Statement of

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Regarding Reauthorization of the Export-Import Bank of the United States

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The Small Business Exporters Association of the United States™

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Representatives Price and Maloney, members of the Subcommittee, good afternoon, and thank you for inviting me to appear here today. I am James Morrison, the President of the Small Business Exporters Association of the United States. SBEA is the nation's oldest and largest association of small and mid-sized exporting companies. We also serve as the international trade council for the National Small Business Association, the oldest nonprofit advocacy organization for small business. SBEA represents more than 22,000 NSBA member companies that export.

<u>We are here today to express our support for the important work that the Export-Import Bank of the United States is doing, and to strongly urge Congress to reauthorize the Bank</u>.

Exports are good for our country.

- Companies that began trading internationally between 1993 and 2001 had about *five times the employment growth* of other companies, a recent study has shown. Companies that stopped trading during this period actually *lost* jobs.[1]

- Export-related jobs also pay more – 15-20% more, on average, than similar jobs in non-exporting companies, according to Commerce Department statistics.

- Each $1 billion in exports generates an average of over 14,000 of these higher-paying U.S. jobs.

But exporting is highly competitive. Companies all over the globe are hunting for good export sales opportunities.

And their governments are backing them up.

Every major trading nation in the world has an "export credit agency" like Ex-Im Bank, and most use their ECA's aggressively.

[1] *Importers, Exporters and Multinationals: A Portrait of Firms in the U.S. That Trade Goods*, Andrew B. Bernard, J. Bradford Jensen, Peter K. Schott, National Bureau of Economic Research, NBER Working Paper 11404, June 2005, pp. 4-5.

Casual observers often attribute this to an affinity for government intervention by some companies and countries. And there is a grain of truth to this.

But the underlying and more important reason is *risk*.

Trade finance, which is necessary when foreign buyers can't or won't pay cash for their orders, inevitably involves foreign risk.

Sometimes that risk can be mitigated. For example, when an exporter borrows money to expand an operation so as to fill a foreign order, the exporter can pledge assets in this country against the risk of the foreign buyer failing to pay for the order. That's called "export working capital" and Ex-Im (and SBA) do quite a few of these transactions.

But most of what Ex-Im and other ECA's do is *buyer* financing.

In many parts of the world, financial systems are underdeveloped or prohibitively costly. Buyers in these countries who need financing almost always ask sellers to provide them with it.

But foreign buyer financing entails a degree of foreign risk that frightens commercial bankers everywhere.

A Mental Exercise

To understand why, try to imagine yourself walking into a nearby commercial bank with a promissory note in your hand. You've just gotten the note from a customer in Peru, who wants to buy one of your tractors. The note obligates the buyer to pay you back over two years. You want to sell the note to the bank because you need the money now, and you don't want to worry about invoicing the buyer every month. So you ask the bank to buy the note.

If this were a domestic sale of your tractor, the transaction would be pretty simple. But it isn't. However polite your conversation may be, the banker's actual thoughts will go something like this: "You want *me* to take the risk on being repaid by a company in *Peru*? A company I've never heard of? Over a period of two years? When the collateral is down there? And has wheels on it? Are you *nuts*? And even if I agreed to do it because I like you, how could I explain it to the bank examiners?"

Whether it's a large company trying to sell many tractors or a small company trying to sell a few tractors, commercial banks react this way. This mind-set changes only when they can access guarantees and insurance to cover most or all of the risk.

A few private sector companies will take on certain limited forms of short-term foreign risk. But for the most part, Ex-Im and other ECA's are the only institutions in any country willing to offer commercial banks this backing. And they do so only if certain criteria are met to assure a reasonable assurance of repayment.

Smaller companies face the greatest difficulties in this area because they can't offer commercial banks a tempting *domestic* banking relationship worth millions of dollars -- in exchange for the export financing.

Bluntly put, then, this is problem: Relatively few commercial banks in the U.S. offer trade financing. Fewer still offer it to smaller American companies that need financing for small export transactions. And even fewer offer it to smaller companies that are not already long-time customers of the commercial bank. And that's even *with* Ex-Im backing.

<u>Without Ex-Im, small company access to foreign buyer financing would be effectively zero</u>.

Ex-Im is not the "bank of last resort" for smaller exporting companies in this country. It is the bank of *only* resort.

One more thing. The value of small business exports has more than quadrupled since the 1980's, and today accounts for close to 30% of the total value of U.S. exports. And this is despite the fact than less than 10% of American small companies currently export.

