

# **EXPORT-IMPORT BANK of the UNITED STATES**



## **REPORT TO THE US CONGRESS ON EXPORT CREDIT COMPETITION AND THE EXPORT-IMPORT BANK OF THE UNITED STATES**

**FOR THE PERIOD  
JANUARY 1, 2009 THROUGH DECEMBER 31, 2009**

*JUNE 2010*





FRED P. HOCHBERG  
CHAIRMAN AND PRESIDENT

EXPORT-IMPORT BANK  
OF THE UNITED STATES

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June 30, 2010

The Honorable Christopher J. Dodd  
Chairman  
Committee on Banking, Housing and Urban Affairs  
SD-534 Dirksen Senate Office Building  
Washington, DC 20510

Dear Mr. Chairman:

In accordance with Section 2(b)(1)(A) of the Export-Import Bank Act of 1945, as amended, I am pleased to forward the report of the Export-Import Bank of the United States on the competitiveness of its export financing services. This report covers the period from January 1, 2009, through December 31, 2009.

This report sets out how well the Export-Import Bank was able to compete with other export credit agencies in 2009, throughout the world. In particular, 2009 was a record breaking year for Ex-Im with total authorizations of \$21 billion supporting \$26 billion worth of US exports. Furthermore, over 20% (\$4.4 billion) of Ex-Im's authorizations directly supported small businesses. This is no small feat especially in light of one of the world's most hard-hitting economic crises. Ex-Im Bank proved itself ready and able to step in with creative tools and responsive programs when the private sector withdrew from export finance. This analysis is vital as we face today's economic challenges, and, going forward, informs Ex-Im in terms of how the Bank can contribute to supporting US jobs by providing competitive financing to US exports.

Sincerely,

Fred P. Hochberg  
Chairman and President





FRED P. HOCHBERG  
CHAIRMAN AND PRESIDENT

EXPORT-IMPORT BANK  
OF THE UNITED STATES

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June 30, 2010

The Honorable Barney Frank  
Chairman  
Committee on Financial Services  
United States House of Representatives  
2129 Rayburn House Office Building  
Washington, DC 20515

Dear Mr. Chairman:

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## **THE 2010 ADVISORY COMMITTEE'S STATEMENT ON THE 2009 COMPETITIVENESS REPORT OF THE EXPORT-IMPORT BANK OF THE UNITED STATES**

The Members of the 2009 Advisory Committee ("Members") have reviewed the 2009 Competitiveness Report to Congress and present our statement on the Report's findings regarding the competitiveness of Ex-Im Bank as compared with other major G7 export credit agencies (ECAs).

### **Methodology:**

The Advisory Committee believes that the general methodology in assessing Ex-Im's competitiveness vis-à-vis the G7 ECAs, while sound, could be improved as is discussed in our collective recommendations below. In particular, given the important role ECAs have played in stemming the effects of the global financial crisis on exporters, the "emerging issues" chapter (Chapter 8) gives a clearer view of the ECA world and how Ex-Im Bank fits into the broader global picture. However, the metrics reflected in the same Chapter could incorporate a more comprehensive side by side comparison with the other G7 ECAs to reflect the most current economic conditions and to better define the Bank's competitiveness compared to its peer group and how it supports US exports and jobs. The Advisory Committee would like to see a broadening of the comparative analysis between G7 ECAs to include data related to volume, product(s), industry sectors, and types of exporters supported (among others) as this would provide an even better understanding as to how well Ex-Im compares with the other ECAs.

The majority of Advisory Committee members believe that the "report card" approach used to define the relative strength and competitiveness of Ex-Im Bank's programs as compared to other ECAs gives a good picture of the ECA landscape. However, in the spirit of improving the response rate of the annual survey of exporters and lenders, the Advisory Committee recommends that Ex-Im Bank invest in the services of a survey expert to evaluate and recommend any changes to ensure that the survey is presented in the best format and is user-friendly (see Strategic Implementation Plan recommendations below). The Advisory Committee recognizes the fact that Ex-Im took the recommendation made in the 2008 Competitiveness Report to assess Ex-Im's environmental program standards with the "report card" approach.

### **Findings:**

- **Core Business Policies and Practices:** The Advisory Committee members applaud Ex-Im Bank for its real-time response to the needs of the entire US exporting community, including small and large companies and for differing loan maturities, during this financial crisis. However, the members are concerned that Ex-Im's internal processing procedures continue to be a source of frustration for exporters and lenders. It appears the slow processing time is, at least in part, a function of stringent underwriting procedures as well as an organizational structure that does not establish accountability with a single individual within the operating groups (see Operational Improvement recommendations below).

- In the Advisory Committee's view, the Bank must also make a concerted effort to address this issue and find the means to broaden its scope and depth of risk in a prudent manner. For example, Ex-Im Bank might consider risk-sharing commensurate with more appropriate rates of return for the user, more co-financing agreements, and/or a portfolio management approach as ways of prudently and thoughtfully managing greater risk. To this point, the Members note that the Bank's ECA counterparts employ several of these tools in a more aggressive, but balanced way, to support their exporters in relatively riskier markets. Thus, unless the Bank finds alternatives to its current risk appetite, Ex-Im's competitiveness on this element of risk-taking will clearly decline over time.

The Members applaud the Bank for its innovations to deal with depleted liquidity in the financial markets. The "Take-Out" Option and capital markets structure have proven to be key competitive tools for Ex-Im and the Advisory Committee commends the use of such tools to help US exporters compete in the global marketplace.

- Major Program Structures: The Advisory Committee recognizes that co-financing is an important tool for Ex-Im Bank and its ability to promote US jobs and exports. The increase in the use of co-financing proves that Ex-Im can finance transactions that would have otherwise not gone forward. Furthermore, the Members are pleased with the competitiveness of the Project Finance and Aircraft programs, particularly given their important role in boosting Ex-Im's precedent-setting 2009 activity and volume. However, the Members encourage the Bank to look at ways to address the technical issues that are constraining Ex-Im's inability to compete vis-à-vis the other ECAs when it comes to foreign currency guarantee program.
- Public Policy Issues: The members of the Advisory Committee, except for the representatives for labor, acknowledge that policy issues such as economic impact, content, and Marad/PR-17/shipping requirements are areas which generate much discussion among Bank officials, exporters and lenders. We would encourage the various stakeholders to reach an agreement with Ex-Im Bank on approaches to these issues. Reconciliation of these policy issues would greatly assist the Bank and the US exporting community to overcome, at least to some degree, the hurdles that these issues present. However, this effort can only go so far before any major changes would require an Act of Congress. Hence, the Advisory Committee needs to be realistic about its expectations of Ex-Im Bank on a number of these issues because the authority to substantively change policies is not within Ex-Im Bank's control, but rather with the US Congress.

However, with regard to assessing the competitive impact that these issues have on Ex-Im Bank, it would appear to the majority of the Advisory Committee members that the approach taken by the Bank represents as fair



an approach as possible by making a qualitative assessment rather than a quantitative “specific grade” assessment. This approach simply acknowledges the fact that when these issues are part of a transaction, the requirements imposed on Ex-Im Bank often delay case processing and can reduce the level of support that Ex-Im Bank can offer. When the public policy-affected transactions face competition from other foreign official ECAs, the US Ex-Im Bank-supported deals are relatively less competitive, all other things being equal, in terms of the financing offered than the other ECAs.

### **Advisory Committee Recommendations:**

- Renewable Energy & Environmental Exports: The Advisory Committee has several recommendations for the Bank with respect to improving its support for the rapidly growing renewable energy and environmental export industry sector.
  - 1) The first recommendation is to improve the marketing and outreach of the Bank’s renewable energy and environmental export programs to U.S. exporters by expanding its efforts in this area through the use of “new media” outlets versus traditional mailings and print media advertising. For example, the Bank could issue a “Deal of the Month” that highlights a recent approval for a U.S. exporter in the renewable energy sector that gets released to the blogging community that focuses on this sector. The Bank should also consider establishing links on the websites of all of the renewable energy industry associations that would lead U.S. exporters in this sector to the Bank’s Environmental Exports Program site.
  - 2) The second recommendation is to increase the usage of the Bank’s renewable energy and environmental export programs via process improvement and enhanced risk tolerance for this sector. Suggestions for implementing this recommendation include providing greater transparency and accessibility in the financial modeling, analysis and credit criteria employed at the Bank for renewable energy projects to both U.S. exporters and lenders, expanding the “Solar Express” fast track approach to other renewable energy sectors, raising the ceiling for the “Solar Express” fast track program to \$20 million and expanding the Working Capital Guarantee Program above the current 90% ceiling for lenders supporting the pre-export working capital needs of small and medium sized U.S. exporters in the renewable energy/environmental sector.
  - 3) The final recommendation is to develop the reputation of the Bank as the “best-in-class” with respect to the renewable energy sector, just as it seen as the preeminent player in aircraft finance. To do so, the Bank should consider providing additional resources dedicated to the Office of Renewable Energy and Environmental Exports, in particular underwriters and loan officers who can advise small and medium-size U.S. exporters on limited-recourse project finance and structured finance loans in order to make the projects “bankable”. Expand the Bank’s acknowledged expertise

in structured trade finance “downward” to include smaller projects that are characteristic of the renewable energy sector.

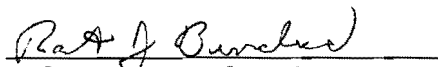
- Strategic Implementation Plan: The Advisory Committee made the following recommendations with focus on outreach programs to assist in the doubling of exports over the next 5 years, and procedures used to develop the Competitiveness Report:
  - 1) Establish small task forces to expedite approvals in key emerging growth markets and industries: Similar to the current pilot program consisting of a team of two (2) credit underwriters and one (1) relationship manager assigned to focus on Mexico transactions, Ex-Im should designate/create/assign teams to other key markets and/or industries to more timely and efficiently address transactions.
  - 2) Leverage the Trade Promotion Coordinating Committee (TPCC) to facilitate Bank business through the following efforts: (i) Obtain contact information and market to companies that benefit from US government programs (i.e. recipients of federal funds from the American Recovery and Reinvestment Act of 2009 as well as the Buy America program); (ii) Investigate other export and trade related agencies to facilitate the promotion of Ex-Im products. Some possible agencies consist of the International Trade Administration, the President's Export Council, the Millennium Challenge Corporation (MCC), the Small Business Administration and the various District Export Councils to name a few; and, (iii) Continue to leverage and educate Department of Commerce's Commercial Service Officers globally to grow US exports via Ex-Im.
  - 3) Research various US agency trade related websites to determine if Ex-Im products and services are sufficiently profiled and easily identified. For example, a link to Ex-Im Bank products and services should be easily accessed under [www.trade.gov](http://www.trade.gov).
  - 4) Work with the State International Development Organization (SIDO, [www.sidoamerica.org](http://www.sidoamerica.org)) to educate various state international representatives about Ex-Im Bank programs.
  - 5) In regards to the Competitiveness Report, in order to increase the annual survey response rate, consider (i) Providing additional resources to assist in direct follow-up of survey recipients who have not responded to the survey; (ii) Use Ex-Im's Regional office staff to assist in direct follow-up of survey recipients who have not responded to the survey; and, (iii) Make the survey transactional and more real time (i.e. to be completed after each transaction is approved). It is also recommended that consideration be given to hiring an independent professional experienced in surveys of this nature to; (i) Review current practices and procedures to developing the survey, reviewing the results, and drafting the report; (ii) Review current questions for objectivity; and, (iii) Make recommendations regarding new methodology (i.e. electronic, online surveys), new questions, and other reporting models (changing the Report Card model). It is further recommended that a change to the timeline for the production of the report be considered to provide the Advisory Committee with more time

for their recommendations to be made. Guidelines should be established to follow-up on the previous year's Advisory Committee recommendations as well as an appendix to the Competitiveness Report should be added detailing all legal and regulatory requirements related to producing the Competitiveness Report (i.e. every three (3) years the survey needs to be approved by OMB, as a result of the Paper Reduction Act)

- Small Business: The Advisory Committee has several recommendations as it relates to supporting the small business community:
  - 1) Expand outreach and marketing efforts to small businesses and the intermediaries who serve them by developing new marketing materials, including web-based marketing, that would expand Ex-Im's messaging beyond direct personal relationships and bank relationships and into such groups as trade associations, insurance brokers, chambers of commerce, accounting firms, private equity sources such as buy-out funds and venture capital funds, and others.
  - 2) Expand marketing to previous small business customers of the Bank who have not used Ex-Im assistance recently, while encouraging existing customers to expand exports to additional markets. Conduct a study of Ex-Im's existing data to develop target lists of previous Ex-Im small business customers who have not recently used Ex-Im financing and current customers who export to only a single market. The goal should be to enable targeted marketing messages for both groups.
  - 3) Study and review the U.S. content rules to determine whether their accounting definitions are unnecessarily restrictive as applied to small businesses, especially small technology businesses and service businesses, and determine whether targeted modifications to the content rules could increase exports and domestic hiring. We know that in the past decade U.S. service exports have outpaced manufacturing exports by over 30% and have produced a trade surplus. We also know that small technology based businesses have been the single largest creator of jobs over the past decade. We also know that both these types of small businesses have a relatively low cost of goods sold compared to capital invested or revenues. This suggests that content rules developed in the 1960s for manufactured goods may not be conducive to encouraging small business exports of services or technology. Notably, Short Term Policy defines Content as "cost," and only refers to Cost of Goods Sold (COGS), while the high R&D content of new technologies may not be captured by the current rules. Labor representatives assert that diluting direct content measures may provide small businesses incentives to move work offshore. Ex-Im should commission a study to determine whether and how a modification of the content rules might be used to encourage the growth of small business exports in these two areas; and to determine how such increased exports might encourage employment growth. The latter may include a review of how the Bank might measure the domestic jobs created or maintained by its activities.

- Operational Improvements: The Advisory Committee makes the following recommendations:
  - 1) The first recommendation is that the existing organizational structure should be changed and the Bank should place overall operating responsibility of the specific operating groups with a single person. In having the functional groups report to a single group head, accountability will be more effectively established for the operation of the group.
  - 2) The second recommendation is that parameters or goals be established for each functional group. The goals should include timeframes for when decisions are expected to be made with respect to an application. These goals or metrics should be clearly defined and each group head should be made responsible for making certain their goals are achieved.
  - 3) The Bank should consider holding periodic application reviews with various users of the program. The discussions should be informative for the users of the program to better understand the Bank's informational needs as well as allow users to communicate any issues faced during the application process.
  - 4) The final recommendation is that a careful review should be performed of the current technology being utilized to process applications. The existing system remains cumbersome and difficult for experienced and inexperienced users to manage. The current on-line system has known flaws that have yet to be addressed and make it difficult for not only new users, but also experienced users to file applications.

**Summary:** The 2010 Advisory Committee would like to commend the Bank for its role in helping to stem off the detrimental effects of the global economic crisis. Ex-Im has played a crucial role for US exporters during a highly volatile period in the global economy. However, as the crisis wanes, which it will eventually, the Bank must be prepared to anticipate new challenges and be ready to address them, but first Ex-Im must acknowledge that the world is a very different place than it was pre-crisis. There is a high degree of uncertainty in the future; the last year has shown just how surprisingly volatile the world can be. Hence, the Advisory Committee strongly urges the Bank to embrace this "brave new world" with a more proactive and competitive strategy and to begin building the framework to adopt and sustain this approach in the years to come. Within this framework, the Advisory Committee believes the Bank must address a number of long-standing issues to ensure that the Bank maintains a high degree of competitiveness with its official ECAs counterparts.



Robert J. Bernabucci,  
Chairman  
2010 Ex-Im Bank Advisory Committee

# 2009 COMPETITIVENESS REPORT

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# Executive Summary

## Background

The 2009 Annual Report to Congress on Export Credit Competition provides a comparative evaluation of the competitiveness of Ex-Im Bank's medium- and long-term programs and policies with those of the major G7 export credit agencies (ECAs) during the calendar year. In conducting this assessment, Ex-Im Bank obtained information from the ECAs themselves, reliable data sources (e.g., WTO, OECD), as well as surveys and focus group discussions with the US exporting community (both exporters and lenders). The analysis compares the specific features and elements of Ex-Im's programs and policies with those of the Bank's major official ECA counterparts.

## Findings

This past year (2009) proved to be an important year for the world of export credits, as ECAs emerged as key players in combating the negative effects of the financial crisis in the areas of short-term trade finance and medium- and long-term export credits. Due to the general lack of liquidity in the financial markets and reduced willingness to handle export finance transactions by many private lenders, ECAs found themselves often being the only option for exporters. ECAs worked diligently to come up with innovative products and methods to keep exports flowing.

Ex-Im Bank had an historic year in 2009. The Bank was able to readily meet exporters' needs and keep transactions viable, even in light of the financial crisis. In terms of exports supported in FY 2009, Ex-Im had its biggest year ever with total authorizations valued at \$21 billion supporting \$26 billion worth of US exports. Moreover, in the "new world" of trade and export finance created by the financial crisis, Ex-Im's competitiveness received an upgrade from an "A-/B+" in 2008 to an "A" for 2009. A summary table in Chapter 7 reveals the details of the overall ratings.

This upgrade is mainly attributable to developments in three areas: (1) co-financing, (2) the Bank's direct lending program and (3) innovations to Ex-Im's medium- and long-term guarantee program, such as the new "Take-Out" Option and a capital markets structure. First, the improvement in Ex-Im's co-financing program in which the Bank supported a record number of co-financed transactions (34). Moreover, while co-financed transactions were still dominated by aircraft transactions, the scope of sectors expanded and involved ECAs with whom Ex-Im had recently concluded bilateral agreements (Coface/France and Euler Hermes/Germany). In addition, the Bank continued to support one-off co-financed transactions with ECAs with whom no bilateral agreement existed, evidencing Ex-Im Bank's willingness to find meaningful solutions.

Further, the availability of the Bank's competitive direct loan program, the "Take-Out" Option, and a capital markets option gave lenders and exporters financing alternatives

that, had they not existed, the transactions most likely would not have gone forward or would have been cost prohibitive for the buyers.

However, the export community cautioned that the relatively positive assessment of Ex-Im Bank may be a “one-time” occurrence that is directly related to the Bank’s ability to step in and make programs and features available to confront a crisis. There is serious concern in the exporting community that, as the financial crisis fades away, core competitiveness issues such as risk taking, public policy issues of content, economic impact and MARAD, and transaction processing time still need to be addressed immediately. Otherwise, these issues will return as impediments to Ex-Im’s effectiveness and competitiveness. Moreover, the exporting community expressed disquiet about the persistent and ever-growing presence of China as a general competitive threat, and in particular, the export credit field where US companies are facing competition against non-standard OECD financing terms.

## **Looking Forward**

Ex-Im made use of its already existing products and also implemented new initiatives to address failures in the banking sector, the lack of liquidity, the instability of the financial markets and the US exporting community’s needs. The G7 ECAs similarly stepped up by expanding capacity and modifying terms and conditions of existing medium- and long-term products. (Direct lending or refinancing for medium- and long-term export credits were put in place by a number of the smaller ECAs.) A number of the G7 ECAs in the EU have also pursued new efforts to address the needs of their SME community on an emergency basis whereas Ex-Im Bank already had programs in place and, when the needs arose, the Bank was able to quickly respond.

In looking ahead, there are a number of factors that are likely to influence how official ECAs will evolve once the financial crisis and all of its ramifications begin to dissipate. The imposition of new banking regulations at the international and national levels, highly leveraged national treasuries and related ECAs, and a flight to higher quality risk suggest that ECAs will retain an enhanced role for years to come. However, to the extent that the market’s concern with risk is accurate, it is not at all clear that the ECA world - as a whole - can or will continue to absorb the kinds and levels of risk currently being presented to them. There do not appear to be any incentives being built into the global ECA system that would encourage ECAs to take a relatively more aggressive approach toward cross-border risks.

Nevertheless, to the extent an ECA sees a counter-cyclical role for itself (as most ECAs have done during the financial crisis) and can do so prudently, such ECAs stand to assume a major position in the international marketplace. In any event, as ECAs from non-OECD countries, such as China, become major export credit providers (and have in fact proven to be during the financial crisis), these ECAs have added another competitive dimension. Their non-standard, non-OECD compliant financing terms must be addressed by the OECD ECAs, including US Ex-Im Bank, to remain competitive in the global marketplace.



In light of President Obama's National Export Initiative (NEI) launched in 2010 that aims to double US exports within the next five years, Ex-Im Bank could play a vital role in achieving this goal by providing access to financing for exporters. As the financial crisis winds down, Ex-Im Bank will be at a critical juncture in maintaining its momentum of increased financing for US exporters, when typically, demand for ECA support winds down as economies recover and private sector lenders re-engage in supporting US export transactions.



# Chapter 1: Introduction

## Background

Pursuant to its Charter (the Export-Import Bank Act of 1945, as amended), Ex-Im Bank is mandated to provide US exporters with financing terms and conditions that are competitive with those made available by foreign governments to their exporters. The purpose of this report, which is required by Section 2(b)(1)(A) of the Charter, is to measure the effectiveness of Ex-Im Bank's programs and policies in meeting the competitiveness mandate during calendar year 2009.

## Scope of Report

This report compares Ex-Im Bank's competitiveness with that of the other G7 ECAs<sup>1</sup>, as these ECAs have historically accounted for approximately 80% of medium- and long-term official export finance. Further, the Competitiveness Report focuses on medium- and long-term export credits (but not short-term activities) because medium- and long-term transactions are subject to the most intense international competition. In addition, there are very few official ECAs that continue to offer short term support. Quantitative comparisons and information on each of the G7 ECAs can be found in Chapter 2 and Appendix D.<sup>2</sup>

## Overall Report Methodology

Based on the "report card" methodology that was introduced in 2002, this year's Competitiveness Report provides a grade for the competitiveness of Ex-Im Bank support. This approach evaluates each of the essential components of Ex-Im Bank's financing and compares them to the capabilities of the Bank's primary foreign ECA competitors.

In addition, Ex-Im's survey of exporters and lenders provides respondents the opportunity to evaluate Ex-Im Bank's competitiveness on individual program factors and public policy issues as they relate to Ex-Im Bank's G7 ECA counterparts. (See below for information on the survey methodology.) However, because the economic philosophy and public policy issues do not affect every case – and because not all of these issues can be evaluated on a comparable basis with other ECA policies – the Report only notes the *direction* of the potential competitiveness impact on an individual transaction when one or more of these factors is rated noticeably different than those of other ECAs.

Consistent with previous years' Competitiveness Reports, the Bank's analysis and competitiveness grades draw upon: 1) objective policy, programmatic and procedural information about other ECAs obtained from a variety of sources; and 2) subjective

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<sup>1</sup> The names and brief descriptions of the other G7 ECAs are contained in Appendix D.

<sup>2</sup> All dollar volume data contained in the Report is in non-inflation-adjusted US dollars.

information provided by the survey of the US export and export finance community and focus group discussions with exporters and lenders.

## **Survey Methodology**

The Bank is required by its Charter to conduct an annual survey of exporters and lenders to determine their experience with competition supported by official export credit agencies during the last calendar year. In 2003, Ex-Im Bank revised its survey to correspond with the grading methodology adopted in the 2002 Competitiveness Report. This approach is being continued because it gives survey recipients the opportunity to provide an assessment of Ex-Im Bank's competitiveness in different financing programs by selecting defined grades from A+ (fully competitive) to F (does not provide program). In addition, survey recipients are asked to note whether certain public policies had a positive or negative impact on the Bank's competitiveness, to the extent they had related experience. After each section, respondents have space to provide qualitative comments on each of their responses. Finally, the Bank continued its practice of distributing the survey to respondents over the internet and allowing them to complete and submit their survey to Ex-Im Bank in the same manner. Recipients could also complete and return the survey either by mail or facsimile if the internet option is not available or desirable. By using internet distribution, Ex-Im Bank has been able to reach a greater number of Bank customers as respondents to the survey with the explicit goal of gathering a broader and more representative population of Bank customers.

Ex-Im Bank carefully evaluated the quality of each survey response. Some specific responses were discarded if a respondent graded a program or feature with which it clearly had no experience. Qualitative responses were discarded if the respondent did not complete the survey in areas where they claimed to have had experience or were based on something other than a comparison of Ex-Im Bank's medium- and long-term programs with those of other ECAs. The survey results are used throughout the Report, and Appendix C provides background on the survey and respondents.

## **Focus Group Methodology**

In addition to the annual survey of the export community, the report also incorporates the results from two focus group discussions – one with commercial lenders and another with exporters. The focus groups provide a venue for members of the export community to supplement their survey responses with anecdotal experience, as well as eliciting more comprehensive information on market trends. While individual focus group comments are occasionally cited in this report, these individual comments were chosen because they best represent the general view of the group.

## **Report Structure**

This year's report follows the same structure used in last year's report. The Ex-Im Bank Advisory Committee Statement follows directly after the transmittal letters to members of Congress. The Executive Summary, which precedes Part I, provides an overview of the major findings of the Report. Following the Executive Summary and this

introductory Chapter 1, Chapter 2 focuses on the international framework within which official ECAs operated in 2009 and the philosophies and missions of competing G7 ECAs. Chapter 3 evaluates Ex-Im Bank's competitiveness on the core financing elements of official export credit support. Chapter 4 provides a comparative assessment of how well the financing elements are packaged into major programs (aircraft, project finance, co-financing, foreign currency guarantees, and services exports support). In Chapter 5, the evaluation of competitiveness addresses US economic philosophy and competitiveness as evidenced by its approaches to (a) tied and untied aid and (b) market windows. Chapter 6 evaluates stakeholder considerations embodied in public policies and the long-term competitive implications of these policies on Ex-Im Bank activity. Chapter 7 summarizes Ex-Im Bank's overall competitiveness, taking into account core financing elements, major programs, and US economic philosophy and public policies.

Chapter 8 deals with emerging issues and this year examines the impact of the global financial crisis on ECAs long-term strategies (Chapter 8C) and their approaches that have been designed to specifically assist small- and medium-sized enterprises (Chapter 8D).

The appendices following the body of the Report include a 2009 Ex-Im Bank transaction list showing the purpose of the Bank's support, Ex-Im Bank efforts to support renewable energy, and other materials intended to provide greater detail and insight.



# Chapter 2: Competitiveness Framework

## Section A: Factors Influencing Export Finance

### Introduction

This chapter provides the context for the environment in which ECAs operate. To understand how ECAs pursue their missions and make changes to operational strategies, one must understand the developments and trends of the wider world of export finance over the past several years.

Undoubtedly the most significant trend in the ECA world over the past decade has been the emergence of two philosophical camps among ECAs. On one side are the ECAs who maintain their position as a “lender of last resort,” playing a gap-filling role, and on the other are the ECAs who have adopted more private sector-oriented approaches to their export credit programs. The operational objectives, risk appetites, pricing and financial drivers of the two groups are quite different.

However, over the past two years, the financial crisis has affected how ECAs operate. With export finance struggling in the wake of the financial crisis, as trade flows shrank and credit markets evaporated, ECAs put their energy into ensuring exporters and lenders had access to ECA cover. This does not mean that the two camps moved closer together in terms of ideology and practice, but the traditional frameworks of all ECAs were tested and modified to meet the demands of both their governments and their exporters and banks. The divide between the groups blurred as each ECA worked diligently to do what they could to keep national exports alive. ECAs were put to the test in terms of their ability to step in and fill the gaps. As a result, ECAs generally became more aggressive and innovative in order to support their economies.

As ECAs found new relevance during the financial crisis, their activity levels increased across the board. There is no doubt that in a world which saw close to a 12 percent decrease in the volume of world trade in 2009, ECAs played an important role, along with other strategic measures imposed by their governments, in preventing the decline from sinking any further. However, it is still too soon to tell the impact the measures and actions taken by ECAs to “step-up” during the crisis will have on individual ECA competitive positions. It is also premature to establish how this newfound role of ECAs will play out in the long-run. Will the volumes sustain themselves at these higher levels or will ECAs eventually phase back to their traditional roles as lenders of last resort and quasi-market players? The single most likely factor will be the extent to which private lending and capital markets return to pre-crisis levels.

As the Competitiveness Report is written to reflect on practices and activities over the past year, the data and information in this report may show nothing more than how the export finance world has changed in light of the financial crisis. It is still too early to determine how the global economy will recover from the crisis and the role the ECAs will or will not play going forward in its revitalization.

## Export Trends

**Figure 1** illustrates the global export of goods over the last five years, with worldwide trade falling in 2009. The OECD countries still compose the most significant portion of world trade in goods and capital goods every year, with the exception of 2009 when global exports fell. While the BRICs were gaining an ever increasing share of world exports, in 2009, their share remained the same as in 2008.

**Figure 1: World Exports of Goods and Capital Goods, 2005 – 2009**

	2005	2006	2007	2008	2009*
<b>World</b>	\$9,951	\$11,541	\$13,183	\$15,112	\$12,102
<b>OECD</b>	\$6,323	\$7,149	\$8,068	\$8,968	\$7,100
<b>BRICS</b>	\$1,222	\$1,548	\$1,893	\$2,276	\$1,810
<b>Rest of World</b>	\$2,406	\$2,844	\$3,222	\$3,868	\$3,192
<b>Exports of Capital Goods (excl. autos)</b>					
<b>World</b>	\$3,853	\$4,443	\$4,878	\$5,306	N/A
<b>OECD</b>	\$2,638	\$2,985	\$3,211	\$3,458	N/A
<b>BRICS</b>	\$573	\$737	\$901	\$1,037	N/A
<b>Rest of World</b>	\$642	\$721	\$766	\$811	N/A
<b>OECD Exports/World Exports (%)</b>					
<b>Goods</b>	64%	62%	61%	59%	59%
<b>Capital Goods (excl. autos)</b>	68%	67%	66%	65%	NA
<b>BRICS Exports/World Exports (%)</b>					
<b>Goods</b>	12%	13%	14%	15%	15%
<b>Capital Goods</b>	15%	17%	18%	20%	N/A

Source: WTO Statistics and CIA Factbook

\*Preliminary Statistics

## Export Finance Trends

**Figure 2** shows that medium- and long-term G7 official export credit volumes grew at a significant rate of 43% from 2008 to 2009. France showed both the highest absolute level of support and the greatest increase in 2009 as compared to 2008 (a 154% increase). All of the ECAs other than Japan increased or maintained their level of support during 2009, representative of the role ECAs played during the financial crisis.



**Figure 2: New Medium- and Long-term Official Export Credit Volumes, 2005 – 2009 (\$US Billion)**

	2005	2006	2007	2008	2009*
<b>Canada**</b>	3.3	5.3	2.8	4.6	4.6
<b>France</b>	11.0	9.3	13.0	11.0	28.0
<b>Germany</b>	12.7	13.3	7.8	10.8	13.3
<b>Italy</b>	8.2	10.7	11.0	10.3	10.7
<b>Japan***</b>	8.4	6.0	0.9	1.1	0.6
<b>UK</b>	3.7	2.6	3.6	2.2	2.5
<b>US</b>	9.8	8.6	8.2	11.0	17.0
<b>Total G7</b>	\$ 57	\$ 56	\$ 47	\$ 51	\$ 77
<b>US % of G7</b>	17%	15%	17%	22%	22%
<b>BICs*</b>					
<b>Brazil</b>	3.5	7.5	7.0	NA	NA
<b>China</b>	18.5	29.0	38.0	59.6	NA
<b>India</b>	3.5	4.0	4.4	13.7	NA
<b>Total B,C,I</b>	\$ 26	\$ 41	\$ 49	NA	NA
<b>B,C,I % of G7</b>	45%	73%	104%	NA	NA

\*Preliminary estimates

\*\*Numbers are different from previous Competitiveness Reports as prior data included Canada's short-term and domestic financing figures. This data includes Canada's market window activity. For a breakout of official vs. market window please see Chapter 5B.

\*\*\*Part of Japanese reporting of export credit support has been modified; hence, comparison with years prior to 2007 is not possible

**Figure 3** shows that, as in 2008, 2009 overall capital flows into emerging markets continued to fall. However, as the global economy recovers, 2010 figures are projected to surpass the 2008 levels. It appears that 2009 saw the bottoming out of world-wide economic and market conditions and those markets are expected to rebound in 2010. Commercial banks retracted even more in 2009, and only the IFIs and equity investors surpassed their 2008 activity. These conditions illustrate the environment in which ECAs operated in over the past year.

**Figure 3: Net External Capital Flows into Emerging markets, 2005-2009 (\$US Billion)**

	2005	2006	2007	2008	2009*	2010**
<b>Official Flows</b>						
IFIs***	-39.0	-30.0	2.7	26.5	45.0	26.9
Bilateral Creditors	-26.0	-27.0	8.7	30.7	23.1	28.8
<b>Private Flows</b>						
Equity Investment	252.0	222.0	296.0	413.4	462.8	562.4
Commercial Banks	146.0	212.0	410.0	123.7	-60.0	54.5
Non-Banks	122.0	131.0	222.0	130.0	32.4	104.7
<b>Total</b>	<b>455.0</b>	<b>508.0</b>	<b>939.0</b>	<b>724.3</b>	<b>503.3</b>	<b>777.3</b>

Source: Institute of International Finance, "Capital Flows to Emerging Markets," January 2010

\* Indicates estimated figures

\*\* IIF projections

\*\*\* International financial institutions

### **Trends in 2009: Focus Group Discussions**

In general, lenders saw an increase in business in 2009 as compared to 2008, but their traditional role as the key source of financing for exports has not returned to "normal" levels. Lenders noted that ECAs salvaged orders that would have otherwise been cancelled. However, the result was not as consistent for exporters whose business trends either increased or decreased depending on the sector. For example, longer-cycle projects did very well due to the long lead time in contracts that had been signed well in advance of the financial crisis. However, shorter-cycle businesses suffered dramatic crashes.

Given the absence of liquidity in the markets, ECAs' financing remained critical and necessary in nearly every medium- and long-term transaction during 2009. Lenders noted that there was and continues to be an uptick in demand for deals with ECA financing. Prior to the financial crisis, banks rarely used ECAs, but during 2009, an ECA was involved in almost every transaction. Furthermore, commercial lenders are increasingly active in the emerging markets where buyers are being offered lines of credit from both OECD and non-OECD export credit agencies such as China.

Compared to 2008, liquidity premiums have decreased. However, the preoccupation of buyers is with availability of financing rather than price. The ECAs were commended by both focus groups for Ex-Im and other ECAs ability to step in and provide financing during the crisis. The lenders admitted, however, that Ex-Im's policies, such as MARAD, add additional costs to transactions (even if the product cost is higher in another country), and in their opinion the numbers generally work in favor of other ECAs regardless of Ex-Im's ability to make financing available.

Exporters expressed the same concerns noted by the lenders, but also believed that Ex-Im products such as direct loans, the "Take-Out" option, and capital markets financing were key competitive tools in 2009 as most other ECAs did not have such products.

Exporters felt that these options kept deals “in play”. On the other hand, lenders felt that EU countries’ interest make-up programs are more favorable to banks as they do not cut them out of the process.

