current focus is on helping countries achieve the Millennium Development Goals (MDGs), which are eight international development goals, established in 2000 at the Millennium Summit, that all 192 United Nations member states and twenty-three international organizations have agreed to achieve by the year 2015. They include reducing extreme poverty, reducing child mortality rates, fighting disease epidemics such as AIDS, and developing a global partnership for development. The World Bank is focused on the following four key issues:

Increased transparency

In response to the criticisms over the decades, the World Bank has made progress. More of the World Bank's decision making and country assessments are available publicly. The World Bank has continued to work with countries to combat corruption both at the country and bank levels.

Expanding social issues in the fight on poverty

In 2001, the World Bank began to incorporate gender issues into its policy. "Two years later the World Bank announced that it was starting to evaluate all of its projects for their effects on women and girls," noting that "poverty is experienced differently by men and women" and "a full understanding of the gender dimensions of poverty can significantly change the definition of priority policy and program interventions.

Improvements in countries' competitiveness and increasing exports

The World Bank's policies and its role as a donor have helped improve the ability of some countries to secure more of the global revenues for basic commodities. In Rwanda, for example, reforms transformed the country's coffee industry and increased exports. Kenya has expanded its exports of cut flowers, and Uganda has improved its fish-processing industry. World Bank efforts have also helped African financial companies develop.

Improving efficiencies in diverse industries and leveraging the private sector

The World Bank has worked closely with businesses in the private sector to develop local infrastructure, including power, transportation, telecommunications, health care, and education.Shanta Devarajan, "African Successes—Listing the Success Stories," Africa Can…End Poverty (blog), The World Bank Group, September 17, 2009, accessed May 23, 2011,http://blogs.worldbank.org/africacan/african-successes-listing-the-success-stories. In Afghanistan, for example, small dams are built and maintained by the locals themselves to support small industries processing local produce.

The World Bank continues to play an integral role in helping countries reduce poverty and improve the well-being of their citizens. World Bank funding provides a resource to countries to utilize the services of global companies to accomplish their objectives.

World Bank

The World Bank consists of two main bodies, the IBRD and the International Development Association (IDA).

The World Bank Group includes the following interrelated institutions:

- IBRD, which makes loans to countries with the purpose of building economies and reducing poverty
- IDA, which typically provides interest-free loans to countries with sovereign guarantees
- International Finance Corporation (IFC), which provides loans, equity, risk-management tools, and structured finance with the goal of facilitating sustainable development by improving investments in the private sector
- Multilateral Investment Guarantee Agency (MIGA), which focuses on improving the foreign direct investment of the developing countries
- International Centre for Settlement of Investment Disputes (ICSID), which provides a means for dispute resolution between governments and private investors, with the end goal of enhancing the flow of capital

The World Bank's mandate

The World Bank promotes long-term economic development and poverty reduction by providing technical and financial support to help countries reform particular sectors or implement specific projects—such as, building schools and health centers, providing water and electricity, fighting disease, and protecting the environment. World Bank assistance is generally long term and is funded both by member country contributions and through bond issuance. World Bank staff are often specialists in particular issues, sectors, or techniques.

The IMF and the World Bank

If you have difficulty distinguishing the World Bank from the International Monetary Fund, you are not alone. Most people have only the vaguest idea of what these institutions do, and very few people indeed could, if pressed on the point, say why and how they differ. Even John Maynard Keynes, a founding father of the two institutions and considered by many the most brilliant economist of the twentieth century, admitted at the inaugural meeting of the International Monetary Fund that he was confused by the names: he thought the Fund should be called a bank, and the Bank should be called a fund. Confusion has reigned ever since.

Known collectively as the Bretton Woods Institutions after the remote village in New Hampshire, U.S.A., where they were founded by the delegates of 44 nations in July 1944, the Bank and the IMF are twin intergovernmental pillars supporting the structure of the world's economic and financial order. That there are two pillars rather than one is no accident. The international community was consciously trying to establish a division of labor in setting up the two agencies. Those who deal professionally with the IMF and Bank find them categorically distinct. To the rest of the world, the niceties of the division of labor are even more mysterious than are the activities of the two institutions.

Similarities between them do little to resolve the confusion. Superficially the Bank and IMF exhibit many common characteristics. Both are in a sense owned and directed by the governments of member nations. The People's Republic of China, by far the most populous state on earth, is a member, as is the world's largest industrial power (the United States). In fact, virtually every country on earth is a member of both institutions. Both institutions concern themselves with economic issues and concentrate their efforts on broadening and strengthening the economies of their member nations.

Staff members of both the Bank and IMF often appear at international conferences, speaking the same recondite language of the economics and development professions, or are reported in the media to be negotiating involved and somewhat mystifying programs of economic adjustment with ministers of finance or other government officials. The two institutions hold joint annual meetings, which the news media cover extensively. Both have headquarters in Washington, D.C., where popular confusion over what they do and how they differ is about as pronounced as everywhere else.

For many years both occupied the same building and even now, though located on opposite sides of a street very near the White House, they share a common library and other facilities, regularly exchange economic data, sometimes present joint seminars, daily hold informal meetings, and occasionally send out joint missions to member countries.

Despite these and other similarities, however, the Bank and the IMF remain distinct. The fundamental difference is this: the Bank is primarily a development institution; the IMF is a cooperative institution that seeks to maintain an orderly system of payments and receipts between nations. Each has a different purpose, a distinct structure, receives its funding from different sources, assists different categories of members, and strives to achieve distinct goals through methods peculiar to it.

Purposes

At Bretton Woods the international community assigned to the World Bank the aims implied in its formal name, the International Bank for Reconstruction and Development (IBRD), giving it primary responsibility for financing economic development. The Bank's first loans were extended during the late 1940s to finance the reconstruction of the war-ravaged economies of Western Europe. When these nations recovered some measure of economic self-sufficiency, the Bank turned its attention to assisting the world's poorer nations, known as developing countries, to which it has since the 1940s loaned more than $330 billion. The World Bank has one central purpose: to promote economic and social progress in developing countries by helping to raise productivity so that their people may live a better and fuller life.

The international community assigned to the IMF a different purpose. In establishing the IMF, the world community was reacting to the unresolved financial problems instrumental in initiating and protracting the Great Depression of the 1930s: sudden, unpredictable variations in the exchange values of national currencies and a widespread disinclination among governments to allow their national currency to be exchanged for foreign currency. Set up as a voluntary and cooperative institution, the IMF attracts to its membership nations that are prepared, in a spirit of enlightened self-interest, to relinquish some measure of national sovereignty by abjuring practices injurious to the economic well-being of their fellow member nations.

The rules of the institution, contained in the IMF's Articles of Agreement signed by all members, constitute a code of conduct. The code is simple: it requires members to allow their currency to be exchanged for foreign currencies freely and without restriction, to keep the IMF informed of changes they contemplate in financial and monetary policies that will affect fellow members' economies, and, to the extent possible, to modify these policies on the advice of the IMF to accommodate the needs of the entire membership. To help nations abide by the code of conduct, the IMF administers a pool of money from which members can borrow when they are in trouble. The IMF is not, however, primarily a lending institution as is the Bank.

It is first and foremost an overseer of its members' monetary and exchange rate policies and a guardian of the code of conduct. Philosophically committed to the orderly and stable growth of the world economy, the IMF is an enemy of surprise. It receives frequent reports on members' economic policies and prospects, which it debates, comments on, and communicates to the entire membership so that other members may respond in full knowledge of the facts and a clear understanding of how their own domestic policies may affect other countries. The IMF is convinced that a fundamental condition for international prosperity is an orderly monetary system that will encourage trade, create jobs, expand economic activity, and raise living standards throughout the world. By its constitution the IMF is required to oversee and maintain this system, no more and no less.

Size and Structure

The IMF is small (about 2,300 staff members) and, unlike the World Bank, has no affiliates or subsidiaries. Most of its staff members work at headquarters in Washington, D.C., although three small offices are maintained in Paris, Geneva, and at the United Nations in New York. Its professional staff members are for the most part economists and financial experts.

