



Business at OECD

Modernizing the OECD Consensus – For a more flexible and market-reflective approach

Position and proposals by Business at OECD (BIAC) on the OECD Agreement modernization talks on payment and credit terms



Key Messages

- The ongoing debate and negotiations within the OECD on the **modernization of its “Arrangement on Officially Supported Export Credits” (OECD Consensus)** are **necessary and urgent**. A common understanding and acceptance is needed among the Participants group and the users of the Arrangement (i.e. exporters, commercial banks as well as global clients) to reduce its complexity and to promote the application of simpler rules.
- *Business at OECD* (BIAC) aims to contribute to this debate and make the OECD Consensus again fit for purpose for exporters in a changed global economic landscape with new products and business models – thereby **re-establishing a global level playing field** which ensures that competition amongst exporters is based on the quality and price of goods and services, rather than on the favorability of public financial support.
- Besides the increased competition outside OECD rules with flexible and fit-for-purpose financing conditions as well as an increased relevance of global value chains, there is product and business model related evidence from the day-to-day business of exporters that makes a **strong case for the adaptation of the OECD Consensus towards a more flexible set of rules**.
- Firstly, the (repayment) limitations of the Consensus do not **reflect longer life cycles of products and goods missing realistic scenarios** concerning their revenues. Secondly, the repayment terms permitted by the Consensus are outdated compared to what common market practice today. Thirdly, pay-per-use business models and new types of products, e.g. cloud-based and software solutions or service-based product offerings are not covered by the current Consensus.
- The **efforts to address climate change should also be reflected in the new OECD Consensus**. While the Common Approaches are outdated and the current Consensus lacks a clear bottom line for applicable standards, BIAC advocates for the revision of universal standards that could derive from the OECD Common Approaches and related standards (IFC Performance Standards, World Bank EHS Guidelines) that could serve as potential guiding principles.
- **BIAC proposes concrete updates regarding the Consensus’ financing terms and conditions** as concerns (1) minimum down payment, (2) starting point of credit, (3) maximum credit terms, (4) market-reflective repayment profiles, (5) scope of Consensus and (6) minimum premium for credit risks.

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Introduction

With this position paper *Business at OECD* (BIAC) aims to contribute to the ongoing debate and negotiations within the OECD on the modernization of its “Arrangement on Officially Supported Export Credits”, more specifically on its payment and credit terms. The proposals are based on previous positions by BIAC with the goal of making the Arrangement again fit for purpose considering the need for new products and business models and the changes in the post-Covid global economic landscape that is still filled with many uncertainties. Resulting in continuing liquidity constraints and supply chain crisis leading to an upcoming global economic down-turn (recession). The overall interest since 1974 has been to create a global level playing field that ensures that competition amongst exporters is based on the quality and price of goods and services rather than on the favorability of public financial support.

Why does the current framework need to be updated?

Besides the widely acknowledged increased competition outside of OECD rules with more flexible financing conditions and the increasing importance of global value chains which are continuously under pressure, there is product and business model related evidence from day-to-day business of exporters that forms a strong case for the adaptation of the agreement towards greater flexibility.

Firstly, re (repayment) limitations of the Consensus do not reflect longer life cycles of products and goods, and are thus less linked to their reality scenarios regarding their revenues and therefore miss the needs of the market. Consequently, instalments are either too high in relation to the generated cash flows or due dates are too tight, especially of the 1st instalment. Positive experience with the various Sector Understandings underline the advantage of more market- reflective repayments, especially as financial markets seem willing and able to support them. In general, however, the approach to provide sector specific conditions should be replaced by a well-balanced and flexible system which covers all industries and sectors.

Secondly, current repayment terms permitted by the OECD Consensus are outdated compared to common market practices today, e.g. annuities instead of fixed repayment instalments plus interest. The current rules are difficult for many customers because they are not familiar with them or consider them as being too rigid and not advantageous for their businesses.

Thirdly, pay-per-use business models and new types of products that are typically not bound to physical exports, e.g. cloud-based and software solutions or discontinuous cash flow scenarios such as service-based product offerings cannot be covered by the current OECD Consensus. In that regard flexible repayment models, open residual values and low (or nil) down-payments must be considered. Similarly, there is not always a traditional sale of goods, e.g., a customer abroad may not buy a machine, but instead a right of use. The respective ECA cover would not relate to a physical export, but a cross-border contractual relationship. The structures and their legal consequences are diverse and would need to be covered by the Consensus as it exists today.