While both groups commended Ex-Im for filling the gaps during the financial crisis, the lenders and exporters commented that they see a significant amount of global competition increasingly coming from non-OECD ECAs. As one exporter noted, “Ex-Im is still playing inside the sandbox while the East Asian ECAs are outside it.” This comment is indicative of the fact although the OECD ECAs were more aggressive and innovative in terms of their ability to finance transactions during the crisis, ECAs outside of the OECD, namely China, do not have to adhere to the “rules” and therefore offer financing packages outside of the purview of the OECD where Ex-Im and the G7 ECAs must compete. In addition, lenders also conducted a larger portion of their business with a number of the multilateral banks, noting that while they may be a bit more expensive, their processing time is much faster and more responsive.

### **Overarching Trends**

The biggest question today is what the role of ECAs will be once the international financial and credit markets finally settle down. The financial crisis brought ECAs to the forefront and they have played a critical role in keeping trade flows open. However, forecasting when and what will happen once liquidity returns to the markets and the private lending community gets back on its feet is difficult to predict. Furthermore, the full depth and breadth of the impact that the crisis has had on the two philosophical ECA models is not yet known, and may not be for several years to come.

The environment for ECAs is likely to remain uncertain for the foreseeable future. Clearly on the horizon is the near certainty that more stringent regulation of the international financial markets will be imposed: Basel III is well underway with potential implications for export credits, including ECA-backed export financing. Moreover, concern regarding country risks may be rising with the economic problems in Dubai and Greece, and the possible ripple effects these events could spawn.

Nevertheless, there are several underlying assumptions or influences that are likely to set the stage going forward. First, exports and their importance in sustaining and supporting economic growth is likely to get more attention as economies search for other engines and areas of growth beyond their national borders and capacities. Second, the ECAs and their guardian authorities, being ever more mindful of the chaos and the causes of that chaos they have just left behind, will be more risk and budget sensitive than before. More regulation of private financial services seems like an obvious factor that financial markets will have to address. Third, supporting domestic employment could become a more central driving force than before.

Taken together, these influences suggest that:

1. ECAs will be more important to private lenders that choose to stay in the export credit and project finance business, because without official support, facilities

guaranteed or insured by ECAs will be less risky and less costly and could be recognized as such by the regulators.

2. ECAs will be more selective in the risks they assume and the premia they charge, being mindful of WTO considerations, but will be aggressive within this milieu.
3. As governments focus more on exports as an important driver of economic growth, the ECAs could (a) push the pendulum more toward national exports (made in vs. made by); and (b) expand their range of products toward non-OECD Arrangement governed products such as untied loans, market windows and investment financing.
4. Non-OECD countries will continue pushing to expand their scope of influence and the methods they employ in order to gain greater global market share and dominance.

## Chapter 2: Competitiveness Framework

### Section B: ECAs' Mission and Place in Government

#### **The Role of Export Credit Agencies**

Traditionally, the purpose of an ECA has been to support the financing of domestic exports. In order to reach this goal, a number of ECAs have changed the scope of their export credit support. While the G7 ECAs must abide by the OECD Arrangement, which sets the most favorable financing terms and conditions that may be offered for official export credit support, each agency's operational structures differ greatly. As long as they stay within the parameters of the Arrangement, individual ECAs have the latitude to pursue their own national policies in support of their country's exports. However, the G7 ECAs also work under a second framework which is more ECA-specific: the ECA's mission as defined by its sponsoring government. This framework determines the extent to which an ECA is able to adapt its policies and operations to a changing landscape and what methods it is allowed to employ to continue to work toward its central goal. These factors define the parameters within which ECAs will compete with each other to facilitate domestic exports and to promote their respective governments' national interests.

#### **Ex-Im Bank's Mission and Place in Government**

As the official US Government ECA, Ex-Im Bank's mission and governing mandates are codified in Ex-Im Bank's congressionally approved Charter (Export-Import Bank Act of 1945, as amended). Ex-Im Bank's core mission is to support US jobs through exports by providing export financing that is competitive with the official export financing support offered by other governments. In addition, the Bank carries a mandate from the Federal budget's "financially self-sustaining" directive and WTO rulings to operate at break-even over the long-term. The Bank's core mission pursues the public policy goal of enabling market forces such as price, quality and service to drive the foreign buyer's purchase decision, not government intervention or the temporarily exaggerated perceptions of risk by private market participants. This public policy mission effectively directs Ex-Im Bank to fill market gaps that the private sector is not willing or able to meet: the provision of competitive financing (largely determined by interest rates and repayment terms) and the assumption of reasonable risks that the private sector is unable to cover at a moment in time.

To support its core mission, Congress has also legislated that Ex-Im Bank's financing be conditioned on:

- supplementing, not competing with, private sector financing; and
- the finding of reasonable assurance of repayment.

Decisions on transactions should be based solely on commercial and financial considerations, unless the transaction:

- fails to comply with Ex-Im Bank's Environmental Procedures and Guidelines;
- causes an adverse economic impact on the US economy; or
- does not meet various statutory and executive branch mandates.

All these directives aim to achieve common public policy goals and to reflect the interests of Ex-Im Bank's diverse stakeholders, such as NGOs (non-governmental organizations), other US government agencies, Labor, and financial intermediaries. Thus, Ex-Im Bank must constantly find and maintain a balance amongst its multiple, sometimes competing, goals and objectives. At the same time, Ex-Im Bank is expected to provide the US exporting community with financing that is competitive with officially supported offers made by foreign governments. Given the G7 ECAs' widely varying missions and operating strategies, comparing Ex-Im Bank's competitiveness vis-à-vis ECA counterparts requires a more comprehensive review that goes beyond the simple comparison of the cost aspects of financing programs and policies. Moreover, during the recent financial crisis, one of the most important functions of this report (and other monetary mechanisms) will be to identify whether there are any competitive consequences of amendments made to or the expansion of ECA mandates and the methods used to implement these revisions.

# Chapter 3: Core Business Policies and Practices

## Section A: Cover Policy and Risk-Taking

### **Introduction**

The extent to which an ECA provides official export support in any particular country serves as a traditional measure of official ECA competitiveness. Moreover, the breadth of markets and depth of risk appetite within specific countries further determine the competitiveness of an ECA. Thus, an ECA's competitiveness may be measured based on the number of countries in which it is "open" for business, the nature and level of risk within those markets, on what terms, and its willingness to take on new business with entities other than sovereign governments or first-class private institutions. It is important to note, however, that it is difficult to obtain comparable data in order to provide a comprehensive picture of ECAs' cover policies and risk appetites due to different reporting techniques and methodologies. Therefore, the data presented in this chapter is more indicative of overall trends rather than a precise measure of risk-taking.

As the financial crisis and relatively poor global economic conditions continued into 2009, the risk appetite of the private market continued to tighten. The lack of market liquidity, combined with a heightened sense of volatility, led to limited private lending capacity on behalf of commercial lenders.

At the same time, official ECAs were being called upon to step into the breach to fill the financing gap across all tenors (e.g., short-, medium- and long-term) of export credits. Many lenders would not lend without official ECA cover and many ECAs had to balance the pressure to bridge the "temporary" gap and the higher risk profiles of transactions with their long-term breakeven mandates. How ECAs chose to handle their response to the financial crisis is as varied as there are ECAs, but one thing they all had in common was the moral imperative to "step up" by their guardian authorities, their exporters, the global markets, and the multilateral institutions that play a multipurpose role (e.g., IMF, WTO, UNCTAD).

While Chapter 8 focuses on the broader impact of the financial crisis on ECAs' collective responses, this Chapter examines one aspect — the ability of ECAs to manage the wavering appetite for risk in this volatile world economy (as evidenced by where and how they conducted business during 2009).

### **Ex-Im Bank's Policy and Practice**

#### ***Sanctions***

Historically, Ex-Im Bank has been one of the leading ECAs in terms of the number of countries in which it is open, its overall willingness to take risk in these countries, and its appetite for non-sovereign business. Moreover, a factor that once negatively impacted Ex-Im's competitiveness in this area was the number of countries subject to

US sanctions barring Ex-Im Bank support. Since 2001, the number of countries with sanctions has gone down from 12 to 6 in 2009. In 2008, Ex-Im Bank had sanctions against providing support to the following countries: Burma, Cambodia, Cuba, Iran, North Korea, Laos, Sudan and Syria. This list was reduced in 2009, when the legislative restrictions on Cambodia and Laos were lifted.

### ***General Cover Policy and Risk-Taking***

Outside national policy considerations, Ex-Im cover policy is driven by the economic classification of countries and financial evaluations of non-sovereign borrowers. In 2009, Ex-Im was open for medium- and/or long-term cover in a total of 170 countries. Moreover, Ex-Im had a relatively well balanced portfolio across geographic regions in 2009. The portfolio was well spread over Asia/Middle East, the Americas, EU and Africa.

In terms of risk-taking, for borrowers to be eligible for cover they must meet the Congressional standard of a “Reasonable Assurance of Repayment” or RAOR. In 2009, out of the 274 cases meeting that standard, 90% or 246 of cases involved non-sovereign borrowers. The Ex-Im Medium-Term program continues to use the credit underwriting and due diligence standards instituted in 2008, referred to as “Know Your Transaction.” These stringent standards and procedures were put in place in an effort to avoid fraud and lower the claims rate in this area of the Bank’s business due to past problems with bad actors. As part of Ex-Im’s approach to risk taking in the medium-term, the Bank routinely applies credit enhancements in the form of security (e.g., liens, corporate/private guarantees, etc.). When undertaking high risk long-term transactions, the Bank compensates for the credit risk through different remunerations in the event of default such as the application of hard asset securities or offshore escrow accounts. Hence, although the Bank is open in a high number of countries (breadth of risk), these credit practices reflect a more cautious approach in the assumption of risk on a transaction by transaction basis (depth of risk). Due to the financial crisis, Ex-Im has tightened up its assessment of new risks, but only in specific markets and sectors, rather than making sweeping changes to the Bank’s overall risk assessment process.

### **G7 ECAs’ Policies and Practices**

It is not easy to compare Ex-Im’s cover policy country-by-country to the other G7 ECAs due to the difficulty of obtaining such data. However, on the risk-taking side, because of the financial crisis, 2009 forced most ECAs to reevaluate their risk assessment processes and risk monitoring procedures. For example, one ECA has modified its approach by opening up in several countries and are taking a more positive approach toward certain countries rather a more conservative view. However, various dialogues with the other G7 ECAs show that the majority of them have become more restrictive and risk averse, not only in their assessment of risks, but also in the monitoring of risks once transactions are approved. A closer eye is now being put on transactions in the underwriting process and also on the distribution of risk within ECAs portfolios. This is evident in the fact that in the past where ECA business was widely distributed among a



number of markets and risks, their activity is now concentrated more in high income OECD countries or less risky markets.

### **Exporter and Lender Survey and Focus Group Results**

The exporter and lender survey revealed frustrations over the fact that there are certain countries where other ECAs are open for business while Ex-Im remains closed. The focus groups believe that the Bank is slow and unresponsive to market changes and process of the Interagency Country Risk Assessment System (ICRAS) to rate countries is not timely. They argue that other ECAs can make changes to cover policy in a real-time manner relatively soon after market conditions change. There is also a general perception that US foreign policy dictates the countries in which the Bank will do business and that Ex-Im is becoming increasingly risk averse because of this.

Furthermore, for the Bank to reach RAOR, securities and other credit enhancements are applied to smaller medium-term transactions which increase the price of a transaction and the processing time. The exporters believe that other ECAs find ways to work in difficult markets, such as in Africa and Latin America, but Ex-Im continually denies cover for transactions in these countries even though the Bank is officially open.

### **Conclusion**

Based on the number of markets where Ex-Im is open and the breadth of Ex-Im's portfolio across markets in 2009, as well as the fact that the Bank has not dramatically tightened up its risk assessment processes due to the financial crisis as compared to the other G7 ECAs, the Bank appears to be relatively competitive vis-à-vis competitor ECAs. However, the perceptions of US exporters and lenders is that Ex-Im is relatively less competitive because of its stringent underwriting and security requirements especially for medium-term transactions, which prove to be costly and time consuming. Furthermore, Ex-Im is the outlier here because such requirements are an exception rather than a rule for how medium-term transactions are handled by the other ECAs. These factors hinder the Bank's ability to compete. Partially offsetting these factors is the breadth of markets in which Ex-Im Bank is open. Thus, the balance between the wide breadth of markets where Ex-Im will do business and a relatively narrower scope of risk-taking in the medium-term, suggests that, on balance, Ex-Im remained relatively competitive with the other G7 ECAs, a grade of "A-/B+".



# Chapter 3: Core Business Policies and Practices

## Section B: Interest Rates

### Introduction

Because of the use of interest rates as a competitive tool in the 1960s and 1970s, establishing minimum interest rates was the first topic taken up when the OECD Arrangement was created in the mid 1970's. Over time, the minimum official interest rate has become less of a competitive threat and more market-oriented. Nonetheless, interest rates can still be a competitive factor when ECA support is involved. Specifically, the quality of an ECA's guarantee or insurance when liquidity is an issue, or when a direct loan is unavailable, can affect the type and level of interest rates charged by a private lender.

Interest rates factor into ECAs' support in three ways: 1) the ECA lends directly to a borrower and charges the official minimum interest rate for the currency of the loan,<sup>1</sup> or 2) by providing interest make-up (IMU) support to a financial institution that agrees to provide a loan to a borrower at the official minimum interest rate. (IMU support guarantees a lender that its cost of funds will be covered if the minimum interest rate is lower than the lender's cost of funds); and 3) the market funding rate for "pure cover" support from an ECA. ECAs that offer "pure cover" provide a repayment guarantee or insurance to a lender willing to lend to a foreign borrower. The repayment guarantee or insurance promises the lender that, in the event the borrower fails to make a payment on the guaranteed/insured loan, the ECA will pay the lender the funds it lent and pursue collections from the foreign borrower.

Over the past decade, the demand for interest rate support (in the form of either direct lending or IMU) has been consistently low while pure cover has become the overwhelmingly dominant form of ECA support. In 2009 however, the demand for and use of ECA direct lending facilities and programs turned upward for the first time in over a decade. The cause of this sudden spike in direct loans is attributed to several factors related to the global financial crisis and recession. First, liquidity dried up and what funding was available was expensive. Private lenders, having to find new capital in a highly adverse environment, could not take on new assets while they were rebuilding their balance sheets. Export credit lenders would not provide funding with any uncovered risk; hence, a number of ECAs increased their pure cover amount from the standard 90% or 95% to 100% (same as Ex-Im) to incentivize private banks to provide the necessary funding. However, in many cases, the 100% guarantee was not enough, so deals either did not go forward at all, were highly priced and included a liquidity premium, or were supported by those ECAs who could offer a form of direct loan support that did not rely on the private lender for the actual funding.

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<sup>1</sup> These minimum interest rates, known as Commercial Interest Reference Rates (CIRRs), are market-related fixed rates calculated using a government's borrowing cost plus a 100 basis point spread. A CIRR is set for each currency based on the borrowing cost of the government that uses that currency; all ECA support for financing in this currency then utilizes the same CIRR.

## **Ex-Im Bank's Policy and Practice**

Since 1934, Ex-Im Bank has had a fixed-rate direct loan program. Ex-Im Bank's direct loan program provides the same coverage and repayment terms as is provided under Ex-Im Bank's pure cover programs, with the only difference being the interest rate. Under Ex-Im Bank's direct loan program, the interest rate is fixed at the time of first shipment at the then-current OECD minimum official interest rate (CIRR) for the US dollar. Under Ex-Im Bank's pure cover program, the interest rate is established by the lender and almost always starts as a floating rate. The rate will be based on LIBOR, the US prime rate, a commercial paper rate, equivalent Treasuries or any other relevant interest rate benchmark.

Ex-Im Bank allows the foreign borrower to determine whether to use the direct loan or pure cover program. Recently, borrowers have requested and used Ex-Im Bank's direct loan program because of the predictability and cost advantage associated with the direct loan (versus the guarantee plus the liquidity premium charged by the private lender) and because the borrower could lock in a fixed market-based rate for the term of the loan versus being subjected to an unpredictable floating rate that, in 2009, could only go up over time. This behavior is to be expected because during periods of rising interest rates, locking in a fixed rate is the likely low-cost option. However, in more stable environments, the private market – with an ECA guarantee and especially a 100% guarantee - is able to under-price with a floating rate that is less than the OECD CIRR fixed rate. Hence, the guarantee option has been the traditional option of choice for many years. While Ex-Im Bank approved only one direct loan during 2007, the Bank has seen a marked increase in the demand for direct loans throughout 2008 and 2009. In 2009, the Bank approved 21 direct loans for approximately \$5.5 billion.

Nevertheless, pure cover remained Ex-Im Bank's dominant form of medium-and long-term support in 2009, with the Bank authorizing 275 transactions for approximately \$12.2 billion. Consistent with recent years, the pure cover interest rates on the longer term, larger transactions were highly competitive with other G7 ECAs. Specifically, the introduction during 2009 of the "Take-Out" Option gave Ex-Im a unique advantage over other ECAs. The "Take-Out" Option gave commercial lenders who received a comprehensive guarantee from Ex-Im the option of having Ex-Im buy back loans should the lender find that its funding costs were changing or that funding was becoming unavailable. The option to sell the loans to Ex-Im helped keep the interest rates offered by lenders lower than they otherwise would have been because without the option to convert an Ex-Im guarantee to a direct loan, the funding and liquidity cost for the lender would be much higher. The "Take-Out" option, in effect, frees up lenders' liquidity should they need to utilize it; hence, by the lender knowing that it has the option to move the loan off of its books, it can charge lower spreads. The "Take Out" option also allowed lenders to use the acquired capital to engage in further lending or to minimize the risk of losses as a result of negative spreads.

Finally, through the use of its guarantee product, Ex-Im also facilitated a unique capital markets structure in which Ex-Im Bank's guarantee was directly placed on bonds issued in the capital markets (See **Chapter 4A - Aircraft** for more details). As a result, the

funding costs – backed by the full faith and credit of the US government – were clearly lower than the standard cost of funds.

Medium-term transactions supported under the Bank’s insurance and guarantee programs do **not** typically achieve rates as attractive as the long-term pure cover transactions. (The difference in interest rates between long-term, large transactions and medium-term, small transactions appear to be the result of commercial banks’ pricing strategies to account for higher overhead costs relative to larger, long-term transactions rather than a function of any Ex-Im Bank support element.) Since the onset of the financial crisis in September 2008, the lack of liquidity in the market has resulted in larger spreads being charged on Ex-Im Bank’s pure cover transactions, which may ultimately lead to an increase in demand for direct loans from Ex-Im Bank (and the other ECAs that offer direct loan products).

### **G7 ECAs’ Policies and Practices**

The G7 ECAs all offer the ability for exporters to access medium- and long-term fixed rate financing at CIRR levels. In addition, Japan, Canada and the US all offer a direct loan program, and Germany has a limited capacity to provide direct loans through KfW<sup>2</sup>. France, Italy and the U.K. offer IMU support. The other G7 ECAs, together with Ex-Im Bank, have provided the bulk of their support under their pure cover programs. However, the quality of their coverage (unconditional or conditional) and the percentage of cover differ from ECA to ECA. Anecdotal evidence indicates that interest rates achieved under the other G7 ECAs’ pure cover support varied widely during 2009.

### **Exporter and Lender Survey and Focus Group Results**

Lenders confirmed that the CIRR-based financing available through Ex-Im Bank’s direct loan program did compete with commercial bank financing during 2009. At the same time, lenders expressed their gratitude for the way that Ex-Im Bank temporarily provided financing when the commercial markets evaporated. In a similar way, exporters expressed satisfaction with the way that Ex-Im Bank stepped in to provide financing with competitive terms given the lack of availability and high pricing of commercial financing during the financial crisis.

### **Conclusion**

The interest rates that Ex-Im Bank has offered in recent years have been consistently equal to the average rates offered by the typical major ECA. During 2009, Ex-Im was able to offer rates on its direct loan program that were more competitive than other ECAs’ pure cover support. As a result of the “Take-Out” Option and the capital markets structure introduced during 2009, the interest rates generated under Ex-Im Bank’s long-term pure cover program were extremely competitive with those of other G7 ECAs given the current low interest rate environment. In the medium-term area, while the interest rates achieved with Ex-Im’s guarantee or insurance product were relatively

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<sup>2</sup> KfW’s program is discussed in further detail in chapter “5B: Market Windows”.

higher than for a long-term guarantee, these rates did not appear to be uncompetitive with other ECA-market generated rates. Rather, the issue with medium-term support appeared to be related to availability of financing instead of the price of financing. In 2009, Ex-Im Bank remained competitive with the other G7 ECAs on this feature, a grade of “A”.

# Chapter 3: Core Business Policies and Practices

## Section C: Risk Premia

### Introduction

To cover the risk of non-payment for a transaction, ECAs charge risk premia, otherwise known as exposure fees. In 1999, the OECD instituted the Knaepen Package which defined the elements for determining sovereign buyer fees and set Minimum Premium Rates (MPR) for sovereign buyer transactions. In order to level the playing field among ECAs, the MPR was developed. The MPR sets the floor for standard export credit pricing of sovereign buyers. Because there is currently no OECD system that specifically addresses non-sovereign buyers, the MPR also serves as the floor for fees of non-sovereign buyers. Over time, ECA business has become more concentrated with non-sovereign buyers; therefore the absence of a buyer risk system generated a push to develop a buyer fee structure, and update the MPR, at the OECD in 2008 when negotiations to create such a framework resumed.

Several elements determine the MPR: (i) the percentage of cover; (ii) the quality of the product; that is, whether the financing is an unconditional guarantee or conditional insurance; and (iii) the claims payment policy. The latter two factors determine whether a product is considered “above standard”, “standard” or “below standard.” Because coverage may differ based on these factors, the three types of products are priced differently, with “above standard” being the most expensive and “below standard,” the least expensive. These variations allow for surcharges or discounts based on the type of product to ensure a level playing field among ECAs. In addition, there are also surcharges and discounts that are applied when the cover differs from the typical 95% level of coverage. For example, for 100% cover, there is a surcharge between 5.3% and 14.3% depending on the risk level of the country; and for 90% cover, there is a discount of 5.4%. While the Knaepen Package establishes a floor for the fees ECAs charge, depending on an ECA's individual risk assessment, the ECA may add other surcharges to the MPR for sovereign risk transactions.

### Ex-Im Bank's Policy and Practice

Ex-Im Bank charges the MPR as set by the OECD for sovereign transactions. For non-sovereign transactions, Ex-Im Bank uses a rating methodology that cross-references a borrower's financial information to various financial indicators and takes into account various credit enhancements that may be applied to the case in order to reach a final rating. The process of rating buyers is unique to Ex-Im Bank due to the heterogeneous nature of the bulk of Ex-Im Bank's borrowers that tend to be smaller companies and/or companies not rated by credit rating agencies. If the borrower is rated equal to or better than the sovereign, then the applicable fee is the MPR. If the borrower is rated more risky than the sovereign, typically an incremental surcharge of 10-15% is added to the MPR.

## **G7 ECAs' Policies and Practices**

Like Ex-Im Bank, the G7 ECAs generally charge the MPR for sovereign transactions. However, risk-rating methodologies, use of risk mitigants, and pricing mechanisms vary widely among the G7 ECAs. As a result, there is a fairly wide divergence in the fees charged by G7 ECAs for similar non-sovereign transactions. The difference among ECAs in terms of experience, portfolios and philosophies generate this wide range in private buyer risk-rating and pricing. This was evidenced during the premia negotiations when different ratings for the same or similar buyers emerged.

The formal OECD discussions on a common approach to non-sovereign risk evaluation and fees resumed in June 2008, following an 18-month pause. The mandates to the OECD Premia Group of the renewed discussions were to recalibrate the MPR, institute a new non-sovereign buyer risk fee structure, and set parameters and benchmarks with which to price Category 0 (high-income OECD) countries. A final agreement was reached early in 2010 with the new agreement to go into effect by August 2011.

## **Exporter and Lender Survey and Focus Group Results**

The exporter and lender survey results indicated that Ex-Im's risk premium was generally competitive with other ECAs, although the exporters considered risk premium to be slightly less favorable than the lenders. The focus groups however, did not consider risk premia for both sovereign and non-sovereign to be a negative competitive issue for Ex-Im Bank. Hence, a reasonable conclusion can be made that exporters and lenders are by and large satisfied with Ex-Im Bank's exposure fees.

## **Conclusion**

While the 1999 Knaepen Package gave all OECD members access to a level playing field on sovereign risk premia, ECAs' disparate philosophies and financial objectives have resulted in a wide divergence in how ECAs approach risk-based pricing. Some ECAs treat the minimum premium more as a reference point (to which significant surcharges may be applied for any type of non-sovereign risk) than as a benchmark. In general, Ex-Im Bank's underwriting and claims experience enables it to typically price within a narrow band above the MPR while maintaining a better-than-breakeven portfolio. As a result, in 2009, Ex-Im premium rates were fully competitive with those of G7 ECAs, a grade of "A".



## Chapter 3: Core Business Policies and Practices

### Section D: Ex-Im Bank's Core Competitiveness

Overall, Ex-Im Bank's core business policies and practices were graded as generally competitive "A", meaning that Ex-Im Bank consistently offered terms that were equal to the average terms offered by the typical ECA such that the core policies and practices level the playing field with the standard ECA offer. **Figure 4** illustrates how Ex-Im Bank fared competitively on sub-elements of each policy or practice, in addition to an aggregate grade for each element. The grades are derived from both the survey and focus group results and the Bank's analysis of how it performed in comparison to its G7 counterparts.

**Figure 4: Grading of Ex-Im Bank's Core Competitiveness, 2009**

Key Elements	Grade
<b>Cover Policy</b>	<b>A-/B+</b>
Scope of Country Risk	A
Depth of non-sovereign risk	A-/B+
Breadth of availability (e.g., restrictions)	A-/B+
<b>Interest Rates</b>	<b>A</b>
CIRR	A
Pure Cover	A
<b>Risk Premium</b>	<b>A</b>
Sovereign	A
Non-sovereign	A
<b>Total Average Grade</b>	<b>A</b>



# Chapter 4: Major Program Structures

## Section A: Aircraft

### Introduction

Ex-Im Bank's support of US export sales extends beyond the standard support of capital equipment and includes the Bank's special financing programs that focus on a particular industry or financing technique. The section below discusses one of those types of programs: the Bank's support for the export of commercial and civil aircraft.

### OECD Aircraft Sector Understanding

Since the mid-1980s, large commercial aircraft that received ECA financing were governed by the OECD's Large Aircraft Sector Understanding (LASU) which established standard financing terms for the provision of export credit support for the sale of large aircraft. In 2001, negotiations on an updated Aircraft Sector Understanding (ASU) began with an expanded list of participants and types of commercial aircraft. The negotiations were focused on bringing the agreement up-to-date with the aircraft financing practices used in the 21<sup>st</sup> century. It also sought to include a wider group of ECAs that support aircraft exports - Brazil and Canada - and incorporate the diverse types of aircraft financing disciplines. After a number of years, the negotiations concluded and a new agreement was signed in July 2007. The ASU was agreed to by the Participants to the Arrangement and also by Brazil who is a Participant to this agreement only and not to the overall OECD Arrangement. The ASU, like the LASU before it, sets out the maximum repayment terms, minimum exposure fees and minimum interest rates that an ECA can charge for all non-defense aircraft finance transactions

The ASU has several notable characteristics that are summarized below.

**Classifies civilian aircraft into three types:** (1) Category 1: large commercial aircraft; essentially, almost all Boeing and Airbus aircraft are termed by the ASU as Category 1 aircraft; (2) Category 2: Regional aircraft (props and jets) that are made by, for example, Bombardier (Canada) and Embraer (Brazil) are considered to be Category 2 aircraft; and (3) Category 3: smaller aircraft such as helicopters, executive jets, and agricultural aircraft that are made by a wide variety of manufacturers.

**Risk Classified Obligors:** The ASU requires that each obligor be assigned a risk rating. This risk rating must be agreed to by all Participants to the ASU and is used to determine the exposure fee for the obligor.

**Repayment Term:** The maximum repayment term is determined by the type of aircraft:

- Category 1 aircraft: 12 years
- Category 2 aircraft: 15 years
- Category 3 aircraft: 10 years

While the ASU became effective in July 2007, a clause was included in the agreement that allowed any Category 1 aircraft under a firm contract that was concluded by April 30, 2007, and scheduled for delivery by December 31, 2010, to be grandfathered under the terms of the old LASU. As a result, an overlap exists between the two agreements in which some aircraft, mainly Category 1, can be financed under the LASU while other aircraft must be financed under the ASU depending on the original delivery date.

By the end of 2009, however, the ASU was put to a test due to the inability of the ASU's Participants to agree upon the proper classification of a new family of aircraft, the C-Series, developed by Bombardier of Canada. The difficulty in reaching consensus as to which category of aircraft the C-Series should be placed led the Participants to decide to renegotiate the ASU starting in 2010.

### Large Commercial Aircraft Industry in 2009

**Figure 5** illustrates the devastating effects that the economic slowdown continued to have on aircraft orders in 2009. While the period between 2005 and 2007 represents a record setting pace for orders, 2008 witnessed a steep drop of 48% from 2007 that was followed by an even greater decline of 69% in 2009. Boeing received 142 net commercial airplane orders during 2009, while Airbus had 310 orders for the year. As worldwide liquidity tightened and economic conditions deteriorated, many orders were either delayed or cancelled.

**Figure 5: Number of Large Commercial Jet Aircraft Orders**

	2005	2006	2007	2008	2009
<b>Boeing</b>	1002	1044	1413	662	142
<b>Airbus</b>	1055	824	1341	777	310
<b>Total</b>	2057	1868	2754	1439	452

Source: [www.boeing.com](http://www.boeing.com), [www.airbus.com](http://www.airbus.com)

As illustrated in **Figure 6**, however, Boeing's deliveries remained strong with foreign buyers representing 74% of deliveries in 2009.

**Figure 6: Number of Boeing Commercial Jet Aircraft Deliveries**

	2005	2006	2007	2008	2009
<b>Domestic</b>	135	167	154	140	125
<b>Foreign</b>	155	221	287	235	356
<b>Total</b>	290	388	441	375	481
<b>Foreign as % of Total</b>	53%	57%	65%	63%	74%

Source: Boeing Corporation

The increased number of deliveries that Ex-Im Bank financed during 2009 is largely a result of the funding gap that existed. The funding gap at the beginning of 2009 was estimated at approximately \$10 billion but was filled by ECAs who stepped in as the private market was in retreat. ECA financing in 2009 represented roughly 40% of the total market for aircraft financing. Expectations for 2010 remain that a funding gap will persist. Ex-Im supported exports of large aircraft worth approximately \$11 billion during 2009; a number that is expected to be matched or even exceeded by the end of 2010. While commercial banks are showing a renewed willingness to lend to certain airlines, and capital markets are slowly returning, those airlines that are still affected by difficult market conditions and who have not seen improving financial metrics will again be restricted in accessing commercial financing.

### **Ex-Im Bank's Policy and Practice**

During 2009, Ex-Im stepped up and played the crucial role for which it was designed: providing financing on a counter cyclical basis when the private market is unable to meet the demand. The financial crisis that started affecting aircraft financing during the second half of 2008 continued throughout 2009. Ex-Im supported a record volume (\$11 billion) of aircraft transactions as a result of the liquidity shortages in the private market. At the beginning of 2009, banks remained hesitant to lend. When banks were lending for aircraft transactions, albeit on a limited basis, spreads were at historically high levels. As the year progressed, spreads were reduced as new lenders entered the market. By the end of 2009, margins remained higher than under normal market conditions but the liquidity problems that were seen at the end of 2008 and beginning of 2009 were witnessing a vast improvement.

In response to the difficult market conditions of 2009, Ex-Im introduced two new financing options intended to simultaneously increase liquidity and lower the cost of borrowing. First, Ex-Im introduced the "Take-Out" Option that gave lenders who received a comprehensive guarantee from Ex-Im the option of having Ex-Im buy back loans from the lender should the lender find that its funding costs were changing or that funding was becoming unavailable. This option to sell the loans to Ex-Im gave the lender the flexibility to use the acquired capital for additional lending needs and to minimize or eliminate the risk of losses due to a negative spread by selling it to Ex-Im Bank.

Additionally, Ex-Im also introduced a capital markets funding option for aircraft transactions. Instead of providing a guarantee on a loan made from a commercial bank,

Ex-Im guaranteed a bond issued in the capital markets and funded mostly by institutional investors. This structure created an alternative source of funding during the difficult lending environment dominant throughout 2009.

In addition to the financing terms and structures noted above, Ex-Im Bank also offered co-financing support for US aircraft sales such that Ex-Im Bank and another ECA could offer support for their respective portions of the sale. For example, Boeing 777s may have British engines, and Boeing 777s and 787s can use Japanese airframe components. In 2009, Ex-Im supported 14 co-financed aircraft transactions with Japan, Korea and the U.K.

In 2009, Ex-Im Bank approved 36 large aircraft transactions worth nearly \$11 billion, over half of Ex-Im's medium- and long-term authorizations, covering 156 aircraft. Of those 36 transactions, 8 were financed in a foreign currency (i.e. Euros). Ex-Im also supports smaller, category 3 aircraft that include business and agricultural aircraft. In 2009, Ex-Im approved 26 category 3 transactions worth approximately \$700 million, 11 of which were co-financed transactions predominantly with Export Development Canada (EDC).

Another special feature available for aircraft transactions involves an OECD-allowable discount on the exposure fee for airlines in countries that have ratified the Cape Town Convention (CTC)<sup>1</sup> and have made the necessary declarations. In 2009, Ex-Im Bank continued its policy of giving a one-third discount to the exposure fee for transactions grandfathered under the LASU agreement. For those aircraft covered under the ASU, a CTC discount in the range of 5% to 20% was offered. The following airlines were some of the beneficiaries of the CTC discount during 2009: Air India Charters (India), COPA (Panama) and NACIL (India).