The structure of the Bank is somewhat more complex. The World Bank itself comprises two major organizations: the International Bank for Reconstruction and Development and the International Development Association (IDA). Moreover, associated with, but legally and financially separate from the World Bank are the International Finance Corporation, which mobilizes funding for private enterprises in developing countries, the International Center for Settlement of Investment Disputes, and the Multilateral Guarantee Agency.

With over 7,000 staff members, the World Bank Group is about three times as large as the IMF, and maintains about 40 offices throughout the world, although 95 percent of its staff work at its Washington, D.C., headquarters. The Bank employs a staff with an astonishing range of expertise: economists, engineers, urban planners, agronomists, statisticians, lawyers, portfolio managers, loan officers, project appraisers, as well as experts in telecommunications, water supply and sewerage, transportation, education, energy, rural development, population and health care, and other disciplines.

Source of Funding

The World Bank is an investment bank, intermediating between investors and recipients, borrowing from the one and lending to the other. Its owners are the governments of its 180 member nations with equity shares in the Bank, which were valued at about $176 billion in June 1995. The IBRD obtains most of the funds it lends to finance development by market borrowing through the issue of bonds (which carry an AAA rating because repayment is guaranteed by member governments) to individuals and private institutions in more than 100 countries.

Its concessional loan associate, IDA, is largely financed by grants from donor nations. The Bank is a major borrower in the world's capital markets and the largest nonresident borrower in virtually all countries where its issues are sold. It also borrows money by selling bonds and notes directly to governments, their agencies, and central banks. The proceeds of these bond sales are lent in turn to developing countries at affordable rates of interest to help finance projects and policy reform programs that give promise of success.

Despite Lord Keynes's profession of confusion, the IMF is not a bank and does not intermediate between investors and recipients. Nevertheless, it has at its disposal significant resources, presently valued at over $215 billion. These resources come from quota subscriptions, or membership fees, paid in by the IMF's 182 member countries. Each member contributes to this pool of resources a certain amount of money proportionate to its economic size and strength (richer countries pay more, poorer less). While the Bank borrows and lends, the IMF is more like a credit union whose members have access to a common pool of resources (the sum total of their individual contributions) to assist them in times of need. Although under special and highly restrictive circumstances the IMF borrows from official entities (but not from private markets), it relies principally on its quota subscriptions to finance its operations. The adequacy of these resources is reviewed every five years.

Recipients of Funding

Neither wealthy countries nor private individuals borrow from the World Bank, which lends only to creditworthy governments of developing nations. The poorer the country, the more favorable the conditions under which it can borrow from the Bank. Developing countries whose per capita gross national product (GNP) exceeds $1,305 may borrow from the IBRD. (Per capita GNP, a less formidable term than it sounds, is a measure of wealth, obtained by dividing the value of goods and services produced in a country during one year by the number of people in that country.)

These loans carry an interest rate slightly above the market rate at which the Bank itself borrows and must generally be repaid within 12-15 years. The IDA, on the other hand, lends only to governments of very poor developing nations whose per capita GNP is below $1,305, and in practice IDA loans go to countries with annual per capita incomes below $865. IDA loans are interest free and have a maturity of 35 or 40 years.

In contrast, all member nations, both wealthy and poor, have the right to financial assistance from the IMF. Maintaining an orderly and stable international monetary system requires all participants in that system to fulfill their financial obligations to other participants. Membership in the IMF gives to each country that experiences a shortage of foreign exchange--preventing it from fulfilling these obligations--temporary access to the IMF's pool of currencies to resolve this difficulty, usually referred to as a balance of payments problem.

These problems are no respecter of economic size or level of per capita GNP, with the result that over the years almost all members of the IMF, from the smallest developing country to the largest industrial country, have at one time or other had recourse to the IMF and received from it financial assistance to tide them over difficult periods. Money received from the IMF must normally be repaid within three to five years, and in no case later than ten years. Interest rates are slightly below market rates, but are not so concessional as those assigned to the World Bank's IDA loans. Through the use of IMF resources, countries have been able to buy time to rectify economic policies and to restore growth without having to resort to actions damaging to other members' economies.

World Bank Operations

The World Bank exists to encourage poor countries to develop by providing them with technical assistance and funding for projects and policies that will realize the countries' economic potential. The Bank views development as a long-term, integrated endeavor.

During the first two decades of its existence, two thirds of the assistance provided by the Bank went to electric power and transportation projects. Although these so-called infrastructure projects remain important, the Bank has diversified its activities in recent years as it has gained experience with and acquired new insights into the development process.

The Bank gives particular attention to projects that can directly benefit the poorest people in developing countries. The direct involvement of the poorest in economic activity is being promoted through lending for agriculture and rural development, small-scale enterprises, and urban development. The Bank is helping the poor to be more productive and to gain access to such necessities as safe water and waste-disposal facilities, health care, family-planning assistance, nutrition, education, and housing.

Within infrastructure projects there have also been changes. In transportation projects, greater attention is given to constructing farm-to-market roads. Rather than concentrating exclusively on cities, power projects increasingly provide lighting and power for villages and small farms. Industrial projects place greater emphasis on creating jobs in small enterprises. Labor-intensive construction is used where practical. In addition to electric power, the Bank is supporting development of oil, gas, coal, fuel wood, and biomass as alternative sources of energy.

The Bank provides most of its financial and technical assistance to developing countries by supporting specific projects. Although IBRD loans and IDA credits are made on different financial terms, the two institutions use the same standards in assessing the soundness of projects. The decision whether a project will receive IBRD or IDA financing depends on the economic condition of the country and not on the characteristics of the project.

Its borrowing member countries also look to the Bank as a source of technical assistance. By far the largest element of Bank-financed technical assistance--running over $1 billion a year recently--is that financed as a component of Bank loans or credits extended for other purposes. But the amount of Bank-financed technical assistance for free-standing loans and to prepare projects has also increased.

The Bank serves as executing agency for technical assistance projects financed by the United Nations Development Program in agriculture and rural development, energy, and economic planning. In response to the economic climate in many of its member countries, the Bank is now emphasizing technical assistance for institutional development and macroeconomic policy formulation.

Every project supported by the Bank is designed in close collaboration with national governments and local agencies, and often in cooperation with other multilateral assistance organizations. Indeed, about half of all Bank-assisted projects also receive co-financing from official sources, that is, governments, multilateral financial institutions, and export-credit agencies that directly finance the procurement of goods and services, and from private sources, such as commercial banks.

In making loans to developing countries, the Bank does not compete with other sources of finance. It assists only those projects for which the required capital is not available from other sources on reasonable terms. Through its work, the Bank seeks to strengthen the economies of borrowing nations so that they can graduate from reliance on Bank resources and meet their financial needs, on terms they can afford directly from conventional sources of capital.

The range of the Bank's activities is far broader than its lending operations. Since the Bank's lending decisions depend heavily on the economic condition of the borrowing country, the Bank carefully studies its economy and the needs of the sectors for which lending is contemplated. These analyses help in formulating an appropriate long-term development assistance strategy for the economy.

Graduation from the IBRD and IDA has occurred for many years. Of the 34 very poor countries that borrowed money from IDA during the earliest years, more than two dozen have made enough progress for them no longer to need IDA money, leaving that money available to other countries that joined the Bank more recently. Similarly, about 20 countries that formerly borrowed money from the IBRD no longer have to do so. An outstanding example is Japan. For a period of 14 years, it borrowed from the IBRD. Now, the IBRD borrows large sums in Japan.

IMF Operations

The IMF has gone through two distinct phases in its 50-year history. During the first phase, ending in 1973, the IMF oversaw the adoption of general convertibility among the major currencies, supervised a system of fixed exchange rates tied to the value of gold, and provided short-term financing to countries in need of a quick infusion of foreign exchange to keep their currencies at par value or to adjust to changing economic circumstances.

