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The Role of Korea's Export-Import Bank in the Country's Export Insurance and Financing Programs

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International Trade & Capital Flows Division
Economic Analysis and Projections Department
Development Policy Staff
The World Bank

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Summary and Conclusions

Export credit insurance and financing programs of most industrialized countries have been evolving into an increasingly-complex structure of nationally-supported facilities to promote exports. This development has been particularly rapid over the past several years. The more advanced developing countries, like Korea, have also begun to play significantly-competitive roles in exporting industrial goods on credit which, in their case, is becoming a major element in the drive to accelerate development.

Korea's emergence as a source of export credit insurance and financing was reflected in two recent events. The first was the establishment of an Export-Import Bank (hereafter "Eximbank") on July 1, 1976 and the other, linked to it, was the agency's acceptance a year later as a member of the Berne Union, the international grouping of official export credit insurance agencies from 27 countries. Korea thus became one of nine developing countries to join the Berne Union 1/ and the first to set up an export-import banking institution.

The variety and nature of Korea's Eximbank services appear to be adapted to the character of Korea's economy (which, like that of the Japanese, is export-oriented and industrialized, dependent upon external sources for virtually all raw material requirements). The Eximbank's programs are modelled upon Japan's intricate pattern of utilizing various funding sources, both public and private, to promote exports, to encourage

1/ The others are Argentina, Hong Kong, India, Israel, Pakistan, Portugal, Singapore and Spain.

imports of needed raw materials, and to finance investments abroad which facilitate both exports and imports. In addition, insurance cover against the usual risks encountered in international transactions is available for private export credits and investment capital. Contrary to the Japanese system, however, Korea's wide-ranging programs are integrated within one institution, the Eximbank.

The formation of the Eximbank is said to be a direct outgrowth of Korea's recent shift from the exports of consumer and light capital goods to the technically more-advanced products of the chemical and heavy capital goods sectors. This change is reflected in the rising share of heavy capital goods and chemical products in manufactured exports from 6 percent in 1962 to 30 percent in 1975 and 37 percent in 1978. Exports from these sectors generally involve larger credits and longer terms than the private sector is prepared to provide without assistance. Korean manufactured exports have traditionally been given substantial Government support, largely through the rediscounting facilities of the central bank (Bank of Korea). However, such support, while extensive, has generally been of a short-term nature. The principal objective behind the Eximbank's establishment was to meet the increasing demand for longer term financing more appropriate to heavier industrial exports and by this means to accelerate their growth. 1/

1/ It should be noted that this report is limited to a summary of the organization, functions, objectives and performance of Korea's Eximbank as the Government's selected vehicle for encouraging the exports of heavy industry. It does not deal with other Government programs of preferential financing for manufactured exports or with the related and extensive support given to material inputs used in the production of manufactured exports. For further details, see Attachment.

The bulk of the Eximbank's financing to date has been focused in the ship export sector and the construction of industrial plants overseas. Eximbank financing takes the form primarily of preferential loans to Korean suppliers at a standard and fixed interest rate of 7 percent per annum with maturities extending from six months to ten years and, exceptionally, to 20 years. Typical Eximbank financing covers 70 to 80 percent of a supplier credit. Since the balance is financed commercially, the "blended" interest rate on Eximbank-supported supplier credits is said to be in excess of 9 percent. The extent of the subsidy element implicit in the Eximbank's preferential lending is suggested in the levels of the commercial prime rate in Korea, currently at 18.5 percent, and that of Eurodollars at close to 11 percent. 1/ The Eximbank's "blended" rate on supplier credits compares favorably with similar financing available in major industrial countries. As of March, 1979, these rates were reported to fall in a range from 8 to just under 10 percent. 2/

The Eximbank is also authorized to offer preferential financing for a large variety of inter-related services which include the extension of credits to Korean firms which provide technical services abroad (generally in connection with the construction of industrial plants), to other governments and private entities abroad which import manufactured goods or technical services from Korea, to Korean imports of essential raw materials including

1/ The six-month LIBOR (London Inter-Bank Offer Rate).

2/ When considering the subsidy element in Eximbank's lending, it is important to bear in mind that the non-Eximbank system of preferential financing for Korean manufactured exports, referred to earlier, also implies a substantial subsidy at comparable rates but for very short maturities. For instance, general commercial bank credit against accounts receivable for exports is currently available for about 80 percent of export value up to 135 days at 9 percent per annum.

those to be used in exported goods and to Korean and foreign investors in other countries who facilitate such imports or promote Korean exports. Not all of these other programs have yet been activated, but they do provide an indication of the unusually-broad scope of the Eximbank's foreign trade objectives.

The volume of Eximbank preferential financing, although small in relation to overall preferential financing for exports (an estimated 10 percent of total preferential financing for exports outstanding at the end of September, 1977), has been expanding rapidly. For instance, credit authorizations of almost \$570 million during 1977 and 1978, the first two full years of the Eximbank's operations, amounted to two-thirds of the aggregate authorizations issued since 1971. Furthermore, the Korean Eximbank's authorizations in 1977 were equivalent to 2.2 percent of total merchandise exports in three years, as against 3.2 percent for the Japanese Eximbank, a major competitor. This international comparison reflects well upon the Korean Eximbank's performance especially in view of its relatively recent origin.

The Eximbank's insurance programs provide cover for most of the same categories of external financing supported directly by its lending facilities. Thus far, the insurance programs have lagged considerably behind the Eximbank's lending, largely because of deliberately cautious underwriting caused by a heavy incidence of commercial payment difficulties. During 1978, for example, insurance commitments amounted to only \$136 million. For the most part, however, the Eximbank's export credit insurance programs are comparable to those offered by other exporting countries.

