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Export Insurance: New capacities on the Parisian market

Update after our 2010 article

Expert analysis and views from France ARNAUD, founder and head of the independent broker SOL MONDO.

2011 started with an explosion of popular movements in different countries, incidents which could disturb foreign economic interests. These current events justify growing interest for insurance possibilities offered to French companies. Expert point of view follows:

These incidents can disturb foreign economic interests in different ways: in affecting the sequence of commercial contracts in process or the functioning of investments realized in the country, leading to damage of the goods or a stand-still in their production .

It is necessary to have a quick reminder of the notion of political risk from the insurer's point of view. What are the facts leading to a claim: political events, social movements followed by physical insecurity, dysfunction of administration, ports and airports… As many facts that have or could have occurred during political tensions in Tunisia, Egypt, Ivory Coast, as well as in Libya , Bahrain, Yemen, Oman, Morocco, or Saudi Arabia…

A new government can offer to renegotiate contracts signed by his predecessor to obtain technical or financial arrangements or even to reconsider them radically because public strategy has changed: this is the "Fait du Prince" ! Political risk can also happen on the exporter's side, if his mother country recommends to repatriate his citizens or even forbids deliveries into a troubled country.

In Libya, the violence of the repression has led the United Nations to adopt sanctions, repeated and hardened by the European ministry Council. The embargo decided on all equipment likely to be used for internal repression has frozen the execution of all current contracts. It is the same as for sanctions decided by the European Union against some companies in Ivory Coast.

The importance of contractual clauses

For these contracts, the main question now is: Of what quality are the contractual clauses?

When political risk appears, the exporter re-reads the contract signed with the buyer and suddenly realizes the importance of the quality of the wording of contractual clauses: how is the "force majeure" clause written? Is it possible to suspend work easily without penalties? In front of which tribunals to enforce rights in the first place, and if troubled times continue, will it be possible to ask for compensation for the loss incurred and receive the appropriate compensation for this loss?

Are bonds conditional or at first demand, « autonomous » from the contract. If yes, are they protected by a sentence detailing, for example, that they can't be called in case of "force majeure"?

In front of these risks, a private insurance market offers adjustable covers, according to the contracts, the market has doubled between 2007 and 2011.

From 600 million to 1 billion euros available per operation

A specialized market with increasing capacity

As opposed to the banking system and to the short term credit insurance, the market of medium term covers has stayed very active even though the 2008 crisis, with the rising of new capacities and opportunities between 2009 and 2010, even on very difficult countries.

This market of political risk is a mature market, born more than thirty years ago following the needs of major multinational corporates (investors and exporters) wanting to cover significant financial risk. It is a worldwide market with subscription centers in Paris, London, Singapore, Australia, the United States and Geneva where the brokers can access as soon as competition and syndication are justified.

The technical specificity and the importance of unitary amounts of risk on this market justify indeed the intervention of specialized brokers who operate following very secured rules and procedures at each step of the process of instruction, placement-binding and follow up. Most insurers on this market refuse to interfere without the assistance of a specialized broker to the client.

Available capacities in Paris :one third of the world market.

Our Moci press release in April 2010 already described very high market capacities. Since then, these have been reinforced by the arrival or three new significant actors: Euler Hermes and Liberty Mutual in Paris and Starr Insurance in London. They bring another capacity of 150 million euros per operation. The French Market now represents one third of world capacities with nine subscription offices.

Here are the capacities :

-On a private buyer, the theoretical global capacity per operation is evaluated to about 600 million euros on risks up to a 7 year term.

- On a public buyer, the theoretical global capacity per operation is evaluated to more than one billion euros on incurred risk for the insurance of contracts, which answers the needs of contracts of much higher nominal amount.

All insurers on this market can engage themselves for 5, 7, 9 or even 15 years if the context of the operation justifies so.

The products: securing of the contracts and protecting the investments.

The market allows to insure investments against confiscation, expropriation, destruction during riots, civil troubles or terrorist attacks.

- Contracts

For the contracts, covers concern financial risk before and after delivery -these are called manufacturing risk and non-payment risk-as well as protection of bonds issued in profit of the buyer.

Before delivery, when it is a special manufacturing, engaged expenses are insured above received payments. Risk appears when political events or the insolvency of the debtor prevent the good functioning of the contract and lead to a premature interruption. This risk exists each time the contract describes the sale of specific products which cannot be sold as they are, to another buyer.

If the buyer is a private project company created « ad hoc »for an operation (non free/paying public service infrastructure), it is particularly important to insure the interruption of contract risk, because, even if the contract stipulates the right for compensation of engaged expenses above received payments, in case of contract interruption, by definition, the company of this project while work is in progress is not solvent.

After delivery, the market insures payments through simple transfers (if the buyer is well known) or through letters of credit (or non-honoring of payment Guarantees). If payments are made through a letter of credit, insurers can:

- Guaranty payments up to 90 or 95%.
  If all conditions for the payment of the letter of credit are brought together, and if the issuing bank is not paying, the exporter can receive compensation for the insured part of the letter of credit. This is what happened in Kazakhstan and in Ukraine when local banks failed.

- Insure the « non-certification » by the buyer. This means to compensate the exporter on his manufacturing risk, which are engaged expenses above received payments when the buyer abusively retains necessary documents and signatures for the payment.

Indeed, letters of credit anticipate often the presentation of various and large number of documents, any material mistake can lead to non-payment. For these cases of « abusive non -certification », insurers offer to complete the non-payment warranty of the letter of credit through a mechanism of compensation of engaged expenses above received down payments . This loss is designated as a «manufacturing risk».

Bonds, when they are at first demand, can be called if the exporter is not fulfilling its contractual obligations, even if he is stopped by a case of force majeure (political violence, withdrawal of export licenses, embargo …). When bonds are insured, the exporter may be compensated of the amount of the bond called as soon as the leading fact is political, independent from the exporters will.

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