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## Russia Credit risk and the credit insurance market

**Entretien** Due to increasing liquidity problems of Russian companies and the higher exchange rate foreign companies are asking for higher Ruble prices and are facing thus increasing competition especially from Chinese companies. It also leads to an increasing demand for longer payment terms. **PROPOS RECUEILLIS PAR ARMAND ANGELI**

### Can you give us an overview of the economic situation in Russia?

It is not surprising to note that due to the international sanctions on trade with Russia the biggest country in the world is slipping into a recession. GDP growth in 2013 was down to 1.3% (3.4% in 2012) and is expected to end at ca.

0% for this year. Another key problem is the strong dependence on the oil and gas sector and the decrease of the oil price recently. However, a strongly devaluating Ruble helps to increase the income out of the sales of raw materials so that the government can tap into its extensive currency reserves in order to

increase investments and to offset liquidity shortages due to sanctions.

Private consumption is only slowly declining as the unemployment rate in June 2014 was only 5%. Retail sales increased during the first half of 2014 for 2.7%.

However, businesses are facing increasing difficulties to raise bank financing. Thus liquidity shortages are showing their effects on payment behavior.

All in all Russia has the possibilities to come out of the current crisis even more strengthened than before.

### How is Russia different from other Eastern European markets in terms of risk (especially credit risk)?

Transparency is surely one of the major differences. Even though a lot of information about companies can be obtained – some even on-line – due to tax evading efforts the legal structures of companies can be fairly complex: most of the companies have established dedicated group companies for different purposes like production, purchasing, asset holding etc. Due to this an evaluation of the credit worthiness is often quite difficult and time consuming if adequate credit decisions are targeted. Another aspect is the very formalistic legal system. As opposed to common prejudices one can obtain correct verdicts at the

different courts and corruption is not that prevailing anymore. However, the high bureaucracy and formalism is not to be underestimated and local experienced lawyers and an accountant are a must.

### What is the situation of your main customers located in Russia? What are their main risks on this market and their needs in terms of risk coverage?

Due to increasing liquidity problems of Russian companies and the higher exchange rate foreign companies are asking for higher Ruble prices and are facing thus increasing competition especially from Chinese companies. It also leads to an increasing demand for longer payment terms and higher credit limits. Clients facing therefore a combination of the existing challenges for adequate risk evaluation of Russian companies, an increasing demand on the credit risk side a more restrictive approach from insurer these days. Solutions? Our clients appreciate a lot our efforts as specialized broker with an own information agency supporting to obtain and keep adequate credit limits for them.

### What are the different solutions available in Russia for credit insurance and financing compared to the rest of Europe?

The three global insurers Atradius, Coface and EulerHermes are in good competition with the Russian players Ingo-ONDD (a joint venture with the Belgian Creditmundi), Soglasie and Exiar, the Russian state owned export credit agency. Together they offer in general the same types of coverage one would find in other parts of Europe.

Each of the private insurers has a lot of experience in

## Comments on the Russian credit insurance market<sup>1</sup>

► **Under the market economy model**, an increasingly effective method of attracting clients is to offer value for money and competitive payment terms. In this relation, the legal entities that provide their clients with trade credit or deferred payment are more competitive than other market players who are paid in advance or upon the actual receipt of cash from the counterparties. Today more and more suppliers in Russia apply this scheme to make settlements with reliable companies. That is why trade credit in total is twice as large as total credit issued by banks.

► **At the same time**, such an approach increases delinquency risks dramatically. In each particular case, past-due receivables may be caused by counterparty's insolvency and commercial and political risks. In order to prevent any adverse effects all these factors may have on operations, Russian businesses increasingly turn to credit insurance or trade credit insurance.

This type of insurance has been used all over the world for more than 100 years. It has proved its importance and fostered the development of various industries. This instrument allows for protection against risks associated with commercial crediting. The leading companies of this insurance sector render the

services regarding assessment of credit risks associated with of a legal entity in relation to its clients.

Crisis phenomena in the Russian economy and limited access to credit facilities thwart the development of Russian businesses. Insurance of commercial credits allows easing credit granting procedures. Besides, insurance policy allows reporting receivables in a more favorable light.

► **Growth of credit insurance market** depends on the growth rate of the Russian economy. The most attractive sectors are those where market players are transparent from the point of view of merchandise and financial turnovers. At the same time, there are cases where a market segment is not so promising for credit insurers, but some businesses have good reputation built on fair work. Generally, these are western companies or their Russian subsidiaries.