Difficulties encountered in maintaining a system of fixed exchange rates gave rise to unstable monetary and financial conditions throughout the world and led the international community to reconsider how the IMF could most effectively function in a regime of flexible exchange rates. After five years of analysis and negotiation (1973-78), the IMF's second phase began with the amendment of its constitution in 1978, broadening its functions to enable it to grapple with the challenges that have arisen since the collapse of the par value system. These functions are three.

First, the IMF continues to urge its members to allow their national currencies to be exchanged without restriction for the currencies of other member countries. As of May 1996, 115 members had agreed to full convertibility of their national currencies. Second, in place of monitoring members' compliance with their obligations in a fixed exchange system, the IMF supervises economic policies that influence their balance of payments in the presently legalized flexible exchange rate environment. This supervision provides opportunities for an early warning of any exchange rate or balance of payments problem. In this, the IMF's role is principally advisory. It confers at regular intervals (usually once a year) with its members, analyzing their economic positions and apprising them of actual or potential problems arising from their policies, and keeps the entire membership informed of these developments.

Third, the IMF continues to provide short- and medium-term financial assistance to member nations that run into temporary balance of payments difficulties. The financial assistance usually involves the provision by the IMF of convertible currencies to augment the afflicted member's dwindling foreign exchange reserves, but only in return for the government's promise to reform the economic policies that caused the balance of payments problem in the first place. The IMF sees its financial role in these cases not as subsidizing further deficits but as easing a country's painful transition to living within its means.

How in practice does the IMF assist its members? The key opening the door to IMF assistance is the member's balance of payments, the tally of its payments and receipts with other nations. Foreign payments should be in rough balance: a country ideally should take in just about what it pays out. When financial problems cause the price of a member's currency and the price of its goods to fall out of line, balance of payments difficulties are sure to follow. If this happens, the member country may, by virtue of the Articles of Agreement, apply to the IMF for assistance.

To illustrate, let us take the example of a small country whose economy is based on agriculture. For convenience in trade, the government of such a country generally pegs the domestic currency to a convertible currency: so many units of domestic money to a U.S. dollar or French franc. Unless the exchange rate is adjusted from time to time to take account of changes in relative prices, the domestic currency will tend to become overvalued, with an exchange rate, say, of one unit of domestic currency to one U.S. dollar, when relative prices might suggest that two units to one dollar is more realistic. Governments, however, often succumb to the temptation to tolerate overvaluation, because an overvalued currency makes imports cheaper than they would be if the currency were correctly priced.

The other side of the coin, unfortunately, is that overvaluation makes the country's exports more expensive and hence less attractive to foreign buyers. If the currency is thus overvalued, the country will eventually experience a fall-off in export earnings (exports are too expensive) and a rise in import expenditures (imports are apparently cheap and are bought on credit). In effect, the country is earning less, spending more, and going into debt, a predicament as unsustainable for a country as it is for any of us. Moreover, this situation is usually attended by a host of other economic ills for the country. Finding a diminished market for their export crops and receiving low prices from the government marketing board for produce consumed domestically, farmers either resort to illegal black market exports or lose the incentive to produce. Many of them abandon the farm to seek employment in overcrowded cities, where they become part of larger social and economic problems. Declining domestic agricultural productivity forces the government to use scarce foreign exchange reserves (scarce because export earnings are down) to buy food from abroad. The balance of payments becomes dangerously distorted.

As an IMF member, a country finding itself in this bind can turn to the IMF for consultative and financial assistance. In a collaborative effort, the country and the IMF can attempt to root out the causes of the payments imbalance by working out a comprehensive program that, depending on the particulars of the case, might include raising producer prices paid to farmers so as to encourage agricultural production and reverse migration to the cities, lowering interest rates to expand the supply of credit, and adjusting the currency to reflect the level of world prices, thereby discouraging imports and raising the competitiveness of exports.

Because reorganizing the economy to implement these reforms is disruptive and not without cost, the IMF will lend money to subsidize policy reforms during the period of transition. To ensure that this money is put to the most productive uses, the IMF closely monitors the country's economic progress during this time, providing technical assistance and further consultative services as needed.

In addition to assisting its members in this way, the IMF also helps by providing technical assistance in organizing central banks, establishing and reforming tax systems, and setting up agencies to gather and publish economic statistics. The IMF is also authorized to issue a special type of money, called the SDR, to provide its members with additional liquidity. Known technically as a fiduciary asset, the SDR can be retained by members as part of their monetary reserves or be used in place of national currencies in transactions with other members. To date the IMF has issued slightly over 21.4 billion SDRs, presently valued at about U.S. $30 billion.

Over the past few years, in response to an emerging interest by the world community to return to a more stable system of exchange rates that would reduce the present fluctuations in the values of currencies, the IMF has been strengthening its supervision of members' economic policies. Provisions exist in its Articles of Agreement that would allow the IMF to adopt a more active role, should the world community decide on stricter management of flexible exchange rates or even on a return to some system of stable exchange rates.

Measuring the success of the IMF's operations over the years is not easy, for much of the IMF's work consists in averting financial crises or in preventing their becoming worse. Most observers feel that merely to have contained the debt crisis of the 1980s, which posed the risk of collapse in the world's financial system, must be counted a success for the IMF. The Fund has also gained some recognition for assisting in setting up market-based economies in the countries of the former Soviet Union and for responding swiftly to the Mexican peso crisis in 1994, but its main contribution lies in its unobrusive, day-to-day encouragement of confidence in the international system. Nowhere will you find a bridge or a hospital built by the IMF, but the next time you buy a Japanese camera or drive a foreign car, or without difficulty exchange dollars or pounds for another currency while on holiday, you will be benefiting from the vast increase in foreign trade over the past 50 years and the widespread currency convertibility that would have been unimaginable without the world monetary system that the IMF was created to maintain.

Cooperation between Bank and IMF

Although the Bank and IMF are distinct entities, they work together in close cooperation. This cooperation, present since their founding, has become more pronounced since the 1970s. Since then the Bank's activities have increasingly reflected the realization that the pace of economic and social development accelerates only when sound underlying financial and economic policies are in place. The IMF has also recognized that unsound financial and economic policies are often deeply rooted in long-term inefficient use of resources that resists eradication through short-term adaptations of financial policies. It does little good for the

Bank to develop a long-term irrigation project to assist, say, the export of cotton, if the country's balance of payments position is so chaotic that no foreign buyers will deal with the country. On the other hand, it does little good for the IMF to help establish a sound exchange rate for a country's currency, unless the production of cotton for export will suffice to sustain that exchange rate over the medium to long term. The key to solving these problems is seen in restructuring economic sectors so that the economic potential of projects might be realized throughout the economy and the stability of the economy might enhance the effectiveness of the individual project.

Around 75 percent of the Bank's lending is applied to specific projects dealing with roads, dams, power stations, agriculture, and industry. As the global economy became mired in recession in the early 1980s, the Bank expanded the scope of its lending operations to include structural- and sector-adjustment loans. These help developing countries adjust their economic policies and structures in the face of serious balance of payments problems that threaten continued development. The main objective of structural-adjustment lending is to restructure a developing country's economy as the best basis for sustained economic growth. Loans support programs that are intended to anticipate and avert economic crises through economic reforms and changes in investment priorities. By using so-called policy-based lending, the Bank stimulates economic growth in heavily indebted countries--particularly in Latin America and in sub-Saharan Africa--that are undertaking, often at much social pain, far-reaching programs of economic adjustment.

In addition to its traditional function as provider of short-term balance of payments assistance, the advent of the oil crisis in the mid-1970s and the debt crisis in the early 1980s induced the IMF, too, to rethink its policy of restricting its financial assistance to short-term lending. As balance of payments shortfalls grew larger and longer-term structural reforms in members' economies were called for to eliminate these shortfalls, the IMF enlarged the amount of financial assistance it provides and lengthened the period within which its financial assistance would be available. In doing so, the IMF implicitly recognizes that balance of payments problems arise not only from a temporary lack of liquidity and inadequate financial and budgetary policies but also from long-standing contradictions in the structure of members' economies, requiring reforms stretching over a number of years and suggesting closer collaboration with the World Bank, which commands both the expertise and experience to deal with protracted structural impediments to growth.

