

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, 2006 THROUGH DECEMBER 31, 2006**

JUNE 2007



JAMES H. LAMBRIGHT
CHAIRMAN AND PRESIDENT

EXPORT-IMPORT BANK
OF THE UNITED STATES

June 29, 2007

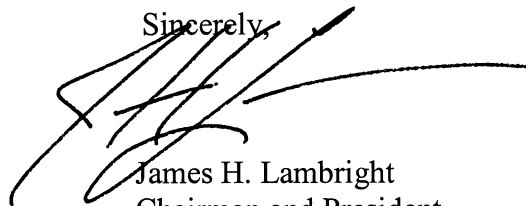
The Honorable Christopher J. Dodd
Chairman
Committee on Banking, Housing and Urban Affairs
United States Senate
534 Dirksen Senate Office Building
Washington, DC 20510

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

Dear Chairman Dodd and Chairman Frank:

Pursuant to Section 2(b)(1)(A) of the Export-Import Bank Act of 1945, as amended, I am pleased to submit the Competitiveness Report for the period January 1, 2006 through December 31, 2006.

Sincerely,



James H. Lambright
Chairman and President



EXPORT-IMPORT BANK
OF THE UNITED STATES

Honorable Christopher J. Dodd, Chairman
Honorable Richard C. Shelby, Ranking Member
U.S. Senate Banking, Housing and Urban Affairs Cmt.

Honorable Barney Frank, Chairman
Honorable Spencer Bachus, Ranking Member
U.S. House of Representatives Financial Services Cmt.

Gentlemen,

We members of the Board of Directors at the Bank are most appreciative to the U.S. Congress for having specifically provided in the Bank's recent re-authorization an opportunity to add our comments on the findings presented in the 2006 Report to the U.S. Congress on export credit competition and the U.S. Export-Import Bank.

In doing so, we wish to begin by clearly stating our endorsement of the Report as prepared by the professional staff at the Bank and reviewed by the Congressionally mandated U.S. Export-Import Bank Advisory Committee. While we are concerned the overall rating of A-/B+ is less than the A the Bank has always received since the rating process was established in 2002, we believe the rating to be accurate.

Through this letter, it is our intent to focus attention at what we hear virtually on a daily basis from the U.S. business community are the primary factors that impact the Bank's ability to provide competitive financing for U.S. exports: economic impact restrictions, international agreements, foreign currency restrictions, co-financing concerns, and perhaps more than any other factor, content requirements. We are respectful that in each of the issues cited there are public policy objectives that are broader than exclusively export finance.

It is our belief that, given the reality of dynamic changes in the global marketplace and the U.S. Export-Import Bank's leadership role in supporting U.S. jobs, a focus of attention for both the Bank and public policy makers should be how to affirmatively address these changes and complex challenges within the context of U.S. Government policy generally and the Bank's mission specifically. Absent such an effort, we are concerned that the value and relevance that U.S. Ex-Im Bank has traditionally provided will diminish at the expense of U.S. exporters and U.S. jobs.

It is our intent over the next few months to begin a dialogue among stakeholders so as to better understand if refinements of current policies might be advantageous and, if so, what those refinements should be. Please be assured we will keep you advised of our efforts as we welcome your advice and counsel.

James H. Lambright, Chairman/President
Linda Conlin, First Vice President/Vice Chair

Senator Max Cleland
Member

J. Joseph Grandmaison
Member

Bijan R. Kian
Member

**THE 2007 ADVISORY COMMITTEE'S STATEMENT ON THE
2006 COMPETITIVENESS REPORT OF
THE EXPORT-IMPORT BANK OF THE UNITED STATES**

The members of the 2007 Advisory Committee have reviewed the 2006 Competitiveness Report to Congress and hereby present our statement on the competitiveness of the Export-Import Bank of the U.S. as compared with the other G-7 major export credit agencies (ECAs). In a majority of Advisory Committee members' opinion, while Ex-Im Bank is still competitive in the basic financial parameters of its typical support, the rapidly changing focus of other ECAs has begun what appears to be a long-term deterioration in the Bank's competitiveness in several of the policy and programmatic elements. Thus, a significant majority of the Advisory Committee agrees with the findings of the Report that Ex-Im Bank has slipped to a level of competitiveness in which Ex-Im Bank is not consistently leveling the playing field for the constituency it serves.

With regard to the Report's structure, methodology and approach, the Advisory Committee offers the following comments:

- We believe that Ex-Im Bank's broadening of the scope of the evaluation of its competitiveness by assessing a variety of directly related elements including its analysis of the changing form and function of ECAs is appropriate as a means to determine its relative success.
- The majority of the Advisory Committee fully supports the continued use of the "report card" analysis and presentation as it succinctly captures a balanced assessment of the Bank's overall competitiveness as well as for the individual programs, policies and practices. However, two members raised concerns regarding the Report's examination of the public policy issues.
- With regard to the comments from other agencies, a majority of Advisory Committee members note that these agencies are neither charged with the responsibility of participating in Ex-Im's Report nor do they have the benefit of the Bank's study, analysis, expert experience and day-to-day involvement with export credits and the specific issues addressed. To this end, the majority of the Advisory Committee considers the other agencies' statements in the Report to not only be inaccurate but also quite illustrative of the obstacles faced by Ex-Im Bank in its attempt to evolve so that is consistently competitive with other major ECAs.

With regard to the specific findings of the Report, a significant majority of the Advisory Committee concurs with the overall assessment that Ex-Im Bank has become less competitive by maintaining its traditional approaches while other ECAs have continually evolved. Therefore, Ex-Im Bank needs to promptly address the specific areas of deficiency in order to reclaim its status as a consistently competitive ECA.

There are several gaps that the Advisory Committee believes are the most critical. First, is the disparity between the level of risk that the private market and other ECAs are willing and able to assume and the Bank's interpretation of the mandate to find a

reasonable assurance of repayment. In this regard, the Advisory Committee appreciates the importance of the Bank's WTO responsibilities, but respectfully asserts that increasing to the next level on the risk scale would not compromise these obligations, and at the same time, doing so would open up more opportunities for the U.S. exporting community.

Another area of widening difference regards foreign currency lending and its increasing importance as a financing option, especially without the requirement for crystallization. Other ECAs are clearly more open to considering eliminating the need for conversion when it involves major trading currencies and are increasingly willing to consider the case-by-case appropriateness of such lending in major emerging market currencies.

The third issue revolves around ways in which Ex-Im Bank can enhance the competitiveness of its content policies without inappropriately diminishing its core "made in" philosophy. The influence of globalization on production options has moved other ECAs operating within very differently structured systems to fundamentally alter their mission goals of exports/employment connection. The challenge for Ex-Im Bank is to achieve similar relevance to the demands of globalization without changing its mission and goals and the export/employment connection.

Further, as briefly noted above, the Advisory Committee appreciates the descriptions and implications arising out of the "New ECA Competitiveness Framework" chapter. Almost all of the members also found the information to be enlightening, capturing the distinctions in philosophy and approach very precisely, raising many thought-provoking questions, and helping to frame the competitive landscape in a forward-thinking manner. Finally, a significant majority of the Advisory Committee applauds Ex-Im Bank in its ability to connect the present and future relevance of long-term trends to current and prospective competitiveness. To this end, the Advisory Committee encourages the continuation of this type of thoughtful thinking and analysis for future reports.

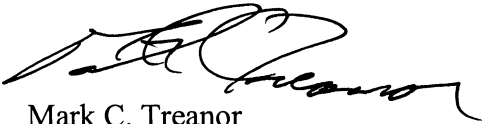
Finally, the Advisory Committee would like to acknowledge Ex-Im Bank's success in increasing its support for small business exporters during FY 2006 and by exceeding its Congressionally mandated set-aside for direct financing support aimed at small business. Small businesses represent a linchpin of economic stability and U.S. export growth; Ex-Im Bank's demonstrated commitment to this critical segment of the U. S. exporting community carries immense value and importance for U.S. exports and U.S. jobs.

Based on our assessment of Ex-Im Bank's findings, the Advisory Committee makes the following recommendations, some of which bear repeating from last year's Report.

- Ex-Im Bank should review, and where appropriate revise and enhance the Bank's key programs and policies related to co-financing, foreign/local currency financing, and the Bank's attitude toward risk assumption.
- Ex-Im Bank should explore the means by which its support can enhance opportunities for exports made in the U.S.

- Ex-Im should continue to track and analyze the international landscape including highly competitive non-G-7 ECAs for emerging trends and issues so that Ex-Im Bank is aware of and can address the competitive implications of these trends.

In summary, the Advisory Committee would like to acknowledge Ex-Im Bank's thorough, thoughtful and candid assessment of its competitiveness contained in the 2006 Annual Competitiveness Report to Congress. A significant majority of the Advisory Committee members believe that it presents a fair and balanced assessment of the state of Ex-Im Bank's position in the ECA world, and serves as a critical reminder that Ex-Im Bank needs to rise to the challenges that lie ahead as noted in this Report by developing new and creative approaches, and rise to them very soon.



Mark C. Treanor
Chairman
2007 Ex-Im Bank Advisory Committee



EXPORT-IMPORT BANK
OF THE UNITED STATES

The members of the U.S. Export-Import Bank's sub-Saharan Advisory Committee appreciate the opportunity to offer comments on the 2006 Competitiveness Report and respectfully ask that our concerns be included in the Report to the U.S. Congress. We agree with the analysis in the Report and with the competitiveness rating of A-/B+. Our comments aim to add value by focusing on specific areas where we believe U.S. companies face particular disadvantages in the African marketplace.

In developing countries, including sub-Sahara Africa, it is not unusual for there to be private sector entities that enjoy a stronger credit rating than the government of that country. However, within the OECD fee system, there is no fee below "sovereign". Therefore, OECD ECAs are non-competitive with non-OECD ECAs in doing business with those companies. A realistic credit evaluation process needs to be created within the OECD to correct this policy inconsistency.

In light of the "aid" realities on the ground in sub-Sahara Africa, most notably free reign 'export credits with aid' practices of non-OECD ECAs and the targeted use of aid, or untied aid generally by OECD ECAs, the current rigidly defined USG policy regarding the use of Ex-Im's War Chest is virtually useless. This policy, particularly for developing countries, needs to be re-considered given the disproportionate negative impact on U.S. exports. Also, as stated in the Competitiveness Report, U.S. Ex-Im Bank is slower than its counterparts in reopening in difficult markets.

The February 2004 U.S. Government one-year "New Lending Moratorium" directive relative to non-concessional lending to countries that complete a multilateral debt reduction clearly discriminates against U.S. companies. In practice, a one-year plus advantage is being given to our economic competitors who have no such restriction.

With foreign/local currency lending an increasing reality in today's world, the rigidly defensive USG requirement for crystallization (converting the foreign currency into U.S. dollars should a transaction default) clearly compromises the competitiveness of U.S. Ex-Im Bank vis a vis their ECA counterparts.

Our observations lead us to believe the greatest competitive challenges for Ex-Im Bank are relative to its non-OECD counterparts. True competitiveness will require encouraging these institutions to conform to the constraints of the OECD practices and fee agreements.

Willene Johnson, Chair
Export-Import Bank of the United States
Sub-Saharan Africa Advisory Committee

2006 Competitiveness Report

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Executive Summary

The 2006 Competitiveness Report provides a comprehensive assessment of the competitiveness of the Export-Import Bank of the United States (Ex-Im Bank) regarding its medium- and long-term export credit programs as compared to the G-7 official export credit agencies (ECAs) and with reference to other large ECAs during calendar year 2006. This assessment is based upon information gathered from a number of sources, including a survey of, and focus group meetings held with, exporters and lenders that used Ex-Im Bank's programs during 2006. The evaluation also uses data from the Organization of Economic and Cooperative Development (OECD), the World Trade Organization (WTO), and the G-7 ECAs in reaching its findings.

This year's report is presented in the same general format as last year's report. Part I contains the assessments of Ex-Im Bank's core programs and policies, Part II is the Emerging Issues section, and Part III contains the Appendices.

In the ECA world of the last 30 years, Ex-Im Bank and its G-7 counterparts have operated with a generally shared philosophy regarding the role of ECAs as "lenders or insurers of last resort." ECAs traditionally fill gaps in the market that the private sector is not willing or able to meet. At the same time, ECAs need to ensure that they are not taking unreasonable risks with taxpayer funds. However, some of the other G-7 ECAs, to varying degrees, are undertaking an evolution that has as its underpinnings a fundamental change in philosophy whereby their programs, policies and operational approaches are more reflective of private sector organizations than of government agencies.

This Report focuses more specifically on the new competitive equation noted above and draws upon the trend identified in the 2005 Report relating to the changing nature of ECAs. In particular, more ECAs are evolving away from the traditional "lender of last resort" model and evolving toward "quasi market participants" with greater independence and flexibility focused on "national benefit." One illustrative example of this movement is the adoption of the "made by vs. made in" approach as it pertains to national content.

The implications of this paradigm shift for ECAs as it concerns Ex-Im Bank have the potential to materially affect Ex-Im Bank's overall competitiveness in the years to come. In fact, the first signs may already be appearing. Specifically, for 2006, the aggregate competitiveness rating is an A-/B+. This rating is the first time since ratings were introduced in 2002 that the overall rating was less than an A.

Agency Comments:

"However, it should be noted that most of the Executive Branch agencies that reviewed this report believe that an A-/B+ is an overly pessimistic grade and under-represents Ex-Im Bank's actual competitiveness vis-a-vis the other G-7 ECAs." [Statement submitted by the Departments of Treasury, 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 2006. Further, in late 2006, Ex-Im Bank's Charter was reauthorized by the U.S. Congress and includes eight new requirements (listed below) to be incorporated into the Bank's Annual Competitiveness Report to Congress. Ex-Im Bank has included four of the eight requirements in this year's Report (noted below). The remaining four requirements could not be incorporated because the preparation of the Report had already begun and it was not possible to evaluate the feasibility or establish the types of data collection and procedures necessary to meet these other requirements and still meet the statutory deadline of June 30.

Included in the 2006 Report:

Renewable Energy: Analysis comparing the level of credit extended for Renewable Energy projects with previous year levels.

Co-financing: Comparison of co-financing programs offered among the major ECAs, including a list of countries with whom Ex-Im has agreements and explanations as to why some ECAs are not on the list.

Ex-Im Bank Board of Directors: Ex-Im Board members' comments on the findings of the Report.

Non-OECD Member Countries: Expansion of analysis to include countries in competition with Ex-Im Bank whose governments are not members of the OECD Arrangement (e.g., China).

To Be Addressed in the Future (to the extent possible):

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.

Services Export Support: Description of Ex-Im Bank support for services exports and a comparison with our major ECA counterparts.

Non-conformance with OECD Arrangement: Detailed information on cases reported to the Bank that appears 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.

ECA Activities Not Consistent with the 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.

Scope

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 that 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.

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. The purpose of this approach is to evaluate each of the essential components of an Ex-Im Bank financial program and to compare these results with the capabilities of our 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 our 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 them 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 our ECA counterparts.

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. exporting 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 in competition supported by official export finance 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 provided 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 were 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 had space to provide qualitative comments on each of their responses. Finally, the Bank continued its practice of distributing the survey to respondents over the internet and allowing them to complete and submit their survey to Ex-Im Bank in the same manner. Recipients could also complete and return the survey either by mail or facsimile if the internet option was not available or desirable. By using the 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 conducted a careful process to evaluate 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. Additional responses were discarded if they 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. Appendix C provides specific information regarding the survey.

Focus Groups

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 provided a venue for members of the export community to supplement their survey responses with anecdotal experience, as well as more comprehensive information on market trends. The results of these discussions are included in the “Exporter and Lender Survey Results” section of each chapter.

Other Comments

In addition to the Ex-Im Bank Board of Directors' comments noted above, there are two other sources of comments to this year's Report. Specifically, Ex-Im Bank's Sub-Saharan Africa Advisory Committee has submitted comments relative to their particular interests, and several U.S. government agencies also submitted comments that appear in selected locations in the Report.

Structure of the Report

This year's report follows the same structure as was used in last year's report and proceeds as follows: the Executive Summary, which precedes Part I, provides an overview of the major findings of the Report, incorporating the standard features with the Emerging Issues, with an overall competitiveness report card grading Ex-Im Bank against its G-7 ECA counterparts. Following the Executive Summary is Part I Chapter 2, which focuses on the international framework within which official ECAs operated in 2006 and the philosophies and missions of competing G-7 ECAs. In Part I, Chapters 3 – 6 consist of separate sections evaluating Ex-Im Bank's competitiveness in the core financing elements of official export credit support. Next, the report provides a comparative assessment of how well the financing elements are packaged into major programs (i.e., aircraft, project finance, co-financing and the foreign currency guarantee). Further, the evaluation of competitiveness addresses U.S. economic philosophy and competitiveness regarding tied and untied aid and market windows. Finally, the report evaluates stakeholder considerations embodied in public policies and the long-term competitive implications of these policies on Ex-Im Bank activity.

Part II is entitled "Emerging Issues" and contains a chapter regarding the new framework for G-7 ECAs. The appendices are contained in Part III, follow the body of the Report and include a list of the purposes for Ex-Im Bank support, Ex-Im Bank efforts to support renewable energy, and other materials intended to provide greater detail and insights.

Chapter 2: Competitiveness Framework

Section A: Factors Influencing Export Finance

Introduction

This chapter provides a snapshot of the world in which official ECAs exist. It also identifies trends and the most significant factors and influences that are affecting how ECAs are operating and likely to pursue their objectives in the future.

Over the last 25 years, the world in which ECAs have existed has been fairly stable, requiring relatively minor and infrequent changes to core operating principles and procedures. This predictable environment was largely a function of a global trading system characterized by competition among well known trading partners with few surprises and framed within a set of known and generally accepted international protocols that were designed to ensure a level playing field. Moreover, the line of demarcation between what the private sector was willing and able to finance without ECA support and what the ECAs perceived as their domain was clear, distinct and constant.

After several years of turmoil, it is now clear that the rules, the competitors and the private sector capacities are changing. These changed circumstances have not been lost on most ECAs. Rather, many have already responded by adapting their roles going forward.

Evolving Landscape of Export Finance

Simply put, the export credit industry is in the midst of considerable and fundamental change – change that has stimulated ECAs to be more flexible, efficient and customer friendly while simultaneously working with, around or attempting to change international guidelines to achieve a competitive niche. A manifestation of this change is that the previously well-defined line between the private sector and public ECAs has lost its distinction, where “doing what the private market cannot or will not” has been supplanted with competition with the private sector.

The major export opportunities in the new world are in a few emerging markets where huge investments in new, improved, and much needed infrastructure and energy are taking place. More and more of the financings of these mega projects are being competitively bid by both public and private financiers. Furthermore, emerging market ECAs are competing more with OECD ECAs in the bidding for these projects. The emerging market ECAs are rising in prominence and influence because they are not compelled to follow the international norms adhered to by the OECD ECAs. At the same time, it seems clear that the standing and influence of the WTO in the field of export credits has become more prominent, forcing the ECA world to adjust accordingly.

Other factors at play that are now part of the expanding ECA spectrum stem from the irreversible impact of globalization in the form of improved governance as depicted in

the challenges associated with the environment and global warming, anti-bribery and corruption, and human and labor rights. Simply put, ECAs find themselves challenged by competing pressures from all sides to include financing conditioned on the enforcement of these public policy demands while simultaneously being expected to meet the competitive needs of their corporate customers.

