Performance

Chief Executive's report

As the world's oldest export credit agency, UKEF has a track record of providing world-class support for UK businesses, leading the way in the field of export credits for the last 100 years. As we enter our second century, we have lost none of our ability to innovate in fulfilling our mission to ensure that no viable UK export fails for lack of finance or insurance from the private sector.

Louis Taylor
Chief Executive Officer

Our focus in this, the final year of our 2017-20 Business Plan, has continued to be on delivering for all our customers. UKEF is helping to level up the UK, from the Belfast firm selling street furniture for the Dubai Arena, to the printing company in Runcorn selling secure high school certificates to the Kenyan National Examination Council, or the start-up from Aberdeen selling mobile mapping technology in the Asia-Pacific region.

We are proud of the fact that 77% of the companies that we directly supported this year were SMEs from across the country, and we are continuing to deliver new products and processes to make our support even easier for them to access.

At the UK Trade and Export Finance Forum (UKTEF) in June 2019, we launched our Small Deals Initiative and General Export Facility. Designed to make our support more flexible and competitive, these innovations will put SMEs in a better position to win business internationally.

We also announced changes to our foreign content policy, that enabled our support for Solarcentury, a renewable energy company based in London, by allowing UKEF to recognise the significant development and design expertise in the solar energy sector in the UK. We provided Solarcentury with nearly £50 million in financing to build 2 of the largest solar plants in Spain. Together, these plants will power over 250,000 homes every year.

Our support for the clean energy sector has been enhanced by UKEF's 'Leading with Finance' initiative, which identifies overseas projects that could benefit from UK expertise. Leading with Finance combines co-ordinated international engagement with marketing and business development to match overseas demand to UK supply chains. This has helped secure additional opportunities for UK exporters to win contracts in renewable energy projects.

Together with our support for the Formosa 2, Changfang and Xidao offshore wind farms in Taiwan, and for solar-powered rural healthcare clinics in Zambia, these transactions demonstrate UKEF's commitment to developing the depth and breadth of our support for clean energy.

Our offer for UK exporters in those sectors was further strengthened in the 2020 spring Budget. The Chancellor of the Exchequer announced a package of improvements to our offering that included two new tranches of recyclable direct lending, with £2 billion allocated to clean growth projects and £1 billion to UK defence and security goods and services. Now that the boost to the facility announced in the Autumn 2018 Budget has also been made permanent, our Direct Lending Facility, recognised as a 'gamechanger' by the British Exporters Association, has had its capacity significantly increased to £8 billion.

The Chancellor also announced half a million pounds to strengthen UKEF's export finance manager (EFM) network in the north of England and Scotland. These new positions will focus on companies that supply to clean growth industries, with targeted marketing activity to support them as they transition away from older technologies to cleaner new ones.

We are also working to implement the recommendations of the Task Force on Climate-related Finance Disclosures (TCFD), as we committed to doing in the Government's Green Finance Strategy published in July 2019. Further detail on TCFD can be found on page 98 and you can also see further details of our response to the parliamentary Environmental Audit Committee's inquiry into UKEF on pages 101 to 102.

UKEF has supported a number of transformational infrastructure projects this year, particularly in sub-Saharan Africa. In Ghana, we provided £110 million in financing for a new maternity hospital that will help reduce infant mortality rates in the Ashanti region, while support worth £40 million will see 83 kilometres of road upgraded in Gabon, benefiting an estimated 1 million people in the Libreville region.

Improved health, energy and transport infrastructure are crucial in helping nations out of poverty as recognised by the UN through the Sustainable Development Goals (SDGs). Through the projects we support, UKEF helps developing countries to close the infrastructure financing gap and achieve greater prosperity, while providing exporting opportunities for UK companies.

Our 2017-20 Business Plan also set out an accelerated path for UKEF to scale up our operations, deliver a higher quality of service for our customers and increase employee engagement. Over its course, we provided £14 billion of support for UK exports, while recording our highest ever levels of staff engagement.

Our success has also been recognised more widely, with UKEF named as Global Trade Review's best export credit agency (ECA) for the last 3 years in a row, and the British Exporters Association (BExA) scoring us 9/10 for our product offering every year since 2014.

UKEF's response to the COVID-19 pandemic has demonstrated the strength and versatility of our product suite, as well as our adaptability as a department. To meet the challenges of this pandemic, we are actively working with HM Treasury to ensure that our support for business continues during this period and position UKEF to be best placed to support UK exporters as the economy recovers.

As stated earlier, 2019 was our centenary year, marking 100 years of innovation and success in support of UK exporters. Our centenary has had a lasting impact, as UKEF staff raised nearly £20,000 for charity over the course of a number of internal events and sporting feats this year.

Business supported

In 2019-20, UKEF provided 135 applicants with finance and insurance and referred a further 62 exporters to a private sector provider; in addition, a further 140 UK companies secured business supplying goods and/or services to a project UKEF is supporting and 2 from direct support and private market assists.

The maximum liability on all new business was £4,423 million. Our short-term trade finance products represented 16% of this total. UKEF earned net premium in the year of £177 million.

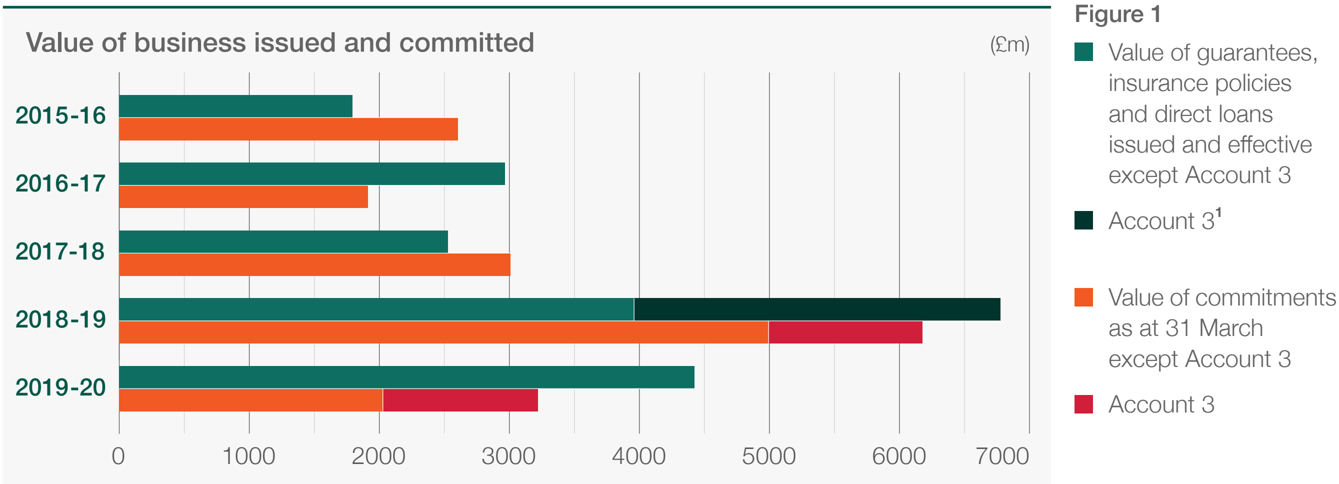


Figure 1

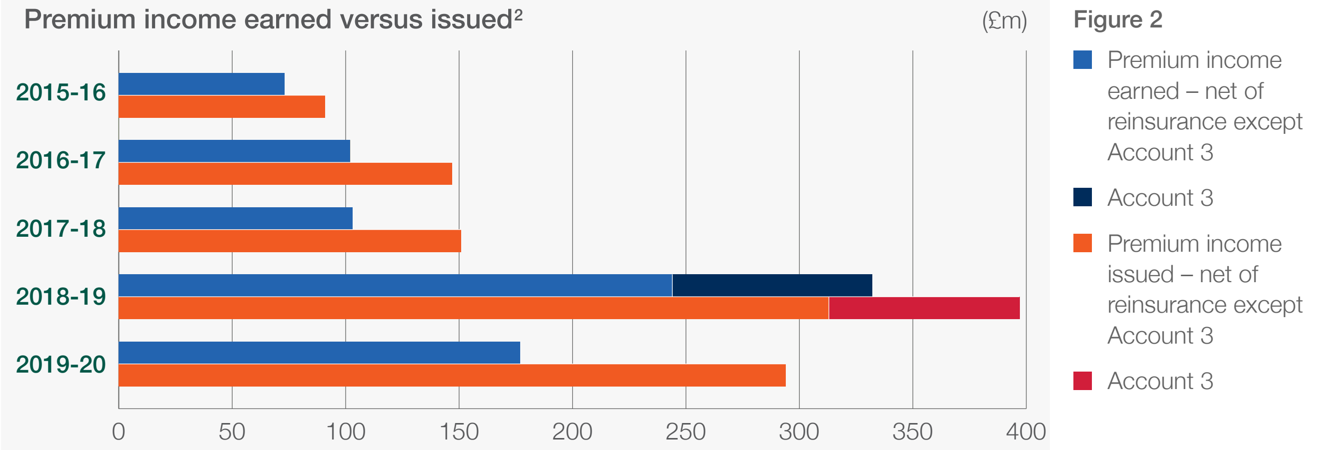
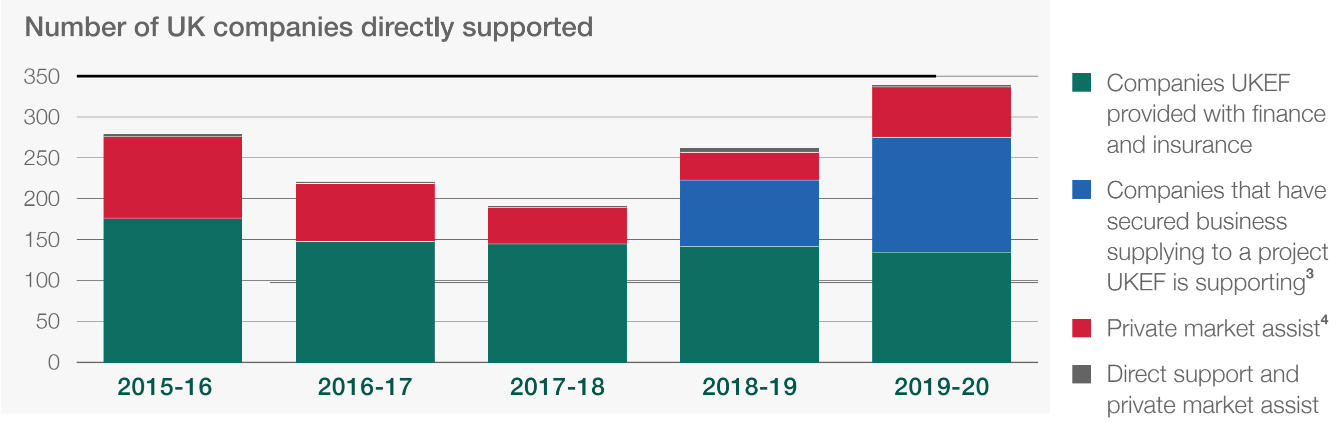
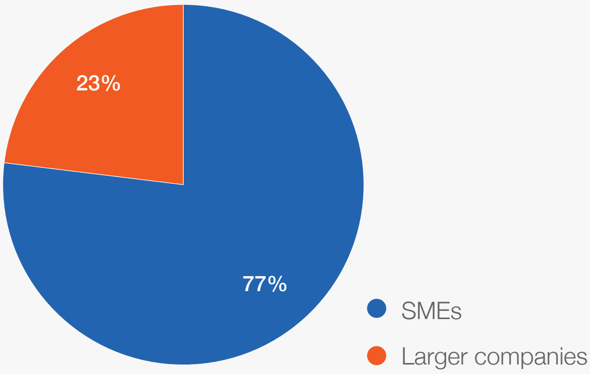


Figure 2

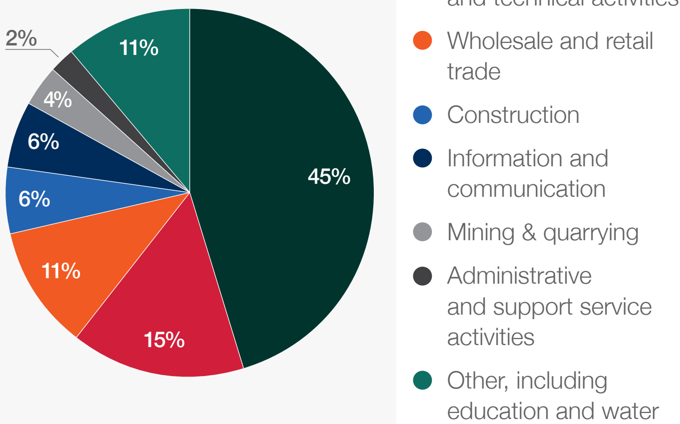


1 For more on what Account 3 is, see page 89.
2 Premium income earned differs from premium income issued because it:
- does not include premium from direct lending, which is amortised as interest income.
- uses an exchange rate fixed at the time premium is received (rather than month-end rates).
- Premium Income earned is based on Accounting Standards (see note 1 of the Financial statements for further details).

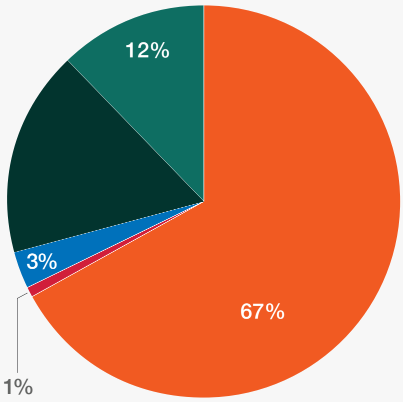
Companies supported by size[5]



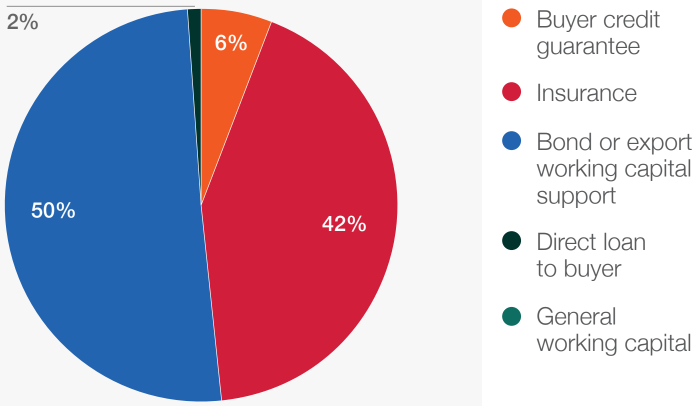
Companies supported by sector[5]



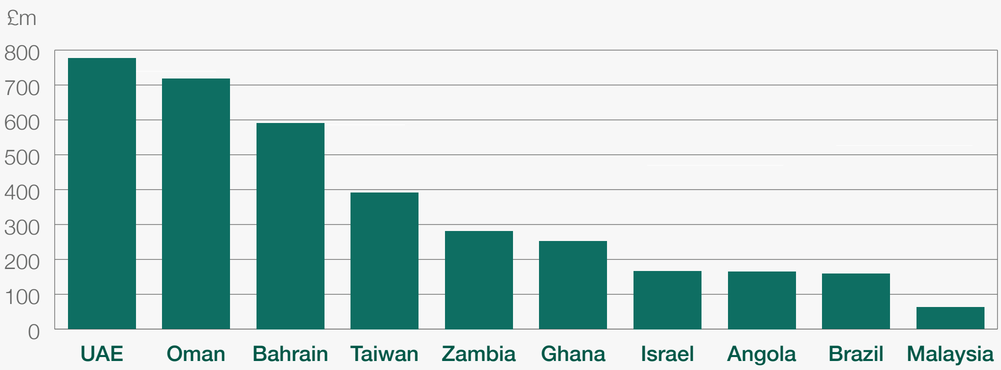
Product use by our maximum liability



Product use by number of facilities



Top 10 destination of exports supported in 2019-20



3 This data was not measured before 2018-19 and therefore cannot be reported.
4 A private market assist is when our engagement has had a material contribution to a company receiving support from the private sector, resulting in an export contract going ahead that was unlikely to have proceeded otherwise.
5 Based on the number of companies UKEF directly supported with finance or insurance.

Our response to the COVID-19 pandemic

The economic impact of the COVID-19 pandemic within this report was limited in the 2019-20 financial year, but it is important to outline how we have been responding to this health and economic crisis, and how we have prepared for the coming financial year, which will be very different.

UKEF's existing range of tried and tested products has been, and will be, vital in supporting UK exports. This includes products such as our Export Working Capital Scheme, which eases cash flow constraints for exporting businesses.

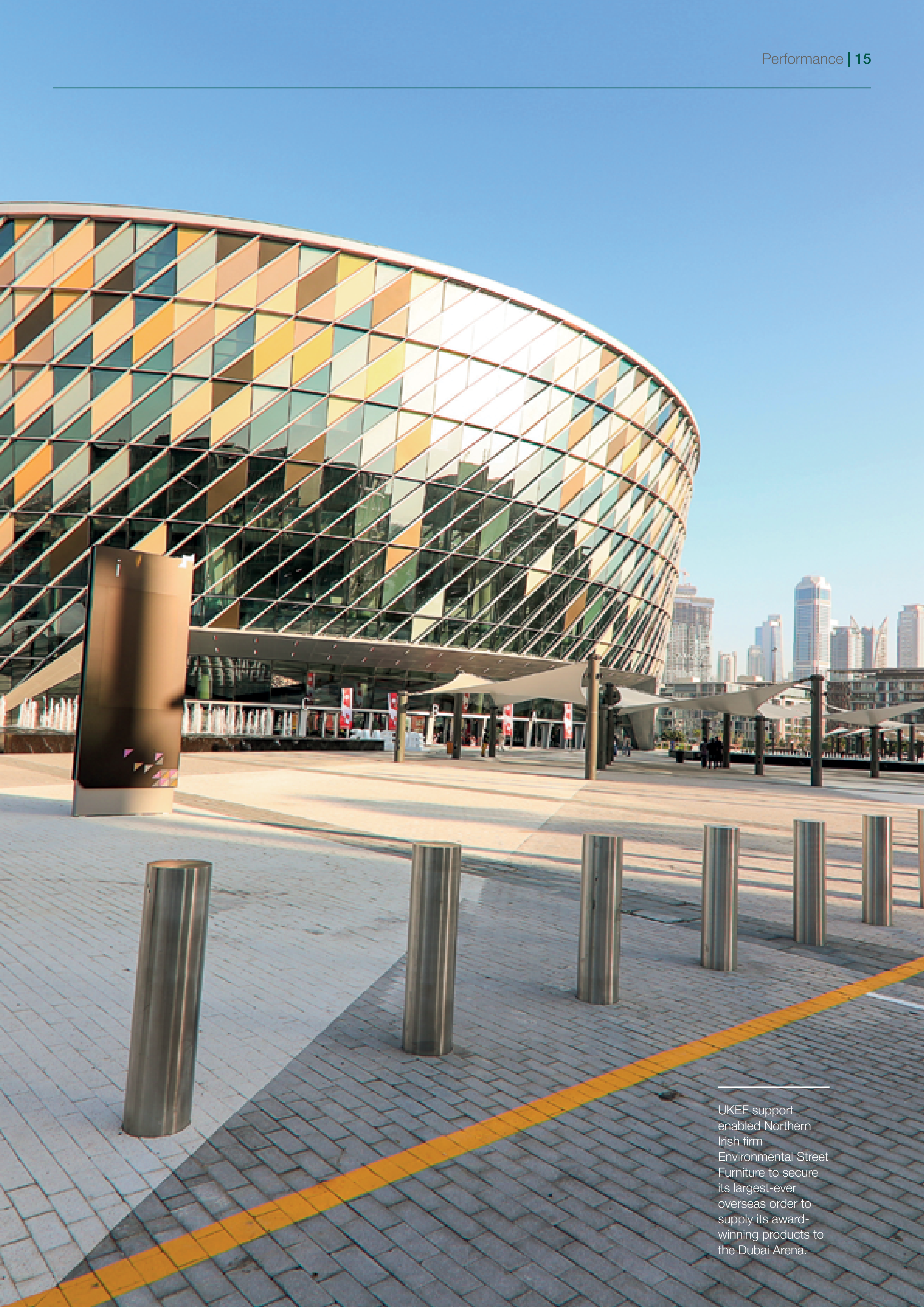
To meet the challenges of this pandemic, we are actively working with HM Treasury and taking a pragmatic approach to supporting businesses during this period. This will allow us to continue to provide finance to customers that we would have supported before the outbreak of COVID-19, even taking account of the commercial impact of the virus on their business prospects. In addition, we are able to protect our customers from financial loss from the pandemic when claims are made on insurance policies or guarantees provided to banks.

We have also accelerated the imminent launch of our General Export Facility and development of the Export Development Guarantee. These products provide a guarantee of up to 80% to support bank loans for general working capital or capital expenditure for UK exporters and is not tied to a specific exporting contract. First used in 2019 to support Jaguar Land Rover, we will be rolling these products out more widely and anticipate they will be extremely popular with businesses whose exports have been affected by the pandemic and require support.

In addition, the scope of our Export Insurance Policy has been extended to include transactions with the EU, Australia, Canada, Iceland, Japan, New Zealand, Norway, Switzerland and the USA so that cover is available in 180 countries in total. Our recently boosted direct lending scheme is also vital in supporting overseas buyers looking to procure from the UK, allowing UKEF to offer support where private sector liquidity is poor.

UKEF has an active role to play both during the pandemic and as we move to the recovery phase. We will continue to innovate and adapt as needed to enable UK exporters to survive and thrive through this challenging time.

You can find more on the potential effects of the pandemic on the UK and global economy in the Economic Snapshot starting on page 32.



UKEF support enabled Northern Irish firm Environmental Street Furniture to secure its largest-ever overseas order to supply its award-winning products to the Dubai Arena.

Measuring our success

The volume of business that UKEF supports year-on-year is a reflection of private sector liquidity and risk appetite, as much as of our activity and success. We complement rather than compete with private sector finance and insurance providers. If support is available from a commercial bank or insurer, we do not seek to displace this. In many cases, we will work with companies and financial service providers to find a solution from the commercial sector (which we report as a 'private market assist').

Our interventions:

- fill market gaps
- provide additional export value for the UK economy
- support growth in overseas markets for the individual companies that benefit, as well as their supply chains

Our support is provided on the following terms (see pages 58 to 85 for more detail):

- we charge a premium to reflect the risk we assume
- commercial rates of interest are charged on the lending we support, at a rate reflecting UK government risk
- the premium we charge must cover our anticipated long-term losses and operating costs
- we aim to operate at no net cost to the taxpayer over business cycles

We have reviewed our performance against the key deliverables set out in our 2017-20 Business Plan, which support our strategic aims:

- **Agile and adaptable:** to be an agile department, able to address the challenges facing UK exporters throughout the economic cycle.
- **Competitive offering:** to be active in ensuring that we are one of the most competitive export credit agencies in the world.
- **Customer service and awareness:** to provide a high-quality service to our customers that is responsive, flexible and efficient with a focus on solutions and innovation.
- **Great place to work:** to be a great place to work, where teams collaborate across functions easily and towards common goals.

Our new Business Plan for 2020-24

As we enter our second century as the UK's export credit agency, it is important to ensure that we have the ambition, resources and strategy to help exporters continue to succeed.

Our last Business Plan for 2017-20 set out an accelerated path for developing the department that saw us scale up our business and operations - all while delivering a higher quality of service, sealing landmark transactions and having a highly engaged workforce. You can find more on how we delivered against this plan on page 18.

The new plan builds on our past experience and successes, so we can remain a world-class export credit agency and help support the government's ambitions for UK exports.

In this plan, we have 4 delivery objectives, which set out what we need to achieve to realise our mission, and 3 organisational objectives, which define the resources, skills and operational capabilities we will need to do that. These are:

Delivery objectives

1. Provide export finance, insurance and guidance to help UK companies sell overseas, supporting the delivery of the government's Export Strategy
2. Continuously adapt and focus our activity on sectors and countries where UKEF support will have the greatest economic benefit for exporters and suppliers of all sizes and across all of the UK
3. Improve awareness and understanding among UK companies, international buyers, prime contractors, sponsors, banks and insurers about export finance and insurance support available from UKEF and the private sector
4. Ensure we retain the confidence of our ministers by rigorously managing risk, improving efficiency and operating within the consent of HM Treasury

Organisational objectives

1. Be a great place to work, engaging and developing our staff to deliver better for our customers, in line with the vision for a "Brilliant Civil Service"
2. Be a customer-centric organisation, delivering high-quality services to the businesses and organisations we support
3. Be agile and adaptable, responding to emerging economic developments and market gaps

You can find out more about how we will achieve each of these objectives in our Business Plan, which will be available online.

Our plan for 2020-21 to achieve against these new objectives can be found on pages 27 to 28.

How we performed against our Business Plan commitments for 2017-20

We said we would…	What we did…
Be a more scalable organisation, able to support higher volumes of business efficiently and effectively, in particular on the short-term trade finance side	Implemented our innovative new bank partnership and digital trade finance service to deliver more efficiently to SMEs
Be a more customer-centric organisation, offering improved response times, quicker decision-taking and improved case-processing	Enhanced our digital service to make UKEF more accessible and user-friendly for our customers
Make meaningful contact with more exporters and other stakeholders, resulting in increased numbers of exporters accessing support	Deployed our "Exporters' Edge" GREAT marketing campaign, generating over 10,000 new responses (exceeding our target by over 20%), and introduced a programme of supplier fairs to help UK companies access the supply chain of projects UKEF supports
Use digital as a primary means for managing relationships with a wider range of stakeholders	Established a web presence for our international customers and continued to develop our digital offer for UK businesses
Be smarter in our decision-taking, using data and market intelligence to guide our interventions	Improved our data management and business analytics so that we can embed insight and analysis across our business, enabling us to make better informed and evidenced decisions
Be a great place to work, with all staff engaged in delivering our mission and clear about the value of their contribution	Scored our three highest engagement scores to date in the Civil Service People Survey; we have also made significant strides forward in improving our operating model, staff development and diversity
Collaborate generously with colleagues in the Department for International Trade, other government departments and other partners, combining our efforts to maximise the benefit to exporters	UKEF is at the heart of the Government's Export Strategy, collaborating generously with other parts of government to provide a joined-up offering to exporters
Continue to be disciplined in our use of resources, and in risk management, in order to operate within the terms of our Spending Review 2015 settlement and Treasury consent, and at no net cost to the taxpayer	Continued to meet our financial objectives set out in the Spending Review 2015 operate at no net cost to the taxpayer; in 2018–19 alone, we generated £332 million in premium income

Our achievements in 2019-20

Agile and adaptable:

Appropriately embed compliance and risk management in all the business we do	Implemented and ongoing (see page 103)
Develop a target operating model to drive and inform UKEF's transformation plan	Implemented and ongoing (see page 57)
Continue to develop our digital services, data and technology to improve customer experience, increase efficiency and support robust decision-making	Implemented and ongoing (see page 57)

Competitive offering:

Develop and deliver a product strategy in support of UK exports while protecting taxpayers' interests	Implemented and ongoing (see pages 48 to 49)
Introduce the General Export Facility, consult the public on our foreign content policy and roll out new and enhanced products including supplier credit and supply chain invoice discounting	Mostly implemented and ongoing (see pages 48 to 49)

Customer service and awareness:

Deploy a marketing campaign with the aim of generating 5,000 new customer responses from UK businesses and an increase in awareness of UKEF among potential UK and overseas customers	Implemented (see page 23)
Continue to roll out our supplier fair programme more widely to maximise the benefits of UKEF support for the UK supply chain	Implemented and ongoing (see page 23)
Further expand our international network of export finance specialists	Implemented and ongoing (see page 23)

Great place to work:

Reduce staff turnover and increase employee engagement to maintain a workforce with the right skills, knowledge and ability	Partially implemented and ongoing (see pages 132 to 134)
Maintain our efforts to diversify our workforce by meeting the Public Sector Apprenticeship target, and by continuing to reduce the gender pay gap and ensuring that 30% of SCS roles are filled by female staff, meeting the commitments we made under the HM Treasury Women in Finance Charter	Implemented and ongoing (see page 135)

'If small businesses were to export more, Britain would see even stronger economic growth. For 100 years UKEF has been enabling companies from across the UK to expand their global reach by helping them succeed abroad. That's why it is at the heart of my plan to get businesses ready to trade.'

