

Construction industry: Euler Hermes Germany insures against disputed claims, theft, and contractual penalties

HAMBURG – 15 JUNE 2016 – The new construction sector policy of Euler Hermes Germany provides comprehensive cover against risks that are common in the sector. It protects construction companies against liquidity bottlenecks caused by disputed claims for example. These are an almost daily occurrence in the sector: instalments or final invoices go unpaid due to objections, which can create major financial problems for companies. This customized insurance also covers many other typical construction sector risks: theft from building sites by employees, contractual penalties for non-compliance with agreed completion dates, as a result of sabotage for example. Insurance cover can include all kinds of surety and guarantee components, e.g. deposit and contract performance guarantees and defect warranties.

No money for a job for up to 3 years: negotiations over disputed claims drag on

"Disputed claims cause many construction companies major liquidity problems," says Jonas Müller, head of Product Development at Euler Hermes Germany. "A builder has completed the construction or construction phase and paid substantial costs in advance. The client refuses to pay because of an objection and disputes the invoice – often over some minor detail. It can take as long as two to three years to reach an agreement. The bigger the construction project, the bigger the resulting liquidity bottleneck. The low margins in the industry exacerbate the problem even further; the money has been reallocated long ago and is needed urgently. During negotiations many construction companies are under so much pressure to reach an agreement that they sometimes waive up to 50% of their invoice even in the case of really minor objections. By taking out a sector policy, the company receives the money from us as insurer immediately and can therefore go into negotiations with no liquidity bottleneck or pressure".

Euler Hermes does not require an expert report on the likelihood of a claim being successfully disputed. The sole condition is that the company subsequently provides clarification and initiates the necessary steps.

Theft from the site: When all the roof tiles have suddenly disappeared, a contractual penalty will not be far away

A wide range of modular components in the sector policy can also cover contractual penalties, e.g. for non-compliance with agreed completion dates, or theft from the building site by employees.

"If all the roof tiles disappear overnight, or half the wood for the roof timbers, it can come as a nasty shock," says Müller. "The material has normally been paid for long since and thus both money and material have gone. Thefts like these can also delay completion. Contractual penalties are then commonly applied, making yet another dent in the construction company's finances."

Where delays have been willfully caused by employees, by sabotage for example, the sector policy covers the resulting contractual penalty.

Warranty claims for defects & performance guarantees: Where would the construction industry be without bonds and guarantees?

Euler Hermes has been a leading provider of guarantees and warranties for many years, particularly for construction projects. Accordingly all the necessary guarantees and bonds are available for sector policies. A deposit of around 10%-30% is usually due before construction begins – this is covered by a deposit guarantee (contract performance security) and normally following by a warranty guarantee (contract warranty security).

"These guarantees ease the pressure on the construction company's credit line at the bank and ensure greater independence," explains Müller. "The company can also significantly improve its liquidity and possibly make interest gains by redeeming cash collateral. When a construction project has been completed, the client generally retains 5%-10% of the amount until final acceptance. By providing a guarantee as security, it can immediately access the money for future building projects. Another advantage is the considerable financial strength of Euler Hermes as guarantor – only a few financial institutions have equally good ratings and therefore such a high level of security."



Mixed outlook for German construction sector: high level of bankruptcies, but slight decrease

The outlook in the German construction sector is mixed. The boom years are over and confidence was down in 2015 despite stable returns and slight growth of 2% in gross production. However, a rise of 3% and thus a slight improvement in 2016 is expected, which is already reflected in corporate confidence at the start of the year.

Euler Hermes believes that public housing construction is the main brake on stronger growth in the industry, whereas private housing construction is growing steadily, causing the gap to widen further. Insolvencies in the sector fell by around 3% in 2015, although overall the construction sector recorded the second highest number of insolvencies nationally.

"This trend is set to continue in 2016," says Ludovic Subran, chief economist at Euler Hermes. "We expect a further slight fall of around 2% in the number of insolvencies in Germany, but levels will remain high, with around 3,800 cases and approximately 16% of all local corporate bankruptcies."

Property prices are another risk factor. Purchasing power cannot keep pace with steeply rising prices. German construction companies are in a better position than their European counterparts however. In France, for example, the construction sector is expected to account for around a quarter of all corporate insolvencies.

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