German Economic Team

UKRAINE

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Export finance conditions in Ukraine: Results from an enterprise survey

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About the German Economic Team

Financed by the Federal Ministry for Economic Affairs and Energy, the German Economic Team (GET) advises the governments of Moldova, Georgia, Ukraine, Belarus and Uzbekistan on economic policy matters. Furthermore, GET covers specific topics in other countries, such as Armenia. Berlin Economics has been commissioned with the implementation of the consultancy.

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About the AHK

The German-Ukrainian Chamber of Industry and Commerce was officially opened in Kyiv in October 2016. The chamber coordinates economic operations of its members, present their interests and provide services to them, support companies and organizations that are not chamber members. The chamber is integrated into a worldwide network of German Chambers of Commerce abroad, which consists of 140 offices in 94 countries. The network's umbrella organization is the Association of German Chambers of Commerce and Industry (DIHK)

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Executive summary

The export finance environment is of key importance for improving trade opportunities for companies in Ukraine. In this policy paper, we assess the current state of affairs based on a survey that we conducted among Ukrainian enterprises. A survey focusing on export finance and export credit insurance has, to the best of our knowledge, not been conducted in Ukraine for several years. The questionnaire has been sent out by the German-Ukrainian Chamber of Industry and Commerce and the Ukrainian Chamber of Commerce and Industry to their members.

The responding companies gave us a picture about the conditions and the major obstacles of the export finance environment of Ukraine which can be summarised as following:

- The major obstacles for export transactions are lack of export finance, payment risks of potential buyers and lack of export experience.
- Exporters' experience with bank export finance products is still extremely limited.
- Ukrainian exporters are frequently confronted with the request for the provision of contract bonds as additional security. This demonstrates a lack of confidence on the side of foreign buyers and is an additional burden for the exporters.
- Securities from the foreign buyer for exports from Ukraine are difficult to obtain for exporters. Most exporters use retention of title, if any security at all.
- The possibility to insure exports against non-payment risks is available only to a limited extent and the majority of exporters is unfamiliar with this instrument.

Our results indicate that the institutional framework of the export finance environment needs to be significantly improved. In particular, a further strengthening of the export finance know-how as well as fostering and extending export credit insurance are policy implications that can be drawn from this survey.

Though the responses to our questionnaire cannot be regarded as statistically representative, they are clear enough to draw some meaningful conclusions on the subject of the questionnaire.

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1 Introduction

Trade and export finance are of key importance for strengthening a country's exports and improving the integration of its export operators into global markets and value chains. In a modern and comprehensive export strategy, export finance products thus play a significant role for achieving and maintaining the exporters' international competitiveness. The other major elements of a comprehensive export strategy are provision of information needed for the access to foreign markets and protection against commercial and political non-payment risks.

Figure 1: Objective and elements of a comprehensive export strategy

Source: own illustration

In economic research it is undisputed that the dynamic growth of world trade during the last decades has been decisively influenced by the rapidly growing availability of trade finance. For most exporters it is difficult if not impossible to act as financier for their foreign buyers for the period between receipt of an export order and the payment for goods or services delivered. The exporter today has to provide an attractive and competitive offer including short term or medium-/long-term credit and, if required, bank guarantees. Depending on the size of the order and the credit terms requested by the foreign buyer the funding by a bank can become very expensive or unavailable at all. The combination of export finance offered by banks and credit insurance by public Export Credit Agencies (ECA) or private credit insurance companies, however, can make export transactions possible which otherwise could just not be executed.

The German Economic Team (GET) has critically followed and advised on Ukraine's efforts to establish a state-of-the-art export financing system. Especially but not exclusively the setting-up of an ECA has been topic of several reports[1]. Until today the Ukrainian system of export financing and risk protection does not convey a coherent and convincing picture. Structural weaknesses and inefficiencies bear a high risk that export opportunities cannot be used to the full extent.

This has motivated GET to put more analytical efforts into the assessment of Ukraine's exporters' activities, their access to export finance products and the experience with credit insurance provided

[1] Janus and Kirchner (2017a, b, c, 2018) and Janus and Poluschkin (2020)

by ECAs or private insurers[2]. An online questionnaire has been developed which has been distributed with the support of the Ukrainian Chamber of Commerce and Industry and the German-Ukrainian Chamber of Industry and Commerce to companies being active in Ukraine. To the best of our knowledge, a questionnaire on the conditions and obstacles in the Ukrainian export finance environment has not been sent out for several years. The next chapter describes the methodological approach of the questionnaire. As a following step, the results of the questionnaire are summarised. Finally, this policy paper concludes and provides some policy implications

