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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

Financial And Other Constraints Prevent Eximbank From Consistently Offering Competitive Financing For U.S. Exports

When financing from the Export-Import Bank of the United States (Eximbank) is not as attractive or available as government-supported export financing offered by other countries, U.S. exporters are at a competitive disadvantage and lose some sales. Eximbank has taken actions to make its financing more competitive, but constraints limit its ability to consistently offer competitive financing.

In view of continuing U.S. trade deficits, the Congress may wish to consider measures to enable Eximbank to more consistently offer competitive interest rates. The Congress should determine whether eligibility restrictions on the Bank's financing should continue to take precedence over the potential loss of U.S. exports.

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To the President of the Senate and the
Speaker of the House of Representatives

This report discusses Eximbank's role in financing U.S. exports, the international competition it faces, and its ability to meet that competition. The report further discusses a number of alternatives the Congress may wish to consider to help strengthen Eximbank's ability to meet foreign competition.

We are sending copies of this report to the Director, Office of Management and Budget; the Secretary of the Treasury; and the President and Chairman of the Export-Import Bank of the United States.

Milton J. Socolar

Acting Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

FINANCIAL AND OTHER CONSTRAINTS PREVENT EXIMBANK FROM CONSISTENTLY OFFERING COMPETITIVE FINANCING FOR U.S. EXPORTS

D I G E S T

The Export-Import Bank of the United States (Eximbank) helps finance the sale of U.S. exports. In some cases, however, Eximbank loans are more expensive than government-supported financing offered by other countries competing for a sale. Also, because of a variety of eligibility restrictions, Eximbank does not finance some exports that other countries finance. In some cases, these factors put U.S. exporters at a competitive disadvantage and has led to some lost sales. Eximbank has taken actions to make its financing more competitive, but there are constraints which limit its ability to consistently offer such financing. (See p. 6.)

EXPORTS LOST BECAUSE OF NONCOMPETITIVE FINANCING

Legislation requires Eximbank to provide export financing at interest rates competitive with other countries' government-supported rates. However, financing supported by Eximbank normally includes both Government and commercial loans, and the blended interest rate depends on commercial interest rates as well as Eximbank's lending rates.

The normal blended rates on long-term loans supported by Eximbank are about 2 to 3 percentage points higher than the normal rates charged by other countries on government-supported export financing (i.e., 10.7 vs. 8.6 to 8.0 percent). On an average loan this can mean as much as $5 million in added interest expense to the borrower. Also, interest rates on Eximbank medium-term financing are as much as 2.4 percentage points higher than other countries' rates. (See p. 7.)

In theory, competitiveness of interest rates should be influenced by borrowers' expectations of future currency exchange rate fluctuations. However, in practice, many U.S. exporters and bankers believe foreign buyers favor the loan with the lowest nominal rate because of the difficulty of predicting long-term currency exchange rates. (See p. 9.)

Eximbank's foreign counterparts set their normal interest rates at the minimums established by voluntary international guidelines. They sometimes offer even lower rates by mixing foreign assistance funds with export loans (mixed credits). Eximbank tries to compete by selectively lowering its lending rates and by financing portions of a sale normally financed by commercial banks. (See p. 8.)

A recent Eximbank analysis showed that 7 of 55 sales lost to foreign competitors (about 13%) were lost primarily because of uncompetitive financing. Responses to a GAO questionnaire show that U.S. firms lost some exports when other countries offered better financing than Eximbank. Questionnaire responses also show that U.S. firms lost sales when they did not apply for Eximbank financing because the expected financing terms were known to be unsuitable. (See p. 10.)

WHY EXIMBANK INTEREST RATES ARE HIGH

Eximbank operates as a self-sustaining institution. Its borrowing costs depend on the market rates for Government securities. In setting its lending rates, Eximbank attempts to cover its borrowing costs, other expenses, and potential loan defaults. Eximbank's foreign counterparts either pay less for their funds or obtain government subsidies. (See p. 11.)

Budget ceilings increasingly prevent Eximbank from using direct loans to more fully support long-term financing, provide medium-term financing, or finance sales under

$5 million. Commercial loans, at record high interest rates, must be used to finance sales or portions of sales not financed by Eximbank. Eximbank's foreign counterparts are not similarly constrained by budget limits. In addition, the degree of government commitment to providing official export credit support is greater for Eximbank's competitors. This is shown by the percentage of total exports officially supported by export credit programs.

Unlike some of its foreign counterparts, Eximbank does not have access to foreign assistance funds for matching other countries' mixed credits. (See p. 14.)

MATTERS FOR CONSIDERATION BY THE CONGRESS

GAO believes the Congress should reexamine the framework and financial constraints within which Eximbank now operates. If foreign governments continue or intensify their use of concessionary financing and/or U.S. commercial interest rates and Eximbank's own borrowing costs continue at current high levels, Eximbank will need increased flexibility and resources if it is to consistently offer competitive financing. There are a number of alternatives that may be considered.

Higher direct loan ceilings would enable exporters to increasingly use Eximbank loans, rather than high-cost commercial loans, for exports facing competition with foreign government-supported financing. However, greater use of Eximbank loans would increase the Federal budget and decrease commercial participation.

An alternative or supplement to increased direct loan authority would be to lower Eximbank's lending rates. However, its lending rates are already below its borrowing costs and, in the long term, this jeopardizes

Eximbank's traditional self-sustaining structure. If Eximbank were to continue or to increase the subsidization of its lending rate with its accumulated reserves, appropriations could be needed in the future if reserves were inadequate to pay loan defaults and claims for which Eximbank is liable. Alternately, the Congress may wish to consider providing Eximbank with annual appropriations to subsidize the difference between Eximbank's normal lending rates and rates offered by other governments competing for a sale. (See p. 14.)

EXPORTS LOST BECAUSE FOREIGN AND DOMESTIC CONSIDERATIONS RESTRICT ELIGIBILITY FOR EXIMBANK LOANS

While other countries base eligibility for export financing primarily on the credit-worthiness of the borrower, eligibility for Eximbank financing also depends on such factors as U.S. foreign policy, the foreign components of an export project, and the domestic impact of an export. (See p. 19.)

Although GAO did not review the impact of all factors affecting eligibility for Eximbank financing, responses to a GAO questionnaire show that some factors are a significant deterrent to U.S. exports. Some respondents said they lost sales because they could not arrange suitable financing for exports ineligible for Eximbank financing. Also, since many of these factors are reviewed on a case-by-case basis, exporters cannot confidently predict the availability of Eximbank support. (See p. 22.)

MATTERS FOR CONSIDERATION BY THE CONGRESS

In view of continuing U.S. merchandise trade deficits and the importance of competitive financing, GAO recommends that the Congress determine whether eligibility restrictions for Eximbank financing should continue to take precedence over lost U.S. exports.

GAO also recommends that the Congress consider clarifying the Export-Import Bank Act to provide Eximbank with sufficient direct loan authority to allow it greater flexibility in financing foreign components of export projects. (See p. 24.)

AGENCY COMMENTS

Treasury agreed with the report's thrust that more Eximbank financing is necessary, but felt the report's supporting arguments were often misleading. Treasury's comments were helpful and GAO strengthened its arguments accordingly. The Office of Management and Budget felt that the program levels sought for Eximbank were sufficient to enable Eximbank to meet critical foreign competitive financing cases. Eximbank agrees that financing is an important aspect of U.S. export competitiveness and that U.S. exports must receive adequate support in both the long and medium term, if the United States is to maximize its export opportunities.

Eximbank stressed that in those cases where it provides most of the financing, its rates have been competitive. GAO recognizes that this is true, but points out that the extent to which Eximbank can offer such financing is limited due to direct loan ceilings and the need to operate on a self-sustaining basis.

Eximbank also stated that it did not believe it needed more resources than the administration was presently in the process of requesting from Congress. Eximbank was confident that the administration's request for some $6 billion per year in direct credit resources (or its equivalent) in fiscal years 1980 and 1981 was sufficient to enable it to continue providing an adequate supply of competitive long-term financing. (See app. III.)

The administration is seeking approval for an "off-budget" approach to provide a $1-billion increase in Eximbank's fiscal year 1980 resources. GAO believes the proposed off-budget approach is contrary to the principle of full disclosure to and review by the Congress of the budgetary requests submitted by the executive branch. If the administration believes Eximbank needs additional resources to consistently offer competitive financing, GAO's opinion is that this increase should be sought through the direct budget process. (See p. 17.)

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ABBREVIATIONS

AID	Agency for International Development
FFB	Federal Financing Bank
GAO	General Accounting Office
NAC	National Advisory Council on International Monetary and Financial Policies
OMB	Office of Management and Budget

CHAPTER 1

INTRODUCTION

U.S. exports have not kept pace with increases in the volume and cost of U.S. imports, resulting in a record $28.5-billion merchandise trade deficit in 1978 and a $24.6-billion deficit in 1979. The U.S. share of the world export market declined during the 1960s. During the same period, Japan, Germany, and France increased their composite share. Although in recent years the U.S. share of world trade has stabilized, increases in the volume and cost of imports, particularly oil, have resulted in continuing trade deficits. Both the administration and the Congress place high priorities on expanding exports to reduce the trade deficit, help control inflation and unemployment, and maintain world economic stability.

Financing is an increasingly important factor in exporting, particularly for sales to developing countries not able to finance expensive capital projects internally. U.S. exporters face strong foreign competition, particularly as other exporting countries develop advanced technology and manufacture competitive products. When competing exporters offer similar prices and products, financing terms often determine who makes the sale.

LIMITATIONS IN COMMERCIAL FINANCING

Commercial banks provide most of the financing required for U.S. exports, but there are limitations, particularly when borrowers require fixed interest rates and long repayment periods. Commercial banks are reluctant to lend at fixed interest rates due to fluctuations in their costs of funds and their dependence on short-term deposits. Private lenders are also reluctant to assume all the political and commercial risks associated with financing exports, such as loan default because of expropriation by a foreign government or insolvency of a foreign buyer. To assure availability of financing for exports, the United States supplements commercial financing with Government-supported programs.

