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REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

Annual Report on negotiations undertaken by the Commission in the field of export credits, in the sense of Regulation (EU) No 1233/2011

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1. Introduction:

Regulation (EU) No 1233/2011 of the European Parliament and of the Council of 16 November 2011 on the application of certain guidelines in the field of officially supported export credits and repealing Council Decisions 2001/76 EC and 2001/77/EC[1] foresees in its Annex I that the European Commission "according to its competencies shall provide to the European Parliament an annual report on negotiations undertaken, where the Commission has negotiating authorisation in the various forms of international cooperation, to establish global standards in the field of officially supported export credits."

The present report covers the period March 2013 to March 2014.

2. Major developments in export credits in 2013:

Traditionally, most of the Commission's negotiation activities in this policy area take place in the Organisation for Economic Co-operation and Development (OECD), which so far remains the only international body which has developed detailed technical rules for export credits. The European Commission, in the framework of its responsibility to carry out trade negotiations, represents the EU in all negotiations concerning the **OECD Arrangement on Officially Supported Export Credits**[2] and its **Sector Understandings** (which cover special financing rules for specific industrial sectors), namely:

- the Sector Understanding on Export Credits for Ships
- the Sector Understanding on Export Credits for Nuclear Power Plants
- the Sector Understanding on Export Credits for Civil Aircraft
- the Sector Understanding on Export Credits for Renewable Energy, Climate Change Mitigation and Water Projects.

The negotiation work in the OECD continues, leading during the reporting period *inter alia* to the adoption of a new Sector Understanding on Export Credits for Rail Infrastructure and to talks on expanding the scope of the Sector Understanding on Renewable Energy, Climate Change Mitigation and Water Projects (for details see section 4).

The OECD Arrangement has in general been effective in providing a level playing field between the export credit programs of its Participants. However, major emerging export credit providers like China, India or Brazil[3] are not parties to it.

The establishing of the International Working Group on Export Credits ("IWG") – following a joint initiative by President Obama and then Vice-Premier Xi Jinping in February 2012 – has created a strategic opportunity for OECD Participants and non OECD Participants to work together on a new set of disciplines on export credits in a completely new environment.

[1]. OJ L 326, 8.12.2011, p. 45.

[2] The "Arrangement" is a Gentlemen's Agreement between the EU, the United States, Canada, Japan, Korea, Norway, Switzerland, New Zealand and Australia that exists since 1978 and has the main objective of ensuring a level playing field between the export credit programs of its Participants. The Arrangement and its subsequent modifications have regularly been transformed into EU law.

[3] A particular case is Brazil, which is only a Participant to the Sector Understanding on Civil Aircraft, but shows no interest to join the general Arrangement as such.

The European Union has therefore fully supported the IWG process from the start. In 2013, the IWG remained an essential priority, relevant activities taking an even bigger proportion in the EU's export credit work than in 2012 (for details see section 3 below).

3. The International Working Group on Export Credits:

It will be recalled that at the outset, altogether **18 "major providers of export credits"** were invited to join the new **International Working Group on Export Credits ("IWG")**: All 9 Participants to the OECD Arrangement on Officially Supported Export Credits (EU, US, Canada, Japan, Korea, Norway, Switzerland, Australia and New Zealand) as well as China, Brazil, the Russian Federation, South Africa, India, Indonesia, Malaysia, Turkey and Israel. It was agreed that a **Steering Group –** composed of the US, the EU, China and Brazil **–** would meet in advance of the plenary sessions of the IWG. The IWG has no permanent chair, secretariat or venue. Meetings are hosted on a rotating basis by the members of the Steering Group.

As mentioned in the Commission's previous report, initial discussions in the **First official meeting of the IWG** (held in Washington in **November 2012**) had not been easy. Most of the IWG participants would have liked to immediately focus on general, horizontal rules applicable to all export credits, China however insisted on a "**sectoral approach**", i.e. that the IWG should first look at export credit practices in specific industrial sectors and only in a second phase focus on horizontal rules. While the principle of the sectoral approach as such was eventually accepted as a working method by the IWG, the choice of the sector(s) to be looked at proved to be controversial: China insisted on the ship sector, although it was well known that the US and several other IWG Members have no export credit activities in that sector at all. Proposals to identify at least a second sector (so that all IWG Members could actively participate) were not immediately successful.