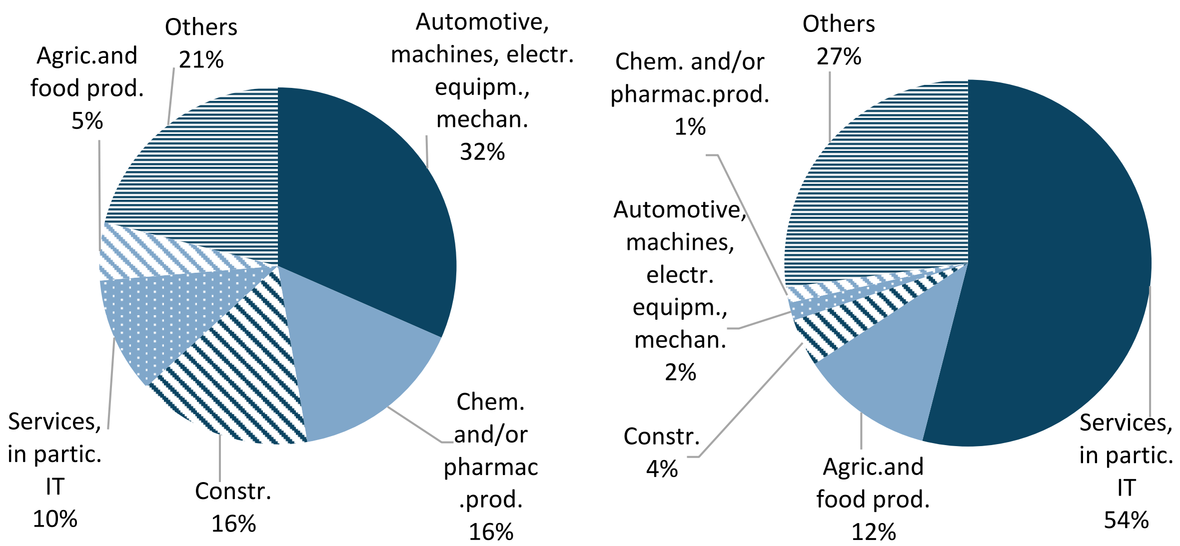
2 Methodological approach: Firm survey

This paper considers the responses to a questionnaire, prepared by the German Economic Team and sent by the German-Ukrainian Chamber of Industry and Commerce and the Ukrainian Chamber of Commerce and Industry to their members. The main goal of this questionnaire is to reach out to export-oriented companies operating in Ukraine and understand their conditions and obstacles in the export finance environment in Ukraine. The questionnaire is split into two parts. In the first one, we ask the companies about their characteristics, such as sectors, annual turnover and number of employees. In this way, we aim at understanding the characteristics of companies reporting any kind of export financing obstacles. The second part embodies explicit questions on the conditions, instruments applied and the obstacles of export financing. In this part, the questions include multiple choices having the option “others” to indicate any kind of particularities. It is worth mentioning that also non-exporting companies are included in our sample. On the one hand, it mixes the recommendations drawn from this questionnaire with regard to export activities. On the other hand, non-exporting responding companies reveal a picture on the obstacles of finance withholding them from exporting. Thus, their responses can be seen as complements to the research question and extend the range of recommendations to connected aspects of export promotion in Ukraine. As this questionnaire is based upon a close cooperation with these two chambers, the respondents are over-proportionally companies related to German businesses. Therefore, the questionnaire cannot be regarded as statistically representative. Our sample overrepresents several sectors including automotive, machines, electronic equipment and mechanisms sector and it underrepresents the service sector.

[2] The availability of information for market access in foreign countries has not been in the primary focus of the survey. The Ukrainian Export Promotion Office (EPO) is an advisory and consultative body to the Ministry of Economic Development and Trade of Ukraine (MEDT) providing such kind of market access information.

Figure 2: Sectoral comparison of our sample vs. the total economy

a. Sectors of our sample **b. Sectors as share of GVA of the total economy**

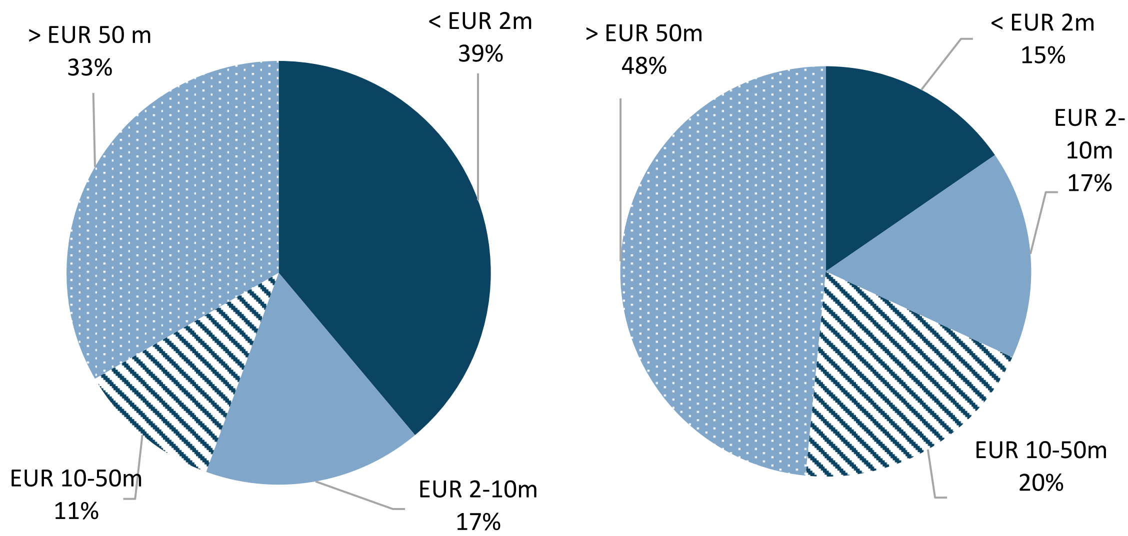


Source: Own questionnaire and Ukrstat, 2019

Furthermore, our sample differs in the representation of the magnitude of companies. Our sample overrepresents companies having an annual turnover of less than EUR 2 m in 2019, while it underrepresents large companies.

