berneunion

YEARBOOK 2020

About

Berne Union Publications

The Berne Union publishes a regular digital industry newsletter, and print periodicals in the Spring and Autumn, as well as interim reports on industry research and statistics.

'The BUlletin' is a bi-monthly newsletter digest of news, views and statistics providing a window into the industry for business partners across the world of trade and export finance.

Our print periodicals curate thought pieces and high-level commentary from industry leaders, presented alongside the Berne Union's data on new commitments, exposure, claims and recoveries in export credit and investment insurance.

About the Berne Union

The International Union of Credit and Investment Insurers (Berne Union) is an international not-for-profit trade association, representing the global export credit and investment insurance industry. Our mission is to actively facilitate cross-border trade by supporting international acceptance of sound principles in export credit and foreign investment. This is achieved by providing a forum for professional exchange, sharing of expertise and networking among members, as well as through engagement in collaborative projects with other stakeholders from across the wider trade finance industry.

Collectively, our members provide payment risk protection for approximately 13% of world annual cross-border trade in goods and services (amounting to $2.5 trillion annually) and since the start of the global financial crisis in 2008, have paid out more than $60 billion in claims.

Production Credits

Executive editor
Paul Heaney, Berne Union

Contributing editor
Katharine Morton, TXF

Production editor
John Smith, TXF

Content planning
Vinco David, Berne Union
Paul Heaney, Berne Union
Katharine Morton, TXF
Dan Sheriff, TXF

Cover design
Constantina Christophide, TXF

For advertising enquiries please contact
Alex Sheriff, Senior Relationship Manager
alex.sheriff@txfmedia.com

berneunion

International Union of Credit & Investment Insurers
1st Floor
Thanet House
231-232 The Strand
London WC2R 1DA
United Kingdom

Tel: +44 (0)20 7841 1110
Fax: +44 (0)20 7430 0375

www.berneunion.org

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Introduction

The Berne Union: Who's Who in 2020/21

The Berne Union is led by the President, Vice President and Management Committee. The Management Committee meet at least four times per year to discuss the strategic direction of the association and provide guidance on operational issues.

The day to day business of the Berne Union is managed by a professional Secretariat, based in London, under the leadership of the Secretary General, Vinco David.

The Management Committee consists of:

- President
- Vice President
- 4 Committee Chairs
- 13 Member Organisations

The 13 Member Organisations are held as institutional positions. These are held by the two largest member organisations from each of the Short Term, Medium/Long Term and Investment Committees. The remaining seven members are put forward from among all four Committees on a voluntary, rotating, basis, also serving for two year terms.

Management Committee 2020/22

President:
Michal Ron (SACE)

Vice President:
Christina Westholm-Schröder (SOVEREIGN)

Short Term Committee Chair:
Julian Hudson (CHUBB)

ECA Committee Chair:
Robert Suter (SERV)

MLT Committee Chair:
Dominique Meessen (CREDENDO)

Prague Club Committee Chair:
Imaad Al Harthy (CREDIT OMAN)

Institutional Members:

- AXA XL
- CREDENDO
- ECGC
- EH GERMANY
- EXIAR
- EXIMBANKA SR
- ICIEC
- KSURE
- MIGA
- PwC
- SINOSURE
- TURK EXIM
- US EXIM

Elected Officials

PRESIDENT

Michal Ron

SACE Italy | Chief International Officer

With extensive experience in structured finance and export credit, Michal is the Chief International Officer of SACE, holding responsibility for the Group's International Relations, Overseas Network and Political Credit Recovery.

She manages SACE's active participation within the OECD and the EU, as well as the relationship with the peer group. Over the past 10 years, she has steered the expansion of SACE's overseas network, supervising international underwriting generated by the 12 offices abroad. Her responsibilities also include all activities related to the Paris Club and other political recoveries.

From 2017 to September 2020 Michal served as the first Secretary General of the International Working Group (IWG). She is currently the Vice Chairman of the Board of Directors of the African Trade Insurance Agency (ATI).

Prior to working at SACE, she spent 10 years at Mediocredito Centrale (Head of Oil, Gas and Petrochemicals, Structured Finance) and seven years with HSBC. With a Business Studies, Risk Management and Finance BSc Honours degree from City University Business School (London, renamed CAAS), Michal has worked in investment banking in several European countries and has been invited to speak in numerous conferences worldwide.

VICE PRESIDENT

Christina Westholm-Schröder

Sovereign Bermuda | Senior Vice President & Chief Underwriter

Christina Westholm-Schroder is Sovereign's Chief Underwriter and Senior Vice President, with more than 30 years of experience in the political risk insurance industry. She is responsible for all aspects of Sovereign's transactional underwriting. Christina also leads Sovereign's successful cooperation with multilaterals and ECAs.

Prior to joining Sovereign, she was a senior officer at the Multilateral Investment Guarantee Agency (MIGA) in Washington, DC. She joined MIGA as one of the first employees and worked in several managerial capacities before assuming the role of Head of Reinsurance. In her earlier career, she worked as a financial analyst and as a broker in Sweden and at Bank of America in New York. Christina has been active in the Berne Union representing Sovereign for a number of years.

She has served on the BU's Management Committee since 2014, and previously held the positions as Chair of the Investment Committee and, before that, Chair of the Technical Panel. She has further served on various working groups, including the Data and Outreach Task Forces. In addition to her BU activities, Christina is also an Alternate Director on the Board of ATI (the African Trade Insurance Agency).

Christina has a degree in international business from Stockholm School of Economics and Business Administration and an MBA in finance from New York University.

ST COMMITTEE CHAIR

Julian Hudson

CHUBB United Kingdom | Global Head of Trade Credit

Julian has 24 years' experience in political risk and credit insurance. He commenced his career as an underwriter with Trade Indemnity (now Euler Group) in London before moving to Asia in 1999 to assume a regional broking role with Jardine Lloyd Thompson in both Singapore and Hong Kong.

Julian relocated to Singapore in January 2007 where he joined ACE (now Chubb) as the Regional Manager for Political Risk & Credit business and established the Asia practice. In July 2014, he moved back to London in the capacity of Chief Development Officer, Political Risk & Credit within Chubb Global Markets where, in addition to day-to-day underwriting responsibilities, he was involved with the promotion of new political risk and credit insurance products, the establishment of new overseas offices and capabilities, and the provision of solutions for multinational companies. In November 2015, he was made Global Head of Trade Credit.

Julian's experience ranges from short-term trade transactions to medium-term specialty credit through to sovereign and sub-sovereign non-payment risk, and protecting debt and equity flows into a variety of projects.

ECA COMMITTEE CHAIR

Robert Suter

SERV Switzerland | Head of International Relations & Business Policy

After completing a Master's degree in International Affairs & Governance from the University of St. Gallen, Switzerland, Robert Suter joined the International Relations team at SERV and has lead this growing team since 2014. It now includes International & Government Relations, Business Policy, Sustainability Analysis and Bank & Country Risk Analysis. He has participated in international negotiations on Official Export Credit Support at the OECD and the IWG as a member of the Swiss delegation and represented SERV at various international conferences and forums, including the Berne Union, for many years.

MLT COMMITTEE CHAIR

Dominique Meessen

CREDENDO Belgium | Head of Reinsurance

Dominique spent 25 years in Credendo ECA's Underwriting and Account Management department where he occupied different positions, including management roles.

In September 2018, Dominique joined Credendo's Reinsurance department. He is currently Head of Reinsurance and is responsible for both Outward and Inward reinsurance activities in Credendo. Dominique has extensive experience in Credit and Political Risk insurance from an ECA perspective but also from a private player perspective thanks to Credendo market activities.

He has attended Berne Union meetings for almost 15 years. He was Chair of the Technical Panel Meeting of the Investment Insurance Committee in 2007 and 2008. Before joining Credendo, Dominique briefly worked in a business law firm in Brussels. Dominique holds a Master's Degree in Law (LL.M.) from the Université Catholique de Louvain (Belgium).

PC COMMITTEE CHAIR

Imaad Al-Harthy

Credit Oman | General Manager Sales

Imaad AL-HARTHY is the General Manager Sales at Oman's national ECA: Credit Oman SAOC with 24 years of experience in underwriting, claims, recoveries, and various management positions. After completing a BA (Hons) in Business Studies from Nottingham Trent University, UK in July 1995, Imaad joined Credit Oman and has been part of its development and evolution. He has been involved with the Prague Club since 2001 and was part of the taskforce that concluded the integration of PCC with Berne Union in 2016.

ST COMMITTEE VICE CHAIR

Sunil Joshi

ECGC India | Executive Director

Sunil joined ECGC in 1988 and over the past 32 years has had comprehensive experience in both the short term and medium- and long term business of ECGC.

He has led client interaction teams on the ground and has also spearheaded design and development of product, policy, and procedures of both its short term and medium- and long term business. He has worked extensively in claims arising from export credit insurance cover extended to banks, which also constitutes the largest segment of ECGC's short term business.

As head of the International Relations Department he has handled ECGC's interactions at bilateral and multilateral forums. He has been a panellist at several international conferences and has published articles on international trade and credit insurance. Sunil holds a Masters' Degree in Physics.

ECA COMMITTEE VICE CHAIR

Irene Gambelli

SACE Italy| Senior Advisor for International Relations

Irene Gambelli is an International Relations specialist at SACE, the Italian Export Credit Agency, looking after company's relationship with foreign ECAs, MDBs and other international institutions, and representing Italy's position within the OECD and EU, including negotiations and working groups on policy-related issues and topics that steer export credit business. She has been with SACE since 2006, spending three years in the underwriting area and additional four years coordinating the business strategy and origination activities of SACE's overseas network in major emerging and developed economies.

Within the Berne Union, from 2014 to 2016, she assisted the former President and Vice President in developing key reforms and initiatives aimed at fostering organisational improvement and visibility worldwide. She has been an active member of Berne Union's focus group on SMEs from 2014 to 2019 and is currently involved in ongoing initiatives on data and digitalisation.

Before joining SACE, Irene worked six years for a business law firm in Rome. She holds a Masters' degree in Political Sciences from the University of Rome, Italy, and a postgraduate certificate in Advanced Marketing and Business Communication from ISM Rome.

MLT COMMITTEE VICE CHAIR

Andrew Underwood

AXA XL | Chief Underwriting Officer – Specialty, UK and Lloyd's

Andrew Underwood is Chief Underwriting Officer, Speciality Insurance, UK and Lloyds at AXA XL. Before joining AXA XL, Andrew was a partner at Hiscox, holding progressively more senior roles in London and New York. He has 30 years' experience in specialty insurance and reinsurance, namely political risk, trade credit and bond, crisis management, cyber, media and entertainment, and mergers & acquisitions.

He is ACII qualified, a past Chair of the Lloyd's Market Association Political Risks, Credit and Financial Contingencies Panel and the current chair of the International Underwriting Association Political Risk Insurance Committee. He is also a regular speaker at industry conferences and is a passionate contributor on regulatory matters, particularly those affecting Insurers and Financial Institutions. He first began working with the Berne Union in 2008.

PC COMMITTEE VICE CHAIR

Martina Jus

HBOR Croatia | Executive Director – International Affairs, Export Credit Insurance, EU Funds and Financial Instruments

Martina Jus joined the Croatian Bank for Reconstruction and Development (HBOR) in 2005 as a legal counsel, following her admission to the State Bar. She has worked in several capacities at HBOR since then, including a management board position. Currently she is the Head of Division for International Affairs, Export Credit Insurance, EU Funds and Financial Instruments. She has been particularly invested in the development of new products and positioning of HBOR on the international market. Martina also served as a member of the Management Board of the Croatian Agency for Small and Medium Enterprises (HAMAG) from 2012 to 2014. Martina holds a Master's Degree in Law from the University of Zagreb (Croatia).

Secretariat

SECRETARY GENERAL

Vinco David

Overall leadership of the Secretariat

Vinco David was appointed Berne Union Secretary General in March 2017. Prior to this, he has served as a Management Committee Member and as the Chair of the Investment Insurance Committee. A Dutch national, he has over 30 years' experience in various aspects of credit and investment insurance, including more than 20 with leading international credit insurer Atradius, in diverse management roles across strategy, product development, economic research, project finance, marketing, underwriting and claims.

Before joining the Berne Union as Secretary General, Vinco David served as a Management Team Member of Atradius Dutch State Business, the Export Credit Agency of the Netherlands. Prior to this he has held positions at the Berne Union Secretariat and the Netherlands Ministry of Finance. He holds an MA in political science and international relations and a BA in economics and Italian language and literature from the Free Reformed University of Amsterdam.

ASSOCIATE DIRECTOR

Laszlo Varnai

Coordination of the MLT Committee

Laszlo joined the Secretariat in June 2015, to advise it on legal matters and to support the Committees (primarily the ST Committee) and Specialist Meetings. Since April 2017, Laszlo has been supporting the MLT Committee and the data development project.

He gained focused experience in policy analysis as he worked for EXIM Hungary for more than five years, leading the ECA's international relations (OECD, EU and Berne Union) and ensuring compliance with WTO, OECD and EU regulations, as well as international sanctions.

Laszlo graduated in law from Peter Pazmany University, holds a DipHE in Law of England and Wales and the European Union from the University of Cambridge, and a diploma of economic diplomacy from the Károli Gáspár University in Hungary.

ASSOCIATE DIRECTOR

Paul Heaney

Strategic Communications

Paul joined the Secretariat in July 2016 and manages all aspects of strategic communications and outreach. He is responsible for developing the key messages of the association and building relationships with industry partners and media, as well as overseeing research and publications.

He has almost a decade of experience working in communications, media and publishing relating to the trade finance and export credit insurance industry.

He holds a Masters in Philosophy from King's College London, and a BA from Trinity College, Dublin.

EVENT LOGISTICS AND OFFICE MANAGER

Nicole Cherry

Logistics, Business Administration and Member Support

Nicole joined the Secretariat in July 2016 and is responsible for all meeting and office logistics. In this role she works closely with Berne Union member hosts and external suppliers, coordinating preparation for General and Specialist Meetings across the world. She also manages office operations, finance and accounts and is the first port of call for all member support and assistance.

Nicole has a degree from Roehampton University and has spent six years working in Tanzania on various charity and not-for-profit projects as well as gaining corporate experience working as the assistant to the CEO of East Africa's largest company.

ASSOCIATE DIRECTOR

Eve Hall

Coordination of the Prague Club Committee

Eve joined the Berne Union Secretariat team in October 2017 with responsibility for managing the Prague Club Committee, a dedicated forum for credit insurance companies from new and emerging markets.

She has nearly 20 years of experience in corporate finance, business development and investor relations. Eve held several positions at various GE media businesses in New York, Hong Kong and London. More recently, she delivered management consulting projects for both young and mature organisations.

Eve holds an MBA in Finance from Bentley Graduate School of Business in Massachusetts, US.

ST COMMITTEE MANAGER

Artūrs Karlsons

Coordination of the ST Committee

Arturs has over 10 years of experience in the field of export credit insurance, mainly with a focus on short term business.

Originally from Latvia, he previously led the export credit insurance/guarantee division of the Latvian ECA, ALTUM. Prior to this he worked at the Ministry of Economics of Latvia with the WTO and export promotion matters and was a project lead for the launch of the export guarantee programme provided by the Latvian ECA.

He holds degrees in Finance and Political Science from BA School of Business and Finance and the University of Latvia respectively.

ECONOMIC RESEARCH ANALYST

Jonathan Skovbro Steenberg

Research and Economic Analysis

Jonathan joined the Secretariat in November 2020 with the primary responsibility to produce research-based industry output for members and other stakeholders.

He has previously worked as an Economist for the Danish Resolution Authority for financial institutions as well as holding student positions in the Ministry of Finance in Denmark and the Trade Council in the Danish Embassy in Malaysia.

Jonathan holds a BA and an MA in Economics from the University of Copenhagen, while also having attended LSE, Peking University, KU Leuven and Nova School of Business and Finance through his studies.

Berne Union Committees

The Berne Union's committees are the fundamental organisational structures through which Members join and participate in the activities of the association. They are also the primary structure for coordinating interaction and information exchange between Members (including in relation to business data).

In October 2020 Berne Union Members voted to adjust the structure of the Committees to better reflect the underlying nature of the export credit and investment insurance industry. Specifically, the adjustment recognises the substantial participation of private insurance in medium and long-term export credit business, through the creation of a new 'MLT' committee, open to the participation of all insurers of MLT credit and political risks who satisfy the relevant business thresholds.

There are four committees:

ST: Short Term Committee

The Short Term (ST) Committee engages on all matters relating to short term export credit insurance: i.e. insurance of cross-border credit and political risks with a prepayment term of 12 months or less.

Participants include public and private insurers.

The ST Committee is led by the Chair Julian Hudson (CHUBB) and Vice Chair Sunil Joshi (ECGC India) with the support of Arturs Karlsons at the Secretariat.

MLT: Medium/Long-Term Committee

The Medium/Long-Term (MLT) Committee engages on all matters relating to MLT export credit, political risk (PRI) and investment insurance. This includes insurance cover for exports with repayment terms greater than 12 months against commercial and political risks, and foreign investments (debt and equity) against political risk.

Participants include public and private insurers.

The MLT Committee is led by the Chair Dominique Meessen (CREDENDO Belgium) and Vice Chair Andrew Underwood (AXA XL) with the support of Laszlo Varnai at the Secretariat.

ECA: Export Credit Agency Committee

The Export Credit Agency (ECA) Committee engages on all matters relating to national export credit support provided by official ECAs, including business strategy, policy, international cooperation and all other matters falling under ECAs' mandates.

Participation is limited to institutions holding mandates from their governments for credit insurance activities in support of national exports.

The ECA Committee is led by the Chair Robert Suter (SERV Switzerland) and Vice Chair Irene Gambelli (SACE Italy).

PC: Prague Club Committee

The Prague Club (PC) Committee addresses the particular issues faced by smaller scale or newly established members of the international export credit and investment insurance community, who often have a local or regional market focus.

It provides Members with information and education resources and assists nascent export credit organisations with sourcing technical support as they proceed through their establishment and development stage.

Participants include a diverse mix of mainly public agencies as well as newly establishing ECAs.

The PC Committee is led by the Chair Imaad Al-Harthy (CREDIT OMAN) and Vice Chair Martina Jus (HBOR Croatia) with the support of Eve Hall at the Secretariat.

The Presidents' interview: Chain reaction

The US elections were not the only Presidential event of 2020 and on 23 October we welcomed SACE's Michal Ron as the 44th President of the Berne Union, taking over the position from Beatriz Reguero of CESCE, who has served since October 2018.

In a year where everything has changed, we asked both Beatriz and Michal to share their views and hopes on where the industry and the Berne Union is heading.

Beatriz Reguero

Michal Ron

Beatriz, when you began your term as President two years ago you can't have envisaged something like 'the year 2020'. How do you think the industry has coped with such an unforeseen and catastrophic situation?

Beatriz Reguero (BR): COVID-19 has had a profound impact across the entire globe and affected almost every aspect of private life, public policy, business and trade. While the ultimate economic cost remains to be seen, there is little doubt that the effects of this crisis will continue to challenge all our countries for at least the next few years.

The crisis has severely affected the business of many of our clients; constrictions on trade and international travel have impacted everything from just-in-time supply chains to long term projects and pipelines. Even so, the industry reacted quickly and has fared remarkably well, managing to avoid significant losses in the first phase while protecting clients and partners, from SMEs to large corporates and banks.

ECAs and credit insurers are fortified by inherently robust governance standards in underwriting, product offering and pricing which allow for swift adjustments under changing circumstances such as these. Moreover, a sustained period of positive cashflows have prepared our systems and companies to withstand potential claims and indemnifications, should the situation change as the crisis continues with second and third surges already occurring in several countries around the globe.

Our industry is well accustomed to managing uncertainty. In fact, this is really the essence of our business. On this occasion, however, we are facing more than uncertainty. There will be 'reconstruction' efforts in many countries and we can expect to see different trade policy reactions. Here, we must be vigilant against further imbalances in the international playing field.

And Michal, you now hold the reins of the Berne Union. What do you think will be (or should be) the priorities of our industry during the recovery period, in order to 'build back better' to a more stable post-COVID world?

Michal Ron (MR): I believe that one lesson to be learned from this crisis is that governments, businesses and financial institutions acting alone cannot fully and adequately address systemic global challenges. The post-COVID recovery must necessarily pass through a more integrated international cooperation and it will be critical to prioritise new and more sustainable ways of doing business, in order to reduce inequalities and mitigate the negative effects of the deregulatory race to the bottom which has fed protectionism and other 'lose-lose' economic strategies over recent years.

Export credit agencies were more involved in the immediate response to the crisis, mainly providing support to domestic companies (especially SMEs) in accessing emergency liquidity. In future months, we will further enhance cooperation between public and private sectors, and create institutional platforms for sharing information, common initiatives and projects of mutual interest. We will necessarily invest in those aspects that proved to be the best tools to confront the current difficult environment, such as digitalisation, innovation and sustainable business practices.

In parallel, and in order to regain an equilibrium between ECAs and private sector insurers and lenders, we will need to ensure a gradual reduction of implicit and explicit subsidies that were temporarily introduced to deal with the emergency – but that may impact negatively on global trade in the longer term.

COVID-19 is of course not the only challenge we are facing at present. Beatriz, which of the developments you have observed during your Presidency do you think will have the most significant long-term impact on our industry?

BR: The forces which will do most to shape our industry in the coming years have been evident for some time now: banking regulation, technological change, environmental sustainability, and political ideology in respect of globalisation. Added to this, the last few years have witnessed an increase in geopolitical tensions, and a surge of local conflicts. The COVID-19 crisis will amplify some of these trends but will probably not change their fundamental nature.

From the perspective of an ECA, this crisis has nicely demonstrated that past experience can really help us prepare better for the future. Lessons learned from the previous crisis have ensured that we were ready to quickly deploy a full set of support instruments and financing – tools which have proven crucial for our clients in protecting their liquidity even as the first shocks of this crisis were being felt. As regards the Berne Union, my personal – and professional – impression is that the increased levels of cooperation and engagement of the last years have helped to enhance the collective profile of our industry and appeal of export credit insurance as an instrument our clients and governments turn to in these times.

Michal, how do you envisage the industry will adapt to this retreat from multilateralism and what role can the Berne Union play?

MR: Due to the current protectionist tendencies and international political instability, the risk of a return to market fragmentation is palpable. During my three-year experience as Secretary General of the International Working Group on Export Credits (IWG)[1], I personally witnessed how political tensions may lead to the polarisation of the debate and jeopardise efforts to focus on common goals.

In this regard, the Berne Union remains an extraordinary example of multilateralism and inclusiveness, in sharp contrast to the surrounding geopolitical context. Berne Union Members constantly engage in sharing information, experiences and practices and this remains a unique and precious feature to be preserved and further encouraged. Discussions within our technical Committees can positively contribute to the improvement of the global level playing field and the abandonment of the outdated distinction between 'advanced' and 'emerging' economies. In addition, taking into consideration the viewpoint of recipient countries (i.e. importers), may also help in better reflecting the present economic reality.

The Berne Union itself has changed quite considerably during the past couple of years. What are your proudest achievements during your term Beatriz? And what are your plans for the future, Michal?

BR: The majority of goals during my term have related to the consolidation of various developments already started by my predecessor: improvement of data quality and reporting, and advancing our outreach efforts, among others. In these areas, we have made fantastic progress and I am grateful for colleagues in the Task Forces and Management Committee whose efforts have helped to drive this work. Beyond this, I would also like to highlight as a particularly remarkable achievement, the restructuring of the Berne Union Committees, completed just last month.

The Berne Union has always been unique

Michal Ron: Export Credit and Investment Insurance remains one of the most powerful tools to promote cross-border trade and economic development, especially in a difficult environment, since credit insurance products have a strong stabilising function.

in its heterogeneity between public and private sector insurers of both ST and MLT risks. While years ago there was almost no overlap between the activities of the different groups of members, over time, it has become increasingly obvious that the divide within our committees between public and private aspects of medium and long term business was inefficient, and lead to a loss of information. The new structure provides a formal forum for broad discussion among private and public insurers on all common issues, while maintaining a separate exchange for ECAs on issues specific to their government mandates.

This decision is the result of an open and rich discussion on the strategy of the Berne Union and I am particularly proud that it has become a reality during my mandate.

Still, perhaps my proudest achievement of all – if we can call it that – is the great number of Berne Union colleagues I have worked alongside these past two years who I can now call friends.

MR: My Vice President, Christina Westholm Schroder and I have outlined together a Presidential Platform which envisages several ambitious goals.

I am particularly fond of two objectives. First, fostering multilateralism and leveraging the diversity of the Berne Union membership group. It is crucial to identify together innovative solutions aimed at supporting exporters and financing banks in the current difficult economic context. Second, improving sustainability in our business practices. Export credit support will no doubt play a critical role in encouraging innovation in environmentally friendly technologies and facilitating the transition towards a more climate-neutral global economy. My contribution will entail promoting open dialogue between the Members, as well as broadening our external relations with international financial institutions and formal/informal groups of increasing relevance for our industry.

A final question for Michal. As you begin your presidency in a rather tumultuous environment, what do you see as the defining conditions of the export credit and investment insurance industry today, which will continue to make the industry relevant in the years to come?

MR: Export Credit and Investment Insurance remains one of the most powerful tools to promote cross-border trade and economic development, especially in a difficult environment, since credit insurance products have a strong stabilising function. At a time when the global economy and political scenarios are characterised by increasing volatility and uncertainty, credit insurance providers continue to evolve and rapidly adapt their strategies, products and services. The use of insurance is no longer limited to the mitigation of risks, but rather a more 'rounded' vehicle used to support global expansion, optimise debt financing and optimise stakeholder value.

New patterns for international competition go beyond the traditional ECAs' rules on 'national versus foreign content' and these have triggered a growing urge to seek new risk-sharing models with other market players.

This includes increasing cooperation, co-insurance and reinsurance agreements between ECAs in different countries, as well as between ECAs and private market players or multilateral institutions. It is evident to many of us that there is a well-earned and justifiable niche for ECAs, successfully stepping up to complement the prevailing capacity from the private sector. A closer partnership between ECAs and private sector providers remains, in my opinion, essential in order to ensure that every avenue of potential support is being explored. ■

Note

1 Established in 2012 subsequent to a joint initiative of the US and China, the IWG is an international forum with the aim of negotiating a set of common rules on Export Credits to be shared by both OECD and emerging countries such as Brazil, China, India, Russia and South Africa, which are not part of the OECD Arrangement. Eighteen countries (including the European Union which represents 28 member states) participate in the IWG with delegates from their Ministries, ECAs and Eximbanks.

The Berne Union: Fast forward 2020

By Vinco David, Secretary General, Berne Union

Now that news about the impact of and response to the COVID-19 pandemic is hitting the headlines so frequently, we could almost forget that there have also been several other noteworthy developments in the export credit and investment insurance industry. As the global trade association for the industry, the Berne Union is the organisation par excellence where all developments are shared and come together.

Credit and investment insurers, and hence the Berne Union, are moving fast in a business environment that is also moving fast. This article will focus on how the Berne Union is changing in this environment. The following developments are highlighted:

- The enhanced exchange of information between insurers/Berne Union members
- Closer cooperation between the private market and ECAs
- Cooperation with stakeholders in the wider industry
- The growing importance of business data
- Digitalisation
- Regulation
- And, of course, the COVID-19 pandemic

Enhancing the exchange of information between Berne Union members

One of the key objectives of the Berne Union is the exchange of information and expertise between its member organisations. This information ranges from the very micro level, such as individual buyers' creditworthiness, up to the macro level, such as the impact of global trade tensions on insurers' business or product offering, and everything in between. This exchange takes place in general and specialist meetings, through regular reporting channels online and through our online discussion forums.

The COVID-19 pandemic has considerably accelerated this trend towards more information exchange online that already existed. All meetings are currently held online, aided by the rapid development of digital platforms for meetings. Several online specialist meetings were held on


Vinco David

topics such as claims and recoveries, blockchain, country risk, investment insurance, etc. Although this is not a perfect substitute for in-person meetings, and many of us look forward to the moment that we can meet again in person, we have also learned to appreciate the effectiveness of online meetings. It is expected that, after the pandemic, online meetings will continue to be hosted alongside live events. One of the great advantages of online events is a much lower threshold to participate. Indeed, there were over 400 registrations at our online Annual General Meeting in October 2020, while in-person AGMs usually attract about half this number.

In addition, we have started several internal projects to further improve the exchange of information via our website. One project is to create a knowledge library, or, simply put: a wiki solution to search all digital documents. There is a wealth of information on many topics on our website. The knowledge library is destined to make this information more easily accessible.

A second project is to enhance the exchange of information on the Berne Union discussion forums through improved website functionality. And a third project is to upgrade the exchange by members of their country risk policy.

Closer cooperation between the private market and ECAs

Over the past 20 years, cooperation between ECAs and private insurers has gradually increased. This has been largely in the area of reinsurance, in particular ECAs reinsuring part of their business in the private market. A number of private insurers have developed appetite and have created capacity for increasingly longer tenors for single risk ECA business, allowing ECAs to reinsure this business with tenors even beyond 10 years. This cooperation has turned out to be mutually beneficial: ECAs can thus expand their capacity, while private insurers tap an additional source of income, diversifying their portfolios at the same time.

The Berne Union has moved along with this market development. Over the last few years there has been an increasing number of meetings where ECAs, private insurers and multilaterals jointly discussed a wide range of topics related to medium/long term credit and investment insurance. In 2021 this cooperation will be further strengthened by the launch of a joint committee for this business.

The COVID-19 pandemic has also seen a flow of reinsurance going the other way around: ECAs providing private insurers with reinsurance, especially for short term business. This cooperation has also been facilitated by the frequent exchange of information between our public and private members in dedicated COVID-19 sessions, forum discussions and member surveys.

Cooperation with stakeholders in the wider industry

Some 80-90% of all cross-border trade benefits from some form of finance or insurance. Often both are needed to make a transaction possible. Information exchange between stakeholders and alignment of finance and insurance are thus essential elements for these cross-border trade transactions. The Berne Union and other bodies have taken the initiative for this information exchange. Periodic meetings to keep each other informed and anticipate developments have been held with:

- The ICC Banking Commission. This commission focuses on medium/long term export finance covered by ECAs. One of the main topics has been bank regulation for ECA covered loans. Another major topic has been sustainable finance.
- FCI and ICISA. FCI is the global association for the factoring industry. ICISA is the (private) credit insurance and surety association.
- Development finance institutions (DFIs). The Berne Union has hosted several annual events dedicated to the so-called Capacity Sharing Marketplace. We have set up this marketplace for the purpose of better connecting the full spectrum of public and private institutions involved in international financing of projects with economic and developmental impact. We see much scope for closer cooperation to try to fill part of the development finance gap, estimated to be $2.5 trillion.

Data is the new oil, some people say; it fuels the modern economy. This is not only true for tech giants, but also for our industry. For buyer underwriting, country risk assessment, exposure management or strategic choices, for example, good, reliable data is essential.

The growing importance of business data

Data is the new oil, some people say; it fuels the modern economy. This is not only true for tech giants, but also for our industry. For buyer underwriting, country risk assessment, exposure management or strategic choices, for example, good, reliable data is essential. The Berne Union collects a large amount of business data from its 84 member organisations. This data includes new commitments, outstanding exposure, claims and recoveries, split by business line (short term credit, medium/long term credit and investment insurance, and direct lending), obligor country and type of buyer. Since 2019 we have expanded this reporting of business lines to include working capital, bonding and a few other lines. We have also added data by industry sector covered, ranging from commodities to infrastructure. The first results of this expanded data reporting were published in 2020, providing even richer insight. These data and reports are much valued by our members and other stakeholders, such as banks, the media and academic researchers. The latest full year report is available via berneunion.org/DataReports.

Digitalisation

Technology not only allows for wider use of data, it also impacts profoundly on the way we conduct our business. Especially in the area of short-term whole-turnover business, digitalisation has taken hold. In addition, for various lines of credit insurance, digital platforms have been developed over the past few years, providing a faster and more extended service. The COVID-19 pandemic has accelerated this process of digitalisation even further. So far, digitalisation by credit insurers has been to a large extend standalone, for example, not yet very linked to other services for exporters, such as finance, logistics or digital document handling. The next phase is expected to include links between these different services, to eventually create a one-stop-shop environment for exporters. Artificial intelligence (AI) will play an increasing role in this, for example for assessing creditworthiness. By organising webinars and workshops on digitalisation, the Berne Union supports members in their development.

Regulation

Another crucial factor impacting on credit insurance is financial regulation. This regulation affects private insurers, ECAs and banks financing cross-border trade in different ways. Bank regulation is important for Berne Union members' business, as banks financing cross-border trade are major clients of public and private insurers. Regulators increasingly recognise credit insurance as a risk mitigant for banks, thus reducing their capital and provisioning requirements. But this recognition is not always aligned between regulators. Sometimes this leads to discrepancies or unintended consequences. Therefore, as already mentioned under cooperation with other stakeholders, bank regulation has frequently appeared on the agenda over the past few years. The Berne Union has set up a dedicated Legal and Regulatory Task Force to advise on a policy for regulatory issues. The Berne Union's role towards regulators has been defined as raising awareness about the importance of credit insurance for trade and trade finance. In April 2020, jointly with other trade associations, we sent letters to several European authorities explaining the importance of credit insurance in combatting the impact of the COVID-19 pandemic on trade. We have also drafted a brochure and flyer for the benefit of regulators and policymakers to have a better understanding of our industry.

The COVID-19 pandemic

COVID-19 has figured many times already in this article. It has considerably affected our business in 2020 and will continue doing so in 2021. So far, the market has responded robustly to the challenge. Members individually, and through cooperation between private insurers, ECAs and governments, have largely maintained capacity for export credit insurance. They have also been able to avoid losses for exporters by allowing payment extensions and debt restructuring of their buyers. In addition, the pandemic has been a driver for product innovation, such as for working capital cover, and technology innovation. Compared to the previous crisis – the global financial crisis of 2008-2009 – the response of both private insurers and ECAs has been much faster and more effective. We appear to have learned from the previous crisis. But the crisis is still there. We expect a significant rise in claims at the end of 2020 and throughout 2021, certainly if government schemes to support companies are being phased out. Any phasing out should be done cautiously, to avoid disruption.

The Berne Union has assisted its members in the response to the pandemic by setting up various channels for the exchange of information and expertise. This included member surveys, an online discussion forum, webinars and discussions at online meetings. Reports on Berne Union members' response to the pandemic can be downloaded from our website.

In conclusion, 2020 has been an eventful year for all of us, dominated by COVID-19. The industry at large is in good shape to withstand the crisis, to offer capacity, support exporters and to pay claims. ■

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Perspectives from the Short Term Committee

By Julian Hudson, ST Committee Chair and Global Head of Trade Credit, CHUBB and Arturs Karlsons, ST Committee Manager, Berne Union

Overview: A year like no other

Julian Hudson: "There has never been a year quite like this one. Just about every aspect of our professional and personal lives have been impacted but while it is easy to focus on the negative aspects of the past few months there are many positives to draw from as well.

The UK officially went into lockdown on 23 March 2020. Prime Minister Boris Johnson was accurate with his opening remarks that, "The coronavirus is the biggest threat this country has faced for decades – and this country is not alone." Whether or not this turns out to be the biggest threat to our industry is still to be determined but if it is not the biggest then it is certainly one of the biggest.

Looking at recent member data we have already witnessed a 7% decline in overall commitments. While this may have been expected, nevertheless it is still the largest drop in commitments since the end of 2014. Further, claims have increased by 4.8% compared to the same period in 2019 although experience varies significantly from member to member. For example, our ECA members have experienced increased claims compared to first half of last year but for our private members it is the opposite.

Forecasts suggest a rocky road ahead for our industry. Increased insolvencies, weakening balance sheets, uncertain economic outlook, repayment plans, reschedulings and refinancing risk are things we are all grappling with today. Of course, not every sector or company is the same with many experiencing growth and demand like never before. Making credit decisions in times like this is not easy but it is what we are tasked to do and we will all learn as we work through this and we will emerge stronger and better equipped as individuals and as an industry.


Julian Hudson


Arturs Karlsons

As a global membership bound together by the support of global trade, the past few months have been very challenging for us all and will continue to be so for the foreseeable future. Staying up to date with current trends during this period will be crucial for all

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members and, with this in mind, I have set the objective to provide relevant regular content for Short Term (ST) Committee members. As always, if you have any suggestions for topics or would like to share your experience with members then please contact either myself or the secretariat.

We will remember this period in our history not just for the challenges but for the positives that have come and which will continue to come, for years to come:

Work – increased use of technology, feeling closer to our colleagues and webinars instead of meetings and conferences.

Life – a better work-life balance, be it spending time with the family, a better working environment, not working to a fixed nine to five routine or simply not waking up to an alarm.

Play – getting fit for the first time, rediscovering a love for exercise, time to cook real food or discovering the beauty of holidays in your own country.

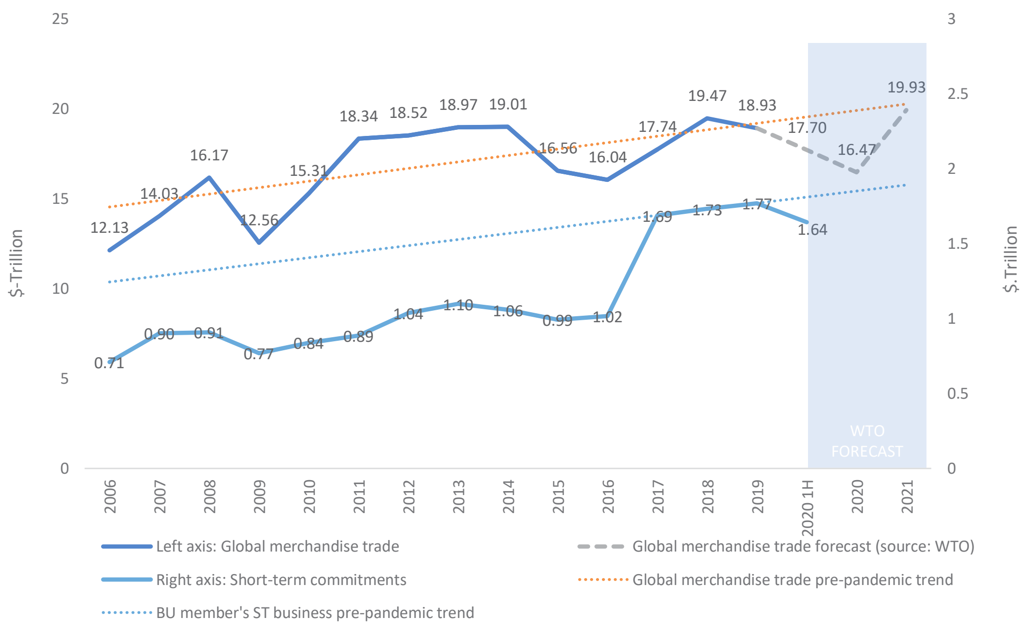
In all your work, life and play I wish you a happy, productive and above all safe year ahead and I look forward to seeing you in person in 2021."

Impact on ST business

Arturs Karlsons: "The first half of 2020 has changed our lives in previously unpredicted ways. When it comes to ST business, one thing that was predictable with relative certainty was that this period will strongly impact the export credit insurance industry as many Berne Union members will experience a decline in commitments compared to the end of first half of 2019. The only question pending was the degree of severity. On aggregate the drop in commitments has been by 7.1%. Falls of such magnitude (more than 7% compared to the previous reporting period) were seen in 2008-2009 during the global financial crisis (GFC) and at the end of 2014 with the significant drop in global commodity prices.

How the trend will continue for 2021 remains highly uncertain. On balance, the

WTO forecast on global trade for 2020 ($ trillion)



Source: WTO, BU

current outlook is not very promising as the continuous impact of COVID-19, unresolved trade tensions and slowing economic growth, will continue to impact members of the Berne Union, especially with obvious volatility of our industry from fluctuations in global merchandise trade. Some insight can be provided by the WTO's forecast on global trade for 2020. As at June 2020, WTO predicted that the fall in global trade volumes would be slightly above 12%. Considering the strong correlation, Berne Union members' ST business could take a similar trajectory, but there are multiple factors that will determine the exact angle of that trajectory.

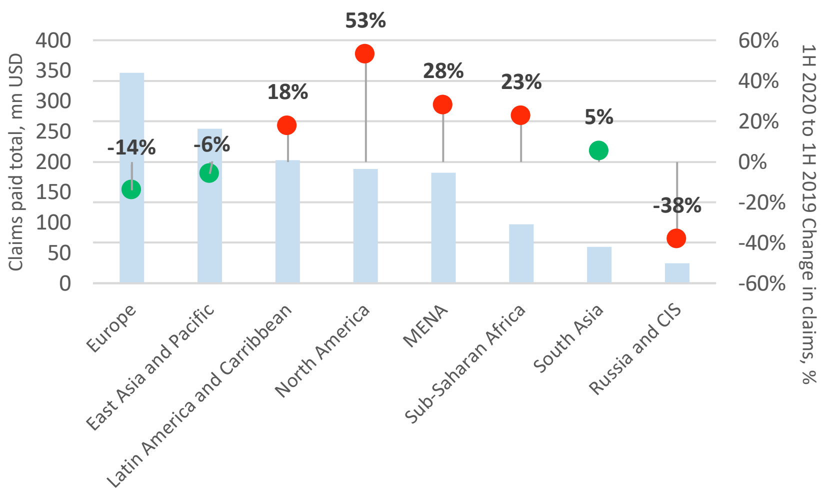
For example, there are factors that could ensure a relatively stable level of commitments as various governments have recognised the crucial role of export credit insurance which ensures liquidity for many corporates. Many support schemes were introduced with an aim to keep credit insurance available even with the growing global environment of insolvency risks. Results and potential future developments in cooperating with governments have been discussed within the ST Committee and it will continue to follow all developments.

Another important indication is the change in volume of claims. For this variable the change has not been that significant with a reported 4.8% increase in the first six months of 2020 compared to the same period in 2019. Despite the increase it is still less than when comparing the first half of 2019 to the same period in 2018. Having said that, it is also important to consider that 'claims paid' as a measure in previous crises has had a longer time deviation. Therefore, the reported business results for the whole of 2020 will give a clearer view of the actual impact on claims.

Another important indication is the change in volume of claims. For this variable the change has not been that significant with a reported 4.8% increase in the first six months of 2020 compared to the same period in 2019. Despite the increase it is still less than when comparing the first half of 2019 to the same period in 2018.

As far as the regional split in the changes in claims is concerned, the most significant increase (if weighted by proportion of total claims) compared to the same period in 2019 has been in claims to North America (up by 53% or by $65 million). For some, maybe unexpectedly, aggregate claims for transactions to Europe as a destination have declined by 14%. Whether this trend will remain for the whole of 2020 is yet to be seen." ■

Change in claims by regional division sorted by claims volumes



Source: BU

Perspectives from the ECA Committee

By Robert Suter, ECA Committee Chair and Head of International Relations & Business Policy, SERV and Irene Gambelli, ECA Committee Vice Chair and Senior Advisor, International Relations, SACE

Impact of the COVID-19 crisis on ECAs

The COVID-19 crisis has led the global economy into a recession of historic proportions, which – in contrast to the global financial crisis – is rooted in the real economy. While companies around the world have gradually restarted production, the context in which they operate remains extremely challenging, and an increase in corporate insolvencies and bankruptcies may still lie ahead.

Before COVID-19, ECAs already offered a number of important tools that allow exporters to conclude and finance transactions even under difficult circumstances. Due to some differences in their pre-crisis toolboxes and a considerable degree of variation in their portfolios, the measures implemented by ECAs in response to the COVID-19 crisis have been quite diverse. In any case, they reflect a significant adaptation to the current situation.

The large majority of ECAs have reacted to the very practical implications of the crisis by extending deadlines, flexibly adjusting terms and conditions and fast-tracking decisions. Some ECAs have also considerably broadened their existing offering by removing restrictions while remaining within the boundaries of their mandate. This includes changes to working capital programmes – for example, lifting thresholds for support in terms of company size, increased percentage of cover, link to single export contracts, etc. – and changed conditions for short-term cover. Managing their existing portfolio has also become a very important activity for ECAs. They are proactively prolonging or restructuring transactions, ensuring that potential losses remain minimal where the long-term prospects of a borrower are intact. Some ECAs which are particularly exposed to hard-hit sectors have agreed to broad debt rescheduling and restructuring, specifically in the passenger air travel and cruise shipping sectors. On the asset side, many ECAs are also involved in the Debt Service Suspension Initiative (DSSI) for developing countries.


Robert Suter


Irene Gambelli

The H1 2020 results reported by major Berne Union ECAs still show a rather contained decrease in overall new business compared to the same period of the previous year ($134 billion versus $141 billion), and no increase in total claims paid.

In addition, due to their know-how and experience in underwriting risk under great uncertainty, some governments have employed ECAs to implement emergency programmes that go beyond the 'supporting cross-border trade and investment' mandate in order to ensure liquidity in the broader economy.

Overall new business of ECA Committee members

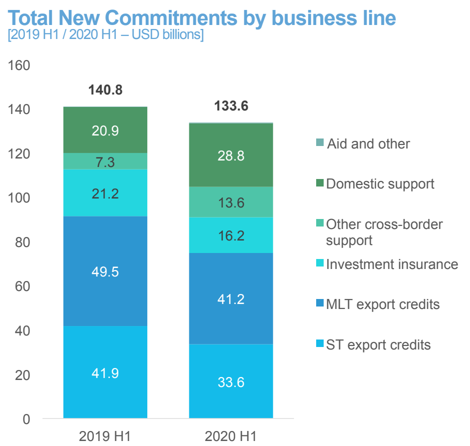
The H1 2020 results reported by major Berne Union ECAs still show a rather contained decrease in overall new business compared to the same period of the previous year ($134 billion versus $141 billion), and no increase in total claims paid. With specific regard to new transactions approved in the first semester of this year, the inevitable decline in the traditional ECA cover (-18% for short-term and medium-long-term export credit support on single contracts[1], and -24% on political risk insurance policies) was to a certain extent compensated by a remarkable growth in other, less traditional business lines, including domestic and untied support. In more detail, support for cross-border transactions not directly linked to specific exports almost doubled year-over-year (from $7.3 billion to $13.6 billion), while domestic support reached a peak of $29 billion (+34% compared to H1 2019). The bulk of this is working capital support, amounting to $24 billion. In some cases, these figures include the various COVID-19-related programmes that have been implemented by ECAs on behalf of their governments. However, it is important to note that some ECAs manage these programmes under a separate account, so the actual figures are likely much higher.

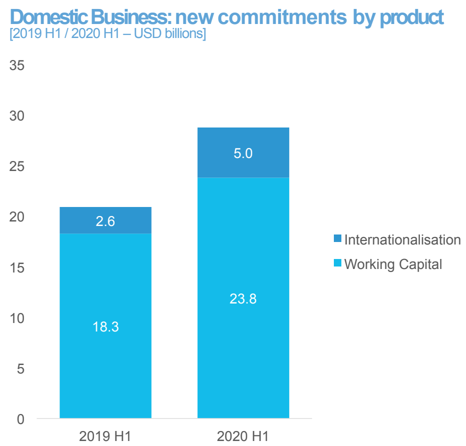
Therefore, although medium-long-term (MLT) and short-term (ST) export credit support still remains the core business of the ECA industry, the crisis has accelerated the gradual but steady shift of ECA activities towards the domestic market seen in recent years.

Note

1 Such data do not include new trade credit cover provided by ECAs by means of revolving whole-turnover policies, as this information is only collected at year-end. However, data on aggregated credit limits granted by Berne Union ECA-Committee Members in the first semester of 2020 show a slight increase year-over-year (from $398 billion to $434 billion), in line with an increasing demand for short-term trade credit and the additional flexibilities introduced by regulators in Europe.

Overview of ECAs' overall business





Source: Berne Union

MLT export credit

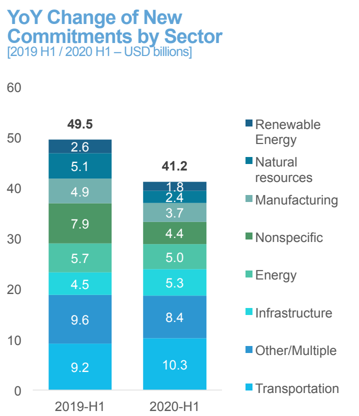
In the area of MLT export credit support, despite the year-over-year decrease (-17%) of new commitments underwritten by the ECA-Committee Members in H1 2020, there were no major changes in terms of sectors and geographies. The main sector for ECA-backed transactions remains transportation (including aircraft, shipping, railway and automotive), followed by infrastructure, energy, manufacturing, natural resources and renewable energy. In terms of geographical areas and obligors, the largest new commitments were in the East Asia-Pacific region (mostly corporate and project risk), followed by the Middle East and North Africa (predominantly sovereign and other public obligors) and North America (almost entirely corporate risk). The only geographies that registered an increase compared to the same period of the previous year are North America (over half of it in the transportation sector) and Sub-Saharan Africa.

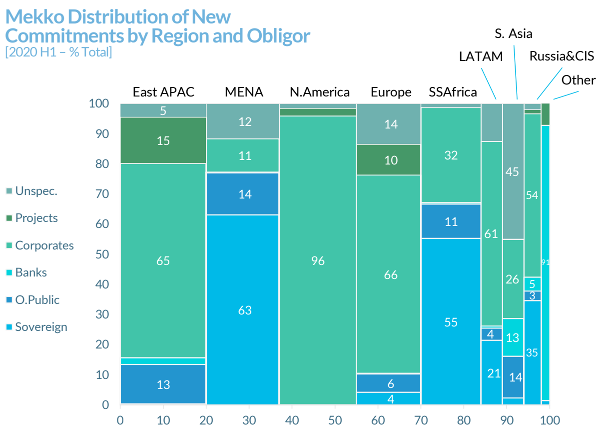
The steady growth in importance of Sub-Saharan Africa, and to some extent of North America, is also confirmed by Member ECAs' exposure data for MLT export credit transactions. Overall, the outstanding commitments before reinsurance amount to $618 billion as of June 2020. Exposure in MENA has also grown significantly but has been on a declining trend since H1 2018 – as are East Asia Pacific, Latin America and Caribbean, Russia and CIS and to a lesser extent also Europe.

Looking at the claims situation in H1 2020, ECA-Committee Members have not registered any increase in arrears on their commitments (i.e. amounts which are overdue for payment but for which claims have not been paid) nor in actual indemnifications. However, current data does not yet reflect the full extent of the COVID-19 economic disruption. Taking a closer look at the dynamics of arrears and claims during and after the 2008/2009 global financial crisis sheds some light on this observation. The time series shows that a significant rise of reported arrears in H1 2009 was followed by a peak in commercial claims only in H2 2009, i.e. a full year after the Lehman Brothers' bankruptcy. This demonstrates how long it takes for claims to show in business data due to the claims waiting period and the assessment of the claim application after an obligor misses a payment and before an actual indemnification is made. Should the current crisis indeed evolve in a similar way to the global financial crisis and create similar cumulative effects, a rise in claims paid by ECAs might therefore be expected starting from H1 2021. Although the extent to which ECAs will have to absorb losses will only become visible in the coming months, the well-known long-term thinking and pragmatic problem solving that our industry has demonstrated in the past will certainly help to reduce the negative impact of COVID-19 on global trade and contribute to the economic recovery.

Focus on MLT Export Credit Activities

New Commitments

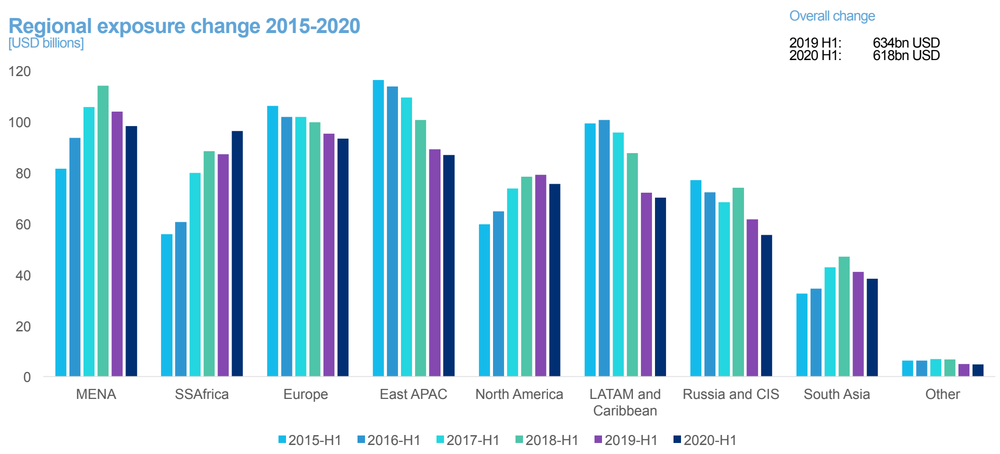




Source: Berne Union

Focus on MLT Export Credit Activities

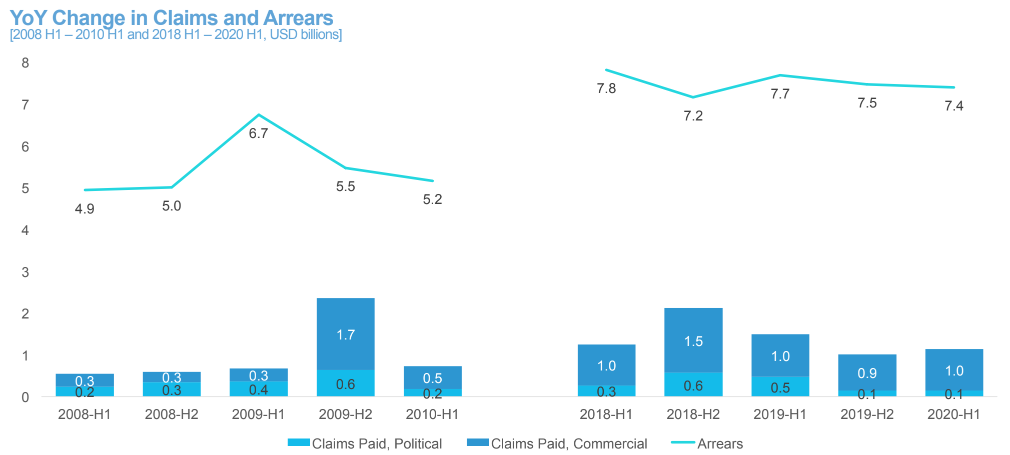
Commitments Outstanding



Source: Berne Union

Focus on MLT Export Credit Activities

Arrears and Claims



Source: Berne Union

Outlook: Macro concerns, a shift to domestic support and sustainability focus

The macro uncertainty of the environment in which ECAs operate remains a major concern. A second wave of rising COVID-19 infection rates has already led to a tightening of sanitary measures in Europe and other regions, creating economic uncertainty about future demand and – as we have seen in the first wave – supply. The risk of a rise in protectionism, government-led onshoring of certain industries and general inward-looking focus of countries remains very real. Companies and even governments are reconsidering large investments, a development which impacts the demand for export financing.

Worryingly, some of our members have already seen a more selective approach of banks in financing transactions, mostly affecting sectors and countries that have been hit hardest by the current crisis. However, the demand for ECA-financing will probably remain stable, as it is precisely the function of ECAs to maintain capacity under high uncertainty and thus to minimise disruptions to trade and investment during a crisis. This is a challenging proposition though, which needs to be carried out in line with certain principles, in order not to cause long-term damage to the export finance system and to avoid resorting to subsidies.

In the coming months and years, we could see a further shift towards the less traditional business lines like domestic support. The role of ECAs and how they employ their capacity to promote trade and investment (and also which kind of trade and investment) has been evolving for some time and this development is likely to gain additional momentum from this crisis. Another trend that is expected to continue is that policy goals outside the traditional sphere of 'jobs and exports' become core pillars of ECAs' mandates – the most prominent being sustainability. The promotion of climate and SDG finance and good governance in executing the export finance business is here to stay. This affects ECAs' mandates and strategies but naturally also those of companies and banks. Estimating the overall sustainability of a transaction, creating a best practice for measuring it and also setting policy to promote projects that improve overall sustainability and limit support for unsustainable projects will be a focus for a large part of the export finance community.

A positive long-term outcome of the COVID-19 crisis would be a renewed appreciation for a well-functioning and sensibly governed international trade system. ECAs are a key component of that, especially in times of crisis, and possess enormous capacity to deliver a positive impact. ECAs will also remain open to new partnerships and cooperation in pursuit of fulfilling their mandates, and the Berne Union supports this through initiatives like the 'Capacity Sharing Marketplace'. The changes in our environment will also require ECAs to become more flexible and to rethink some of the long-standing rules of our business. Governments are already working towards a new consensus on standards and best practices in supporting trade. However, it is not only the rules which need modernising but also the way ECAs connect to their partners and process transactions – digitalisation remains of critical importance. The Berne Union, and in this context specifically the ECA Committee, has historically played a vital role in creating transparency, fostering common understanding and building on each other's experiences and will continue to do so in the future. ■

Endnote: The ECA Committee

The ECA Committee of the Berne Union is currently composed of 34 Export Credit Agencies worldwide, namely (in alphabetical order): ASHRA, ATRADIUS DSB, BANCOMEXT, BPIFRANCE, CESCE, COSEC, CREDENDO, ECGC, ECIC SA, EDC, EXPORT FINANCE AUSTRALIA, EGAP, EULER HERMES GOVERNMENT, EKF, EKN, EXIAR, EXIM HUNGARY, EXIMBANKA SR, FINNVERA, GIEK, K-SURE, KUKE, MEXIM, NEXI, ODL, OEKB, SACE, SERV, SID BANKA, SINOSURE, TEBC, TURK EXIMBANK, UKEF, US EXIMBANK.

