

APEC

Human Resources Development Working Group

Business Management Network

Network for Economic Development Management



**Trade and Investment Insurance
Training Program**

**TIITP '97
Compendium of
Training Materials**



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Introduction to Compendium of Consolidated Training Materials

The APEC Trade & Investment Insurance Training Program (TIITP)

The objective of the APEC Trade & Investment Insurance Training Program (TIITP) is to provide training to those who are working or will work with institutions that provide trade and investment insurance so as to develop human resources for the promotion of trade and investment in the Asia and Pacific region.

This program is a highly innovative and pioneering venture which had not been attempted previously in APEC. It achieved cross-regional participation (utilising the great diversity in APEC), and participation included both senior executives and upwardly mobile management working in a challenging, significant, and rapidly growing field of the trade and insurance sectors.

The TIITP was supported by an allocation of US\$ 500,000 from the TILP Fund for the 1997 program (which was repeated for 1998). Individual economies covered additional internal costs and many concerned with the operation of the overall program or specific offerings, both individuals and relevant institutions, provided considerable additional resources.

The specific purpose of TIITP '97 was to train more than one hundred current (and future) managers working with the institutions that provide trade and investment insurance for the APEC member economies. There were 5 programs in 1997 and further offerings were conducted on a wider but tightly focussed needs basis in 1998. A further program will be proposed in 2000.

Cooperative multilateral project Across the APEC Human Resources Development and Trade Promotion Working Groups.

TIITP has been implemented by the APEC Business Management Network (BMN) and the Network for Economic Development Management Network (NEDM) and since 1997 has become a co-operative project with the APEC Working Group on Trade Promotion. The project was proposed by the Ministry of Personnel of the People's Republic of China initially at the 14th APEC-Human Resources Development Working Group (hereafter APEC HRD-WG) Meeting. Mr. Norihiko Maeda of Japan provided significant inspiration and perspiration in the intellectual and practical conception of this project.

The project, led by China, was co-sponsored by Japan, Australia, Brunei, Canada, Indonesia, Philippines, Thailand and the USA. Significantly it was the first multilateral cooperative project specifically aimed at liberalising trade and investment undertaken by the APEC HRD-WG and the first project of that Group under the Trade and Investment Liberalisation and Facilitation (hereafter TILF) special fund to be approved by the APEC Ministerial Meeting.

An Important APEC Deliverable.

The establishment and successful implementation of TIITP is an important deliverable in APEC's economic and technological cooperation, as well as a significant contribution to APEC's human resources development. It has immense current significance to the promotion of economic and trade development in the Asia and Pacific region. By facilitating the effective use of capital, advancing inter-regional co-operation in human resources development, and especially by improving the professional ability and management skills of those currently, or those in the future, working in international trade, it is a major catalyst to the achievement of the Bogor objectives.

For the promotion for trade and investment liberalisation and facilitation to yield its full potential in terms of delivering economic growth and prosperity with employment generation, insurance issues need to be addressed. If this is not done businesses will be prevented from achieving their potential engagement within the region (and elsewhere) due to risk factors.

TIITP by addressing this need through programs that raise competency levels across the region, and publicising the need for insurance provision, has provided an extremely valuable deliverable from APEC HRD. The 1997 TIITP has been, in very many ways, a regionally significant learning experience with productive outcomes in the form of identifiable APEC deliverables directly contributing to the TILF Agenda. It is well placed via its continuation in 1998 (and beyond) to ensure that the reduction of trade and investment barriers is not frustrated by international risk factors.

The trainees gave a positive appraisal of the 1997 TIITP in regard to organisation, service, and effectiveness of the training programs. The participating 9 member economies benefited from the increase in needed insurance skills and competencies in this crucial area for the facilitation of trade and investment flows within the Asia-Pacific and globally.

BACKGROUND

With its continuous structural changes, rapid economic development, and enormous development potentialities, the Asia and Pacific Region became one of the most prosperous regions in the world. This can be attributed to the regions' development potential, and the benefits of international trade and investment as resources were better utilised and outward looking policies were embraced including increased deepening of market oriented economic reforms. The experience of participation in a globalised environment has brought with it both challenges and opportunities. The impact of the Asian Financial Crisis required many regional economies to accept a higher level of internal structural adjustment than previously envisaged.

APEC endeavours to meet these needs for the economic development of the Asia - Pacific region, by liberalising and facilitating trade and investment in the region while continuing to strengthen cooperation, in economy and technology.

To restore and maintain continuous economic development throughout the Asia and Pacific region will take time and requires that greater attention be given to the implications of integration into the global market economy. Crucial to the overall restoration of economic growth and continuing development with regional prosperity are the benefits of trade and investment. The imperative to liberalize and facilitate trade and investment in the region, strengthening economic cooperation and technology transfer, has become a critical task for the APEC economies.

In the process of liberalizing trade and investment in the Asian and Pacific region, there are some challenges which are worth our heeding:

- ❖ Differences in the level and stage of economic development across the APEC member economies have caused a wide variation in abilities and capacity to liberalise trade and investment, thus variances exist.
- ❖ The region has a serious shortage of senior managers with skills in trade and investment insurance within the Asia and Pacific region. Thus there is an urgent need to develop the competencies of senior managers in order to promote the trade and investment liberalisation in the Asia Pacific region.

For these reasons, the APEC Business Management Network and the Network for Economic Development Management Network undertook the Trade and Investment Insurance Training Program (TIITP) project and had sought the collaboration of the APEC Working Group on Trade Promotion.

IMPLEMENTATION OF 1997 PROGRAMS

As determined by the approved project design and the decisions taken at the APEC TIITP Kick-off Meeting held from 22-23 March, 1997 in Beijing, there were five training programs under 1997 TIITP project:

- ⌘ Program I - Beijing, People's Republic of China;
- ⌘ Program II - Manila, the Philippines;
- ⌘ Program III - (initially planned for Shanghai) Xiamen, PRChina;
- ⌘ Program IV - Jakarta, Indonesia;
- ⌘ Program V - Bangkok, Thailand.

The TIITP 1997 program achieved broad-based participation by the APEC economies both as instructors and as trainees.

- Twenty-eight specialist lecturers from eight economies including Australia, Singapore, Japan, the U.S.A, Canada, Korea, Malaysia, Hong Kong and the prestigious Berne Union were involved in the trainings.
- One hundred and twenty four (124) trainees registered in the thirty (30) courses offered.
- Eighty (80) of the participants were supported under APEC funding,

- Forty four (44) additional trainees were recruited on a self-funding basis.
- One hundred and twenty (120) of the one total of hundred and twenty-four (124) participants received completion certificates at the end of their program. (Four of the trainees were unable to complete the course due to illness and/or other commitments). The trainees came from the following 9 economies Australia, Hong Kong, Indonesia, Malaysia, People's Republic of China, Philippines, Singapore, South Korea, and Thailand.

THE TRAINING MATERIALS IN THIS COMPENDIUM

This Compendium is not a collection of all the presentation materials used in TIITP '97 but a comprehensive selection of edited materials and notes in which repetition and overlap has been eliminated. It does not purport to be a textbook for Trade and Investment Insurance training though it does provide an invaluable set of highly relevant teaching materials for this purpose. No attempt has been made to replicate the verbal presentations of the expert specialist practitioner presenters, but where supporting materials were used such as overhead transparencies or PowerPoint presentations these have been reproduced as notes in text format.

Moreover, the compilers/editors of this Compendium specifically wish to advise readers:

- a. The majority of the topics covered over the TIITP set of five programs were the subject of several presentations. This inevitably resulted in the emergence of some repetition and overlap when the consolidation of the lecture content and training materials was undertaken. An effort has been made to edit out as much of this as possible without detracting from the value of the contributions of the individual lecturers.
- b. Attention is drawn to the fact that the five programs were held between June and December 1997. Clearly some time has elapsed before this compendium of materials was completed. Therefore, while some of the specific information, particularly data, may no longer fully reflect the current position and practices, it is considered that the main substance of the material presented remains valid at this time.
- c. Consequently, individual lecturers may find that not all of their presentations and associated materials appear in the form in which it was presented. For this reason presenters names and institutions have not been attached to specific items but are listed in a separate file (TIITP '97 List of Presenters & Trainees.doc).

The following table details the composition of the five programs.

| | Program I | Program II | Program III | Program IV | Program V |
|--|---|--|---|--|--|
| Time | June 3-13,1997 | Sept. 1-12,1997 | Oct. 21-30, 1997 | Nov 3-13, 1997 | Dec. 11-19,1997 |
| | 11 days | 12 days | 10 days | 11 days | 9 days |
| Venue | Central Garden Hotel, Beijing China | Hotel Sofitel Grand Boulevard Manila, Philippines | International Airport Hotel Xiamen, China | Parkroyal Hotel Jakarta, Indonesia | Swissotel Bangkok, Thailand |
| Subject | Professional funda-mentals on trade and investment insurance | Trade and investment insurance systems in APEC member economies | Trade and export credit insurance | Export credit and investment insurance | Provision & quality management of trade and investment insurance |
| Trainees | Junior and middle level managers from policy bank insurance company. | Middle and senior level managers from export credit organizations | Middle and senior level managers from policy bank insurance company | Middle and senior level managers from export credit insurance Co. Ltd and others | Middle and senior level managers from policy bank insurance co |
| Purpose | To master basic knowledge & skills of trade and investment insurance | To understand the trade and investment insurance & operation systems in APEC member economies | To avoid investment risks and standardize the operation of export credit insurance | To enhance the understanding and knowledge on short term export credit insurance activities | To master the know-ledge & techniques on the marketing, underwriting & risk management of trade and investment insurance |
| Project Overseer | The Ministry of Personnel of the People's Republic of China | National Industrial Manpower Training Council of the Department of Trade and Industry | The Ministry of Personnel of the People's Republic of China | The Ministry of Finance of the Republic of Indonesia | Office of the National Economic and Social Development Board |
| Organiser | Export-Import Bank of China | Philippine Export and Foreign Loan Guarantee Corp | People's Insurance (Property) Co, China | PT. Asuransi Ekspor, Indonesia | Export-Import Bank of Thailand |
| Number of Courses | Nine | Five | Nine | Eight | Seven |
| Lecturers | Eight lecturers from 6 economies | Five lecturers from 3 economies | Eight lecturers from 6 economies | Eleven lecturers, Eight from overseas economies and three from domestic institutes | Seven lectures from 4 economies and Berne Union |
| Trainee Composition | 38 trainees from four economies 20 regular trainees 18 additional trainees | 20 trainees from four economies | 46 trainees from four economies 20 regular trainees 26 additional trainees | 23 trainees from Indonesia | 20 trainees from nine economies |
| Trainees awarded Certificates | 34 | 20 | 46 | 23 | 20 |

Detail of Program Implementation

I. Organizational Model

The organizational model applied in the 1997 was Overall Responsibility by the Project Overseer, a Co-ordination Committee comprising Sponsors and Program Organisers, and a Consultative Experts Group. Each specific Course Overseer (normally the APEC lead institution in the relevant economy) took responsibility for planning, including the recommendation and selection of lecturers, design of programs, recruitment of trainees, as well as co-ordinating and supervising the implementation of the programs by their selected Program Organiser. Program organisers implemented the programs and were responsible for providing supplemental funding and inviting specialist consultants to assist in preparing the curriculum and as presenters. Experience in the implementation and operation of the 1997 programs indicates that this model worked well.

Clearly a key element was in identifying appropriate organisers who would lead the implementation of the programs, find the appropriate consultants, disseminate outcomes and ensure that each program achieved its objectives. The organisers as well as providing supplementary funding, extended the programs' outreach by recruiting additional self funded trainees. Of the one hundred and twenty (120) who received completion certificates, forty-four (44) or thirty-seven (37) per cent were additional self-funded registrants (ie. who were not covered by the APEC TILF special account project funding allocated to this project.)

The Project Overseer was Mde. Wen Haiying, Deputy Director-General of the Ministry of Personnel, Beijing, Peoples' Republic of China, represented by Dr. Wu Wenwu. (Mr. Wang Xiaochu, Deputy Director-General of the Ministry of Personnel, Beijing, Peoples' Republic of China, and Lead Shepherd of the APEC HRD-WG, is now the Project Overseer.)

The membership of the Co-ordination Committee and the Experts Group, plus a listing of the Program Overseers follows. A listing of Specialist Presenters and the Trainees, is in a separate file (TIITP '97 List of Presenters & Trainees.doc).

Co-ordination Committee

Wen Haiying - PR China - Project Overseer (now Wang Xiaochu)
Wu Wenwu - PR China – (representing Project Overseer)
Norihiko Maeda - Japan (Chair in Beijing)
Richard Braddock – Australia (Chair in Guilin)
Narong Nitayaphorn - Thailand
Charles Barrett - Canada
Norma Roque – Philippines

All sponsors representatives and Program Organisers were invited to join the Co-ordination Committee, but membership was voluntary. The APEC Secretariat and a representative of the Working Group on Trade Promotion participate in most meetings.

Others attending, expressing support at Co-ordination Committee Meetings, or providing advice to the Committee included:

Nampung Wongsmith - Thailand
Janin Erih, Brunei Darussalam
Tony Reynolds, Hong Kong, China
Cheol Ho Shin, Korea
Low Hock Meng, Singapore
Isak Shamsudin, Lead Shepherd, WGTP (Malaysia)
Jane Tambanillo, Philippines
Liang Zhidong, PR China,
Li Jianzhi, PR China
David McLean, Co-ordinator BMN (USA)
Yutaka Miyake – Japan
Osamu Morimoto –Japan
Brigida Alcanices – Philippines
Jose Ignacio Vicente – Philippines
Michael Andrews - Canada

Experts Group

Charles Barrett – Canada (Convenor)
Richard Braddock - Australia
K.K. Cheng – Hong Kong, China
Etsu Inaba - Japan
Liang Zhidong - PR China
Derek Hill - Australia

Program Organisers

- I. The Export-Import Bank of China
- II. Philippine Export and foreign Loan Guarantee Corporation
- III. PICC Property, People's Republic of China
- IV. PT. Asuransi Ekspor, Indonesia
- V. Export-Import Bank of Thailand

Program Overseers

- I. Ministry of Personnel of the People's Republic of China
- II. National Industrial Manpower Training Council of the Department of Trade and Industry
- III. Ministry of Personnel of the People's Republic of China
- IV. National Industrial Manpower Training Council of the Department of Trade and Industry
- V. Office of the National Economic and Social Development Board

II . Comparison of curriculums

| Program I | Program II | Program III | Program IV | Program V |
|---|---|---|--|---|
| 1. Commercial Foundation | 1. Orientation and Fundamental Courses on ECI | 1. Principle & Practice of Short Term Export Credit Insurance | 1. Export Credit Insurance- Global View and in Indonesia | 1. Opportunities and Risks in International Trade |
| 2. Short-term Export Credit Insurance | 2. trade and investment Insurance Systems of the US | 2. Short term Insurance Claims and Recoveries | 2. Fundamental of Export Credit Insurance -basic theory and practice | 2. Trade Insurance Marketing |
| 3. Short-term Export Credit Insurance Claims | 3. trade and investment Insurance Systems of Australia and HongKong | 3. Internal Credit Insurance | 3. Short Term Export Credit Insurance Framework | 3. Trade Insurance Underwriting |
| 4. Medium and Long-term Export Credit Funding | 4. trade and investment Insurance System of Canada | 4. Medium and Long-term Credit Insurance | 4. Buyer Risk Management on Short Term Export Credit Insurance | 4. Risk Management |
| 5. Medium and Long-term Export Credit Insurance | 5. trade and investment Insurance System of Japan | 5. Evaluation of Country Risk | 5. Country Risk Management on Short Term Export Credit Insurance | 5. Reinsurance and Quality Management |
| 6. Country Risk Management | | 6. Special Trade Insurance | 6. Claim and Recovery Management on Short Term Export Credit Insurance | 6. Mechanism of EID/MITI Overseas Investment Insurance Policy |
| 7. Overseas Investment Insurance | | 7. Project Underwriting | 7. Medium and Long Term Insurance and Investment Insurance | 7. Trade and Investment Insurance: International Perspective |
| 8. Special Trade Insurance | | 8. Financial Management | 8. Overseas Investment Insurance | |
| 9. Management of Export Credit Insurance | | 9. Reinsurance | | |

The programs were designed for, and met, the specific identified needs of the participating APEC member economies. The individual programs were well structured in terms of their content. The curriculum for each program was clearly designed to meet identified needs and in consequence some of the content necessarily was repeated in other programs though each had its unique characteristics.

III . Method of Instruction

Instruction was conducted through classroom lectures, case studies, discussion group, question and answer sessions and field studies. Discussions and case studies were utilised by most lecturers across the programs, and the participants were divided into syndicate groups for case studies, tasks and discussion. Following the group discussion a presenter, elected by the group, would make a presentation to all the participants. Lecturers would make comments and summarise the session(s). Active discussions were found to help broaden the participants' thinking, and promote active communication between lecturers and trainees, enhancing greater comprehension of the subject and improving the participants' learning and understanding. With ten days of lectures, two days for field studies was considered to provide an appropriate balance via a practical field study. The field studies gave trainees an opportunity to both observe practice and to themselves consider the application in specific instances of the knowledge and techniques conveyed in the classroom. Lecturers accompanied trainees and offered guidance when needed plus a subsequent analysis and group discussion. The field studies were a valuable adjunct to traditional classroom lectures promoting vigorous participation and communication among trainees and lecturers.

IV. Special Arrangements

Each program held an opening ceremony with over 100 participants and trainees (Program 1 150 persons, Program 11 100, Program 111 100, Program V 170). Leaders from the Lead Institution, government departments, commercial banks, exporters, academic institutes, and media attended the opening ceremony, which was followed by several symposiums. With government departments and media involved in the programs, the program generated high profile exposure for this significant APEC deliverable.

A comprehensive evaluation was undertaken in each training program. The program reports indicate that the evaluation survey was conducted mainly through questionnaires though written co-ordinator responses and verbal feedback were also obtained. These were detailed in the Summary Report and have been analysed in other components of the Wrap-up Reports. Comments and Observations to the undersigned:

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SECTION 1

THE COMMERCIAL FOUNDATION OF TRADE INSURANCE

**CHAPTER I THE COMMERCIAL FOUNDATION OF TRADE
INSURANCE**

CHAPTER II SYNOPSIS

CHAPTER I

1. TRADING ORGANISATIONS

Sole Traders

Partnerships

Private Companies

Public Companies

Public Corporations

Subsidiaries of Foreign Firms

All of these may act as exporters and may apply for export credit insurance facilities in the country in which they carry on their operations.

They normally fall into two categories

(a) manufacturers who sell direct to their overseas customer who is responsible for payment to the manufacturer. It is the manufacturer who has the insurable interest and who requires the insurance cover; and

(b) export merchants who carry on business under various descriptions such as export houses, confirming houses or merchant shippers. The export merchant receives the orders from overseas and distributes them among various manufacturers, pays the manufacturer, ships the goods and invoices the foreign buyer for payment. In these circumstances, it is the export merchant who requires the insurance cover.

It is important to note that credit insurance cover is normally only available to the party who is the principal in the transaction. Such cover is not normally available for agency activities and commissions.

2. FORMS OF CONTRACT AND HOW CONTRACTS ARE MADE

(a) in some types of business, especially in the commodity trade, model contract forms applying to specified goods and/ or transactions are in existence and will apply if the parties to the contract so agree;

(b) exporters and importers may embody general terms of business into their contracts;

(c) uniform conditions of a general character have been issued by such bodies as the International Chamber of Commerce or the Vienna Sales Convention and some contracts will make reference to these in the contract documents;

(d) the importance of well drafted general terms of business can hardly be exaggerated and these should be printed on acceptance forms, price lists, offers, catalogues, etc;

(e) contracts for the international sale of goods exhibit a characteristic which is not present in contracts for the sale of goods in the home market. They are entwined with other contracts, in particular with the contract of carriage by sea or air under which the goods are exported, and the contract of insurance by which they are insured. In many export transactions the delivery of the shipping documents to the buyer or his agent plays, as will be seen, an important role in the performance of the contract of sale; the shipping documents consist normally of the bill of lading, the marine insurance policy and the invoice and thus represent elements of the three contracts referred to. The situation is even more involved when payment is made under a bankers' documentary credit because this frequent method of payment in the export trade requires the addition of two further contracts to the export transaction, namely the contracts of the bank with the buyer and seller respectively. In short, the export transaction presents itself to the business man as a natural and indivisible whole and he is apt to pay little attention to its constituent parts, like the motorist who thinks of the components of his car only when he notices a fault in them. We have to analyse the individual contracts, which constitute the export transaction because this is the best method of appreciating the functioning of the

machinery of exports as a whole. From this point of view, the contract for the sale of goods abroad is the principal and central legal arrangement involved in the export transaction and all other contracts, such as contracts of carriage, insurance and credit, have a supporting and incidental character.

(f) in recent years there has been an increasing tendency to make contracts by using the fax machine. While this is generally acceptable, care should be taken to confirm by letter, especially where the fax paper used is likely to deteriorate or fade altogether as time passes.

Verbal contracts should not be relied upon. When made, they should be confirmed in writing within a reasonable period of time.

3. ESSENTIAL ELEMENTS OF A CONTRACT

For purposes of export credit insurance

(a) it should be legally enforceable in both the country of the buyer and the seller and should state the applicable law;

(b) it must define what is to be exported and/or what services are to be provided;

(c) there should be evidence of an offer and acceptance;

(d) it must state when the export/service is to take place;

(e) it must show the destination;

(f) it must show the terms of delivery;

(g) the price of the goods and/or services must be clearly shown

(h) the responsibility for payment must be clearly identified:

(i) the terms and method of payment must be clearly shown

(j) the currency of payment must be identified and it should be made clear which party is to be responsible for exchange rate fluctuations between offer and acceptance;

(k) it is advisable to include reference to the resolution of any disputes which may arise, e.g. the rules of conciliation and arbitration of the Court of Arbitration of the International Chamber of Commerce;

(l) it is advisable to check that the person signing the contract has the authority to commit the purchaser;

(m) it should also be noted that the payment under the contract must not be contingent upon factors which are fundamentally outside the exporter's control, e.g. if payment is dependent upon the buyer receiving payment under another contract.

(n) reference may be made to certain internationally recognised standard terms, e.g. INCO Terms, 1990, Vienna Sales Convention 1980 to be applicable to the contract. For major contracts involving the supply of capital goods and or services on extended payment terms, the following additional factors apply:

(i) Performance Milestones

Where progress payments are involved, the contract terms of payment should provide for payments to be linked to clearly defined performance milestones so that an exporter's entitlement to be paid can be objectively established.

(ii) Governing Law

Whilst it has often been a requirement that contracts be governed by the law of the buyer's country, the possibility of having the contract governed by the law of a jurisdiction with which the exporter is more familiar should not be overlooked. A legal adviser expert in the governing law of the contract should be retained by an exporter.

(iii) Provision for Amendments

It is also appropriate to include a suitable method for amending the contract, especially when it relates to a complex project with an extended performance period. Negotiating amendments will be difficult if the contract does not contain an accurate scope of work

including narrative and drawings. It should not be assumed that amendments can be negotiated whilst the contract is being performed. No amendments should be made to the contract without the prior written consent of the E.C.A. and any amendments must be proved to have been validly executed under the relevant law.

If a material amendment relating to the implementation of the contract is agreed after the contract is signed, it is important that such amendment be incorporated in the contract.

(iv) Penalties

The contract should provide for penalty, payments to the exporters if payments of principal and interest are not made at due date.

(v) "Entire Agreement" Clause

If a contract consists of a series of documents including correspondence between the exporter and buyer, a statement of each document to be included in the contract should be agreed to and signed by both parties.

4. TERMS OF TRADE DELIVERY (INCLUDING INCO TERMS)

It is advisable to use INCO Terms 1990 for ocean transport as our basic model while recognising that there exist some variations in terminology and practice to take account of other means of transport, such as overland and air transportation

FAS

Free alongside ship

(named port of shipment)

FOB

Free on board

(named port of shipment)

CFR

Cost and freight

(named port of destination)

CFR landed

Cost and freight

(named port of destination)

**CIF - cargo insurance obtained by seller cost,
insurance and freight ...** (named port of
destination)

**CIF landed - cargo insurance obtained by seller
Cost, insurance and freight**
(named port of destination)

DES

Delivered ex ship

(named port of destination)

DEQ

Delivered ex quay

(duty paid) ... (named port of destination)

It is important to note:

(a) ECAs normally base their cover on gross invoice value; and

(b) cover normally commences from date of contract or date of shipment.

Shipment is usually defined as the handing over of the goods to the first carrier for through carriage to the place where the buyer is to accept them. They are not regarded as shipped if the exporter retains the legal right to stop their carriage before they leave the

country from which they are to be exported. This is a particular concern in relation to containerisation.

5. METHODS OF PAYMENT IN INTERNATIONAL TRADE

There are six basic methods of payment utilised in International Trade:

- (i) Pre-payment;
- (ii) Irrevocable Confirmed Documentary Credit (CIBC);
- (iii) Irrevocable Documentary Credit (IDC);
- (iv) Cash Against Documents (CAD)/Documents Against Payment (D/P)
- (v) Documents Against Acceptance (D/A); and
- (vi) Open Account (O/A).

These payment terms are listed in order of risk in descending order - open account representing the highest risk for an exporter.

(i) Pre-Payment for Goods

Description

Pre-payment for goods prior to shipment under an export contract is, for the exporter, the safest method of payment in International Trade given that payment will be received prior to the goods being shipped. Buyers, however, are generally unwilling to adopt this method of payment as they effect payment prior to receiving the goods.

For an exporter, there is no post shipment credit risk. However, the exporter may be exposed to a credit risk in the pre - shipment phase. An exporter may be manufacturing to specifications and the buyer repudiates or cancels the contract prior to the agreed payment date.

In any event, it is important to ensure that such payments are irrevocable.

(ii) Payment under an Irrevocable "Confirmed" Documentary' Credit (CIBC);

(iii) Payment under an Irrevocable Documentary Credit (IDC).

Description

An Irrevocable Documentary Credit is a definite undertaking of an overseas bank (issuing bank) to pay a specified sum of money against the presentation of stipulated documents by the exporter (beneficiary) provided that the terms and conditions of the Credit are complied with.

The IDC sets out strict terms and conditions, which must be complied with. The Issuing bank substitutes its creditworthiness for that of the overseas buyer (applicant). Provided the terms and conditions of the IDC are met, the Issuing bank is irrevocably committed to paying. An Irrevocable Documentary Credit cannot be amended or cancelled by the Issuing Bank without the consent of all the parties (i.e. beneficiary, applicant).

The IDC is advised to the exporter (normally by their bank) who, after shipment takes place, prepares the documents required under the IDC (i.e. bill of exchange for the value of the shipment, bill of lading, commercial invoice and any other documents required) and presents the documents to their bank for negotiation. The exporters bank will negotiate the documents and claim reimbursement for the value of the documents from the overseas Issuing bank.

In transactions involving the use of an IDC, ECA's risk moves from the credit - worthiness of the overseas buyer to the creditworthiness of the Issuing bank and country risk.

(iii) "Confirmed" Irrevocable Documentary Letter of Credit

The IDC may specifically provide for it to be "confirmed" by the exporter's bank. The Confirming bank substitutes its creditworthiness for that of the overseas Issuing bank and provides a definite undertaking that payment will be made to the exporter provided that the terms and conditions are complied with. For example, an IDC is issued by the Bank of China in favour of an exporter who banks with the ANZ. The ANZ "confirms" the EDC.

Aside from pre-payment, an IDC confirmed by a reliable bank is the most secure payment mechanism for an exporter. The exporter has no post shipment risk though the bank may wish to insure the business.

There remains a pre-shipment risk, the extent of which will vary, depending on the point in time during the pre-shipment period when the Letter of Credit is opened and confirmed.

General

An LC is a relatively secure payment mechanism provided that the exporter can strictly comply with its terms and conditions (i.e. documentation risk). In practice, IDCs are often very expensive for a buyer to establish and, whilst offering both the exporter and the buyer protection, are being relied upon less as a mechanism to finance international trade. This trend is likely to continue as parties seek less costly alternatives.

(iv) Cash Against Documents (CAD)/Documents Against Payment (D/P)

Description

The exporter presents shipping documents to their bank for presentation to the overseas buyer for immediate payment, using the buyer's bank as an intermediary. The buyer's bank is authorised to release the documents only upon payment. This is a "collection" style method of payment normally transacted through the banking system. In some cases, an agent of the exporter will assume the collecting role of the overseas bank, although this is not common.

Generally, the exporter retains title to the goods - the buyer cannot take delivery of the documents of title (i.e. bill of lading) until such a time as the collection is paid. Documentary collections offer a compromise for the exporter and buyer in that it provides a payment term which falls somewhere in between open account and trading under an IDC. The goods are shipped but the buyer may only obtain possession of the documents of title (e.g. the bills of lading) after making payment for the goods. CAD/DP provides the protection of the Banking system (release of negotiable documents) and is usually the payment method used when companies move from IDC terms.

The exporter is exposed to limited risk in that the buyer cannot take delivery of the goods until payment has been made. However, for the ECA the risk of non-acceptance (repudiation) by the Buyer remains a very important consideration. If a buyer chooses not to take delivery (and,

therefore, does not make payment), the exporter may still incur quite considerable costs for the demurrage, storage, customs fees, insurance and, possibly, repatriation of the goods if a suitable alternative buyer cannot be found in the original country of destination.

The potential for contract repudiation needs to be considered, particularly where the goods involve price volatile commodities eg wool and hides, and where it is difficult to on-sell the goods in the event of the buyer refusing to pay.

(v) Documents Against Acceptance

Documents against Acceptance (D/A) are similar in their nature to Documents Against Payment (D/P) except that there is a usance term (e.g. Payment is due 90 days from date of the Bill of Exchange or 180 days from Bill of Lading date). There will usually be a Bill of Exchange drawn by the exporter on the buyer or a Promissory Note.

Negotiable documents are released to the buyer only upon acceptance by the buyer of the Bill of Exchange for payment on a future date. The buyer's bank (collecting bank) is under no obligation to make payment on the due date and the credit risk is solely against the buyer.

Once the Bill of Exchange is accepted by the buyer, and negotiable documents released by the collecting bank, the exporter loses control of the goods. The buyer has the right to refuse payment on the due date for payment as has their bank if for instance, there are insufficient funds to meet the payment. Hence, the ECA's risk lies firmly on the integrity and financial standing of the buyer in honouring the commitments under the export contract.

(vi) Open Account

In simple terms, a transaction conducted on open account terms presents the highest risk to an Exporter. The goods are shipped and the exporter sends the title documents direct to the buyer. Hence, the exporter loses control of the goods immediately. The ECA's post shipment risk is heightened for contracts conducted on open account terms in that there is no control mechanism for payment and the ECA relies solely upon the ability and integrity of the buyer to make the payment as agreed in the contract.

Open account is favoured by overseas buyers in that it does not incur the level of bank fees associated with the other payment mechanisms. Open Account terms are usually only favoured where this is a long standing trading relationship. They are becoming more prevalent as buyers seek cheaper and more efficient ways to settle international trade.

(vii) Air Shipments

Exporting goods by air has grown in importance as it significantly reduces the delivery time to buyers. However, there are unique features of transport by air.

The air transport document (Air Waybill) is an acknowledgement by an airline company that they have received the goods to be airfreighted. The carrier has an obligation to notify the buyer of the arrival of the goods by issuing a delivery order (the authority to collect the goods.) However, the air transport document is not a document of title to the goods (unlike a Bill of Lading) and the buyer may be able to take possession of the goods without producing the Air Waybill.

The exporter does not have the security of a negotiable Bill of Lading and has limited control over the goods. The risk is no different to business being conducted on open account terms.

For goods delivered by air, use of a documentary collection (D/P or D/A) will provide the protection of the banking system. Where an overseas collecting bank has expressly agreed by prior arrangement the Air Waybill can be consigned to that bank. The airline company will seek the authorisation of that bank- prior to releasing the cargo to the buyer. Banks are generally reluctant to consent to the consignment as they are accepting responsibility for the cargo. Under such circumstances, The ECA's risk would be as for payments under D/P or D/A.

(viii) Bills of Exchange

In simple terms, a bill of exchange is a written demand for payment issued by one party (the exporter) on another party (the buyer).

A bill of exchange is also a negotiable instrument whereby a bank will be willing to buy (negotiate) them for exporters in return for providing trade finance for the

exporter. The bill of exchange (sometimes know as a 'draft') is a very common method used by exporters as a means of obtaining payment form buyers for goods shipped.

Parties Involved and their Responsibilities

(i) The Drawer

The Drawer of the bill is the exporter or the named party to whom the amount is due and undertakes responsibility for drawing the bill of exchange.

(ii) The Drawee

The Drawee will be the buyer or the named party responsible for payment. He is not liable under a bill of exchange unless he has accepted it i.e. agreed to make payment upon presentation.

In accepting a term bill of exchange, the drawee legally pledges himself to pay the bill - if he does not pay, it is classed as dishonoured by non-payment. If the drawee fails to accept, the bill, it is known as dishonoured by non-acceptance.

(iii) Usance

A bill can be drawn requesting immediate payment (at sight or on demand) or for payment at a later date (at term).

Where the bill allows for payment at a later date, the time allowed for payment is know as 'usance' and the terms of the usance (i.e. 90 days, etc.) will be determined in the original negotiations between the exporter and buyer.

Where there is a usance term involved, the buyer will usually be required to 'accept' the draft immediately which is also an unequivocal undertaking to honour the bill at maturity.

(iv) Types of Draft

Clean Bill

A 'clean bill' is probably the simplest and quickest means of settling payment. Payment is simply remitted to the exporter by mail, telegraphic transfer or bank draft. No trade documents are involved.

Documentary Collection

A documentary collection is when the exporter wishes to retain some title to the goods until at least a commitment to pay has been made by the buyer. The draft is forwarded with official trade documents ie shipping documents. customs clearance, etc.. In simple terms, the documents of title eg. the bill of lading, are not released to the buyer until either payment has been received or the draft has been 'accepted'.

(v) Protesting a bill of Exchange

In the event that a bill of exchange is not honoured – be it for non-acceptance or non-payment - the drawer may exercise his right to protest the bill. The protest is a formal certificate confirming that the bill has been dishonoured. However, this can prove to be a costly exercise in some areas of the world and it is the exporter's prerogative to give instructions to his bank whether or not a dishonoured bill should be protested.

CHAPTER II – SYNOPSIS

FUNDAMENTALS OF TRADE INSURANCE

- General Principles
- Purposes and Objectives
- Types and Features of Export Credit Insurance
Political/Country Risk

GENERAL PRINCIPLES

- Break Even or Operate at a Small Profit
- Support Only Reasonable Assurance of Repayment
- Appropriate Risk Sharing
- Supplement to Private Sector Financing
- Speedy Underwriting
- Rapid and Fair Claims Processing
- Limit Risk through Reinsurance/Coinsurance
- Adequate Capital/Cash

PURPOSES OF TRADE INSURANCE

- Encourage Expansion of Exports by:
 - ▶ Reducing Risks of Exporting
 - ▶ Improving Access to Export Financing
- Expand Non-Traditional Exports
 - ▶ Diversify Markets
 - ▶ Add Export Products

PURPOSES OF TRADE AND INVESTMENT INSURANCE

- Improve Balance of Payments
- Increase Employment
- Increase Banks' Knowledge of Export Credit
- Improve Financial Skills of Exporters
- Meet Officially Supported Foreign Competition
- Support Exports Deemed in National Interest
- Increase FX by Support of National Firms' Foreign Investments

TYPES OF TRADE INSURANCE

- Pre-Shipment Insurance
- Post-Shipment Insurance
 - Short-Term Post-Shipment Insurance
 - Medium/Long-Term Post-Shipment Insurance
- Performance Bond Coverage
- Other
 - Lease Insurance
 - Inflation Risk Insurance
 - Exchange Risk Insurance
 - Trade Fair Insurance
 - Local Cost & Third Country Cost Insurance

FEATURES OF POST-SHIPMENT INSURANCE

- Eligible Exports
- Eligible Exporters
- Eligible Buyers
- Insurance Coverage
- Risks Covered
- Amount of Coverage

ELIGIBLE EXPORTS

- Foreign Exchange

- Type of Product
 - ▶ Use
 - ▶ Perishability
- Size of Transaction
- Foreign Content

ELIGIBLE EXPORTERS

- Nationality
- Experience
- Commercial Reputation
- Risks

ELIGIBLE BUYERS

- Location
- Public/Private
- Creditworthiness
- Risks

RISKS COVERED

- Commercial Risks
 - ▶ Insolvency
 - ▶ Protracted Default
- Political Risks
 - ▶ War Risks
 - ▶ Government Intervention
 - ▶ Export/Import Embargo
 - ▶ Cancellation of Export/Import Licenses
 - ▶ Conversion and Transfer Risks

AMOUNT OF COVERAGE

- Percent of Transaction Covered

- Exporter Retention
 - ▶ Commercial Risk
 - ▶ Political Risk
- Interest
- Whole Turnover
- Deductible for Claim Payments
- Aggregate Policy Limit

APPLICATION PROCEDURES

- Approval of Exporter
- Approval of Buyer
- Discretionary Credit Limits (DCL)
- Special Buyer Credit Limits (SBCL)

DETERMINING PREMIUMS

- Exporter Experience & Portfolio
- Export Credit Insurer's Premium Policy

DETERMINING PREMIUMS Exporter Experience & Portfolio

- Premium Schedule/Negotiability
- Number and Types of Buyers
- Countries
- History of Export Credit Losses
- Terms of Payment
- Minimum Payment
- Payment Procedure

DETERMINING PREMIUMS Premium Policy

- Accounting for Risk
- Financial Condition

- National Interest
- Competition
- International Agreements

EVALUATING COMMERCIAL RISK

- Underwriting the Buyer
- Underwriting the Exporter
- Evaluating Credit Information
- Evaluating Commercial Reputation
- Analyzing Financial Statements
- Assessing Security & Guarantees

EVALUATING POLITICAL RISK

- Country Limitation Schedule
- Objective & Subjective Factors
- Country Ratings
- Maximum Exposure Limits per Country

SECTION 2

TRADE AND INVESTMENT INSURANCE IN A GLOBAL CONTEXT

CHAPTER I THE GLOBAL SCENE

CHAPTER II EXPORT CREDIT AND EXPORT FINANCE

**CHAPTER III OPPORTUNITIES AND RISKS IN INTERNATIONAL
TRADE**

CHAPTER 1

THE GLOBAL SCENE

INTERNATIONAL PERSPECTIVE

(a) ORIGINS AND DEVELOPMENTS

Credit insurance, as it is known and recognised today, had its origins in the insurance of domestic credit risks in a number of European countries, especially France, Germany and Switzerland, commencing in the middle of the last century. In Britain, in the latter part of the 19th Century, British merchants shipping goods to Australia created one of the first recorded demands for export credit insurance. After the First World War, the perceived need of many European countries to protect and expand their external reserves and to stimulate employment through the promotion of export activity, added a new dimension to the conception of export credit insurance. This was clearly illustrated in 1919 when the British Government launched the original official export credit scheme with the object of encouraging exports to Eastern Europe where credit risks were considered to be a serious deterrent to the development of British exports.

From that time to the present day, a steadily increasing number of countries in both the developed and developing world have seen in the establishment and development of an export credit insurance scheme an important tool for promoting their export trade, increasing employment opportunities and improving the credit side of their balance of payments. At the same time, the growing incidence of risk in international trading arising from political unrest, trade embargoes and the restrictions imposed by importing countries in balance of payments difficulties on the transfer of foreign exchange required to make payment to foreign suppliers, has boosted the demand from exporters and their financiers for the protection of credit insurance.

(b) THE BERNE UNION AND RECENT DEVELOPMENTS

As long ago as 1934 the emergent practitioners of export credit insurance realised the wisdom and value of co-operating in the development of underwriting techniques and in exchanging information on payment experience and other matters of mutual interest. In that year the export credit insurers in France, Italy, Spain and the United Kingdom founded the Union whose full title today is the International Union of Credit and Investment Insurers.

Since the 1939/45 War, insurance against political and commercial risks in international trade has assumed steadily increasing importance. Both state controlled organisations and private insurance companies constitute the membership of the Union, all participating as insurers and not as representatives of their governments.

The Statutes of the Union provide that its purpose shall be to work for:-

- (i) the **international acceptance** of sound principles of export credit insurance and the establishment and maintenance of discipline in the terms of credit for international trade;
- (ii) international co-operation in encouraging a favourable investment climate and in developing and maintaining sound principles of foreign investment insurance; and
- (iii) to provide for the exchange of information, assistance, expertise and advice in relation both to the commercial and political risks involved in export credit insurance, to the political risks involved in foreign investment insurance and to the range of associated matters relating thereto.

The break up of the Comecon trading bloc has presented a major challenge to the exporters of all the member countries of that group since they now have to compete for business in the international market place.

The responsibility of the management of individual enterprises for the assessment of the creditworthiness of individual countries and individual customers and the need to go to the emerging private market to obtain finance for export activities are new concepts which had to be absorbed and developed once the Berlin Wall came tumbling down. This caused governments to explore and recognise the need for export credit institutions and now only Bulgaria of the old Eastern Bloc countries is without an officially supported export credit institution. Moreover, in the countries of the former Soviet Union there are also developments in this field -in Russia itself and in some of the newly independent States such as Kazakhstan and Uzbekistan.

In other parts of the world, export credit schemes have been.. or are in the process of being, set up in such diverse places as Botswana, Colombia, Chile and Trinidad.

2. THE ROLE OF GOVERNMENTS

Export credit insurance is provided or supported by Governments because they want to encourage national exports. Government intervention has been considered necessary since it is generally believed that the risks, especially the political ones, are too large and unpredictable to be borne by private insurers who need to make a profit to live.

There is no fundamental reason why export credit insurance should not be provided by private sector insurers, at least as far as the commercial risks noted above are concerned. Their evaluation calls for judgements similar to those made by banks and other providers of credit in the ordinary course of their businesses; there are many private sector companies who provide credit insurance against the commercial risk to both domestic traders and exporters. There is, however, much less involvement by the private sector in the insurance of the political risks and such insurance is often only available directly or indirectly from governments interested in furthering their national interest by encouraging exports. Large and unusual commercial risks may also be insurable only with governmental insurers or reinsurers.

In the countries of the European Economic Community it has been determined that Government support in the export credit insurance field should not be applied to business

which can be insured or re-insured by the private sector. This led to the British Government selling the U.K. insurers (E.C.G.D.) short-term business to the Dutch insurer, N.C.M. E.C.G.D. remains as a Government insurer confined to medium and long-term business. In recent years the private insurance market has shown an increasing willingness to become involved with export credit business, including some greater involvement in political risks. However, outside Europe Governments are still by far the major players in this field.

3. INSTITUTIONAL STRUCTURES

The involvement of Governments in the structure and management varies widely from country to country. The main categories are:

- (a) Government departments: ECIS in Cyprus, EID/MITI in Japan, ECGD in U.K.
- (b) State bodies or government agencies: OND in Belgium, SACE in Italy, BANCOMEXT in Mexico, EXIMBANK in U.S.A.
- (c) 100% government owned corporations: EFIC in Australia, EDC in Canada, HKEC in Hong Kong, ECGC in India.
- (d) 100% privately owned companies:
 - (i) operating as agents of government: OEKB in Austria, HERMES in Germany.
 - (ii) with partial reinsurance from government: CASC in Argentina, NCM in Holland, CGIC in S. Africa, ZCIC in Zimbabwe.
 - (iii) with no official link with government but with reinsurance agreements with national ECA's: SIAC in Italy.
 - (iv) purely private: T.I.C. in U.K., FEDERAL in Switzerland, EXGO in New Zealand.

CONTROL AND DECISION MAKING PROCEDURE

Most ECA's have Boards of Directors but their composition varies very much from one agency to the other: representation of shareholders, mixture of private and public bodies, representation of various public bodies and of regions, exporters and export associations and financial institutions, especially Banks, etc.

The role of the Board, its involvement in the daily business, in the setting of guidelines also differs widely from one agency to the other. In some countries the Board has only an advisory function.

Some members also have to report to or receive guidelines from other (guardian) authorities, advisory bodies etc., who usually are an arm of their government or dependent upon it. The impact of these various bodies on the -decision making, again, varies from country to country.

In summary, you are involved in a significant, growing, diverse and challenging aspect of international trade.

4. TRADE INSURANCE

The purpose of export credit agencies (ECAs) is to provide exporters with insurance against the risk of non-payment for their sales to foreign customers. The provision of such insurance often has the additional benefit of facilitating the generation of export finance from banking sources; some ECAs provide export finance themselves.

(a) THE RISKS

ECA's are concerned with two types of risk:

- (i) the commercial (or buyer) risk - the risk that a foreign buyer will fail to meet his payment obligations to his supplier due to default or insolvency, and
- (ii) the political (or country) risks, including:

The transfer risk i.e. the risk that a buyer with adequate local funds available to meet his obligations, is unable to obtain the foreign exchange required to meet those obligations;

the risk that previously issued authorities to import and/or pay for goods ordered and/or supplied may be revoked by the relevant authority in the buyer's country;

the risk that the occurrence of war, revolution etc. may prevent the completion of a transaction either so far as the shipment or delivery of goods, or payment for them, is concerned;

the risk that the authorities in the exporter's country may cancel a previously issued export licence or introduce new licensing requirements that frustrate an exporter's contract.

(b) FINANCIAL OBJECTIVES

As with all insurance operations, ECAs charge a premium for their services. Private sector ECAs seek to operate profitably and therefore charge market rates that they consider likely to achieve this aim. Government or government-backed ECAs are required by the provisions of the WTO* not to operate as a subsidy mechanism and generally, seek to at least break even on their operations over time by charging premium rates adequate to cover claims payments and administrative expenses. The imponderability of the political risks is illustrated by the balance of payments problems experienced by many third world and other countries in the 1980's, which gave rise to very large claims payments by the larger ECAs and to the build up of substantial cumulative deficits on their operations in recent years, which have only recently started to be redressed.

Some ECAs have a 'national interest' provision in their constitutions which enable them to refer to government., propositions which do not satisfy their established underwriting criteria but which are of significance, in terms of the national interest of their country. If government accepts such a risk the premiums and the responsibility to pay any claims are for the account of government and not the ECA.

Australia, United Kingdom, Belgium, Sweden and USA are amongst many countries which have some form of national interest provisions. While there are no generally accepted guidelines, the main criteria for giving support under 'national interest' can be summarised as follows:-

importing country risk (off cover for normal business, not judged creditworthy considering the amount of the transaction, uncertainties as to future, etc.)

risks linked to the project (very high value, long term, aid nature of the contract)

home country consideration (goals set for national policy, especially in relation to support for certain industries, matching unconventional credit terms, encouraging the private sector to get into certain developing markets, i.e. pump priming)

* World Trade Organisation

These criteria are often applied in conjunction with one another.

(c) TYPES OF BUSINESS COVERED

Export credit insurance schemes were originally designed to provide protection for an exporter who entered into a contract of sale with an overseas buyer on credit terms evidenced by a sight draft, bill of exchange, promissory note or some such well established payment instrument. As the provision of credit facilities to oil the wheels of international trade has become both more extensive and increasingly sophisticated, embracing virtually the whole gamut of trading activities in goods and services, export credit insurers have increased the range and scope of their insurance facilities to meet the demand for protection against the various risks of loss.

Consequently most export credit insurers now offer cover against the particular risks arising when services are provided either alone or in tandem with the supply of goods, when constructional works contracts are entered into, when the goods are leased rather than sold or when goods are delivered to stock or sold through the overseas subsidiary of the insured exporter. These are but a few examples of the growing sophistication of export credit insurance facilities.

Moreover, some export credit insurers in countries which are important suppliers of capital equipment, whose sales involve the most extended risks horizons, have introduced various forms of cover in relation to the foreign exchange risk where their exporter is contracting in a currency other than his own. Such cover is usually only applicable from the time the normal forward exchange market facilities are no longer available and/or where the exporter has to quote a firm price in foreign currency and then be exposed to possible currency fluctuations. while the buyer decides whether or not to award the contract to him.

The type of business covered by ECAs can, generally, be divided into two basic categories:

1. short term credit business involving the sale of raw materials, commodities and consumer goods on credit terms of not usually longer than 6 months, and

2. medium and long term credit business involving the sale of capital and quasi capital goods on credit terms up to 5 years or more, depending upon the nature of the equipment to be supplied and the value of the contract. Contracts for the supply of complete projects may attract longer credit terms up to 10 years or beyond in exceptional circumstances.

Cover on transactions on short credit terms is usually made available under an umbrella policy that requires the exporter to offer for insurance, if not the whole of this export turnover, a spread of his business that is acceptable to the ECA. Cover may be made available against the risks outlined above from date of contract or from date of shipment. Exporters of specialised goods likely to suffer a loss should an insured risk occur before shipment, are likely to be interested in the former cover; exporters of more standard items normally find cover from date of shipment adequate for their needs. Premium rates reflect the credit terms involved and the ECAs perception of the risk, in particular its political risk component. The proportion of loss covered is usually less than 100% in order to leave the exporter with an interest in the debt and its recovery. In the case of most causes of loss claims are paid at a set period after the occurrence of loss to allow time for delays in payment for administrative reasons etc. to be remedied.

Cover for transactions on medium and long-term credit is, usually, provided by the issue of an individual policy for each transaction. The general terms and conditions of such cover are similar to those noted above in respect of short-term cover.

A number of ECAs also provide guarantees to banks who finance the exporter's costs of production. These facilities are especially important for many small and medium sized exporters who would not otherwise be able to satisfy the security requirements of their financiers. This has emerged as a major problem in many developing countries and such facilities play an important part in the activities of ECAs in countries such as India, Philippines and Indonesia.

(d) PROCEDURES

The administration of cover involves:

- The establishment of an underwriting policy towards particular foreign markets and the assessment of the creditworthiness of particular buyers.

This requires the export credit insurer to build up a database of credit information and payment performance on the overseas customers of their export clients. Such information is obtained primarily from specialist credit enquiry agencies and banking sources. However some limited discretion to operate without reference to the ECA may be agreed for short term cover on the basis of the ECAs evaluation of the exporter's past experience and credit control system;

- the notification by the exporter to the ECA of business conducted under short term cover thus providing the basis for the periodic collection of premium and the monitoring of the insured's performance; premium for medium and long term cover is usually collected when the insurance policy is issued;
- the notification by the exporter to the ECA of potential losses;
- the establishment of claims examination and payment procedures;
- procedures for the pursuit of debts that have given rise to claims payment i.e. recoveries.

(c) INTERNATIONAL CONSTRAINTS ON ECAs OPERATIONS

The terms of payment supported by ECAs are, in the interest of prudent underwriting and the desire not to distort normal trading practices, regulated by voluntary agreements between ECA members of the International Union of Credit and Investment Insurers (the Berne Union). Additionally, the terms of payment for medium and long term credit transactions two years and over are regulated by the OECD Arrangements on Guidelines

for Officially Supported Export Credits (the Consensus) which sets minimum interest rates, minimum down payments and maximum credit periods permissible for such transactions.

The Berne Union understandings on maximum terms of payment are:

- | | | | | | | | | | | |
|------------------------|---|---|------------------------|---------------|----------|---------|-----------|---------|-----------|---------|
| i) | Raw materials and semi manufacturers | - 6 months | | | | | | | | |
| ii) | Consumer goods and consumer services | - 6 months | | | | | | | | |
| iii) | Consumer durables (including related services) | - Normally 6 months but maximum of 2 years | | | | | | | | |
| iv) | Parts or components (including related services) to be incorporated into quasi capital or capital goods | ~ Normally 6 months but up to 5 years depending on life of the part and unit value | | | | | | | | |
| v) | Quasi capital goods (including related services) | <table border="0"> <tr> <td>Minimum Contract Value</td> <td>Credit Length</td> </tr> <tr> <td>\$75,000</td> <td>3 years</td> </tr> <tr> <td>\$150,000</td> <td>4 years</td> </tr> <tr> <td>\$300,000</td> <td>5 years</td> </tr> </table> | Minimum Contract Value | Credit Length | \$75,000 | 3 years | \$150,000 | 4 years | \$300,000 | 5 years |
| Minimum Contract Value | Credit Length | | | | | | | | | |
| \$75,000 | 3 years | | | | | | | | | |
| \$150,000 | 4 years | | | | | | | | | |
| \$300,000 | 5 years | | | | | | | | | |
| vi) | Capital goods and project services | - 5 years or longer | | | | | | | | |

The following specific agreements apply

The current Agreements are:

Breeding Animals

Normal credit terms are 180 days

The maximum credit terms currently permitted for cattle are:

2 years credit for contracts up to \$150,000 and 3 years for contracts over \$150,000 but, where more than 2 years credit is granted, a downpayment by delivery of 15% of the contract price should be stipulated.

Bus and Bus Chassis

The maximum credit terms currently permitted are:

5 years from delivery with 15% on or before delivery

Containers and Semi-Trailers

The maximum credit terms currently permitted are:

5 years from delivery with 15% on or before delivery

Agricultural Vegetable Reproduction Material

The maximum credit terms currently permitted are:

360 days from delivery

Paper/Pulp and Lumber/Timber

The maximum credit terms currently permitted are:

180 days from delivery

Fertilisers, Insecticides, Pesticides and Fungicides

The maximum credit terms currently permitted are:

12 months from delivery

On-highway Lorries and Lorry Chassis

The maximum credit terms currently permitted are:

5 years from delivery with 15% on or before delivery

5. INVESTMENT INSURANCE

(a) PURPOSE

Apart from supporting the export of goods and services, twenty four of the Berne Union Members provide a foreign investment insurance facility to protect investments by their nationals in foreign enterprises against loss from such events as expropriation, non-transfer of dividends, war and civil strife. The outstanding amount insured is approximately US\$ 43.5 billion.

Two (TREUARBEIT in Germany and OPIC in USA) are specialised in investment insurance, while the others are also export credit insurers. In addition, MIGA, the Multilateral Agency created by the World Bank to guarantee investment is also a member.

CHAPTER II

EXPORT CREDIT AND EXPORT FINANCE

Introduction1. The provision of export credit insurance is a very effective way of stimulating exports. It is, however, a separate activity from the provision and funding of export finance, although they can be closely linked.

Background

2. Each year the 46 Members/Observers of the Berne Union the International Association of Export Credit and Investment Insurers cover about \$420 billion of exports and about \$15 billion of foreign exports, 90% is in respect of goods and services sold on cash or short term credit (i.e. up to 180 days) and about 75% is in respect of exports sold to buyers in OECD countries.

3. It is clear from these figures that it is quite wrong to see export credit as involved only (or even mainly) with:-

- (a) Medium and Long term credit for capital goods or manufactured goods
- (b) Exports to Developing Countries or non-OECD countries

4. Indeed a key reason for having an Export Credit Agency is to encourage and support exports sold on cash or short credit to OECD countries.

Bad Reasons for Having an Export Credit Agency

5. As the rest of this paper shows, there are many good reasons for establishing an Export Credit Agency.

6. However, there are also a numbers of bad reasons. For example:-

(a) It is not helpful to either exporters/banks or the exporting countries themselves to stimulate, encourage or support exports to countries or buyers who will not pay for them.

(b) It is expensive and wasteful to use medium and long term export credit as a way of subsidising interest rates paid by overseas buyers. The beneficiary of the subsidy is of course the overseas buyer. OECD countries have learned the hard way how expensive and distorting and wasteful of public expenditure these blanket subsidies can be; this is why they are being phased out. They are, of course, much easier to introduce than to withdraw.

(c) It is not necessary to establish an ECA in order to provide bank finance to exporters in the manufacturing or pre-shipment stage; especially if such finance is provided at subsidised rates of interest. In any case, the provision of this kind of "overdraft" finance is a normal commercial bank function and it gets banks into bad habits if the Government involves itself in these day-to-day market / commercial decisions, as well as being very expensive for Governments who normally end up with all the bad debts.

Political Risks and Commercial Risks

7. There are many risks involved in exporting but the two categories most usually covered by export credit are political risks and commercial risks.

(a) Political Risks

The main kinds of risk are those relating to the actions of Governments of buying countries in preventing payments being made for imports, e.g. problems with transferring foreign currency, the imposition of import controls, war/civil war, defaults by Government or Public Sector buyers/guarantors.

(b) Commercial Risks

The main risks are the insolvency of the buyer, default or repudiation/refusal to accept goods/services.

8. It is a very common - and very expensive - mistake to believe that it is only political risks which give rise to problems and losses and thus that exports to OECD countries are "safe". Most of the Members of the Berne Union pay substantial commercial risk claims every year - and especially during recessions - on the United States and EC countries. This simply reflects the large number of private companies who every year become insolvent or default on payments.

Protection Against Risks

9. The traditional and still the major reason for having an E.C.A. is first to provide exporters with the confidence to export (i.e. confidence that they will be paid) and second to protect them against losses. For new or smaller companies, one bad debt can be significant enough to cause them to become insolvent.

Access to Bank Finance

10. Export Credit Insurance provides a very useful security for exporters to use with their banks to obtain bank/overdraft finance. In addition, to provide even greater security to a bank, the insurance cover can be given direct to the financing bank by the E.C.A. This is a very important point in most countries but especially in countries where the banking system is undergoing significant change or where new banks may be unfamiliar with the mechanisms and techniques of foreign trade financing.

Information

11. Information on overseas buyers and countries is expensive to obtain and keep up to date. It is not, therefore, cost effective for all exporters (or banks) to try to do this for-themselves. Worse still, is for them to sell (or finance) "blind" with no information. An E.C.A. thus offers the possibility of a single/central body collecting and maintaining

information (and exchanging it with similar bodies overseas) and thus obtaining economies of scale to the potential benefit of all those in the country involved with foreign trade.

Expertise

12. Like information, expertise in technical aspects of foreign trade and trade financing is scarce and expensive. An E.C.A. provides a focal point within which to concentrate these scarce resources (and a cost effective way of obtaining and developing them).

13. In other words, an E.C.A. offers more to exporters and banks than insurance only.

The Importance of Marketing

14. The need for export credit insurance and the many varied benefits it can bring (see paragraphs 9-13 above) are not always obvious to companies, banks and administrators, especially where an economy has been operated on a "State Trading" basis, i.e. effectively where the Government made all the key decisions and took all the risks.

15. Thus there is a vital need:-

(a) for an E.C.A. to develop its products with particular reference to the situation in its own country (and not simply transfer/import products and facilities offered by E.C.A.s in other countries).

(b) to give great attention to and emphasis on active and professional marketing to both companies and banks. In other words, it is no use simply waiting for customers to come to see the E.C.A.. The E.C.A. must get out into the business and banking community and vigorously market its products and services.

Political Risks

16. It is unusual for political risks on buyers and countries outside the OECD to be underwritten either on its own account by a private company or E.C.A. or for the Private Reinsurance market to be willing to reinsure such risks.

17. It remains difficult to reinsure medium and long term political ' risks (including risks on Government / Public Buyers) in the Private Reinsurance Market.

18. Thus, for all those Members of the Berne Union who provide Medium and Long term insurance cover, this business is either reinsured by the Government or written on a "National Interest" basis on the account of the Government. Some short term business may also, in specific circumstances, be handled in this way.

Decisions on Political Risks

19. Decisions on political risks (especially on Medium and Long Term cover) are thus usually taken by the Government. It would be a normal arrangement in most countries for political risks on buying countries or on individual cases to be considered by a Government Committee of some sort. Such a Committee would either take the decision or make Recommendations to the Ministry or Ministers who will take the decision(s).

20. In many countries, the Chairman of such a Committee will often come from the Ministry of Finance or Treasury.

21. Amongst the Government Ministries or Departments or Institutions which would usually be represented at a very senior level on such a Committee would be the following:-

- (a) Ministry of Finance or Treasury
- (b) Ministry of Trade or Foreign Trade
- (c) Ministry of Foreign Affairs
- (d) Ministry of Foreign Economic Relations
- (e) Ministry of Foreign or External Affairs
- (f) Ministry of Industry or Commerce
- (g) Ministry of Agriculture
- (h) Central Bank

22. The decisions taken by such a Committee would either set the limit on business which can be insured on a particular market (e.g. exposure on, say, New Zealand can be underwritten of up to \$25 M on short credit terms and up to \$50 M on a medium and long

credit terms) or to approve an individual case (e.g. exposure of \$15 M can be underwritten on a project to supply engines to the Electricity Board in Turkey). Often such Committees will also approve the premium rates which will be charged for such business/cases.

23. It is often helpful for the Secretariat for the Committee to be provided by the E.C.A. and for recommendations on countries or cases to be made to the Committee by the E.C.A.

Accounting

24. It can be helpful when underwriting such business for two things to happen:-

(a) First, from the premium paid by the exporter for the cover, a fee for the administration of the cover should be deducted and retained by the Export Credit Agency to meet its costs.

(b) Second, for the balance of the premium on such cases to be retained in a special foreign currency account and not paid into general Government revenues. This special account can then be used to finance or pay any claims on such business, which may be submitted in due course by exporters. Thus only if there is not sufficient funds in the account to pay claims would the Government be asked for funds.

Export Finance

25. The points above relate to export credit insurance. However, in many countries there can be problems in funding or financing export credit. They can arise in two main ways.

Pre-Shipment Finance

In some countries, it can be difficult for the commercial banks to provide finance to exporters to enable them to carry out export contracts. In OECD countries, such finance normally comes from an exporter's working capital or from his overdraft from a commercial bank.

However, in other countries, the commercial banks may not be either liquid enough to provide working capital on the necessary scale or they may be cautious about lending on the scale required or may require special security from exporters for such lending.

In such cases, the exporter can sometimes be helped to obtain the necessary working capital for pre-shipment finance if either the insurance from the E.C.A. is assigned to the bank or if the E.C.A. can give some kind of insurance direct to the banks.

29. ECA's need to be cautious about underwriting the exporter (as opposed to the overseas buyer) as there can be problems in sharing security etc. with the banks. However, in some countries, special schemes exist under which the E.C.A. gives cover to the banks who provide working capital/preshipment finance to the exporters (e.g. in Indonesia and Mexico).

Medium and Long Term Finance

It will sometimes be the case that the commercial banks are unable or unwilling to fund medium or long term credit. For example, if an exporter sells on 5 year credit to a buyer overseas, he (the exporter) will normally expect to be paid by his bank by delivery and then the bank waits to be repaid by the overseas buyer/borrower over the 5 years. Repayments of principal and payments of interest will normally be made at six monthly intervals during the credit period. The repayment risks (both political and commercial) will normally be covered by the insurance from the E.C.A. but this still leaves the financing bank with the funding problem. In many countries, this is a problem, which the commercial banks cannot solve, i.e. they are unable or unwilling to raise either from domestic or international sources to the 5 year deposits to "match fund" the credit extended to the overseas borrower/buyer.

-In some countries, this problem/difficulty has been approached by the Export Credit Agency giving guarantees direct to the banks but, in other countries, this has not solved the underlying funding problems and so the Export Credit Agency or some other Government institution have been involved in funding.

The funding, in some countries has been taken over by Eximbanks. There are two main kinds of organisation:-

(a) Direct Lenders

There are institutions who lend direct to overseas borrowers or buyers (e.g. as in the USA and Canada). The advantage of this arrangement is that it is direct and often raises and disperses funds in the lowest cost way. The main disadvantage is that it prevents the commercial banks from developing the ability to borrow and lend for medium/long term credit and can also inhibit the development by the commercial banks of other export and trade finance skills.

(b) Refinancing

There are institutions who raise funds but do not lend direct to borrowers or buyers but refinance or fund facilities extended by the commercial banks (e.g. as in Austria).

33. There is no single best way of organising these institutions and so there are various kinds of banks. For example:-

(a) Institutions such as those in the United States (similarly in Australia, Canada and Turkey) both provide long term loans direct to overseas borrowers and also provide associated and, where necessary, free standing export credit insurance.

(b) Institutions such as those in Sweden, India and Korea operate separately. In other words, the funding and finance is provided for long and medium term exports direct to overseas borrowers/buyers but the associated (or free standing) export credit insurance is provided by a separate institution. It is possible for the export credit institution to provide insurance to the export \ import bank.

(c) In Japan the export credit institution (EID/MITI) and the Exim bank are quite separate and insurance is not provided by the export credit institution 'to the Export Import Bank. In other words, where the Export Import Bank lends on a medium and long term basis, then no insurance will be provided. Conversely, where export credit insurance is provided in respect of medium and long term credit transactions either to exporters or to commercial banks, then the Export Import Bank will not be involved.

(d) In Austria (and soon in the Czech Republic), the institution can raise funds in its own name (or with a Government or Central Bank guarantee) and can then refinance medium and long term credit facilities extended by the commercial banks. Such institutions can either be

part of or separate from the E.C.A.'s. However, if they are part of the same institution then it is very important that the activities (or certainly the Accounts) are kept separate.

What is the Best Kind of Organisation?

34. There is no single "model" which is the best one in all circumstances in all countries.

35. The key should be to produce an institution and an arrangement, which are best suited to the particular needs of the country involved. They may need to change as, for example, the activities and expertise of the commercial banks increase.

Main Activities

36. It is helpful to distinguish between three major kinds of activity in a Financing (or Refinancing) Institution. The major ones are:

(a) Raising Funds

This will probably need to be done in the international capital markets and, for many countries, the finance will need to be raised in the name of, or with the guarantee of, the Government. The "cleaner" the guarantee, the lower is likely to be the margin, which has to be paid to the lenders/providers of the finance. It is important that the borrowing or capital raising activity is very closely aligned with the other international borrowing of the Government and/or the Central Bank. Advice on trimming and pricing and terms can be obtained from foreign merchant banks etc.

(b) Holding Funds

Since it is very unlikely that it will be possible to raise the funds at (a) above exactly to match loans for medium and long term export credit on a case-by-case basis, there will be a need to "hold" funds. In other words, there will be mismatches between borrowing and lending/refinancing. Since interest will have to be paid on the borrowings, the funds must be

used so as to raise income to pay the interest until such time as the funds are used for the export credit contract. This is a "Treasury Management" function but it requires special skills if losses of various kinds are to be avoided.

(c) Lending/Refinancing

This nature of this activity will depend on whether the institution is to be a direct lender or a provider of refinancing. An important point will of course be whether such funds are to be restricted to export contracts which are insured by the E.C.A.

37. In all of these activities the links with the Central Bank will be of central importance but much will also depend on the skills and experience/expertise and balance sheet strength of the commercial banks. The role of the Bank Supervisors will also be important in terms of how they treat (for balance sheet weightings and risk ratios) the export credit lendings of the commercial banks.

Summary and Conclusions

38. The role of the E.C.A. is very important. This can be concentrated on insurance but this can also involve or have a very close relationship with financing and funding. There is no single or best solution of universal applicability. Systems need to be designed with particular reference to the individual circumstances of the country concerned.

39. What is best for an individual country at a particular time depends on a number of factors. It is a mistake to try simply to "transplant" a model from another country. Many countries have tried this and have failed or have had to make rapid changes to the model they "imported".

40. Thus the essential first stages are:-

To analyse the needs of the individual country and its exporters and banks.

(b) To be aware both of the various arrangements which apply elsewhere and the various kinds of institutions which operate in different countries (some of which are referred to above).

(c) To try to develop the institution(s) for the country from the "models" at (b) which should fit the needs of (a).

CHAPTER III

OPPORTUNITIES AND RISKS IN INTERNATIONAL TRADE

INTRODUCTION

At the request of the conference organisers, concentration will be mainly upon short term business which constitutes the bulk of international trade. Accordingly there will be no reference to business conducted on medium to long term credit.

Technicalities will be referred to only briefly. The focus will be on those issues with which managements should be concerned.

OPPORTUNITIES AND RISKS Few opportunities are without risk. However many risks do not necessarily represent opportunity.

To a significant degree they are indivisible elements in the larger picture.

Before turning to a consideration of specific Risks and specific Opportunities several observations of a more general nature, but which bear upon the specifics.

Exploiting opportunity, having first identified it, depends partly on the nature and magnitude of the risks you are prepared to assume.

The identification and exploitation of opportunity in International Trade should flow from the Basic Objectives of your enterprise eg. is International Trade to be Y% of your total revenues or 3Y%? Is it to come from developed countries or undeveloped countries? What is the Maximum Risk Exposure you will accept? The answers will obviously influence strategies and outcomes.

But the first imperative is that the Objectives are clearly defined.

Successful outcomes will rest to an extent upon the Resources committed to the objectives.

The most vital Resources are Capital, Strategic Alliances and People.

Sound capitalisation is fundamental. Although it states the obvious, many have failed to recognise that thin capitalisation may cause the enterprise to falter and perhaps topple in adverse winds. Conversely, sound capitalisation gives both a solid base to the business and an important flexibility - such as the chance to try new markets and to assist in the diversification of your sources of revenue, whilst keeping to the business you know.

Strategic or Operational Alliances often play a valuable part in international trade. Knowledge of local trade and conditions in a foreign country is invariably an advantage and may help cement a profit or avoid a loss! Local partners of good repute and substance are frequently the difference between success and failure offshore. Such partnerships may well be at different levels - Strategic where you are seeking to establish direction and purpose, or Operational for the day to day needs of the business and vital linkage to your home-based staff.

However the most important resource is your people. Successful enterprises usually have quality staff, well selected, well trained, well motivated and rewarded, but above all they will be well led. In tomorrow's world it will be more important than ever for leaders and their people to have the knowledge, intelligence and flexibility to recognise changing economic and industry trends - which will occur faster than in today's world. Then, having recognised them, to devise successful strategies for change.

RISKS

What is the nature and magnitude of the risks in International Trade? How are they to be managed? It is tempting to assume that all risks are external. The fact is that some of the principal risks are internal - with your own enterprise.

They include: failure to clearly identify the Objectives of the enterprise; undertaking business risks with which the business is unfamiliar; setting unrealistic revenue and profit targets, especially in the short term, and finally but not exclusively; having the wrong people in positions of responsibility.

All of these risks are controllable if management is effective. Unfortunately, inadequate management has sometimes ignored or failed to perceive these risks. They can have serious consequences for profit, asset values and at worst, may imperil the very existence of the enterprise.

A common fault in the management of risk (in addition to the failure to understand the risk!) is failure to place monetary limits on the exposure of the enterprise to any one country, industry or buyer. Compounding this problem is the difficulty of recognising the interrelationships, which may exist between different buyers to whom there is an exposure. Ideally your enterprise should be able to withstand the failure of your major debtor risk. This however is a test, which many creditor companies would not survive.

The external risks are perhaps more apparent, if only because they are further away and we are able to focus more objectively upon them.

By definition International Trade involves dealing with buyers in foreign countries whose culture, legal system, and economic well being may be quite different from that to which you are accustomed. Accordingly your knowledge, whether of country, industry, or buyer may not be of the order you would expect of a domestic transaction.

International Trade will frequently involve a greater degree of uncertainty and unpredictability than domestic trade, and your ability to influence or control outcomes will almost certainly not be of the same order.

It is interesting to note that in the period from 1990 to 1995 a significant change took place in the direction of the exports of Thailand and of all of its major export markets. In 1990 Industrialised Countries (excluding Japan) accounted for 50% of Thailand's exports and from 41 % for Singapore to 59% for Japan. By 1995 these figures had fallen to 36% for Thailand, 35% for Singapore and 48% for Japan.

Perhaps not surprisingly, exports to Asia, including Japan, had risen sharply. In 1995 they accounted for 53% of Thailand's exports (39% in 1990), 55% of Singapore's 51 % in 1990) and 44% of Japan (31 % in 1990).

These figures, a representative few, give some indication of how significantly the risk element attaching to the direction of a country's trade had shifted in a short period. Intra - Asian trade had become much more significant than trade with the non Asian world in the relatively brief period of five years.

Adversity can arise with bewildering speed. The events in Asia during recent weeks provide a graphic illustration. The global market place is with us, and nowhere is there a haven from economic or commercial damage.

The rate of change in economies, industries and enterprises is rapid, and not likely to become less so in the near future. It is profoundly important that the risk of change is both anticipated and recognised --- and then turned to advantage.

In today's world, external events are more likely than ever to influence not only international trade but also, and possibly more significantly on occasions, domestic trade.

Globalisation will continue to bring many benefits. It will also create risk. One example is the increasing demand for more liberal terms of payment, Buyers who would in earlier days have almost automatically paid by Letter of Credit are now quite often calling for terms - and, not infrequently, on Open Account. There is little doubt this development is exposing more Exporters to more risk, a risk that can be mitigated by the use of Credit Insurance.

From the technical perspective of a Credit Insurer the specific risks in International Trade fall into two broad categories, Commercial Risk and Political Risk.

Commercial Risk covers the, Insolvency of the Insured Buyer and the Buyer's Protracted Default. The latter comprises only a modest percentage of Commercial claims against Credit Insurers. Coverage is usually for 85% of loss, incurred - With individual Insurers varying this percentage by 5% up or down.

Political Risk covers loss arising from events in the Buyer's country such as war, civil riot or commotion, exchange transfer delays or blockage, and cancellation of import licences. Insurers usually cover approx. 90-95% of the amount of loss incurred due to Political causes.

The majority of claims paid by credit insurers are caused by commercial events. Moreover, from an historical viewpoint, political events causing loss are far more likely to arise in the less industrialised countries. Examples of political events causing claims for credit insurers in recent years have been: conflict in Kuwait; the collapse of the Soviet Union; and banking difficulties in Turkey, Venezuela, Argentina, and Bulgaria.

It is a fact that the distinction between Commercial Risk and Political Risk is becoming a little blurred around the edges. A significant devaluation of the currency of the buyer's country may well have a serious impact on the buyer's ability to meet import costs in his now, devalued currency - a commercial event caused possibly by political developments after the goods were imported.

Traditionally the bulk of Political Risk support has come from Governments standing behind their State owned insurer. However there has long been a private reinsurance market for Political Risk provided partly from Lloyds and partly from the general reinsurance market. There are some indications that the private market may be developing a larger appetite for Political Risk than has been the case for many years. Should this prove to be the case then the demand for such cover may increase still further to capitalise on the additional capacity available.

THE ROLE OF CREDIT INSURANCE IN MITIGATING RISK Briefly put, credit insurance provides policyholders (trade creditors) with protection against loss arising from the insolvency of their trade debtor, or from loss arising from defined "political" causes of loss. Europe was the birth-place of credit insurance. It remains the dominant force to the present time, although strong growth has occurred beyond Europe.

The industry is represented by two world wide bodies. The Berne Union of Credit and Investment Insurers, and the International Credit Insurance Association. Both were formed in the 1920's. The Berne Union membership is composed mainly of Government Departments or Agencies, or corporations in which Governments have a majority shareholding. Of the Berne Union membership of 46 (from 38 countries) most are public enterprises although some of the largest members are from the private sector. The ICIA membership of 45 (from 28 countries) includes a number, which are also members of the Berne Union.

Between them they insure an estimated 10% of exports from member countries. ICIA members also insure an estimated US Dollars 1000 Billion of domestic trade.

It is undoubted that credit insurance has become an important facilitator of trade. This is perhaps not surprising given that credit insurance protects cash flow, profits, assets, and not infrequently the very existence of the policyholder.

It is however important to recognise that credit insurance is not a substitute for effective credit management. Rather it is a particularly useful aid to the competent credit manager. And, most importantly, credit insurance cannot turn a bad risk into a good risk. Credit insurance is also a valuable marketing and sales weapon, an aspect of the industry which has not been sufficiently well presented by the industry, and which accordingly, is not clearly recognised by industry and commerce.

Credit insurers have access to economic, industry sector and credit intelligence on a worldwide basis, so not unreasonably they should be able, and are indeed expected, to add value. Additionally the credit insurer would be expected to have formidable export, and where appropriate, domestic trade sector expertise.

To illustrate the point, Trade Indemnity was the UK's largest privately owned credit insurer, covering in excess of US Dollars 100 billion of trade credit annually of which approx. 25% was export business. Of its 800 staff approximately 130 were engaged in Underwriting or Risk Management for both, Domestic and Export business. They were expected to have trade sector competence (if not expertise), and, for the export business, a strong knowledge of international trade practice and country risk.

A final point before turning to Opportunities is that a close working relationship between the policyholder and the credit insurer is important. The relationship is closer than that of many bank / customer relationships - usually with beneficial results.

OPPORTUNITIES International trade is the economic life force of many nations. It has grown strongly and consistently for many years. In particular it has grown strongly in Asia, where the rate of growth has outstripped that of North America and Europe by a wide margin.

Despite recent upheavals, it is more than likely this story will be repeated over the longer term.

The emergence of China in the next two decades, as an economic powerhouse will itself impact significantly upon world trade, and Asia's role in particular.

There are numerous other influences. Trade barriers are gradually being removed. The wealth of nations is increasing. New middle classes are emerging. International barriers are being lowered. Overseas investment by many countries is increasing. Globalisation has become a fact of life. But perhaps most importantly of all, we have entered a new information / communication revolution which will transform economies, trade and enterprises to a degree we cannot at present imagine.

Each of these developments will create opportunities in international trade. More specifically the ability of an enterprise to be competitive will create opportunity - or lose it! But so it has always been. In future however the pressures to be competitive on an international basis will be far greater.

As an example let us consider some of the opportunities, which may lie ahead for Thailand - somewhat similar considerations would apply to other Asian countries.

A brief backward glance is educational. Thailand's rate of export growth has been exceptional by world standards, but in line with most other Asian countries. However, as mentioned earlier, most of the growth has occurred within Asia. Of the increase in Thailand's exports from 1990 to 1995 some 63% went to other Asian countries, 28% to the U.S.A. 4.2% to the Middle East, 3.6% to Eastern Europe, 1.1% to Africa and less than 1% to the South Americas.

Whilst these figures suggest that opportunities have been captured, they also highlight an undue concentration on two geographical areas. Penetration of Continental Europe is extremely low. Given the size of that market, and the greater dynamism which one would expect from acceleration of the E.U., there would seem to be attractive possibilities in that part of the world. Neighbouring Eastern Europe also has a very low penetration by Thailand. There are some markets which would present opportunity, Poland and Slovenia for example,

but their scale and time horizon would be decidedly more modest than those of Western Europe. A somewhat similar observation may be made of the South Americas.

Developing opportunities takes time, money and effort. We are back to the Resources issue discussed earlier. There is good reason to believe that if the resources are made available, and if an innovative approach is taken to product development and the establishment of alliances, then Thai exporters should be able to diversify their markets to a greater extent than evident in recent years. However we must not expect too much too soon. This is a strategic and tactical error made frequently by Western companies seeking out opportunities in Asia. There is no substitute for sound medium long term planning accompanied by stringent financial objectives and controls.

None of this is to argue for pessimism within the Asian region. You are now experiencing what many of us elsewhere have gone through, and unpleasant as it may be, there are numerous examples of such adversity leading to enhanced strength. There is good reason to feel that Asia will continue to represent one of the major areas of opportunity for Thailand's exporters.

Finally it is impossible to ignore the United States - one of Thailand's major export markets, and one which will continue to provide attractive opportunity, The world's largest economy has considerable underlying strength and flexibility It will surely remain a vital area of opportunity.

What are the risks for exporters in developing these opportunities? First it can reasonably be said that the U.S. and Western Europe represent very low risk from a political cause of loss standpoint. The same cannot be said of Eastern Europe, Africa, the Middle East or the South Americas, where stability, both political and economic, is of a somewhat lower order. Bearing in mind that in the near future both the U.S. and Western Europe could have interesting potential for Thai exporters, this assessment, if valid, is encouraging.

Whether the potential can be captured will depend on the results of research. For example, are your products appropriate, if not can they be adapted for the export market, what is the likely level of demand, what is the level of competition - these and many other questions need to be examined. Your country's Trade Offices often have good market intelligence,

international banks should provide helpful advice, and of course so should credit insurers. These avenues, together with your own research, will help you decide the quality of the commercial risks (as distinct from political risks) you face in developing a new market or more business in an existing market.

Many payment problems for exporters arise from either their excessive optimism about their buyer, based on years of satisfactory payment experience, or from relative ignorance about a buyer new to them. Both of these hazards can be lessened, by a combination of research, effective relationships with Trade Offices and international banks, and perhaps most especially, credit insurers.

A potential for Thai exporters to diversify their markets does seem to exist, and interestingly, if Western Europe is seen as a target, it is an area about which a great deal is known, thereby, one hopes, lessening the risk of engagement.

THE ROLE OF THE CREDIT INSURER IN EXPLOITING OPPORTUNITY

The Credit Insurer should be an essential element in the strategic considerations of any enterprise engaged in international trade. It has the capacity to enable the enterprise to step more broadly and yet more safely in the international arena. Skilfully used, credit insurance should assist in the diversification of markets, (thereby reducing any overdependence on any one market), in product innovation and in the broadening of the customer base. It can and has done all of these things, with enterprises of all sizes.

It has been said earlier that credit insurance protects cash flow, profit, and assets.

It also provides valuable market intelligence and an unrivalled quality of credit and risk assessment.

Close and effective cooperation between Credit Insurer and Policyholder should give the Exporter the potential to make increased sales to existing customers, to develop new customers in existing overseas markets, and to open up new markets.

The principal commodity possessed by Credit Insurers is Risk Capacity, which can be more effectively utilised by the Exporter and the Credit Insurer working in harmony.

The Banks have an important role to play. They are obviously heavily engaged in International Trade. Not infrequently Banks will have as collateral security policies of credit insurance, effected by the Exporter and assigned to the Bank. Whilst it is interesting to observe that Exporters seem to make more effective use of Credit Insurance than domestically oriented enterprises, there is still a good deal of room for better use to be made of Credit Insurance by both Banks and Exporters. Essentially, Banks should be able to lend more support to the Exporter, with a greater degree of security via the Credit Insurer, than would normally be the case in an uninsured transaction.

Competition is creating demand for credit. Many buyers who would previously have paid by Letter of Credit are now demanding terms - and quite often on Open Account. Credit Insurance has a particular value in such circumstances, enabling the Exporter to offer credit terms with the comfort of the Insurer behind the transaction.

Credit Insurers therefore have a practical and valuable contribution to make to the development of opportunities in International Trade. But there is ample scope for more to be achieved.

LOOKING AHEAD

It has often been said that there are only three certainties in life - Birth, Death, and Taxation. There is however another - Change.

The rate at which change now takes place is often literally breathtaking, and so on occasions, is its magnitude. But change so often brings with it Opportunity. Part of the challenge is to recognise the change and then to see how it can be turned to advantage.

The communication and information revolution which we have entered is but one example of tomorrow's opportunities. The emergence of China as an economic giant will be another. So too will opportunity flow from the continuing privatisation of Government enterprises - as will the changing nature of enterprises themselves in the coming decades.

Some of these opportunities will arise in International Trade. They cannot and should not be ignored. But Exporters, Banks and Credit Insurers will need to exercise imagination, intuition and innovation to seize the initiative. This may well require the leaping of a few conceptual hurdles, especially on the part of Credit Insurers and the Banks. But an ability to look beyond the horizon will be an invaluable asset.

The Export Community should regard credit insurance as a potent financial management and marketing and sales weapon. Credit Insurance is a dynamic, not a static weapon. Skilfully brandished it has the potential to Protect and Promote enterprise.

Those present today are either engaged in or about to embark upon careers in International Trade. It is in my experience a highly stimulating career, one which offers not only intellectual challenge but also the immense satisfaction of daily practical application.

There is one special challenge, which has both intellectual and practical application. It is to seek ways for the international community of manufacturers, traders, bankers and credit insurers to work more closely together. In so doing you will truly capitalise on opportunities whilst mitigating your risks.

Appendix 1 - Summary

(Global view on trade and investment insurance)

1. General characteristics of trade and investment insurance -covers risks for which private companies often cannot provide insurance -measure for the promotion of sound external activities -principle of balanced budget
2. Role of trade and investment insurance
 - providing security against risks
 - facilitating finance for external transaction
 - measure for trade policy of Government
3. Administration systems of trade and investment system
 - involvement of government
4. Underwriting policy
 - spread of risks
 - individual contract / comprehensive contract
 - risk analysis necessary for underwriting policy
 - political risk : country risk analysis
 - commercial risk : rating of overseas buyers etc.
 - underwriting condition
5. Future issues related to trade and investment insurance
 - positive underwriting policy as a governmental insurance
 - response to new type of finance
 - implementation of debt-relief
 - cooperation amongst the trade and investment insurance organization

SECTION 3

TRADE AND INVESTMENT INSURANCE SYSTEMS IN INDIVIDUAL COUNTRIES

**CHAPTER I TRADE AND INVESTMENT INSURANCE SYSTEM
IN THE U.S.A**

**CHAPTER II TRADE AND INVESTMENT INSURANCE SYSTEM
IN CANADA**

**CHAPTER III TRADE AND INVESTMENT INSURANCE SYSTEM
IN JAPAN**

**CHAPTER IV TRADE AND INVESTMENT INSURANCE SYSTEM
IN THE PHILIPPINES**

**CHAPTER V TRADE AND INVESTMENT INSURANCE SYSTEM
IN THE HONG KONG**

**CHAPTER VI TRADE AND INVESTMENT INSURANCE SYSTEM
IN THE CHINA**

**CHAPTER VII TRADE AND INVESTMENT INSURANCE SYSTEM
IN THE INDONESIA**

**CHAPTER VIII TRADE AND INVESTMENT INSURANCE SYSTEM
IN THE AUSTRALIA**

**CHAPTER IX TRADE AND INVESTMENT INSURANCE SYSTEM
IN THE THAILAND**

Chapter I

Trade and Investment

Insurance System of the United States of America

TRADE AND INVESTMENT INSURANCE SYSTEM IN THE U.S.

- U.S. Export-Import Bank (Ex-Im Bank)
- Private Export Credit Insurance Companies
- Overseas Private Investment Corporation (OPTIC)
- State/Local Facilitating Organizations

U.S. EX-IM BANK

- Brief History
- Organizational Setup
- Types of Insurance
- Overview of Features
- Short-Term Multi-Buyer Policy in Detail
- Financial Institution Policy in Detail
- Product Development
- Marketing & Promotion
- Underwriting Techniques
- Commercial Risk Management
- Country Risk Management
- Claims & Recoveries
- Support System
- Operating Results

HISTORY OF U.S. EX-IM BANK

- Created in 1934 to foster U.S./Soviet Union trade
- Established under present law in 1945 to support exports, reconstruction of Europe & Asia
- Credit Reform Act of 1990
- Supplement not compete with private capital

- Full Faith and Credit of the U.S.
- Reasonable assurance of repayment
- FCIA * established 1961; Ex-Im Bank assumed operations 1991

EX-IM BANK CURRENT FOCUS

- Support Clinton Administration Strategy for Continuing Export Growth by:
- Emphasizing exports to developing countries
- Aggressively countering trade subsidies of other governments
- Stimulating small business transactions
- Promoting export of environmentally beneficial goods & services
- Expanding project finance capabilities

ORGANIZATIONAL SET-UP OF U.S. EX-IM BANK

- 448 Employees of which 45 in Export Credit Insurance (E.C.I.)
- Board of Directors
- -5 Person appointed by President, with consent of U.S. Senate
- (Chairman, Vice Chairman and 3 additional Board Members)
- -(ex officio) Secretary of Commerce & U.S. Trade Representative
- 10 Departments
- 4 Key Departments report to EVP, including ECI
- Reorganization pending
- Small & New Business
- Working Capital Guarantees
- Insurance
- Business Development
- Structured Export Finance
- Medium & Long Term Loans & Guarantees
- Americas, Asia/Africa, Project Finance, Aircraft & Credit Administration Divisions
- Finance Policy (Country Risk)

* Foreign Credit Insurance Association

- Resource Management

TYPES OF INSURANCE OFFERED BY US EX-IM BANK

- Short-Term Multi-Buyer
- Short-Term Single Buyer
- Bank Letter of Credit
- Financial Institution Buyer Credit
- Medium-Term Single Buyer
- Leasing
- Small Business Environmental
- Umbrella (for Small Business)

U.S.EX-IM BANK INSURANCE FEATURES

- Protect against losses on credit sales
- Policy can be assigned to facilitate financing
- Address needs of exporters and financial institutions
- One buyer or many
- Commercial and political coverage, or political only
- Short-term and medium-term
- Policies for Small Businesses

U.S.EX-IM BANK ECI GENERAL POLICIES

- Restrictions on sales
- No sales for military use
- Only to "Marzist-Leninist" country if President deem to be in National Interest
- Country Limitation Schedule
- Countries where coverage available
 - Open
 - Off-Cover
- Special terms & conditions for coverage

- Public vs Private
- Short Term vs Medium/Long Term
- Bank/Government Guarantees
- Exceptions
- Reasonable Spread of Risk
 - Insure all eligible export credit sales (excluding confirmed L/Cs & Cash in Advance)
 - Political only coverage for sales to subsidiaries/affiliates
- U.S. Content
 - Mandate to support sale/lease of U.S. goods & services
 - ST at least 50% exclusively of U.S. origin
 - Goods shipped from the U.S., no value added after ship

| MT | Foreign Content | Coverage |
|----|-----------------|-------------------------|
| | Up to 15% | All of financed portion |
| | 16-50% | Only U.S. content |
| | More than 50% | No coverage available |

U.S.EX-IM ECI RISK-SHARING

- Exporter Retention
- ST Commercial Risk = 90-95%
- MT Commercial Risk = 90% (of financed portion)
- ST Agricultural Commodities = 98%
- Political Risk = 100%
- Deductible (first dollar loss)
- Not for single sale or small business

• ST MULTI-BUYER POLICY

- Two coverage options
 - "Split coverage" 100% political risk, 90% commercial risk, plus first loss deductible

- "Equalized coverage" 95% of both political & commercial risk, plus first loss deductible
- Documented interest covered
- Eligible Exports
 - Commodities, agricultural commodities
 - Raw materials
 - Consumer durables
 - Spare parts
 - Services (by special endorsement)
- Term
 - up to 180 days
 - agricultural products, fertiliser, consumer durables to 360 days
- Premiums
- Minimum premium in advance of \$500
- Single composite rate for all shipments, determined by
 - Insured's sales profile
 - History of export credit losses
 - Terms of payment
 - Number & type of buyers
 - Countries
- Claim after 180 days default
- Discretionary Credit Limit (DCL)
- Credit Information DCL
- Ledger Experience DCL
- Special Buyer Credit Limits
- Reporting Requirements
- Rescheduling
- Claims
- Recoveries

ECI PROGRAM POLICIES FOR BANKS

- Buyer Credit Policy
- Bank Letter of Credit Policy

BUYER CREDIT POLICY

- Single or Revolving Sales Basis
- Excludes L/C Transactions
- Comprehensive Cover - 90% (political & commercial)
- Political Risks Only Cover
- Policy Period up to 12 Months
- 2 Policy Formats
 - Private Sector: non-documentary
 - Public sector: documentary
- Financial Institution Eligibility
- Allows Banks to Obtain Commercial and Political Risks Cover on Credits Extended
- Directly to Overseas Buyers of U.S. Goods and Services
- Interest Covered

BANK LETTER OF CREDIT POLICY

- Single Transaction or Revolving up to Policy Limit
- Irrevocable L/Cs Only
- Comprehensive Cover Only
 - 100% for sovereign issuers
 - 98% for agricultural products
 - 95% for all others
- Convertibility Currency Denomination
- Policy Period
- Interest
- Subject to Documentation Standards
- Pre-Presentation Agreement Option
- Allows Banks to Expand their Correspondent Bank L/C Relationships

- Eligibility

PRODUCT DEVELOPMENT AT U.S.EX-IM BANK

Responsive to

- Political mandate
- Foreign competition
- Willingness of U.S. Financial Institutions to meet U.S. export financing needs
- New financing techniques
- Address marketing needs, administrative costs

MARKETING & PROMOTION AT U.S. EX-IM BANK

- Brokers
- 95% of sales through Brokers
- Commissions
 - -MT 10% of Premium
 - -ST 8% of Premium
 - -Small Business Multi-Buyer 40% of Premium
 - -Single Buyer 10% of Premium
- Ex-Im Bank Offices
 - -New York, Chicago, Miami, Houston, Long Beach
 - -Staff: 3-5

UNDERWRITING TECHNIQUES: COMMERCIAL RISK

- Exporter's Experience with Buyer
- Ex-Im Bank's Experience with Exporter
- Credit Reports
 - -One for up to \$100,00
 - -Two for up to \$250,000
- Financial Statements
 - -Unaudited F/S \$250,000 to under \$1 million

- -Audited F/S \$1 million and up
- Decision Making
 - -Loan Committee for MT, Board for large or policy issues
 - -ST in Insurance Div.

UNDERWRITING TECHNIQUES: POLITICAL RISK

- Country Risk Division of Financial Policy
- Country Risk Ratings for all US GOVERNMENT Programs to determine subsidy
- Methodology
- Committee
- Quantitative & Qualitative
- Relate to Credit Ratings for Major Credit Rating Agencies

CLAIMS & RECOVERIES

- Claims Division processes claims/recoveries for all Ex-Im programs
- Few claims since debt crisis in developing countries
- Rejected claims due to non-declaration of shipment and non-payment of premium

U.S.ECI SUPPORT SYSTEM

- Brokers
- Ex-Im Bank Regional Offices
- Commercial Banks
- Umbrella Policy Administrators
- Associations
- Coalition for Employment for Exporters (CEE)
- Small Business Exporters Association (SBEA)
- Bankers Association for Foreign Trade (BAFT)
- Export Assistance Centers (EACs)
- State/City Program

U.S.EX-IM BANK OPERATING RESULTS

- Supported 1.5% of U.S. Exports (1996)
- Exposure US\$55.8 billion (without ST ECI)
- Statutory limitation US\$75 billion

| | | |
|----------------|-------------------|------------------------|
| Authorizations | -FY1996 | (of which ECI) |
| -Number | 2,422 | (1,1914) |
| -Amount | US\$11,518bn | (US\$3,868bn) |
| -Export Value | US\$14,597bn | (US\$3,997bn) |
| -Subsidy | US\$894mm | (US\$148mm) |
| Profit (Loss) | US\$1,241mn(1996) | (US\$1,318mm) (FY1995) |

ECI UNDERWRITING RESULTS

| | FY94 | FY95 | FY96 |
|---------------------------|--------|---------|---------|
| ■ Authorizations(US\$m) | 4,273 | 4,555 | 3,868 |
| -Small Business | 37% | 37% | 37% |
| ■ Policies Authorized (#) | 1,576 | 1,961 | 1,895 |
| -Short Term | 1,369 | 1,676 | 1,566 |
| -Medium Term | 107 | 285 | 329 |
| Underwriting Activity(#) | 7,428 | 7,864 | 7,090 |
| -Short Term | 7,067 | 6,999 | 6,251 |
| -Medium Term | 361 | 865 | 839 |
| -Average Processing | 8 days | 9 days | 14 days |
| Export Underwriting | 1,561 | 1,594 | 1,684 |
| -Average Processing | 9 days | 10 days | 8 days |

ECI OPERATING RESULTS

| | FY94 | FY95 | FY96 |
|--------------------------|----------|-------|-------|
| ■ Shipments Covered (mn) | 2,773 | 2,432 | 2,300 |
| -ST Exporter | 1,808 | 1,748 | 1,770 |
| -ST Bank | 774 | 476 | 231 |
| -Medium Term | 919 | 209 | 299 |
| Geographic Region | (FY1996) | % | |
| -Latin America | 1,181 | 51 | |
| -Europe & Canada | 520 | 23 | |
| -Asia | 472 | 20 | |
| -Africa & Middle East | 127 | 6 | |

- Top 3 Markets: Mexico, Brazil & Canada = 38%
- Top 10 Markets = 60%

U.S.PRIVATE SECTOR ECI

- Private Sector Insurers
- American Credit Indemnity (AIC) - Euler Group
- Maryland Netherlands Credit Insurance (NCM)
- AIG Global Trade & Political Risk Insurance (AIG)
- CNA Credit
- FCIA Management Co. (FCIA)
- Exporters Insurance
- U.S. Ex-Im Bank
- 2nd in premium, 6th or 7th in income
- Large Reinsurance Capacity
- Characteristics
- Lower premium rates than U.S. Ex-Im
- More flexibility in products covered
- Limited term (maximum 3 years generally)
- Non-U.S. presence
- Serve large company market

OPIC INVESTMENT INSURANCE

- Programs
 - -Investment Insurance
 - -Loans and Financial Guarantees (all risk)
 - -Investment Fund Guarantees
 - -Contractor Bid, Performance, and Advance Payment Guarantees
 - -Contractual Disputes Coverage (with public sector buyers)
 - -Assets and Business Income Cover
 - -Customs Bond Coverage
- Underlying Bi-Lateral Agreements
- OECD Countries Ineligible
- Political Risks Only
- Currency Inconvertibility
- Expropriation
- Political Violence

Rules of the Game: A Summary

- Applicant/Recipient must be:
- 51% voting share ownership in the private sector
- U.S. owned or controlled investor or lender

Projects must be:

- Registered before investment made or irrevocably committed
- Developmental
- New, or for expansion/modernization
- In approved countries
- Able to show positive effects on U.S. economy

Projects must not:

- Result in negative effect on U.S. employment and loss of U.S. jobs
- Result in negative impact on U.S. trade
- Adversely affect the environment

- Contribute to violation of internationally recognized workers rights

Extent of Coverage

- Maximum term of 20 years
- Maximum 90% coverage
- Maximum of 270% of initial investment
- Applicant can choose:
 - -All political risks covered, or selected risks to be covered
- OPIC cover backed by
 - -Reserves of over \$2.4 billion
 - -Full faith and credit of the U.S. government

STATE/CITY PROGRAM

- Joint effort of Ex-Im Bank & State/City offices
- 33 state and local government offices & private sector

Objectives:

- Support SME companies in exporting
- Lower cost to market
- Create Jobs - expand local tax base
- Programs: Working Capital Guarantee & ECI
- Delegated Authority to commit ST insurance
- Ex-Im Bank trains staffs

Chapter II

Trade and Investment Insurance System of Canada

Export Development Corporation (E.D.C.)

EDC HISTORY & OVERVIEW

What is EDC?

- Canada's official ECA
- Financially self-sustaining Crown corporation that operates on commercial principles

EDC Mandate

- EDC offers a range of financial and risk management services, including export credit insurance, sales financing and guarantees.

