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FOR SAFER TRADE

TRADE CREDIT INSURANCE
UNLOCKING GLOBAL GROWTH

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THIS WHITE PAPER EXPLAINS HOW TRADE CREDIT INSURANCE WORKS AND TIPS FOR SUCCESSFUL IMPLEMENTATION

Top-performing manufacturers know they need to look beyond their existing customers to remain competitive. Slow growth in mature markets and pricing pressures are key reasons why manufacturers must consider a global strategy, according to KPMG's 2016 Manufacturing Outlook.

In fact, a SunTrust Bank report shows that 29% of middle-market companies are looking to expand into international markets, compared with 17% the year before. Unfortunately, market expansion can be risky. To win new business, manufacturers may need to grant favorable payment terms that may extend well past 30 days. But what happens when a customer defaults or a business becomes insolvent?

Manufacturers have several options they can consider to minimize bad debt risk while helping to grow their sales. One of the most effective tools is trade credit insurance. A trade credit insurance program provides manufacturers with the flexibility and confidence they need to move into new markets.

WHY IS TRADE CREDIT PROTECTION CRITICAL?

Manufacturers need to make credit available to remain competitive, but it often comes at a hefty cost. In a 2016 National Small Business Association survey, 44% of respondents said getting paid was their greatest challenge when selling goods and services abroad. That's significant when you consider that, on average, accounts receivables comprise 35% of a company's assets, according to Coface research.

Meanwhile, companies in financial distress often stop paying their key suppliers after they declare bankruptcy. For example, it took more than a year for Target Canada to reach a payment settlement with all of its creditors after filing for bankruptcy in 2015, The Toronto Star reported on March 4, 2016. Under the proposed settlement, creditors will receive 66% to 77% of the amount they're owed, according to The Star report.

Disruptions like this often have a ripple effect, leading to more financial hardships throughout the supply chain. Business bankruptcies are increasing overall, with a 28% rise in business bankruptcies over the first three quarters of 2016, according to the American Bankruptcy Institute. One-fourth of bankruptcies are due to unpaid invoices, a recent Coface study revealed.

Such risk indicators reinforce the need for greater protection against nonpayment. Trade credit insurance policies offer the type of pre- and post-deal security manufacturers need to

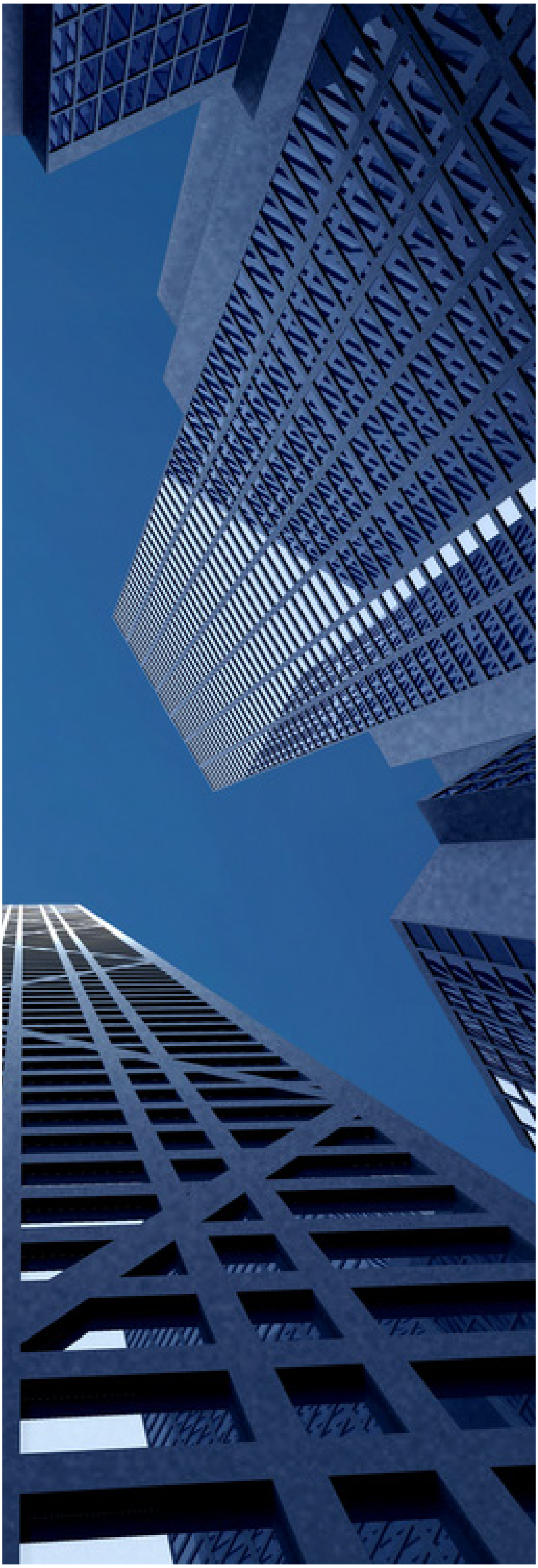
trade credit **insurance policies** offer pre- and post-deal **security**

+28% rise in business **bankruptcies** 2015 to 2016

25% **bankruptcies** due to **nonpayment**

=

greater need for **protection** against **nonpayment**



WHAT IS TRADE CREDIT INSURANCE?