Figure 3: Turnover comparison of our sample and the total economy

a. Companies' turnover of our sample **b. Companies' turnover in the total economy**



Source: Own questionnaire and Ukrstat, 2019

3 Results of the data analysis

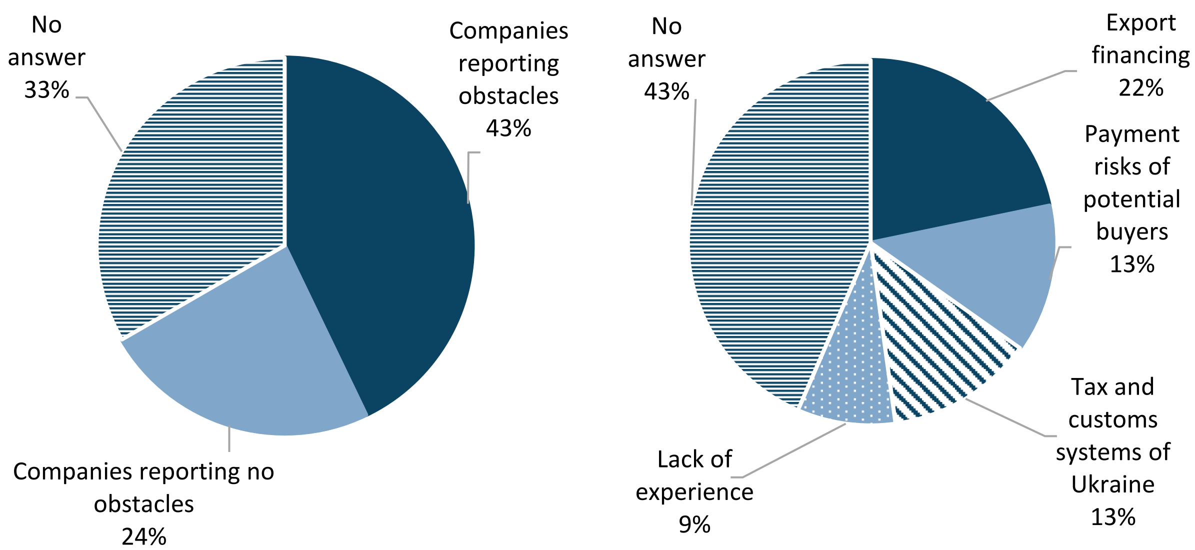
Having discussed the methodological approach and described the characteristics of the sample, this chapter analyses the responses of participating companies on the second part of the questionnaire, which includes the conditions, instruments and obstacles of export finance in Ukraine.

3.1 Obstacles for export business

We asked companies about the obstacles in export transactions they have faced during the last 12 months. 43% of responding companies confirm obstacles in export transactions. More than a third of those mentioning obstacles report about export financing and payment risks of potential buyers as major problems. 13% mention problems with tax and customs institutions as an important obstacle with regard to their export transactions. Another 9% sees a lack of experience of banks to handle foreign currency transactions. Interestingly, one company responds “all obstacles”, though this option is not explicitly provided in the questionnaire. The reasons for difficulties in the execution of export deals can be grouped into three categories: lack of export experience, payment risks of potential buyers and lack of export finance. These answers show that a low level of information, be it information about market access or information on a potential foreign buyer’s creditworthiness, may be regarded as the real problem behind lack of experience and too high payment risks of potential buyers. At the same time the very limited knowledge on export risk management, for example through export credit insurance, is obvious. The problems with the tax and customs system can have various reasons, for example, corruption etc.

Figure 4: Companies facing obstacles in export transactions

a. Companies reporting existence of obstacles **b. Main obstacles reported**



Source: Own questionnaire; note: no answers may refer to non-exporting companies

Conclusion 1: 43% report obstacles. But when asking about specific obstacles, export financing, payment risks of potential buyers, tax and customs systems of Ukraine and lack of experience are the main obstacles mentioned.

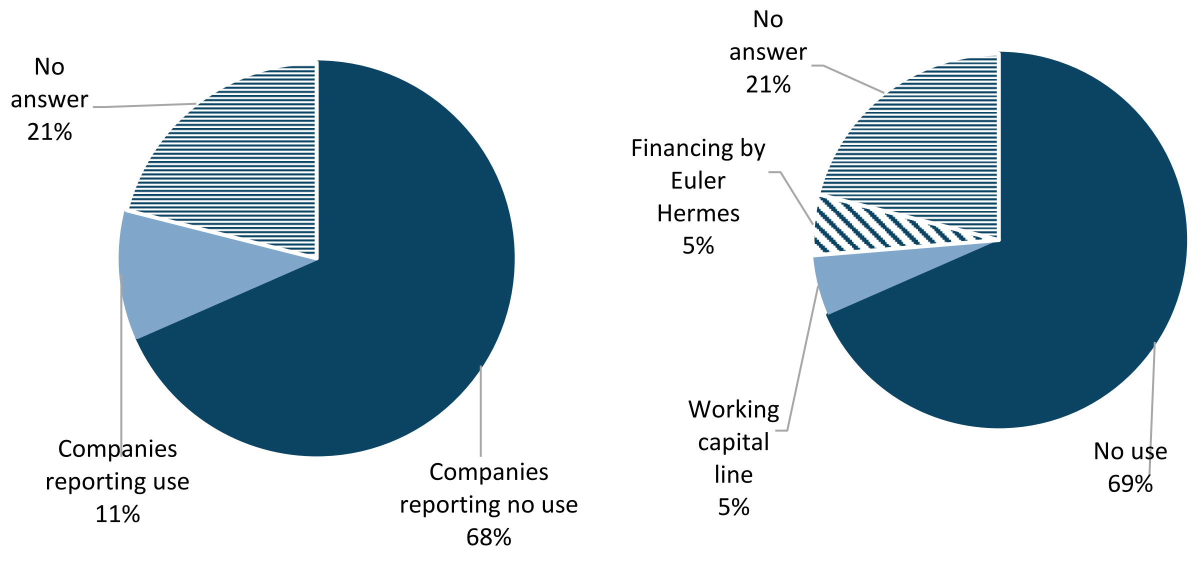
3.2 Use of export financing instruments by banks and major obstacles

