TRADE LINE

Coface's magazine for its clients and partners

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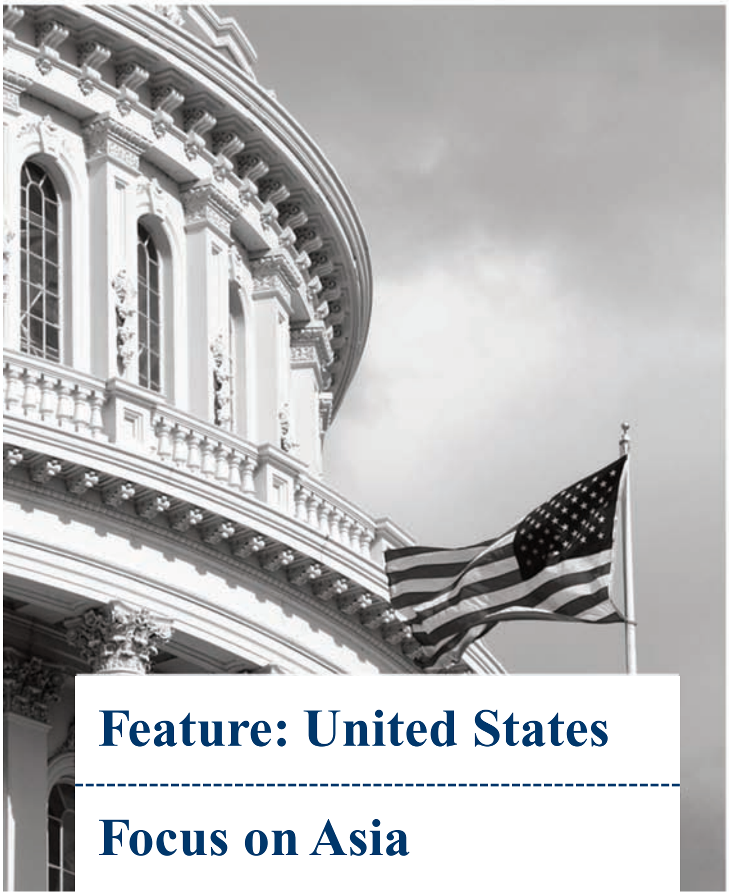

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Construction of the gigantic stadium of Soweto

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The United States faces the spectre of anaemic growth

The United States remains the planet's leading economic power. As evidence, one need only consider the simple fact that the US consumer accounts for 70% of the US economy and 18% of global GDP. The economic spotlights are therefore focused for very good reasons on rising petrol prices, falling housing prices, unemployment and unequal profit distribution, all of which undermine household confidence. The outcome of the political debate between the Republicans and Democrats over the US budget and national debt as well as the Fed's orientation and monetary policy as from July are therefore also under close scrutiny.

Focus on the US economy.

Christine Altuzarra,

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The federal debt burden: pragmatism will likely win out

Coface North America held its Country Risk Conference on the 12th of May in New York against the backdrop of the debate in Washington and the media over raising the US legal debt ceiling at the federal level. On 9 May, the public debt exceeded the $14,290 billion limit authorised by Congress. An ideological gap divides Republicans and Democrats on this issue. The former are conditioning their support for raising the ceiling upon drastic cuts in government spending, in particular the Medicare programme for retirees. The latter are pushing for tax hikes for the wealthiest Americans, whilst agreeing to reductions in some expenses, notably defence-related.

A technical default by the US federal government does not appear likely, since both parties demonstrated their capacity for compromise last November when they voted to extend the Bush tax cuts in order to support the still-fragile economic recovery. This agreement helped the global economy stave off a double-dip recession. In all likelihood, therefore, political leaders will again reach a compromise before the 2 August deadline and after some electoral concessions have been made to assuage pressure from the Tea Party on Republicans. The failure to reach a compromise would undoubtedly create further turmoil for the economy, since growth has not yet become self-sustaining.

But the expected agreement will need to be accompanied by a draft plan to reduce the federal debt over the medium and long term. Placement of the US federal debt (still triple-A rated) on a negative watch by Standard & Poor's in April and by Moody's in June served as warnings regarding the urgent need to stabilise public-sector finances, since the budget deficit is expected to exceed 9% of GDP in 2011.

US purchasing power under pressure

Numerous negative effects are undermining US households' confidence. These factors come on top of the uncertainties surrounding needed reforms to public sector finances, which entail the possibility of tax increases. Consumers must contend with rising prices, notably for petrol. At nearly $4

- Pragmatism of political authorities in the conduct of budgetary policy
- Full employment is one objective of the Federal Reserve, which in the case of price stability tends to focus more on core inflation than nominal inflation; monetary policies are very responsive
- US dollar still plays a preponderant role in the global economy
- One-third of corporate earnings originate abroad
- Historically high net cash positions of large corporations
- Dynamic demographics

- Reforms are harder to implement following the Obama administration's loss of a Democratic majority in the US House of Representatives
- High public-sector budget deficit and federal debt.
- Precarious financial condition of several states
- Consumption accounts for a significant portion of US and global GDP (70% and 18%, respectively)
- Still weak production capacity utilisation rate
- Structurally high unemployment
- Workforce's geographic mobility limited by the collapse in housing prices
- Substantial amount of infrastructure in a dilapidated state

"Public debt: an ideological divide between Republicans and Democrats"

per US gallon, the price has nearly returned to its peak of the spring of 2008, curbing consumers' mobility and consequently their consumption, notably of food and textile products. Compounding the problem of rising consumer prices is the decline in housing values. The residential construction industry is experiencing persistent sluggishness, as new housing starts have plummeted and sales of housing have been depressed since the April 2010 expiration of the first-time home buyer tax incentive. Moreover, stocks of unsold housing could increase to a significant degree, as banks and credit institutions bring foreclosed houses onto the market. The seizure of these assets was in fact suspended last autumn after revelations of non-compliance with foreclosure procedures. Approximately 2 million homes could be added to existing stocks, and at current sales rates it may take three years to sell them all. Property asset values are therefore expected to continue to decline and remain underwater, i.e. below the amount of the mortgages contracted to finance the purchases. This trend is restricting people from job searches, since prior to this latest crisis they were more readily able to move from one state to another and follow the job offers.

In addition to rising prices and declining home values, the fragile labour market recovery is a third factor affecting consumer confidence. The percentage of unemployed Americans remains very high (around 9% of the working-age population) relative to the usual US standards. This figure rises to 16% if one includes tenuous jobs. The share of long-term unemployed workers continues to increase. More than 43% of unemployed workers have been without a job for more than seven months, and even more worrisome, the mismatch between supply (educational services, healthcare and retail) and demand (construction) is an obstacle to a substantial rebound in the labour market. Private sector job creation is expected to continue to increase, but at a rate that is too low to make a significant dent in unemployment. In 2010, only 1.3 million jobs were created, compared to the 8 million lost as a result of the crisis. The upcoming period of budgetary cutbacks at both the federal and state levels will dampen public-sector job creation and also negatively affect the establishment of training solutions that are essential if structural employment is to be reduced significantly.
In spite of these negative factors, however, the extension of the aforementioned tax cuts will support consumer spending, which is expected to grow by more than 2% this year. But this growth in spending will be limited by the continued de-leveraging of US households. Household debt has already fallen from 132% of disposable income in 2007 to 118% in 2010. Concerned about the future, US households will in all likelihood maintain a high rate of savings relative to their past practices, around 6% of disposable income.

Coface's credit risk assessment for the United States has not returned to its pre-crisis level

Coface assesses the average default risk of companies based on their short-term sales transactions, generally a credit period of no more than six months. The rating for the United States (A2) has been assigned a positive watch. Consequently, the country has not yet returned to its pre-crisis rating of A1. To be sure, the US corporate default rate has begun to ebb since mid-2009, when it reached a high of 220 (index base 100 in early 2007), whereas defaults in France and Germany were 130 and 115, respectively. This difference is partially due to the high degree of responsiveness by US companies to the economic cycle, which leads them to enter Chapter 11 protection quickly. Nevertheless, the level of defaults remains well above that observed before the crisis. Payment incidents recorded by Coface have decreased significantly but remain slightly above the global average.

