

Underwriting Bulletin

Edition 11-01

Political Risk

Tunisia and Egypt have demonstrated how quickly previously stable countries can deteriorate. One of the consistent factors with political events which can cause catastrophic losses to exporters and investors is that the largest losses are also the most unforeseen. A good example is that the current unrest and situations, like the Iranian Revolution and the Kuwait War, were not even predicted by the major security services in the USA and Israel.

Canadian companies operating overseas must always be aware that political risks can occur at any time and in any country. Even OECD countries are not immune to civil commotion and general strikes. Recent problems in the Arab world have arisen because of an increase in food prices. The expectation is that food prices will continue to rise well into 2011 which could very well result in further unrest globally. Last year, sovereign debt risks in certain EU nations led to massive austerity measures taken by governments. These risks continue today as the world is left to hope that these unprecedented measures are successful. If not, what are the potential ramifications? It is important that prudent risk management identifies all risks from the perspective of probability and consequences. A corporate strategy for management of political risk must be continuous and comprehensive. The speed with which the political environment, in a region or country, can change makes it impossible to react on a case by case basis.

Fixed assets, mobile assets and financial assets held overseas are all subject to varying degrees of political risk. Equally important are the cash flows from the assets which can be interrupted. The latest financial reporting standards are placing more emphasis on the fair value of assets and cash flow which can be impaired by political events outside of the control of the company.

Political risk insurance coverage from both the private and public sector insurers is available to cover most risks facing companies and financial institutions selling or operating abroad. Some examples of assets that can be covered are:

- ◆ Capital investments
- ◆ Mobile equipment
- ◆ Bank deposits
- ◆ Receivables
- ◆ Contracts with Sovereign entities
- ◆ Frustration of contracts in progress

For further information, contact Millennium CreditRisk Management Limited.

11-02-17