

Chapter VIII

Trade and Investment Insurance System of Australia

Export Finance and Insurance Corporation – E.F.I.C.

- Banks and other infrastructure develop with business, but economic development may need some encouragement and support
 - Export Credit Agencies exist to fill gaps in the national financial infrastructure
 - Australia's history in international trade goes back to 1830, but EFIC only to 1956
 - First major export was wool - still dominates world market - but sold for cash at auction
 - Next the Gold Rush [1851], then wheat, meat and sugar - with corporate financings
 - Australia united and formed on Jan, 1, 1900
 - continued to sell commodities and import everything, but manufacturing began
 - Real change came post World War II
 - end of British Empire trade basis
 - immigration to Australia
 - rise of Japan trade for raw materials
 - growth of European Common Market
 - Serious efforts to increase manufacturing
 - search for new markets for products
 - Need for credit for small, medium exports to new markets
- 1956 - formation of EPIC, Export Payments and Insurance Corporation - A\$6 million loan.
- provided payment insurance for short-term credits.
- 1961 - Australian Government introduced the National Interest Account for higher risk and very large credits.
- needed for large wheat sales
- 1965 - Overseas Investment Insurance Facility
- to support manufacturers forming joint ventures, etc., abroad
- 1971 - Buyer Credit Guarantee Facility
- to support capital goods exports
 - Bougainville Copper mine supplies
- 1974 - Introduced direct lending for capital goods
- Reconstructed as **Export Finance & Insurance Corporation.**
- 1978 - Support for tender performance bonds
- 1983 - Empowered to lend foreign currencies

1986 - EFIC incorporated into AUSTRADE, began to Issue performance bonds

- big Increase In mining projects finance

1991 - EFIC re-established as separate Corporation

- equity capital, callable capital, reserves of A\$ 350 million
- total business supported \$4.8 billion

- EFIC now a full financial institution.

- In 25 years several roles established
 - support for commodity trades
 - support for manufactured exports
 - short-term credit sales
 - overseas stocks
 - investment insurance
 - capital goods exports to projects
 - bonds for contractors, service industries
 - improving relationships with banks on support for capital investments, loans to projects, working capital guarantees, assigned insurance, bonds

- EFIC became finance leader for several massive mining projects in Papua New Guinea

- built on Bougainville experience, OK Tedi mines to provide Innovative seed capital Inputs, including loans to PNG for government equity, first investment co-insurance with Canada, direct loans on a line of credit basis, political risk guarantees to bank syndications.

- Also addressed the market for SME exporters

- intensified marketing, restructured management structure, raised staff training, re-wrote policies in simpler form, worked with banks to improve exporter's access to working capital.
- results promising.

1996 RESULTS

- Total exports supported \$7.5 billion [+20%]
- Insured exports \$6.5 billion [+1496]
- 50 bonds Issued for \$140 million
- 12 overseas investments \$223 million

- 79 working capital guarantees [+100%]
- strong growth in SME business.
 - 209 new SMEs
 - 87% of new clients
 - 60% manufacturers
- exports to 155 countries [from 135]
- Europe is largest insured market [44%]
- Asia is largest for finance facilities [77%]
 - 2nd largest for insurance
- 1996/96 surplus \$12.6 million

EVENTS OF 1995/1996

- Financing and Cofinancing-financing of the billion dollar Lihir Gold Mine In Papua New Guinea
 - ❖ Political risk cover to financing banks
 - \$250 million capital
 - \$120 million interest
 - ❖ Credit Insurance to exporting suppliers
 - ❖ Investment Insurance to Mining Contractors
- EFIC invested in ASEAN Credit Information Co with ECICS [Singapore], COFACE [France]
- Introduced improved Export Finance Guarantee Facility for banks funding capital goods exports.
- Introduced improved Information services
- Streamlined re-organisation

TYPES OF INSURANCE

- Export Credit Insurance Policy
 - ❖ goods shipped / services performed
 - can be selective, with price loading
 - must declare all shipments to an insured buyer
 - ❖ cover against all risks-["seamless"]
 - unless special circumstances
 - co-insurance

- ❖ Ancillary extensions used
 - indirect export cover
 - overseas stock cover
 - processing cover
 - external trade cover
- ❖ Unfair Calling of Bonds or Guarantees Insurance
- ❖ Confirming Bank Policy
 - covers against failure of issuing bank& political risk
- Overseas Investment Insurance
 - covers against political risks
- Political Risk Insurance for capital goods finance by banks