International

Figure 2: World Exports of Goods and Capital Goods, 2000-2006 (US\$ Billion)

	2000	2001	2002	2003	2004	2005	2006*
Exports of Goods							
World	\$6,447	\$6,186	\$6,481	\$7,546	\$9,124	\$10,431	\$11,610
OECD	\$4,264	\$4,104	\$4,245	\$4,885	\$5,766	\$6,750	\$7,410
BRICS	\$332	\$347	\$410	\$541	\$727	\$919	
Rest of World	\$1,851	\$1,635	\$1,826	\$2,120	\$2,631	\$3,281	\$4,200
Exports of Capital Goods							
World	\$2,626	\$2,474	\$2,560	\$2,894	\$3,474	\$3,851	\$4,352
OECD	\$2,015	\$1,896	\$1,919	\$2,147	\$2,504	\$2,919	\$3,328
BRICS	\$101	\$116	\$146	\$210	\$295	\$382	
Rest of World	\$510	\$462	\$495	\$537	\$674	\$549	\$1,024
OECD Exports as % of World Exports							
Goods	66%	66%	65%	65%	63%	65%	64%
Capital Goods	77%	77%	75%	74%	72%	76%	76%
BRICS Exports as % of World Exports							
Goods	5%	6%	6%	7%	8%	9%	
Capital Goods	4%	5%	6%	7%	8%	10%	

Source: WTO On-line Statistics Database

* Preliminary

Figure 2 shows the global exports of goods over the last seven years, with worldwide trade increasing in every year except 2001. Further, the data illustrate the consistently significant role that capital goods exports play in the total export picture, contributing 38% – 40% of the total world exports. The 27 OECD countries have consistently accounted for the bulk of exports – 65% of goods exports and 76% of capital goods exports in 2005. However, since the turn of the century, the 5 countries nicknamed the BRICS (Brazil, Russia, India, China and South Africa) have doubled 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.

Export Financing Trends

Figure 3 shows that new medium- and long-term G-7 official export credit volumes recovered smoothly from the 9/11 slump and recorded steady (5% per year) growth between 2003 and 2006 . On the other hand, the new medium- and long-term official export credit volumes for Brazil, China and India (the three BRICS active in medium- and long-term export credits) nearly doubled during the same time period. As of 2005, Brazil, China and India (B,C,I) supported a volume of exports nearly equal to half the volume supported by the G-7 ECAs. This trend highlights the growing relevance that the BRICS ECAs have to Ex-Im Bank's competitiveness.

Figure 3: G-7 New Medium- and Long-Term Official Export Credit Volumes, 2001-2006 (US\$ Billion)

	2001	2002	2003	2004	2005	2006*
Canada	4.8	4.1	7.0	5.9	6.2	5.3
France	5.6	5.8	5.7	7.7	9.7	9.3
Germany	5.7	5.8	7.8	12.0	14.9	13.3
Italy	1.9	1.8	3.1	5.0	5.2	6.8
Japan	9.2	5.7	11.5	9.0	5.9	5.6
U.K.	3.1	4.7	3.8	3.0	2.8	2.6
U.S.	6.8	7.7	7.7	8.1	8.7	8.6
Total G-7	\$ 37.1	\$ 35.6	\$ 46.6	\$ 50.7	\$ 53.4	\$51.5
U.S. % of G-7	18 %	22 %	17 %	16 %	16 %	17 %
Brazil	1.9	4.0	2.5	2.8	3.4	
China	0.9	5.4	10.1	12.9	18.4	
India	0.7	0.9	1.3	2.0	3.6	
Total B,C,I	\$ 3.5	\$ 10.3	\$ 13.9	\$ 17.7	\$ 25.4	
B,C,I % of G-7	9 %	29 %	30 %	35 %	48 %	

Source: 2001 through 2005: OECD Statistics on Export Credit Activity, except for Brazil, China and India – Annual Report data, and for U.S., Ex-Im Bank data.

* Preliminary.

Figure 4 demonstrates that external capital flows into emerging markets during 2006 continued to play a dominant role in the export finance environment for official ECAs. Overall private capital flows registered at slightly over \$500 billion, roughly equal to 2005 and three 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 2006. Consequently, the data suggest that private sector funding will continue to have a strong influence constraining the level and nature of demand for official ECA lending for the foreseeable future.

Figure 4: Net External Capital Flows into Emerging Markets, 2001-2006 (US\$ Billion)

	2001	2002	2003	2004	2005	2006*
Official Flows						
IFIs**	22.7	6.9	-6.4	-15.0	-40.4	-25.7
Bilateral Creditors	-11.6	-13.3	-13.8	-2.3	-18.1	-22.5
Private Flows						
Equity Investment	148.4	117.6	134.7	195.1	254.5	255.0
Commercial Banks	-26.1	-8.3	26.9	60.8	141.8	143.3
Non-banks	8.2	15.6	67.2	92.9	112.9	103.4
Total	\$ 141.6	\$ 118.5	\$ 208.6	\$ 331.5	\$ 450.7	\$ 453.5

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

* indicates estimated figures

** IFIs – international financial institutions

Trends in 2006: Focus Group Discussions

The exporters and lenders, citing the continuation of globalization, the growth of world trade and in particular capital goods exports in 2006, and abundant liquidity in the world markets, noted that there are many more financing choices from private and public entities. In particular, official ECAs – both OECD and non-OECD – are working strategically and in tandem with their exporting communities in independent and autonomous, customer friendly and effective ways, unfettered by the traditional bureaucracies in order to take advantage of the surge in demand for capital goods exports. Factors that have contributed to this approach are a greater appreciation for the value of exports to their respective economies with governments instituting “industrial” policy, and a “willingness to solve the problems” by granting ECAs the ability to set their own policies and programs so long as they benefit the national economy. Consequently, the traditional line of demarcation between the private and public sector has become ever more blurred with a number of ECAs cooperating with, but more importantly, competing against the private sector.

To complicate the business landscape further, the exporting community explained that a number of ECAs are offering comprehensive packages (similar to the Chinese model) that combine financing for infrastructure build-outs with commercial components/turnkey facilities. As a result, foreign companies are establishing their footprints in markets that effectively preclude competitive bid opportunities well into the future. As one exporter noted, “we don’t even get to try to lose a deal.”

Moreover, exporters and bankers noted that private sources of finance have also expanded in ways that have made previously non-doable deals “doable,” citing the use of risk management techniques such as credit derivatives and establishing a local presence in key markets. Further, private sources of financing can be less costly than ECA financing, when all other factors are equal, and is considered to be more sustainable over the longer term than ever before.

Overarching Trends

In sum, 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 new official competition and a massive influx of private capital to emerging markets. The competitive framework is changing significantly and fundamentally; the rest of the report represents a snapshot of the activities and responses by G-7 ECAs in 2006 as they re-orient themselves to this new world.

Chapter 2: Competitiveness Framework

Section B: ECAs' Mission and Place in Government

The Role of Export Credit Agencies

The traditional purpose of an export credit agency (ECA) has been to finance domestic exports, recognizing that there may be different approaches on how this can be accomplished. Given these varied approaches, there are two frameworks within which a G-7 official ECA may set its strategy to meet its purpose. 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 these 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 and that is the ECA's mission as defined by its sponsoring government. This factor 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 mission. These factors 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 export credit agency. 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 allocated jobs by providing export financing that is competitive with the official export financing support offered by other governments, and over the long-term, to achieve a break-even. The public policy goal of this mandate 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 mandate effectively directs Ex-Im Bank to fill market gaps that the private sector is not willing or able to meet, namely competitive financing (e.g., interest rates and repayment terms) and the ability to assume 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 of 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, but also extends to a review of innovative programs, new guiding principles and the emergence of BRIC ECAs.

Chapter 3: Core Business Policies and Practices

Section A: Cover Policy and Risk-Taking

Introduction

The competitiveness of official ECAs can be evaluated using any number of yardsticks. One traditional measure is whether or not export credit is available in any given market as evidenced by the extent of ECA openness in a particular country, in terms of both breadth of markets 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 number of countries in which it is open, its overall willingness to take risk in those markets in which it is open, and its appetite for non-sovereign business. One factor has had a consistently negative impact on Ex-Im Bank's high-level of competitiveness in this area – the existence of economic sanctions leveled on countries that might otherwise be creditworthy. However, over the past 5 years, Ex-Im Bank's customers have seen a decline (from 12 in 2001 to 8¹ in 2006) in the number of countries for which they could not receive Ex-Im Bank support because of U.S. legislative restrictions.

Meanwhile, Ex-Im Bank still remains one of the top ECAs in terms of number of countries in which it is open and its appetite for small- and medium-sized corporate borrowers. In 2006, Ex-Im Bank supported medium- and long-term transactions, excluding large aircraft transactions, in 29 different countries around the world. Further, Ex-Im Bank's distribution of medium- and long-term risks taken in 2006, excluding large aircraft transactions, was 7% sovereign and public sector transactions and 93% private sector transactions, by number of transactions. Of the 93% private sector transactions, nearly all of them (84% of the medium- and long-term risks taken) were with non-financial institutions and un-rated borrowers. Ex-Im Bank's competitive advantage in this area stems from an underwriting philosophy focused on transaction risks, not portfolio concentrations. Therefore, unlike many of the other ECAs, Ex-Im Bank has neither country nor sector ceilings in its cover policy.

G-7 ECAs' Policies and Practices

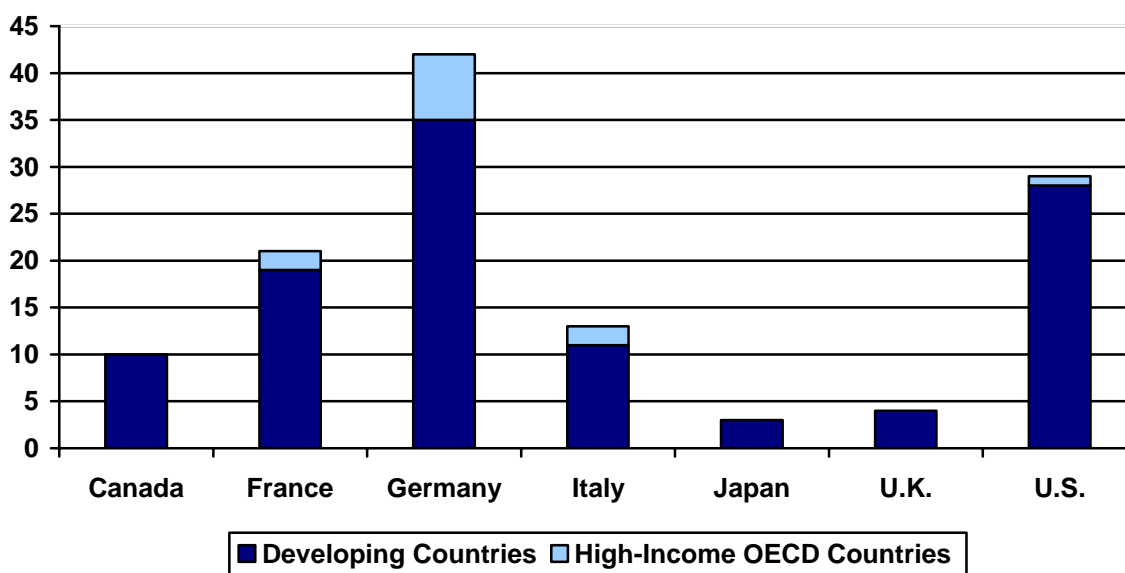
Among the G-7 ECAs, Germany and France take risks across a broad spectrum of countries. As shown in **Figure 5**, in 2006 Germany supported medium- and long-term

¹ In 2006, Ex-Im Bank had legislative restrictions to providing support to the following countries: Burma, Cambodia, Cuba, Iran, North Korea, Laos, Sudan and Syria.

non-aircraft transactions in 42 different countries while France was similarly active in 21 different countries.

Unlike the United States, it is rare for the other G-7 governments to impose sanctions on export credit business. As a result, Iran continued to be an active market for G-7 ECAs in 2006, while Ex-Im Bank maintained its long-standing prohibition of support in Iran. Another interesting trend is the increase in G-7 ECA support for transactions in high-income OECD countries, particularly by the German and Italian ECAs. As discussed in Chapter 8, many ECAs are focused on achieving a balanced portfolio of risks and are therefore taking risks in developed countries as a way of balancing out riskier transactions.

Figure 5: Number of Countries in 2006 In Which G-7 ECAs Supported Non-Aircraft Medium- and Long-Term Transactions²

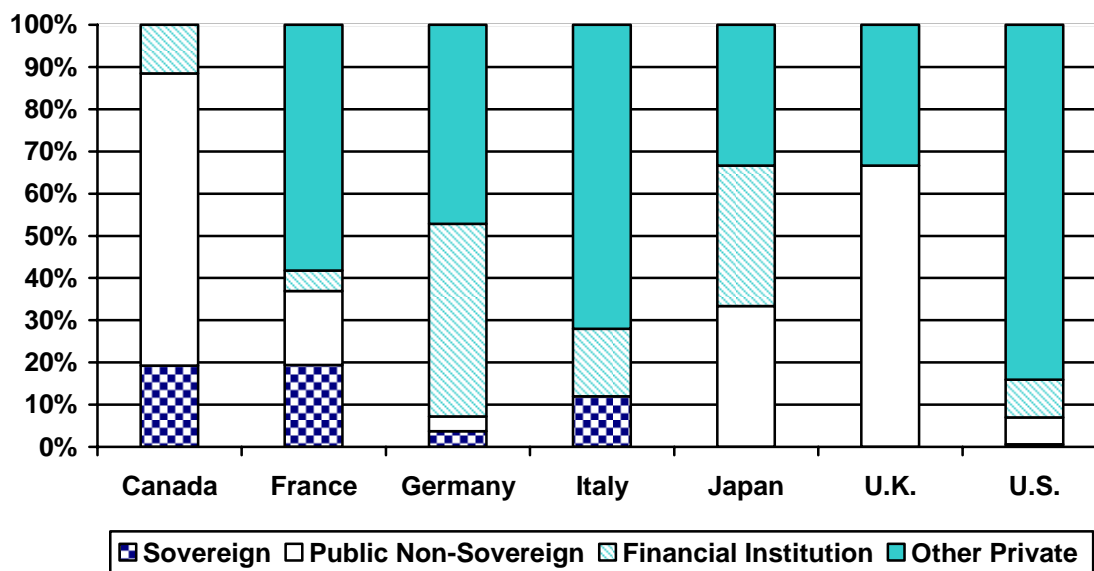


As first noted in 2005, the G-7 ECAs are taking an increasing number of private sector risk transactions, as a percentage of the number of medium- and long-term non-aircraft transactions supported. This trend continued in 2006 with only Canada and the U.K. supporting more public sector transactions than private sector. Germany and the U.S. had the highest percentages of private sector transactions (93% each), however nearly half of the private sector transactions supported by Germany were with financial institutions – generally considered to be less risky than most private companies. (See **Figure 6** on the next page.) Interestingly, some of the non-G7 ECAs are more aggressive in taking the riskier private sector transactions. For example, Sweden only

² This is preliminary information based on transactions reported to OECD members in 2006. Canada only reports those transactions which are subject to the OECD Arrangement (i.e., non-market window transactions) and Japan and Italy have not yet reported all of their 2006 transactions.

supported private sector transactions in 2006, while Spain was very active with small, risky private buyers in Mexico.

Figure 6: Distribution of Medium- and Long-Term Risks Taken by G-7 ECAs in 2006, Excluding Project Finance and Large Aircraft Transactions ²



Export and Lender Survey Results

In 2006, the exporters and lenders continued to comment on their perception that other ECAs have become more competitive in terms of breadth of cover availability. As one lender noted, “other ECAs [. . .] are quicker to reopen in difficult markets” than Ex-Im Bank. The lender cited a deal lost to Germany because of the relative slowness in Ex-Im Bank changing its cover policy in Argentina. In line with that comment, the data indicate that Ex-Im Bank has dropped to second in terms of “breadth of cover availability”. However, the data also indicate that Ex-Im Bank is still, by a narrow margin, the most aggressive ECA in terms of appetite for private sector, non-bank borrowers.

Conclusion

Similar to the findings in 2005, in 2006 Ex-Im Bank is generally competitive in its cover policy vis-à-vis the other ECAs, although its overall grade is edging close to a downgrade. The grades for both depth of non-sovereign risk and breadth of availability both declined slightly, moving the overall grade from a strong “A” in 2005 to a weak “A” in 2006. Consistent with those grades, the data indicates that the competitive predominance that Ex-Im Bank had with its cover policy in the late 90’s to early 2000’s has given way to a “shared leadership” as the other ECAs begin to catch up with Ex-Im Bank.

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 come together and negotiate the official Arrangement for 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 in the provision of official export credits.

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 loan, or by providing interest make-up support (“IMU”) to a financial institution that agrees to provide a loan to a borrower at the official minimum interest rate. Interest make-up 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. (See **Figure 7.**)

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 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 for the U.S. dollar. The resulting interest rate is roughly equivalent to the U.S. government’s cost of funds for a comparable repayment term plus 100 basis points. 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 sometime during the disbursement and repayment periods or remain floating for the life of the loan. It may be based on Libor, Prime, commercial paper or any other relevant benchmark.

It is Ex-Im Bank's practice to allow the foreign borrower, or the borrower's agent – a commercial bank – to determine what kind of support it wishes 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 United States is in a period of slowly rising interest rates, the demand for a direct loan from Ex-Im Bank has been exceedingly limited. In 2006, Ex-Im Bank approved one direct loan for a total financed amount of nearly \$41 million.

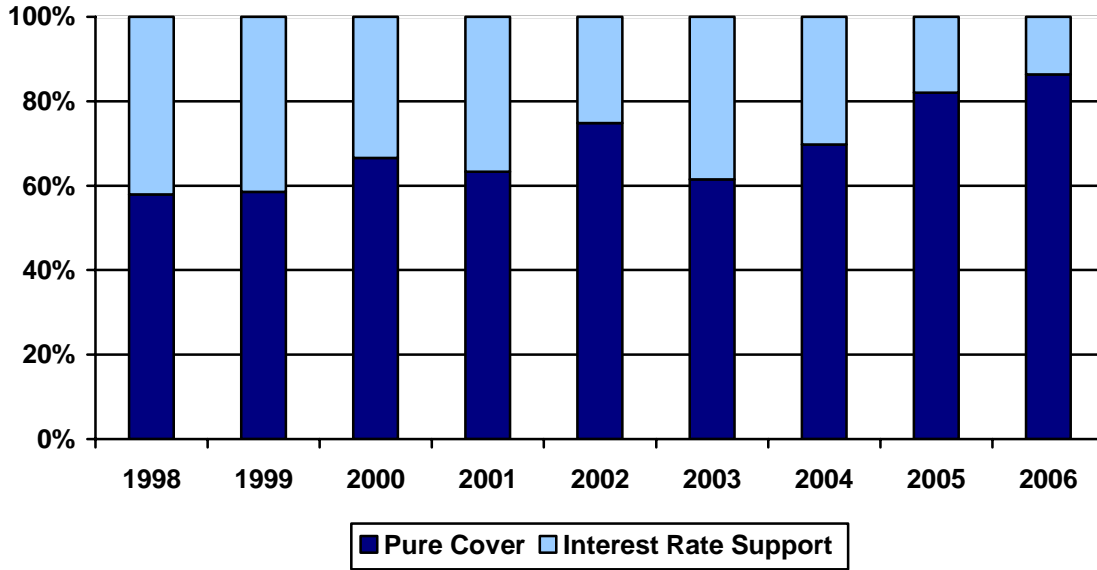
Ex-Im Bank provided medium- and long-term pure cover support in 2006 for 471 transactions with a total financed amount of more than \$7.3 billion. Consistent with previous years, the interest rates on the long-term transactions, which are typically for large dollar amounts, are generally attractive. Specifically, the interest rates achieved on Project Finance transactions are slightly better than can be achieved with the support provided by the other G-7 ECAs, although this pricing benefit is offset by the higher exposure fee that Ex-Im Bank must charge to reflect the "above standard" quality of its guarantee. 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 long-term transactions are also achieving interest rates that are comparable to those achieved with the G-7 ECAs. Interestingly, medium-term transactions supported under Ex-Im Bank's insurance and guarantee programs do not typically achieve attractive rates; the average spread over Libor for medium-term transactions supported in 2006 was more than 170 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.

G-7 ECAs' Policy and Practice

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 United States all offer a direct loan program. France, Italy and the United Kingdom offer IMU support, though the terms of the IMU support differs. Nonetheless, continuing the trend identified in 2004 and 2005, preliminary information indicates that interest rate support continued to decline as a percentage of total ECA support in 2006.

