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FCIB Presentation:

Trade Credit Insurance 101

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The BIG Picture

- A/R can typically represent over 37% of a company’s current assets
- A/R may be some of the most significant, pure exposures a company has
- Trade credit claims have been some of the largest claim settlements in the past several years
- Considering that companies normally insure their INVENTORY, PLANTS, EQUIPMENT– it is prudent to insure this large of an asset class, as well

Trade Credit Overview

What is Trade Credit Insurance?

Protection for a company's domestic and/or foreign Accounts Receivable from non-payment caused by the following*:*

- **Insolvency**
  - Chapter VII, XI or its equivalent in the country the loss occurs
- **Protracted Default**
  - Continued delinquency / non-payment / inability to pay (without a insolvency)
- **Political Risk**
  - Currency Inconvertibility / Transfer Risk
  - Embargos, Moratoriums or War
  - License Cancellation, Public buyer defaults

(Please Note: Policy "Triggers" vary from policy to policy. The three bullet points above do not necessarily trigger coverage for all Trade Credit Programs)

The Benefits of Trade Credit Insurance

Increase Sales
- safely and strategically to new and existing customers
- offer more competitive terms
- support sales strategies

Approve Credit Limits Quicker
- to capture more revenue opportunities
- speed up the sales process
- help align your sales and risk management teams

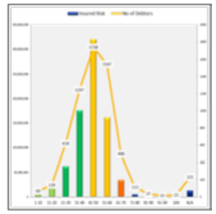
Improve Liquidity and Profitability
- by mitigating your risk of bad debt with proactive credit monitoring to warn of changes to risk
- credit Insurer as business partner – advising on best practice with credit processes for consistency

Improve Risk Insight
- about your customers and prospects to help avoid losses before they occur
- risk information from insurer plus external risk opinion to support your credit risk management protocol

Improve Working Capital
- (often at more favourable rates) since insured receivables translate to secure collateral
- increased facilities by fully employing/leveraging the benefits provided by the program

Enter New Markets / Pursue all Opportunities Fully
- help to identify opportunities via additional market insight
- so you can sell more to foreign markets?

Enhanced Credit Management
- supports structure for risk management discipline and shared best practice across entities
- insurer/Broker MI tools to provide analysis of your risk and support 'group' MI discipline

