BUSINESSatOECD
THE BUSINESS AND INDUSTRY ADVISORY COMMITTEE

The future of the OECD Arrangement on Officially Supported Export Credits

Business priorities

Business at OECD strongly supports effective multilateral approaches to global challenges

The OECD, as a consensus based multilateral organisation, draws its strength from common goals and common rules. Today, effective multilateralism is more important than ever. Amid rising trade tensions, increased protectionist tendencies, and the changes associated with the digital transformation, multilateralism faces significant challenges. Business believes that the OECD has a vital role to play in ensuring the good governance of global markets. Indeed, this ongoing effort is essential for the efficiency and vitality of our economies.

The OECD Arrangement is an important tool in creating a level playing field in international markets

The OECD *Arrangement on Officially Supported Export Credits* (the Arrangement), in place since 1978, aims to foster a level playing field in the terms of export credits offered by Export Credit Agencies (ECAs). Competition amongst exporters is thereby based on the quality and price of goods and services, rather than on the favourability of the terms and conditions of accompanying financial support.

The OECD Arrangement does not operate in isolation, but as part of a wider rules-based system built in the past 60 years by the international finance community. This system includes both development finance and export finance, and includes institutions such as the IMF, Multilateral Development Banks (MDBs) and Development Finance Institutions (DFIs), the OECD Development Assistance Committee (DAC), the OECD, the Paris Club, and the WTO. The system is meant to ensure an orderly functioning of international markets.

Whilst starting with a technical focus, the Arrangement today has a strong and clear value base and promotes a rules-based international order. Step by step the horizon of all OECD activities has broadened towards sustainable growth. To the OECD, this is growth that balances economic, social, and environmental considerations with a long-term, global perspective. Generally, it refers to development that meets the needs of the present without compromising the ability of future generations to meet their own.

For the business community, the Arrangement has been an example of how a common goal can shape common rules for the benefit of all. However, the landscape has been changing, and those goals and rules have come under threat. The changing environment for global trade and investment has put increasing pressure on the Arrangement and in some cases undermined its ability to fulfil its purpose. However, the business community still believes that the OECD Arrangement is, and will continue to be, the best multilateral tool to ensure a global level playing field.

The landscape of global trade has changed…

China overtook the United States as the single largest exporter in 2014. By 2016 it accounted for the highest share of global exports at 17%, having grown from just 7% in 2002 (Eurostat). During this time major OECD economies, such as the United States, EU, and Japan have seen their share of global exports decline in relative terms.

Significantly, between 2011 and 2017, OECD Arrangement activity as a percentage of total trade-related official Medium and Long-Term support has fallen from more than 50 percent to 27 percent (EXIM, 2017 Competitiveness Report).

…putting pressure on the Arrangement

Today, unfair competition in the financing of exports is a reality facing many OECD based businesses. For years the Arrangement provided industry with the essential knowledge and comfort that competition was based on the quality of products and services. Innovation, usefulness, as well as cost efficiency, of a product were the drivers for succeeding against competitors. Financial strength did not pose the most decisive factor as, through the Arrangement, most market participants met on a level playing field.

Over the past two decades, businesses in our network have witnessed significant changes in this regard. New competitors have begun to successfully enter markets with attractive financing. For example, *Business at OECD* is aware of instances of export support from countries not bound by the Arrangement that are more generous than would be permitted under its terms. This situation is compounded by the fact that competitors from non-OECD countries often have cost advantages to those from OECD countries. It is compounded further where OECD countries refer to the Common Approaches for Officially Supported Export Credits for Environmental and Social Due Diligence, strict anti-bribery policies and sustainable debt, while non-OECD countries are sometimes less concerned by such rules and recommendations. This is critical, for example, for European Banks taking into account the great push forward in terms of Financing Sustainable Growth.[1] However, the OECD has been slow in reforming and enhancing the Arrangement to reflect this.

This has led to the introduction, by ECAs of participating countries, of financing products which may be seen as potentially circumventing the Arrangement. While business understands this reaction by member governments, it endangers the integrity of the Arrangement. It leads to unfair competition within the OECD and dilutes the benefits and merits of the OECD Arrangement.

Untied financing schemes, for example, are offered by various countries that technically do not fall under the Arrangement, and appear to be a reaction by OECD members to improve country competitiveness and promote national interest. Many programs use strategic sourcing of raw materials or other national interests as justification, versus exports. At the same time, the nature of the financing actors may be an issue in itself when driving prices too low. Direct lending by public entities on a non-Arrangement basis with subsidized funding is an example of this.

This demonstrates the strategic dilemma faced by OECD member countries in the context of uneven global competition. At the same time, these developments increase pressure on other members to create their own Arrangement breaching programs, and therefore further jeopardize

[1] See European Union's Action plan on Financing Sustainable Growth. Followed by three binding regulatory proposals that include heightened levels of requirements for financial market participants.

the level playing field. However, we understand that ECAs are looking to be more independent and sustain themselves; this meaning that in the long-term they are bound to provide a better service to export-oriented corporates and banks that participate in ECA backed deals.

Governments should seek to expand international agreement on these issues

OECD export credit disciplines, de facto and de jure, have failed to convince non-members to join the Arrangement on a voluntary basis. The International Working Group (IWG) offers a potential way forward, but progress has been very slow to date. Ultimately, more transparency on these deliberations is needed.

As IWG discussions develop we believe the OECD has an important role to play. Using the OECD Inclusive Framework on Base Erosion and Profit Shifting (BEPS), which brings together over 115 countries on policy collaboration and implementation as a model, the final results of the IWG could be housed under the OECD. Building on its deep well of expertise and strong reputation for evidence-based policy work, we believe the OECD would be an excellent candidate for hosting such an agreement in the future.

