

## **Investment promotion for sustainable development**

The roles of DFIs and export credit agencies

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and San Bilal

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### Key messages

Promoting trade and investment along sustainable principles is one of the means to achieve the goals of the 2030 Agenda for Sustainable Development. To this end, *what are the potential synergies between development finance institutions (DFIs) and export promotion agencies (ECAs) in promoting sustainable and responsible investments?*

DFIs and ECAs follow different institutional mandates and objectives to promote investments and exports. But they tend to engage with similar clients and in similar markets. Besides, the sustainability principles required by DFIs and those of ECAs do tend to converge. Potential for synergy and cooperation thus seems obvious.

Yet, DFI-ECA collaboration until now has been rather limited, due to various challenges that need to be overcome, relating to issues such as differing policies, approaches, operating procedures, credit and pricing parameters, tenor and currency preferences, and transaction eligibility criteria. There is a need for a better understanding of the respective business practices and priorities of DFIs and ECAs.

More systematic efforts are therefore needed to enhance the cooperation and synergy between DFIs and ECAs. This must also be steered by policy-makers, so as to foster a more conducive institutional and policy environment and provide the right incentives for each institution to cooperate, building on their respective comparative advantages, towards enhanced sustainability.

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## Acronyms

AAAA	Addis Ababa Action Agenda
ADB	Asian Development Bank
AfDB	African Development Bank
COFACE	Compagnie française d'Assurance pour le commerce extérieur
CSO	Civil society organisation
DD	Belgian Delcredere   Ducreire
DFI	Development finance institutions
DG GROW	Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs
DGGF	Dutch Good Growth Fund
EBRD	European Bank for Reconstruction and Development
ECA	Export credit agency
ECDPM	European Centre for Development Policy Management
EDF	European Development Fund
EDFI	European Development Finance Institutions
EFSI	European Fund for Strategic Investments
EIB	European Investment Bank
EIP	European Investment Plan
EITI	Extractive Industries Transparency Initiative
ESG	Environment, Social Matters and Governance
EU	European Union
EUBEC	EU Platform for Blending in External Cooperation
FDI	Foreign direct investment
GVC	Global value chain
IDB	Inter-American Development Bank
IFC	International Finance Corporation
IFI	International financial institution
IMF	International Monetary Fund
IPA	(Inward) Investment Promotion Agency
ITUC	International Trade Union Confederation
LDCs	Least-developed countries
MDBs	Multilateral development banks

MIGA	Multilateral Investment Guarantee Agency
MNEs	Multinational enterprises
NGO	Non-governmental organisation
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OIA	Outward Investment Agency
OPIC	Overseas Private Investment Corporation
PCS	Preferred creditor status
PRI	Principles for Responsible Investment
PS	Performance standards
RVO	Netherlands Enterprise Agency
SDGs	Sustainable Development Goals
SMEs	Small- and medium-sized enterprises
UKEF	UK Export Finance
UN	United Nations
UNGP	UN Guiding Principles
WTO	World Trade Organization

## Executive Summary

In recent years and in the aftermath of the world financial crisis, economic slowdown in Europe has encouraged European governments and the European Union (EU) to set up support programmes and instruments that can stimulate national economies and help create the jobs needed to tackle both (youth) unemployment and crumbling growth rates. By providing access to (trade) finance and mitigating risk, the ambition is to help enterprises to expand and grow internationally, as “foreign exposure by these companies can increase enterprise competitiveness, provide access to foreign markets and resources, create new opportunities for exports, and generate profits” (UNCTAD, 2015).

At the same time, the United Nations’ 2030 Agenda for Sustainable Development urges all countries to integrate sustainability and development ambitions. To do so, governments increasingly rely on engaging the private sector for development by providing public support instruments designed to trigger sustainable investments:

- In the context of development cooperation, European governments and institutions increasingly rely on using scarce public resources to attract private capital and investments to scale up the available capital in support of the implementation of the Sustainable Development Goals (SDGs). By mitigating commercial, political or any other form of risk, aid can be strategically used to attract loans or equity from other public or private financiers, such as development finance institutions (DFIs), whose relative significance is increasing while being a growing source of development funding.
- Additionally, EU member states have commercially-oriented investment and trade promotion agencies, such as export credit agencies (ECAs), which offer trade credits and mitigate risks by providing guarantees, relevant information and business contacts. Those agencies thereby help domestic companies to boost economic activity and increase foreign direct investment (FDI) flows to countries, including those where there is more (perceived) risk and therefore less supply of investments, needed for local businesses to prosper.

While both sets of instruments are different in terms of underlying objectives, institutional setting and sources of public resources, opportunities to find greater synergies in investment promotion between development cooperation and more commercially-oriented public support instruments are manifold. These should be seized to contribute to the goal of universal sustainable development through promoting investment that is both sustainable and responsible, regardless of the underlying objectives.

This paper therefore tries to shed light on this issue, addressing the following question: *what are the potential synergies between development finance institutions and export/investment promotion agencies in promoting sustainable and responsible investments?* It does so by considering the respective roles of DFIs and ECAs, and the opportunities for cooperation between them to achieve sustainable development goals (SDGs).

### **Why DFIs and ECAs should cooperate?**

Recent research confirms the productivity, economic and development gains that can be derived when foreign-owned and domestic firms interact through direct and forward linkages in developing countries. Supporting such linkages through trade and investment promotion can thus be justified under certain conditions.