In order to find a way out of this stalemate, the **EU Delegation** offered to host an **informal meeting**, in which Delegations could continue discussions at an expert level. This event, organised in Berlin in **March 2013**, had a very positive effect on the working environment in the IWG (technical experiences made by the various participants in various industrial sectors were discussed in a constructive mood). At the **Second Official Meeting of the IWG**, hosted by **China** in Beijing in **May 2013**, it was subsequently possible to agree on a second sector **–** medical equipment. While medical equipment is usually not considered a sector of massive export credit intervention, the absence of specialised export credit practices in this sector makes it a suitable proxy for discussions on general, horizontal rules. The Chinese Delegation has repeatedly acknowledged that the sectoral approach is not supposed to lead to the formal conclusion of Sector Understandings (like they exist for example under the OECD Arrangement), but that the IWG would move to horizontal talks as soon as discussions on the ship and medical equipment sectors have sufficiently matured.

The **Third Official Meeting** was hosted by the **EU** in Brussels in **September 2013**. The EU tabled a detailed technical discussion paper addressing such fundamental issues as the potential overall objectives of the IWG process as well as the role of the discussions on the ship and medical sectors as building blocks for a future horizontal agreement on export credits. Moreover, the paper presented detailed considerations and questions to IWG participants on how to define the scope of discussions (i.e. how to delineate the two economic sectors in question, how to define the official support mechanisms to whom the new guidelines should apply) and how to address specific non-price related aspects (such as down payments, maximum and minimum credit length, repayment profiles and security packages) as well as price related elements of export credit transactions (base interest rates, credit risk premium and fees). This contribution was well received by the other IWG Participants and the Group had very productive discussions in the plenary meeting. There were also a lot of high quality presentations, notably from other OECD Participants, but the non-OECD Participants like China also engaged themselves actively in the discussions. In general, the Brussels Meeting marked a clear step forward, as was the start of genuine technical discussions in the Group.

The **Fourth Official Meeting** was hosted by **Brazil** in Brasilia in **January 2014**. Discussions on the two sectors continued (still on the basis of written answers to the questions included in the EU discussion paper tabled at the Third IWG Meeting). It was concluded that the IWG would move from the phase of exchanges on current export credit practices to more specific text-based discussions (i.e. Delegations would table papers with specific draft financing modalities for the two sectors, in order to allow more concrete discussions). This approach will be applied at the **Fifth Official IWG Meeting**, which the US is going to host in **Washington on 20-22 May 2014**).

If we were to draw a **provisional balance of the IWG process at this stage**, the picture is a mixed one:

On the positive side, it has to be stressed that already the successful establishing and continued operation of such a forum, in which OECD and non-OECD providers of export credits regularly meet to discuss regulatory issues is in itself no small achievement. It must be kept in mind that all previous efforts to notably engage China in similar talks at bilateral or multilateral level were not successful. Among the most important non-OECD export credit providers, only India has so far not formally joined the process, but participated as an observer to the Fourth Meeting.

The EU, although not among the immediate initiators of this process, has asserted itself as a major player, having organised two successful meetings and contributed with a lot of substantial contributions and a paper that still seems to shape IWG discussions.

A real problem at this stage is however the fact that the activities of the IWG are for the time being very much driven by its OECD participants. With the exception of South Africa and Turkey, many non-OECD participants are rather cautious when it comes to making active contributions (e.g. presentations). Written papers have so far almost entirely been provided by OECD Participants.

The meetings to be held in 2014 will certainly be crucial for an assessment whether all IWG Members are seriously committed to the process and whether the latter is likely to develop beyond the level of preliminary talks. In case that the IWG process is likely to enter into a phase of formal negotiations, the Commission would seek the necessary authorization in line with the Treaties.