The role banks play in the area of export finance seems to be very low. Only 11% of the companies confirm to have used bank export financing instruments yet. The only mentioned bank export financing instrument that has been used is a “working capital line”, i.e. a classical product of pre-export finance. All other regular instruments of post-shipment bank export finance have not been selected one single time.

Asked, whether there are obstacles with bank financing instruments already faced by the exporters, the respondents report both the mere availability of export finance instruments and the conditions of such financing. The fact that high transaction costs are not indicated by the respondents should not be misinterpreted in the sense that costs would not be a problem. The opposite is the case. Since 22% respondents see the financing conditions as major obstacle, it may be assumed that these two answer options have been regarded as synonymous. 24% of companies report “no obstacles” (Figure 4). However, this does not confirm the availability of export finance instruments. Only 11% of companies report the use of export financing instruments, namely Euler Hermes financing and working capital line (Figure 5).

Figure 5: Bank export financing instruments

a. Companies reporting use of instruments **b. Export financing instruments reported**

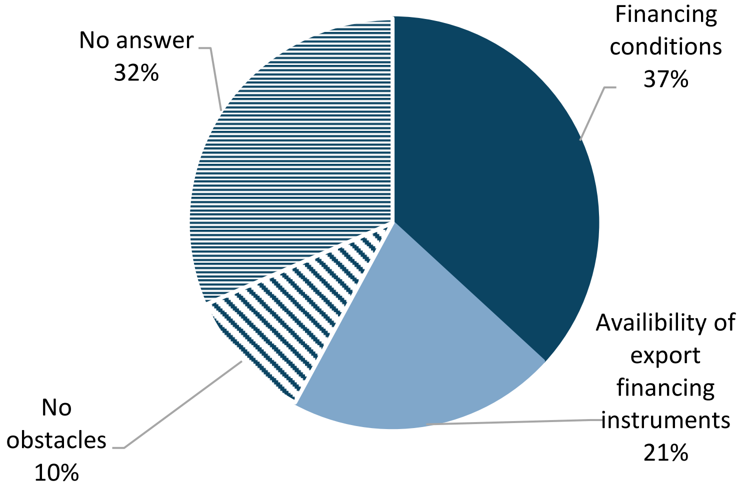


Source: Own questionnaire; note: no answers may refer to non-exporting companies

Most likely the mentioning of Euler Hermes financing refers to bank financed imports to Ukraine with credit insurance provided by Euler Hermes; This assumption would further reduce the importance of banks' export financing products, especially working capital lines. More than two-thirds declare no use of export financing instruments. This result reveals a strong disadvantage in achieving the exporters’ international competitiveness and restricts the Ukraine’s export development.

Asking about obstacles in the provision of bank export financing instruments, the majority of companies, almost 60%, mention financing conditions or the availability of export financing instruments as important issues. Whereas no obstacles in the provision of bank export financing instruments are reported by only 10%.

c. Obstacles in the use of bank export financing instruments



Source: Own questionnaire; note: no answers may refer to non-exporting companies

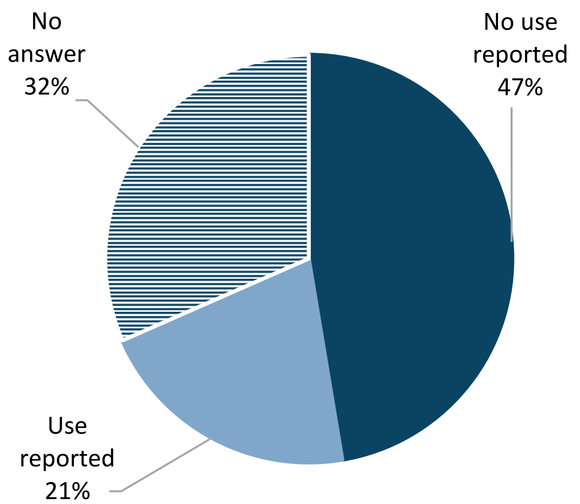
Conclusion 2: 69% of companies report no use of bank exporting financing instruments. A few companies indicate the use of financing by working capital lines.

