FINANCING CAPITAL EQUIPMENT EXPORTS
THROUGH THE EXPORT DEVELOPMENT CORPORATION

by

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We accept this thesis as conforming to the
required standard.

THE UNIVERSITY OF BRITISH COLUMBIA
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April 30, 1976.
ABSTRACT

The objective of this thesis is to evaluate the effectiveness of the Export Development Corporation, Canada's national export credit granting agency, in promoting and financing trade in capital equipment. This objective can be divided into four tasks, an examination of the Corporation's activities in the field of export credit, an examination of the markets of the purchasers of Canadian capital equipment exports, the development of some international standards against which to measure the performance of the EDC and an assessment of the performance of the Corporation in facilitating and developing trade in capital goods.

In Chapter I the importance of capital equipment exports to the world's economy is examined. The evolution and importance of credit in facilitating trade in capital equipment is outlined. The analysis in the chapter shows that there are no effective international agreements to control the field of export credit. This introductory chapter also concerns itself with examining the role of export credit insurance. The balance of the study concentrates on examining the field of export credit in three nations.

Chapter II is concerned with examining the system used by the British government to promote and finance British capital equipment exports. The purpose of this review is to develop some basic measures against which the performance of the EDC can be measured.

Chapter III examines the programs used by the Export-Import Bank of the United States to promote and finance American capital
equipment exports. The chapter also examines the structure of the market for such exports. The analysis is used to determine if the exports being supported by Exim Bank's finance facility have the same basic trade pattern as total American exports. A review of the World Bank's activities in the field of development finance is presented in order to establish that certain types of export credit are really nothing more than a sub-set of development finance. The commodities being supported by the Exim Bank's financing are analyzed to determine if a comparative advantage type of theory can be applied to the products supported by export credit. The Exim Bank's operations also provide a standard against which to measure the EDC's activities.

Chapter IV outlines and analyzes the financing activities of the Export Development Corporation. The analysis includes all phases of the finance facility—the type of product eligible for support, the dollar volume of eligible goods being supported, the importance of the financed goods to the Canadian economy, the structure of the Canadian exporters and the structure of the foreign market. The chapter also attempts to relate the comparative advantage theories of international trade to this specific part of the Canadian manufacturing sector.

Chapter V concerns itself with analyzing how the Corporation is financing its levels of activity. The Corporation's cash flows resulting from its financing activity are analyzed. The study suggests that the Corporation will require substantial amounts of capital in the near future. A new method of financing the activity of the EDC is also presented in this chapter.

Chapter VI is the concluding chapter to this study.
It initially outlines the similarities and differences of the systems used by the three nations to promote exports of capital equipment. The chapter then focuses on determining how effective the mechanisms used by each of the three countries are in achieving their government's policy goal. This comparison shows that the EDC is by far the least effective of the three agencies in achieving its policy goals.

The study also demonstrates that both Canada and the U.S.A. use export credit to support certain industrial sectors. In the American case the aircraft industry receives a great deal of support from the Exim Bank's financing activity. This fact is also true for Canada's ship building industry.

The study then offers a series of recommendations to improve the facilities offered by Canada in support of exports of capital equipment. It is suggested that export credit facilities in Canada can be made more efficient through the introduction of these new measures.
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I. INTRODUCTION

In the thirty year period since the end of World War II world trade has increased dramatically to a level exceeding $U.S. 778 billion in the year ended December 31, 1974. In the 1970's alone, world trade has nearly tripled from the $U.S.282.1 billion recorded in 1970.

Measured in real terms, world trade has also increased at an above average rate. In the first four years of the troubled seventies world trade recorded an annual compound growth rate of 9%.

While this dramatic increase in trade has been well documented in the literature, little has been written about how the purchases resulting from this trade are paid for. The purchaser of imported goods can pay for his purchase by any one of three methods—he may be sufficiently liquid to pay cash, he may arrange short term credit with a local financial institution or he may arrange long term financing provided by special types of financial institutions. The financing term accorded various types of assets is generally regarded as uniform throughout the world. In the case of consumer durables or agricultural commodities short term credit is usually arranged because of the nature of the transaction. However, in the case of capital goods, the purchaser usually tries to match the
expected economic life of the asset with a debt of a similar term i.e. the funds raised by issuing long term debt will be used to purchase long lived assets. A substantial part of world trade consists of capital goods and services. For example, in 1973, $143.9 billion or 27.4% of total world exports consisted of machinery and transportation equipment. The sale of such capital goods in turn requires that some type of long term financing be provided for the purchaser.

The concept of credit in export trade is relatively new. Capital goods purchasers in industrialized countries have access to relatively efficient capital markets and have little difficulty arranging long term credit. However, the situation facing the purchaser in the less developed nations (LDCs) of the world is somewhat different. On one hand capital goods are sought to speed up the rate of development while on the other hand, they do not have access to the funds needed to pay for such assets.

Prior to World War II most of the LDCs were closely tied to colonial centers and were required to maintain a 100% reserve requirement. The LDCs obtained the necessary funds to pay for capital equipment purchases either by way of direct grants from their colonial parent or by issuing securities in one of the international capital markets. The London market was often used for this purpose. Since the mid-1940's the LDCs have had limited access to these capital markets because of the large number of defaults, balance of payments difficulties, and currency inconvertibility. In addition, the investing public has only had a relatively short period in which to evaluate the credit-worthiness of the newly emerging nation states.
Capital equipment exports are important to both exporters and importers. For the LDCs capital equipment is the key to industrialization, while for the developed nations the exports are necessary to maintain their position in the world economy. In the late 1940's credit was not a big factor in the sale of capital goods because the European nations and Japan were busy rebuilding their industrial sectors. As early as 1955, however, the factors affecting the export markets began to change as the industrialized states realized that the successful nations and the successful companies would be those that expanded their trade and investment activities beyond the borders of their own countries.

Traditionally, the private sector has provided the funds needed to finance world trade. Commercial banks throughout the world have served as both a source and a channel for the financing of international trade. The banks provide the foreign exchange, handle the documents, provide the credit and transfer the funds required to facilitate trade transactions. Banks have always concerned themselves with trade and payments and the extension of these activities into the international market place was a logical step. However, banks have traditionally viewed their role as one of providing short term credit only. The nature of their liabilities, i.e. time and demand deposits requires that they have a relatively liquid asset portfolio. Hence, they have been reluctant to grant intermediate term credit.

After World War II most exports of capital goods were financed through the use of bilateral payment agreements. Such agreements usually specified a 1-3 year maximum repayment period. Such loans could, of course, be provided by the commercial banks. This short repayment period did not match the general theory of finance, in that the cost of the
assets was not being apportioned over its economic life. As a result, debtors soon found themselves unable to meet the repayment schedule and the creditors, in order to maintain a normal flow of exports, were forced to negotiate rescheduling agreements. In effect, nominal short term credit evolved into de facto medium term credit. With the world banking system reluctant to provide such medium term credit, the governments of the industrialized countries began to create new agencies or redesigned existing agencies to provide the much needed export credit. All of these national export credit granting institutions have similar objectives including:

1) the promotion of exports from their relative countries. The agencies view their role as being one of supporting normal commercial activities. They are not overly concerned with the problem of development finance. Efforts to develop the industrial sector of the LDCs are of secondary importance to the export granting institutions

2) the insulation of the cost of export finance from changing domestic credit conditions

3) the implementation of more flexible terms in order that commercial transactions may compete against tied aid transactions.

The development of credit granting agencies in meeting the changing needs of the exporters has taken different forms in various countries and is dependent upon:

1) the structure of the financial system
2) the nature of existing institutional arrangements
3) the state of development of the insurance industry.
The United States of America has moved from specialized institutional financing of exports towards insurance, which is provided jointly by the Foreign Credit Insurance Association and the Export Import Bank, while other nations such as the United Kingdom and Canada have moved from heavy reliance on the insurance mechanism to the activation of specialized arrangements for export credit. The system of financing exports in the United Kingdom, with the exception of the rediscount facility, does not make use of any public funds. The American system involves direct and indirect loans being made to the importer by the Export Import Bank (Exim Bank). Under the former plan, the funds are advanced directly by the Exim Bank, while under the latter plan known as participation financing, some of the funds are provided by a financial institution such as a commercial bank. The Canadian Export Development Corporation (EDC) has, until recently, relied almost exclusively on providing direct loans to the foreign purchasers of Canadian capital goods.

The principal characteristic of all such credit granting institutions is that they are structured to be marginally profitable. They more than cover all of their direct costs by charging a sufficiently high rate of interest on their loans to pay for their administrative expenses, to pay for the cost of borrowing the needed capital and to accumulate a reasonable amount of reserves. The costs of borrowing include an annual dividend to the firm's stockholders as well as interest on any outstanding debt. The Exim Bank, for example, in the fiscal year ended June 30, 1975, recorded a net income of $80.5 million of which $20 million was transferred to the U. S. Treasury as a dividend and the balance of $60.5 million was added to the reserve account. On June 30, 1975, this reserve account had
a balance of $1623.5 million.

The various government agencies are also interested in promoting more efficient domestic markets. One of the requirements of an efficient market is that all market participants must have an equal opportunity to purchase relevant information. No one participant may have the exclusive use of such information. In dealing with firms situated around the world it is virtually impossible for the exporter to have adequate knowledge of the financial state of all purchasers of his products. The government agencies, through their various departments are able to acquire this knowledge. They, therefore, help the exporter better evaluate the potential risk and will, if necessary, provide export credit insurance to reduce both the commercial and political risks faced by the exporter.

In the past, exports were basically a function of price and quality. Now, with the increased competition for world markets, flexibility and the ability to respond to market changes have increased greatly in importance. In addition to quality and price, export sales are now a function of availability, service, reputation, marketing effort, interchangeability of parts and credit. The major exporting nations have greatly intensified the competition for world markets and as a result, credit has become one of the key factors involved in gaining sales or maintaining market share. The role of finance in export sales has increased as a result of the heightened competition among the major trading nations, the realization that the growth areas involve products which are technology intensive and the special financing problems of the less developed nations.

The rapid growth of export credit can best be shown by considering the following statistics. The annual volume of Canadian exports assisted
by the EDC through either direct loans or export credit insurance increased by more than twenty times in the fifteen year period ended December 31, 1975. In 1960, the annual volume was $101.7 million, while the comparable figure for 1975 was $2045.7 million. Merchandise exports on the other hand increased just over 600% in the fourteen year period ended December 31, 1974 to a volume of $32,383 million. Exports supported by the facilities of the Export-Import Bank of Japan grew from ¥108.6 billion in 1962-63 to ¥308.2 billion in 1967-68. Export credits granted by the Ausfuhrkredit Gesellschaft mbH, the institution which provides export credit in the Federal Republic of Germany, grew from DM402 million in 1955 to DM2719.7 million in 1967. In the United States of America exports supported by the Export-Import Bank have grown from an annual volume of $ U.S. 533.0 million in 1960 to an annual volume of $ U.S. 8315.0 million in 1975.

In real terms all of these implied growth rates would be reduced. In the six year period ended December 31, 1974, the exports supported by the direct loan program and the export credit insurance program of the EDC increased, in real terms, at an annual compound rate of 25%. The compound annual "real" rate for exports supported by the Japanese Export-Import Bank from 1962-63 to 1967-68 was approximately 30%. Both of these real growth rates provide support for the belief that export credit by any measure increased at an above average rate.

While all these figures indicate how important a factor credit is becoming in the sale of goods and services in the world market place, the true state of nature may be understated in certain cases. For example, consider only those capital exports which have been directly financed by
Canada's Export Development Corporation. In 1970, EDC granted twenty-two such loans for a total of $100 million. In 1974, forty-six loan agreements for a total of $659.4 million were signed. During this same period exports classified as other manufactured goods, excluding motor vehicles and parts exported to the U.S.A., grew from $2970 million to $5453.0 million. Therefore, in 1970 3.3% of eligible Canadian exports were being financed by EDC, while by 1974 this same figure had increased to 12.1%.

With technology advancing and prices rising, more credit will undoubtedly be needed in the future. The cost of a jet aircraft, for instance, in the not too distant past was in the $7-8 million range, but now with the wide-bodied jets, the cost has increased to the $20-25 million range. Such increases have placed a strain on the cash flows of the purchasers and have created a worldwide challenge for the institutions charged with the responsibility of developing adequate financial measures.

II. DEFINITIONS

Capital goods as defined by the U.S. Department of Commerce are said to consist of electrical machinery, construction machinery, mining and oil field machinery, steel and rolling mill machinery, machine tools, office machinery, agricultural machinery, aircraft, railroad equipment, trucks, buses, automobiles, and parts for all of the above. This definition will be implied whenever the terms capital equipment or capital goods are used in this study.

The terms commercial credit, export finance, or export credit will be used interchangeably in this study. However, each must contain
the following elements:

1) an obligation of the buyer to make a down payment prior to the shipment of the goods

2) the loan must be amortized over a period such that regular equal payments are made with no accumulation of unpaid debt at the end of the repayment period

3) the loan must carry an interest rate which in some way is related to the interest rates offered for similar loans in the lending country. i.e. the interest rate must be a commercial rate as opposed to an "aid" rate

4) the credit is confined to the foreign exchange cost of the transaction, with an exception being made for those local currency costs which are directly associated with the contract

5) the credit shall be eligible for national export credit insurance

6) the contract shall not provide for any explicit grace periods.

The less developed nations of the world (LDCs) will be defined as consisting of all countries in the Western Hemisphere with the exception of the U.S.A. and Canada, all of the countries in Africa with the exception of the Union of South Africa, all of the countries in Asia with the exception of Japan and Mainland China, all of the countries in Oceania with the exception of Australia and New Zealand and the European countries of Greece, Spain, Turkey, Portugal, Yugoslavia, Malta, Gibraltar and Cyprus.

Development finance must have as its primary objective the industrial development of the recipient country. The length of the credit, the interest rate attached to such loans, as well as the commercial and political risk questions must be of secondary importance to the lender.
Development finance and foreign aid are both used synonymously throughout this study. Foreign aid programs have been referred to as the "bankers of the poor". There is no hard and fast rule about when an export credit contains enough of a grant or concessionary element to qualify as aid or development finance. Concessionary flows, for the purpose of this study, are defined as official financial flows containing a large grant element and motivated by an interest in the recipient country. The softening of the terms of credit implies any step that tends to raise the concessional element in a transaction. The grant portion of aid flows is deemed to increase as the interest rate is lowered or as the maturity is lengthened.

For this study, a short term credit will have a repayment period of one year or less, an intermediate or medium term credit will be repaid over a period greater than one year but less than five years, and a long term credit will have a repayment period in excess of five years.

III. ATTEMPTS TO DEVELOP UNIFORM EXPORT CREDIT POLICIES

i) GROWTH OF INTERNATIONAL COMPETITION

By the mid 1950's the retooling of the manufacturing sector of the European industrialized nations was complete. The capital goods market turned from a sellers to a buyers market, and as a result, the credit factor became more important in the sale of goods. The industrialized nations desire to promote their exports of capital goods and the LDCs inability to pay for these same goods caused a dramatic change in the
The U.S. Export Import Bank was founded in 1934 and for a number of years was the only large source of export credit. In Canada, a federal crown corporation, the Export Credits Insurance Corporation was founded in 1945 for the purpose of providing export insurance for Canadian exports. In the United Kingdom, the Export Guarantees Act of 1949 stipulated that any funds allocated under the Act had to be utilized to purchase goods or services manufactured in the United Kingdom. Up until 1952, all U.K. export credits exceeding six months in length were subject to the approval of the Foreign Exchange Control Commission. All contracts approved by the Commission required that one-half of the contract price be repaid within six months with the balance payable over a two year period.

In 1952, the United Kingdom, in an effort to stimulate its sagging exports extended the maximum credit period for transactions with buyers outside the sterling area to three years. The term could be increased to a maximum of five years in cases of national importance. Other industrialized nations began adopting similar strategies and soon international competition in the following areas developed:

1) the cost and availability of credit
2) the portion of the contract price the exporter is required to retain for his own account
3) the amount of the downpayment required by the purchaser
4) the length of the term accorded the credit
5) the speed with which the application is processed
6) the premiums charged for credit insurance.
ii) THE BERNE UNION

The governments of the industrialized nations recognized that a credit war was not desirable, so they created the Union d'Assureurs des Credits Internationaux (Berne Union) to try and bring about an international exchange of information on export credit terms and coordination of policies on a voluntary basis. The Berne Union can not require its members to abide by its decisions. It merely provides understandings and recommendations. While the member governments do not have to abide by these recommendations they are required to report any departures from the recommended standards. Members may question other members on the terms and conditions of policies about to be issued. The Union fostered the development of the "matching principle" and prevented the buyer and the seller from overstating the terms being offered.

In 1953, the members of the Union came to an understanding with regard to the maximum terms that should be provided for various types of export credit insurance. They agreed that the maximum credit period should not be greater than five years. This maximum term would only be granted sales of heavy capital goods. Light capital equipment was to have a maximum term of three years. While it was appreciated that these terms were considerably shorter than the life of the associated asset, it was felt that the debt could be repaid more quickly through the use of depreciation, the cash flow from the undistributed profits and the capital asset replacement funds.

Until the early 1960's the Union was effective in coordinating the length of insurance policies thereby limiting the term of export credit.
By that time, the desire to improve their competitive position caused some of the nations to gradually grant more liberal terms. Longer repayment terms were granted de facto by adopting late starting points from which to count repayment periods. In addition, the maximum terms outlined above did not apply to direct loans made by the various institutions. The practice of granting implicit grace periods appears to still be practiced today. Table I indicates that while some of the loans granted by the Exim Bank are repayable in ten semi-annual installments, repayment does not commence for up to five-six years.

The fact that a substantial number of the Exim Bank's loans involve participation financing makes it difficult to determine if grace periods are being granted. Under the participation financing scheme, commercial banks and the Exim Bank combine to provide the necessary funds. The borrower usually repays the commercial bank's loan first and then repays any funds advanced by the Exim Bank.

The Export Import Bank did not begin offering export credit insurance until 1961, when the FCIA was formed, so in effect its activities were not constrained by the recommendations of the Berne Union until that time. Japan, a major exporting nation, only recently joined the Berne Union.

In the early 1960's the Union recommended that insurance policies with terms of greater than five years be extended only to LDCs. The members abided by this recommendation for a short period, but gradually they began to increase the terms accorded any purchaser of heavy equipment.

The Berne Union in the mid 1970's continues to face many of the same problems it faced in the early 1960's. The inability of the members of the Berne Union to bind their governments to the
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<th>PURPOSE, RATE AND TERMS</th>
<th>AMOUNT ( $ MILLIONS )</th>
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<tbody>
<tr>
<td>BRAZIL Varig-Viacao Aereo Rio Grande</td>
<td>Aircraft, one jumbo jet DC-10. Repayable in 10 semi-annual payments. Repayment to commence beginning May 20, 1980.</td>
<td>12.6</td>
</tr>
<tr>
<td>CANADA Air Canada</td>
<td>Aircraft, one jumbo jet 747. Repayable in 10 semi-annual payments to commence on May 20, 1980.</td>
<td>11.6</td>
</tr>
<tr>
<td>DENMARK Steamship Co. 1912 and Svendborg</td>
<td>Steam turbine units repayable in 8 semi-annual payments to commence on Dec. 5, 1979.</td>
<td>1.8</td>
</tr>
<tr>
<td>SENEGAL Ministry of Finance</td>
<td>Tuna fishing vessels, repayable in 8 semi-annual payments beginning on May 10, 1980.</td>
<td>4.2</td>
</tr>
</tbody>
</table>

SOURCE: Export-Import Bank of the United States, Cumulative Records, 1974
recommendations of the Union prevents the Union from achieving meaningful results. While the officers of the various organizations, such as EDC, may agree with the recommendations of the Union they find it hard to resist local political pressure. The politicians, in an effort to help their local exporters, strive to have the terms accorded export credit extended. In addition, membership in the Union comprises only twenty-one countries and it is doubtful if the position of the LDCs is adequately represented in the Union. A recent study of The Role of Export Credit in Development Finance by McKitterick and Middleton found that all the members of the Union did not submit comparable statistics. The Germans and the Italians, for example, do not submit any breakdown of statistics by length of maturity while the Japanese statistics are at least two years old.

The Union's concentration on export credit insurance further restricts its ability to effectively deal with current problems. At times, however, while the Union may be effective in reducing the level of competition amongst the various industrial nations its ability to bring about significant changes in the field of export credit is limited.

iii. GATT

Paragraph four of Article XVI of the General Agreement for Tariffs and Trade (GATT) specifies that the following shall be considered as forms of export subsidy and as such are prohibited:

"the grant by governments (or special institutions controlled by governments) of export credits at rates below those which they have to pay in order to obtain the funds so employed."
This restriction limits to some degree the interest rates that may be offered on export credit loans. However, Table II shows a wide variation in the rates charged by various countries. In December 1968, the rate for medium term credits varied from a low of 4.5% to a high of 8.5%. While these rates are not current there is no reason to believe that similar spreads do not exist in today's market. In the spring of 1976 the local office of the EDC indicated that the current Canadian rate was in the 9-11% range.

### TABLE II

AVERAGE COST OF EXPORT CREDIT ON DECEMBER 31, 1968.

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<tr>
<th>COUNTRY</th>
<th>MEDIUM TERM CREDITS</th>
<th>LONG TERM CREDITS</th>
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<tr>
<td>Belgium</td>
<td>5.75</td>
<td>6</td>
</tr>
<tr>
<td>Canada</td>
<td>6</td>
<td>6</td>
</tr>
<tr>
<td>Denmark</td>
<td>7.0-8.5</td>
<td>7.0-8.5</td>
</tr>
<tr>
<td>France</td>
<td>6</td>
<td>5.7</td>
</tr>
<tr>
<td>Federal Republic of Germany</td>
<td>6</td>
<td>6-6.5</td>
</tr>
<tr>
<td>Italy</td>
<td>5.9</td>
<td>5.9</td>
</tr>
<tr>
<td>Japan</td>
<td>6</td>
<td>6</td>
</tr>
<tr>
<td>Sweden</td>
<td>5.75-8</td>
<td>5.75-8</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>4.5</td>
<td>5.5</td>
</tr>
<tr>
<td>United States</td>
<td>6-7</td>
<td>6-7</td>
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</tbody>
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SOURCE: United Nations, Department of Economic and Social Affairs, Export Credits and Development Financing, National Export Credit System, 1969, p.2

iv. OECD

The OECD has also expressed concern about the problem of export credit and in 1963 formed the Group on Export Credits and Credit Guarantees
for the purpose of discussing policies and improving cooperation among member governments in this field.\textsuperscript{7} This international organization has also had little success in bringing about more international cooperation in the export credit field. For example, in 1964, the Government of the Netherlands proposed that a maximum repayment period of five years be established for all loans involving export sales to industrialized countries. Loans to support small export sales (less than $1.5 million) to LDCs would have a maximum term of five years. A maximum term of eight and ten years respectively would apply to loans granted to support medium and large scale sales to LDCs. Medium sized sales were defined to be between $1.5 and $5.0 million, while sales of greater than $5 million were classified as large. The normal requirements with regard to down payments, local costs, and equal repayment installments would have applied in all cases. Tied aid credit would have a maturity of fifteen years.

The Netherlands' proposal was discussed for two years and eventually dropped when no meaningful agreement was reached.

The OECD Committee was, however, successful in enabling its members to reach an understanding with regard to the credit terms accorded the sale of shipping vessels. The thirteen major ship building nations agreed that export shipping credit supported by each government would conform to the following conditions:

1) a minimum down payment of 20\% would be required of the purchaser

2) the minimum net interest rate applicable to the credit would be 6\%

3) the maximum repayment period would be eight years.\textsuperscript{8}
These conditions appear to still be in effect in 1976.

v. EUROPEAN ECONOMIC COMMUNITY

The European Economic Community (EEC), has attempted to foster more international cooperation in the area of export finance not only among its members, but among all industrialized nations.

In 1960, the members of the EEC formed a Policy Coordination Group to put forward suggestions for the harmonization between member states of terms and conditions for export credit insurance, financial credits, and investment guarantees taking into account the recommendations of the Berne Union. Over the next thirteen years the members of the EEC could not come to an all encompassing type of agreement covering all facets of export credit. The Policy Group then proposed that the nine member states come to a "gentlemen's agreement" with regard to export credit containing the following terms and conditions:

1) all credits of greater than two years duration would have a minimum interest rate of 7%
2) export sales to industrialized countries would have a maximum repayment period of five years
3) export sales to socialist countries would have a maximum repayment period of 8.5 years
4) export sales to LDCs would have a maximum repayment period of 10 years.

By labelling its recommendations a "gentlemen's agreement" the Policy Group hoped to gain approval for its proposals more quickly than if it had proceeded in a more conventional fashion. "Gentlemen's
agreements" only require the approval of the Committee of Permanent Representatives (the Ambassadors to the EEC of the nine member states) and not the larger Council of Ministers. The Policy Group did not want its recommendations to be lost in the political process. After considerable discussion the members adopted the recommendations of the Policy Group.

Representatives of the EEC then set out to obtain American and Japanese support for the proposals. It was hoped that eventually all of the members of the OECD would adopt these four basic conditions. However, the Americans favored a minimum all-inclusive rate of 8.5%. This all-inclusive rate would include the cost of any export credit insurance and bank commitment fees. The EEC representatives agreed with the concept of an all-inclusive rate, but would only agree to a minimum rate of 8%. In addition, both the U.S. and Japan rejected the concept that credits to industrialized countries could have a maximum term of five years. They argued that socialist countries should not receive better terms than the Western Nations. The EEC accepted this argument and agreed to increase the maximum term accorded industrialized countries to 8.5 years. The U.S. and Japan sought a number of other changes including special terms for all contracts in excess of $100 million. The discussions eventually terminated without coming to complete agreement on all conditions.

The attempts of the EEC to bring about more cooperation in the field of export credit show how difficult it is to obtain international agreement on any major issue. In October 1974, Britain, France, Germany, Italy, Japan and the U.S.A. agreed that a minimum of 7.5% interest would be charged on all official credits which had a term in excess of five years.
International cooperation on bringing about more uniform rules on other aspects of export credit has not yet been achieved.

