

EXPORT-IMPORT BANK of the UNITED STATES



REPORT TO THE U.S. CONGRESS
ON EXPORT CREDIT COMPETITION AND
THE EXPORT-IMPORT BANK OF THE UNITED STATES

FOR THE PERIOD
JANUARY 1, 2007 THROUGH DECEMBER 31, 2007

JUNE 2008



JAMES H. LAMBRIGHT
CHAIRMAN AND PRESIDENT

EXPORT-IMPORT BANK
OF THE UNITED STATES

June 30, 2008

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:

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 January 1, 2007, through December 31, 2007.

Sincerely,

A handwritten signature in black ink, appearing to read "James H. Lambright", written over a light gray rectangular background.

James H. Lambright
Chairman and President



JAMES H. LAMBRIGHT
CHAIRMAN AND PRESIDENT

EXPORT-IMPORT BANK
OF THE UNITED STATES

June 30, 2008

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 January 1, 2007, through December 31, 2007.

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James H. Lambright
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**THE 2008 ADVISORY COMMITTEE'S STATEMENT ON THE
2007 COMPETITIVENESS REPORT OF
THE EXPORT-IMPORT BANK OF THE UNITED STATES**

Members of the 2008 Advisory Committee have reviewed the 2007 Competitiveness Report to Congress and present here our statement on the competitiveness of the Ex-Im Bank as compared with the other major G-7 export credit agencies (ECAs).

Methodology: With the exception of the committee members representing labor, the Advisory Committee continues to agree with the Report's overall methodology, "report card" approach, and particularly the continued inclusion of an "emerging issues" chapter in the Report. Most committee members believe that the Report has focused on the appropriate and most significant elements upon which a competitive judgment should be based. The committee members representing labor have expressed concern over the Report's negative treatment of policy-related issues, including foreign content, economic impact, local costs, and U.S. shipping requirements, as well as the methodology used to analyze them. They also have expressed concern regarding the Report and the absence of a detailed discussion about the benefits arising from public policies for economic impact, content, and MARAD/Shipping.

With respect to methodology and approach, the Committee has the following observations:

- The new chapter on Ex-Im Bank's support for services is informative and should be updated as new data becomes available. This appears to be an area in which the Bank is performing relatively well. Because services are becoming an increasing focus of U.S. employment, we believe the Bank should explore ways to enhance its support of U.S. services exports. This may be an additional area where the Bank's commitment to small business opportunities could be positively impacted.
- If the trends identified in Chapter 8 continue (dealing with diverging paths of ECAs), the Bank will face a growing challenge when attempting to measure its competitiveness vis-à-vis other ECAs that are beginning to look and act much differently than traditional ECAs. Whether (and/or how) the focus and methodology of this Report might need to change should be investigated.
- With regard to comments from other Executive Branch agencies (see the end of the Executive Summary on pages 2 and 3), the Advisory Committee questions whether the Competitiveness Report should include such comments when the report is designed to specifically examine how competitive Ex-Im Bank financing was in 2007 compared to that provided by other ECAs. Further, the Committee notes that the other Agencies acknowledge, at least in part, that the changing approach to export financing of many other ECAs may have a negative impact on

the Bank's ability to fulfill its current mandate. The Committee believes that there is no doubt that these developments have significantly negative implications for Ex-Im Bank and U.S. exporter competitiveness. Commercializing ECAs have begun to aggressively pursue new areas of business and to compete on elements other than subsidies. In essence, many ECAs are moving on to "second generation" competitive tools, such as liberalizing foreign content, taking on local currency risk, supporting strategic transactions and underwriting riskier borrowers/countries. The likely result of this expanded scope is that U.S. exporters will increasingly face ECA competition in new forms and in "non-traditional" markets and transactions – areas in which Ex-Im Bank faces a number of external and internal obstacles to being competitive.

Findings: With the exception of the committee members representing labor who question the Report's findings with respect to policy-related issues, the other members of the Advisory Committee agree with the Report's overall findings. That is, (1) the Bank's traditional competitive advantage on "core elements" (such as cover policy, interest rates, premia) no longer exists; (2) the Bank's overall competitiveness is adversely affected by the fact that aspects of its major programs, particularly co-financing, foreign currency, and foreign content support, have not adapted to competitive changes; and (3) the Bank's public policy requirements (economic impact, foreign content policy, and U.S. shipping requirements) negatively impact competitiveness on an increasing number of transactions.

The majority of the Committee believes that the following are the most non-competitive aspects of Ex-Im Bank's programs:

- **Foreign content:** For several years, the Competitiveness Report has highlighted the fact that other ECAs have adjusted their content policies to reflect the increasing globalization of supply chains and the sourcing realities in today's marketplace. The Committee believes that all appropriate constituencies - Congress, Policy Agencies, the Bank and representatives of both business and Labor - should examine the realities of whether it is possible to enhance the competitiveness of the Bank's content policy without diminishing its core "made in the U.S." philosophy and while remaining true to, and perhaps enhancing, commitment to job promotion.
- **Risk-taking:** The decline in the Bank's interest in assuming greater risk (given its mission of acting as a lender/insurer of last resort and its requirement of reasonable assurance of repayment) has been noted for several years. This needs to be closely examined to determine if current approaches are the most appropriate or whether the Bank's risk appetite should be recalibrated.
- **Foreign currency financing:** Ex-Im Bank should actively pursue necessary changes in its foreign currency program if it wants to effectively address the local currency financing needs of a growing number of potential buyers of U.S. goods and services.

- U.S. shipping requirements: The Committee views these requirements as incompatible with the competitive realities of today's export environment, particularly those impacting major projects that are critically important to U.S. suppliers, including smaller sub-suppliers involved in these projects.
- Non-OECD ECAs: As noted in the Report, non-OECD ECAs are rapidly becoming serious competitors and yet are not obliged to follow the OECD Arrangement. As explained in the Report, Ex-Im Bank is subject to various legislative and policy constraints which diminish its capacity to enhance the U.S. exporting community's ability to compete on a level playing field. The majority of the Committee believe that rather than accept this diminishment by a failure to act or decide, all constituencies should examine those constraints and make an affirmative decision to either continue those constraints, thereby accepting a decreasing ability to compete, or develop policies, strategies and procedures which enhance Ex-Im's ability to compete effectively within the new paradigm.
- **Ex-Im Bank needs to continually strive for excellence in customer identification, outreach, education and service.** Enhanced service in the realm of case processing mechanisms to ensure effective and timely decisions is particularly important. In this regard, the Committee recommends that Ex-Im Bank undertake a comprehensive review that examines the organizational structure and case processing systems to identify and pursue necessary modifications that maximize and balance customer service with Ex-Im Bank's legal, regulatory and policy requirements.

The Advisory Committee believes that, as explained in Chapter 8 of the Report, other ECAs are in the process of reinventing themselves in order to remain viable and relevant in today's world. We think the Bank's mission itself is clear and should remain unchanged: to support U.S. jobs by correcting market imperfections arising from foreign ECA financing competition and exaggerated perceptions of risk. We also believe that the Bank should not simply imitate what other ECAs (with very different trade and government philosophies) are doing. However, Ex-Im Bank either has to adapt to the new realities of the export finance marketplace, capitalizing on its own unique strengths and capabilities, or its ability to help U.S. exporters compete in the world market will diminish materially.

Summary: The Advisory Committee would like to acknowledge Ex-Im Bank's well-researched, thoughtful and candid assessment of its competitiveness. However, this Report becomes truly useful only if it stimulates appropriate action. Therefore, the Advisory Committee strongly urges Ex-Im Bank to undertake a process which addresses the multiple challenges noted in this comprehensive report in an expedient manner and includes all relevant stakeholders (e.g., Congress, Labor, U.S. exporting community, etc.).

The warning signs are clear: if it is to remain an effective and value-adding player in the export credit arena, Ex-Im Bank can no longer delay in rethinking its programs and policies within the framework of U.S. Government trade and economic policy. As global competition intensifies, the need for a viable and relevant Ex-Im Bank has never been greater.

A handwritten signature in black ink, appearing to read 'Mark C. Treanor', with a long horizontal flourish extending to the right.

Mark C. Treanor
Chairman
2008 Ex-Im Advisory Committee

2007 Competitiveness Report

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Executive Summary

Background

The 2007 Competitiveness Report provides an assessment of the competitiveness of the medium- and long-term export credit programs of the Export-Import Bank of the United States (Ex-Im Bank) during calendar year 2007. This assessment compares Ex-Im Bank programs to those of the G-7 official export credit agencies (ECAs), the traditional competitors to Ex-Im Bank. The report also incorporates competitive information on other large ECAs, when such information is available and relevant. This assessment is based on information gathered from a number of sources, including surveys and focus groups with exporters and lenders; data from the Organization for Economic Cooperation and Development (OECD), the World Bank, the International Monetary Fund (IMF), the World Trade Organization (WTO); and information from various ECAs and their host governments.

Findings

From the early 1980s to the late 1990s, the world in which ECAs existed was fairly stable, requiring relatively minor and infrequent changes to core operating principles and procedures. Moreover, the demarcation between what the private sector was willing and able to finance without ECA support and what ECAs perceived as their domain was distinct and stable.

Beginning in the late 1990s, however, a near-decade of dramatic shifts in many of the practices, competitors, and private sector capacities that affect export finance have led most major ECAs to change many of the tools and approaches they employ. In order to remain relevant and operationally viable, ECAs are increasingly employing a variety of strategies designed to increase their business. At the core, these strategies focus on (a) greater non-domestic content (large allowances for local cost and more liberal foreign content rules); and (b) more commercial endeavors (financing exports into high-income countries, for example). Because these new strategies are so fundamentally different, they have led many of Ex-Im Bank's traditional competitors to redefine their basic economic roles and missions. Rather than being lenders/insurers of last resort (LILRs), most major ECAs are now well on the way to transforming their organizations into quasi-market players (QMPs). In fact, by the end of 2007, Ex-Im Bank was the only remaining major ECA to remain fully in the LILR category.

By 2007, this paradigm shift was materially affecting Ex-Im Bank's competitiveness in three ways.

- As other ECAs become more comfortable in taking on risk (particularly with non-sovereign borrowers) and improve the quality of their guarantees, Ex-Im Bank's traditional competitive advantage on "core

- elements” (basic components of ECA activity, such as cover policy, interest rates, risk premia) has virtually disappeared.
- Perhaps more significantly, these core elements have become less important to overall competitiveness, while other features of ECA support – such as foreign currency financing, co-financing and project finance flexibility – have become more important. While the Bank’s overall competitiveness in these areas remained unchanged from the previous year, several of these areas (foreign content and co-financing) are among the least competitive Ex-Im Bank programs.
 - Of greatest concern to the U.S. exporting community was the fact that Ex-Im Bank’s unique public policy constraints and requirements – economic impact analysis, foreign content policy, local costs policy, and U.S. shipping requirements – were increasingly out of line with practices of other ECAs and becoming a more negative influence when applicable to a transaction. While these policies have been in place for many years, the globalization of supply chains and the agility of other ECAs in adapting to the new competitive reality has highlighted the negative aspects of these policies on Ex-Im Bank’s competitiveness.

The overall competitiveness rating for Ex-Im Bank in 2007 remains at A-/B+, unchanged from 2006. However, Chapters 2A and 8 explain why and how the fundamental ECA competitive calculus is changing and provide perspective on why a competitiveness grade based on an examination of discrete ECA elements and programs may no longer be the only (or best) measure of Ex-Im Bank’s competitive position in the ECA world.

Agency Comments:

“However, it should be noted that most of the Executive Branch agencies believe that changes occurring in the international export finance system represent a significant economic policy success, and that U.S. exporters remain highly competitive. Principal among these successes is the growing dominance of private markets in meeting the financing needs of U.S. exporters. The success of the OECD Arrangement, in concert with WTO dispute settlement reports, in virtually eliminating subsidies from ECA programs should be seen as a major achievement and has been a long-term USG policy objective. With the Arrangement protecting the system against financing subsidies, ECA efforts to provide increasing amounts of financing on pure market terms are good for U.S. exporters as a one-way street to higher ECA pricing and market-based behavior by these competitors. This strengthens Ex-Im Bank’s competitive position in its target developing-country markets. Ex-Im Bank, the Arrangement, and the WTO can efficiently redress any ECA under- pricing of the market that might occur.

A further policy success is that the Arrangement disciplines have been extended to important entities formerly outside the export finance rules.

Brazil now subjects its largest capital goods export – aircraft -- to the new OECD Aircraft Sector Understanding, and Canada’s “market window” financing from its ECA for its aircraft sales have also moved from outside the Arrangement system to inside it. Germany has recently completed restructuring its ECA’s “market window” in response to European Community litigation intended to force market pricing and behavior on its program. Tied aid has been converted from a trade distortion vehicle to a development tool. Ensuring that untied aid is not used as a trade distortion vehicle remains a high USG policy priority, and we closely scrutinize comprehensive ECA transparency reporting in this area. As noted in the report, China’s rapid expansion of export credits and use of concessional financing that could disadvantage U.S. exporters is a significant concern. The OECD is engaging with China on export finance issues and places great emphasis on bringing Chinese lending practices into conformity with IMF and World Bank debt management policies. Both bilateral and multilateral efforts to engage China on the terms and conditions of its financing are intensifying.

These highly positive developments have all occurred while Ex-Im Bank’s program size has remained fairly stable, and U.S. exports continue to grow rapidly using market-sourced financing. USG policy agencies seek to maximize the scope for market financing and to maintain a level playing field for U.S. exporters to compete under rapidly-globalizing market conditions. The agencies reiterate that domestic content rules are determined by individual governments and their ECAs outside the OECD rules, according to their respective national economic objectives. There has been a significant liberalization by some ECAs in response to the globalization of supply chains. The potential impact of this development on Ex-Im Bank’s ability to fulfill its current mandate should be considered by senior policy makers.”

[Statement submitted by the Departments of Treasury and State, and the Office of Management and Budget.]

Figure 1: Definition of Grades

Grade	Definition
A+	Fully competitive compared to other ECAs. Consistently equal to the (or is the sole) ECA offering the most competitive position on this element. Levels the playing field on this element with the most competitive offer from any of the major ECAs.
A	Generally competitive compared to other ECAs. Consistently offers terms on this element equal to the average terms of the typical major ECA. Levels the playing field on this element with the typical offer from the major ECAs.
A-/B+	Level of competitiveness is in between grades A and B.
B	Modestly competitive compared to other ECAs. Consistently offers terms on this element equal to the least competitive of the major ECAs. Does not quite level the playing field on this element with most of the major ECAs.
B-/C+	Level of competitiveness is in between grades B and C.
C	Barely competitive compared to other ECAs. Consistently offers terms on this element that are a notch below 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.
D	Uncompetitive compared to other ECAs. Consistently offers terms on this element that are far below 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.
F	Does not provide program (Note: The Exporter and Lender Survey included a grade of "F" in the event no Ex-Im Bank program was available.)
NA	Does not have experience with policy/program.

Chapter 1: Introduction

Background

Pursuant to its Charter (the Export-Import Bank Act of 1945, as amended), Ex-Im Bank is mandated to provide U.S. 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 2007.

In addition, in late 2006, Ex-Im Bank's Charter was reauthorized by the U.S. Congress and included eight new requirements to be incorporated into the Bank's Annual Competitiveness Report to Congress. Ex-Im Bank addressed four of the new requirements in last year's Report (and continues to include three of them in this year's Report; the Ex-Im Bank Board of Directors chose not to submit a statement): renewable energy, co-financing, and inclusion of activities of key non-OECD export credit agencies (ECAs). In this year's Report, the Services Exports Support is addressed in Chapter 4, Section E.

The three remaining requirements represent efforts that actually fall outside the purview of Ex-Im Bank and, therefore, are not feasible to include. The requirements, along with Ex-Im Bank's comments, are provided below.

- Competitor Program Accounts: Comparison of competitor program accounts and an assessment if these accounts are being used in the best interest of U.S. taxpayers.

Comment: The information that such a comparison would require is considered confidential by ECAs and is not available for evaluation.

- Non-conformance with OECD Arrangement: Detailed information on cases reported to the Bank that appear to not conform to the OECD Arrangement or exploit loopholes in the Arrangement for the purpose of gaining a competitive advantage. The President of Ex-Im Bank, in consultation with the Secretary of Treasury, may provide this information to the appropriate Congressional Committees in a separate and confidential report instead of including this information in the annual Competitiveness Report.

Comment: To the extent that Ex-Im Bank identifies any such cases, it can establish a consultation procedure with the Treasury Department and provide this information in a separate and confidential report to the appropriate Congressional Committees. In 2007, no such cases were identified.

- ECA Activities Not Consistent with the World Trade Organization (WTO) Agreement on Subsidies and Countervailing Measures (ASCM): A description of the activities of foreign ECAs and other entities sponsored by a foreign government, particularly those not members of the OECD Arrangement, that appear not to comply with the Arrangement and appear to be inconsistent with the terms of the ASCM. In addition, a description of actions taken by the U.S. Government to address these activities. A confidential report, with consultation with the Secretary of Treasury, instead of including in the Competitiveness Report is an option.

Comment: The scope of the requirement is sufficiently broad that a determination of potential WTO ASCM and/or OECD violations far exceeds the expertise of Ex-Im Bank. Instead, responsibility for the identification of potential violations would most appropriately reside with the Office of the United States Trade Representative. However, to the extent Ex-Im Bank should become aware of possible violations, the Bank can provide a report to the appropriate Congressional Committees.

Scope of Report

This report compares Ex-Im Bank's competitiveness with that of the other G-7 ECAs, 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. Quantitative comparisons and information on each of the G-7 ECAs can be found in Chapter 2 and Appendix D.¹

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, the 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 G-7 ECA counterparts. (See below for information on the survey.) 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.

¹ All dollar volume data contained in the Report is in non-inflation-adjusted U.S. dollars.

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 information provided by the survey of the U.S. 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 can 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.

Other Comments

Comments were received from U.S. government agencies that appear at the end of the Executive Summary.

Report Structure

This year's report follows the same structure used in last year's Report. 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 2007 and the philosophies and missions of competing G-7 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 U.S. 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 U.S. economic philosophy and public policies.

Chapter 8 deals with emerging issues and this year examines the competitive implications arising from diverging ECA philosophies and practices.

The appendices following the body of the Report include a 2007 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 an overview of the world in which official export credit agencies (ECAs) operate. Beginning with the influences, trends and developments in this highly dynamic environment, this chapter describes how these factors have affected ECAs' strategies in the recent past and are likely to continue going forward.

From the early 1980's up until the late 1990's, the ECA landscape was relatively stable with minor shifts in philosophies and operations influenced largely by a common understanding that official ECAs' roles were limited to filling market gaps that the private sector would or could not fill, and that market forces, not government supported financing, were the basis for buyer purchase decisions. Moreover, the global trading system was characterized by competition among well-known trading partners and a set of generally accepted international protocols designed to ensure a level playing field.

However, the late 1990s began almost a decade of dramatic shifts in many of the practices, competitors and private sector capacities that impact export finance. These new circumstances, which continue to intensify, have motivated most ECAs to modify the tools and approaches they employ. These changes, in turn, have resulted in some fundamental shifts in these ECAs' basic economic role and mission. The section below broadly summarizes these developments, while Chapter 8 provides more discussion of these changes and shifts.

Evolving Export Finance World

The export finance world continues to evolve in a highly dynamic manner, as both the sources and forms of export finance expand and change. Perhaps the most important shift in export funding sources in recent years has been the growth and ongoing strengthening of banking and capital markets in key emerging markets.

The availability of local financing means that emerging market borrowers, especially the larger ones, are able to obtain financing for their imports through domestic finance sources and often in local currency (which is sought by borrowers whose revenue is primarily earned in local currency). This demand for financing in local currency (rather than in U.S. dollars or major European currencies) by emerging market borrowers has changed the way export finance is structured and has led many ECAs and other lenders to develop programs to offer such financing (sometimes taking on the exchange risk, as well). Given the increasing financial influence of the Euro zone, the popularity of Euro financing has also increased.

Capital markets in the developed world continue to employ new tools and techniques, allowing private lenders and investors to take on more risks and offer longer terms than in the past. In order to meet the financing needs of large projects, the private

market has developed complex and integrated solutions that combine a variety of financing and risk mitigation tools (such as credit default swaps). These developments have allowed private lenders and investors to play a much larger role in export-related financing than in the past. Further, the emergence of large non-OECD ECAs (such as those in China and Brazil) and the entrance of multilateral development banks into the export finance arena have increased total export finance resources.

In addition to changes in sources and forms of export finance, ECAs are facing more formal and informal oversight from an ever broader body of interested parties. Recent additions include attention to corporate social responsibility issues (from NGOs) and sustainable lending (from the IMF and World Bank). The most important “regulatory guidance” may be the WTO’s case rulings that have contributed to a relatively greater focus by many OECD ECAs on financial performance goals (such as long-term breakeven) and relatively less focus on export-related economic benefits arising from their activities.

As a result of the evolution in the export finance arena, traditional business at most developed-country ECAs has stagnated or declined. In order to remain relevant and operationally viable, ECAs are increasingly employing strategies to increase their business. At the core, these strategies focus on either greater non-domestic content (larger allowances for local cost and more liberal foreign content rules) or on more commercial endeavors (financing exports into high-income countries).

Export Trends

Figure 2 shows the global exports of goods over the last 4 years, with worldwide trade increasing by an average of 13% per year. Further, the data illustrate the consistently significant role that capital goods exports play in the total export picture, accounting for about 30% of total world exports. OECD countries have historically accounted for the bulk of exports: 63% of goods exports and 66% of capital goods exports in 2006. However, the 5 countries nicknamed the BRICS (Brazil, Russia, India, China and South Africa) have been steadily increasing their share of both total and capital goods exports. While not yet a major presence across multiple sectors and regions, recent trends suggest the BRICS *will* be in that category within the decade.

Figure 2: World Exports of Goods and Capital Goods, 2004-2007 (\$Bn)

	2004	2005	2006	2007*
Exports of Goods				
World	\$9,113	\$10,407	\$12,028	\$13,278
OECD	6,180	6,756	7,632	8,700
BRICS	996	1,272	1,596	1,800
Rest of World	1,937	2,379	2,800	2,778
Exports of Capital Goods (excluding automobiles)				
World	\$2,736	\$3,032	\$3,488	N/A
OECD	1,960	2,050	2,303	N/A
BRICS	293	374	479	N/A
Rest of World	483	608	706	N/A
OECD Exports as % of World Exports				
Goods	68%	65%	63%	66%
Capital Goods	72%	68%	66%	
BRICS Exports as % of World Exports				
Goods	11%	12%	13%	14%
Capital Goods	11%	12%	14%	

Sources: IMF's International Financial Statistics 2007; OECD; International Trade Centre's Trade Competitiveness Map.

* Preliminary

Export Finance Trends

As shown in **Figure 3**, G-7 medium- and long-term government¹ export credit volumes grew by 50% between the nadir (2002) and what may prove to be the apex (2007) of the current export finance cycle. However, looking only at the average growth rate for these countries disguises two very different trends during that time. Four countries (Canada, France, Germany and Italy) experienced roughly a doubling in their government export credit volumes (with Italy increasing by over 400%). In contrast, three countries (U.S, U.K., and Japan) had government export credit volumes that stagnated or declined (Japan). Moreover, the large volume increases (of

¹ Reflecting the trend toward commercialization within the G-7/OECD ECA community (discussed in detail in Chapter 8), the data in this table are intended to capture the maximum level of government-supported medium- and long-term export financing from each country. The numbers, which were compiled from a variety of sources often requiring extrapolation or averaging, are rounded to the nearest half billion US\$ to highlight their indicative nature.

