

International Trade Procedure and Documentation

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INTERNATIONAL TRADE PROCEDURES AND DOCUMENTATION

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SYLLABUS

International Trade Procedures and Documentation

Objectives: The objective of the course is to make students learn the complete mechanism of export and various documents required for exports

S. No.	Description
1.	Export Procedures and Documents: The Search for an overseas buyer, Processing an Export Order, Negotiation of Documents, Role of Banks in Export-Import Transactions.
2.	Methods of Payments and INCO Terms: Methods of Payment, Financing Exporters and Importers, Instruments of Payment.
3.	EXIM Strategies and Export Marketing: EXIM Business Plan and Strategy, Export Strategy Formulation, Export Financing, Import Strategy (Sourcing Strategy), International Marketing, Export Marketing - Going Global, Different Forms of International Trade.
4.	Methods of Financing Exporters and Business Risk Management: Pre-Shipment Finance, Post Shipment Export Advance, Factoring and Insurance, Types of Risks, Quality and Pre Shipment Inspection.
5.	Custom Clearance of Import and Export Cargo: Clearance of Import Cargo, Clearance of Export cargo, Custom Valuation, The Harmonized System, Carnets, New Developments in Custom Clearance Procedure.
6.	Logistics and Characteristics of Modes of Transportation: Planning Physical Distribution, Benefits of Efficient Logistics System, Concept of Marketing Logistics System, Critical Elements of a Logistics System, International Transport System.
7.	Characteristics of Shipping Industries: History of Shipping Industry, Characteristics of Shipping Industry, Role of Intermediaries in Shipping Industry, Latest Trends in Logistics Operations, Ocean Freight Structure.
8.	Containerization and Leasing Practices: Containerization - Concept and Operation, History of Containerization, Types of Containers, Benefits of Containerization, Global Trade and containerization, Container Leasing Practices and Inland Container Depots.
9.	Export Incentive Schemes: Duty Exemption Scheme, Duty Remission Scheme, Export Promotion Capital Goods Scheme, Special Economic Zones.
10.	Information Technology in International Business: Electronic Procurement, Electronic Marketing, Electronic Logistics.

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Unit 1: Export Procedure and Documentation

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Objectives

Introduction

- 1.1 The Search for an Overseas Buyer
- 1.2 Export Documentation Requirements in India
- 1.3 Packing List
- 1.4 Processing an Export Order
- 1.5 Nature of Export Order
- 1.6 Acknowledgement of Export Order
- 1.7 Clarifications in Export Quotations
- 1.8 Summary
- 1.9 Keywords
- 1.10 Review Questions
- 1.11 Further Readings

Objectives

After studying this unit, you will be able to:

- Discuss the concept of overseas buyer
- Processing of an export order
- Describe the nature and scrutiny of export order
- Understand negotiation of documents
- Explain the role of banks in export-import transactions

Introduction

Export documentation is a very important area in export management. Exporters are required to follow certain formalities and procedures, using a number of documents. Each of these documents serves a specific purpose and hence carries its own unique significance. A clear understanding of all documents and their purpose, how to prepare these, number of copies required, when and where to file, is a must for all export professionals. Usually, one could counter this by saying that experts help is available to do this job, so why should one bother. Sounds convenient too; you may not prepare or file these documents by yourself, but then you will surely be able to crosscheck these for accuracy and correctness of information before allowing someone else to file these on your behalf. After all if anything goes wrong, whether you are an employee or an export businessman, it will be your neck on the noose!

An export manager needs to keep himself thoroughly updated on all documentation requirements to carry out an export transaction successfully and it is one of his primary responsibilities to ensure that all documentary formalities are duly complied with. Export transactions are

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comparatively more complex than domestic business transactions. These require a lot of paperwork and almost nothing is done verbally, while in domestic business, at times, one could do with certain verbal communications. For example, a lot of orders for domestic business are placed and received verbally. This is not possible in international business.

Documentation in export business assumes greater significance as many parties/authorities are involved in a single transaction. There are the buyers and exporters, buying agents, RBI, authorized dealers in India (where the exporter has his bank account), buyer's bank (foreign bank), DGFT, customs and port authorities, VAT and excise authorities, EPCs, insurance companies, inspection agencies, clearing and forwarding agents, shipping companies/airlines and inland haulage carriers, etc. This is just an indicative list!

Proper documentation will ensure smooth sailing with the requirements of each of these agencies and the resulting transaction will be a successful one. Inaccurate or incomplete documentation will result in serious financial and goodwill losses. Such losses can be completely avoided by understanding clearly the documentation requirements of all concerned parties and then meticulously planning to get the right documents in the right numbers, at the right places and at the right time.

To illustrate the extent of damage that faulty or incorrect documentation can inflict, let us take a look at the following points:

- The exporter may suffer financially in terms of higher interest costs/penalties/fines and discrepancy charges.
- He may have to spend extra money on phone/fax/courier services.
- He may suffer heavily due to loss of credit cover from insurance companies.
- He might be forced to pay heavy demurrage charges in his own country/offer compensation to his buyer in the form of discounts if there is delay due to snags in documents, affecting the buyer's ability to claim goods at the foreign ports.
- The exporter may be forced to airfreight goods at his own expense if the shipment is delayed unreasonably because of documentation problems.
- Last but not the least, the exporter may suffer loss of goodwill with the buyer resulting in loss of further business.

1.1 The Search for an Overseas Buyer

Perhaps the most daunting challenge any budding exporter faces is to find buyers for his/her products. Selling in international market has never been simple – with diverse language, geographical distance, cultural difference and lack of market knowledge posing real challenge to any manufacturer/exporter.

However, given right homework and planning, selling in overseas market today is easier, simpler and less expensive than it was a decade ago. There are many silver linings in the forms of positive Govt Policy, favourable international climate, less tariff and non-tariff barriers and above all easy and inexpensive access to an incredibly powerful and all-encompassing medium like Internet. Never before in the history of human civilization so many people from so vastly different places and societies freely interacted with each other as we witness today in Internet.

So, how do today's exporters take advantage of this favourable business climate and become successful? The answer lies in thoughtful planning, effective implementation and perseverance.

In fact, large number of Indian exporters has used these advantages successfully as reflected in unprecedented export growth witnessed over last 10 years.

1.1.1 How to Find Buyers

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To put it simply, there are only two ways you can find buyers of your products – either you find the buyer or buyer finds you. Your sales strategy must take into account both the factors and plan for effective use of both sources.

Some of the ways to locate buyers are:

- Searching directories, trade literature, etc.
- Using buyer-seller meets organized by trade associations
- Conducting Market Research
- Employing Commercial Agent/Representatives
- Subscribing to information services, etc.

Some of the ways of attracting buyers are:

- Advertisement
- Promotion (e.g. direct mail)
- Trade Shows
- Web-sites
- Search Engines, etc.

1.2 Export Documentation Requirements in India

Export documentation in India has evolved a great deal particularly since 1990. Efforts are on, on a faster footing to streamline and modernize the system further (see box 1.1 below). Prior to 1990, the documentation was all manual and not at all coordinated. The result was lot of delays and mistakes, rendering the task very clumsy, tiresome, repetitive and truly frustrating. India adopted the ADS in 1991. ADS refers to Aligned Documentation System, which is the internationally accepted documentation system (see box 1.2 below).

ADS uses a Master Document that contains the information common to all documents forming part of the aligned series.

Box 1.1: Right Click for Fast Delivery

Speed

- 50-page set of forms to replace 120 pages
- EDI linkage to facilitate online filing of documents
- Fast-track mechanism for perishable cargo
- Time limit to be set up for approvals/sanctions
- Importer-Exporter Code (IEC) number to be issued online.

To cut transaction time and costs for exports, which are about five times that of China, commerce and industry ministry announced several measures including a drastic trimming in the number of forms to be filled from 120 pages to 50 pages. The new set–Aayat Niryaat–has been introduced by DGFT.

Union Commerce Minister Kamal Nath said this was in keeping with his promise made in 2006 that exporters and importers would be spared from filing multiple application forms at various stages.

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He said a committee, set up under chairmanship of DGFT, had submitted its report. "We shall be implementing them," he said.

Electronic Data Interface (EDI) linkage will be ensured among all trade partners, like DGFT, customs, banks, export promotion councils, to facilitate online filing, verification and retrieval of documents.

A fast-track mechanism is being introduced for clearance, packaging, quarantine, etc. to facilitate import and export of perishable cargo. Time limits will be laid down for approvals/sanctions to ensure transparency in government departments and to ensure quality of service.

Moving towards an "automated electronic environment", the global trading community can now reach for a single source for all policy-related information, which will be available on the DGFT site. Video conferencing will replace manual filing of documents. This will be done via digital signatures. A special-purpose vehicle for electronic licence use and transfer mechanism is being planned.

A six-month time frame has been set for the customs and DGFT to complete EDI linkages. Once done, manual submission of shipping bills and other documents will be a thing of the past. Online verification will reduce transaction costs and time.

An Importer Exporter Code (IEC) number will be issued online. Linking the DGFT database with the income-tax PAN database, by using digital signatures, will do this.

Other e-governance initiatives are also being planned. The effort is to reduce human interface with DGFT offices.

Source: The Financial Express, April 8, 2005 & www.financialexpress.com.

Box 1.2

Document Alignment is a major trade facilitation activity, whereby trade documents based on the United Nations Layout Key and thus aligned in a standard format. Deriving national document subsets from the UN Layout Key rules simplifies trade documentation on an international scale, bringing considerable benefits to traders.

History

International trade developed over the centuries in an unstructured and ad hoc manner, as countries exchanged goods and products they excelled in for those, which they lacked. Documents accompanying these transactions followed a similarly haphazard path, to where numerous documents in a variety of formats were required for each export shipment. An order number might appear on the right or left side of a form; addresses could be shown as lines or blocks.

The situation started to improve in the mid 1960s with the document alignment work initiated by Sweden, standards developed by the Trade Facilitation Working Party of the UN/ECE WP.4, and the 1965 publication of the United Kingdom Board of Trade's Simpler Export Documents.

Alignment Aims

The objective of an aligned series of documents is to have as many forms as possible printed on the same size paper and to have common items of information occupying the same relative position on each form.

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For example, shipper top left, references top right, signatory details bottom right and so on. This makes forms both easier to complete and easier to process. Since common positions are used for data items, it is possible to use multi-part sets of different forms or to type a 'master document.' This master document can be used to produce a range of documents using a photocopier and overlays (to provide the form outlines and hide unwanted data).

Everyone in the international trade chain benefits from easier document processing. Using documents that comply with UN alignment standards speeds up form preparation, cuts costs and reduces errors. You may actually get paid quicker! Aligned documents simplify document checking and training of new staff. They even enhance an organisation's professional image.

Document alignment has been a major agenda item for the UN/ECE Expert Group on procedures and documentation, with the goal of simplified international trade documents.

Source: Lining up benefits for international trade by Tessa Jones, Head of Publications at SITPRO, the Simpler trade procedures board, the UK's trade facilitation agency; <http://www.unece.org/trade/cnct/art1944>.

The export documentation framework in India can be best understood by classifying export documents in the following two categories:

1. Commercial documents
2. Regulatory documents.

For the purpose of clear understanding, these are discussed under the following broad heads.

1.2.1 Commercial Documents

These documents have their origin in "Custom of Trade" in international commerce and are used by exporters/importers to discharge their respective legal and other incidental responsibilities under sales contract. Commercial documents can be further sub-divided into: (a) Principal commercial documents and (b) Auxiliary commercial documents

(a) **Principal commercial documents:** These documents serve the following purposes:

- ❖ To effect physical transfer of goods and title to the goods from exporter to buyer
- ❖ To realise export sales proceeds.

Principal commercial documents include:

- ❖ Commercial invoice (and the invoice prescribed by the importer)
- ❖ Packing list
- ❖ Certificate of inspection
- ❖ Certificate of insurance/insurance policy
- ❖ Bill of Lading/Airway bill/Combined transport document
- ❖ Certificate of origin
- ❖ Bill of exchange
- ❖ Shipment advice.

(b) **Auxiliary commercial documents:** These documents are required to prepare/procure the principal commercial documents and include:

- ❖ Proforma invoice
- ❖ Shipping instructions

- Notes**
- ❖ Insurance declaration
 - ❖ Intimation for inspection
 - ❖ Shipping order
 - ❖ Mate's receipt
 - ❖ Application for certificate of origin
 - ❖ Letter to bank for negotiation/collection of documents

1.2.2 Regulatory Documents

These are prescribed by various government departments/bodies for compliance of formalities under relevant laws governing export transactions. These include:

- Exchange Control Declaration Form-GR Form
- Freight Payment Certificate
- Insurance Premium Payment Certificate
- ARE I/ARE II Forms
- Shipping Bill/Bill of Export
- Port Trust Copy of Shipping Bill/Export Application/Dock Challan
- Receipt of Payment of Port Charges
- Vehicle Ticket

A detailed description of all the commercial documents is given below:

Commercial Invoice: It is the basic and most important document in an export transaction and extreme care has to be taken by the exporter to prepare this document. A commercial invoice must provide complete and accurate information as is expected. A slight mistake on the part of the exporter may cost him dearly. This document requires the exporter to submit details such as his own (exporter) details, invoice number with date, details of the consignee and buyer (if the buyer is other than the consignee), buyer's order number with date, country of origin of the goods, country of final destination, terms of payment and delivery, pre-carriage details (road/rail), place of receipt by pre-carrier, vessel/flight number, port of loading, port of discharge, final destination, marks and numbers, container number, number and kind of packaging, detailed description of goods, quantity, rate and total amount chargeable.

As can be seen, a commercial invoice contains the complete details of the export order right from order number to quantity, rate, packaging, mode of dispatch and shipping particulars. Normally, the trade practice is to raise and send a proforma invoice to the buyer for his approval, once the order has been finalised. On receipt of the approved proforma invoice, the exporter can use it as part of the export contract.

The commercial invoice serves the following objectives:

- It serves as the exporter's bill as it indicates the total chargeable amount.
- It provides both the consignor's and consignee's (buyer's details if the buyer and the consignee are different) details and the order number.
- It gives the complete details of goods being shipped, corresponding to the export order and letter of credit.
- As per the export order, the exporter is required to ship the exact quantity in the required packing. The invoice depicts both the quantity and packing, which must strictly be in accordance with the specifications of the export contract.

- It also lists the terms of delivery and payment that are to be as per the letter of credit/ export contract.

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Let us now learn to fill each segment of the commercial invoice one by one:

1. **Exporter:** This box appears on the top left hand corner of the commercial invoice. Here, the exporter is required to give his name and complete address specifying the city, state and country along with his phone and fax numbers. The purpose is to establish the identity of the shipper.
2. **Consignee:** This box requires details, that is, the name and complete address of the party to whom the goods are being consigned.
3. **Buyer:** Usually, the buyer and the consignee are the same. However, in cases where the buyer is different from the consignee, his details, that is, the buyer's name and complete address is to be provided in this box.
4. **References and Numbers with date:** In these boxes the relevant references such as exporter's quotation number with date, invoice number with date, buyer's order number with date have to be accurately filled in.
5. **Country of Origin of Goods:** The exporter has to fill this box with the name of the country where the goods have actually been produced.
6. **Country of Final Destination:** This box must provide the name of the country where the goods will be finally delivered.
7. **Terms of Delivery and Payment:** This box has to contain details of the terms of delivery like FOB, C&F, CIF, etc. and the terms of payment such as L/C (letter of credit), D/A (documents against acceptance), D/P (documents against payment), etc. These terms have been discussed in details in chapters titled "Terms of Payment" and "Methods of Payment" respectively.
8. **Pre-carriage By:** This box should provide the name of the carrier/mode of transport used to bring the goods from the place of origin to the place where these were accepted by the pre-carrier.
9. **Place of Receipt by Pre-carrier:** This box has to depict the name of the place where goods were accepted by the pre-carrier.
10. **Vessel/Flight Number:** This box requires the name and number details of the shipping vessel or the aircraft carrier being used for the shipment.
11. **Port of Loading:** The name of the port where goods are loaded on board ship or flight is required to be provided in this box.
12. **Port of Discharge:** The name of the port where goods are finally off-loaded (airport or seaport) is to be filled in this section.
13. **Final Destination:** This box must contain the name of the place that is the final destination of the shipment. This will mean not the port of discharge but the final destination from the port of discharge in the buyer's country. For example, if the airport of the final discharge is JFK, New York, but the goods are supposed to be finally delivered at the Atlantic City, the name of Atlantic City will be given in this box.
14. **Mark Numbers and Container Number:** This box shows the various marks and numbers that are required to be put on the packed cargo. If containers are being used, then the container numbers are also required.
15. **Number and Kind of Packages:** Here, the type of packages being shipped such as cartons, bales, bags, drums, crates, etc. and the total number of such packages being shipped are to be provided.

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16. **Description of Goods:** The detailed description of goods being shipped is to be put in this section. The description has to be the same as required in the export order/letter of credit. If more than one types of goods are being sent, the description of each is required to be given against the respective number and kind of packages.
17. **Quantity, Rate and Amount:** These columns must show the quantity and respective rates of each item being exported and the total amount chargeable, both in figures and words. The quantities and rates have to be the same as in the export contract.
18. **Signature with Date:** The invoice must in the end, have the signatures with date of the exporter or his authorized representative. Unless this is done, the invoice will remain incomplete and therefore ineffective.

At times, the importing buyer may ask for specific commercial invoices as per the customs/requirements of their countries:

- I. **Consular Invoice:** Some countries use consular invoice as a non-tariff barrier. Here, the exporter is required to get the commercial invoice verified by the Embassy/Consulate of the importer's country in his (exporter's) country. This certification is done by way of seal/stamp from the Commercial section of the Embassy/Consulate on payment of the requisite processing fee. For example, many of the Middle East countries require this verification for their imports from India.
- II. **Legalized Invoice:** Many countries require the exporter to get the commercial invoice certified by the local chamber of commerce in the exporting country to verify the correctness of the invoice. Once attested, this commercial invoice becomes legalized for the importing country. For example, Mexico requires such legalized invoices for imports from India.
- III. **Customs Invoice:** Here, the importing country requires the commercial invoice to be prepared in its own prescribed format, usually for safeguard against dumping activity. The information required is almost the same and the exporter is required to self-attest such invoices. Examples of such countries are the US, Canada and Australia.

1.3 Packing List

This document provides the details of number of packages; quantity packed in each of them, the weight and measurement of each package and the net and gross weight of the total consignment. Net weight refers to the actual weight of the items and gross weight means the weight of the items plus the weight of the packing material. In fact, it carries almost all the information as the commercial invoice but for the rate and total amount. It excludes the financial part of the transaction but concentrates on the physical and material part.

In cases where the shipment consists of one item in a single pack, the packing information may be incorporated in the invoice itself. However, as a general trade custom, both the documents are used irrespective of the size of the shipment.

The packaging list serves a useful purpose for the exporter while dispatching the consignment as a crosscheck of goods sent. For the port personnel, it comes handy while planning the loading and offloading of cargo. It is also an essential document for the customs authorities as they can carry out the physical examination of cargo and conduct checks on the weight and measurements of the goods smoothly against the declarations made by the exporter in the packing list.

Shipping Instructions: This document serves as a checklist of the exporter's instructions to the shipping company regarding a particular shipment.

Intimation for Inspection: This is the prescribed format for intimating the Export Inspection Agency (EIA) inviting them to come to inspect the shipment.

Certificate of Inspection: This is the certificate issued by the EIA after it has conducted the pre-shipment inspection of goods for export provided the goods fall under the notified category of goods requiring compulsory pre-shipment inspection.

Certificate of Insurance/Insurance Policy: Insurance is an important area in the export business as the stakes are usually very high. Protection needs to be taken in the form of insurance cover for the duration of transit of goods from the exporter to the importer.

Regular exporters normally opt for an open insurance policy and as they make a shipment, they are required to file an insurance declaration with the insurance company. Against this declaration, the insurance company issues an insurance certificate, which is a negotiable instrument. The policy covers all the terms and conditions of the cargo insurance whereas a certificate issued under an open policy serves as an evidence of insurance of goods shipped.

Bill of Lading/Airway Bill/Combined Transport Document: These documents are also known as Transport Documents. Let us discuss these one by one:

1. **Bill of Lading:** This is issued when goods are shipped using ocean (marine) transport, i.e. ships. When the exporter finally hands over the goods to the shipping company for loading on board the ship for transport to their foreign destination, the shipping company issues a set of Bills of Lading to the exporter. This set serves multiple purposes. It is a receipt signifying physical acceptance of cargo by the shipping company and also a contract of carriage between the exporter and the shipping company for transport of the goods to their designated destination. In addition, the bill of lading also works as a document of title to the goods. The importer gets the right to take possession of the merchandise in his own country only if he possesses the bill of lading. This document is the instrument used for passing the ownership right or title of the goods to the buyer by the exporter.

A bill of lading is a negotiable instrument as it is transferable by endorsement and delivery. However, as already explained above, it also serves some non-negotiable purposes. Therefore, it is always issued as a set containing both negotiable and non-negotiable copies.

A bill of lading can be 'freight paid' or 'freight to pay', depending upon whether the freight is prepaid or is to be collected at destination. The shipping company will stamp the bill of lading as freight prepaid in case the exporter has already paid the freight at the port of loading and the bill of lading will be marked as freight collected or freight to pay if the freight has not been paid and is required to be collected from the importer at the port of discharge.

Bill of lading can be of various types:

- ❖ An On Board or Shipped Bill of Lading signifies that the goods have been placed on board the ship. Such B/Ls are required in case of FOB (Free on Board) shipments.
- ❖ Received for Shipment Bill of Lading signifies that the shipping company has received the goods for shipment. Goods are waiting for shipment and are under the custody of the shipping line. Such B/Ls will work in case of FAS (Free Alongside Ship) shipments.
- ❖ A Clean Bill of Lading is one that does not contain any negative remark on either the quality of goods or on the physical condition of the packaging of the merchandise received by the shipping company. Importers worldwide insist on such B/Ls.
- ❖ A Dirty or Claused Bill of Lading is one that carries a remark put by the shipping company regarding the damage to the goods or their packaging.

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- ❖ A Stale Bill of Lading is one that is presented by the importer at the port of discharge late and as a result he may be required to pay fines and warehousing charges, etc. If this delay is caused due to exporter's late dispatch of documents, the importer is likely to penalize him.
 - ❖ A Transshipment Bill of Lading is needed where goods are required to be transshipped. However, the original carrier who issues such a bill, takes on the role of an agent in all subsequent journeys and thus cannot be held responsible for any loss/damage to the cargo during such subsequent transport.
 - ❖ A Through Bill of Lading is required where goods are to move from one carriage to another. This B/L acts as a combined transport document where the original carrier takes on the role of the principal carrier and thus becomes responsible for the total journey for loss/damage to the cargo.
 - ❖ The shipping company issues a Charter Party Bill of Lading in cases of charter shipping. Such B/Ls require specific authorization in the L/C for purposes of negotiation.
 - ❖ A Short Forms Bill of Lading contains all the elements of a B/L except that it does not have all the attributes of a contract of affreightment. Banks do accept such bills for negotiation unless expressly prohibited by the L/C.
 - ❖ A House Bill of Lading, also called a freight forwarders' bill of lading, is issued by the freight forwarder, consolidator or a NVC (non-vessel carrier). It is a non-negotiable document containing the names, addresses of the parties and specific description of the goods shipped.
2. **Airway Bill:** Airway bill is a bill of lading used when the goods are shipped using air transport. It is also known as an air consignment note or airway bill of lading. It is similar to the ocean bill of lading on two counts. One, it too serves as a receipt of goods by the carrier and two, it also works as a contract of carriage between the shipper and the carrier. However, unlike a marine bill of lading it does not serve as a document of title to the goods. Hence, it is a non-negotiable document.

The goods will be delivered to the party named as consignee in the AWB without need of any further formalities, once the importer obtains customs clearance. Therefore, an exporter is advised to ensure the payment receipt, as it is quite risky to consign goods through air direct to the importer.

As per IATA (International Air Transport Association) norms, an airway bill is issued as a set of 12 copies, having three originals as explained below:

- (a) First Original is green in colour. It is meant for the carrier issuing it and is to be signed by the exporter or his agent
- (b) Second Original is pink coloured and is meant for the importer (consignee) and therefore accompanies the shipment through to the final destination and is signed by the carrier or his agent.
- (c) Third Original is blue in colour and is for the exporter. It is signed by the air carrier after goods have been accepted for airfreight and handed over to the consignor.



Note Airway bill is a very important document when goods are sent through air. It serves the all-important purpose of tracking the shipment and is also required at the time of customs clearance.

3. **Combined Transport Document:** This is also known as Multi-modal transport document. Ever since containers have become popular, the concept of combined transport has gained solid ground.

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Containerization has made it possible to move the goods from the place of origin, i.e. the factory or warehouse, to its final destination, that is the buyer's premises in the foreign country. Containers, in fact are also used in domestic transportation in India. Indian Railways have their door-to-door delivery service. The goods are transported in containers from one country to the other using different modes of transport. From the exporter's premises, the containers are loaded on trailers (road transport), which then use rail transport for carriage up to the port of loading and finally these are put on board the vessel. Likewise, in the foreign country too, the containers travel up to the importers premises using multiple or combined modes of transport. The combined transport document is used to cover this total journey of cargo using the various transport modes.

Certificate of Origin: This document serves as a proof of the country of origin of goods for the importer in his country. Importing countries usually require this to be produced at the time of customs clearance of import cargo. It also plays an important part in computing the liability and rate of import duty in the country of import. This certificate declares the details of goods to be shipped and the country where these goods are grown, manufactured or produced. Such goods need to have substantial value-addition in the country of export so as to become eligible to certification of this nature. Certificate of origin also has the dimension of preferential duty treatment attached to it provided it falls under the GSP category. Accordingly, the Certificate of Origin can be classified in the following two categories:

- (a) **Non-Preferential:** The local chamber of commerce in the country of export normally issues such a certificate of origin. It serves only as a proof of country of origin and does not offer any duty benefits to the importing countries. The exporter is required to make an application to the local chamber of commerce in a prescribed format and the chamber upon scrutiny of this application will issue the certificate of origin. The formats of both the application and the certificate of origin are given in the enclosed CD.
- (b) **Preferential:** These are required by importing countries offering concessional (preferential) import duties to import from certain countries under certain trade agreements. The following preferential certificates of origin currently are applicable for exports from India:
 - ❖ **Generalised System of Preferences (GSP):** Under this system many developed countries like the US, Japan, Switzerland, Canada, Hungary, EU, Norway and New Zealand offer concessional tariffs to developing nations. This instrument is non-contractual in nature and the offer is made on a unilateral and non-reciprocal basis. These countries have their GSP schemes reviewed and updated on a timely basis to give details of specific benefits available under particular product categories. Usually, these benefits are made available to exporters on providing relevant information in a prescribed GSP form.
 - ❖ **Global System of Trade Preferences (GSTP):** This is an arrangement between developing nations under which concessional tariffs are provided on a reciprocal basis. India has such arrangements with many other developing countries. For availing of these preferences, exporters in India can obtain certificate of origin under GSTP from EIA (Export Inspection Agency), which is the sole agency authorized to issue these certificates.

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- ❖ Other preferential systems exist under the SAARC Preferential Trade Agreement (SAPTA), Bilateral Preferential Trading Agreement with Afghanistan, Indo-Sri Lankan Free Trade Agreement etc.

Shipping Order: This document is the reservation slip issued by the shipping company against the exporter's or his agent's request for booking of ship space for a shipment. In case of air transport of cargo, this document is known as Carting Order.

Mate's Receipt: Once the goods are received on board the ship, the master of the ship issues a document called mate's receipt to the port authorities for every shipment. The exporter must then collect this receipt either himself or through his authorized agent from the port authorities by paying all charges due to them. The shipping company issues the bill of lading to the exporter only against the mate's receipt. This document is not a document of title. It is merely a receipt of goods. However, it is a very important document as without it, the exporter will not be able to obtain the title document to the goods, that is, the bill of lading. Therefore, the exporter is best advised to obtain the mate's receipt from the port authorities soon after the goods have been placed on board. Any delay here may further result in greater delays leading to unwanted losses.

Bill of Exchange: Also known as a Draft, this is an instrument for payment realization. By definition, it is a written unconditional order for payment from a drawer to a drawee, directing the drawee to pay a specified amount of money in a given currency to the drawer or a named payee at a fixed or determinable future date.

The exporter is the drawer and he draws (prepares and signs) this unconditional order in writing upon the importer (drawee), asking him to pay a certain sum of money either to himself or to his nominee (endorsee). This order could be made for payment on demand, called a bill of exchange at sight or payment at a future date, called a usance bill of exchange. Usually, sight bills of exchange are used with Documents against Payments (D/P) method of receiving payment and usance bills of exchange are used for Documents against Acceptance (D/A) system. Since both these systems do not provide any security to the exporter regarding payment realization, these bills, in actual practice, are drawn under a letter of credit to ensure guarantee of payment. Usance bills of exchange are drawn for periods ranging from one to six months. These are negotiable and are usually discounted by the exporter.

Shipment Advice: The exporter sends this document, called shipment advice, to the buyer soon after the shipment is made to provide him all the shipment details. This serves as advance intimation of the shipment and allows the importer to arrange for the delivery of the same.

Letter to Bank for Negotiation/Collection of Documents: This is a standard letter covering various instructions that an exporter must give to his bank at the time of submitting shipment documents concerning the negotiation/collection of documents.

Let us understand the regulatory documents now:

Exchange Control Declaration Forms: As per the Foreign Exchange Management (Export of Goods and Services) Act, 2000, all exporters from India excepting those exporting to Nepal and Bhutan, are required to submit an exchange control declaration form in the prescribed format. The purpose behind this declaration is to ensure timely realization of export proceeds by the exporters and to track the defaulters.

FEMA requires the submission of export documents to the Authorised Dealer by the exporter within 21 days from the date of shipment. The time allowed for full export value realisation is six months from the date of shipment.

Following four types of foreign exchange declaration forms are used in India:

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- I. Guaranteed Remittance or GR forms are to be submitted (in duplicate) for all types of physical exports from India including export of software in physical form using magnetic tapes or paper.
- II. Self Declaration Forms or SDF Forms are to be submitted by all such exporters who are shipping from a port/airport where the customs authorities have EDI (Electronic Data Interchange) facility for shipping bill processing. SDF forms are required to be attached with the shipping bill in duplicate.
- III. Software export declaration forms, called SOFTEX forms are required for exports of software in non-physical form; for example, online transmission of data using satellite links. These must be submitted in triplicate.
- IV. Postal Parcel or PP forms are used when exports are done by post. These are also to be submitted in duplicate.

Freight Payment Certificate: This certificate is an evidence of freight payment. It certifies that due freight has been paid by the exporter. It is an equivalent of freight receipt.

Insurance Premium Payment Certificate: This document certifies the payment of insurance premium.

ARE I/ARE II Forms: These are forms pertaining to Central Excise Clearance. These need to be used only by those exporters who are governed by Central Excise.

These forms are basically prescribed application forms for obtaining permission from the Central Excise Authorities for removal of excisable goods for exports. Another form known as CT-1 is used to seek permission from the Central Excise authorities to remove excisable goods without the payment of excise duty for exports.

Shipping Bill/Bill of Export: This happens to be the most important document required by customs authorities for permitting exports. It is called a shipping bill in case of export by sea/air and a bill of export when the export is done using land transport. The goods are allowed to enter the port only after the custom officials have stamped the shipping bill. It contains complete details of the shipment including name of exporter, name of importer, description of goods, port of loading, port of discharge, marks, number, quantity, FOB value, country of destination, name of the vessel or flight number, etc.



Did u know? Shipping bills can be of the following types:

- (a) Shipping bill for dutiable goods
- (b) Shipping bill for duty-free goods
- (c) Shipping bill for claiming duty drawback

Port Trust Copy of Shipping Bill/Export Application/Dock Challan: This form is the same as shipping bill. However, the purpose here is to assess the various port and dock charges. This is used in sea shipments.

Receipt of Payment of Port Charges: This is the receipt issued by the Port Trust Authority on payment of port dues by the exporter.

Vehicle Ticket: It serves the purpose of an entry pass for the exporter to get his export cargo inside the port for export to its final destination.

Notes

Additional Documents/Certificates: In addition to the various documents/certificates discussed above, there may be a need of some additional documents/certificates. These are briefly described below:

1. **Blacklist Certificate:** This is required only in those specific cases where the importing country is at war or has hostile relations with another country and wants to make sure that the exporter is not in any way touching that country for purposes of fulfilling this order.
2. **Antiquity Certificate:** This certificate is needed only in those cases where goods are being exported as antiques and the importer wants their authenticity checked. In India, Archaeological Survey of India is authorized to issue such certificates.
3. **Health/Veterinary/Sanitary Certificate:** Many importing countries require such certificates particularly in case of imports of foodstuff, livestock, hides, marine products, etc. to safeguard against the dangers of diseases and health hazards. The exporter has to get the required certification from the respective health, veterinary or sanitary authorities, before he is able to dispatch his goods.
4. **Fumigation Certificate:** Certain importing countries require fumigation of the cargo before it is allowed to enter their limits. This is again needed for cargo like plants and weeds, to ensure safety against spread of harmful virus. The exporter has to not only get the fumigation done but has to also submit a certificate from the prescribed agency to that effect.
5. **Use of ADS in India:** As already explained, aligned documentation system (ADS) for exports is in use in India for many years now. It offers many advantages and has really made life a lot simpler for the exporter and importer as well as related agencies in both countries.
6. **ADS uses:** Master Document I and Master Document II for preparing commercial and regulatory documents respectively.

To begin with, masks were used to prepare documents under ADS that were used to hide all the information not required in a specific document. In this way, using masks and photocopying the master documents all the aligned documents could be readied. Any additions required could either be pre-inserted or added later.

The commercial documents under ADS are prepared on standard A4 size (210mm × 297mm) paper whereas regulatory documents are prepared using full scape paper measuring 34.5 cms × 21.5 cms. The design of the documents is such that the common slots of information are aligned to perfection and find the same relative space in each of the documents forming part of the system.

An Indian exporter can generate 14 commercial documents out of a total of 16 by using the Master Document I. Similarly; Master Document II could be used to prepare three out of nine regulatory documents.

Widespread usage of computers has made it even simpler to use ADS to prepare export documents. Many software companies sell customized software packages to create export documents as per the requirements of Indian exporters. One hopes that very soon we will see more and drastic changes to streamline the documentation system further.



Task Interview an exporter in your area and try to find out from him the documents that he prepares for his export shipments.

Self Assessment**Notes**

Fill in the blanks:

1. ADS refers to, which is the internationally accepted documentation system.
2. Regulatory Documents are prescribed by various government departments/bodies for compliance of formalities under relevant laws governing transactions.
3. Invoice is the basic and most important document in an export transaction and extreme care has to be taken by the exporter to prepare this document.
4. List provides the details of number of packages; quantity packed in each of them, the weight and measurement of each package.
5. Certificate of Inspection is the certificate issued by the after it has conducted the pre-shipment inspection of goods for export.
6. Bill of Lading is issued when goods are shipped using transport, i.e. ships.
7. is a bill of lading used when the goods are shipped using air transport. It is also known as an air consignment note or airway bill of lading.
8. has made it possible to move the goods from the place of origin, i.e. the factory or warehouse, to its final destination.
9. Certificate of Origin serves as a proof of the country of origin of goods for the in his country.
10. Bill of exchange is an instrument for realization.

1.4 Processing an Export Order

Export order is an important document as it works as a base for other documents to be prepared in international trade transactions. The roles of commercial and regulatory documents are well-known as no international trade transaction can take place without them. Such documents vary from country to country, from port to port within a country and from product to product.



Example: The number of documents used in developing countries is usually higher when compared to developed countries, as developing countries still deploy a variety of documents in order to restrict or control their imports.

Similarly, documents vary between ports within a country such as Export Application, which is used when a shipment is sent from Chennai and Cochin; Port Trust copy is used in case of Port of Mumbai, JNPT and Kandla and Dock Challan is used in case of Port of Kolkata and Haldia, although all of them serve the same purpose. In the LPG&M era, countries have become very sensitive to quality and technical standards of products and may prescribe a specific document to be accompanied for such inspection from a certified agency. Hence; it is advisable that all these matters be discussed in advance and put into paper in an export order.

The first task to be completed by an exporter is to acknowledge the receipt of the order to the foreign buyers. Acknowledging an export order is different from confirming the same and it is advised that an exporter must make a proper scrutiny of export order before confirming it to the foreign buyer. Scrutiny of export order is also important as it provides a final opportunity to make necessary changes in the same. It is to be seen that export order must conform to the terms and conditions as sent to the importer. Important issues to be examined are terms of payments,

Notes

price, delivery date and schedule, product specifications, pre-shipment inspection, special packaging, labeling and marking, quality issues, number of items, quantity, shipping marks, marine insurance, trade documents required, etc. If the exporter has any doubts or confusion, he can seek clarification from the importer in this regard. Once the scrutiny of export order is over and the exporter is satisfied; he can fulfill all terms and condition as mentioned in the export order. He must spontaneously confirm the same to the importer with his acknowledgement of thanks.

Having sent the confirmation of the export order, the exporter shall take necessary steps to enter into a formal international sales contract with the buyers. Internationally, there are no standard rules and regulations with regard to international sales contracts. It has been seen that, in certain cases, it is just a one-page document and in some other cases, it may be a very complex 15-page booklet including many appendices, additional conditions, etc. Sometimes, mere verbal commitments become an international sales contract, but this varies from exporter to importer and vice versa. But it is advisable that exporters must enter into an international sales contract with the importer as international trade is full of risks and a sales contract ensures legal protection through accepted documents during arbitration, in case of disputes. The International Chamber of Commerce also advises exporters and importers to pen down the sales contract in order to avoid disputes and even if disputes occur; the ICC helps the arbitration process to be progressed easily with strong evidences. In some countries; it is mandatory to enter into an international sales contract. All these issues need the attention of the exporter in advance, to avoid any unforeseen situation in the future.

1.5 Nature of Export Order

An export order is a document sent by the importer on the basis of pro forma invoice of exporter, whereby the importer communicates his willingness to purchase items/commodities/services etc. from the exporter. It shall clearly indicate the exporter's pro forma invoice/quotation number and its date including the essential aspects like terms of payments, price, delivery date and schedule, product specifications, pre-shipment inspection, special packaging, labeling and marking, quality issues, items, quantity, shipping marks, marine insurance and trade documents required for the trade deal. The exporter himself, or his trusted manager shall properly and thoroughly scrutinize the export order before confirming it to the importer about his willingness to fulfill the order.

1.6 Acknowledgement of Export Order

Customer is a king whether consumer himself or a foreign buyer and he must be thanked for giving the business or an opportunity to serve. Hence the exporter shall write a simple letter to the importer thanking him for the export order. The exporter should also acknowledge his pleasure and gratitude thank the importer. He should also mention that he would get in touch with the importer shortly after scrutinizing the export order. A letter of thanks shall be formal in language and shall not be long.

Scrutiny of Export Order

"Prevention is better than cure". The same is applicable to an export order. The exporter has to carefully examine the contents of the export order otherwise he may have to face problems while receiving payments in ways such as quality disputes, specifications disputes, discrepancy in documents while negotiating letter of credit, or other situations beyond his and the importer's

control, i.e. exchange regulations of importing country, sanitary phyto-sanitary regulations etc. The important aspects to be examined carefully of export order as follows:

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1. **Item (product):** The exporter has to check whether he has received the order for the same product for which he has sent per forma invoice/quotations, etc. as the same exporter may have sent two or three quotations for other purchase orders to the same importer. It is advisable to check the quotation number with the export order.



Did u know? The usual errors that happen in international trade are:

- (a) The exporter has sent an order for supply of goat meat but receives an order for lamb meat.
 - (b) The exporter has sent an order for male trousers but receives order for female trousers.
 - (c) The exporter has sent a quotation for supply of P-3 computers and has received an order for P-4 computers.
2. **Sizes and Specifications:** The exporter shall check that size and specifications are same as quoted. A minor difference may create havoc.
 - (a) An Indian exporter of pharmaceuticals receives an order from an American importer. After scrutiny of the export order he supplies pharmaceuticals to the importer. After receiving the medicines, the importer refuses to make payments as the medicines supplied vary slightly on specifications as per the US Federal Drug Authority.
 - (b) A firm based at Hyderabad supplies meat to a firm in the United Arab Emirates. The exporter has checked all specifications but forgets to get certificate from the local maulvi, certifying that it is halal meat as per Islamic traditions. The importer refuses to make payments although the meat was biologically safe for consumption and best in quality and price in keeping with industry standards.
 - (c) An Indian exporter gets an order from a German importer for supply of iron pipes. As per export quotation; the circumference size was given as 0.5 cms. In the export order, the circumference size was mentioned as 0.50. The exporter makes a mistake in judging that zero is a limiting factor here and supplies pipes, the circumference of which was 0.51. The importer refuses to make payment, as goods supplied are not as per order. It is to be noted that zero acts as limiting factor in this case. Hence it is advisable that exporter should read between the lines and may take inferences from the zero as well.
 3. **Pre-shipment Inspection:** The Government of India, through its Export Quality Control Act 1963, has made it mandatory to get goods inspected before shipments. Now it is to be seen that inspection is to be done by the buyer-nominated agency or exporter's agency. If it is by the importer's nominated agency, it is advisable to get that agency named in the export order itself. Otherwise, there may be problem to the exporter later on, as the buyer's chosen agency may be located at a distant place and it can have financial implications to the exporter.
 4. **Terms of Payments:** The exporter has to check whether the terms of payments are the same as mentioned in the quotation he has given. Advance payments are considered to be the safest mode of payments but no importer is willing to make payments in advance in this globally competitive era. A letter of credit is another preferred method of payment, but the exporter needs to check its authenticity and transactional cost involved. Documents against Payments and Documents against Acceptance are other method of payments,

Notes

which are widely used in international trade. The buyer has to be careful in choosing his payments terms keeping in mind the creditworthiness of the importer. Open Account Payments are not advisable as the jurisdictions of countries vary and there are no international conventions protecting exporters through arbitration for obtaining payments under the Open Accounts Method. Some of the important issues to be looked at by exporters are:

- (a) Letter of credit, which is opened by the importer bank, shall be confirmed by the Indian bank. Exporters shall also check the creditworthiness of the bank through world banks almanac.
 - (b) The exporter can submit the documents as required in the letter of credit at the time of negotiating these documents with the bank for receiving payments.
 - (c) Payments under Drafts (bill of exchange) drawn are to be 'sight' or 'usance' and to be drawn on the bank of importer or the buyer himself.
 - (d) The exporter has to see whether the credit validity period is sufficient for the collection of all relevant documents or not. If not, it is advisable to get it extended by the buyer in the beginning itself.
 - (e) What is the exchange control regulation of the buyer country? It is possible that the buyer may be interested to make payments but due to importer's country's balance of payments problems, the exporter may not receive payment in freely convertible currency as per Indian regulations.
5. **Special Packaging, Labelling and Marking:** The exporter shall also look into any kind of special packaging requested by importer. It is good to decide the packaging specification of some perishable goods in the export order itself. Certain colours and numbers are taboo in certain countries or for those importers. Countries like Germany impose a legal restriction on exporter to get back the packing material. Exporters must cross-check all such issues and accordingly decide their price involving all such hidden costs.
6. **Shipment and Delivery Date:** If the exporter is comfortable to supply the goods by that date; he shall also crosscheck that he has sufficient time to submit his documents for negotiation/purchase/discounting with the bank for receiving the payments for that export order.



Note Important issues to be examined are as follows:

- (a) Part (partial) shipment allowed.
 - (b) Transshipment is permissible/not permissible.
 - (c) Port of shipment/destination is same or modified.
7. **Marine Insurance:** The exporter shall examine the shipping terms and responsibility of availing insurance cover for the goods. If it is the exporter's responsibility than he shall discuss the insurance policy coverage with the importer and insurance company as obtaining insurance cover in foreign countries is cheaper than in India and it affects price. That is why importers are usually sensitive to this issue while signing a trade deal with Indian exporters.
8. **Documents:** Export documents are same as per quotation, particularly those documents that are required with the bill of exchange, like:
- (a) Commercial invoice is the usual or there may be any specific notation required therein, such as it has to be visa-ed. In addition, consular invoice is also required or

certification by any authority of the commercial invoice in exporter country. For instance, it may have to be legalized or certified by the importing country consular in exporter country.

- (b) Type of bill of lading, is it “straight” or “to order” “shipped” or “received for shipment”, “direct” or “through”, etc.
- (c) The exporter needs to look whether the certificate of origin required is the usual one as issued by a trade association or a chamber of commerce such as FICCI, PHD chamber of commerce or a special one, like that required for GSP concessions or other preferences. The exporter should also check whether the Certificate of Origin required is preferential or non-preferential. Preferential certificate of origin may have lower duty in importer country, thereby making the exporter’s products attractive in importer country markets. Certain countries also demand necessary certification on commercial invoice or a separate certificate of origin.
- (d) Packing list/Cargo manifest as the case may be, if any special thing is required in it is to be checked.
- (e) Marine insurance – general policy, coverage, time duration, etc. are the issues to be looked into.

1.7 Clarifications in Export Quotations

In case the exporter is not satisfied with the terms and condition of export order he can request the importer to change those clauses/conditions on the basis of mutual discussion. Exporter can seek clarification on any of the following issues with the importer.

1. Terms of Payments
2. Price
3. Delivery Date and Schedule
4. Product Specifications
5. Pre-Shipment Inspection
6. Special Packaging
7. Labelling and Marking
8. Quality Issues
9. Number of Items
10. Quantity
11. Shipping Marks
12. Marine Insurance
13. Any other Documents Required.

Other important issues that should be properly looked into by the exporter; are some terms such as immediate delivery, good quality, prompt shipments, etc. used in exporter orders.

The exporter usually doesn’t put any time limit in getting the clarifications and expect that he shall get such clarification from importer in due course of reasonable time. But there is no harm if the exporter puts a time limit of say, fifteen days or so for getting these clarifications from the importer for speeding up the work. Once the exporter has received the clarifications from the importer, he must confirm the same to the importer before starting work. The confirmation is to

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be sent on the printed form or on a simple letter. The usual practice is to repeat the broad terms on which the exporter accepts the export order once again, to get the things clarified thoroughly.

Confirmation of Export Order

In case the exporter is satisfied about different aspects of the export order as discussed above, he shall send a confirmation of the export order to the buyer. In fact, there is no standard format to be used in export order confirmation. It is just a letter to be sent by the exporter to the importer that he is satisfied with all the terms and conditions as mentioned in the order and he shall deliver the goods as per the schedule. Now the importer is required to open a letter of credit in favour of the exporter so that the exporter can start his work on the export order and can avail of the necessary packing credit from the bank.

Reserving Space for Shipment

In order to overcome the problems of shipping space for transporting cargo to importers country with carriers/shipping company; it is advisable for the exporter to get the shipping space booked in advance. He shall take necessary steps to get the space booked with a shipping company from the port of shipments. Nowadays, exporter's works have become easy as freight forwarder takes care of all such responsibilities but it is imperative to inform the freight forwarder for the same. The information of the arrival of ships becomes available at least 10 weeks in advance and accordingly the exporter can get his shipping space booked for transporting the cargo. He shall also see that the product does not demand any kind of special packaging or special shipping facility such as cooling heating, humidity control, etc. If goods are perishable; he must check the carrier's capability to handle it. As the freight forwarder looks at all these issues it is pertinent to appoint an experienced and renowned freight forwarder to handle all these issues.

Delivery Note/Purchase Order

If the exporter himself is the manufacturer; he must send a delivery note to the production department of the firm indicating the delivery schedule and other terms and conditions such as specifications, etc. He can attach the copy of the export order so that the production department may take care of all such requirements as needed in the order. As an industry practice, it is observed that the exporter must send at least 20 days in advance the delivery note to the production department of the firm, but it varies from industry to industry as iron production takes much higher time in comparison to fast moving consumer goods.

In case, the exporter is a merchant exporter he shall immediately contact his supplier to supply the goods and intimate him a time schedule that is at least 5 days in advance of the delivery date. It is advisable to keep a routine tab on the suppliers to get first hand status on the work in progress. Immense care is to be taken regarding quality concerns and specification while getting goods outsourced from the third supplier. Some important contents to be supplied to the production department or third suppliers are:

1. Size specification and standard of the product
2. Quantity required by the exporter
3. Quality clearly defined as expected
4. Delivery time and schedule
5. Any special issues concerning the use of inputs, etc.
6. Labelling and marking requirements, if any

7. Special packaging requirements, if any
8. Storing stipulations for the product

Notes

Self Assessment

Fill in the blanks:

11. is an important document as it works as a base for other documents to be prepared in international trade transactions.
12. of export order is also important as it provides a final opportunity to make necessary changes in the same.
13. The first task to be completed by an exporter is to acknowledge the of the order to the foreign buyers.
14. Payments under Drafts (bill of exchange) drawn are to be and to be drawn on the bank of importer or the buyer himself.
15. If the exporter himself is the manufacturer; he must send a note to the production department of the firm indicating the delivery schedule and other terms and conditions such as specifications etc.



Task Discuss the issues on which the exporter can seek clarification with the importer.

1.8 Summary

- This unit discussed the export documentation framework in India so essential to understand for exporters and export managers alike.
- The importance of proper and accurate documentation in export transactions was duly highlighted. Inaccurate or incomplete documentation will result in serious financial and goodwill losses.
- Export Documentation in India has evolved a great deal particularly since 1990. Prior to 1990, all documentation was manual and not at all coordinated.
- The objective of an aligned series of documents is to have as many forms as possible printed on the same size paper and to have common items of information occupying the same relative position on each form. Under ADS, trade documents are based on the United Nations Layout Key and thus aligned in a standard format.
- The Indian classification of export documents under Commercial and Regulatory documents was then explained in great details taking each document one by one.
- Finally, a brief overview of software packages available to help exporters manage their export documentation better has been given.

1.9 Keywords

ADS: It refers to Aligned Documentation System, which is the internationally accepted documentation system.

Antiquity Certificate: This certificate is needed only in those cases where goods are being exported as antiques and the importer wants their authenticity checked.

Notes

Forfeiting: Forfeiting is a financing mechanism that enables a company to convert credit sale to cash sale, on 'without recourse' basis.

Vehicle Ticket: It serves the purpose of an entry pass for the exporter to get his export cargo inside the port for export to its final destination.

1.10 Review Questions

1. Describe the export documentation framework in India in details. How do you think has ADS helped the cause?
2. Explain the significance of Commercial Invoice in an export transaction. Discuss the various types of invoices that the importing countries may require.
3. What is an Ocean Bill of Lading? How is it different from an Airway Bill?
4. Write short notes on:
 - (a) Mate's Receipt
 - (b) Shipping Bill
 - (c) Nature of Regulatory Documents
 - (d) Blacklist Certificate
5. Discuss the Exchange Control Declaration Forms used in India in detail. What purpose do these serve?
6. Distinguish between the following:
 - (a) Shipment Advice and Shipping Instructions
 - (b) Preferential and Non-Preferential Certificate of Origin
 - (c) Shipped Bill of Lading and Received for Shipment Bill of Lading
 - (d) Proforma Invoice and Invoice
7. Discuss the process to be followed by exporter in processing an international trade transaction.
8. In case of purchase order or delivery note, list down the important contents to be supplied to the production department or third suppliers.
9. Write a brief note on scrutiny of export order.

Answers: Self Assessment

1. Aligned Documentation System
2. Export
3. Commercial
4. Packing
5. EIA
6. ocean (marine)
7. Airway bill
8. Containerization

9. importer
10. payment
11. Export Order
12. Scrutiny
13. Receipt
14. Sight
15. Delivery

Notes

1.11 Further Readings



Books

Aseem Kumar, *Export and Import Management*, Excel books, 2007.

Dr. Ram Singh, *International Trade Operations*, Excel books, 2009.

Pradeep Kumar Sinha and Sanchari Sinha, *International Business Management: A global perspective*, Excel books, 2008.



Online links

<http://www.slideshare.net/dassanjit23/export-procedureanddocumentation-10107667>

<http://www.indianindustry.com/trade-information/documents-required.html>

<http://superindian.net/NewsArticleDetail177.htm>

Unit 2: Methods of Payment and Incoterms

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Objectives

Introduction

2.1 Methods and Instruments of Payment in International Trade

2.2 Incoterms

2.3 Summary

2.4 Keywords

2.5 Review Questions

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Objectives

After studying this unit, you will be able to:

- Describe methods of payment
- Describe financing exporters
- Explain financing importers
- Know instruments of payment
- Understand Incoterms

Introduction

For successfully conducting international trade in the today's competitive international environment, it has become essential for the exporters to offer attractive terms of sales and payments to importers in order to woo them against other competitors. One of the major concerns that an exporter has to take care of is that he has to choose an appropriate payment method in order to minimize his risks related to the payments of trade transaction. This is essentially to be done understanding the whole economic environment of importers country, importer creditworthiness and to certain extent accommodating the needs of the importer.

Table 2.1: Factors to be considered for Choosing Payment Terms

Factor	Require Letter of Credit	Consider Documentary Collection Against Payment	Consider Open Account
Type Of the Customer	Undetermined	Acceptable	Excellent
Relationship	New	Established	Established
Economic Stability	Unstable	Stable	Very Stable
Type of Order	Custom	Regular Production	In Stock
Transaction Size	Large	Moderate	Small
Cash Flow	Always	Never	Never

Source: John Michael Pierobon, *How to Succeed in International Business*.

The exporter can choose any mode of payments depending on risk perception, size of deal, importer creditworthiness and importer's country economic situation.

Notes

In case of domestic business, a major factor that drives salesman decision criteria for realization of payments is based on the buyer's ability, willingness and honesty to make payment coupled with the exporter's trust on buyer. Usually, sales made in the domestic market are on open account and in certain cases, can be on cash in advance. Such methods of payment to be used in domestic market also depend on buyers and seller power to negotiate and the nature of competition. For instance, monopoly conditions will favour the seller; and perfect competition will favour the buyers. However, in case of international trade, the exporter has to take more precautions, as some of the methods of payments used are unique and used usually in case of international trade only. There are five basic methods of receiving payments from the importers in international trade. In addition to these five, new adaptations in mode of payments have evolved in today's liberalised era, such as sales on consignment basis and electronic sales. The various methods of payment have been ranked in order of being most secure for the exporter to the least secure and vice versa for importer. The basic methods of payment are:

1. Cash in Advance
2. Letter of Credit
3. Document against Payments

Table 2.2: Summarisation of Payment Methods

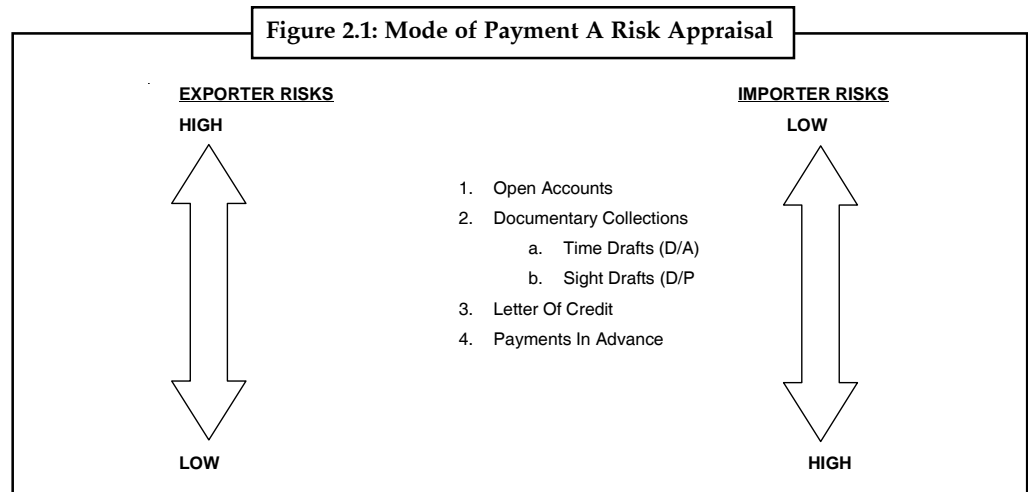
	Payment in Advance	Documentary Credit	Documentary Collection	Open Account
Bank Charges	Lowest	Highest	Medium	Lowest
Payment Risk	Exporter has concerns over the ability and willingness of importer to pay.	Payment is guaranteed by issuing bank if terms of credit are met.	Payment risk unchanged but mitigated by control over the goods.	Exporter is comfortable with the reliability of the importer to pay.
Country Risk	High Exporter requires payment before shipment.	High Exporter requires assurance of a confirmation from a bank in a low risk country.	Medium Exporter mitigates risk by using the banking system to retain control over the goods by holding on to title documents.	Low Open account does not mitigate country risk in any way.
Credit Facilities	Not required	Required	Not required	Not required
Cash Flow	Importer has a good cash position. Exporter needs cash as early as possible.	Importer wants to delay cash outflow. Exporter's cash flow must be able to support the delay.	Importer wants to delay cash outflow. Exporter's cash flow must be able to support the delay.	Importer wants to delay cash outflow. Exporter's cash flow must be able to support the delay.
Price	Importer may be able to negotiate a discount.	Price may be lower in exchange for added security of bank guarantee.	Effect on price depends on terms of collection.	Importer may pay a premium for supplier credit.

Source: www.indianindustry.com

Notes

4. Documents against Acceptance
5. Open Account
6. Other Payment Methods used in the LPG&M era

In a changing scenario in today's era, while choosing any mode of payment, the exporter has to assess not only the risks, but also the degree of risk and where this risk essentially lies. If he is successful in assessing and appraising the quantum and location of risk he can essentially reduce his risk by using alternate modes of payment. For example, if the exporter feels that the importer does not have good creditworthiness he can choose L/C as mode of payment whereby the onus of payment will be on L/C issuing bank rather than on importer, as getting paid in full and on time is of utmost concern for any exporter. The exporter can take the help of international bankers, Export Credit Guarantee Corporation and other credit ranking agencies such as D&B for appraising, assessing and analysing the degree and location of risks involved in a specific trade transaction. The Figure as given below can be of some help for a first time exporter in assessing risk and choosing the method of payment for the trade deal.



Source: Trade Finance Guide, US Department of Commerce

2.1 Methods and Instruments of Payment in International Trade

The following is a detailed elaboration of basic and other methods of payments, which has evolved in today's liberalised era in international trade for realisation of export proceeds from the importer.

2.1.1 Cash-in-Advance

Cash-in-advance is the most safe and secure mode of realization of export proceeds for an exporter as he receives payments for trade deals before the shipment of goods from his country. Using this method of payment, exporter not only can avoid the credit risk involved in the trade deal but actually would have received payments well in advance before the actual transfer to title of ownership of goods in favour of the importer. Payment in advance can be availed of by several ways and; in the modern era, wire transfers and credit cards are the most commonly used cash-in-advance method of payment to exporters. Some major reasons for using wire transfers and credit cards are that the exporter is relieved from all problems that may occur during the process of collection and can immediately use the funds for his business purposes, which is not possible in other modes of advance payment such as, payment by

cheque, which may have been received by the exporter even before shipment, but may result in a collection delay of four to six weeks and therefore frustrate the original intention of payment before shipment. Those exporters; who insist that they would trade only on the basis of this method of payment may lose their foreign buyers to competitors who may be willing to offer more attractive payment terms to the importer for that deal. Cash-in-Advance is most desirable, safe and acceptable for any exporter as this mode of payment is most suitable and secure for him.

However, this mode of payment is not safe and secure for importers as they are at risk of making payment and not having the delivery of goods hence this option of payment is the least attractive option for the importers. This method of payment may have cash flow problems for importers and they are at the mercy of exporter who may even not send the goods to importer. This mode of payment has largely been used in cases where the exporter has sole monopoly in the market and the importer is in dire need of those goods. Presently this method is largely used by teleshopping and Internet-based firms, which demand money in advance for sending goods to buyers. Some popular means for realizing cash-in-advance are tabled as follows:

Table 2.3: Popular means for Realizing Cash-in-Advance

Factor	Wire Transfer	Credit Card	Payment by Check
Cost	Costly for the importer as the cost of remitting funds through wire transfers has to be borne by him	Cost effective method for small transactions	A little costly as the collection charges will be deducted by the collecting bank
Time	Takes least time, in ideal cases as little as 16 seconds from one country to another.	Takes least time and avail the funds to exporter well before the shipment.	Takes time in collection of international cheques, usually 4 to 6 weeks
Safety	Most safe mode of fund transfer	Fraudulent use is possible as the mode of transfer is via online, telephone, or fax methods. Precautions required.	Safe, but exporter has to check the whereabouts of the bank, as fake banks are common in LDC countries.
Ease in use	Very easy to use for large transactions	Easy to use	Requires some efforts at the end of exporter to deposit the cheque through the collecting bank
How it works	Through SWIFT ⁴ System	Through Online, Fax and via telephone.	Collecting bank sends the cheque to importer's bank for transmittals of funds. Lengthy process as compared to other modes.

Key Features of Cash-in-Advance

Some key considerations for any trader, while selecting this method of payment, are:

1. This method is effective in cases where the importer's credit worthiness cannot be ascertained and verified and the importer is quite new to international trade and is unknown to the exporter.
2. The exporter can use this method in cases when the political and commercial risk of the importer country is very high and banks in the importer's country have very low credit ranking and suffer from poor and corrupt regulatory environment.
3. Under Cash-in-Advance method of payment, the exporter will have full or significant partial payment for the trade deal usually through Credit Card/Wire Transfer/

Notes

International Cheque and such payment shall be before the actual transfer of ownership of the goods to the importer.

4. Cash-in-Advance through wire transfer, is one of the safest, most attractive and favourable methods of international trading for exporters and as a result; the least secure and unattractive option for importers.
5. The exporter should avoid the Cash-in-Advance method through the international cheque as time required in international collection of cheques is four to six weeks. This may frustrate the original intention of the exporter of realizing payment in advance and using the money for other purposes.
6. Trading under such mode of payment may result in losing important buyers to competitors as they may offer more favourable and attractive option of payment to importer in today's globally competitive market.
7. Importers are usually not interested in such mode of payments as it reduces their chances of greater cash utilization under other modes of payment, such as open account and documents against acceptance. The importer will use this method only in cases of dire requirement of goods and if the exporter has monopoly on that market.

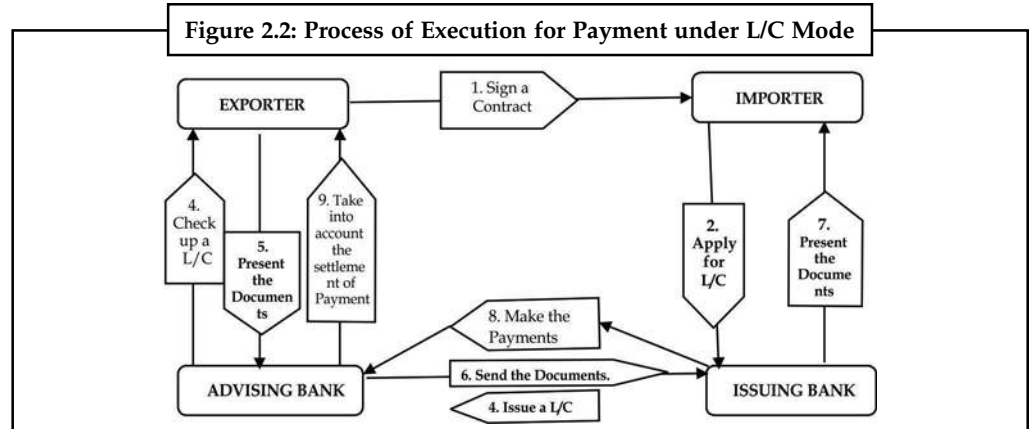


Note Cash-in-Advance method is useful in case of high risk trade relationship and is ideal for teleshopping and Internet-based business.

2.1.2 Letters of Credit

In today's scenario, the letters of credit (LCs) are considered to be among the safest and most secure mode for payment available to the exporter and the importer for trade deals. A Letter of Credit is a commitment by the L/C issuing bank on behalf of the importer that payment will be made to the exporter subject to the fulfilment of the terms and conditions that have been agreed upon between the exporter and importer in the letter of credit. The exporter has to submit the trade documents as agreed in Letter of Credit through his collecting bank to issuing bank for the fulfilment of contract of payments. The issuing bank, upon verification of documents, if satisfied with the documents as submitted by exporter for fulfilment of terms and conditions, is bound to release the payment to the exporter.

The importer has to pay some fees with a request to issue a letter of credit in favour of the exporter. Letter of credit is a reliable and secure mode of payments in case the exporter is unable



Source: International Trade Operations by Dr. Ram Singh

to ascertain the creditworthiness and solvency condition of the importer, as under the letter of credit, the onus of payment shifts from the importer to the issuing bank. Letter of credit is also a safe and secure mode for payment for importer, as he is obliged to make the payment only after the shipment of cargo by the exporter. The process of letter of credit works as shown in the Figure 2.2.

Notes

Parties, Process and Papers in Letter of Credit Transaction

We can understand the process under the documentary credit under the following points detailed as under for a better understanding:

1. **The beginning::** Once the exporter and importer have agreed on the terms of a trade deal, the importer arranges for his bank to open a letter of credit in favour of the exporter.
2. **The issuing bank:** The issuing bank, upon the request of importer issues the letter of credit in favour of exporter therefore enters into a separate contract for making the payment to exporter on the fulfilment of the terms and conditions of L/C contract irrespective of fulfilment of export sales contract.
3. **Letter of credit:** A letter of credit is a contract, whereby the issuing bank makes a promise of the payment to the exporter on behalf of the importer, provided the exporter should comply with all the terms and conditions as laid down in the letter of credit.
4. **The beneficiary:** The exporter, also known as the beneficiary, reviews the terms and conditions of the letter of credit and after manufacturing the goods and arranges with the freight forwarder to deliver the goods to the appropriate port or airport for transporting the cargo to the importer's country. Once the cargo is loaded, the exporter's freight forwarder completes all the necessary trade documents and presents them for confirming/ advising (as the case may be) indicating full compliance.
5. **Advising bank:** The exporter's bank, which corresponds with the issuing banks with all trade documents for release of payment on behalf of beneficiary, i.e. exporter. The advising bank is also referred to as the corresponding bank.
6. **The confirming bank:** The exporter, in order to avoid any kind of risks involved in negotiation process or default of importer bank or importer country economic or political problems used to get their L/C confirmed from a local bank. Such a bank is known as the confirming bank and adds its promise to make payment of the trade deal to the exporter, irrespective of any problems that may come in the way of realization of export proceeds.
7. **The trade documents:** The basis of letter of credit as the payment under a documentary letter of credit is based on trade documents and not on the terms of sale or the conditions of the goods sold. While making payment, the issuing bank verifies that all trade documents are exactly the same as required in the letter of credit. If the trade documents are not as required, a discrepancy exists in negotiation process of L/C, which has to be rectified by the exporter or his bank for realization of the exports proceeds. Hence the full compliance of the trade documents is mandatory for the release of payment under L/C.

The world is not free of corrupt people, systems, flawed regulatory frameworks and weak economic institutions, resulting in all kind of frauds, cheating and thuggishness in case of trade deals as well. Some unscrupulous trader may use the letter of credit as an instrument for defrauding other and some experts may also exploit the same to create discrepancies to deny payments to exporters. In this era of globalisation; it has been seen that LCs are prone to discrepancies. Therefore, they should be prepared by well-trained documenters or alternatively, such functions should be outsourced. Discrepant trade documents accompanying a letter of credit, which may have "I-dot and T-cross"; can negate payment of export proceeds to an exporter.

Notes



Did u know? A letter of credit can be either irrevocable or revocable. A revocable letter of credit is inadvisable and has no value for an exporter, as the importer can at any time, cancel the order or alter the terms and conditions of the contract. A letter of credit can be at sight, meaning that the issuing bank has to make the payments on the presentation of trade documents, or it can be a time or date letter of credit, which means that the payment has to be made at a future date as agreed between exporter and importer.

Table 2.4: Tips for a Letter of Credit Transaction

Precautions to be taken on receiving the letter of credit	Precautions to be taken after shipment of goods in the letter of credit
<ul style="list-style-type: none"> a. Is the letter of credit irrevocable? b. Is the letter of credit at sight? c. Do you trust the paying bank? d. Can you convert the currency to your currency? e. Are the value and quantities correct? f. Are the shipping terms correct? g. Can you provide the required documents? h. Are the letter of credit fees as you had agreed? i. Is the merchandise correctly described? j. Is there sufficient time to meet the shipping date and expiration date? k. Are the shipping terms correct? l. Specify which documents that are required for payment 	<ul style="list-style-type: none"> a. Presenting documents late, after the letter of credit has expired. b. Shipping their goods after the specified date. c. Making a partial shipment when partial shipment is not allowed. d. Not presenting the proper documents. e. Not legalizing the documents. f. Not obtaining completed bills of lading. g. Not obtaining required insurance. h. Submitting copies instead of originals. i. Spelling mistakes. j. Mathematical mistakes.

Source: John Michael Pierobon, *How to Succeed in International Business*.

Sometimes, changes have to be made in the letter of credit after it has been issued. Such changes are called amendments in L/C. The issuing banks levy charges for making any amendments in the letter of credit, which have to be paid by either party depending on the reasons and the request of either side for such an amendment. It is advisable that it must be made clear while framing the terms and conditions of the letter of credit as to which party will bear the cost for such changes to be incorporated in the L/C since the transactional charges for such changes are very high in today's times.

The exporter may experience some delay in receiving payments as funds are first remitted to advising/confirming bank and then transferred to exporter account by the advising bank. For prompt payment, it is advisable that wire transfers shall be used as discussed above, as it is safe, most secure and the least costly and time-consuming method of receiving payments in international trade. The exporter must consult an intentional banker for ensuring timely release of payments as other methods such as discounting of L/C to the bank may increase the exporter's overall transactional cost and make the L/C unattractive as a mode of payment in international trade deals.

Types of Letter of Credit

The following are the types of letter of credit:

1. **Revocable L/C:** A revocable letter of credit is one that can be amended, altered and cancelled at any point of time by the importer without seeking the prior consent of the exporter of submission of documents to the issuing bank by exporter. A revocable L/C is not a safe

and secure mode for payment realization for the exporter and is rarely used in international trade.

2. **Irrevocable L/C:** An irrevocable letter of credit cannot be amended, altered and cancelled by either party of the trade deal without seeking the consent of the other party. In the UCP600, as applicable from July 1, 2007, all letters of credit are irrevocable unless otherwise specified and stated in the L/C. An irrevocable Letter of Credit is quite safe and secure as the issuing bank gives a contractual undertaking to the exporter for making payments, subject to the fulfilment of terms and conditions of the letter of credit.
3. **Unconfirmed L/C:** An unconfirmed letter of credit is one that is forwarded by the advising bank directly to the exporter. Under such letter of credit, the exporter bank does not undertake or commit itself for making payment to the exporter at a future date, but ensures that L/C is authentic and exporter can enter into this trade deal.
4. **Confirmed L/C:** A confirmed letter of credit is one in which the advising bank undertakes and confirms that payment will be made to the exporter provided trade documents are not discrepant and presented accordingly to confirming bank. Such L/C covers the risk of default and insolvency of issuing bank or the unforeseen political conditions in the importer's country, such as restrictions on outflow of foreign exchange, inconvertibility, etc. The confirming bank will impose additional charges for confirming a letter of credit and such charges have to be paid by the exporter, which can be between 2% to 10% depending on the ranking of bank and the importer country's economic and political stability. The confirmed L/C is one of most secure and safest modes of payment in international trade.
5. **Special or Stand by Letters of Credit:** Special or Stand by letters of credit are governed by ISP98 International Stand by Practices of the International Chamber of Commerce and are used as support in cases when a less secure mode of payment has been agreed between the exporter and importer. If the exporter does not receive the payments from the importer under the agreed mode, he can claim payment under the special or standby letter of credit.

Some documents are required for requesting the payment under the Stand by Letter of Credit:

- (a) The original standby letter of credit;
- (b) The sight draft for the amount due from importer;
- (c) The copy of the unpaid invoice;
- (d) The proof of dispatch of goods such as bill of lading and
- (e) A signed declaration from the beneficiary stating that payment has not been received by the due date and therefore reimbursement is claimed by letter of credit.

Post-liberalisation of trade, Special or Stand by Letter of Credit are not very attractive as the transaction cost is high for processing the payment through Special or Stand by Letter of Credit.

6. **Revolving Letter of Credit:** Revolving Letter of Credit is popular among regular traders; dealing in the same nature of goods and services round the year. This type of letter of credit is advisable for those traders who deal in the same product round the year. They need not request, process and understand the terms and conditions of L/C each time as under the revolving L/C; the credit limit will be reinstated automatically for further regular shipments until the credit is fully drawn. Revolving L/C can be framed either on the time basis or on value basis. The most important feature of this type of L/C is that it reduces the time and transaction cost involved in opening amending the L/C and processing

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the documents. Some special arrangements in terms and conditions have to be ingrained for availing of revolving credit.

7. **Transferable Letter of Credit:** The transferable Letter of Credit is popular when there are middlemen or agents involved in a trade deal, as under this types of L/C, the exporter has the right to request the confirming or negotiating bank to make a part of payments in favour of agent or middleman or any other third party involved in trade transactions. The exporter can also extend such facility to raw material suppliers in case the major component of goods input cost comes from a particular supplier.
8. **Back-to-Back Letter of Credit:** The trade deals in the present scenario may involve suppliers from many countries and therefore transferring the part of payment is not a practical and workable proposition under transferable letter of credit. Hence traders can request to bank to open a back-to-back letter of credit in favour of supplier on the basis on letter of credit, which the exporter has received. Under back-to-back Letter of Credit, the original letter of credit is used as security to establish a second letter of credit (B2B L/C) drawn in favour of supplier of inputs or raw materials. The risk exposure is very high under such types of letter of credit hence banks are usually reluctant to open such types of L/C in today's trade environment.
9. **Inland Letter of Credit:** The Inland Letter of Credit is popular among merchant traders who procure material from manufacturers and export it to overseas markets. The original manufacturer may demand such type of letter of credit, as he has to ensure pre-shipment finances under liberal interest rate as specified by the RBI. Such manufacturer, who in turn becomes a deemed exporter, will also wish to avail of other export incentives and benefits and hence may request for Inland Letter of Credit. Such Letter of Credit is becoming popular in India as the units situated in SEZ/EHTP/BTP/STPI/EOU are opening such credit in favour of their local suppliers. An importer willing to procure plants and machinery under the EPCG scheme can also open an Inland Letter of Credit in favour of local suppliers of plant and machinery, if such plants and machinery are locally purchased.

There can be two types of documentary collection payments, which are detailed as under:

1. **Documents against Acceptance:** In a competitive international environment, the exporter sometimes has to extend the credit to the importer to win buyers and penetrate new markets. Such a payment option is also known as Time Draft, as payment is due on the importer and will be made on a mutually agreed future date, usually 30 to 90 days. Such extension of credit helps the importer sell these goods in local markets and make payments. The importer, under this method, is obligated to make payment to the exporter but can default or deny making the payment to exporter. Therefore, this is a risky payment option for the exporter and has to be used after thoroughly verifying and cross-checking the creditworthiness of importer and his country's economic and political situation.

The exporter can smartly use this payment option by insuring the credit risk or by using the factoring or forfaiting services. He can also sell his draft to a bank on discount and thus the risk of non-payment is shifted to the bank. The exporter can also cover his risk to a certain extent by using a Date Draft. A date draft is slightly different from a time draft, as it prevents the importer to delay the acceptance of draft and release of payment.

2. **Documents against Payment:** This is best payment option as such payment term can be acceptable to both the parties in international trade transactions because under this payment mode, the exporter retains the title to the shipment until the cargo has reached the importer's country and payment for the same has been made. The importer is also assured, as he will make payment when the goods arrive in his country. Therefore, the degree of various risks is minimal to both the parties. The collecting bank, on receiving the trade documents

from exporter remitting bank, informs the importer, who is supposed to make payment in exchange for trade documents. The collecting bank remits the payment to the remitting bank, which in turn transfers the funds to the exporter's account. However, this payment option can be used effectively only when an original, clean bill of lading is used, because the bill of lading carries the title of goods and importer must endorse the bill of lading and surrender it to the shipping company for receiving the goods. This payment option can be risky for the exporter when the airway bills are presented for receiving payments, as the airways bill does not carry the title of goods.

Some degree of risks remain even in documents against payments as the importer may change his mind or become insolvent or may be unable and unwilling to make the payment as his creditworthiness has suffered from the time when the cargo was shipped, and trade documents along with drafts are presented for payment by the exporter bank. The trade policies of the importer country may also change resulting in a ban or restriction on export and import of that item or on outflow of foreign exchange from the country. The exporter shall consult his international banker before entering into such payment option for an international trade transaction.

Table 2.5: Key Features of Documents against Payments and Documents against acceptance

Assessment Factor	Documents Against Payments	Documents Against Acceptance
Time of Payment	After shipment, but before documents are released	On maturity of draft at a specified future date
Transfer of Goods	After payment is made on sight	Before payment, but upon acceptance of draft
Exporter Risk	If draft is unpaid, goods may need to be disposed	Has no control of goods and may not get paid at due date

Source: International Trade Operations by Dr. Ram Singh



Task You are required to write a letter to your Banker for opening letter of credit for importing capital goods worth \$90,000 from XYZ Ltd.

2.1.3 Open Account

The most risky mode of payment for any exporter as an open account trade transaction means that the goods or services are shipped or transported and delivered to the importer on credit basis and payment will come after the due date, usually 30 to 90 days. Under this mode of payment, the exporter simply bills the importer and the latter is expected to make payment under agreed terms and conditions at a future date. Hence, this is the most advantageous proposition to any importer as he can sell the goods in local market during the credit period and then make payment to the exporter. The importer has both cash flow as well as cost-advantage under this mode of payment.

Competition is acute in export markets in today's business environment and many suppliers are chasing the same markets and same buyers, making it a buyers' markets in many areas of international trade activity. Importers can exploit such a situation for their benefit by dictating payment terms for supply of goods or services to exporters. This method of payment can be smartly used if the exporter covers his risk through credit risks schemes of ECGC or factoring services. Trade enthusiastic nations today are motivating their exporters for such risks as they want to win new unexplored markets by giving them insurance cover for payments, as this

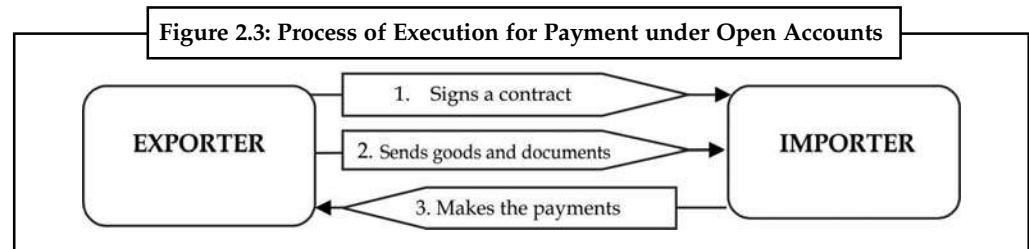
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mode of payment enhances the export competitiveness of a nation in a cutthroat competitive environment in international markets.



Example: Chinese exporters are using this method with active state support for winning buyers in the African continent.

As this is a most risky payment option for any exporter, he must thoroughly analyse, appraise and assess the quantum and degree of political, economic, and commercial risks involved and history of past payment record of the importer as well economic and political stability of the importer country. This mode can be effectively used with those countries where people are enthusiastic about trade and wish to be counted in international markets, like the Germans, Japanese and Italians. It has also been seen that cultural influences have an important bearing in making payments on time and in full.



If the buyers are of sound creditworthiness and have a strong proven history of making payment, this can be a satisfactory mode of payment as it involves least cost in ensuring payments. In fact, many large organizations are using this mode as they have demonstrated long and favourable payment record with their buyers and have thoroughly cross-checked the creditworthiness of the importer.



Note This mode of payment has to be used smartly, as this is a very risky proposition for any exporter as the absence of trade documents and banking channels as an evidence of trade deal may make it very difficult for the exporter to pursue legal enforcement for payment against the exporter.

The exporter has to pursue the claim for payment at the individual level, which is a very lengthy, costly, time-consuming and difficult process in a complex international economic and legal environment spanning two countries. Exporters may also have problems with regard to pre-shipment financing of trade transaction as the receivables under such risky payment terms are usually not financed by the bank, or are financed at high interest rates. Hence it is advisable that exporters should properly and patiently verify and cross-check the political, economic, and commercial risks involved in deal with importer and his country and are advised to consult their international bankers before accepting any such kind of payment option.

Key Features of Open Account Method

1. Such a payment option can be used in safe and secure trade partnerships with importers with whom the exporter has very good trade relations for a long period of time. Such markets are also stable politically and economically, along with having a strong regulatory and legal framework.
2. Such a payment mode, although offering a competitive and hawkish strategy on the part of exporter to win new markets, also has significant exposure to non-payment risk and some additional cost for insuring such risk under this payment mode.

3. Under this payment mode, goods are shipped directly to the exporter along with the required trade documents and the exporter expects that the importer would make the payment on the agreed date; which can be 30 days to 90 days.
4. Such a mode of payment can be effectively used if the exporter smartly uses this mode with export credit insurance, export factoring and forfaiting and keeps in touch with his bankers, the importer and his country's economic and political situation.

Self Assessment

Fill in the blanks:

1. A letter of credit is one in which the advising bank undertakes and confirms that payment will be made to the exporter provided trade documents are not discrepant and presented accordingly to confirming bank.
2. The Inland Letter of Credit is popular among traders who procure material from manufacturers and export it to overseas markets.
3. under cash-in-advance mode of payment may result in losing important buyers to competitors as they may offer more favourable and attractive option of payment to importer in today's globally competitive market.
4. The drawee is basically the party whothe money or agrees to make the payment and to whom the draft is addressed or made out.
5. An irrevocable letter of creditbe amended, altered and cancelled by either party of the trade deal without seeking the consent of the other party.
6. Anletter of credit is one that is forwarded by the advising bank directly to the exporter.
7.is the safest and secure mode of realization of export proceeds for an exporter as he receives payments for trade deals before the shipment of goods from his country.
8.is the most risky mode of payment for any exporter as an open account trade transaction means that the goods or services are shipped and delivered to the importer on credit basis and payment will come after the due date, usually 30 to 90 days.
9. The is the bank of the importer and facilitates in trade transaction by getting the documents for the bank i.e. remitting bank.
10.are used as support in cases when a less secure mode of payment has been agreed between the exporter and importer.