ROLE AND ACTIVITIES OF U.S. EXPORT-IMPORT BANK

Eximbank is an independent Federal agency which helps to finance the sale of U.S. exports. The Export-Import Bank Act of 1945, as amended, directs Eximbank to set interest rates on its loans after considering both the cost of its funds and the rates offered by other governments; to supplement and encourage, but not compete with, private capital; and to semiannually report to the Congress on the competitiveness of its export financing programs.

Financing offered by Eximbank includes:

--Direct loans to foreign buyers for long-term financing (over 5 years); these loans are usually combined with commercial loans.

--Discount loans, which are agreements to purchase medium-term loans (6 months to 5 years) provided by private lenders at fixed interest rates.

--Loans to foreign banks, through its Cooperative Financing Facility, to cover 50 percent of their medium-term loans used to finance the purchase of U.S. exports. 1/

--Guarantees, which ensure repayment to private lenders that finance exports.

--Insurance, which protects exporters against political and commercial risks on short and medium-term loans made to foreign buyers. 2/

Eximbank has traditionally operated as a self-sustaining institution; it does not receive direct appropriations. The money it lends comes from borrowings from the Federal Financing Bank (FFB)3/ and revenues from repayments. Eximbank also has about $2 billion in accumulated income and $1 billion in capital stock issued to the Department of the Treasury. Eximbank revenues consist of interest and fees charged to users of its programs, from which it pays its own expenses, including interest on borrowings from the FFB. Since 1934, Eximbank has paid over $1 billion in dividends to the Treasury for use of its capital, including $35 million for fiscal year 1978.

1/ This program is being phased out by Eximbank.

2/ The insurance is provided through the Foreign Credit Insurance Association, a group of about 50 insurance companies.

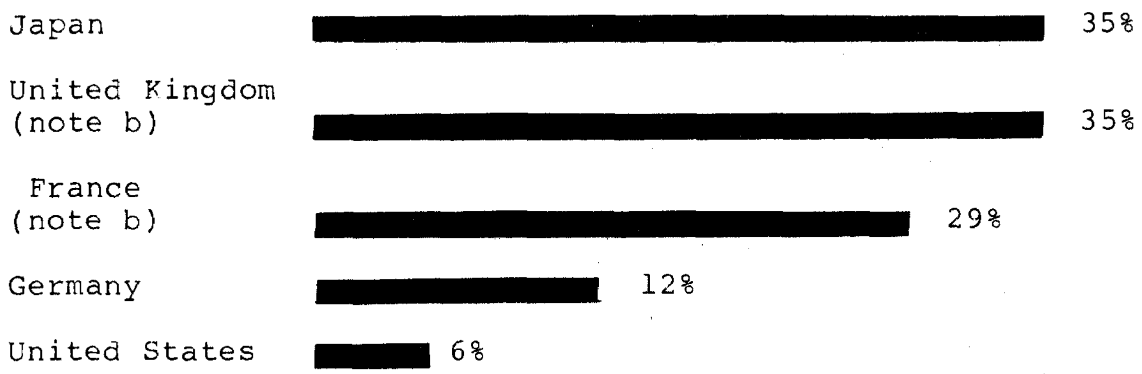
3/ The FFB lends to Federal agencies and federally guaranteed borrowers. Borrowing is centralized in the FFB to minimize the impact of Federal borrowings in private financial markets.

In annual appropriations legislation, the Congress sets limits on the amount of new loans, guarantees, and insurance that Eximbank can authorize. The Export-Import Bank Act limits the total amount of loans, guarantees, and insurance that may be outstanding at any one time. At September 30, 1978, Eximbank had committed approximately $19.3 billion of its $25 billion overall limit, and in November 1978 Congress increased the limit to $40 billion. During fiscal year 1979, Eximbank supported $13.6 billion in exports through $4.5 billion in loans, $951 million in guarantees, and $4.2 billion in insurance.

INTERNATIONAL COMPETITION IN EXPORT FINANCING

Other industrialized nations also have government programs to help finance their exports. Since financing is increasingly important in determining who makes a sale, there is intense competition in financing terms. Unlike Eximbank, some of its foreign counterparts receive operating subsidies from their governments. Also, some mix low-cost foreign assistance funds with export credits (mixed credits), provide insurance against cost escalation and currency fluctuations, and offer other "sweeteners" to make their financing more attractive. The following graph compares governments' financing support (including insurance, guarantees, and loans) of their exports during 1978. It shows that the degree of government commitment to providing official export credit support is greater in other countries than in the United States.

Percent of Total Exports Officially Supported By Insurance, Guarantees and Loans During 1978 (note a)



a/ All countries except the United States require an exporter to obtain commercial and political risk insurance as a condition for obtaining a government-supported loan. The chart excludes exports financed with foreign assistance funds. The U.S. estimate also excludes exports financed by the Commodity Credit Corporation and the Foreign Military Credit Sales program. Estimates for other countries may include small amounts of military and agricultural exports supported by their export credit agencies.

b/ Estimate based on June 30, 1978, data.

In April 1978, to avoid the costs of an international export credit "war," the United States and 21 other nations established voluntary guidelines for government-supported export financing. These guidelines, called the International Arrangement on Guidelines for Officially Supported Export Credits, include minimum interest rates, minimum cash payments, and maximum repayment periods. Participating countries may deviate from these guidelines on a case-by-case basis after notifying other participants. (See app. I for additional information on the Arrangement).

The United States believes the Arrangement can be improved by increasing the minimum interest rates and further restricting the use of mixed credits and certain other practices. However, repeated attempts to negotiate these changes have not been successful. The President concluded in March 1979 that the only feasible course of action was to ensure that U.S. export financing programs and policies remain competitive. (See app. II for a copy of the President's March 1979 statement.) Eximbank's recent semiannual reports to the Congress, however, concluded that in various ways its programs were not competitive with those offered by other countries.

In view of continuing U.S. merchandise trade deficits, the increasing importance of export financing, and the stalemate in negotiations to reduce international competition, we reviewed Eximbank's direct loan program to determine if competitive financing was being offered. We did not review Eximbank's guarantee or insurance programs, because the competitiveness of these programs depends primarily on commercial interest rates rather than on the fees or coverage for Government guarantees and insurance. Our review included a questionnaire survey of all 117 exporters that in 1978 were either denied financing by Eximbank or did not use the financing offered.

CHAPTER 2

EXPORTS LOST BECAUSE OF NONCOMPETITIVE FINANCING

The Export-Import Bank Act of 1945, as amended, requires Eximbank to provide loans at interest rates competitive with the government-supported rates offered by other countries. Eximbank's foreign counterparts have set their interest rates at the minimums established by the International Arrangement on Guidelines for Officially Supported Export Credits, and they sometimes offer even lower rates by mixing foreign assistance funds with regular export loans. However, Eximbank has not consistently matched either the normal or mixed credit rates of its competitors because it (1) operates on a self-sustaining basis, (2) has annual budget ceilings which prevent it from more fully supporting exports with direct loans, and (3) does not have access to foreign assistance funds to compete with other countries' mixed credits. Although we could not determine the total impact of Eximbank's higher interest rates, a recent Eximbank analysis and responses to our questionnaire showed that U.S. firms have lost export sales because of non-competitive financing.

COMPARISON OF INTEREST RATES ON GOVERNMENT-FINANCED LOANS

Eximbank and its foreign counterparts use a variety of approaches to finance exports. Some programs combine low-interest government loans with commercial loans; others either refinance commercial loans or directly subsidize commercial interest rates. Although the approaches differ, the effective interest rate to the borrower is the critical factor and serves as the basis for our comparison.

Rates normally charged

Compared below are the effective interest rates as of December 1979 charged by the United States and its major foreign competitors for a typical government-supported, long-term loan to finance an export to a less developed country.

	United States	Germany	France	United Kingdom (note a)	Japan
	-----------	-----------	percent	-----------	-----------
Base interest rate	10.5	7.5	7.5	7.5	7.5
Plus:					
Fees	.2	.2	.2	.2	.2
Insurance premiums	(b)	.7	.9	.6	.3
Effective interest rate to the borrower	10.7	8.4	8.6	8.3	8.0

a/ Loans denominated in U.S. dollars.

b/ The United States does not require an exporter to obtain commercial and political risk insurance as a condition for obtaining a Government-supported loan.

The base interest rates represent blended government and commercial rates when both types of loans are combined to finance an export. Insurance premiums are included when required as a condition for government support, but they are often included in the price of an export and are not discernible to the foreign borrower as a financing cost.

As shown, all countries except the United States offer a 7.5-percent base interest rate, which is the minimum allowed by the Arrangement. The U.S. rate, based on Eximbank activity for the first quarter of fiscal year 1980, consists of Eximbank financing for approximately half the export value at 8.15 percent, the average rate charged, and commercial bank financing for the remainder at 1.25 percent above their prime lending rate, or 14.6 percent as of December 1979. Combining the two loans results in the blended interest rate of 10.5 percent, which is 3 percentage points higher than the other countries' base rates.

Medium-term loans supported by Eximbank also cost more than financing available to exporters in other countries. As of June 1978, France, Japan, and the United Kingdom offered medium-term, government-supported loans at effective interest rates of 7.85 to 8.10 percent. German commercial banks were able to offer medium-term loans at 8.8 percent with government guarantees. Eximbank does not offer direct medium-term loans, but it supports some commercial bank loans, either through its discount loan program or its Cooperative Financing Facility. The effective interest rates on these programs were 10.2 and 9.05 percent, respectively, as much as 2.4 percentage points higher than the other countries' rates.

