

**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, 2002 THROUGH DECEMBER 31, 2002**

JUNE 2003



EXPORT-IMPORT BANK
OF THE UNITED STATES

PRESIDENT AND CHAIRMAN

June 30, 2003

Dear Chairman Shelby and Chairman Oxley:

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, 2002 through December 31, 2002.

Sincerely,

A handwritten signature in cursive script, appearing to read "Philip Merrill".

Philip Merrill
Chairman

The Honorable
Richard C. Shelby
Chairman, Committee on Banking, Housing and Urban Affairs
United States Senate
Washington, D. C. 20510

The Honorable
Michael G. Oxley
Chairman, Committee on Financial Services
United States House of Representatives
Washington, D. C. 20515

**THE 2003 ADVISORY COMMITTEE'S STATEMENT ON THE
2002 COMPETITIVENESS REPORT OF
THE EXPORT-IMPORT BANK OF THE UNITED STATES**

The members of the 2003 Advisory Committee have reviewed the 2002 Competitiveness Report to Congress and would like to put forward the following statement on the competitiveness of the Bank with regard to the other major export credit agencies (ECAs). In the Advisory Committee's opinion, the Bank continues to fulfill its objective of supporting the creation and maintenance of U.S. jobs.

The Advisory Committee supports the findings and conclusions of the Report that Ex-Im Bank is competitive, and in some cases, highly competitive with its G-7 ECA counterparts. Specifically, we agree that Ex-Im Bank's core financing elements such as interest rate, premia/exposure fees, and cover policy are the "best of the breed." However, in those situations in which public policy or philosophical issues arise, the Report aptly notes that the conditions of Ex-Im support can result in significant competitive challenges to U.S. exports – conditions of support that our ECA counterparts are not required to impose. Nevertheless, the Committee recognizes the importance of public policy in its broad scope.

The individual element over which Ex-Im has primary control that appears to be lagging behind its ECA counterparts is co-financing. In addition, the basis for determining eligibility for tied aid to counter foreign offers seems particularly onerous from the U.S. exporters' perspective. Accordingly, the Advisory Committee strongly urges the Bank to both take the necessary steps to establish a co-financing program, and to provide more workable parameters for the use of tied aid.

The Advisory Committee commends Ex-Im Bank's effort to respond to the 2002 Advisory Committee's recommendation to quantify the overall and the element-by-element competitiveness of the Bank vis-à-vis the G-7 ECAs. The "scorecard" approach used represents a valuable and communicative yardstick that we hope will be repeated in future Reports. While some modifications/refinements to the scoring system may be appropriate, the scorecard presented serves as a basis for future comparisons. The Advisory Committee also applauds the reorganization the Bank undertook in 2002. The reorganization will provide an improved response to its customers' needs as well as greater accountability for performance.

To conclude, in a highly volatile, vulnerable and uncertain international environment, U.S. exporters need every possible tool to effectively compete, and Ex-Im Bank seems to have generally fulfilled that mandate during 2002. Looking ahead, the Advisory Committee supports the effort of the export community in pressing Ex-Im to adapt to a changing world more rapidly and fully. Hence, the Advisory Committee believes that while Ex-Im Bank needs to maintain its competitiveness in the core financing elements, it must also be looking for ways to provide more value to the U.S. exporting community by repositioning itself and leveraging its core competencies in the future.



Edward A. Monto
Chairman
2003 Ex-Im Bank Advisory Committee

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Executive Summary

The 2002 Competitiveness Report provides an evaluation of the competitiveness of Ex-Im Bank's medium- and long-term programs during 2002 based on objective and subjective information gathered from multiple sources. Included in these sources are views from a survey of the U.S. exporting community and data from the public resources of the OECD and G-7 export credit agencies.

This year's report provides a contextual backdrop of the international trade and finance landscape within which Ex-Im Bank and the G-7 export credit agencies (ECAs) operated during 2002, noting trends and competitive implications for Ex-Im Bank going forward. The most significant trends appear to be:

- Activity levels are still below long-run trends (although up from the reduced levels of last year) with an increasing percentage of aircraft in overall volumes.
- The growing globalization of production has created multiple sourcing options for U.S. companies.
- The nature of the demand for ECA financing is changing (e.g., from sovereign to private sector and smaller sized borrowers).

Our G-7 counterparts appear to have noticed and have begun to react to these influences. Specifically, the other G-7 ECAs can be characterized as trying to:

- Provide the highest quality products and service to their respective exporting communities without jeopardizing financial goals and reputational risk. This trend seems to have manifested itself in:
 - Aggressive pursuit of ECA differences and flexibility in the Arrangement;
 - Niche use of "sweetener" features and initiatives; and
 - Continued focus on streamlining operations.
- Proactively and strategically pursue opportunities to ensure a presence in key markets and favored sectors – a form of industrial policy.

As part of this context, a brief comparative overview of the philosophical and operational tactics of our G-7 counterparts is provided, highlighting core differences that have yielded varying programmatic approaches. From these dissimilarities emerge the outstanding competitive issues facing Ex-Im Bank and the U.S. exporting community, most of which involve larger national policy concerns not within the sole control of Ex-Im Bank. The key aspects where empirical and/or anecdotal evidence indicate a less than competitive position for Ex-Im Bank financing are (in rough order of priority and wide differences of importance): shipping/PR 17, foreign content, economic impact, tied and untied aid and market windows.

SUMMARY OF 2002 COMPETITIVENESS REPORT FINDINGS

Core Financing

Ex-Im Bank is considered generally competitive (i.e., equivalent to, if not *the*, best of the G-7 ECAs) in the core financing elements of a given transaction. In particular, Ex-Im Bank's cover policy and risk attitude are generally considered as open as, and in some aspects more open than, our foreign counterparts. Moreover, the risk premia Ex-Im Bank charges for sovereign and non-sovereign risks are fully competitive with those offered by our counterparts. Finally, market financing generated by Ex-Im Bank's 100% unconditional guarantee almost always provides U.S. exporters with a least-cost financing rate.

Program Structures

Ex-Im Bank's project finance, aircraft and foreign currency guarantee programs are considered as competitive as, if not better than, our foreign counterparts. Co-financing, however, is an area in which Ex-Im Bank is seen as lagging significantly behind our European counterparts, due to the limited number of co-financing agreements the Bank has been able to forge thus far.

U.S. Economic Philosophy

Tied aid (which includes "effectively tied" untied aid) and market windows financing collectively present a slightly different competitive challenge to Ex-Im Bank and the U.S. exporting community. Here the conflict is philosophical rather than financial. That is, with both tied aid and market windows there is a fundamental and long-standing U.S. philosophical reluctance to engage in the activity.

The United States rejected state capitalism some 200 years ago as incompatible with the U.S. economic model; similarly, the United States rejected tied aid some 35 years ago as an inefficient and inappropriate means to provide either development aid or commercial support. Hence, the United States has focused for decades, both in policy and in practice, on eliminating these problems (or, at a minimum, achieving greater disciplines) through negotiation. This strategy has had considerable success in the tied aid area; however, in the market windows area, there has been no success in achieving transparency or discipline. The issue today is discerning from conflicting information whether Ex-Im Bank financing is successfully meeting whatever (and it is not clear that there are many) competitive needs of U.S. exporters exist in these areas.

Public Policy

The public policy issues as a group present the most significant competitive challenge to Ex-Im Bank and the U.S. exporting community. That is, the U.S. public policies relating to economic impact, shipping and content all require Ex-Im Bank to consider the longer-term implications for the broader stakeholder population (e.g., interests of other agencies, labor, NGOs, etc.) when supporting specific exports using U.S. taxpayer funds. In effect, Ex-Im Bank operates its programs under both explicit and implicit political (i.e., Congress) guidance on the broader political and economic cost-benefit analysis of a specific export. The competitive impact stems

from the fact that other G-7 ECAs have very little in the way of similar constraints. These policies clearly exert a negative impact of some proportion on the Bank's competitiveness, and the U.S. export community rates these policies collectively as the number one disincentive to using Ex-Im Bank and therefore the number one competitive hindrance on the Bank.

OVERALL

This report has introduced the concept of the report card to facilitate and better communicate comparisons between Ex-Im Bank and the other G-7 ECAs in specific categories and overall. On a grading scale from A+ to F, with A being generally competitive, Ex-Im Bank's core financing terms receive an A. However, the philosophical and public policy areas slightly reduce Ex-Im Bank's overall grade to an A-. See **Figure 1** for the competitive definitions of select grades.

Figure 1: Ex-Im Bank Report Card Definitions

Grade	Definition of Select Grades
A+	Fully competitive: equivalent to (or is) the best competitor
A	Generally competitive: in almost all cases equivalent to the typical G-7 competitor
A-	Selectively competitive: in most cases equivalent to the typical G-7 competitor
B+	Marginally competitive: in significant minority of cases equivalent to the typical G-7 competitor
B	Notch below: can, but only rarely, package a deal equivalent to the typical G-7 competitor
C	Much less competitive: can/does provide a product in the class but is rigidly constrained (or little used)
F	Does not provide program

Ch. I 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 2002.

METHODOLOGY

In comparison to previous years' Competitiveness Reports, this year's report takes a different approach to evaluating Ex-Im Bank's competitiveness vis-à-vis its foreign export credit agency (ECA) counterparts. The 2002 Competitiveness Report distinguishes the core financing elements from the public policy aspects of Ex-Im Bank financing and evaluates the impacts of each on Ex-Im Bank's competitiveness. By parsing out the various elements that come to bear on Ex-Im Bank financing, the Report attempts to provide a more insightful evaluation of Ex-Im Bank's competitiveness. With this structure, the Bank better fulfills its Charter mandate to "indicate in specific terms the ways in which the Bank's rates, terms, and other conditions compare with those offered from such other governments directly or indirectly."

In preparing this report, Ex-Im Bank drew upon: (1) objective policy, programmatic and procedural information about other ECAs obtained from a variety of sources; and (2) subjective information provided by the U.S. exporting community based on transactional experience throughout the calendar year 2002. The Bank is required by its Charter to conduct an annual survey of exporters and lenders to determine their experience in meeting competition supported by public export finance. Notwithstanding a lower response rate than usual (see **Appendix C**), those that did complete the survey are comprised of highly experienced members of the U.S. exporting community. Moreover, in addition to the annual survey of the export community, this year's report also incorporates the results from two focus groups held with commercial lenders and exporters. The purpose of the focus groups was to provide 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 and transactional experience. Hence, the views obtained from the survey and the focus groups appear to be representative of the U.S. exporting community's assessment of Ex-Im Bank's competitiveness.

SCOPE

The comprehensive comparison is primarily limited to the G-7 ECAs, because these countries have typically accounted for roughly 80% of the medium- and long-term official export credits offered by the Organization for Economic Cooperation and Development (OECD) countries. Given the practices of certain non-G-7 ECAs in specific areas, such as tied aid, this report also provides insight, where relevant, into the activity of these ECAs and their impact on the competitiveness of the U.S. export finance community. In all cases, the focus is on medium- and long-term credits, as this sector is the locus of support for capital goods exports and therefore the arena with the most intense international competition. In addition, only a few of the official ECAs continue to provide short-term financing assistance; hence, a comparison of competitiveness in this area would be of limited utility. Quantitative comparisons and information on each of G-7 ECAs can be found in Chapter 2 Section A regarding trends in export finance.

EX-IM BANK CHARTER RENEWAL

The U.S. Congress renewed Ex-Im Bank's Charter through September 30, 2006. The Act was amended in several areas. Those amendments that directly affect either this Report itself or Ex-Im Bank's ability to provide competitive and comparable financing assistance are specifically noted below and are described in more detail in the specific sections in the body of the Report devoted to the individual topic.

1. Charter changes pertaining to the annual Report to the U.S. Congress on Export Credit Competition and the Export-Import Bank of the United States (the Competitiveness Report):
 - The requirement for the preparation and presentation of this Report was amended with a date certain for final delivery of June 30 each calendar year.
 - The Competitiveness Report is to include a competitive assessment of the use of market windows by other governments and government-related entities and the impact on U.S export competitiveness.
 - Ex-Im Bank is to use all available sources of information to estimate the annual amount of export financing available from each government and government-related agency.
 - The Competitiveness Report must include a description of all Bank transactions classified according to their principal purpose, such as to correct a market failure or to provide matching support.
 - Ex-Im Bank must report on its efforts to promote the export of goods and services related to renewable energy sources.

2. The topics noted below represent new or modified language to Ex-Im Bank's Charter and are discussed in more detail in this Report:
 - Economic impact
 - Tied aid and untied aid
 - Market windows

REPORT

The Report proceeds in the following sequence: Chapter 2 lays out both long-term trends that have changed the export finance market over the past decade and short-term patterns affecting ECA financing in 2002. A broad overview of the other G-7 ECA philosophies and missions is also provided for context. Chapter 3 consists of separate sections evaluating Ex-Im Bank's competitiveness in the core financing elements of official export credit support. Chapter 4 provides a comparative assessment of how well the financing elements are packaged into major programs (e.g., aircraft, project finance, co-financing and the foreign currency guarantee). Chapter 5 addresses overarching U.S. economic philosophy regarding tied aid and market windows. Finally, Chapter 6 evaluates stakeholder considerations embodied in public policies and the long-term competitive implications of these policies on Ex-Im Bank activity. The main body of the Report concludes in Chapter 7 with an overall competitiveness report card grading Ex-Im Bank against its G-7 ECA counterparts, based on the collective evaluation of financing, economic philosophy and public policy elements. A number of appendices follow the body of the Report, including a summary of the state of play of international negotiations on export credit issues, the exporter and banker survey summary and other materials intended to provide greater detail and insights.

Ch. II Competitiveness Framework

Section A: Factors Influencing Export Finance

THE PLAYING FIELD

This chapter examines the context within which the developed country official ECAs operate by addressing the multilateral rules governing official export finance, long-term trends affecting financing sources and more recent market developments.

The U.S. government is a Participant to the Arrangement on Guidelines for Officially Supported Export Credits, or the “Arrangement.” Housed within, but not a formal act of, the Organization for Economic Cooperation and Development (OECD), these guidelines set the disciplines for official export finance and serve as the basis upon which member governments cooperate to minimize the use of government subsidies in export finance. A “gentleman’s agreement,” the Arrangement has been incorporated into European Union law and is referred to in the World Trade Organization’s (WTO) Agreement on Subsidies and Countervailing Measures; if a WTO member country adheres to the interest rate (and related) rules of the Arrangement, its official export credits will not be considered prohibited subsidies¹. Since the inception of the Arrangement twenty-five years ago, Participants have established disciplines related to market oriented interest rates, a harmonized risk differentiated fee regime, the use of tied aid and limitations on the length of repayment terms for officially supported credits, in addition to special sector agreements on ships, large commercial aircraft and nuclear power.

The U.S. exporting community has clearly benefited from Arrangement rules. The financing rules have succeeded greatly in leveling the competitive playing field, directing competition to the quality and price of the product and not the nature of the official financing package. However, while the multilateral export credit regime has increasingly codified the financing elements of official export credit support, that success has highlighted a fairly significant disparity in the application of public policy goals to official export credits.

Numerous sources have raised the profile of public policy issues within the ECA world, from the environment to the IMF’s Highly Indebted Poor Country (HIPC) initiative, including local and international pressure from non-governmental organizations and international events such as the 2002 United Nations World Summit for Sustainable Development. The different missions and places of ECAs within governments (see Chapter 2, Section B) have led to vastly differing responses to such pressures from civil society. On one end of the spectrum, some ECAs, such as Ex-Im Bank, work under numerous statutory public mandates, and some ECAs, such as ECGD, are tied with inter-ministerial consultation on public issues. Conversely, other ECAs operate within governmental systems that more rigidly compartmentalize responsibilities. These ECAs provide export credit support in ways that could contradict or undermine goals supported by their own national governments in other fora. In other words, the multilateral export credit regime

¹ The Arrangement has come under increased scrutiny by the WTO over the past several years in the ongoing Brazil-Canada aircraft disputes and in the Doha Round of the WTO. This has led the Participants to the Arrangement to undertake a redrafting of the Arrangement. See **Appendix E** for more information.

currently disciplines the financing elements of ECA support and assures a fairly level playing field. However, the absence of comparable weighting and less attention to public issues by guardian authorities tilts the playing field against those ECAs with public policy constraints

LONG-TERM EXPORT FINANCING TRENDS

Another important context for any evaluation of Ex-Im Bank's (or any ECA's) performance is that the stated role of ECAs has changed dramatically over the last couple of decades. As seen in **Figure 2**, official G-7 ECA activity is generally declining, and ECA financing of total national exports has dropped from 15%-20% to 3%-5% over the past two decades. Today, ECAs cede deals to the private market much more often than to each other.

Four key trends have been observed in the nature of export finance. The first major trend has been an increase in local import financing. As large banks' appetite for cross-border risk has declined with crises such as Latin America in the 1980s and Asia in the 1990s, local banking capacities in emerging markets have gradually expanded. The entrance of multinational banks has advanced this trend into emerging markets. With localization of banking markets, and globalization of banks, many traditional ECA markets have been wiped out, with China the most notable example.

A second key trend has been increased privatization in emerging markets. The sell-off of state enterprises in major utilities and infrastructure to private entities has resulted in an increased flow of foreign direct investment, displacing the need for traditional export credits as a source of capital for investment. Privatization has also expanded local capital markets by, for example, parceling out purchasing decisions in small enough chunks for local finance to digest.

Third, new players have entered the export finance market. Major exporters have established their own finance entities, while capital market participants have used structured finance approaches to mitigate the risks of lucrative projects in many markets. In addition, multilateral development banks have created programs to lend directly to private sector borrowers in emerging economies, while the private political risk insurance market has expanded. All of these players have reduced the need for ECA financing.

Fourth, the core ECA markets have stagnated. From the 1950s to the 1980s, as one group of core buyers graduated from needing ECA support, a new group would usually arise. In the 1990s, however, this pattern deteriorated, with the same group of countries remaining as the core ECA buyers but demand decreasing due to the aforementioned three factors.

This shift from being a core player to being a critical yet marginal player (e.g., in riskier markets or cases) has considerable impact on the operational effectiveness and efficiency of any ECA committed to being both a lender of last resort and a rule abiding member of the international community (e.g., OECD and WTO). In effect, the basic question facing ECAs today is how, within specific national policies and institutions, to structure programs and staff to both fulfill national missions and international responsibilities. For Ex-Im Bank, the pressing issue is how to be competitive (with the bulk of demand increasingly in riskier situations) and break even

over the longer term (both institutionally and case-by-case). The variety of responses to this question across ECAs is one of the major competitive issues today and will likely be an ever more challenging factor in the competitive landscape in the years ahead.

TRENDS IN 2002: FOCUS GROUP DISCUSSIONS

This section summarizes the views shared by U.S. exporters and bankers at the focus group meetings on export finance trends.

The focus group members collectively painted a picture of a politically and economically volatile, somewhat unpredictable international marketplace undergoing considerable changes. If the U.S. export finance community is to compete, these trends will likely dictate changes in their strategies and business models. Globally, focus group participants explained that Ex-Im Bank financing continues to play an important role in supporting U.S. exports, especially for longer term, large amounts and in higher risk markets. In other words, ECAs generally are still viewed as the most reliable risk management tool available for the riskiest and most expensive transactions and projects. However, in less extreme circumstances, the risks associated with many of the emerging markets are increasingly considered acceptable to private sector financial intermediaries due to the development and implementation of more sound legal, accounting and financial systems.

In addition to private sector finance, an ever broadening menu of financing options exists for the U.S. exporting community, including multilateral development banks, such as the EBRD and the World Bank's IFC, and other ECAs, via market windows, untied aid and, to some extent, co-financing. These options reflect the trend toward greater globalization that continues to permeate virtually every industrial sector in the capital goods arena, with significant impact on the U.S. exporting community's strategic decisions. The exporters explained (with the lenders confirming) that the production of goods and services has shifted from a supply chain supported predominantly by U.S. components and semi-finished goods to processes characterized by vertical specialization. This involves the fragmentation of the production process over national boundaries and can take the form of: (1) a supply chain that is increasingly reliant on foreign parts that are incorporated or assembled here in the United States; (2) a supply chain that includes U.S. content but is produced offshore; or (3) sourcing that occurs entirely outside of the United States (primarily through a number of offshore production facilities of multinationals).

The exporters are regularly faced with decisions regarding sourcing options in the near term, in addition to the longer term issue of whether, where and when production locations should be established. In any event, many large U.S. multinationals, including the larger engineering and design companies, as well as a growing number of medium-sized corporations, have sourcing capabilities outside of the United States that they utilize when production and cost efficiencies dictate. Products that were formerly made domestically are now more an amalgamation of components from multiple sources, many of which are outside U.S. boundaries either because the United States no longer has a comparative advantage or the parts are simply no longer manufactured domestically. Hence, the multinationals have the ability to source either from the

United States a product that has relatively less U.S. content or to source from offshore production facilities with or without U.S. content.

Given the changes in production and sourcing options, financing options are being developed that align more closely with the newer business models. The major ECAs appear to be adapting to the more globalized approach to production and sourcing, accommodating exporter needs with relatively greater flexibility in foreign content support and the implementation of insurance co-financing structures (with the exception of ECGD) with other government and private sector export credit insurers. EDC is the most notable example in terms of foreign content flexibility, while the other ECAs have focused on their co-financing capabilities. The U.S. exporting community noted that the absence of co-financing agreements forged between Ex-Im Bank and other ECAs, combined with a less flexible foreign content approach, is undermining their ability to compete from the United States.

Overall, the exporting community considers Ex-Im Bank an essential partner in its competitive pursuit of global market share. However, as the pace of globalization continues to change the international landscape, U.S. businesses are changing their models in order to adapt and compete on the basis of price, quality and service. The new business models which U.S. corporations are being forced to adopt are characterized by multiple sourcing options and therefore require that export finance support be similarly aligned.

The convergence of an uncertain political and economic landscape, the materialization of more attractive emerging markets, and the globalization of production have together yielded an international marketplace in which official ECAs must redefine their role so as not to be marginalized. This redefinition is leading to a metamorphosis that began to emerge in the 1990s, with 2002 revealing ECA strategies characterized by the development of “precision-point” program features, such as local currency financing, designed to exploit untapped areas of opportunity.

SUMMARY DATA

This data was accumulated from a variety of public sources. Moreover, the individual ECA data probably contain transactions outside the definition of “official” export credit (e.g., market window financing).

A review of G-7 medium- and long-term export credit volumes from 1995 to 2002 suggests a slight recovery from 2001, when support dropped to its lowest level during the seven-year time period. The 2002 upturn of 3% still does not bring the G-7 activity up to the recent historical average of approximately \$45 billion.

In any event, ECAs still play an important role, and, as the data indicate, Ex-Im Bank is solidly and consistently one of the top players in medium- and long-term support. It should be noted however, that aircraft plays an increasing role in ECA activity. For example, in 2002, 45% (or \$3.8 billion) of Ex-Im Bank activity was attributable to large aircraft transactions alone. Support

for aircraft was also a significant factor in the business activity levels for Coface, Hermes and ECGD. In fact, aircraft was probably 33% of all G-7 activity in 2002.

Figure 2: G-7 New Medium- and Long-Term Official Export Credit Volumes (\$Bn)

	1995	1996	1997	1998	1999	2000	2001	2002*
Canada	1.9	2.8	5.1	4.5	4.1	5.2	5.5	5.0
France	10.5	6.6	6.6	8.4	5.4	4.5	4.1	6.4
Germany	9.8	13.6	11.3	8.3	6.7	9.8	5.7	5.4
Italy	3.3	1.2	1.7	1.0	1.6	2.6	0.7	2.5
Japan	13.7	10.2	11.3	11.9	14.9	18.5	16.1	12.0
U.K.	3.5	2.5	3.8	3.2	5.1	5.8	2.3	3.3
U.S.	7.8	8.0	9.4	6.6	9.4	9.6	6.8	7.7
Total G-7	50.5	44.9	49.2	43.9	47.2	56.0	41.2	42.3
U.S. % G-7	15.3%	17.8%	19.1%	15.0%	19.8%	17.2%	16.5%	18.2%

**Preliminary results*

Ch. II Competitiveness Framework

Section B: ECAs' Mission and Place in Government

THE CHANGING ROLE OF EXPORT CREDIT AGENCIES

An export credit agency's mission and its place in government determines its business strategies and practices and the extent to which public policies play an important role in its overall business model. Moreover, an ECA's ability to adapt to changing market circumstances is also heavily influenced by its relationship with its national government and the public goals set for it by its government and specific guardian authorities. While the OECD Arrangement codifies many of the terms that apply to official export credit support, individual ECAs have significantly varying degrees of freedom from broader considerations in pursuing their strategies to support domestic exports.

