Credit risk will keep plaguing metals

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Washington - Credit risk will remain a threat to metals companies even if metal prices recover and the industry regains more profitability, metals industry credit advisor ProfitGuard told Platts last week.

Greater acceptance of bankruptcy and more constrictive bank lending policies are among the factors that have increased the risk that companies - even those with unblemished payment records - might default on their debts. "I know one company that went bankrupt three times in ten years," said Craig Bonnell of ProfitGuard. "There were suppliers who had taken a hit twice and were lined up again to sell to the 'new' company." Bankruptcies are no longer seen as a "last resort," Bonnell said, and the action seems to carry less of a negative connotation to many people. Bonnell pointed out that even in the high economic growth period of 1997 - 1999, there were many bankruptcies and defaults in the metals industry, as well as in the overall economy. He estimated that about "30 major defaults" had hit the metals industry since late 1997.

Increased globalization has also changed the nature of economic and credit risk, he added, pointing to the Asian money crisis of the late 1990s as an example. "A handshake no longer carries the weight it did," he commented. A company may have a spotless payment record but suddenly find itself in a credit crunch invisible to creditors, due to such things as an unexpected problem overseas or a sudden tightening by bank lenders, he said.

In fact, many bankruptcies have been involuntary, where "banks come in and seize assets," he said. Creditors can therefore find themselves exposed to much greater risk from debt defaults than they realized, Bonnell said. At the same time, the metals industry has been effectively shut off from new credit insurance policies, he added. Insurance underwriters are rejecting new policy applications due to the current weak state of the metals industry, he explained, likening the situation to trying to buy homeowners insurance in the middle of a flood.

A ProfitGuard sister company, Global Commercial Credit, offers credit insurance, but currently it too is mainly only able to service existing policies, rather than write new ones. ProfitGuard advertises it can "help clients avoid losses while maximizing revenue opportunities." It assesses a company's credit risk by evaluating financial statements and other indicators of financial health, and then it reports back to clients with recommendations on how much, if any, credit exposure to that company is prudent.

The information is gathered and shared with clients under confidentiality agreements, Bonnell said, so ProfitGuard can be candid with its clients without risking legal threats. While many companies could manage credit risk themselves, he said, even very large companies often "don’t have the time or experience" to perform the tasks effectively or efficiently. Smaller companies, which usually do not have full-time credit managers and can be severely damaged if a counterparty defaults on money owed, would be natural ProfitGuard clients, Bonnell said. Surprisingly, he said, some of his best clients are large companies that could dedicate internal resources to credit investigations but choose to outsource instead.