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EXPORT CREDIT FINANCE

With special reference to EEC Countries

submitted for the degree of

Master of Philosophy

UNIVERSITY OF ASTON IN BIRMINGHAM

September 1978

EXPORT CREDIT FINANCE IN THE EUROPEAN ECONOMIC COMMUNITY

SUMMARY

This thesis reports on research investigating the rôle of finance in the United Kingdom's export trade, comparing it with finance for similar purposes in France, Western Germany and the Netherlands. In making these comparisons, it concentrates on those aspects of the foreign countries' systems which are different from the United Kingdom's and which are little known in this country. It also seeks to investigate the assistance given by the Governments of all four countries in the provision of finance.

Part 1 introduces the research, Part 2 the features of financing which are peculiar to the export trade.

Part 3 describes present practice in the United Kingdom and includes a review of developments in the past few decades which have led up to it. It is set in the context of international developments.

For each country, the relevant financial and credit insurance institutions are described, again concentrating on those features which are different from this country's. Short commentaries are added.

The investigation shows that in all countries short-term export finance is available on terms similar to those applying to other forms of short-term finance, while medium- and long-term finance attracts Government assistance. All

the countries have widened the sources of funds for this purpose.

It is found that more Government assistance is available to the United Kingdom exporter than his counterparts.

Part 4 discusses the financing needs of different types of market, the measures taken to curb "credit races", and finally discusses the relevance of interest rates to the securing of export business, expressing the opinion that its importance is usually exaggerated.

FOREWORD

Most of this thesis was written in the first half of 1977, but its completion has been delayed by protracted poor health. Although it has been possible to incorporate minor later developments, most of the information included does not go beyond that available in the first quarter of 1977.

September 1978

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PART 1

INTRODUCTION

CHAPTER 1

AIMS OF THE RESEARCH

The broad purpose of the research has been to examine the financing of visible exports from the United Kingdom and other European Economic Community countries.

It is widely accepted that the level of the United Kingdom's exports is inadequate to sustain an increased, or even stable, standard of living. While there may be some doubts as to the magnitude of the country's shortcomings in this respect, it is not proposed to dispute either the assertion of inadequacy or its importance. The questions which will be considered concern the rôle of finance in this country's export trade, particularly whether lack of finance, or its availability on less favourable terms than in competitor countries, has hindered the growth of United Kingdom exports. They will involve an examination of the systems in use in other countries and the United Kingdom, especially with regard to Government participation and assistance.

CHAPTER 2

SOURCES OF INFORMATION

Although there are surveys in English published by the Bank for International Settlements and the United Nations, both dated 1969 and not subsequently revised, there is little which has been published on comparisons of different countries' systems.

The principal sources used in this research have been annual reports, publicity and explanatory material published by international organisations, Government and other official organisations, and commercial and industrial concerns. These sources have been supplemented by interviews with appropriate personnel in a number of organisations, particularly in:

The British clearing banks at local, regional and national level,

Two British merchant banks,

The London offices of two major French banks,

The Head Office of a large, non-nationalised French bank,

The London offices of three major German banks,

The London office of one major Netherlands bank,

The commercial representatives of two foreign embassies in London,

A number of British industrial and commercial companies,

One trade association concerned with exporting,

Two French exporting companies;

One French University Management School,.

One firm of international accountants practising in the Federal Republic of Germany.

Information has also been sought by correspondence, sometimes as a follow-up to these interviews, sometimes from organisations not included in the foregoing list. There have also been numerous contacts at conferences and meetings, especially those arranged by the Institute of Export.

The choice of these organisations has been dictated by circumstances, especially the limited resources of time and finance which did not permit wide contacts with European organisations. Even in the United Kingdom, the companies interviewed cannot be claimed to represent a cross-section of the country's exporters. Nevertheless it is not thought that this leads to any seriously misleading conclusions, since the financing organisations interviewed cover a wide spectrum of United Kingdom exports.

To present a complete picture it would have been necessary to include non-exporting companies in the survey. The practical difficulties are enormous and the researcher believes that the inclusion of such companies would not have produced any new conclusions. The problem is one of identifying sufficient non-exporting companies whose sole or main impediment to exporting is lack of appropriate finance. Reports appear from time to time in the press that failure to obtain export finance is preventing a company from exporting, with the

Export Credits Guarantee Department usually being criticised. During the present research two such cases were reported in the local press, but contacting the companies produced no additional information - indeed it was indicated (with differing degrees of courtesy) that no useful purpose would be served by pursuing the matter. In such cases the Department correctly refuses to discuss individual applications, but claims that generally the project is not creditworthy for some valid reason. A banker also claimed that no creditworthy export business need be without finance [1]. Although ECGD and banking sources cannot be considered unprejudiced, the researcher is of the opinion that this view is broadly correct if one accepts that in marginal cases there is an element of subjective judgment in what is considered creditworthy. Putting blame on outside sources, such as financing institutions, may well be a (perhaps subconscious) excuse for failures within the organisation.

In addition to the sources already mentioned, substantial use has been made of news items in the press. The quality of the information obtained in this way is viewed with circumspection as the nature of newswork is such that compression and deadlines can give rise to false impressions. Nevertheless, since press items which report facts rather than views are normally taken from notices issued by the relevant organisations, no better published sources are likely to be available.

Information obtained from persons interviewed is also considered to be subject to distortion. Sometimes it has

been possible to contact an executive responsible for only a part of a company's foreign trade, and in the case of foreign nationals based in London there has sometimes been a period of some years since they were in close touch with their own organisations' domestic operations.

The accuracy of official figures is also open to question and it is doubtful whether all are correct to within the limits claimed. For instance, United Nations figures (based on national statistics) of exports from country A to country B frequently differ from B's imports from A, even when both countries have advanced reporting systems. The researcher does not consider this a serious drawback for the purpose of the present survey, but records it as an explanation for the use in the report of expressions such as "approximately", or "of the order of" in places where great accuracy is not essential or is not available.

CHAPTER 3

THE NATURE AND FORM OF THIS THESIS

To explain the format of this report one of the main findings must be anticipated. It is that in all of the countries studied the financing of exports presents no serious special problems to the exporter - a subjective impression is that one may say this of about 95% by value of all exports. There are, however, a number of features which in themselves are controversial, the subject of misunderstanding or are little known; the report seeks to identify these and offer comments. This has the inevitable result that they are given space which is wholly out of proportion to their importance in the overall picture of exporting. While standard institutions and procedures are mentioned for the sake of completeness, a knowledge of their operations is assumed and attention is drawn to less well documented areas. Thus, much more space is devoted to the mechanics of barter than to the procedures used in bill finance. This approach seems justified if it makes some contribution to clarifying misconceptions which undoubtedly exist.

The subject is viewed from an operational standpoint, though some reference will be made to macro-factors.

It has proved impossible to make many useful statistical comparisons. The difficulty is the common one of the lack

of strictly comparable data for all the countries. It also seems that misunderstandings in interpretation have arisen, especially in industrial circles, because systems in use in other countries have been assumed to be the exact equivalent of those used in the United Kingdom when in fact they are not. Some space is therefore devoted to a consideration of these different systems.

Part 2 of the report outlines the basic problems of export finance. It briefly summarises how these are dealt with in conventional financing procedures. It goes on to describe some less well-known methods in more detail.

Part 3 considers the financing of export business in four European countries. Given the aim of the study, the United Kingdom is the starting point. Chapter 6 not only summarises export finance practice, but also serves as a background to the description of the systems used in the other countries, as well as to the wider issues discussed in Part 4. The Federal Republic of Germany has been chosen as being the closest to the United Kingdom in its pattern of goods exported, also because its exporting successes invite investigation. France has a contrasting pattern of exports and financial institutions, and it was thought that a study of this country, together with a small one - the Netherlands, might throw additional light on the topic by including a variety of circumstances. The addition of further countries would have made the project unmanageable, and in most cases would have precluded the use of original source material

because of language problems. The chapters on these three countries describe their systems, drawing attention to the ways in which they differ from those of the United Kingdom.

The following conventions and practices have been used in presenting this report.

The anonymity of those interviewed has been respected. Some insisted on this, others indicated a preference not to be quoted personally. Although no surprising information was obtained from these sources, information given in this report is limited to indications of the nature of the organisation's activities when reference is made to facts and views which have been made available to the researcher.

Throughout the report, the note [1] refers to information obtained by personal contact with respondents, either orally or in writing. To the best of the researcher's knowledge it is not available in published form.

To minimise the repeated use of cumbersome expressions, "exporter", "banker", "financial controller" and similar descriptions refer to executives in responsible positions in the activities concerned. Their precise status is indicated only where the context demands.

Frequently-mentioned organisations and institutions are usually referred to, after their introduction, by the abbreviations which they themselves use.

PART 2

FUNDAMENTAL ISSUES

CHAPTER 4

CONVENTIONAL PROBLEMS AND PRACTICE IN EXPORT FINANCE

1. General.

Within a manufacturing firm's activities it is usually impossible to isolate completely those concerned with export markets from those concerned with the domestic market. Production facilities are usually common to both, many of the financial requirements are common, and the domestic and foreign marketing programmes should be integrated. This is especially true of multi-national companies, the financing of which is often considered an area of study in itself.

There is inevitably a certain arbitrariness in defining the boundaries of export finance. The areas traditionally covered by the literature on this subject comprise those features of export business posing problems which are additional to, or different from, those encountered in domestic markets, and these are the general lines which will be followed in this survey. Some features, particularly those concerned with pre-shipment finance and buyer credits (which are strictly import finance) will be included, in line with current practice. Import finance by way of bond issues, however, is excluded, as are other long-term funds such as equity and debenture issues; these are regarded as part of an organisation's overall corporate finance.

2. Basic problems in export finance.

The problems which distinguish export finance from the finance of domestic trade fall into two broad categories:

- those of a traditional commercial nature, being special difficulties which are not encountered to the same extent, or are not encountered at all, in domestic trade;
- needs of a society, normally expressed by Government action, which may wish to influence its trading relations with other societies.

In modern civilisations, Government activity affects so many aspects of life that it is not always possible to draw a hard and fast line between these categories. Nevertheless, there are some inherent inhibiting features of international trade from the businessman's point of view, and these are now summarised.

1. The period of time for which finance is required for a transaction is longer than for home trade business, because of

   - the customary period of credit in the foreign market;
   - longer transit time for goods;
   - the time required by the banking system to transfer the proceeds of sale.

   These factors increase the amount of finance required for a given turnover and also lengthen the period for which participants in international trade are exposed to the following risks.

2. The exporter is exposed to greater risks, which may be divided into:

commercial

- increased risk of loss or damage in transit;
- exchange risks:
    - if the sale is in the currency of the seller and the buyer's resources are in another currency, appreciation of the seller's currency may affect the ability of the buyer to pay, or
    - if the sale is not in the seller's currency, depreciation of the currency used will reduce the proceeds available to the seller;
    - conversely, the exporter may gain if events move in the opposite direction, but most exporters are more concerned with minimising the risk of loss than taking a chance on a gain;
- costs (physical distribution, marketing and possibly manufacturing) are likely to be higher, reducing profit margins;
- failure to solve marketing problems is more likely;
- the buyer is perceived as less creditworthy than a home trade buyer, because of real or supposed inferior standards of commercial morality, or because it is considered too difficult and time-consuming to obtain reasonable status reports;
- legal and other difficulties in applying pressure for repayment and in recovering bad debts;

politico-economic

- Government restrictions on payment for imports;
- restrictions on exports;
- outbreak of war or other hostilities.

Not all of these problems will be present to the same extent in every case - indeed, there will be many occasions when at least some of them will be entirely absent. Nevertheless, they are real problems inseparable from international business; over the centuries methods have been developed to minimise the risks and to alleviate losses if any misfortune should occur. As would be expected, uniform success has not been achieved, and separate consideration is given to each item.

3. Conventional practices in export finance.

With marine insurance established for centuries, it is possible to insure commercially against practically all risks of damage or loss in transit. While there are gaps in the cover available, these are negligible in the normal run of international trade. It is very rare indeed for any shipment not to be covered against damage in transit.

Fluctuations in exchange rates may be covered in most cases by forward contracts in foreign exchange markets, though this may be slightly more difficult to arrange in some exporting countries than it is in the United Kingdom. The availability of foreign exchange to the buyer is in practice controlled by the authorities in most importing countries, and there is

no commercially available means of safeguarding against the possibility of a buyer not being allowed to acquire the necessary foreign exchange to remit payment.

Costs of physical distribution and marketing will almost certainly be higher than in the domestic market. This is unavoidable.

The risks involved in marketing are often difficult to identify and virtually impossible to quantify. While this is an area which essentially concerns the exporter's competence in all facets of marketing, even the most able are likely to face a greater risk of failure in a foreign market than at home.

Of the commercial risks listed, there remain credit-worthiness and debt collection. Improved communications make the advance assessment of buyers' credit status much less of a problem than a generation ago, and the difficulties are often exaggerated in the eyes of a potential exporter. Even so, uncertainties do exist and over many years payment practices and mechanisms have been evolved affording different degrees of security to both seller and buyer, usually using banks as intermediaries.

Risk may be reduced by the use of Bills of Exchange, the status of which is clearly defined in all legal systems based on those of established trading nations. While it must be admitted that in some markets practical difficulties are found when it comes to applying the law, bills offer greater

security than open account trading, and for still greater safety the conditions under which a bill is negotiated may be rigidly specified (though at some additional cost) by the terms of a letter of credit. The bill may simply be used as a mechanism for debt collection or, because of its negotiable nature, as a means of securing finance. As these are well-established procedures they are not discussed further in this report.

Perceived risks of buyer and seller are also increased or diminished by the time at which payment is made, irrespective of the mechanisms used. It will ultimately depend on the relative power of the buyer and seller, and of other members of the distribution channel (including financing institutions), subject to any over-riding regulations which may be in force. "Cash with order" is clearly the most advantageous to the seller, but is so disadvantageous to the buyer, who must not only forego working capital but also run the risk of late or non-delivery, that he is likely to agree to this only in exceptional circumstances. To a less extent, the same comments apply to "cash before shipment".

In practice, these terms are rarely met in isolation. They are commonly used as part payments, especially with orders for capital equipment, where commonly used terms are "10% with order, 10% before shipment..." While "cash with order" in the case of small orders is probably seen more as risk minimisation than as providing the exporter with finance, in the case of capital goods there is an element of both: the advance payment provides some working capital for the

for the construction of the equipment and also makes it unlikely that the buyer will refuse to take up the order when ready.

Payment at some specified time after shipment is the usual condition. In the case of capital equipment, the payment may be made in instalments over a number of years, especially when the buyer is unable to obtain capital himself because of the weakness of his own currency or ill-developed capital markets in his own country.

With the exception of capital goods, when some negotiation may be expected, the appropriate time for payment has been established by custom in most trades. It will only be altered in case of a major change in circumstances, e.g. shortage of supply. (A little-known but striking example of this is the British Steel Corporation's payment of £25m in advance, to secure supplies of Polish coal over the next fourteen years [2]).

CHAPTER 5

SOME LESS CONVENTIONAL PRACTICES IN EXPORT FINANCE

While all trade, whether between individuals or organisations, ultimately comes down to the exchange of goods and services, their straightforward exchange without the intervention of money and the financial institutions which process it is generally considered rudimentary and not typical of an advanced society. In the words of a well-known textbook, "in all but the most primitive cultures men do not directly exchange one good for another" [3]. Nevertheless, it should be recognised that international business is in fact conducted on non-conventional financial terms which are not far removed from the basic concept of barter, or direct exchange.

Transactions avoiding the use of finance which can be freely exchanged for goods and services cover an infinite range of possibilities. However, they tend to fall into certain broad categories, generally referred to as barter, compensation, bilateral and switch trading, though terminology varies, reflecting the difficulty of establishing clear-cut divisions. Indeed it is also sometimes difficult to see a clear distinction between switch trading and "conventional" financing, constrained as the latter usually is by licensing regulations, quotas and other restrictions.

Barter in international trade is the straightforward exchange of goods or services without payment crossing national frontiers. Payment is made to each of the suppliers in his own currency by an intermediary, probably a Government department or other official organisation, acting through banks. It is probably fairly unusual in the United Kingdom, though it undoubtedly takes place rather more often than the general business world realises. Commodities for tractors, bicycles for chemicals, and spare parts for machinery have been reported [1]. A more complex form of barter deal was reported a few years ago between Switzerland and Czechoslovakia. At the time, the latter country had no hard currency available and paid for the import of instruments to be used in its electrical industry by supplying surplus electric current to Switzerland via Germany and Austria [4]. Barter transactions recorded by United States sources include Turkish chrome ore for American wheat and car components, and Indian ore for Italian fertiliser [5]. In the autumn of 1974 the West German press widely reported negotiations between the Federal Republic and the USSR for the provision of German pipelines to be paid for by supplying electric current to West Berlin, though details had still not been finalised in March 1976.

An earlier instance of a substantial barter deal is provided by Gloster Aircraft agreeing to accept cotton from Brazil in 1952. Although this happened so long ago it still provides a good example of the way in which barter may distort conventional trade. It was alleged that the agreement upset the cotton market and also gave Gloster an unfair advantage

over other creditors by taking all the proceeds of the cotton sale which would otherwise have been available to repay some of the estimated £40m - £50m then owed to United Kingdom exporters [6].

Electricity is regularly supplied to France from the United Kingdom at French peak hours, and in the reverse direction at British peak hours. Payment is made for net sales. It would be an exaggeration to regard this as a barter deal in the spirit of the others mentioned, but it does illustrate the problem of where to draw the line between one form of trade and another.

Compensation transactions also involve the exchange of goods against goods, although a form of payment is involved. One method is for a supplier from a hard-currency country to buy goods, say carpets from Jugoslavia, and pay the carpet supplier in hard currency. The carpet exporter will then offer the hard currency to an importer of Swiss watches, but will charge a substantial premium over the official exchange rate since currency allocations are not available for the import of luxury goods [7].

It is sometimes difficult to distinguish clearly between barter transactions and bilateral trade, especially when one or both parties is a Government department or other official body, as is often the case. The archetypal bilateral trading arrangement would be an agreement negotiated between two countries which jointly establish a clearing account, usually

with a "swing balance" to accommodate fluctuations in trade. This is normally denominated in a hard currency for the sake of convenience, say United States dollars, but the "clearing" dollar balances are of course not convertible in internationaal markets. (To avoid offending political susceptibilities, the clearing may be denominated in neutral units of accoutn, e.g. the Verrechnungs-Einheiten (VE) for trade between the two German republics, but as a matter of practical necessity they must be linked to some widely traded currency or currencies.) The exporter receives payment in his own currency, the importer pays in his own currency, with the central banks or other appointed organisation keeping the accounts and making payments across the frontier only if the balance exceeds the agreed swing. The details are obviously capable of infinite variation, depending on the circumstances.

In reality, matters do not always work out as simply as this. It is much easier in theory than in practice to keep trade in balance. When goods traded are susceptible to interruptions or variations in supply - crop forecasts cannot be completely accurate, inadequate transport systems break down, political unrest occurs, or industrial production falls - country A becomes a creditor of country B. Country B cannot meet its obligations by supplying goods needed by A and in spite of the provisions of the bilateral agreement fails to pay in gold or hard currency to meet the deficit - in this situation it may be possible to arrange a "switch" deal.

The countries concerned may agree to this switch trading to rectify the imbalance. Country A imports goods from a hard currency country, with payment made by B in a hard currency.

It seems at first sight strange that B should be willing to do this when it is unwilling to pay A direct. The reason is that a premium is arranged: for every $100 paid by B, A will pay an agreed percentage in clearing currency, say $105. While there was no intention of effecting such transactions when the agreement was concluded, the clearing balance has reached such a state that A is unable to use its clearing currency credit with B, as the latter is unable to supply goods and services which it needs. Rather than have these unutilised clearing balances, A is willing to concede a part of its claims on B in order to obtain goods from hard currency sources.

Another way of resolving the imbalance is for creditor country A to buy from B goods for which it has an outlet in a third country able and willing to pay A in a hard currency. A then sells the hard currency it receives to B at a premium in clearing currency.

These examples suggest that the initiative comes from one or both countries with the clearing agreement. It may equally emanate from a third, hard currency, country. Here an exporter may be willing to accept payment in clearing currency from debtor country B against shipment of goods to creditor country A if he knows (or believes) he can sell the clearing currency to a third party who wishes to buy goods from B. The sale of clearing currency will be at a discount against the convertible currency.

A summary of a procedure which would be typical in such a transaction illustrates the complexity of such a deal.

- An importer in a country with an unused surplus on a clearing agreement obtains a licence from its exchange control authority allowing it to import equipment from a hard currency source, payment being made from the clearing balance.
- A licence from the debtor country is also obtained. (This implies that agreement between the two clearing partners can be obtained.)
- A banker's credit denominated in clearing currency is opened in favour of an intermediary or clearing currency dealer.
- The latter opens a letter of credit in favour of the hard currency exporter, denominated in hard currency.
- The exporter obtains payment after shipment in accordance with the terms of the letter of credit, debiting the clearing currency dealer's account.
- On arrival of the equipment, the clearing country importer pays the bank in his own currency. The bank in turn releases the clearing account in the debtor country to the foreign exchange dealer.
- With these funds, the foreign exchange dealer either buys goods for export from the debtor country or sells them to another trader who has a market for such goods. [8]

If one adds to these complexities the problems concerned with timing, transit, finance for the foreign exchange dealer whilst awaiting completion of the transaction, plus legal aspects of ownership at different stages of the transaction, the danger

of alterations in exchange control regulations, to say nothing of appropriate trustworthy contacts and outlets for commodities for which there is little demand (otherwise they would be sold on world markets for hard currency) it will be realised that this type of trade is for experts. It is virtually impossible for a manufacturer of, say, capital equipment in the United Kingdom to have the necessary volume of business to contemplate such transactions without the intervention of a specialist intermediary. During the current research, a company having annual exports running into nine figures sterling reported that it left all such matters to outside specialists. In another case, the United Kingdom group of a multi-national organisation (UK exports well into eight figures sterling) leaves these matters entirely to its merchant bank. Yet another subsidiary of a multi-national organisation (UK exports again in eight figures sterling) which has substantial experience of non-conventional financing cannot manage without such intermediaries [1].

The complexity of the operations inevitably brings high costs in its wake. Commissions and trading profit on the sale of goods imported and exported, bank charges, discounts or premiums on clearing currencies all have to be covered. These costs, especially the commissions and premiums on currency conversions may seem extortionate, but they are accepted, even by countries which for ideological reasons have in the past deplored the existence of parasitic middlemen.

In fact, these expenses are not necessarily unreasonable. The countries which feel themselves forced into this form of

trading by their economic weakness invariably have currencies which are not traded on world markets, and exchange rates at which clearing dollars or other hard currency are converted are at best no more than estimates of the appropriate values. Thus a good which is traded at $100 (clearing) might well be traded at a very different level in convertible dollars. In the end, it may well be that a surplus on the clearing balance will bear a disproportionate amount of the distortion introduced by the use of inappropriate exchange rates used in the bilateral agreements, but in the overall trade between the two clearing countries it is not necessarily unjustified. In another case, it may well be that a country can offer nothing more than commodities for which there is no regular trade on world markets and cannot therefore be have an accepted value in any currency; again, the final switch could be regarded as an adjustment to whatever value was assigned to the commodity.

For the intermediaries, there are undoubtedly substantial profits to be made. The greater the imbalance between clearing partners, the greater the need for the creditor country to find a means of using its surplus and, generally, the greater the discount he will be willing to concede. However, the more developed this type of trade becomes, the more opportunity there is for a knowledgeable intermediary to find a counter-party in some other part of the world. This has given rise to a market in blocked currencies, so that practices more closely resemble those of conventional trade.

The full extent of these barter and near-barter deals is not known, The fact that there is a very limited number of traders in this field, located mainly in Vienna (where for

historical reasons there are trading, cultural and even family connections with Comecon and Western countries), Zurich (as a financial centre with relatively few official restrictions) and, probably to a smaller extent, in London and Amsterdam, suggests that as a percentage of world trade it must be very small. Less developed countries move into and out of bilateral and similar forms of trading according to the state of their trade and currencies. The more their trade develops, the more their currencies become acceptable in the unofficial markets; with continued success they achieve acceptability in official markets and withdraw from these forms of trading.

Attempts to quantify trade of this kind are doomed to failure. While isolated figures have been quoted, as far as it has been possible to ascertain countries do not normally publish figures of unused balances on bilateral trade which might be diverted to switch trading. Although details of bilateral agreements are published, they must be regarded as unreliable as the quotas are often not achieved. It is more realistic to regard them as optimistic targets.

An additional problem is that though switch deals have to be done with the official approval of one or both clearing countries, there are ways of circumventing restrictions. Only the naïf will believe that in countries where it is standard practice to pay officials a recognised sum even for carrying out normal duties like clearing goods through customs it is impossible to buy collaboration in breaking regulations. This is not the place to discuss the reasons for the existence of these practices, but the following account illustrates what can happen.

The Creditanstalt, Austria's largest bank, refused to pay against a letter of credit it had opened in London. It is the underlying facts rather than the legal issues which now concern us. A spot check by customs officials in Zurich showed that cases supposedly containing £1.9m worth of antibiotics actually contained rubbish. The consignment was part of a £10m Netherlands-Jugoslavia transaction negotiated through Vienna. The consignee was not reported to have complained at the deception. This may have been due to lack of interest on the part of the financial press, but since at least one paper followed up the story this is unlikely. A report some time later stated that the missing drugs were in Belgium at the Laboratoires Piette, which had, incidentally, received the drug from a Swiss manufacturer. It had also issued a Certificate of Conformity. André Piette suggested that his firm's original document might have been misused to cover a currency export deal: "It is well known that large shipments of 'medicaments' of all kinds go to Liberia and Middle East countries, only to be thrown away, as part of deals for transferring currency." The implications are obvious, though whether the proceeds were destined for a private account in Switzerland or elsewhere, or whether they were intended to be switched to some other trade is a matter of conjecture. [9]

There can be little doubt that many millions of pounds are transferred in similar non-conventional deals. In relation to the totality of world trade such activities are probably of little significance. Not only is the percentage of trade which it represents likely to be small, but in so far as these evasions of official regulations are for the purpose of switch

trading, their effect is to divert rather than curtail trade. The choice of goods to be imported rests with the trader rather than with the government.

For individual companies trading with these markets these deals may be important. This refers not only to intermediaries who make large profits if they are successful, but also to manufacturers whose exports may be financed in this way, probably without their knowledge.

Notwithstanding the small percentage of business financed by barter and similar transactions, its importance may well grow. The examples at the beginning of this chapter show that goods and services bartered are not necessarily those of "primitive cultures." Although one might hope that an expansion of trade and the development of greater sophistication in switch deals would naturally lead to full convertibility of the currencies used, one important group of countries is stressing more and more its liking for bilateral agreements. These are the Eastern European socialist countries. While they do not contribute a large proportion of the trade of the countries studied, they have sufficient potential to justify special consideration. This is discussed in more detail in Chapter 12. Suffice it to say at this stage that United Kingdom exporters are less willing or able than others to participate in this and similar forms of trading.

PART 3

COUNTRY REPORTS

CHAPTER 6

UNITED KINGDOM

1. Export financing institutions and practices

1.1 Clearing Banks

The principal external source of export finance is the exporter's own clearing bank. For longer term credits clearing banks may participate in syndicated loans, usually arranged by merchant banks. Types of finance offered are summarised below; the terminology is that of one of the clearing banks, some of the terms being based on those of the Export Credits Guarantee Department (ECGD).

- Simple overdraft at the bank's current rate for the exporter. This is indistinguishable from his overdraft for general purposes and in practice may have become part of the exporter's "core" finance.

- Advance against an agreed percentage of bills of exchange on approved buyers, held by the bank as collateral security.

- Discounting bills of exchange on approved buyers, either for retention in the bank's portfolio or for re-sale in the money market. Some bank managers prefer to provide finance by discounting bills, since these transactions are self-liquidating and there is no danger of the funds becoming tied up in the general running of the customer's business. Other bank managers have no preference for any one method. Compared with overdrafts and advances, there

may be some slight difference in cost but all consulted agreed that it was negligible. In practice a bank will offer discounting facilities only if relevant ECGD policies are assigned to it.