From the available evidence, it appears that the Korean Eximbank, at a still modest but accelerating pace, is achieving its twin objectives of providing financial incentives to diversify the export product mix (into capital goods) and the geographic destination (toward developing countries) of Korean exports. 1/ On a broader scale, the establishment of the Korean Eximbank also marks an important point in the evolution of developing countries. The growth of capital goods exports from such countries as Korea, their sharpened competition in this area with the traditional exporters in the developed countries, and their dual role as substantial borrowers as well as lenders to finance expanding exports of capital goods, has been one of the less-noted but potentially far-reaching developments of the present decade. The Eximbank, the sole such institution to date in the LDCs, appears well-equipped to provide the Korean Government with a versatile and responsive instrument to expedite this evolutionary process. 2/

Organization

Although the Eximbank was not formally established until mid-1976, its functions were officially promulgated in 1969. Financing operations were temporarily delegated to the Korea Exchange Bank (a commercial bank wholly-owned by the Government and mainly engaged in foreign exchange business and trade financing), while export credit insurance underwriting was entrusted to the Korea Re-insurance Corporation (a private company). Under enabling

1/ A secondary objective of the Eximbank is to facilitate the exports of capital goods to developing countries, where over three-quarters of its credit authorizations were concentrated in 1978.

2/ Korea is not the only developing country to provide preferential financing for capital goods exports, but the only one with an institution like the Export-Import Bank.

legislation, the Eximbank now operates as an autonomous agency of the Korean Government performing the various services noted in this report on behalf of the Government and financed by public funds as well as borrowings on private domestic and foreign markets.

Policy is formulated by the so-called Operations Committee which provides basic guidelines for the agency's financing transactions. The Committee is composed of eight members: (1) four officials at the level of Assistant Minister--one each from the Economic Planning Board and the Ministries of Foreign Affairs, Finance, and Commerce and Industry; (2) an assistant governor of the Bank of Korea; (3) a director of the Korea Exchange Bank; (4) a representative of the Korea Traders' Association; and (5) the President of the Eximbank who acts as chairman and has the right to vote in the event of a tie. Day-to-day operations are managed by a Board of Executive Directors consisting of officials of the Eximbank, chaired by the President.

The insurance functions performed by the Eximbank are under the statutory control of the Minister of Commerce and Industry, assisted by an Export Credit Insurance Council composed of public and private members (see Section II below). The Government pays Eximbank an "agent's commission" to administer the export credit insurance program. An Export Credit Insurance Fund, originally set up in 1969 to support underwriting activities, is now administered by the Eximbank and maintained in an account distinct from its own resources which are utilized exclusively for lending purposes. Thus, the Korean Eximbank acts in its own name, under statutory authority, for financial transactions but in an agent's capacity for export credit insurance. In practice, however, the Eximbank is said to exercise a wide degree of autonomy in export credit insurance matters.

I. Export Credit Financing Programs

A. Resources

The authorized capital of the Eximbank at the end of 1978 amounted to 500 billion won (roughly equivalent to \$1 billion), 1/ of which 140.4 billion won (\$290 million) was paid in. The rapid growth of the Eximbank's activities is reflected in the virtual tripling, during a brief period of less than two and one-half years, of authorized and paid-in capital. The Government directly (40.4 billion won), the Bank of Korea (40 billion won) and the Korea Exchange Bank (60 billion won) are the official subscribers to the authorized capital. The Eximbank may also borrow domestically and on foreign markets up to ten times its paid-in capital. Local currency funds, apart from official paid-in capital, may be procured at preferential rates 2/ from the National Investment Fund (a Government agency to promote domestic investment) and domestic banks. Foreign funds may be raised through loans and credit lines with foreign banks and the Bank of Korea as well as through sales of promissory notes secured with export credit claims. In addition, the Eximbank may have recourse to bond markets and engage in co-financing with foreign banks to support large-scale projects.

1/ The average market rate of 484 won per dollar as reported in the IMF's International Financial Statistics has been used for conversions in this study.

2/ Currently at 5 to 6 percent per annum. As noted, Korean commercial bank lending to prime borrowers is at 18.5 percent per annum.

To date, the Korean Eximbank has had access to foreign exchange resources amounting to approximately \$650 million. Of this amount, \$290 million consist of credit lines, \$40 million with foreign banks and \$250 million with the Bank of Korea. In June, 1977, the Eximbank ventured for the first time on the Eurocurrency market when it sold \$158 million in Notes to a syndicate of ten foreign banks in which Swedish banks predominated. The terms were eight years with an interest rate spread of 1-1/4 percent over LIBOR. The Notes were held by the Eximbank against loans extended to two Korean ship-building firms to finance the export of ships to Sweden and Canada. The transaction was basically a refinancing of export credits on foreign markets but with a fine twist since it facilitated the sale of ships to Sweden with funds borrowed in large part from Swedish banks.

The Eximbank's second Eurocurrency borrowing was a well-publicized and highly-successful syndicated bank loan of \$200 million signed in December, 1978. The terms stipulated a maturity of 10 years including a three-year grace period, and a spread above LIBOR of 5/8 percent for the first two years, and 3/4 percent thereafter. The good terms accorded to the Eximbank's first two transactions on the Eurocurrency markets provided a clear indication of Korea's standing among international lenders and the acceptance of the Eximbank as a creditworthy borrower in its own right.

B. Types of Financing

The discussion that follows deals with the major present areas of activity shown on Tables 1, 3 and 4, as well as with the Eximbank's lending terms and conditions shown on Table 2.

1. Export Credits

Normally private export credits consist of financing provided by a supplier/exporter to an importer/buyer, as well as financing provided by a bank in the exporter's country directly to the importer/buyer. 1/ In the former case, the export financing is termed a supplier credit and in the latter case a buyer credit. The supplier arranges his own financing, generally through commercial banks, but as the on-lender of the supplier credit he assumes the customary commercial and political risks of foreign lending against which, however, insurance cover is usually available. Nevertheless, the relatively long terms and large amounts of credit associated with capital goods exports often impose a strain on the supplier's financial resources. As a result, buyer credits have become an increasingly-popular instrument of financing capital goods exports because the supplier is fully reimbursed at the time of delivery of his goods or completion of a project, leaving unimpaired his capacity to borrow for other needs.

