Credit and political risk insurance in trade finance

TXF RESEARCH

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Foreword

Welcome to TXF's inaugural report on credit and political risk insurance (CPRI) in trade finance. It is certainly timely, with the market at an interesting juncture amid the pandemic, and also structurally, amid calls for greater ESG-related support, and in the wake of frauds, particularly in the commodities sector. This report goes deeper into some of the trends, both anecdotal and quantitative, that are driving the market through the current crisis. In here, you can learn how the players providing and using cover in the sector – in short-term trade, export, and project finance, believe the market is responding.

One thing that does shine out is that, so far, for the private insurance market, it's been more robust than many had feared both in terms of capacity and claims. For sure, CPRI is countercyclical, but claims have not yet materialised in the volumes expected at the beginning of the pandemic. It is still early days, and as state support unwinds in various markets at different rates, sentiment may change too, as will the need for restructuring.

Insurance helps mitigate risk and facilitates trade, but that comes at a cost. In the crisis, was it expensive, and was it worth it? Inquiries for credit risks on private obligors, as against, public obligors have been very high over the pandemic.

Building back better is the mantra in many markets after the crisis, and the importance of ESG-related finance is increasingly the spotlight. Nonetheless, it's important to caution the dominance of the extractive industries for the CPRI market itself. The private market will increasingly be called on both to cover and, paradoxically, also to ignore the non-renewables market. It will be an interesting balancing act.

We'd like to thank the 91 survey respondents, and the 15 interviewees who added context to the survey results, for their time in contributing to the survey and their valuable insights and we'd welcome your feedback so this valuable research can be deepened in the future.

Katharine Morton,
Head of trade, treasury and risk

Executive summary

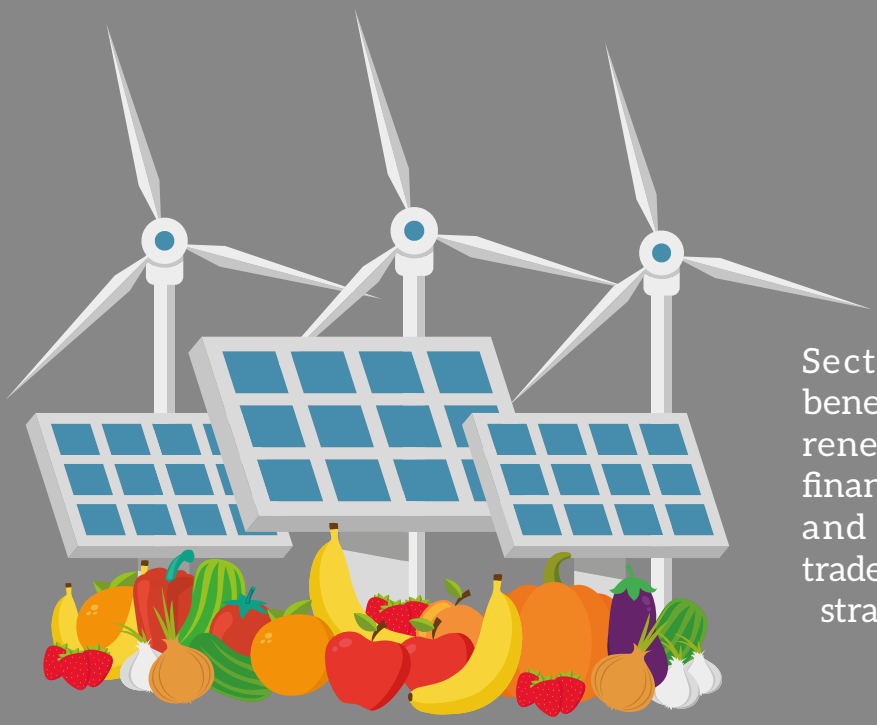
More than 60% of those working in commodity trade finance reported that they feel the CPRI industry is currently in a 'positive' state. CPRI in export finance (50%) and project finance (51%) were both reported as being 'uncertain' industries.

A substantial 92%, 91%, and 87% of respondents in commodity trade finance, export finance, and project finance, respectively, reported that there will not be an exodus of brokers and insurers from the market.

Ninety-one percent, 85% and 73% of banks and corporates in commodity trade finance, export finance and the project finance industry use a broker to access insurers.

Of the recipients of CPRI, 90%, 77%, and 60% of respondents in commodity trade finance, export finance, and project finance, reported that their CPRI products performed well during the Covid-19 pandemic.

CPRI pricing is expected to increase, and risk appetite and capacity set to decrease, across all three sectors over the coming year. However, the qualitative data suggests a more nuanced picture that highlights the interconnected nature of insurance across the three sectors.



Sectors that are considered to be beneficial to the environment, such as renewable energy projects in export finance (63%) and project finance (62%), and agri/softs (43%) in commodity trade finance were reported as the most straightforward to access CPRI cover.

Introduction

A testing time for trade finance[1]

The Covid-19 pandemic taught a deeply damaging lesson to every industry sector plugged into the global economy matrix: nothing is immune.

For export finance, TXF Data showed that across 2020, nearly $17 billion worth of Covid-19 relief support was given financed across the banks and ECAs, mostly in the form of liquidity loans ($15.1 billion) and debt holidays ($1.7 billion); a consequence of many of their clients struggling to make loan repayments because of a global lockdown, travel restrictions, and major supply chain disruptions. Market sentiment too, especially across the exporters and buyers also reflected one of uncertainty, mostly because there continues to be a lack of clarity on when the industry will return to some level of normality (TXF Research, 2021).

Commodity trade finance suffered a similar fate, with TXF Research's *Global Commodity Trade Finance Industry Report 2020* showing that for commodity trade finance banks, 85% of the sample reported a predicted reduction in the availability of credit, with 68%, 56%, and 54% citing an increase in the cost of bank debt across agri/softs, energy/petrochemicals and metals and mining, respectively.

However, commodity trade finance had an altogether unique set of challenges to face across 2020, most of which have continued still into 2021. The much reported wave of fraud cases, primarily out of Singapore and the Middle East, rocked the industry, with Hin Leong, Agritrade International, ZenRock Commodities and Phoenix Commodities at the centre.

Problems have continued into 2021, with Mercuria the victim of fraud when $36 million worth of copper blister shipped from Turkey to China turned out to painted stone slabs, and Vitol, the world's biggest independent oil trader, agreeing to pay $164 million to settle allegations that it conspired to bribe officials to secure Brazilian, Mexican and Ecuadorian oil trades (Bell, 2021). And this is all before the *"Greensill debacle"* (Oganezov, 2021).

Project finance has weathered the Covid-19 storm relatively well, but Proximo Playbook did show it had some effect, with 2020 recording a total of $237 billion worth of volume across 749 deals. This is $32 billion short of the $269 billion worth of volume across 659 deals that closed in 2019.

To compound matters for all these sectors, rising geopolitical tensions, protectionist politics, climate change, trade wars, the growing threat of cyber-terrorism, fluctuating oil prices, and the looming threat of a global recession, add a further layer of complexity for trade finance.

The need to highlight these difficulties across the trade finance industry is because they have brought into sharp focus, the role of credit and political risk insurance (CPRI).

