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ECONOMIC COMMITTEE

NATO COUNTRIES' CREDIT POLICIES
TOWARDS EUROPEAN COMMUNIST COUNTRIES

Note by the Chairman

The attached study has been prepared by the Economic Directorate following a request by the Council on 18th March, 1974 (C-R(74)10) that the Economic Committee examines in depth the whole range of problems concerning Western trade with the Communist countries, with a view to drawing relevant conclusions.

2. This Working Paper is submitted to the Committee for its consideration and comments.

(Signed) Y. LAULAN
Chairman

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This document includes: 3 Annexes

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NATO COUNTRIES' CREDIT POLICIES TOWARDS EUROPEAN COMMUNIST COUNTRIES

I. BACKGROUND

1. Between 1958 and 1972 European Communist countries(1) have increased their imports from NATO countries on average by 14% a year.

2. Capital goods and machinery constituted the bulk of their imports with the exception of some years, such as 1963-1965 and 1972-1973, when large-scale imports of agricultural products took place to make up for shortages in national production. The growth in Communist countries' exports to NATO countries, however, was slower: 12% a year, on average.

3. As actual imports and prospects for further purchases in the West grew faster than the European Communist countries' exports and export potential, these countries were faced with serious balance of trade difficulties compounded by inadequate foreign exchange reserves.

4. However, despite their hard currency shortages, the Communist countries increased their purchases of advanced technology in industrialized market countries by relying increasingly on export credit facilities offered by the exporting countries. Over the period 1965 to 1972 Soviet and East European purchases on credit in NATO countries amounted to $3,882 million and $5,483 respectively(2), and accounted for nearly one quarter of total purchases ($36,840 million).

5. The USSR has increased its purchases in NATO countries on credit considerably since 1964. While at the end of 1964 the outstanding credits to the Soviet Union had amounted to nearly $600 million, at the end of 1969 they reached $1.5 billion and three years later, by the end of 1972, $2.7 billion.

6. The East European countries started to reap the benefits of export facilities offered in NATO countries much earlier than the USSR. As far back as 1962 the outstanding credits to Eastern Europe had reached $1.2 billion, almost as much as the 1969 amount of ($1.5 billion) credits to the USSR. Although in that year the outstanding credits to Eastern Europe still exceeded those extended to the USSR by $700 million, at the end of 1972 the difference was no more than $100 million: $2.8 billion against $2.7 billion to the USSR.

(1) Soviet Union, Poland, German Democratic Republic, Hungary, Czechoslovakia, Bulgaria and Rumania
(2) The credits referred to in this paper are only those which are guaranteed by Governments

Most of the credits extended to the East, in particular to the Soviet Union, have been long-term (over five years) credits. Indeed, at the end of 1972 over 90 per cent of the outstanding credits to the Soviet Union were long-term credits; in the case of Eastern Europe long-term credits accounted for over half of the total outstanding credits(1).

7. In 1972 orders for machinery and equipment by the Communist countries in NATO countries are estimated at $2.2 billion, and those for 1973 at $2.9 billion(2). These orders and the recent declarations of Communist countries' leaders in favour of increased East-West trade and economic co-operation suggest that in the coming years these countries will continue and might even increase their purchases in the West. It would seem, therefore, reasonable to expect them to rely on export credits and other financial facilities even to a larger extent than in the past.

8. In view of the likelihood of large extensions to the European Communist countries it might be considered desirable to develop within NATO the consultation procedure which, for the time being, is mainly based on the periodical reports(3) on guaranteed export credits extended to Communist countries and on <u>ex post</u> notification(4) of over five year credits.

II. THE TERMS ON WHICH CREDITS TO COMMUNIST COUNTRIES ARE EXTENDED

9. In normal practice export credits are issued to all countries which want to benefit from them so long as they have a good creditworthiness rating. According to this criterion most of the Eastern Communist countries, and in particular the Soviet Union, are considered as reliable borrowers. The Soviet outstanding debt to the West, estimated at $2,450 billion at the end of 1972(5) is comparable to the outstanding debt of some of the less developed countries(6), although the latter are not endowed with similar natural resources or industrial productive

(1) C-M(74)10, dated 14th February, 1974
(2) AC/127-WP/387, Annex I
(3) AC/127-D/331
(4) AC/127-D/154(Final) dated 21st October, 1964
(5) JEC, Joint Economic Committee, US Congress, 27th June, 1973 page 702
(6) Source: Development co-operation, OECD Review 1973. Total reported debt outstanding of Brazil amounted to $4,558 million at the end of 1971 and export credits amounted for over half of this debt ($2,558 million). In the case of Chile its total outstanding debt rose to $2,443 million; of this ($1,110 million) were in the form of export credits.

capacity. Moreover, the recent rises in commodity and energy prices have improved the borrowing position of some Communist countries(1), in particular that of the Soviet Union. With regard to the latter, which is the second world producer of gold, its position has been strengthened by the staggering increase in the price of this metal.

