

Credit Risk & Trade Credit Insurance

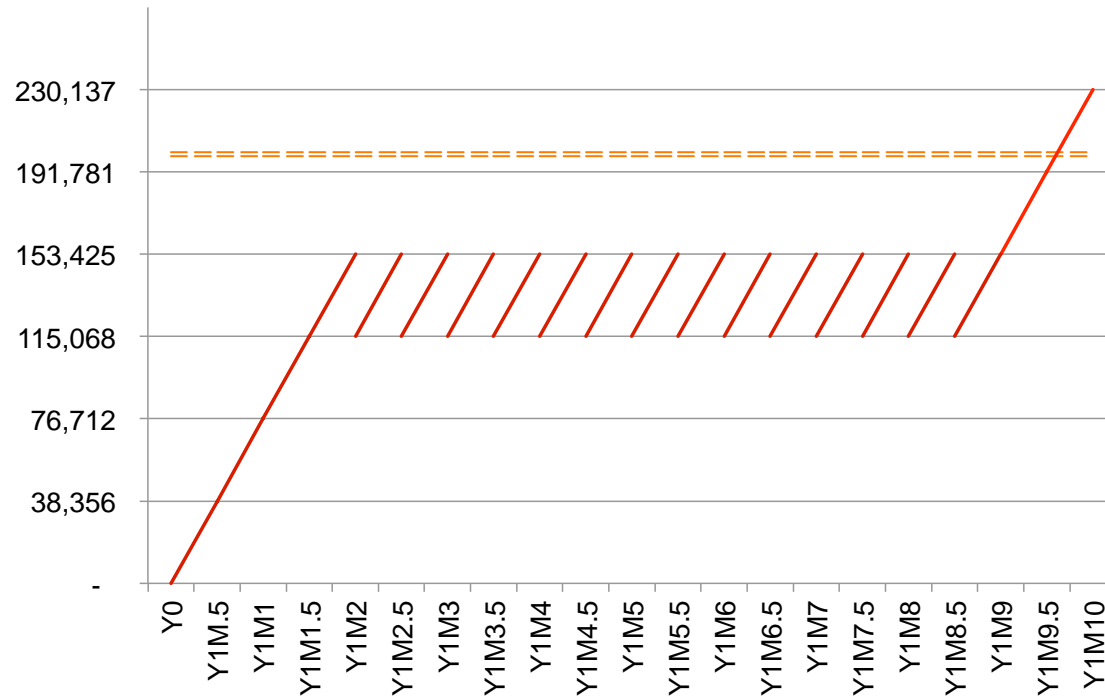
Dr. Aleš Berk Skok, CAIA, FRM

Finance professor @ SEB LU

Managing partner @ ALPHA CREDO d.o.o.



Accounts Receivable Dynamics



Every buyer has its own specific pattern.

Accounts receivable are an aggregate of these individual patterns.

Trade Credit Insurance Program

Trade credit insurance (in its core) offers:

1. Informed risk-taking by having a thorough overview of the portfolio of buyers and their (*updated*) credit ratings
2. Transfer of default risk due to:
 - (any kind of) insolvency procedures
 - protracted payments
3. Transfer of debt collection costs

Who are the stakeholders?

SALES

KYC is key at developing sales strategy and then negotiating with buyers.

Only paid accounts receivable lead to achieving sales goals

RISK

Determining the risk profile

Impact analysis on the business

Risk mitigation

FINANCE

Realization vs. the budget

Securing liquidity (cash flow)

BOARD

Reward/Risk at the company level

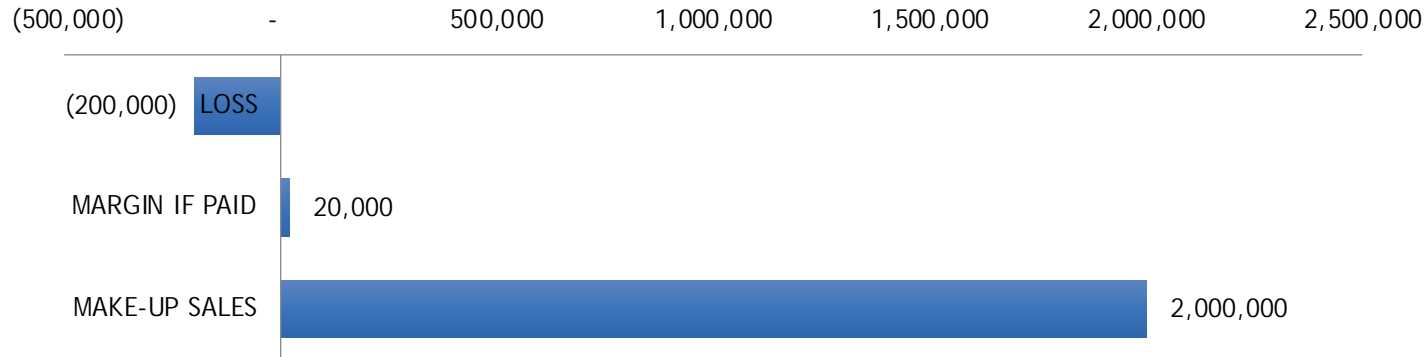
Is credit risk really worth keeping in books?