The next section analyzes Ex-Im Bank's mission and role in government and the resultant impact of this broader context on Ex-Im Bank's ability to respond to market pressures. Following the analysis of Ex-Im Bank is an overview of the context in which other G-7 ECAs operate.

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 the parameters within which it is required to operate are codified in its Congressionally approved Charter (Export-Import Bank Act of 1945, as amended), which was most recently renewed during the summer of 2002 with the next expiry date of September 30, 2006.

Ex-Im Bank's core mandate is to provide export financing that is competitive with the official support offered by other governments. The public policy goal of this mandate is to enable market forces such as price, quality and service to drive the purchase decision, not government intervention or temporarily exaggerated perceptions of risk. 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. Within this broad mandate, Congress has also mandated that Ex-Im Bank follow additional directives. The more significant mandates include:

- Ex-Im Bank should supplement, not compete with, the private sector.
- Decisions on transactions should be based solely on commercial and financial considerations, i.e., the finding of a reasonable assurance of repayment, with the exception of:
 - Environment;
 - Adverse economic impact on the U.S. economy; and
 - Various statutory and executive branch parameters.

All of these requirements have a public policy basis and tend to reflect the views 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 our foreign government counterparts – counterparts that most often have fewer public policy constraints to evaluate when deciding whether to provide financing support. Thus, the formula with which to compare Ex-Im Bank’s competitiveness against our major ECA counterparts is neither simple nor direct, including both quantitative and qualitative components, as embodied in public policy considerations.

THE MISSION AND PLACE IN GOVERNMENT OF OTHER G-7 ECAS

Each of Ex-Im Bank’s G-7 ECA counterparts operates with unique goals and supporting strategies; hence, there is a spectrum of strategies and operating styles. Nevertheless, there are several broad motivational themes with which each ECA can be associated that helps in understanding the differences in levels of activity, products and focus.

Lender of Last Resort: Perhaps the only other G-7 ECA that compares similarly to Ex-Im Bank, in that its primary role is as a lender of last resort, is ECGD of the UK. ECAs with this focus tend to encourage the active participation of the private sector and step in only when taxpayer dollars are needed to meet market gaps. Moreover, lenders of last resort tend to assume a relatively higher level of responsibility for public policy goals as directed by their guardian authorities.

Private Sector Participant: The European ECAs, most notably Coface and Hermes (but also SACE), take on a private sector demeanor due largely to the fact that they are private entities that handle the medium- and long-term book of business on behalf of their respective governments. Driven largely by profit, the controls placed on and the risk profiles of their portfolios tend to be more restrictive (with country exposure limits), resulting in moderate risk-taking. Operationally, many of the European ECAs behave as private sector companies by taking advantage of the efficiencies associated with their private sector side. Finally, the assumption of public policy goals tends to carry less weight for these ECAs because of their narrow focus.

Banker for the Country: For various reasons the Canadian and Japanese ECAs tend to see themselves as the only international bank of any scale in their respective countries. This larger role in the implementation of national trade policy tends to be reflected in broader missions (e.g., national content on specific sales is less important) and more expansive responsibilities.

Ch. III Core Business Policies and Practices

Section A: Cover Policy and Risk-Taking

INTRODUCTION

Cover policy refers to an ECA's willingness to provide protection against commercial and political risks in a particular market. ECAs' cover policies and risk-taking practices significantly impact an exporter's ability to effectively compete for sales. Cover policy decisions are based on an ECA's underwriting approach and its consideration of whether and how to place limits, in terms of risk type or volume, on the business it can support. Limits on transaction size, repayment terms or total commitments per country are the methods many ECAs use to control the flow of new business.

An ECA's approach to non-sovereign risk is another important aspect of cover policy. Exporters whose ECA is willing to take on new business with entities other than sovereign governments or first class private institutions can enter markets and gain competitive advantages over foreign competitors. While most ECAs have historically covered sovereign, public and major bank business, increasing privatization in the developing world has presented ECAs with increasing requests to cover private risks, ranging from large corporations to small businesses. The scope and depth of an ECA's willingness to cover private sector risk, especially of small private entities, has become a more critical competitive aspect of an ECA's cover policy.

EX-IM BANK'S COUNTRY COVER POLICY AND PRACTICE

When open in a market for a given term, Ex-Im Bank is less risk averse than other ECAs in its willingness to extend credit to buyers, including smaller, private entities. In addition, U.S. exporters and banks benefit from the absence of country and sector ceilings on Ex-Im Bank's cover policy.

U.S. exporters realize these advantages because Ex-Im Bank takes a different approach to country cover policy than most ECAs. The goal for Ex-Im Bank is to provide financing for creditworthy export transactions, regardless of destination, when there is foreign ECA-supported competition or when private sector financing is unavailable. In other words, restrictions on the provision of Ex-Im Bank cover in a given market pertain to the creditworthiness issues of a transaction, as opposed to portfolio controls. Ex-Im Bank will typically support transactions without size or country limits as long as there is a reasonable assurance of repayment (and additionality) in each transaction. One exception is when Ex-Im Bank is statutorily prohibited from doing business in a particular market, generally as a result of sanctions.

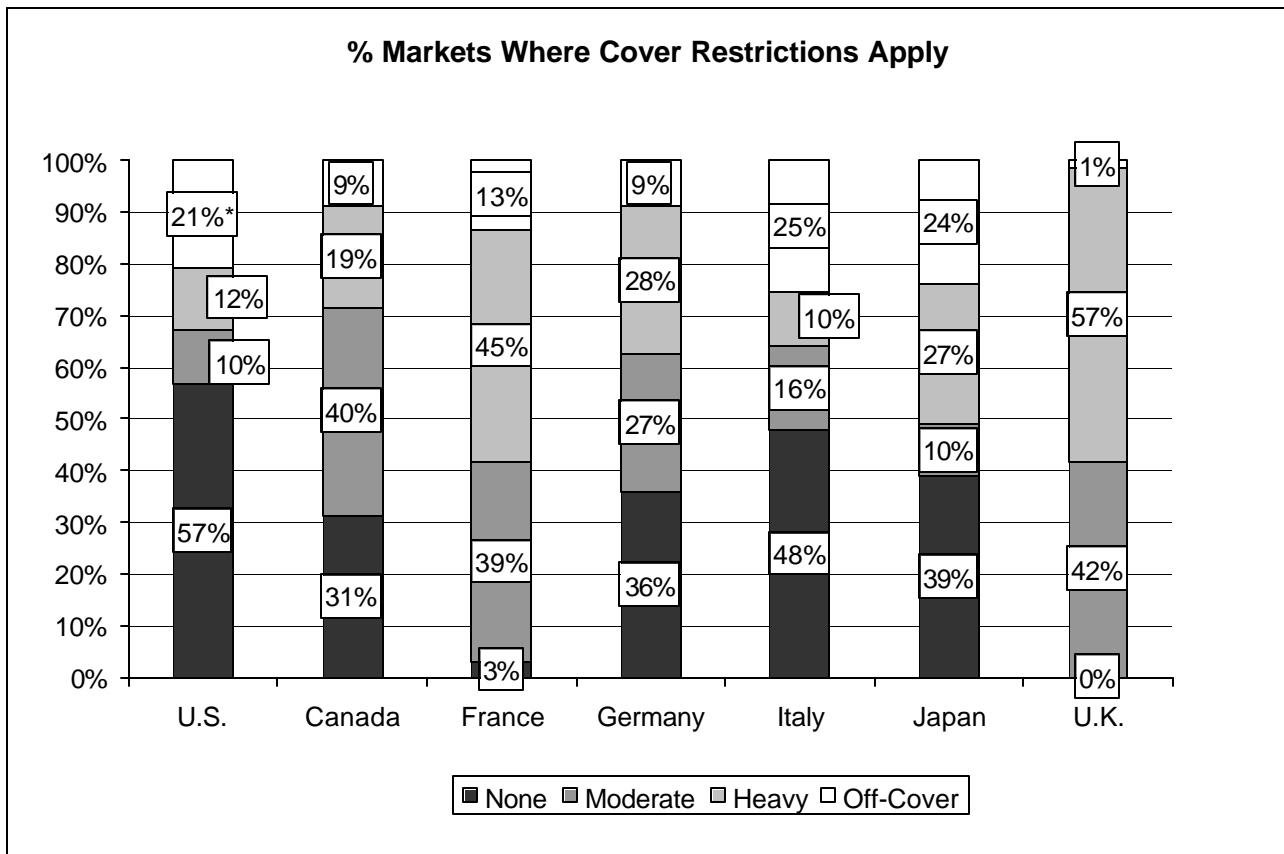
With respect to risk-taking practices, Ex-Im Bank shows a willingness to cover the risk of smaller, private entities and seeks to minimize the requirement for bank guarantees and other forms of security in order to reduce the associated costs of these guarantees to U.S. exporters.

G-7 ECAs' COVER POLICIES AND PRACTICES

Other G-7 ECAs are willing to take on sovereign government risk; however, with respect to private sector transactions, these ECAs tend to be risk averse. They control their risk appetite for private sector business by, for example, imposing country and/or sector exposure limits. In addition, they prefer to focus on well-known or rated entities (which are usually banks) or rely (by requiring risk-sharing of 5%-20%) on the due diligence and underwriting approaches of the banks they cover. The other G-7 ECAs are also facing new challenges with underwriting an increasing demand for cover of private sector risk in emerging markets undergoing privatization efforts.

SUMMARY DATA

Figure 3: Comparison of Medium- and Long-Term ECA Country Cover Policy



*In 6% of the 67 markets, Ex-Im Bank was closed due to legislative sanctions.

Figure 3 shows the overall openness of the G-7 ECAs by comparing cover policy in 2002 for a sample of 67 major ECA markets. As illustrated, there is a difference in approach to overall cover policy and the degree to which ECAs are willing to assume unsecured risks. Specifically, Ex-Im Bank is open in more markets than any of the other G-7 ECAs. Further, relative to its major competitors, Ex-Im Bank generally imposes far fewer restrictions on the provision of cover than other ECAs. Ex-Im Bank is off cover in 21% of the 67 markets; however, Ex-Im Bank was closed for business in 6% of the sample markets due to legislative reasons.

With respect to ECAs' risk-taking practices, **Figure 4** provides a broad characterization of the G-7 ECAs' risk appetite for business with less well-known private entities, as opposed to large corporations or bank guaranteed borrowers.

Figure 4: ECA Risk-Taking Practices

Taking Credit Risk of Smaller, Less Well-Known Private Entities in a Market:				
Never----->Infrequent----->Frequent----->				
NEXI and JBIC (Japan)	ECGD (U.K.)	SACE (Italy), Coface (France), Hermes (Germany)	EDC (Canada)	Ex-Im Bank

Most G-7 ECAs continue to prefer to offer support to well-known or rated entities or rely on risk-sharing to minimize exposure to smaller, private entities. Conversely, Ex-Im Bank is more comfortable taking the risk of smaller, less well-known private entities than competitor ECAs and does not follow other ECAs in their risk-sharing practices.

EXPORTER AND BANKER VIEWS

Banks and exporters were asked to comment on the competitiveness of Ex-Im Bank's country cover policy and risk-taking practices vis-à-vis its competitors. Respondents agreed that "Ex-Im Bank is ahead of the game in risk-taking practices [and] it's the best ...in communicating what risks it will take." One bank noted that Ex-Im Bank is "more willing to do sub-sovereign and corporate risk" than other ECAs. In addition, an exporter stated that "Ex-Im is the best [and it] should protect and maintain its cover policy." On the other hand, exporters noted that legislative sanctions have an adverse impact on their access to markets where there is other officially supported ECA competition.

CONCLUSION

Ex-Im Bank continues to be generally competitive in its cover policy and risk-taking practices. Once Ex-Im Bank is open in a market for a given repayment term, U.S. exporters and banks benefit from the lack of country and sector ceilings that other ECAs place on their cover policies. The one exception to this rule is in the few markets where Ex-Im Bank is statutorily closed yet other ECAs are open. Additionally, Ex-Im Bank is less risk averse in its willingness to extend credit to smaller private entities.

Ch. III Core Business Policies and Practices

Section B: Interest Rates

INTRODUCTION

A key component of the competitiveness of an export finance package is the interest rate that the buyer is charged. Accordingly, early in the life of the OECD Arrangement on Guidelines for Officially Supported Export Credits, member countries established a minimum interest rate to be charged when a member ECA is lending to the buyer (either directly or by providing funding support to a lender). The minimum interest rate, referred to as the Commercial Interest Reference Rate (CIRR), is a fixed, market-related rate that is calculated using the government's fixed rate borrowing costs plus a fixed spread of 100 basis points. The OECD Arrangement contains procedures for offering, setting and holding the CIRR for official lending. Over the past several years, officially supported fixed interest rates have been of declining importance to overall competitiveness, with only 35% of ECA long-term financing support in 2002 offered using official fixed interest rates (including both direct lending and interest make-up systems), as compared to 53% in 1997.

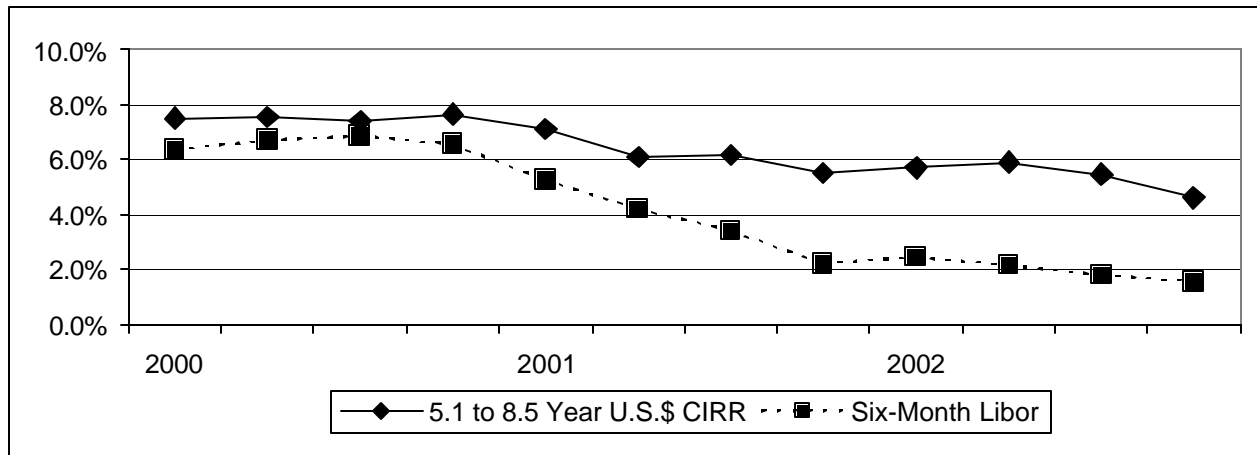
EX-IM BANK'S POLICY AND PRACTICE

Ex-Im Bank provides official support through both a direct lending product and two pure cover² (guarantee and insurance) products. The interest rate for direct lending is set using the CIRR procedures detailed in the OECD Arrangement. Monthly, Ex-Im Bank calculates the U.S. dollar CIRR for three different repayment term scenarios (up to five years, over five to eight and a half years, and over eight and a half years) and uses the current rate (or a previously offered rate that meets the "holding" procedures defined in the OECD Arrangement) to set the interest rate for any direct loans authorized during the month. This interest rate then becomes the fixed interest rate for the life of the transaction, including the construction, drawdown and repayment periods. Because a floating rate CIRR has not been established in the OECD Arrangement, Ex-Im Bank only lends at a fixed interest rate.

For pure cover interest rates, the rate is set by the lender, not by Ex-Im Bank or by reference to the OECD Arrangement. Under pure cover, the interest rate may be either fixed or floating, and it may contain the flexibility to switch from a pure cover floating rate to a pure cover fixed rate at the lender's and buyer's discretion. Generally, a floating rate pure cover interest rate will be based on LIBOR and have a spread in the range of 0 to 100 basis points (for larger transactions) or 20 to 400 basis points (for smaller transactions).

² Definition: official support that covers private bank lending and does not involve the provision of interest rate funding support by the ECA.

Figure 5: Comparison of CIRR and LIBOR Interest Rates



Buyers tend to prefer using Ex-Im Bank's pure cover products because of the greater level of flexibility in the products and (thanks to the generally declining interest rates over the past decade) the lower interest rates that can currently be achieved on a floating basis (see **Figure 5**). Reflecting this tendency, in 2002 less than 3% of the more than \$8 billion authorized under the medium- and long-term programs was for direct loans.

G-7 ECA'S POLICIES AND PRACTICES

Generally, Ex-Im Bank's competitors offer similar products: direct loans, insurance and guarantees (see **Figure 6**). While only Ex-Im Bank offers all three products, five of the six other G-7 ECAs have a mechanism for offering both CIRR rates and pure cover, and all but Germany regularly offer official fixed rate support. However, three of the five do so through banks, using an interest make-up program (IMU). IMU is a means by which governments compensate commercial banks that provide fixed rate export finance at CIRR but fund the cost of loans at floating rates. The commercial bank receives an agreed rate of return based on the floating cost of funds plus an agreed margin. If this return proves to be higher than the fixed rate CIRR, the commercial bank receives the difference between the fixed rate and the floating rate (plus the margin). If the floating rate is lower than the fixed rate, the commercial bank pays to the ECA the difference between the floating rate and the fixed rate (less the margin).

Figure 6: ECA Product Offerings

	Loan	Guarantee	Insurance	IMU
Canada	X	*	X	
France		**	X	X
Germany	X	**	X	
Italy			X	X
Japan	X		X	
United Kingdom		X		X
United States	X	X	X	

* In response to Canadian bank complaints, Canada has recently begun to offer, on a limited basis, a guarantee program.

** Both France and Germany will offer a guarantee for Airbus aircraft transactions.

The CIRR regime represents a common set of rules that should not yield an inherent advantage or disadvantage for any particular country. However, there is the potential for a certain degree of subsidization (either of the administrative costs of banks offering export finance loans or of the interest rate charged on the portion of the financing not covered by official financing support) via IMU schemes. See **Figure 7** below for a comparison of indicative returns to banks under CIRR and IMU.

Under most IMU systems, the floating rate base rate of LIBOR or EURIBOR is used. The spreads range from about 40 to 90 basis points. There are no agreed rules on the level of spreads that governments may offer their banks to provide CIRR loans. The rationale for the level of margin and the purposes for which the margin is intended vary from country to country. Generally, IMU support is offered to cover administrative costs. In some programs, the IMU margin is used to provide a pure profit margin or to cover liquidity costs. The coverage of credit risk is also a major use of IMU margins, including the risks associated with the portion of the financing package that is not covered by the official financing support, i.e., the risk of the 5% portion that the bank must cover. In any case, use of the IMU system has a competitive component to it as the profitability can induce better (or more) “side” financing or terms on the core financing.

On pure cover transactions, the interest rates charged when support is provided by one of the other G-7 ECAs are generally higher than those charged when Ex-Im Bank is providing guarantee support. Banks lending under Ex-Im Bank’s guarantee take no risk on the guaranteed portion due to the fact that the guarantee is a 100% comprehensive unconditional guarantee. In contrast, most other ECAs offering pure cover only offer 95% conditional insurance cover. Under a conditional insurance policy, the commercial bank faces documentary risk, i.e., the validity of a claim will not be determined until the claim is filed. In addition, the commercial bank is exposed to credit risk when the ECA cover is less than 100%. Faced with such risks, most lenders add additional spread over any standard return requirement on official export credits. For instance, spreads on European insurance cover are generally in line with their IMU

spreads, varying between 45 and 90 basis points but averaging closer to 70 to 80 basis points. See **Figure 7** below for a comparison of indicative returns to banks under 100% and 95% cover.

SUMMARY DATA

Figure 7: Indicative Pricing of ECA Supported Export Credit Deals

	Cost of Funds	Interest Rate Charged	Margin to Commercial Bank
Fixed Rates:			
CIRR*	N/A	4.05%	N/A
IMU	Libor	4.05%	75 bp
Floating Rates:			
100% Pure	Libor	Libor + 20 bp	20 bp
95% Pure	Libor	Libor + 62.5 bp	62.5 bp

*5.1 to 8.5 year CIRR as of December 31, 2002

EXPORTER AND BANKER VIEWS

Banks and exporters commented in greater depth this year, as opposed to previous years, on the competitiveness of interest rates associated with Ex-Im Bank financing. From the banks' and exporters' points of view, the CIRR rates offered by Ex-Im Bank are competitive with the CIRRs offered by other ECAs. However, several banks raised concerns about the competitive impact of interest rate make-up systems and how such systems provide excess fee income to the European banks, which may be used to cross-subsidize the uncovered cash payment portion. On pure cover interest rates, the majority of both exporters and banks indicated that interest rates under the Ex-Im Bank guarantee were more competitive in comparison to rates supported by other ECAs.

CONCLUSION

Overall, the extent and depth of ECA competition in the basic area of official interest rates has been gradually declining for nearly two decades. However, differences in the application of that system offer the possibility of some ECAs gaining modest advantages in select transactions.

The use of IMU schemes by Ex-Im Bank's competitors puts Ex-Im Bank at a slight disadvantage on officially financed cases, as IMU can be used to lower the all-in cost of a financing package. On the other hand, Ex-Im Bank has a competitive advantage on pure cover cases with the low interest rates generated under its 100% guarantee cover. The net result is that Ex-Im Bank is generally equivalent to other G-7 ECAs in its ability to support competitive interest rates.

Ch. III Core Business Policies and Practices

Section C: Risk Premia

INTRODUCTION

ECAs charge exposure fees for taking the repayment risk of the borrower. Although many factors influence the all-in cost of an officially supported export transaction, the exposure fee, or risk premia, can constitute a considerable amount of the direct financing costs. In 1999, the OECD adopted the Knaepen Package, an exposure fee agreement that defined the elements for the determination of sovereign fees, including the establishment of the principle of minimum premium benchmarks (MPB) for sovereign risk transactions, below which, with some specific exceptions, ECAs may not charge.

The sovereign risk minimum premium formula is based on the following factors: (1) the percentage of cover (100% vs. 95%); (2) the quality of the product (unconditional guarantee vs. conditional insurance); and (3) the claims payment policy. The latter two factors determine whether a product is considered “above standard”, “standard” or “below standard.” For example, standard products include direct loans and insurance with no claims waiting period, whereas unconditional guarantees are considered above standard. The formula works such that above standard products are the most expensive, and below standard products are the least expensive. Beyond the MPB, the system allows each ECA to use its own fee system to determine whether additional surcharges need to be applied to sovereign transactions. Hence, a common floor exists, but ECAs may add a surcharge to the MPB according to their risk assessment process.

With regard to non-sovereign risk premia, ECAs may not charge less than the sovereign MPB in a given market. However, beyond that one stipulation, ECAs are free to charge any or no additional surcharge for a non-sovereign transaction. Consequently, exposure fees for non-sovereign risks can vary.

EX-IM BANK'S POLICY AND PRACTICE

Regarding sovereign risk premia, Ex-Im Bank's guarantee product is considered to be above standard due to its unconditional cover – the best coverage available. As a result, all other factors being equal, the minimum premium benchmark on an Ex-Im Bank guarantee would be nominally higher than the MPB charged by a competitor ECA that offers a standard product. Nevertheless, the all-in cost of all levels of MPBs is equivalent for pure cover transactions. That is, the lower MPB on standard products is paired with a higher spread over LIBOR, whereas the higher MPBs on above standard products is coupled with lower spreads.

