FINANCE FOR EXPORTS

An article in the June 1961 issue of this Bulletin outlined a number of developments which had taken place in the field of export financing and export credit insurance during the preceding months. The two main developments described were:

1. The scheme under which the Bank of England stand ready to re-finance that part of the finance provided by participating banks, in respect of export credit for periods in excess of three years and covered by an appropriate guarantee of the Export Credits Guarantee Department, which is due to be repaid by the buyer within eighteen months of the date of the re-financing.

2. The issue by E.C.G.D. of financial guarantees for very large capital projects and for ocean-going ships, where there is justification for extending to buyers credit beyond the term of five years from delivery normally covered by E.C.G.D.

Though it was recognised that it was too early to assess how successfully these arrangements would meet the varied needs of exporters, the view was expressed that they should go a long way towards putting the U.K. exporter as nearly as possible on a comparable footing with his rivals overseas.

Since that time, however, criticisms have continued to be made about the arrangements for the financing of medium-term export credits. In particular these criticisms have been:

(*a*) that interest rates in the United Kingdom have been higher than those offered by competitors in other industrial countries, often because of the existence in those countries of some special financing institution or of some other arrangement for producing favourable rates;

(*b*) that foreign buyers were chary of committing themselves to paying a rate of interest which fluctuated with Bank Rate in this country, but that this was the only basis on which the U.K. banks were prepared to provide medium-term export credit;

(*c*) that although creditworthy exporters had no undue difficulty in obtaining from the banks finance for terms up to five years post shipment, it was difficult to find lenders for terms rather longer than this, since the insurance companies, the natural source to which to look, were generally anxious to place their funds for a substantially longer term.

Strength was added to these criticisms by the increase in Bank Rate to 7% in July last year; and exporters pressed for arrangements which would mitigate the effect of this increase.

The official subsidising of interest rates on export credits would have been inconsistent with the declared policy of H.M. Government, who have played a prominent part in promoting international agreement to refrain from subsidising exports. Moreover, it was reasonable to suppose that any move in the direction of such a subsidy would provoke retaliatory action in competitor countries. Any arrangement of this kind was therefore ruled out. The idea of creating a special official institution for the purpose of providing export finance was also rejected. Of itself the creation of a new institution does nothing to provide additional funds. If the institution draws its finance from market sources, it is unlikely to be able to offer lower rates than those at which finance is already available in the market, though it might be able to offer fixed rather than fluctuating rates of interest. If it draws its funds from government sources, the magnitude of its demand greatly aggravates the problems of government finance. It was therefore concluded that attention should be concentrated on the possibility of providing money on more attractive terms through the existing machinery.

The greater part of the finance for medium-term export credit in this country has come to be provided by the main joint stock banks, which have shown gradually increased readiness to accept financing commitments running up to terms of five years post shipment. The banks have, however, been reluctant, save in very exceptional circumstances, to lend at fixed rates of interest. For the interest they pay to their depositors changes with Bank Rate and they are therefore concerned to protect themselves, so far as possible, by lending at rates linked with Bank Rate. In view, however, of the great importance with which the provision of finance at fixed rates for medium-term export credits was officially regarded, the London clearing banks and the Scottish banks agreed to supply medium-term finance for the export of heavy capital equipment at a fixed rate which, for an initial period of five years, was set at 5½%. Previously, their normal lending rate for such transactions was 1% above Bank Rate, minimum 5%. With Bank Rate standing at 6% at the time, this meant an effective lending rate of 7%.

In order to improve the provision of export credit in excess of the five years post shipment which the banks were generally prepared to cover, a parallel approach was made to a number of leading insurance companies, members of the British Insurance Association, to make funds available for longer terms at a fixed rate of interest substantially lower than that then ruling. As in the case of bank finance, this rate would not be changed during an initial period of five years. Agreement was reached for a group of some fifty companies to provide a sum of up to £100 million at a rate of interest of 6½%; the rate previously applied to such loans was 7½%.

It is a condition of loans or advances under this scheme that, in respect of the underlying commercial transaction, E.C.G.D. should have issued either a direct guarantee to the banker concerned or, for longer-term contracts, a financial guarantee under the arrangements introduced in April 1961. Since direct bankers' guarantees are issued by E.C.G.D. only in cases where the amount involved in the contract is £100,000 or more and the length of credit given is three years or more, the arrangements are effectively limited to transactions which meet these criteria. Advances by the banks under these new arrangements will be eligible for re-financing under the Bank of England's scheme.

Insurance companies participating in the scheme intend to establish a new company to administer their side of it. This should facilitate the negotiation of export contracts, as the company will be able to give approval of all the terms and conditions for the financing of the contract on behalf of all the member companies involved. Pending its establishment, an Insurance Export Finance Committee will deal with applications, which will be made through the exporter's banker.

Among the banks, the London clearing banks and the Scottish banks have so far agreed to participate in the scheme. It is hoped that some of the other banks and also a number of pension funds will be prepared to take part.

These arrangements were announced by the banks and insurance companies concerned, and were also the subject of a statement by the Chancellor of the Exchequer in the House of Commons, on the 23rd January. They appear to meet fully the three criticisms mentioned above and have the advantage that they bring the minimum of disturbance to normal financing channels.