The EEC Policy Group has also attempted to introduce a standard type of export credit insurance policy. The Group and Commission believe that such policies are really a type of state aid and as such differences in policies may cause trade distortions within the Community. The members of the EEC accordingly have agreed on the terms and conditions to be included in a standard policy, but they are unable to agree on a common premium schedule. The Group's proposal would see different premium schedules adopted for public and private purchasers. In addition, private buyers would be subdivided into at least two classes. The British have voiced opposition to the proposed premium schedules because, while the proposed premiums for public purchasers are comparable with those charged by the Export Credits Guarantee Department (ECGD), the public body charged with financing British exports, the proposed rates for private purchasers are up to four times as large as those charged by the ECGD. The British believe that the proposed rates would place the European exporters at a competitive disadvantage with exporters in the U.S.A. and Japan. One of the goals of all corporate bodies charged with providing export credit and insurance is to ensure that their exporters are not placed at a competitive disadvantage.

The EEC members have agreed to the following: to ensure that no official aid is provided to exporters for sales within the community; to coordinate their activities with regard to sales to third countries; and to automatically include within the master insurance contract some of the goods manufactured by subcontractors. In addition, the members have agreed to
advise the Commission before granting insurance for credits with a term of more than five years or any type of cover that departs from previously accepted rules with respect to supplier credits, buyer credits, lines of credit or mixed credits. The other members have seven days to voice their disapproval of the proposed transaction and may call for a meeting of the Policy Group to debate the issue. For example, in 1970, France notified the Commission that it wanted to increase the maximum term accorded to credit sales to East Germany. After a discussion of the problem, the Commission agreed to extend the maximum period to eight years from five. This consultative process acts as a restraining influence against the progressive softening of terms.

In their agreements on subcontracts, the members automatically include in the cover provided for a main contractor, cover for goods produced under a subcontract in a member state. The maximum coverage provided for subcontractors varies from 30-40% depending on the size of the main contract.

The increasing world emphasis on large scale projects such as power plants, industrial facilities and aircraft has resulted in firms banding together either in joint ventures or in consortia to produce the required projects. The financial and production risks involved in these major projects may be beyond acceptable limits for a particular firm. The European consortia are at a considerable disadvantage when competing against Japanese or American groups. The disadvantages include the risk incurred in using several currencies as well as the problem encountered in coordinating the multitude of different programs offered by agencies throughout the community. In addition, the Americans have access to a
large resource base and the Japanese have a closer relationship with their government and financial community. In an attempt to overcome these difficulties the Commission proposed that a community export bank be established. This bank, to be called Eurexbank, would provide both an alternate source of export finance and a means of standardizing export credit insurance policies. The national interests of the member countries as well as practical difficulties will undoubtedly hamper the development of such an institution.

IV. EXPORT CREDIT INSURANCE

Prior to the introduction of export credit insurance a vendor was somewhat reluctant to sell his products abroad for fear that it might be both costly and complicated to collect past due foreign accounts. In addition, the average exporter was aware that exchange restrictions might prevent him from repatriating his funds once the receivable had been liquidated. To overcome both these problems the industrialized nations, as early as the 1930's, began to introduce a form of export credit insurance to reduce both the commercial and the political risks associated with foreign sales. The insurance of the commercial risk can be viewed as being similar to that provided for any other risk, such as fire, life, or automobile. The population involved is large and its cells are independent. For political risk, however, it is not possible for actuaries to properly evaluate the risks because of the relatively small number of independent nation states in the world.

The commercial risks which are insured include the insolvency of the buyer and protracted default. The failure of the purchaser to pay
for the goods within six months of the due date constitutes protracted default.

The political risks insured usually include:

1) the transfer risk which is defined as the risk associated with converting the purchaser's local currency into the currency required by the vendor

2) the cancellation or non-renewal of a vendor's export licence

3) the cancellation of the authority of the buyer to import the shipment

4) war, hostilities, civil war, rebellion, revolution, insurrection, civil commotion or similar disturbances

5) expropriation or confiscation of the products or the business of the buyer by a government authority

6) any action having the force of law which prevents the buyer from making payment.

In the case of the Exim Bank only those non-commercial risks specifically outlined in the policy are covered, whereas the Export Credits Guarantee Department and the EDC cover all risks which are deemed to be beyond the control of the supplier or the buyer.

The premiums charged for insuring these risks vary according to the type of policy issued, the buyer's credit worthiness and the grading assigned to the buyer's country. The risk attached to a particular country is in turn a function of that nation's general economic stability, its level of foreign exchange reserves, its foreign exchange policy and its balance of payments prospects. The insurer looks in detail at such factors as the productive capacity of the nation, the technical ability of the people, the structure of the foreign government and the amount of
external debt outstanding. The insurer is interested in the ability of the foreign country to service its foreign debt. The ECGD, as reported by Tomlinson, does not like to see a debt service ratio, defined as the ratio of debt payments to foreign exchange earnings, of greater than 12% for a narrow economy or a ratio of greater than 20% for a broadly based economy. 14

Once the country’s position has been carefully analyzed, it is assigned to one of four risk categories, A, B, C, or D. The A markets are considered the safest and as such are assigned the lowest premiums. Despite the fact that the positions of all nations are under constant review, upward mobility in the ranking structure is limited. Tomlinson found in his review that the ECGD was particularly concerned about the possible introduction of foreign exchange controls. An officer of the ECGD stated that if a country introduced any procedures which delayed or cancelled payment through the lack of foreign exchange then that country would automatically lose its classification and almost certainly would be reclassified to the C or D category. He stated it is "unlikely ever to be reclassified as A or B". 15 Table III shows how some of the countries were classified by the ECGD in July 1969.

It should not be assumed that the insurance policies provide 100% coverage for all risks outlined in the policy, for such is not the case. All policies contain some type of co-insurance clause under which they only provide 90-95% coverage for the political and commercial risks insured. In some cases the policy only covers 70% of the loss for political risks. The premiums vary according to the type of policy issued—whether it covers all export sales or only certain specified items,
### TABLE III

**E.C.G.D. RISK GRADING 1969**

<table>
<thead>
<tr>
<th>A</th>
<th>B</th>
<th>C</th>
<th>D</th>
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<tr>
<td>Australia</td>
<td>Czechoslovakia</td>
<td>Argentina</td>
<td>Afghanistan</td>
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<tr>
<td>Austria</td>
<td>Greece</td>
<td>China</td>
<td>Brazil</td>
</tr>
<tr>
<td>Belgium</td>
<td>Israel</td>
<td>Colombia</td>
<td>Ceylon</td>
</tr>
<tr>
<td>Canada</td>
<td>Malaysia</td>
<td>Guatemala</td>
<td>Chile</td>
</tr>
<tr>
<td>France</td>
<td>Poland</td>
<td>Iran</td>
<td>Cuba</td>
</tr>
<tr>
<td>German Federal</td>
<td>Saudi Arabia</td>
<td>Iraq</td>
<td>Ghana</td>
</tr>
<tr>
<td>Republic</td>
<td>Venezuela</td>
<td>Korea (South)</td>
<td>India</td>
</tr>
<tr>
<td>Italy</td>
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<td>Pakistan</td>
<td>Indonesia</td>
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<tr>
<td>Japan</td>
<td></td>
<td>Peru</td>
<td>Korea (North)</td>
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<tr>
<td>Mexico</td>
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<td>Paraguay</td>
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<td>Portugal</td>
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<td>Syria</td>
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<td>Spain</td>
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<td>Turkey</td>
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<td>Sweden</td>
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<td>United Arab</td>
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<td>Switzerland</td>
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<td>Republic</td>
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<tr>
<td>U.S.A.</td>
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<tr>
<td>Vatican City</td>
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</tbody>
</table>

the overall export credit experience of the firm and the percentage of
the co-insurance carried by the exporter. In general, the premiums
charged on export credit insurance policies have declined dramatically
in the past few years. Premiums to insure "normal type" sales are
currently less than one-half of one percent of the amount insured.

The reduction in premium schedules has occurred as a direct
result of the increased volume of goods being insured. In addition, the
ability of the insurer to evaluate political risk more accurately has
contributed to a reduction in premiums. The insurers are usually public
bodies and as such are not profit maximizers. They are only concerned
with generating sufficient income to cover any losses, to provide a
reasonable level of reserves for future losses and to cover their current
operating expenses. In all countries the export credit insurance loss
ratios have been very small. In their first thirty-three years of
operation, the Export Credits Guarantee Department insured approximately
$28 billion of United Kingdom exports. During this same period less
than 1% of the amount insured ($244 million) was paid out in claims. In
its first three years of operation in the United States the insurance
program insured $1.4 billion of exports. Net losses during this period
amounted to $1.9 million, approximately one-tenth of one percent of the
amount insured.

The volume of exports insured under the various types of
insurance policies has grown rapidly. The annual volume of insurance
authorizations of the Export-Import Bank increased from $693 million
in 1966, to $2929 million in 1975. The annual volume of exports insured by
the EDC increased from $263 million in 1969 to $911 million in 1975.

In order to provide a comprehensive analysis of the entire
export credit picture, it is useful to provide a brief description of the various types of insurance policies available to the exporters. The basic types of policies offered by the Foreign Credit Insurance Association (FCIA) in conjunction with the Exim Bank include:  

1) Master Comprehensive Policy  

Provides blanket coverage (usually 90%) for both political and commercial risks on all of an exporter's eligible short and medium term credit sales.

2) Short Term Comprehensive Policy  

Provides 90% coverage for commercial risks and 95% coverage for political risks on all of an exporter's eligible credit sales which have a term of less than 180 days. To be eligible each sale must have at least 50% American content.

3) Medium Term Comprehensive Policy  

Provides 90% coverage for both political and commercial risks on sales of capital or quasi-capital goods solely of U.S. origin. Eligible sales must offer terms of 181 days to five years. This type of policy usually is issued on a buyer by buyer basis.

4) Short Term Political Risk Policy  

Provides 90% coverage for political risk only.
Eligible export sales are usually required to have a term of less than 180 days.

5) Medium Term Political Risk Policy

Provides 90% coverage for political risks only. Usually issued on a buyer by buyer basis. Covers eligible export sales which have a term from 1/2-5 years.

6) Combined Short Term, Medium Term Comprehensive Policy

Provides coverage for the sale of capital or quasi-capital goods to overseas distributors and dealers. This type of policy is issued on a dealer by dealer basis and provides coverage for the total inventory while it is in the dealers' possession. If and when the products are sold the coverage ceases in the case of a cash sale. In the case of a credit sale, the coverage will remain in effect until the debt is retired provided that the purchaser makes a 10% down payment and forwards promissory notes for the balance to the exporter.

7) Master Political Risk Policy

Provides coverage of 70% for political risks only. Eligible export sales must have a term of less than five years. The premium is based upon the spread of the risks in the foreign markets. The premium for this type of policy is considerably lower than that charged for other types of policies because the exporter is retaining 30% of the risk.
8) Small Business Policy

This policy is designed to meet the needs of firms just entering the export market and to assist those exporters with a modest export sales volume. Under this policy which provides 90% comprehensive coverage for all short and medium term sales, the exporter may choose to insure all export sales or just certain sales to specific markets. To qualify for this type of policy the exporter must have an annual export volume of less than $200,000. The coverage remains in effect until an aggregate of $500,000 of exports have been insured for the exporter or until two years have elapsed since the issue date, whichever comes first. The premiums vary, but are significantly less than those charged on other types of comprehensive policy.

9) Discretionary Credit Limit Policy

Once an exporter has a proven record with the FCIA, he may, under a special type of agreement, be able to qualify transactions for insurance coverage without submitting a special application to the FCIA. The exporter is assigned a maximum credit limit and as receipts are received for past export sales, he may automatically make new export sales and include them in his insured assets. In effect, the exporter has a line of credit with the FCIA and as long as he files a monthly report of his export sales with the FCIA and pays the required premium, he can continue to insure his export sales. The maximum amount of coverage that may be outstanding at any one point in time is, of course, specified by the FCIA.

In addition to reducing the commercial and political risks facing the exporter, insurance policies facilitate the financing of export sales. The exporter may assign the proceeds of an export
credit insurance policy to a financial institution as security for a loan to finance his operating requirements. The commercial banks are usually willing to make such loans on a non-recourse basis because of the strength of the corporation issuing the insurance policy. The bank usually retains the right of recourse to the exporter in the case of default not covered by the policy. The bank also requires the exporter to retain a portion of the credit for his own account. For example, if the policy provides 90% coverage for all political and commercial risks, then the exporter may be required to retain 10% of the net amount of the sale for his own account. The net amount of the sale is the gross contract value less the down payment provided by the purchaser.

The small exporter is unlikely to produce the type of capital good which requires a repayment period in excess of five years. He will, therefore, make little use of the direct lending facilities of the national export credit granting institutions. For example, the EDC has no special facilities to meet the needs of the small exporter. He must obtain any necessary financing from a chartered bank on the strength of his export credit insurance policy or he must ensure that his products qualify for direct loans under Section 29 or 31 of the Export Development Act. The Exim Bank, on the other hand, has developed a cooperative financing facility (CFF) which has greatly aided the small American exporter in financing his sales. (This facility will be discussed in greater detail later in the study.) In the fiscal year (FY) ended June 30, 1974, the Exim Bank authorized 1563 loans for a total of $212.6 million under its CFF and Relending facility. The success of the Exim Bank's program indicates that export credit insurance
by itself cannot meet all of the financing needs of the small exporter.

V. BANKS AND EXPORT CREDIT

The important role that commercial banks play in financing economic activity must not be understated. While the banks have been reluctant to grant credit beyond a five year period, they are slowly beginning to extend their horizons to a 7-8 year period. In addition, international banking consortia are being formed to provide the financing needed to meet the ever-changing needs of international business. An exporter who finds it necessary to offer extended credit in order to complete an export sale usually seeks the advice of his banker first because of his expertise in the field. If the banker is unable to provide the necessary financing, he may be able to identify other potential sources of funds.

The credit terms offered by a bank will not exceed those which are customary in international trade for the type of product involved. The bank will only match the credit terms already established in the international community.

Banks have attempted to increase their international flexibility through the development of financial consortia. For example, the MAIBL consortium was created in 1964 for the purpose of providing medium term financing for projects throughout the world. The founding members were the Midland Bank and the Standard Bank from the United Kingdom, the Commercial Bank from Australia and the Toronto Dominion Bank from Canada. MAIBL became a trend setter in international finance by lending substantial amounts of funds in the 2-7 year area. Banks on their own
were reluctant to enter the international term credit field for a number of reasons including custom and legislation. MAIBL's success proved that the lucrative intermediate term credit field could be tapped if the banks cooperated and pooled their resources.

Banks are slowly becoming more active in the international term credit field. The major factors restricting their growth in this area are the banks' inability to properly evaluate both foreign commercial and political risks, their desire to keep their portfolio in a relatively liquid form and their lack of experienced personnel. The banks' inability to properly evaluate the commercial and political risks can be offset through the use of export credit insurance. The banks will probably never totally overcome their desire to retain a relatively liquid portfolio, but if even a small portion of their loan portfolio is allocated to longer term credits it may prove to be a significant source of credit. The development of consortia like MAIBL and the ORION group may indicate future patterns in international banking. The problem of developing better personnel in the field of international finance may prove to be the most difficult barrier to overcome. The bright, young financial executive rarely sees his future in international finance. Instead, he sees his future managing private investment flows between his company and specific foreign countries. The increasing importance of international finance will hopefully change this attitude in the not too distant future.

VI. CONCLUSIONS

The first chapter of this study has shown the increasingly
Important role that export credit is playing in determining trade flows throughout the world. This introduction has also demonstrated that national export credit practices have developed in a relatively uncontrolled competitive environment. Each nation is primarily interested in ensuring that its market share of world exports does not decrease. The nations, therefore, adopt whatever type of strategy is deemed necessary to protect their position. The probability that the industrialized nations will sign an agreement governing international credit practices is not large. This view is supported by the attempts of the Berne Union, the OECD, and the EEC to bring about a greater amount of international cooperation.

The problems associated with export credit have at least two dimensions, -- export credit insurance and loans. Export credit insurance provides the exporter with the collateral needed to arrange the necessary financing with a commercial bank. Loans to the purchaser allow him to pay cash to the vendor. Direct loans are granted by the national export credit granting institution, which in effect is a type of self-financing financial intermediary.

At some point in its future, the institution's cash inflow consisting of payments on outstanding loans, various non-cash expenditures and net profit should approximately equal the cash outflow created by granting new loans. Any funds that may be required to accommodate a reasonable rate of growth would be obtained by borrowing in the capital markets. The rapid growth of export credit has, however, prevented this theory from being applied by the national export credit granting institutions. The Exim Bank's total debt outstanding has increased by over 400% in the ten year period ending June 30, 1975. In the last fiscal
year Exim Bank's total borrowings increased by $1.5 billion to $6.85 billion. The Export Development Corporation has shown a similar rapid growth in total outstanding debt. On December 31, 1969, EDC's total outstanding debt was $253.6 million. By December 31, 1975, the comparable figure was $965.1 million, an increase of 280% in just six years.

In the past fiscal year EDC signed a total of forty-one agreements for a total of $1,135 million. The value of the contracts signed, net of bank participation, was $935.7 million. In the FY 1973, EDC signed thirty-six loan agreements with a total value of $462.9 million. If these phenomenal growth rates continue into the future a review of the costs and benefits of this type of activity should be undertaken.

It can be argued that organizations such as the Exim Bank and the EDC are not a direct cost to the taxpayer. While it is true that they do not require a direct subsidy for their operations a substantial portion of their outstanding debt is payable to the Treasury of their respective nations. In the case of the EDC, on December 31, 1975, only $14.9 million of its total outstanding debt of $965.1 million was payable to investors in the private market. In addition, one must also consider the commitment these organizations are incurring by signing large volumes of new loan agreements. In the case of EDC, it appears as if a commitment to obtain funds at a certain rate of interest is not obtained when the funds are committed via a loan agreement. Normally, the funds are disbursed over a period of time as the goods are manufactured by the exporter and received by the purchaser. The EDC borrows a substantial portion of the funds it disburses, and the interest rate applicable to these borrowings is established when the funds are drawn down. The interest rate
applicable to the credit, on the other hand, is established when the credit is signed, which may have been 1-2 years earlier. Canadian Crown Corporations such as EDC are able to borrow the necessary funds needed to meet their operating needs from the Consolidated Revenue Fund at a rate of 1/8% above the rate applicable to similar federal government borrowings. With the escalation of interest rates in the past few years it would appear that the operating margin attached to EDC's direct loans should be decreasing.

The total of undisbursed financing under the signed agreements has increased dramatically in the past three years. At the end of FY 1972, total undisbursed financing was $422.9 million and the comparable figure on December 31, 1975 was $1461.8 million. The undisbursed financing figure means that if the EDC stopped signing loan agreements on December 31, 1975, it would still have to borrow an additional $1.5 billion to meet its past commitments. The relatively small size of the Canadian capital market, the great demand for federal government funds, and the capital needs of projects such as the Mackenzie Valley Pipeline all dictate that EDC must raise a substantial portion of its funds in the offshore market. The large interest differential that presently exists between the Eurobond market and the Canadian market should ensure that funds can be raised at a comparable interest rate to that available through the Consolidated Revenue Fund.

The balance of this study will be concerned with examining the overall effectiveness of the Export Development Corporation. The financial impact that EDC's activities will have on the Canadian capital markets will be analyzed; the costs and benefits that accrue to Canada from having a public corporation such as EDC promote Canadian
exports will be discussed and some recommendations for the future will be presented. In effect, the objective function of this study is to find a method by which Canadian capital exports can be maximized in order to maximize the benefits to the Canadian economy.

In order to develop a better understanding of how effective the Canadian system is meeting its objectives, portions of the systems in operation in the United Kingdom and the United States of America will be reviewed. The analysis section will include a breakdown by type of product of all American and Canadian capital equipment exports. The Canadian analysis will also provide a breakdown according to the size of the exporting firm. International trade theories based on various concepts of comparative advantage basically state that nations should export those products in which they have some type of comparative advantage, be it in raw materials, natural resources, skilled labour or technological know-how. The analysis of Canada's capital equipment exports will attempt to determine the applicability of the comparative advantage theory.

Financing facilities and grants such as those provided by EDC, the Federal Business Development Bank, the Department of Regional Economic Expansion, and the Department of Industry, Trade and Commerce are used to broaden the base of Canada's industrial sector. This study will attempt to analyze how successful the financing facilities provided by the EDC accomplish this goal.

A simple well-structured method will be developed to forecast the future cash needs of the Export Development Corporation. The problem of how and where the necessary funds should be raised will be discussed
and a unique solution to the problem utilizing the secondary reserve position of the chartered banks will be presented.

While the goal of maximizing the net benefit to Canada is the basic concern of this study, the purchaser of the goods being exported must also be considered. If a large portion of such capital equipment exports are being purchased by LDCs then perhaps the EDC should be concentrating on developing a hybrid type of financial policy that encompasses both export credit and development finance. It is extremely difficult to determine where export credit stops and where development finance begins. However, the developed nations cannot expect to continue to maintain the existing flows of capital exports to the developing nations without increasing the aid component of such flows. If the industrialized nations continue their existing policies the developing nations will face a serious debt servicing problem or else the annual volume of exports to the LDCs will have to be substantially reduced. At present, Canada has a chance to be a world leader in developing a new policy for dealing with capital equipment exports to LDCs.

Chapter II will provide a description and an analysis of the activities of the Export Credits Guarantee Department in the United Kingdom. Chapter III will focus its attention on the activities of the Export Import Bank of the United States. Chapter IV will provide both the description and the analysis of the activities of Canada's Export Development Corporation. The focus of attention for the chapter will be the financing agreements and guarantees sector. The EDC's activity in the export credit insurance field has already been briefly discussed.
and will not be dealt with at any length in this study. The export credit insurance facility is basically provided on a cost plus very marginal markup basis. The probability of the insurance sector requiring a large injection of funds is very low and could only occur if a substantial portion of the purchasers defaulted on their contracts at the same time. In addition, it is impossible to do an analysis of the exports supported by insurance because of a lack of published information. The analysis will, therefore, concentrate on the export credit and guarantees sector of the export credit field.

In Chapter V the cash forecasting technique will be developed as will the proposed method of raising the necessary funds for the Export Development Corporation. Chapter VI will conclude by summarizing the objectives of the study and the more important results.
FOOTNOTES

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FOOTNOTES CONTINUED


The Export Import Bank's Publication, Exim Bank - How it Works, provides current information on any new type of policies being introduced.

CHAPTER I

THE EXPORT CREDITS GUARANTEE DEPARTMENT

The goal of the British government in establishing the Export Credits Guarantee Department was to ensure that exporters in the United Kingdom are able to compete on equal terms with any foreign competition that has credit insurance or equivalent government support. ECGD does not normally initiate any lengthening of the general terms of credit in international trade. In order to achieve its objectives, ECGD provides both export credit insurance and financial guarantees for the exporter. The standard insurance policy provides coverage against the transfer, insolvency, default, war and other risks associated with export trading. The financial guarantees are provided by ECGD to the British exporter who then obtains the necessary financing from a clearing house bank.

To obtain a guarantee the exporter approaches the ECGD to ascertain if they will support the transaction involving his potential sale. ECGD in evaluating the application considers such factors as the terms being offered, the nature of the export, the credit worthiness of the potential buyer and the financial standing of the purchaser's country—the same basic factors that are considered in evaluating an insurance risk. The export must have a value greater than £100,000 and the repayment period must be greater than three years from the date of
shipment. Once the ECGD guarantee is issued the supplier approaches his bank to negotiate a loan agreement between the purchaser and the bank. The British banking system has been very receptive to such loan applications and generally grants the loan on the strength of the ECGD's guarantee. Once the goods are manufactured by the supplier and received by the purchaser, the funds are released to the exporter. After paying the ECGD its fee for issuing the guarantee he is no longer involved in the transaction. If the purchaser defaults on payment, the bank has no recourse to the exporter but must look to the ECGD to implement its guarantee. The ECGD agrees to provide unconditional payment within ninety days of the due date. The ECGD retains the right of recourse to the exporter for any default on payment not covered by the guarantee.  

The British system revolves around the issuance of insurance policies and financial guarantees. The ECGD is not involved in granting direct loans to either the purchaser or the supplier. The Bank of England, however, provides a rediscount facility for export loans granted by the banks. This rediscount facility will be examined later in the chapter.  

A substantial portion of the export credit granted in Britain is provided by the clearing house banks in London and Scotland. The discount houses, the Export Refinance Corporation and the banking syndicates also supply funds to support British exports. The reliance on the private sector to provide the bulk of export credit makes it difficult to obtain relevant data on the volumes of capital equipment exports which are supported by the ECGD's activities. The British do
not appear to provide a detailed breakdown of the goods financed as a result of guarantees issued by the ECGD. Both the Exim Bank and the EDC provide the name of the purchaser, the products sold and the terms of repayment. In addition, the Exim Bank indicates the interest rate applicable to each loan, but fails to indicate the name of the exporter. The EDC, on the other hand, provides the name of the exporter, but does not indicate the applicable interest rate. Similar information does not appear to be available for British exports and as a result, it is not possible to analyze the British situation in great detail. The balance of this chapter will concentrate on providing some data to indicate the growth and flexibility of the British system.

I. FLEXIBILITY OF SYSTEM

The annual volume of export insurance and financial guarantees issued by the ECGD increased from £300-400 million a year in the early 1950's to more than £2 billion a year in the early 1970's.

The decline in overseas foreign exchange earnings has resulted in the adoption of flexible policies by the ECGD. In October 1960, for example, the ECGD was authorized to support British exports which required a repayment period of more than five years provided that similar terms were being offered by other national export credit granting institutions. The ECGD was authorized to match the terms being offered provided that the support did not take the form of direct aid to the buyer's country. By 1964, the ECGD had provided export insurance with maturities ranging up to thirteen years.4
In the early 1960's the banking system, which provided nearly all of the nation's export financing, and the ECGD appeared to be on a collision course. On the one hand, the ECGD was being forced by international competition to extend the terms of its insurance and guarantees to more than five years, while the banks viewed loans with repayment periods of up to thirteen years as being far beyond the traditional view of an appropriate term for a bank loan. This conflict was resolved with the introduction of the rediscount facility by the Bank of England.