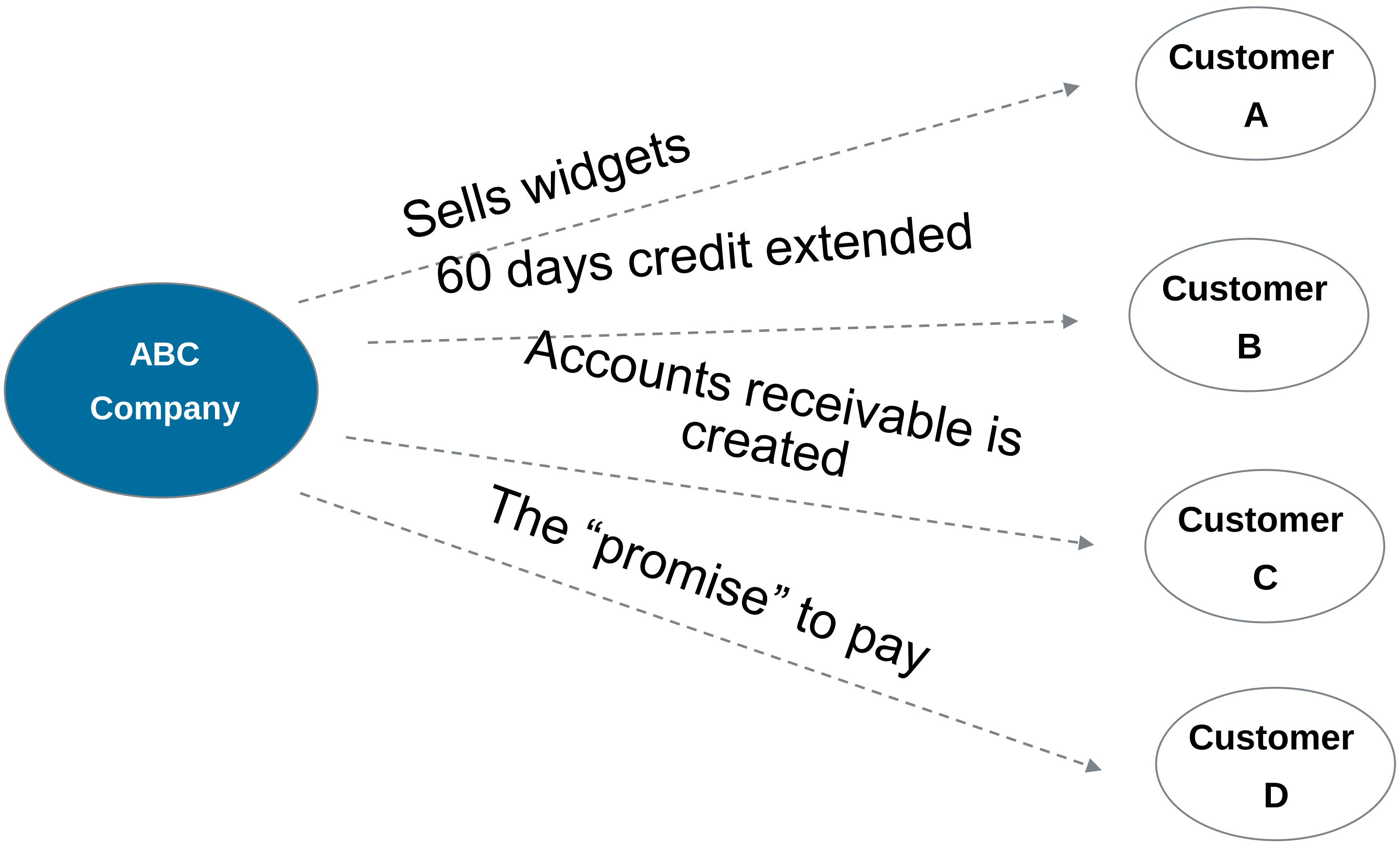


Manage A/R Concentration Risk
- increased awareness of where you are potentially exposed to concentration risk / group debtor exposure
- proactive management of group exposure across multiple entities/countries or region

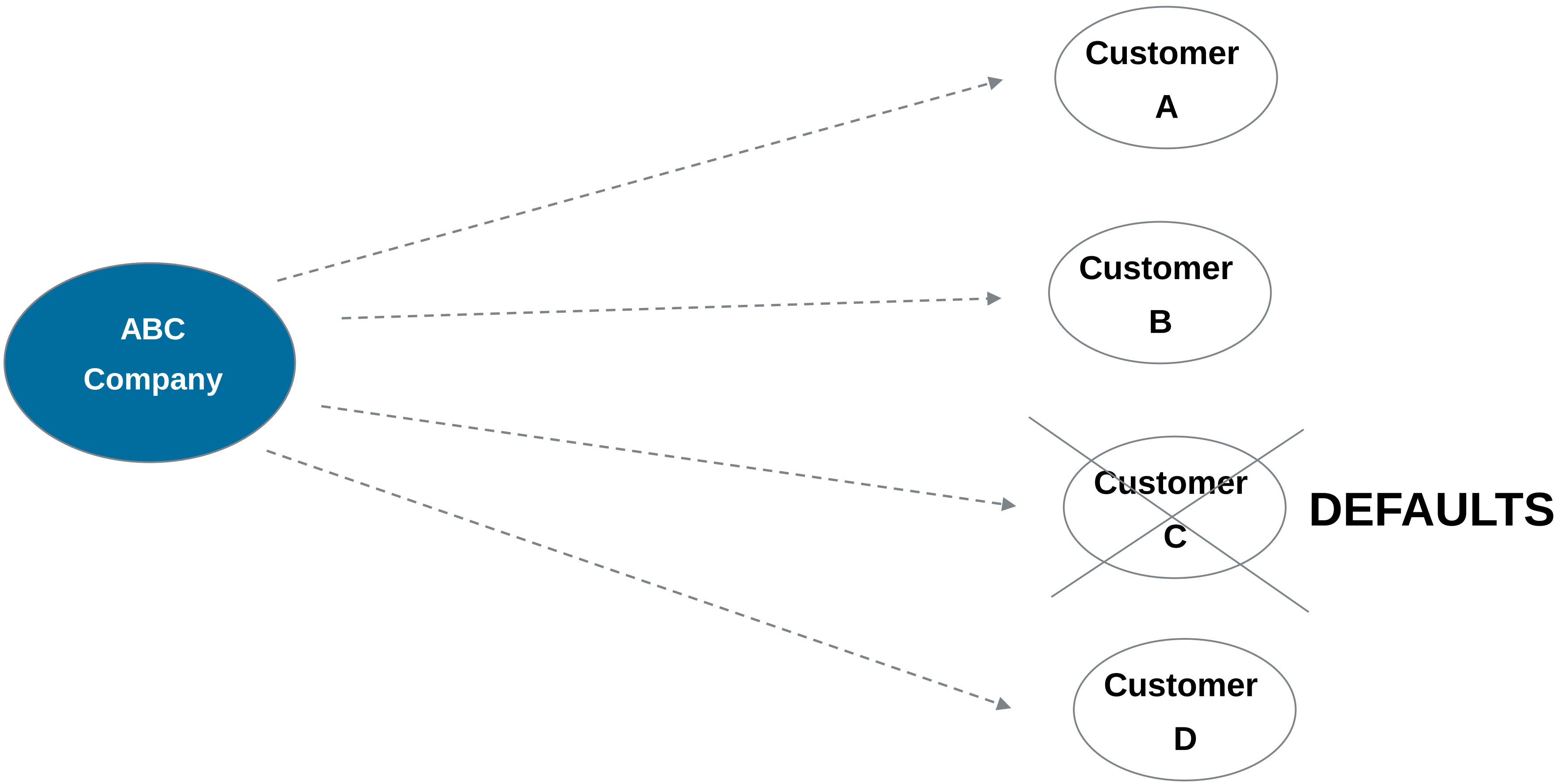
Enhance Customer Relationships
- safeguard against competition and become more competitive by safely raising credit limits or offering better terms to support debtors requirements