The extent to which ECAs will have to absorb losses will only become visible in the coming months, but the well-known long-term thinking and pragmatic problem solving of our industry will certainly help to reduce the negative impact of COVID-19 on global trade and contribute to the economic recovery.

Perspectives from the MLT Committee

By Dominique Meessen, MLT Committee Chair and Head of Reinsurance, CREDENDO and Andrew Underwood, MLT Committee Vice Chair and Chief Underwriting Officer – Specialty, UK and Lloyd's, AXA XL

Global overview

The COVID-19 pandemic and related containment measures have pushed the world's economy into a very deep and synchronised recession. It is the first time that both advanced and emerging market economies have been in recession since the Great Depression of 1930. There is still a lot of uncertainty related to the duration of the pandemic. The recent and relatively quick resurgence of COVID-19 infections in countries where the virus was under control is worrying as it highlights that containment and (voluntary) restraining measures are likely to remain in place (or at least to be periodically reinstalled) for a longer period than initially thought. The COVID-19-related uncertainty and measures have had a large impact on firms' productivity, consumer demand, supply chains, global trade, remittances, tourism, commodity prices, investments and global financial conditions.

In this dire environment, what can we say about medium-long term credit and investment risks? First of all, we must show humility and acknowledge that the impact of COVID-19 on the medium to long-term is uncertain and that it will depend to a large extent on how the crisis will develop further. However, if we look at the recent months, we should appreciate the proactivity and determination shown by the governments and MLAs in implementing strong relief and support measures as well as the goodwill shown by the private insurance market in the search for solutions, which has contributed to the resilience observed until now.

MLT credit in the private market

The private market has remained resilient throughout 2020, having established itself as a complimentary provider of non-payment insurance products as well as continuing to support public agency partners with their goals. With more than 60 active private market insurers, there is depth and diversity,


Dominique Meessen


Andrew Underwood

and theoretical total per-risk capacity has remained stable at around $3.2 billion for public obligor risks and $2.3 billion for private obligors.

Insurers and their clients are mutually dependent upon one another, and during challenging times communication and collaboration are more essential than ever. Those clients – whether financial institutions, exporters or traders – are reviewing and adjusting their insurance requirements and the private market must respond. When we look back at 2020, new business may be higher than some scenarios predicted. In part this is because of the necessity of certain projects (development objectives do not go away in a crisis, and unfortunately may be exacerbated), and in part because the market is looking beyond the news headlines to the merits of each transaction. Supporting good transactions in difficult sectors/countries is business as usual.

Despite the turbulence, the market has continued to see demand for sustainability related transactions. These have been received positively, starting with renewables projects such as wind and solar, and now the interest has opened up to the wider subject of Environmental, Social and Governance (ESG) related transactions. We have seen both public and private markets step up in 2020, whether directly COVID-19 related or more traditional support for the healthcare sector generally. And there is increased demand for non-traditional structures, helping clients to manage an overall portfolio as well as single risk.

One of the silver linings has been the increasing use of electronic placement – the capability has existed to some degree for a while but remote working has accelerated wider adoption. This is a welcome development allowing insurers to run their businesses more efficiently, and in turn this benefits their clients.

While the full amplitude of this crisis won't be known for some time, the private market remains open and active. Claims frequency and severity will vary from one sector to another, but the market stands ready to serve its clients as it has done in previous crises. Claims activity to date has been relatively muted, but there has been pre-emptive action around waiver requests and restructurings in response to the change in circumstances.

Investment Insurance and Political Risk Insurance

Actually, Investment Insurance and Political Risk Insurance (PRI) are relatively small niches when compared to the Trade Credit and Export/Structured Credit insurance markets. This is true both for private insurers and government owned agencies (with a few exceptions). However, since their cover scope is focused upon political risks, it is worthwhile looking at the current status and the future.

Regarding new business produced in 2020, MLT Committee members have had mixed experiences ranging from a strong increase to a strong decrease. There is no trend to be noticed in that respect but those who experienced a decrease believe that it is more a postponement. Corporates especially have just postponed, rather than cancelled, some of their investments abroad, among others, in very large-scale projects. With respect to claims and losses: there have been only very few claims paid and for limited amounts. There is some pre-claims activity but it seems only to be related to COVID-19 in a limited way.

One clear attention point for the sector is the expectation of upcoming discussions between insureds and insurers with respect to the eligibility of future claims under PRI covers. As a reminder, PRI is limited to a list of specific political risks. This has always meant that there can be (sometimes complex) discussions between the insured and the insurer about whether a specific event falls within the insurance policy scope or not. In the context of the current crisis, investors can suffer significant consequences from the extraordinary and unprecedented health protection measures taken by governments in response to COVID-19, including the imposing of broad economic shutdowns and the interference in investors' property rights. In particular, can such measures taken by governments meet the test of the definition of the 'expropriation risk' under Investment Insurance policies when we know that such definition commonly excludes 'Losses caused by any measures or actions that constitute bona fide non-discriminatory measures of general application of a kind that governments normally take in the public interest for such purposes as ensuring public safety, protecting the environment, regulating economic activities…'? It will be a case-by-case approach but it could in the end lead to some insureds questioning the actual added value of the cover they purchased.

On the other hand, it looks like PRI as a specific product still has a clear future. There are different reasons to state that. Some MLT Committee members have already experienced a significant increase in cover inquiries, indicating a positive outlook for the investment plans post-COVID-19. The risk awareness of corporates, SMEs and commercial banks has increased overall and this does definitely include political risks ('pure political risks' as well as sovereign credit risks). Last, but not least, we expect an increase in infrastructure investments as a consequence of stimulus and recovery measures to be taken at government, MLA and DFI levels, which in turn could lead to a higher demand for PRI when such infrastructure projects are made in emerging countries. ■

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Perspectives from the Prague Club Committee

By Imaad Al-Harthy, PCC Committee Chair and General Manager Sales, CREDIT OMAN and Martina Jus, PCC Committee Vice Chair and Executive Director – International Affairs, Export Credit Insurance, EU Funds and Financial Instruments, HBOR

The members of the Prague Club Committee (PCC) are navigating their way through the changing economic landscape. The degree to which the COVID-19 crisis has impacted economies varies according to the precautionary measures put in place, as well as the regional and government-driven support packages available. Our members are responding by supporting the sectors that are strategic or have been particularly hit, diversifying and modifying product lines, all while addressing the gaps left by the private market. Here is a flavour of some responses from emerging ECAs:

Saudi perspectives

Khalid Alhusain, Director of Credit Insurance & Guarantee Department, Saudi Export Program, The Saudi Fund for Development says: "Since the onset of the crisis, the Government of the Kingdom of Saudi Arabia has developed several economic stimuli, especially for SMEs. These measures have helped Saudi companies to sustain and maintain production volumes alongside reducing operating costs.

During the crisis, the Saudi Export Program (SEP) played an important role in promoting and sustaining the position of Saudi exporters in international markets through following a policy that sustains, as much as possible, the credit covers issued by SEP to Saudi exporters. In addition, SEP managed to restructure covers and extend exposure coverage in order to keep pace with the varying size of demand in global markets. Furthermore, SEP, in view of the importance of making liquidity accessible for exporters, has amended indemnifications period to be flexible and premium payments have been postponed, so easing the finance gaps for exporters. In addition, to bear higher risk, a special portfolio has been created with a 'strategic export' characteristic.


Imaad Al-Harthy


Martina Jus

Moreover, SEP has rescheduled due dates and extended payment periods for export finance. However, even despite these measures, SEP export activity dropped due to a decline in world demand and the precautionary measures taken by governments.

Despite the numerous economic stimuli provided by governments, they can be characterised as individual local programmes with limited effects on international trade. It is crucial for countries to work together to create quick and efficient solutions contributing to facilitating movement of world trade and rapidly eliminating obstacles. In this context, under the chairmanship of the Kingdom of Saudi Arabia, the G20 Trade and Investment Ministers have released short and long-term guidelines aimed at promoting trade, operating logistics networks, supporting SMEs, creating stability for global supply chains and strengthening foreign investment aimed at stimulating economic growth.

Moreover, under its Presidency of the G20, the Kingdom initiated the 'Riyadh Initiative for the Development of the World Trade Organization' with the aim to help the world economy flourish, regain trust in the multi-party trade system and ensure equal opportunities for all."

Croatia perspectives

Tamara Perko, President of the Management Board, HBOR says: "The challenges of the global pandemic faced by the Croatian economy in 2020 have affected the activities of HBOR as an export credit agency but also as a development bank. Croatia is a member of the EU, but with a relatively small economy in the world context and a significant share of the service sector in its GDP (for example, revenues from tourism in 2019 accounted for one-fifth of GDP). In addition to the impact of the pandemic on the tourism sector, Croatian industrial production has been significantly affected by the lockdown and reduced demand and consumption in neighbouring countries that are the most important export markets such as, for example, Italy which accounted for 14% of Croatia's total exports in 2019.

To mitigate the negative consequences of the COVID–19 pandemic, at the end of March, HBOR started implementing new measures to preserve the level of economic activity, the liquidity of economic entities, and most importantly, to preserve jobs.

Within the framework of activities of HBOR as a development bank, HBOR introduced measures related to a moratorium on existing liabilities (for certain groups of entrepreneurs up to 16 months), the introduction of new liquidity loan programmes, directly or via commercial banks, whereby the funds from HBOR's sources are approved at an interest rate from as low as 0%. As an ECA, HBOR has introduced new insurance models and adjusted existing ones to facilitate the approval of commercial banks' loans.

In order to enable the approval of more favourable loans and insurance premiums that are several times lower, it was necessary to ask for the approval of the European Commission. In early April 2020, the EC approved HBOR's proposed schemes, thus providing insurance of around €800 million on favourable terms and conditions and loan approvals of €1 billion, i.e. a total of €1.8 billion.

One of the first measures of the Government of the Republic of Croatia after the outbreak of the crisis was to change the umbrella act, by which the mandate of HBOR as an ECA has been extended. This created a framework, under which the range of businesses eligible for credit insurance has been extended, irrespective of the loan purpose: whether working capital loans, pre-export financing or liquidity loans. This intervention made it possible for entrepreneurs with realised income from exports in the previous year and for exporters' suppliers to apply for loan funds in their banks with HBOR support. By changes in the loan insurance programme, support was also provided to the tourism sector as one of the most affected by the crisis.

With an objective of supporting also other branches of the economy, such as the wood processing industry, which has suffered a significant decrease in revenues due to a decrease in customer orders, HBOR has adjusted its programme of insuring pre-export finance loans for the purpose of enabling borrowers to raise new funds they need for current operations at lower funding costs.

Intending to enable easier and simpler approval of loans, HBOR has introduced a liquidity loan portfolio insurance programme – COVID-19 providing 50% cover, and up to 90% cover of approved loan and interest has

"It is crucial for countries to work together to create quick and efficient solutions contributing to facilitating movement of world trade and rapidly eliminating obstacles. In this context, under the chairmanship of the Kingdom of Saudi Arabia, the G20 Trade and Investment Ministers have released short and long-term guidelines aimed at promoting trade, operating logistics networks, supporting SMEs, creating stability for global supply chains and strengthening foreign investment aimed at stimulating economic growth."

“Aiming to support a part of the economy comprised of small entrepreneurs, by amending the programme for insuring short-term receivables for SMEs with annual export revenues of up to €2 million, HBOR created a framework for approving insured amounts three times higher than had been possible before the pandemic outbreak”

been made possible by amendments to the programme introduced at the end of the year. This is an innovative product, for which banks have shown great interest, because they can easily include approved loans into the secured portfolio under pre-defined criteria.

Due to the increased demand for the insurance of short-term export receivables, HBOR also encountered an increase in interest in insuring temporarily non-marketable risks among both current and new clients. This is the result of increased awareness about the insurance of receivables, but also of the lack of supply in the private market due to the pandemic in markets in which Croatian exporters also operate. In the first six months of 2020, the insured amounts increased by three times compared to the same previous year period for temporarily non-marketable risks. HBOR can implement this type of insurance because the EC declared all marketable risks temporarily non-marketable through the Short-term Export-credit Communication, thus enabling the intervention of state insurers in the short-term insurance market until mid-2021.

Aiming to support a part of the economy comprised of small entrepreneurs, by amending the programme for insuring short-term receivables for SMEs with annual export revenues of up to €2 million, HBOR created a framework for approving insured amounts three times higher than had been possible before the pandemic outbreak.

These measures and our efforts throughout 2020 are the result of HBOR's flexibility and fast adjustment to new circumstances in the light of a role that becomes even more important in times of crisis. Going forward, HBOR will continue to offer services to entrepreneurs, large, medium-sized and small ones and to fill in market gaps with an objective of preserving the sustainable development of the Croatian economy.”

Egypt perspectives

Mohamed Azzam, Managing Director, EGE, Export Credit Guarantee Company of Egypt says. “The anxiety fuelled by the media regarding COVID-19 and the varying government responses that followed have caused thematic shifts in global trade flows, closing markets and opening others.

The sudden withdrawal of cover from the private market has deepened the market gap and created opportunities for smaller ECAs to play a key role to seize new entry points created by the crisis. The reinsurance market, although it has been busy licking its wounds, is looking for fresh premiums to normalize its loss ratios.

Without an end in sight, the economic patterns of many economies will be determined by their reaction to a second wave. Debt laden stimulus packages are not an option for many already highly indebted developing countries. Many have already decided to weather the storm without another lockdown. They simply can’t afford it!”

Agility of operations is key

Many PCC members acknowledge the need to supplement government level measures in order to improve export activities. They are prioritising, innovating new products, and putting extra efforts into digitalisation of operations. Agility of operations remains a competitive advantage for smaller ECAs in these difficult times.

Adds Alhusain, “The crisis revealed that it would be imperative to invest in technology in many fields to create a sustained world economy. SEP found it necessary to invest in automation and minimise the reliance on humans in production processes. Also, E-commerce has become a fait accompli and necessary to maintain world trade. It would require more investment in digital infrastructure that contributes to facilitating electronic conclusion and authentication of commercial contracts.” ■

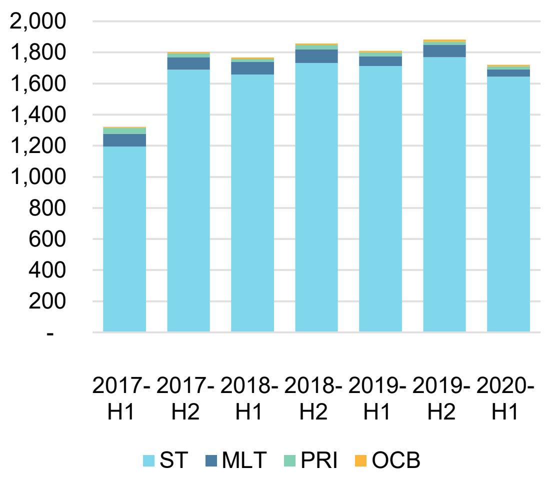
Berne Union Data Snapshot 2020H1

Berne Union Totals

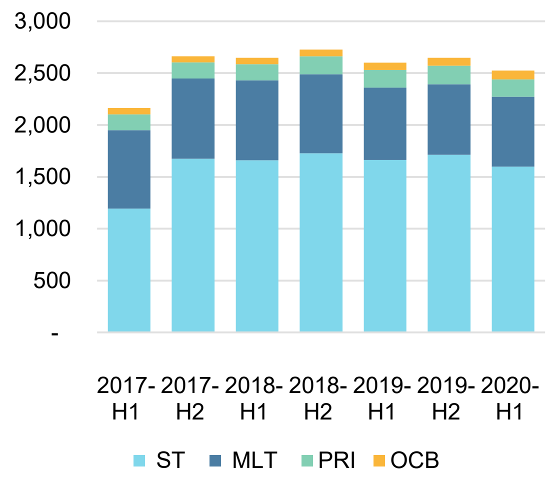
Note: All figures are in USD billions, unless otherwise stated.

ST: Short-Term Export Credit
MLT: Medium to Long-Term Export Credit
PRI: Political Risk Insurance
OCB: Other Cross-Border Insurance

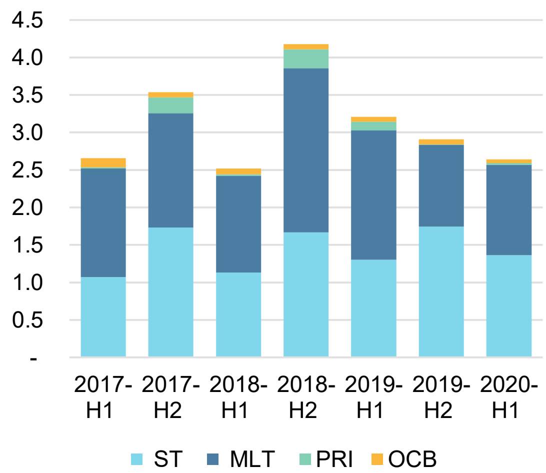
New commitments by business line



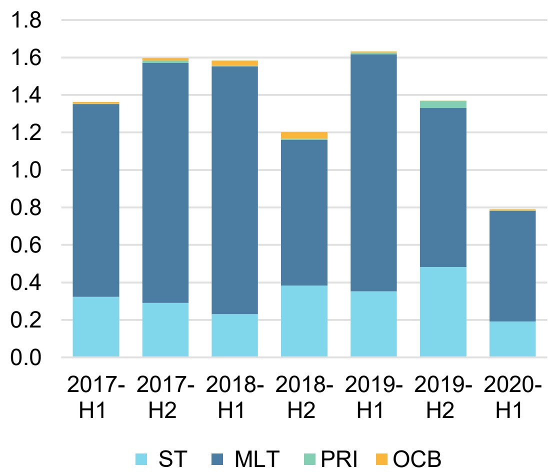
Total exposure by business line



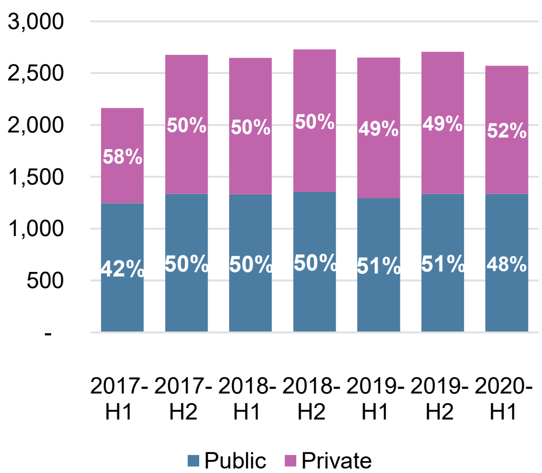
Claims paid by business line



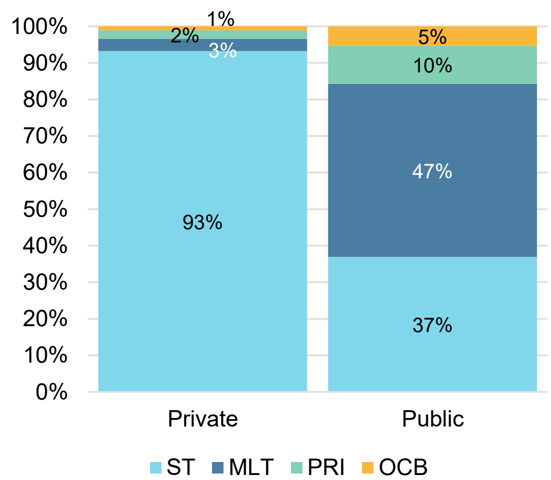
Recoveries by business line



Private and Public member's share of new commitments

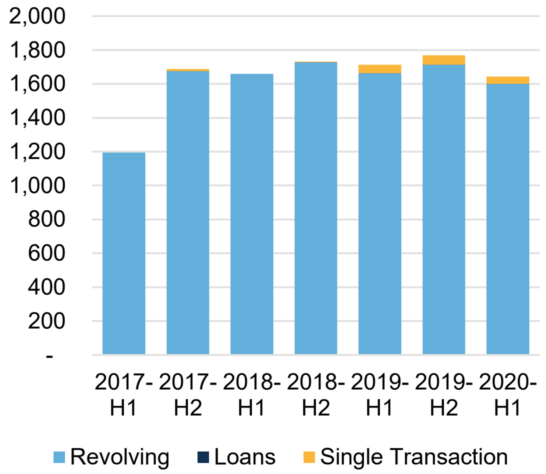


Private and Public members' share of new commitments by business line in 2020-H1

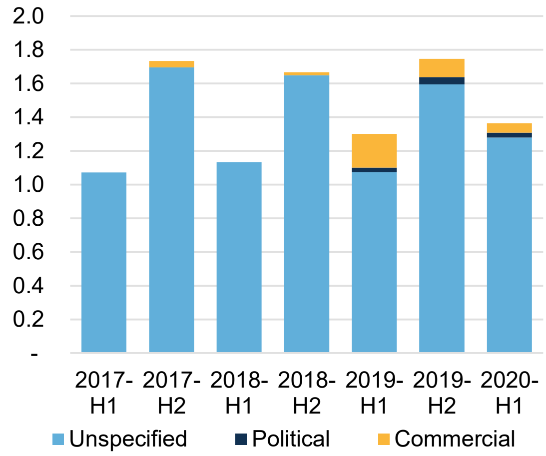


Short-Term Export Credit Insurance

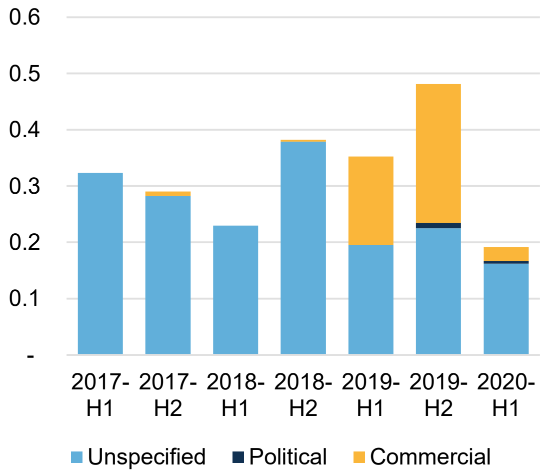
ST commitments by activity



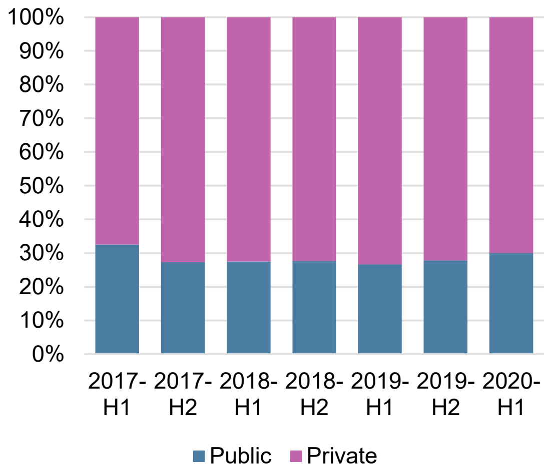
ST claims paid by risk type



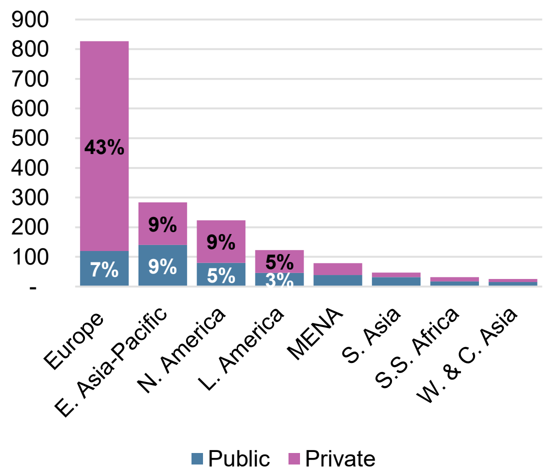
ST recoveries by risk type



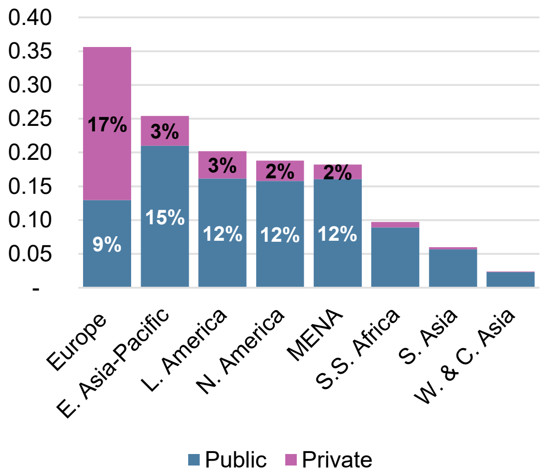
Private and Public members' share of ST commitments



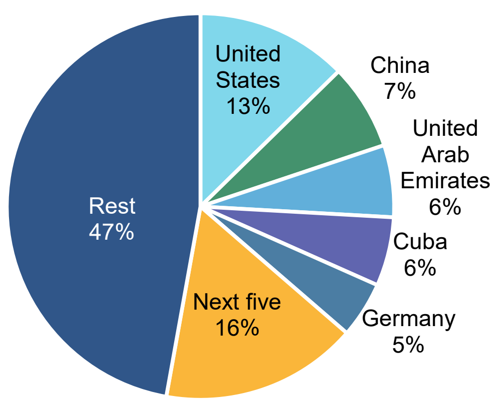
Private and Public members' regional share of ST commitments in 2020-H1



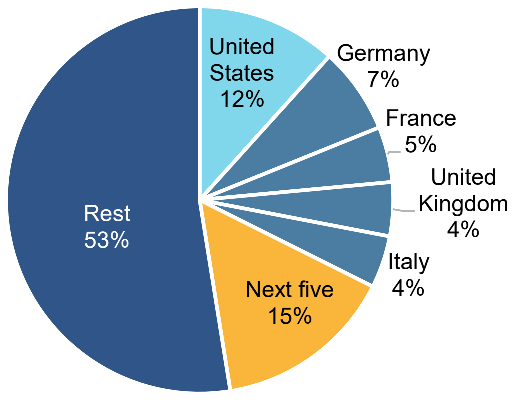
Private and Public members' regional share of ST claims paid in 2020-H1



Top countries for claims paid

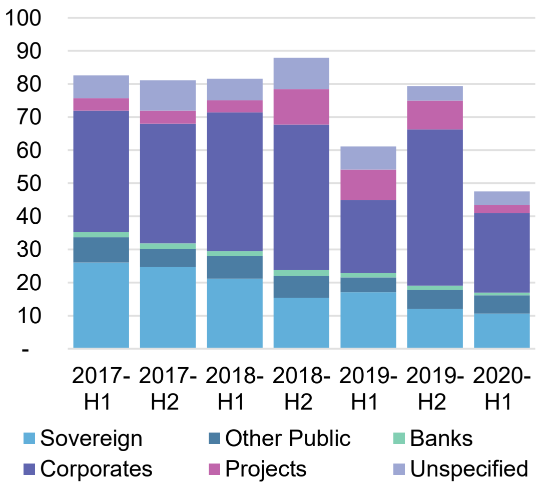


Top countries for commitments

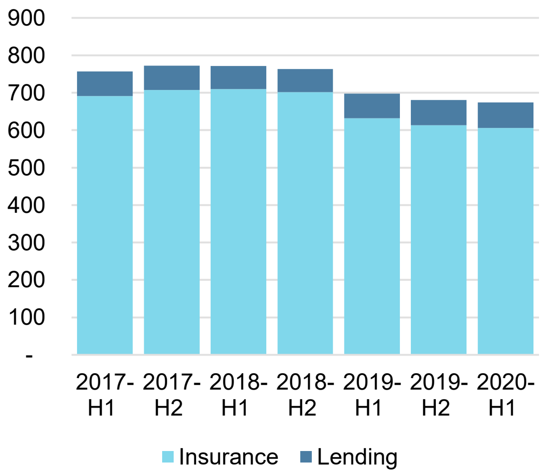


Medium and Long-Term Export Credit Insurance

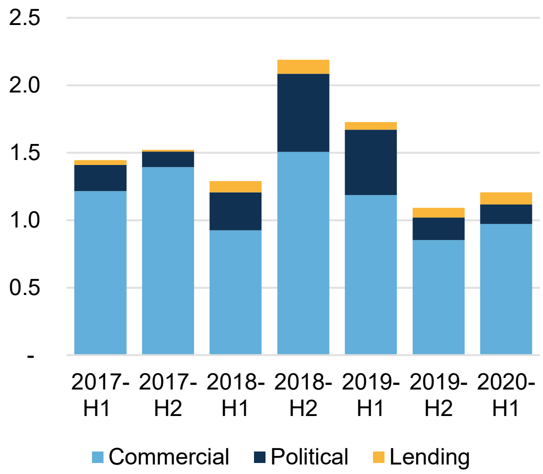
New MLT commitments by obligor



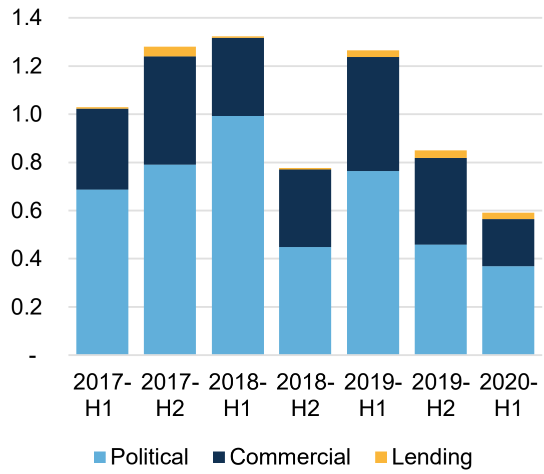
MLT exposure (insurance and lending)



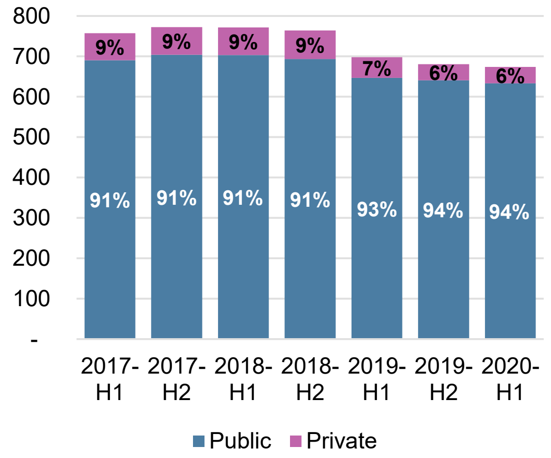
New MLT claims paid by risk type



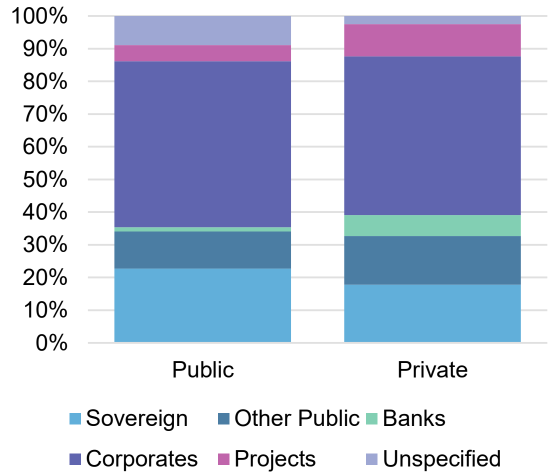
New MLT recoveries by risk type



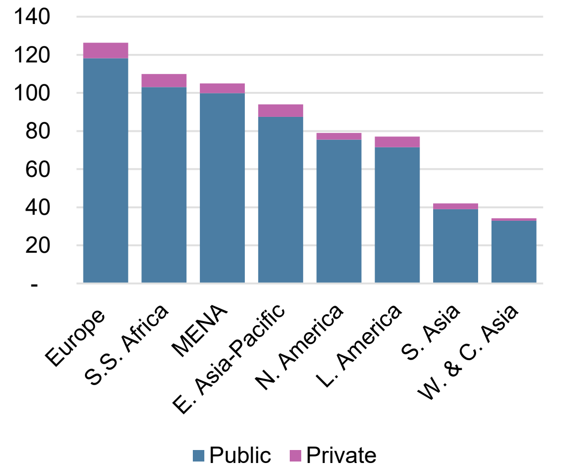
Public and Private members' share of MLT new commitments



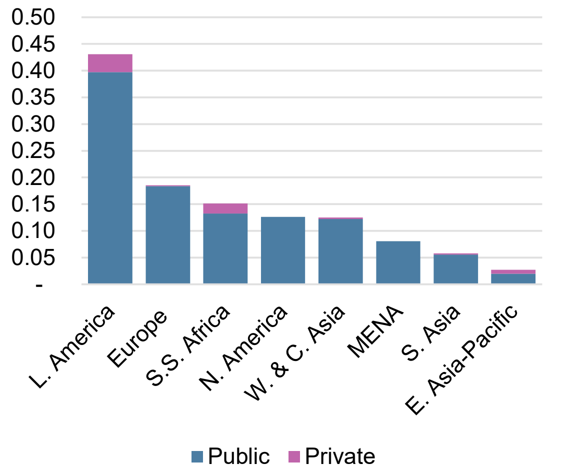
Public and Private members' share of new commitments by obligor in 2020-H1



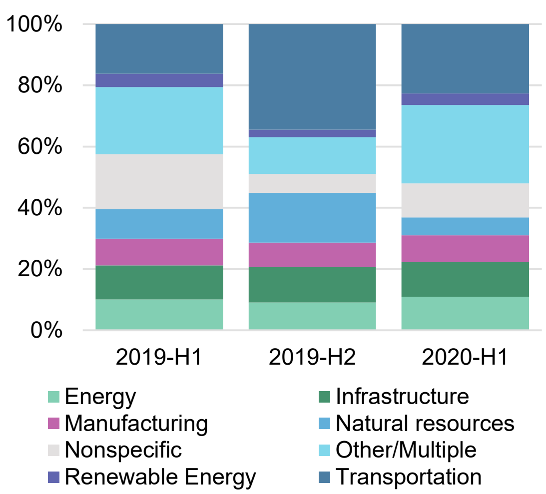
Private and Public members' regional share of MLT exposure in 2020-H1



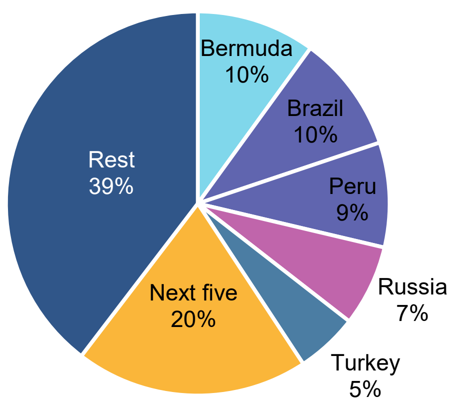
Private and Public members' regional share of MLT claims paid in 2020-H1



Sector split of MLT new commitments

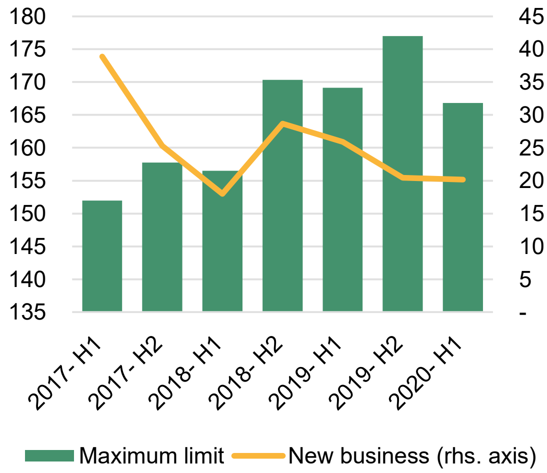


Top countries for MLT claims paid

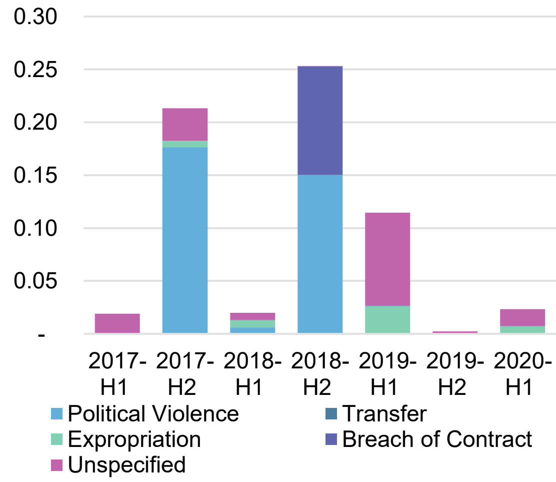


Political Risk Insurance

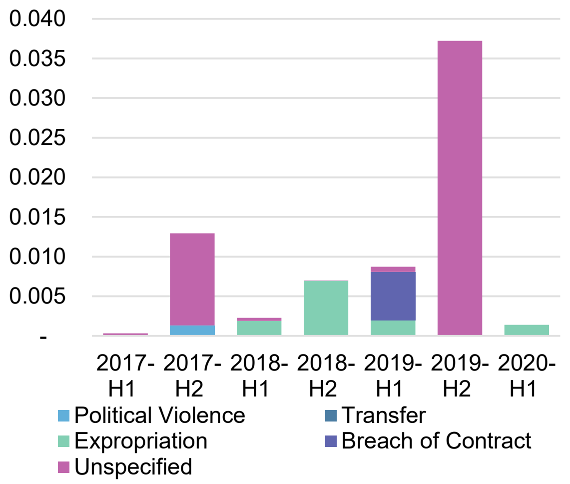
Maximum limit of liability and New Cover Provided, PRI



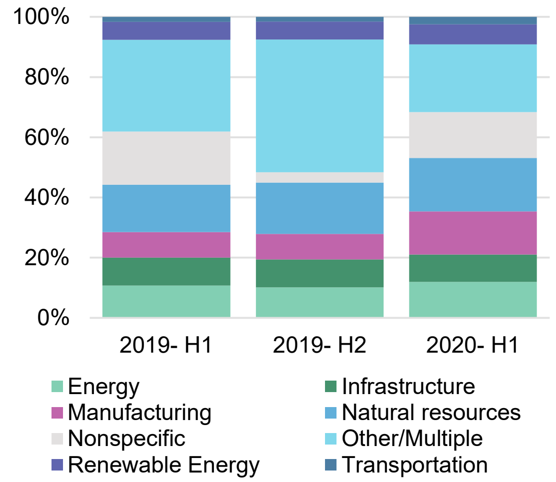
New PRI claims paid by risk type



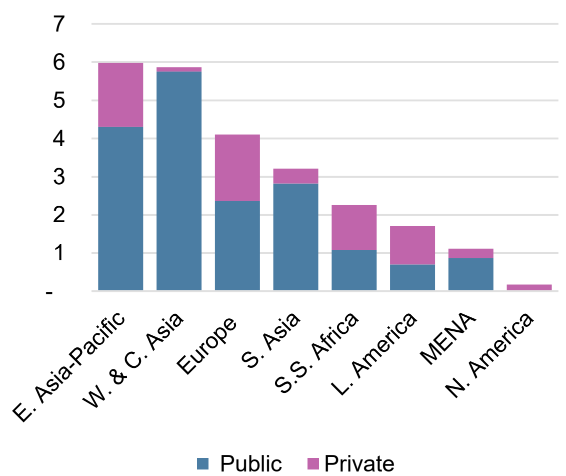
New PRI recoveries by risk type



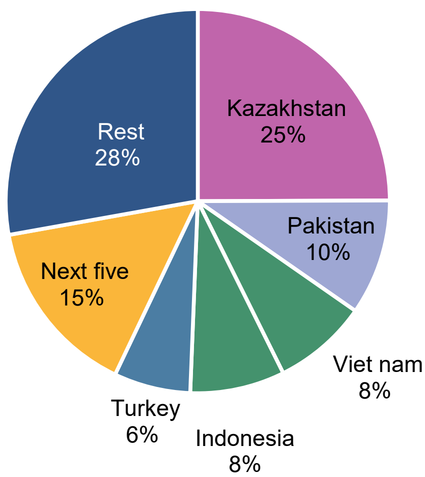
Sector split of PRI maximum limit of liability



Private and Public members' regional share of PRI exposure in 2020-H1



Top countries for new PRI cover for 2020-H1



2

Mega trends

Mega trends interrupted?

Where do we stand, and where are we going? These are questions at the heart of forecasts for this year's Berne Union Yearbook. COVID-19 wasn't the kind of crisis any of us had predicted.

Earlier this year, before the pandemic reached Europe, Berne Union published an article 'mega trends and trade'[1]. It showed the central predictions for 2020, and beyond, of a panel of experts who had met at Berne Union in London in December. Those conclusions still make interesting reading, but what's fundamentally changed? We asked the same participants what's changed with their forecasts and how? And what's not changed? Their answers may chime with your views, surprise you, or challenge you.

David Neckar, Client Director, Willis Towers Watson Financial Solutions, London

"When we met in December 2019 to celebrate the Berne Union's 85th anniversary, a global pandemic was not even mentioned. Instead our forecasts looked at what climate change and new digital technologies would bring, at threats of populism and the weaponization of international trade.

Although it seems to have been a long time since the COVID-19 virus took hold this year, we are in fact only a few months into this strange new world. We are still in early post traumatic shock, with the adrenalin of government crisis measures sustaining our economies.

The most surprising change in my forecasts for 2020 is that they haven't changed. We are still having to grapple with the climate change issues I highlighted: they have been made more evident by wildfires in Australia, Russia and the US. We still feel the growth of Environmental, Social and Governance issues. ECAs are playing increased roles in encouraging renewables and promoting responsible business practices.

On a day-to-day business level, it's a similar 'surprise'. Much of our company's CPRI business has continued without massive discontinuity, despite some slowing down on both the clients' and the insurers' sides as decision-making processes are adapted to reflect the changed risk picture as well as the new virtual business environment.

Attempting to forecast unexpected positives or negatives over the coming five years must surely be dependent upon the discovery of an effective vaccine, or combination of vaccines. This will not produce automatic positives: managing its production and distribution will produce difficult social, political and economic trade-offs, national and international. The squabbling over the supply of masks and PPE in the early months of COVID-19 is an example of the tensions and political risks

The most surprising change in my forecasts for 2020 is that they haven't changed. We are still having to grapple with the climate change issues I highlighted: they have been made more evident by wildfires in Australia, Russia and the US. We still feel the growth of Environmental, Social and Governance issues. ECAs are playing increased roles in encouraging renewables and promoting responsible business practices.

that can emerge. A surprise negative could be reactions in developed countries to the hierarchy of access to medications igniting latent tensions in ordered and law-abiding societies as we saw with the Black Lives Matter movement.

A forecast one can make with confidence is the continuing growth in demand for riot and civil commotion insurance, exacerbated by property insurers now excluding these risks from baseline cover.

Unexpected positives over the coming five years are hard to find, given the dangerous mix of economic downturn and political polarisation, which makes it difficult to see how long-term global issues can be equitably and responsibly tackled. The populism that we talked about in December last year is driving reactions against global initiatives and international cooperation. Let's hope that the Berne Union can counter those pressures by showing the benefits of 86 years of international cooperation."

Beatriz Reguero, outgoing Berne Union President and Chief Operating Officer, State Account, CESCE

How have your forecasts changed – have they been torn up or pushed down the road?

"Obviously 2020 will go down in history as the year a virus disrupted everything. From the way we do business to the way with interact with each other. In an industry based on international mobility, of people and goods, COVID-19-related restrictions have had many impacts. From physical disruptions to trade chains and financial relationships to political ramifications and intensification of nationalist and protectionist trends already visible before it.

As regards the mega trends in trade we talked about in December, I expect a push forward on changes coming from technology and on political and social polarisation with bilateralism and protectionism growing rapidly. Environmental sustainability strategies are still there, maybe with a lower pressure in the very short term but a growing urgency for the medium term. Last but not least, the positive economic framework we were experiencing and expecting to continue has been torn up. Let´s see what the final impact on trade looks like but my guess is that negative elements will clearly overcome the positive ones.

What is the most surprising change in your forecast for 2020?

The COVID-19 virus has not changed the underlying themes, but it has forced us to work on them while absorbing the need, in our case, to implement a support package for Spanish exporters which has resulted in the largest ever number of new transactions in a year. This has required intense coordination and team effort within our company while at the same time orchestrating new ways of working, from home and without the physical exchange of documents with our clients.

Personally I think the most surprising change, aside from the very obvious shock of living a reality that has been thus far the stuff of movies, has been going from a situation where we operated with agendas, forecasts, that gave us relative visibility as to what we were going to be doing and where we were going to be in a few months to moving to a 'one day or a week at a time' mode.

What hasn't changed or is the least surprising?

Again, we've (CESCE´s team has) managed to step up to what was has been requested of us! (I couldn't help myself on this one!) Very much on this line, one probably unsurprising thing is how fast governments can act when there is a common understanding of a need, be it refinancing sovereign debt for the most vulnerable economies, proposing flexibility under the Arrangement, the EU rules, etc. The private sector is of course usually praised for its ability to respond quickly to changes in needs and market trends, and I think we saw

We expect that ECAs will go to greater lengths to support domestic companies, so we anticipate that the famous level playing field will finally, openly, become a thing of the past if nothing is done about international regulation."

that immediately when, in the first months of the year, major deals in the shipping and aviation industries were restructured almost overnight.

Any unexpected positive forecasts for the next five years?

I'm not sure how to respond to this. Turbulent times always bode well for our business, but this time the economic impact of the pandemic is so widespread that it is difficult to foresee what the consequences will be. Additionally, we have already experienced how the pandemic can reappear any time and how difficult it is to predict or contain it.

We expect that at some point during the next year we'll start seeing all major economies consolidating a path of recovery, although it is early to predict how the different 'rhythms' that each region takes will affect the geopolitical balances.

In line with recent trends we foresee an intensification of governments' efforts to support their exporters in more creative ways, making it even more evident that agreements like the OECD Arrangement need to adapt to new ways of doing business and of supporting it. Maybe the one positive surprise might be an actual change in the Arrangement.

The impact of the pandemic on international supply chains may result in opportunities for countries that are geographically well placed to serve as production and logistic hubs for Europe, the US, and other economies, re-channelling production currently coming out of China.

Any unexpected negatives for the next five years?

I would say that the negatives for the next five years are all more or less expected now. With varying degrees of uncertainty and pessimism/optimism, we will see the impact of COVID-19 on all regions, and remain expectant to see how activity (investment, tenders, etc.) recovers and the kind of opportunities that our companies can access. We will also see how sustainable the levels of indebtedness, public and private, incurred to support companies and national economies are.

We expect that ECAs will go to greater lengths to support domestic companies, so we anticipate that the famous level playing field will finally, openly, become a thing of the past if nothing is done about international regulation."

Gabriel Buck, Managing Director, GKB Ventures

How have your forecasts changed – have they been torn up or pushed down the road?

"Our forecasts have neither been torn up nor pushed down the road. In fact we are experiencing our most successful year to date. In the past 12 months we have successfully closed $500 million of projects in Africa. That may be small by the standards of major banks, but as a small boutique we are delighted to see our clients grow their export orders by this amount.

GKB Ventures is an employee-owned, fully independent advisory firm specialising in export finance in Africa. Thus we are very focused and are comfortable in managing what may seem to others a very high geographic concentration risk. This is a market we know well and can manage this risk. This is what we do. Helped, no doubt by having 50 years of combined experience in this field. This year has been a good year, our focus has paid off and we are positive for the future.

I have two predictions which I am fairly confident on. First is that Africa will continue to be a growth market. Second is that the OECD CIRR will keep low for at least two to three years, and potentially for the next five years.

What has been the most surprising change in your forecast for 2020?

Two things have surprised us. First, is how quickly the African markets adapted to COVID-19 and how they embraced the technology to increase dialogue and levels of communication. As a direct result, the period to structure and position a project all the way to close got shorter.

Zoom/Microsoft Teams teleconferencing, and just higher levels of interconnectivity, improved things dramatically. We initially thought that the inability to travel and meet would hinder projects. Quite the opposite has happened. In one example, we were able to have weekly update calls with the Director General of the Ministry of Finance on a weekly basis. Pre COVID-19 each one of those face to face meetings may have taken three or four weeks to schedule and consumed three or four days in travel time.

The second surprising thing has been the divergence between bank funding costs (which have increased) and the OECD CIRR rate (which has decreased to an all-time low). We didn't expect this and we certainly didn't expect this to happen so quickly. It was the speed of change in the early months of the pandemic that surprised us. That was good news for borrowers who are seeking long term ECA financing using the OECD CIRR rate. This drop in the CIRR was, to some extent, a factor as to why many more projects closed so quickly.

What hasn't changed or is the least surprising in your forecasts?

Least surprising is the number of banks still focusing solely on the large ($250 million plus) deals. I am concerned for the industry as a whole that so many institutions are solely focused on this segment of the market. I can understand this strategy when the ECA market was dominated by large oil and gas, shipping and aviation transactions. But now? Some banks are adjusting their business models to reflect the 'new normal'. Others are not.

Any unexpected positive forecasts for the next five years?

Five years is a long time in a fast changing market. What is key is the ability to spot changes and adapt accordingly. I have two predictions which I am fairly confident on. First is that Africa will continue to be a growth market. Second is that the OECD CIRR will keep low for at least two to three years, and potentially for the next five years. The unexpected consequence of COVID-19 is the huge economic stimulus represented by the level of new debt issued by G7 countries. This in turn is lowering yields which directly translates into a lower CIRR rate. Those ECAs that offer the OECD CIRR will do very well going forward.

Any unexpected negatives for the next five years?

I fear that some banks may pull out of the ECA market altogether, or at the very least withdraw to a very small market segment. To some extent this is already happening and I fear this may be accelerated in the next five years. This is not good news for the industry as a whole. Whilst any gap will undoubtedly be filled by new banks or other financial institutions, it is important that the skillset in the market remains. To lose this will have a negative impact for the market as a whole.

Jean-François Lambert, Founder and Managing Partner, Lambert Commodities

What been the most surprising change in your forecast for 2020 as a result of the pandemic? What hasn't changed or is the least surprising?

More than a game changer, the pandemic will act as a catalyst. The backdrop remains one marked by geopolitical and economic polarisation, shortening of supply chains where possible, re-onshoring/regionalisation of trade and manufacturing processes, energy transition and ESG awareness from consumers to investors to financiers. The pandemic and the economic shock will simply accelerate these trends, not challenge them.

The fact that travelling is no longer the norm but has become the exception will make consumers even more aware of the need to keep buffers (food stocks, strategic production) closer to them and therefore will hasten de-globalisation when feasible. The world will re-globalise around clusters (geographies and common value sharing – environmental awareness, democratic processes etc).

This will affect production, consumption, investment and of course finance. All regions will not move at the same pace (think ESG and decarbonisation where Europe will accelerate post COVID-19, therefore faster than China or the US for that matter).

Are there any unexpected positives in your forecasts for the next five years?

The next two to three years will be marked by economic stress, tensions and turmoil, which are inevitable as paradigms shift. Transportation and tourism will need to re-invent themselves. All companies will have to go green to warrant stakeholders support. Consumers are saving more than they are consuming but I believe in three to five years from now, we will see the emergence of a new economic order with a renewed dynamism if COVID-19 has been tamed and the population is vaccinated.

What about any unexpected negatives for the next five years?
Geopolitical tensions could derail recovery and push it out by several years – these include the South China Sea, Turkey's ambitions, India – China/India-Pakistan (a proxy war by China). Inflation? Secular stagnation? In a polarised world these could trigger unrest and exacerbate geopolitical tensions. ■

Note
1 https://www.berneunion.org/Articles/Details/489/January-BUlletin-Mega-Trends-and-Trade

COVID-19 creates record demand for EBRD's trade facilitation facilities

Rudolf Putz Deputy Director Financial Institutions - Head Trade Facilitation Programme (TFP) at EBRD

Global pandemic crisis response under EBRD's Trade Facilitation Programme (TFP)
The EBRD's Trade Facilitation Programme (TFP) was developed to promote and facilitate international trade to, from and within central and Eastern Europe, the Commonwealth of Independent States (CIS) and the southern and eastern Mediterranean (SEMED) region. Under the TFP, guarantees are provided to international commercial banks (confirming banks) thereby covering the political and commercial payment risk of transactions undertaken by issuing banks in the economies where the EBRD invests.

Since 1999, the TFP has facilitated more than 26,000 foreign trade transactions worth more than €22 billion and trained more than 9,000 partner bank staff on trade finance procedures and processes. At present, there are more than 120 issuing banks within the TFP across 30 economies where the EBRD invests, working with over 800 confirming banks and their subsidiaries throughout the world.

In view of the state of the market, the TFP is in increasing demand. Due to its strong effect in sustaining local economies through supporting international trade, the TFP is a prime instrument to respond to the crisis situation in the regions.

Record business volume in excess of €2 billion financed in January-August 2020
The COVID-19 crisis has resulted in a surge of demand for support from the TFP. Between January and August 2020, the TFP has already supported the financing of a new record volume of foreign trade in excess of €2 billion.

What is the outlook for 2021?
In view of the state of the market, the TFP is in increasing demand. Due to its strong effect in sustaining local economies through supporting international trade, the TFP is a prime instrument to respond to the crisis situation in the regions.

The EBRD will play an important role in providing trade finance facilities to banks which cannot get sufficient funding and risk cover from foreign commercial banks, export credit agencies and private insurance underwriters.

It is also the EBRD's experience that TFP demand peaks after the crisis, as economies rebound but the availability of commercial trade finance remains subdued. As countries restore their supply chains post COVID-19 and business and consumer confidence returns, the TFP expects to see the demand to continue in many areas for quite some time, particularly for consumer goods, clothing, pharmaceuticals, medical equipment and food commodities. This is in part due to commercial banks being more reticent to finance transactions without EBRD support.

The 2021 outlook: Climbing out of a deep hole

By Glen Hodgson, Chief Economist, International Financial Consulting Ltd

We will remember 2020 as the most demanding year in a generation, even more dramatic than the 2008-2009 global financial crisis (GFC). The pandemic-induced shutdown plunged the global economy into a deep hole. Many countries were hit with a rapid contraction in GDP of 20% or more in March to May, and a doubling or more in unemployment – followed by a quick partial rebound, but also the risk of recurring pandemic waves and related targeted shutdowns.

The IMF is projecting global growth to contract by 4.4% for all of 2020. The euro area will see a much deeper contraction of 8.3%, reflecting a sharper downturn. The US economy is projected to shrink by 4.2% and Asian advanced economies are facing a more moderate contraction, thanks to a more contained pandemic.

Emerging markets and developing economies are expected to contract collectively by 5.7% in 2020. Many face difficult prospects due to the continuing spread of the pandemic, creating pressures on their fragile healthcare systems, severe shocks to sectors such as tourism and oil production, and dependence on external finance.

An uncertain and risky business environment

The business operating environment has become more uncertain. An uneven rebound is to be anticipated across countries and sectors, with the possibility of a 'K-shaped' recovery – a healthy rebound in some countries, but setbacks in others where the pandemic is not well contained. Forecasters are making frequent major revisions to keep up with developments.

Pandemic management is of course the dominant risk factor, which can only be mitigated with an effective and widely available vaccine. While there has been some promising news on vaccines, widespread global distribution will be still required for a full economic recovery.

Glen Hodgson

The global recession has had severe financial and debt management impacts. The G20 has called for debt service suspension for heavily indebted low-income countries and the unlocking of new funding to developing countries at unprecedented speed. Given the depth of the contraction, further economic scarring should be expected. Impacts include continued elevated unemployment, higher business failures, weak and delayed investment, turbulent oil and other commodity markets, and the likelihood of lag effects.

2021 outlook

Global growth in 2021 is projected by the IMF to recover to 5.2%. This outlook is based on expectations of persistent social distancing, other measures to contain the pandemic and address its public health consequences, and continued significant fiscal, monetary and structural policy intervention. Early widespread vaccine availability could boost the outlook, and a delay would be a drag on growth.

In advanced economies, output growth is projected to strengthen to 3.9%, with inflation remaining low. The eurozone will have a bounce-back of 5.2% and the US and Asian advanced economies are projected to grow by 3% to 3.5%. However, the collective GDP of advanced economies at the end of 2021 will still be 2% below year-end 2019.

In emerging markets and developing economies, collective growth of 5% in 2021 is projected, with inflation declining modestly to under 5%. The rebound will not be sufficient to regain end-2019 level of activity by the end of 2021. China's recovery will be much stronger than most other countries, with the IMF projecting growth of about 10% over 2020-2021 (1.9% in 2020 and 8.2% in 2021). China was the first economy to face a shutdown, and it rebounded faster than expected thanks to strong policy support and resilient exports. By contrast, India's GDP contracted much more severely, by 10.3%, but is expected to rebound by 8.8% in 2021.

