inotes
Newsletter from India's Leading Insurance Broking House
November 2013

Summary

india insure
The risk managers

Message from the Editor

Dear Readers,

There is sweet news in the air for Private non-life Insurers who have been permitted by the Government of India to underwrite Crop Insurance. This move is expected to make the experience of insuring crops farmer-friendly, according to the Ministry of Agriculture.

The Engineering Insurance portfolio of non-life insurers has been witnessing a slump against the backdrop of a sharp slowdown in infrastructure activities. The engineering premium grew by a mere 1.84% during the first quarter of this fiscal.

Credit Management is usually regarded as ensuring that buyers pay on time, credit costs are kept low, and debts are managed in such a manner that payment is received without damaging the relationship of Suppliers with their buyers. Suppliers can manage their outstanding receivables through complex financial solutions. They can also insure against bad debts through a trade credit insurance policy.

This issue of inotes attempts to elaborate the various facets of Trade Credit Insurance. Apart from highlighting the importance of Credit Insurance, the benefits that can be derived therefrom by Business Houses so as to become successful has been brought out in an a vivid manner.

In the interview section of this issue, Mr. N Shankar, Chairman & Managing Director, ECGC and Mr. Bhavesh Patel, Vice President, Specialty Lines, ICICI Lombard General Insurance Co. Ltd. speak about the evolution and development of the Credit Insurance market in India. Also, Mr. S. Hariharan, DGM, Balmer Lawrie expresses his opinion on Credit Insurance.

A case study on a claim on a Credit Insurance Policy highlights the fact that the Insurer has the onus to decide upon and direct action which they consider likely to be effective in making the recovery from the buyer concerned post settlement of the claim.

In the 'Readers Speak' column of this issue, Mr. Deepak Prasad, Head - Corporate Sales & Broking, Magma HDI General Insurance Co Ltd. and Mrs. Shobha Reddy, Regional Manager, Large Corporate & Brokers Office, New India Assurance, Hyderabad express their opinion on creation of a NATCAT Pool.

With best wishes.

V G Dhanasekaran
Editor - *i-notes*

Credit Insurance - a lifeboat for all industries

- *Have you ever experienced credit losses, especially with overseas suppliers?*
- *Have you ever experienced a default in payment due to the insolvency of your customer?*
- *Do your customers delay in making payments beyond the agreed credit period?*
- *Do you sell to new customers and in new markets?*
- *Have any of your customers declined acceptance of goods after they have been shipped?*
- *Have you ever faced a restriction by the buyer's Government resulting in delay of your payment?*
- *Is the fear of approaching a new market due to various risks hampering your expansion plans?*

If your answer to any of these questions is a 'yes', then read on.

Managing credit exposures has become one of the top risks facing businesses in today's global economy. Most trade whether domestic or exports are carried out on credit terms and one of the major risks that the organization may face is non-payment or delay in payment. As far as exports are concerned, majority of trade from India is carried on open account sales. The balance is on Letters of Credit of various kinds and/or other forms of recourse to credit.

Accounts receivable are often the largest uninsured asset on a company's balance sheet - even though it is also the primary source of revenue. Isn't it surprising that though organizations protect their tangible assets such as property and plant; they often neglect and leave open an important exposure - their receivables! Research suggests that 18% of companies go bust because they have experienced bad debt or poor working capital. This brings to focus the importance of Credit Insurance as a risk mitigation tool in both domestic as well as cross border trade.

What is Credit Insurance?

Credit insurance provides a business with protection against the failure of a customer to pay their trade credit debts. This can arise as a result of a customer becoming insolvent or because a customer fails to pay within the agreed credit period. These risks are referred to as 'commercial risks'.

Companies that export in addition to covering '***commercial risks***' can protect themselves against a range of ***'political risks'*** which may prevent or delay payment.

Two basic types of Coverage offered in Trade Credit Policy

Commercial Risks	Political Risks - only for exports
• Non-payment due to buyer insolvency • Delay in payment (Protracted Default) • Non-acceptance of goods • Contract Repudiation	• Inconvertibility • Contract Frustration due to war, civil war, rebellion etc. • Contract Cancellation by Govt. of Insured Buyer • Export/ Import restrictions • Shipment Diversion

Consider these examples:

- A fast growing Apparel company was shaken when their largest customer, a retail giant, declared insolvency. The unexpected failure caused crores of rupees in receivable losses nationwide, and left this apparel company alone facing 82 lakhs in exposure. The catastrophic loss crippled the Apparel Company for a long time and it took them more than 5 years to come back to their former state.
- A Chemical company supplied reactors to an international company that set up its operations in India as a joint venture with an Indian partner. After the reactors were supplied, the plant started operations

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but in a weeks' time some internal dispute between the joint venture partners brought things to a stand- still. The plant was shut down abruptly, employees were laid off and suppliers were left in the lurch without payments. Talks were going on between the JV partners without any definite conclusion and this continued on for more than 18 months. The chemical company which had taken a loan of 80 lakhs from the bank to carry on the work order had to keep paying interest without recovering the capital, leave alone the profit. This had a disastrous effect on the chemical company's balance sheet.