In 1961, the Bank of England agreed that when the banks were in a tight liquidity position, it would refinance a portion of their export credit portfolio. The Central Bank's discount facility applied only to insured export credits which had a term of longer than three years. The amount eligible for refinancing was the greater of that portion of the eligible credit which matured in more than 18 months or 30% of the total amount of the eligible credit. This facility proved to be extremely popular with the banking community because it allowed the banks to classify their eligible export credit assets as a liquid asset for liquidity ratio requirements. Therefore, even if the eligible loan were not refinanced with the Bank of England, the rediscount facility assisted the British exporter.

To ensure that the percentage of eligible loans did not become too large a portion, the bankers agreed that each would refinance that portion of fixed-rate export and shipbuilding credit which exceeded 5% of the average of the bank's gross deposits over the previous twelve month period. The rediscounting facility has not been used extensively
by the British banks. In 1970, the banks made use of the facility for the first time when £127 million of eligible export credit was refinanced.

In 1965, as a result of the gradual lengthening of the repayment period applicable to export credit, the Bank of England introduced a further measure for refinancing export credit. At that time, the central bank agreed to refinance the whole of the outstanding balance of any export credit which had a term of greater than five years and which had been granted more than five years ago. That is, the facility did not become operative until 1970, when those credits granted in 1965 with a term in excess of five years became eligible for refinancing. This refinancing facility effectively reduced the term of any export credit granted by an eligible bank to five years, a term more acceptable to the conservative banking community.

II. INTEREST RATE FOR EXPORT CREDIT

Prior to 1962, the interest rate charged for bank loans secured by export credit insurance policies was \( \frac{1}{2} \) to \( \frac{1}{2} \) more than the Bank of England rate. The interest rate on such loans was usually tied to the Bank of England rate and could fluctuate over the life of the loan. It, therefore, became increasingly difficult for the British exporter to compete against foreign exports which were supported by low, fixed-rate credits. The British banks as well as some insurance companies, in 1962, agreed to provide export financing at a fixed rate. The rate for bank loans repayable within seven years was initially established at 5.5%. This agreement was reached one year after the Bank of England introduced
its refinancing facility.

The 5.5% rate was maintained until 1967, at which time the matter was reviewed. The banks agreed to continue to provide export credit at a 5.5% rate for a further five year period with the understanding that the agreement would be subject to review if there was a major change in the basic structure of the interest rates. The increase in world interest rates in the late 1960's caused the banks some concern as they began to realize that both they and their customers were subsidizing the U.S. exporter or the overseas buyer on a substantial scale. In October 1970, a new agreement, calling for a fixed rate of 7% for export credit was reached. In addition, the banks were permitted to charge a 1% commitment fee for all approved applications for long term credit.

In 1974, the ECGD was reorganized and a new interest rate structure was adopted. For loans repayable over a 2-5 year period a fixed rate of 7% was to be charged, while for those loans repayable over more than five years a variable rate schedule of from 6-8% was adopted. Most of the longer term loans supported by the ECGD are believed to be granted at the lower end of the range.

Export credits provided under the fixed rate schedule as well as credits provided for ship building loans are excluded from any official monetary restraints imposed by the Bank of England.

The problem of establishing a competitive interest rate for export credit is constantly being reviewed and is subject to a number of different interpretations. On the one hand, it can be argued that a hardening of interest rates will make the British exporter less competitive
and it will create more of a debt servicing burden for the developing nations. The LDCs purchase a substantial volume of the world's capital equipment exports. On the other hand, one can argue that the owners and customers of the British banks should not be asked to subsidize the British exporter and/or the overseas purchaser. The banks argue that if the exporter and/or the purchaser is to be subsidized, then such a subsidy should come from government's general revenues. The Articles of GATT, however, theoretically prevent any government from directly subsidizing exports through the use of lower than market interest rates.

The total cost of export credit consists of the interest rate charged by the lender, commitment fees, management fees and export credit insurance premia. The total cost could be well beyond the figure expressed by the interest rate. Fair, in his study of Export Credit Problems, showed that charges other than the interest rate could increase the cost of export credit by 0.75-1.75%.

III. OTHER FORMS OF EXPORT CREDIT

The ECGD may issue financial guarantees to encourage United Kingdom exports or to provide economic assistance to a depressed British industry. In the latter case, the hope is that by providing the financial guarantee, the industry may be more successful in selling its product abroad. The British ship building industry has been the beneficiary of support from both the ECGD and the private sector through the Ship Mortgage Finance Company Limited. The ECGD offers a ship building guarantee which is a type of insurance policy that provides 95%
coverage against all commercial and political risks if the ship builder bears all the preshipment risk. The ECGD's position is secured by mortgage security over the ship. The Ship Mortgage Finance Company Ltd. is a privately owned company founded in 1951 for the purpose of providing medium term loans to the purchasers of ships constructed in the United Kingdom. Both domestic and foreign purchasers are eligible to apply for such loans, which are secured by first mortgages on the ships. Unfortunately statistics outlining the success of these two programs are not available.

The British exporter may also obtain export credit from the Export Refinance Corporation (ERC), a private corporation founded in 1961 for the express purpose of providing medium and long term export credit. All funds advanced by the ERC are secured by ECGD guarantees or insurance policies. The ERC provides the exporter with 85% of the financed portion of the export sale. As the payments are made by the purchaser, the funds are divided proportionately between the ERC and the exporter. The facilities of the ERC appeal to the small exporter and to the firm which encounters difficulty in financing its exports through one of the local banks.

IV. CONCLUSIONS

The ECGD takes great pride in its ability to respond to the needs of the British exporter. It claims to be the world's largest credit insurer and reports that it insures in some form over 25% of the United Kingdom's exports. By comparison, only about 5% of Canada's total exports received some type of EDC support in the year
ended December 31, 1974. The British institution also claims to approve 80% of all insurance applications within 48 hours of receipt. The ECGD has sixteen offices located throughout the United Kingdom as well as an office in New York. Over the years the British corporation has built up a massive credit file on over 150,000 purchasers of United Kingdom exports. The ability to access this information undoubtedly speeds up the processing of insurance applications.

The ECGD offers a unique plan through its Full Percentage Insurance Contract. This plan provides that for contracts of greater than three years duration, the normal percentage coverage (80–90%, depending upon the type of policy and the risk involved) will be provided for both commercial and political risks during the first two years of the contract. At the end of two years, if the contract has run satisfactorily, the coverage on all risks is increased to 100% for the balance of the contract at no extra charge.

The export credit facilities offered in the United Kingdom rely almost exclusively on the private sector to provide the necessary funds. The government authorities have so far resisted the pressures to form an export-import bank modelled after the U.S. Exim Bank because they believe that the private market is capable of providing the needed funds. The competitive nature of the private market helps to develop more efficient domestic capital markets. The public sector through the Bank of England and the ECGD provides the "fine tuning" needed to shape the private market. The rediscount facility of the Bank of England is a good example of the "fine tuning" process.
However, all systems are subject to some form of criticism or at least doubt. While ECGD proudly states that 25% of all U.K. exports are supported by export credit insurance policies, this fact may indicate that export credit is not being provided unless the goods are insured by ECGD. The exporters have been critical of the conservative attitude of the banks. The manufacturers believe that the bankers are too cautious and do not support the manufacturers' sales efforts because of the bankers' ignorance of the products being produced and their unwillingness to send bank staff abroad on sales missions or to trade fairs. The sales representatives of the manufacturers are, in effect, forced to represent the position of the British banks. The exporters believe that the inability of the ECGD to effectively coordinate the efforts of bankers and businessmen is one of ECGD's major failures.

Grossfield, in a study of the effectiveness of investment incentives, is critical of the attention focused on export credit. It is his belief that export credit is ineffective, both in helping a nation develop its industrial structure and in favorably influencing the balance of payments position of that nation. He argues that industrial growth occurs primarily as a result of explicit development policies. Export sales, in turn, accrue to those firms created in response to this type of government policy. Export credit is, therefore, relatively ineffective in developing a nation's industrial sector. Grossfield also states that the balance of payments position of a nation can only be improved in the short run, if the increased exports are not offset by an increase in export credit. If both factors increase, the nation's balance of payments will only be improved over the long run as the
foreign borrower repays the debt incurred when he purchased the article. The type of arguments presented by Grossfield show that the development of an optimal strategy with regard to export credit is a difficult task.
FOOTNOTES

CHAPTER II


3. Loc. cit.


CHAPTER III

THE EXPORT IMPORT BANK OF THE UNITED STATES

The United States is, by far, the world's largest exporting nation. In each of the past thirty years the U.S. has produced at least 11% of total world exports. The enormous size of the U.S. market can be shown by considering the exports of one type of manufactured goods. In 1973, U.S. exports of machinery and transportation equipment (revised SITC 7) were $26.6 billion while total Canadian exports were $25.4 billion. In the same year, Canada's exports of machinery and transportation equipment were $7.9 billion. Considered in another way, U.S. exports in this one category in 1972 exceeded total exports for each of the following regions: all of the developing nations in North, South and Central America; all of the LDCs in Africa; all of the nations in the Middle East; all of the countries in Oceania; and all of the countries of Asia with the exception of Japan. Only the total exports of the EEC, EFTA, the Centrally Planned Economies, and Japan exceeded U.S. exports of machinery and transportation equipment. While this comparison does not allow for the increase in petroleum prices in 1973, it does indicate the enormous size of the American market. The latest published trade figures indicate that the countries or regions which have the greatest share of world trade are the European Economic Community, the Organization of Petroleum Exporting Countries and the United States.

In 1973, the United States had 65% of the world's export market for aircraft; it exported nearly 12% of all telecommunications equipment
and nearly 19% of all railway vehicles. All of these products are capital equipment and as such are eligible for export finance. The Export-Import Bank is the American export credit granting institution designed to support American exports. The Exim Bank's activities have shown a dramatic increase in the past ten years. In FY 1966, the Exim Bank supported export sales with a total value of $2.1 billion, while the comparable figure for 1975 was $12.5 billion. Total annual loan and guarantee authorizations nearly doubled in the five year period ending June 30, 1975.

One of the purposes of this study is to constructively criticize the operations of Canada's Export Development Corporation. In order to have a standard against which to measure the EDC's activities this chapter will provide a review and an analysis of the Exim Bank's operations.

I. PURPOSE AND GOVERNING AUTHORITY OF THE EXIM BANK

Edge Act subsidiaries of U.S. banks, investment companies, factoring firms, and commercial banks in addition to the Exim Bank all provide some form of direct export credit. In addition, both the Domestic International Sales Corporations (DISCS) and the Western Hemisphere Trade Corporations (WHTC) are aimed at increasing U.S. exports. The Agency for International Development (AID) provides direct loans to foreign governments or their agencies to foster the development of the industrial sector of the recipient nation, but its activities are more correctly classified as development finance.
The Exim Bank was originally established in 1934 to provide a means of financing American trade with Russia. No loans were, however, made for that purpose and the objectives of the organization were changed so that it was involved in facilitating and financing U.S. export trade in general. The Exim Bank is primarily concerned with the promotion of U.S. exports and helping the LDCs develop their industrial sectors is of secondary importance to the bank. It is the only U.S. government agency which is actively engaged in project financing in both developed and developing nations. The loans and credits granted by the Exim Bank can only be spent to purchase goods produced by firms domiciled in the U.S.A. The Bank is intended to supplement and encourage, but not compete directly with private capital i.e. the Exim Bank is to act as a lender of last resort and is only to consider those applications which have been rejected by the private financial institutions. Any loans granted by the Exim Bank must offer a reasonable assurance of repayment.

The Export-Import Bank Act of 1945 (which was amended on January 4, 1975) specifically prohibits the Bank from participating in granting credit to a Communist country unless the President determines that it is in the best interest of the U.S.A. Further, the Bank may not have any dealings with those nations which engage in armed conflict with the Armed Forces of the U.S.A.

The governing Act also requires that all U.S. exports, supported by the activities of the Exim Bank, shall be transported in American vessels unless the U.S. Maritime Commission certifies that it is impossible to meet this condition. If the exporter is unable to meet this requirement and obtains the U.S. Maritime Commission's approval, the goods may be
shipped in the most convenient manner.

The Act specifies that the Bank shall remain in existence until June 30, 1978, at which time the Bank's activities must be reviewed by Congress. In the past Congress has readily approved the renewal of the Bank's governing Act for an additional four year period.

The Act also specifies that the maximum amount of loans, guarantees, and insurance that the Bank may have outstanding at any one time shall not be greater than $25 billion. While 100% of all loans are taken into account when calculating this ceiling, only 25% of any outstanding guarantees and insurance policies are included. The Bank may, therefore, have a maximum outstanding liability of $40 billion.

The Act and its ten appendices appear to be all-encompassing and include a conflict of interest clause for the guidance of directors, officers, agents and employees of the Bank; a section requiring the Bank to designate a specific officer to report to the President of the Bank on all matters concerning small businesses; a section specifying the annual salaries of the President, the First Vice-President and the three other directors of the Bank; and innumerable sections describing interests or parties with whom the Bank may not enter into contracts. For example, the Exim Bank is expressly prohibited by Section 409 of Appendix X from extending credit to any nonmarket economy which denies its citizens the right or opportunity to join permanently through emigration, a very close relative in the United States.
II. SERVICES PROVIDED BY EXIM BANK

The promotion of U.S. exports is assisted in four different ways by the Exim Bank. The methods used by the Bank to accomplish its objectives are:

1) short and medium term export credit risks are underwritten in conjunction with the Foreign Credit Insurance Association

2) direct and indirect long term credit is granted to overseas projects which require financing assistance. The projects must use U.S. made capital equipment

3) guarantees are issued to commercial banks and other financial institutions which provide medium term export credit

4) lines of credit are granted foreign governments to enable the small foreign business to gain access to the capital goods produced by American industry

Prior to 1962, the Exim Bank did not provide any type of export credit insurance. At that time, the Foreign Credit Insurance Association (FCIA) was created as a partnership of some seventy stock and mutual insurance companies and the Exim Bank. The FCIA underwrites all commercial risks up to $150,000 per policy. Any commercial risks beyond that figure are underwritten jointly by the FCIA and the Exim Bank. The entire political risk is underwritten by the Exim Bank.

The insurance is available to any exporter resident in the U.S.A. who produces or manufactures goods in the United States to the extent that at least 50% of the value has been added by labour or
material exclusively of U.S. origin.\textsuperscript{5}

The political and commercial risks insured by the FCIA and the Exim Bank are similar to those outlined earlier in this study. The types of policies issued range from a short term political policy to a medium term comprehensive policy. The premiums for export insurance are determined by a method similar to that followed by the ECGD in the United Kingdom. The countries are assigned to one of four risk classes, with category A being the lowest risk. Table IV outlines the countries assigned to each risk category.

In its fifteen year history, the FCIA has been criticized for its relatively high premium schedule and for the length of time needed to process applications.\textsuperscript{6} As a result of such criticism, the FCIA was reorganized to make it more responsive to the needs of exporters. Twelve regional offices were established throughout the U.S.A. and the FCIA embarked on an education program designed to better acquaint the various insurance brokers located throughout the country with the facilities offered by the FCIA and the Exim Bank. Independent insurance brokers are authorized to issue insurance policies on behalf of FCIA. The Exim Bank and the FCIA have also developed a much closer working relationship. In effect, the U.S. now has a quasi-public type of body providing export credit insurance.

i) PARTICIPATION FINANCE

Prior to 1971, the Exim Bank's growth was constrained by the
**TABLE IV**


<table>
<thead>
<tr>
<th>A</th>
<th>B</th>
<th>C</th>
<th>D</th>
</tr>
</thead>
<tbody>
<tr>
<td>All countries in Western Europe</td>
<td>Mexico and most of the</td>
<td>Most Latin American Countries</td>
<td>Argentina</td>
</tr>
<tr>
<td>with the exception of Spain, Portugal, Finland, Yugoslavia and Turkey</td>
<td>Central American countries</td>
<td>Finland</td>
<td>Bolivia</td>
</tr>
<tr>
<td>Canada</td>
<td>Finland</td>
<td>India</td>
<td>Brazil</td>
</tr>
<tr>
<td>Japan</td>
<td>Pakistan</td>
<td>Portugal</td>
<td>Indonesia</td>
</tr>
<tr>
<td>Spain</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

federal government's annual budget. The unified federal budget concept required that all of Exim Bank's disbursements be designated as federal budgetary expenditures and as such they were required to be offset by budgetary receipts. Exim Bank's borrowings, even if made in the private market, were not considered to be budgetary receipts. From a budgetary standpoint, therefore, it was considered essential to minimize disbursements and as a result the Bank began to concentrate on participation financing instead of direct lending. In 1971, the Exim Bank's activities were removed from the unified Federal budget. Under the present system, the Exim Bank is only required to have Congress annually approve its administrative expenses.

While the direct loan program continues to provide much of the Bank's business, participation financing and the cooperative financing facility (CFF) are both rapidly increasing in importance. Both of these latter programs enable the Exim Bank to extend its funds further while drawing private funds into the market. In addition, the programs enable the exporter to obtain a blended interest rate on any export credit he obtains. The Exim Bank is prepared to lend its funds at a rate lower than that charged by the commercial banks. Hence the blending process reduces the effective rate which the borrower must pay. In addition, under the participation financing program the Exim Bank will provide a guarantee, covering a substantial portion of the political and commercial risks, to the financial institution.

The cooperative financing facility was introduced in late 1970 for the purpose of extending export credit to the thousands of potential purchasers of U.S. goods and services who either did not have the
financial resources to purchase the goods for cash, or who were unaware of how to arrange the financing necessary to enable them to purchase the goods.9

The Exim Bank, under the cooperative financing facility, has entered into agreements with nearly three hundred commercial banks located throughout the world.10 Under the terms of the agreement, each bank is designated as a cooperating institution (CI) and must agree to finance U.S. exports of goods and services according to the policy outlined by the Exim Bank. A potential purchaser of a U.S. export, whether he is in Zaire, Colombia or Yugoslavia, can approach the CI in his area to obtain a loan to purchase goods made in the U.S.A. The CI takes the application and establishes the creditworthiness of the customer. If the applicant’s credit standing is satisfactory, the application is approved by the CI and forwarded to the Exim Bank. The application is usually readily approved provided that the following conditions are met:

1) the purchaser must provide a minimum down payment of 10% of the contract price

2) the remaining balance is then eligible for financing. The exporter must agree to retain at least 10% of this eligible amount for his own account. He may, of course, arrange an operating credit through his own bank to finance this amount

3) the remaining balance, 81% of the original contract price, is then financed jointly by the CI and the Exim Bank. The Exim Bank will provide a maximum of one-half of the needed funds (40.5% of the total contract price)

4) the CI may charge the borrower its normal rate of interest on that portion of the loan it provides. However, on any funds provided by the Exim Bank
the CI may charge the borrower a rate 2.5% above the Exim Bank's rate to the CI.

5) the repayment terms must be those normally granted in international trade for that particular type of product. Loans which require a repayment period of greater than five years are acceptable to the Exim Bank.

6) the goods must, if possible, be shipped on a U.S. vessel.

The development of the CFF has proven to be a boon to both small U.S. exporters and to small unsophisticated purchasers throughout the world. In FY 1974, the fourth full year that the CFF was offered, a total of 1491 applications for a total of $207.7 million were approved. The contracts ranged in size from $350 to cover the purchase of an industrial food machine by the Royal Cliff Beach Hotel in Thailand to $1,400,000 to cover the sale of aircraft to the New Zealand National Airways. The mean size of the contract was $139,000. The products exported included spare parts for shrimp trawlers, air conditioners, trucks, sewing machines, and paper cup machines. The terms of repayment ranged from 1-7 years exclusive of implied grace periods.

Table V provides a breakdown of the purchasers of these relatively small American exports. The importers have been grouped into their respective countries. The table includes all exports under the CFF and relending facilities of the Exim Bank for the FY 1974. The analysis shows that only 7.9% by number and 13.1% by dollar volume of this group of exports are being purchased by residents of developed nations. By far, the largest regional importers of this group of products were the developing nations of Central and South America.
TABLE V

LOANS GRANTED UNDER THE EXIM BANK'S CFF AND RELENDING FACILITY
(All currency figures are expressed in millions of U.S. dollars)

Country where the purchaser was resident

<table>
<thead>
<tr>
<th>DEVELOPED NATIONS</th>
<th>NUMBER</th>
<th>AMOUNT IN MILLIONS OF U.S. DOLLARS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>12</td>
<td>2.1</td>
</tr>
<tr>
<td>Austria</td>
<td>2</td>
<td>0.4</td>
</tr>
<tr>
<td>Belgium</td>
<td>7</td>
<td>1.8</td>
</tr>
<tr>
<td>Canada</td>
<td>11</td>
<td>2.7</td>
</tr>
<tr>
<td>Denmark</td>
<td>3</td>
<td>0.2</td>
</tr>
<tr>
<td>Finland</td>
<td>6</td>
<td>2.4</td>
</tr>
<tr>
<td>France</td>
<td>21</td>
<td>5.4</td>
</tr>
<tr>
<td>Germany</td>
<td>5</td>
<td>0.8</td>
</tr>
<tr>
<td>Ireland</td>
<td>2</td>
<td>0.5</td>
</tr>
<tr>
<td>Italy</td>
<td>1</td>
<td>0.3</td>
</tr>
<tr>
<td>Japan</td>
<td>28</td>
<td>4.3</td>
</tr>
<tr>
<td>Netherlands</td>
<td>2</td>
<td>1.6</td>
</tr>
<tr>
<td>New Zealand</td>
<td>6</td>
<td>1.6</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>17</td>
<td>3.8</td>
</tr>
<tr>
<td>Total</td>
<td>123</td>
<td>27.9</td>
</tr>
</tbody>
</table>

II DEVELOPING NATIONS

A. CENTRAL AND SOUTH AMERICA

<table>
<thead>
<tr>
<th>Country</th>
<th>NUMBER</th>
<th>AMOUNT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brazil</td>
<td>680</td>
<td>89.8</td>
</tr>
<tr>
<td>Chile</td>
<td>1</td>
<td>0.5</td>
</tr>
<tr>
<td>Colombia</td>
<td>9</td>
<td>1.3</td>
</tr>
<tr>
<td>Costa Rica</td>
<td>21</td>
<td>1.4</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>2</td>
<td>0.5</td>
</tr>
<tr>
<td>Ecuador</td>
<td>2</td>
<td>0.7</td>
</tr>
<tr>
<td>El Salvador</td>
<td>7</td>
<td>0.4</td>
</tr>
<tr>
<td>Honduras</td>
<td>49</td>
<td>1.6</td>
</tr>
<tr>
<td>Mexico</td>
<td>66</td>
<td>7.5</td>
</tr>
<tr>
<td>Panama</td>
<td>15</td>
<td>2.1</td>
</tr>
<tr>
<td>Peru</td>
<td>2</td>
<td>0.3</td>
</tr>
<tr>
<td>Venezuela</td>
<td>9</td>
<td>2.2</td>
</tr>
<tr>
<td>Virgin Islands</td>
<td>1</td>
<td>0.1</td>
</tr>
<tr>
<td>Total</td>
<td>864</td>
<td>108.4</td>
</tr>
</tbody>
</table>
TABLE V CONT'D

Country where the purchaser was resident

<table>
<thead>
<tr>
<th>Country</th>
<th>Number</th>
<th>Amount in Millions of U.S. Dollars</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>B. ASIA</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taiwan</td>
<td>103</td>
<td>13.8</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>4</td>
<td>0.6</td>
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<tr>
<td>Korea</td>
<td>190</td>
<td>22.5</td>
</tr>
<tr>
<td>Pakistan</td>
<td>1</td>
<td>0.2</td>
</tr>
<tr>
<td>Philippines</td>
<td>14</td>
<td>1.9</td>
</tr>
<tr>
<td>Singapore</td>
<td>6</td>
<td>1.5</td>
</tr>
<tr>
<td>Thailand</td>
<td>69</td>
<td>4.2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>387</td>
<td>44.7</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>C. THE MIDDLE EAST</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Iran</td>
<td>34</td>
<td>4.8</td>
</tr>
<tr>
<td>Israel</td>
<td>84</td>
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<td></td>
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<tr>
<td><strong>F. NOT ELSEWHERE CLASSIFIED</strong></td>
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TABLE V CONT'D

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<th>%</th>
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<td>17.1</td>
<td>8.0</td>
</tr>
<tr>
<td>LDCs Europe</td>
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<td>3.4</td>
<td>11.4</td>
<td>5.4</td>
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<td>LDCs Africa</td>
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<td>Other LDCs</td>
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<tr>
<td><strong>Total</strong></td>
<td>1563</td>
<td>100%</td>
<td>212.6</td>
<td>100%</td>
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</table>

Brazil, with 680 loans for a total of $89.8 million was the largest individual importer.

The success of cooperative financing facility clearly indicates that there is a world wide demand for such a service. The purchasers of U.S. exports are utilizing the financing provided jointly by their local financial institutions and by the Exim Bank. The relatively small U.S. exporter also appears to be benefitting from this activity. The facility must have some merit when one considers that a food machine costing less than $800 can be produced in the United States, sold to a hotel in Thailand and be financed jointly by the Thai bank and the Exim Bank. The fact that nearly three hundred banks are now designated as cooperating institutions indicates that they are also finding the facility attractive. The five big Canadian banks and the Bank of British Columbia are designated as cooperating institutions. In the FY 1974, they granted loans totalling just under $1 million to cover the importation of American goods into Canada.  

In addition to the cooperative finance facility, the Exim Bank also offers a wide array of direct loan and financial guarantee programs. Under the Commercial Bank Exporter Guarantee Program for instance, the Exim Bank enters into a master guarantee agreement with each bank, which not only specifies the terms and conditions of the protection offered by the Exim Bank guarantee, but it also grants the commercial bank a discretionary limit of approval. Under this discretionary limit the commercial bank may commit Exim Bank to the issuance of guarantees within specified limits without the prior approval of the Exim Bank. The commercial bank retains a portion of the fee paid
by the exporter to compensate it for the work involved in processing the
application.  