The Korean Eximbank has thus far provided most of its export financing directly to Korean suppliers. In order to facilitate the export of capital goods, the Eximbank has also introduced (in late 1978) a program of buyer credit facilities in US dollars under which it intends to establish credit lines with individual foreign banks for re-lending by these banks to importers of Korean goods. These credit lines are to be limited to \$5 million, and exceptionally \$10 million, per country. They will at first be

1/ The terms importer and buyer, and supplier and exporter, will be used interchangeably throughout this report unless otherwise indicated.

restricted to developing countries "in order to ease the financial burden" on their purchases mainly of Korean capital goods such as machinery, plants and ships but also automotive vehicles, fertilizer and textile yarn. The Eximbank envisages giving "favorable consideration" to those countries "contributing to the diversification of Korean export markets and the procurement (by Korea) of natural resources and raw materials." 1/ Terms for the credit lines are expected to be limited to three to five years with exceptions on a case-by-case basis while the interest rate is to be determined by mutual negotiation within the range of 7 to 9 percent per annum. Thus far, "letters of intent" have been signed with banks in Chile, Jamaica and Indonesia and negotiations are in progress with banks in ten other developing countries. The Eximbank has publicly indicated that it will seek to emphasize this "relending" buyer credit program in its financing plans for the future.

a. Types of Goods Financed

More than 85 percent of total commitments extended since 1971 2/ by the Eximbank (and its predecessor) have consisted of export credits to Korean suppliers. In turn, these have been heavily concentrated until recently in the ship export sector (see Table 1). For example, disbursements of Eximbank supplier credits during 1976 financed more than 50 percent of Korean ship exports. 3/

1/ The quotations are from the Exim Bulletin, Vol. 2, No. 3, September 1978.

2/ Fiscal and calendar years are identical.

3/ According to Korean trade statistics, Korea's ship exports grew from \$5.5 million in 1973 to \$529 million in 1977. The Financial Times (May 3, 1978) reported that Korea "built 2 percent of the world's ships in 1977." A later report in the same paper (April 4, 1979) listed Korea's share in 1978 at 3.7 percent, placing it fifth among ship-building countries behind Japan, Poland, Sweden and the U.S.

More recently, however, Eximbank lending has shifted to financing the construction of industrial plants overseas for foreign interests. A small amount of supplier credits (\$1.9 million) was provided for this purpose for the first time in 1977. Data for 1978 indicate that such financing expanded sharply to \$174 million, while ship financing was cut back substantially.

The Korean Government is said to find overseas construction particularly desirable not only because it entails the export of considerable amounts of capital equipment and the receipt of workers' remittances but also because it ensures follow-up orders in future years. Korea's success in this area has been typically rapid, particularly in Middle Eastern countries (such as Saudi Arabia, Iran, Kuwait, Bahrain, United Arab Emirates, Qatar, Jordan and Egypt). The drive began in 1975 when Korean construction companies secured contracts worth over \$840 million, mostly in Saudi Arabia. Contracts valued at \$3.5 billion were signed in 1977 and new construction orders were said to have escalated to more than \$8 billion the following year. 1/ In addition to plants, the Koreans have been active in the construction work of various other sectors in these countries, particularly harbors, ships and highways. Special legislation is reportedly under consideration to provide expanded public support for Korean overseas construction, and Eximbank financing is expected to be heavily focused in this area.

Other exports receiving Eximbank's supplier credit support are rolling stock and "machinery." Under this latter category are included industrial equipment for plants in Afghanistan (textiles), Sudan (tires), Saudi

1/ See The Economist (March 3, 1979).

Arabia (cement), Kenya (metal processing) and the Philippines (automated telephone system). In addition, automotive vehicles manufactured in Korea are eligible for Eximbank supplier credits but textiles as such are specifically excluded.

Table 1: EXIMBANK SUPPLIER CREDITS

(US\$ thousands) 1/

	1978	1977	1976	1971-1978
<u>TOTALS</u>	<u>247,231</u>	<u>218,091</u>	<u>169,029</u>	<u>725,239</u>
Of which:				
Ships	47,409	208,399	161,357	493,186
Rolling stock	-	1,907	5,331	18,595
Industrial Plants	173,661	6,911	-	181,345
Machinery	26,161	874	2,341	32,114

Note: Totals do not always add due to rounding.

1/ Converted at the rate of 484 won to one US dollar (IFS line rf).

Sources: Eximbank Annual Reports 1977, 1978.

b. Credit Terms 1/

Exports can involve pre- as well as post-shipment financing. Pre-shipment generally refers to the manufacturing period, which, in the case of capital goods, can be as long as several years. The Eximbank provides local currency loans during the pre-shipment period to Korean exporters of capital goods at a preferential rate currently 8 percent per annum. The Eximbank

1/ See Table 2.

also provides pre-shipment loans in foreign currencies to Korean importers for up to 80 percent of the value of materials procured abroad which are required in the manufacture of capital goods. These "import credits" are repayable within two years currently at 1 percent above the LIBOR rate for 6 months. 1/

Post-shipment financing, or export credits proper, are provided in foreign currency by the Eximbank at maturities varying from six months to ten years depending on the category of the goods and their value. For instance, heavy capital goods are financed with supplier credits of up to ten years maturity provided the value of the exports is over \$1 million, and up to seven years for values up to \$1 million. In setting specific terms, the Eximbank pragmatically takes into consideration the export performance of the goods being supported by its financing as well as the terms said to be offered by other countries. It may, in exceptional cases, even go up to 20 years.

~~Fixed interest rates have been established in a range of 8 to 9~~ percent on Eximbank supplier credits depending on the maturity of a particular export contract. Since 1977, however, a "temporary" rate of 7 percent has been standard for all supplier credits regardless of category or maturity except for short-term credits of under one year on which a rate of 9 percent is applicable. A commitment fee of one-quarter of one percent is charged on undisbursed amounts. As mentioned earlier, the Eximbank applies interest

1/ As mentioned, the six-month LIBOR rate for Eurodollars is currently fluctuating at about the 11 percent level.

rates within a range of 7 to 9 percent under its new buyer credit relending facility. A commitment fee of one-half of one percent is charged on undisbursed amounts of these buyer credits.