Trade credit protection policies cover the unpaid credit balance from sales made to approved customers. They also include credit assessment and collection functions for a business. Each policy is structured individually, and the specific features of coverage vary depending on the insurance carrier and the individual business requirements. The most effective trade credit protection policies typically offer:

Protection against nonpayments arising from bankruptcy, defaults and, in some cases, political risks.

Coverage of short-term invoicing periods, between 60 and 180 days.

Credit risk checks to help ensure policyholders are selling to creditworthy customers. (Insurers with a global footprint, such as Coface, continually compile and monitor the financial health of companies around the world.)

Collection of overdue payments on accounts they cover. Some insurers also offer collection services on accounts that don't fall under the policy.

Trade credit insurance companies typically have high success rates as collectors. That's because debtors know insurers can see their payment patterns beyond a single account and that they may have difficulty obtaining future credit if they don't cooperate.

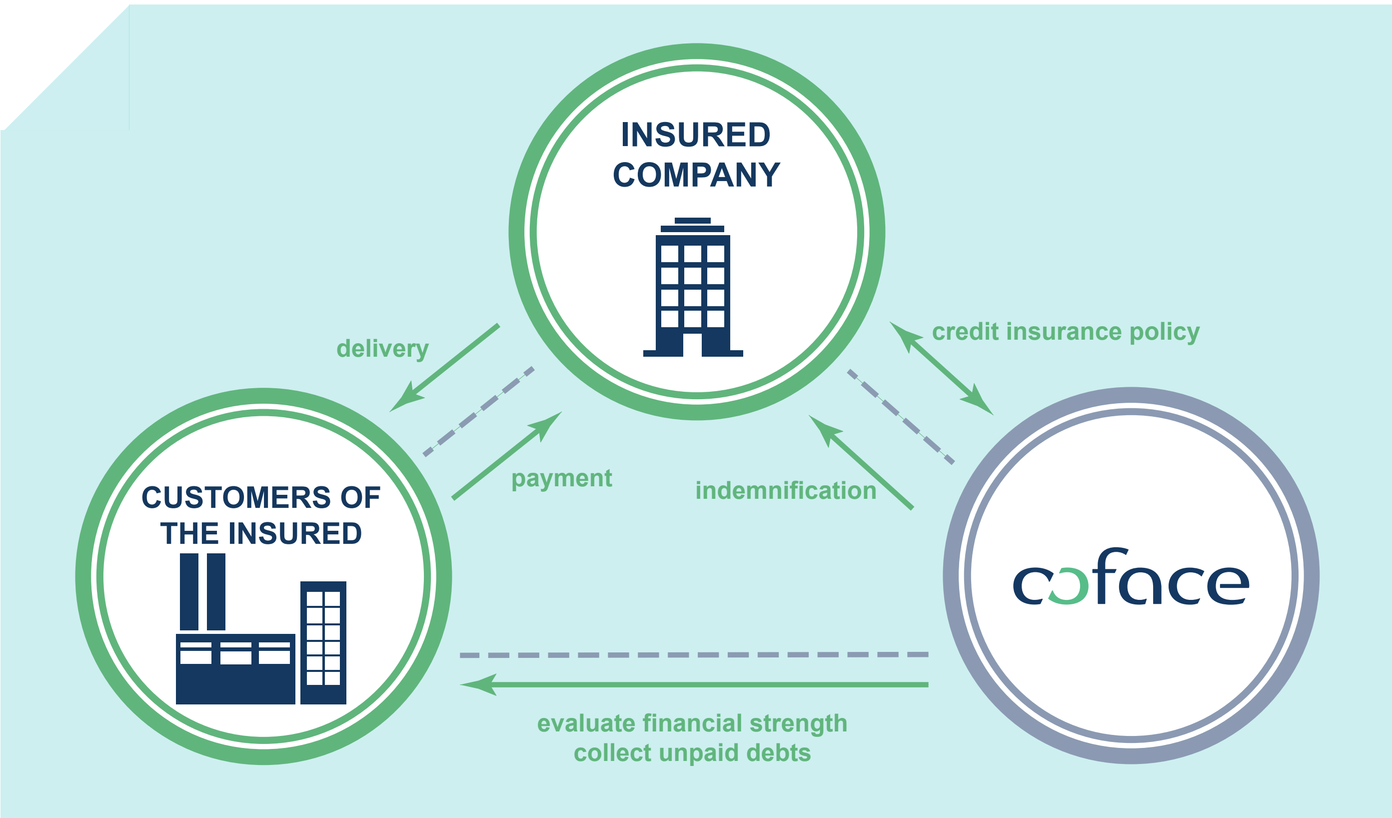
HOW DOES TRADE CREDIT PROTECTION WORK?