The guarantee agreement usually requires that the purchaser
make a minimum down payment of 10% of the contract price, with the
balance payable, in equal installments, as called for in a promissory
note. The exporter must agree to carry at least 10% of the financed
portion. The remainder of the contract price (81%) is provided by the
commercial bank on a non-recourse basis. Under the comprehensive
guarantee plan, the commercial bank agrees to accept 100% of all commercial
risks on the early installments of the loan. Early installments are
defined as those which occur within the first half of any contract with
a maturity of less than three years or those installments which occur
within the first eighteen months of any contract with a term exceeding
three years. Exim Bank assumes the commercial risk on the later
installments and, of course, assumes the political risk on all
installments.  

The Exim Bank's fees for issuing this type of guarantee vary
according to the length of the credit period, the credit worthiness of
both the purchaser and his country of residence and the amount of
coverage provided. A rating system similar to the one used for insurance
purposes is used. The guarantee fee for a one year credit to a
purchaser in the lowest risk category is less than $1/3. The guarantee
fee for a three year credit to a purchaser in the D category is
approximately 5% of the guarantee's value. These fees are one time
charges and not annual interest charges.
The Exim Bank recently introduced a lease guarantee facility. Under this type of guarantee the Bank agrees to provide comprehensive coverage for both commercial and political risks, provided the lease occurs as the result of the export of U.S. equipment. The Exim Bank charges an annual fee ranging from 0.5 – 0.75% on the estimated average outstanding liability of the following year.\textsuperscript{17}

The Exim Bank is also prepared to guarantee loans granted to the foreign purchaser of used American equipment. In issuing its guarantee the Exim Bank considers such factors as the condition and age of the equipment; the method used to determine the value of the equipment; and whether the vendor is going to purchase new U.S. made equipment to replace the equipment being sold.\textsuperscript{18}

The Exim Bank is prepared to issue its guarantee to both domestic and foreign financial institutions.

Both the co-operative financing facility and the commercial bank exporter guarantee program offer a number of advantages over the direct loan type of program. In the former cases neither the supplier nor the purchaser deals directly with the Exim Bank. They approach their local bank, where they are known, and submit their application. Their local bank does most of the administrative work involved in processing the application. When the local bank processes the application, the turnaround time can be significantly less than if the application is forwarded to the central office of the Exim Bank for processing. Turnaround time is defined to be the time elapsed from the date of submission of the application to the date that the applicant is notified of approval or rejection.
The turnaround time will be especially low where the local bank is operating under the discretionary limit granted it by the Exim Bank.

This type of participation financing also reduces the strain on the Exim Bank's financial resources. It stretches the Bank's limited resources by reducing the volume of direct loans. In addition, only 25% of the outstanding guarantees are charged against the Exim Bank's lending authority.

ii) DIRECT LENDING

The Exim Bank has been successful in extending the principle of participation financing to the field of direct loans. The Bank's current policy is to provide less than 50% of the funds needed to finance the export of American capital goods. It is, however, prepared to extend its guarantee to a financial institution which provides part of the funds required by the importer. The joint financing agreements entered into by the Exim Bank and the commercial banks usually provide that any funds advanced the commercial bank will be repaid within five years. Repayment on any funds provided by the Exim Bank will commence after the commercial bank's loan is retired.

In certain cases the Exim Bank prefers to grant direct loans to the purchaser. If, for example, the contract is too large for one financial institution or a group of institutions to handle the Exim Bank will participate in the project. In some cases it is necessary to lower the overall interest rate to meet international competition. The blending of Exim Bank and commercial bank funds achieves this purpose. On occasion the Exim Bank prefers to be in direct contact
with the borrower.

The Exim Bank has achieved some success in reducing the volume of direct loan support provided to American exports. In FY 1973 over 44% of the export value of the goods financed under the Bank's direct loan program was provided by the Exim Bank. In FY 1975, the comparable figure is slightly less than 38%.

In an effort to speed up the processing of direct loan applications the Bank introduced a preliminary commitment facility. Under this plan, the Bank is prepared to provide a commitment to finance the sale of a certain project or of specified goods at a very early stage. The application may be submitted by the prospective borrower, the U.S. supplier or a participating financial institution, and must include details of the proposed project, current financial information on the borrower, appropriate engineering and marketing data to demonstrate the feasibility of the project and relevant information about international competition.

The American exporter has made good use of this facility. As early as 1971 the Exim Bank reported that applications for preliminary commitments were being received at the rate of $750 million per month. At that time approximately 13% of the applications received by the Bank were either denied for credit and technical reasons or cancelled.

iii) DISCOUNT LOAN PROGRAM

In 1966 in an effort to reduce the competition for bank credit in times of monetary restraint, the Exim Bank introduced a discount loan program. Even in tight money situations government authorities
try to ensure that the level of exports is maintained. In order to increase the exporter's ability to obtain the necessary credit when the banks are in a tight liquidity situation the Exim Bank introduced its discount loan program.

Exim normally agrees to purchase the debt obligations from the bank at a rate $0.5-1.0\%$ below the weighted average interest yield of the bill.\(^22\) The yield to the commercial bank may not be less than the applicant bank's prime lending rate. To be eligible for this program the loan must have a term of greater than one year and the commercial bank must state prior to granting the loan that it is unable to provide the necessary funds unless the loan qualifies under the discount loan facility. It is imperative that all loans in this category must have the approval of the Exim Bank prior to being granted. The term of the loan granted the discounting bank may not exceed the term of the original loan. The loan may be prepaid without penalty.\(^23\)

This program has aided the exporter in two ways. It provides additional liquidity for the commercial banks while at the same time it reduces the competition the exporter faces for a scarce resource, namely export credit. In addition, it helps reduce the rate of interest which is charged on export credit. There is no incentive for the lending institutions to charge the borrower a high rate of interest, for if he discounts the note with the Exim Bank he will be forced to pay $\frac{1}{2} - 1\%$ less than the rate charged the borrower.

iv) PRIVATE EXPORT FUNDING CORPORATION
The Private Export Funding Corporation (PEFCO) was established in 1971 by a number of private institutions involved in international trade and finance and the Exim Bank. PEFCO is controlled by the Exim Bank and is designed to mobilize previously untapped private capital sources of export credit. It has attempted to attract institutional funds from pension funds and insurance companies through the issuance of both short and long term obligations which are supported by export paper guaranteed by the Exim Bank. To date, it has met with limited success in achieving its objectives. In 1973, for example, it granted only one loan.

The marginal success of PEFCO indicates how difficult it is to attract private funds into the export credit field. Why should the institutional investor invest his funds in a relatively low yielding asset? An investor, for example, can obtain a higher yield with no foreign exchange or political risk by investing in the domestic mortgage market.

III THE WORLD BANK

To this point this chapter has shown that the Exim Bank offers a wide range of services to meet the needs of the American exporter. In order to identify the net benefits that the American economy receives from the Exim Bank's activities it is first necessary to analyze the exports which are being supported by the Bank's programs. Such an analysis will provide some insight into whether a Heckscher-Ohlin type of comparative advantage holds true for exports supported by
export finance programs. The analysis will also provide an indication of whether export credit is effective in altering trade patterns.

The World Bank's activities have been chosen as the standard against which to measure the exports of the industrialized nations. The World Bank is primarily concerned with helping the nations of the Third World develop their economies in order to effect a better distribution of the world's wealth. This Bank is not concerned with promoting certain types of exports from certain nations and, therefore, provides a good indication of the type of capital goods that are being demanded by the developing nations. A review of the World Bank's activities will be presented in this section to identify the types of capital projects that are being supported by the World Bank. The review will also indicate in which nations the projects are being undertaken.

The capital goods being produced by the United States and financed under the direct loan, CFF, or guarantee programs of the Exim Bank will be analyzed in approximately the same fashion in Section IV of this chapter.

Social and economic progress can not be achieved without growth in the field of agriculture, industry and education. In addition, the developing nations must strive to achieve a "more normal" population growth rate. An analysis of the problems facing developing nations in the areas of agriculture, education and population is beyond the scope of this study. The World Bank's efforts in fostering the development of adequate infrastructures on which industrial sectors can be developed is of concern to this study. The term infrastructure can be
broken down into four main categories: transportation, electric power, telecommunications and water supply. A preliminary review of the financing activities of both the Exim Bank and the EDC indicates that few, if any, exports involving water supply systems are financed by these agencies. Therefore, only the other three infrastructure categories and the development of industrial projects will be reviewed in this section.

i) TRANSPORTATION

The demand for transportation is a derived demand depending on the volume of commodities carried and on the benefits attached to personal travel. The distance the commodity or the people are to travel must also be considered. In the developing nations the movement of bulky low value agricultural and primary products is assigned a high priority. A large percentage of the exports of LDCs are such products. Railroads are normally the most efficient and economic means of moving bulk traffic over intermediate or long distances. Some type of shipping vessel is also usually required to move the exports of the LDCs to their eventual markets. Ships are efficient at moving bulky commodities at a low cost per ton mile over great distances. Air transportation has the advantage of speed and is aimed at the movement of people and goods when time possesses a high value.

By the end of 1971, transportation equipment had become the largest single component of the World Bank's financing activity. It accounted for more than 30% of both lending volume and number of
applications. The developing nations of East Africa, India, Mexico, Pakistan, Spain and Yugoslavia were the primary areas where the projects were undertaken.

In the five year period ended December 31, 1976 the Bank forecast that $4.3 billion would be allocated to transportation projects in the developing nations. This figure implies a 90% increase in spending over the previous five year period. In the most recent five year period the World Bank's activities were concentrated on:

1) developing better feeder roads in the various regions of the developing world.
2) revitalizing decaying railways.
3) devoting more resources to the development of coastal and ocean shipping facilities. The problems for a nation arising from purchasing its own ships include the high capital cost as well as the high operating costs. The benefits include being able to conserve foreign exchange earnings and having an assured means of transportation for its exports. The LDCs must also carefully examine the problem of containerization. This labour saving device is being widely adopted by the developed nations but is of little value to the LDCs.
4) developing airport facilities and navigational aids for air transport. The World Bank does not normally provide funds to finance the purchase of large aircraft.

ii) ELECTRIC POWER

The developing nations investment in generating plants designed to produce electricity has been increasing at an annual rate
of 10% and this rate of growth is expected to continue in the future. A power generating system usually consists of an integrated network of generation, transmission and distribution facilities. Such projects are capital intensive and a very substantial part of the technology and the equipment must be imported from the industrialized nations.

Through 1971 this area had received the benefit of $5.3 billion of World Bank financing. The volume of funds allocated to this area in the five year period ending in 1976 is forecast to be $2.5 billion, or 24% above the actual figure for the previous five years.

The development of nuclear power generating facilities throughout the world has been steadily increasing. However, the development of nuclear power plants in the developing nations poses a number of problems. The capital costs of nuclear power plants are about one-third higher than conventional steam installations. The projects are ideally suited for use in relatively large systems and the problem of using the new technology for purposes other than those for which it was intended must all be carefully considered by both the supplier and the purchaser.

iii) INDUSTRIAL PROJECTS

Through industrialization a nation can generate an increased volume of manufactured goods, increased employment, improved balance of payments and greater efficiency and modernization throughout its economy. The World Bank has devoted 15% of its total financing
activity to this area. The importance of the Bank's activity is understated because it often participates with other financial intermediaries in financing industrial projects.

The World Bank's direct loans usually support relatively large projects, while its indirect loans are concentrated more on light and heavy manufacturers. The majority of the projects concentrate on producing goods which may be classified as substitutes for imports.

In the current five year period the World Bank proposes to increase its activity in this area by some two and a half times the $1.3 billion spent in 1967-1971. Its funds will be allocated to those projects requiring a large capital input, such as steel production facilities, fertilizer plants and forest production complexes. Of secondary importance will be smaller scale projects oriented towards the production of exports.

iv) TELECOMMUNICATIONS EQUIPMENT

Telecommunications equipment aids the economic development of a nation by providing an efficient means of communication for both industry and government. It also aids in the national movement of goods and services and increases the facilities provided for the growing tourist industry. The value of telecommunications facilities is shown by the unsatisfied demand which exists for telephones, radios and other types of telecommunication facilities. In 1970, the developing
nations had only 6.8% of total world telephones.  

By 1971 the World Bank had provided $600 million for the development and expansion of telecommunication facilities. While this area received the smallest amount of support from the World Bank, the importance of the development of such facilities must not be understated. A number of the developing nations, including Argentina, Brazil, Colombia, Venezuela, Iran and Egypt, are slowly developing their own production facilities. One of the key factors affecting the development of telecommunications facilities is the lack of standardization in the equipment produced by the different manufacturers. This factor virtually dictates that future expansion of the system must be undertaken by the initial supplier. The ability of the purchaser to consider the price, quality and finance factors is significantly reduced.  

The World Bank forecast its activity in this area will increase by 50% in the five year period ended December 31, 1976.

In concluding this review of the World Bank's activities in the field of development finance a few conclusions can be made. While all areas of development are important, the World Bank appears to be expressing some doubt about the need for large aircraft, modern bulk carrying water carriers and nuclear generating plants. The developing nations should be primarily concerned with building the infrastructure needed to develop their industrial sectors.

IV COMMODITIES SUPPORTED BY THE EXIM BANK'S PROGRAMS

Tables VI and VII provide better insight into the products
**TABLE VI**

**EXPORT-IMPORT BANK OF THE UNITED STATES**

**ANALYSIS OF CREDITS AUTHORIZED FROM JULY 1, 1973-JUNE 30, 1975**

**MILLIONS OF U.S. DOLLARS**

<table>
<thead>
<tr>
<th>EXPORTED COMMODITY / IMPORTER</th>
<th>DEVELOPED NATIONS</th>
<th>COMMAND ECONOMIES</th>
<th>DEVELOPING NATIONS</th>
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<td></td>
<td>AMOUNT</td>
<td>%</td>
<td>AMOUNT</td>
<td>%</td>
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<td>(29.5)</td>
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<td>(1.3)</td>
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<td>(16.5)</td>
<td>(3.5)</td>
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<td>573.9</td>
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<td>(1.3)</td>
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<td>472.3</td>
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**SOURCE:** Export-Import Bank, Annual Reports
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<th>COMMAND ECONOMIES</th>
<th>DEVELOPING NATIONS</th>
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<td>%</td>
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<td>(13.1)</td>
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<td>ALL OTHERS</td>
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<td>(36.9)</td>
<td>—</td>
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<td>TOTAL</td>
<td>1645.3</td>
<td>24.9</td>
<td>472.3</td>
<td>7.2</td>
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</tbody>
</table>

SOURCE: Export-Import Bank, Annual Reports
being financed by the Export-Import Bank. The exports being supported, in ranked order, are large scale industrial projects; large aircraft and the multitude of capital goods being financed under the cooperative financing facility. Nearly 60% of the financed exports were sold to developing nations, with the majority being located in Central and South America and Southeast Asia. In the two year period, the large number of developing nations in Africa imported approximately the same dollar volume of financed exports from the U.S.A. as did the small number of developing nations in Europe.

Table VI clearly shows the importance of aircraft in the Exim Bank's operations. In the two year period analyzed, nearly 25% of the exports supported by the Exim Bank's export credit facilities consisted of aircraft. Over 50% of those financed aircraft were sold to the relatively small number of developed nations. For the developed nations wide-bodied aircraft such as the Boeing 747 and Lockheed 1011, as well as the more conventional Boeing 727 and 737 models account for more than one-half of the total financed imports from the United States.

The analysis indicates that the developing nations are interested in purchasing all types of capital exports. During the two year period reviewed, the analysis also shows that large industrial projects, aircraft, nuclear power plants and mineral development projects were the main types of products imported from the United States. Aircraft equipment was the only group of capital exports in which the developing nations had less than 50% of the total market.

Table VI shows that telecommunications equipment and railroad equipment constitute two of the lesser groups of products which
are financed by the Exim Bank. One would also expect that U.S. exports of this type of product would be fairly substantial. International Trade Statistics indicate that in 1973 the United States was the third largest exporter of telecommunications equipment and the world's prime exporter of railway vehicles. In 1973 the U.S. exported $1.1 billion of telecommunications equipment and in the two year period ending June 30, 1975, the Exim Bank financed a total of $103.1 million of similar exports. It is difficult to explain this situation, especially when the World Bank states that developing nations have an insatiable demand for such products. It may be possible to explain this situation by carefully examining the products which make up SITC 724 to determine if these U.S. exports are being financed by other methods.

According to the International Trade Statistics published by the United Nations, total U.S. exports of machinery, transportation equipment and other manufactured goods (SITC revised 6, 7 and 8) in 1973 were $37.6 billion. Of this amount, $26.8 billion or 71.2% was exported to developed economies. Of the remaining $10.8 billion, $5.9 billion was exported to developing nations in central and South America and $2.8 billion was purchased by the LDCs in SE Asia. While these figures are not comparable to those presented in Tables VI and VII they do permit one to make some observations. In dealing with total U.S. exports of certain types of capital goods, the U.N. statistics indicate that nearly three-quarters of the total is exported to developed economies. On the other hand, when analyzing the capital
equipment exports financed by the Exim Bank, exactly the opposite results appear—nearly 68% of that group of exports are imported by the developing nations. Both sets of statistics do, however, indicate that the countries in Central and South America and SE Asia purchase the bulk of the U.S. manufactured equipment which is exported to developing nations.

The statistics support the argument that the public institutions which provide export credit must pay more attention to the needs of the developing nations. The attitude of officers in organizations such as the Exim Bank and the EDC who see their role as being solely one of promoting exports should be changed in the near future.

The analysis of the Exim Bank's activities indicates that one of the largest world exporters of capital equipment, the United States, exported $1.4 billion of aircraft and nuclear generating plants to the developing nations over a two year period. On the other hand, slightly more than $0.3 billion of telecommunications and railway equipment was exported to this same group of countries.

In theory, the activities of national credit granting agencies, such as the Exim Bank, should be closely coordinated with the activities of development finance agencies, such as the World Bank. There is a limit to the amount of debt developing countries can service and the harder the terms the lower the limit. Consider for example, that in 1969, one-half of the total external public debt of all the developing nations was owed by only eight countries. These eight countries, Argentina, Brazil, India, Indonesia, Iran, Mexico,
Pakistan and Turkey, include many of the best customers of the national credit granting agencies. These nations have depended heavily on export credit to finance their development and as a result, they may be vulnerable to debt service problems in the not too distant future.

The developed nations are constantly striving to at least maintain the same net annual outflow of exports. The fact that export credit is being repaid annually must not be overlooked. A study by the IMF pointed out that if a loan has a maturity of ten years and an interest rate of 6.5% then the gross flows will have to quadruple in twelve years to maintain a net annual outflow. The study goes on to point out that if the credit has a thirty year maturity and a 2.5% interest rate then the gross flows will only have to double by the twenty-first year to maintain the present net outflow. 37

The Pearson Commission pointed out that projects rejected by the World Bank Group on economic grounds have been subsequently financed by an export credit agency. 38 This lack of coordination and the ease with which export credit can be obtained point out one of the areas where national credit agencies should adopt more responsible attitudes. At present the financing is usually arranged by an overly optimistic civil servant, a politician concerned with his own position or an aggressive salesman who has little knowledge of the overall needs of the developing economy. The World Bank conducts extensive studies before it proceeds with a project and some way of coordinating their activities with those of the national credit granting agencies must be developed.

Recently the World Bank, the national credit granting agencies and various private financial institutions have formed consortia to undertake
major projects. If more of this type of international cooperation is not forthcoming, then the national credit agencies must either mix increased flows of export credit and development finance to ease the debt servicing burden of the developing nations, or they must be prepared to accept progressively more defaults in an increasing number of countries.

IV. CONCLUSIONS

American industry appears to be well served by the facilities offered by the Export Import Bank and the Foreign Credit Insurance Association. The Exim Bank has taken the initiative in developing new types of programs such as the cooperative financing facility, the discount loan program, the comprehensive export credit program and lease guarantee facility, all of which have proved to be most successful.

The Exim Bank is vitally concerned about the welfare of the small exporter and is the only national credit agency reviewed in this study which has a special officer charged with the responsibility for ensuring that the needs of the small businessman are adequately served by the Exim Bank. The success of the Bank in meeting the needs of the small exporter is probably best shown through the cooperative financing facility. In the fiscal year ended June 30, 1975 nearly 1,000 CFF loans for a total of $177.0 million were authorized. The average size of the loan was $181,000.

The Exim Bank's activities have not, however, escaped criticism. A survey of 36,000 exporters and 170 commercial banks was conducted by the Chamber of Commerce of the U.S.A. to look at the Bank's activities.
The commercial banks' most frequent criticisms of the Exim Bank were:

1) the discount loan facility should be more flexible

2) the FCIA is not adequately performing its function and should therefore, become a subsidiary of the Exim Bank.

In early 1975, the FCIA increased its insurance premiums by 50% to compensate for an increase in defaults. The size of the rate increase may provide support for the criticism of the FCIA.

The Machinery and Allied Products Institute reported that a survey of its members in the 1960's indicated that most members were of the opinion that other nations offered more favorable credit terms for financing exports. The members also expressed the belief that Exim "was not particularly interested in making loans under $100,000". This criticism was corrected with the introduction of CFF.

One of the biggest controversies concerning the Exim Bank erupted after the Bank agreed to grant the U.S.S.R. a credit of $289 million to enable it to purchase the equipment needed to develop a fertilizer plant, a trade centre, and truck factory. The attack on this type of loan was lead by Senator H. Jackson who believed the funds could be put to better use in the United States to meet the needs of domestic business. He was also critical of the fact that funds would be lent to the U.S.S.R. at a 6-7% interest rate while the U.S. firms had to pay 11 1/2% to borrow funds in the domestic market. The criticisms eventually lead to an amendment being reintroduced to the Exim Bank's governing act which once again prohibits the Exim Bank from granting
credit to the Soviet Union.

At least one of the large U.S. airlines has also been critical of the Bank's activities. Officers of Pan Am charged that foreign airlines received a competitive edge by purchasing U.S. made planes at Exim Bank subsidized interest rates.43

In total, the criticisms have not been major and indicate that various groups are interested in seeing the services provided by the Exim Bank improved.

The analysis of the exports supported by the Bank indicates that export credit is primarily used to support large scale industry which occupies an important role in the national economy. The aircraft manufacturing industry receives the bulk of the benefit of the Bank's financing activity. The industry would undoubtedly have difficulty in arranging sales of the new wide-bodied aircraft if it were unable to count on the financing provided by the Exim Bank. A slowdown in the aircraft industry can have devastating effects on the local economy, as witnessed by the reduction in activity in Boeing's Seattle plant in the late 1960's. The analysis also indicated that the financed products were exported to those nations where the U.S. already had strong trade ties.—i.e. Central and South America and SE Asia.
FOOTNOTES

CHAPTER III


11. The annual reports of the Export-Import Bank for 1971 and 1972 each provide a description of the Cooperative Financing Facility. The information is provided on pages 38 and 13 of the respective annual reports. The Export-Import Bank's publication *Exim Bank, How It Works*, 1975 on pages 7-8 provides a detailed description of CFF.

12. Details of all CFF loans including the name of the buyer, the purpose, rate and terms of the loan, and the name of the cooperating institution are provided in the Export-Import Bank's publication *Cumulative Records*, 1974, on pp. 95-172


34. Ibid, p. 204

35. Ibid, p.207


Canada is dependent upon international trade to maintain the high standard of living enjoyed by its citizens. Approximately one quarter of our economic activity occurs as a result of activity in the international market place. The relatively small size of our domestic market forces Canadian producers to depend on the export market to reach economic levels of production. In the Canadian manufacturing sector, primarily located in central Canada, producers of capital goods have found the international markets to be very competitive. All of the major trading nations are concerned with the promotion of exports. As outlined elsewhere in this study one of the methods nations have developed to reach this goal is by providing export credit insurance and export finance.

The sale of capital goods usually requires financing which is repayable over a period greater than five years. The chartered banks of Canada have been reluctant to provide such financing because their function, as they view it, is to provide short and medium term financing. The private insurance companies are reluctant to insure the commercial and political risks encountered in dealing in foreign countries. The Canadian exporter, therefore, has found it difficult
to compete in the international marketplace.

In an effort to facilitate and develop trade between Canada and other nations the Federal government in 1944 established the Export Credits Insurance Corporation. The main purpose of this Crown Corporation was to provide insurance for Canadian exporters who wanted to cover themselves against certain risks of non-payment for goods sold to buyers in foreign countries. In 1960 the ECIC's governing Act was amended to allow ECIC to provide long term financing for exported Canadian capital goods and related technical services. Over the years the mechanism used by the government and its agencies to promote exports has gradually changed from export credit insurance to the financing field. As a result of this changing emphasis, the Export Development Corporation was established by an act of Parliament on June 27, 1969.

The Export Development Corporation was "established for the purpose of facilitating and developing trade between Canada and other countries by means of the financial and other powers provided by the Export Development Act." EDC fulfills its function by providing:

1) Insurance for exporters against non-payment by foreign buyers. (export credit insurance)
2) Insurance for Canadian Investment against loss due to non-commercial credit risk. (foreign investment insurance)
3) Loans to foreign buyers of capital goods and major technical services for which extended credit is not available from regular commercial sources. (export credit or export finance).

1. EXPORT CREDIT INSURANCE

The export credit insurance provided by EDC insures the Canadian exporter against the various types of commercial and political
risks detailed previously in this study. The EDC has adopted an all-encompassing definition of risk which provides coverage for any cause which is outside the control of both the purchaser and the seller and which arises from events occurring outside Canada and the continental U.S.A. This interpretation of risk is somewhat different to that adopted by the FCIA. The American agency only provides coverage for those risks outlined in the insurance policy.

The maximum liability that EDC is permitted to assume, at any point in time, under all export credit insurance policies issued is $1.5 billion. This amount is divided equally between policies authorized by the Board of Directors of EDC and policies authorized by the Federal Government. On December 31, 1975, EDC's maximum contingent liability under all issued policies was $816.3 million. Since the Corporation insured $910.7 million of exports in the last fiscal year, it appears that the insurance policies have a relatively short term.

Table VIII indicates that less than three percent of total Canadian exports are being insured under the facilities offered by the EDC. The fact that nearly two-thirds of Canadian exports end up in the American economy undoubtedly explains why this insured figure is so small. The 3% Canadian figure can be compared for example with British figures which indicate that 25% of all United Kingdom exports are insured by the ECGD.