The Eximbank, however, estimates that the "blended" interest rate on the full value of export credit transactions supported by its supplier credits is more than two percentage points higher than the preferential rate charged by the Eximbank. This is because the Eximbank provides a maximum of 70 to 80 percent of the credit so that the exporter must finance the balance at prevailing commercial rates. It should also be kept in mind that downpayments by the buyer prior to delivery of the goods or completion of the contract are required in Eximbank-supported transactions, and these generally are equivalent at least to 15 percent of the contract price, the balance being the amount extended as a credit. ^{1/} Thus, Eximbank financing of 80 percent of a supplier credit will finance 68 percent of the export contract if the downpayment amounts to 15 percent of the contract. Under the buyer credit facility, the foreign bank is restricted to charging a rate no higher than 2 percent above the Eximbank's loan rate to the bank.

Table 2 summarizes the various terms mentioned above.

^{1/} For Korean ship exports, the downpayment is 25 percent of the contract price.

Table 2: EXIMBANK FINANCING TERMS ON SUPPLIER CREDITS

1.	<u>Interest Rates</u>	<u>Percent per Annum</u>	
	a. <u>Pre-Shipment</u>		
	1) Local currency		8.00
	2) Foreign currency for the import component of exports		1.00 above LIBOR <u>1/</u>
	b. <u>Post-Shipment</u> (foreign currency) <u>2/</u>		
	1) 6 months up to 3 years		8.00 <u>3/</u>
	2) 3 years up to 5 years		8.25
	3) 5 years up to 7 years		8.50
	4) 7 years up to 10 years		8.75
	5) Over 10 years		9.00
	6) Current "temporary" rate for all maturities above		7.00
	c. <u>Short-term</u> (foreign currency) (Up to 6 months)		9.00
2.	<u>Maturities</u> <u>4/</u>	<u>Value</u>	
		<u>Over \$1 million</u>	<u>Up to \$1 million</u>
	a. Industrial equipment	Up to 10 years	Up to 7 years
	b. Ships	Up to 8 years	Up to 5 years
	c. Rolling stock	Up to 5 years	Up to 3 years
	d. Automotive vehicles, parts and components	Up to 3 years	Up to 2 years
	e. Unspecified "other"	Up to 5 years	Up to 3 years
3.	<u>Maximum Proportion of Export Credits Financed by Eximbank</u>	<u>Percent</u>	
	a. Industrial equipment including ships		80
	b. Machinery, rolling stock, automotive vehicles, etc.		75
	c. Parts and components		70
	d. Technical services		80
	e. Overseas investment		80
	f. Overseas projects		70

1/ London Inter-Bank Offer Rate for 6 month deposits.
2/ These rates are lower than the "blended" rate for the entire credit in view of the exporter's share which is self-financed at commercial rates.
3/ The established rate for ship exports under all maturities is 8 percent (7 percent temporarily).
4/ Maturities can be extended up to 20 years exceptionally. Repayments normally commence six months after shipment or completion of project.

Source: Eximbank.

The mixture of private export credits extended at market rates of interest and preferential-rate financing provided by the Eximbank appears to be reasonably comparable to similar programs administered by some of the leading trading nations. For instance, it was reported that, on the average, 50 percent of contract values is officially financed in Japan, 60 percent in France and 80 percent each in Germany and the UK. The Eximbank estimates that the blended interest rate on supplier credits supported by it is currently "over 9 percent." The blended rate on comparably-supported export credits as of March, 1979 was estimated at 8.0 percent in Japan, 8.3 percent in the UK, 8.6 percent in France, and 9.9 percent in the US. 1/ In any case, selling price, performance and quality are also important factors and the Koreans are said to be increasingly competitive in this regard.

An interesting example of Korea's competitiveness on credit conditions other than interest rates is in the ship export sector. OECD countries have established guidelines in this sector which stipulate downpayments of no less than 30 percent and maximum maturities of seven years. As noted, the Korean Eximbank's established norms for ship exports entail a minimum downpayment of 25 percent and a maximum repayment period of eight years.

It should also be noted that Korea does not participate in the International Arrangement on Terms for Officially-Supported Export Credits (sometimes called the "Gentlemen's Agreement") to which over 20 countries, mostly from the OECD, adhere. The Arrangement envisages minimum interest rates of 7-1/4 to 7-3/4 percent for maturities of two to five years and 7-1/2

1/ Lending terms and conditions as reported by the US Eximbank.

to 8 percent for maturities over five years; maximum maturities range up to ten years. The longer maturities and lower interest rates are applicable to export credits extended to "poorer" countries.

c. Subsidy Element

Some notion of the subsidy element implicit in the Eximbank's preferential lending to the Korean foreign trading community may be obtained by comparing the level of the Eximbank's interest rates with comparable domestic and foreign rates. For example, it will be recalled that the Eximbank charges an 8 percent interest rate on local currency loans to Korean exporters during the pre-shipment (i.e., manufacturing) period, whereas the non-Eximbank preferential rate for Korean exporters is 9 percent and the non-supported domestic prime rate is 18.5 percent. The Eximbank applies a standard 7 percent fixed rate on all post-shipment supplier credits in foreign currency, compared to the six-month LIBOR rate on Eurodollar credits currently fluctuating at approximately 11 percent per annum (excluding the risk premium, now generally below 1 percent, and other banking charges). Furthermore, the LIBOR rate is adjusted periodically in the light of market conditions while the Eximbank's foreign currency loans are fixed throughout the full term of the applicable maturity, thus permitting the Korean entrepreneur to make a more precise calculation of borrowing costs. 1/

1/ The one exception, as previously noted, are import credits, i.e. Eximbank loans in foreign currency to help finance the imported components of exports.

The Eximbank, in turn, is subsidized by the Government through interest free subscriptions in local currency and preferential access to credit lines in foreign currency at the Bank of Korea. It is this latter source of subsidized foreign exchange which, mixed with the Eximbank's own external financing, enables it to lend foreign currency at competitive rates.

2. Technical Services

This is a relatively new sector of Eximbank financing which is intended primarily to support overseas construction. Loans are extended to Korean firms to help finance technical "know-how," research, design, engineering and supervision related to the installation or operation of industrial plant facilities and the undertaking of public construction works. Eximbank financing amounting to \$15 million was authorized under this category for the first time in 1977. Terms and conditions are similar to those on Eximbank credits to suppliers, as they are for other categories of Eximbank financing, unless otherwise noted.

