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Export Credit Cover Policies and Payments Difficulties

By Eduard H. Brau and Chanpen Puckahtikom

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The following symbols have been used throughout this paper:

. . . to indicate that data are not available;

— to indicate that the figure is zero or less than half the final digit shown, or that the item does not exist;

– between years or months (e.g., 1979–81 or January–June) to indicate the years or months covered, including the beginning and ending years or months;

/ between years (e.g., 1980/81) to indicate a crop or fiscal (financial) year.

"Billion" means a thousand million.

Minor discrepancies between constituent figures and totals are due to rounding.

Preface

In April-June 1984, Eduard H. Brau, Senior Advisor, and Chanpen Puckahtikom, Assistant Division Chief, both of the Exchange and Trade Relations Department, held informal discussions with representatives of ten major official export credit agencies and, in some instances, their "guardian authorities" within the government. These discussions were held to offer an exchange of views and to improve the mutual understanding of experiences with export credit cover policies for borrowing countries in balance of payments difficulties and for those experiencing payments improvements.

Following preliminary consultations, and because of the complexities of the subject and the confidentiality of some of the material, it was agreed that the most useful approach would be to have an informal exchange of views. The ten agencies participating in the review were the Export-Import Bank of the United States (Eximbank); Export Credits Guarantee Department (ECGD), United Kingdom; Compagnie Francaise d'Assurance pour le Commerce Exterieur (COFACE), France; Hermes Kreditversicherungs-Aktiengesellschaft (HERMES), Federal Republic of Germany; Export Insurance Division, International Trade Policy Bureau, Ministry of International Trade and Industry (EID/MITI), Japan; Export Development Corporation (EDC), Canada; Exportkreditnamnden (EKN), Sweden; Nederlandsche Credietverzekering Maatschappij N. V. (NCM), the Netherlands; Sezione Speciale per l'Assicurazione del Credito all'Esportazione (SACE), Italy; and Office National du Ducroire (OND), Belgium. For agencies that are not autonomous in these matters and act as agents of their governments, the guardian authorities of these agencies also participated in the informal discussions. The generous cooperation of the agencies, their national authorities, and the Secretariat of the International Union of Credit and Investment Insurers (Berne Union) is gratefully acknowledged. To preserve confidentiality, the views of individual agencies or governments are not divulged nor are data supplied to the staff by any individual agency. The paper reflects information available prior to June 1984.

To help focus the discussions, the staff reviewed with the agencies specific examples of how their country exposure policies have developed, and a sample of eleven debtor countries was selected for this purpose—Argentina, Brazil, Madagascar, Mexico, Nigeria, Peru, the Philippines, Romania, Turkey, Venezuela, and Yugoslavia. The sample is believed to be broadly representative of the varying payments difficulties faced by debtor countries, ranging from mild or sporadic to acute or chronic. Most of the countries in the sample have undertaken, or approached, a Paris Club (or a similar official creditor group) debt rescheduling. The sample countries account for some one fourth of the estimated total trade-related credits for all developing countries.

Chapter I presents background and a summary of conclusions to the study. Chapter II provides an introductory discussion of general principles and traditional considerations guiding cover policy and the range of policy measures utilized by agencies. Chapter III reviews developments in the policies and practices of the agencies following the external debt-servicing difficulties since 1982. It deals with the adaptation of approaches in the changed environment and their effects on the

agencies' practices. It examines a number of practical aspects, including the move toward a more comprehensive risk assessment, the agencies' responses to debt reschedulings, their criteria for resumption of normal cover policy, the role of internationally coordinated export credit arrangements, and the implications for borrowing countries. Appendix I reviews the experience of the agencies with the sample of eleven debtor countries during the period 1980 to mid-1984. For each country, the description takes account, where appropriate, of developments during the debt buildup phase, the policy turning point, and prospects and issues. Appendix II contains a brief technical note and a glossary of terms used in this paper.

The paper summarizes the authors' understanding of the experiences of the ten agencies in general as well as with the eleven sample debtor countries over the period 1980 to mid-1984. While the authors have benefited from helpful comments by government and agency officials and by Executive Directors of the Fund, the descriptions of the practices of the agencies and the issues raised by their experiences, especially with individual countries, reflect the views of the authors and should not be attributed to any individual agency or national government, the Berne Union or its Secretariat, nor to the management and Executive Directors of the International Monetary Fund. Research assistance was ably provided by David Hicks, then of the Exchange and Trade Relations Department. The authors also wish to thank the editor, Jennie Lee Carter, of the External Relations Department.

I Summary of Conclusions

In the current environment of payments difficulties, a principal role of the Fund remains the encouragement and support of timely adjustment policies of member countries. For their adjustment efforts to be sustainable, adequate financing is needed, which in turn calls for a critical and realistic assessment of financing possibilities and their implications for adjustment strategies. The adjustment programs of many debtor countries have been supported by the use of Fund resources, and in helping country authorities to design these programs, the Fund management at times needs to confirm assumptions concerning the availability of financing from various sources during the program period.

It is in this context that efforts have been intensified to understand better the three main sources of financing open to debtor countries: official development assistance and other bilateral official lending, commercial bank credit, and commercial export credit, whether direct or insured. An understanding of the first two elements is being refined through collaborative efforts among governments and commercial banks. A better understanding of the third element is equally desirable.

Export credit flows are vital for the smooth functioning of the international trade system. These credits have grown rapidly over the years and, given their sheer size, have become an important source of financing. According to recent estimates by the Bank for International Settlements (BIS) and the Organization for Economic Cooperation and Development (OECD), trade credits extended or guaranteed by official creditors to developing countries increased by 7 percent to \$190 billion at the end of 1983 from \$178 billion at the end of 1982, amounting to roughly one fourth of the outstanding external debt of these countries (see Table 1, p. 19). In this period, such credits increased from the equivalent of 39 percent of nonguaranteed commercial bank credits to 41 percent. Furthermore, because of widespread payments difficulties, a large proportion of insured export credit has been subject to debt rescheduling (see Table 2, p. 20). Credit risks have increased generally, and the response of the agencies to this increase will have a major influence on the mix as well as the sustainability of future financing flows to developing countries.

The conclusions of the study focus on issues of current policy interest and are presented under three headings: the debt buildup phase, the debt-servicing difficulty and rescheduling phase, and the recovery phase and beyond. It should be stressed that this presentation is chosen for expositional convenience, and there is no implication that it is regarded as normal or inevitable that borrowing countries pass beyond what is termed the debt buildup phase.

Debt Buildup Phase

The agencies with whom discussions were held agreed that there are built-in tendencies for them as a group, though not necessarily for each agency, to remain on cover too long—even if unintentionally—for countries not in evident difficulties but pursuing policies that could contribute to future debt-servicing problems. They felt that this systemic weakness continued for certain borrowing countries not encountering problems that are apparent. It was agreed that these tendencies helped to postpone adjustment efforts in some borrowing countries beyond when adjustment measures would entail a comparatively light effort.

The agencies stressed that it is in the first instance the borrowing country's responsibility to exercise prudence, and noted that discipline on the lenders' side is complicated by

—the fact that advance warning signals, or leading economic indicators, are rarely fully conclusive;

—given this fact, and in an intensely competitive environment, the difficulty that any single agency faces in attempting to tighten cover policy ahead of other agencies;

—the perception that an individual agency's action may be marginal in the overall outcome;

—the need to ensure that agencies as a group move gradually rather than abruptly so as to avoid precipitating a liquidity crisis for the borrower. It was accepted that a counterpart to the delay in restraining cover

was a delay in resuming cover after improvements in debt-servicing capability had occurred.

In the light of recent experience, the agencies have attempted to strengthen their country risk assessment procedures by placing greater emphasis on leading economic indicators, such as the direction of economic policies in the borrowing country and the medium-term payments and external debt outlook, but further improvements are possible. Efforts are also under way to strengthen project appraisals and, for some agencies, country limits have been adjusted to more appropriate levels. Aside from these steps within the agencies, there remains an interest in exploring collaborative steps on a case-by-case basis to develop sounder lending standards. The agencies agreed that progress in this field would be an important influence on the role they could play, and the magnitude of credit extended/insured by them, in future years. (See also the section, Recovery Phase and Beyond, below.)

Debt-Servicing Difficulty and Rescheduling Phase

A number of observations and issues emerged from the discussions concerning the agencies' policies and practices when debtors experience serious payments difficulties and when debt reschedulings or other special efforts may be needed. The debt-servicing difficulties in evidence since 1982 have seriously affected the agencies' financial operations and have influenced the application of cover policy in important ways. Debt reschedulings and the attendant heavy claims payments by the agencies have caused an unprecedented deterioration in the agencies' financial position. Flexibility in policy application has had to be circumscribed by the need for agencies to adhere to the principle of being financially self-supporting over the medium term. Keeping this requirement in view, the agencies have become convinced of the need to remain pragmatic and have, in diverse ways, exercised greater flexibility in policy applications.

Two notable policy developments are the maintenance of short-term credit flows and the role of internationally coordinated arrangements to provide export credit assistance to countries undertaking appropriate adjustment. All of the agencies have shown a willingness to maintain short-term credit cover for rescheduling countries to ensure financing for essential imports, provided that appropriate conditions are met. A rescheduling country could maximize its chances of continued short-term cover if it makes clear its intention to not seek a rescheduling of short-term debt and if it is seen as being able to honor current short-term obligations. It was broadly accepted that, while trade finance should not be viewed as balance of payments financing, the absence of short-term cover would drain the foreign exchange reserves of the rescheduling countries and would constitute a negative balance of payments financing, which should be avoided. Furthermore, depriving the debtor of short-term credit cover could also result in a deterioration of the terms of trade, since suppliers tend to raise prices to build in a risk premium against delays in payment. Such risk premiums in trade would only compound the payments difficulties.

There was broad support, in principle, for an internationally coordinated arrangement on a case-by-case basis to provide export credit assistance to those debtor countries undertaking appropriate adjustment to achieve an early return to full creditworthiness. However, most of the agencies were skeptical of the effectiveness of formally pledging commitment targets, regarding export credit financing as an inappropriate tool for balance of payments support, and had strong reservations about the provision of export credits on soft or abnormal terms. The agencies felt that future case-by-case efforts would be more effective and better received if they were conceived as achieving consistency in the cover policy stances among agencies. If that were accomplished, and subject to the decision-making sovereignty of the agencies and the condition that the borrowing country's adjustment policies remained on track, requests for cover of the type informally discussed (especially for short-term credits and selected high-priority medium-term credits) could be better accommodated.

In other broader areas concerning debt rescheduling, the agencies' approaches appeared to have been refined in order to more clearly distinguish between debtor countries that face transitional or liquidity problems and those that face longer-range difficulties. For the former, most agencies seemed ready to take a more flexible attitude. Already, a few were prepared to maintain some cover for rescheduling countries, provided credible efforts were being made to redress the situation. In this connection, most agencies regarded the existence of Fund-supported adjustment programs as evidence of credible efforts and compliance with performance criteria as a sign of economic progress. Increasingly, the agencies seemed to be refining their long-standing approaches to the provision of cover for types of debt not subject to rescheduling, and a few agencies had gone further by retaining cover on a limited scale, even for categories of debt that are rescheduled. These steps are to be welcomed when they help to strengthen international cooperation by supporting those debtor countries that are making progress to resolve their difficulties.

The agencies stressed that country decisions were taken on a case-by-case basis with no hard-and-fast rules. Nonetheless, there are several important practical points that would help debtor countries gain the cooperation of the agencies. In particular, there is need for an improved awareness by the borrower of the close practical link between the terms of a debt rescheduling and the provision of new cover, especially short-term cover. In successive reschedulings, an advance in the cutoff date[1] is best avoided, since in that event the agencies are likely to take severely restrictive actions intended only for countries in prolonged difficulty. Attempts to reschedule debt on a unilateral or bilateral basis would also not be well received. These "ground rules" have not formally been made known to the debtor countries by the agencies, either individually or as a group. It was agreed that inadequate knowledge of the ground rules by some debtors may have been counterproductive, in that the disruption in trade and credit flows may have been more severe than was necessary.

Given the practical link between the terms and conditions of debt rescheduling and the provision of new cover, debt rescheduling can hardly be viewed by a debtor country as a low-cost option, and the relevant trade-offs need to be explored as far as feasible. These trade-offs exist when the debtor is assured of a realistic prospect of continued export credit flows, if appropriate conditions are fulfilled. Unless these conditions are made known in broad terms, debtors in only temporary difficulty may seek overly generous rescheduling terms that could adversely affect the cover policy decisions of the agencies. In this connection, the agencies emphasized that their attitudes could be favorably influenced when a debtor country maintains open communication regarding its economic problems and the intended solutions, makes clear its intentions regarding a debt rescheduling, promptly adopts a Fund-supported adjustment program, and concludes a Paris Club (or a similar official creditor group) rescheduling exercise, if necessary.

[1] All debt service on loans contracted prior to the cutoff date is subject to rescheduling.

Recovery Phase and Beyond

It was generally agreed that in the period ahead a shift away from general balance of payments financing for developing countries toward increased reliance on trade and project financing (including equity finance) should be actively encouraged. At the same time, owing to a system-wide increase in credit risk against the background of accumulated external debt, a general increase in demand for export credit insurance (a shift in the demand curve) is virtually certain, even for countries with good track records and prospects. The prospective willingness of export credit agencies to accommodate this demand, and the form and conditions of such accommodation, will strongly influence the mix and availability of credit flows to developing countries.

All of the agencies considered it important that there should be an orderly and timely resumption of normal cover policies for debtor countries successfully pursuing their adjustment strategies. In this regard, however, and following from the discussion in the section, Debt Buildup Phase, above, the agencies were preoccupied with avoiding the financing/insuring of dubious ventures, and they were under pressure to demonstrate domestically that they would succeed in these endeavors. As a result, a few agencies were turning their attention to developing a procedure whereby a borrowing country would be encouraged to present to them for financing only clearly high-priority projects. Other agencies, while sharing the objective, believed that individual efforts by each of them were likely to be inconsistent as well as inefficient. They were searching for ways in which international organizations such as the World Bank could step up their assistance to borrowing countries in the field of overall public investment planning, including project appraisal and selection.

While it was understood that complex issues would need to be resolved, it was felt that constructive interests converge in a mutually beneficial direction. Those borrowing countries undergoing adjustment to lay the basis for sustained growth must reactivate their investment spending to renew growth. At the same time, it is clearly in the interest of lenders to accommodate the demand for financing for well-conceived projects.

II Principles and Traditional Practices of Export Credit Agencies

Objectives of the Agencies

In broad terms, the agencies share the economic objectives of export promotion and maintenance of financial balance (i.e., the self-supporting principle) over the medium term. In practice, differences in emphasis exist within one agency over time, as well as among the agencies at any given time. The balancing of the two economic considerations may vary from agency to agency, depending on the domestic economic setting at the time, the institutional arrangement and degree of financial autonomy, and the philosophical and historical perspectives.

Export credit insurance is accepted by the General Agreement on Tariffs and Trade (GATT) as a legitimate form of export promotion but not as a form of export subsidy. From time to time, agencies might find it necessary to shift policy emphasis away from their strict financial objectives toward a more active support of exports. Such a shift might occur in circumstances of high domestic unemployment overall or in the exporting industries alone. It also might occur where there is weak export performance and a weak balance of payments position. The agencies articulated the conflicting pressures to avoid a loss of market or to protect market shares, to preserve employment at home, and to adhere to strict financial and economic considerations. Most stressed the practical difficulties in striking a proper balance among these factors.

The flexibility of the agencies in policy application also varies with the degree of financial autonomy. Some agencies are statutorily required to be self-sufficient and must adhere strictly to commercial principles—at least over the medium term. Several are supported by the national budget and need to conform to the normal process of national budgetary control and discipline. A few are financially more independent and can resort to market borrowing. These agencies face fewer immediate financial constraints, are in a position to view shorter-term financial considerations more flexibly, and have more room for maneuver. The application of policy differs among agencies, reflecting national philosophy and preferences with regard to the style of economic management and the desired degree of state intervention.

In addition to economic considerations, a few of the agencies indicated that, at times, the overriding policy considerations may be primarily strategic and political. For most of the agencies, principal policy and country decisions are made by a larger interministerial group that represents the diverse interests of the nation. Most of the agencies cited specific instances where national interests played a major role and where exceptional measures were taken, overriding purely commercial risk standards.

The weight given to noneconomic factors varies across agencies. It ranges from a formal legislative requirement to maintain market presence in the national interest under well-defined situations to an informal understanding on the part of the agencies that market presence would be in the national interest. In several agencies, separate accounts are maintained for transactions that are exceptionally risky, exceptionally large, or taken with noneconomic objectives; these are known variously as national interest or state accounts.

Traditional Considerations Guiding Cover Policy

A move to modify terms and conditions of cover policy (i.e., provision of insurance/guarantee) may be triggered by a number of factors. The link between the triggering events and specific policy reactions is not rigid within one agency and varies across agencies. Within an agency, from case to case, emphasis could shift among the various relevant considerations, depending on the debtor country, the type of financing facility, and the project. Some agencies suggested that for short-term business (i.e., whole-turnover policies), the agency's claims experience might be emphasized, while for medium-term loans the general economic

situation of the borrowing country over the longer term might be emphasized. Across agencies, there could be different perceptions of the risk involved, as subjective elements were unavoidable in risk assessment. However, certain tendencies and considerations appeared to be widely shared.

General Country Assessment

All of the agencies suggested that an overall country risk assessment generally would have a pervasive influence on cover policy decisions. Normally, an agency makes a risk assessment of a debtor country based on both economic and noneconomic criteria. Procedures for such an assessment range from periodic reviews (at regular intervals for most agencies) to those carried out on an ad hoc basis when a specific need arises. Until the debt crisis of 1982, economic assessments generally focused on historical analysis and the current financial and external payments position of the country; efforts have since been made to look further ahead in such assessments (see section on More Comprehensive Risk Assessment, below). A few agencies employ quantitative indicators to guide their operations—for example, selected financial ratios such as the debt service ratio or the import coverage of reserves—while others maintain country exposure limits based on qualitative economic indicators. Noneconomic assessments usually concentrate on geopolitical and strategic aspects, and are made on a qualitative basis.

The agencies noted the practical difficulties they have experienced in denying credit applications merely on the strength of an unfavorable country risk assessment. Frequently, in a competitive environment, restrictive actions could not be introduced in the absence of such clearly negative factors as heavy claims payments to insured lenders or a debt rescheduling.

Transfer Delays

All of the agencies indicated that the nature, magnitude, and trend of transfer delays together constituted the prime basis for tightening terms of cover. Transfer delays may not lead to restrictive actions unless the delay is beyond what is administratively customary in the market. Also, agencies may have deferred restrictive actions if the delays were for small amounts, were isolated cases, and were not growing. Moreover, agencies may defer actions in a crucial commercial market by accommodating transfer delays through an extension of the claims-waiting period.

For an individual agency, significant and rising transfer delays to the agency itself were critical elements for policy decisions and would normally result in prompt restrictive actions. Difficult decisions arise when transfer delays emerge—not for the agency itself but for other agencies. In these instances, the agency with no significant arrears would closely examine the situation and might not take restrictive actions unless such arrears became widespread and substantial among agencies.

It is notable that the agencies seemed to consider payments delays as the major deciding factor in taking restrictive action. Some agencies noted that, at times, restrictive actions had been taken before significant arrears emerged, but this was likely to be the exception. In virtually all of the sample countries in the study, the agencies' experience had been for a strict tightening of cover policy whenever substantial arrears emerged and persisted over an extended period. Moreover, most agencies wanted arrears settled largely, if not completely, before a relaxation of the terms of cover would be considered. From an administrative and policy standpoint, several agencies noted that their decisions in this regard were quite clear-cut. Serious transfer delays that result in heavy claims payments have a direct negative financial impact and constitute a powerful argument against such other factors as exporters' resistance to a hardening of the terms of cover. Also, some agencies may have no other option, as strict legal constraints prevent them from continuing cover while claims are being paid. Even in the absence of a statutory requirement, the agencies operate under the long-standing principle that insurance cannot be given against the certainty of loss.

Attitudes of Other Agencies

There was a consensus that the attitudes of the other Berne Union agencies were an important factor in an individual agency's policy decisions. The agencies described the existence of an extensive network through which they informally consult with each other regarding actions being contemplated for a specific transaction, or general policies for a particular market. Among agencies, policies are not coordinated in a formal sense, and the actions resulting from consultations may be very dissimilar, as each of the agencies may have its own considerations.

Although policy reactions are not uniform, the agencies appear to take the views of the other agencies into consideration to quite a considerable extent. In particular, those agencies with a relatively small market share may look to the larger agencies for a lead, if only because the larger agencies are regarded as better

placed at assessing risk since they have a more comprehensive information base. Several agencies also cited their experiences with being out of step with other agencies, especially being the last agency out of a deteriorating market, and thereby finding sudden jumps in exposure arising from the spillover of the demand unmet by others. These agencies were then faced with a situation that quickly went out of control, and they experienced sharp rises in their market shares that eventually resulted in substantial financial losses.

Attitudes of Other Creditors

Most of the agencies described as a relevant policy consideration the attitudes of other creditors. The attitudes of the commercial banks are especially important for decisions concerning countries that are major borrowers in the capital markets. The agencies cited instances of bank payments moratoria leading directly to the introduction of restrictive terms of cover for medium-term business and cautious attitudes for short-term business.

Generally, when a debt-restructuring negotiation with the commercial banks is under way, the agencies adopt a wait-and-see attitude and defer approval of transactions (at least for medium-term projects) until the outcome has been clarified. After the bank rescheduling agreement, the agencies review the overall situation and take action on that basis. Active financial involvement of the commercial banks in resolving debt difficulties in a country could be viewed as a positive factor. Also relevant for policy decisions are the probability and the magnitude of debt relief extended by official creditors outside of the Berne Union, and financial assistance provided by organizations such as the Fund and the World Bank.

Debt Reschedulings

An approach to the Paris Club for a debt rescheduling, or a rumor of an impending approach, may cause uneasiness, but the agencies may not take restrictive action immediately. Depending on the level of and trends in exposure in a particular market and the amounts of offers or preliminary commitments, a variety of holding actions is feasible. However, when a debt rescheduling has been confirmed, or when an official rescheduling request has been made, most agencies would suspend cover. By the date of the multilateral rescheduling discussions, at the latest, most of the agencies would be off cover.

The comprehensiveness of the cover suspension would depend on the scope and type of debt that is rescheduled. Normally, and for most agencies, at least medium-term cover would be suspended, but short-term cover could be retained, depending on whether the country had met and was seen to be able to meet its short-term obligations. The link between the suspension of cover and debt rescheduling has evolved since the debt difficulties of 1982 and is discussed in more detail in Chapter III.

