

Chapter 3: Core Business Policies and Practices

Section A: Cover Policy and Risk-Taking

Introduction

Cover policy refers to an ECA's willingness to provide protection against commercial and political risks in a particular market. ECAs' cover policies and risk-taking practices significantly impact an exporter's ability to effectively compete for sales. Cover policy decisions are based on an ECA's underwriting approach and its consideration of whether and how to place limits, in terms of risk type or volume, on the business it can support. Limits on transaction size, repayment terms or total commitments per country are the methods many ECAs use to control the flow of new business.

An ECA's approach to non-sovereign risk is another important aspect of cover policy. Exporters whose ECA is willing to take on new business with entities other than sovereign governments or first class private institutions can enter markets and gain competitive advantages over foreign competitors. While most ECAs have historically covered sovereign, public and major bank business, increasing privatization in the developing world has presented ECAs with increasing requests to cover private risks, ranging from large corporations to small businesses. The scope and depth of an ECA's willingness to cover private sector risk, especially of small private entities, has become a more critical competitive aspect of an ECA's cover policy.

Ex-Im Bank's Policy and Practice

Ex-Im Bank will typically support transactions without size or country limits as long as there is a reasonable assurance of repayment in each transaction as required by the Bank's Charter. One exception is when Ex-Im Bank is statutorily prohibited from doing business in a particular market, generally as a result of sanctions. The goal for Ex-Im Bank is to provide financing for creditworthy export transactions, regardless of destination, when there is foreign ECA-supported competition or when private sector financing is unavailable. In other words, restrictions on the provision of Ex-Im Bank cover in a given market pertain to the creditworthiness of a transaction, as opposed to portfolio controls. Consequently, U.S. exporters and lenders enjoy a competitive benefit from the absence of country and sector ceilings on Ex-Im Bank's cover policy. When Ex-Im is open in a market for a given term, it is generally less risk averse than other ECAs. Ex-Im Bank shows a willingness to cover the risk of smaller, private entities and seeks to minimize the requirement for bank guarantees and other forms of security in order to reduce the associated costs of these guarantees to U.S. exporters.