The pace of new job creation is insufficient

In an environment marked by cutbacks in public-sector spending and budgetary rigour, the private sector will continue to play a key role in supporting economic growth through renewed hiring and productive investment. As discussed earlier, although the trend observed in the early months of 2011 marks a turning point, with more sustained new job creation, it will not be sufficiently dynamic to bring about a significant reduction in unemployment. Investment spending on capital equipment and software will continue to trend favourably (around 10% in 2011), in contrast to investment in the retail and production areas (-2%). The latter sectors remain in dire straits, even though large corporations posted record earnings in 2010 and are sitting on historically high levels of cash, which in fact facilitate their share buybacks. In spite of these strong results, companies remain cautious.
This caution can be explained in part to the likely impact this year of rising commodity prices on company profit margins, with some sectors concerned that they will not be able to pass on the price increases further down the supply chain or, in the case of the retail sector, directly to consumers. Manufacturing companies – notably chemicals and textile producers, transport companies

and agri-business – will be especially hard-hit by these commodity price increases. Yet another factor weighing on companies is the fallout from the Japanese earthquake and tsunami on the electronics and automotive sectors as regards the distribution channels and the slowdown in the supply of components used in production. For small businesses, meanwhile, the greatest impediment to development is undoubtedly increasingly restricted access to bank financing. This problem is compounded by the fact that regional banks (the main financial partners of small businesses) have themselves been weakened by their exposure to the property sector. In this environment, capital spending and employment will not be able to record any major increases, especially since production capacity utilisation rates, which last April stood at nearly 77% for the overall industrial sector, have not returned to their pre-crisis levels.

The foreign trade contribution remains very weak

Despite the slowdown in economic growth observed in emerging market countries since the beginning of the year, demand from these countries is expected to remain vibrant. As a result, renewed growth in US exports is expected to continue (between 7% and 8%), helped by a favourable US dollar exchange rate. On the flip side, however, the foreign trade contribution would at best make only a very slight contribution to economic growth this year, given the increase in import prices on goods and services from Canada, the euro zone, Australia, Sweden and the United Kingdom. The currencies of all these countries are particularly strong relative to the dollar. Although the dollar bill continues to serve as a safe haven currency and could therefore experience occasional upticks, the trend this year will continue to favour negative pressure on the dollar.

> “Economic growth is supported by budgetary and monetary policies”

The US Federal Reserve policy of monetary easing, commonly known as QE2 (“quantitative easing”), naturally abetted the dollar’s slide. The Fed, it will be recalled, decided to establish a programme to purchase long-term government bonds from financial institutions with a dual purpose.
The first is to raise inflationary expectations and therefore modify the consumption and investment behaviour of households and companies in order to prevent the United States from entering a lasting deflationary period.
The second objective is to drive down long-term interest rates. The liquidity thus injected into the economy should favour lending to economic participants.
We now know that the Fed only partially achieved these goals, since new lending volume remains flat and well below the highs observed prior to the crisis.
This phenomenon must be viewed in the context of the current de-leveraging trend of economic participants, who on the whole are showing little appetite for new loans.

The risk of a slip without QE3

At the time of this writing, a debate is currently under way over the possibility of another round of quantitative easing (QE3) or some other form of monetary support for the economy. All signs suggest that the Fed, whose mission is to ensure both price stability (core inflation target of 2%, i.e. excluding energy and food products) and promote employment (with a “natural” unemployment rate of 5.78% of the working-age population), will extend its policy of monetary easing or reinvestment in government bonds recognised on its balance sheet in order to maintain liquidity in the economy. Clearly the Fed needs to maintain low interest rates and a weak dollar, which supports the export sector and therefore employment, while at the same time funding the federal debt through inflows from non-resident investors. However, rising prices for imported products (excluding commodities, which are for the most part denominated in dollars) would continue, thereby fuelling inflation.
The risk of a surge in consumer price inflation nevertheless appears to be limited, given the modest increases in wages and salaries in an environment of high unemployment. In the first quarter of 2011, core inflation was less than 1%, thus below the Fed’s target.
The continuation of a weak dollar policy would nevertheless be a handicap for the competitiveness of companies in the world’s other economies, and the abundance of liquidity generated by a QE3 would increase the risk of overheating in numerous emerging market countries. That could heighten the risk of a speculative bubble in asset prices.
The well-known adage of John Connally, Richard Nixon’s Treasury Secretary, to a European delegation worried about currency fluctuations – “the dollar is our currency but your problem” – continues to apply today.
Before the crisis, US economic growth was robust thanks to the voracious appetite of companies and households for credit. Since 2008, it has been supported by the US government’s budgetary and monetary policies.
Economic growth will be propped up yet again this year by budgetary stimulus measures adopted in late 2010 and is expected to reach approximately 2.2%. All indications are that the recovery is not yet self-sustaining and that US medium- and long-term growth is expected to be comparable to euro zone growth rates of around 2%. In 2012, the Obama administration will have little leeway to pursue effective budgetary stimulus measures, even in an election year.
And yet household consumption is a decisive factor for self-sustaining growth. US companies clearly hold the key to a return to better economic times through new job creation and a redefinition of profit distributions.

Christine Altuzarra

Céline Choulet,
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Financial regulation: the impact of the Dodd-Frank law remains difficult to assess

The Dodd-Frank Act, enacted 21 July 2010, has been described as the most sweeping reform of the US financial system since the 1930s. This law is intended to promote financial stability in the United States, limiting the inherent moral hazard of some financial institutions "too big to fail" and protect investors and consumers of financial products. The political conflicts and technical difficulties surrounding the implementation of the legislation have nevertheless limited its impact, even as the regulatory agencies complain about the lack of funding to back it up. The Dodd-Frank law required that numerous feasibility studies (67) be conducted and that application rules (243) be drafted by some 10 different regulators. Nearly one year after the act's passage, only 27 rules of the various sections of the law have been specified by the regulators.

A still complex oversight architecture

One federal banking regulator (Office of Thrift Supervision) was eliminated, but some 10 new agencies were created, notably the Consumer Finance Protection Board (CFPB) and the Federal Insurance Office (FIO). The supervision of systemic risk has been assigned to the new Financial Stability Oversight Council (FSOC) consisting of 10 members (the eight federal regulators, including the Federal Reserve, the Federal Deposit Insurance Corporation, the Securities and Exchange Commission, etc., an insurance expert and the Treasury Secretary, who chairs it). This macro-prudential oversight agency seeks to identify systemic risks and issue recommendations to minimise them. It has been designated as competent to arbitrate conflicts among regulators but has not been given any real corrective authority. At the risk of upsetting financial stability, the necessary coordination between the FSOC and the Financial Stability Board (FSB) (created at the London G20 summit in April 2009) is not mentioned in the Dodd-Frank Act.

By introducing legislation as early as the summer of 2010, US regulators sought to take the lead on such major issues as the handling of systemic risk and regulation of derivatives markets. However, the lack of convergence and consistency among the prudential regulatory frameworks of the major economic zones (United States, Europe, Asia) threatens to leave the door open to competitive distortions and regulatory arbitrage at the expense of financial stability. Thus even as the migration towards Basel 2 remains incomplete, no commitments on the full transposition of Basel 3 or on the G20 recommendations as regards financial sector remuneration have been taken so far in the United States. Moreover, US regulators have considerable leeway as regards the interpretation and application of the Dodd-Frank legislation (scope of application, precise definitions of the respective activities and products, compliance deadlines), such that its impact is difficult to assess..

Treatment of systemic risk, cornerstone of the Dodd-Frank Act

The US law seeks to develop an optimal policy for reducing systemic risk (strengthened capital adequacy standards, concentration limits, separation of risky activities from those covered by public guarantees, transparency of derivatives market, tightening of criteria for granting mortgage loans), by ensuring that this policy limits the problems of moral hazard inherent in public-sector guarantees (increased contribution from large institutions to the Federal Deposit Insurance fund, living wills, orderly liquidation and bail-in procedures) and that it protect citizens..

Additional operating charges for banks

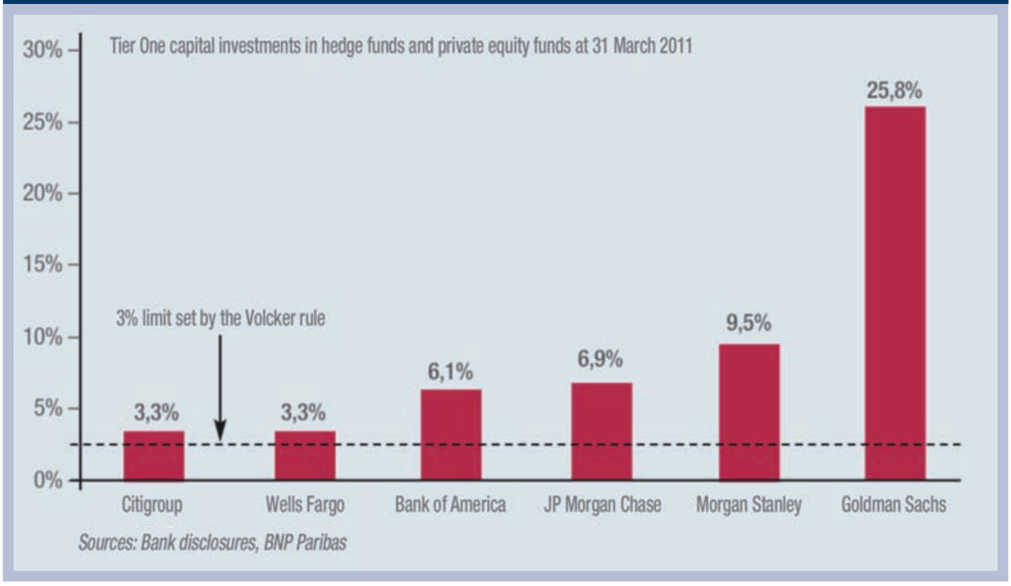
Since the definitive rules have yet to be published, the cost of the new regulations for US banks remains uncertain. Net commission income and income from arbitrage transactions are expected to decrease, while operating expense (compliance measures to be taken by financial institutions to satisfy the new regulations, quarterly reports on overall credit risk exposure of companies, annual resolution and recovery plans) is expected to rise.
Some measures, which are designed to improve the quality of mortgage loans and render the practices of lenders and brokers more transparent, should limit allocations to loss provisions over the longer term. Banks could partially offset the drop in their commission income by raising rates for other services. In fact, that concern may have led to the announcement last 29 March of the entry into force of the Durbin amendment, which seeks to cap inter-bank commissions on debit card transactions and put an end to certain anti-competitive practices of the bank card networks.
The initial proposal, which set a ceiling of 12 cents per transaction, could have cut annual income from these commissions by up to 75%.