10. The recent change in the terms of trade, the increased cost of borrowing in the West and the growing inflationary pressures leading to a fast erosion of the value of several Western currencies raises the question as to whether the present terms on which credits are granted to industrialized countries including Communist ones are appropriate from an economic point of view.

11. The policy of NATO countries on export credits to the Communist countries has so far been based on the principle of non-distrimination between these countries and other industrialized countries.

12. Financial terms

The rates of interest charged by NATO countries have differed considerably over the years and from one country to another(2). Currently the Common Market countries are in the process of reaching a "gentleman's agreement" to charge a minimum 7% interest on export credits, and in the case of Communist countries to limit the duration of credits to 8½ years(3).

13. It will be noted that the above rate is similar to that applied by the Export-Import Bank of the United States. This may be an indication of an attempt to co-ordinate on a *de facto* basis the financial terms of export credits granted by the main credit granting countries which are also NATO members.

14. In the present situation there is a substantial discrepancy between this rate of 7 per cent and the rates currently quoted by central bank discount rates, central government bond yields and commercial bank lending rates to prime borrowers.

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(1) Exports of arms may become an additional source of hard currency earnings for certain Communist countries as demonstrated in 1973 by Russian sales on cash of armaments to Egypt and other Arab countries. This would have a positive effect on the borrowing capacity of these countries, in particular the Soviet Union, East Germany and Czechoslovakia.
(2) See Annex III
(3) Annex I of this paper discusses the procedures which have been set up in the Common Market in respect of export credits.

	Central bank discount rates	Domestic government bond yields	Commercial bank(1) lending rates to prime borrowers
US	7.50	7.57	8.75
Canada	7.25	7.74	9.50
Belgium	8.75	8.14	10.50
France	11.00	9.85	13.45
Germany	7.00	10.55	13.00
Italy	9.00	7.65	10.50
Netherlands	8.00	9.35	12.00
UK	12.50	12.47	14.00
Denmark	10.00	12.94	12.00
Norway	4.50	6.22	7.50
Euro-dollar	-	-	9.13

15. Moreover, with few exceptions, NATO countries will be facing serious balance of payments difficulties because of the steep rise in the prices of oil, raw materials and foodstuffs. The current account deficit of six of the NATO countries alone (USA, Canada, Britain, France, Germany and Italy), in 1974 is estimated around $20 billion(2). Most industrialized countries will probably try to finance their current account deficit by Euromarket borrowings.

16. In the light of the foregoing it cannot be altogether excluded that export credits extended to all industrialized countries could become more expensive for the borrower in future. Such a development, however, might call for a co-ordination of the NATO countries' policies with those of the non-NATO countries(3) to avoid a distortion of the conditions of competition(4). In carrying out such an operation industrialized countries would, however, have to take into consideration the interests of the less developed countries which have been especially hit by the recent developments in world commodity prices and by inflation in the West.

(1) World Financial Markets, Morgan Guaranty Trust Company of New York, 19th March, 1974.
(2) The Economist, 23rd-29th March, 1974, Survey page 8. The European Commission in April 1974 has estimated the balance of payments deficit of the "Nine" at $22 billion for 1974
(3) Japan, the second largest trading partner of the Soviet Union among the industrialized Western countries, is charging between 5.5 and 6.8 per cent on the export credits issues to the USSR (AC/127-WP/390)
(4) See Annex II which reviews the discussion in OECD on this matter.

17. An increase in interest rates on export credits issued in industrialized countries in favour of other industrialized countries would avert distortion of competition between the home producers and foreign producers. Export credits can cause such a distortion especially between countries which belong to a customs union. Export credit facilities encourage the purchaser to buy where the credit is cheap and since, at present, export credits are cheaper than normal domestic commercial credits, the purchaser might prefer to import rather than buy at home. The exemption from duty in a customs union adds to the attraction of imports from other members of the union over purchases in the home market since the advantage margin offered by cheaper credits is not offset by the customs duty.

18. Should inflation in the West continue at its present level - between 8.5 and 20 per cent a year in the OECD countries - an increase in the rates of interest on export credits might become unavoidable. By lending long-term at fixed rates at a time when capital in the Euromarket is in general available for medium-term and at high floating rates(1), the credit granting countries would be encouraging importing countries to borrow even when they are capable of paying in cash. Indeed, higher rates on export credits might well induce the Soviet Union to pay in cash. That it is capable of doing so is proven by the recent Soviet decision to finance the first phase of the large Kursk steelworks project worth DM. 2,200 million.

19. An increase in interest rates on export credits could not be decided without due regard to its possible impact on foreign trade, domestic production and employment. Export credit facilities play an important part in promoting trade between nations. A restriction on them might well have adverse effects on international trade between industrialized countries as well as between market and socialist economies.