The Russian credit insurance market is led by foreign companies Euler Hermes, Atradius, Ingo-ONDD and Coface. They control about 90 per cent of the global credit insurance market.

#### 1. Tamara Kasyanova, PhD in Economics

Senior Vice President of Russian Club of Financial Directors (RCFD), new member of IAFEI

different sectors and products that a local specialized credit insurance broker could point out and find the best match for his clients needs. A challenge is the special legal environment in Russia that needs to be respected: there are restrictions for example on frame contracts, bonus schemes or the legal obligation to insure risks that are generated in Russia through a Russian insurer.

However, Russian insurers are developing their range of products and clauses constantly, mainly driven by demands of international clients and their specialized brokers.

Factoring is compared to trade credit insurance well developed in Russia. More than 50 banks and specialized companies are offering their wide range of solutions. The main business is still recourse factoring – a mirror of the shortage of liquidity through banks. But non-recourse solutions are increasingly popular, including special offers for taking over the non-payment/insolvency risk without the financing function. There is an increasing competition between factoring and trade credit insurance – not the worst situation for clients.

While most factoring companies are bank owned smaller

operations, a few of them have lately developed very smart new schemes that might be especially interesting for foreign groups in Russia. These factors also dispose of a fast network all over Russia and good know how.

### What is your advice for a company that wants to start its operation in Russia?

Go for it – this market can be still interesting for western companies!

Our main advice would be: be prepared! Bureaucracy, the legal environment and the special cultural background are certainly challenges in Russia – but they can be

▶ managed with the right preparation and patience. Make use of service providers who know their way around the numerous authorities regarding setting up an operation/infrastructure, applying for licenses, hiring staff, opening bank accounts and last but not least: attracting clients. Adapting western credit management to Russian standards/requirements helps to find the right ones – concerning their ability and willingness to pay. For managing the risk – especially these days – credit insurance is essential. But also here one needs to look out, so ask the local specialists. ●

## Investment climate in Russia<sup>1</sup>

▶ **Foreign businessmen** still find the Russian market both attractive and risky. On the one hand, according to many experts economic development will be unpredictable because of weak diversification, western sanctions and geopolitical tension. On the other hand, businesses are attracted by the Russian consumer market capacity and potential profits. However, both foreign and Russian investors say that the investment climate has considerably improved in Russia over the last years.

Foreign direct investment into Russia amounted to \$94bn in 2013, which places Russia 3rd in a global ranking on FDI inflow after USA and China. As a comparison in 2012 Russia ranked 9th and the amount in money terms was less by 83 per cent. These figures speak for themselves. Besides, according to the ranking of Doing Business-2015 Russia moved from 92nd to 62nd place.

▶ **The Global Bank reports** on the effectiveness of regulation, i.e., it evaluates how cheaply, rapidly and simply a business transaction can be performed in various countries. Such a dramatic upturn was caused not only by the reconsideration of the methodology but also by qualitative changes as well. The implementation of roadmaps of the Government was of great significance. Thus, the number of procedures to get a construction permit has been reduced to 20, and the overall time decreased to 238 days, which enabled Russia to climb 16 steps upwards. Besides, the com-

plexity level of registration of new companies improved by 24 points, and the speed of registration of new companies improved by 5 points.

It is indicative that many European companies refused to withdraw their assets from Russia after the economic sanctions had been imposed. On the contrary, the business community is actively lobbying for the cancellation of the restrictive measures. In the recent years, investors from the APR have become more involved with Russian projects. Cooperation is getting mutually beneficial: the Russian economy is being fostered by the partners' technology and finance, and the underdeveloped infrastructure provides great opportunities for work.

▶ **Therefore, there are still many issues** to be addressed. As a rule, in order to forge ahead within the Doing Business rating, it is necessary to review the procedures in terms of tariffs, time and number, to ease administrative barriers, and then to reform law institutions. Such large-scale improvements require various reforms to be implemented on an annual basis. Despite all the difficulties, Russia has the potential to achieve its goal, i.e. to be ranked 20th in Doing Business in 2018, namely, it has to move another 42 points ahead.

**1. Tamara Kasyanova, PhD in Economics**

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QUESTIONS À...



