and it decreases the level of their indebtedness. Most of the present proposals emphasise the increased use of loans which will eventually increase the level of indebtedness. Grants will achieve precisely the opposite effect, they will also help to promote development.

The developed creditor countries for their part will forfeit a part of their future stream of overseas income to the extent that they agree to write-off any development debts owing to them. Against this though they will be able to increase their exports of machinery, capital goods, and so on, thereby earning more foreign exchange. This in turn will enable them to pay for their oil imports, and at the same time relieve the pressure on their balance of payments. It will also stimulate domestic investment and the level of economic activity and help to get them out of the downturn which many of them are presently experiencing.

The Arabs will benefit from the scheme as well. By matching capital grants to debt relief they can bring pressure on the developed creditor countries to reduce the debt burden of the developing countries, while they themselves are doing something positive to promote the development of these countries. This will not only earn them the goodwill, understanding and international support which they so badly need, but probably of more direct importance to them, it will ensure that the price of oil stays at, or close to its present level. It is pretty well agreed that the pre October 1973 price of oil was inordinately cheap. By the same token it would appear that the present high prices are due for a roll back. By shifting the spotlight away from the immediate crisis, the scheme ensures that whatever price is finally agreed will reflect the real economic cost of oil. On a broader plane, the Arabs have a very strongly vested and continuing interest in the stability of the international monetary system. It is essential to them, with their new-found wealth, that the system functions smoothly and efficiently, and that the cycling of the massive sums involved cause as little disruption and dismay as possible. Other proposals, by and large, either ignore or marginalise the role and function of the developing countries in the stability of the international monetary system. This one seeks to involve them; obviously it is still somewhat rough around the edges, but the central arguments are strong enough to bear serious consideration.

GEORGE C. ABBOTT

Glasgow.

"Grey-Area" Export Credit: A Comparative Study

For the past several years United States exporters of capital equipment and large, turn-key projects have complained that long-term, low-interest rate credit was available to their competitors in Western Europe and Japan, particularly for exports to developing countries. Such credit terms, they said, were not available to them in the United States, and they could significantly increase exports if the U.S. government were to facilitate the provision of equivalent types of credit. The long-term, low-interest rate credit referred to was usually that falling between maturities of 10 and 20 years and between interest rates of 3 and 6 per cent. This has come to be referred to as "grey-area" export credit. The author undertook this study to determine whether, in fact, U.S. exporters were suffering from a lack of this type of export credit.

Definition of "Grey-Area" Export Credit

This grey-area is so named because it falls between what is normally considered as foreign aid (20 years or more maturity and 3 per cent or less interest rate) and what has generally been thought of as commercial export credit (10 years or less maturity and a 6 per cent or more interest rate). The members of the Berne Union have agreed not to insure export credits of greater than 10 years in maturity, and without such insurance it is very difficult to obtain commercial financing. (There are, unfortunately, more and more exceptions to this Berne rule). This sets a limit for commercial sources of export credit. And, the DAC (Development Assistance Committee) has urged all members to offer credit terms on official foreign aid loans of at least 20 years in maturity.

Given the level of prevailing interest rates, commercial sources
could not provide export financing below 6 per cent.\(^1\) The choice of 6 per cent as an upper limit for the grey area is also related to the interest rate presently charged by the United States Eximbank.

Hence, in any given country, governmental action and policy would have to be involved in the providing of grey-area financing. This would come about in various ways.

1. Foreign aid loans are provided at higher than normal interest rates and lower than desirable maturities.

2. The government subsidizes the export credits which come from commercial sources so as to reduce the interest rate below 6 per cent. This could be done as a direct payment to the commercial banks or by rediscounting the notes.

3. A governmental institution provides export credit using funds at least part of which come from the governmental budget so that the institution can arbitrarily charge an interest rate below 6 per cent.

4. Through governmental decision, cheap, long-term foreign aid loans are mixed with normal commercial export credit for the financing of a given project so that the total financing of that project has an average financing cost and maturity which falls in the grey-area.

**Other Factors in the Cost of Credit**

Obviously the maturity and interest rate charged on exported goods and services are not the only factors involved in determining the desirability of one set of financing terms relative to another. A complete comparison will also involve a study of the following:

1. Does the exporter also make provision for the financing of the local costs associated with the project? What is the cost of this financing? May the financing be used to make the down-payment and pay for other foreign costs?

2. What size of down-payment is required?

3. How long a grace period is given before the first payments must be made?

\(^1\) The research for this study was undertaken during the fall of 1972. Unless otherwise qualified, interest rates referred to were those prevalent at that time.

4. Must the exporter carry part of the financing from his own resources? (This will normally be reflected in the price).

5. What portion of the credit for financing the total project can be insured? (This will determine whether e.g. local costs can be financed in the exporter’s country).

The calculation of the actual cost of credit of a financing package, discounted to present value, is a complicated job. Also, the attractiveness of one financing package as compared with another is somewhat subjective, depending upon the resources and needs of the buyer. In addition, such comparisons are meaningless as generalizations; specific packages must be examined and compared. This could only be done in a case study approach, and should be the subject of another study. Consequently, this study looks only at maturities and interest rates, as they relate to the grey area defined above.

**Grey-Area Export Financing in Germany**

In Germany essentially all long-term export financing comes from the Kreditanstalt für Wiederaufbau (KfW). Another institution, the Ausfuhrkredit Aktiengesellschaft (AKA) provides financing for periods up to 8 years. If the credit terms go over 8 years, AKA can provide that portion up to 8 years and the KfW would finance the portion over 8 years. In addition, it should be noted that German exporters frequently make use of the Eurodollar market as a source of financing for down-payments and for local costs of projects. But, it is difficult to borrow Eurodollars for more than 7 or 8 years.

