berneunion

BUSINESS CONFIDENCE INDEX

Q3.22

AUG 2022

Export Credit Business Confidence

Tracking perceived demand, risk appetite and claims in the export credit insurance industry, based on quarterly surveys of Berne Union Members

Heightened geopolitical risk is driving growing demand for export credit insurance, despite the dampening effects on trade of a decidedly bleak economic outlook. Insurers remain cautious in response to visibly growing levels of insolvency globally

Presented below is an analysis of the results of our seventh quarterly Berne Union Business Confidence Index survey, conducted in July/August 2022.

Throughout the first half of 2022 the global risk environment has remained acutely heightened. Lingering effects of the pandemic have only been further exacerbated by the Russia/Ukraine war (War), with disrupted supply chains, labour shortages and price inflation – especially in food and energy – piling pressure on businesses and governments alike. Interest rate increases translate into higher borrowing costs, which, along with high prices potentially dampens both short term demand and longer-term investments. Global Export Manufacturing Orders[1] have been falling every month since March 2022. During the same period, corporate bankruptcies have been steadily rising while sovereign defaults are also looking increasingly likely.

Despite this bleak outlook, or perhaps partly because of it, overall demand for export credit insurance remains strong, supported by the increased risk perception and uncertainty arising from the current geopolitical environment. Demand for short-term (ST) cover, substantially driven by commodities business, has been especially strong through the second quarter and this is expected to continue in 3Q 2022, albeit at a slightly lower level.

Demand for medium/long-term (MLT) cover has been more sporadic during 2022 so far – falling in the first quarter before picking up again in 2Q. Expectations for the third quarter are for a marginal continued increase, despite hesitancy around investment in new large projects, again, due to the overall high risk perception.

Following a relative surge through 2021, ST risk appetite has remained overall relatively flat this year. This now appears to be tightening in 3Q with a more pessimistic outlook based on compounded impact of the War on prices, supply chains and insolvencies going forward.

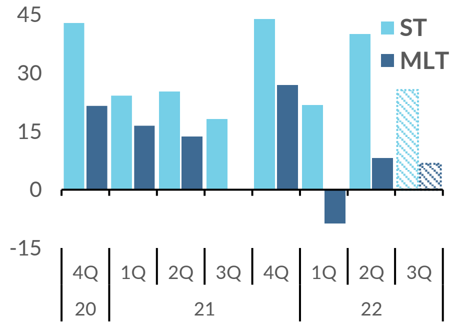
Insurers continue to exercise caution in their MLT underwriting, with overall appetite tighter this year than last, but relatively unchanged moving from 2Q into 3Q. Countries on the watch lists are those most acutely impacted by rising food prices and interest rates.

Although claims were declining around the end of 2021, expectations throughout 2022 have been solidly towards an increase for both MLT and especially ST business.

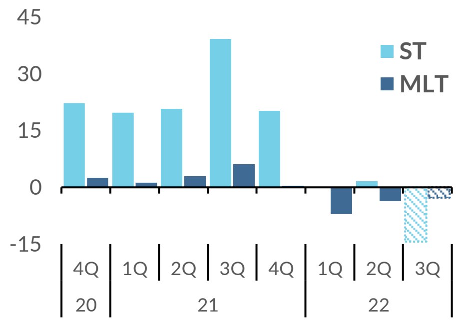
Payment delays directly caused by the War are materialising for some insurers and there is a general expectation that liquidity constraints and higher interest rates will lead to increasing insolvencies in the third quarter. For ST business the expectation is a substantial increase in claims paid, while for MLT the material impact of payment delays will take longer to emerge unless more sovereign defaults start to materialise in late 2022.

