ProfitGuard Know The Risk *Before* You Ship | NEWSLETTER

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ProfitGuard™ is a credit research, analysis, and monitoring service providing account specific credit intelligence exclusively to companies in the metals industry.

Export-Import Bank

July 22, 2015 - - The Export-Import Bank (EXIM Bank) is an independent, self-sustaining agency that supports U.S jobs by financing the export of American goods and services. For the full year 2014, EXIM sustained $27.4 billion of U.S. exports, 164,000 American jobs, and nearly 90% of EXIM Bank transactions directly supported American small businesses. However, due to a lapse in EXIM Bank's authority, as of July 1, 2015, the Bank is unable to process applications or engage in new business.

Democrats in the Senate, though, will likely attach EXIM Bank reauthorization to legislation extending the Highway Trust Fund, which expires July 31 and has been dubbed a piece of "must-pass legislation." Time will tell if reauthorization will occur, as this legislation is likely to face more challenges in the House, where conservatives led the charge against reauthorizing EXIM.

While reauthorization of the EXIM Bank is in limbo, we must discuss private sector alternatives. Here in the U.S. there are approximately a dozen major specialty insurers of trade credit and political risk. While a relatively specialized field, this group will typically yield a number of viable insurance options for most companies.

The programs are custom tailored and each carrier has their own compliance/reporting requirements and approach to insuring your exposures. In the net, you will find that they offer a comprehensive risk transfer program that protects your open credit exposures allowing you to safely expand your overseas sales.

Many companies use export credit insurance to eliminate the need for letters of credit, to level the competitive playing field and offer attractive open credit terms. It is also used to allow lenders to include export receivables in the borrowing base on receivables backed lines of credit.

Our sister company, Global Commercial Credit, is a leading specialty broker of domestic and export credit insurance and works on a direct basis with all of the carriers who write this type of coverage. You can reach out to them at 877 422-7474 or visit their web site at www.gccrisk.com for more information.

While we hope to see Ex Im's charter reauthorized, you may find it worthwhile to explore options in the private sector as well.

Source: EXIM Bank and Global Commercial Credit

Receivables Management

July 22, 2015 - - Accounts receivable usually means you will receive payment by the end of the terms that were set, but if you have ever had to deal with collecting on receivables, you know it is not always that simple. Receivables can be a very tricky asset to manage and can ruin a company if they are not monitored closely. Today we will lay out important instructions that can help you collecting your receivables much more efficiently, while dodging risky accounts.

One of the first steps to managing receivables is to understand the health of the industry in general. A great way to help you assess the state of the industry is by keeping up on events that affect the industries that you conduct business with. Staying informed on industry news is key because it lets you know which debtors may become uncertain accounts and when it may be time to change terms or sever ties altogether. Watching the industry as a whole is a good start, but paying attention to your customers' behaviors and watching for red flags will provide great insight that industry news may not always reveal. Watching a debtor's payment history may give you a few warning signs if you start to see payments coming later and later. However, this red flag does not always present itself as many companies will pay promptly up until they default. This is why it is so important to perform periodical credit reviews on the debtor to be sure there are no rising concerns that might point to the company getting ready to default. Performing credit reviews can help minimize your risk and provide you with the tools to maintain appropriate exposure levels to help avoid a devastating loss.

Prioritizing your receivables can help identify risky accounts and also make the collection process easier and more efficient. Each company might prioritize accounts differently due to the fact that they all do not deal with the same debtors, so there is no true science to this process. With that being said, this next section will explain how to prioritize accounts in a general way that can be applicable to almost any company.

The first priority should be new customers. You want to monitor the new account closely to establish the agreed upon payment terms as being firm and avoid encouraging delinquency. If a new account is given too much leniency, it could lead to the start of poor payment habits, which could progressively get worse and cause significant problems down the road. The second priority should be the accounts that have the highest exposure levels as these will cause the most damage if they aren't collected. Most of these accounts are usually reliable, which is why they have the highest exposure, but they should be monitored to avoid a potential disaster. Lastly, the third priority should be the accounts that consistently produce slow payments. In any business, slow payments are bound to happen, but watching them closely and sending reminders to the debtor can help curve this behavior for the better and prevent their tardiness from getting out of control.

These are some of the more important and effective ways to manage your receivables, but there are many more procedures that can give you an edge during the collection process. Receivables management is an extremely vital part to any company. All it takes is one account to default and not pay and you can find yourself in deep water. Following these tips will help you minimize the occurrence of delinquency and make your company operate efficiently.