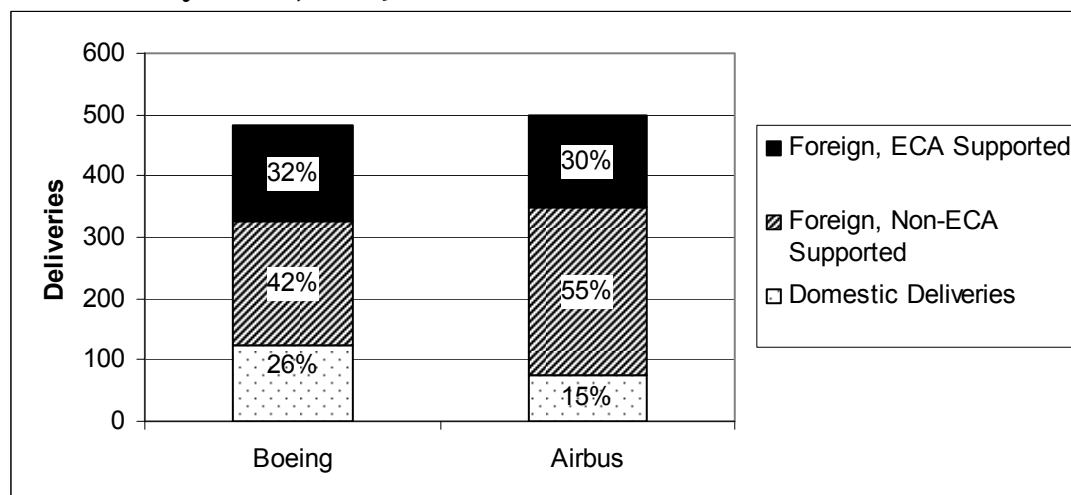
## **G7 ECAs' Policies and Practices**

In 2009, the Airbus ECAs (Coface/France, EulerHermes/Germany, and ECGD/UK) supported an estimated 149 Airbus aircraft delivered during the year for a total of approximately \$10 billion. **Figure 7** (below) illustrates the distribution of each large aircraft manufacturers' deliveries between domestic and export sales with and without ECA support. The figure shows that Airbus has a higher proportion of export sales (85%) as compared to Boeing (74%). **Figure 7** also shows that 32% of all of Boeing's deliveries were financed by Ex-Im Bank while 30% of all Airbus deliveries were financed by the Airbus ECAs. Of the Airbus aircraft that were exported during 2009, 35% were financed with ECA support (150 out of 425 aircraft). This compares to Boeing aircraft where 43% of exported aircraft (154 out of 356 aircraft) were supported by Ex-Im Bank.

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<sup>1</sup> The following countries have ratified the Cape Town Convention and made the necessary qualifying declarations to be eligible for Ex-Im Bank's Cape Town discount as of December 2009: Afghanistan, Angola, Bangladesh, Cape Verde, Ethiopia, India, Indonesia, Kenya, Luxembourg, Malaysia, Mongolia, Oman, Pakistan, Panama, Senegal and South Africa.

**Figure 7: Percentage of Total Large Commercial Aircraft Deliveries Financed by ECAs, 2009**



Source: Boeing Corporation, Airbus data based on limited information from [www.airbus.com](http://www.airbus.com) and press reports.

### Exporter and Lender Survey and Focus Group Results

Overall, exporters and lenders involved in large aircraft exports found Ex-Im Bank highly competitive compared to other ECAs. Lenders believe that the creativity exhibited by Ex-Im Bank in structuring aircraft transactions during 2009 was an important aspect that enabled deals to be completed under difficult financial conditions. Despite the positive steps that were taken to provide financing for exports of large aircraft, concerns were expressed in the survey that the Bank's foreign content requirement continues to negatively impact the Bank's competitiveness, as the Airbus ECAs do not have similar restrictions on foreign content. Although some of the negative impact has been mitigated by co-financing arrangements with other ECAs, there remains the potential that Ex-Im Bank may not be able to support aircraft if one of the co-financing partners steps away from a transaction.

### Conclusion

Ex-Im Bank continues to provide financing terms that are equal to the best terms provided by the Airbus ECAs under the LASU and ASU. The creative approaches to transaction structures together with timely responses to the financial crisis has kept Ex-Im Bank strongly competitive while ensuring that the Bank's overall package of support provides for a level playing field. On balance, Ex-Im Bank is generally competitive compared to the Airbus ECAs, a grade of "A".





## Chapter 4: Major Program Structures

### Section B: Project Finance

#### Introduction

Project Finance (PF) is defined as the financing of projects whose creditworthiness depends on the project's cash flow for repayment. With such a structure, the lender cannot access the assets or revenue of the project sponsor to repay the debt and only has recourse to the assets and revenue generated by the borrower (i.e., the project being financed). PF structures usually cover large, long-term infrastructure and industrial projects.

In 2009, total global PF debt issuances witnessed a decline to \$224 billion after increasing to \$251 billion in 2008, up from \$226 billion in 2007. The total number of OECD project finance deals notified in 2009 (as required by the OECD Agreement for project finance) increased noticeably, from 15 in 2008 to 21 in 2009. Initial information indicates that contract amounts for deals notified in 2009 totaled approximately \$11 billion (compared to \$3.4 billion in 2008), representing over a 200% increase in dollar terms for project finance transactions compared with 2008.<sup>1</sup>

**Figure 8** illustrates the involvement of ECAs in project finance transactions from 2007 to 2009. ECA participation as a percentage of total PF loans (based on dollar volume) averaged 1.4% during 2007 and 2008. However, with reduced liquidity during the difficult market conditions seen throughout 2009, ECA involvement in PF transactions increased to 5% of total PF loans.

**Figure 8: Distribution of PF Loans by Originator, 2007-2009 (\$US Billion)**

	OECD ECAs (excluding Ex-Im)	Ex-Im Bank	All OECD ECAs	Private Lenders	Total
<b>2009</b>	\$7.5	\$3.6	\$11.1	\$212.8	\$223.9
<b>2008</b>	\$2.9	\$0.5	\$3.4	\$247.2	\$250.6
<b>2007</b>	\$2.6	\$0.6	\$3.2	\$223.0	\$226.2

Source: Dealogic, January 2010. The total volume of ECA project finance deals comes from the OECD.

While private financing by commercial lenders and other capital market players clearly continued to dominate PF activity in 2009, Ex-Im was frequently called upon to fill funding gaps in project finance transactions where private sector debt was no longer

<sup>1</sup> The ECA project finance deals are those reported by the OECD ECAs and may not include all ECA project finance deals completed in 2009. Further, they include only those OECD notifications that became authorized transactions.

available. Ex-Im's deal flow increased significantly during 2009 with as many as fifteen active applications in the Bank's pipeline at one time. ECAs and Ex-Im in particular, stepped into a number of project finance transactions throughout 2009 which enabled deals to reach completion that otherwise would have suffered from a funding gap.

Other changes to the PF environment occurred during 2009. Due to financing difficulties associated with the financial crisis, starting in January (of 2009), the OECD instituted temporary flexibility on maximum repayment terms for transactions in high income OECD countries, allowing repayment terms up to 14 years (compared with 10) so long as ECA participation constituted more than 35% but less than 50% of the syndication.

### **Ex-Im Bank's Policy and Practice**

Ex-Im Bank authorized 6 PF transactions in 2009, after having one PF authorization in 2008. However, considering the recent blurring of the line between project and structured finance, these figures account for only part of Ex-Im Bank's activity in this area. Traditional PF transactions create a new company via a special purpose vehicle ("SPV") which establishes and owns the project as well as acts as the borrower. These transactions rely on repayment from revenue generated by the project alone. (PF transactions generally require an average of 8 to 12 months to complete). *Structured* finance transactions generally involve large expansions of companies where repayment is derived from a combination of reliance on the existing company's balance sheet as well as on future revenues resulting from the expansion project. However, in cases where the success of the expansion is integral to the survival of the existing company, they could just as easily be considered "project finance." With this in mind, in 2009 Ex-Im Bank authorized 7 structured finance transactions totaling \$2.5 billion, compared to 10 totaling \$1.5 billion in 2008.

In general, there are five core factors that characterize Ex-Im Bank's competitiveness in project finance transactions. These include: (1) 100% (of 85% of the US supply contract) US government-guaranteed support for all risks (political and commercial) during both the construction and repayment periods; (2) financing of local costs (up to 30% of the amount of US export contract); (3) willingness to utilize the project finance flexibilities provided by the OECD Arrangement with respect to pricing and repayment terms; (4) willingness to capitalize interest during construction; and (5) a reasonable and pragmatic commercial approach to project analysis and risk mitigation.

At the same time, transactions using Ex-Im Bank's PF program can be constrained by a variety of non-financial requirements that other ECAs do not have, including the Bank's content policy, shipping requirements, and economic impact analysis (see the Foreign Content, US Shipping Requirements, and Economic Impact sections in Chapter X for more detail). These policies can negatively impact actual and *potential*<sup>2</sup> PF transactions

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<sup>2</sup> The distinction between *potential* cases brought to Ex-Im Bank (as opposed to actual cases supported by Ex-Im Bank) is an important one. Potential cases are those transactions which are brought to Ex-Im Bank and worked on by the Bank but which are not ultimately supported by the Bank. Potential cases do not include transactions that could have come to Ex-Im, but did not.

more than other types of transactions for two reasons. First, PF sponsors can choose among several sourcing alternatives from around the world, making the cost and quality of competition the most sensitive and intense factor when making the financing decision. Any extra costs or delays associated with a financing source can cause the project sponsor to look elsewhere for funding. Second, the desire of project sponsors to minimize the number of sources of financing gives an advantage to other ECAs with less restrictive content or shipping requirements.

## **G7 ECAs' Policies and Practices**

Compared with Ex-Im Bank, the other G7 ECAs offer broadly similar coverage for PF transactions with some minor differences in the quality of the guarantee. While these quality differences have largely disappeared as other ECAs – including SACE (Italy), ECGD (UK) and JBIC (Japan) – have moved to 100% unconditional guarantees, EDC provides direct loans, and the other two G7 ECAs (Coface/France and Euler Hermes/Germany) provide conditional insurance. In addition, though not exclusive to Project Finance but used most often in PF transactions, are the OECD compliant features of local cost support of up to 30% of the contract value and capitalized interest during the construction period that are utilized by all of the G7 ECAs.

## **Exporter and Lender Survey and Focus Group Results**

Exporters and lenders rated Ex-Im Bank's Project Finance operations as generally competitive in 2009. However, the particular issues of MARAD and content continue to affect Ex-Im financing for many possible PF deals. Specifically, Ex-Im Bank's foreign content rules, when applicable, act as a further obstacle for foreign buyers and US multinational exporting companies, forcing them to consider sourcing from overseas where content requirements by other ECAs are less onerous. Exporters indicated their interest in seeing Ex-Im Bank broaden its content policy beyond the narrowly defined "made in" US requirement. Some companies choose to avoid Ex-Im Bank financing altogether due to the burden involved with tracking content and the associated exporter certification requirements.

## **Conclusion**

The core aspects of Ex-Im Bank's PF offerings continue to be competitive with other G7 ECAs. At the same time, the increase to 100% unconditional guarantees by Ex-Im's competitors means the Bank is on more equal footing in its basic PF offerings. Additionally, Ex-Im's public policy requirements (foreign content policy, shipping requirements and economic impact analysis) can have an adverse impact on the competitiveness of PF transactions when present in a transaction (See Chapter 6 for details on these public policy issues). However, Ex-Im Bank's grade for Project Finance stands at an "A" (competitive with the G7 ECAs) as the public policy issues are not factored into the PF grade but instead are addressed individually in their respective chapters.



# Chapter 4: Major Program Structures

## Section C: Co-Financing

### Introduction

“Co-financing,” “reinsurance,” and “one-stop shop” address some of the financing challenges posed by multi-sourcing. These terms refer to financing arrangements that allow an exporter to market a single ECA financing package to a buyer interested in procuring goods and services from two (or more) countries. Without co-financing, foreign buyers would need to secure multiple financing packages and would incur additional expense and administrative burden to ensure ECA support for exports from various countries.

With co-financing, the lead ECA provides the applicant (buyer, bank or exporter) with export credit support for the entire transaction. Behind the scenes, the follower ECA provides reinsurance (or a counter-guarantee) to the lead ECA for the follower ECA’s share of the procurement. The country of the largest share of the sourcing and/or the location of the main contractor generally determines which ECA leads the transaction. The lead ECA is able to provide a common documentation structure, one set of terms and conditions, and one set of disbursement procedures for the entire transaction. All parties benefit from the administrative ease of a streamlined financing package. The surge in use of Ex-Im Bank co-financing agreements evidences that availability and ease of ECA co-financing have become important and measurable competitive issues.

### Ex-Im Bank’s Policy and Practice

Ex-Im Bank introduced the co-financing program in 2001 with the signing of its first bilateral agreement with ECGD (UK). Since that time, Ex-Im Bank has signed ten co-financing agreements<sup>1</sup> and approved case-specific co-financing arrangements on a transaction basis with OECD ECAs with whom Ex-Im Bank does not have an overall co-financing framework agreement. Ex-Im Bank has not signed any co-financing agreements with ECAs in the BRIC countries or Mexico, but could consider individual requests to co-finance with these ECAs on a case-by-case basis.

In 2009, Ex-Im Bank experienced a dramatic increase of over \$2 billion in the volume of aircraft co-financing transactions. This increase is consistent with the spike in aircraft financing attributable to commercial lending liquidity constraints prompted by the financial crisis. Thus, aircraft continues to lead the co-financing program as it constitutes the majority of the overall number and volume of activity in 2009. As such, almost \$6 billion or over 90% of the volume of all 2009’s co-financed transactions involved some type of aircraft. Specifically, Ex-Im Bank provided co-financing support for 14 large or OECD Category 1 aircraft and 10 small Category 3 aircraft transactions,

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<sup>1</sup> Ashr’a (Israel), Atradius (The Netherlands), Coface (France), ECGD (UK), EDC (Canada), EFIC (Australia), Hermes (Germany), KEXIM (Korea), NEXI (Japan), and SACE (Italy).

including agricultural aircraft. In the majority of the aircraft transactions, without co-financing, the exporter would not have been able to offer the maximum 85% support to its customers in one financing package. Thus, co-financing allowed Ex-Im and NEXI to level the playing field by acting like the Airbus ECAs do in terms of their seamless financing for the European-based commercial aircraft manufacturer.

With respect to non-aircraft transactions, although they continue to form a small part of the overall Ex-Im Bank co-financing portfolio, the number of transactions almost doubled – to 12 transactions – up from the 7 non-aircraft co-financed transactions that Ex-Im Bank reported in 2008. The transactions totaled almost \$450 million and included large projects involving oil and gas as well as power production in addition to the medical equipment transactions that typically populate the non-aircraft data set.

Taken together, the volume of co-financing authorizations in 2009 increased by 50% to almost \$6.5 billion involving a total of 34 transactions (compared to 26 transactions totaling \$4.3 billion in 2008). Large commercial aircraft sales represented the lion's share of the total, upwards of 90% of the total dollar amount of co-financing, and accounted for about 70% of these transactions in terms of number (24 out of 34). About 80% of all transactions were co-financed with G7 ECAs. (See **Figure 9** for a complete listing of the specific transactions).

Ex-Im Bank was the lead ECA in all of the co-financing transactions authorized in 2009. Ex-Im Bank continues to seek opportunities to co-finance as a follower ECA, but has not yet gained much experience in that capacity. A possible reason why Ex-Im Bank has had such a limited role as a follower ECA include Ex-Im Bank's up-front documentary requirements, which the Bank would require even as a follower, whereas the other ECAs are willing to follow without these requirements. Part of the difference lies in the product type: Ex-Im's ECA counterparts offer export credit insurance which by definition does not require upfront review of documents. Ex-Im Bank's co-financing program is a guarantee program that does require upfront document review and because Ex-Im has not been willing to forego these requirements (to the extent the Bank can legally forego them), the Bank's operational mechanics do not match that of the Bank's ECA partners. Reconciling the documentary issues when Ex-Im Bank is acting as a follower ECA has clearly been more burdensome to exporters than working with Ex-Im's ECA counterparts on deals where the Bank is the lead ECA (and little, if any, exporter contact with the foreign ECA is required). Such an onerous process is considered a disincentive to working with Ex-Im's co-financing program structure. Such a restriction has caused delays in the processing of co-financed transactions and at least one transaction where Ex-Im Bank is being asked to follow continues to languish in-house.

**Figure 9: Ex-Im Bank Co-Finance Transactions, 2009 (\$US million)**

<b>Ex-Im Bank &amp; Co-Financing ECA</b>	<b>Market</b>	<b>Project</b>	<b>Financed Amount*</b>
EDC	Brazil	Agricultural Aircraft	\$0.7
EDC	Brazil	Agricultural Aircraft	\$0.7
EDC	Brazil	Agricultural Aircraft	\$0.6
EDC	Brazil	Agricultural Aircraft	\$0.6
EDC	Brazil	Agricultural Aircraft	\$1.3
EDC	Argentina	Agricultural Aircraft	\$1.3
ASHR'A	China	Agricultural Equipment	\$10.0
ASHR'A	Azerbaijan	Agricultural Equipment	\$5.2
EDC	Mexico	Aircraft Manufacturing	\$2.1
EDC	Turkey	Construction Equipment	\$1.3
EDC	Brazil	Construction Equipment	\$0.6
NEXI	Panama	Cranes for Construction	\$2.1
KEXIM	South Korea	Large Aircraft	\$285.8
NEXI	India	Large Aircraft	\$2,012.1
NEXI	United Arab Emirates	Large Aircraft	\$468.2
NEXI	United Arab Emirates	Large Aircraft	\$139.9
NEXI	United Arab Emirates	Large Aircraft	\$322.8
NEXI	United Arab Emirates	Large Aircraft	\$325.6
NEXI	United Arab Emirates	Large Aircraft	\$144.5
NEXI	Netherlands	Large Aircraft	\$142.3
EDC	India	Executive Aircraft	\$19.7
NEXI	United Arab Emirates	Large Aircraft	\$151.1
NEXI	Chile	Large Aircraft	\$242.6
NEXI	United States	Large Aircraft	\$1,241.4
NEXI	Hong Kong	Large Aircraft	\$410.2
EDC	Argentina	Large Aircraft	\$1.2
Euler Hermes	Brazil	Medical Equipment	\$1.6
Euler Hermes	Brazil	Medical Equipment	\$2.0
Euler Hermes & ECIO	Israel	Oil Refinery	\$300.7
EKF	Turkey	Power Plant	\$104.8
SACE	Trinidad and Tobago	Small Aircraft	\$79.7
EDC	Kenya	Small Aircraft	\$5.2
EDC	Brazil	Small Aircraft	\$1.0
EDC	Brazil	Small Aircraft	\$0.7
<b>TOTAL</b>			<b>\$6,429</b>

Source: Ex-Im Bank

\*The financed amount includes financed exposure fee

## G7 ECAs' Policies and Practices

The G7 ECAs have multiple framework agreements among themselves (as shown in **Figure 10**) and have been processing co-financed transactions since 1995. These agreements were originally designed to help European ECAs manage their exposure because many had country limits that made it impossible for them to provide support for exports to riskier markets or to markets where the ECA was close to reaching its country limit. Even in an environment of increasingly liberalized foreign content allowances, co-financing helps achieve operational efficiency and risk management in a world of multi-sourcing.

Unlike most other ECAs, Ex-Im Bank does not require a formal bilateral framework agreement before considering co-financing transactions. In 2009, Ex-Im Bank supported one co-financing deal under a one-off co-financing agreement that involved reinsurance from EKF (Denmark) to support a power plant in Turkey. <sup>2</sup>

**Figure 10: G7 Co-financing Agreements, 2009**

	Ex-Im	ECGD	EDC	Euler Hermes	COFACE	SACE	NEXI
Ex-Im		X	X	X	X	X	X
ECGD	X		X	X	X	X	
EDC	X	X		X	X	X	
Euler Hermes	X	X	X		X	X	X
COFACE	X	X	X	X		X	X
SACE	X	X	X	X	X		X
NEXI	X			X	X	X	

Source: Ex-Im Bank

## Exporter and Lender Survey and Focus Group Results

Participants were “encouraged” by Ex-Im’s willingness to engage in co-financing as both a lead and follower ECA. Moreover, exporters have indicated that the utility of Ex-Im Bank’s co-financing agreements is particularly high due to Ex-Im Bank’s restrictive content policy. That is, co-financing allows Ex-Im Bank to participate with other ECAs on the non-US content portion and provide a streamlined-financing package to multiple buyers that would otherwise need to apply for and execute multiple financing arrangements with various ECAs, whereas without the co-financing option, Ex-Im would be limited to supporting only the US portion and run the risk of the US exporter not winning the sale because the ECA supported portion was either insufficient or the terms and conditions were vastly different, inconvenient and more costly for the borrower.

Exporters and lenders gave Ex-Im Bank modest grades for co-financing stating dissatisfaction with Ex-Im Bank’s lack of willingness to consider additional co-financing

<sup>2</sup> In an effort to expand its partnerships with financial institutions, including ECAs, Ex-Im Bank has sought to work with EKF and other ECAs to promote US exports through collaboration to ensure financing availability for export transactions involving US suppliers.



agreements, particularly with Mexico and the BRIC countries. In this regard, the respondents noted that co-financing with the BRICs has not been made a priority at the Bank despite some case-specific requests. Exporters suggest that case-by-case reviews of such requests are too onerous and that individual transaction timelines cannot accommodate the time Ex-Im Bank needs to decide whether and how it could proceed with the co-financing request. In addition, exporters complained about Ex-Im Bank's significantly limited co-financing activity as a follower ECA and the Bank's unwillingness to streamline the up-front documentary requirements where possible to more closely match those of the partner ECAs.

## **Conclusion**

Although in prior years Ex-Im Bank has been viewed as less than competitive in co-financing, in 2009 Ex-Im Bank's co-financing program has achieved record success, demonstrated by the high volumes of activity and increased use across sectors. This increased activity brought on, in part because of new bilateral agreements concluded in late 2008, raises the grade up to an "A-/ B+" (up from last year's "B") and may reflect exporter need for greater coverage of multi-sourced transactions in addition to increased awareness of its availability, notwithstanding certain limitations that hinder a fully competitive performance in the area of co-financing. Nevertheless, co-financing represents an important competitive tool for US exporters to use as they rise to the increasing challenge to export more.



# Chapter 4: Major Program Structures

## Section D: Environment

### **Introduction**

In an effort to address concerns regarding the environmental impacts associated with Ex-Im Bank financing of large-scale projects in developing countries, Congress added a provision to the Ex-Im Bank Charter in 1992 requiring the Bank to “establish procedures to take into account the potential beneficial and adverse environmental effects of goods and services for which support is requested”. Congress instructed Ex-Im Bank to implement this effort in a manner that would be consistent with its mandate to foster expansion of US exports. Since that time, Ex-Im Bank has worked with the exporting community, non-governmental organizations and international financial institutions to establish and update an environmental review framework for export credit agencies charged with promoting exports.

### **Ex-Im Bank’s Policy and Practice**

Ex-Im Bank’s 1992 Charter language authorized the Bank’s Board of Directors to grant or withhold financial support for transactions after taking into account the environmental effects of those transactions. In response to this language, in 1995, Ex-Im Bank became the first ECA to introduce Environmental Procedures and Guidelines (EPG) to its transaction review process. The EPG established a process for Ex-Im Bank to screen and categorize applications for exports into projects based on the potential environmental impacts of the project. Ex-Im Bank’s EPG describe the nature of environmental reviews that it will undertake in conjunction with its various financing programs, and they set forth the information requirements needed to conduct the reviews. Finally, the EPG establishes the scope of environmental requirements that are applicable to the various types of projects for which financing is requested. Ex-Im Bank staff is charged with reviewing the environmental impacts of proposed projects against the EPG, and recommending approval, approval with conditions, or denial of such projects to the Ex-Im Bank Board of Directors. The Charter authorizes the Board of Directors, in its judgment, to grant or withhold financing support after taking into account the beneficial and adverse environmental effects of proposed transactions.

In the spirit of promoting transparency, Ex-Im Bank was the first ECA to make environmental assessment information about those projects for which it had received a final application for financing publically available. Subsequently, in 2006, Congress increased Ex-Im Bank’s transparency requirements, mandating that the Bank disclose supplemental environmental reports, including monitoring and mitigation plans, following action to approve Bank financing. This provision has become a source of competitive concern among exporters dealing with some buyers and borrowers who are either reluctant or unable to agree to make available certain environmental monitoring information for public scrutiny.

In 1998, Ex-Im Bank became the first ECA to voluntarily track and publicly disclose estimates of greenhouse-gas emissions of fossil fuel projects for which it is providing financing, and in 2009, Ex-Im Bank was the first export credit agency to approve a Carbon Policy.<sup>1</sup>

## **G7 ECAs' Policies and Practices**

In an effort to level the playing field among exporters from competing countries, Ex-Im Bank and the US government (USG) negotiated among the Export Credit Group of the OECD, the “Council Recommendation on Common Approaches on the Environment and Officially Supported Export Credits” (the “Common Approaches”). The Common Approaches established a uniform environmental review framework among ECAs. The 2003 Common Approaches was revised and expanded in 2007, and its current version is currently under review. The Common Approaches moved foreign ECAs towards a common environmental review framework, an idea once considered unattainable. The OECD ECAs support the implementation of the Common Approaches through reporting procedures and technical meetings that intend to ensure consideration of the environmental effects of projects on a consistent basis among the OECD ECAs. Thus, OECD ECAs appear to be reviewing, screening, categorizing and evaluating applications for support in a comparable manner, resulting in few – if any – competitive issues.

Although all ECAs have adopted the minimum guideline requirements set forth in the Common Approaches, there remains a significant difference between Ex-Im Bank and most other ECAs with respect to environmental transparency provisions. The Common Approaches does not require OECD ECAs to routinely disclose estimates of greenhouse gas emissions associated with projects, and it does not require disclosure of environmental monitoring or supplemental environmental performance reports beyond the information contained in the environmental impact assessment. To achieve a level playing field for US exporters, Ex-Im Bank will continue to advocate for a requirement in the Common Approaches that provides for disclosure of the level of greenhouse gas emissions for projects and the routine disclosure of environmental monitoring reports and supplemental environmental information of projects following ECA approval of financing. In addition, consistent with its Carbon Policy, Ex-Im Bank will seek to add reporting and review requirements on high carbon intensity projects and provisions that encourage the reduction of greenhouse gas production into the Common Approaches.

## **Exporter and Lender Survey and Focus Group Results**

There is little evidence that the Bank’s Environmental Procedures and Guidelines have affected US exports, although the complexity of potential effects and the lack of information surrounding such reviews can limit an exporter’s ability to obtain a timely indication of Ex-Im Bank’s willingness to support or deny a particular transaction.

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<sup>1</sup> Although the Carbon Policy was approved in 2009, specific implementation revisions to the Ex-Im Bank Environmental Procedures and Guidelines, that set forth incentives for low to zero carbon emitting projects and disincentives for projects that result in high intensity carbon emissions per unit of electricity, were not approved until 2010. Thus, the competitive impact of the Carbon Policy on Ex-Im Bank will be examined in 2010.

Exporters, lenders and non-governmental organizations periodically opine on Ex-Im Bank's environmental policies, outside of the formal Competitiveness Report focus group process. Specifically, exporters and NGOs have case-specific access to environmental assessment information, including carbon accounting information, and are invited to provide comments prior to Ex-Im Bank action on a particular application for support of US exports to a project. The main concern expressed by exporters has been with respect to Ex-Im Bank's disclosure of environmental information, and more specifically, monitoring reports. Exporters note that borrowers are sometimes reluctant to publically post monitoring information that could become the basis for stakeholder questions about or objections to the project. This impacts their competitiveness because Ex-Im Bank is the only ECA that systematically commits to publishing the monitoring reports.

In addition, exporters and lenders were given the opportunity to comment on Ex-Im Bank's EPG during the Focus Group meetings. One exporter noted that non-OECD ECAs, primarily from Asian countries, represent a competitive threat as these ECAs generally do not conduct any environmental due diligence nor do they have environmental evaluation procedures.

## **Conclusion**

The OECD Common Approaches are a multilateral framework intended to synchronize case-specific environmental due diligence and requirements among ECAs and other multilateral and commercial lenders. Thus, there are growing commonalities among OECD ECA environmental review policies which render Ex-Im Bank's environmental review criteria and procedures generally competitive with those of other OECD ECAs. However, non-OECD ECAs are emerging as a competitive factor in terms of their disparate and generally less rigorous approaches towards environmental impacts.

Nevertheless, within the OECD, differences exist regarding ECA transparency policies; particularly those policies related to environmental information disclosure and public reporting of carbon accounting which to date have only been loosely addressed by the OECD Common Approaches. Exporters have noted their greatest competitive concern stems from the disclosure of environmental monitoring reports subsequent to transaction approval. To the extent that Ex-Im Bank is the sole ECA applying and advocating for disclosure of monitoring information and carbon accounting on a case-by-case basis, which it currently is, Ex-Im Bank will continue to be viewed as "barely competitive" as compared to foreign ECA transparency policies.

Thus, Ex-Im Bank Environmental Policies and the application of the Common Approaches standards, Ex-Im could be graded as an "A", or equal to the average ECA. However, with regard to the application of transparency provisions, Ex-Im could be graded as a "B": modestly competitive with other ECAs. On balance, the overall grade would be an "A-/B+."



# Chapter 4: Major Program Structures

## Section E: Foreign Currency Guarantees

### Introduction

A foreign currency guarantee refers to an ECA-covered export credit that is denominated in a currency other than the ECA's domestic currency. Because official support for transactions denominated in a foreign currency is not governed by the OECD Arrangement, each ECA self-determines whether to provide foreign currency cover; on what basis to provide it (i.e., loans, guarantees or insurance); and on what terms to provide it (interest rate to be covered, whether to crystallize<sup>1</sup> the debt in the event of default, etc.).<sup>2</sup> Despite the recent financial crisis, the US dollar continues to be a crucial trade currency, accounting for about two-thirds of the world's reserve assets in 2009. Additionally, as **Figure 11** shows, the US dollar is frequently used as the currency for export invoicing for non-US destined exports, for other G7 and developing nations.<sup>3</sup> For example, over 70% of export invoices in Australia, Korea, Thailand, and Malaysia are US dollar denominated, though less than 20% of each country's exports are sent to the US.

The types of currencies typically eligible for cover by ECAs are generally referred to as either "hard" or readily convertible currencies (such as the US dollar, the euro, or the yen) and "soft" or emerging market currencies (such as the South African rand or Mexican peso). The phenomenal growth in liquidity in emerging markets during the course of this decade resulted in steadily increasing borrower demands for export credit cover in local-currency-denominated debt. However, with the 2009 global liquidity crunch, traditional lenders were less able or willing to provide local currency financing on their own.

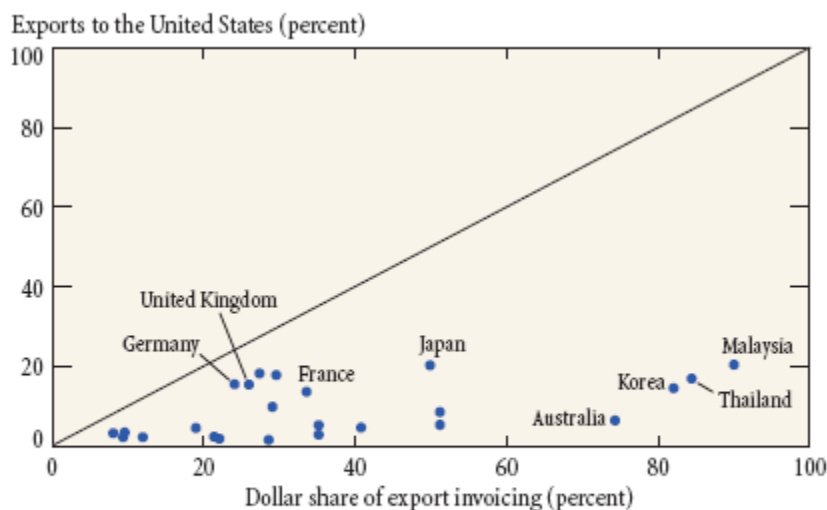
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<sup>1</sup> In the event of a claim payment by the ECA, crystallization requires that the debt (along with any fees incurred) be converted into its hard currency equivalent, and sometimes referred to as conversion. The ECA seeks recovery of the hard currency obligation, and exchange rate risk during the recovery period is borne by the obligor.

<sup>2</sup> However, the use of local currency can be eligible for a premia discount under the OECD Arrangement if certain conditions are met.

<sup>3</sup> The last two sentences are based on information contained in "Is the International Role of the Dollar Changing?" by Linda S. Goldberg, Federal Reserve Bank of New York, January 2010.

**Figure 11: Dollar Use in the Invoicing of Exports**



Source: Goldberg and Tille (2008).

Note: Observations cover various years from 2000 to 2007.

Source: “Is the International Role of the Dollar Changing?” by Linda S. Goldberg, Federal Reserve Bank of New York, January 2010

### **Ex-Im Bank’s Policy and Practice**

Ex-Im Bank offers foreign currency support through its guarantee and insurance programs by working with a commercial bank. The program has been used most widely in aircraft financing because it is an attractive way for an airline borrower to reduce its currency risks by matching the currency of its debt to the currency of its revenues when most of those revenues are not in US dollars.

Ex-Im’s foreign currency claims procedure requires that, in the event of default and irrespective of whether the foreign currency is a hard or soft currency, Ex-Im purchases the foreign currency to pay the claim to the lender and then converts (or “crystallizes”) the debt obligation by the borrower into US dollars equal to the amount that Ex-Im Bank paid to obtain the foreign currency. This policy effectively shifts the post-claim exchange rate risk from Ex-Im Bank to the obligor. In addition, if the note rate is floating, Ex-Im Bank typically accelerates the debt and pays the claim in a single lump-sum payment; however, for fixed rate notes Ex-Im Bank may provide the option for an installment by installment repayment schedule, crystallizing the portion of the obligation due at each payment.<sup>4</sup> While most hard currency cover is readily available with crystallization, Ex-Im only considers soft currency cover on a case-by-case basis (even with the crystallization contingency) after a thorough internal review of the relevant local currency market.

<sup>4</sup> Acceleration of the debt can cause problems for investors if the debt has been securitized (sold by the original lender to various third-party investors, who have needs or obligations requiring cash flows matching the original loan terms).



There are two exceptions to Ex-Im's crystallization/conversion requirement policy. First, for co-financed transactions Ex-Im Bank may offer cover for Euro denominated without the conversion/crystallization requirement. None of the foreign currency guarantees authorized in 2009 involved co-financing. Second, if Ex-Im Bank receives valid evidence that a foreign ECA will provide coverage without conversion for the same transaction, Ex-Im Bank has a matching provision that would allow the Bank to provide foreign currency (including soft currency) coverage without the requirement for conversion. However, these options are rarely, if ever, used.

In 2009, Ex-Im Bank supported 9 foreign currency transactions with a total financed amount of over \$1.6 billion (compared to 8 transactions valued at about \$1.8 billion in 2008). In 2009, all foreign currency cases were denominated in a single hard currency: the Euro. Eight of the 9 transactions were in support of aircraft exports for airlines located in Morocco, the Netherlands, and Ireland (5 of these transactions were in Ireland). One final transaction was for solar photovoltaic equipment to Germany for \$14.5 million.

## **G7 ECAs' Policies and Practices**

The other G7 ECAs distinguish between two types of foreign currency coverage: *hard currency cover* which is readily available without crystallization and usually at no additional cost compared to domestic currency coverage; and *soft currency cover* which is available on a case-by-case and/or currency-by-currency basis and usually results in additional ECA considerations on appropriate risks and mitigants that should be brought to bear on the transaction.

