



A Short
Backgrounder
to Counter-Trade

A free resource developed by
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Counter-trade: An Overview

- Officials of the GATT organization, claim that counter-trade alone accounts for around 5% of the world trade.
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- The British Department of Trade and Industry has suggested 15%, while numerous scholars believe it to be closer to 30%, with east-west trade having been as high as 50% in some trading sectors of Eastern European and Third World Countries.
- A consensus of expert opinions (Okaroafo, 1989) has put the percentage of the value of world trade volumes linked to counter-trade transactions at between 20% to 25%.

Why counter-trade:

- Lack of "hard" currency
- Desire for bilateral trade relations
- A mode of entering a foreign market

The pro's of counter-trade are:

1. The world debt crisis has made ordinary trade financing very risky.
2. The use of counter-trade permits the covert reduction of prices and therefore allows the circumvention of price and exchange controls.
3. "You scratch my back and I'll scratch yours" – Bilateralism
4. Excellent mechanism to gain entry into new markets
5. Countertrade can be a good way to attract new buyers.
6. Countertrade also can provide stability for long-term sales.

The negative implications of a high indebtedness for the creditworthiness of a country are well known from sovereign debt literature. Often a creditors main concern is not so much that a debtor may become insolvent but rather that he may be unwilling to repay. The problem is that foreign debt cannot be collateralized in the same way as domestic debt. Creditors who finance exports to foreign firms or trade organizations need the assistance of local governments to enforce repayment.

The cons of counter-trade are:

1. Each trade is organized on an ad-hoc basis with no central registry of organizations and countries wishing to engage in counter-trade.
2. Very little specific counter-trade expertise is available in third-party organizations (intermediaries) as most counter-trade is done directly between countries and large corporations.
3. There may be problems warehousing and tracking assets.
4. Difficulties in valuing, marketing and reselling traded assets.
5. Recruitment and training costs of counter-trade staff may be high.

Counter-trade is generally conducted between governments and/or large corporations, and comes in various styles:

Barter	The direct exchange of goods or services of approximately equal value.	Not used very often because difficult to find goods of equal value.
Swap / Parallel Barter	Both parties sign two separate contracts that specify the goods and services to be exchanged between them at different times.	Assessing value and disposing of goods is also a problem.
Counter-purchase	Seller gets paid but agrees to purchase goods worth the same amount from the buyer.	This form of counter-trade provides the participants more flexibility in selecting goods and in assessing value. In this way one transaction can go forward even though the second transaction needs time.
Buy-back or Compensation	One party agrees to supply technology or equipment that enables the other party to produce goods. Seller agrees to accept as payment a portion of the output or buy it back.	Technology transfer, quality assurance, and assured payment. Usually utilized in developing or newly-industrialized nations.
Offset	Offset arrangements are designed to offset the negative effects of large purchases from abroad on the current account of a country. Ex: a country buying an airplane may demand that parts and components be acquired in the local economy.	Used frequently by countries to ensure stable currency flow and employment. Allows countries and organizations to offset the negative impact of large purchases on balance of payments.

Variations of counter-trade include:

Switch trading	Allows credits to be sold on to a third party
Clearing account barter	As with a retail barter exchange – credits and debits in a barter account with a number of participants
Debt-swaps	Less developed countries with large debt burdens
Debts-for-equity swaps	Debt converted into equity in the debtors firm
Debt-for-product	Debt converted into product from the debtors firm/country
Debt-for-nature swaps	firms or entities buy what are otherwise considered to be nonperforming loans at substantial discounts and return the debt to the country in exchange for the preservation of natural resources

A great deal of counter-trade involves the partial payment of goods or services in cash.

Most emerging market economies have favoured counter-trade for economic reasons.

Newly Industrialized Countries favour for competitive reason with countries in Western Europe, Japan, New Zealand, and Australia actively participating and promoting counter-trade.