- Shorter term finance up to six months, where goods are exported on open account. Advances may be up to 90% of the amount due to the exporter and are made at the bank's base rate + 0.5%. This is available only when an ECGD direct guarantee to the bank is in force.

- Shorter term finance (bills or notes) up to two years against bills accepted by the buyer or the buyer's promissory notes. Advances may be up to 100% of the amount due to the exporter and are at the bank's base rate + 0.5%. This is available only when an ECGD guarantee to the bank is in force.

- Medium term finance from 2 to 5 years after shipment against bills accepted by the buyer or the buyer's promissory notes. This is available only when an ECGD guarantee to the bank is in force. A rate of interest determined by Government policy and fixed for the duration of the loan is charged.

- By arrangement with an overseas bank, a clearing bank may "confirm" the overseas bank's credit in favour of an exporter. In those cases where the United Kingdom bank is authorised to pay on presentation of documents, it is its own funds which are being used, though strictly it is financing the importer in such a situation.

- Medium term buyer finance from 2 to 5 years. Advances of up to 80% of the contract value are made to the foreign buyer or his bank. This is available only when an ECGD

guarantee to the bank is in force, the exporter paying the premium. A rate of interest determined by Government policy and fixed for the duration of the loan is charged.

- Financial guarantees, sometimes known as project finance, are similar to the medium term buyer finance, except that the amounts loaned are larger, the term is from 5 to 15 years, and it is usual for more than one bank to participate in the loan.

- Lines of credit are made available to overseas buyers or their banks on similar conditions to medium term buyer finance. They may be used for the purchase of a range of capital goods, often from different suppliers. The proportion of the contract value which may be advanced is determined for each contract, but is usually 80% - 85%.

- Pre-shipment finance may be provided on a selective basis when contracts are valued at £1m or more, otherwise pre-shipment finance is from the exporter's own resources or overdraft. The appropriate ECGD guarantee is required for this facility, which so far has been little used.

The clearing banks' main rôle is the provision of finance as just summarised. They apply normal banking criteria and exercise the maximum of prudence in making these facilities available. They minimise their risks by taking the usual collateral security or the specialised security for export business provided by ECGD policies. It will have been seen that these are essential for most of the financing methods listed and further comment is offered in the section dealing with the Department. In common with banks in other countries,

and their credit insurance organisations, they may also require guarantees or endorsements from commercial or central banks, as well as guarantees appropriate to a particular industry.

In addition to financing the exporter or importer direct, clearing banks are the principal source of funds used by a number of specialist organisations which are also engaged in export financing. Due to the pre-eminence of London as the financial centre for international trade in the nineteenth and early twentieth century, which encouraged specialising in limited trades or functions, the United Kingdom has a greater variety of such institutions than the researcher has encountered elsewhere. They may be divided into the following broad categories.

1.2 Export merchants.

Strictly, export merchants use their own knowledge of markets and sources of supply to trade on their own account, and should therefore be classified as exporters in their own right rather than as financing institutions. They tend to specialise in trade with certain countries and in certain types of merchandise. There are some who buy goods from manufacturers and re-invoice to the importer, their rôle being known to, and accepted by, both these parties. These cases are not common, but when they are met the effective part of the export merchant is as a provider of finance (whatever his legal status in the transaction).

1.3 Manufacturer's agent. In international trade "agent" is not synonymous in common parlance with the term as understood

in English law. Agents obtain orders, possibly arrange shipping, obtain necessary licences and perform other functions on behalf of the exporting manufacturers. They may be domiciled in the United Kingdom or, more usual nowadays, in the importing countries. In many cases they pay the manufacturer and extend credit to their buyers.

1.4 Buying agents.

Strictly, buying agents are not concerned with export finance, but sometimes arrange finance for their overseas principals. Their part in United Kingdom exports is very small, unless one includes confirming houses in this category.

1.5 Confirming Houses.

There is confusion over the rôle of these institutions. The British Export Houses Association(BEHA) regards them as "primarily a financing and credit giving service" [10]. The Midland Bank says "These organisations obtain orders for goods from overseas buyers, place them with manufacturers and usually attend to the shipping arrangements. A confirming house, like an export merchant, may undertake responsibility for payment... and itself extend credit to the overseas importer" [11]. Exporters often tend to regard confirming houses as their own agents, so long have established connections existed. Even so, there is little doubt that they act more on behalf of the overseas importer than the United Kingdom exporter, who may find to his surprise that the confirming house is also dealing in competitors' goods. A legal authority says the term "confirming house" has no definite meaning in law or commercial practice [12].

Different parties to a transaction may regard the rôle of the confirming house in different ways. In one case an exporter who used his own sales agent in New Zealand found the confirming house an unnecessary stage in the distribution channel and suggested to a New Zealand importer that all financial and shipping matters be handled direct. The importer would have been glad to accept the credit terms offered and thereby save the confirming charges, but found the confirming house essential for the sole purpose of co-ordinating shipments and for progress chasing in the United Kingdom. Neither the exporter nor the importer found the confirming house useful from the financial standpoint [1].

Overseas companies which originally relied on confirming houses for their finance may well continue to do so as a matter of convenience, but do not regard it as very important. With the growth of local banking facilities and improved international availability of credit information, other sources of finance are now accessible.

Yet in other cases, the confirming house continues to play a vital part in trade. Without the extension of credit to the buyer, through its overseas branches or associates, there would be no business for the exporter. Without the consolidation of a number of small orders into one shipment, transport and financial charges would be exorbitant.

1.6 Factors.

Factors buy sellers' claims on buyers, keep the ledgers and collect payment; in return they receive a fee based on

turnover. They may also advance funds to the seller, usually up to 80% of the face value of collectable items. Interest rates are based on bank base rates with a surcharge to cover services.

An estimate of the part played by these institutions as providers of finance is difficult. Even in those cases where funds are advanced, it is not clear whether access to finance is the main reason why the service is used. In exports funds are advanced by factors in far fewer cases than in domestic trade. A factoring company's internal records show that in 1974 85% of the company's domestic business included the provision of finance against 30% of the export business [1]. The problem of assessment is analogous to that mentioned under confirming houses - which service in the "package" offered by the factor is considered important by the user? An executive of one major factoring company was not sure, but thought that his company's ability to handle turnover of £300,000 a year (at 1975 prices) more competently and economically than an exporter was the main reason. This particular company, which (like its competitors) operates with associates in importing countries, has computerised its operations and claims to be able to obtain credit information from abroad more quickly than ECGD (though it has still taken out an ECGD policy itself!). Its procedures also enable reminders to be sent to importers whose accounts are overdue, in accordance with the language and customs of the country (for instance, different wording is used in different English-speaking countries to conform with local customs and law).

One factoring company's unpublished figures and estimates of that company's share of the factoring market suggest that in 1974 well under 0.5% of United Kingdom exports were factored. If the company's experience was typical of the factoring business as a whole, then only one-third of this will have been financed. It is the researcher's view that the finance will have been obtained by the exporter as a matter of convenience instead of having separate transactions with his bank.

In considering factoring as a source of finance, it should be regarded as an alternative rather than as an additional source. It has been known for bank overdraft limits to be cut when factoring facilities have been granted to exporters, the reduction being equal to the amount of the new facilities in some cases.

Several bank managers were asked "If one of your clients were up to his overdraft limit and then obtained a financing facility from a factor, would you call in part of the overdraft?" Without exception, though with differing degrees of certainty, they said they would; they also expressed the view that this would be the general reaction of most bank managers [1].

1.7 Export Finance Houses.

According to BEHA an export finance house is a company having as its principal function the provision of medium or long term credit, principally for capital goods [10]. It serves mainly the buyer and receives from him payment of charges and interest, sometimes separately from payment for the goods. This is in line with the traditional view of the export finance

house - one which uses its knowledge of overseas markets and of domestic financial markets to take responsibility for all financial aspects of a transaction, including the risk.

The actual situation is not so clearly defined as this view might suggest. As far as purely financial matters are concerned, Syrett and Pither comment: "The operations of the finance houses vary considerably from each other. Some supply finance on a recourse basis, others on a non-recourse basis. Some require the credit insurance cover of the Export Credits Guarantee Department, others do not. On some occasions there is access to the preferential interest rate finance of the clearing banks, on other occasions there is not" [13]. From the limited contacts which it has been possible to make, it seems that if there has been any change since this was written in 1971 it is towards greater reliance on ECGD cover, with a consequent reduction in the level of risk borne by the finance houses.

A Civil Servant in close touch with export work suggested that there was only one of the traditional export finance houses left. Yet an examination of its reports and accounts shows that of the bills receivable from financing international trade, only about 5% have more than one year to run - so much for BEHA's medium and long term finance! (Other debtors shown in the balance sheet could alter the picture, but it is unlikely that medium and long term debts would not be by way of bills. The more likely explanation of other debtors is that they refer to domestic business and short term export

transactions.) Further investigation showed that nearly one-third of the equity is held by one of the clearing banks.

Other export finance houses are connected with clearing banks, and it has been suggested that this is a reason for their decreasing inclination to accept the risk element in financing export trade [1].

In general terms, the facilities provided by export finance houses may be said to put the exporter in a similar position to that provided under clearing bank finance. From an exporter's viewpoint, they offer the advantage that ECGD's minimum contract value under their medium term finance arrangement is not necessarily applied. The overall cost of the facility will probably be higher. Charges vary and may be, for example, 2% over base rate plus a flat rate charge of anywhere between 1% and 5%. All charges are payable by the overseas buyer. A commission or discount may be received from the exporter, and this passed on to the buyer in the form of a reduced price or reduced interest rate [14]. (See also comments on "loading" on page 205 of this report.)

1.8 Leasing and Hire-purchase finance houses.

Specialist finance companies, usually subsidiaries or associates of banks, arrange leasing and hire purchase contracts, usually in association with similar institutions in the importing countries, sometimes through "off-shore" organisations. Though it is claimed that leasing is increasing rapidly in the United Kingdom, this method of financing capital investment seems to be less attractive in most importing countries. No

evidence has been found of leasing and hire-purchase playing a significant part in United Kingdom exports.

1.9 Merchant banks.

Acceptance credits were originally the main business of the merchant banks, and still constitute what one merchant banker described as their bread and butter business [1]. By arrangement with overseas importers or export houses in the United Kingdom, a merchant bank accepts bills of exchange which are then discounted in the London bill market. The traditional "Bill on London" is widely used as an investment for short-term funds by British, international and foreign banks, and because of the standing of the acceptors command keen rates. In the last decade or two, clearing banks and international banks have made some incursions into this business.

Since the mid-1950s there has been a marked trend for certain merchant banks to undertake the arrangement of medium and long term export credits. They are responsible for negotiating financial terms satisfactory to buyer and seller, co-ordinating the facilities provided by the clearing banks and other sources of finance, and for negotiating with ECGD. They do not operate on a fixed scale of charges, their fee depending on the complexity of the arrangements.

One merchant banker commented that he could not understand why the clearing banks did not do the work themselves, because the attractive part of the business was the management fee. The finance under the preferential interest scheme was provided entirely by them, they had the necessary knowledge,

yet they left this lucrative business to the merchant banks. A senior clearing house banker suggested that the explanation lay in the conservative training and personalities of clearing bank staff. He agreed that the merchant bankers knew nothing which was not known in the clearing banks [1]. It is, of course, a matter of common knowledge that the clearing banks now have links with merchant banks; the latter will probably remain nominally independent, but come more and more under the control of the parent bank.

1.10 Overseas banks.

Overseas banks may provide facilities for overseas importers, usually by accepting Bills of Exchange which are then negotiated in financial markets. This may be done by general agreement between the parties or, more usually, by the more formal means of a Letter of Credit.

1.11 Foreign banks and consortia.

Overseas banks are usually taken to refer to long-established banks which have participated in the financing of exports to traditional markets. Other foreign banks have not been so concerned with international trade as with purely financial operations, but since the growth of Euro-currency trading started many have been involved in the provision of loans for front-end financing. It must be supposed that if the United Kingdom Government is successful in persuading exporters and their advisers to arrange medium and long term credits in foreign currencies, these banks will participate more actively than when ECGD direct guarantees were available only to the clearing banks. Information from German banking sources

confirmed that German funds are being used in syndicated loans, both for United Kingdom and other exports. United States banks in London are active in seeking export finance business and it is assumed that banks of other nationalities are also interested in this type of business. One Swiss bank has started up a small subsidiary company which was sounding out the market for non-recourse financing similar to "à forfait" financing, as described under the Federal Republic of Germany (pp 137 ff). [1]

1.12 Further comments on export houses.

In the foregoing classification, clearing banks are considered first, since they form the principal source of export finance. The remainder, as listed, make a rough progression from the trading concern to the purely financial. While convenient, such a classification can be misleading. Since the researcher has found that there is misunderstanding in academic and non-exporting business circles about the nature of export houses and their work, some further comments are offered.

The lines of demarcation between all of the categories (including the clearing, overseas and foreign banks) are by no means as clear cut as the descriptions under 1.1 - 1.11 might suggest. Clearing, and some non-clearing, banks issue market surveys and provide trading information. One clearing bank, announcing the formation of a subsidiary to provide export finance in 1964, stated it would "see to the collection of goods from the supplier and their delivery to the buyer" and would "include the financing of goods in approved cases, if required" [15].

Nevertheless, in spite of these small incursions into marketing research and other non-financial functions, the banks generally concentrate on the provision and organisation of finance. It is those institutions listed under 1.2 to 1.7 where the divisions are blurred. One company "fulfills certain merchanting and confirming house functions as part of its general export finance house operations" [16], another finance house can provide "many other services...to meet the growing needs of international traders such as documentation, insurance, freight, transport and advice on markets" [17]. In the Directory of British Export Houses, an exporter with a substantial turnover is listed as a confirming house, defined as having a predominantly financing function, although it carries out other export functions on a considerable scale. Some very small firms are listed as carrying out six functions - perhaps to give an exaggerated impression of their importance in some cases, but in other cases they will carry out a limited number of transactions in all the listed activities in very specialised markets.

It is not only that demarcation lines between types of institution are not clear - within companies there is often no sharp distinction between departments. It is quite normal for a single delivery of mail handled by a single executive to include transactions on one or more of a merchanting, buying agency, selling agency or confirming basis. An export house (a deliberately imprecise term to cover all commercial activities concerned with exporting) normally prides itself on its flexibility and adapts to circumstances.

This diffusion of activities, both within and among companies, renders the traditional nomenclature of the different types of of export house confusing. It also makes any assessment, whether quantitative or qualitative, of their importance of limited value.

An attempt was made by BEHA in 1968 to quantify export houses' part in United Kingdom exports [18]. Making allowances for non-response and non-membership of the Association, it was concluded that export houses handled or financed about 20% of United Kingdom exports in 1967. The researcher considers it would have been difficult to avoid double-counting, for instance cases of confirming house business financed through a merchant bank. While the Association states that a partial survey in the early 1970s pointed to increased participation by export houses, the figure must be viewed with some reserve because of the absence of reliable data. (This is a reflection of the complexity of the subject matter and the purpose of the survey, rather than a criticism.) The principal activities reported by the respondents, as a proportion of their turnover of United Kingdom exports, included:

sold as principals	30%
financed but did not sell	29%
acted as confirming house	21%.

Clearly, this indicates a substantial involvement in financing those exports handled in some way by members of the Association, but one must apply the same reservations with regard to possible double, or even triple, counting. As has already been pointed out in considering confirming houses, the house's perception of its rôle may be different from the exporter's

and the importer's, so the house's evaluation of its principal activities may be faulty.

No reliable information is available regarding the relative importance of the functions carried out by these export houses, of which there are an estimated 700 - 800 [19]. In their selling function, knowledge of markets and of sources of supply are obviously important, possibly even indispensable to success. As far as finance is concerned, they probably have few resources at their disposal which are not available to exporters themselves. Their strength lies in their knowledge of procedures connected with shipping, insurance, import and export regulations, finance. Procedures are not usually difficult in themselves, but most people find them tedious. They vary from one importing country to another, from one port to another, even from one trade to another. Unless a manufacturer has a large volume of business (the number of transactions rather than value is the criterion), he cannot quickly ascertain and comply with all the requirements. An export house normally has the volume of business to handle these matters with a very high degree of competence; it often works on narrow profit margins and is able to perform these functions more economically than the manufacturer.

Even efficient large manufacturing companies find it expedient to do some of their foreign business through export houses. For medium and long term finance, the biggest exporters still find it essential to use merchant banks or other intermediary to co-ordinate their schemes.

1.13 Distribution Channels.

Although a member of a distribution channel who is not included in one of the foregoing categories is likely to be located in the importing country and will strictly be concerned with import finance, mention must be made of agents, stockists, wholesalers and similar elements in the distribution network. Some exporters very positively look for the ability to finance business when they seek collaborators in importing countries, just as they do in the domestic market. While this has obvious advantages for the small exporter with limited access to funds, it is also true of large companies. It is, for instance, traditional in car business. A capital goods exporter(£1m + per annum) regards ability to finance business, or to arrange finance locally both for himself and end-users, as just as important as technical knowledge and after-sales facilities. From some countries, this manufacturer receives payment for deliveries sooner than from United Kingdom buyers [1]. He is thus one of the exceptions to the general rule that exports require a longer commitment of working capital than home trade transactions.

2. Export Credit Insurance - The Export Credits Guarantee Department and its part in United Kingdom Government Policy.

2.1 Origins and development.

The central rôle of the Export Credits Guarantee Department (ECGD) will already be clear from the description of the clearing banks' part in export finance. It is, in fact, the major vehicle of Government policy in export finance; additionally it has the potential to be used indirectly in other aspects of Government policy. A consideration of its development will serve to set the scene on a wider European scale.

Its origins may be traced to the Faringdon Committee, appointed on 1.7.1916 "to consider the best means of meeting the needs of British firms after the war as regards financial facilities for trade, particularly with reference to the financing of large overseas contracts" [20]. Government committees are not usually set up without some pressure for action being exerted by influential bodies (though the time taken for their deliberations may be used as a means of postponing action). What was the underlying reason in this case?

The Committee noted in §3 of its report [20], the services that British, Colonial and British-Foreign Banks rendered to British trade, especially in the Far East and many parts of South America. It found "also that in the case of large contract operations British contractors with the assistance of Financial Houses have in the past been ready to provide large amounts of capital and to take considerable risks in connection with the operations which they have undertaken,"

but these services were not co-ordinated (§4). Moreover, the British manufacturer might need finance "of a kind which a British Joint Stock Bank...could not prudently provide, whereas the German Banks in particular seem to have been able to afford special assistance at the inception of undertakings of the most varied descriptions, and to have laid themselves out for stimulating their promotion and for carrying them through to a successful completion". It concluded (§§24-5) that there wasscope for setting up a new institution without delay, so that preliminaries could be completed before the end of the war; specifically, it recommended the setting up of a Trade Bank with a capital of £10m. It had reported (§6) the close control which German banks exercised over manufacturing concerns, a feature "which would not be possible, even if it were desirable, in the United Kingdom", and the proposed Trade Bank "should endeavour not to interfere in any business for which existing Banks and Banking Houses now provide facilities". Having noted (§19) how foreign banks syndicated business which was too big for a single institution, the Committee's recommendations included a suggestion that the Trade Bank "should try to promote working transactions on joint account with other Banks to submit to it new transactions which, owing to length of time, magnitude or other reasons, they are not prepared to undertake alone."

The Committee's recommendation resulted in the setting up of the Overseas Trade Corporation in 1917, and the Export Credits Department as a sub-department of the Department of Overseas Trade. It is the Export Credits Department which is important in the present context. It operated various schemes,

usually at a heavy loss, to facilitate exports, relieve unemployment and encourage the economic situation of certain Eastern European countries. Even this modest development was opposed by the banks, and this "led...to the failure on the First and Second Export Credit Guarantee Schemes in 1926 and 1930" [21]. Nevertheless, in spite of opposition the Export Credits Guarantee Department took over the Export Credits Department and developed its work on new lines. It was established as a separate Department and started its credit insurance scheme in 1930, from when there is a continuous line of development to the present day.

The Department was empowered to offer insurance only when cover was not available from commercial sources, and this is still the case. Cover was limited to 75% of the order value and the insurable causes of loss were very limited. The comment:

> "...the whole system [ECGD] was originally devised as a temporary expedient to assist the revival of our export trade after the War. It is conceivable that the Treasury still regards the Department as a stop-gap, to be wound up rather than extended within the measurable future. It would be a pity if this view were still held, for the Department has amply justified its existence, and should be given encouragement to extend its activities" [22]

suggests that it was not taken very seriously by the Government of the time.

Essentially, this remained the position until after the second world war, though by now there was a greater understanding in official circles that exports from this country should be actively encouraged. ECGD undertook a "sales drive" to increase the number of its policy holders. It also insisted on exporters insuring the whole of their turnover on short term credit, thereby spreading the risk and enabling premiums to be reduced.

As the demands on the economies of the industrialised countries subsided after shortages caused by the second world war and the Korean war, manufacturers who for nearly twenty years had been in a sellers' market discovered that they had to fight for orders. One of the weapons was the offer of credit. Newly independent countries lacked both financial resources and the necessary knowledge to finance their purchases - especially purchases of the capital goods which they needed to pursue their economic ambitions. Briefly, the outcome was the development of a "credit war" in this sector. All the industrialised countries assert that competitors started this "credit war" or "credit race". Whatever the precise truth (which is complex) there seems little doubt in the minds of many that the Germans were mainly responsible - or perhaps were more thorough and competent than other countries. Seeking to re-establish a shattered economy, their selling was very aggressive. It included, at least in certain markets, the ruthless use of bribery, and the offer of extended credit. Meanwhile, a number of schemes were devised in different countries to assist exports: an exchange retention scheme and tax rebates in France, a tax rebate and other schemes in Germany, dual pricing for coal and steel in the United Kingdom.

France was regarded by some as "easily the worst offender" in subsidising exports [23]. Meanwhile, "...some British exporters of capital goods [had] found that they [had] lost orders because foreign customers...demanded credit facilities for periods... sometimes up to four or five years" [24]. Looking back from 1971, Syrett and Pither wrote that "some years ago, British exporters found they were losing the best agents in foreign markets to German competitors who gave long credit terms" [25].

The recollections of those engaged in export at this time show that there was a general belief that German credit terms were unfairly aided, but not all subscribed to this view. Another contemporary comment was that "British manufacturers tend to assume that more difficult export markets entitle them to special aid or new facilities......There is no doubt that the credits offered by Germany have often been exaggerated or that...the British manufacturer is at least as competitive on credit terms as his German rival; certainly he usually pays less for his credit" [26].

Although some finance was made available to German export- by the quasi-official Kreditanstalt für Wiederaufbau, most came from the German banking system. "For its part, the German public, instead of clamouring for more imported goods, continues to save its money at a prodigious rate...the credit extended by the reluctant German [to the European Payments Union] is now over $567 millions" [27]. The money was available and the close connection between the banks and industry which had existed before the first world war still continued. There can be little doubt that the two worked closely together and it is

impossible to say which was the dominant force in seeking exports or whether, as seems likely, both were equally responsible.

Meanwhile, preoccupation with supplying an easy home market, exchange control regulations, lack of knowledge of appropriate financing techniques (the activities of institutions having changed since the 1930s) and conservative attitudes combined to prevent a quick adjustment to the new environment. British banks' traditional function was, and still is, to lend only on a short-term basis, in contrast to the German banks which lend long-term funds. Other financial institutions were unable or unwilling to make sufficient funds available for longer periods of credit in export markets. Although it was sometimes claimed that the problem in the United Kingdom was ignorance of the facilities available, the Government found it necessary to allow ECGD to grant longer-term guarantees in "an attempt to meet the oft-repeated complaint that the exporters of other industrial countries (notably the Germans) [were] in a position to give their customers much longer credit than British firms can afford" [28]. Even after the introduction of this facility, some exporters had difficulties. One recalls that a well-known merchant bank withdrew its offer of £500,000 to finance an export order in the mid-1950s, because it found a more profitable use for the money while negotiations were in progress [1].

At this period, ECGD seemed reluctant to grant credit cover in many cases - or to give it quickly enough. It was anxious not to extend credit beyond the limits agreed with other countries. It was prepared to match terms offered

by competitors (if backed by official resources or guarantees), but required proof of these better terms. The Department may have been right in thinking that false information was being given by buyers as a bargaining lever, but hard proof was naturally not easily come by in time to be of use, even if it could be obtained at all. The attitude was described by one exporter: "Prove the horse has bolted and we'll help you close the stable door".

The seeming reluctance of British exporters to offer credit terms undoubtedly had a bad psychological effect in some markets. Through no fault of the Department this effect was sometimes intensified by politicians and the press giving misleading impressions of the extent of the facilities available.

In spite of the difficulties some successful long-term financing took place. Special institutions for the provision of export credit facilities were set up: Air Finance Ltd, to finance credits up to three years for approved export orders for British aircraft was sponsored by three leading merchant banks in 1953, while another sponsored the Manufacturers Export Finance Company to discount bills relating to ECGD-covered transactions, the big banks having been approached for loan facilities. Another arrangement was for a nine-year credit for a hydro-electric plant in Turkey financed by Turkish Government bonds privately placed among the City's financial institutions. These were isolated examples which did not have a significant effect, and in 1954 the Economist could ask: "Have the great houses of finance and industry missed a fine opportunity?" [29].

By the mid-1950s fears of a credit war were becoming more extensive throughout the industrialised world. The United Kingdom seems to have stayed on the path of righteousness in observing conventional practices and such agreements and understandings as existed at that time. This was largely due to the rectitude of ECGD whose cover had become indispensable for obtaining practically all medium-term export finance. In other countries there was concern that all forms of export aid were threatening to get out of hand and the Credit Assurance Association's survey [26] reported that by the end of 1953 the German banks were opposing relaxation of credit terms. During the visit of the British Chancellor of the Exchequer to Bonn in the spring of 1954, the British and German governments had undertaken to collaborate in their efforts to secure general abolition of objectionable export incentive schemes (including over-generous credit terms).

Alongside efforts to obtain some degree of uniformity in the practices of the industrialised nations competition continued, albeit in a less intense form. ECGD sought to improve its cover and the Government persuaded, or at least put pressure on, financial institutions to assist. The main landmarks since the mid-1950s are now summarised.

In 1961 ECGD was authorised to guarantee in selected cases the repayment of loans to overseas buyers of British equipment, applicable only to very large projects. "Buyer credits", as they have now become known, were a departure from the practice which had hitherto prevailed, and came to be

adopted by other exporting countries. It had the advantage of not being technically supplier credit and therefore not subject to any existing international undertakings - hence more flexibility was possible. There was initial resistance from exporters because of the complexity of the arrangements, and one ECGD source says that some residual opposition still exists (mainly because of conservatism on the part of exporters), but the system is now well-established.

On the financing side, the main development in 1961 was to involve both the banks and the insurance companies in the provision of finance for long-term buyer credits. Initially a consortium of insurance companies and pension funds agreed to provide finance for the longer maturities, the clearing banks taking the maturities up to five years (a period which they had by this time come to regard as acceptable for export business). In January 1962, the clearing banks and a number of insurance companies agreed to provide export finance at a fixed rate of interest for this type of business. The banks were responsible for the shorter maturities at 5.5%, the insurance companies for the longer ones at 6.5%. In January 1965 the banks agreed to provide funds at 5.5%, irrespective of the length of the maturities, in place of the previous mixtures of lenders and rates.

Meanwhile, in 1961 (with modifications in 1965) the Bank of England agreed to refinance certain maturities and allow banks to count some of these in their liquid assets for the purpose of calculating liquidity ratios. These arrangements were further modified in 1972 and now take the form described later.

Until 1966 developments had concentrated on longer-term credits, but now a scheme was introduced for credits between 30 days and two years, whereby banks made finance available on bills. In 1967 this was extended to open account transactions involving credit of not more than six months. Originally these facilities were provided at bank rate, but are now at 0.5% above the bank's base rate.

It is essential to have appropriate ECGD policies to qualify for these facilities.

By the mid-1960s it was clear that ECGD had become the key organisation in the granting of export credit, especially medium- and long-term credit. In 1966 it could write:

> "With the effective removal of Exchange Control restrictions on credit terms and with the greatly increased use of ECGD facilities, particularly in the engineering field, the Department has become a chief instrument for controlling the scale upon which credit is granted overseas." [30]

It could have added that the financial institutions were unwilling in practice to make any medium- and long-term (and some short-term) loans without ECGD taking over the risks - a situation which in essence still applies today.

