



Trade Credit Insurance: A Part of Doing Business

Inter-company credit is the main source of the world's commercial credit. Extending credit to customers is the norm in many industries, including the cotton, textiles and apparel sectors. In many cases it is something that companies must do to remain competitive. In providing trade credit, suppliers afford customers the ability to generate revenue before paying; however, in the process, they assume the extra commercial and political risks of their customers and bear the additional costs of financing working capital for an extended period.

Because companies spend years building trust and developing strong relationships with their customers they may be willing to accept delinquency and payment delays as a "cost of doing business" and in an effort not to jeopardize valued relationships. This approach may make sense when viewed through the individual customer lens; however, when you extrapolate the risks associated with trade receivables management across a company's entire customer base and look at the potential impact on a company's balance sheets and its ability to effectively manage its cash flows, it can become quite scary. Managing trade receivables can also be expensive and time consuming and diverts resources from a company's core business.

The global economic downturn led to countless bankruptcies, which inevitably left suppliers waiting for payments that never came. The challenge for many companies is how to grow their business and maintain strong relationships with their customers while insulate themselves from their customers' commercial challenges and financial problems.

Trade Credit Insurance: Mitigating Risks and providing other Benefits

Trade credit insurance provides companies with much needed protection. It shields companies from possible payment default by customers. This could include uncollectable accounts, delayed payment (protracted default), unilateral contract cancellation failure due to bankruptcy. Depending on the insurer, companies may be required to insure their entire portfolio of customers or just their key accounts.

Trade Credit Insurance benefits suppliers in a number of different ways.

- It provides peace-of-mind by reducing a company's overall exposure to nonpayment
- It allows companies to sell more goods on credit terms to customers in order to increase sales
- It provides companies with a tool to evaluate potential customers and explore new opportunities and/or new geographies that may be perceived to be of higher risk allowing them to make better business decisions
- It helps secure future cash flows
- It can mitigate the impact of the insolvency of a key customer and allow a company to secure more favorable lending terms
- It can serve as an alternative to fixed-asset collateral when looking for bank financing

Case Studies: Purchase Order Finance
