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Export Credit Insurance: Business as Usual or a New Approach?

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The answer to the question posed above in this chapter's title is clear and simple: Business as usual will never be enough if the US Export-Import Bank, or any other export credit agency (ECA), wishes to remain successful. Let me first say a few words about business as usual. For more than 50 years, the insurance business of the export credit agencies of the major industrial countries has been guided by three parameters:

- Insurance is desired to protect exporters against international risks that they are not in a position to quantify. Export credit insurance compensates for foreign trade risk, primarily covering politically related risks that are not covered by the risk provisions of the private entrepreneur or the banks. Small and medium-sized enterprises are particularly affected by these risks. A logical consequence is that, in major exporting countries such as Germany and the United States, 85 percent of insurance policies are for small and medium-sized enterprises.
- Government export credit insurance is a complementary instrument that does not compete with the private insurance market and always takes a back seat when the market provides adequate insurance. This is documented most clearly by the fact that government-insured export business tends to account for a shrinking share of total exports in the major exporting countries. In Germany, recent figures show that this share amounts to only about 3 percent. The downward trend may have further to go.

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- Export credit must be seen as promoting foreign trade rather than as an export subsidy. In the long term, therefore, all government-supported export credit systems must operate in the black, or at least break even. Export credit supports products and exporters in their competition for markets. Export credit is not a system in which the finance ministers and taxpayers of the export nations compete with each other.

These parameters will continue to guide the business of the export credit agencies that receive government support. In the twenty-first century, the operations of the government export credit agencies will therefore continue to be based, to a large extent, on the principle of business as usual.

Challenges to Construct a New Approach

Export credit agencies operate, however, in a constantly changing environment. They must demonstrate adaptability, dynamism, and professionalism to survive. In the years ahead, I foresee several major challenges that export credit agencies will have to meet.

Challenge 1: Erosion of the traditional division between domestic and international policy concerns. The defining feature of the world economy today is the increasing integration of national economies. This process erodes the possibility for national policymakers to make autonomous, unilateral decisions. Politicians in some countries find it difficult to accept this aspect of worldwide integration and interdependence.

Challenge 2: Impact of the globalization of business operations on effective market access and its meaning for the multilateral trading system. Export credit subsidies can be just as protectionist and damaging as tariffs. The OECD Arrangement on Guidelines for Officially Supported Export Credits accordingly plays a vital role in the evolution of the multilateral trading system. Just as the rules of the World Trade Organization (WTO) reject protectionism and unfair competition for export markets, so the Arrangement rejects the use of export credit subsidies. Indeed, the Arrangement and the negotiating techniques that led to its adoption provide an effective model for how to roll back the remaining distortions.

The Arrangement provides a framework for the orderly use of export credits. This helps to ensure that exporters compete on the basis of quality and price rather than of the financial support they receive from their governments. It ensures that official export support reflects market practice, that it accounts for the risks inherent in business, that it is undertaken on a sound financial basis without subsidy, and that it conforms to the WTO Agreement on Subsidies and Countervailing Measures.

Challenge 3: Anachronistic practices that still prevail in national export credit *policy.* We have to generalize the successes achieved in the battle against subsidized export credit insurance. These practices hurt firms and workers that they are supposed to help. Let me explain.

Under the current state of globalization, few exporters offer a purely national product. Instead, as a general rule, the exported product contains components from several countries. Particularly in the case of large-scale projects, multisourcing is a key requirement for competitive supply. It is obvious that national taxpayers cannot be expected to cover risks in order to create jobs and generate profits outside their own country. Most export credit schemes have, therefore, narrowly limited the scope of credit insurance for foreign inputs.

Conversely, it is quite clear that an exporter that procures components on a global basis is not interested in negotiating with a half-dozen export credit insurance agencies. The solution for the future must be that export credit insurance agencies take out reinsurance on as broad a basis as possible. This would allow the exporter to obtain export credit insurance from a single source, even for products with a high proportion of foreign content.

In the European Union, the German export credit insurance agency Hermes Kreditversicherungs has already entered into reinsurance agreements with Austria, Denmark, Finland, France, Spain, Sweden, and the United Kingdom. Treaties with Belgium, Italy, the Netherlands, and Switzerland are in preparation. Discussions are being held with Canada, the Czech Republic, and Poland. I believe it is absolutely essential to extend this system of reinsurance treaties beyond the European Union, and above all to include the United States. Government export credit schemes will otherwise no longer meet the needs of dynamic, globally operating companies—whether they be small enterprises or large corporations. The existing cooperation between Ex-Im Bank and Hermes on project financing arrangements and other transactions provides an encouraging basis for the discussion of a reinsurance treaty.

All forms of cooperation, and especially reinsurance agreements, will have an important side effect: They will reinforce what I like to call the worldwide solidarity of export financing experts. This will further contribute to transparency, which is one of the most effective instruments against unfair competition.