Index (0 → *No Q/Q change*)

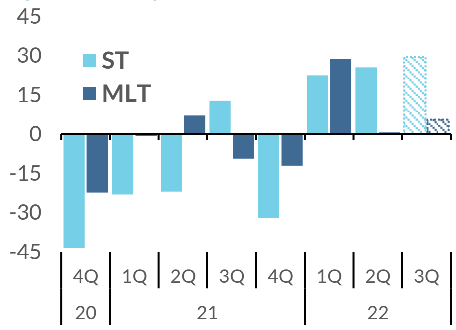
Estimated effect on *demand*



Estimated effect on *risk appetite*



Estimated effect on *emerging claims* and *expected claims paid* (dotted)



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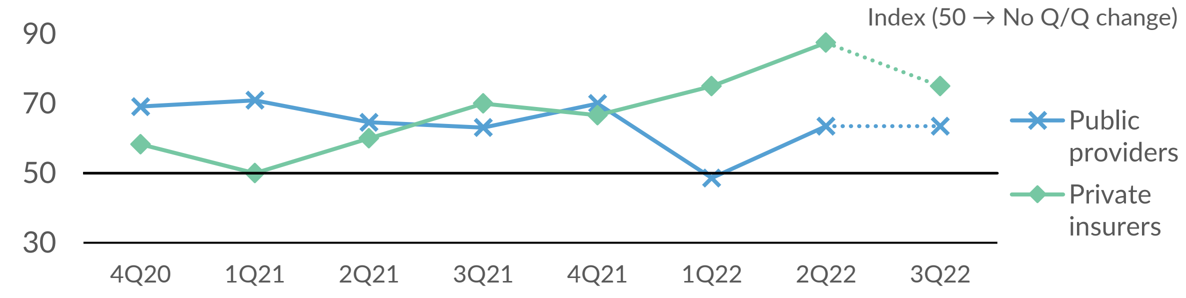
[1] J.P. Morgan Global Composite PMI

Short-term commercial and political risk

The figures below present Berne Union Members' perception of the current and future business situation for short-term commercial and/or political risk. Members were surveyed about their perception of demand, level of claims and overall risk appetite.

Figure 1: Current and expected future *level of demand*



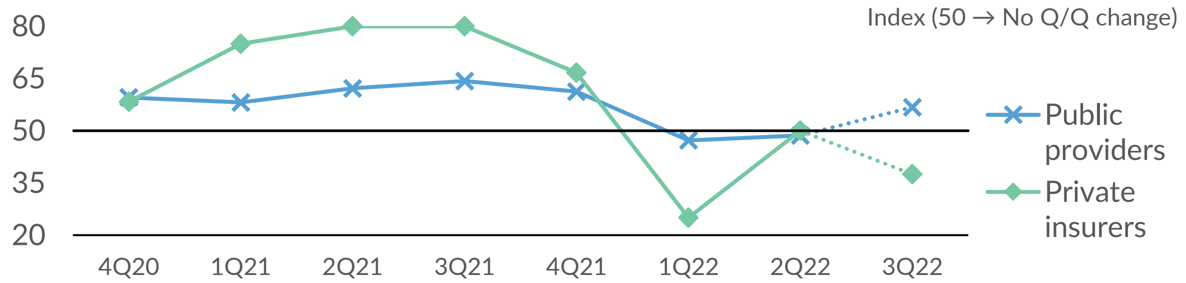
Note: A score above 50 indicates a higher/increasing level compared to the previous quarter, while a score below 50 indicates a lower/deteriorating level compared to the previous quarter.

Insurers saw rising demand for ST cover in 2Q which is expected to continue in 3Q due to rising prices and global tensions

Both public and private insurers saw rising demand in the second quarter of 2022, to an even higher degree than expected in the previous survey. Several insurers noted rising prices as one of the drivers of higher demand, but also highlighted that much of the growing demand is stemming from requests for higher limits from existing clients.

Equally, both public and private insurers are anticipating demand to increase further in 3Q with public insurers in *Middle East & Africa* being most optimistic. The general consensus is that inflationary pressures and commodities will be the driver of much of this increase in cover. However, some members noted that economic slowdown could affect this expected trend.

Figure 2: Current and expected future *risk appetite*



Note: A score above 50 indicates a higher/increasing level compared to the previous quarter, while a score below 50 indicates a lower/deteriorating level compared to the previous quarter.