3.3 Financing of export production (pre-export / pre-shipment financing)

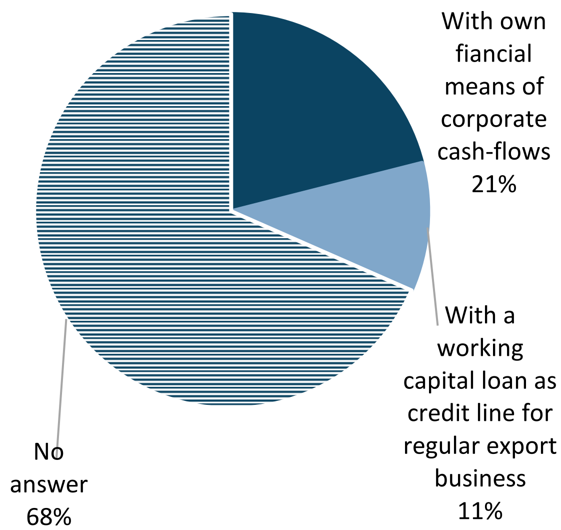
Frequently export transactions cannot be realised because of a lack of finance for the production phase.

Figure 6: Financing in the pre-export phase

a. Use of financing in the pre-export phase



b. Instruments in the pre-export phase



Source: Own questionnaire; note: no answers may refer to non-exporting companies

In general, external financing of export production supports enterprises to have a sufficient level of liquidity for production. Even if corporate cash-flow is used as means of financing, in many cases this is not sufficient for the development of an export production in a larger dimension. Only a tenth of respondents report about a working capital line of a bank for the purpose of financing the regular export business. Other respondents report to have used corporate cash-flow for financing the pre-export phase. In total, almost half of the reporting companies mention that financing of export production in a pre-export or pre-shipment phase is not used at all.

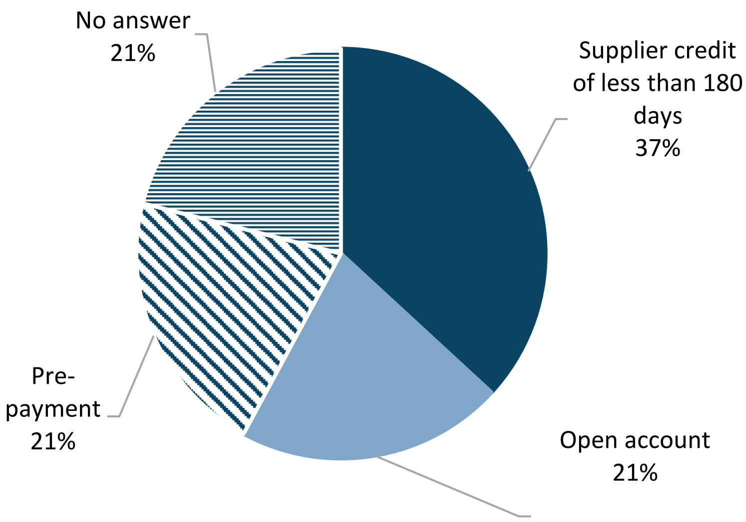
Conclusion 3: 47% indicate no use of pre-export financing instruments and a third of respondents mention the usage of means of corporate cash-flows and working capital credit lines for regular export business.

3.4 Payment terms in export finance and contract guarantees

Usually, the payment terms in international export finance are categorised as short-term (up to 360 days), medium-term (up to five years) and long-term (more than five years). The payment term (tenor) must be appropriate to the kind of exported goods and the financial size of the transaction. The availability of medium-term or long-term export finance is an indication of the level of maturity of the export finance market of a country.

The respondents' answers correspond to the unavailability of bank export finance. Those exporters who cannot negotiate delivery on pre-payment terms, offer maximum 180 days of credit. Their balance sheets most probably are not strong enough to absorb longer durations of credit. Especially for products which would theoretically allow longer repayment terms, this is a clear disadvantage in comparison with competitors from other countries which can offer longer terms as supplier credits or buyers credits offered by banks. The answers to the questionnaire show that several respondents have to provide contractual guarantees in order to secure the fulfilment of their contractual obligations.

Figure 7: Payment terms in export finance



Source: Own questionnaire; note: no answers may refer to non-exporting companies

This is quite unusual since contract bonds are most frequently used for transactions with longer periods of production and assembly, i.e. typically medium and long term transactions.

None of the companies report the use of supplier credit for more than 180 days.

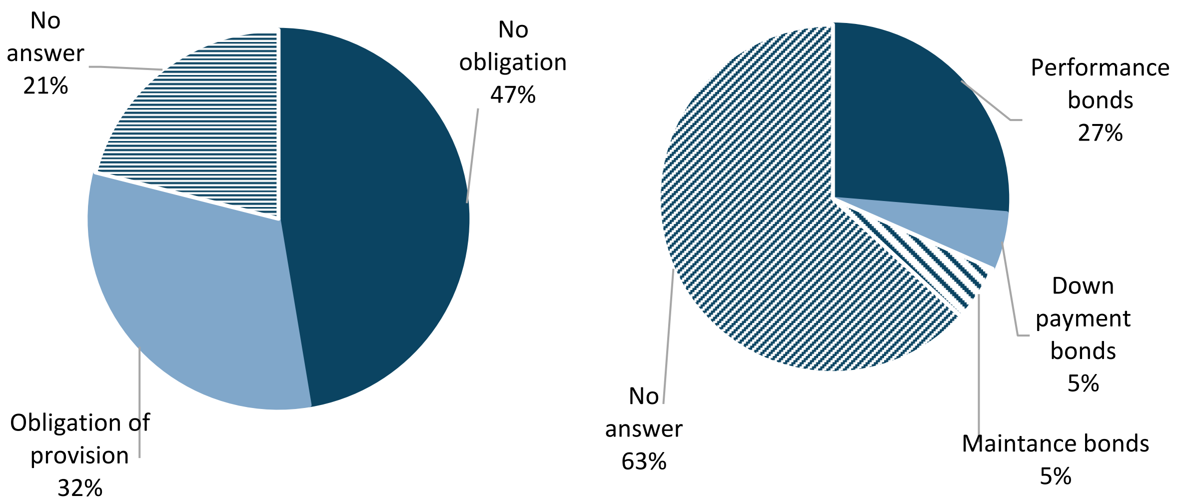
Conclusion 4: Supplier credit of no more than 180 days, open account and pre-payment are the payment terms most frequently mentioned.