Role of the Fund

In assessing the economic outlook of a debtor country facing debt-servicing difficulties, all of the agencies take account of the relations of the country with the Fund. Most agencies regarded as positive factors for policy decisions the existence of a Fund-supported adjustment program with conditionality in the upper credit tranches and prompt negotiations on such an adjustment program. Apparent failure to agree on an economic program, or the apparent unwillingness of a country to enter into negotiations on such a program, could have a negative influence on policy decisions by the agencies. Moreover, when a program is in place, the country's failure to comply with the performance criteria of the program would also be a negative sign, and, in some agencies, would often trigger the tightening of the terms of cover. The test of compliance with the performance criteria is viewed by agencies not in a mechanistic way but rather in terms of the country not reaching agreement with the Fund on additional policy measures that might be necessary.

A few agencies also indicated that on occasion they had relied on the limits on the accumulation of external debt in Fund-supported adjustment programs as an important factor for restraining exposure in a particular country. Some agencies have also used these ceilings in their internal planning of the incremental volumes of business in a country.

The influence of a debtor country's relations with the Fund on the policy decisions of the agencies is considerably weaker with regard to countries that are not encountering debt-servicing difficulties. Very few agencies indicated that they had relied on information such as the general economic policy appraisals contained in the Fund's Article IV consultation reports to obtain advance signals on the financial outlook of a borrowing country. In general, there was a feeling that in the absence of negative claims experience, competitive pressures were such that the agencies could not move to restrict cover on the strength of necessarily imprecise advance signals and imperfect forecast of the medium-term outlook.

Policy Measures and Impact on Exposure

The degree of policy restrictiveness depends on the interplay of the various considerations described above. For an individual borrowing country, the policy reactions and the precise mix of measures depend, among other things, on the country circumstances and the agency's internal procedures. Across agencies, the diversity of policy reactions also depends on noneconomic conditions and on the level and trend of each agency's exposure in the market, including the outstanding volume of offers.[2]

The influence of noneconomic factors cannot be quantified but can be very important in select cases in terms of willingness from the national perspective to maintain political and commercial presence in a particular market. Similarly, the influence of the level and trend of exposure on cover policy decisions is complex. At both the conceptual and practical levels, the link between exposure and policy reactions is ambiguous. For a country where the agency maintains a particularly large market share, and where the country risk weighs heavily in the agency's own portfolio, the agency faces a difficult policy choice from a conceptual standpoint. One extreme is for the agency to attempt to improve the quality of risks by continuing to increase its exposure in the expectation that this will prevent a debt crisis at a later stage. The other extreme is for the agency to regard the existing market share and the portfolio concentration as excessive and in need of correction, and it may tighten the terms of cover to reduce its exposure.

The primary objective of cover policy decisions is to guide the level of exposure in a particular market, ranging in degree from controlling the rate of increase in exposure to effecting a desired rate of reduction. The traditional instruments for modifying exposure can be grouped under two headings: (i) supply measures, intended to directly affect the agency's level of commitments, and (ii) pricing measures, intended to influence demand for cover and thereby indirectly the level of commitments. The outcome of pricing measures may be different from the intent, since the underlying demand factors cannot be accurately predicted, and any attempt at fine-tuning by reliance on the indirect measures may prove unsuccessful. Agency preference for a particular set of measures may follow tradition, as well as such economic criteria as the portfolio of the agencies, the concentration of business in credits of particular maturities, and other financial considerations. These aspects are beyond the scope of the present study. Typical measures to tighten policies and their relative effectiveness are described briefly below; see also Appendix II.

[2] This section is not intended to be an exhaustive listing of all policy instruments and gradations of restrictiveness available to the agencies. Rather, it is intended to serve as a background to the account of policy applications to the eleven countries discussed in Appendix I.

Supply Measures

The supply measure most used is ceilings on commitments, primarily of medium-term and long-term maturities, which can be variously applied. For practical reasons, ceilings on short-term commitments have been rare and, when employed, they are usually revolving limits. Most agencies maintain individual country limits (formal or informal) in terms of total commitments/exposure. As a next more restrictive step and sometimes used in addition to limits on total exposure are ceilings on the amount of new commitments during a specified period, generally for a year or less. Limits can also be used in the reopening phase, as indirect signals to the exporters concerning the agency's willingness and interest in a market. Various ceilings to control exposure have been utilized by some agencies as part of an internationally coordinated arrangement to assist some debtor countries. Ceilings on an individual transaction are used by some major agencies, but rarely by the smaller agencies, and only in extreme circumstances when the agency is effectively, if not formally, off cover.

Additional security could be called for by an agency as a condition for cover. The security varies with the legal and administrative setup of the borrowing country rather than with the preference of the agencies. Frequently, the security is an irrevocable letter of credit, if there is sufficient assurance that the issuance of such a document is effectively controlled by the debtor country. If not, a confirmed irrevocable letter of credit could be required, that is, confirmed by a third-country bank or a bank of the agency's choosing; in these circumstances, the agency is effectively off cover since the cross-border risk has been transmitted to the confirming institution. With the recent debt-servicing difficulties, public sector guarantee is being used more frequently by the agencies, reflecting their experience of a better record of servicing of the debt owed or guaranteed by the public sector than that owed by the private sector. This development could reflect the priority accorded to the public sector in foreign exchange allocations, or it could reflect the fact that the poor economic situation in the borrowing country has worsened the commercial risks for the private sector borrowers. In extreme cases, agencies have also required external or third-country guarantors for unique transactions and other forms of collateral require-

ments, such as mortgages on real properties or tying the provision of cover to the retention of foreign exchange earned by the project (e.g., through escrow accounts).

Along with imposing commitment limits and security requirements, the agencies normally withdraw authority delegated to banks or underwriters. They also tend to assess more carefully the commercial creditworthiness of the private buyers, since these buyers are more vulnerable in countries facing difficult economic circumstances. The next move might be to apply more stringent criteria for project selection, with priority given, or cover confined, to selected buyers, economic sectors, or projects with a direct foreign exchange linkage, or with more compelling economic justification.

Most agencies view the case-by-case approach, that is, considering each application for financing or insurance on its own merits, as an important step in their restrictive actions. A main exception is one agency that applies the case-by-case approach as a matter of general policy, since it does not rely on ceilings on commitments as do the other agencies. For most, the case-by-case approach is adopted usually in the transitional phase, when a firm restrictive policy decision is being deferred, or when a more open cover policy is being considered. Agencies also reported having adopted this approach from time to time as a practical, and politically expedient, alternative to a formal off-cover policy. Under this approach, the agencies could in practice suspend cover by rejecting applications on a case-by-case basis.

The most restrictive supply measure is the suspension of cover, usually but not necessarily, first on long-term, then on medium-term, and finally on short-term transactions. When cover is suspended, the agencies would normally continue to honor preliminary offers that become commercially successful. Outstanding offers would be allowed to lapse when the business is not received by the exporter and would not be renewed, and new offers would not be entertained. While disbursements on outstanding commitments would generally proceed on schedule, most agencies could choose to stop disbursements, depending on the project or the type of goods. Some agencies suggested that for standardized products disbursements may be suspended with less difficulty than for customized products or turnkey projects. Only rarely would the agencies take the extreme measure of halting disbursements, for example, by stopping shipments by whole-turnover policyholders or halting work orders for exporters. The general view is that, except in a situation of hostility, suspending disbursement would not be feasible, since it would unfairly pass the burden on to the exporter.

Pricing Measures

Pricing measures have two direct elements, the basic insurance premium and the surcharge, and a variety of indirect elements, for example, varying the claims-waiting period and the percentage cover.

Several agencies, especially the major ones, do not rely heavily on pricing measures to help limit exposure. Various and, at times, conflicting reasons were cited for this position, mainly that the burden on exporters could not be justified domestically by the agencies. One agency felt that the improvement in its financial position through a practical (and politically feasible) price increase would be so marginal as to not be worthwhile. This is especially true if the demand for cover is so elastic that the high prices would result only in deep cuts in volume. In contrast, another agency suggested that, in its own experience, pricing measures had not been effective in checking demand and controlling exposure, since cover demand was seen to be price-insensitive.

A few of the agencies maintain a premium structure that provides a direct link between the rate of premium and the perceived degree of country risk. For these agencies, the premium rates vary in direct proportion to the country risks, and, as a country's risk deteriorates, the market can be downgraded to effect a higher premium charge. This risk-differentiating feature helps agencies to limit exposure in riskier markets through dampening demand, while ensuring that cover is rationed in an economically efficient manner and that trade is directed to stronger markets.

Some agencies apply a flat-rate premium structure across countries, without differentiating for risk levels. They believe that, on strict insurance principles, the rate differentials required to fully compensate for the different risks among countries would be prohibitive and politically infeasible; for high-risk countries, the hypothetical premium differential could be in excess of 20 percentage points. It was considered that the flat-rate structure had the overriding advantage of political expediency—in avoiding being seen to openly differentiate among countries, with attendant foreign policy repercussions. There was no general agreement among the agencies on the optimum premium structure, and agencies tend to maintain a premium structure tailored to their domestic circumstances. Aside from the basic premium, many agencies reported having imposed premium surcharges on an ad hoc basis to help limit exposure and to partially compensate for the increased cost of providing cover in exceptionally risky situations.

As an indirect pricing measure, all agencies have extended the claims-waiting period (beyond that which is customary for the market) as a restrictive move, to

signal to exporters the agencies' attitudes toward a particular market. In the event of uncertainties, extending the claims-waiting period would buy time as a transitional measure and provide a financial respite for agencies through deferring payment of claims. Most agencies could reduce the percentage cover (i.e., the percentage of any loss suffered by the exporter on which the agency would pay claims) in an effort to dampen exporters' demand for cover; this is achieved through a higher proportion of risk being borne by the exporters. As a relatively effective fine-tuning measure, agencies can reduce the percentage cover in steps, from a normal 90 to 95 percent down to as low as 70 percent, beyond which the required degree of self-insurance becomes prohibitive.

Policy Impact on Exposure

The agencies noted some of the practical difficulties in accurately predicting and measuring the impact of their cover policies on their exposure in a borrowing country; the only exception was direct control on the level of commitments. The unpredictability of the underlying demand for cover is the main factor that makes ex ante analysis of exposure very difficult. In particular, in a difficult and uncertain payments situation, the exporters could perceive deteriorating risk in trade without cover, and for an agency there could result an upward shift in the overall demand for cover. In this case, without strict ceilings on the level of commitments, the agency's exposure could continue to rise in spite of its restrictive policy stance. Conversely, when demand is slack, the agency's exposure could decline even though it is following a liberal policy. Similar difficulties could also arise if irregular and lumpy transactions (e.g., for exceptionally large projects) were concluded after the policy stance had turned restrictive. In all of these instances, the exposure level and trend would distort the underlying policy intent.

In principle, the underlying demand trend could be approximated by an analysis of the changes over time in the proportion of national exports covered by insurance. However, in practice, such an analysis is usually flawed, for several technical reasons. For medium-term exposure, an analysis is not feasible without detailed information on the leads and lags in the disbursements (not just commitments) and the relevant trade flows. For short-term exposure, an analysis of demand relative to national exports may be more manageable than that for medium-term exposure, but only under certain simplifying assumptions—for example, that the relationship between commitments and disbursements does not change significantly over time and that the leads and lags between disbursements and trade flows average out over a longer period, such as one year.

The difficulties of measuring policy impact are further compounded in the comparative context across agencies. Aside from technical problems, there is an added complication of ascertaining the precise policy intention and actual practices of other agencies. This is especially difficult if the other agencies have adopted a case-by-case approach, which, in a practical sense, may range from the intention of moderate restriction to an effective off cover. Also, the quality and the scope of risks covered by each agency may differ in practical terms.

Some of the agencies indicated that at times they have relied on certain data as a rough approximation of the relative degree of policy restrictiveness across agencies. Some have analyzed the variations over time in the proportion of offers that materialize in successful commercial contracts. In the case of Mexico in 1983, the individual agency's percentage of successful offers was not altered significantly, thus suggesting that there was no substantive change in the relative competitive strength and in the market shares across agencies. This outcome was consistent with the prior informal understanding among the agencies to continue cover in step with each other. In other circumstances, an evident shift in the proportion of effective covers, and eventually in the market shares, could indicate that certain agencies are out of step with the others. Several agencies described sharp shifts in their market shares in a very short period as a result of their relatively liberal policies compared with other agencies, combined with the existence of a strong trade link.

The detailed country discussion in Appendix I recognizes the ambiguity in the interpretation of exposure data. Nonetheless, it relies on the variations over time in the ratio of short-term commitments to national exports as a partial indicator of the degree of policy restrictiveness.

III Policies and Practices After Onset of Debt-Servicing Difficulties in 1982

Repercussions of Recent Debt Difficulties

There was a consensus among the agencies that the recent debt-servicing difficulties have seriously affected the agencies' financial operations and have influenced the application of cover policy in important ways. The process through which the agencies adapted to the changed environment has been variously described as a metamorphosis or as a learning process. Several agencies considered that they were still adapting, with a few suggesting that there was room for significant improvement in what was seen to have been an ad hoc process.

It was generally agreed that, while the payments difficulties before 1982 had been confined to a few countries and had been regarded as country-specific, the payments problems since 1982 had become more general. These recent difficulties have already resulted in a record number and scale of reschedulings under the Paris Club framework of debt owed to official creditors.

Financially, the debt reschedulings and the attendant heavy claims payments by the agencies have led to a sharp deterioration in their financial position. Eight agencies drew particular attention to the occurrence, for the first time in their history, of substantial trading losses or operating deficits measured on a cash basis. These large deficits were expected to persist over the next few years, given the current debt outlook for many of the debtor countries. For the two agencies that did not report a significant financial loss, the burden of debt rescheduling had not been openly apparent only because the accounting was on an accrual basis.

On the application of cover policy, all of the agencies have felt the need to adapt their traditional practices and attitudes to the changed environment. They noted that the customary continued strict adherance to risk standards and limits would have led them to confine support to an unduly narrow range of export markets. Already, several of the agencies have faced substantial declines in the volume of business. An application of policies not adapted to the changed environment could also have compounded the economic difficulties and the debt-servicing problems of debtor countries and would have been counterproductive. Some agencies drew attention to the need by the agencies to contribute to international financial stability, by helping to achieve an orderly resolution of the current debt-servicing difficulties while preserving international financial discipline. For these reasons, and in spite of their difficult internal financial situation, the agencies, in varying degrees and at various times, have become convinced of the need to be pragmatic and to exercise flexibility in the application of their policies.

Measures to Improve Agency Finances

The agencies have attempted to improve their financial positions and to enhance their ability to be more flexible. They have examined financial alternatives and have taken significant steps in the financial area. These steps include raising revenues, containing risks, and broadening the scope of borrowing to cover their own deficits.

Revenue-Raising Measures

In an attempt to raise revenue, most of the agencies reported that they had made an upward adjustment in the premium rate structure since 1983. It is significant that most reported that these increases were implemented for the first time in some thirty years. In some cases, the rate increases had been delayed under domestic resistance from interested parties. The increases in the premium rate structure have ranged from a low of 5 percent on average for an agency that has made a gradual rate adjustment over the years to

a high of 40 percent for an agency that took the step for the first time in many years.[3]

Aside from across-the-board premium rate increases, some agencies have sharpened the risk-differentiating features of their premium rate structures. For a few agencies, the rate differentials among countries in different risk categories have been widened substantially, with exceptionally high premium rates now applicable to high-risk or rescheduling countries. Even among those agencies that do not subscribe to the principle of risk-differentiating premium structures, there has been an attempt partially to account for part of the higher risk involved in certain instances. These efforts have involved primarily premium surcharges introduced on an ad hoc basis and ranging from as low as 10 percent to as high as 100 percent of the basic rates.

In addition to the premium rate structure, the agencies have attempted to improve their revenue performance in indirect ways. For example, the rates of interest applied to consolidation amounts under debt reschedulings (which had tended to contain concessional elements in the past) have, in more recent years, moved toward current market rates in nearly all cases, although some debtor countries are pressing for moratorium interest rates at levels close to the cost of government funding.

Risk-Containing Measures

The agencies have attempted to contain risks through the use of traditional risk-containing instruments and, for some agencies, through experimentation with new risk-sharing arrangements with exporters, commercial banks, and the borrowers.

The agencies appeared to have made a greater use of the traditional means of reducing the proportion of transactions eligible for insurance cover. However, some observed that a reduced percentage cover below 90 percent was generally difficult to achieve. Several indicated that for many problem countries the percentage cover had been reduced to 70 percent, the lowest possible level before the degree of self-insurance became prohibitive and the intent of the insurance thereby nullified. In making such difficult decisions, distinctions have had to be made among exporters. The reduction in percentage cover was seen by most as an effective means to contain risks, but this measure was not always successful in helping to limit exposure. Other indirect techniques for containing risks have been employed, such as extending the claims-waiting period and improving the quality of risk through requirements of security or collateral.

In general terms, some agencies have not used more active pricing and risk-containing instruments to ration cover. They felt that the burden would be too great for the exporters to bear in the present context of a mixed credit and aid assistance offered by an increasing number of national authorities. Also, the percentage cover should not be reduced in the attempt to limit exposure, as this would happen just when the exporters needed to be provided as much help for as long as possible. During the upturn or reopening phase, the reduced percentage cover might be used more frequently to test market willingness and the quality of risk.

Increasingly, some agencies have experimented with innovative forms of risk-sharing arrangements. For instance, for one country in the recovery phase, one agency was pursuing a risk-sharing arrangement with commercial banks; initially, the risk-sharing formula was 50/50, but was later altered to 60/40. For other agencies, discussions were under way to share risks with banks and consortia of private insurance companies. Overall, the feeling was that such arrangements would be limited in scope.

Several agencies reported greater flexibility through increased use of special accounts (such as the national interest or state accounts). These accounts had enabled the agencies to continue to provide cover for exceptionally risky transactions or for rescheduling countries. It was pointed out, however, that transactions accepted under state accounts were not without limit, since these accounts must conform to national budgetary control and discipline, and all agencies must comply with the requirement of the General Agreement on Tariffs and Trade that export credit schemes not be run on a subsidized basis.

Deficit Financing

Several agencies have financed their deficits through direct national budgetary contributions. Others have made recent special arrangements that empower them to borrow from public financial institutions or in capital markets to finance their deficits. This added borrowing ability has allowed several agencies to accept more risk than otherwise possible.

Adaptations in Cover Policy Decisions

Most agencies reported having taken actions toward greater flexibility since 1983. The approaches have

[3] Given the complexities of the premium rate structures and the diversities of the indirect cost elements across agencies, it is not possible, for the purpose of the present study, to make a strict comparison of the degree of effective increases in the premium costs for the agencies in the study. Some agencies felt that the current level of premiums was broadly competitive across agencies.

varied, depending on institutional arrangements and the domestic setting, ranging from formal government decisions to an informal evolution of practices. One major agency recently was able to make major policy changes only after the relevant export financing legislation had been amended to permit borrowing to finance its deficits. For another major agency, specific cabinet decisions had been taken to formalize the new policy guidelines with a shift in policy emphasis toward domestic employment and foreign market share considerations, and for the agency to accept higher risk and potentially larger budgetary implications. Another major agency reformulated its policy by redefining the concept of "reasonable chances of repayment" to permit more flexible cover policy decisions. One agency had full flexibility and could modify policy decisions in the consultative context within the government without legislative action.

The agencies described the various practical effects of the more flexible approaches adopted since 1983. In general, the operational borderline between off cover and on cover was now much less clear-cut, and there was more selectivity in reactions and timing. More specifically, the practical effects can be described under four main headings: (i) more comprehensive risk assessment; (ii) broader scope for responses to Paris Club (or other similar official creditor group) reschedulings; (iii) resumption of normal cover policies; and (iv) participation in internationally coordinated efforts.

More Comprehensive Risk Assessment

For most agencies, risk assessment has become more systematic and more comprehensive to allow finer distinctions among borrowing countries as a basis for a range of cover policy decisions. In addition, the agencies have begun to closely monitor countries to permit resumption of cover as soon as possible.

Risk assessment in the past had, in practical terms, centered on the claims experience of the agencies, and the main operational objective was to limit risk and to minimize claims payouts. As a result, there was a tendency to react sharply and automatically to any debt rescheduling, and cover had been suspended for countries with prospects of repeated reschedulings. However, the current debt situation has underscored the dilemma faced by all the agencies, namely, assuming further risk in difficult situations versus a loss of export markets. The agencies have attempted to refine the method of country risk assessment to better guide cover policy decisions in difficult cases.

With a more comprehensive risk assessment, the agencies have subdivided borrowing countries into more detailed policy categories. For the satisfactory markets with reasonable assurances of repayment, cover policies would be normal. For uncertain markets, cover policies would vary depending on whether the country was facing a liquidity problem, hence in the category of transitional markets, or whether it was facing longer-term difficulties, hence in the category of difficult markets.

For the transitional or liquidity cases, the agencies closely monitor developments, and policies evolve to become more or less liberal as the situation warrants. Important considerations for the agencies would be whether appropriate adjustment policies were in place for attaining medium-term payments viability. In this connection, at least two agencies indicated their readiness to maintain some cover for countries with a near-term probability of debt reschedulings, provided that credible efforts were being made to redress current difficulties. For most agencies, credible efforts needed to be in evidence through adherence to Fund-supported adjustment programs to assure medium-term prospects.

For difficult markets having a dim long-term outlook and, irrespective of current adjustment policies, where repeated reschedulings were all but certain, cover policies would tend to be very restrictive. In these instances, policy decisions would be quite clear-cut: only very limited cover would be provided and only on noneconomic considerations.

For a few agencies, the list of relevant risk factors for policy decisions has been expanded to include such leading economic indicators as the medium-term debt-servicing ability and the quality of economic management. In this connection, some agencies observed that, owing to staffing constraints, such a comprehensive risk appraisal still left room for improvement. In this context, attention was drawn to improved coverage in Fund papers of medium-term balance of payments scenarios and external debt outlooks.

Despite some progress in the forward-looking aspect of risk assessment, the agencies acknowledged that there remained an inherent weakness in policy application on the basis of such an assessment. The weakness was particularly notable for countries not yet in evident debt difficulties but pursuing policies that could lead to serious problems. All of the agencies experienced difficulties in introducing sufficiently restrictive policies on the basis of leading indicators, such as the direction of financial policies being followed by the debtor country and the medium-term debt outlook (see, e.g., Argentina, Nigeria, and Peru, Appendix I). Even when the advance warning signals were seen as quite conclusive, an individual agency often considered itself precluded from tightening terms of cover ahead of other agencies, for obvious employment and competitive reasons. Furthermore, each agency tended to

feel that its own action might be only marginal in the overall outcome. There was a general feeling that the agencies as a group should not move to prematurely restrict cover, as the move could become a self-fulfilling prophecy.

The agencies recognized that the inherent tendency for them as a group to stay open too long in the situations described could contribute to an excessive debt buildup. They were also aware that, where adjustment was needed, a continued availability of liberal financing could delay necessary adjustment. There was general agreement that the international financial system would be strengthened if ways could be found for the agencies as a group to gradually limit increases in flows of new credits to countries once the leading indicators pointed to impending difficulties. In this way, the debtor countries would be encouraged to take more timely and less severe adjustment measures, and excessive debt buildups could be avoided.