Export credit insurance is provided for a broad range of raw materials and products produced in the Canadian economy. Inedible fabricated materials are the major group of products insured and the largest single component in this category is wood, pulp, newsprint,
# TABLE VIII

COMMODITIES INSURED BY EXPORT DEVELOPMENT CORPORATION

## SELECTED YEARS

<table>
<thead>
<tr>
<th>COMMODITY</th>
<th>MILLIONS OF DOLLARS</th>
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<tr>
<td></td>
<td>AMOUNT</td>
</tr>
<tr>
<td>Live Animals</td>
<td>6.4</td>
</tr>
<tr>
<td>Food, Feed, Beverages and Tobacco</td>
<td>122.9</td>
</tr>
<tr>
<td>Crude Materials, Inedible</td>
<td>15.3</td>
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<tr>
<td>Fabricated Materials, Inedible</td>
<td>239.7</td>
</tr>
<tr>
<td>Services</td>
<td>6.5</td>
</tr>
<tr>
<td>End Products, Inedible of Which</td>
<td>170.8</td>
</tr>
<tr>
<td>Industrial Machinery</td>
<td>26.7</td>
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<tr>
<td>Communications Equipment</td>
<td>7.3</td>
</tr>
<tr>
<td>Aircraft</td>
<td>78.2</td>
</tr>
<tr>
<td>Automobiles and Parts</td>
<td>4.7</td>
</tr>
<tr>
<td>Farm Machinery</td>
<td>7.6</td>
</tr>
<tr>
<td>Electrical Equipment</td>
<td>8.4</td>
</tr>
<tr>
<td>Other End Products</td>
<td>37.9</td>
</tr>
<tr>
<td>TOTAL</td>
<td>561.6</td>
</tr>
</tbody>
</table>

Canadian Exports: 16820.0

Total Insured Exports as a % of Total Exports: 3.33

Total End Products Inedible as a % of Total Exports: 1.01

### SOURCE:
Export Development Corporation, *Annual Reports*
paper and other paper products, which in 1974 accounted for $319.6 million or 65.7% of total insured inedible fabricated materials. Steel products were the second largest component in this category with 19% of the total.

The inedible end products category consists of capital goods and consumer durables. Table VIII indicates that capital equipment exports comprise about 25% of total insured exports. Exported end products comprise less than 1% of total Canadian exports.

Export credit insurance, in theory, can be justified on the grounds that the exporter is unable to evaluate and therefore disinclined to assume the commercial and political risks of dealing in the international marketplace. However, when one considers that less than three percent of Canadian exports are being assisted by this type of insurance, the value of the service must be questioned. Further, nearly one-third of the insured exports in 1974 consisted of lumber and pulp and paper products. The Canadian forest industry consists of a small number of large-scale producers, such as MacMillan Bloedel Limited, Abitibi Paper Company Limited, Consolidated-Bathurst Limited, Domtar Limited and B.C. Forest Products Limited. It does not appear to be likely that a multinational corporation such as MacMillan Bloedel Ltd., with annual sales volume in excess of $1.3 billion, is not capable of evaluating and assuming the commercial and political risks of dealing in the world market. It is also unlikely that the insurance feature helps a corporation such as MacMillan Bloedel Ltd. obtain the necessary financing for its receivables.

In order to increase industrial output and to diversify its domestic economy, Canada should strive to produce goods in which
she has a comparative advantage. The products must be fully competitive in world markets. Table VIII indicates that less than 1% of Canadian exports consist of inedible end products supported by export credit insurance. The EDC's insurance facility therefore, appears to be of limited value in helping Canada develop a more diversified industrial sector.

II. FOREIGN INVESTMENT INSURANCE

In an attempt to match the facilities offered to nationals of other countries, the EDC developed the Foreign Investment Insurance program. Under this facility Canadian businessmen who invest abroad can obtain protection against the possibility of loss due to expropriation, armed conflict, or factors affecting their ability to repatriate earnings or capital. The program is also designed to encourage Canadian participation in joint ventures with foreign nationals.

The policies are issued for a maximum term of fifteen years and once issued can only be cancelled by the investor, and not by EDC, so long as the basic terms and conditions of the policy are adhered to. The insurance provides coverage for virtually any type of foreign investment. Equity, loans, management contracts and royalty and licencing agreements, are some examples of the type of investment that can be insured. The cost of the insurance is approximately 1% per annum.

The Canadian investor appears reluctant to make use of this type of facility. In the first four years that the EDC offered such insurance, only forty-five policies were issued. In FY 1975 the total number of outstanding policies increased by eleven to thirty-five while the value of investments insured increased by 57% to $68.4 million.
The facility can provide support for Canadian investors who enter joint ventures with the nationals of a developing country. The risks of expropriation and currency inconvertibility are high when dealing with some LDCs. Such risks can be eliminated through the use of foreign investment insurance which will protect the transfer of technology and managerial know-how. The EDC claims the facility provides a stimulus for Canada's foreign trade and undoubtedly hopes that the increased activity in 1975 signals a major breakthrough in the use of foreign investment insurance.\textsuperscript{3}

III. EXPORT FINANCE

Under Section 29 of the Act, E.D.C. may provide direct long term loans to foreign customers to finance the purchase of Canadian capital goods and technical services. The Corporation may also guarantee any such loans made by private financial institutions. Prior to 1973 the Corporation's board of directors was authorized to grant loans or guarantees subject to the proviso that the maximum amount outstanding at any point in time did not exceed $850 million. In 1973, this maximum ceiling was increased to $1500 million, and in 1974 was further increased to $4250 million. In addition to each of these ceilings EDC may also finance capital exports which are special situations considered to be in the national interest by the Minister of Industry, Trade, and Commerce. At present, the maximum additional liability that EDC is permitted to assume under loans directly authorized by the Federal Government is $850 million.

It appears the Corporation's ceilings are established on an ad hoc basis. A review of some of the minutes and evidence of the Standing Committee on Finance, Trade and Economic Affairs for 1973
failed to disclose the method used to determine the ceiling. The belief that EDC's ceilings are established on an ad hoc basis is supported by noting that EDC's total of notes receivable and undisbursed financing on December 31, 1972 was $841.0 million. Without an increase in their authorized ceiling the Corporation would have signed very few new agreements in 1973. The ceiling was subsequently increased to $1.5 billion. However, by the end of 1973, the Corporation was once again very close to the level permitted by the new legislation. On December 31, 1973 the total of notes receivable and undisbursed financing was $1240.2 million. In 1974 Parliament was once again requested to pass a bill increasing the authorized lending ceilings of the Corporation. At that time, in an obvious move to allow for future growth, the Corporation's finance ceiling was increased to $4.25 billion.

To qualify for a long term financing loan from EDC the transaction must be of a type and for an amount which justifies extended credit terms (i.e. beyond five years). The project must be financially and economically sound and the foreign borrower must be creditworthy. The transaction must provide employment and industrial benefits to Canada and in addition the transaction must have a Canadian material and labour content of not less than 80%. All goods and services must be exported from Canada.

Up until 1974, EDC had an unwritten policy of not considering any long term financing contracts which had a value of less than $1 million. This minimum requirement was removed in 1974 and now any capital equipment or service export transaction is eligible for EDC support so long as the transaction justifies extended credit terms.
in accordance with normal international practice.\textsuperscript{5}

The Corporation is primarily concerned with increasing Canada's exports but is hopeful that the financed project will also be of benefit to the recipient country. On occasion, EDC provides advice to the recipient country and may even try to ascertain where the proposed project rates on the host country's scale of priorities. The former president of EDC, H. T. Aitken, however, believes EDC's main purpose is to lend money to major capital projects abroad which make use of Canadian capital equipment. In his view the main purpose of EDC is to promote Canadian trade.\textsuperscript{6}

By providing long term financing EDC hopes to stimulate the Canadian manufacturing sector, thereby providing more jobs and more income for Canadians. EDC commissioned Statistics Canada to undertake a study to determine how many direct jobs are created when EDC finances a capital goods export. Statcan's study concluded that approximately 100 man-years of direct employment are created for each $1 million contract financed by EDC.\textsuperscript{7} In 1975, EDC signed financing agreements totalling $1135 million. Therefore, approximately 114,000 direct man-years of employment should have been created in the most recent fiscal year.

A Canadian exporter is responsible for bringing any proposed export sales which require financing to the attention of EDC. Once an exporter has found a prospective purchaser for his product he approaches EDC to ascertain if they would be willing to finance the sale. In order to evaluate the application EDC requires the exporter to provide detailed information about the project. An application
form for long term financing is included as Appendix II to this study.

Some of the information required in the application includes:

1) detailed financial information on the exporter's company for the last five years

2) detailed financial information on the borrower covering the last five years and including forecast projections for the next five years

3) detailed information about the project including timing, costs and the amount of financing required

4) details of the benefits accruing both to the importing country and to the Canadian economy.

It is unlikely that this type of information would be readily available to the exporter. It appears that the elapsed time from the date of the original inquiry until the final approval by the EDC's Board of Directors could be in the order of 3 - 4 months.

Once the application is approved, EDC signs a financing agreement with the borrower and then, on instructions from the borrower, EDC pays the funds to the Canadian exporter. A project can involve a multiplicity of suppliers. The purchaser must ensure that each Canadian exporter is aware of the fact that the contract is being financed by EDC. Each exporter must submit to the Corporation copies of all invoices for goods purchased from other major suppliers. A minimum purchase of approximately 1/10% of the value of the contract is necessary before the invoice is perused by EDC. The Technical and Financial Services Division of EDC then authenticates each invoice to verify the 80% Canadian content regulation.

The Canadian content requirement restricts the ability of the Canadian exporter to sell his goods in the world market. For example, International Hydrodynamics Company Ltd. (HYCO), a westcoast
firm, has successfully developed and marketed a type of submersible vessel which is used for various types of underwater surveys and recovery work. The product is uniquely Canadian in design, technology and manufacture. In 1975, HYCO financed the sale of a Pisces submersible through the Export Development Corporation. A loan of $1.1 million was granted the purchaser, Vickers Oceanics Limited of London, England. Prior to this contract, EDC had not financed the sale of any similar type of product. As a result, the checking of the Canadian content requirement was fairly involved. The Technical and Financial Services Division is located in Ottawa, while the manufacturer is located in North Vancouver, B.C. The distance between these two groups, coupled with the problems of dealing with a government bureaucracy, appear to have created barriers restricting the ability of this Canadian exporter to compete for world markets.

The vessel being produced by HYCO appears to be an ideal candidate to receive EDC support. The sale financed in 1975, however, represented the first contract which was directly financed by the EDC.

HYCO was established in 1964 by Canadian Investors. By September 30, 1974, 44.33% of the firm's outstanding stock was owned by the Peninsular and Oriental Steam Navigation Company, the large U.K. based shipping line. Perhaps if Crown Corporations like the Export Development Corporation and the Canada Development Corporation were more responsive to the needs of small Canadian businessmen, a larger percentage of the ownership of companies like HYCO would be retained by Canadian investors.

In the past four years EDC's lending ceiling has been increased from $1.3 billion to $5.1 billion. The annual total of
financing agreements signed by the EDC has increased dramatically. Table IX shows that the cumulative total of all contracts signed up to December 31, 1970 was $559.0 million. By the way of comparison, the total of financing agreements signed in the fiscal year ended December 31, 1975 was $1135.0 million. EDC expects its signings to grow at a 10-15% annual rate.\textsuperscript{9} The phenomenal growth in financing agreements is mainly attributed to the ability of the Canadian producers of capital goods and services to win international business.\textsuperscript{10} Some interesting questions have to be asked when one considers this dramatic growth rate—who are these successful exporters, what type of product are they exporting, does Canada appear to have any comparative advantages in manufacturing these products, who are the purchasers of these exports and how are the funds being provided to finance this type of activity?

IV. ANALYSIS OF LONG TERM FINANCING CONTRACTS

In attempting to formulate some answers to the aforementioned questions, all of the long term financing agreements of the EDC have been perused, the relevant academic literature has been reviewed and discussions have been held with the local officers of the Export Development Corporation.

The first stage in the analysis is to identify that group of products which are eligible for support under the EDC's financing facility. Canada's world trade patterns will be considered in order to establish a standard against which to compare the trade patterns of the financed exports. The latter will then be subdivided into the
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<tbody>
<tr>
<td>Agreements Signed</td>
<td>559.0</td>
<td>340.0</td>
<td>283.3</td>
<td>462.9</td>
<td>659.4</td>
<td>1135.0</td>
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<td>Cancellations and Disbursements to Canadian Exporters</td>
<td>418.7</td>
<td>123.9</td>
<td>216.8</td>
<td>224.7</td>
<td>356.3</td>
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<tr>
<td>Undisbursed Financing for Period</td>
<td>140.3</td>
<td>216.1</td>
<td>66.5</td>
<td>238.2</td>
<td>303.1</td>
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<tr>
<td>Cumulative Undisbursed Financing</td>
<td>140.3</td>
<td>356.4</td>
<td>422.9</td>
<td>661.1</td>
<td>964.2</td>
<td>1461.8</td>
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**SOURCE:** Export Development Corporation, *Annual Reports*
categories used earlier in this study when discussing the activities of the Exim Bank and the World Bank. The importance of the various groups of exports to the Canadian economy will then be analyzed. The trade patterns of the financed exports will also be presented. This section will conclude by analyzing the structure of the Canadian exporters and the foreign importers.

Table I of Appendix I indicates that Canada's exports have increased by more than 250% in the six year period ending December 31, 1974. At first glance this growth rate may appear to be totally acceptable. However, it is also worth considering that the following growth rates were recorded in the same six year period:

1) total world exports increased by 351%
2) exports of developed nations increased by 322%
3) exports of the members of the EEC increased by 332%
4) Japanese exports increased by 428%
5) American exports increased by 284%.

All of these figures indicate that Canada, despite the EDC's increased activity, is losing its share of world markets. In that six year period, Japanese exports increased from approximately the same level as Canadian exports to a figure over $20 billion greater than Canada's. In 1968, the exports of all of the developing nations in Central and South America were $1.2 billion greater than Canadian exports. Six years later they were $15.8 billion greater. Part of this substantial gain can be accounted for by the increases in the price of petroleum. All of these comparisons do, however, indicate that Canada is not fully competitive in the international markets.

Approximately 90% of Canadian exports go to developed nations, with the United States being the major importer of Canadian goods.
Canada's exports to the developing nations are less than $3 billion per year. The major share of this market is occupied by the developing nations of Central and South America. Table X indicates that these trade patterns have not changed dramatically in the 1970's.

Table XI outlines the true annual volume of Canadian exports which are eligible for financing under the provisions of the export credit facility of EDC. While all Canadian capital goods are eligible for such financing, certain exports to the United States should be deducted to arrive at a more meaningful figure. Exports of motor vehicles and parts produced under the Canada-U.S. Auto Pact should be excluded because they are not financed by the EDC. Further, in the fourteen year period ending December 31, 1974, less than 1% of financing agreements and guarantees signed by the EDC involved purchasers in the United States. It, therefore, appears to be in order to exclude all capital equipment exports to the United States.

Table XI indicates that eligible capital equipment exports have increased from $779 million in 1968 to $1.848 billion in 1974, a 237% increase. This growth is comparable to that recorded for total Canadian exports. In that same six year period, EDC's annual signings of financing agreements increased from approximately $22 million to $659 million. These figures indicate that an increasing volume of Canada's eligible capital equipment exports are relying on EDC to provide the financing. In 1968, only 2.8% of eligible exports were supported by EDC export credit, while by 1974 the figure had increased to 35.7%.

All of the signed financing agreements of EDC from 1961-1974 were examined to develop a better understanding of the types
<table>
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<tr>
<th>EXPORTED TO</th>
<th>1970</th>
<th>1972</th>
<th>1974</th>
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<tbody>
<tr>
<td></td>
<td>AMOUNT</td>
<td>AMOUNT</td>
<td>AMOUNT</td>
</tr>
<tr>
<td></td>
<td>%</td>
<td>%</td>
<td>%</td>
</tr>
<tr>
<td>THE WORLD</td>
<td>16,184.9</td>
<td>20,177.8</td>
<td>32,783.4</td>
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<tr>
<td>DEVELOPED ECONOMIES</td>
<td>14,651.3</td>
<td>18,182.3</td>
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<tr>
<td></td>
<td>90.5</td>
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<td></td>
<td>65.4</td>
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<td></td>
<td>18.7</td>
<td>14.4</td>
<td>14.8</td>
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<td>235.2</td>
<td>197.6</td>
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<tr>
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<td>1.5</td>
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<td>Rounding</td>
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<tr>
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<td>0.7</td>
<td>1.0</td>
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<td>C. &amp; S. America</td>
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<td>756.4</td>
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<td></td>
<td>4.3</td>
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<td>393.2</td>
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<td>0.7</td>
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<td>3.1</td>
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<tr>
<td>CENTRALLY PLANNED</td>
<td>272.8</td>
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<td>657.3</td>
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<td>ECONOMIES</td>
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<td>TOTAL</td>
<td>16,184.9</td>
<td>20,177.8</td>
<td>32,783.4</td>
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<td>6260</td>
<td>8224</td>
<td>10826</td>
<td>30119</td>
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<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>MOTOR VEHICLES AND PARTS</td>
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<td>3290</td>
<td>4484</td>
<td>5373</td>
<td>15648</td>
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<td>239</td>
<td>313</td>
<td>320</td>
<td>1158</td>
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<td>OTHER PRODUCTS</td>
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<td>1653</td>
<td>2109</td>
<td>3285</td>
<td>8290</td>
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<tr>
<td>2. EXPORTS PRIMARILY ELIGIBLE FOR EDC SUPPORT</td>
<td>779</td>
<td>1078</td>
<td>1318</td>
<td>1848</td>
<td>5023</td>
</tr>
<tr>
<td>LESS EXPORTS CONSISTING OF:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MOTOR VEHICLES AND PARTS</td>
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<td>247</td>
<td>230</td>
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<td>976</td>
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<td>AIRCRAFT AND PARTS</td>
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<td>140</td>
<td>155</td>
<td>113</td>
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<td>OTHER PRODUCTS</td>
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<td>1432</td>
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<td>16</td>
<td>(1)</td>
<td>21</td>
<td>38</td>
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<td>3. BALANCE</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. TOTAL EXPORTS ALL COMMODITIES</td>
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<td>16185</td>
<td>20178</td>
<td>32783</td>
<td>82770</td>
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<td>40.8</td>
<td>33.0</td>
<td>36.4</td>
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<td>2. AS A % OF TOTAL EXPORTS</td>
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<td>6.7</td>
<td>6.5</td>
<td>5.6</td>
<td>6.1</td>
</tr>
<tr>
<td>5. AS A % OF 2</td>
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<td>9.3</td>
<td>21.5</td>
<td>35.7</td>
<td>21.2</td>
</tr>
<tr>
<td>5. EDC FINANCING AGREEMENTS SIGNED</td>
<td>22(E)</td>
<td>100</td>
<td>283</td>
<td>659</td>
<td>1064</td>
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</tbody>
</table>


(E) = estimate
of products being supported by the EDC and to determine if the same trade pattern holds for this select group of exports as for total exports. The results of this analysis, presented in Table XII and Table XIII, indicate that ships, industrial projects with a value of greater than $2 million and commercial electric generating plants are the three main groups of products. The analysis also indicates that over 75% of this group of financed capital goods are exported to the developing nations. This market distribution is exactly the opposite of that recorded for total Canadian exports.

The developing nations in Central and South America received 53% of all the financed goods exported to developing nations. In the financed goods category, exports to the LDCs in Africa are nearly three times as large as the financed exports to the LDCs in Asia. These latter rankings are once again just the reverse of the rankings for total Canadian exports.

The analysis shows that exports to the developed nations consisted primarily of ships and electric power plants. The developing nations, on the other hand, sought all types of capital goods, but were primarily interested in conventional power generating plants and large scale industrial projects. It is not really accurate to make the assumption that because these types of products were being exported to the developing nations they represent the types of products desired by the LDCs. An eager Canadian salesman may have sold a country a project which did not rank high on its priority list.

Ships were the only group of products in which the developing nations were not the major recipients.

Table XII indicates that the activities of the EDC follow
<table>
<thead>
<tr>
<th>EXPORTED COMODITY / IMPORTER</th>
<th>DEVELOPED NATIONS</th>
<th>COMMAND ECONOMIES</th>
<th>DEVELOPING NATIONS</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>AMOUNT</td>
<td>%</td>
<td>AMOUNT</td>
<td>%</td>
</tr>
<tr>
<td>TRANSPORTATION EQUIPMENT</td>
<td>(201.5)</td>
<td>(71.3)</td>
<td>(79.9)</td>
<td>(62.3)</td>
</tr>
<tr>
<td>Aircraft</td>
<td>22.3</td>
<td>7.9</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Railroads</td>
<td>10.4</td>
<td>3.7</td>
<td>55.9</td>
<td>43.6</td>
</tr>
<tr>
<td>Ships</td>
<td>168.8</td>
<td>59.7</td>
<td>24.0</td>
<td>18.7</td>
</tr>
<tr>
<td>ELECTRIC POWER PROJECTS</td>
<td>(44.3)</td>
<td>(15.6)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Conventional Generating</td>
<td>44.3</td>
<td>15.6</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Nuclear Generating</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>INDUSTRIAL PROJECTS</td>
<td>(37.2)</td>
<td>(13.1)</td>
<td>(44.6)</td>
<td>(34.8)</td>
</tr>
<tr>
<td>Greater than $2 Million</td>
<td>37.2</td>
<td>13.1</td>
<td>42.5</td>
<td>33.2</td>
</tr>
<tr>
<td>Less than $2 Million</td>
<td>—</td>
<td>—</td>
<td>2.1</td>
<td>1.6</td>
</tr>
<tr>
<td>Mineral Development</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TELECOMMUNICATIONS</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>RELENDING FACILITY</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>ALL OTHERS</td>
<td>—</td>
<td>—</td>
<td>(3.7)</td>
<td>(2.9)</td>
</tr>
<tr>
<td>TOTAL</td>
<td>283.0</td>
<td>100.0</td>
<td>128.2</td>
<td>100.0</td>
</tr>
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</table>

SOURCE: Export Development Corporation, Annual Reports
<table>
<thead>
<tr>
<th>EXPORTED COMMODITY / IMPORTER</th>
<th>DEVELOPED NATIONS</th>
<th>COMMAND ECONOMIES</th>
<th>DEVELOPING NATIONS</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>AMOUNT</td>
<td>%</td>
<td>AMOUNT</td>
<td>%</td>
</tr>
<tr>
<td>TRANSPORTATION EQUIPMENT</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aircraft</td>
<td>22.3</td>
<td>14.5</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>Railroads</td>
<td>10.4</td>
<td>7.5</td>
<td>55.9</td>
<td>40.3</td>
</tr>
<tr>
<td>Ships</td>
<td>168.8</td>
<td>48.6</td>
<td>24.0</td>
<td>6.9</td>
</tr>
<tr>
<td>ELECTRIC POWER PROJECTS</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Conventional Generating</td>
<td>44.3</td>
<td>15.7</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>Nuclear Generating</td>
<td>--</td>
<td>--</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>INDUSTRIAL PROJECTS</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Greater than $2 Million</td>
<td>37.2</td>
<td>11.9</td>
<td>42.5</td>
<td>13.6</td>
</tr>
<tr>
<td>Less than $2 Million</td>
<td>--</td>
<td>2.1</td>
<td>23.9</td>
<td>6.7</td>
</tr>
<tr>
<td>Mineral Development</td>
<td>--</td>
<td>--</td>
<td>55.8</td>
<td>100.0</td>
</tr>
<tr>
<td>TELECOMMUNICATIONS</td>
<td>--</td>
<td>--</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>RELENDING FACILITY</td>
<td>--</td>
<td>--</td>
<td>(185.0)</td>
<td>(100.0)</td>
</tr>
<tr>
<td>ALL OTHERS NOT ELSEWHERE CLASSIFIED</td>
<td>--</td>
<td>(3.7)</td>
<td>(94.9)</td>
<td>(0.2)</td>
</tr>
<tr>
<td>TOTAL</td>
<td>263.0</td>
<td>16.2</td>
<td>128.2</td>
<td>7.3</td>
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</tbody>
</table>

SOURCE: Export Development Corporation, *Annual Reports*
the activities of the World Bank more closely than do the activities of the Export-Import Bank. Despite the fact that the EDC claims not to be involved in a development finance role, the structure of its market indicates that development finance should play a larger part in its thinking. The fact that EDC supported a greater proportion of exports of railroad equipment and telecommunications equipment than did the Exim Bank might suggest that the officers of the EDC are more cognizant of the needs of the developing countries. It could also indicate that the Canadian producers of this type of equipment have been more successful in selling it than have their American counterparts. Table XV later in this chapter will show that the major Canadian exporters of railroad and telecommunications equipment are either subsidiaries of American corporations or are controlled, to some degree, by American investors. It, therefore, appears that the American manufacturers of railroad and telecommunication equipment service the world market by exporting through their Canadian subsidiaries.

How important are these financed capital equipment exports to the Canadian economy? The benefits include increased employment, increased taxes for all levels of government, the development of a more efficient Canadian industrial sector and the opportunity for Canadian companies to develop products with a high technological component. The readily identifiable costs include a possible misallocation of Canadian productive resources, including labour and scarce natural resources, as well as a misallocation of capital raised in either the domestic or the offshore capital markets.

