Managing Global Risk in a Changing World

An Interview with David Anderson, Head of Credit and Political Risk, Specialty Products, Zurich North America

EDITORS' NOTE *David Anderson, a 15-year Zurich veteran, launched the Sydney, Australia, Credit & Political Risk Underwriting office in 2006; launched the Singapore office in 2009; and managed the Asia-Pacific regional team until 2012. Before joining Zurich, he led FCIA Management Company's eastern region for multi-buyer credit insurance. He earned a bachelor's degree in political science from Amherst College and two master's degrees from University of Texas at Austin: one in Latin American studies and one in business administration.*

David Anderson

How would you describe Zurich's trade credit and global risk offering?

Zurich has been a market leader in structured or single-situation trade credit insurance, mainly for banks, since 2000, and added short-term multibuyer trade credit insurance in 2008. Both these coverages help protect firms from defaults on loans, sales contracts, and invoices. Today, approximately half of our trade credit insurance business is from structured trade credit and half is from short-term multibuyer.

For example, a bank may extend a five-year loan for the import of heavy equipment, running the risk that the importer defaults on that loan. On the short-term side, an auto parts manufacturer may sell parts to distributors around the world on 30-day payment terms, running the risk that those distributors do not pay for goods sold. We help the bank or the auto parts supplier protect themselves from those types of defaults. Almost every company depends on the ability to convert sales to accounts receivable to cash, and trade credit insurance can provide coverage for when it doesn't, helping customers prevent bad debt from torpedoing the balance sheet.

We also have a product called contract frustration insurance, which can provide coverage for a manufacturer or contractor that is selling goods or services on longer payment terms. This coverage includes pre-shipment risks, or risks of events that happen before shipment of goods is made, including unilateral termination of the contract and embargo. It also provides coverage for risks after shipment, including default on the contract.

What perils does your political risk insurance address?

There are three fundamental perils: one is political violence, which provides coverage not just for terrorism but also war, civil war, sabotage, and civil commotion. For companies that have assets in developing countries, those are real risks.

Then there is expropriation coverage, which is the risk that the insured's assets or equity investment in a developing country is seized by the host government and the government doesn't pay compensation.

Finally, we have inconvertibility and nontransfer coverage. There might be an operation in a country that is generating local currency but suddenly finds it has no ability to convert and transfer it out of the country because there is a balance of payment crisis and the central bank has shut down the foreign exchange mechanism.

We can provide coverage for these perils for an investor that has an equity investment or bricks and mortar in a country. We can also provide coverage for a lender who is lending to someone in that country who has to default on that loan because of those three circumstances.

Political risk insurance can also address the risk of sovereign debt default through sovereign guarantee coverage. This provides coverage for the risk of a government entity defaulting on a valid and enforceable loan or contract.

There are many other perils that can be covered with political risk insurance. A popular one is forced abandonment, which is an offshoot of political violence but doesn't require there be physical damage to the property. This applies if an area becomes too dangerous to operate in and a company suffers a loss because it has to abandon assets.

Both political violence and forced abandonment perils have increased for multinational firms because of world events, including in countries like Ukraine, Libya, and Yemen.

Zurich Insurance Group and the Atlantic Council recently released a report called "Our World Transformed: Geopolitical Shocks and Risks." Will you discuss the importance of that research and some of the key trends it addresses?

The report focused on three areas. First was the risk of global protectionism and the possibility that tariff and non-tariff barriers could rise in a number of countries, which could affect economic growth, poverty, and income distribution. Many of these issues can end up feeding into the credit and political risks that we provide insurance for at Zurich.

When protectionism reaches extremes, there are perils that can occur that can be covered on our policies, including import and export embargo or export license cancellation.

Trade credit risks can also arise, if the financial condition of companies deteriorates because of increased tariffs or an economic slowdown.

In addition to trade credit and political risks, companies are increasingly concerned about their supply chain risk. Zurich can help customers assess these risks in addition to providing insurance coverage for supply chain interruptions.

The second category the report touches on is an energy crisis as a result of Middle East conflict. The concern is with the very broad conflict that is going on between Saudi Arabia and Iran, but being fought through proxies throughout the Middle Eastern region and beyond. The risk is that the conflict gets far worse and perhaps even includes the United States or Israel in a way that dramatically affects energy prices which, in turn, can affect the world economy well beyond that region. Globally, renewable energy resources can't be accelerated to offset potential losses from the Middle East. We still need petroleum-based fuel, so this could be a significant risk.

The third area the report addresses is water insecurity and the risk of drought and of flooding. It's a growing problem, especially with the threat of extreme weather. It is also a factor that could aggravate the increased geopolitical risk in many parts of the world, and particularly in North Africa and the Middle East.

When it comes to geopolitical tensions today, is it harder to evaluate risk?

Many of the pillars of global trade and investment and of the political system are shifting today, so it has become more difficult to predict how countries will behave.

Also, social media and the Internet have accelerated the pace of change, which makes it harder to predict what political systems are going to dramatically shift at any point in time.

That makes insurance more relevant than ever. If risk managers cannot fully predict how these risks will play out, then they should at least think about managing the risk in some way, and insurance is one way to do that. ●