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EXPORT FINANCE

Challenges Facing the U.S. Export-Import Bank

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EXPORT FINANCE:
CHALLENGES FACING THE U.S. EXPORT-IMPORT BANK

SUMMARY OF STATEMENT BY ALLAN I. MENDELOWITZ, MANAGING DIRECTOR
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Overlap exists in federal export financing programs, such as that between the U.S. Export-Import Bank (Eximbank) and Small Business Administration (SBA) programs for small businesses and Eximbank and Department of Agriculture programs to finance agricultural products. In its September 1993 plan, "Toward a National Export Strategy," the interagency Trade Promotion Coordinating Committee (TPCC) made some specific recommendations, including a recommendation that addressed overlap between Eximbank and SBA programs. The plan contained no recommendations concerning the overlap of Eximbank and Department of Agriculture programs.

U.S. trade policy has generally been to oppose tied aid and dissuade our competitors from using it through international negotiations. A 1992 Organization for Economic Cooperation and Development (OECD) agreement established guidelines to discourage the use of trade-distorting tied aid. Since the agreement went into effect, Eximbank policy has been to use its "war chest" (a fund for responding to other countries' tied aid practices) only to police the OECD agreement. However, there are doubts about the effectiveness of the policy in view of weaknesses in the agreement and questions about its enforceability. Further, even if a competitor's tied aid offer conforms to the terms of the agreement, it may still hurt U.S. exporters and U.S. economic interests. The administration has recently proposed establishing a $150-million aid fund to finance major capital projects overseas as a way of combating other countries' tied aid use.

Changes resulting from the Federal Credit Reform Act of 1990 increase congressional budgetary control over the Eximbank. Congress limits the maximum costs involved in potential transactions up front--during the budget process. However, credit reform does not help Congress know how much in the way of exports any given authorized budget amount will support.

The Eximbank uses commercial banks and federal, state, and local agencies to make its services available to as many exporters as possible. Some of the Eximbank's efforts to expand the delivery of its services include making changes to increase commercial banks' participation in its programs, administering a city/state program, and using regional offices.

In the Eximbank's congressionally mandated annual survey of its customers (exporters and bankers), respondents perceived that the official export credit agencies of France and Japan have the most competitive programs overall and that the Eximbank has the least competitive programs. The chief complaint of survey respondents was lengthy case-processing time.

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to testify before this Subcommittee on some issues affecting the U.S. Export-Import Bank (Eximbank) in its role of assisting U.S. exporters. As the Trade Promotion Coordinating Committee (TPCC) grapples with the task of defining and implementing the federal export promotion strategy, the Eximbank's role is being examined more closely than ever. Because it is the primary source of federal export credits, particularly in an environment where commercial banks are avoiding export finance, the Eximbank is a significant component of the government's export promotion efforts.

My remarks are based primarily on a GAO report on the Eximbank, and testimonies and reports on federal export promotion efforts in general, issued in the past year.

BACKGROUND

While the demand for export financing is growing in the United States, the availability of commercial financing has been problematic for certain markets. This situation has created an increased demand for Eximbank services. In fiscal year 1991, the Eximbank used virtually all of its budget authority for loans, guarantees and insurance--$11.3 billion--for the first time since 1980. The Eximbank offers a wide range of export financing assistance, including direct loans, loan guarantees, and export credit insurance covering commercial and political risks. It also provides pre-export, or "working capital," financing that is needed to finance pre-export production or to develop foreign markets. In fiscal year 1992, the Eximbank provided $12.3 billion in assistance to U.S. exporters, a significant increase over the amount of assistance provided in previous years. For example, the Eximbank provided $6.4 billion to exporters in fiscal year 1988. Further, the number of transactions authorized by the Eximbank increased from 1,395 in fiscal year 1988 to 1,700 in fiscal year 1992. Nevertheless, the size of the Eximbank's staff did not significantly increase over this period. This circumstance has created many challenges for the Eximbank. Some of the major challenges the Eximbank is facing are (1) its coordination with other agencies and its role within the interagency TPCC, (2) its use of tied aid, (3) the implementation of credit reform, (4) the delivery of its services, and (5) the evaluation of the competitiveness of Eximbank assistance.