History of EDC

- 1944 Export Credits Insurance Act established Canada's first export credit agency - Export Credits Insurance Corporation (ECIC)
- 1946 joined Berne Union (remains member to date)
- 1960 Act amended to provide long-term financing for sales of capital goods
- 1969 Act changed to Export Development Act
- 1972 began to conduct Treasury operations and by 1976 ceased to borrow from Government
- 1993 Ed Act modified to extend powers to allow
 - domestic insurance
 - equity
 - working capital guarantees

EDC Today

Commercial Orientation

- self-sustaining (not reliant on Parliamentary appropriations)
- assess risk according to commercial principles (no subsidies or grants)
- operate on a user-pay basis
 - premiums and fees for insurance
 - all loans fully repayable with interest

- generates profit

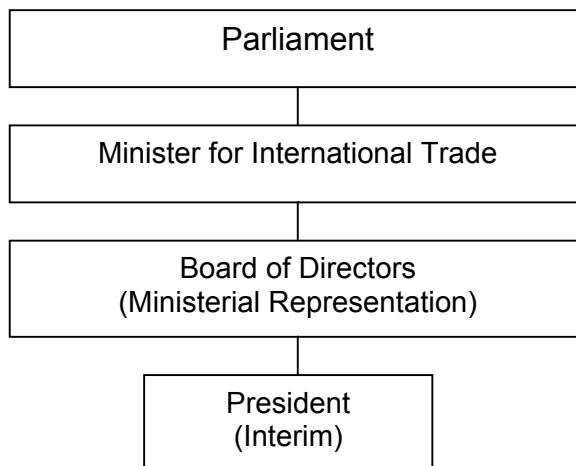
Multiservice ECA

- Most official ECA's act solely as insurers/guarantors for their national government's account
- EDC is a multi-service ECS offering both insurer/guarantor and direct lending services under one roof

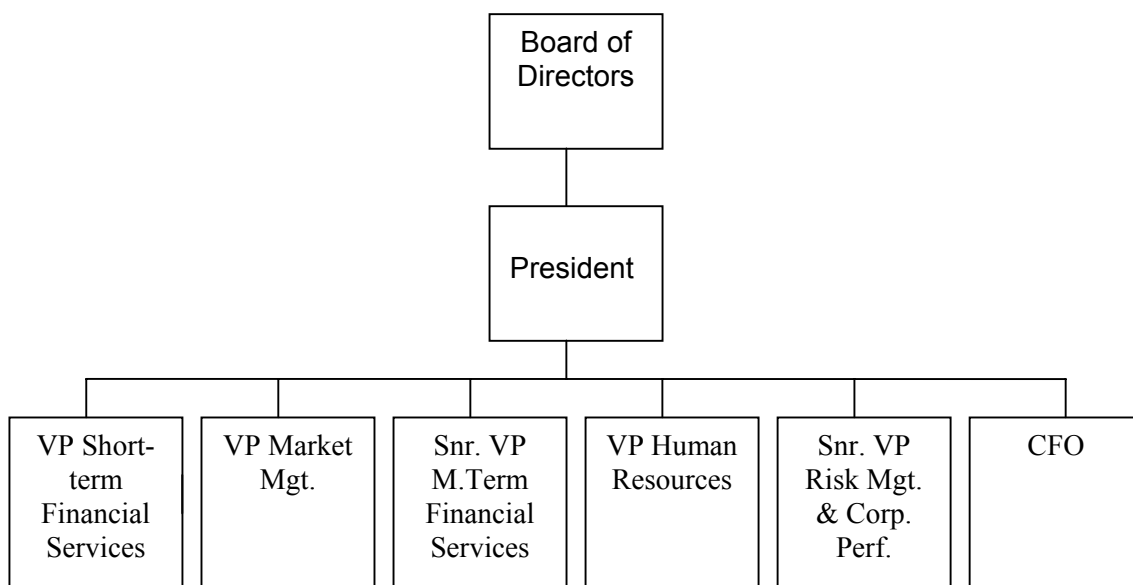
International ECA Competition

| | Canada | U.S. | Japan | Germany | U.K. | France | Italy | Italy |
|--------------------------|------------------------------|--------------|---------------|----------------------------|-----------------------------|---------------|----------------------------|---------------|
| Official ECA | EDC | EXIM | EID/MIT | HERMES | ECGD | COFACE | COFAC | SACE |
| Other Gov't Institutions | | OPIC CCC | JENM | KFW C&L | CDC | | E | Medio-credito |
| Eca Programs | | | I | | | | | |
| Lending | √ | √ | x | √ | x | x | x | X |
| Credit Insur. | √ | √ | √ | x | √ | x | √ | √ |
| FII | √ | x | √ | x | x | √ | √ | √ |
| Guarantees | √ | √ | √ | x | √ | √ | √ | √ |
| Relation to Gov't | Crowa Corp. | Gov't Agency | Gov't Depart. | Gov't Bank | Private -on behalf of Gov't | Gov't Depart. | Private-on behalf of Gov't | Gov't Agency |
| Source of Capital | In house Treasury Operations | Gov't Budget | Gov't Account | Borrows in Capital Markets | Gov't Account | Gov't Account | Gov't Account | Gov't Account |
| Commercial Orientation | √ | x | x | √ | x | x | x | x |
| Cashflow US\$m-1995 | 156.22 | -145.20 | 574.77 | 0.21 | 34.9 | 337.70 | -139.90 | - |
| Cashflow US\$m-1996 | 273.76 | -105.60 | 674.55 | 0.80 | 583.30 | 583.87 | 832.40 | -508.74 |

Corporate Reporting Structure



Organizational Structure

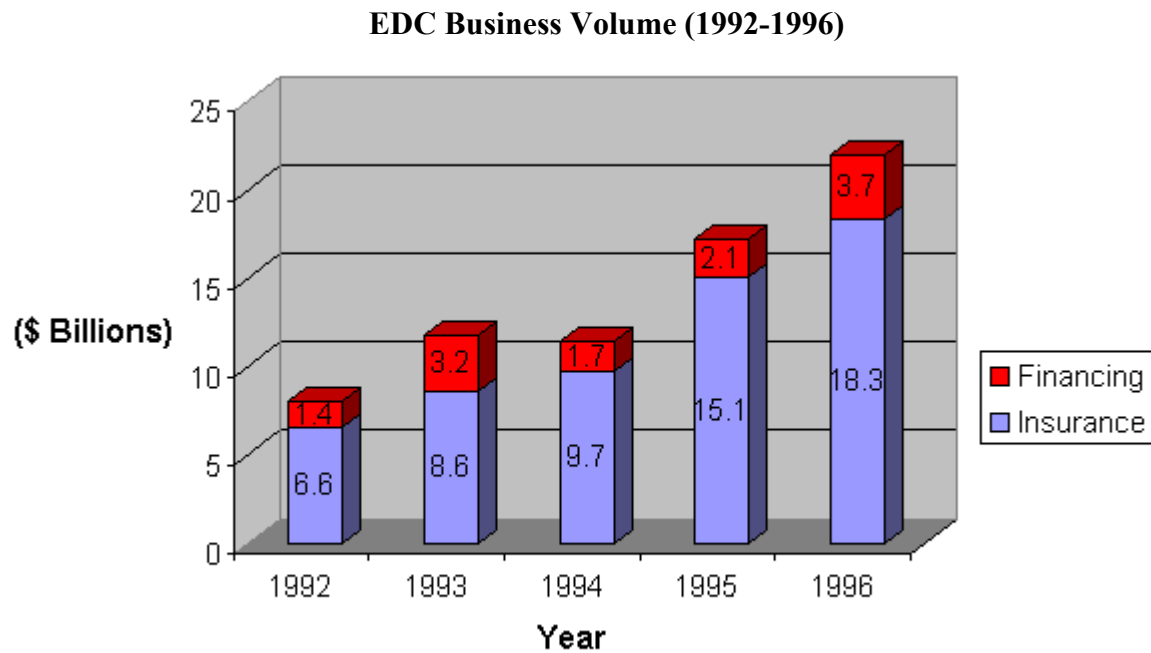


Corporate vs. Canada Account

- Sect 10 (Corp.) vs. Sect 23 (Can.) of Export Development Act
- EDC as Canada Account agent for the Government (paid an admin. fee)
- Cabinet Authority (>\$50mn) vs Ministerial Approval

Track Record

- Exports: EDC has supported more than \$100 billion since the start of 1996 (6% of Canada's total export volume)
- Every region of the globe (137 countries in 1996)
- Every region of Canada
- Every sector of the Economy

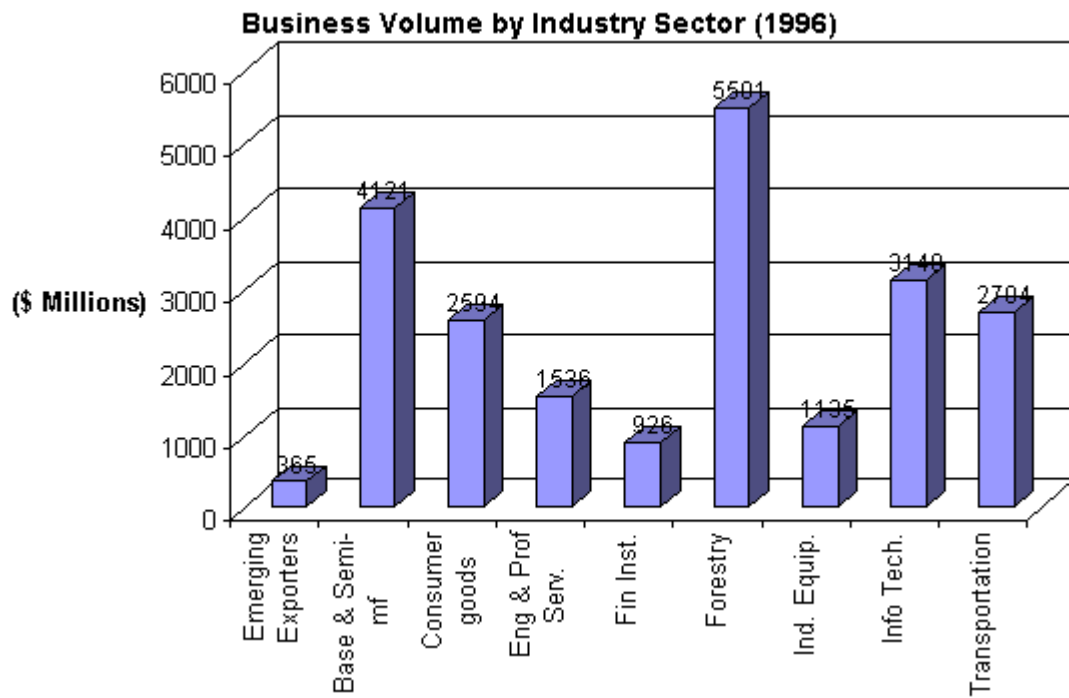


Where We Do Our Business

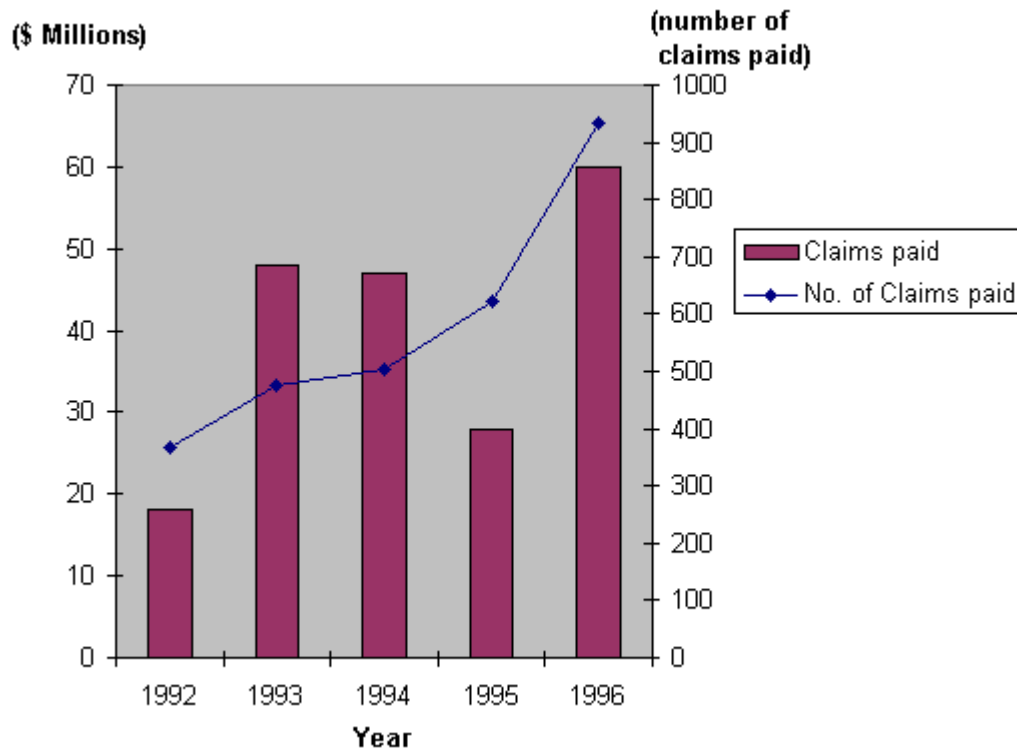
(Diagram EDC Volume by Geographic Market (1996))

(Diagram EDC Volume as % of Cdn. Export (1995))

Business Volume by Industry Sector (1996)

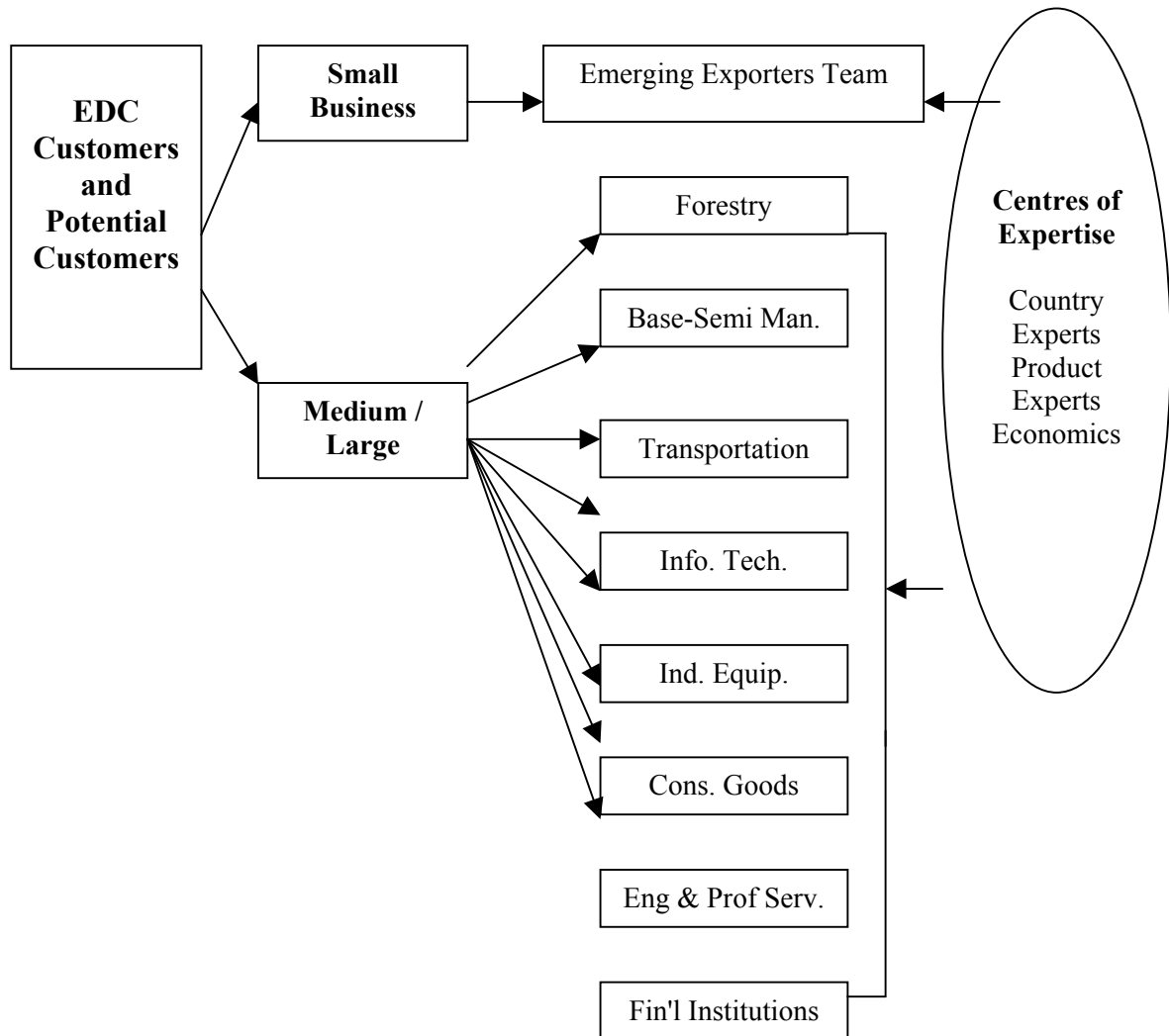


Claims Paid



EDC's New Structure

Customer Focused Teams



EDC - Overview of Financial Services

Financial Services

(1996 - \$Billions)

- Credit Insurance \$15.8
- Financing \$3.7
- Foreign Investment Insurance \$1.5
- Performance Security \$1.0

Coverage for Letters of Guarantee

- 90% coverage to the exporter for:
 - Wrongful call of a letter of guarantee; and
 - Rightful call outside exporter's control
- 100% coverage to the bank for:
 - Any call of a letter of guarantee
 - EDC requires recourse to the exporter
- Used to free up working capital funds

Coverage for Surety Bonds

- Surety Bond Insurance
 - Up to 85% coverage to surety company against exporter's non-performance
 - Proof of default required before payment, hence reduces risk for exporter
 - Typical in North America
 - Flexibility for non-traditional industries and markets
- EDC Surety Bonds
 - Applicable where current programs do not suit transaction
 - Primarily with sovereign buyers

Foreign Investment Insurance

| 90% coverage against political risks | Period of coverage: | Types of investment & coverage: |
|---|----------------------------|--|
| Expropriation | Up to 15 years | Equity: Capital & retained earnings |
| Transfer of funds | | Loan: Principal & interest |
| War, Revolution, Insurrection | | |

Financing Eligibility Criteria

- Exporter
 - Business operating in Canada
 - Technically & Financially capable of completing transactions
 - Benefits to Canada requires 50% Canadian content minimum - If less than 50%, will look into other factors, such as if create more jobs, etc.
- Buyer/Borrower
 - Creditworthy
 - Acceptable country
 - No Iraq, Libya
- Project
 - Technical & commercial viability

Financing Services

Types of Services:

- Direct Buyer Loans
- Lines of Credit
- Note Purchase

Direct Buyer Loans

- Tailored to commercial contract
- EDC disburses funds on behalf of the borrower
- Meets the credit needs of foreign buyers
- Competitive interest rates & fees

Lines of Credit

- EDC pre-negotiated terms with foreign institution
- We disburse funds on behalf of the borrower
- Fast turnaround
- Over 40 lines around the world
- Ideal for small to medium-sized transactions

Note Purchase

- We buy promissory notes issued by the buyer
- Available for sales in commercial markets
- For small to medium-sized supplier credit transactions

Emerging Exporter Team

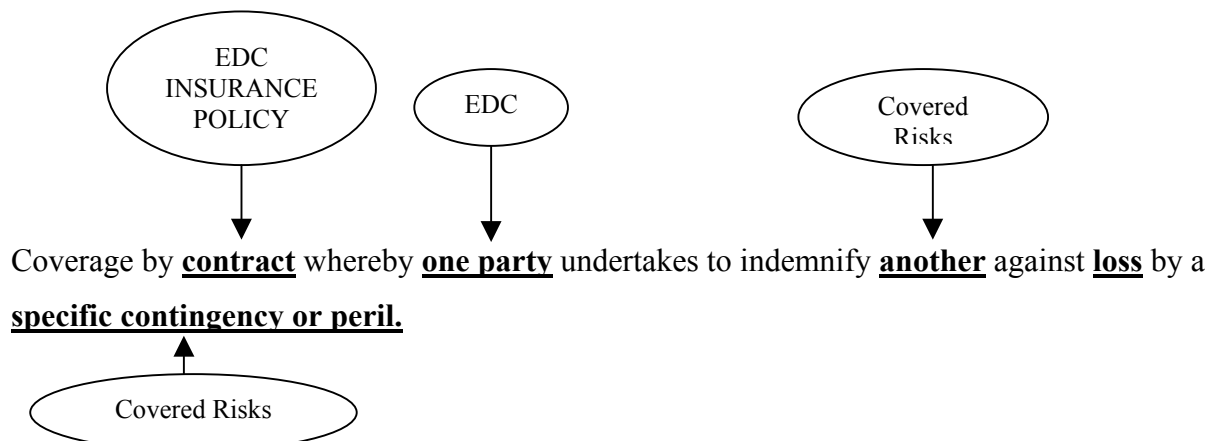
- SME Need
 - ✓ Responds to need for quick turnaround, standardised product and account management
- EDC Role
 - ✓ Provide a centralized, automatic and rapid client service
- Benefits
 - ✓ Higher customer satisfaction
 - ✓ Dedicated attention to the client base
 - ✓ Targeted marketing
 - ✓ Lower overhead
- Status
 - ✓ Launched March 27, 1995

Responding to Customer Concerns

- More than 62% of credit approvals done within 24 hrs
- Short-term policies for SME's issued over the phone
- Toll-free number to reach underwriters directly

Short-Term Insurance

What is Insurance & Who are the Parties?



What is Short-Term Insurance?

Short-term insurance covers exporters against non-payment of their short-term export receivables through the issuance of whole turnover credit insurance policies

- Covers all (most) credit sales - allows some selections if exporters have reasonable spread of buyers
- Standard cover rate 90%
- 1 or 2-year term (1-2 years policy /duration of policy)
- pay-as-you-go - non-refundable
 - monthly declaration or quarterly, pay at time of declaration - be flexible

Short-Term Insurance Policies

- Comprehensive Insurance
 - -Global Comprehensive Insurance Policy (or Export Credits Insurance Policy for smaller exporter) - 90-95% of EDC business
 - -Shipments or Contracts - EXPR can choose either one
 - -Services
- Political Risk Only Insurance
 - -Global or Selective
- Documentary Credits Insurance

What Losses do we Protect Against?

The majority of EDC's policies protect our clients against losses that can occur when they extend credit to their buyers.

- Insurance is purchased to protect against a loss resulting from an event occurring at a future date, which is unforeseen, unexpected and beyond the insured's control
- We generally cover 90% of the loss incurred
- By indemnify we mean that we put the exporter back in the same position as he was before the loss. The insured can not be put back into a better position after the loss

Risks Covered - Credit Insurance

Commercial Risks

Buyer insolvency

Default (non-payment)

Repudiation of goods by buyer (non-acceptance)

Contract cancellation by buyer

Political Risks

Conversion & transfer difficulties

War & related disturbances

Cancellation of import/export permit

Moratorium on country's external debt

What Must the Insured do to be Protected?

- **In order to be protected our clients must have:**
 - an insurable interest (either a contract or a receivable)
 - complied with the terms & conditions of their policy (including paying premium)
 - acted in good faith

Why Credit Insurance?

- risk management
- cost effective provisioning
- bank financing
 - credit quality enhancement
- competition
 - level the playing field
 - competitive advantage

Underwriting - Premium Rates

- Basic Premium Rates
 - Based on Matrix which takes into account
 - Commodity Classification
 - Country Risk
 - Terms of Payment
 - Volume

- Other Underwriting Factors
 - Spread of Commercial/Political Risk
 - Severity of Risk - Individual Credit Limits
 - Historical Incidence of Loss - Industry and Exporter
 - Exporter Risk

- Contracts Policies - Pre-Shipment Cover Rates
 - Length of Pre-Shipment Period
 - Salvage Value

Underwriting - Other Issues

- Discretionary Limits
- Use of Deductibles
 - First Loss Deductible
 - Per Buyer Deductible
 - Non-Qualifying Losses
- Setting the Maximum Liability

Sources of Credit & Financial Information

Traditional

- credit agency report
- specific industry agency report
- bank report
- trade references
- SEC (10Q & 10K)
- annual reports
- investment brokers

Not so Traditional

- Investment Brokers, Vulture Funds
- Bond & Credit Rating Agencies (e.g.S&P, Moody's, DBRS)
- Electronic Media (e.g.Bloomberg, Lexis Nexis,Reuters)

- Financial databases on CD-ROM (e.g. Amadeus - Europe, FAME - UK, PC-Plus - USA/Canada, DIANE - France, JADE -Japan, Worldscope - Europe, Moody's USA & Int'l)
- Industry specialists and trade supplier group associations
- Country specialists

Product Development, Promotion and Marketing

Product Development

Products vs Solutions

- EDC transition from a product-driven company to a solution-driven company
- Multiplicity of products = confusion?

Flexibility with Existing Product Range - Examples

- Coverage of domestic and international sales
- Large buyers only policy
- Multi-country policy

Separate Products vs Separate Delivery Example of SME's

- EDC's Research on SME's concluded:
 - No patience for "red tape"
 - High priority on fast service
 - Lower priority on individualized underwriter relationship

Product Differences

- Claim waiting period in case of default (4 vs 6 months)

Delivery and Administration Differences

- One underwriting team (not industry sector specific)
- Underwriting Team vs individual underwriter
- Product delivery over the phone (1-800 numbers)

- Coast-to-coast coverage during business hours
- No monthly declaration if no insured sales

Recent New "Products"

- Master Accounts Receivable Guarantee (MARG) --for small exporters, provides BANKS with guarantee on loans against receivables
- Grow Export Program--joint working capital guarantee program with Canadian Imperial Bank of Commerce for small high-tech companies
- Northstar Trade Finance--short-term policy tailored to cover medium-term credits (up to 5 years)
- Medium-Term Documentary Credits Policy--broadened short-term DC policy to cover medium-term LC's (up to 5 years)
- Bank Aval Policy--policy in development to cover Canadian banks on foreign bank avals rather than Letters of Credit

Promotion and Marketing

Selling Features of Credit Insurance

- Asset protection
- Enhanced access to bank operating lines
- Increased sales
 - Alternative to more secure terms (ILC or payment in advance)
 - Longer terms
 - Increasing buyer limit
 - New market penetration

Direct Selling vs Selling Through Brokers

- Cost effectiveness
- Product understanding
- Relationship with customers
- Access to certain (larger)potential customers

EDC Marketing Force

- 8 offices across Canada
- Approximately 30 Business Development Managers

Promotional Tools

- Sales Collaterals (Brochures)
- Advertising
- Direct Mailing
- Workshops
- Word of Mouth

Commercial Risk Management

Short-Term Commercial Risk

Commercial risk is defined as non-payment (financial distress or unwillingness to pay) by a buyer of its obligation to a company supported through EDC's short-term credit insurance program.

Emphasis:

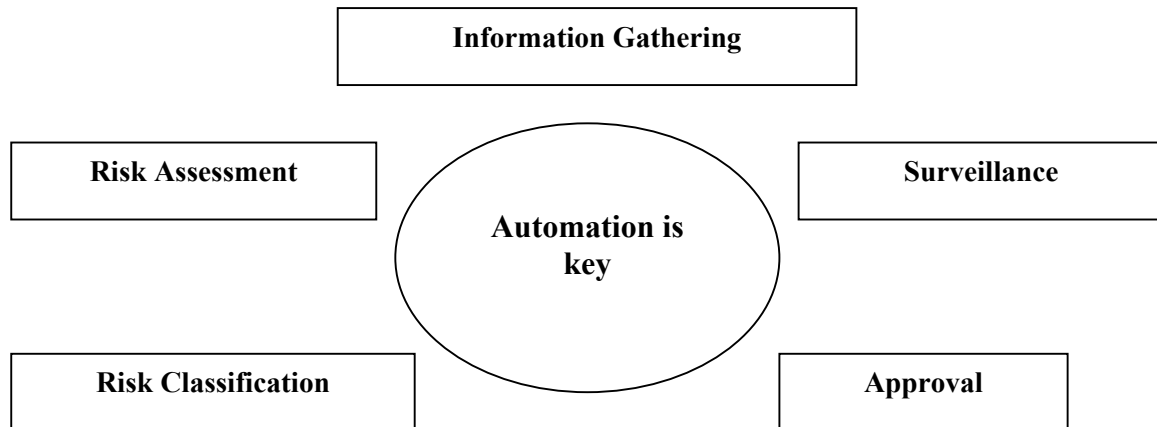
Maximizing automation

- Decision models & limits
- Automatic surveillance & support
- Mainframe-to-mainframe

Management Unit - Organization

- Credit Surveillance and Analysis Department - reports to V.P., Short-Term Financial Services
- Services all Short-Term Insurance Business Teams
- Staff of 40
 - Buyer High Risk Unit (17)
 - Automated Credit Facilities Unit (6)
 - Client Credit Processing/General Admin./Buyer Low Risk (15)
 - Director of Credit and Assistant (2)

Commercial Risk Management - Approval Process

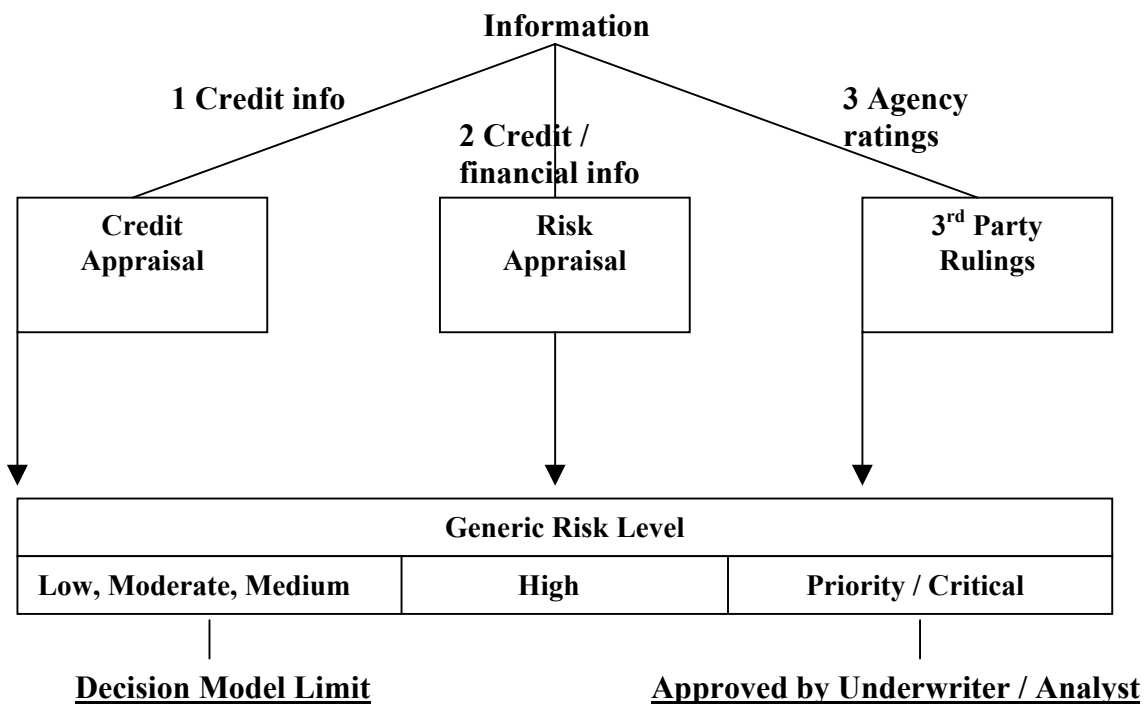


Approval Process - Information

Means of data collection

- Mainframe-to-mainframe links
- On-line access to news services
- Credit & Financial databases on CD-ROM
- Credit agency reports via fax
- EDC Client/Buyer

EDC Risk Assessment



Credit Appraisal Focus & Model

- Years in business
- Business Reputation
- Management Quality
- Banking Experience
- Trade & Payment Data
- Third Party Credit/Financial Ratings
- Credit Appraisal

Plus

- Financial Appraisal Focus/Ratios
 - Liquidity
 - Leverage
 - Coverage
 - Operating
 - Financial Condition

Rating (Third Party) Models

Agencies who assess the credit & financial health of a company to perform as a going concern.

Examples:

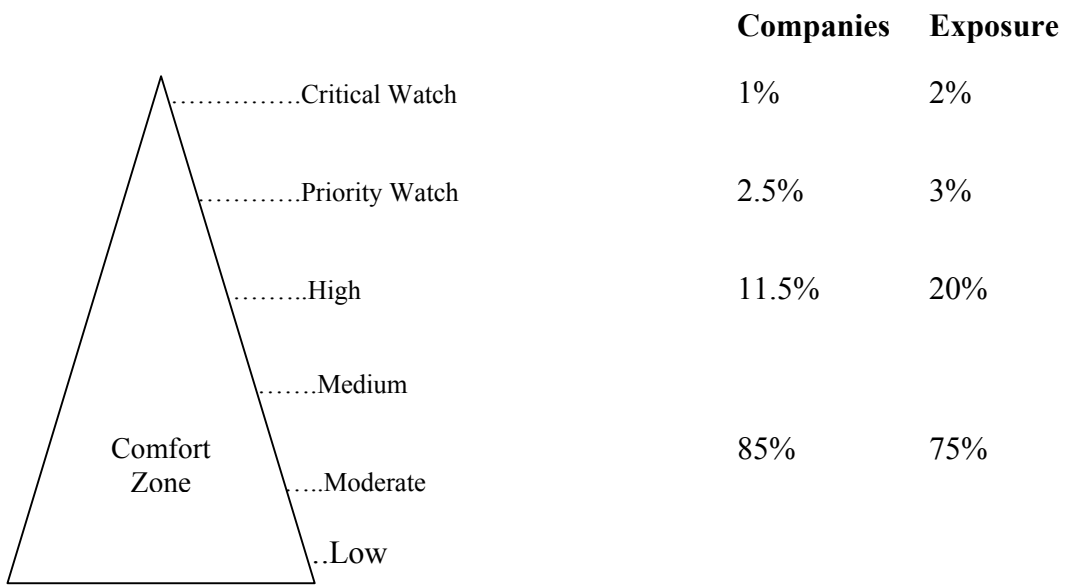
Bond Rating Agencies:

- Moody's Investors Service Inc.
- Standard & Poor's Corporation

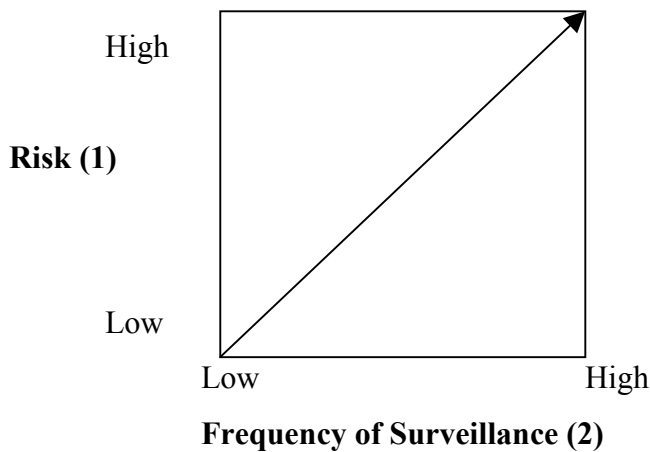
Credit Rating Agencies:

- Dun & Bradstreet (Int'l)
- Lumbermens (USA)
- Japanese Credit Agency (Japan)
- Novcredit (Italy)

Portfolio Risk Level



Automated Surveillance Matrix & Workflow Management



- (1) Influenced by exposure, industry sector and country risk
- (2) Reflects type & frequency of surveillance as well as level of effort and expense

Surveillance Risk Focus

| | Companies | Exposure |
|---|------------------|-----------------|
| Tier 1 <i>Higher Risk</i> Intense Effort | 5% | 10% |
| Tier 2 <i>Large Exposures</i> Moderate Effort | 10% | 70% |
| Tier 3 <i>Comfortable Risk</i> Low Effort | 85% | 20% |

Higher Risks Require:

- Detailed financial analysis
- Industry risk considerations
- Country risk considerations

Through:

- Company visits
- Electronic news media
- EDC's automated risk assessment tools
- Credit and trade groups
- Industry specialists
- Country specialists

Problem Accounts Require

- Fast experienced attention
- In-depth financial analysis
- Visits
- Negotiations

- Credit considerations on future supply
- Third party discussions
 - Trade suppliers
 - Banks/Insurers/Factors
 - Landlords

Buyer High Risk Unit Supports Business Teams

- Dedicated portfolio managers
 - Commercial high risk expertise
 - Industry high risk expertise
 - Country high risk expertise
- Provides risk assessment & acceptance support on additional high risk exposure
- Handles problem accounts - working out rescheduling & credit needs
- Monitors high risk/large dollar exposures

Automated Credit Facilities Unit

- Establishes credit & surveillance standards
- Enhances decision models and provides validation (discriminate analysis, etc.)
- Group risk management
- Reports on Short-Term Insurance operational performance
- Controls automated appraisals & model limits

Benefits to Automated Commercial Risk Management

Since 1990:

- Credit application response time
 - (2 days vs. 12 days)
 - 65% processed within 24 hours vs. 20%
- Consistency
 - The rate of approvals on initial requests for credit increased by 22%
 - The rate of revolving approvals (vs. specific) on initial requests for credit improved by 8%
- Greater business volume

-As at July 31, 1997, insured volume is expected to exceed \$20 b vs. \$3.3 b in 1990.

- Greater risk appetite
 - Decision models accommodate the majority of comfortable risks thus allowing more time to address higher risk credits
- Improved net commercial claims
 - Significant improvement to gross and net claims since the introduction of automation

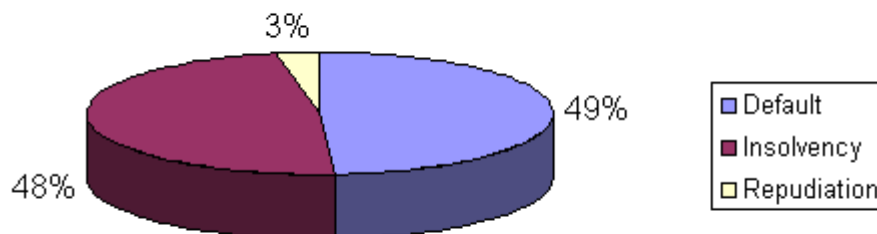
Claims & Recoveries at EDC

Presentation Overview

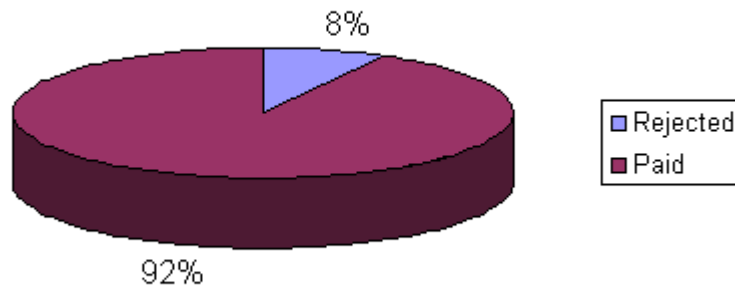
- Scope of claims work
- Mandate & Structure
- Loss Mitigation
- Claim Review & Payment
- Recovery

Claims by Risks Incurred

As a percentage of all commercial risks



Claims Rejected



Organizational Structure of CARD

- Department reports to Vice President and Controller of Finance
- Ten Claim Services Managers (CSM) reporting to a Team Leader
- CSM responsible for claim processing AND debt recovery
- CSM aligned to Business Teams

Mandate of Claims Department

- Loss Mitigation - assisting clients
- Payment of all reasonable claims quickly
- Recovery of indemnities paid

Loss Mitigation

- Clients must report overdues to EDC at 90 days OD (Global Comp policies)
- EDC will assist clients prior to Admissibility - Without Prejudice basis
- Failure to mitigate Loss could result in denial of liability by EDC (Exclusion under the policy)

Claim Submission by Client

- Completion of Declaration of Loss on one page Claim Payment Application form.
- Application form combined with detailed instructions for each data field
- Documentation is to be attached

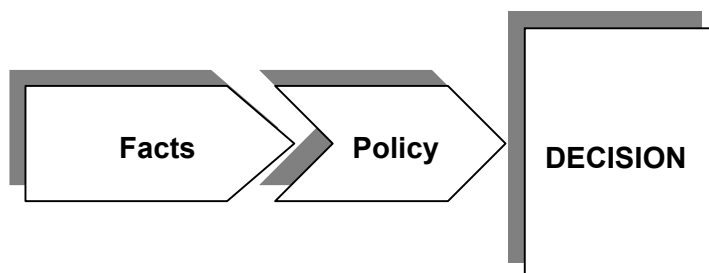
- Upon receipt at EDC, claim submission entered on database; all claim processing is done on- line
- Data links to upstream systems for control & validation

Claim Review – Documentation

| <u>Customer Supplied</u> | <u>EDC Supplied</u> |
|---|--|
| <ul style="list-style-type: none"> ▪ Proof of Debt ▪ Credit Requirements ▪ Other | <ul style="list-style-type: none"> ▪ Policy Coverage ▪ Credit Approval (if applicable) |

Claim Review - Interpretation

- Linkage of underwriting intent with the facts of a loss
- Policy, endorsements, EDC credit approvals reviewed
- EDC relies on that which can be demonstrated



Calculating the Loss

- Calculation of Loss can vary with risk
- Limitations on insured Loss does occur
- Consistency in underwriting practice very important

| <u>Sample Calculation</u> | |
|--------------------------------|--------------|
| Invoice total | \$1,000 |
| Overshipment | <u>250</u> |
| | Net loss |
| Admissible | 750 |
| Deductible | <u>100</u> |
| Shared Loss | 650 |
| <u>EDC@90%</u> | <u>\$580</u> |

Recovery of Indemnities

- Policy requires customer to take all reasonable measures
- Working with EDC, customer should have recovery under way prior to admissibility of loss
- Cost-Effectiveness is the Key

- All costs shared "pro rate" after approval by EDC
- Recoveries shared "pro rate" with the insured loss being in priority to non-insured loss

Tools of Recovery

- Standard (Commercial) risks:
 - Under \$1,000,000 - to a collection agency
 - Over \$1,000,000 - legal action
- EDC takes assignments of all debts under \$50,000 & directs to an agency
- Direct involvement by EDC when viewed as "value added"
- All actions must be approved by EDC

Summary

- Strong support of customers, even before admissibility judged
- Customer is serviced by one CSM to promote industry knowledge and customer specific knowledge
- All claim decisions are fact-based
- Recovery decisions are always based in cost-effectiveness
- Customer Satisfaction Index for claim service is high

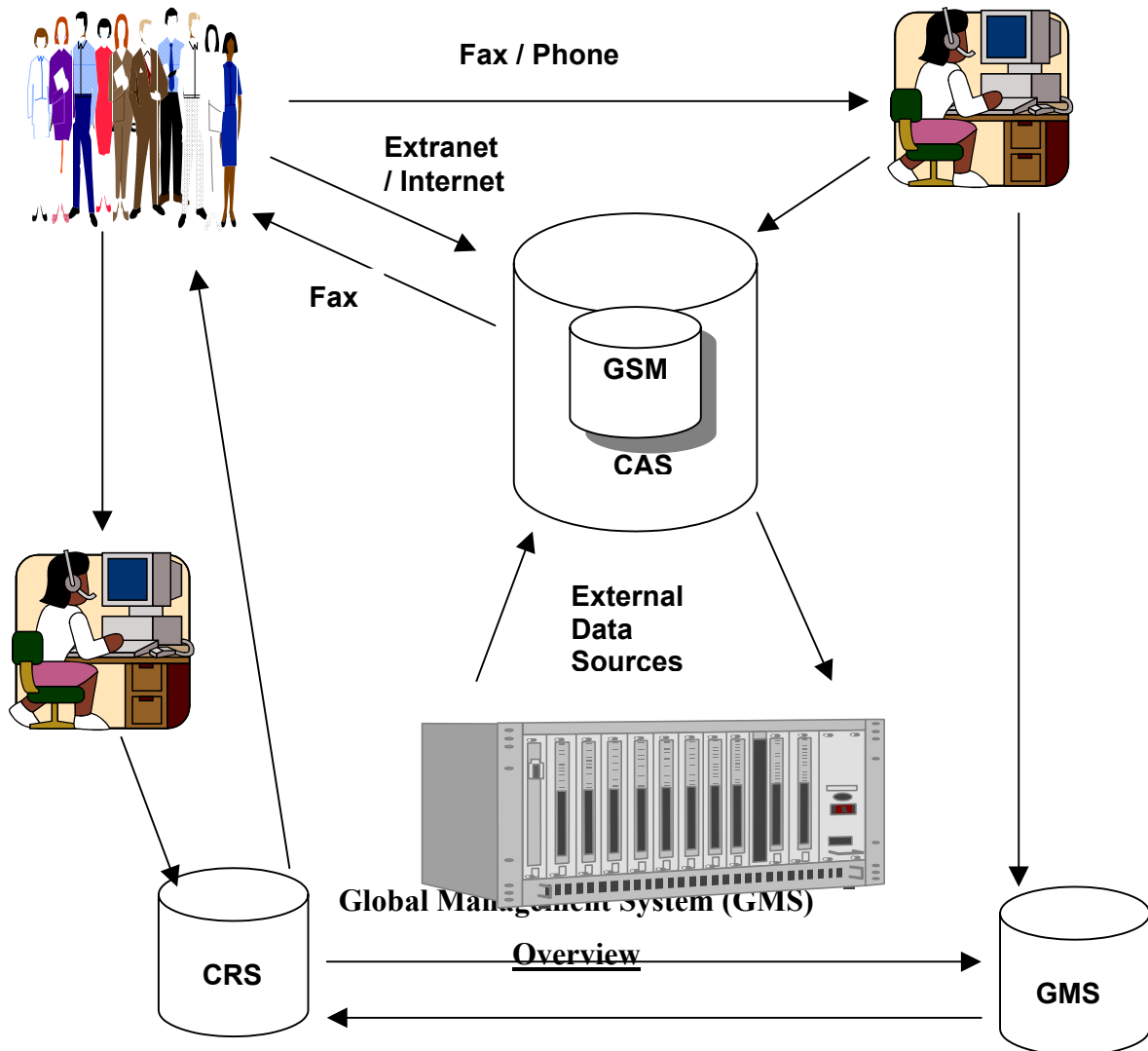
Credits Insurance Support Systems

Overview

EDC uses several key systems to support the delivery and management of Credits Insurance.

- The Global Management System (GMS) is used to underwrite and administer Credits Insurance.
- The Credit Administration System (CAS), with the integrated Decision Support Model (DSM) is used to manage EDC's short-term credit portfolio.
- EDC Direct provides customers with a PC-based interface to CAS.
- The Claims & Recoveries System (CRS) is used to process claims and recoveries.

Used in concert, these systems enable EDC to serve its customers with greater efficiency and effectiveness



The Global Management System (GMS) was originally introduced in 1984 with a view to meet the following business objectives:

- Provide an integrated support system to deliver and manage Credits Insurance.
- Support the Credits Insurance workflow in an efficient and effective manner.
- Standardize the rate calculation process used to underwrite Credits Insurance.
- Enhance customer services using automated facilities.
- Provide timely billings to customers.
- Provide consistent and reliable data to meet the reporting needs of the Corporation.
- Provide underwriters with user-friendly access to policy information.

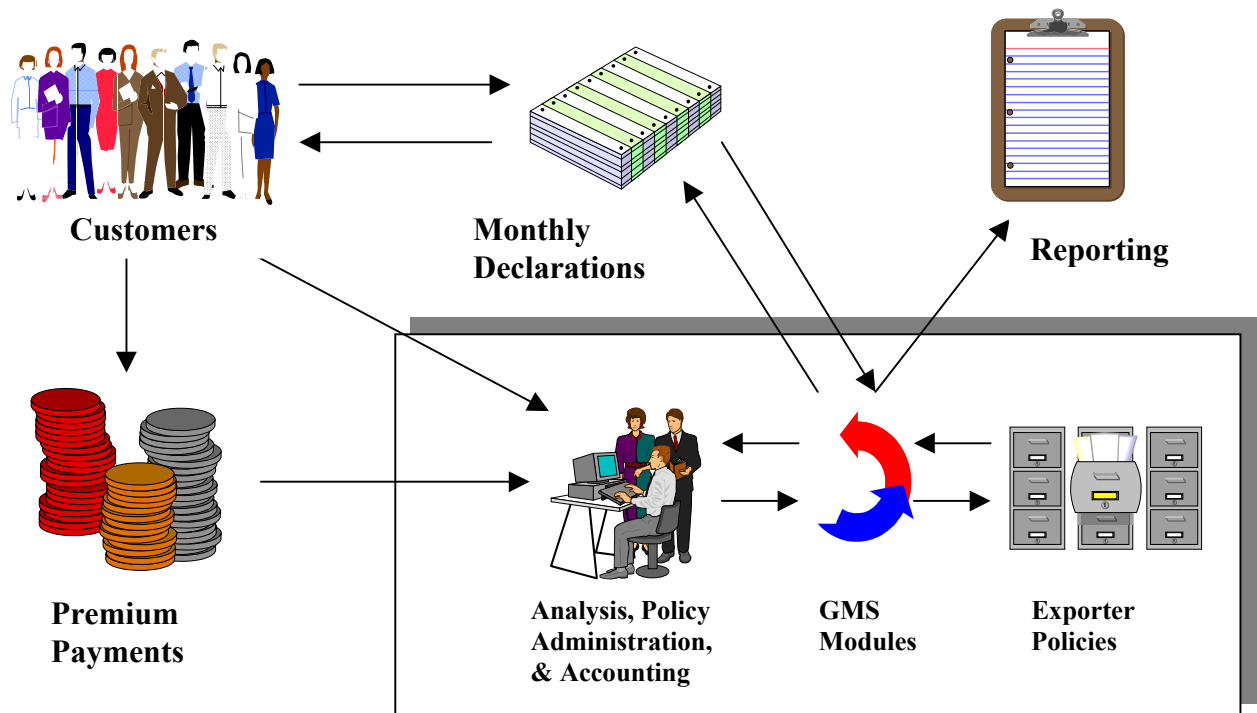
GMS has successfully been applied to manage EDC's growing business

Diagram :”Volume of Credits Insurance supported”

Diagram: Premiums Collected

Diagram: Active Declaring Policies

Today GMS is used to manage all aspects of Credits Insurance including the following:



Credit Administration System (CAS)

Overview

Credit Administration System

Background

- Award winning Mainframe application developed by EDC
- Designed to help STFS analyze and administer EDC's short-term credit portfolio
- First implemented in 1990 as an electronic credit & financial database
- Addition of EDC's Decision Support Model (DSM) in 1992

Credit Administration System

Key Features

- Stores up-to-date credit and financial information on companies that have exposure with EDC
- Direct data transfer of credit and financial information from external sources
- Records all credit decisions
- Keeps track of EDC's exposure
- Enables policy holders to interface with the system using EDC Direct
- Automatically generates letters to inform clients about credit decisions
- Performs credit, trend, and risk analysis
- Generates credit decisions for companies with low, moderate, and medium risk
- Produces risk levels and sets global limits for companies that are stored in the database
- Records and tracks outstanding and overdue payments between exporters and their customers

Volume and Turnaround Time

(diagram Volume and Turnaround Time)

Credit Activity

(diagram Credit Activity)

Policyholder Credit Requests

(diagram Policyholder Credit Requests)

Extranet Using EDC Direct Overview

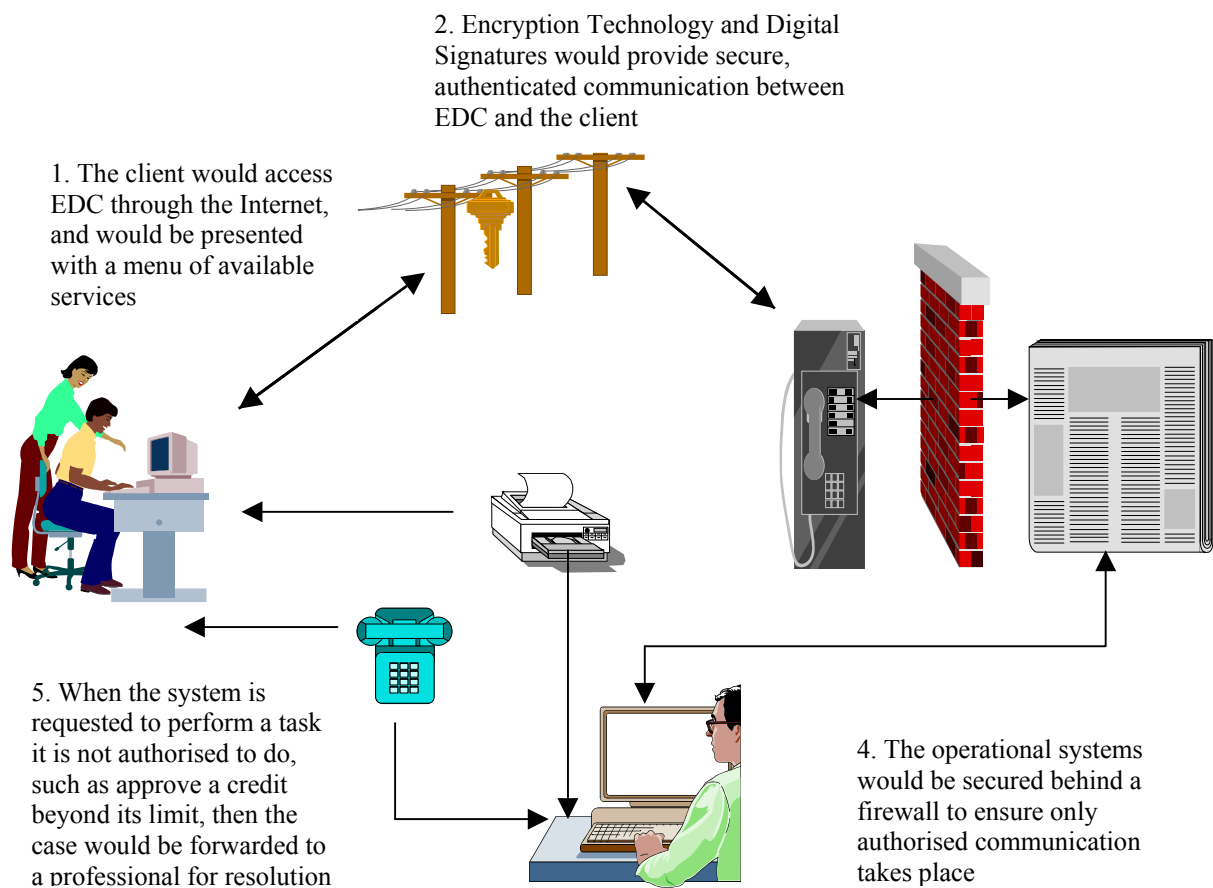
EDC Direct Web Interface

(diagram EDC Direct Web Interface)

What is EDC Direct?

- Enables customers to interface with EDC's Credit Administration System (CAS)
- Built with Internet-based technologies, the service is currently available through a private network
- Secure and reliable data transfer

EDC Direct



EDC Direct Future Enhancements

Policyholders will have direct access to:

- Statement(s) of account(s)
- List(s) of Approved Credit
- Application forms for Small & Medium Enterprises (SME'S)
- Submit declaration forms & claim applications
- Report overdue & problem accounts

Claims & Recoveries System

(CRS)

Overview

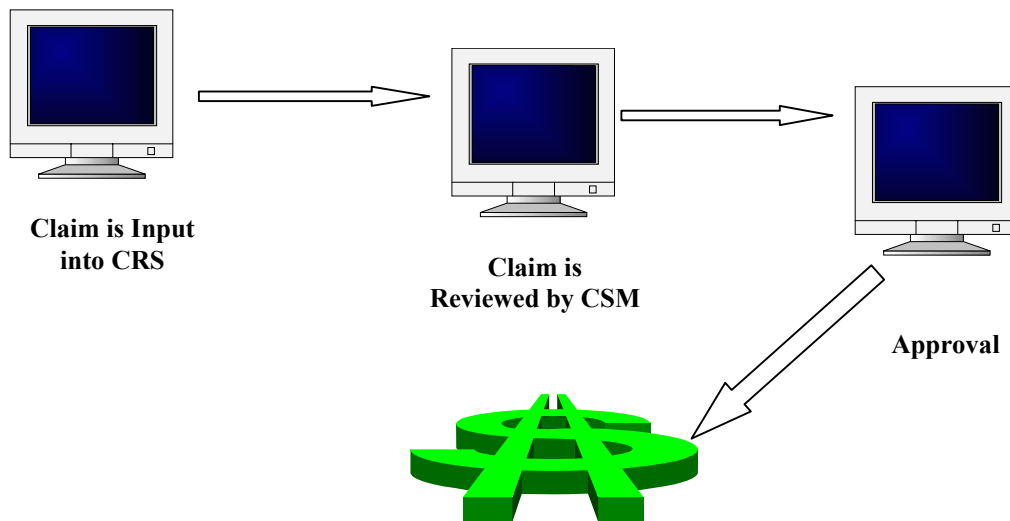
What is CRS?

- CRS is a major corporate control system used for the following purposes:
 - On-line claim processing and approvals
 - On-line recovery processing
- All claims are stored and processed by CRS (i.e. paper files only exist as keepers of paper)
- CRS is linked to all underwriting, accounting and corporate control systems

CRS - History

- CRS went into production in 1988
- CRS was the first automated system at EDC for processing claims
- The application helped EDC leap from a manual process to a fully automated, on-line processing and approval system
- The implementation of CRS resulted in cost-effective improvements to the claims and recoveries business process

Claim Process on CRS



CRS - Controls

- All delegated authorities for approvals are controlled through CRS
- CRS is table driven allowing easy modifications to authority levels, products, and program controls
- The linkages to upstream and downstream systems provides strong control over the claims process

Summary

The use of these support systems has resulted in several benefits, including those outlined below:

- A built-in flexibility to evolve with the business and to support increased volumes
- Build-in features that enhance Corporate control over the approval & payment processes
- Constant improvements in the speed and delivery of services to EDC's customer
- Accurate baseline data that allows for robust reporting both for operational and strategic considerations
- Lower operating costs

Operating Results

Customer Satisfaction

- Annual survey of customers' satisfaction with EDC services
- Composite score (out of 10) rates overall satisfaction and likelihood to recommend

| | | <u>CSI Score</u> |
|------|--------|------------------|
| 1995 | Actual | 8.5 |
| 1996 | Target | 8.6 |
| 1996 | Actual | 8.8 |
| 1997 | Target | 8.8 |

Customers Served

- Increasing number of customers served is priority for EDC shareholder and EDC

| | | <u>Customers Served</u> |
|------|--------|-------------------------|
| 1995 | Actual | 2,462 |
| 1996 | Target | 2,900 |
| 1996 | Actual | 2,965 |
| 1997 | Target | 3,6000 |

Business Volume

- A key measure of EDC's service in meeting the needs of customers is volume of business concluded

| | | Business Volume <u>(\$Billions)</u> |
|------|--------|--|
| 1995 | Actual | 17.2 |
| 1996 | Target | 20.5 |
| 1996 | Actual | 22.0 |
| 1997 | Target | 27.5 |

Productivity

- Productivity is measured by the volume of business supported per dollar spent on administration

| | | <u>Productivity Ratio</u> |
|------|--------|---------------------------|
| 1995 | Actual | 302 |
| 1996 | Target | 317 |
| 1996 | Actual | 367 |
| 1997 | Target | 400 |

Profitability

- Ability to operate on a self-sustaining basis and ability to take more risk on behalf of EDC customers both depend on EDC's ability to operate profitably

| | | <u>Net Income</u> <u>(\$Millions)</u> |
|------|--------|--|
| 1995 | Actual | 44 |
| 1996 | Target | 45 |
| 1996 | Actual | 112 |
| 1997 | Target | 226 |

Chapter III

Trade and Investment Insurance System of Japan

International Trade and Investment Insurance
System of JAPAN

A TABLE OF CONTENTS

- 1. Introduction -Outline of Trade and Investment Insurance System**
 - (1) Brief History of EID/MITI's Insurance System
 - (2) Institutional Framework and Organization Set Up
 - 1) Law scheme of EID/MITI's Insurance System
 - 2) Structure of the Trade and Investment Insurance Special Account
 - 3) Organizations
- 2. Types, Features of EID/MITI's Insurance System**
- 3. Development, Promotion and Marketing of Products**
 - (1) Development of New products
 - (2) Introduction of New Underwriting Scheme for Market Promotion
- 4. Claims and Recoveries**
 - (1) Investment Claims and Recovery
 - (2) Current Status of Insurance Claims and Recovery in JAPAN

1. INTRODUCTION (Outline of Trade and Investment Insurance System)

(1) Brief History of EID/MITI's Insurance System

- 1950 Establishment of *General Export Insurance System* to cover the losses by exporters due principally to preshipment risks
The Export Credit Insurance Law and the Export Credit Insurance Special Account Law were enacted.
- 1951 Establishment of *Export Proceeds Insurance System* to cover the losses suffered by exporters due to inability to reclaim export payment.
- 1953 Establishment of *Export Bill Insurance System* for losses in case where the cargo exchange bills can not be paid along with bill maturity.
The Export Credit Insurance Law was renamed as the Export Insurance Law.
- 1956 Establishment of *Overseas Investment Principal Insurance System* for risks along with acquisition of stock or other shares overseas.
- 1957 Establishment of *Overseas Investment profit Insurance System* for risks along with remittance to Japan of fruits of overseas Investment.
- 1970 Combining Overseas Investment Principal Insurance and Overseas Investment profit Insurance to *Overseas Investment Insurance and* expanding coverage to wider range of Investment such as long term loans and property rights.
- 1974 Establishment of *Exchange risk Insurance System* for exchange risks such as long term deferred export proceeds.
- 1977 Establishment of *Export Bond Insurance System* for losses incurred due to demand from overseas orderer for unfair calling of bonds.
- 1981 Expansion of General Export Insurance, Technical and Other services and Supply Contract Insurance were introduced.

- 1987 Establishment of *Prepayment Import Insurance System* for losses related to the prepaid amount of imports and also expansion of Export Proceeds Insurance, Intermediary Trade Insurance System were introduced. The Export Insurance Law was renamed as *the Trade and Investment Insurance Law*.
- 1991 Establishment of *Short-term Comprehensive Insurance* for losses covering risks- both inability to export and collect of the export proceeds for individual exporters who made supplementary agreement with EID/MITI.
- 1993 Combining General Export Insurance, Export Proceeds Insurance and Intermediary Trade Insurance and integrating into a single insurance policy as a General Trade Insurance
- 1993 Establishment of *Overseas Untied Loan Insurance System* for losses due to the uncollectible long-term loans.

(2) Institutional Framework and organization Set Up

(1) Law Scheme of EID/MITI's insurance System

The International Trade and Investment Insurance system is operated by following statutes with the Trade and Investment Insurance Law as its organic act.

(a) Trade and Investment Insurance Law (Law No. 67 for 1950)

This Law is a fundamental part for the trade insurance system and stipulates the purpose, definition, the type of trade and investment insurance, the premium rate and contract limitation.

(b) Trade and Investment Insurance Law Enforcement Ordinance

(Cabinet Ordinance No. 141 for July 1953)

This ordinance prescribes the type of cargo, the basic premium rate, and the percentage of indemnity.

(c) Insurance Policy Clause

This policy Clause describes the terms and condition of contract such as the scope of indemnity and amount of loss etc. in each type of insurance.

(d) Supplementary Agreement

Under the comprehensive Insurance scheme, EID/MITI made special agreement with export association on behalf of individual exporters. This agreement describes the details of Insurance contract.

(e) Rules for Underwriting

This rules are very important as it prescribes our cover policy for each country in detail such as Total Commitments Limit, Insured Percentage, Usance Period (of payment), and Requiring ILC(irrevocable letter of credit)

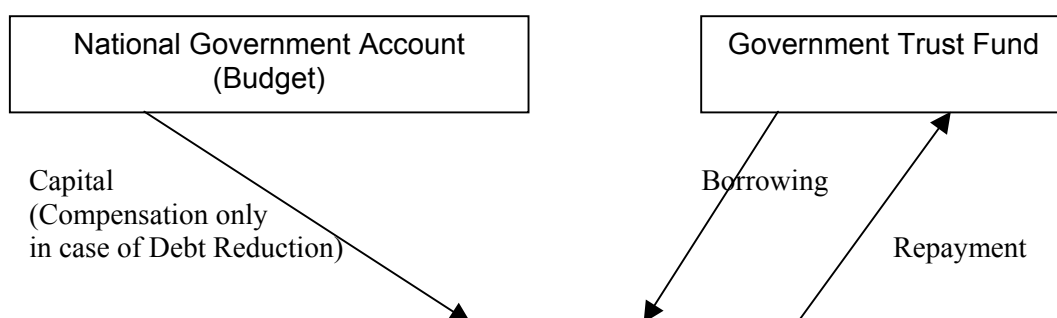
(f) The Trade and Investment Insurance Special Account Law (Law No.68 for 1950)

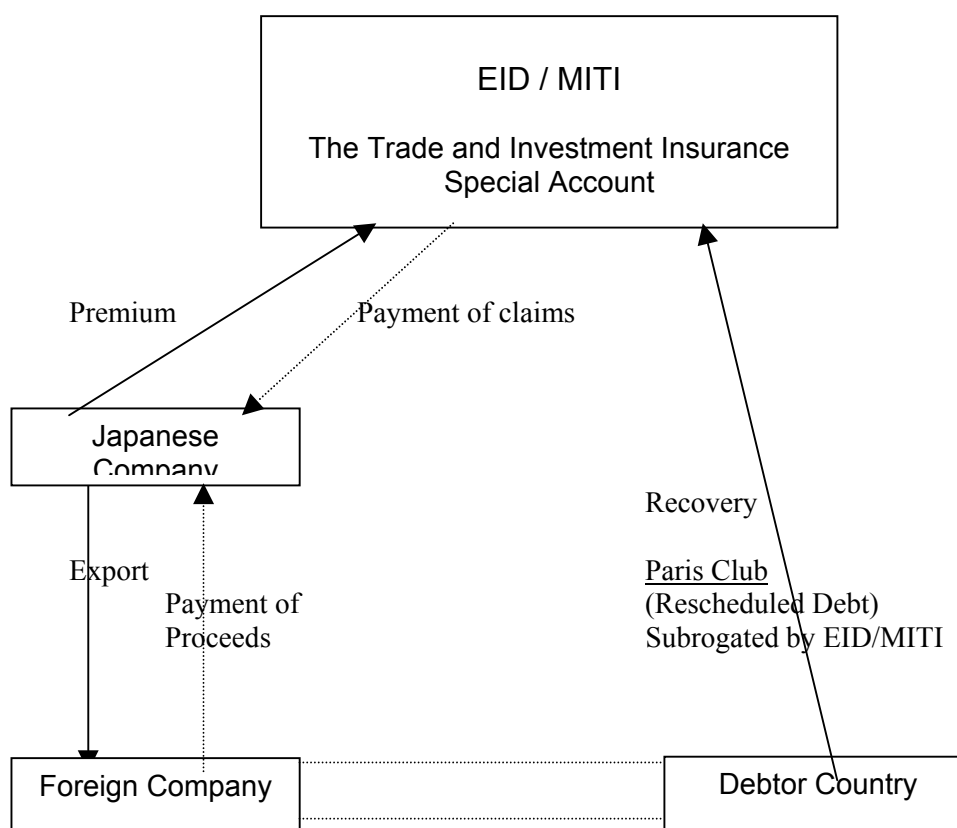
The International Trade Insurance system is operated by a special account premised on self-paying basis (principal of balancing income and expenditure) and this law stipulates the accounting procedures.

(g)The Trade and Investment Insurance Special Account Law Enforcement Ordinance (Cabinet Ordinance No. 205 for June 1950)

The Ordinance prescribes the method of profit and loss account in the special account and the like.

(2) Structure of The International Trade and Investment Insurance Special Account





(3) Organizations

The Export, Import and Investment Insurance Department of Ministry of International Trade and Industry (EID/MITI) is a authority which carries out establishing and amending the insurance system, making decisions on policies concerning the operation of insurance and underwriting policies for individual countries, and conducting negotiations on rescheduling. And simultaneously, EID/MITI is the underwriting organization in Japan actually engaged in insuring export credit and outward investment and in underwriting political risks in a significant way in such transactions. EID/MM is a real underwriter, which is issuing policies, collecting premium, giving limits and paying claims.

Japan Trade and Investment Insurance Organization (JTIO) is entrusted a part of work which relates to EID/MITI's insurance business activities.

Export, Import and Investment Insurance Department

Ministry of International Trade and Industry

Ministry of International Trade and Industry

International Trade Administration Bureau

| | |
|--|--|
| Trade Insurance Division | Overall coordination of each division of trade and investment insurance Accounting for a trade and investment insurance special account |
| Executive Director of Debt Relations and Underwriting Policy | Coordination of debt relations with foreign countries and other related activities |
| International Affairs and Country Policy Office | Analysis of country risk Collecting and exchanging information with overseas institutions |
| Policy Planning Office | Planning of various measures for trade and investment insurance |
| Short Term Insurance Office | Evaluation and underwriting of short-term insurance, credit supervision, appraisals and recoveries relating to commercial risk |
| Claims and Recoveries Office | Credit control, appraisals and recoveries relating to political risk |
| Information Systems Office | Use and development of computer system |
| Long Term Investment Insurance Division | Evaluation and underwriting of long-term insurance with a policy period of two years or more |
| Overseas Investment Insurance Office | Evaluation and underwriting of Overseas investment insurance and Overseas Untied Loan Insurance |
| Project Finance Office | Evaluation and underwriting of transactions relating to project financing |
| Paris Office | |
| New York Office | |

2. Types, Features of EID/MITI's Insurance System

(1) The insurance system is generally operated based on seven types of insurance policies

1. General Trade Insurance

Combination of General Export Insurance, Export Proceeds Insurance and Intermediary Trade Insurance - initiated in 1992

[General Trade Insurance System]

General Trade Insurance

Specific (Individual) Insurance

Comprehensive Insurance (Blanket coverage)

- ◆ For individual commodities and associations:
 - Facilities and Equipment
(Machinery, Electric cable, Automobile, Rolling stock, Ships)
 - Consumable goods
(Steel, Chemicals, Textile)
- ◆ For individual firms:
 - General short-term insurance
 - Technical cooperation
 - Loan contracts

2. Exchange Risk Insurance

3. Export Bill Insurance

4. Export Bond Insurance

5. Prepayment Import Insurance

6. Overseas Investment Insurance

7. Overseas United Loan Insurance

(2) Reason for Indemnity Under General Trade insurance

Political Risk

- (a) Imposition of restrictions or prohibition of foreign exchange transaction in a foreign country.
- (b) Imposition of restriction or prohibition of imports by the country of destination
- (c) Interruption of foreign exchange transactions due to war, revolution, or civil unrest in a foreign country.
- (d) Inability to export goods to the country of destination due to war, revolution or civil unrest in that country.
- (e) Interruption of transportation to the country of destination due to occurrences arising outside of Japan.
- (f) Debt rescheduling agreement between the governments concerned or delay of foreign currency remittance which is imputed to the paying country.
- (g) Any other occurrences arising outside of Japan which cannot be imputed to the relevant party to the export contract etc..
- (h) Imposition of export restrictions or prohibition based on the Foreign Exchange and External Trade Control Law. (only Pre-shipment risk)

Commercial Risk

- (i) In cases where the other party to the export contract, etc. a foreign government, foreign local government entity or similar body, the unilateral cancellation of the relevant export contract, etc. by the relevant other party or the cancellation of the relevant export contract, etc. by the insured due to the excessive requests from the other party. (only pre-shipment risk)
- (j) Bankruptcy of the other party to the export contract, etc. or loan contract, etc.
- (k) Any reason similar to the bankruptcy of the other party to the export contract, etc. (only pre-shipment risk)
- (l) Delay of six (6) months or more in the performance of obligations by the other party to the export contract, etc. or loan contract (Only post-shipment)

EID/MITI treat cases that fall in compensation conditions of (a) to (h) of the policy as **Political Risks**, Which cannot be imputed to the relevant party to the export contract etc., or loan contract- while cases that fall in compensation conditions of (i) to (l) are treated as **Commercial Risks**, treated as risks whose cause the party to the export contract etc., shall be held accountable for.

The relationship of the risks to be indemnified and reason for indemnity is as follows;

◆ Inability to export (pre-shipment)

Condition (a) to (h) [Political Risks]

Condition (i) to (l) [Commercial Risks]

◆ Inability to Collect (post-shipment)

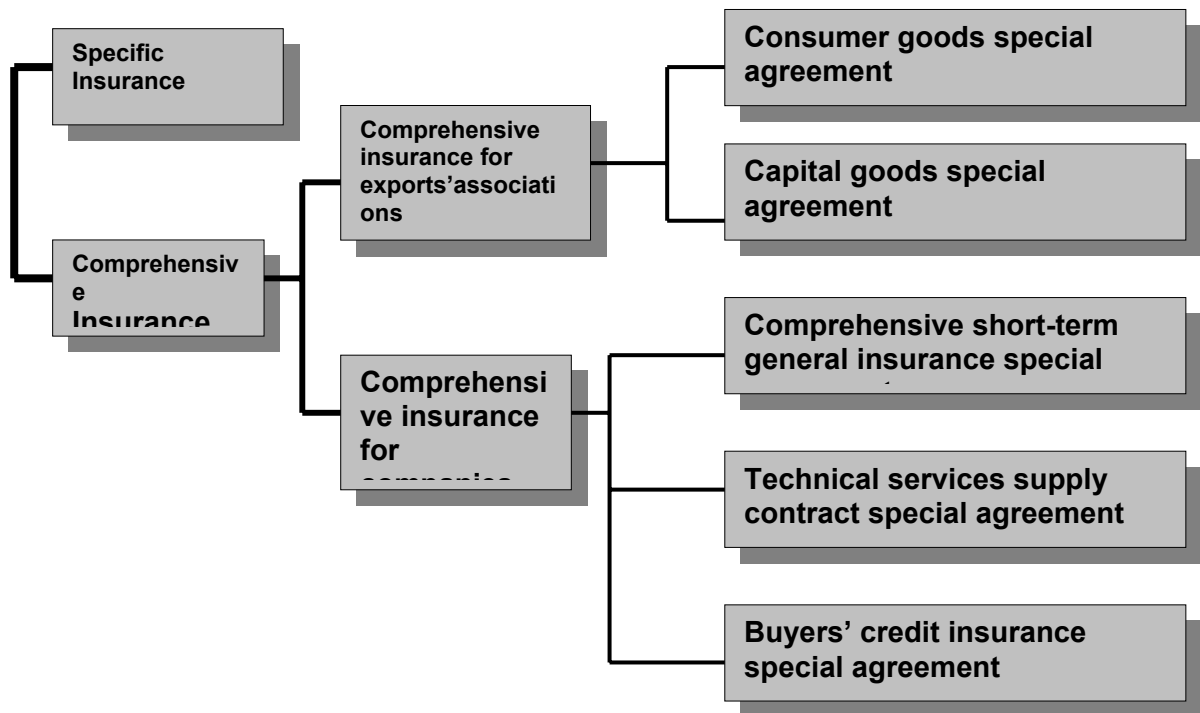
Condition (a) to (g) [Political Risks]

Condition (j) to (l) [Commercial Risks]

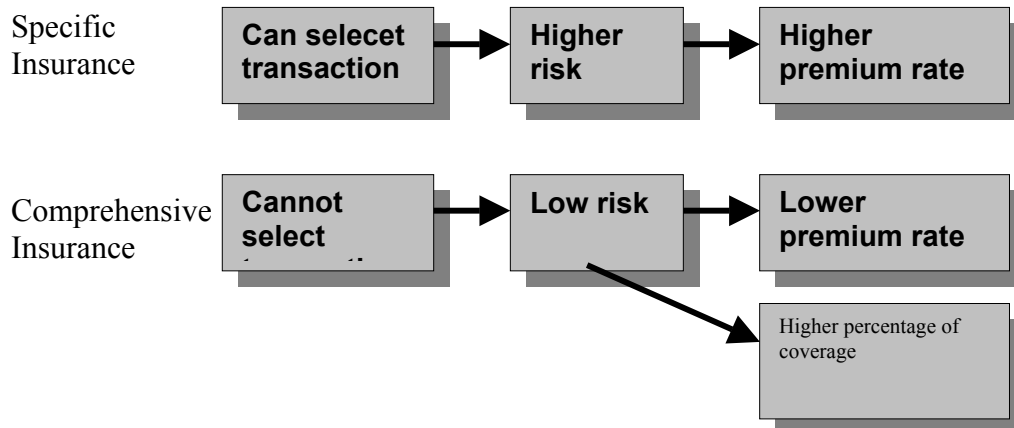
Specific Insurance and Comprehensive Insurance

Specific Insurance---Persons who intend to apply for insurance coverage select transaction for insurance and apply.

Comprehensive Insurance---Persons who intend to apply for insurance coverage apply in respect to all export contracts to be signed within a certain period of time



Advantage of Comprehensive Insurance



Commercial risk under
General Trade Insurance
(Pre-shipment),
Export Bond
Insurance ---% higher

**Exporters' Associations and Goods Covered
by Comprehensive Insurance for Capital Goods**

| Name of Association | Special agreement goods | Lower limit of export contract value |
|--|-------------------------------------|--------------------------------------|
| Japan Machinery Export's Association | Plant machinery, electric machinery | ¥25 million or more |
| Japan Rolling Stock Exporter's Association | Rolling stock | ¥10 million or more |
| Japan Ship Exporter's Association | New or remodeled ships | ¥50 million or more |
| Japan Electric Wire and Cable Exporter's Association | Electric wire and Cable | ¥10 million or more |
| Japan Automobile Manufactures Association, Inc | Automobiles | |

Insured Amount of Comprehensive Insurance for Capital Goods

| Classification | Pre-shipment | Post-shipment |
|-----------------|------------------------------|---|
| Political risk | 80% of export proceeds (FOB) | 97.5% of export proceeds (90 %) for intermediary trade) |
| Commercial risk | 80% of export proceeds (FOB) | 90% of export proceeds (80% for intermediary trades) |

**Exporter' Association and Goods Covered
by Comprehensive Insurance for Consumer Goods**

| Name | Special agreement goods | Lower limit of export contract value |
|---|---------------------------------|--------------------------------------|
| Japan Cotton Textile Exporter's Association | Cotton yarn and fabrics | ¥150,000 or more |
| Japan Silk and Synthetic Textile Exporter's Association | Silk fabrics, synthetic cloth | ¥150,000 or more |
| Japan Woolen and Linen Textiles Exporter's Association | Wool and hemp products | ¥150,000 or more |
| Japan Textile Products Exporter's Association | Textile produces | ¥150,000 or more |
| Japan Iron and Steel Exporter's Association | Iron and steel | ----- |
| Japan Galvanized Iron Sheet Exporter's Association | Galvanized iron and steel sheet | ----- |
| Japan Wire Products Exporter's | Steel wire products | ----- |

| | | |
|---------------------------------------|-------------------|---------------------|
| Association | | |
| Japan Chemical Exporter's Association | Chemical Products | US\$ 10,000 or more |

Insured Amount of Comprehensive Insurance for Consumer Goods

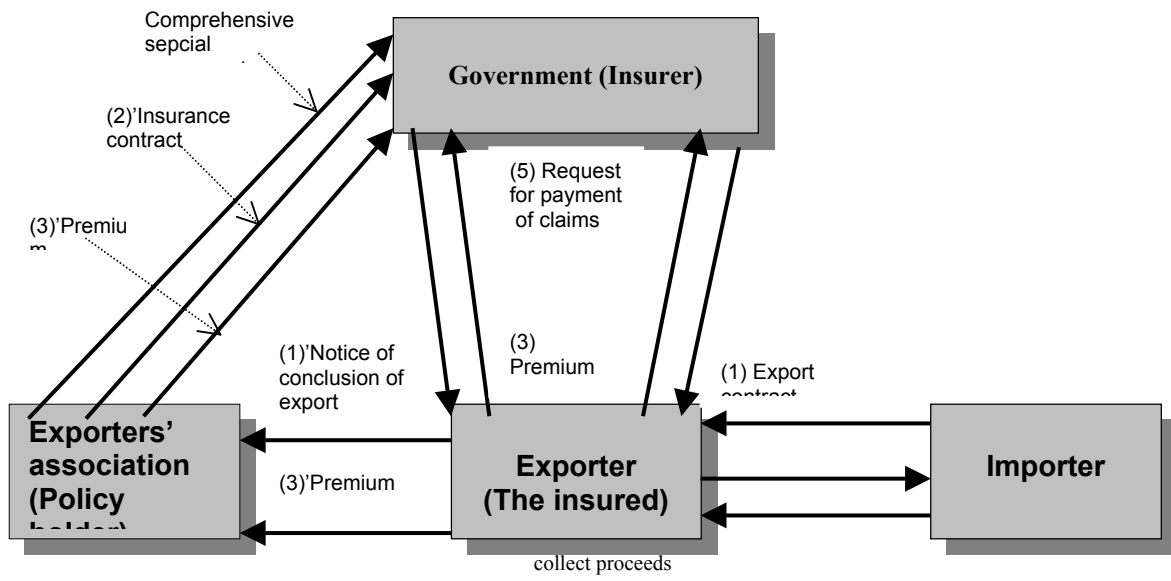
| Name of Association | Pre-shipment | | Post-shipment |
|--|------------------------------------|------------------------------------|------------------------------------|
| | Political risk | Commercial | Political risk |
| Japan Cotton Textile Exporters Association | 30% of export proceeds | 30% of export proceeds | 30% of export proceeds |
| Japan Silk and Synthetic Textile Exporter's | | | |
| Japan woolen and Linen Textiles Exporter's Association | | | |
| Japan Textile Produce Exporter's Association | 30%, 40% or 60% of export proceeds | 30%, 40% or 60% of export proceeds | 30%, 40% or 60% of export proceeds |
| Japan Iron and Steel Exporter's Association | 30% of export proceeds | 30% of exports proceeds | 30% of exports proceeds |
| Japan Galvanized Iron Sheet Exporter's Association | | | |
| Japan Wire Products Exporter's Association | | | |
| Japan Special Steel Exporter's Association | 40% of exports proceeds | 40% of export proceeds | 40% of export proceeds |
| Japan Chemical Exporter's Association | 30% of exports proceeds | 30% of exports proceeds | 30% of exports proceeds |

Parties Concerned with Insurance Contract

Insurer-----Parties who assume obligations to pay insurance claims when an insured occurs. For Trade Insurance, the insurer is the government.

The insured ----Parties who incur losses and hold insurable benefits when an insured risk occurs. For Trade Insurance, the insured is an exporter

Policy holder---Parties who sign an insurance contract and assume to pay premiums
For Comprehensive Insurance for an exporters' association, the policy holder is not the insured but an exporters' association and the insured is an exporter.



Premium Rates for general Trade Insurance

1. Basic Premium Rates

(Unite %)

| Classification | Transactions covered | Pre-shipment | | Post-shipment | |
|-------------------------|--|----------------|-----------------|----------------|-----------------|
| | | Political risk | Commercial risk | Political risk | Commercial risk |
| Special Insurance | Export contract | 0.208 | 0.043 | 0.253 | 0.033 |
| | Technical service supply or loan contract | ----- | ----- | | |
| | Intermediary trade contract | ----- | ----- | 0.316 | 0.033 |
| Comprehensive Insurance | Comprehensive insurance for consumer goods | 0.029 | 0.010 | 0.042 | |
| | Comprehensive insurance for consumer goods | 0.059 | 0.021 | 0.038 | 0.008 |
| | Short-term general insurance | | | | |
| | Technical service supply contract | ----- | ----- | | |
| | Buyers' credit insurance | | | | |
| | Intermediary trade contract | ----- | ----- | 0.048 | 0.008 |

2. Calculation Method for Premiums

Premiums = Insured amount for political risk x Premium Grade of political risk x Premium grade by country + Insured amount commercial risk x Premium Rate for commercial risk.

Premium Rate by Country

Discount or extra premium rates are applied according to the degree of risk.

Rate classification and rate applied for each country.

- (1) Specific General Trade Insurance (political risk)--- 8 grade from 0.5 to 5.0
- (2) Comprehensive General Trade Insurance (political risk) --- 8 grades from 0.5 to 0.8
- (3) Export bill insurance---9 grades from 1.0---3.0
- (4) Prepayment Import Insurance---5 grades from 0.8 to 2.0

| Type of Insurance Grade | | Specific General Trade Insurance | Comprehensive General trade Insurance | Export bill Insurance | Prepayment import Insurance |
|----------------------------|---|-------------------------------------|--|--------------------------|--------------------------------|
| Lower risk | A | 0.5 | 0.5 | 1.0 | 0.8 |
| | B | 1.0 | 1.0 | 1.2 | 1.0 |
| | C | 1.5 | 2.0 | 1.4 | 1.3 |
| | D | 2.0 | 3.0 | 1.6 | 1.6 |
| | E | 2.5 | 3.8 | 1.8 | 2.0 |
| | F | 3.0 | 4.5 | 2.0 | |
| | G | 4.0 | 6.0 | 2.2 | |
| | H | 5.0 | 8.0 | 2.5 | |
| Higher risk | I | | | 3.0 | |

Example of Premium Calculation

Date of export contract: December 5, 1996 (TTB¥11.65/US\$)

Export contract amount: CIF US \$ 1,500,000.00 (FOB US \$ 1,495,000.00)

Payment terms: DP\$% days after BL date

Date of Shipment: March 15, 1997

Rating of buyer: Grade EA

Importing country/paying country: Grade D

- ◆ General trade insurance (Specific)

| | Insured Value | Insured Percentage | Premium Rate | Multiplication Ratio by Country | Premium Amount |
|------------------------------|---------------|--------------------|--------------|---------------------------------|----------------|
| Pre Shipment-Country Risk | ¥166,916,750 | 95.0% | 0.208% | 2.0 | ¥ 659,654 |
| Commercial Risk | ¥166,916,750 | 60.0% | 0.043% | 1.0 | ¥ 43,064 |
| Post Shipment-Political Risk | ¥167,475,000 | 97.5% | 0.253% | 2.0 | ¥ 826,237 |
| Commercial Risk | ¥167,475,000 | 90.0 | 0.033 | 1.0 | ¥ 49,740 |
| Total | | | | | ¥ 1,578,695 |

◆ Short-term Comprehensive Insurance

Comprehensive Insurance for capital goods

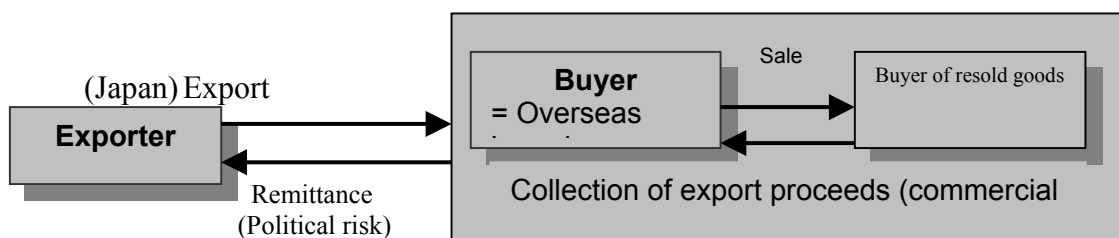
| | Insured Value | Insured Percentage | Premium Rate | Multiplication Ratio by country | Premium Amount |
|------------------------------|---------------|--------------------|--------------|---------------------------------|----------------|
| Pre shipment-Country Risk | ¥166,916,750 | 80.0% | 0.059% | 3.0% | ¥ 236,354 |
| Commercial risk | ¥166,916,750 | 80.0% | 0.021% | 1.0% | ¥ 28,042 |
| Post Shipment-Political Risk | ¥167,475,000 | 97.5% | 0.071% | 3.0% | ¥ 347,803 |
| Commercial Risk | ¥167,475,000 | 90.0% | 0.015% | 1.0% | ¥ 22,609 |
| Total | | | | | ¥ 634,808 |

Transactions Covered by Short-term General Insurance

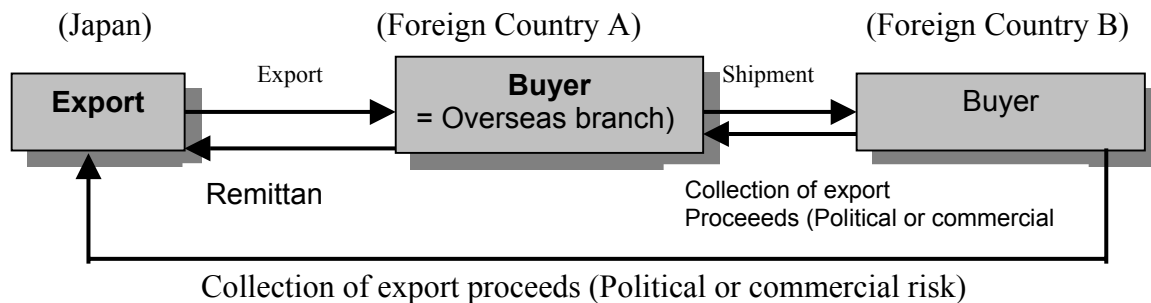
(1) Export contract



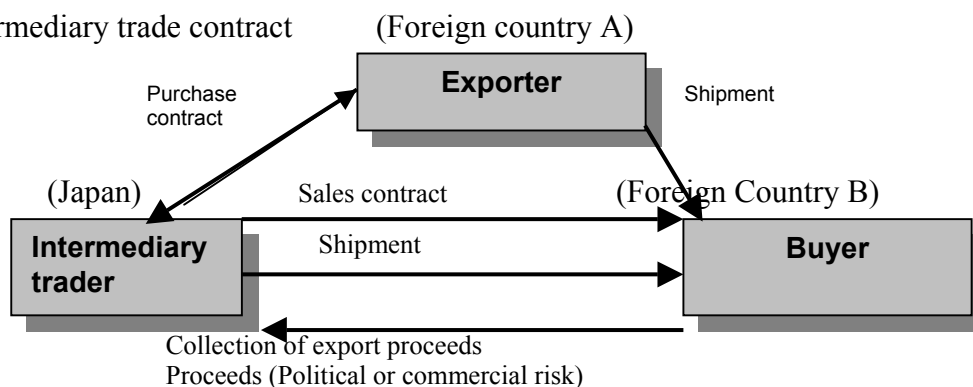
(2) Resale contract



(3) Entrepot (Transit) trade contract



(4) Intermediary trade contract

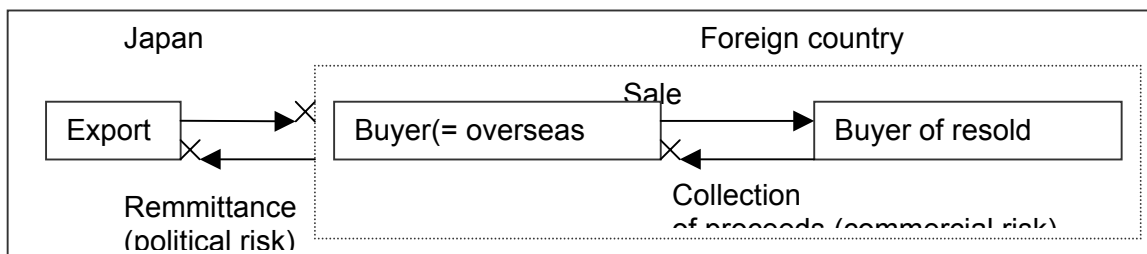


Options of Short-term Comprehensive Insurance

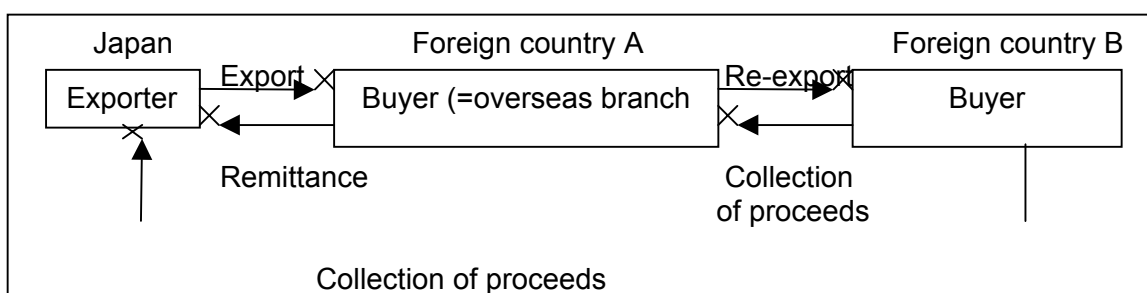
I. Contracts subject of insurance

1. 100% intermediary trade contract (without Japanese goods)
2. Resale contract and re-export contract

Resale contract



Re-export contract



II. EM/EF rating buyer's commercial risk after shipment

(Insurable usance) Six months or one year

III. Result rating

1. Discount of premium by insurance records: Discount of comprehensive rate or insured amount

2. Discount/surcharge by loss rate: Holder of a special agreement or divisions of holder

IV. Special agreement-----One special agreement for all the export contracts

-----Independent Division

-----Specific merchandise

Premium Rates for Short-term General Insurance

1 Basic Premium Rates

| Type of contract | Type of risk | Pre-shipment | Post-shipment |
|------------------|--------------|--------------|---------------|
| Export | Political | 0.059% | 0.038% |
| | Commercial | 0.021% | 0.008% |

2. Calculation Method for Premium

Premium to be paid = Insured amount for political risk × Premium rate × Premium grade by Country
(Political)

Pre-shipment

+ Insured amount for commercial risk × Premium rate × Premium grade by country
Post-shipment (Commercial risk)

+ Insured amount for political risk × Premium rate × Premium grade by country
Pre-shipment (Political risk)

+ Insured amount for commercial risk × Premium rate × Premium grade by country
Post-shipment (Commercial risk)

+ Discount or extra premium rate

Example for Calculating Premiums of Short-term General Insurance ---(I)

1. Precondition

(1) Export contract

| Importing country | Date of contract | Scheduled date of shipment | Contract amount | Payment method |
|--|------------------|----------------------------|-----------------|--------------------------|
| Political risk Premium grade By country ---0.5 | January 10, 1994 | March 1,1994 | US\$5000,000 | D/A 90 days after B/L |

(2) Date of insurance contract: January 11, 1994

(3) Insurance Period : 50 days form the date of the insurance contract to the scheduled date of shipment and 90 days from the scheduled date of shipment to the Payment date for export proceeds

(4) Buyer's Rating: EA rating in the foreign buyers list, Premium grade by country

: for commercial risk Pre-shipment --- 1.0 (in all cases)

Post -shipment --- 1.0

(5) Exchange rate: TTB opening price on the date of the export contract ---¥ 111.45/US\$

Example for Calculating Premiums of Short-term General Insurance ---(II)

2. Calculation of Premiums

| | | | | |
|-------------------|---|-----------------|---|-------------------|
| (Contract Amount) | | (Exchange rate) | | (Insurable value) |
| US\$500,000 | X | ¥111.45/US\$ | = | ¥55,725,000 |

Preshipment

| | | | | | | | |
|----------------------|---|------------------|----------------|----------------|--------|---|-------------------|
| (Insured percentage) | | (Insured amount) | | (Premium rate) | | (Premium grade by country for political risk) | |
| ¥ 55,725,000 | X | 80% | = ¥ 44,580,000 | X | 0.059% | X 0.5 | = ¥ 13,151 1 |
| | | | | | | (Premium grade by country for commercial risk) | |
| ¥ 55,725,000 | X | 80% | = ¥ 44,580,000 | X | 0.021% | X 1.0 | = ¥ 9,361 2 |

Postshipment

| | | | | | | | |
|--------------|---|-----|---|---|--------|---|-------------------|
| | | | | | | (Premium grade by country for political risk) | |
| ¥ 55,725,000 | X | 95% | = ¥ 52,938,750 | X | 0.071% | X 0.5 | = ¥ 18,793 3 |
| | | | (Premium rate for commercial risk A) | | | (Premium grade by country for commercial risk) | |
| ¥55,725,000 | X | 90% | = ¥ 50,152,500 | X | 0.015 | X 1.0 | = ¥ 7,523 4 |

Premium to be paid (1+2+3+4) = ¥ 48,828

Rate Review of Short-term General Insurance

-Application of discount or extra premium rates is based on the results of the past three years

(calculated using the moving average method).

-In principle, the rating moves up or down one rank every year.

However, when the rating moves up or down four ranks or more,

the rating should only be moved two ranks.

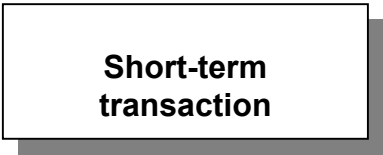
-This procedure is applied from the fourth fiscal year after the special agreement has been concluded.

| Loss rate | Adjustment percentage of insurance results |
|------------------|---|
| 0 ~ 19 | -50% |
| 20 ~ 39 | -40% |
| 40 ~ 59 | -30% |
| 60 ~ 79 | -20% |
| 80 ~ 97 | -10% |
| 98 ~ 102 | -0% |
| 103 ~ 110 | +10% |
| 111 ~ 120 | +20% |
| 121 ~ 140 | +40% |
| 141 ~ 160 | +60% |
| 161 ~ 180 | +80% |
| 181 ~ 200 | +100% |
| 201 or more | +100% or more |

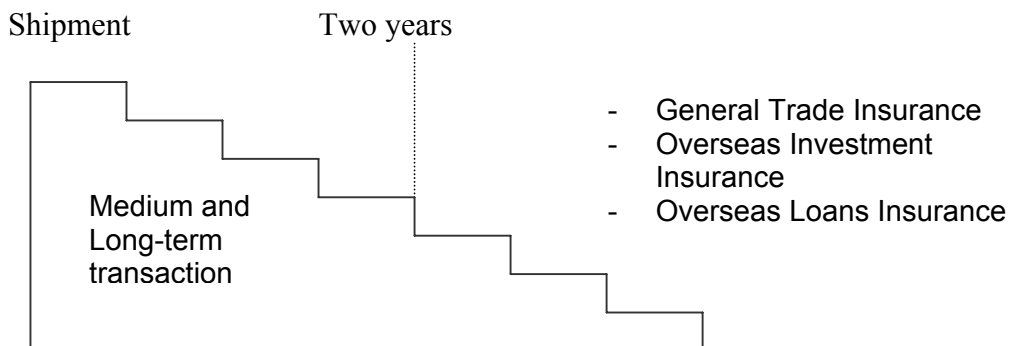
Short-term Transaction and Medium and Long-term Transaction

Short-term transaction--- Transaction in which the proceeds of an export contract are paid within two years after shipment

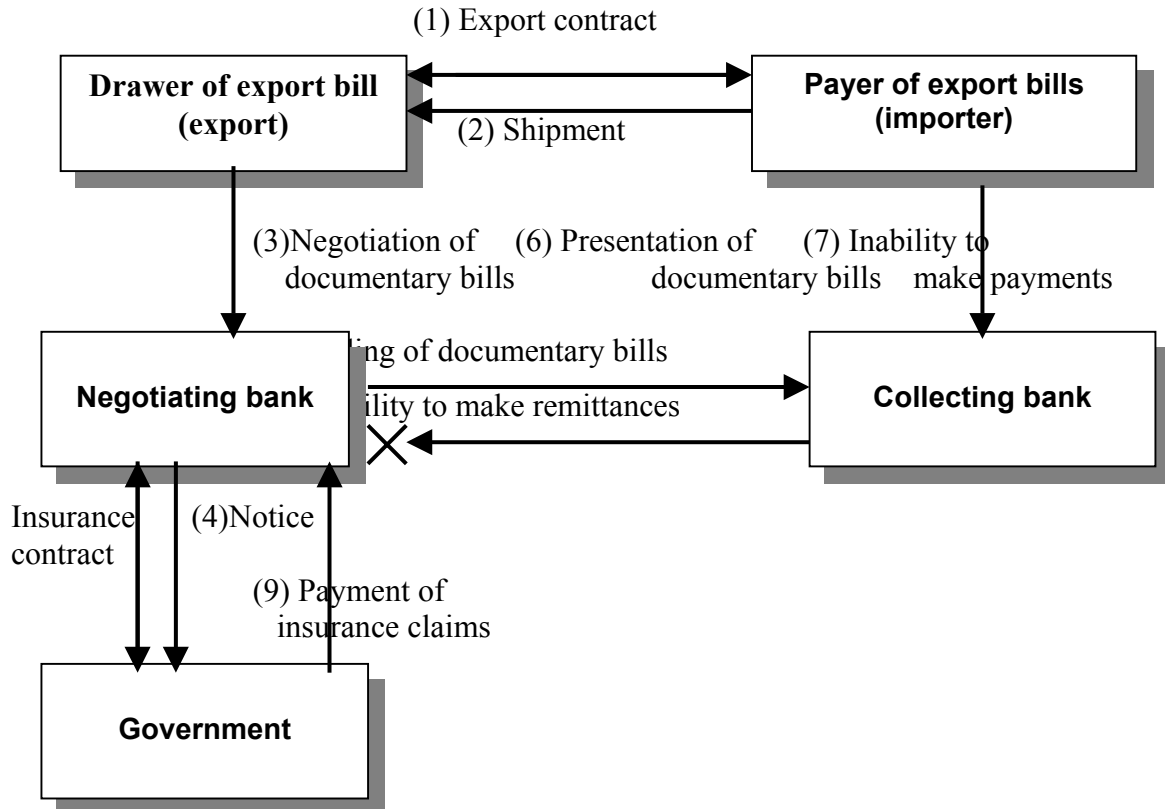
| | | |
|----------|------------------|--|
| Shipment | Within two years | <ul style="list-style-type: none"> -Specific insurance for General Trade Insurance -Comprehensive insurance for an exports' association for General Trade Insurance -Short-term Comprehensive insurance -Export Bill Insurance |
|----------|------------------|--|



Medium and Long-term Transaction --- Transaction in which the proceeds of an export contract are paid two years or more after shipment. Such transactions should comply with the OECD guideline. Furthermore, the case below is classified as follows: when 20% or less of the proceeds is paid separately at a later date as a retention, this portion is classified as a transaction whose payment is made two years or more after shipment and the portion which is paid within two years from the first day for calculating the number of days is classified as a short-term transaction.

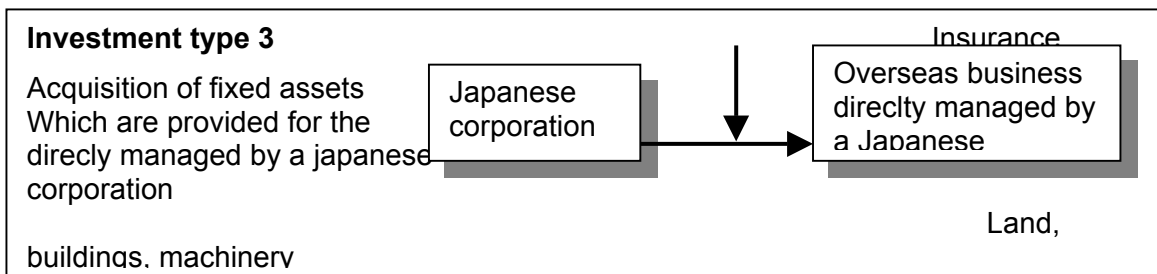
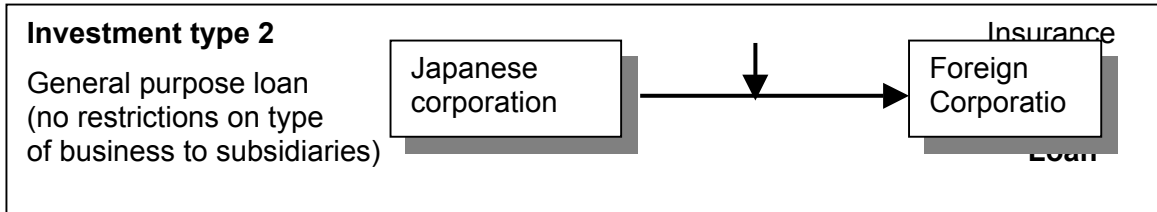
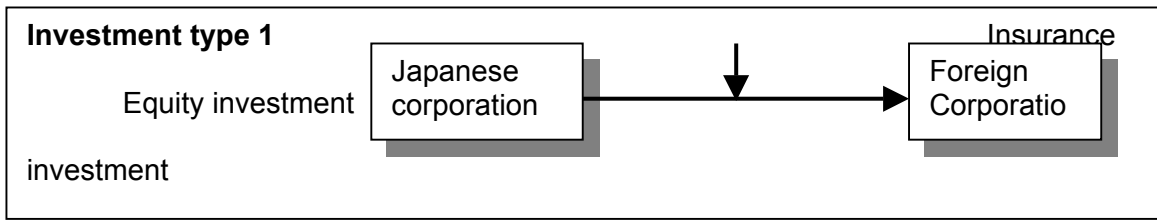


Outline of Export Bill Insurance



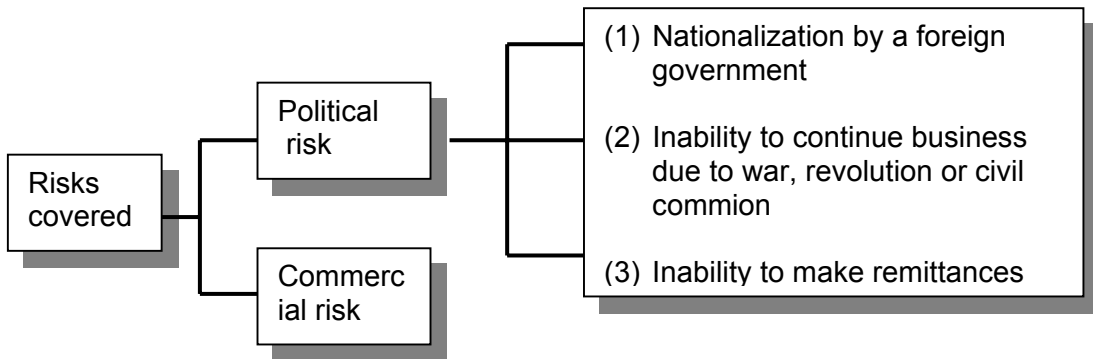
Insurance contracts are concluded at the beginning of each fiscal year.

Overseas Investment Insurance Investments Covered

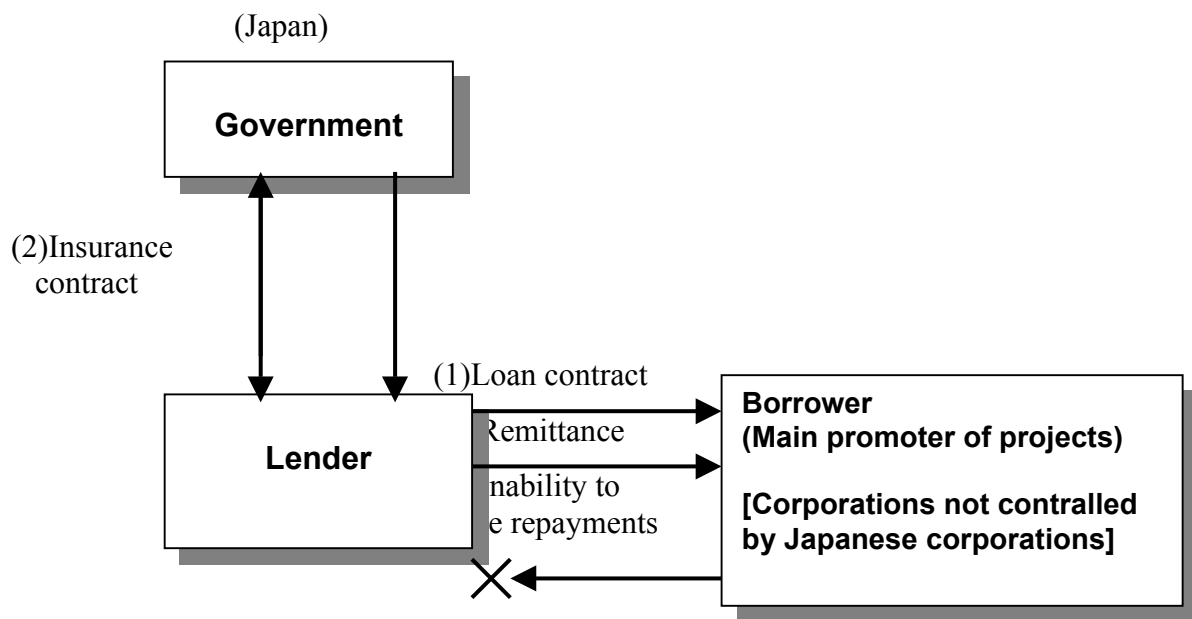


Investment type 4 Surety obligations of the investment type2.

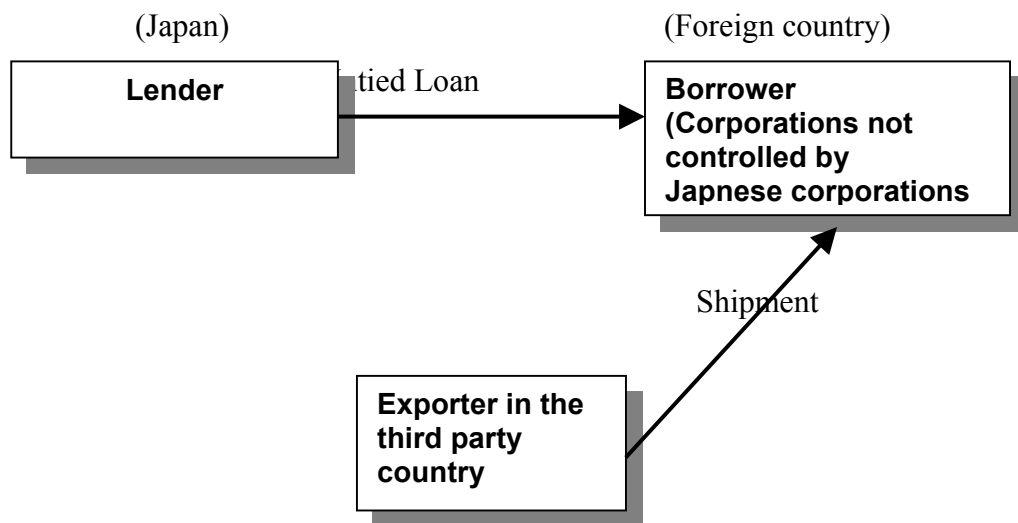
Risks Covered by Overseas Investment Insurance



Outline of Overseas Loans Insurance

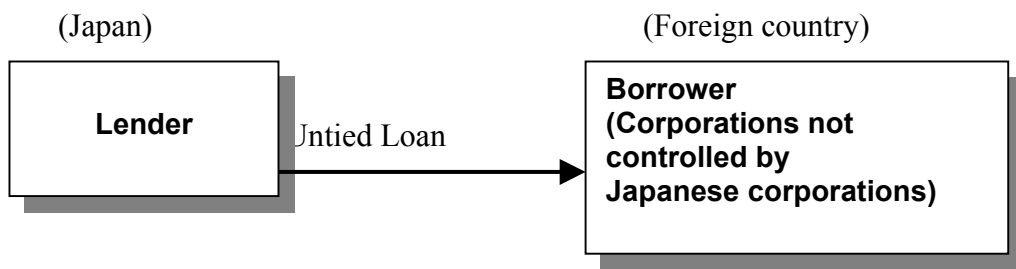


Loans Covered by Overseas Loan Insurance (1)



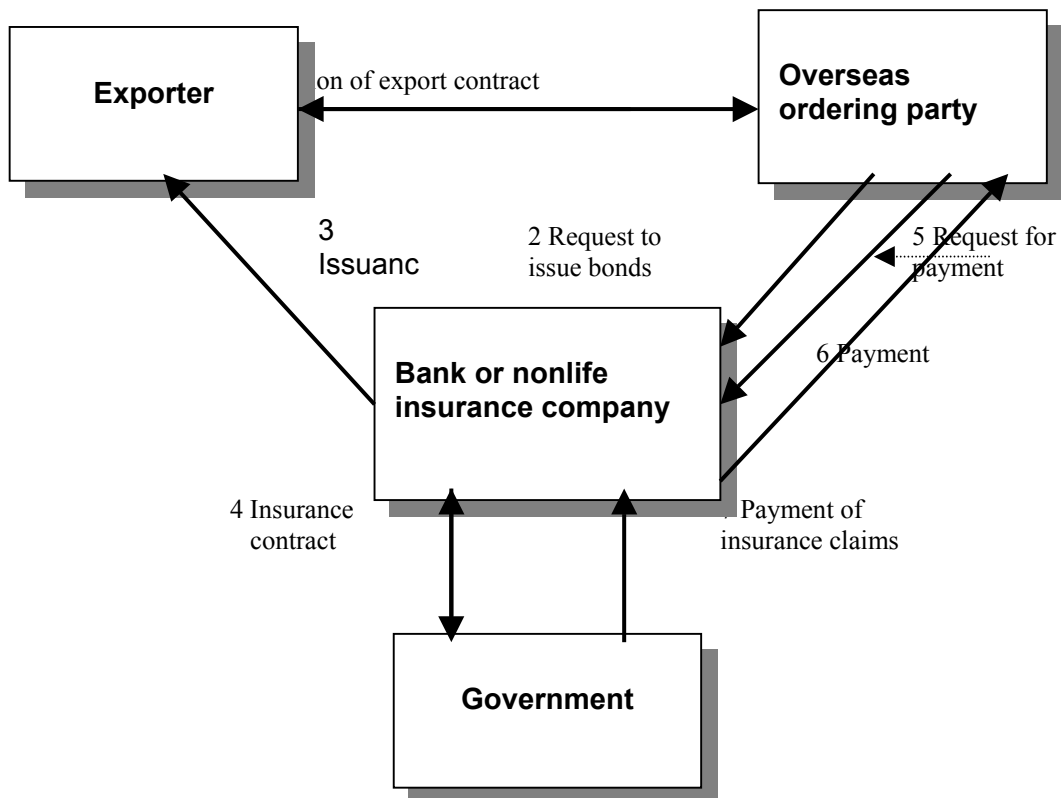
“Not controlled” is determined according to the percentage of shares held (50% or less) or the percentage of executive officers (50% or less)

Loans Covered by Overseas Loan Insurance (2)

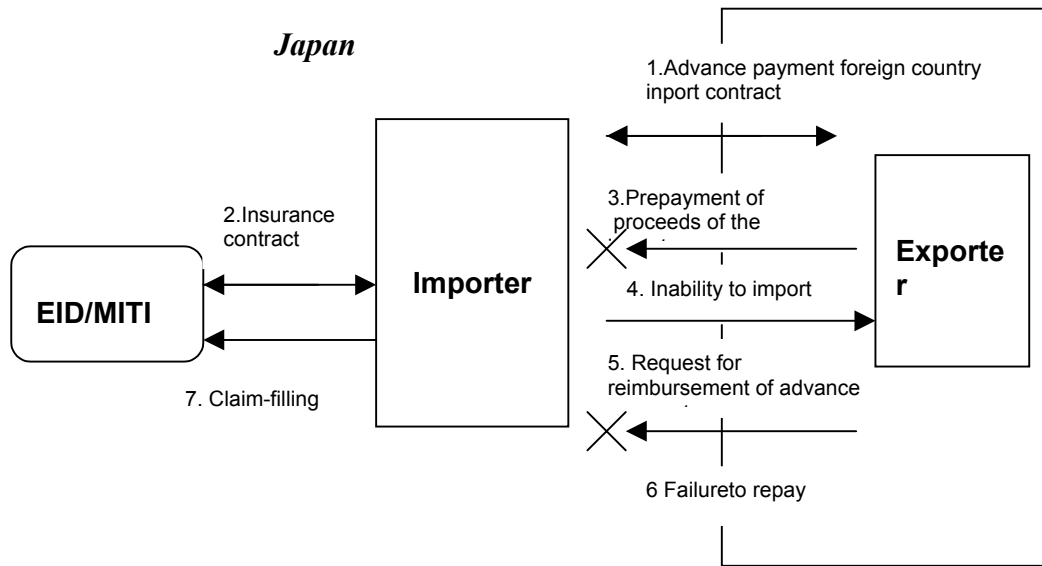


- Exports from 3rd countries
- Goods to replace imports
- Construction of infrastructure
- Refinancing

Outline of Export Bond Insurance



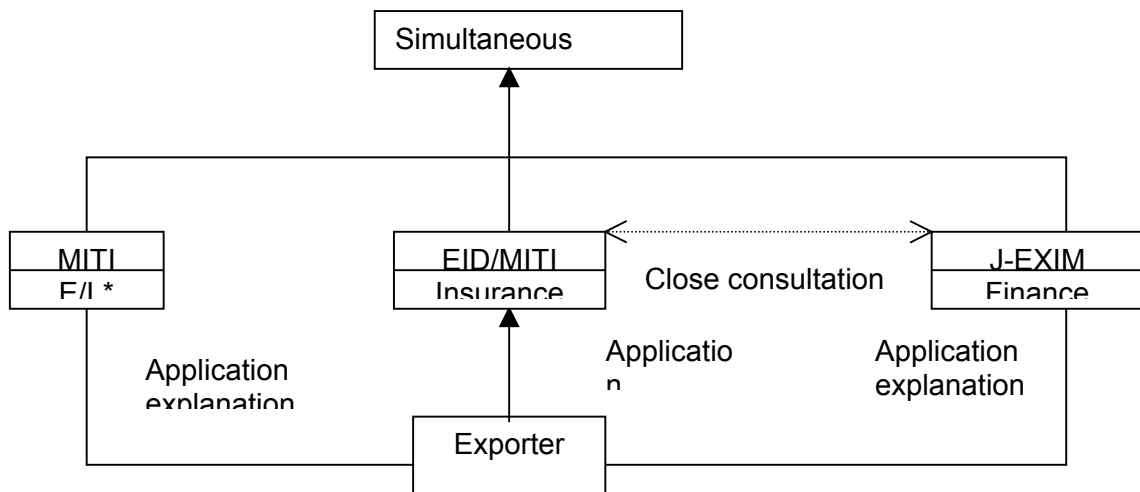
Outline of Prepayment Import Insurance



Relationship between
The Export, Import and Investment Insurance Dept.
Ministry of International Trade and Industry (EID/MITI)
And
The Export-Import Bank of Japan (J-EXIM)

1. The Export Credit Agencies (ECA) in JAPAN and Their Functions
 - 1) EID/MITI: export insurance and export credit policy
 - 2) J-EXIM : finance

2. Cooperation between the EID/MITI and the J-EXIM

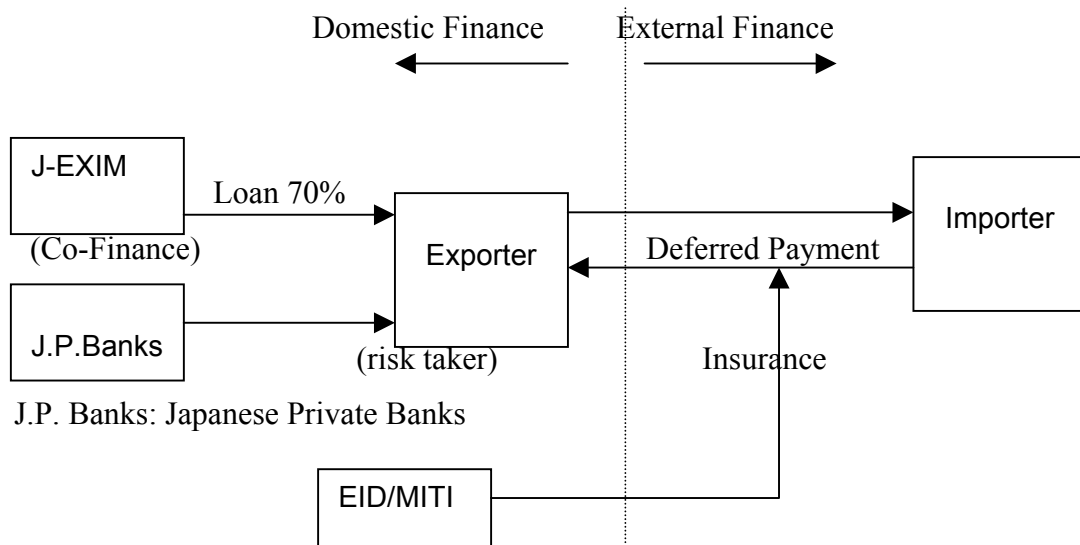


Three main policies are as follows:

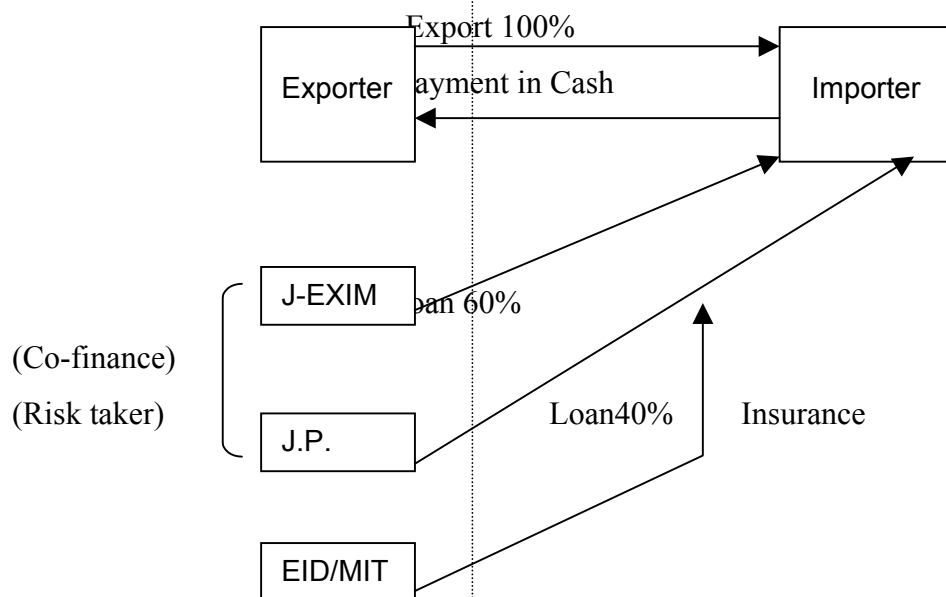
- 1) to provide insurance covering medium/long (more than two-year) term trade contracts.
- 2) to apply arrangement on guidelines for officially supported export credits of OECD
- 3) to provide insurance in cooperation with J-EXIM (on pure finance, no pure cover).