3.5 Guarantees in favour of foreign customers

We also ask companies whether they have to provide guarantees (bonds) in favour of their foreign customers guaranteeing their contractual performance and the form of bonds required.

Figure 8: Provision of guarantees in favour of foreign customers

a. Obligation to provide guarantees **b. Form of guarantees (bonds)**



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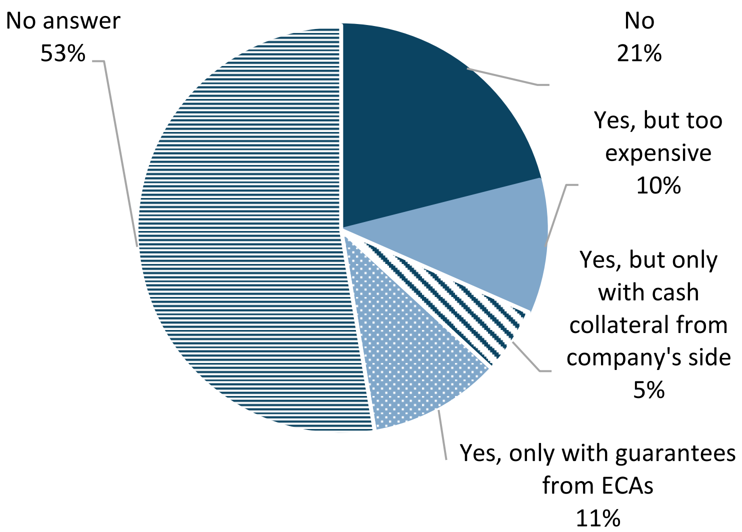
Source: Own questionnaire; note: no answers may refer to non-exporting companies

The fact that Ukrainian exporters have to deliver performance bonds for transaction on short-term, as stipulated by 27% of the respondents, may also reflect a lack of confidence of the foreign buyer in the performance ability and discipline of the Ukrainian supplier.

An open question, for which the questionnaire does not offer an answer is, who acts as the guarantor. In this regard, we ask companies whether their bank offers such guarantees (bonds) for support of their business. 21% state that banks do not provide such guarantees and 15% more characterise the guarantees issued by banks as “too expensive” or available only “with cash collateral” (Figure 9). This leads to the assumption that guarantors most probably are the suppliers’ owners or parent companies.

Figure 9: Provision of guarantees in favour of foreign customers



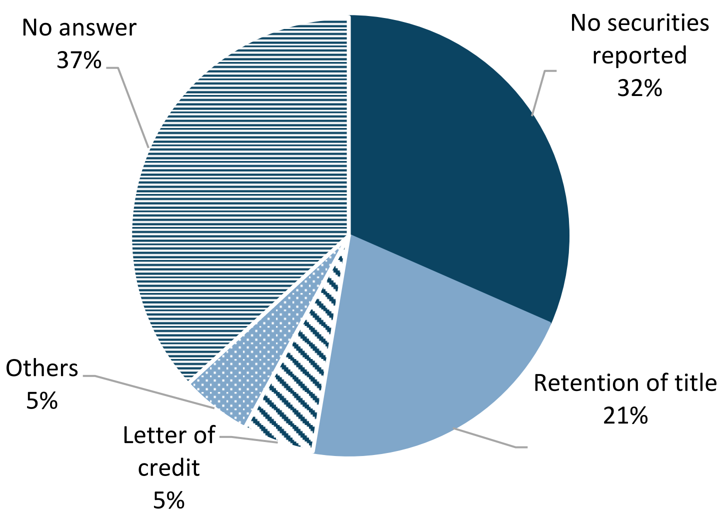
Source: Own questionnaire; note: no answers may refer to non-exporting companies

Conclusion 5: 32% of respondents state that there is an obligation to provide guarantees in favour of foreign customers. The guarantee forms most mentioned are performance bonds, down payment bonds and maintenance bonds. Also, it is mentioned that provision of guarantees is conducted with cash collateral from company's side or other kind of guarantees.

3.6 Securities for Ukrainian exporters

Payment risks of potential foreign buyers is mentioned by a few respondents as an obstacle for export business.

Figure 10: Securities for exporters



Source: Own questionnaire; note: no answers may refer to non-exporting companies

There are two major reasons for a cautious attitude vis-à-vis new foreign customers. The lack of information on the potential customer makes the transaction more risky than other transactions and the financial position of the potential buyer may prove to be so weak that the debtor cannot pay the amounts due as contractually agreed upon. Contractual securities can lift this insecurity from the supplier. Almost a third of companies do not report any kind of securities, while further 31% report securities, such as retention of title, letter of credit or other kind of securities.

The answers given by the respondents are in line with international practice in foreign trade. Suppliers of raw materials, unfinished goods, consumer goods, spare parts etc., which are traditionally traded at short term, most frequently do not have a bargaining power sufficiently strong to request for hard guarantees in the form of bank guarantees or letters of credit. The method to secure the claims therefore is the retention of title.[3] In many cases no securities are available at all.