- Days after announcing an unexpected loss of more than 250 crore due to an elaborately concealed financial swindle, a previously top-rated IT company files for insolvency. A year later, the company's Annual report paints a far bleaker picture, with losses totaling 1000 crore resulting from six consecutive years of misstated financial statements. The manipulation had been intentionally concealed from auditors, and left suppliers and investors shaken. Suppliers who had obtained insurance for their receivables emerged from the disaster unscathed while many others were not so well prepared.

A buyer risk is one aspect while a foreign government problem is another, often perceived to be beyond the insured's control, making it difficult to predict. A good example of this risk was when the Russian government declared a moratorium on all foreign debt in 1998, including trade debt, as a measure to keep hard currencies in the country during its financial crisis.

Commercial as well as Political risks can jeopardize the continued existence of the Company. Late payments slow down growth and reduce profitability because fewer financial means are available to carry out the necessary investments. Invoices that remain unpaid also cause liquidity problems. Consider this example - If a company's profit margin is five percent and one of its customers defaults on debt of Rs. 10,00,000, the company will have to produce additional sales of Rs. 200,00,000 to make up for the lost profits.

Types of Credit Insurance Policies

Credit insurance policies offered in India are of 3 types:

- Whole turnover policy - covers all customers of the policyholder
- Key account Policy - covers the policyholder's largest customers
- Single-buyer Policy - covers a single buyer of the policyholder

Insurers in India are only allowed to sell the Whole turnover policy as per insurance regulations while ECGC (Export Credit Guarantee Corporation owned by Govt. of India) is permitted to sell all kinds of credit policies. The Insurance Regulator IRDA had imposed restrictions on credit insurance in 2010 in the wake of large defaults on credit insurance policies issued by a state-owned insurer.

Currently, ECGC provides most of the coverage, accounting for about 80% of the premium paid for credit insurance while the rest is covered by private insurance companies. Private insurers offer credit cover for domestic sales as well as exports while ECGC covers only exports. India's ratio of trade covered by credit insurance to GDP is around 5%[1] compared to about 10% for China and around 20% in some of major European economies. Many reasons contribute to the low penetration in India including lack of product awareness, self-insurance (maintaining sufficient bad debt reserves), budgetary/cost constraints and limited distribution channels in marketing this specialty product.

Globally, the 'Big 3' (Euler Hermes, Atradius and Coface) dominate the credit insurance market and have been estimated to have a combined global share of 85% of credit insurance premiums. They operate in and out of a growing list of countries and hold credit information on millions of buyers worldwide. Even insurers in India have tied up with these global leaders to offer credit insurance.

How credit insurance works?

The focus here is on the Whole turnover policy as it is the most common form of credit insurance. The Whole turnover policy covers the policyholder's entire customer base for a one year period. Whole turnover policies can be based upon domestic or export trade, or a mixture of both. The cover provided by most insurers is aimed at contracts on credit terms of up to 90-180 days.

Factors considered in Premium Computation: The policyholder has to make estimations of the sales turnover for the coming year and a provisional premium is calculated, based on the expected turnover. The elements considered in the premium calculation are the proposer's industry, the country to which exports are made, the sales turnover, the claim history, the largest customers, the risk spread, terms of payment, etc. Because of the spread of risk, premium rates are usually competitive in a whole turnover policy. The premium can be paid in monthly / quarterly installments and is subject to adjustment at the end of the year based on actuals.

Credit Limits: The insurer analyzes the credit worthiness and financial stability of the policyholder's customers and assigns them a specific credit limit (based on the maximum outstanding amount anticipated during the life of the policy), which is the amount the Insurer will indemnify if that insured customer fails to pay. Underwriting control is exercised primarily through a credit limit set for each buyer covered. The Insurer also assesses country risks and may have a Country limit of liability which is the Insurer's maximum liability for all loss in each particular country. For political risks, ECGC has divided countries into two groups. For countries under the open cover category; political risks are automatically covered under credit policy for exports. For restricted cover countries; prior approval of ECGC is mandatory for political risks cover to be available.

For larger limits, the figure is set specifically by the insurer, but it is common for policyholders to have discretion to set limits for smaller customers without reference to the insurer, on the basis of their credit and collection procedures. When a **Discretionary Credit Limit** is granted to the policyholder, he can decide on the credit limit as long as the exposure remains below the discretionary limit set and the decision taken is along the rules that are set in the insurance contract.

Commencement of Cover: The cover commences on delivery for a local sale and on shipment for export of goods. For technical or professional services provided, cover commences on performance of the services for which payment is due.

Declarations to be made: Transits/ Shipment details must be declared monthly /quarterly by the policyholder in a prescribed format within 30 days of the end of the quarter. At anytime during the policy's life, the insured can request additional limit for trade with any existing customers or cover for any new customer being planned to acquire. After evaluating the risk, the Insurer takes a call of increasing the coverage and will either approve the additional credit limit request or decline it with a clear explanation.