2.2 INCOTERMS

The distinctive feature of export pricing is that it is based on Inco terms; also referred to as terms of delivery, as they demarcate the functional activities to be performed by the exporter and importer such as getting insurance cover, reserving shipping space, customs and excise clearance. It helps the exporter and importer to divide the individual responsibilities and obligations of the trade deal.

International Commercial Terms, briefly known as Inco terms, are an integral part of any export-import transactions between exporter and importer. Through Inco terms, the responsibilities and obligation of both the exporter and importer become clear and both can

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take necessary precautions to minimize their risks associated with particular trade transactions through careful planning and execution.

The major function performed by Incoterms is to clarify that costs and risks are split between the exporter or consignor and importer or consignee in a mutually agreed manner by providing the clarity of financial implications involved in trade deal to both the parties and the same shall be included in international sales contract to provide it a legal sanctity for future purposes.



Did u know? The process for evaluation of such incoterms dates back to 1936 when the International Chamber of Commerce conceived the first version of Incoterms for facilitating international trade. Since then, there have been six revisions of Incoterms and the current version being used is Incoterms 2000, revised, updated and published in year 2000. Such revision and updating has taken place in 1953, 1967, 1976, 1980, 1990 and the current version is 2000. The current version of Incoterms has come into force on 1 January 2000.

2.2.1 Purpose and Scope of Incoterms

The main purposes served by incoterms are:

1. **Clarity in interpretation of trade terms and rules:** Incoterms are globally recognized and their interpretation provides an important understanding to the trader intending to get started in international trade in this era of liberalisation, globalisation, privatisation and marketisation. Both the exporter and importer are clear about their responsibilities and obligations with regard to international trade transactions and know the financial implications of the trade deal.
2. **Minimisation of losses:** Due to the clarity provided by the Incoterms, international trade disputes are fewer. It also reduces the transactional cost of international trade, providing a well-defined mechanism of the responsibilities and obligations. Uncertainties due to different interpretations of such trade terms in various countries can be avoided or can be reduced by considerable degree by use of incoterms.
3. **Base of contract of sale:** Incoterms used in trade deal are the base of that deal. Although; some people misinterpret it as the base of contract of carriage only but incoterms have wider connotations with regards to various aspects of trade deals. Their scope is not limited only to clarify the responsibilities and obligations with respect to carriage or transport of goods. They help in not only deciding the export price to be offered in quotation but also in explaining other responsibilities and obligations of exporters and importers with regard to arrangement of insurance, mode of shipment, customs and excise clearance, payments of duties, etc. This is the main reason that the International Chamber of Commerce has clearly underlined and explained that incoterms deal with the relationship between the exporter and importer in contract of sales and that too in a very distinct manner.

Incoterms being the base of international sales contract; also help in contracts of carriage for delivering the goods to the buyers, arranging the insurance for goods and financing for the exporter. Banks calculate the finances (working capital) required for manufacturing the goods for trade deal and exclude the amount to be used on transportation, insurance, duty payment, etc. as incoterms such as DDP may have higher export price quotation due to various duties and obligations to be performed by the exporter.

4. **Documentary evidence:** Let us assume the exporter and importer have agreed to the use of CFR or CIF-based international sales contract. The exporter has problem in sending the goods via any other means of transport except by ocean transport. If the exporter sends

goods by any other method of transport, he will have problem producing the bill of lading, which is possible only in case of ocean transport. The bill of lading carries the title of goods, which is not possible in any other documents being used in other means of transport such as Airway Bill; Combined Transport Document; Multimodal Transport Document and Customs Transit Challan. It is well-known that the document carrying the title of goods is preferred for documentary collections (D/A and D/P) and payment under Letter of Credit.

5. **A solid base to the contract:** As incoterms provide a solid base to contract execution in international trade transactions, domestic traders, in case of large-scale contract, also use the same, as incoterms are very clear and specific in differentiating the responsibilities of seller and buyer. The reasons of increased use of incoterms in purely domestic transactions are only because of the larger clarity provided by them in exercise of role and responsibilities of seller and buyer. That is why some people have rightly referred to incoterms as incoterms.

2.2.2 Need of Revisions of Incoterms

There have been questions why incoterms have been revised so many times. The answer is very simple because the successive revisions and editions of incoterms have provided an opportunity to adapt them to the ever changing and emerging business and commercial practices in an era of liberalisation and globalisation. The revision; which took place in 1980 introduced another incoterms as Free Carrier (FCA) in order to deal with problems such as receiving goods from Land Customs Station, Inland Container Depo, and Container Freight Station, which was not possible under incoterms FOB as being traditionally used. Such new incoterms were the need of time and were demanded by the trading community, as manufacturing is no more concentrated around seaports or coastal areas. It may be concentrated deep inside the country requiring the stowing of cargo into a container and transport of cargo to nearby seaport for subsequent carriage through rail or road, or a combination of both. It can be said that Incoterm FCA was introduced to facilitate the transport of goods through combined or multimodal transport of cargo, as the management of logistics as well manufacturing activities has been very complex in today's world.

Beginning in the eighties, paper documenting was replaced by fast, transparent and speedy electronic trade documentation and accordingly, the 1990 revision of incoterm provided some clauses dealing with the exporter obligations to provide proof of delivery of cargo. Such clauses introduced provide the proof of delivery of cargo through electronic mode (EDI) by replacing it with paper documentation. Hence; the electronic mode of communication in a legally accepted manner; has not only reduced the transactional cost in international trade but has also improved the speed of work by reducing the trade cycle. It can be said that the International Chamber of Commerce, through the 1990 revision of Incoterms, has played its role in trade facilitation in the best possible way.

2.2.3 INCOTERMS 2000

The dimensions of trade activities worldwide have changed drastically and there has been a significant expansion of trade and investment under the World Trade Organization. Accordingly, the revision of incoterms that took place in 2000 attracted a huge response from the trading community, shipping companies, insurance companies, banks, freight forwarders and respective government being represented through their customs and excise departments. It was a far more democratic revision as all concerned parties participated actively in the revision process. Some trade facilitating institutions particularly the World Customs Union, United Nations Centre for Electronic Trade Facilitation, United Nations Conference on Trade and Development;

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International Maritime Organization, etc. were also active in interpreting the trade terms during the 2000 revision. All sections of the trading community reflected their views in a manner that led to the actual trading practices and solutions to problems faced by traders being incorporated in Incoterms-2000. The huge response surpassing all previous record of incoterms revisions has made it clear that INCOTERMS enjoy worldwide recognition among trading nations, institutions and above all, among trading parties. The International Chamber of Commerce therefore decided that delivery terms should be tailor-made as expected by the trading community and other stakeholders and emphasis was given to consolidation of Incoterms. The changes that were made and incorporated in 2000 revision of Incoterms are as follows:

1. The procedure for clearance of customs and payment of duties obligations under FAS and DEQ was ensured as requested by trading community.
2. The procedure of the loading and unloading obligations of cargo under FCA was ensured as per trading community requirements.

The very interesting fact is that all such changes have taken place only on the basis of rigorous substantive research among users of incoterms. Hence the 2000 revision of incoterms reflected the most participative, democratic and realistic trade mechanism represented according to the wishes of actual stakeholders in international trade in the liberalised era.

Incorporating INCOTERMS

Incoterms must provide clarity and consistency in the trade transactions, particularly when being incorporated in international sales contracts, used for assigning carriers for transportation of goods and determining the export pricing. For example, if the goods are to be shipped from Kolkata on FOB terms, the exporter shall quote it as FOB Kolkata (Incoterms 2000) everywhere in contract of carriage, international sales contract, marine insurance certificate, commercial invoice, consular invoice, certificate of origin, certificate of inspection, shipment advice, shipping bill or combined transport bill, etc. so as to show consistency and clarity in various documents being used in international trade. Such clarity helps the exporter in realization of payment under D/A, D/P and L/C terms of payments.

The failure on the part of the exporter in incorporating the right version of Incoterm may cause a dispute between the exporter and importer and may lead to a costly process of litigation and arbitration. It is, therefore, advisable that the exporter should particularly take care of such circumstances to avoid ambiguity in international trade deals.

Various Types of INCOTERMS

As per the ICC revision of incoterms in 2000, there are thirteen types of incoterms and these are divided into four distinct groups as outlined below:

1. **Group E:** Group E Incoterms indicate that the goods shall be made available to the importer at the exporter's premises; for example, at the exporter's factory gate.
2. **Group F:** Group F indicates that the exporter must deliver the goods to a carrier that has been appointed by the importer for carrying the goods to destination.
3. **Group C:** Group C indicates that the exporter is liable for losses and damages only up to the port of shipment and all losses and damages subsequent to exporter delivery of cargo to shipping company and any additional cost or charges, etc. shall be borne by the importer. The exporter accepts the obligation of all risks of losses or damages to the cargo only before the start of the cargo's journey.
4. **Group D:** The Incoterms under Group D indicate that the exporter will be having obligations and responsibility to incur all the costs, charges and other risks that may be

associated in the course of the journey from the exporter country to the importer country. This is most risky trade term for exporter and more beneficial for importer.

Notes

The various types of incoterms are explained as under-outlining of role, responsibilities and obligations of exporter and importer in a trade deal. Immense care is to be taken in the use of these incoterms keeping in mind; which mode of transport/carriage will be suitable for the transportation of the goods to a particular country and region. The various incoterms provide us the opportunity to choose the best one to be incorporated in international sales contract and contract of carriage. The detailed explanation of these incoterms is as follows:

Group 'E'–Departure

1. **EXW - Ex Works (named place) (any mode of transport):** The exporter shall place the goods at the disposal of the importer at the premises or any other named place. Such goods are yet to be cleared for export and are yet to be loaded on any collecting vehicle of the importer, at his expenses. In this way, EXW Incoterms indicate the minimum involvement of risks of losses and damages to the exporter and the maximum involvement of losses and damages to the importer.



Note Under EXW Incoterms; the importer is responsible for all expenses associated with customs duty clearance, insurance, transportation, documentation work, pre-shipment inspection, etc. from the factory, warehouse or premises of exporter to his country.

When EXW is used, exporter should remember that:

- In this case, the export of the goods is not guaranteed, as the importer may sell the goods in India or keep them in warehouses for an indefinite period or can resell the cargo in India to a third party.
- In the cases where the exporter is not a manufacturer-exporter, the actual point of delivery of cargo to the importer may vary from the place where exporter operates his own business.
- In certain cases, it has been seen that exporter may have to load the goods on a truck without charging a loading fee. Although in EXW, payment of loading charges is the duty of the importer.

Group 'F' – Main Carriage not Paid by Seller

1. **FCA – Free Carrier (named place):** In the FCA shipping term, the exporter is under obligation to take responsibility of all risks and costs that are involved in trade transactions and associated with the cargo until the cargo is not delivered to the named place of shipment and the same has to be collected by the carrier nominated by the importer. Under F Group of Incoterms, the responsibility of export customs clearance is on the exporter.

Sometimes, under FCA Incoterms the carrier of cargo may have to collect the goods from the premises of the exporter but he shall bear the cost of delivering the goods up to the point of port of shipment as agreed in the export sales contract. Sometimes, the exporter's premises are the "named place" in the contract. He may have to load the goods onto the truck but the cost of such loading shall be borne by the importer.

2. **FAS – Free Alongside Ship (named port of shipment):** FAS Incoterm was previously known as FOW (Free on Wharf) as per the 1990 version of Incoterms. The exporter is responsible for delivery of cargo to the named port and place alongside the ship under FAS Incoterms. It means that preparing export import documents, getting goods inspected and custom

Notes

clearance of cargo shall be the duty of the exporter and loading of the cargo shall be done on the expenses of importer.

3. **FOB – Free On Board (named port of shipment):** FOB is the most popular term used in international trade and is the most favoured and widely used Incoterms by exporters in today's times. Under this incoterm, the exporter shall be responsible for delivering goods to the named port of shipment from where the journey to the place of destination will begin. Under this incoterms, the exporter is under obligation to prepare export-import documents, getting goods inspected, export customs clearance and loading of cargo on the vessel.



Caution Under these Incoterms the responsibilities of exporter are over once the goods are loaded on the ship and those of the importer begin. Any damages and losses to the cargo, before it is loaded on vessel shall be borne by the exporter.

When the F Terms are used, exporter should remember that:

- Shipping terms such as FAS and FOB are mono-modal and such incoterms are used when the transportation of goods is by sea route only from the country of origin to country of destination. The bill of lading is a prerequisite document to be used during transportation under the FAS and FOB Incoterms. FOB and FAS Incoterms cannot be used on any other type of transport such as air transport, post parcel, railways and road transport of cargo to the destined country.
- The handling, loading, stowage and other port charges of cargo under FOB shall be the responsibility of the exporter. On the other hand under the FCA shipping terms, such charges have to be borne by the importer.

Group 'C' – Main Carriage Paid by Seller

1. **CFR – Cost and Freight (...named port of destination):** Under this incoterm, the exporter is required to cover all costs related to customs clearance of export shipment, delivering the cargo to the named port of destination and discharging the cargo from the ship, including all port charges. However the risks of the exporter shall be limited to loading of cargo on to the ship at the named port of shipment. This incoterm can be used only in case of inland water and seaway transportation of goods. This shipping term was previously known as C&F or CAF under Incoterms 1990.
2. **CIF – Cost, Insurance and Freight (...named port of destination):** The Incoterm CIF is much similar to the shipping term CFR. The only additional responsibility that the exporter has to bear is that he has to arrange the marine insurance of cargo. Usually, the exporter is advised to procure the insurance cover having minimal cost to exporter. All other responsibilities shall remain the same as in case of CFR Incoterm. This incoterm can be used only in case of inland water and seaway transportation of goods.
3. **CPT – Carriage paid to (...name place of destination):** The shipping term refers to the responsibilities of the exporter up to the delivery of the goods at the named Place of Destination, Container Freight Station, Inland Container Depo, Frontier or Terminal or Quay as nominated by the importer in the country of destination.

The exporter shall also be responsible for all inland freight charges in the country of the importer. Under this shipping term, the importer is responsible for all expenses that are related to customs clearance and other duties payable on consignment, taxes and any other costs that are payable in the country of destination. CPT Incoterm is used for multimodal transport.

4. **CIP – Carriage and Insurance Paid to (named place of destination):** The shipping term CIP is much similar to the CPT. The only difference is that insurance of cargo is also responsibility of exporter as in case of CIF. CIP is also used for multimodal transportation of goods.

Notes

Incoterms such as CFR and CIF are mono-modal terms and these can only be used when the main carriage is by either inland water or seaways transport. Such Incoterms cannot be used for landlocked countries such as Nepal or Afghanistan because under these terms the journey has to be by sea/waterways only.

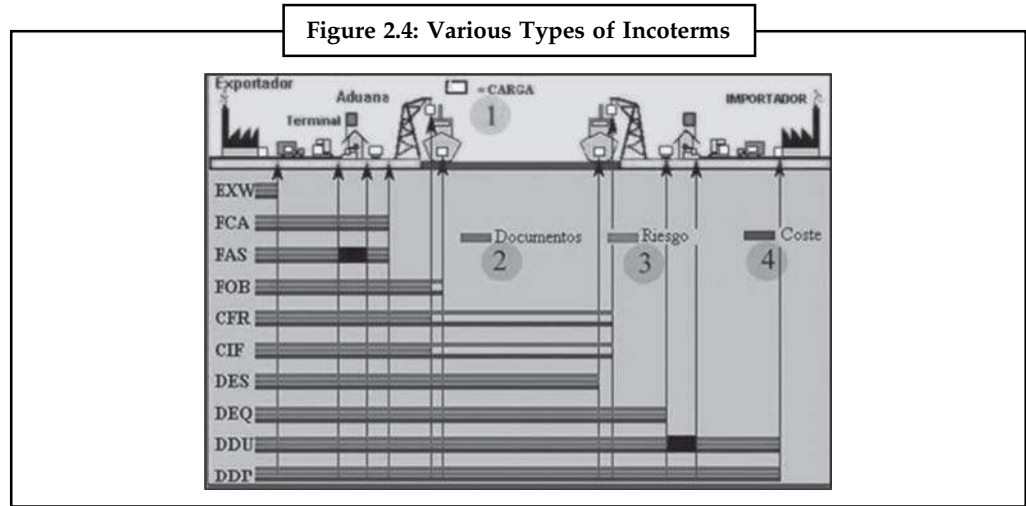
There are two shipping terms under Group C whereby the exporter is under legal obligation to arrange the insurance of cargo. These are CIF and CIP. Under other Incoterms such as CFR and CPT; the arrangement of insurance is an optional responsibility of the exporter and the cost of such insurance has to be borne by the importer of cargo.

Group C incoterms are quite unique from other incoterms because under these terms the point of transfer costs, responsibilities, obligations and risks are precisely segregated between the exporter and importer. In sum, it can be said that under Group C incoterms, the exporter is under responsibility to bear all costs and risks until the goods arrive at the named port or place of destination. Under this Group of incoterms the risks shift from the exporter to the importer at the port of loading at the time of delivery of goods to the carrier for transportation for shipment of cargo to importer's country.

Group 'D' – Arrival

1. **DAF – Delivered At Frontier (...named place):** Incoterm DAF is a mono-modal and can be used for land transportation of goods through road and railways. It simply means that such terms cannot be used for the countries that are surrounded by water or sea and have no inland border with any other countries, such as Australia, New Zealand, Japan and the Maldives.
2. **DES – Delivered Ex Ship (...named port of destination):** The shipping term DES is much similar to CFR in terms of costs and responsibilities involved in transportations of cargo. Under DES shipping terms, the exporter is responsible for all the risks till the goods reach the named port of destination. Under this incoterm, the risk is on the exporter as compared to CFR.
3. **DEQ – Delivered Ex Quay (named port of destination):** Under shipping term DEQ, the exporter is responsible not only for the delivery of the cargo to the named port of destination, but is also under obligation and responsibility to bear the expenses for the unloading of the cargo and placing it on the wharf in the importer country.
4. **DDU – Delivered Duty Unpaid (...named place of destination):** Under DDU shipping term, all the costs and responsibilities involved are much similar to the CPT. The exporter also has to bear all risks until the goods arrive at the named place of destination.
5. **DDP – Delivered Duty Paid (...named place of destination):** Under this incoterm, the exporter has the highest obligations and responsibilities, as he has to bear all the costs and risks involved in delivering the cargo to a named place of destination. Expenditure such as customs clearance, duties and other payments have to be made by exporter in importer's country.

Notes



This is a very risky shipping term as the exporter provides the services till the doors of importer and has to bear all the costs and risks in delivering the goods to the importer in importer's country.

The incoterms DES and DEQ are used in case of mono-modal trade. It is to be noted that such incoterms can be used only in cases where the main carriage for shipment of cargo is by sea freight only.

Applicable Incoterms in Different Modes of Transportation

There are some incoterms that can be used only in case of multi-modal transport and some can be used only in case of land transportation. Some others can be used when the main carriage of transport of goods is by sea or inland water only. International traders should take care which particular incoterm is suitable for conducting the business as such a decision will also be based on the buyer's and seller's bargaining power. Choosing FOB term for a land-locked country such as Turkmenistan will have serious implications for an exporter, as it will be considered as a discrepancy in negotiations of documents while recovering the payment through documentary credit. The table as given below shows the various types of incoterms in relation to the mode of transport to be used for transporting the cargo to the destined country.

Table 2.6: Applicable Incoterms in Different Modes of Transportation

	Air Freight	Road Freight	Rail Freight	Sea Freight
EXW	Y	Y	Y	Y
FCA	Y	Y	Y	Y
FAS				Y
FOB				Y
CFR				Y
CIF				Y
CPT	Y	Y	Y	Y
CIP	Y	Y	Y	Y
DAF		Y	Y	
DES				Y
DEQ				Y
DDU	Y	Y	Y	Y
DDP	Y	Y	Y	Y

Choosing an Incoterm for International Trade Deal

Notes

There are certain precautions to be taken in the use of incoterms.

1. ***Name/place handover along with shipping term:*** The exporter and importer while signing the international sales contract shall take care to mention the name of place; where the goods are to be handed over to the importer or his authorized carriage. For example; if it is a free on board (FOB) incoterm and the place of handover of goods is Bombay; it shall be mentioned as FOB Bombay in the international sales contract. It is to be noted that all incoterms are abbreviated in three letters, to be written in capital letters in the international sales contract.
2. ***Clear mention of incoterms edition:*** The exporter and importer shall also take care regarding the mentioning of a particular edition of incoterms while quoting incoterm in the sales contract and contract of carriage. For example, for FOB incoterms; it shall also be mentioned that it is a 2000 version of incoterms and shall be quoted as FOB 2000 Bombay. As per the International Chamber of Commerce, the “INCOTERMS shall not apply unless the particular edition of a shipping term is not incorporated into the international sales contract by clearly mentioning that this particular shipment is governed by INCOTERMS-2000”.
3. ***Clarity in soul and spirit of incoterms used:*** There has to be clarity in the use of incoterms. For example, if the agreed incoterm is EXW and it was also decided that the exporter shall bear the expenses for the loading of cargo to importer’s carriage/vehicle and the place of loading is Kolkata, it shall be mentioned as “EXW, Kolkata loaded on truck” in the international sales contract, which is to be agreed upon and signed between the exporter and importer. The same shall also be entered in the contract of carriage between contracting parties.
4. ***Understanding the cost, responsibilities and obligations aspects:*** Another important point to be considered is with respect to the cost, obligations and responsibilities of the exporter and importer. For example, the shipping terms CFR and DES have the same point of transfer of cost between the exporter and importer but the fundamental difference to be considered is that CFR is used for the port of shipment and DES is used for Port of Destination. Therefore, the risks, obligations and responsibilities of the exporter shall be higher in case of DES as compared to those of the importer.
5. ***Avoid risky incoterms:*** Some incoterms are very risky for exporters, such as DEQ, DDP, DDU and DES, while others such as EXW, FAS, FCA, are risky for importers. What is required for the exporter and importer is that they should trade-off and chose an incoterm whereby their costs, risks, obligations and responsibilities are distributed in an equitable manner and would be acceptable to both exporter and importer.
6. ***Same incoterm not suitable for each importer:*** The exporter should understand that the same incoterm might not be suitable for each importer. Both exporter and importer need to discuss, appraise and agree, keeping in mind the prevailing circumstances; about the incoterm to be used in the international sales contract for the benefit of both the parties and also reduce the cost involved in trade transactions.
7. ***Understand rules and regulations of importer’s country:*** The exporter should understand the rules and regulations of the importer’s country as some countries in the world have certain laws in place for the use of incoterms. Such countries are usually underdeveloped countries beset with difficulties of foreign exchange and balance of payments. These countries have made it mandatory for their importers to ask the exporter to deliver the goods duty paid. As such countries are trying to control their imports by imposing heavy import duties, controlling the carriage charges to be a part of their policy. The exporter

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has to take care of all such implications involved in the importer country's rules and regulations.

8. **Standard practices of country or region:** Some countries and regions have certain standard incoterm practices in place. For example; many European countries prefer goods to be delivered to the destination country by the exporter. The exporter is at risk under such incoterms practices.
9. **Mode of transport:** Certain incoterms are used for sea transport only and some other for multi-modal transport, including inland transport. The exporter shall take care of such incoterms while incorporating them in the international sales contract or quoting export prices in pro forma invoice.
10. **Avail all information in execution of your obligations and responsibilities:** The exporter must have all the information about the rules and regulations regulating export and import such as what items fall under restricted or prohibited category and then negotiate the incoterms. For example, an exporter has agreed to deliver the goods on DDP terms. Once the goods have arrived in the destination country, the customs department of the importer country may refuse to allow the entry of the goods if those goods fall under the prohibited list and a special license is required to import them. Now, the exporter will be in a problem as the importer does not have a special import license and the former has spent a lot of money on carrying the goods to the importer's country. Thus, all such information pertaining to the use of incoterms must be collected and analysed first-hand by the exporter himself.
11. **Offering competitive incoterms for retaining satisfied importers:** The exporter should choose incoterm that offer the most competitive price to the importer. He should consult the importer and enquire what kind of incoterms would be convenient to retain satisfied importers. It would be wrong and unwise on the part of an exporter to offer the easiest terms at his own end to the importer, because it may not be suitable for his importer. It is well said that "if customer is a king then pricing is a queen". Just like a king is attracted towards a queen, an importer too looks for affordable and suitable prices and the product to be delivered at his convenience. Studying the concept of market mix whereby producer takes care of four Ps – Product Price, Place, Promotion through customer choice expressed as Customer Solution for product, Cost for Price, Convenience for Place and Communication for Promotion can be an eye-opener for an exporter in choosing competitive incoterms and retaining satisfied importers.



Task Why was there a need for the revision of Incoterms?

Self Assessment

Fill in the blanks:

11.helps the exporter and importer to divide the individual responsibilities and obligations of the trade deal.
12. Incoterms must provide clarity andin the trade transactions, particularly when being incorporated in international sales contracts
13. Incoterms indicate that the goods shall be made available to the importer at the exporter's premises.

14. In theshipping term, the exporter is under obligation to take responsibility of all risks and costs that are involved in trade transactions and associated with the cargo until the cargo is not delivered
15. The incotermsand DEQ are used in case of mono-modal trade.

Notes

2.3 Summary

- Special procedures have evolved for dealing with extra risks of international trade and national and international institutions have been established to finance and regulate international trade.
- Before shipping goods to foreign buyers, many exporters require a letter of credit from a reputable bank. This is a guarantee that the exporter will be paid if the goods are supplied in good order.
- Payment is made by a bill of exchange, or draft, which is sent by the exporter to the importer or to the importer's bank. The importer or importer's bank signs the draft. If the draft is payable on presentation, it is a sight draft. If it is payable at a future date, it is a time draft.
- The shipper gives the exporter a bill of lading, the original copy of which is required for collection of the goods. The bill of lading is forwarded to the importer for the goods to be released.
- When an exporter is confident an importer will pay, goods may be sold on an open account, and a bill presented after shipment. When an exporter suspects that the importer may not pay, cash may be demanded before shipment occurs.
- When an exporter lacks trust in the importer's bank or country, the exporter can have the importer's letter of credit confirmed. A confirmed letter of credit is one way of avoiding country risk.
- Export credit insurance is an alternative to letters of credit for avoiding commercial and/or country risks. Export insurance, however, typically involves a deductible portion of coverage and differs from letters of credit in other ways that are sometimes important.
- Official export financing agencies often provide direct buyer credits, as well as guarantees on credits to buyers granted by domestic or financial institutions.
- When an exporter's time draft is accepted by the bank, the resulting accepted draft is called a banker's acceptance.
- Bankers acceptance are a means of short-term trade financing typically up to 6 months.
- The majority of trade occurs between countries which are members of customs unions or free-trade agreements

2.4 Keywords

Bill of Exchange: An order written by an exporter instructing an importer, or an importer's agent, to pay a specified amount of money at a specified time.

Bill of Lading (or draft): A document issued to an exporter by a common carrier transporting merchandise. It serves as a receipt, a contract, and a document of title.

Export-Import Bank (EXIM Bank): Agency of the Central Govt. whose mission is to provide aid in financing and facilitate exports and imports.

Notes

Letter of Credit: Issued by a bank, indicating that the bank will make payment under special circumstances.

Sight Draft: A draft payable on presentation to the drawee.

Time Draft: A promise to pay by the accepting party at some future date.

2.5 Review Questions

1. What do you mean by letter of credit? What are the various types of letter of credit?
2. What are Incoterms? What is their purpose and why are they considered as base of trade transactions?
3. Discuss the various Incoterms in detail. What group of Incoterms is preferable to Exporters? Give reasons.
4. 'ICC revise Incoterms so as to send them to the need of trading community'. Discuss.
5. What are the precautions which should be taken by exporter and importer in selection of Incoterms for international trade transactions?

Answers: Self Assessment

- | | |
|--------------------|--|
| 1. Confirmed | 2. merchant |
| 3. Trading | 4. owes |
| 5. cannot | 6. unconfirmed |
| 7. Cash-in-advance | 8. Open Account |
| 9. Collecting Bank | 10. Special or Standby letters of credit |
| 11. Incoterms | 12. consistency |
| 13. Group E | 14. FCA |
| 15. DES | |

2.6 Further Readings



Books

Cherenilan Francis, *International Economics*, 4th Edition, Tata McGraw-Hill Publishing Company Limited.

Dr. Ram Singh, *International Trade Operations*, Excel books 2009

Aseem Kumar, *Export and Import Management*, Excel books, 2007

Pradeep Kumar Sinha and Sanchari Sinha, *International Business Management: A global perspective*, Excel books, 2008



Online links

www.foreign-trade.com/reference/incoterms.cfm

www.customs.gov.au/webdata/resources/files/Incoterms.pdf

www.eximguru.com/exim/incoterms.aspx



Case Study

Timber Exporter

An exporter of timber products sells an average of 500,000 tons a year. His buyers (about 100 in number) are primarily located in four countries A, B, C and D. The exporter's mill is inland about 200 miles from his country's main seaport. His products may be moved without difficulty by rail to alongside ship in the port of loading.

The exporter's country has domestic ships that are suited to carry the products to the four countries, and it is in need of foreign currency. Also, the insurance risks can be covered by domestic cargo insurance companies. The political situation is stable, and tonnage is easily available.

The buyers' factories are located at inland points some 200 to 300 miles from the respective ports of discharge.

The following conditions have been noted in the different countries:

Country A

A has a well-organized port of discharge and efficient inland transportation by rail and truck but is known for labour disturbances.

Country B

B is known for congestion at its port of discharge: the waiting time of ships varies from 10 to 90 days. Inland transportation however is excellent.

Country C

C has no difficulties of the kind experienced by A and B but the buyers here are not entirely reliable because of difficult economic conditions.

Country D

D has all the advantages and none of the disadvantages of the other three countries in question.

Question:

What delivery term would you suggest for the exporter's sales contracts with buyers in each of the four countries?

Unit 3: EXIM Strategies

CONTENTS

Objectives

Introduction

- 3.1 Need to Go International
- 3.2 EXIM Business Plan and Strategy
- 3.3 Export Strategy Formation
- 3.4 Import Strategy
- 3.5 International Marketing
- 3.6 Summary
- 3.7 Keywords
- 3.8 Review Questions
- 3.9 Further Readings

Objectives

After studying this unit, you will be able to:

- Explain EXIM Bank: Plan and Strategies
- Discuss Export Strategy Formulation
- Describe Import Strategy
- Explain the concept of International Marketing

Introduction

Export-Import Bank of India is the premier export finance institution of the country, set up in 1982 under the Export-Import Bank of India Act 1981. Government of India launched the institution with a mandate, not just to enhance exports from India, but to integrate the country's foreign trade and investment with the overall economic growth. 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.

3.1 Need to Go International

The factors that motivate firms to go international may be broadly divided into two groups:

- The pull factors, most of which are proactive reasons, are those forces of attraction which pull the business to the foreign markets. Such attractiveness includes, broadly, the relative profitability and growth prospects.

- The push factors refer to the compulsions of the domestic market, like saturation of the market, which prompt companies to internationalize. Most of the push factors are reactive reasons.

Notes

Important reasons for going international are given below:

- **Profit advantage:** International business could be more profitable than the domestic one. Even when international business is less profitable than the domestic one, it could increase the total profit. Further, in certain cases international business can help increase the profitability of the domestic business. One of the important motivations for foreign investment is to reduce the cost of production (by taking advantage of cheap labour, for example).
- **Growth opportunities:** MNCs are getting increasingly interested in a number of developing countries as the income and population are rapidly rising in these countries. Foreign markets in both developed country and developing country provide enormous growth opportunities for firms of the developing country too.
- **Domestic market constraints:** The market for a number of products tends to saturate or decline in the advanced countries. This often happens when the market potential has been almost fully tapped. In the United States, for example, the stock of several consumer durables like cars, TVs, etc. the total number of household. Further, the technological advances have increased the size of the optimum scale of operation substantially in many industries making it necessary to have a foreign market, in addition to the domestic market to take advantage of scale economies. Again, when the domestic market is very small, internationalization is the only way to achieve significant growth. For example, Nestle derives only about 2% of its total sales from its home market Switzerland. Similarly with only 8% of the total sales coming from the home market, Holland, many different national subsidiaries of the Philips have contributed much larger share of the total revenues than the parent company.
- **Competition:** Competition may become a driving force behind internationalization. A protected market does not normally motivate companies to seek business outside the home market. Many companies also take an offensive international competitive strategy by way of counter-competition.
- **Government Policies and Regulation:** Many governments offer a number of incentives and other positive support to domestic companies to export and to invest in foreign countries. Sometimes, as was the case with India, companies may be obliged to earn foreign exchange to finance their imports and to meet certain other foreign exchange requirements like payment of royalty, dividend, etc. Further, in India, permission to enter certain industries by the large companies and foreign companies was subject to specific export obligations. Some companies also move to foreign countries because of certain regulations, like the environmental laws in advanced countries.
- **Monopoly power:** Monopoly power may arise from such factors as monopolization of certain resources, patent rights, technological advantage, product differentiation, etc. Exclusive market information as knowledge about foreign customers, market places, or market situations not widely shared by other firms.
- **Spin-off benefits:** International business improve the image of the company. There is white skin advantage associated with exporting, when domestic consumers get to know that the company is selling a significant portion of the production abroad, they will be inclined to buy from such company.
- **Strategic vision:** The stimulus for internationalization comes from the urge to grow, the need to become more competitive, the need to diversify and to gain strategic advantages of internationalization.

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3.1.1 Time Benefits of Going International

When you own a business of any size, from the sole proprietorship to the multi-state company with thousands of workers, there is an important decision to make as the company grows. Ask yourself and your partners, if any, if it's the right time to take the company international, which begins by expanding your market to the consumers in at least one other country.

To create and build brand awareness in an international market, a company must have a 3-5 year plan minimum.

As brand awareness is key to expanding the target market, this time invested will increase the exposure the consumer has to your brand.

Well-established brands gain trust from consumers and the target market are more likely to shop with your brand once they are familiar with it.

3.2 EXIM Business Plan and Strategy

Export-Import Bank of India has been one of the prime institutions that encourage project exports from India. The bank offers wide-ranging services for enhancing the prospect of Indian project exports. Exim Bank's Overseas Investment Finance program gives a variety of facilities for Indian reserves and acquirements overseas. The facilities consist of direct equity participation by the bank in the overseas venture and non-funded activities by the overseas venture and loan to the Indian companies for equity participation in the venture abroad. As part of Exim Bank's marketing Finance Program, the bank offers support to small and medium enterprises in their export marketing efforts consisting of financing the soft expenditure linking to completion of tactical and systematic export market development plans.

3.2.1 Export-Import Bank of India Objective

The primary objective of the Export-Import Bank of India is to provide financial assistance to importers and exporters and function as the top financial institution. Some of the services of the bank include: overseas investment finance, film finance, export credit, finance for export oriented units and agricultural and SME finance.



Note In the period of 2005- 2006 the total amount of loan given out by the bank amounted to 150,389 million, while this figure shot up to ₹ 220,760 million in the flowing year.

The Initiatives

Exim Bank of India has been the prime mover in encouraging project exports from India. The Bank provides Indian project exporters with a comprehensive range of services to enhance the prospect of their securing export contracts, particularly those funded by Multilateral Funding Agencies like the World Bank, Asian Development Bank, African Development Bank and European Bank for Reconstruction and Development.

The Bank extends lines of credit to overseas financial institutions, foreign governments and their agencies, enabling them to finance imports of goods and services from India on deferred credit terms. Exim Bank's lines of Credit obviate credit risks for Indian exporters and are of particular relevance to SME exporters.

The Bank's Overseas Investment Finance programme offers a variety of facilities for Indian investments and acquisitions overseas. The facilities include loan to Indian companies for equity

participation in overseas ventures, direct equity participation by Exim Bank in the overseas venture and non-funded facilities such as letters of credit and guarantees to facilitate local borrowings by the overseas venture.

The Bank provides financial assistance by way of term loans in Indian rupees/foreign currencies for setting up new production facility, expansion/modernization/upgradation of existing facilities and for acquisition of production equipment/technology. Such facilities particularly help export oriented Small and Medium Enterprises for creation of export capabilities and enhancement of international competitiveness.

Under its Export Marketing Finance programme, Exim Bank supports Small and Medium Enterprises in their export marketing efforts including financing the soft expenditure relating to implementation of strategic and systematic export market development plans.

The Bank has launched the Rural Initiatives Programme with the objective of linking Indian rural industry to the global market. The programme is intended to benefit rural poor through creation of export capability in rural enterprises.



Did u know? In order to assist the Small and Medium Enterprises, the Bank has put in place the Export Marketing Services (EMS) Programme. Through EMS, the Bank seeks to establish, on best efforts basis, SME sector products in overseas markets, starting from identification of prospective business partners to facilitating placement of final orders. The service is provided on success fee basis.

Exim Bank supplements its financing programmes with a wide range of value-added information, advisory and support services, which enable exporters to evaluate international risks, exploit export opportunities and improve competitiveness, thereby helping them in their globalisation efforts.

3.2.2 Export-Import Bank of India-Agri Business Group

The EXIM bank of India was established by Govt of India for providing financial assistance to exporters and importers, and for functioning as the principal financial institution for coordinating the working of institutions engaged in financing export and import of goods and services with a view to promoting the country's international trade.

It is further classified into Operating Groups namely:

- **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 credit, buyer's credit, finance for export of projects and consultancy services, guarantees, forfeiting, etc.
- **Lines of Credit Group Lines of Credit (LOC)** is a financing mechanism that provides a safe mode of non-recourse financing option to Indian exporters, especially to SMEs, and serves as an effective market entry tool.
- **Agri Business Group**, to spearhead the initiative to promote and support Agri-exports. The Group handles projects and export transactions in the agricultural sector for financing.
- **Small and Medium Enterprises Group** to the specific financing requirements of export oriented SMEs. The group handles credit proposals from SMEs under various lending programmes of the Bank.

Notes

- **Export Services Group** offers variety of advisory and value-added information services aimed at investment promotion.
- **Fee-based Export Marketing Services:** Bank offers assistance to Indian companies, to enable them establish their products in overseas markets.
- **Support Services groups**, which include Research & Planning, Corporate Finance, Loan Recovery, Internal Audit, Management Information Services, Information Technology, Legal, Human Resources Management and Corporate Affairs.

Some of the Agri Business related Schemes run by EXIM Bank:

The Indian agri sector can avail of a comprehensive range of products and services that Exim Bank offers. Broadly, these can be classified into three categories:

1. **Export Credit:** Exim Bank provides pre shipment and post shipment credit in Indian rupees and foreign currency. Finance is extended for short term i.e. up to 6 months as also for medium/long term i.e. beyond 6 months for eligible products and projects.

Medium/long term export credit is extended by way of supplier's credits i.e. through the Indian exporter with recourse to the exporter or buyer's credits i.e. directly to the overseas buyer with no recourse to the Indian exporter. Certain RBI guidelines apply for such medium/long term export credit.

Exim Bank has been recently permitted by RBI to cover inter alia agricultural commodities and processed foods under the Lines of Credit. Export contracts under Lines of Credits are financed without recourse to the exporter i.e. off balance sheet finance whilst the importer gets credit. Exim Bank extends loans for executing deemed export contracts. Exim Bank also issues guarantees overseas on behalf of Indian exporters.

2. **Finance for Export Oriented Companies:** Exim Bank also offers loans for financing Export Oriented Companies which may be categorized as under:

(a) *Project Finance*

- ◆ Finance for new projects, expansion, and modernization projects.
- ◆ Finance for purchase of equipment both imported as well as indigenous.
- ◆ Working Capital both short term as well as medium term.

- (b) **Overseas Investment Finance:** Overseas investment by Indian companies may be in the form of Joint Ventures (JVs) or Wholly Owned Subsidiaries (WOS). Exim Bank extends term loans against equity contribution/loan extended by Indian companies to their JVs/WOS. Term finance is provided directly to the JVs/WOS with corporate guarantee of the Indian promoter companies. Exim Bank can also participate in the equity of the overseas JV/WOS of the Indian company selectively subject to certain conditions.

(c) *Special Programmes*

- ◆ **Export Marketing Finance (Finance for developing strategic forward linkages):** Term loans are extended to important strategic marketing plan covering inter alia, overseas market research, participating in international trade fairs, promotion of product, brand positioning, international quality certification, mirror product adaptation, preoperative expenses for overseas offices, prospective buyers visits to India, etc.

- (i) **Export Product Development:** Term Loan for product adaptation, pilot plants, product/process development, etc.

- (ii) **Backward Linkage/Vendor Development Programme:** The Export Vendor Development Programme aims to support development of backward linkages by exporters. Rupee term finance is available on competitive terms to exporters for implementing strategic vendor development plans i.e. backward linkage for production of goods for exports in order to increase exports. Export/Trading Houses or manufacturer-exporters with satisfactory track record and strategic plan for development of backward linkages for exports are eligible to seek finance under this programme. Exim Bank may provide farm finance to exporters entering into backward linkages through contract farming with farmers on partnership basis for exports.
- ◆ Finance for Research & Development: Exim Bank also provides lending for Research & Development activities for facilitating exports.
3. **Advisory Services:** Exim Bank offers advisory services to Indian exporters for facilitating forward linkage for agri exports. Exim Bank's international network comprising overseas office, cooperation partners, correspondent banks and financial institutions is leveraged to provide export information on:
- ❖ Overseas markets/market segments.
 - ❖ Direct marketing of product.
 - ❖ Overseas business opportunities.
 - ❖ Information on export/import regulations, finance, etc.

3.3 Export Strategy Formation

There are several ways to evaluate the export potential of your products and services in overseas markets. The most common approach is to examine the success of your products domestically. If your company succeeds at selling in the U.S. market, there is a good chance that it will also be successful in markets abroad, at least those where similar needs and conditions exist.

Another means to assess your company's potential in exporting is by examining the unique or important features of your product. If those features are hard to duplicate abroad, then it is likely that you will be successful overseas. A unique product may have little competition and demand for it might be quite high.

Finally, your product may have export potential even if there are declining sales in the U.S. market. Sizeable export markets may still exist, especially if the product once did well in the United States but is now losing market share to more technically advanced products. Other countries may not need state-of-the-art technology and/or may be unable to afford the most sophisticated and expensive products. Such markets may have a surprisingly healthy demand for U.S. products that are older or considered obsolete by U.S. market standards.

3.3.1 Assessing Your Company's Export Readiness

Answering these general questions about how exporting will enhance into your company's short, medium and long-term goals will help determine your company's readiness to export:

- What does the company want to gain from exporting?
- Is exporting consistent with other company goals?
- What demands will exporting place on the company's key resources, management and personnel, production capacity, and finance and how will these demands be met?

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- Are the expected benefits worth the costs, or would company resources be better used for developing new domestic business?

3.3.2 Developing an Export Plan

Once you have decided to sell your products abroad, it is time to develop an export plan. A crucial first step in planning is to develop broad consensus among key management on the company's goals, objectives, capabilities and constraints. In addition, all aspects of an export plan should be agreed upon by the personnel involved in the exporting process, as they will ultimately execute the export plan.

The purposes of the export plan are (a) to assemble facts, constraints, and goals and (b) to create an action statement that takes all of these into account. The statement includes specific objectives, it sets forth time schedules for implementation, and it marks milestones so that the degree of success can be measured and help motivate personnel.

At least the following ten questions should ultimately be addressed:

1. Which products are selected for export development? What modifications, if any, must be made to adapt them for overseas markets?
2. Which countries are targeted for sales development?
3. In each country, what is the basic customer profile? What marketing and distribution channels should be used to reach customers?
4. What special challenges pertain to each market (competition, cultural differences, import controls, etc.), and what strategy will be used to address them?
5. How will the product's export sale price be determined?
6. What specific operational steps must be taken and when?
7. What will be the time frame for implementing each element of the plan?
8. What personnel and company resources will be dedicated to exporting?
9. What will be the cost in time and money for each element?
10. How will results be evaluated and used to modify the plan?

The first time an export plan is developed, it should be kept simple. It need be only a few pages long, since important market data and planning elements may not yet be available. (Sample format of export plan is given below)

Sample Outline for an Export Plan

Table of Contents

- Executive Summary (one or two pages maximum)

Introduction: Why This Company Should Export

Part I - Export Policy Commitment Statement

Part II - Situation/Background Analysis

- Product or Service
- Operations
- Personnel and Export Organization

- Resources of the Firm
- Industry Structure, Competition, and Demand

Notes

Part III - Marketing Component

- Identifying, Evaluating, and Selecting Target Markets
- Product Selection and Pricing
- Distribution Methods
- Terms and Conditions
- Internal Organization and Procedures
- Sales Goals: Profit and Loss Forecasts

Part IV - Tactics: Action Steps

- Primary Target Countries
- Secondary Target Countries
- Indirect Marketing Efforts

Part V - Export Budget

- Pro Forma Financial Statements

Part VI - Implementation Schedule

- Follow-up
- Periodic Operational and Management Review (Measuring Results against Plan)

Addenda: Background Data on Target Countries and Market

- Basic Market Statistics: Historical and Projected
- Background Facts
- Competitive Environment

From the start, the plan should be viewed and written as a management tool, not as a static document. Objectives in the plan should be compared with actual results to measure the success of different strategies. The company should not hesitate to modify the plan and make it more specific as new information and experience are gained.

A detailed plan is recommended for companies that intend to export directly. Companies choosing indirect export methods may require much simpler plans.



Note Many companies begin export activities haphazardly, without carefully screening markets or options for market entry. While these companies may or may not have a measure of success, they may overlook better export opportunities. If early export efforts are unsuccessful because of poor planning, your company may be misled into abandoning exporting altogether. Formulating an export strategy based on good information and proper assessment increases the chances that the best options will be chosen, that resources will be used effectively, and that efforts will consequently be carried through to success.

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3.3.3 Approaches to Exporting

The way your company chooses to export its products can have a significant effect on its export plan and specific marketing strategies. The basic distinction among approaches to exporting relates to the company's level of involvement in the export process. There are at least four approaches, which may be used alone or in combination:

- Passively filling orders from domestic buyers who then export the product. These sales are indistinguishable from other domestic sales as far as the original seller is concerned. Someone else has decided that the product in question meets foreign demand. That party takes all the risk and handles all of the exporting details, in some cases without even the awareness of the original seller. (Many companies take a stronger interest in exporting when they discover that their product is already being sold overseas.)
- Seeking out domestic buyers who represent foreign end users or customers. Many U.S. and foreign corporations, general contractors, foreign trading companies, foreign government agencies, foreign distributors and retailers, and others in the United States purchase for export. These buyers are a large market for a wide variety of goods and services. In this case a company may know its product is being exported, but it is still the buyer who assumes the risk and handles the details of exporting.
- Exporting indirectly through intermediaries. With this approach, a company engages the services of an intermediary firm capable of finding foreign markets and buyers for its products. EMCs, ETCs, international trade consultants, and other intermediaries can give the exporter access to well-established expertise and trade contacts. Yet, the exporter can still retain considerable control over the process and can realize some of the other benefits of exporting, such as learning more about foreign competitors, new technologies, and other market opportunities.
- Exporting directly. This approach is the most ambitious and difficult, since the exporter personally handles every aspect of the exporting process from market research and planning to foreign distribution and collections. Consequently, a significant commitment of management time and attention is required to achieve good results. However, this approach may also be the best way to achieve maximum profits and long-term growth.



Did u know? With appropriate help and guidance from the Department of Commerce, state trade offices, freight forwarders, international banks, and other service groups, even small or medium-sized firms can export directly if they are able to commit enough staff time to the effort.



Caution For those who cannot make that commitment, the services of an EMC, ETC, trade consultant, or other qualified intermediary are indispensable.

Approaches 1 and 2 represent a substantial proportion of total U.S. sales, perhaps as much as 30 percent of U.S. exports. They do not, however, involve the firm in the export process. Consequently, this guide concentrates on approaches 3 and 4. (There is no single source or special channel for identifying domestic buyers for overseas markets. In general, they may be found through the same means that U.S. buyers are found, for example through trade shows, mailing lists, industry directories, and trade associations.)

If the nature of the company's goals and resources makes an indirect method of exporting the best choice, little further planning may be needed. In such a case, the main task is to find a

suitable intermediary firm that can then handle most export details. Firms that are new to exporting or are unable to commit staff and funds to more complex export activities may find indirect methods of exporting more appropriate.

However, using an EMC or other intermediary does not exclude all possibility of direct exporting for your firm. For example, your company may try exporting directly to such “easy” nearby markets as Canada, Mexico, or the Bahamas while letting an EMC handle more ambitious sales to Egypt or Japan. You may also choose to gradually increase the level of direct exporting later, after experience has been gained and sales volume appears to justify added investment.

Notes

Self Assessment

Fill in the blanks:

1. Exim Bank’s program consist of direct equity participation by the bank and non-funded activities by the overseas venture and loan to the Indian companies for equity participation in the venture abroad.
2. As part of marketing Finance Program, the bank offers support to small and medium enterprises in their export marketing efforts consisting of financing the soft expenditure linking to completion of tactical and systematic export market development plans.
3. The primary objective of the Export-Import Bank of India is to provide assistance to importers and exporters and function as the top financial institution.
4. Exim Bank’s obviate credit risks for Indian exporters.
5. Exim Bank supports in their export marketing efforts including financing the soft expenditure relating to implementation of strategic and systematic export market development plans.
6. Corporate Banking Group, which handles a variety of financing programmes for....., Importers, and overseas investment by Indian companies.
7. Group offers variety of advisory and value-added information services aimed at investment promotion
8. Exim Bank has been recently permitted by to cover inter alia agricultural commodities and processed foods under the Lines of Credit
9. Overseas investment by Indian companies may be in the form of Joint Ventures (JVs) or
10. approach is the most ambitious and difficult, since the exporter personally handles every aspect of the exporting process from market research and planning to foreign distribution and collections.



Task Develop an export marketing plan for a particular product of your choice.

3.4 Import Strategy

Importing

The concept of importing is just the reverse. It refers to the purchase of goods or services by a company based in one country from sellers that reside in another country. Importing is an

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important function for implementing company's international strategies. Importing is thus the bringing of goods and services into a country and results in the importer paying money to the exporter in the foreign country.

Import strategy refers to the ways and means of bringing quality goods and services into one's country from the foreign countries at the lowest price with the best terms and conditions. There are two types of imports:

- Industrial and consumer goods to independent individuals and companies.
- Intermediate goods and services that are part of the firm's global supply chain.

Generally, companies import because they can buy goods or services at lower prices from foreign suppliers, because the goods or services are of higher quality than similar goods produced locally, or because the goods or services needed in their production processes are unavailable from local companies. Essentially, an importer seeks lower-priced or better-quality supplies, materials, or components that help to improve its capability to create value.

It would be practically impossible to manufacture the same products in countries with high labor costs, sell them at a reasonable price, and still make a profit. Similar situations exist in industries with a high degree of global competitive rivalry. Such industries, like consumer electronics and telecommunications, push the procuring company to try to combat import competition by switching to foreign suppliers whose components then enable it to lower the cost or boost the quality of its finished products. The automobile industry exemplifies this situation. Global competition in this industry spurs companies to seek out the highest quality inputs for the lowest price wherever they happen to be made and then import them into the countries that house their factories.

Companies also import products that are unavailable in the local market. For example, North America imports bananas from tropical climates because the climate of North America is not suitable for growing bananas. Simply put, North Americans would not enjoy fresh bananas were it not for imports. Similarly, a potential importer may seek new foreign products that complement its existing product lines, thereby giving it more ways to create value. Finally, an importer, like an exporter, might try to diversify its operating risks by systematically tapping international markets.

There is less research, relative to the study of export strategies, of import strategies. Three broad types of importers are identified.

3.4.1 Types of Importers

1. Those that opportunistically look for any product around the world that they can import and sell.
2. Those that look at foreign sourcing to get the highest quality products at the lowest possible price.
3. Those that use foreign sourcing as part of their global supply chain.

Essentials of Successful Importing

1. *Importing requires a certain degree of expertise in dealing with institutions and documentation:* Not every company commands this proficiency. Consequently, a company may opt to enlist an import broker to manage the process. The import broker obtains various government permissions and other clearances before forwarding the requisite paperwork to the carrier that is scheduled to deliver the goods to the importer. Import

brokers in the United States are certified as such by the US Customs Service to perform the functions needed to transport products into the country.

2. **Requirement of Customs Agencies' Essentials:** When importing goods, a company must be familiar with the customs operations of the importing country because once cargo reaches the port of entry, customs officials take control of the product and process. In this context, 'customs' are the country's import and export procedures and restrictions, not its cultural aspects.

An importer needs to know how to clear goods, what duties to pay, and what special laws exist regarding the import of products. On the procedural side, when merchandise reaches the port of entry, the importer must file documents with customs officials, who assign a provisional value and tariff classification to the merchandise.

A broker or other import consultant can help an importer minimize import duties by:

- ❖ Valuing products in such a way that they qualify for more favorable duty treatment. Different product categories have different duties. For example, finished goods typically have a higher duty than parts and components.
- ❖ Qualifying for duty refunds through drawback provisions. Some exporters use in their manufacturing process imported parts and components on which they paid a duty.
- ❖ Deferring duties by using bonded warehouses and foreign trade zones. Companies do not have to pay duties on imports stored in bonded warehouses and foreign trade zones until the goods are removed for sale or used in a manufacturing process.
- ❖ Limiting liability by properly marking an import's country of origin. Because governments assess duties on imports based in part on the country of origin, a mistake in marking the country of origin could result in a higher import duty.

3. **Understanding of Import Documentation:** Generally, there is a great deal of paper work involved in the import business. The arrival of a shipment at a port requires the importer to file specific documents with the port director in order to take title. Specifically, the importer receives the products without purchasing them—that is, it takes the title of ownership but without laying out any money. These documents are of two different types: (a) those that determine whether customs will release the shipment, and (b) those that contain information for duty assessment and statistical purposes. The specific documents that customs requires vary by country but usually include an entry manifest, a commercial invoice, and a packing list. For example, the exporter's commercial invoice contains information such as the country of origin, the port of entry to which the merchandise is destined, information on the importer and exporter, a detailed description of the merchandise, including its purchase price, and the currency used for the sale.

3.5 International Marketing

Globalisation renders the business environment increasingly global even for domestic firms. The major competition which many Indian firms encounter in the home market now, for instance, is from goods produced in India by MNCs and imports. For example, Nirma encounters competition from global, e.g. MNCs like Unilever, P&G, Colgate Palmolive, Henkel, etc. besides competition from imported products. Thus, many firms in their home market face the technological, financial, organizational, marketing and other managerial prowess of the multinationals.

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International marketing is an important aspect of international business. International marketing is not the same thing as international trade. Only a part of the international trade flows represents international marketing.

International can be defined as “finding out what customers want around the world and then satisfying these wants better than other competitors, both domestic and international”. It will be observed that international marketing has dual aspects, viz. foreign marketing (marketing in foreign countries) and global marketing (coordinating marketing in multiple markets, in the face of global competition).

The emergence of a borderless business world or a global market makes the term global marketing more relevant today than international marketing.

According to Keegan (Warren J. Keegan, *Global Marketing Management*, Prentice-Hall of India, New Delhi, 1995, Pages 3-5), “global marketing is the process of focusing is the process of focusing the resources (people, money and physical assets) and objectives of an organization on global market opportunities and threats”.

Walsh observes that international marketing is perhaps best regarded as a shorthand expression for the special international aspects of marketing and defines international marketing as “the marketing of goods and services across national frontiers, and the marketing operations of an organization that sells and/or produces within a given country when, the organization is part of or associated with an enterprise, which also operates in other countries and there is some degree of influence on or control of the organization’s marketing activities from outside the country in which it sells and/or it produces”.

Further, Keegan points out, “the first and most fundamental fact about marketing is that it is a universal discipline. Marketing is a set of concepts, tools, theories, practices and procedures and experience. Together, these elements constitute teachable and learnable body of knowledge. Although the marketing disciplines a universal markets and customers are quite differentiated. This means that marketing practice must vary from country to country. Each person is unique and each country is unique. This reality of differences means that we cannot always directly apply experience from one country to another. If the customers competitors channels of distribution and available media are different, it may be necessary to change our marketing plan”

3.5.1 Problems in International Marketing

The important special problems in international are given below:

1. **Political and legal differences:** The political and legal environment of foreign markets are different from that of domestic. The complexity generally increases as more number of countries are included in the company’s business portfolio.
2. **Cultural differences:** This is the most difficult area in international marketing. Many domestic markets, however, are also not free from cultural diversities.
3. **Economic differences:** The economic environment may change from country to country.
4. **Differences in the currency unit:** The currency unit varies from country to country. This may sometimes cause problems of currency convertibility, besides the problems of exchange rate fluctuations. The monetary system and regulation may also vary.
5. **Differences in the language:** An international marketer often problems arising out of the differences in the language. Even when the same language is used in different countries, the same words or terms may have different meanings or connotations.

6. **Differences in marketing infrastructure:** For example, an advertising medium that is very effective in one market may not be available or may be underdeveloped in another market.
7. **Trade restrictions:** Trade restrictions particularly import controls, are a very important problem which an international marketer faces.
8. **High cost of distance:** When markets are far removed by distance, the transport cost becomes higher and the time required for effecting the delivery tends to become longer. Distance tends to increase certain other costs too.
9. **Differences in trade practices:** Trade practices and customs may differ between markets.

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3.5.2 International Orientations

The EPRG framework identifies four types of attitudes or orientation towards internationalization that are associated with successive stages in the evolution of international operations. These four orientations are:

1. Ethnocentrism (home country orientation)
2. Polycentrism (host country orientation)
3. Regiocentrism (regional orientation)
4. Geocentrism (world orientation)

Table 3.1: Comparison of Different International Operations

Characteristics	Ethnocentrism	Polycentrism	Regiocentrism	Geocentrism
Management Orientation	Home country orientation	Host country orientation	Regional orientation	Global orientation
Perception of the market	Domestic market is superior. Opportunities are similar between the home and foreign markets. Foreign markets are extensions of home market	Each national market is distinctive. The differences between the home and foreign markets are decisive.	Markets can be differentiated and delineated on the basis of common regional characteristics.	The entire world is a single market that can be effectively tapped by standardized marketing strategy.
Marketing strategy	Extension of domestic strategy to foreign markets	Localization	Trade-off between localization and standardisation	Global standardisation.
Merits	No cost and effort of localization. An easy route to internationalization when foreign markets/ niches exist. With characteristics similar to domestic market exist.	Adaptations to the market characteristics which helps better exploitation of the market potentials.	Some of the advantages of both the localization and standardization strategies.	Economics of scale and lower costs. Advantages of pace.
Demerits	Limits the scope of exploitation of international business opportunities.	High costs of adaptation. Delays associated with adaptation.	Neglect of intra-regional differences in the business environment.	Standardization will not be successful in many cases.

3.5.3 Basic Entry Decisions

In this section we discuss at three basic decisions that a firm contemplating foreign expansion make (a) which markets to enter; (b) when to enter those markets; and (c) on what scale.

Which Foreign Markets

There are number of nation-states in the world, and all of them do not hold the same profit potential for a firm entering foreign markets. The choice must be based on an assessment of a nation's long-run profit potential. This potential is a function of several factors such as:

1. Detail of the economic and political factors that affect the potential attractiveness of a foreign market.
2. Balancing of benefits, costs, and risks associated with doing business in that country.

With regard to political factors the cost of doing business in a country can be increased by a need to pay off the politically powerful to be allowed by the government to do business. With regard to economic factors, one of the most important variables is the sophistication of a country's economy.

As for legal factors, it can be more costly to do business in a country where local laws and regulations set strict standards with regard to product safety, safety in the work place, environmental pollution, and the like.

As with costs, the risks of doing business in a country are determined by a number of political, economic and legal factors.

3. Study of factors such as the size of the market (in terms of demographics), the present wealth (purchasing power) of consumers in that market, and the likely future wealth of consumers.
4. Potential long-run benefits bear little relationship to a nation's current stage of economic development or political stability. Long-range benefits depend on likely future economic growth rates, and economic growth appears to be a function of a free market system and a country's capacity for growth (which may be greater in less developed nations).

By following the above process a firm can rank countries in term of their attractiveness and long run profit potential. Preference is then given to entering markets that rank highly.

Timing of Entry

Once attractive markets have been identified, it is important to consider the timing of entry. The advantages frequently associated with entering a market early are commonly known as first-mover advantages. One first mover advantage is the ability to preempt rivals and capture demand by establishing a strong brand name. A second advantage is the ability to build sales volume in that country and ride down the experience curve ahead of rivals, giving the early entrant a cost advantage over later entrants.

There can be disadvantages associated with entering a foreign market which are often referred to a first-mover disadvantages. These disadvantages may give rise to pioneering costs, which an early entrant has to bear that a later entrant can avoid. Pioneering costs arise when the business system in a foreign country is so different from that in a firm's home market that an enterprise has to devote considerable effort, time and expense to learning the rules of the game, e.g. costs of business failure due to ignorance of the foreign environment, certain liability associated with being a foreigner, the costs of promoting and establishing a product offering including the costs of educating customers, change in regulations in a way that diminishes the value of an early entrant's investments.

3.5.4 A Multi-country Strategy or a Global Strategy

Notes

A multi-country strategy is appropriate for industries where multi-country competition dominates and local responsiveness is essential. A global strategy works best in markets that are globally competitive or beginning to globalize. A global strategy is one where the company's approach is mostly the same in all countries. Although minor country to country differences in strategy do exist to accommodate specific competitive conditions in host countries, the company's fundamental competitive theme (low-cost, differentiation, best-cost, or focused) remains the same world wide. The question of which of these two strategies to pursue is the foremost strategic issue firms face when they compete in international markets. The following table provides a point-by-point comparison of multi-country versus global strategies:

Table 3.2: Multi-country Strategy or a Global Strategy

Multi Country Strategy		Global Strategy
Strategic arena	Selected target countries and trading areas	Most countries where there is high demand for the product; most global companies will have operations in North America, the Asian-Pacific, and Latin America.
Business strategy	Custom strategies to fit the circumstances of each host country situation; little or no strategy coordination across countries.	Same basic strategy worldwide; minor country-to-country variations where essential.
Product-line strategy	Adapted to local culture and the particular needs and expectations of local buyers.	Mostly standardized products sold worldwide; minor country to country variations where essential.
Production strategy	Plants scattered across many host countries, each producing versions suitable for surrounding locale.	Plants located on the basis of maximum competitive advantage (in low-cost countries, close to major markets, geographically scattered to minimize shipping costs, or use of a few world-scale plants to maximize economies of scale and experience curve effects—as most appropriate)
Sources of supply for raw materials and components	Suppliers in host country preferred (local facilities meeting local buyer needs; some local sourcing may be required by host government.)	Attractive suppliers from anywhere in the world.
Marketing and distribution	Adapted to practices and culture of each host country.	Much more world-wide coordination; minor adaptation to host-country situations if required.
Cross-country strategy connections	Efforts made to transfer ideas, technologies, competencies, and capabilities that work successfully in one country to another country whenever such a transfer appears advantageous.	Efforts made to use much the same technologies, competencies, and capabilities in all country markets (to promote use of a mostly standard strategy), but new strategic initiatives and competitive capabilities that prove successful in one country are transferred to other country markets.
Company Organization	Form subsidiary companies to handle operations in each host country; each subsidiary operates more or less autonomously to fit host country conditions.	All major strategic decisions closely coordinated at global headquarters; a global organization structure is used to unify the operations in each country.

Notes



Caselet

Serving European Community Market

A small Canadian firm that has developed some valuable new medical products using its unique biotechnology knowhow is trying to decide how best to serve the European Community market. Its choices are:

- (a) Manufacture the product at home and let foreign sales agents handle marketing.
- (b) Manufacture the product at home and set up a wholly-owned subsidiary in Europe to handle marketing.
- (c) Enter into a strategic alliance with a large European pharmaceutical firm. The product would be manufactured in Europe by the 50/50 joint venture and marketed by the European firm.

The cost of investment in manufacturing facilities will be a major one for the Canadian firm, but is not outside its reach. If these are the firm's only options, which one would you advise it to choose? Why?

Barriers to International Trade

The government's interference with international trade, for whatever motivations, creates barriers to trade. These barriers can be in different forms, but they generally fall into three distinct categories:

- **Tariff barriers:** Tariffs were originally intended to raise revenues for the government. However, they are now commonly used as a form of protectionism to restrict imports to protect domestic industry or to restrict exports to preserve national endowments.
- **Non-tariff barriers:** Non-tariff barriers are restrictions arising from measures such as licensing, product testing, certifications, procedural hurdles, etc.
- **Quota restrictions:** Quota restrictions mean explicit limit (usually measured by volume or sometime by value) on the amount of a particular product that can be imported or exported during a specified time period.

Quotas are a specific form of non-tariff barriers. A quota may be applied on a selective basis, with varying limits set according to the country of origin. It may also be applied on a global basis, which only specifies the total limit and thus leads to benefit the more efficient suppliers.



Task Why is there a need to go international? What problems are encountered while going international?

Self Assessment

Fill in the blanks:

- 11.renders the business environment increasingly global even for domestic firms.
- 12. A global strategy is one where the company's approach is mostly thein all countries.

13. The overall attractiveness of a country as a potential market and/or investment site for an international business depends on balancing the benefits,associated with doing business in that country.
14.risks can be defined as the likelihood that economic mismanagement will cause drastic changes in a country's business environment that adversely affect the profit.
15. Astrategy is appropriate for industries where multi-country competition dominates and local responsiveness is essential.

Notes

3.6 Summary

- Exim Bank plays four-pronged role with regard to India's foreign trade: those of a coordinator, a source of finance, consultant and promoter.
- Exim Bank is the Coordinator of the Working Group Mechanism for clearance of Project and Services Exports and Deferred Payment Exports (for amounts above a certain value currently US\$ 100 million).
- The Working Group comprises Exim Bank, Government of India representatives (Ministries of Finance, Commerce, External Affairs), Reserve Bank of India, Export Credit Guarantee Corporation of India Ltd. and commercial banks who are authorised foreign exchange dealers.
- Globalisation renders the business environment increasingly global even for domestic firms. The major competition which many Indian firms encounter in the home market now, for instance, is from goods produced in India by MNCs and imports.
- International marketing is an important aspect of international business.
- International marketing is not the same thing as international trade. Only a part of the international trade flows represents international marketing.
- International can be defined as "finding out what customers want around the world and then satisfying these wants better than other competitors, both domestic and international".
- It will be observed that international marketing has dual aspects, viz. foreign marketing (marketing in foreign countries) and global marketing (coordinating marketing in multiple markets, in the face of global competition).

3.7 Keywords

Export-Import Bank of India is to provide financial assistance to importers and exporters and function as the top financial institution.

International marketing: International marketing is an important aspect of international business. International marketing is not the same thing as international trade. Only a part of the international trade flows represents international marketing.

Non-tariff barriers: Non-tariff barriers are restrictions arising from measures such as licensing, product testing, certifications, procedural hurdles, etc.

Quota restrictions: Quota restrictions mean explicit limit (usually measured by volume or sometime by value) on the amount of a particular product that can be imported or exported during a specified time period.

Tariff barriers: Tariffs were originally intended to raise revenues for the government. However, they are now commonly used as a form of protectionism to restrict imports to protect domestic industry or to restrict exports to preserve national endowments.

Notes

3.8 Review Questions

1. Write a brief note on the EXIM Bank of India.
2. What is the primary objective of export-import bank of India?
3. Discuss an export plan.
4. What are the strategies for import?
5. What do you understand by international marketing?
6. What are the barriers for international marketing?
7. What are the basic entry decisions that needs to be taken care off?

Answers: Self Assessment

1. Overseas Investment Finance
2. Exim Bank's
3. financial
4. lines of Credit
5. Small and Medium Enterprises
6. Export Oriented Units (EOUs)
7. Export Services
8. RBI
9. Wholly Owned Subsidiaries (WOS)
10. Exporting directly
11. Globalisation
12. same
13. costs and risks
14. Economic
15. multi-country

3.9 Further Readings



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Online links

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Notes



Case Study

Megahertz Communications

Established in 1982, UK based Megahertz Communications quickly became one of Great Britain's leading independent broadcasting system builders. The company's core skill is in the design, manufacture and installation of TV and radio broadcast systems, including broadcast and news-gathering vehicles with satellite links. In 1998, Megahertz's managing director, Ashley Coles, set up a subsidiary company, Megahertz International, to sell products to the Middle East, Africa, and Eastern Europe. While the EU market for media and broadcasting is both mature and well served by large established companies, the Middle East, Africa, and Eastern Europe are growth markets with significant long-term potential for media and broadcasting. They also were not well served by other companies, and lacked an adequate supply of local broadcast engineers.

Megahertz International's export strategy was simple. The company aimed to provide a turnkey solution to emerging broadcast and media entities in Africa, the Middle East, and Eastern Europe, offering to custom-design, manufacture, install, and test broadcasting systems. To gain access to customers, Megahertz hired salespeople with significant experience in these regions and opened a foreign sales office in Italy. Megahertz also exhibited at a number of exhibitions that focused on the targeted regions, sent mailings and e-mail messages to local broadcasters, and set up a Web page, which drew a number of international inquiries.

The response was swift. By early 2000, Megahertz had already been involved in projects in Namibia, Oman, Romania, Russia, Nigeria, Poland, South Africa, Iceland, and Ethiopia. The international operations had expanded to a staff of 75 and were generating £310 million annually. The average order size was about £3250, 000, and the largest £3500, 000. In recognition of the company's success, in January 2000, the British government picked Megahertz to receive a Small Business Export Award.

Despite the company's early success, it was not all smooth sailing. According to Managing Director Coles, pre-shipment financing became a major headache. Coles described his working life as a juggling act, with as much as 20 percent of his time spent chasing money. Due to financing problems, one week Megahertz could have next to nothing in the bank; the next it might have £3300,000. The main problem was getting money to finance an order. Megahertz needed additional working capital to finance the purchase of component parts that go into the systems it builds for customers. The company found that banks were very cautious, particularly when they heard that the customers for the order were in Africa or Eastern Europe. The banks worried that Megahertz would not get paid on time, or at all, or that currency fluctuations would reduce the value of payments to Megahertz. Even when Megahertz had a letter of credit from the customer's bank and export insurance documentation, many lenders still saw the risks as too great and declined to lend bridging funds to Megahertz. As a partial solution, Megahertz turned to lending companies that specialize in financing international trade, but many of these companies charged interest rates significantly greater than those charged by banks, thereby squeezing Megahertz's profit margins.

Coles hoped these financing problems were temporary. Once Megahertz established a more sustained cash flow from its international operations, and banks appreciated the ability of Coles and his team to secure payment from foreign customers, he hoped that they would become more amenable to lending capital to Megahertz at rates that would

Contd...

help to protect the company's profit margins. By 2002, however, it was clear that the company's growth was too slow to achieve these goals anytime soon. As an alternative solution, in 2003, Coles agreed to sell Megahertz Communications to AZCAR of Canada. AZCAR acquired 80% of Megahertz broadcast systems to gain access to the expanding ED market and Megahertz's contacts in the Middle East. For Megahertz, the acquisition gave the company additional working capital that enabled it to take full advantage of export opportunities.

Questions:

1. What was the motivation for Megahertz's shift toward a strategy of export-led growth? Why do you think the opportunities for growth might be greater in foreign markets? Do you think that developing countries are likely to be a major market opportunity for Megahertz? Why?
2. Does Megahertz's strategy for building exports make sense given the nature of the broadcast industry? Why?
3. Why do you think Megahertz found it difficult to raise the working capital required to finance its international trade activities? What does the experience of Megahertz tell you about the problems facing small firms that wish to export?
4. Megahertz solved its financing problem by selling the company to AZCAR of Canada. What other solutions might the company have adopted?

Source: Charles WL Hill and Arun Kumar Jain, International Business, 6th Edition, 2009, Tata McGraw Hill Publishing Company Ltd., Delhi, p.676-678.

Notes

Unit 4: Export Marketing – Going Global

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Introduction

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4.4 Approaches to Reach Buyers

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Objectives

After studying this unit, you will be able to:

- Explain Export Marketing
- Discuss the Common pitfalls
- Discuss the concept of Buying Houses
- Discuss the concept of Communicating with Buyers
- Explain the Different Forms of International Trade

Introduction

Export Management is not confined to compliance of customs formalities and documentation alone. These certainly are important and integral parts of export business. However, the central task facing an exporter or export manager is to procure good business from buyers abroad. An export company essentially has to find foreign buyers for its own products or has to produce/procure goods as per the requirements of the importer. This means one has to deal with foreign nationals/companies to be in exports. Marketing involves identifying customer needs and satisfying the same through goods and services designed around those needs. Thus, export marketing can be defined as identifying willing foreign buyers whose needs could best be met using our products and delivering satisfaction through supply of goods in their countries complying with formalities of international transactions of both countries.

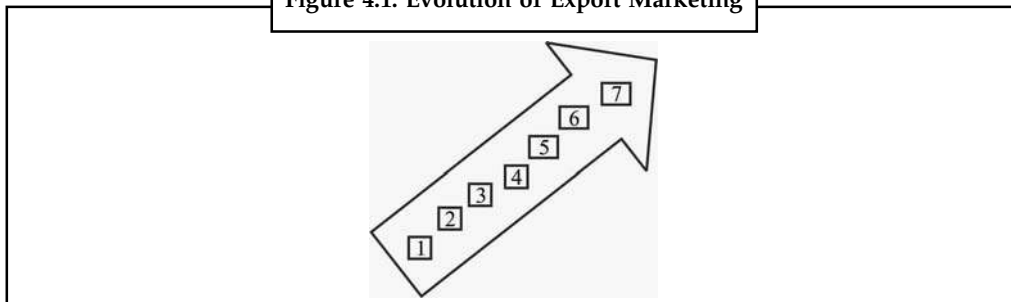
The job is tough and complex compared to domestic marketing. It is easier to locate and interact with local buyers. Supply of goods is also relatively easy. Matters could be dealt with instantly at the domestic front. Less complications and formalities are involved. One knows the mindset of the domestic buyers because one is a part of the same lot. Foreign buyers on the other hand are an unknown commodity. One is literally venturing into the unknown. A lot of research is required to enter a foreign market to source a foreign customer.



Caution Usually, initial export marketing results are obtained from having to fulfil unsolicited export orders. Once the exporter has experienced the success of the game, he feels more confident of exploring more. He becomes interested and works actively towards getting more work from foreign buyers.

The success of one exporter might inspire his local competitors to venture into exports as well. There could be a host of reasons that force or motivate a firm to enter export business.

Figure 4.1: Evolution of Export Marketing



Source: Managing Chaturvedi, Mukesh and Kumar, Aseem, Global Business: A Strategic Perspective, Excel Books, 2005.

The different stages depicted in Figure 4.1 are explained below:

1. **Totally Uninterested firm:** A firm that is fully occupied with domestic business and is not at all interested in exports.
2. **Partially Interested firm:** A firm that has partial interest in exports but not willing to make conscious efforts.
3. **Exploring firm:** A business that is interested and is backing up this interest by exploring various opportunities.
4. **Experimental firm:** A firm that has done some export and therefore, is willing to experiment to get regular export business.
5. **Small Exporter:** A firm that is regularly exporting small quantities.
6. **Large Exporter:** A firm that is doing regular large orders for buyers abroad.
7. **International firm:** A firm that has oriented itself fully with international markets and is actively pursues newer markets with different strategies.

The table 4.1 given below highlights the shifts from domestic business to export business on various counts:

Table 4.1 : Shifts from Domestic Business to Export Business

Management emphasis	Stage: Domestic	Stage: International
Focus	Domestic	Ethnocentric
Marketing Strategy	Domestic	International
Structure	Domestic	International
Management Style	Domestic	Centralized Top Down
Manufacturing Stance	Domestic	Mainly Domestic
Investment Policy	Domestic	Domestic used Worldwide
Performance Evaluation	Domestic Market Share	Against Home country Market Share

Source: <http://www.fao.org>; Global Agricultural Marketing Management (Marketing and Agri-business Texts - 3) by S. Carter (Food and Agriculture Organization of the United Nations, Rome, 1997)

Notes



Did u know? Different organizations could approach export markets at different times, depending upon their motives and understanding of the foreign markets.

4.1 Export Marketing

Export marketing consists of choosing a country/countries and sourcing willing buyers, planning and executing their orders made at home and completing all the requisite formalities. These days, export marketing has virtually become unavoidable because if you do not go to their markets, they will come to yours. The impact of globalization is for everybody to see. Only those firms will succeed that are able to deliver satisfaction for their customers better than their competitors, irrespective of whether the transaction is local or global. This has an additional implication for exporters for their task is not restricted to sourcing buyers and supplying them with ordered goods. They have to look for building long-term relationships with their buyers by giving them expected service consistently and coming up with innovative ways of improving their offerings.

They also need to be proactive in their approach. The idea is to keep looking for new markets and new buyers to conquer. Traditional marketing has to be ably supported with non-traditional channels. New experiments to improve supply chain have to be explored. Improving efficiency to bring down the cost is the order of the day. An exporter therefore, must redefine his role as a marketer. He has to create opportunities by aggressively marketing to the foreign buyers, rather than being satisfied to be at the receiving end, awaiting the mercy of the importer.

Government initiatives also play a crucial role. In India, for example, there are various agencies that help businesses in their export efforts. With all the help and information available, the exporter or the export manager of a business firm has to really take on this challenging yet interesting task of export marketing in his stride to be able to succeed.

The following framework is suggested to approach the task:

- Decision to go international
- Scanning the general business environment
- In-depth market research
- The buyer's sourcing effort
- Communicating with foreign buyers
- The order finalization
- Arranging finance and other resources
- Organizing production
- Pre-shipment activities
- Post-shipment activities

We will discuss those that have a direct relation to the export-marketing task.

Decision to Export: This is not an easy decision but once taken it has to be backed by total management support and commitment. Reasons behind this decision could be positive or negative, intentional or forced but once committed, one is advised to put all forces behind the decision. The reason why many people back out halfway is because they do not probably ponder enough before taking the leap. Export sounds very lucrative but there could be long

gaps between two orders, or there could be payment delays, or goods may face a number of pre-inspection rejections, making the job frustrating. The idea of making good profits through exports is a sound one but one must also bear in mind the pitfalls. One has to be mentally prepared to face all kind of difficult times while attempting exports.

Like domestic markets, export markets are also full of uncertainties. However, handling domestic uncertainties is definitely easy compared to grappling with external uncertainties. The risks are far greater in the export business and unless one is committed to face all risks and difficulties associated with exports, one is well advised to keep away from it. Any firm considering entering into international business transactions must understand that doing business internationally is neither a simple task nor one for the faint-hearted. It is stimulating and potentially profitable in the long-term but requires much preparation and research prior to the first transaction.

In view of the nature of export business as described above, the person aspiring to become an exporter has to analyze all aspects of getting into this trade before finally deciding to do it. Impulse decisions will not get you anywhere. Exports demand serious commitment and not casual romance. The most important attribute of a successful exporter is the willingness or positive attitude to conquer foreign buyers. There is also the added charm of being a foreign exchange earner for one's nation.

4.1.1 Strategic Considerations

- What are the goals of the business?
- What are the implications of the export business in terms of the overall business goals?
- How are these goals to be supported in terms of resources like finance, material, human capital and other infrastructure?
- Is the export business expected to generate sufficient returns to justify the additional investments?

Decisions could also be summarized as 4Ws of export decision-making:

- What to export?
- Where to export?
- When to export?
- To whom to export?

What refers to the decision regarding the product or service one plans to export. If one is already following a particular line, the obvious choice will be to export the same or related item. At times, it could be the other way round – one may get an order for something different from one's core area of competence, or existing business so the decision will become difficult, whether to jump into the unknown or not. If a business is starting new and planning to go into exports without any domestic business background, the decision will be even more complex.

Where refers to the countries and markets that offer the most potential for exports.

When refers to the time and sequencing of the export transactions. It may not be possible in the beginning but subsequently one could plan this to gain advantages.

To whom to, refers to the buyers or importers. This is the micro level and here individual buyers have to be identified as target customers.

Notes



Example: Charms & Co., based at Panipat, is a manufacturer of Home Textile & Home Furnishing fabrics, Rugs, Mats, Durries, Bathmats, Tablemats & Covers, Cushion covers, Handloom Bed covers, Curtains, and Bags. It now purpose to explore export opportunities. Some of the decisions that face the company could be summarized as follows:

- Is the company management really committed to the task of exports?
- Have they worked out a detailed proposal for entering foreign markets including setting of export objectives?
- Does this export proposal match the overall company objectives?
- Is the company in a position to afford/divert the required finance, production and human and other resources to the export project?
- In terms of cost-benefit analysis, does the export plan justify investment in exports?
- What products should the company plan to export to begin with?
- Which countries offer most demand for such products?
- What will be the right time to enter the said foreign markets?

4.1.2 Common Pitfalls

Let us also take a close look at some of the common pitfalls of exporting. An exporter must safeguard himself against falling prey to any or many of these:

- Failure to realistically analyze the proposed export operations
- Inability to develop a suitable export-marketing plan
- Half-hearted commitment/lack of full sponsorship by the Top Management
- Careless/hasty decision-making
- Chasing orders all over the world
- Unwillingness to be flexible in terms of product offerings
- Lack of initiative in gathering sufficient market/buyer information
- Acute focus on short-term gains.

Scanning the general business environment: The decision to export itself needs the analysis of general business environment both at the domestic and international level. However, once you have actually made up your mind to start export business, you need to scan and study the general business environment at length. A starting point could be a geographical segmentation followed by a ranking of different countries on pre-selected parameters like market size and potential for growth. Financial indicators like GDP & PCI, Risk, Governmental Regulations and Control, State of Infrastructural Development, Nature and size of Domestic and Foreign Competition, Accessibility, etc. Each criterion could be assigned weights and the countries can then be ranked on the basis of their overall scores. Easy as it may sound, it is a very complex exercise. However, computer software packages have made the task relatively simple and very much possible these days.

This initial screening will give the serviceable potential pockets. Generating a possible set of products to fit these pockets is another essential step an exporter needs to take simultaneously. The focus has to be on finding a strategic fit between the proposed products and potential

markets. This may require slight changes in existing products or major modifications or entirely new products. Although specific decision-making will come at a later stage, a broad decision on products and markets is required at the very beginning itself.

Notes



Caution Care needs to be exercised here, as the company must make a critical assessment of its capabilities, internal resources and assets as well as that of its mission and objectives. The company has to be flexible enough to respond to the challenges posed by new and unknown markets by adjusting its product portfolio and marketing style as required.