Risk appetite remained tepid in 2Q 2022 while public providers are anticipating to fill market gaps in 3Q

The risk appetite of private insurers was unchanged in 2Q 2022 after seeing a broad fall in the first quarter. This is something of an improvement compared to their expectation last quarter, that risk appetite would continue to tighten. In contrast, public insurers overall reported a slightly lower risk appetite in 2Q 2022 marginally less optimistic than previous expectations. Some insurers noted that their risk appetite was mainly unchanged except countries highly impacted by the war, either directly or indirectly.

Private insurers indicated that their risk appetite might decrease in 3Q 2022, mainly due to the increasing risk environment and a potential economic slowdown – or even downturn – due to inflation, rising interest rates and geopolitical tensions. Meanwhile, public providers expect that their risk appetite will rise, partly to accommodate rising demand in the higher risk environment. A good demonstration of the market-gap filling mandate of public insurers of export credit and investment.

Figure 3: Current level of *emerging claims*

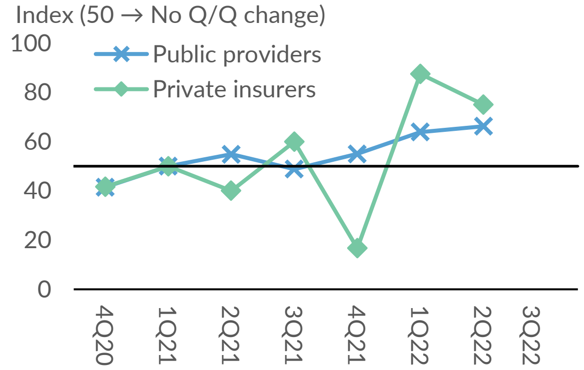
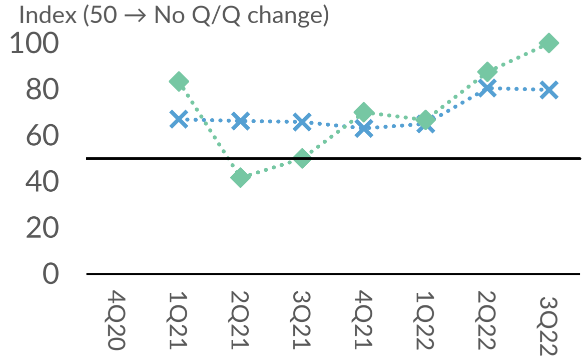


Figure 4: Expected future of *claims paid*



Note: A score above 50 indicates a higher/increasing level compared to the previous quarter, while a score below 50 indicates a lower/deteriorating level compared to the previous quarter.

Insurers are seeing both more emerging claims in 2Q 2022 as well as continuing to expect higher claims paid in 3Q

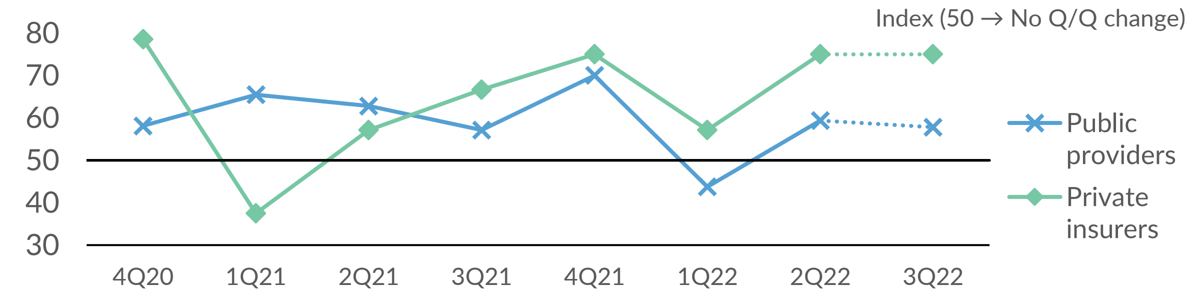
Emerging claims were higher in the second quarter for both public and private insurers. This was the case for insurers in most regions, except those based in *Asia & Pacific*. Insurers note that pre-claim situations are rising but still not at pre-pandemic levels and that many of these are – directly or indirectly – stemming from the War.

