EXPORT CREDIT FINANCING SYSTEMS IN OECD MEMBER COUNTRIES AND NON-MEMBER ECONOMIES

Introduction

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INTRODUCTION

The contributors

The export financing systems of 34 economies are described in this book; 29 are OECD countries and are Members of the OECD Working Party on Export Credits and Credit Guarantees (ECG) (Iceland is currently not an ECG Member). Except for Hungary, Mexico, Poland and Turkey, these OECD countries also constitute the Participants to the Arrangement on Officially Supported Export Credits (the Arrangement); Hungary and Poland are Observers to the Group of Participants. The five non-member economies (Chinese Taipei; Hong Kong, China; Romania; Singapore; Slovenia) whose export financing systems are described in this book, are neither Members nor Observers to the ECG or to the Group of Participants. They have, however, undertaken to endeavour to comply with the guidelines of the Arrangement.

Institutional differences

All 34 economies (although Ireland has now withdrawn its system of state support for export credits) included in this book have put in place systems to assume at least the political risk (risk of non-payment because of government-imposed restrictions) of providing export credits to foreign buyers, and many will also cover the transfer risk (risk of non-availability of foreign exchange to meet repayment obligations), although cover may be restricted in markets with poor payment experience. Most of the export credit agencies (ECAs) providing such cover also assume the commercial risks (risk of non-payment because of the bankruptcy or default of the buyer) and some reinsure such risks taken by private institutions. In addition to insurance facilities, most of the economies are involved with at least one of the three forms of official financing support described above.

As can be seen from the contents of the following chapters, a variety of solutions have evolved with regard to government involvement in export credits. The organisational form of the ECA ranges from a section of a ministry, or a government agency, through to an independent government agency or a semi-public joint stock company, to a private institution operating partly under an agreement with the government. These solutions are reflected in the way these institutions are funded: for example, from the national budget, from special government funds, from loans and capital from the government or from shares and bonds.

Export credits

Broadly defined, an export credit is an insurance, guarantee or financing arrangement which enables a foreign buyer of exported goods and/or services to defer payment over a period of time. Export credits are generally divided into short-term (usually under two years), medium-term (usually two to five years) and long-term (usually over five years).

Export credits may take the form of "supplier credits", extended by the exporter, or of "buyer credits", where the exporter's bank or other financial institution lends to the buyer (or his bank). Official support, through ECAs, may be provided as "pure cover", *i.e.* insurance or guarantees given to exporters or lending institutions without financing support; as financing support, *i.e.* direct credits/financing, refinancing, interest rate support; and/or as aid financing (credits and grants). Official financing support may be provided in conjunction with the basic guarantee or insurance facility, or it may be provided on a stand-alone basis.

The Arrangement on Officially Supported Export Credits

Participation

The Participants to the Arrangement on Officially Supported Export Credits are: Australia, Canada, the Czech Republic, the European Community (which includes the following countries: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden, the United Kingdom), Japan, Korea, New Zealand, Norway, Switzerland and the United States; Hungary and Poland are Observers to the Participants.

The Arrangement, developed under the auspices of the OECD, came into being in April 1978 following agreement among its Participants. It replaced a less elaborate understanding that had been in effect among a more limited number of OECD countries since early 1976.

The Arrangement is a "Gentlemen's Agreement" among the Participants; it is not an OECD Act, although it receives the administrative support of the OECD Secretariat. The full text of the latest Arrangement (2005) constitutes Annex I of this book. The Arrangement is adopted into European Community Law.

Purpose and application

The main purpose of the Arrangement is to provide the institutional framework for the orderly use of officially supported export credits. The Arrangement seeks to encourage competition among exporters on the basis of quality and price of the goods and services exported rather than on the basis of the most favourable officially supported terms.

The Arrangement applies to officially supported export credits with repayment terms of two years or more, relating to exports of goods and/or services or to financial leases, *i.e.* a lease equivalent in effect to a contract of sale. The Arrangement also addresses the circumstances in which official support in the form of trade-related tied and partially untied aid – referred to as "tied aid" – may be given and/or mixed with officially supported export credits.

Military equipment and agricultural commodities are excluded from the application of the Arrangement. However, an export credit understanding in respect of agricultural products is currently being negotiated.

