

NWA mtry
 OFFICE OF THE VICE PRESIDENT

WASHINGTON

~~SECRET/SENSITIVE~~

Memo No. 631-79

July 26, 1979

MEMORANDUM FOR THE VICE PRESIDENT

FROM:

Denis Clift *DC*

SUBJECT:

Foreign Policy Breakfast,
Friday, July 27, 1979

*P.R.C. re
my visit
- Johnston?*

The Shah

During your SALT speaking tour you sent Zbig a message recommending that we review our policy toward the Shah. Vance may raise this at the breakfast. David Newsom has suggested that if the Shah will agree to (1) renounce all political activity and (2) renounce any claim to the throne, we may be able to admit him. The first of these two points makes sense; the second, to me, is a non-starter. I think the key questions that have to be weighed are:

- the likely severe damage to US-Iran relations. I have seen nothing to indicate that we could expect anything but violent condemnation, possible violence to our embassy and Americans in Iran, likely stoppage of oil exports to the U.S. from Iran were we to announce now that we plan to admit the Shah. Despite the domestic heat we are taking on this, I think these concerns require very careful review. (S/S)

MFN for USSR

Secretary Kreps has recommended to the President that he proceed with MFN for the USSR. It is my understanding that in Vienna the President told Brezhnev that he was disposed to proceed with MFN, but that he did not wish to jeopardize SALT's chances in the Senate. Since then, Warren Christopher has been taking soundings on Capitol Hill (Tab A). Those soundings indicate that we should not proceed with MFN until SALT has made its way through the Senate. I strongly support this position.

~~SECRET/SENSITIVE~~

Classified by Multiple Sources

Review 7/25/99

Page 1 of 3

SANITIZED

NLJC-06-077

per 6/7/06 NSC ltr

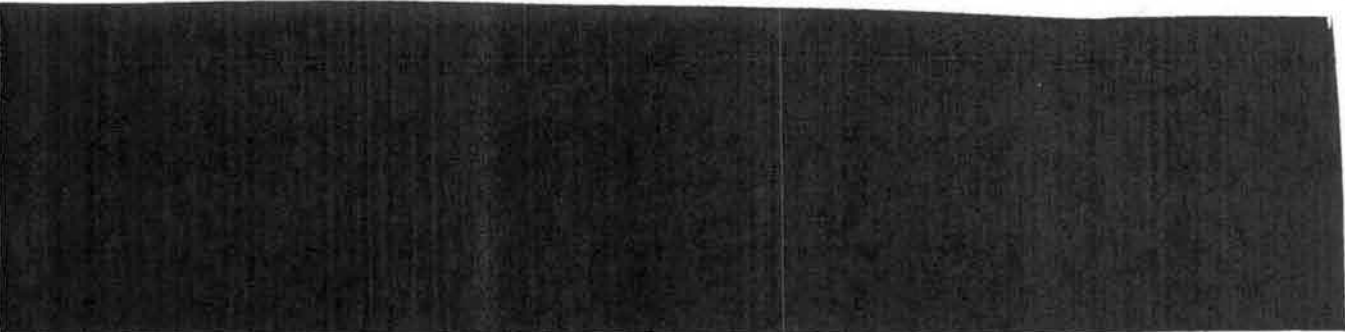
BY S. MCGOWAN 6/29/06

~~SECRET/SENSITIVE~~

I would note that Senator Jackson, whose image has become somewhat dulled and faded in the SALT debate, might well find the fresh strong issue he is seeking should we push MFN now without explicit assurances on emigration from the USSR. (S)

Middle East

The question of whether or not to consider a move toward the PLO is one which you addressed in your conversation with Bob Strauss prior to Wednesday's PRC meeting. Secretary Vance may well review some of the options at the breakfast. I think it is not only a mistake in terms of our Middle East policy, but also in terms of the SALT effort to push ahead with any initiative that might outrage pro-Israeli members of the Senate. I am reminded of the Panama Canal debate in the Senate when you took the lead in advising the President to avoid introduction of contentious and troublesome issues that might have a backlash on the principal business before the Senate. (S/S)



Central America

Assistant Secretary Vaky is currently in Central America on consultations regarding Honduras, El Salvador and Guatemala -- consultations aimed at avoiding another Nicaragua scenario, and aimed at keeping democratic institutions in these countries. (S)

The problem, as I see it -- and the solutions -- is to encourage the leaders to agree to reforms, elections, including elections which may oust them, before the opposition and guerrilla guns start firing. Once that happens, our diplomatic leverage and our effectiveness - short of U.S. troops - which would hardly be desirable - are nil. (S)

~~SECRET/SENSITIVE~~

SECRET/SENSITIVE

Caribbean

On a related front, Phil Habib is working on a US strategy toward the Caribbean. You may wish to ask Vance where that stands. (C)