*Hard Currency Cover:* All G7 ECAs provided support for export credits denominated in hard currencies. Unlike Ex-Im Bank, however, the other ECAs were willing to accept recoveries in hard currencies because they either (a) have accounts in the foreign currency; (b) impose a surcharge used to offset possible shortfalls that could arise from currency fluctuations between the domestic and foreign hard currency; or (c) take a portfolio approach to risk management that allows them to cross-subsidize profits and losses that result from the foreign currency fluctuations. EDC (Canada), SACE (Italy), NEXI (Japan), COFACE (France) and ECGD (U.K.) do not require conversion of the obligation post-claim payment because they have the capability to assume and manage the foreign exchange rate risk. Euler Hermes (Germany) will cover the exchange rate risk for a surcharge. As a result, the Ex-Im Bank requirement on defaulted obligations to convert all foreign debt into US dollars is unique, with the two exceptions stated above (e.g., co-financing and competition)

*Soft Currency Cover:* As **Figure 12** shows, no uniform practice exists among G7 ECAs with respect to acceptance of soft currency foreign exchange risk. However, based on recent data, most (if not all) are now willing to consider (and several have offered) non-crystallized soft currency support. Some ECAs have found that local laws prohibit crystallization of the debt or severely restrict an ECA's recovery efforts, thereby rendering conversion of local currency debt cumbersome and, in some instances,

ineffective. Thus, ECAs assess the risk/reward equation in order to find ways to manage their risks in the face of legal and practical constraints on crystallization.

As countries evaluate their approach to local currency cover by looking at the buyer's financial position along with the country's economic and political situation, the issues of how and when to use the OECD discount<sup>5</sup> come into play. Because OECD notifications of using this discount are only required when the discounted premium is below the minimum premium allowed by the OECD Arrangement, it is unknown to what extent the use of local currency cover results in lower premium than what would have been charged had the transaction been done in a non-local currency.

**Figure 12: G7 ECA Foreign Currency Approaches: Willingness to Accept Exchange Rate Risk and Activity, 2009**

	Exchange Risk Accepted?		Currencies <sup>1</sup> of Approved Transactions (2004-2009)	
	Hard Currency	Soft Currency	Hard Currency	Soft Currency
<b>EDC<sup>2</sup></b>	Yes	Case-by-case	USD, EUR, CAD, JPY, GBP, HKD, AUD	MXN, NZD, PLN, SGD, HUF, CZK
<b>Coface<sup>3</sup></b>	Yes	Yes	USD, AUD, JPY	ZAR, XAF, EGP, MXP
<b>Hermes<sup>4</sup></b>	Yes, with 10% surcharge	Case-by-case, always with a minimum 10% surcharge	USD, GBP, CHF, CND, AUD, JPY	MXP, ZAR, INR, RUB, TWD
<b>SACE<sup>5</sup></b>	Yes	Limited experience	USD, CND, GBP, JPY	EGP, BRL
<b>NEXI<sup>6</sup></b>	Yes	No experience	USD, EUR	none
<b>ECGD<sup>7</sup></b>	Yes	No, convert obligation to Sterling at time of payment	GBP, USD, EUR, JPY	AUD, NZD
<b>US Ex-Im Bank<sup>8</sup></b>	No, convert obligation to dollars at time of payment	No, convert obligation to dollars at time of payment	EUR, JPY, AUD, CND, NZD	MXP, COP, ZAR

1 Currency Key: USD – US dollar, EUR – Euro, GBP – British pounds, JPY – Japanese yen, AUD – Australian dollars, CHF – Swiss francs, NZD – New Zealand Dollar, EGP – Egyptian pounds, CND- Canadian dollar, CZK – Czech koruna, MXP – Mexican pesos, DOP – Dominican Republic peso, ZAR – South African rand, AED -- United Arab Emirates dirham, COP – Colombian peso, BRL – Brazilian real, XAF – Central African Franc, INR – Indian rupee, RUB – Russian ruble, TWD – Taiwan dollar, and MAD – Moroccan dirham.

2 EDC will cover Australian dollar, British pounds, Euro, Japanese yen, US dollar, New Zealand dollar, Norwegian kroner, Czech koruna, Hong Kong dollar, Hungarian forint, Mexican peso, Polish zloty, Singapore dollar, South African rand, and Swedish kroner.

3 COFACE will cover Algerian dinar, Brazilian real, Colombian peso, Indian rupee, Malaysian ringgit, Mexican peso, Morocco dirham, Russian ruble, South African rand, Thailand baht, CFA franc, Turkish lira, Chilean peso.

4 Hermes determines on a case-by-case basis.

5 SACE determines on a case-by-case basis.

6 NEXI – US dollars and Euro.

7 ECGD will consider coverage for any currency that is readily convertible, and where the local financial markets have sufficient depth and capacity to fund the transaction.

8 US Ex-Im Bank will cover Euros, Japanese yen, Australian dollars, Canadian dollars, New Zealand dollars, Brazilian real, British pound, Central African franc, Colombian pesos, Egyptian pound, Indian rupee, Indonesian rupiah, Korean won, Malaysian ringgit, Mexican pesos, Moroccan dirham, Norwegian kroner, Pakistani rupee, Philippine peso, Polish zloty, Russian ruble, Swedish kroner, Swiss franc, South African rand, Taiwanese dollar, Thai baht, and West African franc.

<sup>5</sup> Under OECD guidelines, crystallized local currency cover is eligible for a 35% - 50% discount from the OECD minimum premium.

## **Exporter and Lender Survey and Focus Group Results**

Lenders continue to express interest in foreign and local currency guarantees provided by Ex-Im Bank, even as the financial downturn continues to cause lenders to pursue less risky transactions. Some exporters lamented that Ex-Im's foreign currency policy does not accommodate current US trade realities – for example, these exporters believe the option for foreign currency should be automatically available for transactions in Mexico and Brazil because these markets account for a large share of US exports.

Additionally, the exporter and lender survey results were mixed, with lenders generally viewing current Ex-Im foreign currency policies more favorably than exporters. However, at the same time, focus group results from the lending community showed that lenders continued to view Ex-Im Bank's crystallization policy as uncompetitive relative to other ECAs. Regardless, lenders understand Ex-Im's crystallization policy and, while they don't think it is the best policy, accept it as something with which they have to work.

### **Conclusion**

The annual survey of exporters and lenders, and results from focus group discussions, indicate the demand for foreign or local currency financing is likely to continue to grow over the long-term. In this regard, Ex-Im's strict crystallization policy – that is, the requirement to convert the obligation post-claim payment to US dollars on *all* foreign currencies – is viewed as detrimental to its competitiveness given other ECAs' standard acceptance of non-crystallized cover for hard currencies and more flexible willingness to offer non-crystallized cover for soft currencies. In fact, most European ECAs already have solid US dollar reserves and facilities in place for transactions. Ex-Im Bank's guardian authorities however have told Ex-Im that they simply do not want the Bank to offer local currency support without crystallization except in competitive case-by-case situations or co-financed Euro transactions. Accordingly, the grade for Ex-Im Bank's foreign currency guarantee program in 2009 remains a "B."



# Chapter 4: Major Program Structures

## Section F: Services

### Introduction

Services exports continue to be an extremely important component of international trade, especially for the United States. As of 2008, the US was the top country exporting services in the world, making up almost 14 percent of world services exports.<sup>1</sup> Despite the global financial crisis, which decreased world trade in 2009 by 12-14%, exports of US services were quite resilient.<sup>2</sup> Nominal US exports of services went from \$516bn in 2007, to \$564bn in 2008, to \$525bn in 2009.<sup>3</sup> To show the strength of services in real terms, US services exports decreased by 4% in 2009 over 2008, whereas exports of US goods decreased by over 12%, more than three times as much. Further, real services exports have grown by 40% since 2000, compared to 17% for goods exports. Services exports made up about one-third of all US exports in 2009.<sup>4</sup>

Ex-Im's commitment to financing services exports is also mandated in Ex-Im Bank's charter, Section 2(b)(1)(D), which states "the Bank shall give full and equal consideration to making loans and providing guarantees for the export of services (independently, or in conjunction with the export of manufactured goods, equipment, hardware or other capital goods) consistent with the Bank's policy to neutralize foreign subsidized credit competition and to supplement the private capital market."

### Ex-Im Bank's Policy and Practice

Ex-Im Bank supports services exports over a wide range of service providing industries. As seen in **Figure 13**, over the last three years Ex-Im Bank has provided financing for almost \$8 billion of US services exports (which represents about 13% of the total export value supported by Ex-Im over this 3 year period). Ex-Im Bank support for services includes both "stand-alone" services (services that are not part of a capital goods/project-related transaction) and "associated services" (services that are associated with capital goods exports and/or large projects). The 2009 figure of \$3.8 billion is illustrative of the types of services supported by Ex-Im Bank, with several major industry sectors receiving a large amount of financing.

During 2007-2009, Ex-Im Bank support for services increased steadily. Most of this increase is from additional support for engineering and consulting services, and from additional support for information technology and telecommunications services. Most of the stand-alone services were for engineering and consulting services, and computer software systems design (information technology) services, with the others dispersed

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<sup>1</sup> World Trade Organization (WTO), "World Trade 2008, Prospects for 2009" released March 2009

<sup>2</sup> World Bank, "Global Economic Prospects 2010: Crisis, Finance, and Growth" released January 2010

<sup>3</sup> US Commerce Department, Bureau of Economic Analysis, National Income and Product Accounts

<sup>4</sup> US Commerce Department, International Trade Administration, January 2010 US Export Fact Sheet

across the remaining sectors. With regard to associated services, 80% of Ex-Im Bank support was for mining, oil & gas, and engineering & consulting services in 2009.

Generally, Ex-Im Bank provided associated services exports with repayment terms of 5-12 years. These repayment terms reflect the medium- to long-term nature of the financing requirements of large projects with which they were associated. On the other hand, stand-alone services tend to receive short-term (6-18 months) support because they are typically part of short-term operating expenses.

**Figure 13: Services Supported by Ex-Im Bank, 2007-2009 (\$US Million)**

	2007			2008			2009 <sup>1</sup>			Total		
	Stand-Alone	Assoc.	Total	Stand-Alone	Assoc.	Total	Stand-Alone	Assoc.	Total	Stand-Alone	Assoc.	Total
Engineering & Consulting	25.1	1,451.5	1,476.6	24.4	1,490.4	1,514.8	27.0	2,248.6	2,275.6	76.5	5,190.5	5,267.0
Oil & Gas and Mining	1.6	211.0	212.6	2.1	372.7	374.8	--	769.0	769.0	3.7	1,352.7	1,356.4
Information Technology & Telecommunications	0.2	2.6	2.8	3.6	1.5	5.1	10.5	419.1	429.6	14.3	423.2	437.5
Rental & Leasing	--	16.9	16.9	--	22.7	22.7	--	143.7	143.7	--	183.3	183.3
Legal & Banking	14.7	78.1	92.8	17.9	195.5	213.4	9.8	61.7	71.5	42.4	335.3	377.7
Transportation	7.1	0.3	7.4	4.2	1.9	6.1	11.2	46.8	58.0	22.5	49.0	71.5
Construction	5.8	6.3	12.1	7.7	35.9	43.6	0.5	21.5	21.9	14.0	63.7	77.6
Other Services <sup>2</sup>	8.0	38.8	46.8	6.0	5.0	11.0	--	20.0	20.0	14.0	63.8	77.8
Medical	1.7	0.9	2.6	0.7	--	0.7	0.8	1.0	1.8	3.2	1.9	5.1
Agriculture	4.4	--	4.4	20.7	--	20.7	--	--	--	25.1	--	25.1
<b>TOTAL</b>	<b>54.5</b>	<b>1,766.7</b>	<b>1,875.0</b>	<b>59.9</b>	<b>2,120.6</b>	<b>2,212.9</b>	<b>59.8</b>	<b>3,731.3</b>	<b>3,791.1</b>	<b>174.2</b>	<b>7,618.6</b>	<b>7,879.0</b>

Source: Ex-Im Bank

<sup>1</sup>Due to methodology differences, 2009 data is not immediately comparable to 2007 & 2008 data.

<sup>2</sup>Includes repair services and personal care services.

## G7 ECAs' Policies and Practices

All G7 OECD ECAs appear willing to support services as a general category of exports, with most medium- and long-term support provided for services associated with capital goods exports, although there is little official data from other G7 ECAs regarding the amount of services supported annually. Bilateral discussions with a variety of G7/OECD ECAs, along with a 2008 survey suggest that the sectors reported to be receiving the largest amounts of medium- and long-term support include oil and gas development, power plant construction, mining and refining, and telecommunications. Official G7 ECA support for stand-alone services is relatively uncommon<sup>5</sup>; however, in January

<sup>5</sup> Based on a review on the G7 ECAs' websites, none of the other G7 ECAs referenced support for stand-alone services. Additionally, in a recent request made to G7 ECAs inquiring about services support, none reported any change from the 2008 survey.

2010 Euler Hermes launched a new insurance program targeted exclusively for architects, engineers, and other services exporters.

### **Exporter and Lender Survey and Focus Group Results**

Focus groups noted that Ex-Im's basis for support of services is antiquated in that we use “goods” standards particularly with regard to content determination and origin. Further, these standards do not always fit services, given the intangible nature of so many services especially in the IT area – intellectual property rights, software, etc. Exporters and lenders believe other ECAs are much more flexible and willing to support services exports, but none appear to have a well-defined services policy.

According to the annual Competitiveness Report survey completed by lenders and exporters using Ex-Im's medium- and long-term programs during 2009, there was a general consensus similar to the focus groups that improvements could be made in terms of the availability and flexibility of Ex-Im's services cover.

### **Conclusion**

In effect, for services that typically are associated with capital goods exports, the amount of G7 support for services exports appears to be at least as competitive as that provided to the capital goods exports. However, stand-alone services seem to have no specific short-, medium-, or long-term programs designed just for these services and, as noted above, are almost always underwritten on a short-term basis. Based on exporter and partial information on competitor practices related to services, it would appear that Ex-Im Bank's willingness to support services is equal to at least the average willingness of other ECAs. Additionally, even though Ex-Im does not have a formal program designed around stand-alone services support, the option for such support is generally available. However, exporter and lender survey results indicate Ex-Im's services support has room for improvement in terms of availability and flexibility, which slightly mitigates Ex-Im's inferred relative competitiveness. Thus, the grade for Ex-Im Bank services cover is an “A-/B+” for 2009.





## Chapter 4: Major Program Structures

### Section G: Ex-Im Bank's Major Program Competitiveness

Ex-Im Bank's major program structures were considered to be generally competitive with their G7 ECA counterparts during 2009, which translates into a grade of "A-". Ex-Im Bank's co-financing program saw increased activity and provided support across more industry sectors earning the program a grade of "A-/B+" (up from a "B" in 2008). Meanwhile, Ex-Im Bank's aircraft and project finance programs were again rated as generally competitive with its foreign ECA counterparts. Conversely, Ex-Im Bank's foreign currency support for soft cover was viewed as detrimental to competitiveness given that most ECAs (if not all) are now willing to consider (and several have offered) non-crystallized soft currency support. The grade for the foreign currency guarantee program remained at "B", however, the sub-grade for the availability of soft cover fell to a "B-/C+" (from "B" in 2008).

**Figure 14** shows how Ex-Im Bank's major programs were rated on individual aspects as well as overall. The grades are based on the survey and focus group results and Ex-Im Bank's analysis of how it performed in relation to its G7 ECA counterparts.

**Figure 14: Grading of Ex-Im Bank's Major Program Competitiveness, 2009**

Key Elements	Grade
<b>Large Aircraft</b>	<b>A</b>
Interest Rate Level	A
Percentage of Cover	A
Risk Capacity	A
<b>Project Finance</b>	<b>A</b>
Core Program Features	A
Repayment Flexibilities	A
<b>Co-Financing</b>	<b>A-/B+</b>
Bilateral Agreements	A-/B+
Flexibility in one-off deals	A-/B+
<b>Environment</b>	<b>A-/B+</b>
<b>Foreign Currency Guarantee</b>	<b>B</b>
Availability of Hard Cover	A-/B+
Availability of Soft Cover	B-/C+
Accepts Exchange Rate Risk	B-/C+
<b>Services</b>	<b>A-/B+</b>
Availability	A-/B+
Flexibility	A-/B+
<b>Total Average Grade</b>	<b>A</b>



# Chapter 5: Economic Philosophy

## Section A: Trade-Related Tied and Untied Aid

### Introduction

Tied and untied aid has long been a focus of competitive concern among US exporters. Multilateral rules which restrict donor use of tied aid and untied aid for commercial or trade purposes have reduced competitiveness concerns. However, certain donor governments continue to offer tied aid for commercial gain – albeit in small measure. This chapter will describe the limited competitive issues surrounding tied aid use. **Appendix F** provides a more detailed synopsis of the implementation of the OECD rules and definitions, as well as presents tied and untied aid activity that may be useful to understanding the competitive implications of foreign tied and untied aid on US exporters.

### Overview of Tied and Untied Aid

“Tied aid” is a subsidized, conditional, trade-related aid credit, provided by a donor government, to induce the borrower to purchase equipment from suppliers in the donor’s country. Tied aid is typically offered as development assistance that provides critical support for the recipient country. “Untied aid” differs from tied aid in that it is not formally conditioned on the purchase of equipment from suppliers in the donor country. That is, recipients of untied aid can use the funds to purchase goods from suppliers located anywhere in the world, not just in the donor’s country.

US Government efforts to discipline tied aid at the OECD resulted in a 1991 agreement (also known as the Helsinki Disciplines) that has significantly limited the trade-distorting effects of tied aid and redirected tied aid flows towards legitimate development projects. With respect to untied aid, in 2005, the US secured a transparency agreement that requires OECD Members to (a) notify project loan commitments at least 30 days prior to the opening of the bidding period (to allow for international competitive bidding) and (b) report the nationalities of the bid winners on an annual ex-post reporting basis.

**Figure 15** indicates that in 2009, the volume of Helsinki-type tied aid decreased last year to approximately \$4.6 billion (down from \$7.3 billion in 2008). However, there was a 15-20% increase in the number of tied aid notifications to 135, indicating that more transactions were approved, but at a lower monetary value as compared to 2008 (when three very large transportation projects drove an upward spike in the tied aid activity data). The data for 2009 show a continuation of tied and untied aid trends evidenced over the last five years or so. Specifically, with respect to tied aid:

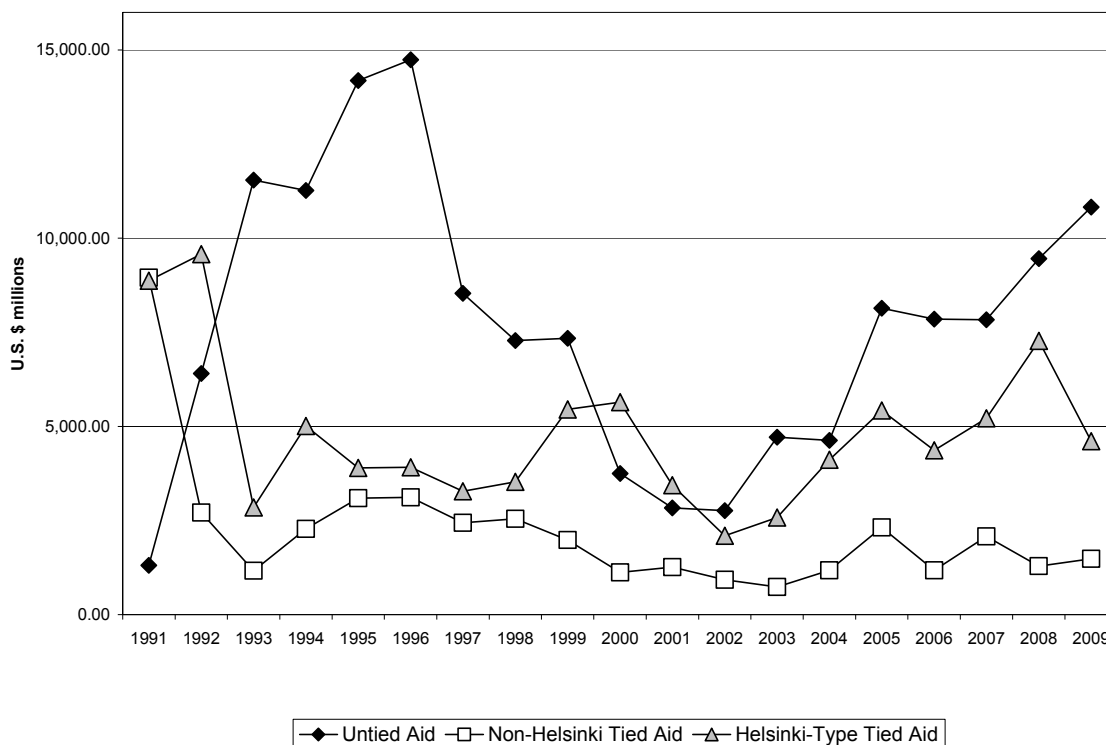
- Spain has consolidated its position as the largest donor of tied aid, accounting for over \$1 billion of tied aid activity and over 25% in terms of percentage share of volume.

- Japan, typically the largest tied aid donor, trailed behind Spain with \$664 million, while Austria ousted France as a major tied aid donor, with offers amounting to over \$530 million in tied aid (compared to France's offers that were below \$300 million). Similarly, Korea provided \$505 million in tied aid. Taken together, Spain, Japan, Austria and Korea accounted for over 60% of all tied aid.
- Although Asia continued to be the primary region receiving tied aid, the main recipient countries shifted. Vietnam received the largest amount of tied aid in terms of volume. China regained its position among the top two recipients of tied aid and is the largest recipient of tied aid in terms of number of tied aid offers.
- With respect to sectors drawing tied aid, resources, transport and storage continued to attract a high volume of tied aid. Water and sanitation in addition to energy generation have also received some tied aid. All told, tied aid was primarily offered for financially non-viable projects.

In 2009, reporting from the untied aid transparency agreement showed that the volume of and number of untied aid notifications increased a modest amount. That is, the volume of untied aid increased from under \$10 billion in 2008 to \$11.3 billion in 2009 (a 13% increase). The number of untied aid offers decreased, from 77 notifications in 2008 to 62 notifications in 2009. Additional noteworthy points include:

- Only four countries (Japan, Germany, France and Korea) reported offers of untied aid under the OECD transparency agreement.
- In 2009, donors appear to be rebounding from the financial crisis and are increasing untied aid resources to levels that are approaching 2007 numbers.
- With respect to main donors, Japan continued to account for the majority of the notifications in terms of volume (over 80%) while Germany reported the highest number of notifications (about 40%).
- The main recipient of untied aid was Thailand, attracting 30% of the total volume of untied aid, followed by China, who received about a quarter of the untied aid spread over 14 transactions.
- In terms of outcomes of the bidding procedures associated with the untied aid offers, more than one-third of the contracts were awarded to top suppliers from China.

**Figure 15: Aid Credit Volume by Type, 1991-2009 (\$US Million)**



Note: Consistent untied aid data reporting began in 1994. Discrepancies between untied aid data reported under the OECD Arrangement and data captured under the 2005 Transparency Agreement on Untied ODA Credits can be attributed to differences in the timing of OECD Notifications -- which are typically made well in advance of (perhaps years before) the contract bid is awarded -- and are, therefore, not comparable on an annual basis with ODA Credit amounts, which reflect actual credit commitments included in bid tenders.

### Competitive Situation

In 2009, Ex-Im Bank continued to hear allegations of targeted tied aid availability by non-G7 ECAs (and some Emerging Market ECAs) which threatened certain US exporter sales prospects. Certain ECAs continue to offer concessional credits for water and renewable energy projects. Exporter complaints regarding the negative competitive landscape have generally not been substantiated by evidence that tied aid offers from G7 countries fail to comply with the OECD disciplines, but rather that tied aid offers supported (in limited and targeted situations) renewable energy or water projects. With respect to tied aid offers directed at projects or sectors considered to be financially and/or commercially viable, Ex-Im Bank was made aware of only one such situation over the past year that was related to a rail project for which Ex-Im Bank had issued and extended a letter of interest a few years ago. The Tied Aid Capital Projects Fund now totals approximately \$171 million.

## **US Government and Ex-Im Bank Policy**

Long-standing US Government policy seeks to encourage all aid flows. As a corollary to that policy, the US has sought to ensure that legitimate development assistance be freely available to bidders from all countries. Absent free availability, trade-distorting or preferential treatment that could be aid, is aid that is offered to benefit suppliers in the donor's country. Historically, trade-distorting tied aid was a competitive issue for US exporters because it was undisciplined and frequently used by foreign ECAs. The US Government has since sought to limit – if not eliminate – trade-distorting tied aid and has subjected untied aid to transparent reporting procedures. Thus, foreign tied aid is now only sporadically cited as a competitive factor impacting US exporter sales abroad.

US Government policy seeks to reduce, and ideally eradicate, trade-distorting tied and untied aid. Consistent with this long-standing philosophy, Ex-Im Bank does not initiate tied aid. Instead, Ex-Im Bank and the US Treasury Department work together to encourage the withdrawal of foreign tied aid offers or ensure that US exporters have an equal opportunity to compete for commercial sales to projects. See **Appendix F** for more details.

## **Exporter and Lender Survey and Focus Group Results**

Exporters were generally not aware of cases involving tied and untied aid. However, certain exporters that had confronted foreign tied aid offers noted that tied aid is an issue in Africa for countries that have received tied aid offers by foreign donors. As borrowers seek to leverage financing available to them, US exporters are pressured to offer concessional terms as well. In addition, exporters noted problems that stem from working with foreign government commercial borrowing limits and the complexities involving multilateral institutions in Ex-Im Bank transactions.

Both lenders and exporters registered their concern that tied aid was offered by both OECD and non-OECD countries and expressed frustration with the burden associated with the Bank's tied aid process.

## **Conclusion**

In 2009, US exporters faced few instances of tied aid when competing for export sales. However, certain exporters report some cases of foreign tied aid that compete with a commercial sale of capital goods to projects that are generally considered to be commercially non-viable (e.g. locomotives and waste water treatment equipment). In those situations, Ex-Im Bank's matching procedures are considered a "hassle" and, as such, a limited competitive response. Therefore, in 2009, tied aid continues to have a modestly negative influence on US exporter competitiveness.

# Chapter 5: Economic Philosophy

## Section B: Market Windows

### Introduction

Market Windows are government-owned institutions that claim to offer export credit on market terms, thereby circumventing the OECD Arrangement rules. Though this implies that they operate as private sector lenders, in reality they receive benefits from their home governments that commercial banks cannot access, such as implicit or explicit government guarantees, tax exemptions and equity capital provided by the government. ECAs which offer Market Windows can simultaneously manage an “Official Window” that offers Arrangement terms for riskier transactions and a Market Window. As domestic export-promoting institutions are neither subject to the constraints placed upon official ECAs via the OECD Arrangement nor to the market limitations of a true commercial bank, Market Windows pose a potential competitive threat in the export finance market.

Market Window institutions consistently avoid discipline in the OECD. Empirical evidence does not exist that proves trade distortion, in part due to the lack of transparency on deal specific terms. Hence, it is difficult to measure and assess the competitive impact of Market Windows. Part of the problem lies in the fact that many US exporters can benefit from Market Window financing if they have facilities in Market Window countries. Therefore, these potential critics have, for the most part, provided no recent evidence of competitive harm.

### Ex-Im Bank’s Policy and Practice

Ex-Im Bank does not operate a Market Window. All of Ex-Im Bank’s medium- and long-term transactions comply with the terms and conditions of the OECD Arrangement. However, in Ex-Im Bank’s re-authorization in 2002, Congress gave the Bank the ability to match the terms and conditions offered by Market Windows. Ex-Im Bank has not yet used this matching authority as there have been no transactions where US exporters have requested matching due to an inability to obtain similar financing terms while facing Market Window competition.

### G7 ECAs’ Policies and Practices

Only two G7 countries provide explicit Market Window support: Canada through EDC and Germany through IPEX-Bank, a KfW subsidiary. The Italian ECA, Sace, recently started a Market Window program which supports untied loans through insurance or guarantees as long as the transaction plays a strategic role for the Italian economy. As of today, only these three G7 countries have Market Window programs.<sup>1</sup> Moreover, a

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<sup>1</sup> Several non-G7 EU ECAs have started market window programs such as ONDD of Belgium and OeKB of Austria.

variety of forces (such as WTO panel decisions and domestic imperatives to make a profit) create incentives for ECAs to increasingly utilize commercial-like procedures and standards. Hence, the distinction between “Market Window” and “official” ECA activity is leaning toward a distinction without a difference for many ECAs.

The following discusses the recent activities and changes in the two G7 Market Window institutions.

- **EDC**

Export Development Canada (EDC) is a Canadian Crown Corporation that operates on private commercial bank principles (i.e., seeks to maximize profits) while providing export credits for Canadian exporters. EDC also operates Canada’s official ECA and allocates business between its official window and Market Window with little transparency.

Data for EDC’s medium- and long-term export credit activity in 2005-2009 reveal significant year-to-year variability. Market Window activity witnessed similar fluctuations, accounting for between 41% and 96% of EDC’s total medium- and long-term export credit business in the years 2005 through 2009, with 2009 seeing the closest balance between Market Window and official window activity (**see Figure 16**). With the agreement of the new Aircraft Sector Understanding in 2007, Canada agreed to bring its aircraft business under its official window. Previously, most of the aircraft business was done through EDC’s market window.

**Figure 16: EDC Medium- and Long-Term Activity, 2005-2009 (\$US Billion)**

	2005	2006	2007	2008	2009
<b>Total MLT export credits</b>	\$3.3	\$5.3	\$2.8	\$4.6	\$4.6
<b>Market Window</b>	2.8	5.1	2.3	3.3	2.7
<b>Official Window</b>	.5	.2	.5	1.3	1.9

Source: EDC

- **KfW IPEX-Bank**

In 2004, KfW Bankengruppe began conducting much of its export credit and project finance activity through IPEX-Bank, a newly-created, 100% KfW-owned, arms-length subsidiary (i.e., a “bank-in-a-bank”). The decision to separate Market Window activity from KfW’s state-sponsored economic support activities was motivated by the European Commission’s concern that KfW’s export financing was unfairly competing with European commercial banks due to KfW’s state support. To fully address the European Commission’s concern, on January 1, 2008, KfW IPEX-Bank began operating as a legally independent entity but still remains a subsidiary of KfW and continues to be closely integrated into KfW’s overall strategy. Although KfW IPEX-Bank has been provided with initial equity upon spin-off by KfW, it has a stand-alone credit rating, which is the basis of its funding costs. KfW



IPEX-Bank is also subject to taxation and German banking regulations, and must earn a risk-adjusted return on capital of 13%, a level determined by IPEX-Bank management and endorsed by KfW's Board.

Due to the financial crisis, KfW IPEX-Bank saw their 2009 total commitments drop by 42% from 2008. Of KfW IPEX-Bank's \$12.4 billion business volume in 2009, 67% consisted of commitments outside Germany of which 41% was export credit business. As in 2008, over 54% of its 2009 export credit business was in support of entities in Europe or North America. In 2009, the three largest industry sectors receiving KfW IPEX-Bank export credit support were the power, renewable and water sector (25%), ships (23%), and basic industries (23%).

KfW IPEX-Bank's export credit business is provided both on Arrangement terms, with official export credit insurance coverage by Hermes, and on Market Window terms. The Market Window support is considered exempt from OECD rules. **Figure 17** below provides a breakdown between the Market Window and official window support provided by KfW IPEX-Bank since 2005. In 2009, approximately 32% of KfW IPEX-Bank's total export credit support was provided without official ECA cover, although some of these transactions may also comply with the OECD Arrangement. KfW IPEX-Bank's market window activity declined significantly in 2009.

**Figure 17: KfW IPEX-Bank Medium- and Long-Term Activity, 2005-2009 (\$US Billion)**

	2005	2006	2007	2008	2009
<b>Total MLT export credits</b>	\$3.2	\$4.0	\$5.4	\$5.9	\$3.4
<b>Market window</b>	1.9	2.2	2.7	2.7	1.1
<b>Official window</b>	1.3	1.8	2.7	3.2	2.3

Source: KfW IPEX Bank

### Summary Data

Combining the two estimates for EDC and KfW IPEX-Bank yields a total of \$3.8 billion in Market Window volume for 2009 (see **Figure 18**).

**Figure 18: Market Window Activity, 2005-2009 (\$US Billion)**

	2005	2006	2007	2008	2009
<b>EDC</b>	2.8	5.1	2.3	3.3	2.7
<b>KfW/IPEX-Bank</b>	1.9	2.2	2.7	2.7	1.1
<b>Total</b>	\$4.7	\$7.3	\$5.0	\$6.0	\$3.8

### Exporter and Lender Survey and Focus Group Results

In general the exporters and lenders remained silent on the market window issue only to note in the survey that such programs have a negative impact on Ex-Im's

competitiveness. Exporters at the focus group meeting noted that EDC's market window poses a competitive issue, but did not know what Ex-Im was doing to address it.

## **Conclusion**

While exporters and lenders are aware of market window institutions and recognize the competitive implications of such programs, no specific cases were highlighted in 2009. However, the threat of Market Windows and their ability to offer more attractive and flexible terms than Ex-Im Bank in competitive situations lingers. The fact that market window activity declined for both EDC and KfW-IPEX Bank is representative of the fact that market activity declined during the financial crisis. Therefore, the ominous threat of Market Windows was not as apparent in 2009. Given this fact and the lack of direct competition, Market Windows in general have a neutral impact on Ex-Im's competitiveness.

## Chapter 5: Economic Philosophy

### Section C: Ex-Im Bank’s Economic Philosophy

#### Competitiveness

The US government philosophy regarding official export credit activity is that ECAs should be able to compete on a level playing field, should supplement, not compete with the private sector, and should operate on a long-term breakeven. This outlook guides Ex-Im Bank offers of export credit support to US exporters. The US has consistently promoted this philosophy amongst its ECA counterparts within the OECD and has sought to ensure that this philosophy is depicted in the OECD Arrangement.

In 2009, Ex-Im Bank did not provide any tied aid activity. US exporters faced few instances of tied aid when competing for export sales. However, the conditions where US exporters saw tied aid competition tended to be for commercially non-viable transactions through which Ex-Im Bank’s matching procedures are considered a “hassle” and, as such, a limited competitive response. Therefore, while Ex-Im tied aid activity was inactive in 2009, tied aid continues to have a modestly negative influence on US exporter competitiveness.

Additionally, there were no specific cases of market windows highlighted in 2009. The fact that market window activity declined for both two prominent ECAs is representative of the fact that market activity declined during the financial crisis. Given this fact and the lack of direct competition, market windows continue to have a neutral impact on Ex-Im’s competitiveness.

**Figure 19** shows the range of impact that these financing features (e.g., *de facto* “tied” untied aid, Market Windows) could have on Ex-Im Bank’s competitiveness in individual cases when similar terms and conditions are not made available by Ex-Im Bank to US exporters.