Responses to Paris Club Reschedulings

Most of the agencies stressed that, while there may appear to be typical policy responses to a Paris Club debt rescheduling (or a similar official debt rescheduling forum),[4] these responses should not be regarded as firm operating rules, since there were always important exceptions. Policy decisions for a particular debtor country were taken on a case-by-case basis and tailored to the country's specific circumstances.

Until 1982, there had been fewer and less complex debt reschedulings, and the agencies may have been able to operate under better-defined guidelines. The recent proliferation of debt reschedulings and the changed circumstances have made it inappropriate for the agencies to strictly adhere to past guidelines. Furthermore, the fluidity of the situation means that the agencies have not yet formulated guidelines on all relevant policy aspects. Most appeared to take the view that in this transitional environment flexibility and broad policy options were appropriate, while many were still exploring policy alternatives, and, in time, new policy initiatives and practices could reasonably be expected. As a result of the recent debt difficulties, the agencies seemed to have broadened their scope and increased their options for retaining cover for rescheduling countries, and long-standing rules appear to have been relaxed.

[4] The agencies' responses to reschedulings other than the Paris Club (such as commercial banks) were more diverse and less clear-cut. The principles and practices in connection with these non-Paris Club debt reschedulings are beyond the scope of the present study, except for the isolated instances mentioned in the case studies in Appendix I.

The typical responses to debt reschedulings appear to be as follows. When a country approaches the Paris Club (or a similar forum, such as the OECD Consortium) for a rescheduling, the export credit agencies normally (and, for most, automatically) withdraw cover—at least for the specific types of debt subject to (or considered likely to be subject to) the rescheduling. A continuation of cover on the types of debt subject to rescheduling is possible only on an exceptional basis, primarily on national interest considerations. More recently a few of the smaller agencies have experimented with retaining limited cover even for the types of debt that had been rescheduled (see Peru, Appendix I). Their experiences have been mixed and the results as yet too limited for any firm assessment of their future intentions. Several considerations favor these restrictive responses: there is a need to protect the agencies' financial positions and to limit risks in rescheduling countries; there is a need to maintain international financial discipline and to avoid a proliferation of debt reschedulings if they were obtained at too easy terms; and there is a need to avoid providing excessive assistance to debtor countries in the form of easily available new credits on top of debt relief, and to gear assistance to an equitable burden sharing among creditors.

The agencies may continue to provide cover for the types of debt not subject to the rescheduling arrangement provided that certain additional conditions are fulfilled. The most significant application of this policy is the provision of short-term cover. All of the agencies appeared ready to maintain short-term cover unless such debt had been rescheduled, and provided that there were no outstanding arrears and the country was judged likely to remain current on its short-term transactions. This practice has traditionally been followed by several agencies and has recently gained even wider acceptance (e.g., see, Brazil, Mexico, and Peru, Appendix I). In particular, one major agency which had hitherto withdrawn cover on all transactions irrespective of the coverage of the debt rescheduling arrangement has recently formally adopted this approach. It was prepared to consider maintaining short-term cover for rescheduling countries and was expecting to accommodate significant increases in demand for cover that might occur.

Other applications of this general policy are less well established, although they are also becoming widespread, as evidenced by the experiences with the countries in the sample. Several agencies appeared to have made an even finer distinction among types of debt. For Mexico, as an example, most agencies were able to maintain cover for public sector debt, the type of which had not been rescheduled. Similar principles seemed to apply for arrears; for example, for Vene-

zuela, the existence of arrears on the private sector debt led most agencies to be restrictive on the private debt, while some agencies were able for a time to continue providing cover for the public sector debt (Appendix I).

This flexibility in cover retention is a welcome development in cases where countries are pursuing effective adjustment. The agencies' readiness under certain conditions to continue short-term cover would support the debtor countries in their adjustment process by assuring financing for essential imports (see, e.g., Brazil, Appendix I). Although trade credits should not be regarded as a source of balance of payments financing, the absence of short-term cover would become a drain on the foreign exchange resources of the debtor countries and represents a negative balance of payments financing that should be avoided. Also welcome are other refinements in the matching of cover provisions with the type of debt not subject to rescheduling and therefore in accordance with the debtor countries' own efforts. These steps help to strengthen international cooperation by supporting those debtor countries that are making special attempts to resolve their difficulties.

In this context, there was general agreement that in the period ahead the demand for cover could increase significantly, reflecting a system-wide deterioration in risk rather than country-specific factors, and the agencies could be faced with a substantial increase in exposure. In principle, it was generally agreed that an increased reliance by exporters and commercial banks on trade finance was to be welcomed and was preferable to the commercial bank (balance of payments) financing of the late 1970s and the early 1980s. To the greatest possible extent, the agencies were interested in seeing banks and exporters extend trade finance at their risk and without official cover. At the same time, the agencies were not under global liability limits that would prevent them from accommodating significant increases in demand for credits. In application, the views of agencies appeared to be more diverse. Some agencies have already accepted significant increases in demand for cover from commercial banks for transactions that were previously conducted by banks at their own risk (see, e.g., the Philippines, Appendix I), and still others indicated that a general increase in demand was expected and would be accommodated. Other agencies indicated an unwillingness to accept sharp increases in demand for cover, if these increases reflected a spillover of demand unmet by other agencies, or if they were to reflect a shift in financing terms from cash to credit. Overall, most of the agencies appeared ready to accommodate a system-wide increase in demand, for example, for short-term cover for a rescheduling country, provided that the actions of other agencies were broadly similar.

Resumption of Normal Cover Policies

Average Length of Cover Interruption

The speed of the resumption of normal cover has varied across debtor countries and has depended on the specific circumstances and the progress made in economic adjustment. For the countries in the case study, the length of cover interruption (measured from the time of the Paris Club multilateral agreement) ranged from as short as one year for Peru to an effective interruption of over four years for Turkey.

Most of the agencies felt that the concept of an average length of cover interruption served no useful policy purpose, as decisions needed to be made on a case-by-case basis. From a purely administrative standpoint, a typical period of cover interruption could last about two to three years. Moreover, as noted earlier, the agencies were never completely off cover for several debtor countries. When selective cover was maintained, this served to further blur the practical interpretation of the concept of cover interruption.

Criteria for Resumption of Cover

Generally, normal cover policies will be resumed after the agencies have perceived an improvement in assurance of repayment and the debtor's creditworthiness has been re-established. Aside from this general principle, most of the agencies were hesitant to be more specific, since the precise conditions for each debtor country and each agency vary with their respective circumstances. The agencies indicated that their policies and practices in this regard generally, and concerning debt reschedulings in particular, have been evolving as a result of the debt difficulties since 1982. At present, they share certain preconditions for cover restoration, which may be described broadly as follows.

First, the bilateral rescheduling agreements should normally be in force and any downpayments should have been received. For some agencies, the bilateral agreements should also be successfully implemented; for example, the downpayments should have been made on time and there should have been a substantial, if not complete, regularization of arrears.

Second, no delays in payments for current transactions should occur.

Third, a satisfactory economic adjustment program should be in place, which should provide a reasonable prospect of demonstrable economic improvement over an adequate period. Most of the agencies regarded the adjustment program as credible when supported by Fund resources with upper credit tranche conditionality, and viewed compliance with Fund programs as demonstrating satisfactory performance.

Fourth, the medium-term economic outlook should be favorable, providing a reasonable assurance that future debt-service obligations would be honored.

Fifth, a favorable political climate should exist and market share considerations should be significant.

Even though these preconditions normally would apply, there are exceptions when, on a case-by-case basis, agencies may not require complete fulfillment of such preconditions before resumption of normal cover for a particular country. On the other hand, a few agencies stressed additional relevant criteria. For a few agencies, the debt consolidation period should come to an end. These agencies are statutorily prevented from resuming cover during the debt consolidation period while claims payments are being made. The relationship between the debtor country and the commercial bank creditors (or other relevant major groups of creditors) should be sound. Either inadequate or excessive commercial bank involvement in the period of debt difficulties could be construed as a negative sign. Aside from intercreditor equity, inadequate bank involvement casts doubts on the ability of the borrowing country to resolve its liquidity problem. Excessive bank involvement raises the possibility of the borrowing country relying too readily on financing, rather than on economic adjustment, and merely postpones rather than resolves the debt-servicing difficulties.

The Reopening Phase

After the preconditions have been met, cover would be resumed in a cautious and step-by-step manner. A typical phasing-in pattern might consist of (i) reinstituting short-term cover on a limited basis for raw material imports, with the added condition of an irrevocable letter of credit; (ii) reintroducing medium-term cover, perhaps with initial small transaction limits which could gradually be increased, and under progressively more relaxed conditions; (iii) gradually increasing the percentage cover; and (iv) gradually increasing country commitment limits.

A few agencies drew attention to special problems that have arisen in the context of the recent debt difficulties. In recognition of the need to avoid repeating past mistakes of financing unproductive projects, project appraisal techniques have generally been strengthened, and for some agencies (where applicable) transaction and country limits have been defined at more prudent levels. Some of the agencies indicated the need for assistance in ensuring that the provision of new export credits would be confined to priority projects, and several felt the need for a clearer notion of priority projects worthy of support. Also, there was a general feeling that there was scope for a more consistent policy approach among agencies on a case-by-case basis when moving toward resuming medium-term cover for rescheduling countries.

Some of the major agencies have taken special measures to overcome the difficulties of project selection. For instance, in the case of Turkey (Appendix I), one major agency has tried preselecting projects for cover by limiting the transaction size and by specifying limits for selected projects to be covered. Another major agency has been able to transfer project selection to the debtor country authorities. However, some agencies stressed the impracticality of such attempts. The limits on transaction size would not provide adequate guidance, and all agencies are not in a position to request that the debtor country authorities undertake the task of project prescreening according to certain criteria. Thus, these agencies indicated that they would welcome closer international cooperation in identifying high-priority projects for countries for which normal credit access was being restored.

In general, the agencies acknowledged that effective restraints and controls on appropriate investment financing could not be expected to result from individual creditor initiatives, given the strength of competitive pressures. The initiatives needed to come from the debtor countries through self-imposed restraints, with expertise provided by impartial multilateral organizations such as the World Bank. These restraints by the debtor country may be in the form of defining and adopting an investment plan of sound projects and appropriate size.

Internationally Coordinated Arrangements

In recent years, all of the agencies have participated in some of the arrangements coordinated internationally on a case-by-case basis to provide special assistance to some debtor countries. The experiences with the arrangements for four countries—Brazil, Mexico, Turkey, and Yugoslavia—were discussed during the course of the study (for details, see the respective country notes in Appendix I).

In principle, broad support existed for the idea of arranging a concerted international financing exercise on an exceptional basis for countries prepared to take

adjustment measures. Aside from the agencies' own specific national interests, other important considerations for agencies to provide assistance as a preventive exercise are to avoid a liquidity crisis and to set the basis for preventing future reschedulings. In practical terms, however, most of the agencies stressed that certain features of the arrangements undertaken so far should be avoided in future attempts to assist countries in an exceptional context, and some also stressed that sovereignty in decision making must be maintained.

In the first instance and at the conceptual level, most of the agencies argued that trade financing should not be used as balance of payments financing, for several reasons. Medium-term export credits would not constitute an effective instrument of balance of payments financing, since credit flows follow commitments after considerable delay. During the adjustment phase, there may not be much demand from the debtor country for medium-term project financing. For short-term export credits (which could be considered balance of payments financing in the sense that their absence constitutes negative financing), a special international arrangement would be redundant, since the agencies were already predisposed to maintaining short-term cover provided that appropriate conditions were fulfilled. Even if trade credits could be used for balance of payments financing, there were practical difficulties in accurately estimating the ex ante financing requirement and in establishing the appropriate individual agencies' commitments.

For the above reasons, most agencies felt that case-by-case international arrangements should not be conceived as an integral part of a financing package to fill a financing gap, with specific target amounts pledged by individual agencies. They felt the effort for Brazil was a one-time exceptional undertaking. Also, a few of the agencies expressed strong reservations about an evolution whereby the Fund became an international pledging forum for export credits.

At a pragmatic level, most of the agencies cited considerations relevant to the shape of future internationally coordinated attempts. It was felt that an informal and unofficial attempt to arrive at a consistent policy approach on a strictly case-by-case basis was more expedient and could be achieved more easily (e.g., the 1982 effort for Mexico). Informal and internal commitment targets could be administered more flexibly, and some agencies preferred to avoid a formal public announcement of their intentions so as to leave open the option of policy adjustment—for either more or less restriction—as the situation evolved. A general view was held that the case-by-case approach should not entail the provision of credit on soft or abnormal terms, for example, three-to-five-year credit terms for consumer goods that were normally covered under short-term credits (e.g., the 1983 Yugoslavia arrangement). Except for one agency that had close trading links and fewer administrative encumbrances in dealing with the debtor country, commitments with abnormal credit terms had not been much utilized. This was caused in part by restricted demand from the borrowing countries and in part by administrative safeguards that had to be introduced by the agencies. Most of the agencies were conceptually opposed to the provision of credit on abnormal terms to countries in difficulties, since there was a risk of proliferation of softer terms to creditworthy countries and a general degeneration of the terms structure for export credit, circumventing established international understandings.

Implications of Agency Practices for Debtor Countries

The agencies indicated that they had not individually made known to any debtor country policy and operational practices that might have a direct bearing on the country. Clearly, policy options for a particular debtor country were confidential and exclusively governmental decisions. National authorities have taken care not to be seen as declaring specific preferred actions for any debtor country that could enable the country to maximize the provision of export credit cover. This type of action would not be viewed as appropriate, since the risk of abuse would complicate relations with the debtor country. On an exceptional basis and for a country with whom there were special historical and trade ties, some of the agencies may have made informal efforts to explore alternatives and advise on the various policy ramifications. Informally and at a high political level, a debtor country may have been advised of the desirability of adopting a Fund-supported adjustment program. Also, some of the agencies may have explained to their national exporters the basis of their specific policy decisions.

While most of the agencies have certain common views and practices, as a group (e.g., within the context of the Berne Union or the OECD Export Credit Group) they have not taken steps to explain these views or to make their practices known to the debtor countries. Informally and over time, certain information has been filtered through the Paris Club chairmanship on behalf of all creditors.

The debtor countries may have inadequate knowledge of a "preferred approach" (from the perspective of the agencies) that could help them to maintain cover. Frequently, in their contacts with the Fund staff, the debtor countries have requested advice on matters directly concerning export credits and res-

chedulings. It is also clear from recent experience that, owing partly to inadequate information, some debtor countries may have taken actions that turned out to be counterproductive, in that the disruption of credit and trade flows became more severe than warranted. A notable example is the tendency for some debtor countries to take extreme positions regarding the Paris Club rescheduling terms, owing in part to uncertainties concerning the potential availability of new cover and prospects for credit flows. These positions could jeopardize the agencies' ability to retain some cover, a distortion in the trade pattern could ensue, and the debtor countries could be faced with a deterioration in their terms of trade—through implicit risk premiums on import prices—as exporters attempt to reflect in their pricing the risks involved in uninsured trade.

There was some support for the idea that, from a broader perspective, an improved awareness by the debtor countries of the "ground rules" would be desirable. Already, such "rules" could be discerned from the discussions on the general practices of the agencies and from specific experiences with the debtor countries in the study. They concern practical and operational issues, in addition to the fundamental need for the debtor countries to adopt appropriate adjustment policies and the long-standing principle against a rescheduling of debt on a unilateral or bilateral basis. The following are some of the approaches which could help the debtor countries gain the cooperation of the export credit agencies in maintaining cover on a selective basis.

Link Between Reschedulings and the Provision and Terms of New Cover

A close link exists between the coverage of a debt rescheduling and the scope and type of insurance cover that the agencies can maintain. As noted earlier, a clear link exists in regard to the provision of short-term cover, and a rescheduling country, through its own action, could maximize its chances of continued short-term cover and could avoid a worsening in its terms of trade. Some countries might also succeed in obtaining cover for the public sector debt if that type of debt is excluded from the Paris Club rescheduling.

A debtor country might be advised against seeking an advance in the cutoff date[5] for successive reschedulings, since such a step could lead the agencies to impose severely restrictive policies intended only for countries in chronic debt-servicing difficulty. In these circumstances, the agencies could withdraw cover except for the most essential imports under special accounts and on noneconomic grounds (see Madagascar, Appendix I). It should be noted, however, that a debtor country's prior commitment not to advance the cutoff date may not necessarily induce the agencies to reintroduce medium-term cover, as such a commitment must be seen as credible in the context of the debtor's medium-term prospects.

The link is much less clear between the overall terms of a rescheduling and the agencies' readiness to provide further cover. Nonetheless, a few agencies felt that when a debtor had chosen to confine the coverage of the rescheduling to only the principal amount (rather than to include, as customary in the Paris Club framework, the interest due), this action had positively influenced their attitudes and decisions, in that the narrow rescheduling coverage was indicative of a milder degree of difficulty and an improved outlook for the debtor country (see, e.g., Yugoslavia, Appendix I). Moreover, it appears that for some agencies, the softer the terms and conditions provided at a Paris Club rescheduling, the harder could become the terms and conditions attached to the provision of new cover. Against this background, a debtor country would be well advised not to view debt rescheduling as a low-cost option in its overall financial planning, and to explore as far as feasible the relevant trade-offs between debt reschedulings and the terms and conditions of new cover.

Link Between Debtor Countries' Other Actions and General Attitudes of the Agencies

Several instances were cited in which the attitudes of the agencies were favorably influenced by actions taken by the debtor country. Most frequently indicated as a positive factor by the agencies was the effectiveness of communication maintained by the debtor country in explaining its financial and economic situation and its plan to overcome its problems; better record-keeping and analysis of the economic situation is also helpful. The Philippines was cited as a case where deficient information and communication at the initial stages had adversely affected some agencies' decisions. Also cited was Romania, where inadequate communication and resultant uncertainty had led some agencies to overreact to protect against a worst possible scenario, and to become more restrictive than eventually was found necessary. On the other hand, several agencies were able to point to specific instances where more flexible efforts were made possible by effective communication (see Mexico, Appendix I).

[5] All debt service on loans contracted prior to the cutoff date is subject to rescheduling.

Another positive factor is for the debtor country to clearly state its intentions concerning debt rescheduling and not to attempt to stop payment before making its intentions clear. Prompt conclusion, both of negotiations on a Fund-supported program and the Paris Club exercise, once these are found necessary, is considered helpful. Instances were cited when payments moratoria had been declared, but the move toward Paris Club discussions had stalled, thus creating uncertainties (see Nigeria and Philippines, Appendix I). In some of these circumstances, the agencies' actions may have already been more flexible in anticipation of a speedy conclusion of a Paris Club agreement, and protracted Fund negotiations and delayed Paris Club discussions only meant that the agencies could further tighten their cover policies; when the eventual agreements are reached, speedy policy relaxation could not necessarily be expected in these situations.

It is also considered helpful if attempts are made by the debtor country to allocate foreign exchange across domestic borrowers on an equitable basis. The agencies cited as important factors in their restrictive decisions vis-à-vis Venezuela the discriminatory treatment given to private sector borrowers, and the apparent absence of "best efforts" to deal with the situation of payments arrears (Appendix I).

A few of the agencies also cited as an important factor the willingness of the debtor countries to adopt a sound debt-management policy. In particular, some of them felt that the debtor country might be encouraged to maintain a better debt information system, including data on uninsured short-term credits. Finally, in the recovery phase, the debtor country might be encouraged to establish a priority investment plan, possibly in coordination with, or with the expertise of, the World Bank.

Appendix I

Policies and Practices for Selected Countries

These individual country notes are based on the informal discussions with the ten agencies on how their country exposure policies and practices have evolved for each country. The notes describe, where appropriate, developments during the debt buildup phase, the policy turning point, and prospects and issues. They are also based on data that the agencies report on a regular basis to the Berne Union Secretariat, namely, quarterly reports on the terms of cover and on the level of commitments (medium-term and short-term) of each agency for each of the countries in the sample (except Madagascar). The basis for reporting may vary from agency to agency, and a strict statistical interpretation of the aggregate agency data is therefore not feasible. The interpretation of the commitment trends for the individual countries is difficult unless supported by additional qualitative and agency-specific information. Moreover, there are practical difficulties in measuring policy impact on agencies' exposure in a given borrowing country; these difficulties are described in more detail in Chapter II (page 9). For these reasons, the descriptions concerning the trend in the exposure of the ten agencies in aggregate for each of the debtor countries included in the sample should be regarded as broadly indicative. The notes reflect information from the informal discussions up to June 1984, and commitment trends through the end of 1984.

The following should be noted in interpreting Charts 1–10. For each debtor country, the top three agencies are identified separately on the basis of medium-term and long-term commitments and short-term commitments, and these top agencies normally are not identical across debtor countries. The ranking is determined at the year of the approximate policy turning point, and can be expected to vary over the observation period 1980 to 1984. For each agency, the annual average percentage change in its commitments is calculated as the average of the quarterly percentage changes (measured over the same quarter in the preceding year); percentage changes for agencies in the aggregate are calculated on the same basis. For each agency, the annual average ratio of short-term commitments to national exports is obtained by dividing the annual sum of quarterly commitments by the annual national exports. The aggregate ratio for the top three and the ten agencies is derived in a similar fashion, that is, by dividing the agency-aggregated quarterly commitments (summed over a year) by aggregated national exports. For all Berne Union agencies, the ratio is derived by dividing the annual sum of quarterly commitments of all agencies by the debtor country's annual imports.

Argentina

Debt Buildup Phase

During 1980–81, there was keen interest in the market and almost all agencies maintained liberal cover policies for Argentina. By 1981, however, signs of the deteriorating political and economic situation were becoming apparent to a number of the agencies. Negative factors cited by these agencies included the volatile political scene, accelerated inflation, and an increasingly overvalued exchange rate. Despite these signs, most agencies were reluctant to take restrictive actions. For eight of the ten agencies, their published terms of cover remained liberal and broadly unchanged in 1981. Only one agency attempted, in the second quarter of 1981, to restrict cover through downgrading the market, imposing transaction limits, and considering applications on a stricter case-by-case basis. In the next quarter, one other agency introduced trans-

action limits. Most agencies maintained a more positive attitude and, at that time, regarded the economic and financial difficulties as temporary and reversible. They also wished to maintain market presence in view of the favorably judged medium-term economic outlook and Argentina's rich resource base. In an effort to deal partially with Argentina's deteriorating economic situation, some agencies adopted a more stringent assessment of the commercial risks in lending to private buyers, but, generally, no further attempts were made to restrict cover.

Given the liberal cover policies of most agencies and the buoyant import demand, there were exceptionally large increases in the agencies' exposure in 1980. Outstanding commitments of the ten agencies in aggregate doubled in that year, although much of the increase came from sharp rises (ranging from 30 percent to over 200 percent) in the exposure of the top three agencies in the market (Chart 1). The trend in 1981 was much less dramatic, in part because of slackened import demand for capitol goods along with growing economic uncertainties. Only one major agency doubled its exposure, while most other agencies saw their exposure decline through the year. Nonetheless, there remained active interest in the market, as evidenced by the generally high levels of outstanding offers. Also, short-term commitments, as a ratio to national exports to Argentina, continued to increase and reached an average of 30 percent in 1981.