[1] For the purpose of this report, the term 'trade finance' is the umbrella term used to refer to export finance, project finance, and commodity trade finance, as opposed to specific trade finance practices and financing solutions.

Credit and political risk insurance in trade finance

CPRI is insurance provided mostly by private companies to cover credit risk and political risk in trade finance.

The International Monetary Fund (IMF) defines credit risk as:

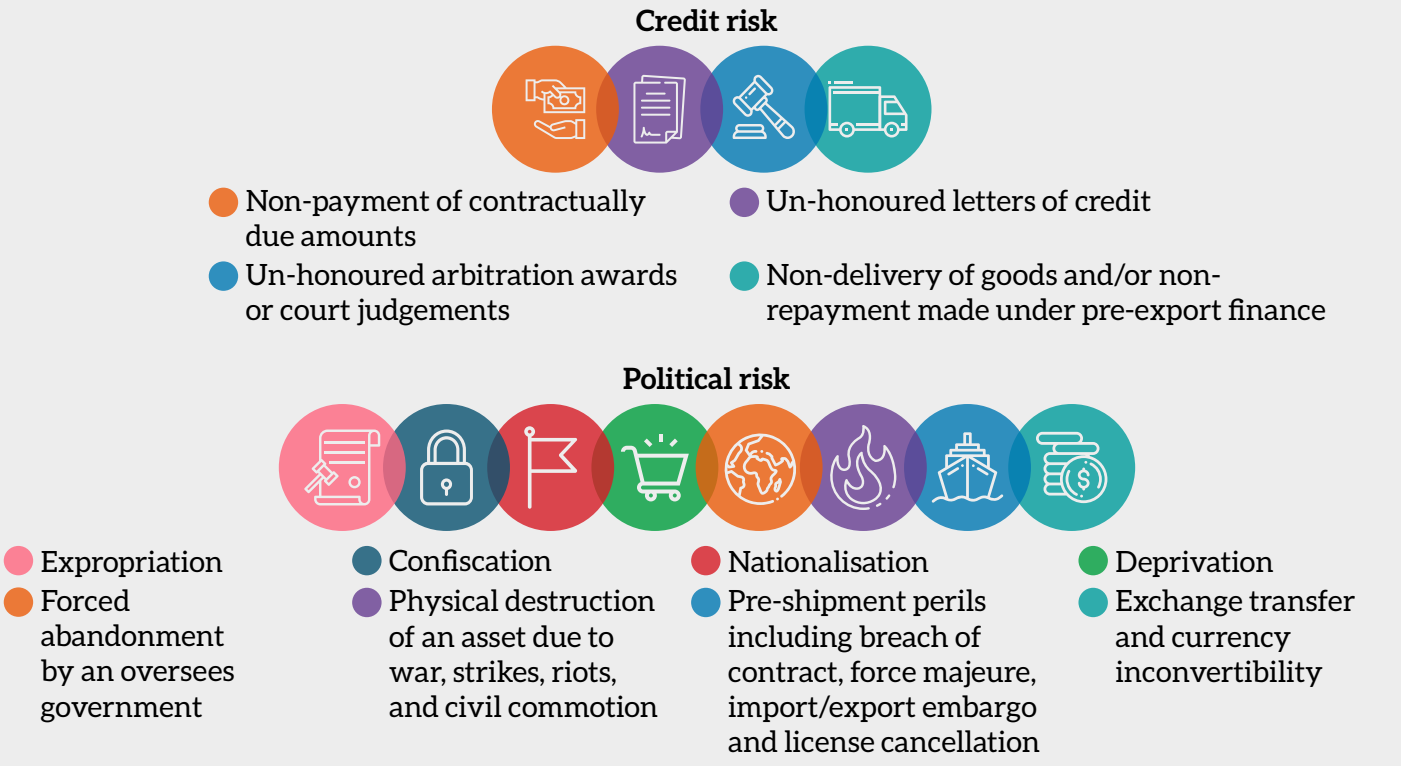
"The risk that one party to a financial contract will fail to discharge an obligation and thus cause the other party to incur a financial loss." **(IMF, 2004)**

The IMF defines political risk as:

"The risk of non-payment on an export contract or project due to action taken by the importer's host government. Such action may include intervention to prevent transfer of payments, cancellation of a license, or events such as war, civil strife, revolution, and other disturbances that prevent the exporter from performing under the supply contract or the buyer from making payment. Sometimes physical disasters such as cyclones, floods, and earthquakes come under this heading." **(IMF, 2003)**

Consequently, insurers provide cover for their clients against political factors that may prevent loans being repaid or payments for services and/or goods being made (see caption 1).

Caption 1.



Private insurers operate across export finance, project finance and commodity trade finance, but export and project finance have the added role of export credit agencies (ECAs), quasi-governmental organisations that tend to provide insurance or payment guarantees for longer tenors. Many ECAs also include private insurer divisions that provide insurance cover on a more trade finance basis, typically for shorter tenors (up to two years).

Questions remain…

To date, there is no focused market sentiment report that delves into CPRI across trade finance, with many questions still unanswered.

How have CPRI products performed for the banks and corporates who took out the policies? How, if at all, has Covid-19 changed the views and attitudes towards private insurance? How, and through what means, is CPRI accessed? How difficult has it been to access CPRI across the different sectors? And what implications has this had for lenders and borrowers? Is there set to be an exodus of insurers from the trade finance industry? And, if so, what implication will this have for the banks and corporates?

This report

Aims and objectives

The aim of this report is to present the latest market trends on CPRI across the commodity trade finance, export finance, and project finance sectors. To meet this aim, the following objectives were undertaken:

- A quantitative survey of 91 respondents across the three sectors
- Qualitative interviews with 15 brokers consenting respondents to explore in greater detail why the quantitative trends might have occurred.
- The inclusion of TXF Data and Proximo Playbook data to add further context on closed deal market information.

Methodology

The data in this report were collected using a mixed methods design that included a quantitative component, an online survey, and a qualitative component, follow-up phone and email interviews. Consequently, the data presented in the subsequent sections is an in-depth and detailed exploration of the latest trends in CPRI across commodity trade finance, export finance, and project finance.

The survey

An online survey (SurveyMonkey) was used to collect the quantitative data across the commodity trade finance, export finance and project finance sectors. Specific questions were developed for each industry type with respondents only seeing questions that were relevant to their experiences.

Responses were collected between January and April 2021. To ensure the aims of this report were met, the survey questions were tailored specifically for the different respondent types to respond to. No duplicate data from the same institution were included. If more than one respondent answered from the same institution, the scores were aggregated and then averaged. This approach ensured that every institution was weighted equally.

There are figures throughout the report where the percentages do not total 100%. The reason for this is because they were a 'tick all that apply' style questions. Where applicable, a footnote has been included to aid understanding and interpretation.

A note on sample size

A total of 91 respondents completed the survey. It is important to note that data presented in this reported is from a sample that only represents a very small percentage of the respective industries. Moreover, the cross-sectional[2] nature of the data means that it is only representative of the industry at the time the data was collected.