Table 3: TECHNICAL SERVICES

(US\$ thousands)

	1978	1977	1976	1971-78
<u>TOTALS</u>	<u>7,822</u>	<u>19,868</u>	-	<u>27,690</u>
Of which:				
Construction	-	15,002	-	15,002
"Other" related services	7,822	4,866	-	12,688

Note and Sources as for Table 1.

3. Overseas Investment

The Eximbank also provides preferential financing to Korean entrepreneurs up to 80 percent of the book value of an investment project to facilitate the development of natural resources and the import of these and other products regarded as important for the Korean economy. The credits are made available in a variety of arrangements including financing the subscription of capital in foreign firms and the acquisition of stock therein by Korean nationals, the provision of funds enabling non-Koreans to subscribe to capital in overseas firms operated "substantially" by Koreans, and the granting of loans for overseas projects of foreign firms in which Koreans have an interest. Included in this category is lending to foreign governments and private entities abroad to facilitate the "leasing" of Korean equipment, such as ships. Associated with the Eximbank investment credit programs are additional financial services not yet implemented which are tailored to specific needs, such as the "overseas project credit" to Korean firms which import from Korea most of the equipment required in the installation, expansion and operation of their overseas plants, and the "major resources development credit" for Korean firms engaged in the exploitation of and export to Korea of designated "major resources."

The bulk of the Eximbank's credits for overseas investment has thus far been committed to facilitate the chartering of Korean ships to foreign entities. This is another area of rapid growth, commitments for which virtually tripled during 1977 and 1978 as compared with 1976.

Table 4: OVERSEAS INVESTMENT

(US\$ thousands)

	1978	1977	1976	1971-1978
<u>TOTALS</u>	<u>36,969</u>	<u>39,219</u>	<u>18,037</u>	<u>96,647</u>
Of which:				
Forestry	-	979	-	3,335
Deep-sea fishing	-	4,000	-	4,066
Ship chartering	31,184	34,240	12,384	77,808
"Other"	5,785	-	5,653	11,438

Note and Sources as for Table 1.

4. Miscellaneous

In addition to the above major programs, the Eximbank is authorized to provide discount facilities and to guarantee the buyer credits of private Korean banks engaged in export and import financing. Performance bonds which guarantee the fulfillment of a contract (usually for overseas construction) may also be issued by the Eximbank. Very few of these services are said to have been provided by the Eximbank to date.

The above list does not exhaust all the authorized programs envisaged for the Eximbank, some of which have not yet been utilized by the Eximbank. The Eximbank's by-laws contain an "elastic clause" empowering it to "perform any other business" related to its specifically-enumerated programs. Among these is a so-called "Economic Cooperation Credit" to be made available when an agreement to this effect exists between the Korean and foreign governments (envisaged as those of other developing countries) on terms determined in the

agreement. In addition, the Eximbank is authorized to refinance credits to foreign governments and foreign banks which are experiencing difficulties in meeting their payment obligations for imports purchased on credit from Korea. The Eximbank may also waive or reduce interest on its credits to Korean firms which are affected by such payment difficulties.

C. Volume

As will be seen on Table 5, the Eximbank's aggregate authorizations have been expanding rapidly, amounting to over \$290 million in 1978. Total authorizations from 1971 through 1978 were \$850 million, of which \$570 million had been authorized since the end of 1976, an indication of the stepped-up pace of official export financing since the formation of the Eximbank in mid-1976. The disbursement rate of 75 percent of authorizations through 1978, of which almost three-quarters was realized in the last two years, is another reflection of effective Eximbank performance.

Nevertheless, as mentioned earlier, Eximbank financing still represents only a small fraction of Korean exports of manufactured goods. For example, official financial support extended by the Eximbank 1/ during 1978 amounted to only 1.9 percent of total exports of manufactured goods in that year. It should be kept in mind, however, that the Eximbank supports exports considerably larger in the aggregate than its own financing in view of the

1/ As reflected in total disbursements by the Eximbank less credits for investment and technical services. The comparison with the Japanese Eximbank in the Summary and Conclusions section of this paper referred to authorizations because recent disbursement data are not available for the Japanese Eximbank.

required downpayment and the exporter's own share of the financing. 1/ Moreover, a large proportion of Korean manufactured exports is sold on a cash or short-term basis whereas the Eximbank provides credit as a rule for manufactures sold on longer terms. Thus, the Eximbank's role, while it may be expected to expand in proportion to manufactured exports, will probably remain more that of a financial catalyst in targeted capital goods areas, such as ship-building and overseas construction. The Eximbank, in fact, plans to expand its lending very sharply during the present year to a level in excess of \$500 million, of which more than 80 percent is envisaged as financing for ships and overseas plant construction. There have been recent indications that the Korean Government may be intending to lessen its emphasis on capital goods exports. Eximbank officials, however, claim that the agency's programs will continue to expand as planned.

Table 5: TOTAL AUTHORIZATIONS AND DISBURSEMENT

(US\$ thousands)

	1978	1977	1976	1971-1978
1. Total credit authorizations	292,023	277,178	187,066	894,577
2. Total disbursements	262,746	198,409	110,285	638,626
3. Disbursements as percent of authorizations	90.0	71.6	59.0	75.2

Note and Sources as for Table 1.

1/ In 1976, Eximbank financing represented about half of the value of the total exports supported under its programs.

D. Destination

Eximbank financing is being focused increasingly on developing country markets. Table 6 indicates that credit authorizations to Africa and Asia during the past two years advanced very sharply, accounting for almost three quarters of all credit authorizations.

In contrast, European and Western Hemisphere shares, which had dominated the regional distribution in earlier years, declined sharply in both 1977 and 1978. 1/ This marked shift in destination is consonant with Korea's export strategy of reducing its reliance on developed markets, particularly in the US and Japan, where it is more vulnerable to import protectionism.

Table 6: CREDIT AUTHORIZATIONS BY DESTINATION
(US\$ thousands)

	1978	1977	1976	1971-1978
Europe	38,362	93,382	142,058	346,924
Africa	113,545	122,276	6,419	242,407
North and South America	8,362	17,523	31,684	62,680
Asia	131,754	40,917	6,905	185,229
Oceania	-	979	-	12,337
<u>TOTALS</u>	<u>292,023</u>	<u>277,178</u>	<u>187,066</u>	<u>849,577</u>

Note and Sources as for Table 1.