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 (e.g., 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 fee that ECAs charge (see Chapter 3C for more information on how these differences are reflected in the fee). 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 transactions supported by ECAs providing "above standard" cover typically are lower and so, the exposure fees are higher. Conversely, the interest rate on transactions supported by ECAs providing "below standard" cover are typically higher and the exposure fees are lower. In 2006, the interest rates achievable under the other G-7 ECAs' pure cover support seem to range from very low (e.g., Libor + 4 basis points) to quite high (e.g., Libor + 400 basis points), irrespective of what type of pure cover support they provide.

Figure 7: Long-Term Export Credits by Type of Credit (All OECD Member States) ¹



Exporter and Lender Survey Results

None of the survey respondents used the direct loan program in 2006. Instead, the exporting community used Ex-Im Bank's insurance and/or guarantee products, which they found to be generally competitive with the other G-7 ECAs. Accordingly, both the exporters and lenders found that Ex-Im Bank's interest rate support is at a position of "shared lead" with the interest rate support available from the major ECAs.

Conclusion

Ex-Im Bank consistently offers interest rates that are the equal of the average terms of the typical major ECA, even though the exposure fee Ex-Im Bank charges reflects a surcharge for the high quality of Ex-Im Bank's guarantee. Through the direct loan program, Ex-Im Bank provides interest rate support that is competitive with the other G-7 ECAs. In addition, the interest rates achievable under Ex-Im Bank's pure cover program are generally competitive with those of the other G-7 ECAs. So, Ex-Im Bank is generally competitive with the other G-7 ECAs.

¹ Source: 2005 Report on Export Credit Activities. TD/ECG/(2006)21 and data from transactions reported to OECD members in 2006.

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 non-repayment on their financing. In 1999, the OECD adopted the Knaepen Package which defined the elements for the determination of sovereign fees and set Minimum Premium Rates (MPR) for sovereign 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 transactions. These rates also serve as the floor for fees in non-sovereign 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 a conditional insurance; and (iii) and 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 that there is a level playing field among the different 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 their 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, with regard to non-sovereign transactions, there are fairly significant differences in both the risk rating methodologies and pricing by the G-7 ECAs which leads to

a divergence in the fees charged for this borrower class. Many of those differences stem from different underwriting processes, as well as different claims experience, that lead to different ratings and differences in pricing for the same borrower. Within the OECD, there have been ongoing discussions about developing a fee system for non-sovereign buyers. An objective of such a system would be to facilitate similar perceptions of risks so that there may be less disparity in exposure fees charged for similar borrowers. Anecdotally, a recent cursory survey of ECA non-sovereign pricing demonstrated the disparity in non-sovereign fees among ECAs. For example, a medium-term transaction for a Mexican corporate buyer showed a fee range of 1% to close to 60% over the MPR. Another example for a Russian bank showed a range of fees of 0% to over 80% of the MPR—with an average of roughly 25%. Ex-Im Bank is typically on the low end of exposure fees charged to borrowers.

Exporter and Lender Survey Results

The exporting community views Ex-Im Bank's exposure fees for sovereign and non-sovereign risks as generally competitive. In particular, Ex-Im Bank was applauded for its transparency by making its exposure fee calculator available on the internet.

Conclusion

The 1999 Knaepen package gave all OECD members access to a level playing field on premium. 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 around the MPR. As a consequence, in 2006, Ex-Im Bank premium rates are fully competitive with the G-7 ECAs.

Chapter 3: Core Business Policies and Practices

Section D: Ex-Im Bank's Core Competitiveness

Introduction

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 8** illustrates how Ex-Im Bank fared competitively on sub-elements of each policy/practice, in addition to an aggregate grade for each policy/practice. 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 8: Grading of Ex-Im Bank's Core Competitiveness, 2006

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: Comparison of 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.

The United States and the European Community agreed, after three years of negotiation, to the first Large Aircraft Sector Understanding (LASU) in 1985. The benefits of the new LASU were that it established standard financing terms for the provision of export credit support for the sale of large aircraft. In the ensuing twenty plus years, the LASU has worked well for the United States, ensuring that export credits for large aircraft were on a level playing field and that Boeing and Airbus were able to compete on price and quality, not financing terms.

In 2001 negotiations resumed among an expanded list of participants on a new, updated Aircraft Sector Understanding (ASU)¹. The purpose of the negotiations is to ensure a predictable, transparent, and stable source of aircraft finance to airlines in all markets on a "level playing field," to complement (without distorting) the commercial aircraft finance market, and to include new aircraft manufacturing countries in the discussion and implementation of aircraft financing disciplines. To that end, Brazil has joined the U.S., Canada, and the three "Airbus countries" (UK, Germany and France) in direct negotiations, with other interested OECD countries participating as well.

The aircraft manufacturers had another great year in 2006, with a total of 1868 new aircraft orders placed. As illustrated in **Figure 9** below, Boeing had a particularly good year – it surpassed Airbus in total orders for the first time since 2000. Deliveries to foreign buyers continued to be a significant portion of the total delivery book for 2006.

Figure 9: Number of Large Commercial Jet Aircraft Orders, 2002-2006

	2002	2003	2004	2005	2006
Boeing	251	250	277	1002	1044
Airbus	300	284	366	1055	824

¹ With the inclusion of Brazil and Canada in the aircraft discussions, the revised agreement is now being referred to as the ASU, because the discussions no longer include just Large aircraft only.

As noted in **Figure 10**, 57% of Boeing’s deliveries were to foreign buyers and Figure _ shows that 28% of the foreign deliveries were financed by Ex-Im Bank. It was within this context that the United States and European ECAs supported large aircraft export sales in 2006.

Figure 10: Number of Boeing Commercial Jet Aircraft Deliveries, 2002-2006

	2002	2003	2004	2005	2006
Domestic	199	127	142	135	167
Foreign	182	154	143	155	221
Foreign as % of Total	48%	55%	50%	53%	57%

Ex-Im Bank’s Policy and Practice

Like the Arrangement terms that apply to standard export credit financing, the LASU sets out maximum repayment terms and minimum interest rates. Ex-Im Bank is fully competitive within these parameters and in particular, Ex-Im Bank support generates tightly priced interest rates from the 100% principal and interest guarantee. (See **Figure 12** for a comparison of Ex-Im Bank and Airbus ECA financing terms for large aircraft.) 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 and made the necessary declarations. However, as Ex-Im Bank applies more stringent structuring and higher documentation requirements connected to its “reasonable assurance of repayment” and other public policy objectives such as U.S. content requirements, its support for large aircraft export financing generates higher financial costs which it cannot always pass along to borrowers.

In 2006, Ex-Im Bank approved 26 large aircraft transactions worth nearly \$5 billion and covering 84 aircraft. Of those 26 transactions, 6 were co-financing transactions with Japan, Korea or the United Kingdom and 6 were financed in a foreign currency (the Euro, Canadian Dollar and New Zealand Dollar).

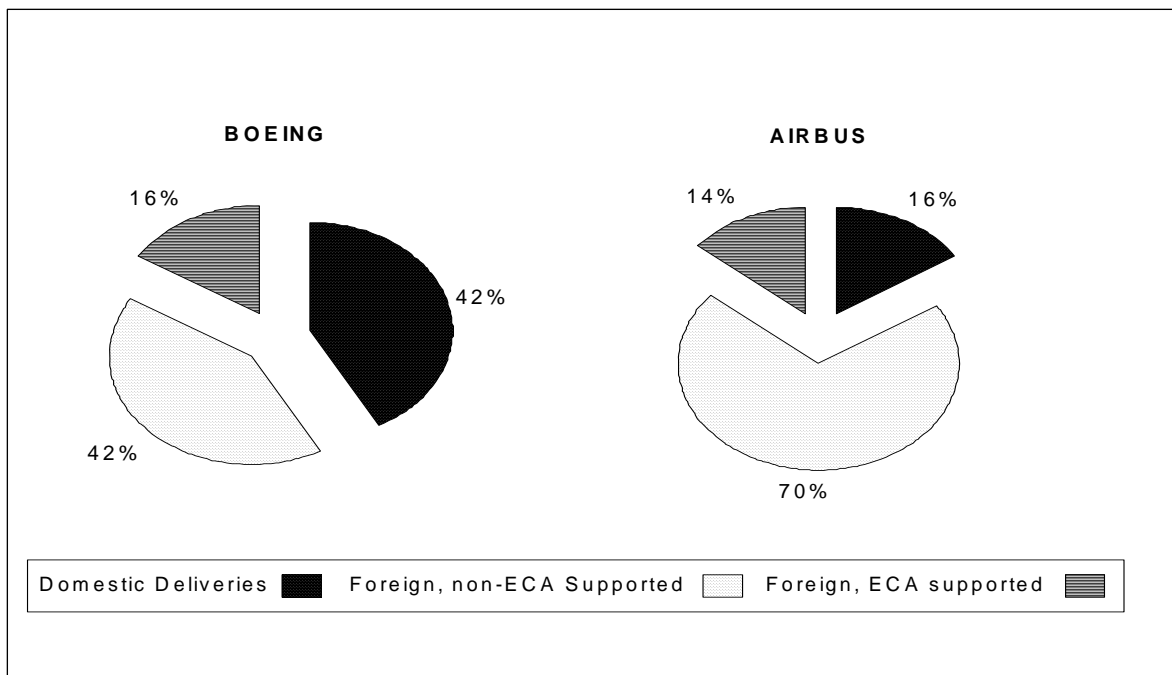
The year 2006 also saw a continuation of Ex-Im Bank’s policy of giving a one-third (1/3) discount to the exposure fee charged an airline if the country in which the airline is based had ratified the Cape Town Convention and made the necessary qualifying

declarations.² The Boeing aircraft purchases by COPA (Panama), TAAG (Angola) and PIA (Pakistan) in 2006 each received the benefit of the Cape Town discount, with a total of \$12.3 billion in authorizations benefiting from the discount since inception. In addition on August 30, 2006, Ex-Im Bank's Board of Directors extended the discount for Cape Town countries until March 31, 2007.³

G-7 ECAs' Policies and Practices

In 2006, the Airbus ECAs supported 60 Airbus aircraft for a total of approximately \$2.75 billion. As illustrated in **Figure 11**, these 60 aircraft represented 14% of all Airbus deliveries in 2006 and 17% of all Airbus foreign deliveries during that time, as compared to Ex-Im Bank's support of 16% of all Boeing deliveries and 28% of all foreign deliveries in 2006.

Figure 11: Percentage of Large Commercial Jet Aircraft Deliveries Financed by ECAs, 2006



² 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 2006: Afghanistan, Angola, Ethiopia, Kenya, Malaysia, Mongolia, Oman, Pakistan, Panama, Senegal and South Africa. Note, Indonesia became eligible for the discount in March 2007.

³ On March 30, 2007 Ex-Im Bank's Board of Directors further extended the discount for Cape Town countries until September 30, 2007.

Like Ex-Im Bank, the Airbus ECAs offer the maximum allowable terms under the LASU. 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 2006, the only currencies they supported were the Euro and the U.S. dollar and they do not offer any discount to airlines based in Cape Town countries.

Figure 12: Aircraft Financing Program Features Available

	Ex-Im Bank	ECGD	Coface	Hermes
LASU Terms:				
Maximum Repayment Terms	12 years	12 years	12 years	12 years
Percentage Cover	100%	100%	100%	100%
Quality of Cover	Above Standard	Above Standard	Above Standard	Above Standard
Interest Rate Support	Direct Loan	Interest Makeup	Interest Makeup	Direct Loan
Special Features:				
Co-Financing	Yes	Limited	Limited	Limited
Foreign Currency	Yes	Limited	Limited	Limited
Cape Town Discount	Yes	No	No	No
Non-financial factors:				
Ease of Use	Average	Very Good	Very Good	Very Good
Risk Capacity	Good	Average	Average	Average

Exporter and Lender Survey Results

Ex-Im Bank received responses from both exporters and banks to its survey on support for large aircraft exports. Overall, the respondents find Ex-Im Bank generally competitive compared to the other ECAs. However, the engine manufacturers believe that Ex-Im Bank's policy of not supporting U.S. engines on Airbus airplanes is a competitive disadvantage for their segment of the industry.

Conclusion

Within the context of the terms allowed under the LASU, 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, Cape Town discounts, 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.

Chapter 4: Comparison of Major Program Structures

Section B: Project Finance

Introduction

Project Finance (or limited recourse project finance) refers to the financing of projects whose creditworthiness depends on the project cash flows for repayment. Under this program structure, the lender has recourse only to the assets and revenue generated by the borrower (i.e., covered project) and cannot access the assets or the revenue of the project sponsor to repay the debt. This structure normally covers relatively large, long-term infrastructure and industrial projects.

In 2006, total Project Finance (PF) debt issuances surged to \$210 billion (an all-time high) up from \$166 billion in 2005—more than a 26% increase. However, the total number of OECD project finance deals notified in 2006 (as required by the OECD Agreement for project finance deals that apply certain modifications to the standard repayment structure) decreased from 20 in 2005 to 15 in 2006. Preliminary information indicates that seven project finance transactions were actually authorized by the OECD ECAs in 2006 (down from 11 transactions in 2005), with contract amounts totaling approximately \$2.7 billion¹.

Figure 13² shows the involvement of ECAs in project finance from 2005 to 2006. Based on dollar volume, ECA participation as a percentage of total PF loans, increased very modestly – from 1.3% in 2005 to 1.4% in 2006. Non-ECA supported PF activity clearly remains dominant over ECA financing due to the continual willingness of providers of capital to extend project financing credit coupled with very liquid markets in 2006.

¹ The ECA project finance deals identified are as reported by the OECD ECAs and may not include all ECA project finance deals completed in 2006. Further, they only include those OECD notifications that became authorized transactions.

² Project Finance International, January 2006. The total volume of ECA project finance deals comes from the OECD the total volume of non-ECA deals comes from Project Finance International. Both sets of numbers exclude brown-field projects and refinancing deals.

Figure 13: Distribution of PF Loans by Originator, 2005 vs. 2006 (US\$ Million)

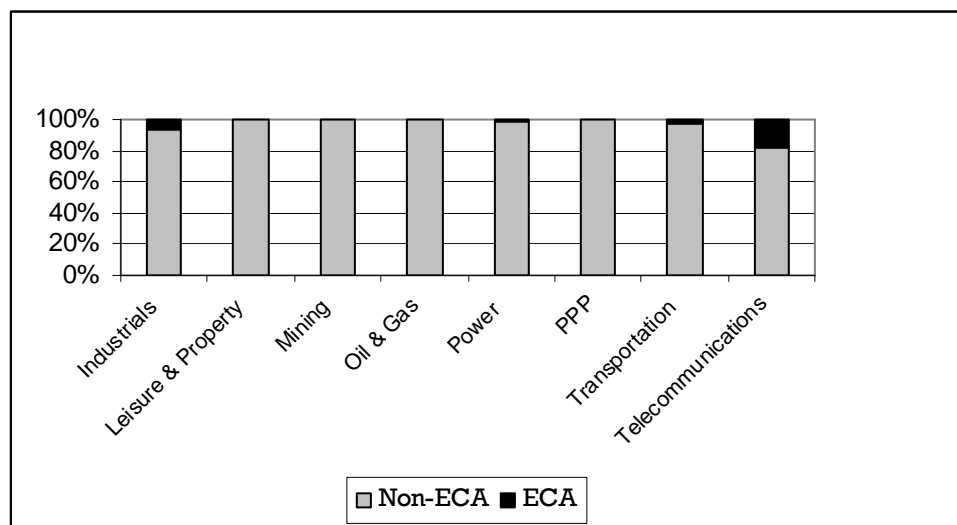
	OECD ECAs	US Ex-Im	All ECAs	Non-ECA	Total
2006	\$2,731	\$0	\$2,731	\$196,233	\$198,964
2005	\$1,674	\$580	\$2,254	\$166,000	\$168,254

Ex-Im Bank’s Policy and Practice

Ex-Im Bank did not authorize any PF transactions in 2006, however there has been a recent blurring of the line between project finance and structured finance. Specifically, traditional project finance transactions create a new company via a special purpose vehicle (SPV) which creates and owns the project as well as acts as the borrower. These transactions rely on repayment from revenue generated from 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. Currently Ex-Im Bank labels these transactions as structured finance. However, in cases where the success of the expansion is integral to the survival of the existing company, the title of Project Finance could just as easily be assumed. In 2006, Ex-Im Bank authorized 9 “hybrid” structured /project finance transactions totaling \$1.3 billion.

While ECA support in PF transactions has historically been relatively small overall, it does have a more important role in certain industries—one reason why ECA support continues to be sought (**See Figure 14**). In particular, the telecommunications and industrial sectors use a relatively larger share of ECA backed PF support than the other six major industry categories. More specifically, current trends also indicate a greater role for ECA support in the petrochemicals industry. Although not obvious from **Figure 14**, ECA support in the oil and gas sectors continues to be sought in those emerging markets that are new entrants to project financing or in markets characterized by a higher degree of political risk than in industrialized markets.

Figure 14: Distribution of PF Loans by Sector, 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 US 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 on Officially Supported Export Credits with respect to pricing and repayment terms, (3) financing of local costs (up to 15% of total financing), (4) availability for capitalization of interest during construction and, (5) Ex-Im Bank's 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 Ex-Im Bank's content policy, shipping requirements, and economic impact analysis (see the Foreign Content, MARAD, and Economic Impact Analysis chapters for more detail). These policies impact potential project finance transactions more than other types of transactions because sourcing options for PF transactions are widely available on world markets and the U.S. does not always have an obvious comparative advantage that helps win contracts for U.S. exporters.

G-7 ECAs' Policies and Practices

G-7 ECAs offer similar coverage for project finance transactions with some differences in the quality of the coverage. For example, Ex-Im Bank and ECGD provide unconditional guarantees, EDC and JBIC provide direct loans, and the other four G-7 ECAs provide conditional insurance. While Ex-Im Bank and ECGD provide a 100% unconditional guarantee cover for political and commercial risks, many other ECAs provide less than 100% cover. Insurer ECAs generally provide between 90% to 95% cover of the political and commercial

risks. (Note: SACE now provides a 100% cover insurance product on a case-by-case basis.) Included in all of the ECAs' cover is support for local costs up to the amount of the down payment (typically 15%) and cover for capitalized interest that accrues during the construction period up to the Starting Point of Credit.

Of note, in 2006 SACE introduced a project bond cover instrument that provides 100% cover (including documentary risk) to issuers of corporate or SPV bonds. The "bond issue cover" is a first demand unconditional and irrevocable guarantee that guards the bond issuer against interest rate risk associated with the proceeds from the bond issue. This product allows borrowers to gain access to lower cost funding, to diversify their funding sources, and access capital markets. SACE's bond issue cover is the first of its kind for ECAs and at least one bond issue has already been covered by SACE.

2006 also marked the OECD's official formalization of the project finance flexibilities. That is, in the latter half of 2005, revised rules for non-standard repayment periods and project finance came into force. In 2006, these rules were permanently integrated into the Project Finance Understanding of the OECD Arrangement. These rules aim to allow member ECAs more flexibility to structure project finance transactions within the OECD framework.

Exporter and Lender Survey Results

Despite the fact that ECA participation in project financings is relatively small, the dollar volume of PF transactions with ECA participation increased marginally in 2006 relative to 2005 and is projected to increase further in 2007 because commercial banks are reaching their maximum lending limits in select markets. However, it is not clear if this pattern will continue because the market is becoming more efficient and taking on risks (both in tenor and in price) more aggressively than ever before. Exporters and lenders rate Ex-Im Bank's project finance program as competitive overall with the caveat that Ex-Im Bank's program has more public policy constraints than other G-7 ECAs.

Conclusion

Overall, Ex-Im Bank's PF program remains generally competitive with those offered by the other G-7 ECAs. Although not considered in the overall grade, an emerging trend is that when public policy constraints are major considerations in a project, the program is often viewed as uncompetitive for that particular project.

Chapter 4: Comparison of Major Program Structures

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

Introduction

“Co-financing” or “reinsurance” addresses the challenges posed by multi-sourcing as they refer to financing arrangements that allow an exporter to market a single ECA financing package to a buyer interested in procuring goods and services from two (or more) countries. Without co-financing, foreign buyers would need multiple financing packages to ensure ECA support for exports from various countries.