The KfW is a governmental institution and obtains its funds directly from the government budget. It has authority to lend at whatever terms it wishes. The KfW also administers the German foreign aid program.

The AKA, on the other hand, is a financial institution which was established by about 50 commercial banks and other private financial institutions, and there is a ceiling (which varies) on the funds at its disposal. Part of the export credit paper of the AKA may be rediscounted at the German Bundesbank at 1½ per cent above the Bank rate.
As to costs, Eurodollars could usually be obtained at costs below 6 per cent. The AKA credit, however, costs about 9.3 to 9.8 per cent. KfW has a flexibility of maturity and interest rate which permits the mixture of its credit with the others to bring the total effective well below 6 per cent and well over 10 years, for guaranteed private exports. In fact, Germany has held quite strictly to the Benelux Union agreements on maturities and KfW rarely brings the total interest rate below 6 per cent.

In 1970 there were only two cases in Germany where guaranteed private credits fell within the grey-area. Both were used to finance the sale of ships to India. They had maturities of 12.25 years and 11.75 years respectively and both were at interest rates of 5.5 per cent.

In 1971 there were no cases of guaranteed private export credit in the grey-area. Many were in the range of 10 to 12 years, but were over 6 per cent interest rate. Most were between 6 per cent and 7½ per cent but some were up to 9 and 10 per cent, depending upon the amount of KfW admixture and the interest rates on its portion.

As noted earlier, the KfW also administers Germany’s foreign aid program. Even most grants are now channelled through the KfW for administration. All of the OOF (Other Official Flows) and ODA (Official Development Assistance) loans are negotiated and administered by KfW.

In 1970 the OOF and ODA loans from KfW were a broad mixture: some were tied, others untied; some as low as 1 per cent interest and others as high as 9 per cent. Only about a half-dozen fell in the grey area, most of them to finance the export of steamships. But, there was one case of a 15.5 year, 5 per cent interest rate credit to Madagascar for the sale of a textile plant ($1.4 million) and a 16.75 year, 5.5 per cent interest rate credit to Colombia for a thermal power plant.

In 1971 only about 18 per cent (in $ volume) of ODA and OOF loans from KfW were tied. Maturities varied from 9 to 40 years, but most were between 25 and 30 years. Interest rates varied from 4.4 to 6 per cent (only one loan was at 6 per cent), but most were at 5.5 per cent. Only two loans fell in the grey area and these were loans for the purpose of rescheduling previous credits.

German exporters feel that they are disadvantaged on cost of export credit insurance as well as on government support of export credit, vis-à-vis all major competing countries. They are always complaining to the banks. They know that the institutions and authorities exist to do much more. But, they realize that the government will not do more, particularly in bringing the interest rate down, as long as the balance of trade and the balance of payments remain unfavorable.

It was difficult, in Germany, to find the occurrence of a mixed credit. Officials of KfW state that they are prepared to use it if, when competing with the French, they find that the French are doing so. The author heard that this has happened on several occasions but could not obtain hard data.

The only case of mixed credit cited was apparently not a conscious plan of KfW. Rather an African country received a loan (20 years and 3 per cent) of DM 100 million from KfW to install a telephone system. Siemens got the contract. Further study showed that the cost would be DM 150 million. KfW refused to increase the level of credit. Siemens had to get the rest as a commercial credit. The result was total project financing in the grey area through a mixed credit. This may have occurred in other cases. The Germans claim that any such mixing would be the result of after-the-fact circumstances rather than a conscious, pre-planned effort on the part of KfW.

Grey-Area Export Financing in the United Kingdom

In the U.K., private export credit may be insured by the Export Credit Guarantee Department (ECGD). The commercial banks which provide the credit may rediscount such medium and long-term credit documents with the Bank of England. The rediscount rate is set arbitrarily by the Bank of England. In 1970 and the early part of 1971 this rate was 5.5 per cent. As a result, there were a considerable number of long-term export credits with maturities over 10 years and with interest costs of 5.5 per cent.

In 1970 there were 22 export contracts totalling $452.3 million which fell in the grey area, all of them at 5.5 per cent interest, most of them between 10 and 13 years in maturity, but one of them (a water turbine for a dam, sold to Argentina for $45.9 million) at 19 years maturity. In 1971, however, there were only 8 such export contracts totalling $108 million, and all of them 13 years or less in maturity.
However, in early 1971 the Bank of England raised its rediscount rate to 6.5 per cent, then to 7.0 per cent, and in 1972 down to 6.0 per cent, where it remains.

The ECGD will guarantee 85 per cent of the export value plus 85 per cent of local costs. With the ECGD guarantee, financing is obtained on both. If the foreign exchange borrowed to pay for local costs is used to pay for imports (as is usually the case) about 97 per cent of the export value can be insured, borrowed and rediscounted. Hence, the effective interest rate to the foreign buyer is only slightly above the Bank of England rediscount rate. But, at present, there is no way that this can be brought below 6 per cent and into the grey area unless the Bank of England again reduces its rediscount rate to below 6 per cent.

As to foreign aid loans, these all come from two different organizations. The Commonwealth Development Corporation (CDC) obtains its funds from the Exchequer for lending (and investment) to Commonwealth countries. These are often used to finance exports. However, although the cost of these funds to the CDC is slightly below the domestic Bank rate, the CDC must cover all overheads. Its interest rates for export credits consequently tend to be between 7 and 10 per cent. Hence, although the maturities on CDC export credits vary from 5 to 25 years, none of them fall in the grey area.

The Overseas Development Administration (OvDA) (the U.K.'s foreign aid agency) administers official development loans. In 1970 and 1971 these were nearly all at 6 per cent interest rate and all were over 20 years in maturity — mostly about 25 years. Hence, none of these fell in the grey area.