However, these caveats are common across many pieces of research, and while they must be acknowledged, they do not detract from the conclusions drawn from the data. Moreover, because inferential statistical analysis is not being conducted on the data, the sample of 91 respondents was large enough to conduct methodologically robust data analysis and, most importantly, for reliable trends and conclusions to be drawn.

Consequently, this report is not making any assumptions or providing definitive conclusions about the global state of CPRI across the different sectors. Instead, the data presented is giving an insight into prevailing sentiments across parts of the CPRI industry – research which to date, does not exist in the CPRI industry.

The interviews

To explain the quantitative trends, semi-structured interviews were conducted via phone and email with 15 consenting individuals. Participants were identified through a final question on the survey that asked if they wanted to be involved in a follow-up interview.

The topic guide for each respondent was based on their survey responses, ensuring that the interview remained focused. The interviews were conducted between January and April 2021. Telephone interviews were audio recorded and email interviews were kept on an encrypted hard drive. To protect the identity of the respondents, all qualitative data has been anonymised throughout this report.

Interpreting the qualitative data

The qualitative quotes used throughout the report are designed to provide additional context and insight to the quantitative trends. The quotes have been analysed against a rigorous framework that promotes transparency and detailed comparison across the interviewees.

This ensured that the quotes are not a collection of anecdotes or isolated views, but instead, an accurate representation across the interviewees. Where there are differing views, these are presented independently within the report.

However, it is important to also state that while the quotes are reflective of the overriding sentiment across all of the interviews, they are not intended to be the defining view of the industry on a specific subject.

TXF Data and Proximo Playbook data

The latest closed deal information from TXF Data is included in this report. TXF Data captures approximately 75% of all closed deal information in the export finance industry. These data will add further context and understanding to this report's findings.

Proximo playbook is a bespoke online data platform that presents closed deal market information on the project finance industry. The platform captures approximately 70% of all project finance deals globally. Closed deal information will be repeatedly referenced throughout this report to provide additional context and insights.

[2] 'Cross sectional' data refers to data collected at a single point in time. Data collected over multiple time periods is known as *longitudinal*.

Findings

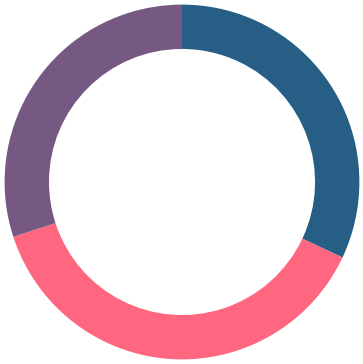
1. Demographics of the respondents
2. Market sentiment
    i. A note in the nuance of project finance
3. Opportunities and challenges on the horizon for CPRI
    i. CPRI and the ECAs: Absorbing residual risk and upping reinsurance
4. The CPRI industry is set to remain steadfast
5. An overall happy client base… mostly
6. Increasing CPRI restrictions at an increased cost
7. The continuing cost of Covid-19 on CPRI
8. An immediate focus on country risk

Demographics of the respondents

Across the respondents, 38% reported operating in export finance, 32% in commodity trade finance[3] and 30% in project finance (figure 1). At least 70% of the respondents across all three industries reported operating at a senior level or above (figure 2), with Europe the most reported region for company headquarters across commodity trade finance (58%), export finance (59%) and project finance (62%) (figure 3).

Most companies across the industries reported operating on an international scale (operating across all continents) (figure 4), with the US dollar and the euro the two dominant currencies used across all three industries (figure 5).

Figure 1. Sector within which respondents operate

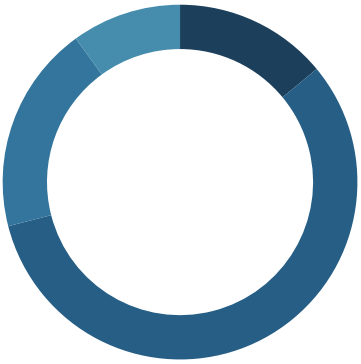


32% **Commodity trade finance**

38% **Export finance**

30% **Project finance**

Figure 2. Seniority of role



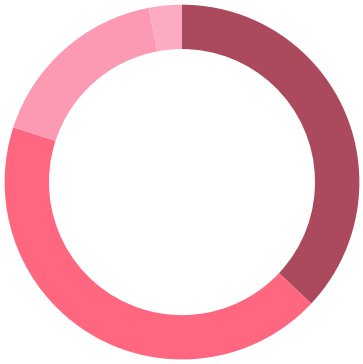
Commodity trade finance

14% Global Head/Director

57% Senior level

19% Mid level

10% Junior level



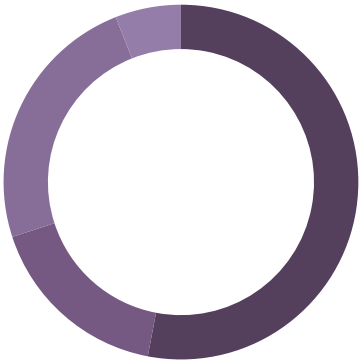
Export finance

37% Global Head/Director

43% Senior level

17% Mid level

3% Junior level



Project finance

53% Global Head/Director

17% Senior level

24% Mid level

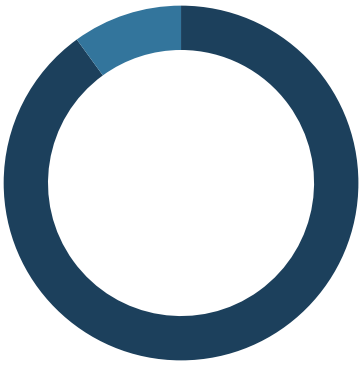
6% Junior level

[3] In the context of this research, commodity trade finance refers more broadly to the supply chain financing of agri/softs,energy/petrochemicals, and/or metals and mining.

Figure 3. Location of company headquarters by Sector

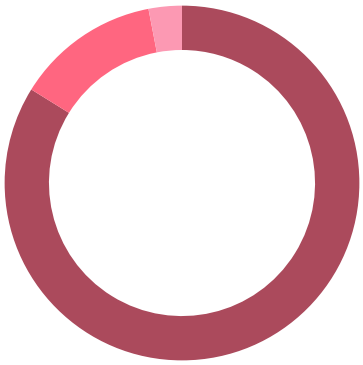
	Commodity trade finance	Export finance	Project finance
Europe	58%	59%	62%
Asia Pacific	11%	24%	10%
North America	32%	17%	28%

Figure 4. Geographical footprint of the organisation[4]



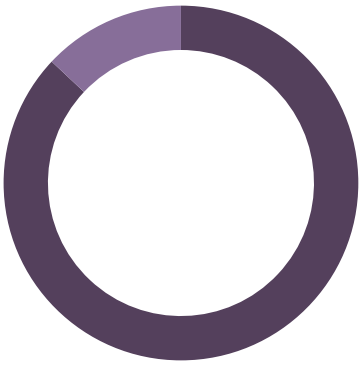
Commodity trade finance

90% International
10% Regional
0% Local



Export finance

83% International
13% Regional
3% Local



Project finance

87% International
13% Regional
0% Local

Figure 5. Most used currencies[5]

	Commodity trade finance	Export finance	Project finance
GBP	43%	47%	34%
Euro	95%	93%	93%
Japanese Yen	19%	3%	7%
Renminbi	5%	3%	13%
Swiss Franc	10%	10%	8%
US Dollar	95%	97%	98%
Other	14%	10%	13%

[4] International was defined as any organisation that operated across all continents. Regional was defined as any organisation that operated across the continent within which they were located. Local was defined as operating in their own country or immediately surrounding countries.
[5] Respondents could choose multiple responses.