Rt Hon Liz Truss MP, Secretary of State for International Trade and President of the Board of Trade

'Having a best-in-class ECA, with over 100 years of experience in supporting UK exporters is an incredible advantage for our country, and we can see the benefits in the admirable results that UKEF achieved this year.'

Graham Stuart MP, Minister for Exports

Trade Secretary Liz Truss addressing UKEF and DIT staff

Finances

UKEF achieved a net operating income of £217 million for the year ended 31 March 2020 compared with £128 million for the year to 31 March 2019.

We met all of our financial objectives, which are set for us by HM Treasury. Page 31 sets out our results against our financial objectives and pages 88 to 93 provide a comprehensive report of our financial performance.

Supporting exports through the business cycle

Many of the loans we support by providing guarantees will be repaid over more than 10 years and, in the event of defaults, we will seek to make recoveries. This means that final business losses, as a result of unrecovered claims paid, can take many years to crystallise.

In this regard our role is best assessed 'through the business cycle', as our business levels and claims rise and fall depending on the impact of market disruptions on UK trade. For example, claims payments and recoveries reported in any single year actually reflect business written over a longer period of time.

Overall, this year, our performance in managing financial risk remained strong. But it is our management of risk through business cycles that is most important. See pages 58 to 85 for a more detailed commentary on how we have managed financial risk.

Performance assessment

An assessment of our performance should take into account:

- the overall volume of our support (as reported on page 30)
- our ability to cover our operating costs and credit losses while providing this support
- the potential demand for our services, as required to complement but not compete with the private sector

Bridging the gap

Our potential market share is partially determined by external factors over which UKEF has no control:

- the regulatory and economic environment and the demand for finance and insurance to support UK exports
- the ability of commercial credit insurers and finance providers to meet the market's demand for finance and insurance

It is also partially determined by factors over which UKEF has a degree of control:

- awareness among exporters of UKEF's ability to help and the willingness of our commercial partners (for example, banks and brokers) to use and promote our services
- our pricing of risk, reflected in the premium and/or interest we charge
- whether we have the product range required to fill particular market gaps

Thanks to UKEF support, power transformers built by BRUSH Transformers and General Electric will be used to modernise Angola's national power grid.

Awareness

In the UK, our ‘Exporters’ Edge’ GREAT campaign continued to engage our target audience of small to medium exporters through PR, online advertising, social media, events, partnerships, direct marketing and re-marketing. We improved our targeting to increase awareness and understanding of UKEF’s offer, and generated over 5,439 new responses from UK businesses against a target of 5,000.

In early 2020-21 we will conduct a further market survey to measure awareness among UKEF’s target audience, against a baseline of 20% awareness in 2016, which had risen to 26% by March 2019. We hope to increase this further as we continue our campaign in 2020-21.

UKEF held 6 Supplier Fairs in 2019-20, introducing 558 UK suppliers to procurement teams for international projects, the most in a single year since our supplier fairs started in 2017. UKEF has participated in 167 other domestic events, engaging directly with UK SMEs to increase awareness and understanding of our offering.

In target markets overseas, we engaged high-value buyers with the potential to source significant volumes of new supplies from the UK to make them aware of UKEF’s capacity to support UK supply chains. To make these connections, we participated in 24 international events.

UKEF’s network of international export finance executives in Brazil, Dubai, Indonesia, Ghana, Turkey, India and Mexico led engagement with local buyers, project sponsors and associated stakeholder networks in post to develop UK export growth in these markets and surrounding regions with the offer of UKEF-supported finance, and we continue to recruit in other regions.

Getting our support to the right companies, at the right time, will remain a significant focus, particularly for our trade finance products. In 2020-21, we will continue to work closely with commercial partners to increase the volume of business introduced to UKEF by banks, insurance brokers and other private sector and government networks.

There is a review of our work with partners on pages 54 to 57.

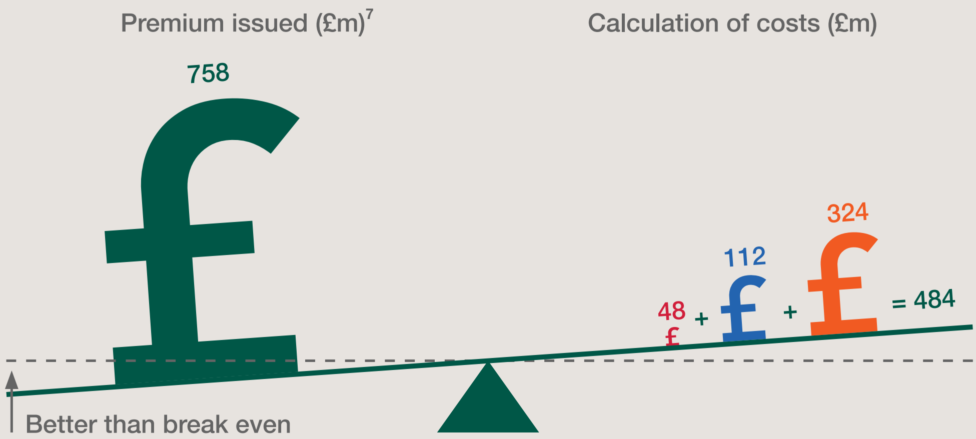
Pricing of risk

We support UK exporter competitiveness through charging only the lowest premium rates permissible, subject to meeting our financial objectives and aligning with our international obligations, most notably the minimum rates set out by the OECD. Our pricing methodology is described in more detail on pages 72 to 75.

How we protect the taxpayer

We price risk to enable us to operate at no net cost to the taxpayer over time. Our aim is at least to break even over business cycles. To help make sure that we do, every month we calculate the premium we earn and weigh it up against an estimate of all the potential costs and losses for the business supported.

We measure this over different 3-year periods. The diagram below shows the result based on actual results for 2017-18 to 2019-20.



The total premium issued between 2017-20 exceeded our costs by £274 million.

The costs have 3 components:

- £ a statistical estimate of potential losses that cannot be recovered
- £ administration costs
- £ a further amount to allow for a portion of unexpected losses

This measure, called a pricing adequacy index, provides assurance that our pricing is sufficient to meet all of the potential costs of the business supported.

See page 73 for further details.

7 The premium accounted for 2017–2020 applied to our pricing adequacy index is the premium income issued for that period. See footnote on page 12 for more detail.

Product range

UKEF's broad product range, strong guarantee, flexible foreign content rules and innovative approach are all advantages for UK exporters. Feedback from trade bodies such as BExA, and trade press such as Global Trade Review and Trade Finance Global recognises these advantages. The strength of our guarantee in financial markets continues to be assured by our longstanding status as a ministerial government department with access to the Consolidated Fund.

In the 2020 Budget the Chancellor of the Exchequer announced that UKEF will be given more money to lend directly to overseas buyers of UK goods and services, particularly for clean growth projects. This takes the amount available under UKEF's Direct Lending Facility from £5 billion to £8 billion. To complement direct lending, UKEF will also amend its Buyer Credit guarantee to allow it to better support export finance provided on a fixed-rate basis by covering break-costs or make whole payments related to interest-rate swaps.

Comparing UKEF with other ECAs

We assess the strength of our support primarily through listening to our customers and comparing our capabilities against other leading ECAs from around the world. Every year we undertake a comparison exercise to review our offering against those of other ECAs.

We also benefit from external scrutiny provided by the ECA benchmarking report produced each year by BExA. Our product range has evolved considerably since BExA's first benchmarking report in 2010, when we scored 4 out of 10, compared to our leading score of 9 out of 10 for the last 5 years.

We continue to have our success recognised, with UK Export Finance named Best ECA by Global Trade Review for the third year in a row and Trade Finance Global for the second year in a row.

Louis Taylor speaking at the BExA Annual Lunch

Other performance factors

Risk management

Managing risk is at the heart of our business model. In addition to the management of credit risks, we face a variety of other risks (e.g. financial, operational, reputational, strategic and legal) from external and internal sources.

As an ECA, our credit risk portfolio will tend to be characterised by:

- a higher risk profile than commercial lenders or insurers
- a strong emerging market risk component
- long risk horizons
- occasional risk concentrations (sectoral and/or geographic)

In this context, the low volume of new claims in each of the past 5 years, when our financial exposure has averaged £19.3 billion, demonstrates a strong capability in managing credit risk. Although past performance is not a guarantee of the future, taking the last 5 years, the average claims paid as a proportion of the average amount at risk would be:

£1 for every £4031 at risk, or 0.02%

We typically seek to recover claims we have paid, so any final loss calculation may not become clear for many years until recovery action is concluded. A detailed explanation of how we manage our financial risks is on pages 58 to 85.

We are also committed to managing operational risk, which involves the possibility of error, oversight or control failure leading to financial loss (other than as a result of properly managed exposure to credit risk), or a failure properly to discharge our obligations.

To manage these risks, we are committed to maintaining a culture of awareness and openness, enabling risks to be recognised, evaluated and mitigated.

There is a detailed description of our approach to the strategic and operational risks facing our business and consequent mitigation measures in the governance statement on pages 108 to 123.

Operational efficiency and effectiveness

We have a continuing programme of investment in digital technology and services to improve the efficiency and scalability of our case processing and customer relationship management, and to be prepared for any increased uptake of our products and services.

The 2015 Spending Review (covering the period to the 2019-2020 financial year) committed us to cost savings of 15% by 2020, which we achieved. However, we were permitted to reinvest these savings to support measures which transform the business and drive efficiency.

These transformative measures included:

- Improving the reliability, scalability and capability of our IT systems, including the improved use of Management Information (MI), moving towards a ‘digital-by-default’ approach, and reducing operational risk

- A service redesign to improve product access for customers and processing by UKEF
- Organisation and workforce change, including a new operating model for the Business Group to achieve more efficient use of our talent across sectors and products, and the introduction of an enhanced business development function

Further detail on these changes is reported on page 57.

The year ahead

As we enter the first year of our new Business Plan for 2020-24, our aim remains focussed on delivering a high quality service for our customers and being a great place to work for our staff.

1. Provide export finance, insurance and guidance to help UK companies sell overseas, supporting delivery of the Government's Export Strategy

To achieve this, we will in 2020-21:

- Work with 'super-buyers' overseas, UK and non-UK prime contractors and 'multipliers' to enable increased opportunities for the UK supply chain to sell into overseas projects backed by UKEF financing
- Launch a new and improved supply chain product range and fully launch our General Export Facility and our Export Development Guarantee

2. Continuously adapt and focus our activity on sectors and countries where UKEF support will have the biggest benefit, helping UK exporters and suppliers win business

To achieve this, we will in 2020-21:

- Appoint up to 10 new international export finance executives in key priority markets and integrate them into our operational planning
- Collaborate with the Department for International Development on the Developing Market Infrastructure Programme
- Use our new tranche of direct lending to further build and develop our clean growth transaction pipeline

3. Improve awareness and understanding among UK companies, international buyers, prime contractors and sponsors, banks and insurers of export finance and insurance support available from UKEF and the private sector

To achieve this, we will in 2020-21:

- Use our marketing activities to generate customer responses and an increase in awareness of UKEF among potential customers
- Develop our web presence, including improved content and functionality for trade finance customers

4. Ensure we retain the confidence of our ministers by rigorously managing risk, improving efficiency and operating within the consent of HM Treasury

To achieve this, we will in 2020-21:

- Ensure governance, compliance and assurance remain in line with government best practice
- Prepare to make climate-related financial disclosures in line with the TCFD recommendations as soon as is practicable after the end of 2020-21
- Actively work with HM Treasury to ensure that we continue to give the best possible support for exporters affected by the COVID-19 pandemic

5. Be a great place to work, engaging and developing our staff to deliver better for our customers, in line with the vision for a "Brilliant Civil Service"

To achieve this, we will in 2020-21:

- Launch our new People Strategy and Employee Value Proposition
- Continue to evolve the way we work through launching the UKEF Smarter Working Programme and completing the refresh of the staff intranet
- Refresh our commitments under the HMT Women in Finance Charter and update the Diversity & Inclusion Plan and associated Wellbeing Plan

6. Be a customer-centric organisation, delivering high-quality services to the businesses and organisations we support

To achieve this, we will in 2020-21:

- Implement our Target Operating Model roadmap and transformation plan
- Scope and implement our customer feedback approach
- Agree benchmarks for our Digital Trade Finance Service and Customer Satisfaction Index

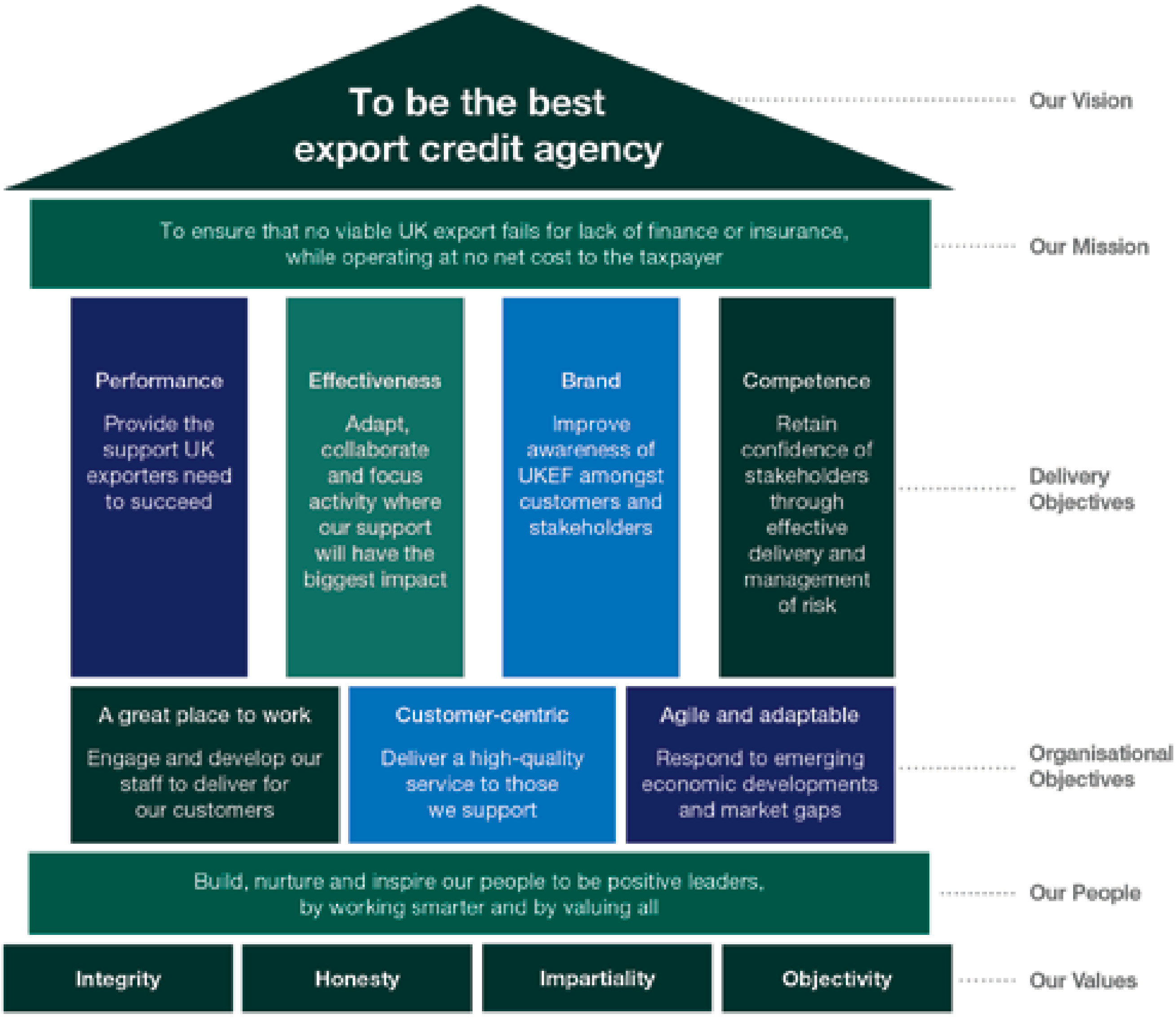
7. Be agile and adaptable, responding to emerging economic developments and market gaps

To achieve this, we will in 2020-21:

- Work closely with the Department for International Trade to develop the government's new Export Strategy
- Implement our Product Strategy and Product Review recommendations, including roll-out of a refreshed Export Insurance Policy
- Innovate and adapt as needed to help our customers during the COVID-19 pandemic and in the recovery phase

UKEF message house

UKEF's message house sets out the vision, mission, strategy and priorities of our Business Plan, as well as the spirit and values with which we will achieve these. It ensures clarity of purpose in all that we do, and creates alignment of departmental, divisional and personal objectives in order to deliver our priorities:



I believe that this report, and the performance reports that follow, are a fair, balanced and understandable account of UKEF's performance in the 2019-20 year.

Louis Taylor
Chief Executive and Accounting Officer
19 June 2020

Performance overview

Financial overview – 5-year summary

	2019-20 £m	2018-19 £m	2017-18 £m	2016-17 £m	2015-16 £m
Business supported	4,423	6,776	2,530	2,966	1,793
Premium income earned	177	332	103	102	73
Premium income issued	294	397	151	147	91
Claims paid	8	0	2	8	5
Net operating income	217	128	5[1]	149	106

Non-financial indicators – 5-year summary

	2019-20	2018-19	2017-18	2016-17	2015-16
Total exporters supported, of which:	339	262	191	221	279
direct support under a UKEF product	135	142	145	148	176
companies that have secured business with a project UKEF is supporting[2]	140	81	-	-	-
private market assist	62	34	45	71	100
direct support and private market assist	2	5	1	2	3
Facilities issued	604	733	580	483	593
Introductions to other sources of support	1,585	1,352	1,328	2,267	1,778

1 The fall in net operating income in 2017-18 was largely due to foreign exchange losses in that year. See page 63 for details of foreign exchange risk.

2 2018-19 was the first year UKEF has measured this.

Financial objectives

Objective and description	Results
Maximum commitment This measure places a cap on the maximum amount of nominal risk exposure (ie the total amount of taxpayers' money that may be put at risk by UKEF).	**Met** The highest recorded maximum exposure in the year was £31.7 billion, against a maximum permissible level of £50 billion.
Risk appetite limit This limit places a constraint on UKEF's appetite for risk at the 99.1 percentile of UKEF's estimated portfolio loss distribution.	**Met** UKEF's 99.1 percentile of the portfolio loss distribution did not exceed £2.1 billion against a maximum permissible level of £5 billion.
Reserve index This index ensures that UKEF has accumulated, over time, sufficient revenue to cover possible losses, to a 77.5% level of confidence.	**Met** The reserve index did not fall below 3.14 in the year, against a target minimum of 1.00.
Pricing adequacy index This index tests whether, over time, UKEF earns sufficient premium income to cover all its risk and operating costs. It is measured over 3 different periods:	
(i) past 2 years and present year.	**Met** This index at 31 March 2020 was 1.57, against a monthly minimum target of 1.00.
(ii) previous, present and next year.	**Met** This index did not fall below 1.54, against a monthly target minimum of 1.00.
(iii) present year and next 2 years.	**Met** This index did not fall below 1.55, against a monthly target minimum of 1.00.
Premium to risk ratio This measure ensures that each year UKEF charges enough premium to cover the cost of risk, together with a sufficient margin to contribute a material amount to administrative costs.	**Met** This ratio did not fall below 1.87, against a target minimum of 1.35.

Pages 58 to 85 set out more detail on these objectives.

Note: These financial objectives apply to business issued since 1991. There are no specific financial objectives in respect of outstanding exposures on business supported before 1991 other than to recover amounts due in respect of claims paid, in a manner that optimises the return to taxpayer, while taking account of the government's policy on debt forgiveness.

Economic snapshot

Richard Smith-Morgan
Deputy Chief Risk Officer

The Great Lockdown

After its initial outbreak in China, COVID-19 has now spread to almost every country around the world. The outbreak and response of national authorities, limiting movement and social interaction, has resulted in an unprecedented economic shock – the so-called 'Great Lockdown'. Both the supply and demand sides of the global economy have been affected, with 'sudden stops' resulting in production slowing, supply chain disruptions, labour force pressures, as well as a significant decrease in consumption. Global growth was already slowing in 2019 – at 2.9%, down from 3.6% in 2018 – and 2020 is set for a sharper contraction than the 2008 global financial crisis.[1]

The size of the impact on the global economy will in part depend on the length, severity and national responses to the outbreak. The ability for each country to limit the damage to their own economies will hinge on underlying structural factors, such as their exposure to commodity price volatility and reliance on external financing, as well as their ability to use judicious monetary and fiscal policy support.

For advanced economies with sufficient policy space, interest rates can be lowered, and fiscal policy expanded to help cushion the fall in demand. However, fiscal stimulus will result in sizeable increases in budget deficits and debt, with potential consequences for funding costs.

For emerging market economies with flexible exchange rate frameworks and manageable exposure to foreign currency-denominated debt, such as Brazil, India and Mexico, there is greater capacity to further ease monetary policy, while taking the opportunity to undertake fiscal and structural measures that help to enhance investor confidence. However, many emerging markets will suffer from under-resourced healthcare systems and tighter financing conditions, leaving them extremely vulnerable to the crisis. Consequently, external support, particularly multilateral, will play a key role in supporting developing economies through the crisis.

The economic outlook for 2020 has rapidly worsened as the virus spread around the globe. The IMF substantially revised down its projections for global economic growth in 2020, by over 6 percentage points, from 3.3% in January 2020 to -3.0% in April 2020.[2] While the three ratings agencies (Fitch, Moody's and S&P) also predict a contraction in the global economy of -2.4% to -4.6% in 2020.[3]

The IMF projects global growth of 5.8% in 2021 as economic activity rebounds from very low levels. This outlook is based on the assumptions that the pandemic fades in the second half of 2020, containment measures are scaled back and policy actions

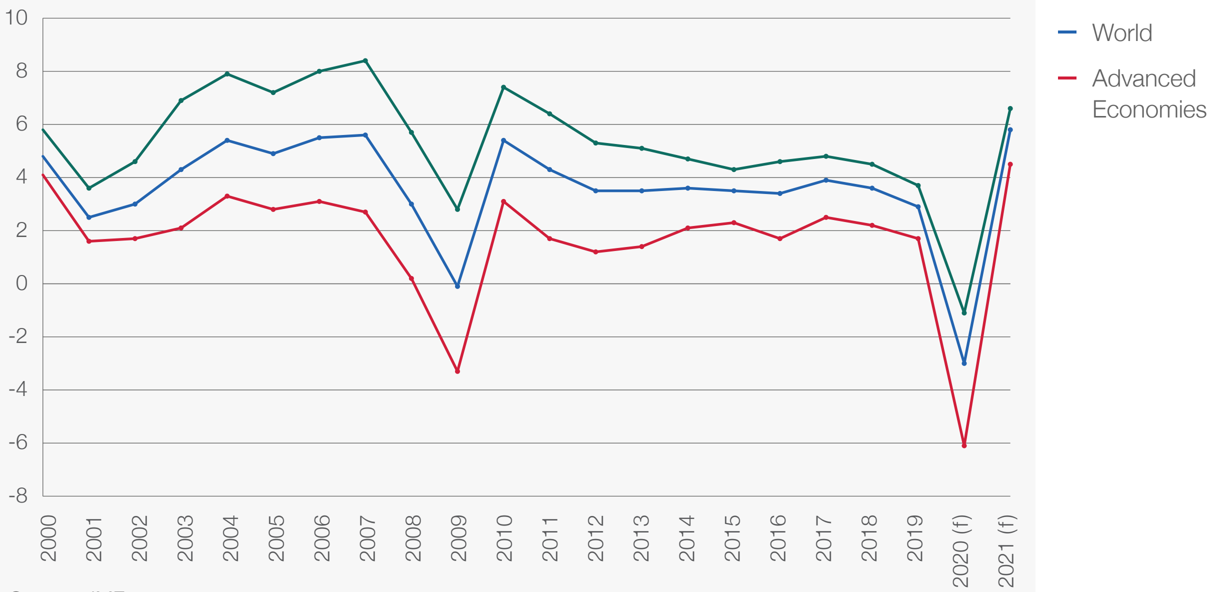
1 IMF World Economic Outlook, April 2020.
2 IMF World Economic Outlook, January 2020; IMF World Economic Outlook, April 2020.
3 Fitch, Global Economic Outlook: Crisis Update May 2020 (26 May 2020); Moody's, Global Macro Outlook 2020-21 (28 April 2020); S&P, COVID-19 Deals A Larger, Longer Hit To Global GDP (16 April 2020).

are effective in preventing bankruptcies, job losses and financial strains. However, this recovery is only partial – the level of global GDP in 2021 is expected to remain about 3% below its pre-COVID-19 forecast.

The near-term outlook is very uncertain. There have been a number of material revisions to global economic forecasts as the impact and duration of the COVID-19 outbreak have become more apparent. In particular, questions remain as to the shape and speed of the recovery. The IMF state that the risks to the outlook are on the downside and that worse growth outcomes are possible. The IMF has modelled alternative growth paths, including a scenario where the outbreak is longer than expected and the global economy contracts by around 6% in 2020 and rebounds by just under 4% in 2021. Under the most extreme scenario, of a longer outbreak in 2020 and a second wave in 2021, the global economy contracts by about 6% in 2020 and a further 2% in 2021. Under both these downside scenarios there is likely to be long-term damage to productive capacity – 'scarring' – as liquidity issues lead to insolvency for businesses and long-term unemployment rises. These effects may be greater in economies where there is limited fiscal space to provide support, and which may in turn worsen longer-term prospects for growth and government balance sheets.