Advantages of Trade Credit Insurance Programs

- Balance the trade-off: risk-taking vs. commercial demands
 - Outsourcing credit risk and additional sale potential (additional margin earned)
- Securing liquidity (default causes: 1/ necessity to replace the buyer (and more), 2/ liquidity gap)
- Coverage of collection costs
- Constant overview of quality of a buyer portfolio with up-to-date information
- Become a supplier with a privileged payment status
- Time-saving when managing defaults
- Improved credit rating of the insured as assets insured and performance less volatile
- Improved negotiating power towards various stakeholders (bank, buyers, suppliers)

Credit insurance program should depend on the business model -> Important role of an Insurance Broker

How Defaults Impact Margins



LOSS	Margin on sales & required make-up sales							
	1% Margin		5% Margin		10% Margin		20% Margin	
	MARGIN IF PAID	MAKE-UP SALES	MARGIN IF PAID	MAKE-UP SALES	MARGIN IF PAID	MAKE-UP SALES	MARGIN IF PAID	MAKE-UP SALES
5,000	50	500,000	250	100,000	500	50,000	1,000	25,000
50,000	500	5,000,000	2,500	1,000,000	5,000	500,000	10,000	250,000
200,000	2,000	20,000,000	10,000	4,000,000	20,000	2,000,000	40,000	1,000,000
1,000,000	10,000	100,000,000	50,000	20,000,000	100,000	10,000,000	200,000	5,000,000
RATIO		100		20		10		5



(500,000) - 500,000 1,000,000 1,500,000 2,000,000 2,500,000

Example of an Insured Event

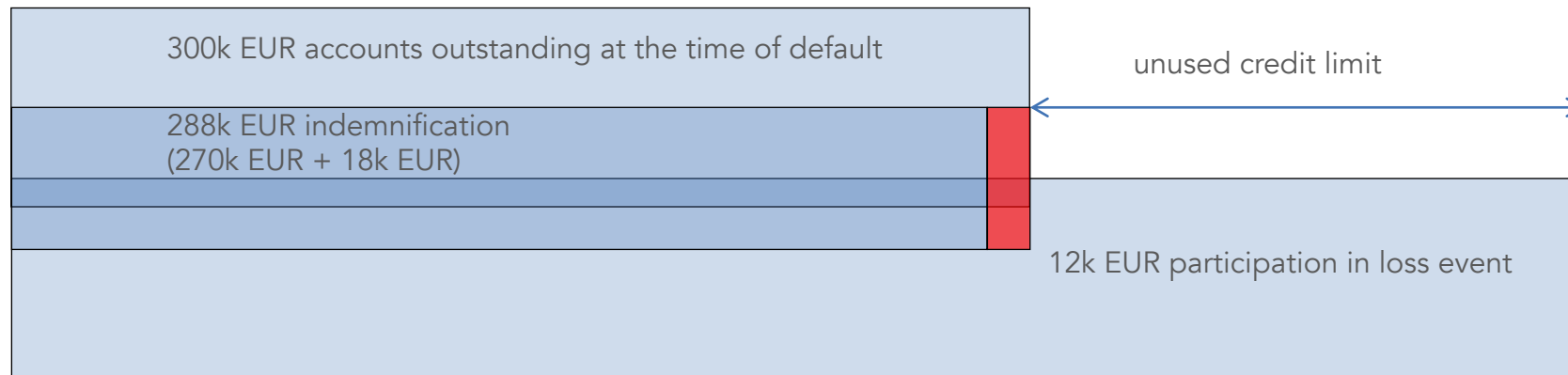
Annual turnover with the buyer: 5 mio EUR (with soe seasonality)

Credit limit: 500k EUR (30 days payment term)