Policy Turning Point

Cover policies for most agencies were reversed abruptly in the second quarter of 1982. In reaction to the South Atlantic conflict in April 1982, seven agencies suspended cover for medium-term transactions; of these agencies, five also withdrew cover for short-term transactions, while the remaining two introduced highly restrictive conditions for short-term transactions. Three agencies did not actively adopt restrictive policies, adopting a wait-and-see attitude, but few applications were approved.

Normal cover policies were not resumed after the South Atlantic conflict ended in May 1982 and since then, for several reasons, policies have been tightened even further. The agencies generally attributed their pessimistic assessment to two sets of factors. First, the domestic economy—already weakened by the conflict—seemed to be deteriorating further in the absence of incisive economic management, coupled with the unsettled political situation. Arrears that had emerged at the time of the conflict remained large and were expected to rise further, making substantial claims payments unavoidable. Second, the external environment had begun to worsen substantively for Argentina, with the virtual closure of international capital markets to Argentina since the second quarter of 1982. The agencies progressively lowered their expectations of Argentina's short-term financial viability. In September 1982, Argentina began negotiations with the Fund on a financial program supported by a stand-by arrangement and initiated discussions with banks, initially on bridge loans and later on a bank debt restructuring. Agreements with the Fund and with the banks were reached in early 1983.

Overall, reflecting the agencies' perception of an increasingly uncertain outlook for Argentina and the large and rising arrears, these agencies were unwilling to become more flexible. For medium-term transactions, by the third quarter of 1982, the number of agencies off cover had grown from seven to nine and by the first quarter of 1983, all ten agencies were effectively off cover. While policies for short-term transactions had been more flexible, they remained quite restrictive. By the third quarter of 1982, only five agencies remained prepared to cover such transactions and only with restrictive conditions (such as total commitment limits, payment guarantee requirements, and a reduced percentage of cover).

A few agencies modestly eased their cover policies in early 1983, in response to some economic improvement and given that a Fund-supported adjustment program was put in place at that time. These steps proved short-lived, and virtually all the initial restrictive policy stances had been restored by June 1984.

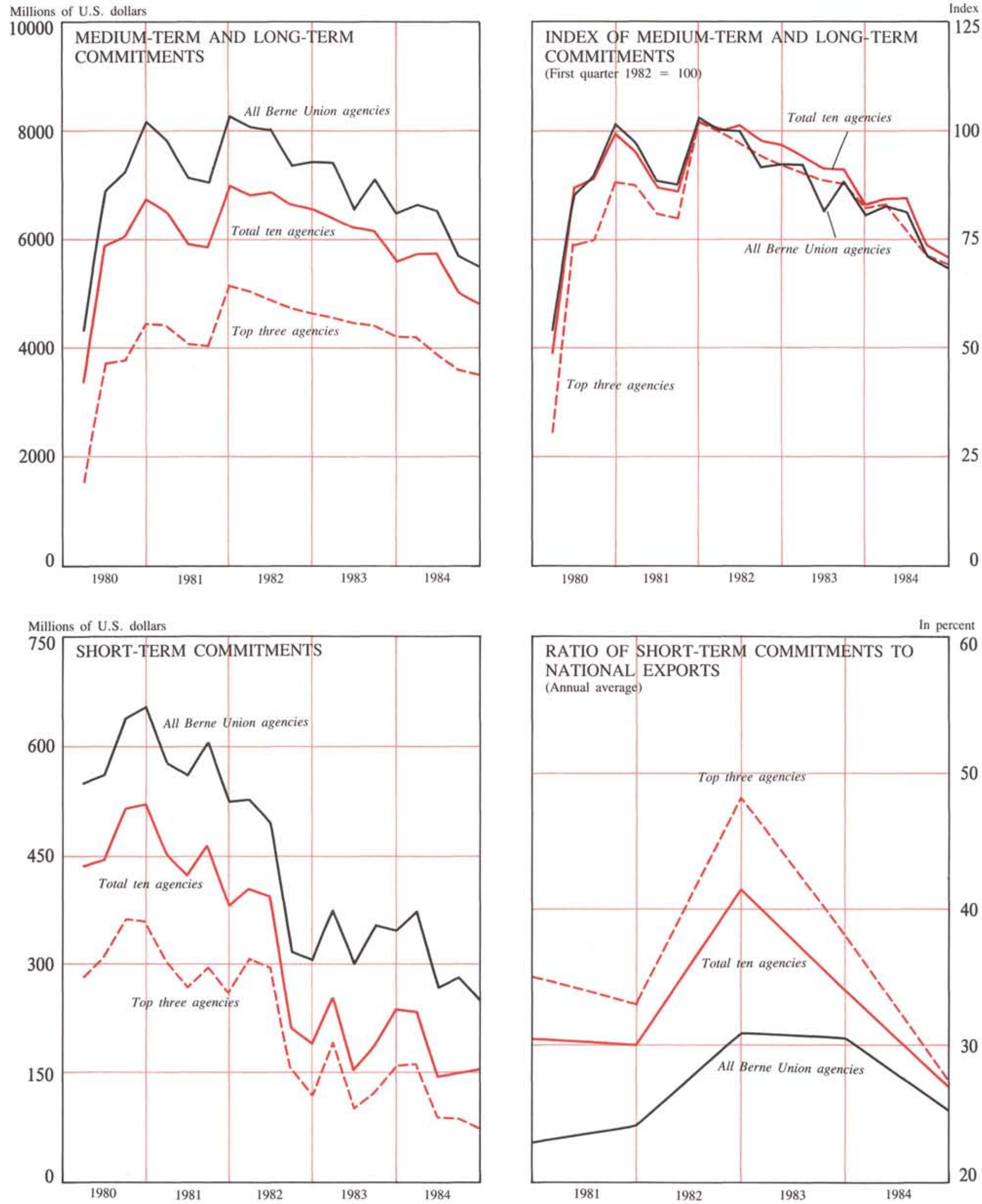
Trends in Exposure

The steady decline in outstanding commitments during 1982–83 were consistent with the restrictive cover policies of the agencies. Every agency's medium-term exposure in Argentina declined steadily during this period (Chart 1). The combined exposure of the top three agencies dropped by 9 percent in 1983; commitments of the ten agencies in aggregate (and also of all Berne Union agencies) showed similar movements over the period. The agencies indicated that only marginal new commitments were made. These were confined to exceptional or unique transactions (such as those related to pre-existing capital projects, tied to preliminary offers already committed, directly linked to foreign-exchange-earning projects with retention provisions, or projects with concessional aid financing components).

Short-term commitments (in U.S. dollar terms) for the agencies in aggregate also declined significantly during 1982–83. However, measured against the trade flows, short-term commitments in fact increased sharply in 1982, and then, even after declining in 1983 (at 34 percent of national exports), remained slightly higher

Chart 1. Argentina: Trends in Commitments, 1980–84

(End of period)



Sources: Data provided by official export credit agencies; and International Monetary Fund, *International Financial Statistics*, and staff estimates.

than in 1981. This overall pattern can be attributed to three agencies (including the top agency in the market) that maintained comparatively more flexible short-term cover policies; a significant shift in the market share in favor of these three agencies has occurred as a result.

Prospects and Issues

Until late 1983, there had been no discussion of a rescheduling of debt owed to official creditors, and the banks had not made such a rescheduling a condition for their own undertaking. However, owing mainly to the accumulation of arrears, the seriousness of the bank debt problems, and Argentina's worsened economic outlook, the agencies' policies have been severely restrictive.

An approach to the Paris Club for a debt rescheduling was signaled in early 1984, although at the time the Argentine proposal left unclear the scope of debt to be rescheduled. With the possibility of rescheduling short-term debt, some agencies that had previously been prepared to consider cover for short-term transactions were then obliged to withdraw short-term cover. By June 1984, all agencies were off cover formally or effectively for medium-term transactions, and over half of the agencies were also off cover on short-term transactions.

Brazil

Debt Buildup Phase

Cover policies for Brazil during the period 1981 through late 1983, when a major policy shift occurred, may be characterized as moderately restrictive. For medium-term transactions, all agencies were on cover, but eight agencies imposed some form of restriction to control exposure. These restrictions included (for four agencies) a case-by-case consideration of applications, a reduced percentage of cover, and limits on commitments (total outstanding, or new annual commitments, or on the size of individual transactions). Policies for short-term transactions were quite liberal, with restrictions imposed by only two agencies. While this overall policy stance reflected in part the uneven economic performance of Brazil in the early 1980s, several agencies attributed their cautious attitudes to the magnitude (in both absolute and relative terms) of their exposure in Brazil and their desire to limit further increases in an effort to improve portfolio balance. A few agencies have tended to follow restrictive policies as they viewed difficulties in Brazil's debt-servicing prospects (after the second oil shock) to be more than temporary.

Beginning in late 1982, the agencies were becoming uneasy with the overall situation. Brazil's latent payments difficulties were at that time exacerbated by the general cutback in bank lending following the liquidity crisis in Mexico of August 1982, and the agencies began to adopt a more critical view of the sustainability of Brazil's heavy debt burden. However, also in late 1982, Brazil began discussions with the Fund on an adjustment program and approached the banks for a refinancing arrangement. At that time, Brazil did not approach the official creditors for debt relief, and an official debt rescheduling was not generally regarded as essential. In early 1983, agreements were concluded with the Fund on a three-year adjustment program and with the banks on a refinancing package. Against this background, by the first quarter of 1983, only four agencies shifted to a more restrictive stance; by then, only one agency had withdrawn cover on medium-term transactions.

As 1983 progressed, however, some arrears to creditors were emerging, and there was extensive publicity of Brazil's economic problems. First, Brazil was experiencing difficulties in adhering to the targets and complying with the conditions of the Fund-supported adjustment program. Second (and related to the difficulties with the adjustment program), commercial banks were reluctant to meet fully Brazil's liquidity needs, and there were growing uncertainties about the package assembled by banks to meet Brazil's 1983 financing needs. Notwithstanding these signs, most agencies did not shift to a more restrictive policy stance.

Policy Turning Point

In the last few months of 1983, the policy switch for all but one of the agencies was directly attributable to Brazil's rescheduling of its Paris Club debt. Following months of increasing uncertainties, the agencies received first indications in August 1983 that a Paris Club rescheduling would be necessary. By September, the approach to the Paris Club was confirmed; the request for rescheduling was received in October, and the Fund-supported adjustment program was reactivated after a five-month interruption. The multilateral rescheduling agreement, reached in November, provided for a rescheduling of arrears and maturities (on medium-term debt) due from August 1983 to December 1984, broadly along standard Paris Club terms.

Changes in the agencies' cover policies for Brazil were well synchronized with the events relating to the Paris Club rescheduling. During the third quarter of 1983, upon the first report of the need for such a rescheduling, most agencies moved to tighten policies (e.g., downgrading the market and reducing the country commitment limits), adopted a wait-and-see attitude, and generally delayed decisions on new medium-term business. Some agencies noted that at that time there was no pressing need for them to quickly impose formal restrictions on medium-term transactions, since credit demand was already being effectively curbed by reduced import demand in Brazil. On short-term transactions, over half of the agencies remained on cover; some transferred transactions to special national interest accounts and monitored more closely their position. For these agencies, more stringent conditions were not considered necessary, since short-term debt was believed to be precluded from the rescheduling and efforts were being made by Brazil to keep current on such obligations. A few agencies, however, introduced more restrictive conditions on short-term transactions (requiring transfer guarantees or imposing tight revolving limits), primarily reflecting their own experience of transfer delays on such transactions.

By the time of the Paris Club request (and in any event no later than November 1983, when the agreement was reached), seven agencies formally or effectively withdrew cover on medium-term transactions. Three agencies remained on cover: one because of national interest considerations and a favorable view of Brazil's long-term prospects, and the other two because flexibility was considered practical given their relatively moderate exposure in the market.

Regarding short-term transactions, only one agency formally withdrew cover and only because of its standard requirement at the time to withdraw all cover in cases of rescheduling; this requirement has been eased. For all other agencies, some forms of restriction continued to be applied, but for some agencies these restrictions appear to have been slightly eased by the middle of 1984.

Trends in Exposure

The data suggest that agencies were generally unsuccessful in their efforts to contain exposure as risk deteriorated in 1983. In line with the increase in demand for cover, as exporters perceived growing risk in trade with Brazil, the agencies' commitments grew strongly in the year approaching the policy turning point in late 1983. For the ten agencies, aggregate outstanding commitments rose by 8 percent on average in 1983, after having fallen in the preceding year; the top three agencies in the market experienced a similar increase in commitments (Chart 2).

The trends for short-term commitments, while similar, were even more pronounced. Whereas trade flows to Brazil in 1983 contracted sharply (by about 20 percent for this group of ten countries), aggregate short-term commitments of these ten agencies in 1983 were almost 20 percent higher than in 1982, with all of the increases attributable to the top three agencies in the market. By 1983, for the ten agencies, short-term commitments as a ratio to national exports reached 34 percent (compared with 23 percent in 1981) and for the top three agencies, the ratio rose even higher, to 40 percent. These ratios continued to rise in 1984, although not quite so sharply as in 1983.

Prospects and Issues

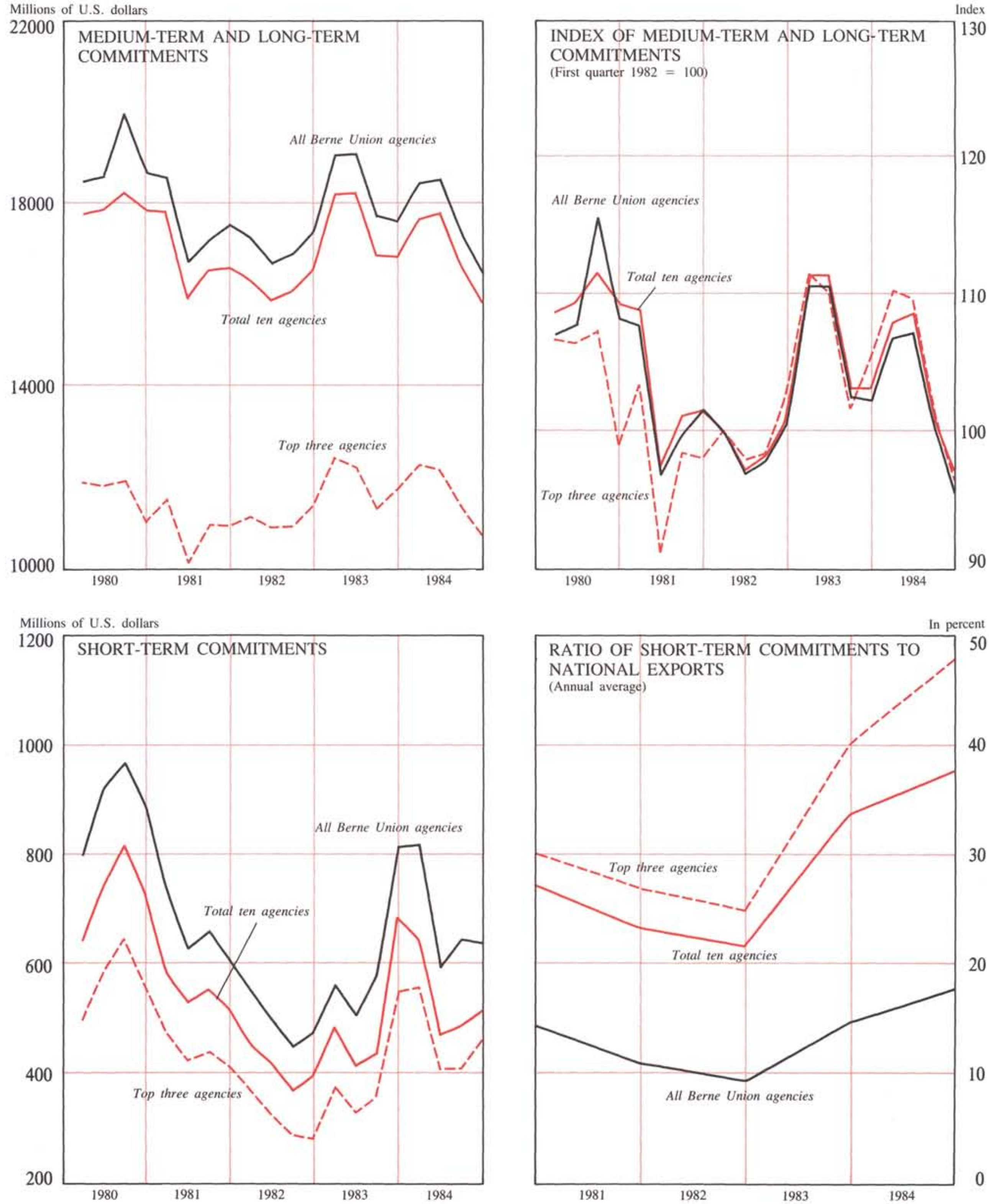
At the same time as the Paris Club rescheduling, efforts were being made to arrange a concerted financing package among some of the agencies. The package was conceived as part of an overall balance of payments financing arrangement and entailed the pledging of target amounts of insurance/guarantee by participating agencies or the national authorities concerned. Support for this concerted package was mixed, with only two agencies expressing unqualified interest. For most participating agencies, the facility had not yet been activated and considerable delays had been encountered in the practical arrangements. For the few agencies that were ready to provide such assistance, there had not been adequate demand for medium-term project financing and the facility remained largely unused. A few agencies also indicated that the facility could be redundant in providing short-term cover insofar as they were already prepared to continue short-term cover. Some agencies considered that trade financing was inappropriate for filling a balance of payments gap.

A notable feature of the agencies' experience with Brazil was their apparent willingness to continue supporting short-term transactions. As is evident from Chart 2, and as noted earlier, most agencies allowed significant increases in short-term commitments through 1984 and appeared to be covering a much greater proportion of trade. (This pattern is followed—to a lesser degree—by Nigeria and the Philippines, but is in contrast to the experience of Mexico; see below.) The agencies' willingness was attributed in large measure to Brazil's effort at redressing its economic problems and the exclusion of short-term debt from the Paris Club rescheduling.

Most of the agencies maintained cautious policies on short-term transactions, and some felt that increases

Chart 2. Brazil: Trends in Commitments, 1980–84

(End of period)



Sources: Data provided by official export credit agencies; and International Monetary Fund, *International Financial Statistics,* and staff estimates.

in demand for cover needed to be held in check. A few agencies thought that the debt-servicing problems in Brazil might be long term and that further reschedulings could not be precluded. Some wished to be cautious, since their outstanding commitments were regarded as already too high. One agency introduced revolving limits on short-term commitments designed to accommodate only traditional exporters or existing whole-turnover policyholders, and to preclude abnormal (e.g., transit trade) or rising demand. Revolving limits were thought especially useful in being self-correcting since the limits would be automatically used up if payments were not made in time. Another agency indicated that, while revolving limits or letters of credit conditions had not been imposed, these restrictive conditions could be introduced, should the cutback in the availability of medium-term credit spill over into an excessive increase in demand for short-term cover.

Madagascar

All of the agencies reported that since Madagascar's first Paris Club debt rescheduling in April 1981 they have suspended cover for Madagascar on all transactions. None of the agencies could suggest that cover might be resumed in the foreseeable future. A number of agencies had become cautious before the 1981 Paris Club rescheduling and had already attempted to limit exposure.

Over the last three years, a few agencies had provided cover on an exceptional basis for essential imports financed under government lines of credit; cover has also been provided for preshipment risks on projects that are aid-financed. Two agencies reported that periodically unique transactions have been covered on a limited scale. For some agencies, ad hoc arrangements for short-term cover have at times been made as a temporary substitute for cover on the state account, when short-term cover was not admissible on the state account. One agency reported retaining cover on short-term transactions, but only with irrevocable letters of credit confirmed prior to the dispatch of the goods by an acceptable bank outside Madagascar. Some agencies also suggested that in this type of market, after years of restriction, demand for cover had in fact become minimal as the market had grown reliant on cash rather than credit.

The agencies considered their cover policy decisions for Madagascar to be relatively clear-cut for two reasons. First, the overall economic situation was regarded as extremely difficult at that time and over the longer term. The debt-servicing difficulties were thus seen as both severe and chronic. Large arrears have accumulated and there were concerns that Madagascar may have difficulty meeting the rescheduled obligations. Second, commercial interest was rather limited, since the market was relatively small. In these circumstances, there seems to be no real dilemma for agencies in balancing risk against competitive interest, and a prudent risk-taking attitude was practical.

Some agencies suggested that the problems of the type faced by Madagascar might better be solved through the provision of direct development assistance, rather than indirectly through exceptional provision of export credits. The main drawback of providing assistance through the export credit system was that the concessional terms and conditions could be seen as precedent-setting and could complicate the rescheduling approaches for other countries. As Madagascar is not included in the countries reported to the Berne Union Secretariat, this section does not contain a description of terms of cover nor an analysis of exposure trends.