*E/L : Export License approved by Export Division of MITI

3. Basic Pattern of Supplier's Credit



4. Basic Pattern of Buyer's Credit



3. Development, Promotion and Marketing of Products

(1) Development of New Products

1) Short -Term comprehensive Insurance

This type of insurance , which provides comprehensive insurance for cooperation, was established in July 1991. This insurance covers trade contracts in which the settlement period for proceeds is less than two years and comprehensively covers political risks involving the inability to export and collect proceeds, as well as other wide-ranging commercial risks. In addition, it covers risks contingent on an intermediary Contract, Resale Contract (in the same country) and Resale Contract (Transit Trade).

2) Overseas United Loan Insurance

This insurance covers losses incurred by Japanese financial institutions, Trading companies or other entities through their inability to collect on loans, etc., or through their performance of surety obligations or their inability to collect amount to be acquired by exercising the right of indemnity due to political risks (inability to remit funds due to war, civil war, restrictions or prohibition of foreign exchange transactions in a country in which such loans have been extended) or commercial risks (for example, the bankruptcy of a party to whom such loans have been extended or a delay of six months or more in the performance of obligations by such party), when such financial institutions, trading companies or other entities have extended long-term loans (those which do not contribute to an increase in exports from Japan and are extended to foreign cooperation not controlled by a Japanese cooperation, foreign government of foreign nationals) for projects to benefit economic development in developing countries.

(2) Introduction of New Underwriting Scheme for Market Promotion

1) Covering for Medium an Long – Term commercial Risk without Letter of Guarantee (NO-L/G)

In principle, EID/MITI requires the applicants for medium-and long-term commercial and political risk insurance to have a L/G issued by the government or a First-class bank.

This principle is based on a concept that L/G secures both commercial risk and political risk.

Reason for securing political risks

- Government-guaranteed Medium and Long-term transaction would be recognized without any trouble even if the debt goes to rescheduling.
- Also, in case of war or revolution etc. in host country, we are expecting the debt to be treated by new government favorably as an official debt.

However, as developing countries undergo privatization, it becomes very difficult to obtain a government L/G. For this reason it is time for EID/MITI to consider the possibility of covering political risks as well as commercial risks without government L/G. Then we have to prepare several basic components inside EID/MITI for covering commercial risks, as a checking body, for risk assessment of each buyer in detail, and rating system for commercial risk accordingly with the credit worthiness of buyer.

Therefore, we cannot cover commercial risks without L/G instantly under the present circumstances.

We intend to make an effort to accumulate our experience and know-how concerning commercial risk. So we are going to cover only reliable cases. We have started to cover with this system since last year.

2) Exchange Rate Compensation System

EID/MITI introduced a new compensation system for the Exchange Risk in the Export Proceeds Insurance.

For the Export Proceeds Insurance, which covers the risk of uncollectable export proceeds, EID/MITI has been using the yen exchange rate based at the time of the contract.

However, in developing countries, due to their rapidly growing economies, the lack of proper infrastructures is a serious concern for the further development in these countries. Under such circumstances, the exporter or contractor used to keep their books in dollar terms, but if

yen were further depreciated against US dollar from the contract time, the exporters will not be able to recover the risk in dollar terms.

To reply to this request, EID/MITI has introduced New Exchange Rate Compensation System. For the time being, we are applying this system for the medium and long term businesses mainly for the project finance case. We now can cover the fluctuation of yen up to twice the amount of the insured value at the time of the contract.

Moreover, together with the above system, we also introduced a comprehension system to cover the losses for the fluctuation of interest within some range. Now the interest portion of insurable value can be changed up to 20% of the application rate in response to the fluctuation of the market rate.

The Interrelation between Exchange Fluctuation and Trade Insurance (Insured Value = \$ 100 million)

| Time of the contract (1 \$=¥ 100) | | Occurrence time of Insured Risk / Depreciation (1 \$=¥ 120) | | Occurrence time of Insured Risk / Appreciation (1 \$=¥ 80) | |
|-----------------------------------|---------------------------------------|---|------------------|--|-----------------|
| Loss Amount | | ¥ 12,000 million (\$ 100m) | | ¥ 8,000 million (\$ 80) | |
| Claims Amount | | Applied rate | Claims | Applied Rate | Claims |
| | Former System | 1 \$ = ¥ 100 | \$ 1 m - ¥ 100 m | 1 \$ = ¥ 80 | \$ 1 m - ¥ 80 m |
| | New Exchange Rate compensation System | 1 \$ = ¥ 120 | \$ 1.2 m - ¥120 | 1 \$ = ¥ 80 | \$1 m - ¥ 80 m |
| Ratio of Coverage ※ | | | | | |
| | Former System | 83 % | | 100 % | |
| | New Exchange Rate Compensation System | 100 % | | 100 % | |

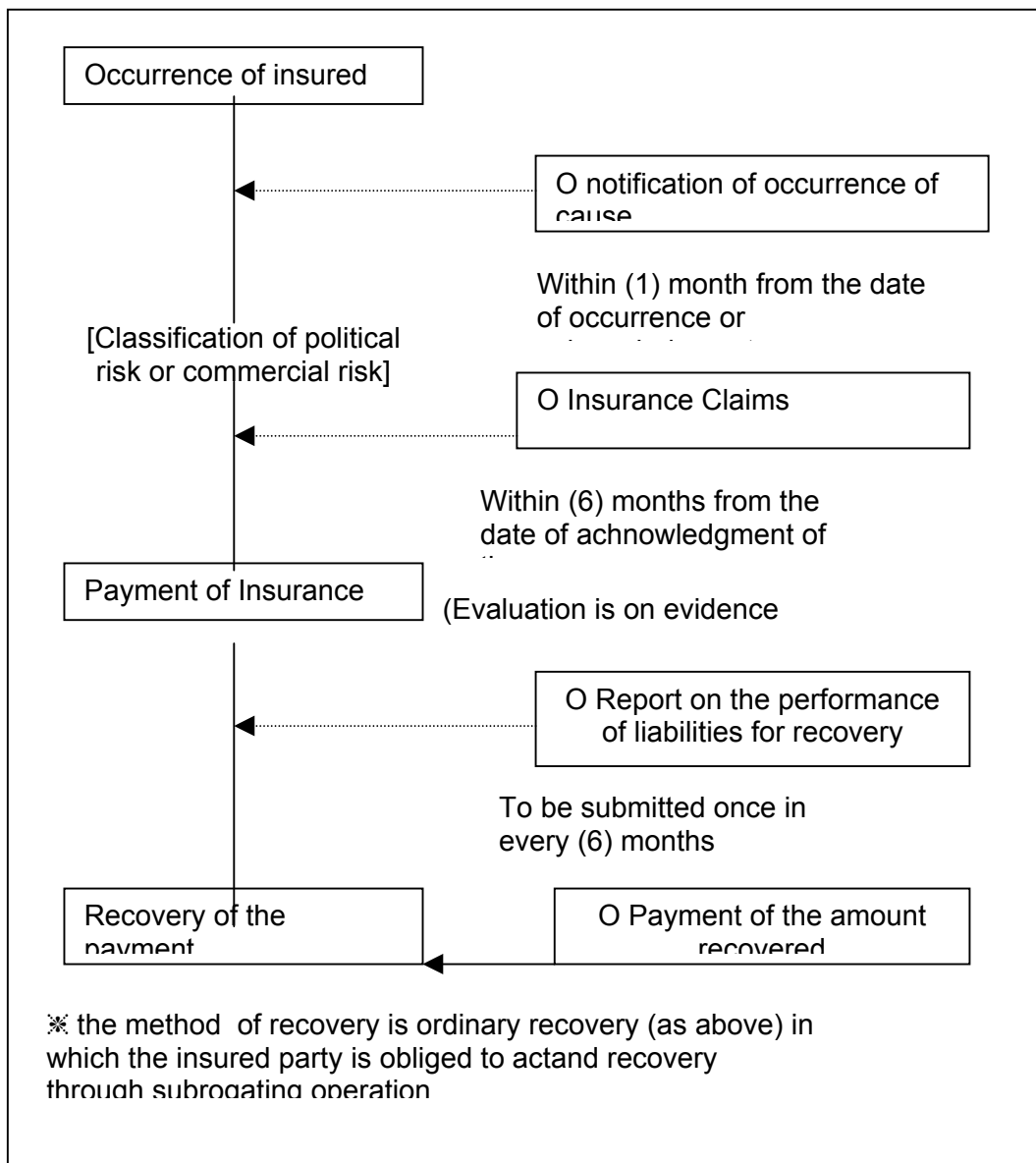
※ Ratio of Coverage = Insurance Amount / Loss Amount

4 Claim and Recovery

(1) Insurance Claim and Recovery (with Focus on Political Risks)

1) Procedures for Insurance Claim and Recovery

(an example of General Trade Insurance)



2) Obligation for Claim and Recovery

O After submission by the insured of the notification, EID/MITI will determine whether the cause of damage is due to political risk or commercial risk. In principle, such determination will be made on the basis of such occurrence of insured cause being attributable to the responsibility of the party or parties to the export contract.

In principle, the insured is to request insurance claim payment within six (6) months after the occurrence of insured cause.

The insured will be obliged to recover the loss after the insurance claim payment, keeping EID/MITI informed of the performance of his obligation, and making efforts in exercising the right of damage compensation demand.

As a consequence of such efforts, the insured will be required to make payment to the national treasury of any money recovered (general scheme of recovery).

Also, in contrast to this obligation of the insured, EID/MITI is also adopting the method of acquiring the right of credit in connection with the causes arising from the Paris Club rescheduling, making such credit a portion of remittances from the debtor country (recovery through subrogating operations).

Recovery of credits through subrogating operation amounted to 60.1 billion yen, or about 61%, of the total amount of 98.3 billion yen recovered in FY1995. On the basis of the number of claims, such recoveries accounted for approximately 13,000, or 58% of the approximately total about 22,000 cases.

O The credit to be acquired by the government is in principle all credit of the Paris Club rescheduling. Until the present, the government has made such efforts with twenty-two (22) countries.

3) Recovery through Subrogating Operation

As mentioned in (2) above, in the Japanese Trade Insurance system, the insured is obligated to expedite and recover the insured commercial debt. Regarding the Paris Club rescheduling, obviously such expediting efforts are not always proving fruitful due to the policies of the debtor country which restrict foreign exchange remittances.

The government (EID/MITI) acquires the credit of the insured when insurance claim payments are made, and conducts high level negotiations with the country's government for expediting and recovery.

Upon acquisition of credit, the insured and the government are to agree to the sharing of any amount recovered at a certain ratio, thus making credit management on individual settlement basis unnecessary and simplifying payments to national treasury.

Method for Calculating Claims Payable for General Trade Insurance

I Inability to export goods

Loss = Amount which cannot be collected of goods not been paid
 Expected profit
 Amount be collected of goods not been paid

Claim payment = Loss amount X 95% ≤ Insured amount

II Inability to collect proceeds

Loss amount = Amount which cannot be collected

Claims payable = Loss amount X $\frac{\text{Insured amount}}{\text{Insurable value}}$

Method for Calculating Recovery to inability to collect export proceeds

1. When recovery is made in respect to inability to collect export proceeds

$$\left((\text{Amount recovered} - \text{Amount recovered}) \times \frac{\text{Amount recovered}}{\text{Loss amount}} \right) \times \frac{\text{Claims paid}}{\text{Loss}}$$

2. When recovery is made through the disposal of goods which cannot be exported

$$(\text{Resale amount} - \text{Appraised amount of the goods}) \times \frac{\text{Claims paid}}{\text{Loss amount}}$$

3. When recovery is made in respect to inability to export goods

$$\text{Amount collected} \times \frac{\text{Claims paid}}{\text{Loss amount}}$$

(Note)

(2) Current Status of Insurance Claims and Recovery in JAPAN

1) Occurrences of trade insurance claims

On viewing the recent occurrences of trade insurance claims in Japan in terms of causes that can be indemnified, the majority of insurance claims on a total claim amount basis were for political risks, accounting for about 98%, in the amount of 211.6 billion yen out of the total amount of insurance claims in FY 1995 of 215.5 billion yen, while 890 claims, approximately 75% of total claims in term of numbers of claim cases, were for political risks.

When examined in terms of insurance types, 773 claims, or about 65% of that total number of claims, were for Export Proceeds Insurance, which accounted for 82% of political risk claims themselves, in terms of claim case numbers.

On a total insurance claim amount basis, Overseas Investment Insurance, entirely comprised of political risks, accounted for 71% of the total insurance claim amount, amounting to 153.2 billion yen, or as high as 72% of the political risk claims.

[Table: Share of Political Risk of Total Occurrence of Trade Insurance Claims]

(units: hundred million yen)

| | | FY 1994 | | FY 1995 | | P.RISK/ TOTAL % |
|------------------------------|-----|---------|--------|---------|--------|-----------------------|
| | | TOTAL | P.RISK | TOTAL | P.RISK | |
| General Export Insurance | (A) | 28 | 4 | 13 | 8 | 61.5 |
| | (B) | 2 | 2 | 12 | 12 | 99.4 |
| Export Proceeds Insurance | (A) | 1428 | 1461 | 773 | 728 | 94.2 |
| | (B) | 929 | 919 | 580 | 554 | 95.5 |
| Export Bill Insurance | (A) | 181 | 6 | 221 | 1 | 0.5 |
| | (B) | 6 | - | 9 | - | 0.3 |
| Overseas Invest. Insurance | (A) | 16 | 16 | 32 | 32 | 100.0 |
| | (B) | 74 | 74 | 1532 | 1532 | 100.0 |
| Prepayment Import insurance | (A) | 0 | 0 | 2 | 0 | 0 |
| | (B) | 0 | 0 | 2 | 0 | 0 |
| Intermediary Trade Insurance | (A) | 70 | 65 | 144 | 121 | 84.0 |
| | (B) | 15 | 15 | 21 | 19 | 89.3 |
| TOTAL | (A) | 1723 | 1507 | 1185 | 890 | 75.1 |
| | (B) | 1026 | 101 | 2155 | 2116 | 98.2 |

(A) Number of Claims,

(B) Total Amount of Claims

Although there had been a considerable decrease in the number of insurance claim cases in FY1995 over the previous year, the total amount of insurance claim payment had doubled due to drastic increase in Overseas Investment Insurance.

2) Current Status of Insurance Claim Payment

Payment of insurance claims in Japan amounted to 57.1 billion yen in FY 1995, a considerable decrease of 23.5 billion yen, or about 30%, from the 80.6 billion yen total of FY 1994. Most insurance claim payments were for political risk claim, which amounted to 56.3 billion yen, or 99% of total payments in FY 1995 and 79.5 billion yen, or 99% in FY 1994.

Regarding individual types of insurance, payment of claims under Export Proceeds Insurance accounted for 88% of total payments and payment of political risk related claims accounted for 87% of total payments.

[Table: Share of Political Risk Claims of Total Payment of Insurance Claims]

(units: hundred million yen)

| | | FY1994 | | FY1995 | | P.RISK/ TOTAL % |
|------------------------------|-----|--------|--------|--------|--------|-----------------------|
| | | TOTAL | P.RISK | TOTAL | P.RISK | |
| General Export Insurance | (A) | 119 | 100 | 51 | 39 | 76.5 |
| | (B) | 2 | 2 | 3 | 3 | 92.1 |
| Export Proceeds Insurance | (A) | 647 | 645 | 1006 | 1003 | 99.7 |
| | (B) | 756 | 752 | 504 | 499 | 99.1 |
| Export Bill Insurance | (A) | 185 | 2 | 61 | 0 | 0 |
| | (B) | 7 | - | 2 | 0 | 0 |
| Overseas Invest. Insurance | (A) | 16 | 16 | 32 | 32 | 100.0 |
| | (B) | 29 | 29 | 54 | 54 | 100.0 |
| Prepayment Import Insurance | (A) | 1 | 0 | 2 | 0 | 0 |
| | (B) | - | 0 | 2 | 0 | 0 |
| Intermediary Trade Insurance | (A) | 9 | 6 | 35 | 26 | 74.3 |
| | (B) | 12 | 12 | 9 | 7 | 84.0 |
| TOTAL | (A) | 977 | 769 | 1185 | 1100 | 92.8 |
| | (B) | 806 | 795 | 571 | 563 | 98.6 |

(A) Number of claims, (B) Total amount of claims

As mentioned above, most insurance claim payments were for political risk claims, while the majority of current payments are due to the Paris Club rescheduling. This applies to No. 6 of Reason for Indemnity of Article 3 of the General Trade Insurance Policy.

Insurance claim payments arising from rescheduling decreased to 57.3 billion yen in FY 1994 and to 35.6 billion yen in FY 1995, whereas they represented high weight ratios of 71% and 62% of total payments in FY1994 and FY 1995, respectively. In FY1991 and FY19892, Insurance claim payments for causes other than rescheduling had high weight ratios, due to the influence of the Gulf War and the collapse of the former Soviet Union.

[Table: Trade Insurance Claim Payments in the past five years]

(in hundred million yen)

| | FY1991 | FY1992 | FY1993 | FY1994 | FY1995 |
|------------------|--------|--------|--------|--------|--------|
| TOTAL PAYMENT | 3,419 | 1,482 | 1,280 | 806 | 571 |
| COMMERCIAL RISK | 76 | 16 | 17 | 11 | 8 |
| POLITICAL RISK | 3,343 | 1,466 | 1,263 | 795 | 563 |
| NON-RESCHEDULING | 2,379 | 948 | 502 | 233 | 215 |
| RESCHEDULING | 1,041 | 534 | 778 | 573 | 356 |

3) Collection of Claimable Assets (Recovery)

Collection of claimable assets in Japan amounted to 98.3 billion yen in FY1995, a considerable increase of 13.0 billion yen from the 85.3 billion yen in FY1994. Most collections were of political risk claims, which amounted to 97.0 billion yen, or 98% of total collections in FY1995.

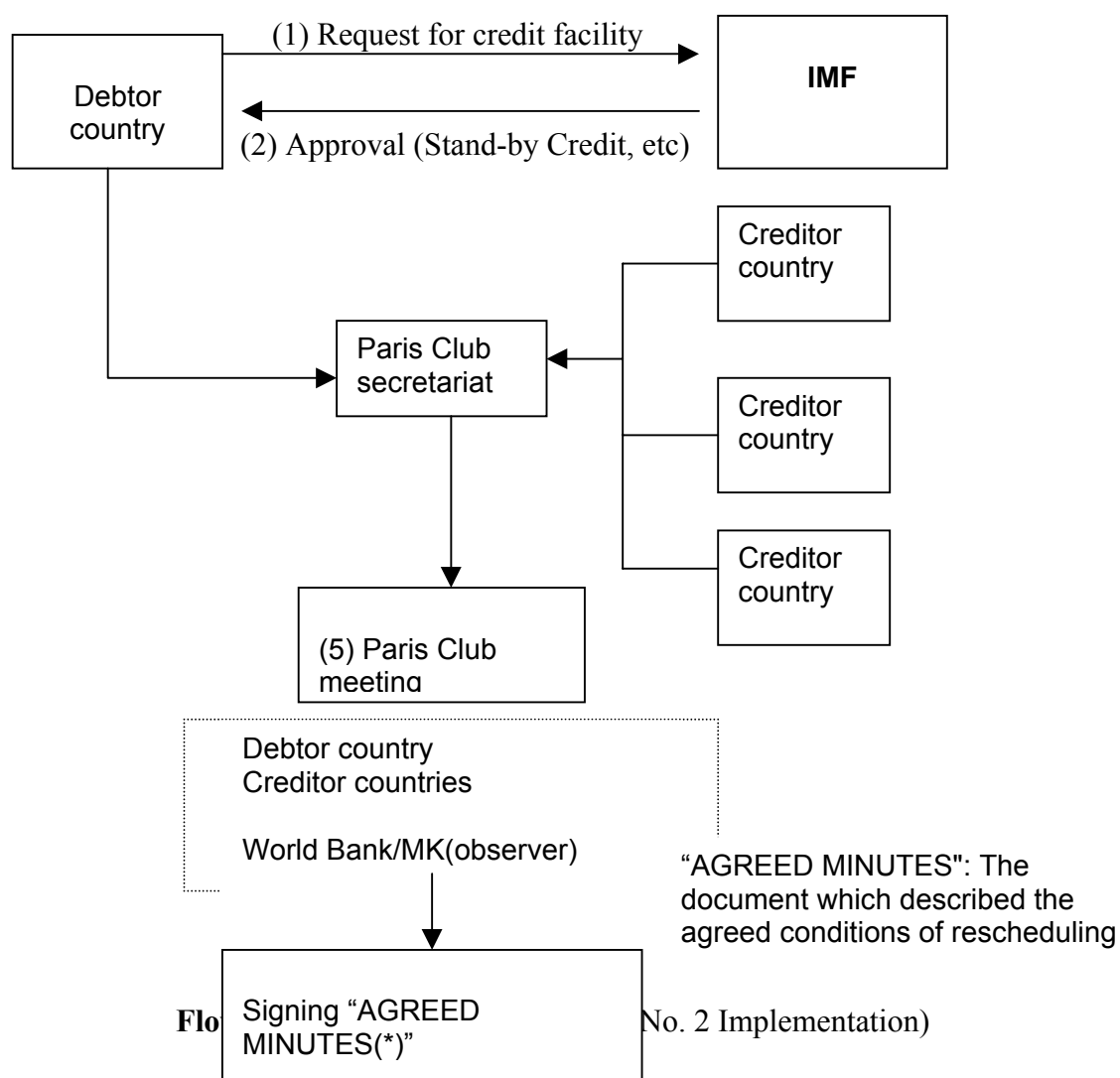
[Table: Share of Political Risk of Total Collection of Claimable Assets]

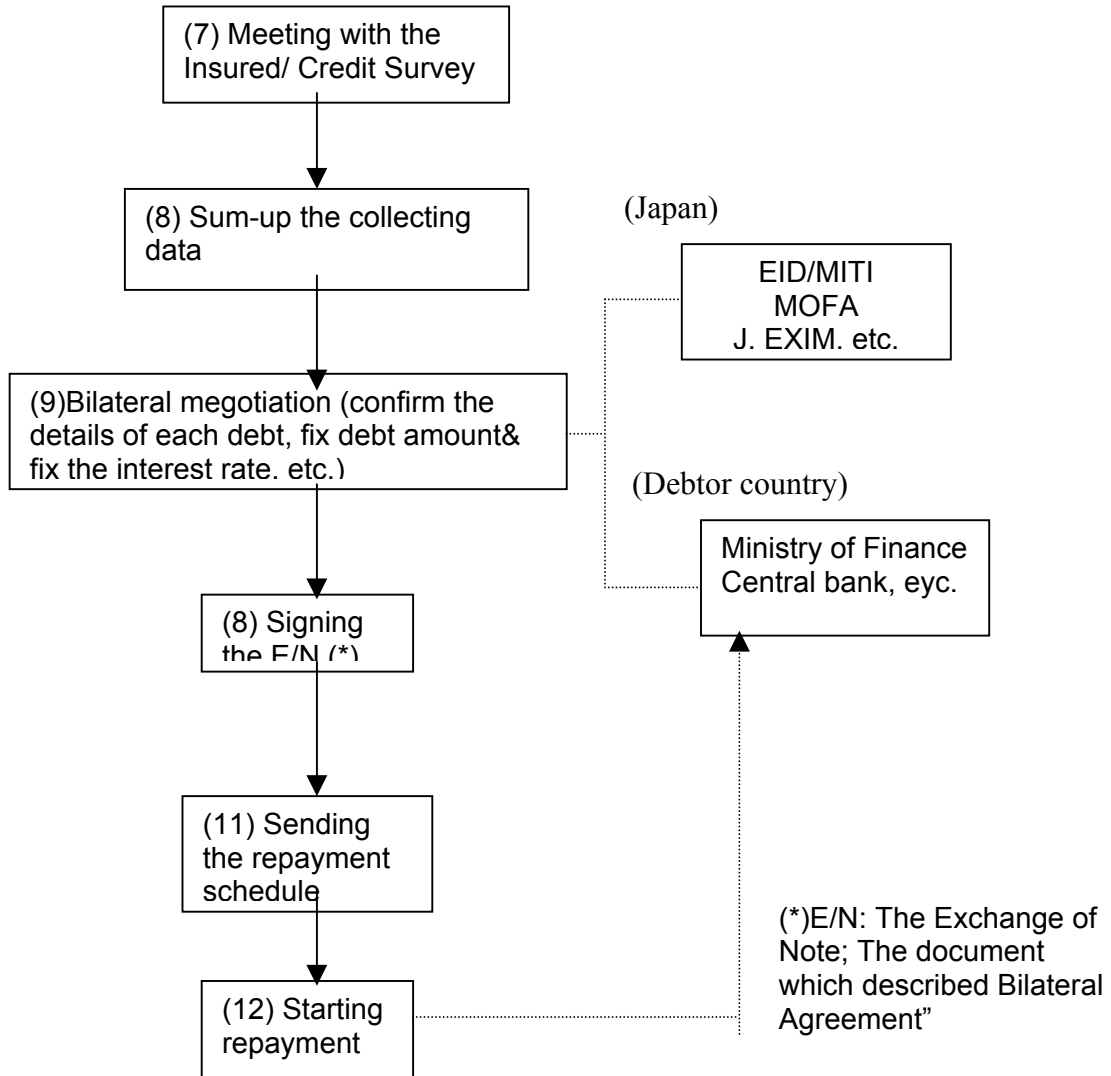
(units: hundred million yen)

| | | FY1994 | | FY1995 | | P.RISK/ TOTAL % |
|------------------------------|-----|--------|--------|--------|--------|--------------------|
| | | TOTAL | P.RISK | TOTAL | P.RISK | |
| General Export Insurance | (A) | 132 | 132 | 154 | 154 | 100.0 |
| | (B) | 2 | 2 | - | - | 100.0 |
| Export Proceeds Insurance | (A) | 13890 | 13872 | 21649 | 21611 | 99.6 |
| | (B) | 839 | 833 | 972 | 962 | 98.9 |
| Export Bill Insurance | (A) | 787 | 416 | 508 | 176 | 34.6 |
| | (B) | 12 | 11 | 7 | 6 | 75.1 |
| Overseas Invest. Insurance | (A) | 0 | 0 | 38 | 38 | 100.0 |
| | (B) | 0 | 0 | 1 | 1 | 100.0 |
| Prepayment Import Insurance | (A) | 1 | 0 | 3 | 0 | 0.0 |
| | (B) | - | 0 | - | 0 | 0.0 |
| Intermediary Trade Insurance | (A) | 4 | 4 | 34 | 34 | 100.0 |
| | (B) | - | - | 1 | 1 | 100.0 |
| TOTAL | (A) | 14616 | 14424 | 22433 | 22013 | 98.7 |
| | (B) | 853 | 846 | 983 | 970 | 98.2 |

(A) Number of claims (B) Total amounts of claims

Flow of Paris Club Rescheduling (No. 1 Implementation)





Chapter IV

Trade and Investment

Insurance System of the Philippines

TRADE AND INVESTMENT INSURANCE SYSTEM IN THE PHILIPPINES

I. BRIEF HISTORY OF EXPORT CREDIT INSURANCE

A. Background

The establishment of an export credit insurance facility in the Philippines had been considered as early as the seventies. A first step taken was the creation by law in 1972 of the Philippine Export Credit Insurance and Guarantee Corporation (PECIGCOR). However, the corporation never took off and was eventually abolished in 1979 by virtue of Executive Order No. 574 which transferred the corporation's functions to PHILGUARANTEE. In 1981, the Export Credit Corporation (ECC) was also established to perform, among others, an export credit insurance function. The corporation which never became operational, was likewise abolished in 1997 and its functions are also transferred to PHILGUARANTEE by virtue of Executive Order No. 127.

In the mid-eighties, the establishment of an ECI was again reviewed. The proposal to establish an ECI facility was deferred as studies have shown that the perceived need of export then was more on pre-shipment financing and guarantee rather than credit insurance.

In 1995, a decision was made to design a comprehensive ECI system suited to the needs of Philippine exporters including an interim system as may be required and to operationalize the system by establishing the appropriate facility in PHILGUARANTEE.

B. Developments

ECI PROJECT STUDY

Technical assistance under the World Bank - Japan Grant Export Development Project was utilized to fund two (2) constancy studies:

1. Establishment of an Export Credit Insurance facility in PHILGUARANTEE; and
2. Establishment of a Comprehensive Credit Information System (CCIS) to back up the ECI Program.

The ECI Project Study assessed the need for an ECI through a market survey of both exporters and bankers. It also contained an evaluation of Philippine export performance profile of exports, market patterns etc. Likewise, a review of existing policies, laws and regulations was made. The consultant's report showed there is a need for an ECI Program and the establishment of the ECI Program on an interim basis was recommended. A comprehensive Program will follow after a review is conducted.

The ECI Program was launched on January 31, 1997 and PHILGUARANTEE became the first and the only institution to offer an ECI facility in the Philippines.

The CCIS study, on the other hand, dealt with comprehensive credit information system, including a foreign buyers database, to provide support to ECI underwriting operations.

II. INSTITUTIONAL FRAMEWORK AND ORGANIZATIONAL SET-UP

A. *Legal Authority for the Establishment of the Export Credit Insurance (ECI) Program at PHILGUARANTEE*

As mentioned earlier, PHILGUARANTEE's authority to perform ECI functions derives from its absorption of the mandates of the two (2) defunct agencies, the Export Credit Corporation (ECC) and the Philippine Export Credit Insurance and Guarantee Corporation (PECIGCOR).

The accumulated legislation describing the powers and functions of PHILGUARANTEE are contained in the following decrees, executive orders and Acts of the Republic.

1. Presidential Decree No. 1080 creating PHILGUARANTEE in 1977.
2. Republic Act No. 6424 of 1972 creating the Philippine Export Credit Insurance and Guarantee Corporation (PECIGCOR) whose functions were transferred to PHILGUARANTEE in 1979 by Executive Order No. 574.
3. Presidential Decree No. 1785 of 1981 creating the Export Credit Corporation (ECC) whose functions were transferred to PHILGUARANTEE in 1987 by the Executive Order No. 127.

On August 29, 1996 the Office of the Government Corporate Counsel (OGCC) issued its Opinion No. 241 which stated that PHILGUARANTEE can offer export credit insurance to any bank or business in the Philippines on the basis of the combined provisions of Republic Act No. 6424 and Presidential Decree No. 1785. By virtue of this opinion, the authority of PHILGUARANTEE to act as an export credit insurance agency is confirmed.

B. Organizational Set-Up

1. **Board of Directors** - The power and functions of the Corporation are exercised by a Board of Directors composed of seven (7) members, as follows:
 - a. The Secretary of Finance, who shall be the Chairman of the Board. Whenever the Secretary of Finance is unable to attend, he shall designate an undersecretary to attend as his alternate who shall not act as Chairman.
 - b. The President of the Corporation, who shall be the Vice-Chairman of the Board, shall assist the Chairman and act in his stead in case of absence or incapacity.
 - c. The Secretary of Trade and Industry.
 - d. The Governor of the Bangko Sentral ng Pilipinas (Central Bank of the Philippine).
 - e. The Director-General of the National Economic and Development Authority.
 - f. The Chairman of the Development Bank of the Philippines.
 - g. The Chairman of the Philippine Overseas Construction Board.

2. Functional Areas:

Philguarantee is composed of nine (9) departments directly supervised by three (3) Senior Vice Presidents, as follows:

- Senior Vice President for Operations Group
 - a. Marketing and Business Development Department
 - b. Guarantees Department
 - c. Export Credit Services Department
 - d. Remedial Management Department
- Senior Vice President for CTA Group
 - e. Controllership Department
 - f. Treasury Department
 - g. Administrative Department
- Senior Vice President for Legal Services Group
 - h. Collection and Litigation Department
 - i. Documentation and Research Department

The Corporate Planning Office and Corporate Secretary's Office are functionally attached to the Office of the President while the ECI Office is attached to the Office of the Executive Vice President.

Since its launching in January 1997, the ECI Program has been operationalized on an interim basis using existing staff as follows:

- **Underwriting function** - handled by the Export Credit Insurance Office (ECIO). It is responsible for evaluating export proposal applications for the establishment of foreign buyer credit limits, issuing offer letter, determining the premium rate to be applied and ensuring the existence of an acceptable spread of risks. It is also responsible for premium billing, issuance of the Policy and maintenance of policy holder files.

- **Marketing function** - handled by the Marketing and Business Development Department (MBDD) which is responsible for recruiting prospective policy holders. It handles all inquiries and assists in filling out the application/proposal forms correctly, and sees to it that the processing fee is billed and receipted properly.
- **Credit Information, Management Information System, Economic intelligence and Country Risk Analysis function** - handled by the Export Credit Services Department (ECSD). These include evaluation of industry and country risks, making recommendations on country classifications, imposition or removal of special country limitation conditions, providing guidance on special industry conditions and trends of potential concern to management.

ECSD is also responsible for interfering with international sources of credit information on foreign buyers through COFACE. It likewise maintains a database on Philippine direct and indirect exporters.

- **Claims Handling and Recoveries function** - handled by the Remedial Management Department (RMD) with the support of Legal Services Group. It receives the Notices of Overdue Account and Notices of Claim and exporters request for intervention as well as evaluates the validity of claims and undertakes recovery measures. In case of payment, it also requests COFACE for reimbursement or funding as the case may be.
- **Accounting function** - handled by the Controllershship Department. It is in charge of remitting fees to COFACE, keeping accounting records and preparing ECI Program financial statements.
- **Treasury function** - handled by the Treasury Department which is responsible for insuring availability of funds for the open Requirements of the Project. It is also in charge of the issuance of official receipts on all collections from ECI operations, providing information/data on foreign exchange rates, processing request for payments of foreign remittances and the maintenance of a separate account designated as Premium Reserve fund in accordance with the terms of the Reinsurance Agreement with COFACE.

The interim organization treats the ECI program as another product along with PHILGUARANTEE's other existing program. This set up is considered most convenient and economical for PHILGUARANTEE since ECT operations are just in the start-up stage. In anticipation of the increase in volume of ECI business, the PHILGUARANTEE Board approved on June 20, 1997 the creation/expansion of the following units to strengthen organizational support for ECI.

1. Expansion of ECIO into a Department with two (2) Underwriting Divisions
2. Creation of Country Risk Assessment Division under ECSD
3. Creation of Visayas-Mindanao Division under MBDD

The Manager of ECI Department will report to the Senior Vice President for Operations.

III. TYPES, FEATURES, TERMS AND CONDITIONS OF INSURANCE

A. Types of Insurance Policies:

- a. **Comprehensive Short-Term Shipments Policy** - covers both political and commercial risks of non-payment of export credits with a term of up to 180 days from shipment date.
- b. **Commercial Risk Only Short-Term Shipments Policy** - where exporter's buyers are all in OECD countries or developed market/economies, a policy may be issued where only commercial risk will be covered.

B. Program Features

- a. Eligible for cover

Any exporter doing business in the Philippines provided that the exported goods and services contain at least 20% local (Philippine) content based on FOB value.

b. Insurable exports include:

1. Philippine exports denominated in an acceptable foreign convertible currency payable in the Philippines
2. Export sales on either documentary or open account term and involving firm contracts for payment up to 180 days from export shipment date.

c. Coverage

1. Maximum of 85% of the amount of loss
2. Global basis, meaning it covers all contracts with buyers covered under the Policy to ensure an acceptable spread of risks. Export sales on cash and irrevocable L/C may however be excluded.

d. Validity Period

The policy shall be valid for one (1) year from date of issue.

C. **Terms and Conditions**

1. Risks to be covered

a. *Political risks include*

- i. currency inconvertibility or transfer payment risk
- ii. foreign government acts which prevent the importation of the goods;
- iii. cancellation of previously issued import licences; and
- iv. war (including civil war), riot, rebellion, revolution, insurrection or other similar disturbances in the buyer's country

b. Commercial risks include:

- i. insolvency of the buyer;

- ii. protracted default or delay in payment i.e. failure of the buyer to pay the exporter the gross invoice value of goods delivered to and accepted by the buyer.

2. Exclusions

- a fluctuations in exchange rates
- b where other insurance coverage applies such as fire and marine insurance
- c insolvency or default of an agent of the exporter or of any bank
- d contract of sale to insured's affiliate
- e non-payment due to sales contract disputes between the exporter and overseas buyer or where either the exporter or buyer commits a breach of any term of the contract covered by the policy
- f cases where the insured exporter authorizes payment in a currency other than the currency stipulated in the contract
- g cases where the insured exporter has entered into a compromise agreement without PHILGUARANTEE's written consent
- h natural catastrophic risks and the nuclear risk
- i war between any of the world's major powers and between the country of the insured and of the buyer.

3. Limitation of Liability

- a. **A Buyer Credit Limit (BCL)** is the maximum amount of credit that can be extended to a particular buyer at a given time based on credit information obtained on that buyer and on underwriting guidelines. However, the BCL shall not exceed a Single Buyer Credit Limit (SBCL). The SBCL shall be set at one percent (1%) of the ECT Program Capital on a leveraged basis. Single buyer shall also mean buyers controlled by the same ownership group. In case there is reinsurance, the SBCL shall be adjusted accordingly depending on the percentage of retention.

- b. **Maximum Liability** is the maximum amount that PHILGUARANTEE shall pay, in the event of loss, to the exporter for all buyers under the Policy. This shall be a certain multiple of the premium paid.

D. **Premium Structure**

A premium shall be computed based on the gross invoice value of goods shipped. The applicable premium rate will depend on the country classification schedule grading credit terms, and underwriting guidelines.

A minimum non-refundable premium shall be paid in advance, computed on the basis of the exporter's estimated export sales at the time of application. Subsequently, the actual premium shall be computed based on submitted monthly exports of actual shipments. If the actual premium is higher than the minimum premium, the difference shall be paid to PHILGUARANTEE at the end of the quarter.

There is also a processing fee to be paid by the exporter. The cost of obtaining credit information on the foreign buyer is likewise passed on to the exporter.

IV. **PRODUCT DEVELOPMENT, PROMOTION AND MARKETING**

A. **Product Development**

- June 30, 1995 World Bank approved the grant from Japan Export Development Project for the Export Credit Insurance (ECT) and Comprehensive Credit Information SYSWM (CCIS) projects
- August 1995 and Training on ECI fundamental (USA)
March 1996 and trade and investment insurance (Japan) for PHILGUARANTEE officers
- January - April 1996 ECI Market survey
- July 1996 Consultancy work m ECI and CCIS started
- August 1996 ECI supplemental survey (large/traditional exporters and foreign banks)
- September 1996 Consultancy Report on ECI submitted

- November 1996 Training on ECI by ECICS Singapore
- December 1996 Consultancy Report on CCIS submitted Training in COFACE, France
- December 27, 1996 PHILGUARANTEE Board's approval of implementation of ECI
- January 31, 1997 Launching of ECT and Signing of Partnership including Reinsurance Agreements between PHILGUARANTEE and COFACE

Upon securing the funding for the ECT and CCIS projects, an ECI Project Committee was created which acted as the local counterpart of the foreign consultants hired to conduct the studies.

All tasks undertaken on the ECI is being coordinated by the Committee from its planning up to its launching and implementation. Its task is still continuing since the ECI program is still in its interim stage until PHILGUARANTEE is able to deliver a comprehensive ECI facility.

Its on-going tasks include:

1. Coordination with COFACE, France on matters regarding Partnership, Reinsurance Agreements
2. Monitoring of the interim ECT facility particularly on how the existing structure/organisation is able to respond/deliver services to exporters
3. Formulation of staff development plan, including identification of training needs/courses on ECI management and operations
4. Design and development of a computerized system to manage the limited facility, including software and hardware requirements with provision for expansion to handle a larger ECI facility
 - a. Management Information System Local Area
 - b. Networking of the Operations Group to integrating all database to be used for all PHILGUARANTEE products
 - c. Database for CCI S - exporters data and foreign buyers' access
5. Formulation of an interim business plan
 - a. determine and set-up of reserve fund/capitalization
 - b. financial budget requirements to operate the limited facility
6. Formulation of a marketing and promotions plan

7. Monitoring of ECI operations to assess/determine probable default rate and risk percentages
8. Review of the insurance policy itself

B. **Promotion and Marketing**

• **Objectives**

- a. To increase awareness among exporters on the features and benefits of the ECI
- b. To solicit clients/policy holders for ECI
- c. To enlist the support and acceptance of the ECI from existing and new PHILGUARANTEE exporter-clients
- d. To establish PHILGUARANTEE as the first and only institution to implement an ECI facility in the country
- e. To ensure the viability of ECI operations in PHILGUARANTEE.

Marketing activities are aimed at informing end users on the features and benefits of the ECI. The long term marketing goal is to establish ECI as an effective facility for exporters. At the macro level, ECI is projected as a means to attain increased productivity in the export sector and to secure them in the global market. We therefore emphasize the gains experienced by other countries where ECI facility was implemented and at the same time create an image awareness in the business community that PHILGUARANTEE is the national export credit agency (ECA) which provides a complete package of financial services to the exporters.

• **Marketing Activities/Strategies**

a. **Launching**

In order to meet the above objectives, the MBDD has drawn up its marketing plan and the ECI Program was launched as being the first of its kind in the country as a well-

publicized event Press from local newspaper, radio and television covered the launching which was held on January 31, 1997 to coincide with the 20th Anniversary celebration of PHILGUARANTEE.

b. Seminars/Conferences/Briefings

This is aimed to sustain the awareness generated by the launching of the program, such activities must be timed so as not to coincide with any major trade/export activity to achieve maximum coverage and participation.

ECI seminars/conferences in various regions of the country where most exporters in the countryside are located were arranged by Marketing staff. In all ECI seminars/conferences, PHILGUARANTEE officers were present to answer/respond to the queries from the exporters after each presentation.

Aside from exporter and trade associations, Seminars/briefings are also being conducted for bankers.

c. Primers/Brochures/Posters

Colorful, simplified and attractive primers/brochures containing features of the ECI program are prepared for distribution.

d. Advertisement

Advertisement in 2 or 3 widely read newspapers is one of the most effective ways of reaching a large number of exporters throughout the country. This is done at least every 6 months to maintain the visibility of PHILGUARANTEE, and to sustain the interest of exporters on the newly launched ECI program. Corporate sponsors shall be tapped to minimize costs. In addition, regular press releases will be issued to announce developments on the program.

e. Pro-Active Approach

The Marketing staff make personal calls on individual exporters and trade associations on a continuing and regular basis. This is viewed as an effective tool since during the meeting, details of the ECI may be further discussed to address certain questions of the exporter/association. Records of visits are kept on file for follow-ups. Those who have shown interest on the ECI program are being given top priority.

f. Others

PHILGUARANTEE also takes advantage of opportunities or occasions not included in its own program of activities, such as invitations to participate in, or sponsor, trade fairs, act as guest speakers or resource persons at conferences or seminars conducted by third parties, sponsorship in magazines or special newspaper supplements or press releases by other institutions/organizations.

V. UNDERWRITING PROCEDURES

The underwriting procedure basically covers the evaluation of the exporter's proposal/applications which includes information on the exporter, export product, and foreign buyer and the establishment of the appropriate premium rates and foreign buyer credit limits. Its objective is to determine whether there is reasonable spread of risk in the Portfolio of export business being offered. Below are the salient features of the underwriting procedure:

- **Processing of the Exporter Proposal/application**

In reviewing the exporter proposal application, the following areas are considered:

- ***Information on the Exporter***

Information needed to determine whether the exporter is acceptable for ECI which covers key questions on the company's general business status, experience, financial condition, and experience of PHILGUARANTEE and other banks with the exporter, if any.

- ***Information on Product and Foreign Buyers***

It is essential to know the products and services being exported and subject of coverage to determine whether it complies with the minimum requirement of local value content. Moreover, this is necessary because some products are inherently more risky due to such factors as short life cycle, potential for obsolescence or low resale value.

The underwriter determines whether the insurable risks being offered represent an acceptable spread of risk. This requires careful consideration of the level and terms of the current orders and overall proposed level of business to be covered, based on past experiences of the exporter with his buyers and markets involved.

- ***Determination of Premium Rates***

The following are the principal factors that determine the appropriate level of premium:

- Estimated volume of business
- Likely spread of business
- Likely level of Buyer risk
- Experience, competence and financial condition of the exporter
- Experience of PHILGUARANTEE with the exporter as insured policy holder
- Need to be competitive and responsive to the particular needs of an exporter

- **Establishment of Foreign Buyer Credit Limits (BCL)**

A credit limit for both the Comprehensive Shipments and Commercial Risks Only policies determines the maximum amount of loss that may be incurred for each buyer insured under the policy by PHILGUARANTEE.

Since PHILGUARANTEE has entered into a Partnership Alliance with COFACE of France and has joined the Credit Alliance Network, a credit information check on the COFACE, and

Credit Alliance Buyer Database will be made for appropriate prescriptive buyer credit limits. However, if PHILGUARANTEE finds it necessary, it may obtain additional credit information to guide its underwriting decision.

In setting or approving the BCL due consideration should be given to the Prescriptive BCL established by COFACE.

Below are some of the issues to be addressed in credit limit assessments:

- buyer's record of Payment of debts
 - record of the directors and management of the buyer in successfully managing the business
 - stability of the buyer's industry
 - exporter experience with the buyer
 - quality of the agency/bank reports
 - solvency or working capital position of the buyer
-
- **Foreign Bank Underwriting**

Credit risk of foreign banks is assessed when underwriting export sales calling for Irrevocable Letter of credit (ILC) payment terms. Usually, information obtained from the Banker's Almanac and other similar publications should be sufficient. In the assessment of banks as credit risks, relevant factors to be considered are size, ownership, financial standing or rating of the issuing bank with other banks, asset quality, liquidity, and capital adequacy.

An underwriting decision will be rendered as to whether the portfolio of business bang offered will be covered or not and on what terms. Thereafter, the Underwriting Unit will review the volume of shipments covered including comparison with projected activity, reassess the country and buyer risks, relate premium paid to projected levels when the policy was issued or renewed, evaluate the claims experience and comments on the policy holders conduct in declaring insurable business and paying premium. In addition, the Underwriting Unit review existing buyer credit limits and makes recommendation for renewal or change in the amount of terms, or cancellation.

VI. CLAIMS AND RECOVERIES UNDER THE ECI PROGRAM

Once the insurance policy is issued the exporter is required to submit his monthly declaration of shipments to monitor his performance under the policy.

Assuming that the foreign buyer fails to pay his obligation on due date, the exporter should file a Notice of Overdue Account (NOA) within 60 days from due date. The submission of NOA is requested by COFACE because this is being factored in the credit information Network so that other exporters would be approved of the status of those buyers who fail to pay on due date.

If the exporter finds that running after the buyer for collection is really negative, he should then file a Request for Intervention (RI) and Notice of Claim within 120 days from due date. Again this notice will be inputted in the Credit Information Network and this will adversely affect the credit that will be made available to the defaulted buyer. What follows after submission of the RI and Notice of Claim is the waiting period. For claims amounting to US\$30,000 and more, the waiting period is 5 months. For claims amounting to less than US\$30,000, the waiting period is only 2 months. During this period, PHILGUARANTEE with COFACE will conduct an evaluation of the validity of the claim.

In case of the buyers' bankruptcy or insolvency, the exporter can immediately lay claim on the insurance subject to the submission of the necessary documents.

Upon determination that the claim is valid, PHILGUARANTEE shall immediately indemnify the exporter within 30 days from end of the waiting period.

Once payment has been made, PHILGUARANTEE will be subrogated to the right of the exporter against his foreign buyer. Any recovery made by PHILGUARANTEE by virtue of the subrogation is shared *pari-passu* with the exporter. However, expenses incurred will also be shared *pari-passu*.

VII. PROGRAM SUPPORT

A. **Philguarantee/national Government**

The ECI Program is backed by the capital resources of PHILGUARANTEE. PHILGUARANTEE's charter (PD 1080) provides that all of its obligations are fully guaranteed by the National Government.

B. **Partnership Agreement with COFACE**

PHILGUARANTEE has entered into a partnership agreement with COFACE of France. Upon signing of the Partnership Agreement with COFACE simultaneously with the launching of the program last January 1997, PHILGUARANTEE became a member of the Credit Alliance Network.

Credit Alliance is an intentional network of credit insurers in the framework of partnership agreement. The partners pool their expertise, systems and financial capacities to provide their clients with protection for their commercial debt throughout the world, providing high quality service at reduced costs.

The coverage of the services available in the Alliance are access to credit information, reinsurance and debt collection overseas.

a. Reinsurance Agreement

Any risk monitored and controlled by COFACE can be included in COFACE, reinsurance. This allows each member of the Credit Alliance to avail of the reinsurance conditions negotiated as a package deal based on supply of high premiums and regularly positive underwriting results.

b. Management Agreement

Through this agreement on-line access to COFACE, credit information database and underwriting system through computerized linkage is made possible. Payment of fees depends on the location/country of the buyer file being requested. COFACE on its part

constantly monitors and updates information and credit limits applicable on the buyer file requested.

C. **Debt Collection**

As an added service to PHILGUARANTEE, COFACE shall make available its own debt collection services for claims filed against defaulting foreign buyers. PHILGUARANTEE may also avail of COFACES worldwide debt collection network, which involves a number of debt collection agencies and law firms in different parts of the world.

D. **PHILGUARANTEE's Credit Information System**

The Comprehensive Credit Information System (OCIS) is the backbone of the ECI Program.

Internally, a foreign buyers directory is being developed. This system is envisioned to derive information on foreign buyers as gathered from various sources (e.g. trade organizations / associations, other government agencies specially those attached to the Department of Trade and Industry). This information classifies foreign buyers by source, country and product group.

The corporation has set-up a Local Area Network (LAN) to increase efficiency in processing and monitoring of exporter accounts.

VIII. OPERATING RESULTS

To date, PHILGUARANTEE, still has to issue its first policy under the Program. A lot of interest by way of inquiries has been generated through the marketing activity; and we are just awaiting the submission of requirement by the exporters to be able to come up with the proposals.

There are five BCI applications removed so far which are in different stages of processing. These applications cover an aggregate insurable amount of P338 Million or approximately US\$12 Million.

PHLGUARANTEE expects to issue its first ECI policy in the next month or so.

Chapter IV

Trade and Investment Insurance System of Hong Kong

Hong Kong Export Credit Insurance Corporation

History

- Founded 1966 by the government of Hong Kong
- To foster emergence of Hong Kong as a world trader and producer
- To facilitate small enterprises entering export trade and protect against:
 - buyer bankruptcy
 - payment default
 - rejection of goods
 - war- 'political' payment blockages

INSURANCE POLICIES

- No. 1 - Comprehensive Shipments Policy
 - covers exports and re-exports
from the date of shipment

Also-covers Services.

- Freight Forwarding
 - Advertising-
 - Testing and Inspection
- No. 2 - External Trade Shipments Policy
 - goods made outside, Hong Kong and delivered direct to buyers
- No. 3 -“Tailor-made” Facilities
 - sales to local buyer for export
 - country risk only

- capital goods on terms up to 5 years or more

Hong Kong Export Credit Insurance Corporation

- Wholly owned by the Government of Hong Kong
- Guarantees ECIC's contingent liabilities
 - current limit HK\$ 7,500 million
 - [US\$ 1 Billion]

ECIC'S MISSION

- To encourage and support export trade through professional, customer-oriented services
- To develop a positive corporate culture devoted to excellence and quality
- Prompt, effective and comprehensive services to meet exporters' aspirations.

FINANCIAL RESULTS

(HK\$ Million)

| | 1996/97 | 1995/96 |
|---------------------|---------|---------|
| Net Premium Income | 81.3 | 74.66 |
| Net Claims | 42.65 | 29.94 |
| Operating Expenses | 54.43 | 51.48 |
| Investment Income | 29.42 | 33.95 |
| Result for the Year | 17.25 | 33.15 |

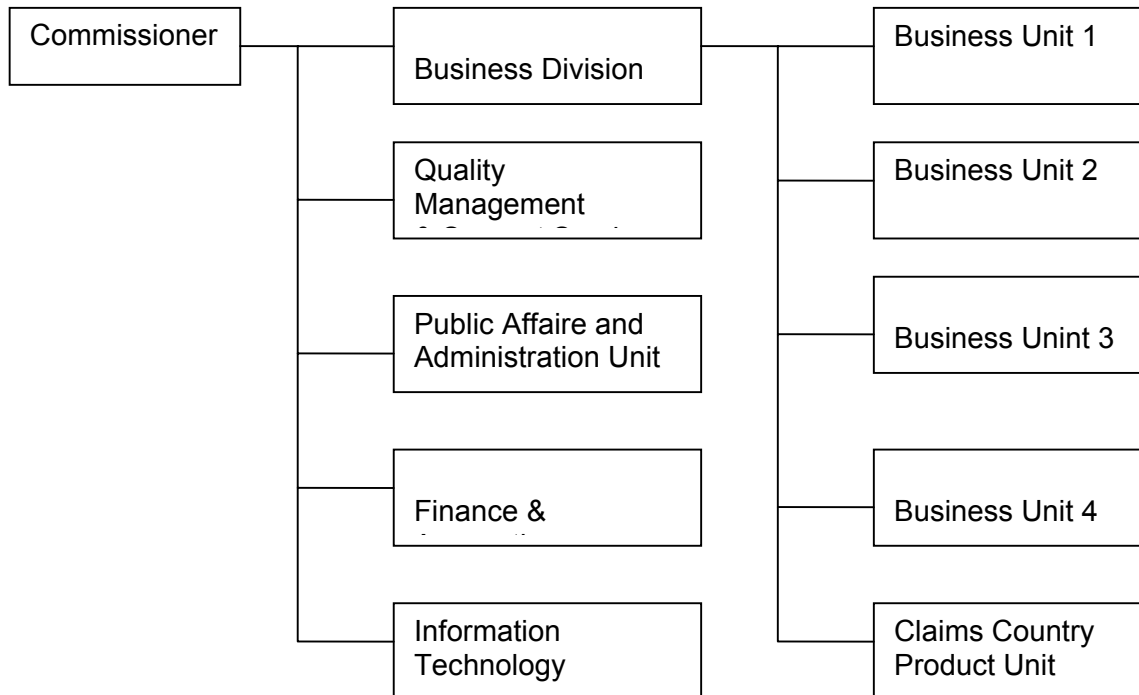
- 48% reduction in Annual surplus, due to
 - higher claims, especially in Germany and Australia
 - one large claim in China
- 14% increase in total business insured
 - HK\$ 20,11.3 million
 - result of targeted marketing

Increases to Asia, Latin America

North America, Latin America

- The Commissioner is appointed by the Government

The organization



Business Result

- Comprehensive Shipments Policy
 - provided 88% of total business
 - Increased by 13
- U. S. A. absorbed 33% - HK\$ 6,667 Million
 - increased 26%,
 - footwear, travel goods, electronics
 - Claims HK\$ 25,92 million [37%]

- U. K. took 17% - HK\$ 3,400 million
 - increased 11%
 - footwear, travel goods, appliances
 - Claims HK\$ 4.06 million [6%]
- Germany imported 11%, HK\$ 2,160 million
 - 3% Increase; cameras, optical, home appliances, travel goods
 - Claims HK\$ 6.15 million [9%]
- Australia took HK\$866 million - **4%** but created
 - Claims of HK\$ 5.76 million [8%]

Main Products Supported

| | |
|----------------------------------|-----|
| Clothing and Textiles | 29% |
| Toys | 12% |
| Plastic, Metal and Leather Goods | 11% |
| Electronics | 9% |
| Office Machinery and Stationery | 8% |
| Others | 31% |

- Premium income HK\$ 108.39 million
- Claims

| | |
|-----------------------------|---------------|
| Gross Claims (47% Increase) | 81.44 million |
| Recoveries | 5.7 million |

Product Development, Promotion & Marketing

- First step has been to develop a responsive, focussed Organisation
- Four Business Units established, each with
 - marketing
 - underwriting
 - risk management functions

- Means that one staff member can handle all client inquiries
 - more efficient
 - quicker
 - better communication

- Flatter Organization results in
 - smoother workflow
 - clearer definition of responsibilities
 - more direct communication
 - more initiative

- Targeting Prospective Clients
 - identify products with growth potential
 - garments, consumer electronics, componentry, PC & peripherals, watches and clocks, toys, gifts

- Liaison with Industry Trade Associations
 - Seminars organized
 - Specialized Databases-expanded -

- Similar strategy for Service Industries
 - Liaison with trade associations
 - for Freight Forwarding, Advertising,
 - Printing, Testing & Inspection.
 - Product development
 - Seminars held and Databases formed.

- Telemarketing used on a quarterly basis
 - followed up by quarterly visits

- Introduced Export Finance Insurance Policy for Banks since July 1996.

- Developed software to enable exporters to declare by diskette - to make their task easier
- Acquired software package for underwriting straightforward applications - to speed processing and ensure consistency
- to maintain the highest quality standards sought ISO certification.
 - Certified to meet ISO9002 in 1994
 - First ECA in the world with this.

Future Market Development

- Develop China as an insured market
- Provide new Comprehensive Policy Cover Policy for
 - exports
 - re-exports
 - third country trade
- Develop new Small Medium Industry Policy for companies with less than HK\$50 million turnover.
- Simplify the Confirming House Cover Policy
- Intensify Staff Training
- Everything is directed at better client service, simplification, reduction of paperwork and the administrative burden on clients

INSURANCE TYPE AND FEATURES

COMPREHENSIVE SHIPMENTS POLICY

- Whole insurable Turnover
 - exporter must declare all exports & re-exports on DP, DA & OA terms
 - only exceptions are 'Ineligible buyers'

- Risks Covered
 - * "buyer" risks
 - insolvency or bankruptcy
 - failure to pay
 - failure or refusal to accept delivery of contracted exports

 - * "country" risks
 - foreign exchange blockage
 - import bans
 - canceled import licenses
 - payment moratorium
 - war, civil disturbance, natural disaster

POLICY FEATURES

- Timing
 - 12 months cover with automatic renewal
 - unless canceled with two months notice

- Credit Limits
 - each buyer is given a 'revolving' credit limit

- Obtaining Credit Limits
 - application timing very Important
 - must apply in good time
 - should supply as much buyer Information as possible

- priority service is available at a cost
- ECIC does not reveal reasons for credit refusals -
 - observes strict confidentiality on all clients' business.
- Declarations
 - must declare all exports and re-exports with payment terms
 - cash against documents or documents against payment [DP]
 - documents against acceptance [DA]
 - open account [OA]
 - * must declare within 14 days of shipment date
 - or risk "no cover"
 - * details required
 - buyer name; country & code no.
 - payment terms
 - gross value in currency of invoice shipment date
 - country of origin
 - brief description of goods/services
- Omission of shipments will mean 'no cover' on the entire policy

Shipments must all be declared, but "over-limit" shipments only covered as earlier shipment payments received.

PREMIUM RATES

- Paid monthly based on shipments
- Level depends on countries, terms, goods, business volume, spread of risks, claims experience
- A Premium Deposit is held for the life of the Policy

PLUS - an Annual Policy fee for policy servicing costs

- based on usage

- Paying Claims
 - “event of loss” must be covered by the Policy
 - exporter has complied with policy terms and conditions
 - contract of sale has been properly executed

- Waiting Period
 - Insolvency / bankruptcy paid as soon as possible
 - protracted default 4 months after due date
 - repudiation: 1 month after re-sale
 - Transfer delays: 4 months after due date or of payment in buyer's own currency
 - all others; 4 months after the “event”

RECOVERY ACTION

- joint responsibility but ECIC can take full charge

- Comprehensive Contracts Policy
 - For general consumer merchandise, but effective from the date of contract
 - Covers pre and post shipment risk

- External Trade Shipments Policy
 - For exports and re-exports of consumer merchandise mainly from China, Macau to Western Europe, United States and the developed markets
 - Exports of non-Hong Kong origin goods from outside to a foreign buyer where the trader / policy holder is in Hong Kong

OTHER POLICY

Confirming House Policy

Confirming house pays the exporter on shipment and grants credit terms to the overseas buyer

- Comprehensive Services Policy
 - covers services rendered to overseas clients
 - ship repairs, conversions, aircraft maintenance,
 - engineering, architecture, consultancy, advertising, etc,

- Extended Term Policy –for consumer durable and light machinery, agricultural machinery, yachts, truck, etc.
 - effective from date of shipment
 - credit from 181 days to 2 years
- Specific Shipments Policy - capital goods and production equipment, ships,
 - oil rigs heavy equipment and machinery, cranes, etc.
 - effective for a specific shipment from date of shipment
- Specific Contracts Policy
 - As above but with risk commencing
 - At date of contract
 - as above but effective from date of contract
- Specific Services Policy
 - covers exports of services which involve medium/long term credit
 - effective for a specific contract

POLICY UNDERWRITING

- Task to determine whether the export transaction is acceptable.
- If it is, determine the basic terms and conditions
 1. The Proposal - supported by sufficient information to make a judgment on its acceptability
 2. The Proposer - must be in business in Hong Kong
 - bona fides very important
 - is his outlook long term?
 3. What volume and spread of business is expected?
 - certain products are more risky - staples are safest
 4. Exporter's experience and financial situation
 - strong, stable businesses attract better buyers, lower costs, less disputes.
 - In all cases exporter experience and business connections are important
 5. Financial Statements seriously needed
 - but often hard to get
 - his bank's attitude is the best indicator - try to establish the details
 - credit control system - as shown by overdues and bad debts a key signal
- Within a reasonable time the Underwriter must issue a quote or decline business - as politely as possible - with suggestions to make the business acceptable
- On accepting the quote the exporter must nominate the 'policy holder' and pay the fees.
 - copies of the Policies and the Policyholders Manual are then issued

POLICY RENEWAL

- Policies are normally allowed to automatically renew after twelve months unless
 - exporter is careless or dishonest

- falls to declare shipments, report recoveries
- has poor claims experience
- makes no declaration for two years

- To terminate ECIC must give two months notice
 - but only in case of serious problems
- Maximum Cover Liability
 - normally 1/3rd of estimated turnover
 - but not less than biggest shipment or \$500,000

- Discretionary Credit Limit
 - allows exporter discretion
 - permitted when exporter understands proper use of facility
 - up to a limit for each buyer

- Premium Deposit
 - approximately 1/12th of annual premium
 - with upper and lower limits

- Policy Fee
 - initially depends on the no. of-buyers
 - on **renewal** the no. of credit applications

PREMIUM RATES

- Matrix of factors
 - country grading
 - payments: DP; [DA - OA]
 - term - 60, 1 2-0, 1 80 days

- Adjusted initially for
 - spread of business [how many "A" markets]
 - type of goods, volume of exports
 - 'client experience and competence
- Re-adjusted after one year's experience
 - good performers receive rebates
 - poor performance can lead to reduced cover, higher premiums, or cancellation

BUYER UNDERWRITING

- Underwriter operates under constraints
 - time pressure
 - available information may be limited
 - even good information may be out of date

- Underwriting is a mixture of science and art
 - depends on feelings, educated by information and experience

- The Underwriter must decide!

- The approach must be as systematic as possible
 1. Is the product viable in the intended market?
 - what are market trends?
 - is obsolescence a problem?
 - is the exporter experienced?
 2. Seek very specific details on the exporter
 - request exact details needed, especially
 - creditworthiness - with history

- Enterprises and markets have many variations

- underwriter must assess them all
- and make a decision on time!

COUNTRY UNDERWRITING

- Exclusive responsibility of the ECIC Commissioner
 - advised by senior group
- Basis is annual review of country economic and financial status
 - supplemented by Berne Union
 - on payments experience twice yearly
- Sudden events and disasters require immediate reactions and adjustments of cover for future shipments
- Country gradings are A,B, C, D and "off-cover"
- Country limits can also be imposed in response to circumstances, either singly or for groups.
- Three broad categories of country limit
 - continuing growth
 - existing levels maintained but *no growth*
 - reducing levels of commitments

CLAIMS AND RECOVERIES

- When Payment Difficulties appear
 - minimize loss as quickly as possible

- protect the validity of the unpaid debt
- clarify the situation with the exporter
- if a breach of policy detected client must be informed

- Policy obliges the policy holder to minimize loss
 - must take all practical steps
 - notify ECIC Immediately when appropriate
 - after a delay of two months notify ECIC within 3 days

- ECIC cannot force the client to -act but may decline to pay a claim if his action - or inaction –has jeopardized ECIC's position

- ECIC must carry out a *MOST CAREFUL*- fact-finding
 - reasons for the claim
 - exact details of the non-payment
 - whether the policy covers the shipment
 - whether new orders are in hand
 - whether the goods are perishable or fashion change prone.
 - what is the country situation
 - is the client's bank involved
 - is that buyer status report up to date
 - what action has the client taken
 - what have others experienced with buyer

- After weighing this evidence ECIC must opt to seek more information, or urge exporter to follow the appropriate procedures for
 - insolvency
 - default
 - repudiation
 - transfer delay
 - import restrictions, cancelled import licenses , war,

- Insolvency
 - Is buyer clearly insolvent? Who is the receiver or liquidator?
 - register the debts with him

- ask the clients to protest bills for nonpayment/non-acceptance
 - recover the goods not accepted or delivered
 - consider local action/presence, by appointing
 - representative/staff visit as appropriate
- Default
 - protest bills as above
 - seek rescheduled payments
 - enlist debt collectors
 - if necessary ask local legal advice
 - have client complain to Chamber of Commerce
 - enlist agent and bank to exert pressure
 - if necessary ask for-legal action
- Contractual Disputes
 - alleged that goods not up to specification
 - alleged arrived too late, too soon
- ECIC will not pay claim until dispute procedures exhausted
 - but pressure to pay likely from client and his bank
 - ECICs Role - seek negotiation by the client
 - press for arbitration if available
 - If not, proceed to litigation [costs to client unless ECIC requested - then shared)
 - Meanwhile form opinion on whether buyer is at fault – evaluate whether it would be best to pay claim

Chapter VI

Trade and Investment Insurance System of P.R. China

1. Brief Review of the History of Trade & Investment Insurance in China

The present international market is full of intense competition. To increase the competitiveness of exports, encourage export and foreign investment, stimulate the domestic employment and promote the economic development, most countries make use of the Officially Supported Export Credit System. China is no exception.

The Trade & Investment Insurance, as an international custom to promote exports, was developed gradually in China with the establishment of the Market Economic System. Generally speaking, it underwent three phases:

Phase 1. Starting from the late 1970s, China began to reform the economic system and adopt an open door policy. To solve the contradiction of economic development and shortage of funds, China began to make use of export credits extended by the foreign countries to import the badly-needed advanced technology and equipment while attracting the foreign investment in big volume. This was proved quite successful and efficient. During this time, it was also realized that China should provide its own export credit to encourage Chinese export to earn more foreign exchange so as to hasten the steps of its reform and modernization. Then at the beginning of 1980s, Chinese government instructed Bank of China to initiate its own export supplier credit. This was a medium and long-term RMB loan facility with preferential interest rate, which is mainly used to encourage export of capital goods. This showed that China had made its first step to the establishment of its own export credit system.

Phase 2: With the expansion of export and supplier credit, people had come to realize that it was not enough to provide merely low interest rate credit. In order to promote export, there was also a need of export credit insurance. At the beginning of conducting supplier credit, insurance was not considered. As a matter of fact, exporters who were financing by supplier credit were obliged to repay the principle and interest according to the loan agreements, no matter whether they could receive the payment from the buyer. That means it was the exporter who undertook the risk of nonpayment. That became an obstacle to the further development of export. After a period of probing and practice, China became aware of the need to set up a system of export credit insurance. The People's Insurance Company of China (PICC) at that time, which was the only insurance company in China, was entrusted by the government to start writing export credit insurance as from Jan. 1, 1989. In the following years, short term export credit insurance was introduced throughout the country. The government took measures to support the operation of export credit insurance and granted many preferential policies, such as exemption from premium tax and provision of funds. The introduction of export credit insurance symbolized that China's export credit system was standing on the two legs, i.e., finance and insurance although they were not coordinating very well at that time. However, it was possible for the Chinese exporters to be protected against non-payment risks through their paying of premium.

Phase 3: In 1992, after the government adopted the multi market of export strategy and Bank of China started buyer credit financing, export credit insurance was paid more and more attention to. From its very beginning, buyer credit in China was incorporated with an insurance mechanism. Risks were born by the insurer and ultimately born by the government, and since then the Chinese exporters could enjoy a credit facility with no or limited recourse. For the purpose of the formation of the socialist market system, the government laid down the

policy to separate policy-oriented financial activities from commercial financial business. It simultaneously announced the commercialization of the four specialized state banks and the founding of three policy banks. China Eximbank is one of the three.

2. The present situation of China's trade and investment insurance

1. Through nearly 10 years of development, China has made rapid progress in the trade and investment insurance. According to statistics, 33 branches of PICC are now writing export credit insurance. In 1989, the insured amount of PICC was only 100 million US\$. 1994 saw 1.4 billion US\$ insured amount. In 1996, PICC underwrote a total of US\$ 1.08 billion, of which US\$ 0.71 billion was short term credit insurance, US\$0.37 billion was medium-long term credit insurance. In addition to that, China Exim Bank in 1996 underwrote US\$0.6 billion, 275% increase over 1995, and had a premium income of US\$6.5 million, 206% increase over 1995. At present, the export credit insurance has been carried out throughout the country and has become a vital tool to encourage export.

2. Improvement has been made in regulations, techniques and the variety of covers increased. The main covers include short term comprehensive export credit insurance, short term specific export credit insurance, medium and long term (deferred payment contract) insurance, contract frustration insurance, buyer credit insurance (guarantee), export bill insurance, overseas investment insurance etc. Also, the markets covered widened with the implementation of the multi-market strategy. At the same time to consolidate the markets in Europe, the United States, Japan and Southeast Asia, we have begun to expand our businesses to East Europe, the Middle East, Latin America and Africa. In addition, in line with the actual situation of export development, more and more products are covered besides machinery and electronic goods.

3. We strengthened cooperation with ECAS, private insurers and brokers all over the world. From the outset, the Chinese export credit agencies received assistance and learned a lot from them. Bilateral visits and exchanging of expertise have occurred. The agencies which helped us and provided training to us include ECGD, COFACE, US Exim Bank, EDC, EID/MITI, JITO, ECIC, KEIC, etc. In 1996, PICC joined Berne Union and became an observer. In accordance with the government's arrangement, the export credit insurers in China should enjoy a common membership and joint participation and share in rights and obligation in Berne Union meetings and activities

APEC -Trade and Investment Insurance Training Program is a grand event of cooperation between China and the world.

3. Institutional Framework and Organizational Set Up

At present, there are two organizations underwriting trade and investment insurance, China Exim Bank and PICC Property. The latter began to write export credit insurance earlier than the former.

In 1994, with the deepening of financial system reform, China began to separate the policy financial business from the commercial activities. Under such circumstances, China Eximbank was set up, with a registered capital of RMB 3.38 billion appropriated from the state treasury. It carries out the state industrial and foreign trade policy, provides the financial policy for the export of machinery and electronic products and complete sets of equipment. It adopts much experience from the international custom. The Board of Directors, responsible for all the activities, is just like an Inter-Ministerial Committee. It is composed of the principle ministries such as the Ministry of Foreign Trade and Economic Cooperation the State Economic and Trade commission, the Ministry of Finance, the State Planning Commission, the Ministry of Electronics Industry, Bank of China, the State Commission of Science, Technology and Industry for National Defense.

The establishment of China Exim Bank marks the termination of a history that China had no special export credit agency, a step forward towards the system of internationalized export credit support and an establishment for the improvement of Chinese export credit insurance. At present it has four functions:

1) Export finance. This includes both buyer credit and supplier credit. The former is in the currency of US Dollars while the latter both in US Dollars and RMB.

In 1996, it approved supplier credits to finance 156 projects totaling RMB12.83 billion and US\$41 million, of which RMB10.7 billion and US\$27.1 million were disbursed. By the year end, the RMB loans outstanding were twice that of 1995. The Bank, also provided US\$12.027 million in buyer's credit for two projects on a trial basis. The credits supported a total of US\$4.3 billion worth of export with emphasis on high-tech and high value-added large mechanical and electronic products and complete sets of equipment. The loan structure was optimized and the credits were well used. The Bank contributed greatly to the nation's betterment of export composition.

2) Export credit insurance and guarantee. Insurance facilities include the short-term, medium and long-term export credit insurance. In 1996, there was a rapid growth in export credit insurance. 84 transactions were covered under export credit insurance with an insured amount totaling US\$610 million, and 49 foreign exchange guarantees were issued amounting to US\$320 million. The combination of export, finance and export credit insurance supplied good-quality service for the exporters and helped reduce the cost of finance. Yet, it must be noted that China Exim Bank was born in the reform of economy and financial system, and a certain period of time is needed to coordinate its relations with other agencies concerned. At present the export credit insurance system in China is still in a transitional period.

3) On lending foreign government's preferential loans to Chinese Enterprises In 1996, the Bank newly approved to on lend US\$1.8 billion to 53 projects, and the outstanding reached US\$15.534 billion. The number of foreign government loan providers increased from 8 countries and 1 bank of the previous year to 14 countries and 1 bank. The newly approved projects mainly focus on introducing advanced technologies and equipment so as to support infrastructural construction and improve investment environment.

4 Chinese Government's Concessional loans. Our bank firmly carried out the State Council's policy on the reform of China's foreign aid program. In the past this kind of loan was in the type of free grants, which was now changed to the present situation to cater for the foreign aid reform. It successively signed 9 agreements on Chinese government concessional loan projects including the Huake Automobile S.A. of Cote d'Ivoire in the amount of RMB850 million. Geographically, the projects are mainly located in the developing countries such as Sudan, Kenya, Botswana and Gabon, etc. The concessional loans involve the fields of oil exploration, forest felling, gold mining, fishery processing, automobile assembly, railway renovation, textile, pharmacy, etc.

4. Marketing and Products

Although as a policy-oriented bank, China Eximbank attaches much importance to marketing. As a new bank established only 3 years ago, some exporters even know little about us. Medias were used such as TV, newspaper etc. Seminars were often held with exporters to help them know more about export credit insurance.

In addition to that, frequent visits are indispensable. We often visit the potential policyholders and help them to be aware of their risks when trading with the foreign counterparts. After the policy has been issued, frequent visits become more important. Especially for the short term comprehensive insurance. We need to instruct the policyholder on the right procedures, how to apply for the credit limits, how to declare shipment, what to do with probable loss. This kind of exchange helps to create the friendly atmosphere and trust between the two parties. Sometimes, the insured can get more clients for the insurer. Some businesses are introduced by commercial banks who provide financing for the exporter.

The covers we can offer so far are the following:

1. Short Term Export Credit Insurance. It covers the exporter against the nonpayment risk including both the commercial and political risks under the contract with credit term not exceeding 180 days, in special cases not more than 1 year. It's a cover on specific contract and the exported goods are limited to machinery and electronic products. It's often connected with supplier credit. That is, the financing bank, when the payment term is of non-LC, will often demand the exporter take out this insurance which will be used as a collateral of finance.
2. Short Term Comprehensive Export Credit Insurance. It is a multibuyer protection, which covers the exporter against the non-payment risk under the contracts which fall into the application of the policy. The products exported are not limited to machinery and electronic products, the consumer goods such as the textile, electrical items can also be covered. With this policy, the exporter can get the easy access to finance.

3. Medium-Long Term Deferred Payment Insurance. It is similar to the first category except the credit term is 1 year or more.

4. Overseas Investment Insurance It covers Chinese investors against the expropriation, war, restriction on transfer arising during the course of investment in the foreign countries.

5. Contract Frustration Insurance The main propose of this insurance is to provide pre-shipment cover. For high-value contract under which goods are not standard but specially made, the importer's frustration of contract before the shipment of goods will cause great losses to the exporter if he has input a lot of money during production period. For instance, it is applicable to shipbuilding contracts with progressive payment terms. Sometimes post-shipment risk is also covered.

6. Buyer Credit Insurance (guarantee) It covers the financing bank which provides the buyer credit to the foreign buyer or foreign bank against the non-repayment risk. The insured amount is 100% of the principal and the accrued interest.

5. Underwriting technique

The underwriting procedure is composed of the three parts:

1) Policyholder risk underwriting.

Three aspects will be looked at:

Volume The potential policyholder's export volume, its markets, buyers etc.

Spread The composition of its main markets and buyers, business concentration etc.

Quality This includes its internal credit control, its past overdues etc.

According to the above factors, potential policyholders will be rated in different categories and different premium rates will be applicable to the corresponding policyholders respectively.

2) Commercial risk underwriting

Commercial risk is the one involving the buyer itself. Before we commit ourselves to underwrite, it is very important to have the information about the buyer such as the starting

year, past business experience, capital, sales and other main financial information. Generally speaking, we will look at the following aspects on the buyer:

- History When the buyer started to do business, its payment record.
- Financial standing. Such as the registered and paid-up capital, sales, profit. Important ratios such as quick ratio, current ratio, debt ratio will be calculated in order to help analysis.
- Business management, such as business experience of the directors , their personal history
- Market trend of the product. Whether the product is going to be out of date or vs it traditional one.
- Development trend. Is the buyer going up or down? This is quite important to make credit decisions.
- Based upon above, the underwriting decisions will be made as to whether to cover, if yes, how much our commitment will be, the percentage of indemnification and special terms and conditions.
- After issuing of the policy and credit limit, we will keep a close watch on the progress of the buyer. In case of any negative change we will inform the exporter and amend the policy terms and conditions.

3) Country Risk Underwriting

The following aspects will be looked at:

- The political and social situation of the subject country, such as political stability, policy longevity, ability to implement policy, social order.
- The economic situation of the country, such as GNP amount, economic growth rate, inflation rate, unemployment rate, fiscal deficit, balance of payment, foreign currency reserves, its dependency on the international economy, etc.
- International relationship. Such as the relationship with the international organizations, with its neighboring countries, esp. with China, whether there is a possibility of war.
- Different countries are rated by 4 categories according to above factors. For medium and long term insurance we have 8 country categories. This will be adjusted regularly once a year and subject to change upon occurrence of emergency.

6. Claims and recoveries

Until now, the claims lodged with us have been very little. So we are not quite experienced in this area.

7. Support system

Information

Information is very important to export credit insurance underwriting. To have a quick access to information an on line D & B information service is needed. Most of the buyers' information can be obtained in seconds. We also have business relationship with other status agencies in different countries.

For the country information, we often accumulate the important information from the newspaper and other public media. The Ministry of Foreign Trade and Economic Cooperation and Chinese embassies in foreign countries are also important resources of information.

Reinsurance

It is not easy for a national program to be supported by private reinsurance market at an acceptable cost. So far our insurance exposure does not have any reinsurance

From the above, you can see that we have made a lot of achievements. Yet we still face some problems. It can be noted that the need for trade and investment insurance in China which is the world largest developing country is far from satisfied in view of its rapid economic development. The insurance volume only accounts for less than 2% of the total export, far behind the average of the world. The exporters insured accounts for 2.7% in number. There are a number of reasons behind that.

(1) Lack of insurance consciousness.

Due to historical reasons, most exporters in China are the state owned companies. Generally, people there tend to have little consciousness of the trade and investment insurance.

From 1949 to 1978 before the economic reform, China was under the centralized planning economy strictly controlled by the central government. All the losses of the enterprises were born by the state as a whole. The annual export-import plan was transferred to the Ministry of Foreign Trade through the state planning commission, and then to be divided into a few professional export-import corporations. The risks during the transition were born by the government and the foreign exchange earned by them could only be submitted to the government. Though facing a highly risky international market, the exporters did not feel exposed to it at all. It was the reform, which made the enterprises the real independent entities but history still has influence upon the present.

Comparatively commercial insurance including cargo insurance and life assurance have been recognized and accepted, but export credit insurance, as a brand new and very special insurance from other commercial insurance, doesn't become so popular. Many Chinese trading companies even have not heard of it. They often confuse it with other commercial insurance.

Some Chinese export & import companies think that it is not worthwhile to buy the export credit insurance. They believe the premium outgo will increase their cost of export and decrease their profit ultimately. They ignore the fact that should they get no payment, the loss will need to be reimbursed by more sales volume, which is more difficult in the present intense competitive market.

Thus, Chinese export credit insurers will have tough task of propaganda to make more people know about this special insurance.

(2) Lack of expertise of the export credit insurance.

The history of trade and investment insurance shows that it developed from the domestic credit insurance. Before export credit insurance came into being, there had been a lot of good preparations for it in terms of personnel, information, underwriting techniques etc. But it's different in China. China has never had domestic credit insurance. The sources it could learn from were the foreign counterparts and other related insurance such as cargo insurance. Compared with its foreign counterparts, China couldn't meet the demand. as it doesn't have the data base on enough foreign buyers, doesn't have the expertise.

Also, the trade and investment insurance is a policy business which should be financially backed by the government. To meet potential claims, the government should appropriate the special fund to cater for the demand. As China is not a rich country, the limited financial resource becomes a constraint of capacity to cover more risks and more markets especially in the large number of developing countries.

At the 14th session of the Chinese Communist Party, China put the social market economy as its reform aim, which demanded the framework of the social market economy, be set up at the end of this century. Under such system, the boundary between the state and enterprise's interest must be clarified. China is now further deepening its foreign trade system reform. When the enterprise can really become the principle of the market economy, that is, to be responsible for its own operation, and the capital fund system are set up, the interest between the state and the enterprise can be defined. This will generate the demand for the protection of the non-payment risk existing during the course of trading.

At present, there are several hundred million US dollars overdue accounts and losses suffered by exporters. This indicates that export credit insurance in China is still at an initial stage, on another hand, it shows there is a great potential of development. In the long run, it can be safely predicted that, trade and investment insurance in China has a brilliant future though China has a long way to go to catch up with the advanced level.

For that purpose we think the following problems should be solved:

1. Attach more importance to draft and promulgation of LAWS ON EXPORT CREDIT INSURANCE and EXPORT IMPORT BANK including ordinance and regulations, in order to clarify the relationships between export credit agencies and other government agencies concerned. These laws will spell out the legal status of the export credit agencies and lay down the basic policies of export credit.
2. Coordinate the relationship between export credit insurance and export credit finance; combine the two functions on the basis of government's industrial and foreign trade policies. To make export credit insurance the pre-condition of export credit finance.
3. Set up our own system of credit risks assessing. We are now too dependent on outside information agencies. We have not built up our own database. It is necessary for us to have

our specialized team to gather and collect all information including that from overseas embassies and to set up information network and data bank by using electronic technology. By doing so, we can have more reliable and more cost effective information in our decision making.

4. Train and cultivate personnel in this field. The shortage of specialized personnel in this field has been the bottleneck for the development of credit insurance. Two trainings we should pay attention to: to train exporters and enhance their risk consciousness by offering credit insurance courses. Secondly, to train our insurance staff We should stick to the principle of "GOING OUT AND INVITING HOME", strengthen exchanges with established export credit agencies through lectures, seminars and training programs, to learn from the outside world.

Ladies and gentlemen, this training program is unprecedented in such a wide and deep aspect. I hope, such program could be held more frequently which is certain to benefit the ever increasing demand of trade and investment insurance in the APEC regions.

Thank you very much.

Chapter VII

Trade and Investment Insurance System of Indonesia

CHAPTER VII

PART 1

EXPORT CREDIT INSURANCE SYSTEM IN INDONESIA

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EXPORT CREDIT INSURANCE SYSTEM IN INDONESIA

I. INTRODUCTION

ASEI is a state owned export insurance company entrusted with the mission of promoting growth of non oil-gas exports. To accomplish this mission, ASEI endeavors to provide high quality services to its clients.

As we approach the upcoming era of free trade, experts in international trade are urgently needed. ASEI has trained human resources to face this challenge by placing key personnel in international institutions in other countries to gain valuable experience and thus steadily improve ASEI's business performance.

II. A BRIEF HISTORY OF EXPORT CREDIT INSURANCE

In an effort to encourage the increase of non-oil and gas exports, in 1985 the government of the Republic of Indonesia established PT. Asuransi Ekspor Indonesia (ASEI), a state owned company which provides Payment Insurance and Guarantee.

The export credit insurance program in Indonesia was proposed by a team from the Ministry of Trade in 1982.

The program was based on the consideration that export growth could be promoted by adopting various terms of payment prevailing in international trade practice, instead of limiting sights to L/C terms for Indonesian exporters.

The role of export credit insurance has become more important along with the growing export activities of small and medium scale exporters of non-traditional products to high risk export destination countries. The tougher competition and the changed world market patterns from seller's to buyer's market make such facilities even more important. In such condition credit payment terms are necessary to strengthen the competitive edge in order to win contracts.

In most developing countries each country has only one export credit insurance institution supported by the respective government, due to its specific characteristic i.e. high risk coverage, especially for political risk element.

III. INSTITUTIONAL FRAMEWORK AND ORGANIZATIONAL SET UP

Following the ordinary course of general insurance business practice in Indonesia, ASEI operations are made in line with the insurance principles and the prevailing government regulations.

III.1. ASEI STATUTES ARTICLE 3

Concerning its objectives and field of businesses, and the Ministry of Finance decision at the annual stockholder meeting on ASEI's budget and work plan of 1993, dated february, 1993 approving business development plan.

1. OBJECTIVES:

To support government policies and programs in national economic development in general, and in particular to expedite the smooth implementation of non-oil and gas export expansion program.

2. To achieve the above objectives, ASEI implements the following business activities:

- a. Providing insurance coverage against the risks of foreign importer default in payment for goods and services exported by an Indonesian exporter.
- b. Providing guarantee against the risks of payment default by an exporter / debtor who received export credit from a creditor / bank or other financial institution.

- C. Carrying out other efforts in insurance or guarantee business to support national development programs in the non-oil & gas export.
- 3. Establishing business or such other profit making activities related to the aforementioned field of businesses.**
- 4. Developing the existing business lines vertically as well as horizontally.**

111.2. ORGANIZATION STRUCTURE

Organization Structure of ASEI can be seen in Annex A.

IV. TYPES, FEATURE TERMS AND CONDITIONS OF INSURANCE

IV.1. TYPES OF PRODUCTS AND SERVICES

All systems of export payment, including sight letters of credit, entail a certain amount of risk. Not all banks conform to international banking regulations, and on top of this there is always the risk of bank failure, or political instability in the nations where banks extending letters of credit are domiciled.

As well as having to rely on their own capabilities, exporters must take measure of the credibility of the importers they deal with. They must also have a firm grasp of the intricacies of international trade, the development trends of the commodities they trade in, the political and economic conditions of their country of export destinations and payment systems used in the importing countries.

ASEI, with a comprehensive line of services and facilities, is prepared to help minimize the possibility of loss due to default in payment. Products and Services include

1. EXPORT CREDIT INSURANCE

Covers the losses incurred by exporters, due to the failure to receive payment from foreign

importers. This includes payment on their goods or services provided by Indonesian exporters. The types of policies and services include

- Comprehensive shipment policy
- Comprehensive Contract Policy
- Political Risks Policy
- Letter of Credit Policy
- Consignment Policy
- Specific Contract Policy
- Specific Services Policy
- Bond Guarantee Policy
- Unconditional Guarantee Policy

2. EXPORT CREDIT GUARANTEE

Covers the losses incurred by the non-payment of export credit obtained by debtors from banks or other financial institutions.

3. FACTORING INSURANCE

Is extended to factoring companies, and covers the losses incurred when claims previously bought up by factoring companies go unpaid because of default by debtors.

4. CUSTOMS BOND

Is a tripartite agreement. First party (surety company or guarantor) provides a guarantee to the second party (principal or exporter-producer) for the benefit of third party / obligee / Bapeksta (Government Authority under the Ministry of Finance that facilitates import tax exemption, suspension or reimbursement).

The guarantee covers non-collectible risk of import tax, sub-charge (if any) and value added tax, that should be paid by the second party to the third party, as stipulated in the prevailing law and regulation.

Such risk is related to possibility that the second party is unable to pay his/her obligation related to the imported material used for export purpose that enjoy the import facility, due to production and / or export failure.

IV.2. FEATURES OF PRODUCTS AND SERVICES OF ASEI

ASEI products and services are developed to provide a wide range of benefits to its clients, among others, as follows :

- I To provide protection for Exporter and/or Banks against commercial risks and/or political risks. Such risks are reflected in the possibility of loss resulted from the failure of credit repayment from Importer to Exporter, and/or from Exporter to creditor/Bank.
2. To accelerate fund mobilization by increasing the liquidity of Exporter and/or Banks through insurance coverage, indemnification payment, and/or Bank discounting, thereby guaranteeing the solid financial standing of the business.
3. To provide information ("Business Information Service") on importers, overseas banks, as well as updates on the economic and political conditions of trading counterpart countries, hence reducing the possible risks for the exporter.
4. To strengthen the competitive edge of Exporters and/or Banks by utilizing credit payment terms insured by ASEI which in turn facilitate penetration to new export markets.
5. To assist exporters in obtaining settlement of export receivables from overseas importer so that risks of export loss can be cut down.
6. To serve as catalyst in fund mobilization to support national economic development as well as maintain the results.

7. To support non-oil and gas export expansion programs the role of export credit insurance becomes more important along with the growing exports activities of small and medium scale exporters of non-traditional products to high risk export destination countries. The tougher competition and the change of world market pattern from seller's to buyer's market make such facilities even more important. In such a condition credit payment terms are necessary to strengthen the competitive edge in order to win purchase contracts.

V. PRODUCTS DEVELOPMENT, PROMOTION AND MARKETING

V.I. PRODUCTS DEVELOPMENT

ASEI performance in 1995 included an increase in liquidity from 225.73% in 1994 to 265.06% in 1995. The solvency ratio also rose from 256.12% in 1994 to 301.92% in 1995. Rentability also improved from 19.43% in 1994 to 21.35% in 1995. Other Financial Highlights can be seen in section Operating result in the last section.

In 1995, insured export commodities varied, ranging from primary commodities to manufactured goods in line with the structure of Indonesian exports. In 1985, only 14 Commodities were covered by export credit insurance. However, by 1995, export credit insurance was available for 82 commodities. The export commodities most commonly insured include fish, coffee, textiles, garments and plywood.

As we approach the upcoming era and in facing the current globalization / free trade era, Indonesian businessmen must improve their competitive edge, to accommodate the need for protection, we provide new products and services for future development include:

1. COUNTER GUARANTEE OF BANK GUARANTEES

Cover against the risk of the beneficiary drawing on a bank guarantee because of breach of contract by the applicant.

2. OVERSEAS INVESTMENT INSURANCE

This insurance is provided particularly for investment in foreign countries related to Indonesian export operations. Political risk insured in this insurance scheme consists of the possibility of investment nationalization by the host country government, and the implementation of tight foreign exchange control. Such insurance policy is provided for a maximum period of 20 years.

V.2. PROMOTION AND MARKETING

For promotion and marketing, ASEI has two branch offices in Surabaya and Medan and one head office in Jakarta. So with the ASEI's existence in a few places in Indonesia, ASEI hopes that it can be reached better and to cover all of Indonesia.

The marketing system in ASEI is also supported by marketing cooperation with other departments and institutions, government or private, that have branch offices in all areas of Indonesia, such as the Department of Trade and Industry, BPEN, DPE, Sucofindo, many Banks etc., so we expect that ASEI marketing can reach in all areas of Indonesia.

ASEI also has taken the standard procedure for promotion and marketing, such as marketing with telephone, letter, fax, direct visit, presentation to almost all institutions that relate to exporters, such as exporters, banks, and trade associations, etc.

ASEI also participates in many activities concerned with exports, such as seminars, workshops, trainings etc. whether as a trainer, speaker or through financial support. ASEI is

also active in advertising the ASEI's products and Services in News papers, and any other advertising methods.

Consequently, we expect that our clients, users, business community and the general public will have knowledge and be familiar with ASEI's products and Services and they will avail themselves of ASEI products and services in the interest of promoting non-oil gas exports and national development.

VI. TERMS, CONDITIONS AND PROCEDURES OF INDONESIA EXPORT CREDIT INSURANCE

Since the issuance of Government Regulation No. 1/1 982 dated January 16,1982 export payment terms have been fundamentally broadened from either in cash or credit guaranteed by L/C (sight L/C, usance L/C) to various terms that are commonly used in international trade practice.

Each payment term bears different level of payment settlement risks. The risks are caused by among others, long credit maturity terms, complex requirements, time consuming administration procedures and difficulties to monitor respective importer activities abroad.

Therefore, it is a prerequisite for Exporters to understand more than merely their own capability. They should also be well informed about respective importer credit worthiness, international trade practices, trend of respective export products as well as economic and political situation of the payment origin or export destination country.

Considering the above conditions, ASEI offers Export Credit Insurance policies which cover various commercial and non-commercial risks. Those policies are directed toward the "whole turnover basis" i.e. all export transactions of the Exporter concerned should be insured in order to distribute the risks more evenly, which in turn lowers premium rates.

Export Credit Insurance policy is a confidential document not to be disclosed to other parties, even to Importer or Foreign Agent. Limited disclosures are only to policy holder, ASEI and Bank/Creditor of the policy holder. However, the Bank is obliged to treat the

policy confidentially. Any breach of such conditions may cancel the exporter rights for indemnification.

VI.1. UNCOVERED RISKS.

The uncovered risks in export credit insurance are as follows:

- I a loss caused by the exporter failure or negligence to comply with the terms and conditions of the export contract and / or exporter negligence to comply with the policy conditions.
2. a loss covered by the general insurance policies (marine cargo, fire, burglary, etc.).
3. a loss caused by the exporter concerned, the exporter's agent and / or the collecting bank's negligence.
4. a loss caused by the currency exchange rate fluctuation.
5. a loss not proven by any evidence.
6. a loss not supported by proper documents.
7. a loss arising from forged documents, or not in accordance with the evidence.
8. a loss in form of interest accumulation, resulting from the importer's payment delay.
9. a loss due to the export not being in accordance with the export contract.
10. a loss due to the export being delivered to an importer who has equity interest and / or managerial relationship with the exporter.

11. a loss which in fact could be prevented or limited by canceling shipment or not delivering merchandise to the importer, as the exporter is in fact proven to have information about the circumstances that would lead to loss prior to export shipment to the importer concerned.

VI.2. COVERED RISK.

The risks covered in export credit insurance consist of commercial and non-commercial risk.

1. COMMERCIAL RISKS are as follows:

- an insolvency of the importer.
- a failure to settle payment within 6 months after acceptance and approval of the goods shipped by the importer.
- a failure or refusal of the importer to accept the goods shipped, and that such refusal is violating the contract, and that it is in fact not the fault of the exporter.

2. NON COMMERCIAL RISKS are as follows:

- a payment delay due to the transfer payment restriction to Indonesia.
- an implementation of an updated regulation on import payment that may create problems in currency transfer.
- a cancellation of legitimate import license.
- a war between Indonesia and the importer's country.
- a civil war, revolution or other social unrest in the importers country.
- a payment failure or rejection caused by other than the concerned importer's fault, subject that ASEI has approved that the concerned importer is guaranteed by its government.
- other incidents outside Indonesia beyond the exporter's or importer's ability to control and / or prevent.

VI.3. UNDERWRITING TECHNIQUES

To determine the performance of importer and country destination of export, our underwriting department analyses many variables that influence the risks of the transaction. Our underwriting department are primarily concerned with two main variables, Commercial and country risks management. Many variables influence both risks as follows:

1. COMMERCIAL RISK MANAGEMENT

Some variables that influence Commercial Risk Management are:

- a. The age of importer company
- b. The company director (management) capability or experience.
- c. Experience in loan payment
- d. The company working capital
- e. The company condition whether loss or profit
- f. The company Networth
- g. The development / trend of the company / business
- h. The risk of the life cycle commodity
- i. The composition and the degree of the company borrowings
- j. Negative information such as disputes, court actions or political issues.
- k. The company performance compared with the average industry performance.
- l. Importer's Sales Turn Over

- m. The Importer Sale's Payment System
- n. The nature of the goods

2. COUNTRY RISK MANAGEMENT

Some variable that influence Country Risk Management are:

- a. Geographical factor
 - Position / Place and geographic location
 - Population
 - Natural Resources

- b. Social / political risks indicator
 - Foreign Dispute
 - Political terrorist activity
 - Civil War
 - Law and order issues
 - Inadequate country economic planning
 - Degree of corruption
 - Bureaucracy
 - Racial / Religious tension

- C. Financial country indicator
 - Rescheduling of the Foreign debt
 - The delay in payment of Foreign loans
 - Limitation of foreign exchange

- d. Economical balance indicator
 - Degree of inflation
 - Debt Service Ratio
 - Reserves / import (International Liquidity)
 - Current Account
 - GNP Growth

VI.4. INDEMNIFICATION

1. AMOUNT OF INDEMNIFICATION

Export credit insurance is a type of sharing coverage, whereas ASEI maximum indemnification is limited to 85 % of the real loss, at the maximum amount of the invoice, the policy holder is responsible for the rest. The purpose of this scheme is to encourage exporter to be prudent in selecting only reliable importers in concluding an export contract, and to keep making efforts to obtain recoveries from importer.

2. TIME OF INDEMNIFICATION

ASEI as the insurer should pay a certain amount of indemnification to exporter after the loss incurred is proven to fall within the covered risks. The indemnification time depends on the cause of loss such as follows

- | | |
|---|--|
| - Insolvency | - Immediately after insolvency |
| - Importer fail to pay for goods | - 6 months after due date of payment |
| - Importer refusal to accept good which have been exported | - 1 month after goods are resold or otherwise disposed of |
| - Other occurrences | - 4 months after occurrences |

VI.5. CREDIT LIMIT

In a comprehensive shipment policy, the limit of coverage for each importer and or for each country is established based on a credit limit system. The credit limit is determined after considering the credibility of the importer, performance of exporter, type(s) of export commodity(ies), and the economic and political conditions of the, export destination or payment origin country.

The credit limit system has a distinctive role in the export credit insurance business activities due to the complexity of credit limit determination and the risk involved.

VI.6. THE PREMIUM

The rate of premium is determined by considering, among other factors, the importing country's trade pattern, market distribution, payment terms, as well as rating of the importing country. As an illustration, rate of premium for export under the L/C terms is lower than that of the Non-L/C terms. The premium rate of export to a sound country in terms of political and economic conditions will be lower than that of to a high risk country.

The premium rate is determined at the time of the issuance of the credit limit decision. As a general guideline, the premium rate for a certain period of time for a comprehensive shipment policy ranges from 0,2% to 4% of the gross export value (Invoices value).

VI.7. ASSIGNMENT

Exporter as export insurance policy holder can transfer the indemnity right to the bank or financial institution which is giving a discount on a Bill of Exchange against the exporter collecting from the importer on the shipment of goods which insurance has already been covered by ASEI, by signing a letter of authority to transfer indemnity right.

With the transfer of indemnity right the discounter of the Bill of Exchange should feel safe and the exporter will obtain funds, otherwise, he must wait for the due date of payment from the importer.

VI.8. RECOVERIES AND SUBROGATION.

ASEI's right for subrogation operates immediately after ASEI indemnifies a claim, based on the application for loss indemnification (STGR) submitted by the exporter

concerned, and other ASEI information sources. The subrogation right is ASEI's right to a part of payment received by the exporter for any future payment made by the importer. ASEI's entitlement for the proportion of recovery is based on ASEI's share in the loss indemnification.

The subrogation is the exporter's debt to ASEI, therefore the exporter should always take necessary actions to obtain the unsettled export payment, even though the loss has been indemnified by ASEI. If necessary, the exporter should furnish ASEI with a power of attorney, authorizing ASEI to undertake necessary actions.

VII. SUPPORT SYSTEMS

To accommodate the development of ASEI, to achieve its goal, to realize the benefits ASEI's product and services to its clients and to give customer satisfaction to its clients, ASEI have several Support Systems such as :

VII.1. MEMBERSHIP IN NATIONAL AND INTERNATIONAL ORGANIZATIONS

1. The Indonesia Insurance Council (DAI)
2. The Forum BUMN G-11
3. The Indonesian Chamber of commerce and industry (KADIN)
4. Berne Union
5. Regional Cooperation Group of Export Credit Insurance (South Asia)

VII.2. INTERNATIONAL NETWORK

For Indonesian exporters to evaluate the degree of both commercial and political risk regarding payments from export destinations, it is essential that they have access to data on trade developments in these countries.

As in any business subject to high risks, ASEI must have information regarding buyers and buyer's countries. One source is overseas government agencies such as the trade attaches at Indonesian embassies and Indonesian Trade Promotion Centers (ITPC). In addition, ASEI also uses highly reputable, private run information services with extensive international networks such as Dun and Bradstreet International, MECOS of Middle East etc.

In 1992, ASEI become a member of Berne Union, a London-based international export credit insurance company association, the association has 45 export credit insurance company members from 35 countries, One of the benefits of being a member of Berne Union is the convenient access to information held by other members.

Operations are supported by sophisticated technology such as EDI (Electronic Data Interchange). EDI allow ASEI to exchange information with other members of Berne Union, via the facilities of the Netherlands based DEXNET BV. Access to comprehensive, accurate information allows ASEI to advise as to levels of commercial or political risk prevalent in importing nations. This data purchase allows potential losses to be minimized.

VII.3. INFORMATION SERVICE

With the support of its technological infrastructure, the professional human resources of ASEI are able to provide comprehensive and accurate business information. Exporters can use this data to help anticipate risks, and minimize risks when planning business expansion. ASEI offers the following information:

1. BUSINESS INFORMATION REPORT

This contains background on companies, together with information on financial management, experience of payment, operations and other key matters

2. COUNTRY REPORTS

These documents systematically examine the political stability and economic conditions in given countries; key additional information with a bearing on exports is also included.

VII.4. TRAINING AND EDUCATIONAL SUPPORT

To anticipate challenges of the future, ASEI works ceaselessly to improve the professionalism and abilities of its human resources. ASEI understands that human resources are its most valuable asset.

ASEI's personnel skill and professionalism is enhanced through sending them for training to various educational institutions, both at home and abroad. Since training focusing on export insurance is not yet available in Indonesia, many personnel go abroad for education to countries such as South Korea, Australia, England and the Netherlands. Staff attend seminars and workshops on management, underwriting technique, claims and subrogation, computers and information technology in exports, and export credit coverage. These sessions are routinely provided by Berne union, and the Regional Cooperation Group of South Asia (RCG).