The following factors should be the focal point of this scanning:

Demographic/Physical Environment

1. Population size, growth, density
2. Urban and rural distribution
3. Climate and weather variations
4. Shipping distance
5. Product-significant demographics
6. Physical distribution and communication network
7. Natural resources.

Political Environment

1. System of government
2. Political stability and continuity
3. Ideological orientation
4. Government involvement in business
5. Attitudes toward foreign business (trade restrictions, tariffs, non-tariff barriers, and bilateral trade agreements)
6. National economic and developmental priorities.

Economic Environment

1. Overall level of development
2. GNP, industrial sector
3. Role of foreign trade in the economy
4. Currency: Inflation rate, availability, controls, and stability of exchange rate
5. Balance of payments
6. Per capita income and distribution
7. Disposable income and expenditure patterns.

Social/Cultural Environment

1. Literacy rate, educational level
2. Existence of middle class

Notes

3. Similarities and differences in relation to home market
4. Language and other cultural considerations.

Market Access, Limitations on Trade

1. High tariff levels, quotas
2. Documentation and import regulations
3. Local standards, practices, and other non-tariff barriers
4. Patents and trademark protection
5. Preferential treaties
6. Legal considerations for investment.

Product Potential

1. Customer needs and desires
2. Local production, imports, consumption
3. Exposure to and acceptance of product
4. Availability of linking products
5. Industry-specific key indicators of demand
6. Attitudes toward products of foreign origin
7. Competitive offerings.

Indicators of population, income levels and consumption patterns should be considered. In addition, statistics on local production trends, along with imports and exports of the product category, are helpful for assessing industry market potential. Often, an industry will have a few key indicators or measures that will help them determine the industry strength and demand within an international market. A manufacturer exporter of medical equipment, for example, may use the number of hospital beds, the number of surgeries and public expenditures for health care as indicators to assess the potential for its products.

Source: www.zeromillion.com



Task Prepare an export-marketing plan for an exporter like Charms & Co., illustrated in this unit.

4.2 In-depth Market Research

Sounds heavy but is essential to uncover the macro and micro characteristics of the potential markets abroad. One of the fundamental decisions and possibly the most critical one that faces a company intent on making forays into the export markets is the selection of the target market(s). It requires a careful study of the potential markets and matching their needs either with the existing products or modified/new products. An exporter needs to undertake a great deal of primary as well as secondary research to define and understand the nature and dynamics of the target market(s).

A thorough analysis of the target market will include customers, suppliers, substitute products and services as well as present and potential competitors. The future competitors may not be those that we know and see today; the newcomers may well enter by changing the rules of the

game in the market. Success against these forces depends upon the company's ability to create a successful product-market fit that offers unique advantages to the customers, reduces costs of operation below those of its competitors, erects barriers to entry into its market places, attracts price premiums for its goods and services and above all creates a strong position in the mind of the customers.

The initial screening of the potential markets will form the basis for target market selection. The essential steps are a thorough analysis of each market against preset definition of the target market. Thus, a company may be looking at South East Asia, Far East and China as its potential markets but a thorough analysis of each of these in terms of demand for a particular product, size and growth potential of the market, income levels of the potential buyers, geographic serviceability, psychographic profile of the customers, nature and size of local and foreign competition, Government regulations, political stability may point that China is the most favoured potential market and China tops as the target market.

Effective marketing programmes require a detailed analysis of the target markets. This analysis can only be developed through achieving adequate information about these markets. Systematic collection on information is crucial to successful strategy development in global markets. Information is needed to:

- (a) To assess new opportunities and threats that may emerge in target markets.
- (b) To better prepare in a better manner, for lack of familiarity in foreign markets and their business environment.
- (c) To monitor market demand, competition, government policies, and other environmental factors in the target markets.



Example: A US company, which brought its tomato ketchup to Japan on the simple assumption that ketchup was not available in Japan and that the company would be able to derive the pioneer advantage. However, Japanese did not like the product as their tastes traditionally favoured a Soya, based sauce. The company paid a heavy price for not conducting proper research to arrive at a suitable product-market fit for its target market of Japan.

The research has to answer the following questions:

- **What are the most exportable products to be offered to target market(s):** To identify products with export potential for distribution internationally, you need to consider products that are successfully distributed in the domestic market. The product needs to fill a targeted need for the purchaser in export markets according to price, value to customer/ country and market demand.
- **What makes your product(s) unique for markets abroad:** Your products must have a unique feature(s) that will interest the foreign buyer to accept them from you compared to anyone else from around the world. The product needs to fill a targeted need for the purchaser in export markets according to price, value to customer/country and market demand.
- **What are the best countries to market your product:** Since the number of world markets to be considered by a company is very large, it is neither possible nor advisable to research them all. Thus, your firm's time and money are spent most efficiently by using a sequential screening process.
- The first step in this sequential screening process for the company is to select the more attractive countries for your product. Preliminary screening involves defining the physical, political, economic and cultural environment. Subsequently, one could identify two or three markets that offer the best potential.

Notes

- ***Who will be your target customers within your chosen markets:*** You will need to identify your target customers within the countries that you have chosen to enter. In addition, you will have to collect detailed information on their current buying-volumes, frequency, reasons for buying from a particular source, etc.
- ***What is the best way to approach the target customers:*** Once you know your target customers, the next step is to get in touch with them to market your company and goods to them. You will need to decide what is the best way to approach them, as also when and where. You could write to them, talk to them on phone, meet them at a trade fair, visit them in their country or catch them in your country while they are visiting for some other purpose.
- What buying companies, agents or distributors would most likely be useful to get you the prospective customers for your export products: You must look for intermediaries that could get you export orders. Your research efforts, therefore, must focus on identifying such sources.
- ***What other sources could be tapped to source export business:*** You should find out about various other secondary data sources that will help you explore export-marketing opportunities.

The buyer sourcing effort: Having completed the basic marketing research to establish particular potential pockets of customers, the next step is to look for orders. For this again one needs to undertake a lot of research to generate as many leads of potential customers as possible. Contact must be established with a large number of potential foreign buyers to look for business wherever possible. The task is tough and could become unreasonably frustrating at times, but it also happens to be the crux of all exports activity. Therefore, the exporter has to be at it till such time that he has achieved success and that also becomes another beginning point of a long journey of getting export orders and executing them again and again to keep the foreign buyers happy. The job is continuous in nature and must be performed with utmost care at all times so as not to lose any potential opportunity.

There are a number of sources available these days that provide useful buyer information in different product/country categories. One of the most important are Government Agencies. A number of government agencies in India are engaged in export promotion activities in their respective fields. Exporters must seek their help in their export marketing pursuits:

- Export Promotion Councils (EPCs),
- Commodity Boards, assisting the exporters in the same manner as the Export Promotion Councils.
- Federation of Indian Export Organisations (FIEO) is an apex body coordinating and supplementing the export promotional activities of various export companies and institutions.
- Indian Institute of Foreign Trade (IIFT), New Delhi, develops and organizes new training programmes, research and market studies in the field of foreign trade.
- India Trade Promotion Organisation (ITPO), New Delhi-110002, provides facilities concerning participation in fairs and exhibitions in India and abroad. (See Box 4.1)
- Development Commissioner for Handicrafts and Small Scale Industries respectively. (See Box 4.2)
- Marine Products Export Development Authority at Cochin helps in the development of marine products meant for export with special reference to processing, packaging, storage and marketing etc.

- Indian government Trade Representatives at various important cities in foreign countries assist Indian exporters regarding promotion of Indian products to the world market.
- Foreign Government Trade Missions in India help in marketing Indian products to their markets.
- 'Niryat Bandhus' are the nodal officers nominated by the states for export promotion work.

Notes

Box 4.1

India Trade Promotion Organisation (ITPO) is the country's apex organisation engaged in export trade promotion through organisation of trade exhibitions in India and abroad, buyer-seller meets, promotion through department stores, contact promotion and product development programmes apart from dissemination of information on products and markets. As the premier trade promotion agency of the government of India, India Trade Promotion Organisation provides a broad spectrum of services to trade and industry so as to catalyze the growth of bilateral trade, particularly India's exports. The main activities of ITPO are:



- Organizing various trade fairs and exhibitions at its exhibition complex, Pragati Maidan, and other centres in India.
- Extending the use of Pragati Maidan for holding trade fairs and exhibitions by other fair organizers both from India and abroad.
- Identifying and nurturing specific export products with long-range growth prospects.
- Cultivating overseas buyers through timely and efficient services.
- Establishing durable contacts between Indian suppliers and overseas buyers.
- Assisting Indian companies in product development and adaptation to meet buyers' requirements.
- Organizing Buyer-Seller Meets and other exclusive India Shows in order to bring buyers and sellers together.
- Organizing India Promotions with Department Stores and Mail Order Houses abroad.
- Participating in overseas trade fairs and exhibitions.
- Arranging product displays for visiting overseas buyers.
- Inviting overseas buyers and organizing their meetings with Indian suppliers.
- Providing assistance in locating suitable foreign collaborators for transfer of technology, joint ventures, marketing tie-ups and investment promotion.
- Organizing seminars/conferences/workshops.
- Encouraging and involving small and medium scale units in export promotion efforts.
- Conducting in-house and need-based research on trade and export promotion.
- Enlisting the involvement and support of the state governments in India for promotion of India's foreign trade.
- Promoting establishment of facilities and infrastructure for holding trade fairs in state capitals or other suitable locations in India, in consultation with state governments concerned.

Contd...

Notes

ITPO's Major Trade Fairs in India: Over the years, ITPO has successfully organized the following big trade fairs in India. These have been widely attended by domestic as well as international audiences:

- India International Trade Fair
- International Security Exhibition
- Aahar (Food Expo)
- Printpack India
- Delhi International Shoe Fair
- Tex-Styles India
- Prakash (Lighting Exhibition)
- India International Leather Fair at Chennai
- International Leather Goods Fair at Kolkata

In addition, ITPO also takes part in major international exhibitions abroad. It also conducts buyer-seller meets to facilitate export business.

Source: www.tadeportalofindia.com

Box 4.2

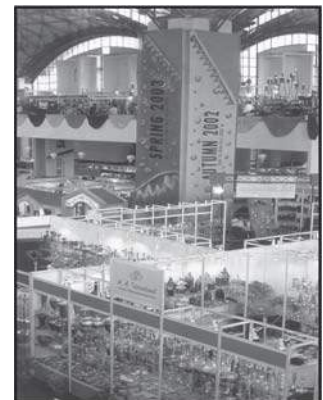
The Office of the Development Commissioner (Handicrafts) functions under Ministry of Textiles for promotion and exports of handicrafts. The office is headed by Development Commissioner [Handicrafts]. It advises the Government of India on matters relating to the Development and Exports of Handicrafts and assists the state government in planning and executing Development Schemes for handicrafts.



EXPORT PROMOTION SCHEME of the Office of the Development Commissioner (Handicrafts): The objective of the scheme is to promote export of handicrafts including hand knotted carpets and floor covering from Indian. Initiatives such as identification of handicrafts concentration area for development of exportable products, undertaking research and studies in order to identify markets abroad, taste and fashion, prevailing designs etc., participation in exhibitions etc. and addressing the issues emerging out of the liberalized and post WTO era would be undertaken under this scheme.

The various activities that cover the scheme are:

- (a) Identification of suitable handicrafts concentration area for development of exportable products.
- (b) Identification of markets for export of handicrafts, research and survey of markets abroad, identify prevailing designs, competitors taste and fashion prevailing and suggest measures.
- (c) Introduction of design technology innovation by sending craftspersons/designers/ technologists abroad and inviting craftspersons/designers/ technologists from abroad for study/development of new/innovative designs, etc.



Contd...

- (d) Twinning arrangements with institutions within the country and abroad for input on designing and technology market intelligence/output and tie-up with foreign professional Institutes.
- (e) Convening workshops/seminars in India and abroad followed by exhibition/live demonstration for exploring international market.
- (f) Publicity through media abroad to generate export.
- (g) Marketing through participation in International exhibition abroad, buyer-seller meets in India and abroad and other events sponsored by EPCH, CEPC, COHANDS or agencies approved by office of the DC (H) to eligible agencies involved in development & marketing of handicrafts.
- (h) Deputation of craftsmen abroad under agreed Cultural Exchange Programme between two countries to create awareness about Indian traditions and heritage abroad to explore export possibilities and vice-versa.
- (i) Improve quality through design innovations and innovation in product and process technology, improved packaging and export awareness of procedure to young entrepreneurs/crafts clusters.

Notes

Source: www.indianhandicrafts.org.in

4.3 Buying Houses

Foreign buying is a complex task. It requires experts who are able to source reliable vendors of quality merchandise from various parts of the world. Companies usually have a separate department or a subsidiary operation to take care of this mammoth task. Buyer is a proper designation in most foreign companies, who source products from other countries. The buyer does the job of buying products for his company from various sources including those located in other countries. These buyers are specialists in their own fields and they travel around the world to source suppliers. For example, we could have a buyer of leather products and another of chemicals. For bigger organizations, the buying departments could be organized product wise. In such cases, we could have a Principal or Chief buyer assisted by several assistant buyers and other staff. Still bigger companies could station resident buyers at different sourcing locations. Another version of this could be appointing local experts as buying agents, who normally work on commission basis. Multinational/global companies go a step further, they set up their own buying offices in different countries where they buy huge quantities and regularly. Most companies actually work with multiple such arrangements, that is, they utilize many buying sources at the same time. This is necessitated because their requirements are mind-boggling.

An exporter, thus, needs to find out such persons/companies who represent any foreign company as their buying agents in his line of work. To begin with, you will be asked to submit a copy of your company profile with details about your existing business, production facilities, supplier base, finances, banker details, list of existing foreign clients, infrastructural support and manpower, etc. The exporter has to make sure to keep this document to the point, crisp and compact such that it leaves a certain impression on the reader. However, it should only contain true information, as the buying companies will invariably crosscheck each detail.

The next stage is the personal meeting that is essentially like a job interview. Explain clearly what you can do. Never accept whatever is beyond your capabilities.

If your factory is approved they might ask you to make a few samples for them. They could give you their own designs or leave the designing also to you. At this stage itself, you must also cost your samples so that you will be able to quote a price for each and also negotiate if required.

Notes

4.3.1 Foreign Visits

An expensive but fruitful way is to visit foreign countries to explore export business opportunities. Business travel abroad can locate and cultivate new customers and improve relationships and communication with current foreign buyers. As with business in the domestic market, there is nothing like a face-to-face meeting with a prospect or existing customer.

Proactive export marketing requires the exporter to physically explore his target markets for sourcing export orders. However, since it is a costly and time consuming effort a lot of preparation and planning must be made before setting out of one's home country.

The following suggestions can help an exporter save time, money, and effort and can really fetch him the maximum value for his money spent on foreign travel:

- The travel plans should reflect what the exporter hopes to accomplish. The traveller should give some thought to the trip's goals and their relative priorities.
- The exporter should accomplish as much as possible before the trip begins by obtaining names of possible contacts, arranging appointments, checking transportation schedules, and so on. The most important meetings should be confirmed before the traveller leaves the country.
- The traveller should check the normal workdays and business hours in the countries to be visited.
- Travel agents can frequently arrange for transportation and hotel reservations quickly and efficiently. They can also help plan the itinerary, obtain the best travel rates, explain which countries require visas, advise on hotel rates and locations, and provide other valuable services. Since the hotels, airlines, and other carriers pay travel agents' fees, this assistance and expertise may cost nothing.
- The traveller should obtain the necessary travel documents two to three months before departure, especially if visas are needed. A valid passport is required for all travel outside the country. Visas, which are required by many countries, are provided for a small fee by the foreign country's embassy or consulate. Visa requirements may change from time to time.
- Likewise, obtaining medical insurance before travelling abroad is also a requirement for many countries and is also otherwise very strongly recommended as medical treatment is very expensive in most foreign countries. The exporter must arrange to obtain such insurance before he ventures out of his country.
- International driving license will also come handy if you could drive a car well and are aware of the international rules and regulations.
- Customs regulations on what can be brought home.
- Carry sufficient copies of your company profile and visiting cards. It will help if your visiting cards are also printed on one side in the foreign language of the country that you are visiting.
- Prepare for your meetings in great details. You should be in a position to answer all technical queries.
- Know your pricing by heart. Also, find about competitive products and their pricing, if you can.
- Be confident of your abilities, your product and your pricing.
- Finally, be very sure of the offer and its terms before you accept it.



Task Supposing you are a manufacturer of handicrafts in India, what schemes of the office of the DC (H) will help you to explore export opportunities?

Visit the website of GAP Inc. at www.gapinc.com. Try to create a plan to approach them for export orders assuming you are a fashion garments exporter from Delhi.

Notes

4.4 Approaches to Reach Buyers

The way company chooses to export its products can have a significant effect on export plan and specific marketing strategies. There are at least four approaches, which may be used alone or in combination:

Passively filling orders from domestic buyers who then export the product. These sales are indistinguishable from other domestic sales as far as the original seller is concerned. Someone else has decided that the product in question meets foreign demand. That party takes all the risk and handles all of the exporting details, in some cases without even the awareness of the original seller. (Many companies take a stronger interest in exporting when they discover that their product is already being sold over-seas.)

Seeking out domestic buyers who represent foreign end users or customers. Many U.S. and foreign corporations, general contractors, foreign trading companies, foreign government agencies, foreign distributors and retailers, and others in the United States purchase for export. These buyers are a large market for a wide variety of goods and services. In this case a company may know its product is being exported, but it is still the buyer who assumes the risk and handles the details of exporting.

Exporting indirectly through intermediaries. With this approach, a company engages the services of an intermediary firm capable of finding foreign markets and buyers for its products. EMCs, ETCs, international trade consultants, and other intermediaries can give the exporter access to well-established expertise and trade contacts. Yet, the exporter can still retain considerable control over the process and can realize some of the other benefits of exporting, such as learning more about foreign competitors, new technologies, and other market opportunities.

Exporting directly. This approach is the most ambitious and difficult, since the exporter personally handles every aspect of the exporting process from market research and planning to foreign distribution and collections. Consequently, a significant commitment of management time and attention is required to achieve good results. However, this approach may also be the best way to achieve maximum profits and long-term growth.

Self Assessment

Fill in the blanks:

1. involves identifying customer needs and satisfying the same through goods and services designed around those needs.
2. can be defined as identifying willing foreign buyers whose needs could best be met using our products and delivering satisfaction through supply of goods in their.
3. provide opportunities to display one's goods and capabilities and also serve as an effective platform for personal interaction between buyers and sellers
4. Communicating with buyers effectively requires a thorough understanding of their language, culture, and social etiquette.

Notes

5. Effective is an essential part of business.
6. The Carnet is a standardized international customs document used to obtain duty-free temporary admission of certain goods into the countries that are signatories to the ATA Convention.
7. An planning to carry product samples must know about the rules governing import of samples and duties to be paid, if any, in the foreign country
8. The objective of scheme of the Office of the Development Commissioner is to promote export of handicrafts including hand knotted carpets and floor covering from Indian.
9. The Office of the Development Commissioner (Handicrafts) functions under Ministry of Textiles for promotion and exports of
10. Systematic collection on information is crucial to successful strategy development in markets.



Task Interview two or three small exporters in your area and try to find out their ways of sourcing export business. Try and create a better plan for their marketing efforts.

4.5 Market Entry Strategies

International trade is the exchange of goods and services between countries. This type of trade gives rise to a world economy, in which prices, or supply and demand, affect and are affected by global events. Political change in Asia, for example, could result in an increase in the cost of labor, thereby increasing the manufacturing costs for an American sneaker company based in Malaysia, which would then result in an increase in the price that you have to pay to buy the tennis shoes at your local mall. A decrease in the cost of labor, on the other hand, would result in you having to pay less for your new shoes. The various forms of international trade are as follows:

4.5.1 Importing and Exporting

Importing and exporting are often the simplest ways a business may go global.

Importing is the purchasing abroad, either directly from target suppliers or indirectly through sales agents and distributors.

Exporting is the selling abroad, either directly to target customers or indirectly by retaining foreign sales agents and distributors.

Products that are made or grown abroad but sold domestically are called imports and products made or grown domestically and shipped for sale abroad are exports. People who engage in this type of international trade are called importers or exporters.

A good question is why a country imports or exports certain products. It may be simply that they do not have that resource internally or that it has an excess of that product. It could also be more complex than this simple answer. A country may have an absolute or competitive advantage.

Absolute advantage: when a country can produce something more cheaply than any other country. For example, Saudi Arabia, due to its natural resources, has an absolute advantage in oil.

Comparative advantage: when a country can make certain items more cheaply or better than other items relative to other countries. For example, Japan, due to its manufacturing efficiencies, has a comparative advantage in automobiles.

4.5.2 Licensing

Notes

Licensing does not have to be an international arrangement. Licensing may take place completely within one country. But, it is also a convenient way for a company to spread its products abroad with minimal risk.

Licensing is an arrangement whereby a firm (the licensor) grants a foreign firm (the licensee) the right to use intangible property such as a patent, logo, formula, process, etc. The licensee pays a royalty or percent of the profits to the licensor. Licensing allows a business to go global relatively rapidly and simply. Rather than trying to export a product directly, incurring shipping costs and delays, among other barriers, a company can license their methods of doing business to a foreign organization.



Example: rather than blend and bottle a soft drink here and then ship overseas, a company may license a foreign bottler who produces the soft drink locally using the licensed formula. This may also allow some adaptation to local tastes and customs.

4.5.3 Franchising

Franchising also does not have to be an international arrangement. Franchising may take place completely within one country. There are many examples of nationally-based franchises with which we are sure you are familiar. It is also another convenient way for a company to introduce its products abroad with minimal risk.

Franchising is a form of licensing in which the parent company (franchisor) offers some combination of trademark, equipment, materials, managerial guidelines, consulting advice, and cooperative advertising to the investor (franchisee) for a fee and/or percentage of revenues (royalties). As with licensing, franchising allows a business to go global relatively rapidly and simply, however, franchising generally requires a greater commitment, financially and otherwise, than licensing by both parties. The most obvious example is the ubiquitous McDonald's franchise. Some other examples are Starbucks or hotel chains such as Hilton. Franchising may also allow some adaptation to local tastes and customs.

4.5.4 Foreign Direct Investment

Foreign direct investment occurs when a company invests resources and personnel to build or purchase an operation in another country. This turns the firm into a multinational company (MNC).

A wholly owned subsidiary is a firm that is owned 100% by a foreign firm

This is a major decision for an organization because costs and risks of direct investment are greater than with franchising or licensing. Although governments usually welcome foreign direct investment, they are also often concerned about this type of investment for several reasons. Due to their size, MNCs may influence the host country's economic and political systems. Control of a country's important resources may pass into the hands of foreign corporations and, perhaps, then governments. Some countries enact programs to counteract these concerns.

4.5.5 Joint Ventures and Strategic Alliances

Joint ventures and strategic alliances are somewhat different from foreign direct investment in that we are not talking about creating wholly owned subsidiaries. Yet, they can be excellent, strategic ways to penetrate different global markets around the world while limiting exposure at the entry phase.

Notes

A joint venture is an organization created by two or more companies or a company and a foreign government in which each party contributes assets, owns the entity to some degree, and shares risk. A joint venture allows a company to partner with a firm from another country thus learning about business practices, cultural differences, etc. This is particularly popular among manufacturing concerns. For example, Ford Motor Company (U.S.) entered into a joint venture with the Mazda Company (Japan) and France's PSA Peugeot Citroen has joined with China's Dongfeng Motor Corp.

A strategic alliance is an agreement between potential or actual competitors to achieve common objectives.



Did u know? Unlike a joint venture they do not actually form a new entity but work cooperatively while maintaining their independence. It allows participants to share costs and risks and to take advantages of each other strengths. Because strategic alliances are built on trust, this type of arrangement should be undertaken with care.

A good example of international strategic alliance is the code sharing done by airlines. For example, you may purchase a ticket in the U.S. on Delta airlines for a flight to Italy and find yourself actually on an Alitalia flight carrying a Delta flight number.

Self Assessment

Fill in the blanks:

11. is the exchange of goods and services between countries.
12. is the purchasing abroad, either directly from target suppliers or indirectly through sales agents and distributors.
13. is the selling abroad, either directly to target customers or indirectly by retaining foreign sales agents and distributors.
14. when a country can produce something more cheaply than any other country.
15. when a country can make certain items more cheaply or better than other items relative to other countries.

4.6 Summary

- This unit focused on the export-marketing task.
- An exporter has to look for markets beyond his country's geographical borders.
- An export company essentially has to find foreign buyers for its own products or has to produce/procure goods as per the requirements of the importer. This means one has to deal with foreign nationals/companies to be in exports.
- Export marketing, can be defined as identifying willing foreign buyers whose needs could best be met using our products and delivering satisfaction through supply of goods in their countries complying with formalities of international transactions of both countries.
- A framework for approaching the export-marketing task has been proposed. The decision to export is not an easy one to make.
- The idea of making good profits through exports is a sound one but one must also bear in mind the pitfalls. Once this decision is made, an exporter then needs to undertake a great

deal of primary as well as secondary research to define and understand the nature and dynamics of the target market(s).

Notes

- A thorough analysis of the target market will include customers, suppliers, substitute products and services as well as present and potential competitors.
- In India, a number of government institutions support the marketing efforts of individual exporters. A list of such institutions was provided and some of these were discussed in detail.
- An exporter needs to find out persons or companies who represent any foreign company as their buying agents in his line of work. The task to follow is to source orders from such setups.
- Finally, the unit described the important role played by communication skills in export marketing. An export manager needs to master this art if he is to be successful.

4.7 Keywords

Absolute Advantage: When a country can produce something more cheaply than any other country.

Comparative Advantage: When a country can make certain items more cheaply or better than other items relative to other countries.

Exporting: Exporting is the selling abroad, either directly to target customers or indirectly by retaining foreign sales agents and distributors.

Importing: It is the purchasing abroad, either directly from target suppliers or indirectly through sales agents and distributors.

International Trade: It is the exchange of goods and services between countries.

4.8 Review Questions

1. What is export marketing? How is it more challenging compared to domestic marketing?
2. Discuss the evolution of an international marketing firm from a domestic firm. Why do firms shift to markets abroad?
3. What kind of research should an aspiring exporter undertake before finally deciding to export?
4. What role do buying companies play in international business? How can an exporter make use of their efforts?
5. What kind of government support available to exporters for marketing their products abroad? Highlight the role being played by ITPO.
6. Write short notes on:
 - (a) Scanning business environment for assessing export potential
 - (b) Tips on foreign travel for business
 - (c) International Trade Fairs
 - (d) Communicating with foreign buyers
 - (e) Common pitfalls of exporting
 - (f) Use of Internet for sourcing foreign buyers

Notes

Answers: Self Assessment

- | | |
|--------------------------------|------------------------|
| 1. Marketing | 2. Export marketing |
| 3. Trade Fairs and Exhibitions | 4. foreign |
| 5. communication | 6. ATA |
| 7. exporter | 8. export promotion |
| 9. handicrafts | 10. global |
| 11. International trade | 12. Importing |
| 13. Exporting | 14. Absolute advantage |
| 15. Comparative advantage: | |

4.9 Further Readings



Books

Charles W.L. Hill, *International Business Competing in the Global Marketplace*, TMH, 2005, (p. 540)

Chaturvedi, Mukesh and Kumar, *Managing Global Business: A Strategic Perspective*, Aseem, Excel Books, 2005.



Online links

http://www.mu.ac.in/myweb_test/TYBCOM%20study%20material/Export%20Mkt...pdf

http://www.exporthelp.co.za/marketing/export_marketing.html



Case Study

Facing the Wall

Aparna and Abhijit, brother-sister duo, are feeling upbeat today. They have shipped an important export consignment to Australia just this morning. They have been working very hard for this consignment for past two weeks. Today, at last the goods have been despatched. Abhijit says, “Hey Sis, how about a little celebration at the club in the evening?” Aparna agrees. The day passes and they are both ready to leave. Abhijit informs Aparna that he will reach the club direct, as he has to meet a friend.

On the way back home, Aparna is feeling happy as well as a little apprehensive. She has not told his brother so far but sooner or later she must tell him. How will he react? What will they do about the problem? Will things work out? She tries to think of other positive things as a distraction, but the questions would not stop flowing. What is she to do?

Before she enters the club, she has made up her mind. After the dinner, she will tell her brother everything. Together they will be able to plan the future course of action.

Dinner over, Aparna after some small talk asks her brother about his future plans. Abhijit actually teaches management at a business school and has come to spend the summer holidays with his sister. So he says, “I will cool my heels here for few more days and then back to work, what else. If you are asking about my marriage plans, Sorry, Sis I am in no mood for a few years.”

Aparna says, “Why don’t you work with me? I could certainly do with someone like you.”

Abhijit says, “Mr. Kharbanda is there to look after your business. He is experienced and reliable, so where’s the need?”

Aparna then tells him that Mr. Kharbanda is not on leave but has left the firm, and not only that, he has also walked away with all the major foreign buyers of the firm. She explains further that Mr. Kharbanda is now running his own export business with her old customers.

Abhijit is stunned. He says, “Why didn’t you tell me before? We could have done something. Have you talked to your old customers? How serious is the damage?”

Aparna tells him that she has tried all the old customers but they are not even prepared to listen. She then tells him that if he agrees they could work together on export marketing of their firm. She says she has some very good ideas on the subject.

Abhijit is pensive for some time but then he says, “Okay Sis, Let’s do it. We will show that Kharbanda. I can easily get a year’s leave without pay. So tell me your ideas.”

Aparna’s business is high fashion garments and her major buyers were retail chains in the U.K. Aparna designs herself and has good control over suppliers and production. Marketing was never an issue with her because her maternal uncle, who has retired and now settled in Bangalore, gave ready business to her. This was five years ago. Mr. Kharbanda was there when she took over and was like a pillar to her as far as marketing was concerned. In fact, she trusted him completely and is really shocked at his leaving like this.

As Aparna tells her brother various ideas to find new buyers for their business, Abhijit who was feeling very determined just a while ago, feels he is facing the wall. He can teach but actually finding business from foreign countries may not exactly be his cup of tea.

Questions:

1. If Abhijit approaches you as an export-marketing expert, how will you help him?
2. What should Aparna have done to prevent Mr. Kharbanda robbing her off her foreign buyers like this?

Unit 5: Methods of Financing Exporters and Business Risk Management

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Objectives

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5.1 Pre-shipment Finance

5.2 Post-shipment Export Advance

5.3 Role of Export-Import Bank of India in Export Finance

5.4 Factoring

5.5 Types of Risk and Insurance

5.6 Quality and Pre-Shipment Inspection

5.7 Summary

5.8 Keywords

5.9 Review Questions

5.10 Further Readings

Objectives

After studying this unit, you will be able to:

- Explain Pre shipment Finance
- Describe Post shipment export Advance
- Explain Factoring and Insurance
- Describe Types of Risk
- Discuss Quality and Pre-shipment Inspection

Introduction

International trade is fiercely competitive. The exporter needs to have a competitive edge over other suppliers from various countries. To this end, access to export finance at competitive rates of interest will immensely serve the exporter's cause. Both types of finance facilities are important. Pre-shipment finance, helps the exporter to get started with procurement and production. Timely availability of funds will define the exporter's ability to ship the right quality of goods at the right time. Post-shipment finance assumes importance in view of the exporter's need to extend credit to the importers to remain competitive. This period, when goods have gone and payment is yet to come, poses severe liquidity challenges to the exporter. Post-shipment finance provides effective solutions to the liquidity woes of the exporter.

Commercial banks offer export finance at special rates to the exporters in tune with the export promotion initiatives of the government to boost exports. Concessional interest rates and liberal schemes have been introduced in India by the Commerce Ministry through the Reserve Bank of India (RBI).

5.1 Pre-shipment Finance

Notes

Pre-shipment credit is provided to the exporters for meeting their need of getting the shipment ready. It is generally offered as Packing Credit (PC). The exporter has to submit the prescribed application form for obtaining packing credit together with the required papers to the bank. The documents required generally are the export order, letter of credit, proof of business address, financial papers like profit & loss account and the balance sheet. The bank thoroughly scrutinizes the application and the attachments. Generally, a physical verification of the exporter's business premises is also carried out. The bank wants to make certain that the exporter has a financially sound business background. In addition, the bank asks the exporter to provide collateral security/guarantee to secure the loan. Banks these days extend packing credit only against firm export orders backed by irrevocable confirmed letter of credit from a prime bank.

Banks also require the exporter to obtain an insurance cover from ECGC against payment risks. The banks themselves also obtain financial guarantees from *Export Credit Guarantee Corporation* and the exporter is required to bear the charges for the same.

The amount of PC extended normally will not exceed the FOB value of the export order. The bank will also consider the domestic cost of production of a particular order. Banks also require the exporter to contribute margin money to ensure his financial stake in the transaction as well as not to finance his profits also. The bank's own risk is also reduced to the extent of the margin money and the exporter becomes personally responsible to the same extent. Each bank decides its own margin requirements as there are no set rules for this.

The period for which PC is granted depends upon the situation in each case. The bank will prepare its own estimate of the time required for completion of the particular order, as well as pay attention to the shipment date. Out of the two, the earlier date normally defines the credit period. The banks decide the repayment period keeping in view a maximum of 180 days as prescribed by the RBI. In certain cases, where the production process is rather long, credit is permissible for up to 270 days. If the credit remains outstanding beyond the specified time period, interest is charged at the normal commercial lending rate, from the start date of the loan.

PC is normally operated as a separate account and the exporter is required to utilize the funds only for transactions related to the particular export order. The bank closely monitors the operation of this account to ensure proper use of funds designated for fulfillment of a certain export contract.

The outstanding loan amount in a PC account has to be settled out of the proceeds of the exported goods as soon as the documents drawn for the same are discounted. At this moment, the pre-shipment loan actually gets converted into post-shipment credit.

Pre-shipment credit is extended in both Indian rupees as well as in foreign currency. The latter is known as *PCFC*, that is, pre-shipment credit in foreign currency. This facility entitles the exporter to borrow funds as pre-shipment credit in foreign currencies like US Dollar, Japanese Yen, Pound Sterling or Euro. Such credit is offered at internationally competitive interest rates to enable the exporter to take advantage of the same under stiff competitive environment. These loans are extended at LIBOR/EURIBOR/EURO LIBOR interest rates. *LIBOR* stands for London Inter-Bank Offer Rate which refers to the rate of interest at which banks are ready to lend money to each other in London's inter-bank market. LIBOR rates are the world's most widely used short-term interest rates. *EURIBOR* is Euro Inter-Bank Offered Rate, the rate released by the European Banking Federation, used for euro inter-bank loan transactions between banks in the euro region. EURIBOR is generally used as the underlying interest rate for euro-denominated transactions. *EURO LIBOR*, as the name suggests, refers to Libor denominated in euro.

Notes

The exporter may also be allowed a *Running Account Facility* if his track record is satisfactory to help him overcome difficulties arising due to long production periods and seasonal availability of raw materials. In such cases, the exporter is granted PC without submitting a firm export order or letter of credit. However, he is expected to submit the same with the bank within a reasonable period. Banks are authorised to use their own judgements in this respect. Box 5.1 below shows SBI's PCFC scheme:

Box 5.1: Pre-shipment Credit in Foreign Currency (PCFC)



SBI's Pre-shipment Credit in Foreign Currency (PCFC) is just what you need, when you are looking for funds in foreign currency. Avail it to meet your manufacturing, processing and packing fund requirements at international interest rates. Not just this, you can also cover the cost of both domestic as well as imported inputs of your export requirements. SBI's PCFC gives you choice of four different currencies in which to operate the scheme – the US Dollar, Pound Sterling, Euro and the Japanese Yen.

SBI has 64 branches across the country handling the PCFC facility for your exclusive convenience. Our Foreign Department, based at Kolkata, is the nodal centre for raising and deploying offshore and onshore funds for lending under PCFC.

Getting Started – Opening a PCFC

Make sure you have firm export orders or confirmed letters of credit, and you will find that obtaining the PCFC facility from SBI is a cakewalk. Of course, you also need to satisfy other credit norms.

Now for the icing on the cake – we let you have a running account facility with us for PCFC if you are an exporter with a good track record. The specified eligibility factor is that your over dues should not exceed 5% of the average annual export realisations during the preceding three calendar years. In cases where a running account facility has been extended, you must produce a letter of credit or a firm export order within a reasonable period of time.

More good news for existing clients – there is no need for a separate sub-limit for PCFC for you! The PCFC can be made available within the export packing credit available to you provided the outstanding amounts under both rupee and foreign currency facilities do not exceed the sanctioned limits.

Operating PCFC

PCFC is to be repaid only with the proceeds of the export bill tendered, under the export bill-rediscounging scheme.

In case of cancellation of the export order, the PCFC line may be closed by selling an equivalent amount of foreign exchange at the TT selling rate that is prevalent on the date of liquidation.

How do the schemes operate?

PCFC and EBR schemes go hand in hand. The operation of these schemes is in three stages, viz.:

- (i) Disbursement of PCFC
- (ii) Disbursement of EBR and simultaneous repayment of PCFC and
- (iii) Repayment of EBR.

Contd...

When the exporter has sufficient drawing power available within his overall limit to accommodate the proposed PCFC advance, PCFC is made available to him either in foreign currency for payment of his import bills or in Indian rupees for purchase of domestic raw material by converting the foreign currency of PCFC at T.T. buying rate.

PCFC is operated like cash credit account with balances in foreign currency. The liability of the exporter to the Bank on account of PCFC is in foreign currency. The rupee equivalent will be shown in the account only at notional rates which really does not concern the exporter. Interest on PCFC will be arrived at in foreign currency and the rupee equivalent thereof will be recovered at quarterly intervals from the exporter's CC or current account.

Source: www.statebankofindia.com

5.1.1 Advances against Duty Drawback/Incentives

Banks may also extend loans prior to shipments against the drawback/incentives receivable from the government covered by ECGC guarantee in certain exceptional cases. This type of advance is normally extended after the goods have been shipped. The exporter will have to present his case as a special one to the satisfaction of the bank. The bank in its own discretion may advance a loan for up to 90 days at any interest rate within the ceiling of *BPLR* (Benchmark Prime Lending Rate) *minus* 2.5%.

5.2 Post-shipment Export Advance

Once the exporter has shipped the goods, there will always be a time gap between the date of shipment and the date of receipt of payment. Post-shipment credit refers to the facilities extended by the banks to the exporter during this period to enable him to tide over his financial needs. It also includes any loan or advance granted by the bank to the exporter against any drawback or other export incentives receivable, permitted by the government. Post-shipment loan runs from the date of extending credit, after shipment of goods to the date of realization of export proceeds. It infuses funds into the business even before the actual payment has been received, thus easing the cash flow. The exporter is in a position to obtain funds for the shipped goods without waiting for the buyer to make the payment.

Post-shipment finance is provided at concessional interest rates as per RBI guidelines. The proof of shipment of goods, serves as the basis of grant of such facility. The basic purpose of this credit is to finance export receivables. Normally, the exporter who has exported the goods is eligible to apply for this facility. Alternatively, the exporter to whom the export documents have been transferred, can apply for this credit.

Post-shipment finance can be granted up to 100% of the invoice value although the normal practice is to give 90%. This credit gets liquidated by the proceeds of export bills received from overseas in respect of the exported goods.

The exporter has the choice to avail post-shipment credit either in Indian rupees or in foreign currency. However, if the exporter has availed the pre-shipment credit in foreign currency, the post-shipment credit has to be essentially in foreign currency since pre-shipment credit has to be liquidated in foreign currency. Under Export Bill Re-discounting (EBR) scheme, for post shipment finance at international rates of interest, PCFC will be liquidated with the discounting of bills. The foreign currency of the bill will be applied to PCFC in foreign currency and if there is any surplus of the bill after adjusting to PCFC, the surplus portion will be converted into Indian rupees and credited to the exporter's CC or current account. The EBR advance, which is a foreign currency loan, will be eventually closed when the overseas buyer pays the bill and the export proceeds are realised.

Notes

The following options are available to the exporter for post-shipment credit:

- (i) Export bills purchase/discounting
- (ii) Export bills negotiated (against letter of credit)
- (iii) Advances against bills for collection
- (iv) Advances against duty drawback receivable from the government
- (v) Advances against exports on consignment basis
- (vi) Advances against undrawn balances

Banks can extend post shipment finance on concessional rates for periods listed below:

- **Demand bills** – the credit period is the Normal Transit Period (NTP) as prescribed from time-to-time by the Foreign Exchange Dealers' Association of India (FEDAI). This period comprises the average period normally involved from the date of negotiation/purchase/discount till the receipt of bill proceeds in the Nostro account of the bank. It is not the same as time taken for the arrival of the goods at the destination.
- **Usance bills** – the credit period is a maximum of 180 days inclusive of NTP plus usance period plus grace period.



Did u know? An exporter can also avail of **factoring services** for his export receivables to finance his post-shipment activities. Under export factoring, the factoring agency factors export invoices drawn on overseas buyers and prepays to clients an agreed percentage of the invoice value immediately.

The following steps are involved:

- The exporter ships the goods to the importer.
- The exporter assigns his invoices through the export factor to the import factor who assumes the credit risk (as per prior arrangement).
- The Export factor prepays invoices.
- The importer pays the proceeds to the import factor, who transfers the amount to the export factor.
- The export factor deducts prepayment already made, other charges and pays the balance proceeds to the exporter.

The agency handling the collection of export receivables of clients (exporters) is called Export Factor (EF) and the factor in the buyer's country who undertakes collection and credit protection services, is called the Import Factor.

5.2.1 Advantages to Exporters

Factoring is beneficial to the exporters in the following ways:

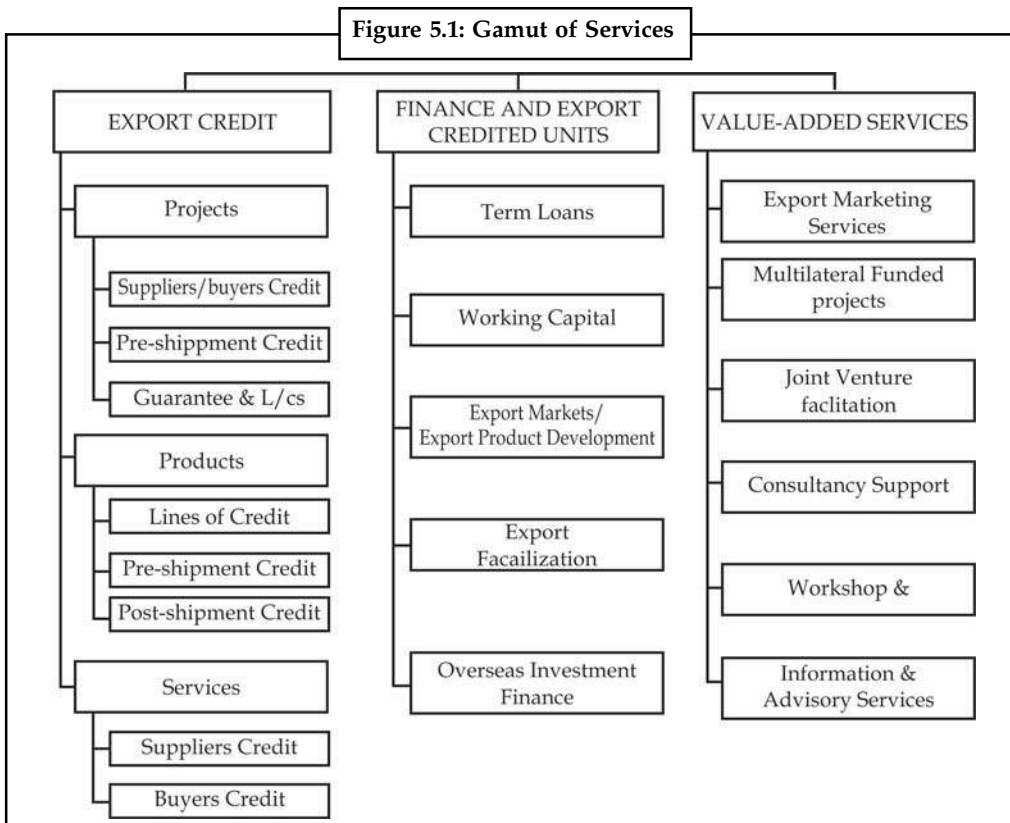
- Elimination of the cost and delays experienced in transacting business under LC.
- The import factor offers credit risk protection in case the buyer does not pay invoices within 90 days of the due date.
- ECGC policy cost can be saved. There is reduction in the administrative cost, as the exporter will be dealing with only one Export Factor irrespective of the number of countries involved.

- The exporter can obtain valuable information on the standing of the foreign buyers on trade customs and market potential in order to expand his business.
- The following up of receivables by import factor will speed up the collections.
- As we provide finance up to 90% on export invoices, the exporter has an improved cash flow and his liquidity improves markedly.

Source: www.sbifactors.com

5.3 Role of Export-Import Bank of India in Export Finance

Export-Import Bank of India, set up in 1982, for the purpose of financing, facilitating, and promoting foreign trade in India, is the principal financial institution in the country for coordinating the working of institutions which are engaged in financing exports and imports. The bank provides competitive finance at various stages of the export cycle. The gamut of services provided by the bank is depicted in the figure 5.1 below:



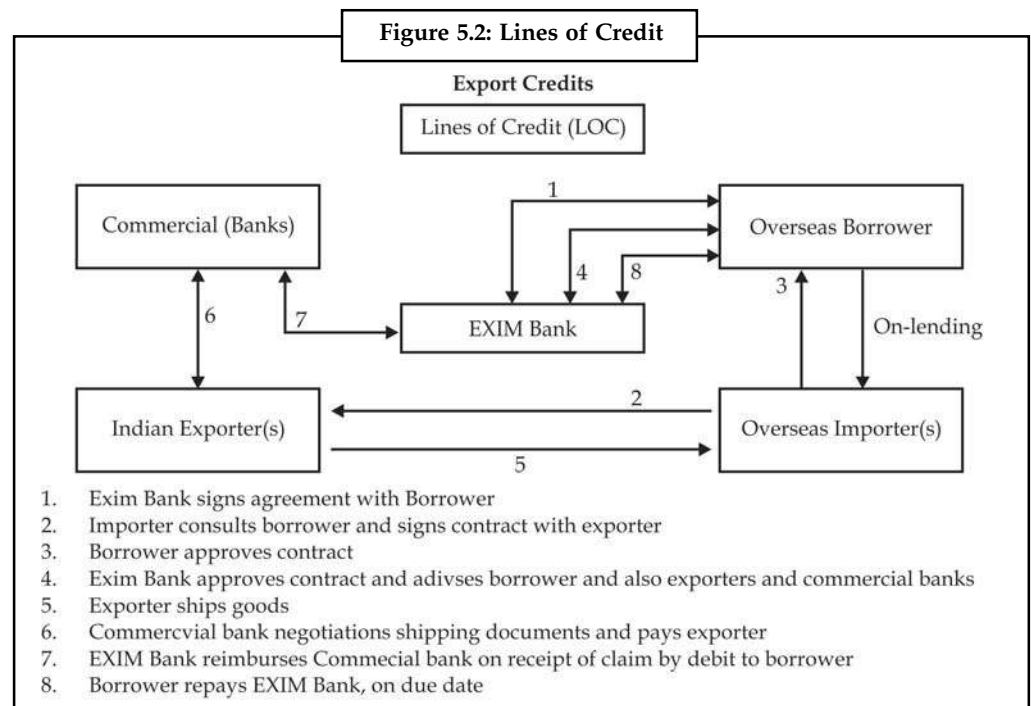
EXIM INDIA operates a wide range of financing and promotional programmes. The Bank finances exports of Indian machinery, manufactured goods, consultancy and technology services on deferred payment terms. EXIM INDIA also seeks to co-finance projects with global and regional development agencies to assist Indian exporters in their efforts to participate in such overseas projects.

The Bank is involved in promotion of two-way technology transfer through the outward flow of investment in Indian joint ventures overseas and foreign direct investment flow into India. EXIM INDIA is also a Partner Institution with European Union and operates for facilitating promotion of joint ventures in India through technical and financial collaboration with medium-sized firms of the European Union.

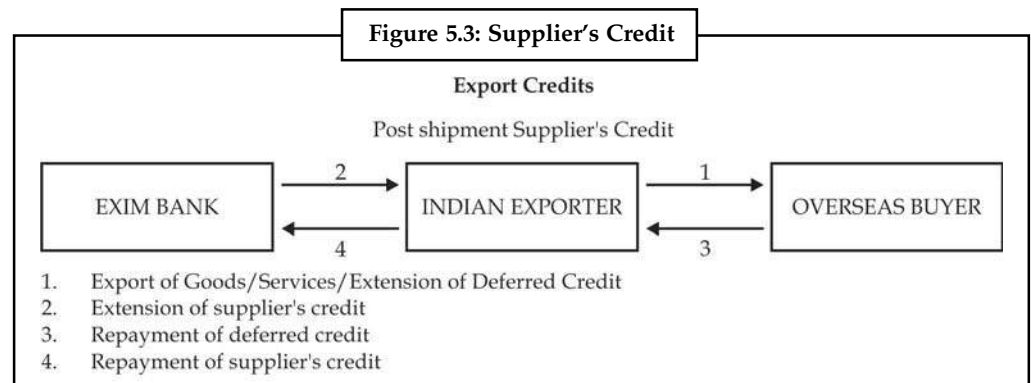
Notes

The Bank provides the following fund based facilities:

- Lines of Credit:** Exim Bank extends lines of credit to overseas governments/agencies nominated by them or financial institutions overseas to enable buyers in those countries to import capital/engineering goods, industrial manufactures and related services from India on deferred payment terms. This facility enables importers in those countries to import from India on deferred credit terms as per the terms and conditions already negotiated between Exim Bank and the overseas agency.



- Supplier's Credit:** Exim Bank offers Supplier's Credit in Rupees or in Foreign Currency at post-shipment stage to finance export of eligible goods and services on deferred payment terms. Supplier's Credit is available both for supply contracts as well as project exports; the latter includes construction, turnkey or consultancy contracts undertaken overseas. Exporters can seek Supplier's Credit in Rupees/Foreign Currency from Exim Bank in respect of export contracts on deferred payment terms irrespective of value of export contracts.



- Overseas Buyer's Credit:** Credit is offered directly to the overseas buyer for a specific project/ contract.

- **Finance for Rupee Expenditure for Project Export Contracts (FREPEC):** This scheme seeks to Finance Rupee Expenditure for Project Export Contracts, to enable Indian project exporters to meet rupee expenditure incurred/required to be incurred for execution of overseas project export contracts such as for mobilisation/purchase/acquisition of materials and equipment, mobilisation of personnel, payments to be made in India to staff, subcontractors, consultants and to meet project related overheads in Indian rupees. The purpose of the programme is to provide a boost to project export efforts of companies having a good track record and sound financials.
- **Pre-Shipment Rupee Credit:** Pre-shipment Rupee Credit is extended to finance temporary funding requirement of export contracts. This facility enables the provision of rupee mobilisation expenses for construction/turnkey projects. Exporters could also avail of pre-shipment credit in foreign currencies to finance the cost of imported inputs for the manufacture of export products to be supplied under the projects.
- **Refinance of Export Credit:** Authorised dealers in foreign exchange can obtain from Exim Bank, 100% refinance of deferred payment loans extended for the export of eligible Indian goods.

Forfeiting: Forfeiting is a mechanism of financing exports through:

- by discounting export receivables.
- evidenced by bills of exchange or promissory notes.
- without recourse to the seller (*viz.* exporter).
- carrying medium to long term maturities.
- on a fixed rate basis (discount).
- up to 100% of the contract value.

In a forfeiting transaction, the exporter surrenders, without recourse to him, his rights to claim for payment on goods delivered to an importer, in return for immediate cash payment from a forfeiter. As a result, an exporter in India can convert a credit sale into a cash sale, with no recourse to the exporter or his banker.

Bills of exchange or promissory notes, backed by co-acceptance from a bank (which would generally be the buyer's bank), are endorsed by the exporter, without recourse, in favour of the forfeiting agency in exchange for discounted cash proceeds. The banker's co-acceptance is known as *availisation*. The co-accepting bank must be acceptable to the forfeiting agency.

Exim Bank works as a facilitator between the Indian exporter and the overseas forfeiting agency. On a request from an exporter, for an export transaction which is eligible to be forfeited, Exim Bank will obtain indicative and firm forfeiting quotes – discount rate, commitment and other fees – from overseas agencies.

Exim Bank will receive avalised bills of exchange or promissory notes, as the case may be, and send them to the forfeiter for discounting and will arrange for the discounted proceeds to be remitted to the Indian exporter. Exim Bank will issue appropriate certificates to enable Indian exporters to remit commitment fees and other charges.


Advantages to Exporters: Forfeiting offers the following benefits to the exporters

- Converts a deferred payment export into a cash transaction, improving liquidity and cash flow
- Frees the exporter from cross-border political or commercial risks associated with export receivables

Notes

- Finance up to 100% of the export value is possible as compared to 80-85% financing available from conventional export credit programmes
- As forfeiting offers without recourse finance to an exporter, it does not impact the exporter's borrowing limits. Thus, forfeiting represents an additional source of funding, contributing to improved liquidity and cash flow
- Provides fixed rate finance; hedges against interest and exchange risks arising from deferred export credit
- The exporter is freed from credit administration and collection problems
- Forfeiting is transaction-specific. Consequently, a long-term banking relationship with the forfeiter is not necessary to arrange a forfeiting transaction
- Exporter saves on insurance costs as forfeiting obviates the need for export credit insurance
- Simplicity of documentation enables rapid conclusion of the forfeiting arrangement.

Source: www.eximbankindia.com



Task

1. Visit a bank branch in your area. Find out the different schemes on offer for both pre- and post-shipment finance.
2. Visit the offices of SBI Factors or visit their website and prepare a detailed study of the type of schemes offered by them to the exporters. Also explore the success of their schemes against the traditional finance options.

Self Assessment

Fill in the blanks:

1. Concessional interest rates and liberal schemes have been introduced in India by the through the Reserve Bank of India (RBI).
2. credit is provided to the exporters for meeting their need of getting the shipment ready.
3. The amount of PC extended normally will not exceed the value of the export order
4. finance can be granted up to 100% of the invoice value
5. Exim Bank works as a facilitator between the Indian exporter and the overseas agency.
6. In a forfeiting transaction, the exporter surrenders, to him, his rights to claim for payment on goods delivered to an importer, in return for immediate cash payment from a forfeiter.
7. Pre-shipment Rupee Credit is extended to finance funding requirement of export contracts.
8. The purpose of programme is to provide a boost to project export efforts of companies having a good track record and sound financials.
9. is Euro Inter-Bank Offered Rate, the rate released by the European Banking Federation, used for euro inter-bank loan transactions between banks in the euro region.

10. **LIBOR** stands for which refers to the rate of interest at which banks are ready to lend money to each other in London's inter-bank market.

Notes

5.4 Factoring

Forfeiting and factoring are services in international market given to an exporter or seller. Its main objective is to provide smooth cash flow to the sellers. The basic difference between the forfeiting and factoring is that forfeiting is a long-term receivables (over 90 days up to 5 years) while factoring is short termed receivables (within 90 days) and is more related to receivables against commodity sales.

5.4.1 Forfeiting

The terms forfeiting is originated from an old French word 'forfeit', which means to surrender ones right on something to someone else. In international trade, forfeiting may be defined as the purchasing of an exporter's receivables at a discount price by paying cash. By buying these receivables, the forfeiter frees the exporter from credit and the risk of not receiving the payment from the importer.

Forfeiting in International Trade

The exporter and importer negotiate according to the proposed export sales contract. Then the exporter approaches the forfeiter to ascertain the terms of forfeiting. After collecting the details about the importer, and other necessary documents, forfeiter estimates risk involved in it and then quotes the discount rate.

The exporter then quotes a contract price to the overseas buyer by loading the discount rate and commitment fee on the sales price of the goods to be exported and sign a contract with the forfeiter. Export takes place against documents guaranteed by the importer's bank and discounts the bill with the forfeiter and presents the same to the importer for payment on due date.

Documentary Requirements

In case of Indian exporters availing forfeiting facility, the forfeiting transaction is to be reflected in the following documents associated with an export transaction in the manner suggested below:

- **Invoice:** Forfeiting discount, commitment fees, etc. needs not be shown separately instead, these could be built into the FOB price, stated on the invoice.
- **Shipping Bill and GR Form:** Details of the forfeiting costs are to be included along with the other details, such FOB price and commission insurance, normally included in the "Analysis of Export Value" on the shipping bill. The claim for duty drawback, if any is to be certified only with reference to the FOB value of the exports stated on the shipping bill.

Cost Elements of Forfeiting

The forfeiting typically involves the following cost elements:

1. Commitment fee, payable by the exporter to the forfeiter 'for latter's' commitment to execute a specific forfeiting transaction at a firm discount rate with in a specified time.
2. Discount fee, interest payable by the exporter for the entire period of credit involved and deducted by the forfeiter from the amount paid to the exporter against the availed promissory notes or bills of exchange.

Notes

Benefits to Exporter

- **100 per cent financing:** Without recourse and not occupying exporter's credit line that is to say once the exporter obtains the financed fund, he will be exempted from the responsibility to repay the debt.
- **Improved cash flow:** Receivables become current cash in flow and it is beneficial to the exporters to improve financial status and liquidation ability so as to heighten further the funds raising capability.
- **Reduced administration cost:** By using forfeiting, the exporter will spare from the management of the receivables. The relative costs, as a result, are reduced greatly.
- **Advance tax refund:** Through forfeiting the exporter can make the verification of export and get tax refund in advance just after financing.

Risk Reduction

Forfeiting business enables the exporter to transfer various risk resulted from deferred payments, such as interest rate risk, currency risk, credit risk, and political risk to the forfeiting bank.

Increased trade opportunity: With forfeiting, the export is able to grant credit to his buyers freely, and thus, be more competitive in the market.

Benefits to Banks

Forfeiting provides the banks following benefits:

- Banks can offer a novel product range to clients, which enable the client to gain 100% finance, as against 80% to 85% in case of other discounting products.
- Bank gain fee based income.
- Lower credit administration and credit follow up

5.4.2 Factoring

Definition of factoring is very simple and can be defined as the conversion of credit sales into cash. Here, a financial institution which is usually a bank buys the accounts receivable of a company usually a client and then pays up to 80% of the amount immediately on agreement. The remaining amount is paid to the client when the customer pays the debt. Examples includes factoring against goods purchased, factoring against medical insurance, factoring for construction services, etc.

Characteristics of Factoring

1. The normal period of factoring is 90 – 150 days and rarely exceeds more than 150 days.
2. It is costly.
3. Factoring is not possible in case of bad debts.
4. Credit rating is not mandatory.
5. It is a method of off balance sheet financing.
6. Cost of factoring is always equal to finance cost plus operating cost.

5.4.3 Types of Factoring

Notes

1. Disclosed
2. Undisclosed

Disclosed Factoring

In disclosed factoring, client's customers are aware of the factoring agreement. Disclosed factoring is of two types:

- **Recourse Factoring:** The client collects the money from the customer but in case customer don't pay the amount on maturity then the client is responsible to pay the amount to the factor. It is offered at a low rate of interest and is in very common use.
- **Non-recourse Factoring:** In non-recourse factoring, factor undertakes to collect the debts from the customer. Balance amount is paid to client at the end of the credit period or when the customer pays the factor whichever comes first. The advantage of non-recourse factoring is that continuous factoring will eliminate the need for credit and collection departments in the organization.

Undisclosed

In undisclosed factoring, client's customers are not notified of the factoring arrangement. In this case, Client has to pay the amount to the factor irrespective of whether customer has paid or not.

ECGC introduces innovative non-recourse maturity export factoring.

Export Credit Guarantee Corporation of India Ltd. (ECGC) has announced introduction of its non-recourse maturity export factoring. The scheme has certain unique features and does not exactly fit into the conventional mould of maturity factoring. The changes devised are intended to give the clients the benefits of full factoring services through a maturity factoring scheme, thus effectively addressing the needs of exporters to avail themselves of pre-finance (advance) on the receivables, for their working capitals requirements.

One of the major deviations in this regard is the very important role and special benefits envisaged for banks, under the scheme.

The services provided by ECGC under its export maturity factoring scheme are 100 per cent credit guarantee protection against bad debts, sales register maintenance in respect of factored transactions, and regular monitoring of outstanding credits, facilitating due collection in the due date of recovery, at its own cost, of all recoverable bad debts.

Payments would be received by the exporter, in his account, through normal banking channels. In the event of non-realisation of dues on factored export receivables, ECGC will promptly make the payment in Indian currency of an equivalent amount, immediately upon the crystallization of dues by the bank (exchange rate applicable, as on the date of crystallization).

The Corporation would facilitate easier availability of bank finance to its factoring clients by rendering such advances to be an attractive proposition to banks. The factoring agreement that would be concluded by ECGC with its clients has an in-built provision incorporating an on-demand guarantee in favour of the bank without any payment or compliance or other requirements to be satisfied by the bank.

The following are the benefits for exporters under the scheme:

- Option to give easier credit terms to customers – better protection than an ILC, without the need to insist on establishing one.

Notes

- More friendly delivery terms offered, like direct delivery to the customer (as against DP/DA) without any risk.
- Reduced foreign bank handling charges on documents.
- Substantial cost savings and complete freedom in monitoring and follow up (telephones, faxes, follow-up visits) of receivables, overdue bank interest on delayed collections and recovery expenses relating to bad debts.
- Increase in export sales, thanks to more competitive terms offered to customers.
- Better security than letters of credit.
- Elimination of uncertainties relating to realization of accounts receivables resulting in better cash management to meet working capital requirements.
- Full attention to procurement/production, marketing and sales and growth of business, due to freedom from chasing receivables.



Did u know? For banks, it would be a win-win situation all the way. Advances given against ECGC-factored export receivables could become the most preferred export advance portfolio for a bank, even better than the advances granted under an ILC. There is 100 per cent credit protection, free of cost.

The other benefits for banks are:

- Prompt and immediate payment by ECGC of the full amount outstanding on the receivables to the bank, within three days of crystallization of the dues, in the event of non-realization of factored receivables on the due date, without any protracted processing or scrutiny and without raising any queries.
- Savings on post-shipment guarantee premium to be paid to ECGC, if any.
- No pre-disbursal risk assessment or post-disbursal monitoring required of the bank. Full risk is on ECGC, with regard to repayment of the amount due (in rupees).
- Opportunity to build 'zero-risk assets', since the bank would not run any risk on the borrower, the country or on the buyer.
- Banks could earn interest on a priority sector lending, without any of the attendant risks or hassles.
- Opportunity to satisfy additional working capital needs of the customer by sanctioning additional limits without enlarging the exposure risks.

Banks would be furnished with a certified copy of the factoring agreement concluded between the client and ECGC. When a limit is established by ECGC on an overseas customer in favour of an exporter-client, the Corporation would directly communicate to the concerned bank branch all relevant details of the limit available to the exporter on that specified overseas customer, and would confirm in writing its obligations to the bank in respect of advances it may grant against such ECGC-factored export receivables.

The bank's role lies in encouraging exporter-customers to explore the possibility of availing of the factoring facility from ECGC. Factoring, being a high-risk premium product, could be made available only in respect of receivables due from select customers.

Banks may consider sanctioning of additional limits to exporters against risk-free advances when ECGC communicates setting up of the factoring facility and the permitting limit in respect of individual buyers.

Banks also could help ECGC to collect factoring charges on each of the factored invoices. ECGC covers every facet of the exporter's risks. It is the only corporation that is committed to taking your exports higher.

Notes



Task What is factoring and write a note on characteristics and different types of factoring.

5.5 Types of Risk and Insurance

International transactions are full of risks of various types. The exporter faces a number of risks when he ships the goods to a foreign importer in another country. It is better to know about the risks in advance that the exporter is able to take appropriate insurance cover for different pitfalls. Risk means uncertainty concerning occurrence of a loss. This means that the exporter, while shipping goods, is in a state of uncertainty about various happenings that could result in loss. There is a possibility of something going wrong somewhere that could spell loss. Exports usually involve a certain size, that is, even a very small order will normally carry a reasonable value. This value faces possibilities of damage/loss. The exporter needs to have a comprehensive understanding of different types of such possibilities, in order to enable him to take preventive measures.

Let us discuss various risk and insurances polices under ECGC.

Export Credit Guarantee Corporation (ECGC)

Export Credit Guarantee Corporation of India Limited was set up in the year 1957 by the Government of India to strengthen exports by covering the payment risk in exports. The basic purpose of ECGC is to provide credit risk insurance to Indian exporters in a manner that helps them export free from the fear of loss, resulting from non-payment either due to credit or political reasons. Credit risk insurance provides protection to exporters who ship their goods on credit to their foreign buyers, thus running the risk of non-payment.

ECGC functions as an export promotion organisation under the administrative control of the Ministry of Commerce, Government of India. The fifth largest credit insurer in the world, they provide a range of credit risk insurance covers to exporters and bankers against payment losses involved in export trade.

ECGC provides:

- (i) A range of credit risk insurance covers to exporters against loss in export of goods and services.
- (ii) Guarantees to banks and financial institutions to enable exporters obtain better facilities from them.
- (iii) Special schemes like Overseas Investment Insurance to Indian companies investing in joint ventures abroad in the form of equity.

Exporters in India can make use of the services provided by ECGC in various ways. They can make use of the ECGC cover to offer more competitive payment terms to their foreign buyers. ECGC cover helps them borrow working capital from commercial banks at special rates for their export transactions. ECGC also provides a credit check on foreign buyers. ECGC has tied up with Dun & Bradstreet Corporation and together they have launched a website called www.indianexportregister.com. This supports Indian exporters in global markets and aids international buyers in sourcing products from credible Indian exporters. It contains a comprehensive list of Indian exporters and is being used extensively by overseas buyers.

Notes

Exporters can showcase their products on the website through on-line catalogue and premium listings. This way, ECGC is also helping exporters in India to market their products to buyers across the world.

The major benefits offered by ECGC to the Indian exporters can be summarised as:

- (i) Offers insurance protection to exporters against payment risks.
- (ii) Makes it easy for Indian exporters to obtain export finance from banks/financial institutions.
- (iii) Makes available information to exporters on different countries with its own credit ratings.
- (iv) Provides information to exporters in India on credit-worthiness of foreign importers.
- (v) Provides guidance to Indian exporters in export-related activities.
- (vi) Helps exporters in recovering bad debts.

ECGC Products and Services: The various offerings of ECGC are:

1. *Credit Insurance Policies*

- ❖ SCR or Standard policy
- ❖ Turnover policy
- ❖ Small Exporter's policy
- ❖ Specific Shipment policy short-term
- ❖ Buyer-wise policy short-term
- ❖ Consignment Exports policy
- ❖ Buyer Exposure policies
- ❖ IT-Enabled Services (Specific Customer) policies
- ❖ Insurance cover for buyer's credit and line of credit

2. *Guarantees to Banks*

- ❖ Packing Credit Guarantee
- ❖ Export Production Finance Guarantee
- ❖ Post Shipment Credit Guarantee
- ❖ Export Finance Guarantee
- ❖ Export Performance Guarantee
- ❖ Export Finance (Overseas Lending) Guarantee

3. *Maturity Factoring*

4. *Special Schemes*

- ❖ Transfer Guarantee
- ❖ Overseas Investment Insurance
- ❖ Exchange Fluctuations Risk Cover
- ❖ Constructions Work Policy
- ❖ Specific Policy for Supply Contract

5.5.1 Standard Policy

Notes

Standard Policy offers to cover risks in respect of all shipments on short-term credit (credit not exceeding 180 days) by exporters with an anticipated annual turnover of more than ₹ 50 lakhs. This policy is also called Shipment (Comprehensive Risk) Policy or SCR. Standard Policy covers the following commercial and political risks from the date of shipment:

Commercial Risks

- Insolvency of the buyer.
- Failure of the buyer to make the payment due within a specified period, normally four months from due date.
- Buyer's failure to accept goods, subject to certain conditions.

Political Risks

- Imposition of restriction by the government of the buyer's country or any government action, which may block or delay the transfer of payment made by the buyer.
- War, civil war, revolution or civil disturbances in the buyer's country.
- New import restrictions or cancellation of a valid import licence in the buyer's country.
- Interruption or diversion of voyage outside India resulting in payment of additional freight or insurance charges, which cannot be recovered from the buyer.
- Any other cause of loss occurring outside India, not normally insured by general insurers, and beyond the control of both exporter and buyer.

5.5.2 Turnover Policy

Turnover policy is a variation of the standard policy for the benefit of all large exporters who pay a total premium of ₹ 10 lakhs or more in a year. It envisages projection of the export turnover of the exporter for a year and the initial determination of the premium payable on that basis, subject to adjustment at the end of the year based on actuals. The policy provides additional discount in premium with an added incentive for increasing exports beyond the projected turnover and also offers simplified procedure for premium remittance and filing of shipment information. It also provides for higher discretionary credit limits on overseas buyers, based on the total premium paid by the exporter under the policy. The turnover policy is issued with a validity period of one year. In most other respects, the provisions relating to standard policy apply to turnover policy.

The holders of turnover policy need not submit monthly declarations of shipment. Instead, they have only to submit a statement of shipments made during the quarter in a prescribed format within 30 days of the end of the quarter.

The basic premium rates applicable for the standard policy will apply to the turnover policy also. However, an exporter holding a standard policy opting for turnover policy will be entitled to an additional discount of 10% over and above the 'no claim bonus' which he enjoys under the standard policy, subject to a minimum total discount of 20%. If an exporter not holding the standard policy avails of the turnover policy, he will be entitled to a discount of 20%. In case of no claims in future, the exporter will be entitled to a further 'no claim bonus' and consequently total discount. Thus, the total discount could go up to 60%.

Notes

Premiums calculated on the projected turnover are payable in four quarterly installments. However, the facility of monthly payment of premium can also be granted on a case-to-case basis.

At the end of the year, if the premium payable on the basis of the actual turnover is less than the premium paid on the basis of the projected turnover, the excess amount paid will be carried forward to the next policy period which could be adjusted in the premium for the first quarter of the renewed policy. In case the policy is not renewed, and if the difference between premium paid and premium payable is more than 10%, the same will be refunded, subject to marginal adjustments.



Did u know? If the premium payable on the basis of the actual turnover exceeds the projected premium by not more than 10%, the excess premium need not be paid and if it exceeds by more than 10%, only the excess of the premium over 10% needs to be paid.

5.5.3 Small Exporter's Policy

This is another version of the Standard Policy, aimed at encouraging small exporters to obtain and operate the policy. It is issued to exporters whose anticipated export turnover for the period of one year does not exceed ₹ 50 lakh. The salient features of this policy that set it apart from the Standard Policy are:

- Small Exporter's Policy is issued for a period of 12 months.
- Premium payable is determined on the basis of projected exports on an annual basis, subject to a minimum premium of ₹ 2000 for the policy period.
- No claim bonus in the premium rate is granted every year at the rate of 5%.
- Shipments need to be declared quarterly.
- Small exporters are required to submit monthly declarations of all payments remaining overdue by more than 60 days from the due date.
- For shipments covered under the Small Exporter's Policy, ECGC will pay claims to the extent of 95% where the loss is due to commercial risks, and 100% if the loss is caused by any of the political risks.
- The normal waiting period for claims under the Small Exporter's Policy is two months.
- In order to enable small exporters deal with their buyers in a flexible manner, following facilities are allowed:
 - (i) A small exporter may, without prior approval of ECGC convert a D/P bill into D/A bill, provided he has already obtained suitable credit limit from the buyer on D/A terms.
 - (ii) Where the value of this bill is not more than ₹3 lakh, conversion of D/P bill into D/A bill is permitted even if the credit limit on the buyer has been obtained on D/P terms only, but only one claim can be considered during the policy period on account of losses arising from such conversions.
 - (iii) A small exporter may, without prior approval of ECGC, extend due date of payment of a D/A bill provided a credit limit on the buyer on D/A terms is in force at the time of such extension.

5.5.4 Insurance Cover for Buyer's Credit and Line of Credit

Notes

Buyer's Credit refers to credit extended by a bank in India to a foreign buyer enabling him to pay for machinery and equipment that he may be importing from India for a specific project. A Line of Credit is a credit extended by a bank in India to an overseas bank, institution or government, for the purpose of facilitating import of a variety of listed goods from India into the foreign country. A number of importers in the overseas country may be importing the goods under one Line of Credit.

ECGC has come out with schemes to protect lending banks from certain risks of non-payment. These covers take the form of an agreement between the lending bank and ECGC and are issued on a case-to-case basis. Credit terms and the length of the credit period should be in conformity with what is appropriate for the export of the relevant items. There should be adequate security for repayments to be made by the borrower. Cover can be granted either for political risks or for comprehensive risks. The premium rates applicable to comprehensive risk cover will naturally be higher than that for political risks cover. Normally, ECGC covers up to 85% of the loss.

The premium rates depend on the country to which exports are made and the period of repayment. At least 20% of the total amount of premium should be paid in advance. The balance amount of premium may be paid on a quarterly basis in proportion to the amount of credit disbursed.

The various guarantees given to banks are presented below:

- Packing Credit Guarantee to enable banks to provide pre-shipment advances to exporters for manufacturing, processing, purchasing or packing of goods meant for exports against a firm export order.
- Export Production Finance Guarantee to enable banks sanction advances at the pre-shipment stage to the full extent of cost of production when it exceeds the FOB value of the contract/order, the difference representing incentives receivable.
- Post Shipment Credit Guarantee to enable banks to extend post-shipment finance to exporters through purchase, negotiation or discounting of export bills or advances against such bills.
- Export Finance Guarantee covers post-shipment advances granted by banks to exporters against export incentives receivables like duty drawback.
- Export Performance Guarantee a counter-guarantee to protect a bank against losses that it may suffer on account of guarantee given by it on behalf of the exporters.
- Export Finance (Overseas Lending) Guarantee to protect a bank financing an overseas project, by providing a foreign currency loan to the contractor from the risk of non-performance.

5.5.5 Special Schemes

Presented below is a brief description of the different special schemes offered by ECGC:

- Transfer Guarantee to safeguard banks in India against losses on account failure of a foreign bank to reimburse it with the amount paid to an exporter, when an Indian bank has added a confirmation to a letter of credit opened by the foreign bank.
- Overseas Investment Insurance to cover the risks on account of war, expropriation or restriction on remittances to Indian investments made by way of equity capital or untied loan for the purpose of setting up or expansion of overseas projects.
- Exchange Fluctuations Risk Cover to provide protection from exchange rate fluctuations to exporters of capital equipment, civil engineering contractors, and consultants who

- Notes** have to receive payment over a period of years for their exports, construction works, or services.
- Constructions Work Policy to provide cover to an Indian contractor who executes a civil construction job abroad.
 - Specific Policy for Supply Contract to cover risks in respect of export of capital goods or turnkey projects involving medium/long term credit.

5.5.6 Exchange Rate Fluctuation Risks

Both importers and exporters run the risk of loss due to fluctuations in the foreign exchange rates in international business transactions. An exporter who agrees to a certain price in a foreign currency today may find himself at a loss after a few months when he actually receives the payment owing to a fall in the exchange rate of the contracted currency. Likewise, an importer's fortunes may also swing up or down with exchange rate movements. For example, let us take an exporter in India who ships 5,000 shirts at US \$ 4 each to an exporter in the US, and expects to receive the payment after 60 days. In today's date at \$1.00 = ₹46.00, he expects a payment of ₹ 9,20,000. After the months, on actual receipt of payment, the US\$ is equal to ₹ 45.30 and he, therefore, receives ₹ 9,06,000, incurring a loss of ₹14,000. This loss is actually due to weakening of the US \$ against the Indian rupee.

Exporters in India can avail of forward exchange covers provided by most commercial banks. See the box 5.2:

Box 5.2: Treasury Products: Foreign Exchange



Treasury Products: Foreign Exchange

We have a state-of-the-art dealing room situated at Nariman Point, Mumbai. The dealing room handles inter-bank transactions and corporate foreign exchange flows generated by the various branches.

Products

- Spot foreign exchange transactions (for value up to two business days).
- Forward foreign exchange transactions (for value greater than two business days).
- Inward/outward remittances.
- Derivatives such as options, currency swaps, etc.

Services

- Active dealings in the inter-bank market for major currencies, spot and forwards.
- Quick and competitive dealing in prices in major currencies.
- Customised solutions for specific client exposures.
- Trading recommendations based on technical analysis.
- Regular fundamental analysis.
- Established correspondent banking relationships.

Source: www.kotak.com

Foreign exchange rates are usually quoted as Spot Rates or Forward Rates.

Notes

1. **Spot Rates:** For immediate requirement of foreign currency, the purchaser has no choice but to buy foreign exchange on the spot (current) market. Spot rates are meant for immediate delivery. It is simply the current market rate decided by demand and supply. Spot contracts are the most basic and widely used foreign exchange contracts. This is an agreement to buy or sell one currency in exchange for another.



Notes Spot transaction requires the receipt of the bought currency in two days and the payment of the sold currency in two days.

2. **Forward Rates:** A forward contract allows the exporter to buy or sell one currency against another, for settlement on some future date. A forward contract eliminates the risk of fluctuating exchange rates by locking in a price today for a transaction that will take place in the future. It does not eliminate losses occurring in future but it makes the outcome of the future transaction certain. This is called hedging for expected foreign currency transactions. A forward foreign exchange contract protects the exporter from adverse currency movements. The forward rate adjustment is a complicated calculation that involves the interest rates of the currencies involved.

The following hedging alternatives are available to exporters in India to deal with foreign exchange fluctuations risks:

- ❖ **Option Dated Forward Contract:** Forward transactions that offer one of the parties to the transaction an option to set any value date within a prescribed period. Such options benefit the party as he may not know in advance the precise date on which he would be able to deliver the currency. An option forward contract helps a company overcome market risk by deciding today, a price for a foreign exchange transaction at a future date.
- ❖ **Foreign Currency Options:** A currency option gives the buyer the right, not the obligation, to exchange two currencies at a fixed rate at a future point of time. Under this type of option, the buyer's downside risk is eliminated while retaining the unlimited upside potential. It is akin to an insurance policy. It is an effective 'hedging mechanism' that permits exchange of one currency for another on a given date, at a pre-arranged exchange rate (strike price), without an obligation to do so. The option may not be used, if the spot rate is more favorable than the option's strike price. With such instruments the buyer is protected against an adverse exchange rate movement while retaining the ability to benefit from a favourable movement. As the name indicates, the party has the option to deal or not. European options allow the exercise of an option on the expiry date only. American options permit the exercise of an option at any time from the date of purchase until expiry.
- ❖ **Currency Swaps:** A currency swap is defined as an exchange of principal and/or interest payments on a loan or asset in one currency for principal and/or interest payments on equivalent loan or asset in another currency at pre-fixed spot/forward rate agreed on the trade date.



Example: Customer in India having a loan in USD may enter into a currency swap in order to hedge its USD interest rate risk as well as the USD/INR exchange risk. Under this type of swap, the client may cover either only interest payment or principal repayment or both.

Notes



Note ECGC also offers a special scheme called Exchange Fluctuations Risk Cover to provide protection from exchange rate fluctuations to exporters of capital equipments, civil engineering contractors, and consultants who have to receive payments over a period of years for their exports, construction works, or services.



- Task*
1. Visit ECGC's website and explore the various credit risk insurance schemes in greater details.
 2. Survey five exporters in your area and find out about their dealings with ECGC.
 3. Visit the website of any general insurance company in India and study the Marine Insurance options available for exports in detail.

5.6 Quality and Pre-Shipment Inspection

The Export Inspection Council (EIC) was set up by the Government of India under Section 3 of the Export (Quality Control and Inspection) Act, 1963 (22 of 1963), as an advisory body to the Central Government, which is empowered to:

- Notify commodities which will be subject to quality control and/or inspection prior to export,
- Establish standards of quality for notified commodities,
- Specify the type of quality control and/or inspection to be applied to such commodities.

Its main activities include:

- Certification of quality of export commodities through installation of quality assurance systems (in-process quality control and self-certification) in exporting units as well as consignment-wise inspection.
- Issue of different types of certificates such as health, authenticity, etc. to exporters under various product schemes for export.
- Training and technical assistance to the industry in installation of Quality and Safety Management Systems based on principles of Hazard Analysis Critical Control Point (HACCP), ISO-9001: 2000, ISO: 17025 and other related international standards, laboratory testing, etc.
- Recognition of Inspection Agencies as per ISO: 17020 and Laboratories as per ISO: 17025 and utilising them for export inspection and testing.

5.6.1 Export Certification Systems

The following Export Certification Systems are available with EIC:

Consignment-wise Inspection- Under this system, each export consignment is inspected and tested by the recognised inspection agency. Samples are drawn using statistical methods and the shipment is tested against prescribed standards. These tests may be carried out either in the field or at any recognised laboratory, depending upon the requirements. If the goods pass

the test, a certificate to that effect is issued that enables the exporter to gain clearance at customs.

In-Process Quality Control- This system emphasises the need to exercise quality control at the process stage. To this end, EIAs approve certain units against applications received in the prescribed format, as possessing adequate levels of quality control systems in all relevant areas, based on its own thorough assessment carried out by a panel of Inter-departmental experts. Units thus approved are granted an option either to issue the certificate of inspection of export worthiness on their own or to obtain the certificate of inspection from EIAs representatives keep making spot checks on such units from time to time.

Self-Certification- This system provides for additional stringent norms over and above in process quality control (IPQC) procedures in the crucial areas of design and development, quality audit, after sales service, housekeeping and maintenance. An export unit needs to apply to the EIA in the prescribed format. Upon receipt of the application, EIA representatives carry out a thorough inspection of the facilities and quality control systems in use at the exporter's premises, particularly in the four designated areas. Once satisfied, the unit is recognised by the Government of India as being capable of issuing certificates of export worthiness for their own export consignments.

Relaxations from Compulsory Pre-shipment Inspection

The following relaxations have been granted from pre-shipment inspection:

- All the star trading houses as well as Industrial Units in Export Processing Zones and 100% Export Oriented Units have been exempted from the purview of Compulsory Pre-shipment Inspection.
- Units approved by EIAs under the system of In-process Quality Control (IPQC) have been authorised to issue statutory certificates by themselves.
- Items which were hitherto subjected to compulsory pre-shipment inspection have been exempted from the same, provided the exporter has a firm letter from the overseas buyer stating that the overseas buyer does not require pre-shipment inspection from any official Indian inspection agencies.


Recognition to Inspection Agencies

EIC operates a scheme to recognise inspection agencies for carrying out the pre-shipment inspection on its behalf. Any agency desiring recognition as an inspection agency for any of the notified commodities under the Act needs to furnish an application in duplicate in the prescribed proforma accompanied by an application fee of ₹ 5,000 (non-refundable) as given in the Schedule of Fee in Clause 9 and a copy of its Quality Manual.