The lead ECA provides the applicant (buyer, bank or exporter) with export credit support for the entire transaction. Behind the scenes, the follower ECA provides reinsurance (or a counter-guarantee) to the lead ECA for 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 Co-Financing “One-Stop-Shop” Arrangements

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 Bank has continued to sign co-financing agreements and to approve co-financing arrangements for specific transactions.

During 2006, Ex-Im Bank approved 19 co-financed transactions totaling approximately \$2.7 billion – much of it was aircraft, of which 7 were co-financed with Japan (NEXI); 4 were co-financed with Canada (EDC); 4 were co-financed with the UK (ECGD); 2 were co-financed with the Netherlands (Atradius); 1 was co-financed with Italy (SACE); and 1 was co-financed with Korea (Korea Exim). Of note is that in 2006, all of the co-financing deals were done under existing framework agreements and none were concluded on a one-off basis. (See **Figure 15** for a listing of specific transactions).

Figure 15: Ex-Im Bank "One -Stop- Shop" Co-Finance Transactions in 2006

Ex-Im Bank & Co-Financing ECA	Market	Project	Amount
Atradius: Netherlands	BRAZIL	Medical Equipment	\$1.5 million
Atradius: Netherlands	BRAZIL	Medical Equipment	\$521,000
ECGD: United Kingdom	INDIA	Aircraft	\$11.5 million
ECGD: United Kingdom	NEW ZEALAND	Aircraft	\$126 million
ECGD: United Kingdom	THAILAND	Aircraft	\$484 million
ECGD: United Kingdom	TURKEY	Gas Turbine	\$15.5 million
EDC: Canada	BRAZIL	Ag Equipment	\$957,000
EDC: Canada	MEXICO	Construction Equipment	\$2.2 million
EDC: Canada	BRAZIL	Helicopters	\$872,000
EDC: Canada	MEXICO	Helicopters	\$1.5 million
K-EXIM: Korea	KOREA	Aircraft	\$142 million
NEXI: Japan	CHILE	Aircraft	\$217 million
NEXI: Japan	CHILE	Aircraft	\$70 million
NEXI: Japan	INDIA	Aircraft	\$900 million
NEXI: Japan	KOREA	Aircraft	\$115 million
NEXI: Japan	NETHERLANDS	Aircraft	\$96 million
NEXI: Japan	PAKISTAN	Aircraft	\$464 million
NEXI: Japan	NETHERLANDS	Aircraft	\$95 million
SACE: Italy	MEXICO	Aircraft	\$2.2 million
TOTAL			\$2.7 billion

G-7 ECAs' Policies and Practices

As shown below in **Figure 16**, the G-7 ECAs have signed multiple framework agreements among themselves and have been processing co-financed transactions since 1995. These agreements were originally designed to help European ECAs manage their exposure because many European ECAs 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, EU ECAs 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. It follows, therefore, that co-financing agreements continue to be valuable to European ECAs as an efficient mechanism to deal with increased multi-sourcing and globalization.

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 transactional co-financing requests on a case-by-case basis. However, the same technical issues that have prevented Ex-Im Bank from signing some bilateral framework agreements (e.g., following the lead ECA's claims and recovery practices in the event of a

default and covering contracts in Euro), have led some ECAs to reject Ex-Im Bank requests for co-financing on a one-off basis.

Specifically, Ex-Im Bank has not signed bilateral framework agreements because the Bank is unable to resolve differences with partner ECAs regarding claims and recovery procedures and Euro cover. These technical issues combined with the transactional time constraints needed to develop solutions to structure around these differences have discouraged some exporters or applicants from pursuing co-financing on a one-off basis.

Figure 16: G-7 Co-financing “One-Stop-Shop” Agreements in 2006

	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

U.S. exporters continue to express concerns regarding the possible outsourcing of U.S. production and the growing demands of sophisticated buyers who regard Ex-Im Bank as a foot-dragger with respect to co-financing, and unwilling or unable to sign co-financing agreements with major G7 ECAs. In particular, survey respondents who commented on co-financing indicated that Ex-Im Bank’s lack of signed bilateral agreements makes the co-financing program less competitive than its foreign counterparts who are “continuing to aggressively expand co-financing.” Moreover, exporters argued that to meaningfully meet the competition, Ex-Im Bank “needs to be willing to (really) follow and be more proactive in seeking opportunities to expand agreements.”

Conclusion

The lack of signed bilateral agreements with the major ECAs of Germany and France is the main contributor to the Bank’s disadvantage vis-à-vis foreign export credit agencies and, to that extent, Ex-Im Bank’s co-financing program is less competitive with the programs of most of the other G-7 ECAs. Although transactional circumstances previously allowed Ex-Im Bank to temper the competitive disadvantage resulting from the lack of bilateral framework agreements, in 2006 no one-off co-financing arrangements were concluded. It appears that the same issues constraining the bilateral agreements are now inhibiting one-off deals, leading to an overall down-grading to a B-/C+.

Chapter 4: Comparison of Major Program Structures

Section D: Foreign Currency Guarantees

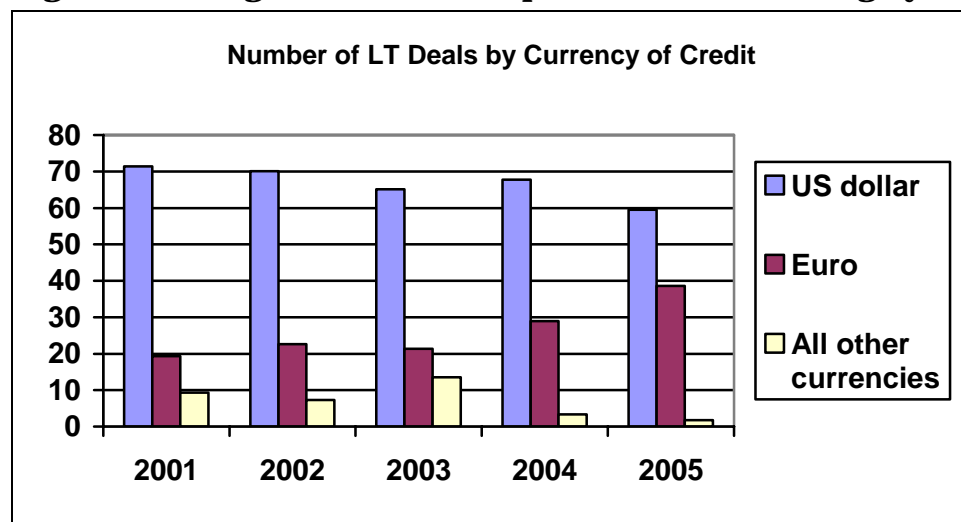
Introduction

Foreign currency financing refers to an export credit covered by an ECA 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 operated robust (i.e., the bulk of their portfolio) foreign currency programs. Today, however, as **Figure 17** shows, the Euro and other currencies are gaining substantial ground vis-à-vis the U.S. dollar. Moreover, emerging market expansion into the global economy and high liquidity in these markets has resulted in borrower demands for export credit cover for soft currency denominated debt. Responding to emerging market interest in soft currency financing over the past five years, many ECAs began offering soft currency cover. Hence, an ECA's ability to provide cover in a currency other than its own is increasingly becoming a competitive issue.

Note that official support for transactions denominated in a foreign currency is not governed by the OECD Arrangement. Each ECA may decide whether (and on what basis) to provide foreign currency cover (i.e., loans, guarantees or insurance) for contracts denominated in a foreign currency and on what terms (e.g., what interest would be covered, whether to crystallize¹ the debt, etc.)

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

Figure 17: Long-Term OECD Export Credit Financing by Currency



Source: 2005 OECD Statistics on Export Credit Activities

¹ Crystallization: the requirement that the depreciation (of the currency) risk must remain with the borrower who will need to pay sufficient local currency to ensure that the costs the ECA has incurred in meeting a soft currency claim are met in full.

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 most widely been used in aircraft financing as it is an attractive way for a borrower (e.g., airline) to reduce the currency volatility of its earnings (when these are not in U.S. dollars) by allowing the borrower to “match fund” i.e., pay off its debt in the currency of its revenue.

Unlike its G-7 counterparts, Ex-Im Bank treats all foreign currency transactions, including hard currencies such as the Euro, with the same policy; that is, 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.³ 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 accelerates the debt, pays the claim in a single lump sum payment and pursues recovery of the entire defaulted amount. (Note: Ex-Im Bank handles its claims process for dollar denominated debt in the same manner regarding acceleration, claim payment, and recovery.)

Ex-Im Bank does have a matching provision that would allow Ex-Im Bank to provide foreign currency (hard or soft) coverage without conversion. Specifically, before any consideration could be given to providing Euro coverage without conversion, Ex-Im Bank would need confirmation that a foreign ECA will provide coverage without conversion for the same transaction for which the U.S. exporter (and Ex-Im Bank applicant) is competing.

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. 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 sought comparable dollar offers to eliminate the potential for a competitive disadvantage that could result from the lower nominal rate associated with a competitor offer.

³ One US exporter reported that the conversion feature in a co-financing transaction resulted in a loss of over \$20 million in U.S. exports to a project in Sri Lanka.

Figure 18 below facilitates a comparison of the policies that affect U.S. exporters and exporters from the other G-7 countries with respect to foreign currency guarantees.

Figure 18: Comparison of G-7 Foreign Currency Guarantees

	U.S. Exporter	G-7 Exporter
Availability of hard currency cover	Automatic availability of hard currency cover	Automatic availability of hard currency cover
Conversion of hard currency debt upon default	Yes	No conversion clause (i.e., debt would not be converted into the G-7 ECA's currency upon default) with payment of a surcharge ranging from 0-10%.
Acceleration of hard currency debt upon default	Yes	No, typically no acceleration of the debt upon default (i.e., borrower would be expected to pay debt according to the original payment schedule except in cases of bankruptcy)

Ex-Im Bank's Foreign Currency Guarantee Activity

In 2006, Ex-Im Bank supported 17 foreign currency transactions valued at more than \$2 billion, in U.S. export value, where the repayment was in a currency other than the U.S. dollar. The majority of foreign currency business was denominated in hard currencies, such as the Euro (12 transactions, with a U.S. export value of \$1.3 billion) and the Canadian dollar (1 transaction, with a U.S. export value of USD \$220 million). In addition, Ex-Im Bank guaranteed the New Zealand dollar (one transaction, valued at USD \$198 million), the Australian dollar (one transaction, valued at USD \$15 million) and the Mexican peso (2 transactions, that resulted in USD \$237 million of US exports). Of the 17 foreign currency guarantee transactions, all but five were on behalf of foreign airlines for aircraft purchases (including one Credit Guarantee Facility to an airline in Mexico denominated in Mexican pesos). The five non-aircraft transactions included four Euro denominated loans for buyers in Lithuania, Russia, Ukraine and Kazakhstan and one denominated in Australian dollars to an Australian buyer.

G-7 ECAs' Policies and Practices

All G-7 ECAs distinguish between two types of foreign currency coverage: *hard currency coverage*, which is readily available and usually at no additional cost compared to domestic currency coverage; and *soft currency coverage*, which is available on a case-by-case and/or currency-by-currency basis and usually results in additional

ECA considerations with respect to the appropriate risks and mitigants that should be brought to bear on the transaction.

Hard Currency Cover: All G-7 ECAs provide support for export credits denominated in hard currencies. However, Ex-Im Bank converts hard currency obligations into U.S. dollars after paying a claim. The other ECAs are 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. The ECAs in Canada (EDC), Italy (SACE), Japan (NEXI), and the UK (ECGD), do not convert the obligation post claim payment because they have the capability to assume and manage the foreign exchange rate risk. The German ECA (Hermes) 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.

Soft Currency Cover: With respect to soft currencies, two types of ECA coverage are generally available: commercial bank guarantees and insurance. ECAs can either accept foreign exchange risk (defined as paying claims and accepting recoveries in the local currency) or “crystallize” the debt (defined as converting the debt obligation into a hard currency obligation after paying a claim or using alternative structuring that protects the ECA from possible shortfalls to its accounts that could result from exchange fluctuations during the recovery phase). As **Figure 19** shows, there is no uniform practice among G-7 ECAs with respect to acceptance of soft currency foreign exchange risk, although some case-by-case experiences are developing.

Figure 19: G7 ECA Foreign Currency Attitude: Willingness to accept Exchange Rate Risk and Activity, 2006

	Exchange Risk Accepted?		Currencies ¹ of Approved Transactions (2001-2006)	
	Hard Currency	Soft Currency	Hard Currency	Soft Currency
EDC	Yes	Case-by-case	USD	none
Coface	Case-by-case	Yes	USD, AUD, JPY	EGP, MXP
Hermes	No, fix rate at time of default, but 10% surcharge lifts cap	Case-by-case	USD, GBP, CHF, AUD, JPY	AED, DOP ²
SACE	Yes	no experience	USD, CHF, GBP, JPY	none
NEXI	Yes	no experience	USD, EUR	none
ECGD	Yes	No, convert obligation to Sterling at time of payment	USD, EUR, JPY	none ³
Ex-Im Bank	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 ⁴

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

Discussions with G-7 ECAs reveal that the interest in ECA support of credits denominated in soft currencies has dropped off in 2006, while cover for Euro denominated debt has soared. Some ECAs reported that requests for soft currency support have been for smaller transactions (which are not systematically reported). Moreover, some ECAs have found that certain local laws prohibit crystallization of the debt or severely restrict an ECA's recovery efforts, thereby rendering conversion of soft currency debt cumbersome and, in some instances, ineffective. ECAs are currently "regrouping" in order to find ways to manage and/or mitigate their risks in the face of legal and practical constraints.

Nevertheless, ECAs continue to demonstrate a willingness to cover soft currencies (with or without a conversion clause) and have generally established a variety of criteria, such as:

- Limiting the transaction size.
- Providing cover for currencies with stable and relatively low interest rates.
- Limiting soft currency cover to borrowers with relatively good credit standings.
- Restricting soft currency cover to transactions with floating interest rates.
- Pricing incremental risk (market-to-market).
- Confirming that the legal regime in the local market is sufficiently developed so as to not interfere with implementation of conversion clauses in the event of a claim.
- Sufficient depth and liquidity in the market so as to enable the ECA to purchase the local currency without impacting its exchange rate.

ECA Activity data

2006 OECD data reveal that long-term export credits offered by OECD countries and denominated in U.S. dollars currently account for 60% of all such long term export credits. This is evidence of a continuing downward trend in terms of U.S. dollar activity, which is down about 10% from 2000 levels. Conversely, a surge in Euro-denominated business by OECD countries is evidenced by the 10% increase in its share of export credit activity since 2005 (i.e., a 10% increase from 28.9% in 2005 to 38.6% in 2006). Local currency financing for longer term export credits (in excess of 5 year repayment terms) has declined significantly – if not vanished -- from ECA activity.

Exporter and Lender Survey Results

U.S. exporters surveyed indicated overall that Ex-Im Bank foreign currency coverage was not on par with that of foreign ECAs because Ex-Im Bank is the only ECA unwilling to provide cover for hard currencies, like the Euro, without conversion into U.S. dollars upon default. Soft currency cover consistently received a lower grade than hard currency cover while exporters pointed generally to limited ECA experience in the area of soft currency cover without conversion, noting that "the emerging local capital markets make the ability to provide local (soft) currency cover a significant competitive factor". Ex-Im Bank support for aircraft transactions denominated in hard currencies

was quite competitive (an A+). Nevertheless, Ex-Im Bank's unwillingness to accept exchange risk (compared to case-by-case approaches taken by most of the major ECAs) yields a B-/C+ grade.

Conclusion

Specialized coverage like that of foreign currencies is increasingly impacting competitiveness in a global environment in which ECAs appear to be continually looking for new ways to gain advantage over one another. Ex-Im Bank's inability to accept exchange rate risk, the result of a more conservative U.S. Government approach compared with other G-7 governments, clearly limits its flexibility vis-à-vis other G-7 ECAs. The inability of Ex-Im Bank to cover surging Euro transactions coupled with the need to confirm comparable foreign competition before accepting exchange rate risk (i.e., no conversion) has proven difficult for exporters as it is rarely known in advance of the export sale negotiations or bidding process which ECAs are competing for the business and what type of currency coverage will be sought. These factors take their toll on Ex-Im Bank competitiveness in this area and, on balance, render a less competitive position than that of last year, or a B.

Chapter 4: Comparison of Major Program Structures

Section E: 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 competitive with its G-7 counterparts. While Ex-Im Bank's aircraft and project finance programs are rated as competitive with our foreign ECA counterparts, the U.S. exporting community graded the co-financing and foreign currency guarantee programs as less than fully competitive. Moreover, they indicated that the relative value of these capabilities had risen due to the increased demand in more markets, and that the current limitations of the programs created more situations in which their lack of comparability made them less competitive. **Figure 20** 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.

Figure 20: Grading of Ex-Im Bank's Major Program Competitiveness, 2006

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
Availability of Soft Cover	A
Accepts Exchange Rate Risk	B-/C+
Pricing	A
Total Average Grade	A-/B+

Ch. 5 Economic Philosophy and Competitiveness

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 not always problematic because it may represent bona fide development assistance that provides critical support for the recipient country. While the USG does not seek to reduce tied aid flows that are for legitimate development purposes, 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 1990, 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 doesn’t provide the recipient country with the best value for their dollar. This can happen when the recipient country doesn’t select the bidder who offered the best price, quality and service for the equipment, but the bidder who offered 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 a subsidy to a recipient country.

USG efforts to discipline tied aid at the OECD have resulted in rules (also known as the Helsinki Disciplines) that have been instrumental in limiting the trade-distorting effects of tied aid, and redirect tied aid flows to bona fide development projects. Since they came into effect in 1992, the OECD tied aid rules have helped

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 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%; whereas 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” refers to projects that can service market- or standard Arrangement term financing over 10-12 years, depending on the type of project.

reduce tied aid to an average of about \$4 billion annually, 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 a year in the mid-1990s. It appeared that Japan was redirecting its tied aid flows into untied aid flows, and offering what was simply “de facto tied” untied aid. (Trade distortions can occur with untied aid through informal understandings or a recipient’s desire to reward the donor by opting to procure from the donor’s country). This led the U.S. to present a series of proposals in the OECD that were geared towards disciplining untied aid similar to the way that tied had 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 United States proposed a pilot transparency agreement for untied aid whereby donors would make their offers public in order to allow for competitive international bidding, and to report the nationalities of bid winners. Specifically, the transparency agreement allows: (1) all OECD Members to access information that will 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, and then 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. By the end of 2008, the transparency agreement may yield sufficiently robust data for analysis.

OECD Tied Aid Rules and Key Definitions

Appendix F provides a more detailed explanation of the various types of tied 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) minimum 35% concessionality; and (3) no tied aid for wealthy countries (those with a gross national income above \$3,465, but the figure usually changes annually because it is based on annual World Bank lending criteria (See Appendix F, Annex 1). The other critical component of the Helsinki Disciplines is that all tied aid must be notified to OECD Members at least 30 business days before the donor can make a commitment to the intended recipient, exporter, or any other party.

OECD Members determine commercial viability on a case-by-case basis. The definition is based on two components: (i) financial viability, which refers to a project's ability to repay market-term financing, or standard ECA financing, over ten to twelve years (depending on the type of project) ; and (ii) the availability of ECA financing for such a project.

If any OECD Member believes that a notified tied aid project could/should be able to service commercial-term financing, then that Member can “challenge” the project's tied aid eligibility. These projects are then discussed in a meeting of the tied aid Consultations Group, and the Group's chairman determines if the project has received the “substantial support” of the Group's members. If so, the project can proceed with tied aid. If not, the project may not receive tied aid.

“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). These types of tied aid are normally not considered to have serious trade-distorting effects and, therefore, are exempt from the Helsinki rules regarding commercial viability, although all tied aid is subject to notification requirements. In addition to notification, stand-alone *de minimis* projects are also subject to minimum concessionality and country eligibility requirements. *De minimis* tied aid can be trade-distorting but, given its small size, does not typically impact the competitive position of U.S. exporters. In any case, the U.S. Government supports automatic matching of *de minimis* tied offers that are made for commercially-viable projects.

