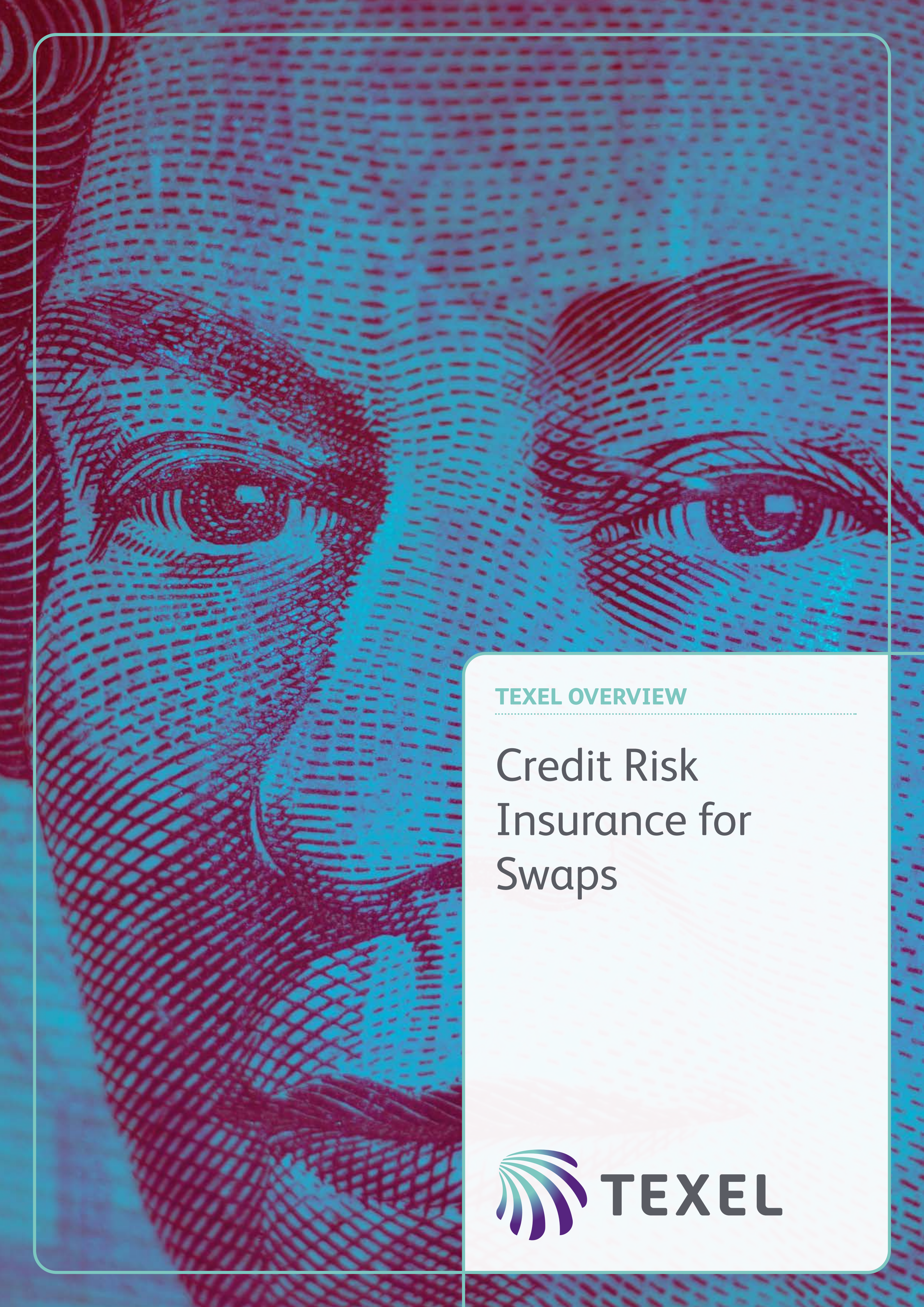

TEXEL OVERVIEW

Credit Risk Insurance for Swaps

TEXEL

Credit Risk Insurance for Swaps

Non-payment insurance ('NPI') for derivatives is a product that has become very useful for banks looking to reduce their capital and credit limits held against their books of swaps and options.

These transactions are typically governed by market-standard documentation from the International Swaps and Derivative Association (ISDA) but a traditional NPI policy would struggle to correctly mirror the underlying transaction structures. Our in-house legal counsel and broking team have regularly helped institutions to draft NPI documentation covering large single counterparty exposures either in the form of multi-transaction interest rate and currency swaps or single trades. These unfunded and uncollateralised exposures often weigh heavily on an institution's capital and counterparty credit limits and therefore a bespoke NPI policy can significantly improve our clients' internal hurdles and allow them to expand their lending relationships with their core counterparties.

It is important to note that the NPI market for these forms of transactions is much less deep in notional capacity. However, the insurers supporting these transactions are staffed adequately with the expertise to understand the structures employed by their clients. Such insurers can thus provide a strong partnership for those clients able to work together with their broker to draft NPI documentation that accurately meets each party's needs. Insurance premium rates for this form of coverage are often charged as a minimum return for the insurers' capacity to ensure that they obtain an adequate return on their capital. This is effectively a commitment fee, with any counterparty credit exposures generating on-risk premium for the insurers based on an agreed and certain premium rate.

Tenors for this form of NPI vary from 3–10 years depending upon the credit quality of the underlying swap counterparty and the trades covered by the NPI policy. The NPI policy will indemnify the insured at the end of the waiting period for the insured percentage of the settlement amount due to the insured from the counterparty in the event of an early termination or maturity of the ISDA.

EXAMPLE TRANSACTIONS

Insured	Multinational bank
Transaction	A portfolio of interest rate and cross-currency swaps
Obligor	(Swap counterparty) sub-sovereign European Electricity Company
Tenor	7 years
Cover	Over USD100m from 3 A+ rated insurers

Insured	Multilateral financial institution
Transaction	A single cross-currency swap which benefited from local currency collateral
Obligor	(Swap counterparty) African telecommunications company
Tenor	5 years
Cover	USD50m from 5 A+ rated insurers

ABOUT TEXEL

The Texel Group is a market-leading specialist insurance broker, primarily focused on the development, structuring and execution of NPI policies for our clients. With over 20 years' experience at the forefront of the international insurance markets, we are staffed by individuals with skills and experience to help our clients understand the product and ensure that it is correctly structured to obtain the maximum capital and limit relief possible for each transaction.

KEY POINTS:

- Portfolio of trades or single trade
- Limited but experienced market of insurers rated A- or better
- NPI can provide capital and credit limit relief if appropriately structured
- Premium generally charged on the insured percentage of the positive counterparty credit exposure under the derivative(s)