\$8-9 billion each) took place in the two countries that are the most outspoken advocates for commercializing ECAs (Canada and Italy).

At least through 2006, Brazil, China and India experienced medium- and long-term government export credit growth rates similar to those of the four G-7 high-growth countries noted above. As a result, government export credit activity in these three countries has increased from one-fourth of the total G-7 level in 2002 to almost two-thirds of that level by 2006.

Figure 3: New Medium- and Long-Term Official Export Credit Volumes (\$Bn)

	2002	2005	2006	2007*
Canada	10.0	12.0	15.5	18.5
France	6.5	10.5	9.0	14.0
Germany	6.0	12.0	14.0	10.0
Italy	2.5	8.0	8.0	11.0
Japan	6.0	9.0	6.0	2.0
U.K.	2.5	2.0	3.0	3.5
U.S.	8.0	9.0	8.5	8.0
Total G-7	\$ 41.5	\$ 62.5	\$ 64.0	\$ 67.0
U.S. % of G-7	19%	14 %	13 %	12 %
Brazil	4.0	3.5	7.5	N/A
China	5.5	18.5	29.0	N/A
India	1.0	3.5	4.0	N/A
Total B,C,I	\$ 10.5	\$ 25.5	\$ 40.5	N/A
B,C,I % of G-7	25 %	41 %	63 %	

* Estimate

According to **Figure 4**, external capital flows into emerging markets grew by over 50% during 2007 and continued to play a dominant role in the export finance environment for official ECAs. Overall, private capital flows registered at nearly \$800 billion, over six times more than just five years earlier. Greater global liquidity, lower interest rates, strong growth, restorative policy adjustments in troubled economies, and increased financial integration continued to encourage private investors and lenders to actively support emerging markets in 2007. Although the U.S.-centered “credit crunch” associated with the sub-prime mortgage crisis is expected to adversely impact credit flows, the forecast level of funding in 2008 (over \$700 billion) suggests that private sector funding will continue to constrain the level and demand for official ECA lending for the foreseeable future.

Figure 4: Net External Capital Flows into Emerging Markets, 2002-2007 (\$Bn)

	2002	2003	2004	2005	2006	2007*
Official Flows						
IFIs	\$7	-\$6	-\$15	-\$39	-\$32	\$3
Bilateral Creditors	-13	-14	-2	-26	-32	-3
Private Flows						
Equity Investment	117	135	195	252	221	299
Commercial Banks	-8	27	61	146	212	266
Non-banks	16	67	93	122	136	217
Total	\$119	\$ 209	\$ 332	\$ 455	\$ 505	\$782

Source: Institute of International Finance, "Capital Flows to Emerging Market Economies," March 2008.

*Estimate.

Trends Identified in Focus Group Discussions

Exporters and lenders noted that some other ECAs (and/or their host governments) are now adopting the "China" approach, in which financial support is based on the strategic importance of a particular borrower, domestic business sector, commodity produced by a borrower, or any other broadly defined "national interest." This has resulted in aggressive and flexible government-backed support with which U.S. exporters cannot compete.

All focus group participants were quite clear that the changing philosophies and operating practices of OECD ECAs were having an increasingly detrimental impact on Ex-Im Bank's ability to compete. As globalization and vibrant private finance market capabilities continued to dominate the thinking of every other ECA, Ex-Im Bank's philosophical underpinnings, operational approaches, and Congressional mandates in 2007 became ever more of a drag on the Bank's competitiveness (in the view of the exporting community). Several participants noted that, even as late as 2006, Ex-Im Bank continued to have at least partial "philosophical and operational allies" with a few European ECAs. However, by 2007, even those allies were adopting very commercialized, flexible approaches to the official export finance aspects that most affect competitiveness in today's world: foreign content support, local costs support, and **no** government policy mandates such as economic impact analysis. Repeating a trend first noted in 2006, a significant number of participants also saw Ex-Im Bank's competitiveness in risk-taking (particularly with private-buyer risk) continue to decline in 2007 when compared to that of other OECD ECAs.

Both groups stated that private capital and lending markets in 2007 continued to be innovative and highly capable of taking on the bulk of the financing needed for large projects and export sales. The credit market turmoil experienced in the latter part of the year had some relatively modest dampening effect on some lenders' exuberance for large, complex transactions; but the main impact seemed to be a slight tightening

in liquidity and increase in funding costs (which still left the private sector in a competitive overall pricing position compared to OECD ECAs). Further, emerging countries' capital and banking markets continued to be quite robust, given these countries' strong economic conditions and high liquidity.

Summary

Ex-Im Bank and the other OECD ECAs are facing a world in which – despite rapid growth in exports – traditional ECAs are being forced to find relevance in the midst of rapidly expanding and changing official competition and a massive influx of private capital to emerging markets. This expanding, evolving ECA world is leading many other ECAs to respond with major new policies and even to rethink their basic mission. The bulk of this Report compares Ex-Im Bank's competitiveness to that of other G-7 ECAs, many of which are reinventing their organizations in light of the new export finance world in which they must operate. This comparison is becoming less instructive, however, as the philosophical and mission fundamentals of G-7 ECAs become ever more disparate.

Chapter 2: Competitiveness Framework

Section B: ECAs' Mission and Place in Government

The Role of Export Credit Agencies

The traditional purpose of an ECA has been to finance domestic exports, although different strategies may be employed to accomplish this goal. In choosing their strategies, G-7 ECAs generally work within two frameworks. The first framework is the OECD Arrangement, which sets the most favorable financing terms and conditions that may be offered for official export credit support. Within the Arrangement parameters, individual ECAs have latitude to pursue their own national policies in support of their country's exports. The second framework is more ECA-specific: the ECA's mission as defined by its sponsoring government. This framework will determine the extent to which an ECA is able to adapt to a changing landscape and what methods it is allowed to employ to continue to work toward its central goal. Together, these two frameworks ultimately define the parameters within which ECAs will compete with each other in promoting their respective governments' national interests.

Ex-Im Bank's Mission and Place in Government

Ex-Im Bank is the official U.S. Government ECA. Ex-Im Bank's mission and governing mandates are codified in its Congressionally approved Charter (Export-Import Bank Act of 1945, as amended). Ex-Im Bank's core mission is to support U.S. exports and the related jobs 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 public policy goal of the Bank's core mission is to enable 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 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 U.S. economy; or
- does not meet various statutory and executive branch parameters.

All these directives aim to achieve a public policy goal and reflect the interests of Ex-Im Bank stakeholders, such as NGOs, other U.S. government agencies, labor, and financial intermediaries. Hence, Ex-Im Bank is required to strike a fine balance among multiple, sometimes competing, goals and objectives. At the same time, Ex-Im Bank is expected to provide the U.S. exporting community with financing that is competitive with officially supported offers made by foreign government counterparts – institutions that most often have fewer public policy constraints to evaluate when deciding whether to provide financing support. Given the G-7 ECAs' widely varying missions and operating modes, the formula with which to compare Ex-Im Bank's competitiveness against these ECA counterparts requires a more comprehensive review that goes beyond the standard comparison of traditional programs and policies. It also requires a review of innovative programs, new guiding principles, and the emerging BRICS (Brazil, Russia, India, China, and South Africa) ECAs.

Chapter 3: Core Business Policies and Practices

Section A: Cover Policy and Risk-Taking

Introduction

One traditional measure of official ECA competitiveness is whether or not export credit support is available in any given market. This is evidenced by the extent of ECA “openness” in a particular country, in terms of both breadth of buyer types and depth of risk appetite. Thus, an ECA’s competitiveness may be measured by the number of countries in which it is open for business and its willingness to take on new business with entities other than sovereign governments or first-class private institutions.

Ex-Im Bank’s Policy and Practice

Historically, Ex-Im Bank has been one of the top 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, the one factor that has had a consistently negative impact on Ex-Im Bank’s traditionally high level of competitiveness in this area – the existence of economic sanctions leveled against countries that might otherwise be creditworthy – has been diminished. Over the past 6 years, the number of countries in which U.S. exporters could not receive Ex-Im Bank support because of U.S. legislative restrictions has declined from 12 in 2001 to 8¹ in 2007.

On the other hand, Ex-Im Bank’s pre-eminence in two other important aspects of risk-taking has dissipated as non-sovereign entities have become the “typical” borrowers and as other ECAS have become comfortable with non-sovereign risk across a wide spectrum of countries. It appears² that over the past few years, Ex-Im Bank has seen its status on the issue of breadth of sovereign risk-taking migrate from “equal to the best” to “equal to the average.” First, as shown in **Figure 5**, only ECGD (U.K.) authorized transactions in fewer countries than did Ex-Im Bank in 2007. (In 2002, Ex-Im Bank was “open without restriction” in more countries than any other G-7.) Second, exporter/banker survey and focus group information, along with anecdotal ECA information, indicate that other ECAs (especially those in Europe) are rapidly enhancing their underwriting comfort with small and medium-sized non-sovereign borrowers. Hence, on the issue of depth of risk-taking, it appears that other ECAS have caught up with Ex-Im Bank.

¹ In 2007, Ex-Im Bank had legislative restrictions to providing support to the following countries: Burma, Cambodia, Cuba, Iran, North Korea, Laos, Sudan and Syria.

² Reflecting fundamental changes in data availability, the methodology used to evaluate “breadth” of country risk-taking has moved through three iterations over the last 5 years. As none of the data sources is available for all 5 years, it is not possible to make comparisons based on cover policy; rather, countries in which transactions occurred must be used as a proxy. Thus, the data cited here is more indicative of overall trends rather than a precise measure of risk-taking.

G-7 ECAs' Policies and Practices

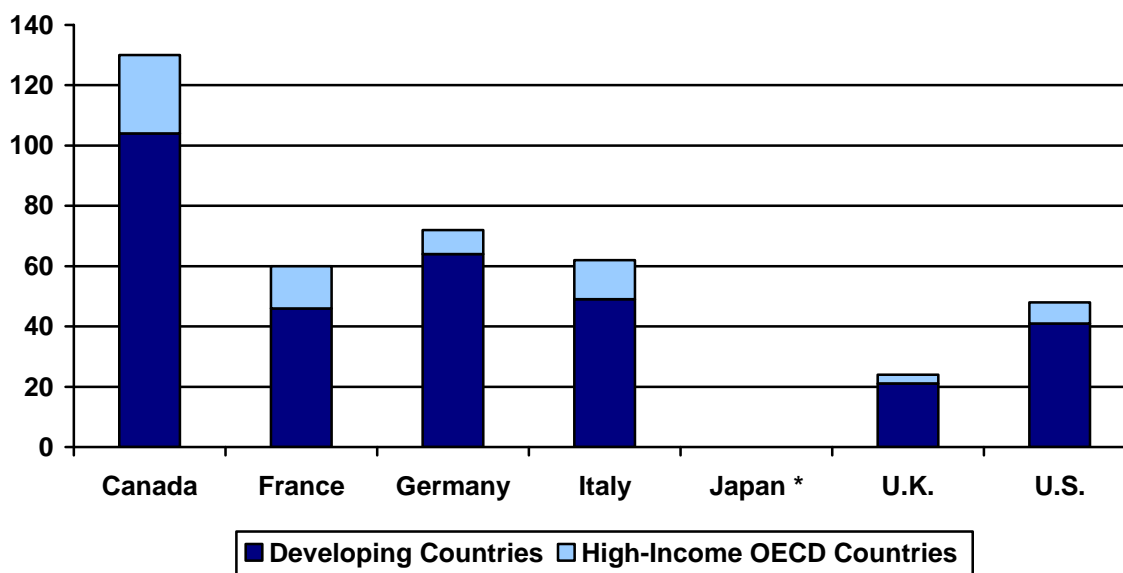
With the exception of the U.K., all of Ex-Im Bank's G-7 ECA counterparts now take risks across a broad spectrum of countries. As shown in **Figure 5**, Canada supported medium- and long-term transactions in 130 countries (and 104 developing countries) in 2007, while Ex-Im Bank was active in 48 countries (41 developing countries). On the other hand, removing European countries from the population of borrower countries puts Ex-Im Bank on a par with France, Germany, and Italy (all supported transactions in about 40 non-European countries).

Unlike the situation in the U.S., it is rare for other G-7 governments to impose sanctions on export credit business. As a result, Iran has been a leading market for G-7 ECAs in recent years. In 2007, however, other G-7 ECAs dramatically reduced their activity in Iran as part of the U.N. nuclear disarmament dispute.

Two trends that are evident based more on anecdotal than aggregate data are:

- the increase in G-7 ECA support for transactions in high-income OECD countries, and
- the continued rapid pace at which the G-7 ECAs are taking on private sector risk transactions.

Figure 5: Number of Countries In Which G-7 ECAs Supported Medium- and Long-Term Transactions, 2007



* Comparable data unavailable.

Export and Lender Survey Results

Exporters and lenders were very concerned that Ex-Im Bank seemed to noticeably tighten its credit standards in 2007 to the point that “the Bank’s standards for taking on private buyer risk are like a commercial bank’s standards, rather than an official ECA’s standards.” At the same time, respondents saw evidence that other ECAs have increased their willingness to support private buyer transactions, even with smaller, less-well-known buyers. Exporters and lenders also noted that Ex-Im Bank is often slower to re-open in transitional markets or imposes more risk-mitigating conditions when it re-opens than do other ECAs.

Conclusion

For a decade after the various debt/liquidity crises of the late 1990’s (e.g., Asia, Russia, Argentina), the ECA world experienced a steady transformation of its customer core from largely sovereign to largely non-sovereign borrowers. Ex-Im Bank’s institutional avoidance of country/borrower limits and its historically extensive involvement with private borrowers allowed the Bank to be more quickly comfortable with a larger variety of borrowers. By 2007, however, it appeared that other ECAs have attained similar (and in some areas, greater) comfort with a variety of borrowers. While Ex-Im Bank may still be among the leaders in its depth of risk-taking (dealing with smaller, less financially documented borrowers), the Bank is in the “middle of the pack” in its breadth of risk-taking.

In 2007, Ex-Im Bank’s status appeared to have slightly deteriorated but not quite enough to justify a downgrade from last year’s grade of a weak “A”.

Chapter 3: Core Business Policies and Practices

Section B: Interest Rates

Introduction

The use, or misuse, of official interest rates as a competitive tool was the impetus for the OECD countries to negotiate the Arrangement on Guidelines for Officially Supported Export Credits in 1978. Establishing minimum interest rates, therefore, was the first topic taken up by the OECD Participants. Over time, the minimum official interest rate has become more market-oriented and less of a competitive threat. Nonetheless, interest rates can still be a competitive factor when ECA support is involved, because the quality of an ECA's guarantee or insurance can affect the interest rate offered by a private lender.

ECAs may support interest rates in two ways: either by lending directly to a borrower and charging the official minimum interest rate for the currency of the loan¹, or 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 even if the minimum official interest rate is lower than the lender's cost of funds.

As an alternative to providing interest rate support, many ECAs offer "pure cover" support. ECAs that support pure cover provide a repayment guarantee or insurance to a lender willing to lend to a foreign borrower. The repayment guarantee/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 and attempt collections from the foreign borrower.

Over the past decade, pure cover support has become the dominant form of ECA support for export credits, with interest rate support (in the form of either direct lending or IMU) steadily declining. Pure cover now accounts for over 80% of G-7 ECAs' medium- and long-term activity. This is largely due to the fact that private capital markets are increasingly able to provide large amounts of longer-term financing at attractive interest rates and need only risk protection in the form of ECA cover.

Ex-Im Bank's Policy and Practice

Ex-Im Bank's charter mandates that Ex-Im Bank make available a direct loan program with a fixed interest rate to borrowers under the medium- and long-term programs. 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. The key difference that borrowers

¹ 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.

see between the direct loan and an Ex-Im Bank guaranteed loan offered by a commercial bank is the interest rate. Under Ex-Im Bank's direct loan, the interest rate is fixed at the time of authorization at the then-current OECD minimum official interest rate (CIRR) for the U.S. dollar. Under Ex-Im Bank's pure cover program, the interest rate is established by the lender. It may be fixed at the time of commitment, fixed at some point during the disbursement and repayment periods, or remain floating for the life of the loan. It may be based on LIBOR, the U.S. prime rate, a commercial paper rate, or any other relevant interest rate benchmark.

Ex-Im Bank allows the foreign borrower or the borrower's agent – a commercial bank – to determine what kind of support to obtain. In the past, borrowers have used Ex-Im Bank's direct loan program during periods of rising interest rates and predominantly the pure cover program at all other times. Although the U.S. is in a period of slowly rising interest rates, the demand for direct loans from Ex-Im Bank has been exceedingly limited. In 2007, Ex-Im Bank approved no direct loans (and approved only one in 2006).

Ex-Im Bank provided medium- and long-term pure cover support in 2007 for 392 transactions with a total financed amount of more than \$7.9 billion. Consistent with previous years, the interest rates on the longer term, larger transactions were generally competitive. Specifically, the interest rates achieved on Project Finance transactions have historically been slightly better than those achieved with the insurance support provided by the other G-7 ECAs. However, as more ECAs gravitate to "enhanced insurance" or guarantee-like cover for larger deals, Ex-Im Bank's historic advantage in this arena is shrinking. The interest rates on large aircraft transactions are comparable to those achieved with the support of the Airbus ECAs, as they have improved their support for large aircraft transactions in order to achieve competitiveness with Ex-Im Bank. Other Ex-Im Bank long-term transactions are also carrying interest rates comparable to those achieved with the other G-7 ECAs.

Interestingly, medium-term transactions supported under the Bank's insurance and guarantee programs do **not** typically achieve attractive rates: the average spread over LIBOR for medium-term transactions supported in 2007 was roughly 250 basis points. At such levels, the spreads on Ex-Im Bank's medium-term transactions are generally equal to the bottom tier of G-7 ECAs. (The difference in interest rates between long-term, large transactions and medium-term, smaller transactions appears to be the result of banks' pricing strategies rather than a function of any Ex-Im Bank support element.)

G-7 ECAs' Policies and Practices

Each of the G-7 ECAs offers both interest rate support, either with a direct loan or with IMU, and pure cover support. Canada, Germany, Japan and the U.S. all offer a direct loan program. France, Italy and the U.K. offer IMU support, though the terms of the IMU support differs. Nonetheless, continuing the trend identified over the past 3 years, preliminary information indicates that interest rate support continued to decline as a percentage of total ECA support in 2007.

Like Ex-Im Bank, the other G-7 ECAs are providing 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. The pricing implications of these differences in cover are reflected in the minimum exposure fees that ECAs charge. (See Chapter 3C for more information on how these differences are reflected in the fees.) The reason for these price differences is to ensure that the “all-in-cost” of a transaction is the same across ECAs. Thus, the interest rate on a transaction supported by an ECA providing “above standard” cover typically is lower, and the exposure fee is higher. Conversely, the interest rate on transactions supported by an ECA providing “below standard” cover is typically higher, and the exposure fee is lower. In 2007, anecdotal evidence indicated that the interest rates achieved under the other G-7 ECAs’ pure cover support ranged from very low (e.g., LIBOR plus 5-10 basis points) to quite high (e.g., LIBOR plus 300-400 basis points), irrespective of the type of pure cover support provided.

Exporter and Lender Survey Results

None of the survey respondents used the direct loan program in 2007. Instead, the exporting community used Ex-Im Bank’s insurance and/or guarantee products, which resulted in interest rates that were generally competitive with those of other G-7 ECA-supported transactions. Very few comments were received from exporters or lenders with respect to Ex-Im Bank’s interest rate competitiveness, given that this element has largely been neutralized as a competitive factor.

Conclusion

Ex-Im Bank consistently offers interest rates that are at least the equal of the average rates of the typical major ECA. Through the direct loan program, Ex-Im Bank provides interest rate support that is competitive with the other G-7 ECAs. Further, the interest rates generated under Ex-Im Bank’s pure cover program remain competitive with those of other G-7 ECAs, although the Bank’s competitiveness in this area is being neutralized as other ECAs improve the quality of their pure cover guarantee. In 2007, Ex-Im Bank remained generally competitive with the other G-7 ECAs on this element (a grade of A).

Chapter 3: Core Business Policies and Practices

Section C: Risk Premia

Introduction

ECAs charge risk premia, also known as exposure fees, to compensate for the risk of loan non-repayment. In 1999, the OECD adopted the Knaepen Package which defined the elements for determining sovereign buyer fees and set Minimum Premium Rates (MPR) for sovereign buyer transactions. The MPR was developed as a tool to level the playing field among ECAs by setting a floor for pricing of standard export credits to sovereign buyers. These rates also serve as the floor for fees in non-sovereign buyer transactions.

The MPR is determined by several factors: (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. Allowing for surcharges or discounts based on the type of product ensures a level playing field among ECAs. Within the OECD, these surcharges and discounts are known as “related conditions surcharges.” 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 may charge, each ECA may add other surcharges to the MPR according to its individual risk assessment process.

Ex-Im Bank’s Policy and Practice

For sovereign transactions, Ex-Im Bank charges the MPR as set by the OECD. For non-sovereign transactions, Ex-Im Bank uses a rating methodology similar to the one used by credit rating agencies to arrive at a particular rating for each borrower. If the borrower is rated equal to or better than the sovereign, then the applicable fee is the MPR. If the borrower is rated worse than the sovereign, an incremental surcharge is added to the MPR.

G-7 ECAs’ Policies and Practices

The G-7 ECAs generally charge the MPR for sovereign transactions. However, fairly significant differences exist for non-sovereign transactions in the risk-rating methodologies, use of mitigants, and pricing mechanisms used by the G-7 ECAs; this leads to a divergence in the fees charged for this borrower class. Many

of these differences stem from different underwriting processes, as well as different claims experience, resulting in different ratings and pricing for the same borrower. Ex-Im Bank is typically on the low end of exposure fees charged to borrowers.

The formal OECD discussions on a common approach to non-sovereign risk evaluation and fees paused in 2007 to allow OECD Participants to consider where consensus may be achieved, given their widely diverse systems, experience and missions.

Exporter and Lender Survey Results

The exporting community views Ex-Im Bank's exposure fees for sovereign and non-sovereign risks as generally competitive and similar to those of other ECAs. (The major concern expressed was about higher "all-in" pricing on Ex-Im Bank transactions, because the Bank charges loan/guarantee commitment fees which are not charged by other ECAs.)

Conclusion

The 1999 Knaepen package gave all OECD members access to a level playing field on premia. However, because of ECAs' disparate financial objectives, some ECAs treat the minimum premium more as a reference point (to which significant surcharges are applied for any type of non-sovereign risk) than as a benchmark. 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-break-even portfolio. As a consequence, in 2007, Ex-Im Bank premium rates were fully competitive with those of G-7 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 an A (generally competitive), 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 6** illustrates how Ex-Im Bank fared competitively on sub-elements of each policy/practice, in addition to an aggregate grade for each. Of particular note is that no sub-element received less than an A-/B+. The grades are derived from both the survey results and the Bank's analysis of how it performs in comparison to its G-7 counterparts.