INDEMNITY PAYMENTS

INSURED RISK	MAXIMUM	PAYMENT DATE
Insolvency	90%	Immediately
Payment delay	90%	4 mths after due date
Repudiation of contract	90%	1 mth after disposal
Exchange transfer delays	100%	4 mths after due date
War, civil war, import ban		
Diversions of voyage, etc.	100%	1 mth after due date or loss even

BOND SUPPORT

- Unfair Calling Insurance - 95%
- Bond indemnity/insurance to financiers
 - up to 95% of cover
- "Unsecured" advance payment bonds

CAPITAL GOODS FINANCE

- Export Finance and Credit provided on competitive terms
 - by direct lending
 - by guaranteed loans from banks
- Observes terms of the OECD Understanding for official export credits
 - 15% down payment

- OECD Credit Insurance Reference Rates [minimum] based on bond rate plus 100 basis points.
- maximum term of repayment depending on goods
- starting date for repayments.
- EFIC charges establishment fee, finance fee for exporter, commitment fee for undrawn funds, 6 monthly repayments,
- EFIC will also negotiate Irrevocable Letters of Credit for small amounts for exporters.

EFIC'S MISSION STATEMENT

“To increase Australia's exports.

To provide our clients internationally competitive insurance and finance services, particularly for countries, companies and contracts which the commercial market may not have the capacity to cover.

To extend EFIC's services as far as we can, consistent with preserving the financial viability essential to the Corporation's long-term support for exporters ”

COMMERCIAL FINANCIAL RETURNS 1995/96

\$'000

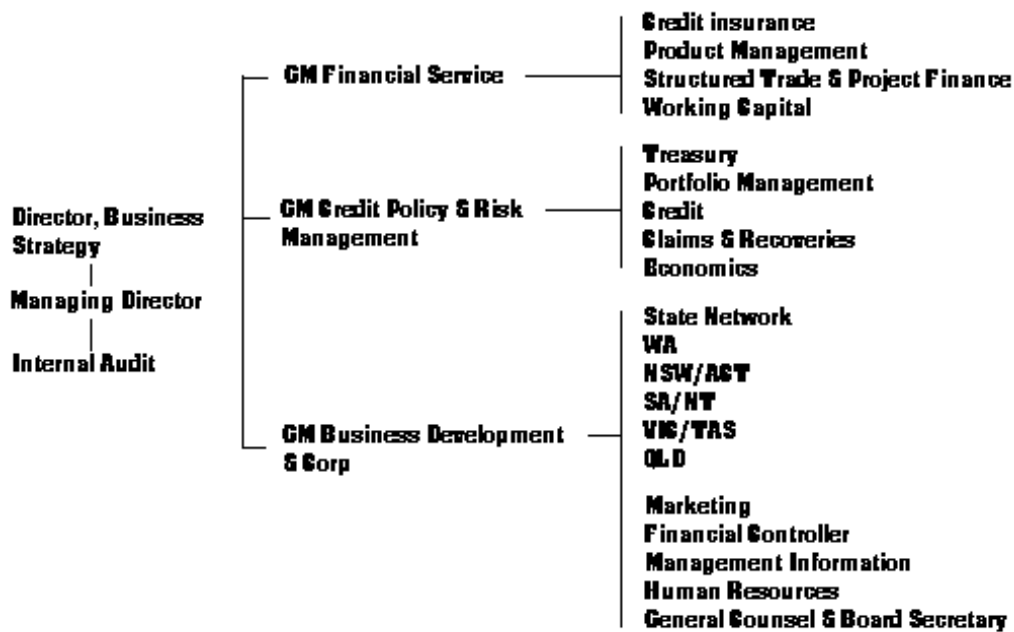
<u>EXPORT BUSINESS SUPPORTED</u>	<u>6,903,155</u>
<u>Operating income</u>	<u>43,616</u>
Investment Income	18,549
<u>Total Income</u>	<u>62,165</u>
<u>Operating Expenditure</u>	<u>25,987</u>
Insurance claims	10,030
Bad and doubtful debts	11,466
<u>Provision for bonds & guarantees</u>	<u>2,117</u>
<u>Total expenditure</u>	<u>49,600</u>
Surplus	12,565

RATIOS AND OTHER STATISTICS

Operating expenses to total income ratio	39%
Operating expenses to total receivables ratio	0.8%
Average staff numbers	185

Export business supported per employee [\$000's]	37,314
Operating income per employee [\$]	214
Operating expenses per employee [\$]	112