Lower rates offered on case-by-case basis

France, the United Kingdom, and Japan selectively finance export projects of particular national importance with a mixture of normal export loans and lower cost foreign assistance funds. France is the most frequent user of mixed credits; in 1978 it combined $295 million in foreign aid funds with 18 export loans to finance $1 billion in exports. The French mixed-credit loans included up to 50 percent foreign aid at 3 to 3.5 percent interest repayable over 20 to 30 years. The United Kingdom designated 5 percent ($72 million) of its 1978 foreign aid budget for mixing with normal export loans. British mixed credits included about 30 percent foreign aid repayable over 25 years at 2 to 4 percent interest. Japan denied that it mixes aid funds with official export financing, but the Japanese have offered what amounts to mixed credits by financing a single export project with both types of loans.

Eximbank has increasingly modified its normal lending policies to try to compete with the normal and mixed-credit interest rates on long-term financing offered by its foreign counterparts. It does this by reducing the interest rates on its portion of a loan and by financing portions of the loan normally financed by commercial banks. During fiscal year 1979, Eximbank made 19 of its 98 direct loans at interest rates averaging 0.67 percentage points below its normal scale to compete with other countries' normal rates. Scale rates ranged from 8.75 to 7.75 percent; while actual rates ranged from 8.75 to 6.00 percent. In 15 of these 19 loans, Eximbank financed the exports without commercial bank participation. On an even more limited basis, Eximbank tries to compete with mixed credits. In one case a U.S. firm was able to win a sale when Eximbank matched a French mixed credit by financing 100 percent of the loan at 6 percent interest.

IMPACT OF HIGH INTEREST RATES FOR U.S. EXPORT FINANCING

Foreign buyers can save millions of dollars in financing costs if they purchase foreign exports rather than those of U.S. firms. For example, as shown below, based on the interest rates on page 7, on a 9-year, $34-million loan, 1/ a buyer could save as much as $5 million.

Country	Effective interest rate (percent)	Interest expense	Savings compared with U.S. financing
United States	10.7	$19,795,000	--
Germany	8.4	15,133,000	$4,662,000
France	8.6	15,530,000	4,265,000
United Kingdom	8.3	14,935,000	4,860,000
Japan	8.0	14,344,000	5,451,000

These interest rate comparisons do not consider the effect of fluctuations in the exchange rate between the currency loaned and the borrower's currency which indirectly affect the cost of a loan. For example, a foreign borrower may have to exchange more of his own currency each year to repay a loan in appreciating Deutschemarks while less currency would be required each year to repay a loan in depreciating dollars. Thus, for example, the U.S. 10.7-percent loan may be considered by sophisticated buyers to be competitive with the 8.4-percent German loan. However, Eximbank reported that, because of the difficulty of predicting long-term currency exchange rates, many U.S. exporters and bankers argue that buyers in developing countries are relatively insensitive to the relationship between interest rates and the strength of the currency in which the loan is repaid. They believe foreign buyers favor the loan with the lowest nominal rate. Also, Arrangement negotiations have not yet been successful in establishing minimum interest rates that vary with the strength of the various currencies loaned.

EXPORTS LOST BECAUSE OF UNCOMPETITIVE FINANCING

We could not develop a comprehensive estimate of exports lost because of uncompetitive Eximbank financing. Since uncompetitive prices, products, and other factors can also result in lost sales, it is not always possible to isolate the impact that financing has on particular sales. Also, there is no Government agency responsible for collecting information on exports that U.S. companies competed for and either won or lost. We did, however, develop information showing that uncompetitive financing has resulted in lost sales.

1/ During the first half of fiscal year 1979, the average loan financed by Eximbank and participating commercial banks was $34 million, repayable over 9 years.

A recent Eximbank analysis shows that some sales were lost because other governments offer better financing than Eximbank. Responses to our questionnaire support this conclusion and also show that exporters lost additional sales when they did not apply to Eximbank because the expected financing terms were known to be unsuitable.

Eximbank reviewed the status of 140 exports which it had offered to finance with direct loans and which were resolved between April 1, 1978 and March 31, 1979. U.S. firms won 62 sales; foreign firms won 55; and 23 were deferred or cancelled. Of the 62 sales won, Eximbank financed 16 at rates below its normal interest rate scale. Eximbank determined that 7 of the 55 sales (about 13%) lost to foreign competitors were valued at $91 million and were lost primarily because of uncompetitive financing; in 4 cases foreign governments offered aid or mixed credit loans and in 3 cases they offered normal export loans. This does not include cases where Eximbank believed uncompetitive financing contributed to a loss but was not the primary reason or cases where Eximbank could not determine the reason for a loss.

Our questionnaire also asked exporters about specific 1978 sales for which Eximbank offered long-term financing. The 86 responses identified 10 sales, valued at $434 million, that were lost to foreign competitors primarily because of uncompetitive financing. Examples of the reported lost sales are described below.

--A U.S. manufacturer bid on a $48-million cement plant project in Thailand. According to the foreign buyer, the U.S. company's offer was rejected because Eximbank's 8-percent interest rate, when combined with the commercial bank interest rate, was not competitive.

--An $8-million sale of grain storage plants to Tunisia was lost because Eximbank financing at 8.4 percent (to be supplemented by commercial financing) was not competitive with 3-percent government financing offered by a foreign competitor.

--A $4-million sale of data-transmission equipment to Brazil was lost because Eximbank financing at 8.5 percent was not competitive with foreign government-supported financing at 7.5 percent.

The 10 lost sales include only those for which exporters applied for and received Eximbank preliminary commitments for long-term financing. We also asked exporters about potential

1978 sales for which they did not formally request Eximbank financing. Eight firms responded that one reason they did not apply was because the expected financing terms were known to be unsuitable. These firms indicated that 44 potential sales, valued at about one-half billion dollars, were lost because they were unable to arrange for competitive financing.

Since Eximbank generally does not use its direct loan program for sales under $5 million or for sales requiring medium-term financing, exporters would not normally apply for direct loans for such sales. Commercial financing for these sales may be eligible for Eximbank's medium-term discount loan program or its Cooperative Financing Facility. However, as noted on page 8, the financing rates provided by these programs are higher than rates on foreign government-supported, medium-term financing. We could not determine how many sales were lost because of uncompetitive medium-term financing. As reflected in the following comments received with questionnaire responses, however, some exporters believe that either the discount rate should be more competitive or smaller exports should be eligible for direct loans.

--The discount loan program is normally the only method of enabling fixed-rate financing for orders ineligible for direct loans. The program is needed by small and medium-size companies and to allow small exports to be competitive. The discount rate needs to be flexible to more nearly approximate the direct loan rate for selective transactions when foreign competition is involved.

--We are concerned by Eximbank's historic reluctance to extend direct credit support for transactions below $5 million. Other export credit agencies around the world don't seem to impose that same constraint.

--Lower interest on discount loans would help the U.S. firm in competition with any European company using government-supported export financing.

FACTORS WHICH PREVENT EXIMBANK FROM CONSISTENTLY OFFERING COMPETITIVE RATES

Eximbank does not consistently match low foreign interest rates because it (1) tries to recover the cost of its own borrowings to remain self-sustaining, (2) lacks sufficient direct loan authority to more fully support long-term loans or to provide medium-term loans, and (3) must rely on its own resources to compete with other countries' mixed credits.

Efforts to be self-sustaining

Eximbank's reports to the Congress on export credit competition state that its selective efforts to be competitive must be tempered so as not to jeopardize its longstanding tradition as a self-sustaining institution; i.e., to remain self-sustaining it must charge interest rates which are not fully competitive.

To pay the interest on its own borrowings and administrative expenses and to provide reserves for loan defaults, Eximbank estimated that it must charge about one-quarter to one-half a percentage point greater than its marginal cost of money (i.e. money borrowed at 9 percent should be lent at 9.25 to 9.50 percent.) Eximbank established its current direct loan interest rate scale in October 1977, when its marginal borrowing cost was 7.25 percent. The table below shows how its cost of borrowing from the FFB has increased since then.

Date of borrowing	Amount borrowed (millions)	Interest rate (percent)
March 1, 1978	$260.0	8.02
June 1, 1978	38.8	8.42
September 1, 1978	218.0	8.49
September 1, 1978	218.0	8.56
December 1, 1978	330.0	9.02
March 1, 1979	403.0	9.35
December 3, 1979	949.8	10.56

During this same period, Eximbank's average lending rate on direct loans was 8.35 percent, or two full points below its latest borrowing cost.

The interest rate on discount loans has been pegged to the New York Federal Reserve Bank discount loan rate since June 1979. Discount loan rates have, therefore, more consistently kept pace with the increasing cost of money to the Bank than have the long-term direct lending rates.

Continued high borrowing costs, which depend on the market rates for Government securities, will adversely affect Eximbank's income and weaken its financial position if its lending rates remain stable or it tries to consistently match lower foreign rates. Eximbank estimates that if its average borrowing rate increases more than one-eighth of one percent per year and lending rates remain constant, it could be operating at a $65 million net loss by 1988. Since the Bank's accumulated income is also its reserve against loan defaults and claims, it cannot use accumulated income to subsidize its lending rates and to absorb such losses without jeopardizing the adequacy of its reserves.

Eximbank's major competitors consistently offer low interest rates on long and medium-term loans because they benefit from either low-cost government borrowings (due to lower market rates) or government subsidies. During 1978 the Japanese and German export financing agencies borrowed from their governments at interest rates of 6.05 and 4.5 percent, respectively. In France and the United Kingdom, where 1978 inflation rates of 9.1 and 8.3 percent meant relatively high borrowing costs, the governments provided $306 million and $210 million, respectively, in subsidies to their export financing agencies.

Budget limitations

Each year the Congress sets a ceiling on the total amount of direct loans Eximbank can authorize, thereby limiting the number of exports and the portion of each export that Eximbank can finance. Since commercial financing must be used for the portions of a sale not financed by Eximbank and commercial rates are at record highs, the direct loan ceiling contributes to the high interest rates.