[1] *http://www.thehindubusinessline.com/industry-and-economy/india-needs-a-flexible-credit-insurance-regime-for-sme-prosperity/article4474744.ece*

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Interview – *Corporate & Insurers*

In the interview section this issue, we have *Mr. N Shankar, Chairman & MD, Export Credit Guarantee Corporation of India* and *Mr. Bhavesh Patel, Vice President, Specialty Lines, ICICI Lombard General Insurance* sharing their views on the credit insurance market in India.

From the Corporate side, we have *Mr. S Hariharan, Deputy General Manager (Finance), Balmer Lawrie & Co.* providing insights on the awareness levels of credit risks in India and the benefit he perceives in opting for credit insurance.

Insurers

What is the size of the credit insurance market in India? How does it compare to its peers and global standards?

Mr. N Shankar, ECGC: The size of export credit insurance market is roughly of the order of Rs.2,75,000 crores (in terms of Sum Insured). During 2012, Berne Union, an Association of Credit Insurers worldwide has insured about 10% of world exports. ECGC provides insurance cover to around 7.72% of India's exports. ECGC's short term business is about 95% of the total insurance market. Thus size of credit Insurance business in India is close to that of the global standard.

Mr. Bhavesh Patel, ICICI Lombard: While there is no dedicated tracking of Trade credit insurance premium at an industry level, market estimates place it at being around INR 500 cr. The export credit insurance market in India would be upwards of Rs. 375 cr (GWP basis). The domestic credit insurance market is estimated to be more than Rs. 100 cr.

The global market for Credit insurance is estimated to be around USD 7/8 bn. Three mono-line Credit Insurance companies (Euler Hermes, Atradius & Coface) control about 85% of this market globally.

What are the key parameters factored in to arrive at the premium of Credit insurance?

NS: Broadly, the premium rate is based on the terms of payment involved in an export transaction and the country of destination of exports. As premium rates are arrived at using various parameters; it varies product-wise.

BP: The premium is determined by taking into account the total sales volume to be covered, level of trade losses in the portfolio, risk factors of the sector and spread of buyers. In exports, the country rating and risk is an additional factor influencing premium.

Which are the industries more keen on seeking Credit insurance and amongst them, which is the industry from where the maximum number of proposals for this cover come from?

NS: Covers for banks form 60% of the total portfolio. The major industries which are into exports viz., engineering goods, readymade garments, textiles, leather products, agricultural commodities, gems/ jewellery and pharma generally do business on credit terms on many occasions without L/Cs where the risks of non-payment by the overseas buyers, countries and banks are high. Currently, the highest value of business covered is in respect of engineering goods, followed by agricultural products and leather manufactures.

BP: All Industries which have substantial credit sales exposure would be keen on Trade Credit Insurance. The Indian Credit Insurance landscape is quite diverse with portfolio across all major industries like IT, Infrastructure, Textiles, Chemicals and Consumer durables. However, IT distribution and Consumer electronic companies are the biggest users of this product.

How has the frequency and severity of credit insurance claims changed over the past few years? Which is the industry from where the maximum numbers of claims arise?

NS: The Corporation paid total claims of Rs.713 crores in FY 2011-12 the highest in its history. The global economic slowdown of 2008-09 brought about an increase in the claims post 2008-09**.** The claims were mainly from Agriculture products (including dairy products and processed foods), Chemicals & Allied Products, Engineering goods, Cotton (fibre, yarn, fabrics made-ups including handloom) and Granite. During FY 12-13, the highest numbers of claims were from readymade garments, other commodities, engineering goods, agriculture products and chemical allied products.

BP: The frequency and severity of claims is largely a function of the state of the economic cycle. For example, in 2008-2009, credit insurers were flooded with claims due to the global financial and economic meltdown.

This year too has been tough with claims across all sectors including some very large claims. Since the market has huge exposures in the IT distribution and Consumer electronic sectors, claims tend to be more severe / frequent here.

However, over a period of time and by implementing good underwriting practices and debt recovery management, loss ratios are controlled and credit insurance policies are generally profitable for the insurers.

The end of Sep 2010 saw IRDA banning all forms of credit insurance (except through ECGC) and 3 months later allowing insurers to provide limited trade credit protection. What has been the impact of this on the Indian credit insurance industry? Has the industry been able to limp back to normalcy over the past 2 years?

BP: The Regulatory disciplinary action did impact the Credit Insurance market adversely, especially the non ECGC players in the market. Under the revised guidelines issued, the market is slowly limping back, although the limitations imposed are still a drawback. There are limitations in terms of % of indemnity and assignment of policy is not currently allowed, which still seriously impacts the export credit and finance backed trade credit insurance, segments of business for the non ECGC players.

But all the non ECGC players have been working hard to develop the Domestic Credit insurance market, and reasonable progress has been made in the last 2 years. Having said that, there is definitely a lot of scope for this product in the future.