Officials of the OvDA state that they are very much against the idea and use of mixed credits, but that, in fact, they have resorted to it themselves on various occasions, under three rubrics.

(1) Matching: If the French government is offering mixed-credit financing for a project on which British firms are also bidding, the OvDA will threaten to do likewise and, on several occasions, has done so. For example, in Chile, the OvDA gave a loan for some local costs and for down-payment, allied with ECGD guaranteed export credits, for a steel mill, and again for a power plant.

(2) Sporadic Export Assistance: Uncommitted OvDA funds already available to a recipient country have been permitted, at the request of that country, to be used as down-payments for imports. For example, this has happened for the importing of locomotives by Pakistan, Sudan and Ghana.

(3) Use of Aid Loan: When a tied loan has been made to a country but no good development project is found on which to spend it, it may be used to finance U.K. exports to that country. For example, a tied loan had been made to Peru, and more than a year passed without its being used. Finally the British firm obtained the contract to engineer and build the dry dock using commercial export credit for expenditures other than the machinery.

The above mentioned cases of mixed credits have taken place over the past five years. There may have been a few others. In any case, they are sporadic and the annual total is relatively small.

The other important factor to note about the British system is that, in March of 1970, the ECGD received authority to draw on government funds to subsidize the interest rate of export credit, similar to the method followed by Mediocredito in Italy (as explained in the following section). This could substitute for the system of rediscounting at the Bank of England, but could bring the effective interest rate much lower. Although this authority has been on the books since 1970, it has not been used. It may be looked upon as a negotiating instrument — a threat — to curb the system of mixed credits as practiced by the French, for with it the effective interest rate to the buyer could be brought as low as necessary to match that offered by foreign competitors.

Grey-Area Export Financing in Italy

In Italy there are three types of export credits which reach into the grey area. There are, first, the normal medium-term export credits which reach beyond 10 years in maturity. Secondly, there are the OOF type of export credits. Finally, there are the regular bilateral loans (ODA) directly from the Italian government to foreign governments.

In 1970, there was a total of only seven ODA loans, of
which two (totaling some $42 million) fell in the grey area. The other five ODA loans were above 6 per cent interest rate. All seven were tied loans.

In the OOF category, the Italian government listed several hundred loans, almost all of which had maturities of four to five years and interest rates above 6 per cent. Only two, for about $34 million, fell in the grey area.

There were, in 1970, only four guaranteed private export credits, totaling approximately $41 million, which fell in the grey area. Both of these were at 5.9 per cent interest rate.

The key institution in Italy for making this grey-area financing available in the guaranteed private export credits is the Mediocredito Centrale, a governmental organism. It is allocated a certain amount of funds from the budget, each year, to subsidize private export credits. It only gets involved if a credit is insured by the INA (the Istituto Nazionale delle Assicurazioni). An intergovernmental "Committee for Export Credit" decides what credits will be insured and for what maturities.

The Mediocredito has three ways of subsidizing export credits:

1. It may rediscount up to 70 per cent of the credit at an interest rate of 3.5 per cent.
2. It may subsidize the interest rate (by a direct payment to the financial institution which is providing the financing) to bring the effective interest rate to the buyer down to 6 per cent or less.
3. It may rediscount 25 per cent of the credit at 3.5 per cent and subsidize the interest on the remainder (by a direct payment to the financial institution) to bring the effective interest rate on the total to 6 per cent or less.

(Note: Commercial banks rarely lend beyond 12 months. All of the medium and long-term export credit comes from one of four financial institutions: IMI, Elbanca, ICIPU, or Mediobanca).

The choice of one of the above three methods is determined by the availability of funds in Mediocredito for private export credits.

The OOF loans provided by Mediocredito are barely distinguishable from the guaranteed private export credits. For the OOF transactions the Mediocredito has access to another fund, which comes from the governmental budget. But, it uses this fund solely to subsidize private export credits by payments to commercial banks to bring the effective interest rate charged the customer down to about 6 per cent.

Grey-Area Export Financing in France

In France, long-term export credits have been refinanced through a combination of GICEX (Groupe Interbancaire pour les Opérations de Crédit à l'Exportation — a pool set up in 1961 by a group of banks to finance maturities of over five years), the BFCE (Banque Française de Commerce Extérieur), the Crédit National and the Bank of France. Recent changes (in 1972) have eliminated the use of the Crédit National and have also increased the cost of rediscounting at the Bank of France. All of this credit still must be insured by COFACE (Compagnie d'Assurance Française pour le Commerce à l'Extérieur).

Consequently, with the Bank of France rediscount rate at 4.5 per cent (end of 1972), but for a limited portion of a long-term credit, the effective cost of guaranteed export credit of 10 years and over was about 6.83 per cent.

In past years, the Bank of France rediscount rate has been as low as 2.3 and 4 per cent. The historical use of each of these rediscount rates is seen in the distribution of rediscounted export credit paper outstanding, held by the Bank of France on December 31, 1971: approximately FF 1.4 billion of 2 per cent paper was being held; FF 5.5 billion of 3 per cent paper; FF 2.0 billion at 4 per cent; and FF 0.5 billion at 4.5 per cent.

In 1970, even though there was a large volume of guaranteed private export credit, only ten transactions totaling $54.8 million fell in the grey area. All of these exports, going to Spain, Yugoslavia, Tunisia, Zambia, Iran, and India, were with maturities between 10 and 12.25 years, and interest rates of 5.75 per cent, except for 3 sales to India, for refinery equipment, where the interest rates were 5.25 per cent.

Details of similar credits in 1971 are not available but, as
the Bank of France rediscount rate was up, the number of transactions in the grey area was undoubtedly even smaller.

On the other hand, a considerable amount of French foreign aid (ODA) loans fall in the grey area. These loans are provided essentially via two different channels. Approximately two-thirds of the loans go through the CCCE (Caisse Centrale de Coopération Économique) all of which goes to French-speaking countries (most of which are former colonies, and some of which are still French territories).