Market sentiment

When asked about the state of their respective industries, those operating in commodity trade finance and project finance held a more positive view of the CPRI industry compared to those who operated in export finance (figure 6).

While the recipients of CPRI were generally more pessimistic about the current state of their respective industries, driven in large part by having to manage the recovery from the pandemic carefully, the CPRI providers were in a buoyant about the current state of the CPRI industry.

For commodity trade finance, one broker suggested that the industry was in a relatively positive state because of the technology in place:

"I think the industry has coped very well. I think the first thought for many was the Great Recession. We did not see the influx of cancelled limits (this is less relevant for banks) as insurers were supporting their clients and have better systems in place (thanks to many of the FinTech/ Blockchain technologies) to monitor credit red flags.

While the CPRI industry tightened up on certain industries (i.e. retail, which was already tight, hospitality/aviation, and oil/gas) it was accommodating for industries they saw as vital such as the tech space." **(Broker; commodity trade finance)**

A similar sentiment was felt across the export and project finance industries:

"In our view the CPRI industry coped well in general. There have been a number of credit claims in the market, but not as many as people would have expected at the beginning of the crisis. Most of the major market losses so far were related to high risk countries and obligors that were having difficulties prior to the pandemic. The pandemic just exacerbated the challenges and accelerated the losses. As far as we are aware of, there haven't been many claims in the CPRI market that were caused purely and directly by Covid-19." **(Insurer; export finance)**

However, the export finance insurer went on to state that for those without CPRI cover, 2020 will have long lasting effects:

"Companies without [insurance] cover will likely feel a deep sense of regret and a worry that those uninsured exposures will now more likely become defaults due to the economic shock caused by the pandemic." **(Insurer; export finance)**

This, the exporter explained, is the likely source of why the export and project finance industries reported uncertainty as the overriding sentiment.

Figure 6. Perception of the current state of CPRI across each industry[6]

	Commodity trade finance	Export finance	Project finance
Healthy	43%	17%	31%
Bruised	14%	10%	22%
Positive	**62%**	37%	**69%**
Uncertain	38%	**50%**	51%
Unclear	14%	10%	22%
Dynamic	33%	40%	31%
Reactive	38%	23%	30%
Proactive	19%	17%	19%
Slow	5%	20%	13%

[6] Respondents could choose multiple responses.

A note on the nuance of project finance

It is important to state that all of the project finance interviewees referred to how resilient the industry has been to the effects of the last 18 months, one possible reason behind why 69% of the project finance respondents reported the industry to be in a 'positive' position (figure 6).

Closed deal data supports this finding. For instance, Proximo Playbook data shows that compared to 2019, which recorded $269 billion worth of volume across 659 deals within project finance, 2020 closed at a $237 billion worth of volume across 749 deals, representing a 12% contraction.

In comparison, commodity trade finance saw a 40% contraction in deal volume between 2019 and 2020 ($200 billion to $120 billion)[7]. A recent roundtable conducted by Proximo also found that the project finance industry has seen relatively few insurance claims, waiver requests, or repayment holidays over the past 18 months, a sign that the industry rude health going into 2021 (Proximo, 2020).

The qualitative data suggests that because project finance operates based on much longer financing structures than its commodity trade finance and export finance counterparts, it has been well insulated from the comparably short, albeit very sharp, consequences of Covid-19, as one developer noted:

"The [project finance] industry has weathered it [Covid-19] well… we are involved in some really long projects, well over 10-year financing packages… we have been having conversations with our lender and we are about to close on a refinancing that will spread the loss in revenue over the life of the project… we don't anticipate any problem in fully repaying our loan within the terms agreed" **(Developer; project finance)**

In addition to having more flexibility and time to refinance, developers also have access to other forms of cover that replace CPRI. One such example is a 'debt service reserve account (DSRA)'. A DSRA is a reserve account specifically set up to make debt payments in the event of disruption to cashflows to the extent that debt cannot be serviced. Consequently, if the threat of non-payment looms (credit risk), the developer can access financial support from the DSRA.

While there are circumstances where project finance banks may access CPRI, namely to optimise use of banks regulatory capital, to increase a bank's ability to sole arrange, and to avoid introducing borrowers to potential bank competitors in syndication, all of which enable a bank to take on more risk than they would otherwise be able to, contingency funds such as DSRAs are an additional feature that project financiers also have at their disposal.

CPRI may have a place in covering political risks associated with project finance, but with interest rates so low, DFIs and MFIs are more likely the preferred option, as their AAA-rated status enables them to price their cover much lower than the CPRI market.

[7] Export finance saw a small increase in activity between 2019 and 2020 but this was due to a raft of Covid-19 support schemes, none of which were defined as 'true' export finance deals.

Opportunity and challenges on the horizon for CPRI

Figure 7 suggests that for all three sectors, the CPRI industry is one that presents 'opportunity' and a 'challenge'.

For all respondents across the three industries, the recent pandemic has brought the importance of CPRI into focus, with the brokers and insurers particularly excited about the potential for new clients:

"There is a great opportunity to get well-structured and well-priced risks on well respected names, plus the possibility of landing new clients that historically have not come to the CPRI market that often." **(Broker; commodity trade finance)**

However, another broker offered a word of caution: while the CPRI market is open to new business, first time organisations may still find it difficult to obtain reasonably priced insurance:

"Insurance is a relationship driven product. It's not a commodity in the sense that there's a going price where insurance can always be purchased. Those organisations that have built up their reputations over the years, have the ability to continue to use insurance from their underwriter partners, especially during challenging credit times.

We saw several underwriters close the door to new clients during the pandemic. It was a tough market to be a first time buyer and organizations that were unable to obtain coverage struggled as buyers were requesting longer payment terms following liquidity issues." **(Insurer; commodity trade finance)**

For potential purchasers of CPRI in export finance, the main challenge appeared to be identifying affordable solutions:

"Not having insurance in place seems to have added to issues in getting affordable financing for transactions." **(Exporter; export finance)**

Affordability of specific products and sectors was a commonly reported problem across commodity trade finance and export finance sectors, particularly if deals and projects were non-sustainable or in certain parts of the world, in particular Asia Pacific.

However, for CPRI providers, one of the main challenges has been the availability of up-to-date information that underwriters can use to identify risk, and how to price that risk.

The continually changing environment over the past 12 to 18 months has made it more challenging for underwriters to accurately assess the credit and political risks associated with any given project or deal.