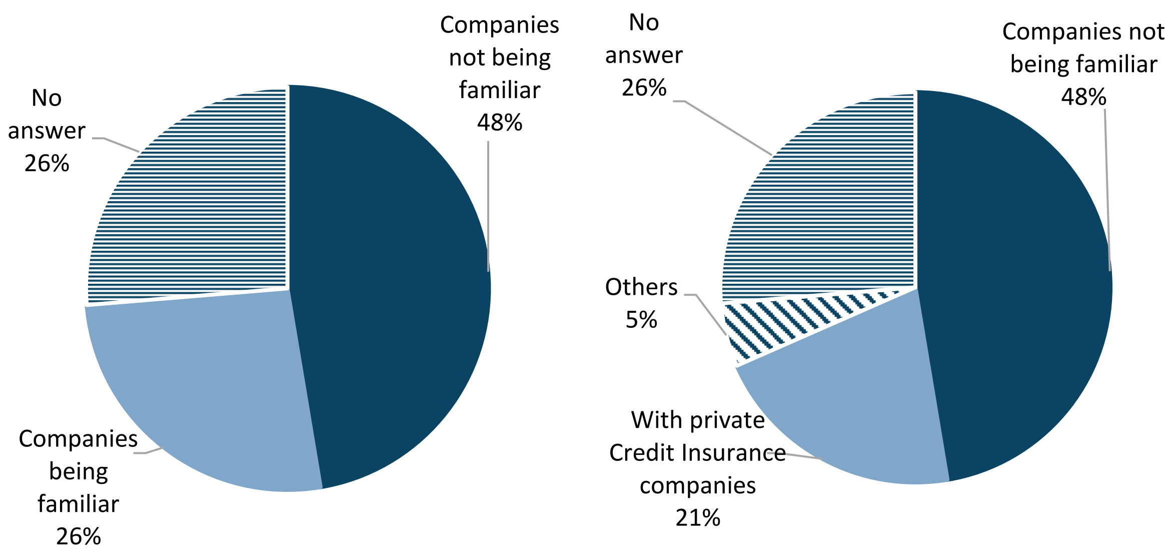
Conclusion 6: Almost one third mention that deliveries are made without securities. Others report about retention of title and letters of credit.

3.7 Credit insurance

If the supplier does not obtain securities from the buyer, he can conclude an export credit insurance contract covering the non-payment of the foreign buyer due to commercial reasons, e.g. insolvency and under certain conditions political risks as well.

Figure 11: Use of credit insurance

a. Familiar with/use of credit insurance **b. Form of use of credit insurance**



Source: Own questionnaire; note: no answers may refer to non-exporting companies

[3] Under the condition that the legislation of the buyer country knows and supports this kind of credit security.

The official Ukrainian Export Credit Agency (EKA) is currently being built up and not yet fully operative.[4] Private credit insurance companies like Euler Hermes, Coface and Atradius are in principle active in Ukraine, but with significant limitations. We ask the participating companies whether they are familiar with or whether they use export credit insurance and if so, how they use them. Almost half of the respondents are not familiar with export credit insurance, 26% respondents confirm their knowledge about credit insurance.

80% of the companies reported being familiar with credit insurance use private credit insurance provided by Euler Hermes, Coface or Atradius.

Conclusion 7: Almost half of the respondents report that they are not familiar with the use of credit insurance. If familiar, private credit insurance companies are mentioned as a form of use.

4 Summary and policy implications

Our survey on export finance experiences clearly demonstrates the shortcomings of export support in Ukraine. Usually there are three pillars of export support: information, financing and risk protection. Only with an institutional set-up addressing all three elements of export support Ukraine will be able to improve its position on world export markets. The results of the survey underline that the biggest deficiencies exist in the areas of export finance and risk protection. Since these two instruments are closely connected and reinforce each other, there is currently no functioning export financing system in Ukraine.

A lack of information, mainly insufficient information on potential foreign buyers and their creditworthiness, is mentioned as an obstacle of export activities. It may be assumed that especially smaller companies are facing such difficulties. Through the network of chambers of industry some relevant information can be achieved, but comprehensive and differentiated information on foreign markets, potential buyers and market access requirements seem to be not easy to obtain. The Export Promotion Office (EPO) has been established in 2016 as a specialised export information and promotion agency serving as an important tool for addressing exporters' needs. An institutionalised cooperation between EPO, practitioners of export finance and EKA is recommended.

According to the results of the survey most exporters use open account or short-term supplier credit up to 180 days as repayment terms in their export contracts. The most frequently agreed security, if any, is retention of title. Export finance instruments of banks play no role for the exporters, at least not for the respondents of this survey. If at all, working capital credit lines are made available by banks to finance the pre-export phase. Other traditional export financing instruments like export factoring, forfaiting, buyers' credits, structured or project finance seem to be rare exceptions. The unavailability of export finance products is a clear competitive disadvantage of Ukrainian exporters.

The export credit insurance in Ukraine is underdeveloped yet. The Export Credit Agency is still under construction and due to its insufficient capital basis hardly able to play a significant role in export

[4] See Janus, Theorie und Praxis staatlicher Exportförderung - Keine Glanzleistung ukrainischer Gesetzgebung [Теорія і практика державного стимулювання експорту - не блискучий досягнення українського законодавства] in: Wissenschaftlich-Praktischer Sammelband zum 10-jährigen Jubiläum der DUJV [Науково-практичний збірник до 10-ти річча НУОЮ], p. 36-47.

support.[5] A well-functioning export credit insurance system would be, however, the trigger for more affordable export financing by banks. Only few respondents have any knowledge about credit insurance and, if they do have, it cannot be excluded that this experience is linked to equipment imports and not to exports.