The aid to Algeria, Tunisia and Morocco is negotiated government to government, project by project, and the CCCE then acts as the executing agent. For the rest of the French-speaking countries, the government (and the Assemblée Nationale) decide on the total aid and the CCCE allocates it by country and by product.

The other third of ODA loans is handled directly by the Ministry of Economics and Finance and flows primarily to the consortium countries (India, Pakistan and Indonesia) or to several Latin American countries.

In 1970 there were 60 ODA loans, totalling $138.2 million, which fell in the grey area; 60 per cent of these "foreign aid" loans had maturities between 10 and 15 years. The interest rate distribution shows that half of the credits were between 3 and 4 per cent, one-third between 4 and 5 per cent, and the remainder between 5 and 6 per cent.

Similar details for all of the ODA loans are not available for 1971. It was learned, however, that in 1971 the 2/3 of total French ODA loans which are handled by the CCCE totalled $157 million. Of these, a total of $56 million were in the grey area.

Henceforth we have spoken of the ODA loans which, in themselves, fall in the grey area. In addition there is the matter of mixed credits. Officials at the CCCE agreed that a policy of mixed credits was followed systematically as a means of channelling the maximum amount of goods and services to the recipient countries relative to the amount of ODA funds allocated by the government and the National Assembly. It was found that all CCCE loans to sub-Saharan Africa in 1971 totalled $45.4 million. Of this, only $7.5 million was loaned without being associated with other types of financing. The other $37.9 million acted as a supplement to other flows, which included $20 million in export credits. This shows a mixed-credit ratio of about 2/3 aid to 1/3 private credits.

### French Mixed Credits to Algeria (1967-1971)

<table>
<thead>
<tr>
<th>Purpose</th>
<th>Non-Returnable Subsidies (million $)</th>
<th>Loans from CCCE (million $)</th>
<th>Guaranteed Private Export Credit (million $)</th>
<th>Total (million $)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sugar refinery</td>
<td></td>
<td>2.5</td>
<td>2.5</td>
<td>5.0</td>
</tr>
<tr>
<td>Cork factory</td>
<td>12</td>
<td>17</td>
<td>0.4</td>
<td>3.3</td>
</tr>
<tr>
<td>Tourist complex</td>
<td>0.6</td>
<td>25</td>
<td>0.7</td>
<td>6.9</td>
</tr>
<tr>
<td>Tourist complex</td>
<td>0.4</td>
<td>1.4</td>
<td>0.4</td>
<td>2.3</td>
</tr>
<tr>
<td>Truck factory</td>
<td>3.7</td>
<td>19.3</td>
<td>31.0</td>
<td>53.0</td>
</tr>
<tr>
<td>Date factory</td>
<td>4.0</td>
<td>8.0</td>
<td>2.0</td>
<td>14.2</td>
</tr>
<tr>
<td>Natural gas line</td>
<td></td>
<td>3.2</td>
<td>18.0</td>
<td>21.2</td>
</tr>
<tr>
<td>Engineering for gas line</td>
<td>1.4</td>
<td>1.9</td>
<td>3.3</td>
<td></td>
</tr>
<tr>
<td>Olive oil plant</td>
<td>0.3</td>
<td>0.5</td>
<td>0.3</td>
<td>1.0</td>
</tr>
<tr>
<td>Expansion of cork factory</td>
<td></td>
<td>0.2</td>
<td></td>
<td>0.2</td>
</tr>
<tr>
<td>Tile factory</td>
<td>0.5</td>
<td>1.5</td>
<td>0.9</td>
<td>2.9</td>
</tr>
<tr>
<td>Modernization of mineral water</td>
<td>0.5</td>
<td>2.4</td>
<td>0.6</td>
<td>3.5</td>
</tr>
<tr>
<td>bottling plant</td>
<td></td>
<td>11.6</td>
<td>16.3</td>
<td></td>
</tr>
<tr>
<td>Date factory</td>
<td>1.0</td>
<td>15.0</td>
<td>11.7</td>
<td>31.7</td>
</tr>
<tr>
<td>Sugar refinery</td>
<td></td>
<td>0.7</td>
<td>0.5</td>
<td>1.2</td>
</tr>
<tr>
<td>Modernization of a brewery</td>
<td></td>
<td>0.2</td>
<td>0.2</td>
<td>0.4</td>
</tr>
<tr>
<td>Gas liquefaction plant</td>
<td></td>
<td>4.5</td>
<td>9.0</td>
<td>13.5</td>
</tr>
<tr>
<td>Modernization of a dairy</td>
<td>0.3</td>
<td>0.7</td>
<td>1.5</td>
<td></td>
</tr>
<tr>
<td>Liquid gas tanker</td>
<td></td>
<td>3.0</td>
<td>13.5</td>
<td></td>
</tr>
<tr>
<td>Fertilizer plant</td>
<td>2.2</td>
<td>21.9</td>
<td>48.6</td>
<td></td>
</tr>
<tr>
<td>Modernization of fish canner</td>
<td>0.7</td>
<td>3.2</td>
<td>5.8</td>
<td></td>
</tr>
<tr>
<td>Paper cellulose plant</td>
<td>0.5</td>
<td>4.0</td>
<td></td>
<td>11.3</td>
</tr>
<tr>
<td>Expansion of fruit and vegetable canner</td>
<td>0.6</td>
<td>1.4</td>
<td>1.1</td>
<td>3.1</td>
</tr>
</tbody>
</table>

In order to present details on how France mixes its credits, the table contains a listing of all of the foreign aid project
loans to Algeria, administered by CCCE, from 1967 to 1971. It is seen that nearly all of them are mixed. An analysis of the totals shows a mixing of about 47 per cent public and 53 per cent private export credits.

