

NOTE FOR FINANCE COMMITTEE

Contingent Liability of the Hong Kong Export Credit Insurance Corporation

PURPOSE

This note informs Members that the Secretary for Commerce and Economic Development intends to introduce a resolution for approval by the Legislative Council (LegCo) in February 2009 to raise the cap on the contingent liability of the Hong Kong Export Credit Insurance Corporation (ECIC) from \$15 billion to \$30 billion.

BACKGROUND

2. ECIC was established in 1966 under the Hong Kong Export Credit Insurance Corporation Ordinance (Cap 1115) to encourage and support export trade through the provision of insurance protection for Hong Kong exporters against non-payment risks arising from commercial and political events.

3. Section 18 of this Ordinance provides that the Government shall guarantee the payment of all moneys due by ECIC, and section 23 stipulates that the contingent liability of ECIC under contracts of insurance (i.e. the amount for which ECIC is contractually liable to indemnify policyholders in respect of its insurance policies) shall not exceed a specified amount which may be determined by LegCo by resolution.

4. Over the years, the cap on ECIC's contingency liability has been raised several times. As recent examples, it was revised from \$7.5 billion to \$10 billion, \$12.5 billion and \$15 billion through resolutions approved by LegCo on 17 December 1997, 13 March 2002 and 29 March 2006 respectively.

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5. As at 31 December 2008, ECIC's contingent liability was amounted to \$14.53 billion; or 96.8 per cent of the maximum liability permitted. Moreover, since October 2008, ECIC has been introducing measures to strengthen its support for small and medium sized enterprises during the current financial turmoil (details at Enclosure).

Encl.

6. With these new measures and the increasing business volume¹, ECIC forecasts that the existing cap on its contingent liability will be reached very soon, by around February 2009. To strengthen ECIC's underwriting capacity and to cater for business growth in the next few years, we propose to raise the cap by \$15 billion to \$30 billion. Taking into account the current economic situation and our need to strengthen support to the small and medium sized enterprises, we consider ECIC would need a larger underwriting capacity to provide buffer for offering sufficient export credit insurance covers to our exporters. The ECIC Advisory Board welcomed the proposal.

FINANCIAL IMPLICATIONS

7. With the introduction of the enhanced support measures and in face of the global financial crisis, ECIC expects that their loss ratio² will increase from currently around 40% and will peak at 65% in 2008-09. It will subsequently reduce to 60% and 55% in 2009-10 and 2010-11 respectively.

8. ECIC has a policy to maintain adequate reserves to meet its obligations, including the contingent liability. Taking into account ECIC's healthy balance of net assets and reserve³, ECIC considers that the implementation of these enhanced support measures would not affect their financial self-sufficiency. When conducting its financial assessment, ECIC has already taken into account the estimated underwriting business and loss ratio in the coming few years and it expects that notwithstanding the financial crisis, it will manage to achieve a profit, albeit at a small amount, in the coming few years.

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¹ ECIC expects that the business insured will be increased from \$42,947 million in 2007-08 to \$46,000 million, \$47,000 million and \$49,500 million in 2008-09, 2009-10 and 2010-11 respectively.

² The loss ratio represents the value of gross claim over the value of gross premium income (turnover).

³ The balances of ECIC's net assets and reserve as at 30 October 2008 are \$1,099 million and \$1,079 million respectively and ECIC expects that its reserve will continue to increase in the coming few years.

9. In view of ECIC's prudent policy and its healthy financial condition, we do not expect the need for Government to provide financial support for ECIC to meet its liabilities in at least the short to medium term. ECIC will continue to conduct its business within the bounds of prudent risk management and review the situation regularly and take necessary actions if the situation warrants.

Commerce and Economic Development Bureau
January 2009

Enhanced measures of the Hong Kong Export Credit Insurance Corporation

Enhanced measures of the Hong Kong Export Credit Insurance Corporation (ECIC) launched a series of enhancement measures in October and November in 2008. Key ones are –

(a) *Higher insurance cover for exports*

ECIC has agreed to be as accommodating and flexible as possible to the small and medium sized enterprises' requests for export credit insurance and increase the insurance cover, within the bounds of prudent credit assessment and risk management. Furthermore, ECIC has introduced a mechanism under which deductibles for claims and lower-than-usual indemnity ratios for the insurable exports (the usual indemnity ratio being 90%) will apply, if necessary, for sharing out the risks.

(b) *Higher insurance cover for emerging markets*

To assist Hong Kong exporters to develop emerging markets, ECIC has reviewed its country/market ratings of 15 emerging markets and upgraded six of them, namely the United Arab Emirates, Kuwait, Chile, Brazil, the Czech Republic and Malaysia. ECIC will, where risks allow, provide higher credit limits for exporters to these markets. The premium rates for the upgraded markets will also be lowered.

ECIC will continue to closely monitor the economic and political situation in other countries/markets and conduct regular reviews. Their ratings will be adjusted whenever appropriate.

(c) *Annual Policy Fee Waiver*

ECIC will waive its annual policy fee^{Note} of \$1,500 for one year from 1 January to 31 December 2009.

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^{Note} Policy fee is an annual fee to cover part of the costs of acquiring necessary credit reports for processing of credit limit applications. The policy fee is charged at the beginning of each policy period.

(d) *Expediting the processing of small credit limit applications*

ECIC has expedited the processing of applications for small credit limit of \$0.5 million or below to two to three days upon receipt of adequate information (normal processing time is currently four days; five days before 1 October).

(e) *Free credit checks*

ECIC will offer each exporter a certain number of free buyer credit assessment service.