Figure 6: Grading of Ex-Im Bank's Core Competitiveness, 2007

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

Chapter 4: Major Program Structures

Section A: Large Aircraft

Introduction

In addition to its standard support of U.S. export sales of capital equipment, Ex-Im Bank has several special financing programs that focus on a particular industry or financing technique. This section discusses the program structure of Ex-Im Bank's support for the export sales of large commercial aircraft.

OECD Aircraft Sector Understanding

Since 1985, ECA financings of large aircraft 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 began on a new, updated Aircraft Sector Understanding (ASU) with an expanded list of participants. The purpose of the negotiations was to bring the agreement up-to-date with aircraft financing practices used in the 21st century and to include new aircraft ECAs in the discussion and implementation of aircraft financing disciplines. In July 2007, negotiations concluded and a new agreement was signed. In addition to the Participants to the Arrangement, the agreement was also signed by BNDES and SBCE of Brazil.

The ASU has several new notable characteristics that are briefly summarized below.

Classifies civilian aircraft into three types: (1) Essentially, all Boeing and Airbus aircraft are termed by the ASU as Category 1 aircraft; (2) aircraft from Bombardier (Canada) and Embraer (Brazil) are considered to be Category 2 aircraft; and (3) smaller manufacturers are considered to be Category 3 aircraft.

Risk Classifies Obligors: Under the new ASU, each obligor is assigned a risk classification. This risk classification, or rating, is 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.

Although the ASU became effective in July 2007, any Category 1 aircraft under a firm contract that was concluded by April 30, 2007 and scheduled for delivery by December 31, 2010 is grandfathered under the terms of the old LASU. As such, no new large aircraft financed are expected to be financed under the terms of the ASU until 2011.

Correspondingly, any competitive implications of the new ASU may not show up until orders for 2011 and beyond come into play (not expected for a year or two).

Large Aircraft Industry in 2007

2007 was a record year in orders for the large aircraft manufacturers, with a total of 2,754 new aircraft orders placed. Boeing recorded 1,413 net commercial airplane orders during 2007, reaching more than 1,000 orders for an unprecedented third consecutive year, and setting a Boeing record for total orders in a single year. Airbus also had a record year with 1,341 orders for the year. As illustrated in **Figure 7** below, Boeing surpassed Airbus in total orders for the second straight year.

Figure 7: Number of Large Commercial Jet Aircraft Orders

	2003	2004	2005	2006	2007
Boeing	250	277	1002	1044	1413
Airbus	284	366	1055	824	1341

Deliveries to foreign buyers continued to represent the majority of deliveries in 2007. As noted in **Figure 8**, 65% of Boeing's deliveries were to foreign buyers and **Figure 9** shows that 22% of all of Boeing's deliveries were financed by Ex-Im Bank.

Figure 8: Number of Boeing Commercial Jet Aircraft Deliveries

	2003	2004	2005	2006	2007
Domestic	127	142	135	167	154
Foreign	154	143	155	221	287
Foreign as % of Total	55%	50%	53%	57%	65%

Ex-Im Bank's Policy and Practice

Like the Arrangement terms that apply to standard export credit financing, the ASU (and the LASU before it) sets out maximum repayment terms and minimum interest rates. Ex-Im Bank is fully competitive within these parameters; in particular, Ex-Im Bank's support generates tightly priced interest rates due to the 100% principal and interest guarantee.

Additionally, Ex-Im Bank offers co-financing support for U.S. aircraft sales that include a large percentage of foreign content, such as British engines on Boeing 777s or Japanese airframe components on Boeing 777s and 787s; foreign currency support for airlines that earn a significant portion of their revenues in a hard currency other than U.S. dollars; and a discount on the exposure fee for airlines in countries that have ratified the Cape Town Convention (CTC)¹ and made the necessary declarations.

¹ 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 2007: Afghanistan, Angola, Cape Verde, Ethiopia, Indonesia, Kenya, Malaysia, Mongolia, Oman, Pakistan, Panama, Senegal and South Africa.

However, Ex-Im Bank's support for large aircraft export financing can generate higher all-in costs due to its generally more stringent structuring requirements and/or its higher documentation burden connected to the Bank's public policy objectives, such as U.S. content requirements.

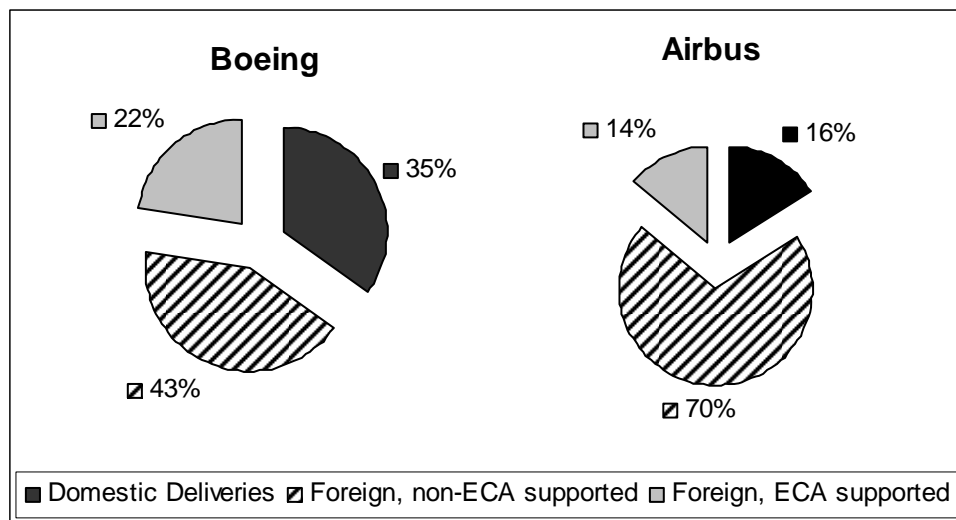
In 2007, Ex-Im Bank approved 26 large aircraft transactions worth nearly \$4.3 billion and covering 99 aircraft. Of those 26 transactions, 9 were co-financing transactions with Japan, Korea or the U.K. and 6 were financed in a foreign currency (the Euro, Canadian Dollar and Korean Won).

The year 2007 also saw a continuation of Ex-Im Bank's policy of giving a one-third discount to the exposure fee charged an airline if the country in which the airline is based had ratified the CTC and made the necessary qualifying declarations. However, although the new ASU provides for a CTC discount, the discount is no longer one-third of the exposure fee but rather 5% to 20%. The Boeing aircraft purchases by Kenya Airways (Kenya), TAAG (Angola), and PIA (Pakistan) in 2007 each received the benefit of the Cape Town discount.

G-7 ECAs' Policies and Practices

In 2007, the Airbus ECAs supported an estimated 70 Airbus aircraft for a total of approximately \$2.9 billion. As illustrated in **Figure 9**, the Airbus ECA-supported aircraft represented about 14% of all Airbus deliveries in 2007, as compared to Ex-Im Bank's support of 22% of all Boeing deliveries in 2007. As a much higher proportion of Airbus deliveries are foreign (84% as compared to Boeing's 65%), the share of Airbus ECAs support of Airbus foreign deliveries is lower (17%) than Ex-Im Bank's share of Boeing's foreign deliveries (34%).

Figure 9: Percentage of Large Commercial Jet Aircraft Deliveries Financed by ECAs, 2007



Like Ex-Im Bank, the Airbus ECAs offer the maximum allowable terms under the ASU. By virtue of their joint financing of Airbus sales, they also provide co-financing support and are generally considered to be less restrictive in terms of structuring and documentation requirements. However, in 2007, the only currencies they supported were the Euro and the U.S. dollar and they did not offer any discount to airlines based in countries that have ratified the CTC.

Exporter and Lender Survey Results

Overall, exporters and banks involved in large aircraft exports found Ex-Im Bank generally competitive compared to the other ECAs. However, some respondents indicated that new ASU may disadvantage Boeing in the future.

Conclusion

Within the context of the terms allowed under the new ASU, Ex-Im Bank is able to provide financing terms that are equal to the average and/or best terms provided by the Airbus ECAs. Additionally, the overall package provided by Ex-Im Bank in terms of special features and non-financial factors also results in a level playing field, especially when assessing the overall availability and attractiveness of support. In total, 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) refers to the financing of projects whose creditworthiness depends on the project's cash flow for repayment. Under this structure, the lender has recourse only to the assets and revenue generated by the borrower (i.e., the project being financed) and cannot access the assets or revenue of the project sponsor to repay the debt. This structure normally covers very large, long-term infrastructure and industrial projects.

In 2007, total PF debt issuances set a new record for the second year in a row, increasing to \$226 billion, up from \$199 billion in 2006. However, the total number of OECD project finance deals notified in 2007 (as required by the OECD Agreement for PF support that incorporates certain modifications to the standard repayment structure) decreased from 15 in 2006 to only 5 in 2007. Preliminary information indicates that contract amounts in 2007 totaled approximately \$3.2 billion (compared to \$3.0 billion in 2006).¹

Figure 10 shows the involvement of ECAs in project finance from 2005 to 2007. Based on dollar volume, ECA participation as a percentage of total PF loans is very modest, generally accounting for only about 1.4% of all PF financing (the same percentage share as in 2006). Private financing by commercial lenders and other capital market players clearly continued to dominate PF activity in 2007, as the private markets remained liquid and very competitive. Financial market volatility in the fourth quarter of 2007 led to some slight reduction in liquidity (and increase in financing costs), but the impact on PF activity was negligible for the year.

¹ The ECA project finance deals are those reported by the OECD ECAs and may not include all ECA project finance deals completed in 2007. Further, they include only those OECD notifications that became authorized transactions.

Figure 10: Distribution of PF Loans by Originator, 2005 through 2007 (\$Bn)

	OECD ECAs (excluding Ex-Im)	Ex-Im Bank	All OECD ECAs	Private Lenders	Total
2007*	\$2.6	\$.6	\$3.2	\$223.0	\$226.2
2006	\$3.0	\$0	\$3.0	\$196.2	\$199.2
2005	\$1.7	\$.6	\$2.3	\$166.0	\$168.3

* All figures in every category except for the 2007 total are preliminary figures due to the lack of complete data.

Ex-Im Bank's Policy and Practice

Ex-Im Bank authorized one PF transaction in 2007 (a petrochemical project), after having no PF authorizations in 2006. However, these figures account for only part of Ex-Im Bank's activity in this area, given a recent blurring of the line between project finance and structured finance. Specifically, traditional PF transactions create a new company via a special purpose vehicle which creates and owns the project as well as acts as the borrower. These transactions rely on repayment from revenue generated by the project **only**. *Structured* finance transactions generally involve large expansions of companies where repayment is derived from a combination of reliance on the existing company balance sheet and 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." In 2007, Ex-Im Bank authorized 5 structured finance transactions totaling \$1.4 billion, compared to 9 totaling \$1.3 billion in 2006.

Overall, there are five main factors that characterize Ex-Im Bank's competitiveness in project finance. These include: (1) 100% (of 85% of the U.S. supply contract) U.S. government-guaranteed support for all risks (political and commercial) during both the construction and repayment periods; (2) willingness to utilize the project finance flexibilities provided by the OECD Arrangement with respect to pricing and repayment terms; (3) financing of local costs (up to 15% of total financing); (4) willingness to capitalize interest during construction; and (5) a reasonable and pragmatic commercial approach to project analysis and risk mitigation.

On the other hand, Ex-Im Bank's PF program is restricted by several 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, U.S. Shipping Requirements, and Economic Impact sections in Chapter

6 for more detail). These policies impact actual and *potential*² PF transactions more than other types of transactions for two reasons. First, there are always many sourcing alternatives from all around the world, making the cost/quality competition the most intense and the consequence of any extra cost or delay particularly adverse. Second, the desire of project sponsors to minimize the number of supply sources gives an advantage to ECAs with looser/lower content or shipping requirements.

G-7 ECAs' Policies and Practices

G-7 ECAs offer similar coverage for PF transactions with some differences in the quality of the guarantee, although these quality differences are quickly disappearing as other ECAs – including SACE (Italy), JBIC (Japan), and ECGD (U.K.) -- move to 100% unconditional guarantees. (EDC provides direct loans, and the other two G-7 ECAs provide conditional insurance.) Included in all of the ECAs' cover is support for local costs up to the amount of the down payment (typically 15% through 2007) and cover for capitalized interest that accrues during the construction period.

Exporter and Lender Survey Results

Exporters and lenders rated Ex-Im Bank's basic PF program as competitive overall in 2007 and particularly appreciate its flexible "customer-oriented" approach. However, they expressed concern over Ex-Im Bank's public policy constraints that are not faced by other ECAs, especially those relating to foreign content. Further, the fact that other countries (notably China and Japan) are willing to provide very aggressive financing packages in exchange for natural resources results in U.S. suppliers facing increasingly intense competition in the PF and structured finance arena.

Conclusion

The basic features of Ex-Im Bank's PF program remain competitive with other G-7 ECAs, although the increase to 100% unconditional guarantees by Ex-Im's competitors means the Bank is starting to lose any edge it may have had in its basic PF support. Further, Ex-Im's public policy constraints (economic impact analysis, foreign content policy, and shipping requirements) come into play on virtually every PF transaction, with the growing impact of these constraints having a noticeably adverse consequence for Ex-Im Bank's overall competitiveness in the PF arena. Although Ex-Im Bank's grade remains an A (generally competitive with the G-7 ECAs), this grade does not reflect the negative effects the public policy issues, when present, have on the overall competitiveness of Ex-Im Bank's PF support.

² 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.

Chapter 4: Major Program Structures

Section C: Co-Financing “One-Stop-Shop”

Introduction

“Co-financing,” “reinsurance,” and “one-stop shop” address the 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 could need multiple financing packages to ensure ECA support for exports from various countries.

In any co-financing transaction, a “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 its share of the procurement. The location of the largest share of the sourcing and/or the location of the main contractor will generally determine which ECA leads the transaction. Thus, 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 growth of intra-European and international 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. Since that time, Ex-Im has continued to sign co-financing agreements and to approve co-financing arrangements for specific transactions.

During 2007, Ex-Im Bank signed no new bilateral agreements but experienced another year of significant co-financing case activity, due in part to aircraft transactions. (In the past, Ex-Im Bank’s co-financing program has been dominated by ECGD, since U.K.-produced aircraft engines are one of two options on the popular Boeing 777 aircraft. Without ECGD co-financing, Boeing would not be able to offer 85% support to its customers in one financing package.) The Bank approved 20 co-financed transactions totaling \$2.7 billion (compared to 19 transactions also totaling \$2.7 billion in 2006). Large commercial aircraft sales (which also dominated 2006 co-financing activity) represented 99% of the total dollar amount of co-financing, but accounted for only about 50% of these transactions in terms of number (11 out of 20). Demonstrating the utility of co-financing in certain non-aircraft transactions was of critical importance in consummating a \$4 million sale of medical equipment to China, and

complementing the Administration's Strategic Economic Dialogue talks with the Chinese. As in the previous year, the majority of transactions were co-financed with Japan, the U.K. or Canada. All of the 2007 co-financing deals were done under existing framework agreements, which was also the case in 2006. (See **Figure 11** for a listing of specific transactions).

Figure 11: Ex-Im Bank "One -Stop- Shop" Co-Finance Transactions in 2007 (\$Mn)

Ex-Im Bank & Co-Financing ECA	Market	Project	Amount
Atradius: Netherlands	CHINA	Medical equipment	\$ 4.4
ASHR'A: Israel	BRAZIL	Medical equipment	\$.5
ECGD: United Kingdom	BRAZIL	Saw grinding machines	\$.5
ECGD: United Kingdom	LUXEMBOURG	Aircraft	\$115
ECGD: United Kingdom	ISRAEL	Aircraft	\$228
ECGD: United Kingdom & NEXI: Japan	KENYA	Aircraft	\$112
EDC: Canada	BRAZIL	Ag Aircraft	\$ 1
EDC: Canada	BRAZIL	Ag Aircraft	\$.5
EDC: Canada	BRAZIL	Ag Aircraft	\$.5
EDC: Canada	BRAZIL	Ag Aircraft	\$.5
EDC: Canada	BRAZIL	Ag Aircraft	\$ 1
K-EXIM: Korea	KOREA	Aircraft	\$243
NEXI: Japan	JAMAICA	Dump trucks	\$ 11
NEXI: Japan	CANADA	Aircraft	\$708
NEXI: Japan	INDIA	Aircraft	\$712
NEXI: Japan	AUSTRIA	Aircraft	\$107
NEXI: Japan	CHILE	Aircraft	\$212
NEXI: Japan	UNITED ARAB EMIRATES	Aircraft	\$247
TOTAL			\$2.7 billion

G-7 ECAs' Policies and Practices

The G-7 ECAs have continued to sign multiple framework agreements among themselves (as shown in **Figure 12**) 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. That is, a European Union ECA would seek reinsurance for third country content from the ECA of the country where the content originated, rather than cover it on its own book. 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. For those ECAs where Ex-Im Bank has not been able to conclude a bilateral agreement, Ex-Im Bank will process co-financing requests on a case-by-case basis. However, in 2007, the same technical issues (e.g., following the lead ECA's claims and recovery practices in the event of a default and covering contracts in Euros¹) that have prevented Ex-Im Bank from signing some bilateral framework agreements both (a) led some ECAs to reject Ex-Im Bank requests for co-financing on a one-off basis, and (b) discouraged some exporters from pursuing co-financing on a one-off basis.

Figure 12: G-7 Co-financing “One-Stop-Shop” Agreements in 2007

	Ex-Im	ECGD	EDC	Hermes	Coface	SACE	NEXI
Ex-Im		X	X			X	X
ECGD	X		X	X	X	X	
EDC	X	X		X	X	X	
Hermes		X	X		X	X	X
Coface		X	X	X		X	X
SACE	X	X	X	X	X		X
NEXI	X			X	X	X	

Exporter and Lender Survey Results

Even when Ex-Im Bank is willing to participate in co-financing arrangements, participants noted that the Bank does not have the mechanisms in place to always respond quickly to such requests; in contrast, other ECAs are quite responsive, given their long-standing involvement in co-financing. Because of Ex-Im Bank's inability to sign bilateral framework agreements, exporters tend to “pursue other ECA avenues that are available these days.”

Conclusion

The lack of signed bilateral agreements with the ECAs of Germany and France (the two key players in the co-financing arena) is the main contributor to the Bank's disadvantage vis-à-vis foreign ECAs and, to that extent, Ex-Im Bank's co-financing program is less competitive with the programs of most other G-7 ECAs. As in 2006, the Bank continues to receive a B-/C+ on co-financing.

¹ In December 2007, Ex-Im Bank received approval to begin offering cover for Euro-denominated co-financing transactions without the conversion requirement.

Chapter 4: Major Program Structures

Section D: 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. Recognizing the commercial reality that trade finance was generally conducted on U.S. dollar terms, most ECAs have historically operated robust foreign currency programs, with the bulk of their portfolios in U.S. dollars. Today, however, as **Figure 13** shows, the Euro and other currencies are gaining substantial ground vis-à-vis the U.S. dollar. In fact, by mid-2007, the value of the Euro in circulation surpassed the U.S. dollar, and the Euro is the currency of choice for companies issuing international bonds. While the U.S. dollar is still the preferred reserve currency, the Euro is following closely behind.

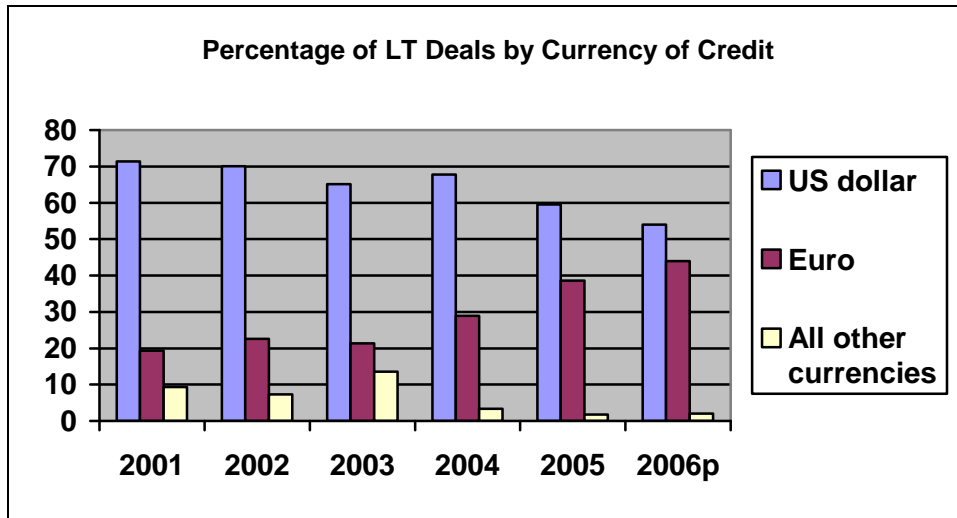
Moreover, the phenomenal growth in liquidity in emerging markets during the course of this decade has resulted in steadily increasing borrower demands for export credit cover in local-currency-denominated (usually "soft" currency) debt. After some reluctance early on, many ECAs began offering local currency cover (some quite aggressively). While local currency offers exceed actual local currency transactions supported, an ECA's ability to provide cover in a currency other than its own is increasingly a competitive tool.

Official support for transactions denominated in a foreign currency is not governed by the OECD Arrangement. Each ECA may decide 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 crystallize¹ the debt, etc.)

The types of currencies eligible for cover are generally referred to as either "hard" or readily convertible currencies (such as the U.S. dollar, the Euro, or the yen) and "soft" or emerging market currencies (such as the South African rand or Mexican peso).

¹ 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. The ECA seeks recovery of the hard currency obligation, and exchange rate risk during the recovery period is borne by the obligor.

Figure 13: Long-Term OECD Export Credit Support by Currency



Source: 2006 OECD Statistics
p = preliminary

Ex-Im Bank Policy and Practice

Like its G-7 counterparts, Ex-Im Bank offers foreign currency support² through its guarantee and insurance programs by backing loans denominated in a foreign currency that are extended by a lender (usually 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 U.S. dollars.

Unlike its G-7 counterparts, Ex-Im Bank employed the same claims procedure throughout 2007 on all foreign currency transactions, including hard currencies such as the Euro: in the event of a default, Ex-Im Bank purchases the foreign currency to pay the claim to the lender and then converts (or “crystallizes”) the obligation into U.S. 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, and unlike any other G-7 ECA, Ex-Im Bank typically accelerates³ the debt and pays the claim in a single lump-sum payment. (Ex-Im Bank uses the same acceleration, claim payment, and recovery process for dollar-denominated debt.) In

² Ex-Im Bank’s foreign currency guarantee program was introduced in 1980 in response to requests that Ex-Im Bank extend U.S. dollar loans at the same nominal fixed rates as those offered by European and Japanese competitors. These competitors were often lending in their domestic currencies which carried lower nominal interest rates (because their *market* interest rates were lower) than did U.S. dollar debt. At that time, borrowers were swayed by the “interest rate illusion” (and did not realize that the differences in nominal interest rates were a function of anticipated exchange rate changes). Thus, U.S. exporters initially sought comparable dollar interest-rate offers to eliminate the potential competitive disadvantage associated with a competitor’s offer.

³ 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).

December 2007, Ex-Im Bank received approval to begin offering cover for Euro denominated co-financing transactions without the conversion requirement.