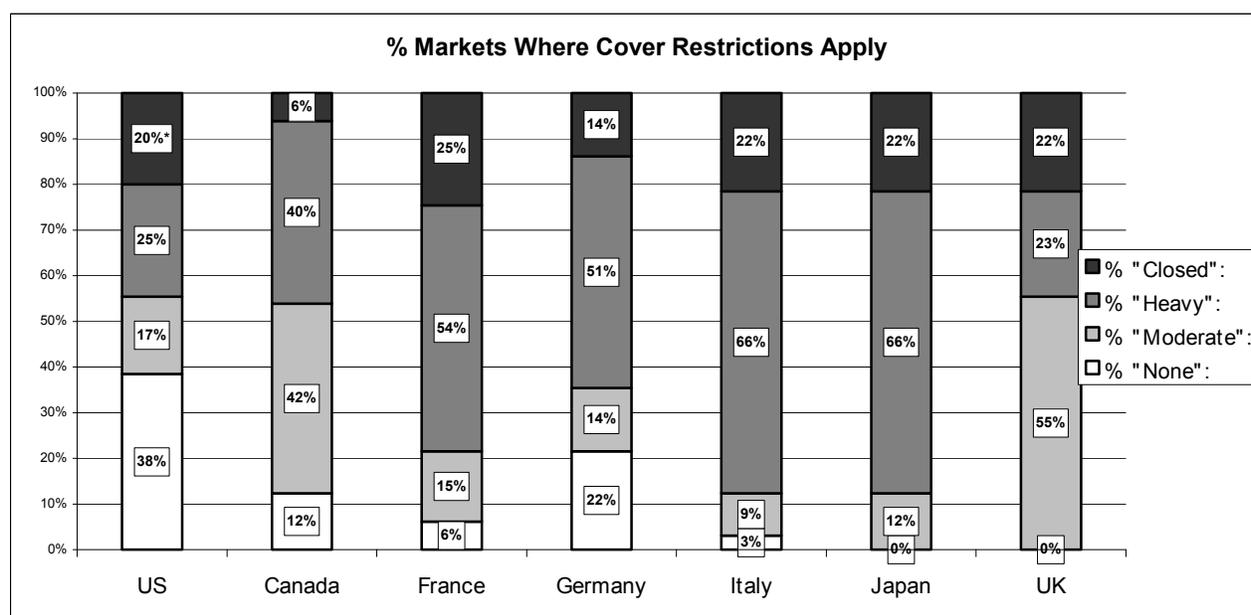
G-7 ECAs' Policies and Practices

Ex-Im Bank and the other G-7 ECAs are equally willing to take on sovereign government risk; however, with respect to private sector transactions, the other ECAs tend to be more risk averse than Ex-Im Bank. They control their risk appetite for private sector business by, for example, imposing country and/or sector exposure limits. In addition, they prefer to focus on

well-known or rated entities (which are usually banks) or rely (by requiring risk-sharing of 5%-20%) on the due diligence and underwriting approaches of the banks they cover. As privatization continues in the emerging markets, the other G-7 ECAs are facing new challenges with underwriting private sector risk – an undertaking with which most have limited experience. Within this context, the other G-7 ECAs do appear to be searching for ways in which they can be competitive while also minimizing the increased risk.

Summary Data

Figure 3: Comparison of Medium- and Long-Term ECA Country Cover Policy



*In 5% of the 65 markets, Ex-Im Bank was closed due to legislative sanctions.

Figure 3 shows the overall openness of the G-7 ECAs by comparing cover policy in 2003 for a sample of 65 major ECA markets. As illustrated, there is a difference in approach to overall cover policy and the degree to which ECAs are willing to assume unsecured risks. Specifically, Ex-Im Bank is open without restriction in more markets than any of the other G-7 ECAs. Further, relative to its major competitors, Ex-Im Bank generally imposes far fewer restrictions on the provision of cover than other ECAs. Ex-Im Bank is off cover in 20% of the 65 markets; however, Ex-Im Bank was closed for business in 5% of the sample markets due to legislative reasons.

With respect to ECAs' risk-taking practices, **Figure 4** provides a broad characterization of the G-7 ECAs' risk appetite for business with less well-known private entities, as opposed to large corporations or bank guaranteed borrowers.

Figure 4: ECA Risk-Taking Practices

Taking Credit Risk of Smaller, Less Well-Known Private Entities in a Market:				
Never----->		Infrequent----->		Frequent
JBIC and NEXI	ECGD	Coface Hermes Sace	EDC	Ex-Im Bank

Most G-7 ECAs continue to prefer financing well-known or rated entities or rely on risk-sharing to minimize exposure to smaller, private entities. Ex-Im Bank is more comfortable than competitor ECAs taking the risk of smaller, less well-known private entities and does not follow other ECAs in their risk-sharing practices.

Exporter and Lender Survey Results

Due to legislative prohibitions, some respondents cited lost export opportunities in Iran and Libya in the oil and gas sector. On the other hand, most respondents graded Ex-Im Bank's cover policy and risk-taking practices highly, with one noting that "Ex-Im Bank's cover policy is competitive for most of our business development opportunities." On balance, the exporting community seems to believe that Ex-Im Bank is generally competitive, largely due to its relatively greater risk appetite vis-à-vis its foreign counterparts.

Conclusion

In 2003, Ex-Im Bank remained generally competitive in its approach to cover policy and risk taking. Once Ex-Im Bank is open in a market for a given repayment term, U.S. exporters and banks benefit from a lack of country and sector ceilings, such as those used by other ECAs. Additionally, Ex-Im Bank is less risk averse in its willingness to extend credit to smaller private entities, although the other G-7 ECAs seem to be gaining more experience in this area.