20. Countries facing balance of payment difficulties are tempted to interfere with their foreign trade flows through various stratagems such as devaluation floating exchange rates or indirect subsidies. The promotion of exports by the manipulation of export credit terms would result in a further distortion of international competition which should, no doubt, be avoided.

(1) Herald Tribune, dated 1st April, 1974

III. THE ATTEMPTS WITHIN NATO TO REACH A COMMON EXPORT CREDIT POLICY, VIS-A-VIS THE COMMUNIST COUNTRIES

21. The various problems discussed above and the difficulties involved in fixing and implementing a common single interest rate between a large number of countries deterred NATO members from discussing in depth in NATO the financial terms of export credits. This reluctance to consider a co-ordination of financial terms resulted to a large extent from discrepancies in the economic situation of the member countries; different rates of inflation, different degrees of dependence on imported energy and raw materials, size of the share of foreign trade in gross national product, balance of payments difficulties and foreign reserve position. All these factors obviously called for a very flexible approach to the problem of how to encourage exports.

22. Therefore, since 1959, discussions at NATO have been based on other than the financial aspects of export credits.

23. As early as 5th August, 1959 the Council decided to establish a reporting procedure(1) on credits extended by NATO countries to Communist countries. In addition, as regards government-to-government credits to the Soviet Union, all member countries agreed, if they intended to grant such credits, to inform the Economic Committee about it so that the matter may be discussed there. The procedure enabled the Council to keep track of the outstanding credits to these countries. A number of revisions to the reporting procedure were made over the years(2). The present reporting procedure has allowed a better assessment of the link between credits and the development of exports to Communist countries. It has also made it possible to evaluate the creditworthiness of the borrowing countries.

(a) Attempts to carry discussions in NATO beyond the procedural level

24. Shortly after the inception of the reporting procedure discussions were initiated in the Economic Committee and in the Council on the advisability of extending credits; the possible effects of such credits on the economic and military strength of the Soviet Union; the need of keeping track of the total credits extended; the wisdom of granting credits to Communist countries rather than to developing countries, the desirability of giving long-term credits to Communist countries. These discussions brought to the fore major divergencies which existed among NATO countries on the question of export credits and prevented them from agreeing on a common policy. Nevertheless, discussions in the Council indicated that certain countries felt that caution must be observed in the credit policies of the Allies towards Communist countries.

(1) C-M(59)75, approved by C-R(59)30 page 10 dated 15th August, 1959
(2) AC/127-D/99(Final) dated 9th July, 1962, AC/127-D/174(Final) dated 23rd February, 1965, AC/127-D/244 dated 21st February, 1968, and AC/127-D/331 dated 2nd February, 1971

25. As for the advisability of extending credits, in particular long-term ones to the Communist countries, discussions in NATO on this question were inconclusive and were, in fact, overtaken by events. On 12th June, 1963 the Councul instructed the Economic Committee to study the implications for the Alliance of the extension of credit guarantees to Communist countries and "the possibilities of evolving an agreed policy to them"(1).

26. The study(2) prepared by the International Staff pointed out that the extension of long-term credits would have significant effects on the economic development of the Soviet Union and on the allocation of resources in that country. In the Committee as well as in the Council considerable time was devoted(3) to the examination of possible effects of long-term credits on the economies of Communist countries and the consequent implications for East/West relations and balance of forces. NATO countries differed considerably in their conclusions and could not agree on a common policy.

27. At that time, a joint approach(4) was made by France, the Federal Republic of Germany, the Netherlands, Belgium and Luxembourg, in favour of restricting government guarantees to export credits of five years duration, limiting the guaranteed portion on credits to 90%, making the buyer pay for at least 15% of the order at the time of the signing of the contract, setting up a procedure to allow for consultations among NATO countries before issuing long-term credits in order to match third country offers and revising the reporting procedure on outstanding credits to Communist countries to show how much credit was in fact extended by individual NATO countries. These suggestions failed to be accepted by all the other NATO members.

(b) <u>The problem of the long-term credits to Communist countries</u>

28. Two schools of thought have existed among NATO countries on the question of long-term credits to the East and have made it impossible in the early 1960s to reach a common position. A number of countries argued that the extension of long-term credits to the East would, in fact, be synonymous with economic aid. In their view even if the total amount of long-term credits were insignificant they could play a vital rôle in the economic development of the Communist countries as the latter were so short of hard currency.

(1) C-R(63)32, Item V, paragraph 83(3)
(2) AC/127-D/144
(3) C-R(63)65 and 66, dated 18th November, 1963
(4) AC/127-D/135, dated 30th September, 1963 or in the Annex of AC/127-D/144

They felt that long-term credits would allow the Soviet Union to devote more resources to military defence and dispense it with the need to allocate funds for research and development in the civilian field. Moreover, the extension of long-term credits to the Communist countries would be depriving developing countries from scarce financial resources which they badly needed.