EXIMBANK'S COORDINATION WITH OTHER AGENCIES AND TPCC

One of the Eximbank's stated objectives is to work more effectively with other government agencies to better serve U.S. exporters. In our December 1992 report on the Eximbank,[1] we reported that

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[1] Export Finance: The Role of the U.S. Export-Import Bank (GAO/GGD-93-39, Dec. 23, 1992).

although the Eximbank had worked well with other agencies to coordinate certain policies at a strategic level (such as developing risk assessment policies), it had not been as successful in coordinating its programs at the operational level (providing services to exporters) with those of other agencies. For example, overlap exists in financing exports: The Eximbank and the Small Business Administration (SBA) both have export financing programs for small businesses, and the Eximbank and the Department of Agriculture both provide financing for agricultural products.

The Eximbank is one of the five core agencies involved in export promotion. (The others are the Departments of Agriculture and Commerce, the Agency for International Development, and SBA.) In several reviews over the past 2 years, we found that federal export promotion programs were fragmented among 10 agencies and suffered from inefficiencies, overlap, and duplication. Further, there was no governmentwide strategy or set of priorities guiding these programs. As a result, Congress charged the interagency TPCC[2] with developing such a strategy in the Export Enhancement Act of 1992. The act intended to set into motion a process, including an annual reporting requirement, through which the administration, working with Congress, can establish priorities for guiding export promotion efforts, reshape their programs to reflect those priorities, and marshal federal resources to fund them.

In September 1993, TPCC issued its first annual plan, "Toward a National Export Strategy," which is a status report on the TPCC's progress to date. The plan includes specific actions to improve the existing export promotion system in areas where TPCC was able to reach consensus. The plan also makes a firm commitment to establish governmentwide priorities and a unified export promotion budget within the context of the fiscal year 1995 budget. The Eximbank and its Chairman were actively involved in developing the TPCC plan.

One area of overlap specifically addressed by the TPCC plan involves the Eximbank's Working Capital Guarantee program[3] and

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[2]The Trade Promotion Coordinating Committee is an interagency committee created by the President in 1990 to address the government's decentralized approach to export promotion.

[3]The Working Capital Guarantee program was developed to meet the specific demand for pre-export financing for small businesses. This program encourages commercial lenders to make loans to small companies that have exporting potential but need funds to produce or market goods or services to export.

SBA's Export Revolving Line of Credit (ERLC).[4] The TPCC plan included a provision to harmonize and integrate ERLC with the Working Capital Guarantee program. Further, if SBA cannot resolve within a 1-year period the problems it has managing the ERLC program, the plan proposed to consolidate within the Eximbank all export finance assistance for working capital purposes. We believe that consolidating the two programs (should an evaluation show that SBA is unable to effectively manage its ERLC program) could not only improve small businesses' access to export financing but also could establish a precedent for reallocating resources across agencies based on each agency's comparative advantage. The plan did not address the overlap between Eximbank and Department of Agriculture programs.

TIED AID

Now I would like to turn to the issue of tied aid. The Eximbank is authorized by its legislation to establish a tied aid program to counteract the use of tied aid by other countries. "Tied aid" refers to foreign assistance that is linked to the purchase of exports from the country extending the assistance. U.S. trade policy has generally been opposed to tied aid and has sought to dissuade our competitors from using it through international negotiations. A 1992 agreement among 22 of the 24 members of the Organization for Economic Cooperation and Development (OECD) establishes guidelines to discourage the use of tied aid that would distort trade.[5] The agreement is meant to (1) restrict tied aid for commercially viable projects (primarily in advanced developing countries) by raising concessionality levels (the percentage of financing that is a grant or grant equivalent) and (2) increase transparency (openness) about tied aid use by strengthening notification and consultation procedures.

Under the terms of the agreement, a participating member country planning to use tied aid must notify OECD. Other member countries may challenge the notifying country's tied aid offer if they believe it does not meet the new OECD guidelines. Once challenged, the initiating country must justify the use of tied aid on

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[4]Through this program, SBA guarantees repayment of loans made by financial institutions to small businesses for export-related purposes. These purposes include financing working capital needed to manufacture products for export, to purchase goods or services for export, to develop foreign markets, or to finance foreign accounts receivables.