Most developing regions – the Middle East, North Africa, Central Asia, Sub-Saharan Africa and Latin America – are expected by the IMF to recover and grow by around 3% in 2021, with wide differences among countries in each region.

The shock to tourism and the oil sector has hit many developing countries hard, but those with more diversified economies are better positioned for a stronger rebound. ASEAN members are projected to experience a robust recovery of 6.2%, as they are closely integrated into Chinese manufacturing supply chains and their performance will be closely affected by developments in China.

Sovereign debt levels are increasing significantly. Sovereign debt in emerging markets and developing economies is projected to rise by over 10 percentage points to 65% of GDP by the end of 2021, although low interest rates should contain debt service. Yield curves (which show interest rates across different maturities) quickly dropped and flattened in most currencies and are expected to increase only modestly at longer maturities in 2021.

Trade and investment

Global trade was once the cutting edge of the global economy, but since the GFC, trade growth has averaged only 2% annually. Due to the pandemic-induced shutdown, global trade volumes will contract by 9.2% in 2020 according to the WTO – a decline similar to that experienced during the GFC. Global trade volumes are expected to rebound by 7.2% in 2021.

The WTO projects regional export volumes to recover and grow in 2021 by 5.4% for South America, 5.7% for Asia, 6.1% for Africa, the Middle East and CIS member countries, 8.7% for Europe, and 10.7% for North America. For the medium term, the IMF is projecting global trade volumes to grow by around 4% on average.

Notwithstanding the more positive projected trade environment, the trade outlook is difficult for tourism-dependent economies and uncertain for oil exporting nations. Travel and tourism are unlikely to see a robust recovery until an effective COVID-19 vaccine is widely available.

Foreign direct investment is a key driver of global value chains and has increasingly been flowing to emerging markets. However, the pandemic has been a shock to investor confidence and a quick rebound in FDI should not be expected.

Implications for Berne Union members

The projected recovery in output and trade in 2021 is a positive sign, but the recovery is taking place within a turbulent operating environment. A combination of a solid economic and trade recovery, weak international investment, and heightened risks will define BU business activity. In this environment, as claims rise due to the economic slump in 2020, it is reasonable to expect demand for credit and political risk insurance cover to be robust. BU members will in turn be expected by their clients to use their capacity for risk management and innovation to support the business recovery.

Many public sector BU members have already been pressed by their governing authorities to step in and address market gaps highlighted by the pandemic. Debt management challenges and the call for debt service suspension in heavily indebted low-income countries, plus new capital flows, are an added complication for BU members.

There are also important medium-term implications to consider. Pursuing SDGs and Agenda 2030 has been thrust into the spotlight as a renewed priority, creating opportunities and raising expectations for sustainable lending and risk management practices. In addition, and as we saw after the GFC, it will take time before the global economy fully recovers and is performing at its potential, most likely beyond 2025.

Moreover, climate risk will need to be fully factored into BU members' risk and portfolio management practices, addressing both the impact of climate change itself and the transition to a low-carbon global economy now well under way. The COVID-19 pandemic revealed how unprepared most nations and institutions were to manage system-wide risks, and climate change poses a comparable risk management challenge over the long term.

The bottom line? The global economy is now climbing out of a deep hole. Berne Union members will have a central role to play in making the recovery happen. ■

Trade policy under the Biden administration

Robert Kahn, Director of Global Strategy and Global Macro at Eurasia Group, offers a brief survey of key international, regional, and bilateral issues for the new administration.

When it comes to trade policy, you can't go home again. The pursuit of freer, more open trade that anchored economic policy since the Second World War reached its zenith even before the election of President Trump, and the COVID-19 pandemic has only intensified pressure on the US to adopt more protectionist policies toward China and other major trading partners. Backlash to globalisation manifested itself in bipartisan opposition to the Trans Pacific Partnership (TPP) in 2016, which led to President Trump's removing the US from the TPP and subsequent US withdrawal from its traditional leadership role in multilateral institutions such as the World Trade Organization (WTO).

Still, elections matter. President Biden is unlikely to return to robust trade liberalisation, which has reached its political and practical limits, but he will aim to reassert US leadership in the multilateral order, continue efforts to bolster domestic manufacturing in strategic sectors, and seek opportunities to strengthen the role of labour and environmental considerations in existing trade arrangements.

Ongoing US free trade agreement (FTA) negotiations with Brazil and Kenya are unlikely to become congressionally ratified FTAs given the likelihood that Trade Promotion Authority (TPA) will expire without being extended in mid-2021. A bilateral agreement with the UK will hinge on the terms and conditions of the UK's trade relationship with the EU. Trade policy authority and influence are likely to be more broadly distributed across the Biden administration than they have been under the Trump administration, which saw a centralisation of authority under US Trade Representative Robert Lighthizer.

Biden's international agenda

The Biden administration will bring US leadership to bear on key international issues

Robert Kahn

where the Trump administration has been a source of disruption. A more consistent, multilateral US approach will make the most difference in shaping the future of the WTO and devising a global approach to digital taxes.

Since China first entered the WTO, the US, Europe, and Asia have expressed growing concerns over its ability to use loopholes in global trade rules to advance its model of state capitalism. While Trump took a unilateral approach to addressing China-driven global market distortions, Biden is likely to enlist US allies to form a stronger front against Beijing. A key objective of that effort will be revamping the WTO.

Electing the WTO's next chief will be the first step to re-establishing the global trade watchdog's relevance. A new director general will be expected to resolve the current gridlock over the appellate body, push members to deliver on long-running talks, and enact a reform agenda to make the WTO more relevant in the fast-evolving, largely digital, and more complex 21st-Century economy. A more up-to-date set of rules will act as an important firewall against the resurgent protectionist instincts many countries are exhibiting.

The EU expects Biden to end a US blockade on appointments to the appellate body, the organisation's top adjudicator, which has lacked a quorum to issue rulings since December 2019 – meaning that the WTO cannot enforce decisions it renders on trade disputes. Despite longstanding US complaints over the appellate body's overreach – complaints that some other WTO members also express – the new administration will likely seek to resolve the stalemate with a broad-based agenda for

WTO reform that broaches subsidies, state-owned enterprises, and technology transfer.

Biden will likely fold these initiatives into a broader campaign against China, aiming to counter the perception that Beijing has been able to cheat the spirit of the rules-based multilateral system, if not the letter. That campaign will include efforts both to heighten scrutiny of the ways in which China uses its policy banks and to boost the US Ex-Im Bank and the Development Finance Corporation as counterweights.

Washington's stance on digital taxes is likely to follow a similar path. US partners will likely be open to extending an end-of-year deadline for negotiations aimed at establishing a global digital tax regime under the auspices of the OECD. That heightened willingness will likely translate into additional deferrals and/or promises by countries such as France that have already adopted digital services taxes to reimburse excess tax payments, ultimately paving the way for a global regime after tough negotiations well into 2021.

Key regional and bilateral issues

US-EU trade relations stand to receive an immediate political boost, even if some of the underlying tensions continue to prove challenging to resolve. The resurrection of robust transatlantic ties will help both parties form a more coherent front in countering China, both via better coordination of domestic efforts and joint initiatives globally. But trade irritants including the long-running aircraft subsidies battle at the WTO will persist, and efforts to deepen commercial ties will remain difficult.

Biden could make quick and easy progress by unequivocally removing the threat of auto tariffs and ending Trump's steel and aluminium tariffs. The EU would respond by lifting countermeasures and withdrawing its WTO complaint against those US tariffs.

Digital tax discussions will get a new lease on life under Biden. Biden is likely to continue using Section 301 probes in instances where US companies are being unfairly targeted, but he is just as likely to register a complaint with a functioning WTO. His senior foreign policy adviser Antony Blinken has pledged to end the 'artificial trade war' with the EU, and Biden will not continue Trump's tendency to use Section 232 and 301 authority to justify tariffs as a punishment of first resort against policies or developments that he deems undesirable.

But ending a trade war does not mean reviving the Transatlantic Trade and Investment Partnership launched under President Obama – for which there is no appetite in either the US or the EU. While Washington and Brussels will not rule out mini-deals to further trade liberalisation, they are more likely to focus on strengthening common ground in other domains, including cybersecurity and climate change. The US is likely to engage early on –and find challenges in – the EU's plan for border carbon adjustment, which is expected to be made public in greater detail by mid-2021. The US would seek to ensure that the EU's methodology for calculating carbon intensity is applied uniformly across imported products, and that US exporters in jurisdictions with robust climate policies are credited and not exposed to possible 'double taxation.'

Meanwhile, the US will continue working towards an FTA with the UK. Washington will chart the course of discussions, and the UK will want to build on negotiations during the Trump administration by enticing Biden with sweeteners on climate, the environment, and labour standards. Still, implementing an FTA will remain challenging – especially as TPA will expire in June 2021, removing the chances of a fast-track approval in Congress and subjecting the agreement to amendments and the Senate filibuster (if it survives).

Trade negotiations with Brazil will likely be slowed or paused, not only due to the unlikely renewal of TPA in 2021, but also due to greater confrontation by a Biden administration over Amazon deforestation and other environmental concerns.

Finally, while further trade escalation with China will be unlikely in the first year of the Biden administration, substantial tariff relief will remain gradual – and potentially elusive – given likely US demands for concessions from Beijing on market access, intellectual property reform, and state subsidies for private industry that Chinese leaders would be unlikely to make. ■

Eurasia Group is a leading global political risk advisory firm. Founded in 1998, corporates and investors come to Eurasia Group for political risk analysis when they are seeking to understand global and country-specific political dynamics, anticipate market movements, maximise returns and manage risks.

MEGA TRENDS

Boost supply chain resilience through advanced capabilities

By Stefan Schrauf, Operations and Supply Chain Europe Partner, PwC Germany

The COVID-19 pandemic has created a huge amount of uncertainty, but one thing is becoming clear: it's time for companies to take a new look at their supply chain priorities.

In the past, cost has been the primary driver behind many companies' efforts to improve or digitise their supply chain. And though cutting costs is still important, some companies are now optimising their supply chain from a holistic perspective to improve return on capital employed (ROCE), (see Figure 1).

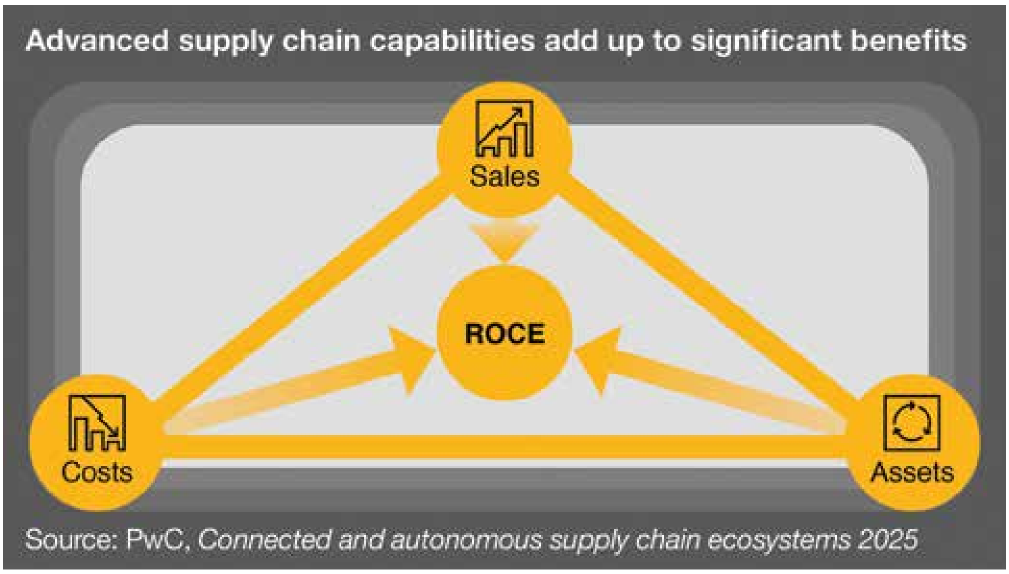
Supply chain setups should be driven not just by cutting costs, but also by enabling sales and getting the most out of assets, to build overall resilience. How can companies get there?

Stefan Schrauf

First things first

COVID-19 has had immediate impacts on supply chains. Across industries, companies have faced major shocks on both the supply and demand side. Demand volatility has significantly increased, and numerous companies have faced unprecedented drop-offs in demand. Some companies are adjusting their supplier base and looking to

Figure 1



Some companies are adjusting their supplier base and looking to implement multi-sourcing strategies. Others are considering greater regionalisation and near-shoring of supply chain activities.

implement multi-sourcing strategies. Others are considering greater regionalisation and near-shoring of supply chain activities. For example, companies with a manufacturing footprint in Europe are shifting their supply base towards European suppliers. According to an analysis by PwC, companies have been reassessing make-versus-buy decisions, and adjusting capacity by up to 20%. Still others have developed new go-to-market approaches and used different channels to reach customers.

All of these changes mean that the time is right for companies to take a closer look at the overall supply chain strategy and make their supply chains both resilient and cost-effective. To do that, companies should focus on optimising their footprint and enhance their financial and cost resilience. And they should draw on the power of advanced supply chain capabilities. By making the most of these capabilities, companies can develop a supply chain ecosystem that's both autonomous and integrated – so they can respond with speed and agility to challenges as they arise.

Advanced capabilities are critical to making supply chains resilient

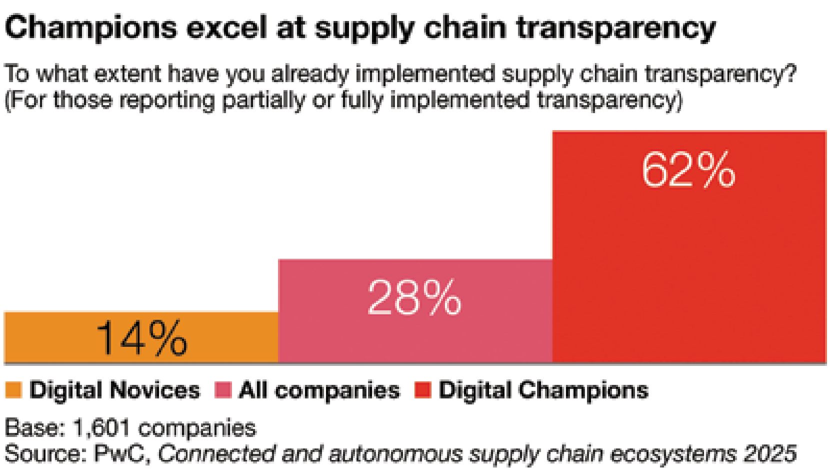
Advanced supply chain capabilities draw on technology, but developing them can require much more than choosing a software solution. It also requires empowering people to use the applications chosen and redesigning processes in order to take advantage of them. A recent PwC report, Connected and autonomous supply chain ecosystems 2025, took a closer look at how companies with the most highly advanced supply chain capabilities – the 'Digital Champions' – use those capabilities to improve supply chain performance and overcome key supply chain challenges. It examined those capabilities that are critical to managing supply chains when a crisis hits, and to ramping back up once it eases.

The report discussed a number of key capabilities, including supply chain transparency, closed-loop integrated planning and execution, dynamic segmentation and smart logistics – all of which are turbocharged by artificial intelligence (AI).

Greater supply chain transparency can help companies better identify and proactively manage risks

Having a 360-degree view of supply chains – not just within their own organisation but

Figure 2



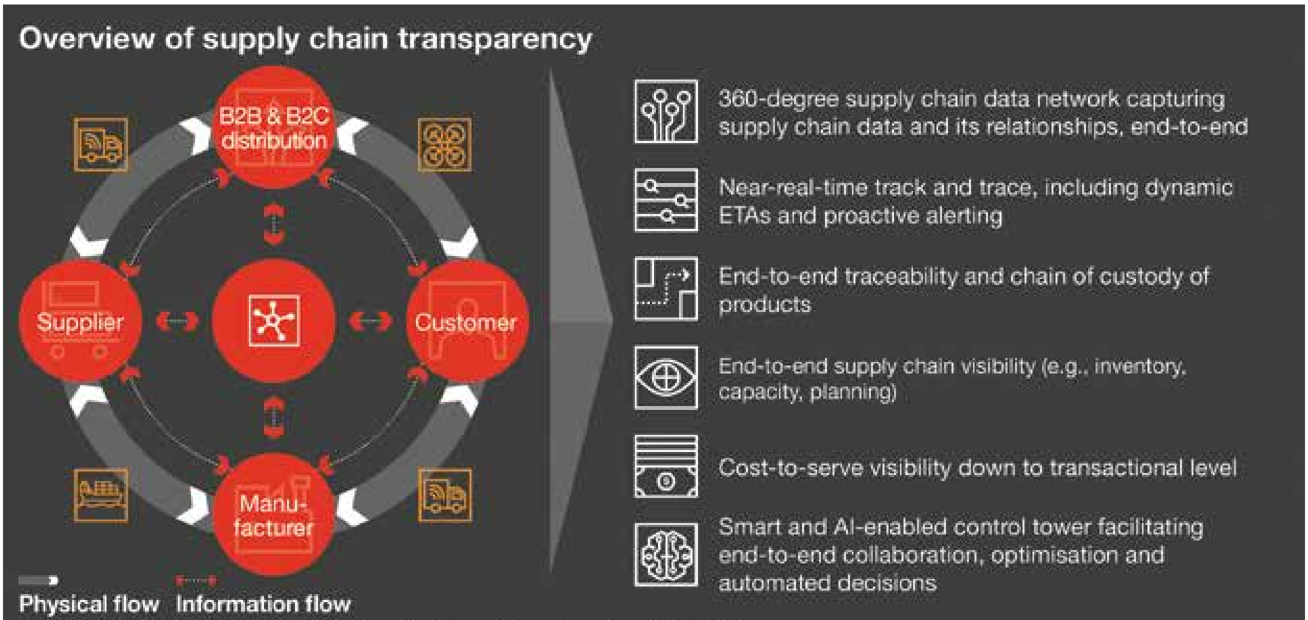
Advanced supply chain capabilities draw on technology, but developing them can require much more than choosing a software solution. It also requires empowering people to use the applications chosen and redesigning processes in order to take advantage of them.

along the entire value chain, from suppliers through to customers – can give companies a competitive advantage during turbulent times and times of relative calm. PwC's report showed that Digital Champions are far ahead when it comes to this area. A full 62% of the group had implemented supply chain transparency (see Figure 2).

Enhancing supply chain transparency gives organisations increased visibility over inventory and capacity, making it easier to identify and manage risks and respond to events, including sharp drops in demand or raw materials bottlenecks. Companies can manage stock levels more precisely, as information on the arrival of raw materials, components of production lines, or finished goods in warehouses is constantly updated. That's especially critical for businesses operating in multiple countries, which could be facing varied operational restrictions.

Another aspect of supply chain transparency is near-real-time visibility over logistics flows, which helps companies manage unique challenges. For example, track-and-trace capabilities help attract customers and strengthen existing relationships by making it possible to estimate arrival times and continually update them based on near-real-time information, and to provide proactive alerts that keep customers aware of shipment status (see Figure 3).

Figure 3



Source: *PwC, Connected and autonomous supply chain ecosystems 2025*

Cash flows are tight, and some companies may be tempted to cut their investments in the development of advanced supply chain capabilities. But that is likely the wrong approach. These investments can pay off, not just in lowering supply chain costs, but in increasing overall resilience.

AI turbocharges transparency

Transparency can be significantly accelerated by the use of AI. In the PwC survey report, 43% of Digital Champions indicated they were making use of AI to generate transparency (see Figure 4).

By detecting relevant patterns in the vast amount of data flowing from the supply chain, AI can help supply chain managers improve visibility into key metrics and better understand the complex workings of their supply chain. This could be the first step on the way to an autonomous supply chain that is resilient to shocks.

AI-powered supply chain transparency solutions can help companies more proactively identify and manage supply chain risks, such as supply shortages, shipment delays or the financial risks of supply chain partners. By simulating different options to address potential threats (for example, selecting an alternative supplier, rerouting shipments), companies gain a better understanding of their potential impact on service levels, lead times and costs. That makes it possible to take proactive measures that will minimise risks to the supply chain.

Stay the course to be ready to ramp up

As governments ease the restrictions they had put in place to combat the spread of COVID-19, transparency becomes increasingly important. Companies will need to be flexible with their suppliers and make sure they can meet rising demand.

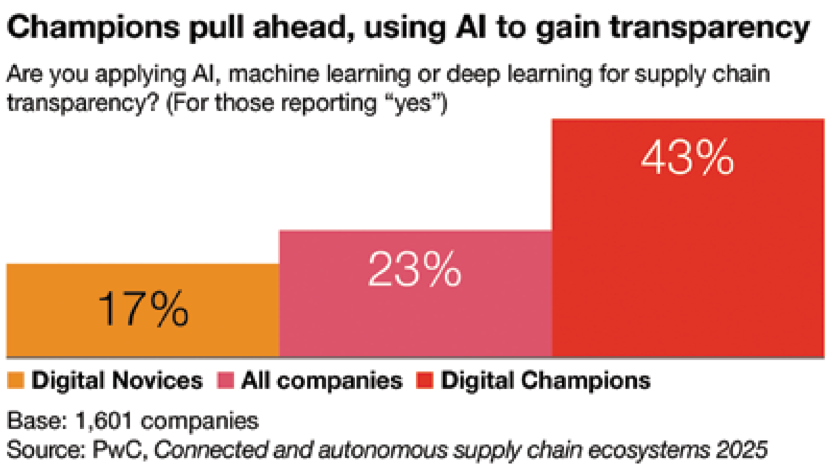
Cash flows are tight, and some companies may be tempted to cut their investments in the development of advanced supply chain capabilities. But that is likely the wrong approach. These investments can pay off, not just in lowering supply chain costs, but in increasing overall resilience.

To learn more about other advanced supply chain capabilities that can help companies take their supply chain to the next level, take a look at PwC's Connected and autonomous supply chain ecosystems 2025 report[1]. ■

Note

1 https://www.pwc.com/digitalsupplychain

Figure 4



Top geopolitics risks for 2021: Expect unique turbulence

By Dr Nicholas Redman, Director of Analysis, Oxford Analytica

The top geopolitical risks for 2021 centre on COVID-19, namely the search for a vaccine, the challenge of inoculating hundreds of millions of people, and the difficulties of economic activity in the pandemic. Add in the prospect of a parting of ways between the US and China over 5G, with both countries vying for the mantle of the world's leading tech power, and the next year will be one of unique turbulence.

In less than a year, there have been 43 million cases of COVID-19 globally and over 1.1 million people have died. At the end of October 2020, a dozen vaccines were in advanced trials globally, with initial results expected before the year-end. This created the prospect that one or a few might be approved, manufactured and released in the first quarter of 2021. Because they are intended to be given to huge numbers of healthy people, rather than far smaller numbers of sick people, the testing and approvals process is usually lengthy and exhaustive. The urgency of finding a COVID-19 vaccine has led to an unprecedented surge in research and development, partly in an effort to shorten what would usually be a timeline of several years.

The vaccine race

For regulatory bodies, safety is non-negotiable. Underscoring this, the US Food and Drug Administration (FDA) strengthened its guidelines on COVID-19 vaccines in October. It now requires trials to have two months of safety data on at least half of their Phase III study participants after a second dose of vaccination (if it is a two-dose regime) before applicants can seek an Emergency Use Authorisation (EUA). Most adverse events occur within two to three months after immunisation.

The FDA has also specified that a vaccine


Dr Nicholas Redman

considered for full licensing will have to demonstrate at least 50% reduction in disease in the test group and safety data spanning at least one year, shown in 3,000 vaccinated persons. Most early-roll-out vaccines will probably be licensed under types of EUAs.

Less than ideal efficacy for first vaccines may be considered, and indeed this is likely. They will still be useful, as they would lower mortality – even if they do not stop the spread of infection – though some social distancing measures are likely to persist.

Beyond the scientific hurdle of developing a good vaccine, its fast and efficient distribution on a global scale requires unprecedented cooperation among manufacturers, governments, cargo operators and ground workers. No vaccine has previously been administered worldwide at maximum capacity and in minimum time, making this one of the biggest diplomatic and logistical challenges encountered by any immunisation programme.

India, China and Europe have the largest capacity to produce vaccines. In 2019, the Coalition for Epidemic Preparedness Innovations (CEPI) was set up to work on vaccines for five priority diseases and also for emerging threats such as COVID-19. A CEPI survey of production capacity involving 113 manufacturers from 30 countries found that two to four billion doses of a COVID-19 vaccine could be supplied by the end of 2021 (catering for 20% of the world population) without compromising other pipelines.

Historically, access to vaccines and therapeutics has not been equitable.

International access to smallpox and polio vaccines, as well as HIV drugs, followed only after high-income countries had procured sufficient supplies. This could happen again with SARS-CoV-2, the virus that causes COVID-19. The Bill and Melinda Gates Foundation estimates[1] that while 33% of COVID-19 deaths can be averted by selling vaccines to high-income countries, this number becomes 61% with equitable access.

The transportation and delivery of vaccines, most of which require cold storage or freezer support, will be a major hurdle. The International Air Transport Association estimates that 8,000 cargo aircraft will be needed to supply a single dose of a vaccine for the world's population. However, it is the vaccine's journey beyond the aircraft that is most vulnerable in areas without a reliable power supply.

The WHO estimates that more than 50% of the world's vaccines go to waste for this reason. This is something the world cannot afford with the COVID-19 vaccine in short supply and where the nature and stability of the vaccine will be extremely important.

The level of vaccine dose needed to elicit an immune sufficient to prevent severe disease or contracting COVID-19 is not yet known. This also means it is unclear whether one or two doses of a vaccine are needed – twin doses have been eliciting stronger immune responses and may be needed for older people whose immune systems are weaker.

To eradicate the virus completely, very high levels of induced population immunity are needed (over 70%), depending on the efficacy of a vaccine and other interventions. If the vaccine in use has sub-optimal efficacy, this coverage threshold may be even higher. This has long-term repercussions for health, and also disproportionately affects economies.

Economic challenges

The IMF projected a loss of $11 trillion from the global economy in 2020-21 and $28 trillion over the period 2020-25, even with the $18 trillion invested to tackle the pandemic. Other metrics on economics from the Institute for Health Metrics and Evaluation show that extreme poverty has gone up by 7%, with 68 million people pushed below the poverty line this year.

In the US, GDP fell by 31.4% in the second quarter of 2020, compared with the first quarter. The supply shock of closed factories at home and abroad was quickly followed by a demand shock, as consumers retreated due to a combination of lockdowns, unemployment and caution over what the future held. The impact varied considerably across the US, with those states heavily reliant on hospitality and tourism bearing the brunt. Manufacturing centres suffered too.

Forecasts for the third quarter see GDP rising by 30% or more, largely but not wholly restoring the lost output. Manufacturing has recovered unevenly, while consumer sentiment remains fragile and vulnerable to a winter wave of infection, further layoffs and constraints on government financial and social support. The regional Federal Reserve banks already report that the pace of recovery in tourism and retailing is slowing. That suggests the states most heavily dependent on accommodation and food services will take longer to recover. Along with uncertainties about the long-term impacts of increased digitalisation, from remote working to e-commerce and online services, this clouds the outlook for commercial construction and real estate. The agricultural sector faces an extended period of low prices and so too does the energy sector.

The key question for the US economy, and for many economies around the world, is whether they will suffer a relapse in the fourth quarter of 2020 and the first quarter of 2021, as COVID-19 case numbers and fatalities rise in many places. Already in October there were signs that economic recovery and employment were slowing as the virus resurged. Add in the end of furlough schemes in many parts of Western Europe, and it is entirely possible that the V-shaped recovery could become a W-shaped one. Some businesses have adjusted to operating in a COVID-19 environment but many cannot, or at least are only able to operate at greatly reduced capacity. The loss of demand, and uncertainties as to how much of it is permanent, further darken the picture. In most of the world, if not all of it, economic activity will take place under the cloud of COVID-19 for all of 2021 and into 2022.

The tech divide in telephony

The year 2020 started with a truce of sorts in the trade war between the US and China, as the two countries signed a 'phase one' agreement that removed some of the tariffs that had been applied in tit-for-tat

The world now stands on the verge of a 'tech separation' between its two leading powers. If there is a parting of the ways, two separate sets of standards and two distinct technology spheres could develop in time.

exchanges over 2019. However, already the dispute had developed a more disturbing aspect: for while the trade war began as an effort to reduce the large US trade deficit and to revive blue-collar jobs there, it soon acquired a technological facet. Parts of the US establishment worried that China was positioned to steal a march in rolling out 5G telephony at home and abroad, which would help the country to become richer, to get a head-start on other emerging technologies and to set 5G standards globally. And in the vanguard of this were companies that had been built partly on stolen US intellectual property.

To slow China down, in May 2019 the Trump administration banned US companies from shipping components and technology to Huawei, and imposed licensing obligations for semiconductor manufacturers using US equipment or software to produce Huawei-designed chips. Huawei was able to withstand these measures by purchasing generic components instead of custom-designed chips or routing purchases through third parties and third countries. It even reported sales growth, albeit driven largely by the Chinese domestic market. To provide long-term solutions, Huawei had invested in alternative options, including powerful chipsets able to replace imported US components. Huawei's Kunpeng chip, for instance, is slated to take over the role of Intel-sourced components.

The US also stepped up the pressure on allies to bar Huawei from their 5G infrastructure, with limited success. Then in August 2020 it announced that it would ban the sale to Huawei of all semiconductor chips using US equipment or software. This targeted the greatest vulnerability in Huawei's plan, because the new measures prohibited the sale to Huawei of all chips manufactured worldwide using US equipment or software.

Only three businesses are able to deliver end-to-end software solutions needed for advanced chip production: US-based Cadence and Synopsys, and Germany's Mentor Graphics, which operates in the US and therefore also falls under these restrictions. Huawei systems run older versions of their design tools. If these cannot be updated or supported, their efficacy will soon diminish.

Companies in certain areas of manufacturing tools are the sole providers of indispensable components. Of these, KLA-Tencor, Applied Materials and Lam Research are US-based. Given these bottlenecks, the latest US measure effectively makes it impossible for Huawei to acquire the chips it needs to manufacture its products.

Huawei sought to stockpile as many components as possible before the ban took effect. It might run out of smartphone components in early 2021, but could have enough components for 5G base stations to last through 2021 and sometime beyond.

Thus far, China's response has been muted. Possibly it is hoping for a change of administration in the US, and a chance to ease the stranglehold on Huawei. The company still needs US technology. Moreover, if the company, and by extension China, are not able to deliver 5G at home and abroad as planned, setting standards along the way, it will deal a blow to China's hopes to become the world's leading nation in AI, robotics and autonomous systems in the mid-2030s.

US policymakers might calculate they can stop Huawei in its tracks, but if Beijing becomes convinced that no deal is possible, it will direct huge resources into breaking free of the limitations and US dependencies that until now it has accepted.

The world now stands on the verge of a 'tech separation' between its two leading powers. If there is a parting of the ways, two separate sets of standards and two distinct technology spheres could develop in time. Few countries would be able to avoid making a choice between one or the other. The implications of that would resonate well beyond 2021, and quite possibly long after COVID-19 has been reduced to a manageable problem by the development and rollout of vaccines to billions of people globally. ■

Note

1 https://www.gatesfoundation.org/goalkeepers/report/2020-report/#CollaborativeResponse

WTO on the enhanced need for trade finance cooperation

Marc Auboin, Counsellor at WTO, examines the phases of the global response to what is proving to be a crisis that has very different features to others and highlights the need for accelerated cooperation in financing trade.

Since the beginning of the COVID-19 crisis, the World Trade Organization (WTO) has been working with its partners, a high-level group of experts in trade finance (private banks, export credit agencies and multilateral development institutions), to monitor the market situation and alert public authorities on rising trade finance shortages. Based on the experience gained in previous crises, governments and international institutions have intervened in various ways.

The 'structural' shortfall of trade finance has been estimated to stand at around $1.5 trillion in recent years, mainly in developing countries, according to the Asian Development Bank's (ADB) trade finance gap study. This shortfall, measuring the excess global demand for trade finance, is the outcome of a combination of factors: macroeconomic (low savings that could be turned into loans in developing countries), financial (the developing state of the financial sector), and international (the reduction in the number of correspondent banking relationships since 2009-10).

Previous economic and financial crises, such as the 1997-99 crisis of emerging economies in Asia, Latin America and Central Europe, and later the global financial crisis of 2008-9, taught that existing shortfalls widen when the perception of risk increases well beyond its actual level. International banks thus 're-shore' lending, focusing on 'safer' customers. While this has already happened since the beginning of the COVID-19 crisis, this crisis is like no other.

The differences this time around

Present difficulties do not originally come from the financial sector, which is much better equipped and prepared to sustain

Marc Auboin

both a supply and demand shock, than it was a decade ago. In the first phase of this crisis, successive regional lockdowns have resulted in significant operational challenges.

Legal documents necessary to process trade finance transactions (customs documents, invoices, bills of lading) have either been delayed or not transmitted at all. These difficulties have come on top of the challenges of moving goods physically. Interim solutions have worked in some countries, with the increased use of scanned documents and e-documents (such as e-bills of lading). Certainly, the digitization of documents has been given a boost during this period. All in all, the trade finance industry has 'coped', despite all prevailing physical and procedural difficulties, and it managed to sustain the flow of essential medical equipment and foods essential during this period, around the first semester of the year.

As operational issues were gradually resolved, liquidity issues and the deterioration of credit risk came to the forefront of concerns about trade finance. Significant liquidity shortfalls emerged in the poorest countries. In Africa, the tightening of liquidity was immediate as several international and regional banks had either cut their funding lines to African financial institutions for trade transactions or increased its cost. In other developing countries, including in Latin America, Northern Africa and Central Europe, liquidity also dried up, notably in US dollars.

Financial institutions also showed increased risk aversion as overall credit risk deteriorated. With the health crisis persisting, banks had been expecting increased payment failures from counterparties, beyond sectors initially impacted by the lockdowns (airlines, aeronautics, tourism, and to some extent the automotive sector). It quickly appeared that one-off extensions of the terms of payment by creditors would be sufficient to alleviate this crisis.

In many developing countries, sovereign risk deteriorated along with corporate risk, resulting in increased caution by international banks to engage in cross-border trade finance. Importers' banks in poor and even middle-income countries could not find counterparties for financing many types of goods, ranging from energy commodities to consumer goods. Domestically, the high demand for large banks' balance sheets also explains the greater reluctance to engage in cross-border trade operations.

Public sector support

Public authorities took on the challenge of supporting markets. As in previous crises, the first challenge is to channel liquidity and credit guarantees to SMEs, as smaller companies are the most 'cash-sensitive' in supply chains. In many countries, central banks provided very large amounts of liquidity to the financial system and government-sponsored schemes such as (trade) loan extension, repayment holidays, undertakings and credit guarantee schemes have offered significant relief to smaller and large companies, particularly those on the main routes of trade. The Federal Reserve revived 14 swap agreements with central banks around the world, in order to provide US dollar liquidity.

Credit insurance schemes have also been helpful in supporting receivables finance and other forms of finance used in supply chain trade, notably by SMEs, thereby avoiding a collapse of supply chains. As described by the Berne Union, a significant response from insurers of export credit, resulted in supporting traders – through flexibility and relaxation of terms for policyholders (exporters), increased capacity through new direct cover and reinsurance by public insurers, support for export finance (including working capital), deferred payments schedules, extended repayment periods, and waivers of some interest and fees. However, this meant in part that the full extent of claims and 'losses' would not be realized immediately.

Multilateral development banks (MDBs) had also been in the 'field' from day one, filling some of the gaps left by a withdrawing financial system. The International Finance Corporation had received support from its Board of Directors on its trade finance program, which was integral to the World Bank Group crisis response, in supporting the imports and exports of essential goods and commodities of the poorest countries. Demand for IFC trade finance facilities had increased by 110% since the start of the crisis. The African Development Bank supported local banks in their requests to have letters of credit endorsed internationally. Supply chain finance programs of the ADB, the EBRD and the IFC were in very high demand, reflecting the effort to preserve the export capacity of developing countries in their countries of operation. The Islamic Trade Finance Corporation also worked through local financial institutions to support SMEs across its membership. Requests for multilateral banks' facilities have come from over 80 countries, showing the global extent of the problem.

The trade finance situation is expected to remain challenging in the months to come, as demand for traded goods picks up, while country and corporate risk continues to be weak in many countries and defaults of payment materialise.

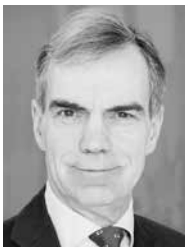
WTO highlighting the need for trade finance cooperation

Against this background, the Director-General of the WTO raised the profile of trade finance as one of the many pressing issues requiring international support and cooperation. On July 1, 2020 he issued a joint statement with six other heads of multilateral development banks, pledging greater coordination in providing support to trade finance markets, particularly towards developing countries.

In parallel, the Director-General has pledged to work with the private sector (the International Chamber of Commerce and the B20) to the same aim of pooling resources and support to trade finance markets. The presence of public actors in markets is visible, and it provides for a stabilizing effect of markets. The situation will continue to be monitored carefully by the WTO through the expert group on trade finance, which remains a very useful forum of dialogue between all the parties involved in supporting trade finance. ■

Risk Outlook 2021

The chief economist of Atradius and the head of macroeconomics for Euler Hermes give their view of the top five risks facing global trade in 2021.



John Lorié, Chief Economist, Atradius Credit Insurance

Global trade resilience during the COVID-19 crisis: Will it last?

When COVID-19 knocked on the door in the early spring, hopes for global merchandise trade were depressed. At that point, our estimates were of a contraction in the range of 15%-30% in 2020. That was based on the experience in the Global Financial Crisis (GFC) when global trade contracted 13%, while GDP contracted by 'only' 0.1%. This time global GDP was forecast to shrink by 5%, so such a deep contraction in global trade in 2020 could even be considered an optimistic forecast. But now, more than six months since the global COVID-19 outbreak began, matters look better. The damage to global trade in 2020 is now expected to be much milder with a 10% decrease compared to 2019, followed by a rebound of 7.5% in 2021 as the global economy recovers.

Several factors have contributed to the relative resilience of global merchandise trade. The GFC was a crisis in the financial system that spilled over to the real economy. The COVID-19 crisis is caused by lockdowns and travel restrictions that particularly affect the services sector (especially hospitality, entertainment and tourism). These service sectors are a substantial part of GDP, but the merchandise trade component is relatively small. Not going to the cinema or a restaurant hits GDP, but hardly global trade. As opposed to the GFC, the current crisis has clear winners, such as IT products and services as a result of working from home and the much higher demand for medical equipment and drugs. These are largely traded merchandise.

Moreover, this time governments and central banks have intervened much earlier in the crisis than during the GFC, and entire sectors as well as households are receiving support rather than just the financial sector. This cushions demand fallout resulting from the high level of uncertainty in this crisis. That lower impact on demand helps alleviate pressure on imports. But, like the GFC, the role of China is crucial. It is the only major economy that is forecast to grow in 2020. After stringent public health measures during the early spring, the country has embarked on a fairly steep recovery path, boosted by government stimulus, predominantly on the supply side: public investments, support for state owned enterprises and liquidity provisioning via the banking system. While consumption growth is still muted, exports have soared. Finally, unlike during the GFC, financing of trade has remained in place, supported by governments that have given export credit agencies more leeway.

While these factors support global trade, the path for 2021 is fraught with risks, predominantly, though not limited to, the downside. The answer to the question of whether the resilience of global trade lasts depends on the following five factors.

The GFC was a crisis in the financial system that spilled over to the real economy. The COVID-19 crisis is caused by lockdowns and travel restrictions that particularly affect the services sector (especially hospitality, entertainment and tourism).

First, the main risk is a second wave of coronavirus infections that would result in renewed lockdowns globally. As restrictions are lifted and social interactions increase, the transmission rate has been picking up again. Should this trend continue, governments reimpose the kind of restrictions that depressed economic activity during the first wave of COVID-19. This would further raise the level of uncertainty in the economy, again depressing consumption and investment by households and firms. Trade would be negatively affected. This risk is increasing in some European countries that suffer from new COVID-19 outbreaks, threatening to push their economies into a double dip recession.

Second, national governments may not get their policies right. The recovery hinges on support from national governments. During the lockdowns in the early spring of 2020, governments were generous to prevent a complete meltdown of the global economy. This was necessary, but not sufficient. During the recovery phase of the crisis, governments should continue to provide support. But their support should strike the right balance between keeping up household income on the one hand, while maintaining the incentives to switch jobs if needed. Governments should also help viable firms, rather than zombies, through the crisis and thus allow the Schumpeterian creative destruction process vital for economic development, and global trade.

Third, central banks, and especially the Federal Reserve and the European Central Bank, have a critical task to keep the world awash with money and finance costs low. Premature tightening may lead to financial unrest, falling equity prices, financial flows away from emerging economies and US dollar appreciation. Against the backdrop of higher debt levels around the globe, especially those of governments, this may result in higher finance costs at the very least. Like in the GFC, trade finance may then be disproportionally negatively affected.

Fourth, protectionism, especially the resumption of the trade war between China and the US, is a risk to trade recovery. Protectionism has been on the rise since the GFC, and 2020 confirms this trend thus far, albeit at a slightly slower pace than during 2019. Harmful trade practices have outpaced liberalisations by roughly three-to-one in 2020, somewhat lower than the four-to-one ratio last year. While this drags on global trade, protectionism in general is a gradual, though harmful, process. The trade war between China and the US is another matter. Currently the average level of US tariffs on Chinese imports is seven times higher than in 2017, with each round of tariff levy negatively impacting bilateral trade. Due to the 'Phase One' deal that the US administration struck earlier in the year, a truce exists. But the resumption of tariff levying between the US and China (and potential extension to the EU) still hangs over the trade environment, independent of the result of the US presidential election. The uncertainty that comes with it is negatively affecting the trade environment.

Fifth, to end on a high note, there is a conceivable upside scenario for global trade in which recovery is more rapid. This is only possible should the four aforementioned downside risks not materialise. In this upside scenario, scientific advances facilitate a faster easing of public health restrictions. As a result, social distancing measures can be relaxed earlier than expected in 2021. The swifter return to normal fosters increased confidence and spending among consumers, as well as businesses. This allows for a more robust pace of economic recovery in 2021, with a clear positive impact on trade as well.

To end on a high note, there is a conceivable upside scenario for global trade in which recovery is more rapid. This is only possible should the four aforementioned downside risks not materialise. In this upside scenario, scientific advances facilitate a faster easing of public health restrictions. As a result, social distancing measures can be relaxed earlier than expected in 2021.

Alexis Garatti, Head of Macroeconomics, Euler Hermes

Credit insurers to play a key role in combating a credit crunch during COVID-19

The importance of intercompany credit

According to a recent study by the Bank for International Settlements (BIS[1]), trade finance accounts for 20% of global GDP, a value close to that of corporate bond financing, while bank loans to these companies represent three times that amount. Trade payables and receivables represent core elements of working capital and intercompany financing. They have a key position in the smooth functioning of global supply chains. However, the COVID-19 crisis has undermined intercompany credit or trade credit through four main channels:

- This crisis has primarily taken place on the real side of the economy rather than within banks or the financial system, as it was the case during the GFC of 2008-2009. The abrupt interruption of all economic activity due to COVID-19 lockdowns, and their possible reoccurrence in the context of a second wave, led to a fundamental disruption in the relationship between customers and suppliers in the usually natural adjustment of payables and receivables. Despite huge liquidity injections and strong support mechanisms from governments, B2B liquidity is likely to have experienced a significant shock.
- The crisis has primarily affected service activities due to lockdowns, and thus has had a greater impact on smaller companies, which traditionally already face higher difficulties in accessing liquidity. Instead of a core-periphery transmission of the crisis, we have had a periphery-core transmission of the shock into the overall economic system, making the identification of fragile actors a more challenging issue.
- Mechanisms of credit guarantees and very rapid interventions of states and central banks to support demand temporarily smoothed the impact of the crisis. For the first time in economic history, help from governments impacted the real side of the economy before the full materialisation of a recession.
- Finally, as the crisis has affected all sectors without discrimination, risk diversification has become impossible. Companies' interlocking chains of receivables and payables can no longer rely on the multiplicity of interconnections and on the protection of credit insurers to absorb the default of any isolated ailing trade partner.

Credit insurers and governments decided to share the risk

The COVID-19 crisis has highlighted the central role credit insurers can play in financing the economy, both locally and internationally. They traditionally offer protection to companies via trade credit insurance (ensuring the compensation of a commercial debt in the event of non-payment by a customer), debt collection (services to help policyholders recover outstanding debts from late or defaulting debtors) and information (providing insights on creditworthiness and business, as well as country risk analysis). However, in the current crisis, credit insurers cannot assume all the costs of this kind of systemically non-diversifiable shock alone. This is the reason why they have pre-emptively asked governments to share the risk. Several risk-sharing mechanisms between states and credit insurers helped avoid a credit crunch scenario, alongside large liquidity injections and credit-guarantee mechanisms.

Mechanisms of credit guarantees and very rapid interventions of states and central banks to support demand temporarily smoothed the impact of the crisis. For the first time in economic history, help from governments impacted the real side of the economy before the full materialisation of a recession.

Were these joint interventions effective?

The evolution of working capital is difficult to measure, along with that of trade credit in general. In order to capture the most recent evolution of intercompany credit, we built a proxy calculating the spread between the growth of credit to the private sector (households and companies) and the growth of deposits of these private actors. The non-deposited part of credit circulates in the economy and serves as a support of intercompany or trade credit. By contrast, the more this spread increases, the more

Table 1: Risk-sharing mechanisms involving states and credit insurers

Country	Mechanism	Guarantee	End date
France	State guarantee (global approach) Additional coverage on a case-by-case basis	• Loss coverage rate: 75% (relay CAP), 95% (State CAP+), 100% (state CAP) • Envelope: €15 billion (€10 billion for the internal market + €5 billion for exports)	
Italy	State Guarantee (to credit insurers established in Italy)	• Envelope: €2 billion • Loss coverage rate : 90%	Dec 2020
Belgium	Reinsurance/quota share	• Envelope : €903 millions • Increasing loss coverage rate with disbursements/premiums ratio	Dec 2020
Portugal	Additional coverage	• Loss coverage rate : 100% (with indemnities paid directly by the government)	Dec 2020
Canada	Additional coverage (global approach)	• Loss coverage rate : 100% up to US$ 100 million	No time limits for exports, Domestic coverage until Dec 2021
UK	Reinsurance agreement (global approach)	• Loss coverage rate : 90% below GBP 1 billion and 100% between GBP 1 billion and 30 billion	Dec 2020
Germany	State guarantee (global approach for German credit insurer)	• Loss coverage rate: 90% up to €5 billion ; 100% between €5 billion and €30 billion	Dec 2020
Norway	Reinsurance agreement	• Envelope : NOK20 billion and a maximum of 35% of each insurer's total coverage volume in 2020 • Loss coverage rate: 90% up to NOK1.8 billion; 100% above NOK1.8 billion	Dec 2020
Netherlands	State guarantee (global approach, for credit insurers established in the Netherlands)	• Loss coverage rate: 90% up to €1 billion; 100% between €1 billion and €12 billion • Envelope: €12 billion	Dec 2020
New Zealand	Additional coverage (on a case-by-case basis)	• Surplus of 100% of guarantee and premiums for the state	No time limits

Sources: Local public authorities, Euler Hermes companies reduce their precautionary liquidity pool, which means that they do not experience, or fear experiencing, payment difficulties, late payments and other payment defaults. Interestingly, Figure 1 shows that there is a close link between this proxy and trade credit as measured by the BIS.

Looking at this indicator, we can see that trade credit is not likely picking up despite powerful mechanisms to guarantee and support corporate credit in general, as well as massive liquidity injections. As of now, credit granted by banks does not really finance trade, but rather inflates the pool of cash that companies are holding as precautionary savings. During the subprime crisis, doubts about the weakest link in the banking system led to a freezing of the money market. In today's crisis, generalised doubts about the solvency of companies has triggered a freezing of intercompany credit. Euler Hermes indeed believes that the number of corporate failures at the global level could rise by around +31% by the end of 2021.

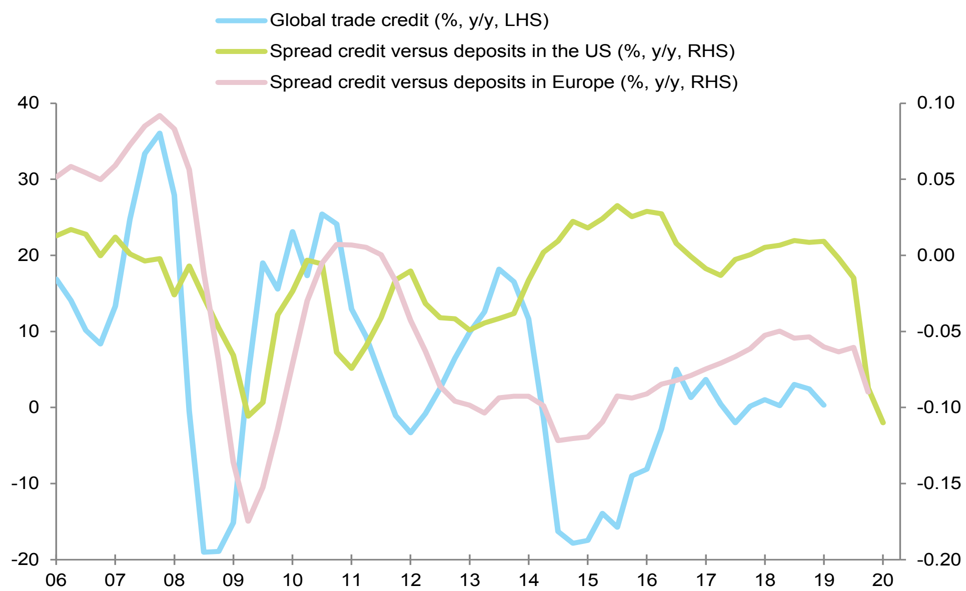
In this context, we expect a yearly contraction of trade in goods and services of -13% (compared to -11% in 2009) in volume terms. The recent depreciation of the US dollar should alleviate the negative price effect of the oil and commodity price shock in H1, bringing the trade contraction in dollar value terms to -16% this year (vs. -20% in our previous forecast). This is equivalent to $4 trillion of trade losses. In 2021, global trade in volume terms should grow +7%, and in value terms it could grow by +13%, finally recovering all its losses by early 2022. ■

During the subprime crisis, doubts about the weakest link in the banking system led to a freezing of the money market. In today's crisis, generalised doubts about the solvency of companies has triggered a freezing of intercompany credit. Euler Hermes indeed believes that the number of corporate failures at the global level could rise by around +31% by the end of 2021.

Note

1 BIS Bulletin, N° 24, Trade credit, trade finance, and the COVID-19 Crisis, Frédéric Boissay, Nikhil Patel and Hyun Song Shin

Figure 1. Global trade credit and proxy (%, y/y)



Sources: Euler Hermes, Allianz Research

3

Market trends


XL Insurance
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The financial strength to support your business across the globe
Political Risk, Credit & Bond Insurance
We believe change is inevitable, and a powerful catalyst for innovation and progress. We also recognise stability and an open way of working are the foundations to building strong partnerships.
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The COVID-19 stress test: Impact and response of the export credit insurance industry

Summary analysis of the Berne Union's COVID-19 Impact Surveys

By Paul Heaney, Associate Director, Berne Union

Although ours is a niche industry, not widely understood outside of specialist circles, its objectives are relatively simple: to provide direct and indirect support for cross-border trade through a combination of risk mitigation (increasing business confidence) and credit enhancement (access to liquidity) tools.

The distinctive features of the COVID-19 pandemic – sudden onset, global but disparate impact, prolonged but uncertain duration and non-financial origin – are uniquely challenging to these objectives, especially when applied to the highly-integrated and complex global value chains which have become so prevalent in the last decades.

The crisis has undermined both the financing and performance of international trade, delivering a double blow with simultaneous impacts on buyers, exporters and counterparties as well as insurers themselves.

The Berne Union has been monitoring the impact of, and response to, the crisis through a series of Member Surveys, the most recent of which was completed in late September 2020.

We asked Members how the pandemic has impacted their business, what specific measures they have introduced in response and their expectations for the future, both in terms of the immediate impact (e.g. claims) and the bigger picture and structural changes to the industry. This article summarises the main findings from these reports.

Paul Heaney

The industry response has been comprehensive and remarkably quick

The speed of response across the export credit insurance industry, from both public and private institutions has been quite remarkable.

At the time of our first survey, in late March, 74% of respondents had already implemented new mitigation measures, and a further 21% indicated they were in the process of implementing this. Six months later, by September, 94% (including 100% of public Members) reported details of at least some COVID-19 support measures implemented. Even those Members who reported no changes in the specific areas addressed by this survey, still indicated increased vigilance, risk management and communication processes.[1]

The response measures introduced by different institutions are highly specific to the circumstances of the individual insurer and the profile of their business. Even so, these can be characterised as targeting the following four broad areas:

1. **Supporting policyholders** – including everything from reduced fees and waivers to flexible adjustments, lightened requirements, expedited processes and non-financial support and advice

2. **Maintaining trade capacity** – with

increased limits, greater percentage cover, and top-up or reinsurance of the private insurance market

3. **Ensuring liquidity** – through new products and extended facilities to provide and/or enable bank lending for working capital and cashflow, combined with adjusted eligibility requirements to ensure access for those in need

4. **Protecting industries** – with targeted support, payment holidays and broad debt rescheduling for the most vulnerable industries or obligors (in the case of the Paris Club Debt Service Suspension Initiative (DSSI)).

Figure 1 shows a summary of support measures by broad category.

These measures have proven effective in their main objectives: Slowing or preventing huge defaults in the immediate wake of the crisis; maintaining access to finance and liquidity for exporters and supporting the most vulnerable sectors.

In many (although not all) cases, ECAs have been a conduit for some part of their government's wider COVID-19 response packages. The response measures reach well beyond pure export support and show a deep understanding of the holistic challenges facing clients.

Figure 1

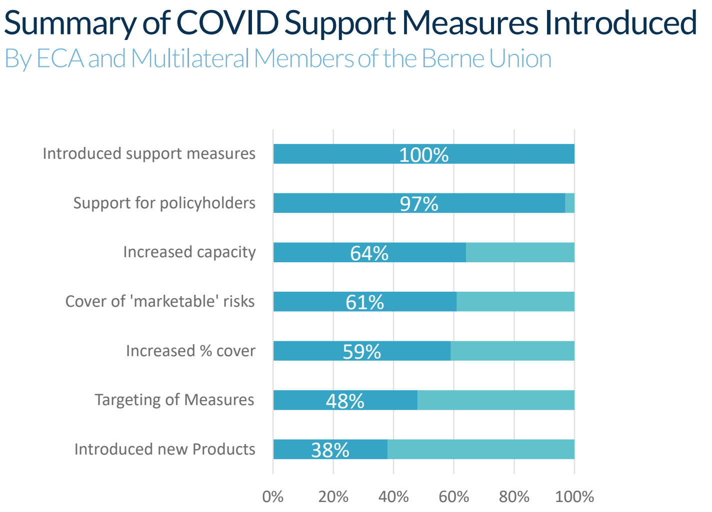
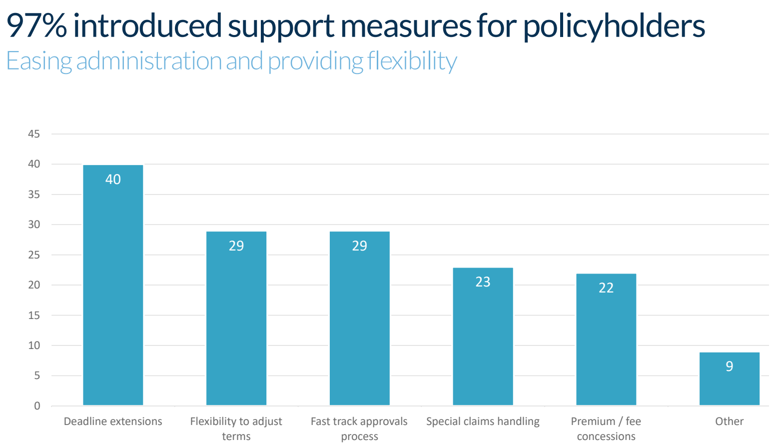


Figure 2



Almost all Berne Union Members have introduced measures in direct support of policyholders

The majority of these measures are administrative adjustments designed to either speed up the processes of the insurer (credit approvals, claims handling), or reduce the burden on the insured (deadlines and documentation requirements). A sizable portion of ECAs offer direct relief in form of premium and fee concessions, but the overall thrust of these measures is 'flexibility'. Flexibility between insurer and insured, but most importantly flexibility between insured and buyers, allowing the proactive risk management of all parties to prevent unnecessary contagion and escalation of credit risks.

Figure 2 provides a breakdown of measures in support of policyholders.

Some of the 'other' soft measures introduced include crisis support, assistance identifying new, free access to collections support, etc.

Public/Private cooperation is critical to maintaining trade capacity

One of the great strengths of the export credit insurance industry (as well as the Berne Union) is the complementary role of public and private sector.

Although these two spheres of the industry are driven by very different imperatives, they operate in a mutually beneficial symbiosis to increase capacity, diversify risks, apply data and reach clients.

