A.I.D. Policy Paper

CO-FINANCING

U.S. Agency for International Development
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Bureau for Program and Policy Coordination
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Executive Summary

The role of co-financing and the potential for its expanded use have been subjects of increasing attention of the international development community over the past several years. A.I.D. has reviewed its experience, and that of other official donors, with co-financing and reaffirmed that it is a useful method of development finance that offers the potential for leveraging and increasing the effectiveness of its resources. Such financing arrangements, moreover, may enhance prospects of the adoption of appropriate economic policies by developing countries.

A major reason for A.I.D.'s enhanced interest in co-financing is a keener appreciation of its potential for increasing the involvement of the foreign private sector in the development process. This aspect of co-financing complements A.I.D.'s somewhat broader private sector initiative, that includes among other things direct loans to indigenous private sector firms as a means of encouraging and enabling their participation in the economic affairs of their respective countries. Co-financing arrangements with the external private sector also may facilitate the transfer of skills and technology, and A.I.D.'s in-country presence and its capability to provide technical assistance, both direct and through the employment of contractors, places it in a favorable position to participate in such arrangements with modest resource inputs.

To assist missions in identifying co-financing opportunities with external private sources of funds, the Administrator has established a co-financing working group to review mission capital projects at the pre-PID or PID stage. Missions are encouraged through their respective Bureaus to utilize the expertise of this group. Moreover, Missions should undertake an assessment of their capability to identify and evaluate co-financing opportunities. On the basis of such assessments respective Washington regional bureaus should be informed of assistance needs and their feasibility with regard to addressing inadequacies.

While co-financing has a number of potential advantages, particular care should be exercised to insure that co-financing does not become an end in itself, but rather remains a mechanism among other alternatives to be utilized when it represents the most efficient application of A.I.D. resources. Thus, against the background of its legislative and general policy framework, A.I.D. will promote and/or participate in co-financing arrangements within the context of respective country development strategies. Fundamentally the Agency will continue its role as a residual lender, and source/origin regulations will apply in most cases. A.I.D. will thus tend to favor the parallel form, but not to the preclusion of joint financing arrangements.

Co-financing arrangements that involve A.I.D. direct loans to indigenous private sector firms will be made as a matter of general policy at or near market rates of interest, with repayment periods determined upon the basis of the financial characteristics and other revelant considerations of respective projects. Moreover, each such loan, when denominated and repayable in foreign currencies, must include features satisfactory to the Agency with regard to the foreign exchange risk coverage. These parameters are included primarily to preserve and strengthen the role of private market forces in the resource allocation process. These requirements, moreover, may support A.I.D.'s efforts that encourage the adaptation and implementation of appropriate economic policies.

Commercial bank participation in A.I.D. sponsored co-financing arrangements should generally be in the form of at risk lending as a means of enhancing the prospects for additionality over the medium to longer term. While A.I.D. in appropriate circumstances is willing to provide "comfort" in various forms, consistent with prudent financial management, it will not generally link its loans to those of other co-financing participants through the use of mandatory cross-default clauses. A.I.D., on the other hand, will be agreeable, in the case of private lenders to link its loans through the use of optional cross-default clauses. Under this type of loan linkage each lender can make an independent determination, rather than be bound to take default action based on the decision of an associated lender.

Finally, A.I.D. will limit its sponsorship and/or participation in co-financing arrangements to those structured in a manner consistent with the Agency's own prohibition on the initiation of mixed credits, and the U.S. Government's obligations under both formal and informal trade agreements, particularly the Organization For Economic Co-operation and Development Guidelines for Officially Supported Export Credits (OECD Arrangement).

I. Introduction

The role of co-financing[1] and the potential for its expanded use as a method of development finance have been subjects of increasing attention by the international development community over the past several years. This stepped-up interest in co-financing arrangements has taken place during a period in which there has been a deterioration of economic conditions in most of the industrial countries, a rapid increase in the resource needs of the LDCs, and reduced growth in Official Development Assistance (ODA). It has thus become clear to a broad segment of the development community that if LDCs are to address their more immediate problems, and over the longer term realize their potential, more effective efforts must be put forth to mobilize all available resources, both public and private, and to increase the efficiency of their utilization.

As a result of this increased interest, there has been over the past several years a number of extensive international efforts to analyze the role and potential for co-financing. Prominent among these has been the work of the DAC Secretariat[2] and the Task Force on capital market access of the IMF/IBRD Development Committee.[3] The work of this latter group was subsequently expanded by the Development Committee Task Force on non-concessional flows.

[1] As used in this paper, the term *co-financing* refers to any formal arrangement under which A.I.D. loan and/or grant funds (denominated in dollars or the local currency of the recipient) are associated with funds from one or more different sources (private or public) outside the borrowing country in the financing of a particular project or program. Participation can be in the form of joint or parallel financing. *Joint financing* refers to a co-financing arrangement for which there is a common list of goods and services and where financing of all or certain items are shared between co-lenders in agreed proportions. On the other hand, *parallel financing* refers to a co-financing operation in which each co-lender finances different goods and services or distinct parts of a project. Joint financing that involves the combining of an official/officially supported export credit and Official Development Assistance (ODA) from the same country would be a *mixed credit* if acceptance of the export credit is made a condition for the ODA. A.I.D's policy and the guidelines that govern Agency participation in mixed credit financing are set forth in A.I.D. Policy Determination Number 2 (new series), "Mixed Credits," September, 1982 and are thus not treated in this paper.

[2] Stepped-up Co-financing [CE (78)11/DAC (78) 21], DAC (79)15; Co-financing Operations of the European Community (DCD/80.35); Co-financing by DAC and OPEC members and International Financial Institutions (DCD/79.12).

[3] The Joint Ministerial Committee of the Board of Governors of the IBRD and the IMF on the Transfer of Real Resources to the Developing Countries, known as the IMF/IBRD Development Committee (DC).

The Development Committee (DC) directed much of its attention toward analyzing and discussing measures which could increase the total flow of external private resources to LDCs. In this context the DC's Task Force on capital market access reviewed the operations and regulations of capital markets in the industrial countries. It concluded that the major impediment to broad participation in the longer-term segments of these markets by the developing countries as a group is an unfavorable perception of their creditworthiness by private providers of funds. This unfavorable perception results in part from an imperfect flow of information. Against this background, and as a means of assisting some LDCs to gain access to long-term private capital, the Task Force on non-concessional flows in its final report, among other things, urged MDBs to give higher priority to co-financing.[4] In this context, it encouraged the MDBs to review their loan policies and procedures with a view to making modifications in their programs that would be developmentally sound and at the same time compatible with a marked increase in their co-financing operations with funds from private sources. The Task Force at the same time was careful to note that such programs would also have to address the anxiety on the part of LDCs that participation in co-financing might on balance turn out to reduce the level of official flows available and therefore yield little quantitative additionality.