[5]OECD is a forum for monitoring economic trends and coordinating economic policy among its 24 member countries, which include the economically developed, free-market democracies of North America, Western Europe, and the Pacific. Although members of OECD, Iceland and Turkey have not signed OECD's tied aid agreement.

developmental grounds and show how the project does not meet the "commercial viability" test. A project is commercially viable if it is able to generate cash flow sufficient to cover the project's operating costs or can be financed by the private market or official export credits. If other countries are not satisfied with the justification, they may then make matching offers.

Although previous OECD agreements did little to reduce the use of tied aid, some U.S. officials believe that the new agreement will be more effective. Since the agreement went into effect in February 1992, Eximbank policy has been to use its "war chest"[6] only to police the agreement by selectively reacting against other countries' offers in cases where tied aid should not be used--particularly where consultations have not resulted in the withdrawal of a tied aid offer that has been considered inconsistent with the agreement. Although there have been seven derogations from the agreement since it went into effect, the Eximbank has made only one matching tied aid offer in that time period.[7]

U.S. exporters, Members of Congress, and others have expressed doubts about the effectiveness of this policy. The 1992 agreement has some built-in weaknesses and limitations. These problems include the difficulty of defining "commercially viable," and the presence of an "escape clause" that allows countries to proceed with a tied aid offer, despite objections by other participants, if that country claims that the project is in its national interest. Also, there are questions about the enforceability of the agreement because participation is voluntary and data are not confirmed or verified. Furthermore, even if a competitor's tied aid offer conforms to the rules of the agreement, it may still hurt U.S. exporters and U.S. economic interests. For example, the agreement still allows tied aid credits for a wide variety of capital goods, such as for large capital-intensive projects (railways or subway systems) with capital costs requiring longer-than-OECD arrangement terms.[8]

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[6]In 1986, Congress authorized the Eximbank to create a "war chest" fund to counter the use of tied aid credits by other countries.

[7]"Derogations" are cases in which the countries making the tied aid offers have proceeded with their offers, despite a decision by OECD agreement participants that the offers do not conform to the rules of the agreement.

[8]The OECD agreement includes guidelines for maximum repayment terms based on the category ("relatively rich," "intermediate" or "relatively poor") of the recipient country.

To deal with the issue of tied aid, the administration has recently proposed funding a $150-million aid fund to finance major capital projects overseas. The $150 million represents the subsidy component of the fund, which will support (under credit reform) $600 million in tied aid credits. The stated purpose of the capital projects aid fund is to combat other countries' use of tied aid. The Eximbank has been given the task of administering the fund, $50 million of which will come from the Eximbank's war chest, with the remaining $100 million coming from "proportional contributions" from the export promotion budgets of other TPCC agencies. But no criteria have been established for how the fund will be used.

During prior hearings, we stated that TPCC should identify the best industry and market candidates for trade promotion assistance as part of its methodology to establish priorities for federal trade promotion.[9] In so doing, the federal government would not be "picking winners and losers," but prudently setting priorities in order to ensure the best use of trade promotion funds. We believe it would be useful if the Eximbank were to follow a similar path in establishing criteria for using the new capital projects aid fund.

Well-developed criteria for using the tied aid fund are important because, as Eximbank officials have pointed out, there is a heavy price tag on providing tied aid credits. This high price accounts, in part, for the Eximbank's past reluctance to use its war chest. The Eximbank has not exhausted the full amount of its authorized annual war chest funds in any year since the war chest's creation in 1986 and did not use the war chest at all in fiscal year 1989. Using war chest funds takes scarce resources away from regular export credit financing. Due to the larger grant component in tied aid credits, they are much more expensive than regular export credit transactions under the terms of the Federal Credit Reform Act of 1990 as it applies to the Eximbank's budget.

CREDIT REFORM

According to the Eximbank's mission statement, its goal is, in part, to facilitate export financing of U.S. goods and services "by absorbing reasonable credit risks that are beyond the current reach of the private sector." Eximbank programs cover commercial and political risks. Because the Eximbank often provides financing for markets that the private sector is reluctant to enter, these markets tend to be riskier. The Eximbank regularly assesses country risk to help it determine the maximum amount of financing exposure (debt payments due) it should have in a market.

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[9]See Export Promotion: Initial Assessment of Governmentwide Strategic Plan (GAO/T-GGD-93-48, Sept. 29, 1993).

Before fiscal year 1992, Congress enacted loan limitations for the Eximbank that determined the maximum amount of loans, guarantees, and insurance it could extend. However, this situation changed with the passage of the Federal Credit Reform Act of 1990, which took effect at the beginning of fiscal year 1992. Under credit reform, the estimated total future costs of the Eximbank's annual transactions must be accounted for when the transactions are made, and are limited by the total amount appropriated for this activity.