When you have a free minute, I would like to brief you on the Grenada question you asked about, and I think you might find it helpful to call Habib in for a briefing on the Caribbean. Looking at the current adverse trends -- adverse in the eyes of many Americans because the trends are so destabilizing -- in the Caribbean and Central America, I think that these regions could become the subject of hot foreign policy debate in 1980, with charges that the Administration is neglecting and imperiling the "soft underbelly of America." Senator Stone, as you know, is doing his best to launch such a debate, with Cuba as his foremost example. (S/S)

SECRET/SENSITIVE

~~SECRET~~

THE SECRETARY OF STATE
WASHINGTON

July 25, 1979

MEMORANDUM FOR: THE PRESIDENT
FROM: Cyrus Vance *CV*

1. Wilson Wyatt - I met this afternoon with Wilson Wyatt to discuss the possibility of his taking on the job in Morocco. He will consider it seriously, but has to see whether he can work his way through several existing commitments and personal matters which he would have to clear away before he could take the assignment. We talked for about 45 minutes, and I have given him material on Morocco which he will take home with him today to read. He has promised to get back in touch with me within a few days. I am somewhat dubious that he will be able to say yes, but I hope he does, as he would do an excellent job.
2. MFN - Warren and Bob Beckel met with Byrd, Javits and Church today to discuss sending up the trade agreements (and waivers for MFN) for the Soviet Union and the PRC. Each of the Senators thinks it would be a serious mistake to send up the Soviet trade agreement and waiver prior to the conclusion of the SALT debate. Byrd believes neither agreement should be sent up until SALT is concluded, while Javits and Church favor sending up only the PRC agreement and waiver at the present time. They will be consulting further on the House side tomorrow, and I will be reporting to you more fully at breakfast on Friday.
3. Nicaragua - Gabriel Lewis called Warren today to suggest that Ambassador Moss join Gabriel and Salamin (Panama's Ambassador to Nicaragua) in flying to Managua to discuss Nicaragua's assistance needs with Nicaraguan Foreign Minister D'Escoto and the junta. We agreed to Lewis' proposal, in part to demonstrate our willingness to continue cooperating closely with Panama on Nicaraguan issues, and in part to enhance our contacts with the junta. Ambler, Lewis and Salamin went to Managua this afternoon and will be returning to Panama tomorrow morning.

~~SECRET~~

DECLASSIFIED

NLJC-06-077
per 6/7/06 NSS (fr
6/29/06

~~SECRET~~

2.

4. Refugees - Dick Clark and Bob Oakley testified today before Fascell's Subcommittee in support of an additional FY 80 \$207.29 million authorization request for Indochinese refugees. Most members applauded the Administration's decision to pick up refugees at sea in US naval vessels, and praised Fritz's speech at Geneva. Fascell closed the hearing by announcing his intention to get full committee support for the additional funds on Friday, with a view to instructing House conferees to include the amended budget figures in the House-Senate conference which begins next Monday.

The atmosphere at the Long Appropriations Subcommittee was less friendly, but the result was positive. Clarence Long said that the PRC ought to be asked to take more ethnic Chinese refugees. Congresswoman Smith (R-Neb) favored rescue at sea and aid through UNHCR, but said she had reservations about letting more refugees into the US. Our strongest supporter was Jack Kemp, who made a strong plea for full and immediate funding of our refugee requests. At the conclusion of the hearing, the Subcommittee voted 7-0, with Mrs. Smith abstaining, to report out the full amount requested for FY 80. Floor action on the appropriation will probably be delayed until after the August recess.

5. Greece - During a farewell call today, Greek Ambassador Alexandrakis expressed concern that he was leaving with some tension, specifically over Cyprus and Greek reintegration into NATO, in our bilateral relationship. I emphasized that we take a strong interest in both subjects, and added that I had expressed to former Turkish Ambassador Esenbel my concern that the Turkish side seemed to be walking back from its commitment on certain aspects of a Cyprus agreement. I noted that Esenbel had indicated that Turkey would press the Turkish Cypriots to live up to their commitments if matched by a Greek Cypriot reaffirmation of the positions they had taken in the Makarios-Denktash guidelines of 1977. I assured him we would keep pressing both sides on Greek reintegration into NATO and would continue to support General Rogers as he picks up Al Haig's effort.

~~SECRET~~

~~SECRET~~

3.

6. Northern Ireland - In response to last night's item on the Northern Ireland arms sale issue, you asked whether the British could simply submit applications for arms exports without indicating the ultimate destination. Munitions control regulations require that applications indicate the end-use (whether for police forces, military, or some other purpose) and the name and address of the foreign end-user. Under these procedures, the British have indicated that the arms were for the Police Authority for Northern Ireland. Divergence from the procedure would raise severe problems.