4. Developments in the OECD during the reporting period:

The participants to the OECD Arrangement finalised a two-year negotiation for the **Sector Understanding on Export Credits for Rail Infrastructure ("RSU")** in November 2013. The RSU, which was a big ambition of the EU, establishes some specific financing conditions for the exports of rail infrastructure assets essential to operating trains, including rail control, electrification, tracks, rolling stock and related construction work. The RSU foresees extended repayment terms for such export credit transactions[4], differentiating between exports to High Income OECD countries (for which the maximum repayment term is 12 years) and to all other countries (for which the maximum repayment term is 14 years) as well as some flexibilities on the repayment profile. In order to achieve this deal, some concessions had however to be made to accommodate concerns that private market financing available concerning High Income OECD countries would not be undercut. RSU based export credits to these countries are subject to prior notification to the other OECD participants (including a comprehensive explanation). If notably export credits account for the majority of the financing of an export to a High Income OECD country, a waiver has to be requested. Globally, Europe is both the biggest market for rail products and has the highest concentration of railway equipment industries.

The EU is also the driving force behind two add-ons to the **2012 Sector Understanding on Export Credits for Renewable Energies and Climate Change Mitigation (CCSU).** The sectoral extensions currently under negotiation concern climate change adaptation projects and electricity smart grids. The EU is home to several key industrial players in these areas. The **Climate Change Adaptation** dossier has been discussed longer and is a bit more advanced than the **electricity smart grids** dossier (on which the OECD has now entered a phase of technical discussions about basic definitions). Not all participants seem to have an active interest of their own in these dossiers.

At the last export credit meetings of the OECD, a joint proposal by the EU and Canada was tabled on climate change adaptation. The US delegation announced that they would comment on the proposal in due course. OECD participants remain in principle open to working further on smart grids, but it will be necessary to propose a generally acceptable definition of the term as well as a sound justification for the need to use export credit financing in this area. The various climate change dossiers will be taken up again by the OECD in the next meetings on export credits in 2014.

An area of strategic importance is the **review of the interest rate provisions of the OECD Arrangement:** The Arrangement includes minimum fixed interest rates provisions agreed on in the 1980's. Participants are currently working on the modernization of these provisions, as well as on the inclusion of rules defining minimum floating interest rates. This overall review has been triggered by changes in banking markets in the aftermath of the financial crisis, which put into question the non-distortive character of existing rules. The EU is probably the

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[4] The Arrangement's general rule on maximum repayment terms is 5 years (under certain circumstances 8,5 years) for exports to OECD High Income countries and 10 years for exports to all other countries, The Arrangement however contains more extended maximum repayment terms for a number of industrial sectors and specific transactions (the most far-going rule being 18 years under the Nuclear Sector Understanding and for certain transactions under the Sector Understanding on Renewable Energies, Climate Change Mitigation and Water Projects)

participant whose export credit system is the most reliant on commercial banks and should as such play a crucial role in the negotiation.

While several other participants have no official position yet, the Commission has managed to obtain the consensus of the Member States on **four guiding principles** on the interest rate review:

1. Further harmonisation of export credit practices concerning the selection and holding of fixed interest rates.
2. The predictability currently embedded in the fixed rate system of the Arrangement should be maintained, but be priced more adequately.
3. The basic construction of the fixed interest rate system (the “CIRR”) should be maintained for reasons of preserving the compliance with the Agreement on Subsidies and Countervailing Measures’ (“ASCM”) “safe haven”, but the margin charged on top of the base rate (currently a fixed number of basis points) should become more reflective of the level of rates charged by commercial banks.
4. Floating rates should be included in the OECD Arrangement.

On the basis of these principles, the Commission is now working on a more substantial proposal, which the EU could table in the OECD later in 2014.

Aircraft traditionally has been the most important export credit sector in commercial terms. In recent time, there have however been no major new developments. Implementation of the **2011 OECD Sector Understanding on Export Credits for Civil Aircraft** (the “ASU 2011”) continues (nominally, a review is foreseen for 2015).

The Commission will duly keep the European Parliament informed on new developments.