The efforts to fight climate change should also be reflected in a new OECD Consensus. The sector understanding on export credits for renewable energy was certainly a good first step to foster climate change mitigation projects. However, in our view, the focus is too narrow. It is mainly limited to renewable energy projects, though many other projects and sectors also contribute to climate change mitigation efforts, e.g. public transportation and electro-mobility. Moreover, the

OECD consensus currently lacks a clear set of minimum ESG standards. The OECD common approaches and related standards (IFC Performance Standards, World Bank EHS Guidelines) could be guiding principles and serve as a potential base line definition. Hence, they need to be fit for purpose to form a strong and respected framework is put into practice through engagement.

Therefore, we propose the following amendments to the terms and conditions of the Consensus.

Down-payment requirement

It remains difficult to source funding for the 15 percent of the export contract value, particularly for large government contracts. For public buyers / borrowers – especially in emerging and developing markets – the liquidity situation is sometimes challenging. Customers are forced to reserve liquidity for working capital that is lacking for investments, i.e., down-payments. Private insurance companies and commercial banks show little or no willingness to provide unsecured financing or risk cover (credit insurance) for "medium-term" advance payment financing. Furthermore, in addition to the effects of the Covid pandemic, many private buyers (e.g., in Southern and Eastern Europe, Asia etc.) often face liquidity shortages due to an increased need for regular working capital and for delivery and service scopes that cannot be covered by ECAs.

We propose that ECAs should have more flexibility to support the financing of the down-payment by a maximum cover of 95 percent of the export contract value, including third country supply, i.e. a minimum of 5 percent down payment but excluding local costs. This would be possible thanks to the amendment in force since 5 November 2021 but:

- This amendment is only valid for 12 months, while most files are discussed over larger periods of time, which might cause potential problems when files are finalized.
- The amendment only benefits loans extended to (or guaranteed) by a Sovereign borrower, whilst excluding most projects with public but non-sovereign entities and private buyers.

We would also like to express our appreciation to the OECD for the recently extended common line for another year until early November 2023. It is important to achieve an overall general need for a broader and more flexible approach to the currently strict handling of the down-payment for all supported projects.

Starting point of credit / start of credit repayment

In many cases customers in emerging markets reported that they face issues related to start-up curves, unforeseeable non-permanent disruptions, or seasonal effects at the time of finalizing a project. Moreover, these costs are associated to market failures caused by external factors but which overall do not disturb the covered business case.

We thus propose that the Starting Point of Credit should always be related to the start of the underlying business. The starting point should be the date of hand-over (e.g. provisional acceptance

date or start of commercial operation) of the underlying business. In cases in which the underlying business would technically allow for several handovers / starting points, the last of such handovers should become the common starting point of credit. The principal shall thus be re-paid and interest shall be paid not less frequently than every six months. Furthermore, the first instalment of principal and interest shall be made no later than 18 months, or at least one quarter after the complete fiscal business year of a borrower following the starting point of credit.

Maximum credit terms

The industry has been pointing to this specific reform backlog for a very long time. Meanwhile, the competitive environment has changed in non-OECD countries as well as in OECD member countries using more flexible conditions which makes the reform even more urgent. The rigid conditions of the OECD Consensus limit the otherwise positive aspects of ECA financing in customer discussions. In this respect, ECA-covered financing is no longer a self-running best seller. Furthermore, the instrument does no longer address the market needs. Many capital goods have a much longer economic life than is reflected by the repayment limitations of the Consensus.

We propose an increase to a maximum repayment period of 18 years for all transactions governed by the Arrangement. A solution is to be found especially when it comes to terms for higher risk categories in financially not viable infrastructure, water and Engineering, Procurement and Construction (EPC) projects. The current differentiation of tenor in the OECD Arrangement between corporate, sovereign, or bank risk loans and guarantees on the one hand, and project finance transactions on the other, should be terminated in favor of the longest possible available term.

All in all, it can be an opportunity to simplify the Arrangement which consider in different Annexes different maximum durations for different goods.

We take the opportunity to make Practitioners aware that the related pricing/premium for those longer tenures should be reasonable and not "over-stressed", as we have to keep in mind the global strong competition especially with global players acting outside the arrangement.

Market-reflective repayment profiles vs. consecutive instalments

In today's highly competitive environment many customers expect more flexible financing solutions. More flexible payment terms are necessary because the current repayment terms permitted by the OECD Consensus are outdated compared to market practice today, e.g. annuities rather than fixed installment amounts.

The OECD consensus lacks flexibility compared to other forms of financing. There is a need for debt service profiles to better reflect expected cash flow of the relevant borrower or project. Current repayment terms do not reflect product life cycles and are insufficiently linked to actual revenue generation. As a result, they do not address market requirements.