7. Non-Aligned Summit - The Cuban draft communique for the Non-Aligned Summit is radical in tone and substance and directly attacks us on a number of issues. We told the Yugoslavs that we plan to approach several of the non-aligned countries on issues in the communique which directly affect us such as Puerto Rico and our interests in Latin America. We would not, however, attempt to dictate to the non-aligned on broader ideological questions. The Yugoslavs support this course, noting that any perception in the NAM that we are interfering in internal NAM affairs -- as opposed to stating our position on matters which directly affect us -- would be counterproductive. The Yugoslavs themselves plan to seek extensive revisions.

Other moderate non-aligned states have also expressed concern over specific aspects of the draft. I have encouraged Mexican Foreign Minister Castaneda to use Mexican influence with other states to revise the document, particularly the Latin American portions.

~~SECRET~~

MEMORANDUM

OFFICE OF THE VICE PRESIDENT
WASHINGTON

~~CONFIDENTIAL~~

INFORMATION

Memo No. 661-79

August 2, 1979

MEMORANDUM FOR THE VICE PRESIDENT

FROM: Denis Clift *DC*
SUBJECT: Foreign Policy Breakfast,
Friday, August 3, 1979 (U)

Visit to People's Republic of China *OK*

1 MEN: You will wish to report on your conversation with Bob Byrd. (U)

2 *OK* Friendly Nation Determination - Secretary Vance has promised to have a position on friendly nation determination he would make with the President's approval, which would permit negotiations to go ahead for reimbursable US hydroelectric assistance to the PRC, with an announcement of such cooperation to be made during your visit. (C)

OK OPIC - Secretary Vance will be prepared to report on the position State is developing which will permit you to inform the Chinese that the Administration is preparing to support OPIC legislation. (C)

X EX-IM Line of Credit - John White informs you (Tab A) that OMB is not prepared to recommend to the President that you be authorized to inform the PRC that we are willing to extend \$2-\$3 billion line of credit. of interest, and flowing from your meeting with the Chinese scholars this Wednesday, the NSC has provided the memorandum at Tab B on what other nations are doing with the PRC in the credit field:

- Japan, \$12 billion plus a possible \$5 billion;
- UK, \$6.2 billion;
- France, \$7.5 billion;

~~CONFIDENTIAL~~

Classified by Multiple Sources
Review August 2, 1999

DECLASSIFIED

NLJC-06-077
per 6/7/06 NSC ST
6/23/06

CONFIDENTIAL

- Canada, \$3 billion,

- Italy and the Netherlands, \$1 billion each.

Vance was supportive of an Ex-Im line of credit during your Wednesday meeting. Tony Solomon was also supportive. I recommend that you take this up directly with the President at the breakfast taking the position that OMB is being overly conservative and cautious, that the proposed line of credit is realistic, and that the timing is not that difficult. (C)

Termination of Obsolete Agreements with Taiwan

I have been advised by State that ~~Defense~~ at the working levels, has stated that it will need at least a month to decide whether US-Taiwanese agreements are, in fact, obsolete. I strongly recommend that you make Harold Brown aware of this bureaucratic foot dragging and ask him to get Defense cracking immediately on this review process. (C)

Middle East

You will wish to report on your conversations with Jewish-American leaders and on your statement to Israeli Television. I have recommended that you have Bob Strauss invited to the Middle East portion of the breakfast. You should ask Vance to review in the clearest possible terms what he sees the U.S. doing in the U.N. when we are obliged to come to grips with the PLO initiative/Kuwaiti resolution in the UN Security Council when it formally comes up for debate and vote on August 23-24. As you know, if we misplay this Middle East card, tilting toward the PLO while alienating and outraging the Israelis and the Jewish-American community, we not only risk a setback in the Middle East but, tactically of great concern, we risk embittering members of the Senate at a time when we are trying to move SALT II through the Senate. (C)

SALT

You may wish to ask Vance and Zbig what responses they plan to give on Secretary Kissinger's testimony. This, again, is of great tactical importance. (C)

CONFIDENTIAL

MEMORANDUM

NATIONAL SECURITY COUNCIL

~~CONFIDENTIAL~~

August 2, 1979

MEMORANDUM FOR: DENIS CLIFT
FROM: MIKE OKSENBERG *MO*
SUBJECT: Financing of China Trade (U)

You will recall that the Vice President requested information on credits extended to China. (C)

At Tab A is a convenient CIA summary of credit lines arranged or under negotiation as of the end of June. At Tab B is a CIA summary. At Tab C is a Department of Commerce paper on potential ExIm Bank lending to China cleared at the Department of Commerce. (C)

The thrust of this material documents the Vice President's sense that we are entering the game late and low even with a \$3 billion commitment. Japan is in the game at \$12 billion with an additional \$5 billion under discussion. The U.K. is in at \$6.2 billion, France at \$7.5 billion, Canada at \$3 billion, and Italy and the Netherlands at \$1 billion each. China's total credit availability is nearing \$30 billion. (C)

