

## Chapter 6

# Consignment

**C**onsignment in international trade is a variation of the open account method of payment in which payment is sent to the exporter only after the goods have been sold by the foreign distributor to the end customer. An international consignment transaction is based on a contractual arrangement in which the foreign distributor receives, manages, and sells the goods for the exporter who retains title to the goods until they are sold. Payment to the exporter is required only for those items sold. One of the common uses of consignment in exporting is the sale of heavy machinery and equipment because the foreign distributor generally needs floor models and inventory for sale. Goods not sold after an agreed upon time period may be returned to the exporter at cost. Exporting on consignment is very risky as the exporter is not guaranteed any payment and someone outside the exporter's control has actual possession of its inventory. However, selling on consignment can provide the exporter some great advantages which may not be obvious at first glance. For example, consignment can help exporters compete on the basis of better availability and faster delivery of goods when they are stored near the end customer. It can also help exporters reduce the direct costs of storing and managing inventory, thereby making it possible to keep selling prices in the local market competitive. However, though consignment can definitely enhance export competitiveness, exporters should keep in mind that the key to success in exporting on consignment and in getting paid is to partner with a reputable and trustworthy foreign distributor or a third-party logistics provider.

### Key Points

- Payment is sent to the exporter only after the goods have been sold by the foreign distributor.
- Exporting on consignment can help exporters enter new markets and increase sales in competitive environments on the basis of better availability and faster delivery of goods.
- Consignment can also help exporters reduce the direct costs of storing and managing inventory, thereby making it possible to keep selling prices in the local market competitive.
- Partnership with a reputable and trustworthy foreign distributor or a third-party logistics provider is a must for success.
- The importing country should be commercially and politically secure.
- Appropriate insurance should be in place to mitigate the risk of non-payment as well as to cover consigned goods in transit or in possession of a foreign distributor.
- Export working capital financing can help exporters of consigned goods have access to financing and credit while waiting for payment from the foreign distributor.

### CHARACTERISTICS OF CONSIGNMENT

#### Applicability

Recommended for use in competitive environments to enter new markets and increase sales in partnership with a reliable and trustworthy foreign distributor

#### Risk

Significant risk to the exporter because payment is required only after the goods have been sold to the end customer

#### Pros

- Help enhance export competitiveness on the basis of greater availability and faster delivery of goods
- Help reduce the direct costs of storing and managing inventory

#### Cons

- Exporter is not guaranteed payment
- Additional costs associated with risk mitigation measures

## **How to Export on Consignment**

If you believe you are ready to export on consignment, the first step is to select a reputable and trustworthy foreign distributor or a third-party logistics provider who is based in a market of interest. The next step is to ensure that you have access to financing and credit and that appropriate insurance is in place to cover consigned goods against loss or damage as well to mitigate the risk of non-payment. As such, exporting on consignment may require the use of one or more of the following trade finance techniques: (a) export working capital financing, (b) government-guaranteed export working capital programs, and (c) export credit insurance. More detailed information on each trade finance technique is provided in Chapters 7 through 9 of this Guide.

## **Partnership in Exporting on Consignment**

To succeed in exporting on consignment, the exporter must partner with a reputable and trustworthy foreign distributor or a third-party logistics provider (3PL) that is based in its selected overseas market. A 3PL is a firm that provides logistics services with expertise in pick-up and delivery of shipments for exporters. 3PLs can help exporters reduce costs, mitigate risks, and manage expenses and time factors as well as to ensure that the consignment is shipped on the most economical and optimal route.

Here is a real life example of how a partnership in exporting on consignment helped a U.S. company. A Midwest-based manufacturer of packaging equipment faced challenges in meeting market demand for quick delivery of its products to Asia as well as in reducing the costs of storing and managing overseas inventory to keep prices competitive. The U.S. manufacturer entered a consigned inventory arrangement with a Japanese 3PL who receives and stocks the goods in Japan and sells them to the end customers in Asia. The Japanese 3PL receives a commission for sales made, and then sends the net proceeds to the U.S. manufacturer as their goods are sold. The U.S. manufacturer's sales increased substantially because exporting on consignment helped deliver their products faster to the local market and kept prices competitive due to reduced direct costs of storing and managing overseas inventory.

## **Export Working Capital Financing**

Exporters who sell on consignment in the global market need financing to ensure that they have access to working capital and credit while waiting for payment from the foreign distributor. Export working capital facilities, which are generally secured by personal guarantees, assets, or receivables, can be structured to support export sales in the form of a loan or revolving line of credit.

## **Government-Guaranteed Export Working Capital Programs**

The U.S. Small Business Administration and the U.S. Export-Import Bank offer programs that guarantee export working capital facilities granted by participating lenders to U.S. exporters. With those programs, U.S. exporters can obtain needed facilities from commercial lenders when financing is otherwise not available or when their borrowing capacity needs to be increased.

## **Export Credit Insurance**

Export credit insurance provides protection against commercial losses (such as default, insolvency, bankruptcy) and political losses (such as war, nationalization, and currency inconvertibility). It gives the exporter conditional assurance that payment will be made if the foreign distributor is unable to pay. Appropriate insurance should be obtained to cover consigned goods in transit or in possession of a foreign distributor.