ECGC, being a tried and tested Insurer certainly continues to have a higher recall for Credit insurance. What is your USP for a customer to opt for a credit insurance policy from you rather than ECGC?

BP: ECGC is a very old established Government owned company with an extremely wide distribution network. They have a wide range of products as well like single buyer, multi buyer policy, etc. The new regulations put in place by IRDA in 2010 have put a lot of restrictions on private companies like banning single buyer policies, offering only 80% indemnity instead of the 90% offered earlier, no assignment to banks, etc. These restrictions do not apply to ECGC and therefore, there is no longer a level playing field between ECGC and the other players.

However, we can cover both exports and domestic sales which is a great differentiator for us. Our policies come with powerful buyer assessment and debt recovery features by virtue of our reinsurance tie-ups with global trade credit insurance giants like Coface. Claims settlement is seamless and the client gets a lot value added services along with indemnification.

These cutting edge features of our solutions coupled with very aggressive pricing attract quality SME and large corporates to avail of our services.

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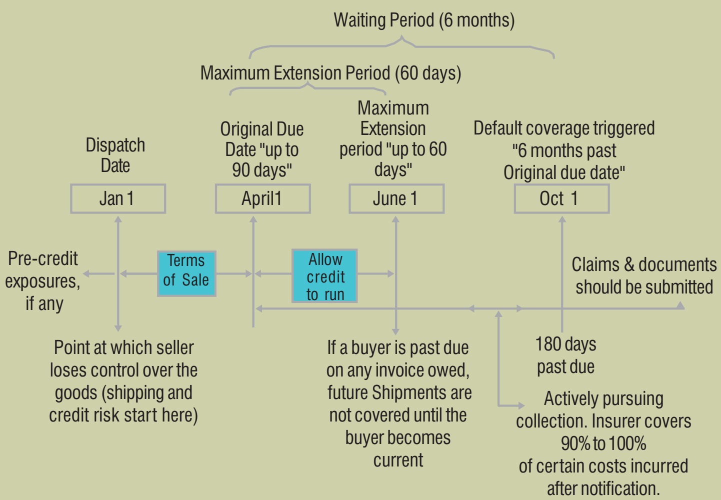
Deteriorating credit conditions: Throughout the policy period, the Insurer pro-actively monitors the credit worthiness of the policy holder's customers. If the information obtained at any point of time indicates that any of the company's customers is experiencing financial difficulty, the Insurer will notify the Insured of the increased risk and help establish an action plan to mitigate and avoid loss. Also the credit limit granted to a customer can be changed at any time, depending on new information available to the insurer. However, any restrictive decision will apply to future transactions only.

Risk Sharing: Like all insurance, credit insurance involves some aspect of risk sharing rather than 100% risk lay-off. Typically 80-95% of invoice value is covered by trade credit insurance, with some insurers giving a higher percentage of cover for vetted customers as compared to discretionary limits.

Limit of Liability: The credit policy also has a limit of liability which caps the aggregate value of claims that will be paid by the insurer during the policy period.

Claims Handling



Unlike other insurances, there is an extension period and waiting period in this policy.

Extension Period: The policy holder has the option to grant extensions to his customer for payment beyond the due date (as per sale contract) but within the maximum credit period specified in the policy without prior approval of the Insurer. The date thus set is called the extended due date. If the debt /outstanding receivable was not paid in full at the extended due date, the Insurer must be informed since this communication is also the start of a waiting period for protracted default.

Waiting Period: There is a waiting period of 4-9 months (varies between policies of insurers) from the due date in case of protracted default before the claim is paid out by the Insurer. In case of insolvency, liability is upon admission of the claim by an appointed liquidator. The waiting period shall not apply to a buyer that is insolvent.

Debt Collection: If the policyholder organizes the debt collection after the extended due date, prior approval must be sought for the expenses from the Insurer. If these are reasonable, the expenses are added to the insured debt and paid at the time of claim.

Some of the large credit insurance claims in India in FY 2013*

Industry	Gross Loss Amount (in Rs. lakhs)
Electronics	1200
Engineering goods	400
Engineering goods	292
Manufacturing	255
Aviation	150
Engineering goods	140
Manufacturing	124
Manufacturing	100
Manufacturing	99
Manufacturing	80

* Data excludes ECGC claims

What the policy does not cover

As important as it is to know what credit insurance covers, it is equally important to know what it does not.

- Disputes between the Insured and his customer must be settled in the Insured's favor to maintain coverage for a disputed sale.
- Sales contract made with government departments and local authorities in the Insured's country.
- Sales contract made with associated companies or sister concerns.
- Decision taken by the government of Insured's country that hinder the execution of the sales contract or prevent the payment of the debt.
- Sales made on terms of cash on delivery, and confirmed or unconfirmed irrevocable letter of credit.
- Certain limitations for risky countries or risky sectors may be incorporated into the policy. For example, insurer may have a maximum limit or may impose an additional claims waiting period.