DFIs mainly focus on investment promotion based on development mandates and principles they need to adhere to. ECAs mainly focus on export/trade promotion to seize economic opportunities driven by commercial objectives. ECAs also engage, though to a limited extent, in investment promotion activities by providing investment insurance for political and commercial risks. As a consequence, it would seem



desirable - from the point of view of effectiveness and efficiency - that DFIs and ECAs increasingly build on one another's activities. Such synergy is reinforced by recent evidence suggesting that FDI follows exports, and that different sources and types of capital are needed at different stages of large-scale projects. Hence, the development community, and particularly DFIs, could build better on ECA export support activities, as well as ECA networks, acquired knowledge and information and lessons, when promoting sustainable investment for development.

Besides, both DFIs and ECAs need to comply with certain sustainability criteria, guidelines or regulations. These mainly go in the direction of 'doing no harm' and respecting human, social and environmental rights and standards. A comparison of their respective sustainability criteria shows that DFIs, which have a development mandate, and ECAs, which have primarily commercial motives, apply very similar sets of sustainability criteria. This increases the chances to improve the sustainability and responsibility throughout operations regardless of the specific mandate of the concerned institutions.

### Overcoming challenges to reach out cooperation potentials

Despite opportunities and potential synergies calling for more collaboration between DFIs and ECAs, various challenges need to be overcome: i) differing mandates with own internal policies and approaches limits possibilities of cooperation, ii) relatively less interaction at business operation level, and iii) differing operating procedures, credit and pricing parameters, tenor and currency preferences, and transaction eligibility criteria.

There is a need for a better understanding of the respective business practices and priorities of DFIs and ECAs, which very much relates also to the lack of cross-institutional communication. Cooperation and synergy between DFIs and ECAs must also be steered by policy-makers, so as to foster a more conducive institutional and political environment and provide the right incentives for each institution to cooperate.

While collaboration until now has been rather limited, there are a number of factors that suggest that more could be done. This mainly relates to sharing knowledge and information on potential clients and contacts, so leveraging each others' networks and collected data, as well as to sharing information on project and investment opportunities in a more formalised and frequent manner. A more systematic exchange of views and agreement on common approaches towards documentation could at the same time make transactions involving both types of institutions more efficient.

Thus, ultimately developing country markets could highly benefit from DFIs and ECAs complementing their instruments, where:

DFIs...	ECAs...
⇒ could benefit from long-term finance from ECAs	⇒ could extend their value proposition through partnering with DFIs, which in turn offer local currency, equity and small-scale funding as well as local manufacturing support
⇒ play their role of catalysts by bringing in more and diverse investors and sources of funding for sustainable development projects	⇒ rely on a strong customer base importing from ECAs' home country markets
⇒ rely on their strong presence and local networks in developing/emerging countries	

**However, making their roles more complementary, and thus, increasing collaboration between DFIs and ECAs, depends mainly on overcoming identified challenges** - both for the respective institutions themselves and cooperation challenges - and building on good practice and lessons in terms of activities, criteria and measurement/reporting. Doing so will allow (development) finance and investments and (commercial) export/internationalisation support to have a sustainable impact on development, if:

- activities are directed in a more sustainable and responsible manner towards countries and regions most in need, which requires balancing risk, return and development impact, and
- FDI and export activities have positive spillovers on domestic companies - both SMEs as much as larger ones - and their ability to sustainably enhance productivity levels and employment creation.

**Failing to do so, though, will be a missed chance** not only for public actors to diversify and better leverage funding sources to implement the 2030 Agenda, but more broadly to effectively achieve sustainability outcomes in promoting investment and trade linkages.

## 1. Introduction

**In recent years and in the aftermath of the world financial crisis, economic slowdown in Europe has encouraged European governments and the European Union (EU) to set up support programmes and instruments** that can stimulate national economies and help create the jobs needed to tackle both (youth) unemployment and crumbling growth rates. At the EU level, this has notably taken the form of a stimulus package, the Investment Plan for Europe (commonly referred to as the Juncker Plan) and its European Fund for Strategic Investments (EFSI).

This increasingly commercially-oriented public support to domestic firms and investment has been combined with an increasing focus on emerging markets outside the EU. The rationale has been threefold. First, with a stagnant economy and aging population, Europe is keen on promoting its business interests in emerging markets, as a way to tap into the dynamism and growth opportunities of new markets for its own companies. The EU predicts that 90% of the economic growth will take place outside the EU, and thus Europe need to trade with and invest in third countries (European Commission, 2015a). Second, Europe has the feeling that it is confronted by a migration crisis. Contributing to prosperity and economic development by providing access to (trade) finance and mitigating risk, the idea is that enterprises are able to expand and grow internationally, as “foreign exposure by these companies can increase enterprise competitiveness, provide access to foreign markets and resources, create new opportunities for exports, and generate profits” (UNCTAD, 2015).

