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CENTRAL BANK OF BELIZE

EXPORT CREDIT INSURANCE

Paper prepared by Roger Bradley
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History

The concept of export credit insurance originated in the city of Berne, Switzerland in 1906 when a company by the name of Federal in Switzerland began insuring exporters against non-payment by buyers abroad on a profit-making basis. Shortly thereafter export credit insurance companies were established in Spain, Germany and France, as private export credit insurers. The first ever government-owned export credit insurance company originated with the establishment of the Export Credit Guarantee Department of the United Kingdom.

In 1934, in the city of Berne, Switzerland, three private export credit insurance companies, along with the Export Credit Guarantee Department of the U.K., founded an association called the Berne Union, the function of which was to provide for the exchange of information concerning export credit among its members in order to enhance the operations of these insurance companies. As time went on, the Berne Union became broader and accepted other export credit insurance companies, as well as others who were involved with investment insurance. At present, the Berne Union membership consists of 40 export credit insurance companies from 32 nations.

Prior to World War II, exporters were insured only against commercial risks, as there were merchants exporting at the time who found it necessary to secure some degree of protection from these insurance companies. However, due to World War II, the concept of political risk had to be implemented as an

additional risk to be protected against due to the fact that the warfare between the countries involved greatly multiplied the risks involved in export trading. The post-war period saw the take-off of export credit insurance and it became very popular in developed countries, and later, developing countries. Besides the Berne Union, other possibilities of setting up more export credit institutions in other countries are being explored.

Introduction

The prime objective of export credit insurers is to provide export credit insurance. Based on these principles export credit insurers also provide bank guarantees to enable exporters to obtain bank finance at the pre-shipment and post-shipment stages.

The insurance policy insures exporters of goods and services against non-payment or delayed payment by buyers abroad due to commercial and political risks. The bank guarantees, comprised of a pre-shipment credit guarantee and a post-shipment credit guarantee, insure commercial banks against non-payment of advances taken by exporters due to insolvency and protracted default of exporters. Normally commercial banks require 100 - 150 percent security against advances granted to the most experienced exporters. With new exporters they are even more hesitant to advance credit. The guarantee, in essence, is an incentive for commercial banks to advance credit on easier terms to exporters.

A study has been done concerning the feasibility of export credit insurance for Belize, however the results have not been disclosed, therefore my paper will be of an information nature rather than an analytical one.

Principles of Export Credit Insurance

Before looking at the concepts of the insurance policy and the bank guarantees more closely, there are a few basic principles of export credit insurance that have been accepted by countries in which this system operates.

1) An applicant for export credit insurance must have an insurable interest, that is, he must have an interest in insuring his exports against non-payment by buyers abroad due to commercial and political risks.

2) The information on the application form is accepted by the export credit insurer in 'utmost good faith'.

3) The holder of the scheme is expected to disclose all material facts about the buyer.

4) Once the export credit insurer pays its portion of the loss to the holder, that latter should make an effort to recover whatever portion of the loss he can. This principle is called indemnification.

5) The principle of co-insurance exists under the policy, that is, under any policy the policy loss will be shared between the export credit insurer and the holder of a policy.

The Insurance Policy

As mentioned earlier the insurance policy insures exporters against non-payment by buyers abroad due to commercial and political

risks. Commercial risks involve: 1) insolvency, 2) protracted default and 3) delayed payment. For this type of risk the export credit insurance company is liable for up to 80 percent of the loss. Political risks include: 1) war and civil disturbances, 2) imposition of import controls, 3) exchange control regulations, 4) cases whereby a ship is unable to dock at the port of a specific country to unload an effected shipment, thereby causing the ship to be diverted to the port of another country, incurring heavy losses, 5) any other cause not being the inherent nature of the goods, but beyond the control of the buyer. Risks not covered include: 1) risks arising due to exchange rate fluctuations, 2) disputes arising due to quality and quantity of goods and 3) mortality of animals.

Type of Shipments Covered

1) Shipments against letters of credit, and those on DP (documents against payment) and DA (documents against acceptance) terms from 30 up to 180 days are covered under the short-term insurance policy. The latter two are protected against both commercial and political risks, while the former is protected only against political risks. Shipments on LC terms include shipments to associate concerns or subsidiaries, those made on consignment basis, and shipments made to agents. In the case of non-payment due to political risk, the export credit insurer will be liable for up to 85 percent of the loss.

Operation of the Policy

Exporters must apply for a credit limit in respect of each buyer. The buyers are analysed and screened based on their credit-worthiness, value of shipments and his country's political and economic situation. Status and agency reports are often called for from banks and credit information agencies respectively, in the screening process.

Terms and Conditions of the Policy

Once a policy is issued, the following terms and conditions have to be adhered to.

1) The exporter is obliged to declare all his shipments covered under the insurance policy within a stipulated period after the shipment using special declaration forms provided by the credit insurer.