Less information was available as to mixed credits to non-French speaking countries. Government officials made vague references to the well known mixed-credit loans to Mexico for the construction of a subway system, but disclaimed having any general policy.

On the other hand, discussions with the head of the export credit department of a major French merchant bank revealed that if a French company comes to the bank for assistance in export financing and insists that credit terms well below those commercially available are required to win the contract, the banker will go to the DREE (Division de Relations Economiques Extérieures) in the Ministry of Economics and Finance, or to the CCCE, and try to convince them to make a parallel ODA loan. It appears that DREE resists all such requests and a strong case must be made before they agree to help. This ODA portion is often then used to finance the local costs of the project and the down-payment on the imported portion. It appears that the government portion of the mix must now be about 25 to 40 per cent to make the French exporter competitive with British and American exporters (on credit terms), but a 50 to 60 per cent ODA portion is often needed to compete with Japanese terms.

Of final interest is a case study of the French subsidiary of an American engineering-construction firm. This firm was bidding on a large expansion of an oil refinery in Pakistan. It was working with its usual merchant bank. That bank first went to DREE to ask it to approve an 11-year export credit guarantee. DREE gave the green-light to COFACE on such a guarantee. The bank then asked DREE to provide parallel financing out of some ODA credits outstanding to Pakistan. The total cost of the project was $15 million, of which $6 million were local costs. Of the remaining $9 million, the bank obtained a COFACE guarantee and financed $4.5 million (rediscouning some at the BFCE and some at the Bank of France) at 11 years and 6.83 per cent. The DREE arranged for Pakistan to draw on the ODA loan for the other $4.5 million on terms of 22 years and 3.5 per cent interest. The result was a mixed credit with credit terms falling in the grey area.

Grey-Area Export Financing in Japan

In Japan, medium and long-term export credit can be insured by the MFTI (Ministry of International Trade and Industry), but most of this is medium term (under 5 years). A review of the guaranteed private export credits from Japan in 1970 reveals that extremely few were financed at interest rates of less than 5 per cent and that most of those below 6 per cent were also below 10 years. Only two cases fell in the grey area. They were both to Taiwan, one for $7.8 million and the other for $7.6 million, both with maturities of 11 years and interest rates of 5.525 per cent. One was for a steam generator; the other for a turbine generator.

Most of the long-term export credit in the range above 5 years will be financed and guaranteed by the Japanese Export-Import Bank. Its terms are usually between 1 year and 15 years but may go up to 20 years. This bank will usually finance an export credit only in cooperation with a commercial bank, or with a consortium of commercial banks. The Exim Bank will usually assume that the importer has made a 10 per cent downpayment and that there is a 10 per cent profit for the supplier. This leaves 80 per cent of the contract price. The Exim Bank will then finance 80 per cent of this 80 per cent (or 64 per cent of the contract price) leaving a commercial bank to finance the remainder.

The source of the Exim Bank’s funds is 80 per cent from a government Trust Fund Bureau (a Fund in which are kept social security retirement funds) and 20 per cent from the government budget. The Trust Fund Bureau lends money to the Exim Bank at 6.5 per cent. That from the government is free. So, the average cost of money to the Exim Bank is about 5.3 per cent. But it exercises great flexibility in its loans; it charges as much as 7 per cent for some loans, and as little as 4 per cent for others, depending upon the recipient country’s relationship with Japan and its financial condition, as well as the competition for obtaining the contract.

The portion of the credit taken by the commercial banks cost in the neighborhood of 8 to 9 per cent in 1971 and was between 7 and 8 per cent in late 1972. So, the weighted average can be as low as 6.6 per cent, but is usually 5.5 to 6.5 per cent.

The Exim Bank also serves as a channel for foreign aid (ODA) loans. When it acts in this capacity, it may do so with the collabora-
tion of commercial banks, or without them. Also, it exercises
greater flexibility on the interest rate.

The other institution for channeling economic assistance to
the developing countries is the OECF (Overseas Economic
Cooperation Fund). This organization obtains 50 per cent of its funds
from the government budget and 50 per cent from the Trust Fund
Bureau. Hence, the average cost of its money is 3-25%.

The OECF may extend export credit, jointly with commercial
banks (the Fund normally finances 70 per cent of the credits — leaving
30 per cent for the commercial banks) on projects which cannot be
adequately financed by the Exim Bank. In this type of commodity
financing, the net interest rate is typically in the range of 4 per cent.

The OECF also makes direct yen loans to foreign govern-
ments for development projects. In this case no commercial banks
are involved. The terms of these loans now tend to be between
20 and 25 years at interest rates of 3 to 5 per cent.

Administration of foreign aid, in Japan, is characterised by
its ad hoc features and by its complexity. At the top of the
pyramid stands the "Ministerial Meeting on Overseas Coopera-
tion", an ad hoc body comprising cabinet members, which was set
up in May 1969 to formulate basic policies. Then, in October
1970 a "Meeting of Coordination of Economic Cooperation"
was formed; it is comprised of director-generals of the various
Ministries which are members of the above mentioned "Minister-
ial Meeting". The administration of the aid programs is in
the hands of several Ministries (Foreign Affairs, Finance, Interna-
tional Trade, Agriculture and Education) as well as the Economic
Planning Agency and the cabinet itself. Finally, implementation
of the official loans is carried out by the Export-Import Bank,
the OECF (Overseas Economic Cooperation Fund) and the OTCA
(Overseas Technical Co-operative Agency), which implements
technical assistance programs.