Focusing on structural reform in recent years has resulted in considerable convergence in the efforts of the Bank and IMF and has led them to greater reliance on each other's special expertise. This convergence has been hastened by the debt crisis, brought on by the inability of developing countries to repay the enormous loans they contracted during the late 1970s and early 1980s. The debt crisis has emphasized that economic growth can be sustained only when resources are being used efficiently and that resources can be used efficiently only in a stable monetary and financial environment.

The bedrock of cooperation between the Bank and IMF is the regular and frequent interaction of economists and loan officers who work on the same country. The Bank staff brings to this interchange a longer-term view of the slow process of development and a profound knowledge of the structural requirements and economic potential of a country. The IMF staff contributes its own perspective on the day-to-day capability of a country to sustain its flow of payments to creditors and to attract from them investment finance, as well as on how the country is integrated within the world economy. This interchange of information is backed up by a coordination of financial assistance to members. For instance, the Bank has been approving structural- or sector-adjustment loans for most of the countries that are taking advantage of financial assistance from the IMF.

In addition, both institutions encourage other lenders, both private and official, to join with them in co-financing projects and in mobilizing credits to countries that are in need. Cooperation between the Bretton Woods Institutions has two results: the identification of programs that will encourage growth in a stable economic environment and the coordination of financing that will ensure the success of these programs. Other lenders, particularly commercial banks, frequently make credits available only after seeing satisfactory performance by the borrowing country of its program of structural adjustment.

Cooperation between the Bank and the IMF has over the past decade been formalized with the establishment in the IMF of procedures to provide financing at below market rates to its poorest member countries. These procedures enable the IMF to make available up to $12 billion to those 70 or so poor member countries that adjust the structure of their economies to improve their balance of payment position and to foster growth.

The Bank joins with the IMF in providing additional money for these countries from IDA. But what IDA can provide in financial resources is only a fraction of the world's minimum needs for concessional external finance. Happily, various governments and international agencies have responded positively to the Bank's special action program for low-income, debt-distressed countries of the region by pledging an extra $7 billion for cofinancing programs arranged by the Bank.

The Bank and the IMF have distinct mandates that allow them to contribute, each in its own way, to the stability of the international monetary and financial system and to the fostering of balanced economic growth throughout the entire membership. Since their founding 50 years ago, both institutions have been challenged by changing economic circumstances to develop new ways of assisting their membership. The Bank has expanded its assistance from an orientation toward projects to the broader aspects of economic reform. Simultaneously the IMF has gone beyond concern with simple balance of payment adjustment to interest itself in the structural reform of its members' economies. Some overlapping by both institutions has inevitably occurred, making cooperation between the Bank and the IMF crucial. Devising programs that will integrate members' economies more fully into the international monetary and financial system and at the same time encourage economic expansion continues to challenge the expertise of both Bretton Woods Institutions.

The International Monetary Fund and the World Bank at a Glance	
International Monetary Fund • oversees the international monetary system • promotes exchange stability and orderly exchange relations among its member countries • assists all members--both industrial and developing countries--that find themselves in temporary balance of payments difficulties by providing short- to medium-term credits • supplements the currency reserves of its members through the allocation of SDRs (special drawing rights); to date SDR 21.4 billion has been issued to member countries in proportion to their quotas • draws its financial resources principally from the quota subscriptions of its member countries • has at its disposal fully paid-in quotas now totaling SDR 145 billion (about $215 billion) • has a staff of 2,300 drawn from 182 member countries	**World Bank** • seeks to promote the economic development of the world's poorer countries • assists developing countries through long-term financing of development projects and programs • provides to the poorest developing countries whose per capita GNP is less than $865 a year special financial assistance through the International Development Association (IDA) • encourages private enterprises in developing countries through its affiliate, the International Finance Corporation (IFC) • acquires most of its financial resources by borrowing on the international bond market • has an authorized capital of $184 billion, of which members pay in about 10 percent • has a staff of 7,000 drawn from 180 member countries

United Nations Conference on Trade and Development

The headquarters of the United Nations Conference on Trade and Development are located in the Palace of Nations (United Nations Office at Geneva, Switzerland).The United Nations Conference on Trade and Development (UNCTAD) (French Conference des Nations unies sur le Commerce et le Development (CNUCED)) was established in 1964 as a permanent intergovernmental body.

UNCTAD is the principal organ of the United Nations General Assembly dealing with trade, investment, and development issues. The organization's goals are to: "maximize the trade, investment and development opportunities of developing countries and assist them in their efforts to integrate into the world economy on an equitable basis."

The primary objective of UNCTAD is to formulate policies relating to all aspects of development including trade, aid, transport, finance and technology. The conference ordinarily meets once in four years; the permanent secretariat is in Geneva.

One of the principal achievements of UNCTAD has been to conceive and implement the Generalised System of Preferences (GSP). It was argued in UNCTAD that to promote exports of manufactured goods from developing countries, it would be necessary to offer special tariff concessions to such exports. Accepting this argument, the developed countries formulated the GSP scheme under which manufacturers' exports and some agricultural goods from the developing countries enter duty-free or at reduced rates in the developed countries. Since imports of such items from other developed countries are subject to the normal rates of duties, imports of the same items from developing countries would enjoy a competitive advantage.

The creation of UNCTAD in 1964 was based on concerns of developing countries over the international market, multi-national corporations, and great disparity between developed nations and developing nations. The United Nations Conference on Trade and Development was established to provide a forum where the developing countries could discuss the problems relating to their economic development. The organisation grew from the view that existing institutions like GATT (now replaced by the World Trade Organization, WTO), the International Monetary Fund (IMF), and World Bank were not properly organized to handle the particular problems of developing countries. Later, in the 1970s and 1980s, UNCTAD was closely associated with the idea of a New International Economic Order (NIEO).

The first UNCTAD conference took place in Geneva in 1964, the second in New Delhi in 1968, the third in Santiago in 1972, fourth in Nairobi in 1976, the fifth in Manila in 1979, the sixth in Belgrade in 1983, the seventh in Geneva in 1987, the eighth in Cartagena in 1992, the ninth at Johannesburg (South Africa) in 1996, the tenth in Bangkok (Thailand) in 2000, the eleventh in São Paulo (Brazil) in 2004, the twelfth in Accra in 2008 and the thirteenth in Doha (Qatar) in 2012.

Currently, UNCTAD has 194 member states and is headquartered in Geneva, Switzerland. UNCTAD has 400 staff members and a bi-annual (2010–2011) regular budget of $138 million in core expenditures and $72 million in extra-budgetary technical assistance funds. It is a member of the United Nations Development Group. There are non-governmental organizations participating in the activities of UNCTAD.

Membership

- UNCTAD Members
- UNCTAD Members at the Trade and Development Board
- Members, List A
- Members, List B
- Members, List C
- Members, List D

Members, to be assigned as of October 2012, 194 states are UNCTAD members: all UN members and the Holy See. UNCTAD members are divided into four lists, the division being based on United Nations Regional Groups with six members unassigned: Armenia, Kiribati, Nauru, South Sudan, Tajikistan, Tuvalu. List A consists mostly of countries in the African and Asia-Pacific Groups of the UN. List B consists of countries of the Western European and Others Group. List C consists of countries of the Group of Latin American and Caribbean States (GRULAC). List D consists of countries of the Eastern European Group.