ORGANISATION CHART



TRADE REVIEW

ASIA AT A GLANCE

30% of total exports supported by EFIC	\$2,227 m
23% of credit insurance	\$1,492 m
77% of medium term loans disbursed	\$ 447 m
71% of new loans	\$ 282 m
51% of bond support	\$ 64 m
42% of working capital guarantees	\$ 25 m
89% of overseas investment insurance	\$ 199 m

South East Asia - Indonesia

- ❖ Largest borrower of capital goods finance
 - Some is mixed credits [with aid funds]
- ❖ A\$120 million - 49% of new loans

- telecommunications
- health & safety project
- ❖ Two Overseas Investment Policies

PHILIPPINES

- ❖ \$49 million mixed credit loans
 - for Manila traffic signal system
 - Baguio water supply
- ❖ Credit Insurance
 - \$112 million - 33% increase
 - iron & steel
 - dairy produce
 - process foods

SINGAPORE

- ❖ Credit insurance up 12% to \$135 million
- ❖ Ship sector loan
- ❖ Working Capital Guarantees
 - telephones
 - computer software
 - process equipment
 - glass re-inforced concrete

THAILAND

- ❖ Credit Insurance up 15% million to \$79 m
 - some small loans
 - first capital goods guarantee for Chiang Mai mining

MALAYSIA

- ❖ Credit insurance down slightly to \$125 m
 - one loan for abttoir

VIETNAM

- ❖ Two new loans - one commercial account
 - \$66 million overseas investment insurance for telecom network

SOUTH ASIA - INDIA

- ❖ 3rd largest medium term borrower
 - due to Pipawar Mine (1991)
- ❖ Credit Insurance \$60 million
 - 64% increase in wool

NORTH-EAST ASIA

CHINA

- ❖ Credit Insurance \$196 million - up 7%
 - iron & steel, base metals
- ❖ 15 new mixed credit loans - \$83 million
 - telecoms
 - water treatment
- ❖ 5 manufacturing investments
 - \$10 m. overseas Investment Insurance

JAPAN

- ❖ Credit Insurance \$213 million
 - 7 working capital guarantees for exporters supplying Japan
- ❖ Most trade is not insured - strong buyers, Japanese trading companies, long-term contracts.

EUROPE

AT A GLANCE

39 % of total exports supported by EFIC	\$2,935 m
44 % of credit insurance	\$2,813 m
19 % of medium term loans disbursed	\$ 111 m
19 % of new loans signed	\$ 76 m

- | | |
|-----------------------------------|--------|
| 3 % of bond support | \$ 9 m |
| 5 % of working capital guarantees | \$ 3 m |
- Credit insurance grew 15% but with higher risks
 - coal, nickel, wool, wine, hides, skins
 - main risks In Italy, UK, Germany
 - \$70 million loans for very fast ferries

NORTH AMERICA

AT A GLANCE

16 % of total exports supported by EFIC	\$ 1,173 m
17 % of credit insurance	\$ 1,091 m
2 % of medium term loans disbursed	\$ 11 m
8 % of new loans signed	\$ 33 m
35 % of bond support	\$ 43 m
46 % of working capital guarantees	\$ 27 m

UNITED STATES OF AMERICA

- Credit Insurance for \$832 million
 - iron & steel, nickel, wine
- Again the highest tally of insurance claims [35 for \$4 m]
 - working capital guarantees for manufacturers

MIDDLE EAST & NORTH AFRICA

AT A GLANCE

8 % of total exports supported by EFIC	\$632 m
10 % of credit Insurance	\$623 m
6 % of bond support	\$ 8 m
4 % of working capital guarantee	\$ 2 m

- 45% growth in insurance due to large wheat sales to Iran.
- working capital and bond support for contractors.

PAOUA NEW GUINEA, NEW ZEALAND AND THE PACIFIC ISLANDS

AT A GLANCE

5 % of total exports supported by EFIC	\$378	m
6 % of credit insurance	\$355	m
2 % of medium term loans disbursed	\$ 9	m
2 % of new loans signed	\$ 8	m
0.3 %of bond support	\$ 0.3	m
4 % of working capital guarantees	\$ 3	m
5 % of new overseas investrment insurance	\$ 11	m

- PNG has third largest EFIC exposure due to large mining projects

AFRICA

AT A GLANCE

2 % of total exports supported by EFIC	\$112	m
2 % of credit Insurance	\$ 99	m
0.2 % of bond support	\$ 0.2	m
6 % of new overseas investment insurance	\$ 13	m