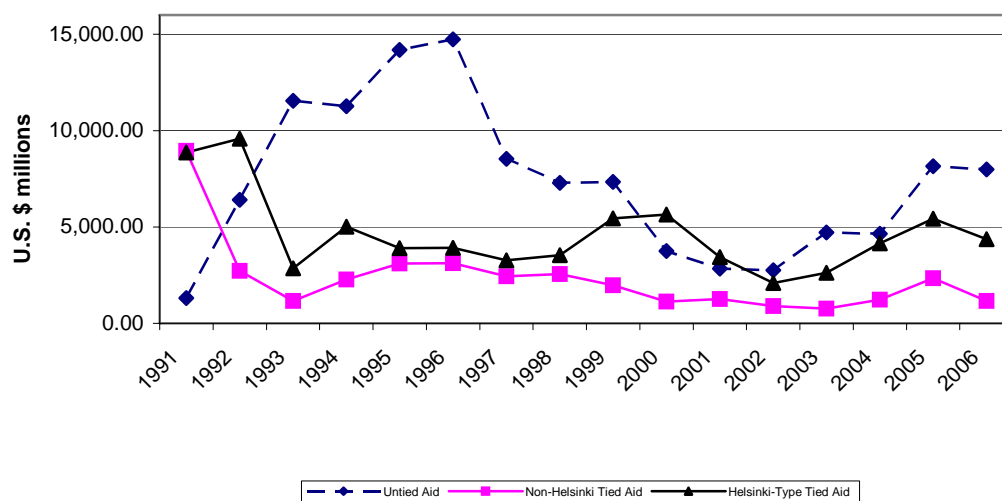
Data

Figure 21 indicates that in 2006, aid of practically every type declined from what appears to have been an aberrant jump in 2005. That is, after nearly doubling in 2005, total aid was down by around 15% in 2006. Nevertheless, in 2006, all categories of aid reported the second highest total since 2000. Helsinki-type tied aid followed the general pattern. After jumping 30% in 2005, Helsinki-type tied aid went down by 20% in 2006. And although the total is the second highest since 2000, two points are critical: (1) the total is still less than it was before the tied aid rules went into effect in 1992; and (2) the composition of tied aid, as it appears that the tied aid that remains represents bona fide development assistance and is not trade-distorting. Untied aid followed a similar pattern, although the percentage change was significantly different. That is, after jumping 75% in 2005, untied aid dropped 2% in 2006. And again, while 2006 was the second highest total since 1997, it was also only about half of its peak in 1996.

While there are too many moving parts to be precise, it appears that the long-term pattern of a few donor and recipient countries are driving the year-to-year changes. Specifically:

- After accounting for almost all of the increase in Helsinki-type tied aid in 2005, Spain accounted for nearly all of the decline in 2006—returning to near typical levels of the last 5-7 years;
- After roughly doubling in 2006, Japan’s untied aid leveled-off in 2006; and
- With total Helsinki-type tied aid of \$146 million in 2006, China seems to be on the cusp of having been the largest recipient in 1995 to being an insignificant recipient by the end of the decade.

Figure 21: Aid Credit Volume by Type, 1991-2006 (US\$ Million)



Note: Consistent untied aid data reporting began in 1994.

Competitive Situation

In 2006, there were no allegations that any of the tied aid offers from G-7 entities failed to comply with the OECD disciplines or were directed at projects in sectors considered to be financially and/or commercially viable (see Appendix F for definitions of financial and commercial viability). During the year, Ex-Im Bank did not authorize any tied aid transactions and therefore did not expend any of the \$227.9 million in the Tied Aid Capital Projects Fund (TACPF). However, Ex-Im Bank did issue (and extend) a Willingness to Match offer to an U.S. exporter competing for tied aid for the sale of locomotives in Indonesia. Moreover, three applications for tied aid were received and the Bank has started the evaluation process. The fact that untied aid levels are about twice that of tied aid indicates the importance in monitoring and evaluating the results of the pilot transparency

agreement, in cooperation with the Treasury and Commerce Departments. Starting next year, this chapter will contain a section reporting these results.

U.S. Government and Ex-Im Bank Policy

The reason USG policy seeks to reduce, and ideally eliminate, trade distorting tied aid is because it:

- Disadvantages U.S. exporters by redirecting business away from those suppliers whose products are superior in quality, price, and service; and
- Closes markets and misallocates both international and developing country resources by sometimes leading to higher contract prices, a capital-intensive development bias, skewed technology choices, and an increased debt burden.

Consistent with long-standing U.S. policy, Ex-Im Bank does not initiate tied aid. Instead, Ex-Im Bank and the U.S. Treasury Department work together to determine whether to match a foreign tied aid offer. (A recent change to Ex-Im Bank's Charter has mandated changes to the inter-agency aspects of the process Ex-Im Bank uses to deal with tied aid cases. This new process will be implemented in 2007.) The decision to match is made on the basis of largely objective criteria to determine if: (1) tied aid would be useful to enforce existing OECD disciplines; or (2) an otherwise OECD-compliant foreign tied aid credit is likely to ensure that future commercial trade with that country, and in that particular sector, will favor donor country firms (a very rare occurrence in recent years). And as mentioned earlier, the U.S. Government supports automatic matching of de minimis tied offers that are made for commercially-viable projects.

Exporter and Lender Survey Results

In 2006, most of the respondents to the survey indicated that they had no experience with tied aid offers from any source. One lender noted that it was difficult to find concrete examples or proof of foreign tied aid offers. Also, a few respondents believe that the increase in framework agreements (which include export credits and concessional components) from China to borrowers in Asian markets make it more difficult for U.S. exporters to identify specific projects endangered by concessional/tied aid funds.

Conclusion

Aid levels (particularly tied aid) were down in 2006 compared to 2005. Tied aid remains below its pre-Helsinki level, and continues to be focused in bona fide development sectors that are appropriate for aid. As in recent years, very little of this aid seems to have been used to compete against U.S. exporters in 2006. Nevertheless, some U.S. exporters of specific goods do episodically encounter

foreign tied aid that competes with commercial sales. In those few instances, the exporters consider that Ex-Im Bank's matching procedures do not typically generate a competitive response.

Chapter 5: Economic Philosophy and Competitiveness

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 they operate as private sector lenders, in reality they have traditionally received 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 prove that Market Windows are indeed a competitive threat. 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 have enabled 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. These changes weaken the potential competitive advantage of Market Windows. In practice, however, 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 without OECD restraints.

Ex-Im Bank 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. In Ex-Im Bank’s re-authorization in 2002, however, the U.S. Congress gave Ex-Im Bank permission to match the terms and conditions offered by Market Windows, an authority that was continued in the Bank’s 2006 reauthorization. Ex-Im Bank’s matching authority has not yet been used because 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 (particularly Japan) could become Market Window players should they perceive a competitive advantage to doing so. Moreover, a variety of forces (e.g., WTO panel decisions and domestic imperatives to make a profit) create incentives for ECAs to increasingly utilize commercial-like procedures and standards.

The rest of this chapter addresses recent activities and changes in these two 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 and Market Windows without effective transparency.

Data for EDC's MLT export credit activity in 2004-2006 reveals significant year-to-year variability in EDC's aggregate business activity. Market Window activity witnessed similar fluctuations, accounting for 75%, 85% and 96% of EDC's total MLT export credit business in years 2004, 2005 and 2006 respectively (see **Figure 22**).

Figure 22: EDC Medium- and Long-Term Activity 2004-2006, (US\$ Billion)

	2004	2005	2006
MLT export credits	3.9	3.3	5.3
Market window	2.9	2.8	5.1
Official window	1.0	0.5	0.2

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. This 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 rendering European commercial banks uncompetitive. Until 2008, IPEX-Bank will operate as a "bank-in-a-bank," i.e., an independent unit of KfW. Though IPEX-Bank is a KfW subsidiary, it will have a stand-alone credit-rating, which will be the basis of its funding starting in 2008. IPEX-Bank will be provided with initial equity upon spin-off by KfW. It will be subject to taxation and German banking regulations, and must earn a risk-adjusted return on capital (RAROC) of 13%, a level determined by IPEX-Bank Management and endorsed by KfW's Board. Meanwhile, KfW itself continues to promote the growth of the German economy in a variety of ways, primarily focusing on domestic investment such as housing finance and support to small businesses.

Of IPEX-Bank's EUR 15 billion business volume in 2006, 66% consisted of commitments outside Germany, of which 32% was export credit business. Consistent with expectations that IPEX-Bank will function more like a private sector entity, over 31% of its 2006 export credit business was in support of entities in Europe or North America. In contrast, these markets comprised 50% and 65% of IPEX-Bank's new business in 2004 and 2005 respectively. The three largest industry sectors receiving IPEX-Bank export credit support in 2006 were basic industries (49.2%), ships (17%), and aircraft (16%).

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 23** below provides a breakdown between the Market Window and official window support provided by IPEX-Bank in the 2004 through 2006 time period and compares it with the equivalent support provided by KfW prior to the creation of IPEX-Bank (pre-2004). In 2006, approximately 55% 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 23: KfW/IPEX-Bank Medium- and Long-Term Activity, 2002-2006 (US\$ Billion)

	2002	2003	2004	2005	2006
MLT export credits	3.3	2.0	3.0	3.2	4.0
Market window	2.1	1.3	1.8	1.9	2.2
Official window	1.2	0.7	1.2	1.3	1.8

Summary Data

Combining the two estimates for EDC and KfW yields an average total Market Window volume of approximately \$5.6 billion per year over the last three years (see **Figure 24**).

Figure 24: Market Window Activity 2002-2006 (US\$ Billions)

	2004	2005	2006
EDC	2.9	2.8	5.1
KfW/IPEX-Bank	1.8	1.9	2.2
Total	4.7	4.7	7.3

Exporter and Lender Views

One U.S. exporter noted that Ex-Im Bank's lack of a Market Window renders the Bank "uncompetitive in this important arena." Exporters as a group, however, remain relatively silent on this issue.

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) weaken Market Windows' potential competitive advantage. Market Windows have a neutral impact on the Bank's competitiveness.

GRADE: NA – Ex-Im Bank can provide Market Window support if necessary. It has not yet been compelled to do so.

Chapter 5: Economic Philosophy and Competitiveness

Section C: U.S. Philosophy and Ex-Im Bank 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 United States has consistently upheld this philosophy and has endeavored to ensure that this framework and principles are adopted by our official ECA counterparts within the OECD and are accurately and fully depicted in the OECD Arrangement.

To a large extent, in addition to the competitiveness issues of “de facto tied” untied aid, tied aid and market windows, the trend that appears to be taking hold and is beginning to change the ECA landscape relates to the “commercialization” of ECAs. While the standard Economic Philosophy and Competitiveness” has not changed in its core features, this evaluation is no longer sufficient as the sole basis for “grading” Ex-Im Bank in relation to its ECA counterparts. This issue is addressed more specifically in Chapter 8, “New ECA Directions.”

During 2006, there was tied aid activity but there has been no documented existence of any “de facto tied” untied aid or instances when market windows have undercut both the market and ECAs, nor even reasonable allegations. 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 25 shows the span of impact that these traditional financing features (e.g., de facto tied untied aid, market windows) are likely to have on Ex-Im Bank’s competitiveness on individual cases when similar terms and conditions are not available to U.S. exporters.

Figure 25: Grading of Ex-Im Bank’s Competitiveness When Confronted with Differing Government Financing Philosophies and Programs, 2006

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

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

** In Ex-Im’s 2002 Charter Reauthorization, Ex-Im 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 export credit agency of the U.S. government. In this role, Congress has given the Bank a mission to provide export financing assistance to the U.S. exporting community that is competitive with, and serves to neutralize, financing offered by the major foreign government ECAs. The basis for this mission is that government intervention is in the national interest when necessary to ensure 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. As such, Ex-Im Bank is expected to consider broader U.S. policies in how it carries 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 (e.g., economic impact 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 such broad public policy considerations.

The following sections of this chapter present a contextual description of selected public policies and an analysis of the competitive implications related to each issue. 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 the production of substantially the same product that is the subject of specified trade measures (i.e., transactions resulting in the production of a good subject to an anti-dumping (AD) or countervailing duty (CVD) order, a suspension agreement from an AD/CVD investigation or a Section 201 injury determination under the Trade Act of 1974); or
- Pose the risk of substantial injury to the U.S. economy. According to Ex-Im Bank's charter, substantial injury is presumed if the volume of new foreign production is 1% or more of U.S. production of the same product.² However, only transactions over \$10 million in Ex-Im financing that meet the substantial injury threshold are subject to further economic impact analysis prior to authorization. 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 the new foreign production). Transactions under \$10 million in Ex-Im Bank financing have been subject to a post-authorization review

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 an AD/CVD investigations. Legislation enacted in December 2006 also requires that the Bank examine whether support for a transaction would facilitate circumvention of the relevant trade measures.

² Legislation enacted in December 2006 requires the Bank to make a judgment as to whether the facility is reasonably likely to be used for producing goods other than the product specified in the application.

to determine if a single buyer, in aggregate, benefited from greater than \$10 million in Bank financing.³

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 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.

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-financed export. In addition, only Ex-Im Bank is required to consider the relevance of trade measures to a transaction.

Summary Data

In 2006, Ex-Im Bank acted on⁴ 593 medium-term insurance and medium- and long-term loan and guarantee transactions. Of these transactions, 324 were applications for long- and medium-term loans and guarantees at the Preliminary Commitment (PC) and Final Commitment (AP) stages, and 269 were applications for medium-term insurance. Thirty-eight percent (227 cases) of total transactions acted upon were scrutinized for economic impact relevance because they supported a foreign buyer's production of an exportable good.

Of these 227 transactions, only six (about 1% of the total number of transactions acted upon by the Bank) required a detailed economic impact analysis (the remaining 221 cases were under the \$10 million threshold). One analysis yielded a net negative economic impact finding due to a U.S. Government consensus that the new foreign production (raw steel) was likely to be in global oversupply when the new foreign production was scheduled to come online. The Bank determined that support for a project that increased global steel-making capacity would be inconsistent with U.S. Government steel policy. This transaction was subsequently denied by the Board of Directors due to economic impact reasons. The remaining five cases 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 2006. Due to this

³ Legislation enacted in December 2006 requires that, for the purposes of determining whether a proposed transaction exceeds the \$10 million threshold, the Bank will 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.

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.

constraint, staff estimates that applicants did not pursue Ex-Im Bank financing for 20 potential transactions in 2006 after learning about the existence of an applicable trade measure. Therefore, while the economic impact policy directly affects a relatively small share of Ex-Im Bank activity, it may also have a “chilling effect” on potential applicants. Of these 20 potential transactions, 18 (or 90%) involved the export of steelmaking equipment, which reflects the large share (more than 50% of all orders) of steel-related AD/CVD orders. A review of G-7 ECA data shows that the other G-7 ECAs supported approximately \$744 million worth of steelmaking equipment and services exports during 2006.

Exporter and Lender Survey Results

While lenders and exporters recognize that the Bank’s economic impact policy is a legislated mandate, some exporters view the requirement as a competitive impediment. One survey respondent noted that if capital equipment export transactions are not supported by Ex-Im Bank, U.S. exporters will lose foreign export contracts and U.S. jobs would be lost. Out of the 27 survey respondents, 16 respondents indicated that economic impact was applicable to their experience with Ex-Im Bank in 2006. Of these 16 respondents, 9 (56%) rated the Bank’s economic impact policy as negative and 7 (44%) were neutral. None of the survey respondents rated the policy as “positive.”

Conclusion

Ex-Im Bank’s economic impact policy directly affected roughly 38% of the Bank’s medium- and long-term transactions acted upon in 2006 (about 1% 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). While economic impact considerations affected mostly capital goods and services transactions related to the steel sector (where both oversupply considerations and trade sanctions are relevant), exporters of capital goods and services outside the steel sector also believed that the economic impact mandate undermines U.S. competitiveness. Because no other G-7 ECA is prohibited from supporting transactions due to economic impact considerations, this requirement appears to have a negative impact on Ex-Im Bank’s competitiveness.

Agency Comments:

“The State Department notes that full consideration for the impacts of foreign competition to the proposed U.S. export, while not part of the mandate from Congress, would significantly mitigate this effect on Ex-Im Bank's ability to compete.”

Chapter 6: Public Policies – Stakeholder Considerations

Section C: Foreign Content

Introduction

Foreign content is the portion of the export that originates outside of 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 of the export. The U.S. content is the \$8.5 million portion of the export that originates in the United States. 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.

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 United States. 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, however there are no specific statutory requirements *per se* relating to foreign content. Rather, the policy reflects a concerted attempt to balance the interests of labor and industry.

For all medium- and long-term transactions, Ex-Im Bank's foreign content policy *restricts* the scope of its financial support to cover only those products that are shipped from the United States to a foreign buyer, and then it *limits* the level of its support to the **lesser of**: (1) 85% of the value of all eligible goods and services contained within a 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 for 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 Participants have differing rules on foreign content and there are no OECD Arrangement guidelines governing the scope or design of foreign content in an officially supported export credit. Thus, 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, today there is a growing and accelerating tide of change with regard to the content policies of ECAs. For example, ECAs are increasingly shifting from the “made in country X” approach to the “made by country X” approach, which allows ECAs to support content produced anywhere so long as it benefits the domestic economy. This more “flexible” approach is particularly relevant to foreign subsidiaries and has allowed several foreign ECAs to support transactions that may not involve a direct export from the home country.

Figure 26 compares the main aspects of the content policies of the G-7 ECAs in 2006. The data illustrate that Ex-Im Bank’s content requirements are more restrictive than its G-7 counterparts.

Figure 26: Comparison of Content Policies of the G-7 ECAs, 2006

	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	Yes	Yes	Yes

Ex-Im Bank is the only G-7 ECA with the requirement that goods be shipped from the U.S. to be eligible for support. Ex-Im Bank also has the lowest “foreign content allowance” (i.e., 15%). In contrast, the European ECAs generally do not reduce cover for transactions that include up to 30-40% EU content and the Japanese ECAs are even more flexible in that cover is not reduced for transactions that include up to 70% foreign content. While Ex-Im Bank does not have a minimum amount of domestic content requirement for the medium and long-term, Ex-Im Bank limits its support to cover 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.

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 27**) indicate a generally stable relationship between Ex-Im Bank transactions and foreign content. That is, while the figures change from year to year, many of the figures in 2006 are similar to 2002. Moreover, although the key ratio of average foreign content per transaction with foreign content is significantly higher in 2006 than 2005 (14% versus 10%), a trend line from 2002 to 2006 would tilt only modestly upward.

However, an analysis of the data in Appendix E differentiating aircraft from non-aircraft transactions shows more pronounced trends over the five-year period. Specifically, the non-aircraft foreign content ratio went from roughly 8% in 2002 to 13% in 2006 and the aircraft foreign content ratio moved from just over 12% in 2002 to approximately 16% in 2006.

Figure 27: Recent Trends in Ex-Im Bank Support for Medium- and Long-Term Activity Containing Foreign Content, 2002-2006 (US\$ Million)*

		Authorizations	2002	2003	2004	2005	2006
Total activity	Export value (\$MM)		\$8,212	\$8,386	\$9,630	\$7,268	\$8,039
	Number of transactions		222	232	260	271	220
Transactions containing foreign content	Export value (\$MM)		\$7,842	\$7,823	\$7,821	\$6,713	\$6,139
	Percentage of total value		95%	93%	81%	92%	76%
	Number of transactions		96	85	95	111	96
	Percentage of total number		43%	37%	37%	41%	44%
Foreign content	Volume (\$MM)		\$836	\$814	\$904	\$691	\$843
	Average per transaction of cases containing foreign content		11%	11%	12%	10%	14%

*These figures exclude medium-term insurance because we had access to MT insurance data for only 2006. Due to the time series nature of this figure, and for comparative purposes, MT insurance was not included above. The complete data set however is incorporated in Appendix E.