The lists, originally defined in 19th General Assembly resolution 1995 serve to balance geographical distribution of member states' representation on the Trade Development Board and other UNCTAD structures. The lists are similar to those of UNIDO, an UN specialized agency. The full lists are as follows:

List A (100 members): Afghanistan, Algeria, Angola, Bahrain, Bangladesh, Benin, Bhutan, Bosnia and Herzegovina, Botswana, Brunei Darussalam, Burkina Faso, Burundi, Cambodia, Cameroon, Cape Verde, Central African Republic, Chad, China, Comoros, Côte d'Ivoire, Republic of Congo, Democratic Republic of Congo, Djibouti, Egypt, Equatorial Guinea, Eritrea, Ethiopia, Fiji, Gabon, Gambia, Ghana, Guinea, Guinea-Bissau, India, Indonesia, Iran, Iraq, Israel, Jordan, Kenya, Kuwait, Laos, Lebanon, Lesotho, Liberia, Libya, Madagascar, Malawi , Malaysia, Maldives, Mali, Marshall Islands, Mauritania, Mauritius, Micronesia, Mongolia, Morocco, Mozambique, Myanmar, Namibia, Nepal, Niger, Nigeria, North Korea, Oman, Pakistan, Palau, Papua New Guinea, Philippines, Qatar, South Korea, Rwanda, Samoa, Sao Tome and Principe, Saudi Arabia, Senegal, Seychelles, Sierra Leone, Singapore, Solomon Islands, Somalia, South Africa, Sri Lanka, Sudan, Swaziland, Syria, Thailand, Timor-Leste, Togo, Tonga, Tunisia, Turkmenistan, Uganda, United Arab Emirates, Tanzania, Vanuatu, Viet Nam, Yemen, Zambia, Zimbabwe.

List B (31 members): Andorra, Australia, Austria, Belgium, Canada, Cyprus, Denmark, Finland, France, Germany, Greece, Holy See, Iceland, Ireland, Italy, Japan, Liechtenstein, Luxembourg, Malta, Monaco, Netherlands, New Zealand, Norway, Portugal, San Marino, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States.

List C (33 members): Antigua and Barbuda, Argentina, Bahamas, Barbados, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cuba, Dominica, Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname, Trinidad and Tobago, Uruguay, Venezuela.

List D (24 members): Albania, Azerbaijan, Belarus, Bulgaria, Croatia, Czech Republic, Estonia, Georgia, Hungary, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Montenegro, Poland, Moldova, Romania, Russia, Serbia, Slovakia, Slovenia, Macedonia, Ukraine, Uzbekistan.

Not assigned countries (6 members): Armenia, Kiribati, Nauru, South Sudan, Tajikistan, Tuvalu. Other states that do not participate are Cook Islands, Niue and the states with limited recognition.

Meetings

The inter-governmental work is done at five levels of meetings:

- The UNCTAD Conference – held every four years:
- UNCTAD VIII in Cartagena, Colombia on 8–25 February 1992
- UNCTAD IX in Midrand, South Africa on 27 April – 11 May 1996
- UNCTAD X in Bangkok, Thailand on 12–19 February 2000
- UNCTAD XI in São Paulo, Brazil on 13–18 June 2004
- UNCTAD XII in Accra, Ghana on 21–25 April 2008
- UNCTAD XIII in Doha, Qatar on 21–26 April 2012

The UNCTAD Trade and Development Board – the Board manages the work of UNCTAD between two conferences and meets up to three times every year;

Four UNCTAD Commissions and one Working Party – these meet more often than the Board to take up policy, programme and budgetary issues;

Expert Meetings – the commissions will convene expert meetings on selected topics to provide substantive and expert input for Commission policy discussions.

Reports

UNCTAD produces a number of topical reports, including:

- The Trade and Development Report
- The Trade and Environment Review
- The World Investment Report
- The Economic Development in Africa Report

- The Least Developed Countries Report
- UNCTAD Statistics
- The Information Economy Report
- The Review of Maritime Transport
- The International Accounting and Reporting Issues Annual Review
- The Technology and Innovation Report

World Trade Organization (WTO)

The World Trade Organization (WTO) is an organization that intends to supervise and liberalize international trade. The organization officially commenced on 1 January 1995 under the Marrakech Agreement, signed by 123 nations on 15 April 1994, replacing the General Agreement on Tariffs and Trade (GATT), which commenced in 1948. The organization deals with regulation of trade between participating countries by providing a framework for negotiating and formalizing trade agreements and a dispute resolution process aimed at enforcing participants' adherence to WTO agreements, which are signed by representatives of member governments:fol.9–10 and ratified by their parliaments. Most of the issues that the WTO focuses on derive from previous trade negotiations, especially from the Uruguay Round (1986–1994).

The organization is attempting to complete negotiations on the Doha Development Round, which was launched in 2001 with an explicit focus on addressing the needs of developing countries. As of June 2012, the future of the Doha Round remained uncertain: the work programme lists 21 subjects in which the original deadline of 1 January 2005 was missed, and the round is still incomplete. The conflict between free trade on industrial goods and services but retention of protectionism on farm subsidies to domestic agricultural sector (requested by developed countries) and the substantiation of the international liberalization of fair trade on agricultural products (requested by developing countries) remain the major obstacles. These points of contention have hindered any progress to launch new WTO negotiations beyond the Doha Development Round. As a result of this impasse, there have been an increasing number of bilateral free trade agreements signed. As of July 2012, there were various negotiation groups in the WTO system for the current agricultural trade negotiation which is in the condition of stalemate.

WTO's current Director-General is Roberto Azevêdo, who leads a staff of over 600 people in Geneva, Switzerland. A trade facilitation agreement known as the Bali Package was reached by all members on 7 December 2013, the first comprehensive agreement in the organization's history

History

The economists Harry White (left) and John Maynard Keynes at the Bretton Woods Conference. Both had been strong advocates of a central-controlled international trade environment and recommended the establishment of three institutions: the IMF (for fiscal and monetary issues);

- The World Bank (for financial and structural issues);

- The ITO (for international economic cooperation)

The WTO's predecessor, the General Agreement on Tariffs and Trade (GATT), was established after World War II in the wake of other new multilateral institutions dedicated to international economic cooperation – notably the Bretton Woods institutions known as the World Bank and the International Monetary Fund. A comparable international institution for trade, named the International Trade Organization was successfully negotiated. The ITO was to be a United Nations specialized agency and would address not only trade barriers but other issues indirectly related to trade, including employment, investment, restrictive business practices, and commodity agreements. But the ITO treaty was not approved by the U.S. and a few other signatories and never went into effect.

In the absence of an international organization for trade, the GATT would over the years "transform itself" into a de facto international organization.

GATT rounds of negotiations

General Agreement on Tariffs and Trade

The GATT was the only multilateral instrument governing international trade from 1946 until the WTO was established on 1 January 1995. Despite attempts in the mid-1950s and 1960s to create some form of institutional mechanism for international trade, the GATT continued to operate for almost half a century as a semi-institutionalized multilateral treaty regime on a provisional basis.

From Geneva to Tokyo:

Seven rounds of negotiations occurred under GATT. The first real GATT trade rounds concentrated on further reducing tariffs. Then, the Kennedy Round in the mid-sixties brought about a GATT anti-dumping Agreement and a section on development. The Tokyo Round during the seventies was the first major attempt to tackle trade barriers that do not take the form of tariffs, and to improve the system, adopting a series of agreements on non-tariff barriers, which in some cases interpreted existing GATT rules, and in others broke entirely new ground. Because these plurilateral agreements were not accepted by the full GATT membership, they were often informally called "codes". Several of these codes were amended in the Uruguay Round, and turned into multilateral commitments accepted by all WTO members. Only four remained plurilateral (those on government procurement, bovine meat, civil aircraft and dairy products), but in 1997 WTO members agreed to terminate the bovine meat and dairy agreements, leaving only two.

It was the biggest negotiating mandate on trade ever agreed: the talks were going to extend the trading system into several new areas, notably trade in services and intellectual property, and to reform trade in the sensitive sectors of agriculture and textiles; all the original GATT articles were up for review. The Final Act concluding the Uruguay Round and officially establishing the WTO regime was signed 15 April 1994, during the ministerial meeting at Marrakesh, Morocco, and hence is known as the Marrakesh Agreement.