Subsequently, ECGD sought to make improvements in the cover it offered and to simplify its operations, but essentially the system has remained the same. These developments will not be reported in detail here since, with the exception of some innovations introduced since this research started, they have been of a minor character in principle. Having traced the

main events in the development of the ECGD, let us move to a consideration of the facilities which it offers at the present time.

2.2 Policies offered.

The Comprehensive Short Term Guarantee is a continuous guarantee, renewable annually, appropriate for repeat business where credit terms are under six months. All an exporter's business must be offered to the Department, though the latter is sometimes prepared to cover a limited range of markets. Either the risk from the date of contract or the risk from the date of shipment may be covered at the exporter's option. There are commonsense restrictions, particularly as to credit limits on individual buyers, but in general the exporter does not have to seek approval for individual shipments up to an agreed limit. The normal cover is 90% or 95% of the loss, depending on the cause of the default.

Premium rates are calculated on the basis of a fixed sum at the beginning of each policy year, the amount being determined individually for each policy holder, plus an ad valorem premium each month on the value of shipments (or contracts, depending on the type of policy). The Department regards its basis of calculation as confidential, but publishes average rates charged during the previous year. These declined steadily from 0.58% in 1954-55 to 0.24% in 1968-70 and 1973-74, since when they have risen slightly to 0.26% in 1975-76. Although the cover is more extensive than in most other countries, these premium rates are believed to be the lowest in the world. They are achieved by insisting on exporters insuring all their business, so that good risks help to pay for the bad ones.

The Supplemental Extended Guarantee is available only to those who already hold the Comprehensive Guarantee. It is intended mainly for companies exporting goods, usually engineering, where the usual terms of payment are between six months and two years. The range of cover is similar to that of the Comprehensive Guarantee, but premiums are based on the country of import and the length of credit and are calculated for each individual transaction; there is no fixed annual payment.

Specific Guarantees are intended for capital goods, which cannot usually be accommodated under comprehensive policies since there is normally no continuity of business. ECGD is prepared to cover sales on up to five years credit, with premiums being assessed individually for each contract. The risks covered are similar to those covered by the Comprehensive Guarantee, but the maximum level of reimbursement is 90%. As an indication, ECGD gave 3 years as the maximum period of credit allowed for contracts up to £50,000 and 4 years up to £100,000 (in 1975).

Only contracts over £2m will be considered for more than five years credit, unless there is evidence of a foreign competitor with government insurance support offering more favourable terms.

Reference to the French section will show that their guidelines are rather more generous to the buyer, but no evidence has been found to show how the French export credit insurers treat these in practice.

Premium rates are not published, but ECGD states that

they should not exceed 1.25% flat for five years credit in strong markets and about 3.4% in weak markets.

- Constructional Works Policies offer similar cover to specific policies, but take into account the highly specialised nature of the business.

There are other special policies covering sales through overseas subsidiaries, consignment stocks, external trade (i.e. trade between two foreign countries transacted from the United Kingdom), aircraft sales, using foreign sub-contractors, leasing, and overseas investments. These are negotiated on an individual basis.

Guarantees for Financing (Supplier credits).

It has been possible since the 1930s to assign policies in whole or in part to a bank, thereby facilitating bill discounting, but the schemes introduced in 1966 and 1967 go much further.

If an exporter holds a Comprehensive Short Term Guarantee, he may apply to his bank for a short-term finance facility. The procedure is that ECGD gives a direct guarantee to the bank that it will pay to the bank the full amount of any sum three months overdue, though the bank will have recourse to the exporter for the amount not covered by the guarantee (usually 5% or 10%), or for the full amount if the bills have not yet been accepted by the foreign buyer. The Department fixes a revolving limit and charges a premium of 0.125% per annum, calculated on the agreed limit, not the use made of the facility. The clearing banks have agreed to extend finance

to exporters using this scheme, at 0.5% over their base rates, against accepted bills or promissory notes. If business is done on open account, there are similar facilities, but giving a direct guarantee to the bank for only 90% of the invoice value, and being available for credits of up to six months against the two years when bills are used. The procedures are naturally a little different, but essentially the two schemes are the same.

This facility might seem attractive to an exporter because it opens up a new source of finance to him. Whether this happens in practice, however, is open to considerable doubt. Although at the Head Office of one of the clearing banks it was said "We should have the Bank of England on us like a ton of bricks if we didn't lend against an ECGD guarantee", it is not certain that the bank will in fact provide the finance. Whatever a Head Office may say, lending is normally arranged at branch level; while it may have to be approved at regional level, it may be stopped at the branch. One case was reported where, reasonably enough, the bank refused the facility on the grounds that export debts were already included in a debenture held as a security against an overdraft. One bank manager said he knew of other cases where the bank was unwilling to go to the limit agreed by ECGD. A number of branch managers who were asked whether they would reduce a customer's general overdraft limit if he negotiated a direct guarantee without exception said they would. (It will be recalled that similar answers were received in respect of factoring facilities, though it was noticeable that there was considerably more hesitation when replying to the question on direct guarantees.) Viewed in this light, the facility

does not automatically open the door to new finance without curtailing an existing source. During the period covered by this research, the banks have had plenty of funds available, but one manager made it quite clear that if money became tight he might prefer to lend for more profitable purposes, e.g. personal loans. [1]

The main attraction of the facility is the cheaper finance, but this too is not necessarily so for all exporters. It may be no cheaper than other sources of finance, say a Eurocurrency loan. But even if one confines oneself to bank finance, the advantage may not be very great. Since the ECGD premium is 0.125% on the agreed ceiling, an exporter having a fluctuating level of trade and an overdraft at 1% over base rate might not find it worth while.

Commerce International quotes an estimate that only about one-third of those entitled to the facility actually use it [31]. Sometimes this is due to ignorance. For instance, a bank manager reported that a small but very sound concern paying 1% over base rate on its general overdraft refused to apply for the facility on the grounds that it would cost too much to administer. (Since he was already administering an ECGD policy, the extra work would have been negligible, and it was estimated that he would save about £3000 a year. Significantly, his bank manager was also ignorant, and could not advise him.) In another company - a very big one - the Financial Controller, apparently like the rest of the accounts department, did not even know that the facility existed. (In view of the millions of pounds which the Government used to keep this company alive, perhaps this small matter was of little practical consequence.) [1].

On the other hand, at least one multi-national company is using this scheme to finance shipments to one of its subsidiaries abroad, then withdrawing the documents from the scheme a day or two before their due dates. One of the clearing banks is believed to have been instrumental in negotiating changes in the regulations to enable this to be done. [1] It is assumed by the researcher that practices of this nature were what Peter Vigger, a director of a merchant bank, had in mind when he referred to the matter in the House of Commons [32]. The Minister commented that "as long as they are exporting we want to encourage them to go on exporting". [33] While one may admire the company for using to the full all the resources at its disposal, it is difficult to see how the system furthered exports in this case. It merely adds to the confusion in any attempt to assess the value of this facility in relation to its declared purpose of encouraging our export trade.

As reported under clearing banks, ECGD also assists in the provision of medium-term supplier credit for up to 5 years at a rate which is fixed at the time of the contract - at the end of 1975 it was 7% minimum. In addition, the bank charges a commitment fee of 1% flat, a negotiation fee of 0.1% flat, and the Department's premium is 0.125% flat. Under this scheme, the Department guarantees to the bank 100% of the value of accepted bills; with typical terms of payment these will usually represent 80% of the contract amount, 20% having been paid in cash.

As with the shorter term bills facility, ECGD retains the right of recourse to the exporter for any funds for which it is liable to the bank. The latter is thereforeat risk only

from the time money is advanced after shipment until the bills are accepted, during which period he has recourse to the exporter. Although the guarantee to the bank is 100%, the exporter will be covered by his policy only to the extent of 90% of any loss - ECGD therefore retains the right of recourse to him in respect of of any losses not covered by the policy, e.g. the remaining 10%, or if the exporter delivers faulty goods.

Banks' refinancing facilities.

Since 1972, if the amount of any clearing bank's export lending on medium-term export finance exceeds 18% of its current account deposits, it can refinance the excess through ECGD. (In July 1976, it was reported that the figure was to be revised "temporarily" to 20%.) Since the banks are lending at fixed rates in markets where rates normally fluctuate, they are compensated for any losses by being paid the difference between the fixed rate and an "agreed rate" built up from the "observed rate", i.e. the mean average yield on Treasury Bills and the lending rate to nationalised industries, plus an "unmarketability" factor. Since 17.10.74, the second element has tapered from 1.25% when the observed rate is 7.5%, to 0.125% when it is 14.5% or more. John Stanley in the House of Commons considered this to be "attractive business" for the banks, when considered in conjunction with the 1% commitment fee charged to customers, though perhaps not too far out of line with normal returns [34].

Guarantees for Financing (Buyer Credits).

Medium-term and long-term credit may also be financed by buyer credits. As already reported, this technique was developed by ECGD and increasing numbers of contracts are

financed this way by all industrialised countries. In the United Kingdom practically all ECGD-backed long-term finance is in the form of buyer credits. From the exporter's point of view, the advantage is that there can be no recourse to him for any percentage of the loan.

Technically, a loan is made by a United Kingdom bank to the overseas buyer (or more usually his bank). Normally the loan will be for 80% of the contract value, the buyer being required to pay 20% in cash before shipment (normally spread over the period of manufacture). This introduces procedural complexities requiring supplier-buyer, lender-borrower and ECGD-lender contracts to be negotiated simultaneously. In practice, the arrangement is for the United Kingdom bank, as lender, to pay the exporter direct, on behalf of the borrower. Curiously, the established procedure does not require a contract between the exporter and the lender, requiring the latter to transfer the payments on the due dates.

Frequently, a merchant bank will undertake all the financial negotiations - a complex business, which may result in a financial agreement running to forty or fifty pages in length. It will charge a management fee for its services, the actual figure depending on the circumstances of the individual transaction but probably of the order of 0.125%. It is also quite common for the merchant bank to arrange for the 20% "front end" finance to be borrowed by the buyer in the Euro-currency market. Since this removes the theoretical advantage of giving the buyer an incentive not to default on the contract before shipment by the commitment of his own funds, it is regarded as risky business and appropriately high interest

rates will be charged. It is not surprising that in many cases no lenders can be found to provide this front-end finance and negotiations founder at this stage.

During the course of this research cover has been made available for pre-shipment finance on overseas contracts with a contract value of at least £1m, which may help to overcome this problem for exporters. However, this cover is available "selectively", and no information is yet available as to its operation in practice. Any pre-shipment finance obtained in this way does not qualify for the preferential fixed interest rates.

Guarantees for lines of credit.

Medium- and long-term finance so far discussed refers to specific contracts. Since 1967 ECGD has guaranteed lines of credit to cover projects or buying programmes comprising a number of individual contracts of relatively small value, sometimes as low as £5000, though the total line of credit may be substantial. ECGD usually gives a financial guarantee to one United Kingdom clearing or merchant bank, which will then get backing from other banks. Finance, usually for between 80% and 85% of the contract value, is made available on the same fixed interest rates as for medium and long-term credits. Because of the varied nature of requirements, each policy is negotiated individually.

ECGD states that the initiative for granting these lines of credit comes from a variety of sources - British manufacturers who have learned of an appropriate project, British or foreign banks who learn of suitable projects, foreign buyers -

but the end result is that a British bank grants a line of credit to a foreign Government or Government agency for projects, or to a foreign bank if a general line of credit is granted. [1] ECGD comprehensive policy holders and those whose contracts would normally qualify for specific cover are eligible.

In the year 1973-74, the last year for which figures were available when this part of the research was carried out, drawings made on these lines of credit amounted to £39m, or 0.3% of United Kingdom exports for that year. [1]

The foregoing policies may be regarded as the main body of ECGD cover available. A number of special policies have been developed, in addition, and these are now briefly considered.

Cost escalation cover is, in essence, a method by which part of increased costs on large contracts is met by the Government. It is claimed that the reason for its introduction was the availability in France of cover against increased costs due to inflation, which it was considered gave an unfair advantage to French exporters. The ECGD cover is intended for major contracts worth at least £2m and requiring a manufacturing period of at least two years. It was originally introduced in 1975. The method of its introduction - as an amendment on the final reading of the Export Guarantees Amendment Bill - is an indication of the haste with which it was conceived (a reading of the debate makes the haste only too clear). Because of the difficulties experienced in its operation, a revised scheme was introduced in 1976 and it is obviously too early to comment on the outcome. It is,

however, apparent that not much use has been made of the scheme. On the one hand, ECGD does not wish to enter into large open-ended commitments, while on the other hand exporters have found that when the details of the method by which cost increases are calculated are carefully examined the cover does not seem particularly attractive.

The "insurance cover" provided by the cost escalation policy is strictly speaking a subsidy, very thinly disguised, and not part of export financing on a strict definition. It was suggested, when the scheme was introduced, that the cost would work out at £50m per annum, but this was obviously very much a guess.

In some construction contracts, performance bonds are required from insurance companies or other financial institutions (the legal position varies according to country of import) to ensure adequate performance by the contractor. In appropriate cases, ECGD is willing to indemnify the bond giver. Depending on the nature of the bond, the cost is 1% or 1.25% per annum. [36]

In some importing countries, bonds are acceptable only if the importer (usually a Government department) is the sole judge of whether the performance of the contract is adequate. ECGD is now prepared to insure against the possibility of the bonds being called without justification, even when the bonds themselves are not supported by ECGD. This cover against unfair calling of bonds is available where the form of the bond is acceptable to ECGD, and the importing country is considered suitable. The cost is 0.50% per annum.

Projects participants insolvency cover, available from the end of 1975, insures main contractors or consortium members participating in major export projects of £20m or more for 90% of the loss arising from the insolvency of a sub-contractor or fellow consortium member. The cost of this cover is 1.5% per annum on the maximum liability.

An exchange risk cover is intended to cover certain limited exchange risks in meeting forward exchange contracts when a buyer defaults. The problem has arisen, not because of any shortcomings in the foreign exchange forward markets or any attempt to encroach on existing commercial and financial practices, but to cover any loss which might arise due to fluctuations in exchange rates between the date of default of a foreign buyer and the date contracted for delivery of foreign currency against a forward exchange contract. The question is really a technical one from the exporter's point of view - if a foreign buyer defaults and the contract of sale is in a foreign currency, for the purpose of claiming against a normal ECGD policy the loss would be converted into sterling at the rate ruling on the date of default, and the exporter would be required to buy foreign exchange in the market at the date stipulated in the forward contract.

These special policies are of such recent introduction that comment on their operation is not possible.

Special aircraft and shipbuilding policies are offered. These are essentially variations of specific guarantees and are obviously of limited application.

Services policies, broadly following the lines of insurance of sales, may cover invisible exports in the form of professional services, royalties, copyright fees and so on. As with small exporters and business promotion policies, there has been so little demand that for practical purposes they may be regarded as extinct.

Addenda

Guarantees for financing. Since this chapter was written, the cost of finance under the direct guarantee scheme has risen from 0.5% to 0.675% above the lending bank's base rate.

Banks' refinancing facilities. The banks' lending for medium-term export finance is now re-financed through ECGD only when it exceeds 24% of non-interest-bearing deposits.

2.3 Export Credits Guarantee Department and the use of foreign currecncies.

Developments which have occurred during the course of this research merit separate mention.

Traditionally, the Export Credits Guarantee Department has been concerned with guarantees expressed in terms of sterling; although it has for a long time been possible in approved cases to have policies endorsed in foreign currencies, it was the sterling equivalent at the date of relevant events which was paramount. Similarly, with the inception of guarantees for financing, all operations were required to be in sterling - indeed the special facilities for re-financing were available only to the clearing banks. Since the beginning of 1977, changes in the rules under which the Department operate have enabled it to arrange finance in currencies other than sterling. (At the same time it is encouraging exporters to consider the merits of invoicing in foreign currencies, but this is a less important issue.)

The object of arranging finance in other currencies for medium and long term credit is, from the United Kingdom Government's point of view, to ease the burden on the Consolidated Fund (through ECGD re-financing) and to shift it to foreign sources of finance, thereby easing the strain on the balance of payments. A more specific reason, not quoted by Government sources, was to reduce the public sector borrowing requirement in order to facilitate the granting of an IMF loan.

The new rules allowed the Department to extend its direct guarantees to foreign banks supplying finance for British exports, and for British lending banks raising loans on the Euro-currency market, usually in US$ or DM. ECGD undertakes to adjust the interest receivable by the bank from the borrower to the level of an agreed rate of return, related to the cost to the lending bank of raising funds in the Euromarket. ECGD is also prepared to adopt the rôle of co-lender, in that it will take over the loan for the remainder of the credit period if the period of the Euro-currency loan raised by the lending bank (usually a maximum of seven years) is insufficient to cover the full term of the credit granted to the buyer, and the bank or an alternative commercial lender is not prepared to carry on the loan.

Although the new rules are of an enabling nature, it became clear that the Department intended to <u>insist</u> on foreign currency being used for this type of operation. The USSR in particular was thought to be likely to resist from the outset, since it was well aware of the advantages of probable sterling devaluations, and would be likely to insist on the use of this relatively soft currency. In the event, the Department admits to having met buyer resistance. [1]

(That this is not an imaginary difficulty is shown by the fate of Italian suppliers in negotiations for a steel plant in Brazil. They dropped out of negotiations when the Brazilians insisted on the finance being available in lire, a soft currency with prospects of being devalued, instead of US$ or DM, which the supplier proposed. The United Kingdom company offering finance in sterling (negotiations having been

started before the new rules came into force!)finally won the contract. [38])

It is understood that, in fact, contracts have been signed utilising foreign currencies as the source of finance, but it is still too early to offer an opinion as to the success of the new method.

3. Commentary on United Kingdom Export Finance.

3.1 The extent of the requirement for special export finance facilities.

The foregoing summary of the facilities available does not fully consider the extent to which they are used or whether there are any shortcomings. Whether they are, in fact, used is not necessarily an indication that they are indispensable or even the most appropriate.

Table 1 helps to bring the overall situation into perspective, showing the pattern of credit granted for United Kingdom exports. The figures are based on Statistical Office surveys which are acknowledged to be subject to some error. As a measure of the time taken to receive payment, more serious than statistical errors are delays in payment, since the figures given represent the contract terms. Nevertheless, possible errors cannot seriously distort the general picture: more than 85% of British exports are supplied on terms of six months credit or less, and less than 5% of British exports require more than five years credit. This pattern has been stable for more than a decade. (While there are some fluctuations in the "over five years" category, this is not surprising, since contracts with these terms are relatively few and values very high. In these circumstances a single contract delayed by a month at the end of the year can make a noticeable difference in the figures for two years.) As would be expected, most financing problems are associated with these longer terms of credit, which are mainly for underdeveloped countries.

CREDIT TERMS EXTENDED FOR UNITED KINGDOM EXPORTS

(AS A PERCENTAGE OF TOTAL UNITED KINGDOM EXPORTS)

	1966	1967	1968	1969	1970	1971	1972	1973	1974
<60 days	56.3	56.6	57.8	57.5	56.6	55.7	55.6	56.4	57.7
61 - 180 days	31.5	31.2	30.2	31.0	32.7	32.4	33.4	33.5	32.9
181 days - 1yr	6.8	5.5	4.7	4.6	4.1	4.9	3.9	3.8	3.3
1yr - 21 mths					1.3	1.1	1.0	1.9	1.5
1yr - 3yrs.	2.5	2.8	2.4	2.2					
21 mths - 5yrs.					2.5	2.7	2.5	1.9	1.9
3yrs - 5yrs.	1.5	1.1	1.7	1.6					
>5yrs.	1.4	2.8	3.3	3.1	2.8	3.2	3.6	2.5	2.7

SOURCES : Board of Trade Journal
Trade and Industry
Business Monitor M4

TABLE 1

When considering United Kingdom export finance, it is relevant to consider the nature of companies importing United Kingdom goods and their relationships with the exporters. The information shows that less than 20% of our exports are by companies with no overseas associates.(Table 2).

While one cannot draw too firm conclusions without much more detail, it seems reasonable to assume that companies under direct foreign, especially United States, control will not rely specifically on United Kingdom sources of finance. They will do so if they find it more advantageous, but if they find it more advantageous to arrange finance through the parent company this is hardly likely to affect their exports. The same considerations will probably apply to the associates of foreign controlled companies, giving a total of 29% (1973) which could probably be financed from abroad without having any serious repercussions on United Kingdom exports. If we add to this the 15% by United Kingdom controlled companies to related concerns overseas, we reach a total of 44% of United Kingdom visible exports for which United Kingdom finance need not be of vital importance. (The extent to which these transactions may be considered to be no longer export finance is illustrated by the fact that official United Kingdom Balance of Payments figures now classify export and import credit between related companies as capital flows.) Moreover, at least some of the companies with overseas affiliates are likely to be big multi-national companies, so that financing their "non-related" exports is partly in the realms of "multinational finance" rather than pure "export finance". Others are large companies, and should have no special difficulty in covering the export financing requirements from their normal

EXPORTS OF UNITED KINGDOM COMPANIES BY NATIONALITY OF CONTROLLING INTEREST.
(AS A PERCENTAGE OF TOTAL UNITED KINGDOM EXPORTS)

	1971	1972	1973	1974
U.S. Controlled	17 (9)	17	17 (10)	17
Other foreign controlled	6 (2)	7	7 (3)	6
Associates of foreign controlled companies	5 (1)	5	5 (1)	4
United Kingdom controlled with overseas affiliates	52 (14)	52	52 (15)	55
Other enterprises	20	19	19	16

( ) = to related concerns.

Source: Business Monitor M4.

TABLE 2

sources. By interpolation in data from Business Monitor M4, it is found that at 1974 prices (with similar patterns for other years) about 60 companies accounted for half the United Kingdom's exports, each one exporting well over £20m. It is reasonable to assume that these are very substantial companies with access to long-term finance without special provision for export. Over 94% of United Kingdom exports were provided by companies exporting over £2m per annum each and it seems likely that many of these will also be substantial companies which would not be seriously affected by the absence of special export finance provisions. Exceptions are, of course, those companies handling multi-million pound contracts for which extended terms are required and where the burden of a succession of contracts would prove impossible without this aid.

For the bulk of United Kingdom exports, the necessary short-term credit poses few problems of substance. Those which do occur usually fall into one of two categories: (a) common to domestic and export business, (b) attributable to ignorance of procedures peculiar to export. The former falls outside the scope of this report and the latter attracts further comment later.

3.2 Commentary on Export Credits Guarantee Department.

It has been seen that the initial rôle of ECGD was to provide insurance against bad debts, and for many years this was its sole function. In recent years it has entered into financing proper, and in the view of one official this now is its most important activity. [1] As far as medium- and long-term credit is concerned, the researcher finds it impossible to separate the two activities.

The volume of its business has grown to cover more than one-third of United Kingdom exports, from only 8% in 1947 (in the last decade, the figure has fluctuated between 33% and 38%). The reasons put forward by ECGD for the increase are (a) improvements in cover, (b) periods of credit required are lengthening, thereby increasing total amounts at risk, (c) the value of policies in securing bank finance. [39] The percentage of exports covered is higher than in any other country in the world operating a similar scheme.

One of the features of the system which has attracted criticism is the "all or nothing" principle which rules short-term guarantees. There can be little doubt that the percentage covered by ECGD is inflated by exporters being compelled to insure a sometimes substantial proportion of their exports where the risk is negligible. It is difficult to believe that exporters would regard developed countries in Europe and North America almost as risky as non-OPEC developing countries, yet 41% of United Kingdom exports to the former area and 43% of those to the latter area are covered by ECGD policies. As much as 62% of ECGD's business covers exports to developed countries, and it seems reasonable to think this percentage would be much lower if exporters had a completely free choice of markets to be covered. This view is reinforced by a comparison of these figures with German and Netherlands experience. The researcher does not consider the issue to be other than a minor one in terms of overall export performance, but it does show the need for modification of claims, by both supporters and critics, that ECGD is instrumental in providing assistance for over a third of British exports - some of the assistance is in fact regarded as a hindrance, however small. [40]

(The "all or nothing" principle has obvious advantages for the underwriters - spread of risk and ease of administration - and one may note in passing that the European counterparts of ECGD are now more actively promoting this principle.)

Although figures are readily available to show the proportion of United Kingdom exports covered by ECGD policies, it is not easy to break these down further by category of credit. ECGD states [40] that 77% of its business relates to exports on less than six months, but gives no details regarding the remaining 23%. Comparison with the figures in Table 1 is not possible because of the different breakdown of credit terms and the fact that Table 1 refers to contracts placed and ECGD figures refer to shipment. However, if one accepts the unanimous view of those interviewed, it may be said that ECGD covers all credit transactions over two years. Using crude calculations and interpolations one may suggest that about 55% of credit transactions between two years and six months are covered (probably nearly 100% at the longer end of the range, tapering to about 30% at the shorter end), with just under 30% of the country's exports at less than six months credit being covered. These are rough estimates, but they are not inconsistent with the published figures or with common sense.

Since its collaboration is thus essential for the provision of medium- and long-term finance and it can facilitate, though not ensure, access to finance at preferential rates for shorter term credit, it occupies a powerful position. In granting all policies, but especially specific policies and direct bank guarantees, the limits it imposes may be restricted

by its view of the financial status of the exporter as well as of the buyer and his country. This is resented by some exporters who feel that it gives a Government department too much power to interfere. There is also apprehension in some quarters of the Department's power to require complete approval of the buyer-seller contract when financial guarantees are given, exemplified in a confidential internal memorandum in a large group some years ago:

> "It is an inflexible principle of ECGD that they must approve any future business by the exporter on credit terms or over a certain amount on cash terms in the territory covered by the Finance Guarantee during the entire currency of the loan and by participating in this agreement [we] have to submit to a curb on the Group's activities in the market in question." [1]

The Department considers this power necessary to prevent companies endangering repayment of existing loans by increasing buyers' indebtedness. The counter-argument is that the Department is powerless to prevent such a danger anyway, since if a British exporter does not supply, a foreigner will.

One may perhaps wonder whether Tim Renton was right when he said in the House of Commons: "The Export Credits Guarantee Department has in many ways become an export bank in all but name", determining entirely terms on which finance is made available and imposing curbs in a similar way to a commercial bank [41]. It has at least partly fulfilled the recommendations of the Faringdon Committee in 1916!

Complaints of interference in other than financial matters have been reported. One multi-national company was engaged

in an argument with ECGD over the inclusion of units to be supplied by its foreign parent company for a multi-million pound project to be supplied by the United Kingdom company. The Department took the view that a British company should have been invited to supply comparable units. There were substantial technical reasons for not doing so, but in any case it was totally unrealistic to expect such a company to supply a competitor's equipment. The company in question expected to win the argument, but greatly resented the time wasted [1].

While it must be recognised that the Department has considerable influence, it must not be forgotten that about two-thirds of United Kingdom exports are not covered by ECGD. It is an open secret that big companies like ICI and Unilever are not policy-holders. Other companies consider their knowledge of individual markets is much better than the Department's and create a reserve for bad debts. They believe this procedure costs less than paying ECGD premiums, even though the latter are allowable expenses for tax purposes.

Criticisms have been heard of the Department's effectiveness. It is particularly criticised for being inflexible, reluctant to take risks and failing to appreciate that business mentality abroad is not sympathetic to Civil Service methods. On all of these, judgments must be subjective because of the nature of the problems, but some limited comments may be made.

Inflexibility is a characteristic of most large organisations, where much of the work of necessity has to be done by relatively junior staff. A number of views have been heard to

the effect that in dealing with the Department the more senior the official and the more he is involved in direct discussions with industry, the more flexible he is likely to be.

Complaints of conservatism and reluctance to take reasonable risks are countered either with denial, or the apparently perennial reply: "it's the public's money we're dealing with." Since the form of accounts and reporting was changed from the 1974-75 year, it has been possible to make some quantitative assessment of this matter. At 31.3.76 the reserve on Commercial Account, i.e. business where normal commercial criteria are required to be applied, stood at 2.4% of the amount at risk, whereas the Department considers 3% as necessary (though why this figure is deemed appropriate is not stated). On National Interest business not considered appropriate for Commercial Account, no target level for the reserve has been set, but on the same date it stood at £132m against a maximum liability of £1m.[42] It is, of course, quite possible that if the Department had applied different criteria and been more liberal in granting policies, the reserves would have been little changed, but on the whole the figures do not support any charge of over-caution.