Challenge 4: Insurance of private-sector risks. In the past, government export credit agencies primarily insured the risks of public-sector buyers. In the course of the worldwide privatization of public services and utilities, the insurance of private-sector commercial risks is becoming more and more important. Government export credit agencies must increasingly devote resources to the analysis of private business and project risks. This means that they will have to become more professional. Tough questions about the ability of government agencies and their employees to achieve this increased professionalism must be faced.

I am convinced that the best approach is to outsource government-backed export credit insurance to an experienced private credit insurer. This gives governments access to the professional skills and experience of private insurance companies. During the past 50 years, Germany has had excellent experience outsourcing to Hermes, a privately owned company that does more than 90 percent of its business for its own account in national and international credit insurance markets. The same applies in France and the Netherlands.

Challenge 5: The currently popular subject of "market windows." On this topic, there are misunderstandings and unnecessary polemics. It is my impression that much of the criticism against market windows is based on assumptions rather than hard facts. What it boils down to is that certain banks—including Kreditanstalt für Wiederaufbau (KfW) in Germany—are providing financing in individual cases for promising projects at their own risk after careful examination. These funds are refinanced in the capital market and provided on market terms. Market windows enable banks and exporters to cooperate on medium- and long-term loans. They are not a subsidy instrument. Market windows require a high level of banking professionalism. That professionalism is what makes market windows attractive and competitive, not any hidden subsidy.

KfW in Germany and also, as far as I know, the Export Development Corporation in Canada are prepared to talk about the transparency of market window operations. In my view, discussion and transparency are essential to ensure that the legitimate use of market windows is not tarnished by the unjustified accusation of unfair competition.

Challenge 6: Decrease in the share of total credit insurance supported by governments. As global integration and the interdependence of national economies increase, the proportion of government-backed export credit will decrease. In short-term business, privatization is already well advanced, and competition with the private insurance industry is increasing. This inevitably spells reduced returns for the government agencies and a concentration of higher-risk business in the government systems. The contraction process will make it more difficult for government agencies to meet the increasingly complex demands of risk assessment, project financing, reinsurance questions, and international cooperation. This trend gives cause for urgently considering the outsourcing of government export credit insurance in countries where this has not yet taken place.

It is essential to respect the well-tried principles of export credit insurance. But business as usual would take us down a blind alley and fail to address the needs of exporters operating in the global world of the twenty-first century. In the years ahead, an open mind in response to new challenges will be required. ECAs that do not accommodate inputs procured beyond their own national boundaries will no longer meet the requirements of the market and exporters. Flexibility points to several recipes to meet the challenges for the future.

A New Approach

In facing these six challenges, four areas for a new approach emerge:

- *Continued OECD cooperation leading to "soft law with hard results."* In the OECD, a high level of collegial frankness has developed between the representatives of the national export credit agencies. This must be maintained and strengthened. Meanwhile, the OECD Arrangement must be revised in line with new developments in export finance techniques.
- *Further development of ECA reinsurance.* The network of reinsurance agreements must be extended. Otherwise, the ECA race to meet the requirements of globalization will be lost.
- *Government outsourcing of export credit insurance.* This is an increasingly urgent subject. Government authorities will encounter serious difficulties in providing the facilities and human resources that are required to run a competitive export credit insurance service in the twenty-first century. The privatization of short-term insurance in Europe is an important step forward. Signs are evident that private-sector competition may soon increase in the medium-term insurance business.
- *Facing the demands of "civil society" in the areas of environment protection and employment standards.* Export credit agencies will have a difficult task responding to the justified elements in the civil society agenda, without forsaking the principles of economic reason and equality of competition. In this area, it will not be possible, for the foreseeable future, to formulate common standards for all export credit agencies. It is essential, however, that the subjects proposed around the world by nongovernmental organizations be included in the dialogue and appropriate agreements reached with ECAs.

Conclusions

In recent years, the business-as-usual philosophy of the export credit agencies has already begun to include a flexible, pragmatic approach to the constantly changing environment. The ECAs are therefore well prepared to meet new challenges with new approaches. In our global economy, this process must entail cooperation and agreement. It would be tragic if institutional egoism or shortsighted nationalism thwarted the process of worldwide cooperation. Those responsible for export financing in government have a major responsibility to avoid conflicts, to provide transparency, and to enhance cooperation. Only in this way will they be able to meet the demands of global players for competitive export finance—bearing in mind that small and medium-sized enterprises are becoming global players.

Unilateralism and the extraterritorial application of national rules and principles will surely generate conflict and destructive competition. Conversely, the worldwide solidarity of experts and professionals will prove to be the major engine of convergence. Let us work to ensure that national politicians continue to tolerate this process of convergence and collective international rule making, even though to some extent it erodes autonomous national decision making. Let it flourish, even though the international rule-making process is not explicitly anticipated in any nation's constitution. This process of collective rule making provides solid ground for fair competition and a level playing field.