When a potential, large export contract arises, the Japanese
supplier typically makes initial contact with officials in MITI to
discuss the matter of a permit to export on extended credit terms
and the question of export credit insurance. At that point officials
in MITI and the Ministry of Finance decide whether the transac-
tion should be financed by the Exim Bank in cooperation with
commercial banks, or by the Exim Bank itself, or whether the
OECF should do the financing, or whether the goods might be
financed out of an existing commodity-type direct yen loan to
the government of the recipient country (if such a loan exists).

It is seen that this system permits a wide degree of flexibility
and results in a confusion between the giving of aid and the
promotion of exports. The officials of MITI of the Ministry of
Finance have a variety of choices each of which permits a
different combination of interest rate and maturity. Their decision
can be influenced by information from the Japanese exporter as
to the competitive situation.

A review of the statistics on the Exim Bank's loans indicates
a rapid increase in the maturities. Between 1969 and 1970,
commitments on maturities in the range of 10 to 15 years more
than doubled, going from $174 million in 1969 to $354 million
in 1970. At the same time, loans with maturities over 15 years
increased from $70 million in 1969 to $69 million in 1970.
However, most of these loans tended, when combined with the
commercial bank portion, to have an effective interest cost of
6 per cent or over.

Japan's ODA loans, as noted earlier, tend to flow either
through the Exim Bank or the OECF, sometimes with and some-
times without parallel financing from commercial banks. In 1970
the Exim Bank served as a channel for nine ODA loans, totalling
$38.1 million, which fell in the grey area. Four of these were
in cooperation with a commercial bank. All of them had interest
rates between 5 and 6 per cent. In addition, the OECF provided
five ODA loans which fell in the grey area. All of these, totalling
$60.3 million, went to Indonesia and had maturities of 19-5 years
with interest rates of 3.5 per cent.

In 1971 Japan considerably expanded her ODA loan program.
Complete information was not available, but that which was
indicated that the maturities of her loans were longer — most of
them at about 20 years, but the interest rates remained in the
range of 3.5 to 5.75 per cent, with a few below and a few above this
range. Some of the loans did fall in the grey area, but detailed
data on them were not available.

The blending and blurring of foreign aid with export credits
and the flexibility of the Exim Bank can best be illustrated by a
case study.
The case of the export of a urea plant to Pakistan

This was a joint project between Mitsubishi and Co. and Toyo Engineering Co. (TEC). To obtain a contract from the Pakistani government, the first thing Mitsubishi did was to insert a condition that this project would be financed by the Yen Loan Program.

The theoretical procedure for use of the Yen Loan Program is that, first, the government of an underdeveloped country applies to the Ministry of Foreign Affairs (MFA) for a yen loan explaining the need for such a loan, and, second, if MFA approves of it, MFA forwards the application to the ORCF for closer feasibility and priority examination, and finally, the Ministry of Finance approves it.

But what in fact often happens is that a private firm prepares the setting for a Yen Loan. The firm negotiates with the government of an underdeveloped country for a contract which includes a clause, subject to confirmation of the Japanese government. When the conditional contract is more or less reached, the firm attempts, with the help of MTTI, to induce the MFA to grant a Yen Loan to the country. The firms that lead in this activity are notably general trading firms and foreign exchange banks.

Mitsubishi obtained the contract of $30 million on the condition that the project would be financed by the 4th, 5th, and 6th Yen Loan Programs. For countries like India and Pakistan the Yen Loan Program is not on a project basis, but on an annual basis, so that several projects could be financed within the Yen Loan Program of any given year. The 4th (1964-65), 5th (1965-66), and 6th (1967-68) programs each provided $30 million at an interest rate of 7.75% (a weighted average rate between the rate of a city bank involved and the Exim Bank's rate) per cent, with repayment terms of 15 to 25 years, and with a grace period of 5 years. The proportion of loan is usually 80 per cent from the Exim Bank and 20 per cent from a city bank. However, in this particular case there was no city bank involved, that is, 100 per cent of the credit was from the Exim Bank at a rate of 4.2 per cent.

So while Mitsubishi were successfully obtaining an informal O.K. from the MFA through MTTI, the Pakistani government filed an application for a loan for the project within the Yen Loan Program(s) with the MFA. The latter approved it and forwarded the application to the Eximbank. Mitsubishi went to the Exim Bank to explain the project in detail. Meanwhile, the Pakistan Industrial Development Corporation (PIDC) explained the project in detail to the Pakistan Industrial Credit & Investment Corporation (PICIC), a development bank. (PIDC was the importer of the urea plant.)

When the government banks of the two countries settled on the terms and conditions of the loan, Mitsubishi was granted an export license from MTTI. The Exim Bank then disclosed a payment plan to Mitsubishi indicating that the Exim Bank would pay for each shipment when the B/L is presented at the Exim Bank by Mitsubishi.

An Analysis of the Availability of Grey-Area Export Financing

A review of the situation in Germany reveals that ODA loans are outside the grey area, and that the cost of guaranteed private export credits is over 6 per cent. Hence, the only evidence of grey-area financing in Germany would be the occasional incidence of a mixed credit. To the extent that the KfW, within the single institution, negotiates and administers Germany's foreign aid program and also provides the financing for export credits with maturities longer than 8 years, it is in a perfect position to provide mixed credits. It appears, however, that the capability is exercised only very sporadically. It exists as a threat to the practice by France, but the infrequency of use makes it negligible as a factor in international export competition.