The questionnaire highlights the shortcomings of Ukraine's export performance. But it also demonstrates clearly where the areas for further improvements are. Strengthening the institutional framework for financing of export transactions by banks and, finally, the development of the Export Credit Agency into a real export promotion institution should be objectives of primary importance.

[5] On 04.02.2021 a draft law amending Ukraine's "Law on providing for large-scale export expansion of goods (works, services) originating in Ukraine through insurance, guarantees and cheapening of export credits" has had the first reading in Verkhovna Rada.

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Annex: Questionnaire

19 Ukrainian companies have responded to the following questionnaire on conditions and obstacles in the export finance environment:

General questions about your company

Economic Sector

1. To which economic sector does your company belong to?

   a. Agriculture and food production
   b. Base metals
   c. Mineral products
   d. Automotive, machines, electr. equipment and mechanisms
   e. Chemical (and/or) pharmaceutical products
   f. Services, in particular IT-services
   g. Others:

People employed

2. How many people are currently employed at your company?

   a. 1-99
   b. 100-249
   c. 250-499
   d. 500-999
   e. >1000

Company's turnover

3. How much was your company's turnover in 2019?

   a. <UAH 58 million (<EUR 2m)
   b. UAH 58 million-290 million (EUR 2m-10m)
   c. UAH 290 million-1.45 billion (EUR 10m-50m)
   d. UAH 1.45 billion-2.9 billion (EUR 50m-100m)
   e. >UAH 2.9 billion (>EUR 100m)

Company's exports

4. Does your company export?

   a. Yes
   b. No

5. If yes, to which country regions do you mainly export?

a. EU-countries
b. China, India and other Asian countries
c. CIS-countries and Georgia
d. Non-EU-countries in Europe incl. UK, Turkey and Israel
e. Others:

6. If yes, how large is the export share in your turnover?

a. 1-20%
b. 21-40%
c. 41-60%
d. 61-80%
e. >80%

7. Do you export to any entity (e.g. parental company, sister company) within your company group?

a. Yes
b. No

8. How large is the share of exports to entities (e.g. parental company, subsidiary company) within your company group (holding)?

a. 1-20%
b. 21-40%
c. 41-60%
d. 61-80%
e. >80%

Questions regarding export finance

Obstacles in exporting

9. Have there been obstacles in exporting during the last 12 months?

a. Yes
b. No

10. If yes, what have the main obstacles been?

a. Lack of export experience
b. Export financing
c. Payment risks of potential buyers
d. Tax and customs system of Ukraine
e. Others:

Instruments in export financing

11. Has your company used bank export financing instruments during the last 12 months?

a. Yes
b. No

12. If yes, in which form?

a. Current account credit
b. Working capital credit line
c. Receivables purchase agreement with your bank
d. Export factoring agreement with a factoring institution
e. Bank loan of your bank to your foreign customer or her bank (“buyers credit”) with disbursement of the loan to you (only medium/long term transactions)
f. No-recourse export forfaiting (only medium/long term transactions)
g. Others:

Obstacles in financing

13. Were there or are there any obstacles your company faced or is facing in financing?

a. Yes, in the availability of export financing instruments
b. Yes, in high transaction costs
c. Yes, in financing conditions (e.g. interest rates, repayment schedule etc.)
d. No obstacles
e. Others:

Financing in the pre-export phase

14. Has your company used financing in the pre-export phase during the last 12 months?

a. Yes
b. No

15. If yes, how has your company financed your activities in the pre-export phase?

a. With own financial means of corporate cash-flow
b. With a credit (working capital) from your foreign customer
c. With a working capital loan of your bank for an individual prospective export transaction
d. With a working capital loan of your bank as credit line for your regular export business
e. Others:

Payment terms

16. Which payment terms do you usually agree with your foreign customers?

a. Pre-payment
b. Open account
c. Supplier credit of less than 180 days
d. Supplier credit of more 180 and up to 720 days
e. Supplier credit of more than 720 days and up to 5 years
f. Supplier credit of more than 5 years
g. Offering of guarantees

17. Do you have to provide guarantees (bonds) in favour of your foreign customer guaranteeing your contractual performance?

a. Yes
b. No

18. If yes, in which form?

a. Bid bond
b. Down payment bond
c. Performance bond
d. Maintenance bond
e. Other forms:

19. If yes, is your bank offering such guarantees (bonds) for support of your business?

a. No
b. Yes, but too expensive
c. Yes, but only with cash collateral from your side
d. Yes, no problems
e. Other guarantees:
f. Other issues:

Securities for export transactions

20. Which kind of securities do you get for your export transactions?

a. No securities
b. Retention of title
c. Bills of exchange or Promissory Notes
d. Letters of credit (L/C)
e. Bank guarantee
f. Others

Export credit insurance

21. Are you familiar with/do you use export credit insurance?

a. Yes
b. No

22. If yes, how do you use export credit insurance?

a. With Ukrainian state-owned Export Credit Agency
b. With private Credit Insurance company, e.g. Euler Hermes, Coface, Atradius