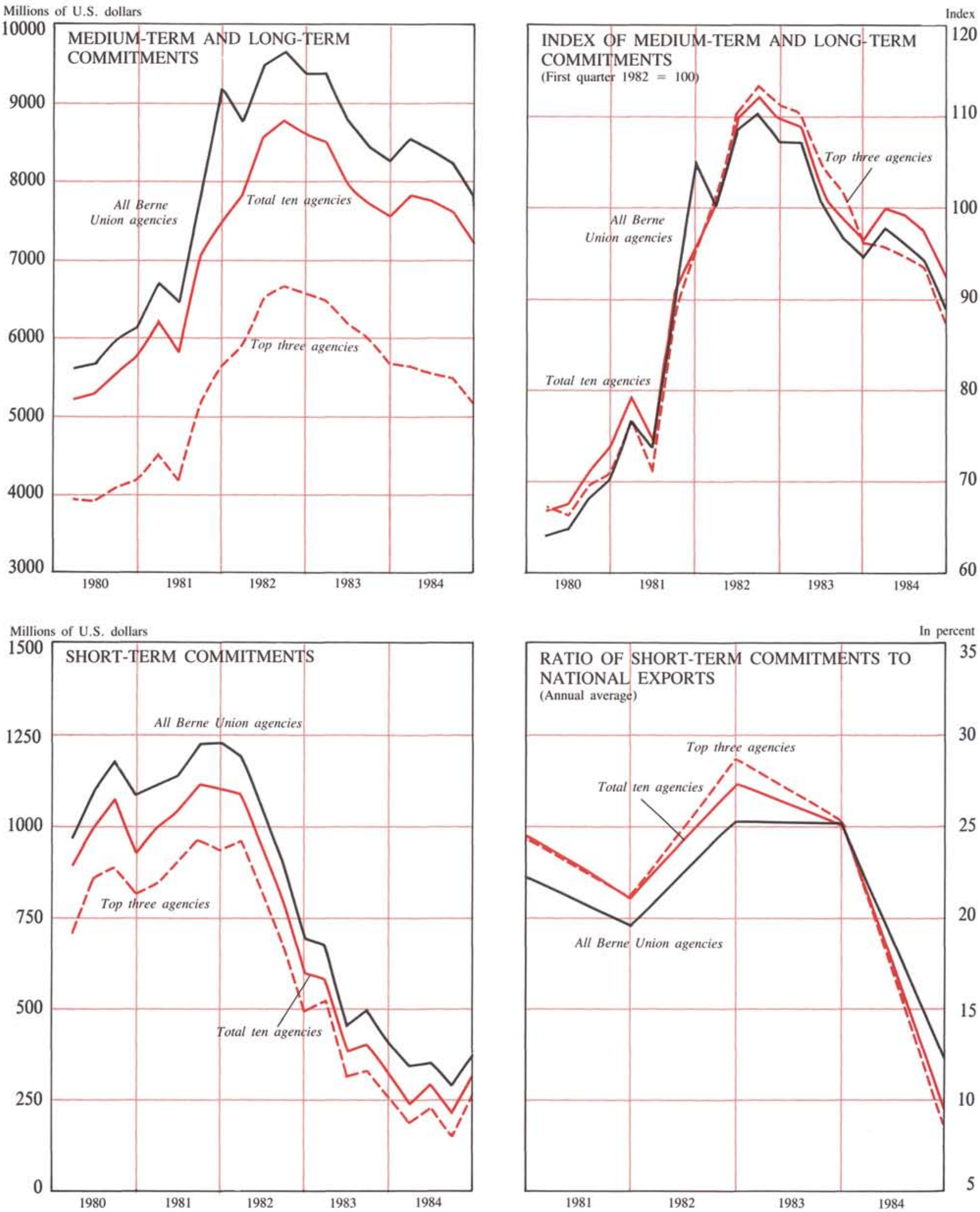
Mexico

Debt Buildup Phase

The debt difficulties of Mexico, which reached a critical stage in August 1982, caught most of the agencies by surprise. The severity of the problem had been underestimated by the agencies in part because the information system on debt (especially on short-term) was too deficient to provide reasonably convincing evidence of deteriorating risks. Also, Mexico's virtual cutoff from access to international capital markets could not have been anticipated. All of the agencies remained on cover without any effective restrictions, and Mexico had generally been rated a better country risk than most developing countries. As a result, commitments of all but two smaller agencies grew strongly in the one-year period approaching the liquidity crisis in August 1982: during the one-year period ending in the third quarter of 1982, total medium-term commitments of the ten agencies rose by 24 percent, and for the top three agencies in the market the increase was even larger at 29 percent. Similarly, the agencies' short-term commitments as a percentage of the countries' exports to Mexico rose steadily from about 21 percent in early 1981 to a peak of 33 percent in the third quarter of 1982 (Chart 3).

Chart 3. Mexico: Trends in Commitments, 1980–84

(End of period)



Sources: Data provided by official export credit agencies; and International Monetary Fund, *International Financial Statistics*, and staff estimates.

Policy Turning Point

Most agencies reacted to the liquidity crisis of August 1982 by adopting a moderately restrictive policy; the exception was the largest agency in the market, which remained open without restrictions. On medium-term cover, except for one major and two smaller agencies which withdrew cover, other agencies remained open with some restrictions, often with limits on total new commitments (sometimes supported by limits on transaction size) and confining new cover to the public sector borrowers or borrowers with public guarantees. For agencies where the practice is feasible, Mexico was downgraded to the country category with higher premium charges. Where applicable, transactions were transferred to the national interest account.

In late 1982, agreement was reached with the Fund on a three-year adjustment program, and debt restructuring negotiations began with the commercial banks. At that time, there was also a coordinated effort among the monetary authorities of the major creditor countries to assist Mexico. However, a multilateral rescheduling of debt owed to official creditors was not then envisaged. For six agencies in the market, their medium-term and long-term cover policies were in the context of this informal coordination effort related to Mexico's adjustment program with the Fund. On short-term business, only one agency withdrew cover, but not until the third quarter of 1983, following the Paris Club rescheduling—in line with its standard practice at the time for rescheduling cases and a practice that has since been modified.

Policy Response to Creditor Group Rescheduling

An approach to official creditors was first made in May 1983, and the multilateral rescheduling agreement was reached in June 1983. As a minimum response, and at the latest by the multilateral rescheduling agreement date, most agencies withdrew cover for the type of debt that was subject to rescheduling, that is, the private debt not guaranteed by the Mexican Government, either through a formal announcement or informally through requiring guarantees of the public sector (including banks). At the time of the staff discussions with the agencies, very few agencies had finalized their bilateral agreements, the delays having been caused by the apparent complications in the assumption by the Mexican authorities of the commercial risk of the private debt that became rescheduled.

For most agencies, it was possible to avoid an unduly restrictive policy stance, for several reasons. First, the financial difficulties in Mexico were seen to be of a liquidity nature. Medium-term prospects were regarded as fundamentally favorable, given the country's resource base and the fact that a Fund-supported adjustment program was put in place promptly to redress the temporary problem. Second, for one of the major agencies, its ability to stay open on cover with minimal restrictions was attributed in part to effective communications, at the initiative of the Mexican authorities, concerning their adjustment program and their intentions on the type of debt to be rescheduled. Third, for another major agency, a positive factor was that its exposure was relatively small and there was scope on portfolio consideration to increase exposure. For all of the agencies, their ability to be open on cover on medium-term for public or publicly guaranteed buyers was influenced by the fact that such debt had been excluded from the 1983 official creditor reschedulings. Fourth, in September 1983, one major agency announced a special guarantee/insurance facility of $500 million to assist Mexico; this facility was expected to be in force in the near future.

Trends in Exposure

The moderately restrictive policy of the export credit agencies, together with the weakened import demand in Mexico, led within one year to a sharp contraction in the agencies' exposure in Mexico. The volume of outstanding offers plummeted to 30 percent of the previous average, and medium-term commitments declined for virtually all agencies. Within one year after the policy turning point, outstanding medium-term commitments of the ten agencies in aggregate dropped by 10 percent; the same decline was experienced by the top three agencies. More important and somewhat surprising, short-term commitments also fell, from an average of 27 percent of national exports in 1982 to 25 percent in 1983—a level which nonetheless was slightly above the average in the early 1980s. These declining trends continued to be evident in 1984.

Prospects and Issues

For 1984, most of the agencies appeared to favor at least a continuation, and for some an easing, of the 1983 policies. There was a general feeling that for 1984 a coordinated approach on export credit (formally or informally) would not be necessary. Factors contributing to the increasingly positive attitude of the agencies include Mexico's good economic performance, its compliance with the Fund-supported adjustment program, and the exceptionally short consolidation period (six months). Some of the agencies seemed to be aiming at further increases in commitments for 1984; two agencies have transferred transactions from the

national interest account back to the commercial accounts. Among the agencies that were off cover in 1983, several had restored cover on all business by June 1984, although some restrictions continued to apply, especially for transactions with the private sector in Mexico. For most agencies, one important outstanding issue at the time of the staff visit discussions with the authorities concerned was the resolution of the complications of private nonguaranteed debt and the consequent delays in concluding bilateral agreements to implement the multilateral rescheduling agreement.

Nigeria

Debt Buildup Phase

Among the countries in the study, the experience with Nigeria best exemplifies the inherent difficulties in containing exposure in a market of large commercial interest and one without persistent and substantial claims payouts. In this example, agencies did not react consistently to the adverse leading economic indicators. Over half of the agencies were unable to resist exporter and competitive pressures and permitted exceptionally large and steady increases in commitments, despite the signs of weak economic management and rising payments arrears.

During the period 1981 through the first half of 1983, the cover policies for most of the agencies may be described as moderately restrictive. For most of them, medium-term cover was confined to transactions of the public sector or those with public sector guarantees; the public sector was strictly defined by that time and was confined generally to the federal government and excluded local governments. Some agencies attempted to contain growth in exposure by imposing some form of commitment limit which, however, often proved ineffective and had to be raised under intense demand pressure. On short-term transactions, most agencies were already requiring lengthy claims-waiting periods ranging from six months to one year. Such requirements were, however, traditional for Nigeria and reflected administrative bottlenecks in Nigeria and the resultant difficulties in effecting payments on time. For most agencies, no especially restrictive actions were reported as having been adopted to restrain short-term commitments in response to growing difficulties. Irrevocable letters of credit were a frequent requirement, but proved inadequate in curtailing exposure since there was no effective control over the issue of such documents in Nigeria during this period.

Beginning in the second half of 1982, economic and financial developments began to deteriorate when the outlook for the world oil market and Nigeria's financial prospects were becoming less favorable—especially with considerable uncertainty regarding the magnitude of the decline in oil prices that would ensue. Over the short term, transfer delays became longer and more persistent, and the amounts involved were significantly larger than under normal administrative delays. Also, substantial arrears were emerging for other creditors such as banks and noninsured suppliers. Domestically, there were few signs of corrective policy actions to compensate for the worsened environment: national elections were due shortly deferring a clear shift in policy direction until the new government was installed.

Against this background, only four agencies (one among the top three in the market) attempted in mid-1982, with some success, to restrict cover. For medium-term transactions, new offers were suspended, the market was downgraded, and more stringent selection criteria were applied to confine credits to essential infrastructure and direct foreign exchange earning projects. In practical terms, one agency was effectively off cover, in that decisions were no longer being made on applications; for two other agencies, most applications were being rejected almost routinely. For short-term transactions, tight individual limits were initially imposed. Later, the medium-term outlook worsened, and there were no prospects for an early Fund-supported adjustment program. By early 1983, at least one agency reported the imposition of the strict requirement of confirmed irrevocable letters of credit and confined short-term cover to essential imports such as raw materials and spare parts. Finally, in January 1983, one major agency formally withdrew cover for private buyers following substantial claims payouts.

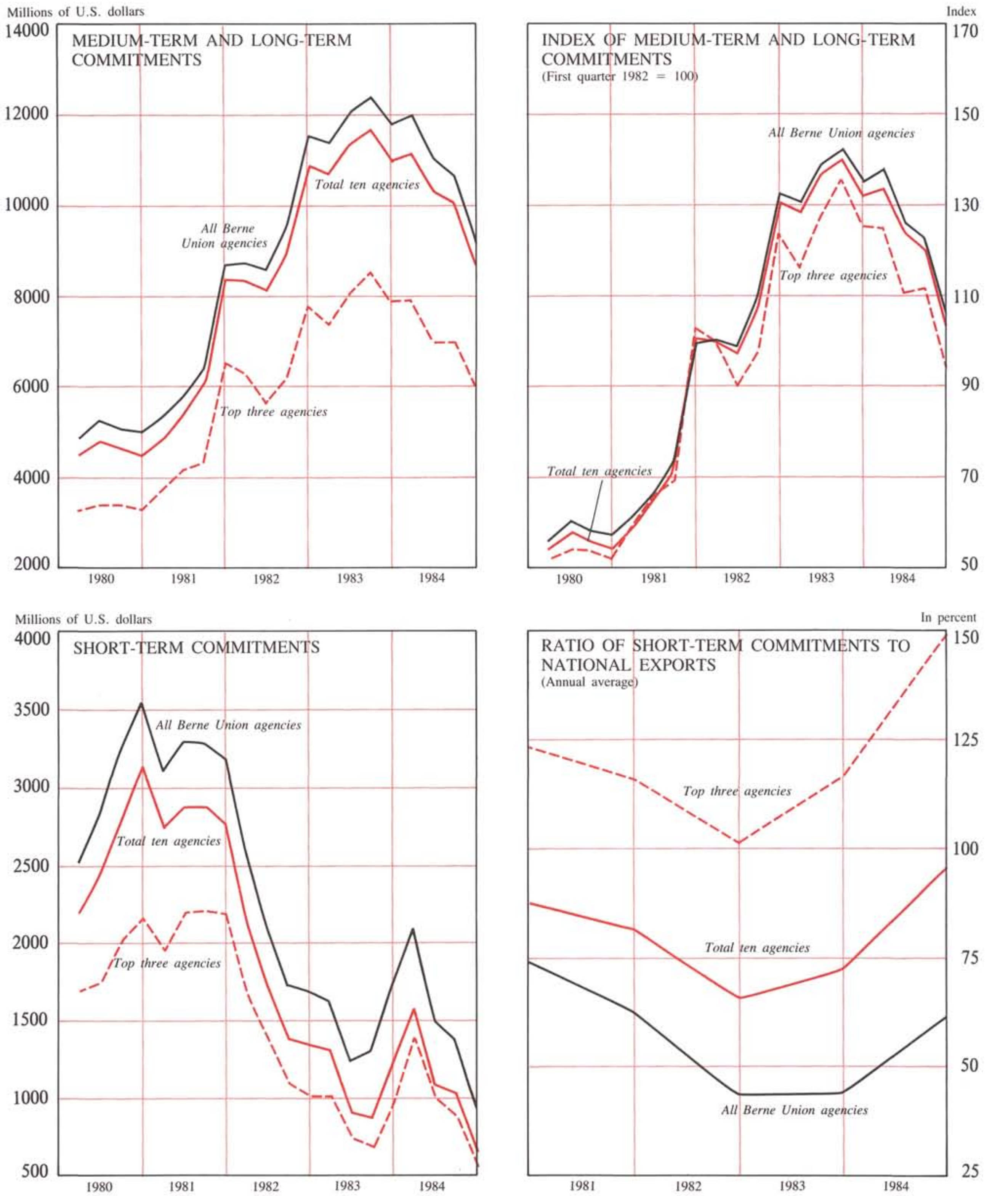
Half of the agencies did not report that they reacted significantly to the deteriorating situation. Initially, they maintained relatively favorable attitudes toward Nigeria, which reflected their confidence in the oil resources. The difficulties were initially expected to be short-lived, much like the wave of temporary financial problems that occurred between the two oil shocks in the mid-1970s. Later, even with the bleaker medium-term outlook, there remained strong commercial interest in the market and competitive pressures precluded agencies from reacting more decisively.

Trends in Exposure

Analysis of available data indicates a remarkable degree of correlation between the reported policy

Chart 4. Nigeria: Trends in Commitments, 1980–84

(End of period)



Sources: Data provided by official export credit agencies; and International Monetary Fund, *International Financial Statistics*, and staff estimates.

stances and the trends in commitments. More so than with other countries in the study, the agencies with restrictive policies (relative to others) succeeded in containing risk, while agencies with comparatively relaxed practices experienced large increases in their exposure. Overall, a significant shift in market shares is in evidence since 1982. The net effect of the two trends in exposure, however, was a significant increase in total commitments for Nigeria (Chart 4). On aggregate, medium-term commitments of the ten agencies grew by 47 percent in 1982 and further by 23 percent in 1983. Short-term commitments, measured relative to trade flows, fell in 1982, but rose significantly in 1983—especially for the top three agencies in the market. This short-term trend is noteworthy because for several agencies short-term arrears were already significant and mounting in 1983. Since the first quarter of 1984, however, short-term commitments have declined uniformly across agencies. Relative to trade flows, short-term commitments in 1984 remained, on average, higher than in most recent years.

Prospects and Issues

Since early 1984, all of the agencies had moved effectively to restrict cover. The reasons cited for this shift were, first, by the end of 1983, the need for a Paris Club debt rescheduling was seen clearly by creditors; second, there were now generalized payments arrears and rescheduling discussions with banks and noninsured creditors; and, third, the economic situation seemed to be deteriorating and the negotiations with the Fund on an adjustment program became protracted.

Nigeria's payments difficulties were centered on short-term maturities, and there were indications that Nigeria would seek to reschedule only short-term arrears and current short-term obligations contracted before a specified date. Although there had not been a request for a rescheduling of medium-term obligations, the agencies were cautious. Most of them either formally or effectively withdrew cover on medium-term transactions; one agency was on cover, but only with severely restrictive terms which included costly premium surcharges. Regarding short-term transactions, despite the need for a rescheduling of short-term arrears, a few agencies remained on cover, albeit on a restricted basis, for example, with revolving commitment limits, presumably because of the Nigerian Government's pledge to keep current with post-1983 maturities. Reflecting this policy stance, while medium-term exposure has begun to moderate, short-term commitments relative to trade flows continued to increase, especially for the top agencies in the market in 1984.

Peru

Resumption of Normal Policies after 1978 Rescheduling

The Paris Club agreement for Peru was concluded in November 1978 and provided for a rescheduling of medium-term principal payments due over a fifteen-month consolidation period. During 1978, agreement was also reached with the Fund on a two-year stand-by arrangement and rescheduling agreements were concluded with banks and other official creditors. With the Paris Club rescheduling, all agencies, as customary, withdrew cover for medium-term transactions and imposed restrictive conditions for short-term business.

The interval of cover interruption was exceptionally short—probably too short in the view of some of the agencies. Cover policies were eased significantly only one year after the Paris Club agreement. As early as the first quarter of 1980, all of the agencies had resumed medium-term cover, although most with some moderately restrictive conditions; one agency among the top three in the market was open for cover without any restriction. As for short-term transactions, over half of the agencies had been open fully ever since the fourth quarter of 1979; it is noteworthy that, for one of these agencies, this liberal move was taken in exception to its normal policy and was regarded as an "advance" reopening. From 1981 through the first half of 1982, agencies maintained, and a few were able to ease further, their generally relaxed policy stance.

The agencies attributed their flexibility in the case of Peru to the following factors. First, in 1979, there was a dramatic improvement in the economic and balance of payments performance, which reflected, in large part, the copper price boom. Further gains in export earnings and a large balance of payments surplus were registered in 1980. The political environment was also stabilized with the new government which was elected in early 1980. Second, in view of the strong external payments position, in late 1979 the Peruvian authorities decided to forgo the 1980 reschedulings, which had already been agreed in principle with official creditors and banks provided Peru complied with the Fund-supported program. Furthermore, Peru was able to make advance repayments of the amounts rescheduled—another factor which was regarded by the agencies as highly positive.

Overall, the agencies were able to ease cover policies in line with these favorable developments. A few of the agencies indicated that, at the time, they viewed with skepticism the permanence of Peru's financial improvement, since it was based heavily on volatile copper prices. Nonetheless, given strong exporter interest and competitive pressure, these agencies could not persist in restricting policies against the majority view.

Trends in Exposure

As to be expected, the agencies' exposure began to increase in line with the easing trend in their cover policies (Chart 5). For the ten agencies in aggregate, medium-term commitments grew by 15 percent in 1980 and further by 9 percent in 1982. The trends for short-term exposure were less pronounced, primarily because the policy shift was much less noticeable.

Policy Turning Point

Beginning in 1982, the agencies' attitudes toward Peru became less favorable. Domestically, the economic improvement proved to be short-lived, and by early 1982 the medium-term prospects began to weaken. Externally, the regional Latin American debt problem which occurred during the latter half of 1982 was creating additional concerns about Peru's debt-servicing ability. In June 1982, a two-year stand-by arrangement with the Fund was put in place. Throughout 1982, the agencies maintained their liberal policy stances; for the few agencies that reported some adjustment in their cover policies, their actions were primarily in the context of agency-wide policy adjustment in the wake of the Mexican liquidity crisis.

In 1983, the economic situation deteriorated further. By the beginning of the second quarter of 1983, after the confirmed report that Peru would seek a Paris Club rescheduling, agencies began to tighten cover policies. By the end of the second quarter, four agencies effectively withdrew cover for medium-term transactions in advance of the Paris Club rescheduling which took place in July; two agencies delayed such action until the fourth quarter of 1983—almost half a year later. On short-term transactions, all agencies but one remained open for cover with moderately restrictive conditions.

Despite the Paris Club rescheduling, four agencies were able to maintain cover for medium-term commitments without severely restrictive conditions; applications were considered on a case-by-case basis and payment guarantees were required. This relatively liberal policy stance was adopted by one other agency that had initially withdrawn cover. For these agencies, the relaxed policy was maintained until early 1984.

Among the agencies that remained relatively liberal, by early 1984 their cover policies were being significantly tightened, primarily in response to Peru's evident need for another Paris Club rescheduling. About half of the agencies had by June 1984 withdrawn cover for medium-term transactions, while others expressed very cautious attitudes. Aside from the 1984 Paris Club rescheduling, other factors cited by some agencies for their actions included the difficulties in concluding the implementing bilateral agreements, the emergence of payments arrears to some of the agencies, and the periodic complications facing Peru in implementing the Fund-supported adjustment program.

Prospects and Issues

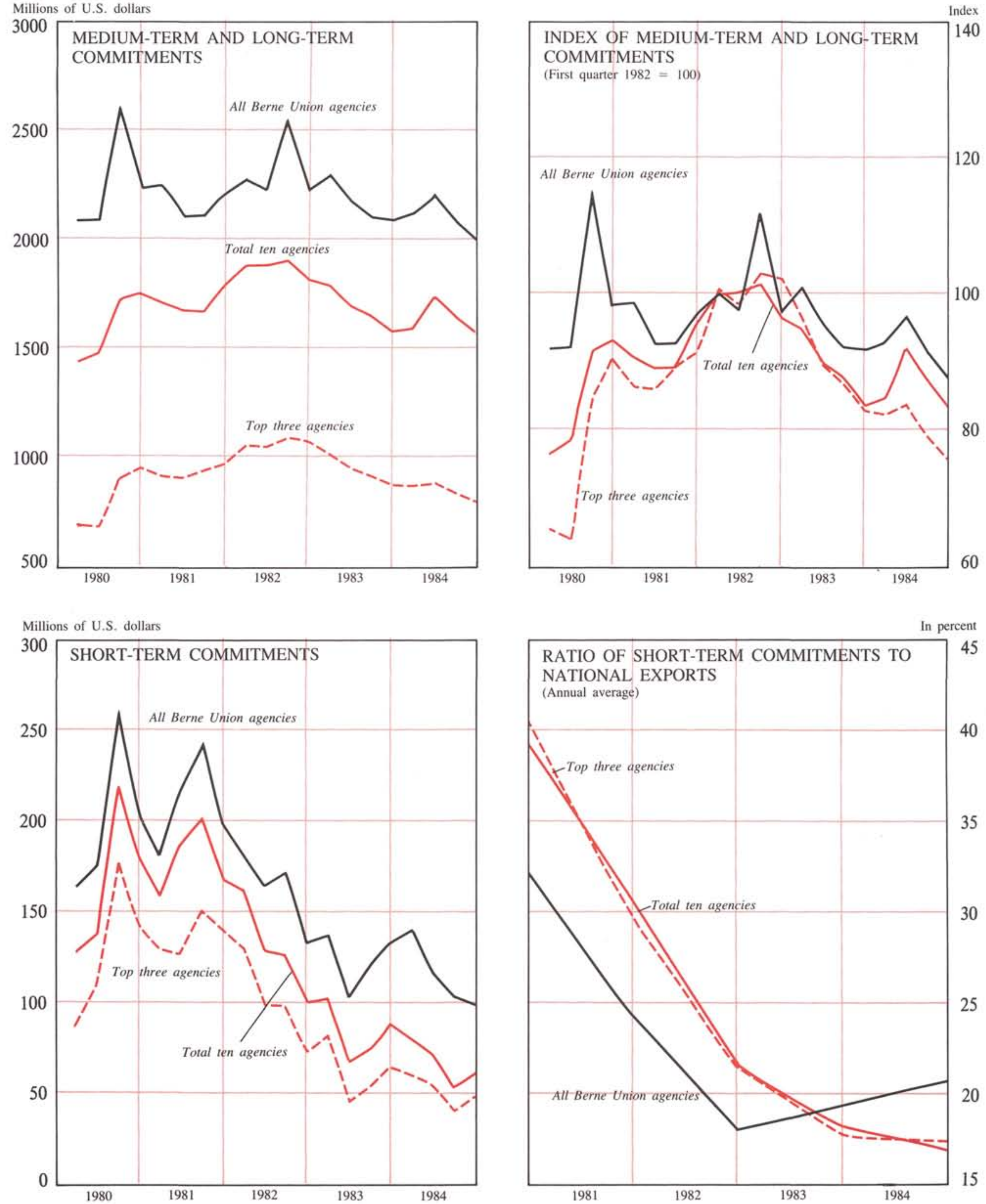
Notable features of agency experience with Peru were, first, the absence of uniform customary reactions to the 1983 Paris Club rescheduling, and second, the apparent weak link between Peru's approach to debt rescheduling and some agencies' willingness of accommodation in their cover policy stance.