In medium and long-term business, one of the principal developments over the past 20 years has been the increasing participation of private insurers, who have increased their appetite for these risks, alongside ECAs and behind them in the form of reinsurance.[2]

Due to their public mandates, it is natural that ECAs are at the centre of the COVID-19 response measures we are discussing here, but it is also worth remembering the significant role private insurers continue to play in maintaining cover and capacity during the crisis.

A good example is the (partial) transfer of so-called 'marketable' risks from private to public sector, following the rapid deterioration of short term credit risks in developed markets as the pandemic unfolded. In the European Union, this is formalised by the Commission's Temporary Framework[3] for State aid measures, in which 91% of EU ECAs indicate participation. But ECAs from countries outside the EU also report temporary interventions with a total of 61% of all ECAs surveyed reporting provision of new temporary cover for 'marketable' risks, ordinarily covered by the private insurance market.

The precise mechanisms vary from country to country, with most ECAs providing cover directly to exporters, and a smaller proportion through reinsurance of the private market (see Figure 3).

New products focus on providing liquidity

In the first phase of the crisis, the biggest risk has been compression of cashflow as firms struggle with a combination of logistic disruptions, reduced demand and tightening finances. For many exporters the challenge is as much in financing their domestic supply and production cycle as their final exports.

This is reflected in the new products or programmes introduced by 37% of ECAs during the crisis, the majority of which relate to working capital and other instruments designed to provide immediate cashflow support, including inventory finance and bridge loans, as well as risk mitigation against demand volatility through e.g. pre-shipment cover/order-cancellation (see Figure 4).

Of course, domestic support for export is not entirely new, and an increasing number of ECAs were already providing these products before the pandemic. Nonetheless, Berne Union data shows a notable +50% increase in new commitments during the first half of 2020, relative to the previous year.[4]

A full 69% of survey respondents note at least some degree of tightening appetite from financing banks, and in many cases it is these who are the direct beneficiaries of the new products, with ECAs providing insurance or guarantees in respect of working capital, liquidity loans, or securitisation for commercial banks as well as other public lenders.

Targeted measures for SMEs and vulnerable sectors

Some form of targeting in the support measures introduced is mentioned by 48% of survey respondents. Of these, 79% indicated special facilities for SMEs. This is not to the exclusion of other clients (some ECAs also introduced schemes specifically for large

Figure 3

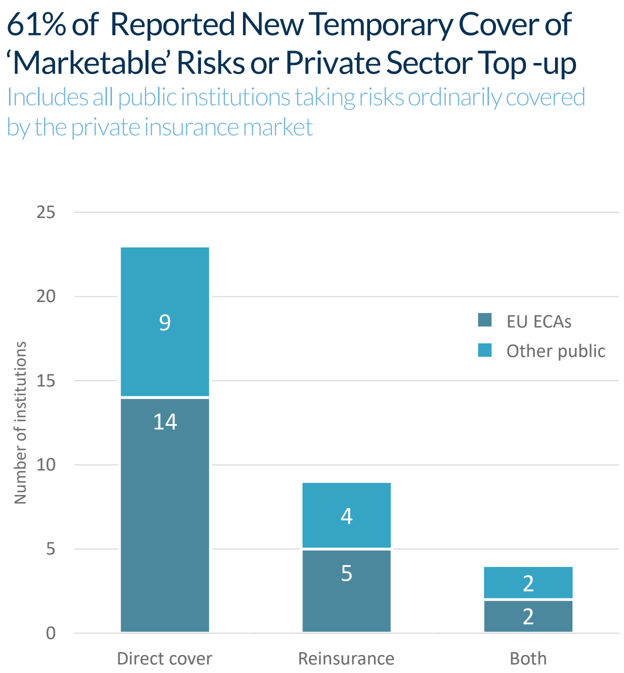


Figure 4

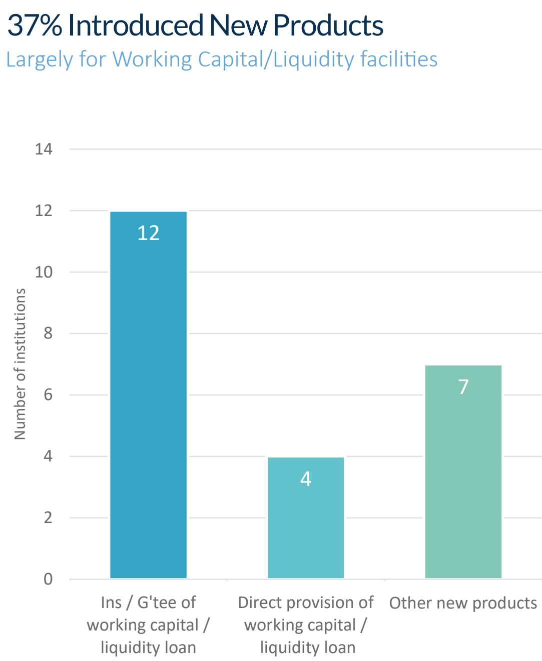


Figure 5

48% indicate some kind of targeted measures

The vast majority (79%) mention SMEs. Other targets include: Vulnerable and essential sectors / high national content / new clients

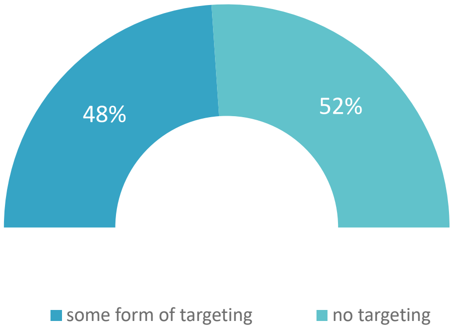


Figure 6

64% increased capacity for at least one line

Largely for cross-border activities

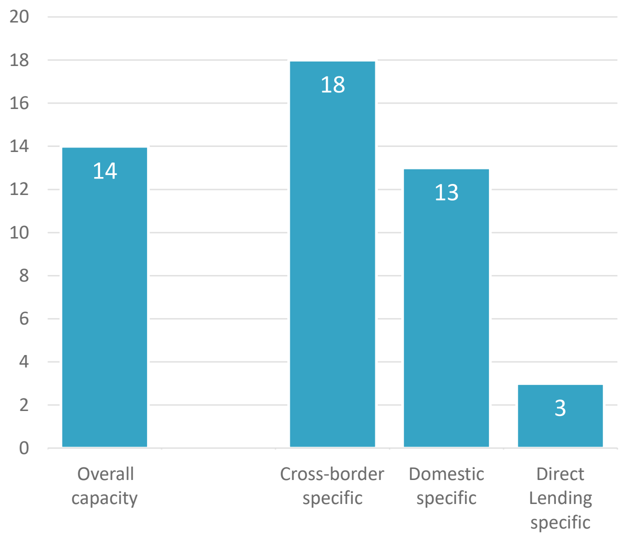
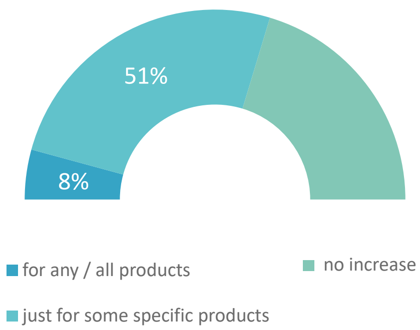


Figure 7

For at least some products



corporates) but rather reflects consideration of the different requirements of different client groups. Changes to definitions used in eligibility criteria – 'SME' or 'exporter', for example – have also been used to allow greater flexibility in support.

Some Members indicated no requirement for targeting due to the relatively homogeneous makeup of their exporters in any case (i.e. often largely SMEs, for smaller countries).

Beyond this, some are targeting sectors especially vulnerable to COVID-19 impact (tourism, construction, retail automotive), while others mention industries core to national interest, support for health infrastructure and supply (PPE equipment) or where national content is high. 'New clients' are also mentioned (see Figure 5).

Members are maintaining capacity as well as a sensible risk underwriting

Aside from filling gaps with new products and market intervention, Berne Union Members have also increased capacity within their ordinary product suite – 64% of survey respondents increased capacity and 59% increased their maximum percentage of cover for at least one product or overall business line (see Figures 6 and 7).

The peculiar circumstances of this crisis entail that, to some extent, the normal rules of credit and country risk no longer apply. ECAs need to direct capacity to supporting viable risks, while continuing to exercise prudent underwriting.

This is reflected in the survey data by reports from the majority of Members that they are reducing limits for individual sectors, countries and counterparties, even while increasing risk appetite overall (see Figures 8-11).

Demand for cover is increasing and utilisation of products with COVID-19-specific measures accounts for a significant proportion of overall business

A full 77% of Berne Union Members report at least some increase in demand for cover. The majority is for short term credit and working capital products – in line with Members' increased provision in these areas. MLT and PRI business is relatively stable in forward pipelines, but with many projects delayed or on hold this will develop slowly.

Of those reporting an increase in demand, 80% indicate a notable increase from new

Figure 8

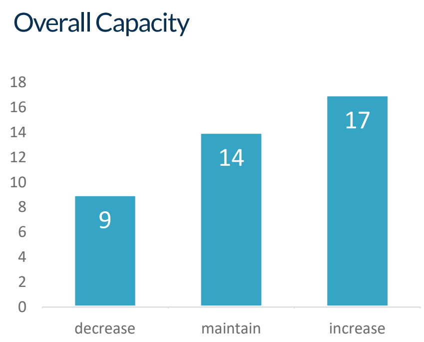


Figure 9

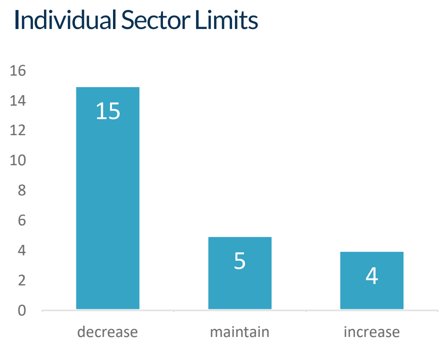


Figure 10

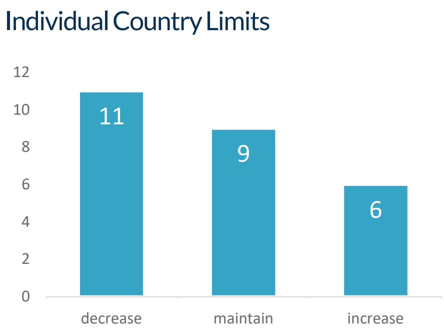
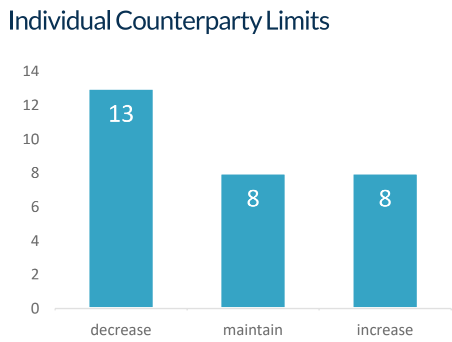


Figure 11



clients. However, increased demand is not necessarily leading to higher absolute volumes of business, since some applications do not meet criteria and large amounts are for small ticket transactions (see Figures 12-14).

When asked which measures have seen greatest utilisation, Members responded in a variety of ways, which can broadly be grouped as:

- relating to a specific product line or facility
- relating to payment deferral, extension or restructuring
- relating to 'passive measures' in support of policyholders including: changes to percentage cover offered, flexible administrative deadlines and documentation requirements, fee waivers and fast tracking.

While there may have been differing interpretations of the question, this gives some general insight into those measures which have been most apparently successful in the eyes of Members (see Figure 15).

Regarding new products or COVID-19 response facilities, specifically, Members who reported on indicated volumes of utilisation indicated some $43 billion in policies issued, limits agreed or offers approved, since introduction. Absolute volumes vary considerably depending on the size of the ECA and their benchmark levels of business.

Claims due to COVID-19 have not made a significant impact so far – these are likely to materialise through the first half of 2021 and beyond

A small number, 4% (three institutions), do not expect to see a notable increase in claims paid due to COVID-19 at all. The remainder (96%) have either already seen some degree of increase (70%) or expect to see one (26%) (see Figure 16).

The limited claims activity in the first half of the year[5] is in part a feature of the natural time lag in the claims cycle from default to indemnification, but it is not unreasonable to conclude that the various support measures introduced by ECAs, and governments more widely, have also played a role in preventing an early avalanche of claims.

Members do note an upward trend of notifications of potential claims, overdue debts and pre-claims situations, especially within short term business and primarily from sectors worst affected by lockdowns (e.g. service, tourism and suppliers to these).

Overall, the consensus is that while claims are coming, these will only really become visible in early 2021 as the cycle takes time to play out – particularly while support measures remain in place to defer this. In the meantime, the current flow of protracted defaults will likely reach a peak around the end of 2020.

Figure 12

77% of Berne Union Members report at least some increase in demand for cover

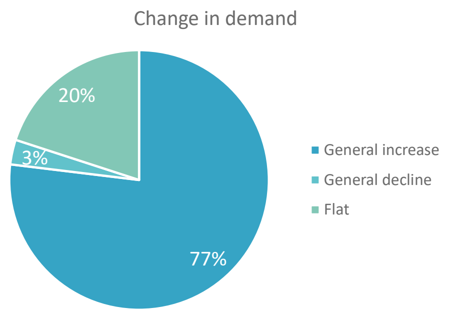


Figure 13

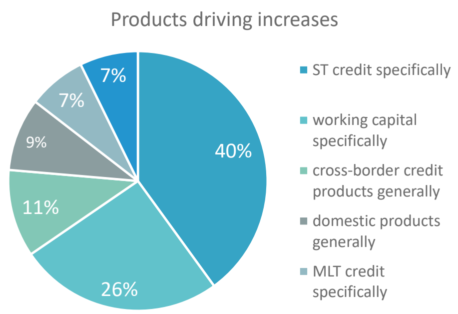
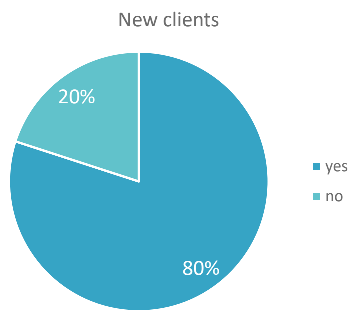


Figure 14



Only the most vulnerable industries have seen broad debt restructuring

A sizable minority of responding Members (15/69) report conducting some degree of relatively broad (industry-wide) restructuring. This includes debt holidays for shipping, aerospace, tourism and offshore oil and gas sectors (see Figure 17).

Many are participating in the Paris Club Debt Service Suspension Initiative (DSSI) and some have received applications from sovereign debtors in relation to this.

Geographically, Members indicate clusters of rescheduling across Africa (including Angola, Nigeria, Uganda, Zambia), Latin America (Argentina) and the Middle East (Lebanon, UAE).

The majority of Members are still handling rescheduling requests on a case by case basis, with the overall message that they are supportive of this process and indication that all relevant applications are being approved.

It is too early to assess the final impact of COVID-19 on credit insurance claims, not least because it is still too early to know how quickly the pandemic itself will come under control

Although claims are low at present, credit extensions and structuring are high, and the industry does expect to see a spike in losses due to COVID-19. Insurers are increasing their claims provisioning accordingly.

Some Members note that their current risk assessment places the expected impact of COVID-19 lower than initial expectations, when the pandemic began. Others project a more cautious outlook given the continuing uncertainty.

The top two risks concerning Members at present are already a reality (see Figure 18):

1. increased corporate insolvencies
2. wide economic recession

The only question is how much and how deep?

Finally, it is worth noting that although most companies currently facing difficulties are likely to reference the impact of COVID-19, this is not always the determining factor. Some sectors were struggling even before the crisis – e.g. oil and gas, airlines – and the more precarious economic environment will continue to expose and pressure these underlying weaknesses regardless of the course of the pandemic.

Figure 15

At least USD 43 bn in policies / limits issued and offers approved

Which Measures have seen greatest utilisation?

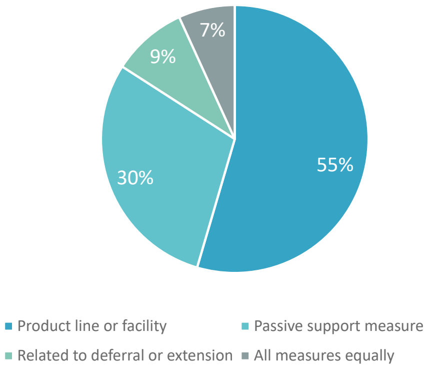
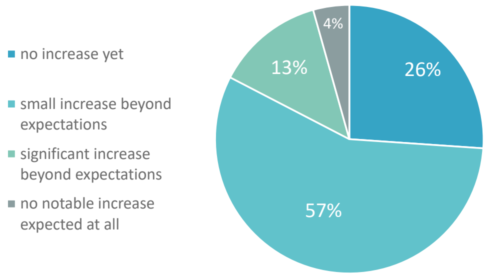


Figure 16

COVID Claims Experience

Relative to usual expectations



More than half of the support measures have a duration of 12 months or less

We asked Members to give an indication of the approximate general timeframe for expiration of temporary support measures introduced.

Responding in September, 42% of Members indicated that these are set to expire by the end of 2020, and another 18% that measures will last until around mid-2021. Only 10% reported temporary measures with a duration longer than one year (see Figure 19).

The extension of the EU's Temporary Framework for State Aid for an additional six months, to June 2021[6] will likely change these timelines, and we will likely see further extensions, not only for measures in relation to 'marketable risks'. Nonetheless, managing the transition away from special support measures will be an important policy decision for ECAs and governments, especially while high uncertainty remains.

How might the industry change in the long run?

The economic and political shifts induced by the COVID-19 pandemic will certainly have far-reaching consequences for our industry. Asked how they believe the industry may change in future, Members focused on a combination of pre-existing trends, extrapolated, combined with developments more specific to COVID-19.

We are likely to see a structural reduction in global trade for some time, as both industry and government adjust their commercial, economic and risk outlook. This may mean we continue to see an increase in domestic activity among Berne Union Members.

There will be a hardening of the private insurance market and, some Members feel, an overall reduction in risk appetite from the private sector. This would result in reduced and more expensive reinsurance capacity and potentially a larger role for ECAs relative to private insurers, but also vis-à-vis banks as they (ECAs) are required to become more proactive as originators.

Other Members offer a different interpretation, whereby a general tightening of the market could drive further public and private cooperation, and an increase in risk sharing as demand consolidates towards a smaller number of larger clients' high-value projects.

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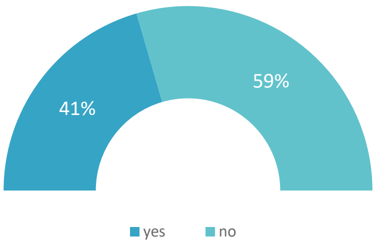
Figure 17

Notable rescheduling activity due to COVID

% of members indicating broad restructuring of certain sectors



- Shipping
- Aerospace
- Tourism
- Oil & Gas

- DSSI countries
- Africa
- LatAm
- Middle East

Figure 18

Macro Risks

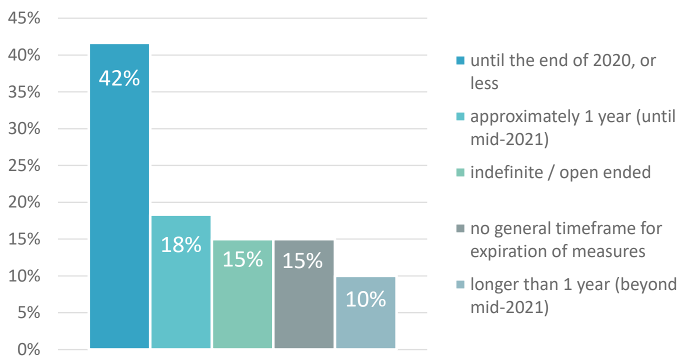
Of most concern for the future

Rank	Concern	Rank Dist
1	Increased corporate insolvencies	
2	Wide economic recession	
3	Increased political / country risk	
4	Reduced investment activities	
5	Supply chain disruption	

Figure 19

Expiration of temporary support measures

As reported in September 2020



Risk underwriting and pricing is likely to become more nuanced following the experience of the crisis and the industry may adopt new models. A prolonged recession could also increase country risk in a number of regions.

Operational changes necessitated by lockdowns are likely to remain, and the digitalisation of both internal processes and client interaction will become standard. Fully digital contracts will quickly usher in new precedents in legal enforcement and recovery disciplines.

From a wider perspective, the crisis could potentially provide momentum and incentive for governments and private companies to put sustainability at the top of their agenda.

Conclusion

The COVID-19 pandemic has placed a spotlight on our industry, and with that comes an important opportunity to demonstrate not only resilience, but also value.

The response of Berne Union Members has so far proven to be highly effective in their objective to support clients and maintain capacity for trade finance.

This success highlights the unique value of our industry in its role as a countercyclical, demand-driven support instrument and also the effectiveness of a long-term perspective and public/private symbiosis in providing lasting stability. ■

Notes

1 The most recent survey closed for responses on 15 September. Quoted results are based on the responses of 69 Member organisations, 59 public (ECA/multilateral) and 10 private insurers. Note that percentage responses relating to COVID-19 support measures are calculated within the public cohort only.

2 In 2020 H1, ECAs' portfolio of outward reinsured MLT commitments rose to $106 billion. Some $27 billon of this is reinsured by other ECAs, leaving $80 billion, of which a significant portion is reinsured by the private CPRI (re)insurance market

3 https://ec.europa.eu/competition/state_aid/what_is_new/sa_covid19_temporary-framework.pdf

4 Berne Union Members' reported new commitments for domestic products in support of exporters increased from $24 billion in 2019 H1 to $36 billion in 2020 H1.

5 Confirmed by Berne Union data for 2020 H1 which shows no year on year increase in claims paid: https://bublob.blob.core.windows.net/assets/documents/events/Media/BU%20Docs/Press%20Releases/092020%20Press%20Release.pdf

6 https://ec.europa.eu/commission/presscorner/detail/en/ip_20_1872

Credit insurance guarantee arrangements during the pandemic

By Robert Nijhout, Executive Director, ICISA

Insurance, as a product and a service, is intended specifically to protect individuals, businesses, property, and investments (among other things) against loss or damage. This is never truer than during crises when insurance is often the first point in helping people and economies to recover and rebuild. While the circumstances of the pandemic are both novel and unprecedented, large-scale events with multiple impacts are certainly not new to the sector.

For private trade credit insurers (as with other insurers), managing business through the peaks and troughs of economic cycles or significant events is something with which they are familiar and for which they are prepared. Through Solvency II in the EU and similar advanced, risk-based regimes elsewhere around the world, the private trade credit insurance market is well-regulated, robust and resilient.

Private players must carefully balance the demands of the market for increased protection during times of crisis with the need to manage their business prudently in the face of more pronounced risk. For existing policyholders, insurers of all types have a duty of care and the nature of trade credit insurance means that ICISA members are engaging closely with clients throughout this time to monitor events and respond where necessary and appropriate.

We have also seen the significant value of trade credit insurance during the pandemic – both from private markets and from ECAs – in keeping trade flowing within and between economies at a time of significant strain on cash flow and liquidity for commercial traders. Indeed, it was the risk that these services may become more restricted in response to increased risk that triggered governments in a number of countries – particularly within the EU – to introduce schemes to ensure continued access to private trade credit insurance.


Robert Nijhout

Private insurers acting prudently in response to a sudden increased risk of insolvency or payment delays in the market, and in line with regulatory requirements to appropriately manage their risks, would normally be expected to reduce the amount of cover available. Governments in a number of markets have sought to provide a guarantee to private trade credit insurers, improving the risk outlook and thus enabling them to maintain these exposures.

It is important to emphasise that schemes have not been introduced due to concerns about the financial stability of the private market. Indeed, the schemes do not benefit insurers, per se, nor are they required to address some form of disfunction in the market. The schemes focus on insured risks and are set up and run for the benefit of commercial businesses that need trade credit insurance for their continued functioning during difficult times. While certainly welcomed by private trade credit insurers, there are also significant challenges and administrative burdens attached to operating within these schemes. This presents a challenge of both cost and resource management for participating insurers.

The guarantee schemes that have been introduced vary significantly in scale and applicability from country to country, but most have tended to be structured as a reinsurance arrangement with the state accepting a certain percentage of the risk insured by private players in return for a certain percentage of premium. This structure is different to arrangements that were seen during the 2008-09 financial crisis, which tended to function either as 'top-up' cover, or as cover from an alternative insurer. Instead, current arrangements provide a backstop to existing cover, which also reduces the need for policies to be withdrawn and then reapplied, which can lead to significant disruption to policyholders.

While schemes of different varieties have been set up in a number of important markets – such as Germany, France, the UK, Canada, Netherlands and Belgium – many more have not introduced specific measures relating to the availability of trade credit insurance. However, most countries have brought in wider measures aimed at helping key parts of their economies weather the difficult months of lockdown and resulting disruption that it has brought to a number of sectors. Most of these measures aim at preventing insolvencies or otherwise limiting the stress on companies that under normal circumstances (or even normal crises) would not go bust, such as through low interest loans, equity boosts or payment holidays. Indeed some countries have amended insolvency legislation to delay declarations, while others have simply seen legal processes slow due to lower capacity in courts related to pandemic restrictions.

For that reason, when evaluating the trade credit insurance schemes where they are in place, it is important to consider the interaction of those other measures, which have reduced the occurrence of insolvencies – one of the key risks against which trade credit insurers (and therefore the credit insurance guarantee schemes) cover – on the schemes themselves. Given the combination of effects, it is perhaps no surprise that the volume of claims seen within the credit insurance schemes is lower than would otherwise have been expected. It will also be important to monitor the impact of the winding down of certain measures in the coming months and whether this leads to increased insolvencies or other scenarios in which credit insurance claims increase.

State credit insurance guarantees are mostly set to expire at the end of 2020, although the European Commission recently extended the applicability of the temporary framework under which they and other measures were introduced by EU member states until later in 2021[1]. Given the uncertainty about how trade credit insurance claims may develop following the removal of some of the additional protections mentioned above, discussions between governments and the private trade credit insurance sector in those markets where guarantees exist are expected. In the European context, once agreement on an extension is reached, it will be for member states to propose these to the European Commission, which will once again review arrangements under the temporary framework from the perspective of their eligibility under EU state aid rules.

The wider economic impact of the pandemic remains a significant 'known unknown' at this time, as does the question of how long tailed the disruption might be. This is particularly the case when it comes to trade credit insurance and the businesses and commerce which trade credit insurance protects. While those issues must be monitored and managed carefully, important lessons have been learned and the key role that trade credit insurance plays in keeping economies function has been made clear. Private players have been challenged by the circumstances, but markets remain open for business and insurers are working closely with policyholders, as well as key partners in governments and ECAs, to meet the particular issues that such an unprecedented scenario gives rise to. ■

Note

1 https://ec.europa.eu/commission/presscorner/detail/en/ip_20_1872

It is important to emphasise that schemes have not been introduced due to concerns about the financial stability of the private market. Indeed, the schemes do not benefit insurers, per se, nor are they required to address some form of disfunction in the market.

Trends in export credit insurance during times of crisis

By Jonathan Skovbro Steenberg, Economic Research Analyst, Berne Union

In early 2020, the spread of COVID-19 reached a worldwide level, and it became increasingly clear that this was, in fact, a pandemic unlike any seen for decades. One by one, countries closed down their borders and cut production, and what began as a health crisis quickly became the start of an economic one. And now as countries are once again introducing lockdowns or other measures that limit the economy, it is crucial to examine previous crises' tendencies within the export credit industry and what to expect looking forward.

The EU was the first region to experience a pan-continental epidemic, causing an economic crisis across the region. In the second quarter of 2020, the EU experienced a decrease in GDP of 11.9%, a drop roughly three times steeper than the largest fall during the Global Financial Crisis (GFC) of 2008. The GFC had dire consequences for growth, but even worse consequences for trade which fell from 81% to 71% of GDP in the EU in 2009 alone.

The GFC affected the EU particularly badly as the initial crisis caused the subsequent European Debt Crisis, which peaked in 2011-2012 but, for some EU countries, continued until as late as 2015. While examining this prolonged crisis,

Jonathan Skovbro Steenberg

it is particularly interesting to delve into the behaviour and development of trade and export credit commitments, as well as the claims of companies.

Export credit during previous crises

The EU is a highly developed economic region, indeed the market for private participants, by far, makes up the largest share of commitments of export credit. Private market participants are primarily focused on short-term commitments (repayments within a year), while commitments by public sector participants are typically medium and long-term, that are mainly used for infrastructure projects or capital equipment. This is evident in Figure 1.

Private market participants' commitments are far more sensitive to financial turmoil, as shown in the overall fall in commitments from the first half of 2008 to the first half of 2010 which are primarily due to a decrease in commitments by private market participants.

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Public sector participants' short-term commitments also experienced a significant fall from the first half of 2008 to the first half of 2009 but not in the same magnitude as private market participants.

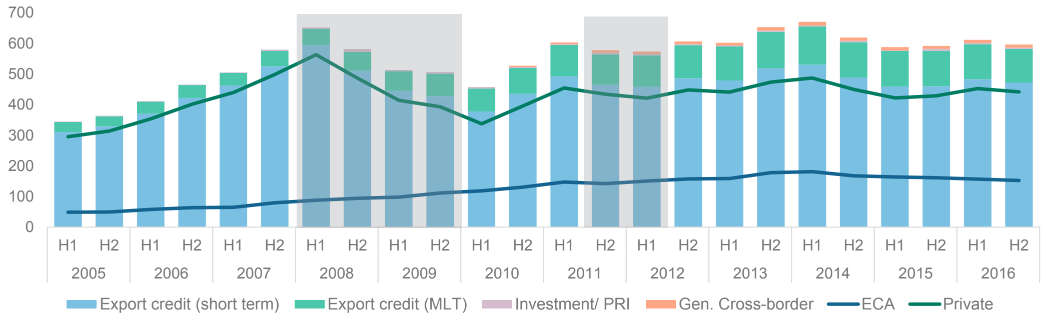
For insurance of medium to long term and PRI, commitments and claims overall appear comparatively less correlated to financial and economic turmoil, and as such, the rest of this report will focus on short-term commitments.

As can be seen in Figure 2, both private and public sector market participants experienced increasing claims as a share of commitments during the periods of financial turmoil. However, while increasing claims seemed to indicate a fall in commitments from private market participants during the GFC, the fall in commitments was not as severe during the worst years of the European Debt Crisis. A significant difference between the two periods is that the consequences of the GFC was pan-European, whereas the European Debt Crisis was far more focused on specific countries, particularly in Southern Europe.

Figure 3 displays the regional contribution to growth of private market participants' commitments. From the latter half of 2008 to the first half of 2010, commitments fell across every region in Europe, followed by a year of growth across the region. In the latter half of 2011 and first half of 2012, commitments again experienced a general decrease in the region, but in this period Southern Europe saw a relatively larger fall in commitments. Southern Europe's short-term commitments fell by 19% from early 2011 to the latter half of 2012 while they increased in the rest of the region by 3%. Indeed, Southern Europe's share of overall commitments fell from 24% to 20%.

Figure 4 shows the regional contribution to growth of public sector market participants' commitments which demonstrates a very different picture.

Figure 1 – Export credit insurance commitments in US$ billion, 2005-2016



Note: Shaded areas are periods of financial crisis. Source: Berne Union.

Figure 2 – Claims as a share of export credit insurance short-term commitments in percent, 2005-2016

Note: Shaded areas are periods of financial crisis. Source: Berne Union.

In addition to having fewer periods of decreasing commitments, short-term commitments to Southern Europe have, except for 2011, continuously contributed to the increase of commitments. From early 2008 to the latter half of 2012, short-term commitments to Southern Europe by public sector market participants increased by 54% while short-term commitments by private market participants fell by 41%.

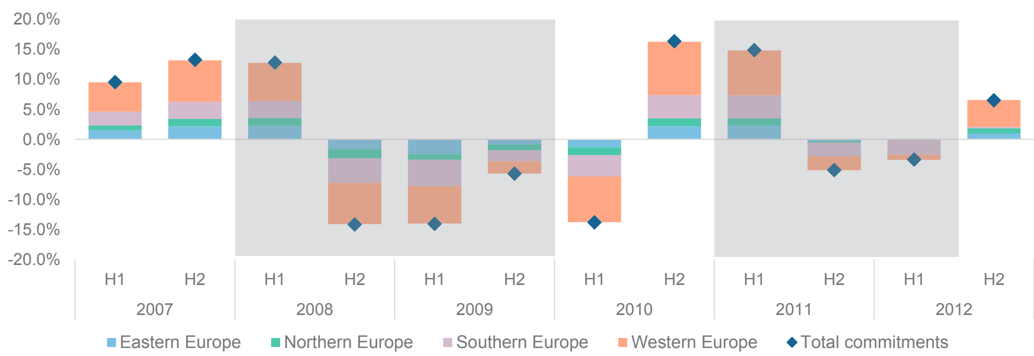
From these figures, one can conclude that the commitments of private market participants decrease in countries experiencing financial and economic turmoil. However, it seems that public participants' commitments are less correlated with this and they are actively stepping in when private market participants are reducing their presence in a market.

In times of financial and economic turmoil, claims for short-term commitment increase. Private market participants' commitments tend to decrease as claims increase. Contrastingly, public participants seem more unaffected by the turmoil and may, in fact, increase their share due to a lower private presence, in what appears to be a reverse crowding-out effect. This tendency is almost certainly caused by governments wanting to stimulate growth in times of turmoil, while private market participants are responding to market conditions.

COVID-19 and the consequences

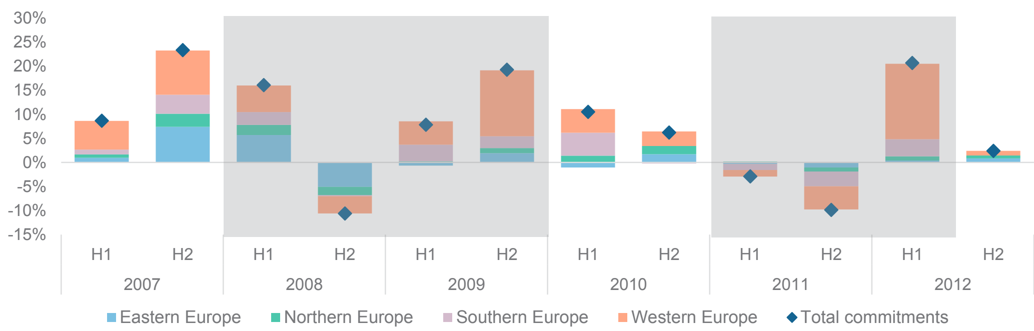
In mid-September, Berne Union released a preliminary report on the business activities of its members for the first half of 2020 and found that new commitments had

Figure 3 – Annual contribution to growth in private market participants' short-term commitments by region, 2007-12



Note: Shaded areas are periods of financial crisis. Source: Berne Union.

Figure 4 – Annual contribution to growth in public sector market participants' short-term commitments by region, 2007-12



Note: Shaded areas are periods of financial crisis. Source: Berne Union

contracted, while the expected increase in claims had not been realised. In fact, the data showed that claims had fallen compared to the first half of 2019.

Focusing again on developments in Europe, claims as a share of short-term commitments fell in the first half of 2020 compared with the preceding period. The September report from Berne Union emphasised that the main reason that claims are not increasing is because of fiscal support from governments and quick responses from lenders and insurers in restructuring deals. The figures below show the disconnect between the current development in claims compared to previous crises.

As fiscal support is slowly phased out by governments and the number of corporate insolvencies start increasing, claims are expected to start rising, as seen in previous crises.

As fiscal support is slowly phased out by governments and the number of corporate insolvencies start increasing, claims are expected to start rising, as seen in previous crises. Most Berne Union members expect to see an increase in early 2021 as they are already reporting a noticeable increase in payment deferrals and pre-claim situations, as reported by the Berne Union in October.

Generally, seeing a slower response of increasing claims is not dissimilar to previous crises where greater surges happened later, in period T+1. The GFC, in particular, saw an insignificant increase in the initial period of the crisis, but grew to almost three times the pre-crisis level after a year (period T+2).

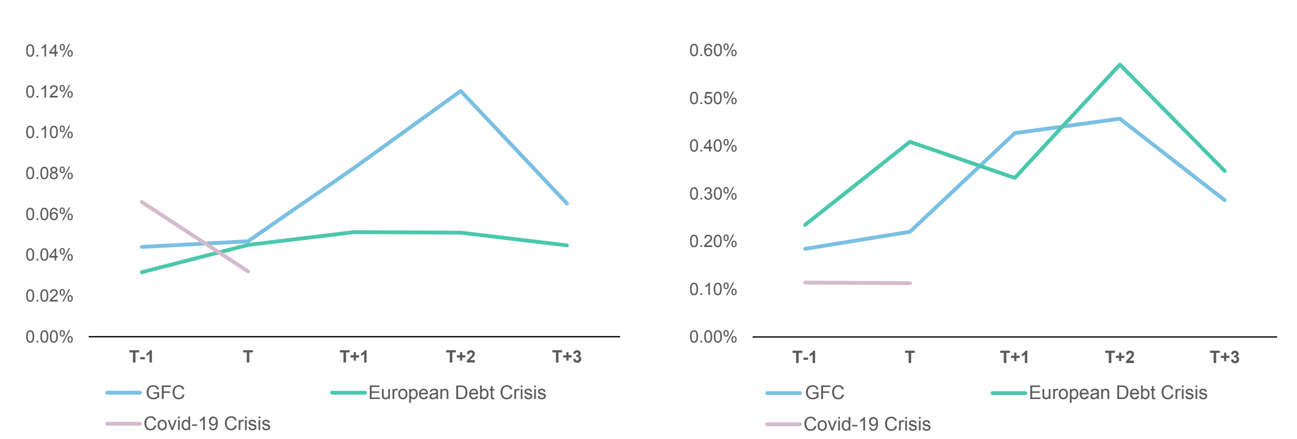
The difference in the scale of rising claims between the GFC and the European Debt Crisis is partly due to the different extents of the crises, but also to the changing geographical composition of the private market participants' short-term exposure. As previously mentioned, the private market participants' short-term commitments had already slowly been decreasing in Southern Europe compared to the rest of Europe, a trend that has been continuing.

The following figures show the change in short-term commitments from the previous period on a biannual basis from the initial period of a crisis and the following three periods.

In the first half of 2020, private market participants' short-term commitments experienced an overall fall of 8% compared to the previous period, representing a greater fall than experienced during the European Debt Crisis but smaller than during the initial periods of the GFC (see Figure 7).

Looking at the subsequent periods, the dynamics of the previous crises diverge. During the GFC private market participants' short-term commitments continued to fall

Figure 5 (Private) and 6 (Public) – Claims as a share of short-term commitments in per cent in crises



Note: T is 2008Q2 for GFC, 2011Q2 for European Debt Crisis and 2020Q1 for COVID-19 Crisis.

for the following three periods, while the development was slightly more favourable during the European Debt Crisis where the fall subdued in the following period and even increased in period T+2. Predicting the development of private market participants' short-term commitments will be dependent on whether the crisis gets the same pan-European grip on economies that was seen during the GFC. There are arguments for and against this. The pandemic is global by nature and hence also pan-European, however the effects of the disease are affecting countries to differing degrees, and some economies have been shown to be more vulnerable than others. Several southern European countries, those whose economies rely more on agriculture, production, and tourism, have been hit harder by the virus, on top of their economies being more susceptible to it.

Public sector participants' short-term commitments increased slightly in the first half of 2020, unlike the previously mentioned crises. This is predominantly due to the quick response by national governments and the European Commission to bridge market gaps, so European ECAs have been able to extend cover of short-term risk, as highlighted in the publication by Berne Union, Export Credit Industry response to COVID-19 Pandemic[1]. In previous crises, governments have been slower or more hesitant to respond, which is why the increase in public sector participants' short-term commitments came in later periods. This is especially so during the GFC where G20 countries agreed to ensure the availability of trade finance for $250 billion in 2009-2010 at the G20 Summit in London. The future development of public sector participants' short-term commitments will depend on the financial strength of countries and the will of governments to support trade in future while economies recover from the pandemic. Initial stimulus packages and commitments from national governments and the EU is an indication that there will be a larger focus on expansive fiscal support this time compared to the austerity measures that defined the period following the GFC. ■

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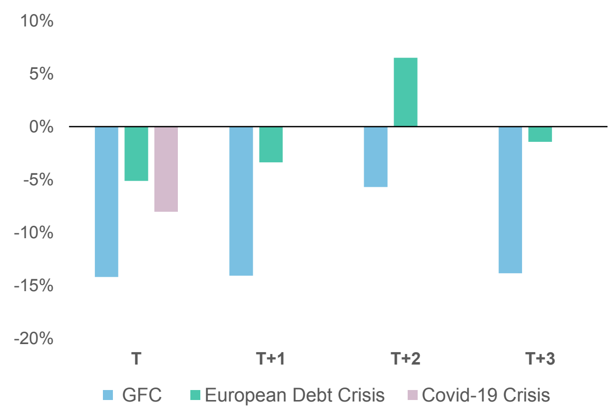
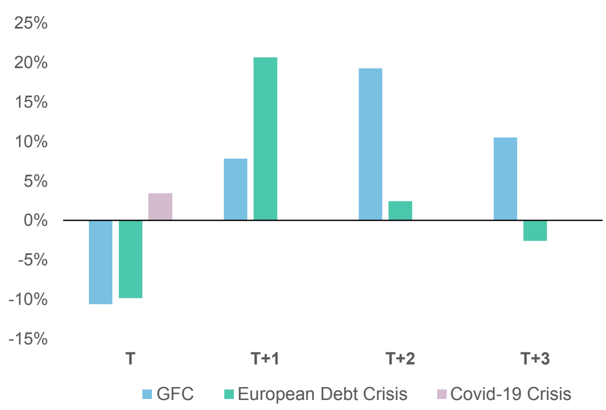
Note

1 https://www.berneunion.org/Articles/Details/506/Robust-response-to-the-COVID-19-pandemic-from-the-export-credit-insurance-industr

Figure 7 (Private) and 8 (Public) – Biannual change from previous period in short-term commitments in crises





Note: T is 2008Q2/Q1 for GFC, 2011Q2/Q1 for European Debt Crisis and 2020Q1/2019Q4 for COVID-19 Crisis.

Crisis and recovery mode: How is the CPRI market responding to COVID-19?

While the final price tag of COVID-19 claims is yet to be determined, the impact on capacity, appetite, pricing and terms in the structured trade credit and political risk insurance (CPRI) market is already being felt. Sian Aspinall, Managing Director at BPL Global, takes stock of the effects on the insurance class, and assesses the risks and opportunities in the longer term

The COVID-19 pandemic continues to cast a thick cloud over the global economy and we are still yet to see the final shape of the insurance industry as it emerges from the crisis. Although widely anticipated, we've not yet seen the expected deluge of claims in the CPRI market. In fact, whether these claims will arrive in the form of deluge – or if it will be more of a wave or a ripple – is not yet clear either. What we do know, however, is that the pandemic's effects on global trade and liquidity are changing CPRI dynamics.

Importantly, it is not just the effects of COVID-19 that have blown winds of change in our market of late. The onset of the pandemic coinciding with the hardening of the market as it entered a new phase of the insurance cycle, alongside low commodity prices, have worked to further shift CPRI supply and demand trends.

So, in the short term, how have the events of the past year caused insurers to redefine their appetite? And looking further into the future, will insurers fundamentally change their operations as a result? And what will the ramifications be on the long-term growth prospects for CPRI?


Sian Aspinall

Despite encountering serious disruptions approximately every decade – the 2008 global financial crisis, for instance – CPRI has grown consistently. We've identified several trends and potential opportunities brought about specifically by this pandemic which we expect will dictate the continued evolution of the market.

Current supply and demand volatility

Generally speaking, the market saw reduced demand for CPRI in the first three months of the pandemic, with a 20% drop in BPL enquiry levels compared to the same period in 2019. Since then, however, demand has recovered, with BPL's enquiry flow at a similar level to that observed in 2019. However, it is clear the composition

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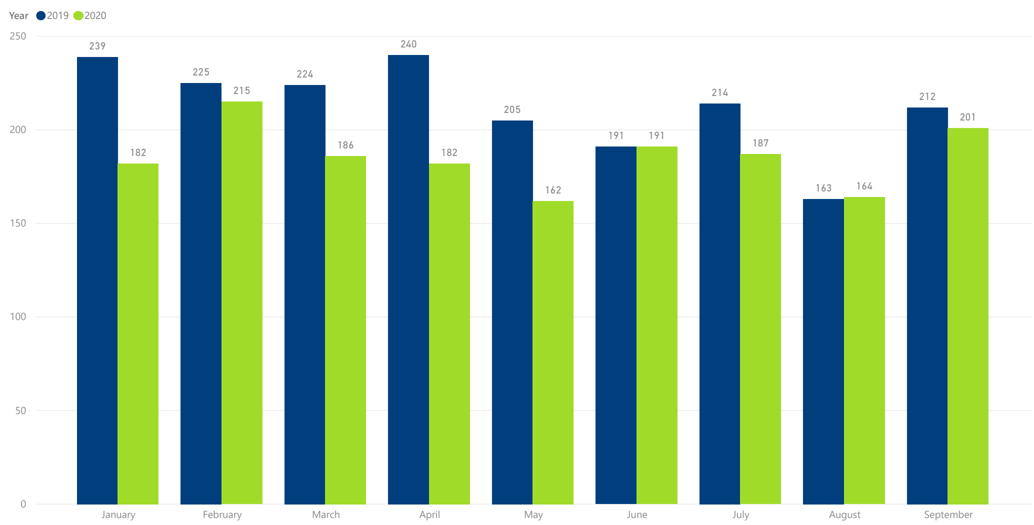
split has changed. A tighter secondary loan market and more conservative credit committees are likely to be behind the rebound in bank enquiries, which have, in fact, increased by 20% in each of the last three months. Conversely, demand from traders and exporters has reduced, reflecting overall contractions in global trade volumes resulting from the current climate. On the supply side, we expect the Covid-19 crisis will have a short-term but moderate impact on CPRI capacity. This is particularly the case for non-traditional risks and transactions with longer tenors. Additionally, resultant claim patterns and volumes, as yet undetermined, will no doubt result in further refinement.

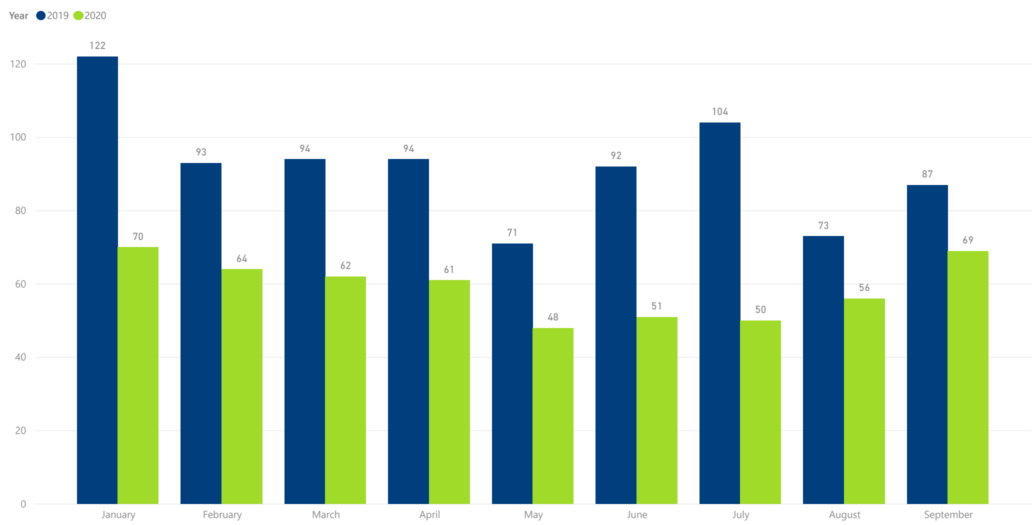
To analyse the true picture, though, it is necessary to dig deeper. We have experienced a notable divergence between insurer appetite and client demand at the transaction level. For the 12 months through to February 2020, BPL Global obtained non-binding indications (NBI) on 69% of all enquiries submitted to the market. This figure declined to 50% or less in each month from March onwards with only moderate improvements seen recently.

CPRI is unlikely to benefit from the capital inflows that investors are currently pouring into some other insurance classes. Though CPRI premiums on average are approximately 20% higher than pre- crisis levels, these rate hikes are not as steep as experienced elsewhere in the insurance

Enquiries in 2019 vs 2020



Enquiries in 2019 vs 2020 for Commodity Traders, Exporters and Investors



sector. What's more, unlike insurers in other classes, those operating in our market are, to a certain extent, constrained by margins in the banking market – which are mostly beyond their control.

Impact on insurer operations

The recent economic volatility has prompted some CPRI insurers to change tack. Although current signs are positive, with Convex and HDI Specialty confidently entering the market, several underwriters have scaled back their CPRI offerings and another has pulled out entirely.

Over the next 24 months, the number of insurers may well decline further due to some exiting the class. That may also occur due to mergers and acquisitions (M&A). More often than not, M&As result in strong, well-resourced teams with the deep expertise required to take the market into new and profitable areas. In a market such as CPRI, this depth of expertise is as important as the number of active players as it drives innovation.

And while in the first few months of the crisis we saw insurers naturally pushing for higher pricing and better terms, this may not be every client's market experience. During disruptions, CPRI insurers have tended to be more inclined to stand by existing clients with whom they have built long-term, trusted relationships. Such clients stand in a good position to quickly mobilise insurance capacity and continue to attract more competitive premium rates than others.

Could COVID-19 recovery plans represent a silver lining?

Certainly, this is not the first crisis that the CPRI market has had to contend with and historically it has emerged post crisis with a stronger, more sophisticated offering. Indeed, the industry is not one to 'waste a crisis' and just as it has done in the past, it is already showing signs of adapting in order to open opportunities across a more diverse pool of asset classes and transactions.

There is opportunity for the private insurance sector to step up, for instance, to insure direct lending to banks domiciled in emerging economies – and particularly those with narrow domestic financial markets. Such activity will complement the recently increased funding support issued by development finance institutions and multilateral lenders, helping to alleviate bank liquidity issues and sustain their ability to finance local exporters and projects.

In fact, following crises, the CPRI market has historically allocated significant capacity to cover bank-to-bank loans to help facilitate both a regional and global recovery. We expect the market to do so again, attracted by the relatively wide margins on bank obligors with which insurers are already familiar.

We can also pinpoint other opportunities arising from the efforts to revive economies from the pandemic disruption. For example, government stimulus packages in both developed and emerging countries have brought about a crop of quality public-private partnership projects. In addition to such new developments, there is likely to be a backlog of projects that were paused given the pandemic, supply chain issues and volatile commodity prices that are primed for revival when markets stabilise.

CPRI insurers have sought to invest the necessary time and resources into understanding Project Finance for some years now, and they know that default rates in the asset class are typically low, with structuring helping to mitigate identifiable risks. Therefore, the market can offer a meaningful amount of capacity and accommodate the long tenors required for project finance with US and Canadian infrastructure projects including toll roads, geothermal power and Liquified Natural Gas facilities currently garnering particular support from insurers.

Another niche within the project finance

The recent economic volatility has prompted some CPRI insurers to change tack. Although current signs are positive, with Convex and HDI Specialty confidently entering the market, several underwriters have scaled back their CPRI offerings and another has pulled out entirely.

arena shows promise: sustainable finance. As we understand it, capacity may be opening up in the CPRI market for renewable energy projects, given the enormous levels of climate-aligned investment needed across the globe for governments to achieve their Nationally Determined Contributions under the Paris Agreement.

Aside from this very apparent need, there are several other reasons as to why sustainable finance may take off in the post COVID-19 CPRI market. According to Moody's, green project finance bank loans tend to have an even lower default risk rate than their vanilla counterparts – attracting insurers looking to recalibrate their loss ratios in the face of COVID-19 claims.

Another driver is the Environmental, Social, and Governance (ESG) mandates of major banks. European banks – which form a key client base of the CPRI market – are concertedly building their portfolios of green projects to meet environmental objectives and incoming regulations. There are instances of some even applying a Green Weighting Factor to RWA analysis on transactions. Of course, where these banks go, the insurers follow – and we expect the latter will provide significant support for such initiatives.

It's not just banks which have ESG mandates to fulfil, after all, insurers are also under their own obligations to cover quality risks with a sustainability feature. Incorporating ESG ratings into asset-side investment decisions is not new among CPRI providers, but how exactly they do so in their underwriting has not been explicit. Recently, however, several insurers have publicly disclosed their approaches for factoring in ESG ratings when writing business and including sustainability-related indicators within their country ratings.

For the CPRI market, sustainable finance also represents an avenue for diversification from its traditional mainstay of Oil & Gas in the longer term. The CPRI market is heavily exposed to these markets via both banks and major traders, which are also key CPRI clients.

Tapping areas of promise

Other areas remain robust and attractive for CPRI providers as lenders focus on enhancing risk mitigation strategies, such as private equity. As mentioned, lender credit committees are currently taking a more conservative stance which is incentivising

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CPRI insurers to expand their lending relationships, such as through 'capital call facilities'. When a fund makes an investment, such loans provide short-term financing on a revolving basis until the receipt of investors' capital contributions towards that investment. The loans are then repaid with the investors' capital contributions.

To avoid credit concentration issues, particularly given the recent growth in fund sizes, major lenders have turned to credit insurers to share this risk. For credit insurers, the appeal lies in the strong security and short risk duration of capital call facilities, and with rising commitment fee pricing and funding rates, insurance premium levels are acceptable for both insurers and lenders. Credit insurers are also favouring secondary fund loans due to their low loan-to-value ratio.

Insurer appetite also seems particularly healthy for repos and hedges (including FX, interest rate, commodity price). Derivatives represent an opportunity for some insurers to underwrite structures that offer an improved recovery rate and strong pricing on strong obligors which they would not usually cover. We expect this niche to grow in response to demand from obligors that want enhanced risk management and those banks that can secure significant RWA savings through insuring some of their mark-to-market exposure.

This year is proving to be wrought with challenges for every industry, and CPRI will continue to feel the reverberations on all fronts. But with appetite and demand trends evolving and broadening, perhaps we could see more opportunities for growth and recovery in the near future. ■

COVID-19 impact on the private credit insurance market

By Fabrizio Mazza, Managing Director, Global Public Agency Leader, Credit Specialties, Marsh JLT Specialty and Abbey Sturrock, Senior Vice President, Deputy Global Public Agency Leader, Credit Specialties, Marsh JLT Specialty

This has been an extraordinary year. The COVID-19 pandemic has led to the largest global economic contraction since the Second World War, which has prompted governments and central banks to engage in an unprecedented and often loosely coordinated monetary and fiscal response, leading to a significant expansion of the public balance sheet.

Furthermore, on the back of the experience matured during the global financial crisis, the importance of short term trade credit insurance for the economy was recognised. It allowed government top-up and reinsurance schemes for private trade credit insurers to be created quickly as a way to minimise the disruption to the credit insurance supply chain.

At the same time, public agencies – which we define as multilateral development banks (MDBs), developmental financial institutions (DFIs), and export credit agencies (ECAs) – have responded to the crisis both by mobilising their own resources, and channelling government funds into their domestic economies to provide counter-cyclical support.

Yet, the response has not only been fiscal. Governments of the G20[1], through the Debt Service Suspension Initiative (DSSI), have acted to freeze principal and interest payments, in respect of official bilateral lending, to a number of emerging market government borrowers that formally requested the support. Meanwhile, some regulators have postponed the implementation of certain Basel III standards, in an effort to support ongoing lending during the crisis.

Fabrizio Mazza

Abbey Sturrock

These measures represent significant risk moderating factors that have already delayed the full impact, and may significantly reduce future impact, of the crisis on the real economy, and with it on the private (re)insurance market.

As we slowly move from the first phase of reaction to a second phase of recovery,

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we begin to assess the pandemic's impact on the private credit insurance industry, and what we expect going forward, particularly with respect to the interface between the public and private sector, which has been one of the leading themes of recent years (public-private cooperation).

Marsh JLT Specialty expects a generalised increase in credit risk, political risk, and performance challenges to foreign investors and overseas lenders, but particularly in countries that were either very dependent on certain sectors (for example, tourism), or certain commodities (such as hydrocarbons), which have been hit hard by the COVID-19 pandemic.

We base these assumptions on credit rating data, which indicate a rapid increase in the risk of default through 2020 and 2021. We therefore expect an associated significant increase in claims for credit insurers due to loan defaults, and a linked increase in exposure to performance surety bonds being called, following a deterioration in companies' ability to perform contractual obligations.

Complex questions for private (re) insurers

These circumstances raise complex questions for private (re)insurers in managing current risk, expected losses, future risk appetite, and risk pricing. The natural tendency in such circumstances would be for (re)insurers to use more caution when considering the risks and an upward adjustment in the cost of risk, as reflected in higher premium rates. This is not a new trend. A general deterioration of the credit book in recent years, triggered by the end of the commodity super cycle, had already begun to affect the appetite of private credit (re)insurers, with pockets of the market hardening (sub-investment grade private obligors). However, the combination of these pre-existing trends and expected COVID-19 losses in 2020, has accelerated a more generalised market adjustment, affecting (re)insurers' appetite and pricing alike.

