BRITISH EXPORTERS ASSOCIATION

23rd April 2020

International Trade Committee Inquiry

https://committees.parliament.uk/work/242/the-covid19-pandemic-and-international-trade/

The Covid-19 Pandemic and International Trade

Overview of BExA

The British Exporters Association (BExA) is an independent national trade association representing the interests of the UK's exporters. Our membership is drawn from across the exporting community, including capital goods manufacturers and international traders (large corporates, MSBs, SMEs and Micro exporters), and their bank, credit insurance and other service providers. BExA seeks to promote the interests of its members and all UK exporters, with a particular focus on trade finance and export credit insurance.

Executive Summary

The current situation is unprecedented in impact and scale. Businesses are being impacted through no fault of their own and should receive the help they need to survive this crisis and to continue creating employment and generating wealth.

UK Government's response to the impact on businesses due to the crisis has been positive in message but has been lacking in delivery. Access to the support schemes needs to be simplified and accelerated if we want the UK to be ready to bounce back after the pandemic. Cover for the Coronavirus Business Interruption Loan Scheme (CBILS) needs to rise to 100% as a matter of urgency to ensure that the maximum number of viable SMEs can survive.

With supply chains under pressure, goods held up in transit, customers conserving cash and many capital decisions now on hold, we risk damaging UK businesses which have a reputation worldwide for innovation and flexibility. Unless the UK can move efficiently to provide support now, companies will not be prepared for the huge demands on their cash resources that they will need to be able to gear up again.

There will be opportunities and UK Government should ensure that the Export Strategy is ready to support businesses grow their export businesses once the pandemic eases. As well as working capital, companies will need market access support and readily available export finance support including from UK Export Finance (UKEF). All forms of support need to be streamlined and as easy to access as possible. Let's make these a sales tool for the UK and promote to the world how easy it is to do business with us.

BExA
www.bexa.co.uk

5th Floor, 83 Victoria Street, London SW1H 0HW
e-mail: michelle.treasure@bexa.co.uk
Tel: +44 (0)20 7222 5419

BExA Response to the International Trade Committee Inquiry's Questions

What impact will the global COVID-19 pandemic have on UK businesses trading internationally, in the short-, medium- and long-term?

For the vast majority of UK exporting business there will be a significant short-term impact. In a few key sectors this will result in an increased demand, however, for the majority of businesses the impact is severe and felt as follows:

Short term:

- Tailing off of demand, firstly in Asia, and now global.
- Inability to complete contracts that require personnel to be present overseas, for example for commissioning and training
- Closure of borders resulting in goods being stuck at borders to land-locked countries.
- Lack of certification
    - by buyers of completion and therefore release of milestone payments
    - closure of overseas Embassies resulting in lack of availability of Certificates of Origin needed to draw from Letters of Credit
- Loss of, or disruption to, labour force resulting in lower output – apart from manufacturing the obvious example is the agri-food industry.
    - Seasonal migrant workers now face quarantine in addition to the 'hostile' political environment caused by Brexit. It is not clear if furloughed and unemployed persons will be easily able to take up these positions or be trained for this type of labour. There is a need also to consider the long-term supply chain / food security / industry risk of using migrant labour.
- Loss of, or disruption to, supply chains, resulting in lower output and the need to source from elsewhere involving delay and higher cost.
- Demand for freight services outstrips supply and with the decline in air traffic and disruption of sea cargo trades, costs have increased substantially (anecdotal evidence that it has risen 6x in some instances in recent times).
- Goods are tied up in transit because of the unavailability of cargo space. This ties up cash flow and leads to delays in being able to deliver products to clients, cancellation of orders, demurrage, and consequences / damage to limited shelf life products.
- Loss of demand for products result in lower revenues for exporters, import substitution and protectionist measures on both health related and economic grounds.
- Customers are asking to extend payment terms on goods that have already been delivered as well as on future orders and this puts additional stress on exporters' cash flow. Where customers (importers) are unable to on-sell the products, they may default on their payment obligations.
- Where credit insurance cover is unavailable, invoices cannot be financed. Financial institutions are taking a more cautious approach to new transactions. As the cost of financing rises, this will affect exporters' margins, or if it is passed on, will stifle importers' abilities to buy.
- Short-term borrowing costs are increasing due to lack of market liquidity, particularly for US Dollar transactions.
- Bank balance sheets have expanded because of high demand for liquidity and potential significant bad debts. Whilst UK banks are generally capable of dealing with the 'stress', foreign banks and their National Treasuries are less likely to be able to do so or provide the necessary support. This will result in payment delays or defaults leading to bad debts and increased credit insurance claims.
- There is a high risk of significant UK company insolvencies during and immediately post lockdown as working capital shortage and lack of banking facilities will affect both ends of the supply chain. Access to short term working capital is a significant challenge now. Exporters and especially those who need to import components to then export a finished product require significantly more working capital than domestic traders and consequently are at greater hazard as they find accessing bank