Insurers are anticipating rising claims paid in 3Q 2022 with the consensus being noticeably obvious among private insurers as all surveyed indicated claims paid related to ST risks will increase. The consensus is that companies experiencing increased pressures on profitability, rising interest rates and less liquidity could lead to an uptick in insolvencies, only exacerbated by the consequences of the War.

Medium and long-term commercial and political risk

The figures below present Berne Union Members' perception of the current and future business situation for Medium to long-term (MLT) commercial and/or political risk. Members were surveyed about their perception of demand, level of claims and overall risk appetite.

Figure 5: Current and expected future *level of demand*



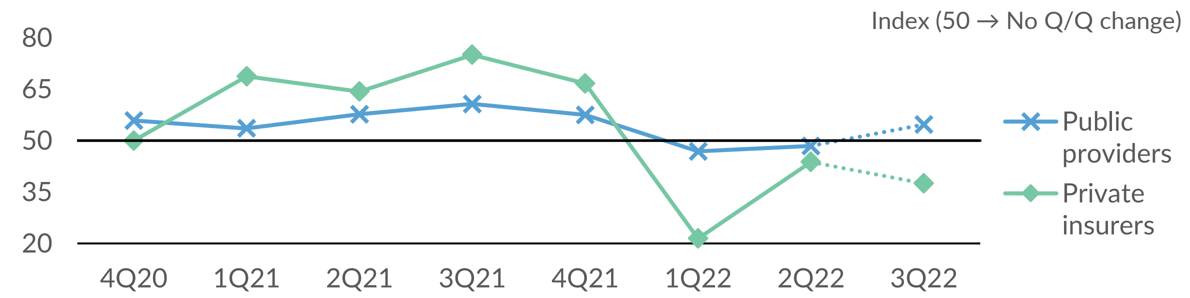
Note: A score above 50 indicates a higher/increasing level compared to the previous quarter, while a score below 50 indicates a lower/deteriorating level compared to the previous quarter.

Demand for MLT risks rose in 2Q 2022 and insurers expect similar growth in 3Q

The consequences of rising interest rates, inflation and the War are having diverging effects on demand with some insurers saying they are causing more interest in cover while others indicate a drop due to a fall in the underlying projects. European ECAs saw a return in demand following a drop in 1Q which means that unlike the first quarter of 2022, the second quarter saw both public and private insurers indicating a rise in demand for MLT risks.

Demand is expected to continue to grow in the third quarter of 2022 with only European ECAs anticipating somewhat lower demand for MLT risks. The overall reason behind the rising demand is the high level of volatility causing more demand for insurance cover in spite of a potential slowdown in the economy and some projects.

Figure 6: Current and expected future *risk appetite*



Note: A score above 50 indicates a higher/increasing level compared to the previous quarter, while a score below 50 indicates a lower/deteriorating level compared to the previous quarter.

Risk appetite continued to contract in 2Q 2022 with public providers expected to step up in 3Q

Risk appetite did not contract as much as in 1Q 2022 and less than feared during the last survey but the second quarter continued to see insurers limiting their risk appetite slightly. Insurers are highlighting some emerging economies and countries particularly impacted by the War as markets where their appetite has been reduced. Insurers are more selective when underwriting new transactions with unknown obligors.

Risk appetite for MLT risks is somewhat similar to the trends seen for ST risks, highlighting that the underlying drivers are macro driven. Private insurers were either indicating a slightly lower risk appetite or an unchanged risk appetite in 3Q but with the caveat that it may decrease if the economic situation worsen more than expected or the quality of risk decreases sharply. Public providers are remaining stable, trying to provide necessary cover, underlying their role as to fill market gap when needed.