Global economic growth rates

% change (year-on-year)

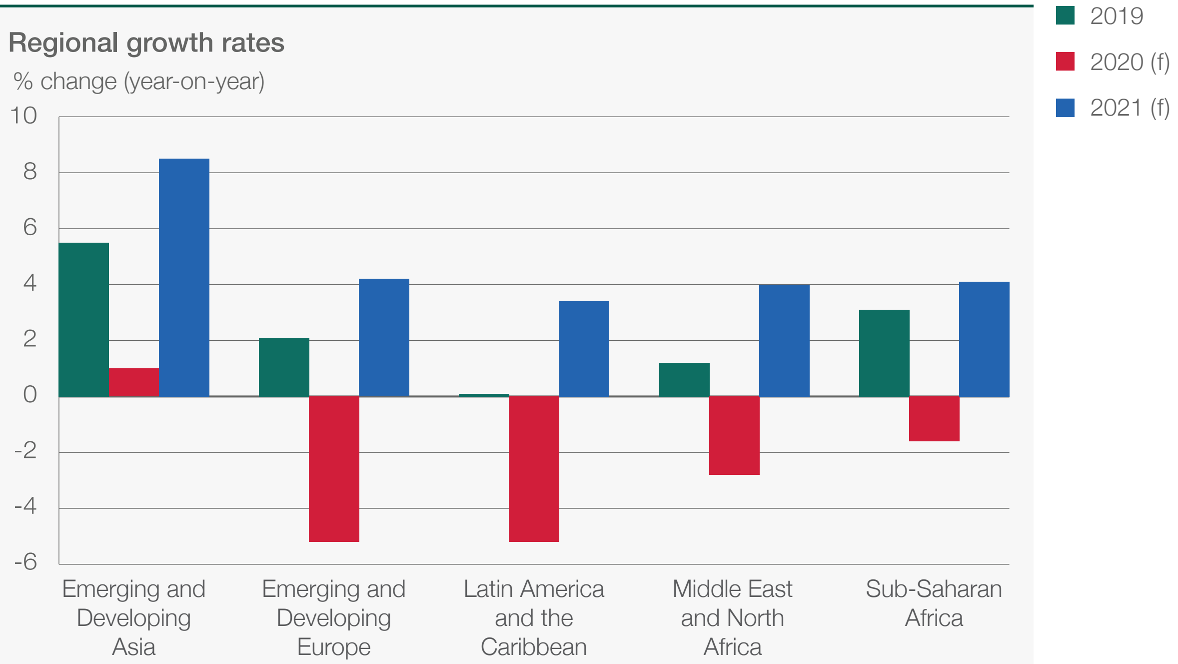


Source: IMF

The IMF forecasts that advanced economies will contract by 6.1% in 2020, compared to 1.7% growth in 2019. All advanced economies are expected to contract in 2020, with some of the biggest falls in Italy (-9.1%), Spain (-8.0%), France (-7.2%), Germany (-7.0%), US (-5.9%) and Japan (-5.2%). This is primarily due to the nationwide lockdowns that these countries have enacted to combat the spread of the virus. Growth in advanced economies is then projected to reach 4.5% in 2021, once lockdowns are removed, but most advanced economies are still likely to end 2021 with a lower GDP level than 2019. Moreover, the IMF note that adverse confidence effects may further weigh on economic prospects over the subsequent recovery.

Similarly, the IMF expects emerging and developing economies to contract by 1.0% in 2020, down from 3.7% growth in 2019. In addition to the public health crisis and reduction in domestic economic activity due to containment measures, many emerging and developing markets are experiencing a substantial fall in external demand, a pronounced tightening of financial conditions and a collapse in commodity prices. Growth is then forecast at 6.6% in 2021 for emerging and developing economies, but this is also subject to high levels of uncertainty. Despite the rebound in 2021, many developing economies will experience economic growth at a considerably lower rate than population growth, resulting in per capita income falling – with likely political consequences.

Emerging market and developing economies: Regional economic growth rates



Source: IMF

Emerging and Developing Asia is the only region forecast to grow in 2020, by 1.0%. However, this is around 6 percentage points below its average in the previous decade. Positive growth in the region is supported by China (1.2%), India (1.9%) and Vietnam (2.7%). The outlook for the region in 2021 depends to a large extent on the speed of the recovery in global economic activity, particularly in China which is forecast to grow by 9.2% in 2021.

Emerging and Developing Europe is forecast to contract by 5.2% in 2020, with Croatia and Montenegro facing the sharpest reductions in economic activity (both at -9.0%). Due to limited access to external financing and underdeveloped banking systems, most economies in the region will struggle to finance substantial increases in their fiscal deficits. Many non-EU emerging economies in Central and Eastern Europe have applied for emergency assistance through the IMF's rapid financial assistance facilities since the outbreak.

Latin America and the Caribbean GDP growth is projected to decline by 5.2% in 2020, with Mexico and Brazil forecast to contract by 6.6% and 5.3% respectively. Many economies in the region were already facing high financing costs, weak growth and increasing public debt levels before the emergence of COVID-19. These factors will all be exacerbated by tighter financing conditions in global markets and contribute to the weakest emerging market regional outlook through 2020/21.

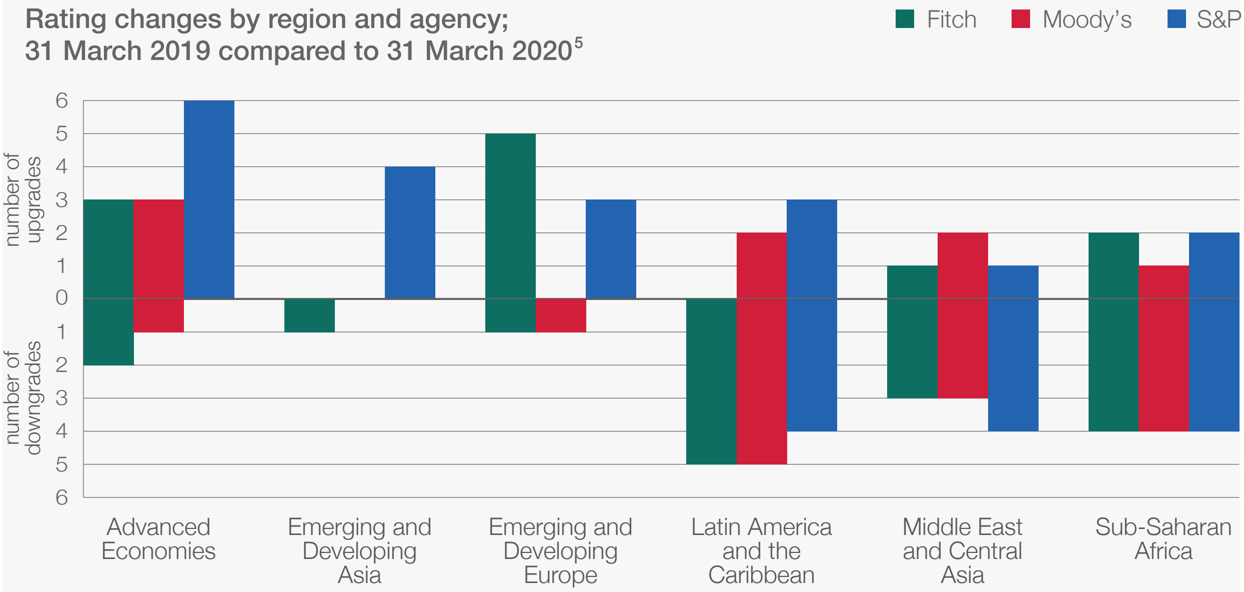
Middle East and Central Asia is expected to contract by 2.8% in 2020, but the growth rate for the Middle East and North Africa region, to which UKEF has significant exposure, is expected to be weaker at -3.3% in 2020. The markets where UKEF has considerable exposure are all projected to shrink, including Iraq (-4.7%), Qatar (-4.3%), Bahrain (-3.6%), UAE (-3.5%), Oman (-2.8%) and Saudi Arabia (-2.3%). The collapse in hydrocarbon prices has resulted in a significant deterioration in the outlook for most Middle Eastern economies. The fiscal positions of many governments in the region are likely to worsen considerably in the near-term as they support their economies through the period of low international oil and gas prices and depressed external demand – a position that can only worsen the longer the recovery takes. The projected pick-up of the global economy should see hydrocarbon prices rise but the outlook remains highly uncertain.

Sub-Saharan Africa is forecast to contract by 1.6% in 2020, the worst annual performance for the region on record. Angola's economy is projected to shrink by 1.4%, whereas Ghana and Uganda's growth rates are positive but were revised down by 4.1 and 2.7 percentage points, to 1.5% and 3.5% respectively.[4] Weak healthcare systems in the region are at risk of being overwhelmed by the spread of the virus if the number of COVID-19 cases grows rapidly. The combination of a sharp drop in economic activity, restricted access to external financing and the decline in commodity prices is likely to severely hit many economies in the region.

Rating changes

External ratings agencies, such as S&P, Moody's and Fitch provide an important benchmark for our own internal risk assessments. Credit rating actions by these agencies allow us to observe whether regional economies have been moving in a generally positive or negative direction over the last year. This is particularly important at present – growing credit weakness before COVID-19 is very likely to be exacerbated by the global recession. Ratings agencies have already downgraded a number of countries (mostly oil exporters) in the first quarter of 2020 as a result of COVID-19 and the fall in oil prices.

Rating changes by region and agency; 31 March 2019 compared to 31 March 2020[5]



Source: Fitch Ratings, Moody's Investors Service and S&P Global Ratings
Note: The number of sovereigns rated differs by agency, therefore the number of rating changes should not be directly compared across the 3 ratings agencies. As of March 2020, Fitch rates 119 sovereigns, Moody's rates 144 and S&P rates 135.

4 IMF World Economic Outlook, April 2020 compared to IMF World Economic Outlook, October 2019.
5 The chart illustrates the change in the long-term foreign currency rating for individual sovereigns since the end of March 2019 to the end of March 2020 but does not take into account multiple changes by the same ratings agency. For example, Argentina experienced multiple rating changes by Fitch over the period. However, Argentina only counts as 1 downgrade for Fitch in Latin America and the Caribbean as Argentina had a lower rating by Fitch at the end of March 2020 than they had at the end of March 2019. The chart groups countries by IMF regional classification, so only includes sovereign rating changes for countries with IMF membership plus individual Emirates within the UAE.

Over the past financial year, countries in the Advanced Economies grouping recorded a large number of rating upgrades, including **Greece**, **Lithuania** and **Slovenia**, reflecting sound macroeconomic management and improving fiscal metrics. Similarly, countries in Emerging and Developing Europe have experienced primarily positive rating changes, such as **Serbia** and **Ukraine**.

In Emerging and Developing Asia, both **Indonesia** and **Vietnam** were upgraded by S&P given strong economic prospects and relative political stability. However, the impact of COVID-19 on fiscal and external positions may weigh on the credit ratings of these 2 export dependent economies.

In sub-Saharan Africa, **Mozambique** was upgraded by all 3 ratings agencies following the conclusion of a restructuring agreement between the government of Mozambique and bondholders in September 2019.

On the downside, a number of countries in which UKEF has significant exposure have been downgraded by the ratings agencies, mainly due to a rise in debt and an increase in uncertainty following the outbreak of COVID-19 and collapse in hydrocarbon prices.

The Middle East has seen primarily negative rating changes over the past year. Notably, **Oman** received a downgrade from all 3 ratings agencies in March 2020. They highlighted the continued deterioration in Oman's fiscal position and lower affordability of its debt, which is expected to increase. Likewise, **Saudi Arabia** was downgraded by Fitch in September 2019 due to the continued weakening in the country's fiscal and external balances.

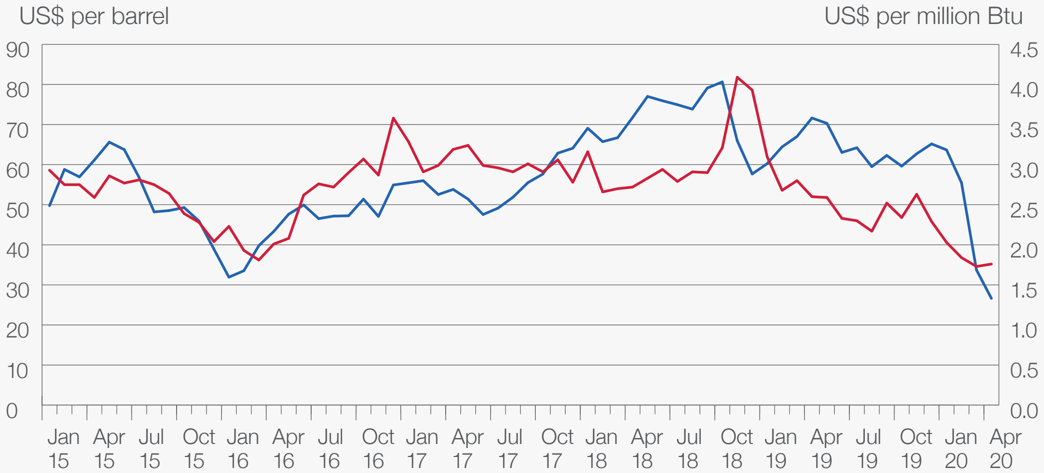
In sub-Saharan Africa, **Angola** and **Nigeria** were downgraded in March 2020, driven by the fall in oil prices as a result of the global economic slowdown and the breakdown of OPEC supply agreements. **Zambia** also received a downgrade from all 3 ratings agencies in 2019. They highlighted the country's large external financing requirements coupled with a trend in falling foreign currency reserves on the back of lower copper exports, restricted access to financing and an increase in debt.

The outlook for sovereign credit ratings in the year ahead will be primarily driven by the economic fallout from the COVID-19 outbreak, and the collapse of commodity prices for commodity-dependent economies.

The outlook for the Middle East region in particular is mixed: low oil prices will weigh on growth and fiscal metrics for some countries, such as **Iraq**, while others, like **Qatar**, are expected to withstand the shock by drawing on their substantial financial buffers. The projected economic rebound in 2021 is likely to be weaker if it takes longer to lift containment measures than assumed, or if there are subsequent surges in COVID-19 infection rates that require the re-imposition of restrictions. The large buildup of oil stocks, and significant excess supply, could see oil prices remain subdued for much longer which could be a further drag on the Middle East's recovery prospects.

Commodity prices – oil and gas price volatility

Hydrocarbon prices; January 2015 – April 2020, monthly average



Source: Bloomberg [CO1, NG1]
Note: Monthly averages based on daily closing prices

The 2019-20 period saw huge volatility in oil prices. Brent Crude oil prices reached a peak of around US$75 per barrel on 24 April 2019, before steadily declining. Oil prices began to drop rapidly at the start of 2020 as the impact of COVID-19, and the policy responses of various governments, led to a large decrease in oil demand. The OPEC+ announcement to cut production in April 2020 caused a brief rebound in oil prices, but it was not enough to reduce excess supply, with Brent oil prices at around US$25 per barrel at the end of April 2020. Meanwhile, limited storage spaces meant that West Texas Intermediate (WTI) Crude oil witnessed a significant fall in prices, reaching a historic low of negative US$38 per barrel on 20 April 2020, before recovering to a positive price. On 12 May 2020, the US Energy Information Administration (EIA) forecast that Brent Crude oil prices will average US$34 per barrel over 2020, down from an average of US$64 per barrel in 2019.[6]

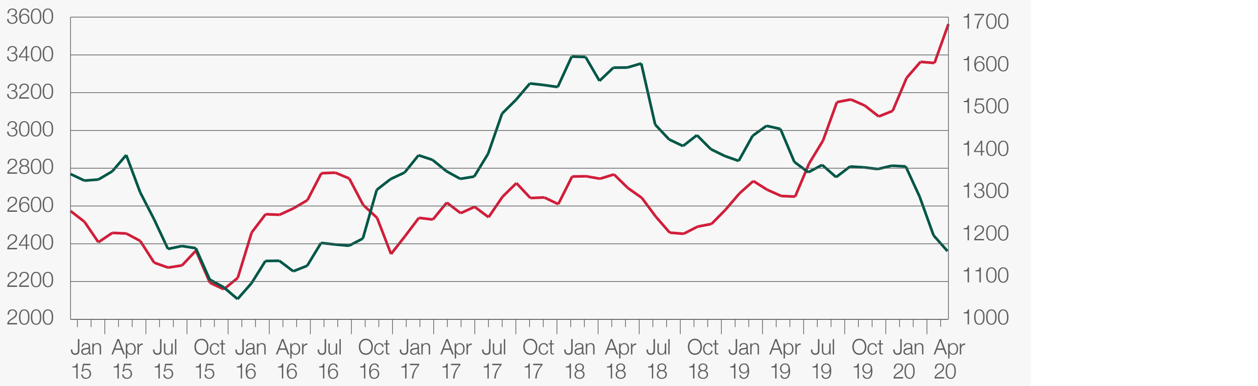
Natural gas prices (indicated by the benchmark Henry Hub price) had generally been falling through the first half of 2019, reaching a low of US$2.1 per million British thermal units (MMBtu) on 5 August 2019. Prices then briefly rebounded to a peak of US$2.9 per MMBtu on 5 November 2019, as a result of colder temperatures, before decreasing to a low of US$1.6 per MMBtu on 2 April 2020, reflecting a sharp drop in demand for natural gas – as in the oil market. The EIA forecast that Henry Hub gas prices will average US$2.1 per MMBtu in 2020, compared to the 2019 average of US$2.6 per MMBtu.

If oil and gas prices remain at these lows throughout 2020, countries which are dependent on producing these commodities, for foreign exchange and government revenues, will suffer and may face balance-of-payments crises. On the other hand, importers of hydrocarbons may benefit from low prices, as it is a key input into manufacturing and transport sectors and consumer goods. However, in the near-term, low oil and gas prices are unlikely to be a significant boost to economic growth in importing countries, due to the sharp drop in global economic activity.

6 EIA, Short-term energy outlook (12 May 2020).

Metals; January 2015 – April 2020, monthly average

Index (1994=1000) US$/oz



Source: Bloomberg [LMEX, XAU]

Note: Monthly averages based on daily closing prices

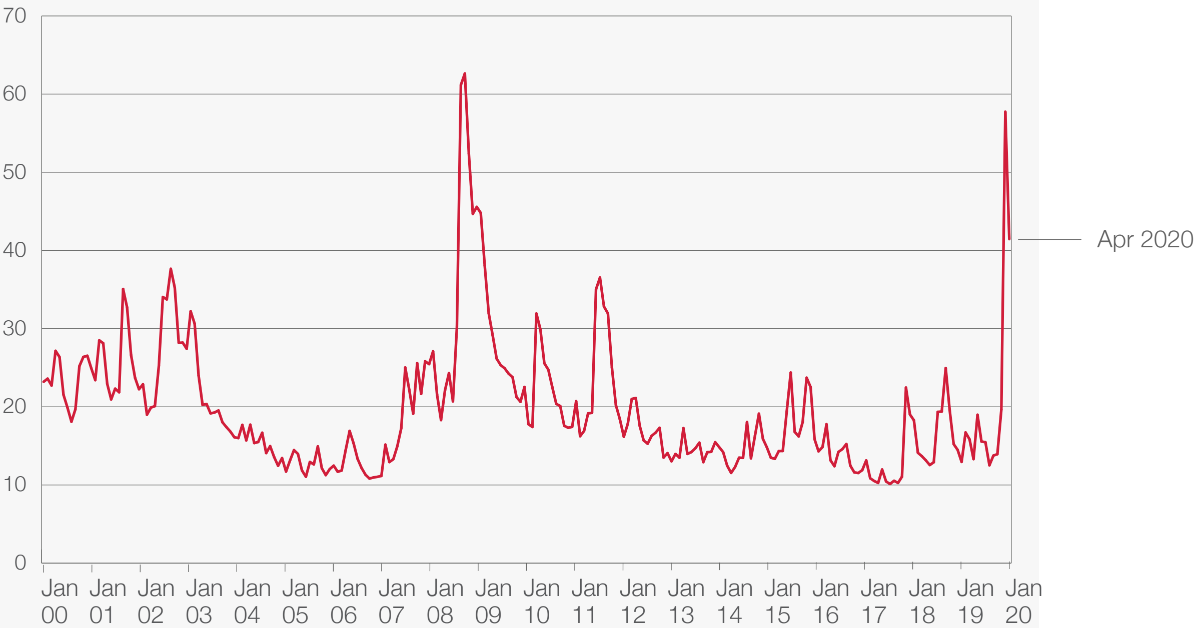
Metal prices, as measured by the London Metal Exchange Index (LMEX),[7] were relatively stable from April 2019 until the end of the year. However, in the first quarter of 2020, metal prices began to weaken as COVID-19 slowed global growth. Future prices are likely to remain low in the short-term but could rebound if the projections of a sharp global pickup in 2021 materialise.

Gold prices rose significantly throughout 2019. Prices picked up rapidly in the first quarter of 2020 to a peak of US$1,675 per troy ounce on 24 February 2020, as investors sought safe-haven assets due to the outbreak of COVID-19. Gold prices have since seen further increases, reaching over US$1,700 per troy ounce towards the end of April 2020.

Financial markets conditions

Chicago Board Options Exchange Volatility Index (VIX); January 2000 – April 2020, monthly average

Index



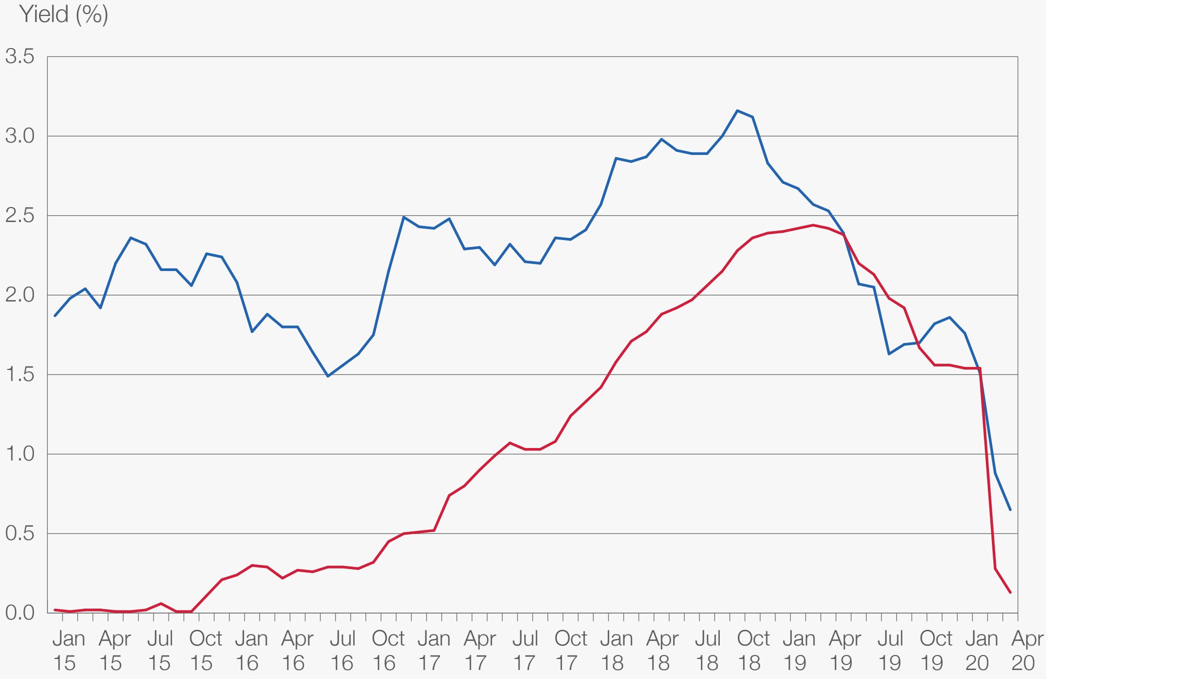
Source: Bloomberg [VIX]

7 Note: 'Metals' is based on the London Metal Exchange Index (LMEX), which is calculated once a day on the basis of the closing prices of the 6 primary metals: copper, aluminium, lead, tin, zinc and nickel.

The VIX, also known as the "fear index", reflects investor estimates of future volatility, where a rising index indicates higher risk. The VIX averaged below 20 throughout 2019 and in early 2020. However, since late February 2020 the index rapidly increased, peaking to a historic high of 82.7 on 16 March. The previous record peak was 80.9 and was reached during the 2008-09 financial crisis.

This is unsurprising, given that global stock markets have been severely impacted by uncertainty around the outbreak of COVID-19, the scale and breadth of the recession and consequences for earnings. Stock markets have seen substantial falls in the first quarter of 2020 as business confidence has collapsed. At the end of April 2020, the FTSE 100 and Dow Jones had fallen by around 22% and 16% respectively since the beginning of January 2020.[8]

US Treasury 3-month and 10-year yields; January 2015 – April 2020, monthly average



Source: Bloomberg [GB03, GT10]

The 3-month and 10-year US Treasury yields have experienced a steady decline since April 2019, with the yield curve inverting in late May 2019 until October 2019. The 10-year yield then began to pick up slightly for the remainder of the year and into January 2020, with the 3-month yield plateauing.

With the outbreak of the virus in 2020, both the 3-month and 10-year yields collapsed as concerns of a global recession grew and investors moved capital towards the safer option of US Treasuries.

The Federal Reserve cut its interest rate target range from 1.5%-1.75% to 1%-1.25% in early March 2020, and the 10-year yield fell below 1% for the first time ever to a record-low of 0.5%. The Federal Reserve has responded to the deepening economic crisis by cutting interest rates further by 1 percentage point to 0%-0.25% in mid-March, a level not seen since 2015.

8 Bloomberg [UKX, INDU].

UK economy

The UK economy grew by 1.4% in 2019, a slight increase from 1.3% in 2018, but lower than 1.9% in 2016 and 2017.[9] The Office for Budget Responsibility (OBR)[10] published analysis of the potential impact of the COVID-19 outbreak on the UK economy, assuming a 3-month lockdown followed by another 3-month period where the lockdown is partly lifted. Under this scenario, the OBR estimates that the UK economy could contract by 12.8% in 2020. This is a much sharper decline than the IMF's growth projections for the UK (-6.5%). However, the OBR's analysis suggests that the UK economy could then expand by 17.9% in 2021, while the IMF forecasts growth of only 4.0%.

As of 30 April 2020, Fitch has been the only ratings agency to downgrade the UK following the start of the COVID-19 pandemic, which it did on 27 March 2020 from AA to AA-. Fitch state that the downgrade reflects a significant weakening in the UK's public finances and fiscal loosening following the "commensurate and necessary policy response" to the COVID-19 outbreak.