For non-sovereign premia, Ex-Im Bank assesses risk by looking at the non-sovereign borrower's risk compared to the sovereign's credit risk. If the non-sovereign borrower, whether it is a bank or public or private entity, is viewed as having a similar or better repayment risk compared to the sovereign, the exposure fee charged would be the same as for the sovereign (i.e., the minimum

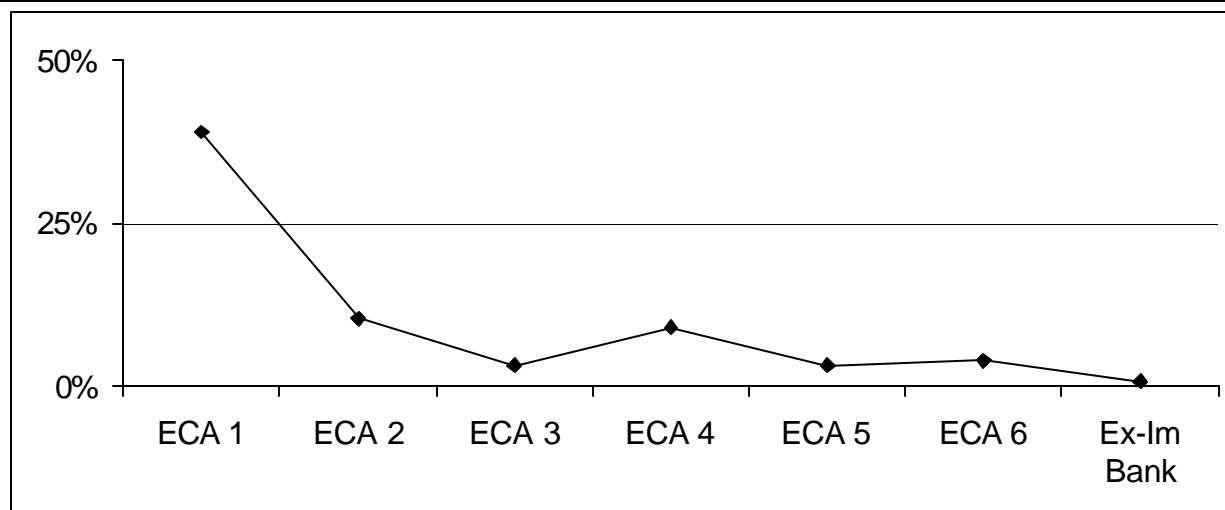
premium benchmark). On the other hand, if the risk is deemed to be higher, then incremental surcharges are added to the minimum exposure fees. Ex-Im Bank's non-sovereign fees tend to be relatively less expensive than those charged by our major counterparts (see below).

G-7 ECAs' POLICIES AND PRACTICES

While the Knaepen Package sets the floor for all sovereign and non-sovereign transactions at the MPB for sovereign risk, ECAs may use their own systems to determine if and under what circumstances surcharges are added. Generally, the insurer ECAs of Europe tend to add specific surcharges depending on the type of the borrower risk. For sovereign risk, most of the G-7 ECAs also add a modest incremental surcharge on many cases. For non-sovereign risk, the typical approach of European ECAs is based on categories of risk as opposed to specific buyer risk. For example, a first-rate bank would be charged the sovereign fee plus a surcharge based on its status as a commercial bank, while a private buyer would be charged the sovereign fee plus a higher surcharge based on its status as a private non-financial entity. On the other hand, Ex-Im Bank and most non-European ECAs price on a transactional basis, assessing a non-sovereign borrower's repayment risk case-by-case.

Figures 8 and 9 compare average exposure fee surcharges for the G-7 ECAs with Ex-Im Bank's pricing practices for sovereign and non-sovereign transactions respectively. As seen below, on average, Ex-Im Bank and most other ECAs charge exposure fees at or slightly above the minimum premium rate allowable for sovereign risk transactions. In addition, most ECAs impose surcharges for non-sovereign risk transactions. Some ECAs do so on a category basis while others use a risk-assessment basis.

Figure 8: Average MPB Surcharges on Sovereign Risk Transactions*



*2002 preliminary data

Figure 9: Sample MPB Surcharges on Non-Sovereign Risk Transactions

Sample Market	ECA	Surcharge
Brazil	ECA 1	87.0%
	ECA 3	25.0%
	ECA 4	17.5%
	ECA 6	9.2%
	ECA 2	2.2%
	Ex-Im Bank	0.7%
	ECA 5	0%
Philippines	ECA 1	157.2%
	ECA 3	30.0%
	ECA 6	26.2%
	ECA 4	15.5%
	ECA 2	14.6%
	Ex-Im Bank	10.5%
	ECA 5	0%

EXPORTER AND BANKER VIEWS

Banks and exporters were asked to provide feedback on the competitiveness of Ex-Im Bank's exposure fees, and most respondents agreed that Ex-Im Bank is competitive vis-à-vis competitor ECAs with respect to transaction pricing. Banks specifically stated that "recent OECD harmonization rules appear to have reduced the major pricing differentials" and that "exposure fees are competitive."

CONCLUSION

The Knaepen Package placed a sovereign-based floor on exposure fees, which creates a level playing field with respect to minimum exposure fees charged. While non-sovereign transactions must meet the same minimum sovereign rates, there can be significant differences in the surcharges ECAs impose. Ex-Im Bank offers very competitive exposure fees vis-à-vis the G-7 ECAs for both sovereign and non-sovereign risks.

Ch. III Core Business Policies and Practices

Section D: Ex-Im Bank's Core Competitiveness

Both collectively and independently, Ex-Im Bank's core financing elements are considered to be generally competitive with (and in many cases, more competitive than) those offered by our G-7 ECA counterparts. Evaluated on a global basis across all programs, Ex-Im Bank's core financing elements fall just short of an A+, or fully competitive. In fact, of the 65%-85% of transactions where CIRR is not relevant, the all-in cost associated with Ex-Im Bank's medium- and long-term financing is typically lower than the all-in cost of the other G-7 ECAs most of the time.

Figure 10: Grading of Ex-Im Bank's Core Competitiveness

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

Ch. IV Comparison of Major Program Structures

Section A: Large Aircraft

INTRODUCTION

In the context of officially supported export credits, large aircraft refers to airplanes with 70 seats or more³. Today there are two primary producers of large aircraft in the world: Boeing in the United States and Airbus SAS (Airbus) in Europe. Airbus is a corporation owned by two European aerospace companies: the European Aeronautic Defence and Space Company (EADS, the result of a merger in 2001 between Aerospatiale-Matra of France, DaimlerChrysler Aerospace of Germany and CASA of Spain) and BAE SYSTEMS of the United Kingdom. The Russians also build large aircraft; however, their products do not compete globally with U.S. and European-produced aircraft.

Because the financing requirements of large aircraft exports differ from other manufactured products (e.g., longer useful life may command longer repayment terms), there is a separate Annex to the OECD Arrangement setting forth the terms of, and procedures for, ECA-supported aircraft financings. The section of the Civil Aircraft Annex that pertains to large aircraft is known as the Large Aircraft Sector Understanding, or LASU. The principal participants to the LASU are the United States and the European Union, which, in this context, represents the interests of France, Germany and the United Kingdom.

The LASU establishes the terms, conditions and special guidelines of export credit support that OECD governments can extend to buyers of large aircraft. It sets a minimum cash payment of 15%, a market-based interest rate for loans extended by an export credit agency (set at 120 basis points and 175 basis points over 10-year Treasuries for 10- and 12-year repayment terms, respectively) and a maximum 12-year repayment term. It also limits the amount of spare parts that can be included in the financing package and bans ECAs from providing support into producer country markets (also known as “home market countries”, which historically have included the United States, France, Germany, Spain and the UK). Finally, the LASU prohibits tied aid financing for large aircraft.

Although Ex-Im Bank and the European ECAs that support the export of Airbus aircraft (i.e., ECGD of the UK, France’s Coface and Germany’s Hermes; collectively the “Airbus ECAs”) are subject to the same OECD guidelines, there have been differences in their respective export credit systems for large aircraft. These differences have enabled each side to capitalize on the relative strengths of its respective export credit system. For example, until the end of 2002, only the United States and the UK offered a 100% unconditional guarantee, which enabled the guaranteed lender to generate attractively priced financing. However, as further discussed below, historically all three Airbus ECAs adopted other policies (e.g., the three-year interest rate lock) that were intended to compensate for the shortcomings in their insurance product. Recently, the Airbus ECAs announced that it was their intent that all three would soon offer a

³ Comparably sized aircraft configured for cargo carrying purposes are included in the definition of large aircraft.

100% unconditional guarantee for financings of large aircraft and dramatically scale back the interest rate lock flexibility. Although differences in approach still exist, neither side appears to have a competitive advantage since the resulting financing is very comparable.

As illustrated in **Figure 11**, Boeing and Airbus have accounted for roughly equal shares of large aircraft orders over the past five years. This 50/50 split reflects the highly competitive environment in which aircraft manufacturers operate.

Figure 11: Orders of Large Commercial Jet Aircraft

	1998	1999	2000	2001	2002 ⁴
Boeing	656 (54%)	391 (45%)	611 (54%)	334 (47%)	251 (46%)
Airbus	556 (46%)	476 (55%)	520 (46%)	375 (53%)	300 (54%)
TOTAL	1,212	867	1,131	709	551

EX-IM BANK'S POLICY AND PRACTICE

Almost all Ex-Im Bank support for large aircraft transactions is done under Ex-Im Bank's guaranteed loan program. Under this program, Ex-Im Bank provides an unconditional guarantee on repayments of 100% of the principal of the loan plus interest at the contractual rate. As a result, this program results in attractively priced financing on the Ex-Im Bank covered portion of the transaction.

G-7 ECAS' POLICIES AND PRACTICES

In the past (and during the year 2002), the European ECAs allowed buyers of large aircraft to lock-in a fixed interest rate up to three years prior to delivery, provided the buyer entered into a purchase contract with Airbus. Buyers had the choice between this locked-in interest rate or another market-determined interest rate established between the time of contract signing and delivery of the aircraft. The effect of this approach was to provide a free interest rate option to buyers at no additional cost. This approach provided buyers with certainty of a maximum interest rate cost for up to three years prior to drawing down financing. In a volatile interest rate environment, the certainty of locking in an interest rate for up to three years in the future was a highly attractive feature to the buyers of Airbus aircraft.

Beginning in 2003, the Airbus ECAs announced that the "free interest rate lock" described above was being changed. In the future, a fixed interest rate could only be "locked in" under the

⁴ Boeing and Airbus received 75 and 67 cancellations, respectively, for a net of 176 and 233 orders, respectively, and a total of 409 orders.

following circumstances: (1) up to three or six months in advance of the delivery of the aircraft; (2) only if the fixed interest rate was the 12-year fixed interest rate (i.e., 175 basis points above the relevant benchmark); (3) only if “breakage costs” were paid in the event that the buyer decided not to use the “locked in” Airbus ECA supported fixed interest rate financing; and (4) only if all three Airbus ECAs had agreed to underwrite the transaction. Alternatively, the buyer of the aircraft could elect to use the Airbus ECAs’ pure cover program, which enables the buyer to choose either a fixed or floating interest rate, but it does not permit the buyer to set the fixed interest rate far in advance of the delivery date for the aircraft.

SUMMARY DATA

The downward trend in total commercial aircraft orders that began in 2001, and that is expected to continue over the near term, creates additional competitive pressure on both Boeing and Airbus to offer their customers products that meet technical specifications at the lowest possible price and at the most attractive financing terms available. This trend is highlighted by the increased ratio of foreign deliveries shown in **Figure 12**. In the year 2002, Boeing delivered 381 commercial aircraft (down 33% from last year) of which 178 (or 47%) were delivered to foreign buyers. Exports (by number of aircraft deliveries) have accounted for 30% or more of Boeing’s deliveries since 1999, and Ex-Im Bank supported exports were about one quarter of Boeing’s export deliveries during the 1999-2001 period. In 2002, exported aircraft accounted for a significantly larger share of Boeing’s commercial activity, and Ex-Im Bank played a significantly larger role, financing more than 41% of its deliveries in 2002, in supporting those exports.

Figure 12: Deliveries of Boeing Commercial Jet Aircraft (by number of aircraft)

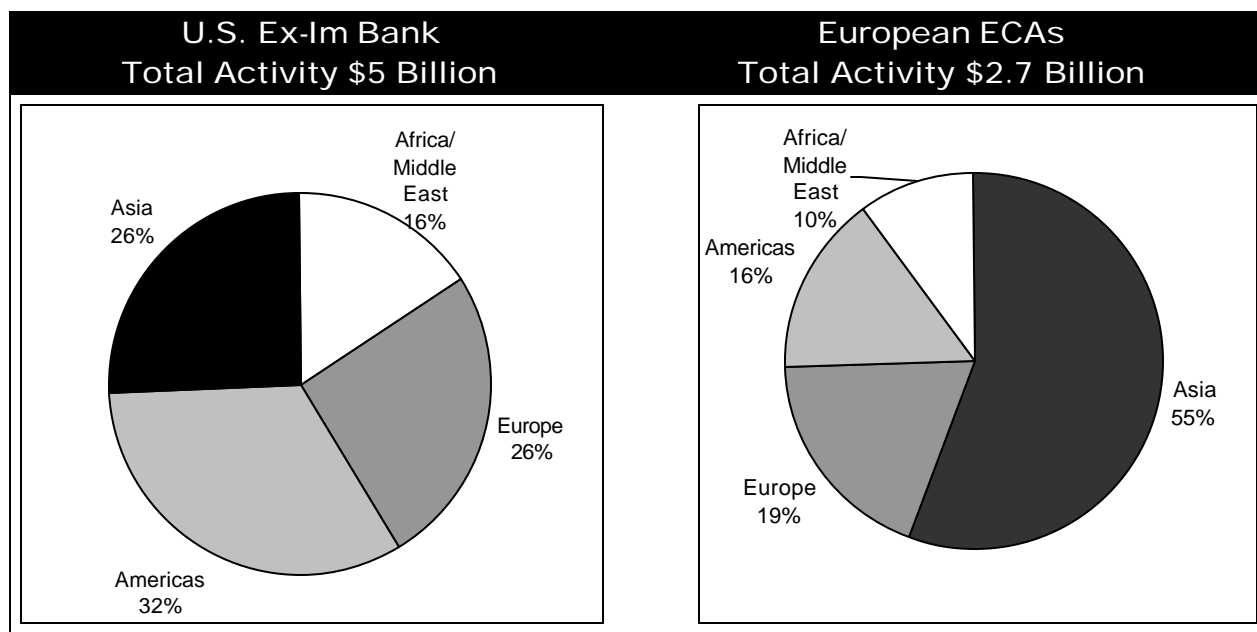
	1999	2000	2001	2002
Domestic	356 (57%)	283 (58%)	363 (69%)	203 (53%)
Foreign	264 (43%)	206 (42%)	163 (31%)	178 (47%)
% Of foreign deliveries supported by Ex-Im Bank	27%	27%	23%	41%
TOTAL	620	489	526	381

As shown in **Figure 13**, Ex-Im Bank and the European ECAs that support Airbus financed more than \$7.7 billion in large aircraft exports during the year 2002. The average volume of U.S. and European ECA supported large aircraft during the 1997-2001 period was \$9.0 billion. Hence, the lower volume of ECA supported aircraft in 2002 reflects the general downturn in worldwide aircraft sales.

In 2002, Ex-Im Bank accounted for \$5 billion (or 65%) and the European ECAs accounted for

\$2.7 billion (or 35%) of the \$7.7 billion total. Large aircraft transactions account for about one-half of Ex-Im Bank's and about one-quarter of Coface, ECGD and Hermes medium- and long-term activity.

Figure 13: 2002 ECA Support for Large Commercial Aircraft by Region



EXPORTER AND BANKER COMMENTS

In response to a survey that addressed the competitiveness of Ex-Im Bank programs and policies for large aircraft exports, Ex-Im Bank received comments that addressed several key issues. Specific comments included:

- The “financial” cost of Ex-Im Bank financing (i.e., interest rate and exposure fees) is competitive with the cost of financing provided by the European ECAs that support Airbus. On the other hand, the nature and cost of legal documentation associated with Ex-Im Bank financing appear to be more complex and more expensive when compared with the European export credit systems. [Note: In light of the European ECAs’ announcement to modify their official export credit financing structures for large aircraft transactions, the difference in legal documentary requirements is likely to fade away as the Europeans adopt financing structures similar to those of Ex-Im Bank.]
- With respect to foreign content, the European ECAs provide more flexibility (for example, the European ECAs finance the cost of U.S. engines on Airbus aircraft). Ex-Im Bank’s willingness to allow foreign content to be calculated on an aggregated basis provides limited benefit to large aircraft transactions but does not address the

fundamental problem of increasing non-U.S. content in aircraft and installed engines. Increasing the maximum foreign content allowance (without a reduction in cover) would be the single most meaningful policy change that would assist in leveling the playing field with Airbus and the European ECAs.

- Regarding market windows (see Chapter 5, Section B), the response to the survey indicated that the lack of transparency associated with financing provided by Germany's KfW prevents a definitive assessment of how market windows impact U.S. competitiveness. Nevertheless, anecdotal evidence suggests that KfW is a very significant presence in support of Airbus aircraft. Consequently, it is believed that one area where Ex-Im Bank "market window" financing could be useful, particularly in the current environment where commercial financing is very scarce, may be in "home markets."

CONCLUSION

Ex-Im Bank financing for large aircraft exports is generally competitive with financing offered by its European counterparts. While the comments from the export community indicated that certain elements of Ex-Im Bank financing could be improved upon (e.g., lower legal fees and increased support for foreign content) the export community did not cite inferior Ex-Im Bank financing as a reason for lost U.S. export opportunities.

Over the next year, changes to the European system are likely to emerge which could have implications for Ex-Im Bank policies, procedures and overall competitiveness. As such, Ex-Im Bank will consult regularly with the European ECAs and monitor any changes the Europeans make with respect to financing for large aircraft exports, including the impact of the changes to the European ECAs' interest rate system and market window financing. Finally, it appears that a consensus among the LASU participants may be emerging to revisit the issue of renegotiating the LASU. If this development materializes, the United States will be afforded the opportunity to introduce contemporary concepts to the agreement and maximize U.S. exporter competitiveness.

Ch. IV Comparison of Major Program Structures

Section B: Project Finance

INTRODUCTION

Although limited recourse project finance (also referred to as project finance) has been around as a financing technique for a number of years, export credit agencies only started working with this tool in the early to mid-1990s. Unlike standard ECA business, structures involving project finance determine creditworthiness by assessing the cash flows of a project (as defined by the contractual relationships within each project) and do not have recourse to a foreign government, financial institution or established corporation. It has taken many years for ECAs to learn the strengths and weaknesses of this financing technique and then to determine how to competitively differentiate themselves with the various features of this technique. Nearly a decade later, most ECAs offer support for project finance structures and, in fact, frequently work together to put in place a structure that fairly balances the risks between ECAs and other financial partners.

In September 1998, the OECD Participants to the Arrangement established a trial period for using additional structuring flexibilities for project finance transactions. This trial period, which was originally established for two years, has been extended twice, and the flexibilities are now being considered for permanent incorporation into the OECD Arrangement. These flexibilities extend the timing of the first repayment of principal, the repayment profile and the maximum repayment term. They are proscribed by limits on the average life of the structure (seven and a quarter years, with the first repayment occurring within the first two years and the maximum repayment term not to exceed 14 years).

EX-IM BANK'S POLICY AND PRACTICES

Ex-Im Bank created its project finance program in 1994. With its 100% political guarantee during the construction period, and a 100% comprehensive guarantee or direct loan available during the repayment period, Ex-Im Bank quickly had a program that was competitive with the other ECAs. However, after the 1997-1998 Asian financial crisis, Ex-Im Bank found project sponsors were having difficulty obtaining construction financing. To better meet customers' needs and expectations, and because Ex-Im Bank had a better understanding of the construction risks (after over four years of experience), Ex-Im Bank added the option of a 100% comprehensive guarantee during the construction period. This addition increased the competitiveness of Ex-Im Bank's program and at this point is a standard feature, with six of the G-7 ECAs offering a form of comprehensive support during the construction period.

Overall, the features of Ex-Im Bank's project finance package are attractive: 100% U.S. government guaranteed support for all risks (political and commercial) during both the construction and repayment periods, willingness to utilize the project finance flexibilities allowed under the OECD Arrangement, maximum availability for capitalization of interest during construction (IDC) and financing of local country costs. On the margins, however,

borrowers still contend with public policy restrictions (such as domestic content and U.S. shipping requirements), advisor and consultant costs and more documentation requirements.

G-7 ECAs' POLICIES AND PRACTICES

Across the board, ECAs offer very similar coverage for project finance transactions. All provide cover for at least 90% of the political and commercial risks during the life of the project, support local costs up to the amount of cash payment and capitalize the interest that accrues during the lengthy construction period. The only difference between ECAs is in the quality of coverage they provide. Ex-Im Bank and ECGD offer unconditional guarantees, EDC and JBIC offer direct loans and the four other G-7 ECAs (Coface, Nexi, Hermes and SACE) all offer conditional insurance. See **Figure 14** for a comparison of ECA program features, **Figure 15** for activity levels from 1998-2002 and **Figure 16** for G-7 shares of project finance transactions.

SUMMARY DATA

Figure 14: Comparison of Project Finance Program Features Offered to Date by the G-7 ECAs

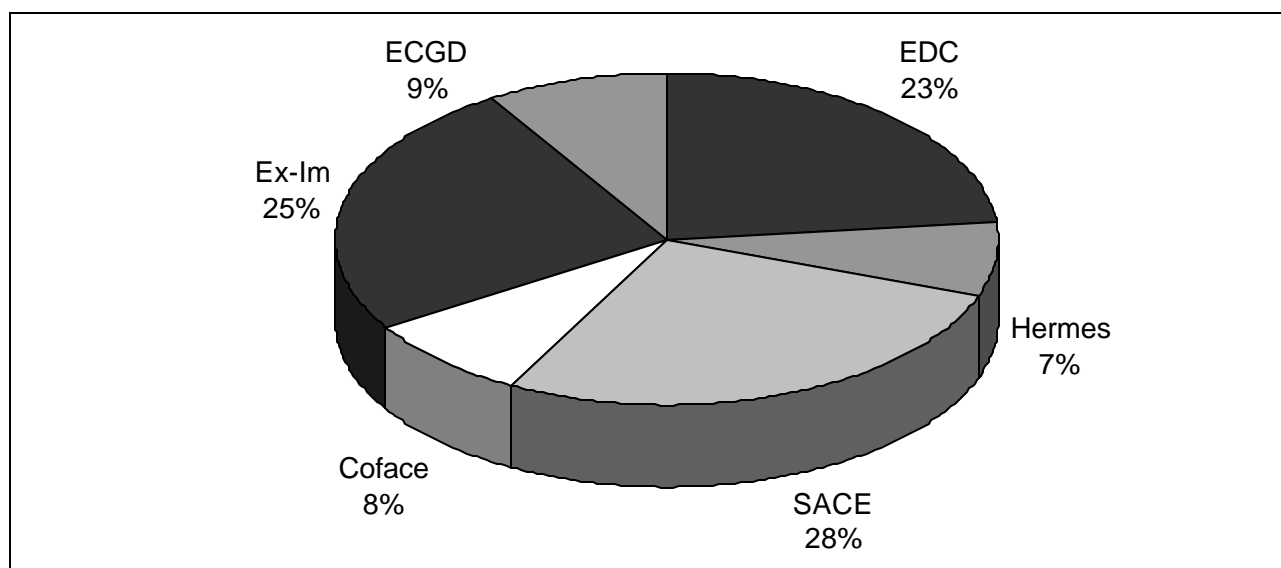
		EDC	Coface	Hermes	Sace	JBIC	NEXI	ECGD	Ex-Im
Pre-completion cover		Comprehensive	Political only	Comprehensive	Comprehensive	Comprehensive	Political only	Comprehensive	Comprehensive
Post-completion cover		Comprehensive	Comprehensive	Comprehensive	Comprehensive	Comprehensive	Comprehensive	Comprehensive	Comprehensive
Related conditions		Standard direct loan	95% below standard insurance	95% below standard insurance	95% below standard insurance	Standard direct loan	97.5% below standards insurance	100% above standard guarantee	100% above standard guarantee
Project finance flexibilities used	1st repayment	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes
	Repayment profile	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes
	Repayment term	No	Yes	Yes	Yes	Yes	Yes	Yes	Yes
IDC up to 100%		Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Local costs up to 15%		Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

Figure 15: Number and Volume of Project Finance Deals Signed*

Number	1998	1999	2000	2001	2002
Signed project financings	458	479	459	276	226
G-7 ECA portion of project financings	19	9	19	7	8
ECAs as % of all project financings	4%	2%	4%	3%	4%
Ex-Im portion of project financings	0	1	7	6	5
Ex-Im as % of ECA project financings	0%	11%	37%	86%	63%
Volume (US\$ Bn)	1998	1999	2000	2001	2002
Signed project financings	\$172.0	\$198.2	\$239.2	\$123.5	\$70.0
G-7 ECA portion of project financings	\$3.6	\$2.5	\$3.6	\$1.4	\$2.2
ECAs as % of all project financings	2%	1%	2%	1%	3%
Ex-Im portion of project financings	\$0.0	\$0.2	\$1.6	\$1.0	\$0.6
Ex-Im as % of ECA project financings	0%	8%	44%	71%	27%

* Source: Dealogic database

Figure 16: Distribution of ECA Project Financings Signed in 2002



EXPORTER AND BANKER VIEWS

The banking industry has been highly complimentary of the Ex-Im Bank project finance program and team. One banker commented: “Ex-Im is far more creative and flexible than most, if not all, other ECAs.” Yet despite the strength of this program, Ex-Im Bank does not have a large piece of each of the deals it supports. When asked, bankers suggested that this was due to the strong dollar and the complexity of Ex-Im Bank’s process. Exporters have agreed with this conclusion. From exporters’ perspective, U.S. exports are included in a transaction only to the extent that it will bring Ex-Im Bank in as the political heavyweight in the event problems arise with the host government, but Ex-Im Bank’s public policy requirements are disadvantageous enough that additional support is not typically desired. What is uncertain is whether U.S. exports are lessened as a consequence.