The multilateral development banks have sought to expand their co-financing programs with both private and public lenders. The United States in its participation in these groups has strongly endorsed their efforts to increase this type of financing, and has encouraged the use of co-financing by the Multilateral Development Banks (MDBs) as a means of increasing the flow of private capital to LDCs and of introducing developing countries to private financial markets. Moreover, at the Economic Summit in Bonn in July 1978 the United States, along with other participants, agreed to encourage governmental and private sector co-financing of development projects with MDBs.

The remainder of this paper first reviews international co-financing experience by official sources; followed by a discussion of additionality, then a review of AID's private sector initiative and policy with regard to co-financing, an analysis of policy issues currently faced by A.I.D., and concludes with directions for A.I.D. policy.

[4] The U.S. strongly endorsed the recommendations of the task force concerning co-financing.

II. Co-Financing Experience by Official Sources

A. Bilateral Donors and the Development Assistance Committee

Bilateral donors and correspondingly the Development Assistance Committee (DAC) of the OECD have directed much of their attention to bringing about a greater realization of the potential that co-financing offers for more effective coordination among official donors. As a result, co-financing has been viewed by the DAC primarily in the context of its ability to improve the quality of assistance rather than its potential for bringing about an increase in the volume of assistance. The DAC has directed particular attention toward the development of a set of relations between Arab/OPEC aid agencies and DAC donors conducive to co-financing operations.

Among the specific advantages that this financing technique provides is the opportunity for donors to combine their resources in a manageable manner to undertake projects of high development priority that require financial, administrative, and/or technical inputs beyond the capacity of a single donor. Moreover, it can permit, as was the case with the Arab/OPEC aid agencies, a more rapid commitment of project resources by donors that are not familiar with a particular country or region and have little experience in providing assistance. For example, over the 1975-81 period Arab/OPEC aid agencies, although relatively inexperienced in providing assistance, accounted for 35 percent of the $21.2 billion of funds committed to co-financing arrangements, compared with a share of 18 percent of all ODA (see Table 1). At the same time it is recognized that co-financing can be administratively difficult compared with single donor projects. The appraisal and implementation of projects frequently suffer delays due to differences among donors with regard to project appraisal criteria, procurement policies and ratification procedures. There is also the potential danger of encouraging or participating in excessively ambitious projects merely because large-scale funds are available through co-financing arrangements.

TABLE - 1

Co-Financing: Amounts Committed 1975 — 1981
($millions)

Year	MDBs	Arab OPEC Agencies	Official DAC Donors	Private DAC Sources[5]	Other	Total[5]
1975	994	870	651	49	65	2,629
1976	828	810	399	19	0	2,056
1977	1,283	1,158	503	65	0	3,009
1978	1,263	974	469	88	66	2,860
1979	2,014	1,517	567	182	106	4,386
1980	1,656	778	489	7	17	2,947
1981	1,246	1,366	736	5	0	3,353
	9,284	7,473	3,814	415	254	21,240

Source: The OECD Observer, No. 117, page 32, July 1982

[5] The OECD data for private lenders significantly understates the actual participation of such lenders in co-financing because it includes only specific loan agreements signed during the respective reporting period, whereas private bank loans in actual practice are arranged only as needed. The OECD also does not include a substantial amount of private bank lending to LDCs that on the face of loan documentation is unrelated to any specific project but which is in fact used in support of co-financed projects. For these reasons, total resources committed to co-financing is importantly understated.

B. **Multilateral Development Banks (MDBs)**

The MDBs, particularly the IBRD, have stepped up their efforts to increase markedly their co-financing operations. These efforts may not only reflect a response to the urging of the developed countries but also an attempt by these institutions to minimize the effects on their lending operations that could result from less frequent and smaller replenishments of their capital by official donors in the future.

Efforts on the part of the MDBs, especially the IBRD, to involve private sector resources in co-financing arrangements has yielded encouraging results. For example, over the 1979–1982 period resources from private lenders committed to co-financing arrangements with the IBRD/IDA were equal to almost 16 percent of the total of $46.8 billion in loan commitments made by IBRD/IDA, compared with a figure of slightly less than 4 percent of the total of $27.8 billion of loan commitments made by those institutions in the previous four years.[6] International commercial bankers have suggested that they might be inclined toward increased participation with the MDBs if they were approached much earlier in the project preparation process, and afforded an opportunity for a greater participation in early discussions with potential borrowers. Moreover, they indicated a need for less cumbersome procedures, and more commercial terms and conditions on their share of co-financed loans.[7] The commercial bankers also cited a need for a significant strengthening of cross-default clauses,[8] preferably to include mandatory provisions.

[6] The figures for private lenders as compiled by the IBRD/IDA include commitments that have been arranged but not signed, since these loans are generally not completed and signed until there is an actual need for the funds. The figures also include all external private loans that assist IBRD/IDA operations, whether or not formal co-financing arrangements are concluded.

[7] In an attempt to address some of these financial issues the IBRD recently approved a trial program of new instruments for co-financing with commercial banks. These instruments, referred to as "B" loans, are designed to permit the IBRD's participation in the portion of a co-financed undertaking that commercial banks finance. This participation can take several forms, including the funding of later maturities, and pro rata funding over the term of the loan.

[8] A cross-default clause sets forth the legal rights and responsibilities of each lender in a co-financing arrangement in the event of default on their respective loans. Mandatory cross-default clauses require each lender in a co-financing arrangement to declare respective loans in default in the event of default on any loan in the co-financing arrangement, and in concert with other participants to seek remedies as set forth in the loan agreements. Moreover, the invocation of a cross-default clause may result in the calling of other unrelated loans and credit facilities to the same borrower.

Of the specific issues raised by the commercial bankers, the call for a mandatory cross-default clause presents the most difficult problem to address.[9] There is serious question in the development community of whether mandatory cross-default clauses are compatible with the traditional role of MDBs as development finance institutions. A mandatory cross-default clause would not permit the MDBs to exercise independent judgement, and if brought into actual effect could lower the credit standing of the MDBs, since it would involve them in actually rescheduling of their loans, a step they have been able to avoid to date. This in turn could lead to increases in their borrowing costs and consequently their lending rates to all borrowers. The failure to adopt a mandatory cross-default clause may well deter some private bankers. Over time, however, as private creditors become more familiar with the approach, the opportunity to participate in co-financing arrangements with MDBs, and take advantage of their expertise and relations with LDC governments, may induce a broader range of commercial banks and other private resources to make funds available for such arrangements.

The U.S. Government has supported the refusal of the MDBs to make use of mandatory cross-default clauses. This support is based on their traditional role as development finance institutions, as well as the fact that their loans are to Governments or are guaranteed by respective Governments. Debt problems that involve official lenders and LDC governments are dealt with in the "Paris Club" as against the "London Club" for problems involving private lenders. The "Paris Club" is considered more adept than the "London Club" in dealing with the development and foreign policy issues that are sometimes associated with the debt problems of developing countries. For similar reasons, as a matter of general policy, A.I.D.[10], the Export-Import Bank, and the Overseas Private Investment Corporation make use of an optional cross-default clause in their co-financing transactions. The same is true for the International Finance Corporation (IFC) of the World Bank (IBRD). Under this type of arrangement each lender can make an independent determination, rather than be bound to take default action based on the decision of an associated lender.