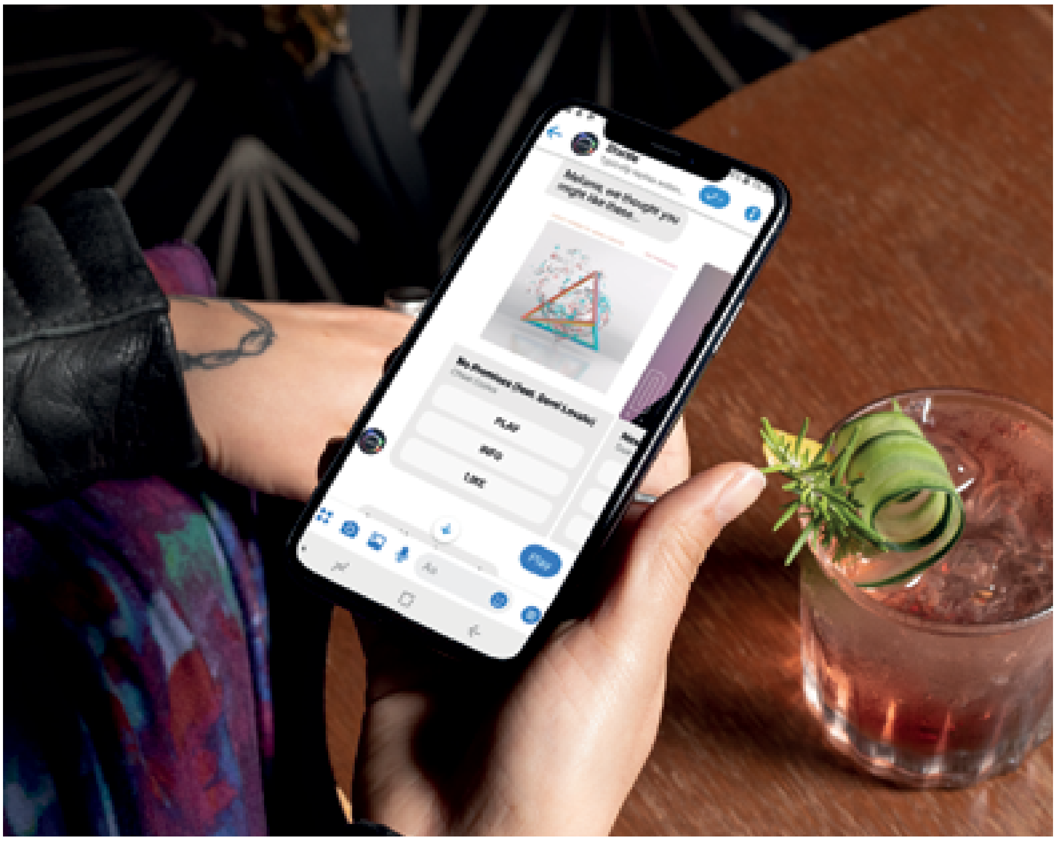
Fitch has also assigned a negative outlook for the UK based on its perception that the deterioration of the fiscal metrics may extend beyond 2020 and uncertainty around the UK's future relationship with the EU hindering the post-crisis recovery. Fitch suggests that the stimulus package could lead to a widening of the fiscal deficit to around 9% of GDP in 2020 from 2.1% of GDP in 2019, increasing government debt to 94% of GDP in 2020 from 84.5% of GDP in 2019.[11]

The UK left the EU on 31 January 2020 under the terms of the revised Withdrawal Agreement (WA), entering a transition period and commencing "phase 2" negotiations on the future relationship between the UK and EU. The WA allows the UK to forge a new economic partnership with the EU that will protect existing trade and supply links, while giving the UK new flexibilities to embrace trade opportunities with the rest of the world. Talks between the UK and EU remain ongoing despite the current crisis with the transition period set to end on 31 December 2020.

9 ONS, Gross Domestic Product: Year on Year growth: CVM SA % (31 March 2020).
10 OBR, Coronavirus reference scenario (14 April 2020).
11 Fitch Downgrades the UK to 'AA-'; Negative Outlook (27 March 2020).

Near-term outlook

The current environment presents both a challenge and an opportunity for UKEF. Export Credit Agencies (ECAs) are essential during periods of global economic slowdown as they play a counter-cyclical role – we support commercial banks through periods of financial market disruption, keep credit flowing and trading networks working. This was the case following the global financial crisis of 2008-09, and we will be doing the same in 2020-21 and beyond. However, the continuing outbreak and scale of its impact means there is heightened risk of defaults, and UKEF has been working with HM Treasury to put in place a temporary refinement of its standard risk management framework, to help us continue to support UK exporters through the current crisis.



UKEF supported music technology firm Startle to expand into the United States

How we operate

UKEF's statutory purpose is to support exports and overseas investments.

We do so principally by providing:

- trade credit insurance to exporters against the risks of non-payment for amounts owed under export contracts
- guarantees to banks to support working capital financing and the raising of contract bonds on behalf of exporters
- guarantees to banks and investors in the debt capital markets in respect of medium- to long-term loans to overseas buyers who purchase goods and services from UK exporters
- lending directly to overseas buyers who purchase goods and services from UK exporters
- political risk insurance for investments made overseas

UKEF supports exports of all types of goods and services (including intangibles) and can help businesses of all sizes that seek protection from the financial risks of exporting.

In doing this, our role is to complement the private market: we seek to support exports that might otherwise not happen, thereby supporting UK exporters and incentivising overseas buyers to source from the UK. The space in which we operate is largely determined by the willingness and capacity of the private market to assume financial risks in support of exports at any given time. We are also bound by state aid restrictions on supporting short-term export credit insurance for exports to EU countries (currently excluding Greece) and rich OECD countries (for example, the US).

The financial liabilities we assume when supporting exports involve a transfer of risk from the private to public sector. Direct lending involves upfront public expenditure while other financial liabilities represent contingent public expenditure – that is, taxpayer funding is required only in the event of claims being made on insurance policies or guarantees provided to banks. When claims are made, we instigate appropriate recovery action on a case-by-case basis or, where there is a sovereign default, through the Paris Club of official creditors to recoup the relevant payments.

UKEF operates under the consent of HM Treasury, which sets financial objectives that we must achieve. These, and the credit risk and pricing policies we operate to meet them, are set out on page 58 to 85.

We also operate under international (principally OECD) agreements that seek to create a 'level playing field' by setting terms under which national credit agencies can support exports. However, not all export credit agencies (ECAs) are party to these international agreements and competition for UK exporters is increasingly from non-OECD countries whose ECAs are not bound by these agreements.

Principles applied by UKEF

On individual cases, we aim to:

- provide a quality of service that is responsive, flexible and efficient, with a focus on solution and innovation
- take account of factors beyond the purely financial, and of relevant government policies in respect of environmental, social and human rights impacts, debt sustainability, and bribery and corruption

Generally, we aim to:

- publish guidance for applicants on the processes and factors we take into account in considering applications
- achieve fairer competition by seeking to establish a 'level playing field' internationally through obtaining multilateral agreements in export credit policies and practices
- recover the maximum amount of debt in respect of claims paid, taking account of the government's policy on debt forgiveness
- abide by such codes of practice and guidelines on consultation as may be published by the government from time to time
- be a great place to work, recruiting, developing and retaining the people we need to achieve our Business Plan objectives

Our export solutions

Our support for UK exports can be categorised as long-term (export credit) and short-term support (trade finance).

Export credit support typically covers exports of capital/semi-capital goods and related services, for example large projects or high value machinery. Due to the high values involved (normally £5 million to more than £1 billion), overseas buyers frequently require loans (usually repayable between 5 and 10 years, or longer) to finance the purchase of such supplies from UK exporters. We provide support under our finance products (such as buyer credit guarantees) to banks that provide export credit loans, thereby covering the risk of default by borrowers. Alternatively, we can lend to buyers directly.

Trade finance support typically covers consumer or intermediate goods and services, for example, consumer durables or light manufactured goods. These goods are typically sold on short credit terms (up to 1 year), which exposes exporters to (a) risk of non-payment, and (b) the need to finance working capital (pre-shipment financing) and the credit period (post-shipment financing). We have products designed to meet these challenges which are available to exporters and in some cases to their direct suppliers.

Export solutions

Longer term credit (2 to 18 years)	**Export credit solutions** Supporting finance for overseas buyers of UK exports	• Providing guarantees to banks on the loans they give to overseas buyers to purchase goods and services from the UK • Direct lending to overseas buyers so that they have the funds to purchase goods and services from the UK	• Buyer credit facility • Supplier credit facility • Direct lending • Lines of credit • Export refinancing facility	Lower volume, higher value
Shorter term credit (less than 2 years)	**Trade finance solutions** Supporting UK exporters	• Reducing or removing the risk of non-payment by overseas buyers • Helping to support a bond required under the terms of a contract • Supporting working capital	• Export insurance • Bond insurance • Bond support • Export working capital	Lower value, higher volume

Investment into the UK

Access to UKEF's products and services can provide an incentive for companies to base their international business in UK, supporting foreign direct investment (FDI) in the UK.

We can also support overseas direct investment by insuring overseas investors against certain political risks, helping to create inward flows of dividends and investment gains to the UK.

The UK Trade and Export Finance Forum in June 2019 was attended by over 700 delegates, with an agenda that provided real and substantive help to exporters and potential exporters looking to grow internationally.

Our support for exports

Business supported

Exporters directly supported	339
Value of support provided	£4.4 billion
Destination countries	69
Largest single facility	£528 million (Export Development Guarantee)
Smallest case	£639 (Export Insurance Policy)
Most popular product	Bond Support Scheme (61 companies)
Highest value product (total use)	Buyer Credit Facility (£2.1 billion)

Gordon Welsh
Business Group Director

The Trade Finance Division: making exports happen

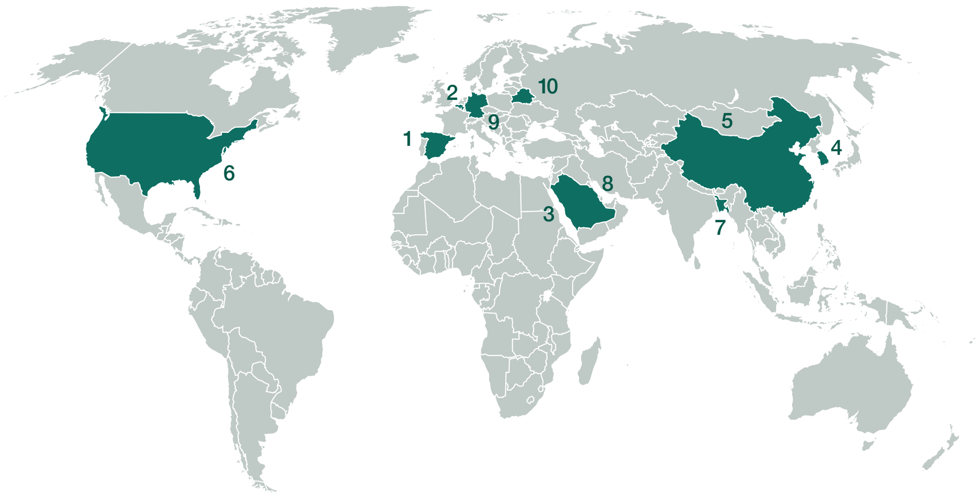
In October 2019 the short-term business of UKEF, comprising trade finance and export insurance, was joined by the export finance managers team and the business support group to form the Trade Finance Division. The alignment of SME business development with our underwriting function and post issue management enables an end-to-end view of the business that creates opportunities for strategic enhancements to our overall customer business activities in this segment of the market. These activities will be incrementally developed commencing in the business planning cycle of 2020-21.

Short term trade finance and export insurance

UKEF's short-term trade finance support allows exporters and direct suppliers to exporters to access finance from banks and other financial institutions to enable export activity where otherwise they may not. Often, this support is a critical factor for a business in winning and then ensuring that they can fulfil a contract. Support is available in the form of guarantees under our bond support and export working capital schemes.

We also provide insurance for exporters, principally against the risk of non-payment by their buyer, where the commercial market is not able to provide the cover required.

Trade finance and export insurance: top 10 markets by value in 2019-20



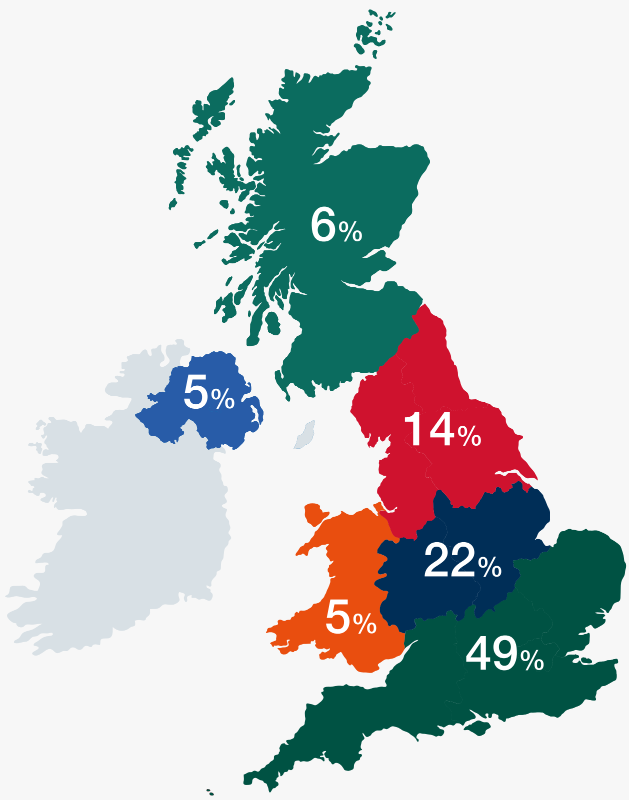
1. Spain
2. Belgium
3. Saudi Arabia
4. Korea, Republic of
5. China
6. United States
7. Bangladesh
8. Bahrain
9. Germany
10. Belarus

Since the launch of our trade finance products in 2011, we have supported £5.84 billion in contracts through these products.

On-the-ground support for exporters: export finance managers

We have 24 export finance managers (EFMs) across the UK, who act as local points of contact to introduce exporters and businesses with export potential to finance providers, credit insurers, insurance brokers, trade support bodies and sources of government support.

Proportion of companies benefiting from UKEF trade finance or insurance by region in 2019-20



This presence across the UK makes a significant contribution to our drive to increase awareness and uptake of UKEF products among small and medium-sized exporters all over the country.

EFMs develop relationships on a local basis, providing on-the-ground support for exporters across the UK. This year, EFMs had 4,116 customer interactions of which 1,170 were with intermediaries including banks and brokers.

In addition to helping companies access UKEF products, EFMs deliver 'exporter assists' – when their engagement makes a material contribution to a company receiving support from the private sector, resulting in an export contract going ahead that was unlikely to have proceeded otherwise. EFMs also made more than 1,585 referrals to third-party sources of support.

There were 145 referrals from our EFMs to services provided by the Department for International Trade (DIT), Scottish Enterprise, Business Wales and Invest Northern Ireland. In addition to the outward EFM referrals, UKEF has received 303 referrals from DIT's International Trade Advisors (ITAs), demonstrating the close linkages between the government's export promotion and export finance support.

Enhancing our products and services

Since the launch of UKEF's bank delivery model and trade finance digital service, UKEF has continued to work in partnership with our 5 current partner banks, Barclays, Santander, HSBC, Lloyds/Bank of Scotland and RBS/NatWest/Ulster Bank, to make further enhancements to the service. Revised legal documentation was agreed in January 2020, which has further simplified the service following the first year of operation, resulting in approximately 60% of all transactions now processed automatically.

Following the announcement of the new General Export Facility in March 2019, UKEF concluded an initial transaction with Jaguar Land Rover in respect of a £500 million guarantee on £625 million of commercial bank lending. Both this and the Supply Chain Discounting initial programme, as announced in January 2019, will provide UKEF with key feedback in relation to these two new products and inform enhancements for full implementation in 2020-21 if proven successful.

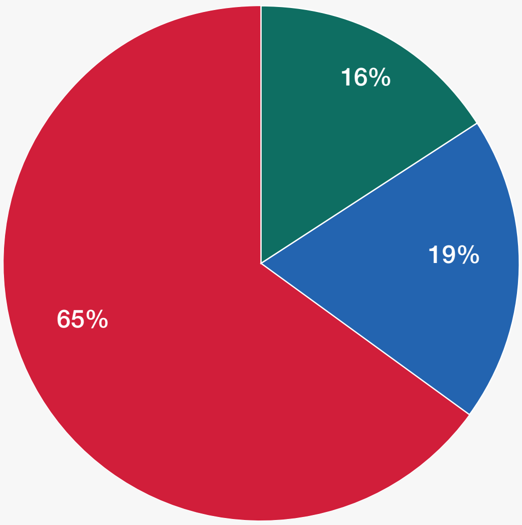
In respect of existing products, UKEF has undertaken a review of the Supplier Credit Facility to better meet the needs of users. Work has taken place to update the existing legal documentation, working closely with UK Finance. Initial improvements in the documentation for paperless loan structures are being finalised for implementation, with additional work planned for alternative finance structures due to be delivered in 20-21.

UKEF has continued to implement policy and process improvements. In July, UKEF published the outcome of the public consultation on Foreign Content policy. Launched in April 2019 as part of UKEF's commitment in the Export Strategy to review its products and policies, the consultation received 28 responses, which were largely supportive of the approach proposed by Government and reinforced the need for the Department's Foreign Content policy to adapt to increasingly globalised supply chains. The revised Foreign Content policy has been used to support, among others, a £47.6 million financing for the construction of 2 large solar plants in Spain, allowing UKEF to recognise the significant development and design expertise in the solar energy sector in the UK.

In addition, UKEF has worked closely with DFID to implement process improvements in relation to application of the OECD Recommendation on Sustainable Lending. These improvements will streamline assessments of the debt sustainability of a project utlising UKEF support, resulting in an improved service to UKEF's customers.

Export credits: helping UK businesses compete in the global marketplace

Export credit business supported (medium/long-term) 2019-20



Sector	UKEF maximum liability, £m
Aerospace	665
Civil – direct loans	775
Civil – guarantees	2691
Defence	6

UKEF provides export credit support by guaranteeing commercial finance or providing direct loans to overseas buyers to purchase goods and services from the UK.

Interest in UKEF's guarantee and direct lending products remains high due to:

- reduced risk appetite and lending capacity for longer tenors among banks
- other governments' budgetary constraints due to low commodity prices and ambitious infrastructure investment which requires extra capacity to be provided alongside other financial resources

Sector support

Civil, Infrastructure and Energy

2019-20 was another busy year for UKEF in the civil, infrastructure and energy sectors, with buyer financing support worth a total of £3.5 billion provided across 16 countries.

In Taiwan UKEF has supported 3 significant wind farms. These are landmark deals for UKEF supporting both offshore wind directly and the first major project financings in the renewables sector for UKEF. These transactions also share a notable feature being financed in local currency.

UKEF also closed its first non-aviation Islamic Financing, being a Murabaha Islamic compliant structure supporting 3 UK suppliers to Serba Dinamik, for 7 projects covering the design, supply, installation and commissioning of equipment and services to improve electricity generation and provide gas storage/transportation equipment in various locations.

UKEF continued its support for healthcare projects with £720 million of finance being guaranteed for 3 hospitals being built in Oman to meet a range of healthcare needs. This was a strong sector for UK export contracts this year with UKEF also supporting healthcare centres and district hospitals in Zambia though a £300 million financing and providing over £100 million of finance for 2 hospitals in Ghana.

Ghana has continued to be a strong market for UK exporters supported by UKEF with 2 airport projects closing this year at Tamale and Kumasi and continued strong future demand.

In a year that featured the UK-hosted Africa Investment Summit UKEF was pleased to continue to grow its support in countries including Uganda, Gabon and Angola where projects totaling over £350 million have been concluded.

In the energy sector UKEF participated with other Export Credit Agencies and commercial lenders in an innovative and award-winning project finance structure to bring up to best in class standards the BAPCO refinery, being the largest single contributor to the Bahrain economy.

The Middle East has been a strong area for UKEF supported projects for many years with this year seeing a landmark design project, the Curve Hotel project in Dubai, also reaching financial close.

The establishment of UKEF’s Smaller Deals initiative was announced at UKEF's Trade and Export Finance Forum in June 2019. That initiative provides support for exporters looking to offer extended payment terms to their overseas customers, often involving smaller / SME exporters trading with smaller / SME partners overseas.

The initiative has supported seven sub-£10 million transactions to date and has a very strong pipeline of future business. The latter has been generated in conjunction with UKEF’s network of Export Finance Managers and International Export Finance Executives, along with counterparty lenders – including the first non-bank institution UKEF has partnered with in the medium-term finance space, London Forfaiting Company.

A range of supporting announcements are planned for 2021-22. UKEF expects this to lead to a significant increase in the awareness of the support UKEF can provide for smaller value export contracts, and to the volume of these transactions UKEF is able to support as a result.

‘UKEF’s flexible finance was key to securing this contract, which will have a marked impact on the lives of people in Gabon and on our future growth. Their support for this project and of other infrastructure projects in the region demonstrates the UK government’s commitment to growing UK trade with Africa’

Carl Fergusson
Chief Executive Officer, Colas UK

Aerospace and Defence

With buyer financing support worth a total of £665 million, the volume of support provided for aerospace transactions reflected the continuing strong appetite of the commercial market for asset-backed lending to airlines. UKEF's support increased compared with 2018-19 (£450 million), although remains relatively low compared with historical levels.

UKEF-supported financing for Rolls-Royce-powered Boeing 787 aircraft continued in 2019-20 with further support provided for 2 B787-8 aircraft delivering to EL AL Israel Airlines, taking the total number of Rolls-Royce-powered Boeing 787 aircraft supported across all customers to 18 to date.

UKEF and its French and German counterparts continued to provide support for Airbus A380 deliveries to Emirates Airlines in 2019-20, supporting the delivery of 6 such aircraft. Support followed satisfactory completion of the extended due diligence process developed to assess applications from Airbus for export credit support. Support was also provided for the delivery of 2 Airbus A330Neo aircraft to Air Senegal, these being the first A330Neo aircraft the ECAs have supported.

On 31 January 2020, Airbus reached settlements with the UK, French and US authorities. In the UK, Airbus and the SFO entered into a Deferred Prosecution Agreement which brought to a close a 4-year investigation into bribery offences.

In 2019-20, a further loan was provided in support of the engine overhauls undertaken by GE Caledonian in Prestwick in Scotland, taking support for GE Aviation overhaul in the UK well over the $120 million mark. Our assistance, delivered in partnership with the Export-Import Bank of the United States, is supporting specialist engineering jobs in the UK, and we continue to work with GE Aviation to identify further opportunities to secure contracts for GE Caledonian.

Defence sector business was much reduced from the significant contribution to UKEF’s business supported figures for 2018-19 reflecting the tendency for large irregular deals in this sector. Proactive management of the existing UKEF exposure in Qatar has ensured retention of UKEF’s risk capacity for new projects. A number of deals were targeted to close near to financial year end and a strong pipeline of new transactions is in place for 2020-21.

Bringing business to the UK

In 2019-20, UKEF has enhanced and expanded the 'leading with finance' approach to bringing business to the UK.

UKEF's supplier fair model is an ambitious programme to help increase UK content in overseas projects UKEF is supporting through procurement-focused events, working with trade associations and the Department for International Trade to activate the UK supply chain. These day-long matchmaking events connect relevant UK suppliers with international buyers who are actively looking for British products and services for their overseas project or projects; this helps the buyer make successful commercial decisions and the UK supplier win overseas contracts. For each supplier fair, UKEF requires a contribution of £12,000 from the sponsor, which goes towards the cost of the event.

UKEF held 6 supplier fairs in 2019-20, connecting over 500 exporters with opportunities potentially worth hundreds of millions of pounds in sectors as diverse as rail, construction and healthcare, with more to come in the future.

'The whole process - from first awareness to departure - was excellent... The ability to inform and involve SMEs in the often impenetrable world of major international corporations in such a way is perhaps unique and is applauded.'
Delegate at a UKEF Supplier Fair

Our partners and operations

Building strategic relationships and collaborating with partners in both the private and public sector is a vital part of our offer to customers.

Partnerships help us to source export opportunities, deliver our products, support exporters and raise awareness of our products and services, ensuring UKEF's support reaches businesses at home and overseas buyers.

Our partners

Other government departments: UKEF's offer of finance is at the heart of the government's Export Strategy and we work closely with other government departments to support UK exporters and overseas buyers.

This year we have collaborated extensively with private and government owned entities like the Private Infrastructure Development Group (PIDG), and CDC Group (the UK's development finance institution), along with the Foreign and Commonwealth Office (FCO), the Department for International Trade (DIT) and Department for International Development (DFID).

We continue to support and educate business-facing colleagues in other departments. UKEF offers an accredited online training course developed with the Institute of Export and International Trade, the Award in Trade Finance, to improve government officials' knowledge of trade and export finance.

Commercial finance (lenders), insurance and re-insurance partners (brokers and insurers): UKEF's role is to complement the commercial sector, and its guarantees, loans and insurance products are delivered through around 100 private sector partners.

We work with over 20 private re-insurance organisations to actively manage concentration risk and to offset some of the risk exposures in the portfolio.

We have continued to develop our bank partnership delivery model for our short-term trade finance support by making the process clearer, simpler and more efficient for all parties to improve turnaround times in banks. In February 2020 we introduced a new Master Guarantee Agreement ("MGA") in conjunction with the 5 largest UK Banks and will continue to onboard new financial institutions to improve accessibility for exporters.

UKEF collaborated with banking partners at our annual **UK Trade & Export Finance Forum held in June 2019**. HSBC bank was the platinum partner, with Standard Chartered, Lloyds Banking Group and Mitsubishi UFJ Financial also supporting the event, highlighting the close collaboration between public and private sector to deliver finance for exports. See page 208 for the amount of sponsorship received for this event.

Export credit agencies: UKEF works with other ECAs to jointly deliver export credit support where transactions include content from multiple countries. To do so, it has reinsurance and co-operation agreements in place with 61 ECAs, this year adding:

- The Export-Import Insurance Company of the Republic of Belarus
- The Export-Import Bank of China
- JSC National Managing Holding (Kazakhstan)
- Korea Trade Insurance Corporation
- Nigerian Export-Import Bank
- The Export Credit Insurance Corporation of the Republic of Poland

In 2019-2020, UKEF worked with BPI France, Export-Import Bank of Korea, Export Development Canada, Euler Hermes (Germany), Eksport Kredit Fonden (Denmark), US EXIM Bank, Garantiinstituttet for Eksportkreditt (Norway), Oesterreichische Kontrollbank (Austria) and Servizi Assicurativi del Commercio Estero (Italy), among other ECAs.