funding challenging even in good times (their OTC/PTP timeline / cash conversion cycle is much longer and more complicated).

- This is exacerbated by some countries having closed their banking establishments for prolonged periods. This not only closes the flow of documents but of course shuts down payments in and out of the country concerned.

Medium to long term:

In addition to the above issues, many of which could stretch into the medium term, we believe:

- We may see established supply chains breaking down with manufacturers having to seek alternative suppliers which is time consuming and could impact costs and therefore revenues.
- There is already considerable discussion on re-shoring or near-shoring activities currently undertaken in Asia, particularly China, to reduce reliance and supply times for delivery and also to better manage quality control. That will be at a cost and will take time.
- The likelihood of more protectionist economic measures and nationalistic tendencies were already emerging pre Covid-19. The rhetoric from already affected countries is giving concern that the position is going to worsen.
- Slow pick up of demand – importers in Emerging Markets (EM) in particular are expected to experience a greater economic shock from Covid-19 and we expect that their governments will have fewer tools to provide financial support to companies compared to more developed markets.
- EM health sectors are very unlikely to cope if they are badly affected. This may result in long-term damage to their economies and the potential for social unrest, and have a chronic impact on already desperately poor countries with considerable debt burdens.
- A consistently low oil price together with less ability to transact FX will affect infrastructure projects and other investments in some markets and in relevant EM economies make repayment of foreign currency Sovereign loans more difficult.
- Banks with balance sheets damaged by Covid-19 will be reluctant to offer facilities to SMEs and growing companies, leading to increased insolvencies and bad debts. Borrowing cost are likely to be higher despite the low interest rate environment.
- We can hope for changes to the way that countries trade from a documentation perspective. It is clear that the use of original documentation is hampering trade at the current time. Governments, banks, insurers, freight companies and bodies such as the International Chamber of Commerce must be encouraged to come together to find electronic means of trading and customs clearance in the future.
- The positive element of the crisis will hopefully be an acceleration of the move towards digital solutions to speed trade flows and find harmonised rules based systems. If the blockages (vested interests) that have hampered digital developments in trade can be overcome this will lead to long-term benefits in acceptance of Blockchain and Internet of Things integration benefits.
- Export credit agencies (ECAs) will be required to play a more significant role for an extended period to accommodate market dislocation and lack of private market appetite. Other countries are likely to empower their ECAs, and we should do similar. The Government will need to accept a higher loss ratio as a cost of keeping jobs and business flowing.

How effectively has the Government responded, both in the UK and in overseas posts, to the short-term negative impact of the pandemic on UK businesses trading internationally? What further steps could be taken to mitigate this impact?

The high level Government response was quickly announced and provided initial comfort to business leaders that they could survive the crisis.