We propose to make more market-reflective repayment profiles possible and to increase the adaptability to current realities. Increased complexity of, e.g., building a large industrial plant, or commissioning an infrastructure investment, clearly needs to be reflected in its financing terms. More flexible repayment structures with the purpose of enhancing the competitiveness of exporters on the one hand but also strengthening borrowers' abilities to repay in a timely manner, is critical for many

sectors. Positive experiences with the various Sector Understandings and Project Finance rules underline the advantage of more market-reflective repayments, especially as commercial financial markets seem willing and able to support them.

We propose tying the loan life closer to the actual economic life of an asset, and, where appropriate, repayments to expected revenues (or budget allocations). This entails a more adequate credit definition, reflecting the commercial use of capital goods, complete plants or factories, as well as longer grace periods in line with borrowers' expected revenues, longer loan tenors coinciding with the reasonable commercial life of the underlying asset and more market-reflective forms of amortization (e.g., straight line semi-annual installments vs. digressive repayment to reflect life cycles, balloon repayment or adapting to seasonal requirements). Justification for longer repayment periods should also be weighed against the size of transactions.

We further suggest that Participants shall be able to support annuity loan (analogous to the aircraft sector agreement) for all sectors. For new business models such as service-based contracts, „pay-per-use“ transactions, cross-border leasing and/or rentals, Participants shall be able to provide individual support based on expected cash-flows. In cases in which an asset has a residual value at the end of the initially agreed credit term, it shall be permitted that the financing will not be fully repaid, but instead a roll-over solution shall need to be established at least six months before the end of the initial term. If this fails, the remaining loan shall have to be repaid fully within the original tenor. With new business models, the requirement for down payment and local cost rules shall not be applicable.

Especially for plant engineering, construction and infrastructure related businesses, there is the possibility of an individual agreement (without further and prior consultation) between users / beneficiaries of the Arrangement (exporters, buyers, borrowers, and banks) that allow them to offer the parties to differ without further and prior consultation as reflected in the following parameters:

- Interest payments are always to be made at least once annually according to the current loan status.
- Participants are granted the possibility to deviate without prior consultation in the OECD Group, leading to a more project finance related approach which would link projected cash-flow to the projected repayment terms going beyond the plain annuity regulation.
- Participants may opt for fixed assets with a normal market life cycle of at least ten years, the possibility of a repayment of 50 percent of the loan amount after ten years with the option of a subsequent one-off repayment or continuation of the repayment agreement for a further five or eight years (for the usual duration with the same repayment installments). Participants may allow to provide balloon repayment points related to repayments for assets with a normal market life cycle without further and prior consultation (notification).

Scope of the Consensus, definition of scope

The scope of the Arrangement is outdated and does not reflect new business models. The Arrangement also does not set parameters for programs outside its scope of rules, such as a provision for untied export credits, untied investment loans or untied development loans and for official support for equity investment.

We thus propose that the Arrangement shall apply to all official support provided by or on behalf of a government for cross border trade related or investment finance, including financial leases and new business models (e.g. service-based contracts, „pay-per-use“, cross-border lease and rent), which

have a repayment term of two years or more.

Minimum premium for credit risks

Non-OECD and OECD Competitors acting outside the Arrangement have created tools and mechanisms to subsidize premiums, interest rates, providing grants etc. without neither publishing nor notifying.

As the ECA premium becomes the ECA's main tool for regulating and pricing the choice of tenor, for assets with a very long-life expectancy or a second life expectancy following rehabilitation services, we propose to permit balloon structures that would not be fully amortized during the loan's life.

This can be especially relevant to infrastructure development and benefit sustainable use of resources. Especially for LDC's, a better coordination and combination with ODA instruments needs to be implemented to keep the global relevance of OECD players alive and foster exports and services from the Participants in the global environment. It might thus be worth considering creating a certain form of bonus related system on the premium for borrowers that have not produced any default, e.g. by providing a one notch better buyer category for the next project to be covered. For smaller transactions the notification requirements should be reduced.

This could be done without questioning the need for the ECA activities to be self-supporting over an economic cycle. Data from the OECD Export Credit Group show that since 1999, prior to any recovery, premiums have covered indemnifications and operating costs.

CIRR reform on a practical pattern

The CIRR is an important tool especially in terms of providing long term and reliable re-financing possibilities for sustainable infrastructure and long-term projects and is also a competitive tool in challenging markets with other global players which are not bound under the Arrangement.

Considering the upcoming implementation of new CIRR models we reach out to the OECD - secretariat and Practitioners to provide in due course further input and calculation possibilities for the upcoming new CIRR model starting from July 2023. We hope that during the 1st quarter 2023 Business representatives via BIAC may discuss practical matters concerning CIRR arrangement before the new CIRR model shall be effective and in force to use.



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