The GATT still exists as the WTO's umbrella treaty for trade in goods, updated as a result of the Uruguay Round negotiations (a distinction is made between GATT 1994, the updated parts of GATT, and

GATT 1947, the original agreement which is still the heart of GATT 1994). GATT 1994 is not however the only legally binding agreement included via the Final Act at Marrakesh; a long list of about 60 agreements, annexes, decisions and understandings was adopted. The agreements fall into a structure with six main parts:

The Agreement Establishing the WTO

- Goods and investment – the Multilateral Agreements on Trade in Goods including the GATT 1994 and the Trade Related Investment Measures (TRIMS)
- Services — the General Agreement on Trade in Services
- Intellectual property – the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS)
- Dispute settlement (DSU)

Reviews of governments' trade policies (TPRM)

In terms of the WTO's principle relating to tariff "ceiling-binding" (No. 3), the Uruguay Round has been successful in increasing binding commitments by both developed and developing countries, as may be seen in the percentages of tariffs bound before and after the 1986–1994 talks.

Ministerial conferences

The World Trade Organization Ministerial Conference of 1998, in the Palace of Nations (Geneva, Switzerland).The highest decision-making body of the WTO is the Ministerial Conference, which usually meets every two years. It brings together all members of the WTO, all of which are countries or customs unions. The Ministerial Conference can take decisions on all matters under any of the multilateral trade agreements. The inaugural ministerial conference was held in Singapore in 1996. Disagreements between largely developed and developing economies emerged during this conference over four issues initiated by this conference, which led to them being collectively referred to as the "Singapore issues". The second ministerial conference was held in Geneva in Switzerland. The third conference in Seattle, Washington ended in failure, with massive demonstrations and police and National Guard crowd-control efforts drawing worldwide attention. The fourth ministerial conference was held in Doha in the Persian Gulf nation of Qatar. The Doha Development Round was launched at the conference. The conference also approved the joining of China, which became the 143rd member to join. The fifth ministerial conference was held in Cancún, Mexico, aiming at forging agreement on the Doha round. An alliance of 22 southern states, the G20 developing nations (led by India, China,[30] Brazil, ASEAN led by the Philippines), resisted demands from the North for agreements on the so-called "Singapore issues" and called for an end to agricultural subsidies within the EU and the US. The talks broke down without progress.

The sixth WTO ministerial conference was held in Hong Kong from 13–18 December 2005. It was considered vital if the four-year-old Doha Development Round negotiations were to move forward sufficiently to conclude the round in 2006. In this meeting, countries agreed to phase out all their agricultural export subsidies by the end of 2013, and terminate any cotton export subsidies by the end of 2006. Further concessions to developing countries included an agreement to introduce duty-free, tariff-free access for goods from the Least Developed Countries, following the Everything but Arms initiative of the European Union — but with up to 3% of tariff lines exempted. Other major issues were left for further negotiation to be completed by the end of 2010. The WTO General Council, on 26 May 2009, agreed to hold a seventh WTO ministerial conference session in Geneva from 30 November-3 December 2009. A statement by chairman Amb. Mario Matus acknowledged that the prime purpose was to remedy a breach of protocol requiring two-yearly "regular" meetings, which had lapsed with the Doha Round failure in 2005, and that the "scaled-down" meeting would not be a negotiating session, but "emphasis will be on transparency and open discussion rather than on small group processes and informal negotiating structures". The general theme for discussion was "The WTO, the Multilateral Trading System and the Current Global Economic Environment"

Functions

Among the various functions of the WTO, these are regarded by analysts as the most important:

- It oversees the implementation, administration and operation of the covered agreements.
- It provides a forum for negotiations and for settling disputes.
- Additionally, it is the WTO's duty to review and propagate the national trade policies, and to ensure the coherence and transparency of trade policies through surveillance in global economic policy-making. Another priority of the WTO is the assistance of developing, least-developed and low-income countries in transition to adjust to WTO rules and disciplines through technical cooperation and training.

i. The WTO shall facilitate the implementation, administration and operation and further the objectives of this Agreement and of the Multilateral Trade Agreements, and shall also provide the frame work for the implementation, administration and operation of the multilateral Trade Agreements.

ii. The WTO shall provide the forum for negotiations among its members concerning their multilateral trade relations in matters dealt with under the Agreement in the Annexes to this Agreement.

iii. The WTO shall administer the Understanding on Rules and Procedures Governing the Settlement of Disputes.

iv. The WTO shall administer Trade Policy Review Mechanism.

v. With a view to achieving greater coherence in global economic policy making, the WTO shall cooperate, as appropriate, with the international Monetary Fund (IMF) and with the International Bank for Reconstruction and Development (IBRD) and its affiliated agencies.

The above five listings are the additional functions of the World Trade Organization. As globalization proceeds in today's society, the necessity of an International Organization to manage the trading systems has been of vital importance. As the trade volume increases, issues such as protectionism, trade barriers, subsidies, violation of intellectual property arise due to the differences in the trading rules of every nation. The World Trade Organization serves as the mediator between the nations when such problems arise. WTO could be referred to as the product of globalization and also as one of the most important organizations in today's globalized society.

The WTO is also a center of economic research and analysis: regular assessments of the global trade picture in its annual publications and research reports on specific topics are produced by the organization. Finally, the WTO cooperates closely with the two other components of the Bretton Woods system, the IMF and the World Bank.

Principles of the trading system

The WTO establishes a framework for trade policies; it does not define or specify outcomes. That is, it is concerned with setting the rules of the trade policy games.[45] Five principles are of particular importance in understanding both the pre-1994 GATT and the WTO:

Non-discrimination

It has two major components: the most favoured nation (MFN) rule, and the national treatment policy. Both are embedded in the main WTO rules on goods, services, and intellectual property, but their precise scope and nature differ across these areas. The MFN rule requires that a WTO member must apply the same conditions on all trade with other WTO members, i.e. a WTO member has to grant the most favorable conditions under which it allows trade in a certain product type to all other WTO members. "Grant someone a special favour and you have to do the same for all other WTO members." National treatment means that imported goods should be treated no less favorably than domestically produced goods (at least after the foreign goods have entered the market) and was introduced to tackle non-tariff barriers to trade (e.g. technical standards, security standards et al. discriminating against imported goods).

Reciprocity

It reflects both a desire to limit the scope of free-riding that may arise because of the MFN rule, and a desire to obtain better access to foreign markets. A related point is that for a nation to negotiate, it is necessary that the gain from doing so be greater than the gain available from unilateral liberalization; reciprocal concessions intend to ensure that such gains will materialise.

Binding and enforceable commitments

The tariff commitments made by WTO members in a multilateral trade negotiation and on accession are enumerated in a schedule (list) of concessions. These schedules establish "ceiling bindings": a country can change its bindings, but only after negotiating with its trading partners, which could mean compensating them for loss of trade. If satisfaction is not obtained, the complaining country may invoke the WTO dispute settlement procedures.

Transparency

The WTO members are required to publish their trade regulations, to maintain institutions allowing for the review of administrative decisions affecting trade, to respond to requests for information by other members, and to notify changes in trade policies to the WTO. These internal transparency requirements are supplemented and facilitated by periodic country-specific reports (trade policy reviews) through the Trade Policy Review Mechanism (TPRM). The WTO system tries also to improve predictability and stability, discouraging the use of quotas and other measures used to set limits on quantities of imports.

Safety valves

In specific circumstances, governments are able to restrict trade. The WTO's agreements permit members to take measures to protect not only the environment but also public health, animal health and plant health.

There are three types of provision in this direction:

- Articles allowing for the use of trade measures to attain non-economic objectives;
- Articles aimed at ensuring "fair competition"; members must not use environmental protection measures as a means of disguising protectionist policies.
- Provisions permitting intervention in trade for economic reasons
- Exceptions to the MFN principle also allow for preferential treatment of developing countries, regional free trade areas and customs unions.

Organizational structure

The General Council has the following subsidiary bodies which oversee committees in different areas:

Council for Trade in Goods

There are 11 committees under the jurisdiction of the Goods Council each with a specific task. All members of the WTO participate in the committees. The Textiles Monitoring Body is separate from the other committees but still under the jurisdiction of Goods Council. The body has its own chairman and only 10 members. The body also has several groups relating to textiles.

