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Central and South America – untapped market or cash drain?

_by Bob Schmitt

Most risk management professionals will appreciate that there are differences, and greater inherent risks, in dealing with international customers in unfamiliar environments. Bob Schmitt, director at US-based CRIBIS Corporation, gives an insight on the challenges associated with information gathering and commercial credit application processing in Central and South America.

When companies expand outside of their domestic environment, the lure of the perceived opportunity can sometimes overwhelm good business sense. When this is the case, due diligence is often sidelined in favour of aggressive efforts to penetrate a new and untapped foreign market.

Central and South America offers the tantalising combination of emerging markets and companies which display a strong ethic for importing goods and sercvices. For many selling companies, this combination is impossible to ignore; but it is exactly that combination that makes Central and South America a potential drain on cash flow if not managed properly.

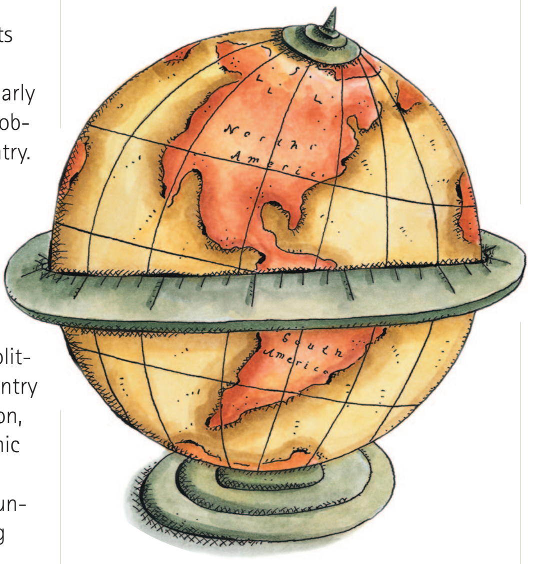
Just as exporting to different continents requires a level head and a steady hand, exporting into different countries (particularly in Central and South America) presents problems and challenges peculiar to each country. One should quickly develop a very real understanding of what is meant by 'normal terms', and one should be aware of local laws and collection practices.

After the determination has been made that there is a market worth attacking, the first thing to do is evaluate the political/economic risk associated with the country in question. In some countries in this region, the political risk will outweigh the economic risk.

There are several sources that offer country evaluations that will aid in determining political/economic risk in each country including:

- bank reports;
- Coface (*www.cofaceusa.com/products_services/country_risk_assessment.html*)
- Rundt's Weekly (*www.rundtsintelligence.com*);
- Periodicals;
- US Foreign and Commercial Service Reports (*www.usatrade.gov*);
- FCIB Country Reports (*www.fcibglobal.org*);
- FCIB Credit and Collection Surveys (*www.fcibglobal.org*);
- FCIB Political Risk Reports (*www.fcibglobal.org*);
- IMF (*www.imf.org*);
- country agencies;
- the World Bank (*www.worldbank.org*);
- colleges and universities (for example, Bryant College – *www.itdn.net*);
- local and regional international groups;
- local agents;
- Export-Import Bank (*www.exim.gov*);

Compounding the issue is the fact that many credit insurers will not cover individual firm risks in some Central and South American countries (especially in those that have a high risk rating). If they do, they may require country risk coverage, thereby increasing the cost of doing business. This makes for increasing levels of competition and puts a premium on making good risk/reward decisions.



The increasing competition allied with the development of individual country markets in Central and South America are encouraging signs for the industry, although this does mean that risk managers are called upon to make ever tougher decisions about what constitutes fair risk and unacceptable risk. These difficult decisions are made even more testing because many importing companies seem very cooperative, potentially increasing the pressure to have credit approved based on that cooperation.

"In many Central and South American countries, the desire to import product is so strong that these firms are extremely willing to supply information," says Robert Lucht of US-based information provider Veritas-USA. "However, it is important to consider the reliability of the financials delivered. It is not uncommon for a firm to maintain several sets of books, so it may be worthwhile to compare financials secured directly with what is reported to a credit reporting firm."

It is therefore advisable to use secondary sources of information to help validate information. Several information providers report on companies in each of the Central and South America countries, including SkyMinder (*www.skyminder.com*), Veritas-USA (*www.veritas-usa.com*) and D&B (*www.dnb.com*).

There are also a number of domestic reporting organisations that provide reports on local companies. All of the following are members of the Latin American Business Credit Reporting Association (*www.alaic.com*) and offer credit reports in these specific countries:

- Chile - Trans World Services (*www.tws.cl*);
- Argentina, Brazil - Sintesis (*www.sintesis.com.ar* and *www.sintesisbrasil.com.br*);
- Columbia - Byington (*www.byington.net*);
- Costa Rica - Protectora de Credito Comercial (*www.protectora.com*);
- Ecuador - Infaes (*www.alaic.com*);
- El Salvador - Altagracia Gregg (*www.alaic.com*);
- Guatemala - Informacion Comercial Internacional (*www.alaic.com*);
- Honduras - Honducredit (*www.alaic.com*);
- Mexico - Profancresa (*www.profancresa.com*);
- Panama - Tribaldos and Asociados (*www.alaic.com*);
- Peru - Credit Report (*www.creditreport-group.com*);
- Uruguay - Sintesis (*www.sintesis.com.ar*);

• Venezuela - Venezolana de Servicios Comerciales, Vesercom (*www.alaic.com*).