5.6.2 Pre-shipment Inspection as per Requirements of the Buyer

We have understood the mechanism of compulsory pre-shipment inspection as required by the Government of India through its network of EIC and EIAs. However, the foreign buyer may waive of this compulsory inspection by a government recognised agency but may insist on pre-shipment inspection by an independent agency nominated for the purpose by him or his own agent. In such cases, the exporter will receive instructions from the buyer and he must follow the same religiously.

Notes

	<p><i>Task</i></p> <ol style="list-style-type: none">1. Visit Export Inspection Council's website and learn about the various schemes that it operates to facilitate pre-shipment inspection in India.2. Interview a few local exporters and compare the quality control practices being followed by them.
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Self Assessment

Fill in the blanks:

11. may be defined as the purchasing of exporters receivables at a discount price by paying cash.
12. Forfeiting business enables the exporters to transfer various risk resulted from
13. is defined as the conversion of credit sales into cash.
14. Factoring is a method of financing.
15. ECGC announced introduction of its

5.7 Summary

- Pre-shipment finance facilities offer liquidity to the exporter to procure raw materials, carry out processing, packing, transporting and warehousing of the goods to be exported. Post-shipment finance provides credit facility from the date of shipment of the goods to the time export payment is realized.
- Pre-shipment finance is generally offered as Packing Credit (PC). The exporter will have to submit the PC application along with required documents. Bank will satisfy itself with document scrutiny and physical verification before sanctioning the loan. This facility is also extended in foreign currency. The outstanding loan amount in a PC account has to be settled out of the proceeds of the exported goods as soon as the documents drawn for the same are discounted. At this moment, the pre-shipment loan actually gets converted into post-shipment credit.
- Post-shipment loan runs from the date of extending credit, after shipment of goods to the date of realization of export proceeds. The options available to the exporter for Post-shipment credit include Export bills purchase/discounting.
- EXIM Bank (Export Import Bank of India) is the principal financial institution in the country for coordinating working of institutions engaged in financing exports and imports. The bank provides competitive finance at various stages of the export cycle. The principal fund-related services of the bank include Lines of Credit, Supplier's Credit, Overseas Buyer's Credit, Loan under FREPEC Programme – Financing Rupee Expenditure for Project Export Contracts, Pre-shipment Rupee Credit, Refinance of Export Loans and Forfeiting.
- In a forfeiting transaction, the exporter surrenders, without recourse to him, his rights to claim for payment on goods delivered to an importer, in return for immediate cash payment from a forfeiter. As a result, an exporter in India can convert a credit sale into a cash sale, with no recourse to the exporter or his banker. Exim Bank works as a facilitator between the Indian exporter and the overseas forfeiting agency.

- In international trade, forfeiting may be defined as the purchasing of an exporter's receivables at a discount price by paying cash. By buying these receivables, the forfeiter frees the exporter from credit and the risk of not receiving the payment from the importer.
- Export Credit Guarantee Corporation of India Ltd. (ECGC) has announced introduction of its non-recourse maturity export factoring. The scheme has certain unique features and does not exactly fit into the conventional mould of maturity factoring.
- Pre-shipment inspection in India is conducted for quality control of export goods under the overall supervision of the Export Inspection Council (EIC), which falls under the Ministry of Commerce, Government of India. The Export Inspection Council (EIC) was set up by the Government of India under Section 3 of the Export (Quality Control and Inspection) Act, 1963 (22 of 1963), as an advisory body to the Central Government, which is empowered under the Act to: Notify commodities which will be subject to quality control and/or inspection prior to export, establish standards of quality for such notified commodities and specify the type of quality control and/or inspection to be applied to such commodities.

5.8 Keywords

Currency Swaps: A currency swap is defined as an exchange of principal and/or interest payments on a loan or asset in one currency for principal and/or interest payments on equivalent loan or asset in another currency at pre-fixed spot/forward rate agreed on the trade date.

ECGC: Export Credit Guarantee Corporation of India Limited was set up in the year 1957 by the Government of India to strengthen exports by covering the payment risk in exports.

EXIM Bank: Export-Import Bank of India, set up in 1982, for the purpose of financing, facilitating, and promoting foreign trade in India,

Foreign Currency Options: A currency option gives the buyer the right, not the obligation, to exchange two currencies at a fixed rate at a future point of time.

Non-recourse Factoring: In non recourse factoring, factor undertakes to collect the debts from the customer. Balance amount is paid to client at the end of the credit period or when the customer pays the factor whichever comes first..

Post-shipment Finance is provided at concessional interest rates as per RBI guidelines. The proof of shipment of goods, serves as the basis of grant of such facility.

Pre-shipment Credit: It is provided to the exporters for meeting their need of getting the shipment ready.

Recourse Factoring: The client collects the money from the customer but in case customer don't pay the amount on maturity then the client is responsible to pay the amount to the factor. It is offered at a low rate of interest and is in very common use.

Turnover Policy: Turnover policy is a variation of the standard policy for the benefit of all large exporters who pay a total premium of ` 10 lakh or more in a year.

5.9 Review Questions

1. What is the need for export finance? Discuss the two types of facilities available keeping in view the export cycle.
2. Discuss pre-shipment finance in foreign currency in detail.

- Notes**
3. What are the different types of post-shipment finance? Is post-shipment finance also available in foreign currency?
 4. What is the difference between Factoring and Forfeiting? Explain with the help of flow charts.
 5. Discuss the role being played by Exim Bank of India to help exporters with finance.
 6. What is Pre-shipment Inspection? What are the various methods of certification available to Indian exporters?
 7. Write a detailed note on EIC and its functioning.
 8. Write short notes on: (i) IPQC, (ii) EIAs, (iii) Recognition of Inspection Agencies by EIA, (iv) Benefits of Pre-shipment Inspection, (v) Relaxation from Compulsory Pre-shipment Inspection.

Answers: Self Assessment

1. Commerce Ministry
2. Pre-shipment
3. FOB
4. Post-shipment
5. forfeiting
6. without recourse
7. temporary
8. Finance for Rupee Expenditure for Project Export Contracts (FREPEC)
9. EURIBOR
10. London Inter-Bank Offer Rate
11. Export forfeiting
12. Deferred Payments
13. Factoring
14. Off balance sheet
15. Non-renewable maturity export factoring

5.10 Further Readings



Books

Aseem Kumar, *Export and Import Management*: 2007, Excel books.

Cherenilan Francis, *International Economics*, 4th Edition, Tata McGraw-Hill Publishing Company Limited.

Dr. Ram Singg, *International Trade Operations*, Excel books, 2009.

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Notes



Online links

http://commerce.nic.in/publications/pdf/CHAPTER_6.pdf

<http://commerce.nic.in/annual2006-07/html/chapter11.html>

<http://www.mbaknol.com/international-finance/export-credit-guarantee-corporation-of-india-ecgc/>

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Notes



Case Study

Increasing the Effectiveness of Pre Shipment Inspection Services

“Preshipment inspection services can improve customs administration, but they are no substitute for comprehensive reform”.

Preshipment inspection refers to the verification of unit prices as well as the examination and reporting of the quantity and quality of exports before they are shipped to the importing country. Preshipment inspection can help control overinvoicing or underinvoicing of imports, misclassification of imports, undercollection of taxes on imports, and misappropriation of donor funds provided for import support. Other possible benefits of preshipment inspection include monitoring of origin and of compliance with national regulations and tariff exemption schemes, better data management, technical assistance and training, trade facilitation and consumer protection.

Preshipment inspection services can provide information that is not readily available to customs authorities in small countries. Such services are provided by private companies in the exporting country. Thus, preshipment inspection can be thought of as a temporary quasi-privatization or contracting out of selected customs functions to meet specific objectives.

Of the various objectives for customs reform, trade facilitation is arguably the most important for efficiency and growth. Because of the potential long-term gains from reform, governments should focus on implementing an effective program for customs modernization and institutional reform, and not view preshipment inspection services as a substitute for this effort. This note reviews recent evidence on the effectiveness of preshipment inspection services; for a comprehensive assessment of preshipment inspection issues through 1994.

Use of Preshipment Inspection Services

The 1993 ratification of the World Trade Organization’s Agreement on Preshipment Inspection gave preshipment inspectors new legitimacy in international trade. Since then the number of countries using pre-shipment inspection has increased from 27 to 37, with Africa having the most active programs.

Perhaps the most striking change in recent years has been the increase in the number of split contracts. While in 1993, Peru was the only Latin American country allowing importers to choose the company they wish to employ from a pre-approved list, in 1999 all Latin American user countries had adapted this approach. This change has allowed more providers to participate. Iran’s program involves 16 providers of inspection services.

The shift in preshipment inspection work away from capital flight and over invoicing toward customs and underinvoicing is reflected in recent contracts. In 1993 all active contracts embodied at least a small amount of capital flight work, but today most contracts focus exclusively on customs work to minimize opportunities for tax evasion—reflecting today’s more liberalized capital regimes.

Usefulness of Preshipment Inspection Services

In general, preshipment inspection is a second-best policy for countries with serious weaknesses in customs administration. Wherever feasible, a preferred approach would

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combine a relatively open capital account (reducing incentives for overinvoicing as a capital flight mechanism), trade liberalization (reducing incentives for underinvoicing as a tax evasion mechanism), and local institution building aimed at improving all customs functions.

But a practical tension often arises. Institution building and structural revenue changes take time. Shorter-term revenue requirements are often pressing in countries that rely on trade taxes as an important source of government revenue. Different views on the effectiveness of preshipment inspection reflect different policy priorities as well as a lack of clear empirical evidence on impact. Consider the three main functions of preshipment inspection.

Disbursement Verification

Low (1995) finds that the World Bank's policy of encouraging governments to use preshipment inspection—and sometimes requiring it as a loan condition—has been driven by concerns about the use of donor funds. This rationale is in line with basic Bank procurement guidelines on import documentation for investment operations.

In addition, the desire to ensure the efficient use of funds through a trade verification procedure is relevant for loans with disbursements that are linked not to the inputs needed to implement specific investments, but rather to balance of payments support through procurement of general imports. In such cases there is a need to verify that prohibited goods are not procured or that agreed goods are procured. Where governments have poor statistical capacity, preshipment inspection can provide useful evidence. But no study exists on the benefits and costs of alternative forms of disbursement verification.

Revenue Collection

Probably the most important reason that governments seek preshipment inspection services is to deal with inefficient or corrupt customs administrations. Such administrations introduce distortions through widespread evasion of trade taxes, either through misspecification of quantity, misclassification of tariff heading, or undervaluation of goods.

It is not easy to directly assess the costs and benefits of preshipment inspection in this area. Preshipment inspection services are often introduced at the same time as policy reforms affecting revenue collections and customs performance, and the full benefits depend on other government actions. Moreover, many preshipment inspection programs have been poorly implemented by administrations that did not want the services because they would reduce available rents.

Although reported revenue savings generally exceed preshipment inspection fees — which are about 1 percent of the value of inspected goods—case studies suggest that the information provided by preshipment inspection companies has often been disregarded, so potential revenue increases have not been realized. Revenue collection shortfalls of up to 50 percent are reported to have occurred in some countries.

Unless governments consistently use a reconciliation system and act on generated information, preshipment inspection will not contribute much to revenue collection. For sustainable revenue collection, customs modernization and institutional reform are also needed, and should specify how preshipment inspection services will be phased out over time. Ideally, this should be a prerequisite for any country signing a preshipment inspection contract.

Trade Facilitation

Opponents often argue that preshipment inspection hinders the flow of goods with the rest of the world. They point out that at best, preshipment inspection creates a series of

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Notes

additional costly steps for traders—and at worst, results in further costs and delays when customs authorities duplicate control functions and question the findings of pre-shipment inspectors. The extra cost is alleged to be especially burdensome for small exporting firms.

Most evidence in this area is anecdotal, and not a single complaint has been lodged under the World Trade Organization's Pre-shipment Inspection Agreement. A plausible explanation is that affected firms must file complaints as identifiable corporate entities, which they may be reluctant to do for fear of jeopardizing commercial relationships.

On the other hand, the Indonesia Chamber of Commerce has argued that preshipment inspection facilitated trade by speeding up the de-douanement (clearing of customs) process. This is an area where further quantification of impact would be helpful. The ultimate objective for customs should be a fully integrated export and import system based on a single submission of minimal control data for all official purposes, backed by upgraded information systems and technical staff trained in risk assessment and prevailing (see UN 1995). With recent advances in information technology, automation, Internet use and electronic data interchange, and business practices such as risk management systems, such an approach should be feasible for most countries if there is political will for change.

Overall, for preshipment inspection to make a positive contribution, it appears essential to ensure:

- Transparent procurement rules for the preshipment inspection contract.
- Preshipment inspection values and classification are an integral part of import documents.
- Good use of provided services (with reconciliation by the ministry of finance as a minimum).
- Arbitration provisions to settle disputes swiftly without holding up goods.
- Enhanced competition for service provision and fee setting (see below).

Options for Increased Competition

How can preshipment inspection services be made an effective transitional instrument for improving revenue collection and facilitating trade?

Competition among Service Providers

A careful assessment is needed of the benefits and costs of parallel competition (split contracts) and serial competition (bidding for a time-bound monopoly franchise, either at the country level or within a certain area). With split contracts, the benefits of competition need to be weighed against higher transactions costs and possibly perverse incentives. With advances in information and control technology, the government's transactions costs in monitoring several suppliers and ensuring effective reconciliation need not be significantly more burdensome. But split contracts can create conflicts of interest, because importers may threaten to switch to another service provider if they are not assessed sufficiently low duty payments. It would be useful to explore why so many Latin American countries have adopted this model, and what other forms of parallel competition might be conducive to increased competition.

For serial competition, the challenge is to design and supervise a bidding process that awards contracts often enough to render the market contestable. With both contract options, termination clauses are desirable for poor performance. It would also be desirable to explore the commercial feasibility of allowing fuller price competition, where pricing

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reflects actual services rendered rather than the current *ad valorem* practice. For instance, bulk goods such as wheat or petroleum could be exempted or should face lower fees.

Competition to Strengthen Customs Administration

Even though preshipment inspection services are described by the industry as temporary, a number of countries have been using them for more than 10 years without concomitant customs modernization. Although one possible solution is to insist on a clearer link between preshipment inspection and customs reform, there may be a basic conflict of interest in appointing a preshipment inspection company as the primary external agent responsible for customs modernization. If the company is successful in customs modernization, it closes off far more profitable flows from preshipment inspection work.

Governments should consider separating preshipment inspection support from customs modernization assistance. This does not preclude governments from using the customs modernization skills of preshipment inspection companies, but merely ensures that a distinct agent be responsible for modernization. That agent could include a preshipment inspection company not participating in the country's preshipment inspection work. Such unbundling can facilitate different fee structures for distinct lines of business, making it easier for prices to reflect services rendered

Question:

Discuss the usefulness of preshipment inspection services.

Notes

Source: <http://www1.worldbank.org/prem/PREMNotes/premnote53.pdf>

Unit 6: Custom Clearance of Import and Export Cargo

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Objectives

After studying this unit, you will be able to:

- Explain Procedure for clearance of imports cargo
- Discuss Custom clearance of export cargo
- Describe Custom valuation
- Explain The harmonized system
- Describe Carnets
- Discuss New developments in custom clearance procedure

Introduction

The provisions under Section 12 of Customs Act 1962 have given the right to customs officials to impose duty on imports as well as exports that originate from the country and go out of the country. The Government of India has prescribed the rate of duty to be imposed under Customs Tariff Act, 1975. Import duty is levied on almost all items in order to restrict unnecessary imports and save precious foreign exchange for the nation, while export duty is levied only on a few limited products, where there is scarcity of Indian products for domestic requirements and the government wants to control the exports of such products or services so as to meet domestic demands. This is done by imposing exports duty on goods and services that go out of the country; thereby making such items expensive to international buyers.



Caution Raising revenue from customs is an important contributor to various expenses of the Central Government and customs duty is one of the main contributors to exchequer.

The main purposes for which customs act has been enacted are as:

1. Regulating the exports and imports of the country in a free and transparent manner according to the laws of the land and controlling illegal trade in drugs and narcotics.
2. Protecting Indian industry from dumping of goods from other countries by imposing antidumping duties and countervailing duties on such country products.
3. Collecting revenue by imposing customs duty on various exportable and importable items from the country so as to meet the developmental requirement of other agencies.

In addition to the above, Indian Customs has been assigned many other activities. Important among them are as follows:

1. Collecting the customs duties as per the Customs Tariff Act, 1975 on exports and imports by following procedure under Customs Act, 1962;
2. Ensuring that the various provisions of the Customs Act 1962 are enforced which has been enacted for the sake of regulating exports and imports of products and services, travel baggage, postal and courier articles and rules for arrival and departure of vessels, air crafts, etc.
3. Ensuring that Customs officials are able to discharge their duties and function under the legal provisions of various customs related Acts for the prohibitions and restrictions on exports and imports which are announced by government of India from time to time.
4. Ensuring that there shall be no drug trafficking, smuggling or narcotics and taking all preventive measures to control them.
5. Processing the facilitating the baggage clearance for international passengers.

6.1 Procedure for Clearance of Imports Cargo

The various procedure for clearance of import cargo are discussed below:

6.1.1 Bill of Entry – Cargo Declaration

1. **Intimation to Customs through IGM:** When goods are imported they are subject to certain duty to be imposed as per customs rules and regulations. The importer has to inform to customs department through Bill of Entry about the arrival of vessel/aircraft. He can submit such bill of entry thirty days in advance so as to process the customs clearance works speedily. As soon as the ship reaches the port, the importer or his CHA has to submit an IGM (Import General Manifest) to the customs official. No cargo can be unloaded or moved without the permission of customs from the port/air cargo station.
2. **Transshipment Allowed:** In cases where the importer is located at far flung places such as Delhi or Ludhiana, the transshipment of cargo is allowed without payment of duty by CHA. The importer has to submit the bill of entry meant for transshipment to the Customs, which allows transit without payment of duty.

In such cases, the importer need not follow the detailed customs procedure. Rather, a simple transshipment procedure is to be followed by the carrier of cargo as well as the customs departments. The importer also needs to comply with the simple procedure for the customs clearance formalities after the arrival of the goods at the customs station. Under the provisions of Customs Act, especially under Section 52 to 56, the importer is allowed for transshipment and customs assessment and payment of duty has to be completed at importer nearby ICD/CFS stations or customs house.

Notes



Note The importer is not allowed the unbundling of cargo and the customs official will put a seal on such cargo to be transhipped, which shall be checked by destined customs official at the time of duty assessment and examination of cargo.

3. **Goods for personal use and warehousing:** The importer has been allowed to warehouse the cargo without the payment of duty as per Section 46 of the Customs Act. As the Government of India wishes to reduce the transactional cost of international trade, the importer is allowed to warehouse the cargo and duty assessment and examination of cargo shall be done at a later stage. The importer will then pay the duty on cargo. For such clearance of cargo, the procedure is very simple: the importer/CHA (Customs House Agent) has to file a bill of entry with custom for warehousing of cargo.

In case the importer has imported the goods for personal use, he can get his cargo cleared by payment of duty as assessed for home consumption after payment of the duties leviable.

4. **EDI Customs clearance:** For making work more efficient and transparent, the government has introduced the customs clearance procedure online and as many as 24 ports/air cargo stations/ICD/CFS are integrated in a single system of customs clearance. Under the EDI system, the importer does not have to submit any formal or physical Bill of Entry, but it is generated in the computer system known as IGATE, which generate a specific number for importer cargo clearance and is transmitted on all systems automatically throughout India. It is to be noted that under the EDI system, the importer has to file a cargo declaration, which shall prescribe particulars as required for processing of the entry for customs clearance.

In the EDI system, the importer need not submit documents as in case of cargo declaration in non-EDI form. In the EDI system, the importer generates all such forms in non-physical form in the electronic format, which contains all the relevant information with respect to various documents and such information, is processed to the Service Centre for duty assessment. However, the importer has to submit a signed paper copy of all such declarations as generated in the system to the service centre operator for confirming the genuineness and non-reputability of the declaration. Importer/CHA generate a checklist so as to verify of data authenticity. The importer submits the data to service centre only after verification so as to avoid any error to the Service Centre Operator. On the submission of such correctness report, the Service Centre Operator generates a B/E Number, which is endorsed on the printed checklist and then returned to the importer/CHA. As such, no original documents are required at this stage and customs officials may demand such original documents at the time of examination and assessment of cargo. For establishing the correctness and genuineness of the documents, the importer has to sign the copy of all such electronically generated forms once again at the time of customs clearance from port/air cargo station.

Under the EDI system, the Import General Manifest is also submitted by the Steamer Agents through EDI or by using the service centre of the Custom House. Hence the noting aspect is automatically examined by system itself, which generates the bill of entry number, which has to be noted on all copies of bill of entry. In EDI form of declaration such manifestation is automatically transmitted/forwarded manually or electronically to the concerned Appraising Group in the Custom House, who is responsible for examining and assessing the cargo for customs clearance. As examination and assessment is a highly technical job, the customs department has assigned the various groups who are earmarked for dealing the commodities, which fall under their domain/chapter only. The Central Board of Excise and Customs has divided the various commodities under different Chapter Headings of the Customs Tariff and the appraising officer takes up further scrutiny for assessment, import permissibility etc. only as per the provisions of the customs manual of CBEC.

5. **Non-EDI declaration:** Under the non-EDI system, the importer has to submit the bill of entry in different copies in the given colour scheme, which are intended for different purposes by the customs officials and banks for making remittances, if any. The importer/CHA shall provide the full information including the classification of goods as per customs provision for clearance of cargo in easy manner under Non-EDI declaration.

As per customs provision and procedure in India, non-EDI declaration in bill of entry requires the following set of copies.

Table 6.1: Copies of Bill of Entry in Non-EDI Form of Custom Clearance

Original	Customs department
Duplicate	Customs department
Third Copy	Importer reference copy
Fourth Copy	To bank for making remittances

Source: Custom Manual, Central Board of Customs and Excise.

Under the non-EDI system, the importer/CHA shall submit copies of the following documents along with the bill of entry:

- (a) Signed copy of commercial invoice
- (b) Copy of Cargo Manifest or Packing list
- (c) Copy of Bill of Lading or Delivery Order/Airway Bill
- (d) Declaration by Importers/CHA for authenticity of documents
- (e) Copy of Import License if required
- (f) Copy of Letter of Credit/Bank Collection Draft (whatever applicable)
- (g) Copy of insurance document
- (h) License if applicable
- (i) Industrial license, if applicable
- (j) Chemical test report if applicable
- (k) Ad hoc exemption order, if importer has it
- (l) Duty Entitlement Pass Book for drawback
- (m) Catalogue or technical write up or literature in case of machineries, spares or chemicals if applicable
- (n) Value of spares, components machineries in split form in separately
- (o) Copy of Certificate of Origin to avail preferential tariff if applicable
- (p) No Commission declaration

At the time of submission of bill of entry for customs clearance with relevant documents as prescribed above, importer has to get the bill of entry noted in the concerned unit which is responsible for examination of the cargo/goods/consignment. Importer shall also care to put the bill of entry no. and all copies of bill of entry as manifested by customs officials. The first stage of processing of bill of entry by appraising officer who examine the cargo is referred as First noting and such noting the bill of entry gets sent to the appraising section of the Custom House for assessment functions, payment of duty, etc.

Notes

6. **Correctness of documents:** The Customs Department is very particular about the genuineness of import documents submitted by the importer and asks him/CHA for misdeclarations/or incorrect information is found, Customs has the right to take legal course of action against such importers. It is, therefore, advised that importer/CHA should take all precautions to avoid such situations and should declare the documents with immense care.

6.1.2 Assessment of Import Cargo

All goods imported have to pass through the procedure of customs for proper examination, appraisal, assessment and evaluation. This helps the custom authorities to charge the proper tax and also check the goods against the illegal import.

The documents submitted by importer are checked and assessed by Customs authorities and then goods are cleared. Section 17 provides that assessment of goods will be made after Bill of Entry is filed. Date stamp of receipt is put on the 'Bill of Entry' and then it is sent to appraising department either manually or electronically

6.1.3 Harmonized System (HS)

Harmonized System is an internationally agreed upon classification system for trade. The HS code is used by Customs agencies worldwide to assess duties, collect trade statistics, and generally to control imports and exports.

1. **Proper assessment as per customs classifications:** It is the duty of the appraising officer to assess the cargo as per the laid down procedure under various rules & regulations of customs classification. He shall take note of classification including various section or notes in assessing the cargo. He shall take note of the various exemption/export promotion schemes that have been enunciated by the Government of India for helping importers while assessing the cargo for payment of customs duty by them. He shall also take note of whether any restrictions/prohibitions/special import license/permission/permit is required in import of such commodities to the country. Some important responsibilities and functions of appraising officer are:
 - (a) Correct assessment of duty to be paid by the importer after having due regard to classification of goods imported by having proper look at the rules of interpretations, chapters and sections notes.
 - (b) Determining in the correct duty liability on importer involving cases where duty is determinable on ad-valorem basis. He shall cross-check the cases of under invoicing, etc. due to difference in actual value and invoice value.
 - (c) Taking proper note of various documents submitted by the importer in duty assessment and also checking the authenticity of such documents.
 - (d) Ensuring that assessment is proper or using his powers as delegated under Section 14 of the Customs Act for re-determination of duty payable.
 - (e) Taking note of the various contemporaneous values and other information on valuation, available with the Custom House for duty assessment.
2. **Representative sample for examination if under invoiced:** In case the appraising officer is not satisfied with classification or description of cargo or he has doubt about the actual nature of product, he has the right under the Customs Act to take representative sample for a detailed examination of the nature of the goods or testing of its samples. He can pass an order regarding the drawing of representative sample for examination, so as to judge

the actual value of duty payable. He shall give such order on the backside of original bill of entry that was presented by the importer/CHA to the appraising staff posted in the docks/air cargo complexes where the goods have come for examination. Such examination shall be taken place in the presence of the importer's representative.

3. **Through assessment of various importable duties:** Once the appraising officer has received the examination report after the testing of representative samples, he assesses the bill of entry by indicating the final classification and valuation in the bill of entry mentioning the various duties, which are imposable such as:
 - (a) Basic customs duty
 - (b) Additional customs duty
 - (c) Countervailing duty if any
 - (d) Anti-dumping duty if any
 - (e) Safeguard duties if any
 - (f) Education Cess as applicable



Did u know? After assessment of such leviable duties, the bill of entry is sent to the Assistant Commissioner/Deputy Commissioner for his confirmation of duty assessment. If the Assistant Commissioner/Deputy Commissioner is satisfied with value limits of import duty, he sends the same to the computist who calculates the duty amount, taking into account the rate of exchange at the relevant date as provided under Section 14 of the Customs Act.

4. **Depositing Customs Import Duty:** Once the duty has been assessed and the computist determines the amount payable, the importer/CHA has to deposit the import duty as assessed and calculated with the treasury or the authorized banks by the customs department. The importer can take the delivery of his cargo/goods from the custodians at the respective port/air cargo station.

In case the appraising officer is satisfied that examination/testing of cargo is not required, as he feels that cargo is under the right classification, he will send bill of entry to the Assistant Commissioner/Deputy Commissioner and on the calculation of duty importer, will deposit the duty so as to take delivery of his cargo.

5. **Appraising Officer is final authority for assessment:** The Appeasing Officer (usually in groups under the same chapter) assesses the cargo on the basis of documents that are submitted by the importer for assessment and calculation of duty. The appraising officer gives due regards to the due procedure of customs clearance as prescribed for giving focus of customs classification chapter/heading and subheading for right assessment of cargo. He also ensures that the goods imported are allowed for imports and crosschecks whether any import license or any permission is required for imports. If he has any doubt, he can ask for a representative sample in order to ascertain the actual nature of goods to determine the duty applicable. If he is satisfied from the second noting of assessment of cargo, he passes the order on the reverse of the duplicate copy of the bill of entry and the importer or his agent can make payment of duty to take delivery of the goods from the import sheds/docks. This way, the appraising officer is the final authority for assessment of duty payable up to second noting. However, the importer, if not satisfied, can make an appeal to the higher authority.
6. **Right to appeal:** In case where the importer is not satisfied with the classification of his cargo and subsequent assessment of duty by the appraising officer, he has the right under provisions of the Customs Act 1962 for a new assessment order of cargo.

Notes



Notes The Customs Act gives the right of appeal to the importer against the assessment order, which can be made to appropriate appellate authority within the time limit and in the manner prescribed under various acts/manuals and provisions.

6.1.4 Examination of Import Goods

1. **Examination under non-EDI system:** As per customs provisions, all imported goods in India are subject to be examined so as to judge the correctness of description/classification as given by the importer in the bill of entry. Such examination is not through hence a part of the consignment is selected and examined randomly. Due to some reason, if the importer does not have complete information with him at the time of import, he can request for examination of the goods before assessing the duty liability or, if the Customs Appraiser/Assistant Commissioner is of the opinion that the imported goods need to be examined before assessment, the goods can be examined prior to assessment of duty payable and such examination is known as First Appraisalment.

The importer has to request for first check examination at the time of filing the bill of entry or at the data entry stage. The reason for seeking First Appraisalment must also be given. On the original copy of the bill of entry, the Customs Appraiser records the examination order and returns the bill of entry to the importer/CHA with the direction for examination, which he should take to the import shed for examination of the goods in the shed. Shed Appraiser/Dock examiner examines the goods as per examination order and records his findings. In case, group has called for samples, he forwards sealed samples to the group. The importer is to bring back the said bill of entry to the assessing officer for assessing the duty. Appraiser assesses the bill of entry. It is countersigned by Assistant/Deputy Commissioner, if the value is more than rupees one lakh.



Caution The goods can also be examined subsequent to assessment and payment of duty.

This is called Second Appraisalment. Most of the consignments are cleared on second appraisalment basis. It is to be noted that whole of the consignment is not examined. Only those packages selected on a random selection basis are examined in the shed.

2. **Examination of cargo under EDI system:** Under the EDI system, the bill of entry, after assessment by the group or first appraisalment, as the case may be, needs to be presented at the counter for registration for examination in the import shed. A declaration for correctness of entries and genuineness of the original documents needs to be made at this stage. After registration, the B/E is passed on to the shed Appraiser for examination of the goods. Along-with the B/E, the CHA is to present all the necessary documents. After completing examination of the goods, the Shed Appraiser enters the report in the system and transfers first appraisalment B/E to the group and gives 'out of charge' in case of already assessed B/E. Thereupon, the system prints the Bill of Entry and order of clearance (in triplicate). All these copies carry the examination report, order of clearance number and name of the Shed Appraiser. The two copies each of B/E and the order are to be returned to the CHA/Importer, after the Appraiser signs them. One copy of the order is attached to the Customs copy of B/E and retained by the Shed Appraiser.

Green Channel Facility

Notes

The Central Board of Customs and Excise on the advice of the Ministry of Commerce has provided the Green Channel clearance facility to some large and status holder exporters.

The purpose of such facility is to help large exporters who have imported raw material for use for export purposes. Such fast clearance of customs reduces their transactional cost and also helps them in completing their work on time. Under the Green Channel facility, clearance of goods is done without routine examination of the goods. Customs officials make the assessment of duty payable on the basis of documents submitted by importer along with his declaration of correctness of documents and allow the cargo for clearance. In cases of doubt, the customs official has the right of physical examination of the goods in case only the marks and number are to be checked. If customs officials have specific inputs about wrongdoing and mischievous activities they have the right to bring the matter to the knowledge of senior officer and investigation can begin on their instructions.



Did u know? In cases where the importer feels that there is duty free assessment or concessional assessment as per various government schemes and notifications, he has to furnish the end-use bonds with a bank guarantee or any other surety required. Such execution of bond and bank guarantee is to be done in prescribed forms before the assessing appraiser.

Payment of Duty

The importer can pay the duty on cash or DD in the designated banks of customs and can also make payment through TR-6 Challans in the treasury. Different Customs Houses have authorized different banks for payment of duty. It is necessary to check the name of the bank and the branch before depositing the duty. The bank endorses the payment particulars in the Challan, which is submitted to Customs.

Amendment of Bill of Entry

In case the importer realizes that he has made a mistake in the submission of documents along with the bill of entry, he can make request for amendments in the bill of entry with the approval of Deputy/Assistant Commissioner. He has to make a request for amendment in the bill of entry along with supporting documents. For example, if the amendment of certificate of invoice is required, a letter from Insurance company authority is required. Customs also allows the amendment in documents that are submitted by importer after the goods have been given out of charge i.e., goods have been cleared on sufficient proof being shown to the Deputy/Assistant Commissioner.

Prior Entry for Bill of Entry

The importer is also allowed under Section 46 of the Customs Act 1962 to submit the bill of entry in advance so as to get faster clearance of the goods. The importer can submit the bill of entry in advance and shall submit the import general manifest on the arrival of the ship to the customs department. Such bill of entry is valid if the vessel/aircraft carrying the goods arrives within 30 days from the date of presentation of bill of entry.

In case of advance filing of bill of entry, the importer, under the provision of the Customs Act, is required to submit 5 copies of the bill of entry. The fifth copy in such cases is known as advance

Notes

noting copy. The importer is required to declare in advance the bill of entry that the vessel/ aircraft is expected to come within 30 days from the date of filing of bill of entry and he will present the bill of entry for final noting as soon as the IGM is filed. It is to be noted that facility of advance noting is available to all imports except in the cases of bond bill of entry and also during the special period.

Mother Vessel/Feeder Vessel

In the cases where the goods are to be brought by feeder vessel from the nearby port, the container will be transferred from the mother vessel to feeder vessel for bringing the cargo to the country. Under such cases, the importer may not know which vessel number he has to put on the bill of entry as he does not know on which vessel or container his cargo is loaded. In such cases, the Customs allows the importer to write the mother vessel number on the bill of entry and the same may be amended to mention the names of both mother vessel and feeder vessel on bill of entry.

Specialized Schemes

The Government of India has notified various schemes in order to provide incentives to exporters in international trade and accordingly various exemptions and remissions of duty are also given such as DFIA/DEPB, etc. For getting goods cleared by customs under situations, the importer has to execute the bonds with the customs authorities to ensure all the conditions of respective notifications as issued by the Government of India from time to time are fulfilled. He has to execute a bond that ensures that he has to pay the duty in case he fails to fulfil the terms and conditions of the notifications for export promotions. It is to be noted that the amount of bond to be executed by the importer in such cases shall be equal to the amount of duty leviable on the imported goods. A bank guarantee is also needed from along with the bond. The customs official has the right under the Customs Act provisions, for relaxing the amount of bank guarantee to be executed by the importer, keeping in mind his status, such as Super Star Trading House/ Trading House, etc.

Bill of Entry for Bond/Warehousing

In some cases, the importer doesn't need the goods immediately for use or consumption. He wishes to get his goods warehoused for future usage/consumption without payment of duty to customs. In such cases, the importer will have to submit a separate bill of entry along with above-mentioned documents for assessment of cargo. The assessment procedure in this case is similar to the normal procedure of cargo clearance. The assessment is required at this stage as customs wishes to ensure the true value of cargo to avoid any unforeseen situation such as misplacement of cargo in future. Once the procedure of duty assessment of cargo is completed, the importer is allowed under the customs provisions to place his cargo in a customs-notified warehouse. He is required to make the payment of import duty at the time of ex-bond clearance of cargo for which the exporter has filed an ex-bond bill of entry. The importer will have to pay the same rate of duty on such goods cleared as he would have paid on his goods if he has got them cleared at that point of time.

Self Assessment

Fill in the blanks:

1. The Government of India has prescribed the rate of duty to be imposed under Customs Tariff Act,

2. Raising from customs is an important contributor to various expenses of the Central Government and customs duty is one of the main contributors to exchequer.
3. Under the system, the importer does not have to submit any formal or physical Bill of Entry, but it is generated in the computer system known as IGATE, which generate a specific number for importer cargo clearance and is transmitted on all systems automatically throughout India.
4. Under the non-EDI system, the importer has to submit the in different copies in the given colour scheme,
5. The system is designed in such a manner that it helps the appraising officer to assess the duty to be payable after taking note of various exemptions/export promotion schemes of the Government of India.
6. The Central Board of Customs and Excise on the advice of the Ministry of Commerce has provided the clearance facility to some large and status holder exporters.
7. In case of advance filing of bill of entry, the importer, under the provision of the Customs Act, is required to submit copies of the bill of entry.
8. The importer can pay the duty on cash or DD in the designated banks of customs and can also make payment through Challans in the treasury
9. The beauty of this electronic system is that it promotes and also helps in processing the bill of entry at high speed.
10. In cases where the importer is located at far flung places such as Delhi or Ludhiana, the trans shipment of cargo is allowed payment of duty by CHA.

6.2 Custom Clearance of Export Cargo

For clearance of export goods, the exporter or his agents have to undertake the following formalities:

6.2.1 Registration

In case of export of cargo, the exporters will have to obtain mandatory PAN-based Import Export Code no. (IEC Code) from the Directorate General of Foreign Trade as it is essential and legal to mention the IEC code number on the shipping bill, which will be submitted by exporter or his freight forwarder to the customs authorities for Let Export Order (L.E.O.). However, in case of the EDI System, the computer system will automatically generate the PAN-based IEC Code number of the importer through ICES Gateway system from the DGFT database. In addition to the above, the exporter is also needed to open an account with an authorized foreign exchange dealer, as he has to realize his export proceeds through his authorized bank. The RBI has abolished registration with itself for foreign exchange since the introduction of PAN-based IEC code number since 2000. Sometimes, the customs authorities ask the importer to open a current account in the designated bank for credit of any drawback incentive.

Registrations of Airline, Shipping Line, Steamer Agent, port or airport is essential with the customs departments as their details such as vessel number has to be put into the Customs System. If any airlines or shipping company is not registered, the shipping bill of exporter will not get processed, as the details of shipping company will not be available to customs officials. The system will withhold the shipping bill. Hence it is recommended that all shipping

Notes companies/airlines/steamer agents shall get themselves registered with Assistant/Deputy Commissioner-in-Charge of EDI System.

Registration in the Case of Export under Export Promotion Schemes

The government notifies various schemes every year for promoting exports and giving incentives to good exporters who bring hard currency into the country. All exporters who wish to avail of the benefit of such government schemes have to get registered their licenses/DEPB book with the Customs Station. Such registration can be made only with the original documents.

Processing of Shipping Bill – Non-EDI

Under the manual system of customs clearance of cargo, the exporter is supposed to submit the shipping bills (in case of ocean trade) or bills of export (in case of land trade). These have to be filed in the format prescribed in the Shipping Bill and Bill of Export (Form) Regulations, 1991. Shipping bills have to be submitted along with all original export documents such as invoice, ARE, packing list, insurance certificate, certificate of inspection, etc. The assessing officer in the Export Department checks the value of the goods, classification under the Drawback Schedule in case of drawback shipping bills, rate of duty/cess where applicable, and the exportability of goods under the Foreign Trade Policy and other laws in force.

After passing of the bill by customs officer the exporter is required to present the goods to the shed appraiser (export) in docks for examination of cargo to be exported. The shed appraiser may mark the document to a customs officer (usually an examiner) for examining the goods. The examination of cargo is carried out under the supervision of the shed appraiser (export). If the description and other particulars of the goods are found to be as declared, the shed appraiser gives a 'let export' order, after which the exporter may contact the preventive superintendent for supervising the loading of goods on to the vessel. In case the examining staff in the docks is dissatisfied with the description of goods as submitted by exporter and found that there is some discrepancy in the goods, the examining staff can mark the shipping bill back to export department/duty drawback group with their observations as well as sample of goods, if needed.

Processing of Shipping Bill under EDI

Under the EDI System for export clearance of cargo, the exporter needs to make declarations in the format as prescribed by customs, which is required to be filed through the Service Centres of Customs. A checklist is generated while submitting the information in electronic system so as to help the exporter check the veracity of various documents and information as provided by the exporter in the system. The exporter can obtain printouts of such checklist, which can be used for future reference.

If the customs officer is satisfied that all the information as submitted by exporter is correct and Service Centre Operator transmit the same on the system, which generates a Shipping Bill Number that is endorsed on the printed checklist and returned to the exporter/CHA. The export cargo, which is subject to export cess as per government provisions, is printed and given by service centre to make payment for the same through the TR-6 Challans. The exporter needs to pay the cess to the customs designated bank. It is to be noted that no copy of shipping bill is made available to exporter/CHA at this stage of export clearance.

Arrival of Goods at Docks

The exporter can bring his cargo for the purpose of examination of cargo by the customs officials. The officials can allow the cargo to be exported with a 'let export' order from customs on basis

of strength of the checklist and other declarations filed by the exporter in the Service Centre. As per customs rules and regulations, the port authorities need to endorse the quantity of goods that have actually been received by them at customs stations on the reverse side of the Check List.

System Appraisal of Shipping Bills

Under the EDI system, the exporter is required to make the declaration in connection to export shipment on the computer system without any human intervention for the processing of shipping bill in order to get the goods cleared from customs for exports. In cases where the assessing officer is of the opinion that there is some difference in the exporter's declaration and actual cargo, he can demand some samples to check and confirm the declared value or ensuring the proper classification for duty drawback schedule, even when sitting at the computer screen. If the assessing officer has any doubt regarding the accuracy of documents submitted by the exporter he has the right under the Customs Act 1962 to give any special instructions for examination of goods.

Status of Shipping Bill

The exporter or his freight forwarder shall keep a tab on the query counter of the Service Centre in order to ascertain whether the Shipping Bill as submitted by him in the computer system has been cleared or not. He is required to crosscheck all this information before the arrival of goods into the docks for the sake of examination and export. If the customs staff have some objection or any query, the exporter is required to answer the same through the service centre, in case his freight forwarder has EDI connectivity. In cases when the customs officer is satisfied, he can pass the shipping bill for export of cargo.

Customs Examination of Export Cargo

Once the cargo has reached the dock, the exporter or his freight forwarder is required to contact the Customs Officer who is designated for this purpose. The exporter or his representative shall present the checklist along with other declarations and original documents such as invoice and packing list, ARE Form, etc. The customs officer verifies the quantity of the goods actually received and enters the same into the system and thereafter marks the Electronic Shipping Bill. He also forwards the original documents to the dock appraiser of the dock who may assign a customs officer for the examination of cargo. He also intimates the name and the packages to be examined to the customs officers.

The customs officer along with the dock appraiser, inspects/examines the shipment of the export cargo. He also puts the details of the examination report in the system. He then marks the electronic bill along with all original documents and checklist to the dock appraiser. In cases where the dock appraiser is satisfied that the particulars entered in the system conform to the description given in the original documents and as seen in the physical examination, he may proceed to allow "let export" for the shipment and inform the exporter or his agent.

Variation between the Declaration and Physical Examination

The appraising officer of the cargo retains the checklist and the declaration along with all original documents. In cases where there is any variation between the declaration made by exporter in the shipping bill and physical documents/examination report of customs, the

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appraiser is required to mark such shipping bill to the Assistant Commissioner/Deputy Commissioner of Customs (Exports) electronically. He can also send these documents in a physical form to Assistant Commissioner/Deputy Commissioner of Customs (Exports) and advise the exporter or his representatives to meet the Assistant Commissioner/Deputy Commissioner of Customs (Exports) so as to settle the dispute. If the exporter is satisfied with the views of the customs department, the shipping bill is required to be processed accordingly. In other cases, principles of natural justice are required to be followed for the finalization of the issues by keeping utmost care that the cargo shall not get perished.

Stuffing/Loading of Goods in Containers

The exporter or his agent is supposed to hand over the exporter's copy of the shipping bill, which shall be signed by the appraising officer permitting "let export" order, to the person in charge of the shipping company. The person-in-charge is required to approach the proper officer (Preventive Officer) so as to get permission for the shipment. If the cargo is to be stuffed in the container, the same shall be done at the dock under preventive supervision of customs officials. It is to be considered that loading of containerised as well as bulk cargo has to be done under preventive supervision. The Customs Preventive Superintendent (Docks) registers the actual number of packages to be stuffed into the container along with the bottle seal number and endorses these details on the exporter's copy of the shipping bill that is presented to him by the steamer agent.

In cases where there is a difference in the quantity/number of packages that are stuffed in the containers/goods loaded on vessel by the exporter and particulars filled by the Superintendent (Docks) on the shipping bill. In such cases, the shipping bill has to be changed/amended as per right quantity loaded in the container.

Drawl of Samples

In cases where orders have been given by the Appraiser Dock (export) for samples to be drawn and tested, the customs officer can draw two samples from the consignment and enter the particulars of such samples testing along with the name of testing agency in the ICES/E system. Under the EDI system there is no separate register for recording dates of samples drawn for testing. The customs officer prepares three copies of the test memo and signs them on behalf of customs and the exporter or his agent is also supposed to sign such test memo of samples collected by customs for testing. The three copies of the test memo are required for following purposes:

1. *Original* – To be sent along with the sample to the test agency.
2. *Duplicate* – Customs copy to be retained with the second sample.
3. *Triplicate* – Exporter's copy.

The Assistant Commissioner/Deputy Commissioner is empowered under the Customs Act to draw the samples for purposes other than testing, such as visual inspection and verification of description, market value inquiry, etc.

Amendments

The exporter can request for any correction/amendments in the checklist, which is generated after filing of declaration to the service centre. In such cases, it is to be seen that the exporter has not submitted the documents and the shipping bill number has not been generated at the service centre of customs. In case the exporter needs to carry out the corrections/amendments after the

generation of the shipping bill number or in cases where the goods have been brought into the export dock, the procedure for corrections/amendments shall be carried out in the following manner:

1. In case the cargo goods have not yet been allowed "let export", the changes, amendments or corrections allowed by the Assistant Commissioner (Exports).
2. In cases where the "Let Export" order has already been given, the corrections/amendments or changes can be permitted by the Additional/Joint Commissioner of Custom House, provided such Additional or Joint Commissioner shall be in charge of export section.

Export of Goods under Claim for Drawback

It is the policy of the Government of India that duties shall never be exported. That is why drawback claims are processed through EDI system on the actual exports by the officers of the drawback branch. Drawback claims are processed on a first-come-first-served basis under Sections 75 and 76 of the Customs Act 1962. Under the EDI system the exporter is not required to file a separate drawback claim. He can ascertain the status of his shipping bills and sanction of the DBK claim through the query counters set up at the service centre. In case there is any query or deficiency in the drawback claim of exporter, the same can be known on computer terminal by the exporter at service stations or freight forwarder having such facility. The exporter can obtain a printout of the query/deficiency from the service centre and is required to reply to all such queries/deficiencies through the service centre. The claim for duty drawback will come in queue of the EDI system once the queries/deficiencies are entered into system by the Service Centre Operator.

The claims cleared by duty drawback department on a particular day are enumerated in a scroll and are subsequently transferred to the bank through the system itself. The bank transfers the duty drawback amount of credits to the respective accounts of the exporters. The bank can keep their exporters updated about such duty drawback credits entered in their accounts by sending the fortnightly statement.

For smoothening the system; it is advisable that the Steamer Agent/Shipping Line should take care to electronically transfer the EGM to the Customs EDI system so as to enable the customs to sanction the drawback claims once the physical exports has taken place.

Generation of Shipping Bills

Once the "let export" order is given by the Appraiser for the export customs clearance of cargo on the system, the shipping bill is generated by the system in two copies. The first copy is for the Customs and another is for the exporter, which is referred to as the Export Promotion Copy and is generated after submission of EGM. The appraiser obtains the signature of the CHA on both copies of shipping bill and examination report along with the customs officer's signature on the examination report on the printout of such system-generated shipping bills. The appraiser is also supposed to sign both copies of the shipping bill along with his seal on it, to specify the place of customs clearance of the export cargo.

The appraiser is also supposed to sign and stamps the original and duplicate copy of the SDF. He retains the original declarations by the exporter along with the customs copy of shipping bill and original copy of the SDF, which is thereafter forwarded to the Export Department of the Customs House. The exporter's copy of shipping bill and the second copy of the SDF can be returned to the exporter or his agent by the appraiser.

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Export General Manifest

As per the Customs Act 1962, it is mandatory for all the shipping lines/agents to submit the Export General Manifest according to the shipping bill, to the Customs Department, electronically. Such manifest must be submitted within 7 days from the date of sailing of the vessel.

In addition to lodging the Export General Manifests in the electronic form, the shipping lines are also required to file manual EGMs along with the exporter's copy of the shipping bills in the export department. It is to be noted that such manual EGMs have to be entered in the register at the Export Department and the shipping lines are supposed to get the acknowledgements mentioning the date and time of receipt of the EGMs by the customs department.

The procedure mentioned above is the general procedure for export goods customs clearance under EDI Systems. However, the exporter is required to follow special procedures that are applicable in case of specified export promotions schemes. The details and applied procedure for such export promotion schemes are notified and issued by the respective Commissionerates through the Public Notice/Standing Orders issued.

6.3 Custom Valuation

India is presently following the provisions of the WTO Agreement on Customs Valuation (ACV) for determination of value on imported goods where Customs duty is levied with reference to value (ad-valorem rates). However, this does not apply to cases where tariff values have been fixed.

India is a founding Member of the GATT (presently WTO) and was actively involved in the GATT negotiations (Tokyo Round, 1973-79), which developed the Agreement on Customs Valuation (ACV). India implemented the ACV in August 1988.

6.3.1 Methods of Valuation

The Customs Valuation Rules, 1988, lays down six methods for the valuation of imported goods. The primary basis for valuation is the "Transaction Value". However, it is subject to adjustment by certain Valuation Factors (see Rule 9). There are also certain conditions for the transaction value method to be applicable (see sub-rule 2 of Rule 4). In certain situations, the Customs authorities could reject the declared value (transaction value method), if the truth or accuracy of the declaration is reasonably suspected (see Rule 10 A). In all such cases where the transaction value method is not applied, goods shall be valued by applying the subsequent methods in a strictly hierarchical order (see Rule 3).

In order to enable the Customs to determine the value by application of the most appropriate method, the importer is required to truthfully declare the full particulars concerning the goods under import. These include full description and specifications of the goods, basis of valuation applied, relationship with the supplier, conditions and restrictions if any attached with the sale, elements of cost not included in the invoice price, royalty and license fee payable in relation to the imported goods, etc. These details are to be declared in a special Valuation Declaration Format designed for the purpose. This is in addition to the entry declaration (Bill of Entry). In respect of EDI processing, the valuation declaration is integrated as a part of the Electronic Declaration. The importer should also provide copies of invoice, purchase contract and other supporting documents.

Transaction Value Method

Rule 3(i) of the Customs Valuation Rules, 1988 states that the value of imported goods shall be the transaction value. Rule 4(i) thereof defines "transaction value" as the price actually paid or

payable for the goods when sold for export to India, adjusted in accordance with the provisions of Rule 9.

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The price actually paid or payable should be adjusted to include all the costs and services (dutiability factors) specified in sub-Rule 9 (1) (see below) if not already included in the invoice value. In short, the transaction value should be determined by suitably adjusting the declared value so as to include all payments made as a condition of sale of the imported goods by the buyer to the seller or by the buyer to a third party to satisfy an obligation of the seller. Since the assessment is on CIF basis, the invoice value should be suitably adjusted to include the freight, insurance and handling charges as applicable under sub-Rule 9 (2).

Valuation Factors

Valuation Factors (see Rule 9) are the various elements (dutiability factors), which should be added while determining the Customs value. The factors should be added to the extent they are not already included in the price actually paid or payable (invoice value). These dutiable factors are:

- Commissions and brokerage, except buying commissions;
- The cost of containers which are treated as being one for Customs purposes with the goods in question;
- The cost of packing whether for labor or materials;
- The value, apportioned as appropriate, of the following goods and services where supplied directly or indirectly by the buyer free of charge or at reduced cost for use in connection with the production and sale for export of the imported goods, to the extent that such value has not been included in the price actually paid or payable:-
 - ❖ material, components, parts and similar items incorporated in the imported goods;
 - ❖ tools, dies, moulds and similar items used in the production of the imported goods;
 - ❖ materials consumed in the imported goods;
 - ❖ engineering, developing, artwork, design work, and plans and sketches undertaken elsewhere than in the importing country and necessary for the production of imported goods;
- Royalties and license fees related to goods being valued that the buyer must pay either directly or indirectly, as a condition of sale of the goods being valued, to the extent that such royalties and fees are not included in the price actually paid or payable;
- The value of any part of the proceeds of any subsequent resale, disposal or use of the goods that accrues directly or indirectly to the seller;
- Advance payments;
- Freight charges up to the place of importation;
- Loading, unloading and handling charges associated with transporting the goods;
- Insurance.

Non-dutiability Factors

The following charges are not to be added for the purposes of determining the Customs value provided they are clearly distinguishable and separately declared in the commercial invoice:

- Buying commission;
- Interest charges for deferred payment;

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- Post-importation charges (e.g. inland transportation charges, installation or erection charges, etc.);
- Duties and taxes payable in India.

Transaction value method not applicable to certain cases

The Transaction value method cannot be applied in cases where the transactions do not comply with the definition under Rule 4 (1). Thus, if there is no sale for export to India in respect of any importation, such as gifts and consignment imports for subsequent sale, there is no transaction value and hence the method is not applicable.

The conditions referred to under Sub-Rule 4(2) are also required to be satisfied for applying the transaction value method. These are:

- The sale is in the ordinary course of trade under fully competitive conditions;
- The sale does not involve any abnormal discount or reduction from the ordinary competitive price;
- The sale does not involve special discounts limited to exclusive agents;
- Objective and quantifiable data exist with regard to the adjustments to be made under Rule 9;
- There are no restrictions concerning the disposition or use of the goods by the buyer (subject to certain exceptions);
- The sale or price is not subject to some condition or consideration;
- No part of the proceeds of the goods (by resale, disposal or use) after importation accrues to the seller;
- Buyer and seller are not related, and if related, the relationship should not have influenced the price.

Transaction value method also does not apply to situations where valuation fraud (under valuation, wrong description, misdeclaration of quantity, grade, specifications, etc.) are shown to have taken place. These are cases where Customs do have adequate evidence to establish the fraud. In cases of suspected fraud, Rule 10 A could be applied to reject the declared value and the transaction value method.

Related Party transactions

The transaction value method cannot be applied in cases where the buyer and seller are related and the relationship has influenced the price. The scope of relationship is defined in Sub-rule 2 (2) of the Customs Valuation Rules. In such cases the burden of proof shifts to the importer, who should satisfy the Customs that the declared price closely approximates to the test values prescribed in sub-rule 4(4). If the importer fails to discharge this responsibility, the declared value could be rejected and valuation done under any of the subsequent methods applied in hierarchical order.

6.4 The Harmonized System

The Harmonized Commodity Description and Coding System generally referred to as "Harmonized System" or simply "HS" is a multipurpose international product nomenclature developed by the World Customs Organization (WCO).

It comprises about 5,000 commodity groups; each identified by a six digit code, arranged in a legal and logical structure and is supported by well-defined rules to achieve uniform classification.

The system is used by more than 200 countries and economies as a basis for their Customs tariffs and for the collection of international trade statistics. Over 98 % of the merchandise in international trade is classified in terms of the HS.

The HS contributes to the harmonization of Customs and trade procedures, and the non-documentary trade data interchange in connection with such procedures, thus reducing the costs related to international trade.

It is also extensively used by governments, international organizations and the private sector for many other purposes such as internal taxes, trade policies, monitoring of controlled goods, rules of origin, freight tariffs, transport statistics, price monitoring, quota controls, compilation of national accounts, and economic research and analysis. The HS is thus a universal economic language and code for goods, and an indispensable tool for international trade.

The Harmonized System is governed by “The International Convention on the Harmonized Commodity Description and Coding System”. The official interpretation of the HS is given in the Explanatory Notes (5 volumes in English and French) published by the WCO. The Explanatory Notes are also available online and on CD-ROM, as part of a database which groups all the available HS Tools, by adding to the information on the Nomenclature, the Compendium of Classification Opinions and the Explanatory Notes, the information relating to the Alphabetical Index and the Brochure on Classification Decisions taken by the Harmonized System Committee.

The maintenance of the HS is a WCO priority. This activity includes measures to secure uniform interpretation of the HS and its periodic updating in light of developments in technology and changes in trade patterns. The WCO manages this process through the Harmonized System Committee (representing the Contracting Parties to the HS Convention), which examines policy matters, takes decisions on classification questions, settles disputes and prepares amendments to the Explanatory Notes. The HS Committee also prepares amendments updating the HS every 5 – 6 years.

6.5 Carnets

A carnet may refer to (in international law):

A document allowing the importation of certain goods to countries without paying customs duty. Three types exist:

- ATA Carnet, for temporary importation of goods and equipment
- Carnet de Passage, for motor vehicles
- TIR Carnet, to simplify administrative formalities of transit commercial goods carried by international road transport.

6.5.1 ATA Carnet

The ATA Carnet is an international Customs document that a traveller may use temporarily to import certain goods into a country without having to engage in the Customs formalities usually required for the importation of goods, and without having to pay duty or value-added taxes on the goods.

The United States allows for the temporary importation of commercial samples, professional equipment and certain advertising materials by a non-resident individual.

Carnets are a security that participating countries accept as a guarantee against the payment of Customs duties that may become due on goods temporarily imported under a carnet and not exported as required. “ATA” stands for the combined French and English words “Admission Temporaire-Temporary Admission.”

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Why Use an ATA Carnet?

The ATA carnet simplifies the customs formalities involved in temporarily importing goods into the U.S. and other countries. Without a carnet it would be necessary to go through the customs procedures established in each country for the temporary admission of goods. The carnet allows the business traveller to use a single document for clearing certain categories of goods through Customs in several different countries. It may be used for unlimited exits from and entries into the U.S. and participating foreign countries during the one-year period of validity. They are accepted as the entry document and satisfy the importer's obligation to post a security in more than 87 countries.

What are the Importer's Obligations?

A carnet holder is obligated to present the goods and carnet to customs to prove exportation. Failure to prove exportation on either a TIB or a carnet subjects the importer to liquidated damages equal to 110 percent of the duty and import tax. Goods imported under either a TIB or a carnet may not be offered for sale.

Who issues ATA carnets?

Domestic associations in participating countries that are members of the International Bureau of Chambers of Commerce issue carnets to residents to be used abroad. The United States Council for International Business has been designated by the U.S. Customs Service as the United States issuing and guaranteeing organization. A fee is charged by the Council for its service. The guaranteeing organization is held liable for the payment of liquidated damages if the carnet holder, such as the importer, fails to comply with customs regulations.

How Long is an ATA Carnet Valid for?

An ATA carnet is valid for one year from the date of its issuance. Merchandise listed on an ATA carnet can be imported to and exported from any of the member countries as many times as needed during the one-year life of the carnet.

What Goods may be Entered under an ATA Carnet?

Commercial samples, professional equipment and advertising material can be imported into the United States by a non-resident.

Other countries permit the use of a carnet to import the above materials and other categories of goods such as:

- Ordinary goods such as computers, tools, cameras and video equipment, industrial machinery, automobiles, gems and jewellery, and wearing apparel.
- Extraordinary items.



Example: Van Gogh's self-portrait, circus animals, jets, band instruments, satellites, human skulls, and the New York Philharmonic's equipment.

What does a ATA Carnet not Cover?

Merchandise not covered by the three above listed categories of goods are not eligible for importation into the U.S. by carnet. In addition, merchandise within those three categories

intended for sale or sale on approval cannot be entered on a carnet – it must be entered as a regular customs entry.

What Happens if the Goods are not Exported?

If the holder of an ATA carnet sells, donates or otherwise disposes of any of the goods listed on the carnet, the issuing organization will be required to pay liquidated damages equal to 100 percent of the import duties and taxes. That organization in turn will attempt to collect these moneys from the holder of the carnet who violated the terms. In some cases, the country where the violation occurred will hold both the organization that issued the carnet and the importer equally responsible. The importer is liable to his/her issuing association (and, in some cases, to the Customs authorities of the country where this transpired) for all duties and/or taxes and other sums which would normally be charged on the importation of such goods, as well as the amount charged as liquidated damages. If the U.S. Customs Service finds that there was fraud involved in the importation, additional penalties may be assessed.

What happens when goods covered by a U.S. issued ATA carnet are reimported into the U.S.?

If goods covered by a U.S. issued carnet are brought back into the United States within the validity period of the carnet, the carnet serves as the Customs control registration document and must be presented on re-importation. Whether the re-imported goods are subject to duty depends on exemption in the Harmonized Tariff Schedule <http://www.usitc.gov/taffairs.htm> and not on their status as carnet goods. See 19 CFR 141.4 for goods that are exempted from entry documentation requirements and 19 CFR 141.2 for goods exempted from duty on re-importation.

What if the ATA carnet has expired?

If the expiring ATA carnet is a U.S. issued carnet there will be no penalties or duties assessed by the United States, however, there may be penalties assessed by a foreign government if the carnet expired before the U.S. merchandise was exported from that country.

If the carnet is foreign-issued then liquidated damages will be assessed by the U.S. Customs Service due to the carnet expiring before the merchandise could be exported out of the United States.

What is contained in an ATA carnet document?

The carnet document has a green cover page which provides the names of the carnet holder and issuing association, the carnet issue date, the carnet number, the countries in which the carnet may be used and a complete description of the goods covered. Two yellow sheets in the package are to be used upon exportation from and reimportation back into the issuing country. White sheets are used for the temporary importation into and reexportation from the second or additional countries. Blue sheets are used when transiting through countries.

Each sheet contains two parts – a counterfoil, which remains in the carnet and describes the actions taken by Customs officers each time goods enter or leave a country, and a detachable voucher, which contains a list of the goods covered by the carnet and serves as the required Customs document.

How is a U.S. issued ATA carnet processed by Customs?

When leaving the United States, the holder of a U.S. issued ATA carnet presents the carnet and the covered goods to a Customs officer. The carnet is reviewed for completeness and accuracy

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and the goods are examined to ensure that they match the carnet list. The officer then validates the carnet document and certifies the appropriate exportation counterfoil and voucher. The carnet and the U.S. Customs-certified export voucher are returned to the carnet holder who retains the voucher as the permanent record of the Customs transaction. (*Note:* The carnet does not affect export control requirements such as the filing of a shipper's export declaration or the requirement to obtain export licenses.) Upon return to the United States, the holder of a U.S.-issued carnet presents the carnet and covered goods to a Customs officer for examination. The officer certifies the appropriate reimportation counterfoil and voucher and returns the carnet to the holder for further use or surrender to the issuing association. (*Note:* On U.S. issued carnets only, the vouchers of the yellow exportation/reimportation sheets will not be detached, but will remain with the document when departing or returning to the United States.)

It is the responsibility of the carnet holder to present the carnet to the Customs authorities when entering or leaving a country in order that the necessary verification and certification of the appropriate vouchers and counterfoils can take place. Failure to do so may result in a claim being made. A claim is a notice from a Customs authority of the country of import that a violation of the carnet system has occurred and payment of duties, taxes, and penalty are required.

How is a non-U.S. issued ATA carnet processed?

When processing a foreign-issued carnet, Customs must create a record of the transaction in order to protect the revenue and domestic commerce. Therefore, the U.S. Customs officer responsible for clearing the temporary importation must ensure that the port of importation, dates of Customs activities, and any departure from the original list of articles, are clearly shown in the appropriate fields.

When the merchandise leaves the U.S. the Customs officer must ensure that the required exportation dates are complied with, that the original list of articles agrees with what is being exported, and that the appropriate voucher is detached and forwarded to the port of importation.

6.5.2 Carnet de Passage

A carnet de passages en douanes is an internationally recognised customs document entitling the holder to temporarily import a vehicle duty-free into countries, which normally require a deposit against import charges for such vehicles (generally countries outside Europe). The carnet is used within the framework of the UN customs conventions of 1954 & 1956. The carnet is issued under the auspices of two international touring organisations – the ait and the fia. Major automobile and touring clubs throughout the world are affiliated to one or both of these organisations and a number are authorised to issue carnets within the ait/fia customs documents network. This includes who are affiliated to the fia. A carnet is valid for a maximum of one year. A carnet holder whose journey goes beyond one year may, obtain a second carnet or in some countries, an extension, by contacting the local motoring organisation and seeking further advice from rac.

6.5.3 TIR Carnet

The TIR Carnet is a customs transit document used to prove the existence of the international guarantee for duties and taxes for the goods transported under the TIR system, within the limit of the amounts specified by the contracting parties and under conditions stipulated in the TIR Convention.

Each TIR Carnet has a unique reference number. A TIR Carnet may have 4, 6, 14, or 20 vouchers, as one pair of vouchers is used per country; the number of vouchers indicates the number of countries that can be transited, including the countries of departure and destination, under cover of this type of Carnet, e.g. a 20-voucher Carnet may be used for a TIR transport through up to 10 countries.

Each individual TIR Carnet can be used for only one TIR transport. Once the TIR transport has been terminated at the Customs office of destination of the goods, the driver is handed back the TIR Carnet duly endorsed by the Customs authorities of destination. Customs authorities must immediately confirm the termination of the TIR transport electronically via SafeTIR. The TIR Carnet is returned to the Association and shipped to the IRU for final control and archiving.

Benefits of Carnets

- Carnets save time, effort, and money.
- One document – one application.
- Good for one year.
- Accepted in 80 countries and territories.
- Covers commercial samples, professional equipment, and goods for exhibitions and fairs.
- Eliminates duties, taxes, and temporary importation bonds (TIBs).
- Payment in U.S. Dollars.
- Paperwork in English.
- Easy exit – easy re-entry.
- No uncertainty, no hassles



Task What is the importance and use of ATA Carnet?

6.6 New Developments in Custom Clearance Procedure

Tarrif Notificatuon

In exercise of the powers conferred by sub-section (1) of section 25 of the Customs Act, 1962 (52 of 1962), the Central Government, on being satisfied that it is necessary in the public interest so to do, hereby makes the following further amendments in the notification of the Government of India in the Ministry of Finance (Department of Revenue), No. 39/96-Customs, dated the 23rd July, 1996, published in the Gazette of India, Extraordinary, vide number G.S.R. 291(E), dated the 23rd July, 1996, namely:

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In the said notification, in the Table, after S.No.38 and the entries relating thereto, the following S.No. and entries shall be inserted, namely:

Table 6.2: Tariff Notification Amendment

(1)	(2)	(3)
*39.	Machinery, equipment, instruments, components, spares, jigs, fixture, dies, tools, accessories, computer software, raw materials and consumables required for the long Range Surface of Air Missile (LR-SAM) Programme of Ministry of Defence	If,— (a) the said goods are imported by authorized works centres of the Long Range Surface to Air Missile (LR-SAM). Programme, as may be designated by an officer not below the rank of Deputy Secretary to the Government of India in the Ministry of Defence; and (b) the authorized works centre produces to the Deputy Commissioner of Customs or the Assistant Commissioner of Customs, as the case may be, at the time of import, in each case, a list of the said goods with their relevant description duly certified by the Programme Director, Programme Office LR-SAM, to the effect that— (i) the goods mentioned in the said list are required for the purposes of the LR-SAM; (ii) the import of the goods mentioned in the said list are authorized by the Ministry of Defence under LR-SAM programme and these goods shall be used only for the purpose of the LR-SAM programme. * Explanation. – Nothing contained in this exemption shall have effect on or after the 25 th day of November, 2012.

ADD Notification

Whereas in the matter of import of Melamine (hereinafter referred to as the subject goods), falling under Chapter 29 of the First Schedule to the Customs Tariff Act, 1975 (51 of 1975) (hereinafter referred to as Customs Tariff Act), originating in, or exported from, European Union, Iran, Indonesia and Japan (hereinafter referred to as the subject countries), and imported into India, the designated authority vide its final findings notification No. 14/35/2010-DGAD, dated the 1st June, 2012, published in the Gazette of India, Extraordinary, Part I, Section 1, dated the 1st June, 2012, had come to the conclusion that –

- (i) the subject goods have been exported to India from the subject countries below its normal value;
- (ii) the domestic industry has suffered material injury in respect of such goods;
- (iii) the material injury has been caused by the dumped imports of subject goods from the subject countries;

and had recommended imposition of definitive anti-dumping duty on imports of the subject goods, originating in or exported from the European Union, Iran, Indonesia and Japan and imported into India, in order to remove injury to the domestic industry.

Now, therefore, in exercise of the powers conferred by sub-sections (1) and (5) of section 9A of the Customs Tariff Act read with rules 18 and 20 of the Customs Tariff (Identification, Assessment and Collection of Anti-dumping Duty on Dumped Articles and for Determination of Injury) Rules, 1995, the Central Government, after considering the aforesaid final findings of the designated authority, hereby imposes on the subject goods, the description of which is specified in column (3) of the Table below, falling under tariff item of the First Schedule to the said Customs Tariff Act as specified in the corresponding entry in column (2), originating in the country as specified in the corresponding entry in column (4), and produced by the producer as specified in the corresponding entry in column (6), when exported from the country as specified in the corresponding entry in column (5), by the exporter as specified in the corresponding entry in column (7), and imported into India, an anti-dumping duty at a rate which is equivalent to difference between the amount mentioned in the corresponding entry in column (8), in the currency as specified in the corresponding entry in column (10) and as per unit of measurement

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as specified in the corresponding entry in column (9), of the said Table and the landed value of imported goods in like currency as per like unit of measurement.

Table 6.3

Sl. No	Tariff item	Description of goods	Country of origin	Country of export	Producer	Exporter	Amount	Unit of measurement	Currency
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
1	29336100	Melamine	European Union	European Union	Any	Any	1537	MT	US dollar
2	29336100	Melamine	European Union	Any country other than EU	Any	Any	1537	MT	US dollar
3	29336100	Melamine	Any country other than European Union	European Union	Any	Any	1537	MT	US dollar
4	29336100	Melamine	Iran	Iran	Any	Any	1446	MT	US dollar
5	29336100	Melamine	Iran	Any country other than Iran	Any	Any	1446	MT	US dollar
6	29336100	Melamine	Any country other than Iran	Iran	Any	Any	1446	MT	US dollar
7	29336100	Melamine	Indonesia	Indonesia	Any	Any	1537	MT	US dollar
8	29336100	Melamine	Indonesia	Any country other than Indonesia	Any	Any	1537	MT	US dollar
9	29336100	Melamine	Any country other than Indonesia	Indonesia	Any	Any	1537	MT	US dollar
10	29336100	Melamine	Japan	Japan	Any	Any	1537	MT	US dollar
11	29336100	Melamine	Japan	Any country other than Japan	Any	Any	1537	MT	US dollar
12	29336100	Melamine	Any country other than Japan	Japan	Any	Any	1537	MT	US dollar

2. The anti-dumping duty imposed under this notification shall be levied for a period of five years (unless revoked, amended or superseded earlier) from the date of publication of this notification in the Gazette of India. The anti-dumping duty shall be paid in Indian currency.

Explanation. - For the purposes of this notification,-

- "landed value" means the assessable value as determined under the Customs Act, 1962 (52 of 1962) and includes all duties of customs except duties levied under sections 3, 8B, 9 and 9A of the said Customs Tariff Act; and
- rate of exchange applicable for the purposes of calculation of such anti-dumping duty shall be the rate which is specified in the notification of the Government of

Notes

India, in the Ministry of Finance (Department of Revenue), issued from time to time, in exercise of the powers conferred by section 14 of the Customs Act, 1962 (52 of 1962) and the relevant date for determination of the rate of exchange shall be the date of presentation of the bill of entry under section 46 of the said Customs Act.

SG Notification

Whereas, in the matter of import of Carbon Black (for rubber application) (hereinafter referred to as the subject goods), falling under tariff item 2803 00 10 of the First Schedule to the Customs Tariff Act, 1975 (51 of 1975) (hereinafter referred to as the said Act), from People’s Republic of China, the Director General (Safeguard), in the final findings, vide number G.S.R. 602 (E), dated the 31st July, 2012, published in the Gazette of India, Extraordinary, Part II, Section 3, Sub-section (i), dated the 31st July, 2012, had come to the conclusion that increased imports of Carbon Black (for rubber application) into India from the People’s Republic of China had caused and threatened to cause market disruption to the domestic producers of Carbon Black and it had necessitated the imposition of definitive safeguard duty on imports of Carbon Black (for rubber application) into India;

Now, therefore, in exercise of the powers conferred by sub-section (1) of section 8C of the said Act, and in accordance with the rules 12, 14 and 17 of the Customs Tariff (Transitional Product Specific Safeguard Duty) Rules, 2002, the Central Government after considering the said findings of the Director General (Safeguards), hereby imposes a safeguard duty on Carbon Black (for rubber application), falling under tariff item 2803 00 10 of the First Schedule to the said Act, when imported into India from the People’s Republic of China at the rate of-

- (a) Thirty per cent ad valorem minus anti-dumping duty payable, if any, when imported during the period from 5th October, 2012 to 4th October, 2013 (both days inclusive); and
- (b) Twenty five per cent ad valorem, minus anti-dumping duty payable, if any, when imported during the period from 5th October, 2013 to 31st December, 2013 (both days inclusive).

Non-tariff Notifications

In exercise of the powers conferred by section 14 of the Customs Act, 1962 (52 of 1962), and in super session of the notification of the Government of India in the Ministry of Finance (Department of Revenue) No.91/2012-CUSTOMS (N.T.), dated the 4th October, 2012 vide number S.O. 2360(E), dated the 4th October, 2012, except as respects things done or omitted to be done before such super session, the Central Board of Excise and Customs hereby determines that the rate of exchange of conversion of each of the foreign currency specified in column (2) of each of Schedule I and Schedule II annexed hereto into Indian currency or vice versa shall, with effect from 19th October, 2012 be the rate mentioned against it in the corresponding entry in column (3) thereof, for the purpose of the said section, relating to imported and export goods.

Table 6.4: Non-tariff Notifications

Schedule I			
S. No.	Foreign Currency	Rate of exchange of one unit of foreign currency equivalent to Indian rupees	
		(a)	(b)
(1)	(2)	(For Imported Goods)	(For Export Goods)
1.	Australian Dollar	55.10	53.70
2.	Bahrain Dinar	144.05	135.85

Contd...

Notes

3.	Canadian Dollar	54.15	52.80
4.	Danish Kroner	9.40	9.10
5.	EURO	69.85	68.20
6.	Hong Kong Dollar	6.85	6.75
7.	Kenya Shilling	63.90	60.00
8.	Kuwait Dinar	193.80	182.15
9.	New Zealand Dollar	43.75	42.45
10.	Norwegian Kroner	9.50	9.15
11.	Pound Sterling	86.10	84.00
12.	Singapore Dollar	43.80	42.75
13.	South African Rand	6.25	5.90
14.	Saudi Arabian Riyal	14.50	13.65
15.	Swedish Kroner	8.10	7.85
16.	Swiss Franc	57.85	56.35
17.	UAE Dirham	14.80	13.95
18.	US Dollar	53.20	52.25

Schedule II

S. No.	Foreign Currency	Rate of exchange of 100 units of foreign currency equivalent to Indian rupees	
(1)	(2)	(3)	
		(a)	(b)
		(For Imported Goods)	(For Export Goods)
1.	Japanese Yen	67.95	66.05



Task Visit the custom clearance website of India and highlight the latest amendments related to clearance of export and import.

Self Assessment

Fill in the blanks:

- The contributes to the harmonization of Customs and trade procedures, and the non-documentary trade data interchange in connection with such procedures, thus reducing the costs related to international trade.
- A may refer to a document allowing the importation of certain goods to countries without paying customs duty.
- An carnet is valid for one year from the date of its issuance.
- A carnet de passages *en douanes* is an internationally recognised customs document entitling the holder to temporarily import a duty-free into countries.
- means the assessable value as determined under the Customs Act, 1962 (52 of 1962).

6.7 Summary

- The Government of India has prescribed the rate of duty to be imposed under Customs Tariff Act, 1975. Import duty is levied on almost all items in order to restrict unnecessary imports and save precious foreign exchange for the nation, while export duty is levied only on a few limited products, where there is scarcity of Indian products for domestic requirements and the government wants to control the exports of such products or services so as to meet domestic demands. This is done by imposing exports duty on goods and services that go out of the country; thereby making such items expensive to international buyers.

Notes

- In case the importer has imported the goods for personal use, he can get his cargo cleared by payment of duty as assessed for home consumption after payment of the duties leviable.
- The Customs Department is very particular about the genuineness of import documents submitted by the importer and asks him/CHA for misdeclarations/or incorrect information is found, Customs has the right to take legal course of action against such importers.
- As per customs provisions, all imported goods in India are subject to be examined so as to judge the correctness of description/classification as given by the importer in the bill of entry. Such examination is not through hence a part of the consignment is selected and examined randomly.
- In case of export of cargo, the exporters will have to obtain mandatory PAN-based Import Export Code no (IEC Code) from the Directorate General of Foreign Trade as it is essential and legal to mention the IEC code number on the shipping bill, which will be submitted by exporter or his freight forwarder to the customs authorities for Let Export Order (L.E.O.).
- The Harmonized Commodity Description and Coding System generally referred to as "Harmonized System" or simply "HS" is a multipurpose international product nomenclature developed by the World Customs Organization (WCO).
- A carnet may refer to: in international law: A document allowing the importation of certain goods to countries without paying customs duty.

6.8 Keywords

A carnet de passages en douanes: is an internationally recognised customs document entitling the holder to temporarily import a vehicle duty-free into countries

ATA Carnet is an international Customs document that a traveler may use temporarily to import certain goods into a country without having to engage in the Customs formalities usually required for the importation of goods, and without having to pay duty or value-added taxes on the goods.

Carnet: document allowing the importation of certain goods to countries without paying customs duty.

Harmonised System: contributes to the harmonization of Customs and trade procedures, and the non-documentary trade data interchange in connection with such procedures, thus reducing the costs related to international trade

Landed Value: It means the assessable value as determined under the Customs Act, 1962 (52 of 1962)

The TIR Carnet: It is a customs transit document used to prove the existence of the international guarantee for duties and taxes for the goods transported under the TIR system,

6.9 Review Questions

1. Explain the custom clearance of imported cargo under non-EDI system of clearance. What documents are needed? Explain the rationale of each of them.
2. Explain the custom clearance procedure of exportable cargo under the Electronic Data Interchange System of cargo clearance.
3. Discuss the custom clearance of imported cargo under EDI system of cargo clearance.

4. Discuss the custom clearance of extractable cargo under the non-EDI system of cargo clearance. **Notes**
5. Explain:
- (a) Green channel facility
 - (b) Bill of Entry
 - (c) Export of goods under claim of drawbacks
 - (d) Export General Manifest
 - (e) Import General Manifest

Answers: Self Assessment

1. 1975
2. revenue
3. EDI
4. bill of entry
5. ICES Gateway
6. Green Channel
7. 5
8. TR-6
9. transparency
10. without
11. Harmonised System
12. Carnet
13. ATA
14. vehicle
15. Landed value

6.10 Further Readings



Books

Aseem Kumar, *Export and Import Management*: 2007, Excel Books.

Cherenilan Francis, *International Economics*, 4th Edition, Tata McGraw-Hill Publishing Company Limited.

Dr. Ram Singg, *International Trade Operations*, Excel Books, 2009.

Pradeep Kumar Sinha and Sanchari Sinha, *International Business Management: A Global Perspective*, Excel Books, 2008.



Online links

[www.ieport.com/Customs_manual/customs-manual-2012\(3\).PDF](http://www.ieport.com/Customs_manual/customs-manual-2012(3).PDF)

www.dov.gov.in/newsite3/clearance_procedure.asp

agritech.tnau.ac.in/export_import/importsysteem_procedure_custom.h...

Notes



Case Study

Apparel Retailer: Duty Drawback

Challenge

This OHL customer is the world's largest designer and retailer of maternity apparel. After importing their products into the U.S. from all over the world, it sells them in the U.S. and in Canada through retail stores and online outlets. As provisioned by the U.S. Customs' duty drawback program, companies can recoup import duty fees on products that are subsequently exported out of the U.S. The process can be difficult and time consuming causing some companies not to reclaim the duty paid while some companies are just unaware of the opportunity.

Approach

OHL met with the customer and developed duty drawback standard operating procedures and compliance manuals prior to filing duty drawback entries. OHL provides the customer with freight management services for its U.S. imports so detailed knowledge of the customer's products as well as access to specific documents required for such entries was already available. OHL handles duty drawback for the customer under summary export procedures in which entries are filed on a weekly basis instead of on every shipment. In addition, a one-time waiver project was initiated to secure duty drawback for exports made in the past but not claimed. This waiver, allowed by U.S. Customs just once, enables importers to recover duties within three years of export dating from the time the waiver is approved by customs. OHL also set up the customer with Accelerated Payment with U.S. Customs which allows the customer to receive their duty refund within 60 days and a Waiver of Prior Notice which allows the customer to export goods out of the U.S. without presenting to Customs for examination.

Value

This customer now recovers more than 90% of its Customs duties. The Accelerated Payment and Waiver of Prior Notice with U.S. Customs allow the customer to receive duty refunds within 60 days instead of the average 500+ days waiting period and save them time and money by not having to process products through U.S. Customs.

Return on Investment

In addition to the time saved by the customer by setting up compliant procedures, handling U.S. Customs entries, and the hundreds of days saved for receiving their duty drawback, OHL helped the customer secure a refund in excess of \$400,000 through the one-time waiver project and over \$500,000 in summary export duty drawbacks in just one calendar year.

Questions:

Write the case facts in brief.

Source: <http://www.ohl.com/sites/ohl/files/casestudy/Apparel-Retailer-Duty-Drawback-Case-Study.pdf>

Unit 7: Logistics and Characteristics of Modes of Transportation

Notes

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Objectives

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7.1 Definition

7.2 Planning Physical Distribution

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7.7 Summary

7.8 Keywords

7.9 Review Questions

7.10 Further Readings

Objectives

After studying this unit, you will be able to:

- Explain Planning Physical Distribution
- Discuss the Benefits of effective logistics system
- Describe the Concept of marketing logistics
- Explain the Critical elements of logistics system
- Discuss Logistics and modern Organisation

Introduction

Logistics is the one of the most important segment of the phenomenon of Marketing in business. It is a subset of Supply Chain Management. In the business functioning, the trader gets order for supply of his goods or services through his marketing executives or directly from customers and then to execute the order to the satisfaction of the customer, the trader or his supplier company prepares the Logistics, i.e. procures the product or services, puts labels on them, or gives some identification trademark name to them, makes necessary packing and packaging so as to save them from damage of any kind during loading, unloading, handling, transportation, etc. till is supplied to the end customer. More simply, it is a bundle of goods finally ready to be supplied to the customer. In Logistics study, all factors contributing till the last stage, when the goods or service is finally supplied to the consumer are systematically studied.