We also have other Support systems that help to achieve ASEI's goals such as Reinsurance, debt collection, lawyer (from local or foreign institution), etc.

VIII. OPERATING RESULT

With the hard work and dedication of ASEI's management, ASEI surpassed the 1995 annual work plan and budget. Net earning rose 40% or Rp. 113.959 billion to Rp. 48.347 billion, showing that ASEI's financial performance is in strong shape. More detail of operating result of ASEI can be seen in financial highlights as below:

FINANCIAL HIGHLIGHTS

(Million Rp.)

| KETERANGAN | 1995 | 1994 |
|------------------------|--------------|--------------|
| Total Coverage | 3,638,428.00 | 4,679,167.00 |
| Underwriting Income | 31,690.00 | 31,881.00 |
| Investment Income | 37,783.00 | 34,903.00 |
| Total Investment | 297,721.00 | 286,018.00 |
| Claims Payable | 2,417.00 | 1,010.00 |
| Current Assets | 15,738.00 | 8,282.00 |
| Current Liabilities | 7,946.00 | 10,642.00 |
| Claim Reserves | 97,053.00 | 106,104.00 |
| Total Equity | 212,011.00 | 182,259.00 |
| Corporate Tax | 11,298.00 | 19,899.00 |
| Net Income After Taxes | 48,347.00 | 34,386.00 |

CHAPTER VII - Part 2

Export Financing and Export Promotion Program :

The Case of Indonesia

Content

1. Basic Concept of Export Financing
2. The Important Role of Export Promotion Program
3. The Role of Bank Indonesia in Promoting Export
 - Post-shipment' Rediscount Facility
 - Local L/C's Rediscount Facility
 - Pre-shipment's Rediscount Facility
 - Swap Facility for "Eksportir Tertentu"
 - Forward Facility for "Eksportir Tertentu"
 - Arrangement between the Central Banks.
 - Initiative of Establishing an Export Credit Agency
4. The Establishment if an Export Credit Agency (A Proposal)

1. BASIC CONCEPT OF EXPORT FINANCING

- Exports mean any economic transactions in the form of shipment of goods and supply of services to out side the border of the custom's territory.
- Export financing is one of the key element for supporting the success of export oriented industries.
- Export financing is available in a simple or direct form and in a more advance form.
- Export financing from Export Credit Agency (ECA) is one of the alternative that is more attractive to exporters because ECA can provide the comprehensive by exporters.

- The ECA is vital for exporting industries as well as for the whole economy especially to promote exports.

2. THE IMPORTANT ROLE OF AN EXPORT PROMOTION PROGRAM

- The external sector in Indonesia's economy plays a role as important as the domestic sector, which is consistent with the Indonesian open economy and free foreign exchange system.
- Export are the main source of the country's foreign exchange earning that are needed to maintain sustainable economic growth.
- Export promotion is vital to Indonesia's economy, especially to reduce the deficit on current account in the balance of payments.
- Export promotion has become a government commitment, which is implemented in joint efforts between ministries, both the monetary and real sectors, and private sectors (Chamber of Commerce, Business Association, and PT. ASEI)
- Joint-Efforts to promote exports among related institutions:
 - ❑ Trade facilitation
 - ❑ Joint Commission and Trade Mission
 - ❑ Implementation of EDI (Electronic Data Interchanger)
 - ❑ "Primaniyarta" awards
 - ❑ Banking Arrangement and Memorandum of Understanding
 - ❑ Export promotion for "*Eksporir Tertentu*" (priority exporters).
 - ❑ "Tim Khusus" (Dedicated Teams) to boost export

EKSPORTIR and KOMODITAS TERTENTU (PRIORITY EXPORTER AND COMMODITIES)

PRIORITY EXPORTER:

Priority exporters are those exporters who have been granted a certificate by the Ministry of Industry and Trade after fulfilling requirement as defined by the related Ministry. Such exporter will have special facility covering custom, taxation and banking facilities.

PRIORITY COMMODITIES:

As today, there are ten export commodities classified as priority commodities:

- Textile and textile product - Footwear
- Wood and Rattan product - Leather product
- Paper - Processed food
- Vegetable oils - Processed rubber
- Toys product - Frozen fish and shrimp

3. THE ROLE OF BANK INDONESIA IN PROMOTING EXPORT

- **Financial Aspects**

- **Post-shipment Rediscount Facility**

- Bank Indonesia provides a rediscount facility to “Eksporir Tertentu”, as well as to ordinary exporters through banks, based on discount transactions between banks and those exporters which had already discounted their drafts to the banks.

- **Pre-shipment Rediscount Facility**

- Bank Indonesia provides rediscount facility to “Eksporir Tertentu” through banks, based on discount transactions between banks and those exporters based on exporter’s *future* export earnings.

- **Local L/C Rediscount Facility**

- Bank Indonesia provides rediscount facility to *local suppliers* that supply goods and services to “Eksporir Tertentu” through banks, based on discount transactions between banks and those suppliers which had already discounted their drafts to the banks.

□ **Swap and Forward Facility for “Eksportir Tertentu”**

minimize risk of currency fluctuation for certain exporters, Bank Indonesia provides Swap and Forward Facilitation to those exporters. These facilities are given through banks, based on Swap and Forward transaction between banks and priority exporters.

• **Non Financial Aspects**

- Arrangement between the Central Banks in the form of Banking Arrangement and Memorandum of Understanding as an umbrella for maintaining continuity of the payment transaction between the commercial banks by allowing central banks to recommend any relevant action if there is a dispute between the commercial banks of the two countries. The central banks, however, will not take over the payment risk of such transaction.

There are 13 arrangements signed since 1992:

- | | | |
|-----------------|---------------|-------------|
| -Iran | -Turkmenistan | -Bulgaria |
| -Russia | Hungary | -Kazakhstan |
| -Kyrgyzstan | Pakistan | -Uzbekistan |
| -Czech Republic | Romania | -Argentina |
| -Slovakia | | |

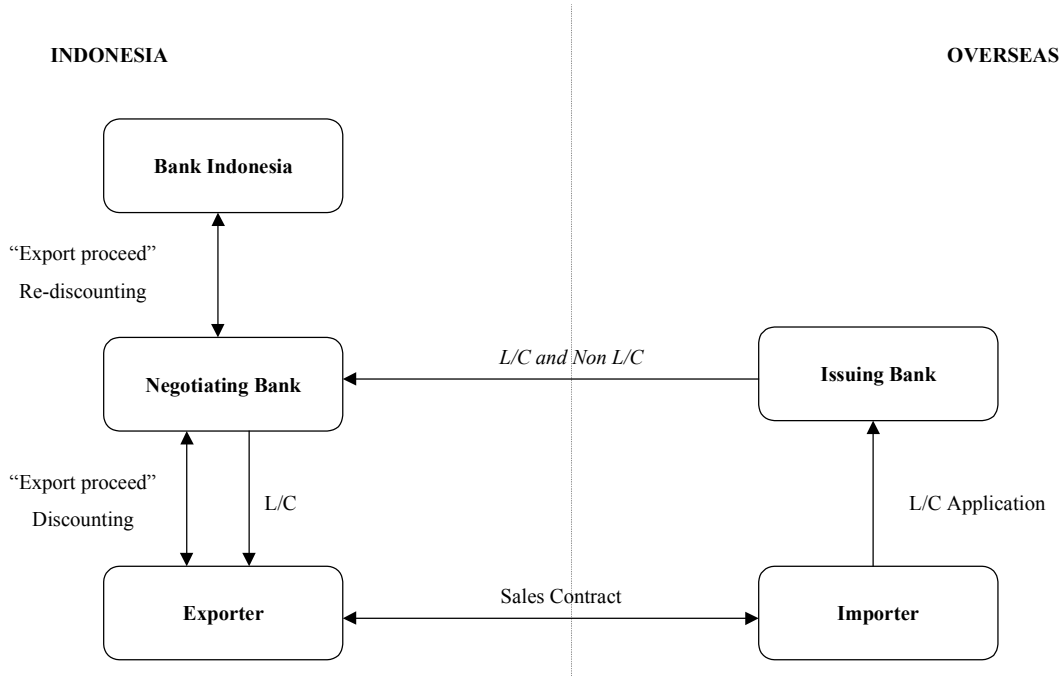
- *Linkage of Bank's Commercial Overseas Borrowing (COB) to Export Credit.*

A bank provided with a COB ceiling is required to extend export credit at a minimum of 80% of the offshore borrowing disbursed to the bank during the current year.

- **Further Initiative For an Export Credit Agency**

To provide medium and long term finance necessary for exports of non-traditional products ie. Capital goods, with a competitive terms and conditions compared with those of commercial banks and other financial agencies which do provide “lending”

**BANK INDONESIA'S REDISCOUNT FACILITY
(POST-SHIPMENT BASIS)**



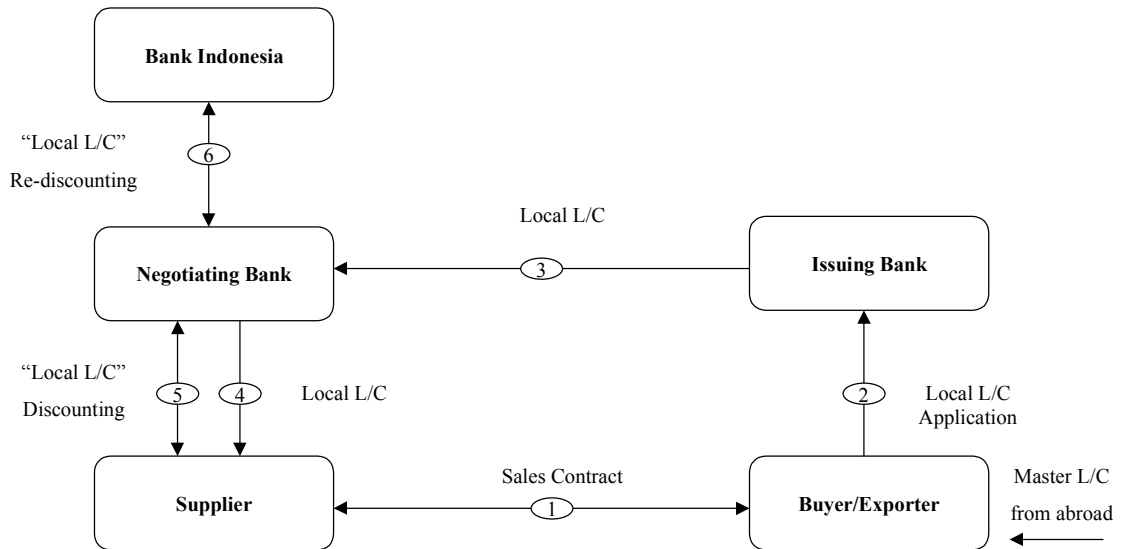
**REDISCOUNT FACILITY
(POST-SHIPMENT BASIS)**

1. Priority exporters and ordinary exporters have Usance L/C from overseas or contracts on Non-L/C basis.
2. Bank asks Bank Indonesia for the facility, and submit document of copy of Export Declaration (PEB), copy of Credit Note to these exporters, and copy Certificate for Certain Exporter.
3. For disbursement of facility, banks submit the draft to the Bank Indonesia in which the value of the facility is equal to the bank's draft.
4. The maximum period of facility is 2 (two) years for certain exporters and 1 (one) year for ordinary exporter.
5. Discount rate is SIBOR* Flat for certain exporters and SIBOR+ 1% for ordinary exporter.

* SIBOR - Singapore Inter Bank Offer Rate

6. Currencies are available in USD and Ruphia.

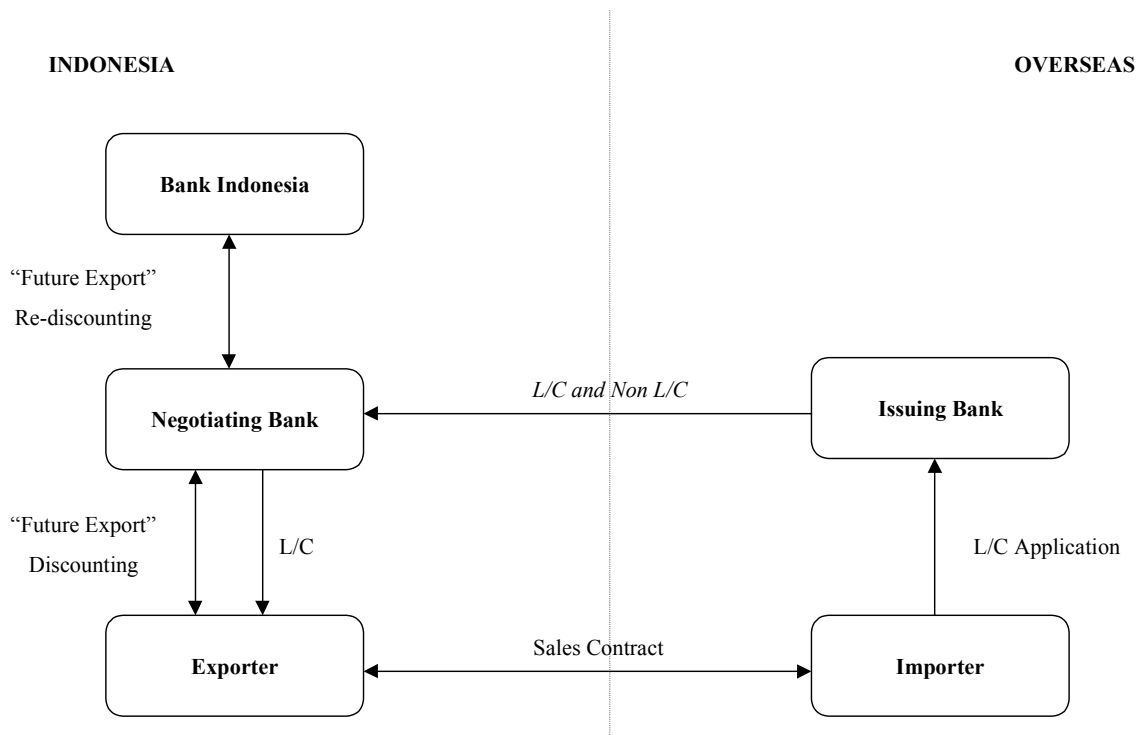
Bank Indonesia's Rediscount Facility On Local L/C



REDISCOUNTING FACILITY ON LOCAL L/C

1. Both beneficiaries (supplier) and buyer (priority exporter) sign Sales Contract and agree to use Local L/C
2. Buyer applies for Local L/C
3. Opening Bank Local L/C
4. Negotiating Bank advice Local L/C to Supplier.
5. Supplier sends goods to buyer and discounts his draft to Negotiating Bank.
6. Negotiating Bank rediscounts his Draft to Bank Indonesia.

**BANK INDONESIA'S REDISCOUNT FACILITY
(PRE-SHIPMENT BASIS)**

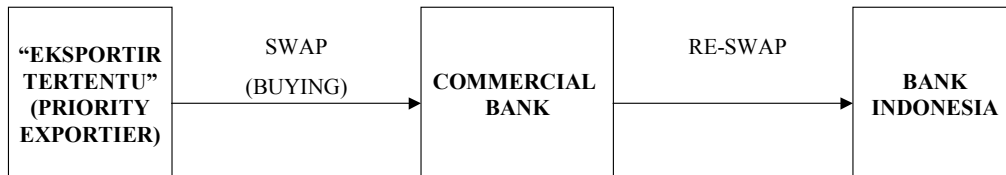


**REDISCOUNTING FACILITY
(PRE-SHIPMENT BASIS)**

1. Priority exporters have a prospect of *future export earnings* within one year and confirmed by beneficiary/exporter's bank.
2. Banks ask Bank Indonesia for the facility, and submit documents of copy Sales Contract, and/or buying order, and/or copy L/C, and copy Certificate for Priority Exporter, and bank's recommendation for credit to exporters.
3. For disbursement of facility, banks submit the draft to Bank Indonesia in which the value is linked to the future export earnings of the exporters.
4. The maximum period of facility is one year.

5. Discount Rate is SIBOR Flat.
6. Currencies are available in USD and Rupiah.

BANK INDONESIA'S SWAP FACILITY



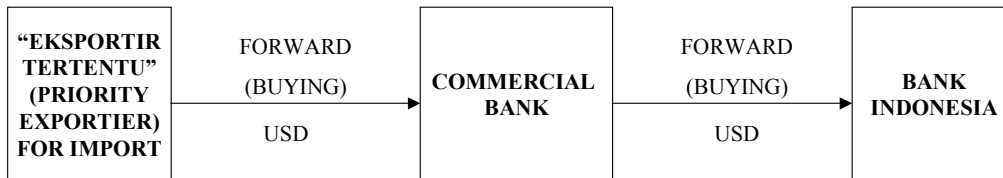
SWAP FACILITY:

1. Priority exporters, who have USD, deal with their banks for swap transaction ie. Sells USD buys Rupiah (spot) and buys USD sells Rupiah (forward)
2. Banks through RMDS (Reuters Monitor Dealing System) re-Swap to BI (Bank Indonesia) (10.00 am – 12.00 noon)

Requirements

- a. Banks re-Swap to BI on the same day as the Swap transaction with Priority Exporters.
- b. The maximum value of re-Swap has the same transaction with Priority Exporters.
- c. The maximum period is 180 days and can be extended once.
- d. The documents:
 - ⇒ Swap confirmation
 - ⇒ Copy transaction with Priority Exporters
 - ⇒ Copy of Certificate Priority Exporters that covers the Swap period

BANK INDONESIA'S FORWARD FACILITY



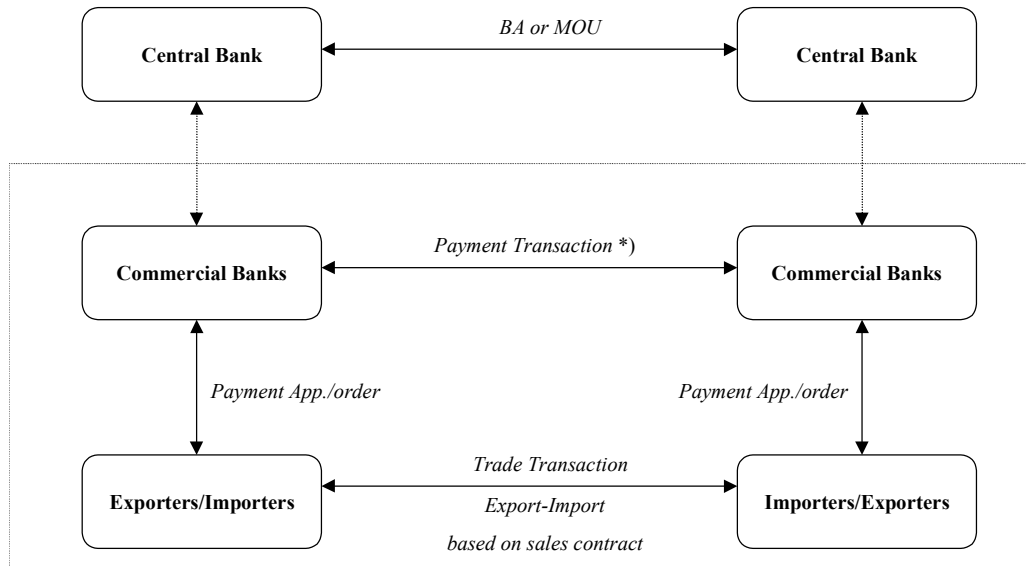
FORWARD FACILITY FOR "PRIORITY EXPORTERS"

1. Priority exporters, who need USD for their imports, deal with their bank for Forward transaction.
2. Bank through RMDS (Reuter Monitor Dealing System) re-Forward to BI(10.00 am – 12.00 noon)

Requirements

- a. Banks re-forward on BI as the same day as the forward transaction with importers.
- b. The maximum value of forward transaction has the same value as the import realisation.
- c. The maximum period is 90 days and can be extended once.
- d. The documents :
 - ⇒ Swap confirmation
 - ⇒ Copy of L/C or sales contract (for non L/C)
 - ⇒ Copy of Certificate of Priority Exporters that covers the forward transaction

**BANKING ARRANGEMENT
OR
MEMORANDUM OF UNDERSTANDING**



**) If dispute arisen between commercial banks, the Central Banks agree to expedite advise for the solution of such dispute*

Banking Arrangement

- Purpose/function:

As an umbrella for maintaining continuity of the payment transaction between the commercial banks by allowing central banks to recommend any relevant action if there is a dispute between the commercial banks of the two countries.
- Arrangement covers:
 - Payment instrument : L/C or non-L/C
 - Payment transaction done through commercial banks with respect to international banking practices and provision in respective countries.
 - Using freely convertible currencies.
 - Enhancing the establishment of an international banking correspondent between commercial banks of the two countries.

- Any dispute between commercial bank will be settled by the concerned commercial banks. Central banks could, however, recommend or advise any relevant solution for resolving a dispute arisen between the commercial banks.

4. THE ESTABLISHMENT OF AN EXPORT CREDIT AGENCY (A PROPOSAL)

- In the last two years, Indonesia's balance of payment (BOP) was characterised by higher (but still sustainable) current account deficit. The ratio of the current account deficit to GDP rose to 3.4% (95/96) and to 3.5% (96/97) compared to only 2.0% (94/95).
- The widening deficit was primarily attributed to weakening non-oil and gas exports on one side and the robust import growth and increased deficit on the service account.
- In the context of improving the BOP performance, by increase of export of non-traditional products, there will be a necessity to review and evolve a program to set up such as an Export Credit Agency.
- The Agency would facilitate medium and or long-term financing needed by exporters of, mainly, non-traditional products or export to prominent market such as emerging markets and the third world countries.

Chapter VIII

Trade and Investment Insurance System of Australia

Export Finance and Insurance Corporation – E.F.I.C.

- Banks and other infrastructure develop with business, but economic development may need some encouragement and support
 - Export Credit Agencies exist to fill gaps in the national financial infrastructure
 - Australia's history in international trade goes back to 1830, but EFIC only to 1956
 - First major export was wool - still dominates world market - but sold for cash at auction
 - Next the Gold Rush [1851], then wheat, meat and sugar - with corporate financings
 - Australia united and formed on Jan, 1, 1900
 - continued to sell commodities and import everything, but manufacturing began
 - Real change came post World War II
 - end of British Empire trade basis
 - immigration to Australia
 - rise of Japan trade for raw materials
 - growth of European Common Market
 - Serious efforts to increase manufacturing
 - search for new markets for products
 - Need for credit for small, medium exports to new markets
- 1956 - formation of EPIC, Export Payments and Insurance Corporation - A\$6 million loan.
- provided payment insurance for short-term credits.
- 1961 - Australian Government introduced the National Interest Account for higher risk and very large credits.
- needed for large wheat sales
- 1965 - Overseas Investment Insurance Facility
- to support manufacturers forming joint ventures, etc., abroad
- 1971 - Buyer Credit Guarantee Facility
- to support capital goods exports
 - Bougainville Copper mine supplies
- 1974 - Introduced direct lending for capital goods
- Reconstructed as **Export Finance & Insurance Corporation.**
- 1978 - Support for tender performance bonds
- 1983 - Empowered to lend foreign currencies

1986 - EFIC incorporated into AUSTRADE, began to Issue performance bonds

- big Increase In mining projects finance

1991 - EFIC re-established as separate Corporation

- equity capital, callable capital, reserves of A\$ 350 million
- total business supported \$4.8 billion

- EFIC now a full financial institution.

- In 25 years several roles established
 - support for commodity trades
 - support for manufactured exports
 - short-term credit sales
 - overseas stocks
 - investment insurance
 - capital goods exports to projects
 - bonds for contractors, service industries
 - improving relationships with banks on support for capital investments, loans to projects, working capital guarantees, assigned insurance, bonds

- EFIC became finance leader for several massive mining projects in Papua New Guinea

- built on Bougainville experience, OK Tedi mines to provide Innovative seed capital Inputs, including loans to PNG for government equity, first investment co-insurance with Canada, direct loans on a line of credit basis, political risk guarantees to bank syndications.

- Also addressed the market for SME exporters

- intensified marketing, restructured management structure, raised staff training, re-wrote policies in simpler form, worked with banks to improve exporter's access to working capital.
- results promising.

1996 RESULTS

- Total exports supported \$7.5 billion [+20%]
- Insured exports \$6.5 billion [+1496]
- 50 bonds Issued for \$140 million
- 12 overseas investments \$223 million

- 79 working capital guarantees [+100%]
- strong growth in SME business.
 - 209 new SMEs
 - 87% of new clients
 - 60% manufacturers
- exports to 155 countries [from 135]
- Europe is largest insured market [44%]
- Asia is largest for finance facilities [77%]
 - 2nd largest for insurance
- 1996/96 surplus \$12.6 million

EVENTS OF 1995/1996

- Financing and Cofinancing-financing of the billion dollar Lihir Gold Mine In Papua New Guinea
 - ❖ Political risk cover to financing banks
 - \$250 million capital
 - \$120 million interest
 - ❖ Credit Insurance to exporting suppliers
 - ❖ Investment Insurance to Mining Contractors
- EFIC invested in ASEAN Credit Information Co with ECICS [Singapore], COFACE [France]
- Introduced improved Export Finance Guarantee Facility for banks funding capital goods exports.
- Introduced improved Information services
- Streamlined re-organisation

TYPES OF INSURANCE

- Export Credit Insurance Policy
 - ❖ goods shipped / services performed
 - can be selective, with price loading
 - must declare all shipments to an insured buyer
 - ❖ cover against all risks-["seamless"]
 - unless special circumstances
 - co-insurance

- ❖ Ancillary extensions used
 - indirect export cover
 - overseas stock cover
 - processing cover
 - external trade cover
- ❖ Unfair Calling of Bonds or Guarantees Insurance
- ❖ Confirming Bank Policy
 - covers against failure of issuing bank& political risk
- Overseas Investment Insurance
 - covers against political risks
- Political Risk Insurance for capital goods finance by banks

INDEMNITY PAYMENTS

| INSURED RISK | MAXIMUM | PAYMENT DATE |
|----------------------------|---------|-----------------------------------|
| Insolvency | 90% | Immediately |
| Payment delay | 90% | 4 mths after due date |
| Repudiation of contract | 90% | 1 mth after disposal |
| Exchange transfer delays | 100% | 4 mths after due date |
| War, civil war, import ban | | |
| Diversions of voyage, etc. | 100% | 1 mth after due date or loss even |

BOND SUPPORT

- Unfair Calling Insurance - 95%
- Bond indemnity/insurance to financiers
 - up to 95% of cover
- "Unsecured" advance payment bonds

CAPITAL GOODS FINANCE

- Export Finance and Credit provided on competitive terms
 - by direct lending
 - by guaranteed loans from banks
- Observes terms of the OECD Understanding for official export credits
 - 15% down payment

- OECD Credit Insurance Reference Rates [minimum] based on bond rate plus 100 basis points.
- maximum term of repayment depending on goods
- starting date for repayments.
- EFIC charges establishment fee, finance fee for exporter, commitment fee for undrawn funds, 6 monthly repayments,
- EFIC will also negotiate Irrevocable Letters of Credit for small amounts for exporters.

EFIC'S MISSION STATEMENT

“To increase Australia's exports.

To provide our clients internationally competitive insurance and finance services, particularly for countries, companies and contracts which the commercial market may not have the capacity to cover.

To extend EFIC's services as far as we can, consistent with preserving the financial viability essential to the Corporation's long-term support for exporters ”

COMMERCIAL FINANCIAL RETURNS 1995/96

\$'000

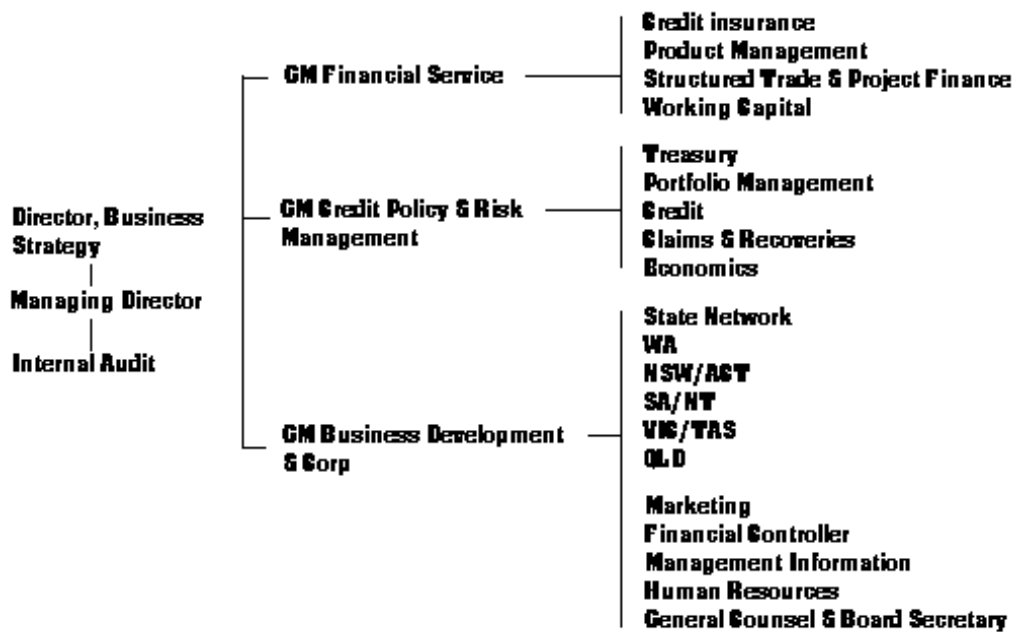
| | |
|---|------------------|
| <u>EXPORT BUSINESS SUPPORTED</u> | <u>6,903,155</u> |
| <u>Operating income</u> | <u>43,616</u> |
| Investment Income | 18,549 |
| <u>Total Income</u> | <u>62,165</u> |
| <u>Operating Expenditure</u> | <u>25,987</u> |
| Insurance claims | 10,030 |
| Bad and doubtful debts | 11,466 |
| <u>Provision for bonds & guarantees</u> | <u>2,117</u> |
| <u>Total expenditure</u> | <u>49,600</u> |
| Surplus | 12,565 |

RATIOS AND OTHER STATISTICS

| | |
|---|------|
| Operating expenses to total income ratio | 39% |
| Operating expenses to total receivables ratio | 0.8% |
| Average staff numbers | 185 |

| | |
|--|--------|
| Export business supported per employee [\$000's] | 37,314 |
| Operating income per employee [\$] | 214 |
| Operating expenses per employee [\$] | 112 |

ORGANISATION CHART



TRADE REVIEW

ASIA AT A GLANCE

| | |
|--|-----------|
| 30% of total exports supported by EFIC | \$2,227 m |
| 23% of credit insurance | \$1,492 m |
| 77% of medium term loans disbursed | \$ 447 m |
| 71% of new loans | \$ 282 m |
| 51% of bond support | \$ 64 m |
| 42% of working capital guarantees | \$ 25 m |
| 89% of overseas investment insurance | \$ 199 m |

South East Asia - Indonesia

- ❖ Largest borrower of capital goods finance
 - Some is mixed credits [with aid funds]
- ❖ A\$120 million - 49% of new loans

- telecommunications
- health & safety project
- ❖ Two Overseas Investment Policies

PHILIPPINES

- ❖ \$49 million mixed credit loans
 - for Manila traffic signal system
 - Baguio water supply
- ❖ Credit Insurance
 - \$112 million - 33% increase
 - iron & steel
 - dairy produce
 - process foods

SINGAPORE

- ❖ Credit insurance up 12% to \$135 million
- ❖ Ship sector loan
- ❖ Working Capital Guarantees
 - telephones
 - computer software
 - process equipment
 - glass re-inforced concrete

THAILAND

- ❖ Credit Insurance up 15% million to \$79 m
 - some small loans
 - first capital goods guarantee for Chiang Mai mining

MALAYSIA

- ❖ Credit insurance down slightly to \$125 m
 - one loan for abttoir

VIETNAM

- ❖ Two new loans - one commercial account
 - \$66 million overseas investment insurance for telecom network

SOUTH ASIA - INDIA

- ❖ 3rd largest medium term borrower
 - due to Pipawar Mine (1991)
- ❖ Credit Insurance \$60 million
 - 64% increase in wool

NORTH-EAST ASIA

CHINA

- ❖ Credit Insurance \$196 million - up 7%
 - iron & steel, base metals
- ❖ 15 new mixed credit loans - \$83 million
 - telecoms
 - water treatment
- ❖ 5 manufacturing investments
 - \$10 m. overseas Investment Insurance

JAPAN

- ❖ Credit Insurance \$213 million
 - 7 working capital guarantees for exporters supplying Japan
- ❖ Most trade is not insured - strong buyers, Japanese trading companies, long-term contracts.

EUROPE

AT A GLANCE

| | |
|---|-----------|
| 39 % of total exports supported by EFIC | \$2,935 m |
| 44 % of credit insurance | \$2,813 m |
| 19 % of medium term loans disbursed | \$ 111 m |
| 19 % of new loans signed | \$ 76 m |

- | | |
|-----------------------------------|--------|
| 3 % of bond support | \$ 9 m |
| 5 % of working capital guarantees | \$ 3 m |
- Credit insurance grew 15% but with higher risks
 - coal, nickel, wool, wine, hides, skins
 - main risks In Italy, UK, Germany
 - \$70 million loans for very fast ferries

NORTH AMERICA

AT A GLANCE

| | |
|---|------------|
| 16 % of total exports supported by EFIC | \$ 1,173 m |
| 17 % of credit insurance | \$ 1,091 m |
| 2 % of medium term loans disbursed | \$ 11 m |
| 8 % of new loans signed | \$ 33 m |
| 35 % of bond support | \$ 43 m |
| 46 % of working capital guarantees | \$ 27 m |

UNITED STATES OF AMERICA

- Credit Insurance for \$832 million
 - iron & steel, nickel, wine
- Again the highest tally of insurance claims [35 for \$4 m]
 - working capital guarantees for manufacturers

MIDDLE EAST & NORTH AFRICA

AT A GLANCE

| | |
|--|---------|
| 8 % of total exports supported by EFIC | \$632 m |
| 10 % of credit Insurance | \$623 m |
| 6 % of bond support | \$ 8 m |
| 4 % of working capital guarantee | \$ 2 m |

- 45% growth in insurance due to large wheat sales to Iran.
- working capital and bond support for contractors.

PAOUA NEW GUINEA, NEW ZEALAND AND THE PACIFIC ISLANDS

AT A GLANCE

| | |
|---|----------|
| 5 % of total exports supported by EFIC | \$378 m |
| 6 % of credit insurance | \$355 m |
| 2 % of medium term loans disbursed | \$ 9 m |
| 2 % of new loans signed | \$ 8 m |
| 0.3 %of bond support | \$ 0.3 m |
| 4 % of working capital guarantees | \$ 3 m |
| 5 % of new overseas investrment insurance | \$ 11 m |

- PNG has third largest EFIC exposure due to large mining projects

AFRICA

AT A GLANCE

| | |
|--|----------|
| 2 % of total exports supported by EFIC | \$112 m |
| 2 % of credit Insurance | \$ 99 m |
| 0.2 % of bond support | \$ 0.2 m |
| 6 % of new overseas investment insurance | \$ 13 m |

EFIC - FUTURE DEVELOPMENT

- Market Research & Product Development
 - studying new markets devised by exporters
 - developing and selling appropriate products
 - conducts client satisfaction surveys
- New exporters and small and medium industries are a high priority
 - simplified policy being tested for small new exporters
- Increased emphasis on working with banks
 - Export Finance Guarantees
 - Working Capital Facilities
 - 79 guarantees this year
- Servicing the Service Sector
 - mainly services connected with the supply of goods
 - working closely with the Industry associations

PROVIDING CREDIT INSURANCE

- Proposal from exporter showing

- exporting experience
- credit management skill
- markets & buyers to be insured
- amounts of cover requested
- payment terms requested

ALSO- details of buyers they DON'T wish to cover

THEN

- face to face discussions
- to be effective cover must have
 - credit limit on bank or buyer
 - valid declaration on shipments
 - premiums paid
 - comply with all conditions
- Exporter must:
 - disclose all material information
 - show due care and diligence In making and fulfilling contracts
 - report all potential problems at the earliest opportunity
 - do nothing to jeopardise EFIC's position
- EFIC offers comprehensive cover
 - "all risks', seamless, etc.
 - selection of buyers to insure not encouraged
 - political risk only can be requested if
 - a] associated buyer
 - b] 'undoubted' buyer
- Credit Limits
 - a revolving limit which can be re-used as payments are made
 - exporters are given discretion on the level of sales up to 180 days to particular buyers
 - within rigid credit analysis condition
 - 3 trade references needed
 - 12 months good experience
- Exporters must inform EFIC of any association with buyer
- Requests for extensions of time to pay are the first sign of trouble
- Early action to minimise loss is vital for avoiding losses and making recoveries

- Claims examination is the time for serious study of each case
if conditions have not been met the claim will be refused

PROMPT PAYMENT OF CLAIMS IS THE BASIS OF THE INSURANCE BUSINESS

OPTIONAL POLICY COVERS

- Pre-Shipment Cover
 - from the time contract is agreed
 - an 'event of loss' before shipment
 - bankruptcy of the buyer
 - political blockage
- two limits to payments
 - costs actually incurred
 - value of the contract
- External Trade Cover
 - to complement local goods
 - up to 25% of turnover
- Consignment Cover
 - for overseas stockholding
 - processing in storage
 - sales form overseas stocks
- Indirect exports
 - where two Australian firms make a transaction, but the goods are destined for export at the next stage

CAPITAL GOODS FINANCE

- Export Contracts for medium/long term
 - for equipment for manufacturing, transport, communications, services which has a long working life
 - minimum terms and conditions under the OECD "Understanding" - the Consensus
- For Smaller contracts "suppliers credit" is normal
 - exporter sells directly on credit terms to the buyer
 - sale is secured by documentary credits - 'negotiated' by EFIC which pays Cash to the exporter, or guarantees the sellers bank.

- For larger contracts “buyers credit” is more normal
 - based on a loan to the buyer from EFIC or a bank guaranteed by EFIC,
 - bank loan can be guaranteed against all risks of just political risks, if the bank is willing to take the commercial risk itself.
- For large projects more diverse structures are developed - often in partnership with other country ECAS, International Financial Institutions (MIGA, IBRD, ADB, IFC, etc.)
- In ‘Project Finance’ several techniques can be used together to assemble the total financing required, e.g. in PNG
 - MISIMA ISLAND GOLD
 - PORGERA GOLD
 - KUTUBU OIL & GAS
 - LIHIR ISLAND GOLD
- These projects employed overseas investment insurance, credit Insurance, guarantees to bank syndications, direct lending, co-insurance and corporate funding.
- Major differences in medium/long, term financing from short-term credit insurance
 - much larger and longer credit exposure for the ECA
 - more complicated legal arrangements
 - innovative planning is needed
 - close co-ordination with sponsors, borrowers and other lenders/guarantors is required
 - similarities with bank corporate finance and close supervision is needed
- Previously much M/LT lending was government guaranteed
 - now greater emphasis on private sector and commercial viability
 - project, contract and buyer/contractor ‘due diligence’ now a critical part of risk management

EFIC has had an important role in financing PNG mines on a purely commercial private sector basis, although the government of PNG has been a minor shareholder in each project.

OVERSEAS INVESTMENT INSURANCE

- Developed to assist manufacturers establishing joint ventures abroad
 - insures investor equity and loans
 - has development aspect to foster Investment
 - has expanded with the growth of the private sector

- later provided cover for bank investments abroad
- cover has extended to provide political risk cover for bank loans to projects
- Investment insurance covers political risks only:
 - loss by expropriation
 - damage by war-like operations
 - inability to transfer royalties, dividends or repatriate capital

Chapter IX

Trade and Investment Insurance System of Thailand

Brief History of Export Credit Insurance in Thailand

Export credit insurance facility is one of the financial services offered by the Export-Import Bank of Thailand (EXIM Bank). EXIM Bank is the first, and currently, the only institution in Thailand that offers such facility. Main reasons behind this facility are to provide exporters operating in Thailand with confidence in exploring and penetrating new markets as well as new customers in familiar markets, and it enables the exporters to offer their customers more favorable terms of payment.

Under this facility, EXIM Bank provides exporters with payment risk coverage for the export of any kind of products to export markets worldwide. In case merchandise is shipped out in compliance with the contract but exporters do not receive payment due to any commercial or political disruptions that obstruct the payment, EXIM Bank will indemnify exporters for the damage.

Institutional Framework and Organizational Set Up

The Export-Import Bank of Thailand is a state-enterprise institution, wholly owned by the Royal Thai Government, under the supervision of the Ministry of Finance. The EXIM Bank was established by the Export-Import Bank of Thailand Act B.E. 2536, which became effective on September 7, 1993. The initial capital of 2,500 million baht was paid by the Ministry of Finance and the Bank of Thailand. EXIM Bank officially started its operation in February 1994 with the official opening on February 17, 1994.

According to the Act, EXIM Bank can engage in various financial activities including short-term and long-term trade and investment financing, export credit insurance, and any financial activities that commercial banks offer, except accepting deposits from the public.

The operations of the EXIM Bank are supervised by the Board of Directors which is comprised of 12 directors as indicated in the Act.

- Six directors are heads of six governmental departments which have the capacity to render their supports to EXIM Bank.

- ◆ Director-General, The Fiscal Policy Office, Ministry of Finance
 - ◆ Director-General, Department of Foreign Trade, Ministry of Commerce
 - ◆ Director-General, The Office of Industrial Economics, Ministry of Industry
 - ◆ Director-General, Department of Economic Affairs, Ministry of Foreign Affairs
 - ◆ Deputy Governor, Bank of Thailand
- Five eminent persons appointed by the Minister of Finance from various professions:
 - One position is for the EXIM Bank's President

The President is appointed by the Cabinet and serves on a 4-year-term basis.. The current President is M.R. Pridiyathom Devakula.

The EXIM Bank consists of 9 departments:

1. Packing Credit Department
2. Business Promotion Department
3. Treasury Department
4. Banking Department
5. Economic Information and Planning Department
6. General Administration Department
7. Management Support Department
8. Business Development Department
9. Accounting and Financial Information Department

In addition, there is an Audit Division which reports directly to the President, and currently there is one representative office in Bangkok and two branches: one branch in Bangkok and one in the Southern province.

The export credit insurance facility is operated under the Business Development Department.

Product Development

EXIM Bank has, from the very beginning, set out to develop a Comprehensive Policy (D/P, D/A shipments). Our staff have gathered information regarding the export credit insurance and other related issues by visiting export credit agencies (ECAS) in the Republic

of China, Malaysia, Hong Kong, and Singapore. The Comprehensive Policy (D/P, D/A shipments) was first introduced to our exporters in November of 1994. The Policy has now been in operation for 2 years, and in May of this year, we have included Open Account (O/A) coverage to our Comprehensive Policy.

At present, we have further expanded our service and coverage, and are in the process of developing the Overseas Distributor Policy. The theme is that EXIM Bank will insure sales to buyers through a policyholder's distributor abroad. The Overseas Distributor Policy will cover only commercial risks caused by insolvency and repudiation.

Types, Features, Terms and Conditions of Insurance

The D/P, D/A shipments Comprehensive Policy and the D/P, D/A, O/A shipments Comprehensive Policy offer post-shipment, whole turnover coverage for exports under D/P, D/A, and O/A terms of payment.

Both policies provide coverage for both commercial and political risks. The commercial risks include insolvency, non-payment, and refusal to take delivery of goods. The political risks include restriction or prohibition of remittance of hard currency, prohibition of importation of merchandise, revocation of the buyer's import license, and occurrence of war, revolution or riot that obstruct payment for the merchandise.

The attentive exporter should start by applying for the export credit insurance coverage. After the policy is approved and assigned to the exporter, the maximum liabilities and the buyers' credit limits will be assigned. EXIM Bank will issue insurance policy according to the agreed credit line.

Insurance premium ranges between 0.3% - 1.8% based on the buyer's country and the term and duration of payment. There is a standard premium table and it is adjusted up or down by the policyholders' loading factor which is determined by overall performance and profile of the policyholder. That is why two policyholders exporting to the same buyer may pay different rates of premium.

For coverage to become effective, policyholders are required to declare every shipment exported under D/P, D/A, or O/A, respective to their policy, to EXIM Bank and pay premium immediately. Under export credit insurance coverage for D/P and D/A, policyholders can negotiate their insured export bills, without additional collateral, at any commercial banks or at the EXIM Bank.

In case the insured are not paid due to any incident under our coverage, EXIM Bank will compensate according to the cause of loss as follows.

| Scope of Coverage | Rate of Indemnity | Time Frame for Payment of Claims |
|---|--|--|
| Commercial Risks: | | |
| Insolvency | 85% of loss realized | Immediately upon receipt of evidence of bankruptcy or insolvency |
| Non-payment | 85% of loss realized | Within 4 months after due date of payment |
| Refusal to take delivery of goods | 70% of loss after proceeds from sale or auction of goods | Within one month after sale or auction of goods |
| Political Risks: | | |
| Restriction or prohibition of remittance of hard currency | 90% of loss realized | Within 4 months after due date of payment or 4 months after the buyer has made irrevocable deposit in local currency at the buyer's bank, whichever is later |
| Prohibition of importing of goods or revocation of buyer's import license | 90% of loss realized | Within 4 months after the occurrence of the incident or after due date of payment, whichever is |

| | | |
|---|----------------------|--|
| | | later |
| Occurrence of war, revocation or riot that obstruct payment for goods | 90% of loss realized | Within 4 months after the incident starts, or after due date of payment, whichever is later. |

Promotion and Marketing

There are several methods of promotion and marketing that are regularly used:

1. Business newspaper and magazine advertisements
2. Trade fair
3. Direct phone call/fax
4. Seminar

EXIM Bank usually places advertisements regarding the export credit insurance facility in several business-related newspapers and magazines. Interested exporters calling EXIM Bank would receive basic information. This is followed by the export insurance officers visiting the exporters at their companies or factories to give details about the facility, answer related questions, and find out more about the exporters and their businesses.

There are several trade fairs held in Bangkok yearly. The fairs are organized by the Department of Export Promotion, a government body, in order to attract foreign buyers to buy Thai goods. The export insurance officers take this opportunity to visit the exporters at their booths and briefly introduce EXIM Bank's export financing and export insurance services. A few days after the fair is over, the officers will give follow-up calls to prospects and talk to them in greater depth if they are interested.

Department of Export Promotion publishes a list of Thai Exporters called Selected List. Thai Chamber of Commerce and various Trade Associations usually have lists of their members as well. With such lists in hand, the export insurance officers of EXIM Bank call up or fax to companies that are listed introducing their services as well as inviting them to apply for the service.

Occasionally, EXIM Bank would organize seminars on export related issues. Main reason for the seminars is to educate exporters regarding exports, such as export financing and various terms of payment, and EXIM Bank's facilities. Small and medium-size business entrepreneurs are target audiences. However, EXIM Bank's clients are also welcome to join the seminar if they feel that they would like to learn more about the issues.

Underwriting Technique

Policy and Buyer Underwriting

Under policy underwriting, the exporters will be evaluated on their operations, financial conditions, and their overall performances, to see whether they can meet their obligations. Then buyers are underwritten based on the following factors:

1. General business information
 - Type and size of business
 - Number of personnel
 - Years in business
 - Other related businesses and branches
2. Financial status
 - Initial capital
 - Net worth
 - Financial ratios
3. Operating results
 - Turnover and profit
 - Trend
 - Management capabilities
4. Financial record or history
 - Relationship with financial institution

- Business reputation
- Comments from credit information agency

5. Payment record

Country Underwriting

Business Analysis and Development Division is responsible for country risk monitoring and assessment, using information and news from several sources, such as Economic Intelligence Unit (EIU), several business magazines, Ministry of Foreign Affairs, Foreign Embassies in Thailand, newspaper, and Reuters. Country rating is reviewed twice a year, and special country conditions will be revised when there are important incidents occurring in **the** buyers' countries that might affect payment of goods.

Claims and Recoveries

In order to receive claim compensation, the exporters need to file claim by submitting claim forms within a certain period of time. That is, six months if exported under D/P term of payment, and eight months if exported under D/A term of payment.

However, prior to submitting claim forms, the exporters are obliged to inform EXIM Bank concerning a likely loss either by phone or by submitting Notification of a Likely Loss form when the following incidents occur.

1. When the exporters know or are aware of any situation that might cause the buyers to be unable to pay for the goods when due.
2. When the buyers do not pay for the goods, whether in part or in whole within 30 days after due date.
3. When the exporters know of any news or information that might relate to receipt of payment.

The exporters are expected to do everything within their power and as recommended by EXIM Bank, to minimize potential loss, as well as to disclose all related information to EXIM Bank. EXIM Bank will pay claim compensation to exporters within a claim waiting period and after the cause of loss is proven valid.

Support System

Credit Information Agencies

Prior to granting credit limit to each buyer, EXIM Bank would gather buyers' information from the buyers' bank and credit information agencies. The credit information agencies that currently provide their services to the EXIM Banks are Dun & Bradstreet, Graydon, Teikoku Databank, etc.

Debt Collection Agencies

Debt Collection agencies are used immediately at the time potential loss occurs. Services might be in the form of general consultation, legal consultation, or hiring them to recover the loss.

Reinsurance

EXIM Bank is currently in the process of studying and searching for the most appropriate type of reinsurance.

Operating Results

As of June 1997, EXIM Bank provides coverage for exports of various types of goods, such as jewelry, agricultural products, food products, frozen seafood, canned food,

garments, and furniture. The aggregate approved maximum liability is 4,204.40 million baht (USD 140.15 million) for the exports to 608 buyers worldwide.

In the first year of export insurance operation (March - December of 1995), the total exports declared was 1,398 million baht (USD 46.6 million), and the figure has gone up 101.7% to 2,820 million baht (USD 94 million) in 1996. The total exports declared for the first six months of this year are 1,958 million baht (USD 65.27 million), more than half the figure at the same period of last year. It clearly shows that the confidence of exporters towards export insurance facility is on the rise. As of today, EXIM Bank has indemnified the Insured totaling 660,966 baht (USD 22,032).

EXIM Bank insures exports to 56 countries in Africa, North and Latin America, Western and Eastern Europe, the Middle East, and Asia Pacific countries. The exports focus mainly to Western European and Asia Pacific countries.

SECTION 4

SHORT TERM TRADE INSURANCE

CHAPTER I WHAT IS TRADE INSURANCE?

CHAPTER II SYNOPSIS

CHAPTER III EVALUATING TRADE INSURANCE - SYNOPSIS

CHAPTER I

WHAT IS TRADE INSURANCE?

Before we look at what types of policies are suitable for an exporter, or seller let us discuss the general concept of trade insurance.

In a nutshell, the concept of trade insurance is the "the insurance of non-payment of trade debts where such non-payment arises from commercial or non-commercial risks".

Trade insurance is quite different from marine cargo insurance or fire insurance policy, which covers the risk of damage or loss of the physical goods. Trade insurance covers against external causes which prevent you, as the exporter, from collecting payment for goods supplied. In international trade, as long as you are selling on credit you are exposed to the risks of your buyer going bankrupt or defaulting on payment because of poor commercial morality, tight cash flow or refusing to take delivery of the goods for no valid reasons. Further, when you sell overseas you are exposed to even more risks i.e. the country-related risks. These can be a blockage or delay in the transfer of payment, imposition of import restrictions or cancellation of a valid import licence. These actions are usually taken by a government to halt a deteriorating balance of payment situation if the country's foreign reserves are running low. Another country risk is war or political disturbance in the buyer's country.

With credit insurance, should any of the above events occur after the goods have been shipped and you can not collect payment, you can claim indemnity under the policy.

WHY DO WE NEED TRADE INSURANCE?

An exporter can benefit from trade insurance in three ways which can be categorised under the tenets of promotion, protection and profitability.

Promotion

You have an advantage over your competitors when competing for overseas orders if you are able to give credit instead of insisting on a Letter of Credit (L/C). Firstly your buyer may not have access to any L/C facility. Or, if he has access to such a facility, the cost of opening an L/C may too high. In certain countries, it is a regulation that an importer deposits 150% of the value of the LC to be opened.

Secondly, export promotion must be broad-based. New markets must be tapped to expand sales. If you are a manufacturer, there must be viable outlets for your products so as to keep your production lines active. You should not limit your export sales to one or two markets. Your markets should be well spread so that you will not be vulnerable even if there is a change in the country conditions of one or two of your markets. Credit insurance therefore not only helps you to develop new markets but also to be more competitive in giving credit.

Protection

While it is every businessman's dream to make more sales and profits, the sale is not complete if payment is not received. In other words, there is no benefit in making the sales unless your buyer pays you promptly. Trade debts usually form one the main items of the current assets of a trading or manufacturing company. Trade insurance therefore protects you from the loss of a valuable asset, which can affect your cashflow. If your business is concentrated on a handful of key buyers, the failure of just one of them can in turn ruin your business. This is what is called the "domino effect".

Profitability

Let's assume that your cashfiow is able to withstand a bad debt loss, profitability would be affected as you would need to recoup the loss from future sales. Assuming that the business makes a gross profit margin of 20% of each sale, you have a bad debt of \$100,000 you would have to chalk up additional sales of \$200,000 to recoup the loss. In other words, there is no profit from these sales.

An alternative to buying trade insurance is to self-insure. But this is only feasible for very large organizations where total cashflow is substantial and who can form a fund to be invested. For the average business, the resources would be better used as working capital rather than to be set aside as a reserve against losses. Also the amount of assets, which can be set aside as reserves is usually not sufficient to cushion a bad debt loss on a key buyer.

TYPES OF POLICIES AVAILABLE

There are different types of policies which are available to an exporter, the most usual is the Comprehensive Short Term Policy for credit terms of up to 180 days.

The Comprehensive Short Term Policy

This policy is suitable for a trader or manufacturer who exports goods which are repetitive in nature and the credit period involved does not exceed 180 days. In certain circumstances, trade credits of up to 720 days could be considered.

The Short term policy can be issued either on a "Shipment" or "Contract" basis. The main difference is that the former cover begins from date of shipment and the latter from the contract date.

A manufacturer of customised goods (i.e. non-standard goods) is usually advised to take up a Contracts Policy to give him the additional protection during the manufacturing or pre-shipment period to protect him against the buyer's insolvency. The pre-shipment loss would have been the material and other manufacturing costs incurred based on the buyer's orders. The loss would be even greater if it is difficult to find another willing buyer for the customised or partly produced goods.

The Short Term policy covers all the commercial and non-commercial risks described in the first section and the insured indemnity is usually 85% of the loss except where the loss is due to the buyer rejecting the goods which have been shipped. In the latter case, the exporter is required to bear the first 20% of the gross invoice value. Thereafter, the balance of the loss shall be indemnified at 85%.

Besides the Shipments or Contracts Policy, domestic sales may, by some Trade Credit Insurers, also be insured under the Domestic Trade Policy. The insured risks would be buyer's insolvency and default. Insured indemnity usually remains at 85%.

Policy Structure

Under the Comprehensive Short Term Policy, the basic Policy structure generally covers the following articles:

1. Risks insured, contracts covered
2. Risks excluded, limitation of liability
3. Insured's obligations
4. Loss ascertainment
5. Action after claims payments
6. General Conditions and Definitions

However, there may also be occasions where some terms under the Policy may need to be changed to take cognisance of the nature of the insured business and trade practices. These changes can be varied by special endorsements to the policy. An example would be the exclusion of the non-acceptance risk if the insured goods are perishable items.

Premium Rating and Calculation

There are many variations of premium rating and calculation adopted by different export credit agencies. Premium rating can be based on a matrix rate or a single rate. Short Term policy premium rating may be done in both ways depending on the insured portfolio.

A matrix premium rate is usually given when the insured portfolio consists of the following:

- Well spread markets ranging from good to higher risk markets;
- The payment terms offered to buyers vary.

A single premium rate is given when the payment term offered to buyers is constant and markets are confined to one category.

The premium for each policy will be rated on many factors based on information provided by the exporter / insured in the Proposal Form and interviews / discussions with the exporter / seller. The exporter / seller will have to complete and supply information in respect of the proposed business to be insured - such as markets, type of goods, loss experience, credit control and spread of buyers to be insured in the Proposal Form. The Proposal Form is an integral part of the Policy.

In determining the premium rate, these factors are taken into consideration:

- a) Type of Company and nature of business of the exporter / seller;
- b) Business experience and turnover offered (sales volume and market spread);
- c) Payment terms offered to buyers;
- d) Credit control and loss experience

Payment of premium is charged on insured turnover.

RENEWING THE POLICY

The policy is usually valid for a year and annual review of the policy will be made at the end of the expiry date. In renewing the policy, the insured's performance such as difficulty in servicing, slow payment of premium and claims experience will be taken into account. During the review for the renewal of a policy, it is also essential for the insurer to obtain information from the insured on his new business strategy and /or changes. In the event that there are changes, new terms and conditions will be added or deleted in the policy.

CHAPTER II

SYNOPSIS

1. What is Trade Insurance?
 - Insurance Against Non-payment

2. Service Scope
 - Credit Assessment
 - Risk Monitoring
 - Trade Support
 - Loss Minimisation

3. Pre-shipment Credit Risks
Losses before shipment
 - Insolvency
 - Cancellation of contract
 - Country Risks

4. Post-shipment Credit Risks
Losses after shipment
 - Buyer Risks
 - Country Risks

5. Buyer Risks
 - Insolvency
 - Payment Default
 - Repudiation

6. Country Risks
 - Transfer Delay
 - Import Ban

- Cancellation of Import Licence
- Payment Moratorium
- War, Civil Disturbance, Natural Disaster

7. Most Common Policies

(1) Comprehensive Shipment Policy (CSP)

- Domestic Exports and Re-exports
- Post-Shipment Risks

(2) External Trade Shipment Policy (ETSP)

- Third Country Exports
- Post-Shipment Risks (except certain country risks)

8. Other Policies

(1) Comprehensive Contract Policy (CCP)

(2) Comprehensive Services Policy

(3) Small and Medium Enterprises Policy (SMEP)

9. More Facilities

- Sales to Buying Offices
- Sales to Local Exporter
- Sales by Overseas Associate / Subsidiary

10. ECIC Insurance Policy

- Each Period 12 Months
- Maximum Liability
- Policy Deposit
- Policy Fee

11. Fundamental Insurance Concept

Whole Insurable Turnover

- Insuring all Credit Shipments
- Lower Premium Cost

- Improve Risk Quality & Spread

Selective Cover if:

- Volume of Business Justifies
- Quality and Spread are Acceptable

12. Credit Assessment

- Policy Underwriting
- Buyer Underwriting
- Country Underwriting

CHAPTER III

EVALUATING TRADE INSURANCE

SYNOPSIS

WHAT DO MEMBERS ACTUALLY DO TO ASSESS EXPORTERS?

- Importance in exporter assessment
- Past - insurable turnover and the sector are essential parameters
- Present - tendency is to better identify the exporter's profile

OBJECTIVES

(1) Exporter vs Credit Insurer - striking a balance

- The balance may be jeopardised if
- Exporter operating in adverse sector
- Exporter facing substantial bad debt losses
- High management cost of small policies

(2) Credit insurance to meet exporter's requirement

(3) Offer price allows for

- wider range of parameters e.g. quality of exporter
- variants resulting from enhanced flexibility in the proposed products and services

SHARING OF EXPERIENCE

Can exporters be ruled out because of:

- their size?
- their sector?
- their financial situation?

Must the quoted price be the primary selection parameter?

FACTORS TO TAKE INTO ACCOUNT IN ASSESSING QUALITY EXPORT ACTIVITY

- Total Export Sales

- Sectors
- Bad Debt Losses
- Credit Management Organization and Methods

(1) TOTAL EXPORT SALES (Key Parameters)

(2) SECTORS

- Essential parameter considering major disparities resulting from known loss ratios in certain sectors
- Need to identify
 - exported products or services
 - exporter is a
 - manufacturer?
 - trader?
 - services provider?
 - exporter's customer base
 - industry
 - wholesalers
 - retailers
 - others

(3) BAD DEBT LOSSES

- Increasing emphasis on this factor
- Credit insurers to determine the following from exporter's books:
 - the provisions
 - the bad debt losses for last 3 financial years
 - the amount and number of outstanding payments
 - the major failures

(4) CREDIT MANAGEMENT ORGANIZATION AND METHODS

- Terms of payment - fundamental information item
- Whether exporter has credit management department

SHARING OF EXPERIENCE

- What is the insurer's view regarding credit management by the exporter?

QUALITY OF APPLICATION

- Obtain as much detailed information as possible in the application form

CUSTOMER BASE SURVEY FORM

- Appended to application
- Exporter to indicate
 - names and addresses of largest customers
 - terms of payment
 - credit limits applicable

OFFER

- Two important parameters in setting quoted prices
 - amount of insurable turnover
 - loss ratio
- Other factors discussed earlier are used to sharpen the quotation

FLEXIBILITY

- Risk sharing particularly on private buyers
 - 90/10 to 50/50
- Threshold
 - used to shift low risks (amounting to several thousand dollars) to the insured
 - limits insurer's management cost

FLEXIBILITY

- First loss
 - Insured assume first loss
 - Reduce management cost
 - Reduce loss ratio
 - Reduced tariffs

SHARING OF EXPERIENCE

- Position of members regarding flexibility in general
- To whom should it be offered?

SPECIMEN - APPENDIX I

Questionnaire to Prospective Policyholder

Name of Company _____

Address _____

A. GENERAL INFORMATION

- 1) Economic Form _____
- 2) Business Category (Exporter / Mfr./Both) _____
- 3) Registration Date _____
- 4) Paid up capital _____
- 5) Ratification Organization of Foreign Trade Business _____
- 6) Shareholders _____
- 7) Management Background _____
- 8) No. of employees _____
- 9) Space of premises _____
- 10) Parent / Associate / Subsidiary companies _____

10). Major export markets

| Market | Annual Turnover | Breakdown By Terms of Payment | | |
|--------|-----------------|-------------------------------|----|---------|
| | | LC | DP | DA & OA |
| | | | | |
| | | | | |
| | | | | |

11) Goods exported

| Goods Exported | Percentage |
|----------------|------------|
| | |
| | |
| | |

B. BANKERS

- 1) Names & branches _____
- 2) Amount of facilities _____

Name of the Exporters:

PROPOSAL FOR A COMPREHENSIVE POLICY (SHIPMENTS)

We have read a specimen of your Comprehensive Policy (Shipments), and request that you will inform us of the terms on which you are prepared to pay to us a percentage of the amount of any loss, as therein defined, that we may sustain in respect of contracts made with overseas buyers for the sale of goods wholly or partly produced or manufactured within Malaysia hereinafter referred to as "Exports", and under which contracts goods are exported from Malaysia during the period from to by reason of the occurrence after the export of such goods of any of the causes therein defined.

DECLARATION

1. NATURE OF GOODS TO BE COVERED UNDER THE PROPOSED POLICY

2. NATURE OF BUSINESS (MANUFACTURER/MERCHANT)

3. EXPORT TURNOVER We give below a breakdown by countries of our total export turnover (shipments destined for an overseas consignment stock should not be included) worldwide during the last twelve months and of our estimated total export turnover worldwide during the period to which the proposed Policy is to apply. Our export sales to our associated companies are included in Table 1 but direct business with buyers in the market concerned, are shown separately.

Table 1 - Country Turnover Analysis

| 1 BUYERS' COUNTRIES (in alphabetical order) | 2 Actual Turnover during last 12 months | 3 Estimated Turnover for next 12 months |
|---|---|---|
| | M\$ | M\$ |
| Total | M\$ | M\$ |

Table 2 - Total Estimated Turnover Analysis relating to the estimated turnover for next 12 months shown in column (3) of Table 1 above.

| | | |
|--|---------------|----------------|
| | CAD or SID/DP | Up to 180 days |
| | M\$ | M\$ |

| | | |
|--|-----|-----|
| (a) Secured by Unconfirmed Letters of Credit | | |
| (b) Unsecured | | |
| Total | M\$ | M\$ |

Note: In Tables 1 and 2, the figures should exclude any contract in relation to any goods exported thereunder where:

- (i) irrevocable payment in full in Malaysia is made therefor prior to the date of, such exportation or payment is made against documents under an irrevocable letter of credit confirmed before exportation by a Bank in Malaysia.
- (ii) terms of payment exceed 6 months credit.

If more convenient. Actual Turnover of the most recent financial year may be given in Column 2 of Table 1.

4. **OVERDUES** Our current overdues in respect of payments outstanding for more than three months from the due dates are shown hereunder:

| BUYER'S NAME & ADDRESS | Amount | Due Date of Payment: |
|------------------------|--------|----------------------|
| | | |

5. **BAD DEBTS** Our actual losses incurred on all buyers overseas arising only from the insolvency of the buyer or the buyer's failure to pay, for the previous three completed years, and the subsequent period to date have been as follows:

| | For each of the three financial years ending | | | Subsequent period to date |
|-----------------------|--|-----|-----|---------------------------|
| | 19 | 19 | 19 | 19 |
| | M\$ | M\$ | M\$ | M\$ |
| Total bad debts | | | | |
| Total export turnover | | | | |

Note: The total export turnover for each of the respective years should be completed accordingly even if no bad debts were sustained.

6. SIZE OF ACCOUNTS The approximate number of our existing accounts (i.e. Credit Limits) are as follows:

| Number of accounts on secured terms | Number of accounts on unsecured terms | Credit Limits* |
|-------------------------------------|---------------------------------------|---------------------|
| | | Less than M\$1,000 |
| | | M\$ 1,001 M\$ 2,500 |
| | | M\$ 2,501 M\$ 5,000 |
| | | M\$ 5,001 M\$10,000 |
| | | M\$10,001 |
| | | M\$25,000 M\$25,001 |
| | | M\$100,000 |
| | | Over M\$ 100,000 |

* A Credit Limit for any one buyer is the maximum amount outstanding for payment at any one time after the goods have been exported and before they have been paid for.

7. CREDIT CONTROL

| | |
|---|--|
| <p>(a) We give opposite the sources from which we obtain information regarding our buyers or prospective buyers.</p> <p>(b) We check the standing of our buyers with sources at (a) as shown opposite (Delete items not appropriate)</p> <p>(c) The bank and particular branch through which we operate is shown opposite</p> | <p>Intermittently / at regular intervals / rely entirely on our own experience</p> |
|---|--|

8. We have not entered into any contract of insurance or indemnity relating to any contract to which this Proposal applies in respect of any cause of loss covered by the Comprehensive Policy (Shipments) and we will not enter into any such contract of insurance or indemnity without your consent in writing.

9: We are not aware of any circumstances relating to any particular buyer or contract which might adversely influence your acceptance of any of the risks submitted.

10. We agree that, unless otherwise agreed by the Company in writing, the Company shall be under no liability in respect of:

(a) any contract made with any buyer in whose profits we have any interest, direct or indirect, or who has any interest in our business, or

(b) any contract made with any buyer in relation to any goods exported thereunder after we have learnt that he is in financial difficulties or that his position appears to be such as to make exports to him undesirable.

11. We undertake to declare under the terms of the Policy all exports made to any and every buyer in all countries, including those specified in paragraph 3 hereof and any other countries to which we may make exports unless otherwise agreed by the Company in writing.

12, We undertake to carry on our business with due care in making contracts and exports and with due regard to the conditions of the contract and the trustworthiness of the buyer.

13. All discussions and correspondence in connection with this Proposal and with any Policy arising therefrom are to be treated by both sides as confidential, and we undertake not to disclose either the existence of the Policy or any of the details thereof to our agents or to the buyers or to any other person or concern, other than in confidence to our bankers, without the prior consent of the Company in writing.

14. We certify that the representations made and facts stated by us are true, and that we have not misrepresented or omitted any material fact which might have a bearing on the Policy and we agree that such representations and facts shall form the basis of and be incorporated in the Policy and that the truth of such representations and facts and due performance of each and every undertaking contained herein or in the Policy shall be a condition precedent to any liability of the Company thereunder.

Exporter's Name:

Exporter's Address:

.....

Company's -Stamp:

Signature:

Capacity of signatory

Date:

- Note: 1. In the case of incorporated companies this Proposal should be signed by an authorised officer for and on behalf of the company and should state the capacity in which the signatory acts (eg. Managing Director, Secretary).
2. In the case of partnerships this Proposal should be signed by a partner in the firm.
3. In the case of sole proprietorships this Proposal should be signed by the proprietor of the firm.
4. The words NIL' or NOT APPLICABLE' should be entered in any space where appropriate.
NO SPACE SHOULD BE LEFT BLANK.
5. If space in any of the above tables is insufficient, please attach separate SIGNED statements.

SPECIMEN - APPENDIX III

COMPREHENSIVE POLICY
PROPOSAL SUBMISSION
(NEW / RENEWAL BUSINESS)

Name of Exporter _____

Address _____

 _____ Tel. No. _____

Fax No. _____

Proposed Policy Period _____ Ref. No.: _____

Other Policies BEFIP expiring _____ Others _____ Expiring _____

| | | |
|----------------------------------|---|--|
| 1. Type of Company | <input type="checkbox"/> Sole Proprietorship <input type="checkbox"/> Partnership <input type="checkbox"/> Private Limited <input type="checkbox"/> Public Company <input type="checkbox"/> Branch Office Date Incorporated: _____ Date Export Commenced: _____ | |
| 2. Parent (P) and Subsidiary (S) | <input type="checkbox"/> _____ <input type="checkbox"/> _____ <input type="checkbox"/> _____ <input type="checkbox"/> _____ <input type="checkbox"/> _____ | Country _____ _____ _____ _____ _____ |
| 3. Board of Directors | _____ _____ _____ | Designation _____ _____ _____ |
| 4. Management Team | _____ _____ _____ | Designation _____ _____ _____ |

| | | | |
|--|---|---------------------|--------------|
| 5. Capital Structure | Authorised Capital _____ | <u>Ownership</u> | |
| | Paid-up Capital _____ | Bumiputra _____% | Local _____% |
| | | Foreign _____% | |
| 6. Brief Description of goods involved | | | |
| 7. Overdue / Bad Debts Experience (exports only) | Amount RM _____ Due Date _____ Payment Terms _____ | Reasons: _____ | |
| | _____ | | |
| 8. Renewal of Policy a) Past Claim Experience | RM _____ Date Claim Paid _____ | Cause of Loss _____ | |
| | : _____ | | |
| 9. Policy Assignment | <input type="checkbox"/> Required <input type="checkbox"/> Specific Transaction <input type="checkbox"/> Whole Policy <input type="checkbox"/> Buyer <input type="checkbox"/> Country <input type="checkbox"/> Not Required | | |
| Name & Address of the Bank | _____ | | |
| | _____ | | |

10. Proposed Estimated Turnover

| ACTUAL | | | | | | |
|-----------------------|--------------------------|---|--------------------|-------------------|------------------------------|------------------------|
| Countries | Market Grading (Current) | Estimated Export Turnover for past 12 months RM | Export Declared RM | Premium Billed RM | Export for next 12 months RM | Markets to be Excluded |
| | | | | | | |
| | | | | | | |
| | | | | | | |
| | | | | | | |
| | | | | | | |
| | | | | | | |
| | | | | | | |
| Terms of Payment: ILC | | 0 | 0 | 0 | 0 | 0 |
| Non-ILC | | 0 | 0 | 0 | 0 | 0 |
| TOTAL | | 0 | 0 | 0 | 0 | 0 |

11. PATTERN OF BUSINESS OFFERED:

Total Estimated Insurable Turnover RM _____

LESS, if applicable, total value of business in markets with associated companies RM _____

a) **NET TURNOVER FOR " WHOLE TURNOVER" POLICY** RM _____

or **LESS** , if applicable, total value of business in excluded markets or/and ILC terms. RM _____

b) **NET TURNOVER FOR "SELECTIVE BASIS" POLICY** RM _____

Turnover offered in A and B markets RM _____

Turnover offered in C and D markets RM _____

c) **CONTRACTS IN HAND** not yet shipped: Total Value RM _____

12. Assessment of Exporter's Status

Std = Base ("0" Score)

| Criteria | Premium Loading (+ OR -) | | Remarks (if any) |
|-------------------------|----------------------------------|-----|------------------|
| | | | |
| 1. Type of Company | Public / Sdn. Bhd. | Std | |
| | Proprietorship / Sole Proprietor | +5 | |
| 2. Nature of Business | Manufacturer | Std | |
| | Merchant | +5 | |
| 3. Type of Goods | Manufactured/Com. | Std | |
| | Perishable | +10 | |
| 4. Turnover | 1 m and below | +10 | |
| | 1 m to < 3 m | +5 | |
| | 3 m to < 5 m | Std | |
| | 5 m to < 10 m | -5 | |
| | 10 m to 20 m | -10 | |
| | Each 10 m (Additional -10) | % | |
| 5. Exporting Experience | No experience | +10 | |
| | L/C Exports | 5 | |
| | < 3 years | +5 | |
| | < 5 years | Std | |
| | Above 5 years | -10 | |

| | | | |
|-----------------------------|------------------------------|------|--|
| 6. Credit Control | Maintains Credit Department | Std | |
| | Regular Check | -5 | |
| | None | +10 | |
| 7. Overdue as % of turnover | Bad Debts > 5% | +10 | |
| | Bad Debts < 5% | +5 | |
| 8. Spread of business | Whole turnover | Std | |
| | ILC Exclusion | Std | |
| | <50% CAD | +5 | |
| | DP Exclusion | +10 | |
| | Selective Market | +10 | |
| | Divisional Cover | +10 | |
| | One Market | +20 | |
| | One Buyer | +20 | |
| 9. Performance (Renewal) | | | |
| a) Premium Contribution | > RM20,000 | - 10 | |
| | > RM 5,000 | -5 | |
| | < RM 5,000 | Std | |
| b) Claims Experience | > RM10,000 | +10 | |
| | > RM 5,000 | Std | |
| | Nil | - 5 | |
| c) Premium Payment | Outstanding | +5 | |
| | Nil if contribution >RM5,000 | - 5 | |
| | Others | Std | |

13. Remark(s) [if any]

a) Premium Contribution RM _____ Premium Outstanding RM _____

| | | | |
|------------------------------------|--------------------------------|----|-------|
| | Tax | RM | _____ |
| b) Coverage: % to be offered _____ | Exporter's gross profit margin | | _____ |
| | Exporter's net profit margin | | _____ |

c) Any comments on markets / Countries

Subject is continuing the policy to cover their export to Iran on D/P for sale of TV sets for USD 200,000.00 of which 10% is paid in advance. No declaration was made during the last policy years.

Recommended to be approved. Renewal Fee: RM 100.00 (To be deducted from provisional premium).

Premium Rate: a) 1.5% on gross invoice value of goods exported to approved buyer in Russia

b) 4.0% on gross invoice value of goods exported to approved buyer in Iran.

Underwritten by : Signature

Name :

Date :

SECTION 5

MEDIUM AND LONG TERM TRADE AND PROJECT INSURANCE AND FINANCING

**CHAPTER I O.E.C.D ARRANGEMENT ON GUIDELINES FOR
OFFICIALLY SUPPORTED EXPORT CREDITS -
SYNOPSIS**

**CHAPTER II MEDIUM / LONG TERM TRADE INSURANCE AND
FINANCE - SYNOPSIS**

APPENDIX 1

**CHAPTER III PROGRAMS OF THE U.S.A. EX-IM BANK DIRECT
LOANS AND GUARANTEES**

APPENDIX 1 EXPOSURE FEES

APPENDIX 2 CASE STUDIES

**CHAPTER IV PROJECT FINANCING - JAPANESE
INVOLVEMENT**

CHAPTER V THE KOREAN APPROACH

CHAPTER I

O.E.C.D. ARRANGEMENT ON GUIDELINES FOR OFFICIALLY SUPPORTED

EXPORT CREDITS*

- SYNOPSIS

LOAN STRUCTURE - ARRANGEMENT

- Amount of cash payment
- Minimum interest rates
- Maximum repayment term
- Level principal payments
- Starting point & pattern of repayments

CONCEPTS: ARRANGEMENT

- Commercial Interest Reference Rate (CIRR)
- Tied Aid
- United Aid
- Cosmetic Interest Rate
- Local Cost

CHAPTER II - SYNOPSIS

Buyer and Seller/Supplier Credit Finance.

CONTENTS

- What is Buyer and Seller / Supplier Credit Finance?
- Reasons for and consequences of using Buyer and Seller / Supplier Credit Finance
- Implications for Buyers and Sellers / Suppliers and Financiers

- Parties involved in Buyer and Seller / Supplier Credit Finance
 - Buyer
 - Seller / Supplier
 - Financier
 - Guarantor / Insurer

- Arrangements needed for Buyer and Seller / Supplier Credit Finance
 - Commercial Contract
 - What is required in a Commercial Contract
 - Loan Agreement
 - What are the features of a Loan Agreement
 - Agreement between Seller / Supplier and Financier
 - Guarantee(s)
 - Insurance Cover

Buyer and Seller/Supplier Credit Finance.

I. a) What is Buyer Credit Finance?

Arrangement when for medium/long term finance:

- Buyer purchases capital goods and services from a Seller/Supplier under a Commercial Contract, which provides for payment to the Seller/Supplier as it performs or on completion of its contractual obligations.
- Buyer enters into separate arrangements with a Financier or Financiers, which provide or arrange funds to finance the payments to the Seller/Supplier.
- Can allow for tax effective financing arrangements, e.g. leasing, capital markets, multilateral agencies and export credit agencies.
- Can be used for purchase of individual items of equipment, projects or lines of credit.

I. b) What is Seller/Supplier Credit Finance

Arrangement when:

- Buyer purchases capital goods and services from a Seller/Supplier under a Commercial Contract, which provides for payment to the Seller/Supplier over time after the Seller/Supplier has performed its contractual obligations.
- Seller/Supplier funds the deferred contract payments from its own balance sheet or enters into separate arrangements with a Financier, which provides the funds to finance the payments to the Seller/Supplier under the Commercial Contract.
- Financing options not always as flexible.
- Financing terms influenced by financial strength of the supplier.
- Most suitable for purchase of individual items of equipment.

II. a) Reasons for and consequences of using Buyer Credit Finance.
i. Type of project being financed. A project with multiple suppliers may be easier to finance.

ii. Separation of supply contract and finance arrangements allow both to be negotiated separately and the real cost of both equipment and finance to be clear. Reduces possibility of cross subsidisation.

Buyer can negotiate financing structure most suited for the project.

Separates commercial and financial rights and obligations.

iii. Seller/Supplier avoids having to also act as Financier.

The Seller/Supplier is not required to assume the role of Financier or to deal with Financiers with respect to the period after project completion. Less likely to have to accept some residual liability for the finance provided.

iv. Can allow Buyer to more easily control finance and coordination of finance terms when multiple sourced equipment supply is involved.

II b) Reasons for and consequences of using Seller/Supplier Credit Finance.

i. Financial strength of the Seller/Supplier

If the Seller/Supplier is financially strong, better financing terms may be secured.

ii. Type of project being financed

If the project being financed has a relatively simple structure, for example involving supply only, the simplicity of Seller/Supplier Credit Finance may be attractive.

The value of the project may be too small to warrant the cost of the Buyer negotiating finance directly with Financiers.

iii. Seller/Supplier rather than Buyer has to organise finance.

The Seller/Supplier is required to assume the role of Financier or to deal with Financiers with respect to the period after project completion. Buyer only has obligations of creditor, not borrower. Seller/Supplier may have to accept some residual liability for the finance provided.

Buyer can avoid the need to negotiate separate finance and commercial terms and agreements.

III Parties involved in Buyer and Seller / Supplier Credit Finance

a) Buyer

- Party undertaking project involving purchase of capital equipment and / or services.
- If an established company and project relates to an existing facility or plant it may be able to fund purchase from balance sheet. However using balance sheet may not be most efficient use of capital - should be able to generate a return greater than the cost of borrowing. Similarly return from asset for which funds borrowed should be greater than cost of funds.
- If a major new project is being undertaken a new project company may be established, which might then not have a balance sheet that can support financing the project. In that case the buyer will certainly need debt finance with repayment dependent on the project revenues.

- May wish to negotiate the price of capital equipment and / or services separately from price of finance to avoid possibility of cross-subsidisation.
 - Negotiating finance directly may allow the buyer to coordinate financing facilities more easily than with Seller / Supplier Credit Finance and allow access to a wider range of financing options.
 - The buyer may not always be the borrower for Buyer Credit Finance.
- b) Seller/Supplier. Role is supplying equipment and services for the project, not acting as financier.
- Will usually prefer to have obligations limited to period of supply and warranty irrespective of whether Buyer and Seller/Supplier Credit Finance.
 - Depending upon size of company, it may not have balance sheet to provide Seller/Supplier Credit Finance.
 - It may not have the capacity to assume any administrative obligations during the repayment period, and will usually want to avoid any residual liability after the supply and warranty periods are completed.
 - Will usually seek trade insurance, etc. against risks of non-payment during the post-completion period.
- c) Financier
- Since the financier is assuming the risk on the capacity of the Buyer to meet its repayment obligations may prefer to deal directly with the Buyer. Separating commercial contract and finance reduces commercial disputes affecting repayment obligations.

- Dealing directly can allow closer monitoring of performance during the performance and repayment periods.
 - Seller / Supplier Credit Finance can avoid the need to negotiate detailed documentation which may not be cost effective. The financier may provide finance under Seller / Supplier Credit Finance and may require non-payment trade insurance or guarantee. The Financier may take direct risk on the Buyer repaying the loan, may reinsure, or may obtain insurance from an export credit agency or commercial insurers.
- d) Guarantor/Insurer
- Provides insurance or guarantees to the Financier and/or Seller / Supplier in relation to the risks of non-payment by the Buyer.

IV. Agreements needed for Buyer and Seller/Supplier Credit Finance. **Commercial Contract.**

What is required in a Commercial Contract?

- Details of the parties to the contract.
- Detailed description of the goods and services to be supplied by all parties to the contract, including land at project site and access to the site.
- Detailed description of the objectives of the contract.
- Details of the shipping and delivery arrangements.
- Detail schedule for all aspects of project implementation.
- Obligations of all parties with regard to the payment arrangements under the contract.
- Mechanism for dispute resolution and contract law.
- Date for the contract to become effective.

- Details of Buyer's obligations such as import licences, approval to borrow and repay foreign currency, etc.
- Agreement as to who carries the foreign exchange risk.
- Compliance with local laws.
- Details on inspection arrangements.
- Details of arrangements for contract variations.
- Clarity.
- Force Majeure.
- Language to apply.
- Enforceability.

For the supply of standard type equipment the contract may be limited to details of goods to be supplied, the currency of payment, the amount to be paid, delivery requirements and method of payment.

Loan Agreement.

What are the features of a Loan Agreement?

- Loan Agreement can be between Financier and Buyer under Buyer Credit Finance or between Financier and Seller/Supplier under Seller/Supplier Credit Finance. Other parties can also be signatory to the Agreement if required, e.g. parent companies of Buyer or Seller/Supplier.
- States the purpose for which the funds can be borrowed.
- Sets out conditions under which funds can be borrowed and basis on which they must be repaid.
- Sets out circumstances when Financier will be entitled to treat the Borrower as being in default.

- States the amounts to be repaid, the dates for payment, the rate of interest payable and the currency of payment.
- States any costs and fees to be paid.
- States the law to apply and the language of the Agreement.
- States what the Borrower represents and warrants.

Agreement between Seller/Supplier and Financier.

Sets out the rights and obligations of all parties during the contract performance and repayment periods.

Guarantee(s)

A Guarantee can be provided by a third party in the Buyer's country or by a credit insurer or guarantor in respect of risk of non-payment by the Buyer.

Trade Insurance Cover

Trade insurance provided by a credit insurer in respect of risk of non-payment by the Buyer.

APPENDIX I

A: THE CREDIT FACILITY

The credit facility and its permitted uses

A1 We will lend you money to help you finance part of the amount payable under the export contract described in item 2 of the Schedule. We will do so by way of a single drawdown or a series of drawdowns. The total amount of all drawdowns will not be more than the amount set out in item 3 of the Schedule. You must not use money we lend you under this credit facility for any purpose except to finance the contract with the exporter to buy:

- new capital goods wholly manufactured or produced in Australia, and
- services provided wholly by people usually resident in Australia.

A2 If the exporter named in item 2 of the Schedule has disclosed the origin of the following types of goods or services to us and we have agreed, you may use the credit facility to finance these goods and services under the contract:

- goods which are only partly manufactured or produced in Australia; or
- services that are only partly provided by people who are resident in Australia;
or
- goods or services from the country named in item 6 of the Schedule valued at up to the amount in item 7 of the Schedule; or
- goods or services from somewhere other than Australia or the country named in item 6 of the Schedule.

It is entirely up to us to decide whether to give that permission.

B: DRAWDOWNS UNDER THE CREDIT FACILITY

We must receive a request for a drawdown under this credit facility

B1 Before we make a drawdown under this credit facility, we must receive a request for a drawdown that is substantially in the form set out in Attachment 1. We will make the drawdown *if* it is within the amount available under this credit facility, *if* it is to be made during the drawdown period set out in item 4 of the Schedule, and *if* the conditions set out in clauses B2-B6 below are met.

- 1.1 If a drawdown is to be paid to the exporter, the exporter must make the request, and the drawdown must be approved in writing by you or approved on your behalf.
- 1.2 If a drawdown is to be paid to you (because you have already paid the exporter the relevant amount) you must make the drawdown request.
- 1.3 Drawdowns will be in United States dollars.

Conditions to be met before the *first* drawdown is made

B2 We do not have to make the first drawdown under this credit facility until each of the following conditions is met.

- 2.1 We are satisfied that the export contract is acceptable from our point of view as a lender.

2.2 We have received, and have accepted as satisfactory, each of the following:

- a legal opinion from a lawyer approved by us which is substantially in the form set out in Attachment 2.
- a signed agreement between us and the exporter relating to the export contract and this agreement.
- specimens of the usual signatures of each person authorised to sign on your behalf (see for example Attachment 3).
- specimens of the usual signatures of each person authorised to sign on behalf of the exporter.
- evidence that the Central Bank of the country named in item 6 of the Schedule has authorised you to enter into this agreement and has approved the borrowing, if an authority or approval is required.
- evidence that any currency or exchange control requirements that apply in relation to this agreement or which you need to carry out your obligations in relation to this agreement and which can be obtained now, have been obtained and satisfied.

2.3 You have paid us all the fees and charges that are due under this agreement in accordance with clause C.

2.4 We are satisfied that any approval required in relation to the export contract, or your performance of this agreement, has been obtained.

2.5 You have paid the exporter the non-refundable deposit set out in item 5 of the Schedule.

No drawdown until we approve documents

B3 We will not make any drawdown under this credit facility unless we have approved the following documents relating to the request for the drawdown:

- the exporter's declaration required under the agreement between us and the exporter.
- if the drawdown is to be paid to the exporter, documents which prove that the exporter is entitled to a payment under the export contract.

if the drawdown is to be paid to you, documents which prove that the exporter was entitled to a payment under the export contract and that you have paid the exporter the amount in question.

No drawdown in case of payment default or other adverse event

B4 We will also not make any drawdown under this credit facility if any of the following has happened:

- 4.1 You have defaulted in making a payment under this agreement for 5 days after it became payable.
- 4.2 One of the other events listed in clause D has happened or we reasonably expect it to happen.
- 4.3 The exporter is in breach of its agreement with us.
- 4.4 We have received evidence that a dispute exists in relation to the export contract, unless you have specifically authorised us to make the drawdown despite the dispute and we agree to do so.

No drawdown unless in accordance with money limits

B5 We will not make a drawdown in any of the following cases.

- 4.1 The drawdown sought is for an amount that is more than the exporter is entitled to be paid at the time under the export contract
- 5.2 The request is for a drawdown of less than US\$50,000, unless the drawdown is for the balance of the credit facility, or is to be the last drawdown.
- 5.3 The request for a drawdown is in relation to costs to be incurred in your country, and, together with all other drawdowns in relation to such local costs, the drawdown would be more than the amount set out in item 7 of the Schedule.
- 5.4 The export contract has been altered, or you have permitted it to be performed, in a way that affects its nature, level of Australian content, scope, price, or time for performance.

Payment of drawdowns

B6 Drawdowns will normally be paid to the exporter. However, if you have already paid the exporter, we will pay the drawdown to you.

C: YOUR PAYMENT OBLIGATIONS

You must repay the drawdowns

C1 You must repay the drawdowns. You must repay by installments. Installments must be paid on the dates set out in item 12 of the Schedule. The amount of each

installment is to be the total of all drawdowns made under this agreement, divided by the number in item 13 of the Schedule.

You must pay interest

C2 You must pay interest on the amount of the drawdowns you have yet to repay.

2.1 Interest accrues daily.

2.2 The rate depends on whether you have chosen a fixed rate or a floating rate. The rate may also depend upon the interest period (a term we explain below). You should choose between the fixed and floating rate and notify us in writing of your choice by the day you sign this agreement. If you don't choose or you don't notify us on time, the floating rate will apply.

2.3. You must pay accrued interest on the dates set out in item 9 of the Schedule.

Calculating the interest rate

C3 If you have chosen the fixed rate, the rate of interest for the entire term of the loan is set out in item 10 of the Schedule.

If you have chosen the floating rate:

3.1 For the first interest period for each drawdown the interest rate is the rate chosen by us in our absolute discretion using the display page "LIBO" of the Reuters Monitor System at about 11am London time two business days before the beginning of the first interest period (rounded upwards, if necessary, to the nearest four decimal places) plus the margin specified in item 11 of the Schedule. The first interest period for each drawdown begins on and includes the day of the drawdown. It ends on and includes the day before next date for payment of interest set out in item 9 of the Schedule.

- 3.2 After the first interest period for each drawdown, the interest rate is 6 month LIBOR plus the margin specified at item 11 of the Schedule. The second and later interest periods begin on and include each date for payment of interest set out in item 9 of the Schedule and end on and include the day before the next date for payment of interest.
- 3.3 6 month LIBOR means, in relation to an interest period, the annual percentage rate of interest determined by us as the average of the offered rates of all banks appearing on the display page "LIBO" of the Reuters Monitor System for a period of 6 months at about 11 am (London time) two business days before the beginning of the interest period (rounded upwards, if necessary, to the nearest four decimal places).
- 3.4 If the display page "LIBO" of the Reuters Monitor System is unavailable, LIBOR will be the rate quoted to us by a reputable bank selected by us in our sole discretion.
- 3.5 If you have chosen the floating rate, you may elect to change to a fixed rate instead at any time until 1 year before the last date set out in item 12 of the Schedule. However, you cannot exercise this choice if you are not in compliance with all your obligations under this agreement or if an event has happened (or is more likely than not to happen) which entitles us to accelerate the repayment of all drawdowns. (Please refer to clause D1).

To change to a fixed rate, you must notify us 30 days before the first date for payment of interest from which you want the fixed rate to apply. Your notification, once given, is irrevocable. The fixed rate will apply until the loan is repaid and you cannot change back to a floating rate or change to another fixed rate. The fixed rate will be the rate nominated by us as the applicable fixed rate on that date for payment of interest under the "Arrangement On

Guidelines For Officially Supported Export Credits" plus the margin specified at item 11 of the Schedule.

- 3.6 A rate per cent (%) per year referred to in this agreement or in the Schedule, or calculated under this agreement or the Schedule, is the rate per cent (%) for a year of 360 days, not 365.

You must pay a commitment fee

C4 You must pay us a commitment fee on the amount set out in item 3 of the Schedule which, at any particular time, we have not lent to you.

The charge is 0.25% per year, accruing daily from the date of this agreement until (and including) the last day of the drawdown period in item 4 of the Schedule.

- 4.1 You must pay the accrued charge on those of the dates set out in item 9 of the Schedule that fall within the drawdown period and on the first of those dates to occur after the end of the drawdown period.

Fees, taxes, costs and expenses

C5 You must pay us each of the following amounts within 7 days after we send you a request for payment:

- the establishment fee set out in item 8 of the Schedule.
- our legal and incidental costs (including reasonable costs for the work done by our in-house lawyers) in connection with any aspect of the credit facility or your transaction with the exporter, including the legal opinion referred to in clause B2.2.
- stamp duty and any other tax payable in relation to this agreement or the credit facility it establishes.

- reasonable costs incurred by us for a consultant or one of our Australian based employees to make an annual visit to premises you occupy or any site connected with the export contract in order to inspect your business or assets.
- Our costs in connection with any event which has happened (or is more likely than not to happen) which entitles us to accelerate the repayment of all drawdowns (please refer to clause D.)\
- Our costs in connection with the administration, enforcement or attempted enforcement or protection of our rights in relation to this agreement.

5.1 You must pay each of these amounts in United States dollars, or in another currency we specify

Your payments must not be Subject to deductions

C6 You must make sure that nothing is deducted or withheld from any amount due Under this agreement. In particular you must not reduce it by any set-off or counterclaim .

6.2 If a law requires you to deduct tax or any other amount of any kind from an amount due or payable to us, and you deduct that amount before paying it to us, then you must separately pay us enough to ensure that we receive the full amount due to us under this agreement. You must make this separate payment just before you pay the amount from which the deduction is made.

6.2 You must make sure that we do not receive less than the amount due or payable to us because of the deduction of bank charges.

Only we have a right of set-off

C7 We are entitled to set off any amount you owe us against any payment we are to make to you. However, you are not entitled to set off any amount we are to pay you against any amount you owe us.

You take the risk that your payments to us can be avoided

C8 If we have to pay an amount to someone else because a payment that you made to us is, or may be, avoided by operation of law, you must pay us that amount again on demand. This obligation continues even after this agreement is terminated.

How to make payments to us

C9 **You must make any payment to us under this agreement on the following conditions**

9.1 Pay in United States dollars, or in another currency we have nominated in writing.

9.2 Deposit the payment to the following bank account:

| | |
|---------------|--|
| Account Name: | Export Finance and Insurance Corporation |
| Bank: | Bank of New York, New York |
| Account No: | 890-0330-813 |
| Fed ABA: | 021000018 |
| Chips No: | 0001 |
| SWIFT: | IRVTUS3N |

or to any other bank account we have notified to you.

9.3 Your deposit must become available for our use no later than 12 noon (New York time) on the due date.

- 9.4 If payment is due on a day which is not a business day, you must pay on the next business day. Business day or date means a day on which banks are open for domestic and foreign exchange business in London and New York.
- 9.5 You must pay the amount due on time, even if we do not give you notice of the amount due.

You must reimburse our currency losses

C10 If, for any reason, you pay us in a currency other than United States dollars, or another currency which we have specified in writing, we will convert the amount we receive from you into United States dollars or that other currency as soon as we can. We will notify you of any shortfall between the amount we receive after that conversion was due under this agreement. You must immediately pay the shortfall to us in United States dollars or that other currency due under this agreement

10.1 The conversion will be at the rate quoted to us by the bank which is performing the conversion for value on the day we deliver the other currency to that bank. We can choose any bank we like to perform the conversion.

10.2 If we suffer a loss because a judgment or order of a court or tribunal is based on an exchange rate which does not reflect the rate we certify to be the buying rate for United States dollars or that other currency on the date or dates payment is required under the terms of this agreement, we will notify you of the amount of our loss. You must immediately pay that loss to us in United States dollars or that other currency. In determining the buying rate for United States dollars or that other currency on a date we will rely on a rate quoted to us (either before or after the date in question) by a reputable bank we select in our sole discretion.

Rules for early repayment

C11 You can repay all - or part of - the drawdowns early if:

- 11.1 you give us 30 days irrevocable notice in writing of your intention to make an early repayment,
- 11.2 the amount to be paid to us is not less than the amount of an installment calculated in accordance with clause C1, and
- 11.3 the payment is made on one of the dates set out in item 12 of the Schedule.

You must pay our funding losses in connection with early or late repayment

C12 You must pay us, and keep us indemnified against, all funding losses connected with this credit facility, if:

- you pay or repay us early,
- you pay or repay us late, or
- we give you notice requiring immediate repayment of all drawdowns not repaid.

Those funding losses include all our losses plus all our expenses less all gains to our account whether incurred or foregone, in connection with:

- our changing, rearranging or ending any financial arrangements entered into by us,
- or to which we are committed, in relation to the funding of this credit facility, our closing out, re-arranging or unwinding of transactions in the nature of futures contracts, swaps/ foreign exchange agreements, forward rate agreements, options or hedge agreements or arrangements having similar purpose or effect,

- Our paying interest or giving up the right to receive interest, and
- identifying the losses, expenses or gains

Financial arrangements include financial arrangements that involve amounts greater than the amount of this credit facility.

How payments are to be allocated

C13 We will allocate any amount which you pay us – or which someone else pays us on your behalf – in relation to this agreement in the following order:

1. fees, taxes, costs and expenses payable under clause C5,
2. commitment fees,
3. interest on overdue amounts (Please refer to clause E),
any other amounts due in relation to this agreement, except interest and repayment of drawdowns,
4. interest,
5. repayment of drawdowns.

D: ACCELERATION OF PAYMENTS ON DEFAULT OR OTHER ADVERSE EVENT

Acceleration of payments

D1. We are entitled to accelerate the repayment of all drawdowns under this agreement and all accrued interest if you default in making any payment for 5 days after the payment became payable, or if one of the other adverse events listed in this clause occurs. When we give you notice of acceleration, you must immediately pay us all drawdowns not already repaid, together with accrued interest and any other payable amount under this agreement.

- 1.1 You have failed to comply with an obligation (other than a payment obligation) or breached a term or condition of this agreement for 10 days.
- 1.2 A representation or warranty by you proves to be materially incorrect.
- 1.3 The export contract has been altered, or, you have permitted it to be performed, in a way that affects its nature, level of Australian content, scope, price, or time for performance.
- 1.4 We have become entitled (subject to giving notice or any period of grace) to declare that all money owing under another agreement with you is immediately due and payable.
- 1.5 You have disposed of or encumbered any right you have either under this agreement or under the export contract.
- 1.6 You have become liable to someone other than us, either in your own right or as a surety, because of your default or someone else's in paying money when it became payable and you have failed to pay the amount for which you are liable.
- 1.7 You have stopped carrying on business (or a material part of your business), or have undergone a reconstruction or amalgamation of your corporate structure, assets or undertaking, or have threatened to do any of these things, without first getting our written approval.
- 1.8 Someone has resumed, appropriated, expropriated, confiscated, nationalised, acquired, or taken custody, possession or control of all or a material part of your issued capital or assets.
- 1.9 You have stopped payment of your debts generally or stopped payment of a class of debts, or- have reduced or tried to reduce your capital (except from a

share premium account) or you have made or tried to reduce your uncalled capital incapable of being called up.

1.10 Distress or execution for more than US\$50,000 (or its equivalent in another currency) has been levied or attempted on you or any of your assets, or an encumbrance has become enforceable against you or any of your assets.

1.11 Any of the following has happened:

- You have declared a moratorium on payment of your debts.
- You have admitted that you are unable to pay your debts as they become due.
- You have gone into liquidation or provisional liquidation or have become bankrupt.
- A resolution has been passed or you have a petition made against you (which is not frivolous and/or dismissed within 14 days) for your winding up.
- You have gone into controlled, extraordinary or insolvent administration.
- An administrator, custodian, judicial manager, receiver or receiver-manager has been appointed to you or any of your assets.
- You have entered into a reorganisation, composition, assignment or arrangement with, or for the benefit of, your creditors or a majority of them.
- An order for distress, execution or sequestration has been made against you.
- You have done something, or something has happened, which is similar in effect to any of the events listed above.

- You have taken irreversible action to achieve or enable any of the happenings listed above.

1.12 The person or persons who have effective control of you when this agreement is entered into cease to have effective control of you.

1.13 A security that you have given for the performance of your obligations under this agreement, or a third party's guarantee or indemnity given in relation to that performance:

- becomes enforceable, or
- is, or is arguably, void, voidable or unenforceable.

1.14 A government authority or approval in connection with this agreement or the export contract has been withdrawn, has lapsed or has been made subject to conditions which are not acceptable to us.

1.15 Any event or combination of events occurs which we reasonably believe have a material adverse effect on you or your ability to comply with this agreement.

Time of notice

D2 We can give notice of accelerating payments at any time after we are entitled to accelerate, even if other things have happened since your default or the happening of the other adverse event. However, we cannot give notice if the default or other adverse event is not continuing

E: CONSEQUENCES OF BREAKING THE CONDITIONS IN THIS AGREEMENT

E1 You must pay a special rate of interest on amounts not paid on time

1.1 You must pay extra interest on any amount that you do not pay on time. A special rate of interest applies since our risk is greater when you do not pay on time than when you do pay on time - partly because it is risk we did not expect to happen, and partly because the risk of lending to a person who has not kept a promise to pay on time is higher than lending to a person who has. This special rate is designed as a genuine pre-estimate by both of us of the risk-based cost to us of being paid late and the extra risk we carry by lending to a person who has failed to pay on time.

1.2 This interest accrues daily. It is payable on demand made by us.

1.3 We determine the special rate of interest as follows.

- the special interest rate applicable to the amount that you did not pay on time is the rate 1% higher than one month LIBOR plus the margin specified at item 11 of the Schedule for so long, as you do not pay us in full.
- one month LIBOR means:
 - the annual percentage rate of interest determined by us to be the average of the offered quotations for a period of approximately one month of all banks appearing on the display page "LIBO" of the Reuters Monitor System at about 11 am (London time) on the relevant setting date (rounded upwards, if necessary, to the nearest four decimal places).
 - The setting dates will be:
 - the date two business days before the day the payment in question should have been made and
 - the same day of each following month (or if that day is not a business day, the next business day) until we are paid - in full - the

amount which was not paid on time plus interest accrued at the special rate.

- If the display page "LIBO" of the Reuters Monitor System is unavailable, LIBOR will be the rate quoted to us by a reputable bank selected by us in our sole discretion.

E2 In addition to amounts payable to us under clause E1, you must pay us for any funding losses under clause C12.

E3 You must also pay us any costs we incur enforcing or attempting to enforce our rights under this agreement or any document provided in relation to it.

- 3.1 Those costs will include costs of travel by our representatives, accommodation for our representatives, legal costs (as billed to us by our internal and external lawyers), notaries' costs and consultants' costs. We do not need to obtain your prior approval or consult you in any way before incurring these costs.

F: **YOUR REPRESENTATIONS, WARRANTIES AND UNDERTAKINGS**

Your representations and warranties

F1 You make the following representations and warranties to us each time you request a drawdown, and each time an amount becomes payable by you. We rely on your representations and warranties in making a drawdown and in deciding whether or not to exercise our right to accelerate payments.

- 1.1 You are a legal person with capacity to enter into and perform all your obligations under this agreement and the export contract. You do not have immunity from the jurisdiction of any court or from any legal process.

- 1.2 You have obtained and undertake to maintain all authorisations and approvals that are needed for you to enter into this agreement and the export contract and to perform your obligations under them.
- 1.3 In entering into this agreement and the export contract, you will not exceed your powers, or breach any law or regulation in any place, or breach any order or obligation, which binds you or your assets.
- 1.4 Your obligations under this agreement and the export contract are binding and enforceable and there are no steps you could take to avoid them.
- 1.5 You have fully and accurately disclosed to us in writing everything which is material to our assessment and acceptance of the risks we undertake in this agreement.
- 1.6 Each person on your list of specimen signatures has authority to sign a document on your behalf until we receive written notice from you withdrawing that authority.
- 1.7 There has been no default or other adverse event, and no material event which could lead to a default or other adverse event, apart from any that you have told us about in writing,
- 1.8 You are not aware of any litigation, threatened litigation or dispute involving you or anyone else that might seriously affect your ability to comply with any of your obligations under this agreement or the export contract.
- 1.9 There is no outstanding dispute in relation to the export contract.
- 1.10 The export contract has not been altered/ and you have not permitted it to be performed, in a way that affects its nature, level of Australian content, scope,

price, or time for performance except after obtaining our prior written approval.

1.11 Your most recent audited financial statements give a true and fair picture of your financial position, disclose all your liabilities (actual and contingent) and any encumbrances on your assets, and have been prepared in accordance with generally accepted accounting principles and practices consistently applied in the country of your business.

1.12 There has been no material adverse change in your financial position or operations since your most recent published and audited financial statements.

1.13 You are not a trustee of any trust, except one which you have told us about in writing and which we have approved.

Your undertakings

F2 You undertake to do each of the following:

2.1 To give us written details of any of the following events as soon as you become aware of them:

- an adverse event listed in clause DI, or another event which might lead to an adverse event.
- a dispute in relation to the export contract.
- any circumstance beyond your control which is likely to prevent you from making a payment under this agreement.

2.2 To take all reasonable steps to overcome any event, dispute or circumstance referred to in F2.1, and to keep us informed of your progress.

- 2.3 Not to assign, dispose of or encumber any of your rights or benefits under this agreement.
- 2.4 To provide us promptly with any report or information we reasonably require in relation to you, the exporter or the performance of the export contract.
- 2.5 To allow us at any reasonable time to inspect, your books, records and accounts relating to the export contract and any goods supplied under it; and to give us your full co-operation in relation to our inspection.
- 2.6 Not to incur liabilities, or to reduce your assets, or to conduct your business, in a way which would prejudice your ability either to comply with your obligations under this agreement or the export contract, or to pay your debts.
- 2.7 Not to dispose of or encumber a substantial part of your assets without our prior written consent except in the ordinary course of business. -
- 2.8 Not to permit a substantial change to occur in your business or business activities.
- 2.9 To provide us, as soon as they become available, but in any case within 120 days after the end of each financial year, with a copy of your audited financial statements as at the end of the financial year.
- 2.10 To arrange and maintain (for as long as any amount remains due to **us** in connection with this credit facility) a policy of insurance which is acceptable to us and is with an insurer we have approved; and which covers you - to their full insurable value - against loss of, or damage to, all the goods to be supplied under the export contract.
- 2.11 To comply with all of your obligations in connection with the policy of insurance; to promptly give **us** a copy of the policy and any renewal of it; to notify us promptly of any event which could give rise to a claim; to make any

claim diligently; to do everything we reasonably require in relation to making a claim under the policy; and to inform us regularly in connection with all claims made.

F3 You now assign to us proceeds of claims under the insurances required under clause F2.11, and promise promptly to notify each insurer of our interest, and to ensure that the policy:[LGLDK1]

- names us a co-assured, and
- requires the insurer to pay us, in priority to anyone else, any claims proceeds. Where a claim is paid for the total loss of the goods insured, you agree that the claim payment will be used to reduce your obligations under this agreement.

G: MISCELLANEOUS

We make no representations etc

G1 We make no representations of any kind to you and give you no warranties of any kind in relation to the export contract. You acknowledge that you have not relied on any representation made by us. Your obligations under this agreement do not depend on the exporter's performance of the export-contract.

Time for currency exchange

G2 Unless an exchange rate is specified for that purpose, any amount which needs to be converted into another currency will be converted at the rate quoted to us for value on the conversion day by a reputable bank which we choose, at our discretion.

Proof

G3 You acknowledge that a notice from us stating that an amount is payable under this agreement, nominating an interest rate or stating how we arrived at an interest rate, is sufficient proof that the amount is payable or the interest rate is correct.

Notices

G4 We must give one another any notice or other information in English and at the addresses set out in item 1 of the Schedule, or at a substitute address that is notified to the other party in writing. This may be done by delivery, by post, by fax or by telex.

4.1 A fax is only effective if the sender's machine prints a report that the whole fax has been successfully transmitted to the recipient's fax number, or to a substitute number notified to the other in writing.

We may require original documents in relation to a request for a drawdown.

Severability

G5 If any part of this agreement is illegal, void, voidable or unenforceable, it is to be deleted and is not to affect the operation of the rest of this agreement. We must both negotiate in good faith to amend this agreement to replace as far as possible the part deleted.