**At the same time, the United Nations’ 2030 Agenda for Sustainable Development urges all countries to integrate sustainability and development ambitions** (Knoll et al., 2015). As articulated in the Addis Ababa Action Agenda (AAAA), achieving the sustainable development goals (SDGs) also requires mobilising domestic and international resources to finance this ambitious endeavour to move from millions to trillions (Kharas and McArthur, 2016; MDBs, 2015; ODI et al. 2015, UN, 2016). To do so, governments in developed countries mainly increasingly rely on engaging the private sector for development by providing public support instruments designed to trigger responsible investments (Bilal et al., 2014; Große-Puppenthal et al., 2016c; Miyamoto and Chiofalo, 2016; OECD, 2014, 2016). Those public support instruments take different forms (financial support, matchmaking and technical support or any combination of these) to support businesses in channelling investments and activities towards reaching development objectives (Große-Puppenthal et al., 2016a). At the October 2016 IMF/World Bank Group Annual Meetings, Gavin Wilson, the CEO of the IFC Asset Management Company stressed that combining commercial capital with development needs requires that private capital funds the goals and that private business implements them.<sup>1</sup>

**As donors and private investors increasingly recognise the merits of cooperation**, one of the biggest challenges will be to use funding from international financial institutions (IFIs) and development finance institutions (DFIs) “to unlock additional capital through blended or pooled financing and risk mitigation” (IFC, 2016a). This can be particularly helpful for infrastructure investments<sup>2</sup> and those supporting private sector development, while the “UN estimates the total investment needs of developing countries to be as much as US\$4.5 trillion per year, while the actual investment stands at less than a third of that” (ibid.). Recently, the German Chancellor, Angela Merkel, stressed that “there is an urgent need for direct investment in African countries because this cannot be shouldered by official development aid alone”.<sup>3</sup> To this end, Germany plans to launch in 2017, as part of its G20 Presidency, a new “Compact with Africa” in order to stimulate investment to Africa.<sup>4</sup>

<sup>1</sup> [http://live.worldbank.org/from-billions-to-trillions?CID=ECR\\_TT\\_worldbank\\_EN\\_AM16\\_EXT](http://live.worldbank.org/from-billions-to-trillions?CID=ECR_TT_worldbank_EN_AM16_EXT)

<sup>2</sup> More information on Investors in Infrastructure in developing countries: <https://ppp.worldbank.org/public-private-partnership/financing/investors-developing-countries>

<sup>3</sup> <http://www.dw.com/en/g20-summit-a-disappointment-for-africa/a-19528089>

<sup>4</sup> [www.bundesfinanzministerium.de/Content/DE/Reden/2016/2016-12-01-b20.html](http://www.bundesfinanzministerium.de/Content/DE/Reden/2016/2016-12-01-b20.html)

**Five pathways to invest in people, the planet and prosperity can be identified, all related to private finance and investment (OECD, 2016):**

1. **Foreign direct investments (FDI)**, for job creation, boosting productivity and technology transfer;
2. **Blended finance**, for improving the scale of investments in developing countries (Bilal and Große-Puppenthal, 2016a);
3. **Monitoring and measuring private funds mobilised**, for better transparency and financing strategies;
4. **Social impact investment**, seeking the empowerment of the poor and promotion of more effective and innovative business models; and
5. **Responsible business conduct**, aiming at better business practices and development results.

These are based on the principle that introducing sustainability to business models can help companies to be more profitable and successful while also ensuring sufficient responsible investments for implementing the SDGs.

**In the context of development cooperation**, European governments and institutions increasingly rely on using scarce public resources to attract and leverage private capital and investment to scale up the available capital in support of the implementation of the SDGs (Development Initiatives, 2016; UN, 2016). By mitigating commercial, political or any other form of risk, official development assistance (ODA) can be strategically used to attract loans or equity from other public or private financiers (Bilal and Große-Puppenthal, 2016; Bilal and Krätke, 2013; Barder and Talbot, 2015), such as DFIs, whose relative significance is increasing while being a growing source of development funding.

**In addition to development instruments**, EU member states have **commercially-oriented** investment and trade promotion agencies, such as export credit agencies (ECAs), which offer trade credits and mitigate risks by providing guarantees, relevant information and business contacts. Those agencies thereby help domestic companies to boost economic activity and increase FDI flows to countries, including those where there is more (perceived)<sup>5</sup> risk and therefore less supply of investments, needed for local businesses to prosper.

While both sets of instruments are different in terms of underlying objectives, institutional setting and sources of public resources, opportunities to find greater synergies in investment promotion between development cooperation and commercial instruments are manifold (Grosse-Puppenthal et al., 2016a). These should be seized to contribute to the goal of universal sustainable development through promoting investment that is both sustainable and responsible, regardless of the underlying objectives. This paper therefore tries to shed light on this issue,<sup>6</sup> addressing the following question: *what are the potential synergies between development finance institutions and export/investment promotion agencies in promoting sustainable and responsible investments?*

**To do so, it considers** i) the role of DFIs in the context of development cooperation, and ii) the role of (investment and) trade promotion agencies for commercial purposes, and addresses the following sub-questions:

- What sustainability criteria and principles do DFIs and ECAs follow?
- To what extent do DFIs and ECAs differ in the products and services they provide?
- How can DFIs ensure that development effectiveness criteria are better implemented?

<sup>5</sup> <https://www.rijksoverheid.nl/documenten/toespraken/2015/07/01/toespraak-minister-ploumen-over-dggf>

<sup>6</sup> This study is a follow-up work to two previous reports, one of which mapped the development cooperation and commercial public instruments supporting the private sector, while the second took a closer look at EU matchmaking instruments that are provided to EU firms that want to invest and trade outside Europe. Both were summarised in a shorter, synthesising Briefing Note. (Große-Puppenthal et al., 2016a/b/c)

- How do DFIs live up to their development mandates and commitments towards sustainability?
- How can ECAs ensure greater sustainability in their activities?