Eximbank selectively provides up to 100 percent of the required financing for an export sale, thereby reducing commercial bank participation and lowering the effective interest rate. However, given the limits on the direct loan program, Eximbank cannot consistently finance a greater portion of individual sales unless it finances fewer exports. Eximbank's annual direct loan ceiling was increased to $3.7 billion in fiscal year 1979 and the Bank used the full amount of its authorization. The administration requested $4.1 billion and $4.3 billion ceilings for fiscal years 1980 and 1981, respectively. Even at these levels, the administration recognizes that Eximbank may not be able to offer competitive financing on all exports facing foreign government export financing support. Also, Eximbank generally does not use its direct loan program for medium-term financing or for sales under $5 million; higher direct loan ceilings would be needed to support these exports with direct loans.

Export financing agencies in other countries have more flexible budget limits than Eximbank. They are able to obtain sufficient budget authority to routinely offer medium and long-term loans at the minimum interest rates allowed under the International Arrangement on Guidelines for Officially Supported Export Credits.

Limited capability to match mixed credits

Some of Eximbank's foreign counterparts mix foreign assistance loans with export credits to reduce interest rates, but Eximbank relies on its own capital and reserves to match these mixed credits. The Agency for International Development (AID) administers the U.S. foreign assistance programs, and Eximbank does not have access to foreign assistance appropriations. Also, while in prior years the two agencies may have supported the same foreign projects, AID now emphasizes agriculture, nutrition, education, and population projects oriented to basic human needs, while Eximbank emphasizes capital intensive projects and commercial equipment sales.

As previously noted, Eximbank cannot consistently match even the normal rates offered by its foreign counterparts without adversely affecting its income.

MATTERS FOR CONSIDERATION BY THE CONGRESS

Eximbank operates on a self-sustaining basis, and within this framework it also tries to comply with its mandate to offer competitive interest rates. However, if foreign governments continue or intensify their use of concessionary financing and/or U.S. commercial interest rates and Eximbank's own borrowing costs continue at current high levels, Eximbank will need increased flexibility and additional resources to help assure that U.S. firms do not lose export sales because other governments offer better financing.

We believe that the Congress should reexamine the framework and financial constraints within which Eximbank operates and consider the measures described below which would allow it to more consistently meet foreign competition. Since some of these measures would increase the Federal budget, they will need to be considered within the context of budget and domestic economic policies and decisions on other programs oriented toward reducing the U.S. trade deficit.

Higher direct loan ceilings would give Eximbank the flexibility to use its own loans, rather than high-cost commercial loans, to more fully support exports facing competition with foreign government-supported financing. Thus, the Congress may wish to consider whether Eximbank should be given additional direct loan authority to enable it to increasingly offer

--up to 100 percent of the required long-term financing in cases where a mixture of commercial and Eximbank loans results in a blended interest rate higher than rates offered by other governments, and

--medium-term direct loans and loans for exports under $5 million in cases where commercial interest rates and Eximbank's discount rate are not competitive with financing offered by other governments.

The specific direct loan authority needed depends on the number and value of exports for which U.S. firms compete, financing terms offered by foreign governments, indirect effect of fluctuating exchange rates, availability and cost of commercial financing, interest rates charged by Eximbank, and value of sales eventually won by U.S. firms.

An alternative or supplement to increased direct loan authority would be lowered Eximbank lending rates, thereby enabling increased commercial bank participation. However, as we previously noted, Eximbank's standard lending rates are already below its marginal cost of borrowing and it selectively offers even lower rates. In the long term, this jeopardizes the Bank's traditional self-sustaining structure. If Eximbank were to continue or increase the subsidization of its lending rates with its accumulated reserves, appropriations could be needed in the future if reserves were inadequate to pay loan defaults and claims for which Eximbank is liable. Another alternative would be to provide annual appropriations to subsidize the difference between Eximbank's normal lending rates and the rates offered by other governments competing for a sale.

AGENCY COMMENTS

Treasury agreed with the report's thrust that more Eximbank financing is necessary, but felt the report's supporting arguments were often misleading. Treasury's comments were helpful and we strengthened our arguments accordingly. The Office of Management and Budget felt that the program levels sought for Eximbank were sufficient to enable it to meet critical foreign competitive financing cases. Eximbank agrees that financing is an important aspect of U.S. export competitiveness and that U.S. exports must receive adequate support in both the long and medium term, if the United States is to maximize its export opportunities.

Eximbank stressed that in cases where it provides most of the financing it's rates have been competitive. While we recognize that this is true, we point out that the extent to which Eximbank can offer such financing is limited due to direct loan ceilings and the need to operate on a self-sustaining basis.

Eximbank also stated that it did not believe it needed more resources than the administration was presently in the process of requesting from Congress. Eximbank was confident that the administration's request for some $6 billion per year in direct credit resources (or its equivalent) in fiscal years 1980 and 1981 was sufficient for it to continue providing an adequate supply of competitive long term financing. (See app. III.)

Administration plan for increased Eximbank resources

During the agency review of our report, the administration submitted a plan for expanding the credit facilities of Eximbank. The plan was sent to Congress on January 28, 1980. Essentially, the plan is a supplemental request for $250 million additional guarantee program authority. This gives Eximbank the equivalent of $1 billion in additional direct loan authority without raising the $4.1 billion direct loan ceiling in the administration's fiscal year 1980 budget. Excerpts from the plan follow.

> "There are several ways to assure that U.S. exporters have Eximbank credit available for their needs. The Bank could, for example, make greater use of the government-sponsored, privately-owned Private Export Funding Corporation (PEFCO). PEFCO raises funds from the private market, using U.S. Government guarantee to attract low rates for its transactions. Eximbank could also be allowed to draw upon the Federal Financing Bank (FFB) for increased funding. Eximbank would guarantee the direct funding provided foreign borrowers by the FFB.

"The Administration has decided to use both possibilities to expand Eximbank's credit facilities. We have, however, decided to lay particular stress upon the FFB option because it permits Eximbank to offer long-term fixed interest rate financing at rates most competitive with those offered by foreign official export credit agencies.

"It is important to note that the FFB credit availability is a standby arrangement. It will be available only for transactions that would otherwise have disrupted the financial planning process. Its use will be governed by guidelines acceptable to Treasury, Eximbank and OMB. In this regard, the Administration is seeking a $250 million supplemental increase in the Bank's FY 1980 program limitation to enable the Bank to extend its financial guarantees for FFB lending.

"The Bank will, therefore, have the following financial resources available to it in FY 1980:

Direct Loan Authority	$4.1 billion
FFB Standby	1.0
Financial Guarantees (mainly PEFCO) . . . .approx.	.7
TOTAL	$5.8 billion"

The supplemental request is evidence that the administration believes Eximbank cannot continue its present course without either jeopardizing its financial viability or its capability to consistently offer competitive financing. However, we believe the proposed off-budget approach to expanding the direct loan program is contrary to the principle of full disclosure to and review by the Congress of the budgetary programs submitted by the executive branch. If the administration believes Eximbank needs additional resources, it is our opinion that this increase should be sought through the direct budget process.

We did not evaluate the adequacy of the administration's supplemental request nor are we recommending any specific level of direct loan authority. Our report points out that higher direct loan ceilings would enable Eximbank to offer financing more competitive with foreign government-supported financing. We believe that the Congress should reexamine Eximbank's financial structure and consider the need for higher direct loan ceilings within the context of budget and domestic economic policies and other alternatives.

CHAPTER 3

EXPORTS LOST BECAUSE FOREIGN AND DOMESTIC CONSIDERATIONS RESTRICT ELIGIBILITY FOR EXIMBANK LOANS

In determining eligibility for a loan, Eximbank considers numerous factors not related to credit risks. Some of these factors, such as U.S. foreign policy considerations, make exports to various countries ineligible for Eximbank financing; others restrict financing for portions of an export not originating in the United States; and still others, such as domestic considerations, make various types of exports ineligible for financing. In contrast, other countries base eligibility for loans primarily on the creditworthiness of the borrower. Although we could not quantify the impact of the more restrictive U.S. eligibility criteria, responses to our questionnaire show that some of these factors are significant deterrents to U.S. exports.

FACTORS WHICH RESTRICT ELIGIBILITY

Factors restricting eligibility for Eximbank loans include:

--U.S. foreign policy on such issues as human rights.

--The national interest vs. financing exports to Communist countries.

--Foreign components of a U.S. export project.

--Potential adverse domestic impact of an export on U.S. employment and industry.

--Foreign environmental impact of an export.

--Effect of an export on availability of materials in short domestic supply.

We did not review the impact of all the factors which restrict eligibility for Eximbank loans; however, in questionnaire responses, the following factors were frequently cited.

Foreign policy considerations

Eximbank financing is intended to help facilitate U.S. exports, but legislation also makes Eximbank financing a foreign policy instrument.

Public Law 95-143, enacted October 26, 1977, required Eximbank to consider the observance of human rights in countries which receive exports that it finances. In November 1978, Public Law 95-630 deleted this requirement and specified that Eximbank cannot deny applications because of human rights, international terrorism, nuclear proliferation, environmental protection, or other foreign practices unless the President determines such denial will clearly advance U.S. policies.

Other legislation currently requires Presidential national interest determinations before Eximbank can support exports to Communist countries and sets a $300-million limit on Eximbank support for exports to the Soviet Union. Pending legislation would eliminate restrictions specifically pertaining to the Soviet Union and allow up to $2 billion in Eximbank support for exports to each Communist country (including the People's Republic of China) whose emigration practices meet certain requirements.

The current legislation is vague about the extent to which foreign policy should influence eligibility for loans--eligibility depends on the "national interest" and can be denied to "clearly and importantly advance United States policy." In the absence of more specific criteria, foreign policy considerations are reviewed on a case-by-case basis, as follows.

--For every application involving a direct loan or financial guarantee, Eximbank obtains specific clearance on human rights issues from the State Department.