1/ North and South America are combined, so that the Latin American share is unknown.

E. Credit Risk Assessment

In evaluating debt servicing capacity, the Eximbank places primary emphasis upon a country's political, social and economic 1/ circumstances, and accords secondary weight to specific aspects of creditworthiness (such as the debt service ratio). Based on such an evaluation, the Eximbank establishes limits on the volume of its aggregate lending to a specific country. The Eximbank also employs fact-finding teams for on-the-spot surveys of overseas markets. During the past two years, Eximbank missions visited countries in Southeast Asia, Latin America and Africa.

F. Promotional Efforts

The Eximbank conducts quarterly meetings with leading representatives of the private sector to exchange information on competitive conditions in export markets, on overseas projects undertaken by participants, and on ways and means of improving the Eximbank's financial services to the Korean exporting community. Attending these meetings are officials of Korea's large general trading companies, heavy capital goods and chemicals industries and the heads of four private associations: the Korea Trade Promotion Corporation, the Korean Traders Association, the Federation of Korean Industries, and the Korean Chamber of Commerce and Industry. In addition, in-depth meetings are held each week with representatives of one different major exporter with respect to the firm's export credits, overseas investments and related problems.

1/ Such as the rate of inflation, the growth rate, the balance of payments, and the country's overall growth potential.

In addition to the provision of preferential export financing through the official institution of the Eximbank, the Korean Government also promotes joint ventures between Korean and foreign banks in overseas markets as well as in Seoul to provide a ready source of funds for Korean exporters. Such joint banking ventures have already been set up between Korean banks and foreign banks in Brussels, Cairo and Panama. In Seoul, Korean banks have become associated with Barclays and Lazard Brothers of London, and Saudi Arabian and Kuwaiti banking interests.

II. Export Credit Insurance Programs

Korea's export credit insurance business was formally transferred to the Eximbank on January 1, 1977, a half-year following the latter's establishment. Under the overall supervision of the Ministry of Commerce and Industry, the Eximbank is entrusted with considerable authority in policy and operational matters in this area. For instance, the Chairman of the Eximbank heads the Export Credit Insurance Council 1/ which determines Eximbank policy as defined in enabling legislation and Presidential decrees. The Eximbank also administers the Export Credit Insurance Fund which provides the reserves for potential claims payments.

1/ The Council consists of a maximum of 12 members including the Chairman of the Eximbank, representatives of the Economic Planning Board; the Ministries of Foreign Affairs, Finance, Commerce and Industry, and Construction; the Bank of Korea, the Korea Trade Promotion Corporation and unspecified individuals with "experience in export credit insurance."

A. Fund Resources

Financed directly by the Korean Government, the Export Credit Insurance Fund amounted to 4 billion won (\$8.3 million) at the end of 1977, more than twice the amount at the end of the previous year, and was augmented to 7 billion won (\$14.5 million) by mid-1978. A further increase to 10.1 billion won (\$21.0 million) is envisaged during the current year. The statutory maximum liability for outstanding insurance contracts was raised from 20 times the official capital in the Fund to 30 times at the end of 1978. With this latest increase, the Fund's reserves constituted 9.7 percent of its contingent liabilities, or almost twice the required level.

B. Insurance Programs

The Eximbank is authorized, acting as agent for the Korean Government, to provide cover against potential losses for various forms of export finance and investment capital, paralleling to a large extent the lending programs operated directly by the Eximbank. Both political risks (defined as those resulting from military or civil disturbances, or specific actions by the government of the importer which tend to prevent or delay the importation of the goods under contract or the transfer of funds to Korean exporters) and commercial risks (for the most part, the buyer's insolvency or default), are insured by the Eximbank. Cover is normally provided up to 90 percent of the value of the export credits (i.e., contract value less downpayments of at least 15 percent) 1/ against potential losses attributable to both political

1/ The required minimum downpayment on ship exports is 25 percent. When the downpayment is 15 percent, maximum cover is thus 76.5 percent of an export contract.

and commercial risks except as noted. (In most other national systems, the proportion covered for political risks is generally higher than for commercial risks.) The Eximbank may specify an actual percentage of cover below the permissible maximum depending on the creditworthiness of the importing country and the buyer. Waiting periods vary under the different categories of insurance before claims are payable and reasonable efforts must be made by the insured claimant to recover the amount at issue which is then reimbursable to the Eximbank. The Eximbank, like other export credit insurance agencies, also lays down lending guidelines for the credits which it insures and which are comparable to the maturities and interest rates applicable under its financing programs. A description of the different categories of insurance follows.

1. General Export

This insurance provides cover to Korean exporters during the pre-shipment (i.e., the manufacturing) period primarily against the risk of losses which would be incurred in the event of a buyer's revocation of an export contract through no fault of the exporter, or the exporter's revocation of a contract due to "reasonable cause." The coverage extends through the period of manufacture but does not include local costs if any (i.e., incurred in the importing country) and interest charges. Generally, capital goods such as industrial plants, ships and rolling stock are eligible for pre-shipment cover. The waiting period for claims payment is three months. As an exception to the general rule, cover against commercial risks is limited to a maximum of 60 percent to ensure "prudent" assessment by the exporter of a buyer's creditworthiness (cover against political risks carries the customary maximum of 90 percent).

2. Export Finance

Under this category, all Korean banks (including the Eximbank) 1/ are covered against political losses sustained on their pre-shipment loans to Korean exporters in the event of the exporters' inability to repay due to non-fulfillment of their contracts or non-receipt of payment from the buyers. Interest payments on pre-shipment loans are not covered. The waiting period before claims are eligible for payment is two months.

3. Export Bills

This insurance covers short-term "export bills" with maturities not exceeding 180 days extended by Korean banks to Korean suppliers to finance "all types of goods" including agricultural and consumer goods but excluding quickly perishable items (such as fish). Interest charges are covered provided these are included in the amount of the export bills. The waiting period is two months.