**The remainder of this paper is structured as follows:** Section 2 maps the context in which trade and investment promotion takes place, recognising increasing internationalisation efforts by both governments and business; Section 3, in the context of development cooperation, considers the role of DFIs to promote sustainable investments, while taking into account the development principles applying to them; Section 4 takes a closer look at the role of ECAs to promote commercial investments and their way to comply with sustainability criteria they need to adhere to; based on these considerations, Section 5 then lays out some of the potential synergies and differences between DFIs and ECAs; while Section 6 concludes by summarising the main findings and lessons learnt, and identifies a number of policy recommendations.

## 2. The context of trade and investment promotion

**To expand growth and export markets, companies increasingly operate outside domestic and EU markets by exporting goods and services and conducting foreign direct investment.** However, due to inadequate information about local supply and demand conditions in foreign markets, as well as a number of uncertainties, firms are generally required to acquire specific knowledge on the foreign market they want to export to or invest in, and therefore tend to follow a gradual internationalisation process (Johanson and Vahlne, 1977).

For the private sector to invest in developing countries the following impediments tend to be particularly difficult to overcome: i) they face a complex and unstable regulatory environment; ii) not all investments succeed, so there will be defaults, which require a proper work-out process to manage those; and iii) often institutional and private investors do not only invest their own money but that of clients, who may have less information and thus more conservative risk preferences, so risk-perception matters and risk-taking ability is limited. To promote investment, the question is thus often how (and to which extent) to de-risk such investments and create more stable and better conditions for the private sector and institutional investors to become more active in such developing foreign markets.

**Yet, given the low or stagnant growth levels in European economies and the uncertainty firms face in foreign - especially emerging and developing - markets,** European governments and institutions are ramping up efforts to support their domestic firms in their endeavour to internationalise - trade and invest abroad - in order to benefit from more dynamic foreign markets and stimulate their domestic economies.

### Investment follows exports

Traditional approaches have focused on the rationale for firms to invest and export, and whether trade and investment complement or substitute one another (Fontagné, 1999; Martinez et al., 2012), suggesting they are both, depending on cases. Taking a time dynamic approach, **recent insights suggest that FDI follows exports.** Conconi et al. (2015) argue that the gradual internationalisation process leads to manufacturing firms “serving a foreign market via exports before deciding whether to invest there, (hence) a firm’s FDI entry in a foreign market is almost always preceded by exports”. Compiling data on Belgian manufacturing firms over a decade (between 1998 and 2008), they find that in almost 86% of the cases, FDI entries were preceded by exports and that in almost 100% of the cases, exporting to a market took place without having previously invested there. Hence, the “probability that a firm starts investing in a foreign country increases with its export experience in that country”, as the uncertainty about earning profits in new foreign markets, makes firms starting to export gain more market knowledge (Conconi et al.,

2015). Investments are driven by the firm's desire to serve foreign markets but these investments can take different forms, as illustrated in Table 1.

Table 1: Horizontal *vis-a-vis* distribution oriented FDI and resulting implications

<i>How?</i>		<i>Implications?</i>
<b>Horizontal FDI</b>	→ Establishment of foreign production facilities	<b>Trade-off between proximity and concentration:</b> → exports bear trade costs, but save the cost of establishing a foreign subsidiary → FDI bears cost of setting up the subsidiary, but less trade costs
<b>Distribution-oriented FDI</b>	→ Investments in distribution centres and/or sales offices	<b>Trade-off between fixed and variable costs:</b> → Using a local agent to distribute products (lower fixed cost) → or setting up own distribution network (lower variable costs)

Source: Conconi et al. (2015).

In both cases, the authors argue that “uncertainty can lead firms to start serving a foreign market via exports before engaging in FDI” and only “if it discovers that it can earn large enough profits in the foreign market, it finds it worthwhile to pay the fixed costs of establishing its own production facility or distribution network to reduce its variable costs”. Similarly, Gazaniol (2014) finds that (in particular first time) investment from multinational enterprises (MNEs) in a foreign country tends to follow an initial exporting phase to that country.

It should be noted however that there are many other classifications and motivations for FDI, differing for instance between (i) resource seeking, (ii) market seeking and (iii) non-marketable asset seeking motivations for FDI decisions (Franco et al., 2008). It should also be stressed that in practice there is no such linear process, which suggests that once you export successfully, FDI will automatically follow, but FDI decisions are dependent on a variety of factors making it more complex than it often seems.

But these findings are important: they highlight the strong complementary and potential synergy that may exist between export promotion and investment promotion, and thus including by and between ECAs and FDIs.

## 2.1. Attracting FDI for development

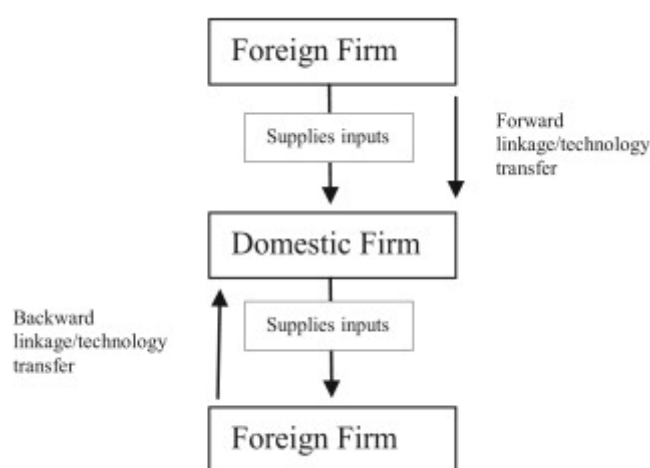
**At the same time, many developing countries made attracting FDI a significant policy priority as part of their development strategies** in order to create jobs and inject capital into the domestic economy (Sutton et al., 2016). The rationale for state intervention in developing countries is based on the premise that attracting FDI can trigger positive externalities for domestic firms and productivity levels with new technologies and innovations being “potentially an important source of productivity growth as they may help host country domestic industries catch up with the international technology frontier” (Newman et al., 2015).