7.1 Definition

The word, Logistics' is derived from French word 'Loger', which means art of war pertaining to movement and supply of armies.

Notes

1. A military concept
2. Fighting a war requires:
 - ❖ Setting an objective
 - ❖ Meticulous planning to achieve the objective
 - ❖ Proper deployment of troops
 - ❖ Supply lines consisting of weaponry, food, etc.
3. A logistics plan should be such that there is minimum loss of men and material.

Similar to fighting a war in battlefield, marketing managers also prepare a suitable logistics plan that is capable of fulfilling the company objective of meeting the demand of targeted customers in a profitable way.



Notes Inbound logistics + Material Management + Physical Distribution = Logistics

1. Inbound logistics means the movement of materials received from suppliers.
2. Material management means the movement of material and components inside a firm.
3. Physical distribution refers to movement of goods outward from the end of the assembly line to the customer.
4. Supply chain management is larger than logistics and it links logistics more directly within the user's total communication network and with the firm engineering staff. It not only includes manufacturer and suppliers but also transporters, warehouses, retailers and customers themselves.
5. According to Council of Logistics Management: "Logistics is the process of planning, implementing and controlling the efficient, effective flow and storage of goods, services and related information from the point of origin to the point of consumption for the purpose of conforming the customer requirement".

Logistics management includes the design and administration of systems to control the flow of material, work-in-process, and finished inventory to support business unit strategy.

7.2 Planning Physical Distribution

The main goals of Distribution in any Organization would be to take care of proper storage and transport. While Storage assures product and packaging quality and constant availability, Transportation's objective is to ascertain that products arrive in good condition, in the right place and at the right time. The less frequent a Firm's re-supply, the greater would be its storage requirements.

7.2.1 Distribution Considerations

For proper Storage & Transportation, the SC Manager has to ensure availability of transportation (i.e., vehicles). He or she has to also take care of security the materials are being transported from one point to another. Security during storage also needs proper attention. What is also important is the availability sufficient storage space/capacity. This shall be based on procurement plan and frequency of deliveries at all levels of the system.

Technology has been changing very fast and as a result, the Product Life Cycles have become shorter. The short shelf life of products has been putting pressure on the Transport Function to deliver goods as quickly as possible. In addition to all these considerations, the SC Manager may have to also worry about appropriate storage conditions (cool chain), if the Products need to be preserved using this facility. What is also important is the mode of transportation to be used. Also, the Pick-up system (facilities collect drugs) or delivery system (warehouses deliver) has a bearing on the Distribution.

Another important factor is the decision to outsource transportation or not. One may have to also worry about aspects such as having appropriate procedures to:

- Verify the products shipped and received – type and quantity,
- Conduct visual inspection for quality assurance, including expiration dates,
- Complete and sign transaction records/vouchers,
- Store the products, and
- Update stock-keeping records

The main objectives of logistics management are:

- Inventory Reduction
- Reliable & Consistent Delivery Performance
- Economy in Freight
- Minimum Damages to the Product
- Quick Response
- Optimum Contribution towards business excellence

7.2.2 Inventory Reduction

Inventory Reductions have far-reaching implications on Company's Return On Investment (ROI). However, really speaking, it is a 'tight rope walk'! While excess stocks may affect the Profitability, not having enough inventories may result in 'Loss of Customers'. Therefore, one has to exercise proper control over Inventory, by taking appropriate steps at the right moment.

Objective of Inventory Control Systems

The objective of an inventory control system is to ensure the constant availability of products, by defining:

- When products should be ordered.
- What quantities of products should be ordered
- How to maintain adequate quantities to meet demand, while avoiding overstocks and stock-outs

Inventory Control Systems

Maximum/minimum Inventory Control System is defined by months of stock. Systems are designed so that stock quantities routinely fall between the minimum and maximum stock levels. The minimum stock level includes safety/buffer stock. Any inventory control system (max/min or other) must take into account safety/buffer stock. (However, in a Just-In-Time environment, the system of maintaining safety/buffer stock is not practiced.)

Notes

Inventory Control Considerations

Some of the prime considerations are:

- Who decides what quantities to distribute?
 - ❖ The lower level (pull) or the upper level (push)?
 - ❖ Decision should be based on training and human resource implications
- Which type of max/min system to use?
- How long should the pipeline be?
 - ❖ Longer pipeline reduces likelihood of stock-outs (more security stock) but increases likelihood of wastage (short shelf lives, increased expiries)
- How to include safety stock levels in a non-max/min system

Reliable and Consistent Delivery Performance

Customer Service is the key interface between Marketing and Logistics. It plays a significant role in developing and maintaining customer loyalty and continuous satisfaction. Logistics also supports the “place” element of marketing mix. However, in the areas of Product, Pricing and Promotion, Competitors may equal! Hence, there is a need to excel consistently in Customer Service through reliable & consistent delivery performance.

Freight Economy

The various Transportation Carrier Options available are: Truck, Rail, Water, Pipeline and Air. Inter-modal transportation is becoming more common since it is really not possible to use only one mode of transportation in most of the cases. Transportation by Road is perhaps the only mode which can be used independently.

7.2.3 Transport Fundamentals

Freight/Transport is the most important component of logistics cost. Usually 1/3 – 2/3 of total cost is the result of Transportation.

Transport involves

- Equipment (trucks, planes, trains, boats, pipeline),
- People (drivers, loaders & unloaders), and
- Decisions (routing, timing, quantities, equipment size, transport mode).



Caution When deciding the transport mode for a given product, there are several things to consider such as mode price, transit time & variability (reliability) and lastly potential for loss or damage.



Note In developing countries we often find it necessary to locate production close to both markets and resources, while in countries with developed distribution systems people can live in places far from production and resources.

Single-mode Service Choices and Issues

Notes

Air

- Rapidly growing segment of transportation industry
- Lightweight, small items (*Products*: Perishable and time sensitive goods: Flowers, produce, electronics, mail, emergency shipments, documents, etc.)
- Quick, reliable, expensive
- Often combined with trucking operations

Rail

- Low cost, high-volume (*Products*: Heavy industry, minerals, chemicals, agricultural products, autos, etc.)
- Improving flexibility
- Inter-modal service

Truck

- Most used mode
- Flexible, small loads (*Products*: Medium and light manufacturing, food, clothing, all retail goods)
- Trucks can go door-to-door as opposed to aeroplanes and trains.

Water

- One of oldest means of transport
- Low-cost, high-volume, slow
- Bulky, heavy and/or large items (*Products*: Nonperishable bulk cargo – Liquids, minerals, grain, petroleum, lumber, etc.)
- Standardized shipping containers improve service
- Combined with trucking & rail for complete systems
- International trade

Pipeline

- Primarily for oil & refined oil products
- Slurry lines carry coal or kaolin
- High capital investment
- Low operating costs
- Can cross difficult terrain
- Highly reliable; Low product losses

Transport Cost Characteristics

Transportation costs will be fixed costs as well as variable costs. Both these costs must be reviewed frequently and efforts must be made to bring these down.

Notes

Examples of fixed costs: Terminal facilities, Transport equipment, carrier administration, Roadway acquisition and maintenance [Infrastructure (road, rail, pipeline, navigation, etc.)] etc.

Examples of variable costs include: Fuel, Labor, Equipment maintenance, handling, pickup & delivery, taxes etc.



Note Cost structure varies by mode.

- Rail
 - ❖ High fixed costs, low variable costs
 - ❖ High volumes result in lower per unit (variable) costs
- Highway
 - ❖ Lower fixed costs (don't need to own or maintain roads)
 - ❖ Higher unit costs than rail due to lower capacity per truck
 - ❖ Terminal expenses and line-haul expenses
- Water
 - ❖ High terminal (port) costs and high equipment costs (both fixed)
 - ❖ Very low unit costs
- Air
 - ❖ Substantial fixed costs
 - ❖ Variable costs depend highly on distance traveled
- Pipeline
 - ❖ Highest proportion of fixed cost of any mode due to pipeline ownership and maintenance and extremely low variable costs

Minimum Damages to Product

Logistics Management must ensure that no/absolute damage happens while the product is in the custody of Logistics. Damage Costs incurred during transportation should be considered as a throughput cost, since they will continue regardless of inventory levels.



Did u know? Damage attributed to Warehouse operation is usually charged to the Warehouse Operator, if the cost is unreasonable.

Quick Response [QR]

Quick Response is generally a retail sector strategy, but can be tried by other industries too. Quick Response applies JIT principles throughout the entire supply chain. The concept works by combining Electronic Data Interchange (EDI) with Bar Coding Technology, so that Customer Sales are tracked immediately. This information is immediately passed on to the Manufacturer and from there to the suppliers to enable all the partners to plan, produce and deliver the replenishments to meet Customer Requirements quickly.

The benefits of such a system are:

Notes

- Inventory Reduction
- Speedier Response
- Lower number of stock-out situations
- Reduced Handling
- Reduction in Obsolescence

Contribution towards Business Excellence

About two decades back, Logistics Function was one of the neglected areas. It was looked at as a Cost Center. Not many organizations managed this function in a profession way. Gradually, the situations changed. With customer becoming more and more demanding, organizations realized the importance of this function and the role played by it in meeting the customers' expectations.

- Logistics primarily embodies the effort to deliver:
- The right product
- In the right quantity
- In the right condition
- To the right place
- At the right time
- For the right customer
- At the right cost



Task What role is played by logistics towards business excellence?

7.3 Benefits of Efficient Logistics System

Logistics has gained importance due to the following trends:

1. Transportation costs have risen rapidly due to the rise in oil prices
2. Production efficiency has scaled new heights
3. Fundamental changes in inventory
4. Proliferating product lines
5. Computer technology
6. Increased use of computers
7. Increase in public concern about the product. Growth of several new, large retail chains or mass merchandise with large demands and very sophisticated logistics services, bypassing traditional channels and distribution
8. Economic regulation reduction
9. Increase in power of retailers
10. Globalization

Notes

The interrelation of different logistic elements and their costs should be based on total cost rather than individual costs.

Self Assessment

Fill in the blanks:

1. logistics means the movement of materials received from suppliers.
2. objective is to ascertain that products arrive in good condition, in the right place and at the right time.
3. The objective of an control system is to ensure the constant availability of products
4. Customer is the key interface between Marketing & Logistics.
5. plays a significant role in developing and maintaining customer loyalty & continuous satisfaction.
6. must ensure that no/absolute damage happens while the Product is in the custody of Logistics.
7. Costs incurred during transportation should be considered as a throughput cost, since they will continue regardless of inventory levels
8. Transportation by Road is perhaps the only mode which can be used
9. The main goals of in any Organization would be to take care of proper storage & transport.
10. Transportation's objective is to ascertain that arrive in good condition, in the right place and at the right time.

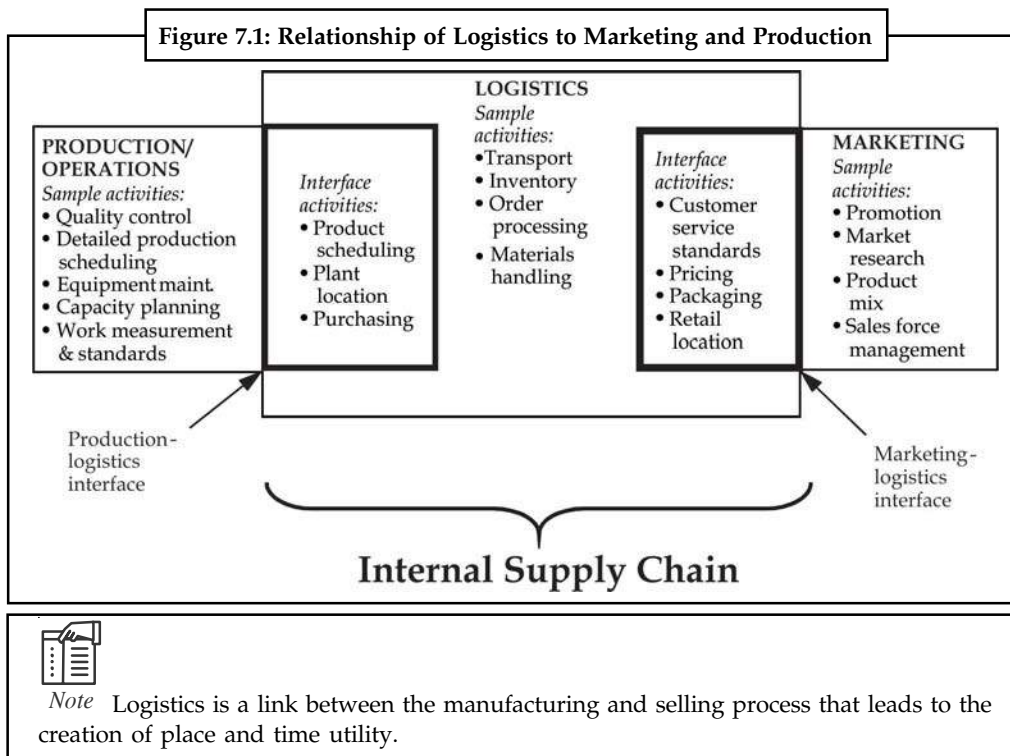
7.4 Concept of Marketing Logistics System

Managing the components of Logistics, like – product (procuring, assembling or self-production), form (shape, size, label, design), time (the period of booking and execution of the order), quality (quantity, material, colour, in view of the competitive products in the market, or as per demand of the customer), price (low, high, competitive), services (labelling, packaging, transportation, supply) – are the vital factors in the overall marketing process. Simply, Logistics is a subsystem of Supply Chain Management, which is a key part of Marketing process.

7.4.1 Relationship of Logistics to Marketing and Production

While the production element in the marketing-mix leads to creation of 'form' utility by taking decisions as product line variety, design, colour brand, etc. The distribution element comprising distribution channel fixation and physical movement, creates 'time' and 'place' utility by ensuring that the produced goods reach the place and time selected by the buyer.

Logistics is the designing and managing of a system in order to control the flow of material throughout a firm. This is a very important part of an international company because of geographical barriers. Logistics of an international company includes movement of raw materials, coordinating flows in and out of different countries, selection of transportation, cost of the transportation, packaging of the product for shipment, storage of the product, and managing the entire process.



7.4.2 Marketing Logistics

In 1991, the Council of Logistics Management (CLM), a prestigious professional organization, defined logistics as “the process of planning, implementing and controlling the efficient, effective flow from the point of origin to the point of consumption for the purpose of conforming to customer requirements”.

Logistics is the art of managing the flow of raw materials and finished goods from the source to the user. To obtain goods from where they arise to the right place in the right form, at the right time, at the right cost. “Logistics or physical distribution or distribution logistics is a part of Marketing Process”.

In order to position logistics in its proper role in today’s business environment, logistics leaders will have to do a better job of communicating, or marketing, logistics. The time for lamenting the lack of interest in logistics from senior management is over, and the time to become proactive is here. The logistics story will be understood when all logistics leaders begin to take the marketing initiative and the successes of the discipline are recognized.

Logistics executives are eager to be considered important players in the corporate game. They want to be involved in important decisions, to do something meaningful for the company, and to be recognized by their peers as members of a winning team. However, it seems that sales, marketing, and manufacturing enjoy the focus of management attention. Why? Let us suggest that logistics executives have done a poor job of marketing logistics within the organization.

This concept of “marketing” logistics borrows from the traditional concept of marketing. In other words, identify your customers, identify their needs, and combine the firm’s resources to meet those needs. However, the concept of logistics marketing goes a little further. The purpose of this paper is to introduce the concept of the 5 P’s and to provide the logistics executive with a framework for its implementation. The following discussion will focus on product, price, place, promotion, and people as elements of the logistics marketing mix.

Notes

Product

One function of logistics marketing is finding out who your customer is and how to get the product or service to the customer. Each customer can have individualized needs so the logistical services provided may vary from customer to customer. Regardless of these differences, the customers expects 100 percent conformance and assured reliability at all times with every transaction.

The goals of this aspect of marketing logistics include filling the order, on-time delivery, precise invoicing and zero damage.

Price

An organization bases pricing decisions on both internal and external factors. Marketing logistics must recognize price drivers. The profile of the customer, the product and the type of order are factors that drive the price. These changes are not typically controlled by marketing logistics.

However, marketing logistics must react to these factors and understand how the factors affect customers' decisions. Discounts for quantities and the related logistical cost structure can impact the price the customer will ultimately pay for the product or service.

Additional factors driving price include the shipping costs based on the size, weight and distance the organization will ship the item. Further, the size of the manufacturing run, labor costs and the types, quantities and quality of the materials used in the manufacturing process can affect price.

Promotion

Promotion is another important aspect of an organization's marketing logistics process. When bringing a product to market, the organization must coordinate the logistics of the various marketing materials.

For example, the art department might design the artwork for the product's box and an outside supplier might manufacture the boxes with the artwork. Marketing logistics can help to ensure that all of these entities work together and produce the marketing materials needed to sell the product.

Place

The function of place in marketing logistics allows the organization to simplify the transactions between a logistics provider and the customer.

The organization must execute logistics in such a way that the customer is not aware of the complexities involved in the logistics process.

For the customer, the output is always more important than the process. The organization should, therefore, never expose the backroom processes involved with logistics delivery to the customer. Also the location of the factory, warehouse and customer can greatly impact the marketing logistics process by increasing or reducing costs.



Example: Locating a factory in Mexico might reduce the labor costs associated with a product. However, at the same time locating the factory in Mexico might increase the shipping costs and negate any cost savings.

People

Notes

The most important element of the logistics marketing concept is people. Without effective people, the other four P's are meaningless. The logistics executive has the responsibility to develop a culture for stellar performance from the individuals in the organization. This can be done in several ways:

- First, help develop an enthusiasm for the business. People will strive harder to accomplish goals that excite them.
- Second, develop a commitment to bring ideas to fruition; delegate responsibility and authority to the people in the logistics organization to make things happen. The logistics executive must encourage results from the organization.
- Third, the logistics executive must develop a team environment within the organization. A true team environment exists when individual successes can be celebrated by the team and individual failures shared by the team. Important to the implementation of teams is the concept of process. Logistics processes must be identified and documented with individuals owning pieces of these processes. True process ownership is a basic requirement for a successful team environment.
- Fourth, the logistics executive must believe in the "pressure up" concept versus the "pressure down" concept. In other words, the logistics executive must provide the atmosphere for individuals to ask for help, to communicate their frustrations, to raise issues with management, and to have inputs to plans. This pressure goes up through the organization until a resolution/remedy/positive action is taken.

Finally, the logistics executive needs to be a leader. People will perform for managers because they have to; they will perform for leaders because they want to. The logistics leader must not be hypocritical. Leaders set practice by example and people will tend more to follow by example. The logistics leader must not be afraid to delegate decision-making authority and responsibility. The logistics leader understands that success comes from the performance of the team, and not from the performance of the individual.

7.4.3 Logistics in Marketing

Marketing process is successfully completed only when:

1. Arrangements are made to supply the goods through selected distribution channels.
2. Products are produced and priced to satisfy the identified needs of the customers.
3. Goods are physically supplied to the buyers at the place and time selected.
4. An awareness is created among the buyers about the availability of the goods through advertisement.
5. Other than satisfying the customers' needs, the marketing process must be profitable to the seller.

Utility does not merely denote the usefulness of a product to satisfy the customer needs but also involves the product from a manufacturing facility to the user.

Figure 7.2: Trends in Marketing

	Past Expectation	Today's Expectation
Products	Standardized Products	Customized Products
Forms	Predefined	Often Configured
Time	Now as available	When wanted
Quality	Acceptable	Exceed Expectation
Price	Low	Competitive
Value Added	Minimal	Complex
Services		

Importance of Logistics in Export Management

International trade is becoming a more important part of the GNP in the industrially advanced countries. Firms in these countries have production centres for markets all over the world. Shortage of local resources, small size of home market and many other reasons have resulted in functional centres being maintained in various countries.

A lot of issues that are associated with international transportation of finished goods are essentially the same as those that apply to transportation in domestic trade. In case of international operations, goods can be out of the exporter's control for longer period of time, more documentation is required, packaging may be more costly and shipping insurance is more costly.

The transportation options include ocean shipping and containerization as well as air freight. The basic activities involved in the flow of goods, like transportation, warehousing and holding of inventories, should be integrated in a systems approach. The systems approach would recognize the trade-offs, such that sometimes more expensive air freight may be opted for, instead of less expensive ocean shipping, because of savings in warehouse and inventory costs.

In the field of exports, transport systems in developing countries are generally not as efficient as in the industrially developed countries. Transportation is often considered to be the most important single factor of plant location.

Firms in international trade also try to reduce amount of unnecessary product packaging, since packing material can account for almost 45 per cent of the weight of the products shipped. A company can reduce inland transportation charges by locating its distribution facilities near to container ports or airports. The burden of documentation can be reduced through computerization.

Export management involves marketing in overseas market. As such, the discussions on the interface of logistics with marketing hold good for the importance of logistics in export management. Still, export management has certain unique features, to be understood in the context of importance of logistics to export management.

7.5 Logistics and the Modern Organization

Logistic Management includes the design and administration of systems to control the flow of material, work-in-progress and finished inventory to support business unit strategy.

Discussion of the concept of logistics, its place in the value-chain process leading to profitability, its contribution as one of the primary functions and its interface with other functions of the firm bring out its importance as a strategic resource. To be of a real strategic influence, a good amount of competency has to be reached and a well-defined logistical mission and aims has to be committed to, by everyone in the firm, especially by the top management.

7.5.1 Logistical Competency

Logistics involves detailed and complex work. Logistical management starts with how logistical competency fits into a firm's overall strategy. It is fundamentally important to view logistics as to how it can be exploited as a main competency. To develop logistical competency, it is important to develop an integrated framework that defines and relates important concepts. This integration should be in such a way that competitively superior logistical performance should contribute to the overall strategy of the firm.

Logistical competency is a relative assessment of a firm's ability to provide competitively superior customer service at the least possible cost. This means that logistical performance is dedicated to supporting any or all marketing and manufacturing requirements in a manner that exploits delivery capability. The strategy is to provide superior service at a cost below industry average.

Alternative logistical capabilities, emphasizing flexibility, operational control, and most of all a commitment to provide perfect service performance typically characterise the service platform of superior logistic achievers.

7.5.2 The Logistical Mission

Logistics exists to satisfy customer requirements by facilitating important manufacturing and marketing operations. The challenge is to balance service expectations and cost expenditures to attain business goals.

Logistical service is measured in terms of:

- **Availability:** Availability denotes having inventory to consistently meet the need of the customer material or product requirements.
- **Operational Performance:** Operational performance means the elapsed time from order receipt to delivery. Operational performance involves delivery speed and consistency. A firm's operational performance can be measured in terms of how flexible it is in accommodating unusual and unexpected request of customer.
- **Service Reliability:** Service reliability pertains to the quality attributes of logistics. For logistics performance to continuously meet customer expectations, it is necessary that management should be committed to continuous improvement.

Total cost is positioned to include all expenditures necessary to perform logistical requirements.

The concept of total cost had not previously been applied to logistical analysis. Managers focused on minimizing functional cost, such as transportation, in the expectation that such effort would achieve the lowest combined cost. The total-cost concept opened the door to examining how functional costs interrelate.

The right level of logistics cost expenditure must be related to desired service performance. The simultaneous attainment of high availability, operational performance, and reliability is expensive. An important managerial challenge comes from the fact that logistical cost and increased performance have no proportional relation.

Notes



Did u know? The typical logistical system in a firm seeks to develop and implement an overall logistical competency that satisfies important customer expectations at a realistic total-cost expenditure.

Logistical management is concerned with operations and coordination. Operations mean strategic movement and storage. To complete the total operations mission attention must be given to integrating physical distribution, manufacturing support, and procurement into a single logistical process. Functioning as an integrated and coordinated process can best provide operational management of materials; semi-finished components, and finished products moving between locations, supply sources, and customers of a firm.

The mission of the logistical system is measured in terms of total cost and performance. Performance measurement is concerned with the availability of inventory, operational capability, and quality of effort. Logistical costs are directly related to required level of performance. The greater the required performance, the higher is the total logistics cost. The key to effective logistical performance is to develop a balanced effort of service performance and total-cost expenditure.

The strategic integration of logistics is fundamental to a firms's success. A firm may not opt to differentiate competitively on the basis of logistical competency; it must perform logistical responsibilities as part of the fundamental process of creating customer value. The relative importance that a firm places on logistical competency will determine the degree of importance on achieving internal and external integration.

Flexibility is important to logistical competency. Logistical flexibility results from integration and from implementing time-based control techniques.

7.5.3 Four Logistics Concepts

- **The systems concept:** The systems concept is mainly based on all functions of organization working together to an maximize benefits. This concept sometimes requires certain components of the organization to operate sub-optimally in order to achieve maximum goals of the system.
- **The total cost concept:** The total cost concept is based on the systems concept; goal achievement is measured in terms of cost.
- **The after-tax concept:** A variation of the total cost concept is the after-tax concept. The goal of this concept is after-tax profit. This concept is becoming very popular because of the many different national tax policies.
- **The trade-off concept:** The trade-off concept links the system together in a way that is very efficient, but can have trade-offs that might be inefficient. The advantages of such high efficiency must be weighed against the risk involved.

Logistics is a system having a number of components, which can be combined in different proportions to achieve a set goal.

The long-term objective is profitability, while the short-term objective is to survive competition by recovering marginal costs.

7.5.4 Logistics Sub-systems

Logistical sub-systems encompass the following:

1. Physical Supply or management of flow of raw materials, spare parts, consumable stores and machinery and tools from suppliers.

2. Physical distribution or management of finished goods from the factory to the customers.
3. Logistical controls for managing the logistics system; these help in the efficient coordination of physical supply and distribution sub-systems.

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The aim of an ideal logistic system is to ensure flow of supply to the customer:

1. In the right quantity
2. At the required location
3. At the required time
4. In a usable condition
5. At the lowest total cost

Thus, the objectives encompass efforts to coordinate physical distribution and material management in order to save money.



Task Study the Barriers to Internal Logistics Integration with reference to a particular company of your choice?

7.6 Critical Elements of Logistics System

Logistics comprises the following fundamental elements:

1. Transportation
2. Warehousing
3. Inventory Management
4. Packing and Utilization, and
5. Information & Communication

Given a facility network and information capability, transportation is the operational area of logistics that geographically positions inventory. Due to its fundamental importance and visible cost, transportation has received considerable managerial attention over the years. Firms, big and small, have managers responsible for transportation. Finding and managing the needed transportation mix is a main responsibility of logistics.

Network of the functional areas of logistics – information, transportation, and inventory – can be engineered into a variety of different operational arrangements. Each arrangement will have the potential to achieve a level of customer service at cost; these three functions combine to create a system solution for integrated logistics. The final functions of logistics namely – warehousing, material handling and packaging – also represent an integral part of an operating solution. These functions do not have the independent status of the three previously mentioned. Warehousing, material handling and packaging are an integral part of other logistics areas. Merchandise typically needs to be warehoused at selected times during the logistics process. Transportation vehicles require material handling for efficient loading and unloading. The individual products are most efficiently handled when packaged together into shipping cartons or other types of containers.

Logistics is viewed as the competency that links a firm with its customers and suppliers. Information from and about customers flows through the firm in the form of sales activity, forecasts and orders. The whole process is viewed in terms of two interrelated efforts, inventory flow and information flow.

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Information flow is an important element of logistics operations. Paper-based information flow increases both operating cost and decreases customer satisfaction. Electronic information movement and management provide the opportunity to reduce logistics expense through increased coordination and to enhance service by offering better information to customers.

Information flow was often overlooked because it was not viewed as being important to customers. The Council of Logistics Management recognized this change in 1988 when it incorporated “material, in-process, finished goods and information” into its definition of logistics.

Transportation is a key activity in the logistics value chain as it moves product through the different stages of production and finally to consumer. The important functions include – product movement, product storage and integration of international production and distribution operations. The major transportation principles involve economies of scale and economies of distance.



Caution The distribution systems should not be designed to hold inventory for an excessive length of time, though there are occasions when inventory storage is justified.

The traditional warehousing role has been to maintain a supply of goods to protect against uncertainty, contemporary warehousing offers many other value-added services. These services can be described in terms of economic and service benefits. Economic benefits include consolidation, break bulk and cross-dock, processing/postponement, and stockpiling. Service benefits include spot stocking, assortment, mixing, product support and market presence.

The handling of products is an important factor in warehouse productivity. Handling activities include receiving, in-storage handling and shipping. Packaging has a significant impact on the cost and productivity of the logistical system. An integrated logistics approach to packaging operations can yield dramatic savings.

7.6.1 Marketing Mix

A marketing mix is a combination of activities designed to attract customers while simultaneously achieving business goals. The four Ps—products/service, promotion, price, and place – constitute a generic marketing mix. The key to formulating an effective mix strategy is to integrate resources committed to these activities into an effort that maximizes customer impact. Logistics ensures that customer requirements involved in timing and location of inventory and other related services are satisfactorily performed. The output of logistical performance is customer service. Logistical competence is a tangible way to attract customers who place importance on time and place-related performance.

Logistics interface with marketing and the system elements brings out the depth of the scope of logistics in the efficient functioning of any business entity. The key to excellent logistics is to achieve integration of both internal and external operations. Such integration requires clear identification concerning the role that logistical competency is expected to play in overall firms strategy.

Important Factors

The important factors involved in efficient and effective logistics system are:

1. Shippers
2. Suppliers

3. Carriers
4. Warehouse providers
5. Freight forwarders
6. Terminal operators
7. The Government

Trade-off Analysis

Trade-off analysis is a family of methods by which respondents' utilities for various product features are measured. The utilities are measured indirectly. Respondents are asked to consider alternatives and state a likelihood of purchase or preference for each alternative. As the respondent continues to make choices, a pattern begins to emerge which, through complex multiple regression techniques, can be broken down and analyzed as to the individual features that contribute most to the purchase likelihood or preference. The importance or influence contributed by the component parts, i.e. product features, are measured in relative units called "utils" or "utility weights."

Respondents are asked to tell the interviewer directly how important various product features are to them.

Trade-off analyses produce several types of information. They tell us what features are most valued by customers. They allow us to model how likely people will be to purchase various configurations of products, the share of revenue these products will most likely receive and what role price plays in the assessment of acceptability.

Now, we will discuss the trade off types briefly:

- **Experimental Design:** A critical issue in most trade-off methods is the selection of product attributes to be combined together to create each product configuration to be tested.

If every possible combination of attributes was included in the study, the study would be said to be using a complete or full factorial design. This is desirable but very seldom practical. When a fractional factorial design is used, only a fraction of the total possible number of product combinations needs to be tested. It must be kept in mind, that whenever a fractional factorial design is used, some information will be lost. It is the job of the researcher creating the experimental design to ensure that the information being sacrificed does not compromise the project's ability to answer the research objectives.

- **Bridging:** Even with the most efficient fractional factorial design, we still end up with more products than can be practically accommodated. One possible solution to that problem is bridging. Bridging allows the attributes to be divided into two or more sets. Each set of attributes is treated like its own trade-off study. A fractional factorial design is created for each set of attributes. Respondents are asked to rate or rank two smaller sets of products rather than one large set. The utilities are calculated for each trade-off exercise independently and bridged together to create one final set of utilities.
- **Cognitive and Non-cognitive Behaviour:** Critical to the selection of an appropriate trade-off technique is the issue of which type of behaviour, cognitive or non-cognitive, best represents the behaviour being measured. Cognitive behaviour is behaviour that is based on rational, conscious decision-making. Such factors as – price, functionality or durability are typically cognitive. Non-cognitive behaviour is behaviour that is based on less tangible or even less conscious factors such as status, aspiration, insecurity, etc. One might argue that the selection of a life insurance policy, a television set or a water purifier are all

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cognitive decisions and that the selection of a whisky, a facial cream or a pair of jeans are all non-cognitive. One might also argue that all decisions made by humans are non-cognitive.

However, trade-off techniques that employ direct questions (self-explicated and hybrid) all assume that the behaviour being modelled is cognitive, because at least some of the product features are being rated in a way that requires both awareness and honesty from the respondent. The respondent must be aware of the degree to which a product feature affects his or her purchase decision and also be willing to admit to that degree of affect.

Additionally, any data collection methods that rely on verbal or written descriptions of product features all assume that the behaviour being modelled is cognitive, because the process of understanding a verbal or written description is itself a cognitive behaviour.

Non-cognitive trade-off models should be based on an indirect trade-off technique (conjoint or discrete choice) and data collection that relies on experience rather than language to communicate the product choices. For example, if you are modelling the pant selection process, show respondents a variety of pants that they can see and touch. A consumer may respond to the phrase "light blue pants" very differently than he or she would to a particular pair of light blue pants.

Self Assessment

Fill in the blanks:

11. does not merely denote the usefulness of a product to satisfy the customer needs but also involves the product from a manufacturing facility to the user.
12. Logistic Management includes the design and administration of systems to control the flow of material, work-in-progress and inventory to support business unit strategy.
13. Logistical is a relative assessment of a firm's ability to provide competitively superior customer service at the least possible cost.
14. A firm's performance can be measured in terms of how flexible it is in accommodating unusual and unexpected request of customer.
15. information flow increases both operating cost and decreases customer satisfaction.

7.7 Summary

- Logistics is that part of supply chain process that manages the flow of goods, information and other resources, including energy and people, between the point of origin and the point of consumption in order to meet the requirements of consumer.
- It improves customer satisfaction directly through rapid response and minimum variance and indirectly through minimum inventory, consolidated movement, improvement in quality and life cycle support.
- It creates value by giving the desired level of value at the least possible cost.
- The objective of an inventory control system is to ensure the constant availability of products.
- Transportation Costs will be fixed costs as well as variable costs. Both these costs must be reviewed frequently and efforts must be made to bring these down.

7.8 Keywords

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Forecasting and Procurement: Forecasting and Procurement functions are critically important to injection safety commodity availability. This requires that financial resources, technical skills, and management systems are in place.

Inventory Control: Inventory management is the process of receiving, storing, issuing, ordering and distribution of injection safety commodities to various sites.

Product Selection: This is dependent on what customers are using or what service providers are prescribing. The products here are single use syringes and needles, safety boxes and needle removers.

Serving Customers: This is the priority of the cycle. Customers are the clients/patients who determine what is done within the cycle.

7.9 Review Questions

1. What do you understand by the concept of logistics?
2. What do you mean by physical distribution? Discuss its importance.
3. What do you think are the benefits of an efficient logistics system?
4. Discuss the concept of marketing logistics in detail.
5. What are the important 'Distribution Considerations?' Discuss in depth.
6. What are the critical elements of the logistics system?

Answers: Self Assessment

1. Inbound
2. Transportation's
3. inventory
4. Service
5. Customer Service
6. Logistics Management
7. Damage
8. independently
9. Distribution
10. products
11. Utility
12. finished
13. competency
14. operational
15. Paper-based

Notes

7.10 Further Readings



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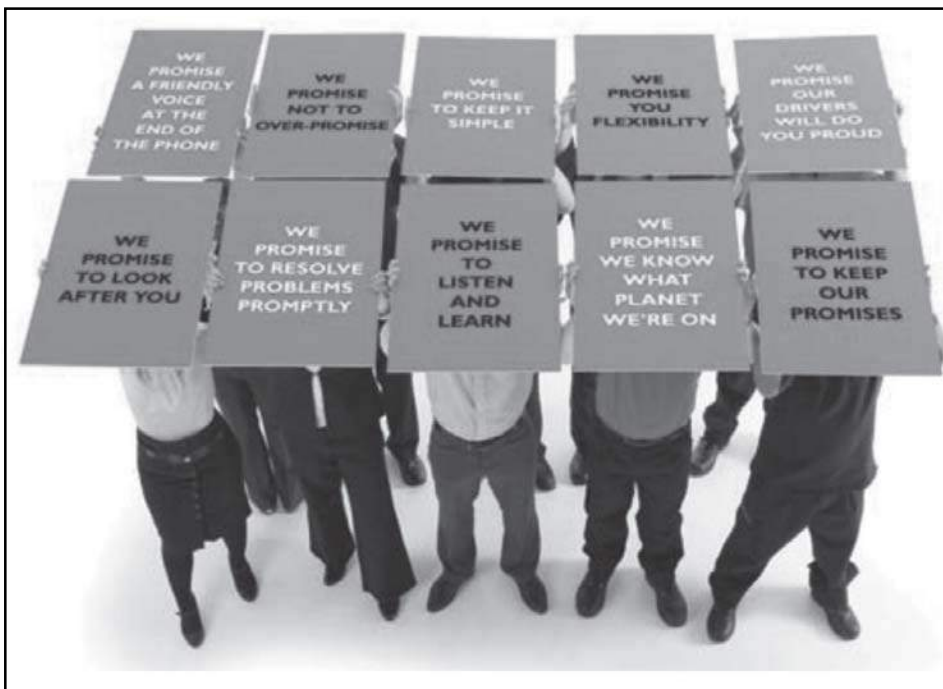
Case Study

Delivering a Superior Customer Experience

The reputation of a business may be affected by what its customers think and say about its products or services. This is driven by the experience of customers when dealing with the business. High quality customer service will encourage customers to become regular or repeat users or purchasers. On the other hand, a poor customer experience may damage a business through loss of consumer confidence.

TNT was founded in Australia in 1946 by Ken Thomas with a single truck. Today, TNT is a global business and the market leader in business-to-business (B2B) express delivery services, delivering up to 150 million items per year. It has the largest individual share of the national market and employs over 10,000 people across the UK and Ireland. TNT operates in the tertiary (or service) sector of the economy which provides widely varying services to other businesses and to consumers. The tertiary sector is the largest sector of the UK economy, ahead of the primary (extraction) and secondary (manufacturing) sectors.

In 2008 TNT recognised that the increasing expectations of customers meant the business had to make major changes to ensure it could meet their needs.



In-depth research showed that customer satisfaction depended not just on the process of delivering the service, but also on how the service was carried out. This resulted in TNT adopting a core strategy focused on delivering a quality customer experience. It developed a two-year programme to implement and communicate its Customer Promise to employees and customers.

In order to achieve the levels of process innovation and continuous improvement that the customer focus strategy required, TNT also needed to ensure the capabilities of its people were aligned to this, particularly in delivering a high quality customer experience. A review of new employees to the company showed that only 10% held qualifications above

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QCF (Qualifications and Credit Framework) level 2, compared to the industry norm of 52% (as identified by Skills for Logistics Research).

This case study examines how TNT's Customer Promise reflects its core strategy of customer focus and aligns with its corporate values to influence the organisation's culture.

Why is Customer focus so Important?

Customer service is a series of activities designed to deliver customer satisfaction. The process of providing customer satisfaction is based on an understanding of what customers want and need. Effective businesses aim to anticipate and meet or exceed these needs. It also requires effective communication.

A high quality customer experience needs to apply from initial contact through to after-sales care, whether the customer generates a one-off transaction or regular repeat business.

There are many different aspects which underpin customer satisfaction in a business. These include:

- *ease of use* – educating customers so that they know how to get the best from the service or product and designing services that are easy to use and access.
- *personal relationships* – building a rapport with customers to make them feel valued and that their needs are important, so that they develop an attachment to the service.
- *appropriate payment systems* – enabling customers to pay in ways that are convenient to them and at appropriate time, such as on satisfactory completion of service.
- *an effective complaints process* – dealing with any problems or complaints promptly and making sure customers know of the outcome.
- *after-sales service* – checking that customers have had a satisfactory experience and offering other potentially relevant services to extend the customer relationship.

The various elements of providing a satisfactory customer experience should relate to customer needs. Relevant factors for TNT customers involve:

- *on-time delivery* – TNT aims to deliver all documents, parcels and freight to the customer's required timescale through its door-to-door integrated air and road network.
- *24/7 tracking* – TNT's sophisticated online technology makes it possible for customers to track where their consignments are at any time of day, giving them reassurance.
- *personal attention* – TNT can accommodate specific customer requirements for safe delivery of unusual or fragile items. For example, on one occasion, the company transported a lifesized fibreglass Friesian cow from Scotland to a farm in Northern Ireland!

The Customer Experience at TNT

TNT's market is highly competitive. In TNT's market there are at least 13 direct competitors. TNT's Customer Promise is designed to deliver a competitive advantage, something that competitors will find hard to copy. As well as providing a 'superior customer experience', the Promise:

- supports TNT's market-leading position
- helps to retain existing customers and attract new ones

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- motivates staff by demonstrating their valuable input
- provides a means of differentiating the business.

In order to achieve differentiation, TNT has embedded the company's values – 'to be a trustworthy, values-based company with a reputation for integrity, transparency and compliance' – into its Customer Promise. TNT claims: 'Actions speak louder than words and that when we say "Sure we can", we mean it'. This 'can-do' attitude and positive mindset affect all aspects of TNT's business.

The Customer Promise highlights the expertise and positive mindset behind TNT's strapline 'Sure we can'. It shows that TNT listens to customers and can add value. For example, TNT promises a 'friendly voice at the end of the phone'. To ensure this, TNT's own knowledgeable people deal directly with customers. Its promise 'to resolve problems promptly' is demonstrated by how it intercepts and repackages damaged parcels to avoid goods being damaged and customers disappointed.

Employees are instructed to be honest with customers – even if there is a problem. This fulfils its promise 'not to over-promise'. TNT aims for its drivers 'to do you proud' by training them so there is the same focus on quality customer service throughout the whole process. Its promise 'to look after you' is demonstrated in a variety of ways: by offering a range of delivery options such as door-to-door delivery as well as online booking which allows customers themselves to reschedule deliveries where necessary to make things easier. Its promise 'to keep our promise' is upheld by the fact that the standards are set at the top by the managing director and communicated throughout TNT so everyone is working to the same values.

Other examples of practical changes to improve the customer experience included an online ordering service for customer stationery and an online invoicing option for those customers who want it.

TNT monitors and reviews regularly all activities relating to the customer experience, both internally and externally, to ensure it remains fresh for both customers and employees.

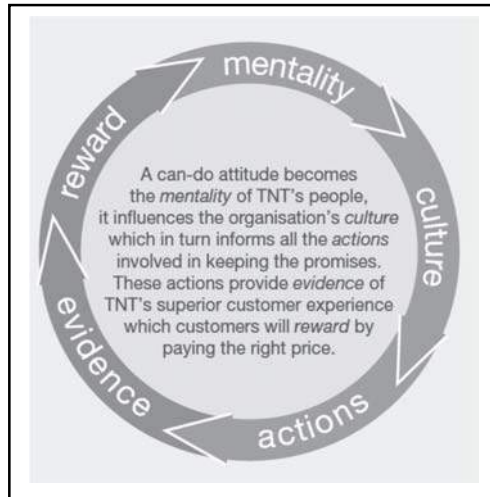
Communicating the Promise

TNT's people meet with or talk to customers on a regular basis. They are the public face of the organisation and represent its brand values. They hear first-hand what customer want or like. TNT recognises that its Customer Promise will therefore only be effectively delivered if its employees understand every aspect of the customer relationship. Part of setting up the Customer Promise involved communicating the change both within the organisation and externally to customers:

- Employees received a letter from the MD announcing the Customer Promise. TNT also arranged workshops to ensure everyone had the same information. It organised a job shadowing scheme so employees could understand how their roles affected other staff and potentially the customer. Alongside this, various communication tools were used to refresh the messages for all employees. These included a pocket guide, a key ring, posters, an internal magazine and videos on the intranet
- Customers received new literature. These included the MD's letter, an information pack for new customers and a regular customer magazine, as well as direct mail about the Customer Promise to 300,000 existing, lapsed and prospect customers. TNT also set up a new feedback option on its website for customers to give their views on the service.

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TNT encourages its people to 'think on their feet'. They are expected to seize opportunities and not just meet customer requirements but also exceed them. This is part of the organisation's entrepreneurial culture. TNT encourages people to make decisions for themselves (based around documented procedures and values), rather than wait to be told what to do.

This helps to give faster responses to customers. TNT also set up an employee suggestion scheme, called I'dea. Employees can make suggestions for improving working practices and TNT can learn from its people as well as helping them to develop. This is part of its two-way commitment model.

Recognising the People behind the Promise

Employees are one of the most important resources a service organisation has and TNT's ability to deliver on its Customer Promise rests in its people. Effective organisations need engaged people who have the skills to deliver the company's aims and objectives. This needs a two-way commitment. Employees need to be committed to the organisation; the organisation needs to support and reward its employees.

TNT recognises the contribution its people make in different ways. First, it invests in developing people, offering a variety of career options from driving to marketing. It carries out a training needs analysis for new employees. This assesses their existing skills and abilities in order to identify the training and development requirements that employees may have in order to carry out their current roles effectively. This also helps them to progress their career within TNT. TNT provides the training people need to do the job (learning the specific skills and knowledge required to work in the TNT way), as well as opportunities for personal development. TNT was one of the first 16 businesses to achieve Investors in People (IiP) status.

This is an independently accredited standard awarded to organisations that demonstrate commitment to people development. Investing in people helps to increase customer satisfaction and leads to more business.

TNT's focus on enhancing people's wider capabilities as preparation for future roles in the company leads to a 'win-win' situation. Employees gain from good jobs with prospects. The organisation gains from employing people who are able to promote its brand values and deliver exceptional service. Developing people helps to ensure the company has the right skills in the workforce to improve performance today and grow the business tomorrow.

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Examples of TNT's training and development programmes include:

- a foundation degree with Hull College – this is mapped to national qualifications and focuses on the logistics industry. This is a great example of workplace learning and bridges the gap between academic study and work
- a foundation degree with Coventry University – this is mapped to national qualifications and focuses on management and leadership
- a five-year apprenticeship programme for young people in vehicle maintenance – this ensures that TNT has the skills it needs to keep its fleet up to standard.

TNT people are recognised in other ways. Employees are encouraged to move between roles to learn more about the company. This form of job enrichment means employees experience variety at work and improve their skills in different areas. TNT also offers the opportunity to develop and progress within the company. Around 70% of supervisory roles are filled internally. Graduates who start working for TNT are expected to take on management roles within five years.

High performing teams and depots receive recognition and rewards through TNT's awards schemes. TNT's 'Delivering More' scheme rewards and recognises those employees who have gone beyond the call of duty. Over 4,000 awards are made each year.

Conclusion

Effective customer service involves meeting or exceeding customer needs. However, customer service is not just about what you do for your customers, it also concerns how the service is carried out. TNT monitors and measures performance to ensure its activities are delivering the strategy. For example, it conducts telephone interviews each week with a sample of customers to review their perceptions of its services and assess levels of customer loyalty.

Since TNT's strategy of focusing on the customer experience was set up in 2009, it has delivered strong results:

- TNT has achieved the highest levels of customer satisfaction in its market measured on 31 aspects linked to the Customer Promise.
- The Customer Promise programme has increased productivity and generated savings overall of almost £660K.
- The company achieved its targets in 2010 and 2011 despite the difficult economic climate.
- 100% of new operations employees will have a relevant qualification, making TNT the industry leader.

Questions:

1. What is customer service? Give two examples of different aspects of customer service.
2. Explain how each of the elements of TNT's Customer Promise relates to customer service.
3. Using the TNT website, identify three additional examples of ways in which TNT provides quality customer service.
4. Evaluate how developing its employees enables TNT to benefit its customers. What drawbacks might there be for the organisation?

Unit 8: International Transport System

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8.5 Significance of Transportation Services

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Objectives

After studying this unit, you will be able to:

- Explain the Concept of transportation
- Discuss the Characteristics of transportation
- Describe the Modes of Transportation
- Explain the Intermodal Transportation
- Discuss the Significance of transportation services

Introduction

When the goods or the products are ready after labelling, pricing, packing, packaging, etc. then these goods are sent to the transport company, which helps in supplying it to the customer through land, air or sea transportation. Thus, transportation of goods or logistics is a key part of the Supply Chain Management.

Life in communities has changed over the years. One of those changes is in transportation. Transportation is a way of moving people or things from one place to another. The importance of international transportation as a fundamental element supporting the global economy is promoted by the growth of the amount of freight being traded as well as a great variety of origins and destinations. Economic development in the whole world has been the dominant factor behind the growth of international transportation in recent years. Transportation is the operational area of the supply chain that geographically positions the inventory. Network structure is established by facility selection. It creates the framework of transportation requirements and simultaneously limits the alternatives available.

Transportation requirements can be accomplished in three basic ways:

- By a private fleet of equipment
- Contracts with transport specialists
- Engage the services of carriers on individual shipment basis.

From the viewpoint of supply chain, three factors related to performance are fundamental to the selection of the mode of transportation: speed, cost and consistency.

Speed of transportation is the time required to complete a specific movement. Speed and cost of transportation are related in two ways:

1. Transport firms capable of providing faster service, typically charge higher rates; and
2. The faster the transportation service, the shorter the time interval during which inventory is in transit and is unavailable.

Thus, a critical aspect of selecting the most desirable method of transportation is to balance speed and cost of service.

Consistency of transportation refers to variations in time required to perform a specific movement over a number of shipments. Consistency is a reflection of the dependability of transportation. If transportation lacks consistency, inventory safety stocks will be required to protect against unpredictable service breakdowns. The quality of transportation performance is critical to time-sensitive operations. Speed and consistency combine to create the quality aspect of transportation.

In the design of a logistical system, a delicate balance must be maintained between transportation cost and quality of service. The cost of transport is the payment for movement between two geographical locations and expenses related to administration and maintaining in-transit inventory. Logistical systems should be designed to utilize transportation that minimizes total system cost.

Transportation cost, which is one of the major logistical costs, can be optimized through movement consolidation. As a general rule, the larger the overall shipment and the longer the distance it is transported, the lower the transportation cost per unit. In addition, the cost is also directly related to the product characteristics. Innovative programmes to consolidate movement by grouping small shipments through overall supply chain integration can lower transportation costs significantly.



Note Transportation creates time and place utility in goods.

The term 'transportation' is derived from the Latin *trans* ("across") and *portare* ("to carry"). In fact, the backbone of the entire supply chain is the transportation management that makes it possible to achieve the well-known seven 'R's- the right product in the right quantity and the right condition, at the right place, at the right time, for the right customer at the right cost.



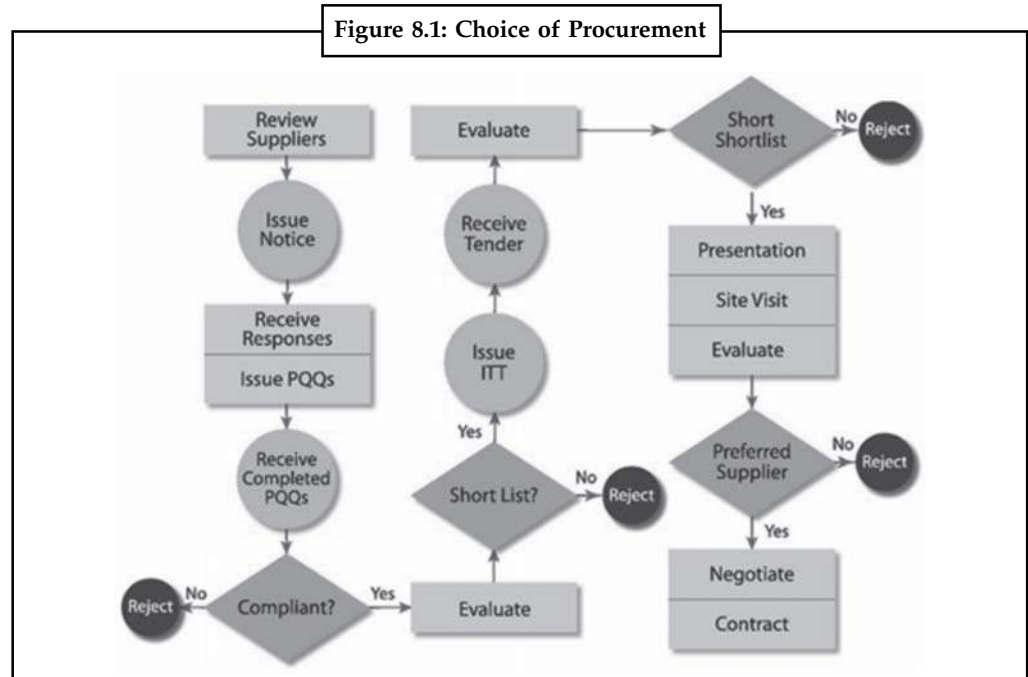
Did u know? Logistics costs are in the range of 12 to 15 percent of the GDP for a developing country while it is around 18 to 20 percent for a developed country.

8.1 Basic Terms in Relation with Transportation

Some of the basic terms used while discussing transportation are given below:

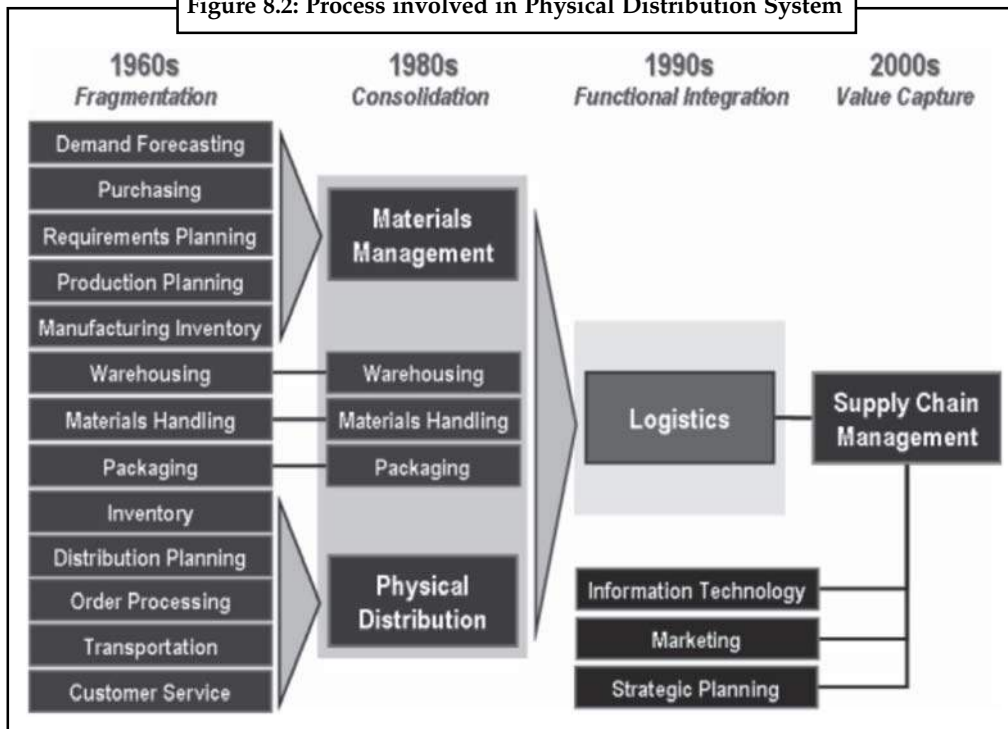
- **Procurement (Purchasing):** The inflow of materials to an organisation is usually initiated when a procurement department sends a purchase order to a supplier. This means that the purchase department finds suitable suppliers, negotiates the terms and conditions, organises delivery, arranges insurance and payment, and does everything needed to get the materials into the organisation. It is now recognised as an important link with upstream activities.

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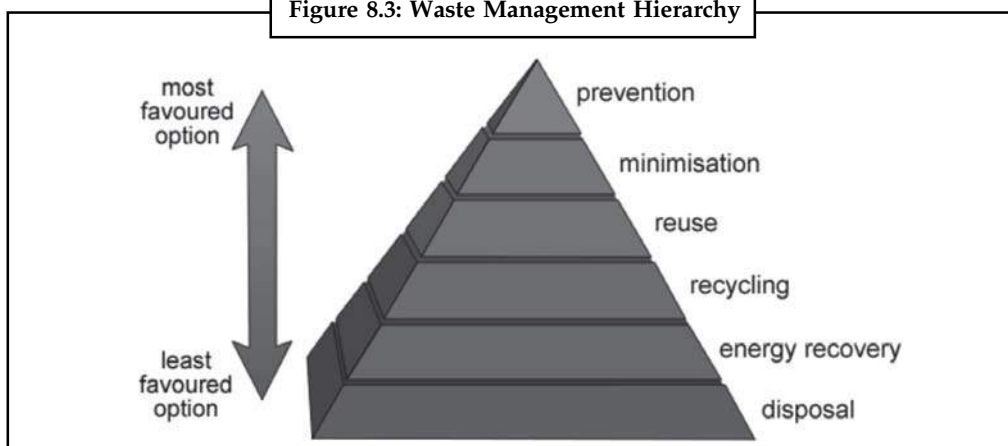
- **Inward Transport (Traffic):** This actually moves material from the suppliers to the organisation’s receiving area. This has to decide the type of transport (road, rail, air, and so on), find the best transport operator, design a route, make sure that all safety and legal requirements are met with and get deliveries on time at reasonable cost, and so on.
- **Receiving:** It makes sure that the materials delivered correspond to the order, acknowledges the receipt, unloads the delivery vehicles, inspects the materials for quality, damage and arranges them in order.
- **Warehousing (Stores):** It includes the movement of material for storage, and takes care of them until the customers utilize them. Many materials need special care, such as frozen food, drugs, alcohol in bond, chemicals that emit fumes, etc. Warehousing activity makes sure that the materials are available right on time when needed, in good condition.
- **Stock Control:** It sets the policies for inventory control. It considers the materials to store, overall investment, customer service, stock levels, order sizes, and order timing and so on.
- **Order Picking:** It finds and removes materials from the storage. Typically materials for a customer order are located, identified, checked, removed from racks, consolidated into a single load, wrapped and moved to a departure area for loading into delivery vehicles.
- **Material Handling:** It moves material through the operations within the organization. It moves materials from one operation to the next, and also moves materials picked from the stores to the point where they are needed. The aim of materials handling is to give efficient movements, with short journeys, by using appropriate equipment, with little damage and using special packaging and handling where needed.
- **Outward Transport:** It takes material from the departure area and delivers them to customers.
- **Physical Distribution Management:** It is a general term for the activities that deliver the finished goods to the customers, including outward transport. It is often aligned with marketing and forms an important link with downstream activities.

Figure 8.2: Process involved in Physical Distribution System



- Recycling Returns and Waste Disposal:** Even when the products have been delivered to the customers, the work of logistics may not be finished. There might, for example, be problems with delivered materials – perhaps they were faulty, or too many were delivered, or they were of the wrong type – and they have to be collected and brought back. Sometimes there are associated materials such as pallets, delivery boxes, cable reels and containers which are returned to the suppliers for reuse. Some materials are not reused, but are brought back for recycling, such as metals, glass, paper, plastics and oils. Activities that return materials back to an organization are called reverse logistics or reverse distribution.

Figure 8.3: Waste Management Hierarchy



- Location:** Some of the logistics activities can be done in different locations. Stocks of finished goods, for example, can be held at the end of production, moved to nearby warehouses, put into stores nearer to the customers, passed on to be managed by other organizations, or a range of alternatives. Logistics has to find the best solutions for these

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activities or at least play a significant role in the decisions. It also considers related questions about the size and the number of facilities. These are important decisions that affect the overall design of the supply chain.

- **Communication:** Alongside the physical flow of materials is the associated flow of information. This links all parts of the supply chain, passing information about products, customer demand, materials to be moved, timing, stock levels, availability, problems, costs, service levels and so on.

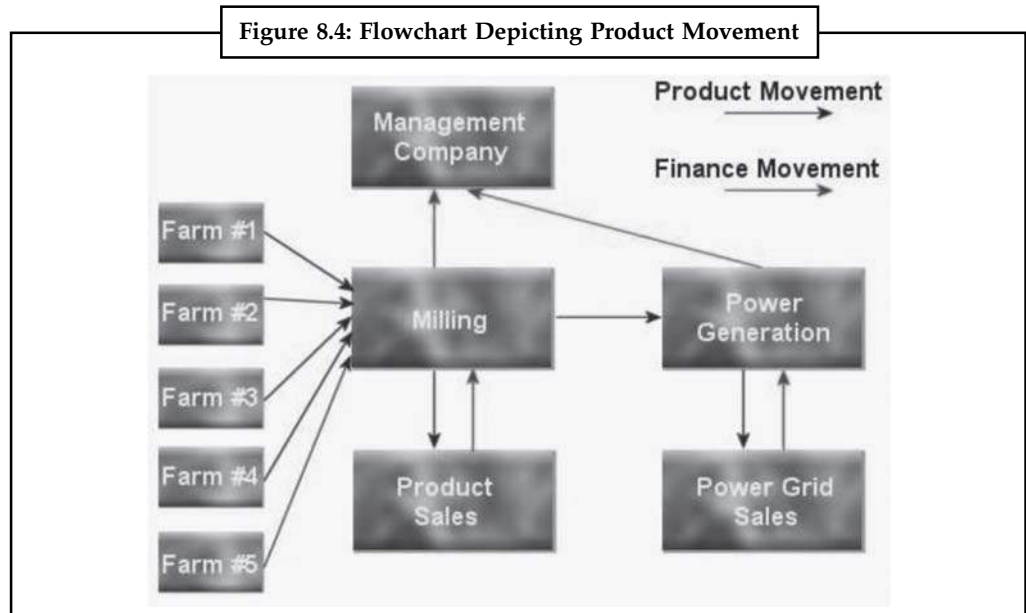
8.2 Characteristics and Relations

Following are the important basic characteristics or components or elements of any medium of transportation:

1. The points of origin and destination.
2. The route through which transportation takes place.
3. The vehicle or the carriers on which the goods or passengers are transported.
4. The kind or type of power/energy used in the vehicle.

Transportation is one of the most visible elements of logistics operations. As consumers, we are accustomed to seeing trucks and trains moving products or parked at a distribution facility. While this experience provides a good visual understanding of transportation elements, it does not allow the necessary depth of knowledge to understand transportation's role in logistics operations. This section establishes that foundation by reviewing functionality provided by transportation and the underlying principles of transport operation. Transportation functionality provides two major functions:

1. Product movement
2. Product storage
1. **Product Movement:** Whether the product is in the form of materials, components, assemblies, work-in-process, or finished goods, transportation is necessary to move it to



the next stage of the manufacturing process or physically closer to the ultimate customer. A primary transportation function is product movement up and down the value chain. Transportation utilizes temporal, financial, and environmental resources, it is important that items be moved only when it truly enhances product value.

The major objective of transportation is to move product from an origin location to a prescribed destination while minimizing temporal, financial, and environmental resource costs. Loss and damage expenses must also be minimized. At the same time, the movement must take place in a manner that meets customer demands regarding delivery performance and shipment information availability. Thus, with the help of following flowchart which is represented in Figure 8.4, you will be able to understand the movement of the product.

2. **Product Storage:** A less common transportation function is temporary storage. Vehicles make rather expensive storage facilities. However, if the in-transit product requires storage but will be moved again shortly (e.g., in a few days), the cost of unloading and reloading the product in a warehouse may exceed the profitability. A second method to achieve temporary product storage is diversion. This occurs when an original shipment destination is changed while the delivery is in transit. Traditionally, the telephone was used to direct diversion strategies. Today, satellite communication between enterprise headquarters and vehicles more efficiently handles the information.

Although product storage in transportation vehicles can be costly, it may be justified from a total-cost or performance perspective when loading or unloading costs, capacity constraints, or the ability to extend lead times are considered. In this situation, movement of goods and products has become more imperative as also wider. Raw materials of one country are processed in the other country and sold out in a third country. Hence, transportation has a significant link with various stages of supply chain.

Transportation plays a very strategic role in the success of any logistical system, because:

1. It ensures speedier and timely physical movement of goods from point of inception to point of consumption;
2. It creates core competency by preventing stock-out and customer annoyance;
3. It provides protective storage during transit;
4. It ensures cost-efficient better customer service; and
5. It fulfils specific service requirements of the corporate enterprises for improvement of logistical capabilities.

Relationships have traditionally been considered as intangible. For more than half a century, there has been a debate about the value of tangible and intangible assets to organisations. Of late, many have come to believe that intangible assets play a very important part in today's competitive environment and can be sources of competitive advantage and above normal financial returns. When we talk of intangible assets, we are principally talking of two related types of intangible assets:

1. **Relational:** Relational market-based assets are outcomes of the relationship between a firm and key external stakeholders, including distributors, retailers, end-customers, other strategic partners, community groups, and even governmental agencies; and
2. **Intellectual:** Intellectual market-based assets are the types of knowledge a firm possesses about the environment, such as the emerging and potential state of market conditions, and the entities in it such as competitors, customers, channels, suppliers and social and activist groups.

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Our discussion is limited to the former. Relational assets arise from the co-mingling of the firm with entities in its external environment, i.e. with its stakeholders. It becomes an asset only when a company plays to its social strengths in a domain where its stakeholders (customers and interested parties) are evidently active.

Relational assets have become increasingly important to organisations as one of the impacts of the internet has been to move the market and its value drivers into the desires and ambitions of the stakeholders.



Caution Organisations have become increasingly aware that they have to make relationship management work, as it is a source of competitive advantage.

This important function has, to a large extent, become the responsibility of the supply chain. The supply chain is basically a customer focused, value maximizing function of an organisation. In recent years, it has also become a strategic weapon for competitive advantage. The most difficult of all the activities supply chain managers perform now, is perhaps relationship management.

Relationship management focuses on improving operations and supply chain performance by eliciting the cooperation of other firms. Underlying the challenge is the question; how best can trust between buyer and supplier be institutionalized, especially as trust is most susceptible to break down.

Trust is developed by doing things jointly and in an aligned fashion over a period of time. There should be no major surprises. Surprises create a poor relationship. If this happens within any link of the supply chain, it can be disastrous for all other supply chain members. With the stakes so high, failure is unacceptable. This is reflected with the progressive increase in the number of companies putting an emphasis on relationship management.

In order to create an efficient and successful supply chain, organizations have to manage the relationships on all fronts – with their upstream suppliers, their internal suppliers, as well as their downstream customers. The buyer and seller, in each of these relationships, need to see each other as partners, each helping the other as much as possible.

The cooperative orientation of relationships means long-term commitment, joint work on quality, and support by the buyer of the supplier's managerial, technological, and capacity development and vice-versa. In India, it may not be easy to develop strong supply chain relationships like those found in Japan. However, in such environments, it becomes even more important to focus on these relationships.

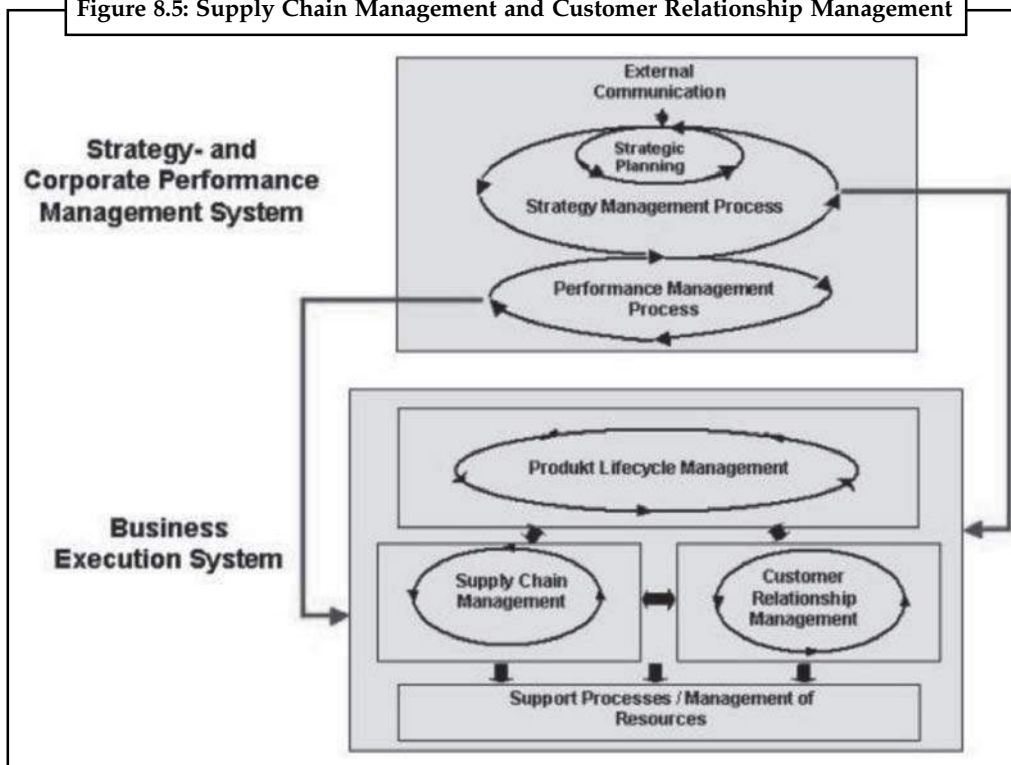
Within a firm, all supply chain activities can be related to one of three macro processes, the customer, the internal supply chain processes, and/or the supplier processes. This, in turn, can be translated into three types of 'focuses' – Customer focus, Internal Supply focus, and/or Supplier focus.

Based on the focus of the processes, the supply chain relationship management processes can be classified into the following:

1. **Customer Relationship Management (CRM):** All processes that focus on the interface between the firm and its customers
2. **Internal Supply Chain Management (ISCM):** All processes internal to the firm
3. **Supplier Relationship Management (SRM):** All processes that focus on the interface between the firm and its suppliers

The three macro processes manage the flow of information, product, and funds required to generate, receive, and fulfil a customer request.

Figure 8.5: Supply Chain Management and Customer Relationship Management



Source: Juergen H. Daum, 2001 (www.juergendaum.com)



Task Write a detailed comparative analysis on different modes of transportation.

Self Assessment

Fill in the blanks:

- is a way of moving people or things from one place to another.
- of transportation is the time required to complete a specific movement.
- of transportation refers to variations in time required to perform a specific movement over a number of shipments.
- based assets are outcomes of the relationship between a firm and key external stakeholders, including distributors, retailers, end-customers, other strategic partners, community groups, and even governmental agencies.
- market-based assets are the types of knowledge a firm possesses about the environment.
- focuses on improving operations and supply chain performance by eliciting the cooperation of other firms.
- occurs when an original shipment destination is changed while the delivery is in transit.
- Traditionally, the was used to direct diversion strategies.

- Notes**
9. Transport takes material from the departure area and delivers them to customers
 10. The faster the transportation service, the the time interval during which inventory is in transit and is unavailable.

8.3 Modes of Transportation

Transportation deals with the movement of men and materials from one place to another. Transport has a very important role to play in general development of the country and especially in its economic development. It is an integrated part of the functioning of any society. In a vast developing country like India, the goal of industrial development can only be achieved through an efficient transportation system of wide and varied nature. Through efficient transportation system, the life of the people can be enriched besides a number of distinct services, e.g. roads and road transport, railways, port, inland water transport, airways, pipe lines, ropeways and conveyors.

Transportation contributes to the economic, industrial, social and cultural development. In the production stage, transportation is required for carrying raw materials like seeds, manure, coal, steel, etc. Similarly in the distribution stage transportation helps at production centres, viz. from farms and factories to the marketing centres for distribution to the retailers and the consumers. In the absence of adequate transportation facilities, it may retard the process of socioeconomic development of the country. The adequacy of transportation system of a country indicates its economic and social development. Transportation infrastructure consists of the rights-of-way, vehicles, and carrier organizations that offer transportation services on a for-hire or internal basis. The nature of the infrastructure also determines a variety of economic and legal characteristics for each mode or multimodal system. A mode identifies the basic transportation method or form.

The five basic transportation modes are rail, road, water, air and intermodal. The relative importance of each mode can be measured in terms of system mileage, traffic volume, revenue, and the nature of traffic composition. Each mode is discussed with respect to these measures.

8.3.1 Road Transport

Most of the logistical operations of corporate enterprises largely depend on this mode of transport. It is mainly due to its moderate contribution in between two extremes of airways and seaways as far as speed and cost are concerned. It ensures flexibility in service for better customer responsiveness. The reliability and economy of this mode is gradually increasing due to continuous improvement in the quality of motor vehicles and the condition of roads. These factors facilitate in the achievement of logistical objectives like lower transit time, lower total logistical costs, and improved customer service.

Road transportation has an average operational flexibility as vehicles can serve several purposes but are rarely able to move outside roads. Road transport systems have high maintenance costs, both for the vehicles and infrastructures. They are mainly linked to industries where rapid movements of freight in small batches are required. Road Transport is an essential element in the infrastructure of all facets of economic activity. Farmers' produce, dairy products, etc. find a ready market in the urban and semi-urban area due to the availability of network of rural roads in the backward areas. It has increased movement as well as productivity and opened up the market at national and international level. Network of rural roads helped in making available basic amenities like medical facilities and primary education in rural villages.



Did u know? Highway transportation has expanded rapidly since the end of World War II. To a significant degree the rapid growth of the motor carrier industry results from door-to-door operating flexibility and speed of intercity movement.

Motor carriers have flexibility because they are able to operate on all types of roadways. In comparison to railroads, motor carriers have relatively small fixed investments in terminal facilities and operate on publicly maintained highways. Although the cost of license fees, user fees and tolls is considerable, these expenses are directly related to the number of over-the-road units and miles operated. The variable cost per mile for motor carriers is high because a separate power unit and driver are required for each trailer or combination of tandem trailers. Labour requirements are also high because of driver safety restrictions and the need for substantial dock labour. In comparison to railroads, motor carriers are best suited to handle small shipments moving short distances.

The characteristics of motor carriers favour manufacturing and distributive trades, short distances, and high-value products. Motor carriers have made significant inroads into rail traffic for medium and light manufacturing. Because of flexibility of delivery, they have captured almost all freight moving from wholesalers or warehouses to retail stores. The prospect for maintaining stable market share in highway transport remains bright.

The primary difficulties relate to increasing cost to replace equipment, maintenance, driver wages, and platform and dock wages. Although accelerating labour rates influence all modes of transport, motor carriers are more labour-intensive, which causes higher wages to be a major concern. To counteract this trend, carriers have placed considerable attention on improved line-haul scheduling that bypasses terminals, computerized billing systems, mechanized terminals, tandem operations that pull two or three trailers by a single power unit, and utilization of coordinated intermodal systems. These enhancements reduce labour intensity and, thus cost.

Specialty carriers include package haulers 'such as Federal Express (FedEx) and United Parcel Service (UPS). These firms focus on specific requirements of a market or product. Despite the aforementioned problems, it is quite apparent that highway transportation will continue to function as the backbone of logistical operations for the foreseeable future.



Task Highway transportation will continue to function as the backbone of logistical operations for the foreseeable future.

8.3.2 Rail Transport

Historically, railroads have handled the largest number of ton-miles continental. As a result of the early establishment of a comprehensive rail network connecting almost all cities and towns, railroads dominated intercity freight tonnage until after World War II. This early superiority resulted from the capability to transport large shipments economically and to offer frequent service, which gave railroads a somewhat monopolistic position. However, with the advent of serious motor carrier competition following World War II, the railroads' share of revenues and ton-miles started to decline.

The capability to efficiently transport large tonnage over long distances is the main reason railroads continue to handle significant intercity tonnage and revenue. Railroad operations incur high fixed costs because of expensive equipment, right-of-way (railroads must maintain their own track), switching yards, and terminals. However, rail experiences relatively low variable operating costs. The replacement of steam by diesel power reduced the railroads'

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variable cost per ton-mile, and electrification offers potential for more reductions. New labour agreements have reduced workforce requirements, further decreasing variable costs.

Railways are composed of a traced path on which the vehicles are bound to run. Historically, railways had accounted for the largest percentage of freight cargo in most of the countries. The major advantage of railways is to efficiently transport large quantities of goods over long distances. Given the high fixed cost and low variable cost of operation, the tariff of railways is low, which encourages large shipments over a longer distance. That is why the bulk shipment of products like fertilizer, cement, food grains, petroleum products, etc. are normally through railways from the production plant to the bulk/central warehouses.

Railways have an average level of physical constraints linked to the types of locomotives and affected by the gradient. Heavy industries are traditionally linked with rail transport systems. Containerization has improved the flexibility of rail transportation by linking it with road and maritime modes. Rising competition with other modes of transport have forced the railways system over the world to be more competitive in its services, viz. speed, handling, freight and improvement of overall efficiency.

Freight is one of the principal determinants of choice of the modes of transportation. The Principle of freight fixation is generally the same the world over. Transportation is a field of a number of national and international activities from village to district towns, from district towns to state and provincial towns, from state towns to national towns and from national towns to international towns. The means of transportation in above exercise vary from pedestrian traffic to animal-drawn transport and finally to jumbo jet aircraft. In between these two extreme modes of transport intermediaries such as cycles, rickshaws, auto rickshaws, scooters and motor cycles, cars, jeeps, buses and rails finally leading to international travels by air or sea. The transport industry, which undertakes nothing more than mere movement of persons and things from one place to another has, constitutes one of the most important activities of men in every stage of advanced civilisation. The whole structure of industry and commerce rests on well-laid foundation of transport. No region or country can ever flourish if it lacks adequate transport facilities.

Amongst the different modes of transport, railways take the uppermost place on account of the fact that in India it carries the largest bulk (90% of passenger and goods traffic). The outlay on railways during the first five-year plan was ₹423 crore. During the 2nd and 3rd plans the outlay was ₹1044 crore and ₹1686 crore respectively. The fourth and fifth five year plans provided for expenditures of ₹1575 crore and ₹ 2350 crore respectively. These amounts are quite substantial and form bulk of the plan outlays on transport.

Railways have brought about many political, social and economic changes in the life of Indian people:

1. Railways have united the people of different castes, religious customs and traditions.
2. Mobility of people has increased, thereby the congested areas can be relieved by congestion and sparsely populated areas can be developed.
3. Mobility of labour has contributed to industrial development.
4. Speedy distribution of finished product is achieved through railways.
5. Railways provide employment to millions of people.
6. The role of railways during emergencies in mobilising troops and war equipment has been very significant.
7. Railways have helped in the mass migration of the population.
8. Railways helped in cost saving in transportation of long haul bulk traffic.

Permanent Way

Notes

The Permanent way is the combination of rails, sleepers, ballast and sub-grade. A permanent way should serve the following requirements:

1. Rail level should be same for both rail lines.
2. Proper curves should be given.
3. Proper super elevation should be provided.
4. Track should be elastic. This will reduce the impact factor.
5. Joints should be given due importance. Joints should be designed carefully.
6. The design of points and crossings should be proper and safe.
7. Drainage facilities should be adequate.
8. Repairs and renewals should not present any problem.
9. Rails, sleepers, ballast, fixture and fastening should be carefully designed.
10. Track resistance should be as low as possible.
11. The track structure should have a good strength and should have a low construction and maintenance cost.
12. The gradient should be uniform and as gentle. Any change of gradient should be followed by a smooth vertical curve, to give smooth riding quality.
13. The rails, fittings, sleepers, ballast and formations must fully satisfy the requirements for which they have been provided.
14. The track should not allow the creep to develop.

Gauges in Railway Tracks

The gauge on Indian Railways is the perpendicular distance between inner faces of the rail. In countries abroad, it is taken as the distance between the inner faces of the rails at a certain vertical distance from the top of the rail table.

The gauge of the railway track is defined as the clear distance between inner or running faces of two track rails. The distance between the inner faces of pair of wheels is called the "wheel gauge". In India, the following gauges are used:

Table 8.1: Type of Gauge and Gauge Width

Type of Gauge	Gauge Width
1. Standard Gauge (B.G.)	1.67m
2. Meter Gauge (M.G.)	1.00m
3. Narrow Gauge (N.G.)	0.762 m
4. Feeder Track gauge (L.G.) (Or Light gauge)	0.610 m

Coning of Wheels

If the distance between the inside edge of the flanges of the wheel is kept equal to the gauge distance then the flanges of the wheel would rub against the inside face of the rail. To prevent this the distance between the inside edge of the flanges is kept less than the gauge distance.

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So there is gap between the wheel flanges and running edges of the rails, nearly equal to 1 cm. (3/8") on either side. Normally, the tread of wheels is absolutely dead centre of the head of the rail, as the wheel is coned to keep it in this position automatically. These wheels are coned at a slope of 1 in 20.

The advantages of coning of wheels are:

1. Tilting of rail results in uniform wear of the head of the rail.
2. Proper gauge is maintained.
3. Life of sleeper and rail is increased.

Disadvantages of coning of wheels are:

1. The horizontal thrust tends to turn the rail outwardly. Sometimes, this results in the increase in the gauge distance.
2. Sleepers under the outer edge of the rail are likely to get damaged. This effect is reduced either by having 'ADZING' of sleepers or by providing inclined base plate. According to American Practice, reducing the slope from 1 in 20 to 1 in 40 reduces the wear on rails.

8.3.3 Maritime Transport

Seaways/waterways are the oldest mode of transport. When goods are transported through the water medium by a ship, it is called seaways transportation. Due to globalization of the world market, seaways have a large potential for foreign trade. Throughout the world, this mode has acquired a very high position due to its advantages like being the cheapest, having a larger capacity and flexibility. But, the greatest drawback of it lies in terms of slow speed.

The main advantage of water transportation is the capacity to move extremely large shipments. Water transport employs two types of vessels. Deep-water vessels, which are generally designed for ocean and great lakes use, are restricted to deep-water ports for access. In contrast, diesel-towed barges, which generally operate on rivers and canals, have considerably more flexibility.

Water transport ranks between rail and motor carrier in respect to fixed cost. Although water carriers must develop and operate their own terminals, the right-of-way is developed and maintained by the government and results in moderate fixed costs compared to rail and highway. The main disadvantages of water transport are the limited range of operation and speed. Unless the origin and destination of the movement are adjacent to a waterway, supplemental haul by rail or truck is required. The capability of water to carry large tonnage at low variable cost places this mode of transport in demand when low freight rates are desired and speed of transit is a secondary consideration.

Typical inland water freight includes mining and basic bulk commodities such as chemicals, cement, and selected agricultural products. In addition to the restrictions of navigable waterways, terminal facilities for bulk and dry cargo storage and load-unload devices limit the flexibility of water transport. Labour restrictions on loading and unloading at docks create operational problems and tend to reduce the potential range of available traffic. Finally, a highly competitive situation has developed between railroads and inland water carriers in areas where parallel routes exist.

Main maritime routes are composed of oceans, coasts, seas, lakes, rivers and channels. But, maritime circulation takes place on specific parts of the maritime space. The Atlantic Ocean is very important since it accounts for 78% of the global trade, 68% of its value and 75% of the maritime trade. The construction of channels and dredging operations are the attempts to facilitate maritime circulation by reducing discontinuity. Water transportation is generally divided into inland waterways (rivers, canals, lakes); domestic coastways and seaways. Water transport is generally used for high bulk,

low value commodities because of low cost per tonne per kilometre, which is of greater importance than speed of delivery. Basic bulk commodities and raw materials such as iron ore, coal, chemicals, petroleum products, cement etc are extensively transported by this mode.