Some measures, such as the Volcker rule, could encourage the transfer of risky activities from the banking sphere to the shadow banking system

The “Volcker rule” seeks to separate some risky activities from those covered by public guarantees, in the spirit of the Glass Steagall Act, passed in 1933 and repealed in 1999. The rule prohibits institutions that receive public backing (deposit guarantees from the FDIC, access to Federal Reserve liquidity) from carrying out proprietary trading activities when such transactions are not performed to cover transactions conducted on behalf of their clients or in their capacity as market makers. Bank investments and sponsoring of hedge funds and private equity funds are also

Chart 1

The Volcker rule weighs heaviest on Goldman Sachs



Sources: Bank disclosures, BNP Paribas limited to 3% of the funds' capital and 3% of the banks' Tier One capital. The compliance deadline was set at two years from the time of the adoption of the definitive rules, which is scheduled for between now and July 2012, renewable annually for up to three years. Even though the requirement to comply with the Volcker rule is not expected to apply until 2014, the large US banks (Goldman Sachs, Morgan Stanley, JP Morgan Chase and Bank of America) have taken the lead by pledging to withdraw from certain activities. While the constricting nature of the first measure remains difficult to evaluate, given that the boundary between prohibited and authorised activities under the Volcker rule is tenuous, the limit on investments in hedge funds and private equity funds should weigh heaviest on Goldman Sachs. At 31 March 2011, four of the six largest US banks had exposure to alternative funds and private equity funds that exceeded the Volcker rule limit by 3 to 23 percentage points *(see chart 1 page 8)*.

The Volcker rule has two major limitations:

- Barring a clarification of the scope of prohibited activities, its application could be countered by legal challenges. The Volcker rule could also create regulatory arbitrage opportunities, since the evaluation of bank investments in hedge funds is subjective. These funds are for the most part recognised as level 3 illiquid assets (assets whose fair value is determined using theoretical models based on unobservable parameters).
- This rule could lead to a transfer of risks from the banking sphere towards less regulated investment vehicles. This risk is even more acute to the extent that the attention focused on large systemic institutions will undoubtedly motivate the creation of smaller entities susceptible of avoiding oversight from regulators.

The size of the shadow banks exceeds that of the commercial banks

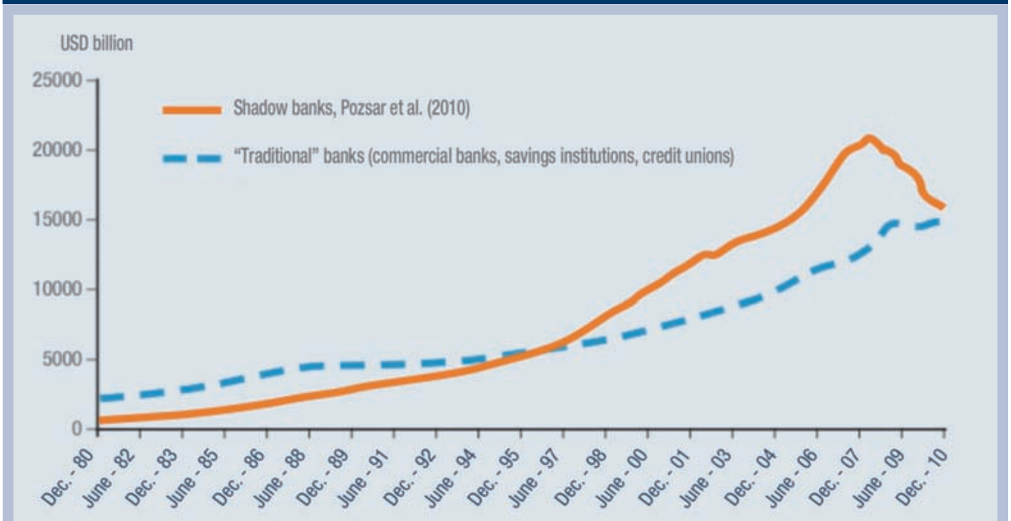
Relying on a study by the Federal Reserve Bank of New York(*), the Financial Stability Board proposed in a memorandum published last April to define the shadow banking system, by its economic function, as "a system of credit intermediation that involves entities and activities outside the regular banking system, and raises systemic risk concerns, in particular by maturity/liquidity transformation, leverage and flawed credit risk transfer, and/or regulatory arbitrage concerns." According to the study's authors, the size of the shadow banking system in the United States at end-2010 was nearly $16 trillion, compared with only $13 trillion for just the commercial banks *(see chart 2)*.
Distinct from traditional banks, shadow banks are not covered by banking regulations and do not enjoy public-sector guarantees. Shadow banks are vertically integrated along a sometimes lengthy intermediation chain and maintain close relations with regular finance. They use a panoply of securitisation and short-term financing instruments (issuance of structured products, repo transactions).
Some provisions of the US banking and financial regulatory law seek to strengthen the oversight of certain components making up the shadow banking system (hedge fund registration with the SEC, regulation of the activities of the rating agencies, strengthening of requirements for credit risk retention and transparency of securitised products).
However, some of the lessons of the recent financial crisis have not been learned. In particular, no proposal was advanced to regulate the risks posed by money market mutual funds or prevent a freeze of the repo transactions market in the event of uncertainty as to the quality of the collateral. The US repo market, whose liquidity is provided by money market funds, therefore remains exposed to a substantial risk of a run, which is what led to the establishment of special emergency measures by the Federal Reserve in 2008.

Céline Choulet

(*) Pozsar, Z., Adrian, T., Ashcraft, A. and Boesky, H. (2010), Shadow Banking, Federal Reserve Bank of New York, Staff Report No. 458.

Chart 2

Size of the shadow banking system in the United States



Sources: Fed, Federal Reserve Bank of New York

US companies are recovering but must change strategy

Most US companies are currently in much better health than they were during the economic crisis. Business volume is anaemic, but several economic factors have contributed to the stabilisation of the growth cycle. Coface North America, a subsidiary of Coface, gives us its point of view and analyses three key sectors of the US economy.

Gross domestic product increased at a 1.8% annualised rate between January and March, after rising by 3.1% in the fourth quarter of 2010. Despite the weakness of these numbers, the US Federal Reserve still expects that growth will continue at a sustained enough rate to bring about a gradual decrease in unemployment, even if the level is likely to remain high through end-2012.

Job creation should provide households with renewed confidence and motivate them to borrow and spend more. Unfortunately, the indicators have been pointing in the wrong direction in recent months.

Along with many economists and political leaders, many Americans continue to worry about the size of the US budget and debt. This concern was exacerbated by rising oil and petrol prices, although in April the price at the pump slipped back as a result of the dual impact of a collapse in demand and the considerable stocks accumulated.

In the banking sector, the situation is improving thanks to a turnaround in asset markets, the de-leveraging of balance sheets and lower interest rates. It nevertheless remains a concern for several reasons. The number of impaired assets and foreclosed commercial and residential property assets remains high, demand for loans is flat and regulations could become more restrictive.

The situation varies substantially depending on the industrial sector. The manufacturing sector will contribute to GDP growth in 2011, thanks in large part to the increase in exports. Chemical industry sales are rebounding after several years of declining production and are expected to grow by 3% in 2011. The pharmaceutical products sector, the largest worldwide, is expected to grow by 3% to 5%. It should receive a boost from the competition between generic drug producers and the large industry players, all coming against a backdrop of healthcare system reforms and the expiration of major patents.

Automotive

Detroit's Big Three automakers (GM, Ford and Chrysler) lost the confidence of US households in 2009 after they

Coface in the United States

Coface has been present in the United States since the early 1990s. Its subsidiary, Coface North America, currently has 400 employees and markets credit insurance solutions in the United States and Canada. It also offers companies commercial and marketing information as well as receivables management services.