Using Statistics Canada's estimate that 100 man-years of
### TABLE XIV

**SELECTED CANADIAN EXPORTS BY COMMODITY FOR YEARS 1972-74**

**MILLIONS OF DOLLARS**

<table>
<thead>
<tr>
<th>COMMODITY / IMPORTER</th>
<th>U.S.A.</th>
<th>OTHER DEV'D NATIONS</th>
<th>ALL OTHER NATIONS</th>
<th>TOTAL</th>
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</thead>
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<tr>
<td>AIRCRAFT</td>
<td>965.6</td>
<td>171.5</td>
<td>186.3</td>
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<tr>
<td>Complete With Engines</td>
<td>17.5</td>
<td>58.4</td>
<td>110.1</td>
<td>186.0</td>
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<tr>
<td>Engines And Parts</td>
<td>948.1</td>
<td>113.1</td>
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<td>RAILROADS</td>
<td>257.6</td>
<td>120.8</td>
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<td>555.1</td>
</tr>
<tr>
<td>Engines and Rolling Stock</td>
<td>46.8</td>
<td>--</td>
<td>140.3</td>
<td>187.1</td>
</tr>
<tr>
<td>Track Material</td>
<td>24.6</td>
<td>--</td>
<td>23.6</td>
<td>48.2</td>
</tr>
<tr>
<td>SHIPS, BOATS AND PARTS</td>
<td>186.2</td>
<td>120.8</td>
<td>12.8</td>
<td>319.8</td>
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<tr>
<td>TELECOMMUNICATIONS EQUIPMENT</td>
<td>442.6</td>
<td>103.3</td>
<td>231.5</td>
<td>777.4</td>
</tr>
<tr>
<td>PULP AND PAPER INDUSTRIAL EQUIPMENT</td>
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<td>--</td>
<td>44.8</td>
<td>69.4</td>
</tr>
<tr>
<td>NAVIGATIONAL EQUIPMENT AND PARTS</td>
<td>96.4</td>
<td>36.5</td>
<td>14.4</td>
<td>147.3</td>
</tr>
</tbody>
</table>

I direct employment are created for each $1 million contract financed by the EDC, we can conclude that in 1974 when $659 million of contracts were signed, approximately 66,000 direct man-years of employment were attributable to the EDC. The total Canadian employed labour force in December 1974 was 9.1 million workers. Canadian manufacturing industries employed approximately 1.8 million workers in 1974. If we assume that each worker was employed for the full year, it follows that EDC's financing activity of $659 million could be said to be responsible for creating 3.7% of the total man-years in the Canadian manufacturing sector. The value of EDC in creating employment for Canadians appears to be overstated.

Over the fourteen year period ended in 1974, large scale shipping vessels are ranked first in the types of capital equipment financed by the EDC. In that period a total of $347.7 million of long term financing agreements involving the sale of various types of container vessels have been entered into by the EDC. Large industrial projects totalling $312.6 million were ranked second in types of products supported by EDC export credit.

Canada is not one of the world's primary shipbuilding nations. According to the United Nations International Trade Statistics publication, the primary producers and exporters of ships and boats in 1973 were Japan, Germany, Norway, Sweden and the Netherlands. These five nations accounted for 72% of total world exports of this type of capital equipment. Canada, with 1.6% of world exports ranked fourteenth.

The Canadian shipbuilding industry consists of approximately sixty firms. In the five year period ending December 31, 1974, the average annual value of shipments of goods produced by these sixty firms was
about $300 million. Therefore, approximately 25% of Canadian shipbuilding construction is being supported by the export credit offered by the Export Development Corporation. This figure appears surprisingly high when considering that the government also offers a 17% subsidy to all Canadian shipbuilding yards under the Shipbuilding Temporary Assistance Program (STAP). All of this government support is being directed at an industry which employed only 15,062 workers in 1973. MacMillan Bloedel Ltd., by way of comparison, employed 24,000 workers in 1973.

The importance of export credit in supporting the Canadian shipbuilding industry is also subject to question. While a great deal of the literature states that each nation must offer extended credit to compete internationally, one must not overlook other factors. For instance, in 1971, Davie Shipbuilding Ltd. was successful in obtaining the contract to manufacture three 80,000 DWT tankers for Varnima Shipping Agency Limited, a Greek company. In 1972, the President of Davie Shipbuilding, Takis Veliotis, stated that Davie got the contract partly as a result of the various government assistance programs, but mainly because the customer "a Greek shipowner, was in a hurry – the Japanese and European shipyards were fully booked and could not meet the required delivery dates". In view of Mr. Veliotis' statement, it appears EDC's $43.5 million loan, granted to support this sale, was of limited value.

Canada does not appear to enjoy a comparative advantage in the production of ships. The most important requirements of the
industry are: access to a supply of low cost iron and steel; the ready availability of a specialized labour force; a good understanding of the latest marine technology; and access to the world's oceans. Canada, as compared to the world's major shipbuilding nations, does not have any special advantages in any of these areas. Why then is the Federal government through the grant program of the Department of Industry, Trade and Commerce and the financing facility of the EDC offering such a large degree of support to this industry? The answer must lie in the belief that the benefits to the Canadian economy in terms of employment and national independence are greater than the direct costs of the Federal government's support.

In 1973, Canada was ranked as the eleventh largest exporter of telecommunications equipment. The five major exporters, with a total of 65.8% of total world exports, were Japan, Germany, U.S.A., Sweden and the United Kingdom. Canada's communication equipment manufacturing industry consists of approximately 225 firms located primarily in central Canada. Some seventeen firms, however produce about 50% of the total value of goods produced by the industry. In 1973, the industry employed 43,000 workers and produced goods valued at $899 million. In that same year $34.8 million of financing agreements related to telecommunications equipment were signed by the EDC—less than 4% of annual production was supported by export credit. However, approximately 35% of the annual production is exported and approximately two-thirds of all exports go to the United States. Therefore approximately $105 million of the total production of this industry is eligible for support under the export credit granted by the EDC. It is more realistic to state, therefore, that roughly
33% of total exports in this industry are being supported by the financing facilities offered by the EDC.

Canada ranks as one of the top five nations in the exports of aircraft and railway vehicles.18 The Canadian aircraft and aircraft parts manufacturing industry consists of approximately one hundred firms which in 1973 had an annual value of production of $538 million. The major producers in the industry are primarily located in Central Canada. Eleven firms produce 74% of the total value of annual production.19 73% of this type of capital equipment is exported to the United States market and is, therefore, realistically not eligible for export credit. EDC's average annual signings involving the export of aircraft or aircraft components are $38.5 million, or 27.5% of total eligible production. The aircraft manufacturing industry employs about 26,000 Canadian workers.

A similar analysis of the Canadian railway rolling stock industry indicates that the industry has an oligopolistic structure with the major producers being located in central Canada. Less than 8,000 workers are employed in the industry which has an annual output of approximately $350 million.20 EDC supports approximately 35% of the average annual eligible exports for this group of products.

In summary, this brief analysis indicates that between 25-35% of the products of these four groups of industries, which are exported to nations other than the U.S.A., are supported by loans granted by the EDC. These four industries employ less than 100,000 workers or approximately 5.5% of all workers employed in the manufacturing sector of the Canadian economy. 47.3% of EDC's signed financing agreements from 1971 to 1974 involved products manufactured by this same group of
industries. These facts appear to indicate that a fairly biased allocation of resources is resulting from the financing activities of the Export Development Corporation.

However, there are at least two different methods by which a government can attempt to diversify its industrial sector. In Canada's case it may be that a concentration of effort in a small number of industries may be nearer an optimal strategy than a diffusion of the Government's effort through many small industries. The EDC therefore, through its financing facility, a relatively new innovation, may be attempting to stimulate and develop certain key industries. EDC's support may be allowing these industries to expand their facilities in order to achieve a more optimal level of production. Without knowing which strategy is being pursued by the Corporation it is not possible to determine if an optimal allocation of resources is resulting from the financing activity of the Corporation.

All of the industries which appear in Table XII are capital intensive and characterized by a few large producers. Table XV lists the twenty firms which have been most successful in utilizing the financing facility of EDC. It is interesting to note that the seven firms which have had the greatest dollar volume of goods financed by EDC are all domiciled in Quebec. The Corporation has financed $746 million of sales for these seven firms. Seventeen of the twenty largest users of EDC's long term financing facility are domiciled in Ontario and Quebec, the industrialized region of Canada.

Exports supported by the EDC's financing must provide employment and industrial benefits for Canada. It could be argued that
<table>
<thead>
<tr>
<th>RANK</th>
<th>FIRM</th>
<th>PRODUCT</th>
<th>LOCATION</th>
<th>OWNERSHIP</th>
<th>AMOUNT $(MILLION)</th>
<th>%</th>
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<td>MARINE INDUSTRIES LIMITED</td>
<td>SHIPS</td>
<td>QUEBEC</td>
<td>CANADIAN</td>
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<td>2</td>
<td>DAVIE SHIPBUILDING LTD.</td>
<td>SHIPS</td>
<td>QUEBEC</td>
<td>CANADIAN</td>
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<td>7.3</td>
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<tr>
<td>3</td>
<td>NORTHERN ELECTRIC CO. LTD.</td>
<td>TELECOMMUNICATIONS</td>
<td>QUEBEC</td>
<td>CANADIAN</td>
<td>98.1</td>
<td>5.2</td>
</tr>
<tr>
<td>4</td>
<td>MLW WORTHINGTON LTD. AND MLW INDUSTRIES LTD.</td>
<td>LOCOMOTIVES</td>
<td>QUEBEC</td>
<td>U.S.A.</td>
<td>89.2</td>
<td>4.7</td>
</tr>
<tr>
<td>5</td>
<td>MONTREAL ENGINEERING LTD. AND ATOMIC ENERGY OF CANADA LTD.</td>
<td>NUCLEAR POWER PLANT</td>
<td>QUEBEC</td>
<td>CANADIAN</td>
<td>83.5</td>
<td>4.4</td>
</tr>
<tr>
<td>6</td>
<td>STAPLER HURTER LTD. AND OTHER EXPORTERS</td>
<td>FOREST COMPLEX</td>
<td>QUEBEC</td>
<td>U.S.A.</td>
<td>82.5</td>
<td>4.4</td>
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<tr>
<td>7</td>
<td>GTE AUTOMATIC ELECTRIC CANADA LTD.</td>
<td>TELECOMMUNICATIONS</td>
<td>QUEBEC</td>
<td>U.S.A.</td>
<td>80.0</td>
<td>4.2</td>
</tr>
<tr>
<td>8</td>
<td>DIESEL DIVISION OF GENERAL MOTORS CANADA LTD.</td>
<td>LOCOMOTIVES</td>
<td>ONTARIO</td>
<td>U.S.A.</td>
<td>69.1</td>
<td>3.7</td>
</tr>
<tr>
<td>9</td>
<td>DOMINION STEEL AND COAL CORP. LTD.</td>
<td>RAILS AND TIES</td>
<td>NOVA SCOTIA</td>
<td>CANADIAN</td>
<td>66.0</td>
<td>3.5</td>
</tr>
<tr>
<td>10</td>
<td>CE CANADA LTD.</td>
<td>GENERATORS</td>
<td>QUEBEC</td>
<td>U.S.A.</td>
<td>44.3</td>
<td>2.3</td>
</tr>
<tr>
<td></td>
<td></td>
<td>STEAM GENERATORS</td>
<td>ONTARIO</td>
<td>U.S.A.</td>
<td>43.5</td>
<td>2.3</td>
</tr>
<tr>
<td>11</td>
<td>BARCOCK AND WILCOX CANADA LTD.</td>
<td>AIRCRAFT COMPONENTS</td>
<td>ONTARIO</td>
<td>CANADIAN</td>
<td>41.2</td>
<td>2.2</td>
</tr>
<tr>
<td>12</td>
<td>THE de HAVILLAND AIRCRAFT OF CANADA LTD.</td>
<td>STEEL MILL EQUIPMENT</td>
<td>ONTARIO</td>
<td>CANADIAN</td>
<td>40.4</td>
<td>2.1</td>
</tr>
<tr>
<td>13</td>
<td>FERRCO ENGINEERING LTD.</td>
<td>MINING EQUIPMENT</td>
<td>B.C.</td>
<td>CANADIAN</td>
<td>38.4</td>
<td>2.0</td>
</tr>
<tr>
<td>14</td>
<td>WRIGHT ENGINEERING LTD.</td>
<td>PULP AND PAPER MILL</td>
<td>B.C.</td>
<td>CANADIAN</td>
<td>37.6</td>
<td>2.0</td>
</tr>
<tr>
<td>15</td>
<td>H.A. SIMONS LTD.</td>
<td>NUCLEAR POWER</td>
<td>ONTARIO</td>
<td>U.S.A.</td>
<td>34.7</td>
<td>1.8</td>
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<tr>
<td>16</td>
<td>CANADIAN GENERAL ELECTRIC CO. LTD.</td>
<td>AIRCRAFT COMPONENTS</td>
<td>ONTARIO</td>
<td>U.S.A.</td>
<td>31.3</td>
<td>1.7</td>
</tr>
<tr>
<td>17</td>
<td>DOUGLAS AIRCRAFT CO. OF CANADA LTD.</td>
<td>MICROWAVE SYSTEMS</td>
<td>ONTARIO</td>
<td>U.S.A.</td>
<td>30.3</td>
<td>1.6</td>
</tr>
<tr>
<td>18</td>
<td>COLLINS RADIO COMPANY OF CANADA LTD.</td>
<td>GENERATORS</td>
<td>QUEBEC</td>
<td>CANADIAN</td>
<td>28.6</td>
<td>1.5</td>
</tr>
<tr>
<td>19</td>
<td>CORUS CONSTRUCTION ENGINEERING SUPERHEATER LTD.</td>
<td>AIRCRAFT</td>
<td>ONTARIO</td>
<td>CANADIAN</td>
<td>28.5</td>
<td>1.5</td>
</tr>
<tr>
<td>20</td>
<td>CANADIAN COMMERCIAL CORPORATION</td>
<td></td>
<td></td>
<td></td>
<td>454.2</td>
<td>24.1</td>
</tr>
<tr>
<td></td>
<td>PROJECTS INVOLVING VARIOUS CANADIAN SUPPLIERS WHO ARE NOT DESIGNATED</td>
<td></td>
<td></td>
<td></td>
<td>151.9</td>
<td>8.2</td>
</tr>
<tr>
<td></td>
<td>ALL OTHERS NOT ELSEWHERE CLASSIFIED</td>
<td></td>
<td></td>
<td></td>
<td>1886.2</td>
<td>100.0</td>
</tr>
</tbody>
</table>

SOURCE: Export Development Corporation, *Annual Reports*
the regions which need the stimulus to develop their industrial bases are the Maritimes, the Prairies and British Columbia. These regions, in turn, have received little benefit from EDC's financing facility. Defenders of EDC's policies would be quick to reply that EDC is not directly concerned with the policy issue of developing the industrial base in all regions of Canada. Rather, they would claim that function is one of the Department of Regional Economic Expansion. They would also use the "trickle down" argument that while the various depressed regions may be receiving little direct help in developing their industrial sectors, the regions are receiving a great deal of indirect help which can be difficult to measure. For example, Mr. J. McAvity, President of the Canadian Export Association, testifying before the standing Committee on Finance Trade and Economic Affairs on April 3, 1973, stated that in one contract financed by EDC, more than 80% of the gross proceeds were divided amongst 376 companies in Canada spread across five provinces. The Minister of Industry, Trade and Commerce, the Honourable A. Gillespie, testifying before the same Committee on November 14, 1974, observed that the export of a nuclear power plant involves upwards of 200 Canadian suppliers with the value of contracts ranging as low as $500. While these arguments are difficult to refute, it would be interesting to know what percentage of the subcontractors is domiciled in Central Canada and what percentage of the total value of the contract they are supplying.

One-half of the twenty largest firms, i.e. those making the greatest use of EDC's financing facility, are owned by Canadians while the remainder are subsidiaries of American corporations. The issue of ownership and degree of control must not be overlooked. Consider
the case of Northern Electric Company Limited. As a wholly-owned subsidiary of Bell Canada, Northern Electric, is shown as being Canadian-owned. However, when one considers who controls Bell Canada it is easy to see that the degree of influence Canadians have over Northern Electric’s policies may be limited.

A more detailed analysis of the largest user firms provides some enlightening information.

Marine Industries Limited was established by Joseph Simard in 1937 after he purchased from the federal government, for one million dollars, a shipbuilding yard located in Sorel, Quebec, and a large dredging fleet. Over the years, the firm prospered by obtaining shipbuilding contracts from the federal government. Joseph Simard had close ties with the federal Liberal party. Eventually, control of the firm was sold to the General Investment Corporation of Quebec, a wholly owned corporation of the government of the Province of Quebec. In mid-1975, the General Investment Corporation increased its ownership in Marine Industries Limited to 86%. The remaining interest in Marine Industries is held by Claude Simard, a Minister in the Quebec government, Andree Simard, the wife of Quebec premier Robert Bourassa, and the Caisse de Depot et Placement du Quebec.

The Simard family continues to retain an interest in Marine Industries Ltd. through the General Investment Corporation (GIC). Arthur Simard is the Chairman of GIC and Jean Simard is a vice-president of the Corporation. Laurent Picard, the former President of the Canadian Broadcasting Corporation, assumed the Presidency of Marine Industries Ltd. on August 1, 1975.

In 1975, Marine Industries Ltd. and several other companies
and individuals were charged with irregularities in connection with certain government dredging contracts. It is alleged that in 1971 three companies, Marine Industries Ltd., J.P. Porter Co. Ltd., a company controlled by Simard interests, and McNamara Corp. Ltd. had agreed to pay a competitor $400,000 for submitting an artificially high bid to deepen the St. Lawrence channel off the Île d'Orléans.  

In mid-1975, an attempt was made to amalgamate Marine Industries Ltd., MLW Worthington Ltd. (the fourth largest user of EDC's finance facility) and Bombardier Ltd. into a conglomerate to be controlled by a holding company, Les Entreprises de J. Armand Bombardier Ltee. The goal of this conglomerate was to create a strong heavy equipment manufacturing group in Quebec. In early 1976, the proposed amalgamation was called off when Bombardier and GIC could not come to an agreement.  

The following table indicates that 41.4% of Marine Industries Ltd. total sales from 1971-74 were financed with export credit provided by EDC. If these sales would not have materialized without this credit, would the firm's net income have been 40% less than that recorded? If this assumption is correct, the value of EDC export credit to Marine Industries is significant because over that four year period the firm recorded a net deficit of $9.9 million.

<table>
<thead>
<tr>
<th>YEAR</th>
<th>SALES</th>
<th>NET INCOME</th>
<th>EDC CONTRACTS SIGNED IN THAT YEAR</th>
</tr>
</thead>
<tbody>
<tr>
<td>1971</td>
<td>58.3</td>
<td>(3.3)</td>
<td>86.0</td>
</tr>
</tbody>
</table>
1972  137.4
1973  119.6  (10.0)  65.0
1974  107.5
422.8  1.5  24.0
(9.9)  175.0

and The Export Development Corporation, *Annual Reports*.

The view that the role of export credit in supporting industrial production may be overstated is further supported by officials of Marine Industries Ltd. In 1974, the Financial Post reported that the firm's shipbuilding capacity was fully booked until 1979 and in the words of one of the company's officers "we are finding customers expressing interest in 1980 and beyond". While it must be appreciated that the building of a ship is a lengthy process, the officer's statements indicate that world demand for Canadian ships is greater than Canadian productive capacity. Even allowing for the prevalence of export credit support arrangements in the international shipbuilding market it seems quite possible that if the credit provided by the EDC to support sales by this firm were removed, the firm would still have sufficient orders to operate at near capacity.

Davie Shipbuilding Ltd., a major eastern Canadian firm, has been the second largest user of the export credit facilities of the EDC. This firm, until recently, was a wholly owned subsidiary of Canada Steamship Lines Limited, which in turn is owned and controlled by the Power Corporation of Canada Ltd. The Power Corporation is one of Canada's industrial giants that is both owned and controlled by a Canadian, Paul Desmarais. The sphere of influence of Desmarais encompasses both the Canadian private and the public sectors. It is said that he has telephone conversations at least twice a week with
Premier Robert Bourassa and that he has frequent discussions with Prime Minister Trudeau. His guests on fishing trips to Anticosti Island have included Simon Reisman, the then Deputy Minister of Finance.

In Newman's words, "the channels of influence that link Power Corporation and the federal Liberal party carry considerable two-way traffic". Desmarais appears to seek communications links with the senior policy decision making officials in Ottawa. One of the ways he achieves such a link is by hiring away from the federal government some of their young officials who want to operate in the private sector. These "bright young shakers" have included John Rae, the son of Saul Rae, Canada's ambassador to the United Nations, Paul Martin Jr., the son of Paul Martin Sr., Canada's High Commissioner to Britain, Bill Teron, the president of CMHC, Anthony Hampson, the president of the CDC, and Maurice Strong of PetroCan. Bryce Mackasey, while out of the Cabinet, acted as a consultant for Canada Steamship Lines Ltd. and Jean-Luc Pepin, head of the Anti-inflation Board was on the Board of Directors of Canada Steamship Lines Limited.

Davie Shipbuilding Ltd. appears to have been acquired by Canada Steamship Lines in the mid 1960's. In 1968, Davie purchased the assets of Geo. T. Davie and Sons Ltd., a shipyard in Lauzon, from Canadian Vickers. Geo. T. Davie and Sons Ltd. was reportedly losing money in 1967. Financial results for Davie Shipbuilding are not available, so the consolidated financial statements of its parent, Canada Steamship Lines Ltd. (CSL) have been used as a proxy. The analysis indicates that 18% of CSL's gross sales in the four year period were financed by the EDC export credit facilities. If we assume that the credit facility was the key factor in generating these sales,
and that they would not have been made without this facility, then we can conclude that in that four year period $14.7 million of CSL's net income was directly attributable to the availability of EDC export credit.

<table>
<thead>
<tr>
<th>YEAR</th>
<th>GROSS REVENUE</th>
<th>NET INCOME</th>
<th>EDC CONTRACTS SIGNED IN THAT YEAR</th>
</tr>
</thead>
<tbody>
<tr>
<td>1971</td>
<td>143.2</td>
<td>10.9</td>
<td>43.5</td>
</tr>
<tr>
<td>1972</td>
<td>170.0</td>
<td>13.7</td>
<td>-</td>
</tr>
<tr>
<td>1973</td>
<td>242.8</td>
<td>24.5</td>
<td>30.4</td>
</tr>
<tr>
<td>1974</td>
<td>223.5</td>
<td>34.1</td>
<td>64.0</td>
</tr>
</tbody>
</table>


It is also interesting to note the Davie Shipbuilding Ltd. was the firm that performed the refit of the aircraft carrier HMCS Bonaventure. The refitting of this vessel was undertaken at a cost of millions of dollars. The vessel was scrapped shortly after the refitting was complete. The entire episode caused a stir in Canada's public sector.

In the early 1970's The International Nickel Company decided to develop a nickel ore body in Guatemala. The entire project was to cost $100 million and $68.25 million of the cost was financed by various international public financing agencies. Of this $68.25 million, the EDC agreed to provide $17.25 million for the purchase
of Canadian mining equipment and engineering services. INCO and its various subsidiaries, because of their expertise in international mining, would appear to be a logical Canadian exporter. The identity of the Canadian exporters for the project is not clear. The developer of the project in Guatemala and subsequent importer was Exploraciones Y Explotaciones Minerals Izabal, S.A. This firm (EEMI) is owned 70% by INCO and 30% by the government of Guatemala. However, the Guatemalan government does not get its 30% share of the equity until ten years after the start of operations. EEMI also pays no income taxes for the first ten years of operation, but does pay $23,000 per year in royalties.

The ore body will be developed as an open pit mine and will employ only 771 Guatemalan workers when it is in full operation in 1977. In effect, the project will do little to develop Guatemala's industrial base. In fact, by helping to finance the project, Canada may well appear to have a profile similar to that of the "ugly American" who aids multinationals in exploiting the natural resources of LDCs.

The main benefit to Canada of financing INCO's activity is the 1700 direct man-years of employment created. However, this benefit is reduced when one considers that in 1971 INCO reduced its Sudbury plant work force by some 5,000 workers. In 1973, a similar project of about $75 million was financed by EDC for an INCO subsidiary in Indonesia. If INCO continues to develop its international ore bodies while curtailling its mining and other activities in Canada, one would question the wisdom of providing Canadian public funds to aid INCO in developing such foreign ore bodies. Do all Canadians or just the shareholders of INCO receive some benefit from the use of public funds
in this manner? Direct employment in Canada certainly suffers. What are the compensations in terms of greater downstream employment induced by possible comparative cost advantages to Canada through exploiting the foreign ore bodies? Without such data, the benefits to Canada of such EDC financing are not at all clear.

One can certainly question whether a corporation with assets of some $2.8 billion requires low cost financing from public sources in order to make a project viable. INCO's financial strength is evidenced by its purchase in 1974 of ESB Incorporated, a large U.S. based battery producer. Of the total purchase price of $233.8 million, INCO found it necessary to raise only $50 million through external facilities.

A further look at EDC's transactions discloses that international subsidiaries of Canadian chartered banks are amongst the borrowers of the Export Development Corporation. One of the most noticeable features of export credit in Canada has been the reluctance of the banks to participate in such financing with the EDC. The Canadian banks do, however, as shown in the last chapter, participate in the long term financing of U.S. capital equipment exports. The involvement of the Canadian banks in providing export credit for Canadian capital equipment manufacturers is gradually increasing and the new President of EDC reported that in FY 1975, the chartered banks were involved in twenty long term financing projects. The banks' participation however was only $200 million, or less than 18% of the total of the signed financing agreements. The Canadian bank participation level is far below that of the U.S. banks, in spite of the fact that the five largest Canadian banks are very powerful, stable and active in the
<table>
<thead>
<tr>
<th><strong>COUNTRY</strong></th>
<th><strong>BORROWER</strong></th>
<th><strong>PRODUCTS FINANCED</strong></th>
<th><strong>REPAYMENT TERMS</strong></th>
<th><strong>AMOUNT OF FINANCING</strong></th>
</tr>
</thead>
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<tr>
<td>Bahamas</td>
<td>Canadian Imperial Bank of Commerce Trust Co. (Bahamas) Ltd.</td>
<td>Components for DC-10-30 Aircraft</td>
<td>20 S.A. from Dec. 31, 1974</td>
<td>1.2</td>
</tr>
<tr>
<td>Cayman Islands</td>
<td>Canadian Imperial Bank of Commerce Trust Co. (Cayman) Ltd.</td>
<td>Components for DC-10-30 Aircraft</td>
<td>20 S.A. from Nov. 20, 1974</td>
<td>1.2</td>
</tr>
<tr>
<td>Liberia</td>
<td>Ogden Saguenay Transport Inc. and Ogden Ottawa Transport Inc.</td>
<td>2 39,000 DWT Oil Tankers</td>
<td>16 S.A. 6 months After Delivery</td>
<td>32.0</td>
</tr>
<tr>
<td>Indonesia</td>
<td>PT International Nickel Indonesia</td>
<td>Mining Equipment and Engineering Services</td>
<td>20 S.A. from Jan. 10, 1977</td>
<td>17.3</td>
</tr>
<tr>
<td>Spain</td>
<td>Bank of Montreal (Bahamas and Caribbean) Limited</td>
<td>CL-215 Aircraft and Spare Parts</td>
<td>16 S.A. from Nov. 21, 1974</td>
<td>18.0</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>The Cunard Steam-Ship Company Limited</td>
<td>2 39,000 DWT Product Carrier Vessels</td>
<td>16 S.A. 6 months After Delivery</td>
<td>30.4</td>
</tr>
<tr>
<td>Venezuela</td>
<td>BNS International (Bahamas) Ltd.</td>
<td>Aircraft Spare Parts and Related Services</td>
<td>10 S.A. from March 1, 1973</td>
<td>28.5</td>
</tr>
<tr>
<td>Guatemala</td>
<td>EEMI</td>
<td>Mining Equipment</td>
<td>20 S.A. from July 15, 1977</td>
<td>17.3</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td><strong>145.9</strong></td>
</tr>
</tbody>
</table>

**SOURCE:** Export Development Corporation, *Annual Reports*
international area. The difference in the attitude of the Canadian banks and the American banks is puzzling when one considers that the last Canadian bank failure occurred some fifty years ago, while the American unity-banking system had eleven bank failures in 1975. The position becomes even more intriguing when one finds that the Canadian banks are borrowers of low cost export finance.