Choice of law and jurisdiction

G6 This agreement is governed by the law of New South Wales, Australia. You submit unconditionally to the jurisdiction of the courts of New South Wales and any other courts in Australia or elsewhere which we, in our absolute discretion, choose. You will not object to the jurisdiction of any of those courts or argue that it is not a convenient forum.

Waiver of sovereign immunity etc

G7 You waive any right you have or may obtain to rely on sovereign immunity or any other immunity from the jurisdiction of a court or from legal process of any kind affecting you or your assets. You acknowledge that entering into this agreement and the export contract, and exercising rights and performing obligations under them, are commercial activities of yours.

Entire agreement

G8 This is the entire agreement between us. It supersedes any earlier agreement or understandings.

Waiver

G9 We may waive any of our rights under this agreement. We are not to be treated as having waived any of your obligations or our rights unless we do so in writing. A waiver by us of any obligation or default by you does not affect your obligations in relation to subsequent performance.

Curing technical defects

G10 We must both do our best to fix or make up for any technical defects in this agreement and in any related agreement or document which might affect their enforcement.

Assignment of rights

G11 We may assign our rights under this agreement without reference to you. You may only assign your rights with our prior written consent which we may withhold at our discretion.

Copy to exporter

G12 We may give a copy of this agreement to the exporter

Authority to fill in blanks

G13 You authorise us to fill in any blanks and make any necessary insertions in the Schedule.

EXECUTED AS A DEED

SIGNED SEALED and
DELIVERED for and on behalf]
of the [] by]
its Attorney/Authorised Officer]
in the presence of:]

Name: _____

Title: _____

Name: _____

Witness

SIGNED SEALED and]
DELIVERED for and on behalf]
of the **EXPORT FINANCE**]
AND INSURANCE]
CORPORATION by its]
Attorneys/Authorised Officers]
in the presence of:]

Name: _____

Title: _____

Name: _____

Witness

Name: _____

Title: _____

SCHEDULE TO THE CREDIT AGREEMENT

BETWEEN

EFIC and []

Dated [] 199[]

Item 1

Your and our details

| | US | YOU |
|------------------------|--|-----|
| Name | Export Finance and Insurance Corporation | |
| Current street address | Level 5, 22 Pitt Street, Sydney NSW 2000 AUSTRALIA | |
| Telex number | 121224 | |
| Facsimile number | 61 2 9201 2290 | |

Item 2

Details of the Export Contract

| | |
|--------------------------|--|
| Exporter's name | |
| Current street address | |
| Type of goods & services | |
| Date of Contract | |
| Contract Price | |

Item 3

The maximum amount of the credit facility is US\$

Item 4

The drawdown period commences on the date of this agreement and ends on
__ / __ / 199__

Item 5

You must pay the exporter as a non-refundable deposit not less than US\$

Item 6

Your country is

Item 7

The maximum amount of local costs (that is, costs to be incurred in your country) that
can be funded from the credit facility is US\$

Item 8

The establishment fee is US\$

Item 9

The dates for payment of interest are 15/__/199__ and each

subsequent 15 [] and 15 [] for as long as amounts remain due or payable to EFIC in connection with this agreement. However, if any of these dates falls on a day which is not a business day, the next business day will be taken to be the relevant date for payment of interest.

Item 10

The fixed interest rate is [] % per year.

Item 11

The margin is []

Item 12

The dates for payment of instalments of principal are

| | |
|------------|------------|
| 1. / / 199 | 8 / / 199 |
| 2. / / 199 | 9 / / 199 |
| 3. / / 199 | 10 / / 199 |
| 4 / / 199 | 11 / / 199 |
| 5 / / 199 | 12 / / 199 |
| 6 / / 199 | 13 / / 199 |
| 7 / / 199 | 14 / / 199 |

Item 13

The number of installments of principal is

ATTACHMENT 1

REQUEST FOR DRAWDOWN

To: Export Finance and Insurance Corporation
 Export House
 22 Pitt Street
 SYDNEY NSW 2000

Credit Agreement **Date:** __/__/199__

Dear Sirs

1. We ask you to:

* pay the exporter US\$_____ Go to 2

* reimburse us US\$_____ Go to 3

2. The Exporter is entitled under the export contract to be paid that amount on __/__/199__ for goods or services which qualify for financing under the Credit Agreement.

3. We paid this amount to the exporter on __/__/199__ for goods or services which qualify for financing under the Credit Agreement.

4. Under the export contract, the exporter has so far received US\$_____

5. * As evidence of the exporter's entitlement to claim this amount, we have signed below.

We also enclose the following additional evidence:

As evidence of our entitlement to claim reimbursement we enclose:

('Strike out whenever inapplicable)

Request for Drawdown dated _____

6. We repeat the warranties contained in the Credit Agreement.

In particular we confirm that.

- We have no knowledge of any dispute in connection with the export contract which you have not already been told about in writing.

- There has been no variation or any performance of the contract which is inconsistent with its terms (excluding an unimportant variation which does not affect the contract price or the date by which the contract performance is to be completed).

7. After deducting anything that is payable by the exporter to you (whether under the, exporter's agreement or in accordance with any other authority given by the exporter), please pay the amount claimed to:

Account name: _____

Account number: _____

Bank: _____

Address: _____

Name of person signing for the
exporter

Position: _____

Date: _____

Name of person signing for the
borrower

Position: _____

Date: _____

ATTACHMENT 2

**FOR EFIC'S CREDIT AGREEMENT
FORM OF LEGAL OPINION**

To: Export Finance and Insurance Corporation
Export House
22 Pitt Street
SYDNEY NSW 2000

You have asked our opinion in connection with a credit agreement (the "Agreement") between [NAME OF BORROWER] (the "Borrower") and yourselves dated [DATE OF CREDIT AGREEMENT].

This opinion is given on the basis that it relates only to the laws of [BORROWER'S COUNTRY].

In connection with this opinion we have examined the Agreement and such have deemed necessary other documents and matters in law and fact as we for the purposes of this opinion.

This opinion assumes:

- (a) the authenticity and completeness of all documents submitted to us as originals; and
- (b) the conformity to originals of all documents supplied to us as certified or photostat copies and the authenticity and completeness of the originals of such later documents.

We have relied upon a certificate of incumbency to ascertain the genuineness of all signatures on documents supplied to us.

On the foregoing basis and subject to the qualifications set out below, we are of the opinion that:

1. The Borrower is duly incorporated and validly existing under the laws of [BORROWER'S COUNTRY] and has all requisite power to own its property and assets and is duly qualified to carry on business under the laws of [BORROWER'S COUNTRY].
2. The Borrower has power to enter into the Agreement and has authorised its officers to do so.
3. The Agreement is a legal, valid and binding agreement enforceable against the Borrower in accordance with its terms.
4. The Agreement is in a proper form to be enforced in the courts of [BORROWER'S COUNTRY].
5. All stamp duty required under the laws of [BORROWER'S COUNTRY] to be paid on or in respect of the Agreement has been paid.
6. The Agreement has been registered and filed correctly and in accordance with the laws of [BORROWER'S COUNTRY] in every place that it needs to be registered or filed.
7. No consents, approvals, permissions, authorisations, orders, licences, filings or registrations are required to be obtained from or made with any governmental authority or agency or with any other person or entity to ensure the validity of the Agreement or to ensure its enforceability or enforcement against the Borrower.
8. The execution, delivery and performance by the Borrower of the Agreement does not and will not violate:
 - (a) any law or regulation of [BORROWER'S COUNTRY],

- (b) any authorisation, consent, order or decree of any government, governmental authority or agency or court in [BORROWER'S COUNTRY], or
 - (c) any Memorandum or Articles of Association or other charter document of the Borrower.
9. The obligations of the Borrower under the Agreement rank at least pari passu with all other indebtedness of the Borrower, except for indebtedness mandatorily referred by law. Indebtedness mandatorily preferred by law means [LIST ALL SUCH INDEBTEDNESS].
 10. Subject only to changes in the laws of [BORROWER'S COUNTRY] there will be no withholding or deduction for any taxes in connection with any payment to be made to you under the Agreement.
 11. I have no reason to believe that any litigations proceeding or dispute is pending or threatened against the Borrower before any court or arbitrator, or any governmental or body or agency.
 12. The choice of the law of New South Wales, Australia, under the Agreement is a valid choice of law.
 13. The Borrower's unconditional submission to the jurisdiction of the courts of New South Wales and any other courts in Australia or elsewhere which you, in your discretion, choose is valid and enforceable.
 14. The Borrower's undertaking not to object to the jurisdiction of any of those courts or argue that it is not a convenient forum is valid and enforceable.

15. The Borrower's waiver of any right it has or may have to rely on sovereign immunity from the jurisdiction of a court, or from legal process of any kind affecting the Borrower or its assets, is valid and enforceable.
16. Under the laws of [BORROWER'S COUNTRY] you will not be treated as resident, domiciled in or carrying on any commercial activity in [BORROWER'S COUNTRY] or subject to any tax in that country as a result only of the execution, delivery, or enforcement of the Agreement.
17. The security constitutes a first priority security interest in the assets intended to be covered by the security and is not subject to any prior interest. The security has priority over a liquidator of the borrower and over any creditors or third parties.

This opinion is given subject to the qualification that we have made no investigation of laws of any jurisdiction other than [BORROWER'S COUNTRY].

Very truly yours

Name: -----

Position: -----

Specimen Signature: -----

Name: -----

Position: -----

Specimen Signature: -----

SIGNED SEALED and] _____
DELIVERED for and on behalf]
of the [] by] Name: _____
its attorney/Authorised Officer]
in the presence of:] Title: _____

Name: _____

Witness

CHAPTER III

PROGRAMS OF THE U.S.A. EX-IM BANK DIRECT LOANS AND GUARANTEES

DIRECT LOANS

- Loan made by Ex-Im Bank
- 85% of- US contract price
- Fixed interest rate
- Exporter paid with disbursement LIC or directly by buyer
- Shipping rules always apply*

CIRR

| Repayment Term | Formula |
|----------------|-------------------------|
| Up to 5 years | 3-yr. Treasury + 100 bp |
| 5 to 8.5 years | 5-yr. Treasury + 100 bp |
| Over 8.5 years | 7-yr. Treasury + 100 bp |

BEST USED WHEN:

- Buyer insists on fixed rate
- Tied aid competition is present

DISADVANTAGES

- Negotiated Credit Agreement
- Disbursement Process
- No Cash Payment Support
- Shipping Requirements

TYPES OF GUARANTEES

* Under Public Resolution 15, shipment on U.S. vessels is required for:

- All Direct Loans
- Guarantees of over \$10 Million

- Comprehensive
- Political Risk Only

GUARANTEE FEATURES

- 100% principal and interest cover for 85% of US Contract Price
- Negotiated interest rate-usually floating
- Fully transferable; can be securitized
- Available in major foreign currencies
- Can switch from floating to fixed rate
- US vessel shipping rules apply for long terms

ADVANTAGES OVER DIRECT LOANS

- Faster documentation process
- Banks assist in the transaction
- Promotes cash payment financing
- Floating interest rate usually lower
- No shipping regulations under \$10 million

MASTER GUARANTEE AGREEMENT (MGA)

- Provides terms applicable to guarantees issued
- Details documentation and procedures
- MGA must be operative
- Any lending institution can apply

GUARANTEE DOCUMENTATION

- Guarantee Agreement - Ex-Im and Lender
- Credit Agreement (LIT only) - Ex-Im, Lender, Borrower
- Disbursement documentation:
 - Invoice
 - Bill of Lading
 - Supplier's Certificate

With provision for both general and statutory waivers.

MEDIUM-TERM PRIORITY LENDER PROGRAM

- Complete Application with Credit Memorandum
- 20 Business Day Turnaround

CREDIT GUARANTEE FACILITY

- Line of credit -- 85% financing
- US lender and foreign bank
- Foreign bank on-lends on same repayment term
- Covers multiple sales to different buyers
- Minimum \$10 million line
- One year availability
- Reserved for high volume, repeat users

MEDIUM-TERM INSURANCE vs. GUARANTEES

- Conditionality
- Flexibility
- Exporter Liability

FEE STRUCTURE

- Application Fee
- Commitment Fee
- Exposure Fee

APPLICATION FEE

| | |
|------------------------|---|
| Letter of Interest | \$100 |
| New Final Commitment | \$100 |
| Preliminary Commitment | 1/10 of 1% of financed portion; \$25,000 cap |

COMMITMENT FEE

| Program | Rate Per Annum |
|---------------------------|---------------------|
| Direct Loan | 1/2% on undisbursed |
| Guarantee | 1/9% |
| Credit Guarantee Facility | 1/16% Flat |

EXPOSURE FEE

Exposure fee determined by:

- Country Risk
- Risk with borrower
- Repayment term

REPAYMENT TERM

Varies by:

- Market category
- Dollar size
- Product convention & sector agreements (O.E.C .D. arrangement and Berne Union understandings)

MAXIMUM REPAYMENT TERM MARKET CATEGORY

Category 1 - Rich

- 8.5 years with prior notification
- Maximum 5 years

Category 2 -- All others

- Maximum 10 years

MAXIMUM REPAYMENT TERM CONTRACT SIZE

| Contract Price | Cat I | Cat II |
|---------------------|---------|---------|
| Up to \$300,000 | Up to 4 | Up to 4 |
| \$300m to \$7mm | 5 | 5 |
| \$7mm to \$11.7mm | 5 | 7 |
| \$11.7mm to \$25mrn | 5 | 8 |

> than \$25mm

5

10

STARTING POINT FOR DETERMINATION OF CREDIT PERIOD AND PROGRESS PAYMENTS

Starting Point:

- Shipment for single shipment
- Mid-point of multiple shipments
- Commissioning of project

Progress Payments - Allowable

STANDARD FINANCE MODEL

| | |
|-------------------|-------------|
| Contract price | \$1,000,000 |
| Cash payment | \$150,000 |
| Financed portion | \$850,000 |
| Exposure fee @ 3% | \$25,500 |
| Total financed | \$875,500 |

FOREIGN CONTENT - 25%

| | Eligible | Ineligible |
|-----------------|-------------|-------------|
| Contract price | \$1,000,000 | \$1,000,000 |
| Less ineligible | -0- | \$250,000 |
| Eligible | \$1,000,000 | \$750,000 |
| Cash payment | \$250,000 | \$112,500 |
| Total financed | \$750,000 | \$637,500 |

(plus exposure fee)

LOCAL COST FINANCING - 15 %

| | |
|------------------|-------------|
| US Export Value | \$1,000,000 |
| Cash payment | \$150,000 |
| Financed portion | \$850,000 |
| 15% local cost | \$150,000 |

Total financed \$1,000,000

Total Contract Price \$1,150,000

AIRCRAFT FINANCE

Interest Rates

- 10 yrs. or less: 10 yr. Treasury + 120 bp
- Over 10 years: 10 yr. Treasury + 175 bp

Exposure Fees:

- Direct Loans 2%
- Guarantees 3%
- **Maximum Term: 12 years**
- **Sector Agreement**

ROLE OF THE ENGINEERING DIVISION

- **Product Eligibility Authority**
- **Environmental Evaluation**
 - Pollutants
 - Other Impact
- **Other**
 - Technical Project Evaluation
 - Monitor Project Progress

ENVIRONMENTAL EXPORTS ENHANCEMENTS

Regular program features, plus:

- Local cost cover
- Capitalized interest during construction
- Maximum allowable repayment terms

USED AND REFURBISHED EQUIPMENT

- Eligible on standard or shorter repayment terms
- Original U.S. manufacture
 - 1-yr. rule if previously exported

- Original foreign manufacture
 - Treated as eligible foreign content
 - 50% of production cost maximum
- Refurbishment normally - eligible US content

TIED AID

- Policy to counter, not initiate
- Budget cost not more than 50%
- Broader market opportunities at stake
- Favorable factors include
 - Competitor country violating tied-aid rules
 - US suppliers are small
 - Environmental or renewable energy project

PROJECT FINANCE

- New or expansion projects
- Repayment from project cash flow
- Two phases:
 - Pre-completion and post-completion
 - Separate exposure fee schedule

OTHER SPECIAL PROGRAMS

- Engineering Multiplier
- Supplier Credits

INTERNAL PROCESSING OF APPLICATIONS

- Application received
- Business Development review; issues LI
- Loan officer review
- Engineering review
- Approval Loan Committee or Board
- Legal review documentation and closing
- Credit Administration - disbursement

HOW TO APPLY

| Type | Eligible Applicant |
|------------------------|--|
| Letter of Interest | Anyone |
| Preliminary Commitment | Anyone |
| Final Commitment | Borrower or Mandated Guaranteed Lender |

Exposure Fees

Determining the Exposure Fee

- Select appropriate Country Fee Level Chart
- Determine if public or private sector buyer
- Locate buyer category
- Determine fee level
- Determine fee from Fee Level Chart

FEE LEVEL CHART
MEXICO
PRIVATE SECTOR CREDITS

| | | |
|---|-------------------|---------------------------------|
| A. SOVEREIGN (e.g.. Finance Ministry Guarantee) | FEE LEVEL | See Public Sector Credits Sheet |
| B. POLITICAL-ONLY COVER | FEE LEVEL | 5 |
| C. TRANSACTIONS OF \$1 MILLION OR LESS | MAXIMUM FEE LEVEL | 7 |

D1. BORROWERS / GUARANTORS with RATED/TRADED CROSS BORDER (HARD CURRENCY) DEBTS

| FEE LEVEL | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
|----------------------------|--------------|------------|------------|----------|----------|----------|----------|----------|
| LONG-TERM (S&P, others) | AA+, AA, AA- | A+, AA | BBB+, BBB | BBB- | BB+, BB | BB | B+, B | B |
| LONG TERM (Moody's) | Aa1, Aa2 | A1, A2, A3 | Baa1, Baa2 | Baa3 | Ba1, Ba2 | Ba3 | B1, B2 | B3 |
| SHORT-TERM (S&P, others) | A-1+ | A-1 | A-2 | A-3 | B | | C | |
| SHORT-TERM (TBW) | TBW-1 | TBW-2 | TBW-3 | TBW-4 | | | | |
| SHORT TERM (Moody's) | | P-1 | P-2 | P-3 | | | | |
| SPREAD (bp) over T-YIELD < | 40 | 70 | 140 | 250 | 400 | 600 | 900 | 1500 |
| SPREAD (bp) over LIBOR < | 10 | 40 | 90 | 220 | 370 | 570 | 870 | 1470 |

D2. BORROWERS/GUARANTORS with INTRACOUNTRY (LOCAL CURRENCY) RATINGS

| FEE LEVEL | 6 | 6 | 6 | 6 | 6 | 6 | 7 | 8 |
|-----------------------------------|--------------|------------|------------|----------|----------|----------|----------|----------|
| LONG-TERM (S&P, TBW) | AA+, AA, AA- | A+, A.A- | BBB+, BBB | BBB- | BB+, BB | BB- | B+, B | B- |
| LONG-TERM (Moody's) | Aa1, Aa2 | A1, A2, A3 | Baa1, Baa2 | Baa3 | Ba1, Ba2 | Ba3 | B1, B2 | B3 |
| SHORT-TERM (S&P, others) | A-1+ | A-1 | A-2 | A-3 | B | | C | |
| SHORT-TERM (Moody's) | | P-1 | P-2 | P-3 | | | | |
| FINANCIAL STRENGTH (Moody's) | A/B | B | B/C | C | C/D | D | D/E | E |
| INTRA-COUNTRY ISSUER (TBW) | IC, A/B | IC, B | IC, B/C | IC, C | IC, C/D | IC, D | IC, D/E | IC, E |
| INDIVIDUAL (ISCA) | A/B | B | B/C | C | C/D | D | D/E | E |
| INDIVIDUAL (Capital Intelligence) | AA+, AA, AA- | A+, A.A- | BBB+, BBB | BBB- | BB+, BB | BB- | B+, B | B- |

E. UNRATED LARGEST (PROFITABLE) FINANCIAL INSTITUTIONS MAXIMUM FEE LEVEL 6

FI. UNRATED BORROWERS / GUARANTORS other than Financial Institutions

DEBT TO TANGIBLE NET WORTH <1X <2X <3X <4X <6X >6X

FEE LEVEL

| | | | | | | | |
|--------------|------|---|---|---|---|---|---|
| | >25% | 6 | 6 | 6 | 6 | 7 | 8 |
| OPERATING | >20% | 6 | 6 | 6 | 6 | 7 | 8 |
| CASH FLOW | >15% | 6 | 6 | 6 | 7 | 8 | 8 |
| (2-YEAR AVG) | >10% | 6 | 6 | 7 | 8 | 8 | 8 |
| TO | >5% | 6 | 7 | 8 | 8 | 8 | 8 |
| DEBT | <5% | 7 | 8 | 8 | 8 | 8 | 8 |

F2. UNRATED FINANCIAL INSTITUTION BORROWERS / GUARANTORS

| | | | | | | |
|-----------------------------------|-------|-------|-------|-------|-------|-------|
| FEE LEVEL | 6 | 6 | 6 | 6 | 7 | 8 |
| SHAREHOLDERS' EQUITY TO ASSETS | >9% | >7% | >6% | >5% | >4% | <4% |
| NET INCOME TO ASSETS (2-YR AVG) | >2.5% | >2.0% | >1.5% | >1.0% | >0.5% | <0.5% |
| BORROWED FUNDS TO NET LOANS | <40% | <60% | <80% | <100% | <120% | >120% |
| LIQUID ASSETS TO ASSETS | >25% | >20% | >15% | >10% | >5% | <5% |
| RESERVES TO NON-PERFORMING ASSETS | >200% | >175% | >150% | >125% | >100% | <100% |

FEE LEVEL CHART
MEXICO
PUBLIC SECTOR CREDITS

| | | |
|---|-------------------|----------------------------------|
| A. SOVEREIGN (e.g.. Finance Ministry Guarantee) | FEE LEVEL | 5 |
| B. POLITICAL-ONLY COVER | FEE LEVEL | See Private Sector Credits Sheet |
| C. TRANSACTIONS OF \$1 MILLION OR LESS | MAXIMUM FEE LEVEL | 7 |

D1. BORROWERS / GUARANTORS with RATED/TRADED CROSS BORDER (HARD CURRENCY) DEBTS

| FEE LEVEL | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
|----------------------------|--------------|------------|------------|----------|----------|----------|----------|----------|
| LONG-TERM (S&P, others) | AA+, AA, AA- | A+, AA | BBB+, BBB | BBB- | BB+, BB | BB | B+, B | B |
| LONG TERM (Moody's) | Aa1, Aa2 | A1, A2, A3 | Baa1, Baa2 | Baa3 | Ba1, Ba2 | Ba3 | B1, B2 | B3 |
| SHORT-TERM (S&P, others) | A-1+ | A-1 | A-2 | A-3 | B | | C | |
| SHORT-TERM (TBW) | TBW-1 | TBW-2 | TBW-3 | TBW-4 | | | | |
| SHORT TERM (Moody's) | | P-1 | P-2 | P-3 | | | | |
| SPREAD (bp) over T-YIELD < | 40 | 70 | 140 | 250 | 400 | 600 | 900 | 1500 |
| SPREAD (bp) over LIBOR < | 10 | 40 | 90 | 220 | 370 | 570 | 870 | 1470 |

D2. BORROWERS/GUARANTORS with INTRACOUNTRY (LOCAL CURRENCY) RATINGS

| FEE LEVEL | 5 | 5 | 5 | 5 | 5 | 6 | 7 | 8 |
|-----------------------------------|--------------|------------|------------|----------|----------|----------|----------|----------|
| LONG-TERM (S&P, TBW) | AA+, AA, AA- | A+, A.A- | BBB+, BBB | BBB- | BB+, BB | BB- | B+, B | B- |
| LONG-TERM (Moody's) | Aa1, Aa2 | A1, A2, A3 | Baa1, Baa2 | Baa3 | Ba1, Ba2 | Ba3 | B1, B2 | B3 |
| SHORT-TERM (S&P, others) | A-1+ | A-1 | A-2 | A-3 | B | | C | |
| SHORT-TERM (Moody's) | | P-1 | P-2 | P-3 | | | | |
| FINANCIAL STRENGTH (Moody's) | A/B | B | B/C | C | C/D | D | D/E | E |
| INTRA-COUNTRY ISSUER (TBW) | IC, A/B | IC, B | IC, B/C | IC, C | IC, C/D | IC, D | IC, D/E | IC, E |
| INDIVIDUAL (ISCA) | A/B | B | B/C | C | C/D | D | D/E | E |
| INDIVIDUAL (Capital Intelligence) | AA+, AA, AA- | A+, A.A- | BBB+, BBB | BBB- | BB+, BB | BB- | B+, B | B- |

| | | |
|--|-------------------|---|
| E. UNRATED LARGEST (PROFITABLE) FINANCIAL INSTITUTIONS | MAXIMUM FEE LEVEL | 6 |
|--|-------------------|---|

FI. UNRATED BORROWERS / GUARANTORS other than Financial Institutions

| | | | | | | |
|----------------------------|-----|-----|-----|-----|-----|-----|
| DEBT TO TANGIBLE NET WORTH | <1X | <2X | <3X | <4X | <6X | >6X |
|----------------------------|-----|-----|-----|-----|-----|-----|

FEE LEVEL

| | | | | | | | |
|--------------|------|---|---|---|---|---|---|
| | >25% | 5 | 5 | 5 | 5 | 6 | 7 |
| OPERATING | >20% | 5 | 5 | 5 | 6 | 7 | 8 |
| CASH FLOW | >15% | 5 | 5 | 6 | 7 | 8 | 8 |
| (2-YEAR AVG) | >10% | 5 | 6 | 7 | 8 | 8 | 8 |
| TO | >5% | 6 | 7 | 8 | 8 | 8 | 8 |
| DEBT | <5% | 7 | 8 | 8 | 8 | 8 | 8 |

F2. UNRATED FINANCIAL INSTITUTION BORROWERS / GUARANTORS

| | | | | | | |
|-----------------------------------|-------|-------|-------|-------|-------|-------|
| FEE LEVEL | 5 | 5 | 5 | 6 | 7 | 8 |
| SHAREHOLDERS' EQUITY TO ASSETS | >9% | >7% | >6% | >5% | >4% | <4% |
| NET INCOME TO ASSETS (2-YR AVG) | >2.5% | >2.0% | >1.5% | >1.0% | >0.5% | <0.5% |
| BORROWED FUNDS TO NET LOANS | <40% | <60% | <80% | <100% | <120% | >120% |
| LIQUID ASSETS TO ASSETS | >25% | >20% | >15% | >10% | >5% | <5% |
| RESERVES TO NON-PERFORMING ASSETS | >200% | >175% | >150% | >125% | >100% | <100% |

FEE LEVEL CHART
CHINA, P.R.
PUBLIC SECTOR CREDITS

| | | |
|---|-----------|----------------------------------|
| A. SOVEREIGN (e.g.. Finance Ministry Guarantee) | FEE LEVEL | 2 |
| B. POLITICAL-ONLY COVER | FEE LEVEL | See Private Sector Credits Sheet |

C1. BORROWERS / GUARANTORS with RATED/TRADED CROSS BORDER (HARD CURRENCY) DEBTS

| FEE LEVEL | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
|----------------------------|--------------|------------|------------|-------|----------|-----|--------|------|
| LONG-TERM (S&P, others) | AA+, AA, AA- | A+, AA | BBB+, BBB | BBB- | BB+, BB | BB | B+, B | B |
| LONG TERM (Moody's) | Aa1, Aa2 | A1, A2, A3 | Baa1, Baa2 | Baa3 | Ba1, Ba2 | Ba3 | B1, B2 | B3 |
| SHORT-TERM (S&P, others) | A-1+ | A-1 | A-2 | A-3 | B | | C | |
| SHORT-TERM (TBW) | TBW-1 | TBW-2 | TBW-3 | TBW-4 | | | | |
| SHORT TERM (Moody's) | | P-1 | P-2 | P-3 | | | | |
| SPREAD (bp) over T-YIELD < | 40 | 70 | 140 | 250 | 400 | 600 | 900 | 1500 |
| SPREAD (bp) over LIBOR < | 10 | 40 | 90 | 220 | 370 | 570 | 870 | 1470 |

C2. BORROWERS/GUARANTORS with INTRACOUNTRY (LOCAL CURRENCY) RATINGS

| FEE LEVEL | 2 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
|-----------------------------------|--------------|------------|------------|-------|----------|-------|---------|-------|
| LONG-TERM (S&P, TBW) | AA+, AA, AA- | A+, A.A- | BBB+, BBB | BBB- | BB+, BB | BB- | B+, B | B- |
| LONG-TERM (Moody's) | Aa1, Aa2 | A1, A2, A3 | Baa1, Baa2 | Baa3 | Ba1, Ba2 | Ba3 | B1, B2 | B3 |
| SHORT-TERM (S&P, others) | A-1+ | A-1 | A-2 | A-3 | B | | C | |
| SHORT-TERM (Moody's) | | P-1 | P-2 | P-3 | | | | |
| FINANCIAL STRENGTH (Moody's) | A/B | B | B/C | C | C/D | D | D/E | E |
| INTRA-COUNTRY ISSUER (TBW) | IC, A/B | IC, B | IC, B/C | IC, C | IC, C/D | IC, D | IC, D/E | IC, E |
| INDIVIDUAL (ISCA) | A/B | B | B/C | C | C/D | D | D/E | E |
| INDIVIDUAL (Capital Intelligence) | AA+, AA, AA- | A+, A.A- | BBB+, BBB | BBB- | BB+, BB | BB- | B+, B | B- |

D1. TRANSACTIONS OF \$10 MILLION OR LESS - FINANCIAL INSTITUTIONS FEE LEVEL 2*

D2. TRANSACTIONS OF \$10 MILLION OR LESS - OTHER THAN FINANCIAL INSTITUTIONS FEE LEVEL 3*

E. UNRATED LARGEST (PROFITABLE) FINANCIAL INSTITUTIONS MAXIMUM FEE LEVEL 3

FI. UNRATED BORROWERS / GUARANTORS OTHER THAN FINANCIAL INSTITUTIONS

DEBT TO TANGIBLE NET WORTH <1X <2X <3X <4X <6X >6X

| | | FEE LEVEL | | | | | |
|--------------|------|-----------|---|---|---|---|---|
| | >25% | 3 | 3 | 4 | 5 | 6 | 7 |
| OPERATING | >20% | 3 | 4 | 5 | 6 | 7 | 8 |
| CASH FLOW | >15% | 34 | 5 | 6 | 7 | 8 | 8 |
| (2-YEAR AVG) | >10% | 5 | 6 | 7 | 8 | 8 | 8 |
| TO | >5% | 6 | 7 | 8 | 8 | 8 | 8 |
| DEBT | <5% | 7 | 8 | 8 | 8 | 8 | 8 |

F2. UNRATED FINANCIAL INSTITUTION BORROWERS / GUARANTORS

| FEE LEVEL | 3 | 3 | 5 | 6 | 7 | 8 |
|-----------------------------------|-------|-------|-------|-------|-------|-------|
| SHAREHOLDERS' EQUITY TO ASSETS | >9% | >7% | >6% | >5% | >4% | <4% |
| NET INCOME TO ASSETS (2-YR AVG) | >2.5% | >2.0% | >1.5% | >1.0% | >0.5% | <0.5% |
| BORROWED FUNDS TO NET LOANS | <40% | <60% | <80% | <100% | <120% | >120% |
| LIQUID ASSETS TO ASSETS | >25% | >20% | >15% | >10% | >5% | <5% |
| RESERVES TO NON-PERFORMING ASSETS | >200% | >175% | >150% | >125% | >100% | <100% |

*MAY NOT APPLY IF A FEE LEVEL HAS BEEN PRE-APPROVED. REFER TO EXPOSURE FEE ADVICE.

EXPOSURE FEES TABLE

\$Per \$100 of Each Disbursement

| Fee Level | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
|-----------|------|------|------|------|------|-------|-------|------|
| Repayment | | | | | | | | |
| Term | | | | | | | | |
| 1 Year | 0.50 | 0.75 | 1.13 | 1.38 | 1.69 | 2.07 | 2.53 | 3.90 |
| 2 Years | 0.63 | 0.94 | 1.41 | 1.73 | 2.11 | 2.58 | 3.16 | 4.75 |
| 3 Years | 0.75 | 1.13 | 1.69 | 2.07 | 2.53 | 3.10 | 3.80 | 5.70 |
| 4 Years | 0.88 | 1.31 | 1.97 | 2.41 | 2.95 | 3.81 | 4.43 | 5.64 |
| 5 Years | 1.00 | 1.50 | 2.25 | 2.75 | 3.33 | 4.14 | 5.06 | 7.59 |
| 6 Years | 1.13 | 1.89 | 2.90 | 3.80 | 4.98 | 6.85 | 10.27 | N/A |
| 7 Years | 1.25 | 1.88 | 3.22 | 4.22 | 5.53 | 7.61 | 11.41 | N/A |
| 8 Years | 1.38 | 2.06 | 3.54 | 4.64 | 6.08 | 8.37 | 12.55 | N/A |
| 8.5 Years | 1.44 | 2.16 | 3.70 | 4.85 | 6.36 | 8.75 | 13.12 | N/A |
| 9 Years | 1.50 | 2.25 | 3.56 | 5.06 | 6.63 | 9.13 | 13.69 | N/A |
| 10 Years | 1.63 | 2.44 | 4.19 | 5.48 | 7.19 | 9.89 | 14.83 | N/A |
| 12 Years | 1.88 | 2.81 | 4.83 | 6.33 | 8.29 | 11.41 | 17.11 | N/A |

MEDIUM / LONG TERM PROGRAMS

CASE STUDIES/ CLASS DISCUSSION

Please answer the following questions for the case assigned to your group:

1. Application process

- A. Of the three types of Ex-Im application, Letter of Interest, Preliminary Commitment, or Final Commitment, which is most appropriate for your case?
- B. Who can submit the application?

2. Policy considerations

Are there military, foreign content, additionality, shipping issues or other policy concerns?

3. Repayment terms

- A. What is the appropriate repayment term?
- B. When would repayment begin?

4. Fees

- A. How much is the application fee?
- B. How much is the commitment fee?
 - i. When does it begin to accrue?
 - ii. Who pays it?
 - iii. Can it be financed?
- C. Determine or approximate the exposure fee.
 - i. When is it paid?
 - ii. Who will pay it?
 - iii. Can it be financed?

5. Financing package

- A. Would you recommend a loan or a guarantee?
- B. How would the interest rate be determined (for loan or guarantee)?
- C. How much can be financed, including the exposure fee if applicable?
- D. Would there be local cost support?

Information.

A. Interest Rates for Direct Loans

Assume the Ex-Im Direct Loan Interest Rates are as follows:

| | Up to 5 Years | From 5 to 8 1/2 Yrs | Over 8 1/2 Yrs. |
|-------------|---------------|---------------------|-----------------|
| Category I | 6.9% | 7.1% | 7.2% |
| Category II | 6.9% | 7.1% | 7.2% |

Note: To determine the four-month hold rate, add 20 basis points (PC's only)

B. Use the Mexico Exposure Fee Table for all cases.

CASE No. 1 BIG TIME EXPORTER

Big Time Co. is bidding on a \$20,000,000 sale of computing equipment that will time the departure and arrival of each train that uses the Central Railway Station in Jakarta, Indonesia, a Category 11 country. Competition has been intense with exporters from Japan, Canada and Germany, as well as your firm from the US, all placing bids. Through negotiation, the governments of those countries have agreed to a common line calling for non-concessional OECD financing terms.

The computer will have some foreign content, which will be imported from abroad and assembled into the computer equipment in the US amounting to 13% of the total cost. There is no local cost support requested. The Central Railway Station serves primarily passenger trains but it is also the point of embarkation for some military transports. The Government of Indonesia will be the buyer. Although the computer equipment will be installed in 6 months, the remainder of the system will take one year in total to complete.

You are the financial vice president of Big Time and need to explore financing alternatives for the potential sale. The Indonesians are requiring that financing be part of the bid submission, and you want to bring them some indication of financing on your upcoming trip.

CASE No. 2 CLEAN ENVIRONMENT INC.

Clean Environment Inc. has won a \$10,000,000 contract to supply capital equipment to a waste water facility 30 miles south of Mexico City. The signed contract is contingent on Clean Environment providing financing for their scope of supply. The financing offer should include comment on local cost financing. Mexico is a Category 11 country.

The company had obtained a Letter of Interest from Ex-Im Bank which proved to be very helpful in their marketing efforts. The Mexican company, Cia. de Agua S.A., is owned by the Mexican Government and is asking you, the Treasurer of Clean Environment, to secure financing. The facility will be built in one year. They are especially interested in the Environmental Exports Program that was mentioned in Ex-Im Bank's Letter of Interest.

They would like to ship the product via rail to Laredo Texas, followed by pickup by a Mexican carder at that point. Some of the software to operate the plant will be shipped by air.

Your next step is to meet with your friendly banker at the Can Do Bank in your city. They are unwilling to take unsecured risk in Mexico but are very comfortable using the Ex-Im Bank programs.

Although the Mexican company is owned by the government, it is not a full-faith-and-credit entity and relies on its own financial merits when obtaining credit. The firm carries a Baal intracountry, local currency, Moody's long-term debt rating.

CASE No. 3 CHEMBRAZIL

A large Brazilian company- ChemBrazil is expanding and is seeking suppliers of capital goods and services valued at about \$550 million.

Because there has been a world-wide slow down in such projects over the past few years, many companies from several countries are fighting hard for the business. Knowing this, ChemBrazil is driving a hard bargain. In addition to the typical financing available under the OECD arrangement, they want support for an additional \$7 million of local costs for the site development and the building to house the expansion, which is in a very nice location on the edge of a national wetlands park. Support for the cash payment is also being requested. The total construction time is estimated at 2 years.

You are a senior vice president at Pay Us Back Bank. Your highly valued customer from Chemsupply, U.S. has talked to you about this transaction and is coming in shortly. You want to be supportive but you are not willing to take the Brazilian risk, although you will do some cash payment financing on a one-year basis.

You have made a preliminary review of ChemBrazil's financial statements and noted that, among other financial characteristics, the firm's operating-cash-flow to total-debt ratio average for the past two years was 11.4% and the firm has a total-debt to tangible-net-worth ratio of 2.4: 1.

Brazil is a Category II country.

CASE No. 4 EARTH PUSHER INC.

Earth Pusher Inc. has signed a sales contract for the sale of ten of its biggest bulldozers, the Super EP2000 to Alpha Goldmines Ltd., a privately-held company in South Africa for a total of \$10 million, subject to Earth Pusher obtaining satisfactory financing for the sale.

The bulldozer is made in the U.S. but Earth Pusher has three options to purchase the motor, transmission and gear assembly: 1) purchase from a U.S. manufacturer and assemble in the US; 2) purchase from a Mexican manufacturer, bring it into the U.S. and assemble it into the bulldozer, or 3) purchase it from the Mexican manufacturer and have it shipped to South Africa where it will be then incorporated into the bulldozer shipped from the U.S. Assume that the total cost of the motor, transmission and gear assembly to Earth Pusher is \$3.0 million for all ten tractors to be exported in each of the three options.

Alpha Goldmines is a growing South African firm, which is starting to obtain credit on an international basis. Last year the firm issued its first international debt placement of \$30 million, a dollar-denominated issue handled by Warsaw and Duff in London. The unsecured debt carries a Baa2 Moody's rating.

South Africa is a Category II country.

You are the banker / advisor to Earth Pusher. You would have no problem making an Ex-Im Bank supported loan to South Africa. You are concerned, however, that the amount of local content will minimize Ex-Im Bank's support and put a higher finance burden on you or the South African buyer. You need to outline to Earth Pusher Ex-Im Bank's programs and make a recommendation as to the sourcing of the motor, transmission and gear assembly.

CASE No. 5 SECOND HAND MINING TOOLS

You are the owner of a small business that buys used mining equipment, refurbishes it and sells it. During a vacation to Argentina, you visited a mine and noticed that their equipment was both obsolete and worn out. You made a proposal to the mine owner that covered the sale of two mining tools with a value of approximately \$ 3 million.

Upon returning home, you find the order waiting in the mail. It is, however, contingent on financing of at least five years. One of the machines was made in the U.S. and will sell for \$1,200,000. The second was made in the United Kingdom. Its cost to you is \$450,000 and will require refurbishment work of \$600,000 to yield a \$1.8 million sales price. It will take about 3 months for the equipment to be reconditioned. Once in Argentina, the equipment will be put into use immediately.

You approach your bank for assistance. The bank is willing to look at the transaction with Ex-Im support. You have obtained financial statements for the past three years and supporting credit information from the buyer, which you have given to the bank. After reviewing the information the bank believes Ex-Im is unlikely to support the transaction without additional financial support for the buyer. You contact the buyer who states that he can obtain the guarantee of a local bank for his company. He submits to you financial statements on the proposed guarantor bank for the past three years. The most current year's financial statements show the following financial characteristics for the guaranteeing bank:

| | |
|-----------------------------------|-------|
| Shareholders Equity to Assets: | 5.5% |
| Net Income to Assets (2-yr avg.) | 0.72% |
| Borrowed Funds to Net Loans | 72% |
| Liquid Assets to Assets | 14% |
| Reserves to Non-Performing Assets | 133% |

Argentina is a Category I country.

CHAPTER IV

PROJECT FINANCING - JAPANESE INVOLVEMENT

1. POLICIES

- Huge investment demands for infrastructure in Asian countries are projected by the World Bank and other institutions.
- Infrastructure investment requirements in developing EAST Asian economies are projected at between \$1.3 - 1.5 trillion for 1995-2004.
- A Certain amount of commercial funds will be expected to fulfil the lack of official funds to meet the demand.
- A Japanese private institution projected a gap of \$ 630 billion for the investment requirements for 1995 - 2010 in Asian region.
- Privatisation or BOT¹ style project in such infrastructure areas as telecommunications, power generation, water supply and highways contributes to development of emerging countries.
- We positively support those transactions through M.I.T.I.'s insurance for commercial lenders, exporters and investors because development of those countries revitalises not only their economy, but also the world economy.

2. PROJECT FINANCE BUSINESS TERMS

COUNTRIES COVERED

- In principle, EID/MITI covers project finance transactions on a case by case basis to Non- L/G countries of our country classification.

RISKS COVERED

- EID/MITI provides a maximum percentage of 97.5% cover for political risk.
- We determine commercial risk percentage of cover on a case by case basis, with usual percentage of cover of 50%, in principle.

RATING OF EXPORT CREDIT PREMIA

- We do not differentiate in our premium system specifically for project finance.

INTERNATIONAL RULES

- All transactions should be structured to comply with OECD Arrangement and / or Berne Union Rules.

3. BUSINESS DIVERSITY

We committed 27 projects² in 11 countries, of which 21 cases have been contracted.

TOTAL INSURED AMOUNT: US \$4 billion

| <u>SECTOR</u> | | <u>AREA</u> | |
|--------------------|-----|---------------|------|
| Power | : 7 | Asia | : 15 |
| Natural Resources | : 6 | South America | : 8 |
| Petrochemical | : 6 | Middle East | : 3 |
| Telecommunications | : 2 | Others | : 1 |

4. CO-FINANCING ASPECTS

- We have co-financed a project with the World Bank on Hub River Power Plant in Pakistan.
- We have two co-financed projects with International Finance Corporation Pagbilao Power Plant in Philippines and Lal Pir Power Plant in Pakistan.

¹ B.O.T. - Build, Operate, Transfer

² Of which two projects were withdrawn and one commitment has expired.

- We basically appraise and support the role, which the World Bank has played as catalyst for infrastructure development in developing countries through its guarantee function.
- Japanese exporters and commercial banks may feel the preferred payment status of the World Bank is somewhat of an obstacle to co-financing with it.
- We believe it useful to exchange information on each project.
- We believe it useful to co-operate in negotiation on security with a host country.

5. RISK SHARING

- We offer partial cover (reduced insured portion) on commercial risk on the whole of the project base.
- Although we do not have legal requirement for a minimum capital contribution, at least 20-30 % capital contribution is preferable as a minimum.
- We basically require a support letter or guarantee from sovereign governments according to the level of their involvement.
- With regard to risk sharing techniques, co-finance with multilateral, regional institutions or other ECA's is preferable.

CHAPTER V

MEDIUM/LONG TERM TRADE AND PROJECT **THE KOREAN APPROACH**

CONTENTS

TOPIC 1: OFFICIALLY SUPPORTED EXPORT CREDIT

1. What is Officially Supported Export Credits

1. Definition
2. Operating Principles of officially supported export credit
3. Types of support
4. Types of ECA support according to the economic development stage

2. Medium & Long Term Export Credit Insurance

1. General Feature
2. Medium & long term export insurance program of KEIC
3. Paris club rescheduling

TOPIC 2: PROJECT RISK ASSESSMENT

1. Risks in Medium & Long Term Export Credit Insurance

2. Risk Phases
3. Types of risk

2. Project Risk Assessment

1. Project risk assessment of ECAs: Past & Present
2. Risk assessment in project finance
 - a. What is project finance

- b. Background
- c. Participants of project finance
- d. Principles of project finance
- e. Project phases & risk takers
- 3. Risks in project finance
- 4. Risks and Mitigants
- 5. KEIC's underwriting points on project finance
- 6. Procedure of risk assessment

TOPIC 3: PREMIUM SYSTEM IN MEDIUM & LONG TERM EXPORT CREDIT INSURANCE

1. Principles of Premium Policy

- 1. Principles of premium
- 2. ECA's principles
- 3. Do ECAs reach the goal of long-term break even
- 4. Trends

2. Determining Premium Level

- 1. Factors in determining premium level
- 2. OECD's efforts to establish harmonized premium level
- 3. OECD's country rating scheme
- 4. Premium factors of individual project

WHAT IS OFFICIALLY SUPPORTED EXPORT CREDITS?

1. Definition

Loans or credits to finance the export of goods and services for which ECA in the creditor country provides guarantees, insurance, or direct financing

2. Operating principles of Officially Supported Export credits

a. Purpose

-facilitate & promote national export

b. Rational of official involvement

- correct the market failure
- defend the national exporter's interest

3. Types of support

(a) Financing support

- Direct financing: ECA provides direct financing to the debtors in importing countries
- Interest subsidy: ECA provides an interest subsidy to the commercial banks which give direct loans to the debtors in importing countries

(b) Insurance & Guarantee

- ECA covers risks - arising in the export or export financing transactions - for the exporters or commercial banks
- Insurance & Guarantees are used interchangeably in the international financing & export credit field
- Insurance & Guarantees are generally divided into short term, medium term, and long term
 - short term: usually under one year
 - medium term: between one and five years
 - long term: over five years

Definition of Insurance & Guarantee by IBRD:

Insurance: offered to exporters to cover the risk of non-payment by the buyer, and often used interchangeably with guarantee

Guarantee: a type of insurance offered to financial institutions to cover the risk of non-payment by the buyer

4. Types of ECA support according to the economic development stage

a. Advanced countries

- Insurance is the main function whereas financing is the subordinate function

b. Developing countries

- Insurance & Financing have the same importance

c. Less developed countries

- Financing is the main function whereas insurance is the subordinate function

Function of ECAs & Financial Market Condition

| | ECAs' Function | Financial Market Condition |
|---------------------------------|-----------------------|-----------------------------------|
| Advanced Countries | Insurance | Well-developed financial market |
| Developing Countries | Insurance & Financing | Immature financial market |
| Less-Developed Countries | Financing | Not developed |

MEDIUM & LONG TERM EXPORT CREDIT INSURANCE

1. General Features

(a) Payment Term

- one to ten years of deferred payment

(b) Transaction Covered

- export transaction of capital goods
- Ships, aircraft, plant, etc

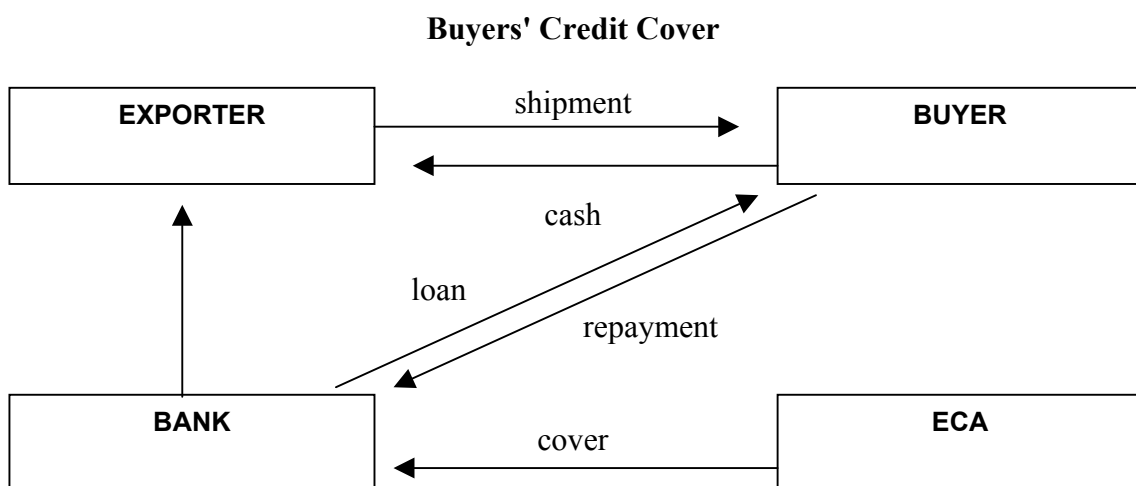
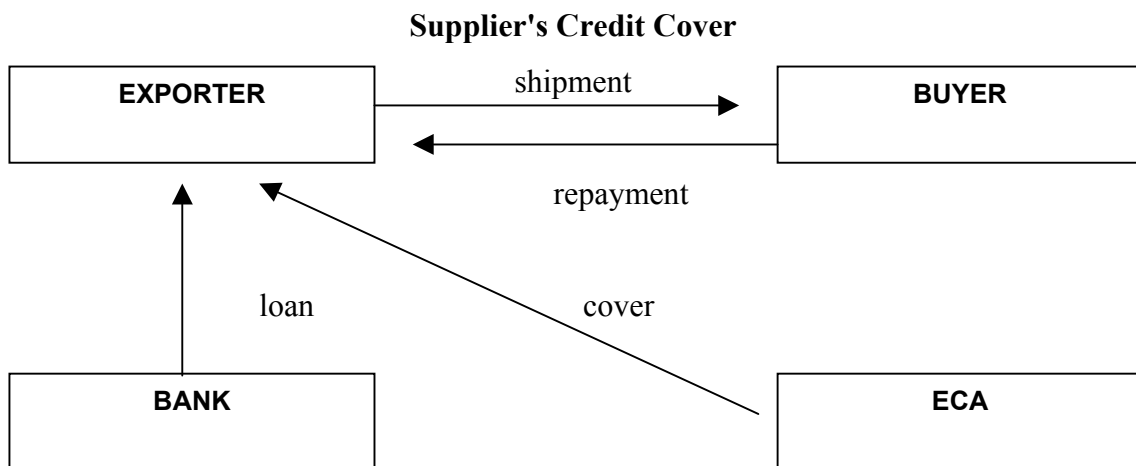
(c) Focus on Political Risk

- demand for ECAs' cover is focused on political risk

Medium & Long Term vs. Short Term Insurance

| Items | M/L Term | S/T Term |
|----------------|----------------|----------------------------|
| Repayment Term | 1 to 10 years | Up to 1 year |
| Goods | Capital Goods | Consumer Goods |
| Who Covers? | ECA | ECA, Private Insurer, etc. |
| Main Risk | Political Risk | Commercial Risk |
| Size | Big | Small |
| Function | Financing | Insurance |

(d) Types of cover



(e) Types of Policy

| Items | Continental Style | American Style |
|--------------------|---|---------------------------|
| Country | European countries such as France, Germany and Japan, Korea | U.S., U.K., etc |
| Type | Insurance | Guarantee |
| Coverage | Partial | Full |
| Documentation Risk | Not covered | Covered |
| Contract Style | Policy basis | Individual Contract basis |

(2) Medium & Long Term Export Credit Insurance Program of KEIC

a. Covered Transaction

-Export transaction of Capital Goods with over two years repayment period

b. Policy types

- Specific policy & Whole policy
- Suppliers' credit policy: Pre-shipment & Post-shipment
- Buyers' credit policy

c. Risks Covered

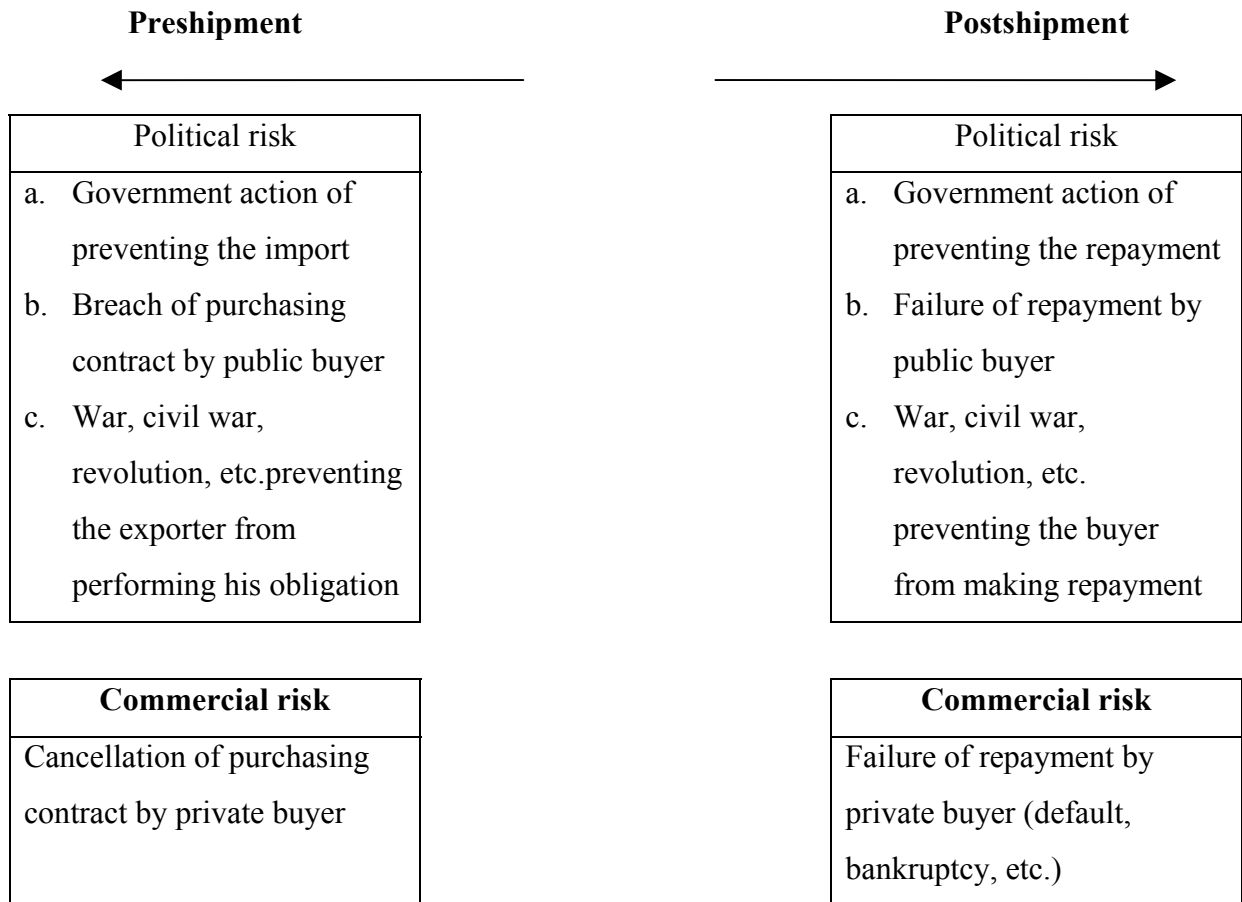
- Preshipment (pre-credit) risk & Postshipment (post-credit) risk
- Political risk & Commercial risk

d. Matrix of risk covered

| Scope | Political risk | Commercial Risk |
|---------------|----------------|-----------------|
| Pre-shipment | Cover | Off cover |
| Post-shipment | Cover | Cover |

Definition of the risks

Shipment

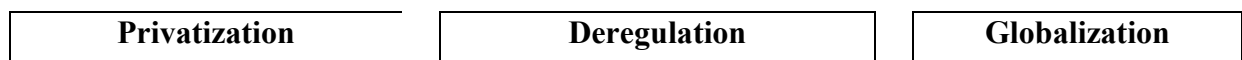


New Trends on Political Risk Cover

Traditional viewpoint of ECAs to political risk

- distinctively separate from commercial risk
- mainly associated with transfer risk, typically the risk of Paris Club rescheduling caused by shortage of foreign currency
- primarily related with individual debtor countries

New trends of global economy



| | | |
|--|--|--|
| <p>-big rush of privatization in developing countries ex)Asian countries, East European countries, South American countries -traditional public projects are initiated by private sector</p> | <p>-deregulation of currency regimes & financial sector ex) flexible exchange rate system, flexible interest rate system -traditional controlling power of Government on the currency & finance is transferred to private sector</p> | <p>-the opening-up of national economy ex)patterns of capital flow become diverse -loan from banks & ECAs (traditional) +foreign direct investment +portfolio investment +bonds</p> |
|--|--|--|

Influence of the new trends on ECA

| Privatization | Deregulation | Globalization |
|---|--|---|
| <p>-drastic decline of the proportion of pure sovereign risks in ECAs' total business -increase in demand for commercial & project risk -project finance is popular</p> | <p>-national economy becomes vulnerable to the external shock -transfer delay & Paris Club rescheduling will be no more typical pattern of risk -depreciation of local currency & payment problem of individual buyer is becoming important risk to consider</p> | <p>-country risk analysis needs more information of the global influence on a national economy -diverse creditors of a nation will influence the negotiation procedure or pattern of the debt rescheduling</p> |

e. Coverage

| | |
|-------------------------|---|
| Insurable amount | Contract amount - down payment + deferred interest |
|-------------------------|---|

| | |
|-----------------------|--|
| Insured amount | Coverage ratio x insurable amount |
| Coverage ratio | 95% |

Cf.) Coverage ration of other ECAs

-Coface, Hermes, SACE and lots of European ECAs: 95%

-U.S. EXIM, ECGD: 100%

-EID/MITI: 97.5%

Insurable Amount of ECAS

| | KEIC | U.S.EXIM | ECGD |
|---|--|--|--|
| Maximum (OECD Guideline) | 85% of contract amount + deferred interest | same as KEIC | same as KEIC |
| Insurable amount | Same as above | U.S. content amount within the above maximum limit | U.K. content amount + EU content (within the limit of 30% of total contract amount) + foreign content (limit of 15% of T.C.A.) |
| Minimum requirement of national content | 30% | 50% | 30% |

f. Claim Period

-bankruptcy: immediately

-delay: three months after the due date

g. Indemnified Amount

-unpaid principal & interest

-interest from the due date to the date of indemnification (KEIC does not cover but is planning to)

h. Two types of indemnification

| | Explanation | Applied Policy |
|----------------------------------|---|----------------------------|
| Pro rata indemnification system | Indemnified Amount = real loss x coverage ratio | Post-shipment cover policy |
| Real loss indemnification system | Indemnified Amount = real loss =<Insured amount | Pre-shipment cover policy |
| WHY? | -pro rata system is used in case of high coverage ratio, i.e. high possibility of total loss -real loss indemnification system is used in case of low coverage ratio, i.e. high possibility of partial loss -in case of pre-shipment cover, real loss system is applied because indemnification is made after deduction of the value of non-exported goods & the expected margin of the transaction | |

How much interest should be covered?

Q. If a lender receives a good deal in loan negotiation with higher interest rate than the usual one, should ECA cover the high interest rate or the usual one?

A. Guaranteed interest rate of ECA is not necessarily equal to the contract interest rate?

-KEIC usually covers the contract denominated interest rate, but if we find an excessive margin for the lender, we can cover on a usual basis

-Other ECAs' practice is the same as KEIC

i. Recovery

Commercial risk

- debt collection agency
- lawsuit
- negotiation with the buyer
- notification to ECAs
- recover the goods & resell

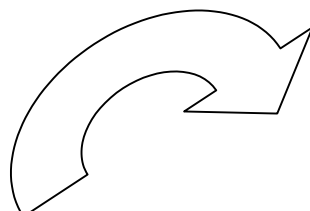
Political risk

- bilateral negotiation
(Government to Government)
- multilateral negotiation
(Paris Club meeting_
- ECAs' common line to the country

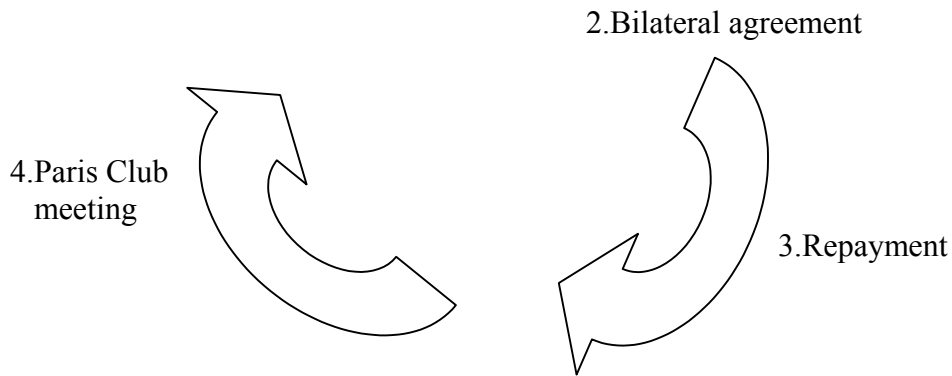
3.Paris Club Rescheduling

- What is Paris club rescheduling
 - creditor countries' meeting to discuss rescheduling terms in case of a payment problem in the importing country
- Debt rescheduled in Paris Club
 - officially financed debt with over 1 year repayment term
 - debt related to export credit insurance with over one year repayment term
- Profile of Paris Club Rescheduling
 - rescheduled 250b dollars with 61 countries since 1976

Procedure of Paris Club Rescheduling



1. Investigation of
Official Credit



RISK IN MEDIUM & LONG TERM EXPORT CREDIT INSURANCE

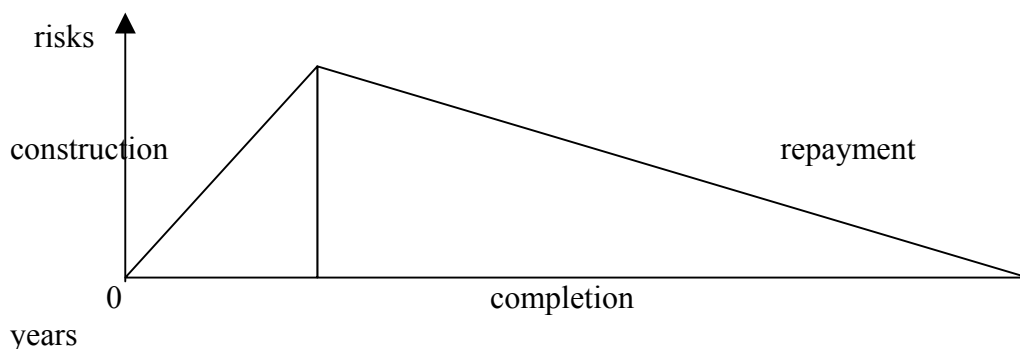
1. Risk Phases

- Pre-completion Risk: failure to complete project
- Post-completion Risk: failure to repay

2. Types of risk

- political risk
- cf.) extended political risk
- commercial risk or project risk

Project Risk Phases



1. Project Risk Assessment of ECAs: Past & Present

a. Past Practice

- ECAs' risk assessment was focused on the country risk analysis
- ECAs had little appetite for commercial risk or project risk

b. New Trends

- rush of privatization in many developing countries
- spotlight on project finance
- ECAs face new demand for project risk or commercial risk

Traditional approach and new approach on risk assessment

| | Traditional | New |
|--------------|--|---|
| Project type | -Public project with MOF guaranteed financing -Private project with 1 st class bank guaranteed financing | -Private project with non-recourse or limited recourse financing (Project Finance) -Project risk (establishment of independent project finance team) |
| Main concern | -country risk | |

Past:

Guarantee based project

- a. Government's will & ability to pay
- b. Importing country's payment experience
- c. Balance of payments
- d. Capital flow to the importing country
- e. Priority of the project in the importing country
- f. Credit status of buyer or guarantor in a private project

Present:

Limited recourse project finance

A Government's supporting policy for the business & the possibility of termination or suspension of the support ex) exemption of tariff, tax benefit, transfer guarantee, etc.

Analysis of the legal, political, social & economical environment for the project, and the influence of the change of the environment on the project feasibility

Project feasibility with cash flow analysis

2 Risk Assessment in Project Finance

a. What is Project Finance

- non-recourse financing
- limited recourse financing

-asset based financing

b. Background

-privatization: high demand of infrastructure in developing countries & limitation of Government capability to finance

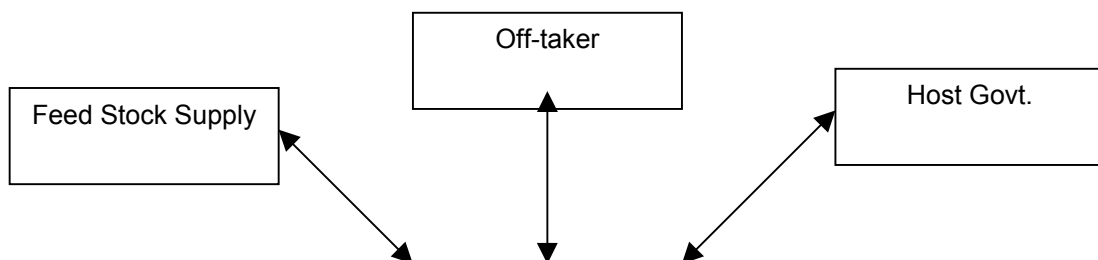
-deflation of the economy of advanced countries

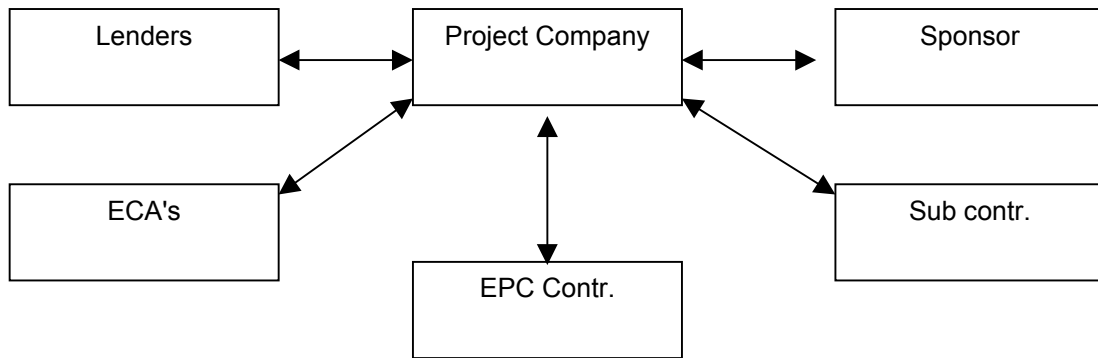
-pursuing the high-yield financing of the banks

c. Participants in Project Finance

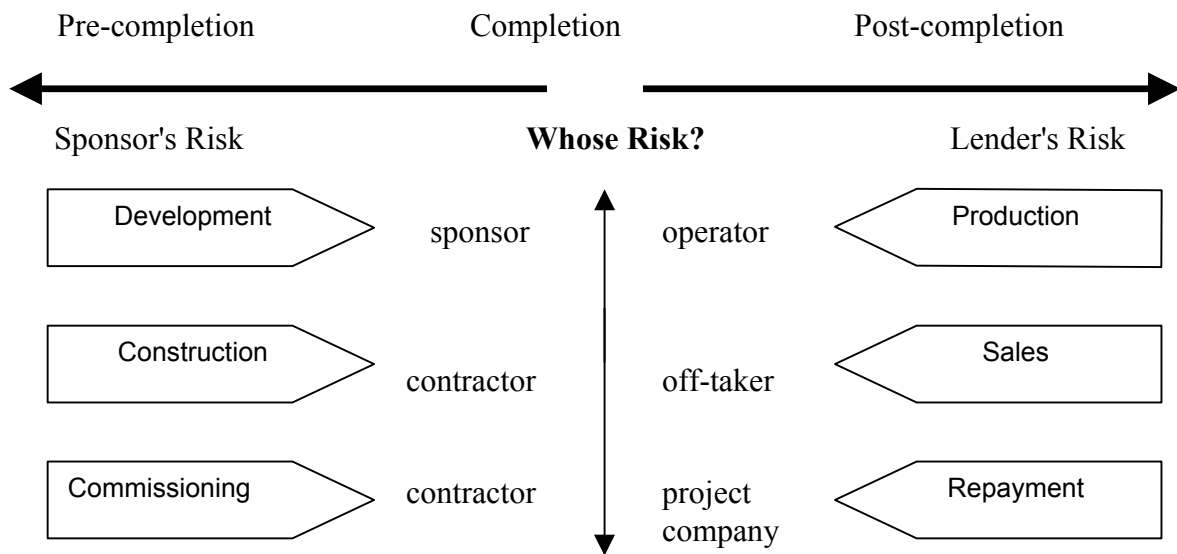
- 1) sponsors
- 2) project company
- 3) EPC contractors and sub contractors - EPC: Engineering, Procurement & Construction
- 4) Lenders
- 5) ECAs
- 6) Others
 - feed stock suppliers
 - long term off-takers
 - host government
- 7) advisors of sponsors & lenders

GENERAL STRUCTURE OF P.F.





e) Project Phases & Risk Takers



3. Risks in Project Finance

- Completion
- Delay
- Cost-overrun
- Country
- Operation
- Market
- Cash-flow

4. Risks and Mitigants

| Risks | Mitigants |
|---|--|
| Bankruptcy of contractor | |
| Failure of equity subscription by sponsor | Equity subscription of sponsors shall be made before the loan disbursement |
| Failure of completion | Completion guarantee of sponsors which is a kind of payment guarantee |
| Cancellation of Government licence | Letter of comfort issued by host Government |
| Force majeure | Insurance cover for damages to project in the event of a fire, flood, etc. |

| | |
|---|---|
| <ul style="list-style-type: none"> • Bankruptcy of contractor • Failure of equity subscription by sponsor | Equity subscription of sponsors shall be made before the loan disbursement |
| Failure of Completion | Completion guarantee of sponsors which is a kind of payment guarantee Letter of comfort issued by host Government |
| <ul style="list-style-type: none"> • Cancellation of Government licence • Force majeure | Insurance cover for damages to project in the event of a fire, flood, etc. |
| | Set up the rational project schedule with the help of an independent consultant |
| Delay of Completion | Date certain construction contract with the liquidated damage clause which can cover financing cost during the delayed period |
| Project is not proceeding within the expected schedule | Review the contractor's past record to perform the same kind of project |
| Incorrect evaluation of the cost Abuse of the funds Additional cost incurred by host government | Cost evaluation of an independent consultant |

| | |
|--|--|
| | |
| Cost over-run | Fixed price construction contract -construction cost over-run is covered by the contractor sponsor's guarantee for the cost over-run |
| Project cost exceeds the budget | -sponsor covers the cost over-run by other reasons except the construction cost |
| Host Govt's breach of undertaking -cancellation of licence, tax benefit, etc -restriction on transferring foreign currency War, insurrection, revolution, etc | |
| Country Risk | Letter of Comfort from host Government -if possible, legally binding one Establishment of Escrow Account -if the project generates revenue in hard currencies |
| Economic difficult in Host country | Co-financing or joint financing with other ECAs and Multilateral Agencies |
| New technology -output doesn't reach to the expected level of quantity & quality -break down of the plant | Use old proven technology -if it is a new technology, thorough feasibility study should be made |
| Operation Risk | Reliable & experienced operator Bonus/Penalty clause in the O & M Contract Cap on the operating cost or indexed to revenue |
| Inexperienced operator -operator is not accustomed to the technology applied to the operation of the plant | |

| | |
|--|--|
| <p>Failure of sales</p> <p>-fluctuation of market condition</p> | <p>Long term off take agreement with creditworthy purchaser</p> <p>-not always possible</p> <p>-wholesale product vs. retail product</p> |
| <p>Market Risk</p> | <p>Market research performed by an independent consultant</p> |
| <p>Decrease of sales volume</p> <p>-production of new items which can substitute for items produced by the project</p> <p>Price down</p> <p>-supply exceeds the demand</p> | <p>Host Government's guarantee for price support (e.g. power plant) or minimum passage guarantee (e.g. toll road, pipelines)</p> |
| <p>Failure of expectation</p> <p>-cost-up by excessive inflation</p> <p>-debt service increased by unusual depreciation or hike of interest rate</p> | <p>Cash deficiency guarantee of the sponsors</p> <p>-limits in amount or period</p> |
| <p>Cashflow Risk</p> | <p>Price indexed to inflation or exchange rate</p> <p>-selling price is indexed to the manufacturing cost & debt service amount</p> |
| <p>Increase of capital expenditure</p> <p>-new guideline is imposed on the plant (e.g. new guideline on environment)</p> | <p>Conservative estimate of the variables</p> |

5. KEIC's underwriting check points on project finance

- What is the creditworthiness status of participants?
- What are the major risk factors in the host country?
- Is the project in an important sector in the host country?
- Does the project generate revenue in hard currencies?

- Does the project have a long-term off-take agreement?
- What support does host government give to the project?
- What is the debt equity ratio?
- Has the proper due diligence been planned?
- What does the completion guarantee of the sponsor cover?
- Does the project generate enough cash flow to repay the loan?
- Do the repayment terms satisfy the OECD Consensus?

6. Procedure of Risk Assessment

| Random Assessment | Regular Assessment |
|---|--|
| <ul style="list-style-type: none"> • Creditworthiness of sponsor | <ul style="list-style-type: none"> • Creditworthiness of project participants |
| <ul style="list-style-type: none"> • Market risk | <ul style="list-style-type: none"> • Deep study on all the risk factors -market risk, feed stock supply risk, operation & maintenance risk • Deep assessment on country risk |
| <ul style="list-style-type: none"> • Attitude of host government | <ul style="list-style-type: none"> • Assistance from independent consultants • Documentation |
| <ul style="list-style-type: none"> • Overall country risk assessment | <ul style="list-style-type: none"> • Securities |
| Issue of Letter of Intent | Issue of Policy |

Topic3: Premium System in Medium & Long Term Export Credit Insurance

PRINCIPLES OF PREMIUM POLICY

1. Principles of Premium

- enough to maintain sound insurance business
- enough to save some portion of profit for dividends & reinvestments
- closely related with the amount of risks

2. ECA's principles

- enough to cover claims & operation cost on a long term basis
- long term break-even is the main target: World Trade Organisation E.C.A.'s are required to break even over time and not subsidise

3. Do ECAs reach the goal of long-term break even?

- average loss ratio of ECAs in advanced countries is about 400-500% and the accumulated amount of loss about USD100billion.
- Dilemma of ECAs; promote nations exports while meeting WTO guidelines of long term break even.

4. Trends

- raise the overall premium level
- strengthen the country risk assessment and project appraisal

DETERMINING PREMIUM LEVEL

1. Factors of determining premium

- a. country risk factor
 - 4 to 8 categories of country rating
 - KEIC has 8 categories
 - Key factors of country rating

-payment record, external debt, debt service ratio, etc

- Gap in premium level according to categories
 - premium of 8th category is eight times the 1st category

b. Other factors

- Repayment period
- Buyer's type
 - public buyer gets 10% discount in KEIC system
- Payment guarantee
 - 25% discount in KEIC's system
- Policy type
 - political risk only policy
 - comprehensive risk policy

*KEIC has no political risk only policy

2. OECD's efforts to establish harmonized premium level

- Background of the harmonization
 - prevent a credit race among ECAs
 - big difference in premium level among ECAs
 - eliminate the export subsidy granted by ECAs due to low premium level
- Consultation in OECD
 - begun in May, 1994
 - concluded in June, 1997

3. OECD's country rating scheme

- Countries rated
 - 70 countries other than OECD countries
- factors of rating
 - payment experience
 - financial situation
 - economic situation
 - political situation
- rating procedure
 - 1st stage: quantitative evaluation

2nd stage: qualitative evaluation

- **Premium table by country category**

| 1 | 2 | 3 | 4 | 5 | 6 | 7 |
|------|------|------|------|------|-------|-------|
| 1.50 | 2.94 | 4.91 | 7.23 | 9.77 | 12.13 | 14.68 |

*On the basis of 11.5 year repayment period

- **Major countries in each category**

- 1st: Singapore, Taiwan, HongKong, Malaysia
- 2nd: China, Czech, Chile, Thailand
- 3rd: Hungary, Poland, etc. (13 countries)
- 4th: Saudi Arabia, Mexico, etc (10 countries)
- 5th: Romania, Russia, Turkey, Vietnam, etc. (15 countries)
- 6th: Pakistan, Iran, Algeria, etc. (11 countries)
- 7th: Angola, Bulgaria, Iraq, Libya, etc. (13 countries)

4. Premium Factors of individual project

a. country grade category

b. exposure period

-half of loan drawdown period + repayment period

-premium level rises as the exposure period increases

e.g.: premium rate of a project with 10 year exposure period in 4th grade country is 6.35%, and a project with 12 year exposure period in the same category is 7.52%

c. quality of policy

-coverage, guarantee or insurance, cover the interest incurred from the due date to indemnification or not.

SECTION 6

SUPPLEMENTARY TRADE INSURANCE FACILITIES

**CHAPTER I NOTE ON SUPPLEMENTARY TRADE INSURANCE
FACILITIES**

**APPENDIX OUTLINE OF ECA FACILITIES IN VARIOUS
COUNTRIES**

CHAPTER I

SUPPLEMENTARY TRADE INSURANCE FACILITIES

The principal facilities offered by E.C.A.'s are described in detail in the various chapters of this manual. However, most E.C.A.'s provide some ancillary or supplementary facilities depending on the nature and needs of their respective country's export trade and the interrelationship between the E.C.A. and the financial system in individual countries.

While no comprehensive summary of such facilities has been tabled , the attention of users of this manual is drawn to Section III, where reference to such facilities is made in the description of the Trade Insurance systems of nine different E.C.A.'s.

In addition, Appendix 1 contains an outline of all the facilities provided by seven E.C.A's in Developed Countries.

Appendix I

Outline of ECA Facilities Countries

| Country Name | Japan | France | U.K | Germany | Germany | U.S.A. | U.S.A. |
|--------------------------|---|--|--|---|--|--|---|
| Organization Name | EID/MITI | COFACE | ECGD | HERMES | TREUARBEIT | EXIMBANK | OPIC |
| Official name | Export-Import Insurance Div. Ministry of International Trade And Industry | Compagnie Francaise d' Assurance pour le Commerce Exteieur | Export credit Gurantee Department | Hermes Kreditversicherungs -Aktiengesellschaft | Treuarbeit Akienges- ellschaft Writscha- ftsprufungsgesell- Schaft Steuerberatu- ngsgesellschaft | Export-Import Bank of the United States | Overseas Private Investment Corporation |
| Established in | 1950 | 1946 | 1919 | 1917 | 1925 | 1934 | 1971 |
| Insurance Type | General Trade Insurance, Export Bill Insurance Exchange Risk Insurance, Export Bond Insurance, Prepayment Import Insurance, Overseas investment Insurance, Overseas United Loan Insurance | Export Insurance Insurance, Cost-up Insurance, Bond Insurance, Overseas Investment Insurance, Intermediary Trade Insurance, Short-term Comprehensive Insurance | Export Insurance, Exchange Risk Insurance, Cost-up insurance Bond insurance, Overseas Investment Insurance Intermediary Trade Insurance, Bank Financing Guarantee Insurance Buyers Credit Guarantee Insurance Short-term Insurance (Sold to NCM in 1991) Technical Cooperation Insurance | Export insurance Exchange Risk Insurance, Lease Insurance, Construction Insurance, Bond insurance, Intermediary Trade Insurance, Short-term Insurance | Overseas Investment Insurance | Export Insurance (Only for short-term and mid-term.) Guarantee for Commercial bank, Lease guarantee (Only for mid-term and Long-term.) | Overseas Investment Insurance |

SECTION 7

EVALUATION AND CONTROL OF COUNTRY RISK

CHAPTER I THE JAPANESE APPROACH

CHAPTER II THE UNITED STATES APPROACH

EVALUATION AND CONTROL OF COUNTRY'S RISK

Chapter 1 THE JAPANESE APPROACH

[1]. What Is Country Risk?

There is no exact definition of country risk. In general, it is risk caused by conditions in the government of a trade partner engaged in international trade, overseas investment, and financing and which are not attributable to the parties to the export contract. In trade and investment insurance, the word political risk is normally used synonymously with country risk.

The following are the main causes of country risk:

- (a) Restriction or prohibition of foreign exchange transaction
- (b) War, civil commotion, revolution
- (c) Restriction or prohibition of imports
- (d) Expropriation

In contrast, there is a commercial risk. Commercial risk is risk for which the trade partner engaged in international trade can be held accountable.

Main causes of risk:

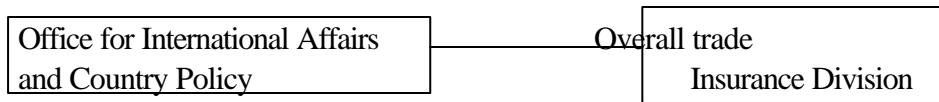
- (a) Bankruptcy of export contract counterparty
- (b) Nonpayment

- (c) Unilateral cancellation of an export contract

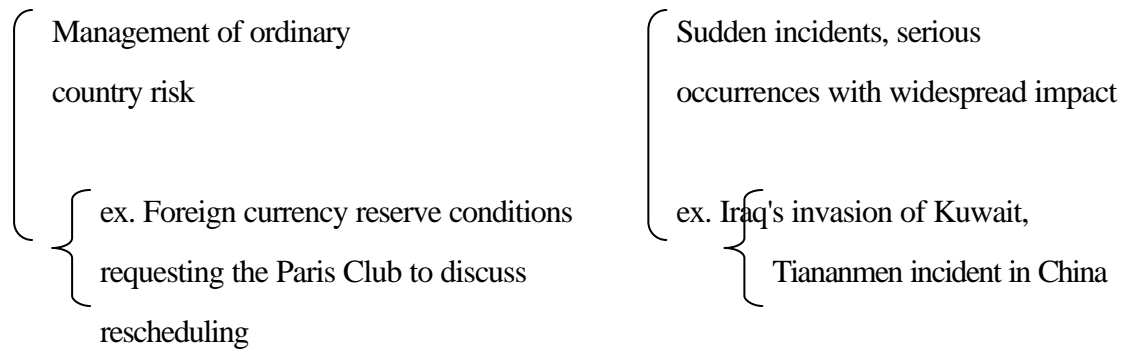
[2] Country Risk Management

Implements Risk Control Country-by-Country to prevent or minimise the need for the trade and investment insurance department to have to make claims.

1. Main Structure of Risk Management

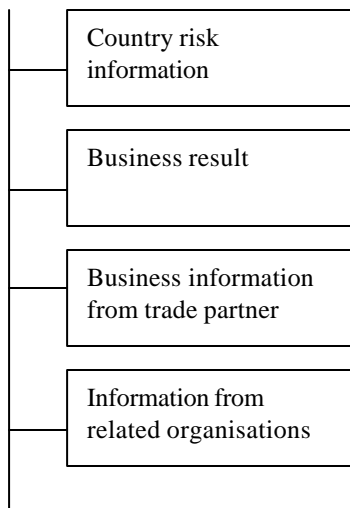


2. Degree of Risk



3. Details of Risk Management

(1) Information Type and How to Grasp it



(2) Processing the above information:

- (1) Collection and distribution
- (2) Analysis and prediction
- (3) Evaluating

(3) Response to Changes in Country Risk

- (1) Determine a method for making changes in underwriting policy, etc.

Meeting to evaluate underwriting policy

The meeting for actual practitioners in the organisation
Chairman: Executive Director for International Affairs
and Country Policy Office
Date: Every Friday morning

- 1) Issuing warning

2) Risk management (Changes in underwriting policy, monitoring system change, establishing the total commitments limit, etc.)

Country risk committee

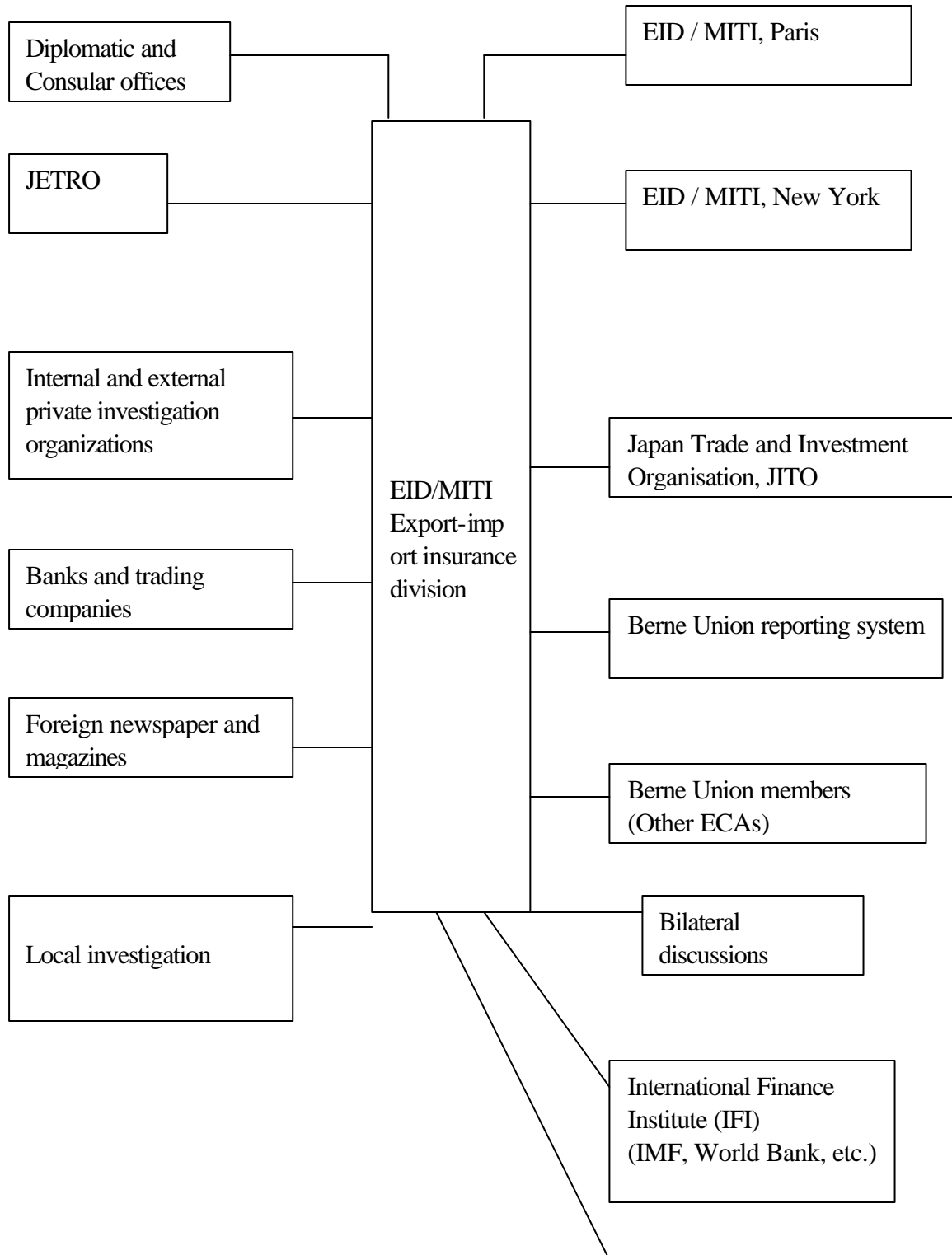
Known as the executive committee
Chairman: Trade Insurance Manager
Date: Every Wednesday afternoon

- 1) Determining underwriting criteria, for example, underwriting policy
- 2) Evaluating transactions which do not fall within the criteria

(2) Establishing country-rating and premium rate by country

[3] Evaluating Country Risk

(1) Information collection organizations



(2) Major Sources for Collection of Information

(1) Reports from organizations which perform various analyses

(a) IMF report

(b) IIF (The Institute of International Finance Inc.) / Washington mainly analyzes country's economies

: Issued **once** or twice a year for major countries, and every other year for other countries.

(c) EIU (The Economist Intelligence Unit) / London Analysis of each country's political situation and economy

: Issued quarterly

(d) PRS (Political Risk Service) / New York

mainly analyzes country's political risk

: Issued annually

(2) Publications

(a) IFS (International Financial Statistics)

Details of economic situation, exchange rate, foreign currency reserve, trade figures, balance with banks, finance, etc.

: Issued monthly

(b) WDT (World Debt Table)

mainly deals with foreign debt of developing countries.

: Issued annually

(3) GRH, (Global Rating Handbook) Standard and Poors;

Country ratings, company ratings, bank ratings (credit strength company ratings)

: Issued monthly

(d) GSMR (Global Short-Term Market Record)

Same as (c); Moodys
: Issued monthly

[4] Response to Changes in Country Risk

1. Making Changes in Underwriting Policy

(1) When acquiring information which leads to a change in underwriting policy, immediately determine the following Basic Policies depending on the degree of risk. By doing this, it is possible to avoid an increase in the amount of new underwriting, which can help minimize the risk of future claims, and increase new underwriting as the country risk decreases in order to increase premium income.

- 1) Suspending underwriting (off-cover)
- 2) Tightening conditions for underwriting
- 3) Easing conditions for underwriting
- 4) Resuming underwriting
- 5) Case-by-case basis

(2) Information which leads to a change in underwriting policy

Obtain information regarding changes in each item of country rating as soon as possible and before the insured can obtain it.

(3) Relationship between the degree of risk and basic policy

- 1) Suspending underwriting (off cover):
 - (a) In the event that payment arrears occurred regarding existing insured credit
 - (b) In the event that a Paris Club Reschedule has been requested
 - (c) In the event that debt has been reduced / (partly forgiven) (Egypt, Poland)
 - (d) In the event that the country's political or economic situation is extremely unstable because of a regional dispute, etc. (Iraq, Angola, etc.)

2) Resuming underwriting (resumption)

The conditions for resuming underwriting are;

- (a) Based on the agreement of Paris Club re-schedule, bilateral agreement is concluded.
- (b) Based on the agreement, repayment of interest is restarted. (once or twice)
- (c) The past rescheduled debt is repaid consistently, and the country risk, such as political and economic situation has improved.

However, in the event that an international agreement for the country exists, or in the light of political considerations, even though the conditions

(b) through (d) are not satisfied, the underwriting might be resumed.

The conditions for resuming for the debt reduced countries are;

- (a) Continuous sound economic performance
- (b) Good relationship with international financial organizations
- (c) Repayment of principal has started

3) Tightening conditions for underwriting

- (a) Based on the Political and economic situation, Specifically, In the event that civil unrest has occurred, or foreign currency reserves suddenly decreased, and an arrears in payment is highly likely. (Although the, conditions for underwriting have been tightened depending on the degree of risk, an automatic change is difficult to implement.)
- (b) In the event that underwriting is continued because of external forces even though arrears occur.

4) Easing conditions for underwriting

- (a) In the case that the condition in (1-(a) is seen to be improving.
- (b) In the case that the country's recovery / progress is satisfactory.

(5) Case-by-case basis

- (a) When resuming underwriting, if there is concern whether payment will be continued, it is possible to stop the underwriting in practice by evaluating each

transaction even though the trade partner's country risk has suddenly become worse. (Resume cover on a case-by-case basis)

- (b) When it is necessary to renew underwriting policy for an inexperienced country for which the underwriting policy has not been fixed. This is because there is not enough information about country risk.
- (4) Conditions for underwriting (Open with certain restrictions)
- 1) The conditions for underwriting are as follows;
 - 1) Country category (Premium rate)
 - 2) Insured percentage, 97.5 ~ 70%
 - 3) Restriction of usance period, one year, six months
 - 4) Requiring ILC (Letter of credit)
 - 5) Limiting the size of Individual transaction
 - 2) For these underwriting policies how to appropriately avoid risk when combining various factors is determined case-by-case based upon past experience.
 - 3) However, it is thought that restriction of underwriting, such as reducing the country grade by one, 70% of insured percentage, shortening usance period (two years to one year), and limiting the size of transactions, can have a, strong positive impact.

2. Rules of underwriting

(1) Rules for suspending underwriting (Off-Cover)

- | | |
|----------------------------------|--|
| 1) Debt reduction | When a request is made to the Paris Club |
| 2) Paris Club reschedule | When a request is made to the Paris Club |
| 3) Claims | When a request is made for claims |
| 4) Increased accumulated arrears | When determined by CR country risk committee |
| 5) Poor condition of the economy | When determined by CR country risk committee |
- because of the United Nations sanctions, political change, etc. (when to change)

(Note) In the case of 1) and 2), transactions that involve suspension of underwriting are Medium- and Long-term and Short-Term transactions over one year.

(2) Rules for Resuming

1) Basically, underwriting is not resumed for debt reduced countries.

Leave the least-less developed country (LLDC) to ODA (ALD facility)

Do not resume for lower- middle income countries for some time.

2) For countries-which have been rescheduled, evaluate when the first payment

is completed and the remaining payments are thought to be complete after the Paris Club bilateral agreement is concluded.

However, even after the first payment, if it is likely to be rescheduled again, maintain close observation.

However, if there is an international agreement for flexibility or a political request, this does not have to be followed.

(3) Rules for starting underwriting

Currently, there are 146 countries and 237 regions for which the underwriting policy is medium- and long-term.

A new underwriting policy is set when a transaction is requested or the trade partner country has requested. The underwriting is decided according to the political and economic situation and underwriting policy of other countries' insurance organizations. Basically, underwriting with limitation is for short-term transactions, and case-by-case for medium and long-term transactions.

(4) Rules for establishing Credit Line

Credit Line is given extremely exceptionally to countries with underwriting with restrictions, or off-cover, in cases which need special care because of the international trade policy or (and) foreign policy.

(In some cases, Credit Line for short-term transactions is only given.)

3. Exposure Control

(1) To Minimize. future payment of claims, set a Total Commitments Limit for each country, and control the exposure.

(2) Establish a system which checks, once a month in advance, that the Exposure (Exposure, = Insured Amount + commitments + Unrecovered Claim) is not higher than the Total Commitments Limit.

(3) Countries which need to be set a Total Commitments Limit

- a) A country which needs to be controlled because a certain degree of increase in underwriting is projected.
- b) A country for which it is thought that insurance without restrictions would substantially increase exposure, if arrears occurred in the future, they would be substantial.
- c) A country which is underwritten for medium -and long-term transactions even though it is rescheduled.
- d) A country for which a Credit Line has been established

- (4) Formula to calculate total commitments limit
- a) Total commitments limit is set for a country which needs controlled exposure, and is calculated according to a formula. There are currently 63 countries for which Total Commitments Limits are set.
 - b) The formula is calculated based on the elements of country risk, such as a country's export volume amount, foreign currency reserves, import volume, and outstanding external debt, including the share of Japan for each elements, and multiplied by a constant coefficient.

(5) Japan's Country Risk Evaluation Method

| |
|------------------------|
| 1. Introduction |
|------------------------|

1. To set the premium rate based on the risk, Japan classifies a country by its country risk, every year, using an evaluation system.
2. This evaluation system is based on the following three indexes.
 - (a) Country's political and economy situation
 - (b) Business Results I (Balance of payment,-,)
 - (c) Business Results II (situation of claim and recovery)
3. To evaluate, first, score for each group explained above, and next, make an adjustment according to the previous year's score, and classify country risk.

4. Maximum score of country risk is 270 points: 1) maximum of 135 points for country's political and economy situation, 2) maximum of 70 points for Business Result I (Balance of payments), and 3) maximum of 65 points for Business Result II (Claim and recovery situation)

5. Japan classifies a country in eight categories (levels) based on evaluation. Reflecting the evaluation results, a different premium rate is applied for each country.

6. The new country classification and premium rate are updated by a new evaluation and applied basically every April at the start of the new fiscal year.

II. Political and Economic Situation

1. Selection of Index

1.1. The index for the country's Political and economic situation is evaluated by the following five categories:

- Domestic political and social, situation
- External relations of the country
- Economic structural factors
- Domestic economy and domestic economic system
- Balance of international payments, outstanding external debt

1.2 Evaluation items and scoring

Each of the five indexes consists of specific evaluation items, and is scored 0 to 3 points. The coefficient of importance is as shown in (), and a higher coefficient indicates more importance.

1.2.1 Domestic political and social situation

- 1) Political stability (2)
- 2) Longevity of policy after political change (1)
- 3) Ability to implement policy (1)
- 4) Risk of civil unrest and social disorder (3)

1.2.2 External relations of the country

- 1) Possibility of war or dispute (3)
- 2) Relationship with international finance organization,
such as IMF and World Bank (2)

1.2.3 Economic structural factors

- 1) GNP (GDP) (1)
- 2) GNP per capita (GDP) (2)
- 3) Industrial products share in exports (1)
- 4) Share of energy imports in product exports (1)
- 5) Self-sufficiency rate in food, or share of food in imports (1)
- 6) Existence of natural resources (3)

1.2.4 Domestic economy and Institutional situations

- 1) Economic growth rate (latest one year) (1)
- 2) Economic growth rate (Tendency in last three years) (1)
- 3) Inflation rate (latest one year) (1)
- 4) Unemployment rate (latest, one year) (1)
- 5) Fiscal deficit (surplus) / GNP (GDP) (1)

- 6) Domestic capital formation or domestic savings / GNP (GDP) (1)
- 7) Establishment of economic system (including legal system) (3)

1.2.5 Balance of International payments, external debt

- 1) Current account balance / export(latest one year) (2)
- 2) Current account balance (Tendency in last three years) (2)
- 3) Total external debt /GNP (GDP) (3)
- 4) Total external debt / Export goods, services and income (3)
- 5)External debt (services) / Export goods, service and
export income amount (latest one year): DSR (debt service ratio)
(including both public and private) (3)
- 6) Foreign currency reserve / monthly import (latest one year) (2)

2.Weight of Index

2.1 Weighting or coefficient of importance is from 0 to 3.

For example, an index for "Politic stability" has 2 for its importance, and its coefficient is multiplied depending on the following elements of stability:

- 3 points Stable
- 2 points Cannot decide
- 1 point Unstable
- 0 point Extremely unstable

If a country is evaluated as Stable (3 points), as this index of importance is 2, the score of this index is 6 points (3 x 2).

2.2 The overall score for country' s political and economic situation is 135 points, and shares 50 % of the total maximum score, 270 points.

III. Business Result I (Balance of payment)

1. Selection of Index

1.1 Business result I is evaluated by balance of payment (only for political risk) for both short-term and medium- and long-term.

1.2 Balance of payment, is evaluated by results itself and the following factors

- Balance of payment = Premium + Recovery - Claim
- Loss ratio = (Claim - Recovery) / Outstanding liability
- Loss occurrence ratio = Loss occurrence amount / Outstanding liability
- Outstanding liability ratio = Outstanding liability / Total Commitment limit

- Balance of payment is an index which shows a country whose record is good.
- Loss occurrence-ratio evaluation includes those countries, which did not have to pay because money was deposited after the notice of occurrence of insured risk was submitted ie. Those who are constantly late payers
- Outstanding liability ratio is an index which shows the actual level of liability calculated against the country's total commitments limit

2. Weight of Index

2.1 Balance of payment is evaluated based on the amount, and other evaluation items as classified by the scoring system.

2.2 Evaluation of balance of payment is classified into 9 levels from a maximum of 24 points (over 1 billion yen) to 0 points (-10 billion yen or below).

2.3 Evaluation of loss ratio is classified into 8 levels from maximum of 21 points (0 %) to 0 point (1,000 % or more).

- When evaluating loss rate, if the outstanding liability is small (below 100 million yen), the evaluation score of a developed country is the maximum 21 points and 12 points for other countries.

2.4 The evaluation for the loss occurrence ratio is classified in seven levels from a maximum of 18 points (0 %) to 0 Points (1,000 Points or more).

- In the case that the Outstanding liability is too small (below 100 million yen) when evaluating the loss occurrence ratio, the evaluation Point, for developed countries is the, maximum 18 Points and 10 Points for other countries.

2.5 Outstanding liability ratio is classified in eight levels from a maximum of 7 points (0 %) to 0 points (100 % or more).

- Proper outstanding liability is a the total commitments limit which is specified for each country. For countries,; whose total commitments limit is not established, the - evaluation score is the maximum 7 points, and 3 for other countries.

2.6 Maximum evaluation score for Business Result I (Balance of payment) is 70 points.

IV Business Result II (Situation of claim and recovery)

While Business Result I (Balance of payment) evaluates country risk from the point of view of contribution and Influence on Japanese trade insurance finance, Business Result 11 (situation of claim and recovery) evaluates the payment, performance and arrears situation of countries in arrears, especially countries rescheduled by the Paris Club.

1. Selection of Index

1.1 Situation of claim

and recovery is evaluated according to the rescheduling agreement of the Paris Club, payment situation based on the rescheduling agreement, and the country arrears situation with other countries,

2. Weight of Index

2.1 Evaluation of a Paris Club rescheduling uses a penalty mark system starting at 40 points.

1) Evaluate the country according to whether the country is actually rescheduling or not, and if the country is actually rescheduling, reduce the score by 10 points.

2) The agreement of the Paris Club is evaluated by adding up the points, which were subtracted according to the range of rescheduling debt for each agreement. Elements for evaluation are as follows.

All past agreements are evaluated. The more recent the actual year is, the greater the minus points. For example, if rescheduling is agreed to in 1996, the elements will be the maximum minus points.

- Overall re-reschedule Maximum of 10 minus points
- Partial re-reschedule Maximum-of 7 minus points
- COD¹ change Maximum of 10 minus points
- Special treatment after COD Maximum of 6 minus points
- Capitalizing delayed interest increased Maximum of 5 minus points
- Capitalizing rescheduled interest Maximum of 10 minus points

3) Adjustment

- Debt reduced countries Decrease to one-third.
- Low and middle income countries Decreases to two-thirds

4) Evaluation formula

$$(40 - 1) - 2) \times 3 = \text{evaluation score}$$

2.2 The score when evaluating the recovery situation is 1) 30 points for recovery rate and re-reschedule rate, and 2) 25 points for balance recovery rate.

1) To evaluate the recovery rate and re-reschedule rate;

(a) evaluate the recovery rate in the list two years using maximum score of 15 points

(b) evaluate re-reschedule rate in last two years in maximum score of 10 points

(c) subtract (b) from (a)

(d) make a final adjustment according to the deviation in arrears situation in the last two years

- Formula for the collection rate is as follows:

$$(\text{Recovered amount} / \text{Recovered amount other than re-rescheduled amount}) \times 100$$

- Formula for re-re-schedule rate is as follows:

$$(\text{Re-reschedule rate} / \text{reschedule amount,}) \times 100$$

- Adjustment method of recovery rate and re-reschedule rate is as follows:

Regarding payment due in last two years.

A country which consistently falls, into arrears three months or more

Decrease the score to one-third

A country which has fallen into arrears three months or more

Decrease the score to two- third

A country which consistently fall into arrears one month or more

Decrease the score to two-thirds

A country which has fallen into arrears one month or more

Decrease the score to five-sixths

2) "Recovery Score" is evaluated in eighteen levels from 0 to 25 according to the ratio of total recovered amount vs. reschedule balance amount in the last two years.

- If the rate resulting from the calculation of the reschedule recovery amount divided by rescheduled debt balance in the last two years is 16% or more, the evaluation for the country is the maximum 25 points.

3) Formula for rescheduled recovery is as follows:

(When evaluating 1996)

(a) (Evaluation score of reschedule recovery rate of 1994 + Evaluation score of reschedule recovery rate of 1995 - Minus points of re-reschedule rate of 1994 - Minus points of re-reschedule rate of 1995) X Adjustment value The minimum evaluation score is 0.

(b) Evaluation score according to balance recovery rate

(c) Evaluation score of past history of insurance (likelihood of claim and the collection situation) (a) + (b)

2.3 Evaluation of Arrears Other Than Reschedule

If a rescheduled country has had the following two arrears other than rescheduled Amounts in the last two years, subtract point from total Of [2.1 Evaluation of rescheduling] and [2.2 Evaluation of recovery]

1) Arrears (Credit before COD (cut-off-date))

For temporary arrears; this may lead to rescheduling in the future. Do not subtract the score immediately. However, if there are arrears beyond any one-year period in the past two years, it is evaluated according to the six levels. The score differs depending on the length of arrears and whether or not the arrears have been resolved.

2) Arrears after COD

if there have been arrears in the post two years, it is evaluated according to six levels.

2.4 Subtotal is calculated by adding (a) the score for the Paris Club rescheduling agreement

2.1 and (b) Recovery/2.2 and subtracting (c) Arrears situation other than rescheduling/2.3.

To evaluate the claims and recoveries, recalculate the total of 95 to a total of 65.

3. Evaluation for Non-rescheduled Country

3.1 To evaluate a country which has been rescheduled by the Paris Club and which does not have debt related to Japan, apply almost the same method explained above with the exception of evaluating the arrears situation relative to G7 countries.

3.2 To evaluate the claims and recovery situation of non-reschedule countries, first evaluate the arrears situation relative to Japan, (for example, if there have been no arrears relative

to Japan in the past two years, score 65 points), and then subtract points according to the arrears situation relative to the remaining G7 countries.

V. Country Classification

1. Country classifications are according to the following eight categories using 270 as the maximum score.

| | |
|------------|---------------|
| A category | 245 or more |
| B category | 225 – 244 |
| C category | 200 - 224 |
| D category | 190 - 199 |
| E Category | 180 - 189 |
| F category | 155 - 179 |
| G category | 128 - 154 |
| H category | Less than 128 |

A suspended – underwriting (off cover) country is generally classified in H category.

2. Premium by category

It is a basic rule of the Japanese trade insurance business that the revenue and payment should be balanced.

Japanese trade insurance law specifies that the premium in the contract of trade insurance is specified by a government ordinance that the income of government insurance business following trade insurance law covers the expenditure,. Also, Japanese trade insurance business is run without receiving any subsidy.

To maintain the balance of insurance business, Japan restricts underwriting, or reduces the insured rate of a country whose risk is high. Also, the premium rate based on risk is revised every year as the risk changes.

Basic premium rate is revised approximately once in three years based on the medium- and long-term vision to keep balance of its result and establish proper premium rates according to risk.

APPENDIX I

IV. Example Evaluation of Country Risk by Country

Algeria, Brazil, Turkey

ALGERIA

1. Political Situation

(1) After the landslide victory in general election in 1991, FIS (Islamic Salvation Front) was illegalized by the government who was afraid of the possible establishment of Islamic government. As the result, it was followed by the intensification of activities by terrorists led by FIS.

(2) Experiencing Political vicissitude over the administration, Mr. Zeroual (from military circle) assumed the office of presidency in February 1994.

(3) At the time of presidential election held in November 1995, incumbent President Zeroual was re-elected with overwhelmingly high support, obtaining 61% of votes when overall voting rate in the election of that Year was as high-as 75.-5%, even though the election was held under the strong opposition by FIS to boycott it.

(4) A national referendum to decide whether to revise the national constitution was approved by majority vote of 85.5%, under the voting rate of 79.8%, despite the opposition group's calling for boycotting the voting. The major points to be revised were to specify: (a) the separation of Politics and religion, (b) a ban to organize a Political party based on the Islamic religion, aiming at an elimination of FIS from its Political activities.

Other points to be revised included denial of violence, principle of democratic and republican system under the majority rule.