--Members of the National Advisory Council on International Monetary and Financial Policies (NAC) review all applications for financial support of $30 million or more.

--The President reviews each application for financial support of $50 million or more for exports to Communist countries.

--The Congress reviews each application for financial support of $100 million or more.

Other countries generally do not consider foreign policy issues, such as human rights, in determining eligibility for government-supported financing nor do their legislative bodies review applications for loans.

Restrictions on foreign components

Some exports, such as power plants and construction projects, involve goods and services from more than one country. In such cases, buyers attempt to obtain financing for the entire project from the primary supplier, including segments supplied from within its own country (local costs) and segments supplied by third countries (foreign content). As a general rule, local costs and foreign content are not eligible for Eximbank loans. Other countries' export financing agencies are more flexible, and some routinely offer such financing within preestablished limits.

Local-cost financing

For exports to intermediate or relatively poor countries, the International Arrangement on Guidelines for Officially Supported Export Credits allows government-supported loans for local costs up to the amount of the cash payment, which is usually 15 percent of the export value. The Arrangement does not allow local-cost financing for exports to relatively rich countries.

The German and Japanese export financing agencies readily support local costs up to the Arrangement maximums. The French and British agencies are reluctant to support local costs, but do so because of competitive pressures.

The United States opposes all forms of government-supported export financing for local costs and has unsuccessfully attempted to negotiate changing the Arrangement to prohibit local-cost financing. Eximbank believes the Export-Import Bank Act generally makes goods and services of non-U.S. origin ineligible for Eximbank financing, and it is reluctant to use its direct loan authority for local costs. Although the Bank has recently matched some local-cost offers on a case-by-case basis, U.S. exporters cannot predict the availability of local-cost financing and this puts them in a difficult negotiating position.

Foreign-content financing

The International Arrangement does not include guidelines for foreign-content financing, which is also an important factor in the competition for some export sales.

Germany, France, and the United Kingdom routinely provide financing for foreign content--up to 40 percent of the contract value for goods from European Economic Community countries and up to 10 percent for goods from other countries. Japan does not have preestablished limits, but it will finance foreign content in Japanese export projects if required by the buyer or if the goods are not available in Japan.

Foreign content generally is not eligible for Eximbank financing for basically the same reasons local costs are not eligible. For some exports that included foreign content, Eximbank has attempted to negotiate cofinancing arrangements with other export financing agencies. For example, in June 1979 Eximbank announced a cofinancing agreement with the Japanese and Italian export financing agencies for financing sales of a jet aircraft predominantly of U.S. manufacture. While such an approach results in each country financing its share of the export, the agreements are rare and apply only to specific exports.

IMPACT OF ELIGIBILITY RESTRICTIONS

Since other countries finance exports that Eximbank does not finance, U.S. firms lose some sales they might otherwise have won. We could not quantify the impact of factors which restrict eligibility for Eximbank financing, because exporters with prior knowledge of eligibility restrictions sometimes decide not to apply for Eximbank financing and/or not to pursue a sale. However, the responses to our questionnaire provide evidence that some eligibility restrictions are significant deterrents to U.S. exports. Respondents said they did not apply for Eximbank financing for some exports during 1978 because of one or more of the following reasons.

--22 cited restrictions on financing exports to Communist countries.

--27 cited human rights considerations.

--12 cited restrictions on local-cost financing.

--17 cited restrictions on foreign-content financing.

Of these respondents, 19 said they were unable to otherwise arrange for competitive financing and lost over $2 billion in sales to foreign competitors. Since some exporters also cited other reasons for not requesting Eximbank financing, we could not determine if the above factors were the primary reasons. It is possible that some of these sales would have been lost even if they were eligible for Eximbank financing; however, without the financing, the U.S. exporters were at a competitive disadvantage.

The comments received with questionnaire responses also illustrate the impact of eligibility restrictions on Eximbank financing. For example, regarding foreign policy considerations, exporters said:

> We have been verbally discouraged from applying to Eximbank for preliminary financing commitments in several cases where human rights and other factors would have made Eximbank support difficult to obtain. As a result, we are reorienting our international marketing to source goods and services from subcontractors, suppliers, subsidiaries, and affiliates located in countries with more liberal and aggressive export credit programs, such as England, Canada, France, Japan, Italy, and Holland.

> In many demonstrable ways, Eximbank is the most highly politicized export agency in the world, as evidenced by the impact of human rights appraisals and the need for NAC and congressional approvals. Some of these aspects can constitute a severe or impossible barrier to Eximbank-supported exports.

Regarding local cost financing, exporters said:

> Eximbank's standard policy on local-cost financing should be modified to meet other countries' programs. At the moment, this is a subject which is reviewed on a case-by-case basis, which puts U.S. suppliers in a difficult negotiating posture.

> Only on rare occasions is Eximbank willing to assist in financing the related local costs of an export transaction, although European and Japanese competitors are more frequently willing to do so.

And, regarding foreign-content financing, exporters commented:

> The strict enforcement of the U.S. content requirement can be especially burdensome and contribute to our uncompetitiveness on certain projects. The export credit agencies of other countries seem far more willing to finance nondomestic products and services if there is overall benefit to the home economy. We particularly feel this bind because, in many parts of the world, industry standards and local requirements result in a need for equipment that is not available in the United States. Indeed, even for domestic projects, many components and subassemblies must be imported.
>
> Financing for foreign content of turnkey projects should be available for up to 25 to 30 percent of a project. Even if 25 percent of the contract is awarded to non-U.S. suppliers, it may be necessary to protect the 70 to 75 percent which would otherwise be lost to foreign competitors offering 100-percent financing.

MATTERS FOR CONSIDERATION BY THE CONGRESS

In view of continuing U.S. merchandise trade deficits and the importance of competitive financing, we recommend that the Congress determine whether eligibility restrictions for Eximbank financing should continue to take precedence over lost U.S. exports.

We also recommend that the Congress consider clarifying the Export-Import Bank Act and adjusting Eximbank's direct loan authority to allow greater flexibility in financing local costs and foreign content. By allowing such financing within preestablished limits, U.S. firms could better compete for projects for which local cost or foreign-content financing is required by the buyer and is offered by other countries competing for the sale.

CHAPTER 4

SCOPE OF REVIEW

We compared the government-supported export financing programs of the United States, United Kingdom, Germany, France, and Japan to determine how Eximbank financing could be made more competitive. Our review focused on critical features of loan programs, since this area of export financing, rather than insurance and guarantees, is the most competitive. We did not review the competitiveness of export financing offered by the Commodity Credit Corporation or other agencies.

We reviewed reports and records and interviewed officials from Eximbank; the Departments of State, Treasury, and Commerce; the Office of the United States Trade Representative; the Agency for International Development; and the Office of Management and Budget. We also met with representatives of commercial banks, industry trade associations, and selected business firms. We reviewed congressional testimony and reports issued by the Congressional Research Service, Chamber of Commerce of the United States, National Association of Manufacturers, and other groups. To supplement this information a questionnaire was sent to all 117 exporters that applied for Eximbank assistance but that during 1978 were either denied direct loan support or did not use the assistance offered; 86 firms responded.

In the United Kingdom, France, Germany, and Japan, the major export financing competitors of the United States, we met with government officials, exporters, and bankers to obtain information on each country's export financing programs. U.S. Embassy staff in each country also provided information and assistance. We could not determine whether the percentage of sales lost by the United States due to uncompetitive financing was greater or less than the percentage of sales lost by other countries, because no comprehensive information is available on sales for which there was competition.

ARRANGEMENT ON GUIDELINES FOR OFFICIALLY SUPPORTED EXPORT CREDITS

For several years Eximbank participated in negotiations with foreign government-supported export credit agencies to establish international export financing standards. In June 1976, the United States unilaterally declared it would comply with specified minimum interest rates and maximum repayment terms and other industrial countries made similar declarations. However, the generality of the terms and the absence of a uniform text made further definition and improvement desirable. After an intensive series of meetings among 22 participating countries, agreement was reached on a new "Arrangement on Guidelines for Officially Supported Export Credits", which was implemented in April 1978.

KEY PROVISIONS OF ARRANGEMENT

The Arrangement's reporting requirements give export credit agencies greater knowledge about the financing terms offered by competitors. If a participant offers more concessional financing than allowed by the Arrangement, other participants must be notified and given the opportunity to match such offers. The visibility resulting from this system is an important factor in minimizing financing competition.

Other key features of the Arrangement are summarized below.

1. Cash payment must equal at least 15 percent of the export value.

2. Repayment terms cannot exceed 10 years for exports to relatively poor countries or 8.5 years for exports to other countries.

3. Minimum interest rates are established based on the wealth of the buyer country and the term of the loan and range from 7.25 to 8 percent.

4. Costs incurred in the buyer country (local costs) can be financed only up to the amount of the cash payment.

5. Export credits can be mixed with foreign assistance funds (mixed credits). If the aid funds comprise less than 25 percent of the total credit, other participants must be notified.

The Arrangement does not apply to military equipment, agricultural commodities, aircraft, nuclear power plants, or some types of ships.

EFFORTS TO IMPROVE ARRANGEMENT

The United States has made several attempts to negotiate changes to the Arrangement and thereby reduce competition in export financing. In late 1978, the Secretary of the Treasury and other U.S. representatives attempted to

--increase the minimum interest rates;

--end official support for local costs;

--put additional limits on the use of mixed credits; and

--include agriculture, aircraft, nuclear power plants, and ship exports.

In March 1979, the President announced that these negotiations did not result in agreements acceptable to the United States and concluded that the only feasible course of action was to assure that U.S. export financing programs and policies remain competitive.

THE WHITE HOUSE

TO THE CONGRESS OF THE UNITED STATES:

The Export-Import Bank Act of 1945 as amended in November 1978 (Sec. 1908(a) of Public Law 95-630) requested me "to begin negotiations at the ministerial level with other major exporting countries to end predatory export financing programs and other forms of export subsidies, including mixed credits, in third country markets as well as within the United States." The legislation called for a report to the Congress on progress toward meeting these goals.