<u>If Congress wants to sustain *and grow* this promising small business export performance, reauthorization of the Export-Import Bank is absolutely essential.</u>

IMPROVEMENTS AT THE BANK

Like any institution, Ex-Im needs improvements and modernizations to handle changed circumstances. And the international trade context is indeed changing. Foreign ECA's, particularly those that are not parties to the OECD "rules of engagement" for export credit, are becoming an increasing force in the marketplace. The growth of global supply chains, with changing casts of suppliers in multiple countries, is making it harder to calculate "domestic content" in Ex-Im transactions. Environmental needs have become more pressing.

The Bank's customer base is also shifting. Ex-Im was born and raised in an era when nearly all of the demand for foreign buyer financing came from larger companies. That is changing.

Trade barriers are falling. So are communication and travel costs. The Internet is leveling the cost of reaching foreign customers. As the fixed costs of export transactions spiral downward, ever smaller export sales to ever larger numbers of countries are becoming profitable.

One result: smaller companies are pouring into exporting. Twenty years ago, 65,000 American small businesses exported. Today it is close to 230,000. Once in the export market, smaller companies migrate upward to larger and more complex sales, with buyer financing.

The Bank's products and processes have not always kept up the pace.

H.R. 5068

To the credit of this Committee, you have taken a very thorough and careful look at course corrections that may be needed to keep Ex-Im engaged and relevant.

H.R. 5068 is an outstanding piece of legislative craftsmanship. The bill addresses nearly all of the concerns about changes in the Bank's environment that we in the private sector and the Bank itself have noted, while balancing that against the Bank's desire to have a relatively straightforward reauthorization.

From our vantage point as small business exporters, there are many desirable aspects of the bill.

- First, the legislation wisely leaves intact the floor for Ex-Im's support for smaller exporters that was established in the last reauthorization – 20% of the Bank's total financing dollars. Ex-Im met this threshold several times in the 1990's and is perfectly capable of doing so again. The fact that the Bank has fallen short of the mandate in recent years should be an occasion to improve its small business products and processes, not one to "move the goalpost".

- Second, H.R. 5068 endorses a constructive recent innovation by the Bank – the creation of a "Small Business Committee," drawn from people across the Bank who have a personal or professional interest in its small business-related products, processes and transactions, and focused on continuous improvements in those areas.

- Third, the bill would unclog the worst and most costly bottleneck at the Bank: "medium term financing" – buyer financing with payback periods of six months to seven years. Unconscionable delays in medium term financing decisions by the Bank are costing exporters -- of all sizes -- customers, cash flows, and business reputations. H.R. 5068 calls for Ex-Im to delegate medium-term financing authority to commercial banks and brokers, as the Bank has done for other products.

Let me dwell on that last point for just a moment. Why is medium-term financing – that is, financing for terms of six months to seven years – so important?

The answer is that these are the financing terms needed by some of our country's most important "value added" exporters.

A foreign buyer who wants five hundred kilos of nails will probably pay cash for it, or seek short-term financing of two or three months.

That's fine, and the U.S. should sell all the nails it can.

But a foreign buyer seeking sophisticated U.S. medical equipment, on the other hand, will generally need several years to pay for it.

Medical equipment, like other capital equipment, is a particularly desirable export.

U.S. capital equipment exports are exceptionally valuable for several reasons:

- they usually utilizes parts and sub-units manufactured by a whole array of U.S. companies.

- they are usually bundled with service exports like training and after-sale-service.

- they help build U.S. product standards and specifications in the buyer's country, paving the way for future export sales.

- they offer the biggest and fastest "bang for the buck" in U.S. job creation.

- in the case of capital equipment exports like medical equipment, construction machinery, road building equipment, food handling equipment and the like, they help demonstrate to our neighbors that the U.S. wants to work with them in improving the health and prosperity of their societies.

One of the least-recognized facts about capital equipment exporting is the smaller U.S. companies are really good at it. (See Chart 1.) And the upside potential is huge. (See Chart 2.)

But capital equipment exports require medium-term financing, and Ex-Im needs to improve in this area. Medium term approvals at the Bank are a notorious bottleneck.

With short-term financing and working capital, the Bank delegates authority to develop the "nuts and bolts" of the transaction to a network of banks and brokers.

Not medium-term. Every deal is handcrafted at 811 Vermont Avenue. And every deal requires multiple levels of approval. So exporters – large and small – wait months or even years for the financing to be approved.

In the meantime, customers walk away, exporters' reputations get bruised and foreign competitors swoop in for the sales.

The simplest and cleanest solution to this problem is for the Bank to delegate medium-term authority – not only to its banks and brokers, but also internally to its underwriters. H.R. 5068 addresses this problem squarely for the banks and brokers. And Ex-Im has the administrative authority to delegate internally -- although it's likelier to do so if this Committee includes encouragement in the Report language on the reauthorization bill.

