STERLING NATIONAL BANK

Ralph C. Aiello
Senior Vice President, Treasury Management Sales Manager

Greg Williams
Senior Product Director, Head of Payables

Maya Vovchuk
Senior Managing Director, Head of Treasury Management

Should You Pay Foreign Suppliers in Their Own Currency?

Paying invoices in U.S. dollars is a common practice for most domestic importers, but using your supplier's own currency could have significant advantages — for both sides of the transaction.

You've probably never thought about the differences in using U.S. dollars versus foreign/local currency for international payments, but you should. Although 90 percent of international transactions are in U.S. dollars, an Aite Group survey of middle market importers in the United States found that most companies paying in suppliers' local currency actually receive average discounts of 1-2 percent, with some reporting discounts of 3-5 percent or even greater than 10 percent.

"There's a common misconception that the preferred currency for international transactions is the U.S. dollar, but most American companies actually pay that way simply because that's the way they've always paid," says Greg Williams, Sterling National Bank Senior Product Director and Head of Payables. "We routinely ask clients which currency they use to pay international invoices. If the answer is U.S. dollars, we strongly suggest that they have a conversation with their foreign suppliers about which currency they would prefer to receive."

Paying suppliers in their local currency is also likely to result in price discounts, extended payment terms, or both. To understand why this would be the case, it helps to understand a little about how international payments work.

Understanding How Foreign Currency Exchange Works

In many ways, the U.S. dollar could accurately be called "the world's currency," because more trade is transacted in dollars than any other currency, and many commodities are priced in U.S. dollars regardless of where buyers and sellers are located. Despite the dollar's ubiquity, of course, foreign nations' own domestic economies are based on their own local currency. For U.S. companies paying in U.S. dollars, the foreign company will eventually need to receive the funds in it's local currency.

Paying international invoices in foreign local currency may mean reducing uncertainty, fees, and delays because you and your financial institution control the currency exchange transaction.

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—MAYA VOVCHUK, STERLING NATIONAL BANK

Paying in dollars may seem more convenient to a U.S. company, but that convenience comes at a cost.

"Most people in American companies working with an overseas supplier assume they will pay in dollars, never thinking about the fact that there's going to be a conversion to the foreign company's own currency, and every conversion has a cost," says Ralph C. Aiello, Sterling Senior Vice President and Treasury Management Sales Manager. "If the transaction needs to pass through correspondent banks, each one will charge a fee."

Foreign suppliers will also often increase the purchase price by 10 percent or more to cover conversion fees. Their mark-up might be reasonable or it might be exorbitant, but the buyer will never know because the supplier controls the conversion.

"It's better to pay in local currency through your U.S. bank, so you can control the conversion and get a better rate because you have a relationship with your financial institution," says Aiello.

Pricing Discounts and Better Terms

Shifting payment to local currency does not just benefit the purchaser, however. From the perspective of the foreign seller, receiving payment in U.S. dollars means bearing the risk of currency volatility. Furthermore, the cost of the currency exchange could damage its profit margins, so their natural response is to factor in the purchase price and require shorter payment terms.

"Most foreign vendors don't have a U.S. dollar account so their bank controls the conversion and they just know that when it lands in their account it's in their local currency," says Maya Vovchuk, Sterling's Senior Managing Director and Head of Treasury Management. "Adding a premium to the purchase price doesn't guarantee they won't lose money on the conversion, so they might be willing to negotiate the price if the buyer is willing to pay in their local currency."

The same can be true for payment terms. Being paid in U.S. dollars often results in delays because the exchange transaction may have to go through several entities in a correspondent bank network.

"The supplier knows that a payment in their local currency will arrive in their account much more quickly," says Williams. "So they might be willing to extend payment terms for a local currency transaction because there is no uncertainty about when they will receive it in their account."

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What You Can Do

TALK TO YOUR BANKER. "Ideally, your banker should be asking you about all the different types of payments you make and suggesting the best ways to save you money, like paying in local currencies or using the best international wire transfer method," says Vovchuk. "But if they haven't done that you should ask about alternatives to paying international invoices in USD. Your bank should be able to help you initiate international payments online in a variety of currencies."

ASK YOUR SUPPLIER ABOUT INVOICING IN THEIR LOCAL CURRENCY. "Both the U.S. buyer and foreign supplier may be making the same assumption: that the other person prefers USD payments," says Williams. "Ask about potential discounts or better terms. If price discounts are not an option, ask about invoicing in both USD and local currency, so you can compare costs."

DON'T IGNORE SMALL INVOICES. "Most people assume big dollar international payments are the only ones to worry about, but that's not the case," says Aiello. "Even on a small invoice, any time you're paying outside the U.S., someone is making money on that transaction. Why shouldn't it be you, the customer, saving money by controlling the payments?"

Sterling National Bank can work with your company to make your international payments more cost effective. To learn about our Foreign Exchange service, contact your relationship manager or Client Services at 855.274.2800.

What Happens When You Pay An International Invoice

PAYING IN U.S. DOLLARS

YOU
Initiate a USD wire transfer

YOUR BANK
Debits your account in dollars, makes USD wire transfer

CORRESPONDENT BANK
Receives USD wire, executes currency exchange based upon undiscussed rates, charges a fee

VENDOR'S BANK
Receives funds in local currency and credits them to vendor's account

PAYING IN FOREIGN LOCAL CURRENCY

YOU
Initiate a foreign currency wire transfer

YOUR BANK
Debits USD from your account, executes currency exchange based on already-agreed upon (often preferred) rates, makes foreign currency wire transfer

CORRESPONDENT BANK
May received wired funds in local currency, based upon vendor's banking situation

VENDOR'S BANK
Receives wired funds in local currency and credits them to vendor's account

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