29. The other member countries insisted that the extension of credits was part and parcel of foreign trade. They served the interests of the lenders just as much as those of the borrowers. Export credits to industrialized Communist countries could not be considered as an instrument of economic aid but were a means of promoting trade. The hard currency resources which would be made available to the USSR in the form of long-term credits would only be a very small percentage of the gross national product of that country and, therefore, would not have a significant impact on the allocation of Soviet resources. The denial of long-term credits would in no way prevent the Soviet Union from procuring essential equipments since, in the last resort, it could concurrently reduce its imports of non-essentials, increase gold sales and its gold production.

30. One NATO country particularly objected to considering straight-forward export credits granted to Communist countries on commercial terms as a form of aid. In matters of export credits that country was reluctant to draw distinctions between industrialized and developing countries or between industrialized market economies and socialist countries.

31. Others have argued that in any case developing countries whose absorptive capacity was limited could not benefit from the export credits destined to the Communist countries, as these were buying the type of goods which were not usually sold to the developing countries. Sales to the Communist countries helped the exporting countries to develop certain branches of their industry, to take advantage of the expansion of new markets, to devote more resources to research and development and thereby to increase their productivity.

32. Unable to reach a common policy on long-term credits the Economic Committee decided to initiate an ex post facto notification procedure(1) on long-term credits they might issue to Communist countries. It was agreed that mutual information on long-term credits would apply to supplier's credit as well as to financial credits. The Council, on the other hand, on several occasions invited the Economic Committee

(1) Procedure in document AC/127-D/154(Final) dated 21st October, 1964

to carry out factual analyses of the significance of the continuing increase in the extension of export credits to the Communist countries(1) and on the credit-worthiness of those countries(2). A number of special reports have been forwarded to the Council during the last few years on these matters(3).

IV. THE RECENT DEVELOPMENTS IN THE FIELD OF EXPORT CREDITS TO COMMUNIST COUNTRIES

33. The change in East/West political climate and the agreement reached in NATO to promote trade with the East as a means of furthering détente(4) have, no doubt, encouraged the rapid increase in the amount of credits, especially long-term, extended by NATO countries. In 1971, for instance, Soviet imports of pipe and machinery from NATO countries were financed up to 35 per cent on long-term credits drawn in that year(5).

34. Over the last few years the European Communist countries, in particular the Soviet Union, have shown great interest in the possibilities of developing industrial co-operation with Western countries. This particular aspect of economic relations between the East and the West is currently examined in the context of the CSCE.

35. The nature of projects which the Soviet Union seems interested in developing with Western assistance (natural gas, oil, timber, nuclear electricity, various ferrous and non-ferrous ores), would suggest that if that country decided to

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(1) C-R(67)30, Item 4
(2) C-R(70)8 and C-R(70)32
(3) C-M(68)6, C-M(72)12, C-M(72)13 and C-M(73)82
(4) C-M(66)84(Final) dated 28th November, 1966 paragraphs 6 and 7 read as follows:

(6) An intensification of trading exchanges between individual NATO countries on the one hand, and the Soviet Union and Eastern European states on the other, would serve a useful purpose, both from the political and the economic point of view, and should be promoted as far as possible.

(7) Many problems in the field of promotion of trade and economic co-operation would, however, have to be taken into account. The Committee of Economic Advisers should intensify its valuable studies of East/West trade, and examine the possibilities of facilitating such trade. This examination could comprise - so far as it is relevant in this context - the possibility of extending the scope of industrial and technical co-operation with the East.

(5) In 1971 Soviet imports of pipe and machinery amounted to $873 million (AC/127-WP/378, Table D.I dated 4th March, 1974). Drawings on credit over five years totalled about $320 million (C-M(74)10, Table IV dated 14th February, 1974).

continue to draw on Western credit facilities it might also benefit from credits of a duration considerably in excess of the 7 or 8 years, which have been granted up to now. Indeed, the lengths of credits is determined by the nature of the goods bought or of the projects envisaged. This could mean that it might be difficult for the Common Market countries fully to adhere to the arrangements which they are at present considering(1).

36. Attention should be drawn in this connection that most East European countries which are much less endowed with natural resources than the Soviet Union may not, to the same extent, benefit from the type of long-term credits discussed above. Moreover, these countries which are not as well off financially as the Soviet Union might find it difficult to increase their long-term indebtedness to the West. The financial weakness of some Eastern European countries have already resulted in requests for loans from some NATO governments. Rumania, for instance, was reported to have requested from West Germany a government loan for $300-400 million, repayable in 15 years. However, the loan which was extended to Rumania was not a government one; it was granted by a German bank with an official guarantee. It aimed at helping Rumania to repay its 1970-71 overdue debts and is to be refunded in four installments between 1978 and 1981: the rate of interest is 9.25%. Information concerning negotiations on a possible West German government loan to Poland of the order of DM. 1,000 million appeared in the Press some time ago(2).

