



When the unthinkable happens

Why credit insurance is useful
and how we deal with sudden defaults

Trade safely with credit insurance

In a perfect world of business trade, goods are shipped, services are provided and invoices are paid. Sometimes however, invoices are not paid and the manufacturer or supplier faces a bad debt or even a loss.

In the case of insolvency or a lengthened default, having credit insurance can reduce the financial impact of non-payment by compensating the supplier for the insured amount.

In general, credit insurance:

- Protects the insured from losses on unexpected buyer defaults – insolvency or protracted defaults
- Includes continuous monitoring and assessment of the credit quality of buyers, and takes action if the quality of a buyer deteriorates so that risks can be mitigated
- Recovers overdue debts in accordance with suppliers' customer relationship goals
- Enables better trade decisions and improves sales efficiency through better buyer information
- Improves access to financing facilities, enhances credit conditions and strengthens cash flow
- Allows assessment of future / new business partners



Our proximity to the market, our relationships with customers and our access to information and market intelligence, help us detect potential insolvencies before they are filed.

Case study

Dick Smith Holdings Limited (formerly **DSE**) was, until 2016, an Australia-wide chain of retail stores selling consumer electronics goods and components. The company was founded in Sydney by Dick Smith and his wife and expanded into several close-by countries. The company closed in 2016, within several years of its acquisition by Anchorage Capital Partners.

The business started in 1968 with a total capital of only AUD 610. Initially, the business focused on installing and servicing car radios.

Dick Smith introduced self-serve shopping, a breakaway from the longstanding counter-sales setup found in component sales at the time. Also he produced an annual mail-order catalogue. In 1980, with 20 stores, the major part of the company was sold to the large general retailer Woolworths Limited.

Two years later the remainder was sold to Woolworths with a total transfer price of AUD 25 million. On 31 January 2012, after nearly 30 years of ownership, Woolworths announced that after the results of a strategic review and an AUD 300 million restructuring, it would close up to 100 Dick Smith stores and sell the business. The company was sold to Australian investment firm, Anchorage Capital Partners, in September 2012.

in AUD 'm

Revenue	791
EBITDA	150
Stock	171
Debt	2
Gearing %	1

2013

Previously a break-even company at best, belonging to the Woolworths conglomerate business.

After acquisition by Private Equity (for circa AUD 110 million), DS underwent major transformation with ambition for growth, opening 25 stores per year.



2014

No company is too big to fail

Companies that use credit insurance can protect their business, limit their trading risks and find new opportunities in an easier and better way.

Yet even secure business environments can be influenced by the growing uncertainty of external factors such as: fraud, political instability, economic fluctuations, natural disasters, unsteady commodity prices, technological developments and digital trends, and more. This makes some insolvencies increasingly difficult to foresee.

Over the last couple of years we at Atradius have seen an increase in unexpected high profile insolvencies across the world that, due to their

size, speed and circumstances, have surprised many. We define these as 'sudden defaults'.

What are sudden defaults?

Sudden defaults are improbable, unpredictable and unimaginable. They are characterised by their size, value and speed of default as well as the circumstances of the default. Often, the triggers for these sudden defaults are a combination of events. The metaphor we use to describe this is the "black swan"*:

These sudden defaults show that no company is too big to fail and that even the most experienced credit manager can be caught by an unexpected insolvency. They also show that these types of defaults

require special expertise and are reason to take 'special' measures. Fortunately we acknowledge that sudden defaults occur, and have the expertise and know how to promptly take appropriate measures.

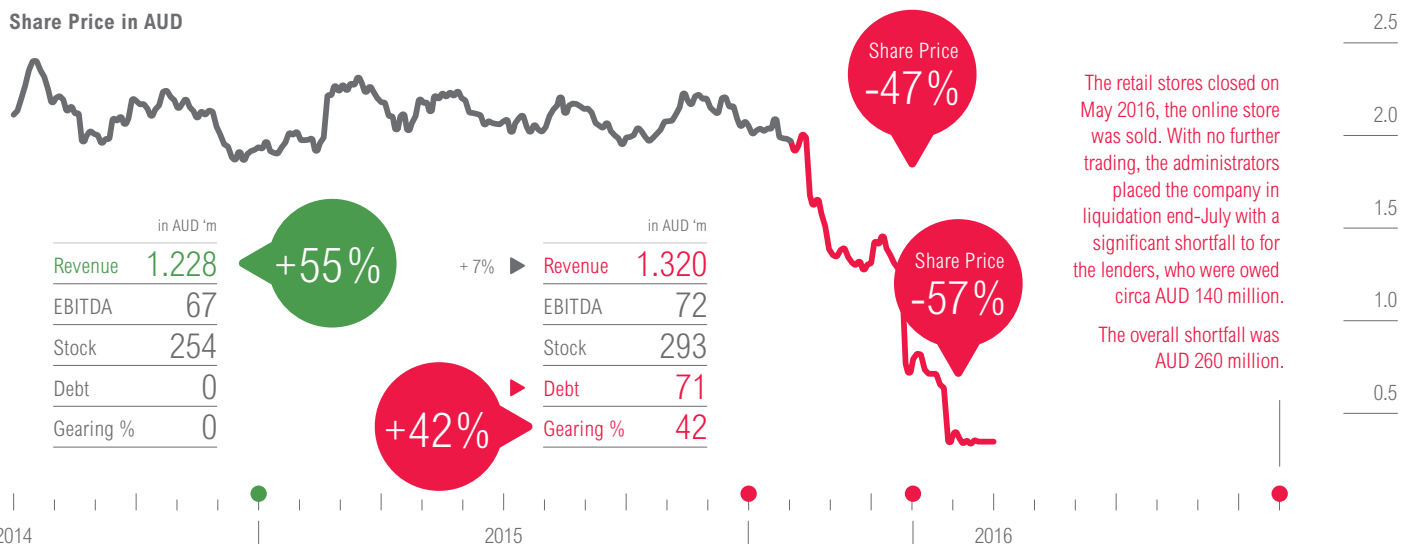
One of the distinguishing differences we offer is the service of our Special Risk Management (SRM) unit, which closely partners-up with our customers. This unit comes into action when a sudden default threatens or has occurred. It is how we respond and interact in such cases that makes the difference.