For commodity trade finance, these challenges have been compounded by the additional scrutiny that the sector has faced because of the high profile fraud cases that came to light in 2020, as one commodity trade finance CPRI underwriter noted:

"There is a very bright and very powerful spotlight being shone on commodity trade finance, especially out of Asia Pacific. This makes decision making and risk identification even more intense. This has been the downside of the past year – insurance providers are now in the spotlight whether we like it or not… the media coverage alone is making what, and who we underwrite, even more difficult" **(Underwriter, commodity trade finance)**

Figure 7. Perception of the future of CPRI across each industry[8]

	Commodity trade finance	Export finance	Project finance
Uncertain	19%	30%	51%
Opportunity	**67%**	**60%**	**71%**
Innovation	29%	37%	23%
Challenging	**52%**	**57%**	**69%**
Positive	24%	3%	23%

CPRI and the ECAs: Absorbing residual risk and upping reinsurance

A unique part of export finance is the role of export credit agencies (ECAs). The fundamental role of an ECA is to identify and mitigate risk. To do this, ECAs provide export credit insurance and loan guarantees to protect a seller from commercial risk - and more often than not - political risk.

Export credit insurance can be short-term, typically up to one-year. For many ECAs, they often have a CPRI-dedicated facility that covers short-term export finance contracts, with the flexibility to insure up to 100% of the deal.

However, for medium- and long-term export finance activity, ECA credit insurance tends to cover no more than 85% of the full value of the contract. The remaining 15% either goes uncovered, or the lender has to look to the private insurance market to absorb the residual risk.

When the export finance insurers were asked about their desire to work more closely with ECAs, there was a strong sense that better collaboration is a viable option:

"We would always like to work with them more. We are keen to help ECAs leverage their massive balance sheets and often full faith and credit support, by enabling them to reinsure to help support their environmental and minority-owned small business clients." **(Broker, export finance)**

As the quote suggests, one primary point of commonality could be in the world of reinsurance. Looking at the smaller ticket sizes, ECAs have always struggled to attract smaller companies, mostly, TXF reports, because of potential issues around pricing, a lack of knowledge, and access to this end of the market (Morton, 2021).

If ECAs were to provide greater insurance for SMEs and then reinsure that exposure with CPRI providers, it would de-risk their portfolio while also allowing them to grow the size of their balance sheet. In short, ECAs can increase collaboration with the private market via reinsurance agreements while also managing capital at the same time.

It is true that ECAs will likely dominate the largest ticket sizes, principally because they are AAA-rated and many have an unlimited capacity to provide cover. For example, Egypt's $1.5 billion ECA-backed loan financing the Assiut oil refinery, which, for the first time, includes a 100% loan guarantee from SACE and is expected to reach financial close this year, is priced at 384 basis points using the fixed commercial interest reference rate (CIRR) (Burnett, 2021).

However, the same principle for reinsurance holds true. If ECAs are able to adequately reinsure parts of their portfolio with the private market, it would free up capacity, further de-risk the project which could attract more lenders and increase the pool of expertise involved in the project.

For emerging markets, an increasingly popular corner of the market where corporates want to delve into, this collaborative approach could facilitate that move.

Furthermore, while ECAs traditionally reinsure ECA-backed debt via the private market, which accounts for the majority of reinsurance deals, ECAs can also

[8] Respondents could choose multiple responses.

access other ECAs for reinsurance. This will be key if capacity in the private insurance market becomes increasingly stretched following a surge in claims over the remainder of the year. As the industry is starting to see, reinsurance frameworks between ECAs, especially OECD ECAs and non-OECD ECAs, are on the rise.

More broadly, for ECAs and the CPRI market to work more closely, it is likely that a number of hurdles would need to be overcome, primarily because ECAs and CPRI providers have different mandates and are backed by different entities (government verses the private sector). Furthermore, ECAs are associated with notoriously long deal gestations, piles of loan documentation and overly complicated application procedures, especially compared to the speedy but more expensive private market process.

Yet, if these challenges could be worked through, it would likely provide more coverage for a larger portion of the export finance industry.

The CPRI industry is set to remain steadfast

When the respondents were asked about a potential exodus of CPRI providers from the industry, there was a strong sentiment that this would not be the case (figure 8).

The qualitative data also support this finding, with one commodity trade finance broker warning that a reduction in the number of players does not mean a reduction in capacity:

"There may be some consolidation [of brokers and insurers] but we've seen insurance capacity grow even in 2020. There's a difference between shrinking the number of players in the market and decreasing the number of capacity in the market.

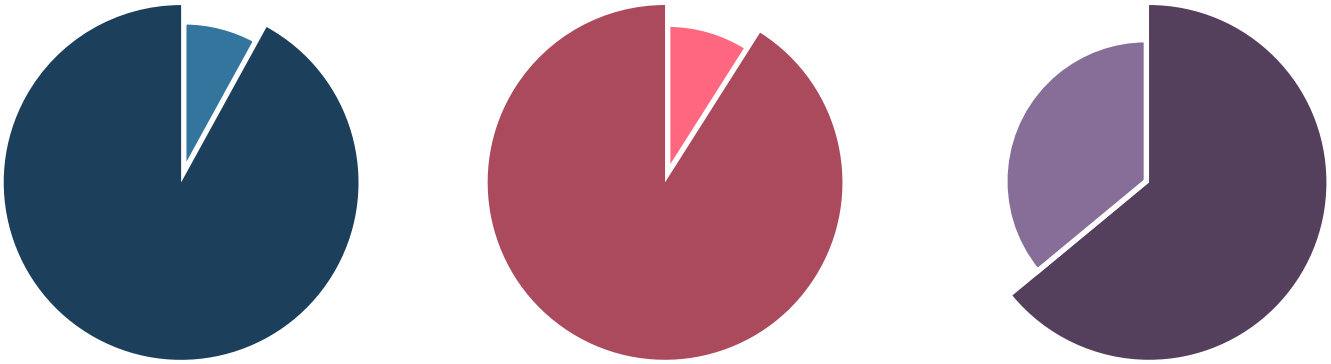
Market trends suggests capacity will continue to rise, especially for non-standard products and tenors. While we may lose an insurer or two, there are rumours of more insurance companies looking to start up teams because the historical returns have been so strong." **(Broker; commodity trade finance)**

Another pointed out that if there is an exodus of brokers and insurers from the market, it will not be any of the established and reputable firms:

"Amid the low interest rate environment during the past few years, the CPRI market has attracted a number of "fly by night" entrants seeking a higher near-term return on their capital. These players lack the long-term commitment to the business and tend to be more sensitive to market volatility.

They would quickly withdraw from the market as soon as a few losses hit or simply when the perceived risk of the business increases. It's worth noting though that ***none*** *of the long established CPRI insurers have exited the market in recent years."* **(Insurer; export finance)**

Figure 8. Views on whether there will be an exodus of insurers (and therefore capacity) from the different markets



Commodity trade finance	Export finance	Project finance
8% Yes	9% Yes	13% Yes
92% No	91% No	87% No

An overall happy client base… mostly

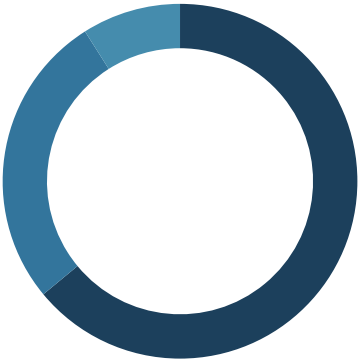
The quantitative data in this section is based on data collected from CPRI recipients, namely, the banks and the corporates.