[9] The MDBs presently use an optional cross-default clause under which respective leaders are not obligated to take action; each retain the option to exercise, or to refrain from exercising, at its own discretion, the remedies of its loan agreement.

[10] The use of mandatory cross-default clauses may be considered on a case-by-case basis.

C. A.I.D. Participation With Other Official Sources

The U.S. has long recognized that co-financing among official donors can be an effective mechanism for bringing about increased and more rapid resource transfers to particular countries, and this feature might prove to be significant to the Agency for achieving its objectives in strategic developing countries.

Clearly a major aspect of A.I.D.'s interest in the use of this financing technique among official donors stems from the opportunity such arrangements offer, through the pooling of resources and efforts, for more intensive dialogue with respective LDCs and other participants to encourage the adoption and implementation of appropriate economic policies. Another major positive aspect of co-financing from A.I.D.'s point of view, is that it provides opportunities for the U.S. Government to be more directly associated with, and have influence on, high priority projects that its resources standing alone would not afford. Nevertheless, co-financing should not become an end in and of itself, but rather should be viewed as a mechanism among other alternatives to be utilized only when it represents the most efficient application of A.I.D. resources in the context of the development objectives of country specific strategies.

A.I.D.'s participation in co-financing arrangements, both joint and parallel, has represented a very modest proportion of its total program. Despite the potential advantages that this financing technique offers, there has been little systematic attention given to the identification of projects suitable for co-financing, nor an organized procedure for the earlier identification and preliminary evaluation of MDB and/or other donor projects suitable for A.I.D. participation.

Although complete data are not available, a preliminary review confirms that over the past five years A.I.D. has participated in 17 co-financing arrangements (see Table 2). All but one was in association with the IBRD/IDA; the remaining project was in conjunction with the European Economic Community (EEC).[11] The largest number of co-financed projects in which the Agency participated over this period were focused on agriculture and rural development.[12] This sector preference is also given high priority by the IBRD/IDA, and has resulted in a concurrence of interest in the poorer developing countries. Moreover, project identification and preparation by the IBRD/IDA may save A.I.D. considerable manpower in those cases in which there is a convergence of interests and objectives. In addition their presence during loan negotiations has proven beneficial in terms of achieving degrees of conditionality that bilateral donors view as desirable but may be unable to achieve when acting alone or in concert with other bilateral donors. On the other hand, potential manpower savings in the project identification and preparation process must be measured against the possibly greater administrative difficulty involved in the implementation of co-financed compared with single donor projects. Even in cases in which administrative difficulties are not encountered, there is the need for A.I.D. to be sufficiently involved in the project implementation process to assure that agreed upon policy measures are not put aside in the interest of maintaining a project on schedule.

Table 2

Select A.I.D. Co-Financing, 1978–82
($ Millions)

Number of Projects	Sectors	Total Cost	Total External Finance	Amount Provided by A.I.D.
9	Agric. & Ru/Dev.	1,324.0	676.9	159.3
2	Power	601.7	418.2	134.2
2	Industry	688.8	402.7	78.0
2	Transp.	50.9	45.3	19.0
2	Health/Pop.	82.7	48.8	5.0
17		2,748.1	1,591.9	395.5

[11] The U.S. has recently held discussions with Japan that may lead to co-financing arrangements with that country.

[12] Examples are (a) a 1979 project in the Arab Republic of Yemen in support of the establishment of agricultural and livestock secondary schools (A.I.D. provided $1.0 million for technical assistance of the total project cost of $21.4 million), (b) a 1979 project in Pakistan in support of a urea plant to meet the country's growing demand for nitrogenous fertilizer (A.I.D. provided $40 million for financing imports of a total of $260 million), (c) a 1980 project in Somalia in support of increased crop and livestock production through the development of all-season access roads and a farm system to preserve the productivity of the land in the Bay region (A.I.D. provided $10.5 million for goods and services of a total of $43.4 million), and (d) a 1981 project in Haiti in support of farmer credits for the purchase of production inputs as well as the building of regional farm-development centers (A.I.D. provided $1.6 million for goods and services of a total of $5.2 million). Missions can obtain more specifics on these as well as other co-financed projects in which A.I.D. has participated from their respective regional bureaus.

A.I.D's participation in co-financing arrangements has in the overwhelming number of cases been in the form of parallel financing. Other DAC donors also heavily use this form of participation. Parallel financing permits each participant in co-financing arrangement to follow its own administrative procedures, criteria and preferences, and to place restrictions on procurement. This latter advantage is important to A.I.D., given its source/origin and other procurement restrictions. Parallel financing also allows participants to be more clearly identified with particular parts of projects than is the case for joint financing. The parallel form of participation in co-financing arrangements, on the other hand, may put additional administrative pressure on LDC government officials, and thereby make it less attractive, since they are required to deal with the differing criteria and operational procedures of a number of financial participants at the same time. Other problems that have been encountered have been generally associated with project implementation, particularly centered on the necessity of keeping the separate but related parts of projects sharply focussed and in harmony.

Although A.I.D.'s source/origin and other procurement rules and regulations are better suited to parallel financing, they do not preclude participation in co-financing arrangements in a joint financing manner.[13] Instead there is a presumption that A.I.D. will conduct its operations in a manner that does not require the frequent use of waivers. Moreover, it is sometimes possible, with careful design and prior planning, for A.I.D. to participate in joint financing arrangements without the use of waivers. The Southern Access Road project in Sudan, undertaken in 1980, is an example of A.I.D. involvement in joint financing. In that project joint financing could be utilized because A.I.D. had considerable assurance before making a formal commitment that the bulk of procurement from its financing would be U.S. source/origin.

It must be realized, however, that A.I.D. procurement policies and regulations apply to all A.I.D. projects, whether or not co-financing is involved. These policies and regulations involve more than just restrictions on the source and origin of goods. Other restrictions apply to the eligibility of commodities, delivery services, and suppliers and contractors; competitive procedures; maximum prices for commodities; and cargo preference. Some restrictions, but not all, can be waived in appropriate cases. The analysis can become especially complicated when co-financing is involved. Therefore the Office of General Counsel should be consulted at the earliest possible stage of any proposed co-financing and long before any agreement in principle is reached with a prospective co-financier on a particular project.

Joint financing with the MDBs can also be accommodated, especially when the major portion of the procurement for the project can reasonably be expected to have U.S. source/origin. It is recognized that with limitations of this type in the co-financing arrangement, complete additionally in terms of increased U.S. exports may not result, since some procurement from the U.S. may have taken place in any case as a result of the international tender system used by the MDBs.

Developing countries typically have a preference for joint financing arrangements under a single lead agency, since they view them as administratively simpler than parallel arrangements. A.I.D.'s legislative requirements and procedures impose a bias toward the use of parallel arrangements. Experience under parallel arrangements might be improved if the Agency examines more closely, before becoming involved, potential coordination problems. It would then be better prepared, in conjunction with other co-financers, to quickly address these problems if they arise. A.I.D. should also be prepared to provide technical assistance when needed to the developing countries to enhance their capacity to deal with complex administrative undertakings, particularly those directly related to managing co-financing operations.