~~CONFIDENTIAL~~
Review on
August 2, 1985

DECLASSIFIED
NLJC-06-077
per 6/7/06 NSC 1F
DATE 6/29/06

ITA

DRAFT

East-West Trade Policy
Staff Paper

The Potential for Eximbank
Financing for
U.S.-P.R.C. Trade

Prepared by:

Allen J. Lenz
Lawrence H. Theriot
Office of East-West Policy and
Planning
Industry and Trade Administration
U.S. Department of Commerce

Draft July 6, 1979

For information call 377-4422
and refer to Project D-59-70

DRAFT



U.S. DEPARTMENT OF COMMERCE
Industry and Trade Administration

THE POTENTIAL FOR EXIMBANK FINANCING FOR US-PRC TRADE

Introduction

The role of credit financing in international trade has grown until today virtually all foreign trade in manufactured goods and industrial equipment is financed on extended payment terms. Moreover, foreign credits have come to play a substantial direct role in financing domestic economic growth in most developing countries. Indeed, many developing nations consciously elect the strategy of importing foreign capital to augment local resources in order to stimulate a more rapid pace of economic advance than would otherwise be possible.

Western Credits in Communist Country Trade

Because of their centralized economic structure and ideological preferences, communist countries have been traditionally reluctant to rely on foreign capital to finance their international trade or economic development. However, in the early 1970s, attitudes changed dramatically in many of these countries. Soviet and East European economic planners became committed to a rapid expansion of trade with Western industrialized countries to acquire up-to-date technology and capital equipment in order to boost economic development. Some East European countries even began to accept Western direct investment capital in joint operations with domestic enterprises. As a result, Western trade with the Soviet Union and Eastern Europe expanded sharply, growing two-fold between 1972-77. However, the growth path for trade has been asymmetrical with communist country imports greatly exceeding their exports. To bridge the gap, the Soviet Union and other communist countries have

used Western credits extensively to ^{help} fuel a rapid expansion of trade with the West.

The People's Republic of China has been a conspicuous exception in this expanded use of Western credits by communist countries. Until very recently China maintained a policy of financing its Western trade with cash or very short term credits, and did not utilize medium or long term loans from the West. However, the Chinese have demonstrated recently that they intend to use large amounts of Western loan capital to finance imports that will be essential to Beijing's economic growth plans. Thus, as China embarks on the ambitious economic development path envisaged in the Four Modernizations Program, it appears that Western medium and long-term credits will fill a role similar to that played in most other communist countries. Indeed, Commerce Department analysis suggests that China's ambitious ^{foreign economic} trade and/growth targets may result in aggregate hard currency trade deficits of at least \$37 billion through 1985, thereby necessitating substantial growth in its hard currency debt.^{1/} One Western bank has estimated China's hard currency debt could reach \$35 billion by 1985, though there are recent signs that China may be unwilling to borrow so heavily.

Role of Western Commercial Banks and Official Export Credit Programs in Financing Communist Country Trade

Private commercial banks provided the bulk of the financing required for the expansion of Western trade with communist countries during the early 1970s. Commercial banks will undoubtedly play a

^{1/} Prospects for PRC Hard Currency Trade Through 1985, Industry and Trade Administration, East-West Trade Policy Staff Paper D-78, February 1979.

a similar pivotal role in China's trade and West European and Japanese banks have already begun to increase their lending to China. Aggregate claims of all Western commercial banks on China grew rapidly from \$301 million in 1976 to \$993 million as of September 1978. Similarly, Chinese owned deposits in Western banks increased from \$1.4 billion to \$3.4 billion as Beijing made greater use of credits offered by Western banks. However, given that steps to normalize U.S.-China relations have been taken only recently, U.S. banks, with total claims of only \$28 million are still in the infancy of developing business with China.

In addition to private credits, governments have been a major factor in financing international trade. This is especially true of trade with many of the communist countries in that Western official credits account for one-third of total Soviet-EE hard currency debt. Although programs vary between countries, virtually all industrialized Western countries offer some form of official financial support for their exporters. Some programs entail direct loans to foreign buyers for purchasing exports from domestic companies. Others provide government guarantees and/or insurance for credits extended by commercial banks or suppliers credits offered directly by exporters. Many governments also provide insurance to support direct investment made by their companies abroad.

The role of government financial support is particularly crucial where exporters are attempting to open a new market. Exporters and their bankers are generally more willing to expand business in an untried market if their domestic government accepts some share of the risk involved.