This unusual practice can perhaps be explained by considering a transaction involving the sale of some used aircraft to Venezuela in 1972. In the Export Development Corporation's annual report for the year ended December 31, 1972 the Auditor General of Canada issued a qualified auditor's report. During that fiscal year, the Department of National Defence (DND) found a market for surplus used aircraft in Venezuela. As might have been expected, the borrower did not have the necessary funds and DND could not afford to carry the receivable account which would arise since DND itself needed to purchase some new aircraft. Normally, when any government department sells surplus goods the funds earned cannot be used to purchase additional goods without the approval of the House of Commons. In effect, therefore, that department's annual budget is reduced by the amount of the earnings from such a sale.

In this case, however, DND managed to avoid the need for parliamentary approval of the transaction. It arranged for the Canadian Commercial Corporation (CCC), a federal Crown Corporation, to negotiate with Canadair, EDC and the Venezuelans on its behalf. Canadair was granted a contract to produce new aircraft for the CCC. The surplus aircraft were then sold by CCC for DND. EDC agreed to finance Venezuela's purchase of the surplus aircraft on the grounds that if it did not
finance the sale of the used aircraft, Canadair would not have obtained the contract to produce the $28.5 million worth of new aircraft purchased by DND. Therefore, EDC argued that they were, in effect, financing a Canadian export.

While the identity of the Venezuelan purchaser of the aircraft is not clear, the borrower was BNS International (Bahamas) Ltd., a part of the Bank of Nova Scotia's corporate structure. The Bank's role could perhaps be explained by their desire to enter the leasing field. At present, the Bank Act restricts banks' ability to operate in the leasing field in the domestic market, but of course, Canada's Bank Act does not apply to a bank's activity outside of Canada. The Bank could, therefore, have purchased the used aircraft from the Department of National Defence and paid for the purchase by borrowing the necessary funds from EDC. The aircraft could then have been leased out to the Venezuelan firm. As the lease payments were made to the Bank, the funds would be used to repay the EDC loan. The Bank of Nova Scotia would indirectly be in the leasing field as the result of a very small capital investment.

In both the INCO case and the DND case it can clearly be argued that the EDC followed a reasonable interpretation of the law and avoided direct contravention of the Act. However, such manoeuvres add little to EDC's credibility in terms of the stated objectives for its existence.
FOOTNOTES

CHAPTER IV

1. Section 10 (1), Export Development Act.


3. Ibid, pp. 21-2


41. This section relies upon testimony before the Standing Committee on Finance, Trade and Economic Affairs on November 14 and November 21, 1974, pp. 11:6-26.
In order to finance the phenomenal growth rates being recorded in recent years, the Export Development Corporation has been forced to increase its borrowings from the Consolidated Revenue Fund (CRF) of the Federal Government. Total loans payable to Canada have increased from $253.6 million on Dec. 31, 1969 to $744.0 million on Dec. 31, 1974. In that same period the Corporation has raised additional funds by borrowing in the Canadian money market. The total short term borrowings outstanding at the end of 1974 amounted to $35.0 million.

The Government of Canada is the sole stockholder in the Corporation and, as such, has contributed $55.0 million in equity capital. In addition, the Government, through the Minister of Finance, has paid in $25.0 million in the form of a capital surplus. The Corporation's reserves and retained earnings were $53.5 million on December 31, 1975. The Corporation's annual net income has increased from $4.8 million in 1970, to $12.8 million in 1975. No dividends have been declared or paid during the past five years.

Being a federal Crown Corporation, the Export Development Corporation is permitted to borrow funds from the Consolidated Revenue Fund at a rate marginally above the rate which the federal government is required to pay to meet its capital requirements. Through this type
of financing arrangement EDC is able to borrow intermediate term funds at a more favorable rate than it could obtain if it were forced to go directly to the capital markets. The Corporation claims that no public subsidy is involved in its financing activity and that the export credit insurance program is not a charge on the Canadian taxpayer.¹

In the 1960's the Corporation's annual borrowings from the CRF were in the $20-40 million range. In the early years of the present decade annual borrowings had increased to the $100-125 million range. In 1974, the EDC's net borrowings were approximately $150 million. The net borrowings for 1975 were $255 million. In addition, in 1975 the Federal Government contributed an additional $30 million in the form of equity capital.

The Federal Government's total financial requirements were less than $700 million a year from 1963-69 inclusive. From 1970 onward these same financial requirements have averaged nearly $2 billion per annum. In the fiscal year ended March 31, 1976, the federal government's total financial requirements exceeded $5 billion. In an attempt to reduce its cash needs the federal government has reviewed its various programs and pared some of the less productive endeavours. The Federal Government would prefer that Crown Corporations such as the EDC reduce their reliance on borrowings from the Consolidated Revenue Fund. John A MacDonald, the President and Chairman of EDC recently announced that the Corporation is prepared to borrow a lot of money in various offshore markets including the Eurodollar market, the U.S. foreign bond market and the Petrodollar market.² Mr. MacDonald hopes that such borrowings will "reduce the Finance Department's concern over our rate of growth. They will remain
simply as our banker of last resort." The Corporation's prospectus is expected to be issued shortly after its 1975 annual report is released.

How great are the Corporation's annual cash needs likely to become? In theory, the Corporation should be able to finance a reasonable rate of growth from the repayment of existing loans, retained earnings, reserves and from non-cash expenses such as depreciation. The bulk of the Corporation's cash needs arise from its long term financing activity. Increases in activity in the export credit insurance field do not create a cash flow problem. The annual premia collected should cover any claims, the operating expenses of the department and provide a reasonable level of profits. Increases in activity in the long term financing field do, however, create a drain on the Corporation's cash resources. The former president of the EDC, Hugh T. Aitken, forecast that future signings of long term financing agreements would continue to increase by 10-15% a year. The Minister responsible for the Export Development Corporation is the Minister of Industry, Trade and Commerce, the Honourable Donald Jamieson. His concern about Canada's trade position virtually makes it imperative for EDC to be very responsive to all applications for long term financing assistance.

In trying to determine how serious a cash flow problem the Corporation will face in the near future, a simple forecasting method utilizing total annual signed agreements has been developed. In theory, a cash forecasting model for the Corporation would analyze all of the past contracts for each type of commodity to each market area to determine a standard cash flow. This standard flow would then be applied to all
future agreements involving that type of product to that particular market area. Unfortunately, attempts to develop such a model have resulted in failure. The small number of contracts signed by the EDC was the prime cause of failure. For example, in each of the past three years, an average of forty-one financing agreements were signed by the EDC for all types of products in all market areas.

The forecasting method developed in this chapter, while not statistically sound, does provide an indication of the magnitude of the net cash flows the Corporation will face in the next three years. The financing agreements are disbursed according to the method used by the Exim Bank. Actual signings are used for each of the past five years. The EDC's signings are forecast to increase by 10% per annum in each of the next three years. Table XVII indicates that disbursements in each of the past three years should have been $198, $308 and $487 million respectively. Comparisons of these forecast disbursements with actual disbursements are not meaningful because the flows resulting from agreements signed prior to 1971 are not included.

Table XVIII analyzes the cash inflows resulting from the financing activity. Most of the capital equipment exports being financed have a lengthy amortization period. The mean repayment period is 9.5 years. The cash forecasting method has, therefore, assumed a nine year repayment period for all contracts, with repayment to commence the year after signing.

Table XVIII also combines the cash receipts and disbursements and obtains a net cash requirement position. Through the use of this method, the net cash outflow for each of the past three years would have
### TABLE XVII

**EXPORT DEVELOPMENT CORPORATION**

**PROJECTED CASH DISBURSEMENTS FOR THE THREE YEARS ENDING DECEMBER 31, 1978**

**MILLIONS OF DOLLARS**

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<thead>
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<tbody>
<tr>
<td>1971 Signings</td>
<td>34</td>
<td>102</td>
<td>68</td>
<td>51</td>
<td>44</td>
<td>299</td>
<td></td>
<td></td>
<td></td>
<td>41.0</td>
<td>340.0</td>
<td></td>
</tr>
<tr>
<td>1972 Signings</td>
<td>28</td>
<td>85</td>
<td>57</td>
<td>42</td>
<td>37</td>
<td>249</td>
<td></td>
<td></td>
<td></td>
<td>34.3</td>
<td>283.8</td>
<td></td>
</tr>
<tr>
<td>1973 Signings</td>
<td>45</td>
<td>134</td>
<td>89</td>
<td>67</td>
<td>58</td>
<td>393</td>
<td></td>
<td></td>
<td></td>
<td>52.4</td>
<td>445.4</td>
<td></td>
</tr>
<tr>
<td>1974 Signings</td>
<td>66</td>
<td>198</td>
<td>132</td>
<td>99</td>
<td>86</td>
<td>581</td>
<td></td>
<td></td>
<td></td>
<td>78.3</td>
<td>659.3</td>
<td></td>
</tr>
<tr>
<td>1975 Signings</td>
<td>114</td>
<td>341</td>
<td>227</td>
<td>170</td>
<td>852</td>
<td>148</td>
<td></td>
<td></td>
<td></td>
<td>135.0</td>
<td>1135.0</td>
<td></td>
</tr>
<tr>
<td>1976 Signings 2</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>150.0</td>
<td>1250.0</td>
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</tr>
<tr>
<td>1977 Signings</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td>165.0</td>
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<td>1978 Signings</td>
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<td></td>
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<td>181.0</td>
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<td><strong>TOTAL</strong></td>
<td>(34)</td>
<td>(130)</td>
<td>(198)</td>
<td>(308)</td>
<td>(487)</td>
<td>(702)</td>
<td>(897)</td>
<td>(1070)</td>
<td>(3826)</td>
<td>(2337)</td>
<td>(837.0)</td>
<td>(7000.0)</td>
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<tr>
<td><strong>UNDISBURSED FUNDS</strong></td>
<td>631.4</td>
<td>930.3</td>
<td>1500.0</td>
<td>1913.0</td>
<td>2076.0</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
</tbody>
</table>

**NOTES:**

1) Disbursements are assumed to be made over 5 years as follows: 10%, 30%, 20%, 15%, 13%. 12% of signings are assumed to be cancelled.

2) Signings from 1976 onward are assumed to grow at an annual rate of 10%.
TABLE XVIII
EXPORT DEVELOPMENT CORPORATION
PROJECTED CASH RECEIPTS AND NET CASH FLOWS FOR
THE THREE YEARS ENDING DECEMBER 31, 1978
MILLIONS OF DOLLARS

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
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</tr>
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<tr>
<td>SIGNED PRIOR TO 1971</td>
<td>55</td>
<td>55</td>
<td>55</td>
<td>55</td>
<td>55</td>
<td>55</td>
<td>55</td>
<td>115</td>
</tr>
<tr>
<td>SIGNED IN 1971</td>
<td>30</td>
<td>30</td>
<td>30</td>
<td>30</td>
<td>30</td>
<td>30</td>
<td>210</td>
<td>299</td>
</tr>
<tr>
<td>SIGNED IN 1973</td>
<td>39</td>
<td>39</td>
<td>39</td>
<td>39</td>
<td>39</td>
<td>39</td>
<td>195</td>
<td>393</td>
</tr>
<tr>
<td>SIGNED IN 1974</td>
<td>58</td>
<td>58</td>
<td>58</td>
<td>58</td>
<td>58</td>
<td>232</td>
<td>349</td>
<td>581</td>
</tr>
<tr>
<td>SIGNED IN 1975</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>SIGNED IN 1976</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>SIGNED IN 1977</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>SIGNED IN 1978</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>TOTAL RECEIPTS</td>
<td>(55)</td>
<td>(85)</td>
<td>(110)</td>
<td>(149)</td>
<td>(207)</td>
<td>(307)</td>
<td>(417)</td>
<td>(1868)</td>
</tr>
</tbody>
</table>

NOTES:
1) Repayment of loans is assumed to be made equally over a nine year period, with a one year lag from the date of signing.
| ITEM                                      | PERIOD FROM 1961-1971 | ACTUAL RESULTS | FORECAST |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
|------------------------------------------|-----------------------|----------------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|
| 1. Signed Agreements                     |                       |                |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| Corporation's Account                    | 789.5                 | 283.3          | 445.4    | 502.2    | 885.0    | 1250.0   | 1375.0   | 1512.0   |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| Government's Account                     | 104.0                 | --             | --       | 157.1    | 250.0    | --       | --       | --       |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| **Total**                                | 893.5                 | 283.3          | 445.4    | 659.3    | 1135.0   | 1250.0   | 1375.0   | 1512.0   |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 2. Cancellations                         |                       |                |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| **Total**                                |                       |                |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 3. Disbursements to Cdn. Exporters       | 537.1                 | 169.3          | 143.8    | 269.6    | 344.8    | 702.0    | 897.0    | 1070.0   |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 4. Undisbursed Financing                 | 356.4                 | 66.5           | 238.3    | 303.0    | 497.6    | 398.0    | 313.0    | 261.0    |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 5. Cumulative Undisbursed Financing      | 356.4                 | 422.9          | 661.2    | 964.2    | 1461.8   | 1859.8   | 2172.8   | 2433.8   |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 6. Repayments by Foreign Borrowers       | 152.3                 | 31.9           | 48.6     | 66.9     | 81.1     | 307.0    | 417.0    | 538.0    |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 7. Net Annual Cash Flow (6-3)            | (384.8)               | (137.4)        | (95.2)   | (202.7)  | (263.7)  | (395.0)  | (480.0)  | (532.0)  |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 8. Net Annual Borrowing from Gov't       | 382.7                 | .96.6          | 121.9    | 143.4    | 264.5    | 100.0    | 100.0    | 100.0    |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 9. Net Borrowing from Private Sector     | -.                    | 45.0           | (29.1)   | 19.5     | (19.9)   | 300.0    | 400.0    | 450.0    |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 10. Net Increase in Equity               | 40.0                  | -.             | 10.0     | -.       | 30.0     | -.       | -.       | -.       |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 11. Total Loans Outstanding from Gov't   | 382.7                 | 479.3          | 601.2    | 744.6    | 1009.1   | 1109.1   | 1209.1   | 1309.1   |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |
| 12. Total Loans O/S from Private Sector  | -.                    | 45.0           | 15.9     | 35.4     | 15.5     | 315.5    | 715.5    | 1165.5   |          |          |          |          |          |          |          |          |          |          |          |          |          |          |

**SOURCE:** Export Development Corporation, *Annual Reports*
been $88,159 and 280 million respectively. The actual cash requirements, as shown on Table XIX (the total of items 8, 9 and 10), were $92.8 million in 1973; $162.9 million in 1974; and $264.6 million in 1975. The technique, therefore, appears to be useful in forecasting the net cash flows of the EOC.

According to Table XVII undisbursed financing contracts should have equalled $631.4 million in 1973, $930.3 million in 1974 and $1,500.0 million in 1975. The actual figures were, $661.2, $964.2 and $1,461.8 million respectively. The technique also appears to be useful in forecasting the levels of undisbursed financing.

Table XIX outlines the capital requirements of the Corporation for the past fifteen years. The results obtained in Tables XVII and XVIII are used to forecast the capital needs of the EDC for the next three years.

The results indicate that the cash needs of the Corporation will increase steadily over the next three years, as will the total of undisbursed financing. By the end of 1978, the EDC will have a total outstanding debt of $2.5 billion. Four years earlier the Corporation had less than $800 million in outstanding debt. Further, by the end of 1978, EDC will have a contingent liability with regard to undisbursed financing contracts of nearly $2.5 billion. These figures support the views expressed by the EDC's chairman that the Corporation will need to borrow a "lot of money" in the not too distant future.6

To maintain an acceptable capital structure the Corporation's equity base will also have to be substantially increased in the near future. Despite the intention of the Corporation to rely more heavily
on the private capital markets in the future, it appears as if more public funds will have to be invested in EDC to at least enable it to raise some of the debt capital it will require.

At present, a large interest differential exists between the Canadian capital market and the U.S. and Eurodollar markets. It will undoubtedly be possible for the EDC to borrow funds in the offshore markets at a more favorable rate than could be obtained in the domestic market. This situation will enable EDC to lend its funds at an internationally competitive rate — i.e. the Corporation's operating margin on its portfolio will be maintained. The large interest differential can not, however, be expected to continue indefinitely and the EDC may have to offer a higher interest rate to attract future capital. If that event transpires, will the operating margin on EDC's portfolio be reduced, or will the interest rate at which EDC is prepared to offer export credit be higher than the internationally competitive rate? Either situation creates problems for the Corporation and/or the Canadian capital equipment manufacturer.

The solution to the problem of trying to locate a large low cost supply of capital which could be used to support Canadian capital equipment exports lies in introducing a rediscount facility for the Canadian banks. In the past, the Canadian banks have been reluctant to grant export credit which had a term of greater than five years. They are slowly being encouraged to increase their participation in this type of investment. In 1975, the banks' share of total signed financing agreements was approximately 20%. The entire problem of getting a greater degree of bank participation in export credit could be given a
substantial boost through the introduction of a rediscount facility.

At present the banks are required to hold 5.5% of their Canadian dollar statutory deposits in the form of secondary reserves. Treasury bills, day to day loans and excess primary reserves are the only investments which qualify as secondary reserves. The secondary reserve facility is primarily used by the Bank of Canada to implement its monetary policy. The chartered banks' Treasury Bill holdings exceed $3 billion, while the total of their day loan portfolio is usually about $0.2 billion.

Treasury bills are a unique instrument. They are extremely liquid, usually being issued for a term of 91 or 182 days. The strength of the issuer coupled with the liquidity feature ensures that Treasury Bills have a low yield. The principal investors in Treasury Bills are the chartered banks and the Bank of Canada. The total amount of Treasury Bills held by each of these investors usually varies with changes in the secondary reserve requirement. For example, the secondary reserve ratio was reduced by 2% between December 1, 1974 and January 1, 1975. The chartered banks' holdings of Treasury Bills from November 1974 to January 1975 decreased by $626 million. In this same period the Bank of Canada's holdings increased by $459 million. At present the total of Treasury Bills outstanding is approximately $6 billion.

In view of the fact that a substantial portion of the Treasury Bill market is really long term Federal Government borrowing which is rolled over 2-4 times a year, it appears reasonable to suggest that a portion of this debt be shifted to a more suitable maturity. It is appreciated that a Treasury Bill market of say $3-4 billion must be maintained in
order for the Bank of Canada to implement the desired monetary policy.

Assume that the Treasury Bill market is reduced by $2 billion. The proposed rediscount facility would allow certain types of export credit to be designated as eligible secondary reserve investments. Eligible export credit would only include long term debt obligations of the Export Development Corporation or a portion of any export credit with a term of greater than three years. To control the terms being offered exporters, the Bank of Canada would require that all such credits be insured by the EDC. A requirement similar to that of the Bank of England could be considered. Eligible secondary reserve investments as related to export credit would be that portion of any loans falling due within 18 months for all credits with a three - five year term. For loans with a maturity beyond five years, one-half of the amount of the loan would be classified as an eligible secondary reserve. Exports to the U.S.A. would not be eligible for support under this program.

The introduction of the proposed rediscount facility could be accomplished through the upcoming revision of the Bank Act.

The rediscount facility would offer advantages for all groups concerned with the promotion of Canadian exports. The benefits would include:

1) Canadian exporters would be able to arrange export credit through their local banks. The small Canadian exporter, as well as the producer located outside of Central Canada would have greater access to export credit. The interest rate offered for credit to support Canadian exports would be competitive with that offered by other nations.
2) The Export Development Corporation would have an assured low cost source of capital funds to finance its activities over the next three years at least. The Corporation would not have to be as concerned about its capital structure. The increased bank participation in export credit would be welcomed. A portion of the routine attached to processing the credit application could be assigned to the banks as is the case in the U.S.A. and the U.K.

3) The chartered banks would merely be shifting from one class of riskless asset to another type of the same asset. The facility would enable the banks to become more active in the field of export credit without being overly concerned about the term. This exogenous stimulus could well have the indirect multiplier effect of pushing the banks into greater participation in export financing. No matter what their initial conservative aversion to such business, its attraction as a substitute reserve vehicle would force them to gear up with the necessary evaluative and processing capabilities. The availability of such internal resources, the latter's probable commitment to increasing their own raison d'être, coupled with a reasonable level of success in rediscounting business would all tend to stimulate the banks to become involved in further foreign credit business on their own account—presumably to the greater benefit of Canadian exports and investors abroad.

4) The Canadian public would benefit by the reduced need to increase their investment in EDC. As discussed previously, the public would also benefit from the encouragement of the development of more efficient financing for export markets.

5) The Federal Government's primary benefit would be in the elimination of its need to concern itself about providing the necessary funds to support the EDC's activities. The cost of financing the $2 billion removed from the Treasury Bill market would be a once and
for all increase of 1-2%.' This cost could also be reduced by a partial and possibly short term increase in reserve requirements to "encourage" banks to participate in the new system. The shifting of the structure of the government's debt could have an effect on the term structure of interest rates in Canada. The Federal Government's attempts to raise an additional $2 billion in the capital market may cause upward pressure on long term interest rates. A detailed discussion of this point, however, is beyond the scope of this study.

In summary, this chapter has shown that the cash requirements of the Export Development Corporation will continue to increase in each of the next three years. The level of undischursed financing will also continue to increase. A simple forecasting technique was designed to forecast the cash needs of the Corporation and a proposal to establish a rediscount facility was developed. Such a relending facility which would greatly benefit all market participants.
FOOTNOTES

CHAPTER V

1. Canada, Parliament, House of Commons, Standing Committee on Finance, 
   Trade and Economic Affairs, Minutes of Proceedings and Evidence 
   on April 13, 1973, p. 11:14 and 
   Export Development Corporation, Annual Report 1974, p. 4

2. ________, "Gov't Export Company Plans to Borrow Funds From Abroad", 
   The Vancouver Sun, January 15, 1976. p. 33

3. Loc. cit.

4. Canada, Parliament, House of Commons, Standing Committee on Finance, 
   Trade and Economic Affairs, Minutes of Proceedings and Evidence 
   on December 10, 1974, p. 16:23

5. Export-Import Bank, Annual Report 1975, p. 23

6. ________, "Gov't Export Company Plans to Borrow Funds From Abroad", 
   The Vancouver Sun, January 15, 1976, p. 33
CHAPTER VI

CONCLUSIONS

This study has been concerned with examining how effectively the Export Development Corporation achieves its primary function of facilitating and developing trade between Canada and the rest of the world. In the first five chapters of this study a considerable number of facts and figures have been presented. In this concluding chapter, the major findings of the study will be summarized in an attempt to constructively criticize the operations of Canada's national export credit granting agency, the Export Development Corporation. Section I will summarize the similarities and differences in the policies and mechanisms used by the United Kingdom, the United States and Canada to promote exports through the use of export credit. Section II will examine the effectiveness of the mechanisms used by the three national agencies to achieve their policy goals. Section III will offer some recommendations for changing the mechanisms used by Canada and more specifically the EDC to promote and finance Canadian trade. The final section will once again look at export credit in the world environment.

1. POLICY GOALS OF EXPORT CREDIT GRANTING AGENCIES

All three of the national export credit granting agencies, the
ECGD, the Exim Bank and the EDC, reviewed in this study have the same basic goal, namely, to promote the exports of their particular nation. They each strive to ensure that credit is not a limiting factor in the sale of capital equipment. The agencies try to ensure that an exporter who is competitive in the world market in terms of price, quality and service is also able to compete in terms of the financing package offered the purchaser.

A substantial volume of the capital equipment produced by the industrialized nations and financed through export credit is purchased by the developing nations. This fact is clearly shown in Table VI and Table XII. However, all three agencies are not overly concerned with the development finance problems facing the LDCs. This lack of concern for development finance is probably best shown in a statement by the former President of the EDC, Hugh T. Aitken, giving evidence before the Standing Committee on Finance, Trade and Economic Affairs on April 17, 1973 stated, "Our aim is oriented to promoting Canadian exports. .......though hopefully a viable project in a developing country which we finance will be of benefit to that country."

While all three agencies have the same basic goal, each one uses a slightly different approach in trying to support the exports of their manufacturing industries.

All of the agencies in this study are willing to underwrite the commercial and political risks of doing business in the world market place. The approach towards export credit insurance in the United States varies slightly from that taken in Canada and the United Kingdom. The U.S. system permits independent insurance brokers located throughout the country to
take applications for export credit insurance on behalf of the FCIA and Exim Bank. In the other two nations, all applications must be submitted directly to either the ECGD or the EDC. The U.S. approach also differs in that the insurer, the Foreign Credit Insurance Association (FCIA) is a partnership consisting of a group of private insurance companies and the Exim Bank.

Both the British and American agencies offer a specific type of policy designed to meet the needs of the relatively small exporter. While there are minor differences in the types of insurance policies offered, international competition and what could be termed the "oligopolistic structure of the industry" ensure the facilities provided are very similar.