Sleep Better at Night
- knowing your risks are covered and your payments are protected and commercial decisions are backed by detailed risk awareness and not taken in the dark!

An Illustration of Trade, the Extension of Credit and the Creation of Accounts Receivable



A Loss Event is Triggered: Company C goes bankrupt, and cannot pay ABC Company



Potential Policy Structures that are Available

- Single Debtor Policy: As the name implies, insures only one key debtor. Premiums dependent on the credit quality of the insured account.
- Key Account Policy: Policy can be structured to insure on a named basis as few as 3 accounts, all the way up to 200 accounts. Typically written with no deductible, and are structured with a 10% coinsurance.
- Whole Turnover: Insures all of a company's sales; typically structured to cover smaller accounts through a blanket level of cover (Discretionary Credit Limit), then larger accounts are named to the Policy.
- Specific Account: Specific accounts selected to be insured; insurers require that selection basis not be totally adverse.

The True Cost of Bad Debt Losses

Amount of Loss/Write Off	**Additional Sales Needed to Recoup that Loss**	
	Assuming 2% pre-tax profit margin	***Assuming 5% pre-tax profit margin***
$5,000,000	*$250,000,000*	*$100,000,000*
$25,000,000	*$1,250,000,000*	*$500,000,000*

The Origins and History of Trade Credit Insurance

The Origins of Credit Insurance in the United States

- In the 1800’s, **FACTORING** was a common practice for manufacturers to obtain funding, collection and protection on their A/R. Factoring is the **<u>purchasing</u>** of invoices and accounts receivable (and was initially done by banks). There are three types of FACTORING ARRANGEMENTS: **recourse, non-recourse, and non-notification**.

- Many consider trade credit to be an offspring of the factoring movement.

- **American Credit Indemnity** (which, over 100 years later, was acquired by Euler) began as a credit insurer in the 1890s.

- **London Guaranty (**later bought by Coface) starts as a credit insurer in 1895.

- The primary industries served by the insurers initially are FUR, LUMBER, JEWELRY, TEXTILES and FOOTWEAR.