A company seeking trade credit insurance would provide information on its business and customers, including a list of top buyers and a recent loss history. The trade credit insurance carrier will review the financial health of the buyers to establish credit limits and terms of business, such as the maximum invoicing period. In some cases, automatic coverage up to a certain amount or percentage of sales is granted to give the policyholder flexibility in trading.

After the assessment the insurer presents a quote that outlines the policy terms and price. The quote would indicate the amount of coverage, the level of coinsurance (typically 10%), whether there is a deductible or a minimum dollar amount threshold for claim.

During the course of the policy, the insurer will continually monitor the buyers and could adjust coverage accordingly. Likewise, as the company expands its sales, new buyers can be added to the policy coverage.

Policyholders are eligible to file a claim when a customer is insolvent or financially unable to pay the outstanding balance owed.



8 tips

FOR EFFECTIVE CREDIT MANAGEMENT

MOST TRADE RISK CAN BE MITIGATED BY PRUDENT CREDIT MANAGEMENT. HERE ARE EIGHT PRACTICAL TIPS FOR ASSESSING CUSTOMERS

1 Establish a direct contact with the company beyond the sales person.
It's important not to intermingle the sales function with the credit function. Make the sale on its own merits and deal with the credit terms in a businesslike manner with someone other than the sales person.

2 Investigate the company.
Obtain a signed credit application that requires at least two credit references (bank or trade). Be sure to check the references. Also, purchase an independent, third-party credit report and check it closely against your internal information to make sure it's accurate. The credit report, at a minimum, should help you confirm a company's location, ownership, key executives, financials (if available), trade relationships and public-record filings.

3 Don't be afraid to ask awkward questions.
Look at the latest financials and check for evidence that the company is trading profitably. You may want to look into other information products such as credit opinions, which give you a suggested credit limit, and credit scores, which calculate a probability of default.

4 Join an industry credit group.
You will stay on top of developments in your industry especially in regards to company creditworthiness.

5 Consider insuring your trade transactions.
This outsources the assessment and monitoring of your portfolio, ensures payment and provides collection services.

6 If you are going to manage your credit function in house, establish and communicate clear rules.
Don't be an "enabler" of your customer by allowing them to exceed their credit limit or become consistently delinquent. Your lack of forcefulness on these points could come back to haunt you.

7 Be precise on the shipping conditions and retain proof that the goods have been received.
You need to make sure the customer has no excuses to later withhold payment.

8 Be vigilant.
When agreeing to special payment arrangements, be reasonably flexible but be sure to fully document all special arrangements and follow up diligently on these.

THE PAYOFF

Companies that need increased access to bank financing often need to demonstrate prudent credit management—professional processes embedded in the organization to mitigate credit risk. Having a trade credit insurance policy in place satisfies this requirement and assures the financial institution that its risk is covered. Banks may also provide larger lines or reduced financing fees for covered receivables. In addition, banks may be added as loss payees to the policy, whereby claims are paid directly to the bank. The opportunities and cost savings provided by trade credit insurance can offset the cost of the policy.

Additional potential benefits include:

Loss mitigation

For example, a manufacturer with a margin of 4% that experiences a nonpayment of $50,000 would need 25 equivalent sales to make up for a single instance of nonpayment.

Expense savings

Manufacturers can reduce their spending on trade credit information and staff time spent on chasing collections. The company can also deduct the cost of the policy as a business expense.

No bad debt reserves

Capital set aside as reserves can be freed and converted to earnings.

Lower cost of capital

Bank borrowing costs are often lower if receivables are insured, due to lower risk for the bank.

Increased sales

Allowing for higher credit lines to existing customers or opening new markets can increase revenue. Multiplying this increase by several customers could easily offset the cost of a policy.

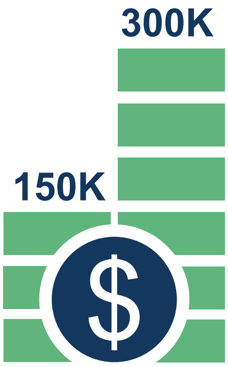
TRADE CREDIT PROTECTION: WHAT IS THE ROI POTENTIAL?