**Figure 19: Grading of Ex-Im Bank’s Competitiveness When Confronted with Differing Government Financing Philosophies and Programs, 2009**

Program	Ex-Im Bank has program (Yes/No)	Impact on Competitiveness
Tied Aid ( <i>de jure</i> or <i>de facto</i> )	Yes <sup>1</sup>	Negative (for few instances)
Market Windows	No <sup>2</sup>	Neutral
Overall Assessment		<b>Negative (on a limited number of transactions)</b>

<sup>1</sup> Ex-Im Bank could use the Tied Aid Capital Projects Fund (TACPF) to match “*de facto* tied” untied aid.

<sup>2</sup> In Ex-Im Bank’s 2002 Charter Reauthorization, the Bank was granted the authority to provide financing terms that are inconsistent with the Arrangement when a Market Window is providing such terms that are better than those available from private financial markets.



# Chapter 6: Public Policies – Stakeholder Considerations

## Section A: Introduction

This chapter identifies relevant public policy considerations that have the potential to impact Ex-Im Bank's competitiveness. The three topics discussed in this chapter – economic impact, content (i.e., foreign content and local costs) and US shipping requirements -- are rooted in legislative processes (such as Ex-Im Bank's charter) that tie Ex-Im Bank activity to broader public goals and values.

For each topic, Ex-Im Bank has developed policy parameters that respond to specific Congressional mandates. These parameters determine the availability and level of Ex-Im Bank financing for specific transactions. If a transaction falls short of these requirements, Ex-Im Bank financing may be reduced or withheld altogether.

A summary of each topic follows:

- The economic impact mandate requires Ex-Im Bank to evaluate the potential negative effects of a Bank supported transaction on the US economy (e.g., displaced US production). Applicable transactions are those that result in foreign production of an exportable good (e.g., increase in foreign fertilizer production capacity). If the economic impact evaluation yields a net negative finding, it can be a basis for withholding Ex-Im Bank support.
- Content refers to components, goods and services in a US export contract that originate in countries other than the US. These products and services may be foreign (that is, goods and services that originate in a third country) or local (that is, goods and services that originate in the foreign buyer's country). Ex-Im Bank generally limits its cover to US content in an export contract. Thus, if a transaction contains 70% US content and 30% eligible foreign content, Ex-Im Bank limits its financing support to 70% of the US export contract, thereby requiring the buyer to identify alternative ways to cover the foreign content. In addition, Ex-Im Bank can cover up to 30% of the US export contract value in local costs. While local costs in long-term transactions are automatically eligible for support, medium-term transactions can only obtain local cost support if the exporter demonstrates need. Exporters can satisfy this requirement by showing either: (1) confirmed ECA-backed local cost financing on behalf a foreign competitor; or (2) lack of private market local cost financing for the transaction.
- The US shipping requirements that pertain to Ex-Im Bank transactions are found in Public Resolution 17 (PR-17). PR-17, administered by the US Maritime Administration (MARAD), requires certain cargo that benefits from US government support to be shipped on US-flagged vessels. For Ex-Im Bank purposes, all direct loans extended by Ex-Im Bank, guarantees for transactions valued at more than \$20 million, and guarantees where the repayment term exceeds 7 years are subject to PR-17 requirements. If a transaction subject to PR-

17 ships its cargo on a non-US-flagged vessel, the transaction is ineligible for Ex-Im Bank support unless the exporter obtains a waiver from MARAD.

While every ECA has its own public policy goals, the limits on Ex-Im Bank financing that result from these specific public policy considerations are generally unique to the United States. These unilateral requirements have the potential to create tensions between the goals of maximizing US exporter competitiveness vis-à-vis foreign ECAs (which tends to maximize Ex-Im Bank financing) and satisfying public policy mandates (which may limit Ex-Im Bank financing).

Ex-Im Bank stakeholders are split in their views on how the Bank should balance competing mandates. On one hand, exporters contend that they are disadvantaged by requirements that curb Ex-Im Bank financing; they believe that Ex-Im Bank's US jobs mission is best served by maximizing US exporter competitiveness. On the other hand, Organized Labor maintains that, as a public institution, Ex-Im Bank should broadly evaluate the overall effects of its financing on US jobs (including any negative effects); they believe the Bank's US jobs mission is best served by considering the net impact of Ex-Im Bank financing on US jobs, including US jobs outside of specific export transactions.

The following sections of this chapter provide: (1) insights into the trade-offs that arise as Ex-Im Bank pursues its competitiveness goal while at the same time fulfilling the letter and spirit of public policy mandates; and (2) analyses of the implications of these trade-offs on US exporter competitiveness.

# Chapter 6: Public Policies – Stakeholder Considerations

## Section B: Economic Impact

### Introduction

All applications brought to Ex-Im Bank are subject to economic impact review, according to Ex-Im’s Charter. The Bank must determine, on a case by case basis, if its support of a transaction would likely cause substantial injury to US industry or enable the production of a good that is subject to a trade measure. If either of these conditions is met, then the Bank may deny the transaction. Applications that involve the export of capital goods and services will, in some cases, require a detailed economic impact analysis. The conditions that prompt a detailed analysis are discussed below.

### Ex-Im Bank’s Policy and Practice

The economic impact review requirement was first incorporated into Ex-Im Bank’s Charter in 1968 and has been subsequently modified eight times (most recently in December 2006). The Charter requires the Bank to assess whether its extension of financial support would result in either of the following:

- Production of substantially the same product that is the subject of specified trade measures;<sup>1</sup> or
- Poses the risk of substantial injury to the US economy.<sup>2</sup> Transactions over \$10 million in Ex-Im financing in which the new foreign production is 1% or more of US production of the same product are subject to a detailed economic impact analysis prior to authorization.<sup>3</sup> In a detailed economic impact analysis, staff examines global supply and demand for the good and assesses the broad competitive impacts on US industry arising from the new foreign production (e.g., whether US production is likely to be displaced as a result of new production).

If a transaction meets these legislatively specified standards, then economic impact can be the basis for denial of Ex-Im Bank support. However, in cases where Ex-Im Bank’s Board of Directors concludes that the benefits of financing a given transaction exceeds

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<sup>1</sup> The relevant trade measures are: anti-dumping (AD) or countervailing duty (CVD) orders; Section 201 injury determinations under the Trade Act of 1974; and suspension agreements from AD/CVD investigations.

<sup>2</sup> Congress defined the threshold for substantial injury in Ex-Im Bank’s Charter. The threshold is met if the foreign buyer’s new production is equal to or greater than one percent of US production of the same, similar, or competing good.

<sup>3</sup> Legislation enacted in December 2006 requires that, for the purposes of determining whether a proposed transaction exceeds the \$10 million threshold, the Bank aggregate the dollar amount of the proposed transaction and the dollar amounts of all transactions approved by the Bank in the preceding 24-month period that involved the same foreign entity and substantially the same product to be produced.

its potential injury to the US economy, Ex-Im’s Charter allows the Board’s decision to override the economic impact prohibition.

The Bank’s Charter also requires that Ex-Im Bank’s Chairman submit a Sensitive Commercial Sectors and Products list (“Sensitive Sector List”) to Congress on a yearly basis. This list is designed to inform potential applicants of industries that have historically faced significant difficulty yielding a positive outcome in the economic impact process, and are likely to be declined. However, it is important to note that the inclusion on the Sensitive Sector List does not indicate an automatic denial of Ex-Im support. The Sensitive Sector List submitted to Congress in April 2009 was comprised of “raw steel-making capacity,” “DRAM semiconductors” and “US market oriented” production.<sup>4</sup>

## G7 ECAs’ Policies and Practices

G7 ECAs have a broad mandate to support transactions that benefit their domestic economies. Only Ex-Im Bank is required on a case-by-case basis to weigh the potential economic costs against the benefits of Bank-supported exports. Ex-Im Bank is also the only ECA required to consider outstanding trade measures when evaluating a transaction.

### Ex-Im Bank Summary Data

Throughout 2009, Ex-Im Bank “acted on”<sup>5</sup> 324 medium-term insurance and medium- and long-term loan and guarantee transactions; this was a decrease from 510 transactions in 2008 (**Figure 20**). Of the 324 transactions acted on in 2009, 218 were applications for medium- and long-term loans and guarantees at the Preliminary Commitment (PC) and Final Commitment (AP) stages, and 106 were applications for medium-term insurance.

**Figure 20: Transactions “Acted On” by Ex-Im Bank, 2008 & 2009**

	2008	2009
Long- and Medium-Term Loans and Guarantees (PC or AP)	287	218
Medium-Term Insurance	223	106
<b>Total Long- and Medium-Term Transactions</b>	<b>510</b>	<b>324</b>

Source: Ex-Im Bank

A total of 88 transactions, or about 27%, were scrutinized for economic impact in 2009 because they supported a foreign buyer’s production of an exportable good. This is a

<sup>4</sup> “US market oriented” production is defined as products associated with projects where a significant portion of the output directly produced by the project is destined for the US market and will compete directly with US production.

<sup>5</sup> “Acted on” refers to transactions the Bank authorized, denied, or disbursed upon (as is the case for Credit Guarantee Facilities and Medium-Term Repetitive Insurance Policies) or applications that were withdrawn by the applicant prior to Bank action.



decrease from 2008, when the Bank reviewed 190 transactions, or 37% of long- and medium-term applications.

As shown in **Figure 21**, of the transactions subject to economic impact scrutiny, 7, or 2.2% of all transactions acted on by Ex-Im in 2009, required a detailed economic impact analysis. (This is a modest change from 2008 when 10 cases, or 1.8% of all cases, required a detailed analysis). Five of the cases that required a substantial injury determination revealed that new foreign production capacity would be less than 1% of current US production. Of the remaining cases, 60 were under the \$10 million threshold, and 16 involved new production of a product considered to be in undersupply<sup>6</sup> on global markets. In 2009, there were no applications that would have enabled the production of a trade sanctioned product.

Of the 7 cases requiring a detailed economic impact analysis, 5 were withdrawn for non-economic impact reasons (e.g. credit) prior to the Bank making an economic impact determination. The remaining 2 transactions underwent detailed economic impact analyses and yielded net positive findings. Both applications were approved by Ex-Im’s Board of Directors.

**Figure 21: Transactions Scrutinized for Economic Impact Implications, 2008 & 2009**

	Number of Long- and Medium-Term Transactions		Percentage of "Acted On" Long- and Medium-Term Transactions <sup>7</sup>	
	2008	2009	2008	2009
<b>Subject to Detailed Economic Impact Analysis</b>	<b>10</b>	<b>7</b>	<b>1.8%</b>	<b>2.2%</b>
<b>Substantial Injury Determination of &lt;1% of US Production</b>	<b>4</b>	<b>5</b>	<b>0.8%</b>	<b>1.5%</b>
<b>Under \$10 Million</b>	<b>162</b>	<b>60</b>	<b>32%</b>	<b>19%</b>
<b>Undersupply</b>	<b>14</b>	<b>16</b>	<b>2.8%</b>	<b>4.9%</b>
<b>Total Cases Reviewed for Economic Impact</b>	<b>190</b>	<b>88</b>	<b>37%</b>	<b>27%</b>

Source: Ex-Im Bank

Although a negative economic impact can be the basis for the denial of support, the Board of Directors may make an exception and override the finding. This did not occur in 2009. Staff estimates that applicants did not pursue Ex-Im Bank financing for 8

<sup>6</sup> The economic impact procedures allow Ex-Im’s Board of Directors to exempt some types of capital equipment transactions from a case-specific economic impact analysis by placing them on the “undersupply” list, if they meet the following conditions: (1) the Board determines that long-term domestic demand for a commodity exceeds its foreseeable available domestic supply of this commodity; (2) additional foreign production capacity of the commodity would benefit the overall US economy; and (3) there are no applicable trade measures.

<sup>7</sup> Percentage “Acted On” may not sum to Percentage of Total Cases Reviewed for Economic Impact due to rounding.

potential transactions in 2009 after learning about the existence of an applicable trade measure or that the export would enable the foreign buyer to produce a good that appears on Ex-Im's Sensitive Sector list. Of these 8 potential transactions, 5 involved the export of equipment to steel producers. These figures are consistent with the fact that exportable steel products reflect approximately 45% of all AD/CVD orders.

### **Exporter and Lender Survey and Focus Group Results**

Exporters expressed their frustration that other G7 ECAs are not required to perform economic impact analyses. The Sensitive Sector List, particularly as it applies to raw steel, has prevented lenders from bringing transactions to Ex-Im. Lenders characterized economic impact as “an extremely complex issue” and “difficult for buyers and exporters to understand.” Lenders also expressed concern that economic impact analyses are triggered too easily. There are some industries that, for a variety of reasons, exist only on a small scale in the US. When the foreign buyer's potential production capacity is compared to current US production, it may easily meet the criteria for substantial injury, and require a detailed economic impact analysis. Lenders recommended that if US production is minimal, then economic impact should have a less prominent role in the evaluation of an application. Exporters and Lenders concurred that the economic impact mandate acts as a disincentive to working with Ex-Im Bank.

### **Conclusion**

Ex-Im Bank's economic impact policy can decrease the Bank's competitiveness when compared to other ECAs. Among G7 ECAs, Ex-Im is the only ECA that is required to use an economic impact analysis process to weigh the benefits against the costs of an export. The Bank's economic impact policy not only adds an additional level of review to an application, but according to the Bank's Charter, it can also be the basis for the denial of support. In both 2008 and 2009, approximately one-third of medium- and long-term applications that were acted on were scrutinized for economic impact implications, and about 2% of applications were subject to detailed analyses. Exporters and lenders describe the economic impact process as extremely cumbersome. According to the export community, economic impact considerations have the potential to discourage applicants from ever approaching the Bank for support. As such, economic impact was once again given a negative rating for its effect on Ex-Im Bank competitiveness.

# Chapter 6: Public Policies – Stakeholder Considerations

## Section C: Foreign Content and Local Costs

### Introduction

Ex-Im Bank's content policies can generally be grouped into three categories: US content, foreign content and local costs. US content is the portion of an export that originated in the United States. Foreign content is the portion of an export that originates outside the seller's and the buyer's countries, whereas local costs are goods and services manufactured or originated in the buyer's country.

Eligibility and cover criteria for foreign content are not governed by international agreement, as each ECA establishes its own guidelines. Thus, foreign content is an area where ECA policies and practices have the potential to diverge substantially and meaningfully. In contrast, the OECD Arrangement sets the basic parameters on official local cost support.

### Ex-Im Bank's Foreign Content Policy and Practice in 2009

In keeping with its mandate to maintain or increase US employment through the financing of US exports, Ex-Im Bank's foreign content policy ensures that its export financing targets the US content directly associated with goods and services exported from the US. Ex-Im Bank relies on US content as a proxy to evidence support for US jobs. Thus, the content policies aim to provide incentives to US companies to maximize its sourcing of US content. Nevertheless, there are situations in which US export contracts contain essential goods and services that are foreign-originated. To accommodate these goods and services, Ex-Im Bank's policy allows the inclusion of some foreign content in the US export contract with certain restrictions and limitations. Ex-Im Bank's foreign content policy is consistent with the objectives mandated in its Charter; however, there are no specific statutory requirements *per se* relating to foreign content. Rather, the policy reflects a concerted attempt to balance the interests of labor and industry.

For all medium- and long-term transactions, Ex-Im Bank's foreign content policy *restricts* the scope of its financial support to cover only those products that are shipped from the United States to a foreign buyer, and then it *limits* the level of its support to the **lesser of**: (1) 85% of the value of all eligible goods and services contained within a US supply contract; or (2) 100% of the US content of that export contract.

### G7 ECAs' Policies and Practices: Foreign Content

As a general rule, ECAs seek to maximize the national benefit resulting from their respective activities. However, the context for that evaluation varies widely and has led to very different ECA content policies.

OECD participants recognize that each country develops its content policy to further individual domestic policy goals. Hence, no OECD Arrangement guidelines govern the scope or design of foreign content in an officially supported export credit. Given the vastly different sizes and compositions of the G7 economies and their respective views on national interest, it is not surprising that foreign content policies vary widely and substantively.

Anecdotally, Ex-Im Bank has learned that the liberalization of foreign content policies among Ex-Im Bank’s competitors has receded slightly due to the global financial crisis. Nevertheless, Ex-Im Bank is the only G7 ECA that does not provide any direct support for non domestic content. That is, though the Bank does not require a minimum amount of domestic content for medium- and long-term transactions, the Bank has the lowest “foreign content allowance” (15%). In addition, Ex-Im Bank is the only ECA requiring that goods be shipped from domestic shores in order to be eligible for support.

**Figure 22** compares the main aspects of the content policies of the G7 ECAs in 2009. The data illustrate that Ex-Im Bank’s content requirements and implementation of those requirements are significantly more restrictive than those of its G7 counterparts.

**Figure 22: Comparison of Content Policies of the G7 ECAs, 2009**

	Ex-Im Bank	EDC (Canada)	European ECAs	JBIC & NEXI (Japan)
Is there a requirement to ship foreign content from ECA’s country?	Yes	No	No	No
Will the cover automatically be reduced if foreign content exceeds 15%?	Yes	No	No	No
Is there a minimum amount of domestic content required to qualify for cover?	No	No	Yes	Yes
Does domestic assembly of foreign inputs transform the foreign-originated input to domestic content?	No	Yes	Yes	Yes

## Ex-Im Bank Summary Foreign Content Data

Over the past five years, aggregate data on the incidence of foreign content in Ex-Im Bank transactions (as shown in **Figure 23**) indicate a slow and steady climb. Specifically, the dollar volume of transactions which include foreign content as a share of total export is slightly over 90%, while the number of transactions falls between 40-45% of all medium- and long-term activity. Moreover, the average foreign content ratio is at 13%, slightly above the 10-12% it has been over the past five years. However, medium-term transactions are lower dollar value, but the average foreign content is slightly higher (16%) than the average foreign content in long-term transactions (13%). (see **Appendix E**<sup>1</sup> for foreign content transaction detail).

**Figure 23: Recent Trends in Ex-Im Bank Foreign Content Support, 2005-2009 (US\$ Million)**

	<b>Authorizations</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>
<b>Total activity</b>	Export value (\$MM)	\$7,791	\$8,718	\$7,833	\$12,082	\$17,449
	Number of transactions	587	485	412	333	275
<b>Transactions containing foreign content</b>	Export value (\$MM)	\$6,722	\$7,235	\$7,457	\$10,750	\$15,946
	Percentage of total value	86%	83%	95%	89%	91%
	Number of transactions	156	149	143	141	115
	Percentage of total number	27%	31%	35%	42%	42%
<b>Foreign content</b>	Volume (\$MM)	\$691	\$855	\$919	\$1,164	\$2,106
	Average per transaction	10%	12%	12%	11%	13%

## Ex-Im Bank's Local Cost Policy and Practice in 2009

When Ex-Im Bank provided medium- or long-term guarantee, loan or insurance support for US exports in 2009, it could also provide support up to 30% of the value of the US exports (including eligible foreign content) for locally originated or manufactured goods and services connected to the US export contract. Ex-Im Bank's local cost policy reflects the premise that some amount of local labor and raw materials are necessary to efficiently build or assemble the end product of the US export. The absence of Ex-Im Bank support for local costs that are integral to the US exporter's contract could undermine the US exporter's chances of winning the sale.

For medium-term transactions, Ex-Im Bank could provide local cost support so long as the local costs were related to the US exporter's scope of work and the US exporter demonstrated either: (1) the availability of local cost support from a competitor ECA; or (2) that private market financing of local costs was difficult to obtain for the transaction.

For long-term transactions, automatic local cost support was generally available provided the local costs were related to the US exporter's scope of work. Automatic local cost support was also available for all environmentally beneficial exports, the

<sup>1</sup> Appendix E provides a more detailed listing of foreign content contained in Ex-Im Bank's medium- and long-term transactions (including medium-term insurance) at the time of authorization in 2007.

engineering multiplier program, medical equipment exports, and exports of products related to transportation security projects (also known as the Transportation Security Export Program), regardless of term. For project finance transactions only, though the local costs did not need to be directly related to the US exporter's scope of work, they must be beneficial to the project as a whole.

### Ex-Im Bank Summary Local Cost Data

**Figure 24** illustrates recent trends in Ex-Im Bank's support of local costs. In 2009, the dollar volume of transactions that received local cost support represented 7% of total medium- and long-term transactions requesting local cost support, up significantly from 2% in 2008. In 2009, 61% of all transactions that received local cost support were for medium-term transactions valued at less than \$10 million. In 2009, almost 65% of local cost financing supported installation costs, on-site construction and labor costs, 25% was generally comprised of import duties and value added taxes and the remaining 10% was to support capital equipment. It is important to note, however, that aircraft (large and small) transactions do not typically receive local cost support and have been excluded from the chart below.

**Figure 24: Recent Trends in Ex-Im Bank Local Cost Support, 2004-2009 (US\$ Million)**

	Authorizations	2004	2005	2006	2007	2008	2009
Total medium-and long-term activity	Export value (\$MM)	\$10,949	\$7,791	\$8,718	\$7,833	\$12,082	\$17,449
	Number of transactions	757	587	485	412	333	275
Medium- and long-term activity containing local costs	Number of transactions	79	88	47	36	37	46
	Percentage of total number of transactions	10%	15%	10%	9%	11%	17%
Local costs	Volume (\$MM)	\$312	\$669	\$54	\$119	\$211	\$1,299
	Percentage of total medium- and long-term activity	3%	9%	1%	2%	2%	7%

### G7 ECAs' Policies and Practices: Local Cost

All G7 ECAs adhere to the basic local cost parameters set forth in the OECD Arrangement. From January 1, 2009 through December 31, 2009, there were 184 transactions notified by 19 OECD Participants in which local cost support exceeded 15%. There were no notifications from Japan (NEXI/JBIC). Euler Hermes notified the most transactions (34) followed by the US (32) and Coface (13). About 70% of local cost financing supported installation costs, on-site construction and labor costs, almost 15% of local cost financing supported capital equipment, and the remaining 15% supported a combination of local costs delivered from local subsidiaries and VAT/import duties. Over 75% of the local costs were explicitly included in the exporter's contract. In

particular, in every notified transaction from Euler Hermes (Germany), Coface (France), and ECGD (U.K.) the local costs were explicitly included in the exporter's contract. Ex-Im Bank accounted for 55% of the cases that supported any local costs outside the contract.

### **Exporter and Lender Survey and Focus Group Results**

The vast majority of survey respondents indicated that Ex-Im Bank's foreign content policy had a negative impact on Ex-Im Bank's competitiveness. Exporters and lenders expressed the view that Ex-Im Bank's "foreign content policy is Ex-Im Bank's number one weakness." Chief among the criticisms from exporter and lender groups was that while "other major ECAs improve and adapt their policies and programs to an ever-changing economic environment, Ex-Im has stayed stagnant" and went on to state that "if Ex-Im Bank does not make substantive competitive changes in the near future its relevance will be undermined."

In contrast, the vast majority of survey respondents indicated that Ex-Im Bank's local cost policy had a positive impact on Ex-Im Bank's competitiveness. Specifically, the focus groups commented that the "30% local cost has been a positive change."

### **Conclusion**

As Ex-Im Bank is the only G7 ECA that does not allow for any direct support of foreign content, Ex-Im Bank's foreign content policy is increasingly less competitive. Given the incidence of foreign content in Ex-Im Bank supported transactions (by volume, 90% of all Ex-Im activity), when transactions include more than 15% foreign content, Ex-Im Bank's policy and practice can have a negative impact on US competitiveness.

Based on both comparative information regarding our G7 ECA counterparts and on the exporting community's actual experience with Ex-Im Bank's local cost policy, Ex-Im Bank's local cost policy is considered to have a positive impact on the Bank's competitiveness.





# Chapter 6: Public Policies – Stakeholder Considerations

## Section D: US Shipping Requirements

### Introduction

Public Resolution No. 17 (PR-17) of the 73<sup>rd</sup> Congress states that certain ocean-borne cargo supported by US government credit entities must be transported on US flag vessels unless this requirement is waived on a case-by-case basis by the US Maritime Administration (MARAD). Ex-Im Bank interprets this legislation as requiring that exports financed through Ex-Im Bank’s direct loan and long-term guarantee programs are subject to the US flag vessel requirement.

PR-17 and other cargo preference legislation aim to support the US-flagged commercial fleet which serves as an important national security asset during times of war or national emergency.

### Ex-Im Bank’s Policy and Practice

Ex-Im Bank requires that, in order to be eligible for Bank support, certain transactions must be shipped exclusively on US-flagged vessels if the cargo is ocean-borne. These transactions include:

- direct loans, regardless of amount; and
- guarantee transactions with either: (a) a financed amount greater than \$20 million (excluding Ex-Im Bank’s exposure fee) or (b) a repayment period greater than 7 years.

If a waiver from MARAD is obtained, Ex-Im Bank may provide financing for goods shipped on vessels of non-US registry. There are four different types of waivers that may be obtained: General, Statutory, Compensatory and Conditional. General waivers may be granted in situations where a US-flagged vessel may be available, but recipient-nation vessels may be authorized to share in the ocean carriage (the recipient nation must give similar treatment to US vessels in its foreign trade). Statutory waivers may be granted when it appears that US vessels will not be available within a reasonable time or at reasonable rates relative to other US carriers. Compensatory waivers may be granted when foreign borrowers or US shippers ship goods on non-US-flagged vessels and subsequently enter into a US Government-supported financing agreement for those goods. In such cases, a Compensatory waiver may be granted instructing an equivalent amount of non-US Government-supported goods to be shipped on US-flagged bottoms within a specified time period. Conditional waivers may be granted for cases where no US-flagged vessel is available to accommodate multiple shipments of “critical item” cargoes during a proposed project time period.

Currently, the US is a party to four bilateral Maritime Agreements (with Brazil, Vietnam, China and Russia) negotiated by US delegations headed by the US Maritime

Administrator. For example, the Brazilian Maritime Agreement allows for half of the shipments under a transaction to be shipped on Brazilian-flagged ships provided the exporter obtains a general waiver from MARAD. For Ex-Im Bank purposes, Ex-Im Bank treats the Brazilian shipping costs as US content. Of note, no waivers were requested or granted under the Maritime Agreement with Brazil in 2009.

**Figure 25** shows the number of Ex-Im Bank-related waivers granted by MARAD over 2007-2009. Although the waivers were granted in these years, the Ex-Im transactions they are associated with may have been approved by Ex-Im in different years. Total revenues to US and non-US flag carriers from 2009 shipments that fell under Ex-Im Bank's PR-17 program was \$35.2 million in 2009, a 112% increase over 2007. On average, about 95% of these revenues go to US flag carrying vessels.

**Figure 25: Number of Approved Ex-Im Bank Related PR-17 Waivers\***

Waiver Type	2007	2008	2009
Statutory	6	12	6
Compensatory	6	9	7
Conditional	0	0	0
General	1	0	0
<b>Total</b>	<b>13</b>	<b>21</b>	<b>13</b>

Source: MARAD

\*Totals reflect the number of Ex-Im Bank transactions associated with individual waivers.

As reflected above, granted waivers have been consistently kept to a minimum since MARAD only has exporters apply for a waiver after MARAD has determined it could not accommodate them with a US flag carrying vessel. This is intentionally accomplished by MARAD staff working with and educating Ex-Im Bank customers on US carrier service options for project cargoes. In tandem with this, MARAD keeps in constant contact with the US flag representatives enabling them to adjust their schedules to new cargo opportunities under this Program. When existing service may initially appear absent, MARAD on an ad hoc basis and when warranted, has been able to influence carriers in diverting ship itineraries to book Ex-Im Bank cargoes. These working arrangements have helped ensure that if there is truly no existing US-flag service, a waiver will be granted.

Because shipping ocean-borne cargo on a US flag carrying vessel can be associated with a higher cost, and because granted waivers are intentionally kept to a minimum, few transactions end up coming to Ex-Im where the PR-17 requirement applies and the cargo is ocean-borne. In 2009, Ex-Im authorized 10 transactions that were subject to MARAD and were not aircraft or being exported to Canada or Mexico. The associated ocean-borne cargo for these transactions included railroad transportation and power generation equipment.

## **G7 ECAs' Policies and Practices**

Of the G7 ECAs, only France and Italy have similar cargo preference requirements.<sup>1</sup> Lenders indicated that France's cargo preference restrictions are more easily waived than the MARAD restrictions that Ex-Im Bank users must follow. Lenders did not comment on Italy's cargo preferences.

## **Exporter and Lender Survey and Focus Group Results**

Cargo preference requirements can make US goods less competitive relative to foreign goods because most foreign exporters have no shipping requirements and US-flagged shippers generally charge higher rates. Lenders and exporters explained that the higher shipping costs and route scheduling challenges associated with shipping via US-flagged vessels is a prohibitive aspect of using Ex-Im Bank support. They note that in some cases US shipping requirements may be the sole reason why a US exporter may lose business to a foreign competitor. These requirements can actually hinder the realization of US exports by mandating shipping logistics and/or costs that make sourcing US equipment prohibitive. Other exporters noted that obtaining a waiver from MARAD is most successful when done far in advance or if a consultant is hired which, in such cases, leads the exporter and lender to give up and source product from another country. For US-domiciled multinationals with significant existing manufacturing operations already overseas, the MARAD requirements are so onerous that they are considering moving major US manufacturing lines overseas, enabling them to access foreign ECA financing without the burden of the MARAD requirements.

An exporter and lender survey conducted by Ex-Im Bank echoed similar sentiments regarding the uncompetitiveness of Ex-Im's US shipping requirements.

## **Conclusion**

As a condition of Ex-Im Bank's direct loan and long-term guarantee financing, US exporters are required to comply with US flag vessel requirements. The MARAD waiver data and anecdotal evidence from the focus groups and survey results suggest that only those exporters pre-approved for waivers by MARAD will be told to apply and eventually obtain a waiver. The process for obtaining a waiver can be long from initial contact with MARAD, and some exporters report having to hire a consultant to navigate the process. Exporters and lenders both assert the cargo preference rules and the higher costs associated with US flag vessels present a competitive disadvantage. Thus, the PR-17 policy, if present in a transaction, remains a negative aspect of Ex-Im financing relative to other ECAs.

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<sup>1</sup> IHS Global Insight, Inc., "An Evaluation of Maritime Policy in Meeting the Commercial and Security Needs of the United States," January 7, 2009.



# Chapter 6: Public Policies - Stakeholder Considerations

## Section E: Public Policy Competitiveness

Ex-Im Bank follows a set of public policy requirements that define the boundaries of where and how Ex-Im Bank can offer support to US exports. These requirements set Ex-Im Bank apart from other ECAs because, of the four policies, only foreign content and shipping have similar counter parts within other ECAs and only one – local cost – is controlled by the OECD. Therefore, the potential impact of these factors on case-specific competition has ranged from positive to neutral to extremely negative.

**Figure 26: Grading of Ex-Im Bank’s Public Policy Competitiveness, 2009**

Policy	G7 ECAs Have Similar Constraint? (Yes/No)	Potential Impact on Case-Specific Competitiveness
Economic Impact	No	Negative
Foreign Content	Yes (waning)	Extremely Negative
Local Costs	Yes	Positive
PR-17	Yes	Negative
Overall Assessment		Negative



## Chapter 7: Overall Results

For 2009, Ex-Im Bank’s overall competitiveness as compared to its G7 ECA counterparts is deemed to be an “A”.

**Figure 27: Grading of Ex-Im Bank’s Overall Competitiveness, 2009**

Structural Elements	Grade
Core Business Policies and Practices	<b>A</b>
A. Cover Policy and Risk Taking	A-/B+
B. Interest Rates	A
C. Risk Premia	A
Major Program Structures	<b>A</b>
A. Large Aircraft	A
B. Project Finance	A
C. Co-Financing	A-/B+
D. Environment	A-/B+
E. Foreign Currency Guarantee	B
F. Services	A-/B+
<b>OVERALL COMPETITIVENESS GRADE</b>	<b>A</b>

As illustrated in **Figure 27**, the balancing of these factors yields an “A” for 2009.

**Figure 28: Direction of Competitive Impact of US Economic Philosophy or Public Policy, 2009**

Areas Affected by US Economic Philosophy or Public Policy	Potential Case-specific Impact
Economic Philosophy:	
A. Tied Aid (de jure or de facto)	Negative
B. Market Windows	Neutral
Public Policy:	
A. Economic Impact	Negative
B. Foreign Content	Extremely Negative
C. Local Costs	Positive
D. Shipping – PR 17	Negative

### Trends

Over the past three years, Ex-Im Bank’s overall competitiveness rating remained at an “A-/B+” until 2009 when the grade increased to an “A” by the positive influences of Ex-Im’s local cost and co-financing programs. As shown in **Figure 29**, there have been three areas of movement in core business policies or major program structures.

**Figure 29: Grade Trends of Ex-Im Bank’s Overall Competitiveness, 2007-2009**

	2007	2008	2009
<b>Structural Elements</b>			
Core Business Policies and Practices	A	A	A
A. Cover Policy and Risk Taking	A	A-/B+	A-/B+
B. Interest Rates	A	A	A
C. Risk Premia	A	A	A
Major Program Structures	A-/B+	A-/B+	A
A. Large Aircraft	A	A	A
B. Project Finance	A	A	A
C. Co-Financing	B-/C+	B	A-/B+
D. Environment	N/A	N/A	A-/B+
E. Foreign Currency Guarantee	B	B	B
F. Services	N/A	N/A	A-/B+
<b>OVERALL GRADE</b>	<b>A-/B+</b>	<b>A-/B+</b>	<b>A</b>

Influencing the overall assessment of Ex-Im Bank’s competitiveness are the philosophical and public policies that the Bank is either required explicitly or implicitly to incorporate into its operational procedures. Tied aid and market windows represent two areas of philosophy in which Ex-Im Bank can respond when faced with foreign ECA competition.

On the other hand, the public policy considerations of economic impact, PR 17/MARAD requirements, and US content have represented negative influences on Ex-Im’s overall competitiveness.

**Figure 30: Directional Trends of US Economic Philosophy or Public Policy on Official Export Credit Activity, Procedures or Practices, 2007 – 2009**

Areas Affected by US Economic Philosophy or Public Policy	Potential Case-specific Impact on Competitiveness		
	2007	2008	2009
Economic Philosophy			
A. Tied Aid (de jure or de facto)	<b>Neutral to negative</b> <i>(infrequent; modest overall competitive impact)</i>	<b>Neutral to Negative</b> <i>(infrequent; modest overall competitive impact)</i>	<b>Neutral to Negative</b> <i>(infrequent; modest overall competitive impact)</i>
B. Market Windows	<b>Neutral</b> <i>(would likely be negative if encountered)</i>	<b>Neutral</b> <i>(would likely be negative if encountered)</i>	<b>Neutral</b> <i>(would likely be negative if encountered)</i>
Public Policy			
A. Economic Impact	<b>Negative</b>	<b>Negative</b>	<b>Negative</b>
B. Foreign Content	<b>Extremely Negative</b> <i>(frequent; significant impact)</i>	<b>Extremely Negative</b> <i>(frequent; significant impact)</i>	<b>Extremely Negative</b> <i>(frequent; significant impact)</i>
C. Local Costs	<b>Neutral</b>	<b>Neutral</b>	<b>Positive</b>
D. Shipping – PR 17	<b>Negative</b>	<b>Negative</b>	<b>Negative</b>



As is illustrated in **Figure 30** above, the views of the exporting community on the public policy aspects have not changed in any measurable degree despite the shift in local costs in becoming a positive competitive factor in 2009. This continuing trend is especially related to the issue of content -- where the exporting community sees the Bank's competitiveness extremely negatively affected over the last three years.