So thank you for addressing this; it's one of the most important reforms in the bill.

FURTHER STEPS

However, in one crucial respect, SBEA believes that the bill still needs further work.

While we have strongly favored the creation of a Division at the Bank for small and medium-sized enterprises, we believe that such an "SME Division" must exercise *authority* commensurate with its *responsibilities*.

In this respect, H.R. 5068 needs further refinement, in our opinion. The bill calls for the SME Division, in conjunction with Ex-Im's "Small Business Committee," to give *advice* to other parts of the Bank, and receive it from them, as well as to offer *business outreach* to smaller companies.

What's missing is the *authority* for the SME Division to improve the customer experience of the companies that the outreach brings in -- and the *authority to take action* on the advice the SME Division gives and receives.

The *authority* to change the Bank's products and processes for SME's, and to approve SME transactions, is crucial, in our view. Crucial not only to smaller exporters, but to Congressional oversight of the Bank.

Some have questioned whether the Bank's SME business outreach and underwriting functions should be consolidated within one Division. The concern apparently is that this would be a kind of "conflict of interest."

Two points are worth keeping in mind:

- Ex-Im did pair these two functions quite successfully in the 1990's and the early part of this decade.

- Despite its name, Ex-Im is not a bank. It is a government agency. An export credit agency, to be precise. Congress gave it the primary goal of increasing exports. Rules and practices pertaining to commercial lenders, who are in the private sector and who do not have a mandate to increase exports, are of limited value in providing a guide to how the export credit agency of the United States should be organized.

If Ex-Im believes that business outreach specialists can no longer be housed with underwriters, then the SME Division should have the underwriters and the business development specialists should be assigned elsewhere.

This would be an unfortunate step, and we do not recommend it, but what ultimately matters is the transactions themselves.

To further clarify the Division's focus, we suggest that its name be the "SME Finance Division".

As it happens, this resembles the name and structure of the "Small and Medium Enterprise Finance Department" at the Overseas Private Investment Corporation.

OPIC

OPIC's Small and Medium Enterprise Finance Department is responsible for one of the most remarkable recent success stories in the history of federal government support for SME's in international trade. In FY 2001, before the Department was created, OPIC handled $10 million in SME transactions. These grew to about $350 million in FY 2005. Yet this meteoric increase was accomplished at zero cost to American taxpayer, without the loss of a single American job, while generating profits in this country as well as economic development abroad.

How did OPIC do it? The short answer is that the agency created a structure with appropriate authority and staffed it with highly-motivated and experienced individuals.

The head of OPIC's SMEF Department, who reports directly to the agency's President, manages the agency resources, expertise and decision-making related to the small business mission. Key features of this organizational structure:

- Both the lending and credit functions are incorporated within the same Department, facilitating quick decision-making for small business applications and greatly reducing the potential for "turf" conflict between lending and credit.

- The Department head has the authority to approve without further review loans up to $10 million, which covers most small business project financing needs and avoids lengthy deliberations by committee.

- The Department's senior staff, who have considerable small business lending and credit experience in the private as well as public sectors, have trained a team of investment officers in the nuances of small business finance, which has different characteristics and risks than larger-scale project financing.

GE CAPITAL

But OPIC isn't alone. Perhaps the single most successful underwriter of SME export finance in the U.S. private sector is GE Capital. GE Capital's Corporate Lending and Business Credit Division is essentially a "sales team" including a loan originator, sales representatives and underwriters. GE Capital's SME exporter portfolio is about $31 million today, and the company has had *only two claims,* both of them nominal, in its entire history.

EDC

Abroad, the "gold standard" of export credit agencies is probably Canada's "Export Development Canada." EDC's SME Division consists of three teams:

- business development, with 28 employees
- export insurance underwriting, with 40 employees, and
- financing and bond underwriting, with 25 employees

The teams and team members work **only** on SME transactions. They are given considerable autonomy. Underwriters have delegated authority to approve transactions. Most can approve deals of under C$1 million on their own. Some can approve deals of C$5 million or more -- and transactions do not require multiple signatures.

This modest staff of fewer than 100 employees delivered more than C$15 billion in Canadian SME export financing last year, or 27% of EDC's overall total of C$57 billion. It handled export financing for 7,000 SME exporters, or one-fifth of Canada's 35,000 exporters.

By contrast, Ex-Im provided $2.7 billion in SME export financing last year, or 19.1% of its overall total of about $18 billion. It handled 2,300 SME exporters, or about 1% of the 230,000 SME exporters in the U.S.