The project sponsors have a similar viewpoint. Over the past year they have suggested including Ex-Im Bank in a deal before they approached, or in some cases even considered, other ECAs. Like the bankers and exporters, the sponsors believe that Ex-Im Bank is more creative and flexible than other ECAs and that Ex-Im Bank is a political heavyweight that becomes essential if problems arise with the host government. However, the project sponsors have a different opinion from the exporters as to why the U.S. often has a relatively small piece of a project. They say that the United States is not competitive in price and, thus, U.S. companies are sourcing outside of the United States to obtain lower production costs. In fact, in one transaction the sponsor asked for maximization of U.S. sourcing, yet the U.S. exporters did not do so because it would have made their price uncompetitive.

CONCLUSION

Ex-Im Bank is a significant, but not dominant, player in the project finance arena. In fact, the five-year trend line shows a high level of volatility in the number and dollar volume of project financing, ECA involvement in project finance and Ex-Im Bank involvement in project finance. Certainly the cyclical nature of the industry – as it is affected by the health of the world economy and of various industries – has an impact on the volatile nature of the business. Nevertheless, Ex-Im Bank's project finance program, in almost all cases, is equivalent to those offered by the other G-7 ECAs.

Ch. IV Comparison of Major Program Structures

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

INTRODUCTION

Responding to exporter concerns regarding comparative efficiency associated with multi-sourced transactions, Ex-Im Bank has established a “one-stop-shop” co-financing program. “One-stop-shop” arrangements allow products and services for one purchase from two (or more) countries to benefit from a single ECA financing package. Without co-financing, the parties would have to secure separate financing contracts with two (or more) ECAs to ensure support for exports from various countries. 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.

The lead ECA provides export credit support for the entire transaction, and the follower ECA provides reinsurance for its share. This situation results in the lead ECA being 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. As use has proliferated, exporters continue to confirm that availability and ease of co-financing has become a measurable competitive issue.

EX-IM BANK’S CO-FINANCING “ONE-STOP-SHOP” ARRANGEMENTS

In 2001, Ex-Im Bank signed one-stop-shop bilateral (i.e., lead and follow) agreements with ECGD (UK) and EDC (Canada) and initiated discussions with other ECAs to sign bilateral agreements. During 2002, Ex-Im Bank began to gain experience under these and other co-financing arrangements by processing transactions. Additionally, Ex-Im Bank is in negotiations for bilateral agreements with Hermes and Coface.

Unlike most other ECAs, Ex-Im Bank does not require a formal bilateral agreement before considering co-financing transactions when the United States is the lead entity. Thus, Ex-Im Bank will process co-financing requests for transactions with ECAs on a case-by-case basis. In addition, Ex-Im Bank will consider co-financing with smaller, non-Category 1 ECAs. In that regard, Ex-Im Bank has approved co-financed transactions with (Hungarian Export Import Bank).

Figure 17 details the one-stop-shop co-financing transactions that the Bank has authorized in 2002. In summary, the Bank authorized eight co-financing transactions (six long-term and two medium-term) in Brazil, Israel, Luxembourg, Mexico, Saudi Arabia and Turkey, totaling approximately \$315 million.

Figure 17: Authorized Ex-Im Bank “One-stop-shop” Co-finance Transactions in 2002

Ex-Im Bank & Co-financing ECA	Market	Project	Amount
Canada: EDC	Mexico	Manufacturing Project	\$4 million
Hungary: HEXIMBANK	Turkey	Power Plant	\$20 million
Norway: GIEK	Turkey	Power Plant	\$10 million
Norway: GIEK	Turkey	Power Plant	\$8 million
United Kingdom: ECGD	Brazil	Oil Field Project	\$8 million
United Kingdom: ECGD	Israel	Large Aircraft	\$114 million
United Kingdom: ECGD	Luxembourg	Large Aircraft	\$146 million
United Kingdom: ECGD	Saudi Arabia	Construction Project	\$6.5 million

G-7 ECAs' POLICIES AND PRACTICES

As shown below in **Figure 18**, the bulk of co-financing agreements exist between the European ECAs who have signed multiple framework agreements between themselves and have been processing co-financed transactions since 1995. These agreements were originally designed to help European ECAs manage their exposure. In addition, most ECAs have seized upon the administrative efficiency that results from the one-stop-shop for export financing as a means of improving their customer service and competitive image.

Additionally, the private sector has benefited from ECA co-financing and is refining it to the benefit of exporters around the world. For example, European banks together with European insurer ECAs (e.g., Coface, SACE and Hermes) have developed a co-financing framework agreement with Algeria's national hydrocarbon company Sonatrach. The European banks and Sonatrach have agreed to a common documentation structure that governs their relationship, and a pre-approved line of credit has been established for various European commercial banks. ECA approval is given on a case-by-case basis, and at that time the transaction is reviewed and tailored to the commercial contract as well as any additional ECA policy or procedural requirements. This process has created administrative efficiencies by establishing a “fast track” review process, and it has facilitated the support of European content.

Figure 18: G-7 Co-financing “One-Stop-Shop” Agreements (as of December 2002)

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

JBIC is the only G-7 ECA that has not signed any co-financing framework agreements.

When determining which transactions are eligible for co-financing, most ECAs agree that this program can be used across sectors and transaction size. While certain ECAs prefer to use co-financing for larger transactions, no fixed dollar limits currently exist on Ex-Im Bank co-finance transactions. In addition, due to the complex nature of project finance transactions, the one-stop-shop is not often used to support exports to non-recourse projects.

EXPORTER AND BANKER VIEWS

About half of the survey respondents indicated that Ex-Im Bank’s co-financing program was less competitive than its foreign counterparts. In particular, several exporters and bankers indicated particular dissatisfaction with the fact that “Ex-Im has only set up two one-stop-shops and that one-off deals are exceptions not pro forma.” Another exporter remarked that the Bank does not seem willing to enter into one-stop-shop deals “when Ex-Im is not the lead lender.” In addition, several bankers encouraged Ex-Im Bank to establish a long-term insurance product to facilitate additional co-financing agreements. Specifically, one banker remarked: “Ex-Im Bank is clearly at a disadvantage (at least for deals over \$10M) given its use of guarantees vs. insurance because guarantees are clearly less flexible, and make co-financing arrangements more difficult to implement.”

On a positive note, some exporters remarked that the co-financing program is “excellent” and “has made it possible to compete with co-financing programs being offered by other foreign ECAs.”

CONCLUSION

Ex-Im Bank's co-financing program is less available (and, to that extent, is less competitive) than the programs of most of the other G-7 ECAs. The lack of signed bilateral agreements with insurer ECAs is the main contributor to the Bank's disadvantage vis-à-vis foreign export credit agencies. Nonetheless, Ex-Im Bank has addressed transaction-specific requests for co-financing. In this regard, Ex-Im Bank is unique in that it will consider co-financing on transactions with foreign export credit agencies that represent a greater risk than the top tier ECAs, and the Bank is willing to consider transactions absent a bilateral framework agreement.

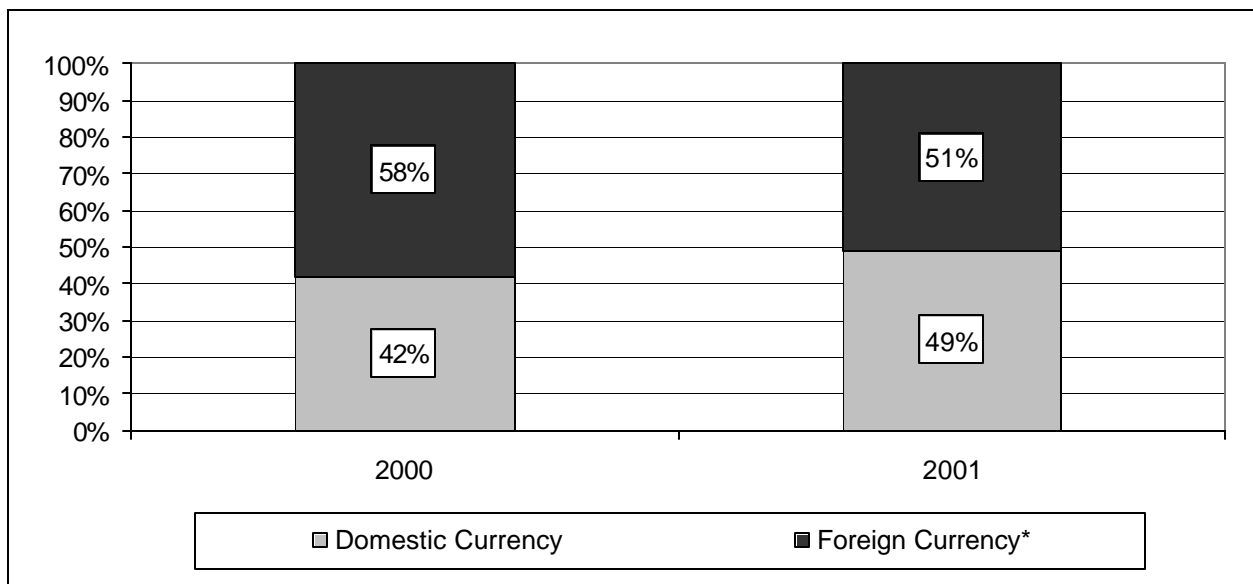
Ch. IV Comparison of Major Program Structures

Section D: Foreign Currency Guarantees

INTRODUCTION

As procedures and guidelines are standardized for numerous aspects of international financing, ECAs are looking for other means to differentiate themselves. One such effort is providing support for transactions denominated in foreign currencies. As seen in **Figure 19**, ECA support for foreign currency transactions (as opposed to domestic currency business, i.e., U.S. dollar for Ex-Im Bank, Japanese Yen for JBIC, etc.) in 2000 and 2001 has comprised approximately 50% of total financing support for long-term transactions, indicating that foreign currency financing is an important ECA offering. For the purposes of this discussion, the term “foreign currency” is broken down into two subsets: hard currency and local/soft currency. Hard currency refers to the legal tender of industrialized countries such as the U.S. dollar, Japanese yen, Swiss franc and the euro (and its precursor currencies), all of which tend to have global acceptance as a medium of exchange and savings. Local/soft currency refers to the currency that is used only in the buyer’s country or local region. Examples include the Mexican peso, South African rand and Indian rupee.

Figure 19: Percentage of OECD Long-Term Transactions Denominated in Foreign Currencies



*Foreign currency includes both hard currency (approximately 99%) and local/soft currency business (approximately 1% of the foreign currency business).

Foreign currency support is based on an ECA’s standard product(s), i.e., loans, insurance and/or guarantees. In essence, a commercial bank (or in the case of EDC or JBIC, the ECA) extends an

export credit denominated in a foreign currency to a foreign importer. The interest rate applicable to the foreign currency transaction is negotiated between the borrower and the lender, and the ECA provides political and commercial risk coverage for both the interest and principal. Because hedging markets are very thin and prohibitively expensive in the medium- and long-term, the existence and utility of ECA coverage has a competitive effect on a buyer's sourcing decision.

EX-IM BANK'S POLICY AND PRACTICE

For more than two decades, Ex-Im Bank has provided comprehensive guarantee and medium-term insurance coverage for foreign currency denominated transactions. Ex-Im Bank originally established this program to enable U.S. exporters to meet the buyer demand for yen-priced offers. Globalization has only intensified and widened such demand.

A key feature of Ex-Im Bank's foreign currency program is how Ex-Im Bank handles the exchange risk arising from a mismatch between the dollars paid to the U.S. exporter and the foreign currency debt obligation provided to the foreign importer. Under standard guarantee policies and procedures, Ex-Im Bank would be exposed to the mismatch risk during the claim payment and recovery period, because Ex-Im Bank would use dollars to pay the lender's claim while the expected recoveries would be denominated in the foreign currency. However, as a special feature of the foreign currency guarantee program, Ex-Im Bank requires the buyer's obligation to be converted to dollars at the exchange rate in effect at the time the claim is paid.

Several years ago, Ex-Im Bank began offering coverage for *acceptable* (as determined by guidance from the Department of Treasury as to the breadth and depth of that currency's market) local/soft currencies on a case-by-case basis. Every year Ex-Im Bank receives roughly five to ten inquiries about support for foreign currency transactions and approves about four applications each year. Customers have evinced interest in continued expansion of the program and note the receptiveness of other ECAs as a further justification for Ex-Im Bank's involvement in local currency deals.

The only significant growth area has been in the size of the transactions for which foreign currency guarantees have been requested, due entirely to the active use of the program by airline industry buyers. Another interesting trend, which is reflective of the current environment, is the shift in the types of currencies requested. In the mid-1990s, the currencies requested were predominantly hard currencies. Today, many of the requests are for local currencies. Nonetheless, the vast majority of Ex-Im Bank's transactions have been denominated in U.S. dollars.

G-7 ECAS' POLICIES AND PRACTICES

As noted in the introduction above (and compared in **Figure 20** below), all major ECAs (including all of the G-7 ECAs) actively support transactions denominated in hard currencies, most significantly U.S. dollar transactions. In 1999, however, ECGD began aggressively

marketing its willingness to support local currency transactions. Since that time, four other ECAs (Ex-Im Bank, EDC, Coface and Hermes) have entered the fray. In reality, very few medium- or long-term local currency transactions have materialized. Ex-Im Bank is aware of at least six medium- or long-term local currency export finance transactions supported by an ECA in the past three years, three of which were done by Ex-Im Bank.

All ECA foreign currency programs have one basic feature in common: they are designed to help buyers control certain risks associated with export credits by effectively spreading exchange rate fluctuation risk among a number of parties. Thus, ECAs take some fluctuation risk with their cover, but they also expect the lender or exporter and the foreign borrower to take some of the risk as well. The sharing of the risk with the borrower is generally accomplished at the time of default. For example, Coface fixes the exchange rate between the foreign currency and the euro at the time of default. So regardless of how the exchange rate fluctuates after the default, the buyer is required to pay enough of the foreign currency to make Coface and the insured party whole. Hermes has a similar feature, although they do not fix the exchange rate until they pay a claim. ECGD caps the total amount of its British pound liability, thus limiting the amount of claim payment and ECGD's exposure to exchange rate risk. Ex-Im Bank's approach is similar to that taken by Coface and Hermes: Ex-Im Bank converts the obligation to dollars at the time of claim payment, basically fixing the exchange rate at the time of claim payment.

One area of significant difference between ECAs offering support for foreign currency transactions is pricing. Under the rules of the OECD agreement on premia, ECAs providing cover for a *local currency* transaction may apply a discount of 35% to 50% (depending on the legal structure of the cover). ECGD has indicated that they would be willing to provide a 50% discount to the minimum required premium for a local currency transaction. Ex-Im Bank has also indicated a willingness to provide a discount, though the structure of our guarantee and insurance programs is such that the Bank could only provide a 35% discount. All the other G-7 ECAs (except SACE, which has not commented) have indicated that, due to the risks inherent in (and/or administrative costs of) a foreign currency transaction, they would charge a surcharge for such cover. For a comparison of ECA foreign currency programs, see **Figure 20** in the summary data section below.

SUMMARY DATA

Figure 20: Comparison of G-7 ECAs' Support for Medium- and Long-Term Foreign Currency Transactions

	ECA Limit to			Discount Surcharge	Hard Currencies	Local Currencies Transactions Approved
	Foreign Currency	Local Currency	Exchange Risk?			
EDC	Yes	Yes	No	Surcharge	USD, EUR, GBP, JPY	N/A
Coface	Yes	Yes	Yes, fix exchange rate at time of default	Surcharge	USD, JPY	None
Hermes	Yes	No	Yes, fix exchange rate at time of claim payment	Surcharge	USD, JPY	Malaysian ringgit (is considering)
SACE	Yes	No	No	N/A	USD, JPY	N/A
NEXI	Yes	No	No	Surcharge	USD, EUR	N/A
ECGD	Yes	Yes	Yes, cap liability in British pounds	Discount up to 50%	USD, EUR, AUD, JPY, CHF	Omani rials and Thai bahts*
Ex-Im Bank	Yes	Yes	Yes, convert obligation to dollars at time of claim payment	Discount up to 35%	EUR, JPY, CAD, AUD	Mexican pesos, Egyptian pounds, South African rand and Indian rupees**

*For non-export credit transactions, ECGD has also supported Indian rupees, Hong Kong dollars, Malaysian ringgits, Egyptian pounds and Pakistani rupees.

**In response to inquiries, Ex-Im Bank has indicated a willingness and ability to support Malaysian ringgits, Thai baht, Israeli shekels, New Zealand dollars, Singapore dollars, Chinese renminbi, Brazilian real, Turkish lira, Korean won, Russian rubles, Philippine peso and CFA franc. Ex-Im Bank will also consider other currencies as inquiries arise.

EXPORTER AND BANKER VIEWS

In the 2002 survey of Ex-Im Bank's competitiveness, both exporters and bankers encouraged Ex-Im Bank to support and expand its foreign currency (including the local currency subset) program. Bankers commented that this program is beneficial to borrowers and that demand for it is expected to increase as local bank and capital markets grow.

Exporters also asked for further development of the program, with one large equipment manufacturer stating that they would be willing to increase their risk participation in a transaction in order to increase usage of this program.

CONCLUSION

Overall, Ex-Im Bank is fully competitive with other ECAs on the qualitative practice of supporting foreign currency transactions, including the local currency subset of that group, and on the quantitative features of its program. One ECA commented that there is a lot of smoke and no fire with the local currency issue.

Ch. IV Comparison of Major Program Structures

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

With the exception of co-financing, Ex-Im Bank is generally competitive with its G-7 ECA counterparts, and in some selected areas Ex-Im Bank is more competitive in the way that technical features are incorporated into programs. With regard to co-financing, Ex-Im Bank's limited number of bilateral co-financing agreements has placed Ex-Im Bank at a competitive disadvantage vis-à-vis our counterparts. Moreover, the absence of a product that fits well with the insurance product used by our counterparts inherently yields differences in co-financing that can be difficult to resolve on a bilateral and on a case-by-case basis. In the general category of major program structures, Ex-Im Bank receives an A-, indicating it is selectively competitive.

Figure 21: Grading of Ex-Im Bank's Major Program Competitiveness

Key Elements	Grade
Large Aircraft	A
Interest rate level	A+
Interest rate determination	A-
Project Finance	A
Core program features	A+
Repayment flexibilities	A+
Policy requirements	A-
Co-financing	B
Bilateral agreements	C
One-off deals	B+
Flexibility re: lead vs. follow	B
Foreign Currency Guarantee	A+
Foreign currency cover	A+
Local currency cover	A+
Total Average Grade	A-

Ch. V Economic Philosophy and Competitiveness

Section A: Trade-related Tied and Untied Aid

INTRODUCTION

Tied aid has been a competitive issue for U.S. exporters (and the U.S. government) since the mid-1970s. At the core of the issue is a fundamental philosophical difference between the economic and aid philosophies of the United States and those of some of our major developed country competitors. Over thirty years ago, the United States concluded that it is bad economic and public policy to blend commercial and developmental objectives by using tied aid credits for capital goods. To bridge the fundamental differences between U.S. views and those of other governments, who believed that tied aid support for major infrastructure projects represented good development policy, the United States used the OECD to negotiate disciplines for the use of tied aid financing.

Accordingly, all Ex-Im Bank tied aid activity over the past two decades (from the mid-1980s War Chest to the current Tied Aid Credit Fund, or TACF) has been used strategically as leverage to create multilateral tied aid rules or enforce the letter (and counter any abuses in the spirit) of the rules.

The OECD tied aid rules have been instrumental in reducing tied aid by over half between 1993 and 2002, to an average of less than \$4 billion annually (despite a massive increase in Japanese tied aid from 1998 to 2001). In fact, total tied aid in 2002 fell to its lowest level on record: \$2.6 billion, an over 70% reduction from the level before the implementation of the tied aid rules (see **Figure 22**).

Nevertheless, many foreign tied aid programs are likely to continue, and many projects supported by these programs contain a significant portion of capital goods that may have commercial implications. As a result, some U.S. exporters that encounter such financing perceive themselves as uncompetitive, because Ex-Im Bank is generally unable to match tied aid offers for capital goods exports to developmentally-focused projects for which foreign tied aid is permissible.

DEFINITION OF THE VARIOUS TYPES OF AID

Official Development Assistance (ODA), or aid, is concessional financial support of which at least 25% is intended to carry no repayment obligations (i.e., contains 25% concessionality or grant element), and the vast majority of it (over 80%) is 100% pure grant. Aid from a donor government to a recipient developing country government normally supports either “general” uses (e.g., balance of payments support) or the purchase of goods and/or services (local, donor country and/or third country) necessary for the completion of an action 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: grants⁵ or credits. However, because grants do not involve significant repayment obligations, they are not viewed as trade-distorting aid (see below) and are not subject to OECD requirements (other than notification).

Tied aid credits refer to financing that is developmental (not commercially viable projects or exports) 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. This type of aid falls within the OECD Arrangement rules. 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 financing that is **not** contractually conditioned upon the purchase of goods and/or services from any particular country. This aid currently falls under the OECD Development Assistance Committee (DAC) rules, which differ from the OECD Arrangement rules in that the DAC provides virtually no restrictions on untied aid use. Therefore, there is a “gray zone” between these two differing definitions (forms) of aid. The resulting ambiguity has often been used to advantage foreign untied aid donors.⁶

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, strict OECD rules 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. As a result, the Arrangement prohibits tied aid credits for such projects. The Arrangement also prohibits tied aid to countries with a per capita income level above \$2,975, because they are considered to have ready access to market financing and official export credits for all types of projects.

By definition, untied aid should be non-trade-distorting, because it should be equally accessible by exporters from all countries. However, through influence exerted indirectly (e.g., through special procedures, required designs and specifications, promises of additional aid, political pressures, gratitude shown by the recipient, etc.), untied aid can become effectively tied while it escapes the Arrangement rules for tied aid. All such aid that is effectively tied must be considered trade distorting. No OECD Arrangement rules currently discipline the use of untied aid except those requiring confidential notification, although the U.S. has proposed such rules. The general lack of Arrangement rules governing the use of untied aid also provides the donor the ability to use very low rates of concessionality with its untied aid, thereby actually encouraging the use of untied aid for inexpensive trade promotion and distortion.

⁵ Credits with a concessionality level of 80% or more are viewed as grants and are not considered trade distorting.

⁶ DAC rules were developed decades ago. Currently, the DAC is discussing whether to accept a U.S. proposal to modify the DAC methodology for calculating grant element levels. The nominal level of grant element that qualifies as Official Development Assistance (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 9% real concessionality and theoretically could provide only 4% real concessionality).

U.S. GOVERNMENT AND EX-IM BANK POLICY

The United States favors aid that represents *bona fide* development assistance. The United States seeks to reduce (and hopefully eliminate) aid that is trade distorting. The U.S. position on this topic is driven by two long-standing objectives for aid:

- Minimize trade-distorting aid because it disadvantages U.S. exporters, i.e., redirects business away from U.S. and other suppliers whose products are superior in quality and price.
- Minimize trade-distorting aid because it is a misallocation of both international and developing country resources. Furthermore, it results in higher contract prices, a capital-intensive development bias, skewed technology choices and an increased debt burden.