Official financing has played an even more important role in expanding exports to communist countries, where the trade partner, a government enterprise, exercises centralized control over all foreign trade and financing. Many Western ^{have} government/bilateral agreements with communist countries/^{that} provide their commercial banks and exporters with an officially sanctioned environment for expanding commercial relations and the eligibility of communist countries for official export credit support indicates to private firms their own government's political commitment to expanded commerce with those countries. More ^{loan} importantly, Western government/guarantees directly increase commercial bank willingness to lend by shifting the lending risk from private sector lenders to the government guarantor.^{2/}

In addition to creating a positive atmosphere, official credit programs have a very direct trade expansion effect by providing credits for longer maturities and at interest rates (usually fixed) somewhat lower than floating rate loans available in private financial markets. Since Western exports to communist countries tend to be concentrated in industrial equipment where long-term financing is usually required, the low rates and extended repayment terms frequently offered by official credit programs are strong inducement to communist countries to source imports

^{2/} By statute, most U.S. banks can make loans to a single borrower equal only to 10 percent of their capital base. Since most communist countries utilize a single entity (usually a foreign trade bank) for international borrowing, U.S. banks face legal ceilings that might be lower than the amounts some banks would be willing to lend some of the larger communist country borrowers, e.g. China, Poland, and the U.S.S.R. However, if a loan is covered by an Eximbank guarantee or insurance, it is considered U.S. risk and not charged against the bank's legal lending limit. Thus, Eximbank support can directly expand the availability of private bank credits.

where official credits are available.

Seeing China as an important new market, several of our competitors have aggressively begun to promote their exports by offering governmental export credits to China. Although China has as yet used only a few loans, Western credit offerings now total almost \$15 billion.

Role of Eximbank in U.S. Trade with Communist Countries

To date, the role of the U.S. Eximbank in expanding U.S. trade with communist countries has been limited by various restrictions.

After being suspended after World War II, Eximbank lending to the Soviet Union resumed in 1972 and by 1974, authorized direct loans had reached \$469 million. However, failure to bring a bilateral trade agreement into effect in accordance with the provisions of the 1974 Trade Act resulted in suspension again of Soviet eligibility for Eximbank facilities in January 1975. Since then, the U.S.S.R. has continued to draw previously committed loans and outstanding direct credits now total \$452 million.

Poland, Romania, and Hungary are currently eligible for Eximbank operations (see table 1). Outstanding direct loans to these three countries ^{totalled} / \$719 million as of May 1979. Although all three countries have access to Eximbank's guarantee and insurance programs for private credits, only Romania has made significant use of these services. During its period of eligibility, the Soviet Union refused to authorize private bank use of Eximbank guarantees.

Eximbank credits are generally used to supplement commercial bank financing in individual/export transactions. On average, Eximbank

direct loans have financed 46 percent of the total value of the export contracts it has supported for communist countries. However, reflecting its recent efforts to increase support for U.S. exports,

Eximbank
worldwide
direct loan participation for contracts it supports/increased to 63 percent during 1978.

The importance of Eximbank support for U.S. exports to communist countries is demonstrated by the fact that during 1977-78 disbursements on direct loans financed 25 percent of total U.S. exports of manufactured goods to Poland/ and 16 percent to Romania From 1973-75 / 14 percent of such exports to the U.S.S.R. were financed by Eximbank. Similar or higher levels of support may be essential to expand exports to a new communist country market like China.

China, A New Customer for Eximbank?

Like all communist countries, in fully normalizing its trade and financial relations with the U.S., China is subject to some specific/ legal and requirements/ and several initial steps are required to reestablish China's eligibility for Eximbank.

The bilateral trade agreement, signed July 7 by both governments, must be approved by Congress and brought fully into effect in accordance with the provisions of the 1974 Trade Act. (Similar trade agreements with Romania (1975) and Hungary (1978) have been accompanied by Presidential waivers of the Title IV so called "free emigration" provisions of the Trade Act.) Subsequently, the President must make a determination that Eximbank operations with China are in the U.S. national interest. Bilateral discussions would then be expected, wherein Eximbank staff would familiarize Chinese trade and

financial officials with the bank's operational procedures. Eximbank lending in support of U.S. exports to China could then begin.

However, before this eligibility process can be concluded, as a practical matter one other important impediment must be removed. Eximbank currently has four outstanding loans to China on its books, amounting to \$26.5 million. These loans were made to Chinese enterprises in 1946, but, Chinese Government, by virtue of having nationalized all private enterprises, because obligor in default on principal and interest payments for these loans. / No payments have been made since 1961. Eximbank claims were not included in the settlement of private property claims and frozen assets which was concluded in May 1979. Consequently, these official U.S. Government claims will have to be satisfactorily dealt with before appropriate administrative steps can proceed to reopen China's eligibility for Eximbank operations.

Effects of Eximbank Lending on U.S.-China Trade

Implementation of the U.S.-China trade agreement, and MFN tariff status for China is likely to boost U.S.-China trade sharply. However, many observers feel the availability to China of U.S. Eximbank loans is even more crucial, with such loans absolutely necessary for U.S. exporters of industrial plants and equipment to compete successfully against European and Japanese competitors who are eager for China's business and often are backed by generous supplies of official credits at very attractive rates.