III. Additionality

A. Co-Financing Among Official Sources

An important issue associated with co-financing is whether it actually results in a net addition to the capital flow to the developing countries. This is a complex question to which no definitive response has emerged. Much depends on the respective sources of co-financing. It is reasonably clear that co-financing exclusively among official donors and the MDBs generally would not provide net additional resources to the developing countries as a group, but may increase the effectiveness of development assistance. The magnitude of funds available to these official providers are fundamentally a function of

[13] Procurement under a parallel co-financing arrangement is left to each co-lender, and thus takes place in accordance with their respective procedures, whereas under joint financing procurement is by the lead agency and usually is by international competitive tender.

their respective budgetary processes, and in the short to medium term is unlikely to be affected by the form that their financial participation in projects takes. On the other hand, there is clear evidence that co-financing can speed up commitments by official sources in some cases, for example the Arab/OPEC donors during their initial years. Moreover, the availability of already prepared high priority projects in sectors of interest to donors may influence their country allocations.

B. Co-Financing With Export Credits

In co-financing arrangements in which official export credits and/or private sector loans participate, the issue of additionality is less clear. Most if not all official export agencies have some system of determining the limit of their exposure to a particular country. These exposure levels are generally quite flexible and opportunities to participate in co-financing arrangements with official donors and/or MDBs in high quality projects have resulted in adjustments in exposure levels for particular countries. Overall, however, these agencies (for example Eximbank), operate under budget and guaranty authorization limits, so that in the aggregate there is a ceiling on the magnitude of their operations. On the other hand, the availability of opportunities to participate in high priority developmental projects that are sponsored by the MDBs and/or other donors may prove instrumental in encouraging export credit agencies to make full use of their credit extension capacity.[14]

C. Co-Financing With Commercial Banks

Commercial banks also generally have exposure limits for developing countries in which they do business. Moreover, these banks at any particular time have a fairly definite idea with regard to their desired overall exposure to developing countries as a group, and thus the foreign component of their total assets. In the short run it seems reasonable to conclude that co-financing has little if any effect on commercial banks' overall willingness to hold foreign assets, but may result in additionality for a particular country or region. In the medium to longer-term successful experience by the group of commercial banks that have undertaken co-financing operations may serve to increase their willingness to hold foreign assets. Moreover, the demonstration effects of these successful co-financings, against their relative profitability compared with domestic loans, may serve to increase the number of commercial banks, and encourage other private market sources to enter into such arrangements. The potential for increased financial flows as a result of co-financing operations, however, remains an area where views continue to differ. Aside from the issue of additionality, co-financing between official aid sources and private banks, gives lenders an assurance that loan proceeds are being used for priority investment purposes, and the availability of the economic analysis of official aid agencies may help private lenders to develop a broader and longer term perspective on specific country economic prospects and assist borrowers overcome unwarranted caution. This may be particularly helpful in encouraging commercial banks to maintain their exposure during periods in which developing countries face short to medium-term liquidity problems. Moreover, the participation of private funds in sizeable co-financing undertakings may serve to enhance the influence of official aid agencies with regard to the economic policies of the recipient government.

IV. Co-Financing and A.I.D.'s Private Sector Initiative

A. Background

A major positive aspect of co-financing from A.I.D.'s view is its potential for increasing the involvement of the foreign private sector in the development process of LDCs. However, except for a project in 1982, in which it participated in parallel form with the International Finance Corporation (IFC) and a private French bank in a leasing project in Peru, A.I.D. has not in recent years entered into any direct co-financing arrangements in which there were foreign private sector providers of risk-bearing loan funds.[15]. To be sure, prior to the Congressional transfer of its authority to issue loan guarantees and provide political

[14] As noted earlier, co-financing which involves export credits or government guaranteed private credits and ODA in a single transaction are considered mixed credits. The joint A.I.D./State policy on mixed credits is set forth in A.I.D. Policy Determination Number 2 (new series).

[15] A.I.D. has used the co-financing approach indirectly to support private sector activities. For example A.I.D.'s loans to LAAD, Bladex and BANEX have generally been conditioned upon their obtaining a specific amount of financing from other sources. A.I.D. has also since the establishment of the Bureau of Private Enterprise made direct loans to indigenous private sector firms, for example to the Siam Commercial Bank in Thailand (for on-lending to Thai-owned small and medium sized agribusinesses) and the Kenya Commercial Bank (for on-lending with the equivalent of its funds to the Kenyan-owned small and medium sized enterprises in the agribusiness sector or in the manufacturing sector in rural areas. These loans, however, cannot be classified as co-financings as defined in this paper because no other external source of funds participated.

risk insurance to OPIC in 1969, the Agency was instrumental in putting together investment packages that had substantial private sector participation. For example, the Phillips Fertilier project in Brazil in 1966 involved loan capital from six private U.S. insurance companies, a direct A.I.D. loan to the Government of Brazil, and equity investment by the Phillips Petroleum Company. When OPIC began its actual operation on January 19, 1971 it inherited from A.I.D. a $169.7 million portfolio of outstanding loan guarantees. It also took over $8.4 billion of political risk insurance that had been issued in support of equity investment made by U.S. companies in developing countries.

The legislation (Public Law 91-175) that established OPIC placed upon that organization primary official responsibility for mobilizing and facilitating the participation of U.S. private capital and skills in the economic and social development of less developed friendly countries. Not only did OPIC inherit A.I.D.'s loan guarantees and political risk insurance portfolios, it also took along key personnel, leaving A.I.D. with little private sector experience and capacity. Until recently, even that diminished capacity had further declined through retirements and other departures from A.I.D. in the ensuing years.

The Bureau of Private Enterprise (PRE) was established within A.I.D. in response to the Reagan Administrations's belief that a vigorous private sector economy can serve as a substantial force for growth in the developing countries. This Bureau, in conjunction with the Regional Bureaus, is expected to play an important role in developing specific programs and projects that are designed to bring about an enhanced private sector role in the developing process of certain designated developing countries. In attempting to achieve this objective, PRE is exploring, among other things, possible participation in co-financed loans to indigenous private sector firms that include external private sector lenders for projects that satisfy Agency priorities and development criteria. While such participations would result in leveraging of Agency resources, they will require careful analysis of country as well as borrower creditworthiness.

For A.I.D.'s private sector initiative to have the fullest impact, the Regional Bureaus and field missions are expected to aggressively seek out opportunities to utilize the private sector in their development programs. In this context, all proposed projects should be intensively reviewed for possible co-financing opportunities, particularly those that envision the provision of substantial resources to intermediate credit institutions,[16] as well as projects that involve large infrastructure investment.[17] Moreover, there should be continuous alertness to opportunities to design and implement projects and programs which will stimulate local private enterprise and encourage entrepreneurial risk-taking. However, when such potential co-financing arrangements involve the financing of foreign trade goods and services they must structure in a manner that is consistent with A.I.D.'s policy on mixed credits, U.S. trade policy in general, and more specifically its obligations under the OECD Guidelines for Officially Supported Export Credits (Arrangement).