Accounts outstanding at the time of credit default: 300k EUR

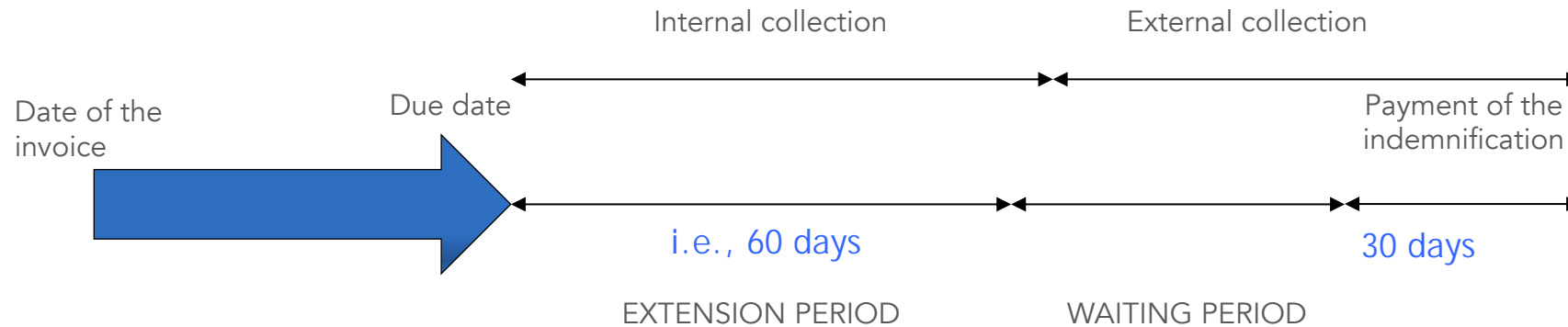
Loss Participation: 10%

Collection costs: 20k EUR

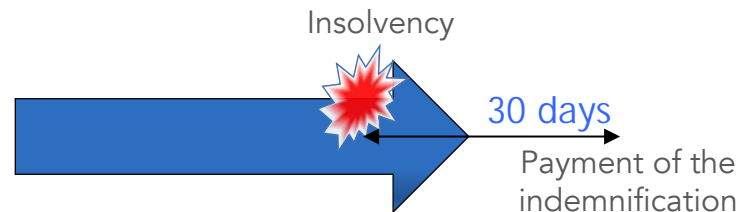


Timeline around an Insured Event

PROTRACTED PAYMENT



INSOLVENCY



Supply Chain Finance

Implemented Trade Credit Insurance enables additional possibilities to further improve credit rating of the insured by the use of various non-recourse trade finance solutions

ASSETS		LIABS	
cash	14		
inventory	20	34	AccP
AccRec	40	80	debt
FA	60	20	equity
TOTAL	134	134	TOTAL

ASSETS		LIABS	
cash	14		
inventory	20	34	AccP
AccRec	10	50	debt
FA	60	20	equity
TOTAL	104	104	TOTAL

280	Annual sales
0.77	Sales/day
52.14	DSO
requir. cash	5%
EBITDA%	10%
EBITDA	28
NFD	80
NFD/EBITDA	2.9

EBITDA%	10%		
EBITDA	28		
NFD	50		
NFD/EBITDA	1.8	38%	reduction



Why Should Companies Cooperate with a Knowledgeable Broker?

- In an extremely complex environment of credit risk management, the Broker, with an established approach, typically significantly improves the quality of the insurance program (cover, costs, operational simplicity).
- By understanding the client's business model, the broker designs optimal insurance solutions and delivers it from (international) insurance markets.
- Broker offers more comprehensive solutions compared to a selected insurance company.
- Broker is obliged to protect interests of a client and NOT the insurance company.
- Specialised Broker has an up-to-date overview and access to domestic and international insurance capacities and significantly reduces information asymmetry.
- The Broker services are free of charge for the client, as insurance legislation requires insurance company pays part of the distribution costs to the broker.
- The Broker contributes significantly to better operational monitoring of the insurance contract, especially in terms of insurance coverage, changed terms of business and claims settlement.

Contact

Dr. Aleš Berk Skok, CAIA, FRM

Managing partner, Ins. Broker (licence #: 40110-0945/2014-4)

ALPHA CREDO d.o.o.

Specialized Credit Insurance Brokerage

Dunajska cesta 159

1000 Ljubljana

www.alpha-credo.com

ales@alpha-credo.com

+386/41/85 85 35