Banks and corporates across the export finance, commodity trade finance and project finance sectors reported a preference for using a broker for of their insurance needs (figure 9).

Across all of bank and corporate interviews, there was a common theme that suggested a broker simplified a difficult and timely process:

"We have big and complex projects with longer project tenors. Very often we need more than one insurer to cover the risk and the use of a broker is beneficial to get the respective volumes covered at a reasonable pricing and it saves time and resources on our side." **(Exporter; export finance)**

Figure 9. How banks and corporates access CPRI

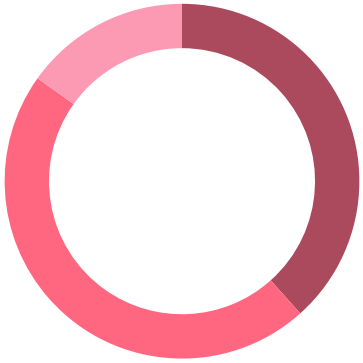


Commodity trade finance

64% We use a broker for all of our insurance needs

27% We use a broker for some of our insurance needs

9% We do not use a broker. We access insurers directly

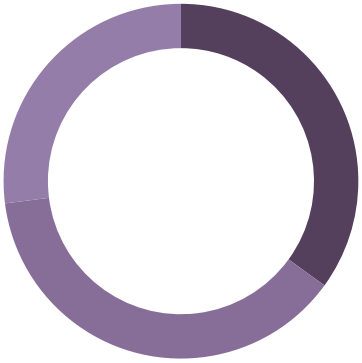


Export finance

38% We use a broker for all of our insurance needs

46% We use a broker for some of our insurance needs

15% We do not use a broker. We access insurers directly



Project finance

35% We use a broker for all of our insurance needs

38% We use a broker for some of our insurance needs

27% We do not use a broker. We access insurers directly

Across the industry sectors, banks and corporates were somewhat satisfied with the customer support they have received from their CPRI providers over the past year (figure 10).

When the CPRI providers were posed with these data, several of the CPRI provider interviewees noted that the normally high quality of customer service has been impacted by the substantial number of queries and claims they have had to deal with:

"The number of calls and requests we were receiving… [it] is nothing like I have seen before… if a claim is made, it backs everything up." **(Insurer; project finance)**

Looking more closely at how well the insurance products have performed[9], 90%, 77%, and 64% of the CPRI recipients were satisfied with how their insurance policies performed throughout 2020 in commodity trade finance, export finance, and project finance, respectively (figure 11).

Satisfaction with how the insurance products have performed, coupled with the turbulent events of 2020, were the driving reason behind why banks and corporates across all three sectors plan to do the same amount of insurance-related activity or more in the future (figure 12).

Almost all of the interviewees reinforced how vital CPRI is to their operations, with one European exporter stating, *"Covid-19 has confirmed why we consider insurance fundamental to how we operate."*

The only respondent that commented on why they anticipate doing less insurance-related activity in the future, was because of rising costs of insurance but with fewer products available.

[9] Defined as having paid out, or in the process of paying out, compensation in accordance with the terms and conditions of the insurance contract.

Figure 10. Banks' and corporates satisfaction with the support they have received from the insurance industry over the past year

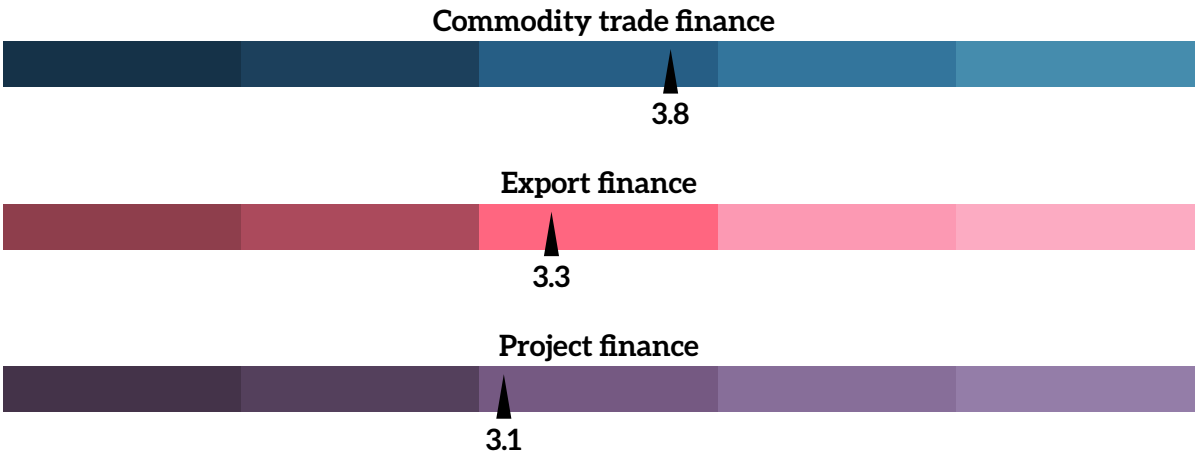
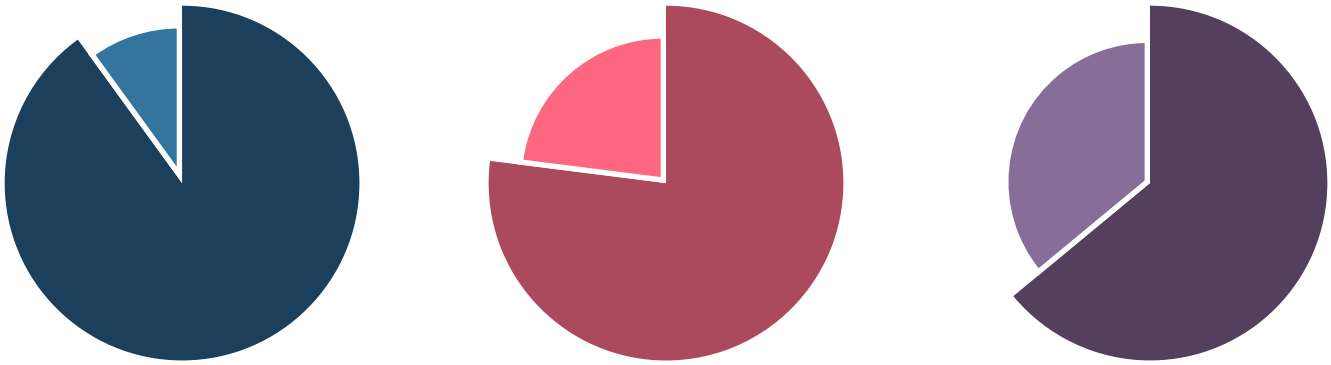
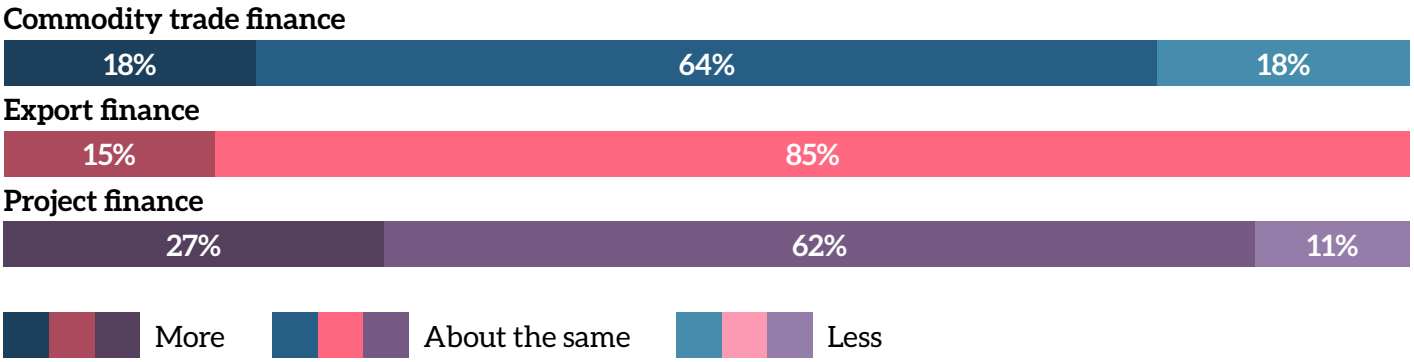


