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Export credit financing

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Introduction

This update provides an introduction to export credit financing and the role it and export credit Financiers play in infrastructure projects. At its most basic level, export credit financing is financing provided by sovereign governments to promote the sale and export of products manufactured by resident companies.

Export credit financing is often used to fund infrastructure projects (especially those in the developing world) in conjunction with, or as an alternative to, more traditional project financing.

It enables SponsorSponsors and project companies to obtain more flexible (and often cheaper) financing arrangements. In addition to financing, export credit Financiers may also provide insurance, particularly political risk insurance that is either unobtainable or prohibitively expensive in the commercial market place.

The largest export credit agencies (**ECAs**) are those in the United States, Japan and Western Europe (for example, France and the United Kingdom). This paper examines the typical contents of an MOU and the practical and legal implications which arise as a result of entering into an MOU.

Generally, ECAs provide financing to two groups:

- manufacturers in their home country
- purchasers of the equipment manufactured by companies in their home country.

Financing for manufacturers

This update focuses on ECA financing for purchasers of equipment, however, we note the usual types of facilities provided to manufacturers are:

- working capital facilities
- loan guarantees.

Financing for purchasers

ECA financing support to purchasers has three basic forms:

- direct finance
- guarantees
- insurance (both commercial risk and political risk).

Direct financing means that the ECA lends money directly to the purchaser of the equipment. In respect of guarantees, there are many forms. One of the most common is a credit guarantee facility under which ECAs provide guarantees to Lenders in their home jurisdiction for loans to foreign banks which are then on lent to foreign purchasers of home jurisdictions goods or services.

The common feature of these types of support is they will only apply to the home country portion of the goods being financed.

Therefore, if a product contains parts manufactured in multiple places it may not be suitable for ECA financing. However, some ECAs, for example the United States' ECA, the Export and Import Bank (USEXIM), will finance goods not entirely manufactured in the United States providing the goods are shipped from the US to the foreign purchaser. There are, however, strict rules as to what foreign manufacture content applies for

USEXIM financing and what does not. Therefore, if this will be relevant to your project you should seek specific advice on this point.

Insurance provided by ECAs can cover both commercial risk and political risk. Political risk covers events like war, expropriation, rescission of licences and imposition of foreign exchange controls. The use of this insurance is discussed in more detail below.

Features of eca financing

Many ECAs also have specific project financing programs which are tailored to suit the requirements of project companies and commercial Lenders. These programs combine the basic forms of financing described above into packages which meet specialised requirements of a limited recourse project financing. The repayment schedule will be tailored to the expected cash flow of the project and should not, in most cases, require repayments to be made until the end of construction. Note, there are limitations on the maximum average loan period which are usually determined based on a location of the project.

For example, the British ECA, the Export Credits Guarantee Department (**ECGD**), will provide direct finance to the Project Company as well as providing credit support. ECGD will provide guarantees to the commercial Lenders of up to 100% of the outstanding principal and interest. Similar facilities are available from USEXIM and COFACE, the French ECA.

If applying for finance under an ECA project finance program, you can expect the ECA to undertake a similar type of due diligence process as commercial Lenders. However, the support provided by an ECA is generally provided on more favourable financial terms than that provided by commercial Lenders. As a result, there will be additional requirements that will have to be satisfied which commercial financing does not require.

ECA financing can also be used to support commercial finance and attract finance that would otherwise be unavailable. In effect, the commercial Lenders rely on the sovereign guarantees provided by the ECAs to support the borrowings of the Project Company. For example, political risk insurance provided by an ECA often forms a crucial part of the credit support package provided to commercial Lenders. As a result, if a project is expropriated prior to the loans being repaid, the ECA will repay up to 100% of the outstanding principal and interest.

Difficulties may arise if financing is sought from two or more ECAs because they often have conflicting rules. For example, USEXIM requires all lending documents to be governed by New York Law whereas ECGD (as well as many of the commercial Lenders) are likely to prefer English Law.

As a result of the strict rules about was does and does not qualify for ECA financing, it is vital that Sponsors and project companies who wish to utilise ECA financing make provision for those rules from the outset. For example, the content requirements may impact on the choice of the construction Contractor. In addition, a Project Company may be willing to accept a higher contract price if as a result of contracting with a certain party or by stipulating certain items of plant and equipment the overall financing will be cheaper.

It is common for EPC Contracts to contain local content requirements that oblige the Contractor to source materials from the country where the project is being constructed. Similar provisions will be required if ECA financing is used to ensure the Project Company continues to qualify under the rules of the relevant ECA.

ECA financing is often used in collaboration with other non-commercial Lenders, for example, the Asian Development Bank and European Bank for Reconstruction and Redevelopment which further decreases the financing costs but can increase complexity, particularly given there are often differing requirements between the ECAs and the banks.

Political and environmental considerations

Increasingly, ECAs have been targeted by environmental activists and other organisations concerned with debt burdens of developing countries. ECAs have been accused of lending money without consideration for environmental or social issues in the countries where the projects to which they lend are located.

Therefore, many ECAs are now undertaking environmental analysis of large scale projects before they agree to lend. In addition, USEXIM is subject to congressional oversight. As a result, there are limitations, both of an environmental and political nature, in relation to the projects USEXIM will finance.

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