4. Medium- and Long-Term Credit

~~This is the basic post-shipment insurance for all supplier credits~~ of more than 180 days, including those for ships and overseas plants. Maturities may range up to 10 years on large capital goods contracts with the possibility of extensions up to 20 years. Interest charges and local costs may be covered when they are included in the contract value. Suppliers may transfer their insurance rights to banks which provide the financing for the supplier credits. Waiting periods are usually four months but, in the event of

1/ The Eximbank is eligible for insurance cover on all forms of export financing for which other banks are eligible.

a buyer's default, the waiting period may be prolonged to six months. Overseas Construction Insurance, a separate category issued for the first time in 1978, protects the Korean supplier in the event of a foreign buyer's revocation of a construction contract due to no fault on the part of the Korean supplier. The conditions for coverage are similar to those for other medium- and long-term credits.

5. Overseas Investment

The Eximbank is authorized to cover Korean investments abroad against potential losses up to 90 percent of either the book or actual value, whichever is less. The risks, as is customary in this form of insurance, are limited to political causes (i.e., expropriation, inconvertibility and war). An investment is covered fully for 15 years. The waiting period for claims payment is generally four months. Profit remittances are also insured up to the actual amount of the principal investment. The types of investment covered are similar to those envisaged in the Eximbank's direct financing of overseas investment, but thus far, as in other categories, the volume of insurance issued has lagged considerably behind the financing programs.

The Eximbank is also a member of the Berne Union's Investment Insurance Committee which was organized in 1974. Not all members of the Union's parent Export Credit Insurance Committee belong to the new grouping, some obviously because they do not provide investment coverage and others because different agencies are authorized to handle this business. Since the Eximbank provides both forms of insurance, it sits on both Committees. The only other developing country participating in the Investment Insurance Committee is Israel.

6. Consignment Sale

Up to 90 percent of the "sales price" is covered against political losses on goods consigned for sale in overseas markets. Coverage is limited to political risks. The "sales price" is calculated at 5 percent above costs incurred in the consignment-sale transaction, less the value of any goods sold. The 5 percent is an allowance for a profit margin. Most types of exportable goods are eligible for cover as under export bill insurance. Only a negligible amount of insurance was issued for this purpose for the first time in 1978.

C. Performance

Since the assumption by the Eximbank of the Government's insurance programs for export credits and investment at the beginning of 1977, the growth in medium- and long-term cover has been particularly rapid. Whereas insurance for short-term credits in 1976 exceeded 90 percent of all business covered in that year by the Eximbank's predecessor, by 1978 the share of short-term insurance policies had shrunk to slightly over 25 percent as may be seen on Table 7. Such a development is contrary to the general experience of other national export credit insurance systems where the bulk of the cover issued is short-term. The Korean Eximbank, however, has stated that it intends to focus its as-yet relatively limited insurance resources on capital goods exports in a role complementary to its financing programs. Another reason cited by the Eximbank for the decline in short-term insurance is that Korean exporters are no longer required to obtain such insurance when seeking short-term export financing.

Table 7: COMMITMENTS OF EXPORT CREDIT INSURANCE 1/

(US\$ thousands)

	1978	1977	1976	1975
<u>TOTALS</u>	<u>136,439</u>	<u>103,686</u>	<u>97,322</u>	<u>33,624</u>
Of which:				
General export	1,483	31,740	2,223	-
Export finance	3,012	4,488	1,767	-
Export bill (short-term up to 6 months)	40,384	58,760	84,502	33,208
Medium- and long-term	65,692	6,274	4,293	416
Overseas Investment	5,029	2,424	4,537	-
Overseas Construction	20,839	-	-	-

/1 In terms of value of export credits insured.

Sources: Eximbank annual reports 1977, 1978 and Eximbank documentation.

During 1977, its first year of managing the Government's insurance program, the Eximbank deliberately adopted a conservative attitude toward the selection of insurance risks. As a result, total insurance commitments (i.e., volume of insurance issued) amounted to \$103.7 million during 1977 as compared with \$97.3 million during the previous year, reflecting only a 6.5 percent growth.

For Korea, this represented an unusually-modest increase, particularly when compared with insurance commitments extended by the Eximbank's predecessor, the Korean Reinsurance Corporation, which had virtually tripled during 1976 over the previous year's volume. The Eximbank attributed this greatly-slackened performance of its insurance business to a deliberate policy

of more cautious underwriting as a result of a rise in claims paid from \$326,000 in 1976, or considerably less than half of the premium income in 1976, to over \$1 million, or slightly above premium income in 1977. As a matter of fact, claims paid had also exceeded premium income in 1975. The Eximbank ascribed the incidence of heavy claims in 1975 and 1977 primarily to insolvency and protracted default on export bills insurance for shipments to private buyers.

Results for 1978 indicate that insurance commitments resumed rapid growth, advancing by about a third over 1977, with the marked shift towards the issuance of longer-term insurance already noted. Claims paid, however, continued at virtually the same high level as during 1977, but premium income rose so that the Eximbank realized a higher net surplus for the year. 1/

Total contingent liabilities (i.e., the value of all outstanding insurance policies) more than doubled by the end of September 1978 to \$149 million (largely as a result of increased longer-term cover) in comparison with the end of 1977.

Table 8: EXPORT CREDIT INSURANCE CONTINGENT LIABILITIES (YEAR-END) 1/

(US\$ thousands)

<u>1978</u> (end Sept.)	<u>1977</u>	<u>1976</u>
148,671	66,164	40,559

1/ Amounts outstanding under all policies.

Sources: As for Table 7.

1/ As a result of reserves from other years, recoveries of past claims and income from investments, the Insurance Fund at the end of 1978 reported reserves of \$240 million.

Despite a sharp decline in new insurance commitments for the first quarter of 1979 (at an annual rate of \$53 million), the Eximbank anticipates that new insurance commitments will rise steeply to a level in excess of \$300 million for the year as a whole, or more than twice that of 1978 due largely to the introduction of various innovations discussed in the following section.

D. Types of Policies

Apart from the different insurance categories already noted, the Korean Government, acting through the Eximbank, permits the choice of coverage for either political or commercial risks, or both in combination where both are specified as available. A higher premium charge is applicable when cover against both classes of risks are chosen. All Eximbank policies are equally available when the buyers are private or public entities in the importing country, but some distinction is occasionally made between the two categories in the percentage of risks covered.