Newman et al. (2015) found that “there are productivity gains associated with direct linkages between foreign-owned and domestic firms along the supply chain (...) including evidence of productivity gains through forward linkages for domestic firms which receive inputs from foreign-owned firms”, as illustrated in Figure 1.

According to Newman et al. (2015), there is “evidence of (i) *positive spillovers* from downstream FDI firms, in particular joint venture FDI firms, to domestic input suppliers, and (ii) *negative spillovers* from upstream FDI firms to downstream domestic producers”. Positive FDI spillovers are assumed because “foreign-

invested firms are technologically superior and that knowledge is transferred through their interactions with domestic firms, which, in turn, leads to productivity improvements". It should be recognised that there are different types of spillovers: (i) *horizontal, or intra-sector, spillovers*: FDI firms transfer knowledge and technology to competing firms in the same sector; and (ii) *vertical, or inter-sector, spillovers*: knowledge and technology transfer through the supply chain from foreign intermediate suppliers to domestic producers, or more commonly from foreign-invested firms to domestic input suppliers.

Figure 1: Definition of FDI spillovers



Note: Direction of linkages is defined from the perspective of foreign firms.

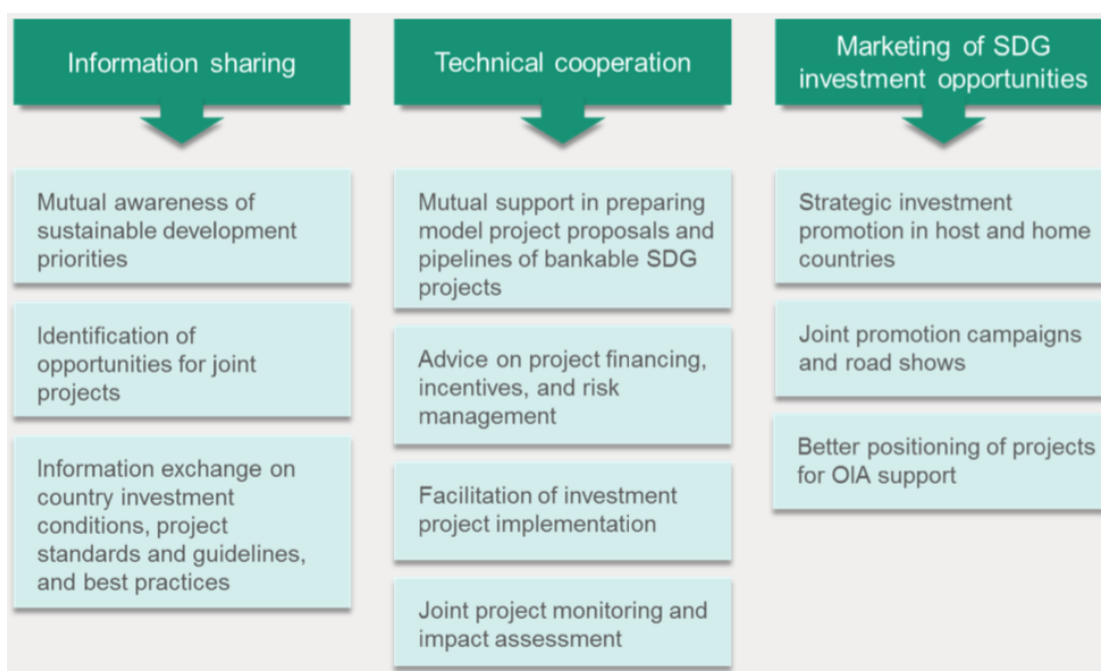
Source: Newman et al., 2015.

Blomström and Kokko (2003) however find that "potential spillover benefits are realised only if local firms have the ability and motivation to invest in absorbing foreign technologies and skills". While a positive correlation between FDI and domestic firms is promising to reap more benefits for domestic companies in the future, there are various - widely reported - negative externalities related to environmental impacts, human rights violations and labour conditions. These remind us to not take positive spillovers for granted but rather consider the FDI-productivity gains relationship as a complex endeavour that needs the right framework conditions to yield development benefits. Knowledge transfer from multinationals or other foreign firms to domestic companies for instance can become more difficult if the technological or knowledge gap is too large. Productivity gains are also difficult to achieve if there is a pure foreign supplier to domestic buyer relationship, as this entails lower positive spillover effects compared to collaboration between foreign and domestic actors.

Taking the positive correlation between FDI and domestic productivity gains into consideration, inward investment promotion agencies (IPAs) in developing countries could therefore attract sustainable development-related projects, as UNCTAD (2015) argues, and enter into partnerships with for instance European outward investment agencies (OIAs). This could have a number of positive effects, illustrated in Figure 2.