In Columbia, as in many other countries in South America, all companies are required to submit some level of financial information. Publicly-held companies are required to file reports with the country's securities regulator. Banks, insurance companies and other types of financial companies are also required to file specific data with appropriate agencies.

"The Columbian DIAN receives full financial information on all companies but this is not publicly available," says Diego Arboleda, Director of Columbia-based reporting organisation Byington. "However, the local chambers of commerce receive most of the relevant figures including total, current, fixed and other assets, current and long term liabilities, net worth, and sales and profits on a yearly basis.

"This public information is readily available but has some important quality limitations," adds Arboleda. "The chambers of commerce do not perform any quality checks, so the user may find that the balance sheets don't balance. Also, the chamber asks for a) sales, b) cost of goods sold or operating expenses, and c) profit or loss. The problem here is in the 'or': the reader may not be able to determine if the figure shown is a profit or a loss or operating expense or cost of goods sold."

No payment information repository

In most Central and South American Countries, there is no commercial repository of payment information, so the information that is displayed in reports is largely generated via references that are contacted individually.

In Peru, Chile, Argentina and Brazil, there is a "protestos" system that reports returned cheques and collections and this information is publicly available. Arboleda reports that in Columbia there is no protestos, but that there are credit bureaux that collect this type of information along with payment information. Access to this data is only permitted when authorised by the subject company, however.

"Based on a period of one year, we established that 5.9 per cent of the 40,000 trade references taken showed terms under 30 days, 64.4 per cent were between 30 and 59 days, 23.9 per cent between 60 and 89 days, 4.8 per cent between 90 and 119 days , 0.7 per cent between 120 and 149 days, 0.1 per cent between 150 and 179 days, and 0.3 per cent over 180 days. On terms such as between 30-60 days, we used the average (ie 45 days)."

Banking information is also difficult to obtain because this information is considered private and will not be released without authorisation of the subject company. This is typically done in the form of a release letter from the subject of the investigation and on company letterhead. The information will invariably take some time to be transmitted.

OPERATIONAL STATISTICS

Country	Average response times in days			Report content			
	Super flash	Flash	Normal	With financial figures	With complete financial	No. of trade refs	No. of banking refs
Argentina	3	5	10	90%	80%	2	2
Chile	2	3	7	80%	56%	3	3
Colombia	NA	4	8	90%	70%	4.6	3.4
Costa Rica	3	5	10	20%	20%	5	NA
Ecuador	3	4-6	10-12	70%	5%	2	2
El Salvador	1	3	5	95%	95%	3	2
Guatemala	3-5	5-10	10-15	95%	70%	3-5	NA
Honduras	3	5	10-12	5%	NA	2	NA
Mexico	5	10	15	80%	70%	3	1
Panama	NA	4-7	10-15	NA	NA	3-5	3-5
Peru	3	4-9	10-15	85%	67%	4.5	2.5
Venezuela	2	4	10	60%	60%	3	2

Table 1: Comparison of speed and quality of reports by country in Central/South America

"Credit reports from Central and South America should be analysed in the same way that a credit report from another region is analysed," says Arboleda. "However, additional weight should be given to slow payments since they are hard to find, given the privacy limitations. For example, if a company shows 10 prompt payments and two slow ones, I would give very special attention to the two slow ones. The big difference really resides in how credit is extended and managed. Invoicing has to be very careful and should de done as per local norms in case defaults take place and legal action is required. Guarantees should also be obtained as per local norms.

"Skip-tracing information is very limited and the legal systems are not efficient, so it is imperative to take quick action against slow debtors," adds Arboleda. "You cannot wait 360 days before contacting a local collection agency – 120 days overdue is the most I would advise."

Low quality of credit reports

In general, the quality of commercial credit reports for companies in Central and South America does not rank with the level of information available in US or western European commercial reports. In Columbia, Chile, Argentina, Peru and Brazil, the report quality is better, and in Ecuador the reports are improving. However, due to historical issues and archaic public record systems, information sources in other countries in the region are limited – and therefore the quality of reports is inferior.

Table 1 (above) compares the kind of information available in a sample of countries in the region and serves as an indication as to the level of information that one can expect to find in reports based on country.

When contemplating doing business with firms in Central and South America on open credit, it is worth remembering that you are likely to have to make decisions with less information than you would when evaluating firms in western Europe or North America. You will also need to utilise other sources and methods, like securing releases from local banks and credit bureaux, in order to evaluate risk. Most importantly, beware! If you give in to the vision of an "untapped market", your cash flow will suffer.

Bob Schmitt is director of US-based CRIBIS Corporation, leading development of the Skyminder business information service in the US, Canada and Central and South America. Email: r.schmitt@cribis.com