Meanwhile, in Europe…

- The World Wars devastated the economies of Western European countries.
- In order to ignite trade following the wars, European governments start credit insurance operations to stimulate the economies and exports.
- In 1919, the U.K. forms the Export Credit Guarantee & Development (ECGD)
- In 1925, NCM was established by a host of banks and insurers in Holland. NCM is backed by the Dutch government.
- SFAC, Svensk, Trade Indemnity, Hermes, Gerling etc. are all formed in various countries, too. Focus of these insurers is to encourage export activity to repair the economies; emphasis is also placed on domestic trade, too
- Companies in Europe become heavily reliant on trade credit as a result, often as an outsourcing of credit departments.

The 1980's spark changes in the U.S.

- U.S. Bankruptcy laws are modified in 1987, leading to bankruptcy being established as a **strategy, as oppose to a form of desperation.**.
- Wickes becomes one of the first major conglomerates to enter Chapter XI as a business strategy.
- Texaco enters Chapter XI after a lawsuit with Pennzoil cuts against them.
- Wall Street promotes junk-bond financing arrangements.
- Wall Street promotes Leveraged Buy-Outs to take companies private, or avoid potential takeovers.
- Economy retracts in the U.S. after the stock market crash of 1987.
- Retail stalwarts like Macy's, Bloomingdales, B. Altman, Zales and others falter under the weight of debt incurred due to LBOs.

Globalization, Complex Financial Products, Fraud and Intense Competition Lead to Fall Outs

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"I don't need credit insurance. I sell to some really strong companies…"
Remember these?

Levitz Furniture

Circuit City

Enron

Best Products

Nortel

WorldCom

Silicon Graphics

Polaroid

Linens-N-Things

The Sharper Image

Toys-R-Us

Adelphia Communications

Border's Bookstores

Lehman Brothers

Target Canada

Phar-Mor Drugstores

Fleming Foodservice

Syms

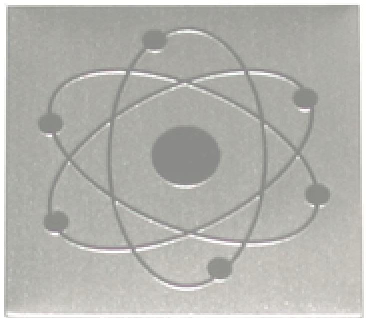
Blockbuster

Parmalat

Kodak

Wynit

“I’m selling into low risk countries - I don’t need political risk cover.”



- The **United States** initiated trade sanctions against India and Pakistan, which voided American exporters’ licenses--causing numerous political risk losses.
- Mad Cow disease caused many European countries to ban the import of **British** beef, another political risk scenario insurers paid on.
- **Argentina’s** economic crises
- **Japan’s** banking system
- **South East Asia’s** economic collapse
- **Greece’s bail-outs**
- **Venezuela’s default**
- **Russian sanctions**

The Trade Credit Insurers Globally, and the Types of Programs Available to Clients

U.S. Trade Credit Insurance Market by "Type"

Catastrophic	Traditional	Distressed	Export Agencies & Syndicates
FCIA, Zurich, AIG, Allied World Assurance Company, QBE the Americas, ACE*, HCC Insurance Holdings, Inc., Equinox Global, Markel, Ironshore	atradius, coface, Euler Hermes	JPMorganChase, Wells Fargo	Lloyd's, Kiln, Liberty Syndicates, Hiscox, Unistrat, Catlin, Ex-Im Bank

* Please note that QBE, HCC, Zurich, ACE and Ironshore are not yet admitted in all US states. Surplus lines or Free Trade Zone provisions may apply.

Trade Credit Insurance in Europe

Catastrophic

Traditional

Distressed

Export Agencies & Syndicates

Trade Credit Insurance in Latin America

Catastrophic

ZURICH

AIG

*

Traditional

atradius
managing risk, enabling trade

coface

EULER HERMES

CESCE
Credit Insurance

MAPFRE

Trade Credit Insurance in Asia

Catastrophic

AIG

ZURICH

ACE

MARKEL

Depth in Leadership. Trusted Partnership.
IRONSHORE
your safe harbour

Traditional

atradius
managing risk, enabling trade

coface

EULER HERMES

QBE
the AMERICAS

Export Agencies & Syndicates

LLOYD'S

Kiln

HISCOX

CATLIN

SINO SURE
中国出口信用保险公司
CHINA EXPORT & CREDIT INSURANCE CORPORATION

Credit Insurance Policy Structures

<u>NON-CANCELABLE CREDIT LIMITS, CATASTROPHIC, EXCESS OF LOSS PROGRAMS</u>

Policies feature a commitment by the Insurer not to amend coverage during the twelve month policy period (certain conditions apply). This is an excess of loss structure with the Insured usually taking a first loss deductible, and utilizing a significant Discretionary Credit Limit to cover most accounts.