In discussing policy responses to the 1983 Paris Club rescheduling, the agencies that either had not withdrawn cover, or had significantly delayed such action, gave various reasons for their decisions. Two agencies suggested that the overriding consideration was commercial, given their relatively large exposure, both in terms of the agencies' own portfolios and the market share; this important commercial interest was further buttressed by their own good claims experience with Peru. The same kind of reasoning led another agency to restrict cover policies in an attempt to correct its market share that was viewed as excessive. One agency took the unusual decision not to go off cover, partly as an experiment for more flexibility in the circumstances of generalized debt-servicing difficulties. It was felt that the experiment was justified since economic information at the time suggested that Peru's problems were temporary and, in any case, the commercial interest was such that any cover suspension probably could not have been maintained for long. Finally, one agency felt that a formal off-cover position was not needed since demand was already slack.

Concerning Peru's approach to the 1983 Paris Club debt rescheduling, most agencies did not react negatively to Peru's initially unclear intention concerning short-term debt, and maintained fairly liberal policies for short-term cover. This relatively relaxed policy stance was reflected in the slight but temporary increase in short-term commitments during 1983.

Chart 5. Peru: Trends in Commitments, 1980–84

(End of period)



Sources: Data provided by official export credit agencies; and International Monetary Fund, *International Financial Statistics*, and staff estimates.

Philippines

Debt Buildup Phase

Developments in the case of the Philippines are notable for the exceptional degree of concentration in this market. For medium-term exposure, the top three agencies account for over 80 percent of the market, and the share of each of the top two agencies is over 35 percent. For short-term exposure, the top agency's share alone is over 80 percent. Thus, except for the top two agencies, the Philippines is regarded by other agencies as a relatively small market in both absolute and portfolio terms.

The agencies reported first signs of economic and financial deterioration in late 1982/early 1983, and there were increasing concerns over the rapid debt buildup. Cover policies of all of the agencies, however, remained liberal. Mild conditions continued to apply to medium-term cover, and for short-term transactions nine agencies remained fully open; for the one agency with restrictions on short-term transactions, it was in the form of a transaction limit that seemed adequate for its market activity. For most agencies, as noted above, exposure was limited in both absolute and relative terms, and a further increase in risk was felt manageable. Only one agency indicated that it was able at that time to reduce its new commitments limit, on the basis of its unfavorable medium-term assessment of the country.

Policy Turning Point

In September 1983, in response to the weakened political situation in the Philippines, and after the full extent of the country's financial difficulties emerged, one agency moved to tighten policy slightly. In the following two months, the economic situation of the Philippines deteriorated rapidly, capital flight accelerated, and reserves quickly diminished. As a result, the Philippines requested a bank-debt moratorium and approached the Paris Club in November 1983. At that time, seven agencies—all with marginal existing commercial interest in the market— withdrew cover (formally or effectively) on medium-term transactions. For short-term cover, these agencies introduced restrictive conditions that included overall revolving limits, reduced transaction limits, requirements of public guarantee in the Philippines, extended claims-waiting periods, and cover confined to transactions on letters of credits. One agency also withdrew cover on short-term transactions.

By mid-1984, only two agencies remained on cover on medium-term transactions. One of these agencies considered its exposure sufficiently small and elected to maintain cover on all maturities for the traditional exporters. One of the top agencies in the market remained on cover for transactions with the public guarantee of the Philippines and/or conditions of irrevocable letters of credit, and applications were considered on a case-by-case basis. The reasons cited for this flexibility were national interest considerations, the slack demand for imports that needed medium-term support, and the fact that exposure could be effectively monitored since irrevocable letters of credit were being issued under strict control within the Philippines.

Trends in Exposure

An unusual feature of the agencies' experience with the Philippines is the absence of large (and broad-based) increases in the levels of commitments in the period approaching the policy turning point. Aggregate medium-term and long-term commitments of the ten agencies rose by 5 percent on average during 1981–82, and actually declined marginally in 1983 before the policy turning point later in that year (Chart 6).

Comparatively, this trend is considerably more moderate than the experience of most other debtor countries in the study. Furthermore, there was a sharp contrast in the agencies' experiences even though they maintained a similar policy stance during this period. Virtually all of the increases in commitments for the group occurred only for the top two agencies in the market. The other eight agencies, with their liberal policies, saw steady declines in their exposure over this period. By the fourth quarter of 1983, however, exposure of all ten agencies fell, and at an average annual rate of 12 percent.

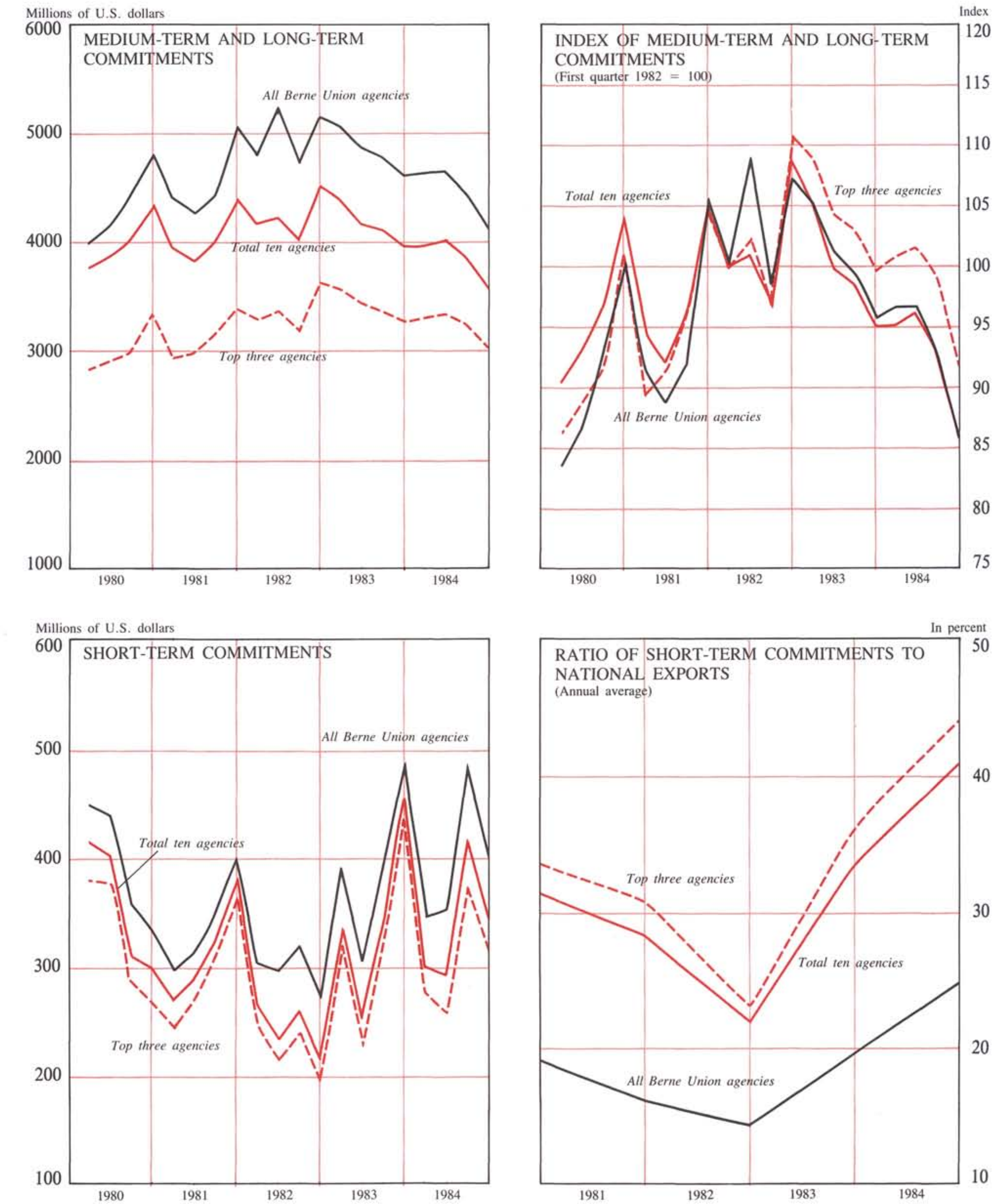
The trends for short-term commitments suggest a significant increase in demand for cover in the months ahead of the policy turning point. In particular, for the top three agencies (together accounting for over 90 percent of the market), their short-term commitments measured against their national exports jumped from 23 percent in 1982 to 37 percent in 1983. As the year progressed, there were even sharper increases in short-term commitments for the top two agencies that remained comparatively more liberal than the other agencies. In 1984, short-term commitments on average were at about the same level as in 1983 although they continued to increase relative to trade flows.

Prospects and Issues

At the time of the discussions with the authors, the agencies' reservations on the Philippine situation con-

Chart 6. Philippines: Trends in Commitments, 1980–84

(End of period)



Sources: Data provided by official export credit agencies; and International Monetary Fund, *International Financial Statistics*, and staff estimates.

cerned the protracted negotiations of the Fund-supported adjustment program and, consequently, the lengthening interval between the announcement of the payment moratorium and the eventual Paris Club discussion. Medium-term arrears had been increasing since early 1984, and the overall payments situation continued to deteriorate. One agency indicated that its policy stance would not be relaxed once a Fund agreement was reached. Rather, its policy could be further tightened should the discussions with the Fund prove unduly prolonged and the liquidity situation in the Philippines worsen. Overall, most of the agencies seemed to have taken a dimmer view of the medium-term outlook for the Philippines. With the full scale of the country's heavy debt burden having become known in early 1984, and along with the Philippines' domestic political uncertainties, some agencies have begun to feel that the Philippines' need for repeated Paris Club reschedulings could not be precluded.

With the lengthening interval between the approach to and the eventual discussion with the Paris Club, a feature of the agencies' experience with the Philippines is the apparent increase in demand for short-term cover and its impact on the agencies' ability to remain on cover. As noted above, in spite of the growing uncertainties and the tight liquidity situation of the Philippines, several agencies retained cover for a time on short-term transactions without tight restrictions; they were willing to do this because there were no transfer delays on this account. A few agencies reported delays on short-term transactions that were concluded before the moratorium date. For some agencies, their flexibility was made possible on the initial expectation of a speedy agreement on a Fund-supported adjustment program. They indicated that their attitude could change as the situation had weakened with the prolonged Fund negotiations, and as they had experienced very sharp increases in their short-term exposure. Some agencies have already, as customary, interpreted this tendency as a sign of deteriorating risk, perhaps reflecting a spillover of demand unmet by other agencies that are relatively more stringent. One agency indicated that much of the increase in demand for cover had not been due to a shift in its market share as such but, rather, from commercial banks for transactions that traditionally had not required cover. With these difficulties and the possibility of short-term arrears, some agencies have moved to tighten short-term cover policies, for example, by withdrawing delegating authority for suppliers' credits and introducing limitations for banks.

Romania

Policy Turning Point

The agencies' attitudes concerning Romania began to change for the worse in early 1981, reflecting in part the general loss of confidence in the debt situation of the Eastern European region in the wake of the Polish debt crisis. Romania was then regarded as particularly vulnerable to shifts in banks' sentiments, given its heavy reliance on short-term bank borrowing. Subsequently, as a result of the precipitous drop in short-term financing—especially from banks—Romania's payments problems quickly worsened and arrears emerged in mid-1981, soon after the conclusion of a stand-by arrangement with the Fund for a three-year adjustment program. During the following two years, Romania concluded a series of multilateral rescheduling agreements with the commercial banks, nonguaranteed suppliers, and with the Paris Club.

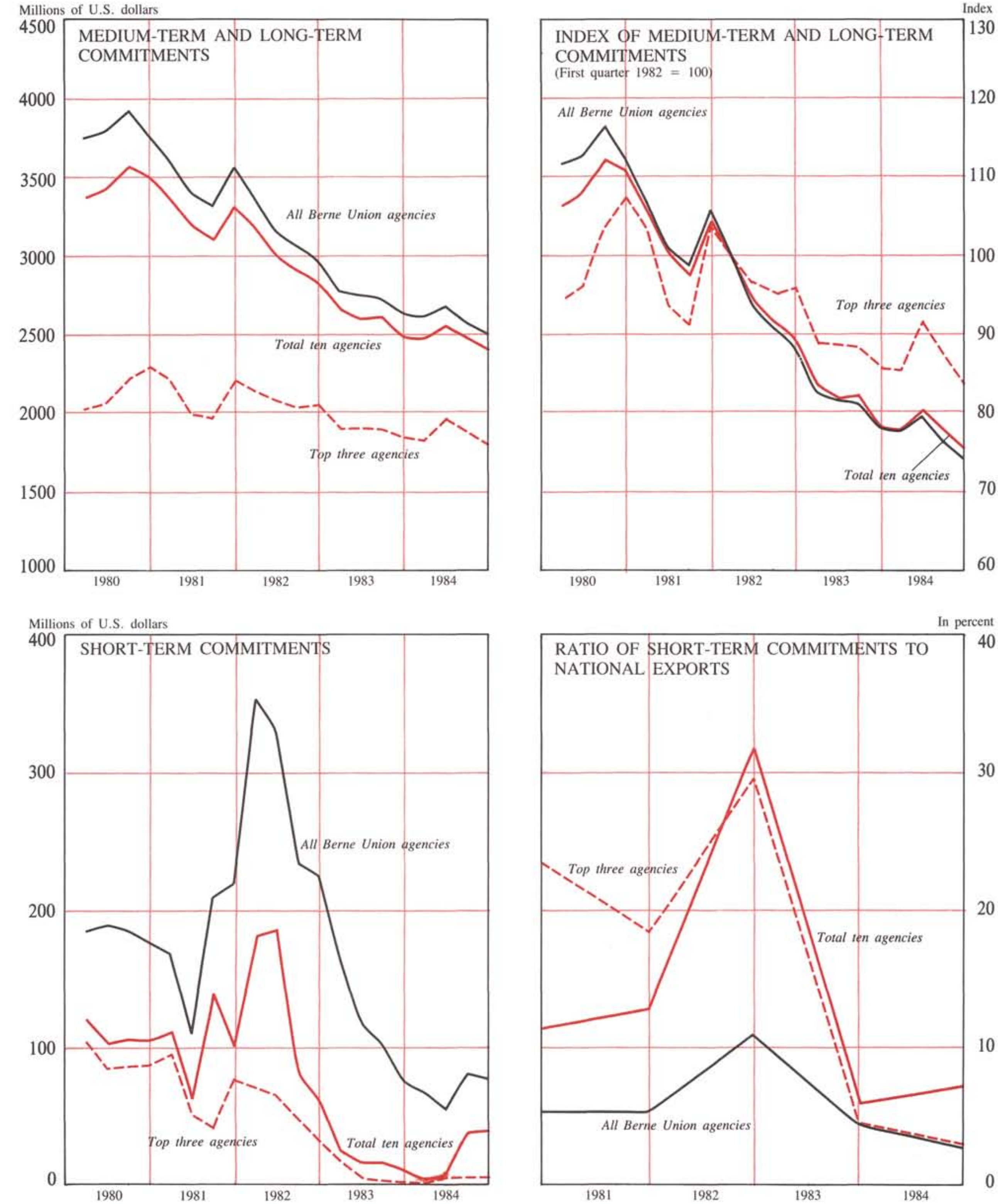
Beginning in mid-1981, in response to the worsening arrears situation, most agencies progressively tightened cover policies for Romania. In the following two years through mid-1983, most agencies maintained a very restrictive stance on both medium-term and short-term cover policies. In late 1981, as Romania attempted unsuccessfully to seek bilateral aid (including a debt rescheduling) from certain creditor governments, eight of the ten agencies moved to significantly tighten cover. On medium-term transactions, two agencies (which were by that time certain of Romania's need to reschedule comprehensively) withdrew cover in practical terms, while four others imposed restrictive conditions, mainly through a case-by-case approach. Similarly, and perhaps more important, for short-term transactions, two agencies were practically off cover, while several others introduced stringent conditions, including the guarantee requirement of the central bank and a reduced percentage cover.

Subsequently, in the first half of 1982, policies were tightened even further upon first report of the central bank's default against irrevocable letters of credit and that Romania would seek a Paris Club rescheduling. By the time the Paris Club multilateral agreement was reached in July 1982, all agencies were practically, if not formally, off cover on medium-term transactions. On short-term transactions, the agencies had suspended further drawings under lines of credit, and only two agencies reported remaining open.

Even with these severe policy restrictions, some of the agencies tightened policy even further and took extreme actions in 1983. In reaction to Romania's

Chart 7. Romania: Trends in Commitments, 1980–84

(End of period)



Sources: Data provided by official export credit agencies; and International Monetary Fund, *International Financial Statistics*, and staff estimates.

difficulty in implementing the 1982 Paris Club bilateral agreements and as the situation deteriorated amid growing uncertainty and rumors of likely bank defaults, one agency took the exceptional measure of stopping disbursements. Moreover, the one agency that had so far avoided withdrawing cover decided to suspend cover formally. Partly for noneconomic reasons, one agency took the exceptional measure of withdrawing cover even for existing revolving short-term facilities and for whole-turnover insurance. By March 1983, all agencies were effectively off cover on medium-term transactions and only one agency remained open on short-term transactions.

Trends in Exposure

The exposure trends for Romania have shown a remarkable degree of correlation with the agencies' policy stance—more so than for the other countries in the study. Given their uniformly restrictive policy stance, the agencies' exposure in aggregate has been declining significantly and steadily since the policy turning point in early 1982 (Chart 7). This declining trend is especially marked because it is clearly shared by all of the agencies. For the ten agencies combined, medium-term commitments dropped by 7 percent in 1981 and at an even sharper rate of 13 percent in 1983.

Short-term commitments remained relatively high during a part of the period for the few agencies that maintained cover. As the situation deteriorated in 1983 and as short-term cover policies were tightened for this group of agencies, short-term exposure of virtually all agencies has diminished to a minimal level, with only one agency maintaining reasonably normal short-term exposure.

Prospects and Issues

Since late 1983, about half of the agencies have eased their cover policies for Romania, mainly for short-term transactions. By June 1984, six agencies had reported restoration of short-term cover on a limited basis by requiring, for example, central bank guarantee, maximum credit terms of six months, and an extended claims-waiting period. On medium-term transactions, three agencies (one in the top three) have restored cover, one on a case-by-case basis and the others with annual commitment limits. There has been some easing of these conditions in recent months. For the first agency that restored cover on medium-term transactions, its decision was influenced by its low exposure in absolute and relative terms, and the action was regarded as a goodwill gesture, in part as an informal quid pro quo agreed in the negotiations of the 1983 Paris Club bilateral agreement.

Since 1982, Romania's external position has improved significantly, with growing surpluses on the current account of the balance of payments. However, for most of the agencies, the policy stance remained cautious, in spite of Romania's successful avoidance of another Paris Club rescheduling for the 1984 maturities and its improved record in implementing the 1983 Paris Club bilateral agreements. Even with the improved payments experience since 1983, some of the agencies continued to have some reservations about Romania and cited several factors for their hesitancy. First, the improved economic performance was perceived by some agencies to be based on a probably unsustainably large deflation of the economy. Second, although payments to the agencies themselves had become current, certain uninsured arrears remained, and for at least two agencies, this fact had adversely influenced their cover policy decisions. Third, for some smaller agencies, policies could continue to be guarded and cautious since there was no effective pressure from exporters to reopen cover. Finally, for some of the large agencies, their relative exposure in Romania had reached such a level that policy needed to be cautious in any case.

A notable feature of the agencies' experience with Romania is the agencies' indication that at times they might have overreacted and might have acted in a more cautious manner than needed. The two reasons most often cited for this tendency were, first, that communications by Romania were initially flawed with Romania giving the impression of being not ready to disclose essential economic and financial information for the agencies' assessment, and, second, agencies took a dim view of Romania's initial attempt to negotiate bilaterally with creditors, both official and nonofficial.

Turkey

Resumption of Normal Policies after 1978, 1979, and 1980 Reschedulings

Turkey's external position deteriorated sharply during the mid-1970s, and significant payments arrears emerged in 1976. In the late 1970s, with rapidly mounting arrears, the liquidity crisis culminated in a series of comprehensive debt reschedulings with official creditors, commercial banks, and nonguaranteed suppliers. For the official creditors, the reschedulings

took place in 1978, 1979, and 1980, all under the aegis of the OECD. These reschedulings provided for comprehensive and exceptional debt relief, including extraordinarily broad coverage of debt to be rescheduled (such as arrears and current maturities on short term); the 1980 agreement also included a rescheduling of maturities extending through June 1983.

In response to the official debt rescheduling of 1978, the agencies adopted a very restrictive policy stance, and virtually all regular programs were closed to Turkey. Over the next five years through early 1983, this tight policy stance was substantially unchanged. The reasons cited for this policy stance included, first, Turkey's evident need for repeated and increasingly comprehensive debt reschedulings, and, later on, the extension into June 1983 of the debt consolidation period agreed for the 1980 rescheduling. Second, for several agencies, the bilateral rescheduling agreements were for a long time not successfully implemented, and during a substantial part of this five-year period, arrears continued to exist. Overall, most agencies indicated that in a strict sense they were off cover for medium-term transactions; for short-term transactions, half of the agencies withdrew cover while the other half required extreme conditions, such as confirmed irrevocable letters of credit.