Figure 11. Banks' and corporates' satisfaction with how the insurance products have performed throughout 2020



Commodity trade finance	Export finance	Project finance
90% Yes	77% Yes	64% Yes
10% No	23% No	36% No

Figure 12. Banks' and corporates' perception on CPRI usage in the future



Increasing CPRI restrictions at an increased cost

Exploring the impact of Covid-19 on the price of CPRI products, risk insurance and capacity, there is a clear story: Cost is increasing but risk appetite and capacity is decreasing across export finance, commodity trade finance and project finance (figure 13). However, the picture is more nuanced.

First, insurance costs are generally a proportion of the underlying credit margin. This means that if banks begin charging more for the risk, so too will the insurers, as one broker noted:

"Insurers do not operate in a vacuum. They see the increased margins being charge by banks and will reflect this in their own pricing and appetite." **(Broker; commodity trade finance)**

Second, CPRI price increase could reflect a change in circumstance:

"We are seeing a 5-10% increase in renewal pricing however we've been pushing back and, in some cases, restructuring the risk in order to keep pricing the same. This could be a change in the pool of buyers or increasing the insured's risk retention. It's important to note that pricing has been soft for around 10 years. It had to harden at some point. 'Hardening' does not mean that rates are at their historical highs but simply may be where they were five years ago." **(Broker; commodity trade finance)**

Moreover, just as in the broker's quote above, another export finance insurer noted that steps are taken to keep price down:

"The cost of CPRI insurance has increased only for high risk projects, most of which insurers try to steer away from in the current environment. In an effort to de-risk their portfolios, underwriters have crowded into the higher quality opportunities by offering competitive premium rates. This has put downward pressure on pricing." **(Insurer; export finance)**

However, the brokers and insurers across all three sectors were clear that in the short-term, capacity is going to vary depending on the type of risk involved, as one underwriter explains:

"Underwriters are all staying away from the challenging credit and political risks, and focusing more of their underwriting capacity on the better quality risks. There has been an increase in the supply of insurance capacity for the good risks which, as result, has led to premium rates on the ***good risks*** *being driven* ***down*** *by the* ***higher supply*** *of insurance capacity in the market."* **(Underwriter; export finance)**

This means that projects deemed lower risk, will benefit from lower insurance premiums, despite the deteriorating market conditions. Conversely, there is a lower underwriting capacity for higher risk projects, and for those that do get insurance, it will likely be at a much higher cost.

The underwriter goes on to explain:

"Good risk" is really a "low-risk project", where the quality of the credit is good (investment grade or similar) and the country political risk is low. In other words, where we are less likely to suffer a claim. A "challenging risk" is just the opposite - a project where the credit and country risk levels are high, where we are more likely to suffer a claim.

As you would expect, underwriters have less capacity, and charge higher premiums, for the "challenging risks", and have more capacity and charge lower premiums for the better-quality risks.

This differentiation becomes more evident during uncertain times like the one we are in now. We are seeing everybody trying to crowd into the "good risks" and stay away from the "challenging risks". As a result, premium on the "good risks" get driven down further by the excess supply of insurance capacity, while insurance capacity dries up and premium becomes expensive for the "challenging risks". **(Underwriter; export finance)**

Notwithstanding Covid-19, Asia Pacific and the Middle East, both regions where commodity trade finance is established, have been rocked by a wave of fraud cases recently which will no doubt increase the risk profile of each region and with it, the uncertainty of insurers.

For export finance, Africa, the Middle East, and parts of Asia-Pacific, are emerging as key jurisdictions for export finance, all of which pose a number of credit and political risks that may make it difficult for projects to identify affordable insurance solutions going forward

Figure 13. Impact of Covid-19 on price, risk appetite and capacity of CPRI providers

Commodity trade finance

	Increased	Stayed the same	Decreased
Price	**64%**	36%	0%
Risk appetite	9%	18%	**73%**
Capacity	18%	18%	**64%**

Export finance

	Increased	Stayed the same	Decreased
Price	**85%**	15%	0%
Risk appetite	0%	15%	**85%**
Capacity	0%	15%	**85%**

Project finance

	Increased	Stayed the same	Decreased
Price	**59%**	24%	17%
Risk appetite	12%	16%	**72%**
Capacity	12%	9%	**79%**

The continuing cost of Covid-19 on CPRI

The quantitative data in this section is based on bank and corporate data only.

Looking at which sectors were reported as most difficult for banks and corporates to access CPRI, it tended to be those that are traditionally non-sustainable and have the most damaging impact on climate change.

In export finance, power (73%), oil and gas (63%) and transport (67%) were sectors identified as 'very difficult' to access CPRI. In commodity trade finance, energy/petrochemicals (33%) and metals and mining (57%) were the most difficult areas and in project finance, it was power (67%), oil and gas (64%), and transport (51%) (figure 14).

The brokers and insurers interviewed were forthright in stating that any sector considered to be harmful to the environment, or to have detrimental social consequences, is priced more highly, or made more difficult to access:

"Coal has become less welcomed in the CPRI market due to corporate-wide environmental policies. And to a lesser extent, market appetite for oil & gas has also shrank, due to a combination of environmental concerns and recent market volatility." **(Insurer; export finance)**

"Many of these sectors [coal, defence, nuclear, and oil and gas] are increasingly difficult to provide CPRI for due to ESG motivations. Oil and gas had a rough year due to low oil prices and this particularly effected borrowing base facilities like reserve based lending." **(Broker; commodity trade finance)**

A note of caution is needed here. Covid-19 notwithstanding, the push towards sustainable

practices and projects across the export finance, commodity trade finance, and project finance industries is arguably the defining feature of each industry, namely because of the looming threat of climate change.

And while the sustainability agenda is vitally important within each industry, it is important to note that a substantial portion of the population in developing regions is still reliant on oil and gas and traditional power projects not just as an energy source, but as a source of revenue.