Key Features*:*

- ✓ Credit Limits “locked” in for the policy period
- ✓ Catastrophic Loss Structure
- ✓ High Discretionary facility provides significant underwriting flexibility
- ✓ Higher client retentions allows for lower premiums
- ✓ Low Policy administration

Credit Insurance Policy Structures

<u>AMENDABLE CREDIT LIMITS/TRADITIONAL PROGRAMS</u>

Policy works as an enhancement to a company's Credit Department. Carriers frequently provide ground up/whole-turnover coverage, and offer continuous insight on customers throughout the Policy period.

Key features*:*

- ✓ Access to Insurers' Global Databases
- ✓ Sophisticated, Online Policy Management Systems
- ✓ Ongoing Account Monitoring;
- ✓ Whole Turnover, Ground-up Coverage
- ✓ Early warning/detection of potential credit risks before they become a loss

Credit Insurance Policy Structures

<u>GLOBAL CREDIT INSURANCE PROGRAMS</u>

Certain Insurers offer [to multi-national companies] Global Policies that can insure a Parent company in one country, as well as their subsidiaries around the world. Policy provides insolvency and protracted default cover, as well as political risk.

Key features:

- ✓ Multiple policies (under one master form) can be written in different languages
- ✓ Worldwide on-line databases offers credit information on a Global Basis.
- ✓ Flexible Structures, Whole Turnover, Ground-up Coverage
- ✓ Economies of Scale to leverage both Rates and Credit Limits
- ✓ More Control and better MIS on global credit risks

Alternative Receivable Protection

RECEIVABLE PURCHASING AGREEMENTS

A more recent entrant to the trade credit insurance suite of products are Receivable Purchase Agreements know in the marketplace as AR Puts. Underwritten primarily by investment houses and/or banks, these products are becoming increasingly popular for clients looking for comprehensive receivable protection.

Key features:

- ✓ Can be written on a Non-Cancelable basis
- ✓ Programs can be structured on highly distressed debtors or DIP debtors
- ✓ Protection is for Bankruptcy only (does not cover protracted default)
- ✓ Loss Occurring and fixed rate on notional for the term
- ✓ Cover available primarily on companies with public debt

Trade Finance and Banking Arrangements

Accounts Receivable Purchase Programs (“RPP”)

Accounts Receivable Purchase Programs allow you to sell your eligible accounts receivable to certain trade finance banks on a non-recourse basis.

Benefits to clients:

- Allows you to monetize the asset upon invoice generation (liquidity)
- May be arranged as a true sale and taken off your balance sheet (improving financial ratios)
- Transfers the non-payment risk
- Policy typically held in the bank or SPV’s name (but not always)
- Rating of insurer(s) more important than obligor’s or customer ratings
- Supplier continues to manage customer relationships
- Structure is more straightforward and simpler to execute than securitizations and vendor finance programs.

Updates on the Marketplace, and an Industry Overview

Current Market Status

- Capacity is tightening as the global economy contracts
- Market currently at 14 insurers as new entrants have come into the U.S.
- 2008 produced volumes of losses to insurers; there was a major bankruptcy every 8 days during the year. 2009 results were even more troubling. Losses stabilized for insurers from 2010 to now, leading to lower premiums/pricing.
- Rates have been rising after being at historic lows. Still remain in the area of .05% to .1% on domestic sales; and .125% to .2% on most foreign. Rates expected to rise sharply in the energy, metals and commodity sectors, as well as for exports.
- Increasing buyer concentrations, as industries consolidate and stronger companies survive
- Insurers far more selective about the risks they write and industry profile. Concerns continue about Southern Europe (Italy), South America (Brazil, Argentina) and Asia (China).
- In 2015, the O.W. Bunker fraud loss, Target Canada's bankruptcy and Skymall insolvency tinged insurers, now Toys-R-Us; markets bracing for major losses in American retail, energy and claims overseas (Brazil, China, Southern and Eastern Europe) in 2016/2017.

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