Critics seem to be on safer ground in criticising the Department for delays in reaching decisions. Although one Regional Director states that replies to requests for decision are sent out on the same day as the queries are received in 60% of the cases [1], over the country as a whole this does not seem to be the case. It is acknowledged by some members of the Department that there have been delays. Some may be inevitable because of the nature of the problems. Project finance is extremely complex, but one major contractor in

this field estimated four to six months as the normal time required to negotiate ECGD cover. Although hard evidence is difficult to come by, this appears to be well in excess of the time required in France and Germany, and some exporters fear that delays may lose orders.

Finally, in this commentary on ECGD activities, we may briefly note the extent of ECGD's intervention in financing proper. On 31.3.76, the Department's re-financing loans to the clearing banks amounted to £1628m. This figure represents 6.3% of the London, Scottish and Northern Ireland clearing banks' total deposits on the same date, or 14.7% of their sight deposits. Whether it would have been practicable, or more effective and desirable, to have insisted on these funds coming from the banking system (in addition to the 18% of non-interest bearing deposits), thereby curtailing current domestic demand, instead of supplying funds from long-term Government borrowings or taxation is a matter of political judgment. Since the amounts required for financing long-term export credit are expected to grow considerably, it seems clear that the United Kingdom banking system on its own, geared as it is to short-term lending, would be unable to cope. (See also addendum p.92)

Since the inception of the present scheme in 1972, the annual cost of the interest rate supplement, effectively a subsidy, has risen from £20m to £140m in 1975-76.

3.3 <u>The rôle of ignorance and incompetence.</u>

One cannot leave the subject of export in the United Kingdom without commenting on the lack of knowledge of export procedures in manufacturing companies and even in banks.

Perhaps because of the historically early specialisation in the United Kingdom, there exists a very high degree of competence in a limited number of institutions, but it seems sadly lacking elsewhere. It is a matter on which the Institute of Export comments frequently. Here, a few examples from the present research will be given.

Most clearing bank officials, including branch managers, not only know nothing about export procedures, they cheerfully admit it. The foreign branch officials, on the other hand, are generally very well informed, keen and conscientious, and banks rely on them to do all the foreign work. The problem is that in many cases all but the biggest industrial enterprises deal only with local branch managers, and the psychological effect, in an export context, is probably damaging. Even an industrialist who is reasonably cynical about the ability of his bank manager is likely to take the view that if export matters are too much for a banker, he cannot expect his own staff to cope. The fact that his bank will be only too willing to arrange for the assistance of one of its foreign branch staff will not necessarily eradicate this impression. In banks, there is rarely, if ever, any interchange of personnel between home and foreign branches to alleviate the difficulty. This particular problem will probably get worse as the "Finance of Foreign Trade" is to be dropped as a compulsory subject in the Institute of Bankers examination (though it will remain as an optional subject).

A company secretary had resisted a proposal to transfer the export office to his company from the distant and

inconveniently located parent company, on the grounds that the work was too complex. He admitted that he had never seen a Bill of Exchange - it was something he had learned about for his examinations twenty years earlier and then forgotten.

Although textbooks aimed at the practical exporter always stress that irrevocable letters of credit confirmed by a reputable United Kingdom bank are completely safe, in real life this safety is frequently relinquished. A full discussion would be lengthy and only peripheral to the main subject of this report, but the principal reason is the failure of an exporter's staff to conform with the terms of the letter of credit. Sometimes circumstances make this inevitable, but frequently it is sheer ignorance or incompetence. This matter has been discussed with several foreign branch bank managers and senior bank personnel; it is clear that at least half of the letters of credit negotiated are done so under indemnity because the documentation is defective. The Financial Controller of a £100m+ exporter was well aware of the problem, but found he could do little about it as his company's salary scales precluded him from recruiting appropriate staff. The fact that in spite of these problems very little trouble is encountered in practice raises the question of whether it is worth using this method of payment on its present scale, since the banks' confirming charges would be saved. The point is: if exporters lack knowledge in this elementary practical field, what knowledge can one expect in other aspects of exporting?

Other examples have already been quoted on page 67.

3.4 Conclusions.

The mechanisms available for the financing of exports are adequate, the key organisation, the Export Credits Guarantee Department, being better developed than in other countries. One of the reasons for this may be that United Kingdom banks have been less enterprising than their foreign counterparts in providing export finance, preferring to lend their money against the safe security of fixed assets, leaving the Department (urged by the more enterprising exporters) to take the initiative.

The only areas presenting substantial problems to the exporter are concerned with credit over two years, especially front-end financing. This is, however, an international problem not confined to this country.

Addendum

In the financial year 1976-77, the cumulative amount of fixed rate sterling export finance which was refinanced by ECGD rose to £2133m, representing 58% of the total. The annual interest cost of the scheme rose to £220m in the same year.

CHAPTER 7

FRANCE

1. Export financing institutions and practices

1.1 Introduction

France has been frequently quoted as a country which has offered its exporters a number of unfair incentives - loans at favourable rates of interest, tax rebates, cost escalation insurance, pre-shipment finance. It had already achieved this reputation in the early 1950s:

> "France, whose exchange retention scheme and substantial tax rebates for exporters make it easily the worst offender..." [35]

and it is clear from comments made during the Second Reading of the Export Guarantees (Amendment) Bill on 10th February 1975 that France is still regarded as guilty of malpractices. Suspicion of French activities in the field of export finance was also expressed by several who were interviewed during the current research.

While there may possibly have been justification for this feeling at one time, at least some of the criticisms of French practice seem due to a failure to understand differences between French and British banking systems. It will be necessary to examine parts of the French system in some detail in order to understand how some of these misconceptions have arisen.

1.2 The banking environment

After the last war, very detailed control was imposed on the banks to ensure compliance with Government policy on reconstruction. The country's foreign currency reserves were so precarious that immediate restrictions on imports were imposed during several crises up to the mid-1950s (even consignments of essential spare parts destined for France had to be retrieved from United Kingdom docks, so sudden was the application of these restrictions). Regulations governing France's international trade, though important, were only a small part of the economic controls which were introduced. Planning, administered by a competent and powerful Civil Service, became an essential feature of post-war economic life, and the banks were compelled to serve the aims of the successive plans by making finance available, sometimes at favourable rates of interest, for those activities which contributed to their aims. (Since they depended on the Central Bank to re-discount most of the commercial paper they held, they had little choice.) Official control of the banking system became firmly established, as will be seen from the following brief account of the major institutions concerned with the provision of export finance.

The Banque de France was nationalised in 1945 and is now run by a Governor and two Deputy Governors, with the assistance of a council of ten (nine appointed by the Government and one elected by the staff) and one inspector with limited powers of veto appointed by the Ministry of Finance. The Banque fulfills the usual functions of a central bank and an issuing bank.

The Conseil National du Crédit was formed in 1945 and is

responsible for decisions on national credit policy. The Chairman is the Minister of Finance, and the Vice-Chairman is the Governor of the Banque de France. The close link between the Conseil and the Banque is further illustrated by the fact that its permanent staff is supplied by the Banque. Among its functions are the formulation of credit policy and the regulation of credit techniques, as well as the rates of interest charged by the banks.

The Banque Française du Commerce Extérieur (BFCE) was formed under the provisions of the law which nationalised the Banque de France, and it began operations in 1947, though it was essentially a revival of the Banque Nationale pour le Commerce Extérieur formed after the first world war. Its shareholders are the Banque de France (24.65%), the Caisse des Dépôts et Consignations (24.65%), the Crédit National (15.77%) and other public bodies and nationalised banks. (The Caisse is an important public body. The Crédit National is not to be confused with the Conseil National du Crédit mentioned in the previous paragraph - it is a specialised institution, being the vehicle through which the Treasury provides finance.) The BFCE's objectives are to facilitate the financing of external trade, both imports and exports. In addition to providing direct assistance with external trade, it now owns shares in a number of financial organisations with specialised functions, e.g. factoring, multinational banks and consultancy organisations.

If one adds that the three biggest banks, the Crédit Lyonnais, the Société Générale and the Banque Nationale de Paris are also nationalised, it will be seen that the state

has direct control over a major part of the banking system. As will be seen, the French credit insurance organisation is also effectively a Government agency.

However, it is not only this complex interlocking of shareholdings which ensure the co-operation of the banking system in serving the needs of economic planning. Day-to-day control of the banks is much greater than in the United Kingdom; it is exercised by the Commission de Contrôle des Banques, the Chairman of which is the Governor of the Banque de France. Moreover, the Banque de France requires monthly returns from all banks showing credits over FF 200,000 granted to any one customer. The purpose of the returns is to check the total advances to individual companies, as it is the normal practice for a company to have several bankers. The Banque de France aggregates the credits granted by each bank to a company, and if the total advanced exceeds the agreed limit all the bankers are informed and an explanation is required from the company. Although one of the industrial sources consulted claimed that there had never been more than routine enquiries concerning the company of which he was the financial controller, another said that there was always a prompt request for an explanation if his company's credit requirements differed appreciably from those forecast. (The apparent difference is almost certainly due to the nature of the business carried out by the two organisations, since the latter company exports substantial amounts on short-term credit, and being part of a multi-national organisation may be called onto supply an overseas customer at short notice if another plant is overloaded, whereas the former has much more easily predictable requirements.)

From the discussions held with French industrial, banking and academic contacts, it may safely be said that the degree of control exercised on French banks reaches a level which is barely conceivable in the United Kingdom. The detailed nature of this control is well illustrated by the list of "les principaux mécanismes de distribution du crédit" published by the Banque de France, which includes nearly 150 forms of credit available to French businesses. When these were explained to a British bank manager, his comment was: "Most of these things would be settled in five or ten minutes in this country - either in my office or on the phone". [1] The facilities listed may be regarded as a highly formalised catalogue of the purposes for which banks are allowed to lend - and then only within the prescribed limits - rather than of special funds over and above those normally available. Whereas a British business would obtain funds for many of the purposes listed by means of a general overdraft, this is not so in France. A British businessman would probably regard an overdraft as the first source of funds to be considered, a French businessman would probably consider it last. In France an "avance en compte débiteur" or "débit compte courant" is essentially short term in practice as well as in theory and is more expensive than a loan under one of the formal credits. (The overdraft rate depends on a combination of the company size and the industry, which determine the basic rate, plus a supplement based on the maximum amount outstanding in any one month; furthermore there may be an additional charge imposed in times of credit restraint based on the increase in overdraft compared with the previous month. Because of this complexity, it is not possible to give a precise indication of overdraft rates.)

Ignorance of this simple but fundamental difference between British and French banking practice is certainly the cause of much of the misunderstanding which has been met. When British businessmen complain that there are special pre-shipment facilities available for French exporters, they do not realise that there is essentially no difference between these and a United Kingdom overdraft for similar purposes. French thinking requires that advances be used for specific purposes, and lenders wish to be sure that their funds do not become "core" lending as has happened in the United Kingdom. (In France there are legal difficulties in assigning debts other than by way of bills of exchange and a relatively low self-financing ratio means that few assets are available as acceptable collateral security.)

Control of the French banks by the authorities extends to the fixing of interest rates. There is therefore no scope for negotiation, and inter-bank competition takes the form of offers of better service. Competition on this basis appears to be quite keen with no understandings about not "poaching" on the preserves of another bank.

Similarly, at national level control is exercised in a much more precise way than in the United Kingdom. While total liquidity can be controlled quickly in the United Kingdom by intervention in the market, its effects are relatively indiscriminate, market forces determining where they fall. In France the tradition has been to influence particular sectors of economic activity directly, with a delayed effect on overall liquidity [43]. As a consequence, the history of French export (and other) finance is littered

with frequent changes in pursuit of the general economic objectives sought from time to time, and to cope with unforeseen events in economic and political life. In line with the tradition of exerting direct influence on the economy, control has been partly by the use of differential interest rates but mainly by the imposition of ceilings on bank advances for specific purposes. If a bank does not lend to its ceiling for export business, for instance, it is not allowed to use the funds for other purposes. The unused part of its quota goes into an inter-bank pool for use by other banks, so there is every incentive for the bank to use its quota to the full.

In order to encourage exports, the Banque de France traditionally offered the banks re-discount facilities on export paper at low interest rates (as low as 2% on short-term paper) with no quota being applied. The result was that at one stage "short term export credit paper...represented about a quarter of the Central Bank's advances [and] it was calculated that to raise the average cost of advances by one point, the Banque de France would have had to raise its rates to the money market by four points" [44].

The increasing level of preferential rate discounting had reached a critical level for monetary policy control. As far as advances for export were concerned, in 1970 they accounted for 58% of the Central Bank's fixed rate discounting and 36% of its total interventions in the banking system.

This led to a reform of the export financing arrangements in 1971, aimed at spreading the load, hitherto borne as to 70% by the Banque de France, 20% by the Treasury and 10% by the

banks. The tentative aim was to achieve in 1975 proportions of 50% by the Banque de France, 25% by the Treasury and financial markets combined, and 25% by the banks [45]. The banks undertook to provide finance in all cases where COFACE (q.v.) policies were in force. In return, the banks were to be guaranteed a favourable rediscount interest rate, but were not to be given full re-discount facilities. The position as from 22.6.76 was that (except for exports to EEC countries) the re-discount rate for medium term export paper was 4.5%, while interest charged to exporters (or to importers in the case of buyer finance) ranged from 7.25% to 8%, depending on the length of credit and category of importing country. While these rates are favourable to the institutions, it should be borne in mind that French banks carry out the functions usually performed in the United Kingdom by both the merchant and the clearing banks. Moreover, the banks were required to finance an increasing proportion of the advance from funds borrowed in the money markets at higher rates of interest - indeed it was reported at one time that banks were taking on export finance business at a net loss in the short term. From 22.6.76, the percentage of medium-term paper eligible for re-discount was reduced to a range running from 72.5% to 60%, depending on the length of credit and the status of the importing country.

Since contracts already in force in 1971 will take years to work through the system - for large projects on long-term credit, perhaps two or three years for manufacture, followed by ten years or more for repayment - rapid effects could not be expected. The extent to which the new scheme is achieving the desired results is difficult to ascertain, since the format

and detail of the national accounts undergo changes from year to year, and breakdowns are not always sufficiently precise. In particular, it is not always clear whether eligible paper is immediately eligible (mobilisable à la Banque de France) or eligible at some future date under the medium-term procedres.

The proportion of the Central Bank's total refinancing activities devoted to exports has fluctuated considerably from year to year. There have been fluctuations in the amounts refinanced and large amounts were made available for other purposês in 1972-73-74, both factors being reflected in the rather volatile ratio. The Provisional Report and Accounts for 1976 (Appendix 11) shows that 50% of all commercial banks' recourse to the Central Bank were for medium-term export credits and this appears to be somewhere near the underlying ratio. From the standpoint of its aim to reduce its commitments to industry while still offering necessary export facilities, the Central Bank appears to have been successful. Table 3 shows the position in 1975 and 1976 - close to the objectives stated on page 100.

1.3 Financing institutions.

There is not the wide range of financing institutions in France which is found in the United Kingdom. The important ones have already been mentioned in the description of the banking environment. Factoring and leasing companies do exist, but play an insignificant part in export finance.

An exporter's transactions are always with a commercial bank, which carries out the functions normally performed by both merchant and clearing banks in the United Kingdom.

France. Medium & long term export credit.

Financed by:	Sources of finance, by percentage of total. 1975	1976
Banks (eligible paper)	13.6	17.7
Banks (non-eligible paper)	13.1	12.5
Banque de France	52.3	52.6
Other	21.0	17.2
	100.0	100.0

Notes.

1. It is assumed that the eligible paper (mobilisable à la Banque de France) financed by banks is the paper which will be eligible at a later date. The non-eligible paper never qualifies for rediscount at the Banque de France.

2. "Other sources" are assumed to be Treasury and Euro-currency markets through BFCE. According to BFCE Annual Report 1975, all their finance was obtained in Euro currencies with the exception of one Treasury loan of unspecified amount.

3. For comparison, figures for short-term export finance show that in both years over 98% is eligible for rediscount. Short-term finance accounts for almost exactly one-third of all export finance outstanding. It includes pre-shipment finance of an unstated amount, which in the United Kingdom would be covered by overdraft or own resources.

4. All figures refer to amounts outstanding at the year end.

(Derived from data in Provisional Report 1976, Appendix 38 Conseil National du Crédit).

TABLE 3

1.4 Export finance facilities available.

The facilities available for financing exports are intended to meet industrial and commercial financing needs arising from export business. They are confined to goods and services originating in France, though materials and parts undergoing substantial processing after being imported into France for incorporation in large contracts may be regarded as French for this purpose. The regulations for granting these facilities are precise, and may be summarised as follows.

Pre-shipment finance.

"Crédits de trésorerie" or "crédits de préfinancement revolving" provide working capital for industrial or commercial undertakings doing business on a continuous basis. They are granted for periods of nine months to one year and are renewable. The approval of the Banque de France is required.

Although the purpose is to provide funds to meet routine requirements of exporting organisations, they may be granted even if there are as yet no firm orders on the companies' books. Nevertheless, the amount is determined by the companies' estimated turnover and the average manufacturing period. It is limited to 50 - 60% of forecast requirements.

Normally no special guarantees or collateral are needed, though the bank granting the credit may require the assignment of the client's credit insurance policy, a guarantee or a bond.

Funds are mobilised by acceptance credit, bills being drawn on the bank, which accepts and discounts them; alternatively bills may be endorsed to BFCE and then discounted. The

paper is eligible for re-discount at the Banque de France.

"Crédits de préfinancement spécialisés" are designed to provide working capital for specific large scale orders. Where sub-contractors are used, the splitting of the facility is compulsory in the case of sub-contracts exceeding F1.5m, and banks usually consider it desirable in case of smaller sub-contracts.

To apply for this facility, which needs prior approval of the Banque de France, the manufacturer must submit details of the contract; a cash forecast relating to the transaction showing monthly expenditure on manufacture, erection and starting-up (taking account of any supplier credit which the manufacturer may receive on bought-out items) on the one hand, and progress payments and receipts on the other hand; summaries of the last three annual balance sheets and profit and loss accounts; if possible, a statement of the financial position within the past six months. Any local expenses which may be incurred in the buyer's country are not eligible for financing in this way.

The decision of the Banque de France is based on its study of these documents. Approval is normally granted unless the manufacturer's own resources are considered adequate, in which case the application may be granted in part or turned down completely, or unless the manufacturer's financial position is considered too weak to justify undertaking the contract, in which case the application will be rejected. One banker with considerable experience of this type of financing

said he had never known a case where an application had been refused on the grounds that a manufacturer's own resources were too great [1]. It is, in fact, difficult to imagine a situation where a manufacturer constantly undertaking contracts of this size would be in such a position. On the other hand, it is clear that the Banque de France makes its decisions on the basis of accepted banking practice in France, looking at the financial situation of the applicant rather than at the desirability of obtaining a particular export order. Indeed, it is unlikely that many unacceptable applications will be forwarded to the Banque de France, since they are submitted through the applicant's own bank which will filter out weak cases in its own interests. The Banque de France's criteria in deciding whether an applicant's financial position is strong enough are that working capital should be adequate, and that own funds (capital + reserves + accumulated profits + blocked current accounts + normal provisions - accumulated losses and intangible assets of all kinds, e.g. patents, leases, research expenses not written off) must equal at least 10% of total short term liabilities to banks + 10% of medium and long term "créances nées à l'étranger" (q.v.) (the latter is the amount not covered by credit insurance).

The finance is made available on a monthly basis at the rate of 90% of the requirement for a particular month, as shown by the cash forecast.

Advances are for as long as necessary, though in practice initial approval is limited to one year as the Banque de France considers cash forecasts covering longer periods to be unreliable.

Finance is made available by discounting promissory notes in favour of the commercial bank providing the loan, or bills of exchange drawn on the commercial bank. This credit is then re-financed at the Banque de France.

In the case of contracts for F1m or more, with a manufacturing period of twelve months or more, the applicant may opt for finance at a fixed rate of interest instead of the usual variable rate. In this case, BFCE endorses bills of exchange and manages the financing.

It is possible to cover manufacturing risks by means of a COFACE policy (q.v.). This may be demanded by the bank as collateral security, though it is not compulsory.

Post-shipment finance - short term.

"Escompte commercial", or discounting of bills drawn on overseas buyers, is rarely used when payment is in French francs as "mobilisation de créances nées" is more advantageous for the exporter. However, where the mobilisation procedure is not available, a commercial bank may be willing to discount a bill for a client. The reasons why the mobilisation procedure should not be available in certain cases are obscure, but a banker stated that there are rare occasions when approval is withheld [1].

Where the bills are in a currency other than French francs, discounting is more common as interest rates on Euro-currency markets are often more advantageous to the exporter. The procedure is similar to that used in the United Kingdom. It

should be noted that as French currency is not so widely used in international trade as sterling, the French exporter is more likely than his British counterpart to receive payment in foreign currencies.

Foreign currency loans for short term transactions may be obtained. The procedure is similar to that used in the United Kingdom. While it is theoretically possible to obtain the loan in a currency other than the currency of the contract, this is discouraged by the banks because of added complications and exchange risks. This method of financing is not allowed in cases where credit is extended to the foreign buyer.

"Crédits de mobilisation de créances nées sur l'étranger à court terme" allow exporters to obtain finance for exports with credit terms of up to six months, or up to eighteen months with the prior approval of the Direction Générale des Douanes et Droits Indirects and the Banque de France. Except where prior approval is needed, the procedure is simple: the exporter signs a promissory note maturing in a maximum of ninety days in favour of his bank. The promissory note may be renewed if necessary. As a matter of convenience, and subject ot the approval of the Banque de France, a number of transactions may be consolidated in a single promissory note.

Post-shipment finance - medium term.

The financing arrangements for medium term credit are known as "crédits de mobilisation de créances nées à l'étranger à moyen terme". "Medium term" is defined by the Administration

and COFACE as 18 months - 5 years, by the Banque de France and BFCE as 18 months - 7 years. For most practical purposes the distinction is irrelevant as far as the exporter is concerned - indeed medium and long term finance is treated under a single heading in some bank literature provided for exporters. In this section, medium term means 18 months - 7 years.

Prior approval of the BFCE and Banque de France is needed for this type of finance.

Finance is obtained from the exporter's bank, acting either on its own behalf or as lead bank. The amount of the facility is normally 100% of the claim on the foreign buyer, excluding local costs, non-French components unless they have already been paid for in cash, and some types of commission. Six months interest is added to the principal.

The facility will normally be made available for the period agreed in the contract between the French supplier and the foreign buyer, subject to the prior approval of the Direction des Relations Economiques Extérieures (DREE).

Credits are mobilised by the endorsement of commercial paper (promissory notes or bills of exchange) to the exporter's bank, which in turn endorses them to BFCE if they have no more than three years to run. BFCE re-discounts this paper with the Banque de France. Meanwhile the longer term paper is retained in the exporter's bank's portfolio until it has no more than three years to maturity, when it is endorsed to BFCE which discounts it, and re-discounts with the Banque de France.

A COFACE policy is usually required by banks, and is compulsory for contracts with credit terms of more than three years. In those cases where BFCE considers that either the terms of the contract or the COFACE cover are not sufficient guarantee against possible default, it will require a counter-guarantee from the exporter's bank.

BFCE may provide finance on a "public buyer" or "private buyer" basis. Again, the BFCE and COFACE definitions of these terms do not coincide. Briefly, the BFCE definition of public buyer is broader and includes those private buyers who are covered by COFACE against political risks and the risks of delayed payment and insolvency. For these, BFCE finance is supplied unconditionally, whereas for private buyers finance is provided "sauf bonne fin", i.e. with recourse to the exporter's bank. The bank's risk is therefore increased beyond the normal 5% - 10% of the outstanding debt which is never covered by COFACE, and it will charge a risk commission.

The provision of finance may be staggered to correspond with part-deliveries if these are required by the terms of the contract.

The arrangements described are those which came into force in November 1974 and were still current at the end of 1975. As far as exporters are concerned, the principles have remained the same since 1st July 1971, though the rates of interest have altered. Nevertheless, the methods by which the banks have refinanced credits have been modified several times and should be considered subject to change if adjustments are needed to further the Government's economic policies.

Guidelines are laid down for the maximum period of credit to be granted:

light capital goods

contracts of F100,000	to	200,000	2 years
200,000	to	500,000	3 years
500,000	to	1,000,000	4 years
over 1,000,000			5 years

heavy capital goods

industrialised countries 5 years

(this is an absolute limit for EEC countries and is almost always applied to others.)

developing countries 5 years

(longer periods are considered for contracts over F10,000,000.)

Post-shipment finance - long term.

Long term finance is in the form of "crédits de mobilisation de créances nées à l'étranger à long terme". In French terminology, long-term finance refers only to that part of a contract exceeding the medium term limit of seven years. While ten years credit would all be classed as long-term in the United Kingdom, in France it would be considered seven years medium-term, plus three years long-term - this can lead to confusion in interpreting data.

From the exporter's point of view, there are a few procedural differences from the medium term system, the main one being that the application must be submitted to an administrative body comprising representatives of DREE, COFACE, Banque de France, the Treasury, and the Commission des Garantis

et du Crédit pour le Commerce Extérieur (which comprises representatives of several ministries, Banque de France, Crédit National and the Centre National du Commerce Extérieur). This is the key committee in the approval of long-term loans.

From the bank's point of view there are two transactions. The medium-term loan is re-financed as previously described, while the long-term loan is financed by funds obtained by BFCE from the money market or the Treasury.

Buyer credits - medium-term and long-term.

France followed the United Kingdom by introducing buyer credits in 1966. These are available for both long-term and medium-term credits, and generally correspond with the "mobilisation de créances nées à l'étranger à moyen et long termes". While there are necessary modifications of the formalities as the credit is technically made available to the buyer rather than the supplier, re-financing arrangements are the same as for supplier credits. Whether buyer or supplier credit is used is a matter of agreement between buyer and seller, the authorities having no preference for one or the other.

Rates of interest charged to the borrower are 0.15% higher than for supplier credits to cover the added risk as the borrower is domiciled abroad.

Crédits mixtes

A discussion of export finance in France cannot exclude mixed credits. Technically, these are combinations of one

of the standard means of finance and development aid. Instead of allocating aid completely separately from normal commercial transactions, the French Government has developed a method of combining the two in such a way that, according to its critics, it appears that cheap credit is being offered by the private sector. It is used for major contracts in less developed countries, the French Government providing aid at a low rate of interest to finance part of the contract, the remainder being financed by "mobilisation de créance née" at the standard rate. The rate quoted to the buyer is the average of the two, weighted according to the proportions of the two methods of finance. Thus, if aid were granted at 3% for 40% (the maximum permissible) of the contract and the current export finance rate were 7.5%, the resultant overall rate would be 0.4 x 3% + 0.6 x 7.5% = 5.7%.

In devising this scheme, the French were clearly thinking of expanding their exports beyond their traditional French-speaking markets. The scheme started with a loan to Mexico in 1963, with Morocco, Tunisia, Turkey, Chile, Pakistan, India, Indonesia, Colombia, Iran and others as beneficiaries in the next six or seven years. By the end of the decade, nearly 10% of bilateral French development aid was being used in this way.

It is claimed by one French source that an increase in French exports to Mexico from 3.5% of OECD capital goods exports to that country before 1963 to 6% in 1969 can be ascribed to this policy, as can similar success in Chile and Iran. No doubt these increases were responsible, at least in part, for the resentment aroused among politicians, officials, exporters

and financial institutions both in the United Kingdom and other countries. During the present research, one United Kingdom civil servant made the point that the United Kingdom had no objection to the French helping their former colonies, just as this country helps its own, but it was not in the spirit of international understandings to subsidise rates of interest in other markets - Iran, in particular, was mentioned.

The French view is that there is no objection to granting their aid in whatever form they wish. By assisting with several projects instead of concentrating the same funds on a single scheme, they claim to be spreading their aid more widely. While this is true, the very strong impression remains that France's main motivation has been the penetration of new markets. In this connection, the following quotation is relevant:

> "...with these mixed credit procedures, France was well placed to win numerous orders. If competition no longer depends on credit, but on other factors where she is less well placed, such as price, delivery, after-sales service, one may with good reason forecast a black time for our industry." [46]

The non-French interpretation of this would run something like: "If we can't compete on price, etc., let us compete on credit".