Chinese eligibility for Eximbank loans will affect U.S. exports in two ways. First, the fully normalized trading environment symbolized by Eximbank eligibility will increase

China's willingness to do business with American companies even where official export credits may not be utilized. Similarly, availability of Eximbank loans will be concrete confirmation of USG support for expanding trade with China that will enhance the willingness of U.S. commercial banks to lend to China even on transactions where Eximbank is not involved.

Secondly, Eximbank eligibility will expand the amount and improve the terms of trade financing available in the United States, thereby directly enhancing the competitiveness of U.S. firms in exporting to China. Although making Eximbank available to China will doubtless have important positive indirect effects on U.S.-China trade, this paper attempts to assess only the second, more direct effects, of Eximbank support for U.S. exports by estimating the potential levels of Eximbank lending to China.

Constraints on Eximbank Lending to China operations with

Eximbank / China will be constrained by at least two factors; the competitiveness of U.S. credit terms and the volume of Eximbank loan funds available. These constraints on Eximbank's lending potential are not peculiar to China but rather effect the Bank's operations world wide.

Under its operating charter, Eximbank must be profitable, i.e. in aggregate, its earnings on loans must exceed the cost Federal Financing Bank, an instrumentality of the U.S. Treasury. of Eximbank capital, borrowed from the / This profitability requirement often results in Eximbank interest rates which are higher than the subsidized rates usually available under the official export credit programs of our competitors. also In addition, competing foreign programs may/subsidize export

financing by protecting exporters from inflation and exchange rate fluctuations and by combining foreign aid funds with official credits. Indeed, in its most recent report to the Congress on its international competitive position, Eximbank concluded "the U.S. is not only noncompetitive with foreign export credit agencies, but is also making little progress in closing the gap."

Given the basic restriction that Eximbank must, overall, be self-financing (i.e., that overall the returns from its loans must cover the cost of its capital and its operating costs) it may have difficulty in competing with the loan terms of competing official credit agencies of other governments in some individual loan transactions. A more important constraint on lending to China, however, is likely to be the limited amount of loan capital available to the bank.

With passage of its new operating authority in 1978, Eximbank's budgeted capital was raised from \$25 to \$40 billion for direct loan and guarantee operations through 1983. This limit on possible loans can be increased only through additional legislative action. Having recently achieved a major increase in its resources, facing the historical reluctance of Congress to provide ever increasing levels of governmental financing for U.S. exports, and considering the overall tight federal budgets^{new} expected to prevail for the foreseeable future, additions to Eximbank's operating capital appear unlikely through 1983. With finite capital resources and a mandate to support U.S. exports to 130 potential trading partner countries, Eximbank necessarily

maintains a diversified portfolio of loans, reflecting both the need to serve many customers around the world and normal banking prudence in diversifying risks by avoiding excessive concentration of loans in one borrower. Thus, the portion of Eximbank capital that can be committed any single borrower, including China, will necessarily be limited.

Estimated Future Eximbank Loans for China

Assuming normalization of U.S.-China commercial relations and no legal impediments to official U.S. export credits for China, but bearing in mind the general constraints on Eximbank's lending,

(1) What level of support for U.S. exports to China could be realistically expected from Eximbank and (2) What direct effects might that support have on U.S.-China trade volumes?

Eximbank has recently become more aggressive in providing U.S. exporters official credit support on terms that match our competitors. Lending activity has thus increased sharply with total FY 1979 operating authority increased to \$4.1 billion from \$3.6 billion last year. Unless increased by Congressional action, total loan authority is likely to be in the range of \$3 to \$4 billion annually through 1983, when Eximbank's current charter expires. The addition of new, large eligible borrowers like the PRC and the Soviet Union would sharply increase the potential demand on Eximbank's resources, without increasing its already limited/loan capital.

Analysis of Eximbank lending to other large borrowers can shed some light on the potential for lending to China. Notwithstanding attention to diversification of risks, the principal