**NICOLAS DUYCK**  
DAF DU GROUPE AFFIVAL

## Comment réussir son implantation en Russie ?

PROPOS RECUEILLIS PAR **OLIVIER TONON**, RESPONSABLE GRANDS COMPTES A.U. GROUP

### Nous travaillons à vos côtés en tant que courtier depuis plusieurs années sur la sécurisation de votre poste clients, pouvez-vous nous détailler vos activités en Russie ?

Le Groupe Affival produit des consommables utilisés dans la fabrication de l'acier en particulier le fil fourré nécessaire pour obtenir des rendus de haute qualité. Nous sommes présents en Russie à travers une filiale créée en 2008 à Kolomna au sud de Moscou. La complexité des barrières douanières pour les exportateurs, nous a conduit à envisager dès le début de notre projet une implantation en local dans une région où les aciéristes sont largement présents et dynamiques. Les principaux acteurs du marché tels que SEVERSTAL, NLMK, MMK, EVRAZ, y développent en effet, des unités de production destinées à alimenter par exemple l'industrie automobile en acier de haute qualité. Nous disposons aujourd'hui d'une usine qui produit environ 2500 tonnes par an de fil fourré essentiellement destiné au marché russe et à certains pays limitrophes.

La Russie est un axe majeur dans notre stratégie de développement international et nous avons le projet de nous renforcer sur cette zone y compris en nous rapprochant des clients situés plus à l'est.

### Quels sont les principaux risques que vous avez identifiés dans le cadre de ces activités ?

Outre les risques liés à la situation politique et aux tensions avec l'Ukraine, nous sommes attentifs aux risques de change et au risque commercial.

Si le Rouble est depuis 2006 officiellement une monnaie convertible, dans la pratique, les banques ont établi un système de contrôle et de vérification des transactions assez contraignant spécialement lorsqu'elles se font en devises ou vers l'étranger. Elles imposent des démarches administratives, un formalisme rigoureux et la communication de données, voir de documents particuliers comme la copie des contrats commerciaux ou la raison des transactions. Ce risque de change est renforcé par la difficulté à trouver les bonnes compétences en local qui maîtrisent outre la complexité des contrôles, les détails des transferts entre le rouble et l'euro car le dollar reste la référence.

L'importance du risque commercial est étroitement liée à la capacité de réguler au mieux les délais de paiement. La moyenne que nous observons est de 100 à 120 jours, mais

ils peuvent rapidement dériver sans une organisation et une discipline adaptées. Nous impliquons les forces commerciales sur le terrain pour effectuer des relances régulières et fréquentes. Nous avons noté qu'il est culturellement important d'instaurer un respect mutuel avec les clients qui se construit grâce à un dialogue constant et dans la durée.

### Quelles solutions avez-vous mis en œuvre pour vous garantir contre ces risques ?

Nous avons choisi un partenaire bancaire fortement implanté en Russie et qui connaît donc parfaitement les problématiques locales. Il nous permet de bénéficier des relais d'informations et d'un support approprié sur place notamment pour les sujets de convertibilité entre rouble et euro. Nous avons également choisi de déployer une solution d'assurance-crédit qui s'appuie sur un contrat local. Il garantit nos transactions commerciales sur le marché domestique russe et à l'export vers l'Europe et les pays limitrophes. Nous y avons également intégré des clauses spécifiques en termes de délais de paiement pour coller au mieux aux spécificités du marché russe.

### Quel serait votre conseil majeur à une entreprise qui souhaiterait s'implanter en Russie ?

Apprendre à s'armer de patience pour passer les barrières à l'entrée. Le temps nécessaire à l'accomplissement des formalités est considérablement plus long qu'ailleurs et il faut en outre, s'attendre à un niveau de formalisme sur les transactions quotidiennes bien plus lourd que celui auquel nous sommes habitués.

Savoir être vigilant et informer sur les règles de « compliance » dans les affaires car les sollicitations sont nombreuses et constantes. La formation et la mise en place de procédure de contrôle en interne sont des points clés pour éviter les dérives qui sont par ailleurs très mal vues et peuvent-vous décrédibiliser rapidement sur le marché.

Enfin ne pas sous-estimer les différences culturelles dans le management des équipes locales et la définition des missions de chacun au quotidien. Il est nécessaire de rentrer dans un niveau de détails important et les directives doivent être extrêmement précises pour laisser une marge d'interprétation minimum risquant sinon d'être déstabilisante. ●