(5) Following the national parliamentary election on 5th June 1997, an incumbent administration RND became the first ruling party but without obtaining the majority. Under the circumstance, it is predicted that RND may go toward the direction of forming a coalition government with conservative parties in the future.

(6) Meanwhile, intensification of terrorist activities has been growing around the capital city of Algiers. However, in the southern part of the country, a main region for being covered by the trade insurance, quite few such activities have been observed. Moreover, hydrocarbon industry, the country's major industry for export has not been attacked by terrorists so far. It is due to the fact that these areas are strictly guarded by local police and at the same time these facilities are also regarded as strategically important for guerillas as well.

(7) Incidentally, Japanese Foreign Ministry has been warning several times to Japanese residents in Algiers to leave the city as soon as possible and to incoming Japanese not to enter this country as Algerian public security has been deteriorating since 90s.

2. Economic Situation

(1) Details in the Past

(a) Due to the sharp fall in oil Price 1986(\$28/B '85 to \$8/B '86), Algerian international balance of payment recorded a substantial deficit in 1988(\$2.2 billion)

(b) In 1994, the first agreement for rescheduling was made in the Paris Club due to the difficulty in cash-flow in Algeria.

(2) Since the secondary rescheduling in 1995, Algerian economy has been going relatively smoothly. However the country's economic structure has not changed as their earning of foreign currency is still heavily depending on hydrocarbon industry (about 90% of total export value).

(a) Economic growth rate

The growth has been predicted in the level of 4% to 5% since 1995. It was attributed to the soaring of oil prices (average \$20/B), and increase of export due to the production increases of hydrocarbon.

(b) Inflation

Due to the increase of crop harvest and restriction of the increase of food price, the country's inflation rate was improved substantially to 15% level compared to its peak of 38% in 1994.

(c) Financial revenue and expenditure

Basically, the financial revenue heavily depends on hydrocarbon industry, affected by the fluctuation of international oil price. Being favorably affected by an increase of hydrocarbon revenue and reduction of fiscal deficit in the past few years, the amount of deficit in GDP has steadily improved in 1993(-8.7%), 1994 (-4.4%), and in 1995(-1.4%)

(d) International balance of payment

The I.M.F. predicts that though the amount of deficit in current balance shrunk, it will not turn into surplus for the time being. However the recent IIF report says that the current balance will be in the black due to revenue from oil in the same year. According to the report by Algerian Central Bank issued in December 1996, the export amount in hydrocarbon industry will reach to \$14.47 billion in the year 2000 from \$11.94 billion in 1996.

(e) Foreign reserves

Attributed to increase of revenue in foreign currency due to the oil price hike, the amount of foreign reserves reached \$3.5 billion in 1996 and was expected to reach \$4.5 billion at the end of 1996. As the result, midterm prospect would be "reasonably favorable" says The World Bank.

(f) Finance

Algeria has received \$1.8 billion from ESAF of I.M.F. in April 1995. Moreover, the World bank is planning to finance \$500 million in the next 2 years to Algeria for its support scheme. The country's relations with international financial institutions have been good since EU agreed to finance \$156 million in December 1996 in order to support Algerian economic reform and African Development bank signed for aid of Fr.1.8 billion to assist fostering small and medium-sized enterprises.

(3) External debt

The IMF reports that the country's payment of foreign debt will face its peak time for DSR(Debt Service Ratio) by 53% in 1998, 59% in 2001 and 52% in 2002 compared to 38 % in 1997.

The prospect of debt payment in Algeria is based on \$17/B crude oil price.

COUNTRY DATABASE: ALGERIA

94 95 96e 97f 98f 99f 0of 0lf

| | | | | | | | | |
|--|-------|-------|-------|-------|-------|-------|-------|-------|
| Real GDP % | -0.9 | 4.3 | 4.2 | 5.5 | 5.7 | 5.0 | 5.5 | 6.6 |
| Inflation % | 38.4 | 21.9 | 15.0 | 6.5 | 4.5 | 4.0 | 3.5 | 3.0 |
| Budget balance -4.4 %GDP | -1.4 | 0.3 | 0.3 | 1.2 | 1.5 | 1.5 | 1.5 | |
| Current account balance(\$ billion) | -1.8 | -2.3 | -2.2 | -2.3 | -1.8 | -1.3 | -1.1 | -1.1 |
| Trade balance (\$ billion) | -0.3 | 0.1 | 0.0 | -0.3 | 0.4 | 0.8 | 0.9 | 0.8 |
| Export (\$ billion) | 8.9 | 10.3 | 11.0 | 11.3 | 12.3 | 13.0 | 13.7 | 14.4 |
| Import (\$ billion) | 9.2 | 10.2 | 11.0 | 11.6 | 11.9 | 12.2 | 12.8 | 13.5 |
| Reserves excluding gold (\$ billion) | 2.6 | 2.1 | 2.7 | 3.2 | 3.4 | 3.6 | 3.8 | 4.0 |
| DSR % | 48.6 | 43.8 | 36.5 | 37.7 | 52.9 | 57.6 | 56.9 | 58.8 |
| ORR % | 331 | 309 | 303 | 311 | 291 | 278 | 261 | 249 |
| Oil price(\$/b) | 16.31 | 17.58 | 17.40 | 16.22 | 16.38 | 16.55 | 16.71 | 16.88 |

(Source: IMF)

TURKEY

1. Political Situation

(1) The coalition government of the Islamist Refah Party and the centre right True Path Party have been under pressure from the army that has the highest authority and plays the role of the guardian of secularism since this year. Finally, Prime Minister Necmettin Erbakan was forced to step down in June.

(2) A new secular coalition government, headed by Motherland leader Mesut Yilmaz, which is more acceptable to the military than the former Islamist / secular coalition was approved by Parliament in mid-July.

(3) The new government is backed by a disparate aggregation of center-right and left-of-center parties, who are united mainly by their opposition to the Islamist, and are unlikely to agree on structural reforms needed for a sustainable tightening of demand management.

(4) The parties supporting the new government are likely to push for early parliamentary elections in 1998, but it will not be easy for these parties to secure a majority after the election. Therefore, we expect that the political uncertainty will remain for the time being.

2. Economic Situation

(1) Having very unstable political situation as stated above, the prompt implementation of structural reform for social security, taxation and privatization can not be expected.

(2) On the other hand, in case if any corruptive action was undertaken under Yilmaz government to win the election, the financial deficit will fall into a more serious situation and

deterioration of macro economy can not be avoided. Unless the political stabilization as achieved and drastic structural reform were to be enforced, we can not deny that there is a possibility of economic crisis.

(3) Trend of macro economy

(a) Economic growth

The growth rate of GDP throughout 1996 had marked 7.2%. According to the macro economic target set by the government in 1997, to restrain the GDP growth rate up to 4%. However a possible early election will boost growth to over 5%.

(b) Inflation

Rising rate of consumer prices have been 80.4% throughout 1996. It is a little lower compared to 1995 but is still high. The annual inflationary rate is expected to be around 80 to 85%, even though it had dropped down to 76% at the end of June 1997. The main cause of high inflation is chronic deficit in government finances.

(c) Financial revenue and expenditure

The interest rate burden of nearly 40% and expenses for national corporations and social security fund which accounted for more than 20% of national expenditures, creating concern over rigidity of the national budget. The core of improvement of financial structure is to reform the social security system and taxation. Also, improvement of inefficient national corporations and encouraging of privatization are also the crucial issues. However we can not expect much progress in these structural reforms under the present fragile coalition government.

(d) Current account balance

Current balance in 1996 marked a deficit of \$4.4 billion as their import has increased, affected by implementation of customs union with the EU in January 1996 and large increase of trade deficit. The current account deficit has also increased to 4.0% of GDP from 1.3% of-GDP. The current deficit will further expand, and is expected to reach 4.4% of GDP in 1997.

(e) Repayment of debt

Foreign debt has gradually been increasing and will reach the level of 40% of GNP to \$78 billion. Also, annual debt service will be maintained for the time being between \$11 billion to \$13 billion and DSR is expected to move around 25%.

The level of short term debt has been increasing as well. This should be watched carefully.

COUNTRY DATABASE: TURKEY

| | 93 | 94 | 95 | 96e | 97f |
|--|-------|-------|-------|-------|-------|
| Real GDP % | 8.3 | -5.5 | 7.3 | 7.0 | 5.5 |
| Inflation % | 66.1 | 106.2 | 93.5 | 80.7 | 86.1 |
| Budget balance %GDP 6.7 | 3.9 | 4.1 | 8.8 | - | |
| Current account balance billion) - | 6.4 | 2.6 | -2.3 | -7.0 | -9.0 |
| Trade balance (\$ billion) | -14.2 | -4.2 | -13.2 | -19.7 | -23.3 |
| Export Billion (\$billion) | 15.6 | 18.4 | 22.0 | 23.4 | 26.5 |
| Import (\$ billion) | 29.8 | 22.6 | 35.2 | 43.1 | 49.8 |
| Reserves excluding gold (\$ billion) | 6.2 | 7.1 | 12.4 | 16.6 | 12.8 |
| Months of imports | 2.0 | 2.8 | 3.3 | 3.7 | 2.5 |
| Total external debt (\$ billion) | 67.3 | 65.6 | 73.3 | 76.5 | 80.8 |
| ORR % | 245 | 218 | 193 | 182 | 172 |
| Total debt service billion) | 7.9 | 10.0 | 11.9 | 11.1 | 12.7 |
| DSR % | 28.7 | 33.2 | 31.3 | 26.4 | 27.1 |

(Source: December 1996 IIF)

BRAZIL

1. Political and Economic Points

(1) With regard to the issue on presidential re-election, a bill to revise nation's constitution that specifies the procedure of re-election of President was approved, and no other candidate seems to be more hopeful, the incumbent President is almost certain to be re-elected at the next election in 1998. In the opinion Doll conducted in June, supporting ratio for President Cardoso marked 40% (if those who answered "average" were included, 81%), so that the move towards the constitutional revision concerning the administrative and financial reform can be predicted to be accelerated, supported by strong political backing.

(2) Division and privatization of communication industry (esp. portable telephone) will be implemented from April. Important stock sales in Rio Doce, (iron ore mining company) took effect on 6th May. In the future, the large scale issues including electric company etc. will be expected to be privatized, resulting in large amount of influx of foreign capital.

(3) Though hyper inflation in the past seems to have settled down (10% in 1996) the government still regards the restraint of inflation as their main policy, but will continue their monetary and foreign exchange policy with high interest rate and high currency exchange rate. Consumption restraining policy has been adopted to tackle the still increasing trade deficit (\$ 5.5billion in 1996) by regulating imported finance and imposing heavier tax on consumer credit. However, an immediate effect can not be expected, and deficit in 1997 may well reach to more or less \$12 billion. With the increased credibility of Brazil in international financial circles, she will be financed by foreign capital related to the above mentioned privatization program.

*Standard and Poors has already decided the up-rating of Brazil

from B+ to BB-) in April and the spread of Brady Bond has been shrinking by nearly 30% during the period from March 1996 to March 1997.

(4) Along with the trade deficit, financial deficit (3.5% against GDP)is also a pending issue for this country but it will take some time as it also requires the revision of the constitution by reducing social security expenditure and correcting excessive transfer of funds of national treasury to the local government. (Meanwhile, an administrative reform bill related to the issue of public officials passed the lower house on 9th of April.)

COUNTRY DATABASE: BRAZIL

| | 93 | 94 | 95 | 96e | 97f |
|--|-------|-------|-------|-------|-------|
| Real GDP % | 4.2 | 5.7 | 4.3 | 2.9 | 4.4 |
| Inflation % | 2540 | 1113 | 22 | 9.1 | 6.5 |
| Budget balance %GDP | -0.7 | 1.3 | -4.8 | -3.9 | - |
| Current account balance (\$ billion) | -0.4 | -1.7 | -18.0 | -24.3 | -29.3 |
| Trade balance (\$ billion) | 13.3 | 10.5 | -3.4 | -5.5 | -8.6 |
| Export (\$ billion) | 38.6 | 43.5 | 46.5 | 47.7 | 50.7 |
| Import (\$ billion) | 25.3 | 33.1 | 49.9 | 53.3 | 59.3 |
| Reserves excluding gold (\$ billion) | 30.6 | 34.6 | 33.5 | 33.2 | 33.2 |
| Months of imports | 8.0 | 8.2 | 7.7 | 8.2 | 7.2 |
| Direct investment (\$ billion) | 0.4 | 0.9 | 2.8 | 10.0 | 12.9 |
| Total external debt (\$ billion) | 168.1 | 173.8 | 184.8 | 195.5 | 204.8 |
| ORR % | 384 | 346 | 335 | 332 | 332 |
| Total debt service (\$billion) | 17.3 | 17.4 | 22.8 | 26.2 | 33.6 |
| DSR % | 30.6 | 34.6 | 41.3 | 44.5 | 54.6 |

(Source: March 1997 IIF)

APPENDIX II

BUSINESS RESULT OF EID/MIT

SEP.%1997
*96fy:estimate
(100Million Yen)

1. Business Result

| Fiscal Year | 89 | 90 | 91 | 92 | 93 | 94 | 95 | 96 |
|------------------|---------|---------|---------|---------|---------|---------|---------|---------|
| Insured Amount | 182.952 | 227.620 | 219.522 | 218.348 | 197.653 | 193.593 | 168.820 | 189.796 |
| Premium A | 342 | 448 | 357 | 447 | 462 | 441 | 435 | 410 |
| Recoveries B | 693 | 387 | 407 | 1.112 | 773 | 852 | 983 | 1.212 |
| Claims C | 1.427 | 1.986 | 3.419 | 1.482 | 1.280 | 806 | 571 | 444 |
| Others D | 14 | 11 | 9 | 12 | 13 | 21 | 18 | 22 |
| A+B-(C+D) | ♦ 406 | ♦ 1.162 | ♦ 2.664 | 65 | ♦ 58 | 466 | 829 | 1.156 |
| Interest E | 144 | 235 | 300 | 346 | 249 | 270 | 171 | 126 |
| Administration F | 23 | 35 | 44 | 45 | 45 | 46 | 44 | 46 |
| A+B-(C+D+E+F) | ♦ 573 | ♦ 1.432 | ♦ 3.008 | ♦ 326 | ♦ 352 | 149 | 614 | 984 |
| Total Debts | 2.941 | 3.698 | 6.378 | 6.886 | 6.744 | 6.224 | 5.360 | 4.041 |

2.Recoveries

(10Million Yen)

| Fiscal | 90 | 91 | 92 | 93 | 94 | 95 | 96 |
|---------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Total Recovery | 387 | 407 | 1,112 | 773 | 852 | 983 | 1,212 |
| Top 5 countries (%) | 173 (44.7) | 229 (56.3) | 879 (79.0) | 587 (75.7) | 550 (64.6) | 752 (76.5) | 942 (77.7) |

Major Recoveries

(100 Million Yen)

| | 90 | 91 | 92 | 93 | 94 | 95 | 96 |
|---|------------|------------|------------|------------|------------|------------|------------|
| 1 | Philip 86 | Philip 83 | Brazil 603 | Brazil 300 | Brazil 249 | Brazil 403 | Brazil 493 |
| 2 | Nigeria 63 | Argent 49 | Nigeria 10 | Philip 189 | Philip 207 | Philip 200 | Argent 234 |
| 3 | Iraq 58 | Nigeria 40 | Argent 79 | Argent 58 | Mexico 91 | Argent 114 | Philip 153 |
| 4 | Turkey 41 | Poland 30 | Philip 65 | Mexico 65 | Argent 65 | Egypt 46 | Mexico 70 |
| 5 | Egypt 15 | Brazil 27 | Egypt 52 | Egypt 39 | Egypt 44 | Mexico 26 | Russia 45 |

Payment of Claims

(100 Million Yen)

| Fiscal Year | 90 | 91 | 92 | 93 | 94 | 95 | 96 |
|-----------------|-------|-------|-------|-------|-----|-----|-----|
| | 1,986 | 3,419 | 1,482 | 1,280 | 806 | 571 | 444 |
| Non-rescheduled | 495 | 2,379 | 651 | 297 | 98 | 204 | 180 |
| Iraq | 291 | 1,446 | 595 | 250 | 62 | 29 | 24 |
| Other | 204 | 933 | 56 | 47 | 36 | 175 | 157 |
| rescheduled | 1,491 | 1,041 | 831 | 983 | 708 | 367 | 264 |
| Russia | - | - | 9 | 522 | 321 | 155 | 181 |
| Others | 1,491 | 1,041 | 821 | 461 | 387 | 212 | 82 |

Major Payment

(100 MilliOn Yen)

| | 90 | 91 | 92 | 93 | 94 | 95 | 96 |
|---|-------------|-------------|-------------|-------------|------------|-------------|-------------|
| 1 | Brazil 383 | Iraq 1446 | Iraq 595 | Russia 522 | Russia 321 | Argeria 183 | Russia 189 |
| 2 | Philip 296 | Iran 777 | Brazil 194 | Iraq 250 | Nigera 142 | Russia 157 | Nigeria 124 |
| 3 | Nigeria 292 | Brazil 246 | Nigeria 182 | Nigeria 155 | Argeria 93 | Nigeria 133 | Argeria 67 |
| 4 | Iraq 291 | Nigeria 179 | Egypt 122 | Egypt 77 | Iraq 62 | Iraq 29 | Iraq 24 |
| 5 | Mexico 179 | Egypt 137 | Philip 95 | Brazil 71 | Argent 48 | Egypt 20 | Syrian 17 |

I. BUSINESS RESULTS OF EID/MITI

1977

(billion yen)

| Fiscal Year | 1990 | 91 | 92 | 93 | 94 | 95 | 96 |
|-------------------|---------|---------|--------|--------|--------|--------|--------|
| Insured amount | 22,762 | 21,952 | 21,835 | 19,765 | 19,359 | 16,882 | 18,980 |
| Premium | 44.8 | 35.7 | 44.7 | 46.2 | 44.1 | 43.5 | 41.0 |
| Recoveries | 38.7 | 40.7 | 111.2 | 77.3 | 85.2 | 98.3 | 121.2 |
| Claims | 198.6 | 341.9 | 148.2 | 128.0 | 80.6 | 57.1 | 44.4 |
| Balance \approx | ¥ 142.1 | ¥ 299.9 | ¥ 31.4 | ¥ 33.9 | 17.1 | 63.2 | 100.6 |

\approx adjusted after paying interest and administration expenses

CHPARTER II

EXPORT-IMPORT BANK OF THE UNITED STATES

COUNTRY LIMITATION SCHEDULE

Special Conditions Pertaining to
EX-IM Bank Loan & Guarantee Programs
and Export Credit Insurance

EFFECTIVE March 21, 1997

It is agreed that pursuant to the provisions of Ex-Im Bank loans and guarantees and Ex-Im Bank export credit insurance policies, the country limitation schedule has been amended effective March 21, 1997. This revision supersedes the November 17, 1996 country limitation schedule and any amendments thereto.

Insureds, and brokers will be notified of any amendments to this country limitation schedule in writing. A full revision is generally completed every six months to on a year. All special conditions should be reviewed as many have been amended.

GENERAL CONDITIONS

Exceptions to any condition or limitation contained herein must be obtained in writing from Ex-Im Bank.

Ex-Im Bank reserves the right to set additional conditions for any particular buyer or issuing bank including the right to set a different percentage of coverage. Ex-Im Bank also reserves the right to reject any particular application.

The sector where the risk lies (public or private) and the country of the obligor, or guarantor if there is one, will generally be used for determining appropriate country limitations and exposure fee.

The following insurance policies are affected by this country limitation schedule. Please note that Short - Term Insurance Policies are governed by the columns titled "Up to one year":

Short - Term Insurance Policies: EBD, ELC, ENB, ENV, ESC, ESM (ST), ESS, ETM(S-T), FB, FB-E, FV, ESP, ESSP, FP, MCP(ST).

MEDIUM – TERM: All medium-term and lease-policy types, ESM, ETM, MCP, IVIRP, MSC, MSC-E, MTR, MTR-E.

Effective Date of

this Endorsement

March 21, 1996

No. C.LS-3/97

12:01 A.M. E.T.

EXPORT – IMPORT BANK OF THE U.S.
COUNTRY LIMITATION SCHEDULE
EFFECTIVE MARCH 21,1977

“X” INDICATES SUPPORT IS NOT AVAILABLE

| TOTAL TERM | PUBLIC SECTOR RISK | | | PRIVATE SECTOR RISK | | | NOTES |
|--------------------|--------------------|--------------|----------|---------------------|--------------|-----------|------------|
| | Up to 1 year | 1 to 7 years | >7 years | Up to year | 1 to 7 years | > 7 years | |
| Afghanistan | x | x | x | x | x | x | #7 |
| Albania | | x | x | x | x | x | #1, #3, #5 |
| Algeria | | | x | x | x | x | #1, #10 |
| Angola | x | x | x | x | x | x | |
| Anguilla | | | | | | | #1 |
| Antigua & Barbuda | x | x | x | | | | #1, #4 |
| Argentina | | | | | | | #6b |
| Armenia | x | x | x | x | x | x | |
| Aruba | | | | | | | #1, #9 |
| Australia | | | | | | | |
| Austria | | | | | | | |
| Azerbaijan | x | x | x | x | x | x | |
| Bahamas | | | | | | | |
| Bahrain | | | | | | | |
| Bangladesh | | | | x | x | x | #1 |
| Barbados | | | | | | | #1 |
| Belarus | x | x | x | x | x | x | |
| Belgium | | | | | | | |
| Belize | | | | | | | #6a |
| Benin | | | x | | | X | #1, #2, #3 |
| Bermuda | | | | | | | |
| Bhutan | | | | x | x | x | #1 |
| Bolivia | x | x | x | | | | #1 |
| Botswana | | | | | | | |
| Bosnia-Herzegovina | x | x | x | x | x | x | |
| Brazil | x | x | x | | | | |
| British Virgin Is. | | | | | | | |
| Brunei | | | | | | | |
| Bulgaria | | | x | x | x | x | #1, #3, #5 |
| Burkina Faso | x | x | x | x | x | x | |
| Burundi | x | x | x | x | x | x | |
| Cambodia | x | x | x | x | x | x | #7 |
| Cameroon | x | x | x | x | x | x | |
| Canada | | | | | | | |
| Cape Verde Is. | x | x | x | x | x | x | |

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EXPORT – IMPORT BANK OF THE U.S.
COUNTRY LIMITATION SCHEDULE
EFFECTIVE MARCH 21,1977

“X” INDICATES SUPPORT IS NOT AVAILABLE

| TOTAL TERM | PUBLIC SECTOR RISK | | | PRIVATE SECTOR RISK | | | NOTES |
|----------------------|--------------------|--------------|----------|---------------------|--------------|-----------|------------|
| | Up to 1 year | 1 to 7 years | >7 years | Up to year | 1 to 7 years | > 7 years | |
| Cayman Is. | | | | | | | |
| Central African Rep. | x | x | x | x | x | x | |
| Chad | x | x | x | x | x | x | |
| Chile | | | | | | | |
| China, People’s Rep | | | | x | x | x | #2 |
| Colombia | x | x | x | x | x | | #7 |
| Comoro | x | x | x | x | x | x | |
| Congo | x | x | x | x | x | x | |
| Cook Island | | | | | | x | #1, #4 |
| Costa Rica | | | x | | | | #6b |
| Cote d’Ivoire | x | x | x | | | x | #1, #4 |
| Croatia | | | | x | x | x | #1, #3, #5 |
| Cuba | x | x | x | x | x | x | #7 |
| Cyprus | | | | | | | |
| Czech Republic | | | | | | | #1 |
| Denmark | | | | | | | |
| Djibouti | x | x | x | x | x | x | |
| Dominica | | | | | | | #1 |
| Dominican Rep. | | | | | | | #6a |
| Ecuador | | | X | | | | #6a |
| Egypt | | | | | | | #1 |
| El Salvador | | | | | | | |
| Equatorial Guinea | x | x | x | x | x | x | |
| Eritrea | x | x | x | x | x | x | #1#3 #4 #5 |
| Ethiopia | x | x | x | x | x | x | |
| Fiji | | | | | | | #1 |
| Finland | | | | | | | |
| France | | | | | | | |
| Gabon | x | x | x | | | | #6a |
| Gambia | x | x | x | x | x | x | |
| Georgia | x | x | x | x | x | x | |
| Germany | | | | | | | |
| Ghana | | | | | | | #5, #6a |
| Greece | | | | | | | |

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| TOTAL TERM | PUBLIC SECTOR RISK | | | PRIVATE SECTOR RISK | | | NOTES |
|---------------|--------------------|--------------|----------|---------------------|--------------|-----------|-------------|
| | Up to 1 year | 1 to 7 years | >7 years | Up to year | 1 to 7 years | > 7 years | |
| Grenada | | | | | | | #1 |
| Guatemala | | | | | | | #6b |
| Guinea | x | x | x | x | x | x | |
| Guinea-Bissau | x | x | x | x | x | x | |
| Guyana | x | x | x | | | x | #1 |
| Haiti | x | x | x | x | x | x | |
| Honduras | x | x | x | | | x | #1 #4 |
| Hon Kong | | | | | | | |
| Hungary | | | | | | | #1 #4 |
| Iceland | | | | | | | |
| India | | | | | | | |
| Indonesia | | | | | | | |
| Iran | x | x | x | x | x | x | #7 |
| Iraq | x | x | x | x | x | x | #7 |
| Ireland | | | | | | | |
| Israel | | | | | | | |
| Italy | | | | | | | |
| Jamaica | | | | | | | #6a |
| Japan | | | | | | | |
| Jordan | | | | | | | #1 #4 |
| Kazaksatan | | | | x | x | x | #1 #3 #5 |
| Kenya | | | x | | | x | #1 #5 |
| Kiribati | | | | | | | #1 |
| Korea, North | x | x | x | x | x | x | #7 |
| Korea, South | | | | | | | |
| Kuwait | | | | | | | |
| Kyrgyzstan | x | x | x | x | x | x | |
| Laos | x | x | x | x | x | x | #7 |
| Latvia | | | | | | | #1 #3 #4 #5 |
| Lebanon | | | x | | | | #1 #4 #5 |
| Lesotho | | | | | | | #6b |
| Liberia | x | x | x | x | x | x | |
| Libya | x | x | x | x | x | x | #7 |
| Liechtenstein | | | | | | | |
| Lithuania | | | | | | | #1 #3 #4 #5 |

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|------------------|--------------------|--------------|----------|---------------------|--------------|-----------|----------|
| | Up to 1 year | 1 to 7 years | >7 years | Up to year | 1 to 7 years | > 7 years | |
| Luxembourg | | | | | | | |
| Macao | | | | | | | #1 |
| Macedonian | x | x | x | x | x | x | |
| Madagascar | x | x | x | x | x | x | |
| Malawi | x | x | x | x | x | x | |
| Malaysia | | | | | | | |
| Maldives Islands | | | | | | | #1 |
| Mali | x | x | x | x | x | x | |
| Malta | | | | | | | |
| Marshall Islands | x | x | x | x | x | x | |
| Mauritania | x | x | x | x | x | x | |
| Mauritius | | | | | | | |
| Mexico | | | | | | | |
| Micronesia | | | | | | | #1 |
| Moldova | | | x | x | x | x | #1 #3 #5 |
| Monaco | | | | | | | |
| Mongolia | x | x | x | x | x | x | |
| Montserrat | | | | | | | 31 |
| Morocco | | | | | | | #6b |
| Mozambique | x | x | x | x | x | x | |
| Myanmar | x | x | x | x | x | x | #7 |
| Namibia | | | | | | | #1 |
| Naura | x | x | x | x | x | x | |
| Nepal | | | x | x | x | x | #1 |
| Netherlands | | | | | | | |
| Neth Antilles | | | | | | | |
| New Zealand | | | | | | | |
| Nicaragua | x | x | x | | | x | #1 |
| Niger | x | x | x | x | x | x | |
| Nigeria | x | x | x | x | x | x | #7 |
| Norway | | | | | | | |
| Oman | | | | | | | |
| Pakistan | x | x | x | x | x | x | |
| Palau | | | x | x | x | x | #1 #5 |
| Panama | | | | | | | #6b |

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| TOTAL TERM | PUBLIC SECTOR RISK | | | PRIVATE SECTOR RISK | | | NOTES |
|---------------------|--------------------|--------------|----------|---------------------|--------------|-----------|-------------|
| | Up to 1 year | 1 to 7 years | >7 years | Up to year | 1 to 7 years | > 7 years | |
| Papua New Guinea | | | | | | x | #1 |
| Paraguay | | | | | | | #6a |
| Peru | | | | | | | 31 |
| Philippines | | | | | | | |
| Poland | | | | | | | #1 |
| Portugal | | | | | | | |
| Qatar | | | | | | | |
| Romania | | | | | | x | #1 #3 #4 #5 |
| Russia | | | | | | x | #1 #3 #4 #5 |
| Rwanda | x | x | x | x | x | x | |
| St. Kitts-Nevis | | | | | | | #1 |
| St. Lucia | | | | | | | #1 |
| St. Vincent-Gren | | | | | | | #1 |
| Sao Tome & Principe | x | x | x | x | x | x | |
| Saudi Arabia | | | | | | | |
| Senegal | x | x | x | x | x | x | |
| Serbia/Montenegro | x | x | x | x | x | x | #11 |
| Seychelles | | | | | | | #6b |
| Sierra Leone | x | x | x | x | x | x | |
| Singapore | | | | | | | |
| Slovak Republic | | | | | | | #1 #3 #4 #5 |
| Slovenian | | | | | | | #1 |
| Solomon Islands | | | | | | | #1 |
| Somalia | x | x | x | x | x | x | |
| South Africa | | | | | | | |
| Spain | | | | | | | |
| Sri Lanka | | | | | | | #1 |
| Sudan | x | x | x | x | x | x | 37 |
| Suriname | x | x | x | x | x | x | |
| Swaziland | | | | | | | |
| Sweden | | | | | | | |
| Switzerland | | | | | | | |
| Syria | x | x | x | x | x | x | #7 |
| Taiwan | | | | | | | |
| Tajikistan | x | x | x | x | x | x | |

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| TOTAL TERM | PUBLIC SECTOR RISK | | | PRIVATE SECTOR RISK | | | NOTES |
|----------------------|--------------------|--------------|----------|---------------------|--------------|-----------|----------|
| | Up to 1 year | 1 to 7 years | >7 years | Up to year | 1 to 7 years | > 7 years | |
| Tanzania | x | x | x | x | x | x | |
| Thailand | | | | | | | |
| Togo | x | x | x | x | x | x | |
| Tonga | | | | | | | #1 |
| Trinidad & Tobago | | | | | | | #6a |
| Tunisia | | | | | | | |
| Turkey | | | | | | | |
| Turkmenistan | | | x | x | x | x | #1 #3 #5 |
| Turks & Caicos. Is. | | | | | | | #1 |
| Uganda | | | x | | | x | #1 #4 #5 |
| Ukraine | | | x | x | x | x | #1 #3 #5 |
| United Arab Emirates | | | | | | | #8 |
| United Kingdom | | | | | | | |
| Uruguay | | | | | | | #6b |
| Uzbekistan | | | | x | x | x | #1 #3 #5 |
| Vanuatu | | | | | | | #1 |
| Vatican City | | | | | | | |
| Venezuela | | | | | | x | #6a |
| Vietnam | x | x | x | x | x | x | #7 |
| Western Samoa | | | | | | | #1 |
| Yemen | x | x | x | x | x | x | |
| Zaire | x | x | x | x | x | x | |
| Zambia | x | x | x | x | x | x | |
| Zimbabwe | | | | | | | #6b |

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Notes:

#1 Discretionary Credit Limits under Short -Term Insurance Policies are withdrawn. Cover not available unless specified in a Special Buyer Credit Limit, Issuing Bank Credit Limit endorsement, or Country Limits of Liability endorsement.

#2 For public sector transactions: Currently, arrangements are in place with the Bank- of China and the State Development Bank to serve as obligor or guarantor for medium and long-term transactions under the Loan and Guarantee Programs. Use of Discretionary Credit Limits and Country Limits of Liability under Insurance policies requires the obligation of one of the following: the Bank of China, the State Development Bank, the China Construction Bank, the Industrial and Commercial Bank of China, or the Bank of Communications. For the Medium -term Insurance Policies, Loan or Guarantee Programs, Ex-Im Bank will consider transactions with other financial institutions or other entities that are able to provide detailed financial information sufficient to enable Ex-Im Bank to reach a credit conclusion.

#3 Prior to accepting an application for a preliminary or final commitment for a public sector transaction, or for any insurance for a public sector transaction, Ex-Im Bank will require an indication of host government support for the application. Contact Ex-Im Bank for more detailed information on specific markets.

#4 Ex-Im Bank cover/support for short and medium-term private sector transactions is limited to transactions with a commercial bank as obligor or guarantor unless otherwise specified by Ex-Im Bank.

#5 Ex-Im Bank cover/ support for public sector transactions is limited to transactions which commit the full faith and credit of the government unless otherwise specified by Ex-Im Bank.

#6 Under Short-Term Insurance Policies, coverage under Discretionary Credit Limits and Country Limits of Liability shall be the lesser of the limits authorized in the policy or:

- a. \$50,000
- b. \$100,000

Higher limits will be considered upon application for a Special Buyer Credit Limit, Issuing Bank Credit Limit, or Country, Limits of Liability.

#7 Support is legally prohibited.

#8 Public sector transactions in Shajah, Fujairah, Ras Al-Khaimah, Umm Al-Qaywayn, and Ajman require the guarantee of the federal government of the United Arab Emirates.

#9 Public sector transactions with total term in excess of one (1) year require the government of Aruba as the borrower.

#10 Support extends only to transactions with Sonatrach with the full faith and credit guarantee of the government.

#11 Support on behalf of the government of Serbia or the government of Montenegro is legally prohibited.

INFORMATION SUPPLEMENT ON MMDILTM- AND LONG-TERM PROGRAMS

'Open for Cover' versus 'Off-Cover' ' The attached Country Limitation Schedule indicates where Ex-Im Bank is "open for cover" and where Ex-Im Bank is "off-cover". The Schedule is organized along three dimensions: the country where the risk lies, sector (public sector or private sector), and term of total exposure (including both disbursement period and repayment term). Ex-Im Bank defines "public sector" as including those obligors or guarantors which are at least 50% owned, directly or indirectly, by the government. Where the CLS presents an X mark, Ex-Im Bank is 'off-cover", and is therefore not willing to consider approval of routine transactions. These "off-cover" determinations are due to economic and/or political risks associated with the country.

Where Ex-Im Bank is Open for Cover. The "open for cover" designation refers to the possibility, rather than the certainty, of Ex-Im Bank support in particular cases. Proposed obligors, guarantors, and transaction structures under medium- and long-term programs are all subject to case-by-case

Bank approval. Approval depends on the case-by-case application of Bank policies, particularly the Bank's determination of reasonable assurance of repayment. The following paragraphs provide very general guidance to the application of policies in markets where Ex-Im Bank is on-cover.

- **Identification of Obligor or Guarantor** Ex-Im Bank will approve a final commitment, a preliminary commitment (PC), or a medium-term insurance policy or commitment (MTIP or MTIC), only if a specific obligor or guarantor has been identified. Ex-Im Bank may approve an indicative letter of interest (LI) for a proposed transaction, subject to the condition that an obligor or guarantor is identified at the time the LI is converted to a final commitment, PC, MTIP, or MTIC; and Ex-Im Bank can accept the credit risk of the proposed obligor or guarantor.
- **Information Requirements regarding Obligors or Guarantor** Ex-Im Bank requires that obligors or guarantors offer "reasonable assurance of repayment." To process applications for final commitments, PCs, MTIPS, and MTICS, Ex-Im Bank will first require Information on proposed obligors and guarantors. Such information includes financial statements and credit references. Engineering data is required for long-term transactions. Generally, Ex-Im Bank will require more detailed information regarding obligors or guarantors when processing relatively large transactions or transactions with obligors or guarantors with which Ex-Im Bank has had no favorable direct credit experience. Ex-Im Bank's application form and program literature specify the Bank's standard information requirements.
- **Sovereign Guarantees for Public Sector Buyers or Obligors** For cases involving proposed public sector buyers or obligors which do not have significant independent sources of revenue outside the central government budget and which do not have independently audited financial statements, Ex-Im Bank will routinely require a sovereign guarantee.
- **Prior Evidence of Host Government Willingness to Provide Sovereign Guarantee in Some Countries** In some countries, Ex-Im Bank requires applications for a final commitment for a medium

or long-term loan or guarantee, or for medium-term insurance, to be accompanied by prior evidence of the host government's willingness to provide a sovereign guarantee.

- **Temporary Suspension of Cover** In countries where the CLS indicates that Ex-Im Bank is "open for cover", Ex-Im Bank may, under certain circumstances, temporarily suspend cover. This is most likely to be the case for public sector obligors and guarantors only, but may involve all obligors and guarantors. In such an event, Ex-Im Bank will advise applicants as quickly as possible.

- **Large Transactions in Smaller Markets** Relatively large transactions in smaller economies, even when sovereign guaranteed, will be subject to special Ex-Im Bank review. Ex-Im Bank will review the potential macro economic impacts of the transaction, in terms of higher debt burden and debt repayment capacity.

- **Private Companies** Ex-Im Bank will accept the direct credit risks of private buyers, If available information suggests that these buyers offer a "reasonable assurance of repayment." For closely - held companies, Ex-Im Bank may require financial information from owners. For holding companies, Ex-Im Bank may require financial information on operating components, and may require their counter-guarantee.

- **Commercial Bank Guarantees** Ex-Im Bank may require the guarantees of acceptable commercial banks in the event that information available to Ex-Im Bank on proposed private buyers suggests that these buyers by themselves do not offer a "reasonable assurance of repayment.'

- **Limited Recourse Projects** Ex-Im Bank will consider limited-recourse project finance structures (those without full recourse to an acceptable, established obligor or guarantor), but only after a comprehensive review of project features. These features shall 'include the financial commitment of the project's equity shareholders over the life of the proposed Ex-Im Bank commitment; the experience and capacity of project participants, including suppliers and offtakers; project cash flow

coverage of foreign currency debt service; and security structures, including hard currency external payments arrangements. Ex-Im Bank will review only well- developed proposals, and will require project sponsors to fund review of project proposals by consultants retained by the Bank. Significant changes to proposed structures may be required.

- **Political-Only Cover** Ex-Im Bank's standard guarantee and insurance cover is "comprehensive", under which Ex-Im Bank will pay claims resulting from both commercial and political perils. For private borrowers, Ex-Im Bank also offers a narrower form of coverage, under "political-only" cover. Ex-Im Bank's guarantee agreements and insurance policies describe in detail and or define the specific risks, which are subject to this form of coverage.

The following is intended as a summary: For long-term transactions, Ex-Im Bank covers default arising from four "core" perils: transfer risk, expropriation, U.S. export license risk and political violence. Transfer risk involves borrowers inability to acquire foreign exchange through legal foreign exchange markets. Expropriation involves the government's confiscation of assets or ownership, or arbitrary or discriminatory intervention in business operations. U.S. export license risk involves the cancellation or non-renewal of a U.S. export license or imposition of certain restrictions on such license after shipment. Political violence involves war, revolution, insurrection, and other such acts. Under medium-term insurance policies, Ex-Im Bank also covers defaults arising from other defined risks.

Suppliers and/or lenders choosing political-only cover must be prepared to assume broad commercial risks associated with the borrower's capacity. Ex-Im Bank's political-only cover does not cover defaults arising from the borrower's capacity to withstand domestic or international commercial market disruptions, or currency devaluation or depreciation. If suppliers and/or lenders are unable to assume these and other commercial risks, then Ex-Im Bank comprehensive cover would be a more appropriate form of coverage.

Political-only cover is offered only for private buyers or borrowers, those which are not subject to the administration of government authorities, and for which it is possible to distinguish between commercial perils and political-risk perils. Political-only cover is not available for guaranteed lenders that are

majority-owned or controlled by the host country government. Political-only cover is the only form of coverage available from Ex-Im Bank for borrowers, which are effectively controlled by suppliers and/or lenders participating in transactions. Political-only cover is available only for countries where EX-IM Bank is "open for cover" for private sector risk.

Where EX-IM Bank is Off Cover for Country Credit Reasons Ex-Im Bank will not consider routine transactions in countries and sectors (public or private) where the country limitation schedule shows that the Bank is off-cover (where there is an X). However, four special categories of transactions may be eligible for Ex-Im Bank support, under restrictive conditions, subject to additional special review:

- **Borrowers on International Capital Markets** Individual borrowers (either public sector or private sector) with a strong, record of independent access or those borrowers which in Ex-Im Bank's opinion could have access to private international capital markets or other international sources of funds, absent external (including, sovereign) guarantees. The fee grade assigned, and the extent of Ex -Im Bank support, will take into account information related to the borrower's financing and ratings. For Ex-Im Bank to consider such borrowers, information on the borrower's international borrowings for at least the last six months must accompany the application. For each traded debt security, the required information includes the maturity and coupon, credit ratings (if any), and recent yield data. For syndicated loans, the required information includes interest rates, arranging fees, maturity profile, amounts borrowed, and names of arranging and key participating banks.
- **Insulated Project Finance Structures** Ex-Im Bank's approval in "off-cover" markets/sectors of limited-recourse structures depends on the establishment of structures which do not require the financial or operating commitments of host government agencies and which are effectively insulated from government involvement. Furthermore, these structures must involve the channeling of project foreign exchange earnings through offshore payments and escrow mechanisms. In some country environments, the only acceptable limited-recourse structures may be "enclave" projects which are almost completely insulated from the broader country

environment. The fee grade assigned, and the extent of Ex-Im Bank support, will take into account project structure and other conditions.

- **Secured Long- Range Aircraft Leases.** Ex-Im Bank approval of asset-secured long-range aircraft lease transactions requires that the airline's country of registry become a signatory to international conventions protecting aircraft property rights. Ex-Im Bank approval for aircraft transactions is more likely for privately- owned airlines with established operating records. Depending on the nature of transaction participants and structures, Ex-Im Bank may also require offshore payments and escrow mechanisms, or may provide a reduced percentage of cover. Aircraft transactions are subject to special fees and covenants.
- **Acceptable Borrower Outside the Country** Support may be available if an acceptable financial institution (e.g., commercial or multinational bank) outside of the country acts as the obligor.

Because these transactions are subject to individual special review, Ex-Im Bank will not approve letters of interest (LIs) for them. It should be noted that these exceptions do not apply in countries where Ex-Im Bank is legally prohibited from operating.

SECTION 8

EVALUATION AND CONTROL OF BUYER RISKS **AND RISKS ON BANKS**

CHAPTER I EVALUATION AND CONTROL OF BUYER RISKS

CHAPTER II SYNOPSIS

**CHAPTER III ANALYSIS OF BALANCE SHEET, PROFIT AND
LOSS ACCOUNT AND CASH FLOW FORECAST
(THE SIGNIFICANT RATIOS)**

**CHAPTER IV EVALUATION AND CONTROL OF RISKS ON
BANKS**

CHAPTER V CAPITAL AND RESOURCES COMPUTATION

CHAPTER I

EVALUATION AND CONTROL OF BUYER RISK

Introduction

Although the process of policy underwriting results in the issue of a contract of insurance providing the policyholders with an overall maximum liability, the policyholder does not begin to be protected and the insurer is not effectively on risk until a valid credit limit is issued.

Buyer underwriting is a process which involves:

- (a) an assessment of the integrity and credit worthiness of overseas buyers, including the marketability of their imports and their own marketing ability, and the risks involved in covering the exports to them.
- (b) a determination of the basic terms and limits within which the policyholder may prudently export to the buyer.

Characteristics of Credit Limit

A credit limit is the maximum amount of loss the insurer may be liable for in respect of each buyer. It is generally revolving, applicable for a credit period not more than 180 days. It can be varied or cancelled at any time based on the strength of information on the buyer and the policyholder and can be restricted by imposing additional conditions. The approved payment term applies automatically to less risky terms.

Underwriting Criteria

In determining a credit limit, the following underwriting criteria should be considered:

- (a) the country and the product
- (b) financial strength of the buyer
- (c) qualitative assessment of the buyer
- (d) policyholder's performance
- (e) underwriting experience

Additional Criteria on Public Sector Buyer

- a) Status in Government Structure (Dept./Public Company/Statutory Body)
- b) Source of Paying Funds (Central Treasury, State Authority, Autonomous etc.)
- c) Is Solvency Action Possible?
- d) Is Recovery of Debt a Practical Proposition?

a) The Country and the Product

The assessment of country involves a detailed study of a country's political system, stability of its government, and its relations with other countries. It is equally important to look at a country's GDP growth, inflation, economic management, balance of payments and its international reserves.

Country risks are distinct from buyer risks, but a country's economic condition has implications on an individual firm's performances. Very often, the number of business failures starts to increase when the economy begins its downturn.

The examination of products in buyer underwriting is concerned with how well the product might sell in the buyer's market. This involves a judgment of the likely obsolescence of the product, the buyer's experience to sell the products, the marketability of the product, and the implication of the brand name and pricing of the product, etc.

b) Financial Strength of the Buyer

A buyer is creditworthy if he has the ability and the willingness to buy, sell and pay in accordance with the agreed payment terms.

In assessing a buyer's ability to pay, the underwriter should try to analyse the buyer's financial condition, his sales and profitability over a period of time, his cashflow and his ability to service debt.

c) Qualitative Assessment of the Buyer

There are quite a number of cases where the buyer is capable of paying the policyholders but comes up with various excuses to avoid payment. The integrity and willingness of the buyer to pay is as important as his paying ability.

In assessing a buyer's willingness to pay the underwriter should look at the buyer's background and his management, the company's payment record and reputation, and the consolidated performance of the whole group.

(d) Policyholder's Performance

Due consideration should be given to the performance of the policyholder under the policy and his need for the full extent of the credit limit. If the policyholder has already proved to be something of a problem, an austere view would be justified. If the policyholder has effective credit control, satisfactory policy performance and good trading experience, favourable consideration can be given.

(e) Underwriting Experience

The aggregate credit commitments and payment experience in respect of the buyer and the buyer's group should be taken into account. The extent to which other credit limits have been used should be examined, and those under-utilized should be clawed back.

Determination of Credit Limit Amount and Terms

The determination of the size of a credit limit requires a decision that the buyer is creditworthy for a certain overall amount after consideration of the criteria mentioned. For shipments made by air or shipments seeking DP terms with a long credit period, open account terms should be offered.

(a) The Appropriate Name and Address of the Buyer

Attention should be paid to the name and address of the buyer as applied and whether it is different from that reported by the credit agency. Different names of a buyer represent different legal entities. An approved CL on a buyer does not apply to the other group members of the buyer.

b) Specific Conditions

When justified, a credit limit condition can be imposed to restrict the use of such limit, e.g. a condition specifying an expiry date, a condition specifying that the credit limit may be used for a specific transaction or group of transactions. However, conditions should only be imposed sparingly.

Discretionary Credit Limit and Automatic Credit Limit Approval

A discretionary limit is a small limit on each buyer extended to a policyholder automatically for cases where the policyholder has not submitted an application. However, the policyholder must obtain a bank or credit agency report on the buyer beforehand and such a report should not indicate any adverse information with respect to the creditworthiness of the buyer.

To improve the response time for small credit limit applications, it is worthwhile to consider approving small credit limits automatically through the computer before obtaining the usual bank or credit agency reports.

Certain exclusions have to be set and the size of the amount should be set at a level to contain the likely occurrence of small claims to an acceptable amount.

Buyer Underwriting Philosophy

All-in-all, buyer underwriting is an operation which combines the disciplines of a science and the subjectivity of an art. To enhance customer satisfaction, it is important to adopt a more pro-active and aggressive approach in handling credit limit applications without losing the quality of underwriting at the same time.

CHAPTER II - SYNOPSIS

CONTENTS

1. General Principle of Buyer Risk Management
2. Credit Management Skills & Methods
3. Buyer Risk Monitoring System
4. Buyers' Rating
5. Application Procedures

1) General Principle of Buyer Risk Management

What is Buyer Risk Management?

- Assessment of buyer ability to pay
- Determination of credit limit
- Monitor buyer performance over time

Purpose of Buyer Risk Management

From exporter eyes:

- Reduce non-payment risk
- Secure cashflow
- Ensure steady profit

From Insurer eyes:

- To accept a reasonable spread of risk
- To contain the amount of claims
- To spot out and monitor risk

What Affects Buyer Ability to Pay?

a) Business Risk

- Economic Conditions
- Competition
- Lack of Credit Facility
- Government Restrictions

b) Financial Risk

- Impact of Rising Interest Rates
- Lack of Liquidity
- Financial Management Skills
- Exchange Rate Fluctuation
- Credit Management Skills

c) Management Risk

- Quality, Experience & Background of Management & Owner

d) Country Risk

- Government Financial Strength / Foreign Currency Reserves
- Government Regulations
- Internal & External Conflict

Role of Credit Insurer

- Insurance to Protect Unavoidable Risk
- Credit Management & Risk Monitoring
- Recovery Advice to Minimize Loss

Underwriting Philosophy

- Pro-active and Aggressive without losing Quality of Underwriting

2) Credit Management Skills and Methods

Problems Facing the Underwriter

- Pressure of Events
- Scarcity of Time
- Insufficient or lack of information

Risk Assessment

Buyer Risks:

- Insolvency & bankruptcy
- Default in payment
- Repudiation

Underwriting Criteria

- a) Product
- b) Buyer Financial Strength
- c) Qualitative Assessment of buyer
- d) Policyholder performance
- e) Underwriting experience

a) Assessment of Products

- Product Life Cycle
- Buyer experience to sell
- Marketability
- Pricing

b) Buyer Financial Strength

- Sales
- Profitability
- Cashflow
- Networth

- Liabilities & Debts
- c) Qualitative Assessment of Buyer
 - Legal status, history
 - Management background
 - Payment record
 - Reputation
 - Performance of the group
- d) Policyholder Performance
 - Genuine need for CL
 - Credit Control
 - Trading Experience
 - Problem PH
- e) Underwriting Experience
 - Aggregate credit commitments
 - Payment experience of the buyer and its group
 - Utilisation of other credit limits

Determination of CL

- Amount
- Terms

Credit Limit (CL)

- Maximum amount of loss covered on a buyer'
- Revolving
- Can be adjusted / cancelled

Be Alert!

- Name & Address of the Buyer Applied
- Air-freight DP Shipments with Long Usance

Specific Condition

- Restrict the use of CL
- Sparingly use
 - Eg. - extending waiting period for claims
 - Imposing an expiry date

3) Buyer Risk Monitoring System

Buyer Risk Monitoring System

- a) Regular review
- b) Credit review committee
- c) Risk management
- d) Buyer under close supervision
- e) Ad hoc review

a) **Regular Review**

Review Frequency?

Review procedures:

- Update information on buyer
- Evaluate
- Check payment position

b) **Credit Review Committee**

- Review from senior management
- Bi-monthly regular review
- Buyer with large commitment

c) **Risk Management**

- Change of payment terms request
- Extension of due dates request
- Payment overdue reported
- Adverse information received

d) Buyer Under Close Supervision

Identify symptoms of trouble:

- Slow or unsystematic payment
- Late in producing financial statements
- Deteriorating operating results
- Other adverse information

4) Ad hoc Review

- Material events: (both adverse & good)
- Market feedback
- Country review

4). Buyers' Rating

Types of Buyer Rating

- Indicative score
- Predictive score

Advantages of Buyer Rating

- Objective
- Efficient
- Consistent

Limitations of Buyer Rating

- Time & Resources required
- May not be cost-effective for small volume of applications and non-repetitive applications

Applications of Buyer Rating

- Credit management
- Risk monitoring
- Automation

5) Application Procedures

Application Procedure

Credit limit application ⇒ report acquisition ⇒ credit assessment ⇒ credit limit issue

Important Information in a CLA

- Name & address of the buyer
- Amount & payment terms applied
- Trading experience
- Any overdue payment
- Orders in hand

CHAPTER III

ANALYSIS OF BALANCE SHEET, PROFIT AND LOSS ACCOUNT AND CASH FLOW FORECAST (THE SIGNIFICANT RATIOS).

(a) General Introduction

In many cases, especially for small buyers and private companies, the underwriter will not be able to obtain balance sheet information and where it is available certain limitations must be recognised.

- (i) The balance sheet and P/L account represent a picture taken at a particular point in time - inevitably at some time in the past and often more than one year ago.
- (ii) Legal requirements and accounting practices vary enormously from country to country and this must be taken into account when evaluating and drawing conclusion from the figures.
- (iii) It is by no means unknown for accounts to be 'doctored' to present a false picture. This is usually very difficult to detect for an ECA faced with a set of figures prepared in a foreign country.

(b) **The Main Components of a Balance Sheet**

A B Company Limited

Shareholders' Funds

Share Capital
Capital Reserve
General Reserve
P & L Appn Account

Fixed Assets

Land and Buildings
Plant and Machinery
Vehicles

Term Liabilities

Mortgage

Current Liabilities

Creditors - Trade etc
Bank Overdraft

Current Assets

Cash in Bank
Inventories
Receivables
Marketable Investments

(c) **The Ratio Analysis Process**

Ratios reduce the amount of data to workable form.

There are three stages:

- (i) calculation of a number of ratios
- (ii) comparison with an appropriate standard to ascertain whether they are satisfactory or otherwise
- (iii) interpretation of the results obtained.

The absolute ratios resulting from the calculation provide little information. They need to be rated as favourable or unfavourable and hence they need to be measured against chosen yardsticks. Analysts use various comparisons including:

- **intra-industry** i.e. comparing the particular company with other companies in the same industry.

- **inter-industry** i.e. comparing the particular company with other companies in different industries.
- **intra-company** i.e. comparing the particular company's ratios across time to identify trends or other relationships.
- **arbitrary standards** i.e. comparing the particular company's ratios to 'traditional' standards which are arbitrary rules of thumb. The application of these standards requires caution.

The simple example below illustrates the use of financial ratios in comparing two companies. Companies A and B are competitors in the same area of business and report profit as follows:

Company A: \$360,000

Company B: \$560,000

How well did these two companies perform in relation to one another?

On first glance it may appear that Company B performed better than Company A, as its reported operating profit was higher.

The following additional information on sales and shareholders' equity was obtained from the financial statements:

| | Company A | Company B |
|---------------------|-----------|-----------|
| Sales | 4,000,000 | 8,000,000 |
| Shareholders equity | 3,600,000 | 7,200,000 |

If we now compare the operating profit as a percentage of sales and shareholders' equity, we obtain the following information:

| | Company A | Company B |
|---|-----------|-----------|
| Operating profit as % of sales | 9.0% | 7.0% |
| Operating profit as % of shareholders' equity: | 10.0% | 7.8% |

These comparisons show that Company A earned 9 cents profit for every dollar of sales, while Company B earned only 7 cents. In addition, Company A earned 10 cents for each dollar invested, Company B earned 7.8 cents.

The Current Ratio

The current ratio measures the relationship between current assets and current liabilities and is widely used to test the short-term liquidity of a company. It measures the strength or weakness of the working capital position and is a measure of the company's ability to meet its short-term liabilities. It indicates the company's ability to satisfy current debt from current assets. The implication being that a high ratio of current assets to current liabilities represents a high degree of assurance that current liabilities will be paid out of current assets.

The calculation of the current ratio is current asset divided by current liabilities.

$$\begin{aligned}
 \text{Current Ratio} &= \frac{\text{Current assets}}{\text{Current liabilities}} \\
 &= \frac{98,754}{57,923} = 1.70 \text{ times}
 \end{aligned}$$

The rule of thumb commonly employed with the ratio is 2 to 1. However this does not mean that a ratio of 1.9 to 1 is unsatisfactory while a ratio of 2.1 to 1 is satisfactory. A ratio around 1.5 to 1 is generally the lowest acceptable.

Many companies operate most successfully over lengthy periods of time with low current ratios, ie in the vicinity of 1 to 1. The nature of the business might require only nominal investments in current assets. For example a retailer selling for cash can operate on a lower current ratio than a retailer selling on credit because of the time lag between making the sale

and collecting the cash. A low current ratio might also reflect excellent cash (ie current asset) management.

The Acid Ratio (or Quick Ratio)

A more stringent liquidity test is the acid test ratio. This again compares current assets to current liabilities but includes only those assets which may be expected to contribute to cash becoming available anthen in the next month or two to help meet the liabilities due for payment.

Acid Test Ratio

$$\begin{aligned} &= \frac{\text{Current assets - inventory}}{\text{Current liabilities - overdraft}} \\ &= \frac{98,754 - 60,161}{57,923 - 1,286} = \frac{38,593}{56,637} = 0.68 \text{ times} \end{aligned}$$

It is suggested that the acid ratio should be 1 to 1 or higher, but this is difficult to substantiate. If inventory is easily realisable and the trading conditions are buoyant, then it is possible to operate with an acid ratio lower than 1 to 1, say 0.8 to 1. However analysts must also look at the composition of both current assets and current liabilities.

Inventory Turnover

One of the key roles of management is to optimise the cash flow and profit from investment in the company's assets. In manufacturing and retailing companies, the investment in inventory is very considerable. Hence its efficient management is critical. The secret of sound inventory control is to hold the inventory levels as low as possible but at adequate levels to meet the needs of production and sales. If the level is too high, capital will be wasted; if too low, sales (profit) opportunities will be lost. Overstocking may result in too much capital which could profitably be invested elsewhere being tied up in inventory,

excessive storage costs and the company may risk a loss through deterioration of inventory or obsolescence. On the other hand, understocking may result in lost sales, emergency purchases from uneconomic sources and higher production costs. The cost of carrying the inventory has to be balanced against the profit opportunities lost by not having the inventory. In a well-managed company there should be a reasonable balance between the levels of sales and inventory.

Inventory earns income when it is sold, hence the rate of inventory turnover is a measure of the efficiency with which investment in inventory is used.

Inventory is listed on the balance sheet at cost, not selling price. Therefore inventory should be compared with cost of goods sold rather than the selling price.

The stock or inventory turnover ratio is calculated by the formula:

$$\text{Inventory Turnover} = \frac{\text{Cost of goods sold}}{\text{Average inventory}}$$

With average inventory calculated as follows:

$$\text{Average Inventory} = \frac{\text{Opening inventory and closing inventory}}{2}$$

$$\text{Inventory Turnover} = \frac{1,520,000}{380,000} = 4$$

This means that inventory turned over 4 times during the year or the average inventory held took approximately 91 days (365 divided by 4) to sell.

The rate at which inventory turns over varies depending on the nature of the business. A rate of 4 may be considered appropriate in the case of a business selling white goods but quite inappropriate for a baker selling fresh bread ... 91 day old bread!!

Debtors Turnover

Another measure of management efficiency is to examine the number of days required to convert trade debtors into cash.

The calculation is trade debtors divided by total sale and multiplied by 365 to convert to a daily basis. All trade debtors figure used excludes the deduction of provision for doubtful debts.

$$\begin{aligned} \text{Days Debtors} &= \frac{\text{Trade Debtors}}{\text{Sales revenue}} \times 365 \\ &= \frac{29,364 \times 365}{319,026} \\ &= 34 \text{ days} \end{aligned}$$

This means that on average it took 34 days to collect debts. As credit terms are normally 30 days, 34 days appears an excellent collection period. However, actual collection period is longer because sale revenue includes an unknown portion of cash sales. A collection period of sixty days would cause concern. In contrast, the retail sector, which tends to avoid substantial credit sales would display average debtor collection periods of around five days. Hence there is a significant variation in the proportion of cash sales across industries and this accounts for large discrepancies in the debtor turnover ratio on an industry by industry basis.

Creditors Turnover

The day's creditors ratio is calculated by dividing trade creditors by sales revenue and multiplying by 365 to convert it to a number of days basis.

$$\text{Days Creditors} = \frac{\text{Trade creditors}}{\text{Sales revenue}} \times 365$$

the calculation is as follows:

$$\begin{aligned}
 \text{Days Creditors} &= \frac{20,507}{319,026} \times 365 \\
 &= 23 \text{ days}
 \end{aligned}$$

In a soundly financed business enterprise there should be a proper balance between funds obtained from the shareholders' equity and borrowed funds. There should also be an appropriate balance between short and long-term borrowing.

As a general rule fixed assets and long-term investments should be financed from long-term sources such as shareholders' equity or long-term borrowing. Short-term borrowing should be used to meet the immediate day to day needs, to pay expenses and to finance varying levels of inventories and debtors.

There is a tendency among new enterprises to rely heavily on bank overdrafts, this often proves disastrous.

The Debt to equity ratio is calculated by dividing total liabilities by the shareholders' equity (excluding minority interests). In practice analysts tend to use only interest-bearing debt and net of cash and deposits when calculating this ratio.

$$\text{Debt to Equity} = \frac{\text{Total liabilities}}{\text{Shareholders' equity}}$$

The ratio is:

$$\begin{aligned}
 \text{Debt to Equity} &= \frac{77,884}{123,296} \\
 &= 0.63
 \end{aligned}$$

There are no hard and fast rules regarding acceptable debt to equity or gearing ratios, however many business enterprises wish to stay below a 1 to 1 debt to equity ratio. What is

an appropriate ratio in a particular case would depend on the nature of the business and its history.

There are many more ratios, which can be calculated from balance sheet and P/L figures. We have concentrated on those which are of most relevance to an underwriter who is supporting with his insurance an actual or potential creditor and who is most often unsecured particularly where consumer goods are concerned.

| |
|---|
| CREDIT SCORING MODEL (BASED SOLELY ON FINANCIAL INFORMATION) |
|---|

SCORING GUIDE

| RATIOS | 1 | 2 | 3 | 4 | 5 |
|---------------------------------------|-----|------|-----|-------|-------|
| CURRENT | 2.5 | 2.0 | 1.5 | 1.0 | <1.0 |
| QUICK | 1.5 | 1.3 | 1.0 | 0.8 | <0.75 |
| TOTAL DEBT/ NETWORTH | 0.5 | 0.75 | 1.0 | > 1.0 | >1.5 |
| CREDIT LIMIT AS % OF NETWORTH | 5 | 10 | 15 | 25 | >25 |
| NET PROFIT ON SALES % | 8.0 | 6.0 | 3.5 | 1.0 | <1.0 |
| ACC RECEIVABLE / TURNOVER (DSO) | 30 | 40 | 50 | 60 | >60 |
| INV/ TURNOVER | 30 | 40 | 50 | 60 | >60 |
| INV / CURRENT ASSETS | 0.3 | 0.35 | 0.4 | 0.6 | >0.6 |

TOTALSCORE

LEGEND:

| | |
|---------|---------------|
| 10 - 15 | EXCELLENT |
| 16 - 25 | GOOD ACCOUNT |
| 26 - 35 | WATCH/CONTROL |
| 36 - 40 | GET OUT |

CHAPTER IV

EVALUATION AND CONTROL OF RISKS ON BANKS

A. RISK PERCEIVED UNDER TRADE CREDIT INSURANCE

1. THE INSOLVENCY OF A BANK
2. THE DEFAULT OR DISHONORING OF PAYMENT
3. POLITICAL RISKS SUCH AS WAR, TRANSFER DELAY & MORATORIUM WHICH MAY DELAY OR PREVENT THE TRANSFER OF FUNDS TO NEGOTIATING OR CONFIRMING BANK.

B. RISK FACTORS OF A BANK

1. OPERATING RESULTS
2. QUALITY OF ASSETS
3. THE STABILITY OF LIABILITIES
4. THE COMPOSITIONS OF ASSETS AND LIABILITIES & SHAREHOLDERS' FUNDS

C. BANK CREDIT WORTHINESS

1. MANAGEMENT RISK (MICRO)

Analysis on the management's capability and efficiency in running the bank in terms of its risk taking policy.

2. COUNTRY ASSESSMENT

Foreign exchange difficulties, war, civil unrest & revolution, natural disaster, moratorium of payment commitments.

D. RATIOS DETERMINING THE SOUNDNESS OF A BANK

1. PROFITBALILTY

(low return may influence or contribute to flight of deposits and other sources of funds)

2. LIQUIDITY

3. ASSETS QUALITY

4. CAPITAL ADEQUACY

CHAPTER V
CAPITAL AND RESOURCES COMPUTATION

1. Capital Funds = x (see A - attached)
2. Net Working Funds = y (see B - attached)
3. Risk Weights = m (see C - attached)
4. Conversion Factors = a or b (see D & E attached)
5. Total Weighted Risk Assets = (i) + (ii) + (iii) = n
- (i) On Balance Sheet items X m
 - (ii) Off Balance Sheet Items X a X m
 - (iii) Foreign Exchange and
Interest Contracts X b X m or 50%*
6. Risk Weighted Capital Ratio = $\frac{x/y}{n} \times 100$

* 50% applicable to counterparties which would otherwise attract a 100% weight since the counterparties in these markets are usually first class names.

A - CAPITAL FUNDS

The constituents of capital funds

In principle, a constituent of capital funds should possess the following characteristics:-

- i) fully paid-up and permanently available;
- ii) freely available and not earmarked to particular assets or banking activities;
- iii) able to absorb losses occurring in the course of an on-going business; and
- iv) represents no fixed charge on the earnings of an institution.

A two-tier system is used in the determination of capital funds. Tier 1 capital (also known as core capital) consists of elements which satisfy the four criteria stated above. They represent resources that can be used to meet current losses while enabling the financial institution to continue operating as a going concern. Tier 2 capital (also known as supplementary capital), on the other hand, comprises elements which are available to meet losses, but which have certain drawbacks compared with the core capital, for example, in the case of a subordinated loan, it cannot be utilised to absorb on-going losses, it can only do so in the event of liquidation. Taking cognizance of the drawbacks, Tier 2 capital components are, in aggregate, limited to no more than the amount of core capital, besides being subject to various other restrictions. In arriving at the final amount of capital funds, certain deductions are made. Goodwill, which cannot be used to support losses on an on-going basis, is deducted from Tier 1 capital. Investments in subsidiaries and other financial institutions' capital are also deducted in assessing capital adequacy on an institutional or global basis (unconsolidated subsidiaries in the case of a consolidated assessment), in order to prevent double-leveraging of capital resources in the system.

Thus, the capital funds would consist of:-

Tier 1 capital: -

- i) Ordinary paid-up share capital;
- ii) Non-cumulative perpetual preference shares;
- iii) Share premium;
- iv) Statutory reserve fund;
- v) General reserve fund,
- vi) Retained profits as in last audited accounts less any accumulated losses, including current unaudited losses;
- vii) After tax surplus arising from the sale of fixed assets and long-term investments in the current financial year;
- viii) Current unadjusted net profits on a half-yearly basis subject to certification by approved external auditors; and
- ix) Minority interests consistent with the Tier 1 capital components (applicable only in the case of consolidated assessment).

Less: Goodwill

Plus: Tier 2 capital (limited to no more than Tier 1 capital):-

- i) Hybrid capital instruments, for example, cumulative perpetual preference shares, perpetual loan stocks and mandatory convertible loan stocks, approved by the Central Bank on a case-by-case basis;

- ii) Minority interests arising from consolidation of the preference shares issued by subsidiaries. (applicable only in the case of consolidated assessment);
- iii) Subordinated term debt approved by Central Bank (eligible amount restricted to 50% of core capital);
- iv) Revaluation reserves of premises; and
- v) General provisions for bad and doubtful debts.

Less:

- i) Investment in unconsolidated subsidiaries; and
- ii) Holdings of other licensed financial institutions' capital.

B - NET WORKING FUNDS

Composition of Net Working Funds

- i) Net amount due to Head Office and Branches Outside Malaysia, denominated in ringgit.
- ii) Retained profit brought forward from previous financial year (as in last audited accounts) arising from their operations in Malaysia (less accumulated losses, including current unadjusted and unaudited losses). However, Bank Negara will permit the following items to be included:-
 - (a) current unaudited profits on a half-yearly basis subject to certification by the bank's approved external auditor; and
 - (b) any surplus after tax, arising from the sale of fixed and long-term investments in the course of the bank's current financial year.

iii) General provision for bad and doubtful debts (as reported in last audited accounts) arising from their operations in Malaysia, provided specific provisions are not staggered.

iv) Reserves arising from the revaluation of premises.

Deduct:

v) Net amount due from Head Branches outside Malaysia in foreign currency.

vi) Net amount due from other banks and financial institutions in and outside Malaysia in foreign currency.

Less

Net amount due to Head Office and branches outside Malaysia in foreign currency (applies only in the case where (v) above is a net inflow).

vii) Net amount due from other banks and other financial institutions outside Malaysia dominated in ringgit.

viii) Net other assets outside Malaysia in all currencies (excluding foreign trade bills).

Risk weights by category of on-balance-sheet assets

- 0%
- a) Cash¹
 - b) Claims on central governments and central banks denominated in national currency and funded in that currency.
 - c) Other claims on OECD², central governments³, and central banks.
 - d) Claims collateralised by cash or OECD central government

| | |
|--|--|
| 0%, 10%, 20% or 50% (at national discretion) | <ul style="list-style-type: none"> e) securities³ or guaranteed by OECD central governments⁴. a) Claims on domestic public-sector entities, excluding central-government, and loans guaranteed⁴ by such entities. |
| 20% | <ul style="list-style-type: none"> a) Claims on Multilateral development banks (IBRD; IADB; AsDB; AfDB; EIB)⁵ and claims guaranteed by, or collateralised by securities issued by such banks⁴. b) Claims on banks incorporated in the OECD and loans guaranteed⁴ by OECD incorporated banks. c) Claims on banks incorporated in countries outside the OECD with a residual maturity of up to one year and loans with a residual maturity of up to one year guaranteed by banks incorporated in countries outside the OECD. d) Claims on non-domestic OECD public-sector entities, excluding central government, and loans guaranteed⁴ by such entities. e) Cash items in process of collection. |
| 50% | <ul style="list-style-type: none"> a) Loans fully secured by mortgage on residential property that is, or will be, occupied by the borrower or that is rented. |
| 100% | <ul style="list-style-type: none"> a) Claims on the private sector. b) Claims on banks incorporated outside the OECD with residual maturity of over one year. c) Claims on central governments outside the OECD (unless denominated in national currency - and funded in that currency - see above.) d) Claims on commercial companies owned by the public sector. e) Premises, plant and equipment and other fixed assets. f) Real estate and other investments (including non-consolidated investment participations in other companies). g) Capital instruments issued by other banks (unless deducted from capital). h) All other assets. |

Notes:

- 1 Includes (at national discretion) gold bullion held in own vaults or on an allocated basis to the extent backed by bullion liabilities.
- 2 The OECD comprises countries which are full members of the OECO or which have concluded special lending arrangements with the IMF associated with the Fund's General Arrangements to Borrow.
- 3 Some member countries interact to apply weights to securities issued by OECO central governments to take account of investment risk. These weights would for example be 10 percent for all securities or 10percent for those maturing in up to one year and 20 per cent for those maturing in over one year.
- 4 Commercial loans partially guaranteed by these bodies -will attract equivalent low -weights on that part of the loan which is fully covered. Similarly. loans partially collateralised by cash or securities issued by OECD central governments and multilateral development banks will attract low weights on that part of the loan which is fully covered.
- 5 Claims on other multilateral development banks in which G-10 countries are shareholding members may at national discretion, also attract a 22 per cent weight.

D - CONVERSION FACTORS

Credit conversion factors for off-balance-sheet items

The framework takes account of the credit risk on off-balance-sheet exposures by applying credit conversion factors to the different types of off-balance-sheet instruments or transactions. With the exception of foreign and interest rate related contingencies, the credit conversion factors are set out in the table below. They are derived from the estimated size and likely occurrence of the credit exposure, as well as the relative degree of credit risk as

identified in the Committee's paper "The management of banks' off-balance-sheet exposures: a supervisory perspective" issued in March 1986. The credit conversion factors would be multiplied by the weights applicable to the category of the counterparty for an on-balance-sheet transaction.

Instruments

| | Credit Conversion Factors |
|---|------------------------------|
| 1. Direct credit substitutes, eg. general guarantees of indebtedness (including standby letters of credit serving as financial guarantees for loans and securities) and acceptances (including endorsements with the character of acceptances). | 100% |
| 2. Certain transaction-related contingent items (eg. performance bonds, bid bonds, warranties and standby letters of credit related to particular transactions). | 50% |
| 3. Short-term self-liquidating trade-related contingencies (such as documentary credits collateralised by the underlying shipments). | 20% |
| 4. Sale and repurchase agreements and asset sales with recourse ¹ . where the credit risk remains with the bank. | 100% |
| 5. Forward asset purchases, forward deposits and partly-paid shares and securities ¹ which represent commitments with certain drawdown. | 100% |
| 6. Note issuance facilities and revolving under-writing facilities. | 50% |
| 7. Other commitments (e.g. formal standby facilities and credit lines) with an original ² maturity of over one year. | 50% |

¹ These items are to be weighted according to the type of asset and not according to the type of counterparty with whom the transaction has been entered into. Reverse repos (i.e. purchase and resale agreements - where the bank is the receiver of the asset) are to be treated as collateralised loans, reflecting the economic reality of the transaction. The risk is therefore to be measured as an exposure on the counterparty. Where the asset temporarily acquired is a security which attracts a preferential risk weighting, this would be recognised as collateral and the risk weighting would be reduced accordingly.

² See footnote 5 in the main text.

8. Similar commitments with an original² maturity of up to one year or 0% which can be unconditionally cancelled at any time.

(N.B. Member countries will have some limited discretion to allocate particular instruments into items 1 to 8 above according to the characteristics of the instrument in the national market.)

Foreign exchange and interest rate related contingencies

The treatment of foreign exchange and interest rate related items needs special attention because banks are not exposed to credit risk for the full face value of their contracts, but only to the potential cost of replacing the cash flow (on contracts showing positive value) if the counterparty defaults. The credit equivalent amounts will depend inter alia on the maturity of the contract and on the volatility of the rates underlying that type of instrument.

Despite the wide range of different instruments in the market, the theoretical basis for assessing the credit risk on all of them has been the same. It has consisted of an analysis of the behaviour of matched pairs of swaps under different volatility assumptions. Since exchange rate contracts involve an exchange of principal on maturity, as well as being generally more volatile, higher conversion factors are proposed for those instruments which feature exchange rate risk. Interest rate contracts³ are defined to include single-currency interest rate swaps; basis-swaps; forward rate agreements; interest rate futures, interest rate options purchased and similar instruments. Exchange rate contracts³ include cross-currency interest rate swaps, forward foreign exchange contracts, currency futures, currency options purchased and similar instruments. Exchange rate contracts with an original maturity of 14 calendar days or less are excluded.

³ Instruments traded on exchanges may be excluded where they are subject to daily margining requirements. Options purchased over the counter are included with the same conversion factors as other instruments, but this decision might be reversed in the light of future experience.

A majority of G-10 supervisory authorities are of the view that the best way to assess the credit risk on these items is to ask banks to calculate the current replacement cost by marking contracts to market, thus capturing the current exposure without any need for estimation, and then adding a factor (the "add-on") to reflect the potential future exposure over the remaining life of the contract. It has been agreed that, in order to calculate the credit equivalent amount of its off-balance-sheet interest rate and foreign exchange rate instruments under this current exposure method, a bank would sum:

- the total replacement cost (obtained by "marking to market") of all its contracts with positive value and;
- an amount for potential future credit exposure calculated on the basis of the total notional principal amount of its book, split by residual maturity as follows:

| Residual maturity | Interest Rate Contracts | Exchange Rate Contracts |
|--------------------|----------------------------|----------------------------|
| Less than one year | nil | 1.0% |
| One year and over | 0.5% | 5.0% |

No potential credit exposure would be calculated for single currency floating / floating interest rate swaps: the credit exposure on these contracts would be evaluated solely on the basis of their mark-to-market value.

A few G-10 supervisors believe that this two-step approach, incorporating a "mark to market" element, is not consistent with the remainder of the capital framework. They favour a simpler method whereby the potential credit exposure is estimated against each type of contract and a notional capital weight allotted, no matter what the market value of the contract might be at a particular reporting date. It has therefore been agreed supervisory authorities should have discretion⁴ to apply the alternative method of calculation described below, in which credit conversion factors are derived without reference to the current market price of the instruments. In deciding on what those notional credit conversion factors should

⁴ Some national authorities may permit individual banks to choose which method to adopt, it being understood that once a bank had chosen to apply the current expenditure method, it would not be allowed to switch back to the original exposure method.

be, it has been agreed that a slightly more cautious bias is justified since the current exposure is not being calculated on a regular basis.

In order to arrive at the credit equivalent amount using this original exposure method, a bank would simply apply one of the following two sets of conversion factors to the notional principal amounts of each instrument according to the nature of the instrument and its maturity:

| Maturity⁵ | Interest Rate Contracts | Exchange Rate Contracts |
|-------------------------------------|------------------------------------|------------------------------------|
| Less than one year | 0.5% | 2.0% |
| One year and less than two years | 1.0% | 5.0% (ie. 2% =3%) |
| For each additional year | 1.0% | 3.0% |

It is emphasised that the above conversion factors, as well as the "add-ons" for the current expenditure method, should be regarded as provisional and may be subject to amendment as a result of changes in the volatility of exchange rates and interest rates.

Careful consideration has been given to the arguments put forward for recognising netting, i.e. for weighting the net rather than the gross claims arising out of swaps and similar contracts with the same counter-parties. The criterion on which a decision has been based is the status of a netting contract under national bankruptcy regulations. If a liquidator of a failed counterparty has (or may have) the right to unbundle the netted contracts, demanding performance on those contracts favourable to his client and defaulting on unfavourable contracts, there is no reduction in counterparty risk. Accordingly, it has been agreed that:

- banks may net contracts subject to novation⁶ since it appears that counter-party risk is genuinely reduced by the substitution of a novated contract which legally extinguishes

⁵ For interest rate contracts, there is national discretion as to whether the conversion factors are to be based on original or residual maturity. For exchange rate contracts, the conversion factors are to be calculated according to the original maturity of the instrument.

⁶ Netting by novation as defined in this context is a bilateral contract between two counter-parties under which any obligation to each other to deliver a given currency on a given date is automatically amalgamated with all

the previous obligation. However, since under some national bankruptcy laws liquidators may have the right to unbundle transactions undertaken within a given period under a charge of fraudulent preference, supervisory authorities will have national discretion to require a phase-in period before a novation agreement can be recognised in the weighting framework;

- banks may not for the time being net contracts subject to close-out clauses⁷ The effectiveness of such agreements in an insolvency has not yet been tested in the courts, nor has it been possible to obtain satisfactory legal opinion that liquidators would not be able to overturn them. However, the Committee does not wish to discourage market participants from employing clauses which might well afford protection in certain circumstances in some national jurisdictions and would be prepared to reverse its conclusion if subsequent decisions in the courts support the integrity of close-out netting agreements⁸. In any event, the Committee will continue its work to assess the acceptability of various forms of netting.

Once the bank has calculated the credit equivalent amounts, whether according to the current or the original exposure method, they are to be weighted according to the category of counter-party in the same way as in the main framework, including concessionary weighting in respect of exposures backed by eligible guarantees and collateral. In addition, since most counter-parties in these markets, particularly for long-term contracts, tend to be first-class names, it has been agreed that a 50 per cent weight will be applied in respect of counter-parties, which would otherwise attract a 100 percent weight⁹. However, the Committee will

other obligations for the same currency and value date, legally substituting one single net amount for the previous gross obligations.

⁷ Close-out as defined in this context refers to a bilateral contract which provides that, if one of the counterparties is wound up, the outstanding obligations between the two are accelerated and netted to determine the counterparty's net exposure.

⁸ The other principal form of netting, payments netting, which is designed to reduce the counterparty risk arising out of daily settlements, will not be recognised in the capital framework since the counterparty's gross obligation are not in any way affected.

⁹ Some member countries reserve the right to apply the full 100 percent weight.

keep a close eye on the credit quality of participants in these markets and reserves the right to raise the weights if average credit quality deteriorates or if loss experience increases.

E CONVERSION FACTORS

Conversion of foreign exchange and interest rate related contracts

Special treatment is given to these items since banks are not exposed to credit risk for the full face value of their contracts, but only to the potential cost of replacing the cash-flow difference if the counterparty defaults. The credit equivalent amount will depend, inter alia, on the maturity of the contract and on the volatility of the rates underlying that type of instrument. To determine the credit equivalent amount of a contract using the "original exposure method", the notional principal amount of such contracts is multiplied by one of the following conversion factors determined according to the nature of the instrument and its maturity:-

| Original Maturity | Interest Rate Related Contracts | Exchange Rate Contracts* |
|-------------------------------------|--|---|
| Less than one year | 0.5% | 2.0% |
| One year and less than two years | 1.0% | 5.0% |
| For each additional year | 1.0% | 3.0% |

*Contracts with an original maturity of 14 calendar days or less are excluded.

The credit equivalent of the foreign exchange and interest rate related contracts is weighted according to the category of counterparty or nature of obligor, except that a 50% weight will be applied in respect of counterparties which would otherwise attract a 100% weight in view that the counterparties in these markets are usually first class names.

The minimum standard and transitional requirements

All domestic financial institutions in Malaysia are expected to comply with a minimum risk-weighted capital ratio of 8% by end-1992, while the target minimum ratio for the foreign banks is set at 10% to reflect the fact that net working funds rather than "genuine" capital funds are used. Further; the foreign banks are not subject to the two-tier system applicable to the domestic financial institutions in the computation of the capital base. The "risk, - weighted capital ratio is calculated based on the formula enumerated below:

$$\text{Risk Weighted Capital Ratio (\%)} = \frac{\text{Capital Funds / Net Working Funds}}{\text{Total Weighted Risk Assets}} \times 100$$

$$\text{Total Weighted Risk Assets} = [\text{On-balance sheet items} + (\text{Off-balance sheet items} \times \text{Conversion factor})] \times \text{Risk Weights}$$

To ensure that the financial institutions are able to meet the target minimum standard of 8% (10% in the case of foreign banks), the Central Bank has set out the following transitional requirements:-

- (i) Commencing from end-September 1989, Financial institutions which have a risk-weighted capital ratio below the target ratio of 8% (10% in the case of foreign banks) would not be allowed to dilute the ratio as at that date, and would be required to achieve 7.25% (9.25% for foreign banks) by end-1990; and
- (ii) Financial institutions which have a ratio of 8% or more (10% or more for foreign banks) as at the end of September 1989 would not be allowed to dilute the ratio to below the 1992 target.

Depending on the availability of figures, the ratios for the above would appear as follows:

1. Notation

- CA: Cash (and due from banks)
- CS: Capital Stock/Paid up capital
- DC: Debt Capital (Long-Term Subordinated Debt)
- EC: Equity Capital
- FA: Fixed Assets
- NI: Net Income
- RA: Risks Assets (total assets less cash and government securities)
- RL: Reserves on Loans and Securities
- TA: Total Assets
- TC: Total Capital (EC + DC + RL)
- TD: Total Deposits

2. Ratios

- (a) TC / TD
- (b) TC / TA
- (c) TC / RA
- (d) Loans / TD
- (e) Provision / Average Lending or loans
- (f) Liquid Assets / Average TC
- (g) Liquid Assets / Average Deposits or TD
- (h) Net Loan / Average Deposits or TD
- (i) NI / TC
- (j) NI / TA
- (k) $NI / \text{Total Operating Income}$
- (l) $\text{Interest Income} / \text{Total Operating Income}$
- (m) $\text{Non-Interest Income} / \text{Total Operating Income}$
- (n) Staff / NI
- (o) $\text{Non Interest Expense} / \text{Total Operating Expenses}$
- (p) $\text{Interest Expenses} / \text{Total Operating Expenses}$
- (q) Capital Formation Rate =

$$\frac{\text{Net Income} - \text{Dividends Paid}}{\text{Total Capital}}$$

Equity Capital (year start)

3. Definitions

- (a) Capital consists of
 - (i) Permanent shareholder's equity (issued and- fully paid ordinary shares/common stock and perpetual non-cumulative preference shares),
 - (ii) Disclosed reserves (created or increased by appropriations of retained earnings or other surplus, eg. share premiums, general reserves and legal reserves)
 - (iii) Minority interests in the equity of subsidiaries, which are less than wholly owned (consolidated accounts only)
- (b) Liquid assets comprise shortest-term assets such as cash, bullion, due from banks (short term deposits with other banks) and investment in securities and other dealing assets.
- (c) Other definitions can be found in a sample bank balance sheet and profit and loss account in Table 2(i) & 2(ii).

Table 2(i)A bank balance sheet and profit and loss account

Consolidated Statement of Condition
as at December 31, 1987

| | 1987 | 1986 |
|--|-------------------|-------------------|
| Assets | | |
| Cash and Due from Banks | 5,425,282 | 6,096,278 |
| Certificates of Deposit | 1,983,805 | 1,411,698 |
| Investment in Securities and Other Dealing Assets | 2,054,389 | 1,596,592 |
| Loans and Advance (less provision for loan losses) | 9,224,882 | 7,568,114 |
| Accrued Interest | 351,820 | 297,702 |
| Investment in Affiliates | 75,365 | 95,554 |
| Property and Equipment | 239,393 | 203,273 |
| Other Assets | <u>288,06.4</u> | <u>210,695</u> |
| Total Assets | <u>19,643,000</u> | <u>17,479,906</u> |
| Liabilities | | |
| Demand Deposits | 2,990,813 | 2,891,912 |
| Savings and Time Deposits | 12,448,424 | 10,893,531 |
| Due to Banks | 2,010,987 | 1,586,962 |
| Floating Rate Notes | 50,000 | 50,000 |
| Accrued Interest on Deposits & Other Funds | <u>224,278</u> | <u>214,327</u> |
| Total Deposits and Other Funds | 17,724,502 | 15,636,732 |
| Provision for Taxes | 46,745. | 59,261 |
| Other liabilities | <u>402,571</u> | <u>337,476</u> |
| Total Liabilities | <u>18,173,818</u> | <u>16,033,469</u> |
| Capital Fund | | |
| Issued and Paid up Shares | 660,000 | 599,169 |
| Proposed Stock Dividend | 66,000 | 60,831 |
| Legal Reserves | 48,316 | 44,649 |
| Retained Earnings and Other Reserves | <u>206,701</u> | <u>336,212</u> |
| Shareholders' Equity | 981,017 | 1,040,861 |

| | | |
|---|-------------------|-------------------|
| Subordinated Capital Notes | 389,000 | 310,500 |
| Minority Interests | <u>99,165</u> | <u>95,076</u> |
| Total Capital Fund | <u>1,469,182</u> | <u>1,446,437</u> |
| Capital Fund and Total liabilities | <u>19,643,000</u> | <u>17,479,906</u> |
| Contra Accounts | | |
| Acceptances | 323,556 | 310,458 |
| Letters of Credit | 2,122,327 | 1,780,757 |
| Letters of Guarantee | <u>2,107,926</u> | <u>2,022,824</u> |
| | <u>4,553,809</u> | <u>4,114,039</u> |

Table 2 (ii)**Consolidated Statement of Earnings**

For the year ended December 31, 1987

| | 1987 | 1986 |
|--|----------------|----------------|
| | US\$'000 | US\$'000 |
| Income | | |
| Interest Income | 1,581,185 | 1,487,442 |
| Interest Expense | (1,195,456) | (1,136,876) |
| Net Interest Income | <u>385,729</u> | <u>350,556</u> |
| Other Operating Income | 293,130 | 347,784 |
| Total Income | <u>678,859</u> | <u>698,350</u> |
| Operating Expenses | | |
| Salaries and Related Costs | 230,536 | 202,980 |
| Occupancy Expenses | 81,550 | 67,214 |
| Depreciation on Property and Equipment | 29,908 | 27,778 |
| Other Expenses | 151,424 | 168,744 |
| Total Expenses | <u>493,418</u> | <u>466,716</u> |
| Net Operating Profit | 185,441 | 231,634 |
| Loan Loss Provision | (70,000) | (112,221) |
| Profit before Taxation | <u>115,441</u> | <u>119,413</u> |
| Taxation for the year | (60,000) | (68,207) |
| Profit after Taxation | <u>55,441</u> | <u>51,206</u> |
| Minority Interests | (17,998) | (29,025) |
| Profit Attributable to Shareholders | <u>37,453</u> | <u>22,181</u> |
| Statement of Retained Earnings and Other Reserves | | |
| At beginning of the year | 336,212 | 218,324 |
| Adjustment to provisions brought forward | (100,000) | — |
| Profit for the year | <u>37,453</u> | <u>22,181</u> |
| | 273,665 | 240,505 |
| Premium on issue of shares | — | 187,500 |

| | | |
|---|----------------|----------------|
| Other Reserve Movements | 12,371 | (19,783) |
| Appropriations | | |
| Proposed Stock Dividends | (66,000) | (60,831) |
| Transfer to Legal Reserves | (4,766) | (4,222) |
| Other Appropriations | (8,569) | (6,957) |
| Carried forward at end of the year | <u>206,701</u> | <u>336,212</u> |

Trend Analysis

The above ratios would be analysed for a number of years to observe the performance and management in terms of trends or changes over those years.

Such ratios would be compared with other similar banks or against the norm of financial institutions if available, to reach a meaningful conclusion of the financial health of the bank evaluated.

Basle Capital Accord

As frequently noted, the role of bank capital is to provide a fund against which to charge off temporary and unexpected loss. It is also a more sound primary indicator of a bank's strength.

In this connection, the Basle Capital Accord adopting the weighted risk asset approach can be used to measure capital adequacy in line with the set minimum.

Appendix A provides an account of the Basle Capital Accord on Capital Adequacy Requirement Risk-weight capital Ratio and also the New Capital Adequacy Requirement of BNM**

In determining the capital adequacy, if figures are available, comparison will be made against the standard set under the Basle Capital accord and also that of BNM's Capital Adequacy Requirement.

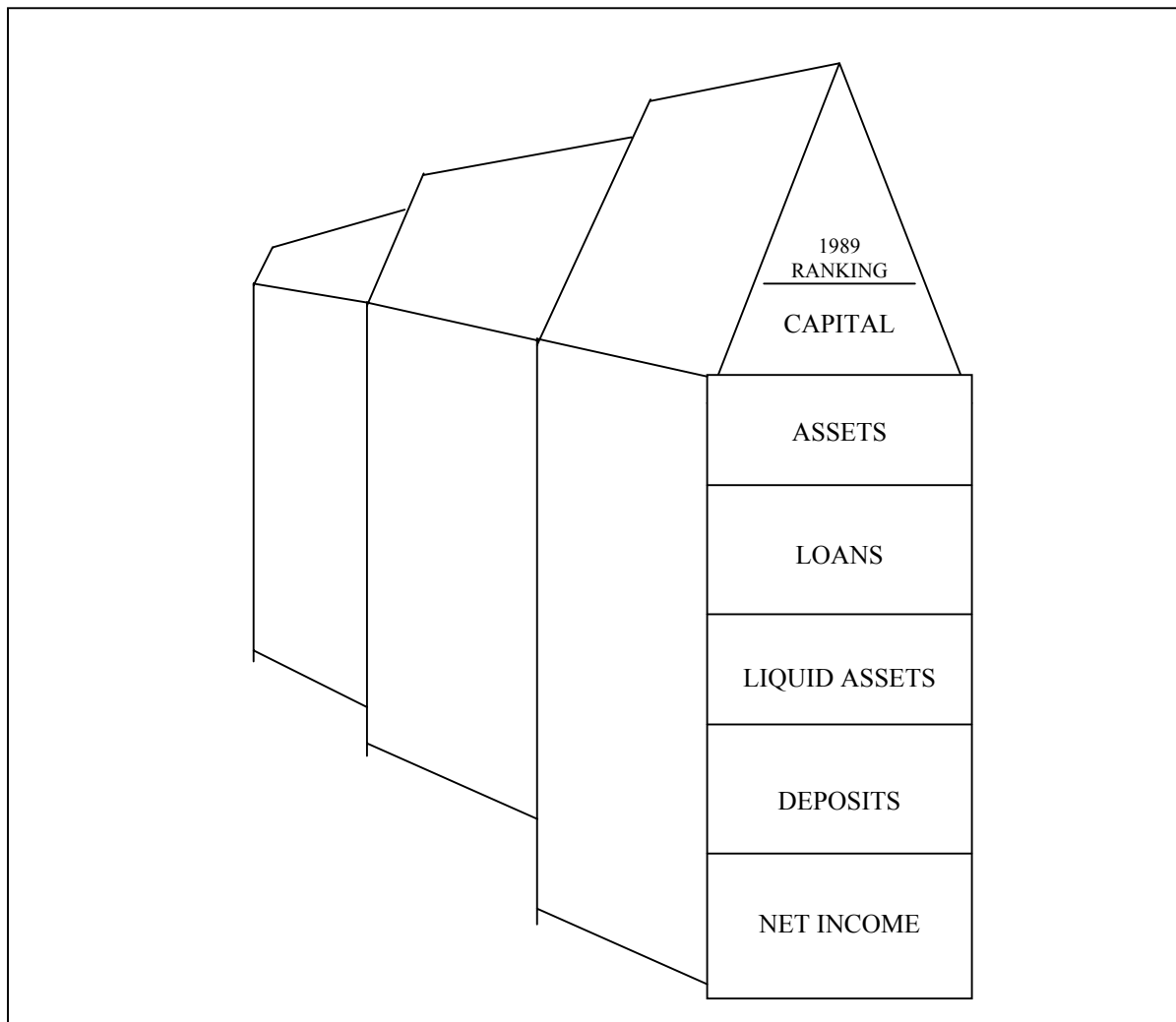
Decision

For the purpose of an analysis to support bank to add confirmation on L/C from a foreign bank, a less complex evaluation can be carried out as indicated in Table 3.

This will be sufficient to enable the analyst to reach his decision whether the risk perceived is acceptable or not.

* Bank Negara Malaysia

Table 3 Profile and basic performance indicators



For a decision to encompass a revolving or operational relationship, it will require an in-depth appraisal on the performance and management.

Credit Limit Submission Sheet

In view of the above, the attached credit limit submission sheet adopted from underwriting a buyer's credit limit will be used to evaluate the financial health of the L/C issuing bank and the fixing of a credit limit.

Capital Adequacy Requirement (CAR)

The computation of CAR on a foreign L/C issuing bank could be made if information for such purpose is available. The basic for CAR however would follow the paper on CAR Risk weighted Capital Ratio see Appendix II on CAR. The CAR is based on a concept of

weighting assets according to their perceived level of risk (categorised into five risk weights of 0%, 10%, 20%, 50% and 100%) and assessing the adequacy of capital on the risk-adjusted assets. The weighted risk asset approach weights both on and off balance sheet exposures of a financial institution to credit risk. The categories of risk weights are broad-brush in their judgement of the riskiness of various types of assets and are not meant to be a substitute for assessment of creditworthiness based on the evaluation of ratios as explained in the above paragraphs.

The risk weighted capital ratio is calculated based on the formula enumerated below:

$$\text{Risk weighted capital ratio} = \frac{\text{Capital Funds/Net working funds} \times 100}{\text{Total Weighted Risk Assets}}$$

$$\text{Total Weighted Risk Assets} = [\text{On-Balance Sheet Items} + (\text{off-Balance Sheet Items} \times \text{Conversion Factor})] \times \text{Risk Weights}$$

How To Obtain Financial Information On L/C Issuing Bank (LCIB)

1. All applications for approval on L/C to be confirmed is required to be accompanied with a latest annual report or financial information especially when the LCIB is the applicant's correspondence bank.
2. A reference will be made to Polk's or other Bankers' Directories to extract relevant financial or other information if available.
3. A direct request will be made to the banker or its parent. This is necessary in connection with the preparation of pre-approved list.
4. BI Group library or other libraries (BNM) may be approached to obtain the required information.
5. If possible or established, to obtain comments from BNM in respect of bank whose L/C is to be confirmed.

APPENDIX I

CASE STUDIES

Case Study 1

Introduction

HKECIC received a credit limit application from its policyholder, AAA Co. Ltd. on an Australian buyer, XYZ Pty. Ltd. The application amount was USD1.5 million DP 30 days. According to the policyholder, he had received USD1.2 million worth of orders from this buyer. The product involved was baby garment. This was a new buyer to the policyholder.

Policyholder's background

The policyholder is one of HKECIC's largest customers who joined the Corporation in 1979 with an annual declaration of over USD25 million. The loss ratio since inception of policy is 22% but the last claim paid dated back to ten years ago. The major insurable markets are Australia, United Kingdom, France and the Netherlands. Most of its insured buyers are large companies. However, almost 80% of its insured business concentrated on one major buyer in Australia, which is a large retail chain store of casual wear.

Buyer's information

The buyer, XYZ Pty. Ltd. is a wholesaler and retailer of children's clothing and footwear started in 1986 with 18 employees. Suppliers reported that payment experience of this buyer has been satisfactory. Usually the buyer would pay in 30 to 50 days. It imports 60% from Hong Kong and Thailand and sells to general public, retailers and also exports to New Zealand. A check on internal records showed no court actions against the buyer and its management.

The Policyholder was able to obtain the buyer's unaudited financial statements for 1993 and 1994. Brief financial extracts are shown below.

| | <u>Financial Year 1995</u> <u>(USD)</u> | <u>Financial Year 1994</u> <u>(USD)</u> |
|---|--|--|
| Operating profit before abnormal items | 381,355 | 233,028 |
| Abnormal items | 0 | 307,930 |
| Operating profit (loss) | 381,335 | (74,902) |
| Retained profit (accumulated loss) at the beginning of the financial year | (164,589) | (128,823) |
| Retained profit at the end of the financial year | 126,561 | (164,589) |
| * | * | * |
| Current assets | 2,513,945 | 1,068,553 |
| Non-current assets | 538,224 | 305,286 |
| Current liabilities | 1,828,378 | 521,693 |
| Long term liabilities | 587,165 | 1,016,674 |
| Networth | 636,625 | (164,528) |

STOP!
ACTION REQUIRED - GO TO QUESTION 1

Additional buyer information

The Underwriter paid a visit to the policyholder in an effort to gather more information on the buyer. The Policyholder advised during the meeting that the buyer had obtained the licence from OBG Inc. to sell its "OB" brand items. "OB" brand is an established brand enjoying good reputation in the children's clothing industry. The Underwriter subsequently obtained information on OBG Inc. and found out that OBG Inc. is a large public listed company in the USA engaging in manufacturing of children's sportswear and casual wear with 7,000 employees. It started business in 1895 and as at 31 December 1996, it had a networth of USD340 million. So far OBG had been operating profitably with steady sales and profit trends.

Under the licence agreement, the buyer can sell "OB" products but all goods from the policyholder have to be checked and approved by the liaison office of OBG Inc. in Hong Kong.

The policyholder was also able to supply more up-to-date unaudited financial statement of the buyer for the year ended 1996 for reference. Extracts of the financial data are shown below for reference.

| | <u>Financial Year 1996</u> |
|---|-----------------------------------|
| | <u>(USD)</u> |
| Operating profit | 342,782 |
| Retained profits at the end of the year | 152,185 |
| * | * |
| Current assets | 3,252,398 |
| Non current assets | 181,163 |
| Current liabilities | 2,190,605 |
| Long term liabilities | 580,711 |
| Networth | 662,245 |

STOP!

ACTION REQUIRED~ GO TO QUESTION 2

New credit limit application

Six months later, another policyholder, BBB Co Ltd. applied for a credit limit for USD1 million DA90 on the same buyer, XYZ Pty. Ltd. and said to have obtained USDO.5 million orders. BBB Co. Ltd. also did not have any trading experience with this buyer before. This PH joined HKECIC in 1987 with no claims record. There was no declaration in the past 12 months.

STOP!
ACTION REQUIRED - GO TO QUESTION 3

ACTIONS REQUIRED

Question 1

- a) Based on the information provided, please decide what credit limit you would issue on this buyer. Please explain the factors you have taken into account.

- b) What additional information you may ask, if any in order to make the credit limit decision.

Question 2

With the additional information obtained, would your credit limit indication in Question 1 above vary? If yes, what credit limit would you issue and why?
If not, why not?

Question 3

How would you handle this credit limit application and state your rationale. What additional information may be helpful for your decision?

- END -

Case Study 2.

CLA for \$16mn on 0A30 days terms on a Hong Kong buying office

The Policyholder

- PH joined us in July 1992. It is a manufacturer of toys, Total declarations since inception amount to \$3mn and total premium \$31,000. Claims record is clean.

The Buyer

- The buying office was established in 1977. Its paid up capital is \$463,000 and turnover for the year ended 31-12-1993 was \$310mn. There are 200 staff in the office.
- Its parent was founded in 1912. It is a publicly listed company in the USA. It is one of the world's leading toy companies and has subsidiaries in many countries. Below are some extracts of the consolidated figures of the group

| | <u>Year ended 31-12-95</u> (US Mn.) | <u>Year ended 25-12-1994</u> (US Mn.) |
|------------------|--|--|
| Sales | 2,858 | 2,670 |
| Net Profit | 156 | 175 |
| Cur. Assets | 1,425 | 1,252 |
| Cur. Liabilities | 870 | 763 |
| L.T. Liabilities | 221 | 219 |
| Networth | 1,052 | 915 |

- Questions:**
- (a) Do you need any additional information on PH and/ or the buyer ? If yes, please specify.**
 - (b) What will be the terms of your CL decision and the reasons for it?**

*(*Please feel free to make possible assumptions.)*

Case Study 3.

Buyer Risk Management Case Study

The following request was received on 30th Aug 95 a PH for approval to change payment terms and to extend due dates of three shipments made to XYZ Ltd., a buyer in U.K.:

| Shipment Date | Shipment Amount (US\$) | Original Payment Terms | Original Due Date | Extended Due Date / New Payment Terms |
|---------------|------------------------|------------------------|-------------------|---------------------------------------|
| 10 Jul 95 | 96,000 | DA 45 | 6 Sep 95 | 21 Oct 95 |
| 15 Jul 95 | 120,000 | DA 45 | 12 Sep 95 | 28 Oct 95 |
| 21 Aug 95 | 120,000 | DP | - | DA 60 |

The buyer told PH that the reason for the request was a cashflow problem.

PH has been trading with the buyer for a few years. Payment experience so far is fair. Similar request was received in Aug 93 for the extension of due dates of a few shipments. The Corp approved the request, and the relevant shipments were subsequently paid.

Additional information:

Goods: Halloween items

CL: \$2.5m. DA 60

O/S: No other outstanding shipments apart from the above three

Questions:

- (1) Would you accept PH's request?
- (2) What other information, if any, would you require to make the decision?

APPENDIX II

SPECIMEN DOCUMENT CREDIT LIMIT APPLICATION

| | | | |
|---|-----------|--|--|
| To: | | 9 Full name and address of Policy holder | |
| In respect of firm business or a current inquiry in excess of the discretionary limit | | | |
| 1 Full name and address of buyer (Block Letters) | | Policy No. | |
| MECIB's Buyer No. | | 10 This application is: <input type="checkbox"/> a new application <input type="checkbox"/> for review of condition 1 <input type="checkbox"/> or 2 <input type="checkbox"/> <input type="checkbox"/> for increase in limit <input type="checkbox"/> for change of payment terms | |
| 2 Full name and address of buyer's banker (Block Letters) | | 11 If a buyer is old or new (Please complete as requested and available) | |
| 3 Goods | | 1. We have been trading with this buyer since _____ Payments during the last twelve months have been * prompt/regular/delay or please specify _____ | |
| 4 | | 2. Amount currently outstanding with the buyer is RM _____ | |
| Country of Supply | Export to | 3. We have* firm orders/are negotiating for order of RM _____ Terms of Payment _____ | |
| | | Shipping programme effective from | |
| 5 Limit applied for (Highest value of exports outstanding at any one time) | | Month | |
| RM | | Value (RM) | |
| 6 Precise Terms of Payment | | _____ | |
| <input type="checkbox"/> ILC Sight/___days* | | _____ | |
| <input type="checkbox"/> DSD/CAD/DP Sight ___days* | | _____ | |
| <input type="checkbox"/> DA/OA ___days* | | _____ | |
| 7 | | 4. We include a detailed description of our past trading and payment experience in FORM OVERLEAF (At least 2 years) | |
| Please obtain express report and charge priority costs to us. <input type="checkbox"/> Yes <input type="checkbox"/> No | | 12 | |
| 8 | | Date of Application | |
| Please confirm whether the buyer is a subsidiary or associate <input type="checkbox"/> Yes <input type="checkbox"/> No | | Policyholder's Signature and Company Stamp | |
| | | _____ | |
| FOR MECIB's USE | | | |
| Correct Style And/Or Address of Buyer (Policy holder should verify the correctness if different from that applied). | | Date Received by | |
| | | Date Received by | |
| | | INFORMATION SOURCED | |
| | | Name Date Sent Reminder Date Received | |
| | | Bank Agency | |
| A Credit Limit is approved/not approved on this buyer for RM _____ Subject to Terms of Payment _____ _____ | | As recommended for RM _____ As recommended or specify: | |
| and the Credit Limit Conditions _____ _____ overleaf and/or attached | | As recommended or specify: | |
| Recommended/Approved | | Approved | |
| Head/Executive Date: _____ | | GENERAL MANAGER Date: _____ | |

Tick where applicable
* Delete where inapplicable

Terms of Payment ILC = Irrevocable Letter of Credit
DSD = Documentary Sight Draft

DP = Documents Against Payment
 DA = Documents Against Acceptance
 CAD = Cash Against Documents

CREDIT LIMIT CONDITION - forming part of the Credit Limit Approved Overleaf

- (1) We are awaiting further information on this buyer. When it is received, our decision will be reviewed and if it is necessary to revise the limit and/or modify the conditions, you will be advised accordingly.
- (2) The Credit Limit Decisions shall apply only to Shipments/Contracts made up to and includingwhen a fresh application should be submitted to the Company accompanied by full details of your trading experience plus your forward shipping programme.
- (3) Notwithstanding any provisions to the contrary stated in this Credit Limit Decision, this Credit Limit Decision shall apply in respect of goods dispatched on or after
- (4) Paragraph 1(x) of the Comprehensive Policy (Shipments) or Paragraph 1(xi) of the Comprehensive Policy (Contracts) shall attach to any contracts to which this Credit Limit Decision applies.
- (5)(a) The Contract Limit shall not exceed the approved Credit Limit shown overleaf.
 (b) The amount of the Contract Limit shall be RM
- (6) (a) The Company shall have no liability unless payment is made under an Irrevocable Letter of Credit established before shipment of the goods.
 (b) The Company shall have no liability in respect of any loss sustained by reason of a cause of loss occurring after the date on which the issuing bank ceases to be liable for payment in accordance with the terms of the Letter of Credit.
- (7) The Policyholder must obtain the written consent of the Company before he can extend any Due Date of Payment in respect of transactions with this buyer.
- (8) Your application is not approved but the provision of Paragraph 11(ii) and (iv)(Discretionary Limit) of the Policy shall continue to be available to you in respect of transactions with this buyer.
- (9) Any contracts or shipments you may make with/to this buyer shall be for your own account and need not be declared to the Company.
- (10) This Credit Limit has been approved on condition that the Company's liability would be restricted to the extent and value of the goods accepted by the buyer.

| POLICYHOLDER TO COMPLETE IF AVAILABLE* | | | | | | |
|--|------|------------|---------|----------|----------------------------|--------------------------------|
| TRADING EXPERIENCE | | | | | | |
| SHIPMENT | | | PAYMENT | | | REASON(S) FOR LATE/NON PAYMENT |
| Invoice No. | Date | Value (RM) | Terms | Due Date | Date Received* (in M'sias) | |
| | | | | | | |

| | | | | | | |
|--|--|--|--|--|--|--|
| | | | | | | |
|--|--|--|--|--|--|--|

* If space inefficient, please attach separate SIGNED attachments.