37. The change in the political climate and the high credit rating which most Communist countries enjoy in the West, enabled them to draw on Western financial resources other than export credits. This is a development which is bound to have considerable repercussions on future East/West financial, economic and trade relations. It should be borne in mind that Western financial facilities have, over the last few months, been considerably stretched as a consequence of Western countries' current balance deficits. It is anticipated that OPEC funds will be flowing into the Western financial markets and thus increase the available liquidity.

38. The demand(3) for these funds, however, is bound to be considerable and should the Soviet Union and other East European countries also attempt to borrow on the market this might lead at least in the short-term to greater competition for available funds and push up interest rates. Consequently, it would be in the

(1) See Part II, paragraph 12 above
(2) Financial Times, 10th October, 1973. At this stage, the only government-to-government loans to Poland are those extended by the United States prior to 1960 and are being gradually reimbursed
(3) Herald Tribune, 1st April, 1974. Kreditbank Luxembourgeoise has estimated that the volume of Euro-currency bank credits totalled around $10 billion in the first quarter - about half of the amount raised during the whole of last year

interests of NATO countries to inform each other of developments in this field to the extent that information is available to them.

39. European Communist countries are able to take advantage of other forms of financing such as lines of credit, medium-term Eurodollar loans and even long-term bond issues. Soviet Eurocurrency borrowing, for instance, has been estimated at over $1,000 million(1). Although it is difficult to judge the accuracy of this information it is not possible to rule it out altogether.

40. Even such a small country as Hungary has succeeded, between 1968 and 1973, to borrow $300 million from the Euromarket(2) to finance the expansion of export-oriented industries such as pharmaceuticals and aluminium. Hungary also raised $75 million in the Eurodollar market through the floating of bond issues(3). Since Hungary has been so active in the Euromarket her accumulated outstanding debt to NATO countries on supplier's credit was only 146 million(4) at the end of 1972, one of the lowest among Eastern countries. Hungary was also able to cover its need for Western financial resources to a large extent through industrial co-operation agreements (since 1964 negotiated agreements totalled $240) and through joint ventures, which helped to reduce her need for export credits or Eurocurrency borrowings(5).

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CONCLUSIONS

41. A review of East/West trade relations and in particular the conditions under which credits are extended to Communist countries has now become necessary because: (i) while on the one hand Communist countries' purchases on credit in Western countries has registered a sharp increase in the last few years and it seems that this trend will most probably continue in the near future(6), (ii) most Western countries are experiencing unprecedented inflation rates along with serious balance of payments difficulties which compel them to adopt restrictive monetary policies which in turn push up the interest rates in the national financial markets as well as in the Eurocurrency markets.

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(1) Financial Times, 19th June, 1973
(2) AC/127-WP/375, Appendix IX
(3) AC/127-WP/375, dated 6th March, 1974
(4) C-M(74)10, dated 14th February, 1974, Table VII
(5) AC/127-WP/375, dated 6th March, 1974
(6) In 1973, for instance, Soviet trade with the non-Communist countries grew by 40% whereas the overall growth of Soviet trade with Socialist countries was merely 9 per cent (Herald Tribune, 11th April, 1974). In 1972 Soviet imports from OECD countries grew by as much as 50%. Other Communist countries also seem anxious to increase their trade with the West. Rumania allegedly wants to increase its imports from the West in 1974 by over 40 per cent (Financial Times, 19th December, 1973). The Poles seem equally anxious to expand their partnership with the West with the help of Western credits and counterpurchase agreements.

42. Consequently, the discrepancy between the terms on which export credits are issued and the terms on which capital is now available to private or public borrowers in national financial markets or in the Euro-currency market is becoming more striking than ever before. An alignment of the terms under which export credits are issued to the conditions prevailing in the financial markets may have, therefore, to be considered. Such an examination would have to cover credits granted to all countries irrespective of their economic system.

43. It would, accordingly, seem that there should now be a more flexible and co-ordinated approach to export credit policies. This would imply a periodic alignment of the terms on which export credits are issued to those which exist in the national and Euro-currency markets. Discussions between NATO countries in appropriate fora might, therefore, be helpful to review the developments taking place in the financial markets and facilitate the necessary adjustments as far as export credit terms are concerned.

44. Moreover, the periodic discussions in NATO might also facilitate the review of the developments in the terms of trade, taking particular account of those with Communist countries. The conditions under which credits could be extended to countries which benefit from an improvement in the terms of trade might be stricter than those extended to countries which do not have benefit from a similar improvement.

45. In this respect, it is noteworthy that the Soviet Union is at present enjoying exceptionally good terms of trade in view of the recent rise in energy prices, gold and raw materials. Sales of petroleum of the order of 50 million tons a year to convertible currency countries would result in Soviet earnings of the order of $2.8 to 3.8 billion in a year which is enough to wipe out Soviet current indebtedness.