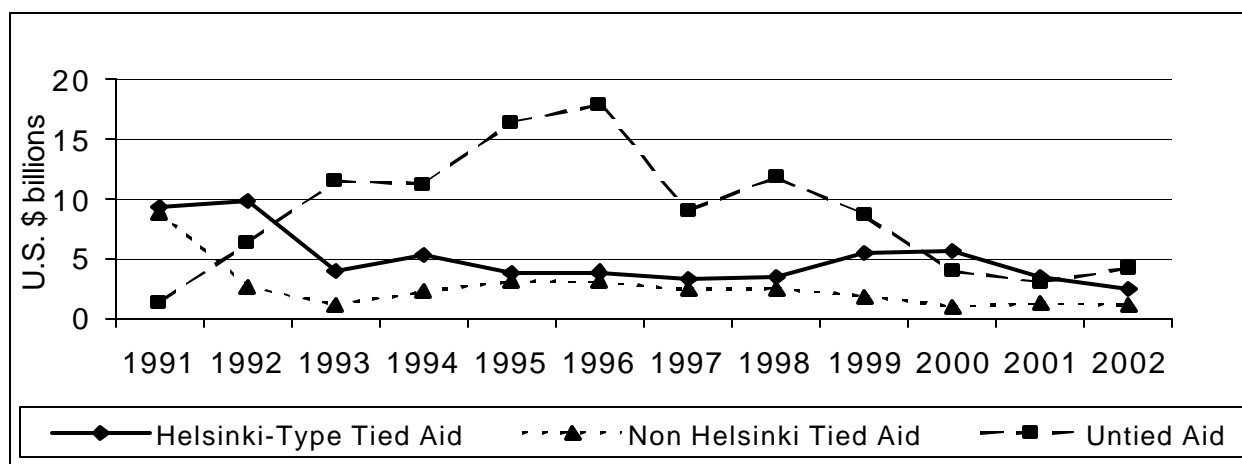
Consistent with long-standing U.S. export financing policy, Ex-Im Bank does not initiate tied aid. Instead, Ex-Im Bank and the U.S. Treasury Department work together to determine whether to match a foreign tied aid offer. The determination to match is made on the basis of largely objective criteria used to determine whether a tied aid match provides negotiating leverage for introducing new disciplines or is useful for enforcement of existing disciplines. The United States considers that tied aid used within the rules to gain a longer-term advantage for sales on market terms violates the spirit of the tied aid rules and should be matched.

ACTIVITY

Implementation of the 1991 OECD Helsinki Package of tied aid rules has greatly reduced the systematic use of trade-distorting tied aid (see **Figure 22**). In 2002, the total volume of tied aid credits reached a record low of \$2.6 billion, which is less than one-fourth of the pre-Helsinki volume in 1991. The data support the success of the Helsinki disciplines in containing tied aid to a much smaller scale and to cases least likely to involve trade distortions.

However, the data (**Figures 22 and 23**) coupled with the belief by some governments that tied aid is a legitimate development tool also suggests that there is little chance that tied aid will be totally eliminated. In fact, tied aid that does not distort trade is acceptable development financing. The United States, however, believes that aid programs driven by commercial objectives undermine basic U.S. development goals, because such programs generate high levels of debt and debt service while not directly addressing basic poverty issues. Other governments have refined their approach to tied aid within the Helsinki disciplines and continue to allocate scarce resources to support their exporters where permitted. In fact, the number of Helsinki compliant tied aid offers notified has grown slightly since the start of Helsinki. Reflecting the sophistication of foreign countries' tied aid programs, 2002 marked the first year since 1992 that every notification was deemed compliant with the tied aid rules.

Figure 22: Aid Credit Volume by Type



“Helsinki-type” tied aid is subject to three principal disciplines: (1) no tied aid for commercially viable projects; (2) minimum 35% concessionality; and (3) country limitation (no country recipients with a per capita income above \$2,995, but the figure may change annually as it is based on annual World Bank data; see **Appendix G, Annex 1**). OECD Participants determine commercial viability based on the nature of the project, a feasibility study presented by the donor, and, if needed, a “consultations” meeting held to discuss the commercial viability of the project if the feasibility study suggests commercial viability based on cash flows.

“Non-Helsinki-type” tied aid includes: stand-alone *de minimis* projects (valued at less than approximately \$2.6 million), grants or near-grants (at least 80% concessionality) and partial grants (at least 50% concessionality) offered to the poorest countries (the UN declared Least Developed Countries, or LDCs). These types of aid are normally not considered to have serious trade-distorting effects and, therefore, are exempt from the Helsinki rules regarding commercial viability and the consultations process (although all tied aid is subject to notification requirements, and *de minimis* tied aid still has to meet minimum concessionality and per capita income requirements).

Figure 23: Notifications of Helsinki Tied Aid and Consultations Group Examinations

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	Total
# Of notifications	137	151	273	226	212	195	191	213	182	155	166	2,101
# Of projects examined by Consultations Group	39	25	31	14	4	2	5	2	4	2	1	129
# Of projects deemed non-compliant with Helsinki rules (i.e., com'ly viable)	16	12	21	4	3	2	5	1	4	1	0	69*

*Of the 69 “non-compliant” cases (i.e., cases deemed commercially viable by the OECD Consultations Group), 19 were abandoned and 33 proceeded within Arrangement procedures or on commercial terms. The disposition of several cases is presently unknown.

Reflecting the twin factors of increasingly compliant tied aid offers from other ECAs and the continued absence of new tied aid negotiations, use of the TACF has been fairly minimal over the last five years. This lack of U.S. tied aid activity can be attributed to the fact that Ex-Im Bank’s matching approach is generally used to either match (to deter) non-compliant foreign tied aid offers, which have been reduced to zero at present, or to create negotiating leverage to establish new disciplines (see **Appendix G, Figures G4 and G5**). The FY2002 budget process rescinded more TACF resources in one year than Ex-Im Bank used in the previous five years combined. [Note: During 2002 there were no new tied aid authorizations. However, there were two amendments to existing tied aid authorizations that utilized \$13.7 million (\$7.0 million for Indonesia and \$6.7 million for Morocco).]

For the past few years, the focus of U.S. concern has shifted to untied aid flows. The concern began in the middle of the past decade when Japanese untied aid peaked at over \$10 billion per year, and there were a few clear episodes of effective (*de facto*) tying. Since that time the United States has been trying to get at least some (or comparable) tied aid disciplines applied to untied aid. However, these discussions have not produced any agreement because of the lack of consensus by the EU and Japan. The United States continues to believe that undisciplined untied aid remains a threat to the tied aid rules, because it provides all aid donors both the opportunity and incentive to shift tied aid to untied aid in order to circumvent the tied aid disciplines and distort trade.

EXPORTER AND BANKER VIEWS

Once the lightning rod for exporter and banker comments on Ex-Im Bank competitiveness, tied aid has garnered fewer comments over the past few years, and 2002 was no exception. Of the total survey respondents, less than half provided comments on tied aid. Only one third of the banks and two thirds of the exporters that responded assessed tied aid. None of the respondents cited untied aid.

The bankers generally did not consider tied aid to be a problem “except [when offered] by Scandinavian countries.” However, two thirds of the exporter respondents indicated that they were dissatisfied with the overall competitiveness of Ex-Im Bank’s tied aid policy. Echoing the views of other respondents one exporter said, “Ex-Im Bank can only react, not initiate tied aid.” Another exporter expressed frustration by saying, “It is difficult to obtain tied aid support from the U.S.G...our perception is that Ex-Im Bank would not match any tied aid transactions and even if there is an intention for the Bank to do so, the process is lengthy involving other U.S.G. organizations such as OMB and U.S. Treasury.” On balance, the exporting community commentary indicates that U.S. tied aid policy is perceived to be less competitive than that of its foreign counterparts.

CONCLUSION

In sum, several of the G-7 OECD Members have aid programs that initiate tied aid and operate within the international disciplines that were set forth in the OECD tied aid rules. The TACF (jointly overseen by Treasury and Ex-Im Bank) is clearly focusing its use on matching only those cases that leverage ongoing negotiations, enforce current disciplines or threaten to distort commercially based competition in the future. Moreover, the competitive environment today is one in which volumes of both tied and untied aid have dropped dramatically over the past decade, almost all foreign aid offers comply with negotiated disciplines and have a developmental cast, and no new tied aid negotiations are ongoing or imminent. As a result, there are very few (and in some years, no) final authorizations of the TACF (although two to three cases per year do meet the current criteria and are offered support from the TACF). The success of the tied aid rules and diminished need for use of TACF to match foreign offers is consistent with overarching U.S. trade policy (although unsatisfactory from the view of some exporters). One partial answer for exporters may turn out to be the pilot mixed credit initiative that Ex-Im Bank and USAID are seeking to implement during 2003 (see **Appendix J**).

Ch. V Economic Philosophy and Competitiveness

Section B: Market Windows

BACKGROUND

In the sections that follow, the concept of market windows will be defined, and the prime market windows players will be identified, their activity quantified and the competitiveness implications estimated. Contractors hired by the Department of Commerce and Ex-Im Bank, on behalf of the Trade Promotion Coordinating Committee, have prepared a report on the effects of market windows on U.S. economic activity and exports. The results suggest a picture that is fuzzy with the colors tending to gray. In fact, most observers of market windows would find comfort in Churchill's 1950s depiction of Russia: "it is a riddle wrapped in a mystery inside an enigma."

While the clarity of the picture on these aspects is slowly getting better, it is still difficult to conclude anything more than that market windows are *probably* a competitive financing issue *of some degree* to at least *a few* U.S. exporters and producers. More importantly, even if continuing research were to enable a conclusion that market windows were *surely* a significant competitive threat to *most* U.S. capital goods exporters (by no means a foregone conclusion), there would remain a major obstacle to any Ex-Im Bank or U.S. government response.

That obstacle was succinctly pointed out by Representative Jim Leach at a 2000 conference celebrating Ex-Im Bank's 65th birthday: to paraphrase, "watch out where you're going with this market window issue; we don't want another Fannie Mae." That is, the essence of market windows (private entities with a public purpose) is basically an oxymoron in the philosophical framework of the U.S. economic system. The grand experiment to date with such entities (i.e., the Government Sponsored Enterprises, or GSEs, of Fannie Mae and Freddie Mac) is now generally considered by public policy professionals to have worked too well.

The TPCC-mandated market window study highlighted the critical need for much greater transparency for market window institutions in order to ever resolve the appropriate relationship with OECD export credit disciplines. The U.S. government will continue to push in international fora for such transparency, and Ex-Im Bank will continue to explore and investigate the nature and extent of any case specific impacts.

Future editions of this report will provide updates on progress with transparency and clarification of competitive impact.

INTRODUCTION

A market window refers to a type of lending activity – typically by a government owned or directed financial institution – that provides medium- to long-term credits to foreign buyers for purchases of capital equipment and services but claims exemption from the OECD Arrangement disciplines because the support is on "market" terms (e.g., priced on a market basis and break

even financially). However, as a result of their direct or indirect relationship with national governments, such institutions derive certain benefits that purely private sector institutions do not, such as tax exemptions and equity capital provided from government budgets. In addition, the term “market window” indicates that such activity may take place within an institution that also provides lending through an “official window” on Arrangement terms. Reflecting this added context, while market window credits may not be programmatically tied to domestic content, they usually involve domestic content or are linked to some form of national interest.

Market window programs have existed for decades, but they became prominent in the world of official export credit over the last decade as OECD agreements on export credit support became fairly codified, leveling the playing field. It is now frequently the case that the key to a particular export deal is an exporter’s ability to find some financing institution that can fill holes in the overall financing package (e.g., cash payment), do something special (e.g., lengthen repayment terms), or accept a level of risk that standard official ECAs or the private markets will not take.

The issue of market windows has proven very challenging in the OECD negotiating context, primarily because of the unwillingness of the two major institutions, Canada’s EDC and Germany’s KfW, to provide any transparency to their market window business (e.g., either to clearly delineate market window activity in annual reports or to apply Arrangement disciplines to this activity). Unlike tied aid, therefore, there is no requirement for EDC and KfW to notify market window activity or even respond to an Ex-Im Bank inquiry. This lack of transparency has made the issue very difficult to address. It has also made it difficult to clearly define and quantify the extent of the problem. Compounding the problem within the OECD was a recent WTO panel finding, in a long-running aircraft dispute between Canada and Brazil, that market window programs are not *per se* prohibited export subsidies. Rather, the determination of a prohibited subsidy would have to be made on a transactional basis – a challenging proposition when the terms of specific transactions are rarely publicly available.

EX-IM BANK POLICY AND PRACTICE

Ex-Im Bank does not operate a market window. Rather, all of Ex-Im Bank’s medium- and long-term transactions comply with the terms and conditions of the Arrangement. In its re-authorization in 2002, however, Ex-Im Bank was given permission by the Congress to match the terms and conditions offered by market windows, regardless of whether such terms are consistent with the Arrangement. Matching is permissible even in the case that a market window institution does not provide sufficient transparency for Ex-Im Bank to assess the terms and conditions of a transaction. The intent of this new ability is to advance negotiations on market windows within the OECD and to level the playing field for U.S. exporters.

G-7 ECAS’ POLICIES AND PRACTICES

Only two of the G-7 countries provide market window support: Canada through EDC and Germany through KfW. It is important to note that there are several others in smaller European countries and that JBIC could become a major player anytime it chooses.

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. The majority of EDC's business is in high-income countries (i.e., the United States and Western Europe) and highly concentrated in the few sectors where Canada has world-class companies: about 78% of EDC's 2001 medium- and long-term business was in the telecom (30%; e.g., Nortel), aerospace/transportation (28%; e.g., Bombardier) and mining (19%) sectors.

The general rule of thumb over the last several years has been that 90% of EDC's medium- and long-term export credit business has been done under its market window. However, in any year the ratio may vary. Applying the general ratio to EDC's medium- and long-term activity over the last five years yields the following (**Figure 24**):

Figure 24: EDC Medium- and Long-Term Activity 1997-2002 (\$Bn)

	1998	1999	2000	2001	2002
MLT export credits	4.5	4.1	5.2	5.5	5.0
Market window	4.1	3.7	4.7	5.0	4.5
Official window	0.5	0.4	0.5	0.6	0.5

KfW

Kreditanstalt für Wiederaufbau (KfW) is a financial institution that is currently owned by the German government (80%) and the federal states (20%). KfW exists to promote the growth of the German economy in a variety of ways. These include primarily domestic investment, export finance and foreign development assistance. Anywhere from 10% to 25% of KfW's annual activity falls under the category "export credits and project finance." This category is broader than just export credits, as it includes corporate and investment finance. "Corporate and investment finance" includes foreign direct investment and investment support, such as that provided by OPIC in the United States. In 2002, corporate and investment finance comprised about 43% of the "export credit and project finance" activity.

The other 57% of the export and project finance business is export credit support. KfW's export credit support is provided both through its market window and its official window. The market window support (roughly 60%-70% of the export credits) is considered to be on market terms and exempt from OECD rules, while the official window support is on OECD Arrangement terms (and mostly covered by Hermes insurance). Applying a market window figure of 65% to KfW's export credit activity (approximately 60% of export and project finance activity) over the last five years yields the following (**Figure 25**):

Figure 25: KfW Export Credit and Market Window Activity 1997-2002 (\$Bn)

	1998	1999	2000	2001	2002
Export credit support	3.8	4.9	6.1	5.6	3.9
Market window	2.5	3.2	4.0	3.7	2.5

Of all of KfW's export and project finance support in 2002, 64% went to Europe, including Central and Eastern Europe. After that, 19% went to Latin America, 11% to North America and 6% to Asia.

In response to a competitiveness challenge and investigation by the European Commission, Germany in 2002 came to an agreement with the Commission to radically restructure KfW's export credit activities. As a result of this agreement, the bulk of KfW's export credit business will be transferred to a separate, but wholly owned, bank subsidiary that will not receive any government privileges. The business that remains under KfW's control will be subject to certain restrictions, such as KfW's participation in a syndicate. This change is expected to be in effect by 2005.

SUMMARY DATA

Combining the two estimates for EDC and KfW yields an average total market window volume in the neighborhood of \$7.0 billion per year over the last five years (see **Figure 26**). The majority (at least two-thirds to three-fourths of this activity) is in the United States and Western Europe, largely supporting Bombardier and Airbus aircraft. In such situations, there is no official ECA competition (and for the EDC regional jets, no U.S. product competition). However, there is a segment of some \$1 to \$2 billion per year in market window activity in middle to upper tier LDCs (especially in project finance). Excluding any Boeing impact for the Airbus sales into the United States, this volume estimate is the market window area of potentially greatest impact on Ex-Im Bank competitiveness as measured in this report.

Figure 26: Market Window Activity 1998-2002 (U.S.\$ BN)

	1998	1999	2000	2001	2002
EDC	4.1	3.7	4.7	5.0	4.5
KfW	2.5	3.2	4.0	3.7	2.5
Total	6.6	6.9	8.7	8.7	7.0

EXPORTER AND BANKER VIEWS

Banks had no view on the extent and scope of the impact of market windows on U.S. exports.

Exporters have not spoken up recently on the general theme of market windows, but they have had positive things to say about both EDC and KfW. In general, exporters are impressed with EDC's customer service. U.S. exporters benefit from this aspect of EDC by having dedicated customer service representatives. EDC is seen as wanting to be an exporter's financier of choice and is willing to negotiate on foreign content, i.e., support U.S. exports. Exporters value KfW's ability to provide 100% financing on a transaction, which reduces documentation and processing. In addition, exporters cited longer terms than available under the Arrangement as an appealing aspect of KfW. KfW is also seen as very competitive on project finance because of its market window business. As a result of KfW's business practices, Germany is gaining a foothold in China, Central and Eastern Europe and Russia.

CONCLUSION

Due to a lack of data and transparency, it is challenging to determine the impact of market windows on Ex-Im Bank and U.S. exporter competitiveness. Nevertheless, if there are market window cases with competitive implications, the 2002 addition of the capacity to match a potentially trade-distorting market window offer would seem to put Ex-Im Bank into C territory on the grading scale.

Ch. V Economic Philosophy and Competitiveness

Section C: U.S. Philosophy and Ex-Im Bank Competitiveness

Ex-Im Bank’s competitiveness in the area of tied and untied aid falls short compared to its G-7 counterparts. Regarding untied aid, the U.S. government has been concerned about the potential for trade distortion that undisciplined untied aid represents. Accordingly, the U.S. government has been trying to get at least some (or comparable) tied aid disciplines applied to untied aid. However, these discussions have not produced any agreement because of the lack of consensus by the EU and Japan.

With regard to market windows, Ex-Im Bank’s competitiveness appears to be fairly low, based on the best available data, with respect to the only two market windows among the G-7 (Canada and Germany, also the only major market windows in the OECD). Identifying and quantifying, much less matching, market windows is a shadow boxing exercise due to the absence of hard data and factual information.

Figure 27: Grading of Ex-Im Bank’s Competitiveness in U.S. Philosophical Framework

Program	Ex-Im Bank has program (Y/N)	Grade
Tied/Untied Aid	Y	B
Market Windows	N*	C
Total Average Grade		B-

*However, in its 2002 Charter reauthorization, Ex-Im Bank was granted authority to match market window transactions.

Ch. VI Public Policies: Stakeholder Considerations

Section A: Introduction

Ex-Im Bank is the official export credit agency of the U.S. government. In this capacity, the Bank is directed by Congress 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. Congress has effectively found that government intervention is in the national interest if it is to ensure that purchase decisions be made on the basis of market factors such as price, quality and service.

Hence, Ex-Im Bank is entrusted with public funds to carry out its mission. In exchange for the access to public funds, Ex-Im Bank is expected to adhere to broader U.S. policy in a variety of areas. Some areas are specified in Ex-Im Bank's Charter (e.g., economic impact and PR 17 on U.S. shipping). Other issues, such as content requirements, reflect the intent of Congress regarding the support of U.S. jobs and attempts to balance U.S. labor and industry interests.

In general, other G-7 ECAs have few such broad public policy considerations, with the exception of domestic content guidelines. Hence, these public policy interests represent those features of Ex-Im Bank financing that are most challenging from a competitive perspective.

The following sections of this chapter present a contextual description of each public policy aspect and some general comments on the competitive implications related to each issue.

Ch. VI Public Policies: Stakeholder Considerations

Section B: Economic Impact

INTRODUCTION

Economic impact refers to the Congressional mandate that requires Ex-Im Bank to assess whether the extension of its financing is likely to cause substantial injury to U.S. industry or would result in the production of a good that is subject to a trade measure⁷. A transaction that has either one of these two characteristics may be denied Ex-Im Bank support. Ex-Im Bank's economic impact procedures are designed to ensure that all of the transactions it supports meet the Bank's Congressional mandate. Cases subject to analysis include all capital equipment transactions that enable foreign buyers to establish or expand production capacity of goods that may compete with U.S. domestic production.

EX-IM BANK'S POLICY AND PRACTICE

The requirement to consider the adverse economic impact of transactions was first incorporated into Ex-Im Bank's Charter in 1968, with subsequent legislation in 1974, 1978, 1986 and 1988. In January 1999, Ex-Im Bank adopted an economic impact policy that required that transactions resulting in the production of a good subject to an anti-dumping (AD) or countervailing duty (CVD) order would be subject to denial based upon economic impact. In 2001, Ex-Im Bank revised its economic impact policy to add section 201 trade measures under the Trade Act of 1974 and suspension agreements from AD/CVD investigations as relevant trade measures that could result in the denial of a transaction. Congress's June 2002 amendments to Ex-Im Bank's Charter codified, with some modifications, the trade measures prohibitions. In addition, to increase the operating transparency of the Bank, Congress also now requires the Bank to provide a public notice and comment period for those transactions that result in the manufacture of a product subject to a relevant preliminary trade action.⁸

G-7 ECAS' POLICIES AND PRACTICES

With respect to the other G-7 ECAs, Ex-Im Bank's economic impact policy is unique. Several ECAs have a broad economic mandate that the transactions they support should benefit their domestic economies. However, only Ex-Im Bank weighs the potential negative economic impacts of its support against the benefits and considers the relevance of trade measures to a transaction, both of which could result in the denial of support. As a consequence, Ex-Im Bank's economic impact mandate initiates a process that has operational consequences (requires Ex-Im

⁷ Anti-dumping (AD) or countervailing duty (CVD) orders, suspension agreements arising from AD/CVD or section 201 injury determinations under the Trade Act of 1974.

⁸ A public notice and comment period is required when there is: 1) a relevant preliminary AD/CVD injury determination and Ex-Im Bank support exceeds \$5 million (or \$10 million for short-term insurance and working capital transactions); or 2) a petition for a section 201 investigation and Ex-Im Bank support exceeds \$10 million.

Bank to dedicate staff and other resources to the issue), may result in processing delays and carries the real risk of denial.

SUMMARY DATA

In FY2002, the Bank processed 491 medium-term insurance and medium- and long-term loan and guarantee transactions. Of these transactions, 238 were applications for loans and guarantees at the Preliminary Commitment (PC) and Final Commitment (AP) stages, and 253 were applications for medium-term insurance. An economic impact analysis was required in 69 of these cases, or 14% of the total number of transactions acted upon. Six of these 69 transactions required a detailed economic impact analysis. Of these six cases, one was eventually denied because of an applicable trade measure, two were found to have a net positive economic impact, and three transactions were delayed, resulting in the applicants' no longer pursuing Ex-Im Bank support.

Since January 1999, Ex-Im Bank's economic impact policy has resulted in the Board of Directors denying nine transactions because of an applicable AD/CVD order or section 201 injury determination (six in FY1999, two in FY2000 and one in FY2002). No transactions have been affected by the notice and comment period for applicable preliminary AD/CVD injury determinations since the Congress amended the Charter in June 2002.

EXPORTER AND BANKER VIEWS

Before adopting the new economic impact procedures in response to the June 2002 changes in Ex-Im Bank's Charter, the Bank held an open meeting for interested parties to express their opinions about how the proposed economic impact procedures would affect them. Several U.S. exporters expressed concern that Ex-Im Bank would deny transactions that other ECAs could support, making them less competitive. In response to the exporter and banker survey, one bank noted that the economic impact policy resulted in the denial of a \$16 million transaction. Additional survey comments included a bank noting that some of its clients preferred not to work with U.S. companies because of Ex-Im Bank's economic impact policy. One exporter reported that the economic impact policy (and other policies) put greater restrictions on Ex-Im Bank vis-à-vis other ECAs and noted that these restrictions make Ex-Im Bank less competitive, because they result in case processing delays and the possibility of lost or denied transactions.

CONCLUSION

With expanded procedures incorporated into Ex-Im Bank's practice as a result of the 2002 Charter renewal, the volume of potential Ex-Im Bank transactions that could be subject to additional review has increased. No other G-7 ECA has similar requirements, but the issue applies to only 10% to 20% of medium- and long-term activity. Therefore, the economic impact element could be seen as a limited detractor on Ex-Im Bank's competitiveness, leaving Ex-Im Bank a notch below the typical G-7 ECA.

Ch. VI Public Policies: Stakeholder Considerations

Section C: Foreign Content

INTRODUCTION

Foreign content is the portion of the export that originated both outside of the United States and the buyer's country, whereas local costs are incurred in the buyer's country. U.S. content is the portion of the export that originated in the United States.

