To Insure or Not to Insure?

Credit insurance protects you if you don’t get paid for your foreign receivables. It’s a great way to manage risk but it comes at a price. So when companies that sell outside of Canada look at buying this insurance, the first question they ask is: Do the benefits outweigh the cost? This white paper explores that question.
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WHAT IS THE COST OF NOT INSURING YOUR RECEIVABLES?

Credit insurance can give you peace of mind because you know you’ll get paid regardless of your customer’s circumstances. For example, suppose the XYZ Company sells super widgets. They have $1 million in annual sales and a profit margin of 5%. However, one of XYZ’s customers can’t pay their outstanding account. Here’s the impact:

<table>
<thead>
<tr>
<th>Without credit insurance</th>
<th>With credit insurance</th>
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<tbody>
<tr>
<td>Profit from $1M in sales (5%)</td>
<td>$50,000</td>
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<tr>
<td>Loss because one customer doesn’t pay:</td>
<td>-$60,000</td>
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<tr>
<td>Resulting loss (-1%)</td>
<td>-$10,000</td>
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<tr>
<td>Recovery of loss as a result of insurance</td>
<td>$54,000</td>
</tr>
<tr>
<td>Resulting profit (3.15%)</td>
<td>$31,500</td>
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Cost of credit insurance (1.25%)* | -$12,500

*Policy premium rates vary according to factors such as the products or services sold, the country where the buyer is located, terms of payment, spread of buyer risk, claims history, loss history and credit practices.

GOING WITHOUT INSURANCE

Many companies choose not to use credit insurance. Instead, they accept the risk of non-payment. But given that receivables can account for up to 40 per cent of your assets, is this really the best choice? It may not protect you from major, unexpected risks. If one of your best customers goes bankrupt, for example, or a change in government policy keeps you from bringing your money back to Canada, you could be facing severe financial difficulties overnight. This is where credit insurance comes in.

The key benefit of credit insurance is that it can shield your receivables from these kinds of risks, covering up to 90 per cent of your losses if you don’t get paid.

CREDIT WHERE CREDIT IS DUE

One way to avoid buying credit insurance is to ask for payment up front. But this may make it harder to close the deal because it places all the risk on the customer. Most international customers demand flexible repayment terms before they’ll do business with you, and using credit insurance means that you can meet their demands while protecting yourself against non-payment. Using insurance also provides peace of mind, allowing you to take on new customers with confidence and a sense of security.
IT’S NOT ALWAYS YOUR CUSTOMER

It’s not always your customer you need to worry about – it’s your customer’s customer.

Another reason companies may feel they don’t need insurance is because they’ve been doing business with their customers for a long time. They’ve never had any issues, so there’s no risk – or so they like to think.

But that kind of thinking is a gamble – maybe a big one. Few companies have inside knowledge of their customers’ financial health and you may not find out, until too late, that an old and trusted customer is having serious cash flow problems. Perhaps your customer’s customers aren’t paying on time, or a supply chain has broken down, or political conditions are affecting the business environment. When things like this happen, even the most reliable customer may not be able to pay, or pay on time.

MORE CASH FROM YOUR BANK

A credit insurance policy can also help you out at the bank. If you don’t have any kind of insurance, you assume the credit risk of doing business, and that fact won’t be lost on your bank. As a result, it might be reluctant to extend financing to you for bigger operating lines, more capital expenditures or overseas expansion. But if your company has credit insurance, the bank may have more confidence that your receivables will turn into cash and that you know how to manage risk. This may make it more willing to increase your firm’s borrowing capacity.

EDC’S CREDIT INSURANCE OPTIONS

Protecting yourself, your business and your assets with insurance is worth the peace of mind it gives you. Whether your business is large or small, EDC has an insurance program that will suit your needs and keep you and your company protected.

Trade Protect, offered exclusively online, is aimed at Canadian companies that want to insure five or fewer international customers against non-payment. If you’re looking to insure $500,000 or less per customer and your customer payment terms are 180 days or fewer, this product may be the one for you. It carries a one-time premium that is calculated according to the coverage period and your customer’s credit risks.

If Trade Protect doesn’t meet your needs, the answer may be Accounts Receivable Insurance (ARI). It’s ideal if you want to insure all your receivables for all of your international customers and you need flexibility in your policy. Fees are based on the type of coverage you need, the type of goods you’re exporting, your customer’s credit risks and the country to which you’re exporting.
CHEMPRO’S FORMULA FOR SUCCESS

Established in 1997, ChemPro creates formulas for a wide range of commercial and industrial products such as adhesives, agri-chemicals, cleaning materials, softeners and lubricants. With no company sales representatives and fewer than 10 employees, the company relies mainly on word of mouth to generate annual global sales of around $1 million.

But thriving in the international marketplace can present challenges for a small business. ChemPro’s Canadian customers pay up front, but the firm discovered that it couldn’t compete effectively for foreign contracts unless it extended credit terms to its overseas customers. Unfortunately, providing credit meant that ChemPro might not get paid when its invoice came due. To solve the problem, ChemPro turned to EDC’s credit insurance.

“We needed to ensure that we could collect our revenues from our international sales. To increase our sales outside Canada and decrease the risks associated with exporting, we approached EDC for credit insurance coverage,” says Alex Moussa, Vice-President, Business Development. “This allowed us to start talking to distributors in markets like Africa. It opened up a lot of new doors.”

In 2014, when EDC launched Trade Protect, ChemPro was one of the first companies to take advantage of this new self-serve, pay-as-you-go credit insurance.

“When you’re on the move,” says Moussa, “it’s nice to have the option to choose when and where you do business. Getting coverage online with Trade Protect for our Mexican client was easy, for example. This process was very simple to complete and saved us a lot of time.”

ChemPro now exports its products and services across North and South America and into Western and Eastern Europe. Recently, the company has been tapping into new foreign markets such as Lebanon, Southeast Asia and Africa.
NEXT STEPS

If you have questions about your specific situation, or would like to learn more about our credit insurance options, call our toll-free number at 1-866-376-3480 to speak to an Account Manager. We’ll answer your inquiries within one business day, weekdays between 9 am – 5 pm EST.