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) in 2006 at the time of authorization.

Exporter and Lender Survey Results

According to the U.S. exporting community, Ex-Im Bank's foreign content policy is not keeping pace with those of other ECAs and is out of date with business practices that have become increasingly more globalized. Ex-Im Bank does not support goods shipped from subsidiaries of U.S. companies located overseas while most ECAs are adopting this "national interest" model. Moreover, the exporting community sees Ex-Im Bank documentation and certification requirements related to content as unreasonable, time consuming and contributing to lost sales. One exporter summarized trends in content as follows: "Ex-Im's foreign content policy is antiquated and causing Ex-Im to be less competitive year after year as Euro ECAs increasingly adopt the "made by" rather than "made in" philosophy. As there is no solution in sight to resolve this impasse at Ex-Im Bank, we will actively pursue foreign ECAs although this is not our preference." Consequently, the Bank's content policy is perhaps viewed as the Bank's most competitively disadvantageous feature when foreign content is a significant factor in a transaction.

Conclusion

G7 ECAs are increasingly adopting "national interest" policies with one of the main characteristics being more flexibility regarding the minimum threshold of required domestic content. As these trends become ever more pervasive, Ex-Im Bank's foreign content policy is becoming an increasing drag on the competitiveness of Ex-Im Bank financing. Today, given the incidence of foreign content (present in roughly half of all transactions/70-80% by volume) and the rapid (and ongoing) deterioration of comparable practices, content is probably the most competitively disadvantageous element in Ex-Im's program and policy menu. In sum, when cases involve foreign content, Ex-Im Bank's approach has a significantly negative impact on the competitiveness of U.S. exports.

Chapter 6: Public Policies – Stakeholder Considerations

Section D: Local Costs

Introduction

Local costs are goods and services originated or manufactured 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. (e.g., cement, construction workers, etc.). In contrast to foreign content, the OECD Arrangement sets the basic parameters on official local cost support. The OECD parameters allow ECAs to provide support for local costs up to the amount of the down payment, which according to OECD Arrangement rules is at least 15%.

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 may also provide up to 15% of the value of the U.S. exports (including eligible foreign content) for locally originated or manufactured goods and services. Ex-Im Bank's local cost policy reflects the premise that there is some amount of local labor and raw materials necessary to efficiently build or assemble the end product of the U.S. export.

For medium-term transactions, Ex-Im Bank may provide local cost support as long as the local costs are related to the U.S. exporter's scope of work and the U.S. exporter can demonstrate 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. That is, ECAs may provide support for local costs related to officially supported export transactions up to the amount of the down payment, which is 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 “adversarial” emerging markets has dramatically improved, which has led to a change in the nature of the local goods and services 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 increasingly being requested to provide support for locally manufactured capital goods.

There is 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. These smaller ECAs are increasingly offering maximum local costs support in order to remain competitive with larger ECAs.

A second way that some ECAs appear to be responding to the demand for greater local costs is in how ECAs are defining local costs vs. national content. For example, a few ECAs are increasingly either supporting sales through their exporter’s local subsidiaries as national content or covering costs typically considered as local costs as part of the domestic supply through the ECAs’ documentary process.

Confirmation of support for greater flexibility for local costs support is evidenced by several official proposals to revise the disciplines in the OECD Arrangement governing the amount of allowable ECA support of local costs. The core concept of the most recent proposal is to: (i) break the connection to the cash payment; (ii) reduce (or even eliminate) the limitations placed on the amount of local costs that can benefit from official support currently set at a maximum of 15% of the export value; and (iii) limit official support for local expenditures to those that are necessary for executing the exporter’s contract. The essence of this proposal is gaining momentum within the OECD.

Summary Data

Figure 28 illustrates recent trends in Ex-Im Bank’s support of local costs. In 2006, only 1% of total medium- and long-term transactions requested local costs support. This drop in volume can be largely attributed to an absence of authorized project finance transactions. Additionally, the dollar volume of the transactions that received local costs decreased significantly due to the fact that the approximately 70% of the transactions that received local costs were for transactions valued at less than \$10 million. In 2006, as in 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 28: Recent Trends in Ex-Im Bank Local Costs Support, 2002-2006 (US\$ Million)

	Authorizations	2002	2003	2004	2005	2006
Total medium-and long-term activity	Export value (\$MM)	\$8,554	\$8,873	\$10,949	\$7,791	\$8,718
	Number of transactions	525	569	757	587	485
Medium- and long-term activity containing local costs	Number of transactions	33	57	79	88	47
	Percentage of total number of transactions	6%	10%	10%	15%	10%
Local costs	Volume (\$MM)	\$184	\$123	\$312	\$669	\$54
	Percentage of total medium-and long-term activity	2%	1%	3%	9%	1%

Exporter and Lender Survey Results

Though the majority of survey respondents indicated that Ex-Im Bank’s local costs policy was generally competitive when compared to its counterparts, exporters and lenders alike indicated that it is the “interpretation of Ex-Im Bank’s local costs policy that sets the U.S. and G-7 ECAs apart.” Specifically, it is the more flexible interpretation and implementation of the policy by some other ECAs that can put Ex-Im Bank behind the others.

Conclusion

Based on comparative information regarding our G-7 ECA counterparts, the availability and eligibility criteria governing Ex-Im Bank’s local cost policy is viewed as competitive. However, over time other ECAs have become more flexible in their approach and implementation while, according to the U.S. exporting community, their experience with the implementation of Ex-Im Bank’s local cost policy renders Ex-Im Bank’s local costs policy less competitive. When considered as a whole, Ex-Im Bank’s local cost policy is considered to have 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. exports less competitive relative to foreign competitors since foreign competitors 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 to be eligible for Ex-Im 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.

Upon request, MARAD may waive the U.S. flag vessel requirement on a case-by-case basis. If a waiver 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 91% approval rate. Statutory waivers may be granted if MARAD determines that a U.S.-flagged vessel will not be available within a reasonable amount of time or at a reasonable rate.

Currently, the U.S. is a party to three Maritime Agreements negotiated by U.S. delegations headed by the U.S. Maritime Administrator. As of 2006, the U.S. has bilateral Maritime Agreements with Brazil, China and Russia, of which 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 2006.

G-7 ECAs' Policies and Practices

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

Summary Data

Figure 29: Number of PR-17 Waivers Approved and Denied

Waiver Type		2002	2003	2004	2005	2006	Total	Percentage of Waivers Approved
General Waivers	Approved	3	0	0	1	0	4	100
	Denied	0	0	0	0	0	0	
Statutory Waivers	Approved	22	29	26	19	17	113	91
	Denied	1	5	2	2	1	11	
Compensatory Waivers	Approved	10	11	5	3	2	31	100
	Denied	0	0	0	0	0	0	
Conditional Waivers	Approved	0	0	0	1	0	1	100
	Denied	0	0	0	0	0	0	

Source: MARAD

Figure 29 shows the outcome of waiver applications to MARAD for 2002-2006. 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.

Exporter and Lender Survey Results

Exporters and lenders consistently note that MARAD requirements play a role in precluding U.S. exporters from winning bids for transactions. In fact, in some cases U.S. shipping requirements may be the sole reason why a U.S. exporter may lose

business to a foreign competitor. For example, lenders and exporters cited one \$300 million transaction that was lost to another ECA due to MARAD requirements. Exporters and lenders state that in cases where waivers are sought, waivers may not be provided because MARAD maintains that U.S.-flagged vessels are available. While this may be true, the shipping costs associated with shipping on U.S. vessels may be four to five times more expensive than shipping on foreign-flagged vessels.

Conclusion

MARAD requirements appear to present a competitive disadvantage for U.S. exporters because none of the other G-7 ECAs have similar shipping requirements. Although the MARAD waiver data appear to present the waiver process as an effective means of addressing any potential hardship or limitation placed on exporters by PR 17, the U.S. exporting community strongly believes that when MARAD rules apply to a transaction, this requirement is a negative factor affecting Ex-Im Bank's competitiveness.

Chapter 6: Public Policies – Stakeholder Considerations

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

Ex-Im Bank has unique public policy requirements when compared to the other G-7 ECAs. The exceptions are (1) local costs support – which is governed by the OECD Arrangement – is where Ex-Im Bank has traditionally been fully competitive with its ECA counterparts and (2) foreign content, though not addressed in the OECD Arrangement, but addressed by our G-7 ECA counterparts is relatively more flexible. Specifically, along that spectrum, Ex-Im Bank’s approach is rated as more restrictive than the other ECAs. The other public policy factors which are shown below in **Figure 30** are areas that, when present in a given transaction – which is happening more often -- have a negative effect on Ex-Im Bank’s competitiveness, as no other G-7 ECA has a comparable requirement.

Figure 30: Grading of Ex-Im Bank’s Public Policy Competitiveness, 2006

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

Chapter 7: Results

For 2006, Ex-Im Bank’s overall competitiveness as compared to its G-7 ECA counterparts is deemed to be an “A-/B+”, meaning that the Bank was marginally competitive with the other ECAs. This rating is slightly less favorable than in 2005 (A). Specifically, for 2006, Ex-Im Bank is rated as inconsistently offering terms equal to the average G-7 ECA. **Figure 31** shows that the core financing elements of premia, interest rate, and cover policy are important areas in which Ex-Im Bank generally met its competition. However, overall, the Bank performed less well on a consistent basis against the average G-7 ECA in the major program structures. The value of these features – foreign currency and co-financing appears to have increased, and therefore, their importance relative to the other factors has grown. The aircraft and project finance programs are still on par with competitors’ programs (when the public policy issues are not part of the equation).

Figure 31: Grading of Ex-Im Bank’s Overall Competitiveness, 2006

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+

In addition to the core structural elements of Ex-Im Bank’s financing, there are philosophical and policy aspects to the Bank’s support of transactions that may impact its competitiveness (see **Figure 32**). Chapters 5 and 6 described the Economic Philosophy and Public Policy objectives of Ex-Im Bank in comparison to its G-7 competition. With respect to Tied Aid and Market Windows, the U.S. position may have a negative (or neutral) impact on the competitiveness of Ex-Im Bank transactions—although the overall impact to competitiveness is minimal as these types of cases are infrequently encountered. With regard to the Bank’s public policy requirements, the Bank’s Economic Impact, Foreign Content and Shipping policies have always been considered to have a negative impact to competitiveness, while the Bank’s Local Costs policy’s impact on competitiveness was considered to be positive. However, in 2006, because other ECAs have changed to make local costs support more broadly available than in prior years, the Bank’s own Local Costs policy was considered to have a neutral impact on competitiveness. Moreover, content is now deemed a “significantly” negative factor. These aspects, taken together, certainly support the downgrade indicated above.

Figure 32: Direction of Case-Specific Competitive Impact of U.S. Economic Philosophy or Public Policy on Certain Official Export Credit Activity, Procedures or Practices, 2006

Areas Affected by U.S. Economic Philosophy or Public Policy	Potential Case-specific Impact on Competitiveness
Economic Philosophy A. Tied Aid (<u>de jure</u> or “de facto”)	Negative (<i>infrequently encountered, therefore, a modest overall competitive impact</i>)
B. Market Windows	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 Negative Neutral Negative

Agency Comments:

"However, as noted in the Executive Summary, other members of the Administration that reviewed this report believe that an A-/B+ is an overly pessimistic grade and under-represents Ex-Im Bank's actual competitiveness vis-à-vis the other G-7 ECAs." [Statement submitted by the Departments of Treasury, State and the Office of Management and Budget.]

Chapter 8: The New ECA Competitiveness Framework

Introduction

Historically, Ex-Im Bank has compared itself to G-7 (and other) Export Credit Agencies using a fairly standard set of criteria and programs generally governed by the OECD Arrangement. Specifically, the features and programs of export credit agencies include: (1) basic features – interest rates, premia, risk attitudes; (2) special programs – co-financing and foreign currency; (3) sector specific programs – aircraft and project finance; and (4) public policies – tied and untied aid, content, economic impact, etc.

However, several factors have recently emerged that have caused a sea-change among a number of our ECA counterparts. The three most significant factors include:

- the evolution of the export credit regulatory (i.e., WTO) framework towards “legitimate” export credit being defined by its financial profitability and relationship to market with an emphasis on the elimination of “prohibited subsidies”;
- the movement of multinational production centers (including many European “national champions”) to emerging markets to take advantage of cost efficiencies; and
- the creation of more sophisticated, liquid, and competitive international capital markets.

When taken together, these forces have caused several ECAs to examine and change how they approach export credits. The active inclusion of export credits within the purview of the WTO has created a pervasive apprehension among ECAs that, unless they can demonstrate that they intend to manage and operate on a long-term breakeven trajectory with market-based pricing, they may be subject to litigation. Globalization of sourcing options has translated into companies becoming multinational in form and creating more competitive supply chains, irrespective of their primary domicile. Further, as buyer countries become more developed, there are other alternatives to export credit. This has led to ECAs no longer being “the only game in town.”

In response to these new challenges, several ECAs have been operating more like the private sector in terms of how and where they do business (e.g., higher income markets) and redefining the equation for determining “national benefit” by extending support to goods produced by a national company in another country. While some of these areas are unregulated by the OECD, other regulated areas are becoming targets for change within the OECD. One of the consequences of these

changes has been an increase in competition between some ECAs and the private sector in search of attractive returns to meet their profit objectives.

Therefore, the historical basis upon which Ex-Im has conducted its comparative analysis may no longer be sufficient and may require adjustment in order to ensure a more meaningful comparison. The purposes of this chapter are (i) to describe one possible example of a new ECA Framework (as compared with the “traditional”)¹; (ii) to identify the key features that could comprise this Framework; (iii) to classify the consequences of the new underlying philosophy of a number of our ECA counterparts; (iv) to classify each of the G-7 ECAs along the spectrum of this alternative Framework, and finally, (v) to identify potential future implications associated with this new Framework.

Traditional role of ECAs

Export credit agencies (ECA) have traditionally gotten involved to: (i) correct market failures, (ii) mitigate against risks that the private sector is unwilling or unable to assume, and (iii) ensure a level playing field for its national industries. In this context, the export credit agency is a public entity or a private company that acts on behalf of the state. This traditional business model is that of the “Insurer/Lender of Last Resort” (ILR/LLR). The scales tip in favor of public interest on a deal-by-deal basis with the understanding (and intent) that future earnings will offset in the long run any short-to medium-term losses incurred by the ECA. The scope of an ILR’s involvement is generally limited to higher risk, longer term transactions and seeks to complement the private sector. This underlying philosophy has historically been shared by most official ECAs with policies and programs designed to fill this role.

Emerging trends

The challenge for ECAs is to develop the ability to respond to the changing needs of its customers which is particularly difficult when the rules and regulations governing these are also changing by becoming more diffuse. The business model required to deal with these changes may be very different from the traditional ILR. Several ECAs have transformed (or are transforming) into a quasi–market player (QMP) that conducts its business on the basis of commercial practices, albeit backed by public capital. The scope of a QMP’s involvement is typically extended to moderate and low risk activity in high yield OECD markets. In the quest to realize profits, QMPs actively seek out and exploit opportunities in niche areas which tend to result in a competitive relationship with the private sector.

¹ The descriptions of the traditional roles of ECAs, the new ECA framework and key elements that distinguish an ECA as an Insurer of Last Resort (ILR) or a Quasi Market Player (QMP) were largely taken from Raoul Ascari’s (SACE) report, *Is Export Credit Agency a Misnomer? The ECA Response to a Changing World*.

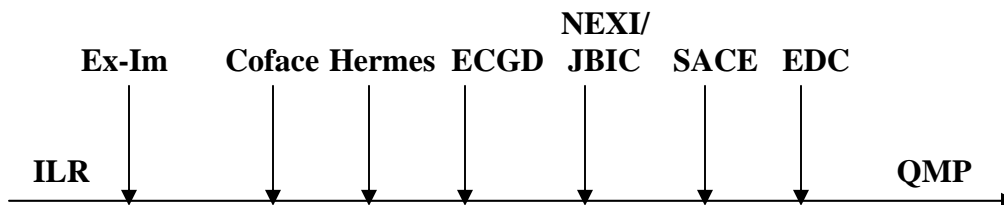
The chart below summarizes the key elements that distinguish an ECA as an ILR or QMP.

Key Elements	Insurer of Last Resort (ILR)	Quasi Market Player (QMP)
Primary Objective	Public Interest	Financial Profit
Financial	Appropriations from the state	Relies on its own financial resources as first protection.
Approach	One-off, deal by deal with no major portfolio goals or constraints.	Overall strategic portfolio management.
Scope	Reactive and responds to market	Proactive and seeks opportunities.
Philosophy	“Made In”	“Made By”

ECA Business Models Along a Continuum *

Using these concepts, it is possible to characterize each G-7 ECA and to represent each along a spectrum classifying where they would fit in the hypothetical world defined by these concepts.

ECA Spectrum:



The political basis for the emerging changes is the concept of “national interest”, which is a more broadly defined benefit than the traditional focus on immediate employment and income. The financial basis of the change is the ability to operate independently without ever (even in periods of financial crisis) relying on federal funds. As the OECD Arrangement continues to evolve and ECAs encourage one another to agree to changes that support their position, an increasing challenge will be for all parties to find an acceptable balance between the two competing philosophies.

*

Ex-Im Bank’s extrapolation of the concepts presented in Raoul Ascari’s report, previously noted.

Potential Competitive Implications

Changes in the global economic and financial environment and the increasing role of the private sector in the economy are among the factors triggering change in the export credit business model. ECAs are faced with the choice of staying with the “made in/lender of last resort” philosophy and seeing their business volumes shrink, or effectively following their national champions offshore by changing their content and business orientation. Using the hypothetical characterization derived from Raoul Ascari’s insightful definitions, one sees a current picture in which three of the G-7 are clearly (or largely) in the “commercial/made by” camp (SACE, EDC and the Japanese), the British appear half-way there (in financial orientation – and are reviewing their content rules), while the Germans seem to be experimenting with change (sector by sector, case by case). This analysis leaves only the French and U.S. pretty solidly in the historical positions of “made in” and “lender of last resort.”

If the divergent worlds typified above do develop and come to dominate agency practices and positions, the task of comparing “competitiveness” will become ever more difficult. Which is more competitive – 50% foreign content allowance at 8% effective cost or 15% foreign content allowance at 6% effective cost? As it becomes more difficult to measure competitiveness among ECAs, leveling the playing field will become an increasingly difficult objective to realize.

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 discussions 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 (i.e., response was an ‘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.	

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. For this report, 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 2006 by purpose and program type.

Figure B1: Ex-Im Bank Transactions by Purpose, 2006

	No Private Sector Finance Available		Meet Competition		Not Identified	
	(\$MM)	(#)	(\$MM)	(#)	(\$MM)	(#)
Working capital guarantees	\$685	292	\$0	0	\$0	0
Short-term insurance	\$3,291	1,640	\$0	0	\$0	0
Medium-term insurance	\$354	247	\$267	7	\$0	0
Guarantees	\$3,062	172	\$3,915	44	\$0	0
Loans	\$57	3	\$0	0	\$0	0
TOTAL	\$7,449	2,354	\$4,182	51	\$0	0

Appendix C: Exporter and Lender Survey Results

Introduction

As part of the Ex-Im Bank's statutory requirement to report annually on the Bank's competitiveness with its major 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 exporters and lenders of Ex-Im Bank programs to get more detailed comments about the global market in which they operated in 2006 and the competitive implications for Ex-Im Bank.

Survey

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 in the policies and programs 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 2006. In total, 83 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 33%. The response rate for exporters was higher than for lenders, with 39% of exporters responding and 28% of lenders responding.

Figure C1: Survey Response Rate, 2006

	Lenders	Exporters	Total
Number surveyed	47	36	83
Number responded	13	14	27
Response rate	28%	39%	33%

Lenders

Figure C2 shows the lender experience levels for both length of time in business and experience in export finance. The large majority of lenders (85%) have been in business for over 11 years with 82% of those over 21 years. Experience in export finance as measured in years indicated that 23% were relatively new to the business (3 had 1- 10 years) while the vast majority had well over 20-plus years of experience in export finance. **Figure C3** shows the volume of export credits extended during 2006. However, about half the respondents answered this question. Of these seven, more than a majority (57%) stated that they had provided over \$100 million but less than \$1 billion in export credits during 2006, while the remaining lenders offered a total amount in the range of \$1 million up to \$50 million.