EX-IM BANK'S FOREIGN CONTENT POLICY AND PROCEDURES

In keeping with its objective of maintaining or increasing U.S. employment through the financing of U.S. exports, the Bank has adopted a policy to ensure that its export financing targets the U.S. content associated with goods and services exported from the United States. In order to accommodate the financing of U.S. export contracts that contain goods and services that are not completely U.S.-produced, the Bank's policy allows for the inclusion of some foreign content within the scope of a U.S. export contract with certain restrictions and limitations. Ex-Im Bank's policy on non-U.S. content stems from its Charter but has no specific statutory requirement *per se* as it relates to non-U.S. content; rather, it reflects a concerted balance between labor and industry interests.

For all medium- and long-term transactions, the 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**: (i) 85% of the value of all eligible goods and services contained within a U.S. supply contract; or (ii) 100% of the U.S. content of that export contract.

G-7 ECAS' POLICIES AND PROCEDURES

In general, all export credit agencies (ECAs) seek to maximize the national benefit for their respective activities. However, context for that evaluation varies widely and has led to very different content policies.

All OECD Participants recognize that each country has developed its content policy to further unique domestic policy goals. Hence, the OECD Participants have not pursued common ECA rules on foreign content, and there are no Arrangement guidelines governing the scope or design of foreign content in an officially supported export credit. Thus, given the vastly different sizes of the G-7 economies and their respective views of national interest, it is not surprising that foreign content policies vary widely and substantially.

Figure 28: ECA Foreign Content Support – Comparison of Policy Parameters

	Ex-Im Bank	EDC	European ECAs	JBIC & NEXI
Application of the policy	In aggregate per U.S. supply contract	In aggregate	In aggregate	In aggregate
Requirement to ship foreign content from the ECA's country?	Yes	No	No	No
Policy implications if foreign content exceeds 15%	Cover reduced	Decided on a case-by-case basis	Decided on a case-by-case basis* *Cover is not reduced for transactions that include up to 30% EU content	Decided on a case-by-case basis *Cover is not reduced for transactions that include up to 70% foreign content
Minimum amount of domestic content	No minimum threshold	If domestic content is less than 50%, coverage terms are set on a case-by-case basis	Generally, domestic content needs to be at least: (i) 85%-90% in the case of non-EU foreign content; and (ii) 60%-70% in the case of EU foreign content	If domestic content is less than 30%, coverage terms are set on a case-by-case basis

Figure 28 compares the main aspects of the content policies of the G-7 ECAs in 2002. The data illustrate that Ex-Im Bank's content requirements do appear far more restrictive than Canada's and Japan's but are not so different overall than those of its European counterparts. The following two points should be noted:

- Most ECA policies are not transparent. In practice, ECAs are not always willing to provide the maximum amount of support for foreign content, particularly in the higher risk markets where ECAs generally have country exposure limits.
- Minimum domestic content requirement: To be eligible for any support, Ex-Im Bank does not have any minimum of domestic content required, while European ECAs

require 60%-90% domestic or EU content. Nevertheless, **Figure 28** shows that though Ex-Im Bank's implementation procedures appear to be generally competitive with the Europeans, the requirement that the foreign content be shipped from the United States is a constraint unique to Ex-Im Bank.

SUMMARY DATA

As shown below in **Figure 29**, the average percent of Ex-Im Bank's foreign content per transaction stayed generally within the 10%-12% range for the last five years. However, the export value (as a percentage) for transactions containing foreign content has increased significantly, from 81% in 2001 to 95% in 2002. This increase is due to the fact that in 2002, Ex-Im Bank support for large aircraft constituted approximately one half of Ex-Im Bank's medium- and long-term activity. Large aircraft transactions are typically high dollar value and include, on average, 11% eligible foreign content.

Figure 29: Recent Trends in Ex-Im Bank Foreign Content Support for Medium- and Long-Term Activity*

	Authorizations	1998	1999	2000	2001	2002
Total activity	Export value (\$MM)	\$6,612	\$10,500	\$9,455	\$7,109	\$8,212
	Number of transactions	225	211	267	227	222
Transactions containing foreign content	Export value (\$MM)	\$5,602	\$9,001	\$7,759	\$5,757	\$7,842
	% Of total value	85%	86%	82%	81%	95%
	Number of transactions	81	92	100	80	96
	% Of total number	36%	44%	37%	35%	43%
Foreign content	Volume (\$MM)	\$542	\$1,076	\$805	\$631	\$836
	Average per transaction	10%	12%	10%	11%	11%

* These figures exclude medium-term insurance. **Appendix F** provides a more detailed listing of Ex-Im Bank foreign content support for medium- and long-term transactions for 2002 (excluding medium-term insurance) at the time of authorization.

EXPORTER AND BANKER VIEWS

Of the 20 survey respondents who commented on the Bank's foreign content policy, 18 indicated that the policy was uncompetitive. Several exporters indicated that the European ECAs are more flexible in terms of directly financing other European Union countries' content as domestic

content. On the positive side, exporters acknowledged that the revised foreign content policy procedural changes were “a significant improvement” over the former procedures.

CONCLUSION

Ex-Im Bank’s approach to foreign content appears to be more transparent and predictable than the approaches taken by our G-7 counterparts. Moreover, the Bank’s approach is viewed as more competitive in 2002 than before the changes in 2001. On the other hand, the other ECAs still have more flexibility and a broader band within which they permit foreign content to be included. Consequently, Ex-Im Bank is marginally competitive as compared to the typical ECA competitor with regard to allowable foreign content.

Ch. VI Public Policies: Stakeholder Considerations

Section D: Local Costs

INTRODUCTION

In contrast to foreign content, the OECD Arrangement sets the basic parameters on official local cost support, which includes the ability of ECAs to provide local costs support for costs related to an officially supported export transaction. This support may not exceed the amount of the cash payment, typically 15%. All ECAs adhere to the local costs parameters set forth in the Arrangement. In fact, most major ECAs allow local costs support only when necessary. Their ability to do future business is constrained by country exposure limits and thus requires that local costs be explicitly included in the scope of the exporter's contract, i.e., for which the exporter bears the entire payment risk.

EX-IM BANK'S LOCAL COST POLICY AND PROCEDURES

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 for project-related local costs for goods and services that are directly related to the U.S. exporter's contractual responsibilities.

In early 2001, Ex-Im Bank approved changes to its local costs policy and procedures. While maintaining the 15% maximum, the changes were intended to make local costs support more readily available, provide greater flexibility for local costs financing in limited recourse project finance transactions and allow the exporter to minimize uncompetitive expenses associated with unintended taxes on locally procured goods and services. This change enabled Ex-Im Bank to capitalize on the absence of country exposure limits, versus our G-7 counterparts who regularly take this factor into consideration.

G-7 ECAS' POLICIES AND PROCEDURES

Nonetheless, there are some ECAs that would like to revise and/or abolish the local cost financing limitation in the OECD Arrangement. Most notably, the Norwegians recently proposed abolishing the OECD local cost limitations based on their view that: (1) such restrictions are no longer necessary to protect the local banking system; and (2) lifting the limit on official support for local costs could reduce the buyer countries' payments in foreign currency.

SUMMARY DATA

As **Figure 30** illustrates, since the 2001 local costs changes, there has been a significant increase in the number of transactions (but a modest increase in dollar volume) that have received local costs support. This increase may be attributed to the fact that the revised procedures provided more small and medium-sized U.S. exporters with greater certainty that local costs support would generally be available provided that the local costs are linked to the U.S. exporter's ability to secure the export sale.

Figure 30: Recent Trends in Ex-Im Bank Local Costs Support

	Authorizations	2000	2001	2002
Total medium- and long-term activity	Export value (\$MM)	\$9,455	\$7,109	\$8,212
	Number of transactions	267	227	222
Medium- and long-term activity containing local costs	Number of transactions	11	18	31
	% Of total number	4%	8%	14%
Local costs	Volume (\$MM)	\$183	\$192	\$213
	% Of total medium- and long-term activity	2%	3%	3%

EXPORTER AND BANKER VIEWS

More than half of the respondents who commented on the local costs policy in Ex-Im Bank's competitiveness survey indicated that the Bank's local costs policy in 2002 was as or more competitive than those of its counterparts. Exporters and bankers alike indicated the 2001 changes "have improved our ability to compete."

CONCLUSION

Based on both comparative information regarding our G-7 ECA counterparts and on the exporting community's actual experience with Ex-Im Bank's revised local costs policy, Ex-Im Bank is considered to be fully competitive with the best ECAs in its local costs support.

Ch. VI Public Policies: Stakeholder Considerations

Section E: U.S. Shipping Requirements

INTRODUCTION

In accordance with policies implementing Public Resolution No. 17 (PR 17) of the 73rd Congress, certain ocean-borne cargo financed by loans or credit guarantees from a U.S. government instrumentality, such as Ex-Im Bank, must be transported on U.S. flag vessels, unless a waiver of this requirement is obtained from the U.S. Maritime Administration (MARAD). Exports financed through Ex-Im Bank's medium- and long-term loan and long-term guarantee programs are subject to the U.S. flag vessel requirement, while exports financed under Ex-Im Bank's short- and medium-term insurance and medium-term guarantee programs are not required to be shipped on U.S. flag vessels.

PR 17 and other cargo preference legislation exists to ensure the continued viability of the U.S.-flagged commercial fleet. This fleet provides American jobs and essential marine services at U.S. ports and is an essential national security asset during times of war or national emergencies. Without cargo preference, the U.S. commercial fleet may decline due to competition from vessels operating under a "flag of convenience", because such vessels are subject to lower taxes and less stringent safety, labor and environmental standards. From the perspective of U.S. exporters, however, the U.S. flag vessel requirement can make U.S. exports less competitive vis-à-vis foreign competitors who have no similar requirements due to, among other things, the higher rates charged by U.S. shippers.

POLICY AND PRACTICE

Exporters are responsible for ensuring that they comply with Ex-Im Bank policy implementing PR 17. Pursuant to PR 17, upon request, MARAD may waive the U.S. flag vessel requirement on a case-by-case basis. There are four types of waivers:

- **General Waiver** allows the recipient country's merchant fleet to carry up to 50% of the cargo when the recipient country provides similar treatment to U.S. flag vessels in its foreign trade.
- **Statutory Waiver** is granted when it appears that a U.S. flag vessel will not be available within a reasonable amount of time or at a reasonable rate.
- **Compensatory Waiver** relates to situations in which goods are shipped on non-U.S. flag vessels, in honest error or through extenuating circumstances, prior to obtaining U.S. government financing, where such goods are otherwise subject to the U.S. flag vessel requirement. In such circumstances, the exporter may apply for a compensatory waiver whereby the exporter agrees with MARAD to ship an equivalent or greater amount of non-U.S. government impelled cargo on U.S. flag vessels within a specific time period.

- **Conditional Waiver** is granted for specific oversized cargoes if no U.S. flag vessel service capable of accommodating multiple shipments of oversized cargoes will be available during a proposed project time period.

If a waiver is obtained, Ex-Im Bank may provide financing for goods shipped on vessels of non-U.S. registry.

G-7 ECAs' POLICIES AND PROCEDURES

After consulting with the other G-7 ECAs, it has been determined that none of the other G-7 ECAs have similar cargo preference restrictions.

SUMMARY OF WAIVER DATA

Data on Ex-Im Bank financed loans provided by the Maritime Administration indicate that over the last five years (1998- 2002), 100% of the general waivers requested have been granted and approximately 93% of statutory waivers have been approved. Specifically, for general waivers, a total of 30 requests were submitted over the five-year period with none denied. For statutory waivers during the same time period, 362 requests for waivers were submitted with 23 denied and the remaining 339 approved. The highest number of statutory waiver requests submitted to MARAD in any year since 1990 was in 1996, totaling 327. Since then, the number of requests has declined from 326 in 1997, 137 in 1998, 66 in 1999, 76 in 2000, 60 in 2001 and 23 in 2002.

VIEWS OF INTERESTED PARTIES

The following comments are from both exporters on the Ex-Im Bank Advisory Committee and respondents to the banker and exporter competitiveness survey:

- Shipping costs for non-container cargo on U.S. flag vessels can be more than double that of non-U.S. flag carriers, and there is no clear definition or application of MARAD's "reasonable costs" doctrine, leaving the exporter open to seriously uncompetitive pricing.
- The age of the U.S. fleet makes the vessels very difficult to insure. While Ex-Im Bank does not require cargo insurance as a condition of cover, exporters feel the need to obtain it for their own risk management purposes.
- Lack of adequate U.S. flag vessels and ship-based loading facilities for the weights and dimensions of the goods being exported have caused exporters to risk damage to goods being shipped on vessels of inadequate dimensions.
- The inability to ship directly from the desired point of departure to the desired port of delivery, solely because of unavailability of U.S. flag carriers in a given port, causes exporters to pay much higher transportation costs, and it lengthens the shipping time and risks damage to sensitive goods.

- One exporter has reported it expects to lose export sales potentially financed by Ex-Im Bank due to higher costs associated with having to comply with PR 17.
- Another exporter explained that when they have a contract valued at greater than \$10 million, they now manufacture and source this equipment from their Canadian production facility rather than from the U.S. facility due specifically to PR 17 requirements. This exporter further explained that, with regard to the contracts that they now source from Canada (i.e., over \$10 million), they have also switched their purchase of components from U.S. suppliers to Canadian suppliers.

On the other hand, maritime unions and other supporters of cargo preference requirements believe that:

- Cargo preference costs are not a significant burden to Ex-Im Bank operations or to the competitiveness of Bank generated projects.
- Cargo preference may help U.S. exporters meet Ex-Im Bank domestic content requirements.

CONCLUSION

As a condition of Ex-Im Bank's direct loan and long-term guarantee financing, U.S. exporters are required to comply with U.S. flag vessel requirements. As no other G7 ECA has similar requirements related to shipping, the cargo preference rules clearly create competitiveness issues for U.S. exporters. Moreover, for large capital goods that cannot use container shipping, U.S. line availability and cost are frequently a competitive problem for U.S. exporters. While MARAD data indicate that the waiver process may be an effective means of addressing such problems, exporters believe that the U.S. flag vessel requirement has a significant impact on their competitiveness. Hence, the U.S. flag vessel equipment renders Ex-Im Bank much less competitive than our major ECA counterparts in this area.

Ch. VI Public Policies: Stakeholder Considerations

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

Public policy requirements tend to be, for the most part, unique to Ex-Im Bank vis-à-vis the other G-7 ECAs. With the exception of local costs support, where Ex-Im Bank is as competitive as its official counterparts, the other public policy factors can and have had an adverse effect on the overall competitiveness of transactions.

However, because any one or a multiple of these requirements affects only a certain portion of cases in any given year (vs. broad and deep impact), the overall impact of the policy factor on Ex-Im Bank support is less than the impact of the core financing elements. This limited impact is reflected in the relatively lower weighting that this category receives (see **Appendix A**), as shown in the summary report card in Chapter 7.

Figure 31: Grading of Ex-Im Bank's Public Policy Competitiveness

Policy	G-7 ECAs have similar constraint (Y/N)	Grade
Economic Impact	N	B
Foreign Content	Y	B+
Local Costs	Y	A+
PR 17	N	C
Total Average Grade		B+

Ch. VII Conclusion

Overall in 2002, Ex-Im Bank operated along a fine line between an A and an A- but ultimately came out with a grade of A-, indicating that the Bank was selectively competitive (i.e., in most cases equivalent to the typical G-7 competitor) with its G-7 ECA counterparts (see **Figure 32**). The specific financing elements such as premia, interest rate and cover policy are essential to each transaction and therefore the most important, and in these core financing areas Ex-Im Bank is most competitive overall. Ex-Im Bank is also considered competitive in the major program structures of aircraft, foreign currency and project finance. The one area within Ex-Im Bank's control where Ex-Im Bank is less competitive is co-financing, primarily because Ex-Im Bank has concluded only two bilateral agreements.

In the economic philosophy and public policy areas, over which Ex-Im Bank has little to no control, Ex-Im Bank fares less well, with the exception of local costs support where Ex-Im Bank is considered slightly better than the other G-7 ECAs. Foreign content, PR 17, economic impact and market windows, when confronted, tend to offset the competitiveness of a given transaction. See **Appendix A** for the background behind the determination of Ex-Im Bank's overall competitiveness grade.

Figure 32: Grading of Ex-Im Bank's Overall Competitiveness

Key Elements	Grade
Core Business Policies and Practices	A
A. Cover Policy & Risk Taking	A
B. Interest Rates	A
C. Risk Premia	A+
Major Program Structures	A-
A. Large Aircraft	A
B. Project Finance	A
C. Co-financing	B
D. Foreign Currency Guarantee	A+
Economic Philosophy	B-
A. Tied/Untied Aid	B
B. Market Windows	C
Public Policies	B+
A. Economic Impact	B
B. Foreign Content	B+
C. Local Costs	A+
D. Shipping/PR 17	C
OVERALL GRADE	A-

Appendix A: Calculation of Ex-Im Bank Grade

In the body of this report, Ex-Im Bank graded its policies and programs. In order to aggregate and average these grades for the determination of the overall competitiveness grade in Chapter 7, indicative 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. Ex-Im Bank averaged multiple sub-category grades to determine a category's grade, resulting in a raw score that did not precisely correspond to a particular grade. **Figure A2** illustrates the range of possible averaged scores that Ex-Im Bank defined for each grade.

Figure A1: Definition of Select Grades

Grade	Definition	Score
A+	Fully competitive: equivalent to (or is) the best competitor	4.33
A	Generally competitive: in almost all cases equivalent to the typical G-7 competitor	4.00
A-	Selectively competitive: in most cases equivalent to the typical G-7 competitor	3.67
B+	Marginally competitive: in significant minority of cases equivalent to the typical G-7 competitor	3.33
B	Notch below: can, but only rarely, package a deal equivalent to the typical G-7 competitor	3.00
C	Much less competitive: can/does provide a product in the class but is rigidly constrained (or little used)	2.00
F	Does not provide program	0.00

Figure A2: Range of Averaged Scores for Each Grade

Grade	Maximum Score	Minimum Score
A+	4.330	4.165
A	4.164	3.835
A-	3.834	3.500
B+	3.499	3.165
B	3.164	2.835
B-	2.834	2.500
C+	2.499	2.165
C	2.164	1.835
C-	1.834	1.500
D+	1.499	1.165
D	1.164	0.835
D-	0.834	0.670
F	0.669	0

With the definitional context of **Figures A1** and **A2**, **Figure A3** provides the detailed grading of Ex-Im Bank's overall competitiveness. The weighting assigned to each category (i.e., 40%, 15%, 5%) is intended to reflect the volume and frequency of transactions that are impacted by the specific element or category. For example, because every medium- and long-term case is affected by the core financing elements, that category receives a 40% weight, whereas tied aid and market window financing affect only a small portion of cases and therefore receive a 5% weight. Each element within each category was not assigned a specific weight out of concern that this grading system does not bear too much numerical refinement.

Figure A3: Detailed Grading of Ex-Im Bank's Overall Competitiveness

Key Elements	Grade	Value	Weight	Score
Core Business Policies and Practices	A	4.11	40%	1.64
A. Cover Policy & Risk Taking	A	4.00		
B. Interest Rate	A	4.00		
C. Risk Premia	A+	4.33		
Major Program Structures	A-	3.83	40%	1.53
A. Large Aircraft	A	4.00		
B. Project Finance	A	4.00		
C. Co-financing	B	3.00		
D. Foreign Currency Guarantee	A+	4.33		
Economic Philosophy	B-	2.50	5%	0.13
A. Tied/Untied Aid	B	3.00		
B. Market Windows	C	2.00		
Public Policies	B+	3.17	15%	0.47
A. Economic Impact	B	3.00		
B. Foreign Content	B+	3.33		
C. Local Cost	A+	4.33		
D. Shipping/PR 17	C	2.00		
OVERALL GRADE	A-			3.77

Appendix B: Purpose of Ex-Im Bank Transactions

Ex-Im Bank's Charter was renewed and amended in 2002. A new reporting requirement was added in Sec. 2(b)(1)(A) which stated that Ex-Im Bank shall include in the annual Competitiveness Report a description of all Bank transactions classified according to their principal purpose. This information is provided below, broken down by program and classified according to the principal purposes for which Ex-Im Bank support was sought.

Figure B: Ex-Im Bank Transactions by Purpose

	No Private Sector Finance Available		Meet Competition		Not Identified*	
	(\$MM)	(#)	(\$MM)	(#)	(\$MM)	(#)
Working capital guarantees	480.6	282	0	0	179.9	71
Short-term insurance	1,780.9	1,742	0	0	0	0
Medium-term insurance	434.5	274	2.9	6	3.5	4
Guarantees	3,921.7	189	2,878.6	25	512.3	17
Loans	210.3	2	0	0	0	0
TOTAL	\$6,828.0	2,489	\$2,881.5	31	\$695.7	92

*At the time of Ex-Im Bank's mid-2002 re-authorization, internal data systems were not completely set up to capture the newly required information.

Appendix C: Exporter and Banker Survey Results

INTRODUCTION

As mandated by Congress, Ex-Im Bank conducts an annual survey of exporters and banks for the Competitiveness Report. This survey is a critical part of this Report as it encourages respondents to compare Ex-Im Bank's policies and practices with those of our G-7 ECA counterparts. With this information, Ex-Im Bank is better informed as to which policies, practices and products make a competitive difference either positively or negatively and where improvements might be made. Exporters and banks selected to participate in the survey were among the top 100 users of Ex-Im Bank programs for 2002, based on total volume of authorizations and the total number of transactions. In addition, a new approach was adopted for this year's report with regard to the export finance community's view of Ex-Im Bank's competitiveness. At the suggestion of members of the exporting community, Ex-Im Bank conducted separate focus group meetings with banks and exporters to enable them to verbally supplement their survey responses with more context on the export finance market in which they operate and related competitiveness implications for Ex-Im Bank.

SURVEY

Ex-Im Bank's survey consisted of five parts focusing 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 two major areas:
 - Cost of financing: exposure fees, cover policy and interest rates
 - Non-cost policies: environment, content requirements, economic impact, co-financing, local cost support, and tied aid policy
- Part 4: Additional comments
- Part 5: Outcome of specific cases of competition faced as a result of the above policies

PARTICIPANT SELECTION

In deriving the list of respondents, Ex-Im Bank screened for survey participants that met the following criteria:

- Used Ex-Im Bank's medium- and long-term programs during 2002;
- Faced officially supported competition in their sales; and
- Were knowledgeable about both Ex-Im Bank and foreign ECA programs and practices.

SURVEY RESULTS

Figure C1 highlights the response rate for participants. The bank respondent rate was 38%, which was less than in 2001. Exporters' response rate was 58%, also less than the rate in 2001. Of the banks that did not respond, the most notable characteristics were that they were either foreign-owned or smaller regional lenders. The exporter non-respondents tended to be large or medium-sized capital equipment manufacturers.

Figure C1: Survey Response Rate

	Lenders		Exporters	
	2001	2002	2001	2002
Number surveyed	30	32	17	19
Number responded	16	12	13	11
Response rate	53%	38%	76%	58%

LENDERS

The 60% of the responding lenders fell into the regional/super-regional category, and 40% were representative of large international lenders, of which three were foreign-owned. As **Figure C2** illustrates, all but two of the banks had been in business for over 20 years and had also been in the export finance business for a similar period of time. The two exceptions were regional banks, each of which had been in business for over 20 years and had at least four years of trade finance experience.

Figure C2: Lender Experience Levels

	1-3 years	4-10 years	11-20 years	20+ years
Time in business	-	-	-	12
Time in trade finance	-	1	1	10

The international lenders were more familiar than the regional/super-regional lenders with the programs and policies of Ex-Im Bank's G-7 ECA counterparts, both in terms of working with and competing against these entities. The ECAs most noted as "frequent" partners were Coface and Hermes, and to a lesser extent SACE and JBIC/NEXI. Interestingly, the same ECAs are cited as those most often faced in the heat of competition by the international lenders. Little difference existed among the respondent lenders with regard to why they used Ex-Im Bank: lack of market financing due to heightened perceptions of risk was the predominant reason (75%-80%) followed by meeting competition (25%-30%). Heightened perceptions of risk tend to drive lenders to Ex-Im Bank, with equal concern regarding the Latin American, African, Asian and Eastern European emerging markets.

Specific comments and ratings received from the banking community through the survey have been incorporated into the chapters on the core and non-core elements that constitute an export credit offer. Comments received through the survey were consistent with those given during the lender focus group meeting. To summarize, Ex-Im Bank was viewed as:

- At least as competitive, if not more so, than its G-7 ECA counterparts in the core business policies and practices;
- Generally competitive across the major program structures, except for, most notably, co-financing; and
- Uncompetitive in the public policy arena (e.g., content, PR 17).