During this period, partly on national interest considerations and given the existence of a Fund-supported adjustment program, some agencies were able to provide cover on an exceptional basis in the context of the OECD Consortium arrangement. Under this framework, the agencies provided medium-term cover under tight commitment limits, with added conditions to ensure that only the most essential imports would be financed. Even then, on short-term transactions, business was often conducted under confirmed irrevocable letters of credit. For several agencies, cover was provided only for externally financed or aid-financed projects. Some agencies also reported the underusage of short-term revolving limits (against irrevocable letters of credit), owing in part to the change in the market structure in Turkey from credit-financed to cash-financed.

Policy Turning Point

Significant improvements in Turkey's external position as well as in its overall economic situation became noticeable beginning in 1981. However, it was not until the middle of 1983 that a few agencies began to relax cover policies and began to provide cover outside the context of the OECD arrangement.

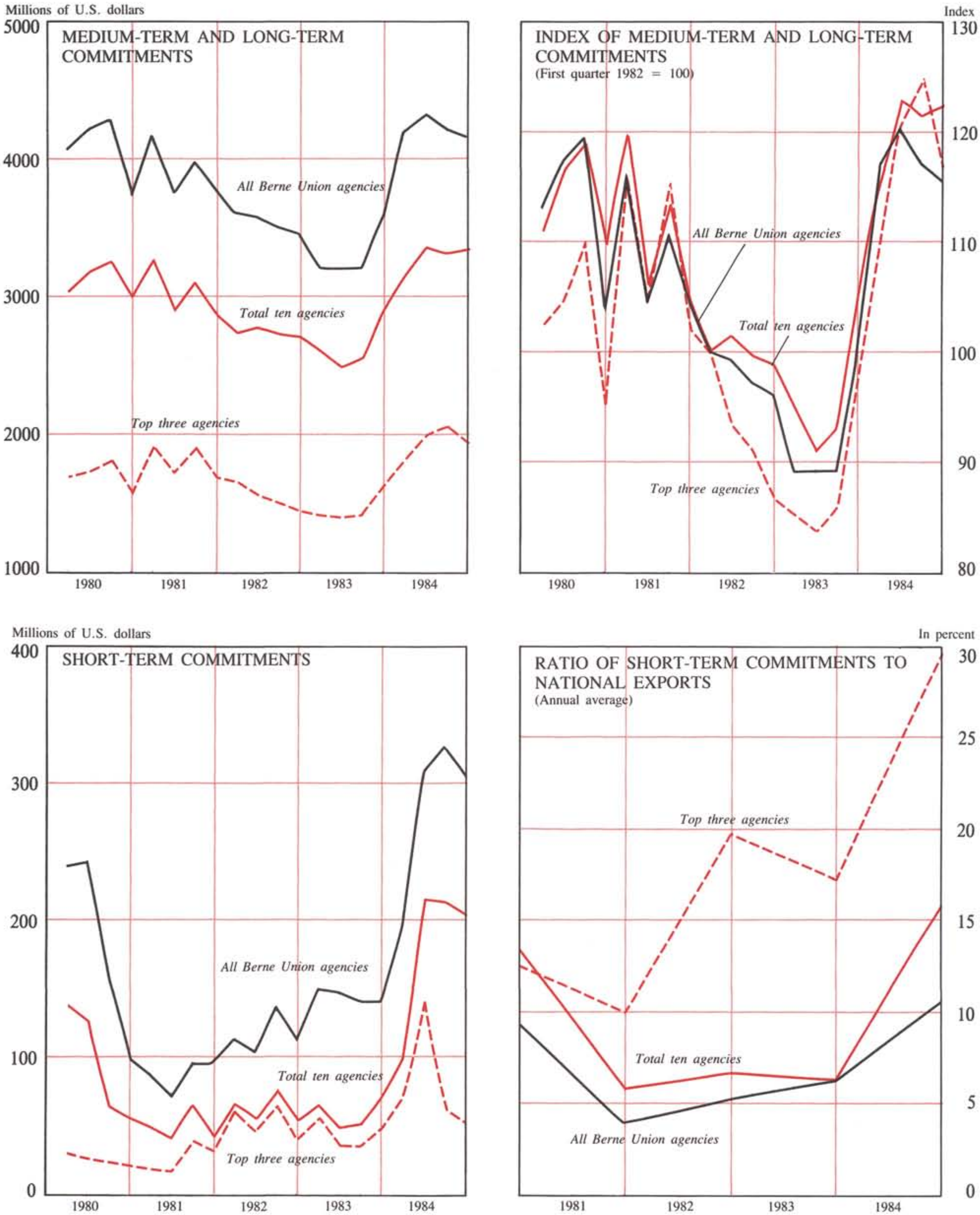
Beginning in early 1981, as a result of the improved financial situation, Turkey was able to service unrescheduled debt as well as to keep current on most payments under the rescheduling agreements to most agencies. Moreover, the Fund-supported adjustment program was proceeding satisfactorily, with drawings made on schedule. In spite of these positive developments, some agencies suggested that they remained reluctant to ease cover policies since medium-term claims payments were still being made, given that the consolidation period would only end in June 1983. Other agencies indicated that, owing to information lags, the financial improvement could be confirmed only with significant delays. Also, one agency indicated that the financial loss associated with the reschedulings of the 1970s was so heavy that there was a need to be especially cautious. Finally, a few agencies indicated that there remained some arrears relating to the rescheduling agreements.

It is significant that the agencies in the study delayed their return to normal cover policies behind the commercial banks. Already, the 1982 bank restructuring for Turkey took place in circumstances of much better relations. Turkey succeeded in obtaining terms and conditions more favorable than previously, and agreement was reached in early 1982 on the first medium-term syndicated bank credit since 1979.

In mid-1983, a few agencies began to ease cover policies, citing the following principal considerations. First, the economic progress since 1982, especially the sharp improvement in export performance, was continuing into 1983 and was now seen to be more significant. Second, the change in government was seen as a positive factor for the continuation of adequate economic management. Third, the debt consolidation period had ended and agencies were no longer paying claims, and, for some agencies, the arrears had been eliminated.

Given that the medium-term outlook nevertheless remained difficult, these few agencies were cautious in their first moves. Special efforts were taken to keep exposure under tight control and to ensure that the additional financing would be economically sound. For one major agency, cover on short-term transactions was restored only gradually, with limits on the transaction size, maximum maturities of 180 days, and confined to whole-turnover policyholders who were national exporters. With the condition of central bank guarantee, there was also a stringent assessment of commodities eligible for cover. Gradually, limits were raised, and the scope and the types of commodities or the group of exporters eligible for cover were widened to include, for example, investment goods under two years. Moreover, there was a variety of single limits for selected projects. Another agency took the unusual move (for this agency) of establishing an annual commitment limit coupled with an individual transaction

Chart 8. Turkey: Trends in Commitments, 1980–84
(End of period)



Sources: Data provided by official export credit agencies; and International Monetary Fund, *International Financial Statistics*, and staff estimates.

limit. These limits were established as guidelines for the Turkish authorities in their attempt, at the agencies' request, to prescreen the types of public sector projects suitable for support. One other agency was able to restore medium-term cover only with a tight market limit coupled with a special risk-sharing arrangement with commercial banks to limit its exposure. One exception to this overall cautious trend was one agency with relatively small exposure that was prepared to approve a large increase in commitments, but this was on the basis of commercial consideration of a possible large project.

More than half of the agencies initially remained cautious and did not ease policies in substantive terms, taking the view that Turkey's medium-term payment ability was still in doubt, given the bunching of scheduled debt-service payments beginning in 1985 when the previously rescheduled payments would fall due. Overall, another debt rescheduling was seen as a possibility. These agencies, however, had begun to reassess their initial positions, given the more liberal attitudes of other agencies and the apparent increasing optimism on the part of commercial banks, and had eased their cover policies further by June 1984.

Trends in Exposure

The exposure trends for Turkey are mixed. During the period 1981–83, there were periodic increases in medium-term commitments of certain agencies that were in a position to participate directly in the OECD Consortium arrangement. For other agencies, where efforts to assist Turkey were in the context of direct aid outside of the agencies proper, there were steady declines in their medium-term commitments for Turkey, in line with the tight cover policy stance. Overall, for the ten agencies in aggregate, medium-term commitments declined throughout this period by an average of 5 percent per annum (Chart 8). Conversely, for the recovery phase, it is noteworthy that, following the apparent easing of policy in 1983, there was a sharp upturn in agencies' exposure in 1984.

The trends for short-term commitments were particularly erratic across agencies in the early 1980s and do not lend themselves to a clear-cut interpretation. For all ten agencies in the aggregate, short-term commitments measured relative to trade flows dropped especially sharply in 1981, possibly reflecting the sharp tightening of short-term cover policy for the major agencies following the comprehensive 1980 debt rescheduling. However, from 1982 onward, when a few agencies began to resume cover on short term, aggregate commitments have recovered significantly. For the top three agencies in the market, their short-term commitments almost doubled in 1982 as a ratio to their national exports, and rose further to 20 percent in 1984.

Prospects and Issues

Significant increases in exposure have followed the shift in policy stance with considerable delay. One agency ascribed this delay, not to the lack of the underlying demand, but to the administrative delays involved in rationing the exceptionally large pent-up demand after years of restriction. As noted earlier, special efforts have been taken by two agencies in an attempt to direct medium-term lending to sound projects of appropriate size. The problems of ensuring a proper project selection were seen to be particularly serious by some agencies. The smaller agencies in the market are not in a position to transfer the task of project prescreening to the Turkish authorities as had been possible for one agency. Generally, agencies are not in a position to appraise projects from the perspective of economic viability for Turkey. Some agencies indicated that their ability to resume cover on medium-term transactions could be enhanced should there be an investment plan with an appropriate project composition that would serve to guide their cover policy decisions.

Venezuela

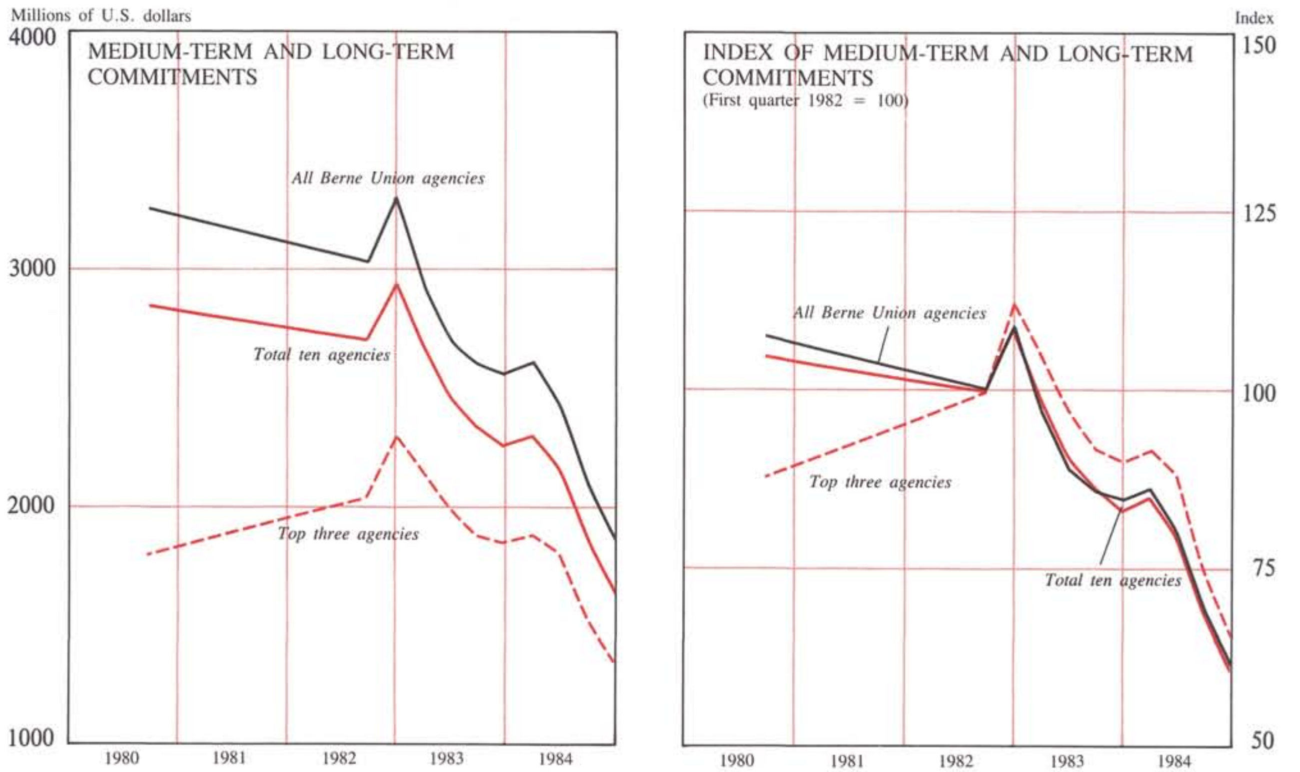
Trends in Exposure

Until early 1983, the agencies had maintained a wide-open approach for Venezuela.[6] Given its oil resources, Venezuela had been considered an excellent credit risk by banks and had enjoyed easy access to capital markets. Consequently, demand for cover had been low and the agencies' exposure had remained relatively small for the market size.

Throughout 1982, the oil market deteriorated and Venezuela's credit standing in capital markets weakened. This reflected in part the regional debt problem

[6] The Berne Union quarterly data for Venezuela are incomplete for much of the period 1980–82 and therefore the discussion in this section is less complete.

Chart 9. Venezuela: Trends in Commitments, 1980–84
(End of period)



Sources: Data provided by official export credit agencies; and International Monetary Fund, *International Financial Statistics*, and staff estimates.

following the Mexican liquidity crisis of August 1982, Venezuela's weak economic performance, and its heavy debt burden. During the second half of 1982, Venezuela experienced significant increases in the spread over the London interbank offered rate for its Euromarket borrowings. Furthermore, the program to restructure its bank debt, to correct the excessive concentration of short-term maturities, began to run into difficulties. By year-end, there were doubts about the viability of the exchange rate and capital flight accelerated. As the overall situation deteriorated, only two agencies reported having tightened policies slightly. One introduced a limit on total commitments, albeit a generous one, and another began to consider applications for over five-year credit terms on a case-by-case basis.

Despite their liberal policy stance, the agencies' exposure in this market declined broadly, owing to slack demand (Chart 9). Only two agencies (including the top agency) saw significant increases in their total medium-term commitments in 1982 compared with those in 1980; during this two-year period, the other eight agencies registered marginal increases or declines (as much as 35 percent at an annual rate). Short-term commitments also fell sharply in dollar terms and appeared to have declined as a ratio to national exports as well.

Policy Turning Point

By early 1983, arrears had emerged and there was considerable capital flight. With a deteriorating external position, Venezuela introduced tight restrictions on the exchange system in early 1983. These restrictions included a three-tier exchange rate system that provided, inter alia, for different exchange rates for the servicing of the public debt and of the different types of private debt. Debt owed or guaranteed by the public sector and certain vaguely defined private debt were to be serviced at a preferential exchange rate, while other types of debt were to be serviced at a free market (and much more depreciated) exchange rate. The administrative arrangements were complicated

and imprecise. In particular, significant payments delays arose from the practical complications and uncertainties surrounding the eligibility requirements for the preferential exchange rate. Arrears were accumulated initially on nonpreferential private debt and later on public debt.

In the first half of 1983, most agencies began to tighten cover policies significantly, mainly in reaction to substantial arrears accumulation and transfer difficulties for the private sector and growing uncertainties concerning the exchange arrangement. One agency adopted a restrictive attitude, not because of its own claims experience as such, but because the claims experience of others had been worse. Initially, some agencies attempted to tighten policies only for the private sector (where transfer difficulties had first been experienced) and continued to provide cover for the public sector on a more cautious basis. In the first quarter of 1983, two agencies withdrew cover on all transactions and six agencies followed in the next quarter by imposing severe restrictions, especially on the private buyers.

By the third quarter of 1983, for medium-term transactions, four agencies had withdrawn cover, while one agency had suspended cover for the private buyers; the other five agencies had adopted a case-by-case approach. For short-term transactions, three agencies had gone off cover and one had withdrawn cover for the private buyers; the others had imposed restrictive conditions. The severe restrictions on short-term transactions were imposed mainly as a result of Venezuela's attempt to unilaterally reschedule short-term private sector debt into three-year maturities.

By late 1983, significant arrears had also emerged for the public sector debt and the agencies had ceased to make distinctions in cover policies in favor of the public sector. Through mid-1984, most agencies progressively tightened policies and, by that time, virtually all agencies had suspended medium-term cover in practical terms, while some had withdrawn short-term cover as well. A few agencies remained open for transactions with the public sector, but did not expect to do much business, as the public sector demand for imports had been marginal.

Trends in commitments through 1984 have already reflected this overall restrictive stance. In the fourth quarter of 1983, medium-term commitments of the ten agencies in aggregate fell by 23 percent, compared with a year earlier. The declines are broadly based and range from some 10 percent for the smaller agencies in the market to a high of 42 percent for one of the top three agencies. Short-term commitments for the latter half of 1983 also fell more sharply than national exports. These trends became more pronounced in 1984.

Prospects and Issues

Most agencies continued to regard Venezuela's medium-term prospects as favorable and considered its current difficulties as temporary, reflecting the weak maturity structure of debt, and amenable to solution. However, the agencies' actions have been severely restrictive over the short term in response to the approach taken by Venezuela in resolving this temporary liquidity problem. They indicated that a resumption of normal policies would be conditional on the satisfactory resolution of the arrears problem, which included a rescheduling arrangement with the official creditors and the active cooperation of Venezuela with the banks and, in the view of some agencies, cooperation with the Fund as well.

The agencies' major difficulties with Venezuela centered around the arrears that had been accumulating and the differential and, for the agencies, unsatisfactory treatment given to debt owed by the Venezuelan private sector. Since the introduction of the multiple exchange rate system in early 1983, it has been intended that the servicing of the public sector debt (contracted before February 18, 1983) would be kept current and would be with guaranteed access to the preferential exchange rate. In the event, owing in part to foreign exchange shortages, arrears have accumulated even on the public sector debt.

Concerning Venezuela's private sector debt, a less favorable arrangement has been made for its servicing. It seems that the servicing of such debt at a preferential exchange rate has been provided for only on the rescheduled terms and conditions that have been set unilaterally by the Venezuelan authorities. This unilateral rescheduling arrangement (known as the "Recadi") has not been accepted by the agencies and, since early 1984, concerted efforts have been made to resolve this issue via a multilateral approach. Paris Club creditors were disappointed that repeated requests from them to the Venezuelan authorities for clarification of the official policies, vis-à-vis debt servicing of official credits, had gone unanswered. Some agencies have informally indicated that should a Paris Club discussion prove impractical (in the absence of a Fund-supported adjustment program in the upper credit tranches), a multilateral rescheduling along the Paris Club format might suffice, provided that a credible adjustment program has been adopted. In June 1984, the dispute remained unresolved, bank refinancing discussions were progressing slowly, and arrears were accumulating.

Yugoslavia

Policy Turning Point

Yugoslavia entered into a three-year stand-by arrangement with the Fund in January 1981 and was able to purchase the full amount available under the arrangement. Despite the improved current account performance, the overall external position of Yugoslavia began to weaken in the second half of 1981, when significant net capital outflows occurred. By that time, commercial banks had begun to sharply cut back new lending, which reflected growing concerns with the overall debt situation in Eastern Europe following the Polish debt crisis and with the rapid buildup of the Yugoslav short-term debt. At that point, three agencies moved to tighten terms of cover; one agency (among the top three in the market) went as far as suspending cover in practical terms.

Most agencies began to significantly tighten the terms of cover during the second half of 1982. Yugoslavia's problem of liquidity and confidence was aggravated in March-April 1982, when one of the Yugoslav regional commercial banks encountered serious debt-servicing difficulties and there were serious transfer delays. The country's access to capital markets became jeopardized, along with substantial outflows of capital owing to the confidence crisis. By the fourth quarter of 1982, in response to arrears accumulation, three agencies had withdrawn cover for medium-term transactions, while four others had imposed restrictive conditions. As for short-term transactions, one agency withdrew cover, while only two agencies retained cover without any restriction.

In early 1983 and in the context of the Fund-supported adjustment program, an approach was made to banks and official creditors for special assistance to meet the 1983 financing need. In the event, governments agreed by referendum (referred to as the Berne Agreement) to provide assistance for export credits, including some rollover of maturities. In January 1984, agreement was reached with official creditors to formally refinance 100 percent of principal payments due in 1984. Since 1983, for most agencies, cover policies for Yugoslavia have been in the context of the Berne Agreement, and disbursements are expected to continue. Governments have also confirmed their willingness to provide credits or guarantees outside the official package.

Experience with Berne Agreement

Under the 1983 Berne Agreement, the agencies were committed to provide export credit assistance to Yugoslavia in broad terms, and in a variety of forms that, however, were not clearly specified in advance. Meanwhile, all regular facilities and programs had been suspended. Most agencies suggested that the normal programs would not be reactivated while the special arrangement was in effect.

Concerning cover policies in the context of the Berne Agreement, the agencies have taken different approaches and have had mixed experiences. Two agencies indicated that their commitments for medium-term cover under the Berne package were sufficient and equivalent to a de facto refinancing loan during the year. Several agencies reported the provision of credit lines for short-term cover for raw materials and essential imports, which were to be utilized under the Yugoslav priority system; one of these agencies had, at the same time, suspended medium-term cover. One agency reported that its experience with the credit line arrangement had been discouraging. First, there was a delay of about ten months before the credit line became effective, as practical difficulties were encountered in agreeing on the provisions and the types of goods to be covered. Moreover, once effective, the credit line was not much used owing to the strict import control in Yugoslavia. In contrast to this experience, one agency indicated that a more positive response—in that its short-term facility with irrevocable letters of credit conditions had been well utilized up to the specified revolving limits.

The experience regarding medium-term and long-term credit facilities under the Berne Agreement was also uneven. Only one agency reported the full use of its target committed under the Berne Agreement, since it succeeded in matching the Yugoslav need for certain imports (e.g., for the production of exportables) and in obtaining payment guarantee of the specified Yugoslav bank. Several agencies explained that their facilities for medium-term insurance cover had not been well used, in part because of stringent control within Yugoslavia regarding projects to be externally financed, that is, the Yugoslav wish to confine the use of export credits to noncapital goods for export-oriented industries. Moreover, a few agencies expressed reservations concerning some of the specifics of the facility, particularly in the effort to provide balance of payments financing through covering trade under abnormal credit terms (e.g., providing three-year to five-year credit terms for consumer goods which would normally be covered under short term). For these agencies, the abnormal terms provision may have been a factor in the low utilization of the facility.

Trends in Exposure

A feature of the agencies' experience with Yugoslavia is the absence of the debt buildup phase (except for short-term exposure) that has been noticeable for several countries in the study. In the period ahead of the policy turning point, medium-term commitments for nine of the ten agencies registered significant declines. In 1981, medium-term commitments of the top three agencies, as well as of the ten agencies combined, fell by 16 percent (Chart 10). These declining trends were to continue into 1982—the difficult period—and into the rescue year of 1983, although at an increasingly moderate pace. These tendencies are consistent with the absence of Yugoslav demand for capital goods imports, given the system of tight import and investment restrictions during this period.