Ex-Im Bank does have a matching provision that would allow the Bank to consider providing foreign currency (including soft currency) coverage without conversion. Specifically, before any consideration could be given to providing foreign currency coverage without conversion, Ex-Im Bank would need confirmation that a foreign ECA will provide coverage without conversion for the same transaction.

In 2007, Ex-Im Bank supported 13 foreign currency transactions with a U.S. export value of \$1.75 billion (down somewhat from the 17 transactions valued at slightly over \$2 billion in 2006). As in 2006, the majority of foreign currency cases were denominated in hard currencies: 6 Euro-denominated transactions had a value of almost \$1.1 billion, with 4 Canadian dollar transactions totaling \$261.7 million. In addition, Ex-Im Bank guaranteed the Swiss franc (1 farm equipment transaction with a Russian buyer for \$6.1 million); the Korean won (1 aircraft transaction with a Korean buyer for \$292 million); and the Mexican peso (1 locomotive transaction with a Mexican buyer for \$130.1 million). Ten of the 13 transactions were in support of aircraft exports, with Canadian airlines seeking Canadian dollar financing; and airlines in Morocco, Turkey, Austria, and Ireland seeking Euro financing.

G-7 ECAs' Policies and Practices

All G-7 ECAs (with the exception of Ex-Im Bank) 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 G-7 ECAs provided support for export credits denominated in hard currencies. Unlike Ex-Im Bank, however, the other ECAs were willing to accept recoveries in foreign 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), and ECGD (U.K.) do not convert the obligation post-claim payment because they have the capability to assume and manage the foreign exchange rate risk. Hermes (Germany) will cover the exchange rate risk for a surcharge. As a result, the Ex-Im Bank requirement to convert all foreign debt into U.S. dollars is unique. (This requirement can be waived for co-financing transactions denominated in Euros as of late 2007.)

Soft Currency Cover: As noted earlier, ECAs can either accept foreign exchange risk (pay claims and accept recoveries in the soft currency) or crystallize the debt (convert the debt into a hard currency obligation after paying a claim or use alternative structuring that protects the ECA from possible shortfalls resulting from exchange

fluctuations during the recovery phase). As **Figure 14** shows, no uniform practice exists among G-7 ECAs with respect to acceptance of soft currency foreign exchange risk. However, based on a recent ECA survey, 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 are currently assessing the risk/reward equation in order to find ways to manage their risks in the face of legal and practical constraints on crystallization.

Given the reduced credit and transfer risk generally associated with local currency financing (especially when the buyer's revenues are limited to the local currency), ECAs continue to demonstrate a willingness to explore the alternatives associated with local currency cover. In this regard, ECAs have established a variety of criteria for evaluating when to offer non-crystallized local currency in a specific transaction/situation. Some of the factors typically considered include:

- limits on the transaction size;
- only provide such cover for currencies with stable and relatively low interest rates;
- limiting such cover to borrowers with relatively good credit ratings;
- pricing for any incremental risk or administrative expense;
- evaluating the status of conversion clauses in the legal regime of the local market; and
- limiting soft currency cover to those currencies with sufficiently deep and liquid markets to enable the ECA to purchase the currency without impacting its exchange rate.

On the other hand, as countries evaluate their approach to local currency cover, the issues of whether and when to use the OECD discount⁴ come into play. Recent cases indicate that buyers may be indifferent between uncrystallized and discounted offers.

⁴ Under OECD guidelines, crystallized local currency cover is eligible for a 35% - 50% discount from the case-specific premium. However, the discount was only offered 4 times between 1999-2007, twice by Ex-Im Bank.

Figure 14: G-7 ECA Foreign Currency Approaches: Willingness to Accept Exchange Rate Risk and Activity, 2007

	Exchange Risk Accepted?		Currencies ¹ of Approved Transactions (2001-2007)	
	Hard Currency	Soft Currency	Hard Currency	Soft Currency
EDC ²	Yes	Case-by-case	USD, EUR	none
Coface ³	Case-by-case	Yes	USD, AUD, JPY	EGP, MXP
Hermes ⁴	Yes, with 10% surcharge	Case-by-case	USD, GBP, CHF, CND, AUD, JPY	AED, DOP
SACE ⁵	Yes	Limited experience	USD, CHF, GBP, JPY	EGP, MAD, BRL
NEXI ⁶	Yes	No experience	USD, EUR	none
ECGD ⁷	Yes	No, convert obligation to Sterling at time of payment	USD, EUR, JPY	none
Ex-Im Bank ⁸	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

¹Currency Key: USD – U.S. dollar, EUR – Euro, GBP – British pounds, JPY – Japanese yen, AUD – Australian dollars, CHF – Swiss francs, EGP – Egyptian pounds, CND- Canadian dollar, MXP – Mexican pesos, DOP – Dominican Republic peso, ZAR – South African rand, AED -- United Arab Emirates dirham, COP – Colombian peso, BRL – Brazilian real, and MAD – Moroccan dirham.

² EDC will cover Norwegian kroner, Czech koruna, Hong Kong dollar, Hungarian forint, Mexican peso, Polish zloty, Singapore dollar, South African rand, and Turkish lira.

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 – Data not available.

⁷ ECGD – Various.

⁸ Ex-Im Bank will cover Brazilian real, Colombian peso, Egyptian pound, Indian rupee, Malaysian ringgit, Moroccan dirham, Pakistani rupee, Philippine peso, Russian ruble, South African rand, Taiwanese dollar, and Thai baht.

The latest OECD data indicate that long-term export credits offered by OECD countries are steadily shifting more toward the Euro and, to a small degree, other currencies and away from the U.S. dollar. For example, over the 5 years through 2006, the proportion of OECD activity denominated in dollars has gone from over 70% to 54%, while Euro-denominated activity has risen from 20% to 44%. Through 2007, the incidence of soft currency transactions is rare.

Exporter and Lender Survey Results

The exporting community noted a somewhat higher demand than in previous years for hard currency/foreign currency support on non-aircraft transactions but viewed Ex-Im Bank's crystallization policy on such cases as more of a disincentive to use than a significant competitive issue. With regard to soft currencies and local financing, demand has been relatively limited. However, where non-crystallized local currencies are supported by ECAs, the attractiveness of such cover is considered so significant that alternative offers would need to match or offer the discount to be competitive.

Conclusion

The demand for foreign or local currency financing is likely to continue to grow, as borrowers (particularly airlines and emerging market infrastructure obligors) seek to match their non-U.S.-dollar revenues with their debt obligations. Thus, specialized cover such as foreign currency support is increasingly important to competitive financing. Ex-Im Bank's inability, from a programmatic perspective, to accept exchange rate risk in any currency during 2007 clearly limited its competitiveness. Accordingly, the grade for Ex-Im Bank's foreign currency guarantee program in 2007 remains a B.

Chapter 4: Major Program Structures

Section E: Services

Introduction

Pursuant to Section 2(b)(1)(D) of its Charter, Ex-Im 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.” Moreover, Section 8(A)(a)(8) of the Ex-Im Bank Act as updated December 27, 2006 requires the annual Competitiveness Report to include a section “which describes the participation of the Bank in providing funding, guarantees, or insurance for services, which shall include appropriate information on the involvement of the other major export-financing facilities referred to in paragraph (1) in providing such support for services, and an explanation of any differences among the facilities in providing the support.” This chapter represents Ex-Im Bank’s first report on support for services.

Ex-Im Bank’s Policy and Practice

Ex-Im Bank has long supported a large volume of services exports over a wide swath of the “tradeable” services sector. As seen in **Figure 15**, over the last three years Ex-Im has provided financing for roughly \$5.2 billion of U.S. services exports. 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 FY 2007 figure of \$1.5 billion was quite illustrative of the overall period with:

- engineering and design services dominating the volume (approximately one half);
- oil and gas process engineering services continuing to be a dominant industry receiving support (approximately one-third); and
- stand-alone services accounting for roughly one-third of the volume.

During the 2005-2007 period, the largest sector in the stand-alone segment supported by Ex-Im Bank was the information technology sector -- most of which appears to have been software. As for associated service exports (such as oil and gas drilling services), Ex-Im Bank has generally provided these 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. 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 15: Services Supported by Ex-Im Bank, FY 2005-2007 (\$Mn)

	2005			2006			2007			Total		
	Stand-Alone	Assoc.	Total	Stand - Alone	Assoc .	Total	Stand - Alone	Assoc.	Total	Stand-Alone	Assoc.	Total
Legal/Banking	\$3	\$13	\$16	3		\$3		\$16	\$16	\$6	\$29	\$35
Construction	250	400	650	150		150				400	400	800
Info. Technology	332		332	316		316	51		51	699	0	699
Engineering & Design	185	381	566	176		176	90	650	740	451	1,032	1,483
Licenses & Copyright				15		15	3	28	31	18	28	46
Oil & Gas		489	489	11	630	641	146	371	517	157	1,490	1,647
Misc	212	38	250	118	3	121	165	5	170	495	46	541
TOTAL	\$982	\$1,321	\$2,303	\$789	\$633	\$1,422	\$455	\$1,070	\$1,525	\$2,226	\$3,025	\$5,251

Competitor ECAs' Policies and Practices

Bilateral discussions with (and anecdotal evidence from) a variety of G-7/OECD ECAs indicate that official medium- and long-term support for stand-alone services is relatively rare. While all G-7/OECD ECAs appear quite willing to support services as a general category of exports, most medium- and long-term support is provided for services associated with capital goods exports. Moreover, although such associated services are provided the same terms as the capital goods exports, stand-alone services seem to generally receive only short-term support.

Reflecting the “associated-with-capital goods exports” nature of most G-7/OECD medium- and long-term support for services, only those countries that have major firms in the business of building things abroad using at least some amount of domestic capital goods actually support significant levels of services. Currently, the number of G-7/OECD ECAs providing more than \$100 million of support annually for services usually does not exceed five -- with the largest G-7/OECD providers of medium- and long-term support for services being Japan, Germany, and the U.S.

Not surprisingly, the leading sectors receiving G-7/OECD ECA medium- and long-term support are engineering and construction services for those sectors that the major capital goods exporters dominate. For example, the sectors receiving the largest amounts of medium- and long-term support include oil and gas development, power plant construction, mining and refining, and telecommunications. Other sectors frequently mentioned by ECAs include manufacturing and construction licenses and leasing of capital goods products.

In effect, for services that typically are associated with capital goods exports, the amount of G-7/OECD medium- and long-term support is substantial and as fully competitive as that provided to the capital goods exports. However, stand-alone services seem to have no designated programs and, as noted above, are almost always underwritten on a short-term basis.

Conclusion

Ex-Im Bank's support for services places it among the leaders in total volume and in support for stand-alone services. Moreover, reflecting the large volume of stand-alone services support, Ex-Im Bank appears to provide financing assistance of substantial proportions to one of the widest ranges of service companies.

Chapter 4: Major Program Structures

Section F: Ex-Im Bank's Major Program Competitiveness

Ex-Im Bank's major program structures were graded A-/B+ which translates into the Bank being a step below generally competitive with its G-7 counterparts. While Ex-Im Bank's aircraft and project finance programs were rated as generally competitive with its foreign ECA counterparts, the U.S. exporting community graded the co-financing and foreign currency guarantee programs as less than fully competitive. Moreover, these areas once again proved to be relatively more significant due to rising demand of non-aircraft/project finance transactions across a broad spectrum of markets and in situations calling for multiple suppliers. The contrast in flexibility, particularly in co-financing and foreign currency programs, between Ex-Im Bank and its G-7 counterparts continues to expand. **Figure 16** shows how Ex-Im Bank's major programs were rated on individual aspects as well as overall. The grades are based on the survey results and Ex-Im Bank's analysis of how it performs in relation to its G-7 ECA counterparts. While a chapter addressing Services has been added this year, no qualitative comparison is possible, given the limited amount of information available on the other G-7 ECAs' programs devoted to services.

Figure 16: Grading of Ex-Im Bank's Major Program Competitiveness, 2007

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

Ch. 5: Economic Philosophy

Section A: Trade-related Tied and Untied Aid

Introduction

The term “tied aid” refers to any trade-related aid¹ credit provided by a donor government for a public sector project in another country that is conditioned on the purchase of equipment from suppliers in the donor country. “Untied aid” differs from tied aid only in that it is not formally conditioned on the purchase of equipment from suppliers in the donor country. Despite its reputation, tied aid is usually not problematic as it may represent bona fide development assistance that provides critical support for the recipient country. The U.S. Government does not seek to reduce tied aid flows that are for legitimate development purposes, but it does seek to reduce -- if not eliminate -- trade-distorting tied aid, which is tied aid that is motivated by trade, but masquerading as development assistance. Throughout the 1980’s and into the early 1990’s, trade-distorting tied aid was commonplace. Untied aid, which has been a source of financing for just as long, can also distort trade if it is not freely available to bidders from all countries as it purports to be.

Overview of Tied and Untied Aid

Tied aid has the potential to distort trade flows when it does not provide the recipient country with the best value for its dollar. This can happen when the recipient country does not select the bidder offering the best price, quality and service for the equipment, but rather the bidder offering the cheapest financing. The potential for trade distortion is most serious in cases where a donor government provides relatively low concessionality² tied aid financing for “commercially viable”³ 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.

U.S. Government efforts to discipline tied aid at the OECD have resulted in rules (also known as the Helsinki Disciplines) that have been instrumental in limiting

¹ A trade-related credit is defined as financial support provided by a donor to a recipient country for the purposes of importing equipment needed for a project.

² “Concessionality” refers to the total value of the subsidy being provided by the donor country 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 of this aid would be 100%. However, a grant of \$35 million combined with a standard export credit for the remaining \$65 million would have a concessionality of 35%.

³ “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.

the trade-distorting effects of tied aid and redirecting tied aid flows to *bona fide* development projects. Since they came into effect in early 1992, the OECD tied aid rules have helped reduce tied aid to an average of about \$5 billion annually today, from an estimated average of \$10 billion annually prior to 1992.

With respect to untied aid, the U.S. was concerned when Japanese untied aid rose to about \$15 billion per year in the mid-1990s. This led the U.S. to present a series of proposals in the OECD that were geared toward disciplining untied aid similar to the way that tied aid has been disciplined. However, the discussions met opposition from the untied aid donors and the donor community at large, who claimed that untied aid poses no serious threat to free trade. Donors also argued that disciplines for untied aid would only reduce much needed aid to developing countries.

As a result of this impasse, the U.S. proposed a pilot transparency agreement for untied aid whereby donors would make their offers public in order to allow for international competitive bidding and would report the nationalities of bid winners. Specifically, the transparency agreement allows: (1) all OECD Members to access information in order to help their exporters (not just exporters from donor countries) compete for sales financed with foreign untied aid; and (2) the OECD Secretariat to compile procurement data provided by donors on an annual *ex post* basis to see if it provides any evidence of *de facto* tying of untied aid to procurement from the donor country. In November 2006, there was insufficient procurement data to make any such determinations, but OECD members decided to renew the agreement for another two years.

In 2007, the reporting from the transparency agreement showed that there was an increase of 30% in the number and more than 130% in the credit volume of untied aid notifications over the previous year--totaling 116 notifications and \$13.0 billion in credit, respectively. (In 2006, there were 87 untied aid notifications with a credit value of \$5.6 billion.) Japan continued to be the main donor, notifying 87% of the total credit volume in 2007. France and Germany were the next largest donors with 23 notifications for \$824 million and 7 notifications for \$335 million, respectively). The main recipients of untied aid in 2007 were Iraq and Vietnam. The report indicates that almost all of this aid has been offered in accordance with the International Competitive Bidding (ICB) procedures.⁴

⁴ Procurement patterns are not yet available. It is likely that data on procurement will not provide definitive evidence of *de facto* tying of untied aid by the time the transparency agreement expires at the end of 2008. The U.S. will press to extend the agreement for an additional two years to better assess the need for untied aid rules.

OECD Tied Aid Rules and Key Definitions

Appendix F provides a more detailed explanation of the various types of aid and how the OECD tied aid rules are implemented. The following is a synopsis of tied/untied aid that may be useful to understanding its competitive implications to US exporters.

“Helsinki-type” tied aid, or tied aid that was the target of the Helsinki Disciplines, is subject to three principal disciplines: (1) no tied aid for commercially viable projects; (2) all tied aid must be notified to OECD Members at least 30 business days before the bid closing or commitment date, whichever is earlier; and (3) no tied aid for wealthy countries [those with a per capita Gross National Income (GNI) above \$3,595, with this figure changing annually because it is based on annually-adjusted World Bank lending criteria. (See Appendix F, Annex 1).] The other critical component of the OECD tied aid rules, that predated the Helsinki Disciplines, is that tied aid offers must have a minimum of 35% concessionality.

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 Appendix F).

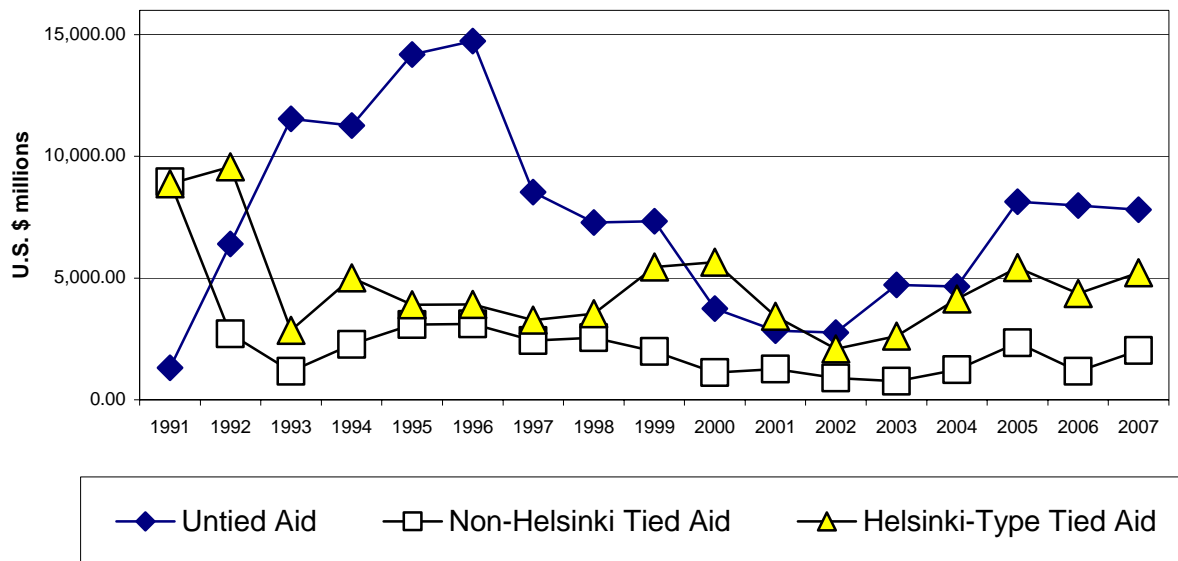
“Non-Helsinki-type” tied aid includes stand-alone *de minimis* projects (valued at less than approximately \$3 million), grants, near-grants (at least 80% concessionality), and partial grants (at least 50% concessionality) that are offered to the poorest countries (the UN-declared Least Developed Countries or LDCs). *De minimis* tied aid can be trade-distorting but, given its small size, it does not typically impact the competitive position of U.S. exporters. In any case, the U.S. Government is prepared to automatically offer U.S. exporters matching financing of *de minimis* foreign tied offers that are made for commercially-viable projects, although U.S. exporters have not approached Ex-Im Bank with any requests to match such offers to date.

Activity Data

Figure 17 indicates that in 2007, Helsinki-type tied aid increased 20% over last year. All tied aid increased by just over 30% of 2006 levels. Despite the increase, however, two points remain critical: (1) the volume of tied aid is still far less than it was before the Helsinki Disciplines went into effect in 1992; and (2) the composition of the tied aid that remains is far different than it was before 1992, representing development assistance rather than trade distortion. The data shows a continuation of the tied aid trends that have dominated tied aid activity for the last five years or so. Specifically:

- Japan is the largest donor of tied aid, accounting for over 45% of all tied aid activity in terms of volume.
- The national ebb and flow of total activity by Japan and Spain account for the bulk of any year-to-year change in activity levels.
- Asia is still home to the largest tied aid recipient (Vietnam in 2007), but China continues to fade as a recipient (5th place in 2007) despite its longstanding position as the largest recipient.

Figure 17: Aid Credit Volume by Type, 1991-2007 (\$Mn)



Note: Consistent untied aid data reporting began in 1994. Discrepancies between untied aid data reported under the OECD Arrangement and that 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) contract bid award -- 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 2007, there were no allegations that any of the tied aid offers from G-7 countries failed to comply with the OECD disciplines or were directed at projects or sectors considered to be financially and/or commercially viable. During the year, Ex-Im Bank approved a Tied Aid Willingness-to-Match offer to an exporter competing for the sale of waste water treatment equipment to a buyer in Sub-Saharan Africa. In addition, Ex-Im Bank re-extended a Tied Aid Willingness-to-Match offer to a U.S. exporter competing for the sale of locomotives in Indonesia.

If these offers are accepted, the \$203 million Tied Aid Capital Projects Fund would be reduced by at least \$48 million.⁵

U.S. Government and Ex-Im Bank Policy

U.S. Government policy seeks to reduce, and ideally eliminate, 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 U.S. Treasury Department work cooperatively to ensure that U.S. exporters have a fair opportunity to compete for commercial sales to projects. Ex-Im Bank's 2006 Charter reauthorization provided greater specificity to the inter-agency tied aid review process.

Exporter and Lender Survey Results

In 2007, most of the respondents to the survey had never encountered any tied aid from any source and were not familiar with tied aid financing. One exporter, however, did note frustration with the tied aid process, indicating that even concrete examples of foreign tied aid offers trigger lengthy deliberations that do not necessarily result in an Ex-Im Bank matching offer.

Conclusion

As in recent years, it seems that U.S. exporters encountered very little aid when competing for export sales in 2007. In addition, in one case that was eligible for consideration (and a second that required extension of a previous offer), Ex-Im Bank approved (and extended) the tied aid offers to maintain a level playing field for the U.S. exporters involved in those competitions. Nevertheless, certain U.S. exporters episodically encounter foreign tied aid that competes with their desired commercial sale of capital goods to projects that are generally considered to be commercially non-viable (for example, fire fighting equipment; tractors; medical equipment). In those few instances, Ex-Im Bank's matching procedures are not typically considered as generating a competitive response; therefore, as in 2006, they had a modestly negative influence in 2007.

⁵ The 2007 budget process resulted in \$25 million rescission of the TACPF.

Chapter 5: Economic Philosophy

Section B: Market Windows

Introduction

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

Market Window institutions have avoided discipline in the OECD for years. Without empirical evidence of trade distortion (due, at least in part, to their lack of transparency on deal-specific terms), it is difficult to measure the competitive impact of Market Windows. Because many U.S. exporters have discovered that they themselves can benefit from Market Window financing, these potential critics have, for the most part, provided no recent evidence of competitive harm.

Recent changes to the Arrangement rules may have weakened the competitive advantage of Market Windows. The Arrangement now enables ECAs to offer relatively more flexible terms, such as permitting longer repayment terms for renewable energy projects, unequal installment amounts for repayment and extended grace periods between the last shipment and the start of the repayment period. However, in practice, these rule changes still cannot completely eradicate Market Windows’ unique strength in the export finance market: the ability to promote national trade interests with government support and without OECD restraints.

