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INVESTIGATING THE REASONS OF GREECE'S UNDERPERFORMING IN FORFAITING

Abstract

The aim of this paper is to point out the characteristics of Forfaiting as it is applied the Greek economy and to investigate the reasons of its underperformance. The conclusions are linked with the dominant role of transactions with free shipping documents instead of time letters of credit.

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Introduction

Forfaiting is consider a medium or long term form of financing that consists of discounting obligations due to mature at a future date with non-recourse to the exporter in case of non-performance.

It is considered as a flexible form of financing that can be adjusted to the varying requirements of the exporters.

Forfaiting covers the credit risk and besides the risks of fluctuation of interest rates and exchange rates. The discounting may be up to 100% of the present value of each transaction after subtracting the expenses. Forfaiting is addressed to exporters giving them flexibility in their credit policy without binding existing credit lines of the companies. It includes 100% financing without recourse. The claims are secured either by the letters of guarantee or by bills of exchange, promissory notes or even letters of credit.

The cost of forfaiting will depend on factors like the country of the importer, the nature of goods (usually capital goods), the importer's name and reputation, the

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value of the goods, the shipment date and the terms of repayment sought by the importer, the quality of the guarantee for the importer's obligation, the currency etc (Credit Suisse – First Boston, Forfaiting An Introduction, FINANZ AG ZURICH).

Pros and Cons of Forfaiting

The advantages of Forfaiting can be summarized in the following:

- Forfaiters finance the exporters without the right of recourse. Therefore the exporters transfer the business and the political risk to the Forfaiters. So, they can export to countries that could not be approached without forfaiting, due to increased risk.
- Additionally, it is the forfaiters than bear the risk of fluctuation of interest rates and the risk arising from the changes in the exchange rates.
- The exporters receive cash immediately after the delivery of their products and therefore their liquidity is improved, the bank borrowing is reduced and their own funds are freed for other activities.
- The exporters don't spend time and money for handling and collecting their claims, as they have been transferred to the forfaiter.
- The exporter is not obliged to assign the whole volume of his works to a single forfaiter as the negotiation for financing through forfaiting takes place separately for every specific transaction (spot).
- The exporter is entitled to demand secrecy over the financing and therefore the transaction can remain confidential.
- As Forfaiting, is a process without recourse, it helps the borrower to have a better looking balance sheet, because instead of having accounts receivable, the borrowing company will have cash.

The drawbacks of forfaiting can be summarized in the following:

Lack of legal framework for the protection of Forfaiter against the risks connected with international transactions.

- Due to the high risks involved in Forfaiting, the cost is very high for the exporters. (Interest rate in Greece around 6%, commission ranges from 4% to 5%, Source: Eurobank).
- Lack of secondary market for the instruments involved and consequently lack of liquidity.
- The exporter needs to find a guarantor acceptable by the forfeiter.
- It is limited to medium and long term transactions and usually to amounts exceeding 100.000,00 euros.

Reasons for Greece's underperforming

The presence of Forfeiting in Greece is too weak. This condition is connected mainly with two basic characteristics of the Greek economy. More specifically with the low performance in exporting and the limited potential of producing capital goods. (Kyrmizoglou)(Albaum G – Duerr E)

According to the World Bank the exports of Greek goods and services as a percentage of the G.D.P. are very low. In the following table we can compare the low performance of Greece with many other countries members of the European Union.

Table 1. Exports of goods & services in the countries of the European Union (% of GDP)

Country	Exports of goods & services (% of GDP 2013)
Austria	53.5
Belgium	82.8
Bulgaria	68.4
Croatia	42.9
Czech Republic	77.2
Denmark	54.3
Estonia	86.1
Finland	38.2
France	28.3
Germany	45.6
Greece	30.2
Hungary	88.8
Ireland	105.3
Italy	28.6
Luxemburg	203.3
Netherlands	82.9
Poland	46.1
Portugal	39.3
Romania	42.0
Slovak Republic	93.0
Slovenia	74.7
Spain	31.6
U.K.	29.8

Source: World Bank.

The World Bank ranks Greece in the 48th position in the Ease of Trading Across Borders. This position (regarding exports) could be much better if the average number of days needed for an export could be less. The exporter on aver-

age needs 15 days to complete an export, compared with an average of 10.5 days needed for the OECD countries. The difference is mainly due to the number of days needed to prepare the required documents (although the number of documents is the same with OECD, namely 4: Bill of lading, Commercial Invoice, Customs Export declaration and Packing List). (Doing Business 2015, World Bank)

It is important to notice that the value of consumer goods exports is (at least) 4 times higher than the value of capital goods exports. As Forfaiting focuses mainly on exports of capital goods (internationally) we realize that under these conditions there is not enough room for Forfaiting to grow in Greece (At least in the short-run).

Besides the composition of the national economic output (Services sector 80.6%, Industry 16% and Agriculture 3.4%), shows the weak position of the manufacturing sector. The fact that the vast majority of the Industrial Production in Greece consists of consumer goods, shows the low potential for Forfaiting in the near future.

Additionally the following reasons lead to difficulties in the spreading of Forfaiting in Greece:

- Forfaiting is a transaction needing specialized staff with long experience.
- Banks do not have an incentive to deal with Forfaiting, as it is a transaction that doesn't necessarily lead to a wider collaboration of exporters with the bank in other fields.
- Forfaiting is usually a form of financing with fixed interest rates and this lack of flexibility makes the Greek banks skeptic and reserved.
- There is a big obstacle for the development of Forfaiting in Greece and it is the existence of the Export Credit Insurance Organization (ECIO). This organization is non-profit seeking and it is supervised by the Ministry of Economy. It has a State Guarantee Capital amounting 1.47 billion euros. ECIO insures against commercial and political risks of non-payment, the export credits guaranteed by exporters to foreign buyers. So Forfaiting, has to face competition from a State Organization, to some extent with unequal terms.
- According to the answers received by bank officers (4 systemic banks) dealing with Forfaiting activities, the difficulties in the spread of Forfaiting are connected with problems inherent in Greece's International Transactions. More than 60% of those transactions are carried out with free shipping documents. This practice implies that exports are addressed to people (companies), they know each other. Exports like this based on the personal relation between the parties involved, do not leave much room for the development of Forfaiting. As the Greek economy is dominated by small firms, we can realize that Forfaiting can do very little for them.

Besides the interviewed officers stressed the imperative need for the banks making their customers more familiar with the concept of Forfaiting.

Perspectives of Forfaiting in Greece

The future of Forfaiting in Greece is connected with changes in Forfaiting itself. It seems that in the last few years, there is a tendency for Forfaiting to include consumer goods and services. It seems also that Forfaiting refers to even longer periods (more than ten years). (Christopoulos A. – Ntokas J.)

The current crisis creates conditions for further spread of Forfaiting as:

- The credit risk increases due to the lack of liquidity.
- Access to bank financing has become more difficult.
- The risk of countries has been increased.

Besides, reforms are expected to speed up, either due to the pressure of the European Commission, the European Central Bank and the International Monetary Fund or because it is widely acceptable in the country, that they are necessary. These reforms will create a more business friendly environment and of course the promotion of exports and less State intervention will be top priorities.

On the other hand, the Greek Banks need to undertake a more active role in informing their customers and making them more aware about the nature of Forfaiting.

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