France's competitors regard this scheme as a straightforward subsidy. Clearly, if sales negotiations are pursued in a certain way, a potential buyer must be impressed by the apparent effort to win the order by offering favourable interest rates, and the psychological advantage to French negotiators must be considerable.

ECGD regards the French tactic as the provision of cheap credit. In applying its general policy of matching credit terms offered by competitors, it regards the overall rate, i.e. 5.7% in the example quoted, as the rate to be matched.

2. Export Credit Insurance - Compagnie Française d'Assurance pour le Commerce Extérieur (COFACE).

2.1 Origins and development.

The Compagnie Française d'Assurance pour le Commerce Extérieur was established by decree on 1st June 1946. While its work includes insurance of import credits, this is a negligible part of its business. It is a private joint stock company, the shares being held by the Caisse des Dépôts et Consignations, the Crédit National, the Banque Française du Commerce Extérieur, the nationalised banks and insurance companies and the Société Française d'Assurance pour favoriser le Crédit. It is administered by a board of fifteen directors appointed by decree after approval by the Minister of Finance and Economic Affairs. The directors are chosen in equal numbers from (a) persons with wide experience of foreign trade matters and representing the main professional associations, (b) representatives of the main trade unions and (c) persons with wide banking experience. There are also two Government Commissioners who may veto any decision taken by the Board of Directors.

COFACE acts on its own account in covering commercial risks in respect of short-term exports, though it operates under state supervision and, if necessary, with financial help from the state. It acts on behalf of the state in covering political, exchange and catastrophe risks for all export transactions, and commercial risks for medium- and short-term transactions. Separate accounts are kept for the two operations, but those dealing with its business on behalf

of the state are regarded as an internal matter and are never published. This makes it impossible to gauge the extent of its activity with accuracy, but it is generally believed to cover nearly as big a proportion of its country's exports as does the ECGD in the United Kingdom.

2.2 Policies offered.

The police globale corresponds very closely with the Comprehensive Guarantee of ECGD. Payments by confirmed irrevocable letter of credit are excluded, whereas under ECGD policies they may be included at the policy-holder's option. Certain countries may be excluded from the policy at the exporter's option, provided that the countries remaining to be covered offer a good spread of risk and a sufficient turn-over. Credits covered by this policy are normally up to 180 days for consumer goods, but may be up to three years for capital goods.

The police d'abonnement defines the general conditions of the guarantee, but leaves the exporter the choice of transactions to be covered. It is intended for exporters of standard or semi-standard capital goods which are made by series or batch production methods and it covers credits up to three years. Its purpose is to avoid the negotiation of a number of individual policies and as such is to be regarded as an administrative convenience rather than as essentially different from the police individuelle, which corresponds with ECGD's specific guarantee, being particularly concerned with heavy capital equipment, machinery built to specification, construction works and technical surveys.

For heavy capital goods, COFACE is prepared to cover political risks only, without covering commercial risks. Also, it is prepared to cover the pre-credit risk, without covering the credit risk itself. In both these respects it is unlike ECGD, though whether exporters are able to avail themselves of these exclusions in practice is not known, since the banks providing the finance may require the cover.

The cost of premiums varies according to the buyer, country, type of goods and type of policy. Unlike ECGD, COFACE publishes details of how they are calulated. Basic rates for each country and credit period, with pro rata temporis supplements covering manufacturing, plus flat rate charges for considering each application are the elements of the premium build-up. Taking all these into account, examples of premium rates are:

Consumer goods (up to 180 days)	public buyer: 0.31-1.48%
	private buyer: 0.50-1.50%
Capital goods (20% payment with	public buyer: 1.10-4.16%
order, balance over 5 years):	private buyer: 2.26-4.47%

These examples cover commercial and political risks, and in the case of capital goods, pre-credit risks.

In addition to the policies covering credit risks proper, other policies have been developed.

La garantie du risque économique, covering cost escalation during manufacture, is undoubtedly the one which has caused most comment. (Under EEC rules, it cannot be used in connection with exports to other community countries.) The purpose is to compensate manufacturers for increases in the domestic cost

of French materials and components used in the manufacture of exports, and is reserved for heavy equipment requiring long manufacturing periods. In return for a premium of 0.5% per annum on the total sum assured, the exporter is indemnified against any increase in costs exceeding the 3% which, when the scheme was introduced, was considered to be the normal rate of increase of international prices. Domestic indices are used to calculate cost increases, but in the case of very large contracts, expert opinion is called in. Settlement of claims is reported to be complicated and long drawn out [1].

With the rate of inflation increasing during recent years far in excess of original expectations, this was becoming virtually an open-ended commitment to cover exporters tendering for large-scale projects against cost escalation, so that they could offer fixed prices to the disadvantage of their foreign competitors. A United Kingdom report stated that by 1976 the French Government had made provision for an expenditure of £150m per annum to cover disbursements and was becoming increasingly worried about the cost of the scheme [1]. The researcher has not found any French source to confirm or correct this figure. Although United Kingdom sources continue to complain about the scheme, a French exporter stated in mid-1975 that difficulties were being met in obtaining cover [1]. and in mid-1976 the Banker Research Unit stated that cover was no longer automatically available [47]. COFACE seeks to avoid covering the risk by insisting on a cost escalation clause being included in the contract for the sale of goods and is said to be willing to offer cover only if it is impossible to get the buyer to agree to an adequate clause. Moreover,

the cost to the exporter is said to have been increased to a premium of 1%, with a 6% threshold, though no change has been made in the official literature.

COFACE issues policies to protect exporters against exchange rate fluctuations. Two types are available: in respect of export goods invoiced in a foreign currency, and in respect of goods and services bought abroad in order to fulfill an export contract. It is normally restricted to currencies commonly used in international trade, and when payments are due at least one year after the date of the contract. The current rate of premium is 0.648% per annum, calculated on the contractual outstanding balances from the date of contract to the final date of payment. The amount covered may be up to 100% of the contract value. The first 2.25% of any variation from the guaranteed rate of exchange is for the exporter's account, gains or losses in excess of this amount being for the account of COFACE.

This guarantee is similar to those available (but virtually unused) in the Federal Republic of Germany and the Netherlands. There is no corresponding policy available from ECGD, though it should be remembered that in French financial markets, especially in the days of strict exchange control regulations, there were fewer facilities than in the United Kingdom for arranging forward currency contracts. In the circumstances it is not considered that this cover has offered French exporters any special advantage.

A special application of this policy refers to losses

incurred by banks on adverse movements of exchange rates in respect of bonds and guarantees in foreign currencies.

Assurance-prospection and assurance-foire are policies covering part of losses incurred in seeking to open up new markets or participate in exhibitions. Although some success was claimed initially for assurance-prospection, it has been reported that little use is now made of these policies [1].

3. Commentary on export finance in France

The overall impression is that, as far as exporters are concerned, the system runs more or less as efficiently as in the United Kingdom, though with rather more bureaucracy. Differences between the two countries are due to dis-similar banking practices as a whole, rather than to incentives applied to exports as such.

In France, as in the United Kingdom, complaints are heard regarding the complexities of export procedures and the difficulties they pose. From the limited hard facts available, it seems that the French system does involve more paperwork, but the researcher suspects that the problem is analagous to that in the United Kingdom, discussed in the section "The rôle of ignorance and incompetence" - companies feel intimidated by strange procedures and resent mastering the requirements of the system.

The range of policies offered by COFACE is probably more extensive than is available from any similar organisation in the world, except ECGD. As already reported, it probably covers nearly one-third of French exports. There is no evidence to suggest that credit insurance is more easy to obtain in France than in other countries. As far as can be ascertained, given the differences in methods of calculation and the degrees of confidentiality in the two organisations, COFACE's premium rates are higher than ECGD's for short-term credit cover, and similar, or a little higher, for longer-term.

During 1975, the waiting period before paying indemnities was reduced to two months. This is generally more favourable

to the exporter than ECGD practice, though it does depend on the cause of the loss.

As in the United Kingdom, any problems of magnitude are in the field of medium and long term finance. No regular statistics are published in France to compare with Business Monitor M4 in the United Kingdom, but a single reference in a BFCE annual report states that 4.4% of France's exports are sold on medium and long term credit. The corresponding figure in the United Kingdom over several years is about 5%, so its overall problems appear to be slightly less. (The figure of 4.4% is surprisingly high, if the United Kingdom figure is correct, since a smaller proportion of France's exports consist of capital goods. Unfortunately, no way has been found of breaking down published statistics into the types of goods which might, and might not, reasonably be expected to require extended credit. The explanation may be that France's exports to developing countries having expanded at a faster rate than those to industrialised countries in the early 1970s, they are supplying a higher proportion of these goods on credit terms than is the United Kingdom, but it has not been possible to come to any conclusion on this.)

CHAPTER 8

FEDERAL REPUBLIC OF GERMANY

1. Export financing institutions and practices

1.1 Introduction.

Regarded for nearly a century as the United Kingdom's principal European competitor in the supply of capital goods, the Federal Republic has attracted accusations of unfair competition in financing exports - the general background has already been given in describing the origins of ECGD. The research on which the present chapter is based was aimed not only at establishing the methods of export finance used in the Federal Republic, but also at ascertaining whether any special aid is in fact available to the German exporter.

1.2 The banking environment.

From a businessman's point of view, there are certain differences to be seen when comparing the banking systems in the Federal Republic and the United Kingdom.

Companies rely on banks to a far greater extent in Germany, where they are much more influential in the running of industrial enterprises than in the United Kingdom, partly because of this greater reliance and partly because banks have considerable voting power through their own shareholdings and the shareholdings of their customers which are entrusted to them.

As in France, banks are more willing to finance specific transactions than to make general advances against fixed assets.

While it is common for companies to have more than one bank, the major one in a company's activities, its "house bank", will undertake the functions performed by specialist institutions in the United Kingdom. As far as export finance is concerned, this means that the intervention of a merchant bank or other export finance house is unusual. Even where an intermediary is used, as in Forfaitierung (q.v.), the house bank will usually make the arrangements.

In the Federal Republic, the banks (including the Central Bank) are much more independent of the Government than is the case in the United Kingdom.

1.3 Financing institutions.

The normal sources of finance are the commercial banks. The main differences between finance for home and export trade are that for export a bank may require a credit insurance policy to be taken out and (where appropriate to the importing country) Bills of exchange (for subsequent re-discounting) to be used. The financing of exports is assisted by two specialist institutions, which are now described in some detail.

The Ausfuhrkredit Aktiengesellschaft was set up in 1952 by a consortium of banks led by the Deutsche Bank, as a non-profit-making corporation for discounting export bills. In 1966 it became technically a private limited company, Ausfuhrkredit-Gesellschaft m.b.H., but is still known as AKA. The 23

banks which originally formed the consortium had grown to 53 by April 1974, and the original capital of DM20m had been doubled.

In 1953 it took over the credit line extended to the Kreditanstaltung für Wiederaufbau and by 1974 had the following sources of funds:

Credit Line A	funds provided by the consortium banks for supplier credit and available only to member banks, for credits of at least 12 months and a maximum equal to the period covered by credit insurance, where this is demanded.
Credit Line B	rediscount line with the Bundesbank (the Central Bank), available to all banks in the Federal Republic, for 12 to 48 months credits.
Credit Line C	first used in 1972; funds provided by member banks for buyer credits and available only to member banks, the maximum credit period being the period covered by credit insurance.

At the end of 1975 the credit ceilings, i.e. the cumulative totals outstanding at any one time, were A line DM4bn, B line DM3bn, C line DM1bn, with an additional 50% of these figures permitted for credit approvals (to be drawn down later).

AKA members are committed to taking over 60% of the Solawechsel (promissory notes) relating to A line credits

in proportion to their shareholdings, the house bank organising the loan being responsible for discounting the remaining 40%, or in a ratio of 75:25 for credits of less than two years. The maximum permissible credit is the invoice value, less pre-payments, less 15% or 10% according to insurance cover (20% or 15% respectively until 1975). Line C credits were originally financed by long-term book credits in the same ratio as for line A, but it was planned to replace this by an issue of bearer bonds in 1976; these will doubtless find their way on to international financial markets. C line credits, being buyer credits, are granted for the full amount of out-standing payments on a contract.

All requests for credit under lines A and C in recent years have been granted. On the other hand, those under line B ran against the upper limit of credit approvals in 1975 and were being refused in early 1976. The Bundesbank, on grounds of its monetary policy, declined to raise the limit. By definition, refinancing is by the Bundesbank, the instruments being the exporter's Solawechsel, backed by his house bank and AKA. The Bundesbank requires the exporter or his bank to finance 30% of credits granted to overseas buyers.

A feature of line B credits is that payments received by the exporter must be used in full to liquidate the AKA credit, unlike line A credits, where receiptsare applied in proportion to AKA's and the exporter's participation. In view of the strict limit of 48 months on these credits and the high self-financing ratio, parallel financing from line A or other source is often called for.

AKA's rules for eligibility are strict but conventional. Firm contracts must be signed, though there is provision for advance commitments for contracts under negotiation; the credit is normally tied to a specific contract, though a revolving limit can be agreed if this is appropriate to the exporter's business; contracts must normally have export credit insurance or other guarantee, though exceptions may be made for particularly risk-free contracts (in fact, over 80% of line A and over 90% of line B credits have this cover.) There are other provisions regarding security and formalities, calling for no special comment.

A and B line credits may be arranged so as to be drawn by the exporter as pre-shipment finance.

Interest rates for AKA credits are variable. The line B credits cost 1.5% above the Diskontsatz (the rate at which the Bundesbank discounts eligible paper) and this itself is varied as an instrument of monetary policy. The rate charged for A line credits fluctuates more - at the end of 1973 it reached 11%, i.e. 4% above the Diskontsatz at the time. AKA calculates that average interest rates have been:

	A line	B line	C line
1956-75	7.42%	5.70%	
1961-75	7.48%	5.80%	
1971-75	8.86%	6.61%	8.87%
1975	8.57%	6.0 %	8.65%

However, these figures in themselves are not an indication of the cost to the exporter of financing a transaction, since topping-up finance is also required. Taking the hypothetical

case of a contract concluded in 1966 (terms of payment: 5% with order, 10% on delivery, 85% in sixteen equal six-monthly instalments starting 18 months after contract date) and assuming the maximum permissible use of A and B line credits, with topping-up at 1% over A line rates, the average rate would have worked out at 7.54%. Had finance been obtained solely for the credit period, i.e. without bridging production and shipment periods, the figure would have been 7.98%

Under the international "gentleman's agreement" in 1974, the exporter is required to pay an average interest rate of at least 7.5% on his refinancing facilities. There is thus a possibility that finance incorporating line B credits could contravene this agreement on the governing date (the day on which the export credit technically starts). In such a case the exporter would be required to repay his loan early and substitute dearer finance.

In addition to interest charges as shown above, various charges are also applied, but as they do not significantly affect the cost are not detailed here.

The second specialist organisation is the Kreditanstalt für Wiederaufbau (KW) (Reconstruction Credit Institute) which occupies a key position in certain types of export credit finance in the Federal Republic. As its function has changed substantially since its operations began on 2nd January 1949 and it has played such an important part in the provision of finance throughout its existence, an outline of its development follows.

Its form is that of a bank, though it is not subject to the usual German banking laws. Its primary purpose, as its name implies, was to finance the reconstruction of the German economy after World War II, "making it possible to carry out reconstruction projects by providing all sectors of the economy with medium- and long-term loans in so far as other banks are not in a position to procure the necessary funds."

Initially, its major source of finance was to be the European Recovery Programme counterpart funds. (It is perhaps now necessary to recall that under the Marshall Plan, the United States made available dollars for the import of essential commodities into European countries. Importers paid the domestic value of the commodities into the "counterpart funds", which were then used for rebuilding war-damaged economies.)

It was originally the intention of the Allied Military Governments that the use of counterpart funds in Germany should depend on prior German contributions from the capital market, but following the very modest subscriptions to two loans in 1949 - probably floated with the intention of showing the Allies that efforts were being made to obtain funds, rather than in a serious belief that there would be a substantial response - the counterpart funds did in fact become the most important source of funds in the early years of the KW. The notes to the 1973 accounts show that over DM6bn (56% of liabilities to all banking institutions including the Federal Republic and the Länder and - if one includes DM247m derived from resources of ERP special funds - 21% of total liabilities)

was still attributable to Marshall Aid after 25 years of operation. The original source of funds is probably of little interest to a consideration of present-day export finance, but it may throw light on certain beliefs regarding German activity in this field, especially the conviction that American funds have helped Germany to give favourable export credit terms. To the researcher's surprise, this view was expressed several times during discussions, not only by older executives but also by some who had not even started their business careers in the 1950s.

Until 1953 funds were used predominantly for industrial reconstruction. Although the category of "export-intensive industry" appears from 1950 to 1953 in KW's commitment of funds, the sources were KW funds and not ERP. Export financing also appears in KW commitments from 1950 onwards - again these were obtained from KW funds initially and it was not until 1954 that ERP counterpart funds were utilised for this purpose. However, although export financing nominally came from KW funds, rediscount facilities were made available by the Bank deutscher Länder (the forerunner of the Bundesbank), originally limited to DM110m and subsequently increased to DM600m. This credit line was granted, at least in part, in anticipation of counterpart funds being made available. Moreover, it was at a preferential rate of interest.

The main aim of the initial reconstruction having been achieved, the emphasis changed from 1954 onwards. The Gesetz über die Verwaltung des ERP-Sondervermögens (Law on the Administration of the ERP Special Fund) of 31st August 1953 required the ERP fund to be administered separately on a

commercial basis. AKA had taken over the KW export finance credit line at the Bank deutscher Länder in the spring of 1953 and KW ended its activity in this field. This is essentially the position today, with AKA undertaking finance up to four years and KW the longer term maturities. Since banks were at that time unable to provide finance for long periods, KW undertook this function as a credit race appeared to be getting under way in the export markets of the 1950s.

An export finance fund of DM100m from ERP sources, augmented by DM100m from institutional investors, was set up. This was increased by another ERP line of DM260m, later made up to DM500m, matched by the same amount from KW funds.

As suggested above, the original source of funds is not specially relevant to present-day activities of the KW and for practical purposes itis best regarded as the agency through which the Federal Government channels its funds for a variety of purposes, both at home and abroad. As far as its contacts with foreign markets are concerned, development aid, untied financial loans and funds for German subsidiaries abroad are the major sectors of operation, in addition to export financing proper. There is undoubtedly some confusion, or even suspicion, of the KW's motives in dealing with all these activities. The fact that for some purposes KW groups together export finance, untied official loans and funds for German subsidiaries abroad in its annual accounts and reports probably adds to the confusion. Nevertheless, all of these activities, as far as can be ascertained, are kept quite separate.

Although development aid and untied loans fall outside the terms of reference of the present research, since the Federal Republic is unique in administering these through the same organisation as its long-term export finance proper, these aspects of the KW's activities are considered briefly to see whether they shed any light on its underlying attitude to German exports.

KW's figures show that <u>development aid</u> started modestly in 1958, grew rapidly until 1963, declined until 1971 after which it rose again. By the end of 1973 total aid granted had reached about DM15bn, other forms of development aid taking the form of technical assistance and contributions to international financing institutions such as IBRD. How much this has aided German exports is not clear. One might suspect that it would encourage the recipients to buy equipment from that country even if they were not formally tied to buying from the donor. Even if there were no official ties, there is obviously scope for them to be applied in practice, since projects for which they are granted are individually appraised.

In the early days motives were perhaps not entirely disinterested in the promotion of German exports. KW concedes that "the aims of German assistance have from the outset...

been almost inevitably entangled in a network of the most varied motives". Other criteria for the appraisal of projects are now applied - very different from those of the early 1960s. Social conditions in the recipients' countries now assume a greater importance and the commitment of loans to the delivery of goods and services supplied by the Federal Republic is said to have been almost completely abandoned. That this shift was already well under way in the mid-1960s is suggested by criticisms then made by German industrialists. In a survey commissioned by the Institue of Export (UK) and carried out circa 1967, a number of German business men complained that of the great sums paid out by the Federal Government, only a relatively small proportion had been returned in the shape of export orders [48]. In 1965, 55% of all aid took the form of untied loans and in 1966, 68%. In spite of these criticisms, German exporters considered that a withdrawal of this untied aid would have an adverse effect on exports, since executives from developing countries studied in the Federal Republic and buyers of equipment were trained by German Development Aid experts.

From April 1972 the Federal Government eased terms for capital aid loans, and the practice has become to grant these loans at standard Development Aid Committee terms - 2% per annum interest for 30 years, with a ten year grace period. For the group of 25 least developed countries, the rate is 0.75% for 50 years with a ten year grace period. Moreover, Germany is moving faster towards covering part of the local costs of projects than are other DAC countries, although strict criteria are applied. Just under 10% of aid is designated for this purpose, compared with a DAC average of about 5%, though this has been seen by some non-Germans as an inducement not offered by other countries to influence the placing of orders

in the financing country.

A careful examination of the complete list of projects which have received development aid from the KW is recent years suggests that they are all projects which would have qualified under most countries' programmes, and so cannot be regarded as an illicit way of providing cheap finance.

Another form of finance for foreign trade administered by KW is an indirect one - untied financial loans. The level of these has fluctuated considerably and is usually determined by one or two major loans. Although some loans have been made to foreign state banks to enable payment to be made for German goods already delivered, e.g. a loan to Romania in 1973, these are really forms of debt re-scheduling which other countries would deal with through other agencies. The loans are, in fact, often concerned with securing sources of supply for essential imports more than with exports.

As with development aid, a list of the projects financed by untied aid gives no grounds whatever for believing that subsidised finance is being granted for normal exports.

KW's export financing proper is concerned with long-term finance for capital goods, usually taking over the longer maturities, AKA providing finance up to four years. However, "Mischfinanzierung", or mixed financing, where development aid funds are supplemented by export credits. This is similar to the crédit mixte used by the French, but has not attracted the same criticism - possibly because fewer schemes have been involved. In 1973, DM21m was committed in this way,

of which DM19m was in respect of a single energy project in Argentina. It is suggested in the 1975 annual report that an extension of this technique would allow the scarce but cheap funds to be stretched further for the more advanced of the poor countries. This argument, it will be recalled, has been used by the French for many years, and the KW may regard its Mischfinanzierungen as a form of retaliation or self-defence.

The overall picture with regard to KW's export financing activity is that for some years it has provided approximately 60% of the finance in those projects with which it has been associated. These have been almost exclusively in developing countries (97% or more each year), as would be expected with long-term finance.

Buyer credits, which were introduced following the passing of the necessary legislation in 1960, have predominated in recent years. The Institute itself states that supplier credits are preferred only in cases of unsatisfactory credit-worthiness of the buyer or a weak foreign exchange position of the buyer's country.

KW's annual reports show that in recent years 70% of the funds advanced have come from KW resources, the remaining 30% from ERP funds. KW funds are obtained in the financial markets at commercial rates; the nominal rate charged for ERP funds is not known. From the point of view of export competitiveness, the important figure is the rate charged to the borrower. This is negotiated individually for each contract - at the end of 1973 they were, in principle, 8.25% for buyer credits and 8.75% p.a. for supplier credits, plus commitment

and other fees.

The assignment to KW of a valid credit insurance policy, together with any guarantees and/or securities stipulated by the insurers, is essential, except in certain approved cases where the guarantee of the exporter himself is needed. Other normal information on the seller's and the buyer's financial situation is also needed.

No published information has been found to show on what basis credits financed by ERP funds are granted.

Recent newcomers to the export finance world are the mortgage banks in the Federal Republic. The banking regulations were amended in 1975 to allow them to refinance 50% of commercial banks' credits for large projects. The Government does not insist on the mortgage banks assuming responsibility for a proportion of any loss which might arise. The stated purpose of this move is to facilitate long-term finance of exports, so it is reasonable to assume that funds for this purpose are expected to become more difficult to find [49].

1.4 Export finance facilities available.

Export finance is normally obtained from the commercial banks in the same way as for home trade finance, with support provided by the specialist banks described. It would not call for further comment but for the fact that in United Kingdom export circles demands are heard from time to time for the provision of non-recourse finance, as is said to be available to German exporters. From discussions in United Kingdom Government departments it is evident that these demands are still being repeated at the present time. When pressed, exporters are unable to provide details of the scheme - in itself this is not surprising, since export executives tend to pick up general information during the course of their work and usually have neither the time nor the specialist knowledge to pursue the matter further. This lack of precision should not be taken to mean that there is no foundation for the belief in the existence of such facilities.

The basis of the stories could well be a system known in German as "Forfaitierung", a hybrid word derived from the French "à forfait" (which itself is sometimes used in German) meaning that an inclusive price is paid for a claim on a foreign buyer. The main characteristic of this form of financing is that the financial institution offering the service agrees to buy a claim from an exporter without recourse to the latter - this is the essential difference from the normal discounting of a bill of exchange. In many respects it resembles some forms of factoring, but is usually concerned with medium term claims (one to five years) rather than the normal maximum of twelve months for export factoring; it is concerned with transactions of a relatively high minimum value rather than

the continuous business associated with factoring (though it is unable to handle very large amounts in a single deal); although arising from individual transactions, the debts are "abstract" and may be traded without reference to the exporter or the goods in any way; finance is often ultimately provided from a third country; unlike factoring, it does not require an appropriate organisation in the importing country, or even that the buyer should have any knowledge of the system; while it is possible to "forfait" book debts as in factoring, the bill of exchange is the more usual debt instrument.

Why should a German exporter choose this method in preference to bank finance? Two main reasons may be adduced, depending on circumstances.

The obvious immediate advantage is that he receives cash. Since there is no contingent liability in case of default, he has greater financial manoeuvrability and is in a more favourable position to rais further finance for other purposes. (Although an exporter may be insured against default with conventional financing, there is alway a proportion at his own risk, probably involving a similar self-financing ratio, which can amount to an appreciable sum in the case of a series of medium term transactions. Additionally, there is always a time lag beforeany insurance claim is settled. Also, there may be occasions when credit insurance is not available, possibly for technical reasons, e.g. there is too big a foreign content in the finished product or because trade with the German Democratic Republic is not insurable under the Government scheme.)

In other cases, there may be too great a risk or the conditions too specialised for conventional financing institutions. For instance, Germany has a substantial trade in capital goods with developing countries and Eastern Europe. C. J. Gmür of the Crédit Suisse suggests that over half of all Forfaitierungen are in respect of exports to these countries [50] and B. T. Häusermann attributes most of the à forfait transactions in Switzerland to German exporters. This, coupled with the fact that some financial institutions engaged in this business buy claims denominated in Verrechnungseinheiten (VE), i.e. the units of account used in bilateral East-West German trade, suggests that these specialised conditions are a strong reason for using this type of financing arrangement. In this connection, mention may be made of a small Austrian bank which very briefly advertises: "Specialists in East-West trade - Switch deals - A forfait", the implications of which are obvious in this context.

As far as the exporter is concerned, procedures are very similar to those used in normal financing. Payment may be made by the importer, or an intermediary, by Letter of Credit, Bill of Exchange (which may be claused to restrict payment to a clearing account) or occasionally by book debt. The debt will then be discounted. A reading of the literature issued by banks dealing in this kind of business shows that it is subject to the rigid conditions one would expect with conventional financing. One would surmise that once continuous business had been developed, access to finance and dealing with the associated procedures would become less difficult so that exporters would find this no more burdensome to handle

than their other financing. Nevertheless, the clear impression gained is that in some respects it definitely may be more troublesome than conventional methods - there is no certainty that funds will be available at any given time for transactions in countries with a high risk factor and the standards of commercial probity and the financial strength of the buyer are probably even higher than with conventional financing. No evidence has been found that these without re recourse transactions are any easier for the exporter to negotiate than ordinary bank finance, and certainly none to suggest that they are available "for the asking" as seems to be thought by some British exporters.

There is little hard evidence available as to the extent of this practice. The only published information is in a single book [51], in a few articles and in the promotional literature of the banks engaged in this business. Häusermann, the author of the book in question, goes into considerable detail regarding technicalities from the banker's rather than the exporter's point of view. Moreover, as a Swiss, he is not primarily concerned with the German exporter, though this need not be a drawback for the purpose of the present survey since much of the Swiss business emanates from Germany. As to its extent, he quotes a number of estimates made in the late 1960s and early 1970s. Two examples will suffice to show how wide is the possible margin of error. One article dated November 1968 quotes the Deutsche Bank AG as estimating "well over DM100m" as the total, while another, less than six months later, suggests "about 1% of total German exports", which works out at ten times the previous estimate.

