

## **Credit Terms**

In bidding for capital goods and services contracts and projects overseas, credit and financing terms are often a major factor. ECGD's aim is to help UK exporters win business, and ECGD will always try to help exporters to construct the best possible credit package. As well as protecting exporters and banks against political and commercial risks, ECGD guarantees can give access to fixed rate finance.

The precise terms that ECGD can support for a particular transaction will vary according to the size and nature of the contract and the buyer's country. However, the credit terms which an exporter can offer to a buyer with ECGD support are usually longer than those available in the commercial market.

This section explains the kind of terms that an exporter can expect in support of business where the buyer requires credit of two years or more. Whilst it will always try to provide the best possible support for UK exporters, ECGD, like similar organisations in other countries, is subject to certain commercial constraints and international obligations, as set out below.

### **Commercial**

ECGD is expected to run insurance operations so as to generate sufficient reserves to give the level of assurance of breakeven required by Ministers. To achieve this, like any other insurer, ECGD has to take in enough premium to its claims and overheads. ECGD has to examine the risks on each piece of business very closely and price them accordingly. While ECGD will always try to help exporters, the risks of non-payment in some countries are so high that ECGD cannot consider insuring them at all, or it may have to limit its exposure and allocate cover on a first come first served basis. Similarly, not all buyers or projects represent acceptable commercial risks.

### **International**

As the UK is a member of the European Union (EU) and the Organisation for Economic Co-operation and Development (OECD), ECGD is bound by the OECD Arrangement on Officially Supported Export Credits (known as the 'Arrangement' or 'Consensus'), which underpins elements of the Subsidies Code in operation at the World Trade Organization. The Arrangement has been incorporated into EU law. This agreement was designed to stop the 'credit race', which was speeding up during the early 1970s, and later to regulate the increasing use of tied aid finance. The Arrangement regulates levels of risk premium, maximum repayment terms and officially supported interest rates for goods and for services involving two or more years' credit. This section concentrates on the maximum terms as set out by the Consensus, including special sectors covering large aircraft, ships and nuclear power stations.

ECGD is also a founder member of the Berne Union, the worldwide association of credit insurers, which promotes the international acceptance of sound principles of export credit insurance and the establishment and

maintenance of discipline in the terms of credit for international trade. This body also acts as a forum for exchanging information and, to a more limited extent than the Consensus, also acts as a brake on escalating credit terms.

## **The Credit Terms**

The terms which ECGD can support for a sound project with a creditworthy buyer are as follows:-

### **• Starting point of credit**

The Arrangement mirrors the Berne Union rules on the point at which the credit period starts. This starting point of credit fixes the date at which the buyer has to start repaying the credit in relation to the type of goods or services being supplied. For parts and components, quasi-capital goods, and capital goods consisting of individual items usable in themselves, the latest date is the date of acceptance of the goods or the weighted mean date of acceptance. For services the latest date is submission of invoices or acceptance of the service by the client. For parts and components, quasi-capital goods, capital goods and project services and complete plants or factories where the exporter has responsibility for commissioning, the latest starting point is at commissioning. For complete plants or factories where the exporter has no responsibility for commissioning, the latest starting point is the date of physical possession of the equipment by the buyer(s).

### **• Length of credit**

The period over which a buyer can pay for the goods and services is governed by the three constraints mentioned above: the Arrangement, the Berne Union and ECGD's underwriters' commercial judgement. The Arrangement sets out maximum credit periods according to the buyer's country. There are two categories of country, set out below, for which the following maximum credit periods apply:

- Category I countries – normally five years but after prior notification up to eight and a half years.
- Category II countries – up to 10 years.

OECD Consensus country classifications can be found at:

<http://www.oecd.org/dataoecd/32/48/43407491.pdf>

A few countries have not been classified as yet by the OECD. If you have a prospective contract in any one of these countries please speak to the underwriter for your sector.

ECGD cannot support credit terms for general capital projects longer than those set out above. Longer credit terms up to a maximum of 18 years can be supported for renewable energy and water projects and nuclear power plants. This compares to 12-year terms available for other non nuclear power projects. For project financing cases ECGD is able to tailor the repayment

terms to the cashflow of the project up to a maximum credit period of 14 years. For further details, please see the section on Project Financing.

The Berne Union has established maximum credit terms for particular categories of goods that also take into account contract values. There are far too many of these to list here, but it is worth bearing in mind that for exports of particular goods or for particular contract values, the payment terms may be shorter than those in the Arrangement. ECGD underwriters will also use their commercial judgement to determine whether these maximum credit terms are appropriate for a particular piece of business.

Repayment of the credit must be in equal half-yearly, or more frequent, instalments. The first is payable six months from the starting point of credit. Interest also has to be paid at least semi-annually and is usually paid on the reducing balance of the principal outstanding.

### **Cash/direct payments**

The Arrangement requires that the buyer must pay at least 15 per cent of the contract value before the starting point of credit. This means that the credit terms outlined above apply to a maximum of 85 per cent of the contract value. ECGD also requires that at least 5 per cent of the contract value to be paid on or before the date on which the supply contract becomes effective.

### **Interest rates**

ECGD may provide interest equalisation support for a fixed interest rate under an export credit loan throughout the period of an export credit – see Officially Supported Rates below – or ECGD may provide a ‘pure cover’ guarantee under which it guarantees repayment of the loan at a fixed or floating commercial interest rate agreed by the lending bank and the Borrower – see Pure Cover below.