Source: Szabo Associates Inc. and ProfitGuard

Recent Events Impacting Credit Risk

July 22, 2015 - - So far 2015 has proved a difficult year for the metals industry which has led to bankruptcies, plant closures, consolidation, and overall elevated credit risk. Below are some significant events that have recently transpired.

Low oil prices continue to batter OCTG industry suppliers. Most recently, Chesterfield, Missouri based Boomerang Tube LLC filed for Chapter 11 bankruptcy, citing weak oil prices and decreased drilling activity. The company was able to secure debtor-in-possession financing and the company's term and asset-based lenders will provide $60 million in new capital injection. Many companies loaded up on cheap debt during the boom to expand and serve this segment. Now with cash flows significantly lower, debt service is becoming difficult for this segment. For the remainder of the year we expect risk to remain elevated within the OCTG segment as oil prices remain subdued and drilling activity low.

In light of low mill utilization rates, steel prices, and industry overcapacity, ArcelorMittal recently announced it would be looking to divest some of its U.S. mills. Andrew Harshaw, president and CEO of ArcelorMittal USA Flat Carbon reported that the company's largest U.S. hot strip average only 70-percent capacity utilization and have been bleeding cash as a result. Most recently, ArcelorMittal is considering closing its Indiana Harbor West operations in East Chicago which has annual capacity of 3.5 million. The closure would curb four to five percent of domestic melting capacity for steel sheet and would represent the first permanent U.S. sheet capacity closure amid recent overcapacity and supply glut issues.

Moving along, after a poor first quarter where a steep drop in scrap prices led to substantial losses and noncompliance issues with lenders, Metalico's board of directors agreed to sell the company to investment firm Total Merchant Limited on June 16, 2015 for $105 million. Total Merchant is controlled by Mr. Chung Sheng Huang, chairman of the board and managing director of Ye Chiu Group, an Asian scrap metal recycler and producer of aluminum and aluminum alloys with operating facilities in China and Malaysia. The deal is expected to close in the third quarter but certain large shareholders are opposing the merger agreement which could add additional obstacles to the deal.

Noranda Aluminum has become a developing risk in the aluminum segment. The company recently engaged Morgan Stanley to pursue strategic alternatives. At the same time, Apollo, the company's largest shareholder and its former private equity sponsor liquidated the last of its shares. None of the proceeds went to the company. The market didn't take this well as the company's stock is now trading below a dollar and its bonds are trading in the deeply discounted range of 55-65 cents on the dollar as investors and stakeholders await an outcome.

Credit risk remains elevated as industry participants face evolving market conditions as illustrated above. Pricing fundamentals in some segments seem to have bottomed and are stabilizing somewhat. We believe this will provide some positive traction in the second half of this year.

Source: American Metal Market, Keybanc, Metalico, and ProfitGuard

Evaluating Credit Risk of Parent and Subsidiary

July 22, 2015 - - Credit professionals are often left with the difficult task of how to effectively analyze the credit risk of a subsidiary and its parent company. The parent-subsidiary link could imply a very different relationship depending on what the parent's economic incentive is in the subsidiary or if there are any legal (or lending) covenants in place. This would determine how the credit risk should be evaluated between the two separate legal entities.

There is no exact science to predict the level of financial support a parent company would offer its subsidiary in a time of distress. However, there are some key factors to understand that would help you determine if the credit risk is different between the parent and subsidiary. Is the subsidiary a guarantor or borrower on the parent's lending agreement? Could the subsidiary trigger a cross-default or cross-acceleration provision in the event of a default by the subsidiary? What is the parent's economic incentive in the subsidiary?

Some of the components of economic incentive would be the subsidiary's strategic importance to the parent, if the two entities shared a name, or what is the significance of the parent's investment? Assessing the strategic importance and the potential reputational issues from allowing a subsidiary to default is a subjective process. Nevertheless, this should be an important step in your credit procedure because it will affect your view of the credit worthiness of the subsidiary.

Answering the above questions will help you to determine if you should consolidate the credit information on the parent and subsidiary during your evaluation. Either way, the subsidiary should not be rated any higher than the parent company because the parent has the ability to shift assets and liabilities to or from its subsidiary.

Source: Standard & Poor's, Morningstar, and Charles River Associates