Specific (i.e., individual) policies are offered for all categories of insurance, but a "whole turnover" policy is mandatory for certain forms of shorter-term export insurance under which recurring exports may be insured up to stipulated amounts without being covered through individual policies. These whole turnover policies had been limited to export credits with maturities from six months to three years but were recently made available for longer-term maturities as well. Whole turnover insurance serves to improve the risk factor (due to the spread of risks in a number of transactions rather than being concentrated in one), generally lowers insurance costs and is considerably more convenient for the exporter.

Cover on bonds issued by commercial banks was another major innovation added at the end of 1978 to the array of available insurance programs.

Bonds have become important in recent years with the sharp growth of exports to oil producing countries. Buyers in these countries are often willing to pay cash for contracts on large projects but require payment guarantees in the form of performance bonds to ensure compliance with the terms of a contract. There are various types of bonds related to the guarantee of an exporter's performance, such as general performance, advance payment and bid bonds, 1/ all three of which are to be eligible in the Korean program. This form of insurance support is important in overseas construction where Korean financial involvement, as has been noted, has been especially marked, and is comparable to similar insurance provided under other national systems of the industrialized countries. 2/ It provides another example of the flexibility of the Korean export promotion system in adapting available services to the specific and changing requirements of the Korean export industry, in this case, the expanding overseas construction sector.

Important services available in some national systems of export credit insurance which Korea has not provided are insurance against the cost increases incurred during the period of manufacture, and protection against exchange rate changes moving against the exporter. Furthermore, cover has not yet been made available for commercial banks' buyer credits although the Eximbank, as noted, is now authorized to do so under its financing programs.

1/ A bid bond is one guaranteeing an exporter's acceptance of a contract that is awarded to him, while an advance payment bond is one guaranteeing repayment of advances made on a contract.

2/ The Eximbank is also authorized, as previously noted, to issue performance bonds under its financing services.

On the whole, however, Korea's export credit and investment insurance services are reasonably comparable in most respects to similar programs offered by other national services.

E. Geographic Coverage

The regional distribution of new insurance commitments, increasingly concentrated in developing country markets, indicates that the largest share went to Africa in 1978 which accounted for over half of the total. This was followed by the Asian area, primarily Japan, the Philippines, Malaysia, Indonesia, Hong Kong and Taiwan. North America and Europe, on the other hand, continued their sharp declines, a trend consistent with Korea's intention to diminish its dependence on exports to developed countries. The shares for Latin America have been relatively negligible, a result which is also consistent with the geographic pattern of Eximbank financing and Korea's overall trading relations.

Table 9: GEOGRAPHIC DISTRIBUTION OF
EXPORT CREDIT INSURANCE

(US\$ thousands)

	1978		1977	
	Amount	Percent	Amount	Percent
Asia	29,393	21.5	47,793	42.2
Europe	8,971	6.6	17,174	16.6
North America	14,676	10.8	25,579	26.6
Latin America	3,934	2.9	3,727	3.6
Africa	78,017	57.2	5,919	5.7
Oceania	<u>1,450</u>	<u>1.0</u>	<u>5,494</u>	<u>5.3</u>
<u>TOTALS</u>	<u>136,441</u> <u>1/</u>	<u>100.0</u>	<u>103,686</u>	<u>100.0</u>

1/ Slight difference from Table 7 due to rounding.

Source: Eximbank annual report for 1978.

F. Premiums

The Eximbank takes into consideration the type of policy and the maturity of the underlying credit when setting premium rates. As a general rule, rates are higher on longer maturities but are said not to be affected by consideration of credit risks. 1/ If payment of the insured credit is guaranteed by an acceptable external entity, appropriate reductions may be granted. No differentiation is made between private and public buyers (i.e., governments or their agencies) as is done in some systems where export credits issued to the latter are insurable at lower rates.

1/ This can be done in other ways, such as reducing the insurance cover on potential losses, prolonging a waiting period, or varying the credit ceiling to a specific country, including discontinuing insurance cover to it entirely.

The average rate on short-term credit policies as of the end of October, 1978, was 0.97 percent expressed as a one-time charge on the insured amount. This rate compares favorably with average rates of other national systems. Premium charges, of course, add to the overall cost of export credits, being generally passed on to the buyer.

G. Cooperation with Other National Insurers

On July 1, 1978, the Eximbank signed a Joint Insurance Agreement with the Belgian national export credit insurance agency (OND). The Agreement is intended to facilitate collaboration between the exporters of both countries in the joint financing of capital goods and services on the same projects. Each agency would be prepared to underwrite that share of the risks involving its own exporters. This move is analogous to the Eximbank's publicly-expressed interest in co-financing ventures with foreign banks on large projects in an attempt to spread the risks and reduce the financial burdens involved.

Attachment: Korean Support for Exports

Sources: Except as noted, the Korean Eximbank (published and unpublished documentation and consultation with Korean Eximbank officials).

KOREAN SUPPORT FOR EXPORTS

A broad range of export incentives through tax and credit preferences has existed in Korea since the 1950's. The main support for export financing had been channeled through working capital loans during the pre-shipment period provided at preferential interest rates largely through the rediscounting facilities of the Bank of Korea. For example, domestic credits for export purposes outstanding at the end of 1975 were estimated to have exceeded one-third of all Korean commercial bank credits outstanding at that date, and the average interest rate on these credits was estimated at less than one-half that on non-supported commercial bank loans.

For detailed discussions of Korea's export promotion policies, see:

1. Industrial Policy and Development in Korea by Westphal and Kim, World Bank Staff Working Paper No. 263, August 1977.
2. The Republic of Korea's Experience with Export-Led Industrial Development, by Westphal, World Bank Reprint Series No. 54.
3. Export Incentives and Export Performance in Developing Countries: A Comparative Analysis, by Balassa, World Bank Reprint Series No. 59.
4. Korea Export Incentives: The Direction of Policy Reform, by Yung W. Rhee (Economics of Industry Division), dated February 6, 1977.
5. A Rationale for Export Credit in Korea, by Ezekiel (IFC), dated March 17, 1977.