### **Officially Supported Rates**

ECGD’s support for fixed interest rates is given through ECGD’s Fixed Rate Export Finance (FREF) scheme in which approved banks participate. This scheme enables a bank to offer fixed interest rates to overseas buyers by ensuring that it will, at the end of each interest period under the relevant loan, receive from ECGD any shortfall between the amount of interest receivable from the borrower at the agreed fixed rate and the amount which would have been receivable if the interest rate had been equal to London Inter-Bank Offered Rate for deposits in the currency of the loan for a term equal to the interest period (“**LIBOR**”), plus the bank’s margin on the loan. Conversely, if, in any interest period, interest on the amount outstanding under the loan at LIBOR plus the bank’s margin is less than the fixed rate interest receivable from the borrower, the bank will pay the excess to ECGD.

The current FREF scheme (2005 FREF) was introduced on 1 April 2005 and is due to expire on 31 March 2011. Under this scheme ECGD interest rate

support will only be available in cases where (a) ECGD has issued an offer of support before 1 April 2011 and (b) all of the conditions set out in that offer have been satisfied before the end of the period for which it is expressed to be open for acceptance. (However, FREF support may be available after 31 March 2011 under such new FREF scheme, if any, as ECGD may introduce in place of the current FREF scheme.)

The Arrangement regulates the minimum fixed interest rates that can be made available with support from exporters' governments. These rates are known as Commercial Interest Reference Rates (CIRRs), and vary according to the currency of finance, and are available for three repayment profile maturities: up to five years; over five and up to and including eight and a half years; and over eight and half years.

CIRRs are calculated on the 15th of each month for most of the main trading currencies according to criteria specified in the Arrangement and are intended to reflect what the market rate would be for long-term, fixed-rate export finance for a first class corporate borrower, if such finance were commercially available. Once the applicable CIRR is fixed in relation to a particular ECGD-supported loan in the manner described below, it remains valid for the entire term of that loan.

The current CIRR rates can be obtained from ECGD's website ([www.ecgd.gov.uk](http://www.ecgd.gov.uk)). For a particular transaction, please contact the ECGD Helpline on +44 (0) 20 7512 7887 for details of the relevant underwriter for your sector.

Under the 2005 FREF Scheme, the interest rate that ECGD may agree to support under the revised scheme will be the CIRR prevailing at or about the time the lending bank releases the relevant loan agreement for signature by all parties. In most cases the interest rate specified in the loan agreement will only be applicable if the loan agreement is signed by all parties within the initial 30-day period. If, within that 30-day period the loan agreement has not been signed by all parties, then the held rate will no longer apply. At this point if ECGD's offer of support is still valid, a new supported rate will be determined on that day and held for a further 30 days and again on each successive thirtieth day within the validity period of ECGD's offer of support. When the period for acceptance of an offer of support has expired, ECGD's commitment to provide FREF support ceases.

However, for contracts with public or sovereign buyers in certain specified countries the initial period for which the rate will be held is 60 days. The countries concerned are: Mexico, Iran, Brazil, Turkey, Vietnam, Libya and Uzbekistan. ECGD will also consider, on a case-by-case basis, other markets for holding of the CIRR for 60 days, subject to customers at that time providing ECGD with legitimate reasons for this proposed concession.

In addition, the initial period for which the rate will be held will be 60 days for Supplier Credit Finance facilities where either the premium is being paid out of

the loan or the transaction involves the use of bills or notes, irrespective of the identity of the borrower or the country where it is established.

Further information about the revised scheme, and any changes made to it from time to time, will be posted on our website ([www.ecgd.gov.uk](http://www.ecgd.gov.uk)).

### **Currency of finance**

Under the 2005 FREF scheme ECGD can provide support for a loan denominated in Sterling, US dollars, euros and Japanese Yen provided that the amount to be advanced under that loan does not exceed £50m, \$90m, €70m or, as the case may be, JPY10,000m. For more information please contact Vasso Agapitou on +44 (0) 20 7512 7040.

### **FREF after 2011**

In December 2007 ECGD launched a public consultation on the future of FREF support. ECGD published an [Interim Response](#) to that consultation in March 2008 which, among other things, announced the extension of the validity of the 2005 FREF scheme to 31 December 2008. The availability of the scheme was further extended twice, to 31 December 2009 and to 31 March 2011, subject to the continuing availability of funds under the existing FREF budget. A Final Government Response will be published prior to the expiry of the current FREF scheme (by 31 March 2011) in order to announce whether, and in what form, ECGD will continue to provide FREF support after that date.

### **Pure cover**

ECGD can give guarantees for the repayment of finance without FREF support – this is known as 'pure cover'. This often means the borrower will have to pay a commercial floating rate of interest, although fixed-rate commercial financing may be available in some currencies.

Contracts financed on a pure cover basis are not bound by the minimum interest rate rules of the Arrangement. However, they are subject to all the other points on credit terms set out in this section.

## Foreign content

In recognition of the fact that UK exporters may source goods and services from a variety of countries, in June 2007, ECGD announced simplified and more flexible rules for UK exporters looking for support for export contracts involving the sub-contracting of work to non-UK firms. The main points of the simplified rules are:

For all contracts (credit or cash) the maximum level of support for foreign content will be 80 per cent of the contract value, where ECGD risk capacity is available;

The distinction between contracts valued at £10m and below or above £10m will be removed;

The distinction between goods originating from the EU or Japan and other countries will be removed; and

Software and related services originating in the UK and exported electronically will be regarded as UK goods/services

Where ECGD cannot support an export contract under its foreign content rules, it may nevertheless be able to do so by obtaining reinsurance in respect of the value of any foreign goods and services comprised in that contract from the national export credit agency of the country from which those goods and services originate.

For information on ECGD's reinsurance agreements with other export credit agencies, please contact Tahir Ahmed on +44 (0) 20 7512 7569.

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