In the United Kingdom the situation is somewhat analogous. In 1972 and part of 1973 the Bank of England was rediscouraging export credits at a rate of 5.5 per cent. As a result, there were some exports insured by the ECGD, with maturities of greater than 10 years, which fell in the grey area. In 1970 these totalled $452 million, out of approximately $800 million in commercial export credits with maturities greater than 5 years. This was a significant amount. However, in early 1971 the United Kingdom changed its rediscount rate to 6.5 per cent, later to 7.0 per cent, and then to 6.0 per cent, which is its present value. As a result, there is no export credit available in the United Kingdom which falls in the grey area. In addition, all of the United Kingdom's foreign aid is given at terms which are below 3 per cent interest (nearly all of it is at 0 per cent) and above 20 years maturity. Hence, there are now only two possibilities of grey-area financing in the United Kingdom. The first is via mixed credits. The ODA admitted to the occasional occurrence of a mixed-credit transaction, but, as in Germany, the practice is so sporadic (several times per year?) as to not be of significance. The other possibility is that the ECGD has been given authority to subsidize commercial export credit to bring the
effective interest rate down into the grey area. But, funds have not been voted to implement this authority and it has not been used.

The case of Italy is somewhat special. The foreign aid program does provide grants, and these are certainly foreign aid in the pure sense. But all of Italy's ODA loans are really the same as export credits. In fact, the interest rates and maturities are such that they tend to be more expensive than much of the commercial credit from other countries. In 1970 only two ODA loans fell in the grey area—the others had interest rates over 6 per cent. As to guaranteed private exports, Italy does have a system of using government funds to subsidize commercial export credit interest rates, but the limitations on such funds result in most of the interest rates falling above 6 per cent. In 1970 only 4 cases, totalling $37 million, fell in the grey area. Detailed data for 1971 were not available, but expert opinion is that it was analogous to 1970.

In past years, France had a system whereby the Bank of France could rediscuss a large proportion of export credit at a low interest rate, (2, 3, or 4 per cent) and make guaranteed private export credit available at less than 6 per cent. Some of it then fell in the grey area. But since March 1972 the policy has changed and the cost of credit, with part of it rediscounted at the Bank of France, is about 6.83 per cent. Hence, none of it falls in the grey area.

On the other hand, most French ODA loans are given at interest rates between 3 and 6 per cent, and much of it is at maturities less than 20 years. Hence, in 1970, a total of $126 million of ODA loans fell in the grey area. It should be noted, however, that 80 per cent of this went to French territories or to former French colonies.

The interesting factor in France, however, is the practice of mixed credits. It appears that the aid going to French territories and former French colonies is mixed to a very large extent with private credits and that the ratio would be about 60 per cent public aid to 40 per cent commercial credits. In 1971 France gave $278 million in bilateral grants (not including technical assistance or food aid) plus $193 million in ODA loans. Most of the grants go for expenditures which do not lend themselves to mixed credits (budgetary support, agricultural development, assistance to health programs, development of educational systems, etc.). The ODA loans are divided so that about 2/3 of these are administered by the CCCE and go to French territories and former French colonies. This $129 million would presumably be mixed with about $96 million in guaranteed export credits. However, much of this will be machinery for French-owned factories. In addition, even with equal credit facilities, it is difficult for foreign firms to compete in these markets. It is, therefore, the author's evaluation that these mixed credits do not significantly affect exports from the U.S. or the other countries in this study.

This leaves the $64 million in ODA loans which went to non-French-speaking countries in 1971. Here the French government is more circumspect, the mixing is on more of an ad hoc basis, and much of it is not mixed. A fair assumption would be that half of it is mixed and that this is mixed on a 50-50 basis, which would lead to a level of $64 million in mixed, guaranteed private export credit. Given equal credit facilities, United States exporters might expect to obtain their "fair" share of this $64 million.

The situation in Japan has its interesting peculiarities, primarily because of the difficulty in differentiating between export credits and foreign aid. Looking first at guaranteed private export credits, we find that the Japanese Exim Bank is involved in all long-term credits of this type. It generally takes 80 per cent of such credit, leaving commercial banks to take 20 per cent. The Exim Bank has great flexibility on interest rates, varying between 4 and 7 per cent. On strictly commercial transactions it tends to charge somewhat less than 6 per cent. But, when mixed with the commercial bank credit, the weighted average is rarely less than 6 per cent. In 1970 only two transactions (totaling $154 million) fell in the grey area.

However, Japan's ODA loans are channeled through two institutions, the Exim Bank and the OECD, both of which charge interest rates in the range of 3 to 6 per cent. Most of the OECD loans are 20 years or over. But some of them fall in the grey area. More of the ODA loans handled by the Exim Bank fall in the grey area. Also, the Exim Bank frequently collaborates with commercial banks in the financing of ODA loans. Hence, there is frequently a deliberate mixing of public and private credits.

Also, it is clear that Japanese companies can, by petitioning MITI, have a project on which they are bidding become a part...
of Japan's foreign aid program, thus making an ODA loan available after the fact.

To the extent that OECP is lengthening the terms of its credits to beyond 20 years, little of this will fall in the grey area. This is also happening to ODA loans from the Exim Bank.

Thus, the existence of grey-area financing is disappearing in Japan. The major factor affecting international competition is the flexibility with which the aid program is operated, making it largely responsive to the competitive needs of Japanese exporters.

This is a result of the Japanese organization for foreign aid. They do not maintain large staffs in the developing countries to study needs in advance. Loans are negotiated to cover future Japanese exports to that country and it is left to Japanese private enterprise to discover projects on which these loans can be spent, or for which loans should be made.

In summary, the existence of grey area export financing and of mixed-credit practices in Germany, the United Kingdom and Italy is negligible. In France, much of the ODA loans fall in the grey area, but this does not relate to United States exports. If these loans were softer, so as to drop out of the grey area, they would result in even greater exclusion of United States exports.

France has an extensive system of mixed credits, but the results of this study make it appear that United States and other exporters may lose a total of between $50 million and $60 million in exports because of this practice. Finally, in Japan many of the ODA loans have, in the past, fallen in the grey area, but the maturities are lengthening and in 1972 very few were in the grey area. There will, however, continue to be a confusion between foreign aid loans and the financing of Japanese exports.