46. Moreover, Soviet exports of certain industrial products are bound to become more competitive in view of the present rates of inflation which are prevailing in the West. In this respect the Soviet Union is in a far better position than Western countries to hold down the prices of its industrial goods. The competitiveness of Soviet goods would also improve a pace with the development of East/West industrial co-operation.

47. The small East European countries, most of which are not endowed with large natural resources, will probably find themselves not in as favourable a position as the Soviet Union. On the other hand, industrial co-operation with the West might help to improve the competitiveness of their industrial products in Western markets.

THE WORK IN THE EEC ON CREDIT POLICIES

1960

In 1960 the EEC created a special group whose task was to propose/formulate suggestions to harmonize the conditions of export credits, financial credits and investment guarantees granted by the EEC countries to their exporters in trade with less developed countries.

The group was also commissioned to work out ways in which less developed countries could use, on a multilateral basis, the resources put at their disposal(1).

1962

On 15th May, 1962, a consultation procedure within the special group was set up(2). The consultation concerned credits of over five years. Work on the harmonization of conditions of credits concerned guarantee of sub-contracts, joint guarantee and risks covered.

1965

Consultation on over five years export guaranteed credits and finance was extended to:

- supplier credits;
- line of credits;
- supplier credit agreements with a given ceiling (accords-cadre);
- financial credits based exclusively on budgetary appropriations;
- mixed credits: public funds coupled with supplier or private financial credits.

Consultation procedures involved:

(a) The consulting member informs the other members on the following points:

- country which will benefit from export credits;
- the type of goods which will be exported;
- duration period requested;
- the conditions of credit that exporting country is considering to extend;
- reasons for offering exceptional facilities.

(1) J.O. 27th October, 1960 page 7339/60
(2) J.O.52, 30th June, 1962 page 1561/62

Within seven days consulted members must forward their precisions, observations or reservations, if any. Should an unfavourable opinion be expressed by any consulted member country the consulting country is requested to suspend its decision pending the taking place of consultation. The only exception is the need for an urgent decision.

Credits derived from State funds and mixed credits must also be notified to all the members on a priori basis. A consultation can be called for within seven days. A meeting should take place four days after the request. Only in those cases where urgency is called for can a member State proceed to a posteriori notification - consultation may still be held after this notification. Final decisions are always reported to all the EEC countries on all kinds of transactions.

1970

Council Directives of 1970(1). The Council Directive of 1970 laid down the common procedure for the way in which guarantees covering manufacturing risks (12 months or more) and export credits (24 months or more) should function in actual practice in all the EEC countries. (Applicable to both public and private importers).

1973

Council Decision of 3rd December, 1973 on consultation and information procedures in matters of credit insurance, credit guarantees and financial credits(2) provides for information and, if called for consultation, to take place before the final decision of the consulting country.

1974

The information provided by the consulting country might either provoke no comments from the other members, or induce other members to request further information, make comments, reservations and even express an unfavourable opinion. These members may also request that a consultative meeting should be held. In any case such meetings take place automatically if five member states express an unfavourable opinion to the transaction in question. (In practice even if there is only one unfavourable reaction a meeting is called).

(1) J.O. No. L.254/1, 23rd November, 1970
(2) J.O. No. L.346/1, 17th December, 1973

(i) The transmission of the information leading to the consultation procedure must take place as soon as possible after initiation of the study either of the guarantees and the proposed credits proper, or any other decision which would constitute a pre-requisite for the subsequent examination of such guarantees or credits. (Article 7).

(ii) The consultation procedure applies to public, private or mixed supplier credits and financial credits linked to individual contracts or global credit arrangements. The latter imply "any understanding or statement, in whatever form, whereby the intention to guarantee supplier or financial credits or to open financial credits, up to a specified or ascertainable ceiling, and in respect of a connected sales of transactions, is made known to a third country, or to exporters or to financial institutions." (Article 3 of Decision 73/391/EEC).

Prior consultation on a global arrangement may be limited to the arrangement itself. It may be extended to individual transactions falling under that arrangement, if, at the time of the oral consultation or global arrangement, at least five member countries request this specific procedure.

Consultation on individual transactions are initiated by the exporting member country, whenever the duration of the supplier or financial credit is likely to exceed five years and/or the balance of the local portion (expenditure in the buyer's country) financed by guaranteed private credit is expected to exceed 5% of the contract price. The consulting country must submit to the other members information on the following points:

- country of destination;
- location of the transaction;
- type of material and number of items to be supplied;
- whether transaction is to be put for international tender;
- principal credit terms applied for by proposed recipient;
- credit terms the authorities in the exporting country propose to offer.