With credit reform, when the Eximbank makes loans or guarantees for exports to "riskier" countries, such a decision costs the Eximbank more than credit activities for a less risky country. Consequently, credit activities for risky countries will have a greater impact than formerly on the Eximbank's ability to lend because credits to them take a bigger portion of that year's budget. For example, $1 billion in budget authority for the Eximbank may only support $2 billion in export loans, guarantees, and insurance for a very risky country. In comparison, the same $1 billion could support $10 billion in exports to a significantly less risky country.

Credit reform, in effect, increases congressional budgetary control over the Eximbank. Congress limits the maximum costs involved in potential transactions up front--during the budget process. However, until the Eximbank knows which countries will be borrowers under its program--and actual loans and guarantees are made--no one knows how much in exports a given authorized budget amount will actually support. To shed some light on this matter, the Eximbank has developed cost assumptions for the budget process to show the combinations of credits (loans, guarantees, and insurance) and country risks possible within Eximbank budget constraints.

DELIVERY OF SERVICES

In view of the growing demand for export finance, delivering services to exporters has become an important issue for the Eximbank. Responding to this demand has been made more difficult by the recent reluctance of U.S. commercial banks to provide export finance, particularly to small- and medium-sized businesses. A key challenge facing government policymakers is how to broaden commercial bank participation in export finance.

The Eximbank's service delivery network is limited, consisting of about 400 employees in Washington, D.C. (including staff for the Eximbank's insurance operation), and 5 new regional offices. The Eximbank uses commercial banks and federal, state, and local agencies to make its services available to as many exporters as possible. Some of the Eximbank's efforts to expand the delivery of its services include making changes to increase commercial banks' participation in its programs, initiating a city/state program, and using regional offices.

Eximbank and Commercial Banks

Perhaps the biggest challenge facing Eximbank is encouraging greater participation by commercial banks in export finance. The Eximbank traditionally has relied on the commercial banking system as its principal means to deliver financing--especially to smaller companies--through its loan guarantee programs. Yet in recent years, the Eximbank's ability to reach exporters has been restrained because commercial banks have been cutting back on their international departments. Some large banks have consolidated their overseas operations and reduced their less profitable lines of business, such as financing smaller transactions. The TPCC's Trade Finance Working Group reported (based on a study conducted in 1991) that the supply of export finance "falls well short of demand," particularly pre-export financing for sellers. According to the report, businesses across a wide range of sectors reported difficulties and even loss of export sales because they were unable to get the necessary financing.

Although one of the Eximbank's main goals is to expand the network of commercial banks that want to participate in its programs, the Eximbank included only 348 banks (out of a total of approximately 11,000 commercial banks in the United States) in 37 states on its bank referral list in 1993 (a list of banks that have expressed an interest in doing business with the Eximbank). Nevertheless, this amount represents 20 more banks than appeared on the Eximbank's 1992 bank referral list. The Eximbank has made efforts to inform more bankers about its programs, and offers training for bankers and others involved in export finance, and 1-, 2-, and 4-day seminars for exporters and bankers. During these seminars, Eximbank officials present information on Eximbank programs and other export financing available through the government.

Further, the Eximbank has enhanced its guarantee programs to attract and retain commercial banks. In fiscal year 1992, the Eximbank increased the interest coverage on new medium-term and long-term guarantee authorizations to 100 percent.

The City/State Program

In 1987, the Eximbank initiated a major effort--the city/state program--to improve the delivery of its services. The city/state program is a partnership between the Eximbank and city and state export finance and development agencies that allows exporters to access Eximbank programs through these city and state agencies. Currently, state or city agencies in 26 locations participate in the program. The city/state program benefits the Eximbank because the city/state participants screen exporters, package loans, and provide exporters with information about Eximbank and other government programs. Common attributes of the more active locations include adequate state or local funding and committed personnel with trade and finance expertise who serve as advocates for the less-experienced exporter.

However, the Eximbank faces some limitations with its city/state program: (1) the delivery of services varies between states in terms of outreach, existing networks, funds, and expertise; (2) the city and state participants need training and experience to use Eximbank programs and determine how best to meet exporters' needs; and (3) the state and local agencies are subject to changing administration priorities and budget constraints.