Figure C2: Lender Experience Levels, 2006

	1-3 years	4-10 years	11-20 years	21+ years
Time in business	0	2	2	9
Time in export finance	1	2	3	7

Figure C3: Volume of Lenders' Annual Export Credits, 2006

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

Figure C4 shows the percentage of lenders' export credits extended during 2006 that were supported by Ex-Im Bank during the year. Nine of the 13 lenders indicated their volumes for 2006. Of these, just under half (44%) of the lenders noted that 50% or less of their export credits had Ex-Im Bank support, while the other 55% reported that 75% of their export credit portfolio had been supported by Ex-Im Bank.

Figure C4: Percentage of Lender Export Credits That Were Ex-Im Bank Supported, 2006

	Less than 10%	10%-25%	26%-50%	51%-75%	Over 75%
Number of lender's whose export credits were supported by Ex-Im Bank	0	2	2	0	5

Nearly all of the lenders surveyed (12 of 13) noted that the lack of useful private sector financing was the reason for pursuing Ex-Im Bank financing, particularly for financing transactions in Latin America, including Mexico, the Caribbean and Central America, Russia and Eastern Europe. Ten (10) of the 13 lenders stated that Ex-Im Bank support was needed to meet competition from foreign companies that receive ECA financing with Euler-Hermes cited as the most frequent ECA with whom they had competed followed by SACE, EDC and Coface. The ECAs identified by the lenders as the most “regular” partners were Euler-Hermes, EDC and Coface.

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, 83% had been exporting for 21 years or more.

Figure C5: Exporter Experience Levels, 2006

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

Figure C6 shows the size of exporters based on sales and export sales volume, for those that reported sales volumes. Nine of the ten exporters who reported sales figures showed 2006 sales volumes of \$1 billion or greater. Six of the nine companies with total sales of over \$1 billion also reported export sales at that amount as well.

Figure C6: Volume of Exporter Annual Sales and Exports, 2006

	Under \$10 million	\$10 - \$50 million	\$51 - \$100 million	\$101 - \$500 million	\$501 million - \$1 billion	Over \$1 billion
Total sales volume					1	9
Total export sales volume			1	2	0	6

Figure C7 shows the distribution of exporters by the percentage of export sales that were supported by Ex-Im Bank. Of the nine companies who responded, six showed that Ex-Im Bank support comprised 10% of its export sales while the remaining three (3) noted Ex-Im Bank support from 10% up to 25% of their sales.

Figure C7: Percentage of Exporters Sales That Were Ex-Im Bank Supported, 2006

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

ECA Cooperation and Competition

Approximately 70% of the exporters surveyed (9 of 13) indicated regular experience working with at least one other ECA, and one exporter noted that it had worked with every G-7 ECA during 2006. The ECAs most frequently cited as “partners” were Coface, and ECGD followed by EulerHermes and EDC. Of the non G-7 ECAs, KEIC (Korea), Finnvera (Finland), GIEK (Norway) and Atradius (Netherlands) were most often cited as a partner with the exporters. All (100%) of the exporters surveyed reported facing regular competition from foreign companies that were supported by their national ECAs throughout 2006. The most commonly identified competitor ECAs (in descending order) were Coface, Euler-Hermes, JBIC, and ECGD.

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.
- 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 (this spin-off will be finalized by 2008). KfW will continue to offer export credit support on a limited basis: in a syndicate for less risky markets and on its own only in the riskiest markets.
- 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 new structure, SACE continues providing medium- and long-term official export credit insurance and began to provide 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.

- 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 that 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.

In July 2004 the U.K. government announced a series of changes to ECGD that were designed to provide greater certainty for ECGD’s future. The most significant of these changes was the announcement that a pilot ECGD Trading Fund will operate from April 2005 as a trial for the statutory Trading Fund, which is scheduled to start in April 2007. The Trading Fund will have a specific target rate of return, but despite fears expressed by U.K. exporters, ECGD’s Chairman of the Board has stated in ECGD’s 2003-2004 Annual Report that the Trading Fund “should not result in any increase in premium or reduction in cover.”

Appendix E: Ex-Im Bank Foreign Content Support for Medium- and Long-Term Transactions Containing Foreign Content, 2006*

Country	Exim Product**	Product/Project	Export Value	Foreign Content Percentage***
ANGOLA	LG	Large Aircraft	\$338,462,258	19%
AUSTRIA	LG	Large Aircraft	\$41,457,190	16%
BRAZIL	LG	Agricultural Equipment	\$482,444	7%
BRAZIL	LG	Drilling Machinery	\$1,803,530	8%
BRAZIL	LG	Large Aircraft	\$144,154,984	16%
BRAZIL	LG	Medical Equipment	\$1,448,527	3%
BRAZIL	LG	Medical Equipment	\$381,922	4%
BRAZIL	LG	Small Aircraft	\$40,956,337	13%
BRAZIL	LG	Small Aircraft	\$5,142,976	15%
BRAZIL	LG	Telecommunications Equipment	\$500,084	13%
BRAZIL	INS	Medical Equipment	\$916,294	20%
BRAZIL	INS	Medical Equipment	\$155,650	10%
BRAZIL	INS	Medical Equipment	\$941,868	9%
BRAZIL	INS	Medical Equipment	\$1,217,648	13%
BRAZIL	INS	Oil & Gas Drilling Equipment	\$4,565,415	3%
BRAZIL	INS	Printing Machine	\$10,853,660	9%
CANADA	LG	Large Aircraft	\$191,143,823	18%
CHILE	LG	Large Aircraft	\$195,597,369	11%
CHILE	LG	Large Aircraft	\$63,119,448	11%
DOMINICAN REPUBLIC	LG	Construction Equipment	\$386,203	8%
DOMINICAN REPUBLIC	INS	Construction Equipment	\$9,198,800	10%
DOMINICAN REPUBLIC	LG	Ship Building Equipment	\$4,733,937	11%
DOMINICAN REPUBLIC	INS	Telecommunications Equipment	\$388,265	3%
DOMINICAN REPUBLIC	INS	Telecommunications Equipment	\$975,674	1%
DOMINICAN REPUBLIC	LG	Transportation Equipment	\$293,869	22%
GERMANY	LG	Large Aircraft	\$74,160,000	17%
GUATEMALA	LG	Agricultural Equipment	\$390,138	6%
INDIA	LG	Large Aircraft	\$163,229,249	16%
INDIA	LG	Large Aircraft	\$367,349,531	19%
INDIA	LG	Large Aircraft	\$900,354,357	14%
IRELAND	LG	Large Aircraft	\$76,168,500	16%
IRELAND	LG	Large Aircraft	\$96,305,000	16%
ISRAEL	INS	Medical Equipment	\$4,693,000	10%
KAZAKHSTAN	LG	Agricultural Equipment	\$606,073	17%
KAZAKHSTAN	LG	Agricultural Equipment	\$9,743,316	15%
KAZAKHSTAN	LG	Agricultural Equipment	\$10,319,468	15%
KAZAKHSTAN	LG	Agricultural Equipment	\$468,009	15%
KAZAKHSTAN	LG	Agricultural Equipment	\$2,095,703	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$12,735,332	16%
KAZAKHSTAN	LG	Agricultural Equipment	\$17,768,400	16%
KAZAKHSTAN	LG	Automated Teller Machines	\$18,216,044	12%

Country	Exim Product**	Product/Project	Export Value	Foreign Content Percentage***
KAZAKHSTAN	INS	Automated Teller Machines	\$1,976,400	11%
KAZAKHSTAN	INS	Automated Teller Machines	\$5,994,150	10%
KAZAKHSTAN	INS	Automated Teller Machines	\$1,502,500	12%
LITHUANIA	LG	Agricultural Equipment	\$6,616,601	13%
MALAYSIA	LG	Telecommunications Equipment	\$94,216,270	5%
MEXICO	LG	Agricultural Equipment	\$524,929	3%
MEXICO	LG	Computer Equipment	\$260,104	11%
MEXICO	LG	Construction Equipment	\$480,147	6%
MEXICO	LG	Construction Equipment	\$730,448	6%
MEXICO	LG	Construction Equipment	\$690,200	4%
MEXICO	LG	Construction Equipment	\$559,437	2%
MEXICO	LG	Food Production Equipment	\$757,690	14%
MEXICO	LG	Industrial Equipment	\$173,379	17%
MEXICO	LG	Industrial Equipment	\$890,169	12%
MEXICO	LG	Industrial Equipment	\$1,366,546	13%
MEXICO	LG	Large Aircraft	\$170,705,760	16%
MEXICO	LG	Large Aircraft	\$15,642,720	14%
MEXICO	LG	Laser Cutting Equipment	\$558,896	23%
MEXICO	LG	Laser Cutting Equipment	\$430,700	35%
MEXICO	LG	Machine Tools	\$750,355	17%
MEXICO	LG	Machine Tools	\$871,586	14%
MEXICO	LG	Machine Tools	\$612,392	6%
MEXICO	LG	Machine Tools	\$435,161	19%
MEXICO	LG	Medical Equipment	\$262,041	12%
MEXICO	LG	Metal Stamping Equipment	\$208,229	31%
MEXICO	LG	Oil & Gas Field Machinery	\$150,000,000	6%
MEXICO	LG	Oil & Gas Field Machinery	\$250,000,000	6%
MEXICO	LG	Oil & Gas Field Machinery	\$100,000,000	6%
MEXICO	LG	Oil & Gas Field Machinery	\$100,000,000	12%
MEXICO	LG	Oil Field Development	\$350,000,000	1%
MEXICO	LG	Plastic Manufacturing Equipment	\$284,613	33%
MEXICO	LG	Plastic Manufacturing Equipment	\$773,282	11%
MEXICO	LG	Power Plant Maintenance	\$24,264,586	16%
MEXICO	LG	Power Plant Maintenance	\$15,323,697	16%
MEXICO	LG	Power Plant Maintenance	\$27,314,049	15%
MEXICO	LG	Small Aircraft	\$19,647,636	24%
MEXICO	LG	Small Aircraft	\$1,389,130	17%
MEXICO	LG	Small Aircraft	\$8,428,759	28%
MEXICO	LG	Textile Machinery Equipment	\$300,000,000	1%
MEXICO	LG	Woodworking Machinery	\$424,190	7%
MEXICO	INS	Agricultural Equipment	\$353,280	3%
MEXICO	INS	Agricultural Equipment	\$4,726,657	3%
MEXICO	INS	Agricultural Equipment	\$1,182,312	13%
MEXICO	INS	Construction Equipment	\$1,050,500	10%
MEXICO	INS	Construction Equipment	\$425,500	10%
MEXICO	INS	Construction Equipment	\$1,115,000	10%

Country	Exim Product**	Product/Project	Export Value	Foreign Content Percentage***
MEXICO	INS	Construction Equipment	\$603,000	10%
MEXICO	INS	Construction Equipment	\$787,000	10%
MEXICO	INS	Construction Equipment	\$920,100	10%
MEXICO	INS	Construction Equipment	\$1,168,000	10%
MEXICO	INS	Construction Equipment	\$973,250	10%
MEXICO	INS	Construction Equipment	\$595,217	10%
MEXICO	INS	Construction Equipment	\$986,000	10%
MEXICO	INS	Greenhouses	\$429,387	5%
MEXICO	INS	Industrial Radiation Processor	\$1,094,503	8%
MEXICO	INS	Laser Cutting Machinery	\$417,128	16%
MEXICO	INS	Medical Equipment	\$2,689,932	5%
MEXICO	INS	Medical Equipment	\$3,000,000	15%
MEXICO	INS	Printing & Software Equipment	\$300,000	7%
MEXICO	INS	Printing Equipment	\$375,000	11%
MEXICO	INS	Telecommunications Equipment	\$305,314	6%
MOROCCO	LG	Large Aircraft	\$72,929,150	16%
MOROCCO	LG	Large Aircraft	\$80,195,800	16%
NETHERLANDS	LG	Large Aircraft	\$94,368,932	15%
NETHERLANDS	LG	Large Aircraft	\$94,368,932	15%
NICARAGUA	LG	Medical Equipment	\$977,858	1%
NIGERIA	LG	Agricultural Equipment	\$12,355,118	5%
NIGERIA	LG	Textile Manufacturing Machinery	\$2,336,506	10%
NIGERIA	LG	Transportation Vehicle	\$4,742,537	16%
PAKISTAN	LG	Large Aircraft	\$408,659,564	15%
PANAMA	LG	Large Aircraft	\$66,196,700	21%
PARAGUAY	INS	Printing Equipment	\$350,000	7%
PERU	INS	Construction Equipment	\$716,000	7%
PERU	INS	Irrigation System	\$500,000	28%
RUSSIA	LG	Agricultural Equipment	\$2,209,215	13%
RUSSIA	LG	Agricultural Equipment	\$1,561,585	6%
RUSSIA	LG	Agricultural Equipment	\$2,401,421	14%
RUSSIA	LG	Agricultural Equipment	\$1,616,878	12%
RUSSIA	LG	Agricultural Equipment	\$10,387,000	13%
RUSSIA	LG	Agricultural Equipment	\$1,538,850	26%
RUSSIA	LG	Agricultural Equipment	\$2,132,844	10%
RUSSIA	LG	Telecommunications Equipment	\$4,650,801	60%
RUSSIA	INS	Automated Teller Machines	\$1,097,458	14%
RUSSIA	INS	Automated Teller Machines	\$1,900,000	11%
RUSSIA	INS	Automated Teller Machines	\$11,764,000	11%
RUSSIA	INS	Automated Teller Machines	\$542,415	8%
RUSSIA	INS	Automated Teller Machines	\$1,652,881	12%
RUSSIA	INS	Automated Teller Machines	\$3,000,000	12%
RUSSIA	INS	Automated Teller Machines	\$2,000,000	12%
RUSSIA	INS	Automated Teller Machines	\$4,093,222	14%
RUSSIA	INS	Automated Teller Machines	\$1,644,368	20%
RUSSIA	INS	Automated Teller Machines	\$1,853,813	14%

Country	Exim Product**	Product/Project	Export Value	Foreign Content Percentage***
RUSSIA	INS	Automated Teller Machines	\$7,000,000	12%
RUSSIA	INS	Chemical Processing Equipment	\$1,943,400	2%
RUSSIA	INS	Turbo Compressor Equipment	\$11,865,000	3%
SINGAPORE	LG	Large Aircraft	\$149,001,440	7%
THAILAND	LG	Large Aircraft	\$371,561,189	27%
TRINIDAD	INS	Medical Equipment	\$4,583,864	15%
TURKEY	LG	Industrial Equipment	\$14,505,523	13%
TURKEY	LG	Large Aircraft	\$175,100,000	16%
TURKEY	INS	Medical Equipment	\$2,048,675	15%
TURKEY	INS	Printing Equipment	\$1,100,058	15%
UKRAINE	LG	Agricultural Equipment	\$3,108,406	15%
UKRAINE	LG	Agricultural Equipment	\$6,509,556	15%
UKRAINE	LG	Agricultural Equipment	\$2,417,901	8%
UKRAINE	LG	Agricultural Equipment	\$8,114,355	16%
URUGUAY	LG	Turbines	\$54,038,249	23%
USA	LG	Large Aircraft	\$65,276,250	18%
TOTAL			\$6,265,361,841	13%

*Data excludes Credit Guarantee Facilities.

**INS equals insurance and LG equals 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 or the transaction may be a cofinancing with another ECA.

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 2006, followed by a discussion of trends in the use of the TACPF through 2006.

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; 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 rules on country and project eligibility 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 has significantly declined (for more details and data trends see Chapter 5). In 1997 (and revised in 2005), Participants issued a document known as “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 World Bank 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

When considering the various forms of aid, it is important to differentiate between bilateral aid to be used at the discretion of the recipient; trade-related aid that typically involves procurement of capital equipment; and trade-distorting aid, which is aid provided with the intention that the recipient government will favor procurement from the donor's country. Specific definitions of the various forms of aid follow:

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). 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 contractually conditioned upon the purchase of goods and/or services from any particular country. This form of aid has historically fallen under the purview of the DAC rules, which differ from the Arrangement rules in that the DAC provides virtually no restrictions on untied aid use. However, the Helsinki Package includes some basic transparency requirements for untied aid. Therefore, there is a wide gap in multilateral requirements

³ The OECD Development Assistance Committee (DAC)'s technique for measuring concessionality (grant element) of ODA is antiquated, using a fixed 10% discount rate, and results in one half of annual ODA levels having a concessionality level below 25%, and some substantially less.

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

between these two differing forms of aid credits. The resulting ambiguity has been used for commercial advantage by foreign untied aid donors.⁵

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 \$3,465 (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

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 2006, the data showed that there were 140 Helsinki-type tied aid notifications, which was a decline from 163 in the previous year. By value, 2006 Helsinki-tied aid offers totaled \$4.4 billion, which was a decline of 20% from 2005 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.

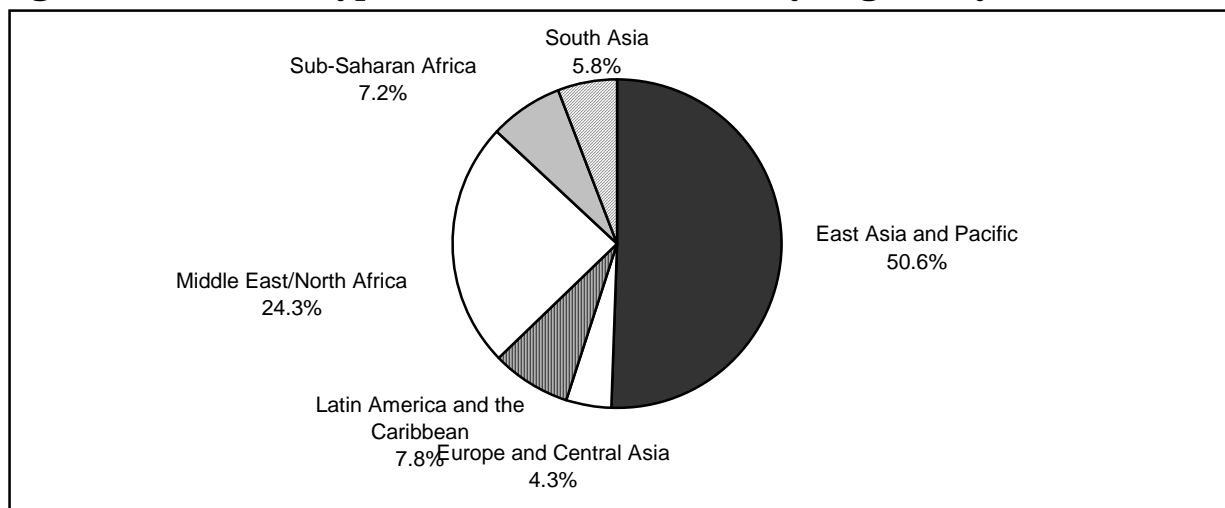
With respect to untied aid, in 2006, Participants agreed to renew for two more years the pilot transparency agreement that they had originally accepted in 2004. In short, the U.S.-proposed agreement requires donors to: (a) make their offers public to allow for competitive international bidding; and, (b) report the nationalities of bid winners on an annual ex post basis. It is a means of developing data that could 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 development 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

⁵ DAC rules were developed decades ago. The nominal level of grant element that qualifies as ODA must be 25%. However, current DAC methodology allows the real level of concessionality to be much lower than 25% (e.g., 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 to update the methodology.

the transparency agreement on January 1, 2005, but it is now extended through the end of 2008 to allow more procurement data to be collected. Without sufficient data, the U.S. will have a difficult time confirming that untied aid is trade distorting.

Figure F1: Helsinki-type Tied Aid Notifications by Region (by Value), 2006



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.