Key Points to bear in mind

Contrary to other insurance policies, credit insurance requires a much greater active participation by the insured during the proposal stage as well as the life of the policy. A detailed proposal form needs to be filled up and the information given to the insurer has a direct bearing on the cover received.

When using credit insurance, it is important to remember these key points:

- The credit period granted to customers must not exceed the 'maximum credit period' specified in the policy.
- Quarterly Declarations on transits/shipments must be made in the prescribed format within the timeline specified in the policy. In case of nil shipments during the period, submit a 'nil' declaration.
- The policyholder shall report to the Insurer on a monthly basis details of receivables for any customer that is overdue (past the due date in the contract of sale) for more than 30 days.
- If the debt /outstanding receivable was not paid in full at the extended due date, the Insurer must be informed.
- The Insurer must be notified in writing as soon as the policy holder becomes aware of any adverse information concerning his customer.
- Claims must be filed with Insurer on completion of waiting period but no later than 6 months after the Waiting Period has expired. (varies between insurers)

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Report Card - September 2013

Gross premium underwritten by non life industry for and up to the month of September 2013* (Rs. In crores)

INSURER	SEPTEMBER		GROWTH OVER THE SAME PERIOD OF PREVIOUS YEAR (%)	APRIL - SEPTEMBER		GROWTH OVER THE SAME PERIOD OF PREVIOUS YEAR (%)
	2013	2012		2013	2012	
New India	874	757	15.5%	5,729	5,100	12.3
United India	753	741	1.6%	5,100	4,763	7.1
National	833	741	12.4%	4,779	4,355	9.7
Oriental	607	539	12.7%	3,687	3,299	11.7
ICICI-Lombard	512	510	0.3%	3,404	2,860	19.0
Bajaj Allianz	342	292	17.2%	2,209	1,884	17.3
AIC	496	722	-31.4%	2,006	1,816	10.4
HDFC ERGO	291	288	1.3%	1,472	1,245	18.3
IFFCO-Tokio	274	270	1.8%	1,472	1,252	17.6
Reliance	187	159	17.8%	1,274	1,041	22.3
Tata-AIG	176	158	11.5%	1,225	1,044	17.4
Cholamandalam	143	125	14.8%	906	787	15.2
Shriram	127	127	0.0%	742	693	7.0
Royal Sundaram	102	110	-7.4%	722	751	-3.9
Bharti AXA	95	87	8.6%	701	572	22.6
Future Generali	102	87	17.9%	613	552	11.1
ECGC	117	103	13.4%	601	541	11.0
SBI General	88	58	52.8%	541	296	82.8
Star Health	110	89	24.2%	478	400	19.6
Universal Sompo	40	43	-8.3%	276	247	11.6
Apollo Munich	44	35	24.0%	234	214	9.2
Magma HDI	33			166		
Max BUPA	25	14	78.3%	130	77	69.0
L&T General	19	10	85.4%	120	79	52.0
Religare	8	1	509.4%	78	10	648.8
Liberty	8			39		
Raheja QBE	2	2	-1.8%	13	10	23.6
PRIVATE TOTAL	2,728	2,464	10.7%	16,817	14,015	20.0
PUBLIC TOTAL	3,680	3,603	2.1%	21,901	19,875	10.2
GRAND TOTAL	6,408	6,067	5.6%	38,718	33,890	14.2

* Source : IRDA

Observations: Performance for April - September 2013

- The non-life industry has registered a growth rate of 14.2% upto the month of September 2013. Total premium collected by general insurer's upto the month of September 2013 was Rs. 38,718 crores vis-à-vis 33,890 crores upto September 2012.
- The accretion achieved by the PSU's during the period April - September 2013 is Rs. 2,026 crores while the private players have achieved Rs. 2,802 crores towards the overall market accretion of Rs. 4828 crores.
- The PSU's have registered a growth rate of 10.2% during the period April-September 2013 vis-à-vis 17.5% for the same period last year while the private players have registered a growth rate of 20% during this period compared to last year's 19.9%.
- The major contributors have been: New India with an accretion of Rs. 629 crores, ICICI Lombard with an accretion of Rs. 544 crores, National with an accretion of Rs. 424 crores and Oriental with an accretion of Rs. 388 crores.
- In terms of growth during the period April - September 2013, SBI General registered a growth of 82.8% followed by Max Bupa at 69%, L&T General 52%, Bharti Axa 22.6% and Reliance General 22.3%.
- The market share of the PSU's has decreased collectively from 58.6% to 56.6% for the period April - September 2013 while the private players have increased their market share collectively from 41.4% to 43.4% during the same period.

- In the event of any payment of a loss under this policy, the Insurer shall be subrogated to all of the policyholder's rights of recovery.

Importance of Credit Insurance

Credit Insurance offers one of the most efficient and cost effective ways of managing credit risk for any enterprise. The key is having the right information to make informed credit decisions and therefore avoid or minimize losses.