There are important differences between the EDC and Ex-Im. EDC competes with the Canadian private sector to some degree, though this is declining. It has more employees overall than Ex-Im, and it handles some transactions that might go to OPIC or SBA here. It also handles some indirect export financing, (which Ex-Im ought to do but doesn't.) Still, for all the differences, it is worth noting that EDC delivered better overall results than Ex-Im despite the fact that the U.S. economy is about seven times as large as Canada's.

What these examples – OPIC, GE Capital and EDC -- have in common is an "SME team" handling SME transactions with a high degree of authority and autonomy.

That is exactly what is missing from H.R. 5068 at this point.

The proposed SME Division at the Bank would have no authority over Ex-Im personnel actually handling SME transactions. It could not develop credit standards. Nor could it alter the Bank's products based on customer feedback. It could offer *advice*, but those receiving the advice would be free to ignore it.

Instead, it would be heavily invested in such "PR" work as attending meetings and sending out brochures. While this kind of "input" work has its value, what matters much more right now is getting the products and processes right for the companies that do come in the door.

In the end, the Bank will be judged on output.

We therefore urge Congress to create an **SME Finance Division** at Ex-Im, headed by an individual as described on pages 3 and 4 of H.R. 5068, and with a team of underwriters and credit specialists *dedicated exclusively* to SME transactions. This Division should be given full authority to alter the Bank's SME products and processes, and to approve its SME transactions.

The **SME Finance Division** also should be held accountable for the Bank's overall SME performance.

That concludes my testimony. I would be happy to accept any questions at this time.

Chart 1

Can American business compete in selling capital equipment abroad? Can small business?

We *can* and *do*!

U.S. Capital Equipment Exports in Selected Major Categories, 2002, By Size of Exporting Business

In Billions of U.S. Dollars

NAICS Code	Description	Total receipts	SME Receipts	% SME
331	Primary metal manufactures	$14.3 billion	$4.4 billion	30.4%
332	Fabricated metal products	$15.9	$4.8	30.3%
333	Machinery manufactures	$65.5	$18.6	28.4%
334	Computers and electronic products	$133.3	$29.5	22.1%
335	Electrical equipment, appliances and parts	$19.5	$4.7	24.3%
336	Transportation equipment	$118.8	$17.5	14.7%
337	Furniture and related products	$1.6	$0.7	42%
339	Miscellaneous manufactures	$22.5	$10.0	44.6%
Totals		**$391.4**	**$90.2**	**23%**

(Sources: *2002 Economic Census* and *2002 County Business Patterns*, U.S. Census Bureau. SME's are small and mid-sized enterprises with fewer than 500 employees.)

Chart 2

Can Exports By American Small Businesses Be Increased? YES!

Examples of economic sectors where strong SME domestic performance could yield more exports -- with the help of export financing

U.S. Domestic Production, 2002, in Billions of Dollars (except as noted)

NAICS Code	Description	Total Receipts	SME Receipts	SME %
2213	Waste, Sewage & Water Systems	$8.3 billion	$4.0 billion	48%
233	Building and developing	$535	$411.4	77%
234	Heavy construction	$174.4	$119.7	69%
2358	Water well drilling	$3.2	$3.0	93%
421	Wholesale trade in durable goods	$2,332.2 (= $2.33 trillion)	$979.3	42%
441	Motor vehicle & parts dealers	$813.2	$683.5	84%
*44122**	*Motorcycle, boat and other motor vehicle dealers*	*$32.9*	*$31.0*	*94%*
4431	Electronic and appliance stores	$92.3	$37.6	41%
444	Bldg equipment, garden equipmt & supply dealers	$288.4	$146.8	51%
45393	Manufactured home dealers	$9.6	$7.2	75%
54136	Geophysical surveying and mapping services	$1.0	$ 0.785	78%
54151	Computer systems design and related services	$181.8	$93.0	51%
5416	Mgmt, scientific & technical consulting svcs	$130.8	$74.3	57%
5418	Advertising and related services	$60.4	$36.0	60%
5419	Market research & public opinion polling	$11.4	$5.5	48%
56	Administrative & support: waste management & remediation svcs	$457.4	$210.3	46%
Total		**$5.1 trillion**	**$2.8 trillion**	**55%**
Total, less 421		$2.8 trillion	$1.8 trillion	64%

Adding just 10% of these SME sales to the export market would increase U.S. SME exports by up to $280 billion annually.

(Sources: *2002 Economic Census* and *2002 County Business Patterns*, U.S. Census Bureau. SME's are small and mid-sized enterprises with fewer than 500 employees.)
* Subset of preceding (441) category, excluded from totals