Industry bodies: UKEF engages with industry bodies to seek market intelligence and insights that facilitate the development of our products and services while promoting our support to their members. Key relationships include:

- the British Exporters Association (BExA), which evaluates UKEF against other national ECAs
- the Confederation of British Industry (CBI), which provides feedback from industry and supports UKEF's business outreach
- the Institute of Exports and International Trade (IOE&IT), which partners with UKEF to increase knowledge of export and trade finance and insurance throughout the business community
- the Federation of Small Businesses (FSB), to understand challenges faced by small businesses in financing export activity
- Make UK, which supports the manufacturing sector and highlights challenges faced by the UK supply chain across sectors to access finance for their exporting business

- the British Chambers of Commerce, which, through its regional network of accredited chambers, works with UKEF's Export Finance Managers (EFMs) to promote exports
- UK Finance, on new product development and delivery, as well as to discover the challenges faced by SME's to access finance and general support. This year we consulted UK Finance on product development for Supplier Credit, General Export Facility, Export Development Guarantee and Trade Finance

Internationally, UKEF plays an active role in negotiations at the OECD, the main rule-making body for export credits. A key topic over the last year has been modernisation of the Arrangement. UKEF is also a founding member of the Berne Union, the trade association of both ECAs and private sector insurers.

UKEF also works with sector-focused trade associations, such as the Energy Industries Council, the Renewable Energy Association (REA), Aerospace Defence and Security (ADS) and Subsea UK to understand emerging trends and challenges faced within their sectors, engage with their members, and raise awareness of overseas projects at supplier fair events.

Multipliers: UKEF has developed strategic relationships with commercial organisations that have an interest in projects in multiple sectors around the world. These businesses cover the full lifecycle of a project from early stage project preparation to work on procurement and construction.

UKEF has formed these partnerships in order to jointly identify projects that would benefit from UKEF financing support and expertise from the UK supply chain. In return, UKEF's partners promote their overseas projects in the UK and generate export opportunities for the UK companies.

Examples of these multiplier relationships include:

- Atkins Acuity, part of SNC Lavalin
- Advisian, part of Worley Parsons
- Maire Tecnimont
- Mace group

Professional services providers: We continue to build our strategic engagement with accountancy, consultancy and legal firms as an important referral channel. Several leading companies including PwC, KPMG, BDO and EY have committed to support the delivery of the Export Strategy by collaborating with DIT and UKEF, deploying their UK and overseas networks to improve awareness of the support on offer.

Our operations

Our Change and Transformation Plan has equipped UKEF with the necessary infrastructure and resources to become more focussed on our customer's needs, delivering on our strategic aims to be agile and adaptable and provide high levels of customer service.

This builds on significant investments in the early years of the 2017-20 business planning period to improve underlying IT infrastructure. In 2019-20, improvements were made to enhance efficiency, resilience and scalability in UKEF's operations, including:

1. continuing improvements to UKEF's digital trade finance service to make it easier for our customers to receive finance through our bank partnership delivery model
2. work on delivering 'straight through' processing of transactions so that they can be completed without manual re-keying of data, making the process quicker and more efficient, as well as reducing operational risk
3. significant improvements to the intranet, to make it easier for staff to communicate and collaborate with each other
4. automated testing capability to improve the way systems changes are assured
5. an upgrade of reporting capability

Members of the Technology, Change and Innovation team meet to discuss the Change and Transformation Plan

Chief Risk Officer's Report

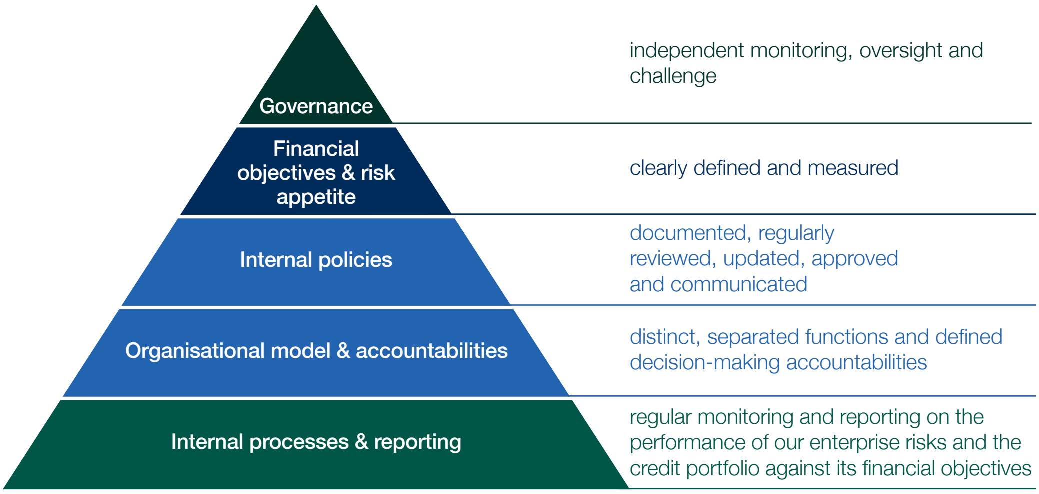
The primary risks to which UKEF is exposed include financial risk (including credit, market and liquidity risk), operational risk, strategic and business risk, environmental and social risks, compliance and legal risks, program and project risk, political risk and external risks.[1]

Samir Parkash
Chief Risk Officer

Within UKEF, conduct, culture and reputational risks are identified, evaluated and monitored on a departmental basis rather than as a separate risk type.

All our risk management practices aim to at least match the financial services industry's best practice standards. However, given our role as a government-backed export credit agency (ECA), the composition of our portfolio is somewhat different. Our UKEF Risk Management Framework is detailed below.

UKEF's risk management framework



1 A description of our approach to operational risk is discussed in the Governance Statement on pages 108 to 123. Environmental, social and human rights risks are discussed in the head of Environment and Social Risk's report on pages 95 to 99.

Risk management

Context

Parliament sets an overall limit of SDR67.7 billion[2] on the commitments into which UKEF may enter. UKEF's powers may only be exercised with the consent of HM Treasury (HMT). The limits of this consent are agreed with HMT, along with financial objectives and reporting requirements that serve to regulate the risk we take on.

As the UK's ECA, our role, mandate and risk appetite differ from financial institutions in the private sector. So, while we do compare our risk management framework with what we consider best practice in the financial services industry, a direct comparison with all the metrics used by regulated commercial entities can be misleading. The portfolios of ECAs will tend to have:

- a higher risk profile
- a focus on emerging market risks
- longer risk horizons
- greater risk concentrations (on counterparties, sectors and geographic regions for example)

Risk governance

The ultimate responsibility for risk management within UKEF lies with the Chief Executive who, as Accounting Officer, is answerable to ministers and Parliament for all aspects of the department's operations. The Chief Executive is supported by a number of committees (principally the Enterprise Risk and Credit Committee (ERiCC)) and UKEF's risk management activities are subject to independent oversight and monitoring.

The UKEF Board provides independent advice, scrutiny and challenge to the Chief Executive across a broad range of areas, including risk management, while its Risk Committee separately reviews the adequacy of risk management and controls across the department.

UK Government Investments (UKGI) represents the Secretary of State on the Board of UKEF. Its officials review the department's risk management function and processes, to help ensure that risk and internal controls are effectively managed. UKGI also works with HM Treasury has also delegated to UKGI monitoring of the department's performance against its financial and non-financial objectives.

Within UKEF, the ERiCC is responsible for advising the Chief Executive on the effective management of our enterprise and credit risk exposures. Its responsibilities include:

- ensuring the effective identification, assessment, management and reporting of enterprise risk across UKEF in accordance with UKEF policies, procedures and risk appetite
- agreeing policies, procedures and methodologies for calculating and charging premium, and monitoring portfolio risk, including risk parameters and assumptions used in PRISM (Portfolio Risk Simulation Model)

2 This limit is expressed in special drawing rights (SDR), an international reserve asset created by the IMF. SDR67.7 billion corresponds to approximately £74.8 billion.

- managing and monitoring credit risk exposures at transaction and portfolio level, and approving credit risk exposures above the level of authority delegated by the Chief Executive to senior risk executives, including through country risk parameters, country exposure limits, minimum Risk Standards for sovereign and corporate obligors, corporate risk assessment methodologies, sector reviews and watch list portfolio reviews
- agreeing credit risk policies
- ensuring that credit risks are properly monitored, controlled and reported through UKEF's processes and systems

It is scheduled to meet fortnightly and can be convened on an ad hoc basis to consider urgent business. The standing members of the Committee are:

1. Chief Executive Officer
2. Chief Risk Officer (CRO)
3. Chief Finance & Operating Officer (CFOO)
4. Business Group Director
5. Deputy Chief Risk Officer
6. Head of Underwriting Policy and Products
7. Head of Portfolio Management
8. Chief Analyst

The Director of Legal and Compliance, or a nominee, will also attend to provide advice on legal and compliance matters. In the absence of the Chief Executive, a unanimous decision of standing members, including the CFOO, must be obtained for any approvals.

Organisational model and accountabilities

UKEF has a functional organisation structure, which separates business origination work from risk, financial control and reporting functions. This basic internal control is designed to avoid potential conflicts of interest and to provide vital and appropriate checks and balances in the business origination, credit approval and risk management processes.

Within the Risk Management Group, there is a framework of delegated credit authorities:

- the CRO has been given authority by the Chief Executive to approve various categories of credit risk within pre-determined limits
- in turn, the CRO has granted authority over certain credit approvals to senior staff within their team
- credit approvals that exceed the delegated authority of the CRO must be approved by the ERiCC (and for larger transactions, also the Accounting Officer)

Enterprise Risk

During 2019-20 UKEF created an Enterprise Risk Division within the Risk Management Group. It is responsible for reviewing, enhancing and developing the department's approach to managing Enterprise Risk. The Enterprise Risk Framework is designed to ensure that adequate processes, procedures, reporting and control mechanisms are embedded in the business to facilitate the identification, assessment, reporting and remediation of risks across UKEF. The Enterprise Risk Division operates through 2 teams:

- The Risk Governance team: responsible for designing, implementing and managing a best practice Risk Appetite Framework within UKEF and supporting business functions to embed it in their day-to-day operations.
- The Operational Risk team: responsible for designing, implementing, monitoring and managing a best practice approach to Operational Risk. This supports the effective management of risks within acceptable boundaries whilst achieving the strategic objectives defined within the UKEF Business Plan.

The Chief Executive has appointed the CRO to be responsible for leading UKEF's overall approach to risk management and ensuring adequate skilled resources are employed to independently influence governance and decision-making forums.

Using a UKEF-issued Export Insurance Policy, Teignbridge Propellers International was able to fulfil a major order to Bangladesh

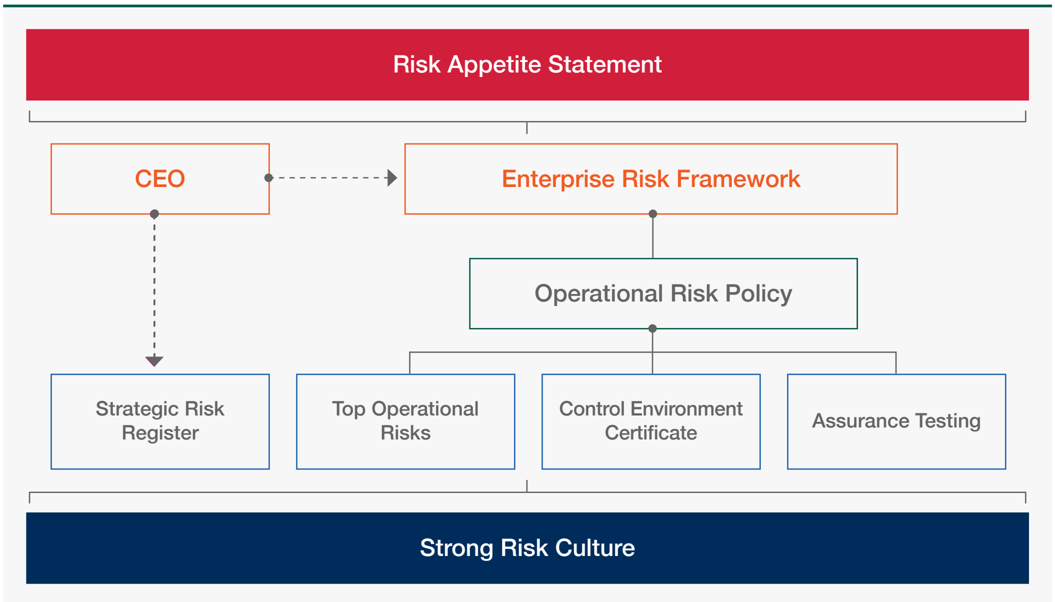
Key components of enterprise risk

The UKEF approach to enterprise risk enables the department to consider the potential impact of all types of risks on all processes, activities, stakeholders, products and services. It allows UKEF to understand and prioritise significant risks and identify the weakest key controls in order that UKEF can make decisions in the knowledge of the underlying risks and manage these risks appropriately.

An Enterprise Risk taxonomy has been approved by the ERiCC. This provides senior management with a structured approach to identifying, assessing, evaluating and reporting known and emerging risks across UKEF. The 8 Enterprise Risk categories are as follows:

Primary Enterprise Risk Category	Definition
Environmental, climate & social risks	The risk of an actual or potential threat to or from the environment arising out of the department's activities
Financial risk (including credit & market risk)	The risk of claims being made against UKEF, and of it suffering ultimate loss arising from defaults by counterparties against which UKEF has a financial exposure.
Strategic & business risk	The risk of direct or indirect loss arising from a suboptimal business strategy or failure to respond positively to changes in the business environment
Political risk	The risk that political decisions, events or conditions will have a significant impact on the department's strategic objectives and priorities
Operational risk	The risk of direct or indirect financial losses resulting from inadequate or failed internal processes, people, systems or external events
Programme & project risk	The risk that defined objectives, plans and change initiatives fail to meet agreed timescales, budgets and/or expected outcomes
External risks	The risks beyond the direct control of the department
Compliance & legal risks	The risk of being exposed to censure, financial loss, civil or criminal proceedings due to failing to comply with applicable laws, regulations or legal obligations

The Enterprise Risk Framework comprises the following key components that define key themes, practices and processes that UKEF has in place to manage risk effectively:



There is a discipline of reappraising the opportunities and risks facing UKEF as both alter with time and circumstances. This is achieved by the regular review, appraisal and update of risk and control assessments by the business. Control Registers have been prepared by all divisions detailing the controls in place to manage key processes. Additionally, incidents are reported by the business. Incidents are monitored and analysed by the Enterprise Risk Division to identify key themes and ensure appropriate remedial action is undertaken.

Top operational risks and strategic risks are regularly evaluated and updated by each group director to ensure current and emerging risks are identified and mitigated as appropriate. Further details are outlined in the Governance Statement on pages X to X.

Enterprise risk is regularly reported and discussed at the Enterprise Risk and Credit Committee (ERiCC) and to the Risk Committee every quarter, providing reports on the key risks and the effectiveness of risk management in UKEF.

Enterprise Risk Management Principles

UKEF senior management has a responsibility to ensure that the appropriate risk management principles, culture and behaviours are embedded in day to day business activities, policies and procedures. Sound risk management is underpinned by an effective and robust risk culture which is embedded in UKEF's 3 lines of defence model.

The UKEF Enterprise Risk Management Principles support our approach and ongoing application of risk management within our business. The principles are:

- Proactive, not reactive
- Ownership of risks by the relevant division
- Risk Management is embedded in day to day processes
- Robust and responsive to change
- Assists in the achievement of UKEF strategic objectives

Assurance across UKEF

The UKEF Assurance Framework is a key component of the UKEF Enterprise Risk Framework and is coordinated by the Enterprise Risk Division. It seeks to provide reliable assurance (evidence) to the Chief Executive and ERiCC on organisational stewardship and the management of major UKEF risks by sample testing and examining key controls detailed in the risk and control assessments and validating statements made in the control environment certificate (CEC) self-certification process. This key assurance process commenced in the last quarter of the 2019-20 financial year and be fully embedded in UKEF during 2020-21.

The CEC is a half-yearly process. It requires Executive Committee members and their senior management teams (typically divisional heads) to provide an assurance assessment and self-certification to the UKEF Chief Executive regarding the management of Operational Risk within their area of responsibility. Furthermore, at the end of the financial year, each Executive Committee member is required to complete a self-assessment of their directorate's compliance with key business processes as well as a governance statement. All self-assessments are completed using a consistent and comparable rating mechanism.

Financial Risk

Credit risk is the most significant source of financial risk for UKEF. Its management is a core competency for the department, which is reflected in our credit risk management framework and operates at every level of the department. The definitions of financial risk are set out in the table below.

UKEF's financial risks

Credit risk: the risk of financial loss if an obligor or counterparty to which we have financial exposure fails to meet its contractual obligations.

Market risk: the risk of losses arising from change of market prices, such as fluctuations in foreign currency exchange rates and interest rates.

Liquidity risk: the risk that we are not able to meet our financial obligations when they fall due or can only do so at excessive cost. Considered low because UKEF’s status as a government department enables us to access the Consolidated Fund.

Financial objectives and appetite

UKEF’s financial objectives, set by HMT, are designed to enable it to fulfil its mandate of supporting UK exporters while ensuring that credit risk and pricing:

- are undertaken on a basis that UKEF should receive a return adequate at least to cover the cost of the risks it is assuming
- do not expose the taxpayer to the risk of excessive loss.

UKEF's credit risk and pricing is governed by 6 financial measures:

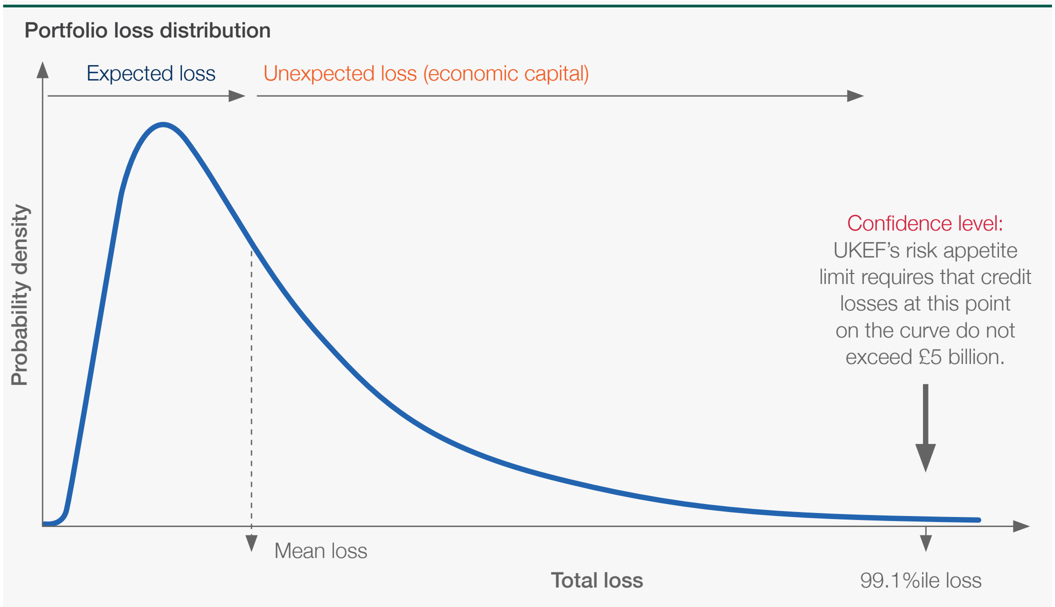
1. Maximum commitment: the total amount of nominal credit risk exposure that the department may incur. This is set at £50 billion[3]
2. Risk appetite limit: a form of economic capital limit of £5 billion (detailed further in the next section)
3. The Exposure Management Framework (EMF): a limit to exposure of £5 billion for any individual market, with reducing capacity as the risk profile increases (detailed further on page 66)
4. Reserve Index: an index that measures whether UKEF has accumulated, over time, sufficient revenue to cover its possible credit losses at the 77.5 percentile on our portfolio loss distribution[4]
5. Pricing Adequacy Index: detailed under pricing policies on pages 72 to 75
6. Premium to Risk Ratio: detailed under pricing policies on pages 72 to 75

The 2019-20 outturn against all our financial objectives is presented on page 31.

The credit risk policy, the pricing methodology and the exposure management framework are the main policies that apply to the management of credit risk within UKEF. Policies are generally reviewed annually – EMF is tri-annual – by the ERiCC and subsequently endorsed by the Risk Committee.

Economic capital and the risk appetite limit

Economic capital (often referred to as capital at risk or CaR) is a measure of risk based on potential future losses. It can be considered as a buffer to cover unexpected losses over a defined future period at a specified confidence level. The chart below illustrates this concept for a hypothetical portfolio of credit risks.



Expected loss is a calculation of anticipated average loss over a defined period based on historical experience. Expected losses essentially represent a 'cost of doing business', implying that when a financial institution assumes credit risk, it should always seek to

3 This limit is set under the HM Treasury consent. The Maximum Commitment and Risk Appetite Limit are no longer subject to adjustments due to exchange rate movements.
4 The reserve index means the ratio of (a) cumulative reserves plus associated provisions to (b) the aggregate of the value of the 77.5 percentile point on UKEF's portfolio loss distribution plus provisions. At the end of each month, the index must be at least 1.

charge an amount at least sufficient to cover the expected loss associated with the relevant loan, guarantee or insurance policy.

Unexpected loss accounts for the potential for actual losses to exceed expected losses, reflecting the uncertainty inherent in the calculation of future losses. Calculations of unexpected loss will tend to increase if a portfolio has high risk concentrations and/or the risks in the portfolio are strongly correlated. UKEF defines unexpected loss as the difference between the portfolio expected loss and the 99.1% value of the loss distribution. (Other financial institutions often consider this to be their economic capital requirement.)

The risk appetite limit set by HMT means that UKEF must manage its credit risk-taking activities such that total losses, as modelled by our portfolio risk management simulation model, will not (with a 99.1% degree of certainty) exceed £5 billion. In other words, at no time should portfolio expected loss, plus provisions against claims already paid, plus portfolio unexpected loss, exceed £5 billion.

Credit risk approach

This sets out the high-level policies and processes used for assessing, measuring, managing and reporting all categories of credit risk to which UKEF is exposed. It establishes minimum risk standards and ratings-based exposure review points.[5] A series of more detailed risk management policies, frameworks and individual risk methodologies sits underneath the credit risk policy.

Exposure management framework

Our Exposure Management Framework (EMF) sets individual country limits based on the following key principles:

- countries with higher levels of credit risk, assessed through individual country reviews using a ratings-based approach, will have lower limits
- the larger a country's economy (as measured by its GDP), the higher the potential country limit (subject to other factors)
- country limits should be set relative to the notional financial resources available to UKEF and consistent with UKEF meeting its financial objectives
- the upper boundary for exposure to any individual country is £5 billion; in very exceptional circumstances, this can exceed £5 billion where the UKEF Chief Executive has been instructed otherwise by a ministerial direction

The ERiCC systematically reviews UKEF's country limits and cover policy. In addition, it sets individual controls on a case-by-case basis within each country limit. Risk and cover policy are assessed and decided for around 200 overseas markets, prioritised based on the size of existing exposures, the assigned credit rating and active, potential new business requirements.

5 The only time when UKEF's internal risk policies might not apply would be if ministers (having regard to the national interest) gave a written direction to the Accounting Officer requiring a specific credit risk to be underwritten. In these circumstances, the credit risk in question would be handled differently, and accounted for under Account 3.

Country risk assessment

We assess each country in which we have an actual or potential credit exposure and use this to produce a credit rating, from AAA (highest) to D (default, lowest). Our risk assessment framework is aligned with that used by Standard & Poor's (S&P) but is additionally informed by a range of external materials, as well as cross-Whitehall forums, local UK diplomatic representatives, triannual OECD[6] country risk expert meetings, and country visits, where appropriate.

Where no external credit rating exists, we typically derive our final letter rating from a World Bank shadow-rating model supplemented by analyst judgement and peer comparisons. In all instances, credit ratings will be reviewed and approved (as appropriate) by the ERiCC.

Corporate, bank and project finance risk assessment

Risk assessments for the majority of our medium to long-term credit exposure to overseas corporates and banks are principally based on S&P methodologies.

We use a number of S&P credit rating templates from which to base our risk assessments on our principal areas of business. This includes specific rating templates with appropriate credit risk factors for passenger airlines, operating lessors, large corporates, SMEs, project finance, banks and non-bank financial institutions.

For each transaction, these rating templates are used in conjunction with an analyst's detailed assessment of the key factors affecting the obligor's business and financial risk profiles, and consideration is also given to factors that the rating templates may not consider explicitly, such as governance and liquidity. Further, this approach is supplemented by S&P derived models that assess the likelihood of government or parental support, which is also considered in the final rating of the obligor. Where relevant, Moody's industry-specific methodologies are used as benchmark rating tools. Additionally, final ratings are benchmarked against industry peers.

For our trade finance business, which typically involves small and medium-sized enterprises (SMEs) and relatively small individual credit risk exposures, we have purpose-built a number of credit assessment methodologies with shorter turnaround times for certain categories of risk. For example, we have adopted a specific credit assessment and approval process for our bond support and export working capital facilities, under which UKEF shares risks with financial institutions for the provision of working capital loans and on-demand contract bonds in support of export transactions.

Similarly, a bespoke credit assessment process has been developed to handle the payment risks that arise under export insurance, and the credit and political risks covered by bond insurance.

From 1 November 2019, UKEF has introduced explicit commentary on environmental, social and governance risk into all non-sovereign credit risk assessments and all sovereign analysis when setting limits.

6 The OECD Arrangement, sometimes referred to as 'the Consensus', limits self-defeating competition on export credits among members of the OECD. OECD members undertake to operate within these guidelines when providing official support for export credits of 2 years or more.

UKEF's credit risk methodologies

Product category	Product	Description	Credit risk party	Credit risk methodology
Credit insurance	Export insurance policy	Covers risk of non-payment under an export contract due to specified commercial and political risks	Overseas buyer	Bespoke UKEF methodology
	Bond insurance policy	Covers unfair calling of contract bonds, or fair calling due to specified political events	Overseas buyer	Bespoke UKEF methodology
Loan/capital market guarantees	Buyer credit facility	Guarantees medium/long-term finance from lenders or capital market investors provided to overseas buyers of UK goods/services	Overseas buyer	S&P methodologies
	Supplier credit facility			
	Lines of credit			
	Export refinancing facility	A buyer credit provided with an undertaking to support refinancing of the bank loan through the capital markets	Overseas buyer	
Trade finance	Bond support scheme	Guarantees contract bonds provided by private lenders	UK exporter	Bespoke UKEF methodology
	Export working capital scheme	Guarantees working capital loans provided by private lenders to UK exporters	UK exporter	Bespoke UKEF methodology
	Letter of credit guarantee scheme[7]	Guarantees for banks that confirm letters of credit issued in favour of UK exporters	Overseas issuing bank	S&P bank rating methodology
Lending	Direct lending facility	Medium/long-term loans from UKEF to overseas buyers of UK goods/services	Overseas buyer	S&P rating methodologies
Investment insurance	Overseas investment insurance	Insures overseas assets of UK exporters against specified political risks	Overseas buyer and its sovereign	Bespoke UKEF methodology

7 This product was withdrawn in April 2020.

Credit risk assessment outputs

Expected loss is a key measure of credit risk at UKEF and is central to our pricing methodologies and our underwriting fund accounting.[8] Our credit risk assessments are used to indicate the 3 components of expected loss:

Expected Loss

Probability of default (%) × Loss given default (%) × Exposure at default (£) = Expected loss (£)

We assign a rating (from AAA to D) to all credit risks within UKEF to denote an associated probability of default. The probabilities are updated at least annually in line with the latest S&P statistics.[9]

Our credit risk assessments also provide an estimate of loss given default: how much we stand to lose if an obligor defaults, expressed as a percentage. Corporate and Project Finance loss given default assessments are conducted on a case-by-case basis, considering the specifics of the transaction in question, including security, priority ranking, recovery prospects by market and likelihood of restructuring, sale or liquidation.