APPENDIX III

CREDIT LIMIT SUBMISSION SHEET FOR BANK OPENING L/C

Bank Ref No:

Claim No:

| |
|-----------------------------------|
| PARTICULARS OF APPLICATION |
|-----------------------------------|

| | |
|--|--|
| BANK'S NAME <input style="width: 90%; height: 20px;" type="text"/> | COUNTRY <input style="width: 90%; height: 20px;" type="text"/> |
|--|--|

| | |
|---|--|
| INSURED'S NAME <input style="width: 90%; height: 20px;" type="text"/> | COUNTRY GRADING & SCC <input style="width: 90%; height: 20px;" type="text"/> |
|---|--|

| | |
|--|---|
| TERMS APPLIED <input style="width: 90%; height: 20px;" type="text"/> | AMT APPLIED <input style="width: 90%; height: 20px; text-align: center;" type="text" value="RM"/> |
|--|---|

| | |
|--|--|
| GOODS <input style="width: 90%; height: 20px;" type="text"/> | CLA DATED <input style="width: 90%; height: 20px;" type="text"/> |
|--|--|

Reasons* New Application Increase in Limit Change in Payment Terms Review of Cond 2

| |
|---|
| CURRENT EXPOSURE & COMMITMENTS |
|---|

| | | |
|---|-------------------------------|---|
| AS AT: <input style="width: 150px; height: 20px;" type="text"/> | CURRENT EXPOSURE LEVEL AMOUNT | <input style="width: 90%; height: 20px; text-align: center;" type="text" value="RM"/> |
|---|-------------------------------|---|

| | | |
|--|--|---|
| IN FAVOUR OF: <input style="width: 250px; height: 20px;" type="text"/> | Terms <input style="width: 150px; height: 20px;" type="text"/> | <input style="width: 90%; height: 20px; text-align: center;" type="text" value="RM"/> |
|--|--|---|

| | | |
|--|--|--|
| <input style="width: 250px; height: 20px;" type="text"/> | Terms <input style="width: 150px; height: 20px;" type="text"/> | <input style="width: 90%; height: 20px;" type="text"/> |
|--|--|--|

| |
|--------------------------------------|
| COMMENTS & RECOMMENDATION |
|--------------------------------------|

| | |
|--|---|
| Agency's Credit Opinion* Insured's Credit Opinion* Insured's Financing Experience with Issuing Bank Assessor's Opinion: AMOUNT : RM TERMS : CONDITION(S) : | Good/Satisfactory/Fair/Adverse/Others Good/Satisfactory/Fair/Adverse/Others TOTAL L/C Value Confirmed RM _____ Period From _____ to _____ Outstanding RM _____ Paying Record: Good/Satisfactory/Fair/Regular _____ NAME & SIGNATURE OF ASSESSOR DATE: _____ |
|--|---|

| | |
|----------------------------|--|
| Department head's decision | General manager's approval |
| | Approved/not approved** SIGNATURE OF GENERAL MANAGER DATE: |

Tick, *Delete or Circle as applicable

| | | |
|---|--------------------|---|
| REG NAME <input style="width: 90%; height: 20px;" type="text"/> | L/C ISSUING BANKER | YEAR STARTED <input style="width: 90%; height: 20px;" type="text"/> |
|---|--------------------|---|

| | | |
|---|---|--|
| AUTH. CAPITAL <input style="width: 90%; height: 20px; text-align: center;" type="text" value="RM"/> | PAID UP CAPITAL <input style="width: 90%; height: 20px; text-align: center;" type="text" value="RM"/> | EMPLOYEES <input style="width: 90%; height: 20px;" type="text"/> |
|---|---|--|

LEGAL STATUS* Government Owned Partnership Private Limited Company

Public Company Co-operative Others _____

TYPE OF BUSINESS* Commercial Bank Finance Company Others _____

FINANCIAL POSITION* Not Available Available Incomplete/
As follows Agency/Bank Report
/Both Received on

From Other Source _____

RATIO ASSESSMENT

| Ratios | Formula | Yr | Yr | Yr | Comments |
|-------------------------|----------------------|----|----|----|----------|
| TC/TD | 26/14 | | | | |
| TC/TA | 26/9 | | | | |
| TC/RA | 26/9(Less 1+2+3) | | | | |
| Loans/TD | 4/14 | | | | |
| Prov/Loans | P/14 | | | | |
| LA/TC | 1+2+3/26 | | | | |
| LA/TD | 1+2+3/14 | | | | |
| Net Loans/TD | 4/14 | | | | |
| NI/TC | P/26 | | | | |
| NI/TA | P/9 | | | | |
| NI/TOI | P/C+1 | | | | |
| Int/TOI | D/C+1 | | | | |
| Non Int/TOI | 1-D/C+1 | | | | |
| Staff/NI | K/P | | | | |
| Non Int Exp/TOE | O/C+O | | | | |
| Int Exp/TOE | C/C+O | | | | |
| Capital Formation Ratio | P-DP/EC (Year Start) | | | | |

NOTATION:

| | | | |
|------|-------------------|---------|---------------------------|
| TC | - Total Capital | NI | - Net Income |
| TC | - Total Deposits | TOI | - Total Operating Income |
| TA | - Total Assets | TOE | - Total Operating Expense |
| RA | - Risk Assets | Non Int | - Non Interest |
| PROV | - Loan Provisions | Exp | - Expenses |
| LA | - Liquid Assets | DP | - Dividend Paid |
| INT | - Interest Assets | EC | - Equity Capital |

Checked & Verified by _____

Date _____

(*) Tick/Delete where applicable

APPENDIX IV

SPECIMEN CREDIT REPORT

Report Dated: 13 January 1995

We have great pleasure in submitting, per your request, our

Status Silver Report - SUPPLEMENTARY

On

BRENTAPAC U K PLC

Which is a

British Registered Company

Company number E1458075

| | | |
|------------------------------|---|--------------|
| Service Requested | : | PRIORITY |
| Opinion Requested | : | US \$160,000 |
| Valid for Insurance Purposes | : | YES |

Free Prompt and Constant Update Service

Please return this form if you do not require the free prompt (notification of filing next accounts)

Please tick below and return if you do require the subject to be added to our Constant Update Service.

Level 1

Level 2

Level 3

(Non Corporate only)

BRENTAPAC U K PLC

| | |
|--|--|
| Address | BRENTAPAC HOUSE CHRISTY WAY SOUTHFIELDS BUSINESS PARK BASILDON ESSEX SS15 6TF |
| Telephone Number | 0268 540560 |
| Fax Number | 0268 540565 |
| Telex Number | 99454 |
| VAT NUMBER | 311991269 |
| The "Status" Rating: (Maximum Exposure) | £150,000 |

STATUS OPINION

Amount of Enquiry: US \$160,000
Date of Analysis: 13 January 1995

The subject company was incorporated 15 years ago, it operates from a substantial capital base.

The latest accounts filed by the subject are for year ending the 31 December 1992, sight of later accounts is preferred and we have therefore deliberately suppressed our Status Rating pending sight of 1993 accounts.

These latest filed accounts indicate that the subject company achieved a very small pre-tax profit on a moderate turnover, during the year, the company paid some of its long term liabilities at a cost to its working capital which has reduced.

The company only retains fair liquidity, nothing however adverse relating to it is on file pending sight of 1993 accounts and with due supervision being applied to the account in view of its modest liquidity, dealings of up to the Status Rating, including your figure are deemed an acceptable risk.

Signed.

Director

Statutory Information

| | |
|---|--|
| Registered Number: | E1458075 |
| Legal Status: | PRIVATE |
| The subject was incorporated in: | 1979 |
| The subject changed its name from: | BRENTAPAC U K CO LTD |
| The latest Annual Return on file is made up to: | 1/04/94 |
| Registered Address | BRENTAPAC HOUSE CHRISTY WAY SOUTHFIELDS BUSINESS PARK BASILDON ESSEX SS15 6TF |

DATE CREATED 30/01/86
 DATE REGISTERED 3/02/86
 MORTGAGOR NAME UNITED OVERSEAS BANK LIMITED,
 LONDON
 MORTGAGE TYPE DEBENTURE
 AMOUNT SECURED ALL MONIES DUE
 REFERENCE 3

DATE CREATED 10/08/88
 DATE REGISTERED 17/08/88
 MORTGAGOR NAME UNITED OVERSEAS BANK LIMITED,
 LONDON
 MORTGAGE TYPE MORTGAGE ASSIGNMENT
 AMOUNT SECURED,- ALL MONIES DUE
 REFERENCE 176

DATE CREATED 8/06/89
 DATE REGISTERED 9/06/89
 MORTGAGOR NAME UNITED OVERSEAS BANK LIMITED, LONDON

MORTGAGE TYPE
AMOUNT SECURED
REFERENCE

LEGAL CHARGE
ALL MONIES DUE
201

Capital Structure

ISSUED CAPITAL AMOUNT 2000000
ISSUED -

| SHARE TYPE | NO. SHARES | VALUE |
|------------|------------|-------|
| ORDINARY | 2000000 | 1.00 |

Directors:

| | |
|------------------|---|
| DIRECTOR NAME | RITA LAURIER |
| DIRECTOR ADDRESS | 61 CRANBOURNE GARDENS LONDON NW110JB (ALSO CO. SECRETARY) |

| | |
|-----------------------|-----------------|
| DIRECTOR SHAREHOLDING | |
| SHARE TYPE | NO. SHARES |
| ORDINARY | 269119 |

| | |
|---------------------|---|
| OTHER DIRECTORSHIPS | BRENTAPAC U.K. PLC BRENTWOOD SACK & BAG CO. LTD LOWESTOFT SACK & BAG CO. LTD. GREAT YARMOUTH PAPER & PACKING LTD |
|---------------------|---|

| | |
|------------------|---|
| DIRECTOR NAME | JOAN VIOLET HALLIDAY |
| DIRECTOR ADDRESS | 26 BRACKEN DRIVE CHIGWELL IG7 5RF |

| | |
|------------------|--|
| DIRECTOR NAME | LIONEL LAURIER |
| DIRECTOR ADDRESS | 61 CRANBOURNE GARDENS LONDON NW119JB |

| | |
|-----------------------|-----------------|
| DIRECTOR SHAREHOLDING | |
| SHARE TYPE | NO. SHARES |
| ORDINARY | 817593 |

| | |
|---------------------|--|
| OTHER DIRECTORSHIPS | BRENTAPAC U.K. PLC GREAT YARMOUTH PAPER & PACKING LTD BRENTWOOD SACK & BAG CO. LTD BRENTSAC ENTERPRISES LTD |
|---------------------|--|

LOWESTOFT SACK & BAG CO. LTD.

DIRECTOR NAME
DIRECTOR ADDRESS

MICHAEL NORMAN LAURIER
17 BARHAM AVENUE
ELSTREE
BOREHAM WOOD
WD6 3PW

DIRECTOR SHAREHOLDING
SHARE TYPE
ORDINARY

NO. SHARES
779985

OTHER DIRECTORSHIPS

BRENTAPAC U.K. PLC
GREAT YARMOUTH PAPER & PACKING LTD
BRENTSAC ENTERPRISES LTD
LOWESTOFT SACK & BAG CO. LTD
BRENTWOOD SACK & BAG CO. LTD

Company Secretary:

RITA LAURIER

SHARE HOLDERS NAME

PHILLIP BENJAMIN LAURIER

SHARE HOLDERS ADDRESS

49 HOPTON GARDENS
MARINERS PARK
HOPTON ON SEA
GREAT YARMOUTH

SHARE TYPE
ORDINARY

NO. SHARES
102023

SHARE HOLDERS NAME
SHARE HOLDERS ADDRESS

JULIEN DAVID LAURIER
1A OAKTREE CLOSE
ELSTREE
BOREHAMWOOD

SHARE TYPE
ORDINARY

NO- SHARES
31280

Subsidiary Names:

BRENTSAC ENTERPRISES LTD BRENTWOOD SACK
AND BAG CO LTD GREAT YARMOUTH PAPER AND
PACKING LTD LOWESTOFT SACK AND BAG CO
LTD

Accounts Commentary

Date Of Accounts:

31 December 1992

Number of Months:

12

Type of Accounts: Full
Auditors Report: Clean and Unqualified

Profit and Loss Account

Turnover: Reduced by more than £230,000 and totalled £5,1220,000.

Operating Profit: Totalled £351,700, this represents an increase of more than £100,000 on the Profit achieved in the prior year.

Pre-Tax Profit: After accounting for interest payable, and also a prior year adjustment whereby bad debts were written off, profits reduced to a very modest £1,550.

Profit after Taxation: A tax credit was utilised increasing profit for the year to £3,530.

Extraordinary Items: None

Dividends: None were proposed or paid.

Retained Profit: Totalled £3,530.

Balance Sheet

Fixed Assets: Total £3,014,000, a net increase of £47 in the year.

Working Capital: Reduced by approximately £100,000 and totals £36,400.

Deferred Liabilities/ Creditors: Reduced by £56,300 and totals £909,000.

Deferred Liabilities None

Other:

Share Capital: Unchanged at £2,000,000

Revaluation Reserve: None

Net Worth: Very marginally increased in the year and totals £2,142,000.

Comments: These are acceptable but extremely modest results for the year.

Notes to the Accounts

1. The Directors consider that it is not appropriate to apply depreciation to its goodwill or freehold properties, this being contrary to statements of standard accounting practice. Had this been done, an additional charge of £53,000 should be made. During the year, the company' s freehold properties were re-valued and that valuation has been utilised in these accounts.
2. The company's bank overdraft increased by £320,000 in the year and totals £1,140,000. There are also deferred loans of £890,000, these having reduced b £20,000 period. Bank borrowings are secured by fixed and floating charges over the assets of the company.
3. The company has contingent liabilities in respect of bills of exchange, letters of credit, performance guarantees to its bankers the liability at the last balance sheet date in this respect total £101,500.

Operations

ACTIVITIES STOCKISTS & MANUFACTURERS OF ALL TYPES OF PLASTIC & PACKAGING PRODUCTS

SIC CODES 6540 4835

VAT TRADE CODES AND 8149 OTHER GOODS
DESCRIPTION

Auditors

HARTLEY LAWRENCE MARKS & CO LONDON

Credit Register

A search of the Credit Register revealed the following credit transactions.

| | |
|----------|---|
| 9/11/94 | Total amount repayable in 37 equal monthly instalments of £152 FINANCE HOUSE |
| 11/01/91 | £38,848 OVER 48 MONTHS FINANCE HOUSE |
| 24/07/89 | £35,010 OVER 60 MONTHS FINANCE HOUSE |

TOTAL = 7 (LAST 3 REPORTED)

NO defaults in payments have been recorded.

Bankers

UNITED OVERSEAS BANK LTD, 19 GREAT WINCHESTER ST, LONDON EC2
SORT CODE 23-35-04

CCJ Searches

A search of the County Court Judgement Register has been conducted. No judgements have been recorded in the last six years.

REF: RJS/MRV

Annual Accounts

| ACCOUNTS DATE | 31/12/92 | 31/12/91 | 31/12/90 |
|---|---------------|-----------|-----------|
| NUMBER OF MONTHS | 12 | 12 | 12 |
| CONSOLIDATED ACCOUNTS | <i>NO</i> | <i>NO</i> | <i>NO</i> |
| PROFIT AND LOSS SUMMARY | | | |
| TURNOVER | 5220918 | 5452963 | 5765397 |
| PRE-TAX PROFIT/LOSS | 1554 | 5146 | -31955 |
| BALANCE SHEET SUMMARY | | | |
| WORKING CAPITAL | 36377 | 135475 | 294393 |
| NET ASSETS/LIABILITIES | 3050666 | 3103405 | 3147110 |
| NET WORTH | 2141685 | 2138153 | 2117007 |
| BALANCE SHEET ITEMS | | | |
| FIXED ASSETS | 3014289 | 2967930 | 2752717 |
| STOCKS | 981658 | 794855 | 1028905 |
| DEBTORS | 500 | 16235 | 9619 |
| TRADE DEBTORS | 1254581 | 1347944 | 1562949 |
| CURRENT ASSETS | 2238987 | 2161033 | 2603380 |
| TOTAL ASSETS | 5253276 | 5128963 | 5456097 |
| LONG TERM LIABILITIES | 908981 | 965252 | 1030103 |
| CREDITORS | 1282908 | 937783 | 1202479 |
| TRADE CREDITORS ' | 919702 | 1087775 | 1106508 |
| CURRENT LIABILITIES | 2202610 | 2025558 | 2308987 |
| TOTAL LIABILITIES | 3111591 | 2990810 | 3339090 |
| SHARE CAPITAL | 2000000 | 2000000 | 2000000 |
| TOTAL ALL RESERVES | 141685 | 138153 | 117007 |
| TAKEN FROM A.R. DATED | 1/04/94 | | |
| REG'D INDEBTEDNESS | NOT STATED | | |
| FINANCIAL ANALYSIS (PERCENTAGES) | | | |
| CURRENT RATIO | 101.65 | 106.69 | 112.75 |
| QUICK RATIO | 57.08 | 67.45 | 68.19 |
| SALES:CAPITAL EMPLOYED | 171.14 | 175.71 | 183.20 |
| RETURN ON CAP EMPLOYED | 0.05 | 0.17 | -1.02 |
| PROFIT:SALES | 0.03 | 0.09 | 0.55 |
| ASSETS:LIABILITIES | 168.83 | 171.49 | 163.40 |
| SALES:FIXED ASSETS | 173.21 | 183.73 | 202.10 |
| SALES:TOTAL ASSETS | 99.38 | 106.32 | 105.67 |
| SALES:NET CURR ASSETS | 9999.99 | 4025.07 | 1958.40 |

APPENDIX V

CREDIT EVALUATION

SOURCES OF INFORMATION

- *TRADE REFERENCES
- *BANK REFERENCES
- *INDEPENDENT ENQUIRIES
- *COMPETITORS
- *AGENCY RATING BOOKS
- *AGENCY'S REPORTS
- *CUSTOMER VISIT
- *FINANCIAL PRESS REPORTS
- *TRADE PRESS REPORTS
- *BUYER'S ANNUAL. ACCOUNTS
- *TRADE COMMISSIONERS'R-EPORTS
- *GENERAL COUNTRY INFORMATION

SECTION 9

CLAIMS AND RECOVERIES

CHAPTER I SHORT TERM TRADE INSURANCE - CLAIMS AND RECOVERIES

CHAPTER II CLAIMS AND RECOVERIES - THE SINGAPOREAN APPROACH

CHAPTER III PRINCIPLES OF CLAIMS AND RECOVERIES

APPENDIX 1 CLAIMS FORM

APPENDIX 2 CASE STUDIES

CHAPTER 1

SHORT TERM TRADE INSURANCE

- CLAIMS AND RECOVERIES

Introduction

Claims are part and parcel of insurer's business: if there were none, insurance protection would not be needed. Below is a brief description of objectives of claims processing and the basis and procedures for handling claims arising from short-term trade business.

Objectives in Claims Processing

The objectives in processing claims are:

- (a) to assist policyholders in pursuing overdue payment and minimising loss;
- (b) to give clear advice on the procedures for establishing valid claims;
- (c) to settle claims pragmatically and efficiently.

Buyer under Close Monitoring

A buyer's financial condition and payment ability are subject to change. There are, however, early symptoms of trouble. The common symptoms are:

- (a) slow or unsystematic payment by the buyer;
- (b) progressively late in producing financial statements by the buyer;
- (c) operating results of the buyer have deteriorated significantly;
- (d) request for longer credit terms for future shipments;
- (e) request for extension of due dates for payments;
- (f) request for change of payment terms for goods already shipped; etc.

Even at this stage, the insurer should review the status of the buyer and consider the buyer's requests. The purpose of identifying the buyer under close monitoring is to seek to prevent and to minimize loss.

Payment Difficulty Cases

Not all cases have early warning signs of the buyer in trouble. Very often, the buyer simply fails to pay debts incurred in the ordinary course of business when they fall due. If the policyholder is aware that a possible loss may arise, he should promptly give such information to the insurer, e.g. buyer files a bankruptcy petition. Otherwise, the policyholder is normally required to inform the insurer when the shipment is overdue for more than 2 months.

The insurer will work jointly with the policyholder to find out the reasons for non-payment and to consider the age of the debt, the conditions of the goods, the country of destination, the buyer's financial position and the economic situation of the buyer's country, etc. in order to arrive at the best course of action to be taken.

The sooner a payment difficulty case is reported, the better is the prospect of resolving the problem.

Loss Minimisation Actions

The policyholder should start to take whatever necessary action one would normally take when faced with a potential loss case, just as if he were not insured.

| <u>Events of Loss</u> | <u>Loss Minimization Actions</u> |
|-----------------------|---|
| Insolvency | <ul style="list-style-type: none"> • register debts with receiver/liquidator • withhold shipments in transit • dispose of goods not accepted by the liquidator • follow-up dividend distribution arrangements |
| Default & Repudiation | <ul style="list-style-type: none"> • protest the bill • pursue payment from the buyer |

| | |
|----------------|--|
| | <ul style="list-style-type: none"> • appoint debt-collector / take legal actions • arrange storage, insurance and resale of goods (for repudiation only) |
| Transfer delay | <ul style="list-style-type: none"> • request the buyer to deposit in local currency • request the buyer to comply with all exchange formalities required |

Claims Examination and Settlement

If the payment problem cannot be resolved, claims settlement should be made upon expiry of a waiting period in accordance with the terms of the cover. The Policyholder has to demonstrate that he has fulfilled the terms of the Policy precedent to the admission of liability by the insurer.

The determining factors on whether there is a case for claim payment are:

- (a) event of loss covered under the Policy
- (b) validity of debts established
- (c) Policyholder's compliance with major policy terms, e.g.
 - I existence of a valid credit limit
 - II shipments properly declared
 - III appropriate loss minimisation actions taken

Claims Supporting Documents

The supporting documents usually required are:

- (a) evidence of the contract of sale
- (b) unpaid invoices
- (c) bills of lading or equivalent evidence of shipment
- (d) purchase/collection/negotiation letters to bankers
- (e) bank advises of acceptance of bills of exchange, of non-payment and of protest

- (f) all correspondence relating to the loss minimisation actions

Export credit insurers normally take a pragmatic approach where the insurer is satisfied that his position under the Policy with regard to actions to pursue recoveries will not be jeopardized or where the non-compliance of any of the essential criteria of the policyholder will not increase the level of risk and the ultimate liability and that the policyholder has acted in good faith. However, intentional or fundamental breaches will not be excused.

Recoveries

The policyholder's obligation to minimise loss generally continues after the claim has been paid. The insurer may decide to rely on that obligation, instructing the policyholder as to the actions to be taken, monitoring progress and relying on the policyholder to repay the insurer any recoveries received.

Subrogation

In certain cases, however, having received a substantial reimbursement of the loss suffered by the non-payment, the policyholder has little real incentive to devote further resources to continue pursuing payment, preferring to spend those resources of time and expense on pursuing new business

Recognising this, the insurer may determine to take direct control of the recovery action on a day to day basis by requiring the policyholder to subrogate his rights. This will involve the insurer maintaining direct contact with buyers, receivers and liquidators, lawyers and debt-collectors. Where possible, the insurer may also arrange to receive recovery proceeds direct, distributing the proceeds between itself and the policyholder

Sharing of recoveries and expenses

The insurer and the policyholder should share in the respective proportion of the amount of claim paid to the amount of total loss in relation to

- (a) all sums recovered in relation to the claim case
- (b) any cost incurred for the purpose of loss minimization actions approved by the insurer. This will relieve the policyholders financial burden and lead to quicker action with better prospects or recovery

Written-off

A claim case should be written off as soon as practicable where the prospect of recovery is non-existent or further recovery action is not cost-effective. The basic objective is to concentrate time and efforts on those cases worthwhile pursuing.

Assignment of Rights under the Policy

The policyholder can arrange with his banker a written authorisation initiated by the policyholder and with the written consent of his banker, requiring the insurer to pay direct to the nominated bank all claims which may become payable under the Policy.

Under the arrangement, it does not in any way indicate admission of liability on the part of the insurer. It simply ensures that in the event a valid claim is admitted by the insurer, the claim will be paid by the insurer to the bank instead of to the policyholder.

Recovery Management

- (a) **Principle of Recovery**
 - Policyholder Obligation Continues after Claim Payment
 - Repay Insurer for any Recoveries Received
- (b) **Determining prospects of recovery**
 - Latest information on the buyer
 - Availability of repayment plan

- Information from insolvency estate
- Debt collector/lawyers Advice
- Country information Embassy, Berne Union, Trade Associations

(c) **Common Recovery Problems**

- Policyholder is inert
- Policyholder retains the recoveries
- No documents proving the amount recovered
- Interest payment

(d) **Ways to tackle**

- Frequent follow up with policyholders
- Establish direct contacts & follow up with banks, debt collectors, or even the buyer
- Take strong action to compel the policy-holder to act
- Check the integrity of the policyholder based on previous experience
- Check outstanding with banks, debt-collectors or buyer
- Pay personal visits

CHAPTER II

CLAIMS AND RECOVERIES

The Singapore Approach - Philosophy and Practice

CLAIMS

Claims is one of the pillars in the insurance industry and if there are 2 pillars the other is underwriting. The former can influence the latter as claims experience is indispensable to future underwriting philosophy and criteria for an insurance company.

Claims can also be used as a marketing tool to promote sales. A relaxed and flexible claim policy will promote sales as no one buys a policy with the wish of not ever making a claim.

Many exporters who perceive and appreciate the risks in selling on credit overseas may buy a credit insurance policy for credit protection, to institutionalise their credit and political risks and to maintain cash flow. The last objective cannot be attained when a risk crystallises unless a claim is filed.

There is, therefore, a need and an important one for any export credit agency (ECA) to decide and adopt a Claim Policy or Claim Philosophy.

Should an ECA adopt a strict philosophy to pay claims strictly on terms and conditions of the Policy or to adopt a flexible and marketing oriented philosophy.

What will be your decision in one of the following instances:

- (i) Claim filed was declared late
- (ii) Claim filed was not declared
- (iii) Claim filed where premium was paid late

- (iv) Claim filed where premium is not paid and still outstanding

- (v) Claim filed where premium was paid but there is substantial premium outstanding under the Policy

Your answers to the above will decide the kind of claims philosophy which you wish to adopt. Will your answers be different if the claims payment had been assigned to Banks under Letter(s) of Authority.

Further how would you deal with disputes will also determine your claims philosophy. Are you prepared to be involved in settlement of disputes, pay a conditional claim or defer claim settlement until the exporter resolves the dispute.

Finally will you adopt a philosophy to pay claims so long as the underlying transaction is genuine. The trade promotion policy of an ECA is to help the cash flow of exporters in addition to support and protect the exporting community against the uncertainties of export trade so long as the transactions are genuine. If we adopt this philosophy then we must know our exporters well -- their integrity, standing in the industry and their credit control policy. These will be useful in assessing the manner in which we will assess the claims filed.

In ECICS we are strict in our claims assessment but for exporters who we know well we are prepared to recommend to the Board claims payment when there is noncompliance under the terms of the Policy eg. we have made conditional claims payment for dispute cases where the genuineness of the transactions were not in doubt; claims payments have been made for exports declared late or where premiums were not paid but the outstanding premium did not relate to the transaction under claims examination.

In Singapore, which is a small country, it is essential for us not to have a bad image as a company that does not pay claims. Hence the role of claims in public relations is quite important.

RECOVERIES

Recoveries is a unit in the insurance company which tends to be forgotten. This can be a grave error as recoveries can be an important resource and cash source for an insurance company especially ECAs involved in lumpy transactions. So while claims payment may create a hole in the pocket (or balance sheet) recoveries can be a major contributor to net surpluses or profits. We experienced this in ECICS last year when the sale of a common stock in a US company (which was received in 1988 as part of a recovery settlement) was sold for a very substantial surplus.

One must, therefore, not pay a claim and forget to recover; then we will become a charitable organisation!

CHAPTER III

PRINCIPLES OF CLAIMS AND RECOVERIES

This presentation on claims and recoveries will be made in the following parts:

- 1 Application of insurance principles
- 2 Ascertainment of Loss
- 3 Minimisation of Loss
- 4 Claims Processing
- 5 Claims Processing
- 6 Recoveries

1 **APPLICATION OF INSURANCE PRINCIPLES (INCLUDING POLICY TERMS)**

The following has to be borne in mind when examining any claims:

1.1 Principle of Uberimae Fidei

This is the general principle of utmost good faith. Has the exporter informed us of all material facts that is within his knowledge or has he misrepresented any facts or more important not disclosed or withheld information material to the risks eg. the buyer is a perpetual late payer but this experience was not disclosed to underwriters.

In ECICS this principle is part of the term of the Policy.

1.2 Allocation of Risk Share

Although for short-term business we issue credit limits for every buyer, exporters very often exceed such credit limits. How do we share the risks in claims payment and recoveries?

Firstly to determine the amounts outstanding for claims examination we have to apply the allocation of monies clause in the policy i.e. all payments received by the exporter has to be applied in chronological order of the invoice dates, not the due dates. Why?

An example to illustrate this:

There are 5 invoices which are as follows where the credit limit is \$300,000 on 30 days D/A.

| <u>Invoice Value</u> | <u>Date of Invoice</u> | <u>Due Date</u> | <u>Date of Payment</u> |
|----------------------|------------------------|-----------------|------------------------------------|
| 1. \$100,000 | 2 February 1997 | 2 March 1997 | Outstanding |
| 2. \$100,000 | 15 March 1997 | 15 April 1997 | Outstanding |
| 3. \$100,000 | 20 March 1997 | 20 April 1997 | Outstanding |
| 4. \$100,000 | 1 August 1997 | 30 August 1997 | 20 September 1997 (L/C 30 days) |
| 5. \$100,000 | 15 August 1997 | 15 August 1997 | 17 August 1997 (L/C Sight) |

The buyer was wound-up on 10 September 1997.

The outstandings on face value is \$300,000 and is covered by the credit limit. However, if we apply the allocation of monies clause (as above) and the automatic suspension of credit limit clause for overdues not paid which means the credit limit is

suspended when there are outstandings above 90 days which remain unpaid then we will get the following outcome:

Allocation of monies clause:

The payment for (4) and (5) will be applied to the outstandings of (1) and (2).

However, the balance amount outstanding is still \$300,000.

But applying the automatic suspension clause the credit limit will be suspended on 1 June 1997 when the 2 February 1997 invoice remain unpaid for more than 90 days.

Therefore, invoices (4) and (5) are not covered.

The outstanding balance, therefore, will be

| | |
|---------------------------|---------------------------------------|
| Invoices Covered | less Payments Received |
| Invoices (1), (2) and (3) | less Payment for invoices (4) and (5) |
| \$300,000 | less \$200,000 = \$100,000 |

Therefore, amount of claims for loss ascertainment is \$100,000.

The allocation of monies clause may seem to be harsh on the exporter but it is meant to protect the recovery prospects of the ECA. Otherwise when bill on D/A or open account terms remain unpaid, the exporter could switch to cash or letters of credit terms enabling him to continue supplying goods to the buyer who will then have no incentive or see no need, to pay bills which are outstanding under the credit terms. This undermines our recovery prospects. Further it might also lead to overtrading causing the buyer to go insolvent.

The apportioning of risk share usually is done by determining the amounts outstanding and what is insured say in the above example if all invoices were not paid then the risk share will be as follows:

Insured Debt 85% of \$300,00 = \$255,000

Uninsured Debt \$200,000 + 15% of \$300,000 = \$245,000

The risk share is almost 50 per cent each.

Risk share also determines how recoveries will be shared. In ECICS case we will share recoveries in the same proportion of risk share i.e. in the above example if \$Y is the net amount recovered our recovery will be \$Y

In some cases I know where the Policy term allows the ECA to take the first bite eg. if \$Y is the net amount recovered, the ECA's shares will be 85% of \$Y so long as \$Y does not exceed \$300,000. If \$Y exceeds \$300,000 then only will the exporter get a share for amounts in excess of the credit limit.

1.3 Proximate Cause of Loss

There can be instances when we have to ascertain the proximate cause of loss from the actual cause of loss in order to pay a claim under the Policy for a cause of loss which apparently is not covered by the Policy.

A good example is diversion of voyage which is not a head of loss covered under a standard export credit insurance policy. Say during the Gulf War when the Suez Canal was closed, ships were diverted via the Cape of Good Hope giving rise to delays which can result in rejection of goods because of very late delivery. The cause of loss apparently is the diversion of voyage but this was caused by the Gulf War which is a risk covered under the Policy. Hence the proximate cause of loss is War and the claim is payable under the Policy unless war risks is excluded.

1.4 Subrogation

This principle applies to recoveries. When an insurance company pays a claim he steps into the "shoes" of the exporter (or insured) to have the right to pursue recovery from the buyer. This right in general principle of insurance law is enshrined under the law of subrogation. It is also a standard policy term.

Hence, when an exporter recovers any monies from his buyer after a claims payment, the exporter has to refund 85% or 90%, as the case may be, to the ECA (less any recovery expenses, of course).

1.5 Assignment

Assignment is the right of one party, in our case the exporter, to assign (or transfer in law)

his rights under the sales contract, to another party, the ECA.

Assignment is another principle that can apply to recoveries. If our exporter is insolvent or he is ineffective in collecting the debt and we wish to take over debt recovery then we will get him to assign the right to the debt to us for recovery action.

We do not require debt assignments as a matter of course after every claims payment because:

1.5.1 there may be problems in some jurisdiction in enforcing rights as an assignee.

1.5.2 the exporter may have a larger risk share than the ECA i.e. the uninsured risk portion is higher than the credit limit.

1.5.3 the exporter is the contractual party and is better able to enforce the debt especially if issues are raised on say quality.

2 Ascertainment of Loss

This is the date when the ECA will examine and assess the merits of the claim and recommend payment or rejection, as the case may be.

The following are the usual date(s) of ascertainment of loss:

| <u>Cause of Loss</u> | <u>Date of Ascertainment Loss</u> |
|----------------------|--|
| Insolvency | Immediately on receipt of acknowledgement of Liquidator, Receiver or Judicial Manager. |
| Default | 6 months after due (or extended) due date |
| Non-Acceptance | 1 month after resale of goods |
| Transfer | 4 months after deposit of local currency |
| Other Risks | 4 months after date of occurrence |
| Payment of claims | should follow soon after the ascertainment of loss. |

If there is a dispute the date for ascertainment of loss will be deferred until the dispute is resolved. Similarly if securities are required in the credit limit eg. a retention of title clause on the goods sold or third party guarantees, the exporter has to effect enforcement of the retention of title clause to repossess the goods and sell same or to enforce the guarantees and obtain judgment against the guarantors. Ascertainment of Loss will follow after such enforcement action.

3 Minimisation of Loss

This is another general insurance principle which has been incorporated as a term of our Policies.

The exporter is expected to minimise and not enhance his loss. Therefore, immediately on non-payment by the buyer the exporter should take steps to minimise loss.

Loss minimisation is most effective when such action is taken as soon as possible, preferably within 3 months after due date. Such loss minimisation action is important to

us as we have the larger interest in the outstandings but the exporter may also want to recover his profit element which is usually in his risk share.

Usually the exporter has a obligation to notify the ECA of any outstandings that remain unpaid 60 days after the due date but the exporter should commence working together with his ECA as soon as possible to effect collection of debt. I do not say recovery as no claim has been paid yet but as we may have an interest in the collection action if claim is payable it is in our interest to ensure as early as possible that the exporter takes the kind of steps to effect collection as we will require. Hence, the need to work as partners.

In loss minimisation it is important for us to recognise the early symptoms of probable loss. In ECICS we require the exporters to notify us of their ageing experience. Every month ECICS prints and sends to all exporters a Bills Maturity Report (BMR) which sets out all the invoices outstanding (as per his declarations). The exporter is required to indicate those bills which are paid on the BMR and return same to us. Our claims officer will then analyze the returns and follow-up on bills which are not paid or partially paid and determine cause of action for collection.

Some early signs of a probable loss are as follows:

- 3.1 partial/erratic payments
- 3.2 request (continuous requests) for extensions of due dates
- 3.3 requests for changes of payment terms ie. longer and longer credit terms
- 3.4 lack of response to payment demands.
- 3.5 slowing down of payments with pattern of excuses
- 3.6 abrupt or frequent change of banks
- 3.7 (increasing) claims, suits filed by suppliers etc.

Exporters should be persuaded to work with its ECA as soon as any of the above occurs as the earlier the collection action starts the better the prospects for a full recovery.

The following are some actions for minimisation of loss and better debt recovery for different heads of loss:

Insolvency

- Withhold shipments in transit
- Register debts with Liquidator/Receiver/Judicial Manager
- Obtain acknowledgment of debt
- Follow-up on dividend distribution

Default

- Issue letter of demand
- Protest for non-acceptance/non payment
- Debt collection agencies/legal action

Non-Acceptance

- Protest for non-acceptance/payment
- Arrange storage and insurance
- Arrange resale or reship goods
- Seek assistance of debt collector/legal action
- Request buyer to make local currency deposit on due date or as soon as possible
- Request buyer to comply with all exchanges formalities.

Others (including transfer delays)

- Liaison with relevant Government authorities in debtors' country eg Central
- Bank, Chamber of Commerce, local ECA or Ministry of Finance.

4 **Claims Processing or Claims Examination**

- 4.1 Claims Processing starts with the submission of Claims Form. From our experience at least 50% of claims or overdue notification do not result in claims. Therefore, until the exporter submits his claims form we do not process the overdue notification as a claim.

A specimen of our claims forms is attached. The claims form is a comprehensive documents setting out the details and data required.

The documents required for claims examination are as follows:

- 4.1.1 Sales contract and invoice
- 4.1.2 Bills of Lading
- 4.1.3 Bill of Exchange/promissory note
- 4.1.4 transport insurance document
- 4.1.5 packing list
- 4.1.6 surveyor's report
- 4.1.7 purchase orders
- 4.1.8 certificate of inspection
- 4.1.9 collection order/letter of credit
- 4.1.10 bank advice
- 4.1.11 protest notes
- 4.1.12 import licence (if applicable)
- 4.1.13 foreign exchange approval (if applicable)
- 4.1.14 bank confirmation of irrevocable deposit of local currency (for transfer claim)
- 4.1.15 all relevant correspondence

- 4.2 In claims examination we have to consider whether we also need:

- 4.2.1 communication with the buyer directly.

This is recommended for transactions of a dubious nature eg where there is a total failure under the policy ie. all exports declared have resulted in claims.

We experienced one such case where the transactions, were not genuine exports but mere indenting transactions with some "importers" who were licensed importers but were merely "lending" their licences to facilitate imports with no obligation to pay for the transactions. The licensed importers were paid a 3 per cent fee.

Direct communication is also useful when fraud is involved. In another case, all buyers contacted denied ever doing business with the exporter. The importers were well established companies whose names were used by the exporter to obtain credit limits. Thereafter, documents were drawn on such buyers for banks to discount bills of exchange which were accepted by the exporter's accomplices masquerading as the buyers' authorised signatories, in many instances forging signatures of the authorised signatories of the buyers.

4.2.2 Visit to buyers

This may be justified to verify above and confirm buyers' version of the transactions.

Usually in a fraud case there is no substitute for visiting the buyers concerned.

4.2.3 Application of Trade terms and terms of Payment

How will you deal with the following:

4.2.3.1 Documents against Payment on FOB terms

4.2.3.2 Documents against Payment on CIF terms

- 4.2.3.3 Documents against Acceptance on CIF terms
- 4.2.3.4 Open account on CIF terms

4.2.4 Visit to Country of buyer

For political risk claims eg transfer debt moratorium, it is inevitable that at least a visit is made to the authorities in the buyer's country. Such a visit will include appointments with senior officials of the Central Bank, Ministry of Finance and any other relevant ministries or Statutory Boards involved in the outstanding debts.

5 **Claims Payment**

- 5.1 The percentage of indemnity amongst ECAs vary between 75% to 95%. The latter for political risks.
- 5.2 The amount of loss will usually be the indemnity percentage, say 85%, of the relevant credit limit or outstandings, whichever is lower.
- 6.3 Payment of claim is sometimes made after setting off outstanding premiums, which are in arrears
- 6.4 Conditional claims payment can also be made where an ECA is of the opinion that a dispute raised by the buyer is frivolous.

6 **Recoveries**

- 6.1 Recoveries as stated above is and can be an essential part of an ECs operations.

One cannot pay claims and forget about recoveries. In ECICS we are of the view that recoveries have to be pursued aggressively until the delinquent buyer is made

bankrupt or wound-up or it does not make economic sense to pursue the recoveries.

6.2 Recoveries action in most case would have been commenced before claims payment. As stated above it makes sense to take legal or debt collection action as soon as the default occurs viz within 60 days after due date.

6.3 Our recovery approach in ECICS is as follows:

6.3.1 Debt recovery action will be taken under the exporter's names (ie. as per subrogation principles)

6.3.2 Reliance is made on the Berne Union list of debt collectors and lawyers, and on credit agencies advice on prospects of the recovery.

6.3.3 Reliance is also made on International Credit Insurance Association or members of factoring chain where applicable.

6.3.4 We ensure that all communications with debt collectors or lawyers are made directly with us and the exporter. We also have the right to give lawyers or debt collectors instructions.

This should be the case as we are bearing the bulk of the recovery expenses especially after payment of claim.

Instructions are usually made by the exporter to channel all recoveries (net of expenses) to ECICS directly.

We will then apportion such recoveries (less expenses) in accordance with the risk share between us and the exporter.

- 6.3.5 In cases where the exporter has overtraded or outstandings exceeded the credit limit, recovery action will usually include such excess portion. Recoveries (and expenses) will then be shared as stated above, in accordance with the relevant risk shares.

In the event the exporter's excess portion might undermine the recoveries under the insured portion, ECICS has the right and which we will exercise, to direct the exporter to assign the insured portion to ECICS for direct recovery action. This could be done easily where bills of exchange or equivalent negotiable instruments are available.

- 6.3.6 For non-commercial or political causes of loss it is usual for ECA to take over all recovery action as such recovery action will involve direct negotiation with relevant authorities in the buyer's country and can result in Paris Club type recovery terms. Although Paris Club involves usually medium and long term debts, there are occasions when the debtor country will include all outstandings, short, medium and long term debts for rescheduling under the Paris Club terms.

We had such an experience for outstandings in Nigeria.

7 **Conclusion**

It can, therefore, be seen that claims and recoveries are important part of export credit insurance operations and in a service industry if we have an understanding claims philosophy and an effective recovery team, our consumers, the exporters, will also be given a competitive edge in the global market place. The former will help the exporters to ease and improve their cash-flows when their buyers default and the latter will enable them to have a comparatively high recovery ratio which usually means better profit margins as the exporters' risk retention is usually their profit element in the contract price.

ECICS LTD

A member of The ECICS Group

CLAIMS FORM

Note: The issue and completion of this Claims Form do not infer an admission of liability on the part of the Corporation.

Policy No:

Date of Issue:

Exporter's Name

Buyer's Name & Address

Loss Sustained (\$\$)

Date of event which caused loss or

Final Due Date(s) for Payment

We hereby declare that we have sustained this loss in connection with a contract with/exportation to the abovementioned buyer.

The loss was caused by (Tick where applicable)

- | | | | |
|----|---|--|---|
| 1. | INSOLVENCY OF BUYER | | Buyer became insolvent as defined in paragraphof our Policy. |
| 2. | ACCOUNTS SIX MONTHS OVERDUE | | |
| 3. | FAILURE OF A BUYER TO ACCEPT GOODS EXPORTED | | Through no breach of condition or warranty on our part or other causes within our control. |
| 4. | EXCHANGE TRANSFER DELAY | | The transfer of foreign exchange funds fromto Singapore has been delayed bymatters. |
| 5. | OTHER CAUSES OF LOSS | | As specified under paragraphof the Policy. |

PART I

(a) We hold a Credit Limit approved by the Corporation under paragraph of the Policy and details of which are:-

Amount S\$Terms of Payment Dated

Conditions:

- (b) We are operating under the terms of a discretionary limit of allowed under schedule 1 to the Policy.
- (c) Our Contract Limit (where applicable) was set at S\$.....(amount)

PART II

The transaction(s) for which premium has been paid forming the subject of this claim is/are set out hereunder:-

| DECLARED AS CONTRACTS (Contracts Policy Only) | | | | DECLARED AS SHIPMENTS (Contracts and Shipments Policy) | | | |
|--|------------------|----------------------|--------------|---|------------------|---------------------------|--------------|
| Actual Date Declared | Date Of Contract | Contract Value (S\$) | Premium Paid | Actual Date Declared | Date Of Shipment | Gross Invoice Value (S\$) | Premium Paid |
| | | | | | | | |

Conversion rate used to convert Foreign Currency to Singapore Dollars for Declaration Purposes as based on the relevant published nominal interbank closing rate of exchange was

NOTE: If the transaction(s) subject of this claim was (were) only part of the amount(s) declared on the particular country and terms of payment in the declarations) referred to above, then the Exporter must show on Part VII the details of other contracts/shipments included in the total amount so declared.

If the claim or any part of it is in respect of goods not yet exported, the following declaration must be completed (see of Comprehensive Policy (Contracts) only).

We enclose our cheque for S\$..... which we declare to be the premium due in respect of unexported contracts or portions thereof forming the subject of this claim. Details of the premium enclosed are:-

| CONTRACT VALUE | RATE OF PREMIUM | PREMIUM PAYABLE |
|----------------|-----------------|-----------------|
| | | |

| | | |
|--|--|--|
| | | |
|--|--|--|

PART III

We attach the following documents, where applicable, in support of the claim:-

- (a) The original or certified copy of evidence of insolvency/and official Receivers/Managers acknowledgement of debt
 - (b) Original or certified copies of relevant correspondence with the buyer and our agent.
 - (c) Original or certified copies of the contract(s) of sale and/or buyer's orders and our confirmation thereof.
 - (d) Certified copies of invoices.
 - (e) Certified copies of bills of lading, air-way bills, partial receipts or equivalent evidence of exportation.
 - (f) Originals of any unpaid bills of exchange, promissory notes (if held).
 - (g) Bank discount slips (if covering draft negotiated) and bank advices of dishonour or nonpayment. (If the Exporter was operating under a discretionary limit, the following additional documents are required)
 - (h) Certified statement of buyer's account to date, commencing two y-ears prior to the transactions forming the basis of the claim.
 - (i) Original information on which the creditworthiness of the buyer was assessed. (In case of Exchange Transfer Delay and Cancellation of Import Licence cover, the following additional documents are required)
 - (j) Evidence that the buyer
 - (i) held a valid Import Licence, if required, covering the subject shipment and/or
 - (ii) held, if required, a prior exchange permit or its equivalent necessary to obtain authority to transfer payment to Singapore.
- (In case of Exchange Transfer Delay, the following additional documents are required)
- (k) Evidence from the collection instating.
 - (i) the due date of payment in respect of the shipment,

- (ii) that the buyer has made a irrevocable deposit in Currency to the full equivalent of the gross invoice value.
- (l) If no irrevocable deposit has been made by the buyer as per (k) then evidence is required from the collection bank in that the buyer is precluded by the laws or regulations in from lodging such irrevocable deposit.

PART IV

The loss is calculated as follows:-

(1) **Goods Delivered**

| | | | | | |
|--|----|----|----|----|-------------------|
| Contract Value or Gross Invoice Value | .. | .. | .. | .. | S\$ |
| Less (a) Amount already received.. | .. | .. | .. | .. | S\$ |
| (b) Sums or credits in our possession and available to the buyer or to us in the reduction of the debt | .. | .. | .. | .. | S\$ |
| (c) Sums saved by the non-payment of agent's commission | | | | | S\$ |
| (d) Any other sums recovered | .. | .. | .. | .. | S\$_____ S\$_____ |
| | | | | | S\$_____ |

(2) **Goods Not Delivered**

| | | | | | |
|---|----|----|----|----|-------------------|
| Contract Value or Gross Invoice Value | .. | .. | .. | .. | S\$ |
| Less (a) Amount already received | .. | .. | .. | .. | S\$ |
| (b) Amounts saved (if any) by non-fulfillment of contract | .. | .. | .. | .. | S\$ |
| CIF charges .. | .. | .. | .. | .. | S\$ |
| Agent's commission .. | .. | .. | .. | .. | S\$ |
| Manufacturing costs, etc. | .. | .. | .. | .. | S\$ |
| Packing costs | .. | .. | .. | .. | S\$ |
| Bank charges | .. | .. | .. | .. | S\$ |
| Interest | .. | .. | .. | .. | S\$ |
| Any other expenses saved | .. | .. | .. | .. | S\$ |
| (c) Any sums recovered by: | | | | | |
| Resale of goods | .. | .. | .. | .. | S\$ |
| Return of goods to stock | .. | .. | .. | .. | S\$ |
| Sale of materials pertaining to the contract | .. | .. | .. | .. | S\$_____ S\$_____ |
| Plus Resale Expenses (List full details) | .. | .. | .. | .. | S\$_____ |

Loss goods not delivered

S\$_____

TOTAL LOSS ON GOODS DELIVERED AND/OR NOT DELIVERED

S\$_____

PART V

(a) Name and address of your local agent (if any)

.....

(b) Description of goods

.....

(c) Where produced or manufactured

.....

(d) Present whereabouts of Bills of Exchange or Promissory Notes

* (e) Whether notice of dishonour (or letter of demand) made

* (f) Whether protested for non-payment on default

(g) Dates on which outstanding items were first declared to the Corporation as overdue

(h) Has there been any dispute or complaint or is there any dispute or complaint still outstanding and unsettled:-

(i) regarding the amount of the debt or any portion thereof?

(ii) regarding the goods supplied?

(iii) regarding the terms of the contract?

(iv) Regarding delivery dates?

(v) On any other ground?

NOTE: If answer to any part of this question is "Yes", please supply full details of the dispute or complaint, the action

(if any) taken by you to refute the buyer's allegations, and copies of all correspondence relating to the dispute

or complaint.

*If answers are "Yes", copies of relevant documents to be attached.

PART VI - POLICYHOLDER'S DECLARATION

NOTE: Discounting and similar operations through Banks and Accepting Houses including the endorsement of any Bills of Exchange and Promissory Notes relating to the contract will normally constitute any assignment or charge of the type referred to in Paragraph 7 of the Insurance Policy. The name of the persons to whom such an assignment or charge has or may have been made should be inserted in the space provided in (d) below. An incorrect declaration might have- serious consequences.

WE DECLARE THAT:

- (a) We have sustained a loss, particulars of which are as stated;
- (b) We have not entered into any contract of Insurance or indemnity in respect of the loss claimed and that except as already disclosed to you we hold no sums, credits, security or indemnity against this amount and that we have no claim:3 against our agents in respect of del credere risks assumed by them;
- (c) We have not assigned or charged any part of the benefits under our insurance policy to which the loss claimed relates or any right or interest acquired by virtue thereof and have not received any security in respect thereof;
- (d) We give below the name and address of each person in whose favour we have assigned or charged any part of the amount owing under each contract to which the loss claim relates or any right or interest acquired by virtue thereof or from whom any security in respect thereof has been received.
.....
.....
- (e) We are in a position to take all steps which the Insurer may require at any time to effect recoveries after payment of claim;
- (f) We understand that any payment which may be made to us or to a third party in settlement of this claim is made subject to the terms and conditions of the Insurance Policy and of the Proposal thereof;
We accordingly claim payment of the amount shown in Part IV of this claim form. The draft in settlement should be made payable to
.....

*Signature

On behalf of

Dated

In the presence of

*To be signed- in the case of partnership by a partner or in the case of incorporated companies by an authoi-ised officer stating the capacity in which he acts.

Claims - Case Studies

Topman Ltd. (Topman) reported to the insurer on 13 Dec. 1996 that a shipment for USD17,000 made on 8 Oct. 1996 to one of its buyers in the U.S.A. was overdue. Topman sold coffee decanters to the buyer since 1985. All the goods were shipped and consigned to the buyer. The detailed outstanding position was as follows

| | Gross Invoice Value USD | HKD Equivalent | Shipment Date | Terms of Payment | Due Date |
|-----|----------------------------|----------------|------------------|---------------------|-------------|
| (a) | 17,000 | 128,000 | 8 Oct 1996 | OA 30 days | 7 Nov 1996 |
| (b) | 14,000 | 106,000 | 31 Oct 1996 | OA 60 days | 30 Dec 1996 |
| (c) | 17,000 | 128,000 | 9 Nov 1996 | OA 60 days | 8 Jan 1997 |
| (d) | 38,000 | 294,000 | 9 Nov 1996 | OA 60 days | 18 Jan 1997 |
| (e) | 17,000 | 129,000 | 8 Dec 1996 | OA 60 days | 7 Feb 1997 |
| | 103,000 | 785,000 | | | |

The credit limit issued by the insurer was for HKD600,000 OA 60 days.

1. On 24 Dec. 1996, the buyer filed a petition for reorganisation under Chapter 11 of the U.S. Bankruptcy code.
2. On 3 Jan. 1997, the buyer proposed to Topman that if Topman agreed to continue to trade on credit terms, it would be paid a deposit of 100cents on the dollar for all undisputed claims for goods delivered before 25 Dec. 1996. Topman approached the insurer for approval whether or not it should accede to the buyer's request. Topman indicated that it would agree to the buyer's request for continued supply on credit terms only if the insurer agreed to provide the cover.
3. On 22 Jan. 1997, the Bankruptcy Court provided Topman a Proof of Claim Form with a pre-printed scheduled amount of USD48,000. Topman immediately notified Bankruptcy

Court that the correct amount of outstanding debt should be USD103,000. Meanwhile, Topman asked the insurer to settle its claim on the outstanding shipments under the insolvency event of loss.

Questions for discussion

1. Please consider whether or not the insurer should agree to Topman's request for cover on new shipments on credit terms to the buyer in return for the settlement of the old debt. Please state your reasons.
2. What measures would the insurer take in order to demonstrate that the insured has properly executed the sales contracts by delivering the goods to the buyer?
3. What would the insurer require from Topman before a claim payment on the outstanding shipments could be considered?

Case Study 2

Claims

Toy Company Limited reported to HKECIC on 10 August 1997 that one of their buyers in the United States did not settle the following shipment of plastic toys:

| Gross Invoice Value | Date of Shipment | Terms of Payment | Due Date |
|---------------------|------------------|------------------|--------------|
| USD 120,000 | 10 April 1997 | DA 30 | 12 June 1997 |

The credit limit approved by HKECIC was USD100,000 DA 30 days.

From documents submitted by the policyholder, no specific reasons for non-payment could be found neither was there evidence showing any disputes between the buyer and the policyholder. Hence, a debt-collector was recommended to Toy Company Limited to pursue payment from the buyer.

From copies of correspondence exchanged between Toy Company Ltd. and the debt collector, it was noticed that the total amount of debt that the debt collector was pursuing was USD200,000 instead of USD120,000. The Claims Officer therefore, asked Toy Company Ltd. to explain why a smaller amount was declared. Toy Company explained in writing that there was only one shipment for USD120,000 and the amount of USD200,000 was wrongly stated in the letter to the debt-collector.

Upon checking with the debt collector, HKECIC was advised that, in fact, two shipments amounting to USD200,000 were outstanding and the other shipment for USD80,000 was effected on 23 May 1997 which was not declared to HKECIC.

Further explanation was sought from Toy Company who then admitted that the shipment for USD80,000 was an omission and that it was a mistake made by one of their clerks who had already resigned.

To have a better understanding of the case, a meeting among the managing director of Toy Company and HKECIC was held. The managing director then alleged that:

- a) they were not aware of the whole insurable turnover requirement;
- b) they assumed that any amount in excess of the approved credit limit on the buyer should be for their own account and should not be declared;

In going through the file, it was noticed that:

- a) Toy company was a leading firm in the trade of toys and the turnover in 1996 was over USD20 million but over 90% of which was local sales,
- b) no declaration of exports have been made to HKECIC since May 1997,
- c) whilst it is not known whether Toy Company had declared all insurable shipments as they should, there is no record showing previous omissions.

QUESTIONS FOR DISCUSSION

Question 1

As a claims officer, please advise whether you accept the reasons given by Toy Company Ltd. for the omission and why?

Question 2

Will you accept the liability for the shipment of USD120,000 declared and ascertain Toy Company Ltd's loss? (Assuming that other terms and conditions have been complied with.) Please state your reasons.

Question 3

What would you require from Toy Company to satisfy yourself that there is no other omission ?

Recoveries

Policyholder: Hong Kong Company Limited
Buyer: Toys Corporation, USA

Background

1. A credit limit of \$1,800,000 DA120 days was issued on the buyer to the policyholder (PH).
2. PH joined us in 1982 and has more than 20 years trading experience with the buyer. The buyer was the major buyer under the Policy.
3. In early January 1997, PH reported that 25 DA120 days shipments totalling \$5,300,000 remained unpaid.
4. PH placed the case to a debt-collector in March 1997. Claims payment of \$1,620,000 (90 % of credit limit) was made in early April 1997.
5. After claim payment, PH received a letter from the buyer (attached) requesting the PH's support.

Questions for discussion

- Q1. Should PH sign the letter? What relevant points should be addressed
- Q2. Please consider the course of actions to be taken to pursue recovery of the outstanding debt.

Letter received from the buyer

10 April 1997

Dear Frank,

We are negotiating with a new bank and it will help our negotiation if you will accept to put the contents of the enclosed letter on Hong Kong Company Limited letterhead to prove that you are in agreement with our decision rest assured we are only doing this as a technicality and whatever the name of the new corporation is to both Peter and John, guarantee your account to the last dollar plus interest.

Now let me explain to you why we are doing this. Basically, we are heavily over inventoried in some items which I feel will bring the closing figures of 1996 to a point where inventory might be considered by our bankers too high in relationship to the volume of Toys Corporation. Therefore, we are being advised by our bank to move some inventory to a new corporation and have the new corporation hold the debt to our overseas supplier which in this respect are none about you.

This will enable Toys Corporation to show a much lower inventory which will enable us to secure financing and hopefully in June 1997, we will be able to bring this nightmare to a close and restore your confidence in us and at the same time restore the confidence of your bankers.

Sincerely,
(signed)
Peter Green

Promissory Note

We attest that both Peter Green and John Green are responsible as officers of Toys Corporation and corporation they spin off to the debt due to Hong Kong Company Limited.

(signed)

Peter Green

(signed)

John Green

Case Study - Recovery

To Whom It May Concern:

I understand that the officers of Toys Corporation, John Green and Peter Green in their discussion with their accountants are now contemplating to spin off a new corporation which will be responsible for the debt to us.

This debt that the new corporation will assume will be more than covered by inventory passed on from Toys Corporation. Whatever decision Toys Corporation undertake, we fully support and we are in full agreement with.

We know Peter the Greens for a very long time and our trust in them is absolute.

Frank Chan

Recoveries

Garment Company Limited made the following shipment of ladies garments to the buyer AAA Co. in the United Kingdom:

| Gross Invoice value | Date of shipment | Terms of payment | Due Date |
|---------------------|------------------|------------------|------------|
| USD500,000 | 10 Sept 1996 | DA90 | 6 Jan 1997 |

The bill of exchange was drawn on the buyer, AAA Co. (a sole proprietor) and was duly accepted. However, the bill of exchange was dishonoured on the due date without any reason for default.

Garment Company had obtained a personal unconditional guarantee from the Managing Director, Mr. A of AAA Co. for USD100,000 as well as a Corporate guarantee from AAA Holdings Ltd. in the United Kingdom, which was a holding company purportedly owned by Mr. A.

The bill of exchange was protested and a claim was paid to Garment Company Ltd.

Please discuss the course of actions to be taken to pursue recovery of the outstanding debt.

SECTION 10

PROMOTING AND MARKETING TRADE INSURANCE

**CHAPTER I ENHANCING INTERNATIONAL TRADE THROUGH
TRADE INSURANCE**

**CHAPTER II MARKETING PLAN, IMPLEMENTATION AND
EVALUATION**

**CHAPTER III MARKETING TECHNIQUES AND HKEC'S IN
MARKING**

CHAPTER IV A NORTH AMERICAN APPROACH

**CHAPTER V PROMOTING AND MARKETING TRADE
INSURANCE - THE MALAYSIAN APPROACH
(SYNOPSIS)**

CHAPTER I

ENHANCING INTERNATIONAL TRADE THROUGH TRADE INSURANCE

Introduction

1. While Irrevocable Letter of Credit (ILC) is the most wanted term of payment in international trade, the offering, of credit is becoming more common as international trade is getting more competitive.
2. If an exporter does not know the buyer well, it is not prepared to extend credit for fear of not getting the money back. It will not accept the orders which will then go elsewhere or, worse still, to an exporter in another country.
3. Export credit insurance assesses the buyer's creditworthiness, monitors the credit risks involved, assists in chasing overdue and compensates the exporter. It also helps obtain export finances. It places top exporters in a very good position to offer flexible payment terms and capture more orders. It, therefore, enhances the exporters' competitiveness in international trade.

Expansion of overseas business

4. Information is vital in assessing credit risks. Exporters, particularly the small ones, usually do not have the resources. A credit insurer has:
 - (a) an international network of credit information agencies;

- (b) an independent team of risk analysts;
- (c) an international network of debt collectors.

It, therefore, possesses the resources and skills to do an impartial and professional risk assessment job.

5. With this assistance and protection, exporters can prudently extend Credit and capture more orders.

Credit Management role

6. A credit insurer is acting more like a professional credit manager than an insurer. On behalf of the exporters, it assesses and monitors risks and assists in chasing overdues. This saves exporters' resources, takes away most of their worries and enables them to concentrate on trading.

Additional Working Capital

7. Working capital is much needed by exporters, particularly the small ones. In Hong Kong, export credit insurance is taken by banks as a valuable collateral for export financing. Over 60 % of the insured use it to obtain financing.

8. There are three kinds of assignments

- (a) whole policy;
- (b) specific countries; and
- (c) specific buyers.

Loss Minimization

9. Through its years of debt collection experience and with its global network of debt collectors, the credit insurer can help exporters chase overdue debts. This will help minimize monetary loss and recoup working capital.

Supplier credit

If export credit insurance can be arranged by an overseas supplier, an importer in China is no longer required to open ILC. More supplier credit can be obtained through this means. Exporters, acting as intermediaries, can win more orders.

CHAPTER II

MARKETING PLAN, IMPLEMENTATION AND EVALUATION

1. Introduction

Alice: "Would you tell me, please, which way I ought to go from here?"

Cat: "That depends a good deal on where you want to get to."

Alice: "I don't much care where."

Cat: "Then it doesn't matter which way you go."

Alice: " So long as I get somewhere."

Cat: " Oh, you're sure to do that if you only walk long enough."

Lewis Carroll - Alice's Adventures in Wonderland.

Unlike Alice, marketing planners must know where they want to get to in order to deploy limited resources and employ the best efforts for the most profitable results. The road that a business chooses to travel in the future cannot materialize from wishful thinking, but will result from objective, knowledgeable, and well-organized judgements about the futurity of its current decisions.

2. Peter Drucker sums up:

"The future will not just happen if one wishes hard enough. It requires decisions - now. It imposes risk - now. It requires action - now. It demands allocation of resources, and above all, of human resources - now. It requires work - now."

Marketing

3. Marketing is about which way to go and how to get there. It has become an important part of business and yet it is extremely difficult to define exactly what it is. There are many ways to define marketing.

4. Marketing, as defined by the American Marketing Association's Board of Directors, is:

"The process of planning and executing the conception, pricing, promotion, and distribution of ideas, goods and services to create exchanges that satisfy individual and organizational objectives."

5. Philip Kotler, in his book entitled "Marketing Management: Analysis, Planning and Control", defines marketing, as the social process by which individuals and groups obtain what they need and want through creating and exchanging, products and value with others."
6. Hugh Davidson, in his book "Offensive Marketing or How to make your Competitors Follow", says: "Marketing, is the process of balancing the company needs for profit against the benefits required by consumers, so as to maximize long-term earnings per share" and "Marketing, is a philosophy and a method of achieving corporate financial objectives."

Strategic planning

7. Planning does not ensure successful performance, but it provides disciplined appraisal, goal setting, and action steps to maximize success. It is a predetermined application of resources for their most profitable use. A marketing plan is an organized thought process and communication system.
8. Strategic planning is vital to steer a company on course. It enables a company to gain a competitive edge by strategically positioning the company in the right markets at the right time, securing rapid and profitable growth during good times or survival in bad times until you can catch the next upswing in the business cycle. Strategic planning is the best vehicle you have to get where you want to go. It gives you a clear vision and direction.
9. Some managers wonder what the difference is between a strategic plan and a business plan. The easiest way to distinguish one from the other is to think of one as general (the strategic plan) and the other specific (the business plan). The strategic plan deals with the whole company

while the business plan deals with detailed implementation of one specific aspect of the strategic plan.

10. A strategic plan is concerned with the entire company: what it produces, where it competes and how it allocates resources. It deals with fundamental choices that will affect the entire organization - choices about the future.
11. Business plans are concerned with the details of implementation after the big strategic choices are made: you first need to decide where you want to go and how you are going to get there. Business plans, therefore, are involved in the last stage of strategic planning: the implementation process.

Implementation

12. A plan is nothing, unless it translates into work. Implementation is the most important part of the whole planning process. There is no point in going through all the effort to create a vision, establish objectives, set goals and devise strategies if you fail to implement the corporate plan inside your company. If the plan is not successfully implemented most of the preparatory work will have been wasted.
13. PA Consultants estimated that over 95 per cent of all strategies designed in the late 1970s and early 1980s were never fully or effectively implemented.
14. Corporate culture is "the way people do things around here". It is a source of motivation and demotivation, of satisfaction and dissatisfaction. It can be a positive tool for competitive advantage or a barrier to change. It is important to develop a clear, positive corporate culture.
15. There are five competing concepts in conducting marketing activities:
 - (a) Production concept

The production concept holds that consumers will favour those products that are widely available and low in cost. Management in production-oriented organizations concentrates on achieving high production efficiency and wide distribution coverage.

(b) Product concept

The product concept holds that consumers will favour those products that offer the most quality, performance and features. Management in these product-oriented organizations focus their energy on making good products and improving them over time.

(c) Selling concept

The selling concept holds that consumers, if left alone, will ordinarily not buy enough of the organization's products. The organization must therefore undertake an aggressive selling and promotion effort.

(d) Marketing concept

The marketing concept holds that the key to achieving organizational goals consists in determining the needs and wants of target markets and delivering the desired satisfaction more effectively and efficiently than competitors.

(e) Social marketing concept

The social marketing concept holds that the organization's task is to determine the needs, wants, and interests of target markets and to deliver the desired satisfactions more effectively and efficiently than competitors in a way that preserves or enhances the consumer's and the society's well-being.

16. Export credit insurance is not simply a tool for protection. It provides a comprehensive range of credit management services. Good customer service is of paramount importance.

17. Implementation is the process to convert strategies into realities. It is said to be the sternest test of management's ability to lead and manage. It involves the following important elements:

1. Leadership
2. Communications
3. Action plans
4. Budget
5. Timetables
6. Reviews

Feedback loop

18. Information is important in ensuring the implementation process is on track and, where necessary, appropriate corrective actions are taken. The feedback loop of channelling external reactions and responses to the company is necessary in the implementation and evaluation procedures. Marketing staff should look out for and even ask for feedback on the company's performance. Critical comments provide opportunities to improve performance.
19. Ten most frequently encountered problems in implementation are:
- (a) Implementation took more time than originally allocated
 - (b) Major problems surfaced which were not identified beforehand
 - (c) Coordination of activities were not effective enough
 - (d) Competing, activities and crises distracted attention
 - (e) Employee capabilities were insufficient
 - (f) Inadequate training and instruction for employees
 - (g) Uncontrollable external factors
 - (h) Inadequate leadership and direction by department managers
 - (i) Key tasks and activities were not defined in enough detail
 - G) Inadequate information systems for monitoring
20. Three main reasons for failures in implementation of marketing plan:
- (a) the company failed to set objectives correctly
 - (b) the company failed to modify objectives in the light of changing experience; and
 - (c) the company failed to execute the necessary actions

Control

21. Three types of marketing control:

- (a) Annual-plan control
- (b) Profitability control
- (c) Strategic control

22. Annual plan control is the task of making sure that the company is achieving the sales, profits and other goals that it has established in the annual marketing plan:

- (a) setting, well-defined goals for each month, quarter or other accounting period;
- (b) measuring its on-going performance;
- (c) determining the underlying causes of any serious gaps in performance;
- (d) deciding on the best corrective action to take to close the gaps between goals and performance.

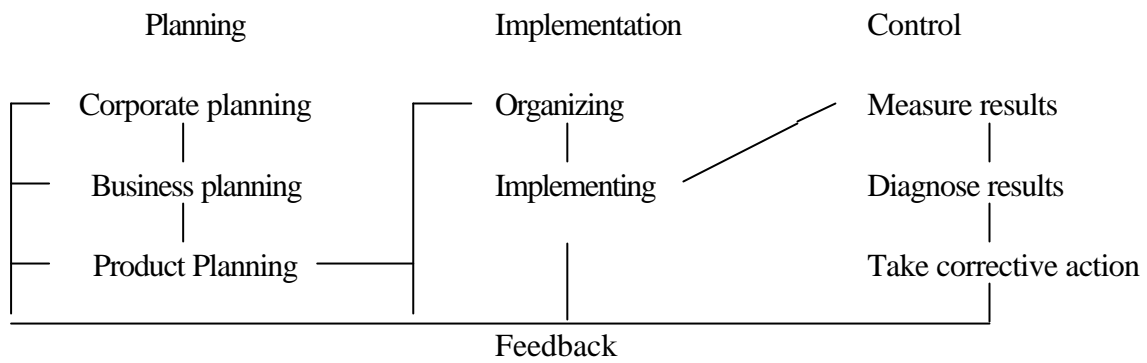
23. Companies also need to analyze periodically the actual profitability of their different insurance facilities. Marketing profitability analysis can be used to measure the profitability of different marketing activities. Marketing efficiency studies might also be undertaken to show how various marketing activities could be carried on more efficiently.

24. From time to time, the company must stand back and critically examine its overall marketing plan and decide whether it continues to make good strategic sense. Marketing, is one of the major areas where repaid obsolescence of objectives, policies, strategies and programs is a common possibility.

25. Through these systems, the company monitors and adapts to the marketing environment. The company takes the factors and forces in the marketing environment into account in developing strategy and positioning itself strategically in the target market.

Strategic planning process

27. The whole planning implementation and control process is:



CHAPTER III

MARKETING TECHNIQUES AND HKEC'S EXPERIENCE IN MARKETING

Market experience in Hong Kong

For an export credit insurer, the total size of the market is the volume of exports that is conducted on credit terms. But there is non-insurable business (e.g. in-house transactions). No official statistics are available to provide an accurate estimate. Survey methods may be used to segment markets and estimate likely demand. The potential markets are those not yet insured and appropriate marketing techniques should be used to tap individual market segments.

2. A commercial credit insurer's goal is to transact profitably in target markets. Official credit insurers may have a different goal, e.g., to support export trade. The company's mission and corporate goal will affect the way it operates in the market.
3. Credit insurance is not monopolistic. Competition may come from:
 - (a) Self insurance;
 - (b) Banks who do not insist on protection;
 - (c) Factoring companies;
 - (d) Foreign insurers through insurance brokers;
 - (e) Local providers - local insurers and local branches of foreign credit insurers.

However, competition in Hong Kong is not particularly fierce from (c), (d) and

(e). Focus is on convincing exporters and/or banks to insure.

4. There are over 180 banks in Hong Kong. They are active in trade and project financing. The banking industry in Hong Kong is indeed very competitive. Many banks no longer insist on full security, and are prepared to accept financing on less secured terms. They increasingly are

accepting HKEC's policy as a valuable collateral security in trade financing. Over 60% of HKEC's insured business adopts this form of security to obtain financing. More business can be tapped through banks.

5. The basis of insurance affects business acquisition. Whole insurable turnover requirement has met with growing resistance. Some exporters will walk away if this concept is rigidly held. More business is possible if:

- (a) Whole insurable concept is not insisted upon
- (b) Flexible terms of cover are offered
- (c) Tailor-made cover is made for large exporters

6. Public awareness of the values of export credit insurance is important to business acquisition. Continuous publicity and promotion are necessary to enhance corporate image and obtain business from potential customers. Though public relations activities are costly, sufficient resources must be allocated.

7. Exporters may have different needs for insurance:

- (a) Protection
- (b) Credit advisory service
- (c) Expansion of export trade
- (d) Debt collection advisory service

An analysis of the needs will enable a company to formulate its market segmentation and targeting strategy-

HKEC's marketing mix

- (a) **Insurance facilities**

8. While the basic insurance facility is offered to the general public, tailor-made cover or flexible cover should readily be extended to certain target groups which:

- (i) insure substantial volume of business.
- (ii) insure a portfolio of good spread of risks; and
- (iii) have a good track record;

Tailor-made cover includes single risk cover and flexible cover includes cover with rebate, no claim bonus, long term contract etc.

(b) Pricing

9. If an exporter seeks cover, it accepts a reasonable level of premium cost. Pricing, however, becomes a crucial element when the exporter loses interest in the cover (through dissatisfaction in the quality of service or the scope of cover or when there are competitors; flexible pricing policy should then be implemented.

(c) Public relations

10. Public relations expenditure is the third largest expenditure item in HKEC, after salaries and credit information. It takes up slightly over 5% of the total operating expenses. The following media are used:

- (a) Leading, newspapers and magazines;
- (b) Roadshows;
- (c) Radio;
- (d) MTR train and stations;
- (e) Direct mailing; and Telephone marketing.

In addition, over 60 seminars are conducted every year.

(d) Distribution channel

11. HKEC relies on its direct sales force to get new business and retain customers.

12. HKEC is now employing a professional broker to market its products. The result is not good. Brokers may be more actively used if competitors are using them.

CHAPTER IV

A NORTH AMERICAN APPROACH

1. MARKETING RESEARCH

Customer Research

- Customer Satisfaction
- Lead Generation
- Lost Account Research

Communications Research

- Advertising Testing and Tracking
- Let's Talk Risk Workshops

Internal Research

- Product Research
- Employee Satisfaction
- Corporate Imaging / Familiarity

Product Development Research

- SME Financing Products
- SME Working Capital

2. ADVERTISING AND DIRECT MARKETING

Advertising & Promotion Objectives

- Set measurable performance objectives:
 - Response rates based on inquiries from 800 lines, reader reply cards, Internet web site
 - Sales conversion rates
 - EDC awareness levels among prospect audiences
 - Recall levels of EDC ads.

Trade Shows

- "Participation" takes many forms:
 - Limited attendance
 - Staffed booth
 - Looping computer presentations
 - Speaking engagements
 - Pre-show delegate letters
 - Post-show delegate follow-up
 - Event sponsorship
- EDC is participating in 17 trade shows this year

Associations

Among EDC's target sectors, 35 industry associations have been identified and are being contacted for a variety of marketing activities:

- Membership lists for direct marketing and lead generation
- Association publications and newsletters for advertising and editorial opportunities
- Events, conferences, trade shows that may warrant some form of involvement
- Key industry contacts

Challenges and Opportunities

- Every year, one in four SMEs go out of business, making awareness building difficult
- The 'decision-maker' who buys the EDC product is either an owner or a financial specialist, rendering vertical advertising ineffective
- Many companies still don't know EDC
- No brand equity in "EDC", corporate signature is confusing

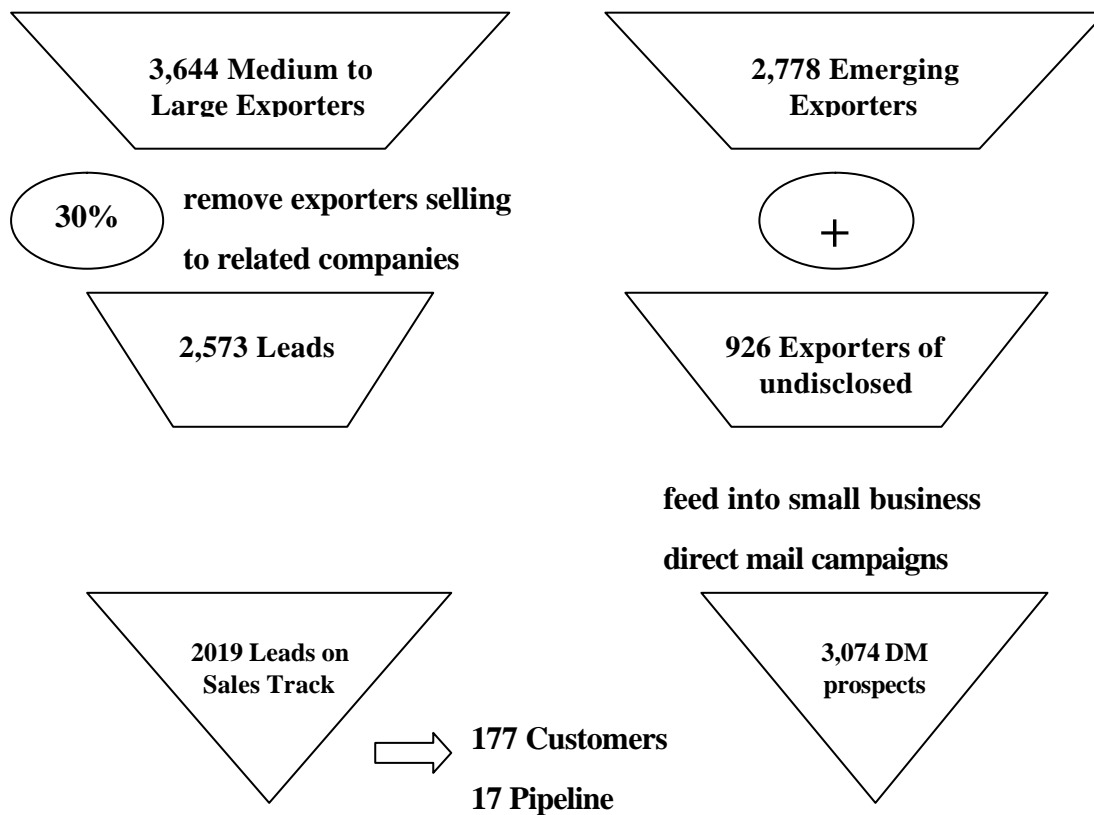
3. EDC MARKETING PROGRAM

Lead Generation Survey - Key Questions:

- Export and total sales
- % of exports to unrelated buyers
- familiarity with EDC
- primary product or service
- likelihood to use credit insurance
- likelihood to invest in developing countries
- export markets of interest

Results - Leads Generated 1996 & 1997 to date

7,348 interviews with Canadian Exporters



Converting Leads into Sales

- Not all follow-ups will result in new business - expect a conversion rate of 10-20%
- Conversion times (after follow-up) range from one day to two years - plan to reschedule many calls

Cost / Benefits of Generating Leads

| | <u>1996</u> | <u>1997</u> |
|---------------|-------------|-------------|
| Cost per Lead | \$30 | \$18 |
| Cost per Sale | \$1,108 | \$1,310 |

- Increased awareness of EDC among exporters, improved EDC knowledge of awareness levels
- Enrichment of Sales Trak with complete contact, product and sales information
- Development of a comprehensive exporter database, generation of mailing lists for Teams

Lead Generation - Quality Control

- Re-interviewing leads not followed-up within the last year
- Set team and BDM targets for lead follow-up rates, conversions
- Acquire more targeted lists of exporters
- Focus business development effort on top tier of prospects

4. Selling Through Brokers

What is a Specialist Broker?

- Experience with export credit insurance covering exposure both within and beyond the North American arena
- Knowledge of technical and legal requirements for trading goods in foreign countries
- Exposures to and understanding of Policy documentation such that assistance and guidance can be provided to a prospective insured with respect to product comparisons
- Knowledge across a broad range of industries such that a potential insured's business requirements are understood and can be fully explained to EDC

Direct Selling vs Selling Through Brokers

- Cost effectiveness
- Product understanding
- Relationship with customers
- Access to certain (larger) potential customers

5. Selling Export Insurance to and via Banks

Role of the Bank

- Provide exporter with access to working capital
- Confirm / negotiate / accept / pay documentary credits

Recent New "Products"

- Master Accounts Receivable Guarantee (MARG) - for small exporters, provides Banks with a guarantee on loans against receivables
- Grow Export Program - joint working capital guarantee program with Canadian Imperial Bank of Commerce for small high-tech companies
- Norhtstar Trade Finance - short-term policy tailored to cover medium-term credits (up to 5 years)

- Medium-Term Documentary Credits Policy - broadened short-term DC policy to cover medium-term LC's (up to 5 years)
- Bank Aval Policy - policy in development to cover Canadian banks on foreign bank avals rather than Letters of Credit

CHAPTER V

SYNOPSIS

PROMOTING AND MARKETING TRADE INSURANCE **- THE MALAYSIAN APPROACH**

Difference Between Selling and Marketing Concept

Selling Concept

- Emphasis is on the product
- Company first makes the product and then figures out how to sell it
- Management is sales-volume oriented
- Planning is short run oriented in terms of today's products and markets
- Stresses needs of seller

Marketing Concept

- Emphasis is on the customers' wants
- Company first determines customers' wants and then figures out how to make and deliver a product to satisfy those wants
- Management is profit-oriented
- Planning is long-run in focus in terms of new products, tomorrow's markets and future growth
- Stresses wants of buyers

Difference between Selling and Marketing Functions

- Both are independent functions
- Selling is focused around the point at which the potential customer becomes convinced of the value being offered by the product and commits to buy.
- Marketing function prepares the ground for the sales function
- Marketing precedes sales
- Marketing is upstream activity

- Selling is made up of a series of individual transactions

Marketing - Preparing the Ground for the Sales Function

- Defining the product / service offer in terms of market wants and how these may change in the future
- Identifying who the market is and what it consists of in terms of different groupings
- Determining how far to go in re-specifying existing offers for different groupings or generating new specialised offers (including prices)
- Determining how the end consumer will be made aware of the offer and its relative merits compared to the alternatives available
- Determining how the product is most effectively carried to the market

Segmentation

- Traditional view - best salesman is the one who "hard sells" to persuade the other person to buy
- Marketing attempts to reverse this traditional order
- The concept of segmentation (or classification) is at the heart of marketing
- The point is to match a customer want with a product or service which is profitable to deliver

Steps in Segmentation

- Find a form of classification which acts to differentiate a group within a mass
- Determine whether it is feasible and profitable for the supplier to segment the offer
- Involves the way the offer is made, communicated and brought to the market
- R & D input will test certain possible differentiating variables among the customers (eg. size, industry, sector, and geographical location)

Public Relations

- Two key components leading to a sale transaction
 - Awareness

- Confidence
- The brand attaches the "values" of the provider, eg., "living up to market expectations"
- Values behind trade insurance are:
 - Government backed
 - Long established
 - Well informed
 - Reliable
 - Fair
 - Caring
 - Courteous
 - Quick turn around for approval

Print Media

- Newspaper
- Specialised trade magazines, journals

Other forms

- Sponsorship
- Promotional activities

Public Relations Strategy

- Define specific public relations obligations
- Set budget
- Plan, coordinate public relations activities

Listening to the customer - customer care

- Selling credit insurance is not merely selling an insurance policy - it is selling a service
- Listening to the customer is a way of obtaining the feedback necessary to provide continuous product and after-sales service
- Customer care should build customer loyalty and enhance repeat business

Environmental Change

- Marketing strategies must respond to the world environment
 - Shifts in directions of trade
 - Currency turmoil
 - Different economies prosper and slip back
 - New industries emerge and old ones fade away
 - Patterns in claims
 - Directions of government trade promotion policies ie. to non-traditional markets

Adapting to Changes

- Identify and track key external measures or trends, eg. volume, composition and destination of exports
- Develop ways of servicing information through policyholder or buyer contact or own claims experience or Berne Union members' experience
- Develop ways of synthesising such information and decide about future direction of business

Special Problem in Marketing Trade Insurance

- Trade insurance sells pieces of paper
- Perceived as expensive and complicated to administer
- Insurance salesmen are often not perceived as well-meaning professionals
- Credit insurance should position itself as selling a range of services which include:
 - Advice on credit risks
 - Collection services
 - Or a whole range of risk management services

Three Key "Pillars" for a Trade Insurer

- Awareness
- Security
- Reputation

Awareness

- Awareness of the risks associated with non-payment
- Easier done during recession than boom time
- Easier in some industries and markets than others
- Trade insurance as an appropriate reference to those risks
- Unwise to insist on insuring LC transactions all the time
- Challenge against self-insurance

Security

- Will the trade insurance pay if the insured business goes bad?
- Ex-gratia claims

Reputation

- Fairness
- Customer care

Added Value in Trade Insurance

- Provide trade insurance more efficiently or effectively - through information technology
- Speed of decision on credit limits
- Consistency
- Ease of access - on line computer
- Reduced cost
- Sell services
- Buyer information
- Country information
- Join an international networking organisation eg. Credit Alliance

SELLING TO THE EXPORTER

Introduction

- How sales are performed and organised - "marketing"
- Selling is only a small part of marketing
- Successful selling process depends on good marketing plan

Organising a Sales Department

Sales Strategy

- Prospecting
- Communicating
- Selling
- Servicing
- Information gathering
- Allocating

Two types of sales organisations:

Full Task Approach

- Prospecting
- Communicating
- Selling
- Servicing
- Information gathering
- Allocating

Narrow Approach

- Prospecting
- Selling
- Information gathering

Advantages and Disadvantages

Which sales organisation to adopt depends on:

- Market situation
- Customer segmentation
- Flexibility in the product
- Competition

Therefore, it is difficult to choose an organisational structure in advance

Controlling the Sales Representatives

- Define clearly general negotiating authority of the sales representative
- To what extent the sales representative may deviate from these general policies
- Sensible control of sales efforts:
 - Clear understanding of general policies
 - Personal authority
 - Flexibility
 - Control by management
 - Quotas
 - Activity plan vs. activity result
 - Regular formal evaluation
 - Customer feedback
 - Coordination between underwriters and sales personnel

Remuneration of Sales Force

Normally consists of:

- A fixed amount
- A variable amount
- Expenses
- Fringe benefits

Organisation and Structure of Sales Activity

Sales Approach

Two basic approaches:

- Order - taker approach
- Order - getter approach
- Sale-orientated approach
- Customer-orientated approach

Sales Parameters

- Advertising
- Direct mail
- Telesales
- Personal sales work in the form of meeting activities (cold / warm canvassing)
- Own information database
- Combination of the above

The Personal Sales Phases

- Marketing plan
- Sales objectives of the company
- Prospecting and qualifying
- Pre-approach
- Approach
- Presentation and demonstration

- Handling objections / negotiation
- Closing
- Follow-up

Prospecting and Qualifying

- Identify and prioritise potential customers
- Basis of identification:
 - Newspaper articles
 - Publicly available registers on companies
 - Present customers' recommendation
 - Industrial organizations
 - Yellow pages
 - Database on CD ROM

Pre-Approach

- Know the customer before approaching such as:
 - Type of business
 - Size of the business
 - Market
- Sales representative then has to decide:
 - When to contact customer
 - The convenient way to contact the customer
 - Which call objectives should be determined for a prospect

Approach

- Initial contact
 - Personal appearance
 - Opening lines
 - Follow-up remarks

Presentation and Demonstration

- AIDA Formula:
 - Attention
 - Interest
 - Desire
 - Action
- Presentation by support tools such as AV, OHP, Laptops etc.
- Distinguish between:
 - Customer benefits, and
 - Product features
- Need - Satisfaction Approach
- Influence strategies:
 - Legitimacy
 - Expertise
 - References
 - Ingratiation
 - Impression management

Handling Objections / Negotiations

- Psychological objections / resistance
- Logical objections / resistance
- Interviewing technique

Closing

- Understand signals from buyers before closing the sale
- Techniques for encouraging closure:
 - Special benefits with prompt decision
 - Offering special product characteristics

Follow-Up

- Ensure customer satisfaction
- Maintenance of lasting business relations
- Always contact customer

APPENDIX 1

SELLING TO EXPORTERS

CASE STUDY

Sales representative A of Malaysia Export Credit Insurance Berhad, has identified XYZ Bhd. as an interesting prospect. By way of credit information, a newspaper article about the company's successful expansion and the annual accounts received from the local register of companies he has obtained the following data on the company:

| | |
|----------------------------------|---|
| Total turnover | USD 20,000,000 |
| Export turnover | USD 12,000,000 |
| Net worth | USD 4,000,000 |
| Terms of Payment | Normally net 60 days from date of invoice |
| Major export markets | United Kingdom 28% of exports |
| | Japan 20% |
| | USA 27% |
| | Taiwan 10% |
| | Singapore 10% |
| | Canada 5% |
| | France 5% |
| Line of business | Furniture |
| History | Established in 1948 |
| Experience with credit insurance | None |

Furthermore he learned from calling the company's Financial Manager that the company has had two bad debts during the past three years totalling approx. USD 30,000 (one in Germany and one in Mexico). During the conversation the Financial Manager also expressed his interest in hearing more about the possibilities of insuring the company's export debtors as the company has a current outstanding balance of approx. USD 50-60,000 on each of its 25 debtors. The solution must include

cover for both commercial and political risks. In comparison, the current balance for each of the company's other 175 debtors does not exceed USD 15,000.

He stressed however, that since the company has sustained very few losses on its debtors, they were only interested in paying a very small premium for the insurance as they had so far been quite satisfied with not having any insurance, which had proved profitable when calculated over a number of years.

The expansion they have experienced in the past few years has, however, resulted in a considerable influx of new buyers and to a certain extent, new markets (Mexico, France, Pakistan) and specifically in this area they might be interested in taking out insurance until they know these buyers better, said the financial manager. On the other hand, business conditions are improving on most of the markets for which reason the risk of sustaining a loss is assumed to be reduced considerably.

APPENDIX II

SELLING TO / VIA BANKS

FACTORING

Banks as Brokers

- Marketing - individuals and companies can go to one address for all their financial needs
- Company has good access to the clients who have only bought bank product, to sell insurance to and vice versa.
- Bank-related brokers are called "dependent" or "bank-related"

Questions

- Do you use banks as a distribution channel?
- Do you experience any difference between independent specialised brokers and bank-related brokers?
- Do you have a special incentive program for bank-related brokers?

Banks as "Influencers"

- Banks can use credit insurance as a tool
 - To provide attractive financing
 - With extra security for themselves

Questions

- Do banks in your country give a higher credit-facility if a customer has an insurance policy?
- How do banks in your country view the value of a credit insurance policy as a pledge of the accounts receivables?
- Do you use this benefit of credit insurance as an important selling argument?

Banks as Competitors

- Both banks and credit insurers offer financial services
- Different types of credit, but some overlap:
 - Bank credit
 - Sellers credit

Questions

- Do you consider L/C's as an important competitive product?
- Can you compete on price with L/C's?

Factoring

- Factoring - a credit management service
- The factor offers a range of services:
 - Cash advance
 - Administration
 - Debt collection
 - Credit insurance
 - The client is not obliged to buy the whole service, but can select parts.
- A factoring company is a rival for a credit insurer
- Factoring is more expensive than credit insurance

Questions

- What are the advantages and disadvantages of factoring?
- For which companies could factoring be attractive?
- Do you encounter competition from factoring companies?
- Do you have any experience with factoring companies as clients?

SECTION 11

OVERSEAS INVESTMENT INSURANCE

**CHAPTER I OVERSEAS INVESTMENT INSURANCE
 THE JAPANESE MODEL**

**CHAPTER II OVERSEAS INVESTMENT INSURANCE
 THE KOREAN MODEL**

CHAPTER I

OVERSEAS INVESTMENT INSURANCE - THE JAPANESE MODEL

I. Summary

Overseas Investment Insurance is insurance covering Japanese companies which have made overseas investments, and covers losses in regard to their rights as shareholders or creditors. Such losses are caused by political risk and include the inability to continue business activities due to expropriation, war, or civil war or to remit dividends etc. or make repayments because foreign exchange transactions have been restricted by, the government of a host country, and losses caused by commercial risk, including bankruptcy of the companies in which the investments are made.

This insurance covers losses caused by the political risk and commercial risk involved in overseas investments so that Japanese companies need not be concerned when making, such investments. Moreover, such insurance contributes largely to international economic cooperation.

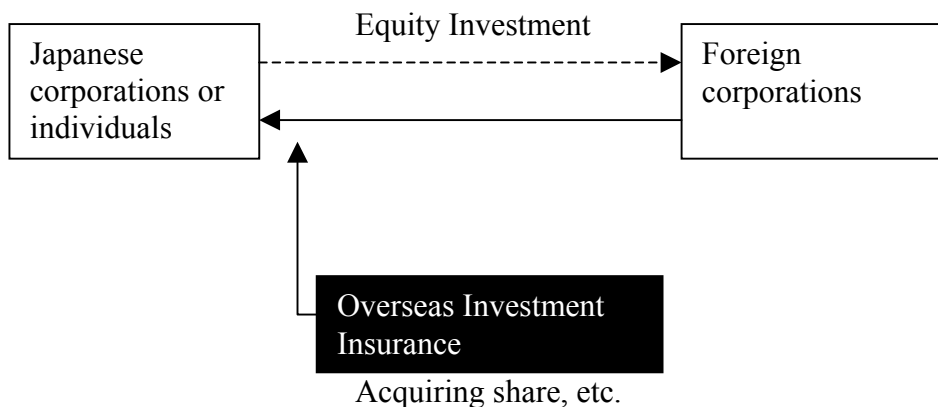
| Name | Type of Investment | Insurance Policy | Coverage |
|---------------------------------------|---|---|---|
| Investment type 1 (share, etc.) | Obtaining shares in foreign corporations (including the securitization of debt and securities investments) | Overseas Investment (Share, etc.) Insurance Policy | Political risk 95% Commercial risk 40% |
| Investment type 2 (Claims, etc.) | Long-term loans to foreign corporations (substantially managed by the Japanese investor) as funds for business activities | Overseas Investment (Claims, etc.) Insurance Policy | Political risk 95% Commercial risk 40% |
| | Assumption of surety obligations regarding the above | Overseas Investment (Surety Obligations) Insurance Policy | Political risk 95% Commercial risk 40% |
| Investment type 3 (Real estate, etc.) | Acquiring real estate, plant and equipment, etc., for overseas business activities | Overseas Investment (Real estate, etc.) Insurance Policy | 95% |

2. Subject & Insurance Coverage

Overseas Investment Insurance is classified as follows by the type of investment:

- **Overseas Investment Insurance on Equity Investments**

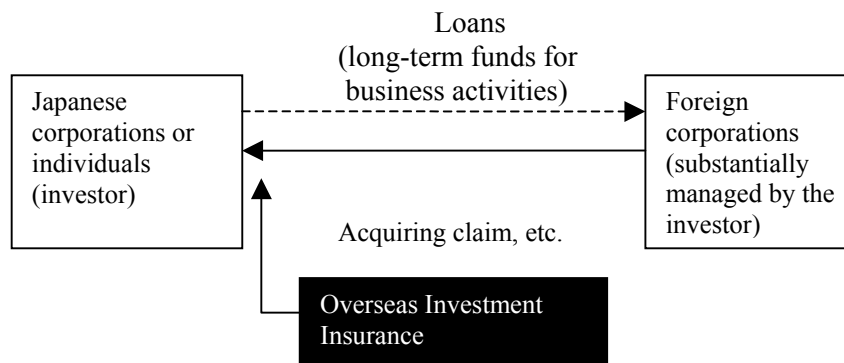
This insurance covers risks assumed by corporations when establishing overseas subsidiaries, establishing overseas joint-venture companies with foreign partners, or making investments in existing foreign companies. (Investment type 1 share, etc.)



Overseas Investment Insurance for Loans

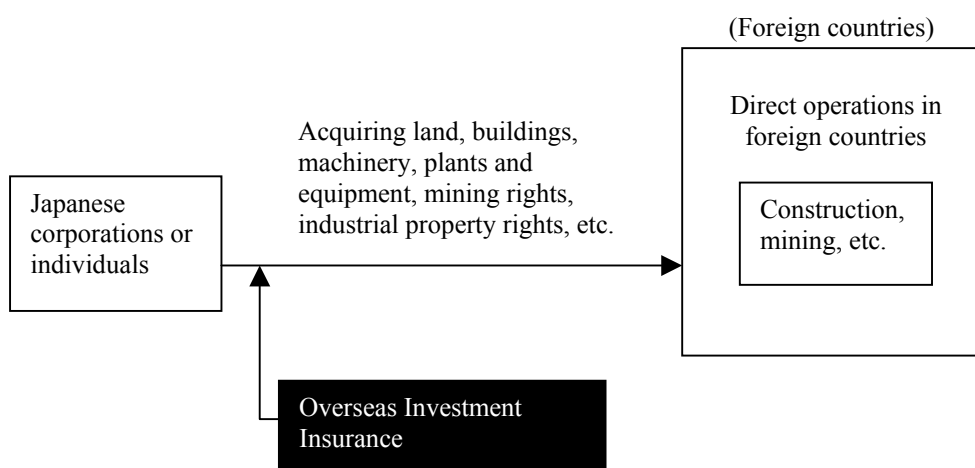
This insurance covers risks related to long-term loans of funds required for business activities by foreign corporations (which are substantially managed by the Japanese investor).

(Investment type 2 - Claims, etc.)



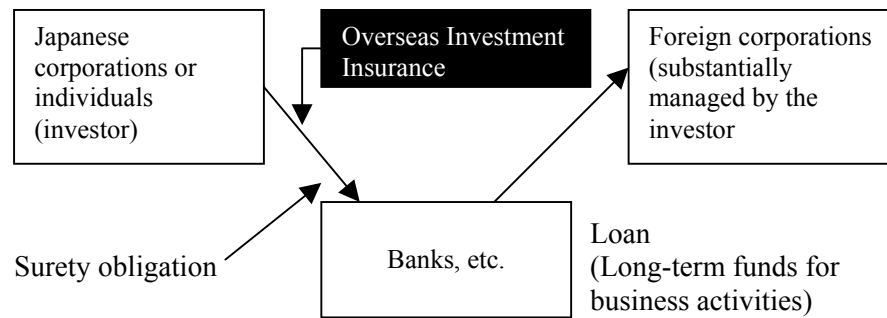
Overseas Investment Insurance for Real Estate Rights, etc.

This insurance covers risks assumed by Japanese corporations which engage directly in business in a foreign country in connection with real estate rights, mining rights, and other rights to plant and equipment transported directly to a foreign country in order to conduct such business. (Investment type .3 - Real estate, etc.)



▪ **Overseas Investment Insurance for Surety Obligations**

This insurance covers risks assumed by Japanese corporations in connection with surety obligations for long-term loans to foreign corporations (which are substantially managed by the Japanese investor). (Surety obligations for claims, etc.)



The definition of "substantially managed" by a Japanese corporation is as follows: The phrase "corporation whose management is substantially controlled by a Japanese company or by a Japanese national through the ownership of shares or other methods" in Article 2, paragraph 16 of the Trade and Investment Insurance Law, refers to any of the following cases:

- (1) A Japanese corporation or a Japanese national who has made an overseas investment holds more than 50 percent of the shares or other interests with voting rights in such foreign corporation.
- (2) More than 50 percent of the executives in a foreign corporation (limited to executives who hold voting rights at a meeting of the board of directors; the same shall apply hereinafter) are executives or employees of a Japanese corporation or are Japanese nationals.
- (3) A Japanese corporation or a Japanese national holds no less than 25 percent but no more than 50 percent of the shares or other interests with voting rights in such foreign corporation and comes under any of the following:
 - a) The Japanese corporation or Japanese national involved is the largest shareholder in such foreign corporation
 - b) More than 25 percent of the executives in such foreign corporation are executives or employees of a Japanese corporation or are Japanese nationals.

- (4) If the Minister of International Trade and Industry considers that a Japanese corporation or a Japanese national substantially controls the management of such foreign corporation

3. Underwriting Requirements for Insurance

The requirements for underwriting insurance for overseas investments stated in 2. above are as follows:

- (1) Such investments must contribute to the sound development of overseas transactions by Japanese corporations.
- (2) Any such investment must be a new transaction.
(including transactions following the expiry of the insurance period for Overseas Investment Insurance)
- (3) The political and economic conditions in the host country involved pose no particular problems.
- (4) Protective measures in regard to foreign capital in the host country involved have been fully established.
- (5) Such investments have been permitted by the host country involved.
- (6) If surety obligations are assumed, whether or not it can be confirmed by a guarantee contract or other similar documents that a guarantee has been appended to or included in the original obligations, and if the guarantor performs such surety obligations, the acquisition of indemnity rights has been clearly stipulated in the guarantee contract or other similar documents.

4. Risks to be Covered

The risks to be covered by Overseas Investment Insurance are: political risk; (expropriation; war; failure to make remittances) and commercial risk (bankruptcy).

(1) **Political Risk**

▪ **Expropriation risk** (Investment type 1 - 3)

- 1) The expropriation, by a foreign government, etc. of the principal, etc., of an investment (rights relating to the principal of equity, etc. or claims, etc. or right to claim dividends from stock, etc. or right to claim interest from claims, etc.) or rights, etc. related to real estate.
- 2) Inability to continue business due to damages incurred by the party in which the insured investment was made (invested company) caused by the interference of a foreign government, etc. in the rights related to real estate, plants and equipment, raw materials and other goods, mining or industrial property rights, or other rights or interests, which caused the inability to conduct the business involved.
- 3) The performance of surety obligation, due to the non-performance by the principal obligors of their obligations as a result of losses to the said obligor's properties for the above reasons (Surety obligations for claims, etc.)

▪ **War Risk** (Investment type 1-3)

- (1) If any of the following occur in relation to the insured company; (a) Inability to continue business activities, (b) bankruptcy, etc., (c) suspension, etc. of transactions with banks, and (d) suspension of business for over six months caused by war, revolution, civil war, riot or other forms of civil disturbance
- (2) The performance of surety obligations due to the non-performance by the principal obligors of their obligations due to any of the above reasons (a)-(d) as the result of losses to the said obligor's property, caused by war, etc.
(surety obligation for claims etc.)
- (3) Insured's inability to exercise their rights, etc. related to real estate, involved in the business activities due to the interference with such rights caused by war, etc.

▪ **Remittance Risk** (Investment type 1-3)

Inability for over two months to remit to Japan any transfer proceeds, dividends from share, repayment of loan principal and interest, sales proceeds from real estate, and any amount obtained from the main obligor by executing surety obligations because of the restrictions on foreign exchange transactions in a foreign country.

(2) **Commercial Risk**

Bankruptcy due to depressed business conditions of the invested company or other similar reason.

The term "bankruptcy" in this article must satisfy all three following conditions:

- 1) The liabilities of the invested company are in excess of their net worth.
- 2) Dissolution of the invested company.
- 3) Involvement by the judicial authorities in the host country.

5. Insurance Period

The following are insurance periods according to the risks to be covered:

- (1) For political risk, it should in principle, be from 3 to 15 years.
- (2) For commercial risk, it should in principle, be from 3 to 10 years.

In exceptional cases, if a considerable period of time is required before the party to the insured investment will start an operation, such as the construction of factories, the following period designated by the Minister of International Trade and Industry can be added to the above periods:

- (1) For political risk, the actual period required to start overall operations.
- (2) For commercial risk, a period not exceeding the period until the start of operations.

6. Insured Amount

The insured amount which refers to the upper limit of insurance claims to be paid when losses occur, is determined to be no more than the amount obtained by multiplying the "total amount for acquisition" for each risk covered by the designated coverage rate.

The coverage rates are as follows:

| | |
|--|-----|
| (1) Political risk in Investment types 1, 2, and 3 | 95% |
| (2) Political risk in surety obligations for Investment type 2 | 95% |
| (3) Commercial risk in Investment types 1 and 2 and surety obligations for Investment type 2 | 40% |

7. Insurance Claims Payable

The insurance claims to be paid should be calculated by multiplying the loss amount by the coverage rate and should not exceed the insured amount. (Actual loss coverage system)

The following formulae are used for the calculation of insurance claims:

(1) For political risk

▪ Expropriation and war risk

$$1) \left(\begin{array}{l} \text{Amount appraised} \\ \text{immediately before the} \\ \text{insured risks occur or} \\ \text{the total amount for} \\ \text{acquisition, whichever} \\ \text{is smaller} \end{array} \right) - \left(\begin{array}{l} \text{Appraised amount} \\ \text{immediately after} \\ \text{the insured risks} \\ \text{occur} \end{array} \right) - \left(\begin{array}{l} \text{Amount} \\ \text{recovered,} \\ \text{etc.} \end{array} \right) = \left(\begin{array}{l} \text{Amount} \\ \text{of loss} \end{array} \right)$$

$$2) \quad \text{Amount of loss} \times \text{Coverage rate} = A$$

3) The insurance claims should be the amount in A above or the insured amount, whichever is smaller.

▪ **Remittance risks**

1)

$$\left(\begin{array}{l} \text{Amount which cannot} \\ \text{be remitted or the} \\ \text{amount for acquisition,} \\ \text{whichever is smaller} \end{array} \right) - \left(\begin{array}{l} \text{Amount saved due} \\ \text{to insured risks} \end{array} \right) - \left(\begin{array}{l} \text{Amount} \\ \text{recovered, etc} \end{array} \right) = \left(\begin{array}{l} \text{Amount} \\ \text{of loss} \end{array} \right)$$

2) Amount of loss X Coverage rate = B

3) The insurance claims should be the amount in B above or the insured amount, whichever is smaller.

(2) For commercial risk

1)

$$\left(\begin{array}{l} \text{Amount of} \\ \text{Acquisition} \end{array} \right) - \left(\begin{array}{l} \text{Amount} \\ \text{recovered etc.} \end{array} \right) = \left(\begin{array}{l} \text{Amount of} \\ \text{loss} \end{array} \right)$$

2) Amount of loss X Coverage rate = C

3) The insurance claims should be the amount in C above or the insured amount, whichever is smaller.

8. Basic Premium

(1) Premium rate

1) Political risk

On a case-by-case basis with an annual rate of ¥0.55 per each ¥100 of the insured amount as the basic rate

2) Commercial risk

On a case-by-case basis with an annual rate of ¥1.00 per each ¥100 of the

insured amount as the basic rate

The premium rate will vary according to the profitability of parties in which an investment was made, and the country risk involving any host country.

(2) Review of premium rate

The premium rate for commercial risk is reviewed in the fourth, seventh, and tenth fiscal year from the beginning of the obligation period of the insurance.

9. Duties Regarding Collections on Investments and Payment of Funds Collected

(1) Duties Regarding Collections on Investments

Even after requesting payment of the insurance claims payable, the insured shall make every effort to collect on the loans, etc. any compensation for losses, or on any other monetary claims of a similar nature.

(2) Payment of Funds Collected

Should any funds be collected after requesting payment of insurance claims payable, the insured shall notify the Minister of International Trade and Industry of the receipt of such funds within one month from the date immediately following the date when the collection was made (if the date when the collection was made falls on or before the date the payment of the insurance claims payable was received, the date when the payment of the relevant insurance claims payable was made) and pay the amount designated by the revenue collector to the National Treasury on or before the date designated by such collector.

10. Procedure for Overseas Investment Insurance

To conclude an insurance contract, the following procedures should be taken:

(1) Preliminary Application

To conclude an insurance contract, submit a preliminary application on or before the day prior to the remittance day (if two or more remittances are to be made, the first remittance day).

A preliminary application will be accepted by the Overseas Investment Insurance Office, Export, Import and Investment insurance Department (EID/MITI) and Regional Bureaus of MITI.

(2) Formal Application

After the preliminary application has been submitted, submit a formal application to the Overseas Investment Insurance Office, no less than one month after the remittance day.

(3) Insurance Contract

The formal application will be evaluated by MITI before concluding an insurance contract.

(4) Issuance of Insurance Policy, etc.

On behalf of MITI, Japan Trade and Investment Insurance Organization will issue (1) The overseas investment insurance policy, (2) Approval of changes in (1) (including any increase or decrease in the insured amount, and other approvals for changes), and (3) Notice for payment of the overseas investment insurance premium.