As I indicated on September 26, 1978, in my Statement on Export Policy, this Administration attaches high priority to increasing American exports. The Export-Import Bank plays a very significant role in that effort. Accordingly, this Administration has sought to make the Bank's financing more competitive with the official export financing provided by other governments and, at the same time, to improve the International Arrangement on Export Credits so as to avoid costly and self-defeating export credit competition between sovereign governments.

I directed the Secretary of the Treasury to undertake the appropriate negotiations. In fact, Secretary Blumenthal had already alerted foreign governments to the need for a broadened and strengthened International Arrangement at the OECD Ministerial Meeting in June 1978 and the issue was again raised at the meeting which prepared the agenda for the Bonn Summit. In September 1978, Secretary Blumenthal emphasized to the Finance Ministries of our major trading partners the importance of substantive improvements in the International Arrangement on Export Credits. He presented detailed proposals designed to bring the financing terms set forth in the Arrangement closer to worldwide commercial practices and to broaden the Arrangement to cover sectors presently excluded from coverage.

Briefly, these proposals called for increases ranging from 1/2 to 3/4 of one percent in the minimum interest rates called for by the Arrangement, the elimination of local cost support by export credit agencies, and greater restraint in the use of highly concessional mixed credits. In addition, maximum repayment terms and minimum interest rates were proposed for aircraft, nuclear power plants, and liquefied natural gas (LNG) tankers, sectors presently excluded from the Arrangement. Similarly, a proposal was made to have the Arrangement cover credits for agricultural commodities in excess of three years but not more than ten years. Additional possibilities for improving the Arrangment emerged during the subsequent discussions.

These proposals were presented to the twenty-two countries participating in the International Arrangment on Export Credits for consideration at their October 1978 meeting. At our urging, these countries agreed to establish a working group to consider improvements in the Arrangement. The working group met in December 1978 and in January 1979. In addition, representatives of the U.S. Government discussed these proposals at length in bilateral meetings with other governments.

Although the substance of our proposals appeared to constitute a basis for negotiations, the required unanimity for the changes we sought in the Arrangement were lacking. As a result, no agreement regarding modifications in the Arrangement acceptable to the U.S. Government could be reached.

I have therefore reluctantly concluded that further negotiations would not be productive at this time. If the countries which have opposed the improvements we have suggested evidence their willingness to be more forthcoming, I would be prepared to resume negotiations at any time.

For the present, however, the lack of progress requires us to reexamine our own efforts to assure that we remain competitive in the export credit field. Our examination may well indicate that we should modify some of our own programs and policies until such time as there is more willingness among our trading partners to impose the needed self-discipline on export credit practices.

Meanwhile, the United States will continue to adhere to the International Arrangement on Export Credits because it remains a useful, if limited, instrument of international discipline in the provision of officially supported export credits. Within this framework, the Export-Import Bank, operating in consultation with the National Advisory Council on International Monetary and Financial Policy (NAC), will provide the necessary export financing support to allow American exporters to meet foreign official export credit competition. For example, Eximbank will continue its recently adopted policy of matching mixed credits on a selective basis, a policy which proved effective recently when an American exporter was awarded a contract based on an Eximbank financing package that matched the mixed credit offer of a foreign government.

Finally, in my FY 1980 budget, I have asked the Congress for $4.1 billion in direct lending authority for Eximbank, an increase of $500 million from FY 1979 budget. I have asked for this increase, together with $6.8 bilion in insurance and loan guarantee authority, in a year in which I am determined to cut the Federal budget deficit to below $30 billion. I expect the Bank to husband these new resources carefully, but I also expect the Bank to aggressively meet official export credit competition.

The attached annex details the discussions and the actions taken to improve the International Arrangement and provide competitive official export credit financing.

JIMMY CARTER

THE WHITE HOUSE
March 16, 1979.

EXPORT-IMPORT BANK OF THE UNITED STATES
WASHINGTON, D.C. 20571

PRESIDENT
AND
CHAIRMAN

CABLE ADDRESS "EXIMBANK"
TELEX 89-461

January 18, 1980

Dear Mr. Fasick:

Thank you for the opportunity to comment on the GAO draft entitled, "More Competitive Eximbank Financing Is Needed to Help Increase U.S. Exports." While I agree with the substance of your conclusions--which I take to be that financing is an important aspect of U.S. export competitiveness and U.S. exporters must receive adequate support, in both the long- and medium-term, if the U.S. is to maximize its export opportunities--I do not believe that Eximbank needs more resources than the Administration is presently in the process of requesting from Congress in order to provide adequate support for Eximbank. (See p. 16)

Looking first at the long-term (over five-year repayment) arena, I must say that I believe Eximbank has been quite competitive in this area for the last two to three years. There are three particularly relevant points to make in support of that conclusion:

1. In only one of the last three fiscal years (i.e., FY 1979) was Eximbank able to attain the level of credit authorizations allowed by the budget. Hence, resource availability has not recently constrained Eximbank's ability to provide an adequate volume of competitive financing. (See GAO note 1)

2. When one looks at the total all-in cost (including both interest rate charged the borrower and insurance premium charged the exporter), the Eximbank "cost" in the majority of non-aircraft cases is very comparable to other systems. The average all-in cost of the five major competitors is between 8.25 and 8.50 percent, which compares quite favorably with an average all-in Eximbank rate of 8.35 to 8.50 percent when Eximbank offers 85 percent coverage (see Appendix A for technical comment on Eximbank rate calculation). (See GAO note 1)

3. The point that the U.S. lost some volume of sales due to uncompetitive financing should not be taken as an indictment of the system unless it can be established that the ratio of U.S. sales lost for (See GAO note 2)

that reason is noticeably higher than the ratio of Japanese, German, or other foreign competitor sales lost for that reason.

Although the future is always uncertain, I feel confident in saying that the Administration's request for some $6 billion per year in direct credit (or its equivalent) resources in FY 1980 and FY 1981 (See p. 16) is sufficient for Eximbank to continue providing an adequate supply of competitive long-term export financing. I would be quite surprised and disappointed if an exporter survey taken on events of the next year were to turn up anywhere near the $1.0 billion in U.S. sales lost due to uncompetitive financing that was found in your survey.

In the medium-term (one- to five-year repayment) arena, the past few years clearly must be considered a time of uncompetitive U.S. (See GAO note 3) Government support. However, we are analyzing the impact of that status on U.S. export performance and evaluating the appropriateness and feasibility of providing more competitive financing.

The issue of increasing Eximbank's equity is simply premature. (See GAO note 4) If the United States were totally unsuccessful in ever getting OECD agreement to raise the minimum interest rates while Eximbank's cost of funds stayed near present levels, it would take most of the 1980's before Eximbank's annual net income could turn negative. However, I believe I am being reasonable in assuming both an ever-increasing number of governments are realizing the foolish expense of subsidizing export credit and that U.S. interest rates will not remain at present levels throughout the 1980's. If I am right, Eximbank will not need any increase in equity in the foreseeable future.

In sum, I believe you are right in saying that Eximbank must increase its competitiveness; but I believe Eximbank can accomplish that result within presently envisaged resource constraints. We at Eximbank welcome working with the Congress to this end.

Sincerely,

John L. Moore, Jr.

Mr. J.K. Fasick
Director of International Division
Room 4804
U.S. General Accounting Office
441 G Street, N.W.
Washington, D.C. 20548

APPENDIX A

TECHNICAL COMMENTS

p. ii: While it is true that Eximbank has no access to foreign assistance funds and, therefore, cannot offer true "mixed" credits, GAO overlooked the fact that Eximbank does match selected mixed credits by structuring Eximbank's credit offer to simulate exactly the foreign mixed credit offer. (See GAO note 5)

pp. 9-10: The comparison of U.S. and foreign rates is faulty in two major respects. First, it assumes that the prime lending rate averages around 11.5 percent over the next five years. While that may be true, it does not seem a reasonable nor unbiased base on which to build so sensitive a figure as Eximbank's "blended" rate. Using a more neutral estimate like 10 percent reduces the blend to under 10.0 percent. More importantly, however, the comparison ignores the fact that, on the majority of non-aircraft cases receiving Eximbank offers of assistance, Eximbank provides 70 to 85 percent coverage. With an 85 percent Eximbank credit at 8.375 percent, the U.S. cost is around 8.6 percent--equal to France and noticeably higher than only Japan. **(See p. 7)**

p. 18: It probably should be noted that the 6.05 percent and 4.5 percent rates mentioned for the Japanese and Germans were primarily due to low market rates in those countries, not to some government subsidy or intervention scheme. (See GAO note 6)

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

ASSISTANT SECRETARY

FEB 4 1980

Dear Mr. Fasick:

Thank you for giving the Treasury Department an opportunity to comment on the GAO draft entitled "More Competitive Eximbank Financing is Needed To Help Increase U.S. Exports." While I agree with the report's thrust that more Eximbank financing is necessary, the report's supporting arguments are often misleading.

For example, the chart on page 5 of the report (See GAO note 7) shows the percentage of total exports supported by official export credit programs in several countries. It implies that countries such as Japan and the United Kingdom finance 35 percent of their exports through direct credits. However, the figures shown in the report include the guarantee and insurance programs of these countries -- which the draft report states on page 7 "are usually of minor importance in international competition for export sales." The more accurate comparative figures in 1978 for long-term direct credits alone are as follows:

	Long-Term Direct Credits as Percent of Total Exports		GAO Report
Japan	2.2%	as compared to	35%
United Kingdom	1.6%		35%
France	3.9%		29%
Germany	1.8%		12%
United States	2.7%		6%

I believe the report could make the point that other nations provide significant subsidies for exports by directly analyzing the subsidy element in foreign official export credit programs, rather than by indirectly inferring a subsidy from the percentages of exports covered by those programs.