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were particularly hard hit by the global economic crisis. This crisis also showed that the vehicles offered by these three companies were not competitive against cars with more modern designs, reflecting more aggressive research and development efforts.
Moreover, the Big Three's sales consist mainly of pick-ups and SUVs as opposed to smaller cars, which run on less petrol and are increasingly favoured by consumers in the light of higher petrol costs. This trend could affect the profitability of the US carmakers, which is largely dependent upon sales of pick-ups and larger vehicles. Ford and GM have nevertheless reoriented their strategy and chosen to manufacture smaller, more compact cars, as well as mid-size sedans such as the Ford Fiesta, Ford Fusion, Chevrolet Cruze and Chevrolet Malibu. All of these models sell well. Thanks to their ample net cash positions, Ford and GM will also be able to withstand any temporary setbacks.
The large US automotive manufacturers have recorded dramatic improvements to their operating income. In 2010, Ford's sales increased by 19% to 1.94 million vehicles, while those of GM and Chrysler rose by 7% and 17% to 2.2 million and 1 million units, respectively. In the first quarter of 2011, Ford recorded a profit for the seventh consecutive quarter after years of losses. This profit was the highest since the first quarter of 1998. GM's first-quarter 2011 profit was $1.7 billion, the highest since 11 years ago, when it recorded a profit of $1.8 billion in the second quarter of 2000. Meanwhile, Chrysler recorded its first quarterly profit ($116 million) since 2006. After its disposal of Volvo, Ford has only the Ford, Lincoln and Mercury brands, while GM has refocused its activities on four major lines – Chevrolet, Buick, GMC and Cadillac – and has sold or discontinued the Saturn, Hummer, Pontiac and Saab brands.
Ford also decided to round out its line of luxury cars (Lincoln) at the expense of Mercury brand vehicles, which the company ceased manufacturing as from end-2010. Ford plans to launch seven new Lincoln models over the next four years, including a small car.
The earthquake, tsunami and nuclear disaster in Japan seriously disrupted the activities of automotive manufacturers and suppliers worldwide. Automotive equipment supply chains incurred various disruptions, which led to production interruptions, workday reductions and order cancellations.
The United States is the leading sales market for Japanese vehicles, and by itself Japan accounts for 13% of global automobile production. Some 40 Japanese automotive suppliers experienced production problems as a result of the shut-down of the nuclear power plant and power outages caused by the earthquake.
The supply chain disruptions would appear to be less serious than initially thought, and many suppliers believe that their production will return to normal by the fourth quarter of 2011 or first quarter of 2012. The catastrophes that occurred in Japan also represent an opportunity for US and European automakers to regain market share. Also, even if parts shortages were to last in the best case scenario until the fourth quarter, the drop in demand should enable the affected companies to recover. In the meantime, the drop in supply has prompted manufacturers to offer fewer sales promotions, which may enable them to generate higher margins on the still unsold vehicles.

Retail

Last year, a number of factors prompted households to reduce their spending: the sluggish economy, an unemployment rate near 9.5% and the persistent recession in the residential housing market. These factors all motivated household consumers to be more conservative and weighed on retail sales in 2010.
The number of defaults in the sector remained stable in 2009 and 2010. Blockbuster, the largest electronics retailer in the United States, sought Chapter 11 bankruptcy protection and Borders, the second-largest bookstore chain, did as well in February 2011. Two smaller, regional retailers Bernie's (Northeast) and Ken Crane's (West Coast), also filed for bankruptcy protection last year. With no major mergers or acquisitions in the sector, the market shares of the respective players remain essentially unchanged.
Many of the large electronics mass market retailers, such as Best Buy, HHGregg, Gamestop, RadioShack and Rent-A-Center, have ceased offering sales promotions as generous as those

advertised in 2009, in the wake of the 2008 recession. Some smaller distributors may, on the other hand, be tempted to extend their sales promotions, thereby leading to lower profit margins and cash flows and causing their key debt ratios to deteriorate. It can seem wise to cut prices in order to attract customers. But such a strategy entails risks: too small to take advantage of the efficiency of the supply chain and having only marginal leverage to pursue favourable price terms with their suppliers, these retailers could be drawn into a vicious circle of sales promotions even as consumers remain cautious in their discretionary spending.

Overall, mass market electronics retailers stand to lose from any deterioration in household confidence, as consumers become less inclined to purchase high-tech gadgets. Any time the economy experiences a period of sluggish growth and consumers become gloomy, their first spending cuts are made in luxury products and consumer appliances.

In spite of these handicaps, retailers appear to be well positioned to benefit from a recovery.

The National Distribution Federation (NRF) estimates that retail sales will increase by 4% in 2011, an estimate that is nevertheless based on the unexpected vigour of sales during the Thanksgiving and year-end holidays. They could nevertheless suffer the impact of inflation resulting from rising commodity prices and the still high unemployment rate. Even online sales, which reached a record high of $43.4 billion in the fourth quarter of 2010 (up 11% relative to the previous year), could fall if the price volatility of foodstuffs and energy continues to force households to make cuts in discretionary spending.

Department store earnings are expected to disappoint in 2011, given the radical change in consumer behaviour and the fact that these retailers are incapable of recouping the market share taken away by discount and super-discount stores during the recession. Their sales growth is expected to be less than 1% this year, even as retail sales are expected to record modest overall growth.

Performance will vary from one store chain to the next. The large national chains such as Kohl's, Nordstrom and Macy's will in all likelihood generate relatively satisfactory earnings. The smaller, regional chains such as Dillard's and Bon-Ton will face an uphill battle, as they struggle to differentiate themselves from the large national chains.

The discount and super-discount chains are expected to hold on to the market shares that they seized from department stores during the recession. Concerned above all with shopping at the lowest possible price, households will probably continue to favour these discounters over the department stores. This trend should be confirmed over the next 18 months.

US department store earnings are expected to increase at a very modest rate in 2011, much like those of other retailers. The lack of confidence and increasingly scarce credit are leading consumers to take fewer risks. The NRF's forecast of higher consumer spending nevertheless limits the risk of incurring losses. Better stocks management and cost reductions during the recession made it possible to improve margins. However, the effects of these changes have already been felt. In order to generate continued growth in profits, retailers will need to boost sales. It is not certain that they will succeed, given the aforementioned reticence shown by consumers. Moreover, increased transport expense and an unfavourable exchange rate for imported goods could weigh heavily on gross margins in 2011. The increase in textile commodity prices, which manufacturers are currently passing on to retailers, could affect the retailers' profit margins.

Construction

In 2010, some but not all segments of the construction industry experienced renewed growth. Individual home construction picked up slightly at the beginning of the year, but sales of new homes fell once again following the expiration at end-April of the federal tax credit offered to new home buyers. Builders responded by cutting their prices, and these reductions weighed on their margins. The scope of the stimulus measures proposed by the US administration (to renovate motorways and bridges as well as in the environmental area) is partially limited by the increasing scarcity of bank credit and widening budget deficits at the state and municipal levels. This situation also weighs heavily on some types of construction such as offices and schools.

For the remainder of 2011, the outlook must be analysed with an eye toward the fact that the US economy has indeed begun to grow again, but still faces major handicaps. The drop in consumer confidence combined with the increase in the number of foreclosed homes – which was already very high – only exacerbates the difficulties. At the same time, the weakness in the labour market and restructuring of the retail sector increase the supply of offices and stores even as demand remains flat.

“The discount and super-discount chains are expected to hold on to the market shares that they seized from department stores during the recession”

Coface North America

Interview with Kenneth Moyle,

Executive Vice President of Coface North America

“Investment spending is picking up again, led by purchases of capital equipment”

The situation in the property market remains challenging, but the large banks have turned around, as have corporate earnings. The dollar’s weakness also makes US exports much more competitive. Overall, companies that lacked the resources to obtain guarantees during the crisis are now increasingly turning to credit insurance.

What is the situation of US companies on the credit front?

Kenneth Moyle (KM): The economic recovery has enabled our clients to increase their sales. This increase is accompanied by increases in available credit and Coface credit insurance guarantees.

We are also observing renewed interest in credit insurance. During the crisis, the need to control costs was such that US companies did not have the means to purchase guarantees. Now that they are seeing their sales grow slightly in a market that is still fraught with substantial credit risk, they are more inclined to obtain credit insurance. They do not want to see the considerable efforts made to survive the crisis reduced to nothing as a result of an unexpected default.

Have some sectors returned to normal business volume?

KM: The turnaround in the North American automotive sector is noteworthy. During the credit crisis, manufacturers experienced their own crisis. Demand was collapsing and consumer credit was all but unavailable. This crisis not only provoked the insolvency of General Motors and Chrysler, but also that of many automotive suppliers. Although the large automotive suppliers are well known to the general public, the crisis clearly highlighted the true scope of the supply chain. We thus discovered a panoply of SMEs which, at first glance, had nothing obvious to do with the automotive industry. Subsequently, it became apparent to what extent subcontractors who manufacture parts and components for large automotive suppliers were affected by the near total production stoppage at GM and Chrysler.