Moreover, these sectors are still a very good source of revenue for banks and insurance providers, which is why, one commodity broker noted, *"CPRI insurers still have high existing exposures to oil and gas."*

In Africa and Asia Pacific, two regions with a high proportion of developing countries, TXF Data shows that in export finance, in 2020, oil and gas and traditional power projects account for 66% and 51% of the overall deal volume in Africa ($22.6 billion), and Asia Pacific ($12.6 billion), respectively.

Similarly, for project finance in 2020, Proximo Playbook data shows that oil and gas and traditional power projects account for 71% and 60% of the overall deal volume in Africa ($27.4 billion) and Asia Pacific ($22.6 billion), respectively.

These data suggest that while renewable energy projects are vital for the future of planet, oil and gas and traditional power[10] projects are here for the foreseeable future. Consequently, these projects need adequate CPRI cover to ensure they are financed.

[10] Excluding renewable energy projects

Figure 14. Reported level of difficulty for banks and corporates accessing CPRI across different sectors

Commodity trade finance

	Very difficult	Somewhat difficult	Not difficult
Power (coal, nuclear)	-	-	-
Oil and gas	-	-	-
Renewables	-	-	-
Transport	-	-	-
Agri/softs	14%	43%	**43%**
Energy/petrochemicals	**33%**	33%	33%
Metals and mining	**57%**	14%	29%

Export finance

	Very difficult	Somewhat difficult	Not difficult
Power (coal, nuclear)	**76%**	17%	7%
Oil and gas	**63%**	20%	17%
Renewables	17%	20%	**63%**
Transport	**67%**	25%	8%
Agri/softs	-	-	-
Energy/petrochemicals	-	-	-
Metals and mining	-	-	-

Project finance

	Very difficult	Somewhat difficult	Not difficult
Power (coal, nuclear)	**67%**	21%	12%
Oil and gas	**64%**	23%	13%
Renewables	21%	17%	**62%**
Transport	**51%**	29%	20%
Agri/softs	-	-	-
Energy/petrochemicals	-	-	-
Metals and mining	-	-	-

An immediate focus on country risk

The data presented above leads us naturally to the question: What are the immediate areas of focus for CPRI across commodity trade finance, export finance, and project finance?

One global head at an international insurance company noted,

"Export finance, project finance, and trade finance have been fairly well insulated over the past year. There are ongoing concerns with some sectors, including energy, aviation, shipping (in particular the cruise ship industry), and certain parts of the commodities world, but the focus for insurers over the rest of 2021 will be heightened country risk. This is partly due to certain international financing support running out and rising debt levels.

Countries such as Ghana, Zambia, Argentina, and Turkey to name a few, are all at heightened risk of needing additional financing support going forward. For example, Turkey is experiencing prolonged currency pressures and severe pressure on foreign exchange reserves resulting in increased risk of exchange controls and currency inconvertibility. And they are not an isolated case."

Ironically, the respondent went on to mention that these country risk-related challenges also present an opportunity:

"There is a debate in the insurance industry as to whether countries truly go bankrupt. Insurers may pay out substantial claims from time to time but the recovery history on sovereign non-payment risk has been quite favourable. This makes insurers willing to take such risks and especially over a long period of time."

While it remains to be seen which countries will experience difficulties going forward, it is believed that, unlike in 2020, the insurance industry will be more preoccupied with country-specific insurance challenges rather than sector-specific.

The exception might be certain commodities such as energy trading, metals & mining and soft commodities which will require additional due diligence as cover for supply chains continue to grow in focus. Nonetheless, commodity trade finance, export finance and project finance will continue to receive strong support from the insurance market in 2021.

Concluding comments: What next for CPRI?

The aim of this report was to present a detailed insight into the CPRI industry across the export finance, commodity trade finance, and project finance industries. Using a mixed methodology that combined 91 survey responses with detailed insights from 15 qualitative interviews, this report concludes:

The CPRI industries across all three sectors are in a healthy position. Given the countercyclical nature of insurance, it is perhaps unsurprising that the insurance sector is in rude health after a global pandemic. The short term nature of commodity trade finance has caused the industry to experience more volatility than its export finance and project finance counterparts, which is why the brokers and insurers in this sector were relatively positive.

However, respondents in export finance and project finance, both of which operate on much longer timescales, were more able to absorb the consequences of Covid-19. CPRI has a significant role to play in export finance, particularly if they can forge a path forward with ECAs. For project finance, however, an industry that also has ECA presence, and the ability of project finance developers to draw on other structures that compliment or supersede CPRI (for instance, DSRAs, cashflow waterfalls, DFI and/or MFI insurance cover), CPRI appears to have a less prominent role.

The CPRI industry offers both opportunity and a challenge going forward. The pandemic has reminded the world about the fundamental importance of insurance. In commodity trade finance, this is even more true given the wave of fraud cases that came to light in 2020, and the losses experienced by lenders that had taken large, unsecured, and uninsured positions in the likes of Hin Leong, Agritrade International, Phoenix Commodities, and Zenrock Commodities.

For the CPRI providers, there is likely to be a substantial spike in insurance and reinsurance enquiries, particularly in commodity trade finance and export finance. Yet, the providers must manage how the risk is identified and crucially, how it is priced. It was reported that those seeking CPRI cover are facing an uphill battle in finding affordable solutions so providers need to ensure they do not price themselves out of identifying new clients.

It is expected that the price of CPRI products across all three industries will increase, despite a reduction in risk appetite and capacity. It is true that price looks set to increase but the qualitative data suggests that brokers and insurers are taking steps to try and keep the price reduction low. Moreover, it is important to state that insurers do not operate in isolation. Insurance costs are generally a proportion of the underlying credit margin. This means that if banks begin charging more for the risk, so too will the insurers. Consequently, brokers and insurers are fluid organisations, reacting to other parts of the commodity trade finance, export finance, and project finance as they change. As the cost of bank debt has increased over the past year, insurers have increased their price to accurately reflect changes in their respective markets.

The sectors most likely to face the most difficulty in accessing CPRI are those that are considered 'non-green'. There was a clear pattern across all three industries: Oil and gas, traditional power projects, energy/petrochemicals, and metals and mining, were all reported by banks and corporates as sectors that are 'very difficult' to identify affordable CPRI cover. The brokers and insurers were open in stating that this is because there is a concerted effort to move towards sustainable deals, and any project that may be harmful to the environment will likely be priced high, with fewer CPRI products available.

It remains to be seen if brokers and insurers move away from these unfashionable sectors, especially if they already have high exposure to them, but if they do, it could plunge a substantial portion of the global population who are reliant on oil and gas and traditional power projects, into energy poverty.

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TXF Research makes up one third of TXF Intelligence along with TXF Data and TXF Essentials. TXF Research supplies the most detailed market insights into the export, commodity, and trade finance industries. Using an in-depth and robust methodology that combines quantitative trends with thought provoking qualitative insights, TXF Research provides unique and proprietary data and analysis based on primary sources. In addition, TXF Research offers a bespoke research service to paying clients. Working in collaboration, TXF Research collect, collate, analyse, and write reports to the focus and scope of the research, with the final product being a thought leadership piece to be used by the client as they choose.

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