EFIC - FUTURE DEVELOPMENT

- Market Research & Product Development
 - studying new markets devised by exporters
 - developing and selling appropriate products
 - conducts client satisfaction surveys
- New exporters and small and medium industries are a high priority
 - simplified policy being tested for small new exporters
- Increased emphasis on working with banks
 - Export Finance Guarantees
 - Working Capital Facilities
 - 79 guarantees this year
- Servicing the Service Sector
 - mainly services connected with the supply of goods
 - working closely with the Industry associations

PROVIDING CREDIT INSURANCE

- Proposal from exporter showing

- exporting experience
- credit management skill
- markets & buyers to be insured
- amounts of cover requested
- payment terms requested

ALSO- details of buyers they DON'T wish to cover

THEN

- face to face discussions
- to be effective cover must have
 - credit limit on bank or buyer
 - valid declaration on shipments
 - premiums paid
 - comply with all conditions
- Exporter must:
 - disclose all material information
 - show due care and diligence In making and fulfilling contracts
 - report all potential problems at the earliest opportunity
 - do nothing to jeopardise EFIC's position
- EFIC offers comprehensive cover
 - "all risks', seamless, etc.
 - selection of buyers to insure not encouraged
 - political risk only can be requested if
 - a] associated buyer
 - b] 'undoubted' buyer
- Credit Limits
 - a revolving limit which can be re-used as payments are made
 - exporters are given discretion on the level of sales up to 180 days to particular buyers
 - within rigid credit analysis condition
 - 3 trade references needed
 - 12 months good experience
- Exporters must inform EFIC of any association with buyer
- Requests for extensions of time to pay are the first sign of trouble
- Early action to minimise loss is vital for avoiding losses and making recoveries

- Claims examination is the time for serious study of each case
if conditions have not been met the claim will be refused

PROMPT PAYMENT OF CLAIMS IS THE BASIS OF THE INSURANCE BUSINESS

OPTIONAL POLICY COVERS

- Pre-Shipment Cover
 - from the time contract is agreed
 - an 'event of loss' before shipment
 - bankruptcy of the buyer
 - political blockage
- two limits to payments
 - costs actually incurred
 - value of the contract
- External Trade Cover
 - to complement local goods
 - up to 25% of turnover
- Consignment Cover
 - for overseas stockholding
 - processing in storage
 - sales form overseas stocks
- Indirect exports
 - where two Australian firms make a transaction, but the goods are destined for export at the next stage

CAPITAL GOODS FINANCE

- Export Contracts for medium/long term
 - for equipment for manufacturing, transport, communications, services which has a long working life
 - minimum terms and conditions under the OECD "Understanding" - the Consensus
- For Smaller contracts "suppliers credit" is normal
 - exporter sells directly on credit terms to the buyer
 - sale is secured by documentary credits - 'negotiated' by EFIC which pays Cash to the exporter, or guarantees the sellers bank.

- For larger contracts “buyers credit” is more normal
 - based on a loan to the buyer from EFIC or a bank guaranteed by EFIC,
 - bank loan can be guaranteed against all risks of just political risks, if the bank is willing to take the commercial risk itself.
- For large projects more diverse structures are developed - often in partnership with other country ECAS, International Financial Institutions (MIGA, IBRD, ADB, IFC, etc.)
- In ‘Project Finance’ several techniques can be used together to assemble the total financing required, e.g. in PNG
 - MISIMA ISLAND GOLD
 - PORGERA GOLD
 - KUTUBU OIL & GAS
 - LIHIR ISLAND GOLD
- These projects employed overseas investment insurance, credit Insurance, guarantees to bank syndications, direct lending, co-insurance and corporate funding.
- Major differences in medium/long, term financing from short-term credit insurance
 - much larger and longer credit exposure for the ECA
 - more complicated legal arrangements
 - innovative planning is needed
 - close co-ordination with sponsors, borrowers and other lenders/guarantors is required
 - similarities with bank corporate finance and close supervision is needed
- Previously much M/LT lending was government guaranteed
 - now greater emphasis on private sector and commercial viability
 - project, contract and buyer/contractor ‘due diligence’ now a critical part of risk management

EFIC has had an important role in financing PNG mines on a purely commercial private sector basis, although the government of PNG has been a minor shareholder in each project.

OVERSEAS INVESTMENT INSURANCE

- Developed to assist manufacturers establishing joint ventures abroad
 - insures investor equity and loans
 - has development aspect to foster Investment
 - has expanded with the growth of the private sector

- later provided cover for bank investments abroad
- cover has extended to provide political risk cover for bank loans to projects
- Investment insurance covers political risks only:
 - loss by expropriation
 - damage by war-like operations
 - inability to transfer royalties, dividends or repatriate capital