When considering COVID-19's effects on the private credit insurance market, we cannot avoid looking at the wider industry. The impact of COVID-19-related losses on the property and casualty market – which cannot be modelled and is therefore unlikely to have been priced in last year's treaty renewal season – could be significant to the reinsurance and retrocession (retro) market[2],

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particularly as they accumulate with this year's losses from the storm and wildfire seasons.

COVID-19 losses will take a long time to assess, yet at the top-end of analysts' estimates, once added to catastrophe losses, they could make 2020 the highest yearly loss for the insurance market to date. So far, however, the data gathered by Guy Carpenter paints a less severe scenario with H1 2020 total losses incurred amounting to $43 billion, including $25 billion of COVID-19 related losses[3]. Yet with further claims accumulating in the second half of the year, a total industry loss of around $100 billion now seems realistic. This would include incurred COVID-19 losses together with catastrophe losses in the year to date, and average catastrophe losses, based upon historical experience, that may reasonably occur through the remainder of the year. This figure, while not making 2020 a record-breaking year, will still make it the fourth year in history when total losses reach $100 billion.

If capital were to leave the reinsurance and retro markets as a consequence of the 2020 losses (following very high 2017 losses, and not insignificant periods in 2018 and 2019), the impact on the direct insurance market would be more severe and more sustained. The alternative capital market[4], which now represents approximately 20% of the total retro capital base, could be particularly volatile as it is more mobile than traditional reinsurance capital. Changes in the broader (re)insurance and retro insurance markets may therefore trigger top-down pressure for private credit insurers in 2021 and beyond, to reconsider coverage and pricing in addition to the changing market conditions caused by the increase in credit risk due to the pandemic crisis.

Drilling down to expected credit insurance losses arising from COVID-19, analysts have published a considerable range of estimates, between $8 billion and $60 billion over a two-year horizon[5]. While the risk environment is constantly changing – influenced by the continuing impact of the risk-moderating factors listed earlier, among other things, which if withdrawn may result in significant higher claims to the insurance market – the current range of claims estimates is thought to be comfortably within the capital capability of the private (re)insurance market.

This is because most large international insurers and reinsurers are capitalised in accordance with the Solvency II regulation. This has considerably strengthened underwriter security and capital structures since the global financial crisis. Encouragingly, while there are expectations of steady growth throughout 2021, actual global claims to private credit insurers arising from the lockdown have been relatively low. Marsh JLT Specialty, drawing comparisons with data gathered during the global financial crisis, estimates private credit insurance losses (across trade credit, political risk, structured credit, and surety) for the two-year horizon to be between $20 billion and $45 billion. This level of loss would clearly be very significant, but is a moderate catastrophe exposure in wider insurance market terms[6]. Moreover, new business opportunities are growing (such as in the private equity space), and premium rates have risen in light of changes in the risk environment. This should act to reduce impact.

COVID-19 not major threat to private credit insurance

As such, we believe that COVID-19 is unlikely to represent a major threat to the private credit insurance market. Yet, it will undoubtedly have some lasting effects on appetite and the cost of risk. This will affect all clients, but particularly public agencies, which have increasingly contributed to the growth of public-private partnerships in recent years.

We can in fact observe that, while the deteriorating risk environment is pushing many private credit insurers to strategically pursue a ‘flight to quality’ via enhanced partnership with public agencies, given the perceived benefits of working with such institutions in terms of lower loss ratios and higher potential recoveries, certain new limitations are becoming apparent.

The most significant is the emergence of a pricing gap. As risk premiums increase in the commercial market, we do not see a corresponding improvement in the premium rates offered by public agencies, particularly ECAs. In fact, constrained by OECD Consensus Arrangement guidelines (applicable to ‘officially supported’ ECAs), and bound by their mandate to support their countries’ exporters in international tenders against aggressive bidders – often from ECAs outside the Arrangement – ECAs are increasingly pushed to offer borrowers the most aggressive financing package possible (especially when it comes to sovereign borrowers).

Yet, these same aggressive conditions cause some ECAs to find it more and more challenging to attract buyers for the risks they intend to share with the private market. This is compounded by the fact that the main growth for ECAs in recent years has been in regions with a comparatively higher risk profile, such as sub-Saharan Africa, as a result of the significant opportunities arising in government-guaranteed infrastructure financing. However, the reduced quality of borrowers means that certain ECAs only have a limited internal capacity allocated for these projects and credit quality internally.

As such, we believe that COVID-19 is unlikely to represent a major threat to the private credit insurance market. Yet, it will undoubtedly have some lasting effects on appetite and the cost of risk. This will affect all clients, but particularly public agencies, which have increasingly contributed to the growth of public-private partnerships in recent years.

This results in an increased need for private market reinsurance as a way to bridge the gap, mitigate excessive concentrations, and ultimately avoid breaching internal risk guidelines.

However, the private (re)insurance market has also been insuring the same sub-Saharan Africa risks for many years; supporting a large number of exporters, traders, and banks financing trade and investment in the continent. Therefore, the remaining pool of capacity in this region available for ECA reinsurance – particularly at the OECD Consensus pricing levels – is becoming shallow and constrained. Given that Africa has seen a further deterioration of the credit metrics for most borrowers, we can infer that ECA demand for increased reinsurance needs will only continue, likely leading to a widening gap between this level of demand and what the private reinsurance market is able to absorb at current pricing conditions.

It is not only ECAs who are facing mounting challenges. Other public agencies such as MDBs and DFIs, while less or unconstrained by rigid OECD Consensus Arrangement guidelines, have also found pricing and capacity limitations when seeking to mobilise private capital. We see in this case a growing gulf between MDBs' requirements, with a mandate to lend countercyclically to challenging borrowers at highly competitive rates, and those of private market insurers that, while still keen to support, often find such rates not commercially viable in the current risk environment, even behind an MDB.

That said, overall appetite for public-private partnership remains strong. However, the current situation is putting a strain on this model. The defaults that will inevitably occur in the next couple of years will also represent a litmus test, as private market insurers will observe with interest the performance of public agencies in respect of claims brought to the (re)insurance market, and eventual recoveries. The outcome could either strengthen the case for partnership, giving substance to the assumption that supporting public agencies provides a halo effect for private (re)insurers, or dampen the excitement and lead private (re)insurers to be more cautious when supporting public agencies business, and more selective of their partners going forward.

For public agencies, who have come to rely on the private market's steady support, it has become more important than ever to work alongside an experienced intermediary, who is able to understand the evolving market dynamics and can provide guidance on how best to attract (re)insurance capacity under these new conditions – structuring solutions that not only meet their internal requirements, but also private (re)insurers' commercial requirements. ■

Notes

1 The Group of Twenty, or the G20, is a forum for international economic cooperation bringing together leaders of both developed and developing countries from every continent?. For further information: https://g20.org/en/Pages/home.aspx.?

2 The retrocession (retro) market is where reinsurers purchase reinsurance.

3 Reported losses of approximately 150 publicly traded groups in the insurance industry. US mutual groups do not publish catastrophe losses estimates. Guy Carpenter is a reinsurance broker, a Marsh & McLennan company (NYSE:MMC)

4 The alternative capital market is made up of hedge funds, mutual funds, pension funds, and other institutional investors, which provide reinsurance and retro capital via a variety of instruments such as insurance linked securities (ILS).

5 References include but are not limited to: UBS Global Research 'COVID the biggest insured loss ever?' 24 April 2020 and Morgan Stanley '(Trade) Credit where Credit's Due', 5 May 2020.

6 The insurance market's average yearly catastrophe losses are in the region of $60 billion.

For public agencies, who have come to rely on the private market's steady support, it has become more important than ever to work alongside an experienced intermediary, who is able to understand the evolving market dynamics and can provide guidance on how best to attract (re)insurance capacity under these new conditions – structuring solutions that not only meet their internal requirements, but also private (re)insurers' commercial requirements.

Early lessons from managing the crisis: The need and feasibility of rethinking the public versus private model

By Jérôme Pezé, CEO and Founder, Tinubu Square

There are lessons to be learned for many in the trade industry as we reflect on recent events. In normal times, both domestic and foreign trade experience ups and downs. Therefore it is always advisable for small and medium-sized enterprises to have credit insurance to help them grow their businesses safely. For trade credit insurers who provide such support to businesses and make a strong contribution to trade, the risks that are transferred to them fluctuate as well.

The financial crisis in 2008 caused a huge disruption to the trade sector and today COVID-19 is having an even more drastic impact. We have seen a worldwide response to try and manage the crisis for the trade industry. Here we consider changes that may come from the involvement of governments and the long-ranging implications, which may include rethinking models for the future of the trade credit insurance industry.

Impact of the crisis both on trade and the trade credit insurance industry

Trade credit insurers are the providers of risk coverage that is adjusted as a normal part of credit monitoring. Generally, this is positive.


Jérôme Pezé

Yet, when there is a global economic crisis, it is inevitable that unique risks are presented to credit insurers as assessing risk becomes a fast-moving target. When a company needs credit from a supplier, there is a strain on capacity which creates a pro-cyclical effect on the company. Additionally, a company is squeezed when credit insurers withdraw their cover, which reduces the credit risk protection for the company and for its suppliers, and also squeezes the company using factoring or other financial arrangements. The more the company becomes at risk, the more fragile its economic stability becomes, all of which accelerates the initial crisis.

There is also the further impact when delays and timing issues on the part of credit insurers interrupts an economic upturn. The company is then at an even greater disadvantage. In effect, once the initial disruption in the normal credit insurer

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business model occurs, other changes occur.

Governments step in with support

All of this disruption occurred both in the global financial crisis of 2008 and in the current COVID-19 crisis. As a result of the instability, governments provided massive emergency support schemes to companies that allowed for cash facilities, subsidised employment costs and delayed tax payments.

In the spring, as a result of COVID-19, trade credit insurers were afraid they would be unable to pay huge losses to businesses. Fearing the worst, major private insurers took the urgent initiative to ask for government support. Out of their concern for the pro-cyclical effect of short-term credit insurance and to reduce a possible worsening impact of a delayed rebound from the crisis, governments answered insurers' concerns. They stepped in to cover the anticipated credit insurer losses and implemented massive reinsurance schemes, with insurers agreeing to the governments' requests for the premiums to go to them. In some cases, it was anticipated that the claims could be 10 times greater than the premiums.

It was very difficult for governments to estimate what the actual losses would be or to what extent their massive support schemes would contain company insolvencies. In most countries where such programs were implemented, the expectation was for massive – potentially never before experienced – levels of claims. In effect, trade credit insurers had transferred their losses to the government.

Effect of government support

There is no question that government support to the trade credit industry was and is very important. Government actions allowed insurers to continue to provide coverage and for businesses to stay alive.

Now that some months have passed, we are learning that the level of claims and anticipated credit insurance losses are drastically lower than expected. In other words, the insurers might not have needed the assistance, or needed as much. In turn, those government schemes turned out to be financially very profitable for governments, while largely under-utilised by businesses.

The point here is that it was difficult to assess the real impact of the COVID-19-induced economic crisis on businesses. We must also consider the effect of some governments' sizable actions which serve to benefit individuals and corporations for the long term, through tax rebates and delays, social subsidies, financial, treasury support, loans and guarantees.

Questions to consider for the future: The reach of governments

It is prudent to expect that governments and credit insurers will reflect on how recent events might reshape the future. For example, how do these events change the business model of credit insurers and will governments continue to provide assistance?

Globalisation is here to stay, and trade is becoming more and more volatile. Companies have to rethink how they control supply chains. While some countries have undergone mass digitalisation of businesses, there are those still evolving countries that have more challenging structures within which to work. Economic situations could become so uncertain that there is a need to implement a sustainable model for governments to take on a more permanent role. This is a complicated picture, yet one that presents many options.

The current global crisis and the response to it, as well as what we are learning now will necessarily mean that some governments

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will consider different options for the respective roles of the private and public sectors in short-term credit insurance and the framework in which they operate. The mission of trade credit insurance has always been essentially as a private market. Any involvement of the public sector would involve big changes.

Governments may expect that helping trade credit insurance is a new normal. Trade credit insurers may believe there is a need for governments to provide capacity when the private sector is unable to. These ideas change the existing model and may force the industry to address the parameters as to how far the public sector can go.

Governments could decide to play a role in implementing regulations that force private insurers to strengthen their solvency ratios to better support their mission on their own. This would mean credit insurers would then theoretically eliminate government support in times of crisis, because they would be better prepared to respond. Governments could set limits on cover withdrawals and credit during crisis. This raises concerns for the prevailing credit insurance business models, pricing structure, value proposition, and the compatibility of any future changes.

Reconsidering the role of ECAs?

Another possibility is to reconsider the future role of Export Credit Agencies (ECAs). Traditionally, ECAs have a limited role, yet it could be expanded. Governments might promote ECAs as having a direct role for temporary periods during times of crisis, with terms and conditions to be locally defined. Or, that role could extend beyond the case of global crises to support other scenarios, such as when trade sectors undergo a major restructuring.

If such a new role were assigned to ECAs, would they be capable to fill it? Several ECAs have gone, or are already going through, digital transformation to be more flexible, more reactive, more cost effective, and to provide a high standard of customer experience, sometimes doing better than the private sector. Yet, others are way behind.

Finally, we can raise the question of the feasibility of a hybrid solution where the public and private sectors could team up to provide a joint sustainable and efficient solution for the mutual interests of companies. Indeed, notably in markets where the private sector is well-developed, often with very few dominant players, several significant obstacles appear, such as conflicting agendas and issues relating to transparency, operating mode, and local business practices.

Promoting a discussion

Serving as an independent partner of both ECAs and private insurers around the world, I offer these views to promote a discussion between the trade industry and its constituents. It is in times of crisis, such as the one we are still enduring, that we can often learn the most valuable information to help plan for the future. ■

Governments may expect that helping trade credit insurance is a new normal. Trade credit insurers may believe there is a need for governments to provide capacity when the private sector is unable to. These ideas change the existing model and may force the industry to address the parameters as to how far the public sector can go.

ICIEC works its way through the pandemic

By Oussama Kaissi, CEO, ICIEC

The COVID-19 pandemic has caused a multitude of economic shocks. Once lockdowns became enforced by governments globally, demand for goods and services drastically decreased across various sectors. This low demand then translated into businesses reducing their productive capacity. Mass lockdown measures have also prevented many citizens from working at full efficiency, if they are able to work at all, stifling incomes and business productivity in the process. These shocks on both the supply and demand components of the economy are leading to a significant reduction in exports and overall trade flow – which in turn is reducing government revenue.

Most analysts are predicting the COVID-19 pandemic will lead to a recession deeper than the 2008-09 global financial crisis. UNCTAD estimates that world merchandise trade is set to plummet by at least 20% in 2020. Foreign direct investment (FDI) is also projected to decline sharply, with UNCTAD estimating a 40% decrease in FDI for 2020.


Oussama Kaissi

A decrease in output is also projected, with the International Monetary Fund expecting a 4.9% contraction in global GDP for 2020.

Though these numbers do imply a major rollback to the global economy, they don't signal a complete collapse. Many governments have made progress to flatten the curve of their rates of infection, reduce the pressure on health care systems, and move towards regular operations with guidelines. With economies opening back up, there is light at the end of the tunnel. The ultimate impact will depend on the longevity and severity of the pandemic.

Pandemic protectionism

One of the major implications of the pandemic on global trade is the increase in protectionism and geopolitical instability.

Projected decline in economic indicators for 2020 (%)

Source: UN Conference on Trade and Development (UNCTAD), June 2020

The pandemic has exposed how fragile existing supply chains are – particularly when it comes to politically sensitive products such as food and healthcare supplies. In revealing these fragilities, many nations became reluctant to share their resources and are taking a more protectionist approach to trade. This effect was particularly pronounced in the healthcare sector. The World Bank reported that by July 2020, 91 countries had implemented a total of 187 export controls on medicines and medical supplies since the beginning of 2020, with most having done so at the height of the pandemic. Major producers such as the United States, Britain, and China are included in this list. Additionally, 32 countries have imposed 48 export controls on agriculture and food products since the beginning of 2020. Such protectionism can have disastrous implications for countries that heavily rely on imports for necessities. This is especially true for those in the 'Global South' with already strained healthcare infrastructure and supply chains.

Addressing this protectionism calls for forging deeper regional trade and investment ties. Islamic Corporation for the Insurance of Investment and Export Credit (ICIEC)'s mission and vision is to promote trade and cooperation among member countries, making its role in forging relationships and expanding intra-Organisation of Islamic Cooperation (OIC) trade relations more important than ever.

The ECA environment

While the impact on global trade and investment flow is unavoidable, it is essential that institutions with the mandate and means to stabilize the trade ecosystem step in to do so. There is ample opportunity for government-backed institutions and multilateral export credit and investment insurance providers, such as ICIEC, to support relief efforts.

The unfavorable conditions for global trade are only worsened by a tightened export credit insurance market. In itself, credit insurance is designed as a risk-mitigation tool to support trade through challenging environments. Private insurers reducing or pulling credit limits due to the increased risk leave scores of businesses significantly exposed. In this context it is no surprise that the demand for trade credit and investment insurance increases dramatically during times of economic downturn or difficulty.

According to an OECD survey conducted in May, ECAs are undertaking various new initiatives and restructuring current facilities to ensure that their clients survive these difficult times. These measures include increasing flexibility to the terms and conditions of official support (largely for existing transactions), enhanced facilities and cover for working capital, and in some cases ECAs' statutory limits have been increased. By maintaining, and hopefully expanding, the availability of trade credit insurance solutions to businesses in need, the global economy can deter unnecessary defaults due to short-term conditions and avoid grinding to a halt.

ICIEC's response

Thanks to its strong performance in recent years, ICIEC is well positioned to take on these challenges. That being said, it is taking a balanced and strategic approach to business going forward. ICIEC is committed to continue support for member countries in combatting COVID-19, while also being proactive in maintaining its own portfolio viability.

As part of the IsDB Group's efforts to combat the pandemic, ICIEC's commitment of $150 million is being used to provide insurance for critical transactions, including for the import of emergency medical kits and food supplies. Over $100 million has already been allocated to support short-term trade transactions for the import of medical equipment, essential foods and energy commodities. This has benefited numerous member countries, including Tunisia, Burkina Faso, Mauritania, Senegal, Cameroon, UAE, Oman, Jordan, Egypt and Pakistan.

ICIEC is taking a balanced and strategic approach to business going forward. ICIEC is committed to continue support for member countries in combatting COVID-19, while also being proactive in maintaining its own portfolio viability.

"ICIEC's commitment of $150 million is being used to provide insurance for critical transactions, including for the import of emergency medical kits and food supplies."

There is also a great need for infrastructure development – especially in terms of healthcare for ICIEC's least developed member countries. ICIEC is covering projects that help to build infrastructure, especially in the health sector. For example, it provided €143 million cover for the construction of two new hospitals and five new medical units in five pre-existing hospitals in the West African Republic of Côte d'Ivoire. ICIEC also extended $2.3 million in coverage toward purchasing state of the art medical equipment for hospitals across Punjab, Pakistan. ICIEC is targeting immediate efforts that address urgent demands – such as pharmaceuticals, healthcare supplies and agricultural commodities.

For a long-term recovery, a boost to international trade will be a key part of the world's economic restart. This implies critical access to insurance cover and credit, meaning ECAs will have plenty of business opportunity in the months ahead. However, we would be foolish to underestimate the impact of this crisis on all financial institutions, including ECAs. In the case of ICIEC, despite the fact that markets in which we operate have been significantly impacted by the pandemic, claim rates are currently stable and ICIEC's insurance business remains well capitalized. However, it is entirely within reason to anticipate that claim rates will increase in coming months. The ultimate impact will depend on the longevity and severity of the pandemic.

Looking ahead

In addition to its immediate commitments to fighting the pandemic, ICIEC remains committed to its strategic long-term goals. This includes working alongside member countries to set their individual development agendas back on track. Given the significant gaps in underlying conditions, developing country economies are expected to take more time to recover from the pandemic than their developed country peers.

While the impact on global trade and investment flow is unavoidable, it is essential that institutions with the mandate and means to stabilize the trade ecosystem step in to do so.

ICIEC is also prioritizing projects with the most significant developmental impact. For example, it recently provided €50 million cover to expand 4G telecommunications coverage across Indonesia. Social distancing and quarantine measures have led to isolation for many citizens and the need for stronger telecommunications systems is apparent. The project was prioritized as it ensures that 90% of Indonesia's population, including those in rural areas, can enjoy better coverage.

Lastly, ICIEC's ongoing commitment to the UN's Sustainable Development Goals (SDGs) is stronger than ever. What better time to implement transformational solutions and create a better life for all member country citizens? The SDGs are a foundational focus for the ICIEC, and they are intertwined with all aspects of the organisation. This commitment is clear both through the impact of the projects ICIEC insures, as well as how the SDG focus is immersed in all the initiatives the organisation undertakes. This work continues unabated, as eventually the pandemic will subside, and our gaze will return to the many challenges and opportunities that will shape our world in decades to come. ■

In addition to its immediate commitments to fighting the pandemic, ICIEC remains committed to its strategic long-term goals. This includes working alongside member countries to set their individual development agendas back on track.

Managing credit risk post COVID-19: Remember the five-'C's

By Lillian Labbat, Global Head Credit & Political Risk, Zurich Insurance

When the coronavirus pandemic hit, the impact, both human and economic, was felt in almost every corner of the world. Financial institutions, both insurance companies and banks, have worked hard to support customers through this unprecedented crisis by extending financings and coverages to help bridge the gaps in liquidity. What has become clear is that financial institutions have needed to rethink how they evaluate risk, both credit and country risk. This view of exposure to risk is something that is forever changed.

The global economy has faced recessionary pressures in 2020 and will continue to feel the impact into 2021 as pressure on gross domestic product in many developed and developing countries continues. Those of us who consider ourselves experts in credit risk have had to look at risk in new ways. How solid is an investment-grade rating from a credit agency that was provided pre-COVID-19? Do 2019 financial statements provide a true picture of the company in 2020? How are lockdowns impacting supply chains? What impact will ongoing travel restrictions have on international projects if international workers cannot access work sites? Is the inability of a supplier to follow through on a contract due to lockdowns truly a force majeure? We are all left to ponder these difficult questions.


Lillian Labbat

Determining safe zones

The first thing many evaluators of credit risk did to tackle the issue of identifying 'safe zones' was to divide industries into three groups: red, orange and green. All the industries that were severely impacted by the pandemic, such as aviation, shipping, tourism and retail, were classified as red. There were those industries significantly impacted, such as oil and gas, automotive, commodities and construction, which received an orange classification, while everyone hoped for a turnaround in prices and demand. Then there were those in the green category, which seemed relatively safe, such as healthcare, power, telecommunications and consumer. But what we quickly found was that this was unreliable and too simplistic a measure of risk. In fact, in almost every sector, it was possible to identify companies in a position of strength versus those with weaker fundamentals. Looking at sectors is only one variable and yet we need many more.

The global economy has faced recessionary pressures in 2020 and will continue to feel the impact into 2021 as pressure on gross domestic product in many developed and developing countries continues. Those of us who consider ourselves experts in credit risk have had to look at risk in new ways.

The ability to have access to reliable data was one of the biggest challenges facing providers of credit in 2020. It was crucial to have a view of a company's operations and liquidity at the end of the second quarter to truly assess a company's resiliency. Many companies who are facing serious impacts to their business today had limited access to cash and high debt on their balance sheet pre-COVID, with little room to manoeuvre following a changed demand for their product or service. Those companies who are faring better are those with a diversified product mix who are experiencing growing demand for some products which are offsetting declines in others. Also, the ability to quickly convert to online services in some sectors is crucial to survival. Those companies with access to liquidity and low interest payments are able to handle depressed revenues and increased costs without a significant impact on the health of their balance sheet.

Rating agencies also responded to the need for better access to data, attempting to update their assessments and corporate ratings throughout 2020. Essentially, 2019 financials and corporate ratings were of little value. Obtaining interim figures and an updated ratings outlook is key to evaluating credit.

The ability to have access to reliable data was one of the biggest challenges facing providers of credit in 2020. It was crucial to have a view of a company's operations and liquidity at the end of the second quarter to truly assess a company's resiliency.

Multiple countries feeling the strain

In cross-border credit insurance and trade finance, an additional element that comes into play when evaluating credit risk is the country of risk. A large portion of single-situation credit risk in the credit insurance world involves credit to developing countries. Countries dependent on oil revenues or tourism were the first to feel the strain. The response of the international community to such crises is something that is difficult to predict when evaluating credit but is quite impactful on the outcome. For example, the G-20 debt relief program and the response of multilateral institutions prevented many private creditors from having to face difficult restructurings. One can take comfort in witnessing the international safety net thrown around countries in need. But what is unprecedented in this crisis is the number of countries needing support. This is different from an International Monetary Fund rescue plan for a single country, such as Argentina earlier this year or in previous years. The challenge going into 2021 is determining how much more support will be needed and if there is a point where private creditors will need to face country rescheduling.

When I think back on my credit training days, I recall instructors stressing the five 'Cs' of credit: character, capacity, condition, capital and collateral. I have touched upon the financial and quantitative elements that one must rely upon when evaluating credit. But anyone who has been in the credit world for many years will tell you not to underestimate the importance of the first of the five 'Cs', namely, character. Knowing with whom you are doing business and having a good history with business partners is key to making good decisions. The ability of a company to successfully steer through rough waters and to make the right decisions on people, costs and strategy is often what defines a company as resilient, no matter the sector or the geography. ■

But anyone who has been in the credit world for many years will tell you not to underestimate the importance of the first of the five 'Cs', namely, character. Knowing with whom you are doing business and having a good history with business partners is key to making good decisions.

Is COVID-19 the final blow to globalisation?

By Jean-François Lambert, Founder and Managing Partner, Lambert Commodities

In December 2019, near the Huanan Seafood Wholesale Market in Wuhan, a city of 11 million people in the Hubei province of China, 27 people were infected by an unknown type of viral pneumonia. Unfortunately, we know the rest of the story all too well. Several lies and a lot of denial later, the world was engulfed into a major pandemic with, so far, over a million deaths. For the first time in modern history, despite cutting edge technology and science, the most developed countries in the world opted for the most archaic response to a health threat: lockdown. Consciously, across Europe, Americas, and in many parts of Asia, economic engines have been literally shut down.

More than 10 months after the Wuhan incident, we are faced with the most daunting task: re-igniting economies, while COVID-19 has not been ringfenced. Few doubt that with the brightest minds at work around the world, entrusted with almost unlimited resources, we will be able to overcome the pandemic. A matter of months or a matter of years is the question, not whether we will prevail. We will, but when? And in the meantime, how much economic damage will have occurred? How long will it take to be 'back to normal'?

What does 'normal' mean?

'Back to normal' is probably what most people aspire to. But what is 'normal' and is it realistic to believe that we can resume our pre-COVID-19 life as if the pandemic and its consequences were only a blip in the course of history? That might not be feasible and this is for a few reasons.

Jean-François Lambert

Before the pandemic reached every shore like a slow but relentless tsunami, the world was already facing profound shocks which were altering its course. These were essentially triggered by the political and economic consequences of the 2008 financial crisis. Globalisation was already under attack, particularly in western democracies, where populations believed that it had brought unfair competition from the developing world and very little benefit to them.

The polarisation between the two largest economies, the US and China, was reshaping the world order, with trade increasingly weaponised. Where possible, supply chains were being overhauled to factor in geopolitical risks. Thanks to technology, re-onshoring and concentration around safer regional clusters were already being seriously considered.

More fundamentally, awareness about energy transition was spreading across the world and the 2016 Paris Accord epitomised global concern about climate change and actions necessary to be undertaken at the earliest opportunity. In effect, the world was already on a path of deep change.

How will COVID-19 affect these dynamics? It is unlikely that globalisation finds sudden supporters in western countries, even if

The pandemic will merely act as a catalyst, probably accelerating the transition which found its roots in the 2008 crisis.

international collaboration is the surest and most effective way to fight a global pandemic. Will the rivalry between the two juggernauts abate, even after the leadership situation in the US is resolved? Probably not as one of the very few points of consensus across the political spectrum in the US, and to an extent Europe, is the view that China's ambitions are increasingly threatening the world order.

Acceleration of supply chain restructuring

Far from being held back, the restructuring of supply chains is likely to be accelerated by the pandemic. Panic hoarding in the consuming countries disrupted the just-in-time management which had prevailed among supply chain managers and a growing concern about over-dependency on staples and strategic products is likely to trigger a broad review of supply versus demand management in-country.

The strong undercurrents running before COVID-19 even appeared in Wuhan will not subside. The pandemic will merely act as a catalyst, probably accelerating the transition which found its roots in the 2008 crisis.

Even if the actual timing for a full recovery cannot be scheduled until the pandemic fight is won, five key trends will probably help shape a post-pandemic world in the long run.

Politics 1 – Economy 0

Many governments in western democracies have been criticised for their management of the health crisis and are likely to face harsh reactions in forthcoming elections. As economies struggle to get back in shape, voters will call for more control and protection. Free market dynamics are likely to be affected with more protectionist measures.

Polarisation

The US's inward-looking stance found its roots many years before the inauguration of the Trump administration. Under Chairman Xi, China has made no secret of its ambitions and is unlikely to change course in the next decade. Europe is now more aware than it has ever been that it needs an international strategy to try to counterbalance two players currently trapped in a dangerous rivalry. Many other countries or regions display similar behaviour (Brexit, India vs China, Brazil, Turkey). Economic dynamics and trade flows are likely to reorganise themselves around these increasingly polarised blocks and this, where feasible, calls for shorter supply chains, those less likely to venture beyond potentially dangerous regional boundaries.

Re-industrialisation

As the world partially de-globalises, demand will grow for strategic supply to be at reach rather than depending upon long and more hazardous supply chains. Call for re-onshoring (think 5G) will be more prevalent in our economies. This will be encouraged by governments and fostered thanks to the rapid development of technologies such as 3D printing and robotics inter alia. Renewable energy sources will also be developed where possible (solar, wind, and soon hydrogen). The prevalent trend whereby western economies have been largely dependent upon services will not be overturned anytime soon, but a peak might have been reached (tourism, entertainment, even global financial services?) and industrial value-added could gain traction again in several developed countries.

Acceleration of the energy transition

With lockdowns, populations have rediscovered a pollution-free environment and awareness about hazardous emissions has grown. Renewables and circular economies are seen both as a way to do what is right, but also to lower dependency on energy supply. Every company, however small, wherever positioned on whatever supply chain, is clearly expected to come up with a convincing plan to get greener. Before long, investors and banks will no longer be in position to support any party who does not display a clear ESG strategy with deliverables.

Closer trade, unless it is strategic

What about trade in this context? It will adapt to new realities. Within the main blocks, it will keep thriving, and probably be facilitated by technology (Internet of things, document digitalisation, decentralised ledgers) allowing more efficient control and monitoring and therefore financing. A large portion of trade will remain dependent on long haul transportation, notably for strategic commodities. However, the trade gap, notably involving low income countries is likely to widen further, as risk appetite further dwindles amid more challenging geopolitics. ■

MARKET TRENDS

Counting the cost in the medium term CPRI market

By Julian Spiegel, Senior Reinsurance Underwriter, Credit, Surety and Political Risk, Navigators, a brand of The Hartford

Going into 2020, there was a general expectation of a mild recession and – in line with those expectations – credit (re) insurance markets were beginning to harden. The very long economic cycle, which had started in the wake of the Global Financial Crisis (GFC), was perceived to be drawing to a close. With the escalation of COVID-19 into a worldwide pandemic in March and with many regions heading into an unprecedented economic downturn in Q2 2020, the outlook for the credit insurance industry quickly and drastically deteriorated. In terms of profitability and claims expectations, the credit insurance industry reached its lowest point around May. The GFC had been the industry's largest loss event so far and forecasts for the current crisis were expecting claims levels even in excess of those losses.

It took some time for the credit insurance industry to appreciate the very strong impact of governmental countermeasures which came much more swiftly and broadly than during the GFC. Most government interventions took place in mature markets and some were specifically targeted at the credit insurance industry, including temporary reinsurance programmes and a broadening of ECA mandates into domestic markets. With its stronger focus on emerging market business, the Credit and Political Risk Insurance (CPRI) industry was initially perceived to benefit less directly from governmental interventions than the short term credit insurance industry (which is mainly active in mature markets). As a result, the market capacity for short term credit insurance could be maintained at much more stable levels than during the GFC. The CPRI industry, on the other hand, reduced capacity much more significantly in the early weeks of the crisis. With the exception of business relating to strong counterparties and transactions, there was very little new CPRI business being written for some weeks. In the absence of widespread losses, CPRI market capacity started to come back, however without yet regaining its pre COVID-19 levels.


Julian Spiegel

CPRI exposure to commodities

The CPRI market has significant exposure to transactions involving commodities and to projects located in commodity exporting countries. Commodity markets have shown high levels of volatility over the last months. This is particularly true for the energy markets which account for an important portion of the CPRI market premium. The emergence of COVID-19 as a global pandemic coincided with the ongoing Russian-Saudi oil war and – as a result – oil prices suffered an historic collapse in the first weeks of the crisis. A combination of sharp production cuts and a pickup in consumption led to a partial recovery of oil prices in Q3 2020. Going into a renewed round of lockdowns, pressure is building up again on oil prices and times remain challenging for the CPRI industry and its clients at least through the winter.

With the exception of some significant CPRI market losses in Singapore and Dubai however, there has not yet been a widespread increase in CPRI claims. Berne Union members have even reported fewer medium term credit claims in H1 2020 than in H1 2019. The relatively benign credit claims environment can probably be explained with the help of the following observations. Firstly, some claims might have already occurred but have not yet materialised due to extended waiting periods and suspended insolvency regimes. With the reinstatements of insolvency regimes and with waiting periods coming to their end, those claims could start appearing relatively shortly. Secondly, some claims are being temporarily postponed with the help of short-term liquidity infusions but will occur when government interventions draw to a close. Those claims will likely materialise in Q1 or Q2 of 2021. Thirdly, some claims will not just have been postponed but will also have been avoided. Companies with viable business models that have been facing only temporary liquidity issues will emerge from the crisis with higher debt loads but structurally sound. The total effect of governmental interventions will most likely include a temporary shift of some credit losses from 2020 into 2021 but also a reduction of the overall credit market losses. Contrary to initial expectations, not only does the short term credit insurance market seem to have benefitted from governmental interventions but also the CPRI market. Government interventions have indirectly supported commodity markets by propping up western demand. Some governmental measures were specifically targeted at highly exposed industries like aviation and cruise. To those industries, the CPRI market has non-negligible credit exposures via facultative ECA reinsurance, aviation finance and ship finance.

The wake of fraud scandals

So far, the only significant market losses during the crisis took place in Singapore and Dubai, where a number of companies had to file for insolvency in the wake of highly publicised fraud scandals. Most of those insolvencies have related to traders that have been accused of hiding significant debt levels behind opaque corporate structures and sometimes with the help of double counting of receivables. The emergence of fraud-related credit losses per se is not unusual in an economic downturn. Houses of cards that could persist in a more benign economic environment tend to fall apart in a crisis. On a global level, fraud related credit losses will probably remain a low frequency-high severity issue for the CPRI markets.

While actual claims remain at manageable levels, CPRI underwriters report very high levels of claims mitigation activities including payment deferrals and temporary covenant breaches. With the strong support of ECAs and in accordance with banks (the main buyer group of CPRI) a multitude of measures are being taken to prevent short-term liquidity issues from turning into avoidable insolvencies. On the flip side, government measures have significantly increased corporate debt levels. In the US, so-called zombie companies that are not able to pay down the principals of their debts anymore, have reached a long-term high, according to the Leuthold Group. Even with global economic growth forecasted at 4.6% in 2021, Euler Hermes predicts a sharp 31% increase in global insolvencies in 2021 compared to 2019.

The sovereign space faces similar issues. According to the IIF, the pandemic has pushed global debt-to-GDP levels to a new record. For some emerging markets with a strong reliance on commodity exports and limited FX reserves this can lead to a combination of debt restructurings, multilateral bail outs, import stops and currency controls. Ongoing sovereign restructurings include Zambia, Ecuador, Lebanon, Belize, Suriname and Argentina. Potentially ensuing social spending cuts will also increase the risk of social tension and political violence, according to Shailesh Kumar, The Hartford's Head of Country, Credit and Economic Research..

With soaring debt levels for corporates and sovereigns and a likely increase in corporate insolvencies in 2021, CPRI claims activity is expected to pick up in 2021. The emergence of CPRI claims is anticipated to be partially offset by a continued hardening of the CPRI market. Banks are trying to

CPRI market will likely emerge from the crisis with a book of business that has improved in terms of quality of risks, and that has higher pricing, shorter tenors and stronger structures than going into the crisis.

Trade routes and FDI flows will be impacted and the CPRI industry will prove its worth by supporting its clients through these exciting times. As the economist Joseph Schumpeter put it, "at the heart of capitalism is creative destruction."

manage their aggregates and have expanded their demand for the CPRI product. With CPRI market capacity still below pre COVID-19 levels, the market can be more selective in terms of new business. As a result, the CPRI market will likely emerge from the crisis with a book of business that has improved in terms of quality of risks, and that has higher pricing, shorter tenors and stronger structures than going into the crisis.

CPRI reinsurance

CPRI reinsurance is a niche market within the overall reinsurance market. A hardening of the overall reinsurance market typically also leads to a hardening of the CPRI reinsurance market. According to Moody's and Fitch, the overall reinsurance market has been hardening since January 1, 2020 renewals and is expected to continue on that path into 2021. The anticipated increase in reinsurance pricing will likely not be sufficient to compensate for the increase in pandemic-related reinsurance losses and for the negative impact that low interest rates have on the asset sides of reinsurers' balance sheets. As a result, the upward pressure on reinsurance pricing will likely persist in the medium term. This puts upward pricing pressure also on CPRI reinsurance which is competing against other reinsurance lines for capacity.

In line with many reinsurance lines, January 1 is the most important renewal date for CPRI reinsurance treaties. Since the beginning of the crisis, most CPRI reinsurers have maintained their through-the-cycle perspective and have not significantly shifted reinsurance capacity away from the CPRI market. As a result, CPRI reinsurance capacity has been much more stable over the last months than during the GFC. This strategy will be put to the test at the January 1 renewals against the backdrop of an accelerating surge in COVID-19 cases during the winter months and a potential double-dip recession in Europe. Given the hardening of the overall reinsurance market, the hardening of the underlying CPRI market and the persistent high level of uncertainty going into 2021, there will likely be further increases in CPRI reinsurance prices at the January 1 renewals.

Outlook for 2021 and beyond

Most forecasters are cautiously optimistic that the development of vaccines will bolster the global economy next year and will lead to solid growth levels in the medium term. At the time of writing this article, this optimism is being supported by the positive news coming from Pfizer and Moderna. In the absence of inflation, the Fed and other central banks seem to be willing to maintain their policies of cheap money into the foreseeable future. Many companies will be able to work off their post COVID-19 debt levels in this environment of economic growth and low interest rates. Some companies however will not be able to sustain those debt levels and there could be an increase in CPRI claims in 2021, hopefully at manageable levels for the CPRI industry.

This base case is exposed to significant downside risks including further waves of COVID-19 in 2021 and longer procurement times for a COVID-19 vaccine. There are also risks unrelated to COVID-19 that seem to have temporarily faded into the background but that have not gone away. There is no clarity on the repercussions of a potentially hard Brexit. The future relationship between the US and China remains unclear with a new president-elect in the US and the recent signing of the RCEP trade agreement. Ongoing disputes at the Sino-Indian border and in the South China Sea could escalate into further political violence, to name just a few risks.

In the longer term, the pandemic could have an enduring impact on the global economy including on business travel and the disentanglement of supply chains, the continuing departure from multilateralism and on the ongoing energy transition. Trade routes and FDI flows will be impacted and the CPRI industry will prove its worth by supporting its clients through these exiting times. As the Austrian economist Schumpeter has put it, "at the heart of capitalism is creative destruction." ■

Berne Union claims perspective

By Laszlo Varnai, Associate Director, Berne Union

Unexpected, unpredictable and full of twists and turns, 2020 is not the year anyone anticipated. Although the dominant headline for the year has, of course, been the COVID-19 pandemic and resulting economic recession – induced in part by the necessary public health measures in response – this has not been the only major development relevant to claims for export credit or political risk insurance.

Trade volumes were already in decline through the course of 2019 as businesses grappled with an increasingly unpredictable macro environment and deepening trade conflict between some of the world's largest economies. The oil price war between Russia and Saudi Arabia, coinciding with an acceleration of the COVID-19 impact, in March, only served to highlight weaknesses in some countries, industries and companies. The emergence of several high-profile fraud cases among commodity traders is a prime example of a crisis exposing underlying problems.

The COVID-19 crisis itself is relatively unique from the perspective of both political/credit risk management and public policy. It is neither a classic political peril, nor a directly financial disruption and the risks are highly correlated in general. As such, it has demanded a completely different response from government and industry.

From a claims perspective, things have not turned out as badly as many predicted during the original shock reports in the Spring. As a counterbalance to the health and safety measures imposed, and learning form the global financial crisis (GFC) a decade ago, swift government actions were able to provide solutions for both individuals and businesses (with over 40 million estimated furloughed employees in 2020), as well as the credit insurance industry (for example, states' reinsurance programmes), resulting in an unexpected, lower rate of insolvency (Q2 2020 versus Q2 2019) on a global scale, after all.[1]


Laszlo Varnai

For many companies, the primary issues were not wholly financial. For example, these include physical inability to operate effectively (if at all), staff shortages due to health/self-isolation, supply chain disruptions and reduced demand and decreased revenues, as well as pressure from creditors. Because of this, financial measures (including credit insurance and new working capital products) are only part of the path to recovery.[2] Nonetheless, broad government interventions (in the form of providing options and capacity for credit extensions and rescheduling) have been highly effective in preventing or at least delaying sector wide disruptions (especially in transportation and retail) – even if these could not save some major companies that were already walking on a tightrope.[3]

In the long run, political expediency and practical necessity are required to strike a fine balance between consideration of public health and protection of the economy (as well as government balance sheets). Many of the financial support programmes are temporary in nature and as these expire it is likely the insolvency rates will start to rise as we head through Q4 2020 and 2021. Ultimately, global trade levels are only projected to return to pre-crisis levels by 2023.[4]

Governments have not only focused on their domestic economic stability. There is also a trend of increasing public debt-to-GDP ratios in low and middle-income countries, and at least half of the poorest countries are at high risk of debt distress, or are already in debt distress, with estimated official bilateral debt service payments alone in these countries totalling almost $14 billion in 2020. In response to the increasing risk of non-payment, the most developed creditor countries (G20) signed the Debt Service Suspension Initiative in April 2020, offering a temporary suspension of government-to-government debt payments to 73 countries[5] (44 had signed up by 17 November 2020), also inviting commercial creditors to participate on comparable terms. In addition, from April through September 2020, the World Bank also committed $14.8 billion in financing for participating debtor countries, of which $5.4 billion was in the form of grants.[6]

As we can see from the above, governments have reacted swiftly and firmly to prevent rising claims, which has had an undisputable positive impact on our industry, too.

From the Berne Union's perspective, we also observed a softer impact than initially anticipated through the lens of our members' data. The chart on the left indicates that the overall level of claims paid in 2020 H1 ($3.6 billion) was only slightly higher than the recent reporting periods, but did not show signs of systemic shock, yet.

In 2020, so far, claims have not risen to the level of the GFC, when, in 2009 H2, ST claims rose by 42% to $1.4 billion and MLT claims increased by 250% to $2.4 billion, almost entirely due to commercial claims. The data is independently confirmed by our latest member survey, which recorded that only 13% of our responding members report significantly higher than expected claims levels.

Looking at the toll of the first few months, it is visible that the private insurance business has paid significantly fewer claims than the ECAs (bar chart on the right), while the growing levels of ECA-paid claims were mainly attributed to 'Other cross-border business' and two specific members. These observations do not immediately indicate any systemic crisis, especially considering the typically 'lumpy' nature of MLT claims activity.

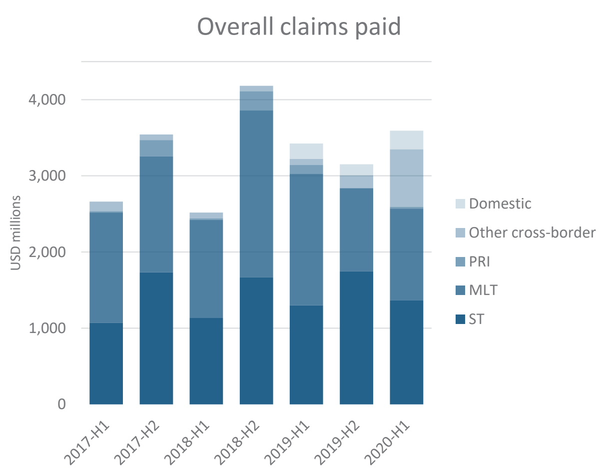
Even if the current crisis were to significantly raise the volume of commercial claims, we are still a long distance from exceeding previous peaks. At the same time, the introduction of the DSSI has reduced the probability of claims arising from sovereign non-payment, at least from that cohort of lowest income and highly indebted countries.

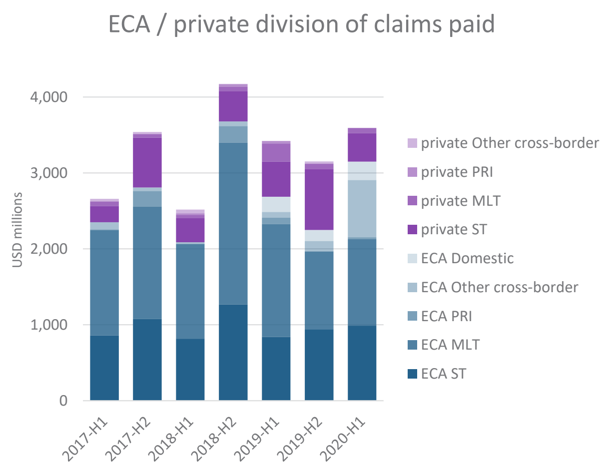
Considering the above, it is premature to make any conclusions on the final claims trends of 2020, as most of our members are either still processing the claims submitted up to November, or awaiting the potential loss notifications. With the effective government measures in place and their delaying effect on insolvencies, the claims levels of 2020 and 2021 will probably show a dome-shaped curve, rather than a sharp blip.

For more detailed data on claims paid by our members, please check the Committees' business trends report and the general business overview provided by the Berne Union. ■

Notes

1 https://www.pwc.com/gx/en/deals/assets/global-restructuring-trends-2020.pdf page six
2 https://worldfinancialreview.com/how-covid-19-trading-pressures-impacts-corporate-insolvency-levels
3 For specific examples, please see the Berne Union 2020 H1 ECA business trends report
4 https://www.eulerhermes.co.uk/newsroom/covid-19-to-drive-43percent-rise-in-uk-insolvencies.html
5 https://www.worldbank.org/en/topic/debt/brief/covid-19-debt-service-suspension-initiative
6 https://www.worldbank.org/en/news/factsheet/2020/05/11/debt-relief-and-covid-19-coronavirus





MARKET TRENDS

Claims and recoveries in a disrupted market

By David Chadwick, Partner, Kennedys and Naomi Vary, Partner, RPC

As is now increasingly evident, COVID-19 has caused widespread disruption across all parts of the supply chain. Reductions in demand, goods shortages, price fluctuations, disrupted orders caused by safety restrictions, import and export restrictions, and bankruptcy of suppliers are all challenges currently facing buyers and suppliers globally. Those who operate across long international supply chains have been particularly affected by the pandemic.

Difficulties in recovering payments in a world where COVID-19 has impacted almost every industry has meant that many businesses have turned to finding ways out of their contractual obligations due to lack of funds, or by seeking to rely on force majeure provisions or the frustration doctrine.

As delayed and failed payments become increasingly likely, organisations will become heavily reliant on their trade credit insurance policies to keep them afloat. In this unprecedented situation, we may also see new problems arise with certain credit risk mitigation products such as trade receivables asset backed securities (ABS) and reverse factoring.

Preparing for an increase in claims

Given the above, trade credit insurers should be (and indeed are) preparing for an increase in claims by policyholders in the coming months. Although it is hoped that banks will support debtors through these difficult times by avoiding automatic loan default triggers and by demonstrating lenience regarding losses, insurers are uniquely placed as an essential support for companies and the economy in general. At present it might be more accurate to say that COVID-19 pressures are preventing already stressed trading situations from resolving themselves rather than COVID-19 itself being the main cause for default. However, over time this dynamic will change.

David Chadwick

Naomi Vary

Some European authorities have offered help to their domestic trade credit insurance markets by raising their insurers' loss absorbing capacities through guarantees backed by public funds. France has introduced a €10 billion programme which will reimburse insurers for payments made to suppliers whose buyers have defaulted, with an extra €2 billion for exports. Credit insurers in Germany will pay €500 million of the first €5 billion in claims, with the government reimbursing them for a further €25 billion, in exchange for 65% of their 2020 premiums. However, some countries are coping well despite having no government assistance.

With traditional lenders tightening their purse strings, suppliers are looking to non-private sources of financing short-term trade, and official export credits for longer projects. As they did in response to the 2008 global financial crisis, governments are having to look to Export Credit Agencies (ECAs) to meet the demand for finance and to ensure that supply chains are maintained. Some ECAs have responded by offering assistance with flexible terms and programmes developed specifically in response to COVID-19.

CIGA in the UK

It is currently moot as to whether COVID-19 is the main cause of corporate/trading distress or just one factor. In the UK, the level to which financial distress caused by COVID-19 can be separated from 'non-COVID' related financial distress impacts whether a company can take advantage of some of the measures prescribed by the Government in an attempt to mitigate the economic effects of the pandemic. The Corporate Governance and Insolvency Act 2020 (CIGA) introduces various measures intended to protect distressed companies. These include a new form of director-led moratorium, in which the company is granted a payment holiday in respect of certain debts and continues to trade under the supervision of a monitor. Although the original text of CIGA made it a condition of the moratorium that the monitor considers it likely to result in the rescue of the company as a going concern, this has now been amended. The monitor is now required to consider that the moratorium is likely to result in the rescue of the company or that this would be the case "if not for any worsening of the financial position of the company for reasons relating to coronavirus." It remains to be seen how the monitors deal with this decision in practice.

Certain provisions of CIGA may be of interest to trade credit insurers providing cover to an insured dealing with a buyer that takes advantage of the CIGA protections:

- The distressed company is granted a payment holiday over its 'pre-moratorium debts'. The terminology is deceptive, as certain debts arising during the moratorium are also termed 'pre-moratorium debts' and are excused from payment. These include debts where the relevant obligation – such as delivery of the goods – was performed before the moratorium, but where the date of payment arises during the moratorium. In other words, the company does not have to pay for goods delivered on credit before the moratorium, if the credit period expires after the moratorium commences. The company can, however, dispose of these goods during the moratorium if this is in the ordinary course of its business.
- Any provision in the insured's contract with the buyer that enables the insured to cease supply or terminate the contract by reason of the buyer's insolvency no longer has effect; unless granted a dispensation by the buyer, the monitor (in the case of a moratorium), or the court, the insured will be required to continue shipments. This provision applies to a wide array of insolvency processes and could create an obvious tension with stop shipments provisions in a trade credit policy. In theory the buyer is required to pay for all goods delivered during the moratorium, so if this is the relevant insolvency process this should at least mean that the continued trading should not increase exposure, but practical operation may see a different effect.
- More widely, any other provision in the contract enabling the insured to cease supply or terminate the contract for any reason (such as non-payment) also loses effect if the right arose before the insolvency process commenced but had not been exercised by that time. It is possible that rather than saving companies this provision could hasten their demise as it may lead suppliers to be less forgiving with regard to payment delays, for fear of losing their remedy should the buyer enter into a moratorium or other insolvency process. That said, to the extent the contract provides for termination in the event of non-payment, and goods supplied during the insolvency period are not paid for, the supplier retains the right to terminate on that basis, if not by reason of circumstances arising before the insolvency process commenced.
- In keeping with protective legislation in many other jurisdictions, CIGA prevents creditors from commencing insolvency proceedings, or pursuing legal action, against debtors taking advantage of the CIGA protection.

The above protections focus on the distressed buyer, with obligations for debt deferral and continued supply passed up the supply chain, to a company that may well have trade credit insurers standing alongside. Discussions are already underway as to how the CIGA moratorium will interact with the trade credit provisions, and lawyers in this area expect some debate on these issues as the economic impacts of the pandemic continue to be felt.

What is clear is that globally, governments are taking steps to provide a degree of support (either financial or legislative) to companies in these difficult times. Trade credit insurers need to take advantage of these wherever possible. ■

How is COVID-19 affecting capital structures?

By Valerio Ranciaro, Director General, SACE SRV

Financial structure refers to the combination of debt and equity that a company uses to finance its operations. It is the structure of the company's finances.

Many models have been developed to identify the specific benefits and costs of using debt (i.e. the tax effects and the costs of financial distress) and equity. However, the greatest contribution remains the 'trade-off theory' by Modigliani-Miller and their followers. A company decides on the amount of debt and equity that should finance its investments by balancing the relevant costs and benefits.

Debt is cheaper than equity and the relevant fiscal benefits are important. Even the most cash-rich companies in the world (e.g. Microsoft, Apple and Amazon, to name a few) are generally better off with debt than without. With low costs of borrowing since 2018, an increasing number of companies are taking advantage of cheap money. Nevertheless, at a certain level, the tax benefit of the debt is balanced by the increased costs linked to a greater probability of default or possible financial distress.

Over the last 10-15 years, the proportion of debt to equity ('leverage') has been significantly increasing, especially in companies subject to takeovers by institutional investors, like investment funds. Sovereign debt as well, especially in the emerging and developing countries, increased drastically and it is now showing signs of distress.


Valerio Ranciaro

During a downturn, highly levered firms are at greater risk of becoming insolvent than their less-levered peers are, since they must continue to make interest payments on their outstanding debt even when their business may have slowed down.

The measures adopted worldwide in order to contain the spread of COVID-19 are resulting in significant operational disruption for many companies: staff under quarantine, weakening supply chains, scarcity of inventories and sudden reductions in demand from customers. These disruptions are creating serious issues for companies across a wide range of sectors.

Businesses in various sectors have been forced to temporarily close due to increased occupational safety and health measures, or due to other business disruptions. Some sectors have decided to terminate business altogether as a result of changed consumer behaviour.

Therefore, there is a shock on the offer side, a shock on the demand side and a looming uncertainty in general: a very dangerous trifecta. These shocks will trigger a significant increase in insolvencies and,

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Companies restructure for a variety of reasons, including in response to business downturns. Companies now need to revisit their business models, assess the impact of COVID-19 on short-term objectives while keeping an eye on long-term performance.

As companies understand the impacts on their businesses, timely measures need to be identified and rapidly implemented to ensure their viability, while managing stakeholders and planning for the future.

Steps in the restructuring process

The steps in the restructuring process involve:

1. **Due diligence**, both legal and financial. Legal due diligence usually takes into account consideration of the underlying credit documents of each creditor and the legal constraints of the legal regime in the debtor's jurisdiction. The purpose of financial due diligence is to gain a full understanding of the current financial and organisational positions, future cash flow position, strengths and weaknesses

2. **Standstill**, a commonly employed technique to provide sufficient time to all stakeholders to assess the position of the business, the legal rights and to determine a restructuring strategy, without additional pressures being created by precipitous creditor action. During this stabilisation phase, due diligence and assessment for organisational change will occur

3. **Development of a restructuring plan**, namely the development of a financial and organisational strategy to address the causes of the corporate crisis. A sustainable restructuring can only be achieved if the elements giving rise to the crisis are resolved. A contingency plan will also need to be devised, in case of any unforeseen situation which may jeopardise the execution of the restructuring plan

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4. **Negotiation and implementation**, the final part of the process where the preparatory analysis from the preceding steps is converted into an operable restructuring agreement.

Throughout these four steps, the stakeholders' management (working with management, the Board and external stakeholders to help navigate the company through the restructuring) is of paramount importance.

The restructuring process is a lengthy and demanding mechanism that enables an exchange of reliable information upon which a debtor and its creditors can then design a restructuring plan. As the ongoing pandemic is accelerating structural changes in many sectors, restructuring a stressed or distressed capital structure will need to pace itself to the new, faster rhythms. ■

Valerio Ranciaro is also co-author of: *Innovation in financial restructuring: Focus on signals, processes and tools* published by Virtus Interpress.

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Pandemic recovery calls for public/private collaboration

Dan Riordan, President and Chief Underwriting Officer for Political Risk, Credit and Bond at AXA XL examines the need and opportunities for collaboration between government and business to build for a future beyond the pandemic.

A major lesson in 2020 so far is that the public and private sectors need each other to keep economies moving. In addition to claiming hundreds of thousands of lives, the coronavirus pandemic has inflicted financial shocks around the world. As governments and businesses begin the process of recovery, they have many opportunities to collaborate, rebuild and invest for future growth.