2) Remittances of premia, as agreed in the policy, are sent along with the monthly declarations.

3) Approval of buyers must be obtained from the export credit insurer prior to the shipment.

4) The exporter should notify the corporation of all material facts pertaining to the insurance policy.

5) Notification of overdue shipments must be furnished to the export credit insurance company monthly.

6) most important, the exporter should take reasonable care and prudence in effecting shipments, for example, an importer should in no uncertain terms effect a second shipment to the same buyer, when proceeds from the first shipment have not yet been realised.

7) The exporter should not disclose to the buyer that he possesses an insurance policy, thereby avoiding multiplicity of the probability of non-payment situations.

Advantages of the Insurance Policy

1) Losses may be minimised by screening the buyer and buyer's country.

2) The insurance company can be indemnified once losses are recovered by the exporter.

3) The exporter only sustains above 15 - 20 percent of possible losses.

Bank Guarantees

The bank guarantees, as was mentioned earlier, are designed to insure commercial banks against non-payment of advances given to exporters due to insolvency and protracted default. Two of the main types of bank guarantees are: 1) pre-shipment credit guarantee and 2) post-shipment credit guarantee. I will explain the two schemes in more detail.

Pre-Shipment Credit Guarantee

The prime objective of the pre-shipment credit guarantee scheme is to allow exporters to secure credit on easier terms from commercial banks at the pre-shipment stage.

The scheme is a revolving credit agreement, thereby making credit continually available once repayment of advances are made. The non-availability of bank finance for the execution of export orders in order to effect shipment by a required date. Exporters need capital for purchase of raw materials, manufacturing, processing, packing and final preparation of goods for export. Inability to raise this capital could result in the exporter losing both the buyer and the market. It is in view of these facts and situations that give rise to the need for the pre-shipment credit guarantee. This guarantee is designed as an incentive for commercial banks to advance credit to exporters at the pre-shipment stage on more liberal terms, insuring them against non-payment by exporters due to insolvency or protracted default. Normally, export credit insurance companies provide protection of around 65 - 75 percent of the loss that may be sustained by commercial banks and not to the importer. As the insurance cover provided by the export credit insurance company is for a higher limit, the banks need not ask for 100 percent security from the exporter.

The commercial banks are urged to seriously adhere to the terms and conditions of the policy as adherence will be used as a major part of the criterion used to determine whether a claim is paid or nor. The usual principles of export and credit insurance will apply to the pre-shipment scheme.

Terms and Conditions of the Pre-Shipment Scheme

Once a pre-shipment scheme is granted, the following terms and conditions must be adhered to:

1) The commercial banks are obliged to declare all advances to exporters under the scheme within a stipulated period using special declaration forms provided by the credit insurer.

2) Remittances of premia, as agreed in the scheme, are sent along with the monthly declarations.

3) Approval of exporters must be obtained from the export credit insurer prior to the shipment.

4) The commercial banks should notify the corporation of all material facts pertaining to the pre-shipment scheme.

5) Notification of overdue advances must be furnished to the export credit insurer monthly.

6) most important, the commercial banks should take reasonable care and prudence in granting advances, for example, a commercial bank granting advances over a certain period will not blindly continue to grant advances unless repayments are being made. The company will only be liable for about 65 - 75 percent of the loss.

Advantages of the Scheme

The advantages of the scheme include: 1) encouraging exporters to export more, 2) to attract new exporters into the export business, 3) to open up new markets and 4) to promote new export products.

The Post-Shipment Credit Guarantee

Many countries insist on the policy as a pre-condition for issue of the post-shipment credit guarantee. Exporters need financial assistance at the post-shipment in order to continue their working capital. Without this type of facility importers may not be able to export goods to buyers abroad on credit terms nor fill present orders because of lack of finance. In view of these needs, the post-shipment credit guarantee scheme is provided to the commercial banks. It is designed to protect commercial banks from losses in respect of advances granted to exporters in respect of advances granted to exporters in respect of bills purchased or negotiation of export bills. This will enable commercial banks to extend post-shipment finance on more liberal terms. Like the pre-shipment scheme, it is revolving facility thereby always making credit available to the exporter as long as they fulfil the terms and conditions of the contract. The principles of export credit insurance inva-

riably applies to the post-shipment scheme. Similar terms and conditions as in the pre-shipment scheme need to be adhered to.

Operation of the Policy

The pre-shipment credit guarantee is granted to commercial banks on behalf of exporters based on exporter's performance under the insurance policy and advances are granted up to a permitted limit. The banks are again advised to take necessary care and prudence in advancing credit to importers during the post-shipment stage. The advantages of the post-shipment credit guarantee is to help exporters to continue in export business after shipment without being constrained by the inadequacy of working capital and offers the incentive to commercial banks to offer credit to exporters on easier terms.

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