Häusermann's own estimate illustrates the difficulties in attempting to reach a conclusion. It is not known how many banks are engaged in this type of work, and not all are compelled to make public their accounts. He starts from the published balance sheets of two of the three main banks known to be dealing in à forfait trading in Zürich, assumes that all the bills of exchange relate to Forfaitierungen, makes estimates as to the proportion which they will have retained in their own portfolios and the proportion of all Swiss business for which they are responsible. He then estimates, in effect, that 85% of Swiss business originates in the Federal Republic and that this represents half of total German Forfaitierungen. (Concerning the last assumption, he notes that reputable German financial institutions have made estimates ranging from 20% to 70%.) The scope for error is acknowledged to be great, but he estimates somewhere between DM0.9bn and DM1.4bn for 1970.

He appears to overlook the fact that this will represent the amount of claims in existence at any one time and not an annual rate. If an average time to maturity of 2.5 years is assumed for the outstanding bills, an annual rate of less than DM500m may be assumed for 1970, subject now to an even wider range of possible error. This estimate is not inconsistent with another quoted by Gmür of $500m per annum on a world-wide basis, which in effect is mainly the Federal Republic, Switzerland and Austria. If correct, less than 0.5% of the Federal Republic's export trade would have been financed in this way and no more than 5% of the medium term credit business.

What type of financial institution engages in this business and what are the sources of funds?

Although the term Diskont à forfait is mentioned in the 1947 edition of a Swiss banking reference book (Handbuch des Bank--, Geld- und Börsenwesens der Schweiz) it seems that only small private banks engaged in this business in the early post-war years. According to Häusermann, one West German bank founded in the late 1940s offered à forfait services in order to attract customers. At that period such a service would obviously have been attractive, and this bank was so successful that it is nowa substantial institution. The system in general grew to the extent that the big banks entered the market, though discreetly. One of the big three, the Deutsche Bank AG, became active in this field, while the other two regarded it as a complementary service to meet the wishes of their customers. As a result of the intervention of the big banks, some of the smaller ones have withdrawn from the market, though others still regard these services as a means of getting new customers. (This strongly suggests that the system is not sufficiently widespread for it to be easily available.)

The banks may buy claims à forfait to retain in their own portfolios, to sell to other financial institutions, either with or without their own endorsements on the the bills of exchange, or may simply act as intermediaries. The opinion of one German bank official in the United Kingdom was that his own bank kept very few, if any, of these claims in its own portfolio, and he doubted whether the other big banks did. However, he stressed that he did not know for certain, as

this would be a matter for high-level decision and very few of the bank's personnel would have access to this information [1]. Gmür states that banks may retain a small portion of these assets for their second-line liquid reserves, as they normally give a high yield. After sale by the exporter's bank, these claims may be held temporarily until a long-term home is found with aggressively run financial institutions. Interest arbitrage also attracts holders of long-term paper who borrow at relatively low rates of interest in the Euro-dollar markets - Gmür states in passing that some have had their fingers burned. According to him, building up a loyal and financially strong clientèle willing to invest in these claims is one of the major tasks of banks handling this business [50]. (This may be why one of the relevant Swiss banks has opened an office in London.) The placing of Forfaitierungen is done on an international basis, with the main centres in London, Paris, New York (for Latin American debts) as well as Zürich and the West German financial centres. Although Austria, because of its rôle in East-West trade, is active in arranging à forfait transactions, the ultimate source of most of its finance is believed to be London.

As far as German exporters are concerned, the main channels used in addition to the big banks are a quite small number of private banks who transmit, either as intermediary or by sale, the claims to a much smaller number of Forfaiteure, mainly in Zürich. The availability of finance for sales to different countries will depend on the view of these institutions of the risks involved, and facilities offered will vary. To illustrate this, the following extracts are taken from the

promotional literature issued by one of the better known Zürich banks: "Currencies: Swiss francs, German marks, US dollars; additionally, at the present time, French francs, Belgian francs, Dutch guilders, Austrian schillings and Italian lire, also possibly Swedish crowns, Norwegian crowns and Danish crowns" (May 1971) and five months later:"...Swiss francs, German marks, US dollars, French francs, Belgian francs, Dutch guilders, pounds sterling, Italian lire and Norwegian crowns...other currencies are possible according to the state of the market." The same bank's annual report for 1973 stated: "The possibilities of placing non-recourse transactions with third parties have diminished." The 1972 annual report of a similar bank notes: "First-class Spanish paper was again favoured by investors. A constant demand for investments in Portugal could not always be satisfied... Demand for funds covering export sales to Yugoslavia ..remained so strong that the market could only partly absorb the paper... Transactions for Poland and Romania with repayment periods of seven and eight years could be placed in large amounts without difficulty. Contrary to the previous year, substantial amounts were made available for exports to Czechoslovakia..."

Those engaged in this business lay stress on the probity of others in the chain of transactions. As it is not certain that a Bill of Exchange can in fact be ceded without recourse to the drawer under all legal systems, faith must be placed in declarations of the type "...we categorically confirm that we relinquish all rights of recourse against yourselves as drawers of the Bill, on behalf of ourselves and all holders in due course." Foraiteure in turn must be confident that in case of

default investors in this type of paper will not in fact take legal action against an exporter. Furthermore, they are careful to ensure that paper does not arrive in the hands of an individual or organisation which might be unacceptable on personal or political grounds to the importer, exporter or the government of either. As in some other types of international financial transactions, business is frequently done by telephone, further underlining the need to deal with institutions and individuals whose reputation is beyond question. For policy reasons which are not directly relevant to the provisions of export finance, Swiss Forfaiteure generally work with the German exporter's bank, which makes a modest charge for its services either by way of commission or its turn on the discounted paper. It is unusual for the Swiss institution to deal direct with the German exporter.

Although enough business has developed for major Swiss and other banks to have established subsidiary and associate companies in Zürich for the purpose of participating in à forfait financing, it remains relatively small, specialised and subject to fluctuations in the currencies which are acceptable, the importing countries for which facilities are available, and the interest rates charged. Conventional financing, of ourse, suffers from similar fluctuations - insurance cover can be withdrawn or restored according to circumstances and interest rates vary, but as these are in large measure determined by Governments and other big institutions responding to large scale influences over longer periods of time they are usually much less volatile.

The cost of finance in this form is determined by the current medium term rates in the Euro-currency markets. The principal institutions publish lists at regular intervals indicating the rates for different currencies, importing countries and maturities. They may quote separately for the "risk premium", or include it in an all-in rate. This extra charge will depend on an essessment of the economic and political situation in the debtor country, the quality and reliability of the debtor and guarantor (if any), the length of credit required and, exceptionally, the currency of the receivables. These rates become established by market forces, being the consensus of subjective opinion rather than detailed risk calculations. Although Häusermann goes into some detail on risk estimation, the one direct contact it has been possible to establish during the current research is quite certain that the interplay of opinion in the market is far more important than any formal calculations.

An examination of such a rate list published in March 1975 shows discount rates varying from the equivalent of 0.75% per annum above the corresponding Eurocurrency rate for importers in economically sound countries such as the Netherlands, to the equivalent of 5.5% per annum over the corresponding Euro-currency rate when the importer is located in Yugoslavia. The margins quoted seem very reasonable for the exporter, bearing in mind that they cover the financial institutions' profit and the risk premium. It is not possible to comment on the cost of this risk element without knowing what the cost of official credit insurance would have been. Two British bankers with current experience of export finance expressed the view that

the rates were keen and that their own banks could not have offered cheaper rates if a similar system were used in the United Kingdom.

Although a major Swiss bank states that "financing without recourse is naturally more costly than conventional export financing", there may well be occasions when this is not so. There have been occasions when medium term Eurocurrency loans have been cheaper than domestic finance, and Häusermann reports that he formed the impression that at times German exporters have had the advantage of this interest differential.

In considering the rates quoted, it must be borne in mind that they are published as an indication and not as a firm commitment, but in view of the international standing of the parent bank they are probably an accurate reflection of the rates actually charged. Furthermore, the larger institutions which publish rates are probably the most conservative and deal in only the safest paper - for instance, the list itself states that Verrechnungseinheiten are not accepted for transactions with the German Democratic Republic. The annual report of another bank states: "We continue to purchase mainly claims which are guaranteed by first-class banks or companies. In Western Europe we sometimes finance non-recourse transactions with the commercial risks covered by a first-class credit insurance company". The literature of other companies makes it clear that they follow similar policies.

(The rates do not include remuneration of the exporter's bank or other intermediary, but in standard type transactions

it is said to be small.)

It has not been possible to determine the rates charged by the smaller companies dealing with less conventional export business. It is difficult to identify them, at least within the scope of the resources available for this research, and it is thought unlikely that much information would have been made available regarding their less publicised activities. Approaches by correspondence to one bank which advertises from time to time brought no response. It must be assumed that the charge for the risk element will be considerable in cases where blocked currencies are being traded, though the West German exporter will be able to adjust his prices to take this into account. Alternatively, one of the financial intermediaries or the Forfaiteur himself will make an appropriate adjustment to his conversion rate.

If some <u>evaluation of the importance of Forfaitierung</u> is to be attempted from the available literature and the very limited contacts which are possible in this country, it must be that non-recourse financing makes a small but useful contribution to German export trade as a whole, and may well be an indispensable aid to some companies. It is probable that, insofar as trade with Eastern Europe is concerned, the system provides a mechanism for smoothing out imbalances in bilateral trade.

Undoubtedly the growth of this method of financing owes something to the special conditions prevailing in Germany in the early post-war years. Insofar as transactions could be financed from third countries, it would obviously have been

welcome in the days of financial stringency. For geographical and linguistic reasons, as well as its established position as a centre for international finance, Switzerland would have been such a convenient source. Unfortunately, no evidence is known to the present writer which would suggest whether the need for foreign finance was a major factor or not. His subjective feeling is that a more cogent reason was that at the time export credit insurance and financing facilities were not so well developed in the Federal Republic, requiring a much higher self-financing ratio than for instance in the United Kingdom. Non-recourse financing was already established in Switzerland for Swiss exports, many of which were not eligible for cover by the official export credit organisation, the Exportrisiko-gesellschaft, because of their foreign content (especially components and parts bought from neighbouring countries). As Häusermann reports, Swiss banks actively sold their à forfait services to German banks. Since German banks are competitive, businesses not being tied to a single bank as is usual in the United Kingdom, some promoted this service in order to secure new business, so encouraging the growth of this form of finance.

Although British export houses have traditionally provided a form of non-recourse financing (probably now very insignificant) there has been no development of Forfaitierung-like arrangements in Western countries, and it has perhaps been tempting to see a link between non-recourse financing and the almost legendary success of German exporters. However, the volume of business transacted does not suggest that it has been essential for German exports, and the researcher suggests that its importance has been greatly exaggerated in British export circles.

2. Export Credit Insurance - Hermes-Kreditversicherungs-AG.

2.1 Origins and development.

This company, with two major insurance companies as its principal shareholders, has been active in credit insurance since 1917. From 1926 it administered the Government's export credit insurance scheme, until it was replaced by the current scheme in 1949. This work is now performed jointly with the Deutsche Revisions- und Treuhand-AG, though the latter company is not directly involved with industry. Both companies act solely as agents for the Federal Government, to which premium income accrues and which appropriates funds in the Federal Budget to meet anticipated claims and the companies' fees. No figures relating to this business appear in the published accounts, though a separate report covering all guarantees is published by the Federal Government [52]. The power to give guarantees is vested in the Inter-Ministerial Committee for Export Guarantees, assisted by representatives of manufacturers, export merchants and banks. Contracts over DM1m require endorsement by the Ministries for Economic Affairs and Finance.

Measured by premium income, export insurance business has been over 2.5 times the company's commercial insurance business in recent years. If one further considers that the company acts on behalf of the Government in respect of certain other forms of insurance, its dependence on official business is such that its status as an independent company has little practical significance as far as policy is concerned: it is simply administering a Government scheme.

The function of Hermes is to provide credit insurance for German exports, both under buyer and supplier credits. The broad purpose is essentially the same as ECGD's, and attention will be drawn to the main differences between the two systems. Most of these differences are, in fact, expected to disappear over the course of the next few years. When this research started, the main features of the Hermes system had remained unchanged for a number of years. The Federal Government had been awaiting the emergence of a harmonised EEC scheme, towards which considerable progress had been made, but the enlargement of the Community has caused indefinite postponement of the harmonisation and the German system is now being overhauled.

(In addition to Hermes, two independent companies - Gerling Konzern Speziale Kreditversicherungs AG and the Allgemeine Kreditversicherung AG - offer export credit insurance against commercial risks only. Their activities in this field are very small in relation to the totality of German exports.)

2.2 Policies offered.

Unlike other countries' export credit insurance schemes, Hermes policies offer the German exporter much more flexibility in choosing which short-term contracts to cover. The Einzelgarantie, corresponding with ECGD's specific guarantee, is available when credit of less than twelve months is involved. A variation of this is the revolvierende Garantie, covering regular business with a given foreign buyer, for which there is no corresponding ECGD policy. The Pauschalgarantie roughly corresponds with ECGD's comprehensive guarantee, though the German scheme appears to leave greater freedom to omit certain

markets at the exporter's option than does the ECGD guarantee. While it is officially reported that more exporters are becoming interested in the Pauschalgarantie, which gives more favourable premium rates and makes for simplified administration, the contracts covered in this way amounted to only DM3.0m, DM3.0m and DM2.9m, or 21.5%, 19.7% and 14.6% of total insured exports, in 1973, 1974 and 1975 respectively. This appears to be in conflict with the official claim, but is probably irrelevant as far as the future is concerned, since the Federal Government has declared its intention of moving over exclusively to the comprehensive form of guarantee for all short-term (i.e. up to twelve months) and certain medium-term business.

As with ECGD, medium-term contracts are covered by the Einzelgarantie, or specific guarantee. This will also cover the long-term part of a contract.

Traditionally the percentage cover of any loss is smaller with Hermes than with ECGD. Post-shipment commercial risks are covered as to 80%, political risks 85% when the causes are exchange losses arising from exchange rate fluctuations after a delay in payment, transfer and moratorium risks, and 90% for other political risks. From 1976 these have been increased to 85% for commercial risks and 90% for all political risks. In the case of tied financial loans (buyer credit), it may be increased to 95% if the bank makes the necessary application and agrees not to "roll off" the 5% balance on to the exporter or insure it elsewhere. In the United Kingdom, the percentages are 90% for buyer risks (i.e. commercial risks) and 90% or 95% for political risks, although in the case of buyer credits

ECGD gives the bank a 100% guarantee, retaining the right of recourse to the exporter in respect of the uncovered balance.

With regard to risks covered by Hermes policies, the main difference from ECGD practice is that insolvency is essentially the only commercial risk covered - protracted default or wilful refusal to take up goods are not included. No cost escalation cover, performance bonds or consortium insurance cover is available from Hermes. An exchange risks policy was introduced in 1972, but has been little used. Hermes policies may be taken out to cover pre-shipment risks only; this facility is not available from ECGD, though it is considering its introduction [1].

Premiums charged on contracts with private buyers are at the rate of 1.5% (0.75% for cash against documents terms) plus 0.1% for each month beyond the first six, for post-shipment risks. An additional 0.75% is charged for pre-shipment risks. These are calculated on the guaranteed amount, so that the percentage at the exporter's risk (usually 20%) and any pre-payments should be deducted from the contract value before applying these rates. Direct comparison with ECGD is not possible, as the latter quotes only average rates based on full contract value, but clearly the German rates are appreciably higher both for short-term (average United Kingdom rate was 0.25% in 1974-75) and medium-term (the United Kingdom claiming 1.25% - 3.4% flat on five year credits, according to the strength of the market). If Hermes judges contracts to be subject to more than average risks, it reduces the percentage of loss covered, rather than increases its premium.

3. Commentary on German export finance.

No evidence has been found of excessive help from the Federal Government in financing exports at the present time, and it is doubtful whether it has ever been given. While a limited amount of slightly cheaper finance is available for some medium and long term credits, this is by no means as great as the virtually open-ended commitment of the United Kingdom Government to provide finance for all creditworthy business of this kind.

German banks do not receive the 100% guarantee provided by ECGD schemes, and the tradition of involvement, noted by the Faringdon Committee over fifty years ago, still thrives in the German banks.

In the area of export credit insurance, it is an inescapable conclusion of a study of Hermes and ECGD that the cover available to the German exporter is inferior in a number of respects to that available to the United Kingdom exporter. Risks covered are fewer and the premiums higher.

In spite of frequently heard comments in British export circles about the help German exporters get from Hermes, the figures in Table 4 do not support the view that it gives more help than ECGD. It is particularly noticeable on considering published figures in more detail that German exports to developed countries are covered to a much smaller extent than the United Kingdom's exports to similar markets - 6.4%, 8.6% and 10.6% in 1973, 1974 and 1975 respectively, compared with over 40% in the United Kingdom (see p.84). Whether this

PERCENTAGE OF TOTAL EXPORTS COVERED BY OFFICIAL EXPORT CREDITS INSURANCE POLICIES IN THE UNITED KINGDOM AND GERMANY

	HERMES	ECGD
1963	7.7	25.1
1964	8.8	27.0
1965	9.4	26.8
1966	10.2	29.7
1967 - 70	NOT AVAILABLE	
1971	7.4	36.3
1972	5.1	35.0
1973	6.1	33.0
1974	8.5	33.8
1975	11.9	35.6

Sources: Bank for International Settlements
Hermes
ECGD

TABLE 4

difference is due to the relatively high premiums in the Federal Republic, the "all or nothing" principle of ECGD, the fact that commercial credit insurance is used in Germany without covering against political risks, is not known; it may well be a combination of all three.

Although Hermes is considered good by German exporters, one comes across complaints about delays in giving decisions. They were recorded in the 1960s, when delays of two or three months were reported [48], and a current German view is that there has been little change since then [1]. This complaint is not confined to Germany, of course - similar comments are heard, sometimes with more justification, in other countries.

As in the other countries studied, the official credit insurance policies are required for much medium-term and long-term export credit finance, thus making the Government the effective decision-maker as to which projects qualify for finance.

CHAPTER 9

NETHERLANDS

1. Export financing institutions and practices

1.1 Introduction.

The smallness of the country has necessitated the development of widespread trading links, and the Netherlands has well-developed facilities to support them.

1.2 The banking environment.

Little comment is called for in considering the banking system in the Netherlands. The banks are more prominent in influencing companies than in the United Kingdom, but much less so than in the Federal Republic.

1.3 Financing institutions.

The normal source of finance is the commercial banking system, and there is no difference between the financing of domestic and export business. Exporters will normally obtain export finance from their commercial banks (or their wholly-owned specialist subsidiaries) or from one specialist bank, the NV Export-Financering-Maatschappij. Registered as a private company in 1951, EFM's major shareholder is the Nationale Investeringsbank, the successor to the reconstruction corporation set up after the last war, holding just over half the shares. The Netherlands Government thus has the ultimate controlling interest. The remaining shareholders are the big commercial banks.

The function of this institution is to finance exports of capital goods manufactured in the Netherlands and to provide facilities for engineering and other contracting business carried out abroad by Netherlands companies. Its activities are not concentrated on developing countries, as is its counterpart's in the Federal Republic - indeed the United Kingdom is usually well at the head of the importing countries to be financed by the bank, with 32% of the total outstanding in 1973, 29% in 1974 and 23% in 1975. The operations of the institution are financed by medium-term loans from the private sector, and by the issue of debentures. Calculations from annual balance sheets show that the ratio of capital (20% paid) plus free reserves to external long-term borrowings has declined from 12% in 1971 to 8% in 1975. The proportion of Government provided funds in the operation is therefore small, though the uncalled part of the share capital held by the Government clearly offers a form of security for depositors and debenture holders.

As a rule, medium-term post-delivery loans are made in Dutch guilders. They may take the form of discounting bills or promissory notes in the case of supplier credit, or of loans to foreign buyers for the purpose of buying Dutch capital goods. The latter are normally for periods between five and eight years, with quarterly or half-yearly redemptions.

Whether finance is obtained from EFM or the exporters' own banks, interest rates charged to exporters are based on commercial rates in most cases. The exceptions are those exports financed under the "export-financering-arrangement"

(efa), by which the Nederlandsche Bank (the Central Bank) rediscounts export bills or accepts them as collateral for loans (depending on the length of time remaining to maturity) provided they fulfill certain conditions. The main requirements are that the bills form part of a series maturing in at least five years, though individual bills in the series maturing in over five years are not eligible for rediscount until they have no more than five years to run. Thus, the banks are required to finance the longer portion of the loan. The transactions must be covered by export credit insurance policies and be registered with the Central Bank at the negotiation stage. Under this scheme, banks must charge a reduced rate of interest. This rate is equal to the average effective yield of three government bonds with an average of five years to redemption, minus 0.75% p.a., rounded to 0.125%. This applies to the full duration of the transaction and is fixed in the month in which application for the facility is made.

The aim is to provide lower interest rates for exports of capital goods. It does not meet with universal approval, EFM commenting that "the application of this arrangement boils down to an export subsidy provided by the banks, in that export bills and promissory notes placed under this arrangement are taken over by them at rates lower than usual for this kind of transaction" [53]. The EFM does not press this point too hard; rather it queries whether the system is desirable in general terms. There is justification for EFM's objection only if the banks have more profitable outlets available for their funds. This may well have applied in the "squeeze" of 1974 when efa rediscounted paper was yielding 9% against a market

return of 11.5% and the bank may have been sounding a warning that it would have to reconsider its position if these conditions continued.

The extent of the reduction in interest rates when finance is obtained through the efa, as stated, depends on the difference between the rates on Government stock and on commercial bills. In June 1975 the rates were:

Normal export finance	9.625%	computed half-yearly
or	9.375%	on the insured portion if thre is a direct guarantee to the bank
Export-financerings-arrangement	7%.	

At first sight, this appears to be a substantial difference, but further consideration modifies this impression. If the rate for export finance is taken to be 9.375% (since direct guarantees are a condition of access to the scheme), the advantage of using the efa is 2.375%p.a. on the insured part of the credit, say 85%. Assuming that 20% will have been paid before shipment, this means that the advantage is reduced to 2.375 x 0.85 x 0.80 = 1.615%p.a. calculated on the contract value. This is reduced further, since the efa applies only to those bills maturing in five years or less; thus for seven years credit, the effective reduction is 1.154% p.a. calculated on the contract value. In round figures, this is equivalent to a price reduction of about 4% on the total contract value.

The efa is not open-ended. Ceilings are applied, and while these are raised from time to time, there have been occasions

when available funds have been fully committed and exporters have had to use normal financing. The ceiling for this efa was raised to hfl 1500m in 1975, with hfl 100m being allotted to a similar scheme for maturities of 3 - 5 years.

A special, but similar, efa exists for general export loans to Eastern Europe and the more advanced developing countries, and is available to Dutch banking consortia. The 1975 ceiling was hfl 200m overall, with a hfl 50m limit for any one country.

2. Export Credit Insurance - Nederlandsche Credietverzekering Maatschappij NV.

2.1 Origins and development.

The Nederlandsche Credietverzekering Maatschappij (NCM) is a public limited company formed in 1925 to provide insurance against credit risks. At the time there was no institution in the Netherlands offering such insurance, and although it had brief competition from two other organisations in the 1920s it has enjoyed a monopoly for virtually all of its existence. It is a historical curiosity that the initiative for setting up the NCM came from the Hermes Kreditversicherungsgesellschaft in Hamburg, one of the two companies with which Netherlands businesses usually placed credit insurance.

The principal shareholders are now Netherlands banking and insurance companies. The NCM offers insurance against all types of credit risk - domestic, import and export. As with the corresponding organisations in France and Germany, the State reinsures certain risks in connection with export transactions (also with import transactions, but the amount is of the order of 1% of export business). However, NCM's main business is for its own account. Domestic business has exceeded foreign since 1970 if measured by the value insured, or since 1973 if measured by premium income. Even on the foreign side, a substantial proportion is for the company's own account - between 39% and 53% from 1970 to 1974, though a sharp rise in State reinsurance brought the percentage down to 33% in 1975. Notwithstanding the rise in 1975, there was little growth trend in State reinsurance during the decade

1965-1975, though there was considerable growth in own account foreign business.

In common with France and Germany, decisions in respect of state reinsurance are not made by the company, which concerns itself solely with formalities. The Ministry of Finance is responsible for decisions where credit terms exceed five years and the amount is more than hfl 5m, otherwise decisions are delegated to the Dagelijkse Commissie voor Export- en Import-garanties, made up of representatives of the Central Bank. The risks reinsured by the state are, briefly:

Political, including transfer, risks,

All risks of non-payment by "official" buyers,

Risk of protracted non-payment by private buyers in developing countries, in addition to the insolvency of these buyers, when the credit period exceeds two years from the date of delivery,

Similar risks in developed countries when the credit period exceeds five years.

While the last two items may seem limited, it is understood that the Netherlands Government is willing in principle to reinsure commercial risks, but the NCM prefers to cover short-term commercial risks on its own account.

The exchange risks mentioned later are also reinsured by the State.

2.2 Policies offered.

The two main types of policy offered are similar to those found in the other countries studied.

Whole turnover policies (omzetpolissen) include all short-term business in respect of a given country, several countries or all countries, at the option of the insured. In the years 1970-74, 75% - 85% of insured shipments were covered by this type of policy. It corresponds with ECGD's comprehensive guarantee in many ways, but as the insured has the option of selecting which countries to cover and whether to cover against commercial risks, political risks, or both, no direct comparison is possible. One form of whole turnover policy, the European policy, includes buyers in the domestic market and eight foreign countries (more if desired) on a single policy, so that even home and export trade are not distinguished.

Specific policies (speciale polissen) may cover commercial and/or political risks on individual contracts. Some cover raw materials, but most relate to capital goods.

Policies may cover buyer and seller credits, and may be assigned to financial institutions. NCM also offers direct guarantees to the banks up to the insured percentage of the contract in the case of seller credit, or financial guarantees in respect of buyer credits. These guarantees allow some relief in respect of the standards which are required of the commercial banks' balance sheets. The overall arrangement with regard to these guarantees is very much like ECGD's.

The risks covered by NCM have traditionally been very similar to those covered by ECGD in respect of standard shipments. A theoretical difference between NCM and ECGD on the one hand and Hermes and COFACE on the other has been that

the former have provided for unforeseen circumstances by, in effect, covering all risks not specifically excluded, whereas the latter have covered only specified risks. The number of claims which this can have affected in practice must have been infinitesimal, and the distinction is in any case disappearing as the United Kingdom and the Netherlands fall into line with the other EEC countries.

Cost escalation cover and consortium insurance cover are not provided by NCM.

Insurance against certain exchange rate fluctuations, which is not available in the United Kingdom, is offered. When payment is to be made in a foreign currency and credit extends over more than two years, the exporter may insure against the exchange rate varying. As in the French scheme, the exporter is compensated if the rate moves against him, but is required to pay any profits which arise from a favourable movement, the first 3% of any change being disregarded. When this part of the research was carried out, only one policy had been approved in the eight months the current scheme had been in operation. An earlier scheme had been withdrawn in 1971 through lack of support, and it has been suggested that, as in the Federal Republic, exporters have succeeded in concluding contracts in their own currency or have found adequate facilities in forward exchange markets.

Premium rates for commercial risks are set by NCM, those for political risks by the Government. Because of the various types of cover offered, premium rates differ appreciably,

according to the turnover, importing country, length of credit and the risks covered, but for medium turnover and an average spread of buyers on a whole turnover policy the indicated range is 0.4% - 0.6% for industrialised countries and 0.75% - 0.9% for developing countries, for sixty days credit and 75% cover, with the risks covered corresponding to those covered by ECGD. For medium term credit (say, 20% before delivery, the balance over five years in half-yearly instalments) a Netherlands bank suggests that the premium covering pre-shipment and post-shipment risks for the most creditworthy markets might work out at 2.1% on the contract value, plus some small additional charges. Since specific policies are granted on an individual basis, direct comparison is again not possible, but these figures are consistent with the statement in its house journal that its rates are higher than ECGD's, but roughly in line with those of other exporting countries [54].