In the case of sovereign risk, persistence of default is also included in the calculation of potential loss. Based on empirical research, persistence of default (the predicted duration of a country's default) is calculated as a function of its per capita income, the severity of its indebtedness and whether the default is a liquidity event or an insolvency.

The third output of our assessments is exposure at default, meaning the credit risk exposure we have at the time of default.

Another measure of credit risk we monitor closely is unexpected loss, which is integral to our credit risk appetite (see 'economic capital and the risk appetite limit' on pages 65 to 66).

Risk concentration and correlation

Given UKEF's role, it is almost inevitable that our credit portfolio will have risk concentrations. Consequently, portfolio modelling (particularly the impact on unexpected loss) plays an important role in helping to determine the maximum amount of credit exposure UKEF might assume on a single obligor or group of related obligors.

For any given case, our modelling will seek to account for the likely correlations between risks in the portfolio. ERiCC will only consider approving a case or making a positive recommendation to the Chief Executive if it is satisfied that a given level of credit exposure calculated using this modelling will not threaten any of the department's financial objectives.

8 Expected loss applies both at an individual transaction level and at a portfolio level. At a portfolio level, it is simply the sum of the expected losses of all risks in the portfolio and equates to the mean of the portfolio loss distribution.

9 UKEF subscribes to S&P Global's CreditPro database that provides a strong statistical foundation to assess ratings migration and default rates across geographical regions and industry sectors.

Portfolio modelling is one of a number of measures in place to manage risk concentrations. In addition:

- individual exposures within a country must not in aggregate exceed the country limit, as established under our exposure management framework
- UKEF may not give a single commitment in excess of £200 million without the agreement of HMT
- periodic reviews of single obligor, sector and regional/geographic concentration risks are undertaken

Further work is being undertaken to refine risk appetite measures in respect of individual counterparties, sectors and geographies.

Practical means of reducing risk concentration include reinsurance and counter-guarantees from the private (re)insurance market, as well as, from other ECAs. UKEF may seek (re)insurance when it is acting as lead ECA in a transaction where goods/services are sourced both from the UK and from other countries.

Active portfolio management

UKEF's risk management strategy aims to reduce concentrations of risk in its portfolio to decrease the likelihood of idiosyncratic losses, and/or free up headroom in country limits to support more UK exporters. Under the active portfolio management (APM) program, UKEF can buy facultative reinsurance from the private market, subject to cost-benefit analysis and positive value for money. During 2019-20, UKEF successfully placed around £400 million of risk in the private reinsurance market, primarily aimed at addressing portfolio concentrations in the Africa and Middle East region across a variety of sectors.

Credit processes and reporting

All material credit risks must be approved by the Chief Executive, the ERiCC or a designated member of the Risk Management Group with the appropriate delegated authority. Once approved, credit exposures are regularly monitored and reviewed at both portfolio and individual transaction level.

The ERiCC oversees portfolio-level monitoring. This includes stress testing and scenario analysis every 6 months, and a monthly review of portfolio movements, particularly focusing on exposure, expected loss and unexpected loss changes. Monthly management information reports the performance of the credit portfolio against our financial objectives. We also monitor monthly whether exposures are within the agreed country and other limits.

At a transactional level, we regularly update the ratings allocated to countries and individual obligors. UKEF maintains 'watch lists' of obligors whose credit risk is materially deteriorating; if the credit of a non-sovereign borrower deteriorates such that UKEF might expect to pay out under a guarantee or insurance policy, the case will be managed by a dedicated unit.

Post Issue Management

Once an exposure is declared "effective", it is handed from the Business Group teams to the an in-house Post Issue Management team, which reviews and monitors cases on an ongoing basis until maturity.

Amendments, waivers and compliance with documentation are monitored with the help of the agent functions of the lending banks. Requests for waivers and amendments are considered on a case-by-case basis through a chain of delegated authorities and reported to senior management.

The Claims and Recoveries Unit

Claims and Recoveries are an integral part of the Risk Management Group, examining Claims, admitting liability and, if valid, paying out to customers. In addition, the C&R team is responsible for Recoveries, undertaking recovery actions, recouping amounts due from debtors and minimizing risk for UKEF. The Claims and Recoveries unit submits regular reports to the ERiCC on all accounts it is responsible for and seeks approval for its recovery actions. Once a claim has been paid, the unit makes provisioning recommendations to the ERiCC on a case-by-case basis, with a full provisioning exercise conducted at the end of each financial year. This exercise is discussed in detail and agreed with UKEF's external auditors.

Sovereign defaults that lead to debt renegotiations through the Paris Club[10] are managed by a team within the CFOO's Group that specialises in rescheduling, working in conjunction with HMT. Paris Club developments are monitored by the Enterprise Risk and Credit Committee, which must approve any provisions made against this exposure.

The process of recovery through Paris Club rescheduling is often protracted; a number of still active reschedulings relate to exposure principally incurred prior to 1991.[11]

UKEF helped Devon-based Green Resource Engineering secure a £1.1 million order from South Korea for a water-cooling system

10 The Paris Club is the informal group of official creditors that seeks to establish coordinated and sustainable solutions to debt service difficulties experienced by debtor countries.
11 This was the year in which the Insurance Services Group was privatised.

Pricing policies

Context

On the principle of maintaining a 'level playing field', the OECD Arrangement requires ECAs to charge risk-based premiums that are sufficient to cover their long-term operating costs and credit losses. This mirrors the provisions of the WTO Agreement on Subsidies and Countervailing Measures, which classifies export credit guarantee programmes that do not cover their long-term operating costs and losses as 'prohibited subsidies'.

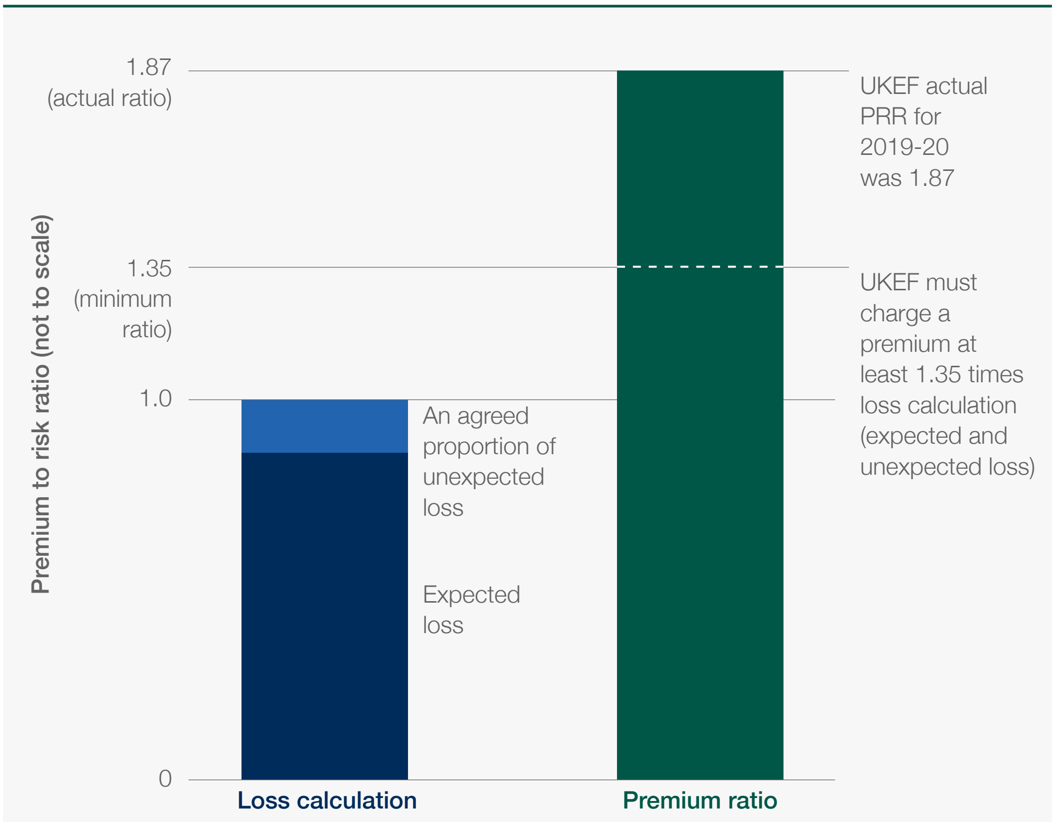
Financial objectives

Consistent with these principles, HMT has set UKEF 2 financial objectives designed to ensure, as far as practicable, that the premium rates we charge reflect the risk taken on and are sufficient for us to operate at no net cost to the taxpayer over time.

Premium-to-risk ratio (PRR)

Firstly, the premium-to-risk ratio states that, each month, we must demonstrate that the premium charged on the business issued, or forecast to be issued in the financial year, will be at least 1.35 times greater than an agreed level of expected and unexpected loss corresponding to those transactions as measured at the time of pricing.

The ratio at 31 March 2020 was 1.87 against the 1.35 ratio minimum.

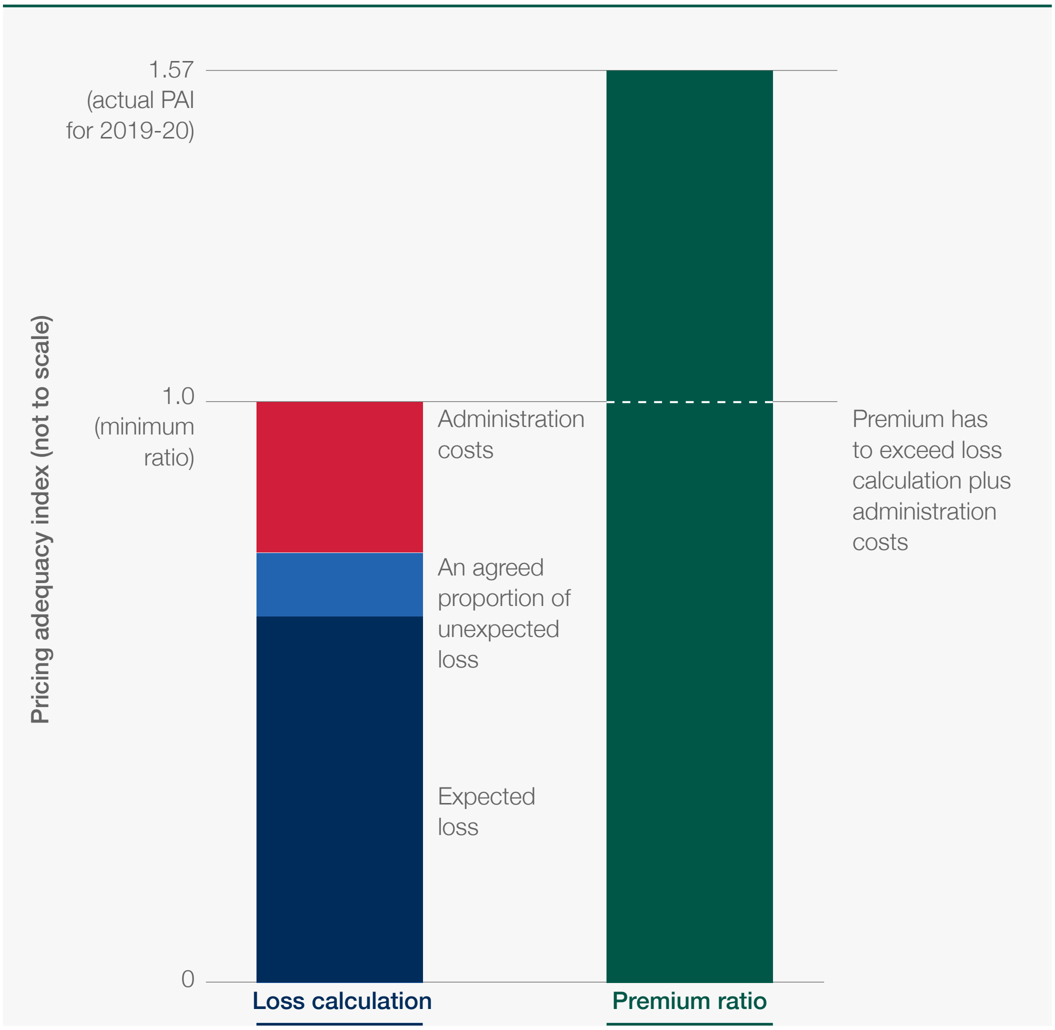


Pricing adequacy index (PAI)

The second objective set out by HMT is the pricing adequacy index. Whereas the premium-to-risk ratio serves purely as an annual measure, the pricing adequacy index considers a 3-year time scale, applied across 3 accounting periods:

- the 2 previous and the present financial years
- the previous, current and next financial years
- the present and the next 2 financial years

For each period, UKEF must demonstrate that the actual/forecast premium will cover and exceed the 'cost of doing business', meaning administration costs and an agreed level of possible losses. The ratio for the past 2 years and the present financial year was 1.57 against the minimum of 1.0.



Forecasting approach

Business and premium forecasts are based on the judgements of our underwriters who draw on available transaction pipeline information, market intelligence and the estimated likelihood of transactions materialising within the current or future financial years. In addition, we perform regular sensitivity analysis to supplement these 'central' forecasts and to test the robustness of forecast financial performance against the agreed premium-to-risk ratio and pricing adequacy index targets.

UKEF Export Finance Manager Anne Lockett speaking to Petford Tools MD Melvin Sinar. Support from UKEF enabled the Dudley-based firm to double its staff

Pricing methodology

We set risk-based premium rates for all of our products using pricing methodologies and parameters that are reviewed annually by the ERiCC, endorsed by Risk Committee and agreed by HMT.

UKEF aims to support UK exporter competitiveness. It is, therefore, our policy that we set the lowest tenable premium rates, subject to the following:

- premium rates may not undercut the minimum rates set out by the OECD (where applicable) and must comply with our international obligations, including state aid rules
- no individual premium can be below the expected loss of the associated transaction
- aggregate premiums must satisfy the premium-to-risk ratio and pricing adequacy index objectives

In practice, the vast majority of medium and long-term transactions are priced at the minimum rate permitted under the OECD Arrangement.

Portfolio modelling

UKEF uses its own portfolio risk simulation model (PRISM) to undertake all portfolio-level credit risk modelling and to produce portfolio loss distribution curves. The model is also used to carry out stress testing, and to simulate the extent and timing of potential gross cash outflows as a result of claims payments, to inform cashflow forecasts and liquidity management.

Modelling assumptions

PRISM operates under a range of assumptions, including correlation matrices and credit default behaviour. It is essential to keep these assumptions as up-to-date and as robust as possible. We do this through a regular review process, with each assumption fully checked on a minimum 3-year cycle. Each review is accompanied by a report to ERiCC, with recommendations for action as appropriate. Examples of assumption reviews in 2019-20 include:

- Persistence of default. This is the time it will take for each sovereign, in the event of default, to exit default. This has a significant effect on our valuation of sovereign exposures. We investigated industry-best-practice and the latest evidence and confirmed that we did not need to change our approach
- Application of correlation assumptions. This review identified an effect causing overly high correlation levels within certain segments of the portfolio. In order to align with empirical evidence and industry-best-practice, we designed and implemented a solution that constrained the simulated risk to better match the underlying assumptions, following approval by ERiCC

Stress testing and scenario analysis

UKEF's policy is to undertake extensive stress testing of its credit portfolio. Stress testing assesses the impact of various adverse scenarios and is conducted every 6 months.

These scenarios are designed to reflect potential emerging risks and may vary in each exercise but may include, for example, a general emerging markets crisis or an extended period of very low oil prices. They generally involve simulating:

- rating downgrades
- increases in loss given default
- a series of large individual defaults
- a combination of downside scenarios

The ERiCC reviews the results of the analysis and particularly considers the impact of each stress/scenario on the value of the 99.1% point of the portfolio loss distribution, relative to the risk appetite of £5 billion.

To complement existing stress testing and scenario analysis, in 2018-19 UKEF introduced reverse stress testing. Instead of quantifying the impact of scenarios on UKEF's portfolio, reverse stress tests identify the specific portfolio parameters (such as individual risk ratings and loss given default assumptions; and industry and geographic correlations) required to breach our portfolio limits and assesses events and circumstances that would cause our business model to become unviable and to design strategies to mitigate the risk of such business failure.

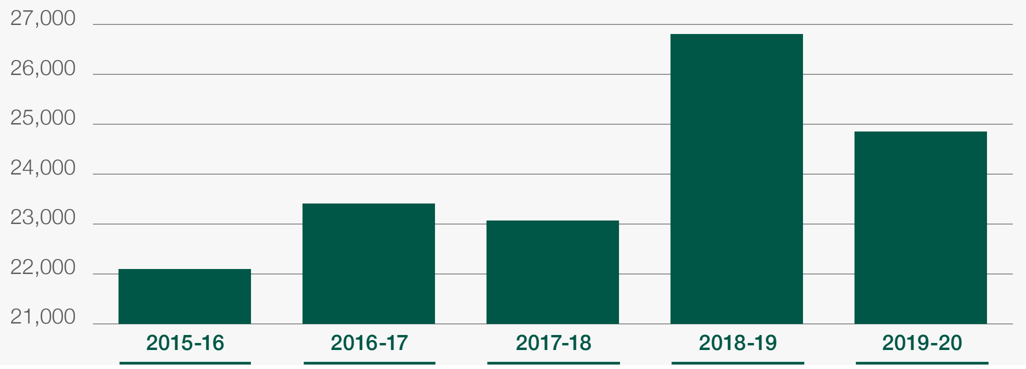
Credit risk performance 2019-20

In 2019-20, we were again fully compliant with all our financial objectives relevant to the credit portfolio. A full summary of performance against financial objectives is reported on page 31.

- total exposure including commitments and legacy Account 1 exposure decreased from £26.8 billion to £24.9 billion[12] – the decrease being due to run-off of existing exposure and foreign exchange movements exceeding the new business written
- UKEF's portfolio of risks remained stable in terms of sector concentrations, while regional concentrations increased in the Middle East and Africa and the overall credit quality decreased slightly. However, the portfolio remains well within the maximum commitment limit and risk appetite limit
- stress testing and scenario analysis shows that UKEF's portfolio remains resilient and should continue to meet its financial objectives even in a number of extreme scenarios
- UKEF's active portfolio management programme successfully placed 1 tranche in the private reinsurance market, reducing portfolio concentration in Africa, the Middle East and certain single obligors
- expected and unexpected loss rates increased, but we experienced a very low level of claims paid (see section on page 82)

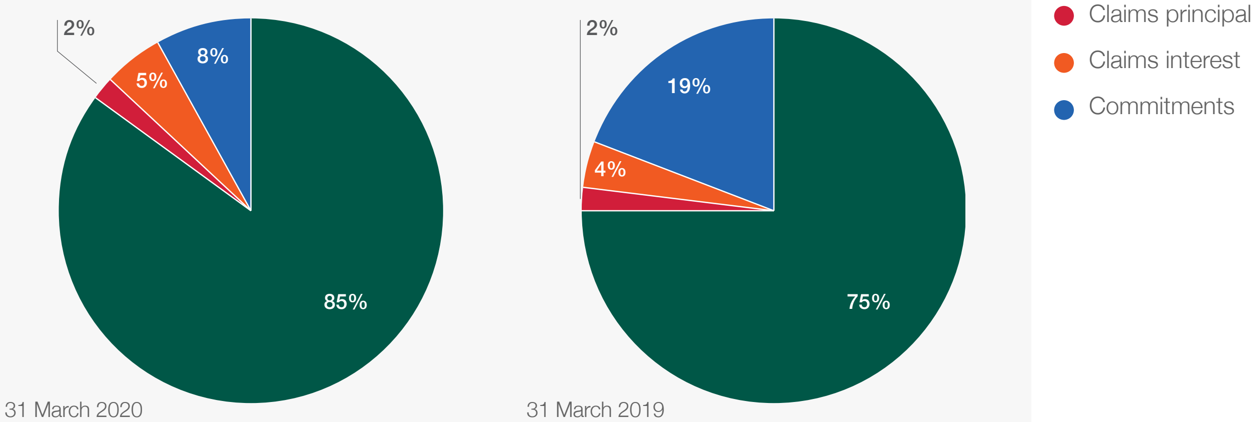
12 This, and all data that follows in this section, is net of Account 3.

Credit risk exposure at year-end (£m)



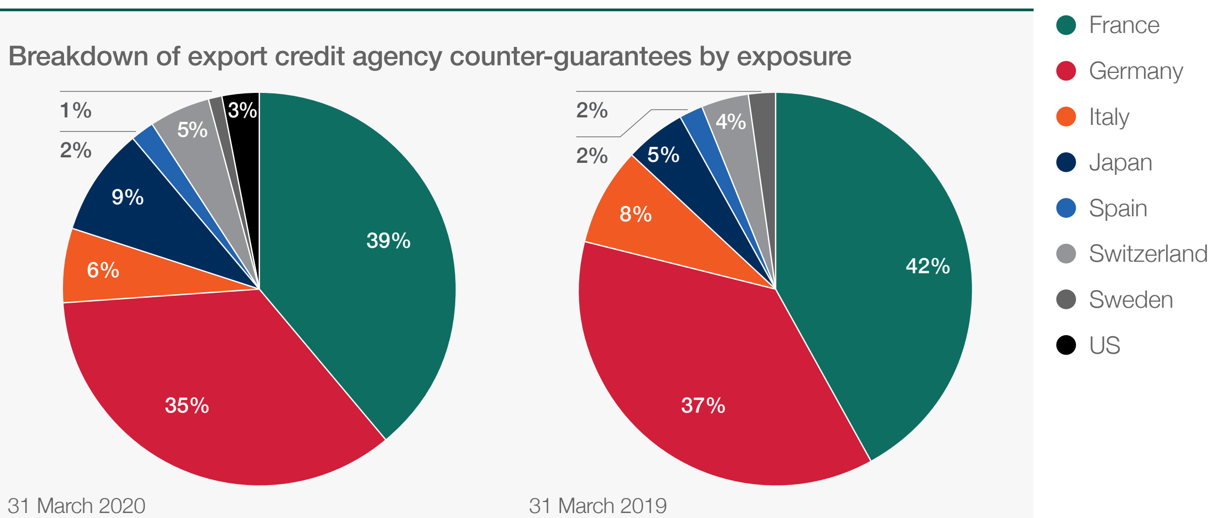
The charts below show the breakdown of this exposure between AAR, claims (principal and interest) and commitments.[13]

Breakdown of total exposure



At 31 March 2020, total AAR amounted to £21.1 billion (£20.0 billion in 2019). This figure includes £3 billion of counter-guarantees provided to UKEF by other European ECAs (£3.8 billion in 2019), principally related to Airbus business, and £1.1 billion of private reinsurance used to manage risk concentrations in our portfolio (£0.9 billion in 2019).

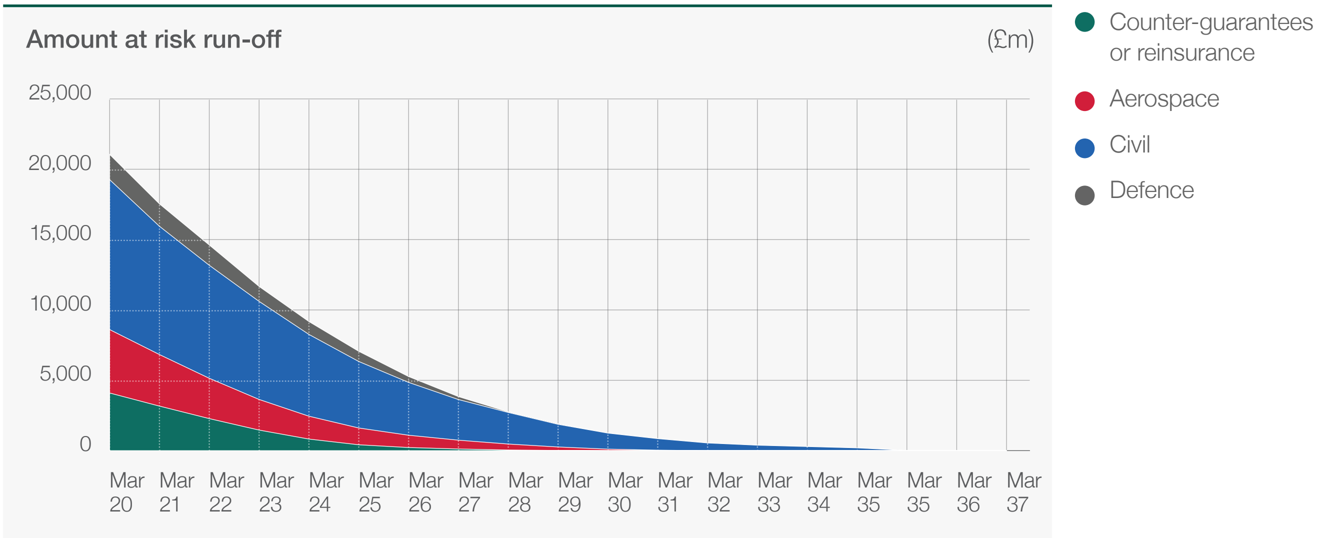
Breakdown of export credit agency counter-guarantees by exposure



13 Commitments are cases not yet the subject of an issued and effective guarantee, but for which UKEF has communicated its intention, before a specified date and subject to conditions, to provide support.

Horizon of risk

The vast majority of our credit exposure is made up of medium to long-term finance. The chart below illustrates how our current portfolio is expected to run off over time in terms of overall AAR. Over the next 12 months, around 17% will run off, with around 56% of the current portfolio expiring within 4 years.