U.S. trade partners are, as would be expected, also Eximbank's largest customers (see table 1). For example, the bank's largest single customer for direct loans has been Brazil where commitments totaling \$3.5 billion have financed exports worth \$ 4.7 billion since 1958. Poland is the largest currently eligible communist country borrower from Eximbank with direct loan commitments of \$315 million having financed exports of \$501 million since 1973. Brazil, which currently has outstanding direct loans and undrawn commitments from Eximbank of \$1.3 billion, is among the bank's largest debtors, holding 8.5 percent of its outstanding loans. These loans, however, are diversified among 102 different Brazilian borrowers, with 3/4 of the total held or guaranteed by the Brazilian government. Furthermore, the \$1.3 billion total has gradually mounted over a long period of eligibility. Eximbank's claims on Brazil today exist in a context of a vigorous \$ 5.8 billion two-way trade relationship, more than \$1 billion in U.S. exports of manufactured goods in 1978, the type of export typically financed by Eximbank loans. New Eximbank commitments to Brazil were only \$133 million last year, while Eximbank disbursements on direct loans to Brazil totalled \$90 million actual and thereby supported only a very small portion of U.S. exports. Similarly, current loan exposure to Mexico of \$1.3 billion has accumulated since 1958. New Eximbank loan commitments to Mexico were up sharply to \$611 million in 1978, but \$70 million in loan disbursement financed only a small part of the \$5.7 billion in nonagricultural U.S. exports to Mexico.

An additional possible constraint on future Eximbank lending for exports to China could result from the U.S. commitment to

"evenhandedness" in developing commercial relations with both China and the Soviet Union, possibly acting to keep loan commitments to the two countries at roughly equal levels. We have estimated elsewhere³⁾ that absent any special restrictions, a realistic total for Eximbank direct loan commitments to the Soviet Union would probably not exceed \$1.5 billion by^{end} 1984.

All things considered (i.e. loan capital limitations, risk diversification, equal treatment for China and the U.S.S.R.), our judgment is that, even assuming rapid progress in normalizing U.S.-China trade, cumulative commitments by Eximbank to direct loans to China are unlikely to exceed \$300 million per year through 1983, the remaining life of the current Eximbank operating charter.⁴⁾ If loan commitment activity began in 1980, this would raise Eximbank exposure to China to \$1.5 billion by end 1984. If this were matched by a similar amount (\$300 million per year) of new Eximbank commitments to the U.S.S.R., the \$600 million total would alone represent 15-20 percent of the \$3-\$4 billion annual Eximbank new loan authority that is likely to be available. Furthermore, Eximbank's exposure to China and the U.S.S.R. would rapidly escalate to levels that other borrowers (e.g., Brazil, Mexico) took much longer to achieve.

Direct Effect of Eximbank Lending on U.S.-China Trade --Fixed Exposure Scenario

Given our projections of the amounts of available Eximbank credit, we can also estimate the direct support available for financing U.S. exports to China.

³⁾ A. Lenz and L. Theriot, "The Potential Role of Eximbank Credits in Financing U.S.-Soviet Trade" in Issues in East-West Commercial Relations, published by Joint Economic Committee, January 1979.

⁴⁾ In actual practice Eximbank loans are authorized on a case by case basis to support specific U.S. exports. Eximbank does not set a specific exposure limit for any individual country.

Eximbank financing of an export transaction involves, a several stage commitment-disbursement payback cycle:

- o Eximbank commitment to an export loan;
- o Later disbursement of funds to support the export;
- o A return flow of repayments from the borrower.

While the time periods obviously vary from loan to loan, table 2 depicts a sequence we believe would be typical for loans to the PRC.

Applying the cycle described in table 2 we have calculated the effects on U.S. exports and bank exposure levels under two differing scenarios.

Under the first scenario:

1) Eximbank is assumed to make annual direct loan commitments of \$300 million for U.S. exports to China until total exposure reaches \$1.5 billion of commitments in 1984.

2) After reaching \$1.5 billion of commitments in 1984, to stabilize exposure at that level, new commitments each year are limited to principal amounts repaid from earlier loans. (See Table 3).

Under this scenario, / new commitments of \$300 million in 1980 (line 1) are disbursed during 1982 when the financed exports are actually shipped. A grace period then extends until the exported equipment is made operational in the buyer country--a process assumed to take two years--through 1984. Repayment of the portion of the contract funded by commercial banks thus commences in 1985 and is completed in five equal installments in 1989. The Eximbank financed portion of the loan is then repaid, also in five equal amounts, through 1994.

Assuming Eximbank continues to commit financing of \$300 million annually, \$1.5 billion of loan authorizations would

be reached in 1984. If the bank then relies on recycled capital from repayment of earlier loans, thereby holding its exposure to \$1.5 billion, no funds would be available for new loan commitments to support exports until 1990. Thus, Eximbank would face a sharp "valley" in its ability to continue supporting U.S. exports to China beyond 1984. Moreover, repayments of old loans would initially be small (assuming five equal annual installments, only 20 percent of outstanding loans are repaid each year) and would provide only \$60 million for new commitments in 1990. Indeed, in the table 3 scenario available funding for new loans does not again reach \$300 million until 1995 and then declines once again to only \$72 million in the year 2000.

A similar, but delayed, cycle applies to the actual disbursement of funds and the exports they finance (lines 3 and 8). Assuming Eximbank continues to finance an average of 63 percent of the export contracts it supports (as in 1978) with commercial banks exporters or buyers providing the remaining 37 percent, the \$300 million committed in 1980, would finance \$476 million in exports when disbursed in 1982. Of course, if Eximbank finds it necessary to finance an even larger portion of each contract to meet Western competition, total exports generated by the \$1.5 billion in loans would be correspondingly less.