We are also observing an uptick in retail sales thanks to the recovery of US consumption. The evaporation of a substantial portion of their property and financial market assets during the crisis prompted households to exercise considerable caution and reduce their indebtedness. They are once again ready to borrow, albeit clearly in a more careful manner than before, but consumer spending is again on the rise.

> “We have a long way to go and we are still witnessing many secondary and tertiary effects”

Are there other sectors that are struggling to rebound?

KM: The market situation for residential construction and real estate remains problematic. Many assets are still subject to foreclosure proceedings. And the stock of vacant housing units remains very high relative to any relief through demographic growth.
We therefore have a long way to go and we are still witnessing many secondary and tertiary effects. Demand for furniture, flooring and household appliances is highly correlated with new home sales.
A turnaround in residential construction cannot be excluded at the regional level this year. It should be noted that the central regions of the United States experienced a record number of natural disasters this year. Between floods and tornadoes, towns in some regions were entirely destroyed and they need to be rebuilt.

Is the banking sector back on solid footing?

KM: The large New York banks have without a doubt recovered. Most have already paid back the funds received as part of the TARP plan and consolidated their balance sheets by bolstering their equity. The massive losses and impairment charges on credits and derivatives are now behind them and their operations are returning to normal.
I believe that credit standards have improved, but that demand remains well below the pre-crisis peaks.

> "Despite the consolidation in the second quarter of this year, consumption spending remains higher than it was during the recession"

According to some articles published in the trade press, US companies have accumulated record levels of cash. Is that really the case and what are the consequences?

KM: The *Fortune 1000* rankings show that companies have massive liquidity reserves. The turnaround in earnings due to cost reductions generated substantial cash, which companies are choosing to hold. However, a significant share of this cash remains abroad, as companies would prefer not to repatriate their foreign profits so as not to incur the tax liability in the United States. The large corporations' massive liquidity is not always available to be invested in the domestic market.

Are US company investments back on the rise?

KM: US companies have cut back on their investments. They are concerned about rising energy prices and a possible slowdown in global economic growth. That said, we are observing renewed growth in investments since the end of the crisis. They are expected to record overall growth of 6% to 8% this year, driven mainly by capital equipment purchases. Meanwhile, construction spending will remain weak.
We are also observing an increase in technology investments by companies. Microsoft Vista was a failure from their point of view. They now appear to be turning to Windows 7 and are beginning to replace old computers using the Windows XP operating system.

Consumption, the US growth driver, is waning once again. What are the consequences?

KM: Despite a drop during the second quarter of this year, consumption spending remains higher than it was during the recession. While the turnaround may be modest, the trend is favourable. US companies see it as grounds for optimism.
However, as long as unemployment hovers around its current level of more than 9%, the growth in consumption will remain limited.

What impact will President Obama's plan to stimulate exports have on the US economy?

KM: Industrial companies, whose production accounts for 12% of the country's economic output, remain the spearhead for the recovery begun in June 2009. They are benefiting from companies' investments in new capital equipment and the demand from emerging markets such as China, Brazil and Mexico. US exports reached an all-time high in March. While the weakness of the US dollar may upset some of our trading partners, it nevertheless has the effect of making US exports significantly more competitive.

The United States represent an enormous outlet market for consumer electronics made in Japan. Does the recent catastrophe there affect US companies?

KM: The events in Japan will in all likelihood affect the automotive and retail sectors. Japan is a leading supplier of specialised automotive components, and the supply chain will be disrupted at least temporarily. As regards retailing, high-end brands such as Tiffany & Co., which generate a significant portion of their sales in Japan, will be negatively affected. Other retailers with a strong presence in Japan such as Gap, Inc. and American Apparel will record sales declines in their Japanese stores. Wal-Mart Stores, which owns more than 400 stores and supermarkets in Japan, will also feel the impact.
A substantial portion of consumer electronics production has been transferred from Japan to other low-cost countries such as China and South Korea. Nevertheless, the manufacture of essential components, in particular certain memory cards, remains exclusive to Japan. Thus disruptions are to be expected, but they will be more localised than widespread.

Interview by
Trade Line

Roy Rabinowitz,
Senior Vice President of Finance, L'Oréal USA

"The hidden benefits of credit insurance"

L'Oréal USA is the US subsidiary of the cosmetics industry's global market leader, which is based in Paris. It sells to large department store chains and thousands of smaller, local boutiques. It has subscribed credit insurance from Coface North America (CNA) for four years as part of a policy managed by Roy Rabinowitz, the company's Senior Vice President of Finance. Although his main responsibilities involve legal matters (including taxation and customs duties), Rabinowitz is also the person responsible at the company for determining customer credit limits.

"We pay close attention to our 50 largest customers, who account for the vast majority of L'Oréal USA sales," notes Roy Rabinowitz. To limit these major risks, L'Oréal USA has worked with CNA to come up with a special credit insurance policy: credits of less than $25,000 are not insured, those between $25,000 and $2 million are reviewed and those above $2 million are systematically guaranteed."

For credit lines of that size, direct and frequent contacts with the main CNA underwriters are necessary. According to Roy Rabinowitz, CNA's underwriters are first-rate financial professionals. They are open-minded and capable of obtaining suitable guarantees.

> "Credit insurance enabled us to get closer to our customers and refine our sales policy"

Based on his experience in credit insurance, Rabinowitz has discovered two unexpected benefits. "The most important is unrelated to the insurance policy we subscribed. Naturally, credits represent an important part of our balance sheet, for which guarantees against non-payment are useful. But there are two other additional benefits.

First, the decision to subscribe insurance requires us to establish rigorous and standardised procedures for managing credit problems. To some extent, such procedures reassure subscribers with whom we communicate more easily."

In addition, credit insurance has enabled L'Oréal USA to get closer to its own customers. "We really need to understand their business, in order to better define their needs as regards credit," says Roy Rabinowitz. For example, during the economic crisis, we discovered that our cosmetics product displays attracted customers in the department stores, thereby confirming the role of L'Oréal USA as an essential supplier to these stores. That enabled us to convince Coface that the department stores, cognisant of L'Oréal's importance, would settle their bills on time.

Mr Rabinowitz recognises that this understanding of the customer could lead to a change in direction. "Even if the answer to the credit request is negative, we will continue to seek to minimize the risk profile by organising, for example, smaller or more frequent deliveries or perhaps by monitoring stocks."

Interview by
Coface North America

Jean-François Rondest,
Group Communications and Claims Department, Coface

Handbook on US Bankruptcy Code's Chapter 11

The US Bankruptcy Code consists of 15 chapters; since October 2005 and with the exception of Chapter 12, they are all odd-numbered.
The Chapter 11 procedure deals with the reorganisation of legal entities in difficulty ("bankruptcy reorganisation") and, occasionally, of individuals. Thanks to its substantial flexibility, this chapter is often a reference point for the bankruptcy reorganisation laws of many other countries.
The US court-ordered insolvency processes are administered by the bankruptcy courts, which are special federal courts.

Initiation of the procedure

The request to initiate bankruptcy reorganisation process is made by the debtor when it can no longer satisfy its liabilities (voluntary petition) or, more rarely, by three creditors (involuntary petition) whose total credits amount to at least $14,425 (this amount was adjusted most recently in April 2010). To support the reorganisation request, the debtor must produce various balance sheets and financial statements, the list of the 20 largest unsecured creditors and make a payment of $1,039 to the court clerk's office for case handling and administrative fees.

The debtor remains in charge of the business

The debtor is responsible for turning the company around and undertakes all measures aimed at reconstituting the company's treasury. The debtor is known as the "debtor in possession", or DIP.
That is the unique feature of the system, since the debtor is also the trustee (except where fraud, deceit, incompetence or gross negligence is involved, at which point a case trustee is appointed).
The manager may undertake all current management and asset disposal actions independently as part of the company's activities. The manager continues to operate the company normally.
For unusual transactions, the debtor needs to obtain court approval after consulting with a committee of creditors.
It is up to the debtor to settle normal expenses incurred following the "bankruptcy reorganisation" and, each quarter, US trustee fees until the process is either converted into a Chapter 7 (liquidation) proceeding or concluded through a vote on the Chapter 11 reorganisation plan.

Automatic stay

Individual claims by creditors are suspended for all claims originating prior to the declaration of insolvency. That is the so-called automatic stay.
This breathing spell is supposed to provide the manager with an opportunity to reorganise the company's business free from any external pressure, which explains the commonly used expression of a company seeking bankruptcy protection under Chapter 11.
Creditors with secured claims may not exercise their financial guarantees, unless expressly authorised by the bankruptcy court.