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. This matching authority has yet to be used, as there have been no cases where U.S. exporters have sought matching due to an inability to obtain similar financing terms after facing Market Window competition.

G-7 ECAs' Policies and Practices

Only two G-7 countries provide explicit Market Window support: Canada through EDC and Germany through IPEX-Bank, a KfW subsidiary. Other G-7 ECAs could become Market Window players should they perceive a competitive advantage to doing so. Moreover, a 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 tending toward a distinction without a difference for many ECAs.

The following discusses the recent activities and changes in the two G-7 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 2004-2007 reveals significant year-to-year variability. Market Window activity witnessed similar fluctuations, accounting for between 75% and 96% of EDC’s total medium- and long-term export credit business in the years 2004 through 2007 (see **Figure 18**).

Figure 18: EDC Medium- and Long-Term Activity, 2004-2007 (\$Bn)

	2004	2005	2006	2007
Total MLT export credits	\$3.9	\$3.3	\$5.3	\$3.9
Market window	2.9	2.8	5.1	3.3
Official window	1.0	0.5	0.2	0.6

- **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 will continue to be closely integrated into KfW’s overall strategy. Although KfW IPEX-Bank will be provided with initial equity upon spin-off by KfW, it will have a stand-alone credit rating, which will be the basis of its

funding costs. KfW IPEX-Bank will also be 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.

Of IPEX-Bank's \$22 billion business volume in 2007, 78% consisted of commitments outside Germany of which 32% was export credit business. Consistent with expectations that KfW IPEX-Bank will function more like a private sector entity, over 65% of its 2007 export credit business was in support of entities in Europe or North America. The three largest industry sectors receiving KfW IPEX-Bank export credit support in 2007 were ships (30%), rail and road (15%), and basic industries (14%).

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 19** below provides a breakdown between the Market Window and official window support provided by KfW IPEX-Bank since its creation in 2004. In 2007, approximately 50% of 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.

Figure 19: KfW/IPEX-Bank Medium- and Long-Term Activity, 2004-2007 (\$Bn)

	2004	2005	2006	2007
Total MLT export credits	\$3.0	\$3.2	\$4.0	\$5.4
Market window	1.8	1.9	2.2	2.7
Official window	1.2	1.3	1.8	2.7

- **Summary Data**

Combining the two estimates for EDC and KfW IPEX-Bank yields a total of \$6 billion in Market Window volume for 2007, which averages to about \$5.7 billion per year over the last four years (see **Figure 20**).

Figure 20: Market Window Activity, 2004-2007 (\$Bn)

	2004	2005	2006	2007
EDC	\$2.9	\$2.8	\$5.1	\$3.3
KfW/IPEX-Bank	1.8	1.9	2.2	2.7
Total	\$4.7	\$4.7	\$7.3	\$6.0

Exporter and Lender Survey Results

Representative of the exporting community's view, one lender noted that U.S. exporters could provide examples of Market Windows activity but lacked confidence that Ex-Im Bank would be able to adequately address the competitive problem. Another lender noted that Market Windows are no longer even an issue because "all ECAs – except Ex-Im Bank – are operating like market windows in so many ways."

Conclusion

U.S. exporters have not highlighted any specific examples of competition from Market Windows for Ex-Im Bank's attention. Recent changes to the OECD Arrangement rules (e.g., longer repayment terms for renewable energy projects, unequal installment amounts for repayment and extended grace periods between the last shipment and the start of the repayment period) have weakened Market Windows' potential competitive advantage. Market Window data also show two interesting points:

- The focus of much of the formal Market Window activity is in Europe and North America, regions where Ex-Im Bank rarely provides support.
- The major industries supported have little U.S. competition (e.g., shipping and regional jets).

Thus, the two formal Market Windows appear to operate so rarely in areas which intersect Ex-Im Bank's field of activity as to be a neutral influence on Ex-Im Bank's competitiveness.

Chapter 5: Economic Philosophy

Section C: Ex-Im Bank's Economic Philosophy Competitiveness

The U.S. 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. These principles serve as the foundation upon which Ex-Im Bank offers export credit support to U.S. exporters. The U.S. has consistently endeavored to ensure that this framework and principles are fully depicted in the OECD Arrangement.

Tied aid activity occurred in 2007, but Ex-Im Bank addressed the few cases brought to it. Moreover, there was neither documented existence, or even reasonable allegations, of any “*de facto* tied” untied aid, nor instances when market windows had undercut both the market and ECAs. Nonetheless, the U.S. exporting community continues to believe that when U.S. exporters face any one of these forms of financing (the details of which are next to impossible to obtain or criteria are difficult to meet), their competitive position can be undermined.

Figure 21 shows the span of impact that these financing features (e.g., *de facto* tied untied aid, Market Windows) are likely to have on Ex-Im Bank's competitiveness in individual cases when similar terms and conditions are not available to U.S. exporters.

Figure 21: Grading of Ex-Im Bank's Competitiveness When Confronted with Differing Government Financing Philosophies and Programs, 2007

Program	Ex-Im Bank has program (Yes/No)	Impact on Competitiveness
Tied Aid (<i>de jure</i> or <i>de facto</i>)	Yes ¹	Neutral to Negative (infrequently encountered)
Market Windows	No ²	Neutral (would likely be negative if encountered)
Overall Assessment		Negative (on what appears to be a very limited number of transactions)

¹ Ex-Im Bank could use TACPF to match “*de facto* tied” untied aid.

² 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

Ex-Im Bank is the official ECA of the U.S. government. In this role, Congress has given the Bank a mission to promote and maintain U.S. jobs through exports by providing export financing assistance to U.S. exporters that is competitive with financing offered by the major OECD ECAs. The basis for this mission is that government intervention is in the national interest when necessary to (a) act as a lender/insurer of last resort for credit-worthy foreign importers of U.S. goods and services and (b) neutralize financing offered by the major OECD ECAs, so that purchase decisions are made on the basis of market factors such as price, quality and service.

As a U.S. government institution, Ex-Im Bank is entrusted with public funds to carry out its mission and is expected to consider broader U.S. policies when carrying out its core mission of providing export finance to U.S. exporters. Sometimes these broader U.S. policy objectives conflict with the Bank's main objective of facilitating exports and, consequently, may impact its competitiveness. Some of these other policy objectives are specified in Ex-Im Bank's Charter or other legislation (such as economic impact legislation and PR 17 on U.S. shipping). Other issues, such as content requirements, reflect the clear intent of Congress expressed over the years regarding the support of U.S. jobs. The impact of these other policy objectives on Ex-Im Bank's competitiveness can be magnified in specific cases because, in general, other G-7 ECAs have few, if any, such broad public policy considerations.

The following sections in this Chapter present a contextual description of public policies that affect the Bank's competitiveness and an analysis of the competitive implications related to each one. Because the public policies are not expected to impact the same volume of transactions as the core financing and program elements, survey respondents were asked to indicate if they had experience with any of the public policies and economic philosophies and, if so, did it positively, negatively or neutrally affect Ex-Im Bank's competitiveness.

Chapter 6: Public Policies – Stakeholder Considerations

Section B: Economic Impact

Introduction

Pursuant to Ex-Im Bank's Charter, the Bank is required to assess whether its financial support for a transaction would likely cause substantial injury to U.S. industry or result in the production of a good that is subject to a relevant trade measure.¹ Either of these outcomes could result in a denial of Ex-Im Bank support. While all cases seeking Ex-Im Bank support are subject to economic impact scrutiny, only those cases that involve capital goods and services exports that either enable foreign buyers to establish or expand production capacity of an exportable good or result in the production of an exportable good subject to a relevant trade measure are subjected to a more detailed analysis.

Ex-Im Bank's Policy and Practice

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

- result in the production of substantially the same product that is the subject of specified trade measures (see footnote 1); or
- pose the risk of substantial injury to the U.S. economy. Transactions over \$10 million in Ex-Im financing in which the new foreign production is 1% or more of U.S. production of the same product are subject to a detailed economic impact analysis prior to authorization.² That is, Ex-Im Bank staff analyzes the global supply and demand situation of the product in question and assesses the broad competitive impacts on U.S. industry arising from the new foreign production (e.g., whether U.S. production is likely to be displaced as a result of this 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, legislation provides that the

¹ 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.

² 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.

economic impact prohibition will not apply in any case where the Ex-Im Bank Board of Directors determines that the benefits of the transaction outweigh the costs.

In addition to these legislative mandates, Ex-Im Bank's Charter now requires the Bank's Chairman to submit a Sensitive Commercial Sectors and Products List to Congress each year, beginning in 2007. The Sensitive Sector List submitted to Congress in April 2007 included "raw steel-making capacity," "DRAM semiconductors" and "U.S. market oriented" production.³ Inclusion on the Sensitive Sector List is not an automatic indication that Ex-Im Bank will not support a transaction. Rather, this list serves as a notice to potential applicants that, based on the Bank's past experiences, there is a relatively high probability that their transaction will not receive financial support for economic impact reasons.

G-7 ECAs' Policies and Practices

Although G-7 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 and benefits associated with a specific Ex-Im Bank-supported export. In addition, only Ex-Im Bank is required to consider the relevance of trade measures to a transaction.

Ex-Im Bank Summary Data

In 2007, Ex-Im Bank acted on⁴ 586 medium-term insurance and medium- and long-term loan and guarantee transactions (compared to 593 in 2006). Of these transactions, 327 were applications for medium- and long-term loans and guarantees at the Preliminary Commitment (PC) and Final Commitment (AP) stages, and 259 were applications for medium-term insurance. Thirty-five percent (205 cases) of total transactions acted upon were scrutinized for economic impact relevance because they supported a foreign buyer's production of an exportable good. (This compares to 38% of cases in 2006.)

Of these 205 transactions, only 9 (about 1.5% of the total number of transactions acted upon by the Bank) required a detailed economic impact analysis. (This compares to 1% of total transactions requiring such an analysis in 2006.) Of the remaining 196 cases, 187 were under the \$10 million threshold and 9 involved new production of a product considered to be in undersupply on global markets. Three of the 9 economic impact analyses yielded net positive economic impact findings and were approved by Ex-Im Bank's Board of Directors. Of the remaining 6 cases, 2 were withdrawn for economic impact reasons while Ex-Im Bank staff was evaluating the transactions for economic

³ "U.S. 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 U.S. market and will compete directly with U.S. production.

⁴ "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.

impact; the remaining 4 were withdrawn for non-economic impact reasons before the cases came to fruition.

Because of the economic impact mandate, Ex-Im Bank does not support transactions that would result in the production of a good subject to a relevant trade measure, unless the Board of Directors makes an exception, which was not done in 2007. Due to this constraint, staff estimates that applicants did not pursue Ex-Im Bank financing for 13 potential transactions in 2007 after learning about the existence of an applicable trade measure. Of these 13 potential transactions, 12 involved the export of steelmaking equipment, which reflects the large share (just under 50% of all orders) of steel-related AD/CVD orders. In contrast, the steel sector was one of the top 5 industrial sectors supported by other G-7 ECAs last year, with several billion dollars worth of steelmaking equipment and services exports supported during 2007.

Exporter and Lender Survey Results

Although exporters and lenders recognize that Ex-Im Bank's economic impact policy is a legislated mandate, they view the requirement as a distinct competitive impediment for transactions in certain sectors (such as steel and semi-conductor production equipment). Further, the newly implemented Sensitive Sectors List has caused exporters with transactions only remotely related to these sectors to decide to avoid "getting caught in the economic impact quagmire." While the economic impact policy directly affects a relatively small share of Ex-Im Bank activity, the export community stressed that it has a "chilling effect" on potential applicants. Exporters point out that no other ECA is charged with the responsibility to assess economic impact and that the U.S. has other agencies specifically charged with protecting U.S. producers against unfair foreign competition.

Conclusion

Ex-Im Bank's economic impact policy directly affected roughly 35% of the Bank's medium- and long-term transactions acted upon in 2007 (about 1.5% were subject to a detailed analysis and the remaining were subject to an upfront trade measure evaluation, substantial injury determination and/or post-authorization review). Economic impact considerations affected mostly capital goods and services transactions related to the steel sector (where both oversupply considerations and trade sanctions are relevant); however, exporters of other capital goods and services noted the "chilling effect" that the economic impact mandate has on their willingness to approach Ex-Im Bank for support. They also noted that the "chilling effect" was exacerbated by the addition of the Sensitive Sector List. Because no other G-7 ECA is prohibited from supporting transactions due to economic impact considerations, this requirement has a negative impact on Ex-Im Bank's competitiveness.

Chapter 6: Public Policies – Stakeholder Considerations

Section C: Foreign Content

Introduction

Foreign content is the portion of an export that originates outside the seller's and the buyer's countries. For example, a \$10 million U.S. export contract may include a \$1.5 million component sourced from a third country. In this case, the foreign content is the \$1.5 million portion, and the U.S. content is the \$8.5 million portion of the export that originates in the U.S. Because eligibility and cover criteria for foreign content are not governed by international agreement, 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.

Ex-Im Bank's Policy and Practice

In keeping with its mandate to maintain or increase U.S. employment through the financing of U.S. exports, Ex-Im Bank's foreign content policy ensures that its export financing targets the U.S. content directly associated with goods and services exported from the U.S. In order to accommodate U.S. export contracts that contain essential goods and services that are foreign-originated, Ex-Im Bank's policy allows the inclusion of some foreign content in the U.S. export contract with certain restrictions and limitations. Ex-Im Bank's foreign content policy is consistent with the objectives mandated in its Charter, although 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 U.S. supply contract; or (2) 100% of the U.S. content of that export contract.

G-7 ECAs' Policies and Practices

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, OECD ECAs have differing rules on foreign content, and 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 G-7 economies and their respective views on national interest, it is not surprising that foreign content policies vary widely and substantively.

Moreover, over the past several years, there has been a growing and accelerating tide of change in content policies. For example, OECD ECAs are increasingly shifting from the “made **in** country X” approach to the “made **by** country X” approach, which allows ECAs to support more content produced anywhere so long as the overall transaction benefits the domestic economy in some way. This more “flexible” approach is particularly applicable to transactions involving foreign subsidiaries of domestic “champion industries;” and it is leading to a steady increase in the number of ECAs which can support transactions that may not involve direct exports from their home countries.

Figure 22 compares the main aspects of the content policies of the G-7 ECAs in 2007. The data illustrate that Ex-Im Bank’s content requirements and implementation of those requirements are significantly more restrictive than those of its G-7 counterparts.

Figure 22: Comparison of Content Policies of the G-7 ECAs in 2007

	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 is the only G-7 ECA requiring that goods be shipped from domestic shores in order to be eligible for support and, the only one to disallow domestic assembly to transform inputs into “domestic” content. In addition, 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%).

The liberalization of foreign content policies among Ex-Im Bank’s competitors has accelerated over the past several years: in addition to increasing foreign content allowances, European ECAs have generally dropped a previous requirement that, in order to receive maximum foreign content support, that content had to come from an EU country. In 2007, for example, ECGD (U.K.) liberalized its foreign content policy to allow up to 80% foreign content, which raised the G-7 ECA average foreign content allowance to around 65%. The U.K. made this change in order to remain competitive with other ECAs and noted that, so long as ECGD continues to meet its financial goal (of not being a direct cost to the U.K. government), such use of ECGD resources is justified by the “overall benefits” of securing some portion of contract awards (even relatively small portions) out of the U.K.

Ex-Im Bank Summary 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 generally stable relationship between Ex-Im Bank transactions and foreign content. That is, the volume of transactions which include foreign content ranges between roughly 80-90%, while the number of transactions falls between 40-50% of all medium- and long-term activity.

However, the average foreign content ratio has edged up from around 10-12% to 14% over the past two years. Moreover, an analysis of the data in Appendix E¹ over the past five years -- differentiating aircraft from non-aircraft transactions -- shows more pronounced trends. Specifically, the aircraft foreign content ratio moved from just over 12% in 2003 to approximately 15% in 2007, and the non-aircraft foreign content ratio went from roughly 8% in 2003 to approximately 12% in 2007. In addition, the number of non-aircraft transactions with foreign content in excess of 15% jumped from 14% of total non-aircraft transactions in 2003 to 34% of the non-aircraft total by 2007.

¹ 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.

Figure 23: Recent Trends in Ex-Im Bank Foreign Content Support* (\$Mn)

	Authorizations	2003	2004	2005	2006	2007
Total medium- and long-term activity	Export value	\$8,386	\$8,935	\$7,268	\$8,039	\$7,833
	Number of transactions	232	260	271	220	230
Medium- and long-term activity containing foreign content	Export value	\$7,823	\$7,821	\$6,713	\$6,139	\$6,575
	Percentage of total activity value	93%	88%	92%	76%	84%
	Number of transactions	85	95	111	96	108
	Percentage of total activity number	37%	37%	41%	44%	47%
Foreign content	Volume	\$814	\$904	\$691	\$843	\$914
	Average per transaction of cases containing foreign content	10%	12%	10%	14%	14%

*Due to the series nature of these figures, medium-term insurance transactions are not included above because data on these transactions are not available prior to 2006. However, complete data are incorporated in Appendix E.

Exporter and Lender Survey Results

Exporters and lenders see Ex-Im Bank’s foreign content policy as now totally out of date compared to what other ECAs are doing in this arena and to the requirements of globalized supply chains. “This issue is the most critical problem facing Ex-Im and became even more critical in 2007,” noted one exporter, while another claimed that, “Ex-Im is dead last in competitiveness on this issue.” Because Ex-Im Bank’s foreign content policy affecting more and more cases than do the other public policy factors, exporters and lenders view it as the most significant deterrent to using Ex-Im Bank support. Survey participants provided numerous examples of transactions in which other ECAs agreed to support foreign content which Ex-Im Bank could not support, resulting in the shifting of entire procurement contracts out of the U.S. As one exporter stated, “The flexibility of other ECAs [in supporting foreign content] has an undeniable effect on how exporters source deals.”

Conclusion

Globalization of manufacturing continues to grow; and, in response, G-7 ECAs are increasingly adopting “national interest” policies, with one of the main characteristics being more flexibility on the minimum threshold of required domestic content. By 2007, G-7 ECAs’ average “standard” foreign content allowance stood at over 60% of the contract value, while the maximum case-by-case allowance in an increasing number of ECAs reached to 100%. In the context of such numbers, Ex-Im Bank’s maximum foreign content allowance of 15% stands (far) out. As these trends become more pervasive, Ex-Im Bank’s foreign content policy is an increasing disincentive on the use of Ex-Im Bank financing. Today, given the incidence of foreign content (present in roughly half of all transactions; 80-90% by volume) and the rapid (and ongoing) liberalization of competitors’ practices, foreign content is probably the most disadvantageous element in Ex-Im’s program and policy menu. In sum, when transactions involve more than 15% foreign content, Ex-Im Bank’s policy and practice can have a significantly negative impact on the competitiveness of those U.S. exports.

Chapter 6: Public Policies – Stakeholder Considerations

Section D: Local Costs

Introduction

Local costs are goods and services manufactured or originated in the buyer's country. Local costs are historically related to goods and services that, from a practical perspective, would not be sourced from the U.S. (such as cement or construction workers). In contrast to foreign content, the OECD Arrangement sets the basic parameters on official local cost support. Until recently, the Arrangement allowed ECAs to provide support for local costs up to the amount of the down payment, which must be at least 15%. (Beginning in 2008, the Arrangement rules will decouple local costs from the down payment and allow up to 30% local cost support.)

Ex-Im Bank's Policy and Practice

When Ex-Im Bank provides medium- or long-term guarantee, loan or insurance support for U.S. exports, it can also provide support up to 15% of the value of the U.S. exports (including eligible foreign content) for locally-originated or locally-manufactured goods and services. Ex-Im Bank's local cost policy reflects the premise that some amount of local labor and raw materials is necessary to efficiently build or assemble the end product of the U.S. export.

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

For long-term transactions, automatic local cost support is generally available, provided the local costs are related to the U.S. exporter's scope of work. Automatic local cost support is also available for all environmentally beneficial exports, the 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, the local costs need not be related to the U.S. exporter's scope of work, although the local costs must be beneficial to the project.

G-7 ECAs' Policies and Practices

All G-7 ECAs adhere to the basic local cost parameters set forth in the OECD Arrangement. In 2007, ECAs were able to provide support for local costs related to officially supported export transactions up to the amount of the down payment, typically 15%.

Over the past five years, pressure from both a globalizing world and content regulations in many buyer countries have been forces leading to a large expansion in the establishment of local subsidiaries around the world. As a consequence, local capacity in many emerging markets has dramatically improved, leading to a change in the nature of the local goods and services that ECAs are being requested to support. Traditionally, ECAs have provided local cost support for local labor and basic materials; however, due to a combination of legal requirements to procure locally and improved local capacity, ECAs are more frequently being requested to provide support for locally manufactured capital goods.

As subsidies have been removed to a large extent from export credits generally, it appears that some ECAs have chosen to expand/liberalize their use of local costs support as a way to enhance their competitiveness. Perhaps as a consequence, it appears that most ECAs now offer more local costs support fairly regularly. In addition, because ECAs have different interpretations of what costs are considered "local" vs. "domestic," competitiveness among ECAs can vary significantly on a case-by-case basis.

The growing interest among some ECAs (especially smaller ECAs) and exporters in enlarging the scope of official local cost support within the OECD to directly cover more non-domestic content led to a change in Arrangement guidelines effective 2008. In late 2007, the Arrangement guidelines were changed to allow up to 30% local cost support. During a three-year trial period, Arrangement Participants will be required to submit prior notification (including some detail on the nature of the local costs being supported) when support exceeds 15%. As in the past, the Arrangement defines local costs as expenditures for goods and services in the buyer's country that are necessary either for executing the exporter's contract or for completing the project of which the exporter's contract forms a part.

Ex-Im Bank Summary Data

Figure 24 illustrates recent trends in Ex-Im Bank's support of local costs. In 2007, the dollar volume of transactions that received local costs support represented 2% of total medium and long-term activity, up slightly from 1% in 2006. The decrease from 9% in 2005 can be largely attributed to the low level of authorized project finance transactions (seven in 2005; none in 2006; 1 in 2007). Moreover, the significant decrease in the dollar volume of transactions receiving local costs support during the last two years reflects the fact that the majority of transactions (approximately 90% in 2006 and 2007) were medium-term transactions valued at less than \$10 million. In 2007, as in the two

previous years, almost three-quarters of local costs financing supported installation costs, on-site construction and labor costs. The remaining one-quarter was generally comprised of import duties and value-added taxes.

Figure 24: Ex-Im Bank Local Costs Support, 2003-2007 (\$Mn)

	Authorizations	2003	2004	2005	2006	2007
Total medium- and long-term activity	Export value	\$8,873	\$10,949	\$7,791	\$8,718	\$7,833
	Number of transactions	569	757	587	485	412
Medium- and long-term activity containing local costs	Number of transactions	57	79	88	47	36
	Percentage of total number of transactions	10%	10%	15%	10%	9%
Local costs	Volume	\$123	\$312	\$669	\$54	\$119
	Percentage of total medium- and long-term activity	1%	3%	9%	1%	2%

Exporter and Lender Survey Results

Participants noted that local costs support is critically important to certain types of projects (large infrastructure) and to certain types of exporters (such as large engineering firms). In these situations, the fact that Ex-Im Bank's policy allows for the same percentage of local cost support as those of its major competitors is an important competitive factor. However, Ex-Im Bank often takes a more conservative approach in deciding what costs can be defined as "local," which can put the Bank at a competitive disadvantage when compared to its G-7 counterparts.