Under the assumption of 63 percent financing by Eximbank, however, \$300 million of loans would support \$476 billion in exports each year 1982-86. Then, because of the "valley" in new committable funds during 1985-89, no loan disbursements would occur from 1987-1992 (line 3) and exports to China during this period would have to be financed exclusively by private

banks.

Nevertheless, by the year 2000, the original \$1.5 billion in loans through recycling would result in total loan disbursement of about \$3 billion (line 4) financing export contracts valued at \$4.8 billion (line 9).

The "valley" in lending capacity illustrated in table 3 as occurring if exposure is limited is, of course, not something that would be unique to the U.S. Eximbank. Rather it may pose a dilemma for all Western countries which extend large amounts of long term official credits and guarantees of private credits to China. In keeping with the OECD consensus, most extensions of official credits by other governments probably will involve ten year maturities similar to those assumed in our scenario. But as the table 3 presentation highlights, long term lending means extended delays in capital flowback so that, after an initial round of heavy lending, Western governments will face the prospect of either reducing new ^{credit} commitments (at the expense of reducing Chinese export) the level of new orders, or continuing to increase their loan exposure over an extended period until repayments can finance new loan

The alternative scenario which follows the effect on illustrating to provide illustrates how exposure levels of continued new long term financing for exports to China.

An Alternative Scenario-- Unlimited Exposure

Table 4 provides an alternative scenario for future official U.S. lending for exports to China wherein new loan commitments of \$300 million continue to be made each year with no limit on

Eximbank total exposure. (This scenario again assumes 10 year Eximbank loans with a typical repayment pattern illustrated in table 2.)

In this case, the "valley" in export financing is avoided as new commitments of \$300 million are made each year, again supporting annual exports of about \$476 million per year. However, by continuing to make new loans, Eximbank's exposure (undrawn commitments and principal outstanding) also continues to grow before stabilizing at \$4.2 billion in 1993, at which time repayments match new commitments. In view of its limited operating capital (\$40 billion until 1983) and demands from many borrowers, it may be unrealistic to expect Eximbank each year to commit such a large portion of its capital in direct loans to a single country.

Western Credit Competition for China Trade

The 1976 OECD consensus on acceptable credit terms for official export financing programs. sets specific limits on minimum interest rates and maximum maturities for governmental financing of exports to various groups of countries. Since the consensus applies to exports world wide, it will necessitate specific limits on terms of official credits extended to China.

OECD

The/ consensus does not, however, affect the volume of official credits that may be offered to China by our competitors, which already total nearly \$15 billion, including \$6.9 billion from France and \$2 billion or more each from Japan, Canada and the U.K. (see table 5). Even Italy, whose trade potential with China may be somewhat limited, has extended a \$1.0 billion credit line.

Based on the current economic and political environment, our judgment is that Eximbank lending will be more modest, unlikely to average more than \$300 million per year over the foreseeable future. Clearly, the credit offerings of some of our competitors tend to make the lending levels we project for Eximbank seem modest indeed.

Nor is the \$15 billion of already available official credit offerings to China by our competitors likely to represent an upper limit. In the past, Other Western governments have demonstrated a clear willingness to continuously increase their risk exposure in providing official credits for their exports to the Soviet Union and Eastern Europe. Seeking employment and balance of payment benefits, they are likely to follow a similar pattern in lending for exports to China, at least for the years immediately ahead. Consequently, it seems reasonable to conclude that Eximbank will not be able to provide the massive amounts of financing for U.S. exports to China envisioned by some, but that unless competitive patterns change, other Western nations may well be willing to do so, albeit at the cost of constantly escalating exposure levels.

Obviously our judgment of relatively low Eximbank lending to China could prove incorrect. The many factors that could conceivably increase lending to China include, for example, U.S. lend special to a political decision to emphasize the development of trade with China, or a decision to compete more intensely with other Western nations through a general increase in the use of official export credits in expanding U.S. exports worldwide.

Alternatively, it may be argued that in making large official loans now, our Western competitors are opting for short term boosts to exports from long term lending, without much attention to the future/^{risk} exposure levels that will result, and that they may be unable or unwilling to sustain this technique over an extended period. The need for the U.S. to match our competitors in continuously extending long-term loans to China would consequently be less.



MINNESOTA HISTORICAL SOCIETY

Copyright in the Walter F. Mondale Papers belongs to the Minnesota Historical Society and its content may not be copied without the copyright holder's express written permission. Users may print, download, link to, or email content, however, for individual use.

To request permission for commercial or educational use, please contact the Minnesota Historical Society.



www.mnhs.org