

THE ROLE OF THE EXPORT-IMPORT BANK IN
DEVELOPING THE EXPORT POTENTIAL OF AIRCRAFT SALES

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Abstract

A description of the current patterns, terms, and conditions of Eximbank commercial jet aircraft export financing will be given. As time permits, some discussion of the factors affecting export financing will be noted.

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Let me make a few basic observations. Number one, Eximbank is a US Government agency. Number two, its principle objective is to facilitate US exports; you can forget about the "Import" in our name. Number three, we are to supplement and not compete with private sources of financing. Number four, any loan that we make must have a reasonable assurance of repayment; in other words, we are supposed to act as a banker and not as an AID-type agency. To give you an idea of Eximbank's authorized size, we can have total outstanding loans, guarantees and insurance of up to \$20 billion. We have \$1 billion of outstanding capital stock held by the US Treasury Department and \$1.3 billion of reserves. We could borrow from the Treasury Department at any given time up to \$6 billion. As of June 30, 1971 we have total assets of \$5.8 billion. Subtract \$2.3 billion net worth from that and our liabilities were about \$3 $\frac{1}{2}$ billion. In fiscal year 1971 we earned close to \$120 million and paid a dividend to the Treasury Department of \$50 million. The balance of our earnings go into our reserve account.

Question: What kind of a return on investment is that?

Answer: The net income is about a 5% return on net worth.

Let me give you an idea of the amount of financing we have been doing for commercial aircraft. In 1957, we financed four aircraft worth about \$30 million and loaned 16 $\frac{1}{2}$ million dollars to do that.

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Over this period we have been involved in more and more transactions and the dollar volume has been going up. However, the amount of money we actually put up per transaction, on a percentage basis, has gone down. In other words we are utilizing more and more private financing in specific transactions.

On a \$10 million transaction, a typical financing pattern would call for a cash payment from the buyer of 10-20%. The buyer raises the cash payment from non-US sources. The other 80-90% of contract price is the financed portion. Eximbank puts up one-half and the other one-half comes from private sources, either in the U.S. or from foreign sources. The repayment term on the financing would be 10 years for a new commercial jet aircraft or anywhere from 5-7 years for used commercial jet aircraft. The amount of cash payment varies somewhat depending on who the buyer is. If you're talking about the major European airlines, cash payment will be 20% or greater. If you're talking about a weaker buyer in Africa, Asia or Latin America, it would probably be closer to the 10% figure.

Question: You require a higher down payment from the Europeans—what's the theory behind that. Usually the better the credit is, the lower the down payment? They are the biggest customers of the US. It seems to me that we should try to figure out some way to encourage greater sales.

Answer: Eximbank has to balance various objectives of the US Government, including the encouragement of greater sales through lower cash payments versus balance of payment improvement through higher cash payments.

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We don't require supplier participation any more as a general rule. Supplier participation being Boeing, McDonnell-Douglas, or Lockheed extending credit to the buyer. We used to, and will continue to in a certain number of transactions involving higher risk buyers. Our present interest rate is 6% per annum. We charge a commitment fee on our loans of 1/2 of 1% per annum. If we guarantee the private financing, as we do in many cases, we charge 1/2 of 1% guarantee fee. On loans to strong European buyers, we try to get as much of the private portion from off-shore as we can. In many cases the buyers are able to raise financing equal to 20-25% of total contract price from offshore sources.

Question: When you say 6% interest charge--is that your current rate?

Answer: That's our current rate.

Question: Can you tie that somehow to your own cost of funds?

Answer: Since 1945, Eximbank's lending rate has been consistently higher than its borrowing rate at the U. S. Treasury and has never been lower than the average rate on the total public debt. On a cumulative average, Eximbank's operations have never entailed a subsidy cost.

Question: Wouldn't it be difficult for Pan Am and TWA to compete with foreign airlines against this kind of loan?

Answer: What you've got to take into account is the fact this difference between 6% and whatever Pan Am has to pay for their borrowing is only one element of total cost. There are other national interest reasons

why you would want to keep this rate at 6% and try to sell aircraft abroad. One basic reason is if we don't sell these aircraft abroad, our balance of payments and balance of trade are going to deteriorate and weaken the dollar in the world money markets. This could hurt Pan Am and TWA more than any 6% interest rate we charge the foreign airlines. In addition, this 6% only relates to possibly 40% of the transaction. The foreign buyer still has to pay a market rate on the other half of the financing. Also what you are talking about is 10 year Exim financing in contrast to Pan Am and TWA borrowing at 15-20 years.

Question: That could still be a huge difference though. If you're lending money at 6% to KLM and Pan Am has to pay 10% or 11% and the airlines have a huge part of their capital structure on debt, that's going to be a significant factor.

Answer: We have no reason to believe that Pan Am or any other major U. S. carrier is paying interest rates approaching 10% or 11% for their equipment purchases.

We have other programs to help finance U. S. exports, including guaranteeing aircraft leases. Many small aircraft are financed through our FCIA insurance and commercial bank guarantee programs described in our brochure. We have a cooperative financing facility and a discount loan facility through which many of the small to medium size transactions

are handled on terms up to say five years. Follow-on spares and other airline equipment are financed through these programs. We also finance U. S. goods and services which go into the airport construction and facilities.

Over the ten years I have been working at the Bank, the programs, methods of financing and outlook of the bank have changed, and I believe that is going to be the case in the future. Thus, if you're interested in how Exim is going to change in the next 10 years in financing U. S. exports, you have to keep in mind such factors as balance of trade and balance of payments. When you see them getting bad, greater efforts will have to be made to encourage and increase U. S. exports. If we don't we are going to have to cut back on other things that we are doing abroad or limit imports. International political and economic developments will also affect U. S. export financing. Eximbank's life is extended every five years. Thus, Congressional support in the following years is essential.