Risk concentrations

Context

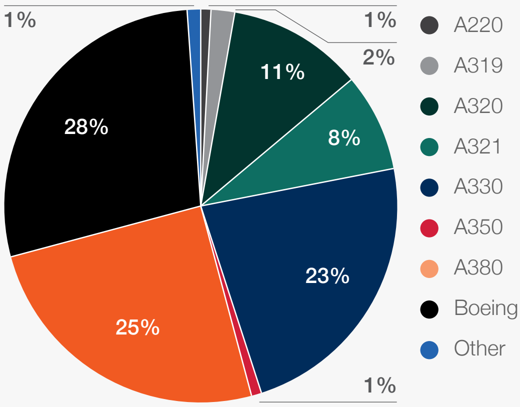
Our credit portfolio is dominated by long-dated emerging market risk, consistent with our role as the UK's official ECA. We are limited in our control over the geographic or sectoral composition of our portfolio, as we assume credit exposure in line with the needs of UK exporters rather than in the pursuit of a well-balanced portfolio.

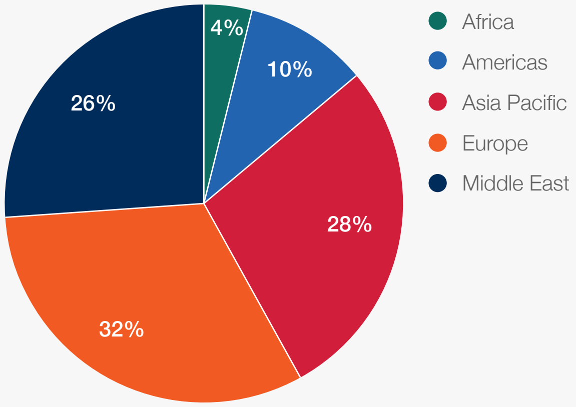
Sectors

UKEF's largest risk concentration remains in aerospace, accounting for 27% of the AAR (net of ECA reinsurance/counter-guarantees) as at 31 March 2020 (32% for 2019). This sector has been significantly impacted from the consequences of the current COVID-19 crisis and resulting travel restrictions. As a result we have seen negative rating migration in this portfolio. The UKEF aerospace portfolio remains nonetheless well diversified across airlines and aircraft-leasing companies, aircraft type and geographical region, detailed below. Actual exposure is down year-on-year given run-offs and reduced levels of new business written during this financial year. Exposure is likely to rise again in 2020-21 as a result of the impact of COVID-19.

The majority of aerospace exposure is secured on the underlying aircraft.[14]

Aerospace exposure by aircraft type and geography





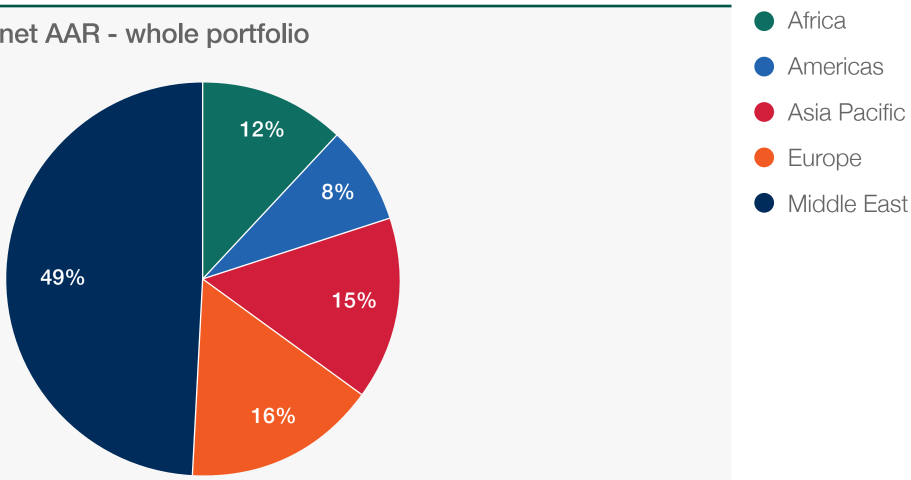
At 31 March 2020, UKEF had £2.6 billion credit exposure to commercial real estate, representing 22% of our overall AAR (net of export credit agency reinsurance/counter-guarantees), mainly in the Middle East. Other sector concentrations were to the gas and power industry (£3.6 billion AAR) and the chemicals industry (£1.7 billion AAR), spread across the Middle East, Asia and South America.

Geography

As of 31 March 2020, the Middle East accounted for 49% of our net AAR portfolio. The majority of this resulted from support of UK exports to Oman, Dubai, Iraq and Saudi Arabia.

Asia Pacific accounted for 15% of net AAR, with around £1.2 billion attributable to civil aerospace business with a number of airlines. In the Americas, around £0.5 billion of exposure was attributable to the aerospace sector, and the remaining exposure largely centred on Brazil.

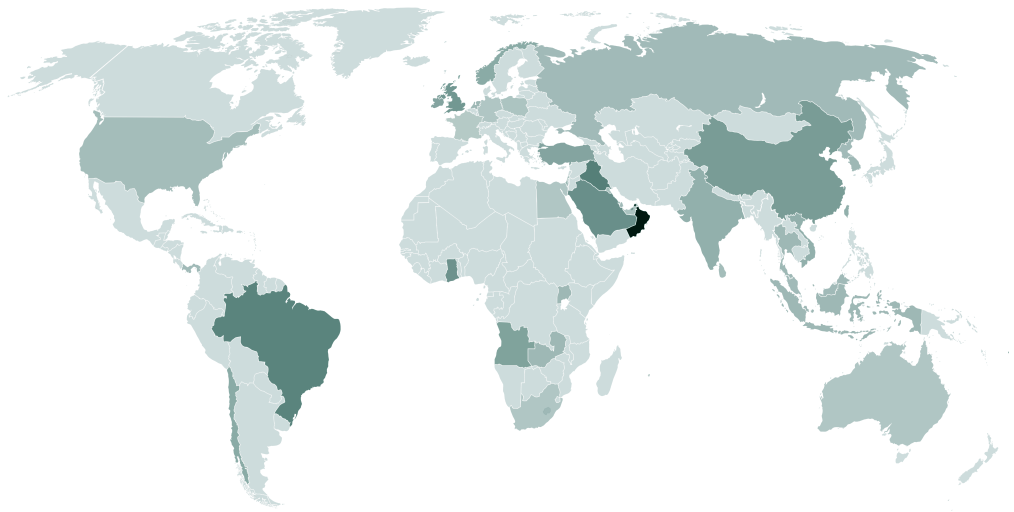
Regional breakdown of net AAR - whole portfolio



14 This means that UKEF can take possession of aircraft from defaulting airlines. Following the 9/11 terrorist attacks, we took possession of, leased and eventually sold 44 aircraft, ensuring a minimisation of losses both to the airline industry and UK taxpayer during this difficult period.

Global AAR at 31 March 2020

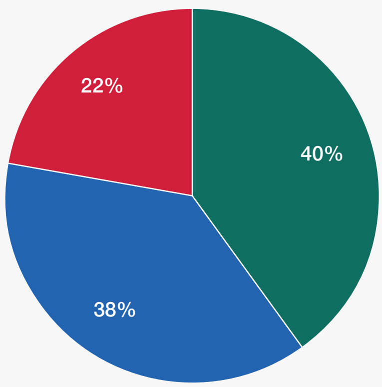
Darker shading indicates higher AAR



Credit quality

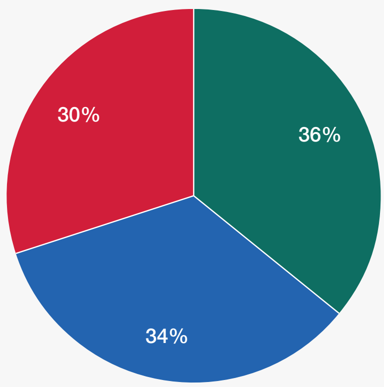
The most notable change regarding the credit risk quality of our portfolio in 2019-20, concerns the increase in the B+ or below segment. As at 31 March 2020, 40% of AAR (net of reinsurance) was rated B+ or below by UKEF (compared to 36% in 2019). This increase was in part due to new business issued in the year and in part due to a few rating downgrades in relation to existing transactions.

Net AAR by rating



31 March 2020

Net AAR by rating

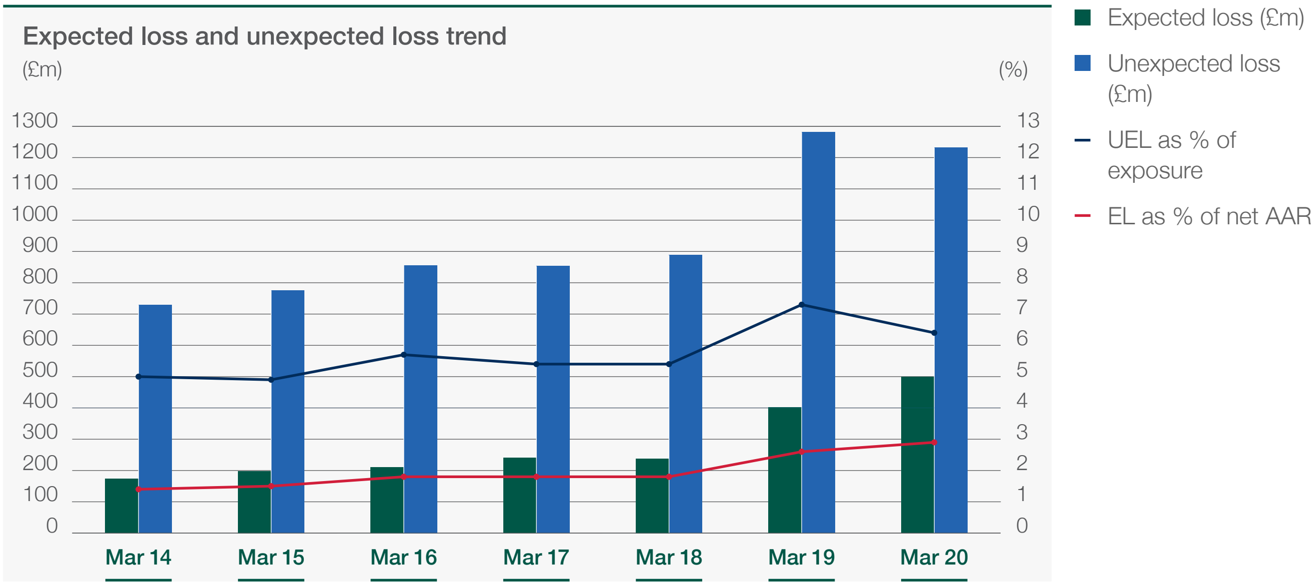


31 March 2019

- B+ or below
- BB+ to BB-
- Investment Grade

Portfolio expected loss increased, from £402 million to £499 million, representing 2.9% of AAR (net of reinsurance). This movement is consistent with an increased AAR and is also, in part, a reflection of the increase of AAR rated B+ or below by UKEF.

Portfolio unexpected loss decreased slightly to £1.2 billion as of 31 March 2020, from £1.3 billion in 2019, representing 6.4% of total exposure (7.3% in 2019). This decrease is in part due to the application of revised correlation assumptions, as indicated on page 73.



Risk appetite limit

The projected portfolio loss to the 99.1 percentile has remained at around £2 billion and is still comfortably below the financial objective limit of £5 billion set by HMT.

Portfolio stress testing

UKEF conducts an exercise twice a year to analyse the impact of shocks on its portfolio of exposures. These are split between specific political and economic scenarios - such as a crisis in the Middle East or a collapse in oil prices - and more generic shocks, such as a 3-notch rating downgrade of sovereigns and corporates across the board or the default of major counter-parties. While our modelling framework is based around UKEF's current underlying assumption that the Covid-19 pandemic will be of moderate size, duration and intensity, under which scenario UKEF firmly remains within its Risk Appetite Limit, we have also modelled the portfolio, among a number of other scenarios, on the basis of a severe and prolonged global pandemic. Under this very extreme modelling scenario, undertaken to the 99.1% point on the loss distribution curve, UKEF, not surprisingly, does breach its Risk Appetite Limit (to £6.6bn versus its £5bn limit). We continue to monitor the risk environment to ensure that our existing scenarios are revalidated and updated as necessary and new bespoke scenarios are designed as appropriate.

While rating migration across the UKEF portfolio has historically been relatively modest, the effects of COVID-19 have begun to accelerate this trend with rating downgrades in the aero and real estate portfolios in particular. This trend is expected to continue depending upon the severity and longevity of the pandemic.

New claims paid in the year

Whilst UKEF experienced an increased number of claims paid over the prior year (across 7 counterparties compared to 1 in 2018-19), in absolute terms and relative to the size of the portfolio, the quantum of claims remained low during the course of 2019-20. The increase in numbers did not reflect any specific sector or country trends but did signal a turning of the economic cycle (pre-COVID). The level of new claims is mitigated by rigorous credit risk assessments, thorough underwriting and structuring of transactions, and risk management standards more generally. The degree of concentration by counterparty in UKEF's portfolio can lead to lumpiness in the timing and quantum of claims being realised. The level of claims is expected to be cyclical.

Outstanding claims paid and provisions

The bulk of outstanding claims paid and still to be recovered by UKEF arose on business issued and defaulting prior to 1991. Almost all of the £1.41 billion (down from £1.44 billion in 2019) of outstanding claims paid on this business refers to sovereign exposure that is subject to Paris Club rescheduling, the most significant part of which is for Sudan (including a substantial amount due to accrued interest).

The overall provision amount for this business decreased slightly on 31 March 2020 to £1.15 billion (down from £1.17 billion in 2018-19).

Outstanding claims paid on Account 2 from business issued after 1991 has reduced slightly in the year to £347 million at 31 March 2019 (down from £360 million in 2018-19) in line with scheduled Paris Club repayments overtaking increases in accrued interest. Sovereign exposure in Zimbabwe and Indonesia (the latter rescheduled at the Paris Club and performing in accordance with the agreed rescheduling) makes up the majority of this. Historical aerospace claims have now completed paying down in accordance with agreed rescheduling.

Recoveries

Overall recoveries (on all business, both principal and interest) amounted to £102 million as at 31 March 2020 (£100 million in 2018-19), reducing total recoverable claims (excluding interest on unrecovered claims) to £590 million (£647 million in 2018-19). The majority of recoveries (£92 million) were made through the Paris Club and related to historical sovereign debt reschedulings. Recoveries from a number of corporate names made up the balance.

Market risk management

Context

Market risk is the risk of losses caused by movements in market prices. For UKEF, this arises from changes in interest rates and foreign exchange rates.

UKEF's principal exposure to interest rate movements is through its legacy fixed-rate export finance scheme, which was closed to new business in 2011.

Foreign currency risk arises from 2 main areas:

- **transaction risk:** the risk of changes in the value of foreign currency interest receipts on conversion into sterling
- **translation risk:** the risk that UKEF's statement of financial position and net operating income will be adversely affected by changes in the sterling value of assets denominated in foreign currency, and by liabilities from changes in foreign currency exchange rates

Interest rate risk

Fixed-rate export finance (FREF) scheme

Until 2011, UKEF operated a fixed-rate export finance scheme, under which it supported medium and long-term fixed-rate lending by commercial banks at internationally agreed 'commercial interest reference rates' (CIRRs) to overseas borrowers.

The lending banks funded the loans at floating rates (LIBOR plus a margin). Through 'interest makeup' arrangements, UKEF made up the difference when the lender's floating rate was more than the applicable CIRR. When the floating rate was less than the applicable CIRR, the lender paid UKEF the difference. This system exposed UKEF to interest rate risk.

Before closing the scheme in 2011, UKEF pursued an active interest rate hedging policy, eliminating, as far as possible, its exposure to interest rate risk via a portfolio of matching interest rate swaps. These interest rate swaps remain in place, reducing in line with the amortising profile of the loans themselves.

HMT no longer applies a quantitative financial objective addressing this legacy portfolio. Also, given the substantially matched position of the interest make-up arrangements and the interest rate swaps, no new hedging activity has been undertaken since 2011, nor is currently planned for the future.

Internal policies in relation to active hedging have been discontinued. Nevertheless, we monitor the financial position of the scheme and its residual interest rate risk closely.

The portfolio is valued on a daily basis with its profit and loss performance measured against a series of internal limits. Movements in excess of these limits are immediately reported to the CFOO and the ERiCC for appropriate action. No such excess movements occurred in 2019-20.

These arrangements, along with several other reporting provisions relating to the scheme, are approved annually by the ERiCC. Periodic sensitivity analysis is carried out on the portfolio to gauge the financial impact of interest rate movements on UKEF.

Due to portfolio run-off, the amounts involved in the FREF scheme are immaterial.

Direct lending

In 2014, UKEF introduced a Direct Lending Facility. This provides loans to buyers of UK goods and services at the Commercial Interest Reference Rate (CIRR). UKEF is not charged interest by HMT on the funding provided to it for making these fixed-rate direct loans. Consequently, movements in interest rates during the life of the loans do not affect the financial performance of our direct lending activities.

To ensure that interest earned on each CIRR-based direct loan adequately covers the government's borrowing costs, a check is made prior to commitment that confirms that the sterling CIRR applicable to the direct loan is higher than the corresponding National Loans Fund rate.

If this is not the case, then interest on the direct loan will be charged at the higher rate. A similar arrangement, involving an interest rate check based on cross-currency swap methodologies, applies where direct loans are denominated in eligible foreign currencies.

Foreign currency risk

Translation risk

A material proportion of our guarantees and insurance policies are written in foreign currencies (usually US dollars). This exposes us to foreign currency risk, and associated volatility, in our financial results. The most significant year-on-year fluctuations in financial performance (evidenced by net foreign exchange gains/losses in the statement of Comprehensive Net Income) stem from the currency movements applicable to our non-sterling insurance assets (recoverable claims).

HMT does not permit UKEF to hedge its foreign currency exposures, so no active hedging is undertaken. This is based on a number of HMT considerations such as:

- our foreign currency assets and liabilities generally have long tenors such that the transaction risks can extend long into the future, and the timing and size of the amounts needing to be converted are uncertain, which could well make for expensive hedging arrangements
- our balance sheet provides some natural hedging of translation risk, and foreign exchange hedging is not straightforward and would require some specialist skills to operate it, adding to our operating costs
- UKEF's FX exposures potentially being offset elsewhere in government, allowing HMT to hedge centrally its overall net exposures more efficiently

Currency movements also have an impact on the sterling value of our contingent liabilities (principally guarantees and insurance policies). These movements can cause significant fluctuations in the sterling value of the department's AAR and, consequently, overall credit risk exposure.

Direct lending

Direct lending in currencies other than sterling is likely to increase foreign currency risk for UKEF. The lack of permission for UKEF to undertake foreign currency hedging applies equally to the department's direct lending activities. Accordingly, changes in the sterling value of direct loans as a result of foreign exchange rate movements will be reflected in the financial performance of our direct lending business.

Liquidity risk management

Liquidity risk is the risk that a business, though solvent, either does not have the financial resources to meet its obligations as they fall due, or can only secure those resources at excessive cost. As a government department, UKEF can draw on the Exchequer to meet its financial obligations as they fall due if required.

The nature of some of UKEF's products means that significant payments could be required within a few days in the event of a default by an insured or guaranteed party. Arrangements to cover this eventuality have been pre-agreed with HMT. Regarding UKEF's direct lending activities, the requisite funding is provided by HMT.

Our exposure to foreign exchange movements has the potential to impact our ability to remain within the resources allocated to us by Parliament. Our voted control totals include headroom to mitigate this risk. However, between the last opportunity to adjust voted control totals in January and 31 March, there is a small risk that exchange rates could move and reduce our net income by more than the headroom agreed with HMT and voted for by Parliament. This would result in a breach of expenditure limits and require a vote to approve the excess.

Statutory limits

The Export and Investment Guarantees Act 1991 sets limits on our commitments and requires us to report our commitments against these limits annually. The table below shows the statutory limits at 31 March 2020 and 31 March 2019 and the outstanding commitments against them.

	At 31 Mar 2020				At 31 Mar 2019			
	Sterling	Foreign Currency	Sterling Equivalent in SDRs	SDR Total	Sterling	Foreign Currency	Sterling Equivalent in SDRs	SDR Total
	£m	SDRm	SDRm	SDRm	£m	SDRm	SDRm	SDRm
Section 6(1) amounts								
Statutory Limit	0	67,700	0	67,700	0	67,700	0	67,700
Total Commitments	2,281	23,050	2,066	25,116	1,734	26,154	1,637	27,791
Section 6(3) amounts								
Statutory Limit	0	26,200	0	26,200	0	26,200	0	26,200
Total Commitments	0	0	0	0	0	0	0	0
	Sterling	Foreign Currency	Sterling Equivalent in SDRs	SDR Total	Sterling	Foreign Currency	Sterling Equivalent in SDRs	SDR Total
	£m	SDRm	£m	£m	£m	SDRm	£m	£m
Section 6(1) amounts								
Assets	0	1	0	1	0	1	0	1
Section 6(3) amounts								
Assets	5	-	4	4	10	-	10	10

UKEF is the most ethnically diverse department in government and has seen a fall in its gender pay gap.

Chief Finance & Operating Officer’s report

This report summarises and highlights the department's financial performance for the year ended 31 March 2020. Given the importance of the management of UKEF's portfolio, this report should be read alongside the Chief Risk Officer’s Report. The detailed financial performance commentary (see below) for the year has been divided into operating segments (lines of business) and there is also a summary of UKEF’s overall performance against resources voted by Parliament.

Cameron Fox
Chief Finance and Operating Officer

There may be rounding differences to the detailed underlying financial statements and notes found in the latter part of this document. Commentary is based on summarised data (in most case rounded to nearest million).

Overall Results

UKEF achieved a net operating income of £217 million for the year ended 31 March 2020 compared with £128 million for the year ended 31 March 2019. On an FX-adjusted basis the net operating income for the year ended 31 March 2020 was £162 million compared with £82 million for the year to 31 March 2019. The change in net operating income for the year primarily comprised of a £41 million improvement in the investment return and a higher release of excess credit funds of £41 million (see Reserving for Insurance Liabilities below for more detail).

Foreign exchange

As a significant proportion of UKEF's guarantees, insurance policies and loans are written in foreign currencies (mainly the US dollar), UKEF is exposed to foreign currency risk and associated volatility in terms of the financial results (UKEF is not authorised by HM Treasury (HMT) to hedge exchange rate exposures – see the Chief Risk Officer’s Report on pages 58 to 85). During the year, sterling appreciated by approximately 2% against the US dollar (see Note 6 and Note 20 of the financial statements which includes details of the currency profile of our insurance assets, financial instruments and capital loan commitments).

Operating expenses

These were higher in 2019-20, at £41 million compared with £37 million in 2018-19. This increase was largely due to a planned increase in staff (see our people: staff and remuneration report). UKEF, however, delivered on efficiencies related to our Spending Review 2015 saving commitments.

Long-term assets and liabilities

Given the nature of the business that UKEF supports, the department has a significant holding of long-term assets and liabilities.

UKEF's major asset classes are, direct lending loans (see Account 5 description below) and recoverable claims (both denominated in a range of currencies, however predominately US dollars). The Account 5 direct lending loan book continued to grow and increased from £957 million in 2018-19 to £1,322 million this year. Gross recoverable claims however reduced from £647 million to £591 million as recoveries were made.

Reserving for insurance liabilities

UKEF applies the fund basis of accounting (see the financial statements from page 155 for a fuller explanation) for its medium and long-term business. At the end of the year the (net) underwriting funds stood at £958 million compared with £896 million at the end of 2018-19. The increase in the fund was as a result of new business written in year. Releases from the funds during the year (being business written in 2010 and 2016) was some £76 million in 2019-20. This release (which is a surplus of premium written over risk and costs of writing the business) reflects the quality of the underwriting and credit decisions made in 2010 and 2016.

Accounts 1 to 5

UKEF currently operates 5 accounts (business segments):

- **Account 1** relates to guarantees and insurance issued for business prior to April 1991 and to insurance issued by UKEF's former Insurance Services Group (the main part of which was privatised on 1 December 1991)

- **Account 2** relates to guarantees and insurance policies issued for business since April 1991

- **Account 3** relates to guarantees and insurance issued for business since April 1991 and the provision of direct lending underwritten on the written instruction of ministers, and that UKEF's Accounting Officer advised did not meet permitted underwriting criteria

- **Account 4** relates to the provision of support for Fixed Rate Export Finance (FREF) to banks (now closed for new business), together with arrangements for reducing the funding cost of FREF loans and for certain interest rate swap arrangements

- **Account 5** relates to the provision of direct lending underwritten in the normal course of Business (since 2014)

Management commentary — 5-year summary

	2019-20 £m	2018-19 £m	2017-18 £m	2016-17 £m	2015-16 £m
Overall value of guarantees and insurance policies issued and effective:					
New business supported – net of reinsurance – A/c 2	3,499	3,372	1,865	2,178	1,507
New business supported – net of reinsurance – A/c 3	-	2,139	-	-	-
Total new business supported – net of reinsurance	**3,499**	**5,511**	**1,865**	**2,178**	**1,507**
Amounts at risk – gross of reinsurance	21,838	21,538	16,988	18,859	17,111
Statement of comprehensive net income:					
Premium income net of reinsurance	177	332	103	102	73
Staff, other administration and operating costs	41	37	34	30	30
Foreign exchange gain/(loss)	55	46	(65)	57	13
Net operating income – total	**217**	**128**	**5**	**149**	**106**
Account 1	57	35	9	63	33
Account 2	88	45	22	70	64
Account 3	(1)	-	-	-	-
Account 4	-	1	2	4	6
Account 5	73	47	(28)	12	3
Net operating income – foreign exchange adjusted	162	82	70	92	93
Statement of cash flows:					
Claims recoveries – total	**71**	**69**	**76**	**120**	**133**
Account 1	38	39	34	47	49
Account 2	33	30	42	73	84
Interest recoveries in the year – total	**31**	**31**	**27**	**31**	**28**
Account 1	29	30	26	28	24
Account 2	2	1	1	3	4
Claims paid – total	**8**	**-**	**2**	**8**	**5**
Account 2	8	-	2	8	5
Net cash flow from operating activities - total	**321**	**484**	**225**	**272**	**199**
Account 1	67	69	60	74	73
Account 2	181	241	114	158	109
Account 3	(11)	95	-	-	-
Account 4	-	1	2	3	5
Account 5	84	78	49	37	12
Statement of financial position:					
Recoverable claims before provisioning	**591**	**647**	**701**	**800**	**876**
Account 1	402	433	463	515	539
Account 2	189	214	238	285	337
Recoverable claims after provisioning	**197**	**247**	**292**	**368**	**429**
Account 1	145	168	190	223	234
Account 2	52	79	102	145	195
Interest on unrecovered claims after provisioning	**118**	**106**	**116**	**134**	**134**
Account 1	117	105	115	133	133
Account 2	1	1	1	1	1

Underwriting funds – net of reinsurance	**958**	**896**	**629**	**582**	**547**
Account 2	873	811	629	582	547
Account 3	85	85	-	-	-
Recoverable capital loans before provisioning	**1,327**	**967**	**505**	**381**	**119**
Account 4	5	10	15	32	51
Account 5	1,322	957	490	349	68

Account 1

The main activity relating to this account is the administration and collection of the claims paid out against these guarantees and insurance policies. In accordance with standard accounting practice, UKEF provides prudently against the possible non-recovery of debts. Where the outlook for recovery improves, the level of provision is reduced accordingly, releasing profit to the statement of comprehensive net income. The key results (rounded to the nearest million) were as follows:

- net operating income was £57 million compared with £35 million in 2018-19. The change in net operating income was due to a £25 million improvement in the investment return
- recoveries of claims paid were £38 million compared with £39 million in 2018-19
- recoveries of interest on claims paid were £29 million compared with £30 million in 2018-19
- the balances for gross claims decreased from £433 million in 2018-19 to £402 million during the year, while those for net claims decreased from £168 million in 2018-19 to £145 million during the year
- interest on net unrecovered claims increased from £104 million in 2018-19 to £118 million during the year
- there is no non-claims exposure on this account

Account 2

The key results were as follows:

- the total of guarantees and insurance policies (net of reinsurance) that were issued and effective during the year was £3,499 million compared with £3,272 million at 31 March 2019
- net premium income was £177 million compared with £332 million in 2018-19
- net operating income was £88 million compared with £45 million in 2018-19. The change in net operating income was mainly due the release from the funds was £76 million in 2019-20 compared with £35 million in 2018-19
- claim recoveries for the year were £33 million compared with £30 million in 2018-19
- gross claims balances were £189 million compared with £214 million in 2018-19
- net claims balances were £53 million compared with £78 million in 2019-20

Account 3

- There was no new Account 3 business issued and effective in 2019-20 compared with last year where UKEF entered in Account 3 business for the first time in over 30 years with support provided for BAE Systems and MBDA UK in relation to the provision of military aircraft and related equipment to the State of Qatar.