## Chapter 8: Financial Crisis

### Section A : Introduction

In looking back over the last 4 decades, there seems to be two distinct periods of significant change, with the beginning of each shift marked by a single cataclysmic political and/or economic event: the first structural change started with the abandonment of Bretton Woods (and the gold standard) in 1970; the second began in 1990 with the fall of Berlin Wall. The question now is whether the global financial crisis represents a third global shift as a turning point for the next 20 years, or has it just imposed a modest “pause” from the trends of the last 20 years?

Within that context, the purpose of the Prologue, Chapter 8B, is to set the stage for the current financial crisis by briefly reviewing the history and trends of the past 40 years, noting special highlights and turning points.

Chapter 8C takes a snapshot of the G7 ECAs’ overall responses to the financial crisis with an eye toward detecting if (1) the ECA world has reached another critical juncture as reflected in their respective mandates and philosophies, or (2) has the financial crisis simply offered an “opportunity” for ECAs to step up on a temporary basis to fill the most critical gaps in the export credit world.

Finally, Chapter 8D reviews, examines, and compares the efforts made by governments to bring export financing assistance to small- and medium-sized enterprises (SMEs) during the financial crisis.



## Chapter 8: Financial Crisis

### Section B: Prologue

The purpose of the Prologue is to provide a brief historical background and chronology of the evolution of the export credit world in the G7 countries over the last 20 – 25 years. While a major structural shift occurred in 1970 and lasted until the 1990s, the export credit landscape evolved in a fairly stable and predictable manner. However, in the late 1990s, major shifts brought about by both internal and external influences began to occur. These influences set the stage and direction for ECAs in the two decades that followed, but the recent financial crisis has dramatically affected their longer term strategies – if only on a “temporary” basis. Hence, the Prologue will mainly concentrate on the decades after the 1990s, rather than prior to this period.

From Ex-Im Bank’s perspective, one of the significant issues to emerge from the financial crisis is the impact the crisis could have on the competitiveness of ECAs. Prior to the financial crisis, the ECA world had been evolving toward a distinctly bifurcated system that included the Quasi Market Players (QMPs) who sought to become more commercialized and profit-oriented, but still with an official government status. At the other end of the spectrum, Lender/Insurer of Last Resort (LILR) ECAs have operated more as official public policy instruments seeking only to provide support when and where it was needed and on a long-term breakeven basis. This philosophical dichotomy had raised the question as to the nature of ECA competition going forward: whether the two camps could co-exist in harmony and compete on a level playing field, or whether they will be so disparate as to render competitive comparisons useless.

If the financial crisis has only put a “pause” in the QMP ECAs commercializing modality, then the outcome is more likely to be one in which mismatches occur and comparisons become much more difficult, if even possible. On the other hand, if the financial crisis has caused a more fundamental return to the traditional lender/insurer of last resort ECA, then competitive comparisons across programs and products will be more useful and transparent.

#### **Chronology of the Export Credit World from 1970 to 2010**

##### **1. 1970 - 1990**

The abandonment of Bretton Woods in the late 1960’s/early 1970’s forced all ECAs to re-evaluate their missions. As a consequence, OECD ECAs assumed the lender/insurer of last resort role. With the development of the OECD Arrangement during this period, greater discipline, structure, and transparency became the new ECA world order. With this new framework came the broadly held principle of neutralizing financing as a competitive instrument and the first step toward minimizing and controlling the costs of ECA export financing. Export promotion via export credits was beginning to wane as well as financing advantages were removed.

The next major shift came with the fall of the Berlin Wall in the late 1980s and triggered a chain reaction that once again transformed the ECA world. The entry of former Soviet-bloc countries in Eastern Europe and the emergence of China and other parts of Asia into the commercial world offered unprecedented economic opportunities at magnitudes not witnessed in the world since the early part of the last millennium.

Globalization of supply chains centered in Asia, Eastern Europe, and other low-cost labor countries began an irreversible and meteoric increase in manufacturing sourcing options, and with it, a dramatic increase in global trade flows. Moreover, global perceptions of risk, and in particular political risks, began to decline, and with it, concerns over commercial risk also diminished. Collectively, these events and influences effectively set the stage for a much expanded scope for risk-taking by both ECAs and the private sector in terms of the countries and buyers with which they were willing to do business. At the same time however, perhaps due to an overly optimistic perception of risk, overlooked pockets of risk did emerge, particularly in Latin America, that led to some ECAs' retraction and rebalancing by the end of the decade.

## **2. Decade of the 1990s**

In the US, the early 1990s at Ex-Im Bank witnessed a greater attention to risk, having just responded to the Latin American debt crisis. The export credit industry was dominated by Ex-Im Bank because the private sector was in a fledgling state. The private export credit industry in the US included AIG, the most prominent export credit provider (and foreign direct investment insurance); Chubb, who focused mainly on political risk cover, and Exporters, another small boutique insurer located in New York.

At the time, Ex-Im Bank was engaged in a partnership with the Foreign Credit Insurance Association (FCIA) which was, for all intents and purposes, an Ex-Im satellite located in New York. While FCIA was previously "owned" by an association of banks and exporters, the Latin America debt crisis of the 1980s effectively chased the private investors away, leaving Ex-Im Bank as the sole owner of FCIA. The Ex-Im Bank/FCIA relationship was one in which Ex-Im Bank assumed all political and commercial risks for short and medium-term insurance, while FCIA was charged with the responsibility of processing all short-term insurance applications. Ex-Im Bank handled the medium-term insurance.

In the early 1990s, a government-wide directive was issued that mandated that US government agencies should not delegate what was considered to be "inherently governmental functions" (IGF). Included as an IGF was the responsibility to determine how government funds should be allocated, and in the case of Ex-Im and FCIA, the delegated authority to underwrite and commit Ex-Im cover on behalf of the US government. Largely because of this directive, Ex-Im decided to terminate its agreement with FCIA, allowing FCIA to take those customers that they, as a private sector insurer, found attractive and left Ex-Im with the rest of the book of business, most of which were SME customers and/or customers that had relatively riskier portfolios.

As a result of this separation, Ex-Im was able to focus exclusively on those exporters that the burgeoning private export credit insurance industry did not want. Additionally, Ex-Im took proactive steps to ensure that it was not competing with the private market. For example, Ex-Im Bank intentionally increased its pricing across the board to assure the private insurers that Ex-Im would not undercut their pricing. Over the rest of the decade, the private export credit insurance industry in the US grew dramatically and successfully while Ex-Im's book of business became one dominated by and concentrated on small business exporters with a relatively lower overall dollar value. Concurrent with the growth of the private insurance industry was the expanded risk appetite of the commercial banking sector. Hence, the financial services industry was making important inroads into what had previously been the exclusive domain of the official ECAs.

During this period in Europe, a similar process was underway in which the government ECAs were divesting themselves of their short-term business. However, this was not because the ECAs actively chose to. Rather, as part of the European Union process, the EU Commission issued a directive in which it ordered the government ECAs to stop offering short-term support for "marketable risks" within the EU. What this effectively meant was that the government ECAs had to remove themselves from the short-term export credit business in any geographical area considered attractive to the private sector. While Ex-Im Bank had a clear and statutory requirement to assist SMEs, there was no similar mandate in the EU.

Canada and Japan, the other two G7 countries, and their ECAs, EDC and NEXI/JBIC respectively, continued by offering the full range of products from short-term up through long-term. While there was a small private export credit insurance industry in Canada, EDC was clearly the dominant player and had no directive or mandate to not compete with the private market. In fact, competing with the private market was openly permitted, whereas in Japan, there was no private export credit insurance industry. Much later (around 2005), the Japanese government encouraged NEXI, the official export credit insurer of Japan, to make sure that it was considerate of the emerging private sector, of which several were the foreign subsidiaries of European companies and US companies, like AIG.

Thus, by the end of the decade, the export credit insurance industry in the short-term field had undergone a major transformation with private insurers clearly taking a dominant and leading role in the short-term trade finance business. For those ECAs like US Ex-Im Bank and JBIC/NEXI of Japan, the governments acknowledged that there was a need in the short-term arena for government participation, but that participation should be limited to that part of the market where the private sector was not willing or able to step in. In the medium- and long-term areas governments continued to be the major export credit providers although a few private companies (e.g., Zurich and AIG) had begun to venture into the medium-term.

With the private sector demonstrating its ability and willingness to participate in handling risks that heretofore they were not able to assume, an evaluation of the need for and role of official ECAs was inevitable. The OECD, having previously set

parameters aimed at minimizing costs for ECAs, saw the expanded role of the private sector as a prime opportunity to squeeze as much subsidy out of export credits as possible and to eliminate the official ECAs' promotional role as well. They explained that, for this approach, it was necessary that ECAs not compete with, but supplement the growth of the private sector's capacity.

## **2. 2000 - 2007**

The early part of the decade were boom years as the global economy and exports grew at record rates. Competition was stiff worldwide and globalization had taken hold as a significant and irreversible trend. Globalization changed traditional business models by supplanting standard supply chains with low cost provider options in the developing world, many of which capitalized on and exploited their major economic differences. The big emerging markets in every corner of world of China, Brazil, India, Russia and South Africa, as well as the Eastern European countries, experienced record growth as well. Having employed sound and necessary economic reforms, the emerging markets' growing independence enabled them to thrive without having to rely entirely on the developed world. In fact, a major paradigm shift was the emergence of south-south trade. Furthermore, the traditional role of the West as the center of the economic world was challenged by the growing power and resilience of the emerging countries, most notably in Asia with China as the rising star.

At the same time, as the emerging markets proved their economic prowess and strength, the financial markets and banking industry took notice. Specifically, the markets began viewing the risk of these markets as more acceptable, rarely requiring the support of government risk protection. Official ECAs became less important and less necessary as the private sector's appetite for cross border risk grew dramatically. Clearly, the historical rationale for the existing ECAs as the lender/insurer of last resort yielded a relatively stagnant level of business at an ever higher degree of risk.

Another important intervention during this period was the mounting interest of the World Trade Organization (WTO) in the export credit world, an area within its purview but one that had not received much attention since the Tokyo Round in 1980. Heretofore, the OECD had operational responsibility for overseeing the proper behavior of official ECAs and had, for the most part, been highly successful, helping to establish international guidelines on ECA financing to avoid an expensive export credit "race to the bottom."

In the OECD, the focus was to create a level playing field among member ECAs so that buyers' purchase decisions would be made on the basis of market factors and not on government-supported and subsidized financing. However, when Brazil and Canada became entangled in a multi-year suit/counter-suit campaign at the WTO over the export credit financing of regional aircraft, the WTO created a critical role for itself in the ECA world by officially ruling on the meaning of key components of the Agreement on Subsidies and Countervailing Measures (ASCM). Perhaps the most important guidance to come out of the WTO ruling and the several other cases that followed was that ECAs needed to proactively seek and take all necessary steps to ensure that they



would break-even over the long-term. While even these rulings were open to interpretation, the ECA world chose to interpret this to mean that they had to do a better job of matching fees to risk on a case-by-case basis.

In some cases, ECAs chose to change their fundamental business model, transforming themselves from the LILR to more commercialized, private sector-like but still government-run ECAs – the QMPs. Others, like Ex-Im, chose to remain as the gap-filling type ECA focusing on complementing, not competing, with the private sector and taking reasonable risks. These ECAs tried to balance, but not necessarily do more than offset potential losses over the long-term. For Ex-Im, the difference between its primary responsibilities and the private sector purview was clearly divided. The Bank operated on the philosophy that so long as the private sector could and would assume the risks associated with cross-border exposures, then Ex-Im would assume the rest as long as it could find a reasonable assurance of repayment and could break-even over the long-term.

At the same time, motivated by the confluence of declining business volumes, the elimination of subsidies and the WTO rulings, other official ECAs of Canada (EDC), and Italy (SACE) in particular, saw their roles quite differently. Instead, making a profit and supporting transactions that were in the national interest (made by vs. made in) were their primary goals, even if it meant competing with the private sector. This became their *raison d'être*. Nevertheless, for the most part the OECD ECAs all operated within the confines of the OECD Arrangement and financing wars were the exception, not the norm.

However, just as peace was prevailing within the OECD ECA world, the use of financing as an export promotion tool blossomed in the East. That is, non-OECD ECAs, and in particular, the Chinese ECAs showed strong signs of growing usage of export credits for export promotion purposes, especially in Africa where they were offering preferential loans either in exchange for much needed resources (e.g. oil) or low cost loans on very extended repayment terms on projects in order to gain market share. Most of the terms and conditions of their financing *did* not and *do* not fit within the OECD guidelines, but China is not, and has never been, a member of the OECD; therefore they have no obligation to follow the OECD Arrangement.

In the short-term trade finance area, the only ECAs that continued to offer official support were Ex-Im, NEXI and JBIC of Japan and EDC of Canada while the other major ECAs stayed out of this area. The private insurance market was flush with business and was even beginning to go down market to the larger end of the SME population. Advances in information technology introduced capabilities to underwrite large numbers of small transactions at a profit. Hence, segments of the exporting population which were previously out of bounds showed promising results, including a limited foray into the medium-term export credit arena.

Moreover, the private European insurers invested serious capital and efforts to break into the large untapped potential in the US market, driving premiums down and

pushing underwriting standards to the limit. This approach also spread throughout the world as the private companies expanded to all corners of the global marketplace.

Thus, by 2007, the entire world of trade seemed to be growing by leaps and bounds and many of the major players in the export credit world became more active players than ever before. Clearly, the private sector insurers and banks were growing and expanding their respective scopes and taking on risks that were traditionally outside their comfort zones.

For official ECAs, with the emergence of China as a financing competitor, the tensions related to the “race to the bottom” during the 1970s and 1980s returned but in an unfamiliar form and in a different environment. However, the OECD ECAs found themselves restrained in their ability to respond because of perceived WTO limitations. Moreover, a number of ECAs found their roles stagnating and their relevance dissipating. As the world neared the end of the last decade, traditional ECAs faced major strategic decisions regarding the nature of their role and how to deal with an “old” competitive threat in a very different and new world.

### **3. 2008 - Present**

The collapse of Lehman Brothers and the near collapse of AIG in 2008 brought the financial systems and credit markets to an abrupt and grinding halt. As liquidity dried up globally and financial markets hit record lows, the export credit world suffered right along side the general market conditions. The short-term trade finance area was identified as having a very large and critical gap estimated at roughly \$250 billion. This gap was considered to be contributing to the dramatic slowing of essential trade. The IMF, the WTO, the OECD, and the World Bank convened an emergency G20 Task Force to address the gap by encouraging governments to commit to supplying much needed financial assistance.

For the US, however, the need for additional government assistance beyond what Ex-Im Bank could provide was not necessary. Ex-Im already had a short-term export credit insurance business in place and operated when the private insurance market providers’ support for trade finance dried up as well. Hence, Ex-Im Bank stood ready to absorb the additional demand. Moreover, Ex-Im’s risk assessment in the short-term program changed little, if at all, which contributed to significant increases in both applications and authorizations (See **Chapter 8D**).

In the EU, however, because the short-term credit insurance programs of official ECAs had all but shut down (with the minor exception of Euler Hermes’ government program), the EU exporters had no where to go for this type of short-term support. (The details of the short-term export credit insurance shortage and its impact in particular on SMEs are described in detail in **Chapter 8D**.)

During this period, the private lenders and the financial markets export credits for medium- and long-term tenors also dried up with little cross border transactions occurring except for those covered by official ECAs. Demand for official ECA support in

2008 and 2009 spiked dramatically. Without ECA support, neither commercial banks, nor syndications, nor the capital markets were willing or able to provide the same type or level of support that they did prior to the financial crisis. Moreover, many of the US lenders struggled to deal with their own losses and balance sheets, and tried desperately to recapitalize. Simply put, the global marketplace was perceived as more risky than ever before with much less credit available for any tenor and what was available was prohibitively expensive.

As 2009 came to an end, signs of a global economic recovery were emerging. Most parts of the financial market had stabilized and equity market activity slowly inched back up. Today, lenders seem to be returning to short-term trade finance, but not necessarily independent of ECA support. Demand for medium- and long-term export credits with ECA cover, however, has remained strong.

In looking back over the last 40 years, the official ECAs and the private sector have played musical chairs, with one being more dominant while the other played the supportive role. The most recent set of circumstances marked by the financial crisis have positioned official ECAs once again as playing a critical role in sustaining global trade flows.

In retrospect, the key issues for ECAs that have been raised over the last 18 months stemming from our somewhat chaotic environment include:

1. A global shortage of short-term trade finance;
2. A heightened absence of export financing support for small business exporters;
3. An increase in demand for direct ECA funding as the best, and in many cases, the only source of export credit financing;
4. The need for large volumes of support in the form of reinsurance capacity; and
5. The need for ECAs to act in their traditional role as lenders of last resort.



# Chapter 8: Financial Crisis

## Section C: Current State of Export Credits

### I. Introduction

The focus of last year's "Emerging Issues" chapter of the Competitiveness Report was to illuminate the impact of the global financial crisis on ECA business and the particular measures ECAs and their guardian authorities took to combat the crisis' impact on their national economies. International financial organizations, such as the OECD, the WTO, Berne Union, IMF, as well as individual ECAs acted quickly to keep international trade flows going with as little interruption as possible. Obviously, the actions of these parties could not halt the effects of the global economic downturn, but the measures taken to fill the gaps left by the retreat of commercial lenders from international finance, no doubt played an important role in keeping export financing more readily available and accessible.

The Report identified three kinds of trade and export finance concerns brought on by the crisis:

- 1) Availability of credit/financing
- 2) Liquidity
- 3) Pre-export/Short-term post shipment financing

International concerns about the impact of the financial crisis were mainly focused on short-term trade finance and how the retraction of the commercial lenders from export finance would affect trade flows. The past year, however, highlighted the fact that medium- and long-term exports were negatively affected by the scarce availability of financing and liquidity in the market. In response, ECAs played a critical role in keeping such transactions alive.

Last year, Chapter 8 concluded with questions as to how the measures imposed by ECAs and their governments enabled the ECAs to play an effective role in managing the financial crisis and their impact on ECA competitiveness. Some of the major areas of concern included protectionist measures, impact of domestic loans or guarantees, "Market Window-type" facilities and national interest initiatives, untied aid and untied loans. Furthermore, many ECAs were preoccupied with the ability of some ECAs (including Ex-Im Bank) to offer direct loans, when many others were not able to do so. In 2008, no one knew what role ECAs would play **after** the crisis was over and if there would be a "race to the bottom." Today, that question still persists.

ECAs undoubtedly have filled necessary gaps to keep exports moving during this tumultuous time; however, given the fact that many of the measures put in place to deal with the crisis are temporary (most measures sun-setting at the end of 2010), it is still too soon to tell which tools and mechanisms will stay and which will go. To handle the impact of the crisis, some ECAs reworked their mandates and business targets to make room for new products, while others responded with already existing tools. ECAs

economized on what resources they had available to them, but at the same time, became more creative and innovative in their responses to these new challenges.

In looking ahead, the fundamental question is did the financial crisis change the philosophical approaches of the Lenders/Insurers of Last Resort (LILRs) that include the US, France, Germany and Japan, and the Quasi-Market Players (QMPs) that include Canada, Italy and the UK? In other words, will the return to “normalcy” after the crisis further differentiate the approaches of the LILR and QMP ECAs or has the impact of the global crisis lessened the differences between these two groups? In order to understand the potential reorientation of these groups, it is important to observe the measures taken to combat the crisis and determine if amendments to mandates and strategic measures undertaken follow a pattern by either side.

**2. National Export Credit Initiatives to Address the Financial Crisis**

To find common trends within and between the two camps, an examination of changes made to business mandates, level of risk capacity, and risk assessment practices is discussed below. The key point here is to determine if actions undertaken by the ECAs within the two camps are indicators of an effort to maintain the philosophical approach pre-crisis or indicators of a major philosophical shift. The following six areas noted in **Figure 31** are key components to ECA business operations. A response of “yes” indicates that specific changes were made to that approach or practice, while a “no” response indicated no changes were made in light of the financial crisis.

**Figure 31: Changes to National Export Credit Approaches due to the Financial Crisis**

	Changes to Business Mandate or Targets	Changes in Level of Risk Capacity	Changes in Risk Assessment	Changes in Underwriting Terms and Conditions	Changes in Products	Changes in Monitoring Existing Portfolio
<b>Lenders/Insurers of Last Resort</b>						
<i>France</i>	No	Yes	No	No	Yes	No
<i>Germany</i>	No	No	No	Yes	Yes	Yes
<i>Japan</i>	No	No	Yes	Yes	Yes	Yes
<i>United States</i>	No	No	Yes	Yes	Yes	No
<b>Quasi-Market Players</b>						
<i>Canada</i>	Yes	Yes	No	No	No	Yes
<i>Italy</i>	No	Yes	Yes	Yes	Yes	No
<i>United Kingdom</i>	No	No	No	No	Yes	Yes

- **Changes to Business Mandate or Targets<sup>1</sup>**

Canada is the only ECA whose mandate changed because of the financial crisis. However, this change impacted their domestic financing sector rather than export credits, where their support for internal trade was broadened. While the other ECAs have said they made changes to their mandates, in fact the changes and modifications were made to products and risk assessment approaches rather than their fundamental philosophies. For example, France has been asked by their guardian authorities to enhance products to ease the financing of export contracts in light of the crisis. Japan is supplying insurance to Japanese banks to enhance their lending capacity and Germany's export credit cover facilities have been enhanced. On the QMP side, Italy began providing support for factoring and dealership financing as well as increased their percentage of cover.

- **Changes in Level of Risk Capacity**

Canada, Italy and France were the only ECAs to change their level of risk capacity in light of the financial crisis. In 2009, Coface saw their capacity increase in some major countries. Additional capital was injected into EDC, and the scope of their activity increased. As mentioned above, Sace's percentage of cover increased to 100 percent for transactions, determined on a case-by-case basis.

- **Changes in Risk Assessment**

Japan, Italy and the US made changes to their risk assessment approaches. NEXI began making more detailed assessments of buyer and bank risks, as well as enhanced attention to sovereign MLT transactions. Sace is paying more attention to the liquidity risk of their buyers and banks, while Ex-Im has changed some of its assessment of new risks in high-risk markets and/or sectors due to the economic conditions of the specific regions rather than the risk profiles of any particular buyer. Italy and Japan have placed a more watchful eye on risks and have instituted more monitoring into their risk assessment approaches and Ex-Im has changed its risk approach on particular parts of this portfolio.

- **Changes in Underwriting Terms and Conditions**

Sace is the only QMP ECA to have adjusted their underwriting terms and conditions. They have done this through having more risk-reflective premia and higher cover to facilitate the involvement of banks in transactions. Euler Hermes now allows the self-retention component of their supplier credit cover to be reduced from 15 to 5 percent. However, a higher premium is charged for such a decision. NEXI adjusts their terms and conditions when the OECD downgrades a country. Ex-Im now takes the depreciation of various currencies into

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<sup>1</sup> The changes noted in each section do not cover all of the changes/measures undertaken by the G7 ECAs. They are only indicative of the actions taken by each ECA.

consideration where appropriate. Doing so in effect “tightens up” its underwriting terms and conditions in the relevant markets. Furthermore, Ex-Im uses credit enhancements more frequently as tools to help determine the reasonable assurance of repayment of a buyer.

- **Changes in Products**

EDC is the only ECA to not make changes to their offered products. On the LILR-side, Coface amended its cover conditions for SMEs and offer better cover of export contracts during the manufacturing period. Euler Hermes now allows counter-guarantees to be obtained without supplier credit cover. Furthermore, the total eligible amount for counter-guarantees has been raised. NEXI now supports the loan financing for working capital of Japanese overseas subsidiaries. US Ex-Im modified its working capital program, is offering a premium reduction for SMEs under its short-term small business multi-buyer exporter policy and its short-term small business environmental exports policy, and introduced the “Take-Out” Option to help banks with their liquidity issues. ECGD has introduced a letter of credit guarantee scheme and Sace will now consider the extension of credit to the banks to be on lent to SMEs.

- **Changes in Monitoring Existing Portfolio**

Both Germany and Japan have strengthened the monitoring of their covered transactions to know sooner about any changes to the risks in their transactions. Canada has added resources to monitor their existing portfolio, and the UK has done the same.

### **3. Implications of the National Initiatives**

It is evident that each ECA has worked to fill market gaps and meet demand. Interestingly, the changes and initiatives undertaken by the G7 ECAs do not seem to draw a definitive line between the LILRs and QMPs. The changes seem to be driven by demand and to meet the individual needs of buyers/borrowers. For example, throughout the crisis, Ex-Im has maintained its role as a lender of last resort that does not compete with the private sector. Given the absence and inability of the financial markets to operate at full capacity throughout the financial crisis, demand for Ex-Im’s products increased. The Bank worked within its current structure to fill the gaps. In contrast, ECAs such as EDC and Sace, also did not make fundamental changes to their organizations, but actively addressed the needs of their customers.

Changes to address the crisis were not so much in terms of modifications to fundamental mandates, but rather strategic efforts by each ECA to be more proactive in terms of amending their products and approaches to meet demand. The LILR ECAs made the most changes to their products and risk assessment processes, filling their traditional role as “gap fillers” during times of market failures (**Figure 32**). The QMP ECAs made limited modifications to their export credit programs. However, this is not to say they did not work to combat the effects of the crisis in their respective economies.



**Figure 32: Spectrum of Changes to National Export Credit Systems**

Least Changes			Most Changes			
1	2	3	4	5	6	7
Canada	United Kingdom	Italy	Japan	Germany	France	United States

Hence, there is no indication that the actions taken by ECAs because of the financial crisis had any impact on the identities and philosophies of the diverging camps. Rather, it appears, for now, that ECAs worked within their existing frameworks to weather the crisis and support their national economies.



# Chapter 8: Financial Crisis

## Section D: Impact on Small- and Medium-Sized Enterprises & G7 Responses

### Introduction

The financial crisis has adversely affected virtually every layer of the US economy from the financial services industry, wholesale and retail trade, services, manufacturing, construction, and home sales. The small- and medium-sized enterprise (SME) community has been hit especially hard and has struggled to stay afloat in an unfriendly credit environment. This environment has been particularly prevalent when SMEs' business transactions have involved the riskier venture of exporting and obtaining the financing to facilitate exports. The general credit environment in which SMEs have operated was outlined in the Prologue to Chapter 8.

This section of Chapter 8 is to provide a comparative evaluation of the G7 ECAs and their respective governments' efforts to address the unique export financing issues confronting SMEs during the financial crisis. The focus of this examination is primarily the short-term trade finance area because it is the product and program area most used by SMEs. Moreover, the short-term area is not governed by the OECD. While the Berne Union offers guidelines on the proper conduct of this type of business, the guidelines are simply that and are not enforced in any way other than by moral suasion.

Generally, a competitive evaluation of the official short-term trade finance programs across ECAs has not been conducted because (1) short-term sales are not an area where financing elements typically have a competitive influence and (2) there are very few official ECAs that offer short-term programs. As previously explained, the EU ECAs except for Germany dropped all of their official short-term export credit insurance programs. This occurred because all EU risks were considered to be "marketable" and could be handled by the then-modest, but growing and privatized export credit insurance industry. However, due to the financial crisis, a gap evolved that was precipitated by a hastily retreating private export credit insurance sector that was designed to replace the government programs, a reluctant private lending sector, and the absence of any emergency response capability. SME exporters in the EU were clearly left without any source of support for their exporting and trade finance needs.

In the US, Canada and Japan, however, the official ECAs stayed in the trade finance business, driven at least in part by the recognition that the private sector would only go so far, especially as it concerned SMEs. US Ex-Im Bank in particular has a statutory mandate to support small business with at least 20% of its authorizations available for small business exporters. Even dating back before the small business set-aside was codified, Ex-Im Bank readily accepted its role as the SME trade finance facilitator because the private sector either did not exist or the private insurers who were in the market were clearly not interested in handling the smaller and less experienced

exporters. Private insurers welcomed Ex-Im Bank’s presence in this corner of the market.

The sections that follow discuss the approach the major ECAs and their governments have taken and compare the general and specific programs developed by the ECAs focused on SMEs.

### Overview and History of Official ECA Support for SMEs

The export credit world is comprised of both private and public sector ECAs. Virtually all private sector ECAs operate in the short-term export credit area (0 - 360 days) and several also operate in the medium-term credit range (1-5 years). On the other hand, official ECAs operate primarily in the medium- and long-term with relatively fewer offering short-term programs. Small SMEs tend to produce products and services that fall into the short-term arena such as consumables, commodities, spare parts, and finished goods, whereas medium and large companies tend to produce capital goods, aircraft and participate in large projects. The US, Canadian and Japanese ECAs all offer official short-, medium- and long-term export credit support. (See **Figure 33**).

**Figure 33: Official G7 ECAs— Overall Menu of Program Offerings**

ECA/ Program	Ex- Im/ USA	EDC/ Canada	ECGD/ United Kingdom	Coface/ France	SACE/ Italy	Euler Hermes/ Germany	NEXI/ JBIC Japan
Pre-Export/ WC	Yes	Yes	In process	No	No	No	No
Short-term	Yes	Yes	Letter of Credit guarantee - temporary	“CAP Export” <sup>1</sup> temporary	No	Yes; limited	Yes/No
Medium-Term	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Long-Term	Yes	Yes	Yes	Yes	Yes	Yes; temporary re- financing	Yes

However, as noted in the Prologue to Chapter 8, in the EU, the major official ECAs (with the exception of Euler Hermes of Germany) do not and have not provided short-term export credit support for approximately the last 12 years because of an EU Directive. Subsequently, greater attention was turned to SME export financing needs because many small businesses were having difficulties in accessing short-term export credit insurance or financing support from the private sector. Whether this attention was in response to the market gap or was purely coincidental is not clear. In 2005, the EU Commission extended the Directive until December 2010 and modified the guidelines effective January 2006 to allow EU ECAs to provide short-term insurance cover for SMEs, recognizing the financing difficulties SMEs faced in their international endeavors.

<sup>1</sup> CAP Export is a temporary short-term export credit program authorized by the EU Commission to the public part of Coface of France in cases where the private sector is not available and the transaction meets credit standards.

Specifically, in 2005, the EU Commission noted that:

“...due to the unavailable or insufficient cover in the majority of Member States of export credit insurance offered by private insurers to small companies with a limited export turnover, which is caused by no or very low profitability reflecting an insufficient spread of foreign countries/buyers and lack of education and knowledge of the complexities of export credit insurance among such companies entailing significant handholding and processing costs, the Commission is prepared to consider their export related risks as temporarily non-marketable in these Member States where there is no adequate offer by the private market, also in consideration of the need for the commercial insurers to adapt to the increased market sized created by the EU enlargement.”<sup>2</sup>

In 2007, the Final Report of the Expert Group on Supporting the Internationalization of SMEs notes that on the issue of export credit support for SMEs, one of the main barriers to SME internationalization is the lack of financial resources with access to sufficient and affordable finance. This is considered a fundamental pre-requisite for internationalization. The report continues: "Government programmes must focus on the provision of expertise usually associated with individualized programmes on the available financial support mechanisms." The report concludes on this point, however, "For trade related finance existing mechanisms (trade credit insurance, guarantees, factoring, etc.) the level of information and availability is good across most European countries."<sup>3</sup>

Even more recently, in 2008, the EU passed the “Small Business Act for Europe” or SBA that reflects the Commission’s political will to recognize the central role of SMEs in the EU economy and for the first time puts into place a comprehensive SME policy framework – with 10 guiding principles - for the EU and its member states. The Act applies to all companies which are independent and have fewer than 250 employees. 99% of all European businesses meet these criteria. According to Gunter Verheugen, EC Vice-President for Enterprise and Industry:

“Now is the time, once and for all, to cement the needs of SMEs in the forefront of the EU’s policy. The SBA brings the full weight of Europe behind SMEs – enlisting all the resources of Europe to help small business in their daily business and to clear the path for these that want to create more jobs and grow in Europe and beyond.”<sup>4</sup>

On December 15, 2009, the Commission adopted a report by a panel of experts on progress made in implementing the SBA, both at the EU and national level. While the

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<sup>2</sup> Official Journal of the European Union, Communication of the Commission to Member States amending the communication pursuant to Article 93(1) of the EC Treaty applying Articles 92 and 93 of the Treaty to short-term export-credit insurance (2005/C 325/11). Page 1.

<sup>3</sup> European Commission Enterprise and Industry Directorate –General, “Final Report of the Expert Group on Supporting the Internationalization of SMEs”, page 23. Feb. 2010

<sup>4</sup> [http://ee.europa.eu/enterprise/policies/sme/small-business-act/index\\_en.htm](http://ee.europa.eu/enterprise/policies/sme/small-business-act/index_en.htm)

findings articulated in this recent report note that access to finance by SMEs is of critical importance, the Report does not discuss specific components of the need for export related financing.<sup>5</sup>

As far as SMEs are concerned in the medium- and long-term area, the EU ECAs do not offer any special programs for small businesses but rather expect them to use the standard programs they have available for exporters of all sizes. Unless the SME exporter and their buyers qualify under their standard programs that are designed to earn a profit for the ECAs, SMEs' transactions may not be considered financeable and do not receive special attention.

It is important to note that, during this most recent period of global financial stress, those ECAs that continued to offer short-term export credit cover (Ex-Im Bank, EDC and NEXI) were praised by the world-wide banking sector. Without the insurance of the government ECA, the banks would have had to significantly limit their support, especially to SMEs. Conversely, trade finance lenders operating in the EU have not been willing to proactively participate because many of the private export credit insurers have retreated and are viewed as unreliable partners by the banking community.

In addition, many had begun to question the long term viability of some of the credit insurers, especially after the near collapse of AIG. Specifically, on March 2, 2010, it was reported that Coface's long-term counterparty credit and insurer financial strength was downgraded by S&P from A to A-; its short-term ratings were also lowered from A-1 to A-2. The consequence of such a downgrade could manifest as a lower level of confidence that the company will honor its obligations and accordingly, customers could shift their allegiance to another private or government ECA provider. The net effect is a lower level of overall capacity to meet market demands. As noted by the OECD, the WTO, and the G20 Trade Finance Experts, a significant gap in trade finance estimated at \$250 billion emerged during this financial crisis and was cited as contributing to the steep decline in global trade and economic growth.