It is important to note that Credit insurance does more than just ensure that invoices are paid. It can help a business succeed by providing the following benefits:

- Safer business expansion
- Intelligent market prospection and Customer insights
- Protecting the Company balance sheet
- Better borrowing and financing options
- Debt Collection

Conclusion

The global crisis has sharply brought to focus the importance of Credit Insurance as a risk mitigation tool in home trade as well as cross border trade. With the increase of world trade, many companies are entering new markets and extending their supply chains across multiple regions – all of which further increases the need to protect themselves from risks involving commercial trade debts. Credit insurance thus can be a very effective tool in accelerating cash-flows, improving working capital and protecting the balance sheet. In the midst of a global recessionary climate, with an increase in the number of insolvencies forecasted and the tightening of credit across the board, credit insurance is more important than ever for a business' success.

News TitBits

Public non-life insurers finally form healthcare TPA

Source: Asia Insurance Review

The 4 public general insurers have finally incorporated their common in-house health insurance TPA. The company will start operations in April 2014. It has been named as 'Health Insurance TPA of India' and was incorporated on 14 August and has held its first board meeting. Mr G Srinivasan, the chairman and MD of New India Assurance is the chairman of the board of the TPA company which is based in New Delhi.

IRDA extends new norms for life insurance plans by 3 months

Source: Livemint.com

IRDA has agreed to extend the deadline of new product regulations for the life insurance industry to 1 January 2014 from 1 October 2013. IRDA's new products guidelines—namely linked insurance products regulations and non-linked insurance products regulations—aim to make insurance policies friendlier for customers.

IRDA allows banks to act as insurance brokers

Source: The Economic Times

IRDA has allowed banks to act as brokers to increase the penetration of the sector across the country. There is no capital requirement for insurance broking business carried out by banks. To qualify for the licence, each bank will have to have the principal officer - an officer of general manager or equivalent category, who is appointed exclusively to carry out the functions of an insurance broker.

Will creation of NATCAT pool provide the much needed respite at the time of natural disasters? Are there any other viable options for natural catastrophe risk transfer?

In the last issue of inotes, we had invited our Readers opinion on the above topic.

Response from Mr. Deepak Prasad, Head – Corporate Sales & Broking, Magma HDI General Insurance Co Ltd.

Creation of the Pool will not bring any relief. It can only help to increase the capacity in the country. At the end of the day, the right kind of rates bring about resilience, whether within the country or in the international market. The advantage of a NATCAT pool to manage risks within the country is that it will ensure the Indian market stays insulated from adverse experience internationally.

By separating cat risks from non-cat risks, the insurance premiums might shoot up for the customer in the early stages, till a reasonable corpus is created. What is important is that the pool managers should have the wisdom to understand what the optimum size of the pool should be, beyond which lenience could be shown on the rates.

Government support should not be counted on, in any commercial venture. Ideally, Government should create pools through contributory schemes or fund allocation to take care of the poor and the marginalized who need assistance.

Preferably, the cover can be made mandatory for home owners who would be left without any recourse after a tragedy. This could, in fact, be a one-time collection at the time of registration of the property. Commercial ventures should take care of themselves. We should also start thinking in terms of Natcat Bonds which will bring in stability.

Response from Mrs. Shobha Reddy.G, Regional Manager, Large Corporate & Brokers Office, New India Assurance; Hyderabad

India with its vast geographical area is exposed to varied climatic conditions. If the recent trend of increasing Multi NatCat events is any indication then, the time has come for Indian insurers to examine the unpredictable effects of climatic changes and start planning for future.

If as of now, the losses for the Indian insurers are not alarming, it is mainly due to low insurance penetration coupled with NatCat occurrences in less developed areas. Had the realization dawned on the likely impact on the national economy, had these losses occurred in areas of high value concentration/well industrialized areas; concrete efforts would have been initiated for improving the possibilities of catastrophic management with Pool as one of the solutions.

To make Nat Cat Pool a success, commitment is required from all parties concerned. We already have the experience of operating the Indian Market Terrorism Risk Insurance Pool. However in the case of Nat Cat Pool it would be appropriate if Multi NatCat pool is conceptualized to provide a comprehensive diversified coverage with no scope for selectivity. Since we do not have a strong data base for risk analysis, to start with insurers can explore the following possibilities:

1. NatCat premium component to be made mandatory for all risks including personal lines of insurances. This would ensure a wider spread and diversification of risks thereby facilitating competitive pricing for the unpredictable Nat Cat losses. Over a period of time this would pave the way for building up capacities.
2. Awareness on the cover to be created at all levels more specifically at financier's level.
3. Irrespective of location, uniform rate to be adopted across the country for risks to be segregated on the lines of viz. industrial risks/non industrial risks/personal lines of insurances, etc. This will make the process of administering the pool easier since the premiums can be bifurcated to Nat Cat premium and Non Nat Cat premium.
4. Simultaneously a database on the risks is to be created, for scientific improvement on the rating based on loss experience.