United States trustee

The US trustee – a civil servant of the US Department of Justice appointed by the bankruptcy court – oversees the implementation of the process and reviews the monthly reports prepared by the debtor.
The trustee is responsible for convening and presiding over the creditors' meeting (the so-called 341 meeting of creditors in reference to article 341 of the Code) between the 20th and 40th day from the initiation of the process. At this meeting, the debtor testifies under oath on the conduct of the company's activities and all its assets.

Filing a proof of claim

As a general rule, creditors do not have to file a proof of claim if they also appear in the debtor's schedules.
That is not the case, however, in the case of conditional, illiquid or disputed claims, which require that a claim be filed with the bankruptcy court clerk within the prescribed deadline, so as to then be recognised and authorise the creditor to vote on the bankruptcy plan and receive dividends.

Creditors' committee

The US trustee appoints a creditors' committee consisting of the seven largest unsecured creditors.
This committee plays a major advisory role during the process, controls sales transactions conducted by the manager and participates in the development of the plan.

The reorganisation plan

Along with a disclosure statement that presents the financial information of the company to enable creditors to reach an opinion on the feasibility of the proposals, the reorganisation plan must be presented by the debtor within 120 days and approved within 60 days following its presentation (total of 180 days).
The court may grant a deadline extension, which may not exceed 18 months, plus 60 days for approval (total 20 months).
At the confirmation hearing, the reorganisation plan is approved if it receives more than half the votes in number and two-thirds in amount of recognised claims for each class of creditors.
Only those creditors whose claims are modified by the plan (impaired claims) may vote.
The plan, whose average duration is between three and five years, is then submitted to the court for certification.
A plan rejected by a class of creditors may nevertheless be certified by the court (cramdown method) if the court deems that the plan does not discriminate against the dissenting class and has been presented in good faith, thereby preserving all of a company's chances for recovery.

The concept of "critical vendors"

This concept originates with the doctrine of the need for payment and case law.
If the company's reorganisation runs the risk of failure because vendors, who are already creditors, choose to withhold new shipments essential for the company to maintain its commercial activity, the debtor may obtain court approval for these vendors to receive preferential payment for their pre-petition claims and new deliveries. These vendors are given the status of "critical vendors".
In January 2002, the critical vendor doctrine was contested as part of the K-Mart Corporation bankruptcy proceedings before the Seventh Circuit Court of Appeals in Illinois, which had to address the abuse of the number of critical vendors receiving preferential payments. Going forward, the debtor must justify that the deliveries required for the continued operation of the business will ultimately benefit all other creditors.

Jean-François Rondest

Sylvie Portero,

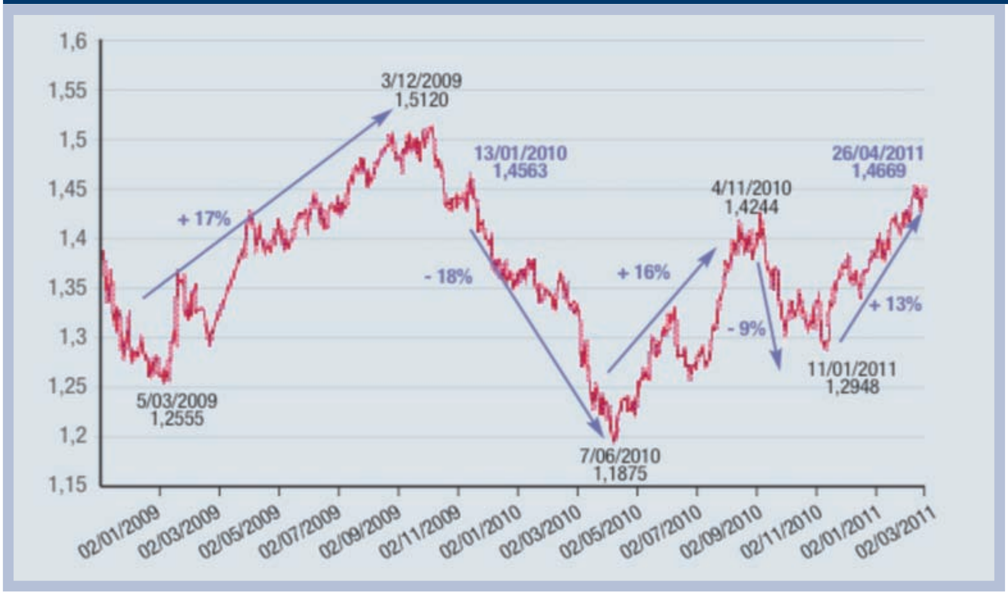
SME International Development,
Public Guarantees Department, Coface

The euro's surge against the dollar, a handicap for exporters

The start of 2011 was once again marked by a sharp increase in the euro/dollar parity.

After the European Central Bank increased its benchmark rate from 1% to 1.25%, the first change since May 2009, the euro reached a new high of 1.47 against the dollar, a level not seen since December 2009 and a 13% increase in the first four months of 2011.
The appreciation occurred following a highly uneven trend in 2010, as the common currency fluctuated in line with attitudes ranging from mistrust to appetite for the euro.
As evidenced by the trend line on the chart below, the euro lost 18% against the dollar during the first six months of 2010, at the height of the Greek debt crisis. This downward trend was then halted by a confluence of several factors: the creation of a euro zone stabilisation fund, the end to the strict yuan/dollar peg, the establishment of budget austerity plans in Europe, etc.
The euro then embarked on an upward trend in the second half, albeit with frequent corrections, and regained 16% between June and November 2010.
This situation weighs on European exporters, whose competitive position

Euro versus dollar trend



has deteriorated relative to companies whose costs are denominated in US dollars.
Companies that engage in occasional foreign currency transactions must therefore be able to stabilise the price upstream from the transaction, as soon as the bid is made and even before the commercial transaction outcome is known.

That is the principle behind Coface's "exchange risk for negotiation cover", as part of the guarantees it manages on behalf of the State. Given the fluctuating environment, the exchange rate guarantee is essential to maintain competitiveness and profit margins. It is not surprising that demand for guarantees increased by 22% in 2010 relative to the previous year.

At present, considerable uncertainty reigns: the debt crisis in Europe, persistent political upheaval in the Middle East, the nuclear crisis in Japan, US deficit, etc.
In other words, companies need to be cautious and hedge against currency risk.

Sylvie Portero

Depending on the status of the negotiations, Coface offers two guarantees:

➔ Exchange risk for negotiation cover Coface: immediately upon responding to an international tender

- Protection against currency losses: 100% indemnification of any currency loss recorded at the time of payment.
- In the version with participation: opportunity to benefit from a 50% to 70% rise in the currency during the commercial negotiation period in order to improve competitiveness.
- 11 currencies are covered: US dollar - British sterling - Canadian dollar - Swiss franc - Yen - Singapore dollar - Australian dollar and Hong Kong dollar - Norwegian krone - Swedish krona and the Danish krone.

Also, under certain conditions, the Czech koruna and Polish zloty.

The cover binds the exporter only if the bid is accepted.

➔ Coface exchange risk cover for contracts: in the final negotiation phase or for contracts signed within the past 15 days

- Contracts up to €15 million maximum
- US dollar and British sterling covered

The cover binds the exporter only if the contract takes effect.

Michael Deschodt,

Director of Trade Services at the French American Chamber of Commerce in New York

How to approach the US market

The US economy's vast size attracts European exporters. Michael Deschodt has helped exporters approach this market for seven years. He offers some tips.

Focus on the local connection

According to Michael Deschodt, "in the United States the key is not necessarily to sell but to provide high-quality service to the market. A French company can easily manage its exports to a neighbouring country such as Germany using its existing infrastructure. Thus an office equipment supplier based in Lyon can sell his products in Frankfurt without any difficulty. But when you serve the US market, what do you do if business does not go as planned, or if trouble arises? You first need to reassure your customer, let him know that you will take care of him. For most industrial companies, that means having an on-site presence. In some sectors, such as wine production or fashion, companies are fortunate to have a well-honed distribution network that French exporters may use. But in other branches, everything needs to be started from scratch. Companies find that they are isolated."

Develop a culture of service

"The US business culture revolves around services. In the United States, companies expect to work with local subsidiaries, and any difficulties should be resolved at local level. Customs clearance, for example, should take place even before new relations are developed with a customer. Stocks should be kept on site, and in order to succeed the company must be able to provide local service.
Companies should have a full-time representative in the United States. A customer will be reassured to see a US address and telephone number on a supplier's business card. The customer will then feel confident that he will not encounter communications problems related to time zones or language with his new business partner.
Deschodt concedes that such an effort to maintain a local presence requires time and money. "The employees are the key to success," he adds. And that is where the challenge lies for small export companies. Many face a dilemma. To establish a local presence, they would prefer to send an expatriate that they know and trust rather than hire someone on site. But the people with the best chance for success are the ones who are native to the country".
One effective method consists of using a French controller working with a local partner, who becomes the company's ambassador in the US market. Deschodt recognises that "it may be more costly, but it can also increase the chances for success".