Below you will find an example case study of a typical sudden default.

The Dick Smith case was transferred to SRM on 30 November 2015. We undertook both a Real Outstanding Exposure (ROE) and a security review exercise. As we insured key suppliers significant exposures, exit had to be carefully orchestrated. We worked with our policyholders to significantly reduce the collective position by monitoring payments, stock levels and supply.

Meetings between Atradius and the CFO established there was a purchasing and subsequent inventory issue. This was not considered terminal at the time, provided all stakeholders maintained their support (DS purchasing decisions were heavily influenced by supplier rebates attempting to maximise profit).

Share Price in AUD



The retail stores closed on May 2016, the online store was sold. With no further trading, the administrators placed the company in liquidation end-July with a significant shortfall to for the lenders, who were owed circa AUD 140 million.

The overall shortfall was AUD 260 million.

October 2015, following announcement in June 2016 that profit would be AUD 5-8 million lower than predicted, the share price fell 47% over the next 3 days.

A month later, DS faced a non-cash impairment of AUD 60 million, following a review of inventory. The share price fell a further 57% to AUD 0.28.

Despite ambitious growth targets, revenue for year-ending June 2015 was only 7% up, while the company had taken on AUD 71 million of debt and gearing had increased to 42% from nil.

Following its listing on the ASX in June 2014, DS boasted a revenue growth of 55% to AUD 1.2 billion.

Our Special Risk Management (SRM) team is standing by for you

When the circumstance of an extraordinary case requires additional expertise, special attention and tailor made solutions, we are the right partner. Our SRM unit is a team of international experts in underwriting, legal affairs, claims and recoveries, that come into action to support and help you recover outstanding debts as soon as one of your customers gets in a situation that begins to deteriorate - or worse.

The SRM team, specialists in restructuring, operate on a country as well on a cross border level. We work in close collaboration with you and your customers, together with lawyers, financing and consulting parties and other stakeholders.

What's in it for you?

- We protect you, the supplier, from further non-payments
- We help restructure the debt of your customer, the buyer, in a way that - if possible - trade can continue. If not possible for trade to continue, we support you with the most optimal exit-strategy
- We save time and achieve cost efficiencies for you in the proceedings and negotiations
- You can benefit from our cultural, lingual and legal expertise in more than 50 countries
- We align our services with your business strategy and aims regarding your customers
- We support you in creating a stronger creditor position
- We help maximise your recoveries

Our international network helps consolidate the processes and resolution of insolvency proceedings so that solutions can be found on an individual case basis, with recovery amounts often exceeding the results that may be achieved without us.

Actions that Special Risk Management (SRM) take

If your customer is transferred to our SRM unit, our international experts take the following actions:

- 1** We internally execute a detailed evaluation of your customer and the trade sector as well as review its securities
- 2** We contact your customer as soon as possible, together with its suppliers and other stakeholders like banks, consultancy agencies etc., to get an impression of its financial and economic situation
- 3** We develop a plan for your customer, for you and for your peers in the specific trade sector, and share this with all involved parties
- 4** We try to reach an agreement with your customer on actions to reduce further non-payments, for example by:
 - Controlling and conducting deliveries
 - Arranging payment procedures
 - Determining securities/pledges
 - Adapting credit limits and cover arrangements
- 5** Provide credit limits without triggering negative signals to the restructuring process (e.g. impacting other suppliers in the sector)
- 6** Participate in meetings with financing and consulting parties (our international network, enables us to conduct the insolvency proceeding through one party)
- 7** In the case of an insolvency, we support by agreeing on, or implementing the right for Retention of Title
- 8** Through participation in creditor committees we represent the interests of the suppliers (you)

* *A black swan is an event, positive or negative, that is deemed improbable yet causes massive consequences.*

Black swan events explain almost everything about our world, and yet people are blind to them.

The Black Swan
The Impact of the Highly Improbable
by Nassim Nicholas Taleb (Author)

Drive your business forward with powerful, easy-to-use credit management tools. Simple, relevant, transparent

Have a look at Atradius Atrium - our unique online credit management hub. Through this single portal you can manage your daily policy activities, get an overview of your customer portfolio and analyse them. In addition, it offers you easy entry to our latest publications and events.

Furthermore, through Atradius Atrium you can directly access Atradius Insights, which is designed to help you monitor your portfolio performance in detail, identify risks and opportunities, detect trends and respond proactively to changes.

Connect with Atradius



atradius



@atradius



atradiusgroup

atradius_sudden_defaults_20171124_01



Contact us
Atradius.com

Atradius

Trade Register Madrid: M-171.144
Registration: Atradius Crédito y Caución S.A. de Seguros y Reaseguros