Similar synergies and complementarities could be envisaged between European DFIs and ECAs, where their collaboration could increase their impact for sustainable development through benefiting from each others' activities and characteristics, as discussed in the following sections.

Figure 2: Potential goals and benefits from OIA-IPA partnerships



Source: UNCTAD, 2015.

## 2.2. Promoting exports and investment

While developing countries' governments increase their efforts to attract FDI, European counterparts develop support mechanisms and strategies to support their domestic firms to internationalise, mainly through export promotion. At the same time, recent research confirms that there are productivity gains when foreign-owned and domestic firms interact through direct and forward linkages in developing countries. Therefore, from a commercial point of view there seems to be merits in promoting investment and trade for both commercial and developmental objectives.

Development cooperation tools that engage with or support the private sector aim at fostering sustainability and development objectives, while other public support instruments rather pursue economic (self-)interests. In both cases, these are done through agencies that provide (financial) support to businesses. UNCTAD (2015) divides OIAs into three categories:

- **outward investment promotion agencies (IPA)** “promote outward investment, often in combination with the promotion of inward investment and export”. In Europe, these include agencies such as Business Sweden, Team Finland, Germany Trade & Invest (GTAI), Netherlands Enterprise Agency (RVO), the UK Department for International Trade (DIT)<sup>7</sup>;
- **development finance institutions (DFIs)** are “national, regional, or international organisations which have the dual role of investment banks and development institutions, providing loans, equity, and grants for projects in developing countries and regions and in transitional economies”. These include the International Finance Corporation (IFC) as part of the World Bank Group, and at the European level, European Development Finance Institutions (EDFIs) such as the Dutch FMO, the British CDC, the German DEG or the French Proparco.
- **investment guarantee schemes** “insure non-commercial and/or commercial risks abroad to encourage foreign investment”, such as the Multilateral Investment Guarantee Agency (MIGA) as

<sup>7</sup> Formerly UK Trade & Investment (UKTI) but as of July 2016 renamed to UK DIT.



part of the World Bank Group, and ECAs, such as in Europe the UK Export Finance, SACE in Italy, COFACE in France, Euler Hermes in Germany and Atradius in the Netherlands.

Sections 3 and 4 focus on the roles of DFIs and ECAs respectively, with a view to highlight which **potential synergies and complementarities between DFIs and ECAs can be triggered**, discussed in Section 5.

DFIs mainly focus on investment promotion based on development mandates and principles they need to adhere to. ECAs however focus mainly on export/trade promotion to seize economic opportunities driven by commercial objectives. But ECAs also need to comply with certain sustainability criteria, guidelines or regulations. These mainly go in the direction of doing no harm and respecting human, social and environmental rights and standards.

Besides, it is important to note that small- and medium-sized enterprises (SMEs) rarely export directly but indirectly via larger companies through input supply for instance. Hence, investment promotion really matters for indirect export promotion, thus the need to link investment promotion with export promotion in the context of global value chains (GVCs).

Moreover, ECAs also carry out investment promotion activities, though on a limited basis, by providing investment insurance for political and commercial risks.<sup>8</sup>

It therefore seems that both ECAs and DFIs could increasingly build on one another's activities taking into account that FDI follows exports and that different sources and types of capital are needed at different stages of (large-scale) projects. Hence, the development community and particularly DFIs could build on export promotion activities, building on ECA networks, acquired knowledge and information and lessons, when promoting sustainable investment for development. To identify such synergies and complementarities the following two sections look into investment and trade promotion from a development (role of DFIs) and commercial perspective (role of ECAs) respectively, paying particular attention to criteria and principles they have to comply with.

## 3. Promoting sustainable investments in the context of development cooperation

### 3.1. The role of DFIs

**One of the rationales for the existence of DFIs is to provide financial resources in regions and sectors where access to capital is limited** (Ebert and Posthuma, 2010). Therefore, DFIs should not compete with private sector banks but rather generate funding for projects that are considered too risky by the majority of private banks, hence, additional to what the market is providing. DFIs are mostly government-controlled and make investments in private sector projects with a dual objective:

- 1) DFIs aim to contribute to sustainable development, and
- 2) they have to remain financially viable institutions.

This requires striking a difficult balance between development impact, the level of intervention, which can lead to market distortions, the risk they are willing and able to take, and financial return (Bilal and Große-Puppenthal, 2016b).

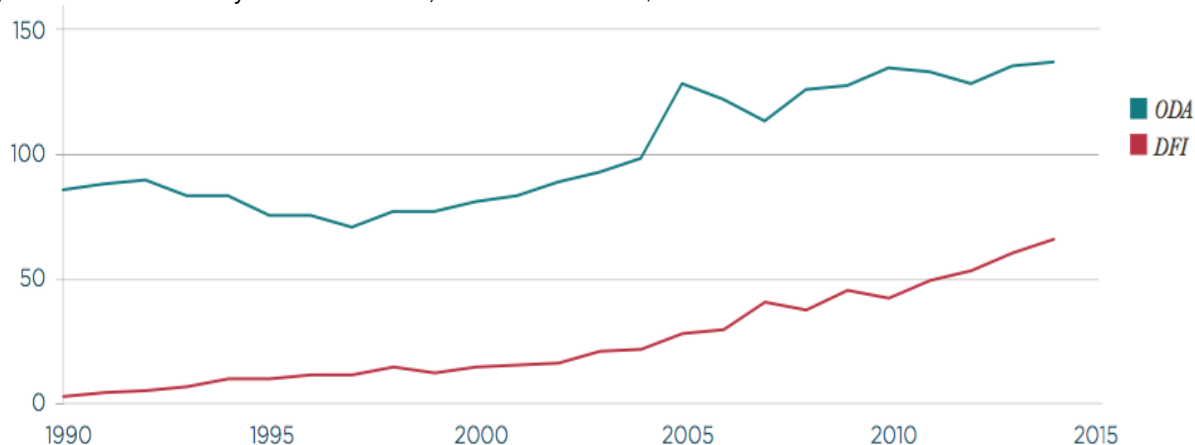
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<sup>8</sup> <http://www.investopedia.com/terms/e/export-credit-agency.asp>