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8.3.4 Air Transport

When goods are transported by air, the mode of transport is called airways. This mode of transport is the newest and least preferred mode, especially for domestic purposes. One of the significant advantages of the air transportation lies in the speed. It needs only a few hours for a shipment from one place to reach another, in contrast to the days required with any other modes. That is why; it is a most preferred mode of transport for perishable goods like flowers or for emergency services like supply of a spare part during the breakdown of a machine. In the present day's considerable international trade and growing awareness about logistical services, the growth of this mode is gradually increasing.

A coast-to-coast shipment via air requires only a few hours contrasted to days with other modes of transportation. One prohibitive aspect of air transport is the high cost. However, this can be traded off for high speed, which allows other elements of logistical design, such as warehousing or inventory, to be reduced or eliminated.

Air transport still remains more of a potential opportunity than a reality. Although the mileage is almost unlimited, airfreight accounts for significantly less than 1 percent of all intercity ton-miles. Air transport capability is limited by lift capacity (i.e., load size constraints) and aircraft availability. Traditionally, most intercity airfreight utilized scheduled passenger flights. While this practice was economical, it resulted in a reduction of both capacity and flexibility. The high cost of jet aircraft, coupled with the erratic nature of freight demand, has limited the assignment of dedicated planes to all-freight operations.

However, premium air carriers such as Federal Express and United Parcel Service Overnight provide dedicated global freight operation. While this premium service was originally targeted at documents. It has expanded to include larger parcels. For example, both United Parcel and Federal Express have extended their air freight service to include overnight delivery from a centralized distribution centre located at their air hub. This is an ideal service for firms with a large number of high-value products and time-sensitive service requirements.

The fixed cost of air transport is low compared to rail, water, and pipeline. In fact, air transport ranks second only to highways with respect to low fixed cost. Airways and airports are generally developed and maintained with public funds. Likewise, terminals are normally maintained by local communities. The fixed costs of airfreight are associated with aircraft purchase and the requirement for specialized handling systems and cargo containers. On the other hand, air freight variable cost is extremely high as a result of fuel, maintenance, and the labour intensity of both in-flight and ground crews.

Air routes are practically unlimited. Air transport constraints are multidimensional and include the site (Runway for landing and take off), the climate, etc. Air freight is used whenever the benefits of fast delivery are more than the increased transportation cost.

8.4 Intermodal Transportation

Intermodal transport (or intermodal transportation) involves the use of more than one mode of transport for a journey. Intermodal transport can be of two types:

1. Intermodal passenger transport
2. Intermodal freight transport

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Intermodal passenger transport involves more than one mode of transport of passengers. Some modes of transportation have always been intermodal. A major goal of modern intermodal passenger transport, at least in developed countries, is to reduce dependence on the automobile as the major mode of ground transportation and increase use of public transport. Intermodal freight transport involves the transportation of freight in an intermodal container or vehicle, using multiple modes of transportation (rail, ship, and truck), without any handling of the freight itself when changing modes. The method reduces cargo handling, and so improves security, reduces damage and loss, and allows freight to be transported faster. The modes of transport which can be used for the movement of:

1. *Passengers, Livestock and Goods are:*

- (a) *Rail:* Rail transportation is typically used for long-distances. Though it is less expensive than air transportation, it also takes more time to reach a destination. Transport by rail has been a major factor in allowing the centralization of the industry and in opening new markets. Also, Rail transport is ideal for heavy goods and has a wide range of applications.
- (b) *Road:* This is the most widely used means of transportation for passengers and is generally used in case of intercity travelling. In case of livestock, herding by road was the only form of transport available in the not-too-distant past, and it is still the main method of moving cattle on the farm, and often from farm to farm. Also in case of transportation of goods it is the most commonly used method in practice today. The numbers are getting smaller as more and more companies export but it is still the most used mode of transport by a wide margin.
- (c) *Air:* Air transportation offers the advantage of speed to passengers and is to be used for long-distance transport. For livestock air usually costs more than by sea. However, air transportation is fast. Also, because shipping by air is fast, animals may not have to endure as much stress as when travelling by sea. Similarly for goods air freighting is commonly used by companies who work with short lead times, or advanced service levels. Shipping by air certainly isn't the cheapest alternative, and is only advisable for certain size/weighted products.
- (d) *Water:* Shipping by sea opens up some areas that do not have airports with animal handling facilities, and the cost per head is usually lower. Ships also can handle larger numbers of animals than aircraft. However, sea transportation is relatively slow; and requires additional expenses for food, water, bedding and medical supplies. For Goods sea transportation is usually used by companies who ship a large amount of goods at once, with longer lead times. This mode of transport is the longest, yet is ideal for bulk shipments such as coal and minerals.



Task Study the transportation modes of a particular company of your choice.

8.5 Significance of Transportation Services

Transportation is a non-separable part of any society. It exhibits a very close relation to the style of life, the range and location of activities and the goods and services which will be available for consumption. Advances in transportation has made possible changes in the way of living and the way in which societies are organised and therefore have a great influence in the development of civilisations. This unit conveys an understanding of the importance of transportation in the modern society by presenting selected characteristics of existing transportation systems, their use and relationships to other human activities.

Transportation is responsible for the development of civilisations from very old times by meeting travel requirement of people and transport requirement of goods. Such movement has changed the way people live and travel. In developed and developing nations, a large fraction of people travel daily for work, shopping and social reasons. But transport also consumes a lot of resources like time, fuel, materials and land.

8.5.1 Economic Role of Transportation

Economics involves production, distribution and consumption of goods and services. People depend upon the natural resources to satisfy the needs of life but due to non-uniform surface of earth and due to difference in local resources, there is a lot of difference in standard of living in different societies. So there is an immense requirement of transport of resources from one particular society to other. These resources can range from material things to knowledge and skills like movement of doctors and technicians to the places where there is need of them.

Place, Time, Quality and Utility of Goods

An example is given to evaluate the relationship between place, time and cost of a particular commodity. If a commodity is produced at point A and wanted by people of another community at any point B, distant x from A; then the price of the commodity is dependent on the distance between two centres and the system of transportation between two points. With improved system, the commodity will be made less costly at B.

Changes in Location of Activities

The reduction of cost of transport does not have the same effect on all locations. Let at any point B, the commodity is to be consumed. This product is supplied by two stations A and K which are at two different distances from B. Let at present the commodity is supplied by A since it is at a lesser distance but afterwards due to improvement in road network between B and K, the point K becomes the supply point of product.

8.5.2 Social Role of Transportation

Transportation has always played an important role in influencing the formation of urban societies. Although other facilities like availability of food and water played a major role, the contribution of transportation can be seen clearly from the formation, size and pattern, and the development of societies, especially urban centres.

Formation of Settlements

From the beginning of civilization, the man is living in settlements which existed near banks of major river junctions, a port or an intersection of trade routes. Cities like New York, Mumbai and Moscow are good examples.

Size and Pattern of Settlements

The initial settlements were relatively small developments but with due course of time, they grew in population and developed into big cities and major trade centres. The size of settlements is not only limited by the size of the area by which the settlement can obtain food and other necessities, but also by considerations of personal travels especially the journey to and from work. The increased speed of transport and reduction in the cost of transport has resulted in variety of spatial patterns.

Notes

Growth of Urban Centres

When the cities grow beyond normal walking distance, then transportation technology plays a role in the formation of the city. For example, many cities in the plains developed as a circular city with radial routes, whereas the cities beside a river developed linearly. The development of automobiles and other factors like increase in personal income, and construction of paved road network, the settlements were transformed into urban centres of intense travel activity.

8.5.3 Political Role of Transportation

The world is divided into numerous political units which are formed for mutual protection, economic advantages and development of common culture. Transportation plays an important role in the functioning of such political units.

Administration of an Area

The government of an area must be able to send/get information to/about its people. It may include laws to be followed, security and other needful information needed to generate awareness. An efficient administration of a country largely depends on how effectively government could communicate this information to all the country. However, with the advent of communications, its importance is slightly reduced.

Political Choices in Transport

These choices may be classified as communication, military movement, travel of persons and movement of freight. The primary function of transportation is the transfer of messages and information. It is also needed for rapid movement of troops in case of emergency and finally movement of persons and goods. The political decision of construction and maintenance of roads has resulted in the development of transportation system.

A message proceeds along a channel from the source to the receiver; information theory defines for any given channel a limiting capacity or rate at which it can carry information, expressed in bits per second. In general, it is necessary to process, or encodes, information from a source before transmitting it through a given channel. For example, a human voice must be encoded before it can be transmitted by telephone.



Caution An important theorem of information theory states that if a source with given entropy feeds information to a channel with a given capacity, and if the source entropy is less than the channel capacity, a code exists for which the frequency of errors may be reduced as low as desired. If the channel capacity is less than the source entropy, no such code exists.

Self Assessment

Fill in the blanks:

11. The gauge on Indian Railways is the distance between inner faces of the rail.
12. are the oldest mode of transport.
13. The main advantage of transportation is the capacity to move extremely large shipments

14. passenger transport involves more than one mode of transport of passengers.
15. Critical aspect of selecting the most desirable method of transportation is to balance speed and

Notes

8.6 Summary

- Transportation is a non-separable part of any society.
- It exhibits a very close relation to the style of life, the range and location of activities and the goods and services which will be available for consumption.
- Given a facility network and information capability, transportation is the operational area of logistics that geographically positions inventory. Because of its fundamental importance and visible cost, transportation has received considerable of managerial attention over the years. Almost all enterprises, big and small, have managers responsible for transportation.
- Transportation requirements can be accomplished in three basic ways. First of all, a private fleet of equipment may be operated. Second, contracts may be arranged with transport specialists. Third, an enterprise may engage the services of a wide variety of carriers that provide different transportation services on an individual shipment basis. These three forms of transport are typically referred to as private, contract and common carriage. From the logistical system viewpoint, three factors are fundamental to transportation performance: cost, speed and consistency.
- The cost of transport is the payment for movement between two geographical locations and expenses related to administration and maintaining in-transit inventory.
- Logistical systems should be designed to utilize transportation that minimizes total system cost. This means that the least expensive transportation does not always result in the lowest total cost of movement.

8.7 Keywords

Air Transport: When goods are transported by air, the mode of transport is called airways.

Facility: An installation, contrivance, or other things which facilitates something.

Intermodal Transport: Intermodal transport (or intermodal transportation) involves the use of more than one mode of transport for a journey

Logistics: Logistics is the management of the flow of resources, between the point of origin and the point of destination in order to meet the requirements of customers or corporations.

Procurement: Procurement is the acquisition of goods or services.

Seaways Transport: When goods are transported through the water medium by a ship, it is called seaways transportation.

Transportation: Transport or transportation is the movement of people, animals and goods from one location to another.

8.8 Review Questions

1. Briefly explain the concept of international transport system.
2. What are the basic terms involved in the study of transportation?

Notes

3. Describe the political role of transport.
4. Discuss the importance of intermodal transportation.
5. Throw light on the economic effects of transportation.

Answers: Self Assessment

1. Transportation
2. Speed
3. Consistency
4. Relational market
5. Intellectual
6. Relationship management
7. Diversion
8. telephone
9. Outward
10. Shorter
11. perpendicular
12. Seaways/waterways
13. water
14. Intermodal
15. cost of service

8.9 Further Readings



Books

Agrawal D K, *Textbook of Logistics and Supply Chain Management*, MacMillan India Limited, 2003.

Ailawadi C Sathish and Rakesh Singh, *Logistics Management*, Prentice Hall India, 2005.

Reji Ismail, *Logistics Management*, Excel Books, Delhi.



Online links

www.fhwa.dot.gov/.../int_ppp_case_studies_final_report_7-7-07.pdf

www.internationaltransportforum.org/Proceedings/.../09Lee1.pdf

www.worldbank.org/transport/roads/rdt_docs/annex8.pdf



Case Study

Atkins Transport Systems

Atkins Transport Systems (ATS) is a world leader in highway engineering with the total capability to deliver all the processes involved in the planning, design and construction of highways and highway structures. Its procurement experience includes framework consultant delivering design and project management services, the variations of early contractor involvement and Design, Build, Finance and Operation (DBFO) contracts, as well as advisory roles and equity participation in Private Finance Initiatives (PFI) and Public Private Partnerships (PPP). ATS designs intelligent transport systems to solve the most complex urban transport problems. Its expertise covers the full range of highways systems, travel information systems, vehicle telematics, and urban traffic management and control systems.

The Challenge

The Highways Agency (HA) maintains, operates and improves the network of trunk roads and motorways in England. Recent policy decisions have resulted in the on-going transformation of the control of the network from the 30 Police Control Offices (PCOs) to a regime of 7 Regional Control Centres (RCCs). This change is accompanied by the transfer of the majority of operational responsibilities from the Police to the staff of the highways Agency. A major consequence of this national programme is the need to merge a large number of systems and associated data stores, together with the introduction of new systems.

The Solution

In order to achieve the aims of this programme the HA appointed a consortium of consultants, with the requisite skills and experience, to work closely with the Highways Agency staff, stakeholders and other consultancies in a partnership capacity.

The consortium, known as TANDEM, is responsible for the technology aspects of the overall programme and is led by Atkins Transport Systems and supported by IPL, Cambridge Consultants and Hyder Consulting.

The objective of TANDEM is to ensure that the integration of existing systems and the introduction of new systems is effectively planned and executed.

IPL has played an important role in the overall project, including:

- provision of technical advice/reports on subjects such as Requirements Traceability and Resilience/Risk
- technical support for the design, documentation, planning, data configurations, change control, and testing of the Highways Agency Traffic Management Systems (HATMS) technology
- technical support on the new Command and Control system.

The Highlights

The Highways Agency's road network provides a vital service to commerce and industry and has a huge impact on the lives of individuals and communities.

The RCCs will eventually control 2750 km of motorway in England (approx 1800 miles), with more than 151 billion vehicle kilometres of journeys taking place on the network every year.

Contd...

Notes

The success of this contract has recently been evidenced by the first RCC going live in April 2005 only one year after the appointment of TANDEM. IPL has several consultants with long term specialist knowledge in the road transport sector whose expertise continues to be made available to assist the Highways Agency and their partners at both a strategic and at a tactical technical level.

About IPL

Founded in 1979, IPL has a long history of successfully delivering excellent value consultancy and end-to-end solutions to both the public and private sectors. IPL's consultancy is renowned for its quality and value. Our consultants are talented and independent-minded individuals with extensive industry experience. We consistently exceed our clients' expectations through a combination of imaginative thinking, managerial and technical expertise and many years of systems engineering experience. IPL's track record in end-to-end solutions development is exceptional. Our proven development methodology allows us to cut through technical complexity, manage risk and completely focus on delivery. We consistently deliver reliable, efficient and accurate systems to a precise schedule. IPL is an ISO9001:2000/TickIT registered company having a permanent workforce of 245, revenues of ca. £22M p.a. and 40,000 sq ft of secure office space in central Bath.

Questions:

Summarise the case and write the case facts.

Unit 9: Characteristics of Shipping Industries

Notes

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- 9.1 History of Shipping Industry
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- 9.3 Different Modes of Shipment
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- 9.5 The Best Method
- 9.6 Conference System & Practices
- 9.7 Ocean Freight Rate Structure
- 9.8 Chartering Practices
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- 9.10 Role of intermediaries in Shipping Industry
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Objectives

After studying this unit, you will be able to:

- Discuss the History of shipping industry
- Explain Role of shipping intermediaries
- Describe Ocean freight structure
- Discuss the Latest trends in logistics operations

Introduction

Shipping plays an important role in the Indian economy with around 95 per cent of the country's trade by volume and 68 per cent in terms of value being transported by sea. As on 1 January 2012, India had a fleet strength of 1,122 ships with Gross Tonnage (GT) of 11.06 million, the public-sector Shipping Corporation of India having the largest share of 36.17 per cent. Of this, 372 ships with 10.01 million GT cater to India's overseas trade and the rest to coastal trade.

The gross foreign exchange earnings/savings of Indian ships in 2010-11 were 10,666.45 crore. The country with the highest Dead Weight Tonnage (DWT) is Hong Kong. Though India has one of the largest merchant shipping fleets among developing countries, it is ranked eighteenth in the world in terms of DWT with a share of only 1.09 per cent as on 1 January 2011. In comparison, China is ranked ninth with a share of 3.78 per cent.

9.1 History of Shipping Industry

The Indian shipping Industry plays a crucial role in Indian economy. As 90% of the Nations trade by volume is done via sea. India has been the largest merchant shipping fleet among the developing nations. The Indian Shipping Industry supports transportation of national and international cargoes and also provides various other facilities such as ship building, ship repairing, lighthouse facilities, freight forwarding, etc. Indian Shipping Industry with emergence of globalisation and liberalisation is firmly ready to acquire new dimensions in terms of demand and infrastructural development.

In order to sustain itself with the stiff competition posed by foreign companies, the Indian industry is striving hard to bring about rapid transformation. Over the years the way cargo traffic was handled has changed. Initially, it was by the protected environment by the tonnage committee who decided as to what type and size of ships the companies should be given a chance. Government subsidy vessels were only assured for the Cargo was assured. Recently after a long period of decline, both tonnage and fleet size have grown, with the addition of ships – tugs, survey vessels, towing vessels as well as pilot vessels belonging to ports and maritime boards. During April 2002 and March 2003 these were added. There are as many as 55 shipping companies in the Industry, out of which 19 deal with coastal trade and 29 are engaged in overseas trade. The rest operate in both types of trade.

The Indian Shipping industry is governed by 3 separate Acts such as The Merchant Shipping Act in 1958, The Inland Vessels Act in 1917 and The Coasting Vessels Act in 1838. Most of the vessels are registered under Merchant Shipping Act and are dealt within the sector, smaller barges and coastal vessels are governed by the other two Acts.

Historically Shipping industry has catered to only domestic shipping requirements, while the private sector companies like Great Eastern Shipping Company and Essar Shipping are increasingly getting involved in international cross trade.

Terms and in value terms, it is much lower to a meager 12% of India's total overseas shipping bill of USD 5.0 billion. It is due to the negligible share of shipowners in the Indian trade of high value goods like general cargo and containers. The focus is on Indian trade and shipowners' share in the country's overseas trade is hardly 30% in volume.

Shipping Industry is meaning not only just vessels and tonnage. Shipping capabilities of any country are not solely measured in terms of the quantum of tonnage under control. While in knowledge based economy, soft intangible parameters like human capital, information technology and expertise are becoming increasingly important for increasing innumerable opportunities. Today India has become the source of quality seafarers to global shipowners. Indian shipping firms normally rely on the inherent IT skills of Indians to play a pivotal role in IT activity involved in international shipping and the country can come up with a business center for information processing requirements of the international ship owners.

Usage of sea transport for the bulk cargo transport is the natural advantage of a vast coastline of India. Due to the policy of liberalization, the Indian shipping industry, major ports, as road ways have been given to the private sector. The categories of ships are crude tanker, product tanker, bulk carriers, etc. All these are brought under the Open General License (OGL) to facilitate acquisition at competitive price.

For acquisition of such companies the Automatic approval is also available even for the categories which are not covered under OGL, i.e. barges, tugs and boats, etc. Shipping companies have been given liberty to retain sale proceeds of their ships abroad and utilize them for fresh acquisition.

Approval for Foreign direct investment up to 74% is also provided by the Time Charter of ships by Indian Shipping Companies. 140 shipping companies were in operation in India at the end of March 2003, with the Shipping Corporation of India being the biggest in the country claiming a 42% share of the total Indian tonnage. The country presently has 12 major ports, 184 other ports, nine shipyards and a coastline of 7517 km.

Size

Indian shipping Industry has become the 14th largest fleet in the world as per deadweight tonnage. The shipping fleet of India consists of around 515 vessels with a GRT of 7.06 million and DWT of 11.5 million ones. It has about 616 ships, with a total capacity of 6.62 million tons Gross Registered Tonnage (GRT). Out of which about 258 ships are engaged in overseas trade and the rest ply inland routes.

Total Contribution to the Economy/Sales

When compared to World Shipping Tonnage the share of Indian Shipping Tonnage as in term of tonnage (GT) by Flag of Registration stood at 1.19% on 1.1.2006, 1.1.2007 at 1.16% and 1.18% on 1.1.2008 as per data available.

9.2 Characteristics of Shipping Industry

Around 90% of world trade is carried by the international shipping industry. Without shipping the import and export of goods on the scale necessary for the modern world would not be possible.

Seaborne trade continues to expand, bringing benefits for consumers across the world through competitive freight costs. Thanks to the growing efficiency of shipping as a mode of transport and increased economic liberalisation, the prospects for the industry's further growth continue to be strong.

There are around 50,000 merchant ships trading internationally, transporting every kind of cargo. The world fleet is registered in over 150 nations, and manned by over a million seafarers of virtually every nationality.

India's freight transport system carries approximately 1000 billion ton-kilometres; the modal share being, road 60-65%, rail 30-32% and coastal shipping 6-7%. The modal share of coastal shipping in European Union is more than 40%. With Indian economy growing at 6-7%, the freight transport demand is likely to grow to 2000 billion tonne-km in next 8-10 years. As such, there is a need for integrated transport planning accompanied by modal shifts in favour of cost efficient mode such as coastal shipping. The need for modal shift arises mainly from the environmental concerns and the need to alleviate congestion, not to mention the economic return. Lack of integrated approach will only add to chaos on the road and rail, besides further distorting the modal mix.



Did u know? The total volume of the traffic handled by all the Indian ports during 2004-05 was 521.58 million tonnes, of which 383.75 million tonnes i.e. around 74 percent was handled by Major Ports and remaining 137.83 million tonnes by the non-major ports.

9.3 Different Modes of Shipment

Table 9.1: Three Types of Shipping Method

1. Door to door courier	International courier service providers deliver the goods at the customers door step. For this the buyer can create an account with them on there own or they can use the Seller account.	
	Freight Charges:	
	Best Suit for:	Small Shipments (up to 90 kg)
	Goods travel time:	Within 4 to 5 working days (Courier)
2. At senders nearest Airport	Shipping can be organized through various airlines. The goods has to be picked by sender only from their nearest airport and they themselves has to handle the custom procedures.	
	Freight Charges:	The freight charges are subjected to the airlines itself and they changes it depending on the petrol prices and the space available with them on that particular day.
	Best Suit for:	Medium Sized Shipments (90 kg to 250 kg)
	Goods travel time:	Within 5 to 9 working days (Air line carriers)
3. At senders nearest Sea Port	Shipping can be organized through various shipping companies. The goods has to be picked by them only from their nearest Seaport and they themselves has to handle the custom procedures.	
	Freight Charges:	The freight charges are subjected to the airlines itself and they changes it depending on the petrol prices and the space available with them on that particular day.
	Best Suit for:	Big Sized Shipments (more than 250 kg)
	Goods travel time:	Within 20 to 30 working days (Shipping carriers)

9.3.1 Modes of Shipping based on Medium

Air transport: This method is by far the fastest and much safer, unless you are offering some electronic product or service online which can be downloaded in real time. Despite of being safe and fast, suppliers (specially the small ones) are often reluctant to use this mode, mainly because of high cost associated with it. This should be helpful when delivering some valuable goods or when a quick delivery is needed.

Water Transport: Most probably the oldest method used in trade for overseas supplies. In ancient times traders travelled by means of water, carrying several goods and products to sell in foreign countries. Inexpensive but relatively slow, certainly not a good choice when quick delivery is needed. However, when the time is not an issue and shipment is quite large, maritime transportation becomes an automatic choice.

Road Transport: This is the most widely used method, especially in domestic trade. Even when air or water transport is the prime source of shipment, road transportation is still needed to carry the goods from the ports to the buyer. Although limited to domestic trade, this method is both time saving and cost effective.

Additional Methods: There are some other rarely used methods like rail cars, or a combination of two or more of these. Another form of shipment rising out of the internet growth is electronic shipment which takes place on the internet in no time after the customer has made the payment.

9.4 Selecting Suitable Mode for Shipment of Cargo and Capacity

Notes

Measurement

Different methods have different positives and negatives. Some are safer, some really fast and others have a plus point of being inexpensive.

In order to supply their products to the customers, wholesalers and trade suppliers have to choose among various shipment methods. Depending on the following important characteristics/factors the sender may select any one or multiple modes. They normally consider some factors before settling on the shipping mode. These factors are:

1. Business Size
2. Cost
3. Safety
4. Delivery Time
5. Frequency of Delivery, Goods to be delivered, once, occasionally, or regularly.

A shipment method will be evaluated by following characteristics.

1. Speed
2. Cost
3. Safety
4. Convenience

9.5 The Best Method

Each mode of freight transport has its own unique advantages. Choosing an appropriate method is heavily dependent on distance, the geographic location of the desired destination, the nature of items, seller's budget, and any necessary deadlines or schedules that must be adhered to.

Items that must be moved quickly should be shipped by air, while goods that are not needed in a hurry can be shipped inexpensively by sea. Most shipping routes often require the use of several different modes of transport. Finding the best way to coordinate this logistic chain can save any business a lot of time and money in the long run.

9.6 Conference System and Practices

A conference is an association of two or more liner shipping companies. The first conference was formed in 1875, known as UK-Calcutta Conference. The characteristics of conference shipping are:

1. **Restrict/Eliminate Competition:** They are organised to restrict/eliminate competition in trade, regulating and rationalising sailing schedules and ports of call. They operate on the basis of written agreement, defining rights and obligations of members. The members are expected to follow the rules set by the conference under agreement. In the event of violation of rules by any member, the agreement provides penalty. Penalty may be as high as the forfeiture of the amount deposited by the member.
2. **Benefits:** The basic aim is to minimise losses and maximise profits by combating competition among ship owners. There is a rate agreement in respect of the sailings between the liner ships. The sailing schedules are regulated. They can be compared to

Notes

Bhopal Local bus owners association where the local bus owners are the members of the association. They enjoy unity and work with strict discipline for their common good.

3. **Particular Trade or Geographical Area:** The conference practice is followed by the shipping lines engaged in a particular trade or operating in a specified geographical area. The competition from other shipping lines is encountered by entering into agreements with other conferences operating on alternative routes in such a way that each conference works in one route

9.7 Ocean Freight Rate Structure

The ocean transport industry provides a wide range of shipping services, which may be broadly split into two main categories: liner shipping and tramp shipping. The determination of the freight rates are different for unlike forms of shipping.

9.7.1 Liner Shipping

Liner shipping takes place in an environment which is totally different from tramp shipping. In that liner services are provided on the basis of fixed schedules and itineraries. Until recently, the liner-shipping sector was largely oligopolistic in that these services were controlled by cartels, called shipping conferences. A conference exists for each major trade route, and it is the conferences that draw up tariffs, scheduling freight rates at which goods will be transported. However, since the mid-1970s many independent carriers have entered the liner-shipping sector, and they fix their rates on the basis of 'what the traffic will bear,' essentially applying market-pricing techniques.

Two basic factors affect rate fixing in liner shipping—port and distance related factors and cargo related factors. For general cargo, liner tariff rates are assessed on cargo weight, measurement or value. Goods measuring less than 40 cu.ft. per 1,000 kg are charged on a cargo weight basis and above that measure by the measurement tariff scale. If goods are of very high value, they are charged irrespective of weight and measurement on an ad valorem basis. Under liner freight tariffs, carrier assumes responsibility for loading and discharging expenses, as well as the carriage of the goods by sea.

In container shipping, different charges are applied to 'Less-than-Container-Loads' (LCL) and 'Full-Container-Loads' (FCL). In the former case, the rates are usually the same as those charged for conventional shipments. For FCL containers, there exists the principle of Commodity Box Rates (CBR). CBR is a lump sum payable for the carriage of a container stuffed with a particular commodity. The rate is based on the average utilisation of the box, e.g. 13 tons in a twenty-foot container. As a more recent development, container carriers have introduced the 'freight-all-kinds' (FAK) principle. FAK rates are non-discriminatory by treating all commodities the same way. They are basically average cost rates; the ship owner distributes his projected total costs over the anticipated number of containers to be moved.



Caution In combined transport arrangements by one carrier under a through document, an intermodal freight rate is charged. This rate is the sum of charges in the port of loading, ocean freight rate, charges in the port of discharge, and the road or rail haulage to the final destination.

9.7.2 Conference Shipping

There are three types of conference rates, including commodity rates, class rates, and commodity-class rates. Under the first category, rates are quoted individually for several hundred

commodities; under the second category tariff specific commodities are grouped into a limited number of classes. The third category represents tariffs, which are a combination of the two others.

Despite the existence of conferences and because of the increasing role of independent carriers in the liner trades, the rates actually charged vary widely and often deviate substantially from published tariffs. Carriers offer loyalty bonuses and apply rebates in violation of conference agreements. Service contracts are gaining importance whereby individual shippers pledge a minimum amount of cargo to be shipped during a certain period in return for specially discounted rates offered by the contracted carrier.

9.7.3 Tramp Shipping

The environment in which tramp shipping takes place is close to the model of perfect competition, and pricing is fully governed by the law of supply and demand. The charter rates are quoted on a competitive basis through brokers in various exchanges throughout the world. The major elements which influence the fixing of a specific rate are:

- (a) Ship specification;
- (b) Trade and route;
- (c) General market conditions;
- (d) Terms of charter party, i.e. distribution of costs between ship owner and chartered;
- (e) Duration of charter;
- (f) Urgency of the charter; and
- (g) Convenience of the charter to the ship owner.



Task Discuss the significance of ocean freight structure.

Self Assessment

Fill in the blanks:

1. method is by far the fastest and much safer, unless you are offering some electronic product or service online which can be downloaded in real time.
2. is most probably the oldest method used in trade for overseas supplies.
3. is the most widely used method, especially in domestic trade.
4. Choosing an appropriate method is heavily dependent on, the geographic location of the desired destination, the nature of items, seller's budget,
5. A is an association of two or more liner shipping companies.
6. shipping takes place in an environment which is totally different from tramp shipping.
7. Two basic factors affect rate fixing in liner shipping- port and distance related factors and related factors.
8. In container shipping, different charges are applied to 'less-than-container-loads' (LCL) and '.....' .

Notes

9. There are three types of conference rates, including commodity rates,, and commodity-class rates.
10. When a tramp carrier is engaged, it is said to be under.....

9.8 Chartering Practices

When a tramp carrier is engaged, it is said to be under charter. The charterer (person who engages or hires the tramp) can hire the tramp either whole or bulk of the space. The agreement between the ship owner and charterer for hiring the ship is called charter party. A tramp may be chartered in one of the most important forms:

- (a) **Voyage Charter:** A ship may be engaged for a single voyage (say from port A to port B) or for consecutive voyage (say from port A to port B to port C) or return voyage (say from port A to port B and return to port A). The ship owner provides the vessel to the charterer for carrying an agreed quantity of cargo from a particular port in a country (Mumbai, India) to another port in a different country (Baltimore, USA). Instead of one port, ports of loading in India could be more (Mumbai, Chennai) and in similar way ports of discharge can be more than one in USA (Baltimore, New York). Alternatively, the agreement (known as charter party) provides carriage of cargo between ports within a certain range (say from any port in India to any port in USA). In the later case, the charterer has to convey the names of the specific ports to the master of the vessel before the commencement of voyage.

The agreement may provide that the charterer has to pay for the freight according to the actual quantity loaded or for the total capacity of the ship. Even if the charterer is not able to load the total quantity agreed upon, he has to pay the freight for the agreed quantity. The remaining capacity not booked by the charterer can be hired by the ship owner to another charterer. In this case, the ship owner has to bear the total expenses for the voyage such as fuel, port charges, salaries of crew, stores and provisions, depreciation, insurance, etc. In other words, ship owner has to bear all running expenses and operating expenses for the voyage. The ship owner recovers the freight charges from the charterers in the form of revenue. After meeting all expenses, balance of revenue becomes the profit for the voyage to the ship owner.

For a comparison, this practice can be compared to engaging a total bus by a marriage party with understanding that fifty seats would be paid at an agreed rate and the balance 10 seats can be sold to other passengers by the bus owner. Even if the marriage party does not come in full swing of total booking made, still the bridegroom's party has to pay for 50 seats, as agreed. The bus owner is free to book the balance 10 tickets to another marriage party, provided he is able to synchronise!

- (b) **Time Charter:** Under time charter arrangement, a ship is hired for a fixed time period with the condition that the ship is to be operated in specified territories. Though the primary essence of the agreement is for the fixed time, still the charterer can employ the ship only within the specified territories. The charterer cannot operate the ship beyond the territorial jurisdiction. The ship owner has to deliver the ship to the charter, on the agreed date, in a seaworthy condition. Besides, it is the duty of the ship owner to ensure the ship, in the same seaworthy condition, during the period for which the ship has been given on contract to the charterer to enable him to use the ship for the purpose of carrying cargo during the contracted period. It is the responsibility of the ship owners to provide the crew and maintain stores and provisions for the crew during the period of voyage. All the operating expenses such as insurance, depreciation and other fixed expenses have to be borne by the ship owner. All the running expenses like fuel, port charges, canal dues and cargo expenses have to be met by the charterer. The charterer has to pay the agreed hire charges, generally

in advance, whether the ship is used or not during the contractual period. After the period is over, charterer has to return the ship, in the same seaworthy condition; it has been given, back to the ship owner, except the normal wear and tear.

The ship owner is assured of the contracted hire charges. By a long-term contract of affreightment, the charterer is protected from the vagaries of fluctuations in freight rates during the long-term contractual period. The charterer can also sublet the ship if the agreement so provides. If the market rates improve and the ship is sublet later, then the charterer may earn more money than what he has to pay in the form of hire charges to the ship owner and stands to gain.

The charterers have greater responsibility under time charter compared to voyage charter. However, under time charter, the ship owners have to undertake the responsibility that the ship is maintained in a seaworthy condition during the contract period. The ship owners have to exercise all reasonable care and diligence to maintain the ship, in seaworthy condition. This implies that the ship owners are responsible in keeping the hull, machinery and equipment in a thoroughly efficient condition during the contract period so that the charterers are able to employ the ship for carrying the cargo without any problem, whatsoever.

- (c) **Bare Boat Charter or Charter by Demise:** Under this agreement, the bare boat is let out by the ship owner to the charterer for a fixed period. The ship owner hands over the boat in a seaworthy condition to the charterer. The ship is at the disposal of the charterer during the period. It is the responsibility of the charterer to bear all running expenses like paying salary to crew and maintaining the necessary provisions and stores, in addition to bearing all the operating expenses, as mentioned above in the charter voyage. The charterer has the right to appoint the master of the crew and the Chief Engineer, subject to the approval of the owners.

The difference between the time charter and bare boat charter lies in the fact that in the later case the ship lies in the bare form with the charterer who has the full right to operate the ship, in the way he desires. The ship owners have the minimum responsibility and are considered as 'dead' as they have no concern about the expenses and the use of the ship. Under this type of chartering arrangement, which is frequently also termed 'chartering by demise,' the ship owner virtually relinquishes all responsibilities and rights in respect of his vessel for a specified period, in return for a pre-arranged and regular payment of hire.

The charterer becomes an assumed owner, operating, crewing and chartering the ship as if he were, in fact, the owner. They have to return the ship in the same seaworthy condition as they have received, except normal wear and tear. For the agreed period, the ship owners are paid a fixed sum per ton, calculated on dead weight of the ship. The charterer is totally free to use the ship for carrying the cargo during the specified period and has to bear all running and operational expenses.

9.9 Global Trade and Container Traffic

Shipping is truly the lynchpin of global economy and international trade. More than 90% of world merchandise trade is carried by sea and over 50% of that volume is containerised. In today's era of globalisation, international trade has evolved to the level where almost no nation can be self-sufficient and global trade has fostered an interdependency and inter-connectivity between countries. Shipping has always provided the most cost-effective means of transportation over long distances and containerisation has played a crucial role in world maritime transport.

Notes

Global merchandise trade has been growing at CAGR 10.3% (value terms) during 2001-2005, which was the highest average growth rate of world merchandise trade in the last three to four decades. The high merchandise trade has pushed container traffic worldwide. In 2005, it is estimated that world merchandise trade has witnessed an excellent growth rate of 13% in volume terms and container traffic has registered an estimated growth rate of 13.89%. Containerisation accounts for over 50% of world merchandise trade and is expected to go up further. During 2001-2005, world container traffic has increased at CAGR 9.2%.

9.10 Role of Intermediaries in Shipping Industry

- **Freight Forwarders:** Freight forwarders typically act as a shipper's agent during the shipping process. Freight forwarders select the mode and carrier for their clients' shipments, provide and process documentation, and make freight, terminal, and handling payments on behalf of their clients. In operational terms, forwarders primarily focus on consolidating or combining many small shipments into a single large shipment, which can then be shipped at a lower cost. Typically, a freight forwarder will purchase unit(s) from a carrier and sell space within the unit(s) to several shippers. The cost charged for this space is significantly less than the cost of an entire unit and thus allows small shipments to be processed efficiently.

A forwarder can engage a number of intermediaries on both ends of the cargo movement to enable door-to-door service. Door-to-door movement of cargo can reduce transportation costs and give control of the shipment to the exporter.

- **NVOCCs:** Non-vessel Operating Common Carriers (NVOCCs) buy space from ocean carriers for consolidated shipments from a variety of clients. NVOCCs specialize in less than-container load (LCL) shipments and perform many of the same functions as freight forwarders. Unlike forwarders, however, NVOCCs are common carriers that use containers rather than vehicles or vessels. NVOCCs are frequently the customers of freight forwarders and the clients of ocean carriers. A typical situation might involve a NVOCC combining a partial load from Durban bound for Antwerp from Forwarder A with a partial load bound for Antwerp from Forwarder B, and subsequently hiring an ocean carrier to move the loaded container from Durban to Antwerp.



Note As transport costs for loaded and empty containers are often the same, NVOCCs try to find backloads for empty containers returning to port from inland locations, which allows NVOCCs to obtain revenue on the return of empty containers to port while enabling the flow of goods.

- **Customs Brokers:** Customs brokers escort goods through the customs process and have experience with local customs regulations and trade practices. Brokers ensure compliance with laws and verify that customs documentation has been completed.
- **Export Packers:** Export packing firms supply packaging materials and services for overseas shipments. Export packers specialize in packing for maximum shipment cost efficiency and typically are familiar with any agricultural restrictions and quarantines that pertain to packaging material.

Typical clients of packers are producers that are capable of marketing products locally but that lack the expertise to correctly protect their goods for international movement. Packers are also employed by exporters that require specific packaging of their goods for transport.

- **Export Management Companies (EMC):** EMCs act as agents for domestic firms in overseas markets. Using an EMC gives a producer immediate access to foreign market knowledge and export know-how, regardless of its experience in foreign markets. An EMC is an independent firm, which in effect acts as the exclusive export sales department for a producer or industrial group. An EMC functions in foreign markets just as a sales representative or exclusive wholesaler functions for a manufacturer in the domestic market.
- **Export Trading Companies:** Export trading companies locate buyers in foreign markets and manage most of the export arrangements for the product. This may include documentation, inland and overseas transportation, and compliance with foreign governmental regulations.

Efficient intermediaries enable a manufacturer to effectively move goods in three ways: through heightened compliance, timelier clearance and movement, and more cost-effective allocation of resources.

It is essential that the efficiency of transport intermediaries be achieved through universally agreed-upon trade procedures and practices with the use of electronic techniques for information transfer. Such practices will significantly improve trade efficiency.

9.11 Latest Trends in Logistics Operations

Logistics management's primary focus is on optimizing the delivery of service to customers, by managing complex tradeoffs between customer service, transportation, warehousing and inventory. Some World Class companies have been able to reduce the costs of their logistics operations to 50% of the levels of their competitors.

9.11.1 Trends in Logistics

Radio Frequency Identification (RFID)

The first use of Radio Frequency Identification (RFID) was documented in the 1940's by the British Royal Air Force to identify aircraft in World War II and was part of the refinement of radar. During the 1960's RFID was first considered as a tracking solution in the commercial world. The first applications involving RFID were developed over the next twenty years. These commercial applications were concerned with identifying an item inside a single location. The latest attempt to commercialize the use of RFID started in 1998, when researchers at the Massachusetts Institute of Technology (MIT) Auto-ID Center began to research new ways to track and identify objects as they moved between physical locations. This research centered on radio frequency technology and how information that is held on tags can be effectively scanned and shared in real time.

Mechanics of RFID

The basic principle of RFID is identifying an object using a radio frequency transmission. The technology can be used to identify, track, sort or detect a wide variety of objects. Communication takes place between a reader or interrogator and a transponder or tag. Tags can either be active, which means it is powered by battery, or passive, which is powered by the reader field. The communication frequencies used depends to a large extent on the application, and range from 125KHz to 2.45 GHz.

Notes



Did u know? Regulations are imposed by most countries to control emissions and prevent interference with other industrial, scientific or medical equipment.

In a typical system tags are attached to objects. Each tag has some internal memory which it stores information about the object, such as its unique ID number, or details including date of manufacture and item information. When a tag passes through a field generated by a reader, it transmits this information back which identifies the object. Until recently the focus of RFID technology was mainly on tags and readers, which were being used in systems where relatively low volumes of data are involved. This is now changing as RFID in the supply chain is expected to generate huge volumes of data, which will have to be filtered and routed to ERP or Warehouse Management systems.


Electronic Product Code (EPC)

Electronic Product Code is the emerging RFID standard developed by the MIT AutoID center. It is the RFID version of the barcode standard. EPC RFID also provides access to additional data about the origin and history of the specific batches or serial numbers. The EPC tag itself identifies the manufacturer, product, version and serial number.

Benefits of RFID Supply Chain Management is investing in RFID as it can give them advantages in visibility of their products through the supply chain. The benefits are seen as improving on other methods of visibility such as EDI, bar coding and Advance Ship Notifications (ASN). Other benefits of RFID can be seen outside of normal supply chain such as a reduction in theft from the store, transport or storage, and a deterrent to increasing product counterfeiting. Both of these issues are costing companies billions of dollars each year.



Caution Pharmaceutical companies are increasingly worried about counterfeiting and RFID tags on each product may help with this issue.



Task Visit the shipping company of your choice and find out the intermediaries and their roles involved in the complete process.

Self Assessment

Fill in the blanks:

11. The tag itself identifies the manufacturer, product, version, and serial number.
12. The basic principle of is identifying an object using a radio frequency transmission.
13. management’s primary focus is on optimizing the delivery of service to customers, by managing complex trade-offs between customer service, transportation, warehousing and inventory.
14. EMCs act as agents for firms in overseas markets.
15. typically act as a shipper’s agent during the shipping process.

9.12 Summary

Notes

- The demand for transport services is a derived demand. The derived demand is dependent upon the nature of goods traffic in international trade. If the demand for a commodity is more, the relative nature of that goods traffic becomes more.
- In India custom clearance is a complex and time taking procedure that every exporter faces in his export business. Physical control is still the basis of custom clearance in India where each consignment is manually examined in order to impose various types of export duties. High import tariffs and multiplicity of exemptions and export promotion schemes also contribute in complicating the documentation and procedures. So, a proper knowledge of the custom rules and regulation becomes important for the exporter. Indian Shipping consists of 31 major companies (INSA members) with Shipping Corporation of India (SCI), the central PSU being the largest one. The country has the largest Merchant Shipping fleet among the developing countries and is ranked 17th in the World. Regulation of merchant shipping is governed by Merchant Shipping Act, 1958. Apart from facilitating transportation of national and international cargoes, Indian maritime sector also provides a variety of other services such as cargo handling services, ship building and ship repairing, freight forwarding, light house facilities, training of marine personnel, etc.

9.13 Keywords

Cargo Ship or Freighter: A cargo ship or freighter is any sort of ship or vessel that carries cargo, goods, and materials from one port to another.

Conference: A conference is an association of two or more liner shipping companies.

Containerisation (or Containerisation): It is a system of intermodal freight transport using standard intermodal containers as prescribed by the International Organisation for Standardisation (ISO).

Shipping Line: A shipping line is a business that operates ships.

Time Charter: Under time charter arrangement, a ship is hired for a fixed time period with the condition that the ship is to be operated in specified territories.

9.14 Review Questions

1. What are different modes of shipment? Identify their important characteristics.
2. Write a brief note on the history of shipping history in India.
3. Discuss the role of intermediaries in shipping industry.
4. Highlight the latest trends in logistics operations.
5. What are the significant characteristics of shipping industry?
6. What is Conference System and Practices in International shipping?
7. Explain the Chartering Practices used in shipping Industry.
8. Explain the role of Clearing and Forwarding agent in shipping Industry.

Answers: Self Assessment

1. Air transport
2. Water Transport

- Notes**
3. Road Transport
 4. distance
 5. conference
 6. Liner
 7. cargo
 8. full-container-loads
 9. class rates
 10. charter
 11. EPC
 12. RFID
 13. Logistics
 14. Domestic
 15. Freight forwarders

9.15 Further Readings



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Online links

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Case Study

Recycled Timber Dunnage a Win for the Shipping Industry Illawarra S&N Enterprise

Illawarra S&N Enterprise collects, reprocesses and resells timber used in shipping bulk cargo—cargo that does not get transported in shipping containers. Called ‘dunnage’, the timber is used to chock, support and distribute the weight of the cargo. Before Illawarra S&N Enterprise developed a business for doing this, the timber had previously not been recycled, and was dumped as waste.

Company Characteristics

Illawarra S&N Enterprise was established in 2002 for the specific purpose of recycling dunnage. The company is located in Port Kembla, NSW, and is owned by Habibul Haque—the sole operator.

Seeing enormous potential in dunnage recycling, and well aware of the environmental benefits it offered, Illawarra S&N Enterprise approached Austral Asia Line (AAL) Shipping Agencies and was granted approval to collect and use the dunnage generated from its general cargo liner services docked at Port Kembla.

Shipping and stevedoring agencies incorporate the cost of supplying new dunnage into every shipping load. The quantity of dunnage used per voyage varies. However, it would not be unusual for between 50–70 cubic metres of dunnage (approximately 5–6 trees) to be used for every brake bulk cargo vessel departing Australia. Metal strapping and cables are also used to secure cargo and are included in general waste dunnage material calculated for this project.

What did they do?

AAL Shipping Agencies provided their support for the idea, and the next step for Illawarra S&N Enterprise was promoting the reuse concept to the existing market, while at the same time exploring and developing new markets for a recycled dunnage product.

Once collected from AAL Shipping vessels at the Port Kembla multipurpose wharf, the dunnage was processed. The timber had to be de-nailed, recut into suitable lengths, bundled and fumigated. Certified fumigation is an essential step in the recycling process because the timber has to meet strict international quarantine requirements. Illawarra S&N Enterprise then resold the recycled dunnage back to AAL Shipping, at a significantly reduced price compared to the cost of buying new dunnage.

Why did they do it?

With many years experience in the merchant navy, the principal of Illawarra S&N Enterprise, Habibul Haque, saw first hand the amount of unnecessary waste generated during transportation of brake bulk cargo.

Further, he became disillusioned and frustrated when he learned that disposing of this waste overboard in international waters was common practice. Jettisoned dunnage at sea is a hazard to marine life, particularly large mammals such as whales and dolphins, but also coral reefs and shoals. It can also severely damage vessels or spoil coastlines and beaches.

Contd...

Notes

Illawarra S&N Enterprise saw an opportunity for reusing a viable resource rather than considering it as a waste product. The company estimated it could process the waste dunnage and resell it back to clients for approximately half the cost of supplying new dunnage.

What are the Environmental Gains?

From August 2002 to October 2003 AAL Shipping purchased 486 cubic metres of recycled dunnage back from Illawarra S&N Enterprise.

This equates to approximately 50 trees not having to be cut down to supply virgin dunnage. Approximately 12 cubic metres of metal strapping, cables and wire has been recovered from vessels and recycled as scrap metal. This would normally be dumped at sea along with the dunnage.

What are the Costs and Savings?

Current market costs for virgin dunnage range from \$248 to \$285 (+ GST) per cubic metre. This compares to one standard price of \$190 per cubic metre for recycled dunnage supplied by Illawarra S&N Enterprise.

Using the example from AAL Shipping of 486 cubic metres for 14 months:

virgin softwood @ \$248/m ³	\$120,528 + GST
virgin hardwood @ \$285/m ³	\$138,510 + GST
recycled dunnage @ \$190/m ³	\$92,340 + GST

This demonstrates potential savings for AAL of between \$28,000 and \$46,000 for the 14-month trial period (not including GST).

Where to now?

There is now acknowledgement throughout the industry that dunnage recycling is a viable service that warrants ongoing industry support and recognition.

Indeed, during the trial it emerged that the demand for reused dunnage outweighed the available dunnage supplied by AAL vessels. Alternative dunnage sources need to be identified and secured from across the broad shipping, freight forwarding and stevedoring industry.

Industry Acceptance

“As a result of the Illawarra S&N Enterprise dunnage recycling program, AAL Shipping has noted an obvious environmental advantage. We will continue to use Illawarra S&N Enterprise recycled dunnage and have taken additional steps to implement similar recycling methods in Hobart.”

Question:

Discuss the environmental gains of the adoption of reuse concept in this case

Unit 10: Containerization and Leasing Practices

Notes

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10.3 Transportation of Containers

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10.5 Container Leasing Practices

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10.7 Keywords

10.8 Review Questions

10.9 Further Readings

Objectives

After studying this unit, you will be able to:

- Explain Concept of containerisation
- Discuss Types of container
- Discuss the Benefits of containerisation
- Explain Global trade and containerisation
- Describe Container leasing practices

Introduction

Containerisation is a method of distribution of goods using containers. The use of containers has not only facilitated but has also revolutionized the carriage of goods among developed countries. Exporters in developing countries are also making greater use of containers for the transportation of the goods. The enactment of Multimodal Transportation of Goods Act, 1993 has enabled exporters from India to use containers for transportation of export cargo. Train or road to the seaports carries the containers, where they are loaded on the ships for onward transportation to their destination.

Exporters do not need to carry the cargo to the seaports any longer rather they can approach the container freight station or the Inland Container Depot (ICD) to book the cargo there for transportation to the destination. The custom clearance of the cargo is provided at ICDs and in the process, the exporters are able to save lot of time. The packing of cargo in a container can be done either in the container depot or in the factory of the exporter.

The holds of container vessels are fitted with a series of angle guides, adequately cross-braced, to accept the container. Such holds are completely dedicated to either the 20 or 40 ft. containers. The containers are stacked, such that, the one above rests securely on the weight-bearing corner castings of the one below. The angle guides also facilitate discharging and loading by guiding spreader frames of container cranes onto the corner castings of containers without any need for the crane driver to make any fine adjustments to line up the lifting frame.

Notes

Container berths are either purpose built for exclusive container use, or multipurpose in which container and other types of cargo vessels are handled. A purpose built container berth is usually the more efficient and produces the most productive container throughput. The most modern one would be computer-operated.



Caution Computerization plays an important role in the operation, controlling the delivery and pick up of containers from the truckers as well as the movement and positioning of all containers in the terminal.

Time spent in loading and discharging containers varies by port and circumstances. In very broad terms, one can attain 25/30 containers per hour for discharging cargo whilst for exports the figure is 20/25 per hour per crane of single container capacity. The high merchandise trade has pushed container traffic worldwide. In 2005, it is estimated that world merchandise trade has witnessed an excellent growth rate of 13% in volume terms and container traffic has registered an estimated growth rate of 13.89%. Containerisation accounts for over 50% of world merchandise trade and is expected to go up further.

10.1 Different Types of Containers

The container, as the meaning implies, is an equipment used to store and carry goods. In shipping, the term was used to refer to any type of box used to carry cargo. Presently too, a container is known as 'box' or 'an' in many countries, particularly in the U.S.

The International Organisation for Standardisation (ISO) defined a freight container as:

An article of transport equipment,

- Of a permanent character and accordingly strong enough to be suitable for repeated use;
- Specially designed to facilitate the carriage of goods by one or more modes of transport, without intermediate reloading;
- Fitted with devices permitting its ready handling, particularly its transfer from one mode of transport to another;
- So designed as to be easy to fill and empty – Having an internal volume of 1m³ (35.3cu.ft) or more.

10.1.1 Classification of Containers

1. **By raw material:** A container can be classified in terms of its building or cladding materials i.e. it is defined by what it is made of. The maximum numbers of containers are made of steel, aluminium or GRP (Glass Fiber Reinforced Plywood). Almost 65 percent of the entire container fleet presently consist of steel containers.
2. **By size:** The ISO has worked a great deal on standardisation of container dimensions and published recommendations. Containers are defined in multiples of 10 ft. i.e. 10ft or 20 ft, or 30ft, or 40ft. Presently 20ft, 40ft containers are used predominantly, and around 65-70 percent of world fleet consists of 20 ft containers. Twenty-foot containers are referred as Twenty Foot Equivalent Unit or TEU and 40 footers as FEU (Forty foot Equivalent Unit). If all the containers are expressed—in terms of TEU, it becomes easier for the container terminal operators and ship owner to estimate the space required in a container terminal or inside the vessel.

Most of the containers have width of 8 ft. However, in height containers vary from 8ft to 8Y2 ft. Presently about 75 percent of world box fleet have a height of 8Y2 ft. and about 20 per cent have a height of 8 ft. However, there is an increasing tendency to use containers of 9Y2 ft (High cube)



Did u know? The most widely used type of container is the general purpose (dry cargo) container having a nominal length and height of 20' x 8.5', 40' x 8.5', and 40' x 9.5'. Referring to the Dimension of General Purpose Containers below, the dimensions shown in the table are not fixed, that is, the external and internal dimensions may vary among containers of the same length and height.

The container capacity is the total cube a container can accommodate. The term cube often refers to the cubic measurement of cargo. The capacity (i.e., the internal volume) is determined by multiplying the internal dimensions, that is, the product of internal length, width and height. The capacity may vary among containers of the same length and height.

3. **By use:** Containers can also be classified by their uses. Containers maybe broadly classified into three types by cargo to be stowed therein.
 - (a) *The General Cargo Container:* The General Cargo Container is the most representative type for general cargo (packed cargo) that does not require temperature control. This type occupies an overwhelming share of the total number of containers. The type is called Dry Cargo Container in ordinary parlance. It is generally of the closed van type with a door at one end.

These containers are closed and are suitable for the carriage of all types general cargo both solid and liquid. Access for loading and unloading is through full width doors. The dimensions of general-purpose containers as follows:

Table 10.1: Internal and External Dimensions of Cargo Containers

Oveall Dimensions	Inside Dimensions	Cubic Capacity
1. 20 x 8 x 8.5 ft. (6.1x ² . 4x ² .6 mt)	5.98 x 2.34 x 2.400 mt.	32.7 m ³
2. 40 x 8 x 8.5 ft. (12.2 x ² . 4 x ² . 6 mt)	12.015 x ² 2.345 x ² 2.400 mt.	66.3 m ³

Based on the length of the container, the container is generally known as a 20 ft container or 40 ft. container in practice.

- (b) *The Thermal Container:* The Thermal Container is designed for cargo requiring refrigerated or insulated storage. It is covered with material of low heat transfer such as polystyrene foam.

Thermal containers are classified into three types:

- (i) Refrigerated (or Reefer) Container (for cooled foodstuffs, meat, fish vegetables etc.)

It has insulated walls, doors, roof, and floor, which limit the range of temperature loss or gain. It is used for perishable goods like meat, fruits and vegetables
- (ii) Insulated Containers for fruit, vegetables etc.

Notes

Here dry ice is used as the cooling medium. It does not use any device for cooling and/or heating.

- (iii) The ventilated Container allows for the passage of air by means of apertures on sides or ends. This type is used for cargo such as fruit or vegetable, which requires respiration. They are required for carriage of special cargo like tea, coffee, etc. which may lose moisture, that is; they may “sweat” if carried in closed box type containers.

Considerable advancement has been made with regard to refer containers. Controlled Atmosphere and Modified Atmosphere systems have been introduced.

- (i) **Controlled Atmosphere:** In the Controlled Atmosphere, there is computerised controller. The refrigeration unit maintains the set temperature and the controller maintains the ideal atmosphere by sensing the product’s consumption of oxygen and production of carbon dioxide. By integrating this information the controller continuously adjusts air exchange valves and activates the required scrubbing systems to maintain the atmosphere of the pre-set level.
 - (ii) **Modified Atmosphere system:** In the Modified Atmosphere system, the desired atmosphere is created in the container when it is stuffed. The container is then sealed to prevent changes in the original atmosphere due to ventilation. The modified atmosphere system is limited to shorter voyages and fewer commodities than the controlled atmosphere system.
- (c) *Special Containers:* The third category of container comprises of the balance types under the broad head of “Special Containers”. Prominent type in this head are: Bulk containers, Tank containers, open top Containers, Side Open containers, Flats, Car containers, Pen containers (to carry livestock).
- (i) **Bulk Containers:** These containers are designed for the carriage of dry powders and gram substances in bulk.
 - (ii) **Ventilated Containers:** These containers have full length ventilation galleries.
 - (iii) **Half Height Containers:** Half-height version of the open top container is designed for the carriage of heavy dense cargoes such as steel, pipes and tubes etc.
 - (iv) **Tank Containers:** These containers are generally constructed for the carriage of a specific product or range of products in mind.
 - (v) **Open Sided Containers:** These containers are designed to accommodate specific commodities such as plywood, perishable commodities and livestock.
4. **Dry Cargo Containers:** Dry cargo containers are by far the maximum in use. They are of different types. A standard dry cargo container is a of box type with a door at one end. Sometimes containers are provided with side doors, i.e., the entire side of the container can be opened for easier stuffing and destuffing. These types of containers are useful when stuffing operations are carried out while the container is mounted on a wagon or trailer. There are various “dry specials” like open top containers, flat racks, bulk containers, garment container, ventilated containers, etc.
- (i) *The open top Container:* The open top container is one having no roof and usually provided with a polythene lined tarpaulin to cover the container. The advantage of this container is that heavy machineries, structurals, etc. Can be easily hoisted by a crane and put inside the container through its open roof.

- (ii) *Flat container:* Flat rack or flat container is a container having its base only. Usually a cargo of odd size and weight is put on to this container and is lashed to it:
- (iii) *Bulk Container:* Bulk container is a container fitted with manholes to facilitate loading of bulk cargo through gravity.
- (iv) *Garment Container:* Garment containers are fitted with hangers to help loading a large number of garments in hangers into the containers.
- (v) *Liquid Containers:* Liquid containers are usually made of stainless steel and have manholes for loading and unloading liquid cargo.
- (vi) *Gas Containers:* Gas containers are special containers with fixtures and fittings for filling and emptying liquid gas. They also have special features like thick walls of special metal for safety during transit.

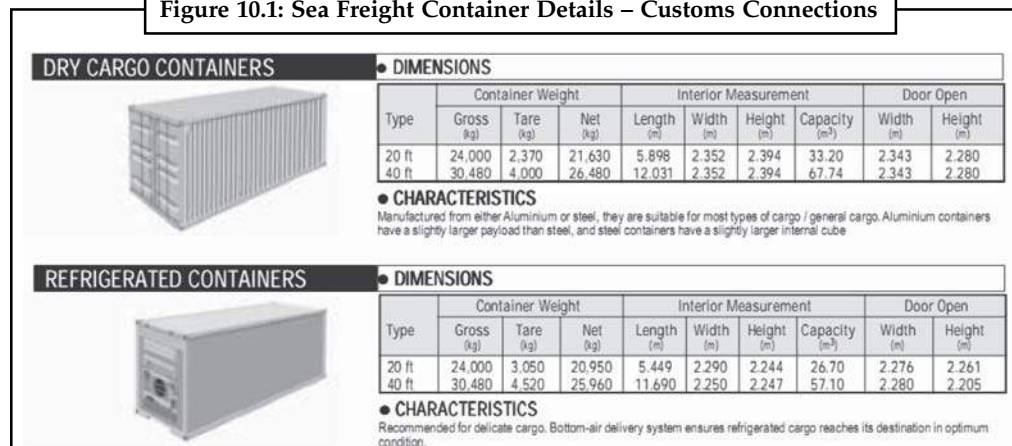
10.1.2 Other Containers

- (i) *Insulated Containers:* Such containers protect the cargo against heat loss or gain and are used in conjunction with a blown-air-refrigeration system to protect perishable or other cargo which needs to be carried under temperature control.
- (ii) *Fruit Containers:* These are insulated containers with internal dimensions slightly longer.
- (iii) *Refrigerated Containers:* These containers are fitted with their own refrigeration units which require an electrical supply for their operation. These containers are 12.2m long, 2.4 m wide and 30 m high.
- (iv) *Hanger Containers:* These containers are used for dry cargo and are equipped with removable beams in the upper part. They are used for the shipment of garments on hangers.
- (v) *Bin Containers:* These containers have no doors and are ideal for heavy dense cargoes such as steel, pipes etc.

10.2 Design of Containers

A freight container are generally rectangular in shape, weatherproof, used for transporting and storing a number of unit loads, packages or bulk material; it confines and protects the contents from loss or damage, it can be separated from the means of transport, handled as a unit load and transshipped without rehandling the contents.


Figure 10.1: Sea Freight Container Details – Customs Connections



Contd...

Notes


OPEN TOP CONTAINERS



Type	Container Weight			Interior Measurement				Door Open	
	Gross (kg)	Tare (kg)	Net (kg)	Length (m)	Width (m)	Height (m)	Capacity (m ³)	Width (m)	Height (m)
20 ft	24,000	2,580	21,420	5.629	2.212	2.311	32.00	2.330	2.263
40 ft	30,480	4,290	26,190	11.763	2.212	2.311	65.40	2.330	2.263

CHARACTERISTICS
Allowing cargo to be loaded from the top, open top containers are particularly suitable for bulky cargo such as machinery. They are fitted with a PVC tarpaulin cover and attachable bows with cable sealing devices. The container doors can be removed to make the stuffing of cargo more convenient. Manufactured from steel.


FLAT RACK CONTAINERS



Type	Container Weight			Interior Measurement			
	Gross (kg)	Tare (kg)	Net (kg)	Length (m)	Width (m)	Height (m)	Capacity (m ³)
20 ft	30,480	2,900	27,580	5.624	2.236	2.234	27.90
40 ft	34,000	5,870	28,130	11.786	2.236	1.968	51.90

CHARACTERISTICS
Flatracks are especially suited to heavy loads or cargo that needs loading from the top or sides, such as pipes and machinery. They are collapsible and non-collapsible containers with or without walls. Manufactured from steel.


GARMENT CONTAINERS



Type	Container Weight			Interior Measurement				Door Open	
	Gross (kg)	Tare (kg)	Net (kg)	Length (m)	Width (m)	Height (m)	Capacity (m ³)	Width (m)	Height (m)
20 ft	24,000	2,240	21,760	5.898	2.352	2.394	33.20	2.343	2.280
40 ft	30,480	3,885	26,595	12.031	2.352	2.394	67.74	2.343	2.280

CHARACTERISTICS
Used for all kinds of garment. The containers are specially designed for garment product and related industry. There are some options of using a string or bar system or a combination of both. The containers allow increased flexibility, greater load Internal Capacity and savings on transportation and handling cost.

HIGH CUBE CONTAINERS



Type	Container Weight			Interior Measurement				Door Open	
	Gross (kg)	Tare (kg)	Net (kg)	Length (m)	Width (m)	Height (m)	Capacity (m ³)	Width (m)	Height (m)
40 ft	30,480	3,980	26,500	12.031	2.352	2.698	76.30	2.340	2.585
45 ft	30,480	4,800	25,680	13.544	2.352	2.698	86.00	2.340	2.585

CHARACTERISTICS
With high cube containers, you gain an extra foot in height compared with general-purpose containers. Ideal for light, voluminous cargo or bulky cargo. These extra volume containers come in steel and aluminium.

For identification, containers have markings showing:

- (a) Owner Code, Serial Number and Check Digit.
- (b) Country Code and Type Code.
- (c) Maximum, Gross and Tare Weight.

This is illustrated below:

Enrollment in local colleges, 2005				
Owner Code	Serial Number	Check Digit	Country Code	Type Code
ABZU	001234	3	FXX	2030
MAS Gross	00000	kg		
	00000	Lb		
Tare	0000	KG		
	0000	Lb		

10.2.1 The Concept of FCL and LCL

FCL, the charge is meant for one party. All goods are stuffed at the premises of the seller and are destuffed at the consignee's warehouse.

In LCL, the cargoes are meant for different parties. Here the carrier collects cargo packages from various shippers and stuff all of them into one or more containers, depending on the total

volume, at the pier. At the port of destination, the carrier's agents destuff and deliver the cargoes to the respective consignees. Discriptions and examples are as follows:

Notes

Figure 10.2: 10ft Container



Figure 10.3: 40ft Double Door Container

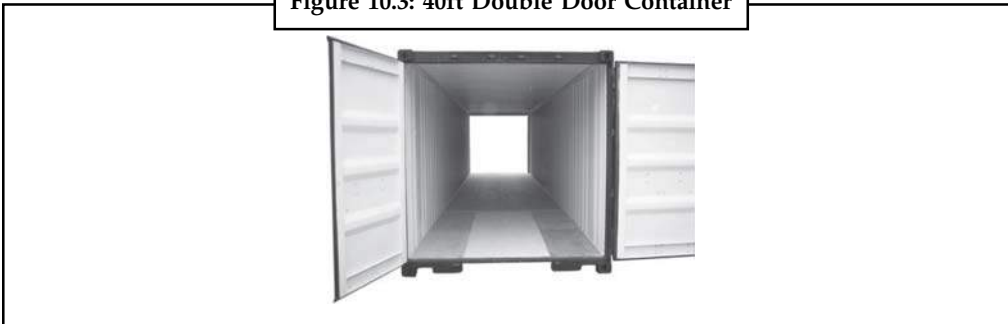


Figure 10.4: 40ft Double Door Conversion Container



Figure 10.5: 40ftCSC Plated Flat Rack Container



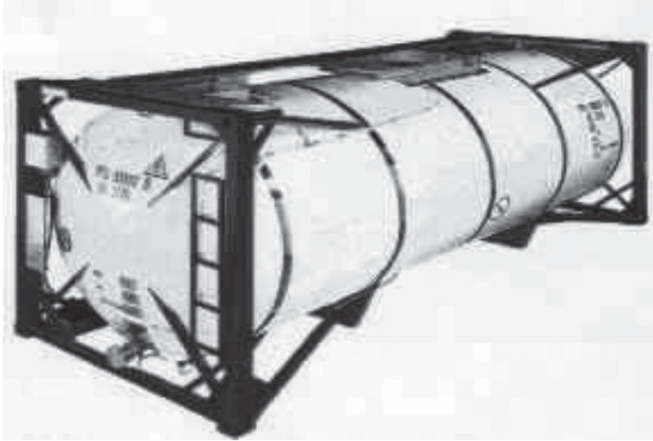
Figure 10.6: Bulk Containers



Notes

- 20 TO 28 FT. Long
- Tank Capacity
- 4,000-6,000 GAL.
- Bulk containers designed with a steel structure around the outside to facilitate stacking

Figure 10.7: IMO 1 (Highly Flammable, Toxic and Corrosive)



- 316 Stainless Steel Shell
- 3,158-6,974 Gal. capacity
- Transport for hazardous liquids
- Flash point below 32 degrees fahrenheit
- IMO 2 (flammable liquids, herbicides and insecticides)
- 316 stainless steel shell
- 3,158-6,974 gal. capacity
- Transport for low-hazard liquids
- Flash point between 32-142 degrees fahrenheit

Figure 10.8: IMO 5 (Fammable Gases)



- 316 stainless steel shell
- 3,846-6,710 GAL. capacity
- Transport of gases, Propane, Butane, Anhydrous Ammonia and Refrigerants

Notes

Figure 10.9: IMO 7 (Cryogenic/Refrigerated Liquids)

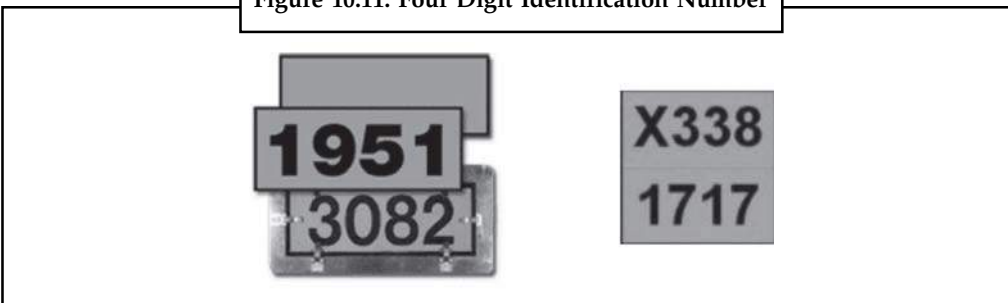


- 2,105-5,263 GAL. capacity
- Transport of bulk liquids
- Oxygen, nitrogen, carbon dioxide, argon, ethylene
- Placards
- Intermodal containers are placarded according to highway placarding regulations

Figure 10.10: Different Placards Used



Figure 10.11: Four Digit Identification Number



Intermodal containers must have a United Nations four-digit identification number assigned International carriage of dangerous goods by road (adr)

Notes

- Additional orange placard above the 4 digit UN number
- ADR Hazard Identification Number (HIN) also known as “the Kemler code”
- “the Kemler code”
- 1st digit: Primary hazard
- 2nd two digits: Secondary hazards
- When a number is doubled, it indicates that the hazard is intensified for that specific hazard

What are Shipping Containers?

Manufactured to the ‘International Standards Organisation’ (ISO) specification in respect to their dimensions.

What are they made of?

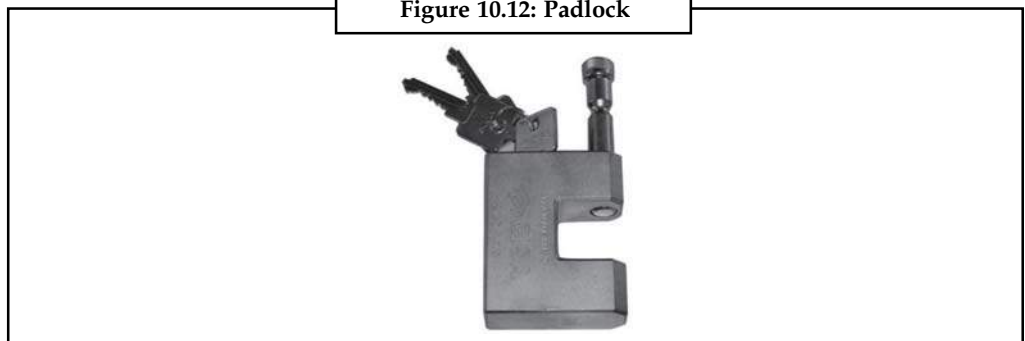
- Some are made of aluminum and steel, they are now mostly made entirely of a special steel called “Corten” which is a rust prohibitive type of steel.
- Steel frame, fitted with 8 weight bearing corner casting fitted into the 8 corners,
- Filled in with corrugated steel panels which are between 1.5 mm to 3.00 mm thick.
- Normally 4 locking bars which interlock with the frame top and bottom.
- 27mm thick wooden ply floor

Supported on load bearing crossbearers approx 12" apart, making the container capable of withstanding loads of 20 to 35 tons .

Few questions that need to be asked for understanding the characteristics of different containers are:

- How heavy are they?
2.5 tons for a 20' and 4 tons for a 40'
- Are they water tight?
Designed to be fully waterproof including the doors which are fitted with full wrap around seals.
- Are they secure?
When padlocked through the available holes in the door gear they are fairly secure but can be made more secure by the fitting of a lock box which conceals the lock from interference.

Figure 10.12: Padlock



- Notes**
- How old is a used container?
They are sold by shipping lines after 10 years of age.
 - What colour will it be?
Variety of colours – The type of paint is usually chlorinated rubber or vinyl, both manufactured to resist sea water, sun and abrasion.
 - Are they affected by condensation?
A container exposed to sunlight and cold can cause condensation, especially if the interior or if the contents of the interior are damp.
Condensation can normally be easily prevented by the use of disposable dehumidifiers.

Shipping Container Dimensions and Capacity

Length

- 9.8125 feet (2.991m) as 10 feet
- 19.875 feet (6.058m) as 20 feet
- 29.9375 feet (9.125m) as 30 feet;
- a40 feet (12.192m)

Width

8 feet (2.438m)

Height

- 8.5 feet (2.591m) and
- 9.5 feet (2.896m)

Handling of Containers

1. **Stuffing of Cargo in Container:** Stuffing of cargo in the container is concerned with packing of the cargo. The exporter or the shipper should formulate a proper stowage plan prior to packing a container. This would help the shipper to:
 - (a) Achieve optimal utilisation of container capacity
 - (b) Simplify and increase the speed of packing and unpacking.
 - (c) Plan for necessary cargo securing aids well in advance.
2. **Arrangement of Container:** The exporter should approach the cargo agent for hiring of the container. The cargo can be sent on FCL/LCL basis. FCL stands for Full Container Load' and LCL stands for Less than Container Load. The exporter can arrange for' packing of the cargo in the container in his factory if so desired. The cargo's agent will arrange for the packing and thereafter the containers are shifted to the container depot. Alternatively, the exporter can bring the cargo to the container depot and the cargo is stuffed in the container after custom clearance. The government has established number of inland container depots to provide the facility of export through containers by sea routes. The containers after

Notes

custom clearance are moved to the seaport for their loading on the ships on their way to destination. The movement of the containers can be done either by road or by rail.

3. **The Concept of Unit Load:** Containerisation is a method of distributing merchandise in a unitized form, thereby permitting an inter-modal transport system to be evolved providing a possible combination of rail, road, canal and maritime transport.

With a view to saving time and cost while handling, loading, discharging and transporting, cargoes are consolidated and made as huge a unit as possible (like 5 tons, 20 tons, 40 tons, etc.) so that at every point of handling of the unit, time is saved, hence cost is saved.

This system helps to increase many fold productivity in cargo handling by displacing labour. Moreover, when unit load is bigger, manual operation is not possible hence; mechanical methods are introduced involving capital investments.

4. **Container Marking:** For identification, containers have markings showing:

- ❖ Owner Code, Serial Number and Check Digit
- ❖ Country Code and type code
- ❖ Maximum Gross and Tare Weight

5. **Advanced Systems in Container Management**

Container Management Systems

Container Management Systems (CMS) are a New Dimension in Supply Chain Execution (SCE) and Collaborative Logistics Technology. The basic concept is to develop a responsive system for providing vital information inputs to decision makers and consignees for Efficient Asset Tracking and Control of the goods in transit.

- Focused on Returnable Transport Containers (RTCs) and other mobile assets.
- Deployed where asset has high actual, strategic regulatory or intrinsic value.

CMS Integrate Multiple Elements

- Container identification
- Container data capture/mobile computing
- Application software and hardware
- Integration software and hardware

A good container management for risk reduction involves the entire product life-cycle starting from the manufacturing of containers and then through entire value chain up to consumption of contents and the reuse, recycling or disposal of containers. Depending on the user groups the life cycle of a container can be divided into following five stages:

- (i) Product formulation and container design;
- (ii) Distribution;
- (iii) Use, handling and cleaning (e.g. triple-rinsing of containers, application equipment);
- (iv) Collection; and
- (v) Re-use, recycling or disposal.

At the product and container design, the container is with container manufacturing organisation, in stage 2 it passes to the user group (primary consumer) through distribution or industrial marketing, in stage 3 it is taken by the secondary user who use it to load and transport their products. Then the container passes to the transporter and through a series of loading and unloading with multiple transportation mediums it reaches its destination. Here the products and other contents are removed and supplied to the consumer. The empty containers are collected and taken back to the stage 2 after reconditioning for reuse.

Self Assessment

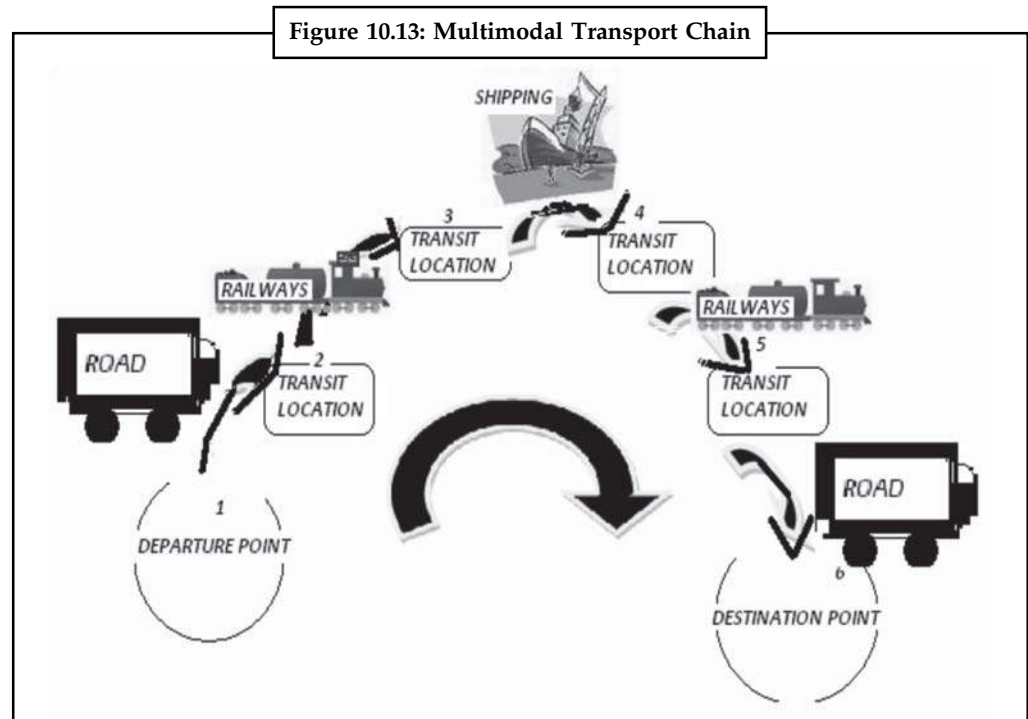
Fill in the blanks:

1. is a method of distribution of goods using containers.
2. Act, 1993 has enabled exporters from India to use containers for transportation of export cargo.
3. The most widely used type of container is the purpose (dry cargo) container.
4. of cargo in the container is concerned with packing of the cargo.
5. A good container management for reduction involves the entire product life-cycle starting from the manufacturing of containers and then through entire value chain up to consumption of contents and the reuse, recycling or disposal of containers.
6. Depending on the user groups the life cycle of a container can be divided into stages.
7. CMS stands for
8. The government has established number of container depots to provide the facility of export through containers by sea routes.
9. A container are generally rectangular in shape, weatherproof, used for transporting and storing a number of unit loads, packages or bulk material.
10. Container Management Systems concept is to develop a responsive system for providing vital information inputs to and consignees for Efficient Asset Tracking and Control of the goods in transit.

10.3 Transportation of Containers

The carriage of goods across the countries may take place by sea, by air, by road and rail or through multi-modal transportation. The nature and content of contract of carriage of goods also depend upon the mode of transport used. By contract of carriage of goods we mean a contract whereby a person agrees to carry goods from one place to another in return for a payment. The party who undertakes to carry the goods for payment e.g., the shipping company or the airways, is called the 'carrier', and the person who delivers the goods for carriage is known as the 'consignor' or the 'shipper'. Specific contracts between the carriers and the shippers are mostly based upon international conventions which are duly incorporated in the national laws. In many cases, however, contracts acquire legal entity when concluded on the basis of mutually accepted terms provided these terms do not go against any specific legal requirement in the concerned countries. In this unit, you will learn about all the international conventions and the relevant provisions of the Indian Acts governing the international carriage of goods by sea, by air, by road and rail and through multi-modal transportation.

Notes



The most far reaching impact of containerisation on the role of freight forwarders is their involvement in multimodal transport, i.e. carriage of goods by more than one mode of transport under a single contract. When a freight forwarder acts as a multimodal transport operator, he assumes responsibility for the execution of the multimodal transport contract, and of the carriers participating in the multimodal transport operations. He may enter into separate contracts with individual transport operators and provides of services, but these subcontracts would not affect his obligations to the consignor for the performance of the MMT contract and his liability to him arising under the contract.

10.3.1 Documentations

In multimodal transport, a variety of documents and information needs to be exchanged between shippers, transport companies and consignees as well as authorities, insurance companies, etc. The need for communication and amount of information naturally increases with the number of partners involved in the transport chain. The TCMS (Transport Chain Management System) was developed to make this easier. TCMS (Transport Chain Management System) is a fully Web-based system to be used to control a door-to-door transport where several transport modes are involved. TCMS automates the exchange of information and documents needed for the organization of multimodal transport in such a way that the user has no additional effort compared to uni-modal transport. Obstacles to multimodal transport and logistics services which may exist can be grouped into (a) infrastructure and technologies, (b) security and safety, (c) facilitation, (d) legal aspects and (e) market access.

10.3.2 Liability of Carriers

Air Way bill evidences a contract which, as noted earlier, is governed by the Warsaw Convention. The carrier is fully liable while cargo is in its charge, both at the airport as well as when the cargo is being held for loading, delivery or transshipment. It is its contractual duty to carry cargo safely and without delay by exercising due care and taking all necessary measures to avoid loss.

The Warsaw Convention provides for maximum liability of 250 Gold Francs per kg. of gross weight lost or damaged or higher declared value as agreed upon between the carrier and the shipper. One Gold Franc is equivalent to 65.5 milligrams of gold of 900 milisimal fineness.

National laws enacted on the basis of Warsaw Convention provide for liability mainly in terms of US dollars. The Convention states that the carrier cannot reduce its liability from the Warsaw Convention provision.

Under the Convention, the carrier is to issue a copy of Air Waybill at the destination to the consignee and give delivery against surrender of this COPY. In case of non-delivery of cargo, the consignee is to lodge complaint to the carrier not later than 14 days of the arrival date or the expected arrival date. In case of damage, consignee is to give notice to the carrier within seven days of the receipt of cargo. Where carrier has not accepted the claim, case against the carrier is to be filed within two years of non-defective delivery.

10.3.3 Bailment

A bailment is the relationship created by the transfer of possession (not title) of an item of personal property by one party called the bailor, to another party called the bailee, for the accomplishment of a particular purpose. Whenever you transfer, lend or store personal property to, or for, another you should think bailment.

Common Carrier is an enterprise that agrees, for a fee, to transport goods for anyone who applies, provided the goods are lawful and fit for shipment. It enforces reasonable rules and regulations for the conduct of its business. Example it may enforce rules stating how goods must be packed. It can charge an amount negotiated with the Bailor or, if the carrier is regulated by the government, charge the scheduled rate.