Having a sales culture

"Another key factor is understanding that the US sales culture is very different from the French one", adds Deschodt, who himself has dual nationality. "French companies have a hard time understanding that US companies do not respond to sales pitches based on a demonstration of their worth in the past." The French approach consists of developing a good reputation and then explaining the company's activities in detail, whereas the US approach is much more direct.
"The US customer wants to know how you are going to satisfy his expectations, the time it will take and the cost."

Suitable products for the market

"Don't be afraid to adapt your product or how it is sold or marketed," says Deschodt. Wine is a good example. US customers appreciate wine from around the world: United States, France, New Zealand, South Africa, etc. So while the concept of terroir (local area of origin) may have major connotations for French wine consumers and exporters, a US consumer will in all likelihood have a more general approach and will talk of a "French chardonnay" as opposed to referring to a specific wine region or French village.
According to Deschodt, "the solution is to visit the market and talk to some customers who might be interested in a product like yours." There are many organisations such as the French American Chamber of Commerce that can bring together exporters and potential customers. "The value of such market research cannot be overstated. Americans will answer you honestly. It is up to you to listen and adapt your products and services to satisfy their needs", he adds.
The French American Chamber of Commerce is the largest organisation in the United States in the area of Franco-American inter-company relations. For more information on this institution, please visit: **www.faccnyc.org**

Interview by
Coface North America

Philippe Tissot,
CEO & Chairman of EIE Global

"Ambition and caution", two key words when approaching the US land of opportunity

Philippe Tissot jumped into the US market in 1999. Over 10 years, he has experienced ups and downs, successes and failures, but has ultimately seen his project through. As a French Foreign Trade Advisor, he also devotes some of his time to sharing his experience with other SMEs interested in exporting.

For a service company such as yours, how does one launch a venture in the United States?

Philippe Tissot (PHT): As with any international project, you need a good business plan, with a clear and well-defined strategy. You need to ask yourself many questions. Where will I be in five years? How will I get there, and with what resources? What are the obstacles I will encounter along the way? What will help my company's development? How are my products and services better than those that already exist on the market? For the United States, you need to examine the regulations in your sector closely, and also come up with a distribution network. You also need marketing initiatives adapted to the scale and diversity of the country. Use a local agency. It will have a better understanding of the market, how to approach it, the requirements of your future customers, the tone to use, the best product design, etc. I think you need at least three years in order to find a niche. No improvising allowed. You also need a substantial budget to cover specialised legal fees and marketing expenses.
As you can imagine, for all that you need time and a flawless organisation. A small company's strategy can only be implemented by its manager. He needs to be the one who visits the country, at least in the beginning, and therefore cover his bases by entrusting the management of his company in France to a reliable deputy. Once on site, the company needs to implement reporting tools quickly in order to control and monitor the activity closely and respond quickly in the event of problems.

Doesn't taking one's time run counter to the rapid response instincts of Americans?

PHT: You also need to allow for a key expectation of our American friends, i.e. responsiveness. Generally speaking, French entrepreneurs are not responsive enough. An American businessman will ask a question or note a problem and expect to receive an answer in quasi-real-time. Otherwise he'll have no qualms looking elsewhere. While the French are known for having good ideas and good products, they also need to improve the quality of their sales support.

Is the use of lawyers a defining characteristic of the United States?

PHT: Absolutely! The omnipresence of lawyers in this country is impressive. Lawyers are everywhere, both in private life as in the business world. You have to protect yourself against everything! For example, never interview a female job applicant alone to avoid being accused of harassment. Leave your office door open during the job interview or meet the job applicant along with another employee. There are roughly as many lawyers in Chicago as there are in all of France. In practice, remember that in the legal area, jurisprudence takes precedence over the law itself. In the case of a dispute with a customer, employee, supplier or even a partner, the contents of the contract are binding, regardless of the actual law. If you have signed a contract with a loophole, the opposing party will seize it and it will be your tough luck! Don't wonder whether or not you need a legal advisor to monitor your activity. It's essential. The only question one should ask is how much to budget in the business plan, knowing ahead of time that it will need to be substantial! In the United States, the rules of the game are clear. In the event of a legal dispute, the parties' lawyers are there mainly to haggle and earn money based on weaknesses in the opposing party's contract.

➔ You refer only to specialised lawyers.

PHT: Yes, it's better to avoid generalist lawyers, even if they may be useful initially to get the lay of the land. You will want to find a lawyer specialising in intellectual property to protect your brand, another to draft your sales contracts, one for your employment agreements, another to handle an agreement with a distribution network, etc. The proverbial image of how the West was won in the 19th century involves a six-shooter in one hand and a Bible in the other. Today, the market is won with a fistful of dollars in one hand and a lawyer in the other. In order to choose well, you can look to the French Foreign Trade Advisors who are present in the United States. They are experts in guiding you to the best specialists.

➔ What are the typical characteristics of an American businessman?

PHT: It is always dangerous to generalise, but the business man clearly has great qualities. He is open, welcoming, empathetic, trusting and enthusiastic. He has a solid understanding of business and a penchant for innovation. Americans like foreigners and are quick to accept immigrants. Foreigners speak several languages, which for a native American is rare. Being a foreigner is "a plus". Take advantage of it!

Open and welcoming, the American business man has no trouble talking about his business and experience. If he trusts you, the US business man will be perfectly ready to recommend you, even to a competitor. Being known and trusted by one's customers or prospects is necessary, but not always sufficient. Don't think that the excellent relations you have with a customer will last forever, even if the relationship is tantamount to friendship. Far from it. Americans, pragmatic as they are, are not always loyal in business. Watch out for compliments, which they are fond of doling out. You may occasionally have the impression that you have sealed the deal since your contact person appears enthusiastic and full of praise. Americans like to talk about what is working, and only rarely about what isn't. You therefore want to be careful not to fly too high. It helps to be a bit paranoid. No one is looking out for you, and everyone wants your money or the benefits of your products and services. Nothing is free.

➔ Do Americans have a flair for innovation?

PHT: I would even go further and say that innovation is one of the driving forces behind business in the United States. Americans flock to innovation. They will leave you at a moment's notice for a supplier who, in their eyes, is more innovative, more profitable and more efficient, or who offers them greater value added.

➔ In other words, competition s merciless?

PHT: The world's largest economy is naturally a highly competitive market. Competitive trends need to be monitored very closely, in particular innovations within the sector. Customers are constantly seeking new partners who can provide them with more value added. For that reason, you will be readily welcomed by companies, but also just as easily pushed to the sidelines. You must keep selling the customer on the advantages of using your products and services, and less on the purely technical aspects. French SMEs are clearly not sufficiently aware of this principle and continue to focus more on the technology than on the marketing.

EIE Global, an advisory firm

EIE Global is a service provider that helps companies exhibiting at international trade shows increase the return on their investment.

The firm advises customers on the communications and production strategy and control of event-related costs.

It also manages operations at the global level and delivers turnkey solutions in each country where the company exhibits: trade show communications, stand and event production, related services, travel and accommodations.

The firm specialises in the defence, aerospace, security, energy, environment, healthcare, information and communications technology and luxury goods sectors.

Its growth strategy is based in part on winning market share in the United States, where the firm generates more than 50% of its annual revenues.

At present, the firm has 12 full-time employees and annual sales of €2.5 million.

What advice would you give as regards payment means and collection techniques?

PHT: As regards payment means, everything goes. In our case, our services are payable before the service is performed, which avoids any threat of unpaid bills. But in the event of trouble, use a high-quality collection agency based in the United States to act quickly and forcefully. Here again, the best solution is to have the general sales conditions and commercial contracts be as bullet-proof as possible, i.e. be drafted with the assistance of specialised lawyers.

What do you think of the French support system for SME exporters?

PHT: In France, we have a remarkable and efficient system of support and subsidies. This system has also made significant strides and become more professional in the past 10 years. It is probably one of the most comprehensive in all of Europe. It is one of the paradoxes of our country, which favours redistributing profits over lowering taxes. The lack of equity held by SMEs is offset by the subsidies and grants available to them. Thus, before you venture abroad, contact the economic departments of your regional or departmental council, your chamber of commerce, the local Coface office, Ubifrance, Oséo or the French Foreign Trade Advisors. It may appear that understanding how these agencies function and taking the time to meet the people there and fill out all the forms is time-consuming. But in the end it will help you save time and undoubtedly enable you to take advantage of needed subsidies that can help you reduce your risk. Go to the meetings that they sponsor in your area. That will also allow you to meet people from other SMEs and understand the reasons for their success and causes of their failures. Export subsidies involve a wide range of fields: management recruiting, customer development tax credit, equipment and intangible investment financing, WCR, receivables protection, export diagnostic, etc. Take advantage of them! In fact, the French Foreign Trade Advisors (CCE), UBI France and Chambers of Commerce and Industry are organising the third North American springboard in February 2012 to enable 100 French SMEs to gain a foothold in the United States or develop their business activities there (www.cnccef.org).