"Views expressed herein are purely personal and do not reflect the views of the Company"

Background

Axom, an upcoming telecom company was in the process of establishing its market presence in Qatar. For this purpose, it tied with several distributors in Qatar to promote sales of its product - the mobile phone. A year later, in 2005, Axom decided to terminate the distributor contract of one of its agent "Jameel Enterprises" in Qatar on grounds of failure to do enough to promote sales. "Jameel Enterprises" protested the termination, demanded compensation and refused to pay for some shipments amounting to value in excess of Rs. 15 lakhs made immediately prior to the notice of termination.

Jameel also threatened to commence proceedings against Axom in respect of the distribution contract. This made Axom anxious that "Jameel Enterprises", whose principal was a man of high status, would make it difficult for them to operate successfully in the region and were also concerned of the threat of a large counter claim against Axom. Matters drew on without a conclusion and neither party made any move towards legal proceedings, but several meetings were held and correspondence exchanged.

The Issues

Axom had a trade credit insurance policy with Lighthouse Insurance Company to cover losses resulting from the failure of trade debtors to pay amounts due from them. As per the terms of the insurance policy, Axom declared the payments for the goods sold as overdue and eventually, submitted a claim under the "protracted default in payment" section of the policy.

The Insurer agreed to pay the claim but before that requested that

Next Issue: *Banks as Brokers*

IRDA has recently allowed banks to act as brokers and sell products of more than one insurer so as to increase the penetration of the sector across the country. There is no capital requirement for insurance broking business carried out by banks. These new regulations will lead to an open bancassurance architecture and will drive banks to align their interest with their customers by offering them a wider choice of products.

Would these new regulations lead to much needed deeper penetration and enhance distribution for the insurance industry?

Your opinion is solicited.

Please send your responses in 200 - 300 words to knowledge@indiainsure.com

News TitBits

Chidambaram launches IRDA's insurance repositories system

Source: smetimes.in

FM P. Chidambaram inaugurated insurance repositories, which will help policy holders keep insurance policies in electronic form and undertake modifications and revisions.

fulfilling Policy Obligation

Axom sign a 'Letter of Undertaking' which included an obligation that *"We (Axom) will continue to take action against the debtor…..to recover the outstanding debt in full"*. Axom signed and returned the letter and Lighthouse paid the claim subject to Axom "continuing its action to obtain payment".

Eventually, in 2006, the Insurer checked with Axom on the action being taken on the debtor and requested a report of progress on the legal proceedings. Axom pointed out that they had decided at an early stage not to take the legal proceedings route for commercial reasons and restricted their pursuit to occasional letters and meetings and have finally written it off as a bad debt. Lighthouse claimed that Axom had failed to take all reasonable, prudent and practical measures to recover the debt as required under the terms of the policy. The Insurer immediately requested repayment of the money paid against the claim, with interest, on the grounds that Axom has not preserved the recovery rights of the insurer. Axom refused to comply and Lighthouse commenced proceedings against them.

The Outcome

In the Court, the Insurer explained that they have been prejudiced by Axom's failure to enter proceedings against "Jameel Enterprises" and, thus, Axom was in breach of policy terms, making them liable to refund the proceeds of the claim, which had been paid conditionally. Axom in turn clarified to the Court about the problems of entering legal proceedings in Qatar and the likely damage to Axom's business if such a course were taken. They also pleaded that the instructions from the Insurer were imprecise and the Insurer had not made it clear that they expected legal proceedings to be undertaken.

The Judge examined the policy wordings which included the following clause:

(ii) You will take all practicable measures available to you to prevent any loss arising (to you and/or us) and should any loss arise to minimise it.

(iii) After we have made a claim payment to you in respect of an INSURED BUYER you will continue to take all practicable measures to collect or realise or apply any SALVAGE and if required by us you will assign the relevant INSURED DEBT to us and we shall account to you for any uninsured proportion of any recoveries.

While the Learned Judge criticized the lack of clarity with which Lighthouse had expressed its expectations; he also made it clear that the Insured had no right to proceed entirely on their own opinion of what was the reasonable action to take. It was for the Insurer to decide upon and direct action which they considered likely to be effective in making recovery. Axom was bound to return the claim payment because they were in breach of the terms of the insurance contract. Additionally, the Court held that Lighthouse had not failed to mitigate its loss by failing to pursue the claim itself pursuant to its rights of subrogation as it was entitled to rely upon Axom's agreement to do so. The Court went further in making the observation that, on strict interpretation of the policy, the original dispute over the distributorship agreement was a "dispute" as defined and would have entitled the insurer to decline to consider the claim until that dispute had been settled.

Interview – Corporate & Insurers.... Contd. # 3

Do you have a declined list of industries? / Which are the industries from which more claims come in?

BP: There is no decline list as such. However, we do have a low to high risk grading of all industries which is an integral part of the underwriting process.

The only industry which we avoid is the Gems and Jewellery sector.

Do you have a declined list of countries? Which are the countries from where more claims arise?