The trends in short-term commitments seem indicative of the agencies' willingness to support trade finance for Yugoslavia. Total short-term commitments measured relative to trade flows have increased since 1981, and reached 18 percent of national exports by 1983 for the ten agencies in aggregate. This rising trend is all the more notable because it has been achieved through a sharp shift in the market shares among the top three agencies in the market.

Prospects and Issues

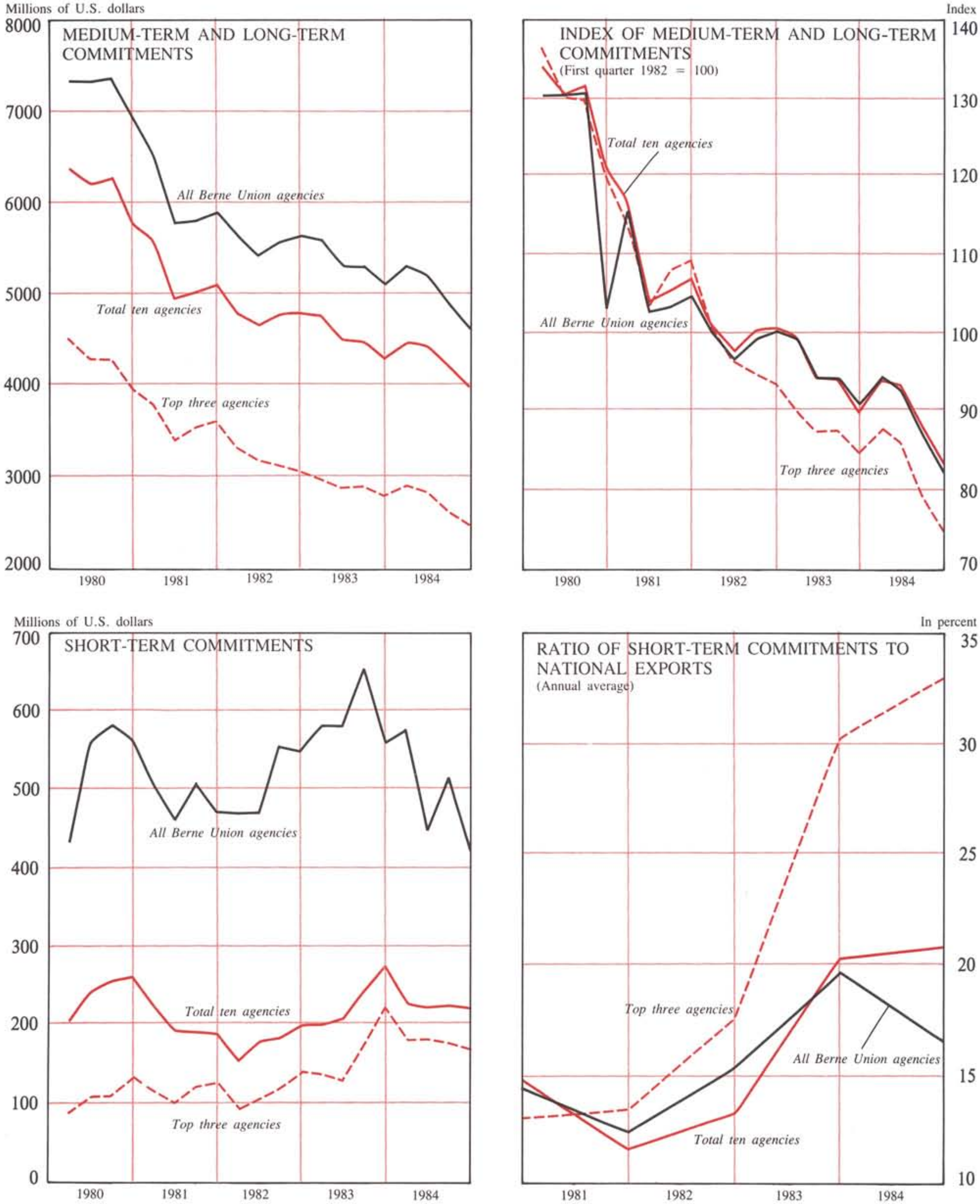
For 1984, there was no formal concerted financing package (of the type arranged in 1983) for Yugoslavia. Disbursements remained to be made for most agencies on the 1983 Berne Agreement, and there was a formal rescheduling agreement for 1984 maturities (see below). For 1984, only one agency indicated that its contribution would be along the lines of its successful facility that was provided in 1983. For several other agencies, the views were mixed and some were adopting a wait-and-see attitude. One agency indicated that the 1983 arrangement in fact had not yet been activated after long delays, since arrears remained outstanding.

Some agencies suggested that regular facilities could not be introduced until after the special arrangements had been completely utilized. In this connection, a few also observed that had the special arrangement not been made they may have been off cover for a few months, but market interest would be such that a resumption of cover on a limited scale would have become necessary in any case. One agency considered that the existence of a special facility, providing cover at abnormal credit terms, may have hindered its ability to provide cover under regular programs. Also, several viewed the difficulties in Yugoslavia as temporary—mainly in the weak capital account, owing to an inappropriate interest rate policy. Once policies are adopted to correct the difficulties, and in the absence of a special arrangement, they would be prepared to resume the normal approach.

A feature of the 1984 financing arrangement for Yugoslavia was the rescheduling of medium-term debt owed to official creditors, which was not formally undertaken in the 1983 arrangement. Following this rescheduling, a few agencies have resumed medium-term cover with some restrictions and on a case-by-case basis. Short-term cover has been retained by most on a limited basis, for example, with conditions of irrevocable letters of credit issued by the agency's resident banks. Some agencies also indicated that they viewed favorably the Yugoslav effort to confine the 1984 rescheduling to the principal amount. This narrow coverage of rescheduling was regarded as a confidence factor, indicative of the mild degree of financial difficulties faced by Yugoslavia. One agency felt its cover policy decision could be positively influenced, since there was an implicit link between the terms and conditions of new cover and the agency's financial burden of debt rescheduling. However, another agency, perhaps less affected by the financial cost of debt rescheduling, suggested that, while Yugoslavia's ability and willingness to be current on interest payments may have been a positive influence, the decisive factor remained the political will of governments to assist Yugoslavia.

Chart 10. Yugoslavia: Trends in Commitments, 1980–84

(End of period)



Sources: Data provided by official export credit agencies; and International Monetary Fund, *International Financial Statistics*, and staff estimates.

Appendix II

Technical Note and Glossary of Terms

This note describes the technical and operational aspects of export credits and export credit cover policies. It also provides additional explanation for, and definition of, some terms relating to export credits that are used in this study, particularly as background to the country descriptions in Appendix I.

Berne Union

Founded in 1934, the Union is an association of 36 export credit agencies, all participating as insurers and not as representatives of their governments. The main purposes of the Union are to work for sound principles of export credit insurance and maintenance of discipline in the terms of credit in international trade. To this end, members exchange information and furnish the Union with relevant information, consult together on a continuing basis, and cooperate closely.

Claims Payments

Payments made by export credit agencies to the suppliers or banks (the insurees) to compensate for transfer delays and for losses under the terms of the guarantee or insurance contracts.

Country Exposure/Commitments

These terms are used interchangeably in this paper. The descriptions of trends in exposure/commitments and the charts in Appendix I have been based mainly on the data on commitments reported to the Berne Union Secretariat. As noted in Chapter II, caution must be exercised in the interpretation of trends and aggregated figures. The definition of terms for these data, according to the standard basis of reporting established by the Berne Union agencies, may be described as follows.

Commitments

Commitments are defined to include principal and contractual interest payable by the importing country on disbursed and undisbursed credits. They are defined as total payment obligations of the importing country and not just the maximum liabilities of the agency. Thus, commitment figures will include, among other things, the percentage of loss that could be borne by the exporter bank, nontransferable amounts, and adjustments for possible price increases where premiums have been paid. The data are reported in U.S. dollars, corrected for exchange rate variations for contracts expressed in local currencies.

For most agencies, commitments refer to insured suppliers' credits and guaranteed buyers' credits or financial credits provided by banks or other financial institutions. Commitment data for the Eximbank and the Export Development Corporation include export credits extended directly by these agencies. Most other agencies in this sample also guarantee or insure a large part, if not all, of export credits extended by official financial institutions, and such guaranteed or insured export credits are included in the commitment figures for these agencies as well.

The maturity classification is by type of insurance or guarantee policy, that is, short-term transaction relates to comprehensive or whole-turnover policies, while all other transactions are related to other policies, such as specific financial or suppliers' credit guarantee policies.

Short-term commitments usually are commitments for sales of consumer goods and raw materials, which are normally covered under comprehensive or whole-turnover policies for which credit terms longer than six months are not normal. For some agencies, owing to their specific guarantee or accounting system, short-term commitments may be up to two years.

Short-term commitment data entail elements of estimation. Since most of the transactions are covered under comprehensive or whole-turnover policies, com-

mitment figures are estimates based on exporters' declarations. Agencies adopt different methods of estimation, depending on the guarantee system, the quality and availability of exporters' information, and the pattern of trade.

Medium-term and long-term commitments in this paper are all commitments other than short-term, including unallocated commitments. The data may include, for example, commitments whose specific terms are not yet known and amounts overdue (including claims under examination and not yet paid). They also include special project-type business that is payable in cash or on short credit terms, which are normally covered under specific financial or suppliers' credit guarantee.

Cover and Cover Policy

The provision, and the related policy, of export credit guarantee or insurance against risks of payment delay or nonpayment for export transactions. Cover is usually, though not always, provided both for commercial risk and for political risk.

Policy measures can be classified broadly by measures affecting the supply (availability) of insurance or guarantee and measures affecting the pricing of cover.

Supply Measures

In generally increasing order of restrictiveness, supply measures can be summarized as follows.

Ceilings on commitments. Ceilings are commonly applied to medium-cover and long-term maturities and can be in various forms. Most agencies in the study maintain individual country limits for total commitments/exposure. Across agencies, the formality and the degree of restrictiveness of these ceilings differ, and for some agencies, the ceilings may be renewable and subject to easy upward modification. For other agencies, some limits may merely represent informal administrative guidelines, while others serve as strict ceilings for approving applications, depending on the intended policy stance at the time. One agency suggested that ceilings imposed by an agency are a less effective control than those set by an interministerial committee because the former is subject to more frequent review and modification. Ceilings on short-term commitments have been used rarely, chiefly because of the difficulty of maintaining up-to-date figures of the extent to which agreed cover is actually being used. When short-term ceilings are imposed, they are usually revolving limits.

Ceilings may also be limits imposed on new commitments during a specified period, usually for a year or less. They may also be limits imposed on individual transaction size—a practice favored by some major agencies. Such ceilings have been considered by a few major agencies as highly effective in controlling exposure, not only for the magnitude but also the type of project eligible for cover. Others tend to avoid these ceilings on the grounds that for the debtor countries smaller transactions may not necessarily be more economic than large transactions.

Security requirement. Agencies could call for additional security as a restrictive condition for cover, with the type of security requirement varying primarily with the legal and administrative setting within the borrowing country. Frequently, the security is initially in the form of an irrevocable letter of credit, if the issuance of such a document is believed to be effectively controlled by the debtor country; such control could be exercised through the system of foreign exchange allocation, or some central system of approval by the monetary authorities or authorized banks. If an internal check within the borrowing country is absent, the agency could require additional security in the form of a confirmed irrevocable letter of credit, confirmed by a third-country bank or a bank of the agency's choosing who takes over the cross-border risk; in these circumstances, the agency is effectively, if not formally, off cover.

Several variants of security requirement have proliferated in recent years. For instance, with the experience of the better debt-servicing record of debt owed or guaranteed by the public sector, the agencies have increasingly required a payment guarantee by the public sector as the condition of cover. However, this type of guarantee would be an effective protection only if sufficient foreign exchange were available and only if transfer delays had been caused by problems in the administrative system of rationing foreign exchange. When there are serious foreign exchange shortages, such a guarantee is at best symbolic and cannot realistically be enforced.

In extreme cases, external or third-country guarantors could be required for unique transactions, and there could be other collateral requirements, such as mortgages on real properties, or the provision of cover tied to the retention of foreign exchange earned by the projects (e.g., through escrow accounts). In these instances, however, the agencies are still faced with the possibility of worsened commercial risks of the project, for example, by fluctuations in export earnings owing to volatile prices. In some instances, such collateral and escrow accounts have not proved effective.

Selective cover. The next restrictive move, after more stringent commitment limits and security requirements, is to adhere to firmer criteria for project

selection, with priority given (or cover confined) to selected buyers, economic sectors, or projects with a direct foreign exchange linkage and with more compelling economic justification.

Off cover (cover suspension). Cover can be suspended, generally though not necessarily, first on long-term transactions, next on medium-term, and last on short-term. Cover can be provided from the date of contract or date of shipment, and a decision to suspend cover usually applies to both. An exporter who has been provided cover from date of the shipment only would be without cover for future shipments. For an exporter with cover from the date of contract, the agency must decide whether or not goods should be delivered or projects should be completed. If the agency decides that the goods should not be shipped or the project should not be completed, the agency must settle the claim immediately.

Pricing Measures

These measures consist of two direct elements, the basic premium and the surcharge, and a variety of indirect elements, for example, varying the claims-waiting period and the percentage of cover.

Premium structure. Agencies maintain differing structures of basic premiums and charges that are not readily comparable. In broad terms, the premium rates generally vary with maturities, mainly between short-term and medium-term transactions. For some agencies, the premium rates also vary with the country risk. For others, the rate structure also distinguishes between public and private buyers—with the rate being lower for public buyers, the premise being that the public buyers are less risky and payments collection is better managed, and that assessing the creditworthiness of the private buyers is more costly and payments collection more cumbersome. Aside from the basic premium, premium surcharges can be imposed on an ad hoc basis to help limit exposure and to partially compensate for the increased cost of providing cover in exceptionally risky situations.

Claims-waiting period. The period for which exporters/banks must wait after transfer delays occur before claims payments are made. The normal claims-waiting period varies slightly across agencies, but tends to be about three months. As a restrictive move, the claims-waiting period can be extended to signal to exporters the agency's attitude toward a particular market. An extended claims-waiting period may not necessarily signify that a restrictive policy is in place. For markets where transfer delays can normally be expected because of administrative bottlenecks, an extended waiting period beyond the customary three months may be a neutral move—for example, Nigeria in 1980–81. When the agency extends the period (beyond that which is customary for the market) as a restrictive move, the deferral of claims payments provides the agency with a financial respite.

Reducing percentage cover. Percentage cover is the proportion of any loss suffered by the exporter on which the agency will pay claims. A reduction in percentage cover results in a higher cost for the exporter because of the higher proportion of risk being borne by the exporter. To gradually increase the degree of policy restrictiveness, the agency can reduce the percentage cover in steps, from a normal 90 to 95 percent down to as low as 70 percent, beyond which the required degree of self-insurance becomes prohibitive. When the percentage cover is reduced, the exporters are not normally permitted to seek reinsurance through private insurers of the portion uncovered. Even when reinsurance is permitted, there is substantial additional cost. Two major agencies reported they have not relied on varying the percentage of cover, mainly because the cost burden to exporters could not be justified.

Export Credits

In this paper, two broad and frequently overlapping types of officially supported export credits have been described.

(1) Export credits with guarantees or insurance provided by official export credit agencies of the exporting countries. The financing (as opposed to the guarantee/insurance element) may come from a variety of sources, for example, through the commercial banks as financial trade-related credits and provided either to the suppliers (suppliers' credits) or to the importers (buyers' credits); or directly through the suppliers (also suppliers' credits); or through the direct support of the export credit agency itself or of another public financial institution specializing in export promotion.

(2) Export credits extended directly by official institutions of the exporting countries, usually through long-term finance as a supplement to resources of the private sector, and generally for promoting export of capital equipment and large-scale, long-term projects.

The role of the official export credit agency and the scope of its export credit facility, in terms of providing insurance/guarantee and direct export finance, differs across countries. In many countries (e.g., eight of the ten agencies participating in this study, excepting the Eximbank of the United States and the Export Development Corporation of Canada), the export credit agencies provide only guarantee or insurance and do not extend direct export credits. These agencies, however, also guarantee or insure a large part of export credits extended by other official institutions.

OECD Export Credit and Credit Guarantees Group

A forum in which 22 OECD member countries participate in the arrangement on Guidelines for Officially Supported Export Credits, that is, the "Consensus Arrangement," which became effective on April 1, 1978. Under the current guidelines, the matrix of minimum interest rates applicable to medium-term and long-term credits (the consensus matrix) is adjusted bianually in accordance with the formula adopted by participating countries in October 1983, which reflects the weighted average of long-term government bond yields of SDR currencies. Aside from coordinating export credit terms, the OECD Export Credit Group has also served as a forum for exchange of country information and agency practices; the regular meeting of the Group is attended by representatives of export credit agencies and their guardian authorities.

Offers

Amounts for which agencies are committed to provide cover if the exporter succeeds in obtaining the contract. The amounts cannot be exact and normally do not include interest. The figures provided to the Berne Union Secretariat by agencies will often overlap, as more than one agency will compete for the same project. If an agency has made more than one offer of cover in relation to a particular project, not more than the total obligation of the importing country on that business should be reported. Most agencies do not make offers for normal short-term business; the agencies who do are not required to report such data, and offers data should refer only to medium-term and long-term business.

Transfer Delays

Delays experienced by creditors in securing payments from debtors on the due date. In this paper, transfer delays refer only to those delays caused by the failure of the authorities of a debtor country to effect a transfer of foreign exchange on behalf of the debtors to settle on the due date an external payments obligation, after the debtor has made the required local currency deposit.

Table 1. Guaranteed/Insured and Direct Trade-Related Credits Relative to Nonguaranteed Bank Credits, 1982–83

	End-December 1982				End-December 1983			
			Total trade-related credits (1) + (2)				Total trade-related credits (1) + (2)	
	Guaranteed bank credits (1)	Nonbank trade-related credits (direct/insured) (2)	In millions of U.S. dollars	In percent of non-guaranteed bank credits	Guaranteed Bank Credits (1)	Nonbank trade-related credits (direct/insured) (2)	In millions of U.S. dollars	In percent of non-guaranteed bank credits
Argentina	1,924	1,994	3,918	18.2	1,210	2,091	3,301	14.4
Brazil	4,455	6,538	10,993	20.3	4,845	6,538	11,383	20.9
Madagascar	144	83	227	98.7	113	147	260	115.0
Mexico	2,053	3,993	6,046	10.5	2,755	3,843	6,598	10.8
Nigeria	1,810	3,114	4,924	87.0	2,641	3,301	5,942	93.9
Peru	730	1,052	1,782	38.2	649	675	1,324	29.8
Philippines	1,117	1,781	2,898	39.2	1,187	1,627	2,814	39.8
Romania	663	554	1,217	31.8	314	529	843	24.7
Turkey	482	2,405	2,887	90.7	503	2,653	3,156	91.1
Venezuela	414	1,679	2,093	9.1	339	1,398	1,737	7.9
Yugoslavia	1,651	1,897	3,548	42.2	1,656	1,905	3,561	44.6
Total eleven countries	15,443	25,090	40,553	21.3	16,212	24,707	40,919	22.0
Total developing countries	56,047	121,601	177,648	38.6	55,437	134,727	190,164	40.6
Sample countries as percentage of all developing countries	(27.6)	(20.6)	(22.8)	(. . .)	(29.2)	(18.3)	(21.5)	(. . .)

Sources: Bank for International Settlements (BIS) and Organization for Economic Cooperation and Development (OCED), *Statistics on External Indebtedness: Bank and Trade-Related Non-bank External Claims on Individual Borrowing Countries and Territories at end-December 1982* and *end-December 1983* (Basle: BIS; Paris: OECD, April 1984 and November 1984); and International Monetary Fund, staff estimates.

Table 2. Eleven Debtor Countries: Selected Chronology on Payments Difficulties, 1980–June 1984

	Argentina	Brazil	Madagascar	Mexico	Nigeria	Peru
Relations with export credit agencies						
Emergence of transfer delays[1]	1981 Q3[1]	1983 Q2	1981 Q3[1]	1982 Q2[1]	1981 Q3[1]	1982 Q3
Paris Club multilateral agreement date(s)	. . .	November 1983	April 1981 July 1982 March 1984	June 1983[2]	. . .	November 1978 July 1983 June 1984
Coverage of debt consolidated[3]	. . .	P, I, A	P, I, R, A	P, At	. . .	P, I
Consolidation period[3]	. . .	17 months	18 months	6 months	. . .	15 months
Relations with commercial banks						
Restructuring agreement date	. . .	February 1983 January 1984	July-November 1981 September 1983	August 1983	July 1983 September 1983	June 1978 December 1978 January 1980 July 1983
Relations with Fund						
Board approval of program	January 1983[4]	March 1983	June 1980[4] April 1981[4] July 1982[4] April 1984	January 1983	. . .	June 1982[4] April 1984
Type of program[3]	SBA	EFF	SBA	EFF	. . .	SBA

	Philippines	Romania	Turkey	Venezuela	Yugoslavia
Relations with export credit agencies					
Emergence of transfer delays[1]	1983 Q4	1982 Q2	1981 Q3[1]	1982 Q3	1983 Q1
Paris Club multilateral agreement date(s)	. . .	July 1982 May 1983	May 1978[2] July 1979[2] July 1980[2]	. . .	January 1982[2]
Coverage of debt consolidated[3]	. . .	P	Pt, It, At, R	. . .	P
Consolidation period[3]	. . .	12 months	36 months	. . .	12 months
Relations with commercial banks					
Restructuring agreement date	. . .	. . .	June 1979 August 1979 August 1981 March 1982	. . .	October 1983 May 1984
Relations with Fund					
Board approval of program	February 1980[4] February 1983[4]	June 1981[4]	June 1980[4] June 1983[4] April 1984	. . .	June 1980[4] January 1981[4] April 1984
Type of program[3]	SBA	SBA	SBA	. . .	SBA

Sources: Data provided by official export credit agencies; and International Monetary Fund.

Key:

P	Principal, medium-term and long-term
Pt	Principal, debt of all maturities
I	Interest, medium-term and long-term debt
It	Interest, debt of all maturities
A	Arrears on principal and interest, medium-term and long-term debt
As	Arrears on principal and interest, short-term debt
At	Arrears on principal and interest, debt of all maturities
Ap	Arrears on principal, medium-term and long-term debt
R	Previously rescheduled debt
SBA	Stand-by arrangement
EFF	Extended Fund facility

[1] Country may have incurred arrears before the third quarter (Q3) of 1981.
[2] Non-Paris Club, mainly OECD Consortium arrangement.
[3] Refers to the most recent arrangement.
[4] Canceled or expired as of June 30, 1984.

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