Nevertheless, the city/state program is an encouraging example of how federal and state or local agencies can work together to assist U.S. exporters. The TPCC plan recommended that the city/state program be expanded.

<u>Eximbank Regional Offices</u>

In 1992, the Eximbank took over the five regional offices (New York, Chicago, Miami, Los Angeles, and Houston) that had previously been administered by the Foreign Credit Insurance Association (FCIA) Management Company to market Eximbank insurance programs.[10] The Eximbank is now using these offices to market all of its programs--loans, guarantees, and insurance. The Eximbank has no overseas offices.

An interesting comparison can be made between the Eximbank's network and the networks of U.S. competitors' export credit agencies. For example, France offers a network of 22 domestic offices where exporters can obtain export finance assistance, but has no overseas offices. Japan's Export-Import Bank has 2 domestic offices and an overseas network with staff in 17 locations, including offices in New York City and Washington, D.C.

In order to improve the federal government's delivery of its export services, the TPCC plan proposed establishing one-stop shops to provide local export communities with a single point of contact for all federal export promotion and finance programs. The one-stop shops will primarily integrate representatives of the Department of Commerce, SBA, and/or the Eximbank. The first one-stop shops will be established in Baltimore, Chicago, Los Angeles, and Miami.

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[10]The Foreign Credit Insurance Association Management Company administered the Eximbank's export credit insurance program until September 1992, when the Eximbank cancelled its contract with the FCIA Management Company and began administering its insurance program in-house.

COMPETITIVENESS OF EXIMBANK SERVICES

In accordance with a congressional mandate, the Eximbank conducts an annual survey of its customers--bankers and exporters--who have had recent experience with Eximbank programs. The Eximbank then reports to Congress on the survey results. In a survey covering 1992, the Eximbank asked survey respondents to measure (1) the competitiveness of Eximbank support relative to the support offered by six competitors'[11] export credit agencies and (2) the success of the Eximbank in meeting the needs of the U.S. exporting community. Some discretion is necessary in reading the survey results pertaining to comparisons between the Eximbank and competitors' export credit agencies. As the Eximbank reported, many bankers and exporters are not really knowledgeable about competitors' programs, so their responses are often based on perceptions.

The key results of the survey were the following:

(1) Bankers and exporters who reported being familiar with the practices of foreign export credit agencies perceived France and Japan as having the most competitive programs overall. They considered U.S. (Eximbank) programs as being the least competitive in four of the six categories polled, including project risk support, local cost support, foreign content requirements, and tied aid availability.

(2) The chief complaint of exporters and bankers was the Eximbank's lengthy case-processing time. Almost half of the banks reported losing export transactions because of the Eximbank's "sluggishness." Another problem cited by exporters--particularly smaller businesses--was Eximbank paperwork requirements. One respondent noted that the financial statements required by the Eximbank for transactions under $1 million were "excessive and prohibitively expensive for small businesses to produce."

Identifying the problem areas is the first step in improving quality, and the Eximbank has done so by conducting its survey. With limited resources and serious budget constraints, meeting the growing needs of its customers will require planning and innovation on the Eximbank's part.

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Mr. Chairman, this concludes my prepared statement. I will be happy to try to answer any questions you or other Members of the Subcommittee may have.

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[11]France, Japan, Italy, Canada, Germany, and the United Kingdom.

RELATED GAO PRODUCTS

Export Promotion: Governmentwide Plan Contributes to Improvements (GAO/T-GGD-94-35, Oct. 26, 1993).

Export Promotion: Initial Assessment of Governmentwide Strategic Plan (GAO/T-GGD-93-48, Sept. 29, 1993).

Export Promotion: Governmentwide Strategy Needed for Federal Programs (GAO/T-GGD-93-7, Mar. 15, 1993).

Export Finance: The Role of the U.S. Export-Import Bank (GAO/GGD-93-39, Dec. 23, 1992).

Transition Series: International Trade Issues (GAO/OCG-93-11TR, Dec. 1992).

The U.S. Export-Import Bank: The Bank Provides Direct and Indirect Assistance to Small Businesses (GAO/GGD-92-105, Aug. 21, 1992).

Export Promotion: A Comparison of Programs in Five Industrialized Nations (GAO/GGD-92-97, June 22, 1992).

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