There are other weaknesses with the report's analysis. The report appears to accept the notion that numerous foreign buyers suffer from an interest rate illusion. Buyers suffering from this illusion are (See GAO note 13) said to be concerned only with the nominal interest rate on a loan and not with the currency in which a loan is denominated. The rationale for the illusion is that future exchange rates are unpredictable, and hence currency expectations will be disregarded by foreign borrowers.

No one can predict with confidence what relative exchange rates will be in the future, but the existence of this illusion is supported neither by experience nor by theory. Buyers ordinarily do have some exchange rate expectations in mind when considering competing export credit offers. Indeed, expected exchange rate movements are generally reflected in interest rate differentials. Some buyers may suffer from interest rate illusion, but it is unlikely that all buyers are ignorant of the difference between dollar finance and Swiss franc finance. It makes little sense to recommend that the U.S. Government should answer an illusion of this type by offering, say, the Swiss franc interest rate for a U.S. dollar credit. (See GAO note 13)

This leads to another example of how the draft might be improved. The table on page 12 demonstrates only that a higher interest rate means a higher interest cost. What it should show as well is the borrower's total cost in each currency. Had the table shown a borrower's total cost in Deutsche mark or Japanese yen vis-a-vis the dollar over the last nine years, Eximbank might have seemed very competitive.

As a corollary of this point, the draft is mistaken when it implies that the normal rate on Eximbank loans is 10.3 percent. Eximbank's recent average lending rate has been 8.2 percent. The higher rate is found only when (See GAO note 1) Eximbank blends its rate with private export rates on an equal basis. In cases of foreign competition, however, the Eximbank participation is often 70 to 85 percent.

On page 14, the draft cites an Eximbank study of Eximbank-supported export bids which were turned down by the buyer. Of fifty-five lost sales, which had been supported by Eximbank, only seven were lost because the buyer had a more attractive foreign official export financing offer. And of the seven, four were lost because of foreign aid financing, not foreign official export credits. Thus only three -- less than 6 percent -- were lost because of foreign official export credit competition. If U.S. Eximbank rates are as uncompetitive as the draft would have us believe, why weren't more than three sales lost because of uncompetitive Eximbank financing? Clearly other factors -- such as price, quality and service -- are important to foreign buyers. (See GAO note 8)

It would also be helpful if the present GAO report considered the arguments set forth in a 1975 GAO report, "Weakened Financial Condition of the Export-Import Bank of the United States" before recommending that the Bank lower its interest rates to compete more aggressively with foreign export credit programs. The earlier report (See GAO note 9) noted that Eximbank had weakened itself by charging overly low interest rates on its loans. It recommended that steps be taken to remedy this situation, for otherwise, "Eximbank's status as a self-sustaining institution will be in doubt." Is the GAO no longer concerned with the Congressional mandate that the Bank take into consideration its average cost of money when offering direct credits to borrowers?

Despite these criticisms, I too believe that Eximbank should have adequate resources to meet foreign official export credit competition. There is no doubt that our competitors subsidize their exports through low cost credits. While we are attempting to strengthen the ground rules in the International Arrangement on Export Credits, it is appropriate to seek a stronger Eximbank, both to minimize the competitive disadvantage that our exporters may face, and to demonstrate to foreign governments that we are prepared to negotiate the reduction of export credit subsidies from a position of strength. (See GAO note 13)

APPENDIX III

Mr. John Lange, Director, Office of Trade Finance, would be delighted to give your staff any assistance they might want in strengthening the draft report's analysis.

I hope my comments have been helpful.

Sincerely,

C. Fred Bergsten

Mr. J. K. Fasick
Director
International Division
United States General
Accounting Office
Washington, D.C. 20548

 APPENDIX III

EXECUTIVE OFFICE OF THE PRESIDENT

OFFICE OF MANAGEMENT AND BUDGET

WASHINGTON, D.C. 20503

Allen R. Voss
Director
General Government Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Voss:

I am responding on behalf of OMB to your request for comment on GAO's draft report, "More Competitive Eximbank Financing is Needed to Help Increase U.S. Exports".

Two aspects to your recommendations for improving Eximbank's ability to offer competitive financing are of particular relevance to OMB: 1) increasing the level and flexibility of the Bank's direct loan program, and (2) enhancing the Bank's ability to increase the interest subsidy on its financing.

> GAO believes that the Congress may wish to consider providing Eximbank higher, more flexible direct loan ceilings....(page ii)
>
> If the Congress decides Eximbank should consistently offer competitive financing, it could authorize the Bank to use its reserves to subsidize lending rates.... Alternatively, the Congress could authorize appropriations to subsidize the difference between Eximbank's normal lending rates and the rates offered by other countries. (page iii)

First, with regard to increasing Eximbank's program level, the Administration has already taken a number of steps to improve our competitive position and improve the export climate. The growth of Eximbank's programs in dollar value, coverage and competitiveness reflect that concern. This Administration has steadily increased the Bank's budgetary resources and the Bank has rapidly increased the average cover of its loans in financial packages (from 45% of export value during 1972-1977 to 61% during 1978-1979). Eximbank has also consistently provided fuller competitive cover on a case-by-case basis as required. The draft GAO report does not adequately reflect the substantial steps that have been taken. (See p. 15)

The Administration's budget proposals for Eximbank reflect a careful weighing of the Bank's requirements along with those of other programs, both those oriented towards the trade sector as well as those with other domestic and international objectives. The overall policy of fiscal restraint has required difficult choices among competing programs. The program levels sought for Eximbank and approved by Congress have reflected the competing priorities and have been judged sufficient to supplement private sector financing and provide resources to meet critical foreign competitive financing cases. A higher Eximbank lending program would necessitate reductions in other programs which are also judged to be of high priority. (See GAO note 10) (See p. 15)

The GAO draft report appears to recommend establishing a highly flexible program ceiling for Eximbank without an effective limit, such as exists in some competitor countries. This would effectively turn Eximbank into an "entitlement" program. In addition to the direct budgetary cost of such a step, there are two significant dangers. First, such a step would make Eximbank the lender of first resort, attracting foreign borrowers who normally would finance through commercial banks at higher rates. Second, it would set a clear precedent for expanding Federal credit programs to assist other sectors of the economy. This would run counter to the Administration's current efforts to limit the growth of government credit programs. (See GAO note 11)

Second, the draft report's recommendation to increase interest subsidies raises serious issues. As you indicate: "it is the clear intent of Congress that Eximbank be self-sustaining, and within this framework Eximbank also tries to comply with its mandate to offer competitive interest rates" (page 21). Interest rate competitiveness, therefore, is a complex issue. Today, Eximbank's standard rates and the rates in blended financial packages are above those of competitor countries, but well below its own cost of funds and private market rates. In competitive export cases, however, the Export-Import Bank does match competitor rates by raising its coverage and cutting interest rates. By avoiding this practice in all cases, the Bank encourages private sector participation and avoids the use of unnecessary and costly interest subsidies. The negative spread of well over 1 percent between the Bank's average interest expense rate and average interest receivable rate is costing the Bank over $125 million annually in lost income and additions to reserves. This is a good indication of the efforts being made to meet foreign competition. (See GAO note 1)

The Administration does have other concerns as well. The self-financing aspect of the Bank has been a matter of policy. The Bank needs to strike a careful balance in matching competitive rates on difficult export cases, avoiding undercutting private banks on export cases without foreign official financing, and maintaining its self-sustaining basis. The export trade sector is obtaining financing today on terms far more favorable than many other sectors of the economy have access to. The Administration does not believe that additional resources for subsidizing Eximbank's lending rates are warranted by the current trade situation. (See GAO note 12)

3

In addition, discussion and negotiations on the International Arrangement on Export Credits are continuing; and we are hopeful that some of the alternative control mechanisms under review (that would bring lending rates in export finance into closer conformity with domestic lending rates) may prove to be acceptable to a majority of the Participants. (See GAO note 13)

One other aspect of the report deserves comment. The report asserts that the United States has suffered from a continuous decline in its trade share and that the current "massive" trade deficits call for action to restore U.S. exports. U.S. exports have, however, grown dramatically in the past two years and the U.S. current account will be approximately in balance in 1979 and 1980. The dramatic and continuing surge since 1970 in our surplus on the services account has given the United States a relatively comfortable position, even with respect to Japan and Germany today. Further, recent detailed analysis of developments in the U.S. world trade share indicate that the decline of the U.S. trade share during the 1960s was arrested in the 1970s and that our share has fluctuated around a level trend since 1970. While the Administration will continue to press to improve the export climate and reduce restrictive factors where feasible, the current trade situation now appears more favorable than it was until recently thought to be. (See GAO note 12)

We trust that these comments will be helpful to you. We will be glad to meet with you and your staff to further discussion if you think that will be useful.

Sincerely,

Edward R. Jayne II
Associate Director for
National Security and
International Affairs

GAO'S EVALUATION OF AGENCY COMMENTS

GAO NOTE 1 - Comparable rates

The executive organizations noted that Eximbank has been making greater efforts to match competitor rates by raising its coverage and reducing interest rates. In sum, they argue that Eximbank has been quite competitive in long-term financing the last few years.

Our evaluation

Eximbank's direct loan authority and direct loan commitments for fiscal years 1977-79 were as follows:

Fiscal year	Direct loan authority	Direct loan commitment
	(billions)	
1977	$ 3.88	$ 0.70
1978	3.60	2.87
1979	3.75	3.75

Since 1977, U.S. commercial interest rates increased to levels above those of foreign government-supported rates. Thus, demand for Eximbank financing has increased. Eximbank, in its attempt to offer competitive financing, has increasingly financed a larger portion of individual sales. This is reflected in its increased direct loan commitments.

As discussed on page 7 of the report, the standard rate on Eximbank long-term financing (considering the blended Government and commercial segments of the loan) was about 2 to 3 percentage points higher than the base rate on government-supported financing offered by Germany, France, the United Kingdom, and Japan.