In two words, what are the key principles to remember when

PHT: Two words: “caution” and “ambition”, in no particular order. You need both to succeed in this huge country. Do your homework and don’t be naive. Your success depends on you, your energy, perseverance and the resources you set devote to succeeding in the United States. The cost of being unprepared and unprofessional is very steep. The opposite is also true. If you are well prepared, well informed, professional, well advised, ambitious and cautious, the United States is still the promised land.

Interview by
Trade Line

Clément Lescanne,
Head of Sales and Marketing, Ober

"Start with a French partner, such as a French VIE international intern"

How do you view the US market?

Clément Lescanne (CL): Winning market share in the United States is not easy, especially with the euro's rise against the dollar in recent years. For a company like Ober, which specialises in high-end decorative wood wall panels, having an original product line that also integrates sustainable development in a comprehensive fashion thanks to its continuous search for innovation, is one way to stand out from the competition. Another is to develop increasingly high-end products. For example, we had panels created by fashion designer Christian Lacroix. It is also very important to invest heavily in communications resources.

How did you enter the US market?

CL: We set up a representative office in New York in 2009, with an employee responsible for coordinating and developing our activity locally. She meets with architects to show them our collection, manages our distribution network and establishes industrial partnerships to outsource production. I am convinced that for an SME such as our company, this approach is the best, most cost-effective and easiest to manage. In fact we adopted the same approach successfully in Dubai and Seoul. All these office openings were made with the help of Coface's business development insurance. Later, we will undoubtedly open offices in other US cities where the architect community is well represented: Chicago, San Francisco and Miami.

Was Coface's business development insurance a useful product?

CL: Indeed, although not for the reasons typically put forth. I'll start by saying that business development insurance is only useful after a decision has been made, based on all available information, to enter a foreign market. Once this decision-making process was over, Coface enabled us to progress more quickly, thanks especially to the financial advance we received. It is a real boost and also offers the advantage of reassuring banks and making your project even more credible. In our case, the business development insurance advance enabled us to finance the start-up of the office and the advertising and promotional campaigns.

What advice would you give our readers planning to enter the North American market?

CL: Leaving aside the traditional rules of marketing and communications, in my experience it is better to have a French employee working in the United States, at least during the start-up phase (for example a VIE international intern). As I mentioned, we sent over a young woman with strong qualifications: the equivalent of a master's degree (French baccalaureate degree +5 years secondary education) and four years of work experience in Asia. In my opinion, that turned out to be less expensive and simpler than it would have been to hire an employee locally. Moreover, that move enabled us to avoid relying on lawyers, who have a tendency to complicate matters and slow things down. We'll see how it goes and whether our sales increase at a sufficient rate. At that point, it will undoubtedly be necessary to add to the staff with one or more American employees.

Interview by
Trade Line

Ober, an SME specialising in high-end, decorative wood panels

With the Oberflex and Marotte product lines, Ober offers decorative wood panels used to furnish stores, offices, hotels, conference and event rooms and to decorate individual homes. Our customers include mainly architects, designers, contractors and carpenters. The company currently has some 220 employees in France. In 2010 it generated sales of €41.7 million (+65% relative to 2009), of which 60% abroad.

Yves Zlotowski,
Chief Economist, Coface

With the exception of Japan and especially Vietnam, Asia is doing well

Back from Asia, where he participated in country risk conferences sponsored by Coface in late May in Hong Kong and Beijing, Yves Zlotowski believes that most Asian economies will record solid and balanced growth.

Overall, the Asian economies are performing well, says Coface's chief economist. Most will enjoy solid and balanced growth, which does not give rise to any specific concerns. However, hat is not entirely the case for Japan and Vietnam. As for China, says Yves Zlotowski, growth will remain promising, since any concerns are primarily microeconomic in nature, namely the growing role of that country's employee/consumers.

Japan: the crisis is expected to end in 2012

A broad consensus is emerging that Japan will experience three recessionary quarters, followed by a recovery in the fourth quarter of 2011 and largely positive growth in 2012, as the economy rebuilds from the vast damage caused by the earthquake early in the year. Ultimately, the impact of the Japanese catastrophe on Asian production chains appears to be limited. There will clearly be a slightly negative impact on Thailand's industry in the first quarter of 2011. However, Korean companies appear to have been able to take up the slack left by Japanese companies, which sparked the growth of high-value-added Korean exports.

Vietnam: investors remain reticent

The Vietnamese economy is the source of the greatest concern in Asia, with a substantial current deficit, limited currency reserves and successive devaluations of its currency, the dong. While the authorities have taken various measures to combat any overheating, the economists attending the Hong Kong conference expressed concern over the recent caution shown by foreign investors in early 2011. After all, foreign investment was a key driver of Vietnam's economic lift-off. A sudden landing of the Vietnamese economy is therefore a risk that bears watching.

China: changing times

China is yet another key area of concern. For the participants and economists at the Coface conferences in Hong Kong and Beijing, this country has reached a true turning point and fundamental changes have been under way since the end of the crisis.
China managed to steer its way through the crisis in remarkable fashion. It used the tools at its disposal skilfully and with determination: substantial credit growth, stabilisation of the yuan, policy of support for companies, and a major stimulus plan. The result is that 2010 will remain, at least to all outward appearances, a major success with 10% GDP growth.
2011 will undoubtedly be a more uphill battle. The country has taken up the struggle against inflation, a stated objective of both the national and local

“Wage and salary demands will represent the most spectacular change in China”

authorities. The devil will be in the details so as not to suffocate growth. Interest rates are rising, as is the exchange rate, even as access to credit is falling. Chinese growth is therefore expected to slow in 2011. The only question is whether this slowdown will be sudden, accompanied for example by a bursting of the property market bubble, or only gradual. This second assumption remains the most widely held.

But this forecast is based on the idea that the authorities still have control over the economic levers. While that is probably the most likely scenario, a few counter-examples are worth considering. To control the development of credit, the authorities successfully brought about a sharp slowdown in the official supply of bank credit. In response to this restrictive policy, however, shadow banking is showing signs of growth. Back-room banking units, which are proliferating outside of any control, lend money to companies unofficially and at occasionally usurious rates. To that must be added the growth in inter-company lending and debt issues. By its nature, inter-company credit creates a risk of fragility by way of a domino effect if a company’s insolvency spreads to customers and suppliers. This initial macro-economic analysis highlights weaknesses in the area of the effectiveness of economic policy-making, but not of any long-term fundamental concerns.

At the micro-economic level, the credit risk exposure of companies is tending to rise. The Chinese government’s commitment to put a halt to the overcapacity of its companies is real. The country’s production capacity needs to be streamlined, especially since the goal is to shift production toward higher-end products. The authorities would also like to reduce the relative share of investment in the country’s GDP in favour of household consumption. Moreover, companies no longer enjoy the tax incentives implemented during the crisis or easy access to credit. Other challenges include a rising currency following an extended period of nearly fixed parity, higher commodity prices and rising inflation.

But the most spectacular change will come from wage and salary demands. They have been a topic of conversation for years, but they are now real. One year ago, the wave of suicides at Foxconn and the strikes at Honda were broadly publicised by the Chinese media. The notion that value-added now needs to be shared with employees is gaining weight. Wage and salary demands are front and centre.

The annual rate of wage and salary increases, around 10%, was interrupted during the crisis before returning with a vengeance, averaging more than 20% in 2010. That is a priority for the Chinese authorities, since the increase in household income is the key instrument that will enable the dynamic growth in household consumption, one of the major economic policy goals for the years ahead.

Meanwhile, labour market reforms are being implemented: wage negotiations institutionalised within companies, strengthened employee representation on boards of directors, formalisation of employment agreements, etc. The road is long, but the process of a growing role for the Chinese employee/consumer has begun. This trend is essential for the sustainability of Chinese growth. But in the short term it means that companies will need to experience disruptions and that as a result the credit risk is greater.

For many years, the growth model was premised on an abundant supply of cheap and malleable labour. However, the commitment of the well-documented “migrant workers” who agreed to travel far from their home villages is starting to crumble. The “single child” policy has led to a surfeit of individualism. The working age population will begin to decline in 2015. The Chinese worker is now increasingly looking out for himself and is less willing to make substantial sacrifices for the community.

Overall, the Chinese market remains extremely promising, with a growth model that is undergoing fundamental changes, but the market should be approached with caution and a complete understanding of the facts, as this transition may be fatal for some non-viable companies even if it benefits the country’s economy as a whole. These labour-intensive companies were highly favoured in the growth model that reigned up until now but are less welcome in the new model that is emerging, which is not kind to overinvestment.

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