B. The OECD Arrangement

The Arrangement is an informal agreement applicable to participants, including the United States, with regard to officially supported export credits with a repayment term of two years or more, regardless of whether they relate to contracts for sale of goods and services, or to leases equivalent in effect to such contracts, or to pure service contracts. The major medium and long term goals of the Arrangement are the reduction and eventual elimination of trade-distorting export credit subsidies and thereby lessen the prospects for trade wars, as well as the promotion of international trade on the basis of price competition and quality considerations. The Arrangement applies strictly to independent transactions, and the independence of one transaction from another is determined on a legal rather than an "in fact basis".[18] Official export credits for military equipment, agricultural

[16] The provision of resources to intermediate credit institutions offers opportunities to attract the participation of private external lenders in co-financing arrangements that could, in time, permit A.I.D. to withdraw as a source of funds. Moreover, the use of indigenous privately owned financial intermediaries can strengthen and enhance the role of the private sector in the development process.

[17] Large infrastructure projects may offer opportunities, given appropriate design, to generate private sector undertakings that might be attractive for co-financing participation by external lenders and/or firms.

[18] For example, in an electric power plant project in Egypt, A.I.D. financed one generator on its regular concessional terms and Exim Bank another on its near market terms in separate transactions. The two transactions were in fact linked. Association or linkage "in fact" is determined on the basis of consideration to such factors as (i) the existence of informal understandings between the recipient and the donor authority, (ii) the intention of the donor through ODA to facilitate the acceptability of a financing package, (iii) the effective tying of the whole financing package to procurement in the donor country, (iv) the tying status of ODA and the modality of tender and/or of the contract of such financing transaction.

commodities, aircraft, nuclear power plants, and certain ships are exempt, however, from the provisions of the Arrangement.

Specifically, the Arrangement sets forth minimum interest rates and maximum repayment terms, and other loan features that participants agree to adhere to. For purposes of minimum interest and maximum repayment terms countries are separated into three respective groups. Countries with GNP per capita greater than $4,000 (1979 dollars) are classified as relatively rich (Category I). Countries eligible for IDA or IBRD/IDA credits or on the UN list of "least developed countries" are classified as relatively poor (Category III). All other countries are classified as intermediate (Category II). Respective applicable Arrangement minimum interest rates and maximum repayment terms are set forth in the table below.[19]

Present Conforming Arrangement Minimum Interest Rates and Maximum Repayment Terms

Classification of Country	Repayment Maximum Terms (Years) 2-5	Over 5-8.5	Over 8.5-10
I. Relatively Rich	12.15%	12.40%	n/a
II. Intermediate	10.85	11.35	n/a*
III. Relatively Rich	10.00	10.00	10.00

*Countries newly moved to this Category as of July 6, 1982 may continue to receive a maximum repayment term of 10 years.

The Arrangement also governs other elements of permissable loan features. A cash down payment of not less than 15 percent of the export contract value is required. This has the effect of limiting to 85 percent the proportion of a transaction that can be financed. Moreover, the principal of an official export credit shall normally be repayable in equal and regular installments of not less frequently than every six months, with a grace period of not longer than six months. Interest cannot be capitalized. Financing to cover local costs which are necessary either for executing the exporter's contract or for completing the project of which the exporter's contract forms part cannot exceed the cash payment, or carry interest rates or repayment terms more favorable than those for the export to which such local costs are related.

Participants in the Arrangement can of course derogate from its provisions, but when doing so there is an obligation to notify other participants at least 10 calendar days before making a commitment that involves:

1. Support of a tied aid credit[20] with a grant element of less than 25 percent.

2. Support of non-conforming payment practices with respect to principal or interest.

Other derogations must be reported after the fact—that is after a commitment has been made. The significance of the Arrangement's prior notification requirement is that it gives other participants the opportunity to match the non-conforming offer, and in this manner discourage the use of export credit subsidies as an unfair trade promotion mechanism.

C. **Joint and Parallel Financing**

Under the provisions of the Arrangement A.I.D. can participate in co-financing operations that include external private sector resources that take the form of joint financing. However, within the context of its own policy, and U.S. trade policy as well, it can do so only in cases in which its loan carries terms that are not more concessional than provided for under the Arrangement. Specifically, A.I.D.'s PD-2, new series, allows the "combining" of A.I.D. resources, that are made available on concessional terms, with those from private sources in a single transaction only in cases in which an otherwise low and responsive U.S. exporter stands to lose a sale due to unfair financing offered in support of a non-U.S. exporter. Moreover, it would be inconsistent with broad U.S. trade policy for A.I.D. to initiate a mixed credit in the form of joint financing.

As a result of the use of a legal basis to determine the independence of one transaction from another, A.I.D. can initiate parallel financing undertakings with external private sources of funds in which its credit carries Arrangement conforming or non-conforming terms. Even so, A.I.D. cannot provide a credit with a grant element of less than 20 percent.[21]

[19] These financial terms are subject to regular periodic review and change by Arrangement participants. A more detailed discussion of relevant provisions of the Arrangement is included as Annex A.

[20] Participants have agreed not to provide tied aid credits with a grant element of less than 20 percent. A tied aid credit is a credit which is provided for development aid purposes and which is financed either exclusively from public funds or as a mixed credit, partly from public and partly from private funds.

[21] The grant element is that percentage of the face value of a loan which in economic reality represents a grant of assistance. The grant element of a loan is determined by (a) computing the discounted present value of its stream of repayments (principal plus interest) using the OECD/DAC discount rate of 10 percent, (b) subtracting the value computed in (a) from the face value of the loan, and (c) dividing the value found in (b) by the face value of the loan (this result is multiplied by 100 to change from a decimal to percent basis).

To do so would violate the no-derogation provision in the Arrangement, which the USG strongly supports.[22] Moreover, if A.I.D. planned to provide a credit with a grant element of at least 20 percent but less than 25 percent it would be necessary to provide a 10 calendar day notification to other Arrangement participants before making a commitment. This would provide them an opportunity to match the credit, exactly (term for term), or with other support. Of course, until the whole prior notification procedure is worked through, A.I.D. could not be sure of the project, since other participants may match and be chosen, and it may have already made considerable investment in preparing a project. On the other hand, if the grant element is 25 percent or higher prior, notification would not be required, other participants would not have an opportunity to match, and A.I.D. could be assured of the project.

D. Implementation

Among the elements that missions should consider in identifying co-financing opportunities with private sources of funds, aside from A.I.D.'s regular requirements, are (a) the regulatory climate in respective developing countries for private business, (b) the economic policy framework, (c) the potential contribution to achievement of A.I.D. country specific development objectives, (d) projected financial profitability of the potential project, and (e) the creditworthiness of potential private sector participants for commercial loans and their capacity to provide the required managerial, technical, and financial participation to implement and maintain the flow of economic benefits that justify A.I.D.'s participation in a specific project and/or activity.