## DFIs' activities

**The role of DFIs is increasingly important in terms of both scope and impact in the development finance landscape** (Savoy et al., 2016). "Private investment and tax payments are the dominant sources of financing to support development" (EDFI, 2016), while playing a particularly important role in blending, which Commons Consultations (2015a) consider "a revival of industrial policy within international development". During 2012-2014, "US\$36.4 billion was mobilised from the private sector through ODA interventions in the form of guarantees, syndicated loans and shares in collective investment vehicles (development-related investment funds), [while] the overall amount followed an upward trend, with guarantees mobilising the largest share (Benn et al., 2016). Figure 3 shows that "annual commitments by bilateral and multilateral DFIs exceeded US\$65 billion at the end of 2014, while net ODA has been stagnant in real terms" at around US\$140 billion (EDFI, 2016). The total DFI activity level has been constantly increasing with an average annual growth rate of around 5%.

Figure 3: Annual activity level 1990-2014, constant 2014 US\$billion



Note: ODA is net ODA from DAC countries; DFI is actual commitments from DFIs. Current prices have been converted to constant 2014 prices by dividing current price series by the 'Total DAC' deflator.

Source: EDFI (2016).

In 2014 the annual commitments were shared between three larger groups: i) 40% by **multilateral financial institutions**, such as the World Bank's IFC and MIGA; ii) 35% by **bilateral DFIs**, such as the EDFIs, US OPIC and Japan's JBIC; and iii) 25% by **regional development banks and financial institutions**, including the Asian Development Bank (ADB), the African Development Bank (AfDB), the European Bank for Reconstruction and Development (EBRD), the EIB and the Inter-American Development Bank (IDB) (EDFI, 2016).

Hou and Lemma (2015)<sup>9</sup> further provide DFI profiles and a mapping of DFIs regarding **ownership** (multilateral vs. bilateral), **activities and instruments** (mainly loans but also guarantees and equity), **their size** (multilaterals being bigger than bilaterals due to a wider geographical coverage and available resources), **regional** (mainly Sub-Saharan Africa (26.9%) and Asia (25.5%)) and **sectoral distributions** (finance and infrastructure sectors), and **DFI terms of investment**, which relates to investment duration, interest rates, maximum amount of equity investment, maximum loan size, preferred currencies and average loan or investment length. Their mapping additionally criticises the "disjointed nature of DFI reporting", as DFIs use various reporting systems for their diverse set of operations, which makes it difficult to compare DFI activities, as they use different categories (for instruments used, regional categorisation and sectoral categorisation) and additionally complicates "the identification of particular gaps in investments".

<sup>9</sup> This mapping primarily looks at the biggest members of the EDFI plus two non-EDFI members (the German KfW and the Japanese Bank of International Co-operation (JBIC)).

Both the German KfW's private sector-focused DFI, DEG<sup>10</sup>, and Dalberg (2010) consider investments in the private sector - so DFIs providing private sector finance - as a **third pillar in (Europe's) development cooperation**, the first being aid channelled by public and civil society actors through bilateral and multilateral ways, and the second being development banks providing public sector lending and guarantees. DFIs provide loans, guarantees and equity finance to the private sector through providing "finance to financial institutions that provide long-term capital and know-how to local SMEs; to private sector intermediaries (such as funds of funds) which in turn, invest in underlying private enterprises that are involved in development projects; and to underlying private enterprises" (Hou and Lemma, 2015). There are also agencies that combine financial provision with technical assistance or advisory services.

**The recent European Commission announcement of the European External Investment Plan (EIP)** further pushes IFIs and DFIs to take on a bigger role in contributing to achieving inclusive and sustainable growth and creating jobs, as the EIP aims to leverage "funds from the EU, its Member States, other donors, financial institutions and the private sector".<sup>11</sup> The EIP aims at triggering investments in Africa and the Neighbourhood, while tackling some of the root causes of migration. To do so, the EU will provide €3.35 billion until 2020 from its budget and other sources, including the European Development Fund (EDF), to "support innovative guarantees and similar instruments in support of private investment, enabling the EIP to mobilise up to €44 billion of investments".<sup>12</sup> If the EU's contribution is matched by EU Member States and other partners, the total amount of investments could reach up to €88 billion (see also Bilal and Große-Puppenthal, 2016a).

### **EDFI - the Association of European Development Finance Institutions**

**The EDFI group consists of 15 DFIs all operating government-controlled revolving funds with the mandate to invest in developing countries** (Commons Consultants, 2015b; Dalberg, 2010).<sup>13</sup> Revolving funds mean that returns from completed projects are reinvested into new development-oriented projects of the EDFIs. Their importance and growing influence is increasing with a "portfolio of committed investments of €36.3 billion at the end of 2015", which means that it has more than tripled over the past 10 years, mainly due to increased shareholders' equity, as shown in Figure 4 (EDFI, 2016).