NS: ECGC country Risk Classification comprises of 216 countries. We carry out an internal assessment of country risk and grading of countries is updated on quarterly basis based on the risk perception. As of 30th June, 2013, there are 179 countries in Open Cover category where branches are delegated with powers to underwrite export transactions. Countries where risks are perceived to be very high are placed in two separate Restricted Category lists and exports to these countries are underwritten on a case-to-case basis at HO level. As of September, 2013, there are 27 countries in Restricted Category I and 10 countries in Restricted category II. Please refer to our website www.ecgc.in for our latest list of country classification.

During FY12-13, the top five countries from which claims arose are USA, UK, Italy, Brazil and Spain.

What do you think is the prime reason for Credit insurance not catching up with industries as it ought to have? How do you think that insurers/ brokers can create more awareness regarding this line of business which is still considered Niche and one which requires selective selling?

NS: Generally exports with L/Cs of reputed banks don't require credit insurance. Also, exporters have a wrong perception that past experience would hold good for future and take unwarranted risk. Post 2008-09 they were proved wrong as many insolvencies occurred.

BP: Export credit insurance has good penetration in the market. Domestic credit insurance requires a lot of concept selling and by virtue of the complicated nature of the product, the sales cycle has a long gestation period. Some brokers/channel partners lose interest due to this reason.

However, there is a need on part of intermediaries to educate their clients about all the benefits of credit insurance. We have also organized seminars and knowledge conclaves dedicated to credit insurance for both our existing clients and good prospects. We intend to continue organizing such events.

We are confident that as more and more companies adopt global best practices in risk management, awareness and demand for this product will grow significantly.

In the financial year 2012, the brokered premium of credit insurance has been just 0.5% of the total credit premium. How do you think the broking channel could be utilized in improving the marketing of this line of business?

NS: Generally insurance brokers are oriented towards selling life/non-life products. They need special training to sell credit insurance products. Hence currently their contribution to the business is limited.

BP: As mentioned earlier, brokers need to educate themselves better by interacting extensively with credit insurance underwriters. As initiated by ICICI Lombard, there is a need on part of the brokers to organize seminars and conclaves for their clients and prospects, dedicated to credit insurance.

What are the likely factors that will drive the robust growth of credit risk insurance in India and what are the challenges?

NS: Increase in exports will drive the growth of credit insurance. Self insurance and re-insurance availability are the challenges for credit insurance.

(Contd... 08)

Interview – Corporate & Insurers.... Contd. # 7

BP: Credit risk management is a key component of any organization's risk management framework. As more and more Indian companies adopt global risk management practices, demand for credit insurance will increase and will result in a significant expansion of the market.

The primary challenges remain the perceived "high cost" of the product along with the tight regulations which have not allowed flexibility and innovation in product offerings.

How do you see credit insurance picking up in India in the next decade?

NS: We can target covering 15% of India's exports in the next decade as the risk awareness amongst exporters increase and higher value of exports is transacted on non-L/C terms.

BP: The market for credit insurance will definitely expand rapidly as we see a convergence between the penetration rates of credit insurance in developed countries and the Indian market in the next decade.

Corporate

What is your view on the awareness levels of credit risks and risk mitigation among Indian corporate today?

Mr. S Hariharan, Balmer Lawrie & Co: I would rather say that the awareness level of credit risks among the Indian Corporate is not very high except in case of banks/NBFC. Such being the case, the degree of defaults is also very high (even in case of Banks/NBFC) leading to higher provisioning for bad debts in the Accounts.

Balmer Lawrie has been in operation since over 140 years. At what point in time did the credit insurance policy become part of your insurance program and why?

SH: Credit Insurance Policy has become part of our insurance program since 2006. We had faced difficulties in realizing our debts which, in a few cases (including corporate clients), had become bad resulting in write-off.

How have you benefitted by opting for this credit insurance policy?

SH: The scheme has given us some amount of confidence with respect to collection of unsecured credits. This is particularly because of the stringent KYC norms adopted by the Bankers before providing the creditworthiness of the client., based on which the proposal for insurance is given. This has given us room for selection of customers which ultimately improves the top/bottom line.

In case there has been a claim reported under the policy, how would you describe your overall claim experience?

SH: There is no claim reported in the last so many years.

Although credit risk has always been present, it has exacerbated over the last decade. What do you think are the root causes of increased credit risk?

SH: The real reason for credit risk is mainly due to mushrooming of corporates and NBFCs and the way the credits are extended without assessing the KYC norms. Above all, the risk is mainly due to trading beyond capacity and the motive.

Do you believe that the credit insurance policy available today is aligned to completely meet your requirement? If no, what are the areas of improvement you would look for?

SH: We are satisfied with our present credit insurance policy which meets our requirement. Though there were no claims, we have become very mature in selecting the customers and extending credit. However, we are continuously trying to make improvements in the policy which will make the underwriting more effective and business oriented.

"Views expressed herein are purely personal and do not reflect the views of the Company"

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