Special sector understandings

Four Sector Understandings (for Ships, Nuclear Power Plant, Civil Aircraft and Renewable Energies and Water Projects) are annexed to the Arrangement. These set out the special terms which may be officially supported for the sectors concerned.

Provisions of the Arrangement

The Arrangement places limitations on the terms and conditions of export credits that benefit from official support. Such limitations include minimum premium benchmarks, the minimum cash payments to be made at or before the starting point of credit, maximum repayment terms and minimum interest rates which benefit from official financing support. There are also restrictions on the provision of tied aid. Finally, the Arrangement includes procedures for derogations from and permitted exceptions to its disciplines, as well as procedures for prompt and prior notification, exchanges of information and review. These disciplines include the following:

- At least 15% of the contract is to be covered by cash payments.
- The maximum repayment term is five years (or eight-and-a-half with prior notification). This may be extended to ten years for poorer developing countries.
- Minimum interest rates apply to official financing support. The minimum interest rates are the Commercial Interest Reference Rates (CIRRs). The CIRRs are adjusted on a monthly basis, and reflect final commercial lending rates for first-class borrowers in the domestic market of the currency concerned. The condition on interest rate minima applies only to credits benefiting from official financing support.

Helsinki Package, 1991

In addition to export credit activity, at the end of 1991, the Participants to the Arrangement agreed a package of reforms to the Arrangement including new rules on tied and partially untied aid. This set of reforms, known as the "Helsinki Package", included disciplines aimed at redirecting such tied aid away from better-off developing countries (*i.e.* those whose per capita GNP makes them ineligible for 17-year loans from the World Bank), which are generally creditworthy and thus able to attract commercial credits and towards developing countries which have more difficulty in accessing market funds. In addition, the new disciplines prohibit tied aid for commercially viable projects in all but the LLDCs.

The Participants agreed two key tests for evaluating whether projects are commercially non-viable and therefore eligible for aid financing:

- Whether the project is financially non-viable, *i.e.* whether the project lacks the capacity, with appropriate pricing determined on market principles, to generate cash flow sufficient to cover the project's operating costs and to service the capital employed.
- Whether it is reasonable to conclude, based on communication with other Participants, that it is unlikely that the project can be financed on market or Arrangement terms.

The Arrangement also stipulates that tied aid shall not be provided if the concessionality level is less than 35% (or 50% if the recipient is an LLDC).

Schaerer Package, 1994

In August 1994, the Participants agreed to a set of reforms to the Arrangement, known as the "Schaerer Package", the key features of which included:

– Abolition over time of the last of the subsidised interest rates (the SDR-based rates) so that, henceforth, market-based CIRRs would be applied as the minimum interest rates for all markets.

– Introduction of an automatic classification of countries to determine the maximum repayment period. The new classifications depend on per capita GNP as recorded by the World Bank.

– Adjustment to the discount rate for calculating the concessionality level (a concept similar to the grant element) of aid loans, which better reflect market realities.

– Approval of a new work programme, including premium fees and related conditions, export credit disciplines for agricultural products, the further untying of aid and further consideration of the issue of market windows.

Ex Ante Guidance on Tied Aid, 1996

In November 1996, the Participants reached agreement to "*Ex Ante* Guidance for Tied Aid". This was the result of over four years of implementing the tied aid disciplines of the 1991 Helsinki Package. It was derived from the evaluation of over 100 individual project notifications for tied aid which had been discussed at monthly meetings of the Participants held since February 1992.

The purpose of the *Ex Ante* Guidance [publicly available as OCDE/GD(96)180], is to help project planners anticipate, at an early stage, whether or not a project is likely to pass the two key tests (outlined above) on commercial viability, which determine whether a project is eligible for tied aid financing. The *Ex Ante* Guidance seeks to identify the key technical and economic characteristics of previously evaluated projects which had impacted significantly on the Participants' decisions as to whether a project was considered eligible or ineligible for tied aid financing. The *Ex Ante* Guidance provides useful information on the probability of the commercial viability, or otherwise, of a project. It is not intended to pre-judge or pre-empt the evaluation of individual projects; rather, the Participants recognise that all projects must be considered on a case-by-case basis in relation to their particular circumstances.