Hence, private short-term export credit insurance in the EU has not always been an option and even when it has been available, lenders and small business exporters had become more reluctant to rely upon it, especially during the financial crisis. Thus, with the absence of consistent and reliable levels of official support, the bottom line is that lenders and small business exporters operating in the trade finance area in the EU have not had ready access to short-term export credit support from the private sector.

## **ECAs' Support for SMEs**

### **A. US Ex-Im Bank**

Ex-Im Bank is committed to providing needed export credit financing assistance to small business exporters and the US jobs that they maintain and support. In fact, about

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<sup>5</sup> European Commission, Commission Working Document, "Report on the implementation of the SBA", Brussels, COM (2009) 680.

85% of the Bank's transactions support small businesses. Small businesses can access all Ex-Im Bank products, including specialized small business financing tools such as the working capital guarantee and export credit insurance.

Recently, the Bank set a goal of doubling Ex-Im Bank's support for small business to \$8 billion over the next 2 years. Ex-Im Bank is approaching it from three angles. First, the Bank is focusing on outreach strategies involving partnerships and venues to reach a greater number of SME exporters to make them aware of Ex-Im Bank and the services to help them compete on a level playing field. In addition, the Bank is exploring improvements to its products and operations to make the Bank faster and easier with which to work; and, exploring new products and new channels of delivering existing products and leveraging the origination of underwriting capabilities of financial intermediaries. (In a recent ranking undertaken by the British Exporters Association, Ex-Im Bank and EDC of Canada each scored the highest in terms of offering the most extensive line of products).

During FY 2009, Ex-Im's short term export credit insurance program witnessed a dramatic increase in applications of 85 – 90% over year ago levels due to a significant number of private insureds migrating to Ex-Im Bank and previously uninsured exporters perceptions that credit insurance could bring value to their overseas sales efforts and their balance sheets. Moreover, the Bank's approval rate of buyers in the short term program during 2009 was roughly 80 – 90%, suggesting that Ex-Im's risk assessment practices in the short-term program had remained fairly stable.

With regard to Ex-Im's basic program menu, the Working Capital Guarantee and insurance products enable small businesses to increase sales by entering new markets, expanding their borrowing base, and offering buyers financing while carrying less risk. Often, small-sized exporters do not have adequate cash flow or cannot get a loan to fulfill an export sales order. The Ex-Im Bank Working Capital Guarantee was designed with the small exporter in mind and assumes up to 90% of the lender's risk so exporters can access the necessary funds to purchase or produce US-made goods and services for export.

Ex-Im Bank's short-term insurance policies protect an exporter against non-payment by their foreign buyers due to both commercial (insolvency, bankruptcy and default) and political risks (war, revolution, transfer risk) and also allows exporters to extend competitive credit terms to their foreign buyers. To qualify for Ex-Im's Small Business Policy, the exporter must be a small business according to the US Small Business Administration's definition of a small business, and have annual export credit sales of less than \$7.5 million (excluding confirmed letters of credit and cash in advance) for the last two years (including those of their affiliates). For the Small Business Policy exporters, special terms apply and include:

- No first-loss deductible
- Simplified premium-rate schedule

- Enhanced assignment (for qualified exporters), an attractive financing feature that allows a lender to add foreign receivables into the borrowing base or advance funds on the insured receivables with limited risk.

Ex-Im Bank's Small Business Group serves as the Bank's primary outreach and business development group for small business domestic customers. Exporter contacts are made through a network of regional offices and staff at the Washington, D.C. headquarters including Women and Minority Outreach, Trade Association Outreach, and Multiplier Training and Outreach.

In particular, Ex-Im Bank works with small businesses at the local level through its five regional offices that provide assistance to companies in their territories. The regional office network is the vital link between exporting communities located throughout the United States and Ex-Im Bank. The regional office network provides a geographic market-focused enterprise which broadens Ex-Im Bank's reach into small-size US exporting companies. The regional offices also work in partnership with other agencies through the US Export Assistance Centers serving the export communities' needs in order to harness all available Federal, State and Local resources to enhance and encourage small business export activity.

Ex-Im Bank also works through a nationwide network of over 50 city-state partners - state and local organizations that provide information and assistance on the Ex-Im Bank's products. The Bank also collaborates with 120 delegated authority lenders in all fifty states and the District of Columbia that can directly commit Ex-Im Bank's guarantee on working capital loans. In addition to the regional office staff, insurance brokers in every state can assist with Ex-Im Bank's export credit insurance applications.

## **B. EU ECAs' Support for SMEs**

The EU ECA model is one that is most often characterized as a private company that acts on behalf of their government in the medium- and long-term while the private side of the ECA operates on behalf of the private company. One common theme among all of the ECAs briefly described below is that they provide support on a "made by" vs. "made in" basis in varying degrees whereas here in the US, Ex-Im Bank supports "made by" US exports only. That is, Ex-Im Bank finances only the US portion of US goods and services, whereas the other ECAs will support up to 100% of the value of an export that contains a fairly high degree of foreign content.

1. **ECGD/United Kingdom:** ECGD was one of the first official ECAs to divest itself of its short-term export credit insurance book. In 1992, ECGD sold its short-term portfolio to NCM of the Netherlands, now known as Atradius. Since then, ECGD has operated only in the medium- and long-term export credit area and does not offer any special programs aimed at SMEs. However, as a temporary measure, the Government of the UK introduced a general purpose working capital guarantee program (not through ECGD) but it is not limited solely to export needs. ECGD introduced a letter of credit guarantee program in October 2009 to address the lack of liquidity in the short-term trade finance area.



While this temporary capacity is not focused exclusively on SMEs, presumably SMEs could benefit. ECGD has received inquiries from the UK exporting community regarding their re-entry into the short term insurance market. The Government is examining the market to determine if there is evidence of any systematic market failures that could justify a government intervention.

- 2. Coface/France:** Coface is a private company that acts on behalf of the French Government in the medium- and long-term export credit area but for the short-term book of business, Coface operates its credit insurance for its own account. Coface does not offer any special programs for SMEs. However, the public side of Coface has begun offering short-term insurance on a temporary basis (the CAP program) pursuant to permission obtained from the EU Commission from which SMEs could benefit. In addition, Coface has noted that it has modified a number of its terms and conditions of existing products for the benefit of SME exporters. Examples include removing per company thresholds, product and process simplification, and increasing percentage cover from 95% to 100% for SME insurance.
- 3. Euler Hermes/Germany:** Euler Hermes (EH) Germany is a private company that acts on behalf of the German Government in the medium- and long-term export credit support (along with PriceWaterhouse Coopers – PWC). It operates a bifurcated program in the short-term in which some of their portfolio is written on behalf of the private company with a limited amount on behalf of the German Government. In the past year, EH Germany increased the per exporter limit with their counter-guarantee program used primarily for performance bond purposes. Additionally, EH Germany, KfW, and the Federal Ministry of Economics and Technology created a new refinancing program. Most recently, Euler Hermes announced the creation of the Export Hotline and a promise to include more SMEs in trade delegations. However, to date the government scheme has no programs that are designed specifically for SMEs other than advisory services.
- 4. SACE/Italy:** SACE is a joint stock company backed by the Italian Government. Its short-term program is considered a private entity while SACE operates the medium and long-term programs for the Italian Government account. According to SACE, it has expanded the scope of its products generally and the terms and conditions (e.g., 100% cover on a case-by-case basis); SMEs can benefit as well as large exporters.

### **C. Other Official ECAs**

- 1. EDC/Canada:** EDC is a Crown Corporation of the Government of Canada and operates as the official ECA of Canada. EDC's support for exports spans all terms (short, medium, and long) as well as pre-export support mainly in the form of export working capital. EDC has a very strong focus on Canadian SMEs with the pre-shipment working capital and short-term programs aimed primarily at this segment of their exporting community. In addition to export support, EDC also provides domestic financing support acting as a one-stop-shop for SMES for their

domestic and export financing needs. Since the beginning of the financial crisis, the scope of EDC’s responsibility has been greatly expanded providing financing support for domestic funding needs, some of which are aimed at specific sectors. EDC has also enhanced some the terms and conditions of its export programs to include increasing the percentage cover for commercial banks from 85% to 100%.

2. **NEXI/Japan:** NEXI is one of two official Japanese export credit agencies with the other one being the Japan Bank of International Cooperation (JBIC). NEXI provides short-, medium-, and long-term export credit insurance. NEXI has increased its capacity for all export credit programs.
3. **JBIC/Japan:** JBIC is the lending ECA of Japan and offers direct funding for medium- and long-term exports but no support for short term export financing. Like NEXI, JBIC has increased its overall capacity and is offering consulting services to SMEs as well as offers loans to SMEs exporting to buyers in Asia.

## Summary

Of the G7 ECAs, US Ex-Im Bank and EDC of Canada offer the most robust menu of programs designed with SMEs in mind (**Figure 34**). Moreover, the support that these ECAs offer today are a “constant” and a relatively reliable source of export financing for small businesses. However, SMEs in other major exporting countries, especially in the EU, have not enjoyed this level or type of consistency and dependability.

**Figure 34: Official G7 ECAs Programs – SME Export Credit Support**

ECA/ Program	Ex-Im/ USA	EDC/ Canada	ECGD/ UK	Coface/ France	SACE/ Italy	Euler Hermes/ Germany	NEXI/ Japan	JBIC/ Japan
Pre- Export/ WC	Yes; WCGP	Yes; WCGP	In process	No	No	No	No	NA
Short-Term	Yes; SB Policy	Yes	Letter of credit	No; presumably CAP Export will do	No; “SACE BT” created	Yes; under “escape” clause; Launch of “Export Hotline”; trade delegations	Export credit insurance for SMEs (2005)	NA
Medium- Term	Standard	Standard	Sovereign Star Trade Finance Facility (ECA specific) <sup>6</sup>	Standard	Cassa Depositi e Prestiti easy loans private sector partner w/SACE	Standard	Standard	SME loans in Asia; Advisory & Consulting office for SMEs
Long-Term	Standard except for Tied Aid <sup>7</sup>	Standard	Standard	Standard	Standard	Standard	Standard	SME loans to Asia; Advisory services

<sup>6</sup> Sovereign Star Trade Finance Facility is a private sector export credit lender who provides fixed rate medium-term loans valued at 50,000 pounds up to 2 million pounds sterling for British exporters and is insured by ECGD.

<sup>7</sup> Under the Tied Aid program, Ex-Im Bank generally will not require that small business transactions meet the multiplier criteria such as evidence of follow-on sales to be done on commercial terms to match *de minimus* tied aid offers for commercially viable projects.

The trade finance gap identified during the current financial and economic crisis is emblematic of the exponential credit gap that has grown for SMEs since 1997. However, the EU Commission and Member States have apparently recognized the market failure that exists across their continent regarding trade finance for SMEs and efforts to address it are clearly underway.



## Appendix A: Calculation of Ex-Im Bank Grade

In the body of this report, the US exporting community provided “grades” on Ex-Im Bank policies and programs. In the sections of the report pertaining to the core financing programs and practices, grades based upon survey responses coupled with focus group responses and Ex-Im Bank’s analyses were assigned to each program and practice. In order to aggregate and average these grades for the determination of the overall competitiveness grade in Chapter 7, values were assigned to each grade that are comparable to those used in a typical US university. First, **Figure A1** provides the meaning and score of select grades. Averaged sub-category grades determined a category’s grade, and **Figure A2** illustrates the range of possible averaged scores that defined each grade. If a survey respondent did not have experience with a program or policy (that is, response was “NA”), the response was not calculated into the grade for that program or policy.

**Figure A1: Definition of Select Grades**

Grade	Definition	Score
<b>A+</b>	Fully competitive compared to other ECAs. Consistently equal to the (or is the sole) ECA offering the <b>most competitive</b> position on this element. Levels the playing field on this element with the most competitive offer from any of the major ECAs.	4.33
<b>A</b>	Generally competitive compared to other ECAs. Consistently offers terms on this element <b>equal to the average</b> terms of the typical major ECA. Levels the playing field on this element with the typical offer from the major ECAs.	4.00
<b>A-/B+</b>	Level of competitiveness is in between grades A and B.	3.50
<b>B</b>	Modestly competitive compared to other ECAs. Consistently offers terms on this element <b>equal to the least</b> competitive of the major ECAs. Does not quite level the playing field on this element with most of the major ECAs.	3.00
<b>B-/C+</b>	Level of competitiveness is in between grades B and C.	2.50
<b>C</b>	Barely competitive compared to other ECAs. Consistently offers terms on this element that are a <b>notch below</b> those offered by any of the major ECAs. Puts exporter at financing disadvantage on this element that may, to a certain extent, be compensated for in other elements or by exporter concessions.	2.00
<b>C-/D+</b>	Level of competitiveness is in between grades C and D.	1.5
<b>D</b>	Uncompetitive compared to other ECAs. Consistently offers terms on this element that are <b>far below</b> those offered by other major ECAs. Puts exporter at financing disadvantage on this element so significant that it is difficult to compensate for and may be enough to lose a deal.	1.00
<b>F</b>	Does not provide program.	0.00
<b>NA</b>	Does not have experience with policy/program.	

**Figure A2: Range of Averaged Scores for Each Grade**

Grade	Maximum Score	Minimum Score
A+	4.330	4.165
A	4.164	3.75
A-/B+	3.74	3.25
B	3.24	2.75
B-/C+	2.74	2.25
C	2.24	1.86
C-	1.86	1.50
D	1.49	0.50
F	0.49	0

Because the public policies and economic philosophies are not expected to impact the same volume of transactions as the core financing and program elements, survey respondents were asked to indicate if the public policies and economic philosophies would positively, negatively or neutrally affect Ex-Im Bank’s competitiveness. **Figure A3** shows the scale that was used by survey respondents to assess the competitive impact of these policies and philosophies.

**Figure A3: Assessing Impact of Economic Philosophies and Public Policies on Ex-Im Bank’s Overall Competitiveness**

	Effect on Competitiveness	Description
+	Positive	Philosophy, policy or program has a positive impact on Ex-Im Bank’s competitiveness (moves Ex-Im Bank’s competitiveness grade up one notch).
*	Neutral	Philosophy, policy or program has a neutral impact on Ex-Im Bank’s competitiveness (no impact on Ex-Im Bank’s competitiveness grade).
-	Negative	Philosophy, policy or program has a negative impact on Ex-Im Bank’s competitiveness (moves Ex-Im Bank’s competitiveness grade down one notch).

## Appendix B: Purpose of Ex-Im Bank Transactions

Congress requires Ex-Im Bank to include in the annual Competitiveness Report a breakdown of the purposes for Ex-Im Bank support for transactions. In that regard, the two purposes of Ex-Im Bank support for transactions are to either fill the financing gap when private sector finance is not available or to meet foreign competition. **Figure B1** shows the number and amount of Ex-Im Bank transactions authorized in 2009 by purpose and program type.

**Figure B1: Ex-Im Bank Transactions by Purpose, 2009**

	No Private Sector Finance Available		Meet Competition		Not Identified	
	(\$MM)	(#)	(\$MM)	(#)	(\$MM)	(#)
Working capital guarantees	\$927	329	\$0	0	\$0	0
Short-term insurance	\$8,784	2,261	\$0	0	\$0	0
Medium-term insurance	\$74	33	\$176	75	\$0	0
Medium & Long-Term Guarantees	\$2,536	26	\$8,712	34	\$0	0
Loans	\$2,942	9	\$2,601	9	\$0	0
<b>TOTAL</b>	<b>\$15,263</b>	<b>2,658</b>	<b>\$11,489</b>	<b>118</b>	<b>\$0</b>	<b>0</b>





# Appendix C: Exporter and Lender Survey Background

## Introduction

As part of Ex-Im Bank's statutory requirement to report annually on the Bank's competitiveness with its G7 ECA counterparts, Ex-Im Bank is also required to conduct a survey of exporters and lenders that used the Bank's medium- and long-term programs in the prior calendar year. This Congressionally-mandated survey provides critical information for the Report, as it encourages respondents to compare Ex-Im Bank's policies and practices with those of its G7 ECA counterparts during the calendar year. Ex-Im Bank continued its approach of administering the survey on-line, which permitted the survey to reach a larger number of potential participants. In addition to the formal on-line survey, Ex-Im Bank conducted focus group discussions with experienced users (exporters and lenders) of Ex-Im Bank programs to get more detailed comments about the global market in which they operated in 2009 and the competitive implications for Ex-Im Bank.

## Survey Questions

Ex-Im Bank's survey consisted of five parts that focused on the following areas:

- Part 1: General information on the profile of the respondent.
- Part 2: Respondent's experience in both receiving support from and facing competition from other ECAs, in addition to reasons for using Ex-Im Bank.
- Part 3: Respondent ratings of and comments on Ex-Im Bank's competitiveness with foreign ECAs with respect to the policies and programs described in the Competitiveness Report.
- Part 4: Additional comments.
- Part 5: Outcome of specific cases of competition faced as a result of the above policies.

## Participant Selection

The survey was sent to companies that used Ex-Im Bank's medium- and long-term programs during 2009. In total, 100 lenders and exporters were asked to participate in the survey.

## Survey Results

**Figure C1** highlights the response rate for the survey participants. Overall, the response rate for the survey was 32%. The response rate for lenders was higher than for exporters, with 50% of lenders responding and 21% of exporters responding. Looking forward, Ex-Im is examining ways to increase survey participation for future Competitiveness Reports.

**Figure C1: Survey Response Rate, 2009**

	Lenders	Exporters	Total
Number surveyed	38	62	100
Number responded	19	13	32
Response rate (%)	50	21	32

- **Lenders**

**Figure C2** shows the lender experience levels for both length of time in business and experience in export finance. A majority of lenders (74%) have been in business for over 21 years or more while the remainder (26%) has been in business from 4 to 20 years. Years of experience in export finance showed that 16% were relatively new to the business (3 had 4 to 10 years), while the large majority (84%) had over 11-plus years of experience in export finance.

**Figure C2: Lender Experience Levels, 2009**

	1-3 years	4-10 years	11-20 years	21+ years
Time in business	0	2	3	14
Time in export finance	0	3	3	13

**Figure C3** shows the volume of export credits extended during 2009. Of the 16 lenders who indicated these values, more than one-third (38%) reported having extended \$50 million or less during 2009, while the remaining offered between \$51 million to over \$1 billion. These data suggest that the more active lenders participating in Ex-Im Bank medium- and long-term programs were focused more on larger (in value) export transactions.

**Figure C3: Volume of Lenders' Annual Export Credits, 2009**

	Under \$10 million	\$10 - \$50 million	\$51 - \$100 million	\$101 - \$500 million	\$501 million - \$1 billion	Over \$1 billion
Number of Lenders	4	2	1	2	2	5

**Figure C4** shows the percentage of lenders' export credits extended during 2009 that were supported by Ex-Im Bank. Eighteen of the 19 lenders indicated the percentage of lender export credits that were Ex-Im Bank supported in 2009. Of these, 72% of the lenders noted that 75% of their export credits had Ex-Im Bank support, while the other 28% reported that less than 75% of their export credit portfolio had been supported by Ex-Im Bank.

**Figure C4: Percentage of Lender Export Credits That Were Ex-Im Bank Supported, 2009**

	Less than 10%	10%-25%	26%-50%	51%-75%	Over 75%
Number of lender's whose export credits were supported by Ex-Im Bank	0	2	2	1	13

Additionally, out of all 19 lenders, all but one noted that the lack of useful private sector financing was regularly the reason for pursuing Ex-Im Bank financing and that this need was worldwide. Nine of the 25 lenders stated that Ex-Im Bank support was regularly needed to meet competition from foreign companies receiving ECA financing, with Euler-Hermes/Germany, SACE/Italy, Coface/France, NEXI/Japan, and China Ex-Im/China cited as the most frequent ECAs with whom they had competed. Other ECAs cited on a slightly less frequent basis were EDC/Canada and ECGD/UK.

- **Exporters**

**Figure C5** shows the distribution of exporters by time in business. The majority of exporter respondents were long-standing, large companies. Except for one exporters who reported being in business for 4-10 years, all of the other exporters had been in business for 21 years or more, and of these, 62% had been exporting for 21 years or more.

**Figure C5: Exporter Experience Levels, 2009**

	1-3 years	4-10 years	11-20 years	21+ years
Time in business	0	1	0	12
Time in exporting	0	1	4	8

**Figure C6** shows the size of exporters based on sales and export sales volume. Eight of the 12 exporters who reported sales figures showed 2009 sales volumes of \$1 billion or greater. Seven exporters with sales of over \$1 billion also reported the same volume of export sales.

**Figure C6: Volume of Exporter Annual Sales and Exports, 2009**

	Under \$10 million	\$10 - \$50 million	\$51 - \$100 million	\$101 - \$500 million	\$501 million - \$1 billion	Over \$1 billion
Total sales volume	0	2	1	1	0	8
Total export sales volume	1	1	1	2	0	7

**Figure C7** shows the distribution of exporters by the percentage of export sales that were supported by Ex-Im Bank. Of the 10 companies who responded, 6 showed that Ex-Im Bank support comprised less than 10% of their export sales while the

remaining 6 indicated that Ex-Im Bank supported from 10% to over 75% of their sales.

**Figure C7: Percentage of Exporters' Sales That Were Ex-Im Bank Supported, 2009**

	Less than 10%	10%-25%	26%-50%	51%-75%	Over 75%
Percentage of export sales supported by Ex-Im Bank	6	3	2	0	1

Eleven of the exporters reported facing regular competition from foreign companies supported by their national ECAs throughout 2009. The most frequently identified competitor ECAs (in descending order) were Euler Hermes/Germany, EDC/Canada, COFACE/France, EGDC/UK, and China Eximbank, with the remaining ECAs identified equally as frequently with one another. Furthermore, three exporters reported facing regular competition with BNDES/Brazil.

### **Working with Other ECAs**

Three exporters noted that they had never worked with another ECA, whereas two exporters explained that it worked regularly with every G7 ECA.

Frequent partners identified by the lenders were all of the G7 ECAs, led by Euler-Hermes. Non-G7 ECAs cited as partners were Korea Eximbank, Atradius, EKN, Finnvera and CESCE.

## Appendix D: G7 Export Credit Institutions

- Canada**   ▪ **Export Development Canada (EDC)** is a “Crown Corporation” (i.e., a government entity that operates on private sector principles) that provides, among other products, short-term export credit insurance, medium- and long-term guarantees, and medium- and long-term direct loans, which may or may not be provided on a CIRR basis. EDC also offers investment financing products and operates a “market window.” EDC also offers domestic credit insurance.
- France**   ▪ **Compagnie Française d’Assurance pour le Commerce Extérieur (COFACE)** is a private insurance company that provides, in addition to short-term insurance for its own account, official medium- and long-term export credit insurance on behalf of the French government.
- Germany**   ▪ **Euler Hermes Kreditversicherungs-AG (Hermes)** is a consortium of a private sector insurance company and a quasi-public company that provides official export credit insurance on behalf of the German government, similar to COFACE of France. Hermes also provides short-term export insurance for its own account according to standard market practices as well as a small portion for the state account under an EU “escape clause”, which has been extended due to the financial crisis on a temporary basis.
- **Kreditanstalt für Wiederaufbau (KfW)** is a financial institution that is owned by the German government and the federal states (Länder). KfW exists to promote the growth of the German economy in a variety of ways. One of its missions, though not its largest, is the funding of German export credits, both at market rates and through a government-supported window to achieve CIRR financing. KfW offers trade and export credit support on a limited basis and also administers the provision of German tied aid funds on behalf of the German government. The decision as to where and how tied aid should be used rests with another part of the German government. In 2008, the majority of KfW’s export credit business was spun off into an independent, 100%-owned subsidiary called KfW-IPEX Bank. In addition, the KfW-IPEX Bank offers project finance and carries a “AA-” rating.

- Italy**
- **SACE**, or Servizi Assicurativi del Commercio Estero, provides official export credit insurance. Pursuant to a law enacted in 2003 and effective January 1, 2004, SACE became a limited liability joint stock company whose shares are wholly owned by the Ministry of Economy and Finance. Under this structure, SACE provides medium- and long-term official export credit insurance on behalf of the Italian government, and short-term insurance for its own account.
  - **SIMEST** provides interest rate support to commercial banks in order to achieve CIRR. SIMEST is a development financier, with public and private participation, instituted in 1990 for the promotion and construction of joint ventures abroad. The Ministry of Foreign Trade is the majority shareholder. The private shareholders consist of Italian financial institutions, banks and business associations.
- Japan**
- **Nippon Export and Investment Insurance (NEXI)** is an independent governmental institution responsible for official export credit insurance operating under the guidance of the Ministry of Economy, Trade and Industry (METI).
- Historically, Japanese exporters were required to insure all of their short-term business through NEXI, but in 2004, the Japanese government removed this requirement and began welcoming private insurers into the Japanese export credit insurance market. NEXI offers short-, medium- and long-term export credit insurance.
- The **Japan Bank for International Cooperation (JBIC)** is a government bank that falls under the Ministry of Finance. In its capacity as an export credit agency, JBIC provides direct loans in combination with commercial bank financing. In addition, JBIC provides untied and investment loans, guarantees and import credits. Beginning in October 2008, JBIC began operating within the purview of the Japan Finance Corporation Law. As a result of this change, JBIC will also be responsible for promoting overseas development of strategic natural resources, supporting efforts of Japanese industries to develop international business operations, and responding to financial disorder in the international economy.
- United Kingdom**
- **Export Credits Guarantee Department (ECGD)** is a separate department of the UK government that provides export credit guarantees and interest rate support for medium- and long-term official export credit transactions. As a consequence of the financial crisis, ECGD is offering a letter of credit guarantee for short term on a temporary basis.

## Appendix E: Ex-Im Bank Foreign Content Support

### All Transactions

Product/Project	Medium-Term*		Long-Term*	
	Export Value	FC%	Export Value	FC%
Aircraft	\$43,082,000	23%	\$10,454,323,471	14%
Oil and Gas Projects	\$990,000	15%	\$3,472,470,530	7%
Construction Equipment	\$19,454,985	13%	\$94,183,285	11%
Power Plant	0	0%	\$1,136,988,893	20%
Other	\$141,157,081	14%	\$583,674,913	16%
<b>All</b>	<b>\$204,684,066</b>	<b>16%</b>	<b>\$15,741,641,092</b>	<b>13%</b>

### Medium-Term Transactions

Country	Product/Project	Export Value	Foreign Content Percentage**
Argentina	Construction Equipment	\$797,485	4%
Argentina	Medical Equipment	\$112,516	15%
Azerbaijan	Farm Equipment	\$2,859,512	17%
Azerbaijan	Metal Manufacturing Equipment	\$6,183,124	2%
Brazil	Construction and Mining Equipment	\$3,076,699	10%
Brazil	Construction and Mining Equipment	\$2,645,123	16%
Brazil	Construction Equipment	\$335,000	29%
Brazil	Construction Equipment	\$3,780,860	15%
Brazil	Large Aircraft	\$5,247,000	15%
Brazil	Medical Equipment	\$2,468,459	11%
Brazil	Medical Equipment	\$1,448,500	14%
Brazil	Medical Equipment	\$1,803,235	11%
Brazil	Medical Equipment	\$518,000	10%
Brazil	Medical Equipment	\$900,000	15%
Brazil	Medical Equipment	\$998,750	19%
Brazil	Medical Equipment	\$5,000,000	15%
Brazil	Medical Equipment	\$557,000	10%
Brazil	Medical Equipment	\$912,950	29%
Brazil	Medical Equipment	\$513,000	15%
Brazil	Medical Equipment	\$1,800,000	15%
Brazil	Medical Equipment	\$3,331,920	27%
Brazil	Medical Equipment	\$740,000	15%
Brazil	Medical Equipment	\$489,798	7%
Cayman Islands	Small Aircraft	\$14,600,000	31%
China	Industrial Machinery Manufacturing	\$9,122,067	23%
China	Medical Equipment	\$6,094,129	21%
Colombia	Printing Equipment	\$8,200,000	20%
Costa Rica	Refrigeration Equipment	\$1,068,758	0%

Dominican Republic	Construction Equipment	\$460,000	3%
Dominican Republic	Medical Equipment	\$1,426,200	22%
Dominican Republic	Medical Equipment	\$283,000	6%
Dominican Republic	Medical Equipment	\$270,000	6%
Dominican Republic	Medical Equipment	\$264,387	16%
Dominican Republic	Oil and Gas Field Equipment	\$990,000	15%
Guatemala	Farm Equipment	\$567,593	9%
India	Farm Equipment	\$9,050,000	6%
India	Solar Water Plant	\$2,202,082	17%
Indonesia	Small Aircraft	\$23,235,000	19%
Indonesia	Telecommunications Equipment	\$7,871,997	12%
Jordan	Farm Equipment	\$3,000,000	14%
Mexico	Construction Equipment	\$949,361	27%
Mexico	Construction Equipment	\$2,354,450	14%
Mexico	Construction Equipment	\$366,875	14%
Mexico	Construction Equipment	\$1,189,132	3%
Mexico	Farm Equipment	\$419,368	6%
Mexico	Printing Manufacturing Equipment	\$490,335	6%
Mexico	Printing Manufacturing Equipment	\$2,408,620	10%
Mexico	Telecommunications Equipment	\$997,772	12%
Nigeria	Boats	\$39,895,630	10%
Russia	ATMs	\$7,627,119	24%
Russia	ATMs	\$3,155,875	26%
Russia	ATMs	\$4,530,385	13%
Turkey	Printing Equipment	\$1,000,000	15%
Turkey	Printing Machinery	\$575,000	9%
Virgin Islands (British)	Construction Equipment	\$3,500,000	15%
<b>Total &amp; Average</b>		<b>\$204,684,066</b>	<b>16%</b>

### Long-Term Transactions

Country	Product/Project	Export Value	Foreign Content Percentage**
Bahrain	Power Plant	\$191,279,880	22%
Brazil	Aircraft Parts	\$16,000,000	15%
Brazil	Locomotives	\$98,899,843	17%
Canada	Construction and Mining Equipment	\$21,923,040	8%
Canada	Construction Equipment	\$51,462,151	13%
Canada	Locomotives	\$11,620,186	9%
Canada	Small Aircraft	\$132,385,340	30%
Chile	Large Aircraft	\$50,114,701	13%
Chile	Large Aircraft	\$227,293,839	9%
Czech Republic	Large Aircraft	\$87,083,486	15%
Egypt	Large Aircraft	\$223,493,976	15%
Germany	Photography Equipment	\$17,400,000	20%



Germany	Photography Equipment	\$5,507,000	7%
India	Large Aircraft	\$1,452,341,931	15%
India	Large Aircraft	\$18,137,455	14%
Ireland	Large Aircraft	\$508,000,000	15%
Ireland	Large Aircraft	\$504,000,000	16%
Ireland	Large Aircraft	\$264,000,000	16%
Ireland	Large Aircraft	\$330,000,000	16%
Ireland	Large Aircraft	\$264,000,000	16%
Israel	Large Aircraft	\$86,000,000	15%
Israel	Large Aircraft	\$43,000,000	15%
Japan	Large Aircraft	\$191,000,000	9%
Japan	Large Aircraft	\$157,920,000	12%
Kuwait	Large Aircraft	\$89,000,000	15%
Mexico	Oil and Gas Field Equipment	\$228,574,041	2%
Mexico	Oil and Gas Field Equipment	\$685,722,123	2%
Mexico	Oil and Gas Field Equipment	\$171,430,531	2%
Mexico	Oil and Gas Field Equipment	\$114,287,020	2%
Mexico	Oil and Gas Field Equipment	\$342,861,061	2%
Mexico	Power Plant	\$65,312,000	15%
Morocco	Large Aircraft	\$97,400,000	15%
Netherlands	Large Aircraft	\$125,565,721	12%
Netherlands	Large Aircraft	\$38,194,709	15%
Netherlands	Large Aircraft	\$77,405,084	16%
Nigeria	Power Plant	\$16,537,676	2%
Norway	Large Aircraft	\$276,765,800	15%
Panama	Large Aircraft	\$78,888,219	16%
Papua New Guinea	Natural Gas Projects	\$1,929,595,754	11%
Peru	Railroad Services	\$13,515,211	4%
Russia	Large Aircraft	\$75,899,998	15%
Russia	Large Aircraft	\$28,354,969	15%
Russia	Large Aircraft	\$26,000,000	15%
Saudi Arabia	Power Plant	\$132,040,929	20%
Saudi Arabia	Power Plant	\$137,747,122	24%
Saudi Arabia	Power Plant	\$534,182,310	19%
Singapore	Large Aircraft	\$299,250,000	16%
Spain	Telecommunications Equipment	\$183,523,424	11%
Switzerland	Construction Equipment	\$20,798,094	9%
Trinidad and Tobago	Small Aircraft	\$11,294,805	24%
Turkey	Large Aircraft	\$35,302,900	21%
Turkey	Power Plant	\$59,888,976	18%
United Arab Emirates	Large Aircraft	\$144,681,000	12%
United Arab Emirates	Large Aircraft	\$284,838,000	12%
United Arab Emirates	Large Aircraft	\$287,274,000	12%
United Arab Emirates	Large Aircraft	\$429,171,000	12%

United Arab Emirates	Large Aircraft	\$686,000,000	14%
United Arab Emirates	Large Aircraft	\$132,226,244	13%
United Arab Emirates	Large Aircraft	\$143,550,000	12%
United Kingdom	Telecommunications Equipment	\$237,209,249	21%
United States	Large Aircraft	\$1,422,500,000	15%
United States	Large Aircraft	\$537,755,000	15%
United States	Small Aircraft	\$588,235,294	13%
<b>Total &amp; Average</b>		<b>\$15,741,641,092</b>	<b>13%</b>

Source: Ex-Im Bank

\*Data excludes Credit Guarantee Facilities.

\*\*When eligible foreign content exceeds 15%, the buyer is required to make a minimum cash payment equal to the amount of foreign content.

# Appendix F: Tied Aid Report

## Introduction

Sections 10(G) and 2(b)(1)(A) of the Export-Import Bank Act of 1945, as amended, require Ex-Im Bank to submit a report to Congress on tied aid. Congress specifies that the report contain descriptions of the following: (a) the implementation of the OECD Arrangement rules restricting tied and partially untied aid credits for commercial purposes, including the operation of notification and consultation procedures; (b) all principal offers of tied aid credit financing by foreign countries, including information about offers notified by countries who are Participants to the Arrangement, and in particular, any exceptions under the Arrangement; (c) any use of the Tied Aid Credit Fund by the Bank to match specific offers; and (d) other actions by the United States Government to combat predatory financing practices by foreign governments, including additional negotiations among participating governments to the Arrangement.