COVID-19 has caused the deepest global recession in decades, and the World Bank forecasts the global economy will shrink by 5.2% in 2020. By comparison, real GDP in 2019 grew by 2.4%. That is a stunning drop, and it's even steeper in advanced economies, as the pandemic disrupted supply and demand, trade and finance. Behind those numbers is an enormous human cost, with millions of people out of work and many forced into poverty. Recovery will take a long time, but that timeframe can be shortened if governments and the private sector combine their strengths.

A recent World Bank analysis identified four shocks to global value chains from COVID-19:

Dan Riordan

- Employment: The pandemic has caused a global drop in employment due to business closures and social distancing.
- Trade costs: COVID-19 has raised the cost of imports and exports due to various factors, including increased inspections, reduced hours of operation, route closures, and higher transport expenses.
- Tourism: International travel and tourism have dropped sharply. To put this into perspective, international air passenger traffic has fallen nearly 89% in 2020, according to the TSA screenings. The International Air Transport Association also says 2020 will be the worst year financially in the history of aviation.
- Services: Populations in quarantine have shifted away from purchasing services that require close human interaction, such as mass transportation, restaurants and recreational activities. Instead, they are consuming more goods, which can be delivered to people's homes.

Some governments are encouraging private institutions and banks to step up and support the rebuilding of critical infrastructure. This is a process of 'crowding in' private-sector organizations to balance and supplement public financing with private capital.

Crowding in the private sector

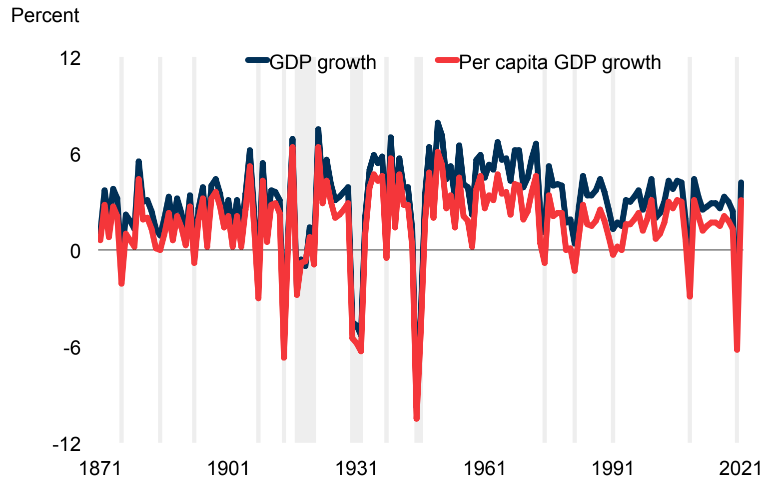
A range of organizations, from government agencies, to international banks, multilateral agencies and development financing groups, are trying to determine what's next after COVID-19. Some governments are encouraging private institutions and banks to step up and support the rebuilding of critical infrastructure. This is a process of 'crowding in' private-sector organizations to balance and supplement public financing with private capital.

The table shown, offers a sampling of new or expanded programs to aid economic recovery. While the challenges from the pandemic are numerous, the diversity of such programs is a positive sign that shows a great deal of opportunity for public/private partnerships.

'Build it back better'

A rallying cry that can stabilize economies and support businesses to put people back to work is 'Build it back better.' This

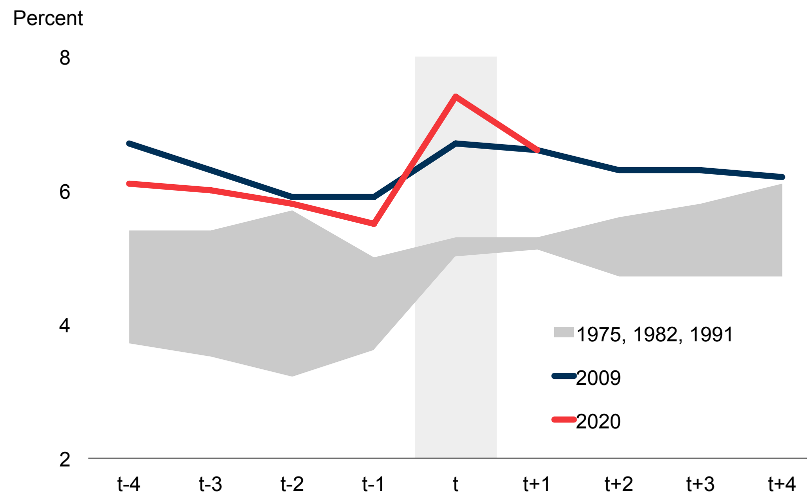
Global GDP growth



Source: Bolt et al. (2018); Kose, Sugawara, and Terrones (2019, 2020); World Bank.

Note: Data for 2020-21 are forecasts. Shaded areas refer to global recessions.

Unemployment rate



Source: International Monetary Fund; Kose, Sugawara, and Terrones (2019, 2020); World Bank.

Note: Year "t" denotes the year of global recessions (shaded in light gray). The darker shaded area refers to the range of the three global recessions—1975, 1982, and 1991—with available data. Unemployment rates for 2020-21 are based on forecasts by the International Monetary Fund in April 2020.

A rallying cry that can stabilize economies and support businesses to put people back to work is 'Build it back better.' This philosophy, which we fully endorse at AXA XL, should inspire investment in critical industries such as transportation, energy, health care and financial services.

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Although investments entail risks everywhere, not just in emerging and developing markets, there also are tools to mitigate those risks. Political risk, credit and bond solutions offer ways to protect investors, balance portfolios, achieve capital relief and ensure that projects are completed.

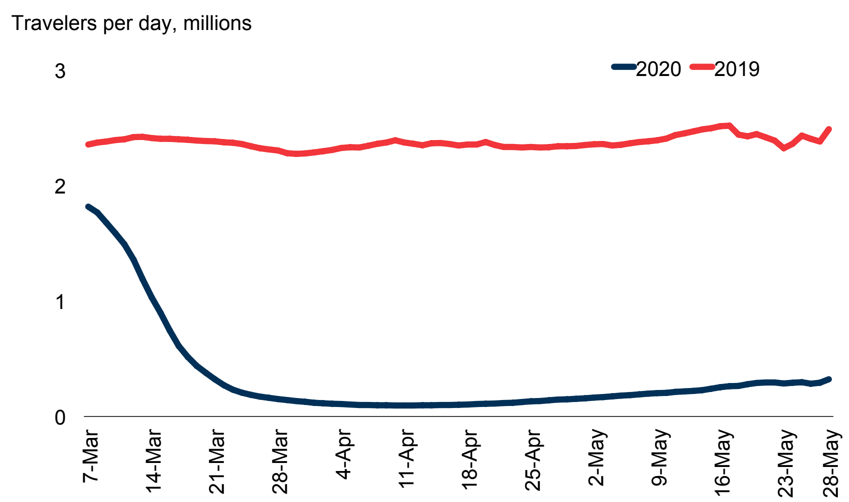
Understanding complex risks and providing innovative solutions is in AXA XL's DNA – from our underwriters to our risk analysts, we look to find solutions among the challenges. We therefore take pride in sharing our expertise on every project for which we provide financial support. We are eager to partner with governments, development agencies and financial institutions on strategic projects, to accelerate global economic recovery and drive growth into the future.

All in all, AXA XL is committed to help our clients exchange uncertainty for certainty by offering the coverage to invest and conduct cross-border trade with confidence.

The shocks from the COVID-19 pandemic make clear that the risks to critical infrastructure sectors are sizable. At the same time, those same sectors also represent opportunities for the public and private sectors to work together and make a difference. A bigger risk, frankly, is to remain on the sidelines. ■

Dan Riordan is President and Chief Underwriting Officer for Political Risk, Credit and Bond at AXA XL and is based in Washington, DC. Before joining AXA XL, he held various senior executive roles in political risk, specialty and global corporate property and casualty insurance. He has had a long association with the Berne Union, serving as president from 2013 to 2015.

TSA passenger traffic



Source: Transportation Security Administration; World Bank.

Note: TSA = Transportation Security Administration. Figure shows a 7-day moving average. Last observation is May 28, 2020.

Agency	Selected New or Enhanced Programs due to COVID-19
World Bank	• Real Sector Crisis Response Facility (IFC) • Global Trade Finance Program (IFC) • Working Capital Solutions Program (IFC) • Combined Global Trade Liquidity and the Critical Commodities Finance Programs (IFC) • Health Emergency Preparedness and Response Multi-Donor Fund (HEPRF) • COVID-19 Fast-Track Facility (IFC & MIGA) • Managed Co-Lending Portfolio Program (MCPP) (IFC)
US EXIM Bank	• Working Capital Guarantee Program • Medium-Term Single-Buyer Insurance Policies Issued to Exporters or Financial Institutions • Bridge Financing Program • Pre-Delivery / Pre-Export Financing Program • Supply Chain Financing Guarantee Program
European Bank for Reconstruction and Development	**Solidarity Package** • Trade Facilitation Program • Vital Infrastructure Support Program
Asian Development Bank	• $20 Billion COVID-19 Pandemic Response Package • COVID-19 Active Response and Expenditure Support Program • Supply Chain Finance Program • Asia Pacific Disaster Response Fund (APDRF)
Finnvera	• Finnvera Guarantee • Start Guarantee • SME Guarantee
US Development Finance Corporation	• Rapid Response Liquidity Facility
Export Development Canada	• Business Credit Availability Program (BCAP)
Inter-American Development Bank	• Sustainable Development Bonds • Contingent Credit Facility for Natural Disaster Emergencies (CCF)

Setting long term positive strategies for ECAs

By Valentino Gallo, Founding Partner, Javalyn Partners

The COVID-19 crisis has accelerated the redefinition of the international trade landscape which had already been underway for a few years due to the combined effects of the implementation of climate change policies, the advancement of technological innovation, and the spread of protectionist policies and trade sanctions around the world. These forces and their complex interconnections are reshaping cross-border trade and global supply-chain flows, with long term ramifications for the strategies of the export credit agencies.

With the move from relief measures to mitigate the effects of the pandemic on exports, to the post-emergency phase focused on stimulus, the strategic priorities of ECAs have shifted to initiatives aimed at helping exporters secure new business. This is proving challenging because major capital investments in sectors that drove the growth of ECA activity over the last few years, in particular cruise lines, airlines and energy, are being cancelled or postponed due to corporate financial distress in the travel industry and the prices of oil and other commodities that are affecting the energy sector. In addition, in the specific case of exports, the introduction of protectionist measures such as the increase of local content requirements in a growing number of countries, are making it more difficult

Valentino Gallo

for international contractors to win business in foreign markets. As a result, the competitive environment facing international contractors has become much tougher and proactive support from the export credit agencies can become a critical differentiating advantage.

Favourable considerations

There are, however, some more favourable considerations which temper the adverse scenario depicted above and can help ECAs to set the direction of their long term strategies:

i) Governments and corporations around the world are pledging to be carbon-neutral and to the implementation of transition strategies to zero emissions. The transition to a zero-emissions economy is already having an impact on global capital spending across multiple sectors. Redefining the way people live at its foundation (from housing to nutrition, work, mobility, education, healthcare) will require gigantic investments in the construction, upgrade and retrofitting of the infrastructure that supports the

Under the current very uncertain scenario, it may be mutually helpful for ECAs and exporters to have a broader, strategic dialogue, with an eye to the future.

activities of businesses and consumers alike. Investments in renewable energy, electric and hydrogen fuelled transportation, smart grid, hydrogen power, nuclear power, biofuels, waste management, clean water and sanitation will take a central place in export finance activities in the years to come.

ii) The pandemic has also highlighted several vulnerabilities in the way businesses, governments and consumers are connected to one another and operate in an increasingly digitised society. The new buzzword is resilience. Through the lockdown and remote-working digital infrastructure has shown its importance as never before, but also its weaknesses. The broader the usage of artificial intelligence and machine learning, the further the growth of online services for consumers (for example, education, telemedicine, wellness, home security, financial investments) and businesses (for example, remote working, blockchain, cryptocurrencies, data-driven remote diagnostics, digitised trade finance, collateral surveillance) will require major capital spending in telecom/digital infrastructure globally (including submarine cables, 5G networks, data-centres, towers and geospatial technology).

iii) For many years, jobs and investments associated with manufacturing activities have moved from developed market economies to emerging markets. More recently there have been hints of a reversal of the trend, with many businesses having implemented or announced plans to shift at least a portion of their supply chain to developed countries. Some reasons are financial. Tariffs are obvious, but automation, robotics, and the reduction of energy costs in some regions have materially reduced the labour and production cost gap that made the original outsourcing so attractive. On the non-financial side, ESG concerns of high carbon footprints are a growing factor, as are resilience and national security concerns with long supply chains. These trends are expected to be particularly pronounced for high-tech sectors and industries for which energy is a key input and will require major capital investments.

The capital spending and investment landscape is still so volatile and complex that even the most solid and best organised exporters are struggling to build a solid pipeline of new contracts. The problem is more acute for projects in developing countries and large transactions that require all hands on deck negotiations with dozens of counterparties, which are difficult to be conducted effectively on a remote basis. Travel restrictions are affecting installation works and testing due to the inability of specialised professionals to reach project sites. The disruptions caused by COVID-19 have been so pervasive that most businesses are reassessing their plans and developing new business origination strategies. ECAs are no exception and are going through the same reassessment process.

Call for national strategic reviews by global ECAs

Under normal circumstances the interaction between ECAs and exporters is mostly transaction-specific and deal focused. Business-reviews between ECAs and exporters are more the exception than the norm and are often triggered by the need to address specific and urgent issues. Under the current very uncertain scenario, it may be mutually helpful for ECAs and exporters to have a broader, strategic dialogue, with an eye to the future.

ECAs, leveraging their institutional role and organisational capabilities, can promote and lead a strategic review of their sponsoring countries' long-term national export prospects. The review can be framed within the broader economic initiatives

Participation in the review should be extended to a wide spectrum of businesses and institutions beyond traditional users of ECA support. Such participants would complement and give valuable inputs that could help to identify the export opportunities of the future and a new breed of clients for the ECAs, on both the exporter and importer side.

that many governments have recently launched to make the post pandemic recovery strong, durable, sustainable, and inclusive. Exporters should be encouraged to participate in the dialogue. Given the awareness across the business community about the unprecedented challenges that each national economy is facing, as well as the correlation between the ECA mission and the Sustainable Development Goals and ESG policies embraced by the corporate world, it is very likely that an ECA-led initiative would be welcomed and would motivate businesses to join the call for action.

The capital spending and investment landscape is still so volatile and complex that even the most solid and best organised exporters are struggling to build a solid pipeline of new contracts.

The results of these strategic reviews can become the pillar of ECAs' long-term business plans and provide valuable information for their preparation. The reviews should be designed with the dual goal of identifying both immediate and long term opportunities. Immediate opportunities are likely to be identified in the sectors of traditional strength for national exports. Longer term areas of focus should also target business in new sectors with high growth potential.

Participation in the review should be extended to a wide spectrum of businesses and institutions beyond traditional users of ECA support. Such participants would complement and give valuable inputs that could help to identify the export opportunities of the future and a new breed of clients for the ECAs, on both the exporter and importer side. The list of participants may include representatives from the following organisations:

i) Corporations in highly innovative/high growth sectors, e.g. the circular economy, renewable energy, plant-based nutrition, water treatment, telecommunications and space, biotechnology/biomedical

ii) Technology companies, including start-ups, operating in these high growth sectors and those in the fields of trade finance fintech, robotics and artificial intelligence

iii) Non-bank supply chain finance providers

iv) Local institutional investors engaged in infrastructure, ESG, sustainability and impact-investing

v) Banks and law firms active in export and project finance. These entities benefit from strong international networks and have a vested interest in collaborating with ECAs

vi) Other national agencies active in trade and investment promotion

vii) Development finance institutions

viii) Microfinance networks

A strategic review would identify a shortlist of priority clients and opportunities, existing and prospective. Climate-change, digitisation and resilience should be the central components of the discussion with priority clients. As such, two related questions could help to identify many opportunities:

1) What is your climate change strategy and what are the investments you will be making as part of it?

2) What are your digital and resilience strategies and what are the investments you intend to make?

Exporters and ECAs would then have the opportunity to respond to clients with valuable solutions, including effective equipment and service solutions and an attractive export credit financing package to complement the offering. ■

A strategic review would identify a shortlist of priority clients and opportunities, existing and prospective. Climate-change, digitisation and resilience should be the central components of the discussion with priority clients.

CORPORATE VIEWS

Staying match fit

If ECAs and companies had an athlete's mindset, the future could be even better, argues Andreas Back, Senior Manager, Financial Services, Wärtsilä

Wärtsilä is a global leader in smart technologies and complete lifecycle solutions for the marine and energy markets. By emphasising sustainable innovation, total efficiency and data analytics, Wärtsilä maximises the environmental and economic performance of the vessels and power plants of its customers. In 2019, Wärtsilä's net sales totalled €5.2 billion with approximately 19,000 employees. The company has operations in over 200 locations in more than 80 countries around the world. Andreas Back, Senior Manager, Financial Services at Wärtsilä, gives his unique take on the sustainable power sector for exporters in the post COVID-19 world. It's a question of the right mindset, and forward-thinking ECAs will be vital.

- Customer finance may become decisive as investors hesitate
- Post-COVID-19 energy landscape is yet to be shaped, but massive upheaval might be around the corner
- A holistic view is desirable, and financiers must not forget energy security matters

Post-match roundup

"Injuries of various seriousness form part of many athletes' careers. Unfortunate events will happen to everyone involved in professional sports, and the most regrettable of them occur whilst preparing for a major sporting occasion. Although injuries can temporarily spoil a season, or even a dream, there is always the day after tomorrow, and a young and otherwise healthy athlete can always draw comfort that there are many competitions ahead if only the mindset is right.


Andreas Back

Having the right mindset is equally important in the business world. The pandemic can be regarded as a serious injury, and many corporates' 2020 season was spoiled due to the virus. Now the question is what do forthcoming seasons have to offer?

Looking at the energy market, it is quite safe to claim that the virus has speeded up the energy transition from traditional thermal forms of generation to renewables. In the ideal future, our planet's energy generation will be based on renewables as base load, with fast and flexible generation or battery storage providing peaking power, stability and back-up.

As a consequence, many manufacturing companies are forced to modify their product range to meet the shift in demand. Coal and large combined cycle gas turbine plants are being replaced with solar and wind, whereas battery storage and flexible natural gas, synthetic gas or even hydrogen will serve the peaks and stabilise the grid. Investment decisions will be taken not only based on underlying technology and revenue

ECAs should have the capability to support societies so that they can enjoy a secure and stable power supply based on an optimal mix of generation types.

streams, but also on the holistic fit of the investment in the energy system.

Changing role of ECAs in a sustainably-powered future

The crisis has highlighted the changing role of financial institutions and the growing importance of adaptability in ECA-backed financial solutions. As major capex-driven investments are being transformed into a more scattered landscape of wind and solar PV farms, the market for critical additions from an energy security perspective will grow as well. Forty to 50 years ago, the financial community was focusing on large base-loaded coal or nuclear plants, as they were capital intensive and contributed to nice fees and margins.

The upcoming massive investments in renewables may snow-blind traditional financiers and investors just as was the case back in the day. This could lead to huge opportunities for the insurance market. Although it is sensible to embrace renewables as the new base load of the world, they are volatile by their nature, and achieving an optimal generation mix, avoiding immense overinvestments and costs, requires active participation by the insurance market. Therefore, it is of utmost importance to stress the role of balancing power in a renewables-intense system.

This is where the ECAs in particular will have a central role to play. New players are popping up in the capital markets, many of whom are focusing on sustainable and green financing. Insurance companies and pension funds are also in the game, and the large multilaterals are claiming their share. There will be ample liquidity for renewable investments as supporting green initiatives is trendy, and rightly so.

It might not be as appealing to look beyond the individual investment and form an opinion on the energy system as a whole. ECAs should have the capability to support societies so that they can enjoy a secure and stable power supply based on an optimal mix of generation types. This means extending loans and guarantees not purely based on renewables' merits (with traditional risk assessment not forgotten), but also on the applicability of the solution in the market or energy mix.

Critical role of ECAs

The traditional definition of the mandate of an ECA is not to compete with private sector lenders, but rather provide financing for transactions that would otherwise not take place because commercial lenders are either unable or unwilling to accept the political or commercial risks inherent in the deal. Going forward, in order to achieve sustainable and economically sound energy markets, the mandate should acknowledge that ECAs have a role to fill in investments that may be critical for the people, but do not necessarily fall under the renewables category. This particularly concerns the battery storage sector, as the OECD Consensus is a bit vague with regards to battery storage and where the asset should belong. Going forward it would be advisable to define the role of energy storage, and it would make sense to include it in the renewables' framework.

This market gap has to be filled if the transition to a less carbon intensive world can be successful. Having said this, one should also remember the tremendous developments occurring in the field of synthetic gas and hydrogen. In the future, power security may well be achieved in an economically sustainable way using proven technologies operated on carbon neutral fuel.

Athletes that have been plagued with injury do often return more motivated and determined to show the world that they're still in the game. There are even cases where setbacks have blossomed into world records. There is no doubt that we as corporates can do the same, but it will require flexible and agile partners and a deep understanding of market dynamics. The good old times are gone, but the future will be even brighter." ■

The OECD Consensus is a bit vague with regards to battery storage and where the asset should belong. Going forward it would be advisable to define the role of energy storage, and it would make sense to include it in the renewables' framework.

CORPORATE VIEWS

Credit insurers, your exporters need you

What do exporters need in this crisis? An impassioned call to action for credit insurers to exporters, from an exporter. David Avram, Trade & Export Finance Director at Fives sets out the case.

Fives is an industrial engineering group, which among other things, designs and supplies machines, process equipment, and production lines. In 2019 it had close to €2 billion in sales across 30 countries and is a significant user of export finance.

One of the strength of Fives is its large geographical exposure allowing it to take advantage of diverse regions to develop its activities. And 2019 was strong for the company in Europe, in France, in US and in Japan – which was a compensation for some slowdown in some emerging economies.

In terms of the finance Fives offered corporate clients before the crisis, it mostly worked with Bpifrance (about 80% of its contracts). But it also has worked with SACE, UKEF and CESCE (where its plants are installed). The majority of financing was in the form of buyer credits, and a few supplier credits with ECAs. Quite often, it had the opportunity to propose using political risk insurance in the private market.

How is the 200-year old company being affected by the current crisis and what will happen next?

"We have reasons to be optimistic for the Fives group despite a difficult year due to the COVID-19 crisis. Thanks to a diversified portfolio of activities and to its large geographical footprint Fives is in a position to reduce the impact of the crisis on its level of activity.

In this very challenging environment, the trade and export finance areas are taking an even more important role. Indeed, securing our sales when almost all economic studies announce a strong increase in company failures in the coming months is more mandatory than ever!

On this subject we are working with several key players. For one of them, the credit insurers, I want to send the following message: please consider the specificities of the period, continue to support our activities, use the different supports set up by different governments as much as possible. We exporters need you!


David Avram

Contract security and compliance

One last word about contract security outside of the trade finance area: when business is more difficult and competition is enhanced, more than ever we need to be fully aligned with our compliance policies. It is not because we need to fight harder to win an order that we should feel authorized to deviate from these rules.

That being said, let's focus on how our export finance activities have evolved during the past months. While I was even recently working on contracts for amounts of several dozens of millions of euros, I am now also active on the smallest opportunities, let's say below €20 million. That means that, to work on our deals, banks will have to review their policies and accept to work on smaller tickets.

In France we have had the chance to take advantage of an offer from Bpifrance which can finance 'small' export finance contracts. That will be very useful for us for our coming deals, but we hope that we will also be able to give business to French commercial banks.

Just a word on export credit insurance activity: today we need to be more competitive than ever and the French export credit agency has a role to play to help reach this objective. In recent weeks we have had the chance, to obtain support on a complicated but strategic deal from Bpifrance. They need to continue to invest time in understanding our needs and probably, in the future coming months, to accept to support some deals with different risk profiles." ■

Export Credit Developments at the OECD

Silvia Gavorníková, Director International Relations, EXIMBANKA SR and Chairperson of the Working Party on Export Credits and Credit Guarantees (ECG) reflects on the main good governance issues relevant to official export credits in respect of environmental and social due diligence, anti-corruption and debt sustainability.

Rising importance of official support for sustainability in exports

There are unprecedented challenges facing the whole export finance ecosystem, including those who provide official support to exporters. Beside the impact of the COVID-19 pandemic, the sustainability dimension of cross-border trade keeps increasing in importance. Topics such as climate change mitigation, sustainable development and transparency have become some of the key points of interest and discussion for governments, academics, businesses, industry, civil society and the general public alike.

Export Credit Agencies of governments gathered under the multilateral OECD forum, where officially supported export credits disciplines are created, implemented and monitored, do not only want to keep pace with current developments but rather to engage actively, streamlining responsible business conduct and good governance values throughout their activities. The essence of the Working Party on Export Credits and Credit Guarantees (ECG) mission is three OECD Council Recommendations, covering the main good governance issues relevant to the area of official export credits in respect of environmental and social due diligence, anti-corruption measures, and debt sustainability.

Complex challenges and opportunities amid pandemic

The COVID-19 pandemic has affected our work as well. Despite this, current developments, reflected in our work are a balance of challenge and opportunity. Technological advances and the need to shift regular meetings online have given us the opportunity reach out to more non-OECD counterparts. We were encouraged by the participation of China, Nigeria, South Africa, alongside Brazil, Bulgaria, Kazakhstan, Romania, Russia and Ukraine at our events. Outreach activities with civil society organisations and industry or private and public financial institutions have provided a unique opportunity to familiarise ourselves with different frameworks, opinions, approaches, practices and standards employed in the respective fields. But most importantly they are helping us to strengthen cooperation built on shared values and principles. Business practices nowadays justify this approach, since the globalised export finance field and project complexity is increasingly bringing together stakeholders from different countries, industries and institutions.


Silvia Gavorníková

Reflections on the continuous commitment to deter bribery

The revision of the Recommendation of the Council on Bribery and Officially Supported Export Credits, which was adopted in 2019, fostered transparency of due diligence policies by considering various relevant parties involved in export credit transactions and broadened its scope on domestic public officials and private sector bribery, where prohibited under the national laws of OECD members. As 2020 marked the first year of the revised Recommendation being in force, the initial phase of the implementation has been launched in the form of a members' survey. This exercise reconfirmed the continuous commitment of governments to take appropriate measures to deter bribery in export transactions, explained measures put in place and shared the overall implementation experience. As a result, an informal technical expert panel has been established to take work forward. Moreover, in the short term we are planning to organise a workshop for bribery experts aiming to build a body of experience by considering best practices, relevant international developments and the evolving business environment.

Sustainability from an environmental, social and human rights perspective

Sustainability of the official support of exports from an environmental, social and human rights perspective and related initiatives for minimising possible negative impacts keeps playing a role of the utmost importance within the ECG agenda. A level playing field in terms of a common approach to addressing the potential adverse environmental and social (E&S) impacts of projects had been guided by the Recommendation on Common Approaches on the Environmental and Officially Supported Export Credits. This document, adopted by the OECD Council, serves as a framework for ECAs, setting requirements and benchmarking of E&S performance of transactions against established international standards.

Technical experts, responsible for assessment of transactions sustainability from a good governance perspective, are gathered in dedicated subgroup of E&S Practitioners. The increasing number of large projects worldwide is resulting in a more frequent and necessary cooperation of private and public institutions as well as national and multinational financial institutions from different countries and with different mandates. In order to improve cooperation in terms of administrative procedures and cost efficiency, ECG annually brings together experts from a broad range of financial institutions, including multilateral development banks as well as Equator Principle financial institutions, to share experiences and discuss coordination from a technical perspective and further convergence of standards employed.

The role of export finance stakeholders in climate change mitigation efforts is a central element of general discussions. There are ongoing experience sharing discussions under the auspices of the ECG and its expert subgroups with the aim of supporting ECAs' efforts in terms of gradual transition of economies to more green and environmentally sustainable models. Emphasis is put on the assessment of climate related impacts of ECAs' portfolios, as an essential part of a sound and ambitious climate strategy.

Transparent and sustainable support for the developing world

As OECD member states are major providers of officially supported export credits, ECG members are aware that all activities have to be pursued in a responsible manner with respect to the development needs and capabilities of developing countries. The aim is to help ensure that lower income countries do not run up unsustainable external debts that might impact their ability to alleviate poverty and improve the lives of vulnerable communities. We acknowledge that the COVID-19 pandemic and oil crisis pose yet another challenge for developing countries, as their revenues are often closely linked to global demand. Therefore, ECG regularly invites representatives of the International Monetary Fund and the World Bank to its meetings to inform members of current developments regarding developing countries and debt policies of both institutions which are being reviewed regularly. We believe that sharing knowledge, experience and data is crucial for ECG members in order to improve their own strategies to provide responsible support to developing countries, ensuring that their external debts do not grow extensively. This commitment was also supported by the transposition of the Recommendation of the Council on Sustainable Lending Practices and Officially Supported Export Credits into the OECD legal instrument.

The continuing efforts of governments to deliver sustainable finance has also been reflected in the renewal of the mandate of the ECG in 2019 for another five years, endorsing the work on finding the best responsible, sustainable and transparent support for all business activities. The Good Governance Export Credits Instruments, the so called Green Book[1], has been recently issued and includes up to date wording of the instruments mentioned above. ■

Note

1 https://www.oecd.org/trade/topics/export-credits/documents/Good-governance-export-credits-instruments-2020-web.pdf

A new deal for the OECD Arrangement?

Pekka Karkovirta, Chairman of the Participants to the Arrangement on Officially Supported Export Credits and Vice President, International Relations, Finnvera takes a look at the future of the OECD Arrangement as it, arguably, faces a mid-life crisis. How will the jigsaw pieces fit together?

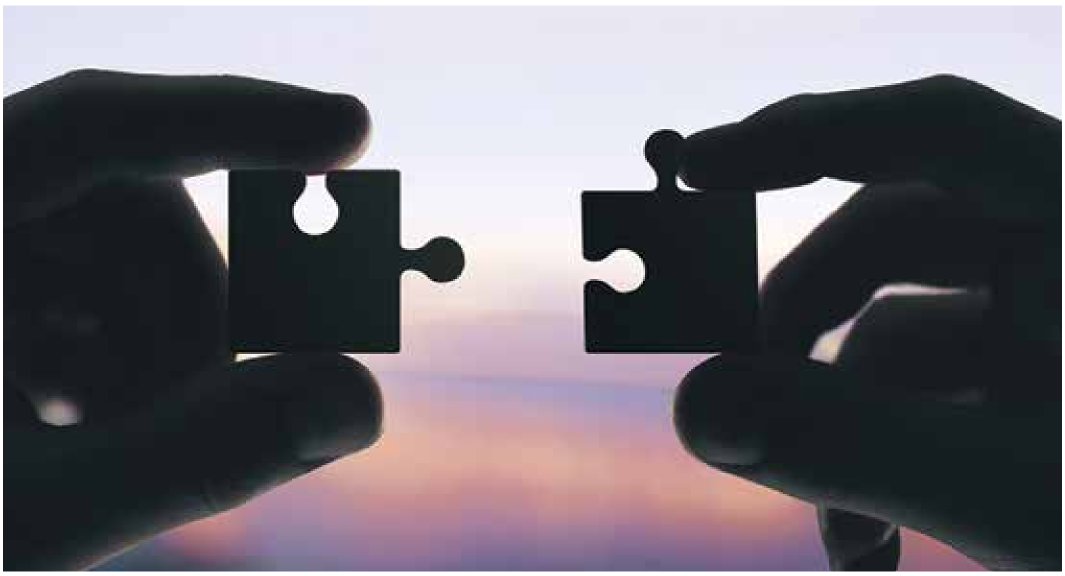
"After around 40 years of existence, the Arrangement on Officially Supported Export Credits has become middle-aged and suddenly appears to be asking itself, "What is this all about, what is my life, why has everything changed around me, where am I going to?"

In recent years, we have seen a continuous build-up of pressure towards the Arrangement. Banking market regulation, blending of various public financing sources in a transaction, renewed ECA business models and competition with non-Arrangement financing – all this has changed the game. Arguably, the biggest export credit provider in the world is not a Participant. Just add COVID-19 and heightened pressure, practically in all countries, to support companies and exports with various measures taken by governments.

The Arrangement of today is a document of around 150 pages long, and is relatively difficult to read. It has been written by professional export credit negotiators as a compromise text between the Participants. It is not always very clear, and it may not always meet the needs of markets, exporters, buyers or projects. Would it be time to have a fresh look?


Pekka Karkovirta

During its 40 years of life, new negotiated texts have been added piece by piece to the Arrangement. Clearly, in the first years, outright subsidies were removed such as the matrix of fixed interest rates not based on markets (and the same rates for all currencies!), and later, major improvements were made. These included: the introduction of rules on premiums, tied aid rules, various sector understandings such as for nuclear power plants, aircraft, railways, coal-fired electricity generation, climate change mitigation, project finance,



etc. This piecemeal approach has now been questioned. Could we have simpler, more straightforward rules and in consequence leave it for financial professionals in ECAs to underwrite relevant tenor, repayment profile, down payment, local cost support, etc, for each transaction? As many banks have opted out of export finance or reduced these services and ECAs are offering increasingly more funded solutions or providing direct credits, there is no doubt ECAs are today the real professionals in this business and can provide the necessary financial engineering.

Five challenges ahead for the new thinking

The first challenge is maintaining the objective of a level playing field. This is even more important today as new instruments, programmes and schemes of public finance emerge. The raison d'être of basically neutralising competition on publicly supported financial terms has not disappeared.

Secondly, a fundamental pillar of sound underwriting, extreme flexibility may lead to excessive financial terms offered. After all, ECAs are government policy tools, and policy based interests could override sound underwriting in specific situations. For example, it is relatively difficult to shorten tenor in an industry once an ECA offers, say, 20 years of repayment terms. The ECA and the others following would actually establish the 'market standard'. The dangers of a race to the bottom and crowding out private markets do exist.

Thirdly is the use of correct levels of premiums. At least, a look at premium levels for longer tenors would be considered if and when longer tenors were allowed with renewed flexibility. What levels would be the right ones considering market pricing, credit risk and self-sustainability and being relatively 'prohibitive' in excessively long tenors? The other option is to have a maximum repayment period established as in the current Arrangement.

Fourthly, it is of no surprise that climate issues are on the table both in a restrictive mode, like for coal-fired electricity generation projects, as well as an incentivising mode like for climate change mitigation projects. How can a comprehensive and logical 'climate approach' be written? So far, mainly longer tenors are allowed for specified climate friendly transactions. Obviously, this leaves other 'green' transactions without this specific support. With overall longer tenors possibly for all, how should green transactions be incentivised? The issue of reduced premiums may be in conflict with the issue of self-sustainability and subsidisation. The question remains what is the collective level of ambition of Participants to the climate issue?

Fifthly, public financing outside the Arrangement rules has really changed the game. How could Participants to the Arrangement negotiate rules for other sources of public finance, for example development finance, that may compete with ECA financing? Clearly, a whole-of-government approach is a must for entering any such discussion, and the question to be asked is whether these programmes cause a trade diversion. To be able to even to analyse the situation, transparency is of paramount importance.

Understanding that the Arrangement will remain the only global agreement governing export credits, the task ahead is a balancing act of finding compromise between various angles: competition, underwriting flexibilities, reasonable pricing, climate, blended financing, etc. It is a jigsaw puzzle of fitting together pieces of concepts, government policies, real life exports, various players and increasing political attention. ECAs and export credits have become at the forefront of government instruments supporting our economies." ■

The first challenge is maintaining the objective of a level playing field. This is even more important today as new instruments, programmes and schemes of public finance emerge. The raison d'être of basically neutralising competition on publicly supported financial terms has not disappeared.

Developments in export finance in Latin America

By Pedro Carriço, Founding partner of T|X|P Partners and ECA, Bureau of Experts

The last half-decade has not been easy for Latin American economies, especially when compared to the recent past when it seemed they could do no wrong. Although there is an ongoing structural shift in global growth towards developing countries, the region has not been able to consistently take advantage of emerging opportunities. This is in part due to the uncertainties of the current global trade environment, with sudden policy moves and protective measures implemented by key players on a recurring basis, and the relatively low prices of the commodities that still represent a major share of the region's exports. The region's inability to adapt to an evolving world is also a result of internal political turbulence arising from corruption scandals, social inequality, and institutional fragility.

Most countries in the region had been moving forward in their processes of addressing important internal issues and adapting to the new realities of the world, albeit in fits and starts. As such, the year 2020 was supposed to provide some relieving tailwinds, with a slight acceleration of local economies in a context of improving world GDP growth. There were, as always, visible yet unalarming headwinds on the horizon. That is, until COVID-19. Latin America is a region accustomed to crises of all sorts, but it had been left largely untouched by previous pandemics of recent memory and was unprepared to deal with such a novel situation. The human and economic costs of dithering or ill-suited action have piled upon existing problems, aggravating the demands on future policy making.

Pedro Carriço

OECD and Berne Union surveys have clearly shown that countries with ECAs reacted quickly by leveraging capacity for support, expanding working capital programs, creating new facilities, and increasing flexibility of terms and conditions of their traditional products. The emphasis of the policy response has been on rescuing SMEs, the hardest hit and least-prepared segment of the fabric of any economy. Most Latin American countries, however, lack the availability of cemented instruments to deal with the trade and export finance challenges of our pandemic world. Consequently, crisis response has been slower, smaller and less far-reaching.

Latin America is a region accustomed to crises of all sorts, but it had been left largely untouched by previous pandemics of recent memory and was unprepared to deal with such a novel situation.

Trade difficulties exacerbated

In normal conditions, the region was already facing a difficult trade environment. The year 2019 saw a decline in exports of 7% year on year in South America and 11% in the Caribbean, due mainly to lower commodity prices and lower demand from China. Intra-regional trade suffered with sluggish growth in the larger economies of Argentina, Brazil, and Mexico. The lockdowns brought on by the pandemic worldwide have worsened last year's setback by increasing competition in regional and external markets as industrial powers with excess product seek alternative buyers. Adding insult to injury, global risk aversion exacerbated the financing difficulties faced by Latin American exporters, especially SMEs, while advanced economies' firms could find some assistance in emergency programs to sustain production and seduce buyers.

There have been noteworthy developments in the region to make up for policy shortcomings in the area of export promotion. Changes have involved the creation or reorientation of existing structures, from development banks to guarantee funds, as well as the mobilisation of resources from multilateral institutions. A few examples to illustrate the measures taken in the region include:

Argentina

The Argentine development bank BICE (Banco de Inversión y Comercio Exterior) has gained renewed importance. Although macro financial conditions provide limited room for injection of resources, the bank seems to be shifting its focus to greater support of manufactured exports. In an effort to recover the loss of thousands of exporting firms recorded since 2009, BICE has created working capital and pre-export finance lines for manufacturing SMEs with extended tenors and low fixed interest rates. A small financial sector and reduced access to external funding are hurdles on the path of this restructured export scheme, but the degree of success also depends on FX and trade policy reforms as well as changes in central bank and tax regulations.

Colombia

In Colombia, exports have stagnated at around 15% of GDP since the 1980s. Bancóldex, the Colombian export-import bank, was folded into Grupo Bicentenario in late 2019, a conglomerate of financial entities with state participation. The bank has continued its support to exporting firms, now bolstered by multilaterals, but with little apparent innovation. At state level, a set of measures to promote internationalisation of Colombian companies has been reinforced this year. With the participation of the FNG (Fondo Nacional de Garantías), another Grupo Bicentenario institution, SMEs can get assistance to find new markets and increase competitiveness while gaining access to guarantees for investment in fixed assets used in export production.

Mexico

Mexico is another example of multilateral engagement to boost export support. Unlike in Colombia, where the focus has been in smaller firms, the Mexican authorities also turned their eyes to strategic industries with long supply chains and strong international linkages. A recent US$200 million credit line from CAF to Bancomext was set up to support exporting firms in the steel and automotive industries.

Brazil

Colombia was not the only country caught in the middle of a restructuring of its official export support scheme when the pandemic hit. In Brazil, the export credit finance apparatus has suffered from various budget restrictions, organisational restructuring, policy reorientation, and procedural uncertainty for the last two years. At the same time, engineering service companies

The lockdowns brought on by the pandemic worldwide have worsened last year's setback by increasing competition in regional and external markets as industrial powers with excess product seek alternative buyers.

If the countries in the region are intent on climbing the value-added ladder, they must offer a suite of dependable financing instruments to attend to the needs of their exporting industries, in good and bad times.

lost access to official support because of questionable methods used to win contracts in certain countries, leaving capital goods suppliers orphaned by large projects that mobilised demand from extensive supply chains. As a result, manufactured exports, which should have benefited from continuous BRL depreciation, fell 7% and 15% in the eight months to August in 2019 and 2020, respectively.

The focus at the state companies involved in export support has shifted to privatisation efforts in varying degrees, with Banco do Brasil/Proex less affected while ABGF is being wound down altogether. At the national development bank BNDES, which historically finances about 90% of long-term exports, internal reorganisation has eliminated the export finance department and redistributed staff as export specialists into other sectoral areas. In the meantime, the government has created inter-ministerial working groups to redesign the model of official export finance support, taking into account private sector stakeholder inputs. Such an effort is a time consuming enterprise in normal times, and pandemic restrictions, with associated hardships, have only pushed back the deadline for the setup of a new model while throwing into question many of the accepted assumptions in the process.

Furthermore, in the roster of measures announced by Brazilian authorities to help companies wrestle with the current economic crisis, there are no policies directed specifically at assisting firms with their exporting difficulties. Although the instruments for official support still exist, it has been challenging for responsible officials to put them to work in a context of policy transition and intense budgetary restrictions. The apparent stronger-than-expected recovery from pandemic lockdowns, although obviously positive for the economy, may only make the financing gap more evident, as lenders allocate funds to hot domestic infrastructure sectors, such as water utilities, natural gas and housing, to the detriment of MLT export transactions.

Some silver linings?

Nevertheless, the COVID-19 crisis has – as a silver lining in a fog of destruction – highlighted to Latin American authorities the importance of having tools at their disposal that can fill financing gaps in times of sudden market withdrawal. If the countries in the region are intent on climbing the value-added ladder, they must offer a suite of dependable financing instruments to attend to the needs of their exporting industries, in good and bad times. ■

Pedro Carriço is Founding Partner of T|X|P Partners and ECA | Bureau of Experts, providers of solutions for Trade, eXport, PPP, Project, and Agency finance in Latin America.

In Brazil, the export credit finance apparatus has suffered from various budget restrictions, organisational restructuring, policy reorientation, and procedural uncertainty for the last two years. At the same time, engineering service companies lost access to official support because of questionable methods used to win contracts in certain countries, leaving capital goods suppliers orphaned by large projects that mobilised demand from extensive supply chains.

Building on the halal brand with ECI Islamic

Etihad Credit Insurance (ECI) has launched its Islamic Finance suite of products in the eye of the COVID-19 crisis. It's part of the agency's drive to narrow the trade finance gap and tap into the potential of the halal market globally. ECI's CEO, Massimo Falcioni, and Zishan Iqbal, Director of Murabaha Solutions, spoke to Katharine Morton, Head of Trade, Treasury & Risk at TXF about the agency's plan and the products.

ECI Islamic, a Shariah-compliant trade credit and export finance insurance suite of products, was launched by Etihad Credit Insurance (ECI) at the end of October. ECI is the UAE Federal export credit company which is mandated to increase diversification in non-oil trade. UAE is playing an increasing role in world trade, and specifically in halal trade worldwide. ECI may be a new player, established a full century after the first export credit agency (ECGD in 1917, currently UKEF), but it has the unique potential to develop trade financed according to Shariah law.

"As ECI stays true to its mandate of supporting the UAE's non-oil sector in line with the vision of the wise leaders, ECI Islamic offers Shariah-compliant trade credit, finance and investment solutions in order to provide Islamic businesses a competitive swing in the international market," says Zishan Iqbal, Director of Murabaha Solutions at ECI.

ECI Islamic is designed to boost the UAE's halal export industry and to push its strong position as a global leader in the fast-growing Islamic economy and ECI is one of the first sovereign export credit agencies in the Middle East to offer Shariah-compliant export credit insurance and guarantee solutions.

This aspect of 'Etihad' (togetherness, cooperation) is the financial dimension of the expanding consumer Muslim halal culture which has broadened beyond the food sector into the pharmaceutical and lifestyle industries. Specifically, through its use of Shariah compliant financial mechanisms and products, ECI aims to be recognised as the leading innovative world class ECA in the Middle East and throughout the world where Islamic companies trade and their banks operate.

ECI has worked in partnership with the Dubai Islamic Economy Development Centre (DIEDC) to develop its offering and the suite of ECI Islamic products has been signed off as Shariah-compliant by Dar Al Sharia, a Dubai consultancy firm consisting of professionals with expertise in Sharia, law, banking and finance. The portfolio is re-insured by the Islamic Corporation for the Insurance of Investment and Export Credit (a member of the Islamic Development Bank) which is the only agency to offer such services for the member countries of the Organisation of Islamic Cooperation.

Massimo Falcioni

Zishan Iqbal

ECI Islamic aims to address the needs of four customer segments: banks, investors, large corporates and SMEs. Export credit solutions offered under the ECI Islamic banner include trade credit insurance (which includes whole turnover policy, single risk short term policy, and single risk long term policy), Letter of Credit confirmation insurance, Islamic export finance, foreign investment insurance, and surety bonding.

Risk sharing at the heart

At the heart of ECI Islamic is the concept of risk sharing – rather than risk transfers – and transparently sharing the surplus generated in the future. There are two separate funds associated with the products – one a pooled policy holder fund, and the other a shareholder fund.

Banks globally will be able to use the product. At the outset, ECI Islamic is targeting Islamic banks, and conventional banks that have Shariah-compliant products through dedicated windows. "We are not limiting ourselves and we are willing to collaborate with banks that have Shariah-compliant solutions," says Iqbal.

Collaboration with other ECAs on Islamic solutions?

Does ECI plan to help other ECAs access the Islamic finance market? ECI has already been partnering with multiple ECAs – including SACE, UKEF and Sinosure and is in discussion with other leading ECAs, Iqbal says. "The aim is that if a transaction meets the eligibility criteria of the ECAs concerned, ECI can issue cover based on Islamic and Shariah principles and our partners can stand at our back and reinsure us," he adds. "We have that capability and our proposition is end-to-end Islamic."

Benefiting from the trusted 'halal brand'

According to ECI the global halal industry has gained substantial traction over recent years. The Pew Research Centre estimates that by 2050, the number of Muslims worldwide will grow from today's 1.7 billion to 2.76 billion, comprising 29.7% of the world's population.

Their growing number has also resulted in growing halal and Islamic faith-inspired ethical consumption needs. In the 2019 State of the Global Islamic Economy Report released by US-based research and advisory firm DinarStandard, the halal spending of Muslims reached $2.2 trillion in 2018, spread across the food, pharmaceutical and lifestyle sectors. The report also projected this number to increase to $3.2 trillion in 2024. Halal products are also being used by non-Muslims.

Iqbal is keen to point to the opportunities that stretch beyond simply the use of the products for religious reasons. "Halal and Islamic solutions have become a brand – a brand of trust, of corporate social responsibility, of transparency and a brand of sharing the risk and moral values," he says.

The broader picture in a COVID environment

To counteract the current crisis, ECI's CEO Massimo Falcioni points out that ECI has increased financial and insurance guarantees without increasing fees. It has more than 1600 revolving credit guarantees of US$1.2 billion equivalent to support the non-oil economy. During tough times, its commitment has increased, he says. Prior to the crisis (in August 2019), ECI launched specific support to SMEs in the form of an online solution 'SME Protect' which provides simple to access support via an OTC product helping businesses broaden their understanding of trade credit solutions and providing guarantees to receivables so SMEs can provide credit to clients without financial loss.

Encouraging investment through flexibility

ECI is flexible on local content requirements, adds Iqbal. "If you look at some global ECAs' eligibility criteria, some are quite strict, wanting 100% and some only want 20%. Given the dynamics here on the ground in UAE, we can be more flexible. [UAE has] a lot of re-exports and a lot of companies use us as a hub for Asia and Africa in particular. We are [happy] to look at each transaction and at how it contributes to the GDP of UAE, it can go down as far as 10% as long as it is exported and re-exported from UAE."

ECI is also providing support to incoming projects, particularly in renewable energy, waste management and greenfield projects. While not a member of the OECD, the OECD Arrangement will sometimes provide a good template basis for ECI to use, although it will also be flexible on this.

Meanwhile, Falcioni remains optimistic amid the looming synchronised global recession. He argues that in these unprecedented times, the past is not always a good guide as macroeconomic forecasts are based on models that will have inputs skewed by past projections.

"The UAE has proven to be very a resilient economy during the crisis with a very agile and visionary government which is looking to implement 17 Sustainable Development Goals (SDGs) as its first mandate; the vision for UAE's Energy 2050 policy is to reduce carbon/fossil dependency. UAE is a country looking forward thanks to its inspired leadership. Retreat is never an option, looking forward with optimism is the key to success." ■

More information is available from ECI on info@eci.gov.uae

Venezuela: A Brief Update

By David H Anderson, Principal, Anderson Risk Consultants

For most of the export credit and investment insurance world, and indeed for most of the financial world, Venezuela long ago fell off the radar screen. When information about the country is published, it tends to contain the words 'economic catastrophe,' 'humanitarian crisis,' or 'failed state.' Even for agencies tasked with aiding distressed countries, Venezuela poses daunting challenges. However, as risk takers in Latin America, we ignore Venezuela at our peril. It is too important to the region in terms of geography, natural resources, and size. If you have not read about the country for a while, never fear, this article will give you a brief update and sources for additional research.

Berne Union Activity

Berne Union members have reduced their exposure and new commitments dramatically over the past several years as per the figures below (in millions of US dollars).

Some of that reduction is by legal necessity as economic sanctions have been implemented by the US and the EU. However, most of it is driven not just by the country risk outlook but by loss experience. The spike in MLT claims in 2018-2019 followed many years of significant claims levels. Carmen Vara, Director at Spanish export credit agency CESCE, says that the turning point for her agency was in 2011, when CESCE started having problems on a supplier credit transaction to the Venezuelan state. At that point, CESCE stopped issuing new coverage. She expects that eventually such debts will be negotiated via the Paris Club. I recall when some types of political risk cover and short term credit coverage (particularly against offshore PDVSA-controlled entities) were available from private insurers, but those days are over. A quick survey of private insurance brokers reveals that no one is quoting these days, even where a transaction would be theoretically permissible by sanctions.


David H Anderson

Berne Union Activity

Medium-Long Term Credit	2015-YT	2016-YT	2017-YT	2018-YT	2019-YT	2020-H1
New Commitments	90.5	570.6	0.0	0.0	0.0	0.0
Commitments Outstanding	6,863.8	4,896.6	4,038.8	1,952.7	292.8	248.4
Claims Paid	11.5	41.3	29.9	678.3	348.9	40.6
Recoveries	0.1	0.4	6.6	0.0	0.0	0.0

Political Risk Insurance	2015-YT	2016-YT	2017-YT	2018-YT	2019-YT	2020-H1
New Commitments	304.02	161.46	160.07	24.14	6.40	0.00
Commitments Outstanding	1,169.37	875.26	338.75	245.34	232.68	227.43
Claims Paid	0.00	3.70	6.82	0.00	0.00	0.00
Recoveries	0.00	0.00	0.00	0.00	0.00	0.00

Short Term Credit	2015-YT	2016-YT	2017-YT	2018-YT	2019-YT	2020-H1
Commitments	1,141.12	385.63	283.18	262.16	570.74	161.73
Claims Paid	202.42	56.24	25.56	1.05	0.34	1.76
Recoveries	25.01	11.93	19.52	0.24	0.00	22.50

Source: Berne Union

The economic abyss

The prolonged economic depression in Venezuela is among the worst of any country since the Second World War. Oil is still the lynchpin of the economy, and it has been hit dramatically by the effects of low oil prices, dramatically falling production due to lack of investment and mismanagement, and sanctions by the US, the EU and other countries. The IMF expects a 25% drop in GDP in 2020, coupled with 6,500% (hyper) inflation, and that follows five years in which US dollar GDP had already contracted by 60%.[1] Since 2015, gross foreign exchange reserves have been drawn down from US$16 billion to $6.5 billion.[2]

The debt picture is similarly grim, with gross government debt at 232.8% of GDP.[3] Having defaulted on multiple bonds from 2017 to 2019, Venezuela's access to new debt, even to formerly willing creditors such as China and Russia, appears to have been nearly shut down. Attempting to cut off the regime's financing sources, the US prohibited the purchase of Venezuelan debt in 2018. Accordingly, the 2027 bonds were trading at less than 10 cents on the US dollar as of mid-September 2020.[4]

The effects on Venezuelans have been severe. While there was some progress in fighting poverty under the high oil prices and social programmes of the previous administration [under former President Hugo Chávez], more than 80% of the population now lives in extreme poverty.[5] With the bankruptcy of most of the private sector, the middle class has been essentially wiped out. Venezuela has fallen well behind its neighbour Colombia in human development indicators like life expectancy, infant mortality, and child malnutrition.[6] Even before the onset of COVID-19, Venezuela's health care crisis was well underway. Locals perceive crime, which is often perpetrated by military and police officers, as worse than ever.

One area of improvement has been the supply of basic goods, a problem until the second half of 2018 because of the government's price and foreign exchange controls. The government liberalised those controls quietly in 2019 and the shortages stopped. However, new prices are beyond the reach of most Venezuelans, and hyperinflation keeps it that way.

Millions of Venezuelans have chosen migration as a way of surviving. Of a current population of 28.4 million, approximately five million Venezuelans have left the country in the last six years. It is 'the largest external displacement crisis in Latin America's recent history', according to the International Organization for Migration."[7] The vast majority of Venezuelans on the move (4.2 million) have stayed within Latin America. Colombia hosts the greatest number at 1.8 million. Other hosting nations include Peru (861,000), Chile (455,500), Ecuador (366,600) and Brazil (253,500). According to the Wilson Center, the influx of Venezuelan migrants and refugees has placed considerable strain on the resources of host countries, particularly the health and education systems. It has also increased competition for jobs in the areas where Venezuelans are concentrated, which has the potential to inflame xenophobic sentiments among locals.[8]

With this kind of economic turmoil, one would be excused for thinking that no foreign business would continue to operate in this environment, but that is not the case. "Companies in oil services, chemicals, and food production still see long term potential in Venezuela and are staying," says Raul Gallegos, who covers Venezuela for Control Risks, a specialist risk consultancy. "In addition, the regime has figured out that it has to become more capitalistic in order to survive, and there are many key infrastructure assets that it can sell off to private interests from China, Russia, Iran and others. The regime has options to maintain the status quo for a long time."

The prolonged economic depression in Venezuela is among the worst of any country since the Second World War. Oil is still the lynchpin of the economy, and it has been hit dramatically by the effects of low oil prices, dramatically falling production due to lack of investment and mismanagement, and sanctions by the US, the EU and other countries.

For the great majority of export credit and investment insurers, there will be no new commitments until conditions materially improve, and the main focus will be on the Paris Club, reschedulings, and claims recoveries.

Political quandary

One reason that President Nicolas Maduro's regime has options is that there is no institution or opposition within Venezuela to check its power. In May 2017, Maduro convened a constituent assembly that later declared itself to be the legislature, though many countries refused to recognise it. Chávez had packed the Supreme Court in 2004, and then all its members were hand-picked by Maduro in 2015. The military has been shrewdly and corruptly brought under control, with help from Cuba, since the Chávez administration.[9] It is true that Maduro's popularity is extremely low (one poll says 13%), but opposition leader Juan Guaidó (who is recognised as interim President by about 60 countries) is only at about 26%.[10]

Gallegos asserts that there are three main elements propping up the regime: Corruption, criminalisation of officials (which then binds them to their government enablers), and surveillance. According to Transparency International, Venezuela's corruption level is now in the same league as Democratic Republic of the Congo, Somalia, and Afghanistan.[11]

There are significant international pressure and sanctions on the regime. The US and most Western Hemisphere countries do not recognize Maduro as legitimate, rather they see the National Assembly-elected Guaidó as the interim President. Talks between the regime and the opposition mediated by Norway stalled in 2019 after Maduro pulled out, citing US sanctions.

Maduro still has significant supporters, including Russia, China, Cuba, Turkey, and Iran. Although China and Russia were the regime's principal financiers, all of the debt is in default and none of these countries is now willing to provide new loans to the regime. New transactions are frequently done on a cash or barter basis. With China and Russia backing the regime, the US has been blocked from mobilising the UN Security Council to exert more pressure.[12]

With the regime in control, the opposition in disarray, and the international community divided, it is difficult to see how conditions in Venezuela could improve. If there is going to be change, analysts agree it may have to come from within 'chavismo,' (groups that were loyal to Chávez originally and now are part of Maduro's regime). Schisms in the military may develop, but anything approaching another coup attempt is still seen as a low probability event, mainly because of the regime's controls. Poland's Lech Walesa or the Soviet Union's Mikhail Gorbachev may provide better models as to how change could occur.