Council for Trade-Related Aspects of Intellectual Property Rights

Information on intellectual property in the WTO, news and official records of the activities of the TRIPS Council, and details of the WTO's work with other international organizations in the field.

Council for Trade in Services

The Council for Trade in Services operates under the guidance of the General Council and is responsible for overseeing the functioning of the General Agreement on Trade in Services (GATS). It is open to all WTO members, and can create subsidiary bodies as required.

Trade Negotiations Committee

The Trade Negotiations Committee (TNC) is the committee that deals with the current trade talks round. The chair is WTO's director-general. As of June 2012 the committee was tasked with the Doha Development Round.

The Service Council has three subsidiary bodies: financial services, domestic regulations, GATS rules and specific commitments. The council has several different committees, working groups, and working parties.

There are committees on the following: Trade and Environment; Trade and Development (Subcommittee on Least-Developed Countries); Regional Trade Agreements; Balance of Payments Restrictions; and Budget, Finance and Administration. There are working parties on the following: Accession. There are working groups on the following: Trade, debt and finance; and Trade and technology transfer.

Decision-making

The WTO describes itself as "a rules-based, member-driven organization — all decisions are made by the member governments, and the rules are the outcome of negotiations among members". The WTO Agreement foresees votes where consensus cannot be reached, but the practice of consensus dominates the process of decision-making.

Richard Harold Steinberg (2002) argues that although the WTO's consensus governance model provides law-based initial bargaining, trading rounds close through power-based bargaining favouring Europe and the U.S., and may not lead to Pareto improvement.

Dispute settlement and Dispute settlement in the WTO

In 1994, the WTO members agreed on the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU) annexed to the "Final Act" signed in Marrakesh in 1994. Dispute settlement is regarded by the WTO as the central pillar of the multilateral trading system, and as a "unique contribution to the stability of the global economy". WTO members have agreed that, if they believe fellow-members are violating trade rules, they will use the multilateral system of settling disputes instead of taking action unilaterally.

The operation of the WTO dispute settlement process involves the DSB panels, the Appellate Body, the WTO Secretariat, arbitrators, independent experts and several specialized institutions. Bodies involved in the dispute settlement process, World Trade Organization.

Accession and membership ANS World Trade Organization accession and membership

The process of becoming a WTO member is unique to each applicant country, and the terms of accession are dependent upon the country's stage of economic development and current trade regime. The process takes about five years, on average, but it can last more if the country is less than fully committed to the process or if political issues interfere. The shortest accession negotiation was that of the Kyrgyz Republic, while the longest was that of Russia, which, having first applied to join GATT in 1993, was approved for membership in December 2011 and became a WTO member on 22 August 2012.

The second longest was that of Vanuatu, whose Working Party on the Accession of Vanuatu was established on 11 July 1995. After a final meeting of the Working Party in October 2001, Vanuatu requested more time to consider its accession terms. In 2008, it indicated its interest to resume and conclude its WTO accession. The Working Party on the Accession of Vanuatu was reconvened informally on 4 April 2011 to discuss Vanuatu's future WTO membership. The re-convened Working Party completed its mandate on 2 May

2011. The General Council formally approved the Accession Package of Vanuatu on 26 October 2011. On 24 August 2012, the WTO welcomed Vanuatu as its 157th member. An offer of accession is only given once consensus is reached among interested parties.

GATT and the World Trade Organization

In 1993, the GATT was updated (GATT 1994) to include new obligations upon its signatories. One of the most significant changes was the creation of the World Trade Organization (WTO). The 75 existing GATT members and the European Communities became the founding members of the WTO on 1 January 1995. The other 52 GATT members rejoined the WTO in the following two years (the last being Congo in 1997). Since the founding of the WTO, 21 new non-GATT members have joined and 29 are currently negotiating membership. There are a total of 159 member countries in the WTO, with Laos and Tajikistan being new members as of 2013.

Of the original GATT members, Syria and the SFR Yugoslavia have not rejoined the WTO. Since FR Yugoslavia, (renamed as Serbia and Montenegro and with membership negotiations later split in two), is not recognised as a direct SFRY successor state; therefore, its application is considered a new (non-GATT) one. The General Council of WTO, on 4 May 2010, agreed to establish a working party to examine the request of Syria for WTO membership. The contracting parties who founded the WTO ended official agreement of the "GATT 1947" terms on 31 December 1995. Montenegro became a member in 2012, while Serbia is in the decision stage of the negotiations and is expected to become one of the newest members of the WTO in 2014 or in near future.

Whilst GATT was a set of rules agreed upon by nations, the WTO is an institutional body. The WTO expanded its scope from traded goods to include trade within the service sector and intellectual property rights. Although it was designed to serve multilateral agreements, during several rounds of GATT negotiations (particularly the Tokyo Round) plurilateral agreements created selective trading and caused fragmentation among members. WTO arrangements are generally a multilateral agreement settlement mechanism of GATT.

International trade Policy and Strategy (17BAU602B)

Unit V - MCQ

SI. NO	Question	Option 1	Option 2	Option 3	Option 4	Option 5	Option 6	Answer
1	Several levels of economic integration are possible. Three such levels from the least integrated to the most integrated are…………………….	free trade area, customs union, common market	customs union, political union, economic union	free trade area, political union, common market	common market, customs union, political union			free trade area, customs union, common market
2	Regional economic integration can be seen as an attempt to achieve gains from…………………. beyond those attainable under international agreements such as the WTO.	common currencies	region-specific tariffs	the free flow of trade and investment	gains from common access to intellectual property			the free flow of trade and investment
3	One of the main impediments to regional economic integration is the cost that individuals must bear even while the country as a whole might gain. The second major impediment is the……………	increased concern about monetary policy	loss of national sovereignty	loosening of control over fiscal issues	the increased costs of defending and monitoring borders			loss of national sovereignty

	……..							
4	If, prior to NAFTA, the U.S. produced its own textiles at a higher cost than Mexico, but after NAFTA imports them from Mexico……… …	trade has been diverted	trade has been created	Mexico is worse off	the U.S. is worse off			trade has been created
5	Regional economic integration, for example, the EU, offers significant opportunities to US businesses including…… ……	non-EU companies no longer need to set up subsidiaries in EU countries	companies can realize significant cost economies by centralizing operations where factor costs and skills are optimal	it makes no difference where in the EU one locates an operation since the costs are the same throughout	cultural differences and national consumer preferences are now irrelevant			companies can realize significant cost economies by centralizing operations where factor costs and skills are optimal
6	Regional economic integration presents potentially significant	long-term improvements in the competitive positions	the end of a “fortress” mentality means other	the end to efforts to rationalize production and	the imposition of US standards, recognized as a pioneer in			the end to efforts to rationalize production and reduce

	threats to business outside the area, including……………….	of firms inside the areas.	firms outside the area will be able to enter the areas more easily to compete with existing area firms	reduce costs	regional economic integration, which means US firms will not be able to get around the legal barriers			costs
7	The North American Free Trade Agreement (NAFTA)………	set up a common trading area for all states in the upper Midwest and New England	created the world's largest free trade zone	includes only Canada and the United States	includes only Canada and Mexico			created the world's largest free trade zone
8	How has NAFTA affected Mexico?	There is increased confidence on the part of foreign firms to invest in Mexico.	Reduced economic advantage of Mexican labor over its American counterpart	Increased surplus of more than $2 billion in farm trade with America	Reduced farm subsidies to improve the efficiency of agricultural exports			There is increased confidence on the part of foreign firms to invest in Mexico.
9	Which of the following is not a preferential trading arrangement?	EU	NAFTA	OECD	Anti-dumping duty			OECD
10	Because wages in Mexico before the NAFTA were only a small	Prior to NAFTA, Mexican workers were paid	After NAFTA, most U.S. firms	After NAFTA, most U.S. firms	Prior to NAFTA, since U.S. tariffs			Prior to NAFTA, since U.S. tariffs