Conclusion

During 2007, Ex-Im Bank's local costs support policy continued to be -- *on its face* -- competitive with that of its G-7 counterparts, in that all OECD Arrangement Participants allow the same maximum level of local content support (15% in 2007, increasing to 30% in 2008). However, differences in definitions of local cost and the increasingly pro-active use of local costs support as a competitive tool by other ECAs are working to make Ex-Im Bank's local costs policy somewhat less competitive. When considered as a whole for 2007, these trends are not yet significant enough to move the "impact" of the deal. Hence for 2007, Ex-Im Bank's local cost policy continued to be evaluated as having a neutral impact on competitiveness.

Chapter 6: Public Policies – Stakeholder Considerations

Section E: U.S. Shipping Requirements

Introduction

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

PR-17 and other cargo preference legislation aim to support the U.S.-flagged commercial fleet which serves as an important national security asset during times of war or national emergency. From the perspective of U.S. exporters, however, cargo preference requirements can make U.S. goods less competitive relative to foreign goods because foreign exporters have no shipping requirements and U.S.-flagged shippers generally charge higher rates than their competitors.

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 U.S.-flagged vessels. 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.

In October 2004, Ex-Im Bank and MARAD negotiated a new Memorandum of Understanding on PR-17 shipping requirements that raised the threshold for the application of the requirement to Ex-Im Bank's guarantee program from \$10 million to \$20 million. The Memorandum, which includes the language below, went into effect on October 26, 2004.

“For transactions that are greater than \$20 million or are of terms greater than 7 years (even if the transaction is for less than \$20 million), exporters are still required to follow the traditional process. Specifically, exporters are responsible for ensuring that they comply with Ex-Im Bank policy implementing PR-17. Pursuant to PR-17, upon request, MARAD may waive the U.S. flag vessel requirement on a case-by-case basis.”

If a waiver from MARAD is obtained, Ex-Im Bank may provide financing for goods shipped on vessels of non-U.S. 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 U.S.-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 U.S. vessels in its foreign trade). Statutory waivers may be granted when it appears that U.S. vessels will not be available within a reasonable time or at reasonable rates. Compensatory waivers may be granted when foreign borrowers or U.S. shippers ship goods on non-U.S.-flagged vessels and subsequently enter into a U.S. Government-supported financing agreement for those goods. In such cases, a Compensatory waiver may be granted instructing an equivalent amount of non-U.S. Government-supported goods to be shipped on U.S.-flagged bottoms within a specified time period. Conditional waivers may be granted for cases where no U.S.-flagged vessel is available to accommodate multiple shipments of “critical item” cargoes during a proposed project time period.

Since 2002, according to MARAD data, 100% of all General, Compensatory, and Conditional waivers requested have been approved. Statutory Waivers have a 92% approval rate.

Currently, the U.S. is a party to four bilateral Maritime Agreements (with Brazil, Taiwan, China and Russia) negotiated by U.S. delegations headed by the U.S. Maritime Administrator. The Brazilian Maritime Agreement has particular relevance to Ex-Im Bank because it 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 U.S. content. Of note, no waivers were requested or granted under the Maritime Agreement with Brazil in 2007.

G-7 ECAs’ Policies and Practices

None of the other G-7 ECAs have similar cargo preference restrictions.

Ex-Im Bank Summary Data

Figure 25 shows the outcome of Ex-Im Bank-related waiver applications to MARAD for 2002-2007. According to MARAD, all applications for statutory waivers that were denied were due to a determination by MARAD that U.S.-flagged vessels were available to carry the cargo within a reasonable amount of time and/or at a reasonable rate.

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

Waiver Type		2002	2003	2004	2005	2006	2007	Total	Percentage of Waivers Approved
General	Approved	3	0	0	1	0	1	5	100%
	Denied	0	0	0	0	0	0	0	
Statutory	Approved	22	29	26	19	17	6	119	92%
	Denied	1	5	2	2	1	0	11	
Compensatory	Approved	10	11	5	3	2	6	37	100%
	Denied	0	0	0	0	0	0	0	
Conditional	Approved	0	0	0	1	0	0	1	100%
	Denied	0	0	0	0	0	0	0	
Total	Approved	35	40	31	24	19	13	162	94%
	Denied	1	5	2	2	1	0	11	

Source: MARAD

Exporter and Lender Survey Results

The exporting community is unanimous and adamant in its position that the procedures employed by MARAD over the last 3-4 years have had a cumulative negative effect of such proportions that, by 2007, U.S. exporters with major projects were not even given a chance to compete for some sales (e.g., where ECA financing was expected to be needed.) The exporters and banks point to aspects such as the following.

- While MARAD doesn't deny many waivers, the sometimes year-long wait and paperwork burden to obtain a waiver have led some buyers to declare that they will never again deal with a U.S. exporter imposing MARAD requirements.
- Because denial of a waiver can add 5-10% to the overall export price, several U.S. exporters who have experienced denials no longer bid certain kinds of projects from the U.S.
- The decline in waiver requests in the face of a global boom in exports is indicative of the significant negative impact of MARAD requirements.

Conclusion

MARAD requirements appear to have created a major disincentive for U.S. exporters bidding on large projects. Although the MARAD requirement now applies to fewer cases (due to the increase to \$20 million for guarantee transactions), the bulk of the burden falls on exporters of large capital equipment sales and/or projects. The U.S.

exporting community strongly believes that when MARAD rules apply to a transaction, those rules have a decidedly negative impact on Ex-Im Bank's competitiveness.

Chapter 6: Public Policies -- Stakeholder Considerations

Section F: Ex-Im Bank's Public Policy Competitiveness

Compared to other G-7 ECAs and, in fact, other OECD and major emerging market ECAs, Ex-Im Bank's set of public policy requirements more tightly parameter where and how Ex-Im Bank can offer support to U.S. exports. Of the four policies evaluated here, only two have an even broadly similar influence in other countries and only one -- local cost -- is controlled by the OECD. Not surprisingly, the potential impact these influences have on case-specific competition varies from neutral to very negative. In fact, reflecting the many realities of a globalizing world, one of these policies -- content -- is now considered the primary obstacle to case-specific competitiveness of an Ex-Im Bank offer of support.

Figure 26: Grading of Ex-Im Bank's Public Policy Competitiveness, 2007

Policy	G-7 ECAs Have Similar Constraint? (Yes/No)	Potential Impact on Case-Specific Competitiveness
Economic Impact	No	Negative
Foreign Content	Yes(waning)	Extremely Negative (frequently encountered)
Local Costs	Yes	Neutral
PR 17	No	Negative
Overall Assessment		Negative

Chapter 7: Overall Results

For 2007, Ex-Im Bank's overall competitiveness as compared to its G-7 ECA counterparts is deemed to be an A-/B+, the same as in 2006. However, there are multiple signals in the 2007 developments that the Bank's competitive position is weakening. The key areas where weakening has, or may have, begun in 2007 are highlighted below.

First is the ever-expanding difference related to content flexibilities. The differences between Ex-Im Bank and the G-7 ECAs (as well as most other OECD ECAs) have both widened and deepened to such a degree that content has become a serious competitive issue for U.S. companies of all sizes. In 2007, ECGD, long a philosophical ally and policy "soul mate," instituted a dramatic change by requiring only 20% UK content. Moreover, according to a number of major U.S. exporters, the ripple effect of this deterioration is reaching down into the industrial hierarchy, so that small companies are no longer being awarded sub-contracts because multinationals are sourcing from outside the U.S. Consequently, Ex-Im Bank is clearly isolated at the far end of the restrictive spectrum, with the impact of the Bank's position regarding content being felt more sharply than before. Hence, the Report has accented this greater degree of "negative" by describing the impact of this factor as "extremely negative."

As illustrated in **Figure 27**, the second factor concerns the core financing element of cover policy. The Bank's performance with regard to cover policy and its attitude toward risk in 2007 was judged to have remained at an A grade, with Ex-Im Bank "equal to the average." However, based on limited data and anecdotal information, indications suggest that this element deteriorated slightly in 2007.

Figure 27: Grading of Ex-Im Bank's Overall Competitiveness, 2007

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

Figure 28: Direction of Case-Specific Competitive Impact of U.S. Economic Philosophy or Public Policy on Certain Official Export Credit Activity, Procedures or Practices, 2007

Areas Affected by U.S. Economic Philosophy or Public Policy	Potential Case-specific Impact on Competitiveness
Economic Philosophy A. Tied Aid (<i>de jure</i> or <i>de facto</i>) B. Market Windows	Neutral to negative (<i>infrequently encountered; therefore, a modest overall competitive impact</i>) Neutral (<i>would likely be negative if encountered</i>)
Public Policy A. Economic Impact B. Foreign Content C. Local Costs D. Shipping – PR 17	Negative Extremely Negative (<i>frequently encountered; therefore, a significant impact</i>) Neutral Negative

Thus, while the movements described above are not all neatly quantifiable, a look around the export credit arena leaves the definite impression that the Bank’s relative competitiveness slipped a bit, but not enough to warrant a downgrade. Hence, Ex-Im Bank’s overall competitiveness relative to its ECA counterparts remains at an A-/B+.

Further, Chapter 8 describes the growing philosophical and operational disparity between Ex-Im Bank as a lender-of-last-resort ECA and most other G-7/OECD ECAs operating in a private sector mode. This trend, which began several years ago, has proceeded at a fairly steady pace, and in 2007, reached a stage where the playing field was looking unfamiliar (if not unlevel).

Chapter 8: The Competitive Implications of Diverging Paths: Lenders of Last Resort vs. Quasi-Market Players

Introduction

Reflecting the major changes which have occurred in the export credit world over the past 5 to 7 years, the Competitiveness Reports of the last few years have identified the emergence of a new competitiveness framework for G-7/OECD¹ ECAs. As described in past Reports, many of these ECAs initially responded to this changing world with relatively subtle and isolated shifts in their policies and approaches. However, as the years progress, an increasing number of these ECAs have redefined their roles and revamped their policies to the point that two distinct types of ECAs can now be identified: those continuing to operate along traditional lines as lenders/insurers of last resort, and those moving to a different trajectory and operating as quasi-market players. Previous chapters of this report have touched on some of the competitive implications of the differences in specific policies and procedures employed by these two types of ECAs. This chapter provides a broader look at (a) how this still-evolving dichotomy in fundamental orientation and philosophy affects strategic choices on objectives and use of tools; and (b) how these strategic choices impact the day-to-day reality of competitiveness.

A Changing Export Credit World

The new competitiveness framework is primarily the result of four significant developments in the export credit world in which G-7/OECD ECAs operate.

- Largely as a result of official export credit disciplines put in place at the insistence of the U.S. over the last 20 years at the OECD (supported by favorable global economic trends over the past decade and guided by recent WTO panel rulings), financial subsidies have been eliminated from OECD ECA medium- and long-term systems. “Market-related” operating mechanisms are the rule going forward.
- International capital markets have become more sophisticated, liquid, and efficient; and emerging market credit and capital markets have expanded dramatically in the last decade.
- Globalization has resulted in complex supply chains, with virtually all capital equipment having some significant amount of foreign content.

¹ The bulk of this Report generally focuses on G-7 ECAs, since these ECAs have historically been the main competitors within the export credit arena. Because this chapter looks at broader issues and changes, many of which are being led by OECD ECAs outside the G-7, the chapter generally focuses on *all* OECD ECAs.

Buyers often import equipment related to one transaction from more than one country.

- Non-OECD ECAs, such as those in China and Brazil, have emerged as major players in medium- and long-term business in the traditional developing country markets and operate without the constraints of the OECD Arrangement.

The 2004 and 2005 Competitiveness Reports discussed the implications of the rise of the non-OECD ECAs. The 2006 Report identified the looming split of ECA models due to the impact of the first three developments. This year's Report (and particularly this chapter) examines the strategic implications these significant developments have for ECA objectives and practices – and ultimately on the measure of an ECA's competitiveness.

In effect, these market evolutions have created an export credit environment strongly suggesting that ECAs alter their operating paradigms in one or more of three very important ways or risk becoming marginalized.

- WTO rulings tend to focus institutional rationales for existence more on financial outcomes than on economic accomplishments. The emergence of profitability at ECAs over this decade has provided most with sufficient financial independence from their governments to refocus their rationales.
- As the capacity of international and emerging capital and credit markets to finance capital goods purchases has grown, ECAs are no longer “the only game in town.” They now need to develop new ways to attract business and compete with other ECAs (and maybe even with private financial market entities) in order to remain relevant players.
- The increased foreign content in exported goods has led many ECAs to redefine the equation they use for determining the national value attributable to their activity. The basic devolution has been from the economic/financial needs of specific transactions to broad and often hard-to-quantify “national benefits.”

As G-7/OECD ECAs adjust to these three pressures for change, a steadily increasing number of them are putting in place objectives and practices that do not fit the traditional Lender/Insurer of Last Resort paradigm. The implications of this paradigm split are already significant to case competitiveness and may become fundamental to an ECA's core mandates.

The Two Types of ECAs²

As introduced in last year's Report, the multiple and diverse reactions to these influences are creating a yawning gap in the world views of G-7/OECD ECAs. The two basic camps can be represented as follows.

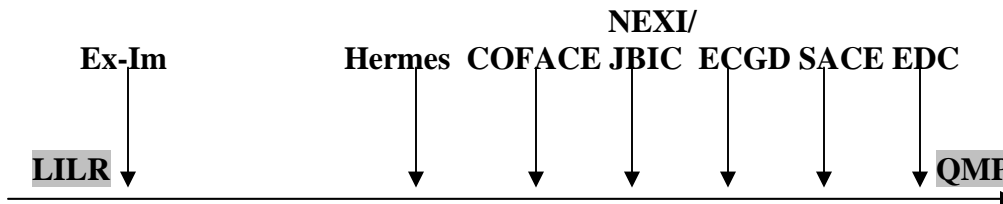
- **Lenders/Insurers of Last Resort:** Most OECD ECAs have traditionally focused on correcting market failures, mitigating against risks that the private sector is unwilling or unable to assume and ensuring a level playing field for their national industries. In this context, the ECA is a public entity or private company that acts on behalf of the government. This traditional business model is that of "Lender/Insurer of Last Resort" (LILR). An LILR is generally focused on supporting higher-risk, longer-term transactions and seeks to complement (not compete with) the private sector. Historically, this philosophy was broadly shared among most G-7/OECD governments and shaped their ECAs' policies and programs. However, today it seems dominant only in the US and an important factor in only a few other countries (e.g., France, Germany, and Switzerland).
- **Quasi-Market Players:**³ The bulk of the G-7/OECD ECAs are transforming their organizations more or less towards "Quasi-Market Players" (QMP), which are more commercial-like in their products, procedures, and strategic outlook. While a QMP still has a public mission, it is usually very broad and loosely defined: rather than tying its support directly to domestic jobs and exports, a QMP justifies its support on the basis of broad national benefits such as those arising from exports by a *foreign subsidiary* of a domestic company. The scope of a QMP's activity tends to include a significant volume of moderate- and low-risk activity in OECD markets as a safety "ballast". In the quest to absolutely minimize even short-term operating losses, QMPs may seek to have a significant volume of activity in high-income OECD markets and exploit niche opportunities in highly commercial areas – both of which can sometimes result in a competitive relationship with the private sector.

The illustration below characterizes and represents each G-7 ECA along a spectrum moving from an LILR approach to a QMP approach. In general, most other Western European ECAs are between Hermes and SACE, with more tending toward SACE than Hermes.

² Descriptions of the traditional roles of ECAs and key elements of an LILR and QMP were largely taken from Raoul Ascari's (SACE) 2006 report, *Is Export Credit Agency a Misnomer? The ECA Response to a Changing World*.

³ "Market windows" were an early hybrid form of this type of ECA. However, the inherent competitiveness of a market window approach is starting to be superseded by more fundamental changes as ECAs embrace the QMP approach.

ECA Spectrum



Operations and Policy in LILR and QMP ECAs

In order to compare LILRs with QMPs, it is helpful to look at how these two types of ECAs tend to operate in three important areas: financial profitability, private sector competition, and national content support. (In order to communicate the essence of differences most clearly, the comments below are expressed more broadly and sharply than the policies are typically presented or implemented by individual ECAs. Moreover, a full-blown QMP would likely be changing its approach in all three areas; however, most OECD ECAs exploring this model are changing in only one or two areas.)

- **Financial Profitability**

LILR: For an LILR, financial results are one measure of its operations, but achieving profitability is not a goal in and of itself. This means that the LILR makes a decision about whether or not to support an individual transaction based on that transaction's economic/financial need for such support and then ensures that the risk is responsibly and consistently priced and evaluated. Concerns with portfolio balance are not allowed to override the needs of an otherwise "good" transaction. In other words, operating processes such as underwriting and pricing are structured and organized to facilitate and support the fundamental decision on economic/financial need (while also meeting other institutional mandates such as OECD guidelines on individual cases and WTO long-run break-even guidance).

QMP: For a QMP, financial aspects are a driving force behind virtually all operating decisions. In fact, a QMP may seek to be more profitable than simply breaking even over the long term, avoiding any chance of even a short-term drain on the national treasury. A QMP actively manages its risk portfolio on a continuous basis by using a variety of tools, such as credit default swaps and reinsurance from the private sector. Overall portfolio management concerns (such as excessive risk concentration by country or sector) could be a deciding factor when determining whether to provide support for an otherwise creditworthy and appropriate transaction. In effect, a transaction generally has to first meet a variety of financial standards before a QMP looks to what the "national benefit" might be.

Potential Policy Implications: The ECA tools most relevant to financial profitability are the core competitive ones of interest rates and fees. Moreover, these tools are the ones most affecting potential subsidy use. Not surprisingly, therefore, these aspects have been at the center of decades of OECD and WTO efforts to bring discipline to official export credits. These years of discussion and study have illuminated the fact that there is a policy trade-off between maximizing an ECA's economic contributions that come from being an LILR and minimizing the possibilities of experiencing short-term losses. That is, to the extent an ECA exists to do what the market does not do consistently or dependably, that mission is compromised the more the ECA mimics private market characteristics. Conversely, nothing so threatens the long-run viability of a QMP as having a sub-portfolio of transactions in riskier markets or in which lower interest rates or fees were needed to match those offered by an LILR.

Hence, LILRs tend to advocate interest rate and fee systems that support economic goals by emphasizing long-run stability, consistency, and dependability. In contrast, QMPs tend to advocate rate and fee systems that support financial objectives by emphasizing short-run "mark to market" characteristics. Over one or two decades, the average rates and fees of both types of ECAs might not differ much. However, the moment-to-moment differences could be significant, with QMPs having higher rates/fees in riskier markets and times and lower rates/fees in less risky markets and times. If the OECD/WTO regulatory mechanisms ultimately come down unambiguously on one side or the other of this divide, such a decision may well lead to a shut-down or paradigm shift by the other ECA model.

- **Private Sector Competition**

LILR: In order to justify the use of government resources (including implicit ones such as those accruing from a "full faith and credit" status) , an LILR seeks to do only what the private sector cannot do and avoids competing with private lenders, reinsurers, and other financial market players. While an LILR monitors the riskiness of its overall portfolio over the long term, it does not actively manage its risk portfolio over the short term. Hence, this philosophy generally prohibits an LILR from regularly selling off part of its loan portfolio to private investors (the portfolio should be one which private investors cannot take on) or reinsuring a portion of its portfolio with private insurers (any ECA use of reinsurance would absorb limited market capacity for protection no official ECA economically needs). In sum, an LILR responds to the private sector by filling gaps in the commercial market and is careful not to give itself (or one part of the private sector) an unfair (government-supported) advantage.

QMP: Given its focus on profitability, a QMP may regularly find itself in competition with the private market. While this poses no problem if the overall government philosophy incorporates a “state capitalism” element, it leads to a vastly different approach to new business and portfolio structure than that of an LILR. For example, a QMP would tend to seek out low-risk transactions from high-income OECD markets to incorporate a safety wedge in its portfolio. The impact of such different portfolio preferences is already showing up in OECD statistics. For example, over the last 7 to 8 years, the share of OECD ECA medium- and long-term activity in High Income markets (the richest countries in the world) has climbed from roughly 20% in the late 1990’s to over 40% in 2006.

Potential Policy Implications : For over 25 years the Arrangement had very few parameters addressing business in developed countries (particularly on terms beyond 5 years), largely because none of the OECD ECAs did more than a *de minimus* level of business in such markets. In fact, for most of this period, the EU had internal guidelines prohibiting long-term official ECA support among its members. However, since the beginning of this decade, ECA activity in developed countries has steadily increased, as has the Arrangement’s attention to issues related to this activity. For example:

- In 2004, “project finance flexibilities” (which govern some project finance terms) were codified with amendments opening up High Income markets for long-term official export credit support.
- Over the past several years, at least one reason given by some for increasing attention to buyer fees is the mounting interest to apply fees below MPRs in better markets.

The divergent goals in this arena have several key policy implications.

- The incursion of OECD ECAs into American and Western European markets clearly widens the scope of ECA involvement in global trade. Because this widening is occurring in countries where there has never been any allegation that capital markets are inefficient or incapable, it would seem that increased activity in such markets is more likely to distort trade than to facilitate additional trade.
- A shift in activity and attention toward better markets/borrowers maximizes a QMP’s strength (providing sophisticated buyers just the mix of support they want in a “customer-friendly” fashion) and minimizes an LILR’s strength (taking concentrated amounts of risk). Thus, as ECA competition increasingly moves to the less risky borrowers/countries, an LILR will be at a comparative

disadvantage when supporting its exporters who are bidding against QMP-backed competitors in this lower-risk arena.

- **National Content (“Made In”) vs. National Interest (“Made By”) Support**

LILR: An LILR justifies its existence by correcting private market imperfections and must be an efficient provider of the economic benefits resulting when the market is “corrected” to work as it should have. The measurement of these economic benefits tends to emphasize the direct employment effects of ECA-supported activity. Therefore, an LILR focuses its support on those exports actually produced and shipped from the LILR’s country. This focus means that an LILR takes a conservative approach to supporting foreign content and local costs by closely monitoring and strictly defining these items. For example, foreign content generally includes any item not actually made domestically, even if the content is made by a foreign subsidiary of a domestic company. Local costs support is largely limited to goods and services that are directly related to the particular sale and sourced from the buyer’s country. This “made in” approach tends to emphasize economic measures of success that relate to labor, the *physical* factor of production.

QMP: Because a QMP operates under the condition of not generating a budget cost to the government, a QMP generally has a great deal of flexibility in how it justifies its existence and quantifies its worth. Its “government” mission is likely to be fairly loosely defined by whatever broader (frequently indirect), longer-term benefits may accrue (to the country, somewhere, someday) from its support of a particular transaction. Most importantly, this wide-open approach means that QMPs are able to handle situations such as following their “national champion” companies offshore and supporting their off-shore subsidiaries’ exports. This approach to production eligible for QMP support has also blurred the lines between “tied” (to domestic inputs) and “untied” assistance, opening the door to QMPs’ supporting a variety of transactions that may be only tangentially related to an actual export from the host ECA’s country. In the most extreme case, no part of the transaction may originate in the host country. In such cases, the QMP justifies its involvement on the basis of a *very* broad definition of national benefits, facilitated by the fact that the transaction will be a money-maker for the QMP. This “made by” approach tends to emphasize financial measures of success that relate to private-sector corporate profitability, the *capital* factor of production.