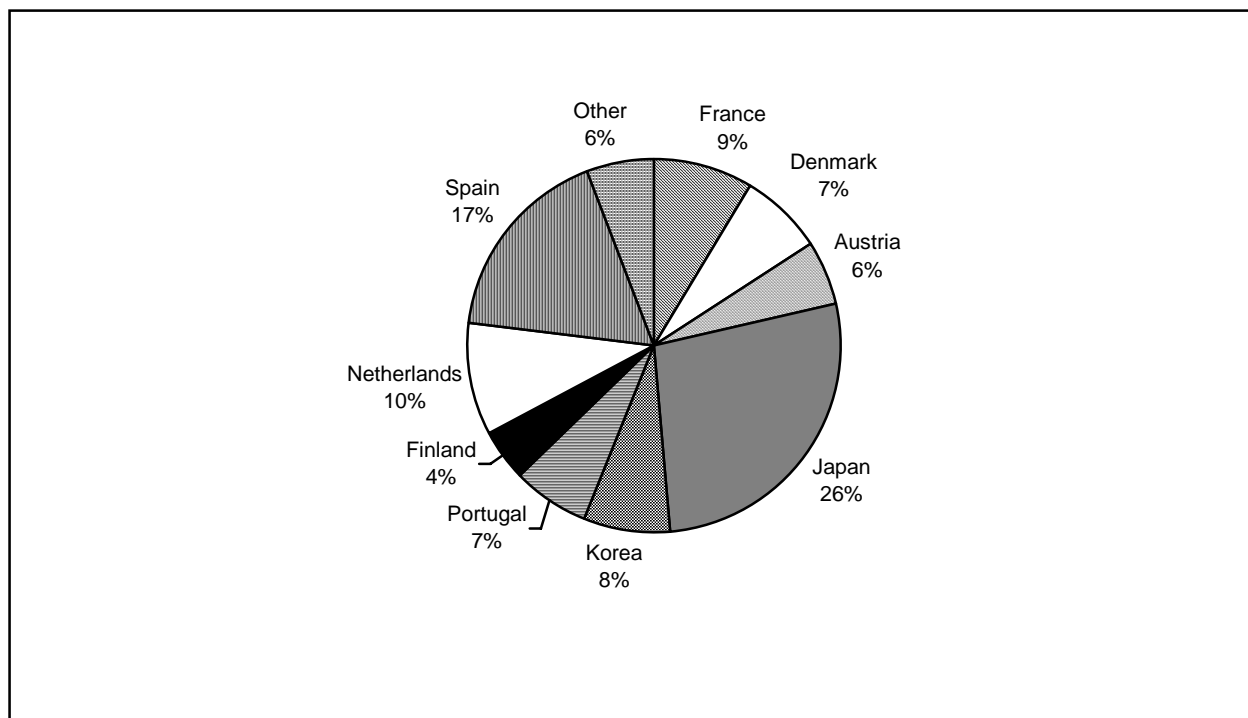
Figure F1 shows the distribution of Helsinki-type tied aid offers by region in terms of value. In 2006, the major beneficiary region was the East Asia and Pacific region (50.6% of all Helsinki-type tied aid). The most significant recipient – Vietnam - was in this region and was offered \$1.6 billion (or 36% of all Helsinki-type tied aid). The next largest recipient was Egypt⁶ with \$565 million, followed by Indonesia with \$340 million.

Figure F2 shows the variety of donor countries that offered tied aid in 2006. Japan was the largest donor country of Helsinki-type tied aid – with the Spain, Netherlands, and France trailing far behind and by a notable margin. While Spain was a large donor the previous year, in 2006, its support of Helsinki-type tied aid was roughly 45% of

⁶ In 2006, there were multiple matching notifications for two separate tied aid projects in Egypt. As it is unclear whether these offers are mutually exclusive, the stated figure may overstate the actual amount of tied aid offered for Egypt.

2005 levels. By comparison the United States did not notify any Helsinki-type tied aid in 2006.

Figure F2: Helsinki-type Tied Aid Notifications by Donor (by value), 2006



As far as sector concentration, during 2006, Helsinki-type tied aid 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 one Participant as eligible for tied aid, but which another Participant believes to be *ineligible* for tied aid because it appears 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 don't **require** them, or an unnecessary subsidy is being introduced and trade distortion is occurring. As **Figure F3** illustrates, the Consultations Group has not examined many projects in recent years.

Of the 2,588 tied aid projects notified to the OECD from March 1992 to June 2006, 133 projects were examined by the Consultations Group. Of the 133 projects examined, 71 projects were found to be CV or ineligible for tied aid. The remaining cases were found eligible for tied aid based on a variety of factors, including lack of commercial or standard export credit term financing in the market. Of the 71 projects deemed ineligible for tied aid, 43 projects proceeded with other financing sources, including tied⁷ and untied aid, commercial financing, and standard export credits. See **Annex 3** for a list of projects generally considered CV, for which tied aid is prohibited. See **Annex 4** for a list of projects generally considered commercially non-viable, for which tied aid is permitted.

⁷ The OECD rules require tied aid donors who elect to proceed with a tied aid offer that was deemed ineligible for tied aid to provide a letter from their government to the OECD Secretary General indicating the Participant's intent to derogate from a Consultations Group finding. Three derogations have occurred since the rules were established and all three derogations occurred in 1992.

Figure F3: Notifications of Helsinki Tied Aid and Consultations Group Examinations, 1992-2006

Year	Number of Notifications	Number of Projects Examined by the Consultations Group	Number of Non-compliant Projects
1992	128	39	16
1993	138	25	12
1994	262	31	21
1995	226	14	4
1996	212	4	3
1997	195	2	2
1998	191	5	5
1999	213	2	1
2000	181	4	4
2001	123	2	1
2002	136	1	0
2003	128	2	1
2004	145	0	0
2005	166	2	1
2006	140	0	0
Totals	2,584	133	71*

*Of the 71 “non-compliant” cases (i.e., cases deemed commercially viable and, therefore, ineligible to receive tied aid by the OECD Consultations Group), 21 were abandoned and 43 proceeded within Arrangement procedures or on commercial terms. The disposition of the remaining 7 cases is presently unknown.

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 significant future benefits, as well.

Ex-Im Bank has issued 4 tied aid matching offers since 2000, with the most recent one in 2002. **Figure F4** shows cumulative offers since 1992, and compares the offers and

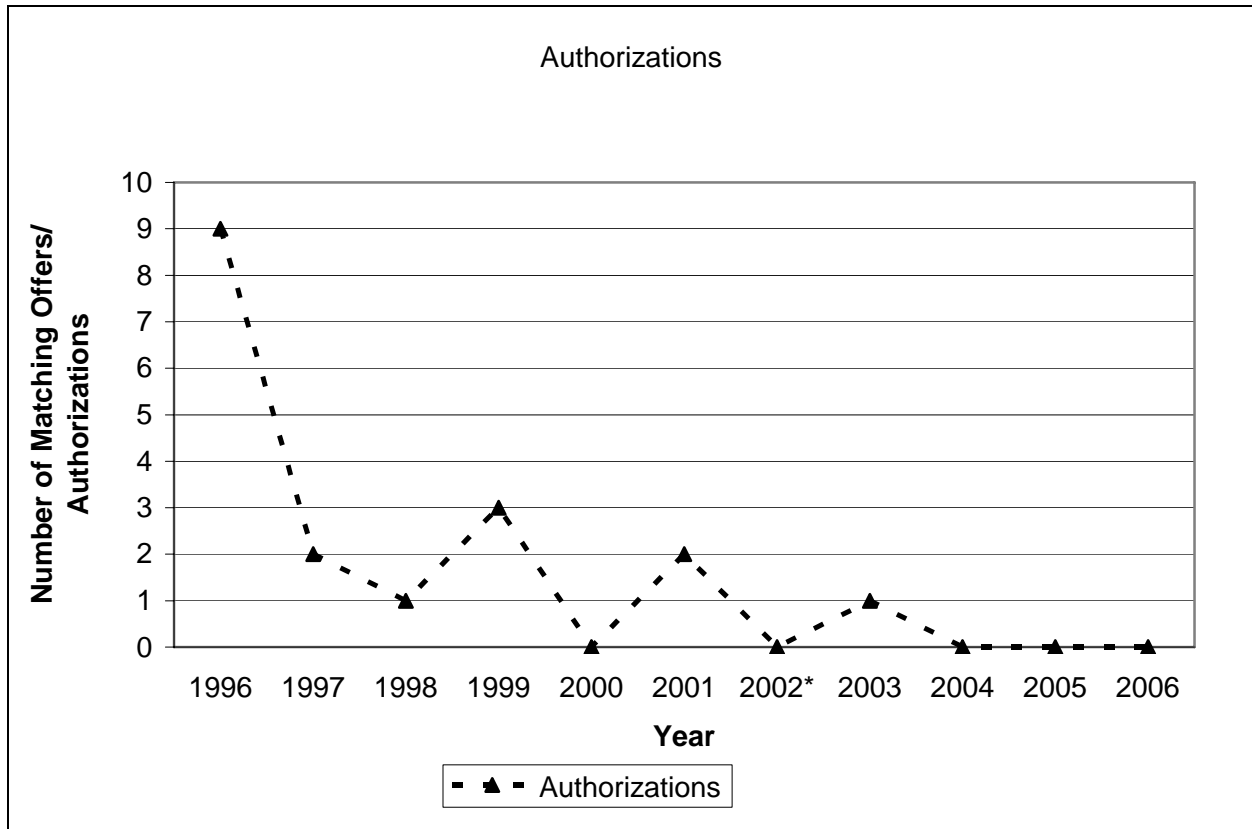
outcomes from the years 1992-1999 to the 2000-2006 period. The period-to-period comparison shows a dramatic drop-off in the number of tied aid offers. Since 2000, Ex-Im Bank has matched four cases (compared to 40 in the years 1992-1999); of these four cases the United States won 2 and lost 1, with one case remaining outstanding with no decision. In 2006, Ex-Im Bank did not issue any new tied aid commitments.

Figure F4: Cumulative Ex-Im Bank Matching of Previously Notified Foreign Tied Aid Offers, 2000-2006

	2000	2001	2002	2003	2004	2005	2006	1992-1999	2000-2006
New matching offers	1	2	0	1	0	0	0	40	4
U.S. win	17	19	19	19	19	19	19	16	2
U.S. loss	23	23	23	24	24	24	24	21	1
Outstanding, no decision	1	1	1	1	1	1	1	3	1
Cumulative total	41	43	43	44	44	44	44	40	4

As shown in **Figures F4 and F5**, 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 2006. 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 1997-2006.

Figure F5: U.S. Tied Aid Authorizations by Year, 1996-2006



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. The reasons for requesting a common line can vary, but one reason is to determine if another OECD Member is considering supporting the same project. If so, that Member will reject the common line and the initiator of the common line will have confirmed what it set out to confirm. However, if all OECD Members accept the common line, then aid is prohibited for that project for a renewable two year period and one’s exporter is free to compete for the project on commercial terms without fear of encountering foreign tied aid competition. Acting upon an Ex-Im Bank proposal, the OECD Members may approve “no aid” agreements for particular projects of interest to U.S. exporters that could otherwise receive tied aid under the OECD rules. With such agreements in place, U.S. exporters can compete without concern about tied aid competition and without the need for Ex-Im Bank to provide a matching tied aid offer. 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. **Figure F6** shows the results of the no aid common line requests initiated by Ex-Im Bank from 2000 through 2006.

Figure F6: U.S. Proposed No Aid Common Lines (2000-2006)

	2000	2001	2002	2003	2004	2005	2006	2000-2006
Proposed	8	1	0	3	2	1	0	15
Rejected	5	0	0	1	1	1	0	8
Accepted	3	1	0	2	1(*)	0	0	7

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. The results of the bid are not yet known.

It is worth noting that, although the no aid common line is ostensibly a practical way to coordinate donor activity and to limit aid to projects that truly need concessional financing to go forward, in practice, U.S. exporters sometimes do not want a common line proposed on their behalf because they fear that the buyer will penalize the U.S. exporter for its role in seeking to limit the concessional funds available to that buyer (so-called “buyer-backlash” against the U.S. exporter seeking to win the bid on standard - rather than concessional - terms). Although common lines are intended to be anonymous to prevent this situation, in practice, buyers are often aware of which donors/exporters are competing for specific projects and, consequently, they know who proposed the common line.

(*)For example, a recently accepted U.S. proposed no-aid common line resulted in subsequent bidding difficulties for the U.S. exporter who lost the sale (despite the fact that it had previously sold equipment on commercial terms). The U.S. exporter claimed to be shut out of the market as a result of the U.S. common line. Moreover, the buyer contacted Ex-Im Bank seeking assurances that the U.S. would no longer interfere with bilateral aid offers from third countries.

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.

Appendix F Annex 1

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. (These countries had a GNI per capita above \$3,255 in 2004 and \$3,465 in 2005).

**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 non-financial 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 of human rights concern. Countries not on that list are pre-cleared. Where a proposed transaction over \$10 million dollars 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 2007, 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 2006, Ex-Im Bank has 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

The Trade Promotion Coordinating Committee (TPCC) is an interagency committee that is comprised of 19 U.S. government agencies.¹ The committee was formed from the enactment of the Export Enhancement Act of 1992, which founded it with the object of harmonizing U.S. government export promotion activity under the leadership of the Secretary of Commerce. In addition, the President and Chairman of the Export-Import Bank serves as the Vice-Chair of the TPCC. The TPCC agencies involved are considered to be critical to the achievement of progress on the Administration's goal of maximizing U.S. export potential.

One of the main tasks the TPCC is responsible for is the creation of the National Export Strategy (NES) report, which is delivered to Congress annually and delineates the Administration's trade promotion agenda. In its most recent form, the 2006 NES report highlights the increased ease of exporting today as barriers to trade slowly dissolve due to improved trade negotiations both at the multilateral and bilateral levels; the more concentrated interconnectedness among those in the commercial community due to technological and physical infrastructure improvements; and an expanded and easily-accessed resource base to assist U.S. exporters in their endeavors. Most importantly, the report emphasizes the value of interagency coordination and linking government at all levels with the U.S. private sector to strategically involve the business community in target markets. Those achievements stemming from TPCC action that concerned Ex-Im Bank in 2006 are briefly discussed below.

Highlights of TPCC Accomplishments during 2006

Among the several achievements seen by the TPCC in 2006, several that are particularly noteworthy involved Ex-Im Bank. These include:

- Ex-Im Bank's City/State Partners Program, a national marketing initiative that brings export financing services to more SMEs through closer cooperation with state and local governments and private sector organizations. Ex-Im Bank now has 45 City/State partners in 35 states and the Commonwealth of Puerto Rico. Ex-Im Bank staff have quantitative

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.

goals for adding new partner relationships, including City/State Partners. Six new partners, representing a 10 percent increase, have been added in recent months in Hawaii, California, Idaho, Michigan, Delaware and West Virginia. This program adds to the rolls of the SME exporters that Ex-Im Bank supports each year and greatly enhances Ex-Im Bank's reach nationwide.

Partner training, supply of marketing materials and banner displays are routine components of the City/State initiative. Ex-Im Bank develops state-specific direct mail campaigns with select interested partners utilizing targeted mail lists provided by the City/State Partner. Nearly 25,000 pieces were mailed during FY2006¹. The City/State Partners, including Ex-Im Bank's regional business development staff, promptly follow up with respondents. City/State Partners also identify exporters and organize solo or joint marketing meetings with Ex-Im Bank business development officers to insure awareness of financial tools that are available in support of international sales."

Ex-Im Bank Partners Program: Ex-Im Bank has incorporated extensive use of partners into its strategy to reach the broadest possible universe of U.S. exporters. Specifically, the Bank's SME strategy not only employs the use of partners, but features an active effort to expand the partner groups. Ex-Im Bank's financial products, designed to expand U.S. exporting activity, fit into the business model of many financial institutions, export credit insurance brokers, City/State partners, industry associations and the USEACs of the Department of Commerce. Ex-Im has developed close working relationships with these partners to make its trade finance products more widely known and available. Long-time key lender partners include JP Morgan Chase, Comerica Bank, Silicon Valley Bank, PNC, Bank of America, UPS Capital and M&T Bank.

FY 2006 marked a record (nearly \$3.2 billion) in direct financial support for SMEs, representing 26% of total Ex-Im authorizations – also a record. Key to this success was the continuing growth of Ex-Im Bank's Working Capital Guarantee Program, largely administered by delegating authority to the lending banks to achieve faster approval.

During FY2006, due to the concentrated efforts of the Bank's Business Development Division, the multiplier network of financial institutions, brokers and City/State partners increased over 10% to more than 300 enterprises nationwide. Supplementing this success has been the continuing excellent cooperation with the USEACs and the Small Business Administration. Ex-Im Bank/SBA collaboration on working capital transactions was renewed and extended for another five years during

² Ex-Im Bank figures are reported on a USG Fiscal Year (FY) basis while the TPCC NES Report is conducted on a Calendar Year (CY) basis.

FY2006. Over \$45 million of U.S. exports were supported by Ex-Im Bank/SBA co-guaranteed transactions during the most recent year of activity. Ex-Im Bank and the SBA also agreed to a joint marketing arrangement that will feature shared use of customer data bases as a means of expanding, through collaboration, the universe of financial institutions offering programs from both agencies.

- Ex-Im Bank has developed and implemented “Ex-Im Online” – an online system for processing and issuing credit insurance and guarantees. These programs support export sales by U.S. companies to overseas corporate customers that require short term credit or medium term financing in connection with their purchases of products and services. Ex-Im’s short term credit insurance program is heavily focused on providing support to small and medium-sized businesses and Ex-Im Online is designed to expand and improve services to this segment of the U.S. exporting community. As it evolves, Ex-Im’s online system may provide U.S. exporters, particularly SME’s, with greater opportunities to make the extension of short term trade credit a more customary and widely available e-commerce payment option.
- Ex-Im Bank has made a concerted commitment to increasing its financing support for sales of U.S. goods and services to the countries in sub Saharan Africa. In FY 2006 as compared to FY 2005, Ex-Im Bank’s authorizations increased 22% from 115 to 140 transactions. Amounts authorized also rose 15% from \$462 million in 20 countries to \$532 million in 23 sub-Saharan countries.

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.

Ex-Im Bank responded to the Congressional mandate in a variety of ways during 2006:

Under the leadership of Ex-Im Bank Director Linda Conlin, Ex-Im Bank continued to successfully market the extended repayment terms (up to 15 years) available under the OECD Special Financial Terms and Conditions for Renewable Energies and Water Projects that went into effect on July 1, 2005 ¹.

Specifically, in 2006 Ex-Im Bank authorized approximately \$9.8 million of support for renewable energy technologies in the form of guarantees, insurance and working capital guarantees (compared to \$16.8 million in authorizations in FY 2005). That is, in FY 2006, U.S. renewable energy equipment for solar and wind energy projects as well as services for geothermal plants benefited from Ex-Im Bank support. Included in this total were authorizations of three insurance transactions totaling \$1.5 million to support exports of wind and solar energy products, an authorization for a financial guarantee of \$7.8 million covering the sale of equipment for a solar energy project, and an authorization for a working capital guarantee of \$450,000 that will support nearly \$2 million of services for renewable geothermal power projects. In addition, Ex-Im Bank authorized a working capital guarantee totaling \$13.5 million that will support exports totaling approximately \$80 million for equipment to produce photovoltaic devices that will be used for solar energy conversion.

Further, Director Conlin continues 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 participated in a number of outreach and marketing events intended to promote renewable energy exports. Participation in these events involved organizing panels, making presentations, meeting with individual exporters and meeting potential buyers.

Specifically:

- Two well-attended clean technology conferences in California in November 2006;
- Direct marketing outreach;
- Targeted trade shows; and
- New marketing materials such as flyers, brochures, and displays with new branded image and tagline.

¹ The agreement was accepted for a two-year trial period set to expire in June, 2007, and was subsequently extended until June, 2008. 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."

Finally, as part of a continuing effort to showcase environmental success stories, in 2006, The Robbins Company was named Ex-Im Bank's Small Business Environmental Exporter of the Year. The Robbins Company is a small business that designs and services tunnel boring, hydroelectric, sewer rehabilitation and irrigation machinery.