To make the Arrangement fit for the future we should return it to its core principles

Business believes that reconciling, and returning, to the core values of the OECD Arrangement is central to ensuring it can continue as a vital multilateral tool.

It is clear that the global context has changed since it was first adopted. In 1978, there were no non-members with sufficient financial capability to compete with member countries, let alone exceed them. Furthermore, available repayment terms for private financing have extended substantially and loans are more readily available.

As such, the time is right for Participants to consider a fundamental review of the Arrangement and the convening of the OECD Export Credits Forum is a good first step in this regard. In our view any future reformulation or replacement of the OECD Arrangement should be guided by a set of core principles:

- Be a consistent, predictable, and easily understood framework
- Be a strong force for promoting a global level playing field: eliminating financial competition, and respecting rules on financing sustainable growth and the transition to a low carbon economy
- Act to expand international consensus
- Be adaptable to changing realities in international markets
- Act to promote good business practice: reducing corruption, promoting competition, and supporting sustainable, long-term business relationships

While these core principles should guide any future review or update of the Arrangement, such a process may take a long time to complete, and is a long-term vision. A number of changes could be made to quickly improve the Arrangement. As the business community, we offer ‘spotlights’ on specific issues that currently hamper the effective functioning of the Arrangement from a private sector perspective, and offer recommendations to resolve them.

Spotlight: local costs

Business at OECD has highlighted for a number of years that current treatment of local costs does not reflect market realities. Developments such as localisation of manufacturing and services (including public procurement requirements), increased international sourcing, the lack of commercial long-term lending in local currency, and the changing role of ECAs, means change is needed. The traditional OECD ECA approach towards local costs does not reflect these developments and should be updated. Similar to internationalization of material sourcing having influenced ECA's foreign sub supplier policies, we strongly recommend adapting the Arrangement to reflect and support the growing industrial base in emerging markets. Specifically we call on governments to change Article 10.d of the OECD Arrangement as follows: "The Participants may provide official support for local costs, provided that: official support provided for local costs shall not exceed the export contract value."

In addition, the nature of construction export is such that building or infrastructure "products", such as roads, railways, ports, dams, hospitals, etc. are not exportable and therefore it is necessary for construction exporters to source construction materials, labour force and sometimes also equipment locally. Hence, *Business at OECD* calls upon the OECD to recognise in future amendments to the current Arrangement the fact that the export of engineering and construction services requires a much higher amount of local costs than of other goods and services.

Spotlight: flexible repayments

The positive experience with the various sector understandings and project finance rules underline the advantage of more flexible repayment terms, especially as the financial markets seem willing and able to support these.

Increased complexity in bringing into production a larger industrial plant, or commissioning an infrastructure investment, needs to be reflected in its financing terms.

A closer tying of repayment terms to expected revenues will enable investors to promote projects following the OECD core values of the OECD arrangement.

Instead of limiting the total tenor and setting strict rules on grace period and amortization (e.g. straight line/semi-annual instalments) we propose to regulate the average loan life. Besides introducing more flexible repayment terms, we also propose longer grace periods orientated alongside the expected revenues of a borrower.

For assets with a very long-life expectancy we propose to permit balloon structures which would not be fully amortized during loan life. This can especially support emerging markets in developing infrastructure. Additionally, we propose the reduction of down payments for developing countries. This will help such countries to finance large infrastructure projects.

Spotlight: matching

More flexibility in the Arrangement could be found by improving the ability to match specific offers from outside the Arrangement. Provisions for matching the terms of an offer, from both inside and outside the Arrangement, are written into the Arrangement under Article 45. However businesses report that this process remains difficult to follow in practice, especially in the case of matching with non-participants.

In particular the requirement that "the matching Participant shall make every effort to verify such terms and conditions" appears difficult for businesses to support in practice where terms and conditions may be confidential.

Ultimately, a quick and reliable matching process needs to be found. Doing so can send a strong signal to non-member countries and provide them with an incentive to join, or associate themselves with, the Arrangement. In order to ensure the stability and integrity of the Arrangement it will be essential to find an adequate notification mechanism amongst member countries.

Spotlight: aligning development finance and export credits

Business would like to engage in discussions on how export credits can serve their primary objective of supporting international trade, while additionally supporting the Sustainable Development Goals (SDGs). Therefore, better alignment of development finance and officially supported export credits with OECD member policy goals is important. As the world works towards meeting the SDGs, OECD members are emphasizing the importance of export finance, and appear keen to measure its development impact. As a result, OECD members should promote and enhance ongoing discussions with International Financial Institutions (IFIs) and Development Finance Institutions (DFIs) to develop a common set of eligibility criteria, categorization standards and incentive measures, aimed at fostering already existing synergies between ECAs and DFIs / IFIs.

This coordination effort will bring the additional benefit of protecting the level playing field and preventing commercial finance being crowded out by more explicit or implicit subsidies, such as blended finance, used by IFIs and DFIs. Going forward, it will be important to ensure the compatibility of rules on aid as set out in the Arrangement, and new and emerging rules on Official Development Assistance (ODA) from the OECD Development Assistance Committee (DAC). Specifically, there are a number of priorities for a future global framework for all official finance:

- Common risk-based pricing system for all forms of cross border trade- or investment-related official finance / guarantees.
- Common terms and conditions on maximum repayment periods, maximum grace periods, repayment profiles, minimum officially supported interest rates, maximum amounts for official support for all forms of cross border trade – and investment-related official finance/ guarantees.
- Common regulations on all forms of tied aid and (partially) untied aid (incl. ODA).
- Adequate and verifiable transparency on all forms of official finance with priority to (i) tied aid, (ii) export credits, (iii) untied development finance (multilateral and bilateral ODA and non-ODA), (iv) untied investment loans and guarantees and (v) other forms of official finance (e.g. equity investments).