When Eximbank provides all the required financing on an export sale (85 percent coverage after a 15 percent downpayment) at interest rates of 8.35 to 8.50 percent, its terms are indeed more competitive with financing offered by other countries. Page 8 of the report notes that in fiscal year 1979 Eximbank made 19 of 98 loans at interest rates below its normal scale and that in 15 of the 19 it provided all the financing without commercial bank participation. We point out that Eximbank only goes below scale or provides 100 percent cover on an exception basis.

However, the extent to which Eximbank can offer such financing is limited; as it finances a larger portion of individual sales, annual direct loan ceilings constrain the number of exports for which it can offer competitive financing. For example, during fiscal year 1979, one export project won by U.S. firms required about $936 million in direct loan authority, or about 25 percent of the full year's authority. Lacking sufficient budget authority to provide the total financing in fiscal year 1979, Eximbank split the transaction and authorized $504 million in fiscal year 1980.

Also, Eximbank's standard lending rates, as well as the lower rates offered on a case-by-case basis, are below its marginal cost of funds (10.5 percent as of December 1979). At these lending rates, Eximbank must internally subsidize its loans through decreased contributions to reserves.

Thus, the report shows that the Bank cannot be fully competitive in all cases because of budget restraints and that it cannot continue charging less for its money than its costs to borrow the funds without running into financial difficulties in the years ahead. We, therefore, have called for a congressional reexamination of the framework and financial constraints within which Eximbank now operates.

Based on agency comments, we updated the calculation of Eximbank's lending rates and added more detail to highlight its efforts to be competitive on a selected basis. (See pp. 6 to 8.)

GAO NOTE 2 - Indictment of the system

The point that the United States lost some volume of sales due to uncompetitive financing was not intended as an "indictment of the system." The lost sales illustrate the point that government-supported export financing can be critical in the competition for some export sales. The examples were intended to demonstrate the potential effect of Eximbank's current inability to consistently offer competitive financing.

GAO NOTE 3 - Medium-term financing

Eximbank agrees that its medium-term programs clearly must be considered uncompetitive. One alternative for improving competitiveness is to make exports requiring medium-term financing eligible for direct loans. This and other alternatives should be considered within the context of a broader reexamination of Eximbank's role and financial structure.

GAO NOTE 4 - Increasing Eximbank's equity

We have not recommended an increase in Eximbank's equity. However, we do believe it is necessary for the Congress to reexamine Eximbank's financial structure. In view of agressive foreign government-supported export financing, high U.S commercial interest rates, and Eximbank's high cost of borrowing, Eximbank is faced with the prospect of higher loan exposure and proportionately decreasing contributions to reserves. While an increase in Eximbank's equity may be one avenue toward resolving this conflict, other alternatives should be considered, as presented on pp. 14 and 15 of our report.

GAO NOTE 5 - Mixed credits

The fact that Eximbank does selectively match mixed credits is pointed out on page 8 of our report. The referenced section of the digest (page ii) stated that Eximbank does not offer mixed credits. This is technically correct in that "mixed credits" are a mixture of aid funds and normal export loans and Eximbank does not have access to aid funds. To clarify this, we modified the digest.

GAO NOTE 6 - Japanese and German rates

We do not state in the report that the German and Japanese lending rates are achieved through government subsidies. The only subsidies discussed are related to the French and British export financing agencies.

Long-term government bond market rates in Japan and Germany have recently increased to or above the 7.5-percent officially supported export financial rates. The rate at which the Japanese Export-Import Bank borrows from its government increased from 6.05 to 6.65 percent in 1979, compared with Eximbank's March 1979 borrowing cost of 9.35 percent.

GAO NOTE 7 - Chart on export credit support

We have clarified the chart title and included a footnote to better identify that the chart does include insurance and guarantee programs as well as direct credits. The chart is intended to illustate the overall degree of government commitment to providing official export credit support, as discussed on page 3. The chart is not intended to compare the relative importance of the various types of support offered by each country.

We clarified our previous statement that insurance and guarantee programs "are usually of minor importance in international competition for export sales." Insurance and guarantee programs provide access to commercial financing, but, at a time of record high U.S. commercial interest rates, Eximbank's insurance and guarantee programs generally do not lower the interest rates to competitive levels. On the other hand, in Japan and Germany, where commercial rates are lower, the government-supported insurance and guarantee programs are of relatively greater importance because they provide access to commercial financing.

The point that other nations provide export financing subsidies is already discussed on pages 3 and 13 of our report.

GAO NOTE 8 - Lost sales

As noted on page 9 of our report, we could not develop a comprehensive estimate of sales lost because of uncompetitive Eximbank financing. While we agree that price, quality, and service are certainly important to foreign buyers, the examples of lost sales are included to illustrate that financing can also be critical and that some sales were lost because other governments offered better financing. The seven lost sales identified in Eximbank's analysis include only those where exporters applied for and received Eximbank preliminary commitments for long-term financing. We cannot estimate the total lost sales attributable to uncompetitive financing because there is no comprehensive information available on all sales for which U.S. exporters competed.

GAO NOTE 9 - Lower rates and 1975 GAO report

We have not recommended that Eximbank lower its interest rates, and the issues set forth in our 1975 report are of increasing concern today. As discussed on pages 7, 8, and 12 of the report, Eximbank's standard lending rates, as well as the lower rates offered on a case-by-case basis, are below its marginal borrowing costs. We also noted that Eximbank's current selective efforts to be competitive must be tempered if the Bank is to remain self-sustaining.

On page 9 of our 1975 report, we stated that:

"We recognize that Eximbank's purpose is to promote exports and we believe it should do everything possible to do so on a self-sustaining basis. If that cannot be achieved, Eximbank should more clearly identify the extent to which public subsidization of its operation is required."

The matters for consideration in our current report are consistent with the 1975 report. As noted on page 14, we suggested that the Congress reexamine the framework and financial constraints within which Eximbank now operates.

GAO NOTE 10 - Program levels

OMB said that the program levels sought for Eximbank and approved by the Congress have reflected the competing priorities and have been judged sufficient to supplement private sector financing and to provide resources to meet critical foreign competitive financing cases. (Underscoring supplied.) As of January 23, 1980, the date of OMB's comments, the Congress had not yet approved the administration's fiscal year 1980 $4.1-billion direct loan program authorization nor had it acted on the administration's fiscal year 1980 $250-million supplemental request for the guarantee program.

GAO NOTE 11 - Entitlement program

We definitely are not recommending a limitless Eximbank budget. Our point is that additional budget authority would allow Eximbank to be more competitive in a greater number of cases. We are raising an issue, but not providing an answer to the amount of money the Bank should be authorized; that is a decision for the Congress. Also, we stated that the Congress should consider increasing the Bank's budget, not that it should increase it.

We are not advocating that Eximbank establish an entitlement program or become a lender of first resort. Rather, we believe that the Congress, as part of its reexamination of Eximbank, needs to focus on Eximbank's legislative mandate to offer competitive financing.

GAO NOTE 12 - Current trade situation

We agree that U.S. exports have shown marked improvement in the past 2 years and that the U.S. current account was approximately in balance in 1979. (Preliminary estimate for the 1980 current account balance is a deficit of $3.5 billion.) However, the U.S. merchandise trade balance for 1979 is still a deficit of about $24.6 billion; fourth quarter activity showed a widening of the trade deficit as imports increased faster than exports.

The Government analysis of development in the U.S. trade share does show a cessation of the decline of the U.S. share of world trade and a level trend since 1970. The analysis also showed that other countries now have increased ability to compete with the United States. Thus, the future most likely will involve more intense competition to maintain even the new reduced U.S. share of world trade.

GAO NOTE 13 - Interest rate illusion and the Arrangement

Treasury and OMB both raised the issues of interest rate illusion and the related efforts under the Arrangement to establish an acceptable method of reflecting the strength of various currencies in the minimum interest rates established for government-supported export financing.

Our evaluation

On page ii of the digest and page 9 of the report, we point out that fluctuations in exchange rates can affect the real cost of a loan and complicate comparisons among nominal interest rates. However, the significance of the fact must be considered in the following context.

1. The possibility of comparing interest rates in "real" terms is limited by the uncertainties in predicting long-term exchange rate fluctuations. While a retrospective analysis of the Deutschemark and Japanese yen vis-a-vis the dollar may reveal that the Eximbank interest rates in real terms were competitive, buyers 9 years ago faced the difficulty of predicting the exchange rate fluctuations and face the same problems today. As noted on page 9, Eximbank reported that many U.S. exporters and banks argue that buyers in developing countries are relatively insensitive to the relationship between interest rate and the strength of the currency borrowed.

2. The interest rates quoted on page 7 of the report for the United Kingdom are for loans denominated in U.S. dollars and, therefore, can be directly compared to the interest rates on Eximbank-supported financing. While the German and Japanese Government's export financing agencies have to date resisted pressures by their exporters to offer dollar financing, both offer exchange rate fluctuation insurance intended to partially protect exporters that privately convert loans to dollars.

3. Recent negotiations on the International Arrangement have focused on establishing a method to reflect the strength of various currencies in the minimum interest rates established for government-supported export financing. Lack of agreement on this issue and reliance on a single interest rate minimum for all currencies reflect the conflicting views concerning the significance of anticipated exchange rate movement on buyers' evaluations of nominal interest rates.

4. Some economists argue that the prevailing exchange rates already reflect not only current differences in the strength of currencies but also the discounted effect of future movements in the strength of currencies.

5. Exporters or foreign buyers can negotiate forward exchange contracts through commercial sources to partially protect themselves against exchange rate fluctuations.

We are not recommending that the United States provide export financing at rates that exactly match the nominal rates offered by other governments. In setting its lending rates, Eximbank should consider all factors which influence the competitiveness of its rate, including, to the extent practical, the market's perception of the influence of exchange rate fluctuations.

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