In the field of export credit all three nations take a somewhat different approach. The British system relies almost exclusively on the private financial institutions, supported by the ECGD's guarantees, to provide any credit needed to support British exports. In order to ensure that British export credit is comparable to that offered by other nations, the Bank of England offers a rediscount facility for certain types of export credit. This rediscount facility not only allows the British banks to offer terms beyond five years, the normal cut off point for bank credit, but it also helps insulate the cost of export finance from changing domestic credit conditions.

The American system is designed not to compete with private capital which is willing to provide export credit. The Exim Bank tries to encourage and supplement the private capital flows. Through the
participation financing program, the co-operative financing facility and
the commercial bank exporter guarantee program, the Exim Bank has been
very successful in attracting private capital flows to finance U.S.
exports. Under all of its lending programs the Exim Bank tries to limit
its participation to less than 50% of the value of the contract.

Both the purchaser and the supplier of American capital
equipment exports, which are financed through one of the Exim Bank's
facilities, often do not have any direct dealings with the Exim Bank.
The applications are taken and processed by the local financial institution
which then communicates directly with the Exim Bank. In some cases the
local financial institution may approve the credit, under the discretionary
limit of approval granted it by the Bank.

The U.S. agency offers a rediscount facility which is not as
complete as that offered by the British. In the American system, the
eligible export credit of the commercial banks can not be used to improve
the liquidity position of the banking system. Further, the American
system requires the commercial bank to obtain Exim Bank's indication
that the loan is eligible for the discount loan program prior to it (the
commercial bank) granting the loan.

The American approach also differs from both British and Canadian
systems in that the Exim Bank is prepared to support the leasing of U.S.
made capital equipment as well as the purchase of used U.S. capital
equipment. The preliminary commitment procedure is also a unique feature
of the American system.

The Canadian system has, until recently, focused nearly all of
its attention on the field of direct lending. Up until 1974, EDC's
financing facility was used to support relatively large scale projects. The Board of Directors has now removed the notional $1 million eligibility criterion for EDC financing. Any capital equipment transaction that requires extended terms, according to international standards, is now eligible for EDC's support. It still remains to be seen however, whether this formal relaxation will result in a greater proportion of EDC financing being directed to smaller projects. The EDC is also gradually moving towards the participation principle so successfully adopted by the Exim Bank.

The Canadian system does not offer any type of rediscount facility; applications may only be submitted directly to the corporation; the EDC does not grant any lending limits to commercial banks and the Canadian direct lending system does not have any programs designed specifically for the small Canadian exporter.

A comparison of the three national export credit granting agencies would be incomplete without a brief comment on the type of commodities being supported by these programs. The lack of relevant data on the British system necessitates its exclusion from this comparison. However, both the American and Canadian systems indicate that certain industries are receiving the bulk of the support from their national agencies, in particular the aircraft industry in the U.S.A. and shipbuilding in Canada.

Tables VII and XIII indicate that for both Canada and the United States the majority of the financed exports are being purchased by the developing nations. In both cases the LDCs of Central and South America are the main purchasers of this type of export.
II. EFFECTIVENESS OF THE THREE SYSTEMS

Now that a brief comparison of the three systems has been completed, the results of the study will be condensed in an effort to determine how effectively each system meets its policy goals. Three basic criteria for judging the effectiveness of the system, have been identified, —the ability of all market participants to have access to export credit; the relative cost of the credit; and timeliness or the speed with which applications are processed. In an efficient market, all of the potential participants, from the very small to the very large, should theoretically have an equal opportunity to generate activity.

The British system, on the basis of these three criteria, can be said to be effective in promoting British exports. The ECGD makes extensive use of the British banking system and thus all types of exporters can gain access to export credit. Most firms usually have an established working relationship with a commercial bank. The firm, therefore, finds applying for export credit little different from applying for a normal type term loan. The time required to process an application for export credit is not significantly different from that needed to process a normal credit application. The speed with which the ECGD processes insurance applications should indicate that applications for ECGD's guarantee would also be promptly attended to.

The rediscount facility of the Bank of England is effective in both increasing the supply of export credit and keeping the interest rate down. The ability of the banks to reclassify eligible export credit
for liquidity purposes is undoubtedly more important to the banking system than the ability to actually rediscount notes.

The major criticism of the British system is that it can suffer from the conservative attitude of bankers. The bankers may not be as aggressive as the British exporters, and the promotion of British exports may suffer as a result.

Judging by the three aforementioned criteria, the American system is very effective in promoting exports. The CFF along with the concept of participation financing as discussed in Chapter III, indicates that all American exporters of capital equipment have equal access to export credit. The fact that over 1500 applications were processed and approved by one of 300 banks located throughout the world indicates that the program is effective in both promoting American exports and attracting more private capital into the field of export credit.

The cost of American export credit is kept to an internationally competitive level through the use of the "blending principle". The concept of participation financing allows for the mixing of private and public funds to generate the necessary export credit. The Exim Bank, being a public body not overly concerned with the profit maximization principle, is prepared to lend its funds at a rate below that charged by the private institutions. The "blending" of these two interest rates helps to ensure that an internationally competitive rate is offered to support American exports.

The American rediscount facility appears to be of limited value both in terms of increasing the supply of funds and in reducing the
cost of export credit. If the facility were more flexible and perhaps
did not require the banks to designate such loans prior to granting them,
it might be of greater value.

A substantial part of the processing of applications in the
American system is done by the participating bank. This feature, along
with the preliminary commitment procedure, ensures that the turnaround
time in processing applications for export credit is kept to a minimum.

It appears as if the American system supports products in
which the United States enjoys some type of comparative advantage.
However, while the U.S. enjoys a technological advantage in manufacturing
aircraft, the Exim Bank may be supporting the industry for other reasons.
One such reason, the inability of the industry to obtain private financing,
was outlined in Chapter III. While the United States appears to enjoy
some advantages in the production of heavy equipment, such as railroad
rolling stock, the Exim Bank facilities are not used to any large degree
to support such exports. On the other hand, Canadian subsidiaries of
U.S. corporations which produce railroad equipment, make a great deal
of use of the financing facility of the EDC. This fact appears to
indicate that corporate strategy, rather than the comparative advantage
theories, may provide more of an insight into why certain groups of
products are financed.

The capital goods supported by the Exim Bank do not follow
normal U.S. trade patterns, as nearly two-thirds of such exports are
purchased by LDCs.

The Canadian system, as judged by the criteria outlined in this
study, is the least effective of the three systems in meeting its policy
goals. The EDC financing facilities are not readily available to the small exporter. In FY 1975, out of a total of 41 loan agreements signed, only two were for less than $1 million. These smaller agreements involved the export of aircraft components for the Douglas Aircraft Company of Canada Ltd.

The Canadian system does not provide for the efficient processing of loan applications. All such applications must be submitted directly to the EDC. Once these applications have been processed by EDC's central office in Ottawa, they must be approved by EDC's Board of Directors, which only meets once a month. The fact that the checking of the Canadian content requirement is administered from EDC's Ottawa office also adds to the processing time.

The Canadian system, through the use of public funds, has been effective in keeping the cost of export credit down. In fact, the EDC may have been overly effective in this regard when one considers that foreign subsidiaries of Canadian corporations as well as some of Canada's largest banks are among the borrowers of the Corporation. The EDC's increased levels of activity have created a cash flow problem. Chapter V showed that the corporation will require substantial amounts of new capital in the near future. If this capital is raised in the private market, a practice not used extensively by the EDC in the past, the ability of the corporation to continue to offer a competitive interest rate, without eroding its operating margin, may be subject to question.

The analysis of the exported commodities supported by EDC shows that three-quarters of such exports are purchased by the LDCs.
This pattern is just the reverse of Canada's trade pattern for total exports, but is similar to the counter-pattern of U.S. trade supported by the Exim Bank.

The analysis presented in Chapter IV shows that the ship building industry, which has received the greatest amount of support from the EDC, is one in which Canada has few advantages as compared to other nations. After analyzing the corporate structure of two of Canada's largest ship building firms, both of which are major users of EDC's financing, one begins to have some doubts about the efficiency of Canada's export credit market.

III. RECOMMENDATIONS

The general tone of the study has indicated that the net value to the Canadian economy of the EDC's activity may not be as large as at first believed. Despite the fact that record levels of exports are being supported by the EDC's activities, Canada's trade position deteriorated in 1975.

Chapter IV showed that Canada's position in the world market place is deteriorating. The ability of the free market system to effectively operate in Canada has recently been questioned by Prime Minster Trudeau. This study has shown that a public agency, the Export Development Corporation, designed to facilitate and finance Canada's trade, does not perform its function as effectively as similar agencies in two other industrialized nations. The study will now concentrate on outlining various mechanisms
which, if adopted, would permit the EDC to promote Canadian trade more effectively. The recommendations should lead to the development of a more efficient export credit market in Canada.

The Federal Government should adopt two new measures with regard to the field of export credit and development finance. First the objectives of EDC should be reviewed and clarified. While the Corporation claims not to be in the field of development finance, the results of this study show that it definitely is in that field. The Corporation should, therefore, consider the needs of the LDCs and the debt servicing problem facing these nations. Perhaps one large government agency consisting of elements from both CIDA and EDC could be formed to coordinate Canada's efforts in development finance leaving EDC to concentrate on Canadian sellers' need for export credit. Second, the introduction of a rediscount-secondary reserve facility, for eligible export credit, similar to the one outlined in Chapter V should be given a high priority. The advantages of such a facility to all sectors of the Canadian economy were clearly outlined in the last chapter.

Armed with this new mandate and a new source of financing, the officers of the EDC should review the facilities being offered, both in the fields of export credit insurance and export finance. In the field of export credit insurance, the EDC should adopt two new measures. First, in order to ensure that all Canadian exports, whether they are located in Pugwash, Nova Scotia or Sandspit, B.C., can readily purchase export credit insurance, the EDC should permit independent Canadian insurance agents to issue such policies on EDC's behalf. If this strategy was implemented, a substantial part of the processing of the applications would be performed by the insurance agents. The costs of introducing
this measure include paying the agents a commission for their services and EDC would have to undertake a massive training program to ensure that all registered agents were aware of the advantages of export credit insurance. Second, the corporation should introduce a small business type of policy similar to the policies offered by the ECGD and the Exim Bank. While the corporation's present policies may be flexible enough to serve the needs of the small exporter, a new and specific policy might encourage more Canadian exporters to sell their products in the international market place.

With the introduction of a rediscount-secondary reserve facility by the Bank of Canada, the chartered banks will undoubtedly be much more receptive to financing exports of Canadian capital equipment. To meet the demand for eligible export credit the EDC would adopt the principle of participation finance and would strive to keep the level of public funds below 50% of the value of any contract. EDC's new facility would be similar to the one operated so successfully by the Exim Bank.

Every branch of every chartered bank located in Canada would be granted a discretionary limit of approval which could be tied in with the branch's discretionary lending limit granted by its Head Office. This new financing facility would allow all exporters much better access to export credit. The Canadian public would no longer have to concern itself with the issue of political patronage and export credit.

With the introduction of the new facility the EDC should adopt a more decentralized corporate structure. Canada is simply too large a nation to be served by only four offices. Functional regional offices with authority to issue special types of insurance policies and approve
export credit applications would make the marketplace more efficient. The regional offices would be granted discretionary limits of approval. The checking of the Canadian content requirement could also be performed by the regional offices.

In view of the chartered banks' desire to enter the leasing field the EDC should also introduce a lease guarantee facility similar to the one offered by the Exim Bank.

A firm strategy with regard to financing the export of used Canadian capital equipment should be adopted. This new strategy would provide the Corporation's officers with some guidance in situations such as the sale of used aircraft by the Department of National Defence.

With the introduction of all these measures the Corporation would be well on its way to making the export credit market in Canada more efficient. The EDC would be better equipped to facilitate and finance Canada's trade. The problems of the LDCs would be dealt with more specifically in terms of their needs by a specialized export credit granting agency with terms of reference concentrating upon development financing.

Armed with this new facility the Canadian businessman would have the opportunity to become more aggressive in world markets. At present, Canadian manufacturers are content to serve the large U.S. market, the British and Japanese markets, and the domestic market. They seem to fail to realize that by the 1980's Brazil could be a larger economic power than Britain and that by 1985, Japan is forecast to be one of the world's major suppliers of foreign investment capital.

One has only to peruse any Canadian financial paper to find
evidence of the reluctance of Canadian manufacturers to compete abroad. An article in the September 27, 1975 edition of the Financial Post states, for example, "there are few Canadian companies displaying their wares at trade fairs—a major method of selling the German market—or making contact with importers or the Chambers of Commerce". Similar views are expressed by Czechoslovakian officials who state that "Czechs will even go so far as to buy Canadian goods in Europe because they are unable to get a Canadian manufacturer to sell directly to Czechoslovakia". In one international trade fair in Europe, eleven Canadian firms took a total of 90 square meters of space. At that same German fair, Swiss suppliers rented 4,193 square meters of space.

In the past a combination of factors has led to the deterioration of Canada's world trade position. For example, in the early 1970's Canadian research was involved in the development of STOL Aircraft. Canada, however, for a variety of reasons, failed to exploit her position. Foremost International Industries Ltd. is a relatively small Albertan manufacturer specializing in off-the-road transportation equipment. The vehicles are ideally suited to the export market, but in past fifteen years EDC has extended only one direct loan to support the export of Foremost's vehicles. The case of International Hydrodynamics and the Pisces submersibles could be added to this list.

It is to be hoped that in the future, a more aggressive Canadian business community supported by a more efficient export financing agency should be able to avoid the recurrence of situations similar to those cited in the last paragraph. Canada would then be on
her way to regaining a stronger position in world trade.

IV. EXPORT CREDIT IN THE WORLD ENVIRONMENT

The distinction between export credit and development finance is very fine and all national export credit granting agencies are likely to address themselves to the coordination of both these areas in order to foster the development of industrial sectors in nations of the Third World.

The rising cost of energy over the last two years has intensified the debt servicing problem of the LDCs. The twenty-four non-oil producing developing nations are forecast to have a combined current account deficit of $30 billion in 1976. Funds to finance this deficit will have to be obtained from some source, and the options available to this group of nations is gradually being reduced. In early 1976, the Republic of Zaire had to suspend payment on a $500 million Eurocurrency loan. Other nations reportedly facing repayment problems or financial difficulties include Zambia, Ghana, Argentina, Brazil and Mexico. Some of these nations are the "better" customers of the developed nations. One would hope that the latter, if only for their own self-interest, would take the necessary steps to help the developing nations play a more meaningful role in world affairs.

Among the more expensive projects that the industrialized nations have been exporting are nuclear power plants. Up until recently the U.S. had a virtual monopoly in this field, but now nations such as Canada, West Germany and Japan all export nuclear power facilities.
The total cost of a nuclear power system is very large. The annual report of the Exim Bank for FY 1971, indicates that six such projects were authorized for a total of $259.3 million. In the past two years Canada has announced the sale of two CANDU reactors. The total value of these two contracts is more than $800 million. Canadian credit to the purchasers will amount to $459.5 million.

The Canadian nuclear system has cost the Canadian taxpayer millions of dollars to develop and now the benefits are slowly beginning to be received—or are they? How do countries supplying nuclear knowledge ensure that it will not be used for other purposes? Canada's proposed sale of a CANDU Reactor to Argentina is a good case in point. Argentina's intentions are perhaps questionable when one notes that within 10 days of the Indian nuclear blast in May 1974, the Indian foreign minister visited Buenos Aires. The safety of nuclear power is also being questioned in the industrialized nations. In the early 1960's a nuclear power facility was constructed in New Jersey over the objections of scientists who claimed that the marine life in the area would be damaged. Since then millions of dollars have been spent trying to repair the damage caused to the ecological systems. California is considering a referendum to stop construction of more nuclear plants. This type of criticism indicates that perhaps the suppliers of nuclear power generating facilities should carefully review the costs and benefits to society as a whole before future units are sold to the developing nations.

Canada's recent sale of a CANDU reactor to Korea does, however, indicate a new trend in export credit. The exporting nations are slowly beginning to show signs of more cooperation. The total value of the Korean
sale is estimated to be in excess of $700 million and the financing is being provided by the EDC, a consortium of Canadian banks headed by the Royal Bank and a group of British banks headed by Hambros Bank Ltd. EDC will provide $300 million and the Canadian banks will provide an additional $30 million to support Canadian exports. The British banks, secured by the ECGD's guarantee, will provide $50 million to support British exports. The balance of the cost of the project will be provided by the Republic of Korea.

The intense international competition in the field of export credit has resulted in each of the various agencies striving to develop new techniques and methods of financing capital equipment exports. The Exim Bank, for example, is now prepared to offer up to 15% of the value of the export components to finance "local costs" which are necessary to complete the project. The Japanese and the Europeans are also prepared to provide local cost financing. In effect, the practice of providing local cost financing is really a means of reducing the purchaser's down payment.

France and Italy already have a system of guarantees to protect the exporter against increased costs, while France, Germany and the Netherlands are also prepared to provide guarantees against certain losses occurring as a result of changes in the value of foreign currencies. If guarantees against foreign currency exchange losses are offered by agencies, the exporter will easily be able to extend his activities into the world marketing sphere.

The World Bank has also been successful in introducing a joint
financing technique to mix export credit and development finance. The World Bank in conjunction with the developing nations reviews the needs of the country and prepares an application for credit. Interested developed nations then agree to provide a certain amount of long term export credit to their capital equipment suppliers who are successful in obtaining portions of the larger contracts. All of the national credit granting agencies must agree in advance as to the terms and conditions of the export credit. There can be no competition in the credit field. This type of international cooperation is certainly a step in the right direction. However, after this technique had been used five times to finance projects in Brazil, Mexico and Colombia, all areas where the U.S. is the dominant supplier, the Exim Bank began to register opposition to the process. The U.S. exporters are in general reluctant to bid on World Bank contracts and as a result, the Exim Bank claimed the project technique was disrupting historical U.S. trade patterns.

In concluding this study it appears that the developed nations can support the economic growth of LDCs by one of three methods. By the first method, the developed nations would increase their flows of "aid" to the 1% figure recommended by the Pearson Commission. By the second method, they would establish an international body, such as the World Bank, to coordinate funds and review the credit needs of each LDC. Each of the latter would be assigned a maximum amount of external debt that it could have outstanding at any point in time. Each developed nation would in turn assume some responsibility for ensuring that its capital equipment exports were meeting the LDCs higher priority needs. By the last method, and the one most likely to evolve, the existing system with all its inherent dangers will be maintained.
FOOTNOTES

CHAPTER VI


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## APPENDIX I TABLE I

**WORLD TRADE BY REGION, COUNTRY OR AREA**

**VALUE IN MILLIONS OF U.S. DOLLARS**

**EXPORTS F.O.B.**

<table>
<thead>
<tr>
<th>Region</th>
<th>1948</th>
<th>1958</th>
<th>1968</th>
<th>1974</th>
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<tr>
<td>WORLD</td>
<td>57500</td>
<td>108600</td>
<td>239700</td>
<td>842500</td>
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<tr>
<td>DEVELOPED NATIONS</td>
<td>36600</td>
<td>71400</td>
<td>168700</td>
<td>542800</td>
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<tr>
<td>LESS DEVELOPED COUNTRIES</td>
<td>17200</td>
<td>24900</td>
<td>43700</td>
<td>228800</td>
</tr>
<tr>
<td>CENTRALLY PLANNED ECONOMIES</td>
<td>3700</td>
<td>12300</td>
<td>27300</td>
<td>70900</td>
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<tr>
<td>U.S.A.</td>
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<td>17755</td>
<td>34191</td>
<td>97144</td>
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<td>5045</td>
<td>12602</td>
<td>32784</td>
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<tr>
<td>LDCs-AMERICA</td>
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<td>9600</td>
<td>13850</td>
<td>48610</td>
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<td>EUROPE</td>
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<tr>
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<td>15330</td>
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<td>DEVELOPING MARKET ECONOMIES-ASIA</td>
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<td>-</td>
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<td>OCEANIA</td>
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<td>LDCs-OCEANIA</td>
<td>70</td>
<td>140</td>
<td>340</td>
<td>1340</td>
</tr>
</tbody>
</table>

export development corporation

information required in an application for section 29 or 31 financing

To be submitted in triplicate to:
Export Finance Division, Export Development Corporation,
P.O. Box 655, Ottawa 4.

Commitments of long term export financing under Sections 29 or 31 of the Export Development Act are given only on the basis of an application submitted by the Canadian prime exporter requiring long term financing to obtain a major order of capital equipment, and/or engineering services for a sound transaction or project abroad. No commitment of any kind can be given by the Export Development Corporation until full particulars of the transaction or project have been submitted. The Canadian exporter applies for the credit on behalf of the foreign borrower; therefore the application must include complete and detailed information which may be obtained only from the borrower.

This form is to be regarded as a guide to the information required and not as a questionnaire to be completed with brief answers. Any additional relevant information not specifically called for under the listed headings should definitely be included in the application.

It is essential that satisfactory feasibility studies, tender specifications and/or other reports be presented with the application to establish the technical and economic soundness of the transaction requiring financing.

Detailed answers to the questions asked hereunder do not preclude EDC from requesting further information relating to the transaction at a later date.

General summary

1. Name of Exporter:
   (a) Head Office address
   (b) Plant address
2. Name and address of prospective foreign buyer.
3. Outline of the project indicating the total cost, total foreign exchange cost and the amount of EDC financing requested. List the major equipment, materials and services to be supplied from Canada showing their dollar value.

Information concerning exporter

4. Describe exporter's corporate history and operations, including subsidiaries, affiliates, major shareholders and parent company (if any.)
5. If the exporter is a subsidiary, does it have complete freedom to initiate export business? If not what manufacturing and/or selling limitations are placed on its operations by the parent company?
6. Attach audited financial and ancillary statements of exporter for the past five years. For each of the past five years list exporter's total domestic and export sales, domestic and export sales of equipment of the type requiring present financing.
7. On the basis of existing plant capacity state in dollar value: a) maximum output, b) optimum output, c) normal output, d) present output, e) level of output if proposed project undertaken.
8. Show the number of employees of exporter as of the latest available date and as of at least one year ago. Give exporter's average annual employment over the past five years.

9. Describe the employment situation in the area where production facilities are located, giving the latest number and percentage of unemployed, and for the last three years.

10. INFORMATION CONCERNING BORROWER
(If in private sector)

(a) Describe borrower's corporate history and operations, including subsidiaries, affiliates, major shareholders and parent company (if any).

(b) Attach audited financial and ancillary statements of borrower for the past five years, including details of payment terms and interest rates of borrower's present outstanding debts.

(c) Attach borrower's forecast:
   (i) balance sheet
   (ii) income statement
   (iii) statement of source and application of funds including working capital
   (iv) capital expenditure schedule
   (N.B.: forecast should cover the period of construction and extend for a further period of at least five years)

(d) Provide details of additional equity and debt financing contemplated by the borrower during the above forecast period.

(e) If borrower is undertaking a new venture, or entering a new field of activity, supply in complete detail provisions which will be made for supply of experienced management during the first five years of borrowers proposed operations.

11. INFORMATION CONCERNING BORROWER
(If in public sector)

(a) Provide the exact name of government department, agency or entity that will be acting as borrower.

(b) If borrower is a government owned or controlled agency or entity, supply a copy of the statute or decree etc. establishing the organization.

(c) Does the central government guarantee the payment of all the borrower's capital debts?
   If not provide the information requested in Section 10(a) to (d) inclusive.

12. INFORMATION CONCERNING PROJECT

Describe the project fully, giving detailed information on the following:

(a) nature of project
(b) location
(c) economic and technical soundness
(d) viability
(e) national and regional importance in the importing country
(f) further engineering before construction commences
(g) whether sale will be on a f.a.s. or c.i.f. basis — if f.a.s., will insurance claims be paid in Canadian or U.S. dollars?
(A) TIMING
State the anticipated periods and/or dates for the following with reference to the project:
(a) completion and/or start up
(b) construction period
(c) delivery period of the equipment/material at site
(d) placing of orders
(e) signing of a commercial agreement.

(B) COSTS
Provide details of project costs as follows:
(a) total cost of project
(b) local costs and how financed
(c) foreign exchange costs (Canadian)
(d) foreign exchange costs (Non-Canadian) and how financed
(e) foreign agents commission, other commissions, fees and royalties (if any) and how financed
(f) exporter's anticipated net profit after income taxes.

(C) CANADIAN CONTENT
State the overall percentage of Canadian content of the project calculated according to EDC criteria.
Indicate the equipment, material and/or services to be supplied by the exporter and by his main suppliers, giving names of suppliers, and dollar values. For equipment or materials purchased in Canada it should be recognized that most items have non-Canadian content which should be considered when computing the overall Canadian content of the project.

(D) TERMS OF FINANCING REQUESTED
(a) state financing terms required for project
(b) supply detailed and verified information justifying the financing terms requested (i.e. what is foreign competition offering?)
(c) state name of agency or department of government which will provide guarantee of principal and interest
(d) state name of central bank, etc., which will provide guarantee of foreign exchange availability.

13. BENEFITS OF THE PROJECT TO THE ECONOMY OF THE IMPORTING COUNTRY
(a) As a result of this project coming into production what economic benefits will the importing country derive, including employment, use of domestic raw materials, additional revenue to the government and foreign exchange savings?
(b) If the importing country has a National Development Plan, attach a copy of the Plan and give the priority of this project under the Plan.
14. BENEFITS OF THE TRANSACTION TO THE CANADIAN ECONOMY

(a) Describe any special industrial advantages to be derived from this transaction in terms of utilization of labour force and plant capacity, of assistance or encouragement in developing new designs or lines of production, and of increasing Canadian manufacture of equipment or component parts.

(b) Specify the export trade promotion benefits that may be expected to result from this transaction with regard to:
   (i) direct market development prospects in the country of purchase and in the general area; and
   (ii) continuing market for replacement parts of Canadian origin.

(c) What will be the direct and indirect labour effects in Canada:
   (i) for the applicant company
   (ii) for each of the main associated firms and sub-contractors; and
   (iii) for the total transaction

15. CERTIFICATION

Please certify as follows:

We certify that the representations made and facts stated by us are true, and that we have not misrepresented or omitted any material fact which might have a bearing on this application, and further certify that no fees, commissions, grants, gifts or payments of any kind other than those listed in this application have been paid or will be paid to anyone in Canada or abroad in connection with this transaction or application for financing.

Name of Company

Signature...............................................................(TITLE)

Address......................................................................

Date.........................................................................19......