The <u>percentage</u> of any loss <u>covered</u> may be between 75% and 90%, depending on the nature of the risk and the profit margin (a high percentage cover and a high profit margin might reduce the exporter's degree of prudence!). In the case of financial guarantees for buyer credits, cover may reach 95%. Government reports give some help in estimating the normal percentage cover. Total values of reinsured goods and the amount for which the state is at risk are given. The necessary arithmetic shows that for the fifteen years ending in 1975, the average percentage cover in each year fell between 84% and 88%. Since the import component in the figures is negligible, and in practice cover proceeds in 5% steps, it is reasonable to infer that most contracts with medium-term credit have 85% cover,

with some at 90% or 95%, offset by a few at 80% or lower [55]. This percentage cover is less than ECGD's, which is normally 90% or 95%.

Payment of claims is less favourable to the exporter than with ECGD, though individual policies have different provisions.

3. Commentary on Netherlands Export Finance.

The striking feature of Netherlands export finance facilities compared with those of the United Kingdom is the small extent to which they rely on Government assistance. Table 5 compares the percentages of total exports covered by insurance policies in the Netherlands and the United Kingdom. The usual reservations must be made about strict comparability, but the overall position is very clear. As shown by answers provided in response to questions raised at a seminar organised by NCM in 1973, the situation with regard to exports of capital goods provides a striking contrast with United Kingdom practice. After explaining difficulties of definition arising from the form of Netherlands statistics, it was stated that in the decade 1963-1972 exports of capital goods from the Netherlands varied within quite narrow limits, at 21.0% to 23.9% of total exports. Of these capital goods, NCM issued policies in respect of 8.5%, 6.4%, 8.1%, 6.3%, 5.5% and 8.2% in each of the years 1967 to 1972 (figures for the other years are not available) [54] ECGD's Trading Results in recent years show that under "machinery" and "transport equipment" nearly half of United Kingdom exports were covered by credit insurance. If one allows for the fact that spares and small items of equipment will be included in the total exports, the percentage of capital goods insured will probably be higher still.

Is there any explanation for the lower reliance on official facilities than in the United Kingdom, especially the lower percentage of exports insured? The present researcher suggests there are a number of contributory factors.

PERCENTAGE OF TOTAL EXPORTS COVERED
BY CREDIT INSURANCE POLICIES IN
THE UNITED KINDGOM AND THE NETHERLANDS

	NCM	REINSURED BY STATE	ECGD
1965	6.8	4.6	26.8
1966	7.6	4.7	29.7
1967	7.3	7.0	33.1
1968	7.7	5.1	34.6
1969	7.0	4.3	32.8
1970	5.9	3.7	36.0
1971	6.1	3.2	36.3
1972	7.0	4.0	35.0
1973	7.0	2.9	33.0

Sources: NCM
Rijkscommissie voor Export-, Import- en Investeringsgaranties
ECGD

TABLE 5

The country is small and companies of even modest size are used to trading abroad - they cannot manage to keep going without trading at least with neighbouring countries. (The relative importance of international trade to the Netherlands is illustrated by the fact that the ratio exports:GNP is very roughly twice as high in the Netherlands as in the United Kingdom and three times as high as in France.) They regard exports as normal, not an activity requiring special facilities. Moreover, three-quarters of Netherlands exports go to EEC countries where special export insurance is considered unnecessary.

Companies which must be responsible for a substantial part of Netherlands exports are very large, and their export financing requirements are insignificant in the context of their multi-national operations. They are probably also sufficiently powerful to impose their own, very safe, terms of payment. (The 1974 edition of "The Major Companies in Western Europe" compiled by the Commerzbank,Hamburg, includes three Netherlands companies in the first four by size of turnover. Although two of these are Anglo-Netherlands companies, the Netherlands part of one of them would still head the list if the two components were split. If AKZO and Hoechst are considered as a German-Netherlands operation, one may regard four of the five biggest companies in Western Europe as firmly established in the Netherlands.) These companies are mainly concerned with producer and consumer goods, for which only short-term credit is customary, and which are therefore less likely to be insured.

For the longer term business, it was suggested at the NCM seminar that a large proportion of the capital goods

exported were single installations or machines delivered to big companies able to undertake their own financing or were considered creditworthy without insurance. It was also pointed out that in both the United Kingdom and France a credit insurance policy is a pre-requisite for access to officially subsidised finance, while this is not necessarily the case in the Netherlands.

It has also been suggested that "quite a large, but unquantifiable, part" of exports are not eligible for insurance cover as they are either destined for subsidiaries abroad or are paid for by letter of credit [56].

In spite of these features peculiar to the Netherlands, businessmen periodically appeal to the Government to bring up the standard of the facilities to those offered by other countries to their exporters [57]. This suggests that the industry considers itself poorly treated, by comparison with its competitors. The limited personal contacts which have been possible indicate that it is the United Kingdom and France which are considered to give more generous assistance to their exporters, while facilities in the Federal Republic are regarded as about the same as in the Netherlands. The present researcher's view is consistent with this.

With regard to the provision of finance, the self-financing ratio of Netherlands businesses is higher than in France or Germany, and the need for external sources less than in those countries. This high self-financing ratio has been declining since the 1960s [58] and it will be interesting to see

whether this leads to an increasing reliance on external export finance in future.

Until now, the contribution of the authorities has been modest, amounting to the provision under the efa of hfl 1.8bn in all. If one assumes that the efa has been used for average credit terms of 2.5 years, hfl 720m of this "cheap" money has been available every year. This amounts to no more than 0.8% of Netherlands exports (1976). However, viewed in the context of exports to developing countries, it must have played a significantly greater part. Less than 20% of Netherlands exports go outside Europe, and efa assistance would be concentrated on that portion of these exports representing medium-term credit transactions with developing countries. It has not been possible to reach a reliable estimate of the size of this portion, but if one were simply to hazard a guess that it comprises only 2.5% of Netherlands exports, then 32% of the finance would have been provided at the cheap rate. This is modest when compared with the situation in the United Kingdom, where virtually all finance for these transactions is provided at preferential rates.

PART 4

SOME GENERAL CONSIDERATIONS

CHAPTER 10

GENERAL CONSIDERATIONS

It has been seen that in all the countries studied (as well as in most other exporting countries) some assistance is given towards the financing of exports to developing countries on medium and long term credit. The purpose may generally be considered to be the encouragement of these exports, though the underlying reasons are very diverse. A substantial number of these underlying reasons have been encountered, but here it is proposed simply to accept that industrialised countries do wish to promote exports and that assistance with their financing is one of the methods used. The following chapters are devoted to a consideration of some aspects of the general issues involved.

CHAPTER 11

"CREDIT RACES"

1. Introduction.

A "credit race" or "credit war" which developed in the 1950s, and concern that it might get out of hand, have been mentioned in Chapter 6. In fact, apprehension goes back much further than the 1950s, as will be seen.

The granting of credit, and its cost, are generally accepted as marketing tools. Critics of special assistance from Governments are concerned that so much credit may be granted that debtors will not be able to repay the loans, and that recipients of cheap credit will have an unfair competitive advantage.

A widely held view is exemplified by an anonymous, but from internal evidence United States, writer who refers to "official policies to increase exports", "concessionary lines of credit...having an important distorting effect on international competition" and "powerful government backing in the form of cheap export finance...covering an increasing share of the market in big international projects." He claims that "more and more projects are won not so much because the exporter offers the lowest price, the most advanced technology or the best back up service, but because one country offers more favourable export credit subsidies than another...The availability of cheap long-term finance is a critical factor in determining which company wins the contract" [59].

Netherlands industrialists have complained to their government about better credit facilities available in a number of countries [60].

A German newsletter, available to subscribers only, and reputed to be in close touch with authoritative circles in Germany, has railed against subsidised interest rates in a number of other countries. Its facts are accurate, but its tone rather intemperate, exemplifying the heat which this topic tends to generate [61].

In France, David reports that there are many complaints about inferior facilities in France, though he insists that most are unjustified [62].

In the United Kingdom, various references to other countries' facilities are to be found in the report of the House of Commons debate of 10.2.75 [63].

2. Restrictions on the granting of export credit facilities by Governments.

It is clear from these, and other, examples that apprehension has been, and remains, widespread. Governments have been concerned for years to minimise risks of a credit war (although this has not prevented some from indulging in dubious practices) and a number of organisations and agreements have been developed over the years.

The first serious formal attempt to control the proliferation of easy credit terms goes back to pre-World War II days,

when Government-backed facilities were primitive compared with today's. The "Berne Union" (International Union of Credit and Investment Insurers), the membership of which comprises major international credit insurance organisations, was formed in an attempt to keep insurance cover within commercially sound limits. It has attracted unfavourable comments on account of its ineffectiveness in imposing limits on its members. Its success was certainly very limited, the generally accepted explanation being that the members, with the exception of ECGD, acted only as agents of the Governments in their respective countries and were therefore unable to enter into any binding agreements.

At the present time, the rôle of the Union is generally recognised to have changed. Its main purpose is now the exchange of information on credit terms and technical matters relating to credit insurance; to some extent it provides a forum in which relevant issues may be discussed. In these activities it is valued by all member countries; its services are much used, ECGD claiming to make some 2000 enquiries annually on credit terms being offered by other countries. It is obligatory for members to notify to the Union all terms offering more than five years credit and to provide information on other credits at the request of a member. United Kingdom sources state that the scheme works well on the whole. Although there have been a few occasions when there have been grounds for suspicion that some members were concealing facts about current negotiations, there have been other occasions when the first intimation of contracts being under negotiation came via the Union [1].

The position nowadays is that the real decisions are taken in certain international organisations and at Government level.

Article xvi §4 of the <u>General Agreement on Tariffs and Trade</u> prohibits export subsidies except for basic raw materials. Its effectiveness may be judged by David's comment that "subsidy" is sufficiently imprecise to allow French representatives, particularly well versed in the art of juggling with concepts, to extricate themselves without difficulty in international conferences. "In short, as long as export aid is not too obvious, it is very rare for a country to be attacked in GATT. Moreover, it is very difficult to envisage any sanctions the organisation could apply..."

With regard to the effectiveness of the <u>Organisation for Economic Co-operation and Development</u>, we may turn again to David: "In the British club atmosphere which prevails in this organisation, it would be considered vulgar to do more than ask a country simply to give information on its export aid procedures " [60]. Many would agree with this (and its implications), but it is refreshing (and rare) to see such candour in print. He goes on to report a formal exchange of information procedure which was started as a first step in the fight against a credit auction in international trade (cf. the Berne Union procedure).

More effective has been the <u>European Economic Community</u>. Articles 111 and 113 of the Rome Treaty have been interpreted to provide for harmonisation and co-ordination of commercial

policies, and work was well under way to securing a unified EEC export credit policy. The accession of the United Kingdom, Eire and Denmark has postponed the introduction of a common credit insurance policy, which is not now expected to be introduced in the immediate future. Nevertheless, the EEC has been effective for instance in causing the French to abandon, by 1971, favourable re-discount rates for medium term export credits in intra-Community transactions.

Pending complete harmonisation, and to accommodate major trading nations which are not members of EEC, present practice is governed by a "gentleman's agreement" between the world's main exporting countries: the United States, United Kingdom, Federal Republic of Germany, Italy, Japan and Canada.* The main points of the agreement, which came into force on 1.7.76 are:

Minimum cash down payment of 15%

Minimum rates of interest to be

for "rich" countries (GNP over $3000 per head)

2 - 5 years	7.75%
over 5 years	8.0 %

for "intermediate" countries (GNP $1000 - $3000 per head)

2 - 5 years	7.25%
over 5 years	7.75%

for "poor" countries (GNP less than $1000 per head)

2 - 5 years	7.25%
over 5 years	7.5 %

Maximum length of credit

for "rich" countries	5 years
for "intermediate" countries	8.5 years
for "poor" countries	10 years.

For comparison, typical combined rates, including bank charges, but not insurance premium, immediately before these guidelines came into force were:

	Medium term	Long term
United Kingdom	7.5 - 8.0%	8.0 - 9.0%
Germany (Fed. Rep.)	6.75- 7.5%	7.5 - 8.0%
France	6.3 - 7.5%	7.5%
Netherlands	7.25- 8.0%	7.5%

(Source: Banker Research Unit)

These figures are not strictly comparable as the definitions of medium term differ for the countries concerned, being in this context 2 - 5, 1 - 4, 1.5 - 6 and 1 - 5 years respectively. At the time, domestic interest rates were particularly high in the United Kingdom. It should also be borne in mind that credits of this nature are normally decided on a case by case basis, so some degree of uncertainty is inevitable since not all the countries are supplying the same types of machine to the same markets.

This agreement appears to be generally honoured. While it is a step towards uniformity, the differing rates of inflation in the different countries mean that in practice "real" rates are much more advantageous in some currencies than others.

* France later agreed to observe the guidelines from the same date.

CHAPTER 12

GENERAL FINANCING REQUIREMENTS FOR DIFFERENT TYPES OF MARKET

1. Introduction.

While all markets have their individual requirements, a useful categorisation is (a) industrialised countries, (b) centrally-planned socialist economies, (c) other developing countries. The requirements within each of these categories are broadly similar, and are now considered separately.

2. Industrialised countries.

There seems to be no reason for using other than normal commercial criteria in financing exports to these countries. Financial facilities are available locally for buyers (always trade and industrial buyers with established banking connections) and the creditworthiness criteria will normally be similar to those in exporting countries. The provision of credit should therefore be considered a matter of providing facilities more conveniently for a buyer, without his having to "shop around". Commercial banks in many developed countries are often small compared with those in the United Kingdom and may easily reach their limits on individual borrowers. The offer of credit may relieve them of the trouble of negotiating with several banks, but give them no other incentive. The current ECGD-backed lines of credit where interest is charged by the local bank at its normal rate of interest are examples.

3. <u>Centrally-planned socialist economies.</u>

The term "socialist" is used as a convenient term for the USSR and China, and those countries falling under their influence. For practical purposes in this context it means the Eastern European countries; they are by far the most important, though China offers obvious potential for the development of its present 10% share of the United Kingdom's trade with Socialist countries.

Why should the socialist countries be considered as a separate category? In many respects they are like other developing countries, needing imports of capital equipment for developing their economies. The differences lie, firstly, in the large quantities and the high degree of sophistication of the equipment likely to be needed, since they have vast resources to develop and already have sound technological foundations, and, secondly, in their political and economic philosophy, requiring a different approach to the markets. It is this second feature which will merit particular consideration.

Since the USSR dominates the Eastern European countries, its attitude is of paramount importance. Fundamental to an understanding of its approach to business is the fact that purely economic considerations, as seen through Western eyes, have not been the most important factors in Russian decisions - probably the most significant example of this is the rejection by the socialist countries, at Russian insistence, of Marshall Aid after World War II. The profound suspicion with which the Russians viewed the West and its institutions is not realised

by most business men. Although attitudes are changing on both sides, Western exporters still need to make an effort to meet Russian ways of thought if they are going to be successful.

On the Russian side there are undoubtedly more officials with a knowledge of Western economies, but they are probably still inadequate in numbers. Remnants of the old belief that the capitalist world was neither necessary nor desirable are still to be found. One British Civil Servant expressed it: "You have to remember that until relatively recently Russia did not reckon it needed foreign trade very much, so that many ministry officials are simply not geared to dealing with Western businessmen..." [65].

Nevertheless, there is now a desire to expand trade. As much as possible they wish to do this on socialist terms, in particular by bilateral and compensation trade. The importance of this can hardly be over-stressed. Although the socialist countries are moving towards some compromise with Western systems, e.g. by the development of the "convertible rouble" or "transferable rouble" for use in trade within the CMEA (Council for Mutual Economic Assistance) countries with the intention of making it fully convertible in ten to fifteen years time, and by the European socialist countries raising $2104.3m in Euro-currency markets in 1975, they still cling to the idea of barter and similar deals [66,67].

There have also been some changes of attitude on the part of United Kingdom exporters. Broadly speaking, in the 1950s the Russians would have liked bilateral deals, but conformed

with Western insistence to pay cash. Any resistance was little more than a token, and the belief among many successful exporters to the USSR was that if they dug in their heels, there would be no difficulty in obtaining sterling or other convertible currency. No doubt this view was justified in the days when the USSR was actively seeking limited supplies of specialised equipment needed to meet the requirements of the current economic plan. This view may still be justified in those cases where suppliers are technically well ahead of their competitors, but these cases must be getting fewer and fewer. Some British exporters have been prepared to consider bilateral deals for a number of years, and others aremoving in the same direction. One company with exports of over £100m per annum sometimes takes part payment (perhaps 5%) in goods which are disposed of through a specialist trading house. It has no doubt that in practically all these cases its position has been strong enough to hold out for 100% cash, but is prepared to make a gesture of goodwill towards its socialist customers in the interests of future trade. Another multi-million pound exporter, the United Kingdom subsidiary of a European multi-national company, also reported doing some business on a barter basis, leaving its merchant bank to arrange for the sale of socialist exports [1]. Massey-Ferguson, the United Kingdom subsidiary of a Canadian company, has been reported on a number of occasions as having concluded barter deals over the past ten years or more. It has not been possible to make any estimate of the extent to which this practice is now followed, but the impression is that it is growing. The cases quoted are intended only as examples and it is known that other companies have been involved in bilateral deals, but on the basis of communications with British, French,

Dutch, German (East and West) business and financial sources, as well as published statements, it seems to be undeniable that other nationalities have been much more active than the British. The USSR Deputy Minister of Foreign Trade, in February 1976, gave France, the Federal German Republic, Italy, Finland, the USA and Japan as leading in the development of new forms of trade co-operation with the USSR. The United Kingdom does not appear in his statement [68].

While it is dangerous to take statements out of context, and allowance must be made for posturing in public statements which may be intended as no more than starting points for further negotiations, the following series of quotations is probably not an unfair indication of the attitudes in the countries concerned.

> "While talking about the large scale economic co-operation based on compensation agreements involving multi-million and often multilateral arrangements, which to an ever-growing degree determine the development of Soviet foreign trade, I do not mean to say that the traditional methods and patterns of trade have lost their importance...
>
> "What I wanted you to realise is that we can hardly expect a major breakthrough in our trade and economic relations unless British companies join the big game where they certainly are able to show a much better performance than we have seen so far."
>
> (V.M.Ivanov, Head of Soviet Trade Delegation, at a seminar organised by the North of England Development Council. 10.3.76.)

"...the rate of growth is far from matching potential possibilities for the expansion of our mutual trade, especially taking into account Britain's traditional rôle of the biggest trade partner for the Soviet Union among the capitalist countries in the 60s....In 1975 Great Britain was only seventh in the list of our trading partners among the capitalist countries."
(V.M.Ivanov, Soviet-British Conference. 10.5.76) [69]

"The Soviet Union has enormous reserves which one must prise loose. That can only be done by either buying more raw materials or semi-fabricated products, or by co-operation arrangements under which internationally competitive goods are produced."
(Ernst.Wolf Mommsen, former Chairman of Krupp Executive Board, Germany.) [70]

"You cannot expect a computer manufacturer to find an outlet for chemicals."
Lord Layton, British Steel Corporation.) [71]

We turn now to <u>prospects for the future</u>. Assessing potential trade and the concomitant financing requirements is even more hazardous with the Soviet Union and the socialist states than with other countries. The Russians are not very communicative, either with official statistics or in everyday business matters; there is probably a great deal of truth in the statement that in Soviet eyes marketing research is the equivalent of commercial espionage, and that Soviet diplomats in Western countries have gone to trouble and expense to acquire information which is freely available in a good public library.

In spite of its normal reticence, the USSR has given many indications of the substantial business it would like to negotiate with capitalist countries. As far as the United Kingdom is concerned, the biggest is concerned with the provision of a pipeline in Siberia. Although the Western company is located in the United States, the share of its British subsidiary in the $8bn project would be £770m at end-1975 prices, and indications are that ECGD would be prepared to guarantee the financing of the necessary credit facilities. The project which is still in the early stages of negotiation, is understood to be conceived on a "buy-back" basis, i.e. it will be paid for over a number of years by the sale of natural gas.

Enticing prospects of increased trade are offered, but how realistic are they? Only personal opinions can be offered, but the present writer's view is that the socialist statements of their requirements should be taken at their face value. American businessmen, though hampered by their own country's laws on trading with socialist countries, are sufficiently optimistic to maintain full-time executives in Moscow for nineteen companies, including three banks [74]. In Germany the opinion has been expressed amongst the largest of the 1500 companies trading regularly with the Soviet Union that exports to that country alone could be up to DM27bn by 1980, from just over DM 8bn in 1974 [75]. This optimism may not be wholly justified, but it seems certain that business worth many hundreds of million pounds worth of business is available to Western nations if they can offer the right goods with the right credit terms, though negotiations will inevitably take several years.

Of the countries studied in this report, the Federal Republic of Germany is perhaps best placed for carrying out the type of trade required. The Germans have a history of trading with the socialist countries and not only have the necessary experience but a very positive and forceful approach which seems to be lacking in many British companies faced with unfamiliar financing techniques. One might also hazard a guess that the German banks could use their influence with companies to a much greater extent than British banks to finalise deals. It is not difficult to visualise a situation where an exporter's house bank knows of a company which could take imports from the trading partner. Considering the power of German banks, the two companies could probably be persuaded to collaborate rather more readily than two independent companies in, say, the United Kingdom being cajoled by a merchant bank. Whether overt pressure is, in fact, applied would require access to the deliberations of company boards, but even a suggestion from a house bank could well be taken more seriously than the most persuasive arguments of an independent merchant bank.

In spite of the attractions of the business at stake, there are serious drawbacks to participating in this kind of trade on such a scale. The magnitude of the credit facilities required make them into a national, or even international, rather than a company problem. The Siberian natural gas project already mentioned was shelved in 1974 because the American parent company was unable to raise finance in the United States. It was revived in 1976 with contributions from British, French and West German banks supported by their credit organisations [76]. For this one project alone, credit of $8bn dollars would be required over ten or twenty years. This

is more than the United Kingdom's gold and currency reserves have been for most of the past few years. While there was never any prospect of the United Kingdom getting the whole of this order, it provides a good illustration of the potential impact of even a single order. To forego receipts for exports which can make such a difference to the country's external finances is a decision which properly belongs to Governments, and the credit insurance decision will be concerned with the macro-aspects more than the probity of the buyer.

Barter deals have their dangers, too, at both company and national levels. Where payment is by exchange of goods, the dangers of poor quality are obvious. One Scottish machinery maker accepted payment by counter-purchase of components from Poland, but found the quality so low they could not be used. Meanwhile the Poles are doubtless copying the machines delivered. Another company has a large stock of unsaleable shoes. Another company accepted payment by importing cycles, which it sold to employees at £10 each, with obvious potential repercussions on British cycle manufacturers [1]. Similar effects on a much larger scale can be expected when payment is to be made by the supply of petroleum products, which will displace existing supplies; in addition, existing oil companies will have to supply marketing facilities and modify refineries for the new feedstock. In the chemical industry, some German companies are expressing fears about the incursion of Eastern European chemicals into their markets when payment for chemical plant is made from the output of the plant.

Attractive though the prospects may seem, it must be clear that socialist insistence on this method of payment

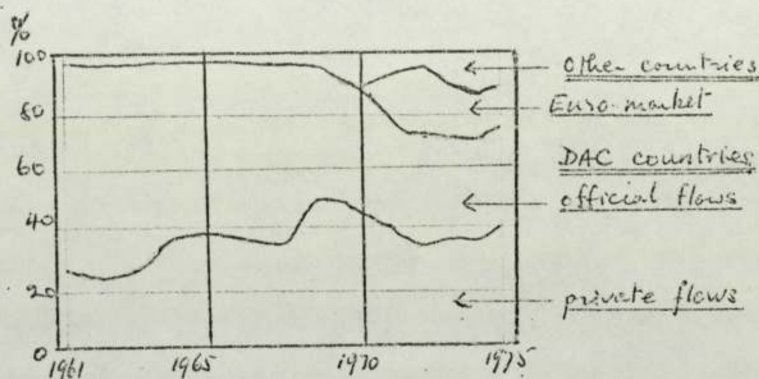
implies the application of considerable Western manufacturing and marketing resources to the development of the socialist economies. Whether this is desirable will depend partly on one's personal views and partly on the prospects facing our own Western economies if and when the prospects of business become firmer.

4. Non-socialist developing countries.

As with the socialist countries, the needs of other developing countries are enormous. Their economies are in different stages of development, ranging from Spain, generally regarded as the most advanced European "developing country" and perhaps now almost a developed country, down to countries of negligible economic achievement. While some are not averse to barter and similar arrangements, they generally fall under the influence of Western institutions and export finance takes on a more conventional aspect.

There is little contention about the main underlying issue. For a number of worthy reasons, and also self-interest, it is thought that developing countries' economies should be helped. To do this, advanced countries' resources have to be made available on a permanent or a temporary basis - in financial terms by grants or loans. Hitherto, aid has been of various kinds, and broadly speaking may be classed as "official" (bilateral grants and aid; multilateral - contributions to and participation in international organisations; credits tied to specific projects; contributions by central banks to IBRD) and "private" (bilateral flows, such as export credits, investments; multilateral loans to, say, local development banks).

Over fifteen years, from 1961 to 1975, the volume of OECD official development assistance remained almost constant. During this period, aid expressed as a percentage of assisting countries GNP dropped from 0.53% to 0.3% in 1973, recovering to 0.36% in 1974 and 1975. At the same time, the percentage taking the form of grants dropped from over 80% in 1961 to a little under 60% in 1971, recovering to 60% in subsequent years. The development of fund flow sources may be seen from the following sketch.



Source: KW, based on OECD/DAC statistics

In the country reports, it has been seen that Euro-currency sources are widely used in financing exports of capital equipment - in the United Kingdom by front-end financing, followed by Government pressure for post-shipment financing to be in foreign currencies, in France by BFCE raising finance in the Euro-bond market, and syndicated loans by banks of all countries. Though it cannot be said that all of the Euro-currency shown in the sketch is for export finance, the bulk of it will be. The essentially short-term nature of Euro-currency deposits makes the whole market vulnerable to withdrawals at short notice. This is a matter of concern to exporters in all of the countries considered, since it is now clear that many importing countries are likely to default on the repayment of their loans, at least on their original terms.

Confirmation of the increasing importance of private flows is to be found in World Bank figures [76], which show that of the total debt outstanding by 86 developing countries, 11% was attributable to financial markets at end-1967 and 24% at end-1974. At the same time total external public debt has increased at an accelerating pace: an annual rate of 13.8% from 1967 to 1971, 19.0% from 1971 to 1974 and 22.6% in 1974. While the growth of debt to official lenders increased by 17.9% in 1974, debt to private lenders grew by 33%. A consequence of this evolution is a change in the debt structure of importing countries. Official loans frequently have a grace period of five to ten years and are usually for periods of 25 years or more, while financial market loans are for five to seven years. Thus there is more pressure on repayments, and average loan commitment maturities, which have fluctuated between 19.1 and 16.9 years between 1967 and 1974 must be expected to shorten [77].

Official loan interest rates, though touching over 4% (DAC average) in 1969 have usually been no more than 3.5%, and in recent years have dropped to 2.5%. Financial market loans are usually made at a higher rate, putting further pressure on debt service. (For some years it has been usual to arrange loans on a roll-over basis at a spread over LIBOR (London Inter-Bank Offer Rate) making the calculation of future commitment impossible.)

A further feature of export credit finance which has been recorded in the country reports finds confirmation in the aggregate figures - the shift from supplier credit to buyer credit. At end-1967 supplier credits made up 72% of outstanding export credit debts, and only 36% in 1974 [77]. The two

categories were almost equal at end-1972, and since these refer to outstanding debts, it is probable that in new credits granted buyer credits took the lead in 1969 or thereabouts. A clear implication for financial institutions is that in the first instance it is they rather than the suppliers who are at risk, so that in the event of default they are more likely than before to find their liquidity endangered. In the longer run, it may not make much difference because of official export credit insurance and possible recourse which they may have to suppliers. No information is available as to the actual vulnerability of the lenders but it will be recalled that the United Kingdom is the only country where official export credit insurance gives the financing bank a 100% guarantee. It will also be recalled that front-end financing, normally 20% of contract values, is required by official insurance organisations, so at least 20% will be at risk, subject to whatever commercial or central bank guarantees may be obtained.