Forecasters of various persuasions have a long history of being wrong about Venezuela. One thing is certain, it is possible for the existing economic conditions and regime to continue for years. For the great majority of export credit and investment insurers, there will be no new commitments until conditions materially improve, and the main focus will be on the Paris Club, reschedulings, and claims recoveries. Some bold companies will continue operations there, but they will generally do so without credit or political risk coverage. ■

Notes

1 https://www.imf.org/en/Countries/VEN
2 https://tradingeconomics.com/venezuela/foreign-exchange-reserves#:~:text=Foreign%20Exchange%20Reserves%20in%20Venezuela%20averaged%2012295.51%20USD%20Million%20from,Million%20in%20September%20of%201962.
3 https://www.imf.org/external/datamapper/profile/VEN/WEO
4 https://www.bloomberg.com/news/articles/2020-10-19/venezuela-s-government-is-trying-to-revive-moribund-debt-talks
5 https://www.imf.org/en/News/Articles/2020/01/29/tr012920-transcript-of-the-january-2020-western-hemisphere-department-press-briefing
6 http://hdr.undp.org/en/countries/profiles/VEN
7 https://www.iom.int/venezuela-refugee-and-migrant-crisis
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10 https://www.economist.com/the-americas/2020/06/25/how-venezuelas-regime-plans-to-win-this-years-legislative-election
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Buyer information in Africa

By Vinco David, Secretary General, Berne Union

Improving the quality and availability of buyer information in Africa is a key to boosting trade. Why is it needed and how can it be made better?

Amid the avalanche of news about the impact of the COVID-19 pandemic on the economy, we could be forgiven for forgetting that there also are other issues affecting trade. One of these is the lack of reliable credit information in many developing countries, in particular in Africa. This is an impediment to the much-needed growth of trade – which is both important for economic growth, and combatting poverty. Here is an analysis of the problem and some possible solutions.

The role of credit insurance

About 13% of global cross-border trade is credit insured. Not all trade requires protection against credit risk. Payment risk in inter-company trade, or for goods and services paid in advance, or trade on spot markets, such as for oil, is negligibly low. But many goods and services are sold on credit to companies and governments, with tenors ranging from one day to over 20 years. A fair amount of these transactions would only go ahead if credit insurance is available. This protects the continuity of the seller and unlocks bank financing for working capital for the seller and extended payment terms required by the buyer.

The role of buyer information for credit insurers

Buyer credit information is the basis for the underwriting of credit risk on commercial

Vinco David

buyers. Many countries have legislation and control systems in place to ensure the quality, timeliness and accessibility of (at least) corporate annual accounts. This enables credit insurers to assess the credit risk, in addition to assessment of other risk factors, such as more qualitative information, and political, macroeconomic and sector analyses.

But developing countries are the ones that could benefit most from trade support. That includes much of the African continent where reliable corporate financial information is not available. This is a major reason why credit insurers – both public (ECAs) and private, both African and from other regions – are holding back on underwriting corporate risk in Africa. And without credit insurance, many transactions on credit terms will simply not take place. This is a considerable impediment to the development of intra-African trade and imports into Africa.

The share of Sub Saharan Africa as a destination region for credit insured trade is around $40-50 billion annually or 2% of global credit insured trade. This includes both intra-African trade and imports into Africa. This amount is far below the potential and needs of the region.

Buyer credit information is the basis for the underwriting of credit risk on commercial buyers. Many countries have legislation and control systems in place to ensure the quality, timeliness and accessibility of (at least) corporate annual accounts.

(Note: these data refer to trade credits – so-called short-term credits. It does not include export credits to Africa – the so-called medium/long-term credits. These medium/long-term credits often benefit from credit risk mitigants such as government guarantees, offshore structures etc.)

Is it all that bad for trade credit?

Generally, it is bad for trade credit in Africa, but there are a few exceptions:

- Listed companies. They are required to make available and file their audited accounts.
- Some regional variance (e.g. South Africa).
- Buyers with up-to-date, reliable accounts who are willing to share these. This is quite a labour-intensive process. The buyer needs to be contacted and explained the importance of sharing the accounts with a supplier and an insurer they do not know for the benefit of being able to buy on credit.
- In many countries the Registrar of companies allows for public search of company information (i.e. shareholders, directors, share capital). However, this process is manual, so requires traveling to the Registrar. Additionally, the records are not always up-to-date and do not include the accounts.
- Some institutions, such as Afreximbank, are setting up depositories of buyer credit information. However, this is still in an initial phase.

What needs to be done?

At various levels measures are required to better enable credit insurance and thus promote and support trade. These measures start with the right legislation and regulation needed in most Sub-Saharan countries:

- A change in legislation requiring companies to submit audited financials with their annual returns in a timely manner. Many countries throughout the world have such legislation, mandating Registrar such as Companies house, Chamber of Commerce or other organisation to collect audited financials and disclose them. The example from the UK can be found here.
- Allow third parties to access the information. It is important that this collected financial information is made available online by these mandated organisations, so that remote access is possible by any member of the public, usually against a (small) fee.

Certainly in times of limited travel possibilities, such as during the current pandemic, it is essential to digitise buyer credit information to a much larger degree than has been done so far.

- Implementation and enforcement of globally accepted auditing standards that all certified public accountants must adhere to. Standards based on GAAP, IFRS, as applicable, or any other internationally accepted standard.
- Improve education of certified public accountants. There are many national and international accountants' associations and universities that provide education in internationally accepted accounting standards.
- More frequent updating of records/information held at Registrars. Non-financial information, such as names of directors, should be updated in a timely fashion. Financial information should be updated at least once yearly within a certain timeframe after close of each financial year.
- More reliable information from credit reference bureaus. Bureau information, if available at all, is often of low quality and therefore not reliable. This low quality is a function of limited reliable financial information being publicly available.
- Sanctioning and prosecution of fraudulent activity in trade, such as impersonation fraud.
- More generally, a culture of more financial openness by corporates should be stimulated.

The need for more digitisation amid the pandemic

Credit insurers underwriting risk in Africa often tend to visit the buyers (the importers) to get a better understanding of the credit risk on them. This is, of course, a very labour-intensive and costly activity. Certainly in times of limited travel possibilities, such as during the current pandemic, it is essential to digitise buyer credit information to a much larger degree than has been done so far. ■

4

Future trends

Time to double down on trade digitisation? On counting virtual beans

There are distinctions between virtual and real in trade digitisation. How much is the current crisis helping drive change? The challenges are more than simply counting metaphorical beans. Katharine Morton, Head of Trade, Treasury & Risk at TXF reflects on the state of play.

How many beans make five? A bean a bean, a bean and a half, half a bean and a bean. I have been growing runner beans for the first time, and this children's game leads me to think about reality, digitisation and trade finance in the current crisis. Digitisation is an awfully big adventure, a very big beanstalk to climb.

Talking about digitisation of trade, both in terms of logistics and finance, has been something the industry has been good at, for years. Talking, that is. COVID-19 increases the financiers, borrowers, exporters/importers, insurers and lawyers and others' desire to make sure documents are prepared, sent/received, verified and signed electronically. The pandemic appears to have gingered the pace up, and discussion of trade digitisation has been more animated of late. How much is talk really becoming action? There are great hopes for the ICC Digital Trade Standards Initiative (DSI), the rebadged UTN launched again in March under the ICC's wing, supported by ADB funding, and a new Managing Director appointed in September, Oswald Kuyler, could help pick up the pace.

Katharine Morton

Distinguishing the 'virtual' from 'not real'

One of the elevator pitches for digitisation is that it provides, hopefully, a more transparent approach than paper, and traceability is there to highlight and eliminate human error and discrepancies. Distinguishing the virtual from the not real, the non-existent, the double invoiced, the fraudulent is a problem for paper, as recent expensive high profile frauds in trade and commodity finance have shown. A problem also of counting real beans versus virtual ones.

The continued use of paper-based transactions, cumbersome due diligence requirements for banks, and lack of adequate business information on borrower firms, especially SMEs, are key challenges in trade finance provision. Rapid developments in digitisation and automation should offer

Distinguishing the virtual from the not real, the non-existent, the double invoiced, the fraudulent is a problem for paper, as recent expensive high profile frauds in trade and commodity finance have shown. A problem also of counting real beans versus virtual ones.

promise in addressing these challenges.

A trade distribution head at a major trade bank told me, off the record, "I'm very optimistic on digital trade from a trade finance perspective. I think it's accelerating, regulations are changing and there will be focus on the business and it will be driving the industry and there will be efficiency gains." Nonetheless, he says while he is 'gung ho' about the prospects for trade, "The question is how do we accelerate digitisation, and not just in trade distribution but end to end. There are positive signs, especially with e-bills of lading (eBL), but there needs to be scale."

Positive signs on cargo, piecemeal elsewhere?

E-bills of lading are certainly getting a lot more discussion amid the crisis – the Digital Container Shipping Association (DCSA) has been pushing for eBL standardisation for cargo, and UN/CEFACT are all pursuing initiatives such as the UNCITRAL Model Law on Electronic Transferable Records (MLETR). EssDocs announced its partnership in India with Portall to deliver eBL in July and Bolero also notes a spike of interest in moving away from paper for trade. "The impact of COVID-19 on carriers, corporates and banks has shown that paper processes and business continuity planning scenarios can fail and COVID-19 is not going away soon. Thus meaning that traditional and contemporary trade is embracing the use of e-documents for anything from open account trade up to DLT Marco Polo transactions," a spokesperson from Bolero said.

The need to step up actual digitisation as a way of facilitating and financing trade is pressing. Financing cross border trade and working capital via supply chain finance (SCF) is also underpinned by digitisation (specifically of invoices, and electronic developments in a/r and a/p and integration with ERP systems help facilitate working capital management digitally). Some lessons

from this space can be applied in other areas of trade digitisation.

Acceleration of digitisation on blockchain platforms is proceeding amid the crisis, but it is sectoral and a bit stop/start. Says one trade blockchain provider, off the record, "On blockchain we've not had many new projects into 2021 since the start of the crisis, and some, such as in aviation have been dead in the water, and auto has been tough. But we have had fulfilment on project commitments to year end. Another interesting trend has been in agriculture blockchain where a lot of companies that spent a lot digitising quickly and badly are now having to unpick what they did."

Standards are stumbling blocks

Regulation, collaboration and scalability will continue to be important to underpin progress. But standardisation is key. As Joel Schrevens, global solutions director at China Systems asks: "Considering that trade is a business that is heavily driven by the exchange of documents is it realistic to expect that trade DLT platforms are able to get global cross-industry traction without fundamentally solving the requirement or having at least a clear roadmap to enable portability of digital original documents between existing trade processing infrastructure and their own platform? While APIs can resolve specific integration challenges, considering the number of parties involved, a more fundamental approach is required to solve the challenge for trade documents."

The key to mass adoption, and not just some efficiency gains from 'one by one partner integration' is fundamental digitisation of standardised documentation, or at the least a clear plan to achieve that. Schrevens, for one, is excited that the technology for standardisation and secure exchange of digital original documents exists today, that there has been progress with the cargo industry and that lessons can be learned from the e-invoicing space. But, he cautions. "At this point, I do not see a coordinated cross-industry initiative to create standards for a core trade dataset with a customer-centric mindset, with the customer being the originator of trade transactions and managing their OTC/P2P processes mainly on the basis of purchase order (PO)/ invoice related activities."

He argues that a holistic approach should be taken to standardise trade data (starting with the source data stored in POs and invoices, which subsequently flows into other documents, such as BL, CMR, AWB, CIM, CO, B/E, P/N, insurance documents etc. as a result of a logistical, insurance or financial service), bridging physical and financial supply chain services. That requires the involvement of financial institutions, the transport industry and representation from trade originators. It's a big ask, but surely not insurmountable. Shouldn't a body such as SWIFT be at the heart of the integration?

"Today banks look at SWIFT for financial messaging, but the reality is that SWIFT Trade messaging, while definitely automating parts of the trade process, has been and today still is disconnected from standardisation activities in the logistical and trade origination world. The added value of moving current trade processes to a different technology platform, without achieving interoperability and portability of trade documents and data between systems used for trade origination, logistics and settlement, will be relatively low. Whether it is SWIFT or another organisation, without a holistic approach or at least a roadmap with clear milestones for this challenging journey, to convince those standing on the side lines, any progress is likely to be based on piecemeal developments, only serving the few, further increasing the digital divide and putting a block on adoption," Schrevens says.

Regulation, collaboration and scalability will continue to be important to underpin progress. But standardisation is key.

Are banks picking up the pace on paper?

What about the banks financing trade? In the ICC Global Survey on Trade Finance 2020 released at the end of July, 54% of the 346 bank respondents said emerging technology, digital trade and online trade platforms were an immediate priority over the next year. Some 70% also said traditional trade finance was a priority in the same period. The report went further into digitisation. Although there's been progress, the results weren't stellar and documentary transactions are rarely wholly digitised.

In the three areas looked at, issuance/ advising, settlement/financing and document verification, the latter remained the most paper-dominated area. That's discouraging.

It's important to remember that, according to the ICC survey, 90% of trade finance is provided by just 13 banks. The estimated global value of trade finance transactions processed by respondents is $9 trillion. The top three to five trade finance banks likely account for a very high proportion of that figure.

Anecdotally speaking, it is players in those top trade finance banks (let's call them HSBC, Citi, StanChart, DBS for starters) are the most positive about digitisation. Nonetheless, the survey says while 83% of global banks supposedly have a digital strategy, only 46% of local banks report having one. This highlights a growing gap between players of different scale and reach.

Compliance was seen as the biggest obstacle for banks' growth in financing international trade (AML/ KYC requirements 63% and counter-terrorism and international sanctions regulation and compliance 61%). Compliance may be a major headache, but it is also stopping the bad hats. Nonetheless, for smaller players, compliance is an onerous burden.

One development at the end of August that flew under the wire was encouraging, the ability to embed Legal Entity Identifiers (LEIs) in digital certificates under ISO standards. LEIs should help with identifying legitimate players digitally. Another development was a trade digitisation memorandum of intent first signed at Davos (by banks, the ICC insurers and traders) but then developed at the end of SIBOS in early October. Through this, Singapore's INFOCOMM and SWIFT intend to leverage the SWIFT network to encourage the use of the TradeTrust interoperability framework. ITFA (International Trade and Forfaiting Association) too has been working hard on the DNI, digital negotiable instruments initiative, all making positive progress.

Digitising the horse: Back to the magic beans

Fundamental questions remain as to whether digitisation is changing the game, or just transposing Henry Ford's proverbial faster horse onto outdated instruments – new ways of doing the same old thing. Should LCs become embedded into the logistics process, so the financing is included in the purchase and bundled into the transportation process? That's a discussion for another day. But in the meantime, the transition to digital trade remains an imperative that is still in search of coherent and consistent standards. I'm optimistic there's a way to get through – but complicated approaches are not helpful. Who knew a year ago that Zoom would 'win'?

Economist John Maynard Keynes speculated in the commodities futures market. There is an old story he took delivery of actual real beans and had to store them in King's College Cambridge. My undergraduate memory doesn't serve well, as when I checked it was Argentinian wheat in 1936, which he didn't actually store in the chapel crypt as it was too small, so he used the ruse to object to its quality so he didn't actually receive it, but I'll stick with the apocryphal beans as it suits my imaginings better.

Arguably Keynes's reflationary policies helped move the global economy out of the slump of the great depression (but not directly by buying wheat or beans), and yes, I know it's a big argument that's kept post war economists in business. Here's hoping the ICC's DSI – whose stated goal is to 'work towards the ambitious aim of establishing a globally harmonised, digitised trade environment' – can help with an answer to standards to support effective digitisation. ■

This is an updated version of an article that first appeared on TXF (https://www.txfnews.com/News/Article/7045/Time-to-double-down-on-trade-digitisation-On-counting-virtual-beans).

Fundamental questions remain as to whether digitisation is changing the game, or just transposing Henry Ford's proverbial faster horse onto outdated instruments – new ways of doing the same old thing.

Digitalisation in trade: The situation report

John Bugeja, Managing Director at Trade Advisory Network explores the current landscape on trade digitisation in depth. Where are we now, why is digitisation necessary and where are we heading?

What Is digitalisation?

Digitalisation is the use of electronic records to drive processes through the use of interfaces or through integration. The precursor to digitalisation was the use of telex and cable to initiate transactions in place of paper-based communications between banks. This began to change in 1973 when SWIFT was formed by 239 banks from 15 countries. In order to improve efficiency, eliminate re-keying errors and achieve 'straight through processing' functionality, banks quickly started to build interfaces connecting their processing platforms to their SWIFT gateways.

The challenge and the business benefits

The challenge for finance providers now is to use data produced in corporate supply chains to drive financial interventions. Currently, much of this data is printed to paper and then presented to banks who then enter the data into their own systems to create new electronic records used in transaction processing. At Trade Advisory Network, we are frequently approached by Fintechs who purport to have solved some element of this challenge. Our first question is typically: 'what problem are you trying to solve?' We can categorise the potential business benefits under a number of headings:


John Bugeja

1) Efficiency gains

This is a legitimate, though somewhat bank-centric, business benefit. By avoiding the use of paper, banks can streamline operations processing, speed up transaction execution, minimise delays and reduce costs. Paper documents generate huge costs. They are printed and amended multiple times, each time adding cost and creating a version-control challenge. They are moved from one party to another – often several times and across several continents. The have to be stored, indexed, retrieved and archived. Certain paper documents confer rights upon the holder and are, as a consequence, 'valuable' in their own right (e.g. negotiable payment instruments and documents of title) necessitating further costly measures to protect against loss and fraud.

2) Increased credit availability

Traditional documentary trade finance is seen as 'short term, self-liquidating and secure' resulting in increased credit appetite

Traditional documentary trade finance is seen as 'short term, self-liquidating and secure' resulting in increased credit appetite relative to unstructured, unsecured debt. Its use has, however, been in long term decline as trading parties have increasingly favoured open account settlement.

relative to unstructured, unsecured debt. Its use has, however, been in long term decline as trading parties have increasingly favoured open account settlement.

Digitalisation promises to deliver the benefits of documentary trade finance. If paper documents were to be replaced with electronic records and the data contained therein used to drive automated decision-making technology, it would be possible to replicate the benefits of documentary trade finance (i.e. visibility, control and security) without the labour and cost associated with paper.

In addition, through the use of digital marketplaces, secondary markets and distribution channels, the available liquidity pool could be broadened, benefiting both borrower and traditional lenders with capital or funding constraints.

3) Innovation

Digitalisation will facilitate innovation. The aim should not be to merely digitalise existing processes, but to find new, more efficient ways to meet clients' financing and risk mitigation needs, exploiting the functionality that digitalisation brings. For example, a digital negotiable payment instrument could be integrated into a paperless workflow to create a more effective insurance backed finance solution.

4) Sustainability

The movement of goods across the globe between producers, manufacturers, distributors and retailers in different countries is bound involve a significant carbon footprint.

Times are, however, changing. In addition to heightened awareness of the impact of trade on climate change, political factors are also challenging the status quo. Increased protectionism is eroding low labour cost benefits due to the imposition of tariffs and non-tariff barriers, as is the increased use of robotics in manufacturing, further eroding any labour cost advantage.

These factors appear to be driving a move towards on-shoring and near-shoring. It is probably naïve to suggest that the changing trends in global trade are being driven primarily by environmental concerns, but the effect should nevertheless be beneficial in terms of carbon footprint.

Trade finance is also a carbon footprint offender. The documentation associated with trade is often excessive with the same data being repeated in multiple different paper documents. The environmental impact is huge. At every stage in the process, there are carbon implications, including:

- use of paper
- movement of paper between parties on a global basis
- storage of paper
- disposal of paper

Digitalisation offers the potential to eliminate these carbon-heavy processes as electronic records can easily be created and transferred between parties.

5) Fraud prevention (and AML, WMD and non-proliferation compliance)

Fraudulent paper documents are very easy to create and very difficult to spot. In recent years fraud has become a major cause of loss in trade finance, particularly in respect of commodities trading where fraudulent bills of lading and warehouse receipts have been used to secure financing. Fraud prevention often goes hand in hand with regulatory compliance, so banks are at risk of more than just incurring a loss.

Digitalisation may offer certain benefits relative to paper documents in terms of fraud protection, but caution is required at this stage given the nature of electronic records.

6) Business continuity

The disadvantages of being paper dependent have been thrown into sharp

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focus by the global pandemic. Many banks have found it impossible to transport paper documents efficiently due to resourcing challenges faced by couriers. Document checking has proven more difficult and time-consuming due to the move to working from home. The combined effect has been delays in financing and settlement of trade transactions, causing further financial stress for trading companies. The need to digitalise trade has now become a top priority business continuity issue.

The problem with electronic records

A digital signature appended to an electronic record is similar to a 'wet signature' on a paper document. Common/civil law in most jurisdictions generally recognises that a digital signature reflects the signatory's intention to be bound by the content of the record.

A conventional electronic record can, however, be replicated on multiple systems and devices so the concepts of 'originality' and 'possession' are not accommodated, even if it is digitally signed. This is a problem where possession of an original document is required, as is the case in trade finance with negotiable instruments and documents of title. In addition, there is nothing in a conventional electronic record that can prove that the content has not been changed following application of the digital signature.

The Fintech industry has developed two approaches to addressing the problems inherent in electronic records: closed user groups and digital original documents.

Closed User Group Solutions

Electronic bills of lading

The first example in trade was probably Bolero which started in the mid-1990s and continues today. Bolero delivers electronic bills of lading whereby the title to the goods is recorded in a title registry. Users agree to abide by a rulebook, making transfer of title subject to contract law rather than maritime law. This approach avoids the problem of originality and possession and is a good mitigant against fraud. The disadvantage with this model is, of course, that legal enforceability only applies to users that have signed up to the rulebook.

There are now several competitors to Bolero giving users greater choice and promoting greater acceptance of the concept. Unfortunately, the proliferation of such solutions, each using its own technology and with its own rulebook, also makes it more difficult to achieve critical mass using a common legal and technological framework.

Digital marketplaces and auction sites

The emergence of platform-based marketplaces and auction sites through which funders can be matched with borrowers is a more recent development. These sites are also membership based, restricting access to parties that have signed up. The traded assets are almost invariably receivables so, behind the scenes, the traditional process of assignment has to take place.

The need to digitalise trade has now become a top priority business continuity issue.

These platforms would benefit from the use of negotiable instruments, such as bills of exchange or promissory notes, as they are unconditional, irrevocable and independent and are tradable in their own right, making them ideal for both the primary and the secondary markets. The independence of these instruments is key as the acceptor cannot use contractual non-performance as a defence against non-payment. In addition, common/civil law in most jurisdictions provides clear rules for transferring the title rights and benefits from one holder to another by endorsement and delivery – known as negotiation.

A conventional electronic record cannot, however, perform the function of a negotiable instrument as the concepts of originality and possession are central to the latter's enforceability.

Consortia

These are also membership-based solutions with users signing up to a set of rules governing their rights and obligations. The challenge, as with other closed user group solutions, is that each consortium is effectively a digital island where payment obligations are only enforceable amongst members.

Digital original documents

The principle here is to replicate the functionality of paper documents in digital form, including the ability to:

- distinguish between an original and a copy
- transfer ownership (and associated title rights and benefits) by delivery
- provide assurance that the content has not been tampered with in any way

The functional specification for the use of digital original documents as payment undertakings has been defined by ITFA (the International Trade and Forfaiting Association) through their DNI (Digital Negotiable Instruments) initiative.

The technology to deliver the required functionality, branded 'trace:original' has been developed by Enigio Time and is available without the need to join a closed user group. The solution is open to all whether they are members of a consortium or not. Indeed, trace:original documents can act as a vehicle for interoperability between consortia.

ITFA and the ICC are leading the effort to ensure legal enforceability of digital bills of exchange in key markets. The obstacle in the UK, for example, is the current ruling regarding possession of an intangible. As transfer of possession (by endorsement and delivery) is fundamental to the negotiability of a bill of exchange, clarity on this point is essential. The consultative process is in progress and a statutory amendment in anticipated within 12 – 18 months. In the meantime, an interim solution has been defined by ITFA allowing electronic payment undertakings with similar practical functionality to be created using this new technology.

What next?

Though closed user group solutions have the potential to deliver the benefits of digitalisation, it will be difficult to achieve critical mass due to the lack of common technology standards coupled with the inability of conventional electronic records to replicate the functionality of paper documents in respect of originality and possession. Reliance on registries or databases, whether centrally held or distributed, limits the scope for adoption to members of a common club.

Though closed user group solutions have the potential to deliver the benefits of digitalisation, it will be difficult to achieve critical mass due to the lack of common technology standards coupled with the inability of conventional electronic records to replicate the functionality of paper documents in respect of originality and possession.

The need to develop technology standards that facilitate interoperability has been recognised and is the subject of the ICC's Digital Standards Initiative (DSI). It is felt that ITFA's DNI initiative could become a key enabler in support of the ICC's DSI.

The ICC is also developing Uniform Rules for Digital Trade Transactions (URDTT) to complement their existing rules governing letters of credit, collections, forfaiting and guarantees.

Overall, there is room for optimism regarding the application of digitalisation and the delivery of significant business and environmental benefits. Certainly, we need the regulators to be visibly supportive, but the real drive must come from the practitioners. ■

There is room for optimism regarding the application of digitalisation and the delivery of significant business and environmental benefits. Certainly, we need the regulators to be visibly supportive, but the real drive must come from the practitioners.

ECA support for software exports: An analysis

By Didem Erdoğan, Project Loans and Trade Finance Specialist at Turk Exim

According to the OECD, software refers to 'programs, procedures and data associated with the operation of a computer system'. However, given the impact of digitalisation, globalisation, and the concept of Industry 4.0, the software sector is playing such an important role in our daily lives that all definitions have become insufficient. Every item used is made 'smart' thanks to software, and the success of software exports has had a big economic impact.

The revenue of the global software market amounted to $456 billion in 2018[1]. The ever-marching spread of the internet, the ease of storage, streaming and processing services have all contributed to the further development of the software industry and, in terms of trade volumes, software trade is significantly underestimated because it is usually based on the value of physical goods rather than content and is often bundled with computer hardware. In trade statistics, while digitally delivered software is not generally measured at all, software and copyright trade are rarely taken into account[2]. However, despite all these obstacles, while the share of telecommunications services has declined, computer services receipts more than doubled in value, increasing their share of Information and Communication Technologies (ICT) trade from 65% to 78%. Computer services, including database development, data processing and software design, have benefitted from technological changes such as an increase in businesses moving their IT operations to cloud computing[3] (see Figure 1).


Didem Erdoğan

Moreover, the COVID-19 pandemic has caused an unprecedented surge in demand for software amid global lockdowns. This has caused the software market to expand while

Figure 1

Source: WTO-UNCTAD-ICT estimates[4].

other industries dwindle. According to the *Financial Times*[5], the tech-heavy Nasdaq 100 rose 15% in April, and during the lockdown period, companies like Amazon and Netflix were clear winners since their shares both increased by about 30% in the early months of the crisis. That's not to forget the increase in the gaming industries too. Aside from the new virtual reality releases, console and PC products are skyrocketing.

Surveying exporter needs and ECA support

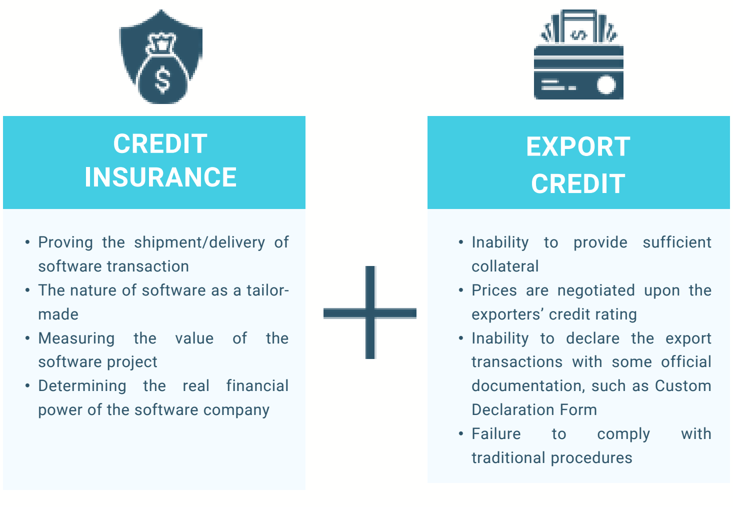
In order to understand to what extent such an important sector is supported by ECAs, whose main mission is to support their national exporters in order to stimulate trade volumes in their favour[6], research was conducted among 51 ECAs/development banks around the world and another survey was conducted to accurately identify the needs of software exporters in Turkey, in which 71 current/potential software exporters participated.

According to the latter survey, 67% of software exporters would like to benefit from credit insurance while 77% of them prefer exporter credits to buyer credits, and they want to use these credits in the medium to long term (12-36 months) and also starting from the pre-shipment period. Furthermore, software exporters indicate their interest in acquiring credits for their staff expenses, research and development expenses, promotion and marketing expenses, respectively.

With regards to the ECA/development banks' survey, support of ECAs for software export is very limited and this sector is generally evaluated under general export credit or credit insurance programmes. In this study, responses collected from BNDES (Brazil), EDC (Canada), ECGC (India), Eximbank of India (India), K-sure (South Korea) and US Ex-Im (the US) were taken as sample and highlighted due to their applicability to the software sector. Among 51 ECAs, only ECGC has a particular programme dedicated to software exports. The programme includes a special cooperation with the Reserve Bank of India. Most importantly, they solved the problem of software trade valuation by introducing a SOFTEX Form. Interestingly, Eximbank of India has also a special programme for software which is not for exports, but for

According to the *Financial Times*[5], the tech-heavy Nasdaq 100 rose 15% in April, and during the lockdown period, companies like Amazon and Netflix were clear winners since their shares both increased by about 30% in the early months of the crisis.

Figure 2



the establishment of software training institutions. For US EXIM and EDC, a loss in return fees and contract cancellation is not covered. As software projects are generally tailormade, this situation creates a problem for exporters.

Moreover, in the case of BNDES, due to the evidence of export documents requested in the pre-shipment credit line, software companies often choose other types of local financing to access the working capital needed, even if this way is more expensive. In this context, the difficulties for software export support are summarised as follows.

Whether related to credit or insurance, it is obvious that ECAs or development banks cannot support software export trade sufficiently. The barriers for supporting software by ECAs around the world stem from one fundamental difference, there are no procedures that are appropriate for the different nature of software as an export item (see Figure 2).

Suggestions to improve support

In the era of knowledge, software trade does not receive the support it deserves when considering its importance for digitalisation, and the 'new normal' order for the world. In order to increase software export volumes with the help of more ECA support, structural changes in international trade are needed.

Accurate measurement

In this regard, starting with the 'you cannot manage what you cannot measure' motto,

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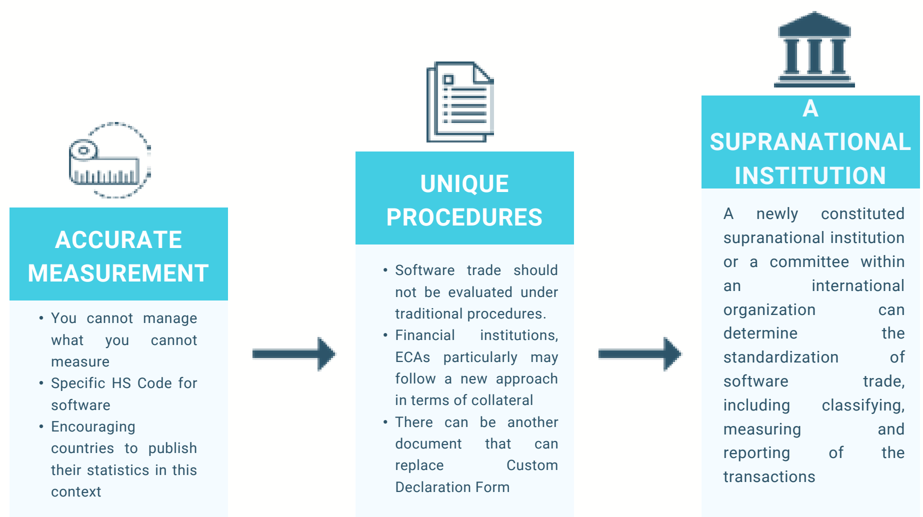
initially, software trade should be numerically determined. Although international trade in software goods and services is reaching higher volumes every year, these volumes are actually underestimated due to the reasons explained. One thought is the introduction of specific Harmonised System (HS) codes, if incorporated into the sector by the World Customs Organization or a similar body may provide the measure required for this industry. Countries could be encouraged to publish their official statistics in this way (see Figure 3).

In order to increase software export support, a non-traditional approach can be used by ECAs considering the dynamic and intangible nature of software. For example,

Figure 3



ECAs could offer their own collateral to software exporters and in terms of valuation as in the case of ECGC, A SOFTEX form could be introduced and there could be another document that could replace the Custom Declaration Form.

Unique procedures

Additionally, with reference to the survey results, personnel expenditures are one of the most important reasons why software exporters want to use credit. According to the information collected from the 51 ECAs, only K-sure paid attention to this demand with its 'Service Export Credit Insurance Programme', even if it is not a credit programme. Another conclusion is that special loan programmes should be developed for software exporters for the pre-shipment period and the medium and long term. With regards to the lack of collateral for software export credits, ECAs may follow a new approach, such as creating their own warranty with the help of insurance policies or assessing software companies based on their licensing values, etc.

Supranational institution

The last suggestion actually involves the two previous suggestions and relates to the establishment of a supranational institution that determines the standardisation processes of software trade including classification. This institution (or committee) could be in charge of every detail of software trade, such as classifying, measuring, and reporting respectively.

Supporting 'software first'

Last but not least, with the latest transformation all over the world, the importance of software and software trade has been brought to the fore. Even when exports of various physical products and services such as tourism and transportation became almost impossible, software exports were not affected and even increased their growth momentum with the introduction of new products.

However, due to reasons that mainly emerge from the nature of software, software exports are not supported at a level comparable with other sectors. Therefore, this sector lacks sufficient direct or indirect support and most software exporters are forced to find their own solutions. In this context, within the context of growing international software trade, some steps should be taken, especially by the ECAs whose main goal is to contribute to their national export volumes.

As a result, in today's 'software first'[7] world, it is necessary first to establish standardisation in classification and measurement methods and then to introduce new solutions in line with the needs of software exporters so that ECAs would be able easily to support software exports, and thanks to this success, many countries would benefit from conversion to the information society and increasing world trade volumes. ■

Notes

1 Statista. (2020, October 20). Statistics and Market Data on Software. Retrieved August 08, 2020, from https://www.statista.com/markets/418/topic/484/software/

2 OECD (2002). OECD Information Technology Outlook ICTs And The Information Economy.

3 OECD (2020, October 25). Retrieved from https://stats.oecd.org/glossary/detail.asp?ID=4905

4 WTO (2019) World Trade Statistical Review. Retrieved from https://www.wto.org/english/res_e/statis_e/wts2019_e/wts2019_e.pdf

5 Financial Times (2020, May1)

6 OECD. (2020). Export Credits. Retrieved from https://www.oecd.org/trade/topics/export-credits/

7 Tessler, Shirley, Barr, A., & Hanna, N. (2003). National Software Industry Development: Considerations for Government Planners. Retrieved December 10, 2019, from http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.601.766&rep=rep1&type=pdf

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Legal perspectives on blockchain technologies for financing trade

By Michael Morris, Partner, Clyde & Co, Dubai and Emma Fidler, Associate, Trade and Corporate Finance, Clyde & Co

This year has brought unprecedented challenges to industry which have been felt in every corner of the globe. The full financial impact of the COVID-19 pandemic remains to be seen. What is clear, however, is that there has been a seismic shift in the way that businesses operate and, as a result, in the strategies and business development models employed to navigate this uncertainty and drive organic growth. Digitalisation will play a crucial role in realising this objective, both in terms of unlocking capital through taking advantage of cost-savings and in preventing the risk of fraud.

Here we examine how blockchain and distributed ledger technologies (DLT) can be successfully utilised to prevent instances of trade finance fraud and, more generally, their place within the current trade finance infrastructure as a document verification tool.

Trade finance fraud

The prevalence of fraud in trade finance remains a concerning issue to all stakeholders, including traders, banks, financiers and credit insurers. Every year individual markets around the world are hit with a least one multi-million dollar fraud and even more during an economic downturn. Just look at the issues currently being seen in the commodities trading sector in Singapore.

Michael Morris

Emma Fidler

Unfortunately, the current trading infrastructure lends itself to exploitation by fraudsters, deploying a number of different tactics for illegitimate purposes. The investigation of suspected fraud is a cumbersome process and often comes at significant expense to the insurer.

The most common instances of fraud which lead to considerable loss, and are often most difficult to detect, can be summarised as follows:

a) 'Double discounting', where the trader discounts the same invoice with two or more financial institutions

b) Traders issuing multiple invoices for the same transaction, inflating the price and obtaining separate financing each time

c) Fake trades or 'fresh air' invoicing in circumstances where the documentation is completely falsified and there is no shipment

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or sales of goods at all.

The potential for fraudulent activity and problems encountered arise primarily due to the following factors:

(i) participants, and especially banks in this context, place a great deal of reliance on physical, hard-copy documents which derive special legal status (such as letters of credit or bills of lading)

(ii) such documents can be easily forged or tampered with

(iii) participants are usually based in different jurisdictions spanning continents, time zones and cultures, each using different systems and platforms which often impedes communication. The existing methods and tools used in any given finance transaction are outmoded when considered against the current climate in which traders operate (and especially in a post-COVID-19 environment where increasing reliance is placed on electronic communications to conclude transactions).

How can blockchain address these issues?

The inherent qualities and characteristics of blockchain and DLT mean that it is well placed to address, and go some way in preventing, attempts by fraudsters to 'hack' the existing systems in place.

The 'de-centralised network' and peer-to-peer transmission

One key attribute of DLT which has the potential to radically transform the current processes and procedures of trade finance is the nature of the network, namely, each party participating on a blockchain platform has access to the entire database and its complete history. No single party controls the data or information, and each participant can verify the records of every transaction directly (without recourse to an intermediary). Every transaction and its associated value are visible to anyone with access to the system. The acceptance and verification of such records by each user on the platform creates consensus.

The requirement for consensus ultimately reduces the responsibility of any given participant to verify documents and detect fraudulent entries. The very structure of the platform increases overall transparency and lends legitimacy to data entries which would ultimately prevent fraudsters from, for instance, issuing several invoices in respect of the same shipment.

Irreversibility of records

Once a transaction and its documents are created and transferred via a DLT platform and the ledgers are updated, the records cannot be changed. Each entry contains a unique 'hash' code, and the code for the previous data block which came before it, meaning that it is almost impossible for fraudsters to tamper with any of the data entries, since to do so would invalidate the other blocks in the chain.

To prevent hackers from retrospectively changing the data in the block and regenerating the hash IDs for each block in the chain, various security mechanisms (such as the 'proof-of-work' functionality) are built in to the DLT network, which effectively slow down the creation of new data blocks. This, combined with the nature of peer-to-peer transmission, means that it would be almost impossible for participants to successfully defraud the system.

The execution of certain types of contracts, which would traditionally have required parties to sign in person, have left lawyers grappling with the need to find legal (and, perhaps more importantly, practical) solutions to these issues. The significance of this hurdle and the degree of collaboration required to overcome it cannot be overstated. Before governments can be convinced to support this effort, industry must agree on the best practices and standards of technology across international borders.

Blockchain and the legal landscape

Readers will be familiar with the plethora of complex maritime law, regulations and commercial codes which give rights of ownership between parties and across jurisdictions. Such laws and international conventions have been developed over decades (even centuries) of trade, and plainly many of these laws and regulations will not be suitable for a new digitally-defined, automated and decentralised network utilising DLT.

The global impact of the COVID-19 pandemic has recently brought questions of legal validity and status in e-commerce to the fore. For example, the execution of certain types of contracts, which would traditionally have required parties to sign in person, have left lawyers grappling with the need to find legal (and, perhaps more importantly, practical) solutions to these issues. The significance of this hurdle and the degree of collaboration required to overcome it cannot be overstated. Before governments can be convinced to support this effort, the industry must agree on the best practices and standards of technology across international borders.

Many questions surrounding COVID-19's impact have been raised. As the pandemic has highlighted the gaps in legal validity of digital transactions what practical solutions to this have been attempted? To what extent has the pure necessity of the current situation already gone some way to driving an industry/legal consensus or are, from a legal point of view, these kind of digital contract execution processes (without signatures) suffering from not really having been 'tested' in law?

Generally speaking, in English law, electronic signatures are capable of being used if the authorised signatory intends to authenticate the document in this way. The biggest challenge however has been in trying to find solutions for the execution of documents which would typically require both parties to meet in person (and, in the case of deeds, for example, sign in the presence of a witness).

The Law Society in the UK recently published instructive guidance[1] on its position on the use of virtual execution and e-signatures during the pandemic, which sets out the various options and recommended approach for each contractual arrangement based on any customary or statutory requirements. As each situation is different (and the formalities required for valid execution vary on a case-by-case basis), establishing industry-wide consensus is difficult at this early stage given that many of the new processes adopted remain 'untested'. It is certainly true that COVID-19 has brought these issues (digital execution processes) to the forefront of lawyers' minds and it will be interesting to see how technologies (and the legal position) develops over time.

As with any new technology which promises to transform the existing systems and structures which underpin our daily lives, it is usual to expect that such radical advancement would be met with some suspicion. The potential for blockchain and DLT to streamline the trade finance process and reduce instances of fraud are self-evident, but there are inevitably more hurdles to overcome.

The future of blockchain

As with any new technology which promises to transform the existing systems and structures which underpin our daily lives, it is usual to expect that such radical advancement would be met with some suspicion. The potential for blockchain and DLT to streamline the trade finance process and reduce instances of fraud are self-evident, but there are inevitably more hurdles to overcome. Collaboration between organisations, financiers, and other stakeholders will be crucial to its success as a long term solution. ■

Note

1 https://www.lawsociety.org.uk/en/topics/coronavirus/our-position-on-the-use-of-virtual-execution-and-e-signature-during-the-coronavirus-covid19-pandemic

Machine Learning explored: Can ECAs benefit?

By Dr Simone Krummaker, Senior Lecturer at the Faculty of Actuarial Science and Insurance at Cass Business School and Professor Dr Mathias Bärtl at Offenberg University

What does Machine Learning offer to help ECAs predict claims? Simone Krummaker and Mathias Bärtl look at the data in depth.

Berne Union members have done well in avoiding claims for a long while, by and large. From 2005 to 2018, the claims-to-exposure ratio in medium- and long-term (MLT) insurance was, on average, in the order of just 0.4%. However, within that, there has been a huge variety in how hard individual Export Credit Agencies (ECAs) have been hit (see Figure 1).

Claims prediction remains as critical a challenge for ECAs as it does for any insurer. Not only do claims affect the capacity to underwrite further business, they may also have an impact on premiums. In order to predict claims and related reserves, private insurers have been using a range of deterministic and stochastic methods, such as the Chain Ladder or Bornhuetter-Ferguson method, (Baudry and Robert 2019), while ECAs have focused on more traditional approaches. But regulatory developments as well as a growing uncertainty in export credit risks increase the need for the application of more sophisticated methods for both private and public providers (England and Verall 2002; Verall, Hossjer and Bjorkwall 2012). Therefore, Machine Learning (ML) may come with benefits that have not been fully exploited by traditional claim prediction methods (Thesmar et al. 2019).

Dr Simone Krummaker

Dr Mathias Bärtl

The ML exploration study

ECAs provide data to the Berne Union twice a year as a mechanism to share their business information. This joint effort has resulted in the creation of the most extensive collection of structured data on export credit insurance and finance (Auboin and Engemann 2014). So far, the database has been made available to support two scientific studies which analysed the impact of trade credit and trade finance availability on trade (Auboin and Engemann 2014; Korinek, Le Cocguic and Sourdin 2010). In 2019, a third study was undertaken in cooperation between the Berne Union Secretariat and the Institute for Trade and Innovation (IfTI). This study targeted MLT claims (excluding recoveries) of the 33 largest ECAs and investigated to what extent ML can serve to exploit the Berne Union database beyond its primary purpose.

ML in a nutshell

Supervised ML algorithms search available data with the aim to uncover patterns that allow a prediction of a target attribute, for example, the volume of expected claims, based on available input attributes (Varian 2014) such as the conditions surrounding a given contract. In a way, this can be likened to mimicking the experience of a long-serving underwriter who has seen hundreds of contracts including the events leading up to them, and has developed a pretty good instinct about whether or not a certain transaction is going to go well.

The scientific literature suggests a wide range of approaches to conduct this task but provides no guidance on how to link a particular problem to the most suitable ML technique (Kuhn and Johnson 2013; Wanke and Barros 2016). Therefore, the study explored four common ML techniques, namely Decision Trees (DT), Random Forests (RF), Neural Networks (NN) and Probabilistic Neural Networks (PNN), and compared their ability to accurately predict export credit insurance claims.

Preparing the ground for ML

A popular fantasy sees ML as some electronic hyperintelligence that can be unleashed onto whatever data is available to come back with smart insights. This is far from the truth.

First, a careful preparation of the data is paramount to the development of meaningful models. For example, the aggregate exposure of all ECAs to a given export destination country might be a relevant factor in determining the country's likelihood to incur claims. However, no ML algorithm comes up with that proposition all by itself. Prior to any ML exercise the algorithm needs to be able to access potentially relevant information at the right time in the right format. In total, we derived 25 attributes on ECAs and destinations to indicate their size, general development, business diversification and claims history.

Secondly, all data needs to be separated into sets for training, validation and testing. It is widely known that ML algorithms can overfit, meaning that they model the training data well but perform poorly when confronted with new data. This can be countered by using the training set for building the model, and a validation set to assess the model's performance (Kuhn and Johnson 2013; Mullainathan and Spiess 2017).

In addition, a range of parameters are controlled externally, such as the number of branches a DT should be allowed to grow, or whether training should be based on an amount of data that is large (which can take a long time but might be more precise) or small (which is faster but might miss

Common Machine Learning techniques explained

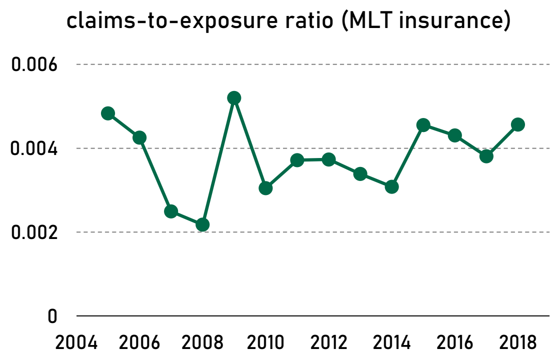
Decision Tree (DT): DT algorithms search all available input attributes and select the one which, at an optimal split value, separates the data so that their target attribute distributions diverge as much as possible from one another.

Random Forests (RF): RF consist of many DT, which all have been developed based on randomly selected subsets of all training data. An RF's prediction for new data is the majority vote of each of these DT's individual predictions for the data.

Neural Networks (NN): NN consist of layers of so-called neurons. Neurons in the input layer pick up input attribute values and apply an activation function to calculate a 'signal' value as output. The output is forwarded to the neurons in the subsequent layer, which each combine all inputs they receive and, again, convert the results into a signal to be forwarded to the next layer and so on. In prediction, the learned rules are applied to new data, and the resulting output conditions are used as prediction values.

Probabilistic Neural Networks (PNN): PNN are a modification of NN. They replace the traditionally sigmoid activation functions with statistically derived exponential functions, which satisfy certain additional optimality criteria founded in Bayesian Decision Theory.

Figure 1:
2005 – 2018 Claims-to-exposure ratio for MLT Business



Source: Berne Union data

important patterns). Therefore, we used data from 2007 to 2017 to train and validate a total of 47,520 models to reflect a range of potential variations. From those, we selected the best models and exposed them to 2018 data to test their ability to predict claims with three different levels of precision:

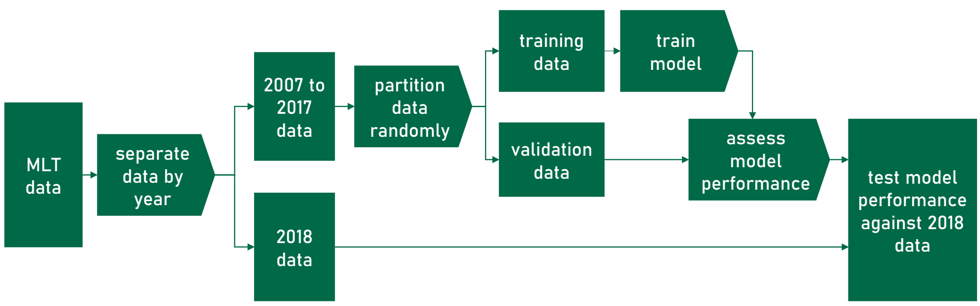
- 'Claims YES/NO': A prediction of whether or not a given export finance condition will incur claims as a simple yes/no decision.
- 'Ratio class': A prediction of the magnitude of claims, expressed as one of five predefined classes of claims-to-exposure ratios.
- 'Ratio': A prediction of an actual claims-to-exposure ratio as a single value.

Finally, we needed to decide how to measure the performance of ML models by comparing their predictions with reality. We calculated 'accuracy', the percentage of correctly predicted records, and 'Cohen's k', which adjusts the accuracy measure for correct predictions that would occur at random. Accuracy and Cohen's k do not work well for the claims-to-exposure ratio task, for which we calculated R2 instead. R2, the coefficient of determination, measures the percentage of variation in the dependent variable (in our case, the ratio) that is explained by the prediction model. However, while these measures allow for a comparison of the different techniques amongst each other, they do not answer the question 'is it worth it?'. In other words: would a much simpler approach yield equally good results? Therefore, we also created a simple benchmark (BM) that predicts claims based on a moving average of claims from previous years (see Figure 2).

How did ML perform?

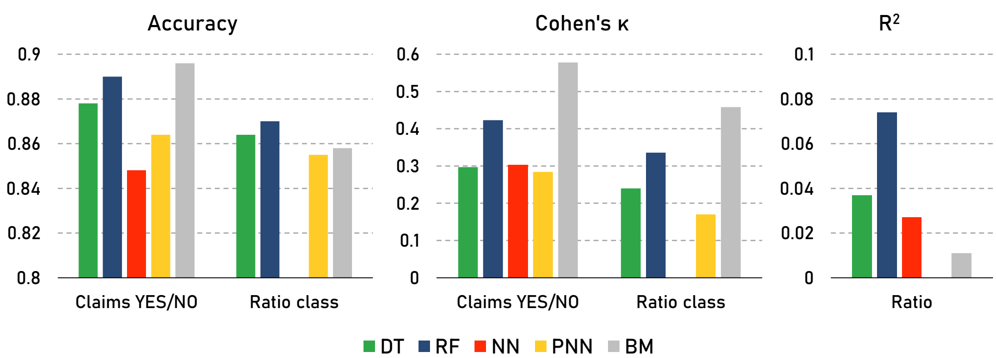
All ML techniques performed relatively well in predicting whether or not claims would be incurred, and, with limitations, in predicting their order of magnitude. No satisfactory results were achieved predicting actual

Figure 2: ML Exploration Method



Source: Berne Union data

Figure 3: ML Exploration Study Results



Source: Berne Union data

claims-to-exposure ratios. Consistent with previous studies, RF achieved the best results against all prediction tasks, and most reliably carried their validation performance forward to test performance. However, the simple benchmark heuristic often outperformed even the best ML models.

Does that mean they are useless? Not quite. Actually, assessing them against the BM is somewhat unfair. All ML models are generic and can make claim predictions for any ECA and destination, irrespective of whether or not the ECA has had business with that destination before. The BM, on the other hand, can only make forecasts for business relations that already exist. In conclusion, and viewed positively, ML models are capable of predicting the virtue of a business relationship (almost) as well as if it had materialized already, even if it has not (see Figure 3).

Conclusions and outlook

Most ECAs have an insurance history with many destinations. Therefore, they are well positioned to predict claims equally well or better than ML models by applying a simple heuristic. However, in cases where such a history does not exist, ML might well serve as a useful decision aid. The findings of our (and other) works recommend using the RF technique. Further research could abandon the requirement for ML models to be generic, and investigate ECA-specific time series of claims. This could add insight into how ML compares to traditional claims prediction approaches.

All ML techniques, and the benchmark even more so, performed poorly in predicting actual claims-to-exposure ratios. Finding the lowest performance against the most challenging task is unsurprising, but the huge lag behind the two other tasks is unusual. A more detailed inspection indicates that singular events of high claims prevented the creation of satisfactory prediction models; no technique was capable of capturing the conditions preceding their occurrence. However, irregular, exceptionally high claims are certainly of utmost interest to ECAs. A follow-up study could investigate the prediction of claims of specifically that type, although this may require more detailed data and the addition of external economic data sources such as OECD. ■

The full article, including descriptions of the ML techniques employed, is available at https://www.mdpi.com/2227-9091/8/1/22

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A popular fantasy sees Machine Learning as some electronic hyperintelligence that can be unleashed onto whatever data is available to come back with smart insights. This is far from the truth.

Working towards a commitment to net zero

By Astrid Bronswijk (Dutch Ministry of Finance), Ranya Gabriel (EDC), Thomas Hale (Oxford University) and Andreas Klasen (Offenburg University)

In the grip of battling an unrelenting pandemic and economic collapse, some of the world's biggest political and financial powers are setting out bold visions for a zero carbon economy that is healthier, cleaner, more resilient and more regenerative than our pre-COVID-19 systems.

In the last few months, the EU, China, Japan, South Africa, South Korea and the UK have pledged to reach net zero emissions by 2050 or 2060 (taking the world by surprise, in some cases). Meanwhile, the UN Net Zero Asset Owner Alliance has grown from 12 members with $2.4 trillion under management to 30 with $5 trillion in its first year alone. These governments and investors see the root causes behind the health and economic crisis we're now in –pollution, deforestation, drought, food scarcity, climate change impacts such as storms and wildfires – and are seeking to build resilience to future shocks. But, crucially, they also recognise the immense opportunity that comes with shifting investment from fossil fuels to industries that promote public health, nature conservation and regeneration and job creation.

The global economy is undoubtedly on a race to zero emissions by the middle of the century, and it's gaining momentum by the day (Figure 1). So what role can members of the Berne Union play in this 'race to zero'? We suggest it's time for the Berne Union, too, to join the pursuit of this zero emissions world.

To achieve global climate goals and build a more resilient economy, the rules and institutions of global economic governance must align around green economic transition. Financing for climate action related activities has become a priority in trade and development finance in recent years. Private climate finance provided on average $326 billion per year in 2017 and 2018, according to the Climate Policy Initiative. Public finance actors and intermediaries also play a crucial role regarding global financial flows for low carbon and climate-resilient development, committing an annual average of $253 billion in climate finance in 2017/2018. National development finance institutions (DFIs) such as the Dutch development bank FMO, Proparco in France and Germany's DEG were the largest groups among the public finance institutions. However, at the same time, much public finance continues to flow to incumbent, carbon-intensive sectors.

Astrid Bronswijk

Ranya Gabriel

The importance of climate finance for ECAs, Exim-Banks and PRIs

Green finance is also a major topic for export credit agencies (ECAs) and export-import banks (Exim-Banks). Although most organisations are demand-driven, climate action-related matters are priority themes for governments and official export finance instruments in many countries, and for their clients. Furthermore, dealing with the impact of climate change is increasingly important for public and private political risk insurers (PRIs). This includes scaling down support not consistent with the 2015 Paris Climate Change Agreement, a contribution to climate resilient development and low-carbon financing, and the support of low-carbon transformation related transactions.

ECAs, Exim-Banks and PRIs provide financing and risk mitigation tools addressing challenges inherent to a large part of low-carbon investment. Looking at selected Berne Union members, climate action is a key priority of Credendo's latest strategic plan. EKF in Denmark is one of the most important green finance institutions in the global export credit universe. In Germany, climate action has become an important area of activity in particular in 2020. CESCE recently developed a new framework regarding commitment to sustainability. UK Export Finance (UKEF) is a crucial element of the government's 'Green Finance Strategy'.

Canada and the Netherlands in detail

Over the past several years, Export Development Canada (EDC) has been very purposeful regarding sustainability and impact. Supporting cleantech companies in many sectors is a corporate priority. EDC is the largest provider of financial solutions for Canadian cleantech companies looking to expand internationally. With global interest in climate financing continuing to rise, EDC also issued its fifth green bond last year and provided C$100 million in climate finance in support of the Government of Canada's commitment to the UN Framework Convention on Climate Change, which

Thomas Hale

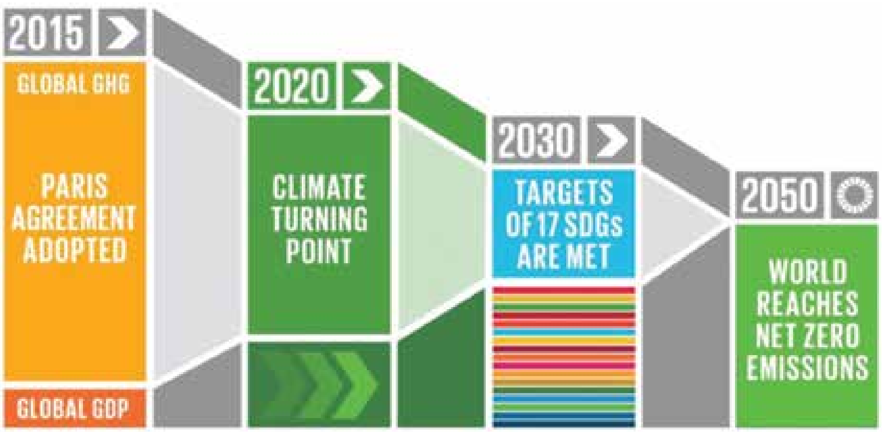
Andreas Klasen

focuses on EDC's support for low-carbon or carbon-resilient transactions in developing countries.