- **Bailment for hire:** A bailment for hire arises when the bailor, for a fee, provides personal property (such as a car, truck, tool, machine, or other equipment) for use by the bailee.
- **Bailment's for Sale:** Goods may be sent on consignment by a manufacturer to a retailer.



Note In all legal systems, the peculiar liabilities imposed on carriers extend only for the duration of the carriage, that is, from the time the goods are delivered to the carrier for shipment until the carrier has taken all reasonable steps to deliver them to the consignee.

10.3.4 Loss Prevention

The broad scope of the transporting freight makes loss prevention an issue. The transportation provider has one all-encompassing job of maintaining the goods from one location to another location. Of course, there are many risk factors associated with this task. Loss prevention activities include plant inspections to assess transportation risks in exportation products and review of processing techniques, packaging, freezing methods, controls, material handling, proper stuffing and stowage, in order to reduce risks and eventual claims.

Operation losses are the cost of conducting business. Equipment fails, employees make mistakes, and breakdowns happen. These mishaps are responsible for contributing to business loss but they are a built-in expense. A different, more controllable category of loss is asset and property theft. Employee pilferage is known to be the most common reason for theft within a company. Naturally, there are industry-established precautions to curb these statistics.

Having a strong employee structure keeps the checks and balances to make certain people are accountable for their behavior. Sometimes, hiring an outside consultancy specializing in loss

Notes

prevention is a strategic business move. As a part of their program, they make sure that no one has too much freedom away from accountability. Checking employee backgrounds is a major part of creating the right team of trustworthy people.

10.4 Leasing of Containers

Containers are normally taken on lease by carriers from manufacturers of containers. If containers are taken on lease for just one voyage, it is called Trip Lease and if they are taken for long period such as 2 to 5 years, it is called Long-term Lease.

Another system is the Financial Lease, which works like the hire purchase system. A fixed amount is paid by the lessee at fixed intervals and at the lease period, the ownership of container is transferred to the leased.

10.4.1 Present Procedure of Clearance of Goods at Ports

- The Shipping lines/steamer Agents/carriers/Consol Operators file the Import General Manifest (IGM) in accordance with Section 30 of the Customs Act, 1962. After filing the IGM and on arrival of the goods, Custom House Agent/Importer files Bill of Entry (cargo declaration) in terms of Section 46 of Customs Act, 1962. The first stage for processing a Bill of Entry is noting/registration of Bill of Entry (B/E). The B/E is then forwarded to the concerned Appraising group in the Custom House dealing with the commodity sought to be cleared.
- The assessing officer in the appraising group assesses the duty liability, taking due note of any exemption or benefits claimed by the importer. Necessary checks regarding any restriction or prohibition on the goods imported are followed. In case of doubt, the officer may give an examination order in advance of finalization of assessment. Otherwise, the B/E is finally assessed and the importer deposits the duty calculated with the nominated banks.
- After assessment the B/E is passed on to the Shed Appraiser/Superintendent for examination of goods along with the B/E. The Shed Inspectors/examiners examine the goods and enter their report on the B/E with signature of the importer/CHA in token of examination in their presence. After completing the examination of the goods, the shed Appraiser/Superintendent would give order for "Out of Charge".
- However, in rare cases, if some discrepancy is found between the declaration and the result of examination of cargo, the Assistant Commissioner/Deputy Commissioner (AC/DC) revises the assessment on the basis of examination report.
- After issuance of Out of Charge order on the B/E, the importer presents the same to the Custodian who in turn issues the Gate Pass after Verification of correctness of Bill of Lading and number of packages. The importer/CHA presents importer's copy of the B/E and the Custodian Gate Pass to the Customs Officer at the gate while taking the goods out of the Customs area.
- As regards exports, Shipping Bills are required to be filed along with other documents such as invoice, Application for Removal (ARE), packing list, etc. The Assessing Officer in the export department checks the value of the goods, classification, rate of duty and others with regards to different provisions and the Foreign Trade Policy and related documents.
- After the Shipping Bill is passed by export department, the exporter presents the goods to the Shed Appraiser (Export) for examination. The examination is carried out under supervision of Shed Appraiser/Superintendent (Export) and after examination, officer gives a "Let Export" order, after which exporter may load the goods into vessel/aircraft under supervision of Customs Officer.

Present Procedure of Clearance of Goods at CFS

Notes

The Main function of CFS is receipt, dispatch and clearance of Containerized Cargo, up-to-date inventory control and tracking system to locate containers/cargo. The goods received at ports are brought to CFS and stacked in CFS after verification of the seal by Customs Officers. In respect of import consignment, the Steamer Agents/liners/Importers desiring to take the consignment to CFS, file Import General Manifests in the port.

After obtaining the permission from the AC/DC, the Container moves to CFS under Customs escort or under bond and bank guarantee. The CFS allows de-stuffing of the goods. The CHA/importer files the Bill of Entry at Customs House and then Customs formalities of assessment, examination and payment of duty are completed. Thereafter, Customs gives "Out of Charge" and the Custodian releases the goods from CFS by issuing a Gate-Pass.

In respect of exports, the goods are brought directly to CFS under a Shipping Bill. The export cargo in Less than Container Load (LCL)/Full container Load (FCL) is received by the Custodian of CFS for safe custody. After stuffing of the goods, Container/Customs Bonded Truck (CBT) is sealed by the Custom Officer and the same is removed from CFS for export through the desired Port.

Storage of Containers

The exporter should have the following information for the storage planning:

1. The type of container suitable for the cargo.
2. The exact weight and measurement of the cargo to be loaded and its packaging.
3. Exact inside dimension and permissible load limits of the containers.

The plan for packing should be developed on the basis of the factors outlined above as this will decide the kind of packing the exporter should use. The following rules should be followed while packing the cargo:

1. The different types of packages (for example, card board boxes and wooden boxes) should be stacked separately.
2. The container should be lined with paper or foil in the case of specially sensitive goods.
3. The container should be made odourless or properly washed out in case the goods are sensitive to odour.
4. The packing in the boxes should be carefully checked before stuffing them into container.
5. The exporter should not pack together:
 - ❖ The wet goods with dry goods.
 - ❖ Goods with protruding parts, sharp edges or corners with goods in comparatively soft packaging such as sacks or card board boxes.
 - ❖ Dusty goods with dust sensitive goods.
 - ❖ By placing the heavy packets on light packets.
 - ❖ Odour emitting goods with odour sensitive goods.

Notes

Precautions for Packing the Containers

The exporter should take the following precautions while sending the goods through container. The container should be thoroughly got checked to ensure that:

- There are no holes or cracks in the walls and roofs
- Its doors can be easily operated
- Locking doors and handles function properly
- There are no placards/lables pasted of the previous cargo.
- Container is waterproof.
- Container is dry from inside
- Container is clean, free of dust and cargo residue.
- Container should be odourless in the case of odour sensitive goods.
- Checking of Container after Packing

The exporter should check the container once the cargo has been stuffed into it to ensure the following:

- A copy of the packing list is fixed at an easily visible position inside the container.
- The quarantine regulations should be complied with in case the goods are being shipped in wooden packaging to Australia or New Zealand or a country having similar quarantine regulations. A copy of the quarantine certificate issued by the appropriate agriculture authority should be pasted inside the container.
- Door handles are secured by seals to reduce the risk of pilferage.
- In case of open top containers, it should be ensured that the tarpaulins and the ropes are correctly fixed.

Losses Occurring during Movement of Materials

- *Marine Loss:* Occur from the time the Bill of lading is issued by the shipping company up to the time the shipping company hands over custody and control. It is the difference between stated quantity on the bill of lading and quantity discharged when shipping company turns over custody and control.
- *Port Loss:* Occur at the port.
- *Transit Loss:* Occur during transportation from port to destination.
- *Warehouse Loss:* Occur in the warehouse during storage
- *Distribution Center Loss:* Occur during distributions or at distribution center.

Use of Material Handling and Storage Equipment to Avoid Losses

In any industrial process, the product being manufactured passes through various phases and it needs to be transported from place to place. This could involve processes such as transporting of raw material to the machines and then shifting the machines from one station to another station and finally to the store or warehouse. This involves the use of material handling equipment. Simplest form of material handling is to take material from one place to another place manually or with the help of worker. In large production setups, where the production rates are high and the product to be handled is such that manual transportation is not possible, sophisticated material handling systems would be required.

These material handling equipment can be generally classified as:

Notes

- Transport equipment is used to move materials from one location to another. It includes cranes and industrial trucks.
- Positioning equipment is used to handle material at a single location, so that it is in the correct position for subsequent handling, machining, transport, or storage. It includes hoists and lifts. Unlike transport equipment, positioning equipment is usually used at a single workplace.
- Unit load formation equipment is used to maintain integrity when handling a single load during transport and for storage. It includes pallets, bags and skids.

10.5 Container Leasing Practices

Containers are taken on lease by carriers from container manufacturing companies or leasing companies who own containers. There are four types of leasing arrangements.

1. **Trip Lease:** Trip lease or short term lease. The lease is for one voyage or one trip. (Voyage implies to and fro trips and trip connotes one leg only).
2. **Long Term Lease:** Containers are usually leased for a period of 3 years to 5 years.
3. **Financial Lease:** This is more of a hire-purchase or instalment purchase scheme rather than a lease as in this case at the end of the term for which containers are taken on financial lease, the ownership of the container is transferred to the lessee.
4. **Master Lease:** In this case, one shipowner concludes a deal with a container leasing company for a period of usually 1-2 years whereby he guarantees that a minimum number of containers will always be under his lease from the leasing company. Against this guarantee, the container leasing company also assures the ship owner that a minimum number of empties will be made available to the ship owner at the various ports as agreed upon between the two contracting parties.

Lease rent is charged at per day container. The rate depends upon the supply and demand situation. The International Container Lessors Association has drawn up forms of contract to assist the working of the leasing market. The rent component can also include insurance premium for loss/damage to a limited extent.

Users normally prefer to lease a container than owning it. This is more true of shipowners who use bulk of the containers available. Owning involves investment of capital, maintenance, workshop management etc., but owning containers provide self-reliance to shipowners and also source of advertisement for their lines wherever containers move.



Caution There is Institute of International Containers Lessors (IICL), New York, which covers the largest nine lessors, of which three largest members control 63 percent of the leased fleet of containers and 27 percent of the total owned and leased units worldwide. (These figures change from time to time).

Self Assessment

Fill in the blanks:

11. The across the countries may take place by sea, by air, by road and rail or through multi-modal transportation.

Notes

12. The party who undertakes to carry the goods for payment e.g., the shipping company or the airways, is called the
13. is a fully Web-based system to be used to control a door-to-door transport where several transport modes are involved.
14. A is the relationship created by the transfer of possession (not title) of an item of personal property by one party called the bailor, to another party called the bailee, for the accomplishment of a particular purpose.
15. The main function of is receipt, dispatch and clearance of Containerized Cargo, up-to-date inventory control and tracking system to locate containers/cargo.

10.6 Summary

- The use of containers has not only facilitated but has also revolutionized the carriage of goods among the developed countries.
- The exporters in developing countries are also making greater use of containers for the transportation of the goods.
- Train or road to the seaports carries the containers, where they are loaded on the ships for onward transportation to their destination.
- The exporters do not need to carry the cargo to the seaports any longer rather they can approach the container freight station or the Inland Container Depot (ICD) to book the cargo there for transportation to the destination.
- The custom clearance of the cargo is provided at ICDs and in the process, the exporters are able to save lot of time.
- The packing of cargo in a container can be done either in the container depot or in the factory of the exporter.

10.7 Keywords

Container Management Systems: They are a New Dimension in Supply Chain Execution (SCE) and Collaborative Logistics Technology. The basic concept is to develop a responsive system for providing vital information inputs to decision makers and consignees for Efficient Asset Tracking and Control of the goods in transit.

Conventional Liner Services: It include additional stops. These stops are concentrated in the vicinity of the two end points. Each extra stop in a service attracts additional cargo from another geographical area and thus increases revenue. The purpose of the additional stop may be to achieve sufficient loads or enable a viable increase in frequency of service.

Open Sided Containers: These containers are designed to accommodate specific commodities such as plywood, perishable commodities and livestock.

Shuttle Service: Shuttle services i.e. liner services between two points without intermediate stops. Shuttles are extremely efficient and therefore produce services at the lowest cost. Uncomplicated production makes them largely invulnerable to internal production disruptions. Their disadvantage is their rigidity.

10.8 Review Questions

1. What do you understand by term 'containerisation'? Discuss the genesis of containerisation.
2. Briefly discuss the development of containerisation in Indian scenario.

3. Classify the container in various categories. Also identify their applications examples. Notes
4. Write a brief note on container leasing practices.
5. What do you understand by shuttle service?
6. Highlight the importance and scope of container management system.

Answers: Self Assessment

1. Containerisation
2. Transportation of Goods
3. general
4. Stuffing
5. risk
6. five
7. Container Management Systems
8. inland
9. freight
10. decision makers
11. carriage of goods
12. 'carrier'
13. TCMS (Transport Chain Management System)
14. bailment
15. CFS

10.9 Further Readings



Books

David Blanchard, *Supply Chain Management: Best Practices*, John Wiley and Sons, 2010.

Raji ismail, *Logistics Management*, Excel books. 2008.

S.K. Bhattacharya, *Logistics Management*, S. Chand & Company Ltd. New Delhi, 2008.

Upendra Kachru, *Production and Operations Management*, Excel Books, 2007.



Online links

http://www.slideshare.net/subhash_ae/a-brief-presentation-on-containerisation-presentation

http://www.exporthelp.co.za/modules/16_logistics/containerisation.html

Notes



Case Study

Containerised Cargo: Safely into the Future?

The case that I am going to discuss today could have come out of the pages of detective fiction. It is, however, a true story which highlights the fact that containerisation has certainly not meant an end to claims for the Cargo Underwriter.

Setting the Scene

In this case, the insured shipment comprised readymade garments, which were sold by a shipper in South-East Asia to a buyer in Durban, South Africa.

The goods were sold on a "DP at sight" (documents against payment) basis. Freight was prepaid and insurance was taken out by the shipper in South-East Asia. Ten separate Certificates of Insurance were issued, for a combined insured value in excess of 4 million US dollars.

The goods were packed into ten 40' containers. The containers were loaded onboard two vessels at a South-East Asian port. Ten separate Bills of Lading were issued. The vessels proceeded to Singapore, where the containers were transhipped onto five vessels for onward carriage to Durban.

The vessels arrived at Durban, and berthed at the Container Terminal. In every case, the containers were landed from the vessels shortly after arrival.

The containers were uplifted from the port by privately owned transport, within one week of having been landed, and were delivered to an address outside Johannesburg, 600 kilometres from Durban. The empty containers were turned in to the premises of various privately owned container depots in Johannesburg.

A claim for the theft of the entire shipment was instituted by the shipper. We were instructed by the Insurers some four months after the alleged theft had taken place.

Our starting point was to establish contact with the purported buyer.

The South African Buyer

The buyer's premises were located in a small building situated within an industrial area near Durban. The building was in a state of considerable disrepair.

After some difficulty, contact was made with the owner of the company. He repeatedly refused to speak to us. However, after gentle persuasion, he eventually stated that:

1. He had not ordered the goods in question, nor had he ever heard of or had any dealings with this particular shipper;
2. The first time he had heard about the goods was when his bankers had contacted him and advised that they had received documents relating to the goods from the shipper's bankers;
3. He had instructed his bankers to return the documents to the shipper's bankers;

He refused to say any more, and referred us to his lawyers. His lawyers refused to speak to us.

Although we were less than satisfied with his statement, we found no firm evidence during our investigation to suggest that he had taken delivery of any of the containers or goods.

Contd...

The Shipping Line's Durban Agents

Upon contacting the shipping line's Durban agents, we were advised that they were not prepared to comment, or to provide any information whatsoever. We were further advised that the matter was in the hands of their liability insurers.

The Banks

We turned our attention to three local banks, which had been named as the Consignees on the various Bills of Lading. Assuming that original Bills of Lading had been presented to the shipping line's agents for release of the containers, it followed that someone must have paid for the goods in order to obtain the original Bills of Lading from the banks.

The banks advised us that the original Bills of Lading, Supplier's Invoices, Packing Lists and Certificates of Insurance had been returned to the shipper's bank.

There had been a considerable exchange of correspondence between the banks and, ostensibly, the purported buyer, well after the containers had been removed. The correspondence related to requests by the purported buyer for extensions and/or amendments to the terms of payment.

We concluded that the shipping line's Durban agents had apparently released the containers without production of the original Bills of Lading.

The Container Terminal

A Container Terminal Order (CTO) must be issued for containers to be released by the Container Terminal.

During the investigation, meetings were held with the Administration Manager at the Container Terminal. He stated that to his recollection, all the CTO's pertaining to the containers in question had been issued by the shipping line's local agents in Durban.

He was unable to provide us with copies of the CTO's or indeed any other documentation relating to the containers. He explained that he simply did not have the documentation, that he assumed this had been taken by the Police in the course of their investigation, and that no copies had been left on file.

He stated that the containers appeared to have been released in the normal manner.

Customs Documentation

The Bill of Entry is a Customs clearance document, which is framed by the importer or his agent and presented to Customs & Excise.

The requirement for presentation of these documents is to prevent the release of containers before Customs duties have been paid.

We obtained copies of the Bills of Entry issued in respect of the containers, and noted the following:

1. Each Bill of Entry contained a Customs Export stamp.
2. The remover was shown as a company based in Mozambique.
3. The Bills of Entry were signed, ostensibly, by the South African buyer.
4. All the Bills of Entry were in the same handwriting and issued on the same date.

In discussions with representatives from the Department of Customs & Excise, it was confirmed to us that the Bills of Entry were fraudulent. We were advised that the Department was conducting its own investigation into the matter.

Contd...

Notes

We concluded that the Bills of Entry had been fraudulently prepared and presented for the sole purpose of obtaining release of the containers from the Container Terminal in Durban.

The Road Transport Brokers

In each and every instance, the instructions for delivery of the ten containers had originated from a single transport brokerage company in Durban.

The transport brokers advised us that their instructions had been received from an individual who we will refer to as "Mr X". The transport brokers maintained that the instructions had been given telephonically, and that they had never actually met Mr X. They also maintained that no written instructions had been received, and that the deliveries had been undertaken on a "cash on delivery" basis.

The transport brokers provided us with copies of their individual instructions issued to sub-contractors who were, variously, other transport brokers or physical road transport companies.

This practice is quite customary in South Africa. A transport broker will receive an instruction from an importer or his agent, after which that broker may in turn subcontract to another transport broker who will in turn subcontract to the physical road transport company, each party taking his percentage at the various stages. It is not uncommon for five or six different transport brokers and/or road transport companies to be involved in the collection and delivery of a single container.

The transport brokers produced a copy of a cash cheque in the amount of ₹ 50,000 which was apparently given to them as payment for the delivery of the containers. The cheque had been presented to the bank and dishonoured.

The transport brokers advised us that they had subsequently met with an unknown party in a parking garage outside Johannesburg, and collected the amount of ₹ 50,000, in cash, in a brown paper bag.

The transport brokers maintained that they had heard no more from Mr X after the deliveries of the containers had been effected. They supplied a mobile telephone number for Mr X. This was found to have been disconnected.

The transport brokers stated that, in their opinion, the goods were long gone, and had been sent exactly where they were intended to be sent.

The Scene of the Crime

We attended at the address outside Johannesburg to which the containers had been delivered. The address was that of a private house.

The owner of the house was interviewed. He confirmed that Mr X, who drove a red Porsche sports car, had rented the house from him. Mr X had subsequently disappeared without having paid the rent, and also after having removed some of the more expensive fittings from the house.

The owner was also aware that at least one shipping container had been delivered to the house. Cardboard cartons had been removed from the container and stacked against the house. The cartons had subsequently been removed by a fleet of light delivery vehicles.

The owner confirmed having reported the matters of outstanding rent and theft of fittings to the Police.

Contd...

Police Investigation

Initial attempts to contact the two Police detectives investigating the case were unsuccessful. We were subsequently advised that following a disciplinary enquiry, both detectives had been transferred out of the Police unit responsible for investigating matters of this nature.

A special Police task force, financed by local business interests, had been set up with a brief to investigate not only this alleged theft but also various other similar and possibly connected thefts of containers. We met with detectives assigned to the task force in Johannesburg.

They advised us that container theft in South Africa, as in other parts of the world, was believed to be the work of organised crime syndicates, some with international links. Outwardly respectable businessmen, Customs officials and policemen were believed to be involved in the criminal activities of the syndicates.

The detectives advised us that it would not be in their interests or ours for them to share any information with us. All the detectives were prepared to say was that Mr X was known to them, and was being sought by them in regard to the matter of the ten containers.

Restatement of Facts

It is clear from the following restatement of facts that the movement of the containers was orchestrated as follows:

1. The shipper appeared to have believed that he had sold the goods to a buyer in Durban, South Africa. Freight was prepaid and insurance was taken out by the shipper.
2. The purported buyer was intended to receive the relevant original documentation on a "cash against documents" basis, the original documents being held by three South African banks
3. The goods were packed into ten 40' containers which were loaded onboard two vessels in South-East Asia. The containers were transhipped onto five vessels at Singapore for onward carriage to Durban.
4. The containers were landed at the Container Terminal in Durban. The initial movement of the containers was controlled by the shipping line's Durban agents.
5. The initial sale between the shipper and the purported buyer (if there was in fact a sale, which is doubtful) apparently fell through, and the shipper intended that the containers should be held in bond pending the re-negotiation of the sale.
6. During these negotiations, the containers were uplifted by various road transport companies and delivered to premises outside Johannesburg.
7. Fraudulent Customs documents were prepared and presented to the Container Terminal in order for the containers to be uplifted.
8. The original sale documents, specifically the original Bills of Lading, were never released by the banks. There was evidence to suggest that the shipping line's Durban agents had released the containers without the presentation of the original Bills of Lading.
9. In every instance, the road transport instructions were issued by a single road transport brokerage, which was in turn acting in accordance with verbal instructions received from a Mr X. The deliveries were all undertaken on a "cash on delivery" basis.
10. There was no firm evidence to suggest that the purported buyer had received the goods. Similarly, there was no firm evidence to suggest that he was directly involved in the disappearance of the containers.

Question:

Discuss the importance of custom documentation in detail.

Notes

Unit 11: Inland Container Depots

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11.5 Constraint in Growth of ICDs

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Objectives

After studying this unit, you will be able to:

- Explain ICD Roles and Functions
- Discuss Export Clearance at ICD.
- Describe Clearance Procedure for Imports
- Explain CONCOR
- Discuss CONCOR and ICD

Introduction

The concept of ocean-going containers was introduced in India for the first time in 1968 in a seminar held jointly by the Indian National Shipowners' Association (INSA), Directorate General of Shipping, the Shipping Corporation of India Ltd. (SCI) and the All India Shippers Council (AISC) at Bombay.

In early 1970s, the SCI acquired the first semi-container ship with three holds designed to carry containers along with two holds full general cargo. Other shipping companies like Scindia Steam Navigation Co. Ltd. and India Steam Navigation Co. Ltd. followed on the steps of the SCI. India Steamship Company went ahead to acquire a small cellular container ship.

In 1971, Cochin port received containers for the first time from a conventional general cargo vessel of the American President Lines. They were handled by the ship's derricks.

In 1973, the American President Lines began scheduling their cellular feeder container ships to Mumbai and brought the necessary handling equipment with them. The action was repeated by the lines of European and other countries who also thereafter started scheduling their cellular ships to Indian ports.

However, India began to seriously adopt containerisation only in 1978. Major ports like Mumbai, Cochin, Chennai, Haldia/Calcutta commenced to equip themselves for handling container ships and containers in the appropriate way.

Shippers and consignees also responded to the opportunities and benefits in containerisation. The buyers of Indian goods abroad stipulated in their letters of credit that the goods should be containerised. Hence, despite the need for heavy investments and numerous problems in smooth flow of goods, India was forced into containerisation to stay with the dominant trend in the world economy.

11.1 Inland Container Depot (ICD) – Roles and Functions

The full benefits of containerisation can be obtained only if the containers are permitted to move to the locations of the original cargo generation points. The Government of India decided to set up Inland Container Depots (ICDs) which are also called dry ports. Shipping formalities can be completed in ICDs for containerised cargoes instead of at the exit gateway port.



Note Inland Container Depots are interfaces between connecting modes of transportation.

An Inland Container Depot is an organisation offering a total package of activities to handle and control container and general cargo flows between road, rail and waterways, and vice versa, resulting in maximum service for inland transportation at minimum costs.

Normally ICDs provide the following services:

- (i) **Handling of Containers:** Handling of containers from road, rail and barges to a temporary storage area container yard.
- (ii) **Intermediate Storage:** Intermediate between the various transportation modes. Special containers and or cargo may require additional provisions, such as refrigeration services and special areas for dangerous cargo.
- (iii) **Receipt and Delivery of Containers and General Cargo:** This may include activities such as weighing, inspection of seals and damages, sticker and safety plate control and container information control. Stuffed containers may be received from the satellite Container Freight Stations (CFS) in ready condition to be transported to the exit port. Shippers may also directly bring Less than Container Load (LCL) cargoes for the purpose of consolidation and despatch.
- (iv) **Cargo Consolidation and Distribution:** If the container cannot be received or delivered directly at the final consignee's door. In this case, containers are stuffed with or destuffed for LCL, depending upon the direction of the cargo movement prior to despatch.
- (v) **Depot Functions, for the Storage of Empty Containers:** Space may also be required for temporary storage of loaded containers awaiting movement out of ICD.
- (vi) **Other Facilities** include container cleaning services, pretrip trials of reefer containers to check the function of refrigeration equipment, maintenance and repair services for containers, container handling equipment, refrigeration equipment, road chassis, etc. In this respect, ICD should make itself a self-sufficient unit.
- (vii) **Custom's Clearance Activities:** at inland terminals could help to decrease the dwell-time of containers in deep-sea ports. These activities include checking of LCL cargo prior to stuffing or after stripping, checking container seals, assessment and valuation of cargoes, perusal of container manifests, and so on. The transport of containers under bond to ICDs

Notes

from deep sea ports is a necessary feature of well-developed multi modal transport systems because this has proved to be a time and cost saving function.

- (viii) **Physical Distribution Services:** These can be provided economically at or close to the ICDs. Garments can be ironed and packed, prices tagged on consumer goods, liquids in bulk can be bottled—in short, a variety of cargo-related services to finished goods can be placed near the ICD itself. For agricultural products, ICDs may provide refrigeration plants and warehousing facilities to prepare meat, fish and vegetables for export.

Guided by economic and strategic considerations, each ICD may decide what functions it should have.

Indian ICDs perform many of the possible functions outlined above. These include stuffing, destuffing, locking, sealing; providing trailers chassis, railway flats, repairs, handling equipment, storage, facilities for reefer, customs examination and processing of customs documents, issuance of combined transport documents by carriers.

ICD is a declared Customs Area for the purpose of import and export but only limited facilities of noting of shipping bills, valuation and examination of export cargo are afforded at ICD. Exports, however, are deemed to be effected from the gateway port only.

ICDs are connected with gateway ports. Following are examples of some of the ports and the ICDs connected to them.

Within 24 hours of landing, the containers consigned to the ICDs are dispatched by rail. At the ports, ICD containers and transshipment containers are moved on priority basis. Similarly, stuffed containers, on completion of customs formalities at the ICD, are dispatched to the terminal port within 24 hours.

The railways provide the transport link between the ICDs and the gateway ports.

11.2 Container Freight Stations (CFS)

CFS have been established to speed up export cargo and to specially help small exporters whose consignments are less than container (LCL) loads.

The CFS has facilities of modern godown accommodation under export supervision. Facilities of banking, custom examination, clearance, safe handling, stuffing, sealing and transportation of containers are available. Both import and export consignments are handled here.

Location of ICDs and CFSs is regulated by the Ministry of Commerce of the Government of India. While this ministry is encouraging liberalisation and competitiveness with a view to making transport more attractive and customer friendly, it must maintain the inter regional balance. CFSs and ICDs should not be concentrated only in a particular region; they must be spread throughout the country depending upon present and future potentiality of cargo traffic.

The supportive network of surface transport with the location of Container Freight Stations and Inland Container Depots has to be in the hinterland. The location depends upon the potentiality of generating volume of export cargo or where distribution of import-cargoes can be easily facilitated.

Further, CFSs and ICDs should be complementary to each other. CFSs are cargo aggregating points, which should conveniently feed the ICDs for carriage to gateway ports in sizable quantities and over long distances. Conversely for imports, the goods may be brought over the same route to an ICD for distributing to the various users.

11.3 Maritime Container Rates (Freights)

Notes

General practice is to formulate individual rates by container type capacity, actual origin and destination of the merchandise.

Though rate will embrace the inland transportation cost known at the time of despatch, embracing collection and terminal handling expenses, it will usually exclude customs clearance charges, demurrage, etc. This practice applies to FCL traffic. Some large multinational companies own/lease ISO containers. They are usually of a specialised type offering a two-way traffic flow. The tariff for such traffic is usually specially negotiated contract rate.

LCL traffic rates are calculated on weight or cubic measurement basis, whichever produces greater revenue. They naturally reflect the origin and destination of such merchandise together with collection and terminal handling charges. For consignment such as livestock or indivisible loads requiring heavy lifts, additional charges are raised.



Caution Maritime container rates are very competitive and this mode of transport now constitutes a substantial volume of deep sea world general merchandise cargo.

11.3.1 Export Clearance at ICDs

At ICDs the exporter is required to file the shipping bill in seven copies:

1. Original, 2. Duplicate, 3. Quick drawback payment scheme, 4. Exchange control Copy Exporters, 5. Copy, 6. Transference copy

The exporter should mention the name of 'Port of Exit' and serial numbers of container. The exporter should obtain in advance, space availability certificate from the Railway/Combined Terminal Operator.

- (i) **Checking Details of the Shipping Bill:** The shipping bill should mention details of goods, their classification, name of the port of exit, identification mark, number of containers, weight and value of goods. Contents of cargo should be declared and proper statistical code number must be given. GR forms should accompany, without fail, the shipping bills.
- (ii) **Scrutiny of Shipping Bills:** Duly completed shipping bills are put in the Noting Box provided at the ICD. The receiving clerk after noting them scrutinises them and accompanying documents. The receiving clerk will give a running serial number on shipping bill if no discrepancy is found. Otherwise, these may be returned for resubmission after correction.
- (iii) **Classification and assessment:** The Central Registration Unit of the ICD completes the classification and assessment. The rate of duty is filled by appraisal department. The original shipping bill is retained and the balance six copies are handed over to exporter for completion of examination.
- (iv) **G.R. Formalities:** A full set of GR forms has to be submitted along with the shipping bills. The full value of export will be verified on the GR form.

The assessing officer will retain the original GR form for release to the RBI. Duplicate copies are retained at ICD. Shipment certificate on the GR form shall be furnished after custom examination of the export cargo and sealing of container by proper officer at ICD. Duplicate copies are then released to the exporter for his use.

Notes

- (v) **Examination of Goods:** Custom Inspector/examiner conducts the examination of goods, keeping in view the restrictions in force under Acts/Rates and Regulations. After examination, goods are shifted into the container and same are sealed by the custom seal. The customs officer records on the shipping bill
- (a) Quality of goods loaded
 - (b) Number of packages shut out.
- The exporter at this stage is to prepare and present an invoice and container-wise packing list (both in four copies) indicating
- (a) Number of packages with marks and numbers.
 - (b) Description and total quantity net weight packed in each container. The Appraiser/ Superintendent/Inspector/Examiner with the details presents these two documents for certification.
 - (c) Duplicate copy of the shipping bill is retained at the ICD and exchange control copy is returned to exporter.
- (vi) **Transit to Gateway Port/Port of Exit:** The two transferee copies are sealed in an envelope for custody of the Railways who are responsible for subsequent presentation to the customs officer at the Gateway Port Exit Port.
- (vii) **Procedure to be followed at Exit Port:** The sealed containers are allowed to be exported in preventive supervision on verifications with the seal being intact, without any further examination. However, if seal is found tampered with, examination may be done at the port two.
- ❖ The customs officer at the port will be entitled to open and examine the contents of any container, if otherwise warranted.
 - ❖ The preventive officer at the port will endorse the two transference copies of the shipping bills regarding the containers being intact and custom seal being intact, and adds his dated signature.
 - ❖ The steamer agent shall be required to file the Export Manifest in duplicate regarding cargo containers with the container unit of export department of the customs house.
 - ❖ After that, shipment transference copies of the shipping bills shall be sent to ICD within 48 hours of shipment.
- (viii) **Endorsement of Shipment:** from gateway port on quick drawback payment section copy of shipping bills.

The exporter, after enquiring from the export unit of ICD regarding receipt of transference copies shall obtain certificate to this effect on the quick drawback copy of the shipping bill and can claim drawback from Quick Drawback Payment Section.



Did u know? The quick drawback copy of the shipping bill is valid for a period of 90 days from the date of shipment i.e., loading of goods in container. In case shipping bills are not submitted within stipulated period, they shall have to be followed up with Residency Drawback Section.

Clearance Procedure for Imports

Notes

- In addition to the vessel's Import General Manifest, the Shipping Agent should submit a sub-manifest in duplicate exclusively for the containerised cargo.
- The Shipping Lines or the shipping Agent should file the transshipment application (in triplicate) for transshipping the containers by rail/road and file the required bond for transshipment.
- After unloading of the container at the port of entry, the particulars of the containers should be checked with the manifest filed and container secured with customs seal. For this purpose, Import Noting Department should send two copies of the submanifest to the docks soon after receipt.
- The fact of loading of containers should be endorsed by the Preventive Officer on all the three copies of the transshipment permit.
- The Railway/Road Carriers authorities are responsible for the carriage of transshipment permit copy and the two copies of the manifest with the container.

They must hand over these documents to the Customs authorities at the ICD.

At the ICD

- On arrival of the containers at the ICD, the Railway Road Carriers will present the sealed cover to the Customs Officer. The particulars of the containers, seals etc. shall be checked with reference to the transshipment permit received followed by the endorsement of the transshipment permit.
- On de-stuffing of the containers at the ICD, which is carried out in the presence of the Customs Officer, a representative of the Railways or Road Carriers, the packages should be tallied with the documents and marks and numbers compared with reference to the manifest.
- The clearance of the goods for home consumption from ICD will be on the basis of Bills of Entry (B/E) to be filed by the Importer at the ICD.
- The BE's details is noted against the copy of the submanifest followed by the duty assessment procedure involving classification, assessment, payment of duty and examination.

Self Assessment

Fill in the blanks:

1. The concept of ocean-going containers was introduced in India for the first time in
2. In early 1970s, the acquired the first semi-container ship.
3. are interfaces between connecting modes of transportation.
4. CFS have been established to speed up export cargo and to specially help small exporters whose consignments are than container (LCL) loads.
5. On arrival of the containers at the ICD, the Railway Road Carriers will present the sealed cover to the

Notes

6. On of the containers at the ICD, a representative of the Railways or Road Carriers, the packages should be tallied with the documents and marks and numbers compared with reference to the manifest.
7. The clearance of the goods for home consumption from ICD will be on the basis to be filed by the Importer at the ICD.
8. The Carriers authorities are responsible for the carriage of transshipment permit copy and the two copies of the manifest with the container.
9. The Shipping Lines or the shipping Agent should file the application (in triplicate) for transshipping the containers by rail/road and file the required bond for transshipment.
10. Duplicate copy of the is retained at the ICD and exchange control copy is returned to exporter.

11.4 Container Corporation of India (CONCOR)

With the increase in containerisation, a separate undertaking under the Indian Railways to manage the ICDs and CFSs became necessary. While ICDs provide all facilities for effecting containerised shipments, CFSs are limited only for stuffing into and destuffing of cargoes from the containers.

The Container Corporation of India Ltd. was constituted as an autonomous public sector undertaking under the Ministry of Railways in March 1988. The basic objective of CONCOR is to organise multimodal transport logistics with prime task of facilitating the nation's foreign trade. Its operations are directed towards efficient, economical and expeditious handling and transit of containerised goods, relating to both international and domestic trade traffic.

It works with various agencies and offers services including warehousing, road and rail transport, palletisation and packing, simplification of documentation and custom formalities. CONCOR accepts containerised cargoes, issues waybill and coordinates with railways to carry containers to gateway ports and vice versa. They are the prime coordinating agencies to container traffic.

Setup with an authorised capital of 100 crores and a paid up capital of 65 crores, CONCOR started functioning from March 1988. CONCOR now functions as a PUBLIC COMPANY under the Ministry of Railways.

11.4.1 Activities of CONCOR

- (i) Spearhead the container revolution in India.
- (ii) To build and operate Infrastructure and organise Rail and Road linkages for accelerated inland penetration of International containers in the country.
- (iii) To set up and manage Inland Container Depots (ICDs) and Container Freight Stations (CFSs) all over the country.
- (iv) To act as an effective liaison with all the agencies involved with containerisable trade in India so as to provide comprehensive services for door-to-door movement of international cargo.

11.4.2 Objective of CONCOR

CONCOR operates on the following objectives:

- (i) To develop inter-modal logistics, infrastructure for the fast, efficient and economical transportation.

- (ii) To establish a Network of ICDs/CFs/IPSCTs to facilitate national and international trade.
- (iii) To offer a single window service, co-ordinating all connected departments/sections.
- (iv) To function as a multi modal transport operator (MTO).

Notes

11.4.3 Performance of CONCOR

- CONCOR took over seven ICDs on 1st November 1989 from Indian Railways. Within a short span of time, it made substantial progress. The company has, for the first time, started business of bonded warehousing at Whitefield in Bangalore from February 1996.
- The 1400 sq. m. area bonded warehouse capacity is utilised 100 percent. CONCOR has also pioneered the transport of POL traffic in tank containers.
- CONCOR's business continues to maintain its high growth pattern in terms of both throughput and income. From a level of 109,000 TEUs in 1991-92, the traffic throughput has reached 703,452 TEUs in 1996-97—more than a six-fold increase in five years. International traffic it carried was 424,741 TEUs in 1996-97.
- Apart from serving international traffic, CONCOR has pioneered and is developing containerisation in domestic trade.
- CONCOR has made small beginnings as Multimodal Transport Operator (MTO) and also as a consultancy organisation for multi-modalism.
- December 28, 1994 CONCOR registered as Multimodal Transport Operator under the Multimodal Transportation of Goods Act, 1993.

11.4.4 Collaboration of CONCOR

Central Warehousing Corporation (CWC) is playing a vital role in operating some CFSs. There is proper coordination between CONCOR and CWC for smooth flow of cargo between CFSs managed by different agencies. The largest CFS at Kalamboli on Mumbai-Pune Highway and import warehouse near Jawaharlal Nehru port are both managed by CWC. There is also a CFS for export and import at Dronagiri Node, in Navi Mumbai. In addition to the public sector CFSs, there are private CFSs at Chembur, Taloja and Mulund in the Mumbai area. CONCOR coordinates with some of the state warehousing corporations, for example, the Punjab State Warehousing Corporation (PSWC). CWC and PSWC have jointly set up a CFS linked to the ICD at Ludhiana.



Note The Shipping Corporation of India Ltd. has set up CFSs at Jaipur and Varanasi (Babatpur), exclusive ventures serving the exporters at their doorstep. Export cargo is collected at shipper's godown for containerisation at CFS. Consolidation facility is also available.

Establishment and Operation of ICDs under CONCOR

As the country heads towards achieving containerisation in greater proportions, the development of Inland Container Depots (ICDs) and Container Freight Stations (CFSs) becomes crucial. Contrary to its dubious status as being a laggard in containerisation, the country is making serious efforts to boost the intermodal network and Container Corporation of India (CONCOR), which has taken up the formidable task of setting up ICDs and CFSs spanning the length and breadth of India.

Notes

The Indian Railways set up seven ICDs, the first being at Guntur in December 1980, followed by Bangalore in 1981. The need was, however, felt to set up a separate undertaking under the Railways to manage the ICDs and CFSs. Hence CONCOR was established in 1988 to provide for an integrated development of ICDs and CFSs to meet future growth requirements.

11.5 Constraint in Growth of ICDs

The slow growth of ICDs and CFSs was due to the combined effect of high capital costs involved, resource constraints and lack of attention.

A few anachronistic procedures as far as containerised cargo is concerned are as follows:

- (i) Inland containers cannot move directly to the ICDs unless special permission is obtained from the Collector of Customs for which the shipping agent has to file an application.
- (ii) Movement of containers between the quay, container yard, rail terminal and shed requires specific permissions from port and Customs authorities, which delays the movements.
- (iii) Movement of containers outside the port requires a bond for the container to be furnished by the shipping line even though it moves by rail and remains all along in the custody of a Central government agency.
- (iv) In the case of ICDs, three bonds are required—one for the container, other for the cargo in case it moves by road and third for the movement of container outside the ICD to the shipper's premises.
- (v) All the import containers are opened and examined by the Customs, requiring double handling of all the containers. Normally, 10 percent of the cargo is examined unless there are special reasons to do a more thorough examination.

However, instead of examining 10 percent of the number of containers, 10 percent of the cargo in each container is examined.

11.5.1 Port Infrastructure for Containerised Cargo

Out of the 11 major ports in the country, only Madras, Haldia and Nehru Ports have full-fledged container terminals. Bombay, despite provision of container handling facilities, cannot be stated to have a container terminal as connected operations are widely dispersed in the dock area. Cochin and Calcutta have only basic facilities and due to draft and crane limitations, can handle only small feeder vessels. Other ports do not have specific container handling facilities but the Indian government made provisions in its Eighth Five-Year Plan for setting up container handling facilities at all the major ports. Despite lack of container handling facilities, the container traffic has been increasing at Indian ports due to the pressures of international traffic.

11.6 International Scenario

The earlier limited and experimental efforts apart, regular containerised shipping of cargo in international trade commenced with the institution of container service between the US and Europe in 1966 across the Atlantic. This was followed by container service between Japan and the US across the Pacific in 1967, between Australia and Europe in 1969, between Japan and Europe in 1971, culminating in the coverage of nearly all major routes by 1973. The containerised shipping of cargo has seen tremendous growth thereafter. To meet the increasing demand for containerised services and to cut costs, ship sizes have also increased from under 500 TEU capacities to over 3000 TEU capacity. Intermediate ports at major routes have developed into important centres of aggregation and dispersal of cargo where larger vessels discharge and pick

up containers, smaller vessels providing the feeder services to and from other ports served by the transshipment port.

Notes

Further penetration of containers from the ports to inland destinations was a logical extension of this massive growth in the containerised movement of international cargo resulting in the setting up of Inland Container Depots (ICDs) and Container Freight Stations (CFSs). Operational versatility of containers has brought into effect the concept of land bridging, that is, substitution of the part of the ocean route by shorter land route. With mini land bridges providing coast to coast overland bridges and micro land bridges linking ports with inland locations, a cost-effective multi modal system has evolved.

With the setting up of ICDs/CFSs, the shipping services are now closer to business/commercial centres, giving the added advantage of issuing through bills of lading and discounting by the banks providing for easy cash liquidity.

Self Assessment

Fill in the blanks:

11. CONCOR started functioning from March
12. CONCOR took over ICDs on 1st November 1989 from Indian Railways.
13. Out of the major ports in the country, only Madras, Haldia and Nehru Ports have full-fledged container terminals.
14. The was constituted as an autonomous public sector undertaking under the Ministry of Railways in March 1988.
15. The basic objective of CONCOR is to organise transport logistics with prime task of facilitating the nation's foreign trade.

11.7 Summary

- Both ICD and CFS is an infrastructure facility, owned and operated by public or private authority, especially designed for offering services of handling, storage and movement of containerized cargo and cargo under Customs supervision.
- ICD/CFS is a logistic hub for LCL cargo thus consolidation became more easy.
- ICD/CFS assist exporter/importer is reducing inventory cost.
- ICD/CFS are owned and operated by public and private authorities thus every user gets quality service at competitive rates.

11.8 Keywords

Inland Container Depot is an organisation offering a total package of activities to handle and control container and general cargo flows between road, rail and waterways, and vice versa, resulting in maximum service for inland transportation at minimum costs.

Container Freight Stations (CFS): CFS have been established to speed up export cargo and to specially help small exporters whose consignments are less than container (LCL) loads.

The Container Corporation of India Ltd. (CONCOR) was constituted as an autonomous public sector undertaking under the Ministry of Railways in March 1988.

Notes

11.9 Review Questions

1. What do you understand by Inland container depot?
2. What are container freight stations? Discuss its importance.
3. Write a detailed note for the growth of the Container Corporation of India Ltd.
4. What are the major collaborations of CONCOR?
5. Discuss the clearance procedure of exports.

Answers: Self Assessment

- | | |
|----------------------------|--|
| 1. 1968 | 2. SCI |
| 3. Inland Container Depots | 4. less |
| 5. Customs Officer | 6. de-stuffing |
| 7. Bills of Entry (B/E) | 8. Railway/Road |
| 9. transshipment | 10. shipping bill |
| 11. 1988 | 12. seven |
| 13. 11 | 14. Container Corporation of India Ltd. (CONCOR) |
| 15. multimodal | |

11.10 Further Readings



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Online links

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Case Study

Container Cargo Management

Container Corporation of India Ltd. (CONCOR) is a multimodal (Rail and Road) logistics support provider for country's Export-Import and Domestic trade and commerce, working under Ministry of Railways, Govt. of India. It handles the Imports and Exports of the country from 40 dry ports or terminals spread across India. This case study discusses the problems faced and solution given by CMC in streamlining their operations.

Highlights

1. Operations spread across 40 Terminals all over India requiring sharing of information for Containers, Cargo and Wagon Tracking.
2. The solution comprising a centralized system capturing the online information from all units using LAN and WAN
3. Result: Availability of online data of all terminals for faster analysis and on time decision making
4. Reduced the duplication of work and helped in proper planning of the activities.

The Challenge

CONCOR required a system to capture the online operation and commercial data at all the terminals with very complex business processes and sharing the required data across terminals for advanced planning. For example, the train with Import containers going from Port Terminal to Container depot requires the data to be available at the Container depot before train arrival so that next operation can be planned. Also the analysis data should be available to Regional office and corporate office for timely decision. Interface with Customs and Railways and CONCOR's customers were also required.

The Assignment

With this background CONCOR entrusted CMC with business mapping, process reorientation, development and implementation of a solution keeping in mind CMC's success in computerization of their largest terminal handling 30% of their total operation at Tughlakabad Delhi. The solution was to cater to the requirements of CONCOR's Inland Container Depots (ICD), Container Freight Stations (CFS) and Port side Container Terminals (PSCT) as well as Regional Offices and Corporate Office.

The Analysis

After Initial discussions with CONCOR it was felt that some business process re-engineering is required at different terminals to take care of the varying practices at different terminals.

A centralized system was found to be most appropriate which can work on their existing VSAT WAN infrastructure and which can cater to all terminals requirements.

The Solution

The system was developed on a modular architecture so that different terminals can use the modules as per their requirements. Terminal wise parameters were made for customization of the application according to a particular terminal's requirements. Scalability and flexibility were the other issues kept in mind while design and development

Contd...

Notes

of the system. EDI interface with Customs were provided and Interface with Railways and CONCOR's customers like Shipping Lines were also provided

The Implementation

CMC helped CONCOR in faster implementation of the system at all the terminals. After initial hassles and new discoveries in the processes at different terminals where solution was sometimes very tricky, the system worked well and user acceptance started coming. CMC persons went to all the terminals for initial training and handholding support to actual field staff, while a team of dedicated developers at Central site in Delhi took care of the customization requirements.

The Benefits

After system implementation the tracking of Containers, Cargo and Wagons has become easy and is possible from any location in India. Duplicate entries have been eliminated resulting in less no of errors. CONCOR's customers have also benefited with facilities like payment at a single location, better information and coordination.

The Future

Now CONCOR has more data for planning activities and focus on reducing time taken to service it's customer. It can now use it's scarce resources like Trains and Containers more efficiently and their improved productivity has helped improve profitability of operations for CONCOR.

Question:

Discuss the future and benefits of cargo management.

Unit 12: Export Incentives Schemes

Notes

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Objectives

After studying this unit, you will be able to:

- Explain Export incentives
- Describe Duty Exemption Scheme
- Discuss Duty Remission Scheme
- Explain Export promotion capital goods

Introduction

The Commerce & Industry Ministry on 7th April, 2006 announced trade initiatives in form of Annual Supplement, 2006 to the Foreign Trade Policy 2004-09 (AS) to put country's exports on a trajectory of quantum growth and to create large number of jobs.

Exports emerge as a major source of job creation in the Indian economy:

- 1.4 million incremental jobs created through exports in 2004-05.
- 8 million additional jobs projected through exports by 2009.
- Textiles, garments, leather goods, gems & jewellery, horticultural exports of fruits & flowers, dairy products, processed foods, pharmaceuticals, and automobiles identified as high growth sectors for employment.

Notes

Merchandise Exports

Merchandise exports cross 100 billion dollars in 2005-06.

- 25% growth rate registered in 2005-06.
- Merchandise exports jumped by 60% from 63 billion dollars to 101 billion dollars within two years.

New Initiatives

Product Market Focus- To focus not only on neutralizing duties and levies but also provide additional stimulus to export of products having large employment potential and for greater penetration in strategic markets:

Product Focus

It proposes additional duty credit facility @ 2.5% of FOB value of export turnover of notified products, such as value added fish and leather products, stationery, fireworks, sports goods, handloom products, bearing handloom marks and handicraft items. The scheme is to offset inherent infrastructure bottlenecks in rural and semi-urban areas.

Market Focus

Duty credit facility @ 2.5% of the FOB value of export of all products to notified countries. This scheme aims at offsetting the high freight cost and other disabilities faced in accessing select international markets.

Expanding Vishesh Krishi Upaj Yojana

Duty free scrip @ 5% of FOB value of exports under VKUY to incentivise the export of Gram Udyog products.

- The scheme is renamed as Vishesh Krishi and Gram Udyog Yojana.
- Additional benefit on use of domestic farm produce in agricultural exports.
- This will promote in indigenous procurement of inputs for agricultural exports and help the farming community.

India as a Gem & Jewellery Hub

Measures for facilitating export of value added products catering to changing needs of the market, facilitating easier product movement across the borders and allowing import of precious metal scrap for refining.

- Export of jewellery on consignment basis allowed.
- Re-import of rejected jewellery allowed.
- Import of precious metal scrap/used jewellery for melting and re-export permitted.
- Exporters will be allowed to export stones for treatment abroad and subsequent re-import without payment of customs duty.

India as an Automotive Hub

Notes

- Provision to allow import of new vehicles by auto component manufacturers for R&D purposes without homologation is being introduced.
- To further accelerate India's emergence as an important centre for sourcing auto components.

India as a Refuelling Stop

- Supply of stores (food, beverages etc.) and refuelling of long distance flights has emerged as a big business opportunity.
- Such export of supplies brought on equal footing with other exports for claiming duty neutralization benefits under various export promotion schemes.
- This will enable India to offer competitive fuel prices and attract mid route stops for international flights.

Benefit of Un-rebated Service Tax and FBT

- Incidence of un-rebated service tax and Fringe Benefit Tax (FBT) on exports will be factored in the various duty neutralization and remission schemes.
- Details are being worked out and would be announced separately.

Trade Facilitation Measures

- Interest for delayed payment of refunds would be made by the government to ensure accountability and cut delays.
- Fast track clearance procedure for units in EOUs. Now, units having physical turnover of ₹ 15 crore can avail of the facility of receiving goods and warehousing on self-declaration basis.
- Advance licencing liberalised where norms are not fixed.
- Pre-shipment certificates in lieu of test report for faster clearances.

Source: Annual Supplement 2006 Foreign Trade Policy (2004-09)/ www.pib.nic.in

India's exports are booming and the Government of India is following up this progress by introducing new initiatives to further boost the exporters' efforts. Exports reflect foreign exchange earnings of a nation and therefore, it is imperative to provide full support and motivation to the export community so that they can remain both active and competitive in the international markets. This is more important for a growing economy like India. The WTO regime insists on globalization, that is free flow of goods and services across physical borders of countries. India is working very hard to liberalize its business activities to be able to keep in tune with international forces. As a result, the current Foreign Trade Policy aims to promote exports at an unprecedented rate. Indian exports have grown by an impressive 60% in the last two years, from 63 billion dollars to 101 billion dollars. The winds of positive changes are beginning to show improvements and the exporters in India are hopeful of more reforms, better facilities, sound incentive schemes and aggressive promotional measures.

Let us now study the various incentives/exemptions available to exporters in India in greater details:

- Sales Tax/VAT Exemption
- Excise Exemption

Notes

- Duty Drawback
- Income Tax Concessions
- Export Promotion Capital Goods
- Duty Free Import Authorisation Schemes
- Duty Exemption Passbook Scheme
- Free Trade & Warehousing Zones
- Star Export Houses
- EOUs, Electronic Hardware Technology Parks, Software Technology Parks
- Biotechnology Parks
- Deemed Exports

12.1 Sales Tax/VAT Exemption

An exporter has to duly register with sales tax/value added tax authorities. However, no sales tax/value added tax is payable for goods meant for exports. Sales tax/VAT is an indirect tax that the manufacturer collects from the customer and deposits to the Central/state authorities. To make export prices internationally competitive, exports have been kept immune from the impact of sales tax/value added tax.

Sales tax in India has been replaced by Value Added Tax (VAT). The new system came into effect from April 1, 2005. VAT is a multipoint tax system. As each item passes through various stages of production and distribution, some value addition takes place at each stage. VAT is a tax on such value addition at each stage. It provides for set off of tax paid on purchases at each point of sale. VAT is a superior system than the earlier used sales tax as it does away with tax on tax.

For exports, the goods exported are zero rated under VAT. This actually means that the exporter will get full input tax credit and the rate applied to such transaction will be zero. Simply put, under this system the exporter need not charge any tax or pay any VAT on his export sales and he can reclaim any VAT that he has been charged on the goods exported or any input tax that he has incurred in the production of goods exported.



Did u know? VAT at zero rate and full credit of input tax is also available to a dealer directly selling to an exporter provided the same goods are actually exported.

The exporter needs to provide the following documents as evidence of goods exported:

- Copy of export contract or order from a foreign buyer
- Copy of the customs clearance certificate
- Copy of the commercial invoice issued to the foreign buyer
- Copy of Bill of Lading/Air-Way Bill
- Proof of payment from the foreign purchaser or letter of credit

The exporter can make use of 'H Forms' supplied by the CST (Central Sales Tax) authorities that are being continued even now in the VAT regime. The exporter needs to apply in the prescribed application form to the concerned sales tax office for issue of Form H. The application has to be supported by the following documents:

- Copy of Customs Certified Shipping Bill
- Copy of Customs Certified Invoice

- Copy of Letter of Credit
- Copy of Confirmed Export Order

Notes

The exporter will also be required to execute a surety bond in a prescribed form by the authorities. This bond works as a guarantee for safekeeping of the Statutory Forms issued to the exporter.



Note Once the application is accepted as being satisfactory, the sales tax office may order issue of Form H to the exporter.

Now, for goods bought from a supplier, the exporter can issue an H Form instead of paying the VAT. Form H will be filled by the exporter in triplicate. He will give two copies of the form to the dealer and retain one copy with him. The exporter also needs to maintain a proper record of Form H in the prescribed form/register. This record will have to be submitted to the STO in prescribed time.

The supplier, on the other hand, can submit the following documents with his VAT return to justify zero rating of his particular sale to the exporter:

- Purchase order from exporter.
- Form 'H'.
- Copy of Bill of Lading/Air-Way Bill

12.2 Excise Exemption

Excise is a tax on production or manufacture of goods. It is a duty levied on the production of goods and the liability of payment of excise duty arises immediately upon manufacture of goods. In India, excise duty is governed by the provisions of the Central Excise Act, 1944.

Excisable goods can not be removed from the place of manufacture unless prescribed excise duty has been paid. The manufacturer, whose unit falls under the purview of excise, needs to register it with the excise office. The unit, once registered, needs to maintain records of production and removal of goods as per the requirements of the excise rules.

Exports in India are exempt from the payment of excise duties. This is based on the internationally practiced trend of keeping exports free from the burden of indirect taxation. Exporters can avail excise clearance in the following ways:

- Exports under Claim of Excise Rebate- As per Rule 18 of Central Excise Rules, exports are eligible for full refund of excise duty paid on raw materials and finished products except for goods exported to Nepal and Bhutan. Thus, under this scheme, the exporter first makes payment of the total excise duty and later applies for full rebate as the goods have been exported out of India. The exporter is not eligible for this rebate in case he has claimed benefits under the Duty Drawback Scheme or CENVAT (Central Value Added Tax) Credit under the CENVAT Credit Rules, 2002.

The exporter will first prepare the ARE-I/ARE-II forms in sextuplicate, giving all particulars and declarations. The exporter will then deliver triplicate, quadruplicate, quintuplicate and sextuplicate copies of ARE-I/ARE-II forms to the Superintendent of Central Excise having jurisdiction over the factory or the warehouse, within twenty-four hours of the removal of the consignment. The exporter would retain the original and duplicate copies for presenting along with the consignment to the Customs Officer at the point of export.

The jurisdictional Superintendent of Central Excise shall examine the information contained in ARE-I/ARE-II and verify the facts of payment of duty and other certificates/declarations made

Notes

by the exporter. After he is satisfied that the information contained in the ARE-I/ARE-II is true, he will sign at appropriate places in the four copies of ARE-I/ARE-II submitted to him and put his stamp with his name and designation below his signature. He would then dispose of the triplicate, quadruplicate, quintuplicate and sextuplicate copies of ARE-I/ARE-II as under:

Triplicate: To the rebate sanctioning authority viz. Maritime Collector of Central Excise or the Assistant Commissioner of Central Excise as declared by the exporter on the ARE-I/ARE-II. This copy on the request of exporter may be sealed and handed over to the exporter/his authorized agent for presenting to the rebate sanctioning authority.

Quadruplicate: To the Chief Accounts Officer in the Commissionerate Headquarters.

Quintuplicate: Office copy to be retained by the Central Excise Officer.

Sextuplicate: To be given to the exporter.

The exporter also has the option of examination and sealing of the goods by excise authorities at his premises so that the goods may not be examined by the customs authorities at the port/airport. Here again, the exporter will prepare and submit copies of ARE-I/ARE-II forms as already explained above. The Superintendent of Central Excise may depute an Inspector of Central Excise or may himself go for sealing and examination of the export consignment. The Central Excise Officer examining the consignment would draw samples if necessary in triplicate. He would hand over two sets of samples, duly sealed, to the exporter or his authorized agent, for delivering to the Customs Officers at the point of export. He would retain the third set for his records.

The original, duplicate and sextuplicate copies of the ARE-I/ARE-II shall be presented by the exporter/his authorized agent to the Customs Officer at the point of export along with the goods, Shipping Bill/Bill of Export and samples sealed by the Central Excise Officer. The export consignment shall be checked by the Customs Officer to see whether the seals are intact and the marks and number tally and if found in order he may allow exports after ensuring that the Number of the ARE-I/ARE-II has been indicated in the Shipping Bill/Bill of Export.

The samples shall be treated as per instructions/standing orders of the Collector of Customs or the Central Board of Excise and Customs. After the goods have been shipped, the authorized Customs official would make necessary endorsement in the original, duplicate and sextuplicate copies of the ARE-I/ARE-II at appropriate places and put his stamp with his name and designation below his signature. The Customs Official will hand over the original and sextuplicate copies back to the exporter. The original copy will be used by the exporter in filing the claim for excise rebate. The duplicate copy will be sent by Customs to the Rebate Sanctioning Authority. This copy, on a request from the exporter, may be sealed and handed over to the exporter/his authorized agent for presenting to the rebate sanctioning authority.

12.3 Procedure for Filing the Rebate Claim and its Sanction

Depending upon the exporter's option declared on the ARE-I/ARE-II, the claim should be filed with the jurisdiction of Maritime Collector of Central Excise and/or with Assistant Collector of Central Excise having jurisdiction on the factory of the exporter for claiming the rebate of excise duty on goods exported. The following documents need to be filed for claiming rebate:

1. Application in the prescribed form
2. Duplicate copy of ARE-I/ARE-II in sealed cover received from Customs Officer
3. Duly attested copy of Bill and Lading
4. Duly attested copy of shipping bill (export promotion copy)

5. Original copy of duly ARE-I/ARE-II duly endorsed by the Customs Officer certifying the export of the consignment
6. A disclaimer certificate in case where the claimant is other than the exporter.

Notes

The claim needs to be filed within six months i.e. time prescribed under Section 11B of Central Excises and Salt Act.

The Maritime Collector or Asstt. Collector, Central Excise would verify and compare the original copy of ARE-I/ARE-II received from exporter with the duplicate copy of ARE-I/ARE-II received from Customs Officer and triplicate copy of ARE-I/ARE-II received from Range Supdt. Once satisfied that the claim is in order, he will sanction the rebate.

The rebate sanctioning authority must point out deficiency, if any, in the claim within 15 days of lodging the same and ask the exporter to rectify and dispose off the claim within a period of two months. If the exporter does not receive the rebate amount within three months of the date of his filing the claim, he is entitled to interest @ 20% p.a. for the time between the expiry of three months and the date of receipt of the amount.

- **Export under Bond-** Under Rule 19 of Central Excise Rules, an exporter is permitted to remove excisable goods for export without payment of excise duty by executing a bond (legal undertaking) in favour of the excise authorities for the amount of the excise duty payable. This bond needs to be duly supported by an appropriate Bank Guarantee. This will ensure safeguard for the excise department and put the ultimate onus on the exporter in case he fails to export the excisable goods within the permitted time. The liability of the exporter under this bond stands until he exports the goods and submits proof of the same to the excise authorities. On satisfactory submission of the proof of exports, his liability under the bond gets discharged.

Here, there are three possibilities for obtaining excise clearance and executing the legal undertaking. Goods can be examined at the exporter's premises. The exporter can remove goods under self-certification. The third option is to get the excise examination and clearance done at the port/airport.

Normally, the goods, for which the bond is executed, must be exported within a period of six months from the date of excise clearance.



Caution However, in certain special cases the Central Excise Authorities may grant an extension against application made by the exporter seeking such extension.

12.4 Duty Drawback

Duty drawback is an incentive given to the exporters of different categories of goods under the "Customs and Central Excise Duty Drawback Rules, 1995". The duty drawback scheme is administered by the Directorate of Duty Drawback in the Ministry of Finance, Government of India.

The basic purpose of drawback is to protect the exports from the burden of indirect taxes like excise and import duty. Drawback is a rebate of duties chargeable on any excisable material and on any imported input used in the goods manufactured and exported from India. Thus, drawback has two components – excise portion and customs portion. Drawback is an internationally practiced concept and is widely used to encourage exports.

Notes

The Directorate of Duty Drawback is responsible for fixing and announcing rates of drawback from time to time. There are two types of drawback rates:

- **All Industry Rates:** These are published by the Directorate every year. These are fixed for a particular class of products manufactured and take into account the averages of input consumption, taxes and duties paid, wastages, and FOB prices of exported products. These rates are prescribed in value terms like percentage of FOB value or in quantity terms like per kg./per tonne etc.
- **Brand/Special Brand Rates:** These are special rates allowed to a specific manufacturer for a particular product. These are usually decided for those exporters who approach the Directorate with special requests either in cases where there is no industry rate available or where the existing rate does not provide adequate refund of duties paid. The Directorate on its own discretion may decide special rates under such circumstances.

A different shipping bill bearing green colour, called Green Shipping Bill needs to be used by the exporter at the time of shipment, if the item being exported is eligible for drawback claim. The Customs official will provisionally accept the drawback claim at the time of shipment by duly verifying the shipping bill. However, the claim is finally settled by the Customs Office later.

Many of the Customs Houses in India like Delhi, Mumbai, Kolkata, Chennai, Hyderabad and Chandigarh have EDI (Electronic Data Interchange) Systems in operations these days. The drawback claims under the EDI system get automatically settled and the amount of drawback gets transferred to the drawback account of the exporter. The State Bank of India and Punjab National Bank have facilities for exporters to open such accounts at their branches/extension counters functioning at various ports/airports.

In cases where the settlement of drawback claims take time and huge amounts are blocked, the exporter can approach his bank and take a loan against the pending receipt of drawback amount.

12.5 Income Tax Concessions

Till about a few years ago, export income in India was totally exempt from income tax. However, the same was withdrawn in a phased manner. At present, no income tax benefit is available to the exporters under Section 80 HHC.

Under Section 10A of the Income Tax Act, 1961 undertaking operating from a Special Economic Zone (SEZ) that manufactures articles/things or computer software are eligible for deduction of export profits. For undertaking commencing operation from the notified Special Economic Zones (SEZs) on or after 1st April, 2002, the tax holiday is available for a total period of seven assessment years, comprising of a deduction of 100% of export for five years followed by deduction of 50% of export profits for subsequent two years.

Self Assessment

Fill in the blanks:

1. in India has been replaced by Value Added Tax (VAT).
2. is a tax on such value addition at each stage. It provides for set off of tax paid on purchases at each point of sale.
3. For exports, the goods exported are rated under VAT.
4. is a tax on production or manufacture of goods.

5. Excisable goods cannot be removed from the place of manufacture unless prescribed has been paid
6. in India are exempt from the payment of excise duties.
7. Normally, the goods, for which the bond is executed, must be exported within a period of months from the date of excise clearance
8. is an incentive given to the exporters of different categories of goods.
9. The drawback claims under the system get automatically settled and the amount of drawback gets transferred to the drawback account of the exporter.
10. Green Shipping Bill needs to be used by the exporter at the time of shipment, if the item being exported is eligible for claim.

Notes

12.6 Export Promotion Capital Goods Scheme

The Export Promotion Capital Goods Scheme focuses on less costly imports of capital goods for the exporters to increase their cost and manufacturing competitiveness in the international markets. Under the scheme, exporters are allowed to import capital goods at concessional rates of import duty against acceptance of certain export obligations. The scheme came into force in 1990 and has been revised a number of times to meet the changing needs of the export community.

The scheme permits import of capital goods for pre-production, production and post production (including CKD/SKD thereof as well as computer software systems) at 5% customs duty subject to an export obligation equivalent to 8 times of duty saved on capital goods imported under EPCG scheme to be fulfilled over a period of 8 years reckoned from the date of issuance of licence. Capital goods are allowed at 0% duty for exports of agricultural products and their value added variants.

However, in respect of EPCG licences with a duty saved of ₹100 crore or more, the same export obligation is allowed to be fulfilled over a period of 12 years.

Capital goods under the scheme include spares (including refurbished/reconditioned spares), tools, jigs, fixtures, dies and moulds. EPCG licence may also be issued for import of components of such capital goods required for assembly or manufacturer of capital goods by the licence holder. Secondhand capital goods without any restriction on age are also allowed to be imported under the EPCG scheme.

The scheme covers manufacturer exporters with or without supporting manufacturer(s)/ vendor(s), merchant exporters tied to supporting manufacturer(s) and service providers. Import of capital goods is subject to the Actual User condition till the export obligation is completed.

The export obligation needs to be fulfilled by the export of goods capable of being manufactured or produced by the use of the capital goods imported under the scheme. The export obligation under the scheme shall be, in addition to any other export obligation undertaken by the importer, except the export obligation for the same product under Advance Licence, DFRC, DEPB or Drawback scheme.

In the case of EPCG licences issued to agro units in the agri export zones, a period of 12 years reckoned from the date of issue of the licence has been permitted for the fulfilment of export obligation. The agro units in the agri export zones are also allowed the facility of moving the capital good(s) imported under the EPCG within the agri export zone.

In the latest Annual Supplement to the FTP 2004-09, released in April 2006, the Finance Minister has introduced further flexibilities in the conditions relating to maintenance of average export

Notes

performance under the EPCG Scheme, and also in the extension of export obligation period by 2 years, based on certain conditions.

12.7 Duty Free Import Authorization Scheme

This scheme is the latest improvement announced in the Annual Supplement 2006 to the FTP 2004-09. The new scheme seeks to club the Advance Licencing scheme and the Duty Free Replenishment Certificate and were to come into effect from May 1, 2006. The new scheme will offer the facility to import the required inputs before the exports. It will also allow transferability of scrip once the export obligation is complete. Imports made under this authorization will be exempt from payment of basic custom duty, additional customs duty, education cess, anti-dumping duty and safeguard duty, if any. The scheme proposes to combine the salient features of both the earlier schemes. Earlier, an exporter could either avail Advance Licencing or DFRC. This improvement promises best of both the schemes to the exporter.

Advance Licencing scheme provides for issue of an import licence to allow duty free import of inputs, which are physically incorporated in the export product (making normal allowance for wastage). In addition, fuel, oil, energy, catalysts etc. which are consumed in the course of their use to obtain the export product, are also allowed under the scheme.

Advance Licence can be issued for the following:

- (i) **Physical exports:** Advance Licence may be issued for physical exports including exports to SEZ to a manufacturer exporter or merchant exporter tied to supporting manufacturer(s) for import of inputs required for the export product.
- (ii) **Intermediate supplies:** Advance Licence may be issued for intermediate supply to a manufacturer-exporter for the import of inputs required in the manufacture of goods to be supplied to the ultimate exporter/deemed exporter holding another Advance Licence.
- (iii) **Deemed exports:** Advance Licence can be issued for deemed export to the main contractor for import of inputs required in the manufacture of goods to be supplied to the categories specified in the Foreign Trade Policy.

Advance Licence is issued for duty free import of inputs subject to actual user condition. Such licences (other than Advance Licence for deemed exports) are exempted from payment of basic customs duty, additional customs duty, education cess, anti-dumping duty and safeguard duty, if any. Advance Licence for deemed export shall be exempted from basic customs duty, additional customs duty and education cess only. However in case of supplies to EOU/SEZ/EHTP/STP/BTP under such licences, anti-dumping duty and safeguard duty shall also be exempted. These provisions were further upgraded in the Annual Supplement 2005 to the Foreign Trade Policy. Now, Safeguard duty and anti-dumping duty have been exempted on inputs under Advance Licence for deemed export supplies made to projects under ICB (International Competitive Bidding) procedure (Circular No. 30/2005-Cus.12th July, 2005).

Advance Licence and/or materials imported thereunder are not permitted to be transferred even after completion of export obligation. The scope of Advance Licence for Annual Requirement has been extended to all categories of exporters having past export performance. Earlier, the licences were issued to status-holders only.

Transfer of duty free material imported or procured under Advance Licence from one unit of the company to another unit of the same company has been allowed with prior intimation to the jurisdictional central excise authority. Earlier, prior permission of the jurisdictional Central Excise Authority was required.

Export obligation under Advance Licence is based on Value Addition. The Foreign Trade Policy has defined Value Addition as follows:

Notes

$$V.A. = A-B/B*100$$

Where,

V.A. Value Addition

- A FOB value of the export realized /FOR value of supply received
- B CIF value of the imported inputs covered by the licence, plus any other imported materials used on which the benefit of duty drawback is being claimed.

An Advance Licence contains:

- (a) The names and description of items to be imported and exported/supplied
- (b) The quantity of each item to be imported or wherever the quantity cannot be indicated, the value of the item shall be indicated. However, if in standard input-output norms, the quantity and value of individual inputs is a limiting factor, the same shall be applicable
- (c) The aggregate CIF value of imports
- (d) The FOB/FOR value and quantity of exports/supplies.

Advance Licence is valid for a period of 18 months from the date of shipment/despatch of goods from the foreign country. This validity period may be extended by a maximum of 6 months, based on the merits of each case at the discretion of the competent licencing authority. The exporter must fulfill his export obligation under advance licence within a period of 18 months from the date of issue of the licence. Two further extensions of 6 months each are possible after the expiry of the original period on the payment of composition fee at prescribed rates.

Duty Free Replenishment Certificate is issued to a merchant-exporter or manufacturer-exporter for the import of inputs used in the manufacture of goods without payment of basic customs duty. However, such inputs are subject to the payment of additional customs duty equal to the excise duty at the time of import. DFRC is issued in respect of exports for which payments are received in non-convertible currency.



Caution DFRC is issued only in respect of products covered under the Standard Input Output Norms (SION) as notified by DGFT.

The DFRC and the specific inputs procured against it are subject to actual user condition under the following circumstances:

- (i) The export proceeds have not been realized and the exports have not been made under an irrevocable letter of credit or the bill of exchange is not availed/co-accepted/guaranteed
- (ii) The DFRC is issued against a SION with actual user condition
- (iii) Specific inputs under a SION are subject to actual user condition.

Under all other circumstances, the inputs procured against DFRC are freely transferable. However, in case of fuel, the import entitlement will be allowed to be transferred only to the companies which have been granted authorization to market fuels by the Ministry of Petroleum & Natural Gas.

DFRC is valid for a period of 18 months. An application for grant of DFRC may be made to the Regional Authority concerned in the form given in 'Aayaat Niryaat Form' along with the

Notes

documents prescribed therein. An application for DFRC shall be filed only after realisation of export/supply proceeds. However, in case of exports/supplies against:

- (a) Confirmed irrevocable letter of credit or confirmed irrevocable inland letter of credit
- (b) Bill of exchange is unconditionally Avalised/Co-Accepted/Guaranteed by a bank and the same is confirmed by the exporter's bank,

The application may be filed after exports/supplies.

The application for DFRC shall be filed within six months from the date of realisation in respect of all shipments/supply for which DFRC is being claimed. In case of exports against confirmed irrevocable Letter of Credit/supply against confirmed irrevocable Inland Letter of Credit or Bill of Exchange is unconditionally Avalised/Co-Accepted/Guaranteed by a bank and the same is confirmed by the exporters bank, the DFRC shall be filed within six months from the date of exports/supply for all shipments in respect of which DFRC is being claimed. For exports/supply against advance payment, DFRC shall be filed within six months from the date of exports against advance payment. Wherever provisional shipment has been allowed by the customs authorities, DFRC against such exports shall be issued only after the release of the shipping bill by the Customs. The time limit for filing of application in such cases shall be six months from the date of release of shipping bill or three months from date of realisation, whichever is later.

The applicant shall file one application relating to one export product group from one port of export. Where export products falling under one product group have been exported from different ports, the exporter shall file more than one application for the same export product group.

12.7.1 Duty Entitlement Passbook (DEPB) Scheme

Under DEPB (Duty Entitlement Passbook) Scheme, exporters are allowed to claim customs duty credit as a specified percentage of FOB value of exports made in freely convertible currency. The objective of DEPB is to neutralize the incidence of Customs duty on the import content of the export product. The neutralization shall be provided by way of grant of duty credit against the export product.

The scheme launched in 1997 is likely to be replaced by some superior alternative that is being worked out through a dialogue with the export community. Under the DEPB, an exporter is eligible to apply for credit, as a specified percentage of FOB value of exports, made in freely convertible currency. This credit is available against such export products and at such rates as are specified by the Director General of Foreign Trade by way of public notice issued in this behalf, for import of raw materials, intermediates, components, parts, packaging material, etc.

The DEPB is valid for a period of 24 months from the date of issue. The DEPB and/or the items imported against it are freely transferable. The transfer of DEPB shall however be for import at the port specified in the DEPB, which shall be the port from where exports have been made.

Normally, the exports made under the DEPB Scheme are not eligible for drawback. However, the additional customs duty/excise duty paid in cash or through debit under DEPB shall be adjusted as CENVAT Credit or Duty Drawback as per rules framed by Department of Revenue.

DEPB credit may also be utilized for payment of customs duty on any item which is freely importable. The holder of DEPB is permitted the option to pay additional customs duty, if any, in cash as well. DEPB credit is available only for those items for which rates are available. Therefore, the exporters are not in a position to avail of this facility in respect of items for which DEPB rates have not been announced.

12.7.2 Free Trade and Warehousing Zones

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This scheme was formalized under the FTP 2004-09 with a view to create trade-related infrastructure to facilitate the import and export of goods and services with freedom to carry out trade transactions in free currency. The scheme proposes creation of world-class infrastructure for warehousing of various products, state-of-the-art equipment, transportation and handling facilities, commercial office-space, water, power, communications and connectivity, with one-stop clearance of import and export formality, to support the integrated zones as 'international trading hubs'. These zones would be established in areas proximate to seaports, airports or dry ports so as to offer easy access by rail and road. These zones shall be a special category of Special Economic Zones with a focus on trading and warehousing.

The zones can be set up by public sector undertakings or by public limited companies either independently or in collaboration with experienced infrastructure developers. The proposal will be considered by the Board of Approvals in the Commerce Ministry. Once the proposal is approved, the developer will be issued a letter of permission to develop, operate and maintain the zone. 100% FDI (Foreign Direct Investment) is permitted in this regard.

The proposal must entail a minimum outlay of ₹100 crore for the creation and development of the infrastructure facilities, with a minimum built up area of five lakh sq.mts. The developer shall be permitted to import duty-free such building materials and equipment as may be required for the development and infrastructure of the zone.

The units functioning out of such zones will be extended:

- (i) Income Tax Exemption as per Section 80-IA of the Income Tax Act
- (ii) Exemption from Service Tax
- (iii) Free foreign exchange currency transactions
- (iv) Other benefits as applicable to units in Special Economic Zones



Task Prepare a comparative study between Drawback and DEPB schemes using data available from the various reports and the Internet. Which scheme has been more successful and why?



Caselet

Press Release

PIB Press Release

Wednesday, April 27, 2005

Six Free Trade and Warehousing Zones to be set up

The MMTC Limited will establish six Free Trade and Warehousing Zones in accordance with the Foreign Trade Policy of 2004-09.

Six locations tentatively identified for Free Trade & Warehousing Zones (FTWZs) are Kandla, Noida, Mumbai, Haldia, Kochi and Ennore, to be set up in phases. The estimated investment for each warehouse would be ₹100 crore approximately. It envisages creation of world-class infrastructure for trading and warehousing of various products.

Source: pib.nic.in

Notes

Units in FTWZs shall be net foreign exchange earners. Net foreign exchange earning shall be calculated cumulatively for every block of five years from the commencement of warehousing and/or trading operations.

12.8 Star Export Houses

Under the current foreign trade policy, Merchant as well as Manufacturer Exporters, Service Providers, Export Oriented Units (EOUs) and Units located in Special Economic Zones (SEZs), Agri Export Zone (AEZs), Electronic Hardware Technology Parks (EHTPs), Software Technology Parks (STPs) and Bio Technology Parks (BTPs) are eligible for applying for status as Star Export Houses.

The categorization of applicants is based on his total FOB/FOR export performance during the current plus the previous three years as follows:

Table 12.1: FOB/FOR Export Performance

Category	Performance (in ₹)
One Star Export House	15 crore
Two Star Export House	100 crore
Three Star Export House	500 crore
Four Star Export House	1500 crore
Five Star Export House	5000 crore

The following special privileges are available to Star Export Houses:

- They are allowed licence/certificate/permissions and Customs clearances for both imports and exports on self-declaration basis.
- Fixation of Input-Output norms on priority within 60 days.
- They are allowed exemption from compulsory negotiation of documents through banks. The remittance, however, needs to be received through banking channels.
- 100% retention of foreign exchange in EEFC account.
- They are permitted enhancement in normal repatriation period from 180 days to 360 days.
- They are entitled for consideration under the Target Plus Scheme.
- They enjoy exemption from furnishing of Bank Guarantee in schemes under the foreign trade policy.

12.9 EOUs, Electronic Hardware Technology Parks, Software

Technology Parks, Biotechnology Parks

Units committed to exporting their entire production of goods and services can choose to set up in any one of the following schemes:

- Export Oriented Unit (EOU) Scheme
- Electronic Hardware Technology Park (EHTP) Scheme
- Software Technology Park (STP) Scheme
- Biotechnology Park (BTP) Scheme

These units are permitted manufacture of goods, including repair, re-making, re-conditioning, re-engineering and render of services. Trading units, however, are not covered under these schemes. An EOU/EHTP/STP/BTP unit is allowed to export all kinds of goods and services except items that are prohibited by the government.

An EOU/EHTP/STP/BTP unit is allowed to import and/or procure from DTA or bonded warehouses in DTA/international exhibitions held in India without payment of duty all types of goods, including capital goods, required for its activities, provided they are not prohibited items of import. The units are also permitted to import goods including capital goods required for the approved activity, free of cost or on loan/lease from clients. The import of capital goods is possible on self-certification basis.

Such units can also import secondhand capital goods without any age limit, duty-free. An EOU/EHTP/STP/BTP unit must be a positive net foreign exchange earner. Net Foreign Exchange (NFE) earnings are calculated cumulatively in blocks of five years, starting from the commencement of production.

The following special benefits/exemptions are extended to such units:

- Reimbursement of Central Sales Tax on goods manufactured in India
- Exemption from payment of Central Excise Duty on goods procured from DTA on goods manufactured in India
- Reimbursement of Central Excise Duty/additional excise duty paid on bulk tea procured from licenced auction centres
- Reimbursement of duty paid on fuels procured from domestic oil companies as per the rate of drawback notified by the DGFT from time to time
- Exemption from payment of service tax
- Exemption from payment of Income Tax as per the provisions of Sections 10A and 10B of the Income Tax Act
- Exemption from industrial licensing for manufacture of items reserved for the SSI sector
- An Offshore Banking Unit will extend credit on the same terms and condition as extended to units in SEZs
- Export proceeds will be realized within 12 months
- Will be allowed to retain 100% of its export earning in the EEFC account
- The units will not be required to furnish bank guarantee at the time of import or going for job work in DTA, where the unit has (i) a turnover of rupees 5 crore or above, (ii) the unit is in existence for at least three years and (iii) unit having an unblemished track record
- 100% FDI investment permitted through Automatic Route similar to SEZ units.

12.10 Deemed Exports

As per the foreign trade policy, deemed exports are those transactions in which the goods supplied do not leave the country and the payment for such supplies is received either in Indian rupees or in free foreign exchange. These are not real exports but are granted special status of exports because of the nature of transactions involved.

The following types of supplies of goods manufactured in India are treated as deemed exports:

1. Supply of goods against Advance Licence/Advance Licence for annual requirement/DFRC under the Duty Exemption/Remission Scheme

Notes

2. Supply of goods to Export Oriented Units (EOUs) or Software Technology Parks (STPs) or Electronic Hardware Technology Parks (EHTPs) or Biotechnology Parks (BTPs)
3. Supply of capital goods to holders of licences under the Export Promotion Capital Goods (EPCG) scheme
4. Supply of goods to projects financed by multilateral or bilateral agencies/funds as notified by the Department of Economic Affairs, Ministry of Finance under International Competitive Bidding in accordance with the procedures of those agencies/funds, where the legal agreements provide for tender evaluation without including the customs duty
5. Supply of capital goods, including in unassembled/disassembled condition as well as plants, machinery, accessories, tools, dyes and such goods which are used for installation purposes till the stage of commercial production and spares to the extent of 10% of the FOR value to fertilizer plants
6. Supply of goods to any project or purpose in respect of which the Ministry of Finance, by a notification, permits the import of such goods at zero customs duty
7. Supply of goods to the power projects and refineries not covered in (6) above
8. Supply of marine freight containers by 100% EOU (domestic freight containers-manufacturers) provided the said containers are exported out of India within 6 months or such further period as permitted by the Customs
9. Supply to projects funded by UN agencies
10. Supply of goods to nuclear power projects through competitive bidding as opposed to International Competitive Bidding.