Money market conditions, availability of funds, and interest rates are going to affect what Exim does. Some critics say Exim should not finance jet aircraft exports today because ample funds are available at this time from the U. S. commercial banking sector. They fail to consider that U. S. commercial banks have a liquidity situation, resulting in limited funds from this source on repayment terms exceeding 5-6 years. Today it is very difficult to find commercial financing for new jet commercial aircraft on anything like 7 or 10-year terms. On the other hand, the overseas buyer, as well as Boeing, McDonnell Douglas and Lockheed would like to see Eximbank start supporting terms up to 12 years.

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Another factor is that Eximbank is a US Government agency subject to annual review of its operations by the Administration and Congress. Eximbank does not operate on annual appropriations, however, and pays all its expenses out of earnings.

Question: What kind of debt security do you take versus commercial banks?

Answer: In typical transactions, we get notes from the buyer. The commercial bank does exactly the same thing. The notes are usually guaranteed by financial institutions or governments. Mortgages are not required in most instances.

Question: Who has first rights to proceeds from foreclosure when mortgages are taken?

Answer: If the mortgages were required to secure all lenders on a pro-rata bases, then the proceeds would be distributed accordingly.

I should also mention that in a 10 year transaction, Exim is prepared to take the last 5 years maturities and allow a commercial bank to take the earlier maturities. In this way, we are able to meet the commercial bank's requirement for liquidity.

Question: Are these figures typical of all transactions or do you differentiate between aerospace and other products?

Answer: When we're talking in terms of large projects and products, the typical transaction would be a 10% cash payment and 90% financing

of which Eximbank's share would be one-half. As an exception, we have been able to get 20% cash payments from major European carriers for jet aircraft sales because of the competitive advantage of the US aircraft industry in recent years. In other transactions, the typical cash payment is 10%.

Question: Do you know what the Europeans are offering in Latin America?

Answer: Basically, it's 10% cash, 10 year repayment term with a subsidized interest rate. The BAC 111, Caravelle, and A-300B are all offered on those terms.

Question: Are the interest rates comparable?

Answer: The British interest rate is about 6 $\frac{1}{2}$ -7% to the borrower on the total financing. They will change theirs as time goes along. Eximbank charges 6% on one-half the financing, while the commercial banks usually charge the prime rate plus a mark-up on a fluctuating bases. At this time, the rates are probably reasonably competitive.

Question: You said you had a 6% interest rate, plus a $\frac{1}{2}$ % guarantee fee and another fee. Could you explain?

Answer: Eximbank charges a $\frac{1}{2}$ of 1% per annum commitment fee on the amount of Eximbank's loan from 30 days after authorization until the loan funds are drawn down. The borrower pays a 6% interest rate on amounts which are drawn down. If Eximbank guarantees the private

financing, the Eximbank guarantee fee of $\frac{1}{2}$ of 1% per annum is charged on the private financing from dates of draw down until repayments are made.

Question: Could you comment on Russian YAK-40 financing rates being so low?

Answer: It really doesn't make any difference because the Russians can change the price of their product and the interest rate in any manner they want. Profit isn't their main consideration.

Question: Have European manufacturers offered concessionary terms?

Answer: In some instances in the past, British and French manufacturers have gotten soft loan assistance for their buyers. US AID funds have not been used to finance commercial jet aircraft sales.

I think the extent of non-US content in US commercial jet aircraft will require more and more attention. It's becoming more and more difficult to sell aircraft abroad without some non-US content. Also, the prospects of a major new commercial jet aircraft being manufactured with 100% US companies involved may be very difficult. Other factors requiring consideration are (1) the importance of the non-US market to any new aircraft project, (2) exporting US technology, (3) foreign competition and (4) development of foreign aerospace industries.

Question: When you have multi-national interest and foreign equipment, is the bank precluded from loans on the portion that's foreign?

Answer: As a basic policy, Eximbank finances goods and services of U. S. manufacture and source only. If the amount of foreign content is sizeable, it would be deducted from the contract price and all percentages applied to the net U. S. content.

Question: What effect will the proposed Civil Aviation Financing Plan have? Can that help finance aircraft for foreign airlines?

Answer: Dr. James could answer that question better than I, though it is my understanding that the intent of the legislation is to provide capital to make possible the manufacture of new aircraft and not to provide financing for the ultimate purchaser.

Question: Wouldn't a reduction in cash payments increase sales?

Answer: Possibly, but the question is whether a reduction in the cash payment would increase U. S. exports sufficiently to make an appreciable difference and will increased sales be offset by the reduction in balance of payments from reduced cash payments.

Question: How is the policy of the bank established?

Answer: Basic policy is established by Congress and is set forth in our legislation. To carry out that policy, we have a five-man board of directors appointed by the President with advice and consent of the Senate.

Question: Are you prepared to say that you look upon your activities as a benefit as opposed to whether you exist or whether you didn't exist. In other words, you stimulate sales by existing and if you didn't exist you wouldn't.

Answer: I believe the answer is affirmative. There are many cases where US manufacturers, US commercial bankers, and other financial institutions cannot afford to take the risk that's involved in foreign sales. The only source available in the US to take that risk is the US Government. It is a legitimate objective of the US Government to take such political and economic risks. All of the other countries around the world do the same thing. We're in a buyer's market today.

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