To assist Missions in this process, the Administrator has established a co-financing working group to review Mission capital projects at the pre-PID or PID stage for possible co-financing with private sector sources of funds. Missions are encouraged through their respective Bureaus to utilize the expertise of this group for assistance in identifying and evaluating potential private co-financings, as well as in the design and financial packaging of specific projects.

Even with a concerted effort to identify A.I.D. activities amenable to co-financing with external private sector lenders the amount of A.I.D. resources utilized for such co-financing arrangements will probably be modest over the next several years. For most of the low income developing countries in which A.I.D. operates, the market's perception of their creditworthiness sharply limits their access to private risk bearing external medium to long-term credit. From the market's perception it appears reasonable to expect that most co-financings that involved private sector loans over the next several years will continue to be concentrated on the middle to higher income countries.[23]

V. Policy Issues

A. Source/Origin Procurement Requirements

As noted above, A.I.D.'s source/origin requirements, unless waivers are used, can limit its participation in co-financing arrangements that take the form of joint financing. One possible approach to this problem could be the adoption of a liberal policy on waivers and/or a general exemption of co-financing arrangements from these requirements. On the other hand, there does not appear to have been any actual cases in which these requirements have proved insurmountable preventing A.I.D. participation in projects it considered of high priority. It could thus appear to be premature, aside from the changes associated with the use of PRE's revolving fund transactions now under Congressional consideration, to seek legislative changes in procurement provisions or a general liberalization of procurement policy with respect to co-financing. Moreover, any attempt to gain legislative changes would have to take account of other bilateral donors' policies on tied aid. Considerable discussion has taken place in the OECD/DAC over the years on aid untying but no consensus acceptable to the U.S. has emerged. Thus, until greater experience with co-financing is obtained, procurement issues should be considered on a case-by-case basis in close consultation with appropriate A.I.D. officials.

[22] In addition, the Development Assistance Committee of the OECD (OECD/DAC), of which the U.S. is a member, recently adopted a set of Guiding Principles for the Use of Aid in Association with Export Credits and Other Market Funds. OECD/DAC members agreed to refrain from providing associated financing, in which there is an ODA component, with a combined grant element of below 20%. There are, however, no prior reporting requirements with respect to members' derogations. Moreover, for purposes of computing the grant element only officially-supported export credits, ODA, and other official flows are included. The grant element of officially-supported export credits is considered to be zero for this purpose.

[23] In the present world economic environment, in which an increasing number of LDCs have had to seek rescheduling of their debt service payments, private lenders have become very cautious about continued lending to developing countries, especially those that already have large amounts of debt outstanding and debt service payments to private lenders.

B. **Direct Private Sector Lending**

As noted above, PRE intends to continue and in appropriate circumstances to expand its program of direct loans to indigenous private sector firms, singular and/or within the framework of a co-financing arrangement in which external private lenders participate. Such operations have and will continue to require some modifications in A.I.D.'s term loan assessment policy.

On Government-to-Government loans, creditworthiness analysis is basically limited to an assessment of the overall capacity of the borrowing government to meet its overall external contractual repayment obligations.[24] This fundamentally entails a review of the borrowing country's economic/financial management and policies, the outlook for economic growth, and its balance of payments prospects. A.I.D.'s attention to this aspect of its lending has tended to focus on the long-term and has generally glossed over the medium-term.

Direct loans to private sector firms, unlike Government-to-Government loans, will entail a currency convertibility risk whether the project financed does or does not earn foreign exchange. Such lending, in addition to a careful creditworthiness analysis of the private borrower, will require a more careful assessment of a country's balance of payments prospects over the medium-term. This need arises because these direct loans usually will not carry long grace periods and will require foreign exchange repayments within a few years, in contrast to the 10 year grace period often associated with most A.I.D. loans. Even a highly successful investment, in terms of earnings in local currency, may be unable to meet external repayments if the country has inadequate foreign exchange to allow convertibility. Moreover, the situation may not be materially changed if the project earns foreign exchange, since most LDCs require the surrender to the Government of such export earnings. To minimize problems associated with currency convertibility, each direct indigenous private sector loan approval paper should explicitly assess the currency convertibility risk over the medium-term. Moreover, such papers should clearly indicate the manner in which A.I.D.'s audit rights as set forth in A.I.D. Handbook 1, Supplement B, Section 24B are provided for.

[24] Within the context of country creditworthiness, the selection of projects financed is based upon an analysis of the economic benefits of each project, against the background of mutually agreed development priorities and objectives.

VI. Conclusions

Co-financing is a useful method of development finance. However its relevance to missions will vary depending upon their respective country development strategies and resource availabilities. Co-financing offers the potential for increasing the effectiveness of A.I.D.'s resources by broadening the scope of investment opportunities beyond those that are within its singular capacity. This potential advantage could prove to be valuable to all A.I.D. missions, particularly those whose resource availabilities preclude direct A.I.D. funding of important development projects or programs. For such missions, co-financing may be especially useful as a means of becoming associated with and having influence on higher benefit yielding projects than its resources in singular application would afford. In certain cases this technique of aid coordination may also provide an opportunity to maintain an A.I.D. presence without a small field mission, especially in those cases in which another bilateral donor has a permanent presence and has a coinciding development program emphasis. Nevertheless, these potential advantages, particularly in cases in which A.I.D. provides a minor share of overall project cost, must be assessed against the background of possible loss of influence over the planning and implementation of the overall activity. It will also be necessary to exercise particular care against the loss of necessary control in instances in which A.I.D.'s participation takes the form of providing financing for technical advisors supplied by other co-financing participants. A.I.D.'s experience in such instances includes cases in which it was difficult to provide appropriate direction to such advisors, and where as a result tension developed between A.I.D. and the advisors' parent organizations.

Co-financing may also be used to leverage A.I.D. resources with those of the external private sector, as well as to facilitate the transfer of skills and technology. This may, in turn, enhance the role of the private sector in the economic and social development of less developed countries. Moreover, A.I.D.'s overseas in-country presence and its capacity to provide technical assistance, both direct and through the employment of contractors, places it in a favorable position to participate in substantial co-financing arrangements with modest resource inputs. Missions are thus encouraged to identify and consider such undertakings with the external private sector in appropriate circumstances. The expertise of the A.I.D. co-financing working group is available to provide advice and other assistance to Missions in this regard, as well as for co-financing arrangements involving indigenous private sources of funds.

Direct loans to private sector firms in developing countries may be constrained by A.I.D. source/origin procurement requirements, but in any case will entail risks that are not present in A.I.D.'s usual government-to-government lending. Such lending will require careful assessment. Moreover, particular attention will have to be given to ensuring that A.I.D. does not become involved in the financing of mixed credits in a manner that would contravene the purposes of A.I.D./State policy on mixed credit financing, and inconsistent with U.S. obligations as a participant in the OECD Export Credit Arrangement.