The growth of absolute figures, the increasing share of financial markets in loans to developing countries, shorter loan terms and higher interest rates combine to cause apprehension about the repayment of the loans. The global figures quoted refer to borrowings by all developing countries from all developed countries for all purposes, so can only be indicative of general trends in export finance. Further examination of the figures shows, as one would expect, that private finance has grown more in the wealthier, and therefore safer, of the importing countries, and that official aid to poorer countries has remained fairly constant. Obviously, the situation varies from country to country, but the overall picture of increasing financial pressure and fear of default

is clear. In some countries, default is imminent.

Unofficially it is considered that some United States banks have overlent to South American countries. This does not directly affect the present study, but the interlinking of loans through the Euro-currency markets and the international banking system mean that any substantial defaults will have repercussions on the exporting countries covered by this report.

If one considers importing countries' debt service ratios (capital repayments plus interest payments as a percentage of exports) one may get a rough idea of the countries' ability to repay its debts. Available figures from the World Bank are subject to serious limitations, especially when used for forecasting purposes. Exports of many developing countries are notoriously subject to fluctuation in value due to volatile commodity prices, with obvious effects on the debt service ratio. Loans from private sources are more and more with variable interest rates, from as low as 0.5% to more than 2.0% above LIBOR, and the World Bank has calculated a hypothetical swing of $840m in interest charges on the end-1974 figures of total outstanding debt, 75% being concentrated in Latin America and the more advanced of the Mediterranean countries. It points out that the amount of the swing is small in relation to the exports of developing countries, but could cause problems in some cases.

Examination of World Bank tables shows that six countries had debt service ratios of over 20% in 1973, but the difficulty of arriving at reliable figures for forecasting is illustrated

by the case of Zambia, with a ratio of 28.5% in 1973, but under 6% in each of 1967, 1970 and 1974, with no figures available for the intervening years. Clearly debt service ratios of the order of 20% and more are likely to be crippling, and debt relief will have to be arranged.

An additional problem is the well-known question of the source of funds for the Euro-currency markets. Much is deposited on very short term and apprehension is caused particularly by the share of OPEC, estimated at $34.6bn out of $205.0bn at end-1975.[79] There now seems less fear than a few years ago that these funds would be withdrawn quickly, but this risk still cannot be ruled out as these countries are reputed to deposit their funds at very short term. Familiar political and military considerations are relevant in this context.

Thus, the financing of capital goods exports is seen to be at risk from two sides - the increased burden falling on financial markets, both in terms of amounts advanced and the risks, and the ever-present danger of funds being withdrawn. Whether exports to these developing countries should be encouraged is a matter of political aims, but if the decision is that they should be encouraged, the implications should be realised: it involves a substantial shifting of resources from exporting to importing countries. Although the magnitude of the problem can only be guessed, it seems safe to assume that developing countries need more imports than can be physically provided in the foreseeable future, and the limit will be decided by the willingness of advanced countries to make resources available. Whether resources are transferred by multilateral or bilateral aid derived from general taxation,

or by private institutions with Government backing (in the form of rediscount facilities of one kind or another, financed by taxation - or inflation) is largely a matter of political expediency. Experience suggests that, in fact, no conscious decision will be taken to transfer the necessary resources, since electorates in the advanced countries are not prepared to reduce their own standards of living to do so. For the reasons already discussed, the Eurocurrency market is unlikely to be both able and willing to support much more of this type of business.

What will undoubtedly happen is that importing countries will default on existing private loans, officially negotiated debt relief arrangements will spread the burden over a longer period, lenders will be reimbursed to the extent of their cover and will have to carry the remaining loss. This will probably prove to be an on-going process for many years. It is intellectually unsatisfactory, but practically it may be the best way - it obtains money from private sources without a direct call on the electorate, saves these sources from complete disaster, while incorporating an incentive to prudence. The alternative, if it is wished to encourage this type of export, is to make funds available for direct aid.

CHAPTER 13

THE RELEVANCE OF INTEREST RATES TO BUYING DECISIONS

As stated in Chapter 11, much concern has been expressed by businessmen about the possibility of their foreign competitors having more favourable financial facilities at their disposal than they have themselves. These facilities comprise the availability of additional funds and their provision at subsidised rates of interest. There can be little doubt that if more funds are available for export credits (either for allowing credit for more projects or for allowing longer credit terms) the needs of the developing countries are such that more business will be available. But are lower interest rates really effective in giving a competitive advantage? As such strong feelings are generated by this subject, the present chapter will consider the issue at some length.

It is widely assumed, whether as an application of the law of the downward sloping demand curve or as plain common sense that a reduction in the price of a good will result in increased demand, the only question being the extent of the increase in demand (except, of course, where total demand is finite). Hence, any decrease in interest rates which will reduce the financing costs, and therefore the total price, of a good will result in increased demand. While it has long been recognised that kinks, backward sloping demand curves and other anomalies exist, they seem to be regarded as minor aberrations.

Some years ago (1963-67) a professor of economics repeatedly argued in favour of a devaluation of sterling on the grounds that it would reduce export prices and therefore produce "a dramatic rise in exports". It is not known whether this economist still holds the same views, though in an article dated 24.4.77 on the subject of export competitiveness he suggested that the recent rise in the sterling exchange rate provided "a strong warning against encouraging the exchange rate to float upwards". While he acknowledged that quality, service and delivery are not measured by indices, he clearly accorded price a major part in export performance [80].

Contributions to the newspaper concerned (with copies to the economist) challenging the view that lower prices would produce the dramatic rise in exports were unpublished. Discussions with other professional economists at the time showed that they regarded such a challenge as untenable.

It is not suggested that all economists take the same view. For instance, Otteson, et al. have noted that in the 1930s economists, albeit grudgingly, included product differentiation and selling effort in their model of the firm, though price was still regarded as the key economic variable [81]. Oxenfeldt "...is not convinced that price theory does describe, accurately enough for many purposes, how most - or the most important - markets behave. Factors not taken up by price theory seem to exert a major influence on resource allocation" [82]. In the United Kingdom, Lady Margaret Hall recognised that "we have...to decide whether the people concerned <u>are</u> trying to better themselves in the economists' sense of the phrase," thereby implicitly questioning whether

buyers do, in fact, always decide in favour of the lowest-priced article. "The facts themselves become too complicated ...to be capable of being reduced to a tidy set of rules... For a complete analysis, we should have to know the complete behaviour pattern both of buyers and sellers" [83]. A NEDO report comments: "Despite the analytical attraction of interest as a determinant of investment, empirical work has frequently found that the response of investment to changes in the rate of interest has been small" [84].

In spite of these, and other, reservations, the basic view remains that any price reductions, including those attributable to the provision of cheap finance, will inevitably result in increased sales. This will be considered more closely.

During the present research, the very clear impression was obtained that those not directly concerned with export negotiations were much more impressed with the importance of price differentials as a determinant in real life buying decisions than were exporters themselves. One Civil Servant, clearly unwilling to yield ground, supported his traditional view with the assertion that "interest rates are what everybody talks about". Most of those interviewed readily agreed that "non-price factors" are more important than was once thought, but still accord them less weight than do exporters themselves. The closer respondents were to being involved in actual export transactions, the more likely were they to hold the view that exports are not highly sensitive to small price changes. This applied irrespective of nationality - and the

topic was discussed with manufacturers, bankers and/or officials from all four countries studied.

Can some useful attempt be made to assess the importance of financing costs, with their influence on offered prices, in obtaining export orders? Since it is through lower prices that favourable interest rates are reputed to work, the discussion is essentially one of the rôle of price in buying decisions.

Evidence is too fragmentary to provide conclusive answers, but it suggested that there are sufficient indications to allow limited conclusions to be drawn. As seen by Lady Margaret Hall, the behavioral characteristics of buyers and sellers are complex, but in the last two or three decades marketing studies, drawing on the behavioral sciences, have made some contribution to an understanding of the problems. Even so, the basic difficulty of identifying real buying motives remains.

An appreciation of the basic mechanisms involved in a buying decision will show why it is, in fact, highly improbable that it will be affected by small price differentials. The following brief exposition will concentrate on capital goods, since they form the most contentious sector in discussions of export finance costs. To attempt to cover all eventualities with all types of goods would be too complex, though the general principles still apply.

It is misleading to think of a buying decision as a single action. While authorities have formulated different models and terminology, there will be little disagreement

among marketing experts with the following summary of the stages in a buying decision. (It should be noted that there will often be interplay and chronological overlapping between the different stages.)

1. Problem recognition. A buyer recognises a need or desire. This may be very precise, e.g. a Rolls Royce car, in which case the availability of resources rather than a detailed consideration of the price will be all-important. However, it is much more likely that the "problem" will be seen as a general one, e.g. the need for a luxury car, or a generating set, and the buyer will pass on to the next stage.

2. Search. A potential buyer will seek from his existing knowledge or from outside sources a means of "solving" his problem. This search may possibly reveal only one potential supplier of a solution. (whether because of an inadequate search, or because only one supplier actually exists), in which case price differentials are irrelevant. More likely, there will be more than one possible solution, so the next stage is initiated.

3. Evaluation of possible solutions. If one assumes that cost-effectiveness is the major criterion, a number of practical difficulties arise.

3.1 Most manufacturers of capital equipment have developed their own technical methods and direct comparison of alternatives is impossible.

3.2 Estimates have to be made on such factors as delivery dates, maintenance costs, including frequency of stoppages, availability of spare parts, cost of training personnel (are staff and workers

already familiar with the type of equipment? are language problems likely to be more serious with one supplier than another?), availability and cost of supplier's personnel for commissioning, and so on - the list will depend on the nature of the equipment. They are all rational and identifiable factors, but not easily quantified.

3.4 The cost in the buyer's own currency will depend on the exchange rate when payment is made. This cannot be forecast with accuracy. (While forward exchange markets exist in major currencies, this is not so with currencies of developing countries, with which we are primarily concerned.)

3.5 Adequate technical and financial skills may not be available to make the necessary evaluations.

So far we have considered only those easily identifiable factors which contribute to an evaluation of cost effectiveness, and it will be realised that even here there is much scope for error. If we add behavioral factors, we find the situation becomes even more complex and uncertain.

3.6 Even if adequate technical and financial skills are available, the balance between different factors is likely to be determined by personality or status, since it is highly improbable that all the skills will be present in one individual. A maintenance engineer, a production engineer and a financial controller will all have different criteria which will in practice probably be resolved on non-rational grounds.

3.7 Subjective opinions are required on a number of factors mentioned in 3.1 to 3.4. These will be influenced by the personality, experiences and beliefs of the individuals. These may affect the evaluation very considerably, and subjective factors can dominate objective ones. It is unlikely that anybody approaches evaluation with a completely neutral attitude, and this will affect perception of facts communicated to the individual - psychological mechanisms resist attitude change, at least within certain limits.[85] This may manifest itself in favour of goods of a certain nationality, of a certain make or employing certain technical principles. The influence of this subjective factor will often more than outweigh quite substantial price differentials.

It should be borne in mind that in many under-developed countries, the business élite comprises no more than a handful of people who trade in a wide range of goods, and objective criteria which can be used are minimal. These people occupy their positions because of social status or political record and have little knowledge of modern industry. No-one who has repeatedly taken his turn with fruit merchants, textile manufacturers, leather goods merchants and others to sell machinery to a single individual, then been ostentatiously watched in the urinal to make sure he is not attempting to bribe an employee, will be easily convinced that a buying decision based on the study of photographs, printed specifications and reputation will always be

rational. Moreover, many decisions on large-scale capital expenditure are taken by Government and quasi-Government organisations staffed by officials not dedicated by inclination or training to profit maximisation. Even in advanced economies, little realistic appraisal of investment decisions is made in some companies and Government departments. The chances of this being done in less-developed economies are more remote.

3.8 There are undoubtedly other evaluative criteria, but little information is available. In what must include by far the most comprehensive review in existence of the literature relating to buyer behaviour the authors state that the "literature on other criteria used is quite meager" [86].

Being aware, either consciously or subconsciously, of the scope for error in their evaluations, decision-makers will probably find there is a "short list" of offers of apparently the same order of merit worth taking to the next stage.

4. Purchasing processes. This is essentially concerned with all aspects of buyer-seller negotiations, and in practice is usually closely connected with the evaluation process. Information supplied and subjective impressions conveyed will influence the evaluation - a trusted salesman can have an enormous advantage.

There is one respect in which this stage is important in the specific context of export finance: the form in which the price is described and the method by which agreement is reached. A hypothetical case will provide a simple example. An article is offered and the seller

expects to receive £95 for it. Does he ask £95 on a take-it-or-leave-it basis? Or £100 less 5% discount? Or £100 and then bargain down to £95? Buyers are going to react differently, depending on their personality, culture and skill. The researcher knows of no controlled experiment to shed light on this problem, but is confident that these different approaches would produce different outcomes in terms of sales. One may add a further possibility: what would be buyer reaction to "£90 + 5% surcharge"? It is suggested this approach would be less likely to be successful than any of the other approaches, though on objective criteria it is more advantageous to the buyer.

No doubt some of the misunderstandings about the importance of price have arisen from accounts of bargaining sessions, which can be lengthy and fearsome. As one exporter with over thirty years experience put it: "An Indian feels cheated if he doesn't get his bargaining session. It's better than a night out for him and he feels insulted at a 'take it or leave it' attitude" [1]. Failure to adjust to local customs in this respect can create psychological discomfort leading to a distrust of the seller, which will adversely affect his credibility on matters of fact. Even failure to observe minor points of local custom can have a serious effect. One academic dismissed these with the words "One says 'how quaint' and moves on to more important matters" but in real life gaffes of this kind can be disastrous.

Negotiating skill may be more important than price. Since buyers are usually less well-informed on the merits of machinery than are the sellers, they concentrate on

the areas in which they feel at home. Part of their skill is giving the impression that competitors are offering more favourable prices and terms. Though not always well versed in appraisal techniques, they are often extremely well informed on interest rates and insurance premiums, and this can give a distinct advantage to the buyer over a less skilled seller. (The Commercial Secretary at a United Kingdom Embassy in the Middle East has told the researcher he could find out current (confidential!) ECGD rates more quickly by telephoning his contacts in the bazaar than by cabling London.)

The seller will use counter ploys, the usual one being to "load" the price for the equipment so as to allow scope for bargaining - not only on the price of the equipment, but on financial terms, too. There are strong indications that this is done even where buyer credits are negotiated as separate agreements with financing institutions. In other words, the interest rates quoted are not necessarily genuine.

If the purchasing processes stage is successfully completed, the final stage will be:

5. <u>Post-purchase evaluation</u>. Since this is primarily concerned with subsequent negotiations, it will not be considered further here, except to point out that the subjective factors already mentioned may in part be based on post-purchase evaluations of previous transactions.

In the foregoing survey, it was assumed that cost-effectiveness was the most important evaluative criterion, and even with this limitation there have been so many uncertainties that the chances of minor price differentials being critical seem

very small. Yet it should not even be assumed that cost-effectiveness is always the most important objective of decision makers. As individuals, they have different personalities, differing abilities and are subject to influences from family, social class, business, educational and other reference groups. Their value systems inevitably cover a wide spectrum and in these circumstances it would be a remarkable coincidence if all who contribute to purchasing decisions have cost-effectiveness as their goal. The traditional view would be that those who do not achieve maximum profitability (of which cost-effectiveness is a part) will be forced out of business by more efficient enterprises, though it is now accepted that there are a number of hindrances to this happening quickly. In developing countries, total absence of effective competition in many cases makes the traditional economists's view totally irrelevant. Given the further complication of a range of goals other than cost-effectiveness, the chances of minor price differentials assuming paramount importance are still further diminished.

Evidence to support the view that price differentials are less important than is traditionally believed is largely anecdotal. Much is opinion, and the credibility of sources must be weighed carefully. This is unsatisfactory for those who insist on rigorous quantitative analysis, but it is the best evidence available. "Theory which proceeds without constant verification of its hypotheses is a menace" [83] and one may perhaps ask what rigorous quantitative analysis supports the view that price is always the key determinant.

The following examples support the view that factors other than strictly goal-orientated ones are prominent in buying decisions. Most are drawn from economically advanced countries and it seems reasonable to suppose that less developed countries will be no less likely to incorporate irrational factors in their decision-making.

The relevance of the country of origin in evaluating products is known to most international salesmen. One United Kingdom exporter who obtained a substantial order from West Germany for machinery is convinced that he was successful because the real decision-maker was pro-British and anti-Swiss, though the technical factors clearly favoured the Swiss in this case [1].

More formally, a small number of cross-sultural studies have been carried out, among them one which compares Japanese and United States ratings of products from various countries. These show that different attitudes exist in the two countries; some supplier countries will be favoured in one of the markets, others in the other market [87].

A consultancy firm's survey of machine-tool buying decisions mentions price as a buying factor only once in a list of seven importing countries, and for this one country it was placed fourth in order of importance [88].

The now retired sales manager of a chemical company recalled his astonishment on being told by a potential customer in the Netherlands when he first tried to enter export markets: "We are not interested unless you are prepared to do business

on a long term basis. We don't want to change suppliers for every small price differential - we want continuity of supply and quality." The company's annual export business is now worth well into eight figures sterling and it is now also exporting from its overseas plants. While prices are largely dictated by world markets, the company still finds that minor deviations do not cause loss of business [1].

A British merchant banker said that on several occasions he had arranged extended credit for German exports on financial terms "infinitely inferior" to those he could have arranged for similar British machinery. He was unwilling to be more precise because of confidentiality, but said that German reputation counted for more than a substantial price reduction. Since he was never concerned with projects of less than £5m (1974 prices) and £50-£100m was his usual range, interest charge differentials would have had an appreciable effect [1].

One of the few British exporters with an intimate knowledge of Eastern Germany reported that production engineers (who knew nothing about price) often specified in writing the manufacturers of equipment being ordered from abroad through the State Trading Organisation. Although this was strictly against regulations and the buyers themselves did not like the practice, they did not seek cheaper sources of supply - they did not want to be blamed if production norms were not met [1].

Sources of supply being specified by engineers without knowledge of the price is considered to be common. Recently an informant in the buying department of an internationally known British engineering company reported that requests for

machinery from engineering managers were never subjected to scrutiny or appraisal. He commented that the chief buyer was no more than a chief clerk [1]. He was unaware that the same description had been used by PEP [89].

One very competent exporter (£100m+ p.a.) directs his attention to preliminary work, so that specifications of overseas buyers include as far as possible features which only his company can provide. As sealed tenders are common in this business, lower prices are often rejected on grounds of non-conformity with specification without reference back to the would-be supplier [1].

A striking example in the United Kingdom was made public in a television programme early in 1976, which showed how a major purchasing decision was made by the British Steel Corporation. The present researcher's view of the proceedings was confirmed by at least six others with whom he subsequently discussed the programme. It was an object lesson in how to put on to a committee the responsibility for what was manifestly not only a purely personal decision of the Chairman, Sir Monty Finniston, but one which was taken in the face of all calculations clearly pointing to another course of action. He conceded that his opponent on the committee "had a point", but added that these questions are ultimately a matter of judgment beyond mere financial questions. One must beware of false impressions which can be created by the editing of television programmes, but the original impression was confirmed by a subsequent press report - the Chairman had said afterwards he thought people would be surprised by both the sophistication of the planning analyses and the fact that considerations other

than computer projections could decide a development! [90].

A survey of machinery buying in a British industry showed that in many cases appropriate appraisal techniques were not used and psychological factors played an important part in decisions. "In the main these businessmen prefer to avoid a dependency on the skills of others and group decision-making which would depersonalise their business activities" [91].

An East German diplomat, encouraging British exporters to seek business in his country assured them that "if..... in third or fourth place" price were right, there was business to be done. Announcing in advance that price is not the main consideration is a striking reversal of the usual bargaining procedure! [92].

It is suggested that these, and other, examples offer substantial evidence that small price variations are not necessarily critical. But the question which has been avoided so far is "how small is 'small'?". Some indications may be given, but there is no definitive answer.

A French manufacturer and exporter of precision-engineered components used in industry was confident that a price differential of at least 5% would be needed for him to break into his competitors' markets, or for them to break into his [1].

A German banker thought that up to 5% was unimportant. A French banker expressed a similar view [1].

A British official with direct experience of negotiations

suggested that as long as a rate of interest appeared to be in line with current market rates, buyers were not concerned that another supplier's interest rates were rather more favourable because of easier conditions in his financial markets [1].

More accurate indications may be found in "How British Industry Buys" [93]. Here it is stated that about half of industrial buyers would not change their main suppliers for a price advantage of less than 5%, and about one-fifth would not change for less than 10%. These figures represent expressions of intention which in the event might not be carried out. In fact, it seems likely that lack of time and resources in most companies would effectively cause an inertia which would increase these thresholds. It must also not be overlooked that even if cost-effectiveness is a company objective, it may not be consistent with the private goals of the responsible employee.

A survey of industrial pricing practices suggests that the effective price range within which competition takes place (the percentage difference between lowest and highest competitive prices) is wider than many would have thought. Even assuming that all non-respondents on this particular issue should have been placed in the lower bands, the effective price range was thought to cover more than 10% above the lowest competitive price in 64% of replies, and more than 20% above the lowest competitve price in 19% of replies. There was little variation between different channels of distribution; the figure for capital goods was slightly higher than for components. As the survey notes, there are methodological problems and it is clear that at least some firms have an

imperfect knowledge of competitors' prices. Even so, it is reasonable to make the general inference that there is a substantial range of acceptable prices in markets for industrial goods, perhaps of the general order of 10%-15%, but with cases of more than 50% reported [94].

Gabor and Grange similarly noted a range within which price may be not much of a factor in studies of consumer goods in the United States [95].

In considering the relevance of price to buying decisions, it should be noted that price sensitivity is not synonymous with elasticity as traditionally understood. The elasticity concept implies that if business is lost through an increase in price, it will be regained by restoring the price to its former level. In most cases this will not happen since (a) the bases for the buyer's evaluation of subsequent offers will have changed, as there will now be advantages in continuing business with the new supplier, and (b) there will be a psychological disinclination to return to the original supplier because of the ego-involvement of the buyer in having once rejected him. (One may comment in passing that this view is entirely consistent with catastrophe theory, currently being propounded.)

These factors leading to relative insensitivity to price changes are reinforced by the distribution channels. All channels impose some degree of inertia, but this is even more characteristic of export than of domestic channels. This is often overlooked by commentators, who often tend to look upon business as a number of independent dyadic transactions, even

though "ease of entry" has long been recognised in theory as a pre-requisite for rapid adjustment. In practice, should either exporter or importer be dissatisfied with any aspect of a continuing relationship, it is difficult for him to find an alternative partner quickly. As far as price is concerned, if a well-established exporter insisted on raising his price, it is likely that members of the distribution channel would lower their profit margins until they could find alternative sources of supply, at which point demand for the existing product would drop catastrophically. (In the case of a single large order, as with capital equipment, the agent might be willing to accept a reduced commission rather than risk losing the order.) Thus, even if an exporter's price reaches a level which might endanger his chances, there is always the possibility of assistance from members of the distribution channel.

To summarise a highly complex situation, it is suggested that the traditional concept of a smooth demand curve is misleading. Rather, there is a range of prices acceptable to a market; its limits are not easy to ascertain, but could well be of the order of 2% - 5% for undifferentiated products (for which terms of payment are typically very short term credit) and 20% or more for highly differentiated capital equipment. A central trend line is conceptually elegant and is useful for some purposes, but it is not descriptive of reality at company level for many manufactured goods. Within the acceptance range, demand for a particular supplier's goods will be relatively stable, but once the buyer's acceptance threshold is crossed, demand will fall substantially. In the case of unique orders, e.g. hydro-electric power stations

requiring specific studies, there can, of course, be no existing demand to fall, but there is no reason to suppose that there will not be an acceptable price range for the equipment offered - between a price which the buyer is not prepared to exceed and one below which he will be suspicious of the quality or the specification of the equipment.

With the exceptions mentioned in the next paragraph, no evidence has been found of interest rate differentials between the exporting countries studied approaching the levels needed to affect total contract prices by the amounts suggested in the last paragraph. It cannot be claimed that interest rates are completely irrelevant to buying decisions, since it is quite possible that a price without financing charges is already near the rejection threshold and high interest rates might mean the difference between success and failure. The researcher is of the opinion that such cases are infrequent, but there is no means of testing this.

The exceptions just mentioned are the French crédits mixtes, which have already been discussed in Chapter 6, and the very high interest rates in the United Kingdom during much of the research period. The latter may have put some exporters at a substantial disadvantage in cases where credit has been granted for, say, one or two years. If this has happened, it may well be attributable to failure to finance the transaction in a foreign currency or by means of a foreign currency loan at lower interest rates. It can have affected only a very small percentage of British exports, since credits of over two years have been subsidised. Although this has done no more than

allow United Kingdom exporters to offer nominal interest rates similar to those of competitors, the falling value of the pound (with which the prevailing high domestic interest rates were closely connected) has given these exporters an advantage, since the "real" rate of interest has been much lower than for credit in other currencies. The extent to which this factor has been of practical assistance cannot be known, since buying decisions will have been influenced, if at all, by the buyer's own forecast of the future value of sterling, and not by any objective criteria.

This topic has been pursued at some length because of the persistence of the view that cheap finance, through its impact on price, is an important factor in buying decisions. It is suggested that the evidence, though fragmentary, very strongly supports the view that price differentials of the order produced by interest rate differentials are not a critical factor in importers' decisions. This has considered the matter from the point of view of individual decisions, but some evidence is available on the macro-scale to support the opinion that price is not the most important factor in a country's exports.

There are problems of measurement, in particular it is difficult to make strict comparisons because of product variations, to obtain accurate data on which to base statistics, and to allow for substantial changes in rates of exchange. Nevertheless a comparison of two sets of figures may be helpful.

Year	UK share of world exports (1)	UK Trade Terms Index (2)
1966	13.2	106
1967	12.2	106
1968	11.3	100
1969	11.2	99
1970	10.6	100
1971	10.9	102
1972	10.1	103
1973	9.4	94
1974	8.8	94

(1) More precisely, the percentage share of main manufacturing countries' exports of manufactured goods. (Source: BOTB)
(2) The index compares the average price of UK exports with the average price of manufactured exports of main competitors, measured in US$. (Source: Economic Trends)

The fact that, when United Kingdom prices have declined in comparison with competitors', its share of world exports have also declined leaves little doubt that there are factors which are very much more important than price in deciding the level of exports. Hence, the importance of interest rates is minor.

CHAPTER 14

CONCLUSIONS

Short term finance for exports presents no special problems in any of the countries studied, other than insignificant procedural inconvenience.

With minor exceptions, differences in export finance facilities between the countries are attributable more to differences between the existing financial institutions and practices than to any special arrangements being made.

Problems are concentrated in the sector involving more than two years credit for developing countries. Total potential demand from these countries is so great that sufficient finance is not available from private sources and the risk of default so high that decisions and most risks are effectively taken by Government departments, especially in France and the United Kingdom. Finance is provided more and more from Euro-currency sources (effectively US$ and DM) either directly, or through long-term funds raised by specialist banks in France, the Netherlands and the Federal Republic. Internal sources of finance for these credits have been extended - in the United Kingdom, the Consolidated Fund supplements the financial institutions, in France, the emphasis is shifting from official sources to the banking system, in Germany the mortgage banks have joined the commercial banks and the Government in providing funds, and in the Netherlands there is Government assistance

to the commercial banks.

More Government intervention is encountered in France (where it is typical of all banking and economic activity) and the United Kingdom than in the Federal Republic and the Netherlands, in both of which countries industry and the banking system as a whole appears to be more self-reliant in export matters.

Differences in overall export performance can not now be generally attributed to special export finance. While in the 1950s and 1960s there may have been some selective aid, the importance of this has been exaggerated. Exporting countries are now so apprehensive of widespread defaulting that assistance is limited by agreement. This is not to say that there is never any attempt to "bend the rules" on occasions, but exchange of information is so well organised that there would would soon be complaints if it became common. Rather as in oligopolistic competition, participants tend to compete on the fringes, but do not want to become involved in an all-out war.

Viewing the facilities as a whole, United Kingdom exporters probably receive more assistance than other countries. France comes a close second, though because of the tradition of detailed Government control over all French banking activity, it is impossible to make a direct comparison. Germany and the Netherlands give less support.

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Ausfuhrkredit-Gesellschaft m.b.H.

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