	fraction (perhaps 1/10) of wages in the U.S., we should infer that…………..	far below their productivity	would be unable to compete with imports from Mexico	would close their U.S. plants and move to Mexico	against Mexico were small, the productivity of Mexican workers must also have been only a small fraction of that in the U.S			against Mexico were small, the productivity of Mexican workers must also have been only a small fraction of that in the U.S
11	European Union was established in………..	1995	1985	1993	1983			1993
12	Which of the following is not a key quality of an international organization?	voluntary cooperation	shared interests	communal management	sovereignty			sovereignty
13	In most cases, support by states for regionalism is motivated primarily by………...	the desire for economic cooperation	the desire for political unity	the desire for social cohesion	the desire for shared military protection			the desire for economic cooperation
14	Realists believe that……….	Option states lost their credibility and political rights following world war two	the global system is anarchic	states trust long-term cooperation and alliances	humans are naturally cooperative			he global system is anarchic
15	All but one of these qualities increase the integrative	Their economic equality and	Like-mindedness among	The absence of interest	The capacity of decision-			The absence of interest

	potential of states. Mark the exception…………..	compatibility	their elites	group activity	makers to respond to public demands			group activity
16	Which of this is not a useful approach to the study of the EU?	international organization	unique	nation	political system in its own right			nation
17	How is governance best defined?	the rules and norms that lie at the basis of a system of government	an arrangement in which power is shared among groups in divided societies	an arrangement by which decisions are made without the existence of formal institutions of government	an administrative system in which power is shared and distributed horizontally and vertically among different levels of government			the rules and norms that lie at the basis of a system of government
18	Which of these best describes a federal system?	one in which authority is divided between two or more layers of government, each with independent powers	one in which the local units of government have more powers than the national government	one in which power is distributed both horizontally and vertically	one in which states pool authority in the hands of a powerful joint government			one in which authority is divided between two or more layers of government, each with independent powers
19	Which of the following countries is not a federation?	Germany	France	Austria	India			France

20	Which one of these statements best describes a confederal system?	national government has more power than is the case in a federal system	authority is divided between two or more layers of government, each with independent powers	power is shared among groups in divided societies	states come together in a loose political union, using joint institutions with limited authority but leaving most of the power in the hands of the states			national government has more power than is the case in a federal system
21	The most successful example of regional integration to date is………..	The European Union	NAFTA	OPEC	ASEAN			The European Union
22	How many countries belong to ASEAN today?	10	12	15	16			10
23	ASEAN was founded on……	1956	1967	1968	1969			1967
24	What does ASEAN stand for?	Association of Southwest Asian Nations	Association of Southnorth Asian Nations	Association of Southeast Asian Nations	Association of South Asian Nations			Association of Southeast Asian Nations
25	Which country joined ASEAN in 1999 ?	India	Singapore	Srilanka	Cambodia			Cambodia

26	What is the name of the anthem of ASEAN?	The ASEAN Way	The WTO way	The GATT Way	The FTA way			The ASEAN Way
27	How many colours are there on the flag of ASEAN?	4	5	6	2			4
28	What does the blue colour on the flag of ASEAN represent?	Prosperit y	peace	Peace and stability	Economi c developm ent			Peace and stability
29	What is the correct motto of ASEAN?	peace	Peace and stability	Prosperit y	One Vision, One Identity, One Communi ty			One Vision, One Identity, One Communi ty
30	How many countries in ASEAN does the Mekong River flow through?	4	5	6	2			5
31	When is ASEAN Day celebrated annually?	12-Sep	31-Mar	August 8th	9-Jul			August 8th
32	Which among the following is not a part of UNO?	ASEAN	FAO	IMF	WTO			ASEAN
33	SAARC……… ..	South Asian Associati on for Regional Co-operation	South Asian Associat ion for Regiona l Culture	South Asian Associati on for Regional Class	South Asian Associati on for Regional cluster			South Asian Associati on for Regional Co-operation

34	When was SAARC established?	#######	#######	#######	#######			8-Dec-85
35	Where was SAARC established?	Dhaka	NewDelhi	Colombo	Pakistan			Dhaka
36	How many countries joined together to form SAARC?	7	5	6	8			7
37	Which country was included as 8th member of SAARC at the 14th SAARC Summit held in New Delhi 2007?	Afganistan	Japan	Iran	Srilanka			Afganistan
38	Who originally mooted the concept of SAARC?	Abul Ahsan	Ziaur Rahman	Manmohan Singh	Jaimohan			Ziaur Rahman
39	What was the main aim of SAARC?	Non - alignity	Regional cooperation	Non - interference in other's internal affairs	Inter trade			Regional cooperation
40	Where is the permanent secretariat of SAARC situated?	Dhaka	Kathmandu	Colombo	Afganistan			Kathmandu
41	In which city of India was the second SAARC Summit hosted in 1986?	New Delhi	Bangalore	Chennai	Hydrabad			Bangalore

42	Where was the first SAARC Cultural festival held in 1992?	Colombo	Delhi	Dhaka	Kathmandu			Delhi
43	SAFTA means………. ….	South Asian Association for Regional Co-operation	South Asian Association for Regional Culture	South Asian Association for Regional Class	South Asian Free Trade Agreement			South Asian Free Trade Agreement
44	SAFTA came into effect from…..	Jan-06	Apr-08	Oct-01	Dec-02			Jan-06
45	Consider the following statements: I. The Agreement of SAFTA came into effect from January 2006. II.As per the agreement terms, India, Pakistan and Sri Lanka have to scale down their customs duties to the level of 0-5 percent by 2013. Which of the statement given below is/are correct?	I Only	II Only	Both I and II	Nether I or II			II Only
46	South Asian Free Trade Area (SAFTA) is an agreement reached on 6 January 2004 at	10	11	12	13			12

	the ……...SAARC summit							
47	SAFTA SAARC Summit in……..	Pakistan	India	Srilanka	Afghanistan			Pakistan
48	SAFTA to reduce ………. of all traded goods to zero by the year 2016	Excise Duty	VAT	Custom duties	GST			Custom duties
49	One of the principles of SAFTA……… …	encourage trade between Asian Countries	negotiation of tariff reform step by step	reduce custom duties	Prohobit terriorism			negotiation of tariff reform step by step
50	SAFTA to reduce customs duties of all traded goods to zero by the year …………	2014	2015	2016	2013			2016
51	SAFTA agreement by the ………...governments	5	6	7	8			7
52	The main objective of the agreement is to promote……	free trade	competition	meet demand	supply money			competiton
53	SAFTA aims to benefit the people of the countries by bringing…….	unity	free trade	competition	transparency and integrity			transparency and integrity

54	SAFTA to …………...customs duties of all traded goods to zero by the year 2016	reduce	increase	constant	significantly			reduce
55	The instrument involved in SAFTA……..	increase the level of trade	economic cooperation	medium and long term contracts	Institutional Arrangements			Institutional Arrangements
56	The South Asian Free Trade Agreement (SAFTA) has not been a success because of I. narrow export base of countries, II. Lack of bilateral free trade agreements III Political hurdles. Select the correct answer using the codes given below:	I and II only	I and III only	II and III	I, II and III			I and III only
57	India has signed Comprehensive Economic Partnership Agreement (CEPA) with 1. USA, 2. Singapore, 3. Japan Select the correct answer using the codes given below.	1 and 2	3 only	2 and 3 only	1,2, and 3			2 and 3 only

58	The Indo-Sri Lanka Free Trade Agreement (ISFTA), which was signed on 28th……..	Jan-98	Feb-98	Dec-98	Oct-98			Dec-98
59	The 13th amendment has been a point of contention between India and Sri Lanka. The 13th amendment provided for 1. establishment of provisional councils 2, taking action against the human rights violators 3. creation of a second chamber in central legislature. Select the correct answer using the codes given below.	1 only	1 and 2	2 and 3	1,2 and 3			1 only
60	SAFTA to reduce customs duties of all ……….. to zero by the year 2016	services	traded goods	manufactured goods	ITES			traded goods