Potential Policy Implications: Over the past 5 years, the average domestic content requirement of G-7/OECD ECAs (excluding Ex-Im Bank) has gone from about 70% to about 35%. (See **Figure 29**). Moreover, while most G-7/OECD ECAs had fairly firm floors on minimum domestic content five

years ago, today's domestic content figure is more of a target. Separately, at the end of 2007, the OECD Arrangement local costs maximum went from 15% to 30% (for a trial period).

Hence, looking at just the four European G-7 ECAs in a standard long-term transaction, the typical domestic content has gone from 74% (\$85 domestic content for every \$115 in ECA support) to 38% (\$50 for every \$130). Similar trends are evident throughout the OECD ECAs. While the basic direction of both local and foreign content trends has been driven by the macroeconomic globalization trend rather than mercantilist strategies, the increasing amount of “untied” (to domestic inputs) money now available from a steadily growing number of ECAs creates openings for major competitive leverage.

Figure 29: OECD ECAs' Domestic Content Requirements, 2002 vs. 2007

	% of Standard Domestic Content, 2002	% of Standard Domestic Content, 2007
Ex-Im Bank	85%	85%
Other G-7 OECD ECAs	70%*	35%**
Non-G-7 OECD ECAs	50%*	40%**

* European Union ECAs could increase foreign content from 15% to 30% if the content was from other EU countries.

** At least half the ECAs could go below the standard – theoretically, to 0% domestic content -- for appropriate “national interest” considerations.

Overarching Implications for Ex-Im Bank Competitiveness

As the paths of ECAs continue to diverge more markedly, Ex-Im Bank is becoming the most absolute LILR ECA, existing for very different reasons and operating with very different policies and practices than the increasingly dominant QMP model. This development poses unique and fundamental competitive challenges for Ex-Im Bank.

For example, while the emergence of non-OECD ECAs poses a competitive threat, Ex-Im Bank could compete with such ECAs by using its existing authority and tools if it (and larger U.S. Government trade policy) chose to do so. On the other

hand, competing effectively with QMPs could imply a number of changes that are not compatible with overall U.S. government philosophies on the role of government in general or in trade.

In the meantime, the task of comparing “competitiveness” becomes ever more difficult as G-7/OECD ECAs continue to diverge along the two paths outlined above. Even though the driving motivations behind the movement toward QMPs appear non-mercantilist, the increasing importance of philosophically incompatible elements in OECD export credit systems creates an environment in which comparing competitiveness becomes very difficult.

Appendix A: Calculation of Ex-Im Bank Grade

In the body of this report, the U.S. 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 U.S. 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
A+	Fully competitive compared to other ECAs. Consistently equal to the (or is the sole) ECA offering the most competitive position on this element. Levels the playing field on this element with the most competitive offer from any of the major ECAs.	4.33
A	Generally competitive compared to other ECAs. Consistently offers terms on this element equal to the average terms of the typical major ECA. Levels the playing field on this element with the typical offer from the major ECAs.	4.00
A-/B+	Level of competitiveness is in between grades A and B.	3.50
B	Modestly competitive compared to other ECAs. Consistently offers terms on this element equal to the least competitive of the major ECAs. Does not quite level the playing field on this element with most of the major ECAs.	3.00
B-/C+	Level of competitiveness is in between grades B and C.	2.50
C	Barely competitive compared to other ECAs. Consistently offers terms on this element that are a notch below 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
D	Uncompetitive compared to other ECAs. Consistently offers terms on this element that are far below 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
F	Does not provide program.	0.00
NA	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	1.50
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 2007 by purpose and program type.

Figure B1: Ex-Im Bank Transactions by Purpose, 2007

	No Private Sector Finance Available		Meet Competition		Not Identified	
	(\$MM)	(#)	(\$MM)	(#)	(\$MM)	(#)
Working capital guarantees	\$805	336	\$0	0	\$0	0
Short-term insurance	\$3,343	1,963	\$0	0	\$0	0
Medium-term insurance	\$80	65	\$172	123	\$0	0
Guarantees	\$1,993	83	\$5,636	123	\$0	0
Loans	\$0	0	\$0	0	\$0	0
TOTAL	\$6,221	2,447	\$5,809	246	\$0	0

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 G-7 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 G-7 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 2007 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 2007. In total, 61 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 36%. The response rate for lenders was higher than for exporters, with 45% of lenders responding and 28% of exporters responding.

Figure C1: Survey Response Rate, 2007

	Lenders	Exporters	Total
Number surveyed	29	32	61
Number responded	13	9	22
Response rate (%)	45	28	36

- **Lenders**

Figure C2 shows the lender experience levels for both length of time in business and experience in export finance. A majority of lenders (62%) have been in business for over 21 years or more while the remainder (38%) have been in business from 4 to 10 years. Years of experience in export finance showed that 38% were relatively new to the business (5 had 1 to 10 years), while the small majority (62%) had over 11-plus years of experience in export finance.

Figure C2: Lender Experience Levels, 2007

	1-3 years	4-10 years	11-20 years	21+ years
Time in business	0	5	0	8
Time in export finance	1	4	2	6

Figure C3 shows the volume of export credits extended during 2007. Slightly more than half (54%) reported having extended \$50 million or less during 2007, while the remaining 31% 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 are focused more on mid-sized export transactions and are regional (as opposed to money-center) banks.

Figure C3: Volume of Lenders' Annual Export Credits, 2007

	Under \$10 million	\$10 - \$50 million	\$51 - \$100 million	\$101 - \$500 million	\$501 million - \$1 billion	Over \$1 billion
Number of Lenders	3	4	1	1	0	2

Figure C4 shows the percentage of lenders' export credits extended during 2007 that were supported by Ex-Im Bank. Eleven of the 13 lenders indicated their volumes for 2007. Of these, 64% of the lenders noted that 75% their export credits had Ex-Im Bank support, while the other 36% reported that 50% or less 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, 2007

	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	3	1	0	7

Of the lenders that responded to the question (11), all noted that the lack of useful private sector financing was the reason for pursuing Ex-Im Bank financing and that this need was worldwide. Five of the 11 lenders who responded stated that Ex-Im Bank support was needed to meet competition from foreign companies receiving ECA financing, with Euler-Hermes cited as the most frequent ECA with whom they had competed. Other ECAs cited on a slightly less frequent basis were EDC, SACE, COFACE and JBIC, as well as a number of non-G-7 ECAs that included Finnvera, Atradius/Netherlands, ONDD/Belgium, China and Korea Eximbank.

- **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 exporter who reported being in business for 11-20 years, all of the other exporters had been in business for 21 years or more, and of these, 75% had been exporting for 21 years or more.

Figure C5: Exporter Experience Levels, 2007

	1-3 years	4-10 years	11-20 years	21+ years
Time in business	0	0	1	7
Time in exporting	0	2	0	6

Figure C6 shows the size of exporters based on sales and export sales volume. Six of the 7 exporters who reported sales figures showed 2007 sales volumes of \$1 billion or greater. All of the 6 exporters with sales of over \$1 billion also reported the same volume of export sales.

Figure C6: Volume of Exporter Annual Sales and Exports, 2007

	Under \$10 million	\$10 - \$50 million	\$51 - \$100 million	\$101 - \$500 million	\$501 million - \$1 billion	Over \$1 billion
Total sales volume	0	0	0	0	1	6
Total export sales volume	0	1	0	0	0	6

Figure C7 shows the distribution of exporters by the percentage of export sales that were supported by Ex-Im Bank. Of the 5 companies who responded, 2 showed that Ex-Im Bank support comprised less than 10% of their export sales while the remaining 3 indicated that Ex-Im Bank supported from 10% to 50% of their sales.

Figure C7: Percentage of Exporters' Sales That Were Ex-Im Bank Supported, 2007

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

All of the exporters except one reported facing regular competition from foreign companies supported by their national ECAs throughout 2007. The most frequently identified competitor ECAs (in descending order) were Euler-Hermes and COFACE, with the remaining ECAs identified equally as frequently with one another.

Working with Other ECAs

Two exporters noted that they had never worked with another ECA, whereas one exporter explained that it worked regularly with every G-7 ECA as well as a number of other ECAs (e.g., Atradius/Netherlands, ONDD/Belgium, Korea Eximbank, Ashra/Israel, CESCE/Spain, and GIEK/Norway). With the exception of the Japanese ECAs, all of the other G-7 ECAs were cited at least once as a regular partner and cited at the same level.

Frequent partners identified by the lenders were all of the G-7 ECAs, led by Euler-Hermes. Non-G-7 ECAs cited as partners were Korea Eximbank, Atradius, Finnvera, ONDD, and private insurers.

Appendix D: G-7 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.”
- France** ▪ **Compagnie Française d’Assurance pour le Commerce Extérieur (COFACE)** is a private insurance company that provides, in addition to short-term insurance that goes on its own book, 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 on its own account, according to standard market practices.
- **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. KfW also administers the provision of German tied aid funds. The decision as to where and how tied aid should be used rests with an inter-ministerial committee. At the end of 2003, KfW announced that the majority of its export credit business would be spun off into an independent, 100%-owned subsidiary called KfW IPEX-Bank (with this spin-off to be finalized by 2008). KfW will offer trade and export credit support on a limited basis: in a syndicate for less risky markets and on its own only in the riskiest markets. In addition, the new entity will offer project finance and will carry an AA- rating.

- Italy**
- **SACE**, or Servizi Assicurativi del Commercio Estero, provides official export credit insurance. Pursuant to 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 and short-term insurance on 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.
- 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, investment, and import credits. Beginning in May 2007, JBIC falls 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 U.K. government that provides export credit guarantees and interest rate support for medium- and long-term official export credit transactions. ECGD also maintains a “top-up” reinsurance facility with a private insurance company in the event the private sector is unwilling to provide short-term export insurance to a U.K. exporter who wishes to sell a product to a market where official export credit support is customarily available from other countries.

Appendix E: Ex-Im Bank Foreign Content Support for Medium- and Long-Term Transactions Containing Foreign Content in 2007*

Country	Exim Product**	Product/Project	Export Value	Foreign Content Percentage***
AUSTRIA	LG	Large Aircraft	\$95,625,000	14%
AZERBAIJAN	INS	Agricultural Equipment	\$3,119,175	9%
AZERBAIJAN	INS	Agricultural Equipment	\$1,957,571	14%
AZERBAIJAN	LG	Building Construction Equipment	\$7,288,566	16%
BRAZIL	INS	Medical Equipment	\$780,000	12%
BRAZIL	INS	Medical Equipment	\$280,000	6%
BRAZIL	INS	Medical Equipment	\$670,000	10%
BRAZIL	INS	Printing machinery Equipment	\$2,375,000	11%
BRAZIL	LG	Construction Equipment	\$3,912,273	32%
BRAZIL	LG	Construction Equipment	\$3,216,304	33%
BRAZIL	LG	Large Aircraft	\$122,292,300	17%
BRAZIL	LG	Large Aircraft	\$30,783,143	17%
BRAZIL	LG	Large Aircraft	\$494,236,706	16%
BRAZIL	LG	Machine Tools	\$484,389	17%
BRAZIL	LG	Medical Equipment	\$2,026,485	17%
BRAZIL	LG	Medical Equipment	\$699,274	17%
BRAZIL	LG	Medical Equipment	\$614,550	7%
BRAZIL	LG	Medical Equipment	\$484,814	6%
BRAZIL	LG	Metal Manufacturing Equipment	\$822,091	5%
BRAZIL	LG	Small Aircraft	\$1,956,636	32%
CANADA	LG	Large Aircraft	\$616,361,091	15%
CANADA	LG	Large Aircraft	\$105,939,918	17%
CANADA	LG	Large Aircraft	\$35,588,200	17%
CANADA	LG	Large Aircraft	\$107,973,341	17%
CHILE	LG	Large Aircraft	\$63,240,000	9%
CHINA	LG	Medical Equipment	\$4,464,037	8%
COLOMBIA	INS	Construction Equipment	\$510,000	28%
COSTA RICA	LG	Construction Equipment	\$1,245,645	8%
DOMINICAN REPUB	LG	Construction Equipment	\$411,756	26%
DOMINICAN REPUB	LG	Construction Equipment	\$946,777	25%
DOMINICAN REPUB	LG	Mining Machinery	\$314,026	17%
DOMINICAN REPUBLIC	INS	Construction and Mining Equipment	\$3,000,000	10%
DOMINICAN REPUBLIC	INS	Medical Equipment	\$402,240	10%
DOMINICAN REPUBLIC	INS	Medical Equipment	\$313,738	7%
GERMANY	LG	Agricultural Equipment	\$1,134,030	15%
GERMANY	LG	Large Aircraft	\$49,279,931	25%
GHANA	LG	Gas Equipment	\$109,533,785	7%
INDIA	LG	Food Production Equipment	\$647,300	14%
INDIA	LG	Industrial Machinery	\$500,000,000	9%

Country	Exim Product**	Product/Project	Export Value	Foreign Content Percentage***
INDIA	LG	Large Aircraft	\$173,804,260	17%
INDIA	LG	Large Aircraft	\$203,126,625	13%
INDIA	LG	Large Aircraft	\$419,177,161	13%
INDIA	LG	Machine Tools	\$1,840,872	38%
IRELAND	LG	Large Aircraft	\$224,565,750	17%
IRELAND	LG	Large Aircraft	\$393,975,000	17%
ISRAEL	INS	Industrial Machinery Equipment	\$2,500,000	15%
ISRAEL	LG	Large Aircraft	\$175,175,330	13%
KAZAKHSTAN	LG	Agricultural Equipment	\$1,878,626	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$7,607,712	14%
KAZAKHSTAN	LG	Agricultural Equipment	\$9,431,048	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$13,627,625	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$608,900	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$14,416,000	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$14,422,800	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$16,231,770	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$14,122,349	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$13,954,826	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$18,035,300	16%
KAZAKHSTAN	LG	Automated Teller Machines	\$15,826,743	11%
KAZAKHSTAN	LG	Telecommunication Equipment	\$4,525,561	12%
MEXICO	INS	Agricultural Equipment	\$630,021	3%
MEXICO	INS	Agricultural Equipment	\$478,669	3%
MEXICO	INS	Agricultural Equipment	\$231,000	2%
MEXICO	INS	Computer Programming Software	\$1,199,303	12%
MEXICO	INS	Construction and Mining Equipment	\$475,000	10%
MEXICO	INS	Construction Equipment	\$1,170,000	10%
MEXICO	INS	Construction Equipment	\$886,800	8%
MEXICO	INS	Construction Equipment	\$924,000	4%
MEXICO	INS	Construction Equipment	\$886,800	8%
MEXICO	INS	Medical Equipment	\$341,176	8%
MEXICO	INS	Medical Equipment	\$1,233,709	10%
MEXICO	INS	Medical Equipment	\$624,834	8%
MEXICO	INS	Nuclear Power Generators	\$686,470	11%
MEXICO	INS	Printing Machinery Equipment	\$5,486,000	10%
MEXICO	INS	Printing Machinery Equipment	\$363,221	10%
MEXICO	LG	Construction Equipment	\$992,260	5%
MEXICO	LG	Construction Equipment	\$1,166,120	21%
MEXICO	LG	Dairy Manufacturing Equipment	\$1,886,923	15%
MEXICO	LG	Highway Billboard Structures	\$519,078	12%
MEXICO	LG	Industrial Machinery	\$158,795	19%
MEXICO	LG	Industrial Machinery	\$200,000,000	7%
MEXICO	LG	Machine Tool Equipment	\$522,538	26%
MEXICO	LG	Machine Tools	\$431,208	12%
MEXICO	LG	Oil and Gas Field Machinery	\$113,223,349	7%

Country	Exim Product**	Product/Project	Export Value	Foreign Content Percentage***
MEXICO	LG	Packaging Machinery	\$686,880	20%
MEXICO	LG	Plastic Manufacturing Equipment	\$228,540	12%
MEXICO	LG	Plastics and Rubber Machinery	\$822,035	12%
MEXICO	LG	Railroad Transportation	\$112,255,176	20%
MEXICO	LG	Railroad Transportation	\$80,429,188	17%
MEXICO	LG	Shade Houses	\$644,286	21%
MEXICO	LG	Small Aircraft	\$437,345	3%
MOROCCO	LG	Large Aircraft	\$81,509,789	17%
NIGERIA	LG	Drilling Equipment	\$9,337,522	9%
NIGERIA	LG	Large Aircraft	\$71,823,648	16%
NIGERIA	LG	Oil and Gas Field Machinery	\$14,096,322	6%
NIGERIA	LG	Ship Building Equipment	\$1,631,367	7%
PANAMA	LG	Construction Equipment	\$486,107	2%
PANAMA	LG	Large Aircraft	\$32,325,528	17%
PANAMA	LG	Large Aircraft	\$32,545,599	17%
PERU	INS	Agricultural Equipment	\$175,000	12%
PHILIPPINES	LG	Broadcast Production Equipment	\$7,105,781	47%
RUSSIA	INS	Automated Teller Machines	\$3,180,593	12%
RUSSIA	INS	Automated Teller Machines	\$1,595,847	12%
RUSSIA	LG	Agricultural Equipment	\$3,573,826	19%
RUSSIA	LG	Agricultural Equipment	\$1,362,253	19%
RUSSIA	LG	Agricultural Equipment	\$9,954,376	8%
RUSSIA	LG	Agricultural Equipment	\$2,889,028	7%
RUSSIA	LG	Agricultural Equipment	\$4,942,335	18%
RUSSIA	LG	Agricultural Equipment	\$8,076,294	17%
RUSSIA	LG	Agricultural Equipment	\$17,888,666	15%
RUSSIA	LG	Agricultural Equipment	\$9,760,457	15%
RUSSIA	LG	Agricultural Equipment	\$5,417,725	17%
RUSSIA	LG	Agricultural Equipment	\$5,336,496	15%
RUSSIA	LG	Agricultural Equipment	\$2,517,489	14%
RUSSIA	LG	Agricultural Equipment	\$12,401,588	15%
RUSSIA	LG	Agricultural Equipment	\$11,529,211	15%
RUSSIA	LG	Agricultural Equipment	\$11,425,429	15%
RUSSIA	LG	Agricultural Equipment	\$17,094,924	15%
RUSSIA	LG	Agricultural Equipment	\$10,586,154	15%
SAUDI ARABIA	LG	Construction Equipment	\$9,975,852	16%
SAUDI ARABIA	LG	Petrochemical Project	\$586,649,537	13%
SINGAPORE	LG	Semiconductor Equipment	\$609,733,033	16%
SRI LANKA	INS	Printing Machinery Equipment	\$232,500	5%
SRI LANKA	LG	Steam Turbines	\$23,785,159	11%
THAILAND	INS	Fitness Equipment	\$225,000	10%
TURKEY	LG	Fire Trucks	\$49,561,707	4%
TURKEY	LG	Hospital Equipment	\$183,144	6%
TURKEY	LG	Large Aircraft	\$101,607,029	17%
UK - GIBRALTAR	INS	Automated Teller Machines	\$3,000,000	12%
UK - GIBRALTAR	INS	Printing Machinery Equipment	\$5,000,000	10%

Country	Exim Product**	Product/Project	Export Value	Foreign Content Percentage***
UKRAINE	LG	Agricultural Equipment	\$8,251,054	17%
UKRAINE	LG	Agricultural Equipment	\$5,156,680	15%
UNITED ARAB EMI	LG	Large Aircraft	\$215,730,000	14%
UNITED STATES	LG	Large Aircraft	\$72,666,500	17%
UNITED STATES	LG	Large Aircraft	\$97,934,900	3%
UNITED STATES	LG	Large Aircraft	\$77,919,500	17%
URUGUAY	INS	Construction Equipment	\$1,652,640	4%
TOTAL & AVERAGE			\$6,903,638,666	14%

* Data excludes Credit Guarantee Facilities.

** **INS** stands for insurance and **LG** stands for a loan or guarantee.

*** 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

This appendix sets forth the annual report on tied aid credits, required by Sections 10(G) and 2(b)(1)(A) of the Export-Import Bank Act of 1945, as amended. This appendix first addresses the implementation of the OECD Arrangement rules on tied aid (also known as the Helsinki Package, the Helsinki tied aid rules or the Helsinki Disciplines) during 2007, followed by a discussion of trends in the use of the TACPF through 2007.

Implementation of the OECD Arrangement

Tied aid is concessional financing support provided by donor governments in the form of a grant or a “soft” loan for which procurement by recipient countries is contractually linked to procurement from firms located in (or in some way benefiting the economy of) the donor country (see below for “**Definitions of the Various Types of Aid**”).

In 1991, the Participants to the OECD Arrangement agreed to rules governing the use of tied aid (the Helsinki Package). The Helsinki Package specifically established the following for the provision of tied aid: (1) country eligibility requirements for the provision of tied aid; (2) transparency (notification) requirements for tied aid offers; and (3) project eligibility requirements, along with a mechanism for discussing specific tied aid offers to ensure that the projects conform to the established guidelines. The OECD rules on country and project eligibility basically resulted in two restrictions on the use of tied aid: (1) no tied aid in “rich”¹ countries; and (2) no tied aid for “commercially viable” (CV) projects. In addition, since the mid-1980s, the Arrangement has required that tied aid contain a minimum *concessional* level of 35% as measured with a market-based discount rate².

The tied aid rules went into effect in February 1992. Since that time, the use of tied aid for CV projects (as defined by the OECD) has significantly declined. (For more details and data trends, see Chapter 5A.) In 1997 (and revised in 2005), Participants issued a document known as the “*Ex-ante* Guidance” which compiles the case law of the project-by-project consultations that were held from 1992 through 1996 and then less frequently after that. The case law describes which projects are typically considered to be commercially viable and non-viable (CNV). (See below for further details.)

¹ Gross National Income (GNI) above \$3,465 per annum (based on 2005 data).

² The term “concessional” 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 concessional 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 concessional level of 35%.

Definitions of the Various Types of Aid

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*),³ and the vast majority of it is 100% pure grant (such as from USAID and the Millennium Challenge Corporation). Aid from a donor government to a recipient government normally supports either “general” uses (e.g., balance of payments support) or the purchase of specific goods and/or services (local, donor country and/or third country) necessary for the completion of an investment or specific project. The latter, with the exception of some local purchases, is trade-related aid.

Trade-related aid may be either “tied” or “untied” to procurement from the donor country and can be provided in two forms: grants or credits⁴. However, because grants involve little or no repayment obligations (i.e., no export leverage), they are viewed as having a negligible potential for trade distortions (see below) and are not subject to OECD disciplines other than notification.

Tied aid credits refer to concessional loan financing that is trade-related and contractually conditioned upon the purchase of some or all of the goods and/or services from suppliers in the donor country or a limited number of countries. Note: Concessional loans can be provided as mixed credits which are a combination of an export credit and a grant, or as soft loans, which are long-term export credits offered with very low interest rates. This type of aid falls within the OECD Arrangement rules. Such aid credits may only be provided to eligible countries and for eligible (commercially non-viable) projects. Also, using the Arrangement’s financial measurement methodology, tied aid to developing countries must be at least 35% concessional, and tied aid to least developed countries must be at least 50% concessional.