## Implementation of the OECD Arrangement Rules Governing Tied and Partially Tied Aid: Overview and Definitions of the Various Types of Aid

Tied aid has the potential to distort trade flows when the recipient country selects the bidder offering the cheapest financing rather than the bidder offering the best price, quality and service for the equipment. The potential for trade distortion is most serious in cases where a donor government provides relatively low concessionality<sup>1</sup> tied aid financing for “commercially viable”<sup>2</sup> projects. Under these circumstances, a donor government’s tied aid offer may be an attempt to “buy” a sale for its national exporter through the provision of an official subsidy to a recipient country. This can establish the exporter’s presence and technology in the country to create longer-term international trade advantages. Below is a description of the various forms of aid and the OECD disciplines that may apply to each.

Tied aid is generally considered to be concessional financing support provided by donor governments that links procurement by recipient countries to firms located in the donor country or a limited number of countries. Tied aid can take the form of a grant (that can be offered as a grant plus a standard export credit) or a “soft” loan (that can be offered as a long-term loan bearing a low interest rate and/or extended grace period).

The OECD Participants have agreed to rules that govern a subset of the broader tied aid – the most egregious subset from a trade-distorting perspective. The OECD rules governing tied aid are also known as the “Helsinki rules”. Accordingly, “*Helsinki-type*”

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<sup>1</sup> The term “concessionality” refers to the total value of the subsidy being provided by the donor to the recipient country for any one project or purchase. For example, if a country receives a grant of \$100 million for a \$100 million project, the concessionality level of this aid would be 100%, whereas a grant of \$35 million combined with a traditional export credit for the remaining \$65 million would have a concessionality level of 35%.

<sup>2</sup> “Commercially viable” means that a project can service market-term or standard Arrangement- term financing over 10-15 years, depending on the type of project.

tied aid was tied aid that was governed by the Helsinki Disciplines that were agreed in 1991. Thus, the Helsinki Disciplines, coupled with the then existing requirement for 35% concessionality (number 4, as follows), today, govern tied aid and can be summarized as: (1) no tied aid for commercially viable projects<sup>3</sup>; (2) all tied aid must be notified to OECD Members at least 30 business days before the ECA makes a financing commitment; (3) no tied aid for wealthy countries [defined as those with a per capita Gross National Income (GNI) at or above \$3,855, with this figure changing annually because it is based on annually-adjusted World Bank lending criteria – see **Annex 1** and **2** for details]; and (4) tied aid offers must have a minimum of 35% concessionality.

“*Non-Helsinki-type*” tied aid includes all other tied aid offers excluded from the “Helsinki-type” tied aid. These are (1) *de minimis* projects (valued at less than approximately \$3 million), (2) grants or near-grants (at least 80% concessionality), and (3) partial grants (at least 50% concessionality) that are offered to the UN-declared Least Developed Countries or LDCs.

*Official Development Assistance (ODA)*, or aid, is concessional financial support of which at least 25% is intended to carry no repayment obligations (i.e., contains 25% grant element)<sup>4</sup>, and the vast majority of it is 100% pure grant (such as from USAID). Aid from a donor government to a recipient government that supports the purchase of specific goods and/or services from local, donor country and/or third country suppliers, necessary for the completion of an investment or specific project is trade-related. ODA can be tied or untied to procurement from the donor’s country.

*Untied aid* refers to concessional financing that is trade-related, but which should **not** be conditioned (contractually or otherwise) upon the purchase of goods and/or services from any particular country.

## **Implementation of the OECD Arrangement**

In 1991, the Participants to the OECD Arrangement agreed to rules governing the use of tied aid (the Helsinki Package). The tied aid rules went into effect in February 1992. Since that time, the use of tied aid for commercially-viable projects has significantly declined. In 2005, the OECD Participants revised a 1997 document known as “Ex-Ante Guidance Gained for Tied Aid” which compiles the project-by-project outcomes of OECD consultations that were held from 1992 through 1996. The “Ex-ante Guidance”

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<sup>3</sup> Commercial viability, which OECD members determine on a case-by-case basis, has two components: (1) financial viability, which refers to a project’s ability to service market-term, or standard Arrangement-term, financing over 10-15 years (depending on the type of project); and (2) the general availability of ECA financing for such a project. See **Annex 3** and **4** for details.

<sup>4</sup> The OECD Development Assistance Committee’s (DAC) technique for measuring concessionality (grant element) of ODA is antiquated. The DAC uses a fixed 10% discount rate, which results in one half of annual ODA levels having a real concessionality level below 25%, and some substantially less. For example, untied aid credits have been notified with as low as 6% real concessionality and theoretically could provide only 4% real concessionality. The United States has been seeking agreement in the OECD to update the DAC methodology.

describes which projects are typically considered to be commercially viable (CV) and commercially non-viable (CNV). See Annex 3 and 4 for details<sup>5</sup>.

In sum, since they came into effect in early 1992, the OECD tied aid rules have helped reduce tied aid to an annual average of about \$5 billion, from an estimated average of \$10 billion annually prior to 1992. Most remaining tied aid volumes have been re-directed away from commercially-viable sectors and toward commercially non-viable sectors.

### **Current Status of the OECD Negotiations on Tied and Untied Aid 2009**

The OECD and the US continue to monitor the effectiveness of the Helsinki tied aid rules that came into effect in early 1992. In 2009, the data shows that the tied aid disciplines have generally contained the use of tied aid. There were no tied aid offers that were examined by the OECD Consultations Group in 2009.

With respect to untied aid, historical concerns regarding Japanese untied aid (that reached its highest levels -- about \$15 billion-- a decade ago) prompted the US to seek the same disciplines for untied aid that were agreed for tied aid. Donor and recipient countries resisted US efforts to discipline untied aid (claiming that untied aid did not pose a serious threat to free trade and that disciplines for untied aid would only reduce much needed aid to developing countries). However, in 2005, the OECD agreed to a transparency agreement for untied aid that requires OECD Members to (a) notify project loan commitments at least 30 days prior to the opening of the bidding period; (to allow for international competitive bidding); and (b) report the nationalities of the bid winners on an annual ex-post basis. In 2009, the untied aid transparency reporting showed that in terms of outcomes of the bidding procedures associated with the untied aid offers, more than one-third of the contracts were awarded to top suppliers from China.

### **Tied Aid and Untied Aid Activity**

With respect to tied aid, in 2009, the volume of Helsinki-type tied aid decreased to approximately \$4.6 billion (down from \$7.3 billion in 2008). However, there was a slight increase in the number of tied aid notifications to 135, indicating that more transactions were approved, but at a lower monetary value as compared to 2008 (when three very large transportation projects drove an upward spike in the tied aid volume). The data for 2009 shows a continuation of tied and untied aid trends evidenced over the last five years or so. Specifically, Spain has consolidated its position as the largest donor of tied aid, accounting for over \$1 billion of tied aid activity. Asia continued to be the primary region receiving tied aid. The main recipient countries were Vietnam (in terms of volume) and China (in terms of number).

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<sup>5</sup> The OECD Consultations Group examines projects that have been notified by a Participant as eligible for tied aid, but which another Participant believes to be *ineligible* for tied aid because they appear to be CV. Sovereign guarantees from the recipient government do not factor into the determination of “commercial viability” because they can be provided for any kind of project – CV or CNV.

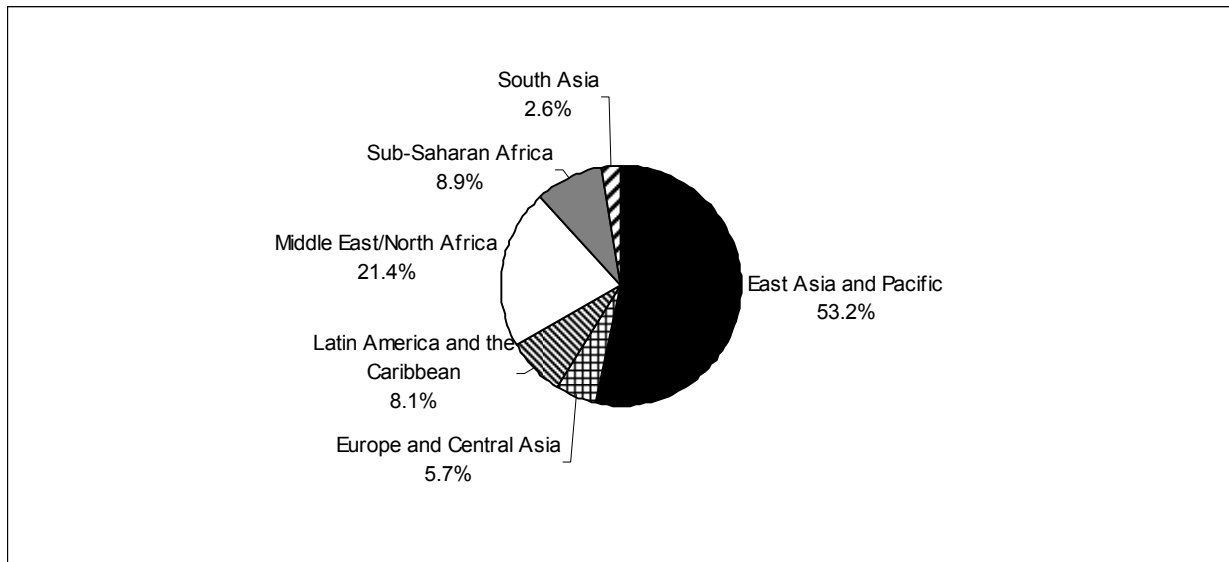
With respect to untied aid, in 2009, the volume of and number of untied aid notifications increased a modest amount. That is, the volume of untied aid increased from under \$10 billion in 2008 to \$11.3 billion in 2009 (a 13% increase). The number of untied aid offers decreased, from 77 notifications in 2008 to 62 notifications in 2009. Japan continued to account for the majority of the notifications in terms of volume (over 80%) while Germany reported the highest number of notifications (about 40%). The main recipient of untied aid was Thailand, attracting 30% of the total volume of tied aid, followed by China, who received about a quarter of the untied aid spread over 14 transactions. In terms of outcomes of the bidding procedures associated with the untied aid offers, more than one-third of the contracts were awarded to top suppliers from China.

**Eligible Markets, Major Donors and Sector Concentration**

The OECD rules designate a number of key markets as ineligible for tied aid financing. Specifically, the OECD rules ban tied aid into high- or upper middle-income markets (those that are ineligible to receive 17-year loans from the World Bank) and tied aid into Eastern Europe and select countries of the former Soviet Union, unless the transaction involves outright grants, food aid or humanitarian aid. (See **Annex 1** for a list of key markets for which tied aid is prohibited and **Annex 2** for a list of key markets eligible for Ex-Im Bank tied aid support.)

**Figure F1** shows the distribution of Helsinki-type tied aid offers by region in terms of value. In 2009, the major beneficiary region continued to be Asia (including South and East Asia and Pacific), attracting over half of the Helsinki tied aid offers, or roughly 53%.

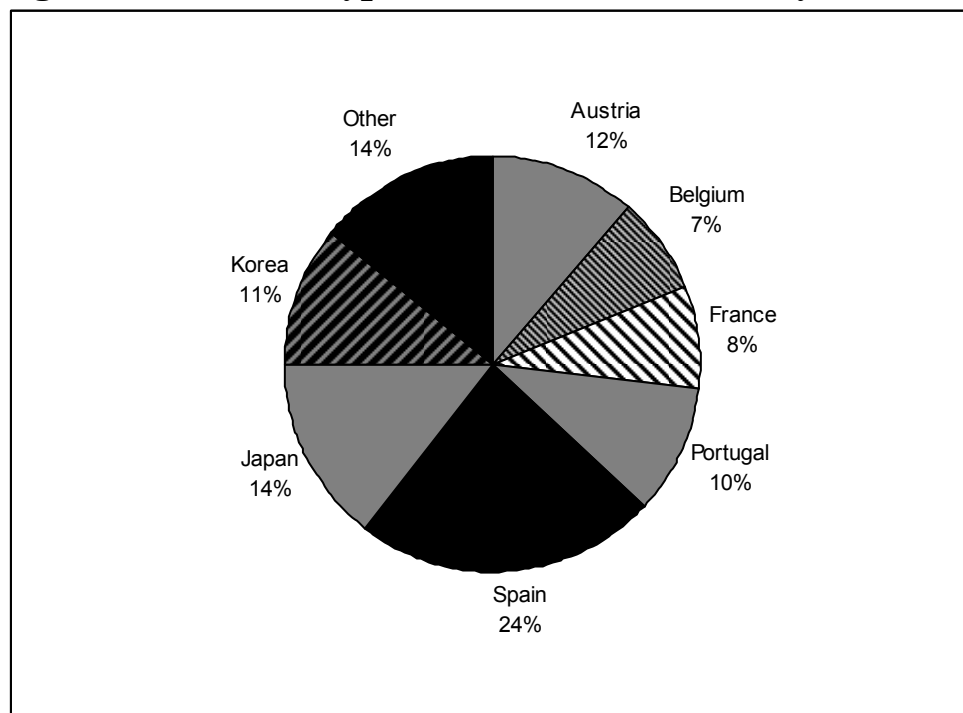
**Figure F1: Helsinki-type Tied Aid Notifications by Region (by Value), 2009**



**Figure F2** shows the variety of donor countries that offered tied aid in 2009. Spain has consolidated its position as the largest donor of tied aid, accounting for over \$1 billion of

tied aid activity. Asia continued to be the primary region receiving tied aid. The main recipient countries were Vietnam (in terms of volume) and China (in terms of number). See Chapter 5A for more details.

**Figure F2: Helsinki-type Tied Aid Notifications by Donor (by value), 2009**



Looking at sector concentration, in 2009, about over half of the total number of Helsinki-type tied aid notifications were concentrated primarily in the transport and storage sectors (principally road, rail and water transport). Although energy generation and supply (including renewable and non-renewable energy projects) attracted a modest number of notifications, most of the projects benefitting from tied aid were in the public health and water sanitation sectors, that tend to be considered commercially non-viable (CNV).

In 2009, no projects were evaluated by the OECD Consultations Group.

### **Trends in the Use of the Tied Aid Capital Projects Fund**

Ex-Im Bank, in consultation with Treasury, has established guidelines for the use of the Tied Aid Capital Projects Fund (TACPF). These guidelines have two core components:

1. A series of multilateral and/or domestic efforts (e.g., no-aid agreements, preliminary offer of “willingness to match”, actual offer of matching) that attempt to get competitors to drop consideration of tied aid use and/or let tied aid offers expire for projects of interest to US exporters.
2. A set of “multiplier” criteria (e.g., prospect of future sales without the need for tied aid) that attempt to limit tied aid support to those transactions

whose benefits extend beyond that particular project, but can be expected to generate future benefits, as well.

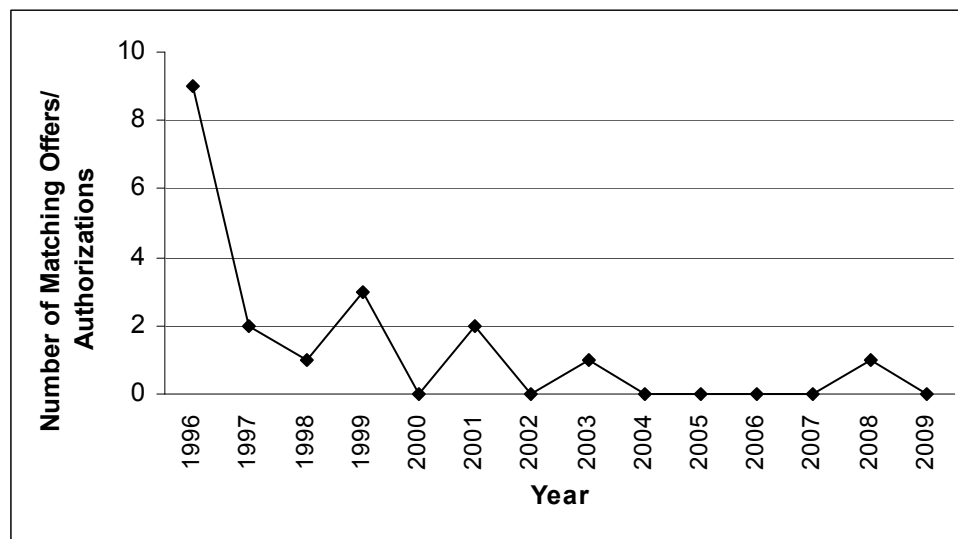
In addition, and in response to the 2006 Ex-Im Bank Reauthorization, Ex-Im Bank and Treasury have worked collaboratively to develop Tied Aid Procedures to guide tied aid application processing.

As reflected in **Figure F3** and **F4**, in 2009, Ex-Im Bank did not issue any new tied aid offers. However, one tied aid offer (authorized in 2008) was won by the U.S supplier and became operative in 2009. **Figure F3** also shows cumulative offers since 1992, and compares the offers and outcomes from the years 1992-2004 to the past five years, 2005-2009. The period-to-period comparison contrasts the sharp decline in Ex-Im Bank tied aid offers in recent years when compared with Ex-Im Bank tied aid matching activity between 1992 and 2004. Specifically, over the past five years, one project in Sub-Saharan Africa, approved in 2008, has benefitted from tied aid funds. Other instances of US exporter interest in Ex-Im Bank tied aid involve financing of certain capital equipment (e.g., rail cars; wind turbines; medical equipment) that were allegedly destined to commercially non-viable projects.

**Figure F3: Cumulative Ex-Im Bank Matching of Foreign Tied Aid Offers**

	2009	1992-2002	2003-2009
New matching offers	0	43	3
U.S. wins	1	19	2
U.S. losses	0	24	1
Outstanding, no decision	0	3	1
Total	1	43	3

**Figure F4: US Tied Aid Authorizations by Year**





It is important to note that the sharp decline in US tied aid matching offers coincides with the data showing that the majority of foreign ECA tied aid offers are made in accordance with the OECD rules. Nevertheless, despite the dwindling tied aid offers, US exporters sporadically express concerns regarding the use of tied aid by non-OECD Members, such as China. In addition, US exporters seeking to do business in Sub-Saharan Africa or certain Least Developed Countries (LDCs) encounter commercial lending limits and borrowers requiring concessional financing for US goods, which US exporters are not able to provide. These concerns regarding limited financing availability are exacerbated by the lack of uniform aid financing rules between the OECD, the Development Assistance Committee (DAC), the International Monetary Fund (charged with monitoring country debt) and the borrower countries. Thus, US exporters confront varying financing packages (provided by OECD or non-OECD Members, in accordance with OECD, DAC, IMF or borrower country rules) that are not readily comparable or “matchable”. For example, the DACs rules governing aid offers requires that aid financing be 25% concessional (compared to the OECD 35% concessional requirement). Such disparities create lengthy processing delays and result in US exporter frustration regarding the role and purpose of the Tied Aid Fund.

### **US Government Actions to Combat Foreign Tied Aid**

In addition to monitoring the OECD rules governing tied aid, the U.S government has used “common lines” as a way to combat predatory financing practices by foreign governments. A “common line” is an agreement whereby one OECD Member anonymously proposes that all Members refrain from providing aid for a specific project that is otherwise eligible to receive aid. When Ex-Im Bank receives an application for financing in a tied aid eligible country and the US exporter has reason to be concerned about the possibility of tied aid financing competition, Ex-Im Bank may propose a no aid common line in hopes of eliminating this possibility. If the common line request is accepted, all OECD member countries agree not to offer tied aid financing for the particular project for a period of two years (with the possibility of extensions). If the no aid common line request is rejected (any one Member can reject a common line request, irrespective of their involvement in the particular project), OECD member countries may make tied aid financing offers for the project.

The most recent US proposed no aid common line occurred in 2005, for rail cars (locomotive sales) to Indonesia. The common line was rejected and as the US exporter had evidence of competitor offers and documented the possibility of follow-on sales on commercial terms, Ex-Im Bank issued a tied aid Willingness to Match offer to the US exporter in 2005, and subsequently extended this offer until it expired in 2009. The results of the bid are not yet known.

Common lines are intended to be anonymous to prevent buyer retaliation against an exporter whose government issued a common line on its behalf. In practice, however, buyers are often aware of which donors/exporters are competing for specific projects and can determine who proposed a common line.

In sum, US exporter experience with common lines has been mixed. Of the 15 common lines proposed since 2000, a little less than half (7 of 15) were accepted. Because of the potential for buyer backlash, common lines are not issued without prior exporter approval and none have been issued in recent years.

<b>Key Markets Where Tied Aid is Prohibited</b>	
<b>Americas*</b>	Argentina, Chile, Jamaica, Mexico, Panama, Uruguay, Venezuela
<b>Asia*</b>	Hong Kong (China), Korea, Malaysia, Singapore
<b>Middle East*</b>	Bahrain, Israel, Kuwait, Lebanon, Oman, Qatar, Saudi Arabia, Turkey, United Arab Emirates
<b>Africa*</b>	Botswana, Gabon, South Africa
<b>Eastern Europe</b>	Czech Republic, Hungary, Poland, Slovak Republic, Belarus**, Bulgaria, Latvia, Lithuania, Romania**, Russian Federation**, and Ukraine**.

\*These markets are not eligible for tied aid because their Gross National Income (GNI) per capita for at least two consecutive years was sufficient to make them ineligible for 17-year loans from the World Bank.

\*\*Article 33. b 5 of the OECD Arrangement states the Participants' agreement to "avoid providing any tied aid credits, other than outright grants, food aid and humanitarian aid as well as aid designed to mitigate the effects of nuclear or major industrial accidents or prevent their occurrence" to these markets. Only such projects as described here would be eligible for tied aid in these markets.



<b>Key Tied Aid Eligible Markets</b>	
<b>Asia</b>	China, India, Indonesia, Philippines, Thailand, Vietnam
<b>Americas</b>	Colombia, Dominican Republic, Ecuador, El Salvador, Guatemala, Paraguay, Peru
<b>Africa</b>	Egypt, Namibia
<b>Middle East</b>	Jordan

Note: In addition to OECD tied aid eligibility, the US Government has developed criteria to apply to tied aid requests to determine whether tied aid can be made available (e.g., follow on sales criteria and “dynamic market” evaluation).



<b>Projects Generally Considered Commercially Viable (Helsinki-Type Tied Aid Prohibited)</b>	
<b>Power</b>	<ul style="list-style-type: none"> <li>▪ Oil-fired power plants</li> <li>▪ Gas-fired power plants</li> <li>▪ Large hydropower plants</li> <li>▪ Retrofit pollution-control devices for power plants</li> <li>▪ Substations in urban or high-density areas</li> <li>▪ Transmission and/or distribution lines in urban or high-density areas</li> </ul>
<b>Energy Pipelines</b>	<ul style="list-style-type: none"> <li>▪ Gas transportation and distribution pipelines</li> <li>▪ Gas &amp; oil transportation pipelines</li> </ul>
<b>Telecommunications</b>	<ul style="list-style-type: none"> <li>▪ Equipment serving intra- and inter-urban or long-distance communications</li> <li>▪ Telephone lines serving intra- and inter-urban or long-distance communications</li> <li>▪ Telephone lines serving internet or intranet system</li> <li>▪ Switching equipment serving urban or high-density areas</li> <li>▪ Radio-communications equipment serving urban or high-density areas</li> <li>▪ Air traffic control equipment</li> </ul>
<b>Transportation</b>	<ul style="list-style-type: none"> <li>▪ Freight railroad operations (locomotives, cars, signaling)</li> </ul>
<b>Manufacturing</b>	<ul style="list-style-type: none"> <li>▪ Manufacturing operations intended to be profit-making</li> <li>▪ Privately-owned manufacturing operations</li> <li>▪ Manufacturing operations with export markets</li> <li>▪ Manufacturing operations with large, country-wide markets</li> </ul>





<b>Projects Generally Considered Commercially Non-Viable (Helsinki-Type Tied Aid Permitted)</b>	
<b>Power</b>	<ul style="list-style-type: none"> <li>▪ Power projects that are isolated from the power grid</li> <li>▪ Distribution lines to low-density, rural areas</li> <li>▪ Some transmission lines to low-density, rural areas</li> <li>▪ District heating systems</li> <li>▪ Renewable energy (e.g., geothermal power plants, small wind turbine farms, small hydropower plants connected with irrigation)</li> </ul>
<b>Telecommunications</b>	<ul style="list-style-type: none"> <li>▪ Telephone switching equipment serving low-density, rural areas</li> <li>▪ Switching equipment serving low-density, rural areas</li> <li>▪ Radio-communications equipment serving low-density, rural areas</li> </ul>
<b>Transportation</b>	<ul style="list-style-type: none"> <li>▪ Road and bridge construction</li> <li>▪ Airport terminal and runway construction</li> <li>▪ Passenger railroad operations (locomotives, cars, signaling)</li> <li>▪ Urban rail and metro systems</li> </ul>
<b>Manufacturing</b>	<ul style="list-style-type: none"> <li>▪ Highly-localized, small scale cooperatives</li> <li>▪ Highly-localized, small scale food processing</li> <li>▪ Highly-localized, small scale construction supply</li> </ul>
<b>Social Services</b>	<ul style="list-style-type: none"> <li>▪ Sewage and sanitation</li> <li>▪ Water treatment facilities</li> <li>▪ Firefighting vehicles</li> <li>▪ Equipment used for public safety</li> <li>▪ Housing supply</li> <li>▪ School supply</li> <li>▪ Hospital and clinic supply</li> </ul>



## Appendix G: Human Rights and Other Foreign Policy Considerations

The Export-Import Bank Act of 1945 was amended in 1978 by legislation referred to as the “Chafee Amendment,” P.L. 95-630, 92 Stat. 3724. The Chafee Amendment, as amended in 2002 by P.L. 107-189, states “Only in cases where the President, after consultation with the Committee on Financial Services of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate, determines that such action would be in the national interest where such action would clearly and importantly advance United States policy in such areas as international terrorism (including, when relevant, a foreign nation’s lack of cooperation in efforts to eradicate terrorism), nuclear proliferation, the enforcement of the Foreign Corrupt Practices Act of 1977, the Arms Export Control Act, the International Emergency Economic Powers Act, or the Export Administration Act of 1979, environmental protection and human rights (such as are provided in the Universal Declaration of Human Rights adopted by the United Nations General Assembly on December 10, 1948) (including child labor), should the Export-Import Bank deny applications for credit for nonfinancial or noncommercial considerations.” 12 U.S.C. § 635(b)(1)(B).

It should also be noted that, pursuant to Executive Order 12166, the President has delegated his authority to make Chafee determinations to the Secretary of State, who must consult with the Secretary of Commerce and the heads of other interested Executive agencies.

Ex-Im Bank and the State Department, including the Bureau for Democracy, Human Rights, and Labor, have developed procedures for regular consultation on human rights concerns. According to these procedures, the State Department provides to Ex-Im Bank a list of countries with human rights concerns. Countries not on that list are pre-cleared. Where a proposed transaction over \$10 million involves goods or services to be exported to a country that has not received “pre-clearance,” Ex-Im Bank refers the transaction to the State Department for human rights review. In addition, Ex-Im Bank country economists may work in concert with the State Department, where appropriate, to examine human rights and other foreign policy considerations in their assessment of the risks associated with transactions in specific countries.

Various other statutory provisions addressing human rights and other foreign policy concerns may also impact Ex-Im Bank programs. For example, with respect to Ex-Im Bank’s approval of support for the sale of defense articles or services for anti-narcotics purposes, Ex-Im Bank may approve such a transaction only following satisfaction of a number of statutory criteria, one of which is that the President must have determined, after consultation with the Assistant Secretary of State for Democracy, Human Rights and Labor, that the “the purchasing country has complied with all restrictions imposed by the United States on the end use of any defense articles or services for which a guarantee or insurance was [previously] provided, and has not used any such defense articles or services to engage in a consistent pattern of gross violations of internationally recognized human rights.” 12 U.S.C. § 635(b)(6)(D)(i)(II).



## Appendix H: Equal Access for US Insurance

Pursuant to the Export Enhancement Act of 1992, Ex-Im Bank is required to report in the annual Competitiveness Report those long-term transactions approved by Ex-Im Bank for which an opportunity to compete was not available to US insurance companies.

At the time the legislation was enacted, Ex-Im Bank had neither encountered nor been informed about any long-term transaction for which equal access for US insurance companies was not afforded. Consequently, Ex-Im Bank, the Department of Commerce and the Office of the United States Trade Representative agreed that the establishment of a formal reporting mechanism was not necessary. It was also agreed that should Ex-Im Bank identify any long-term transaction in which US insurance companies are not allowed equal access, a more formalized procedure would be created. As of December 2009, Ex-Im Bank had not identified any long-term transaction in which US insurance companies were not allowed equal access.



# Appendix I: Trade Promotion Coordinating Committee (TPCC)

## Introduction

This section of the report responds to Section 8A(a)(2) of Ex-Im Bank's charter which requires the Bank to report on its role in implementing "The National Export Strategy" (the NES). The purpose of the NES is to outline the trade promotion agenda of the acting Administration and it is compiled by the Trade Promotion Coordinating Committee (TPCC).<sup>1</sup> For the next five years, the NES will follow the activities and recommendations of the National Export Initiative (NEI) which was created by President Obama with the aim to double American exports by 2015. As part of the Initiative, Ex-Im Bank is a member of the Export Promotion Cabinet and will meet alongside top leaders from Commerce, Treasury, State, Department of Agriculture, Small Business Administration, and the United States Trade Representative to report on Ex-Im's focus and progress on key issues of the Initiative.

Highlights of Ex-Im Bank activities and achievements related to the NEI in 2009 include:

### Small business initiatives:

Pursuant to Section 3(f) of its charter, Ex-Im Bank established a Small Business Division to encourage the participation of small business in international commerce by providing outreach and transaction advocacy on behalf of small businesses. In FY 2009, the efforts of the Small Business Division yielded noteworthy results:

- Ex-Im Bank authorizations of \$4.86 billion (or 17% of total authorizations) in direct support of small businesses;
- Ex-Im Bank approved 2,700 transactions (or 87% of the total number of transactions) for the direct benefit of small business exporters.
- Ex-Im conducted 93 outreach events (or 25% of Ex-Im's trade promotion activities).

### Renewable Energy and Environmental Initiatives:

Ex-Im Bank is committed to increasing the level of support it provides to US exporters of environmentally beneficial goods and services, as well as to US exporters participating in environmental projects located internationally. To achieve this objective, Ex-Im Bank provides enhanced levels of financial support for a broad range of renewable energy and other environmentally beneficial exports. In FY 2009, Ex-Im Bank's initiatives to support renewable energy and environmentally beneficial transactions yielded noteworthy results:

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<sup>1</sup> The NES is not required to be published during a year in which there is a transition in Administration. Thus, for 2009 there was no published National Export Strategy.

- Ex-Im Bank became the first ECA to adopt a comprehensive Carbon Policy to guide its support of United States exports in light of climate change concerns. Included in the policy is a commitment to explore ways to further improve the Bank's transparency in the tracking and reporting of CO2 emissions from projects that it supports. As a part of this policy the Bank has established for the first time a \$250 million facility to finance renewable energy exports, including solar, wind and geothermal energy. The policy also commits the Bank to be a leader in financing climate-friendly technologies made by American workers, including those that reduce greenhouse gas emissions and increase energy efficiency.
- Ex-Im Bank's Renewable Energy and Environmental Exports Program were presented at the five international conferences and more than 60 trade promotion events. Ex-Im Bank staff was the key speaker at wind and water energy conferences to promote the Bank's renewable energy and environmental finance programs. Ex-Im Bank was able to promote project financing for renewable energy and environmentally beneficial projects because of the flexible terms allowed under its participation in the OECD (Organization for Economic Cooperation and Development) Renewable Energy and Water Projects Understanding.

	Environmentally Beneficial	Renewable Energy
2009 Authorizations	\$ 385.42 million	\$100.04 million

### Emerging Markets:

Africa: In 2009, Ex-Im Bank participated in outreach events to Angola, Cote d'Ivoire, Kenya, Nigeria, and South Africa and presented at four conferences in Africa on Ex-Im's offerings and initiatives. Ex-Im joined five other US government agencies to promote US business and investment to Africa. The events aimed to foster trade and relationships between producers of US agricultural and energy equipment producers and African markets. In addition, Ex-Im worked with three US-African Chambers of Commerce to personally meet with groups of African buyers and lenders to endorse US export interests.

A comparison of G7 ECA and US Ex-Im Bank medium- and long-term support in this region in 2009 is reflected in **Figure I1** below.

**Figure I1: G7 ECA Medium- and Long-Term Activity in Africa, 2009 (\$US million)**

	Africa
G7*	\$ 7,988.2
US	\$379.3 (4.7%**)

\*Includes medium- and long-term officially supported export credits by ECAs in Canada, France, Germany, Italy, Japan, UK, and the United States

\*\* Values in parentheses represent the % of total G7 medium- and long-term support to the region



## Appendix J: Efforts to Promote Renewable Energy Exports

In 2006 Congress extended Ex-Im Bank's 2002 mandate to report on efforts to promote support for renewable energy exports and accomplishments resulting from those efforts to Congress on an annual basis. Accordingly, since 2002 Ex-Im Bank has reported on the activities and accomplishments undertaken to respond to the mandate.

During 2009, Ex-Im Bank responded in three major ways to the Congressional mandate:

1. **Banner Year Authorizations.** In 2009, Ex-Im Bank tripled its renewable energy authorizations to over \$100 million in 2009. This activity represented a record amount over that of previous years (\$30.4 million in 2008; \$2.7 million in 2007; and \$9.8 million in 2006). Ex-Im Bank financed a wide array of US renewable energy exports, including renewable energy technologies for solar, wind, geothermal and hydro-power projects. Ex-Im Bank supported five financial guarantees for \$61 million, one working capital guarantee for \$3.6 million, and 12 export credit insurance transactions totaling \$35.4 million.
2. **Policy changes.** In June 2009, US efforts at the Organization for Economic Cooperation and Development (OECD) to expand financing options for renewable energy exports contributed to a permanent agreement on Enhanced Financing Terms for Renewable Energy and Water Projects, that allows, among other enhancements, for a repayment term of up to 18 years. In addition, in November the Ex-Im Bank Board of Directors approved the Ex-Im Bank Carbon Policy, making the Bank the first export credit agency to approve a policy addressing climate change impacts of transactions receiving its financial support. The Carbon Policy calls for the Bank to consider a full range of incentives for renewable energy exports to foreign buyers. Specific incentives for such technologies were approved in 2010.<sup>1</sup>
3. **Expanded Marketing Efforts.** Ex-Im Bank has redoubled its marketing efforts and added two additional staff members to the Office of Business Initiatives, responsible for renewable energy and other environmental exports. These additional human resources made it possible for Ex-Im Bank to process its record number of renewable energy applications while at the same time continuing its participation in a number of renewable energy conferences. Ex-Im Bank also held significant speaking roles – including a keynote speaker role at the India 2009 Expo; American Wind Energy Association Annual Conference; American Water Works Association Annual Conference; the Water Environment Federation Annual Trade Show (“WEFTEC”), and the Powergen Renewable Energy Trade Show.

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<sup>1</sup> Please see **Chapter 4D** for more details.