However the implementation of these schemes has been less successful:

- Large organisations with split credit ratings are waiting an unacceptably long time before receiving responses on the Bank of England Covid Commercial Finance Facility (CCFF) scheme, leading to delays and uncertainty in putting in place much needed additional liquidity facilities to withstand the current crisis.
- Smaller businesses are struggling to access the British Business Bank's (BBB) CBILS. The scheme requires a commercial bank to apply on behalf of the business and also to take 20% of the loan guarantee. This has meant that a large number of applications are being rejected before they get to the BBB as banks are evaluating applications based on the stricter lending criteria brought in after the 2008 financial crisis. Banks either need to be guided to relax these criteria or HMG needs to cover 100% of the loan. We have also received anecdotal evidence around banks misinterpreting BBB eligibility criteria and refusing applications from UK exporters whose income is predominantly from overseas clients, claiming that it does not meet the 'Be UK-based in their business activity' criteria. In addition, we are still hearing reports of Directors being asked to put up personal collateral in order for banks to forward applications. The current situation will see SMEs suffer and fail if the scheme continues as it is.
- The relaxing of UKEF's ability to support short-term transactions in wealthy nations is welcome however we are concerned that the demand may overwhelm UKEF's current resources. The UK benefits from a world-class credit insurance private market, UKEF support could be utilised to provide guarantees to these institutions to provide cover and therefore make use of their capacity and expertise. This issue has been raised with Government by the Association of British Insurers and is one that BExA fully endorses.

Improvements that could be implemented:

- There are success stories of schemes that have been working well, HMRC's "PAYE payment deferral plan" seems to be simple to access and, as HMRC take 100% of the risk, is available to companies who have a good track record with HMRC on a "commercially-viable" basis. This could form the basis of accessibility to the CBIL scheme.
- Less loans and more grants – many smaller exporters will not be able to afford to borrow funds when their trading is so severely impacted. Grants could be clawed back from future years' profits say over 3 to 5 years.
- UKEF to facilitate guaranteed bank loans for larger corporates, thus ensuring that they can continue to fund themselves in stressed banking markets.

What medium- and long-term negative impacts could arise from the pandemic for UK businesses trading internationally? What steps could the Government take to mitigate these impacts?

The Export Strategy is the key piece of legislation that will mitigate the medium and long-term impacts of the pandemic. The UK needs to look outside its borders and grow business through export. We should have a renewed focus on breaking down the barriers to export and HMG needs to increase its efforts on implementing the aims of the Export Strategy.

Businesses require financial assistance, more so than ever before, to get back up and running as well as to investigate and break into new market destinations. This support needs to be made available to both new and existing exporting businesses who are trying to access markets that are new to them. An enhanced scheme based on the defunct "Passport to Export" with additional budget and flexibility would seem to fit the bill.

The Government's ongoing commitment to free trade should not be diminished; tariff free access to the EU and current preference markets will drive export growth and has the potential to drive inward investment in the UK too.

In relation to steps that could be taken we believe:

- UKEF could take a more active role in insuring / covering the debtor books of UK exporters in cases where payment delays are being experienced to ensure continuity of cash flow.
- UKEF to improve product offering such as revolving lines of credit for smaller business and re-introduction of the Letter of Credit guarantee scheme.
- Improve information available / better promotion of what support is available for exporters – many are not aware of some of the schemes designed to assist them.
- Better co-ordination between UKEF, Chambers of Commerce is vital to ensure that exporters have access to as much support as possible.
- Remove tariffs if trading on WTO terms.
- Be realistic in terms of what can be achieved regarding Brexit given the time lost focusing on the pandemic – a delay would be sensible.

What steps can UK businesses take to mitigate the negative impacts of the pandemic on international trade?