Information on the terms include the percentage of the deal provided by credit, duration of credit and starting point thereof; repayment rate (schedule of payments), amount of effective interest subsidy, if any, where interest is different from that generally charged; interest rate if the credit is to be granted out of public funds; credit insurance charges; scope and terms of any financing of local expenditure (in buyer's country).

Global credit arrangements are also subject to consultation. The consulting country must submit information on the following points:

- country of destination;
- ceiling of global credit arrangements;
- purpose of credit (type of material to be supplied);
- credit terms and eligibility requirements for individual contracts (e.g. closing dates, minimum contract prices to be set);
- reasons for granting credits of a duration exceeding five years and the fixing of local costs beyond 5%.

The final decision of the consulting member country will be made known to the other member states. If this decision diverges from the points of views of the other members, the consulting country is required to explain the reasons for which it was unable to take account of comments, reservations or unfavourable opinions expressed by the partners consulted.

The Common Market countries have initiated discussions with a view to reaching a gentleman's agreement on financial and certain other aspects of export credits. They are proposing to fix the minimum interest rate at 7 per cent on export credits to limit the duration of export credits extended to industrialized countries to five years, to Communist countries to 8½ years and to developing countries to 10 years(1).

(1) ICE 20th March, 1974

THE WORK IN THE OECD ON EXPORT CREDITS(1)

Objective

To avoid a credit race and the distortion of trade competition.

In its approach to the question of export credits the major preoccupation of the OECD has been to prevent the development of uncontrolled credit competition among its members.

The OECD countries have to avoid a credit race which, if not checked, could inevitably result in a distortion of the conditions of trade competition.

Ways and means proposed and/or adopted for controlling credit competition.

As early as 1962 the OECD initiated discussion on how to control competition in the field of export credits.

Confrontations of policies in the field of export credits.

In 1962 a special high-level group on Export Credits and Credit Guarantees was set up. It was commissioned to hold regular confrontations on the policies pursued by governments of member countries in the field of export credits and credit guarantees. The whole purpose of such confrontations was to allow for (i) the analysis of national policies; (ii) the identification of problems and (iii) consideration of possible solutions. Once national policies and problems were identified and solutions accepted, the aim would be to adopt common guiding principles and to bring about improved co-operative action among the OECD countries by means of prior consultation, notification and/or question and answer procedures.

Limitation of the duration of credits to five years.

The Special Group which met for the first time on 26th and 27th April, 1962 examined in detail the proposals of the member states of the Common Market for the limitation of terms and payment to give years (from the date of delivery) on credits extended to developed countries which included the Communist countries. Derogations from this rule would be possible only if the issuing country agreed to consult its OECD partners before reaching a decision. In short, the Common Market countries wanted prior consultation before any extension of credits beyond five years. It was hoped that consultation would provide the opportunity for dissuading a member country from a course of action which its partner might consider undesirable.

Prior consultation rule.

(1) The following information is given on the basis of documentation which was available to the International Secretariat. Therefore, it may not be completely up-to-date.

Obligation to report long-term credits extended to LDCs.

A further derogation to the five year limit concerned credits extended to less developed countries. Credits beyond five years could be extended to less developed countries on condition that the creditor country agreed to inform the other members of the OECD of its decisions. This information to be supplied as soon as a firm offer of guarantee has been made to the exporter. The obligation to inform would also apply to promises of Government credits tied to supplies from the member country concerned(1). The United Kingdom argued that it would be difficult for her to reconcile the proposed distinction between developed and underdeveloped countries with the ECGD criterion which was that of the borrower's credit-worthiness.

A maximum ceiling on percentage cover.

The EEC proposals also provided for a limitation to 90% guaranteed proportion of export credits or private financial credits tied to national supplies. No agreement could be reached on this matter.

Joint guarantees.

The Common Market countries also proposed that OECD countries should undertake to guarantee sub-contracts originating in another member country up to 30% of the total amount of the contract. This proposal was received favourably by the other members though certain countries, for statutory reasons, e.g. United Kingdom and United States, stated that they could not accept joint guarantees(2).

Improved co-operation.

Discussions on the Common Market proposals showed that divergences between the practices of member countries were too great to permit the adoption of detailed rules prescribing uniform conditions for issuing and guaranteeing export credits. The Special Group therefore attached greater attention to the promotion of co-operation between member countries by setting up an exchange of information and consultation procedure based on a notification of credits beyond five years as well as on a question and answer system. The latter would take place on a bilateral basis between the countries concerned. The question as to whether the consultation and information procedure should

(1) OECD/TC(62)15; Annex I gives the full text of the EEC proposals
(2) TC(62)15, 25th May, 1962

apply to guarantees and credits extended to less developed countries was once again raised. Since it proved difficult to agree on a criteria to distinguish between export credits which have a predominantly aid character from those which are basically of a commercial kind, the Special Group recommended that: (i) member countries should undertake to notify the Organization of all the transactions exceeding five years immediately after the guarantee is issued or the credit is granted; (ii) confrontation should follow notification on supplier credits and tied financial credits, but credits extended on the basis of inter-governmental agreements and transactions essentially of a political character would be exempted from the consultation procedure. It was thought that the notification and consultation procedure would be of great help in the elaboration of common guiding principles governing the terms of credits beyond five years. The German Government proposed that global credits "les accords cadre", tied financial credits and/or tied loans granted exclusively from public funds should not be subject to notification procedure(1).