Account 4

The results were as follows:

- the direct funding balance represents the funds originally loaned by HM Treasury to reduce the cost of FREF. The balance continued to reduce during the year to £5 million from £10 million in 2018-19, as regular instalments were made
- net operating income was £0.1 million in 2019-20 compared with £1 million in 2018-19

Account 5

This account relates to direct lending activity issued in the ordinary course of business.

- during the year 6 new loans (not including facility increases) were originated (6 loans were originated in 2018-19). There are now 28 loans drawn or drawing
- There is only 1 loan which has been assessed as impaired (see Note 1 of the financial statements for details of the relevant accounting policy)
- there was a net operating gain of £73 million in 2019-20 compared with net operating gain of £47 million in 2018-19. This change was largely as a result of a £12 million larger foreign exchange gain as most of the loans originated were in US dollars and a £17 million improvement in investment return.

Explanation of variances between Estimate and outturn summary

Parliament sets a limit on the annual amount of resource and capital that UKEF can consume through the Supply Estimates process. The table below compares UKEF's Estimate with actual outturn. Further information on the Supply Estimate is available on UKEF's website at www.gov.uk/uk-export-finance.

In the absence of any operating income outside the ambit of the Estimate, UKEF's net resource outturn and net operating cost or income are identical.

UKEF supports export credit loans denominated in foreign currency and as a result is exposed to foreign currency exchange risk arising from fluctuations in exchange rates of various currencies. Almost all of UKEF's premium income arises in currencies other than sterling (mostly US dollars) and net assets are denominated in a variety of currencies, of which the largest is US dollars. As UKEF is not authorised by HMT to hedge exchange rate exposures, it faces challenges to ensure compliance with Parliamentary voted control totals.

From January each year, which is the last opportunity to adjust voted control totals, to 31 March, there is a risk that exchange rates move and reduce net income by more than the headroom agreed with HMT and voted by Parliament.

	SOPS Note	2019-20 Estimate £'000	2019-20 Outurn £'000	2019-20 Variance £'000
Budget spending				
Departmental Expenditure Limit (DEL)	SOPS1(a)	916	911	5
Annually Managed Expenditure (AME)	SOPS1(a)	124,842	(217,744)	342,586
Resource Total & Net Operating Cost / (Income)		**125,758**	**(216,833)**	**342,591**
Non Budget / Resource total	SOPS1(a)	-	-	-
Net Resource Outturn & Net Operating Cost / (Income)		**125,758**	**(216,833)**	**342,591**
Budget spending				
Departmental Expenditure Limit (DEL)	SOPS1(b)	300	135	165
Annually Managed Expenditure (AME)	SOPS1(b)	836,811	307,710	529,101
Capital Total Payments / (Receipts)		**837,111**	**307,845**	**529,266**

Significant highlights:

All UKEF income and expenditure is classified as either DEL or AME and there are no non-budget totals.

Resource – Note SoPS1(a):

AME £343 million – This variance is largely due to provisions and foreign exchange movements which cannot be forecast with certainty and are unhedged. A more detailed explanation of UKEF's foreign exchange risk can be found in the Chief Risk Officer's Report on pages 84 to 85 and Note 20 of the financial statements.

Capital – Note SoPS1(b):

AME £529 million – This variance is largely due to the Direct Lending Facility. Most business is written in currencies other than Sterling (primarily US Dollars) therefore it is subject to foreign exchange volatility. The variance is largely due to the fact that while it is necessary to ensure there are sufficient voted funds, and therefore headroom to meet potential demand in year, it is not possible to predict actual demand (and therefore the associated drawings). Many deals may not close for reasons beyond the control of the department or the timing of loan origination changes. More details of UKEF's risks, including foreign currency and liquidity risk, can be found in the Chief Risk Officer's Report on pages 58 to 85 and Note 20 of the financial statements.

Head of Environmental and Social Risk's report

UKEF examines the environmental, social and human rights (ESHR) risks and potential impacts of projects it is asked to support and monitors their ESHR performance in line with our published ESHR policy.[1] In addition, we collaborate with other export credit agencies and financial institutions regarding ESHR matters, with the aim of establishing a 'level playing field' and sharing good practice in respect of implementing proportionate and effective ESHR risk management across these institutions.

Max Griffin
Head of Environmental and Social Risk Management

During 2019-20 all transactions that fell within the scope of the OECD Recommendation of the Council on Common Approaches for Officially Supported Export Credits and Environmental and Social Due Diligence (the 'OECD Common Approaches') and/or the Equator Principles were screened for ESHR risks. Where we identified significant risks, we designated the project as either a Category A (high risk) or Category B (medium risk) and we carried out an ESHR review of these transactions.

In undertaking ESHR reviews, we place emphasis on early dialogue with exporters and other relevant parties to the transactions. The aim is to ensure that the projects to which UK exports are destined align with the relevant international ESHR standards prior to our support being provided and subsequently throughout the period of UKEF support. In order to achieve this we work with the relevant parties (e.g. project sponsors and UK exporters) to establish and clarify the areas of ESHR management which may need improving to meet international standards and support robust implementation of management systems that achieve this which both mitigate negative impacts and enable positive impacts where possible. UKEF's benchmark ESHR standards are typically the International Finance Corporation's (IFC) Performance Standards on Environmental and Social Sustainability, covering the 8 ESHR topics indicated below:

Source: IFC Performance Standards

1 https://www.gov.uk/government/publications/uk-export-finance-environmental-social-and-human-rights-policy/policy-and-practice-on-environmental-social-and-human-rights-due-diligence-and-monitoring

Our ESHR due diligence and monitoring is carried out by UKEF's professionally qualified and experienced E&S (Environmental and Social) team, supported by the E&S teams of our co-financing institutions and external ESHR consultants, where appropriate.

As well as reducing negative ESHR impacts, the E&S team considers the ESHR benefits which are inherent to many of the proposed projects we review and monitor. Examples of these benefits include:

- enhanced health and well-being within the host communities where hospitals have been supported
- improved availability of clean water and sanitation from the development of water supply and treatment projects
- provision of jobs, training and project-related economic growth made available through the construction and operation of UKEF supported projects overseas

Through ensuring the implementation of our benchmark ESHR standards, these developmental benefits may be enhanced beyond the level that would be provided without UKEF's support. Further work to define these inherent benefits and determine their alignment with the UN Sustainable Development Goals is provided below.

ESHR due diligence

In 2019-20, we worked with a wide variety of project developers and exporters to help them understand and manage ESHR risks associated with their project activities. We supported[2] 15 category B and 3 category A projects that fell within the scope of the OECD Common Approaches and/or the Equator Principles.

UKEF's involvement had a positive impact on projects through implementing ESHR risk management systems and plans in various Category A and Category B projects supported in 2019-20, for example:

Offshore wind farm, Taiwan (Category A):
The project, to build and operate a wind farm off the coast of mainland Taiwan, comprising 47 wind turbine generators (WTGs), together with associated jacket WTG foundations, is UKEF's first offshore wind deal.

UKEF's E&S due diligence involvement, along with a consortium of other ECAs, led to a more rigorous impact assessment by the project sponsor, beyond Taiwanese regulatory Environmental Impact Assessment requirements.

This led to their engagement of international E&S specialist consultants who developed a more robust biodiversity management and mitigation plan to demonstrate how potential biodiversity impacts on a critically endangered population of Chinese white dolphins situated near the project area should be managed. The analysis of the Livelihood Restoration Plan developed to assess the potential impact to the local commercial Fishery Association supported the establishment of a Fishery Compensation and Cooperation Agreement to address potential loss in earnings and provide opportunities for future diversification.

2 'Supported' refers to transactions where finance documents were signed and became effective (for example, the first drawdown took place and UKEF is on cover) within the 1 April 2019 – 31 March 2020 period.

Details of the ESHR risk and impact categorisation of all cases which required an ESHR review under UKEF's ESHR Policy and for which support was issued during 2019-20 are available on UKEF's website.[3]

ESHR monitoring

UKEF conducts ESHR monitoring of all category A and B projects where support has been issued. This allows us to track the implementation of ESHR commitments and to be satisfied that the projects continue to align with the relevant international standards for the duration of our support, during project construction, operations and, potentially, decommissioning.

Our monitoring includes reviewing self-monitoring reports produced by project developers, commissioning independent environmental and social consultants (IESCs) to monitor projects on our behalf, and carrying out site visits. The level and frequency of our monitoring varies relative to the ESHR risks involved.

UKEF seeks to positively influence the application of standards throughout the monitoring process in order to improve and attain positive tangible ESHR outcomes. Examples of this include influencing the project developer:

- to promote positive health and safety behaviours, minimising accidents, injury and loss of life
- in re-establishing the livelihoods of people affected by the project
- in the provision of appropriate worker conditions and accommodation
- in promoting positive project impacts

3 https://www.gov.uk/government/publications/eshr-risk-and-impact-categorisations-2019-to-2020

The following are examples of our ongoing monitoring commitments for 2019-20 across both Category A and Category B projects

Nghi Son Refinery & Petrochemical plant (NSRP), Vietnam (Category A)
UKEF, along with other ECAs and lenders, conducted an E&S operations monitoring visit of the NSRP petrochemical refinery complex. Whilst the facility seemed to have made good progress on health & safety management as it transitioned from construction into the operations phase, some concerns remained regarding compliance with social requirements – particularly resettlement, where 30 households have yet to receive compensation, some 6 years post-physical resettlement.

Whilst NSRP has constantly worked with the local government authorities to settle the matter, the progress to broker resolution, address compensation and implement the Livelihood Restoration Plan (LRP) is still pending. This matter was raised strongly by the ECA group during the monitoring visit.

We have since been encouraged that NSRP (with support from the IESC), is now more actively progressing resolution of these matters. Latest actions are formalised in an updated action plan for lenders to keep them informed of implementation progress.

Monitoring visit of Kumasi market, Kumasi airport and Bekwai hospital (each a Category B project):
The E&S team conducted a site visit to Ghana for two projects in Kumasi (Kumasi market and Kumasi airport) and Bekwai hospital. The visit to Kumasi market focused on the relocation process to move existing traders from the current market location during the construction period. The visit to Kumasi airport and Bekwai hospital were used to assess compliance with the construction environmental and social management plans. The works are in in compliance with the approved ESIA and CMP. The E&S team identified some minor issues relating to environmental and health and safety management, including showers in need of repair and expansion of secondary containment. These were communicated to the management team and have since been rectified.

A summary of cases where we are undertaking ongoing ESHR post-issue monitoring can be found on our website.[4]

International ESHR cooperation

In support of UKEF's objective to achieve fairer competition by seeking to establish a 'level playing field' for all OECD exporters, we work alongside other ECAs at the Environmental and Social Practitioners' Group of the OECD Export Credit Group. We are actively involved in setting the agenda, sharing experiences, participating in working groups and seeking to achieve consistency in ECAs' approach to ESHR risk management practices under the OECD Common Approaches.

In May 2018, UKEF was re-elected by the Equator Principles Financial Institutions (EPFI) for an additional 2-year term on the Equator Principles Steering Committee in a management support role. Having served 2 terms, Equator Principles Governance rules will require UKEF to stand down from this role in June 2020.

4 https://www.gov.uk/government/publications/eshr-risk-and-impact-categorisations-2019-to-2020

During 2019-20 UKEF have led a ten-member Working Group focused on establishing the update to the Equator Principles (EPs), as first announced in 2017, with respect to the scope of their application. This process completed in November 2019 when the next iteration of the EPs, termed 'EP4', was approved by the EP Association with over 98% of EPFIs voting in favour of the update.

UKEF's E&S team were actively involved in the Equator Principles Annual General Meeting held in Singapore in October 2019, sharing experience and engaging and collaborating with EPFI colleagues. The E&S team continues to lead the EP4 Scope Working Group to develop implementation guidance which will be agreed and published before EP4 becomes mandatory, which is currently scheduled for 1 October 2020.

UKEF also participates in ESHR practitioner meetings of several multilateral financial institutions. This includes the International Finance Corporation's (IFC) Community of Learning, as well as meetings of other development and commercial banks and ECAs. UKEF attended and spoke at a number of international ESHR industry conferences this year, including at the ICC-Berne Union Sustainable Finance Working Group and the Future of Export Finance UK.

ESHR Policy review

UKEF commenced a review process relating to our publicly stated Environmental and Social Policy and Practice Statement (E&S Policy), as we committed to doing when it was initially drafted in 2016. This review continued during 2019 as part of UKEF's ongoing consideration of ESHR and climate change factors in its activities.

Task Force on Climate-Related Financial Disclosures

In July 2019 it was announced in the UK Government's Green Finance Strategy that UKEF will be making financial disclosures in line with the Task Force on Climate-Related Financial Disclosure (TCFD) as soon as practicable following the close of the 2020-21 financial year. A project is underway to implement the TCFD recommendations through 2020, as well as further develop the integration of climate change considerations across all the products and services that UKEF provide in alignment with wider government policy and practice, including that provided as part of the UK's hosting of the UN Climate Change Conference of Parties (COP) 26 in 2021.

The Formosa 2 offshore wind project in Taiwan will be built with British expertise thanks to UKEF support.

UN Sustainable Development Goals (SDGs)

The UK Government was at the forefront of negotiating the Sustainable Development Goals (SDGs), unanimously agreed in 2015 by all 193 member states of the United Nations and has committed to be a leader in their delivery. The SDGs lay out a transformative agenda to tackle the world's most pressing social, environmental and economic challenges by 2030.

As a UK government department delivering support to UK exporters and their overseas buyers, UKEF has an important role to play in supporting progress towards the SDGs. This is reflected in our new Business Plan for 2020-24, where we commit to providing support, alongside Overseas Development Assistance and commercial financing (as relevant) in markets and sectors where there are demonstrable developmental and prosperity benefits with secondary benefits to the UK supply chain. You can see more about our new Business Plan on page 17.

UKEF actively contributes to the UK's progress towards and achievement of the following SDGs:

This year, we have undertaken a project to better understand UKEF's current impact on the SDGs, which has identified the role we play unlocking finance for delivery of projects in destination markets for UK exporters has clear potential for ancillary contributions to other SDGs. UKEF is actively exploring opportunities to improve sustainability at every stage of our work, both directly and indirectly.

By fulfilling our mandate and improving our understanding of the role and scale of required contribution towards the SDGs, we can ensure that UK exporters play their role in support of the SDGs whilst maintaining their competitive global standing.

Supporting the SDGs in 2019 -20

This year, we have enhanced our product range to ensure that we can support the global sustainable development agenda. For example, our change to our foreign content policy enabled our support for Solarcentury to build 2 of Spain's largest solar plants, and we have also added a £2 billion tranche of dedicated direct lending capacity for clean growth projects. We have also been collaborating with the Department for International Development on the new Developing Market Infrastructure Programme a concessional financing facility for sustainable public-sector infrastructure projects in developing countries.

Through its marketing and origination activities, UKEF has been seeking new opportunities for UK companies to contribute to projects in sectors with clear inherent SDG benefits such as sanitation, hospitals and renewable energy. This year, for example, saw UKEF contribute to its first ever support for offshore wind as well as a number of healthcare projects in sub-Saharan Africa.

Export Guarantees Advisory Council report

Alistair Clark
Chair, Export Guarantees Advisory Council

The Export Guarantees Advisory Council (EGAC) is an Expert Committee that advises the Secretary of State for International Trade and the Minister for Exports on the policies applied by UK Export Finance (UKEF) when doing business, particularly those policies related to ethical matters. These policies are guided by international agreements that relate to export credit agencies (ECAs). The Council provides advice to ministers and senior UKEF officials on bribery and corruption, environmental, social and human rights risks (ESHR), sustainable lending and transparency, including freedom of information.

2019-20 has seen some significant changes for EGAC. I took over from Andrew Wiseman as Chair of the Council in March 2019, when he reached the end of his term. I was appointed Chair having served as a member of the Council for 10 years and believe it fulfils a valuable role in providing UKEF and its ministers with strong, independent expert advice. I very much look forward to leading the Council going forward.

The work of the Council is varied. The Council's status means that it can address its views directly to ministers at any time, on any subject where it deems it appropriate to do so. The Council's main role is to review the application of ethical policies to past decisions that UKEF has made to support export transactions – we are not involved in taking decisions on cases which are currently under consideration by UKEF. We also make sure that UKEF continually informs the Council of developments related to relevant international agreements, and the policies set by ministers which guide UK Export Finance's operations, so that these can be considered by Council members in providing their advice.

Council members are appointed by the minister responsible for UKEF. It is a body of experts who act in a personal capacity. Council members have a wide range of skills and experience in the areas of commerce, international trade and academia, with experience of the practical application of ethical policies. I would like to record thanks to members for the invaluable advice that they provide and the time that they commit to carrying out their duties.

In 2019-20, EGAC underwent a recruitment exercise to replace the members who left during the year. In addition to Andrew Wiseman, John Newgas and Anna Soulsby also reached the ends of their appointment terms. Both were valuable members of the council, and their advice and guidance was greatly appreciated by UKEF and its ministers. Dr Ben Caldecott from Oxford University, and Vanessa Havard-Williams from Linklaters were appointed as EGAC members. I welcome them to the Council and look forward to working with them.

The Council's current members are:

Chair

- **Alistair Clark**, Corporate Director, Environment and Sustainability Department, European Bank for Reconstruction and Development

Members

- **Dr Ben Caldecott**, Associate Professor and Senior Research Fellow at the University of Oxford Smith School of Enterprise and the Environment.
- **Alexandra Elson**, Senior Stakeholder Relations Adviser, Shell plc
- **Vanessa Havard-Williams**, Linklaters Partner specialist in sustainability law and policy, risk management and sustainable finance.
- **Neil Holt**, corporate anti-bribery adviser
- **John Morrison**, Executive Director, Institute for Human Rights and Business
- **Stephen Prior**, Partner, Prinia Consulting LLP and an experienced sales director in emerging markets
- **Dr Roseline Wanjiru**, Senior Lecturer and Programme Leader, Newcastle Business School

The Council met formally 3 times in 2019-20, and contributed informally to strategic policy discussions throughout the year.

Environmental Audit Committee

In March 2019, the Council Chair appeared in front of the Environmental Audit Committee (EAC) investigation into the scale and impact of UKEF's financing of fossil fuels in developing countries. The EAC report made the following specific recommendation in respect of the Council:

> *The remit of the Export Guarantees Advisory Council (EGAC) should be expanded to include assessing how UKEF's activities contribute to the UK's climate commitments and greenhouse gas net zero targets. The EGAC should report regularly on this progress to the Secretary of State for International Trade.*

To address these recommendations the government has stated that it would carry out a review which will impact on the work of the Council to a large extent and will set the direction of our work for the future. The government agreed the following actions:

> *The Secretary of State would consider EGAC's remit to provide advice on UKEF's climate-related policies and how it applies them to the businesses that it supports;*
>
> *EGAC would review its reporting to the Secretary of State for International Trade to consider the climate-related impacts of UKEF's support;*
>
> *UKEF will describe EGAC's governance role on climate-related risks and opportunities in further detail when it issues its first climate-related disclosures statement; and*
>
> *EGAC will play an active role in advising UKEF as it develops its strategy on climate-related risks and opportunities. In order to support EGAC in this role, UKEF will seek to add further climate change expertise to EGAC through additional recruitment of a climate change expert to join EGAC.*

A transcript of the hearing and the evidence submitted by the Council is available on the parliament website:
https://www.parliament.uk/business/committees/committees-a-z/commons-select/environmental-audit-committee/inquiries/parliament-2017/uk-export-finance-17-19/

EGAC Governance

Following the recommendations of the Environmental Audit Committee, the Council is re-examining its role. In June 2019, EGAC considered how lessons could be learned from other export credit advisory councils. The Council looked at the advisory council of Export Development Canada, and recommended that UKEF and its ministers look at best practice there when considering the role of EGAC. In September, the Council examined how it could work more closely with the UKEF Board. In March 2020, the minister agreed that the Chair of EGAC should be an ex-officio member of the UKEF Board. This will improve the link between the Council and the UKEF Board, and ensure that the expertise of Council members in climate change, environmental and human rights matters, anti-bribery and corruption and debt sustainability is factored into the deliberations of the UKEF Board, as these issues cut across the wider perspective of UKEF's role and remit more than ever before.

Environmental and social risk management and the OECD

While the strategic decisions are being made on the future role of EGAC, the main business of the Council continues.

In 2020 the OECD will review some significant environmental policies which will apply to UKEF. OECD members will review the Recommendation of the Council on Common Approaches for Officially Supported Export Credits and Environmental and Social Due Diligence (the "Common Approaches"). In February, EGAC discussed the review with UKEF. The Council recognises that UKEF has been fully engaged in the process so far and provided advice on UKEF's strategic approach to working with likeminded countries to discuss and agree where to strengthen the recommendations, prior to the negotiations being opened.

The OECD Coal-Fired Electricity Generation Sector Understanding (CFSU) was implemented in February 2016 and was due for review by OECD Participants in June 2020. In February, the Council discussed the UK's approach to the CFSU discussions, and recommended that UKEF use bilateral contacts to test the appetite of other countries as to what might be possible in resetting the agreement.

Environmental, social and human rights (ESHR) policy

UKEF's Environmental and Social Risk Management (E&S) team identifies, reviews and, where support is provided, monitors ESHR risks and impacts in accordance with the OECD Common Approaches and the Equator Principles. Part of the Council's role is ensuring that the E&S team is properly equipped to carry out the necessary ESHR reviews, and in 2019-20 the Council was satisfied this was so.

While ensuring that UKEF's ESHR policies are properly applied to cases, the Council examines a number of cases that have been supported by UKEF each year. The Council can examine any project which UKEF supports and will review at least one project classified as higher ESHR risk or 'Category A' each year. In June 2019, the Council examined the environmental and social due diligence which had been carried out by UKEF in relation to its support for the Samawa and Dhi Qar Power Stations in Iraq. Both had been classified as Category A projects. The Council noted that UKEF was the only export credit agency engaged on the project and noted that UKEF had been able to exert positive influence on the project, for example where it had required a redesign of the plant to incorporate more emission reducing equipment. In February, the Council considered the policies that were applied to a Category B case in Benin. The Council recognises that UKEF can positively influence UK exporters and their projects by assisting their capability to assess and manage ESHR risks resulting from their activities.

Climate Change

In 2019-20 the Council also held discussions in respect of UKEF's role in the development and delivery of the UK government's climate change policies. For example, the Council looked at UKEF's alignment to the UN Sustainable Development Goals (SDGs). The Council commended the approach that UKEF was taking in its considerations, noting that UKEF's statutory role is to support exports, and that UKEF would be considering both positive and negative contributions to the SDGs. We also looked at initiatives being implemented by other governments and gave advice on the approach UKEF could take. The Council also recognised the efforts UKEF undertook in 2019-20 to bring climate change awareness to the forefront of its work. In December 2019, UKEF purchased 150 licenses for staff to take an accredited online course from Imperial Business School on Climate Change Financial Risks and Opportunities. The Council is aware that climate change will continue to be a significant consideration for UKEF, and is supportive of initiatives like this to train UKEF staff.

Anti-bribery and corruption

The Council carried out its annual consideration of the application of UKEF's anti-bribery policies and practices in December 2019. These policies are mainly derived from the 2019 OECD Recommendation on Bribery and Officially Supported Export Credits (OECD Bribery Recommendation) and UKEF's polices that originated in Government's public consultations on UKEF's anti bribery policies and practices in 2005-6.

The Council also reviewed the work UKEF is doing to strengthen its work in this area. The Council welcomed the process that had seen UKEF's Compliance function fully overhauled from February 2019. The function is led by senior civil servants with policy and legal backgrounds, and staff within this function are encouraged to obtain professional qualifications in this area.

The Council was pleased to hear that UKEF took a principal role at the first OECD workshop on anti-bribery and corruption since the adoption of the 2019 Recommendation. UKEF led a session with stakeholders including ECAs, Multilateral Development Banks, banking and business representatives, and NGOs on measures to deter bribery in international business transactions, including relevant international developments, evolving business practices and future steps.

In June 2019, the Council considered changes to the wording for buyer credit policies in respect of bribery and corruption. The revised wording was clear and the approach UKEF had taken was appropriate. The Council was pleased to see satisfactory progress being made in this area. The Council will continue to look at anti-bribery and corruption issues in 2020-21.

Transparency

The Council conducted its annual review of UKEF's treatment of information requests made under the Freedom of Information Act (FOIA) and the Environmental Information Regulations (EIR). The Council recognised UKEF's continuing high performance in terms of responding to requests within the statutory deadline. UKEF responded in time to 99% of requests, compared to a central government average of 91%.

Overall, 2019-20 was the beginning of a transformative period for the Council. I expect 2020-21 will see a continuation of this process and with a refreshed mandate and membership, the Council's work will be refocused and strengthened.

The Council's Terms of Reference, Register of Members Interests, minutes of its meetings and contact details can be found on the government's website: www.gov.uk/government/organisations/exportguarantees-advisory-council.

For further information on the work of the Council please contact the Council Secretary: chiefexecutiveoffice@ukexportfinance.gov.uk.