UK businesses have already had to take steps to mitigate the effects of the pandemic. Those that are able have already:

- Put in place scenario planning, detailing estimations of how long the effects of the pandemic may be felt and the impact on revenues and cashflow.
- Reviewed if there is sufficient liquidity to survive in the worst case scenarios.
- Investigated additional liquidity. Some strong companies are still able to do this commercially but pricing is uncertain and banking appetite is changing daily. The most common solution is to look to Government supported schemes to cover the additional liquidity required. This can only work if the Government schemes are accessible and reactive.
- Reviewed ongoing costs to see where savings can be made. If only a portion of the workforce is needed then businesses have been utilising the Job Retention Scheme and furloughing workers to ensure that they are not overly financially disadvantaged. Some businesses have been looking to implement furloughing on a rota basis to ensure that employees are impacted fairly across the workforce.
- Identified supply chain issues and where possible planning alternatives.
- Put in place continual monitoring of the above as the pandemic continues.

The current situation has been and continues to be incredibly tough for a large number of businesses - this is one crisis where Government intervention is not only justified but essential.

How best can the UK Government facilitate trade in essential goods during the pandemic?

The UK Government should already have identified those UK businesses involved with the trade of essential goods and services during the pandemic. It is likely that these companies will have experienced a spike in demand like never before. Therefore it is important to understand the supply chains that these companies rely on and identify any potential bottlenecks to supply. If that is through financial hardship then a fast track route through the Government support schemes should be implemented. If it is due to difficulties in transport then Government should look to subsidising freight costs, i.e. to use air freight rather than sea, to ensure supply chains run as optimally as possible.

How should the Department for International Trade work with the rest of central government, as well as devolved, local and regional government, to deliver a coordinated response to the pandemic?

Similar to the Export Strategy, where all of Government needs to work together to promote UK exports, this pandemic requires all of Government to work together to ensure this country has the ability to bounce back afterwards.

DIT's role during the pandemic should be to:

- Ensure the continuation of trade in essential goods and services;
- Ensure exporting businesses survive the pandemic; and
- Provide the framework (Export Strategy) for UK businesses to grow exports quickly post the pandemic

How can the UK Government engage with countries at the World Trade Organization and bilateral trading partners – including those with which the UK has a significant trading relationship or one facilitating trade in priority goods – to promote international cooperation and a coordinated global response to the pandemic?

Clearly this is a global problem and it will be extremely important for Governments globally to co-ordinate to ease the economic and social impacts of the pandemic. It requires global co-operation to ensure sufficient supply of essential goods. This could include relaxing of tariffs on a wide range of goods when trading under WTO or bilateral trade agreement terms and easing of customs clearance procedures.

The use and acceptance of electronic copies of documents where the originals cannot be furnished for bank / customs purposes should be facilitated by local regulatory authorities / Central Banks wherever possible and practical.

The SME markets in particular require an injection of funding to support free flow of goods and services. Apart from direct funding, this may be by way of supporting banks to issue import Letters of Credit for re-supply and assist with security of payment for exports, thereby alleviating congestion in the credit insurance markets where cover may have been much diminished or withdrawn. As the local banking sectors issuing these instruments may be weaker, ECA/MLA support for these banks and instruments will likely be required.

There have been initiatives to delay debt repayments for poor nations: these should be extended beyond only the poorest 27 with a pragmatic approach being taken to debt and interest repayments on sovereign debts across the board and should include commercial transactions supported by ECAs. Payment extensions and interest repayment holidays should be investigated and implemented.

How might the pandemic impact global trade patterns and international supply chains in the long-term?

It is likely that in the long-term global trade patterns will revert to pre-pandemic norms. However the pandemic also offers opportunities to effect change and it would be remiss of the UK to pass this up when the global economy starts to recover.

The UK needs to have the Export Strategy ready and willing to support UK businesses in growing their exports, from marketing support to export financing support. We are also blessed in the UK with an excellent financial services sector, and we need to encourage this large resource to mobilise in support of UK exporters – this may require Government guarantees through the likes of UKEF or it could be through streamlined legislation to support exports. The choice is UK Government's to make but the goal is clear – use the Export Strategy to make exporting a success.