Furthermore, the Canadian ECA updated its environmental and social risk management framework, to ensure it serves customers in a progressive, responsible and sustainable way that meets the latest international standards. An important commitment towards the United Nations Sustainable Development Goals (SDGs) is EDC's standalone Climate Change Policy. Approved in 2018, it provides the principles and commitments that guide EDC's approach to the organisation's climate change-related risks and opportunities. With the new policy, EDC recognises that it can contribute to the aims of the Paris Agreement through the choices the ECA makes about the provision of financing and insurance, and through continued support of Canadian companies' innovation and transition as the country works towards achieving net zero emissions by 2050.

In the Netherlands, climate action has also become a crucial topic. The Dutch government is committed to tackling climate

Figure 1: The Road to Success



Source: Mission 2020

Despite progress on mobilising finance to support a global green deal, there is much more to do. Ultimately, we need to ensure all finance is 'net zero' finance.

issues on a global scale. The country's climate policy is mainly aimed at reducing greenhouse gas emissions. With an ambition to become one of the 'greenest' ECAs, Atradius Dutch State Business (Atradius DSB) has also started to put emphasis on climate financing. For example, the Dutch agency was involved in project financing of two large offshore wind farms in Taiwan last year. It also issued four financing policies to Climate Investor One, for instance, for a solar project in Southeast Asia and a hydropower plant in Uganda. The support is provided within the scope of the Paris Agreement targets.

Multidisciplinary teams were also set up at Atradius DSB last year to deal with corporate social responsibility themes. These include greening the business, reporting on green transactions within the portfolio of issued policies, and reporting on the impact of transactions on the SDGs. In addition, Atradius DSB developed a green label methodology in 2019 to determine whether a transaction meets the criteria to be labelled as 'green'. The purpose is to map out how green the export credit insurance portfolio is. As shown in Figure 2, transactions are labelled 'green' if they contribute substantially to reducing the speed of climate change or adapting to the effects of climate change. There is also a third category of 'other footprint reduction'.

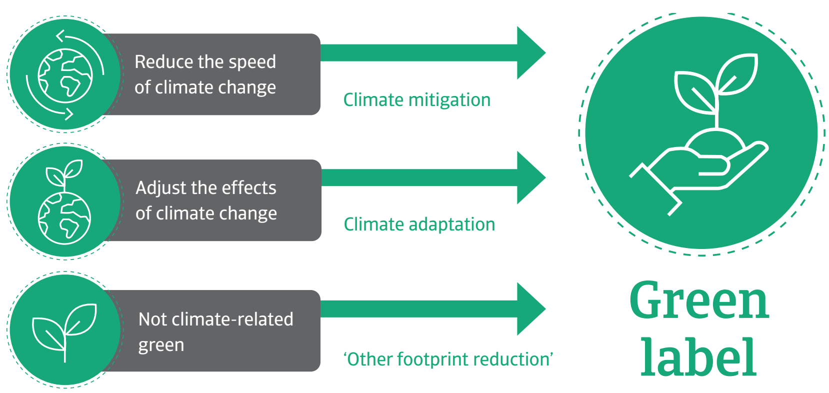
Aligning global economic governance to climate goals

Despite progress on mobilising finance to support a global green deal, there is much more to do. Ultimately, we need to ensure all finance is 'net zero' finance. Aligning global economic governance to climate goals will require additional reforms across the trade and investment regimes.

The Paris Agreement aims to reach net zero emissions by mid-century, in an effort to stem the global temperature rise to well below 2°C, and ideally 1.5°C. Scientific findings since then make clear the enormous differences between those two temperature goals: millions more lives would be lost and billions more dollars' worth of destruction would be sustained. The impacts of climate change, such as wildfires, extreme heat, flooding and tropical storms, are accelerating even faster than scientists predicted. Meanwhile, air pollution, deforestation, inequality and other underlying problems have magnified the impacts of COVID-19 and put us at greater risk of future shocks.

Those are the drivers behind the shift to a healthier, cleaner, more resilient and more regenerative economy. But there is opportunity, too. The race to zero emissions offers us a route to recovering from this

Figure 2: Going Green in the Netherlands



Source: Atradius DSB

crisis in a way that reduces future risks. More than 200 central bankers, G20 finance ministers, and academics from 53 countries agree that many of the most effective solutions to recovering from COVID-19 are those that reduce carbon emissions, according to a report by the Oxford Smith School of Enterprise and the Environment[1]. Investment in climate-resilient infrastructure and decarbonisation will create new and better jobs in the near term while protecting the economy, and today's near-zero interest rates make this the perfect time to jump in, according to McKinsey.

A new research project explores these shifts further, looking at a potential package of reforms across many sectors in order to create structural change. The project was initiated by the Blavatnik School of Government at Oxford University, the ClimateWorks Foundation, and Mission 2020, a shared global campaign convened by the former Executive Secretary of the United Nations Framework Convention on Climate Change (UNFCCC) Christiana Figueres.

In July 2020, a brainstorming workshop with more than 40 participants including colleagues from Afreximbank, the Berne Union Secretariat, Columbia University, EKF, Offenburg University, the OECD, Oxford University and the World Trade Organization (WTO) discussed ideas for this potential package of reforms. Topics included how to support countries to develop WTO-compatible national climate policies, enhancing attention to climate issues in WTO Trade Policy Review mechanisms, an alignment of UNCITRAL reform of investor-state dispute settlement with climate goals, and climate protection in preferential trade agreements. Furthermore, the idea of a 'Berne Union Net Zero Club' attracted enormous interest.

Working towards a commitment to net zero

What could a 'Berne Union Net Zero Club' look like? As discussed earlier, several ECAs, Exim-Banks and PRIs are already implementing ambitious climate-related policies. These include scaling down and ceasing operations not consistent with the Paris Agreement. For example, some agencies have started to apply stricter rules on exports related to coal-fired power generation. Furthermore, there are substantial contributions to low carbon and climate resilient developments with more export promotion of climate-friendly technologies in many countries. There are also commitments to international policies and standards from numerous institutions, for example to the Climate Change Sector Understanding (CCSU) and the Coal-Fired Electricity Generation Sector Understanding (CFSU), or through the application of UN Global Compact, IFC standards and guidelines, and the Equator Principles.

Although there are significant efforts undertaken by many Berne Union members, there is an opportunity to accelerate net zero transformation. An important starting point would be full transparency regarding support for both high emission projects and

Figure 3: Berne Union Net Zero Club

Source: IfTI

With economic weight shifting toward net zero, now is the time for ECAs, Exim-Banks, and PRIs to lead. Despite previous success, aligning global economic governance to climate goals requires additional activities across export finance and investment insurance institutions.

low-carbon transactions, for example with harmonised methodologies and approaches. Developing and implementing concrete plans for how to get to net zero might include realigning mandates and corporate strategies, principles of intervention, as well as ECA, Exim-Bank and PRI operating models. This might, for example, lead to an alignment of all new financing and insurance activities with the objectives of the Paris Agreement. A stronger integration of climate risks will help to reduce support for high emission projects and lead to a broader shifting of portfolios towards low-carbon projects. Members of a 'Berne Union Net Zero Club' (Figure 3) might learn from peers such as Sweden with its commitment to cease support for fossil fuel exploration and extraction projects by 2022. Other best practices to look at are Denmark's combination of export support with Denmark's Green Future Fund. Combining climate-related guarantee instruments such as the Swiss Technology Fund with export credit insurance can be another opportunity to work towards a commitment to net zero. As ECAs, Exim-Banks, and PRIs consider in more depth what net zero looks like for our sector, collaboration and exchange through forums like the Berne Union can help us all move forward more quickly.

The way forward: Join the club

Climate financing has become a priority in trade and development finance in recent years. Although development banks are most relevant regarding financing for climate action activities, several ECAs, Exim-Banks and PRIs have started to support low-carbon transformation related transactions. In addition, scaling down support not consistent with the Paris Agreement has become much more relevant. Further to green finance activities, the assessment of environmental impacts plays a major role for numerous ECAs, Exim-Banks and PRIs. Important examples of ECAs' commitment towards SDGs include EDC's Climate Change Policy and Atradius DSB's teams to deal with greening the business, reporting on green transactions within the portfolio, and on the impact of transactions on SDGs.

With economic weight shifting toward net zero, now is the time for ECAs, Exim-Banks, and PRIs to lead. Despite previous success, aligning global economic governance to climate goals requires additional activities across export finance and investment insurance institutions. The new research project initiated by Oxford University, ClimateWorks Foundation, and Mission 2020 including other practitioners and academics from institutions such as Atradius DSB, Columbia University, EDC, FMO and Offenburg University focuses on reshaping future trade and investment governance in light of climate action. The idea of a 'Berne Union Net Zero Club' is an important item in a potential package of reforms. This can include realigning mandates and corporate strategies, principles of intervention, as well as ECA, Exim-Bank and PRI operating models in order to accelerate net zero transformation. Full transparency regarding Berne Union members' activities would be an excellent starting point. We invite all interested parties in the sector to come together to chart our own path to net zero. ■

Note

1 https://www.smithschool.ox.ac.uk/news/articles/200505-building-back-better-net-zero-emissions-recovery.html

Astrid Bronswijk is Head of Export Finance and Investment Guarantees at the Ministry of Finance in the Netherlands.

Ranya Gabriel is Head of International Relations with Export Development Canada (EDC).

Dr Thomas Hale is Associate Professor at the Blavatnik School of Government, Oxford University.

Dr Andreas Klasen is Professor of International Business and Director of the Institute for Trade and Innovation (IfTI) at Offenburg University.

Sustainability: A key part of our due diligence work

By Kamil Zabielski, Head of Sustainability at GIEK

Sustainability, including environmental, social and financial aspects, is a key part of GIEK's due diligence work. GIEK has been an active contributor to ECA guidelines and the regulatory framework that promotes sustainable business. GIEK's work on sustainability is aimed both at reducing our clients' business risks, as well as contributing to Norway's work on the Agenda 2030 and the Sustainable Development Goals (SDGs).

Agenda 2030 is a global roadmap for eradicating extreme poverty through sustainable development and for promoting good governance and peaceful societies by 2030. Agenda 2030 defines 17 Sustainable Development Goals (SDGs), each with their own subset of targets, as a guide for nations' efforts to eradicate extreme poverty while protecting planetary boundaries [a concept involving Earth system processes that contain environmental boundaries] and promoting prosperity, peace and justice.

Collaboration is crucial

Agenda 2030 is clear on the fact that the SDGs can only be met through the collaborative efforts of both public and private sectors, and other relevant stakeholders. By enabling an environment for the private sector, such as creating dedicated financial instruments for projects that actively contribute to SDGs, governments can foster sustainable, responsible growth. In an environment where green finance is growing rapidly, SDG friendly finance is quickly becoming its own niche, and offers great opportunities for both new and mature businesses looking for alternative financial opportunities.

Kamil Zabielski

Preferential financing terms for SDG friendly projects

It is in this new financial environment that GIEK is looking for ways to promote business opportunities that contribute to SDGs. We are exploring ways in which we can incentivise projects that actively contribute to them. In order to be able to provide preferential terms, a system for evaluating projects against SDGs needed to be developed.

GIEK has been working on developing a methodology, with feedback from like-minded ECAs, that enables us to better evaluate a project's contribution to SDGs.

GIEK aims to make the SDG assessment tool available to peers in the not too distant future. We hope to encourage other financial institutions to make use of the tool. GIEK hopes that this tool can be the starting point for the creation of a common framework for the financing of SDG-positive projects for ECAs, contribute to a level playing field, as well as increasing ECA support for SDG-positive projects and transactions.

In the context of providing financing to customers, being able to document a clear and transparent SDG-assessment is essential to ensure a level playing field for all our customers, while remaining accountable to our owners.

GIEK has developed a SDG assessment tool

The SDG tool is intended to support financial institutions in evaluating a project/transaction's contribution to SDGs. The methodology is a rather simple approach that guides the user through the goals and targets, offering some guidance and benchmarking where appropriate. The SDG evaluation does not replace an ESG assessment and has a prerequisite that regular due diligence against applicable standards has been conducted. A project/transaction's contribution to each of the SDGs is reflected in a score, ranging from -1 to +2, where -1 indicates the residual negative effect (post-mitigation efforts) on a particular SDG, and +2 indicates that the project has a particularly positive effect on the specific SDG.

The methodology allows the assessor to indicate projects as having both negative and positive effects on the same SDG. GIEK has developed guidance in order help to support efforts that targets and their scoring are understood by the assessor. This would in turn contribute to a more consistent result independently of the financial institution. GIEK has been using this tool for the past year in all relevant new credit cases.

The intention is that the individual SDG evaluations gives the assessor the basis for making an overall SDG-assessment of the project or transaction. A project or transaction can be 'very positive', 'positive' or 'neutral'. A project or transaction that has significant negative effect on one or more of the SDGs should not be assessed for its contribution to the SDGs.

The results of this evaluation are displayed in a 'rose', showing in a simple and clear manner how the project affects SDGs. In advance of providing a guarantee for a project, it allows decision-making bodies, such as a credit committee or board, to quickly understand the sustainability aspects of a transaction, and make better informed decisions.

When using the SDG-tool earlier in the project life-cycle, it may support the ESG practitioner to have a dialogue with the project owner on how to make the project more 'SDG positive'. The tool may also help identify at an early stage where a project may have a significant negative effect, and therefore need improvement.

A starting point for the creation of a common framework?

GIEK aims to make the SDG assessment tool available to peers in the not too distant future. We hope to encourage other financial institutions to make use of the tool. GIEK hopes that this tool can be the starting point for the creation of a common framework for the financing of SDG-positive projects for ECAs, contribute to a level playing field, as well as increasing ECA support for SDG-positive projects and transactions.

GIEK at a glance

GIEK is a public-sector enterprise, fully owned by the Norwegian Ministry of Trade, Industry and Fisheries, that provides both short- and long-term guarantees on behalf of the Norwegian state in order to encourage Norwegian participation in international trade and exports. Backed by Norway's AAA rating, GIEK provides guarantees on commercial terms for loans, investments and product deliveries. Guarantees are provided to Norwegian companies, international buyers and banks. GIEK is subject to international rules and agreements governing ECAs. ■

The SDG tool

Harnessing Asia's offshore winds

By MeiYean Lim, Senior Underwriter for AXA XL's Global Political Risk

Many Asian countries have ideal conditions for generating electricity from offshore wind turbines. However, before the region can rely on this limitless source of green energy, some obstacles will have to be overcome. MeiYean Lim, AXA XL's Senior Underwriter for Political Risk-Credit & Bond, has the details.

There is a lot of power in offshore wind. So much so that analysts calculate that it has the potential to generate more than 18 times current global electricity demand.

However, while wind resources are there, harnessing it efficiently and safely is a daunting undertaking. Offshore wind projects require massive upfront investments, and there are numerous challenges and risks involved in constructing and operating these facilities in marine environments. Plus, the energy grid needs to be capable of distributing the power produced.

Nonetheless, the amount of energy generated by offshore wind is projected to increase threefold by 2025. While established markets are expected to see continued growth in generation capacity, analysts predict that many countries across the Asia-Pacific region have the potential to become leading producers of energy from offshore wind.

MeiYean Lim

Transitioning to low-carbon energy production

Most Asian countries have relied on nuclear energy and fossil fuels to power their fast-growing economies. Following the Fukushima Daiichi accident and also due to the world's increasingly urgent need to transition to low-carbon energy production, many countries across Asia now aim for dramatic increases in the percentage of their electricity produced from renewable sources, including offshore wind.

In recent years, China has embarked on an ambitious effort to meet more of its energy needs from wind power. It is now the world leader in wind power with more than one-third of the world's total installed capacity,

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followed by the U.S., Germany and India, which collectively generate about as much electricity from wind turbines as China. The remaining one-third is produced in a variety of countries, including many in the European Union.

In developed markets like Japan and South Korea, the volume of installed wind power currently is quite small, even though they have areas with strong, consistent winds and possess significant manufacturing expertise. And in emerging markets like Vietnam, the Philippines, Indonesia and Malaysia, commercial wind operations are still in the planning phase.

However, change is – so to speak – blowing in the wind. Countries across the region are beginning to establish the policies, infrastructure and expertise needed to build and operate wind farms in promising offshore locales. Vietnam, for example, could have around 10-12 gigawatts (GW) from offshore wind online by 2030. That is about one-third of what is installed today.

Why the emphasis on offshore? In short, turbines sited offshore typically generate more electricity at a steadier rate than their onshore counterparts. In many parts of the world, those factors tend to outweigh offshore wind's higher construction and operational costs and risks.

Enabling a new industrial sector

All of these countries face the difficult challenge of creating what is essentially a new industrial sector. That is no simple undertaking. First and foremost, governmental policies need to be enacted governing the siting and licensing of offshore wind operations. And given current market realities –including the absence of carbon taxes – creating a viable offshore wind industry requires some level of price support at the outset.

These commonly take the form of feed-

First and foremost, governmental policies need to be enacted governing the siting and licensing of offshore wind operations. And given current market realities – including the absence of carbon taxes – creating a viable offshore wind industry requires some level of price support at the outset.

in tariffs, or FiTs, whereby governments incentivize private investments in renewable energy by offering long-term contracts to producers based on production costs – plus a reasonable return for their investment. Also, the price levels built into these contracts are often adjusted to reflect the overall costs of developing different technologies. For example, offshore wind and solar photovoltaic projects may be awarded a higher per kilowatt-hour (kWh) price compared to a tidal-power facility, based on the current capital costs for constructing and operating the respective operations as well as their expected future generating capacity.

Moreover, feed-in tariffs commonly are 'laddered', meaning they are set at a high level at the beginning to help a country introduce new technologies, like offshore wind, then reduced gradually over time. This can make a critical difference. Although the raw material – be it wind, the sun's rays or the Earth's heat – is 'free', ramping up renewable energy production initially is

In developed markets like Japan and South Korea, the volume of installed wind power currently is quite small, even though they have areas with strong, consistent winds and possess significant manufacturing expertise. And in emerging markets like Vietnam, the Philippines, Indonesia and Malaysia, commercial wind operations are still in the planning phase.

relatively costly while the supply chains, infrastructure, project finance and local expertise are still immature. However, once these elements are established, scale and efficiency gains start to kick in, and the upfront costs and ongoing operating expenses begin to decline.

Note, for instance, that the FiT currently in place in Vietnam is $0.098 per kWh. However, this is less than in some other Asian countries. China, by comparison, has an upper limit around $0.12 per kWh. There is some speculation, on the other hand, that as the offshore wind industry becomes further established in other Asia countries, Vietnam will have to revisit its tariff levels to remain competitive in a growing market.

Attracting international investors

While financiers have many criteria for assessing potential projects, their judgements ultimately centre on three factors:

- the estimated costs – both construction and operational
- the projected revenues over the lifetime of the operation
- the terms and conditions of the power purchase agreement (PPA) between the lender and the 'offtaker' – that's the entity that agrees to purchase the energy produced by the wind turbines. The PPA plays a vital role in mitigating the various risks associated with offtaker's ability to live up to its commitments.

However, once a project gets underway, there are myriad ways in which the on-the-ground realities can unfold differently from the business plan. Construction, for example, can take longer than expected and/or prove more costly. Either way, and even with the government's tariff scheme, the projected revenue stream may well start later than expected or may not be enough to cover the actual construction costs profitably. Also, the natural catastrophe exposures in many parts of the region are not trivial – there is always the possibility that typhoons or seismic events could severely damage, if not destroy, facilities.

Moreover, financing for offshore wind facilities typically runs for 20 years, and individual projects are owned by special-purpose vehicles having few, if any, other assets. Thus, lenders need to be comfortable participating in ventures with long risk horizons and limited collateral.

Given these factors – an untested industry sector, the natural catastrophe exposures, and ownership by special-purpose vehicles – credit insurance is, not surprisingly, a prerequisite for international investors. In addition to helping mitigate against possible loan defaults, credit insurance enables lenders to:

- Manage in-country risks
- Achieve a better rate-of-return
- Establish a competitive advantage by supporting higher lending limits.

Also, the availability of credit insurance from established re/insurance markets like AXA XL – which has strong experience insuring project finance, offshore wind turbines and the region's natural catastrophe exposures – is a critical consideration for leading renewable-energy investors looking to expand their portfolios into new territories.

Notwithstanding the severe challenges confronting the global economy currently, wind will continue to blow, and with proper planning and risk mitigation, more and more of that energy will be transformed into electricity from burgeoning offshore turbines.

MeiYean Lim is Senior Underwriter for AXA XL's Global Political Risk, Credit and Bond team. In this role, she develops risk mitigation solutions to help enterprises trade and invest in emerging markets. She joined AXA XL in 2016 after a career spanning nearly 13 years in trade credit insurance, commodity trading and reinsurance. MeiYean is based in Singapore and can be reached on meiyean.lim@axaxl.com. ■

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Does the Paris Agreement prevent EU ECAs from supporting oil and gas projects?

By Henri d'Ambrières, HDA Conseil

The first objective of the 2015 Paris Agreement is to 'keep the global temperature rise this century well below two degrees Celsius above pre-industrial levels (1861-1880) and to pursue efforts to limit the increase even further to 1.5 degrees'. To make this happen, NGOs, Green parties and some development banks, among others, propose to stop financing oil and gas and to prevent EU Export Credit Agencies (ECAs) from financing them.

The International Energy Agency (IEA) said in its Outlook 2019 that, without any investment, the production of oil could be as low as seven million barrels of oil per day (mbpd) by 2050 versus 97.7 mbpd in 2018.

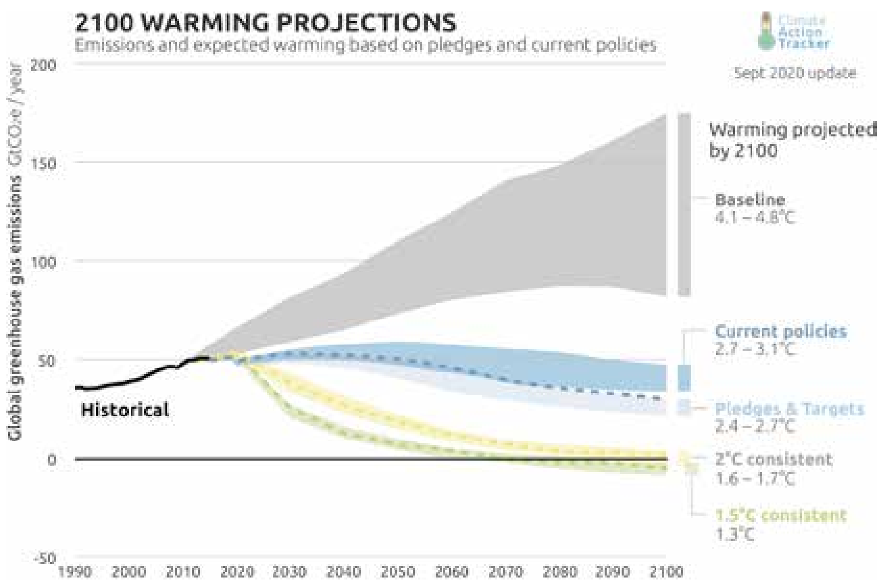
Henri d'Ambrières

With investments limited to existing fields, production would be 22.4 mbpd.

Greenhouse gases and the Paris Agreement

The main driver of global warming is the emission of greenhouse gases (GHG). The main GHG are carbon dioxide (CO2) which account for 76%, methane (16%), nitrous oxide (6%) and fluorinated gases (F-gases). In its 2014 report[1] the IPCC

Figure 1



Source: IPCC Report 2014 / Climate Action Tracker presented the link between global warming and cumulative GHG emissions, which were 1,900 gigatonnes (GT) equivalent CO2 in 2010. If annual new net emissions were to remain at their levels of 2010 (49 GT equivalent CO2/year), cumulative emissions would amount to 7,000 GT CO2 by 2100 and global warming could reach four to five degrees by 2100. To limit global warming below two degrees, cumulative net emissions would have to be capped at 2,380- 2,430 GT CO2 by 2100, or zero net emissions between 2070 and 2100. To limit global warming to 1.5 degrees, zero net emissions must be reached between 2050 and 2070 (see Figure 1).

To reach zero net emissions, there must be absolute reduction and capture technology, with natural tools such as reforestation and instruments such as CCUS (Carbon Capture, Utilisation and Storage).

The Paris Conference decided to share the efforts to reduce emissions of GHGs through Nationally Determined Contributions (NDCs). Each country has to update its Intended NDCs (INDCs) every five years. The more polluting (and richer) countries committed to reduce their emissions more rapidly. In 2015 the EU agreed to reduce its emissions in 2030 by 40% versus 1990 (or 30% vs 2005). Now the EU considers zero net emissions by 2050, which means reductions in 2030 by 55% vs 1990 or 40% vs 2005. Some less-developed countries were allowed to increase them but were also requested to present two scenarios: Business as Usual (BAU) and another based on reduced emissions. As the second scenario is more costly, its costs are supposed to be mainly supported by richer countries.

The view of the IPCC on primary energy sources in 2050

In 2019, the IPPC considered 90 scenarios and retained four consistent pathways to limit global warming at 1.5 degrees by 2100. All assume zero net emissions by 2050 (see Figure 2).

1. Pathway one is based on dramatic changes with a de-growth scheme (a political choice) and has no recourse to CCUS. Reforestation is the only way to increase captures of GHG.
2. Pathways two and three are based on more sustainable growth, energy efficiency and recourse to some CCUS including BECCS (Bioenergy with Carbon Capture and Storage[2]).
3. Pathway four is based on limited energy efficiency and massive recourse to CCUS. The absence of changes in energy needs and the massive use of CCUS is questionable.

The report says two sources of energy, renewables and nuclear will develop. Interestingly, the IPCC also considers that in all pathways, the use of oil will mainly decrease after 2030 (after coal) but not disappear. Gas use will decrease later than oil (and even increase in the case of the third pathway – see Figure 3).

Figure 2

IPCC Scenarios (1.5° global heating)	Pathway 1		Pathway 2		Pathway 3		Pathway 4	
	2030	2050	2030	2050	2030	2050	2030	2050
Final energy demand (vs 2010)	-15%	-32%	-5%	2%	17%	21%	39%	44%
GHG Emissions (vs 2010)	-50%	-82%	-49%	-89%	-35%	-78%	-2%	-80%
Cumulative CCS until 2100 (GT CO2)		0		348		687		1,218
including BEBCS (GT CO2)		0		151		414		1,191

Source: IPCC Report 2019

Figure 3

Sources of primary energy (vs 2010)	Pathway 1		Pathway 2		Pathway 3		Pathway 4	
	2030	2050	2030	2050	2030	2050	2030	2050
Renewable (but biomass)	430%	833%	470%	1327%	315%	878%	110%	1137%
Biomass	-11%	-16%	0%	49%	36%	121%	-1%	418%
Nuclear	59%	150%	93%	98%	98%	501%	106%	468%
Coal	-78%	-97%	-61%	-77%	-75%	-73%	-59%	-97%
Oil	-37%	-87%	-13%	-50%	-3%	-81%	86%	-32%
Gas	-25%	-74%	-20%	-53%	33%	21%	37%	-48%

Source: IPCC Report 2019

The view of the IEA on primary energy sources in 2050

In its 2020 Outlook, the IEA also considers different scenarios for 2040 and 2050 including:

- Stated Policies Scenario (STEPS), based on public INDCs. Global warming would be two to three degrees Celsius.
- Sustainable Development (SDS), assuming zero emissions by 2070 and global warming of 1.8 degrees.
- A new Net Zero Emissions by 2050 (NZE2050) inducing a global warming of 1.5 degrees.

The SDS is presented with more data than NZE2050. The prerequisites of the SDS are clear:

- Economic production should be much more energy-efficient (by a factor of two). With GDP multiplied by 1.86 between 2019 and 2040, demand for energy would reduce by 10%.
- Energy production should be much cleaner. CO2 intensity (tonne of CO2 per tonne of energy) would fall from 2.29 to 1.09. This would be achieved through a reduced use of fossil fuels and some recourse to CCUS instruments.

In the NZE2050, energy demand would be 11% lower than in the SDS in 2030 and the recourse to CCUS would be more important.

In the SDS, the use of coal and oil would regularly decrease (in different proportions) over the whole period while gas would remain stable until the mid-2030s, to manage the transition, and then decline as it remains a source of GHG. However, they will not disappear before 2050 for several reasons (see Figure 4):

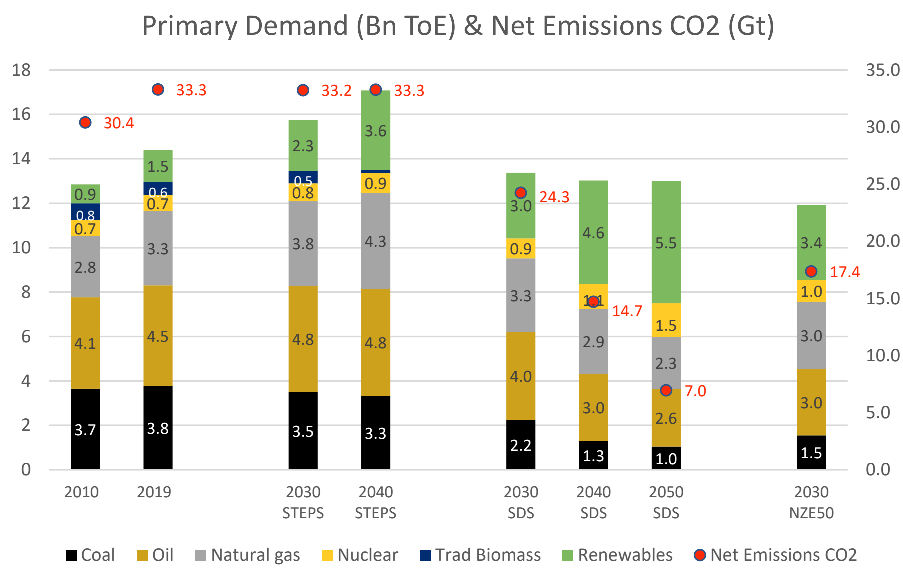
- For some non-energy usages, there are no credible alternatives yet (anodes; steel or cement for coal; bitumen and lubricants for oil; some chemical products for gas).
- As a source of energy, they cannot be always fully displaced as electricity cannot be used in every situation and renewable energies will not secure supply as long as the storage issue remains unsolved.
- Natural gas might be blended with biomethane and low-carbon hydrogen, when produced under satisfactory conditions (possibly around 2040).

Emerging and developing countries will consume most fossil fuels in 2040 (91% of coal, 62% of oil and 70% of gas). This use is consistent with the elimination of poverty and increased standards of living, combined with less financial resources than in developed countries to switch to cleaner sources. The EU will become a marginal consumer (2% of coal in 2040 versus 5% in 2019, 5% of oil vs 10%, 6% of gas vs 10%).

Electricity will become increasingly important (31% in SDS in 2040 vs 24% in STEPS in 2040 or 19% in 2019) but fossil fuels will remain predominant (see Figure 5).

Generation of electricity would rely first on

Figure 4



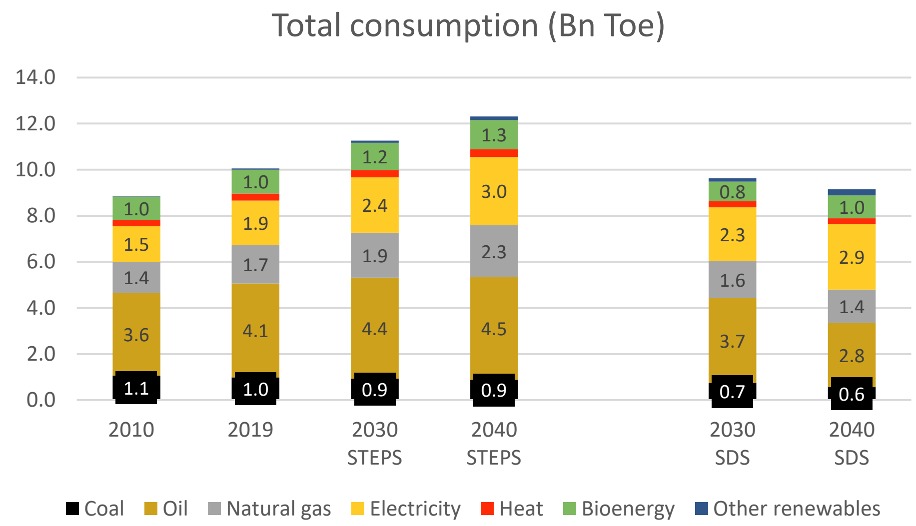
Source: IEA – Outlook 2020

more renewables (27% in 2019, 52% in SDS in 2030, 72% in 2040 or 60% in NZE2050 in 2030) and also on some more nuclear (11-12% vs 10%). In the SDS 2040, renewable energies will be mostly be wind (31%, six times more than in 2019), hydro (24%, up 60%) and solar (21%, 10 times more).

The SDS (and NZE2050) scenario also includes the completion of two other Sustainable Development Goals (SDGs):

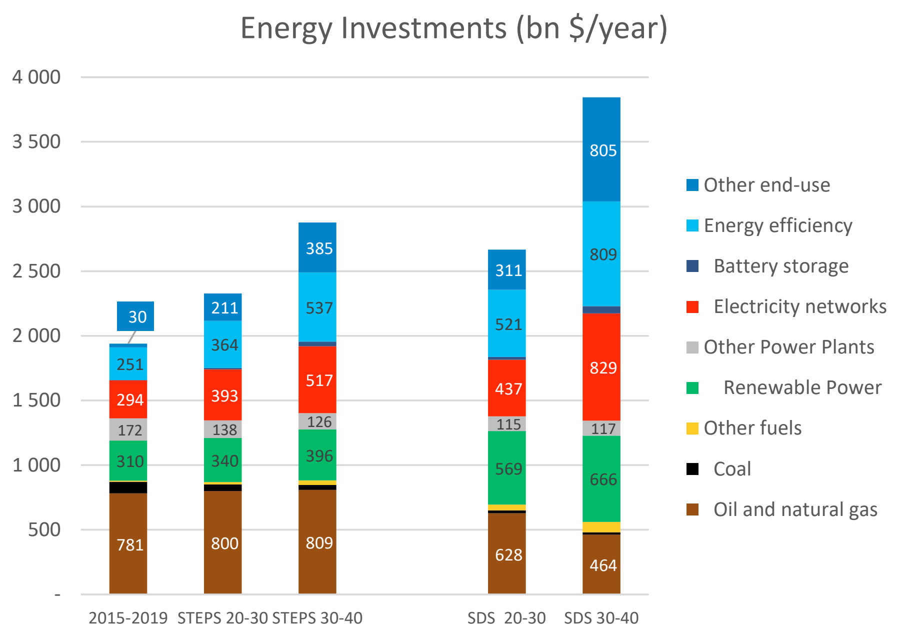
- Universal access to electricity (bearing in mind that 770m people had no access to it in 2019, mainly in Africa) with off-grid solar energy, mini-grids and also better distribution networks.
- Access to clean cooking fuels for 2.6 billion people who still use traditional biomass today. This could be achieved with more efficient wood stoves, Liquified Petroleum Gas (LPG) or some access to electric cooking. The impact on deforestation and public health (with much lower emissions

Figure 5



Source: IEA – Outlook 2020

Figure 6



Source: IEA – Outlook 2020

of particulates) would be very positive. In Sub-Saharan Africa, two thirds of energy demand was linked to biomass in 2018. To reduce it, for example, Ghana's INDCs[3] indicate that LPGs could serve 55% of cooking needs in peri-urban and rural areas in 2030 instead of 5% in 2015.

These figures were affected in 2020 by the consequences of the COVID-19 crisis as some people lost their access to electricity or returned to biomass use.

The switch from STEPS to SDS or NZE250 requires improvements in energy production and use but also changes in individual behaviours (0.8 GT CO2 saved in 2030 in SDS/2.8 GT in NZE2050 or 18% of total savings). The IEA lists 11 individual behaviours including, for example, limited usage of air conditioning or increased eco-driving (see Figure 6).

In SDS, energy investment would be doubled to reach $3.9 trillion per year around 2035. They will be mostly dedicated to end use (individual renewable sources of energy – seven times – and energy efficiency – four times) as well as to electricity networks (two times) and some power plants. SDS is more costly (by 34% in the 2030s) than STEPS. Investments in production of energy would remain stable, with more investments in renewable and less in oil and gas.

The production of oil was 97.7 mbpd in 2018. Without any investments in existing fields, production would be as low as 6.8 mbpd in 2050 (58% of the level expected in the IPCC – P1). With investments limited to existing fields, production could drop to 22.4 mbpd (50% of the IPCC - P2 level or 40% of the IAE – SDS level). Similar impacts would appear for gas and it would question the use of gas during a transition period (in the 2020s and 2030s). Hence, investments in new fields are required. Oil prices would decline, while they would increase in STEPS, which assumes higher levels of production

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in 2040. It will create a pressure to support only low-investment cost oil and gas projects (see Figure 7).

According to the IEA, the emission intensity varies widely with average life-cycle emissions of 630 kg CO2 per barrel but best practices are 440 kg. It estimates that these emissions could be reduced by 40% between 2019 and 2030. Limiting methane leaks would be a very important development.

Financing investments in oil and gas

The IEA says that its NZE2050 is very similar to the IPCC - P2. These scenarios converge on the 1.5 degree global warming of the Paris Agreement, with some growth. They also mean:

- A need to stabilise energy demand, with an increased recourse to electricity thanks to renewables (and nuclear). It means more investments in networks and on the end-user side.
- A sharp reduction of coal which will remain very important for some developing countries
- A reduced role for oil (down by 50% in 2050 in P2)

Figure 7

Sources of primary energy (vs 2010)	Pathway 1		Pathway 2		Pathway 3		Pathway 4	
	2030	2050	2030	2050	2030	2050	2030	2050
Renewable (but biomass)	430%	833%	470%	1327%	315%	878%	110%	1137%
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Coal	-78%	-97%	-61%	-77%	-75%	-73%	-59%	-97%
Oil	-37%	-87%	-13%	-50%	-3%	-81%	86%	-32%
Gas	-25%	-74%	-20%	-53%	33%	21%	37%	-48%

Source: IEA – Outlook 2020

- A need for natural gas during an interim period until the mid-2030s before its reduction (-53% in P2)
- Some recourse to CCUS.

These levels of production of oil and gas will require new investment. The lack of supply would question the transition, especially in developing economies, as it could preserve more polluting sources of energy such as wood or coal, which are the cheapest energies. These countries might not meet SDGs by 2030 in the absence of sufficient energy.

Many financial investors adopted coal policies, with a ban on investment in coal-related projects. However, most of them limit it to thermal coal, considering that for some industrial usages (steel, cement, anodes, etc), there is no viable alternative today. And some organisations, including NGOs, recognise that, in some remote places, there is no alternative to coal-fired power plants. A nuanced approach would be appropriate for oil and gas, considering the need for a transition phase. Developing countries will need financing coming from Europe and other rich countries to develop and reach the SDGs. Europe itself can probably afford to support a reduction of 40% of net emissions of CO_2 in 2030 (vs 2005) with less oil and gas.

In SDS, investments in oil and gas might be in the range of \$464 bn/year in the 2030s (vs \$781 bn today). Hence, financing required by these projects will decrease. In order to select projects, a few criteria might be considered, such as:

- Compliance of the project with INDCs. The lack of consideration by developed countries for the INDCs prepared by developing countries might question their role in the latter.
- The compliance with stringent rules on environmental, human and social impacts such as the Equator Principles (EP). Most large energy projects, including those based on solar or wind energy, are classified as impacting projects (Category A) and so need to be reviewed carefully when they are financed by commercial banks. If EU actors were to ban the financing of oil and gas, there is a risk that less cautious financial players, in the Americas or Asia, not as regulated as in developed countries, could intervene with looser Environmental and Social (E&S) criteria.
- The efficiency of the production process in terms of associated GHG and natural resources, using the best available practices and targeting a level below the average of 630 kg CO_2 per barrel
- The capacity to face the low prices envisaged by the IEA in the SDS (below \$60/ barrel)

OECD ECAs and energy

The first purpose of ECAs is to support domestic exporters. While the business model of private credit insurers includes recoveries (in the range of 50% of indemnifications), OECD ECAs cover all their costs (operation and indemnifications) with premiums. Over the period 1999-2018, with recoveries of €119 bn, €132 bn were returned to taxpayers. Hence, ECAs are not subsidised (see Figure 8).

Most OECD ECAs' covers are related to transport (39% in 2009-2018) and industrial projects (22%). Natural resources, including mining, represent 9% and electricity 14%, with a growing share for renewables (55% in 2018 vs 32% over 2005-2018).

Building on obligations

The success of the Paris Agreement will require more investment in the end-

The success of the Paris Agreement will require more investment in the end-use segment, in power transmission networks and in renewables. Its successful implementation also means the use of some fossil fuels in the next 30 years, but at lower levels than now. NGOs give stringent lectures about the Paris Agreement, which is their mandate, but a nuanced approach, referring to the all IPCC pathways (and not only P1) or IEA data, should prevail.

use segment, in power transmission networks and in renewables. Its successful implementation also means the use of some fossil fuels in the next 30 years, but at lower levels than now. NGOs give stringent lectures about the Paris Agreement, which is their mandate, but a nuanced approach, referring to the all IPCC pathways (and not only P1) or IEA data, should prevail. In IPCC P2 or the IEA NZE2050, oil and gas consumption in 2050 at 50% of existing levels would require the development of new fields.

The EU might consider that the burden of investing in new fields has to be left to other countries as its marginal consumption could be satisfied by existing fields or new fields in the North Sea, outside of the EU. In line with EIB policy, EU ECAs would also be prevented from supporting new projects out of the EU too. Other sponsors and ECAs will probably develop these fields with looser E&S criteria, including the generation of more GHGs in their production.

The EU might also decide still to support its ECAs in some projects on a selective basis with some clear criteria (strict E&S standards, efficient production regarding GHGs for instance, below the average of 630 kg CO2 per barrel, low costs of production to support prices in the range of $50-60/barrel, compliance with INDCs, etc). New fields would be developed in a more sustainable way and make available the production that the world, including developing economies will probably require in 2050, unless all countries agree on a de-growth scheme.

It should also be recognised that gas is crucial during a transition phase. This will not prevent EU ECAs from covering renewable energy projects or transmission systems, as they do today, or from supporting European exporters of new technologies such as hydrogen or storage facilities. Such support would not contradict zero net emissions in the EU in 2050 as it is the starting point of the IPCC P2 or the IEA NZE 2050 schemes. And it might also be very helpful to support the growth required in most developing countries to reach SDGs. ■

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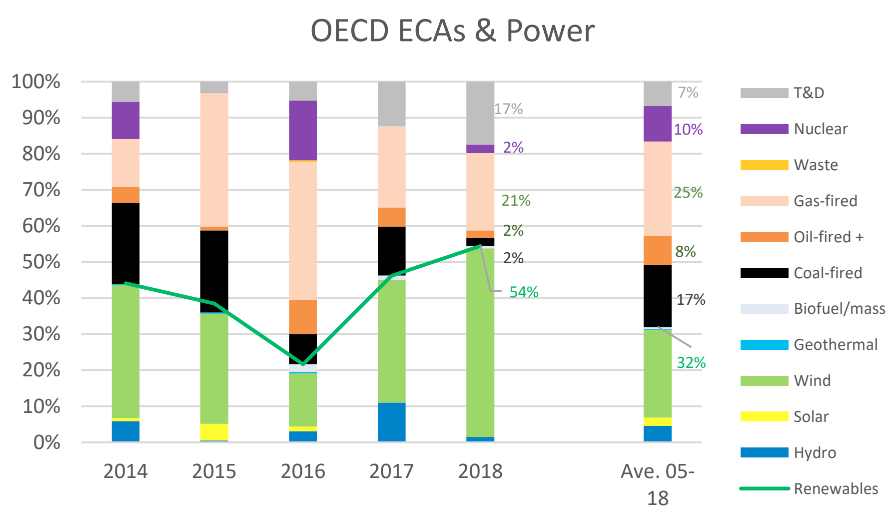
Notes

1 https://www.ipcc.ch/site/assets/uploads/2018/02/SYR_AR5_FINAL_full.pdf
2 https://www.globalccsinstitute.com/wp-content/uploads/2019/03/BECCS-Perspective_FINAL_18-March.pdf
3 https://www4.unfccc.int/sites/ndcstaging/PublishedDocuments/Ghana%20First/GH_INDC_2392015.pdf

Figure 8



Source: OECD Export Credit Group / Cashflows and Business Activities

Blended insurance programmes in difficult times

We need a change in the requirement profile of public funds. That is a central conclusion of Thomas Mahl and Franz Karmann, Managing Directors, SFR consulting, reflecting on their practical experience in Sub Saharan Africa.

The business perspective looks rather gloomy with a high risk of uncertainty in the COVID-19 crisis. That almost goes without saying. In particular the finance and insurance market has started to become more cautious and risk sensitive with respect to capacity allocation. To avoid an accelerated economic downturn, the public sector has stepped in as an 'insurer of last resort' to minimise potential losses and enhance the investment climate.

Reflecting the risk environment in Sub-Saharan Africa, our company is spearheading the effective use of scarce public funds for risk mitigating instruments. We want to share our view of the impact of the crisis in our daily work and, in particular, the need for a change in the requirement profile of public funds' allocation.

COVID-19 has accelerated the risk of increased uncertainty now and for the near future. To cope with these challenges, governments and public institutions have provided – in addition to existing development programmes – financial support to the private sector. In light of the scarce availability of public funds, the additional burden on public budgets will emphasise and enhance the importance of the effective use of public money in the future.

Thomas Mahl

Franz Karmann

Efficient use of public funds

Insurance programmes in partnership with the public sector can be very efficient if they are structured in the right way. Here we summarise some important factors:

In particular the finance and insurance market has started to become more cautious and risk sensitive with respect to capacity allocation. To avoid an accelerated economic downturn, the public sector has stepped in as an 'insurer of last resort' to minimise potential losses and enhance the investment climate.

- Risk appetite of the commercial insurance and reinsurance sector will be mirrored in the risk position of the public funds. In the case of new and unknown risk – where hardly any underwriting experience is available – commercial insurance markets tend to prefer the allocation of public fund as a buffer in the form of a first loss tranche. This is in contrast to other cases, where for example the tail end of the loss distribution is unknown (for example, climate risk), and the insurer tends to allocate additional public funds as a second loss tranche.
- Pricing needs to incorporate the goals of public funds. No one wants to provide money for free. On the other hand, if the risk portion of public funds is priced too high, this will ultimately lead to increased insurance premiums for the insurance buyer which could contradict the objective of the public funds' earmarked development goals. Therefore, the focus of the pricing of the public funded risk portion should be on the enhanced attractiveness of the investment climate to channel a sustainable capital flow towards the achievement of development goals.
- Eligibility criteria are often very narrow and complex. Usually programmes implemented by Development Finance Institutions (DFIs) are designed in a way that eligibility criteria follow regional or sector-specific goals. Often additional requirements are incorporated into those programmes. Insurance operates on a portfolio perspective where diversification is key to generate premium discounting effects. Having a narrow scope of insurance programmes runs counter to that fundamental principle and subsequently increases the price of those programmes.

If we structure an insurance or reinsurance programme with public funds, the underlying risk does not usually meet the commercial market risk appetite for one reason or another. Public funds as risk capital (via guarantees or other forms of insurance coverage) can be structured in a way that the remaining risk distribution becomes attractive for the commercial insurance market. Although those blended structures could move the barriers of insurability, the bureaucratic and inflexible processes of public institutions tend to limit private insurance market interest in pursuing this type of business opportunity.

African Energy Guarantee Facility (AEGF)

The African Energy Guarantee Facility (AEGF) is a reinsurance platform for commercial, reactive and comprehensive risk mitigation solutions, with a high coverage capacity and without sovereign guarantee requirements. The AEGF was initiated by the European Investment Bank (EIB), Munich RE and ATI. It is supported by KFW and provides $1 billion in reinsurance capacity for energy access, energy efficiency and renewable energy projects that are in line with SDG7 objectives.

Limiting factors of blended insurance programmes

Insurance programmes are efficient if the fundamental principle of a diversified portfolio is met. Size and grade of diversity of a portfolio determines the allocation of risk capital and the portfolio resilience in case of claims. As the insurance market operates on the basis of reliable future promises regarding premium and claims payments the quality of the portfolio is one of the crucial components to secure a sustainable product offering in the future.

Lessons from AEGF

Looking at the AEGF, we were originally confronted with diversification limiting factors like regional focus (Sub Sahara Africa) and product (mainly political risk

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insurance) for the portfolio. Now, with the accession of KfW and a running technical assistance programme sponsored by the EIB, we are working on several enhancements of AEGF to improve the composition of the portfolio. The COVID-19 crisis-related focus on enhanced efficient fund allocations helps with the discussion to open up programmes.

Donors often claim that strict eligibility criteria are one of the paramount prerequisites to avoid misuse of public funds. This is an important factor, but we should always have in mind that public funded insurance solutions are deemed to correct potential market gaps. Hence, also in the view of sustainability, diversity of the portfolio should steer the scope of eligibility criteria in future.

Looking at past experience of blended insurance programmes, there are hardly any solutions which have gone from pilot status into the next phase of scaling. In fact, a lot of public fund supported innovative insurance programmes have been dissolved after a few years as business volume did not meet the requirements to build up a self-sustainable portfolio. Besides the failed development objective, a discontinuation of an insurance programme is a huge reputational risk for the private insurance company that operates it. It is understandable then that the local primary insurance market, in particular, shows limited appetite to expand and enhance its product offering in the development finance space.

The way forward

COVID-19 has changed the risk landscape for the financing industry. Although there is abundant available capital to be invested, affordable and attractive risk transfer solutions will continue to gain in importance as a way to channel capital flows in future. If we want to achieve the ambitious development goals, a paradigm shift in respect of development policy is requested. Instead of adding additional public funds in the already capital abundant finance industry, we would recommend building up intelligent and attractive risk transfer solutions which enhance the investment climate for the private sector.

We hope that as consequence of the impact of the COVID-19 crisis, the development finance industry fosters the paradigm shift of development policy towards risk transfer solutions by adapting its available instruments towards this unique market's needs where diversification and portfolio setup is key.

Blended insurance programmes that are currently publicly supported could play a crucial role. However, to follow this route a shift from the current donors' mindset and practice is required. A pure continuation of public fund distribution which is restricted to single project investment-orientated eligibility criteria and stipulations does not work. Insurance operates on the portfolio perspective which instead requires a broader scope. We hope that as consequence of the impact of the COVID-19 crisis, the development finance industry fosters the paradigm shift of development policy towards risk transfer solutions by adapting its available instruments towards this unique market's needs where diversification and portfolio setup is key. ■

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5

Directory

Berne Union Members

The Berne Union has 84 members from around the world, including 2 Observers. The membership is diverse and includes private insurance, government-backed ECAs and multilateral organisations, both large and small. Together they represent all aspects of the export credit and investment insurance industry worldwide.

As of October 2020, the Berne Union's 84 members include: 69 ECAs, 11 private insurers and 4 multilateral institutions. We also welcome 2 guests of the Prague Club Committee.

The Berne Union member directory has moved online – this allows us to ensure that member information and contact details are always current and accessible. For contacts and more detailed information about each member please visit:

https://www.berneunion.org/Members

AIG United States of America
American International Group, Inc.

AOFI Serbia
Serbian Export Credit and Insurance Agency

ASEI Indonesia
Asuransi Asei Indonesia (Asuransi Asei)

ASHRA Israel
Israel Export Insurance Corp Ltd

ATI Multilateral
African Trade Insurance Agency

ATRADIUS The Netherlands
Atradius NV / DSB

AXA XL United Kingdom
AXA Group Insurance Company SE

BAEZ Bulgaria
Bulgarian Export Insurance Agency

BANCOMEXT Mexico
Banco Nacional de Comercio Exterior S.N.C.

Bandex Dominican Republic
Banco Nacional de las Exportaciones

BECI Botswana
Export Credit and Guarantee Company

BPIFRANCE France
Bpifrance Assurance Export

CESCE Spain
Compania Espanola de Seguros de Credito a la Exportacion

CHUBB Switzerland
Chubb Insurance Company

COFACE France
Compagnie Française d'Assurance pour le Commerce Exterieur

COSEC Portugal
Companhia de Seguro de Créditos, S.A.

CREDENDO GROUP Belgium

CREDIT OMAN Oman
Export Credit Guarantee Agency of Oman

DHAMAN Multilateral
The Arab Investment & Export Credit Guarantee Corporation

ECGC India
Export Credit Guarantee Corporation of India Ltd

ECGC Z Zimbabwe
Export Credit Guarantee Corporation Of Zimbabwe

ECI UAE
Etihad Credit Insurance

ECIC SA South Africa
Export Credit Insurance Corporation of South Africa Ltd

ECIO Greece
Export Credit Insurance Organization

EDC Canada
Export Development Canada

EFA Australia
Export Finance Australia

EGAP Czech Republic
Export Guarantee & Insurance Corporation

EGE Egypt
Export Credit Guarantee Company of Egypt

EGFI Iran
Export Guarantee Fund of Iran

EH GERMANY Germany
Euler Hermes Aktiengesellschaft

EIAA Armenia
Export Insurance Agency of Armenia

EKF Denmark
Eksport Kredit Fonden

EKN Sweden
Exportkreditnämnden

Enterprise SG Singapore
Enterprise Singapore

EXIAR Russia
Export Insurance Agency of Russia

EXIM HU Hungary
Hungarian Export-Import Bank Plc.

EXIM J Jamaica
National Export-Import Bank of Jamaica Limited

EXIM R Romania
Eximbank of Romania

EXIMBANKA SR Slovak Republic
Export-Import Bank of the Slovak Republic

EXIMGARANT Belarus
Eximgarant of Belarus

FCIA United States of America
FCIA Management Company, Inc

FINNVERA Finland
Finnvera Plc

GEXIM Ghana
Ghana Export-Import Bank

GIEK Norway
Garanti-Instituttet for Eksportkreditt

HBOR Croatia
Croatian Bank for Reconstruction & Development

HKEC Hong Kong
Hong Kong Export Credit Insurance Corporation

ICIEC Multilateral
Islamic Corp for the Insurance of Investment & Export Credit

Indonesia Eximbank Indonesia
Export-Import Bank of Indonesia

JLGC Jordan
Jordan Loan Guarantee Corporation

KAZAKHEXPORT Kazakhstan
Kazakh Export Credit Insurance Corporation

KREDEX Estonia
KredEx Credit Insurance Ltd.

KSURE Korea
Korea Trade Insurance Corporation

KUKE Poland
Export Credit Insurance Corporation Joint Stock Company

LIBERTY United Kingdom
Liberty Mutual Insurance Europe Limited

MBDP Macedonia
Macedonian Bank for Development Promotion

MEXIM Malaysia
Export-Import Bank of Malaysia Berhad

MIGA Multilateral
Multilateral Investment Guarantee Agency

NEXI Japan
Nippon Export and Investment Insurance

NZECO New Zealand
The New Zealand Export Credit Office

ODL Luxembourg
Luxembourg Export Credit Agency

OeKB Austria
Oesterreichische Kontrollbank Aktiengesellschaft

PICC China
People's Insurance Company of China

PwC Germany
PricewaterhouseCoopers AG

QDB Qatar
Qatar Development Bank

SACE Italy
Servizi Assicurativi e Finanziari

SEP Saudi Arabia
Saudi Export Program

SERV Switzerland
Swiss Export Risk Insurance

SID Slovenia
SID Inc, Ljubljana

SINOSURE China
China Export & Credit Insurance Corporation

SLECIC Sri Lanka
Sri Lanka Export Credit Insurance Corporation

SONAC Senegal
Société Nationale d'Assurances du Crédit et du Cautionnement

SOVEREIGN Bermuda
Sovereign Risk Insurance Ltd

SWISS RE CORPORATE SOLUTIONS Switzerland
Swiss Re Corporate Solutions

TEBC Chinese Taipei
Taipei Export-Import Bank of China

THAI EXIMBANK Thailand
Export-Import Bank of Thailand

TURK EXIMBANK Turkey
Export Credit Bank of Turkey

UK EXPORT FINANCE United Kingdom
Export Credits Gurantee Department

UKREXIMBANK Ukraine
Joint Stock Company the State Export-Import Bank of Ukraine

US EXIMBANK United States of America
Export-Import Bank of the United States

USDFC United States of America
U.S. International Development Finance Corporation

UZBEKINVEST Uzbekistan
Uzbekinvest National Export-Import Insurance Company

ZURICH United States of America
Zurich Surety, Credit & Political Risk

berneunion

1st Floor Thanet House, 231 - 232 Strand, London WC2R 1DA
Tel: +44 (0) 20 7841 1110 | Fax: +44 (0) 20 7430 0375

www.berneunion.org