Lee C. Nebert

---

**BANCA NAZIONALE DEL LAVORO**

**HEAD OFFICE: ROME**

**VIA VITTORIO VENETO, 199**

**ANTONINO DONATI** - Chairman

**ALBERTO FERRARI** - Managing Director

**GUIDO PICCOLO** - Deputy Managing Director

**GIOVANNI VICINELLI** - Central Manager (Foreign Dept.)

**GIOVANNI NINNI** - Central Manager

**PIRASANTI PANTIZZI** - Central Manager

**PAOLO LARIATTA** - Central Manager

**FEDERICO FANICO** - Central Manager

---

**Condensed Statement of Condition of the Bank and its Special Credit Sections, December 31, 1973**

<table>
<thead>
<tr>
<th>ASSETS</th>
<th>Bank</th>
<th>Special Sections</th>
<th>B.N.L. Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(in thousands of U.S. dollars)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and due from Banks</td>
<td>3,590,953</td>
<td>—</td>
<td>3,590,953</td>
</tr>
<tr>
<td>Treasury Bills and other Securities</td>
<td>3,717,780</td>
<td>59,353</td>
<td>3,777,133</td>
</tr>
<tr>
<td>Loans, Discounts and Correspondents</td>
<td>11,373,800</td>
<td>323,870</td>
<td>11,697,670</td>
</tr>
<tr>
<td>Mortgage Loans</td>
<td>1,713,190</td>
<td>1,713,190</td>
<td></td>
</tr>
<tr>
<td>Current Accounts between Bank and Customers</td>
<td>3,416,441</td>
<td>3,416,441</td>
<td></td>
</tr>
<tr>
<td>Bills for Collection</td>
<td>428,947</td>
<td>428,947</td>
<td></td>
</tr>
<tr>
<td>Other Assets</td>
<td>332,773</td>
<td>78,695</td>
<td>411,468</td>
</tr>
<tr>
<td>Due by Capital Subscribers</td>
<td>6,541</td>
<td>6,541</td>
<td></td>
</tr>
<tr>
<td>Investments in Subsidiaries and Affiliates</td>
<td>60,954</td>
<td>60,954</td>
<td></td>
</tr>
<tr>
<td>Premises, Equipment, etc.</td>
<td>58,535</td>
<td>58,535</td>
<td></td>
</tr>
<tr>
<td>Deposits</td>
<td>18,941,838</td>
<td>—</td>
<td>18,941,838</td>
</tr>
<tr>
<td>Current Liabilities for Guarantees, Acceptances, etc.</td>
<td>7,171,752</td>
<td>6,648</td>
<td>7,178,400</td>
</tr>
<tr>
<td>Deposits for Forward Foreign Exchange Transactions</td>
<td>3,325,573</td>
<td>—</td>
<td>3,325,573</td>
</tr>
<tr>
<td>Deposits for Forward Foreign Exchange bought</td>
<td>3,100,000</td>
<td>—</td>
<td>3,100,000</td>
</tr>
<tr>
<td>Deposits on Deposits</td>
<td>2,455,751</td>
<td>285,292</td>
<td>2,741,043</td>
</tr>
<tr>
<td>Deposits with Third Parties</td>
<td>3,325,573</td>
<td>121,415</td>
<td>3,446,988</td>
</tr>
<tr>
<td>Total</td>
<td>32,202,627</td>
<td>4,312,149</td>
<td>36,514,776</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>LIABILITIES</th>
<th>Bank</th>
<th>Special Sections</th>
<th>B.N.L. Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital and Reserve Funds</td>
<td>8,787,436</td>
<td>777,436</td>
<td>9,564,872</td>
</tr>
<tr>
<td>Reserves and Special Funds</td>
<td>77,436</td>
<td>174,302</td>
<td>251,738</td>
</tr>
<tr>
<td>Abnominations of Investments, Premises, etc.</td>
<td>96,694</td>
<td>12,974</td>
<td>109,668</td>
</tr>
<tr>
<td>Staff Benevolent Fund (Bank and Sections)</td>
<td>165,074</td>
<td>165,074</td>
<td></td>
</tr>
<tr>
<td>Deposits, Current Accounts and Correspondents, banker's cheques in circulation</td>
<td>16,806,553</td>
<td>143,571</td>
<td>16,949,124</td>
</tr>
<tr>
<td>Special Accounts and Deposits, Bearer in circulation, etc.</td>
<td>29,041,813</td>
<td>29,041,813</td>
<td></td>
</tr>
<tr>
<td>Current Accounts between Bank and Customers</td>
<td>178,065</td>
<td>121,815</td>
<td>299,880</td>
</tr>
<tr>
<td>Refunds</td>
<td>196,455</td>
<td>196,455</td>
<td></td>
</tr>
<tr>
<td>Bills for Collection</td>
<td>6,541</td>
<td>6,541</td>
<td></td>
</tr>
<tr>
<td>Miscellaneous Accounts, Unearned Interest, Discounts, etc.</td>
<td>6,541</td>
<td>6,541</td>
<td></td>
</tr>
<tr>
<td>Net Profits</td>
<td>4,000</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>2,736,436</td>
<td>2,736,436</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Guarantees, Acceptances, Confirmed Letters of Credit, etc.</td>
<td>6,541,813</td>
<td>5,624</td>
<td>6,547,437</td>
</tr>
<tr>
<td>Deposits of Securities sold</td>
<td>3,325,573</td>
<td>—</td>
<td>3,325,573</td>
</tr>
<tr>
<td>Total</td>
<td>6,541,813</td>
<td>5,624</td>
<td>6,547,437</td>
</tr>
<tr>
<td>Total Capital Funds after Approval of the Balance Sheet and Allocations to Reserves</td>
<td>32,202,627</td>
<td>4,312,149</td>
<td>36,514,776</td>
</tr>
</tbody>
</table>