Figure 7: Current level of *emerging claims*

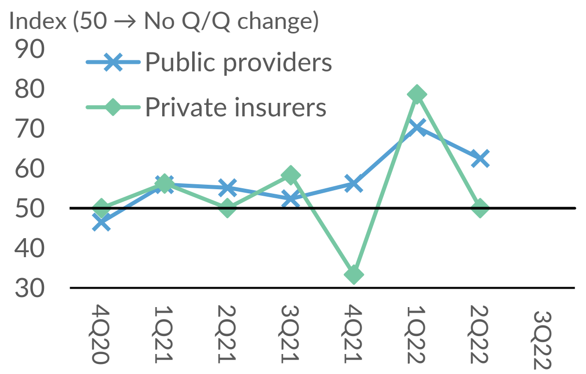
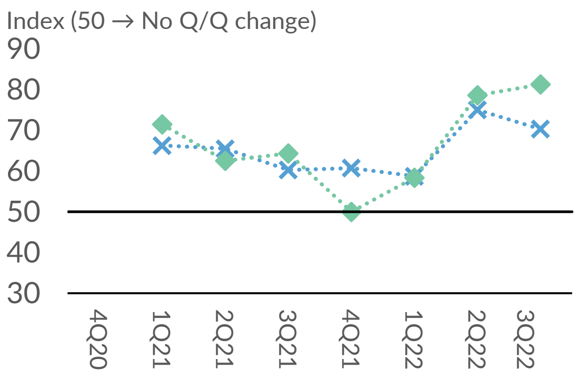


Figure 8: Expected future of *claims paid*



Note: A score above 50 indicates a higher/increasing level compared to the previous quarter, while a score below 50 indicates a lower/deteriorating level compared to the previous quarter.

Rising emerging claims was less severe in 2Q while expectations for claims paid continue to be high for 3Q 2022

Public insurers are still seeing higher emerging claims in the second quarter although to a smaller degree than in 1Q 2022. Some ECAs highlighted that the War is having an effect on pre-claims situations from both disrupted business relationships as well as second order effects, such as the energy crisis, rising costs, and additional disruptions in supply chain. Fears of further sovereign defaults or payment issues were also noted, especially since Sri Lanka's default. Meanwhile, private insurers saw an unchanged volume of emerging claims noting that they have not seen any immediate effects on pre-claim situations yet.

Both public and private insurers anticipate that claims paid will be higher in 3Q 2022. This is mainly due to higher borrowing costs along with less liquidity which can severely affect the viability of future projects as well as the financial situation of certain countries which were already in difficult space – with supply delays, rising input costs, and scarcity of labour.

Methodology

The Berne Union's *Business Confidence Index* was launched in 2021, with the objective to provide a continuous indicator of the overall perception of demand, risk appetite and claims in the export credit insurance industry.

The Index is based on quarterly snapshots of our Members' assessment of their current and imminent business situation with respect to these factors. In line with industry norms, we distinguish between short-term (ST) and medium to long-term (MLT) commercial and/or political risk.

Estimated effects figures are weighted by respondents' commitments and are therefore a closer approximation of the quantitative change experienced by the export credit and investment insurance industry. The y-axis must not be confused with quarter over quarter (Q/Q) percentage change. The index is between -50 and 50, where a score of 50 means that all members indicated an increase and -50 means that all members indicated a decrease.

Business perception figures are unweighted and meant to represent Members' sentiment of current and future business situation of the industry, rather than quantitative effects. The index should be interpreted in the following way: If all members indicated an increase, it would be 100 and if all members indicated a decrease, it would be 0. A score of 50 means an unchanged level. For example, if a score was 61 in one period and 73 in the following period, this means that both periods saw an increase, but the increase was stronger in the second period.

For more information on the report, measures and analysis, please contact Jonathan Steenberg at the Berne Union Secretariat. – jsteenberg@berneunion.org

* *Note: 'emerging claims' indicates pre-claim situations upon which the underwriter anticipates a high probability of paying claims at a later date – e.g. due to notifications of possible problems with a buyer.*

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