The banking community unanimously agreed that the elements posing the greatest competitive constraints on Ex-Im Bank are its public policies. Moreover, although they acknowledged that the public policy issues were not entirely within Ex-Im Bank's control, they nevertheless felt it important to offer recommendations as to how to minimize the adverse consequences. These included the following suggestions:

- Liberalize foreign content policy and interpretation of PR 17;
- Expand co-financing capabilities with a streamlined process and the addition of a long-term insurance product; and
- Significantly improve Ex-Im Bank's case processing time, especially in the medium-term, where turnaround time has deteriorated significantly (one lender cited a lost sale due to delays in processing).

EXPORTERS

The exporter respondents to Ex-Im Bank's survey were large multi-national corporations that have had extensive experience with exporting and using Ex-Im Bank programs, as illustrated in **Figure C3**.

Figure C3: Exporter Experience Levels

	1-3 years	4-10 years	11-20 years	20+ years
Time in business	-	-	-	11
Time in trade finance	-	1	-	10

These corporations are well qualified to comment on and provide insights about Ex-Im Bank's competitive position vis-à-vis its G-7 ECA counterparts in terms of both cooperation and competition with them. Hermes, EDC and SACE were cited as the ECAs from which the exporters had obtained export credit support, while Coface, Hermes, JBIC/NEXI, ECGD and, to a lesser degree, SACE, were identified as the ECAs most frequently encountered in competitive situations. Lack of market financing was the primary reason for using Ex-Im Bank, followed closely by the need for competitive financing to counter offers from other official ECAs.

The exporters evaluated Ex-Im Bank's competitiveness as follows:

- Ex-Im Bank is as competitive, and often more competitive, in the core business policies and practices.
- Ex-Im Bank is generally competitive in the major program structures (e.g., project finance, aircraft).
- Market window financing, though hard to quantify, is becoming a more serious threat in more markets and across more sectors.
- Ex-Im Bank is uncompetitive in the public policy areas.

Much like their banking colleagues, the exporters agreed that the most significant impediments to Ex-Im Bank's competitiveness with its G-7 ECA counterparts are the public policy elements. They too noted that these issues were the most difficult and complex to overcome, given the political sensitivity of the multiple interests typically involved. However, given the importance and growing frequency of these factors in competitive situations, the exporters felt it critical to articulate their views and recommendations for resolution. The specific suggestions included the following:

- Create a long-term insurance product to facilitate co-financing structures;
- Develop a long-term lease guarantee;
- Guarantee performance bonds; and

- Ensure a continued ability to explicitly match any and all ECA financing offers, including market windows.

CONCLUSION

Two consistent themes emerged from both lenders and exporters:

- Components over which Ex-Im Bank has absolute or near total control were considered to be very competitive as compared to its foreign ECA G-7 counterparts: interest rates, premia, cover policy and risk assumption and local cost support.
- Components that required the participation of outside parties (e.g., labor, Congress, industry, other U.S. agencies and other ECAs) to develop, improve or strike a more reasonable balance (and in some cases would require statutory modifications) represented those elements in which Ex-Im Bank was considered less than competitive (e.g., economic impact, foreign content, PR 17, co-financing, tied aid, market windows).

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 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 export credit insurance on behalf of the French government.
- Germany**
- **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 another part of the German government.
- Italy**
- **SACE**, or the Istituto Per I Servizi Assicurativi Del Credito all’Esportazione, is a public company with its own assets and operational authority. It provides official export credit insurance.
 - **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). Japanese exporters are required to insure all of their short-term business through NEXI, the result being that NEXI provides a tremendous volume of short-term insurance relative to other countries, where the lion's share of short-term export credit insurance is provided by the private sector.
- 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 is customarily available from other countries.

Appendix E: State of Play in the OECD

INTRODUCTION

One of Ex-Im Bank's primary objectives is to level the playing field for U.S. exporters facing foreign competition supported by their governments' official export finance programs. Ex-Im Bank's financing, while critical to U.S. exporters in developing and emerging markets, cannot neutralize every competitor's best offer on every deal. Should there be no multilaterally accepted export credit regime, the aggregate weight of the competing governments, who are more inclined to pick winners, would quickly overcome Ex-Im Bank support. Moreover, to the extent that governments are allowed to subsidize export financing (e.g., by charging below-market interest rates, providing tied aid for commercially viable transactions or not charging risk-related fees, etc.), the private sector is crowded out as exporters and buyers are drawn to cheap government-provided financing.

In this context, the best tool for long-run success in achieving a level playing field is the negotiation table. Since the Arrangement came into force twenty-five years ago among the major exporting industrialized nations, the United States and the OECD as a whole have negotiated disciplines on repayment terms, interest rates, tied aid and exposure fees, in addition to rules on specific sectors such as large commercial aircraft. These disciplines have significantly reduced the potential volume of subsidized transactions that would need to be neutralized by matching financing. Indeed, with the interest rate disciplines alone, Ex-Im Bank has eliminated losses that, in the early 1980s, were up to \$50-\$100 million per year for every \$1 billion loaned. Another key accomplishment has been the tied aid regime, which, it is estimated, has saved the U.S. government \$300 million per year since 1993. Critically, these official export finance disciplines have created room for the private export finance sector to operate.

With these disciplines, official export credit agencies have significantly reduced their operating losses, and the OECD Export Credit Group in aggregate has experienced positive cash flows since the mid-1990s. This development, while obviously positive, has nonetheless removed the major impetus ECAs had to reach multilateral agreements on additional financial disciplines. In fact, the 1997 Knaepen Package on exposure fees was the last major financial discipline added to the export credit field. Since then, the member countries have made progress on a variety of issues along a much broader spectrum of concerns ("social" issues such as environment, bribery, Highly Indebted Poor Countries, etc.); such work continued in 2002.

OFFICIAL EXPORT CREDIT NEGOTIATIONS: KEY 2002 DEVELOPMENTS

The process of adopting multilateral rules to eliminate official export credit subsidies and level the playing field typically involves the following five stages:

1. Agreement to exchange information or establish transparency in order to provide the basis for work on a particular issue;
2. Creation of a system or framework of rules that can lead to reductions in subsidy and/or further level the playing field;
3. Establishment of a yardstick within the framework by which progress can be measured (e.g., charging market level interest rates or requiring a project to be commercially non-viable in order to allow tied aid);
4. Moving the yardstick higher (i.e., requiring ever higher interest rates until zero subsidy is achieved, or increasing the minimum concessionality in tied aid); and
5. The ongoing process of refining and adapting any rules as more knowledge becomes available and/or the world changes.

Against this framework, 2002 witnessed the following developments:

ARRANGEMENT

The Arrangement has been moving through these stages over time, evolving to significantly parameter the rules and conditions for the provision of official export credits. As evidence of its place in the multilateral trade regime, it is referenced in the WTO's Agreement on Subsidies and Countervailing Measures (ASCM) as a safe haven under which official export credits may be provided without being considered a prohibited subsidy. This safe haven, item k(2) of Annex I of the ASCM, refers only to the "interest rate provisions" of the Arrangement. As a result of the Canada-Brazil aircraft disputes over the past few years, WTO Panels and the Appellate Body have made several rulings on the Arrangement that have raised the concern of the Participants. These rulings include the judgment that pure cover transactions are not covered under the safe haven of item k(2) as the Arrangement has no "interest rate provisions" (no minimum interest rate system) related to pure cover. In addition, the Panels found that matching non-conforming transactions is not in conformity with the WTO, i.e., being in conformity with the Arrangement *as a whole* (provisions beyond the "interest rate provisions") does not equate to being in conformity with the WTO.

Spurred by these findings, and by export credit related presentations made by non-Participants at the WTO, the Participants agreed in 2002 to undertake a re-draft of the Arrangement. The goals of the re-drafting exercise were clarity, consistency (within the Arrangement and with the WTO) and transparency for non-Participants. It is anticipated that a final draft of the new Arrangement will be achieved by the end of 2003.

INTEREST RATES

Official export credit interest rates are subject to disciplines that have, for the most part, eliminated potential subsidies in this area. In principle, ECAs that compete on a fixed rate Commercial Interest Reference Rate (CIRR) regime basis should be in a neutral competitive position with respect to interest rates. However, there are two areas of potential competitive concern. First, the different ways in which ECAs interpret the CIRR rules (setting and holding of CIRR rates) can have potential competitive implications. Second, the CIRR regime provides potential for a certain degree of subsidization via interest make-up (IMU) schemes. As has been the case since 1998, little formal action was taken on any of the CIRR issues during 2002. This lack of formal action was primarily due to the fact that the issue of revising the CIRR regime has been linked to other issues, such as market windows and interest make-up. It is uncertain when or if work will progress on this issue. In sum, the interest rate negotiations on the current CIRR regime as a whole have advanced to stage 5 and represent the issue for which the most progress has been achieved to date.

Discussions of creating a floating rate CIRR largely stalled in 2002, with both the United States and the European Commission opposing the creation of such an instrument. This issue arose in 2000 as a result of the WTO dispute between Canada and Brazil over export credit support for regional aircraft. In the Brazil-Canada cases, the WTO held that, under the ASCM, officially supported export credits are a prohibited subsidy unless they are on market terms (from the borrower's perspective, i.e., the benefit to the borrower test) or the support is in compliance with the OECD Arrangement interest rate provisions. The WTO held that the OECD interest rate provisions only yield a safe harbor for the CIRR fixed interest rate and, therefore, provide no safe harbor for individually determined floating rate lending by ECAs or for pure cover.

However, due to the technical and philosophical complexity of designing a floating rate CIRR that does not compete with commercial bank activity, work on a floating rate CIRR has not progressed beyond stage 1.

MARKET WINDOWS

A topic closely entwined with both the interest rate and Arrangement discussions is market windows. A market window is an institution (or a part of an institution) that claims to operate on a commercial basis while benefiting either directly or indirectly from some level of government support. Over the years, market windows have come under scrutiny with allegations that they provide non-market financing terms that skirt Arrangement restrictions. Market windows have posed transaction-specific problems to other ECAs because:

- the support provided by such entities is only available to their national economic interests; and
- the attractiveness of the financing packages (especially interest rates) provided by market windows tends to stretch the boundaries of what a private institution might be willing to provide.

The United States believes that the growth in market window activity represents a potential threat to the disciplines that the OECD Arrangement negotiations have sought to instill in all official lenders. In 2002, the United States proposed a transparency exercise in the OECD to shed more light on the nature and potential impact of market window transactions, and this exercise was rejected. The Participants with major market windows (Canada and Germany) have consistently made the point that transparency conflicts with their commercial confidentiality rules. Until some way is found to reduce or avoid that conflict, little progress can be made on the market window issue. Thus, the market windows issue has not even reached stage 1.

To evaluate the possible effects of market windows on the U.S. economy, the U.S. Trade Promotion Coordinating Committee (TPCC) recommended in 2002 the commissioning of a study on the effects of market window institutions.

EXPOSURE FEES (RISK PREMIA)

The Knaepen Package, which seeks convergence on the pricing of officially supported export credits of over two years repayment term, came into force on April 1, 1999. The agreement sets minimum exposure fees for sovereign transactions. In addition, the sovereign benchmark sets the minimum rate for all other transactions within the country. Exposure fees are the charges imposed by ECAs for taking the risk that the obligor will not repay. All transactions other than aircraft, military, agriculture and ships are subjected to its disciplines. In the past these charges varied tremendously between ECAs in any given market.

The fee negotiations have remained at stage 3 for the past few years. In 2002, discussions continued on enhancing the feedback mechanism for evaluating the fee system, and transparency exercises were conducted on buyer risk pricing. There continues to be some pressure from European ECAs, who have a structural system of assessing surcharges on non-sovereign buyers, to open negotiations on buyer risk pricing. It is anticipated that discussions on buyer risk and evaluating the existing premium rate system will continue in 2003.

LARGE COMMERCIAL AIRCRAFT

The provision of official export credit support for large commercial aircraft (typically those airplanes that have more than 70 seats and are powered by a jet engine) is governed by a special sub-set of rules, known as LASU (Large Aircraft Sector Understanding). In short, the rules that apply to large commercial aircraft have been customized to better fit the unique characteristics of this business. Contrary to standard official export credit transactions, LASU does not explicitly address the issue of exposure fees (risk premia).

Ex-Im Bank meets regularly with its foreign counterparts to discuss issues of common interest and to refine the rules of the Arrangement that govern official export credit support provided by OECD members. Nonetheless, in 2002 there were no resolutions between the European ECAs and Ex-Im Bank regarding modifications to the LASU.

The beginning of production of over 70-seat aircraft by Canada and Brazil has created a need to re-open the LASU, and major negotiations may begin in 2003. Thus, this issue remains in stage 4 but could move to stage 5 during 2003.

TIED AND UNTIED AID

A major accomplishment of 2002 was the formal agreement reached in November on defining “projects” to include front-end engineering and design studies, architect and engineering work, and procurement-related technical assistance. Japan agreed that the tying status of its support for upfront technical assistance will now match the tying status of its support for the project itself, i.e., both will be tied or both will be untied. The United States sought for years to end the Japanese practice by which the financing of upfront consulting work was tied to Japanese firms, because discussions with U.S. exporters yielded a uniform opinion that tied technical assistance virtually dictates the outcome of the bidding process for the ensuing project procurement receiving “untied” aid support. In this regard, the tied aid negotiations remain at the early phase of stage 4.

In 2002, the Participants continued to discuss the application of tied aid rules to untied aid. There are currently no Arrangement rules governing untied aid, because the donor government does not legally tie procurement to its firms. However, untied aid can be “de facto tied” and used to circumvent the tied aid disciplines that require a minimum concessionality and preclude tied aid for commercially viable projects and to rich countries. Discussions on extending the Helsinki disciplines to untied aid continued during 2002 with little progress. However, untied aid is notified and is the subject of an extensive statistical annual report. Untied aid discussions have therefore still not moved beyond stage 1. The United States will continue to seek disciplines on untied aid practices in 2003.

ENVIRONMENT

At the end of 2001, negotiations within the ECG on common environmental guidelines stopped when the United States refused to agree to the draft text, because it failed to provide sufficient *ex ante* transparency with regard to sensitive projects and because it failed to set international environmental standards (e.g., World Bank) as a minimum requirement rather than as a benchmark. In 2002, the rest of the ECG began to voluntarily and unilaterally implement their own environmental review procedures, based on the draft set of recommendations on ECAs and the environment.

Throughout 2002, ECG members gave presentations on their environmental review policies and practices. In September, a group of environmental practitioners met to exchange practical experience with implementing the Common Approaches, as the draft OECD text is called. The technical exchanges in 2002 indicate that progress is truly being made by most OECD ECAs in implementing meaningful environmental review of projects. There appears to be greater convergence toward World Bank guidelines, although some members have not clearly specified what standards and guidelines they use to assess projects. *Ex ante* transparency remains a larger

challenge, as several members are subject to strict confidentiality rules that limit their ability to disclose project-related information.

The information exchanges from 2002 will lay the groundwork for the review of the Common Approaches in 2003. The United States will continue to seek common rules of engagement to maintain a level playing field and to prevent an environmental “race to the bottom”, in which the lack of common rules provides a competitive advantage to financing packages and project design supported by ECAs with the most lax standards.

Thus, the environment negotiations did not advance in 2002 but will likely do so in 2003. Ex-Im Bank is encouraged by the efforts made by other ECAs and hopes the group will achieve stage 4 by the end of 2003.

Appendix F: Ex-Im Bank Foreign Content Support for Medium- and Long-Term Transactions* in 2002

Country	Product	Export Value	Foreign Content Percentage**	Estimated Budget Increase***
Australia	Large Aircraft	\$666,839,965	10%	\$1,045,268
Austria	Large Aircraft	\$234,381,127	16%	\$2,202,035
Bolivia	Manufacturing Equipment	\$988,200	2%	\$2,866
Brazil	Manufacturing Equipment	\$68,196,277	20%	\$36,881
Brazil, Czech Republic, Mongolia and Turkey	Large Aircraft	\$455,395,840	15%	\$2,839,267.35
Bulgaria	Concession Equipment	\$2,182,388	4%	\$14,428
Bulgaria	Foam Extrusion System	\$1,155,275	2%	\$3,069
Cameroon	Trucks & Equipment	\$1,358,366	13%	\$28,085
Canada	Large Aircraft	\$546,995,000	15%	\$4,020,411
China (Mainland)	Engineering & Construction Services	\$175,350,552	5%	\$14,694,247
China (Mainland)	Medical Equipment	\$8,443,000	1%	****
China (Taiwan)	Large Aircraft	\$149,232,027	5%	\$478,489
Cote D'Ivoire	Trucks	\$1,133,679	15%	\$15,338
Dominican Republic	Heavy Construction Equipment	\$30,199,690	8%	\$281,277
Dominican Republic	Pre Fabricated Housing Units	\$25,101,230	5%	\$209,166
Dominican Republic	Project Management Services	\$16,973,720	12%	\$197,383
Dominican Republic	Sporting Equipment	\$49,590,074	5%	\$2,019,008
Dominican Republic	Exporter Services	\$39,823,735	10%	\$2,034,759
Dominican Republic	Engineering And Procurement Services	\$70,706,426	1%	\$589,850
Dominican Republic	Engineering And Procurement Services	\$83,838,464	0.3%	\$575,197

Country	Product	Export Value	Foreign Content Percentage**	Estimated Budget Increase***
Dominican Republic	Ocean Transport Services	\$100,000,000	10%	\$4,952,480
Dominican Republic	Air Conditioners	\$22,671,280	8%	\$72,526
Dominican Republic	Training	\$68,027,767	12%	\$529,541
Ireland	Large Aircraft	\$95,000,000	15%	\$196,191
Ireland	Large Aircraft	\$155,000,000	15%	****
Ireland	Large Aircraft	\$248,000,000	15%	****
Israel	Large Aircraft	\$114,300,000	14%	\$2,429,246
Israel	Motor Starter	\$3,127,312	10%	****
Kazakhstan	Software	\$420,016	24%	\$2,624
Kenya	Large Aircraft	\$80,914,678	16%	\$202,913
Korea, Republic	Large Aircraft	\$125,000,000	14%	\$1,537,452
Korea, Republic	Large Aircraft	\$460,000,000	8%	\$3,990,363
Luxembourg	Large Aircraft	\$146,000,000	19%	\$388,212
Federation of Malaysia	Large Aircraft	\$710,264,008	9%	\$2,551,180
Mali	Graders, Dozers, Compactors And Trucks	\$2,152,290	5%	\$18,109
Mexico	Legal Services	\$86,162,300	12%	\$1,350,925
Mexico	Technical Services	\$30,407,167	4%	\$305,034
Mexico	Base Transceiver Stations Systems	\$100,000,000	15%	\$476,706
Mexico	Gas & Steam Turbine Generators, Controls	\$179,125,000	12%	\$3,736,622
Mexico	Paper Converting Machine	\$16,910,592	9%	\$13,430
Mexico	Gas Turbine Compressors	\$64,281,885	12%	\$1,290,125
Mexico	Wholesale Industrial Machinery	336,395,494	4%	\$849,446
Mexico	Well Drilling Services	\$223,950,914	0.4%	\$54,609
Mexico	Geophysical Instruments & Equipment	\$223,986,474	4%	****
Mexico	Punch Machine	\$310,080	18%	\$777
Mexico	Greenhouses	\$853,688	13%	\$1,971
Mexico	Shrimp Harvesting Equipment	\$942,870	7%	****
Mexico	Plastic Manufacturing Equipment	\$4,168,260	8%	****
Morocco	Large Aircraft	\$43,400,000	15%	\$515,646

Country	Product	Export Value	Foreign Content Percentage**	Estimated Budget Increase***
Morocco	Large Aircraft	\$37,900,000	16%	****
Mozambique	Trucks	\$672,660	12%	\$13,354
Nigeria	Submersible Motor Pumps	\$117,641,154	1%	\$1,544,181
Nigeria	Hardware, Software, Training & Services	\$10,183,261	23%	\$231,345
Nigeria	Prefabricated Workshops	\$786,697	3%	\$2,196
Panama	Large Aircraft	\$139,400,000	17%	\$2,205,627
Peru	Medical & Laboratory Equipment	\$1,500,000	10%	\$24,260
Philippines	Hydraulic Rotary Pipe Sander	\$506,469	8%	\$841
Romania	Transmitter Systems	\$71,469,583	6%	\$3,251,607
Romania	Steam Turbine Parts & Technical Svcs	\$29,676,464	7%	\$162,029
Romania	Various Medical Equipment	\$4,265,889	14%	\$44,740
Russia	Construction Management	\$15,700,000	4%	\$499,115
Russia	Wheel Loaders and Bulldozers	\$3,536,053	7%	\$39,603
Russia	Wheel Loaders and Bulldozers	\$1,042,057	5%	\$8,027
Russia	Drill Attachments And Tractors	\$3,326,500	7%	\$5,383
Russia	Truck, Wheel Loader, Hydraulic Excavator	\$9,322,313	10%	\$144,043
Russia	Dump Trucks & Cold Weather Components	\$11,750,000	15%	\$83,368
Russia	Communications Network	\$10,296,250	14%	\$70,010
Saudi Arabia	Trucks	\$6,670,548	23%	****
Senegal	Trucks & Road Construction Equipment	\$804,800	8%	****
Senegal	Bulldozer, Graders, Loaders, Excavator	\$2,068,999	5%	\$15,579
Senegal	Backhoe, Drilling & Gold Mining Equipment	\$304,235	15%	\$7,284
Senegal	Refrigerated Truck	\$251,109.00	10%	\$577
South Africa	Large Aircraft	\$210,000,000	15%	\$304,779
Thailand	Solar Cells	\$203,900,000	12%	\$2,918,877
Thailand	Large Aircraft	\$299,964,569	5%	****

Country	Product	Export Value	Foreign Content Percentage**	Estimated Budget Increase***
Turkey	Aircraft Engines	\$80,758,374	15%	\$1,055,674
Turkey	Financial Services	\$69,520,157	17%	\$4,377,737
Turkey	Generator Set	\$8,195,900	12%	\$112,726
Turkey	Hotel Equipment	\$13,500,886	26%	\$134,635
Turkey	Hospital Equipment & Machinery	\$14,512,215	13%	\$80,332
Turkey	Heating and Cooling Equipment	\$10,796,272	15%	\$258,984
Turkey	Molecular Biology Laboratory Instruments	\$2,584,851	14%	\$24,959
Turkey	Construction Machinery	\$5,044,786	15%	\$76,574
Uganda	Trailers With Forklifts	\$1,928,000	5%	\$15,926
Uganda	Construction Equipment	\$805,264	2%	\$2,657
Uzbekistan	Combines Transmission, Drive & Gear Box	\$16,105,845	15%	\$367,202
Uzbekistan	Multi-service Node & Switching Equipment	\$5,184,814	15%	\$136,655
Venezuela	Diesel Engine Parts	\$19,426,392	5%	\$4,822
Venezuela	Water-To-Air Cooling Module	\$93,353,300	21%	\$2,333,192
Venezuela	Marine Air Conditioning & Refrigeration	\$8,859,445	6%	\$8,830
Venezuela	River Hopper Barges	\$6,156,730	7%	\$21,685
Venezuela	Oncology Systems	\$2,211,293	6%	\$3,191
Venezuela	Wastewater Treatment Plant Equipment	\$4,629,200	5%	\$118,013
Venezuela	Cable System	\$6,647,635	2%	****
Venezuela	Material Handling Equipment	\$849,763	12%	\$4,871
Venezuela	Telecommunications Network Equipment	\$8,600,000	20%	\$193,879
Total		\$7,842,267,842	11%	\$76,327,689

*Preliminary data, excludes Credit Guarantee Facilities

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

***Increase in the estimated budget amount for the U.S. portion of the contract due to the inclusion of foreign content in the financing package

****No budget increase (negative budget cost)

Appendix G: Tied Aid Report

Implementation of the Helsinki Tied Aid Disciplines

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 during 2002, followed by a discussion of trends in the use of the TACF through 2002. Finally, it addresses other actions and plans to combat predatory financing practices.

IMPLEMENTATION OF THE OECD ARRANGEMENT RULES

This section describes the continued implementation of the Helsinki Package of tied aid disciplines, including foreign governments' compliance, the operation of notification and consultation procedures and, finally, the outcome of Consultations Group activity.

Tied aid is concessional financial support provided by donor governments in the form of a grant or a "soft" loan for which capital goods procurement by developing countries is contractually linked to firms from the donor country. In December 1991, the Participants to the Arrangement agreed to the Helsinki Package of rules on tied aid credits aimed at limiting the use of concessional financing for projects that should be able to support commercial financing. The rules went into effect on February 15, 1992. The Helsinki Package established: (1) country and project conditions for the provision of tied aid; (2) rules requiring notification of tied aid offers; and (3) mechanisms for consulting and in some cases challenging whether tied aid offers conform to established guidelines.