Knaepen Package, 1997

In June 1997, the Participants reached agreement on the Knaepen Package on Guiding Principles for the Setting of Premia and Related Conditions. These Guiding Principles set minimum premium rates for sovereign and country credit risks, irrespective of whether the buyer/borrower is a private or public entity, which:

- Are risk-based/risk-reflective.
- Eliminate distortion of competition and thus create a level playing field, taking into account different qualities of cover.
- Are not inadequate to cover long-term operating costs and losses.
- Are transparent among the Participants to the Arrangement on Officially Supported Export Credits.

The key elements of the Knaepen Package include:

- An econometric model to assess country risk.
- Minimum premium benchmarks assigned to seven country risk categories.
- Some differences in the minimum rates to be applied according to the quality and percentage of cover being provided (*i.e.* premium rates will reflect different related conditions in order to provide a level playing field from the viewpoint of the exporter).
- Review procedures to ensure that, over time, the rates remain commensurate to risk and do not become inadequate to cover long-term operating costs and losses.
- A comprehensive electronic exchange of information in order to maintain maximum transparency among the Participants.
- A system of permitted exceptions for premium discounts for risk externalisation/mitigation.

The Knaepen Package, which took effect on 1 April 1999, applies to all officially supported export credits whether provided by direct financing, refinancing, insurance or guarantees (except that transactions of large aircraft and those ships subject to the Sector Understanding on Export Credits for Ships are not subject to the Guiding Principles).

Project Finance Understanding, 2005

Following agreement among the Participants in 2005, the Understanding on the Application of Flexibility to the Terms and Conditions of the Arrangement on Officially Supported Export Credits in Respect of Project Finance Transactions was incorporated in the Arrangement as Annex X, without time limit.

Common Approaches on Environment

The Members of the ECG have, over the past few years, initiated discussion and action in respect of the environmental impact of business benefiting from officially supported export credits. OECD Ministers mandated the ECG in 1999, and renewed in 2000, to strengthen common approaches to the environment. The following four public statements have been issued by the ECG on the environment; the full texts are in Annex III:

- 2000 Work Plan
- 2000 Action Statement
- 1999 Agreement on Environmental Information Exchange for Larger Projects
- 1998 Statement of Intent

The ECG Members negotiated Common Approaches to the environment and export credits with the aim of concluding an agreement by the end of 2001 in the form of a Draft OECD Recommendation. ECG Members decided to apply, voluntarily and unilaterally, the Common Approaches as from January 2003. Subsequently, the OECD Council adopted revised Common Approaches in the form of an OECD Recommendation on 18 December 2003 for implementation from the beginning of 2004; Annex V is the text of the OECD Recommendation; it was updated in 2004.

Action on Bribery, 2000

In 2000, the ECG issued an Action Statement on Bribery and Officially Supported Export Credits. The Statement highlights the importance placed by OECD governments on ensuring that they do not support export deals where bribery is involved in the award of contract, and signals their commitment to take concrete, co-ordinated measures in support of this objective, bearing in mind that countries operate under different judicial instruments and institutions. The Action Statement is under review with the intention of enhancing it.

In parallel with the development of the 1997 OECD Convention on Combating Bribery of Foreign Public Official in International Business Transactions, and since the Convention came into force in February 1999, the ECG has examined national export credit systems to establish how the Convention should be taken into account when providing officially supported export credits. The result of this examination has been an agreement to take appropriate measures. The Action Statement is given in full at Annex IV.

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* Annex II in earlier publications, *i.e.* Terms and Conditions Applicable to Project Finance Transactions, is now incorporated in Annex I; accordingly all annexes herein have been renumbered.

ABBREVIATIONS

Arrangement	Arrangement on Officially Supported Export Credits
CIRR	Commercial Interest Reference Rate
DAC	Development Assistance Committee
EC	European Communities
ECA	Export Credit Agency
HIPC	Highly indebted poor country
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IFC	International Finance Corporation
L/C	Letter of Credit
LDC	Less Developed Countries
LIBOR	London Interbank Offered Rate
LLDC	Least Less Developed Countries
ODA	Official Development Aid
SDR	Special Drawing Rights

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