Aside from possible advantages in the physical application of development assistance resources, co-financing also offers the potential for enhancing the effectiveness of A.I.D.'s policy dialogue with the respective LDCs and other project participants. Moreover, the skillful use of co-financing may enable A.I.D. to influence directly and indirectly the allocation of resources of other lenders, both official and private, as to country and/or sector of application. For example, A.I.D. can design projects, for sectors and/or in countries to which it accords great importance, that have a high probability of attracting other co-lenders. This approach might be particularly attractive to the Arab Funds, that have demonstrated a receptiveness to participate in co-financing, but often are not in a position to take the initiative due to their limited field presence and technical capacity. In addition, A.I.D.'s project selection and design procedures can be modified to encourage indigenous private sector participation that may immediately or over time be conducive to the participation of private foreign lenders in co-financing arrangements.

To more fully explore co-financing opportunities with the regional MDBs, other bilateral donors, and the private sector, A.I.D. is reviewing its planning and programming procedures to ascertain how they might be modified to include a more systematic consideration of the use of the co-financing mechanism as an integral part of its development strategy. It is quite possible that a systematic approach to co-financing with these groups could serve to enhance the effectiveness of A.I.D.'s resource flows. The specific focus of this effort will be the establishment of regular information exchanges with the MDBs and other bilateral donors with respect to A.I.D.'s interests and projects. More complete information exchanges will permit A.I.D. in the planning and design of projects to take into account from the outset the interests of and the prospects for the participation of regional MDBs and other bilateral donors. Moreover, Missions should undertake an assessment of their capacity to identify and evaluate co-financing opportunities, particularly with private sources of funds. On the basis of such assessments respective appropriate Washington regional bureaus should be informed of assistance needs and their feasibility with regard to addressing inadequacies.

Although co-financing has a number of potential advantages, particular care should be exercised to insure that co-financing does not become an end itself, but rather remains a mechanism among other alternatives to be utilized when it represents the most efficient application of A.I.D. resources in the context of the development objectives of country specific strategies.

ANNEX A
Select Provisions of The OECD Export Credit Arrangement

The OECD guidelines (Arrangement) for officially supported export credits is a gentleman's agreement applicable to participants with regard to officially supported export credits with a repayment term of two years or more, regardless of whether they relate to contracts for sale of goods and services, or to leases equivalent in effect to such contracts, or to pure service contracts. The major purpose of the Arrangement is essentially, through the standardization trade subsidies provided through financing, to remove tensions that could lead to trade wars, and in this context the promotion of international trade on the basis of price competition and quality considerations. The Arrangement applies strictly to independent transactions, and the independence of one transaction for another is determined on a legal rather than an "in fact basis". Official export credits for military equipment, agricultural commodities, aircraft, nuclear power plants, and certain ships are exempt, however, from the provisions of the Arrangement.

Specifically, the Arrangement sets forth minimum interest rates and maximum repayment terms, and other financial features that participants agree to adhere to. It also includes procedures that participants agree to follow if they elect to derogate from its financial terms and features. Some of the more important elements of the Arrangement, particularly those that relate to tied aid credits and that have a bearing on co-financing are set forth and dicussed below.

Arrangement Financing Norms

Cash Payment: Not less than 15 percent of the export contract value to be paid at or before the starting point.

Definition of Starting Point

(i) In the case of a contract for the sale of capital goods consisting of individual items usable in themselves (e.g., locomotives), the starting point is the mean date or actual date when the buyer takes physical possession of the goods in his own country.

(ii) In the case of a contract for the sale of capital equipment, equipment for complete plant, or factories where the supplier has no responsibility for commissioning, the starting point is the date when the buyer is to take physical possession of the entire equipment (excluding spare parts) supplied under the contract.

(iii) In the case of construction contracts where the contractor has no responsibility for commissioning, the starting point is the date when construction has been completed.

(iv) In the case of any contract where the supplier or contractor has a contractual responsibility for commissioning, the starting point is the date when he has completed installation or construction and preliminary tests to ensure that it is ready for operation. This applies whether or not it is handed over to the buyer at that time in accordance with the terms of the contract and irrespective of any continuing commitment which the supplier or contractor may have, e.g., for guaranteeing its effective functioning or for training local personnel.

(v) In the case of paragraphs (ii), (iii) and (iv) above where the contract involves the separate execution of individual parts of a project, the date of the starting point is the date of the starting point for each separate part, or the mean date of those starting points or, where the supplier has a contract, not for the whole project but for an essential part of it, the starting point may be that appropriate to the project as a whole.

Maximum Repayment Terms: Repayment terms are according to country classification. Category I countries are those with GNP per capital of over $4,000, measured in 1979 dollars as shown in the 1981 World Bank Atlas. Category II countries consist of those not classified in I or III. Category III consists of IDA eligible countries.

Category I Countries: 8-½ years. However, if repayment term exceeds 5 years prior notification to other Arrangement participants of not less than 10 calendar days is required before a commitment can be made.

Category II Countries: 8-½ years. However, for countries newly moved to this classification as of July 6, 1982 the maximum repayment term is 10 years.

Special Provisions.

Conventional Power Plants. The terms listed above for countries by categories apply except that the maximum repayment term may be 12 years. If a participant intends to support a repayment term longer than 5 years for relative rich countries and longer than the relevant maximum set forth above for other countries (8-½ and 10 years) the participant is required to give prior notification to other participants of not less than 10 calendar days before making a commitment.

Ground Satellite Communications Stations. The terms listed for countries by categories apply, except that the maximum repayment term to any country may not exceed 8 years.

Grace Period and Repayment Method: Principal of an official export credit shall normally be repayable in equal and regular installments of not less frequently than every six months after the starting point. Prior notification of 10 calendar days is required to other participants before making a commitment if these normal terms are not to be followed.

Minimum Interest Rates:
Present Conforming Arrangement Minimum Interest Rates and Maximum Repayment Terms

Classification of Country	Repayment Maximum Terms (Years) 2-5	Over 5-8.5	Over 8.5-10
I. Relatively Rich	12.15%	12.40%	n/a
II. Intermediate	10.85	11.35	n/a
III. Relatively Poor	10.00	10.00	10.00

A. If U. S. commercial lending rate on dollar loans fails below the minimums above, a U. S. official export credit can be extended at the commercial lending rate plus .3 percentage points per annum.

B. Interest is not to be capitalized during the payment period and shall be payable not less frequently than every six months after the starting point. Prior notification to other participants of at least 10 calandar days is required if normal procedures are not be followed.

Local Costs: Expenditures for the supply from the buyer's country of goods and services (not including commissions payable to the exporter's agent in the buyer's country) which are necessary either for executing the exporter's contract or for completing the project of which the exporter's contract forms part. Exported goods and services include goods and services supplied by third countries.

Category II and III Countries: The amount of local cost supported on credit terms will not exceed the cash payments. Such support, if in the same currency as that of the export credit, cannot carry interest rates or repayment terms more favorable than those supported for the exports to which such local costs are related.

Category I Countries: Same as for Category II and III countries, except that support will be confined to insurance or guarantees.

Tied Aid Credits: A credit which is provided for development aid purposes and which is financed either exclusively from public funds or as a mixed credit, partly from public and partly from private funds.