SCENARIO #1

Using Trade Credit Insurance to Increase Profits

Company A seeks to expand sales with current customers, but is uncomfortable with offering a higher internal credit limit. Company A can turn to protection from Coface to cover its customers. And, if Coface approves the higher credit limits then Company A can increase its credit limits, grow revenues and deliver more profits.

In the following example, Company A is able to capture $300,000 of incremental gross profit from just one trading partner. Those benefits could be multiplied across a broad portfolio of its customers.



Gross Income with Credit Insurance

	WITHOUT CREDIT INSURANCE	WITH CREDIT INSURANCE
Credit limit	$250,000	$500,000
6 turns per year	$1,500,000	$3,000,000
Margin on sale	10%	10%
Gross income	$150,000	$300,000

SCENARIO #2

Using Trade Credit Insurance to Improve Lending Terms

A wholesaler of chemicals and raw materials based in northern New Jersey is one example of a company that has improved its ability to secure credit by adding credit insurance. The company, which sells to customers outside of North America, needed a solution that provided more transparency to its lender which was concerned about the foreign receivables in the borrowing base.

“We purchased credit insurance initially to facilitate the perfection of our credit line facility,” says the managing director and CFO. “From the initial objective of providing comfort to our banks, the service added depth to our business decisions.”

The interaction with Coface allows the company to assess its clients’ condition more accurately and has been a valuable tool in business development.

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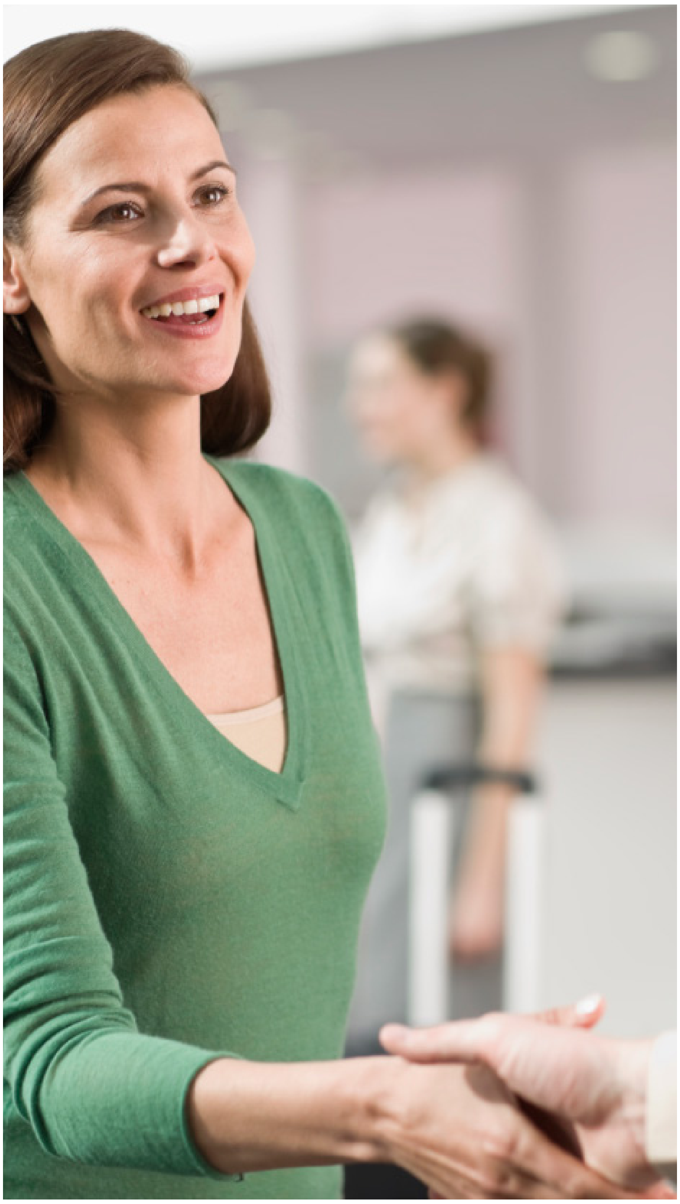

CONCLUSION

More manufacturers are realizing the importance of trade credit protection as they expand their market presence. They know that winning new business oftentimes depends on their ability to offer payment terms to customers. Also, demands for upfront payment will simply drive customers elsewhere, while other options, such as self-insurance or letters of credit, are either too risky or cumbersome to undertake.

Coface trade credit insurance can help companies through every phase of the credit process — from analyzing credit risk of customers to collection of debt to reimbursement for losses due to insolvency of one or more customers. Coface provides accounts receivable protection to 50,000 companies around the world. Our strength and integrity is supported by excellent ratings from Moody's and Fitch.

To learn more about how Coface can help your business grow, visit **www.coface-usa.com**.

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