Notification of all credits beyond five years. Consultation subsequent to notification.

Further attempts at improving consultation on long-term credits to LDCs.

In 1964 the OECD concentrated on the question as to whether commercial credits to LDCs should be granted on the same conditions as aid facilities. Certain OECD countries insisted that credits tied to commercial transactions should not exceed ten years and that the minimum duration period for aid facilities should be 15 years. Certain other countries, however, argued that commercial lending between 10-15 year range could well be justified if the objective was to allow for repayment from the earnings of the project in question or to take into account the recipient country's balance of payments situation and its debt servicing capacity. Other countries argued that funds available for aid credits were limited and, therefore, needed to be supplemented by longer term export credits. One member country argued that aid usually affected trade flows and countries which did not have the possibility of extending aid out of budgetary resources should not be prevented from competing by extending long-term commercial credits(2).

(1) OECD TC(63)27, 27th May, 1963
(2) OECD TC/ECGW(64)2

The discussions revealed that unless the terms, and in particular the duration of tied aid loans, were controlled or subjected to common principles, the terms of credits issued in connection with commercial transactions could not be expected to be more rigid or to be subjected to common rules.

Long-term credits to industrialized countries

Proposals put forward by the Common Market countries in favour of prohibiting the extension of credits or guarantees beyond five years to industrialized countries proved to be unacceptable to the other member states of the OECD(1).

Exchange-of-information system on export credits of over five years duration

Attempts to agree on a system of exchanging information were made over the period 1965-1971. In the latter year an understanding was reached whereby countries taking part in the exchange of information undertook not (without prior notice) to guarantee any deal in which the terms of credit offered were better than the most favourable terms already notified in the course of the exchange of information.

Entry into force of the Exchange-of-Information system

The entry into force of the exchange-of-information system, however, was held up since the Common Market countries insisted that this should coincide with the date of entry into force of the prior consultation procedure on long-term credits(2) between industrialized countries. The International Secretariat is not aware whether this issue is now settled.

Proposed prior consultation procedure

Prior consultation procedure would have involved an undertaking by each participating country that contemplates guaranteeing a long-term commercial credit to notify the other participants of the terms envisaged, and not to take any final decision before a fixed period of time has elapsed in which its partners may put forward their comments(3).

The consultation procedure, like the exchange-of-information system, would not have covered interest rates, nor local expenditure.

(1) TC/ECGW(64)21 First Revision, dated 20th January, 1964. These proposals were also submitted to NATO and met with the same result
(2) See above page 2
(3) OECD: C(72)92, dated 6th April, 1972

Some OECD countries were unable to accept this procedure since it involves binding waiting periods coupled with disclosure of sensitive commercial information before the conclusion of contracts.

INTEREST RATES ON MEDIUM/LONG TERM EXPORT CREDITS IN NATO COUNTRIES

	As of 1st July, 1971		1974(1)	
	up to five years	over five years	up to five years	over five years
UNITED KINGDOM ***				
Buyer Credit	7%*	7%*	7%	6 - 8½%
Supplier Credit	7%*	7%*	7%	6 - 8½%
FRANCE ***	up to five years	seven years or more	1972(2) seven years or more	
Buyer Credit	6.31%	6.83%	6.50%	
Supplier Credit	6.16%	6.67%	6.35%	
	+ 0.5% (where the insolvability of the buyer is not guaranteed by COFACE)			
CANADA ***	5 - 9.99 years	10 - 14.99 years		
	6 1/8% Commercial prime base	6 11/16% c rates 1 or 2% higher than the rate which was 6.5% in July 1971	+ Commission ½%	
ITALY **	1971	1972		
	5.5 - 7.5%	6.5%		
NETHERLANDS *** Buyer Credit	6.5 - 7%	The rate of interest does not vary with the duration of the credit + commitment fee 1%		
Supplier Credit (a) not covered by a guarantee	8 3/4%			
(b) covered by a guarantee	8.5%			
NORWAY *** At an average	7 3/4%	+ Commission ½ and 3/4% a year		
BELGIUM	6½%			
USA	7%			

* On 15th November, 1971 the rate was lowered to 6.5%
** Banca Nationale del Lavora Quarterly Review September 1972, page 306
*** OECD - TC/ECG/72.3
(1) Financial Times, 15th February, 1974
(2) Le Monde, dated 31st August, 1972