Documents to be Attached to the Formal Application

Documents to be attached to the formal application will vary according to the type of investment, methods for remittance, type of business, and the legal system in the host countries in which investment activities occur. In general, copies of the following documents are required:

- (1) Investment and loan contracts, etc.

For example, joint venture contracts, loan agreements, guarantee contracts, business collaboration contracts, etc.

In the case of a capital increase, the minutes of the general meeting of shareholders when the capital increase was approved should be attached. In the case of an investment in wholly owned subsidiaries of Japanese companies and direct business activities related to Investment type 3, the minutes of the board of directors meeting of the insured (investors) should be attached.

- (2) Investment permission, etc. issued by the government of the host country
- (3) Report to the Bank of Japan
- (4) Any documents which provide evidence that investments and loans have been made

[Cash remittance]

Remittance statements related to investments which were issued by authorised foreign exchange banks and remittance applications with an indication of the foreign currency used, amount paid in yen, conversion rate, date of remittance, remittee, remitter, purpose of remittance, bank's certification stamp, and investment report number assigned by the Bank of Japan.

[Investment in kind]

Export approval, shipping documents, supply contract, receipt of payment for exported cargo, asset ledgers, etc.

[Capital increase without compensation]

Documents which provide evidence of the capital increase and the foreign exchange rate on that day

[Surety obligation]

Documents of the main obligor (borrowing company) which provide evidence that the loans were made and the foreign exchange rate on the day the proceeds of the loans were received (opening price of customer spot T.T. selling rate announced by foreign exchange banks)

If the remittance was made in installments or was made by several banks, attach "List of total remittance amount"

- (5) Articles of incorporation of the other party to the overseas investment
- (6) Repayment schedule list (for loans)

- (7) Notice of evaluation results on preliminary applications for overseas investment insurance
- (8) Other documents required for each transaction

Documents to be Attached to the Preliminary Application

- **Political Risk**

Business projections, financial statements, etc. (balance sheets, profit and loss statements, statements of appropriations, and income and expenditure statements)

- **Commercial Risk**

A copy of the following documents related to the insured (investors), partners, the other party to the overseas investment.

- I Documents related to the insured (investors)

- 1) Balance sheet (for the three years prior to the preliminary application)
- 2) Profit and loss statement
- 3) Surplus appropriations statements or deficit disposition statements
- 4) Income and expenditure statements

- II Documents indicating the partner's ability to perform activities

- III Documents related to the other party to the overseas investment

- (A) New Companies

- 1) Feasibility study statement
- 2) Business projections
- 3) Projection of funds
- 4) Estimated balance sheet (for fiscal terms to be covered by the insurance)
- 5) Estimated profit and loss statement
- 6) Estimated surplus appropriations statement or deficit disposition statement
- 7) Estimated income and expenditure statements
- 8) Loan and investment contracts, etc. (including guarantee contracts)

(B) Existing companies

In addition to the documents in (A) above, the following documents for the three years prior to the preliminary application (for companies in which investments were made with less than three years business experience, for the period of their operation should be attached)

- 1) Balance sheet
- 2) Profit and loss statement
- 3) Surplus appropriations statement or deficit disposition statement
- 4) Income and expenditure statements

CHAPTER II

OVERSEAS INVESTMENT INSURANCE

THE KOREAN MODEL

OVERSEAS INVESTMENT INSURANCE

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- I. INTRODUCTION
- II. OVERSEAS INVESTMENT OF KOREA
- III. FINANCIAL ASSISTANCE PROGRAM FOR OVERSEAS INVESTMENT OF KOREA
- IV. OVERSEAS INVESTMENT INSURANCE SCHEME OF KEIC
- V. RECENT DEVELOPMENTS OF ECAs' OVERSEAS INVESTMENT INSURANCE PROGRAM
- VI. CASE STUDY

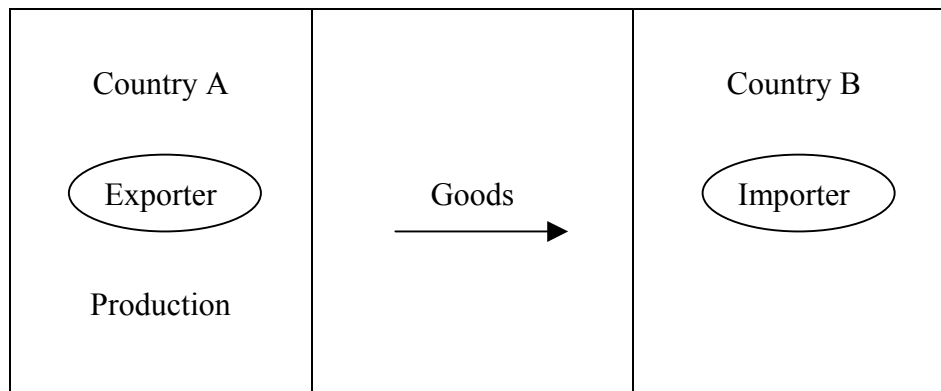
OVERSEAS INVESTMENT INSURANCE

1. INTRODUCTION

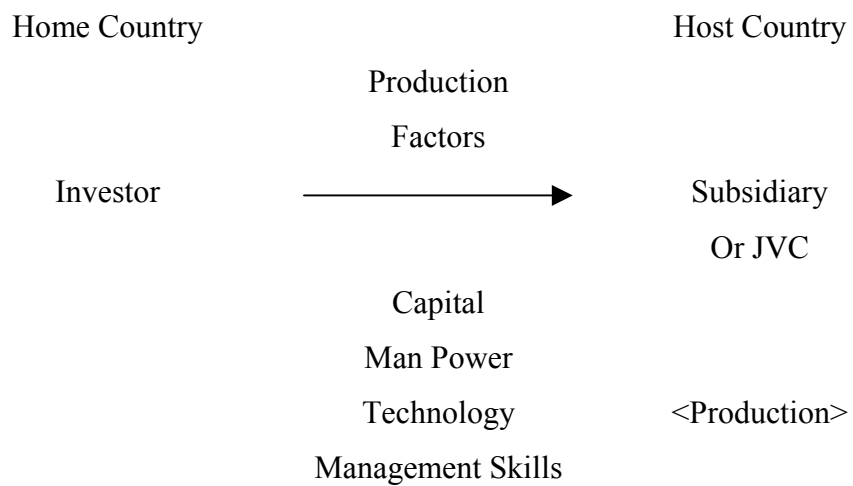
1. Concept of Overseas Investment

(Export vs Overseas Investment)

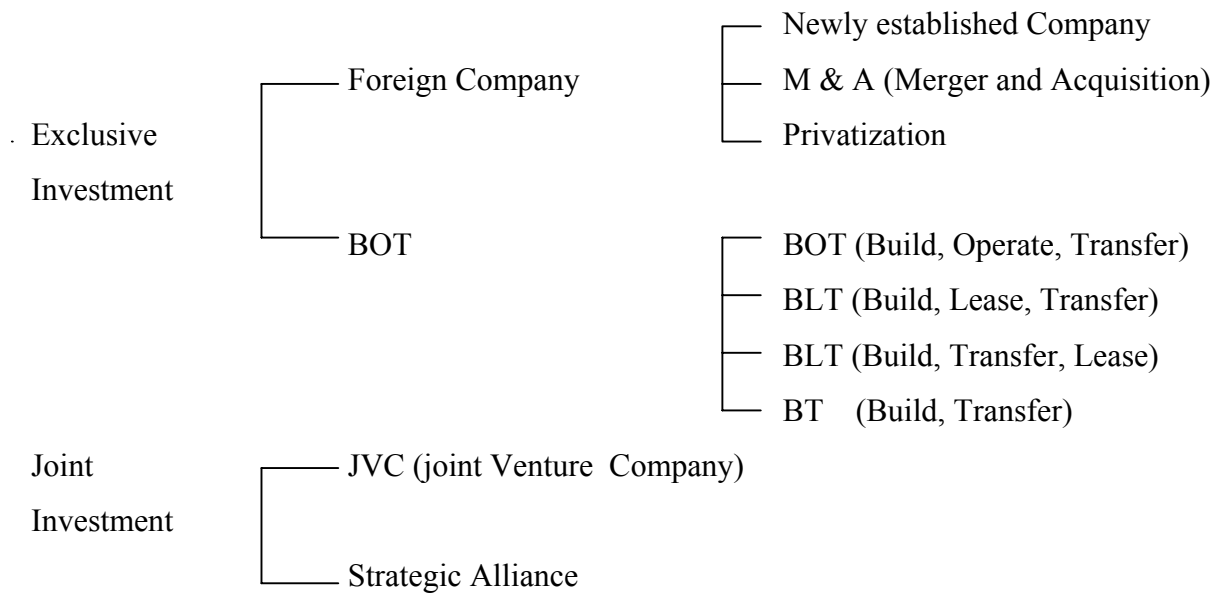
- Export



- Overseas Investment



2. Types of Overseas Investment



3. Environment Surrounding Overseas Investment

- Expansion of Overseas Investment Opportunities
- Accelerated Integration of World Economy
- Enlargement of Regionalism
- Intensified Protection of Technology
- Reorganisation of International Economic Structure
- Extensive Privatization in the Transitional Economies

<Trend of Integration of World Economy>

| 1960 | 1970 | 1980 | 1990 | 2000 |
|------|------|------|------|------|
| 9% | 13% | 19% | 24% | 31% |

(Trade & Sales by Overseas Investment/GDP)

4. Motives of Overseas Investment

- Market-Oriented Investment
 - to maintain already established markets in response to tariff and/or non-tariff barriers

- to develop and enter new markets with great potential purchasing power
- Production Efficiency-Oriented Investment
 - to secure long-term and stable supply of natural resources
 - to strengthen competitiveness by taking advantage of cheap and good-quality production factors (man power, etc.)
- Technology-Oriented Investment
 - to acquire advanced manufacturing technology, marketing skills and management know-how
- Economic Cooperation-Oriented Investment
 - Development Aid, Direct loan into host country

Globalization of Company

| | | |
|----------|-------------------------------------|---|
| | | Domestic Production and Management |
| Phase 1: | Export | Marketing through Local Agent or Representative Office |
| Phase 2: | Internationalization & Localization | Active Overseas Investment Local Production, Marketing and Diversification |
| Phase 3: | Globalization | Global Optimization of Production, Resources & R&D |

5. Economic Effects of Overseas Investment

(from the view point of Home Country)

- Effect on Balance of Payment

| | Financial Effects | Trade Effects |
|---------------------|---|--|
| Feature | <ul style="list-style-type: none"> • Flow of Funds | <ul style="list-style-type: none"> • Export and Import of Goods |
| Affirmative Factors | <ul style="list-style-type: none"> • Inflow of Dividend, Interests, Royalty and Commissions, etc. • Recovery of Invested Principal and Loan • Investment in kind and Local Finance, etc. (substitution of out-flow of funds) | <ul style="list-style-type: none"> • Induced Export of Capital Goods and Intermediary Goods • Decreased Import of Raw Materials and Intermediary Goods • Increased Export due to growing Income of Host Country |
| Negative Factors | <ul style="list-style-type: none"> • Investment in cash • Repayment of Debt | <ul style="list-style-type: none"> • Substitution of Export • Reimport of Finished Products |

Employment

- | | | |
|--|---|-----------|
| <ul style="list-style-type: none"> • Declined Domestic Investment • Reimport • Substitution of Export | } | ⇒Decrease |
| <ul style="list-style-type: none"> • Inducement of Export | } | ⇐Increase |

Industrial Structure

- | | | |
|---|---|--|
| <ul style="list-style-type: none"> • Domestic Fading Industry • Labour-Intensive Industry • Technology-Oriented Investment | } | ⇒Promotion of Adjustment of Industrial Structure |
| <ul style="list-style-type: none"> • Comparative-Advantage Industry | } | ⇒Overseas Transfer of Technology, Weakening of International Competitiveness |

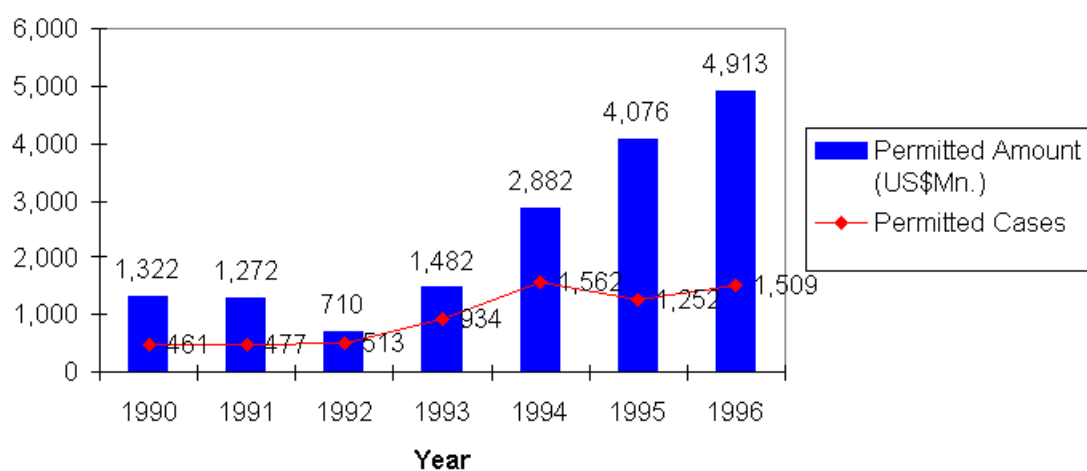
II OVERSEAS INVESTMENT OF KOREA

1. Overview

| | Major Industry | Feature |
|-----------|--|---|
| 1968-1974 | <ul style="list-style-type: none"> • Forestry • Fishery | <ul style="list-style-type: none"> • In 1968, first Overseas Investment made by Korea Nambang Development Co. for the forestry development project in Indonesia |
| 1975-1980 | <ul style="list-style-type: none"> • Natural Resources • Construction | <ul style="list-style-type: none"> • Oil, Gas, Coal, Iron Ore, etc during period of oil shock • Construction Boom in Mid-East Countries |
| 1981-1985 | <ul style="list-style-type: none"> • Labour-Intensive Industries • Trade | <ul style="list-style-type: none"> • Textile, Footwear, Leather, etc. • To the Developing Countries • Made by Medium & Small Companies • To North America & Europe to meet import restrictive measures • Made by large Companies |

| | Major Industry | Feature |
|-------|---|--|
| 1986- | <ul style="list-style-type: none"> • Capital and Technology Intensive Industries | <ul style="list-style-type: none"> • Communication, Electronics, Semiconductor, Automobiles • R & D • Outstanding Investments as of the end of 1996 <p>:US\$13,8 Billion (6,653 Cases, 2.8% of GDP)</p> |

2. Recent Overseas Investment Trend



3. Outstanding Balance of Overseas Investment (As of the end of 1996)

(1) By Industry

| | Manufacturing | Trade | Construction | Fishery | Transport & Storage | Mining | Forestry | Others | Total |
|-----------------------|---------------|-------|--------------|---------|---------------------|--------|----------|--------|--------|
| Project | 4,459 | 982 | 208 | 143 | 88 | 65 | 21 | 687 | 6,653 |
| Amount (US\$ million) | 7,723 | 2,819 | 528 | 90 | 91 | 900 | 84 | 1,521 | 13,756 |

(2) By Region

| | South-East Asia | North America | Europe | Latin America | Oceania | Africa | Middle East | Total |
|-----------------------|-----------------|---------------|--------|---------------|---------|--------|-------------|--------|
| Project | 4,806 | 920 | 384 | 268 | 179 | 57 | 39 | 6,653 |
| Amount (US\$ Million) | 6,055 | 4,327 | 2,104 | 556 | 312 | 274 | 128 | 13,756 |

(3) By Project Size

| | Less than 1,000 thou | 1,000-2,000 | 2,000-5,000 | 5,000- 10,000 | Over 10,000 | Total |
|-----------------------------|-------------------------|-------------|-------------|------------------|-------------|--------|
| Project | 5,107 | 643 | 483 | 200 | 220 | 6,653 |
| Amount (US\$ Million) | 1,361 | 944 | 1,565 | 1,465 | 8,421 | 13,756 |

III. Financial Assistance Program for Overseas Investment of Korea

1. The Export-Import Bank of Korea

- The largest supplier of Overseas Investment Credit with preferential rate
- Non Eligible Projects
 - Projects in countries which received E rating(5/5) from the Bank
(Exception: Investment in free-trade zone, and countries which concluded an agreement on the promotion and protection of investments with Korea)
 - Real estate-related projects such as real estate rent, management of entertainment and leisure facilities, etc.
 - Projects related to banking, insurance, housekeeping, entertainment
 - Projects that are operated by an individual, not an entrepreneur

Major Terms and Conditions of Overseas Investment Credit

- Eligible Borrower : Korean investor
- Credit Coverage :Up to 90% of investment amount
- Maturity :Up to 10 years (including a 3-year grace period)
- Interest Rate(per annum)

| Floating rate | Fixed rate | Remark |
|--|-------------------------|-------------------|
| <ul style="list-style-type: none"> • Payment guarantee by domestic or foreign financial institutions :Libor + 0.5% • Secured Mortgage :Libor + 0.75% • Credit | Swap rate +0.5% ~ 1.25% | Investor's Option |

| | | |
|--|--|--|
| :Libor +1.0 ~1.25% | | |
| * LIBOR - London Inter Bank Offer Rate | | |

2. Economic Development Cooperation Fund (EDCF)

- Operation
Ministry of Finance and Economy : Management of EDCF
KOREA EXIM BANK : Projects Appraisal, Execution of Loan Agreement and
Administrative Work related to extending loans
- Eligible Project
 - Business not suitable for borrowing from the Korea EXIM Bank or other commercial financial institutions with general terms and conditions
 - Investment business of the economic cooperation for developing countries
 - Agriculture, Forestry, Fisheries, and Development of Mineral Resources
- Eligible Borrower : Small / Medium size companies
- Major Terms and Conditions of EDCF
 - Interest Rate :5~6% p.a.
 - Maturity :15 years (including a 5 year grace period)

3. Commercial Banks and State-run Companies

| | Major Terms and Conditions of Loan |
|------------------------|--|
| Foreign Exchange Banks | -Up to 70% of Investment Amount (Up to 80% in case of small / medium size companies) -Interest Rate : Libor + 1.0% p.a. -Repayment Period : Maximum 10 years |
| Korea Mining Promotion | -Up to 80% of Investment Amount -Interest Rate : 5% p.a. -Repayment Period : Maximum 15 years |

| | |
|---|---|
| Corporation | -Important Development Projects of mining resources except for petroleum |
| Korea Petroleum Development Corporation | -Up to 70% of Investment Amount -Interest Rate : less than 6% p.a. -Repayment Period : Maximum 18 years -Petroleum Development Project |

List of Countries which concluded an Agreement on the Promotion and Protection of Investments with Korea (As of June, 1996)

Contracting parties (38 Countries)

U.S.A., Germany, Switzerland, Netherlands, Belgium, Luxemburg, U.K., France, Sri Lanka, Senegal, Hungary, Tunisia, Denmark, Bangladesh, Malaysia, Thailand, Poland, Pakistan, Mongolia, Austria, Russia, Italy, China, Uzbekistan, Vietnam, Lithuania, Paraguay, Indonesia, Romania, Turkey, Czech, Peru, Finland, Greece, Spain, India, Laos, Tajikistan

Signatory parties (9 Countries)

Philippines, Argentina, South Africa, Portugal, Sweden, Brazil, Egypt, Kazakhstan, Bolivia

List of Countries which concluded an Agreement on Avoidance of Double Taxation with Korea : As of June, 1996

Contracting parties (45 Countries)

Japan, Thailand, Germany, U.K., Denmark, Belgium, U.S.A., Canada, France, Singapore, Netherlands, Switzerland, Finland, Sweden, Malaysia, New Zealand, Australia, Norway, Bangladesh, Turkey, Sri Lanka, India, Philippines, Luxemburg, Pakistan, Austria, Indonesia, Tunisia, Hungary, Ireland, Brazil, Poland, Italy, Mongolia, Egypt, Vietnam, China, Romania, Spain, Mexico, Fiji, Czech, Bulgaria, Russia, South Africa

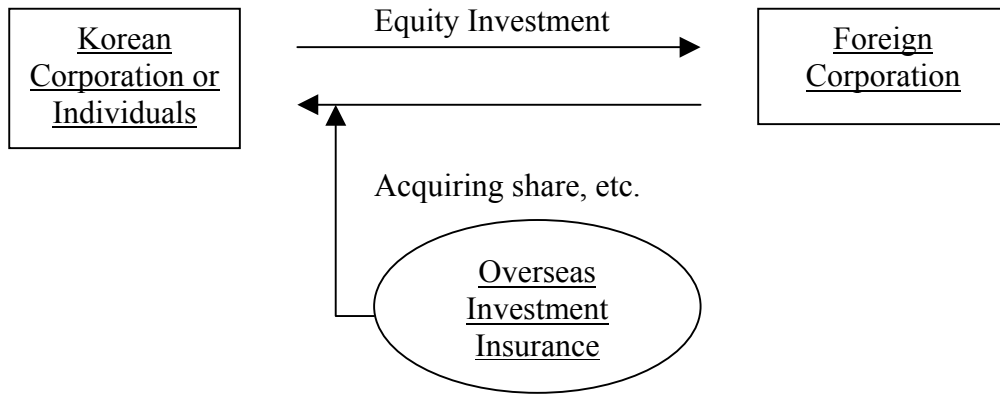
Signatory parties (2 Countries)

Greece, Portugal

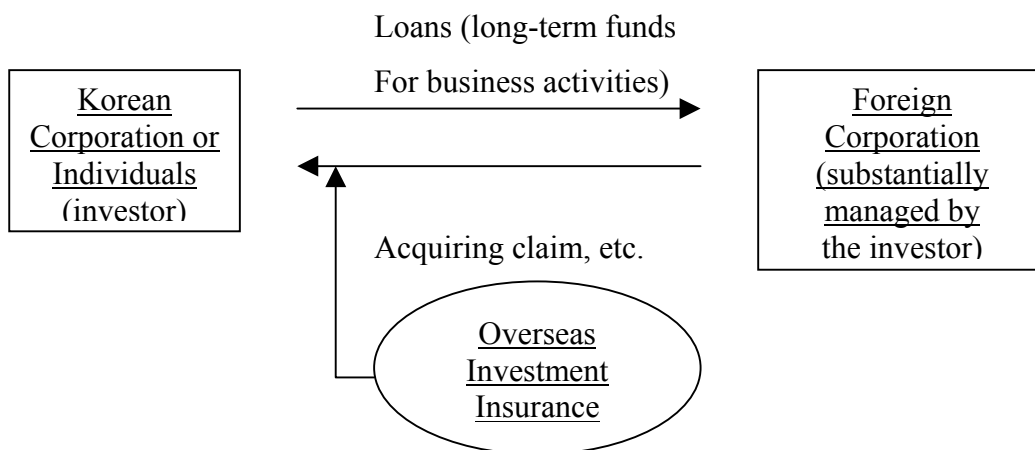
IV. Overseas Investment Insurance Scheme of KEIC

1. Eligible Investments

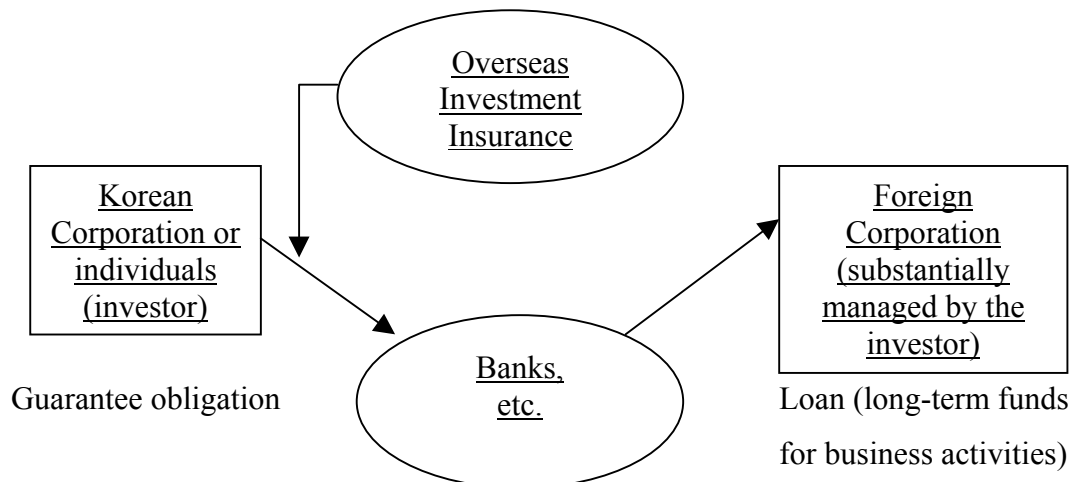
- **Equity**



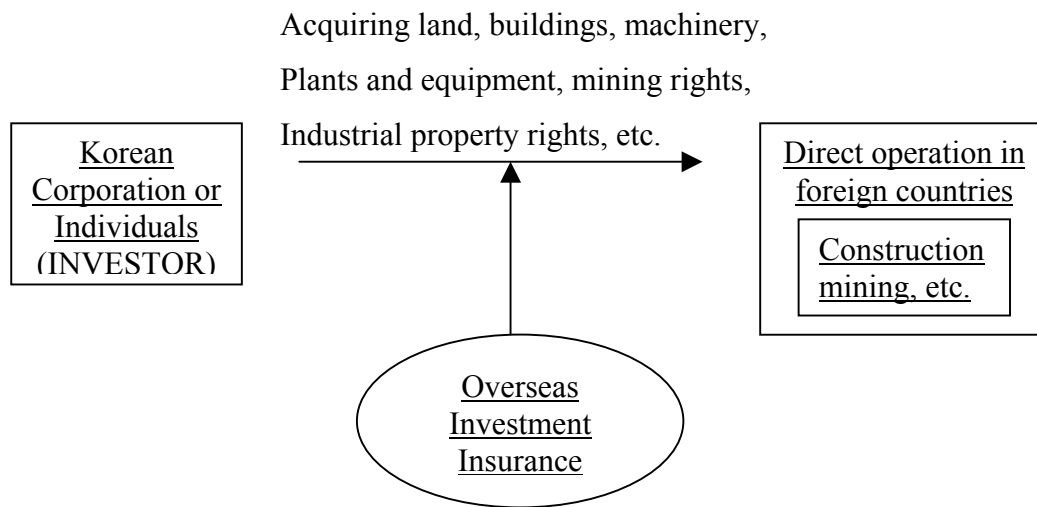
- **Loan**



- **Loan Guarantees**



- **Rights**



2. Underwriting Requirements

- Contribution to the Sound Development of Overseas transaction
- A New Investment
- No Adverse Political and Economic Situation in the Host Country
- Foreign Investment Protection Treaty with the Host Country

3. Risk Covered (Political Risks only)

- Expropriation Risk

1)

Expropriation by a host government of

- right of the principal of equity or claims
- right to claim dividends from stock
- right to claim interest from loan
- right related to real estate

2)

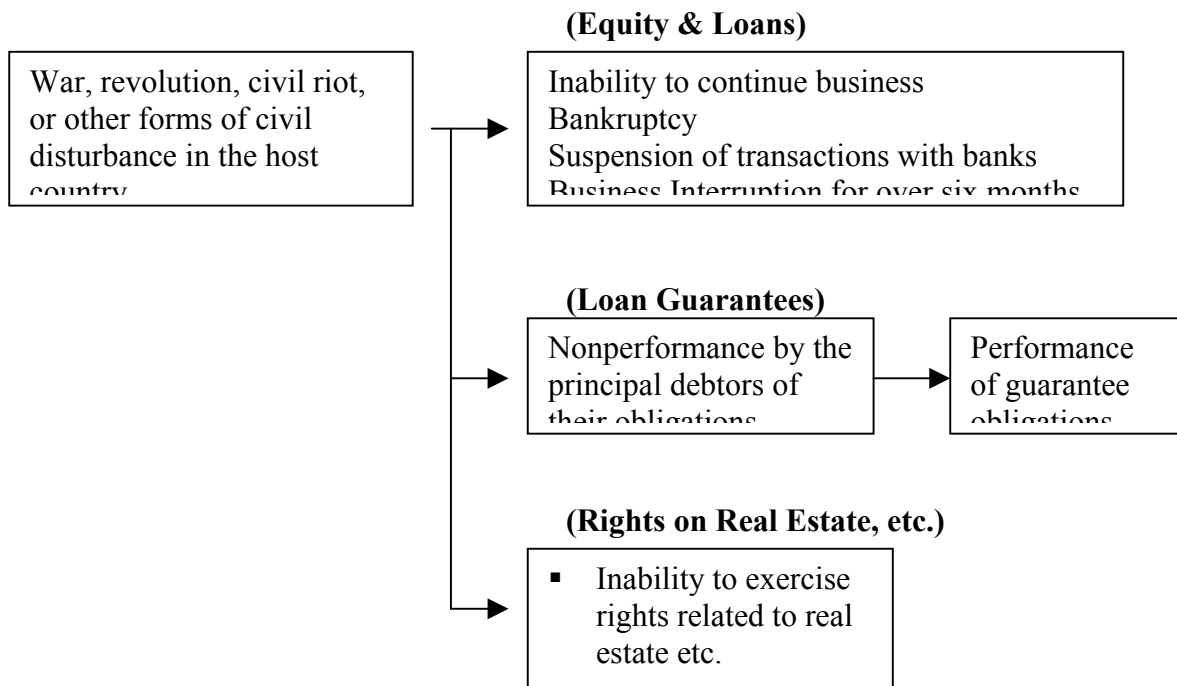
Interference of a host government in

- the rights related to real estate, plants and equipment, raw materials, mining or industrial property rights, etc.

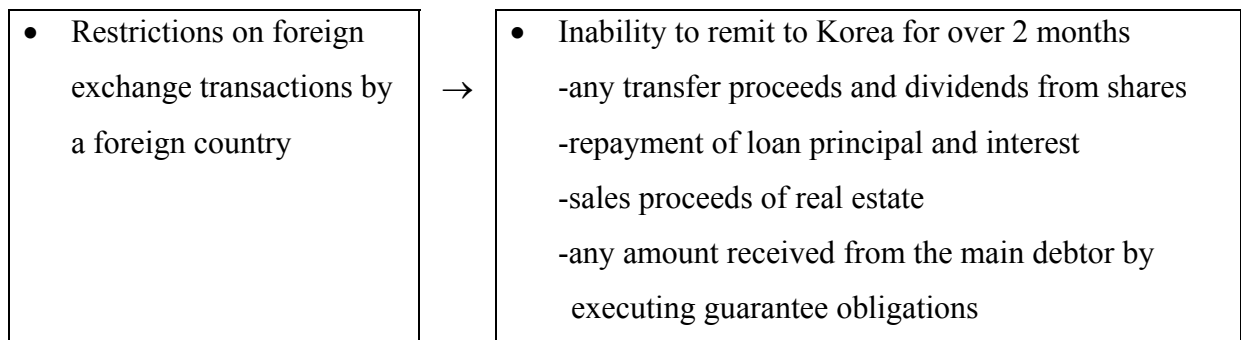
⇒

- inability to continue business
- - bankruptcy
- -suspension of transactions with banks
- business interruption for over 6 months

- **War Risks**



- **Transfer Risks**



3. Insurance Period

- Minimum 1 year to Maximum 15 years

4. Percentage of Cover & Claims Paid

- Percentage of Cover

- Insurable Value : Korean Won equivalent to the Invested Amount

- Insured Amount : Up to 90% of Insurable Value (Up to 95% in Case of Small / Medium size Company)

- Claims Paid

$$\begin{array}{|c|} \hline \text{Amount of} \\ \hline \text{Claims Paid} \\ \hline \end{array} = \begin{array}{|c|} \hline \text{Amount of} \\ \hline \text{Loss} \\ \hline \end{array} \times \begin{array}{l} 90\% \\ \text{(or 95\%)} \end{array} < \begin{array}{|c|} \hline \text{Insured} \\ \hline \text{Amount} \\ \hline \end{array}$$

5. Premium Rate

- Basic Rate

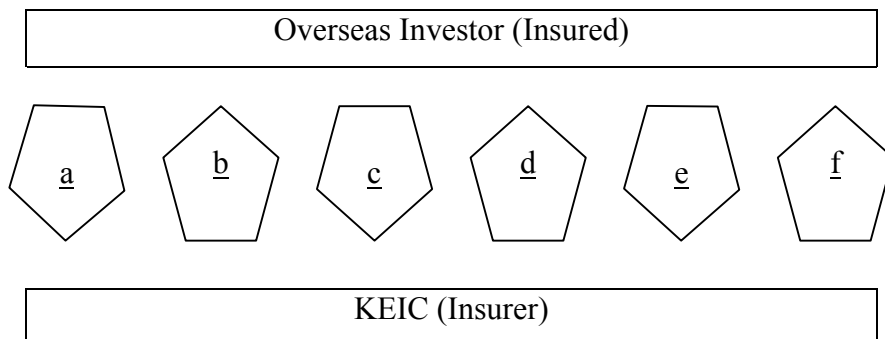
| Country Grade | A | B | C | D | E | F | G | H |
|-------------------------------|------|------|------|------|------|------|------|------|
| Premium Rate (1Year Basis) | 0.18 | 0.36 | 0.47 | 0.58 | 0.68 | 0.79 | 1.08 | 1.44 |

- Discount Rate

| | Discount Rate |
|--|---------------|
| *Discount Rate for Payment Guarantee | 25% |
| Discount Rate for Small or Medium-Size Enterprises | 15% |

*Payment Guarantee by institutions in the host country is not eligible for the discount rate.

6. Underwriting Procedure



a. Preliminary Application

- Before the investment is made

- Documents to be attached
- Business plan or estimated financial statement
- Outline of investment partner in case of Joint-Venture

b. Acceptance Notice for Preliminary Application

- Main Check Points
- Political risk of the host country
- Prospects of the investment

c. Main Application

- Within one month after the investment is made
- Documents to be attached
 - Investment Agreement, Loan Agreement, or Guarantee Agreement
 - Certificate of Remittance
 - Approval of the Host Country (if any)
 - Approval of Korean Government (if necessary)
 - Business Plan, etc.

d. Approval of the Main Application

- Main Check Points
 - Business Environment of the Host country
 - Host Country's Ability to repay the external debts
 - Contents of the Investment Agreement or Investment Plan
 - Types and Purposes of the Investment
 - Credibility and Financial Standing of the guarantor (if any)

e. Payment of Premium

| | Premium Period | Payment of Premium |
|-------------------------------|--|---|
| 1 st Business Year | Approval Date~Dec.31 of the following year | Within 10working days from the approval date |
| Business Years thereafter | Jan, 1~Dec.31 | Within 10 working days from last day of the previous year |

f. Issuance of Insurance Policy

After the insured has paid the premium for the 1st business year

7. Overseas Investment Insurance (Loan) vs Medium & Long Term Export Insurance (Buyer Credit) in Project Financing

| | Overseas Investment Insurance (Loan) | Medium & Long Term Export Insurance (Buyer Credit) |
|------------------------|---|---|
| The Insured | Overseas Investor or Financial Institution | Financial Institution |
| Eligible Object | Loan to Overseas Project Company | Export Credit |
| Risks Covered | Political risk | Political risk, Commercial risk |
| Coverage Ratio | Up to 90% | Up to 95% |
| Merit | OECD Guideline not applied | Commercial risk covered |
| Demerit | Commercial risk not covered | OECD Guideline applied |

V. Recent Developments of ECA's Overseas Investment Insurance Program

1. Major ECA's Overseas Investment Insurance Scheme

| | KEIC | EID/MITI (Japan) | OPIC (USA) | ECGD (UK) | MIGA (Multi-national) |
|--------------------------|---------------------------------------|---|--|--|---|
| Eligible Investor | Entities with legal capacity in Korea | Any person or corporation existing in Japan | U.S. citizens, corporations and foreign corporations at least 95% owned by U.S. citizens | Persons and companies carrying on business in the UK | Natural persons and juridical persons in a member country |

| | | | | | |
|-------------------------------------|---|--|--|--|---|
| | | | or commercial entities | | |
| Eligible Investments | Equity, loans, loan guarantees, rights or real estate Portfolio investment ineligible | Equity, loans, loan guarantees, rights or real estate Portfolio investment ineligible | Equity, loans, loan guarantees Portfolio investment ineligible | Equity, loans, loan guarantees Portfolio investment ineligible | Equity, loans, loan guarantees Portfolio investment eligible |
| Eligible Foreign Enterprises | No restrictions | No restrictions | Developing countries and some post-communist countries | No restrictions | Category Two (developing country) members of MIGA. Members are signatories of the MIGA Convention |
| Risks Covered | Expropriation, War, Transfer blockage, Breach of contract by host government | Expropriation, War, Transfer block, Breach of contract by host government, Bankruptcy after 2 years operations | Expropriation, War, Transfer blockage, Breach of contract by host government | Expropriation, War, Transfer blockage, Breach of contract by host government | Expropriation, War, Transfer blockage, Breach of host government commitments |
| Coverage Ratio | 90% | 95% (Political) 40% (Commercial) | 90% | 90% | 90% |

| | | | | | |
|--------------------------------|----------------|-------------------------------------|--|---|--|
| Duration | Up to 15 years | Minimum 3 years to maximum 15 years | Minimum 3 years to maximum 20 years | Minimum 3 years to maximum 15 years | Minimum 3 years to maximum 15 years |
| Maximum Amount of Cover | No Limited | US\$500M per project | US\$100M per project | No Limit | US\$50M per project |
| Waiting Period | 2 months | 2 months | Expropriation : 12 months War : None Inconvertibility : 1~2 months | Expropriation : 12 months War : 12 months Inconvertibility : 6 months | Expropriation : 12 months War : none Inconvertibility : 3 months |

VII. Case Study

1. Equity Investment in Vietnam

- Description of Project
 - Investor : Samyang Tongsang Co.Ltd
 - Host Country : The Socialist Republic of Vietnam
 - Foreign Enterprise
 - Name : Samyang Vietnam Company Ltd
 - Ownership : 100% owned by investor
 - Main Line of Business
 - Manufacturing and selling leather-footware
 - Legal Capital : US\$ 9.2 Million
 - Operation Duration : 30 years
 - Purpose of the Investment
 - To raise price competitiveness of its products by hiring relatively low-wage workers

-Korea's export promotion through the supply of the equipment and raw materials from Korea

- Details of Insurance Application
 - Insured : Samyang Tongsang Co Ltd
 - Type of Insurance : Overseas Investment Insurance (Equity)
 - Insured Investment : The amount of US\$9.2 million for paying up the capital of Samyang Vietnam Co Ltd
 - Risks Covered : Expropriation, War and Transfer blockage
 - Coverage Ratio : 90%
 - Insurance Period : 1997.1.31 ~ 2011.12.31 (15 years)

Analysis of Risks

| | Negative Factors | Affirmative Factors |
|---------------------------------------|--|---|
| Political situation | <ul style="list-style-type: none"> • Widening gap in the income level among regions and classes • Wide-spread decay and illegality • Possibility of territorial dispute with China | <ul style="list-style-type: none"> • High support to the present government • Friendly relationship with neighbours and western countries • Full diplomatic normalization with U.S.A. |
| Economic situation | <ul style="list-style-type: none"> • Excessive external debt (US\$20.4 billion outstanding as of the end of 1995, 85.1% of GDP) • Continued Current Account Deficit • Relatively high inflation | <ul style="list-style-type: none"> • Steady economic growth since 1986 (annually 6-8%) • Ample natural resources • National characteristics • Upward trend of foreign exchange reserves |
| Foreign Investment Environment | <ul style="list-style-type: none"> • Fragile banking system • Limited availability of foreign exchange | <ul style="list-style-type: none"> • Vietnamese government's aggressive efforts to induce foreign investment • Active foreign investment |

2. Loan Guarantee to Subsidiary in Papua New Guinea

- Description of Project
- Investor : Daewoo Corporation, Korea Heavy Industries & Construction Co., Ltd
- Host Country : Papua New Guinea
- Foreign Enterprise
 - -Name : Hanjung Power Pty Ltd (HPPL)
 - -Ownership : 50:50 owned by the investors
 - -Main Line of Business
 - Construction of 24 MW Diesel Power Plant in PNG's capital city, Port Moresby
 - Selling electric power to PNG Electricity Commission (ELCOM) for 15 years in accordance with the Power Purchase Agreement with ELCOM,
 - Legal Capital : US\$15.75 Million
 - Operation Duration : 15 years BOT
- Purpose of the Investment
 - to get more experience in independent power project
 - Export promotion through the supply of the equipment and raw materials from Korea
- Details of Insurance Application
 - Insured : Daewoo Corporation, Korea Heavy Industries & Construction Co., Ltd
 - Type of Insurance : Overseas Investment Insurance (Loan Guarantees)
 - Insured Investment : Loan Guarantees to financing banks by the Investors (US\$15 Million respectively)
 - Risks Covered : Expropriation, War, Transfer blockage, Breach of contract by the host government or government agency
 - Coverage Ratio : 90%
 - Insurance Period : 1997.11.1 - 2012.12.31 (15 years)

- **Analysis of Risks**

| | Negative Factors | Affirmative Factors |
|---------------------------------------|---|--|
| Political situation | <ul style="list-style-type: none"> • Disharmony of coalition cabinet • Frequent tribal disputes | <ul style="list-style-type: none"> • Close relationship with Australia • Member of International organisations such as APEC, ASEAN, etc. |
| Economic situation | <ul style="list-style-type: none"> • Weak industrial base • High inflation • Heavy external debt | <ul style="list-style-type: none"> • Surplus on current account • Increasing foreign exchange reserves • Implementation of Adjustment of Industrial Structure |
| Foreign Investment Environment | <ul style="list-style-type: none"> • Weak Infrastructure • Shortage of skilled labour | <ul style="list-style-type: none"> • Various incentives to foreign investors • Considerable mineral resources |
| Possibility of contract breach | - | <ul style="list-style-type: none"> • Strategic importance to power generation • 100% state-owned enterprise |

SECTION 12

REINSURANCE

CHAPTER I REINSURANCE

REINSURANCE

CHAPTER I

- Reinsurance is the **transfer** from one insurance company (the ceding company) to a second insurance company (the reinsurer - assuming company) all or part of a **risk** originally accepted by the first company
- As at December 31, 1996, reinsurance of \$122 million was deducted from Export Development Corporation – Canada insurance policies in force leaving a contingent liability on insurance and guarantees of \$7.4 billion
- EDC remains fully liable to policyholders for the insurance obligations with recourse to the reinsurer

Two main types of reinsurance:

- Treaty reinsurance
 - coverage on predetermined book of business
- Facultative reinsurance - EDC's Experience
 - individual risks are reinsured by offer and acceptance

Three Methods of achieving spread of risk:

- Proportional method
- Excess of Loss
- First Loss

Common types of first (and excess of) loss insurance:

- Per risk
- Per event
- Stop Loss
- Spread Loss

Common types of proportional reinsurance:

- Quota Share
- Surplus Share

Example

EDC has provided Foreign Investment Insurance to Oil and Gas Pipelines, a Canadian oil and gas transportation company, to cover the political risks associated with its equity investment in a project in Venezuela. Total insured volume is \$140 million and premium is \$3 million. ABC Reinsurance provided reinsurance of \$40 million in respect of Transfer and Expropriation risk on a first loss basis. The reinsurance premium is \$1 million.

EXAMPLE OF TERMS OF REINSURANCE AGREEMENT

- Liability
 - Reinsurer liable to EDC on a first loss basis up to \$40 million with respect to losses arising as a result of Transfer risk or Expropriation risk.
 - EDC retains for its own account 100% of the excess of Transfer and or Expropriation losses above \$40 million up to \$140 million.
- Premium
 - Full premium for EDC's share and reinsurer's share billed and received by EDC. Reinsurer to receive their share of premium within 45 days of effective date of Agreement.
- Payment of Loss by Reinsurers
 - When reinsurers liable to EDC in respect of payment of loss, EDC will give reinsurers advance notice and request payment from reinsurer of its percentage share of loss be received by EDC on the date payment is to be made to insured.
- Recoveries
 - Recoveries to be retained by EDC and shared between EDC and reinsurer on a proportional basis. Recovery expenses to also be shared on a proportional basis.

| Maximum Liability Schedule | | | | |
|----------------------------|-------------|---------------------|----------|--------------|
| Policy No: FLL-01-0001 | | | | Claims |
| From | To | Maximum Liability | | Expiry |
| Date | Date | Amount | Currency | Date |
| Feb 1,1997 | Jan 31,2002 | 140 million (GROSS) | Cdn. | Jan 31, 2003 |
| | | 40 million (CEDED) | | |
| | | 100 million (NET) | | |

REINSURANCE ACCOUNTING ENTRIES

1) GL Entries created upon issuance of policy

| | | |
|-------------------------------------|-----------|-----------|
| Premium receivable | 2,000,000 | |
| Reinsurance premium receivable | 1,000,000 | |
| Deferred premiums | | 3,000,000 |
| (to record receivables) | | |
| Deferred reinsurance premiums | 1,000,000 | |
| Reinsurance premium payable | | 1,000,000 |
| (to record amount due to reinsurer) | | |

2) Monthly recognition of premium income and provision

| | | |
|------------------------------------|--------|--|
| Deferred premiums | 50,000 | |
| Reinsurance income ceded | 16,667 | |
| Deferred reinsurance premiums | 16,667 | |
| Premium income | 50,000 | |
| (to record monthly premium income) | | |
| Provision expense | 25,000 | |
| Allowance for claims (ceded) | 8,333 | |
| Provision expense (ceded) | 8,333 | |
| Allowance for claims | 25,000 | |

(to record monthly provision expense at 50%)

1. $\$3,000,000/5 \text{ yrs} = \$600,000/12 = \underline{\$50,000}$

2. $\$1,000,000/5 \text{ yrs} = \$200,000/12 = \underline{\$16,667}$

3) Receipt of premium

| | | |
|---------------------------|-----------|-----------|
| Bank | 3,000,000 | |
| Medium term bank suspense | | 3,000,000 |

4) Allocation of cash receipt

| | | |
|--------------------------------|-----------|-----------|
| Medium term bank suspense | 3,000,000 | |
| Premium receivable | | 2,000,000 |
| Reinsurance premium receivable | | 1,000,000 |

5) Cash Disbursement

| | | |
|-----------------------------|-----------|-----------|
| Reinsurance premium payable | 1,000,000 | |
| Bank | | 1,000,000 |

REINSURANCE RECONCILIATION AT END OF POLICY TERM

| Deferred Premiums | Premium Receivable | Premium Income | | | |
|--|----------------------|-------------------|----------------------|---------------|---------------|
| 3,000,000 (2) | 3,000,000 (1) | 2,000,000 (1) | | | |
| | | 2,000,000 (4) | | | |
| | | 3,000,000 (2) | | | |
| <table style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: center; border-bottom: 1px solid black;">Provision Expense</th> <th style="text-align: center; border-bottom: 1px solid black;">Allowance for Claims</th> </tr> </thead> <tbody> <tr> <td style="border-right: 1px solid black; padding: 5px;">1,500,000 (2)</td> <td style="padding: 5px;">1,500,000 (2)</td> </tr> </tbody> </table> | | Provision Expense | Allowance for Claims | 1,500,000 (2) | 1,500,000 (2) |
| Provision Expense | Allowance for Claims | | | | |
| 1,500,000 (2) | 1,500,000 (2) | | | | |

| | | |
|----------------------------|----------------------------------|--------------------------------|
| Reinsurance Premium Rec | Deferred Reinsurance Premiums | Reinsurance Premium Payable |
| 1,000,000(1) | 1,000,000(1) | 1,000,000(1) |
| 1,000,000(4) | 1,000,000(2) | 1,000,000(5) |

| | | |
|-----------------------------|------------------------------|---------------------------------|
| Reinsurance Income Ceded | Provision Expense (Ceded) | Allowance for Claims (Ceded) |
| 1,000,000(2) | 500,000(2) | 500,000(2) |

REINSURANCE RECONCILIATION

| | |
|--------------|----------------------|
| Bank | Medium Term Suspense |
| 3,000,000(3) | 3,000,000(4) |
| 1,000,000(5) | 3,000,000(3) |

FINANCIAL STATEMENT PRESENTATION REINSURANCE

Balance Sheet

Allowance for claims

Gross \$1,500,000

Reinsurance ceded (500,000)

Net allowance for claims \$1,000,000

Note: Disclosure either on Balance Sheet or in Notes to Financial Statements.

INCOME STATEMENT

Revenues

| | |
|----------------------------|-------------|
| Gross premiums earned | \$3,000,000 |
| Reinsurance premiums ceded | (1,000,000) |
| Net premiums earned | \$2,000,000 |

SECTION 12

INTERNAL TRADE INSURANCE

CHAPTER I INTERNAL TRADE INSURANCE

INTERNAL TRADE INSURANCE

This is the insurance of local sales for non-payment arising from insolvency and default.

The principles and philosophy in export credit insurance in regard to underwriting and claim will generally apply to domestic credit insurance.

We in ECICS, Singapore started domestic credit insurance in the late 70's, not long after we started export credit insurance in 1976, by insuring indirect exports i.e. local sales to companies who in turn export same or use the goods purchased to manufacture finished goods for exports.

In 1986 when we commenced factoring, both domestic and export sales, we also extended our facility to include domestic credit insurance. Therefore, for clients who do not want funding or factoring but only credit protection we were able to offer domestic credit insurance.

Our domestic credit insurance facility is as follows:

- | | | |
|-------|-------------------------|---|
| (i) | Contracts covered | Sale of goods or services with maximum terms of 180 days. Contracts with a longer credit period is done on case by case basis. |
| (ii) | Risks covered | Insolvency Protracted Default |
| (iii) | Percentage of Indemnity | 85% |

- (iv) Ascertainment of Loss
- 1) **Insolvency**
Immediately after acknowledgement of debt by liquidator, receiver or judicial manager.
 - 2) **Default**
180 days after due date provided there is no dispute.
- (v) Amount of Loss Payable - 85% of invoice value less any set-offs, counter-claims, etc.
- (vi) Documentation - We endorse our Comprehensive Policy to cover domestic credit insurance.
- (vii) Operations
- 1) **Credit Limit**
Every buyer must have a credit limit or be covered under a discretionary limit.
 - 2) **Declarations**
Usually monthly
 - 3) **Premium**
Payable monthly on issue of invoice.
 - 4) **Bills Maturity Report**
This gives a print out of all outstanding, which is sent monthly to the exporter for him to advise whether payment has been made or not.

Domestic Credit Insurance has enabled us to develop the followings:

- (i) a good credit information database of local companies.
- (ii) build information on local market and industry trends.
- (iii) develop a credit management system through:
 - (a) ageing record of local customers
 - (b) level of failures (defaults)
 - (c) level of bankruptcies
 - (d) (b) and (c) enabled us to identify symptoms of potential defaults for the local market and by industry sector.
 - (e) marketing tool to develop export credit insurance.

The above has enabled us to joint-venture with COFACE and EFIC in a company, Credit Singapore Pte. Ltd., to provide credit information on Singapore companies and businesses which will be extending its services for companies and businesses in South-East Asia.

Domestic Credit Insurance has also enabled us to have a better feel for:

- (i) small companies;
- (ii) exempt companies, are private companies which by law are not required to file their accounts;

(iii) shareholders and directors of (i) and (ii); and

(iv) ability and credibility of (iii) as guarantors.

The information we have built-up has enabled us to provide our fellow International Credit Insurance Association (ICIA) and Berne Union members information on local companies and individuals. As credit insurers we need to know not only our overseas markets but also our own and domestic credit insurance is an indispensable part of our business as credit insurers.

SECTION 14

PRINCIPLES AND PRACTICE OF THE MANAGEMENT OF TRADE INSURANCE

CHAPTER I ORGANIZATION PRINCIPLES

CHAPTER II THE CANADIAN PERSPECTIVE

CHAPTER III MANAGEMENT OF MEDIUM TERM INSURANCE

**CHAPTER IV PRINCIPLES AND PRACTICE OF MANAGEMENT
OF AN I.T. TRADE INSURANCE SYSTEM**

CHAPTER I

ORGANIZATION PRINCIPLES

- Shared vision of objectives at all levels
- Good communication throughout the organisation
- Sound and comprehensive information systems
- Profitable performance as a key value
- Customer-driven business orientation
- Openness to outside influences
- Willingness to undertake new projects and programs
- Strong, consistent leadership
- Commitment to recruiting the best people
- Progressive Human Resources Development practices

CHAPTER II

The Canadian Perspective

Risk Management

Risk Management Office

- Optimises EDC's capacity and appetite, consistent with Corporate Business Plans and Objectives
- Assesses financial support for larger transactions recommended by business teams
- Formulates a policy framework and standards for all credit and insurance transactions
- Management of Corporate portfolio risk

- Risk Management Committee
 - Review and approve credit and concentration risks

- Asset Liability Committee
 - Membership includes President, Senior Vice Presidents of Operations and Treasury and Controller
 - Manages Asset Liability exposures on a Corporate basis including:
 - ⇒ Interest Rate, Foreign Exchange, Credit, Term Risks

- Reports to the Audit Committee of the Board of Directors

EDC Country Ratings

- Relating EDC Country Risk Ratings to probabilities of Default:

Once we determine EDC Country Risk Ratings for specific countries, we estimate expected annual probabilities of default for each EDC Country Risk Rating category.

Probabilities are estimated using:

- ⇒ EDC Economic's Department and International Markets Department analysis
- ⇒ Moody's and Standard & Poor historical data
- ⇒ OECD Consensus/Bernie Union historical data

EDC Country Limits

- After associating each country of the world into one of the 8 EDC Country Risk Rating categories, we determine an EDC Country Limit based on:
 - Probability of default pursuant to risk category
 - Canadian exporter demand
 - Country's annual exports income
 - Country's annual foreign debt service obligations
 - Country's economic variables and trends
 - Country's default history
 - Country's availability to funds from IMF programmes

Risk Analysis at Origination

- Transaction teams perform the roles of:
 - Relationship Management
 - Business Development and Marketing
 - Transaction Identification, Negotiating , and Structuring
 - Risk Credit Analyses and Presentation
- Transaction team can authorise EDC exposure subject to Delegation of Authorities
- All transactions in excess of USD5 million must be endorsed by Risk Management Office and/or Risk Management Committee

Risk Analysis at Origination

- Transaction team performs a risk analysis very similar to analysis performed by commercial bank, investment bank or insurance company
- EDC assesses and prices risk very similarly

- Credit limit and credit term of counterparty exposure is determined pursuant to risk analysis
- Commercial conditions, covenants, and events of default negotiated
- Credit surveillance benchmarks identified

Post-Commitment Portfolio Management

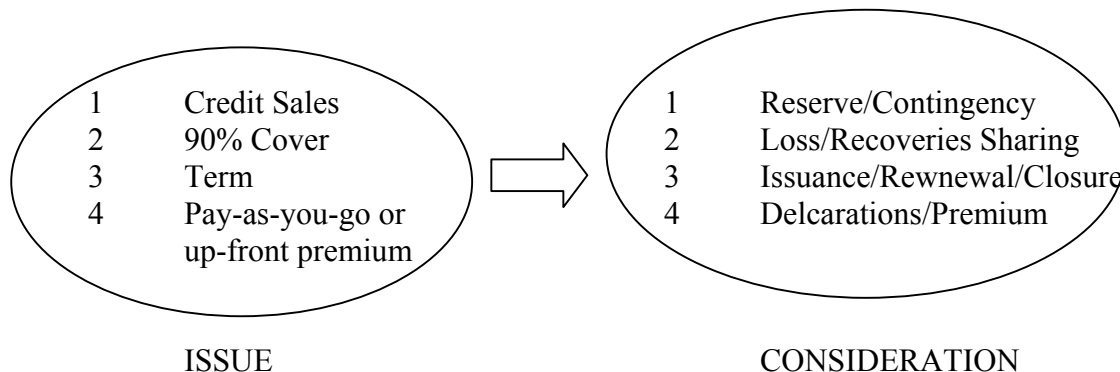
- Two Portfolio Management groups dedicated to monitoring EDC's book of assets and exposures after commitment:
 - Short term exposure
 - Long term exposure
- Monitor the credit-worthiness of all risk counterparties and country risk
- Monitor industries to which EDC has high concentration of assets or exposures
- Monitor loan covenant and conditions

Summary

- Speedy evolution of company structure in a high growth environment drives the controls needed
- Controls exist at the macro level and the micro level
- Inter linkages of all processes is growing as team focus evolves
- Controls on processes shaped by product and geared to proper financial management
- Financial Management takes place within the framework of the corporate Risk Management loop

Control Aspects & Issues

Control Considerations



Delegation of Authorities to EDC Employees

- Decision-making authorities based upon value are delegated to EDC employees to increase effectiveness of the service to the customer
- Delegation is based upon an employee's position, experience and competency
- 12 levels of authorities
 - Level 1 - Board of Directors
 - Level 12 - no delegated authorities
- The Table of Authorities sets out the dollar limits for each function of the employee

Premium Payment Process

- Short Term
 - Declaration form sent out, customised to each client
 - Entered in short term insurance computer system
- Medium Term
 - Premium paid in advance
 - Payment recorded in medium term computer system
 - Liability recorded

Claim Process

- Admissibility period based upon Risk Incurred
- Admissible Loss may be the full value declared, or less
- Verification of admissibility of the claim
 - Declarations
 - Period of cover
 - Other
- Payment decision by Claims Department
- Payment instructions to General Accounting
- Claims Accounting by Insurance Accounting

Claim Process Controls

- Operating Standards written for use by all members of the department
- Every claim is entered on database when received
- Database identifies Business Team of client which leads to the Claim Officer responsible
- Sophisticated computer reporting to control flow of work
- Computer System (CRS) controls approvals

Claims and Recoveries System

Claim Asset Control

- Paid claims carry an estimate of recovery in percentage terms
- Recovery estimates will change: Write Ups/Downs
- Asset carried on the books as long as recovery is determined to be cost effective
- If recovery prospects are not cost effective ⇒ Write Off
- Decisions taken in Claims Dept, through CRS

Claim Recoveries Control

- All incoming cheques handled by General Accounting for recording and deposit
- Data entered on CRS by General Accounting including payee and references
- Amount allocated to claim by Claims Officer

- Effect is to adjust the asset Claims Paid

Claim Reporting

- CRS is a sub-system of the accounting system
- Cash transactions handled in the accounting system when triggered by CRS
- Information breakdown, eg claims by product, by program, etc, all drawn from CRS

Business Control Summary

- Controls evolve: increasing insured volumes driving process improvements
- System of checks & balances within processes to ensure appropriate behaviour
- Cross-checks between business process and accounting processes

The Future Structure and Controls

- As EDC Corporate structure evolves, processes, controls and accounting methods must adapt
- Technology will play an important role in the evolution of EDC
- Underwriting and Claim systems upgrades
- Looking at greater asset control for all of EDC's assets

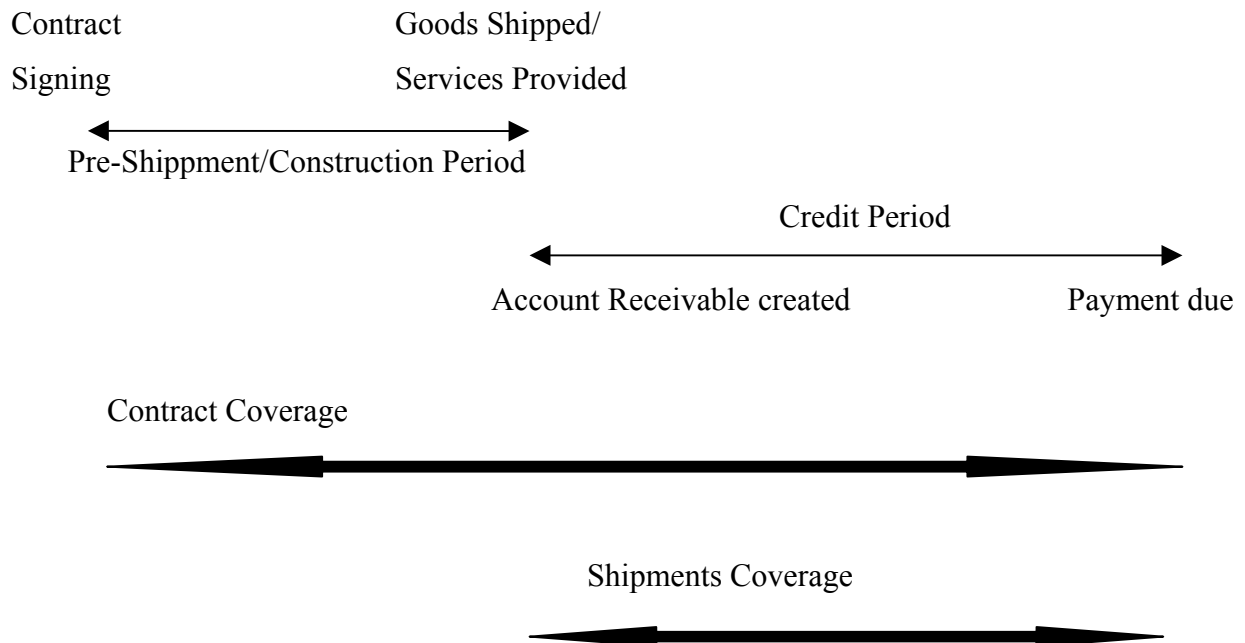
Management of Short Term Insurance

Short Term Insurance

Interface with other Systems

- Short Term Insurance pipeline
- Cash Receipts system
- Claims and Recoveries system
- General Ledger system
- Corporate Tables
- Credit Administration system

Short Term Insurance Contract



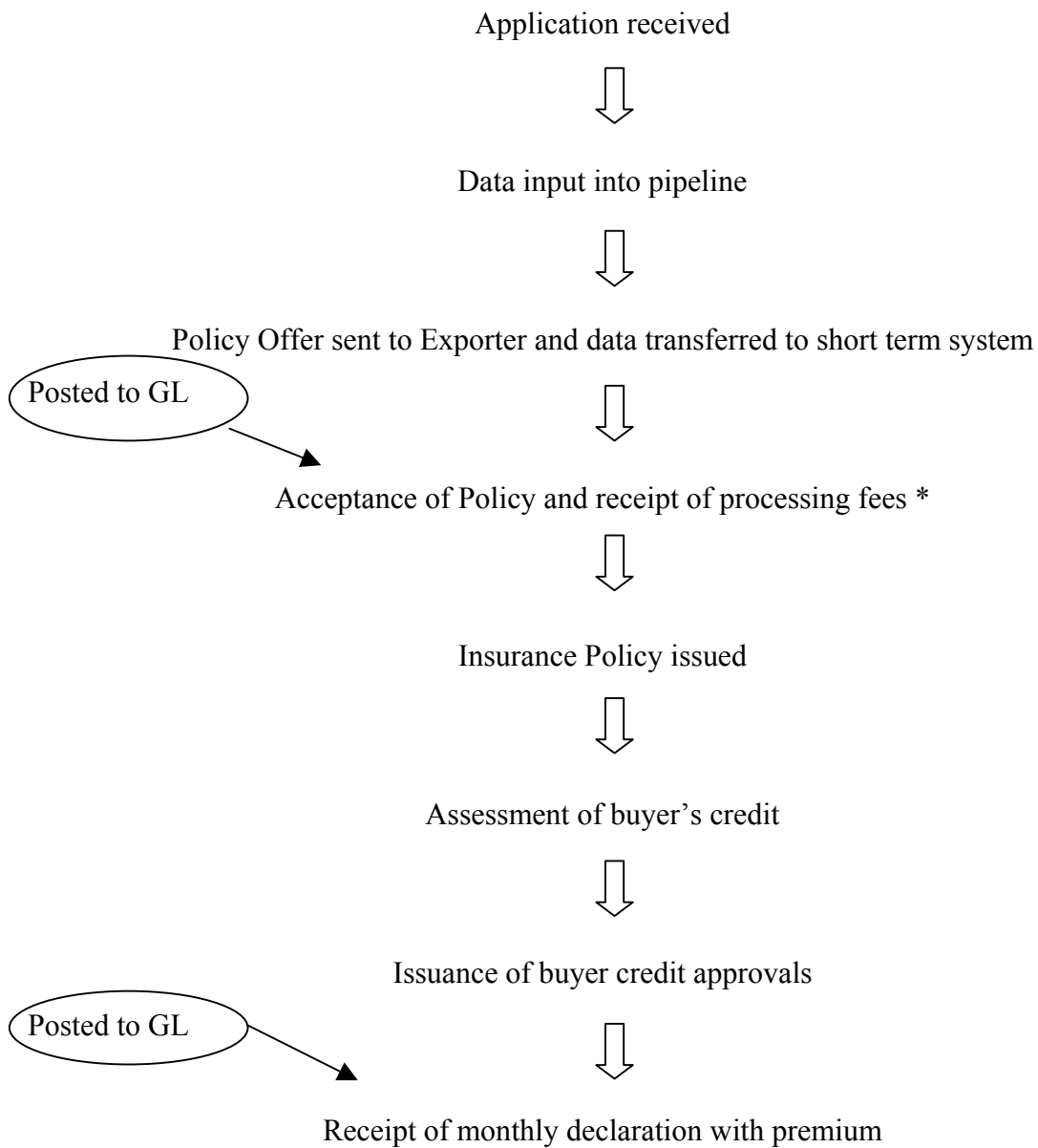
Credit Administration System

Analyse creditworthiness of buyer

- Credit reports
- Exporter's past experience
- Financial Statements

Identify level of risks related to the buyer. Also assess the buyer on a periodic basis to make sure that the level of risk remains acceptable to EDC.

Short Term Insurance



* Cheque for the processing fees is received by the Mailroom and input into the Cash Receipts system

Premiums

For short term insurance policies, premiums are taken into income at the commencement of coverage

Short Term Policy Example

EDC issues a short term Global Comprehensive policy. Coverage in the policy includes France. The processing fee is \$150.

Goods are to be shipped to France as per following schedule:

| | Amount | Terms of payment |
|----------|---------------|-------------------------|
| January | \$50,000 | net 30 days |
| February | \$66,000 | net 30 days |
| June | \$15,000 | net 30 days |

Policy Schedule

| Country | Terms | Quoted Rate* |
|---------|---------|--------------|
| Canada | 60 days | 5.00 |
| France | 60 days | 5.00 |
| Germany | 90 days | 5.10 |
| Japan | 45 days | 5.20 |

* per 100

Credit Approval

| Buyer | Term | Amount |
|----------|---------|-------------|
| Abc Cie. | 30 days | Cdn\$50,000 |
| France | | |

Continuing Credit Approval

Shipment of goods

January 15, 1997, the exporter ships Cdn \$50,000 of goods to the Abc Cie. in France with terms of payment of 30 days.

By the 10th of February, EDC should receive from the exporter the declaration form together with a cheque for the premium due on the January shipments.

The declaration will be as follows:

| Country | Term | Rate | Volume | Premium |
|---------|---------|------|--------|---------|
| France | 30 days | 5.00 | 50,000 | 2,500 |

Premium Accounting Entries

- GL Entries created upon issuance of policy and receipt of cheque processing fees

| | |
|--------------------------|-----|
| Bank | 150 |
| Short term bank suspense | 150 |

- Money applied to proper policy in short term system

| | |
|--------------------------|-----|
| Short term bank suspense | 150 |
| Processing fees | 150 |

Monthly Declaration

- Monthly declaration for previous month's shipment

| | |
|--------------------|-------|
| Account receivable | 2,500 |
| Premium income | 2,500 |

- Recognition of provision expense at 50%

| | |
|----------------------|-------|
| Provision expense | 1,250 |
| Allowance for claims | 1,250 |

- Receipt of premium and allocation to proper policy

| | |
|--------------------------|-------|
| Cash | 2,500 |
| Short term bank suspense | 2,500 |

| | |
|--------------------------|-------|
| Short term bank suspense | 2,500 |
| Accounts receivable | 2,500 |

Monthly Reconciliation

Short Term Insurance System

General Ledger

Statement of Account by policy = Accounts receivable by policy

Unallocated cash receipts = Suspense Account

General Expense

- Costs which vary indirectly with premiums such as administrative expenses are charged to expense as incurred
- Although indirect administrative expenses are not broken down by insurance program for Financial Statement presentation purposes, costs are allocated by program for internal program profitability reporting
- EDC recently installed “ABC”, an Activity Based Costing module for this purpose

Activity Based Costing

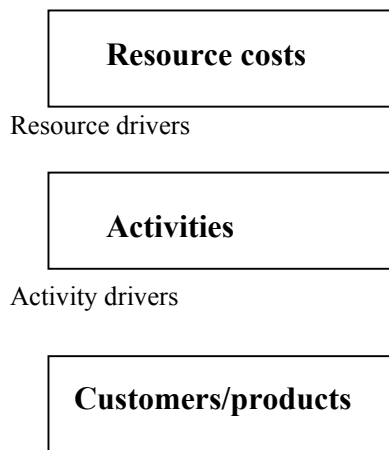
What is ABC?

- ABC goes beyond the traditional cost view by responsibility centre by restating costs according to the way resources are consumed
- Provides adequate information to properly evaluate costs by customer and costs by product
- ABC resolves misallocations by using resource and activity drivers that reflect **unique consumption** patterns and **link cause and effect** to the cost-assignment process
- ABC provides a closer match between costs and output

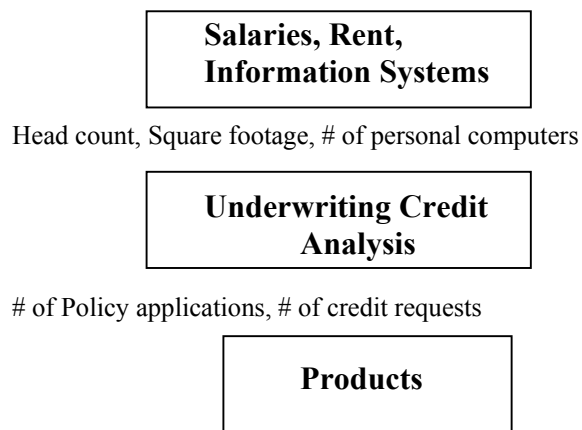
How does ABC Work

- ABC is a *two-stage* cost distribution system
 - Identify the activities that are performed within the organisation, and how these activities consume resources costs
 - Identify how these activities are consumed by each customer/product

Model



Example



Types of Activities

- There are three major types of activities:
 - **Business Sustaining:**
Costs associated with a function required to stay in business and which cannot logically be associated with Costs Objectives
 - **Cost Object Activity**
A cost object is an item that absorbs a cost and which can be reported on. Activities can be allocated to each cost object using activity drivers.
 - **Reallocation Activity**
Some activities performed may be support activities. The cost associated with these may need to be spread over other departments and activities.

INSURANCE ACCOUNTING

AGENDA

Part 2

1. Accounting Principles and Practice
2. Premiums and Expenses
3. Reinsurance
4. Claims Management
5. Foreign Exchange
6. Contingent Liabilities
7. Case Studies

Accounting Principles and Practices

- Financial Statements are in accordance with GAAP (Generally Accepted Accounting Principles)
- Canadian Institute of Chartered Accountants provides standards for complying to GAAP
- Canadian Institute of Chartered Accountants is a member of the International Accounting Standards Committee
- International Accounting Standards and Canadian pronouncements correspond very closely and differences will be pointed out

Accounting Principles and Practice

- Integrity and objectivity of Financial Statements are Management's responsibility
- Financial Statements must be approved by EDC's Board of Directors
- The Audit Committee of the Board composed of Board Members, meet regularly to review Financial Statement and accounting policies
- The Corporation is audited by the Auditor General of Canada
- The Corporation must comply with limits as set out in the Financial Administration Act

Financial Reporting in the Insurance Industry

Insurance Financial Statements are specialized due to the following reasons:

- Insurance deals in the sale of services rather than the purchase/manufacture and sale of goods. The terminology used in insurance accounting reflects this difference. However, despite these differences, the accounting principles applied are the same.
- Most business enterprises are faced with the challenge to reduce risk. However, the insurance industry deals with the assumption of risk, which is then managed by spreading it among a large population. It is this element of risk that makes the financial reporting of insurers so specialized.

Financial Reporting

- For example:
 - The major cost of the insurer (claims) can occur at any time, and sometimes not at all, during the period at risk for which the premium was received.
 - Claims can be reported to the insurer long after the expiry of the period of cover.
 - Unlike most businesses, the actual cost of the insurance product is not known at the time the product is sold. The cost, therefore, must be estimated and a liability set up. In addition developments such as inflation can affect a claim due to the timing differences between setting up of the claim estimate and the settlement date.

Financial Reporting

In view of these characteristics, problems can arise in the appropriate matching of revenue and expenses. The generally accepted approach is that.

- Premiums should be taken into the income statement evenly over the life of the policy,
- Claims should be recognized as a cost of operations and actuarial principles applied to determine appropriate reserves and
- Expenses should be charged to operations in a way to achieve a reasonable association with revenues.

Overview of Financial Statements

Balance Sheet

The Balance Sheet reflects the financial condition as at a point in time.

This statement reflects the type and value of assets, the nature and value of liabilities and the net worth of shareholders.

- **Assets**

Most of the assets of an insurer will be in the form of **investments** as most of the cash a company receives from the insurance of policies is not needed until losses occur. Since losses may occur at any time, a company must maintain a fairly liquid position. The remaining assets consist of receivables connected with normal business operations, fixed assets, deferred expenses and recoverable insurance claims.

- **Liabilities**

The two major liabilities of an insurance company are **Deferred Premiums** and the **Allowance for Claims**

Deferred Premiums (Unearned Premiums)(Premium Reserve)

Normally insurance premiums are received in advance, however, the liability only ends when either the policy expires or is cancelled. Since the premiums are received in advance the insurer has a continuing liability to return the unearned portion of the premium in the event of termination of the policy. It is, therefore, necessary for the insurer to carry this unearned portion as a liability.

Allowance for Claims (Unpaid Claims)(Claims Reserve)(Loss Reserve)

The insurer must show the liability for unpaid claims, which is intended to cover the amount necessary to settle claims which have been reported but not paid, incurred but not reported and also future claims not yet reported or incurred which will arise from the insurance policies in force.

Overview of Financial Statements

Income Statement

While the Balance Sheet is a snapshot of a company's financial condition at a particular date, the Income Statement reflects the underwriting and investment activities.

The major items of an insurer's Income Statement are:

1. Underwriting

Premiums and Fees Earned

Claims Expense (Claims Incurred)

Operating Expenses

Underwriting gain or loss

2. Investments

Investment Income

Investment Expenses

International Accounting and Reporting

- Historically, insurance accounting has varied significantly because of the different purposes for which insurers prepared annual accounts. In some countries more emphasis is placed on solvency of insurers and strength of Balance Sheet, whereas in other countries greater emphasis is placed on earnings.
- Situation has improved with European Community Directive which attempted to make difference transparent by requiring much more detail.
- The work of the International Accounting Standards Committee has improved the harmonization of regulations and accounting standards relating to the presentation of Financial Statements.
- For comparative purposes, however, it is still necessary to understand the available accounting and valuation options in each country.

CLAIMS

CLAIMS ALLOWANCE

The allowance for claims on insurance is based on an actuarial review of net loss experience and potential net losses and represents Management's best estimate of the net present value of the liability under existing policies.

CLAIMS ALLOWANCE

There are two steps in booking the expected losses to the allowance:

1. Expected loss ratios of net claims paid to premiums are calculated based on 10 year historical claims experience. Monthly charges using these rates are booked against premium income over the life of the policy and charged to the provision expense on the income statement and the claims allowance on the balance sheet.
2. At year end an actuarial valuation is calculated by EDC's actuary and the provision expense and claims allowance are adjusted if necessary.

EXPECTED LOSS RATIO AVERAGE 10 YEAR RUNOFF

| Underwriting Year | Premiums | Net Claims Paid | | Expense Ratio* |
|----------------------|----------|-----------------|--------|-------------------|
| | | 1987 | → 1996 | |
| 1987 ↓ 1996 | | | | |
| Totals | | | | |

- Net Claims Paid/Premiums

ACTUARIAL VALUATION OF THE CLAIMS ALLOWANCE

CLAIMS VALUATION

"The purpose of the claims valuation is to disclose the amount of policy and claim contingent liabilities in the Corporation's balance sheet that would make proper provision for future payments under the Corporation's **policies in force** as at December 31, 1996"

CLAIMS VALUATION

- The Valuation is comprised of:
- Provision for future claims
- Provision for incurred claims but not reported (IBNR)
- Claims reported but not yet paid (pending claims)

Claims valuation

Components:

- Provision for future claims
- Provision for incurred claims
but not reported (IBNR)
- Claims reported but not yet paid
(pending claims)

Balance Sheet

- Deferred premiums
- Allowance for claims

=

Estimation of Future Claims

- Frequency and severity model
- Frequency is estimated probability of occurrence of a claim in a single year on a single policy
- Severity is the estimated cost of the claim, expressed as a proportion of the maximum claim (ie net of recovery)
- How to estimate is dealt with later

DATA

- Extracted from EDC systems
 - Credit Approval System, Short Term system, Medium Term system and Claims and Recoveries system
- Checks for
 - Consistency
 - Continuity
 - Trend
 - Reasonableness

General Methodology

1. Provision for Future Claims (ie Obligations Not Yet Incurred or Reported)

Policy obligations on policies in force on the valuation date that will arise due to events occurring after the valuation date are determined as the present value on the valuation date of future claim payouts net of recoveries.

Coverage Period and Discount Rate

- Coverage Period
 - Medium and Long Term - Balance of policy term
 - Short term - One Year
- Discount Rate - Government of Canada Medium Term Note

Modelling

- Monte Carlo method of simulation using frequency and severity
- Use 95% confidence level
- Average or mean = expected loss and difference between mean and reserve at 95% confidence level represents Provision for Adverse Deviation (PAD)

Concentration of Risk

- Size concentration

- Country concentration
- Industry concentration
- Project concentration
- Calculated policy liability must cover
 - Expected losses (mean)
 - Provision for adverse deviation (PAD)
- Policy liability should not cover
 - Excess statistical fluctuation
 - Catastrophe
 - It is the role of capital and surplus to provide for these

KEY ASSUMPTIONS (COMMERCIAL RISK)

FREQUENCY

- Short term
 - Future O/S credit approvals by buyer
 - Expected declarations in following year under policies in force
 - Expected loss frequency
 - >> Dun & Bradstreet (U.S.) default rates by industry
 - >> Non U.S. (from Economic Unit)
 - >> Short term economic outlook (from Economic Unit)
 - >> EDC experience
- Medium term
 - Medium/long term EDC experience
 - Medium term economic outlook

Severity

- Short Term
 - Ratio of submitted claim amounts to maximum authorised credit
 - Recovery rate average
 - Coinsurance
 - Deductibles
- Medium Term

- Medium/Long term EDC experience
- Medium term economic outlook
- For Foreign Investment insurance policies, economists in Political Risk Assessment department provide estimates of expected loss severities

KEY ASSUMPTIONS (POLITICAL RISK)

Frequency

- Based on risk in higher risk countries
- Aggregate risk for each program by country
 - Assumption: if one defaults they all do

Severity

- Varies by program

2. Valuation of Incurred Claims

- Reported, not yet paid (pending)
 - Inventory per Claims and Recoveries system
 - Cost, net of recovery estimated claim by claim by EDC
- IBNR (Incurred But Not Reported)
 - Short term
 - >> Determine based on past declarations and estimated lags
 - Medium Term
 - >> No specific calculation
 - >> Any "suspected" in pending
- No reductions for expected recoveries on paid claims because those shown as asset on balance sheet

RESERVE SUMMARY FOR SHORT TERM INSURANCE

Assumptions (Commercial)

96/12/31

| | |
|---------------------------|-----|
| 1. Frequency | 1% |
| 2. Severity | |
| (a)% of authorised credit | 50% |
| (b)% recovered | 50% |
| (c) Severity | |
| (a) x {1.00-(b)} | 25% |

Results (\$M)

| | |
|---------------------------------|----|
| (a) Mean Loss | 50 |
| (b) PAD (@95%) | 25 |
| (c) Total Provision = (a) + (b) | 75 |

CLAIMS ACCOUNTING ENTRIES

Example

- 1) On October 1, EDC pays a claim in the amount of \$50,000
- 2) At the end of October, the Claims Officer estimates \$30,000 of the \$50,000 paid is recoverable
- 3) In November, the Claims Officer incurs \$2,000 in travel expenses in attempting recovery of monies owned
- 4) EDC recovers \$50,000 in December

BALANCE SHEET (000'S) AS AT DEC 31**ASSETS**

Other Assets

Recoverable Insurance Claims

Opening Balance 0

Claims Paid 50

Claims Recovered (50)

Write ups/downs 0

Total Recoverable Insurance Claims 0

LIABILITIES

Other Liabilities and Deferred Revenues

Allowance for Claims

Opening Balance 0

Provision for Claims 60

Claims Recovery Expenses (2)

Re-evaluation of Recoverable Claims 0

Allowance for Claims at End of Period 58

CLAIMS ACCOUNTING ENTRIES1) Monthly provision expense booking (year to date)

Provision expense 60,000

Allowance for claims 60,000

2) Claim Payment

Claims suspense account 50,000

Bank 50,000

(claim payment)

3) Allocation of claim payment

| | | |
|-------------------------|--------|--------|
| Claims paid | 50,000 | |
| Claims suspense account | | 50,000 |

4) Anticipated recovery

| | | |
|---|--------|--------|
| Allowance for claims | 20,000 | |
| Recoverable insurance claims write-down | | 20,000 |

(Claims department estimates anticipated recovery is 60% of amount paid. Insurance accounting adjusts recoverable insurance claims account accordingly.)

5) Claims incurs travel expenses in attempting recovery

| | | |
|----------------------|-------|-------|
| Allowance for claims | 2,000 | |
| Bank | | 2,000 |

6) Claim payment recovered

| | | |
|---------------------------------------|--------|--------|
| Bank | 50,000 | |
| Claims recovered | | 50,000 |
| (to record recovery) | | |
| Recoverable insurance claims write-up | 20,000 | |
| Allowance for claims | | 20,000 |
| (to reverse write-down) | | |

CLAIMS RECONCILIATION

| Claims Suspense | Bank | Claims Paid | Write up/down Recoverable Insurance Claims |
|-----------------|-----------|-------------|--|
| 50,000(2) | 50,000(2) | 50,000(3) | 20,000(4) |
| 50,000(3) | 2,000(5) | | |
| | 50,000(6) | | 20,000(6) |

| Allowance for Claims | Claims Recovered | Provision Expense |
|----------------------|------------------|-------------------|
| 60,000(1) | 50,000(6) | 60,000(1) |
| 20,000(4) | | |
| 2,000(5) | | |
| 20,000(6) | | |

CONSOLIDATED BALANCE SHEET AS AT DECEMBER 31, 1996

ASSETS

(\$Millions)

Cash and Investments

| | |
|--------------------------------|-------|
| Cash and marketable securities | 1,037 |
| Investments | 407 |
| Accrued Interest | 15 |

1,459

Loan Receivable

| | |
|---------------------------|-------|
| Net loans receivable | 8,048 |
| Accrued interest and fees | 140 |

8,188

Other

| | |
|------------------------------|----|
| Recoverable insurance claims | 25 |
| Other | 34 |

59

9,706

CONSOLIDATED BALANCE SHEET AS AT DECEMBER 31, 1996
 LIABILITIES (\$millions)

| | |
|--|-------------|
| Loans Payable | 7,735 |
| Loans Payable | 94 |
| | <hr/> 7,829 |
| Other Liabilities and Deferred Revenues | |
| Accounts payable | 80 |
| Deferred insurance premiums | 11 |
| Allowance for claims and guarantees | 205 |
| Deferred loan revenues and other credits | 164 |
| | <hr/> 460 |
| Shareholder's Equity | |
| Share capital | 983 |
| Retained earnings | 434 |
| | <hr/> 1,417 |
| | <hr/> 9,706 |
| | <hr/> |

CAPITALIZATION & ALLOWANCES

| | 1992 | 1993 | 1994 | 1995 | 1996 |
|---|-------|-------|-------|-------|-------|
| <hr/> | | | | | |
| S/H Equity: | | | | | |
| Capital | 788 | 788 | 813 | 851 | 983 |
| R/E | 91 | 107 | 278 | 322 | 434 |
| <hr/> | | | | | |
| Capitalisation | 879 | 895 | 1,091 | 1,172 | 1,417 |
| <hr/> | | | | | |
| Allowances: | | | | | |
| Loans | 609 | 751 | 935 | 1,256 | 1,458 |
| Insurance | 98 | 111 | 149 | 181 | 205 |
| Treasury | 6 | 13 | 13 | 20 | 20 |
| <hr/> | | | | | |
| Allowances | 713 | 875 | 1,097 | 1,457 | 1,683 |
| <hr/> | | | | | |
| Capitalisation & Allowances | 1,592 | 1,770 | 2,188 | 2,630 | 3100 |
| Non-accrued capitalised Interest (NACI) | 828 | 843 | 929 | 927 | 998 |
| <hr/> | | | | | |
| Total Capitalisation & Allowances and NACI | 2,420 | 2,613 | 3,117 | 3,557 | 4,098 |
| <hr/> | | | | | |
| % increase from prior year | | 8.0% | 19.3% | 14.1% | 15.2% |
| <hr/> | | | | | |

FOREIGN EXCHANGE

- All ending monetary balances on the Balance Sheet are translated to Canadian dollars calculated at month end conversion rates.
- All monetary income and expense amounts for the period on the Income Statement are calculated at month average rates
- Foreign Exchange gains and losses arise when there is a difference between the exchange rate used on Financial Statement translation and the foreign exchange rate in effect on the transaction date (or previous month end close exchange rate for opening balances carried forward)
- Foreign exchange gains/losses should be taken into income as incurred to remove monthly distortions, EDC books gains and losses evenly over the year

FOREIGN EXCHANGE RISK

- Foreign exchange risk exists where there is a mismatch between assets and liabilities in any currency
- This risk should be measured, monitored and controlled
- Treasury Strategy Guidelines provide acceptable exposures

Contingent Liabilities

- Contingent liabilities are an off-balance sheet item and are disclosed in the Notes to the Financial Statements.
- The corporation is subject to a limit imposed by the Export Development Act on its contingent liability programs. The Act specifies that the corporation's contingent liabilities in respect of the principal amounts owing under all outstanding arrangements shall at no time exceed \$ 15 billion, an amount equal to ten times the authorised capital of the Corporation. As at December 31, 1996, the position against this limit is \$8.9billion (1995 - \$7.9 billion).
- The contingent liability is calculated as the insured volume x the cover rate (normally 90%) minus any claim payments.
- The contingent liability remains in force until the claims expiry date is reached.

S.T. Contingent Liability – Top 5 Countries

1. Iran
2. Mexico
3. Brazil
4. Canada
5. U.S.

Short – term contingent Liability 1996 - \$5,081 million

M.T. Contingent Liability – Top 5 Countries

United Kingdom

Argentina

Turkey

Colombia

Canada

1996 Medium – term contingent Liability \$2,351 million

CHAPTER III

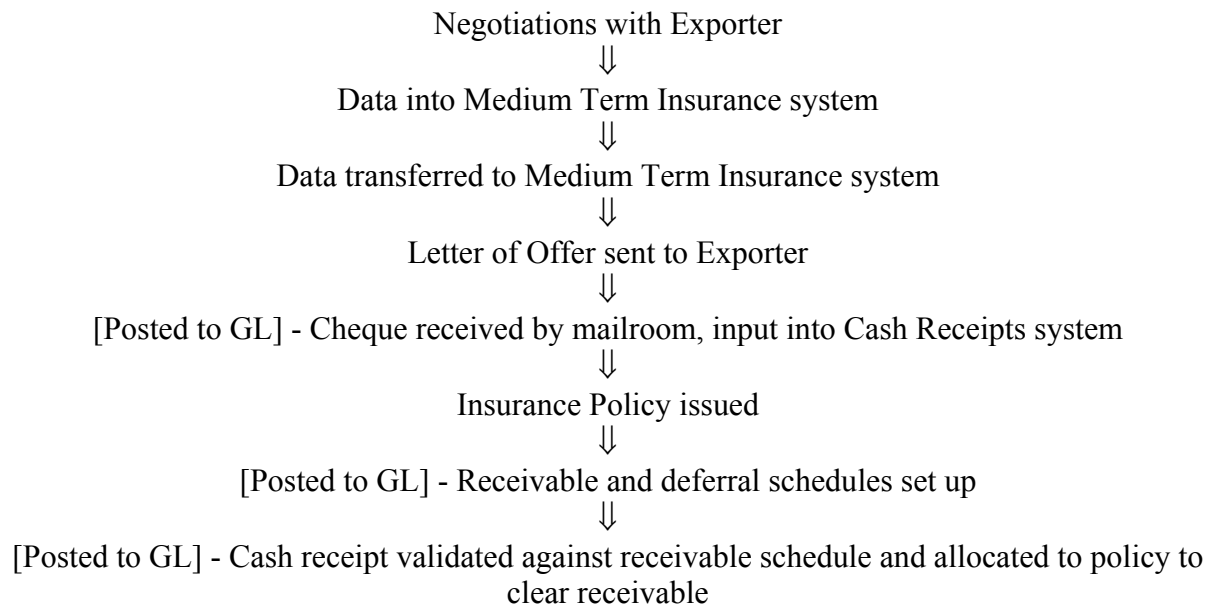
Management of Medium Term Insurance

Medium Term Insurance

Interface With Other Systems

- Medium Term Insurance Pipeline system
- Cash Receipts system
- Claims and Recoveries system
- General Ledger system
- Corporate Tables

Medium Term Insurance



Premiums

For medium term policies, premiums are taken into income using methods which reflect the exposures over the terms of the policies

Expenses

Direct Expenses

- Generally direct expenses should be expensed in the same period as the related revenue.
- Up front expenses such as broker fees and commissions which do not cover ongoing services and are not recoverable are expensed as incurred.

Indirect Expenses

- Indirect expenses are which cannot be directly allocated to a specific policy (eg general office expenses and salaries)
- Indirect expenses are expensed as incurred.

Medium Term Policy Example

Example 1

EDC issues a Specific Transaction insurance policy with a five year term to insure the export of Canadian goods to Venezuela. Total insured volume is \$1 million and total premium is \$60,000. The business is done through a broker and the broker fee is \$6,000. The expected average loss rate is 50% of net premium income.

*(In this case the broker **dose not provide ongoing service** and the broker fee expense is **not recoverable**. Expense, therefore, is expensed at commencement of coverage)*

Policy Details

| | | | |
|-----------------------|--------------------------|--------------|----------------------|
| Policy Number: | <u>STI-01-00001</u> | Status: | <u>Policy Issued</u> |
| Policy Holder: | <u>ABC Marine</u> | Status Date: | |
| Exporter: | <u>ABC MARINE</u> | Underwriter: | <u>Jane Doe</u> |
| Buyer: | <u>Atlas Ltd.</u> | | |
| Country: | <u>Venezuela</u> | | |
| Classification: | <u>High Risk</u> | | |
| Selection of Act: | <u>Corporate Account</u> | | |
| Insured Amount: | <u>\$1,000,000</u> | | |
| Issued Date: | <u>Feb 1, 1997</u> | | |
| Period of Cover From: | <u>Feb 1, 1997</u> | To: | <u>Jan 31, 2002</u> |
| Claims Expiry Date: | <u>April 30, 2002</u> | | |

Premium Accounting Entries

GL entries created upon issuance of policy

1) Set up of premium receivable

| | | |
|---------------------|--------|--------|
| Premiums receivable | 60,000 | |
| Deferred Premiums | | 60,000 |

2) Set up of broker fee payable and expense broker fee

| | | |
|--------------------|-------|-------|
| Broker fee expense | 6,000 | |
| Broker fee payable | | 6,000 |

3) Receipt of premium

| | | |
|---------------------------|--------|--------|
| Bank | 60,000 | |
| Medium term bank suspense | | 60,000 |

4) Allocation of cash receipt

| | | |
|---------------------------|--------|--------|
| Medium term bank suspense | 60,000 | |
| Premiums receivable | | 60,000 |

5) Cash disbursement

| | | |
|--------------------|-------|-------|
| Broker fee payable | 6,000 | |
| Bank | | 6,000 |

6) Monthly recognition of premium income

| | | |
|---|--------------------|-------|
| Deferred Premiums | 1,000 ¹ | |
| Premium income | | 1,000 |
| (recognition of monthly premium income) | | |

1. $60,000/5\text{yrs} = 12,000/12 = \underline{1,000}$

7) Monthly recognition of provision expense at 50%

| | | |
|----------------------|-----|-----|
| Provision expense | 500 | |
| Allowance for claims | | 500 |

(1,000 * .50 = 500)

Accounting Reconciliation at End of Policy Term

| | | | | | | | | | | | | | | | | | | | | | | | | |
|--|----------------------|--|-------|--|-----------|-----------|--|-----------------------|--|-------------------------|--|----------|-----------|--|-----------------------|--|------------------------|--|-----------|--|-----------|--|--|-----------|
| <table border="0"> <tr><td colspan="2" style="text-align: center;">Bank</td></tr> <tr><td colspan="2" style="text-align: center;">-----</td></tr> <tr><td style="width: 50px;">60,000(3)</td><td style="border-left: 1px solid black; width: 50px;"></td></tr> <tr><td></td><td style="border-left: 1px solid black; text-align: right;">6,000(5)</td></tr> </table> | Bank | | ----- | | 60,000(3) | | | 6,000(5) | <table border="0"> <tr><td colspan="2" style="text-align: center;">Medium Term Suspense</td></tr> <tr><td colspan="2" style="text-align: center;">-----</td></tr> <tr><td style="width: 50px;">60,000(4)</td><td style="border-left: 1px solid black; width: 50px;">60,000(3)</td></tr> </table> | Medium Term Suspense | | ----- | | 60,000(4) | 60,000(3) | <table border="0"> <tr><td colspan="2" style="text-align: center;">Premiums Receivable</td></tr> <tr><td colspan="2" style="text-align: center;">-----</td></tr> <tr><td style="width: 50px;">60,000(1)</td><td style="border-left: 1px solid black; width: 50px;"></td></tr> <tr><td></td><td style="border-left: 1px solid black; text-align: right;">60,000(4)</td></tr> </table> | Premiums Receivable | | ----- | | 60,000(1) | | | 60,000(4) |
| Bank | | | | | | | | | | | | | | | | | | | | | | | | |
| ----- | | | | | | | | | | | | | | | | | | | | | | | | |
| 60,000(3) | | | | | | | | | | | | | | | | | | | | | | | | |
| | 6,000(5) | | | | | | | | | | | | | | | | | | | | | | | |
| Medium Term Suspense | | | | | | | | | | | | | | | | | | | | | | | | |
| ----- | | | | | | | | | | | | | | | | | | | | | | | | |
| 60,000(4) | 60,000(3) | | | | | | | | | | | | | | | | | | | | | | | |
| Premiums Receivable | | | | | | | | | | | | | | | | | | | | | | | | |
| ----- | | | | | | | | | | | | | | | | | | | | | | | | |
| 60,000(1) | | | | | | | | | | | | | | | | | | | | | | | | |
| | 60,000(4) | | | | | | | | | | | | | | | | | | | | | | | |
| <table border="0"> <tr><td colspan="2" style="text-align: center;">Deferred Premiums</td></tr> <tr><td colspan="2" style="text-align: center;">-----</td></tr> <tr><td style="width: 50px;">60,000(6)</td><td style="border-left: 1px solid black; width: 50px;">60,000(1)</td></tr> </table> | Deferred Premiums | | ----- | | 60,000(6) | 60,000(1) | <table border="0"> <tr><td colspan="2" style="text-align: center;">Premium Income</td></tr> <tr><td colspan="2" style="text-align: center;">-----</td></tr> <tr><td></td><td style="border-left: 1px solid black; text-align: right;">60,000(6)</td></tr> </table> | Premium Income | | ----- | | | 60,000(6) | <table border="0"> <tr><td colspan="2" style="text-align: center;">Provision Expense</td></tr> <tr><td colspan="2" style="text-align: center;">-----</td></tr> <tr><td style="width: 50px;">30,000(7)</td><td style="border-left: 1px solid black; width: 50px;"></td></tr> </table> | Provision Expense | | ----- | | 30,000(7) | | | | | |
| Deferred Premiums | | | | | | | | | | | | | | | | | | | | | | | | |
| ----- | | | | | | | | | | | | | | | | | | | | | | | | |
| 60,000(6) | 60,000(1) | | | | | | | | | | | | | | | | | | | | | | | |
| Premium Income | | | | | | | | | | | | | | | | | | | | | | | | |
| ----- | | | | | | | | | | | | | | | | | | | | | | | | |
| | 60,000(6) | | | | | | | | | | | | | | | | | | | | | | | |
| Provision Expense | | | | | | | | | | | | | | | | | | | | | | | | |
| ----- | | | | | | | | | | | | | | | | | | | | | | | | |
| 30,000(7) | | | | | | | | | | | | | | | | | | | | | | | | |
| <table border="0"> <tr><td colspan="2" style="text-align: center;">Allowance for Claims</td></tr> <tr><td colspan="2" style="text-align: center;">-----</td></tr> <tr><td></td><td style="border-left: 1px solid black; text-align: right;">30,000(7)</td></tr> </table> | Allowance for Claims | | ----- | | | 30,000(7) | <table border="0"> <tr><td colspan="2" style="text-align: center;">Broker Fee Payable</td></tr> <tr><td colspan="2" style="text-align: center;">-----</td></tr> <tr><td style="width: 50px;">6,000(5)</td><td style="border-left: 1px solid black; width: 50px;">6,000(2)</td></tr> </table> | Broker Fee Payable | | ----- | | 6,000(5) | 6,000(2) | <table border="0"> <tr><td colspan="2" style="text-align: center;">Broker Fee Expense</td></tr> <tr><td colspan="2" style="text-align: center;">-----</td></tr> <tr><td style="width: 50px;">6,000(2)</td><td style="border-left: 1px solid black; width: 50px;"></td></tr> </table> | Broker Fee Expense | | ----- | | 6,000(2) | | | | | |
| Allowance for Claims | | | | | | | | | | | | | | | | | | | | | | | | |
| ----- | | | | | | | | | | | | | | | | | | | | | | | | |
| | 30,000(7) | | | | | | | | | | | | | | | | | | | | | | | |
| Broker Fee Payable | | | | | | | | | | | | | | | | | | | | | | | | |
| ----- | | | | | | | | | | | | | | | | | | | | | | | | |
| 6,000(5) | 6,000(2) | | | | | | | | | | | | | | | | | | | | | | | |
| Broker Fee Expense | | | | | | | | | | | | | | | | | | | | | | | | |
| ----- | | | | | | | | | | | | | | | | | | | | | | | | |
| 6,000(2) | | | | | | | | | | | | | | | | | | | | | | | | |

Financial Statement Presentation

BALANCE SHEET

ASSETS

| | |
|---------------------|------------------------|
| Cash | \$54,000 |
| Premium | <u>0</u> |
| TOTAL ASSETS | <u>\$54,000</u> |

LIABILITIES AND SHAREHOLDER'S EQUITY

LIABILITIES

| | |
|--------------------------|----------------------|
| Broker fee payable | 0 |
| Deferred Premiums | 0 |
| Allowance for Claims | <u>30,000</u> |
| TOTAL LIABILITIES | <u>30,000</u> |
| NET INCOME | <u>24,000</u> |

| | |
|---|------------------------|
| TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY | <u>\$54,000</u> |
|---|------------------------|

INCOME STATEMENT

| | |
|------------------------------|------------------------|
| Premiums and Fees Earned | \$60,000 |
| Broker Expense | <u>(6,000)</u> |
| Net Premiums and Fees Earned | <u>54,000</u> |
| Provision Expense | <u>(30,000)</u> |
| NET INCOME | <u>\$24,000</u> |

Medium Term Insurance

| Fee Summary | | |
|-------------------------|------------------|----------------|
| Policy No: STI-01-00001 | | |
| Currency: Cdn | | |
| Installment Type | Total Receivable | Total Received |
| Risk Premium | 60,000 | 60,000 |

| Cash Receipts | | | | | | |
|---------------|--------------|------|----------------|-----------|-----------------|-----|
| Document# | Receipt Date | Curr | Receipt Amount | System ID | Unallocated AMT | APP |
| DDB5820 | Feb 11,1997 | Cdn | 60,000 | MTI | 0 | X |

Medium Term Policy Example

Example 2

EDC issues a Specific Transaction insurance policy with a five year term to insure the export of Canadian goods to Venezuela. Total insured volume is \$1 million and total premium is \$60,000. The business is done through a broker and the broker fee is \$6,000. The expected average loss rate is 50% of net premium income.

(In this case broker provides ongoing service and the broker fee expense is recoverable. Broker fee is, therefore expensed in the same period as the related premium revenue.)

Premium Accounting Entries

All journal entries are the same as required for Example 1 except for the following entries:

2) Set up of broker fee payable and deferral

| | | |
|--------------------|-------|-------|
| Deferred premiums | 6,000 | |
| Broker fee payable | | 6,000 |

Monthly recognition of broker fee expense

| | | |
|--------------------|------------------|-----|
| Broker fee expense | 100 ¹ | |
| Deferred premium | | 100 |

1. $6,000/5\text{yrs} = 1,200/12 = \underline{100}$

Medium Term Insurance

Endorsements

- An endorsement is a change in an existing policy which may result in either an additional premium, a return premium, or no premium adjustment. Endorsements may be made at any time during the policy term.
- The accounting for endorsement premiums is the same as accounting for original premiums.
- Examples of endorsements include extending or reducing period of cover, increasing or decreasing insured amounts.
- An endorsement cannot adjust a prior period after the period has been balanced and closed.

Monthly Reconciliations

The Accounting Administrator:

- Reconciles receivable, deferral and revenue balances in the Medium Term Insurance System to ending balances in the General Ledger
- Reconciles unallocated cash receipts in Cash Receipts system to medium term suspense account balance in General Ledger
- Notifies underwriters of all policies with receivable balances

Case Studies

Premiums

Example 1

On October 1, a short - term policy is issued to cover insured volumes of \$ 1,000,000 in Algeria. The processing fee is \$200.

Required:

Record the journal entries required to account for the following events:

- 1) On October 1, the processing fee of \$200 is received.

- 2) On November 10 1997, a declaration is received from the exporter with a premium cheque in the amount of \$10,000. The expected loss rate is 50% of premium income.

Answer to Example 1

| | | |
|---|--------|--------|
| 1) Bank | 200 | |
| Short term bank suspense (receipt of processing fee) | | 200 |
| short term bank suspense | 200 | |
| processing fees (processing fee applied to policy) | | 200 |
| | | |
| 2) Accounts receivable | 10,000 | |
| premium income (set up of accounts receivable and recognition of premium income) | | 10,000 |

| | | |
|--|--------|--------|
| Provision expense | | |
| Allowance for claims | | 5,000 |
| (recognition of provision expense) | | |
| Bank | 10,000 | |
| Short term bank suspense | | 10,000 |
| (receipt of premium) | | |
| Short term bank suspense | 10,000 | |
| Accounts receivable | | 10,000 |
| (allocation of premium to proper policy) | | |

Example 2

A medium term insurance policy with a premium amount of \$ 120,00 is issued to cover insured volumes of \$ 2,000,000. The period of cover s from January 1, 1997 to December 31, 2001 and the Claims Expiry date is December 31, 2002. The export's co-insurance ration is 10%. The expected loss rate is 50% of premium income. There is no broker involved.

A) Record the journal entries required to account for the following events:

- 1) The policy is issued on January 1, 1997. Record the set up of the receivable and deferred accounts
- 2) The premium amount of \$120,000 is received on January 10, 1997. Record the allocation of the cash receipt.
- 3) Record the premium income and provision expense account entries for the month of January

B) What is the balance remaining in the Deferred Premium account on December 31, 1997?

C) What is the Contingent Liability for this policy?

D) When does the Contingent Liability expire?

Answer to Example 2.

A)

| | | |
|--------------------------------|---------|---------|
| 1) Premium receivable | 120,000 | |
| Deferred premium | | 120,000 |
| (to record premium receivable) | | |

| | | |
|--------------------------------|---------|---------|
| 2) Bank | 120,000 | |
| Medium term bank suspense | | 120,000 |
| (to record receipt of premium) | | |

| | | |
|---------------------------|---------|---------|
| Medium term bank suspense | 120,000 | |
| Premium receivable | | 120,000 |
| (to allocate receipt) | | |

| | | |
|---|-------|-------|
| 3) Deferred premiums | 2,000 | |
| Premium income | | 2,000 |
| (to record premium income = $\$ 120,000/5 = \$ 24,000/12 = \$2,000$) | | |
| Provision expense | 1,000 | |
| Allowance for claims | | 1,000 |
| (to record provision expense = $\$ 2,000*.50$) | | |

B) Deferred Premium at December 31, 1997

| | |
|---------------------|------------|
| Opening Balance | \$ 120,000 |
| Less premium earned | (24,000) |
| Ending Balance | \$96,000 |

C) Contingent Liability = \$ 1,800,000
($\$2,000,000* .90$)

E) The Contingent Liability expires on December 31, 2002 which is the claim expiry date

Case Studies

Expenses

Example 3

Refer to example 2.

What additional accounting entries would be required if a broker was involved in providing the business and a non-recoverable fee of \$10,000 was charged by the broker?

Answer to Example 3

| | | |
|--|--------|--------|
| Broker fee expense | 10,000 | |
| Broker fee payable | | 10,000 |
| (to record set up of broker fee payable and expense) | | |
| Broker fee payable | 10,00 | |
| Bank | | 10,000 |
| (to record payment of broker fee) | | |

Example 4

If the broker in example 3 provided ongoing services throughout the policy, describe how the accounting treatment would differ from example 3.

Answer

The broker fee would be expensed over the life of the policy.

Case Studies

Foreign Exchange

Example 5

On October 3, 1997, premium in the amount of U.S. \$ 100,000 is received for an insurance policy. The Financial Statements of the insurer are translated to Canadian dollars.

The daily close exchange rates are as follows:

| | |
|-------------------|--------------------|
| October 3, 1997 | US\$ = \$1.40 Cdn. |
| October 31, 1997 | US\$ = \$1.50 Cdn |
| November 30, 1997 | US\$ = 1.35 Cdn |

- 1) What is the exchange rate gain or loss on the Income Statement for the period ended October 31, 1997?
- 2) What is the exchange rate gain or loss on the Income Statement for the period ended November 30, 1997?

Answer to Example 5

| <u>1) Assets</u> | <u>US\$</u> | <u>Exchange Rate</u> | <u>Cdn Equivalent \$</u> |
|-------------------------------|--------------------|-----------------------------|---------------------------------|
| Oct 3, 1997 | \$100,000 | 1.4 | \$140,000 |
| Oct 31 1997 | \$100,000 | 1.5 | \$150,000 |
| Foreign Exchange Grain | | | <u>\$10,000</u> |

Note: *In this case the US\$ has appreciated in value relative to the Cdn \$, therefore since this is an asset account there is a foreign exchange gain on translation.*

| <u>2) Assets</u> | <u>US\$</u> | <u>Exchange Rate</u> | <u>Cdn Equivalent \$</u> |
|------------------------------|--------------------|-----------------------------|---------------------------------|
| Oct 31, 1997 | \$100,000 | 1.5 | \$150,000 |
| Nov 30, 1997 | \$100,000 | 1.35 | \$135,000 |
| Foreign Exchange Loss | | | <u>(\$ 15,000)</u> |

Note: *In this case the US\$ has depreciated in value relative to the Cdn\$, therefore since this is an asset account there is a foreign exchange loss on translation.*