A. Participants agree not to support tied aid credits with a grant element of less than 20 pecent.

B. If participants intend to support tied aid credits with a grant element of at least 20 percent but less than 25 percent they are required to give prior notification of at least 10 calendar days to othe participants before making a commitment. Other participants then have the right to match, exact (term for term), or with other support under appropriate notification procedures.

Calculation of Grant Element: The grant element of the ODA or concessional portion is calculated in accordance with the method adopted by the Development Assistance Committee of the OECD and the grant element of the export credit portion is considered zero. The grant element of a tied aid credit is determined by dividing (1) the sum of the results obtained by multiplying the face value of each credit comprising the tied aid credit by the respective grant element of each credit by (2) the aggregate face value of the credits. The grant element of the export credit portion of a tied aid credit is considered to be zero for purposes of the Arrangement.

Procedures

All reporting requirements will be handled by respective Washington A.I.D. Bureaus in coordination with Exim Bank. Missions should understand how the procedures operate in order to take them into account in their project planning and the importance of providing their respective Bureaus timely and complete information.

(a) Derogations: Procedure for Prior Notification and Discussion

(1) Notification and Discussion: If a Participant intends to take the initiative to support terms not in conformity with the Arrangement or to support a tied aid credit having a grant element of less than 15 percent, the Participant will notify all other Participants of the terms it intends to support at least ten calendar days before issuing any commitment. If any other Participant requests a discussion during this period, the initiating Participant will delay an additional ten calendar days before issuing any commitment on such terms. Normally this discussion shal be telex. In extreme cases face to face discussion may be requested and would be arranged, preferably in the country intending to derogate. If the initiating Participant moderates or withdraws its intention to support non-conforming terms, it must immediately inform all other Participants accordingly.

(2) Match (identical or by other support): On and after the expiry of the first ten day period referred to above if no discussion is requested (or on and after the expiry of the second ten day period if discussion is requested) and u:less the matching Participant has received notice from the initiating Participant that the latte has withdrawn its intention to support non-conforming terms, any Participant shall have the right to support:

(i) With respect to identical matching, terms which include the identical non-conforming element but which otherwise conform to the guidelines provided that the matching Participant notifies, as early as possible, its intention to do so; or

(ii) With respect to other support prompted by the initial derogation, any other non-conforming element of the terms, provided that the responding Participant introduces a fresh derogation, initiating a five calendar day prior notification and five calendar day discussion procedure and awaits its completion. This period can run concurrently with that of the prior notification and discussion procedure initiated by the derogating Participant, but cannot elapse before the end of the ten or twenty days period referred to under Paragraph (a)(1) above.

(3) Terms Offered by a Non-Participant: The Participant which intends to meet non-conforming terms offered by a non-Participant will follow the prior notification and discussion procedure under (1) and (2) above. Before considering meeting non-conforming terms, the Participant shall make every effort to verify the non-conforming terms are receiving official support. The Participant shall inform all othe Participants of the nature and outcome of these efforts.

(4) Information on Commitment: As soon as a Participant commits itself to support non-conforming terms, it must in all cases immediately inform all other Participants accordingly.

(b) Procedure for Prior Notification without Discussion

(1) Notification: A Participant will notify all other Participants of the terms it intends to support at least ten calendar days before issuing any commitment, if the Participant intends:

(i) to support a credit with a repayment term of "over 5 to 8.5 years" to a relatively rich country, or

(ii) not to follow normal payment practices with respect to principal or interest, or

(iii) to support a tied aid credit having a grant element of 15 percent or more but less than 25 percent, or

(iv) to support credit conditions for any type of ships to which the existing OECD Understanding applies, which would be more favourable than those credit conditions permitted by this Arrangement.

(2) If the initiating Participant moderates or withdraws its intention to give support, it must immediately inform all other Participants accordingly.

(3) Matching (identical or by other support): On and after the expiry of the ten day period referred to above and unless the matching Participant has received notice from the initiating Participant that the latter has withdrawn its intention to support terms referred to in Paragraph (b)(1) above, any Participant shall have the right to support:

(i) With respect to identical matching, terms which include the identical element referred to in Paragraph (b)(1) above but which otherwise conform to the guidelines provided that the matching Participant notifies, as early as possible, its intention to do so; or

(ii) with respect to other support, any other element of the terms which does not conform to the guidelines, provided that the responding Participant initiates a five calendar pariod notification procedure without discussing and awaits it completion. This period can run concurrently with that of the prior notification procedure started by the initiating Participant, but cannot elapse before the end of the ten day period referred to under Paragraph (b)(1) above.

(4) Information on Commitment: As soon as a Participant commits itself, it must in all cases immediately inform all other Participants accordingly.

(c) Prompt Notification Procedure

(1) Notification: As soon as a Participant commits itself to support a tied aid credit having a grant element of 25 percent or more, the Participant must notify all other Participants accordingly.

(2) Matching: No prior notification need be given if a Participant supports terms to match a tied aid credit with a grant element of 25 percent or more.

(3) Information on Commitment: As soon as a Participant commits itself, it must in all cases immediately inform all other Participants accordingly.

STANDARD FOR NOTIFYING PRIOR COMMITMENTS FOR INDIVIDUAL TRANSACTIONS

Points to be covered in each and every notification:

1. Name of authority/agency responsible under the Arrangement for making notifications.

2. Reference number.

3. "We are notifying in accordance with the provisions of Paragraph 6(a) the following transaction for which the credit terms are not in conformity with the guidelines as modified with the effect of ...."

4. Not applicable.

5. Country of buyer/borrower.

6. Name and location of buyer/borrower

7. Nature of project/goods to be exported; location of project.

8. Value of project or contract: both total value and value of exporter's national share(*).

9. (If relevant) specify any minimum contract value(*).

Category	I:	up to	600,000	SDR's	
Category	II:	from	600,000	to	1,000,000 SDR's
Category	III:	from	1,000,000	to	2,000,000 SDR's
Category	IV:	from	2,000,000	to	3,000,000 SDR's
Category	V.	from	3,000,000	to	5,000,000 SDR's
Category	VI:	from	5,000,000	to	7,000,000 SDR's
Category	VII:	from	7,000,000	to	10,000,000 SDR's
Category	VIII:	from	10,000,000	to	20,000,000 SDR's
Category	IX:	from	20,000,000	to	40,000,000 SDR's
Category	X:	exceeding	40,000,000	SDR's	

10. Credit terms which 1. intends to support:

(a) cash payments;

(b) repayment term (including starting point of credit, frequency of installments for repaying principal amount of credit, and whether these installments will be equal in amount);

(c) interest rate;

(d) support for local costs (including the total amount of local costs expressed as a percentage of the total value of goods and services exported, the terms of repayment, and the nature of the support to be given).

11. Dates concerning the prior commitment:

(a) Date on which this prior commitment was made.

(b) Date of expiry of this prior commitment.

12. Any other relevant information (including references to related cases).

(*) Values shall be stated in terms of value ratings in accordance with the following scale in Special Drawing Rights (SDR's):