The Helsinki rules on minimum terms and conditions basically resulted in two disciplines being imposed on tied aid: (1) no tied aid in "rich" countries; and (2) no tied aid for commercially viable projects. These new rules were built on an OECD agreement in the mid-1980s that set a minimum concessionality level for tied aid of 35%⁹ and instituted a market-based system for measuring concessionality.

TIED AID ELIGIBLE MARKETS

A number of key markets are no longer potential targets for tied aid financing as a result of the implementation of the Helsinki Package and other OECD agreements. These markets include

⁹ The term "concessionality" refers to the total value of the subsidy being provided by the donor to the recipient country for any one project or purchase. For example, if a country receives a grant of \$100 million for a \$100 million project, the concessionality of this aid would be 100%, whereas a grant of \$35 million combined with a traditional export credit for the remaining \$65 million would have a concessionality of 35%.

several important countries in Africa, the Americas, Asia and the Middle East, all of which are either “high income” or “upper middle income” countries according to World Bank criteria. In addition, as a result of a separate OECD agreement, U.S. exporters bidding on commercial type transactions in the major markets of Eastern Europe and the former USSR do not confront tied aid (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.

TIED AID ELIGIBLE PROJECTS

The Helsinki Package established the principle that tied aid should not be used for “commercially viable” projects, defined as revenue-generating projects which:

- generate operating cash flows sufficient to repay debt obligations on standard OECD Arrangement export credit terms; and
- could potentially attract standard export credit financing (two OECD export credit agencies would, in principle, be prepared to provide export credit).

A Tied Aid Consultations Group was formed to address those Helsinki-type tied aid issues relating to projects that, following required notification, may be challenged by other governments as being potentially commercially viable.

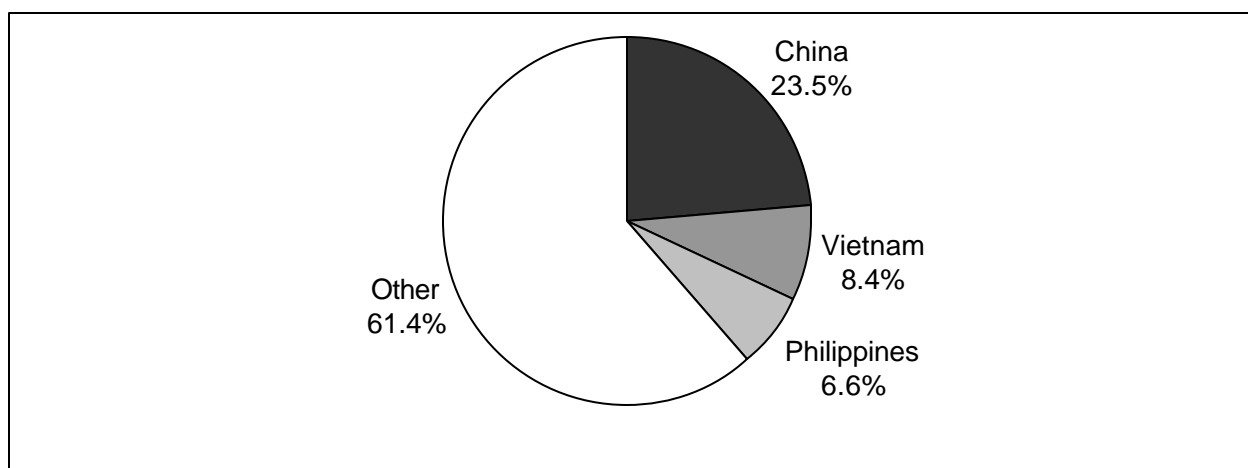
In December 1996, the OECD countries agreed to and publicly published *Ex Ante Guidance for Tied Aid*, a set of guidelines which assists export credit agencies, aid agencies, project planners and aid recipients in judging at the outset whether potential projects will be eligible for tied aid. These guidelines, designed to avoid the use of official aid to encourage exports that could proceed without aid, encapsulate the body of experience of the Consultations Group and have been a useful tool. In November 2002, the Ex Ante Guidance was updated to incorporate the results of Consultations since 1996, and energy pipelines were added to the list of normally commercially viable projects. From 1992 to 1995, an average of 27 cases were challenged each year, with on average half found commercially viable. From 1996 through 2002, a total of 20 cases have been challenged, with 16 of these deemed commercially viable. See Annex 3 for a list of projects generally considered commercially viable, 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.

Of the 129 projects examined by the Consultations Group from March 1992 to December 2002, 48 projects (37.5%) were found to be commercially non-viable, or eligible for tied aid financing under the Helsinki rules, and 69 projects (53.5%) were found to be commercially viable. Of the remaining 12 cases, no conclusion was reached on commercial viability on four cases. Others were committed before the inception of the Helsinki disciplines, three had been committed prior to notification (and thus considered derogations) and only one was a matching transaction.

In the post-Helsinki period, energy (43.3%), telecommunications (26.0%), manufacturing (15.7%) and transportation (12.6%) represented 97.6% of all the projects challenged and

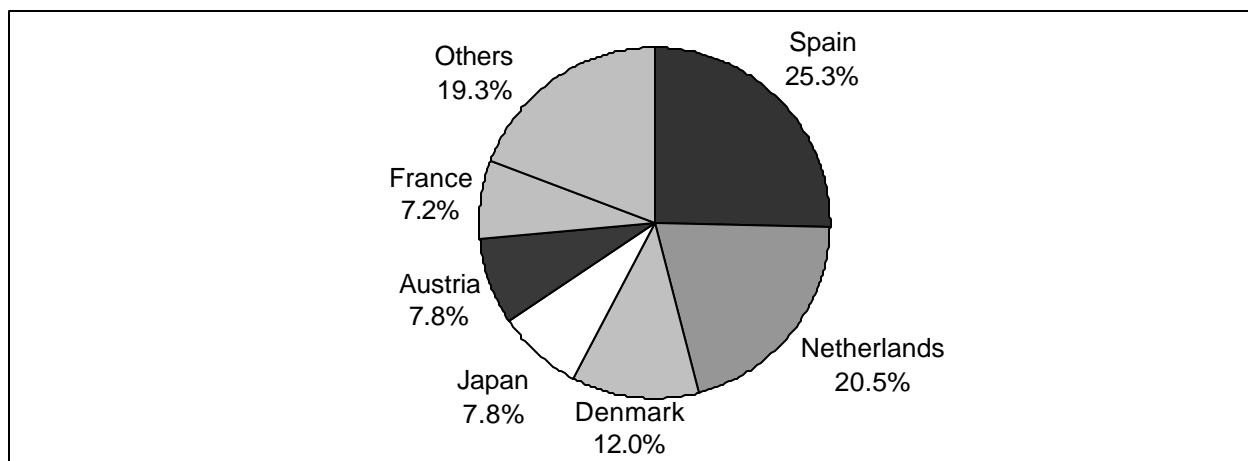
considered by the Consultations Group. Only two projects in the social services sector were challenged. Regarding recipient countries, China accounted for the largest number of notifications evaluated by the Consultations Group during the post-Helsinki period with 39 notifications (23.5%), followed by Vietnam with 14 notifications (8.4%) (see **Figure G1**).

Figure G1: Challenged Notifications by Recipient Country



During the post-Helsinki period, Spain initiated the highest number of notifications considered by the Consultations Group (42), followed by the Netherlands (34), Denmark (20) and Japan and Austria (13 each) (see **Figure G2**).

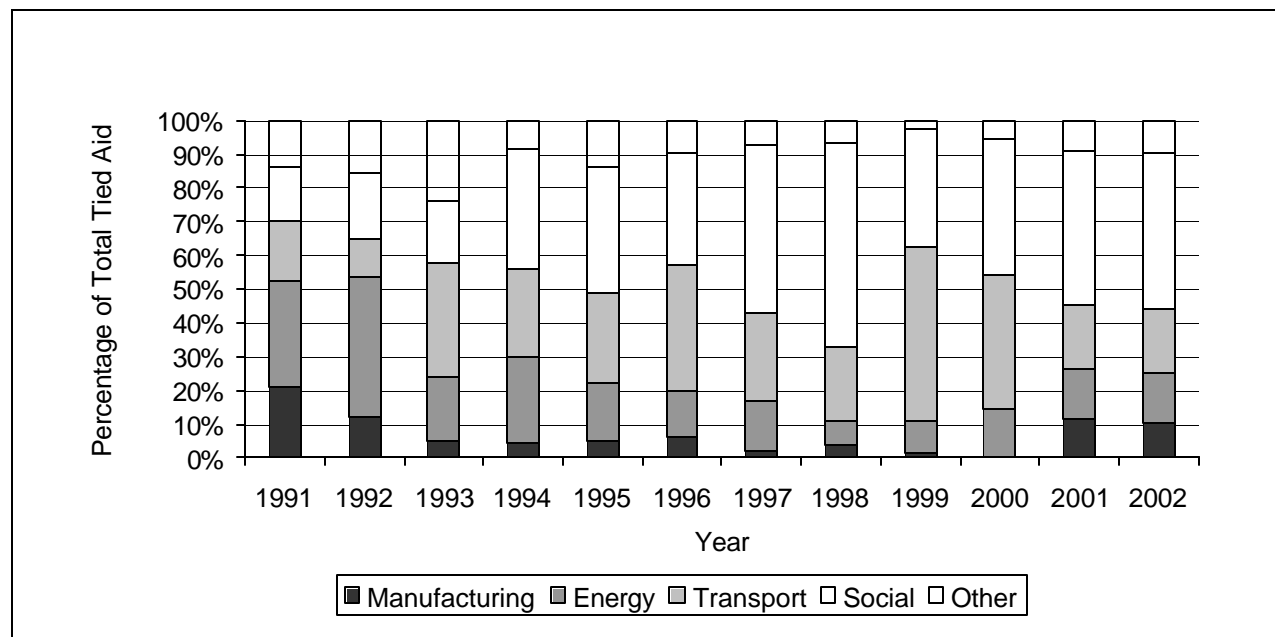
Figure G2: Challenged Notifications by Notifying Country



As can be seen in **Figure G3**, Helsinki has had a dramatic and continuing impact. Simply put, tied aid in the pre-Helsinki period was dominated by energy and manufacturing (at roughly 50% of activity); by 2002, the transport (e.g., subways) and social sectors accounted for nearly 64.8%

of activity. Thus, the types of projects notified and the decrease in the number of projects challenged suggest that the Helsinki disciplines have encouraged donors to redirect tied aid towards commercially non-viable projects.

Figure G3: Trends in Tied Aid by Sector



TRENDS IN THE USE OF THE TACF

Ex-Im Bank, in consultation with the Department of Treasury, has established guidelines to limit and direct the use of the TACF. These guidelines have two core components:

1. A series of steps (e.g., propose an OECD no-aid agreement; when appropriate, a consultations challenge; when appropriate, an Ex-Im Bank indication of a willingness to match a foreign tied aid offer) that attempt to get competitors to drop consideration of tied aid use and/or let tied aid offers expire.
2. A set of “multiplier” criteria (e.g., prospect of future sales without the continued use of tied aid) that attempt to limit tied aid support to those transactions with a benefit that would extend beyond the individual tied aid offer and generate the most benefit to the U.S. economy.

Although in the past Ex-Im Bank matching policy achieved some limited success in deterring foreign tied aid offers as part of the overall U.S. tied aid strategy, in recent years Ex-Im Bank has been faced with fewer opportunities to match tied aid. From 1994 through 2002, of the 25 cases in which Ex-Im Bank tried to discourage tied aid use by issuing “willingness-to-match” indications, seven saw the competing tied aid offer withdrawn; U.S. exporters won five out of these seven cases on standard Arrangement terms. Eight cases have been lost to foreign tied aid

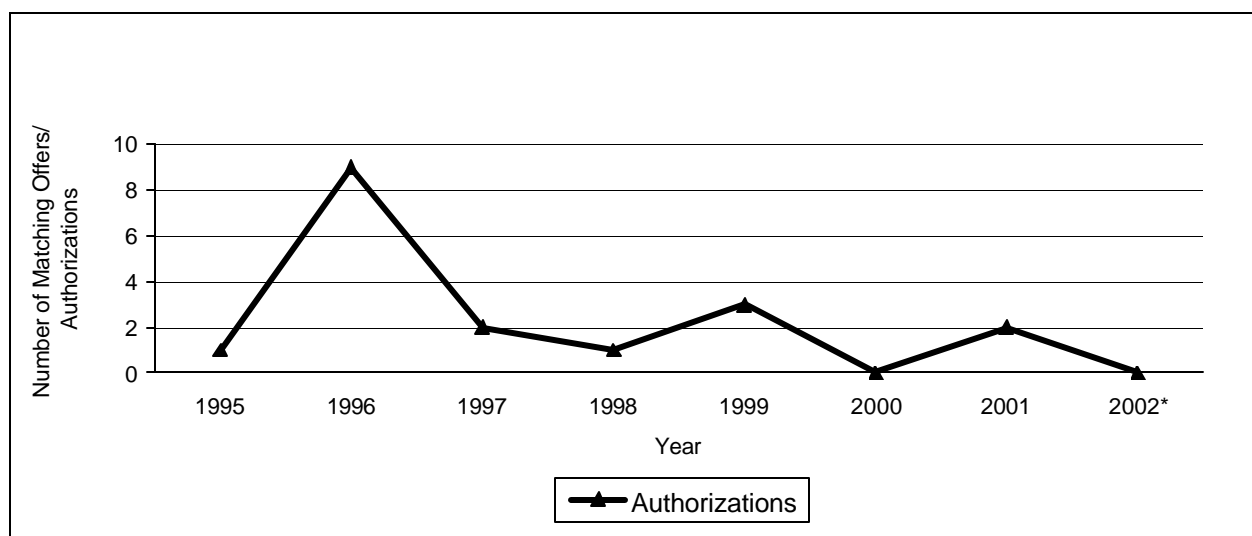
financing, while ten remain outstanding or have been indefinitely delayed. Notably, however, most matching success occurred in the years immediately following the Helsinki Package when the lines between commercial and aid financing were being drawn. By the end of 1996, 30 matching offers had been made.

As shown in **Figure G4**, of the 43 cases where Ex-Im Bank matched, the United States has won 19 while losing 23. The one remaining case was indefinitely delayed.

Figure G4: Cumulative Ex-Im Bank Matching of Previously Notified Foreign Tied Aid Offers

	1996	1997	1998	1999	2000	2001	2002
New matching offers during year	7	4	2	4	1	2	0
U.S. win	10	12	13	16	17	19	19
U.S. loss	7	10	10	21	23	23	23
Outstanding, no decision	13	12	13	3	1	1	1
Cumulative total	30	34	36	40	41	43	43

Figure G5: U.S. Tied Aid Authorizations by Year



As shown in **Figure G5**, in 2002 there were no new tied aid authorizations. However, there were increases to existing tied aid authorizations that utilized \$13.7 million (\$7.0 million to Indonesia and \$6.7 million to Morocco) of TACF. The U.S. pattern reflects the downward trend in tied aid authorizations generally.

EX-IM BANK INITIATED NO AID COMMON LINES

When Ex-Im Bank receives an application for financing in a tied aid eligible country for a project that is commercially non-viable, and the U.S. exporter has reason to be concerned about the possibility of tied aid financing competition, the U.S. government may propose a no aid common line in hopes of eliminating this possibility. If the common line request is accepted, other OECD member countries are prohibited from offering tied aid financing for the particular project for a period of two years (with the possibility of extensions). With such agreements in place, U.S. exporters can compete without fear of tied aid competition and without the need for Ex-Im Bank to provide a matching tied aid offer. If the no aid common line request is rejected, other OECD member countries may make a tied aid financing offer for the project. Since April 1994, there have been 26 cases where the OECD Secretariat, acting upon U.S. request, has obtained OECD-wide approval of “no aid” agreements for particular projects of interest to U.S. exporters. **Figure G6** shows the results of the no aid common line requests initiated by the U.S. government from 1996 through 2002.

Figure G6: U.S. Proposed No Aid Common Lines

	1996	1997	1998	1999	2000	2001	2002
Proposed	19	24	5	13	8	1	0
Rejected	13	17	5	12	5	0	0
Accepted	6	7	0	1	3	1	0

The no aid common lines have had limited utility for U.S. exporters in the past few years: generally, the United States has proposed these common lines, and foreign governments have rejected them out of hand, considering this additional restriction as limiting their flexibility and competence to provide aid within the Helsinki disciplines.

Appendix G: Annex 1

Key Markets Where Tied Aid is Prohibited	
Americas*	Argentina, Brazil, Mexico, Venezuela
Asia*	Hong Kong, Korea, Malaysia, Singapore, Taiwan
Middle East*	Bahrain, Israel, Kuwait, Lebanon, Oman, Qatar, Saudi Arabia, Turkey, United Arab Emirates
Africa*	Botswana, Gabon, South Africa
Eastern Europe	Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic and Slovenia
Transitional Economies**	Belarus, Bulgaria, Romania, the Russian Federation and Ukraine

*These markets are not eligible for tied aid as a result of the fact that their Gross National Income (GNI) per capita was sufficient to make them ineligible for 17-year loans from the World Bank for at least three consecutive years (using 2001 IBRD data, those countries with a GNI per capita above U.S.\$2,975).

**These markets are covered by the Participants' agreement to try to avoid tied aid credits other than outright grants, food aid and humanitarian aid. For the purposes of the soft ban, the decommissioning of nuclear power plants for emergency or safety reasons can be regarded as humanitarian aid.

Appendix G: Annex 2

Key Tied Aid Eligible Markets*	
Asia	China, India, Indonesia**, Philippines, Sri Lanka, Thailand, Vietnam**
Latin America	Colombia, Dominican Republic, El Salvador
Africa	Egypt, Morocco, Namibia, Tunisia

*Markets classified as both eligible for tied aid by the OECD and eligible for Ex-Im Bank tied aid support as “Dynamic Markets”.

**May need additional factors to enhance eligibility under Ex-Im Bank tied aid guidelines due to budget cost impact.

Appendix G: Annex 3

Projects Generally Considered Commercially Viable (Helsinki-Type Tied Aid Prohibited)	
Power	<ul style="list-style-type: none"> ▪ Oil-fired power plants ▪ Energy pipelines ▪ Gas-fired power plants ▪ Large stand-alone hydropower plants ▪ Retrofit pollution-control devices for power plants ▪ Substations in urban or high-density areas ▪ Transmission lines in urban or high-density areas
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"> ▪ Air traffic control ▪ 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 G: Annex 4

Projects Generally Considered Commercially Non-Viable (Helsinki-Type Tied Aid Permitted)	
Power	<ul style="list-style-type: none"> ▪ Transmission lines to low-density, rural areas ▪ Geothermal power plants ▪ Small wind turbine farms ▪ District heating systems ▪ 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 H: Human Rights and Other Foreign Policy Considerations

Pursuant to the 1978 amendments to the Export-Import Bank Act of 1945, Ex-Im Bank may deny financing based on international human rights or other foreign policy considerations only upon a determination by the President that such denial furthers U.S. policy goals (this legislation, P.L. 95-630, 92 Stat. 3724, is also referred to as the “Chafee Amendment”). The Chafee Amendment, as amended in 2002 by P.L. 107-189, states that the Board of Directors of Ex-Im Bank may not deny applications for non-financial or non-commercial reasons unless the President determines that such denial will clearly and importantly advance U.S. policy in such areas as international terrorism, nuclear proliferation, the enforcement of the Foreign Corrupt Practices Act of 1977, the Arms Export Control Act, the International Emergency Economic Powers Act, the Export Administration Act of 1979, environmental protection and human rights (including child labor).

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 has developed procedures with the State Department, including the Bureau for Democracy, Human Rights, and Labor, for regular consultation regarding human rights concerns. According to these procedures, Ex-Im Bank periodically receives a list of countries where the State Department has found no “consistent pattern of gross violations of internationally recognized human rights.” Where a proposed transaction over \$10 million dollars involves goods or services to be exported to a country that has not received “pre-clearance” on such list, 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 to, where appropriate, examine human rights and other foreign policy considerations in their assessment of the risks associated with transactions in specific countries.

Appendix I: 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 legislative requirement was imposed on Ex-Im Bank, 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 2002, Ex-Im Bank has not identified any long-term transaction in which U.S. insurance companies were not allowed equal access.

Appendix J: Trade Promotion Coordinating Committee (TPCC)

INTRODUCTION

The Trade Promotion Coordinating Committee (TPCC) is an interagency committee consisting of 19 U.S. government agencies,¹⁰ each of which has a stake in maximizing U.S. export potential. The Export Enhancement Act of 1992 established the TPCC to coordinate U.S. government export promotion initiatives under the leadership of the Secretary of Commerce. The President and Chairman of the Export-Import Bank serves as the Vice-Chair of the TPCC.

Among the responsibilities of the TPCC is to prepare and submit to Congress an annual report entitled the National Export Strategy (NES) that outlines the Administration's trade promotion agenda. In April 2003, the TPCC issued the most recent NES report to Congress which provides a status report on progress made toward implementing the recommendations presented in the 2002 NES report. TPCC accomplishments during 2002 that pertain to Ex-Im Bank are summarized below.

HIGHLIGHTS OF TPCC ACCOMPLISHMENTS DURING 2002

Highlights of the TPCC's major accomplishments during 2002 that directly impact Ex-Im Bank and its competitive position vis-à-vis foreign export credit agencies include:

- Ex-Im Bank, SBA, the U.S. Commerce Department's Census Bureau and International Trade Administration, and the U.S. Department of Agriculture established a joint marketing task force that now meets regularly to coordinate literature and pavilions at major domestic trade shows, trade financing seminars and direct mail campaigns.
- Enhancing U.S. export competitiveness by marketing Ex-Im Bank programs during the initial stages of project development: this initiative is referred to as early project development, in which teams have identified projects in key markets (Brazil, China, Mexico and Russia) and pioneered new ways to market the availability of Ex-Im Bank programs.
- Over the last year, agencies have developed a set of procedures for the U.S. government's first mixed credit pilot program, combining U.S. Agency for International Development grants and Ex-Im Bank financing. The program was

¹⁰ Members of the TPCC are the following U.S. government agencies: 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.

launched formally in April 2003 with instructions to U.S. foreign posts. Over the next year, the challenge will be to educate posts on how to use the program.

- The creation of an interagency training program: In January 2003, the TPCC conducted the first interagency trade specialist seminar to train field staff to view federal trade promotion as a team approach focused on customer account management. TPCC agencies were extremely receptive to this approach, with nine agencies represented by the participants. Achieving the desired culture shift requires that the TPCC agencies extend this training to all field staff and that agencies make a long-term commitment of resources.
- Ex-Im Bank is also working on an initiative with the SBA to collaborate by providing parallel financing and joint marketing for working capital transactions. This effort is designed to provide the small business exporter with a seamless approach to access working capital financing needed to increase export sales.

These initiatives seek to maximize U.S. exporter competitiveness by leveraging resources across agencies, educating U.S. exporters and foreign buyers alike on available trade finance options and creating opportunities for small, medium and large U.S. businesses to reap the benefits of international trade.

Appendix K: Efforts to Promote Renewable Energy Exports

In Ex-Im Bank's 2002 reauthorization process, Congress inserted in Ex-Im Bank's Charter the requirement to report on efforts to promote renewable energy exports.

In 2002, Ex-Im Bank actively engaged in the promotion of renewable energy exports. Most notably, Ex-Im Bank was the first export credit agency to convene a Renewable Energy Exports Advisory Committee. Comprised of renewable energy experts from industry, civil society and academia, the Committee's purpose was to advise Ex-Im Bank on how it can modify its programs, add new financing products and improve outreach to U.S. renewable energy exporters and foreign buyers. The Committee met three times throughout 2002.

In addition to the Renewable Energy Exports Advisory Committee, Ex-Im Bank staff joined the U.S. delegation to the U.N.'s World Summit on Sustainable Development in Johannesburg, South Africa in the summer of 2002. At the Summit, Bank staff participated in several panels and seminars at which renewable energy was addressed.

Finally, Ex-Im Bank held two conferences in September 2002 to promote environmentally beneficial exports, including renewable energy exports. The first took place on September 10 and 11 in Budapest, Hungary and brought together U.S. environmental exporters with Southeast European government and industry representatives. The second occurred on September 23 and 24 in Mexico City and focused on promoting renewable energy projects in the Mexican municipal sector.