Notes The benefits of deemed exports shall be available under (4), (5), (6) and (7) only if the supply is made under the procedure of International Competitive Bidding (ICB).

Deemed exports are allowed the following privileges:

- Advance Licence for intermediate supply/deemed export/DFRC/DFRC for intermediate supplies
- Deemed Export Drawback
- Exemption from terminal excise duty where supplies are made against International Competitive Bidding. In other cases, refund of terminal excise duty will be given.



- Task*
1. Visit the Seepz website and make a detailed report on the facilities available to units there.
 2. Visit a local exporter and find out the various incentive schemes that he is using. If you feel that he can use.

Self Assessment

Fill in the blanks:

11. The focuses on less costly imports of capital goods for the exporters to increase their cost and manufacturing competitiveness in the international markets.

12. Advance scheme provides for issue of an import licence to allow duty free import of inputs, which are physically incorporated in the export product
13. Under Scheme, exporters are allowed to claim customs duty credit as a specified percentage of FOB value of exports made in freely convertible currency.
14. exports are those transactions in which the goods supplied do not leave the country and the payment for such supplies is received either in Indian rupees or in free foreign exchange.
15. The DEPB is valid for a period of months from the date of issue.

Notes

12.11 Summary

- Export incentives are important to motivate exporters of the country to perform better.
- Indian exports have shown promising growth in the past few years. This has been possible largely due to policy initiatives to create a positive and hassle-free export environment.
- The Annual Supplement 2006 to the Foreign Trade Policy (2004-09) has also announced certain measures to further boost Indian exports.
- The Indian exporter is entitled to many incentives/concessions/exemptions and special treatments. These have been discussed under various heads: Sales Tax/VAT Exemption, Excise Exemption, Duty Drawback, Income Tax Concessions, Import Concessions, Special Economic Zones, Free Trade & Warehousing Zones, Star Export Houses, EOUs, Electronic Hardware Technology Parks, Software Technology Parks, Biotechnology Parks and Deemed Exports.

12.12 Keywords

Duty drawback: It is an incentive given to the exporters of different categories of goods under the "Customs and Central Excise Duty Drawback Rules, 1995".

Duty Entitlement Passbook Scheme: The exporters are allowed to claim customs duty credit as a specified percentage of FOB value of exports made in freely convertible currency.

Excise is a tax on production or manufacture of goods.

Export Promotion Capital Goods Scheme: It focuses on less costly imports of capital goods for the exporters to increase their cost and manufacturing competitiveness in the international markets.

Value Added Tax: VAT is a tax on such value addition at each stage. It provides for set off of tax paid on purchases at each point of sale

12.13 Review Questions

1. What are the excise procedures available to exporters in India for exporting goods without excise duty?
2. Discuss the various import concessions available to exports from India.
3. What is meant by a SEZ? Discuss the benefits available to units working from SEZs.
4. Write a detailed note on EOUs and units working from EHTPs, STPs and BTPs in India.
5. Attempt short notes on: (i) Star Export Houses, (ii) Deemed Exports, (iii) Form H, (iv) Duty Drawback, (v) Free Trade & Warehousing Zones

Notes

Answers: Self Assessment

1. Sales tax
2. VAT
3. zero
4. Excise
5. excise duty
6. Exports
7. six
8. Duty drawback
9. EDI
10. Drawback
11. Export Promotion Capital Goods Scheme
12. Licencing
13. DEPB (Duty Entitlement Passbook)
14. deemed
15. 24

12.14 Further Readings



Books

Aseem Kumar, *Export and Import Management*, 2007, Excel books

Cherenilan Francis, *International Economics*, 4th Edition, Tata McGraw-Hill Publishing Company Limited

Dr. Ram Singg, *International Trade Operations*, Excel books 2009

Pradeep Kumar Sinha and Sanchari Sinha, *International Business Management: A global perspective*, Excel books, 2008



Online links

www.slideshare.net/vinodraieng/export-incentives-12141898

www.fieo.org/uploads/files/xxx.pdf

www.exportscale.com/export_incentives.html



Case Study

Duty Exemption and Remission Schemes

The EXIM Policy (1997-2002) will become redundant after March 31, 2002, as a new comprehensive EXIM Policy for the next five years (2002-2007) is expected to be announced by the government of India (GUI) shortly. Though annual EXIM policies have been announced intermittently, they were within the broad framework of the five-year EXIM Policy (1997-2002). In this context, it is pertinent to highlight the issues encompassing the prevailing export-linked duty exemption and remission schemes on account of the liberalisation of imports through the phased elimination of quantitative restrictions (QRs) announced till March 31, 2001.

There are three export-linked duty free import schemes, viz, Advance Licensing Scheme (ALS) with duty exemption, Duty Free Replenishment Certificate (DFRC) and Duty Entitlement Pass Book (DEPB) schemes with duty remission. The ALS is a pre-export duty-free import facility whereas both DEPB and DFRC are post-export duty-free import schemes.

Advance Licensing Scheme; The ALS with Actual User (AU) condition facilitates duty-free import of inputs required for export production subject to the fulfilment of a time-bound export obligation. The material inputs and consumables such as oil, fuel, energy, catalysts, etc, used in the production of products exports can be imported against an advance licence without duty. Advance licences can be issued for physical exports, intermediate supplies and deemed exports. Imports against advance licences are exempted from payment of basic customs duty, additional customs duty, antidumping duty and safeguard duty. But countervailing duty, if any, has to be paid. The EXIM policy announced for the year 2001-02 has modified the ALS by raising the entitlement in certain cases, fixing new standard input-output norms (SIGN) for 506 items, coverage of additional ports under the scheme, simplification of the formalities, etc.

Duty-free Replenishment Certificate Scheme: The import under DFRC is exempted from basic customs duty and special additional customs duty. However, additional customs duty is payable but it can be drawn back through CENVAT as far as manufacturer exporters are concerned. Under DFRC, anti-dumping, safeguard and countervailing duties, if any, are payable. Imports of products for which SION have been notified by the Directorate General of Foreign Trade (DGFT) are eligible for DFRC except those for which AU condition is mandatory. The DFRC is also subjected to a minimum value addition of 33.3 per cent in the FOB value of exports. Though nexus (between exported products and imported items) is mandatory, the DFRC and the materials imported against it are freely transferable. The EXIM Policy for 2001-02 has modified DFRC scheme by raising the validity from 12 to 18 months, incorporating the provision for claim of DFRC against advance payment of import duty, coverage of additional ports, split-up facility, automatic calculation of CIF value without reference to international prices of individual inputs, etc.

The exporters can thus opt for either the pre-export licensing route of ALS or post-export licensing route of DFRC to import materials and other consumables used in the production of products for export.

Duty Entitlement Pass Book Scheme: DEPB provides for duty-free imports by exporters without passing through any licensing route. Under the DEPB scheme, the incidence of customs duty payable on the import content of the export product is neutralised by granting duty credit against the export product. The duty credit under the scheme is calculated on

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the basis of the deemed import content of the concerned export product as per SION, respective basic customs duty and value addition (subject to a minimum of 33.3 per cent) achieved in export. The import under DEPB is exempted from the payment of additional and special additional custom duties. However, anti-dumping, safeguard and countervailing duties, if imported against it are freely transferable. The EXIM Policy for 2001-02 has modified the scheme by adding a provision for claiming DEPB against advance payment of import duty, rationalisation of the DEPB rates in line with the changes in customs duty in the budget, coverage of additional ports, etc. It is learnt that the DEPB scheme may not continue in the present form in the forthcoming EXIM policy since certain existing provisions have been identified as incompatible with the relevant provisions of the World Trade Organisation (WTO).

These schemes have been implemented with the main purpose of encouraging the exporters by facilitating duty-free import of quality inputs at international prices. Thus the duty-free imports are expected to enhance the competitiveness in cost and quality of Indian products in the world market. The perceived objectives of the schemes are well-founded against the crucial need to enhance export earnings. However, the range of products that can be imported under these three schemes has been widened over time on account of the phased elimination of QRs and removal of other import restrictions.

Elimination of quantitative restrictions: Under Article XI of the GATT 1994, no prohibitions or restrictions other than duties, taxes or other charges shall be initiated or maintained, by any contracting party on importation and exportation of any product. Notwithstanding the provisions under the Article XI, quantity or value based restrictions on imports can be applied to safeguard the external financial and BOP positions of the contracting parties (Articles XII and XVII of the GATT 1994). Again, QRs and other import restrictive measures can be applied on grounds related to the protection of public morals, human life, animal life; plant life, national treasures, etc (Article XX of the GATT 1994) and on national security grounds (Article XXI of the GATT 1994). By 1997, India had successfully negotiated a mutually agreeable solution to phase out QRs taken on BOP grounds over a six-year period ending March 31, 2003. But when the Dispute Settlement Panel and Appellate Body of the WTO ruled against India in a dispute filed by the US, India had to commit the removal of QRs before April 1, 2001. On March 31, 2000, QRs on 714 items were removed followed by the removal of QRs on another 715 items on March 31, 2001. Thus by 2001, QRs on 9,363 tariff lines (at HS 10-digit level) have been dismantled. However, India is still maintaining QRs on around 800 items under Articles XX and XXI of the GATT 1994. Though the elimination of QRs was initiated in the early 1990s, the hue and cry against it has acquired momentum only during recent years. The main reason for the phenomenon was that most of the products for which QRs have been removed during the recent years are widely used consumer goods and sensitive items [Goldar and Mehta 2001: 990-91]. In order to tackle the consequences of the removal of QRs, the EXIM policy announced on March 31, 2001 included the creation of a 'war-room' to track, collate and analyse import data on 300 sensitive items which are of importance to the public and advise the government if situations of massive imports of any items arise [GOI 2001: 13]. Perspectives on Rationalisation of Duty Exemption and Remission Schemes: Under ALS and DFRC, all items with SION and meeting other conditions can be imported but licensing is mandatory. Hence, the authorities in times of exigency have the liberty to restrict imports of certain items on an ad hoc basis though the same is not evidently established in the relevant orders or EXIM policy. But with the liberalisation of imports and elimination of different non-tariff barriers, the chances of a prohibition of the duty-free import of individual items have become remote. Under the DEPB scheme, any item for which QRs do not exist can be imported. Thus the range of items which can be imported under DEPB got widened with

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each phase of the elimination of QRs. Now, all items except those for which QRs are still operative (numbering around 800) can be imported under DEPB.

Duty-free imports are more detrimental compared to imports under OGL from the angle of the domestic producers. Under a fully WTO-compatible trade regime (which India has committed to design), the only weapon available in normal circumstances to check imports which are injurious to the domestic industry is the flexibility in the fixation of customs duty subject to the committed bound rates. But as import under the export-linked schemes are duty-free, surge in such imports cannot be arrested through the tariff rate mechanism. Hence, it is necessary to rationalise the duty exemption and remission schemes so as to control duty-free import of sensitive and vulnerable items. As imports under the duty exemption and remission schemes are not related to the bound rates committed under Article II of the GATT 1994, GOI has the liberty to restrict the number of items and quantity imported through the duty-free channels. Otherwise, a surge in duty-free imports of sensitive and vulnerable products may signal transfer of investible resources from the respective sectors of the economy leading to eventual dependence on external sources. Moreover, the potential repercussions of the perceived trend may lead to hardship for small and marginal farmers and gradual collapse of inputs and intermediate products manufacturing segments of the industry in the long run. Therefore, relevant provisions have to be clearly spelt out in the new EXIM policy empowering the government to control duty-free import of vulnerable items through duty exemption and remission schemes at times of emergency. In the absence of such relevant provisions, GOI will have serious constraints in countering the surge in imports of sensitive products through duty-free channels.

Question:

What do you understand by Duty-free replenishment certificate scheme? Discuss the scheme in detail.

Notes

Source: <http://wtocentre.iift.ac.in/DOC/Duty%20Exemption%20and%20Remission%20Scheme.pdf>

Unit 13: Special Economic Zones

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Objectives

After studying this unit, you will be able to:

- Explain Special economic zones
- Discuss the Procedure for setting up SEZ
- Describe Approval of new units
- Discuss the Present debate on SEZ

Introduction

Realizing and anticipating that export are vital to the country's economic success, India was one of the first Asian countries to recognize the significance and effectiveness of the Export Processing Zone (EPZ) model in promoting exports from the country, which resulted in setting up of the first EPZ in Asia at Kandla (Gujarat) in 1965. India subsequently extended its policy of Export Processing Zones to other places in the country for the purposes of tapping its innate skills of manpower, natural resources and for accumulating foreign reserves through exports for the larger development of the country. EPZs in India have played a great role in export expansion, though not comparable to China. India's exports through EPZs increased from ₹ 10 lakh in 1965 to \$1 billion in the late nineties. On the other hand, Shenzhen SEZ1 alone has attracted an investment of \$38 billion and is now the backbone of China's export success in the international market. Taking note of the success of SEZs in other countries, particularly in China, the Government of India realized the need to overcome the shortcomings that our EPZs have been experiencing on account of the multiplicity of controls and clearances; absence of world-class infrastructure, high transaction cost and an unstable fiscal regime. The Government of India decided to replicate the Chinese success story in India with model changes in its the Special Economic Zones (SEZs) Policy, which was announced in April 2000 for the purposes of promotion of export, providing world-class infrastructure, reducing transaction cost of export-oriented firms resulting in low cost of Indian product in international market, making India a global centre of manufacturing, trading and services and attracting larger foreign investments in India.

Table 13.1: SEZ – The Growth Engine

Notes

Year	Value of Physical Exports from SEZs (₹ crore)	Growth Rate (over previous year)	Otherwise Country Export Growth Rate
2003-2004	13,854	39%	24.91%
2004-2005	18,314	32%	21.62%
2005-2006	22,840	24.70%	22.13%
2006-2007	34,615	52%	21.83%
2007-2008	66,638	92%	19.01%
CAGR since 2003-04		81%	23%

Source: Inputs from Ministry of Commerce, GOI.

SEZ is a special geographical area created within the country with economic laws that are different from a country's typical economic laws, with the major objective of attracting foreign investment to the country and ensuring the effective utilization of a country's physical and non-physical resources in shaping economic success. Alternatively, in economic terms; it can be said that SEZ is specifically delineated duty-free enclave and shall be deemed to be foreign territory within the country for the purposes of international trade operations, duties, tariffs and foreign exchange laws. Countries where SEZs have been very successful in export promotion and external economic engagements are China (highly successful), the UAE, Malaysia, India, Jordan, Poland, Kazakhstan, the Philippines, Russia and to some extent North Korea. At the beginning of 2008, there were over 4,000 special investment zones in the world. Countries like China, the UAE and Malaysia have emerged on the global trade map in a very short span of time due to SEZs, because of following reasons:

1. SEZs have emerged as focal points for promoting foreign investments in the country.
2. It is estimated that SEZs have attracted almost over 20% of foreign direct investment into these country.
3. SEZs have contributed almost 25% of these country's exports to overseas markets.
4. SEZs have served as testing grounds for economic and trade reforms and industrial policies for these governments.
5. SEZs have helped in improving the competitiveness of local and indigenous industry, job creation, local skill upgrading and technology absorption as the overall economic environment of the country get a boost from FDI, international business and management practices and norms.

India began modifying and restructuring its EPZ on the Chinese SEZ model from April 1, 2000. Initially, the legislation governing SEZs was under the Foreign Trade Policy and it used to have so many lacunae like lack of central legislation defining the role and rationale of SEZ, rigid labour laws and was implemented through piecemeal, with ad-hoc amendments to different laws, besides executive orders resulting in non-takeoff of the SEZs in India. India has been rather envious of China's larger and more successful Special Economic Zones. Sensing that a central legislation is essential for attracting investments (see table 13.2), ensuring good working environment, cutting red tape and bureaucracy and instilling confidence among developers and investors is essential, the Government of India provided a long-term and stable policy framework with minimum regulation and enacted the SEZ Act, 2005. This Act provides an umbrella legal framework, covering all important legal and regulatory aspects of SEZ development as well as for units operating therein.

Notes

Table 13.2: How SEZs Drive Foreign Investments in India

Financial Year	Amount of FDI inflows (in US\$ million)
1991-1992	167
1996-1997	2,770
2000-2001	2,908
2003-2004	2,634
2004-2005	3,755
2005-2006	5,549
2006-2007	14,400
2007-2008	24,600
2008-2009	32000
1. Total investment in Special Economic Zones as of 30.6. 2008: ₹ 81093 crores	
2. Incremental investment since February, 2006: ₹ 77058 crores	

The role of state governments in SEZ legislation got enhanced as it was decided that land would often be provided for SEZ purposes by state governments at concessional rates, and both developer and operating units are entitled to tax exemption up to 15 years subject to the condition that they are export-oriented and net foreign exchange earners. Red tape and inspector raj regulations were cut short as the provisions in the SEZ Act ensured the single window clearance mechanism for the units located in the zone.

13.1 Scenario Comparison of SEZs in India and China

SEZs have been very successful in export promotion, improving economic and investment climate and employment generation in China as well as in India. India has adopted the Chinese model of SEZs but its benefits cannot be expected to be the same as in China's case, because of the following vital differences in the Indian model of Special Economic Zones:

1. Special Economic Zones in China or Free Zones in the UAE are mostly state-funded with the objective of enhancing economic gains and prospects for foreign investment, improving industrial climate and do not suffer from worries regarding financial viability. The Chinese model is based on the communist approach of state planning and the UAE model is based on immense wealth generated from oil exports. Free Zones in the UAE are largely developed as Service Centres or Trading Centres. In China as well as in the UAE, it is the respective governments that are responsible for marketing and promoting these zones so as to invite and attract tenant industries for the purposes of manufacturing trading and services. On the other hand, the Indian model is largely based on market forces such as the interest of private players based on viability of the project and it is mostly private sector that has to shoulder the responsibility or risk of financing, marketing and promoting these zones for attracting possible tenants or units. Unfortunately, Indian industry is still naive, inexperienced but is learning fast for developing Special Economic Zones in the country.
2. India is a democracy, with a weak federal government and plenty of regional disparities. The Central Government, in practice, does not command the Indian economy, as there are regional aspirations, petty politics, and peasant movements. SEZs in India are very small as compared to China. Foreign investment is also not confined only to SEZs but is also moving in domestic tariff areas unlike in China, which has developed SEZs mainly to channelise foreign investment into the country for capacity enhancement realizing that Taiwan and Hong Kong no more have the scope for such capacity enhancement in trading, services and manufacturing. It seems China has successfully banked on the constraints of the Taiwanese and Hong Kong economies for attracting investors in SEZs.

3. China has offered several additional tax sops and incentives with favourable working environment, world-class infrastructure and liberal labour legislation. China, being an authoritarian communist state has successfully tamed its labour unrest. On the contrary, India being a democracy is has to contend with trade and labour unions. The Congress-led UPA coalition government, buckling under the supporting Left parties' pressure was compelled to withdraw Section 50(b) of SEZ Act, which empowered the state government to liberalize labour laws for SEZs located in their states. India has strong labour unions, usually affiliated to political parties. A small unrest becomes a national issue unlike China, which uses liberal and simple labour laws as economic levers to attract investments and industries from the global marketplace.
4. SEZs in the services sector have been very successful in India and in case of manufacturing, in China. As compared to China, India has some advantages that include significantly, a very large English-speaking workforce, skilled manpower for the IT and IT-enabled sectors, biotechnology, drugs and pharmaceuticals and immense untapped potential for agro-based industries. It is expected that India will eventually become a global services hub with large scale high-tech exports. India will derive benefits from SEZs in capacity development, forward integration and skill under process, unlike China, which has focused on undifferentiated production of commodities with a clear cut strategy of mass production and mass consumption so as to tap the economies of scale.
5. China has been ahead of India in its economic engagements with the global economies, particularly with ASEAN and Africa. It has far deep economic relations with almost all countries in East, South East, Middle East and South Asia and a major chunk of investment has flown into China from these regions. India on the other hand, has focused on developed countries, particularly in the EU and NAFTA Regions and has been late in deepening its relationship with its immediate neighbours for investment attraction and exports.

13.2 Special Economic Zones

As discussed, the policy of SEZs was adopted by the Government of India in order to instil confidence among foreign investors and to ensure a one-window clearance under a stable central legislation for the prospective investors, developers and units to be located in the SEZs. The SEZ Act has ensured clarity, stability and consistency regarding the various benefits/incentives offered by the government for promoting exports from the country, thereby generating greater economic activity and employment through the establishment of SEZs in all areas of manufacturing, services and logistical value chain. An umbrella and comprehensive draft SEZ Bill was prepared after extensive discussions with the various stakeholders in order to improve the country's economic growth, environment and regime in the LPG & M era. The Ministry of Commerce, Government of India planned a number of visits and interaction with various stakeholders throughout the country so as streamline the SEZ bill as per industry and investor aspirations and give momentum to exports. The draft of the SEZ Bill received around 800 comments/suggestions from economic and trade experts, Industry associations, investors, agriculture farmers and chambers of commerce. Finally, the Special Economic Zones Act, 2005, was passed by Parliament and the SEZ Act, 2005, supported by SEZ Rules 2006, came into force on February 10, 2006, opening a new chapter in India's economic liberalization history and paving the way for drastic simplification of procedures and for single window clearance on matters relating to central as well as state governments. The main objectives of the SEZ Act are:

1. Ensuring that SEZs may act as generator of additional economic activity for quicker economic development.
2. Looking forward to SEZs becoming the centres of excellence in India's efforts for promotion of exports of goods and services.

Notes

3. Ensuring that simplification of procedure and cutting down the red tap will result in promotion of investments from domestic and foreign sources.
4. Maintaining that SEZ will help in creation of employment opportunities for the people of the country.
5. Envisaging SEZs helping in development of infrastructure facilities in backward areas and tapping the country's innate resources.
6. Looking forward to SEZs becoming major centres of activity in realizing the cherished dream of making India a world-class centre of manufacturing, trading and services and putting it in the league of global export champions.

Table 13.3: What activities can be planned in SEZs

Manufacturing /Trading	Service
1. Apparel, Garments and Leather	1. IT-enables services, Biotechnology
2. Automobile and Auto Components	2. R & D Services
3. Engineering– Light, Heavy and Application	3. Healthcare
4. Pharmaceuticals	4. Financial Services
5. Food Processing	5. Knowledge (Education) Services
6. Telecom Equipment	6. Entertainment, Leisure and Recreation
7. Computer Hardware and Microelectronics	7. Sports and Related Activities
8. Consumer Electronics and Appliances	8. Organized Retail
9. Gems, Jewellery and Diamonds	9. Business Services (Convention/Exhibition)
10. Wood, Rubber, Plastic and Leather Products	10. Warehousing and Trade-related Services
11. Handicrafts	

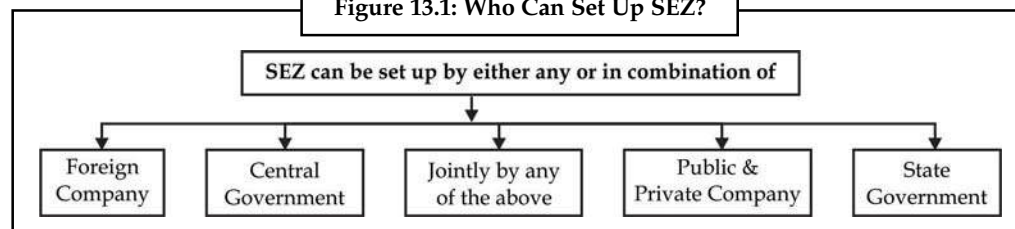
Source: Inputs based on SEZ Act 2005 and SEZ Rules 2006

The SEZ Act 2005 is unique in the sense that it also envisages a key role for state governments in export promotion and creation of related infrastructure and thus involves state governments as active partners in export promotion. Application for setting up SEZ will be processed in Single Window Approval Mechanism (SWAM) through a 19-member inter-ministerial SEZ Board of Approval (BoA). The applications, which are duly recommended by the respective state governments/UT administration, shall be considered by the BoA periodically, for consensus on setting up SEZs.

13.2.1 Procedure for Setting up SEZ

In India, SEZs can be set up by state governments, or their various agencies or the public, private or the joint sector. Even foreign companies can set up SEZs in India.

Figure 13.1: Who Can Set Up SEZ?



Source: Inputs based on SEZ Act 2005 and SEZ Rules 2006

For setting up SEZ, the interested party has to fill up an application with the name, address, and status of the developer and co-developer. The developer is also required to submit a project report with details about the proposed location of SEZs, details of infrastructure that already exists, details of infrastructure that will be established, and the total area of the proposed SEZ. The project report of the proposed SEZ that will be submitted along with the application form should also contain investment details, which would include the financing mode and the project's viability. It should also contain details as to whether the proposed SEZ would be a multi-product or specific industries zone and foreign equity details. The application, along with the project report for the setting up of an SEZ unit, is submitted to the Chief Secretary of the State.

Table 13.4 Approval Procedure of Setting up an SEZ in India

Form-A	Proposal by person intending to set up SEZ to the concerned state government	Proposal may also be made directly to the board; after approval by the board, the person will require to obtain state government concurrence within a period of 6 months.
First Step		
Second Step	The state government forwards the proposal along with its recommendations to the board	Within 45 days; the state government to ensure that requirements of minimum land area, and the exemption of taxes at state level, delegation of powers to DC as recommended are made available to developer and units
Third Step	Approval or refusal by board	The board may approve the proposal with or without modifications, or reject it. In practice, the board accords in-principal approval pending land acquisition in Form B-1
Form-B	Issuance of letter of approval by the Government of India	Within 30 days of receipt of BOA recommendation; LOA will incorporate any additional conditions imposed by the board in its recommendation. LOA validity is for 3 years, during which time the developer shall take effective steps to implement the approved proposal.

The state government in turn forwards the application to the Board of Approval, Department of Commerce, and Government of India. State governments have to give their commitment that the area where the proposed SEZ will be set up is free from all kinds of environmental restrictions and it would provide electricity, water, and various other services when required, and that it would allow transmission, generation, and power distribution inside the SEZ along with the application. Further, the state government has to give the commitment that it would exempt the proposed SEZ from sales tax, turnover tax, and Mandi tax on the goods supplied from the area of domestic tariff to the units in the SEZ. Also, the government of the state has to give the commitment that it would declare the units of the SEZ as public utility service and that the system of single point clearance and minimum inspection would be provided to the SEZs. The Board of Approval will consider such application forwarded to it by state governments and will issue a permission letter or refusal note to the developer of SEZ and also inform the state government.

Table 13.5: Who's Who in SEZ Approval Committee (BOA)

1.	Secretary, Department of Commerce	Chairman
2.	Member, CBEC	Member
3.	Member, IT, CBDT	Member
4.	Joint Secretary (Banking Division), Department of Economic Affairs, Ministry of Finance	
5.	Joint Secretary (SEZ), Department of Commerce	Member
6.	Joint Secretary, DIPP	Member

Contd...

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7.	Joint Secretary, Ministry of Science and Technology	Member
8.	Joint Secretary, Ministry of Small Scale Industries and Agro and Rural Industries	Member
9.	Joint Secretary, Ministry of Home Affairs	Member
10.	Joint Secretary, Ministry of Defence	Member
11.	Joint Secretary, Ministry of Environment and Forests	Member
12.	Joint Secretary, Ministry of Law and Justice	Member
13.	Joint Secretary, Ministry of Overseas Indian Affairs	Member
14.	Joint Secretary, Ministry of Urban Development	Member
15.	A nominee of the State Government concerned	Member
16.	Director General of Foreign Trade or his nominee	Member
17.	Development Commissioner concerned	Member
18.	A professor in the Indian Institute of Management or the Indian Institute of Foreign Trade	Member
19.	Director or Deputy Secretary, Ministry of Commerce and Industry, Department of Commerce	Member Secretary

Source: SEZ Act 2005

13.2.2 Criteria for Approval

Proposals for setting up SEZ in the public/private/joint/state sector are required to meet the following conditions:

1. The minimum size of the multi-product SEZs shall not be less than 1,000 hectares but it would not apply to existing EPZs, which are converted into SEZs. The minimum area requirement for SEZ for specific sectors is 10 hectares. For small states such as Goa and

Table 13.6: Defining Processing and Non-Processing Areas in SEZ

Processing Area	Non-Processing Area
1. The processing area is that area in an SEZ where units can be located for the manufacture of goods or rendering of services.	1. The non-processing area is the area which is intended to provide support facilities to the SEZ processing area activities
2. The processing area shall have specified entry and exit points and be fully secured by taking such measures approved by the board.	2. No vacant land in the non-processing area shall be leased for business and social purposes such as educational institutions, hospitals, hotels, recreation and entertainment facilities, residential and business complexes, to any person except a co-developer approved by the board.
3. The land or built-up area or free trade warehousing zone shall be given on lease only to the entrepreneurs holding a valid Letter of Approval and shall not be less than 5 years. The lease rights would cease to exist on the expiry or cancellation of the LOA.	3. The developer or co-developer may lease the completed infrastructure along with the vacant land.
	4. The infrastructure for business or social purpose in the SEZ as approved by the board shall be entitled for exemptions, concession and drawbacks.

Source: SEZ Act 2005 and SEZ rules.

Sikkim, there is relaxation in minimum area for setting up SEZ as these states have land constraints owing to their smaller size. The table below gives a comprehensive explanation regarding the minimum size, built-up area and any relaxation in setting up SEZ.

2. The SEZ units are supposed to abide by local laws, rules, regulations or bye-laws with regard to local area planning, sewerage and disposal system, pollution control mechanism and the like. They are also required to comply with industrial and labour laws and such other laws/rules and regulations as may be locally applicable to other units for ensuring better administration and management of area. Hence the SEZ developer is required to make adequate arrangements to fulfil all the requirements of laws, rules and procedures applicable to such SEZ.
3. Only those units that are approved under the SEZ schemes for setting up in SEZ zones are permitted to be located in the SEZ.
4. The developer is required to ensure that at least 50% area of the SEZ shall be used for processing purposes, such as developing industrial area for setting up such units.

Table 13.7: Minimum Area Requirement Stipulated for Various Categories of SEZs

Type	For states other than special category states/UTs		Areas for special category states/UTs	
	Minimum Total Area Requirement	Processing Area Requirement	Minimum Total Area Requirement	Processing Area Requirement
Multiproduct	1000 Hectares	35%	200 hectares	35%
One/more services	100 hectares	50%	100 hectares	35%
Sector specific/port/airport	100 hectares	50%	50 hectares	50%
Electronic hardware and software or information technology enabled services	10 hectares with minimum built up area of one lakh sq. mts	50%	10 hectares with minimum built up area of 1 lakh sq. mts	50%
Gems & jewellery	10 hectares with minimum built up area of 50 thousand sq. mts	50%	10 hectares with minimum built up area of 50 thousand sq. mts	50%
Bio-tech/non conventional energy including solar energy equipments/cells	10 hectares (and minimum built up area of 1 lakh sq. mts for IT)	50%	10 hectares (and minimum built up area of 1 lakh sq. mts for IT)	50%
Free trade warehousing zone	40 hectares (min. built up area of 1 lakh sq. mts)	50%	40 hectares (min. built up area of 1 lakh sq. mts)	50%

Source: Inputs based on SEZ Act 2005 and SEZ Rules 2006

Notes

Self Assessment

Fill in the blanks:

1. India was one of the first Asian countries to recognize the significance and effectiveness of the model.
2. EPZs in India have played a great role in expansion.
3. SEZ is a special geographical area created within the country with economic laws that are different from a country's typical laws, with the major objective of attracting foreign investment to the country.
4. SEZs have emerged as focal points for promoting foreign in the country.
5. The Act has ensured clarity, stability and consistency regarding the various benefits/incentives offered by the government for promoting exports from the country.
6. The SEZ Act 2005 is unique in the sense that it also envisages a key role for in export promotion and creation of related infrastructure.
7. The minimum size of the multi-product SEZs shall not be less than hectares.
8. For small states such as Goa and Sikkim, there is relaxation in minimum area for setting up SEZ as these states have land constraints owing to their smaller
9. The developer is required to ensure that at least area of the SEZ shall be used for processing purposes, such as developing industrial area for setting up such units.
10. The functioning of the SEZs is administered in a way that there shall be hassle-free regulatory environment with minimum chances for and control.

13.3 Approval of New Units

In case one wishes to set up a unit in the Special Economic Zones; he needs to submit a proposal for setting up units under EOU/SEZ scheme under the automatic route to the Unit Approval Committee, which will consider the following points while extending the permission for the same:

1. Proof of residence in respect of individual/partnership firms of all directors/partners. (Passport/ration card/driving licence/voter identity card or any other proof to the satisfaction of Development Commissioner;
2. Income tax returns of all the promoters for the last three years;
3. Experience of the promoters;
4. Marketing tie-ups;
5. In case of EOUs, inspection of the project site by an officer;
6. A report from other DCs as to whether any case under SEZ/EOU Schemes in regard to diversion of goods, etc. is pending.

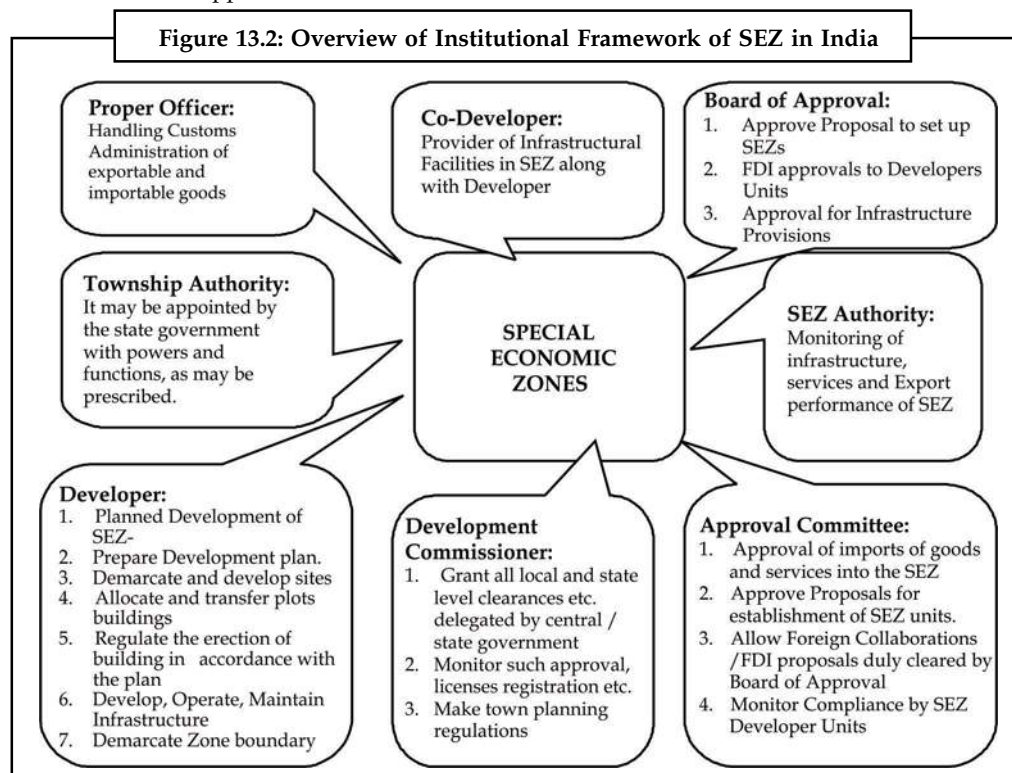
Whether necessary, the above may be verified through personal interview with the promoters of the project. In the event of the promoters being a well-established entity, the procedure of personal interview may be dispensed with. The Unit Approval Committee shall meet every week on Monday. In case of the absence of the Development Commissioner, the next senior

officer in the Zone will hold the meeting. The unit shall intimate the problems it faces in advance. In the meetings, apart from the promoters, the other concerned agency with which difficulties are being faced by the unit may also be called.

13.3.1 Administrative and Institutional Set Up of SEZ

The functioning of the SEZs is administered in a way that there shall be hassle-free regulatory environment with minimum chances for red tape and control. The regulatory administration mainly comprises of the Board of Approval, Approval Committee and Development Commissioner. A Proper Officer of Customs is deputed to look after day-to-day functioning with regard to customs administration. The Board of Approval is the apex body and is headed by the Secretary, Department of Commerce. The Approval Committee, which deals with approval of units in the SEZs and other related issues, acts at zone level only. A Development Commissioner, who is also the ex-officio chairperson of the Approval Committee of the Zone, heads each Zone.

Once the Board of Approval approves an SEZ and the Central Government has notified the area as the Special Economic Zone, units can be set up in the SEZ. All proposals for setting up of units in the SEZ are approved at the Zone level by the Approval Committee consisting of the Development Commissioner, customs authorities and representatives of the state government. All post-approval clearances including grant of importer-exporter code number, change in the name of the company or implementing agency; broad-banding diversification, etc. are given at the Zone level by the Development Commissioner. The performances of the SEZ units are periodically monitored by the Approval Committee and units are liable for penal action under the provision of Foreign Trade (Development and Regulation) Act, in case of violation of the conditions of the approval.



Source: Author Constructions based on SEZ Act 2005 and SEZ Rules 2006

Notes



Note The other important institutional agency that facilitates the working and functioning of SEZ are township authority, which may be appointed by the state government to look after the local and command area development and ensure that township may have full-fledged facilities and services as prescribed under the rules.

SEZ Authority monitors the overall performance of SEZ vis-à-vis export performance and infrastructural improvement in the area. The developer is the lead person or company who has the responsibility for development of the SEZ. Sometimes, there can also be a co-developer as the size of SEZ may be very big or the developer may want to include a co-developer so as to use his specialised knowledge in development of SEZ or to meet the financing requirement.

13.3.2 Incentives and Facilities to the SEZs

The following benefits/incentive are available to SEZ developers and SEZ units in Special Economic Zones and are categorized as under:

1. Incentives and Facilities available to SEZ Developers:
 - (a) Exemption from customs/excise duties for development of SEZs for authorized operations approved by the BOA.
 - (b) Income tax exemption on income derived from the business of development of the SEZ in a block of 10 years in 15 years under Section 80-IAB of the Income Tax Act.
 - (c) Exemption from minimum alternate tax under Section 115 JB of the Income Tax Act.
 - (d) Exemption from dividend distribution tax under Section 115 O of the Income Tax Act.
 - (e) Exemption from Central Sales Tax (CST).
 - (f) Exemption from Service Tax (Section 7, 26 and Second Schedule of the SEZ Act).

Table 13.8 Fiscal Incentives/Benefits to Developer and Units in Special Economic Zones

S. No.	Types of Benefit	Nature and Description of Benefits	Legislative Provision
1.	Income tax holiday (for units in SEZs)	1. For first five years: 100% of the eligible profits or gains. 2. Next five years: 50% of the eligible profits or gains 3. Next five years: 50% of the eligible profits or gains subject to creation or specified reserve.	Section 10AA of the Income Tax Act 1962
2.	Income tax holiday to developer	Deduction of 100% of profits derived from developing an SEZ for a period of 10 consecutive assessment years out of the first 15 years from the year in which the SEZ is notified by the Central Government	Section 80 -IAB of the Income Tax Act 1962
3.	Minimum Alternate Tax	Exemption from the provisions of Minimum Alternate Tax for developer as well as SEZ unit.	115JB of the Income Tax Act 1962
4.	Service Tax	Exemption from Service Tax under chapter VI of the Finance Act 1994 on taxable services provided to a developer or unit to carry on authorized operation in an SEZ	Under CENVAT Rules 2004

Contd...

				Notes
5.	Provisions regarding capital gains	Exemption from capital gains or transfer of specified assets in consequence to shifting of industrial undertaking from urban or other areas to SEZ subject to certain conditions.	Under Income Act 1962	
6.	Custom Duty relief	Exemption from customs duties for development of SEZ for authorized operation approved by BOA	Under Customs Act 1962	
7.	Excise Duty	Exemption from any duty or excise, under the Central Excise Act, 1944 or the Central Excise Tariff Act, 1985 or any other law for the time being in force, on goods brought from Domestic Tariff Area to a Special Economic Zone or Unit, to carry on the authorized operations by the developer or entrepreneur.	Central Excise Act 1944 and Central Excise Tariff Act 1985	
8.	Dividend Distribution Tax	Exemption from Dividend Distribution Tax declared or paid after 1st April, 2005 by an enterprise engaged in developing or developing and operating or developing, operating and maintaining a SEZ.	115 O of the Income Tax Act 1962	
9.	Securities Transaction Tax	Exemption from the Securities Transaction Tax leviable under Section 98 of the Finance (No.2) Act 2004 in case the taxable securities transactions are entered into by a non-resident through the International Finance Service.	Under Income Act 1962	
10.	Import Duty	Duty-free import domestic procurement of goods for development, operation and maintenance of SEZ units.	Under Customs Act 1962	
11.	Central Sales Tax	Exemption from Central Sales Tax/VAT on sale or purchase of goods.	Under Central Sales Tax.	

1. *Incentives and Facilities to Units in SEZs:*

- (a) 100% Income Tax exemption on export income for SEZ units under Section 10AA of the Income Tax Act for first 5 years, 50% for next 5 years thereafter and 50% of the ploughed back export profit for the next 5 years.

Table 13.9: Types of SEZ in India

Free Trading and Warehousing Zones	SEZ for Multi-Product	SEZ for Sector Specific	SEZ in a Port or Airport
Free trading and warehousing is a special category SEZ with a focus on trading and warehousing. The objective of such a zone is to create trade - related infrastructure to facilitate import and export and import of goods and services with freedom to carry out trade transactions in free currency. In a standalone free trading and warehousing zone, at least 50% of the area shall be earmarked for developing processing area. Free trading and warehousing may also be set up as a part of SEZ for multi product.	"Special Economic Zone for multiproduct" means a Special Economic Zone, where units may be set up for manufacture of two or more goods in a sector, or goods falling in two or more sectors, or for trading and warehousing, or rendering of two or more services in a sector, or rendering of services falling in two or more sectors.	"Special Economic Zone for specific sector" means a Special Economic Zone meant exclusively for one or more products in a sector or one or more services in a sector.	"Special Economic Zone in a port or airport" means a Special Economic Zone in an existing port or airport.

Source: SEZ Act 2005 and Rules 2006

- Notes**
- (b) Exemption from minimum alternate tax under Section 115JB of the Income Tax Act.
 - (c) External commercial borrowing by SEZ units up to US \$ 500 million in a year without any maturity restriction through recognized banking channels.
 - (d) Exemption from Central Sales Tax.
 - (e) Exemption from Service Tax.
 - (f) Single-window clearance for Central and state level approvals.
 - (g) Exemption from state sales tax and other levies as extended by the respective state governments.

13.4 Present Debate on SEZ

India, with a robust, booming and shining economy and favourable economic environment for further economic growth has witnessed a huge rush from private sector companies who are very keen to set up Special Economic Zones (SEZs) as they wish to make India a base for manufacturing, trading and services due to its cost advantages. The new SEZ legislation was approved in February 2006, and the government has already received over 500 applications till August 2008 out of which 250 have already been notified by the Board of Approval with Andhra Pradesh leading with 56 Special Economic Zones, Tami Nadu 41, and Maharashtra with 36. There were 19 notified SEZs, which include 7 EPZs converted into SEZs before the new legislation on SEZ was adopted in 2006. The new legislation that replaced the previous scattered approach of reference to different acts and rules making the process and execution cumbersome has opened a Pandora's box of debate on the utility and importance of SEZ in India, although new legislation provides a uniform SEZ policy and comprehensively covers all aspects of establishment, operation and fiscal oversight. Some of the major area of contention and debate are:

1. **Loss of revenue to the State:** Policymakers, including the central bank have cautioned on revenue implications from duty and taxes foregone from the mushrooming of SEZs across the country. The RBI is very critical of the SEZ policy and has time and again raised questions on the sustainability of revenue inflow to the state, which may cause severe mismanagement for public finances. Though, it is expected that SEZs would boost investment and economic growth in the country, they could also aggravate the uneven pattern of development by pulling out resources from less developed areas to more prosperous or coastal areas. Major SEZs are coming up in costal areas only because of transaction cost advantages.

The Finance Ministry is worried that the development of SEZs and the duty and taxes so forgone would result in unjustified revenue loss to exchequer (over ₹ 1,00,000 crores) due to direct tax drain only. It is expected that it will be around 0.5% to 0.7% of the GDP. The RBI has also echoed these concerns and has cautioned the government about such heavy revenue loss. It further emphasizes that such benefits/incentives may be justified if the SEZ units can ensure forward and backward linkages with the domestic economy, thereby catalysing greater competitiveness in the entire economy, rather than only in zones.

2. **Uneven economic development:** The success of SEZs in regional economic development largely depends how smartly the state can play its role in promotion of commercial activities from such zones, as the role of the state government is vital in the development of these zones. It has been seen in India that different state governments differ markedly in the quality of their vision, their capacity of built infrastructure and the political constraints under which they operate. For example, two Indian states namely Gujarat and Bengal have different stories with regard to development of SEZs. While Gujarat has been a leader in commencing operations from such zones, Bengal suffers consistent turmoil with

political and peasant problems leading to inertia in mindset. For instance, the Salim Group (chemicals), TCS (IT) and Infosys (IT and ITES) have refused to begin operations in Bengal due to unfavourable business climate.

3. **Misuse of agriculture land:** There were also allegations that a large portion of agriculture land was being converted into SEZs. This statement, however, holds no ground, as the total proposed area for SEZs is about 75,000 hectares, i.e., only 0.000625% of India's total area under cultivation.
4. **Most SEZs are driven by tax benefits only:** The current mushrooming on filing of SEZs is largely aimed at winning tax benefits offered to developers as well units under the present Act and Rules, which allow 100% exemption from corporate income tax for the first five years; 50% for the next five years and, for the final five years, 50% of the profits ploughed back will be exempt from tax to the units and an exemption for 10 years in block of 15 years to the developer. Another factor that has driven companies for filing many applications is that existing tax exemptions to export-oriented units such as STP/BTP are supposed to expire in financial year 20104.
5. **Indian SEZs do not have scale advantages:** We believe that one of the key purposes of SEZs is to build scale-related advantages. However, most of the SEZs currently being planned are minuscule in size. The new law allows the minimum area for SEZs to be 1,000 hectares (3.9 square miles) for multi-product zones, 100 hectares for product specific zones and just 10 hectares for IT, gems and jewellery and biotechnology zones (subject to minimum built-up area norms).

We believe that with the rapid globalisation of manufacturing scale, small SEZs appear to have outlived their relevance in today's environment. Among the ones announced, there are probably only two medium-scale SEZs being taken up for development. Both these zones are being set up by Reliance Industries, India's largest private-sector company.

The largest (in terms of size) is being set up in the state of Maharashtra near Mumbai. This is a twin SEZ project, a merger of Navi Mumbai SEZ and Maha Mumbai SEZ. The total size of this project is 12,000 hectares or 46 square miles. Phase I of the project, to be implemented by 2007, envisages an investment of US\$1.1 billion. The big advantage of the twin SEZs is their location. Given its proximity to the city of Mumbai, this SEZ should be able to leverage the city's infrastructure and will have easy access to quality manpower. The other large SEZ is being set up by Reliance in the northern state of Haryana. This SEZ will have a size of 10,000 hectares or 38 square miles. Both the Mumbai twin SEZs and Haryana SEZ projects are being set up on a PPP basis.

We believe that both these SEZs should be a big improvement over the current SEZs and better than most other new SEZs announced in the country. However, they will still be smaller than the major SEZs operating in China. The top three SEZs in China (i.e., Shenzhen, Xiamen and Zhuhai) cover 126, 51 and 47 square miles, respectively.

6. **Labour laws will still be an issue:** The new SEZ law is unlikely to address the critical issue of labour flexibility. A restrictive labour law environment has, in our view, been one of the major hurdles to the development of the Indian manufacturing sector. Currently, over 40 labour-related statutes have been enacted by the central government. In addition, state governments have enacted various statutes on this subject. The most restrictive central government regulation is the one that requires all employers with more than 100 employees to gain compulsory government approval (normally a long drawn-out process) before retrenching workers or closing part of an enterprise. This provision has not changed since 1982. As highlighted in the official report on employment released by the Planning

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Commission of India, although the law does not bar retrenchment or closure and only requires prior approval, in practice the Act has been interpreted in a way that has made retrenchment almost impossible. In practice, termination at the end of a probation period has also been treated as retrenchment, even if the termination was due to failure to pass a test that was a condition of employment.

The original draft of the new SEZ law intended to give state governments the freedom to allow implementation of flexible labour laws within the SEZ area. However, before the final approval from the lower house of parliament, the government was forced to drop this clause in the face of Leftist opposition. The National Common Minimum Program (NCMP) of the United Progressive Alliance also prevented the government from implementing a hire and fire policy. Labour being a Concurrent issue, individual states still have the option to amend their specific legislations to allow labour flexibility in SEZs set up under their jurisdiction.

7. **Private sector may not take up development of large SEZs needed:** Most of the infrastructure facilities for SEZs tend to be public. In addition, investment returns from SEZs tend to be spread over a long period. These investments are best suited for government balance sheets than the private sector. We do not expect the private sector to be very enthusiastic about undertaking such investments.
8. **Some policymakers oppose the SEZ law:** The Ministry of Finance (MOF) has been vocal in opposing the government's liberal approach towards the setting up of SEZs. The MOF has been concerned over potential revenue loss and has suggested an increase in the minimum area required. The government-appointed empowered group of ministers has decided against this. The government, however, has decided to cap SEZ approvals at 150 during the first six months after the notification of the SEZ Act (February 10, 2006). The government has also indicated that it will not allow the movement of existing businesses into SEZs. We believe that given the tax savings, companies may choose the new SEZ route for expansion plans that they otherwise would have pursued outside the SEZ area.
9. **Good concept, but poor execution:** Although, trade expansion in the last six years has been good at 23% CAGR, India's share in world goods exports is yet very small – at 1.5% for 2008. Experts say it is due to poor execution of policy framework governing international trade; red tape, bureaucracy and wrong handling of widely known gaps in the business environment. The existing SEZ policy does not seem to be in tune with Indian SMEs, which contribute almost 40% of India's foreign trade. The present SEZ policy has failed to create bigger inroads into small and medium scale manufacturing and trading. Efforts shall be made to make existing SEZs policy particularly helpful for small and medium-scale entities, which cannot afford to set up captive infrastructure facilities, but can certainly emerge as competitors in cost and scale of operations due to their specialization in horizontal production lines and can successfully attract foreign capital and technology in their specialized areas of activity. Moreover; India has to tailor its SEZ policy such that it should promote and encourage the country's manufacturing exports in international markets, so that India can also stand at par with China as a low-cost supplier of goods to world.
10. **Is undertaking large SEZs a real solution?:** One dimension of the present debate is that India should focus on developing large-size SEZs in a few key states. The prime motive of attractiveness of SEZs is low cost of operations due to good infrastructure and allied services. Hence the Central Government and key state government should pool their resources along with private sector players to create SEZs that can compete with China and attract foreign capital and technology.



Task Visit the Special Economic Zone website and study the various provisions for setting up a unit in one of the SEZs.

Notes

Self Assessment

Fill in the blanks:

11. Once the Board of Approval approves an SEZ and the Government has notified the area as the Special Economic Zone, units can be set up in the SEZ.
12. SEZ Authority monitors the overall performance of SEZ vis-à-vis export performance and improvement in the area.
13. Most of the infrastructure facilities for SEZs tend to be
14. The prime motive of attractiveness of SEZs is cost of operations due to good infrastructure and allied services.
15. The existing SEZ policy does not seem to be in tune with Indian SMEs, which contribute almost of India's foreign trade.

13.5 Summary

- In conclusion, we can say that India should continue its policy of SEZs in order to derive benefits of factors such as availability of a large and skilled workforce, intrinsic comparative advantage in several industries, a strong policy framework, availability of complementing and supporting ancillary industry, an already buoyant export sector and vast local markets.
- It is expected that through SEZs, India can combine these factors into a powerful alchemy to attract the best technology and large inflows of foreign investment.
- If domestic regulation is strengthened further, including looking at prevalent rigid labour laws, supportive bureaucracy, cutting down red tape, improving overall infrastructure, etc.
- SEZs could automatically become a panacea for all economic problems and diseases.
- Differences of opinions will always be there on the incentives, benefits and facilities to SEZs, but these shall not hamper India's march towards emerging as global hub for manufacturing, trading and services and regaining our past glory of being export champions by 2020 by garnering 5% share in world trade.

13.6 Keywords

Export: A function of international trade whereby goods produced in one country are shipped to another country for future sale or trade.

Import: A good or service brought into one country from another. Along with exports, imports form the backbone of international trade.

SEZ: SEZ is a special geographical area created within the country with economic laws that are different from a country's typical economic laws, with the major objective of attracting foreign investment to the country

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13.7 Review Questions

1. What are SEZ? How far SEZs have been successful in Indian Export Promotion Drive?
2. SEZ in China have been more successful than in India. Justify.
3. Discuss the procedure for setting up SEZ. What is the criteria for giving approval for SEZ?
4. Discuss the various benefits/incentives/subsidies available under India's SEZ Act and SEZ Rules 2006.
5. What are the main reasons of on-going debate on SEZ? Discuss.

Answers: Self Assessment

1. Export Processing Zone (EPZ)
2. export
3. economic
4. investments
5. SEZ
6. state governments
7. 1000
8. size
9. 50%
10. red tape
11. Central
12. infrastructural
13. public
14. low
15. 40%

13.8 Further Readings



Books

Aseem Kumar, *Export and Import Management*, 2007, Excel books

Cherenilan Francis, *International Economics*, 4th Edition, Tata McGraw-Hill Publishing Company Limited

Dr. Ram Singg, *International Trade Operations*, 2009, Excel books

Pradeep Kumar Sinha and Sanchari Sinha, *International Business Management: A Global Perspective*, Excel books, 2008



Online links

www.sezindia.nic.in/

www.eximguru.com/exim/special_economic_zone_sez/default.aspx

Unit 14: Information Technology in International Business

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14.2 E-Marketing

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Objectives

After studying this unit, you will be able to:

- Discuss the Introduction to IT in international business
- Explain Electronic procurement
- Describe Electronic Marketing
- Discuss Electronic Logistics

Introduction

Computerization has changed the way business is conducted the world over. No aspect of business has remained untouched by the information technology (IT) revolution. This is especially true of international business where people located in different parts of the world conduct transactions with each other. The activities of international business include manufacturing, inland transportation, customs and excise matters, port operation, shipping, clearing and forwarding. During the course of these transactions, a large number of documents are created and exchanged, many of these documents or the information contained therein is repeated, while creating and mailing these documents before the advent of IT., hundreds of man-hours would be lost in repetitive operation, innovations in IT have revolutionized international business; the use of technology in managing and processing information.



Note Especially in large organizations helps save time, bring down costs, and reduce manpower, manual data input and transfer has now become not only obsolete, but also irrational.

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Areas

In international business today, IT finds maximum utility in the following areas:

1. Electronic procurement
2. Electronic marketing
3. Electronic logistics

A modern competitive enterprise seeks to hold an edge over the market. IT helps provide this competitive advantage through its various applications tools. By adapting these tools in various areas of business, the organization can gain many advantages in terms of accessibility to a customer or supplier in any part of the world, speed of operations, reduction in manpower, etc. due to the reach of the internet it is possible to conduct buying and selling transactions irrespective of geographical location. Internet banking helps in the speedy execution of payments and settlement of accounts. A website can be a virtual showroom, where products can be displayed, demonstrated and sold. Such a website can also provide various after-sales service tips and suggestions, launch discussions forums, ask for customer feedback and educate the customer.



Did u know? IT application such as Electronic Data Interchange (EDI) has also enabled logistics operations to be paperless.

14.1 Electronic Procurement

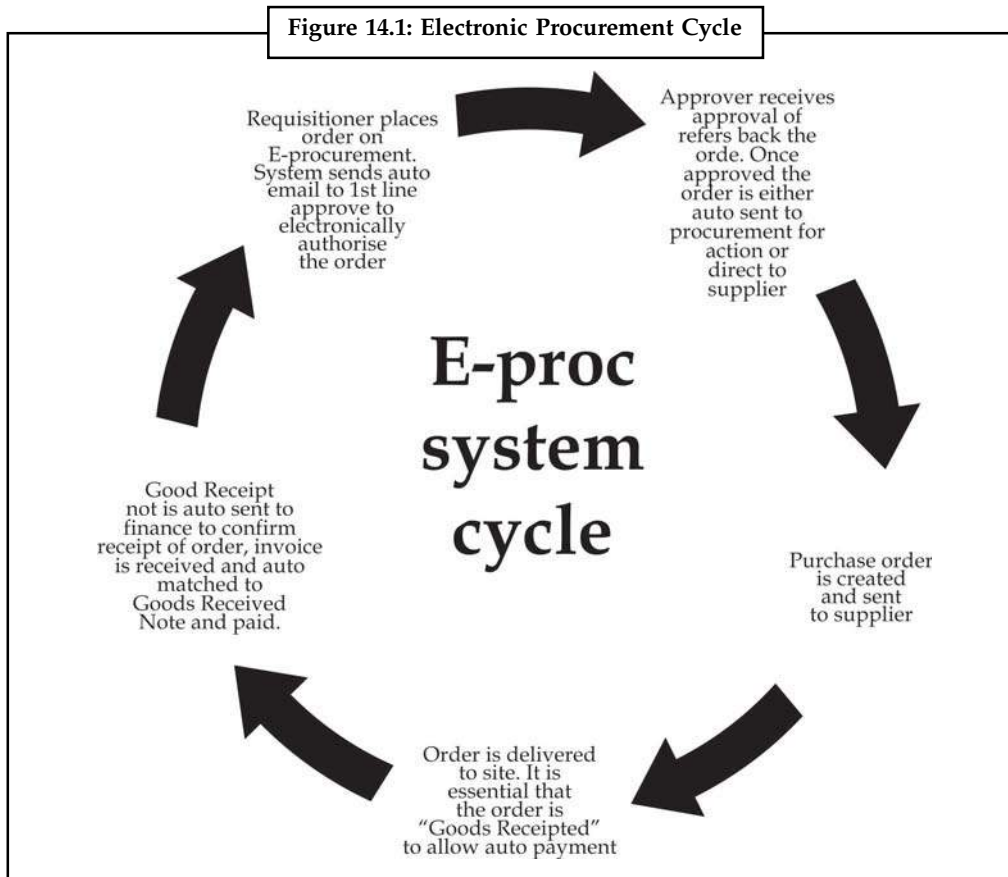
Electronic Procurement (also known as e-procurement) is a way of using the Internet to make it easier, faster and less expensive for businesses to purchase the goods and services they require. While e-procurement is a general term that covers a wide assortment of techniques, such as reverse auctions, its overall goal is to streamline the purchasing process so businesses can focus more management time on earning revenue and serving customers.

Implementing an electronic procurement system offers a company many benefits. For example, if an employee needed to purchase a laptop computer for a business trip, he may at one time have been told to visit the local business supply store and charge the purchase to the company account. He may have been given a spending limit or may have been required to bring back a receipt for his purchase; however, those rules were not easy to enforce or to keep track of. He could purchase a top of the line laptop more for personal use than for business, but it would be the company that would foot the bill.

With electronic procurement, those types of situations are much less likely to occur. For one thing, all purchases are easier to track because they are done over the Internet and the company's managers can easily see who made which purchases without having to wait to receive a monthly revolving credit statement. Furthermore, many companies incorporate product specifications into their e-procurement systems, so an employee wanting a laptop might only be able to purchase a certain brand with specific features, memory capacity and software.

Also, e-procurement saves time. Buyers do not need to leave their desks or make phone calls to suppliers in order to place orders; they simply go through the Internet. And, because suppliers receive the order almost immediately, they can also fulfill and ship it much faster than with the traditional procurement methods.

Although the benefits of e-procurement are plentiful, there are obstacles that can arise in implementing this type of process. The biggest pitfall is treating all areas of procurement and all products the same. The reality is that what may work for one good or service may simply not work for all of them, so successful e-procurement systems use a number of different techniques.



The best way to illustrate this point is through a comparison of products. One product is what is called a urgent item. These items are those which are supplied by only a few companies or individuals but which are in high demand. Most companies stock up on urgent items if possible so that they do not run out and find themselves in a difficult situation. Another product might be classified as a noncritical item, such as printer paper or coffee filters. These type of items are extremely important to the business but they are needed. Generally, this category of items accounts for 80% of all company purchases.

While both products are needed by the company, they would require different procurement techniques or else the buyer would end up paying more. With an urgent item that is in high demand, for instance, a buyer would never want to hold a reverse auction because the seller would be able to drive up the price since they, not the buyer, have all the power in that relationship. Reverse auctions work quite well, on the other hand, for non-critical items and can lower costs for these items by as much as 35%.



Caution Understanding the various e-procurement techniques, therefore, is critical if a company plans to successfully implement such a system and many have.

Some studies indicate that most companies today use e-procurement processes to some extent, yet these processes deal with a small amount of all the purchases these companies make regularly. As companies become more comfortable with using the Internet to handle their purchasing needs that number will continue to grow. Once companies see the potential benefits of such a system, they can only choose to move forward.

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14.1.1 E-Procurement Systems

E-procurement systems, applications designed to allow businesses use the Internet in order to acquire the necessary goods and services, are not all created equal. The term itself is quite broad and actually includes several varieties of applications. Part of a successful implementation involves choosing the appropriate application.

In general, there are three main categories of e-procurement systems. One type focuses on improving the transactions and the decision-making capabilities of the company. Businesses may deal with hundreds of transactions weekly, but these applications simplify the process and help foster stronger relationships between buyers and suppliers.

The second category of e-procurement systems involves managing assets. Systems in this category provide inventory management, maintenance scheduling, in-house product availability, as well as other similar services. These applications are useful for businesses that need to keep a close idea on the quality of their direct materials in stock. Finally, the last category includes systems designed to optimize a company's production operations. Many of these applications deal with the entire production cycle, including the procurement of materials when the inventory runs low, the management of supplier contracts, and the production scheduling.

Because of the differences between the systems, it is important for companies to choose the one that is most appropriate for their industry. However, the decision isn't as difficult as one might at first think. Businesses involved with manufacturing, such as automobile makers, would be more likely to use systems from the third category. Those types of applications would allow them to maintain a specific amount of direct materials in their inventory but they also need to have a system which helps them plan and forecast their production.

On the other hand, companies that deal with repair and/or maintenance, such as automotive repair shops, would be more likely to use e-procurement systems from the second category. Since they need to keep track not only of their inventory of car parts, but also of helping them set repair schedules.

Regardless of the type of e-procurement system a company chooses, the company can expect to receive similar benefits including saving money on purchases, improving the timeliness of the purchasing process, and eliminating waste. In addition to these benefits, companies can also improve the efficiency of their supply chain.

Supply chains essentially include every business, manufacturer, and distributor that supplies the goods and services necessary to create a product, so any improvement in the speed of those transactions is obviously beneficial. Additionally, using e-procurement to enhance supply chain relationships can make it easier for accounting departments to track and keep a record of payments and invoices.

E-procurement systems don't automatically boost supply chain efficiency, however. The company must select a system that has the capabilities necessary to achieve those benefits first. For example, the system must include applications to assist with contract management, including storing pricing information, maintaining sales terms and helping negotiations. By having all of this information in one place, the purchasing process is expedited. Another offering that must be included in the application is the ability to easily compare suppliers so that the best one can be chosen to meet that company's particular needs. After all, choosing the right supplier depends on more than just price; it also involves product availability, customer service, industry reputation and quality.



Caution Despite the differences in e-procurement applications, the bottom line is that a company must choose one that works for its industry and one that will help make its supply chain more efficient if the system implementation is to truly be successful.

14.1.2 Benefits of Electronic Procurement

- Reduction in Manpower Cost
- Reduction in Purchase Cycle Time
- Wider Choice of Vendors
- Better Prices for the Purchased Goods
- Reduction in Transaction Cost
- Fewer Human Errors
- Better Relations with the Vendors
- Better Compliance with Regulations

14.2 E-Marketing

Internet marketing, also known as web marketing, online marketing, webvertising, or e-marketing, is referred to as the marketing of products or services over the Internet. Internet marketing is considered to be broad in scope because it not only refers to marketing on the Internet, but also includes marketing done via e-mail and wireless media. Digital customer data and Electronic Customer Relationship Management (ECRM) systems are also often grouped together under internet marketing.

Internet marketing ties together the creative and technical aspects of the Internet, including design, development, advertising and sales. Internet marketing also refers to the placement of media along many different stages of the customer engagement cycle through Search Engine Marketing (SEM), Search Engine Optimization (SEO), banner ads on specific websites, email marketing, mobile advertising and Web 2.0 strategies.

In 2008, The New York Times, working with comScore, published an initial estimate to quantify the user data collected by large Internet-based companies. Counting four types of interactions with company websites in addition to the hits from advertisements served from advertising networks, the authors found that the potential for collecting data was up to 2,500 times per user per month.

14.2.1 Types of E-marketing

E-marketing is broadly divided into the following types:

- **Display Advertising:** The use of web banners or banner ads placed on a third-party website or blog to drive traffic to a company's own website and increase product awareness.
- **Search Engine Marketing (SEM):** A form of marketing that seeks to promote websites by increasing their visibility in Search Engine Result Pages (SERPs) through the use of either paid placement, contextual advertising, and paid inclusion, or through the use of free search engine optimization techniques.

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- **Search Engine Optimization (SEO):** the process of improving the visibility of a website or a web page in search engines via the “natural” or unpaid (“organic” or “algorithmic”) search results.
- **Social Media Marketing:** the process of gaining traffic or attention through social media websites such as Facebook, Twitter and LinkedIn.
- **Email Marketing:** involves directly marketing a commercial message to a group of people using electronic mail.
- **Referral Marketing:** a method of promoting products or services to new customers through referrals, usually word of mouth.
- **Affiliate Marketing:** a marketing practice in which a business rewards one or more affiliates for each visitor or customer brought about by the affiliate’s own marketing efforts.
- **Inbound Marketing:** involves creating and freely sharing informative content as a means of converting prospects into customers and customers into repeat buyers.
- **Video Marketing:** This type of marketing specializes in creating videos that engage the viewer into a buying state by presenting information in video form and guiding them to a product or service. Online video is increasingly becoming more popular among internet users and companies are seeing it as a viable method of attracting customers.

14.2.2 Advantages and Limitations of E-marketing

The advantages of e-marketing are as follows:

- **24*7 Connectivity** – The buyer can access the seller’s website 24 hours a day and 7 days a week.
- **Less Expensive** – E-Commerce websites can be launched with a very small budget. The expenses involved are website development charges, web-space rental, hosting charges and website maintenance charges.
- **Worldwide Reach** – The biggest benefit of business over the internet is its global reach.
- **Online Payment Facility** – The buyer can make online payments via credit card. This facility speeds up the transaction, assuring the seller of payment.
- **Measurement of Effectiveness** – By putting a counter on the website, the seller can count the number of visitors to the website and the number of buyers who actually made online purchase.
- **Ease of Operation** – The buyer need not leave the comfort of office or home to purchase goods on the internet. The payment can be made with a click of the mouse and the goods can be delivered at the buyer’s door step.
- **User-Friendliness** – Most e-marketing websites are very easy to use. The buyer is guided through various procedures to purchase the good online. Many sellers have established call centers to be in direct touch with the buyer.
- **Personalized Service** – Visitors to the websites are normally advised to register themselves, so that each time they visit the website they are recognized and provided suitable services.
- **Creation of Consumer Databases** – The seller can keep a data base of the name, age, address, sex, contact numbers and important dates, such as birthdays and marriage anniversaries of online buyers.

Limitations**Notes**

One of the challenges that internet markets face (as does the general public) is that many internet products are outright scams or promoted with deception making it difficult to know what one is buying. This is especially the case with products that are supposed to train or aid internet marketers in making money. While the quality of products has improved in the past few years, ethics is still often missing in internet marketing. Many so-called money making products are “empty boxes” in which there is essentially nothing there yet a buyer is to make money by reselling this empty box to others. Pyramid schemes are also still prevalent.

The consumer is unable to physically feel or try on the product which can be a limitation for certain goods. However a survey of consumers of cosmetics products shows that email marketing can be used to interest a consumer to visit a store to try a product or to speak with sales representatives.

Marketer will not be able to use the x-factor/personal touch factor/human touch factor to influence the audience as the marketing is completely based on the advertisement and the information..

Self Assessment

Fill in the blanks:

1. is a way of using the Internet to make it easier, faster and less expensive for businesses to purchase the goods and services they require.
2. Internet marketing, also known as web marketing, online marketing, webvertising, or, is referred to as the marketing of products or services over the Internet.
3. Search engine marketing (SEM) is a form of marketing that seeks to promote websites by increasing their visibility in through the use of either paid placement, contextual advertising, and paid inclusion, or through the use of free search engine optimization techniques.
4. marketing is the process of gaining traffic or attention through social media websites such as Facebook, Twitter and LinkedIn.
5. advertising is the use of web banners or banner ads placed on a third-party website or blog to drive traffic to a company’s own website and increase product awareness.
6. marketing is a method of promoting products or services to new customers through referrals, usually word of mouth.
7. a marketing practice in which a business rewards one or more affiliates for each visitor or customer brought about by the affiliate’s own marketing efforts.
8. Inbound marketing involves creating and freely sharing informative content as a means of converting prospects into customers and customers into repeat
9. is type of marketing specializes in creating videos that engage the viewer into a buying state by presenting information in video form and guiding them to a product or service.
10. involves directly marketing a commercial message to a group of people using electronic mail.

14.3 Electronic Logistics

The use of modern technology, such as the Internet, enables logistics supply businesses to grow and allows for significant improvement of their logistics customer service (LCS), which is very much needed to meet the challenges and expectations of their global consumers. If utilized correctly, the Internet could enable logistics supply chains, even for smaller firms, to effectively market their products and services worldwide through web-based commercialism.

Electronic logistics is use of web –based technologies to support warehousing and transportation management processes. E-logistics enables distribution to couple routing optimization with inventory tracking and tracking information.

In international trade and distribution, computerization is slowly but surely tacking hold of every aspect of business. From computerized trade leads available through the department of commerce, to electronic letters of credit, to telecommunicated documents, to computerized freight booking, tracing and documentation system, to electronic freight tariffs, automated freight payment systems, computerized loss and damage reporting.

There is a tremendous scope of the application of IT in logistics. In fact, modern supply chains are held together by the strength of IT, through its ability to transmit huge amount of data speedily, or make global data available to expedite the decision-making process.

Due to the advantages offered by IT, many logistics providers are planning to handle majority of their commercial transactions electronically. Also, exporters are already using IT for various activities ranging from e-procurement of goods to availing transportation services on the net.

14.3.1 Important Electronic Tools

Shipping lines are keen to encourage their customers to use the internet and have developed a number of attractive tools. The biggest benefit of these tools is that both shippers as well as shipping lines gain by using them. Following are some of the important tools:

- Electronic receipt of vessel schedule information
 - Tracking and tracing of cargo
 - Remote bill of lading (B/L) printing
 - Single data entry reporting
 - Exception reporting
 - Online tendering, etc.
1. ***Electronic Receipt of Vessel Schedule Information:*** Shippers can visit a logistics portal to check the schedule of different shipping lines and choose what suits their supply chains the best. This saves shippers time and effort. The shipping lines, too, benefit as they do not have to inform individual shippers about their voyage schedules. At present, the only limitation to this system is that not every portal maintains information about every shipping line, nor does every shipping line provide updated information on their sites or related portals.
 2. ***Tracking and Tracing of Cargo:*** The biggest benefit shippers enjoy as far as e-logistics is concerned, is tracking and tracing the cargo. With e-connectivity they need to spend less time per enquiry with shipping lines about the status of their cargo and significantly improve their supply chain visibility. However, different portals offer different services.

3. **Remote Bill of Lading Printing:** The main benefits of this facility are reduced production and distribution costs for the carriers. The shipper's gain is fast and error-free receipt of documents. More and more shippers are using this facility and are demanding simplified transmission of transport documents. One of the reasons for this is error-free transmission of Bill of Lading. Shipping lines normally dispatch the Bill of Lading within 48 hours of vessel sailing.
4. **Single Data Entry Reporting:** With the aligned system of documentation, the format of various shipping documents is now standardized. Information once keyed in any document will automatically appear in all aligned documents. This system saves repetitive data entries and also saves substantial time and cost.
5. **Exception Reporting:** Shippers across the world, who work tirelessly towards manufacture of quality products, also want reliable delivery schedules. Exception reporting by the shipping line helps the shipper to know if there are any deviations from the instructions, which he/she has given to the shipping line.
6. **Online Tendering:** To find out the ocean freight rates from various shipping lines, the shipper has to send an enquiry separately to each shipper. Online tendering helps the shipper to send out rate enquiries to as many shipping lines as desired by merely pressing a button. Today, in the era of rationalization, mergers and acquisitions, the shipper's global requirements are getting increasingly complex. Online tendering helps them get competitive quotations from shipping lines operating on various routes. These multinationals maintain databases of such quotations in order to choose the most competitive rates on various routes.

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14.3.2 Benefits of E-commerce

One main element of web-based logistics supply management is electronic commerce, or simply E-Commerce. Through this method, supply chain managers are now able to track product orders and shipments in real time; disseminate information rapidly and trade documents instantly instead of waiting for several days to complete documented transactions; and resolve logistics issues and other concerns remotely. They can also enable chat or discussion boards on their business-to-business (B2B) websites to allow their consumers to give their feedback, which could help them improve online operations and service delivery.

- **Efficient Delivery:** Service and goods delivery is far less complicated to set up over the Internet than with traditional document delivery systems. With the use of web-based communications, logistics managers and transportation companies can now exchange cargo documents electronically in a matter of seconds. They can exchange bill of lading instructions, freight invoices and other documents with increased accuracy and efficiency because these forms are all available online. Best of all, the only tools required to experience this powerful business solution are a personal computer and an Internet browser.
- **Global Networking:** The Internet gives logistics supply managers the opportunity to reach out to thousands of contingent business partners worldwide through online networking. Logistics managers can participate in the Global Logistics Network, which includes participants such as major enterprises (shippers of goods and their customers), freight forwarders, customs brokers, transportation providers, third-party logistics providers, transportation e-marketplaces and other logistics intermediaries, to expand their business network and to establish formidable partnership with the industry's key players.

Notes

- **Communication Tools:** Supply chain management can now take advantage of streamlined collaboration via the Internet. Web conferences, online meetings and email correspondence are just a few ways to contour effective communication processes. Through the use of these communication tools, logistics managers can readily address the concerns and demands of their business partners and consumers with ease and execute sound logistics practices that will enhance their overall operations in the logistics supply industry.

Self Assessment

Fill in the blanks:

11. Electronic logistics is use of web-based technologies to support and transportation management processes.
12. The biggest benefit shippers enjoy as far as e-logistics is concerned, is and tracing the cargo.
13. One main element of web-based logistics supply management is,
14. The Internet gives logistics supply managers the opportunity to reach out to thousands of contingent business partners worldwide through networking
15. The main benefits of are reduced production and distribution costs for the carriers.

14.4 Summary

- Technology is changing at a very fast pace.
- Various aspects of electronic business such as e-procurement, e-marketing, e-logistics use a number of technology products. The life cycle of technology products is very short.
- We are living in a knowledge-driven era, where everyone has access to information thanks to internet and a variety of other sources of information.
- However, the market is dominated by those, who translate information into knowledge and use the knowledge to improve productivity and efficiency of their enterprises.
- India is enjoying an enviable position because of its leadership in the area of information technology.
- A number of business solutions are developed in India for world wide applications. However, such applications take a long time to be implemented in India itself.

14.5 Keywords

Affiliate Marketing: a marketing practice in which a business rewards one or more affiliates for each visitor or customer brought about by the affiliate's own marketing efforts.

Electronic Logistics: This is use of web-based technologies to support warehousing and transportation management processes.

Email Marketing: involves directly marketing a commercial message to a group of people using electronic mail.

E-procurement: Electronic Procurement (also known as e-procurement) is a way of using the Internet to make it easier, faster, and less expensive for businesses to purchase the goods and services they require.

Inbound Marketing: Involves creating and freely sharing informative content as a means of converting prospects into customers and customers into repeat buyers.

Notes

Internet marketing: It also known as web marketing, online marketing, webvertising, or e-marketing, is referred to as the marketing of products or services over the Internet.

Referral Marketing: a method of promoting products or services to new customers through referrals, usually word of mouth.

Video Marketing: This type of marketing specializes in creating videos that engage the viewer into a buying state by presenting information in video form and guiding them to a product or service Online video is increasingly becoming more popular among internet users and companies are seeing it as a viable method of attracting customers

14.6 Review Questions

1. What do you understand by the concept of electronic procurement?
2. What do you mean by electronic marketing?
3. What are the various types of e-marketing? Discuss in detail.
4. Discuss the growing importance of electronic logistics?

Answers: Self Assessment

1. Electronic Procurement
2. e-marketing
3. Search Engine Result Pages (SERPs)
4. Social media
5. Display
6. Referral
7. Affiliate marketing
8. buyers
9. Video marketing
10. Email marketing
11. Warehousing
12. Tracking
13. electronic commerce
14. online
15. Remote Bill of Lading Printing facility

14.7 Further Readings



Books

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Notes

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Online links

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<http://www.supplychainstandard.com/assets/getAsset.aspx?liAssetID=779>



Case Study

Argos Goes Full Speed Ahead with Automated DC

Customer Challenge:

Need to handle substantial growth in sales, number of sales channels and growth in choice for the consumer, while at the same time increase competitiveness in the market.

Solution:

Automated distribution centre including VISION™ Warehouse Control System integrated into Argos' OMI WMS.

Benefits:

- Lower operational costs
- Higher efficiency, productivity and picking accuracy - Better control over direct imports
- More efficient handling of reverse flows

Outlook:

- Continuous improvement program through on-site 24/7 maintenance and support team

The Customer Challenge

Argos is the largest non-food retailer in the UK with annual sales close to £4.3 bn (€ 5.4 bn). The company sells a wide range of home, electrical, garden and DIY products through its catalogue, website and over 700 shops in the UK and Ireland.

Faced with significant growth, Argos wanted to increase product availability and reduce costs. Argos was dealing with a rapidly expanding product range and increasing price competition in many core product areas. Being a catalogue retailer, the catalogue is in fact an all-season promise of product availability to the customer. It means that Argos has to stock all those products throughout the season. Security of supply and pick accuracy are very important.

Argos decided to centralise the distribution of small items to increase national availability by concentrating supplier deliveries to one site and improving picking efficiency. At the same time Argos also wanted more control and continuity of supply of direct imports, which make up a growing proportion of the product range.

The Solution

The distribution centre encompasses several processes, including a central warehouse for imported products (CDI) and a store order picking function for small items (CDC). The CDI operation is essentially a bulk storage and container-to-palletisation factory' providing speed and efficiency in replenishment and supply.

The CDC includes complex integration of technology, including automated storage and retrieval, goods-to-man order picking, and associated warehouse management and control systems. Vanderlande Industries' vistorspi Warehouse Control System (WCS) is integrated into Argos' OMI WMS.

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Notes

'Vanderlande Industries showed good understanding of our business requirements. Their solution gave us the best overall Return-On-Investment,' says Catherine McDermott, Distribution Director at Argos.

'We were impressed by Vanderlande Industries' rigorous approach and by the creativity they showed in finding new ways to deliver smooth, efficient processes,' comments Mark Jones, Distribution Development Project Manager at Argos. 'They clearly have a lot of expertise in the distribution sector and this really showed in the quality of their proposal.'

The goods-to-man ODS order picking solution is undoubtedly the highlight of the operation. It is faster, has more built-in error proofing and uses space, capital and labour more efficiently than any currently available alternative.

Picking is coordinated and several totes of the same product may be circulating at any time, allowing many orders requiring that item to be picked simultaneously. When a new product tote arrives at an order picking station, a screen shows product details and indicates how many are to be placed in which order totes. The operator picks the appropriate number of items from the storage tote and places them in the order totes. To increase speed and accuracy, a display is illuminated below each order tote requiring that product, indicating the order number and how many of that product is required.

Efficiency is further increased by Dynamic Routing.

The company is able to continuously determine the most efficient sequence for feeding totes to each order picking station, based on the workload at each station, product requirements around the system and the urgency with which particular products are needed.

This significantly increases throughput per operator, with a resulting substantial reduction in the need for floorspace, capital investment, recruitment and training.

Argos also tackled reverse logistics at Barton. "Reverse flows are a commonly neglected area of the retail supply chain. There is a lot of non-value added handling involved which consumes valuable supply chain capacity. We took the opportunity to co-locate our damaged returns operation to Barton and automate some of the processes. That has given us benefits in terms of improved inbound transportation and helped smooth some of the heavily seasonal work patterns in the distribution centre," says Ms. McDermott.

The benefits

Argos has significantly reduced operational costs, freeing up resources at busy regional distribution centres. Managing direct imports in bulk yields greater savings and ensures continuity of supply.

"Barton provides a focal point for the growing flow of direct imports. This has helped us to remove much of the manually intensive handling. It also provides a way of handling the slow moving tail of products generated by the growth of choice within the business," says Ms. McDermott.

The ODS solution requires 40% less floorspace than a zone picking solution with a similar throughput. "The very high productivity achieved with ODS is leading to substantial savings in operating costs," comments Mr. Jones. "For our business, it really is a big improvement on alternative systems and gives us a lot of flexibility to adapt to new throughput profiles as the business develops".

Contd...

"By taking products which are small enough to be handled in totes Argos have been able to automate much of that activity and that helps compensate in terms of driving efficiency.

The operation is delivering substantially improved productivity as well as improved pick accuracy," says Ms. McDermott.

Argos and Vanderlande Industries continuously work together to improve operating efficiency and system performance, maximise availability and to help Argos' operations team to achieve their Key Performance Indicators, which are reviewed daily. For this purpose Vanderlande Industries has a team on site at Barton 2417. This allows Argos to fully concentrate on their core business.

Question:

Write a brief analysis of the case highlighting the problem and solution of Argos.

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Source: <http://www.supplychainstandard.com/assets/getAsset.aspx?liAssetID=779>

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