Untied aid credits refer to concessional loan 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. This form of aid has historically fallen under the purview of the OECD Development Assistance Committee’s (DAC) rules, which differ from the Arrangement rules in that the DAC provides virtually no restrictions on untied aid. However, the Arrangement rules include some basic transparency requirements for untied aid. Therefore, there is a wide gap in multilateral requirements between tied aid – which is regulated – and untied aid – which is not.

³ 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, and results in one half of annual ODA levels having a 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.

⁴ Credits with a concessionality level of 80% or more are viewed as grants and considered to have a negligible potential for trade distortion.

Trade-distorting aid refers to aid credits for which the motivation is largely or significantly connected to promoting the sale of goods from the donor government's country. Because tied aid credits by their nature can be trade-distorting, there are rules to discipline their use. For example, it would be considered trade distorting to provide tied aid credits for projects that can service *commercial* term financing, including standard export credit financing (i.e., CV projects). As a result, the Arrangement prohibits tied aid credits for such projects unless located in an LDC or unless the concessionality level is 80% or greater. The Arrangement also prohibits tied aid to countries with a per capita income level above \$3,595 (again, unless the concessionality level is 80% or greater), because those countries are considered to have ready access to commercial financing and official export credits for all types of projects.

Current Status of the OECD Negotiations on Tied and Untied Aid 2007

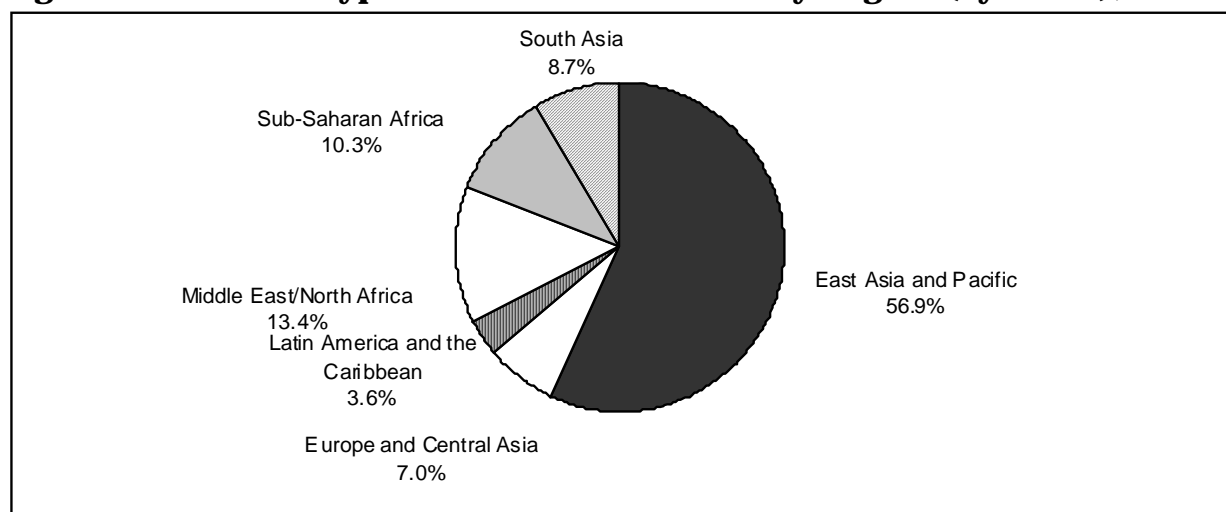
The OECD and the U.S. continue to monitor the effectiveness of the Helsinki tied aid rules that came into effect in early 1992. In 2007, the data showed that there were 127 Helsinki-type tied aid notifications, which was a decline from 140 in the previous year. By value, 2007 Helsinki-tied aid offers totaled \$5.2 billion, which was an increase of 20% from 2006 levels. All available evidence supports the assumption that tied aid has been directed at projects that are considered commercially non-viable and for countries where ECA and commercial sources of financing was either limited or restricted.

With respect to untied aid, in 2006, the Participants agreed to renew for two more years the pilot transparency agreement that they had originally accepted in 2004. In short, the U.S.-proposed agreement requires donors to: (a) make their offers public to allow for competitive international bidding; and, (b) report the nationalities of bid winners on an annual *ex post* basis. It is a means of developing data that would form the basis for future negotiations on extending the tied aid disciplines to untied aid. The transparency agreement represents a compromise between those governments seeking to discipline untied aid (as a way of reducing the potential for trade distortions arising from *de facto tied* untied aid offers) and those donors who believe that untied aid rules are unnecessary and would limit *bona fide* developmental assistance.

By definition, untied aid should be equally accessible to exporters from all countries. However, through influence exerted indirectly (e.g., through lack of transparency, required designs and specifications, promises of additional aid, political pressures, gratitude shown by the recipient, lack of multilateral accountability, etc.), untied aid can become effectively tied, or “*de facto* tied” untied aid.

Participants began implementing the transparency agreement on January 1, 2005, but it is now extended through the end of 2008. (See Chapter 5A for details.)

Figure F1: Helsinki-type Tied Aid Notifications by Region (by Value), 2007



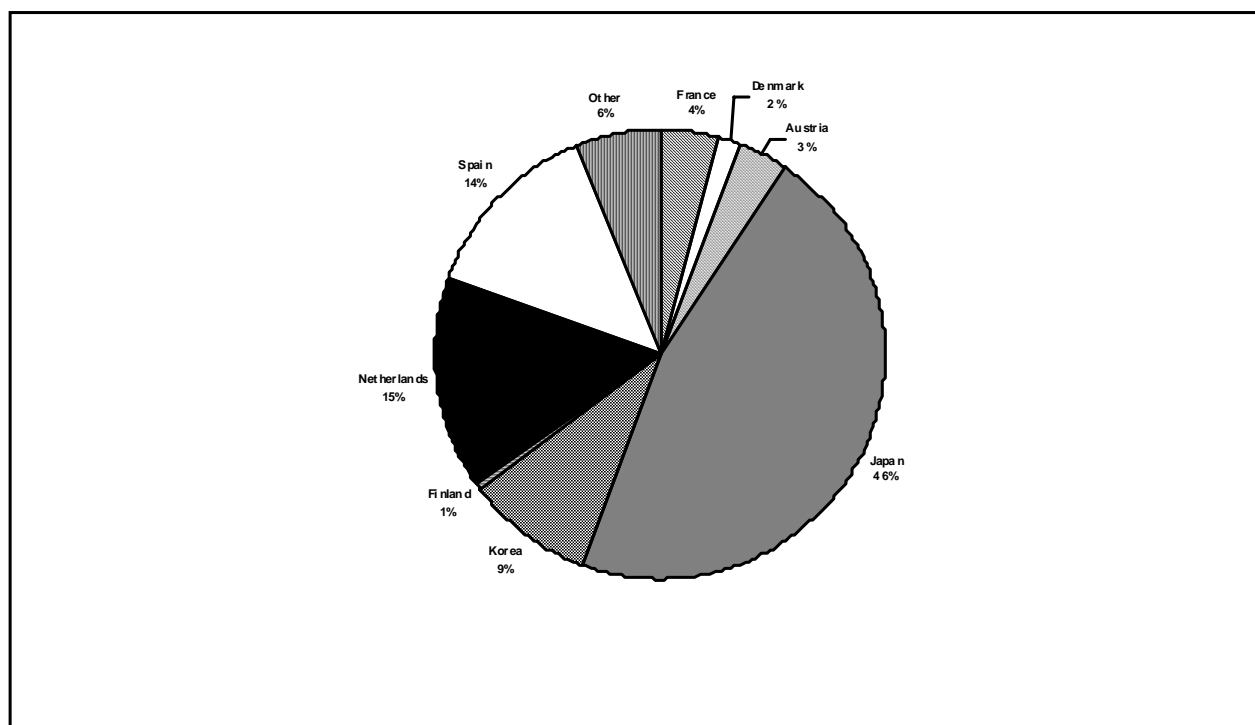
Tied Aid Eligible Markets

The OECD rules designate a number of key markets as ineligible for tied aid financing. Specifically, the Helsinki 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 2007, the major beneficiary region continued to be the East Asia and Pacific region (56.9% of all Helsinki-type tied aid). The most significant recipient – Vietnam – was in this region and was offered \$1.2 billion (or roughly 25% of all Helsinki-type tied aid). The next largest recipient was Thailand with \$950 million. China is back on the scene, having been offered almost \$400 million in tied aid in 2007 -- up 160% over last year. Conversely, tied aid offers to Indonesia fell significantly (about 150% from 2006 levels) to about \$150 million.

Figure F2 shows the variety of donor countries that offered tied aid in 2007. Japan was by far the largest donor country of Helsinki-type tied aid – with the Netherlands, and Spain trailing far behind and by a notable margin. Spanish tied aid continues to decline – albeit by a lesser margin – while Dutch tied aid nearly doubled last year, amounting to almost \$800 million. By comparison the United States did not notify any Helsinki-type tied aid in 2007.

Figure F2: Helsinki-type Tied Aid Notifications by Donor (by value), 2007



Looking at sector concentration, Helsinki-type tied aid in 2007 was concentrated primarily in the transport and storage sectors (principally rail and water transport), and water and health sectors -- all of which tend to be commercially non-viable.

Tied Aid Eligible Projects

The Helsinki Package established the principle that tied aid should not be used for CV projects, which are those that:

- generate operating cash flows sufficient to repay debt obligations on commercial or standard export credit terms [referred to as “financially viable” (FV)]; and,
- could attract standard export credit financing (at least two OECD export credit agencies would be prepared to provide support) which, combined with FV determination, leads to a CV conclusion.

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. One of the goals of the tied aid rules is to keep concessional resources **away** from projects and countries that do not **require** them; otherwise, an unnecessary subsidy is being introduced and trade distortion is occurring.

Trends in the Use of the TACPF

Ex-Im Bank, in consultation with Treasury, has established guidelines for the use of the 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 U.S. 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 continue to work collaboratively to develop Tied Aid Procedures that would guide the application processing in an efficient manner.

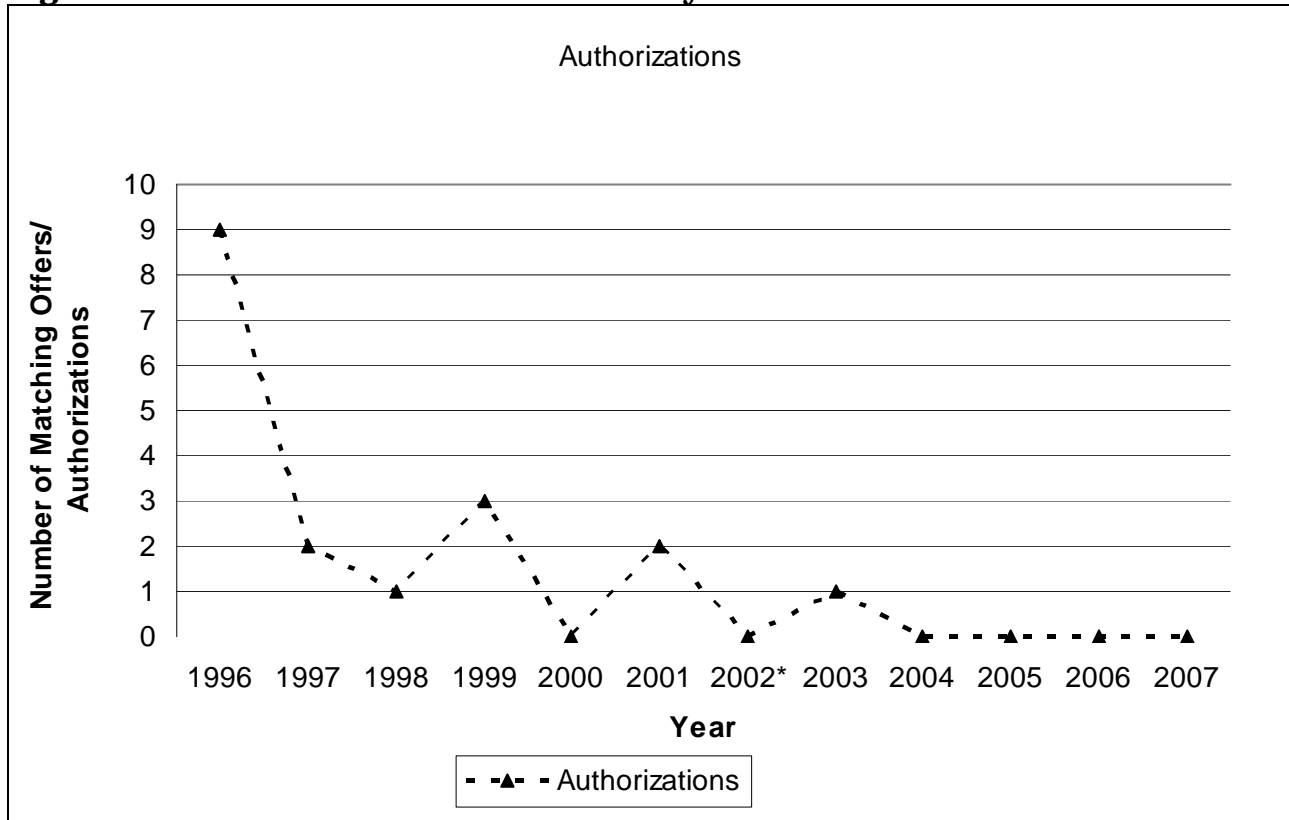
Ex-Im Bank has issued 3 tied aid matching offers since 2003, with the most recent one in 2007. **Figure F3** shows cumulative offers since 1992, and compares the offers and outcomes from the years 1992-2002 to the past five years, i.e., 2003-2007 period. The period-to-period comparison shows a dramatic drop-off in the number of tied aid offers. Since 2003, Ex-Im Bank has matched three cases (compared to 43 in the years 1992-2001); of these three cases, the U.S. lost one and the other two cases remain outstanding with no decision. In 2007, Ex-Im Bank extended an existing tied aid offer and issued one new tied aid Willingness-to-Match offer.

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

	2003	2004	2005	2006	2007	1992-2002	2003-2007
New matching offers	1	0	0	1	1	43	3
U.S. win	19	19	19	19	0	19	0
U.S. loss	24	24	24	24	0	24	1
Outstanding, no decision	1	1	1	1	2	3	2
Cumulative total	44	44	44	45	46	43	3

As shown in **Figures F3 and F4**, the pace of Ex-Im Bank tied aid matching activity has slowed dramatically in recent years with the number of tied aid authorizations showing a similar downward trend and no authorizations in 2007. This tracks with a sharp increase in compliance with the tied aid rules as evidenced by a reduction in the annual average number of tied aid consultations, from 23 per year over 1992-1996 to fewer than 3 per year over 1997-2007.

Figure F4: U.S. Tied Aid Authorizations by Year



No Aid Common Lines

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 U.S. 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 U.S. proposed no aid common line occurred in 2005, for rail cars (locomotive sales) to Indonesia. Although the common line was rejected, the U.S. exporter presented evidence of competitor offers and documented the possibility of follow-on sales on commercial terms. Accordingly, in 2006, Ex-Im Bank issued a tied aid Willingness to Match offer to the U.S. exporter and extended this offer again in 2007. 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, U.S. 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.

Key Markets Where Tied Aid is Prohibited	
Americas*	Argentina, Belize, Mexico, Panama, Uruguay, Venezuela
Asia*	Hong Kong (China), Korea, Malaysia, Singapore
Middle East*	Bahrain, Israel, Kuwait, Lebanon, Oman, Qatar, Saudi Arabia, Turkey, United Arab Emirates
Africa*	Botswana, Gabon, South Africa
Eastern Europe	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 "try to avoid 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.

Appendix F Annex 2

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

Note: In addition to OECD tied aid eligibility, additional U.S. Government criteria are applied to transactions to determine whether tied aid can be made available (e.g., follow on sales criteria and “dynamic market” evaluation).

Appendix F Annex 3

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

Appendix F Annex 4

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

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.

In the latest renewal of Ex-Im Bank’s Charter, Congress asked the Bank to evaluate whether there is an accountability function within the Bank to ensure compliance with environmental, social, labor, human rights and transparency standards. The Bank ensures accountability for these issues through its due diligence processes, which include consultations with the State Department and other agencies on significant transactions and vetting for human rights abuses. In FY 2008, Ex-Im Bank will report to Congress about the Bank’s compliance with these standards.

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 U.S. 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 U.S. 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 U.S. 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 U.S. insurance companies are not allowed equal access, a more formalized procedure would be created. As of December 2007, Ex-Im Bank had not identified any long-term transaction in which U.S. 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" (NES). This report is compiled by the Trade Promotion Coordinating Committee (TPCC). Its purpose is to outline the Administration's trade promotion agenda.

The TPCC is an interagency committee comprised of 19 U.S. government agencies¹. It was established by the Export Enhancement Act of 1992 to harmonize U.S. government export promotion activity under the leadership of the Secretary of Commerce. The President and Chairman of Ex-Im Bank serves as the Vice-Chair of the TPCC.

The NES report emphasizes the value of coordination among relevant U.S. Government agencies and the private sector to strategically involve the U.S. business community in target markets and to maximize U.S. export potential. Achievements stemming from TPCC action that concerned Ex-Im Bank in 2007 are summarized below.

Highlights of TPCC Accomplishments during 2007

Highlights of Ex-Im Bank-related issues contained in the 2007 NES report include the following.

- Small business initiatives, where Ex-Im Bank's focus was twofold.
 - (1) 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 2007, these efforts yielded noteworthy results:
 - Ex-Im Bank authorizations of \$3.4 billion (or 26.7% of total authorizations) in direct support of small businesses.
 - Ex-Im Bank approval of 2,390 transactions (or 85.6 of the total number of transactions) for the direct benefit of small business exporters.
 - Of these small businesses, 369 were first-time users of Ex-Im Bank programs.

¹ Members of the TPCC are: U.S. Departments of Commerce (Chair), State, Treasury, Agriculture, Defense, Energy, Transportation, Interior, Labor, the Overseas Private Investment Corporation, Ex-Im Bank, U.S. Agency for International Development, Small Business Administration, U.S. Trade and Development Agency, U.S. Trade Representative, Environmental Protection Agency, the Council of Economic Advisors, National Economic Council and the Office of Management and Budget.

- (2) The implementation of Ex-Im Online, an interactive, internet-based application system that provides exporters with a fast, easy application process and the ability to monitor the status of applications.
- Emerging and/or New Generation Markets, with a particular focus on the following countries.
 - (1) **China**, where Ex-Im Bank signed two bilateral agreements designed to expedite financing for transactions that will help support U.S. export jobs and promote China's sustainable development. These agreements consisted of (a) a memorandum of understanding on a form of standard Long-Term Credit Agreement for transactions valued over \$20 million; and (b) a framework for expediting financing support for medical equipment sales from the U.S. to hospitals in China.
 - (2) **India**, where Ex-Im Bank is currently pursuing an infrastructure initiative to maximize opportunities for U.S. exporters to bid on major projects including power, oil and gas, refineries, LNG, renewable energy, rail, airports, aircraft, water treatment systems and telecom. During 2007, Ex-Im Bank supported transactions to various sectors in India, including the petroleum refining, aircraft and various manufacturing sectors.
 - (3) **Turkey**, where in 2007 Ex-Im Bank supported the aircraft, fire fighting vehicles, medical equipment and a host of other manufacturing sectors.

A summary of G-7 ECA support in these three markets in 2007 is reflected in **Figure II**.

Figure II: G-7 ECA Medium- and Long-Term Activity in Select Markets, 2007 (\$Mn)

	China	India	Turkey
G-7*	\$ 10,085	\$ 4,330	\$ 3,165
U.S.	\$ 5 (<.1%)**	\$ 1,415 (33%)	\$ 170 (5%)

* Includes medium- and long-term officially supported export credits by ECAs in Canada, France, Germany, Italy, Japan, U.K., and U.S.

** Values in parentheses represent the U.S. (Ex-Im Bank) percentage of total G-7 medium- and long-term support to the country.

In China, the three dominant providers of G-7 ECA medium- and long-term export credits in 2007 were France, Japan and Germany. In India, all G-7 ECAs actively supported transactions in 2007, but the U.S. and Japan were responsible for the bulk of G-7 ECA medium- and long-term activity. In Turkey, Germany provided more than twice as much medium- and long-term support as did any other G-7 ECA in 2007.

Appendix J: Efforts to Promote Renewable Energy

In Ex-Im Bank's 2006 reauthorization process, Congress maintained in Ex-Im Bank's Charter the requirement to report on efforts to promote renewable energy exports. During 2007, Ex-Im Bank responded to the Congressional mandate in a variety of ways.

Under the leadership of the Ex-Im Bank Vice Chairman and Vice President, Linda Conlin, Ex-Im Bank established the Office of Renewable Energy and Environmental Exports in 2007 to coordinate on-going efforts to increase its financing for U.S. renewable energy exports and exports of environmentally beneficial goods and services. In addition, Ex-Im Bank enhanced its marketing efforts to expand awareness of the extended repayment terms (up to 15 years) available under the OECD Special Financial Terms and Conditions for Renewable Energies and Water Projects¹ that went into effect on July 1, 2005, and were extended in July 2007 for an additional three years.

In FY 2007 Ex-Im Bank authorized approximately \$2.6 million in export credit insurance transactions that supported U.S. renewable energy exports, consisting of equipment for solar and wind energy projects as well as geothermal plants. This insurance support exceeds the amount provided in each of the past three fiscal years.

Further, Vice Chairman Conlin continued to lead an inter-divisional Environmental Exports Team (EET). The EET met throughout the year to ensure Bank-wide coordination and contribution to the Ex-Im Bank renewable energy promotion efforts. As a result, staff made presentations, organized panels, and participated in a number of outreach and marketing events intended to promote renewable energy exports. The most important efforts include the following.

- In March, 2007, Vice Chairman Conlin led a team of staff members who participated in the PowerGen Renewable Energy Conference in Las Vegas, NV and supported U.S. Commercial Service match-making sessions held to familiarize foreign buyers with U.S exporters of renewable energy technologies.
- In June 2007, Ex-Im Bank hosted a seminar on "Financing International Sales for Environmental & Renewable Energy Technology" in concert with the New Mexico Department of Economic Development.
- In October 2007, Ex-Im Bank, in partnership with The Port of Los Angeles and East West Bank, hosted an environmental and renewable energy conference in San Pedro, CA, titled: "Starting Local, Going Global: Financial Solutions for Environmental Exporters."

¹ Hydro power projects are also eligible for up to 15-year repayment terms provided that the projects "in all respects meet the requirements of the relevant aspects of all World Bank Group Safeguard Policies...[recognizing] the value of the relevant aspects of other international sources of guidance, such as the draft sustainability guidelines produced by the International Hydropower Association and the Core Values and Strategic Priorities of the World Commission on Dams report."

- Vice Chair Conlin and staff participated in a round-table discussion at a conference hosted by Silicon Valley Bank entitled “What’s Next for Cleantech?: a Public Policy and Private Sector Discussion,” in Santa Clara, California.

Finally, as part of a continuing effort to showcase environmental success stories, Gunderboom, Inc. was named Ex-Im Bank’s Environmental Exporter of the Year in 2007. Headquartered in Anchorage, Alaska, Gunderboom provides marine construction and specialty dredging equipment and services, among other product lines. With Ex-Im Bank’s support, Gunderboom will use their patented filtration technology to minimize sediment exposure and environmental damage to the Panama Canal and surrounding bodies of water.