According to EDFI (2016), "companies and projects supported by European DFI financing directly or through investment funds" contributed to the creation of 4 million direct jobs, 74,000 GWh of electricity supply, and €11 billion in tax payments to governments in 2015. Putting those numbers in context though is difficult due to diverse reporting mechanisms and differing interpretations of results attribution, as it is not always clear which specific results have been achieved solely because of the DFI contribution. A large bulk of investments by European DFIs goes to Sub-Saharan Africa (31%) followed by Latin America and the Caribbean (20%), and South Asia (14%) (EDFI, 2016). In terms of sector distribution, European DFI portfolios focus on financial services (30%), power (18%) and industry/manufacturing (16%).

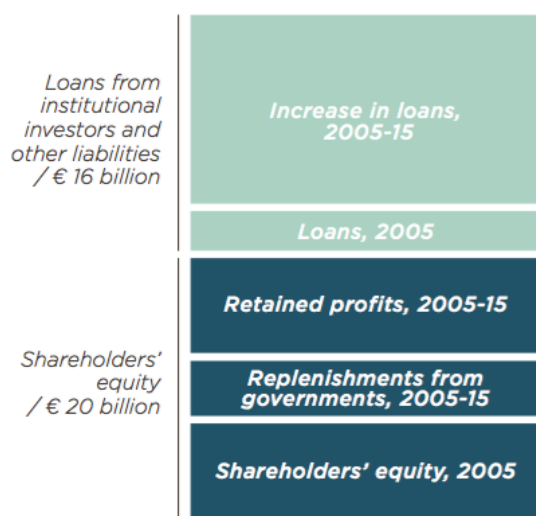
<sup>10</sup> <https://www.deginvest.de/International-financing/DEG/Die-DEG/Was-wir-tun/#2>

<sup>11</sup> [http://europa.eu/rapid/press-release\\_MEMO-16-3006\\_en.htm](http://europa.eu/rapid/press-release_MEMO-16-3006_en.htm)

<sup>12</sup> [http://europa.eu/rapid/press-release\\_IP-16-3002\\_en.htm](http://europa.eu/rapid/press-release_IP-16-3002_en.htm)

<sup>13</sup> The EDFI members are: BIO, Belgium - CDC, United Kingdom - COFIDES, Spain - DEG, Germany - FINNFUND, Finland - FMO, Holland - IFU, Denmark - NORFUND, Norway - OeEB, Austria - PROPARCO, France - SBI/BMI, Belgium - Sifem, Switzerland - SIMEST, Italy - SOFID, Portugal - SWEDFUND, Sweden.

Figure 4: European DFI investment resources in 2005 and increase 2005-2015



Note: Figures reflect resources on and off balance sheet. For EDFI members established after 2005, the initial shareholders' equity in establishment year is stated in replenishment figure (OeEB and SOFID).

Source: EDFI, 2016.

### 3.2. Criteria and principles of sustainability and development

In order to increase the effectiveness of aid and development cooperation, various declarations and documents, such as the Rome Declaration for Harmonisation (2003), the Paris Declaration on Aid Effectiveness (2005), the Accra Agenda for Action (2008) and the Busan Partnership for Effective Development Cooperation (2011), have advanced the agenda in recent years.<sup>14</sup> While the Paris Declaration refers to five main principles (ownership, alignment, harmonisation, managing for results and mutual accountability) to increase the aid effectiveness, the Busan Partnership agreed on the following four shared principles to enhance the effectiveness of development cooperation: i) ownership of development, ii) focus on results, iii) inclusive development partnerships, and iv) transparency and accountability to each other.

Additionally, mainly official multilateral or international organisations, such as the UN, G20, the World Bank and the Organisation for Economic Co-operation and Development (OECD) amongst others, rather than private sector actors or civil society organisations (CSOs) have developed various guidelines, principles and standards (Byiers et al., 2016). Vervynckt (2016) provides an overview of the most relevant responsible finance standards, such as the 2006 UN Principles for Responsible Investment (UN PRI), the 2011 UN Guiding Principles on Business and Human Rights, the 2011 OECD guidelines for multinational enterprises, the 2006 Equator Principles or the 2012 IFC Performance Standards (PS), which are all voluntary despite the IFC PS being mandatory for all clients regarding their responsibilities for managing their environmental and social risks.

Table 2 provides an overview of the areas and actors targeted by those guidelines, principles and standards, while it should be recognised that this report mainly looks at institutional investors, development banks and DFI activities though national governments and multinational enterprises can exert leverage to increase compliance.

<sup>14</sup> OECD website: *The High Level Fora on Aid Effectiveness: A history*.

Table 2: Main areas and actors targeted by selected guidelines, principles and standards

	<b>Target areas</b>	<b>Targeted actors</b>
<b>UN Principles for Responsible Investment</b>	<ul style="list-style-type: none"> <li>● Protection of human rights</li> <li>● Protection of the environment</li> <li>● Tax</li> <li>● Public consent &amp; transparency</li> </ul>	<ul style="list-style-type: none"> <li>● Institutional investors</li> <li>● Private banks</li> <li>● MNEs (secondary targets, financial sector)</li> </ul>
<b>UN Guiding Principles on Business and Human Rights</b>	<ul style="list-style-type: none"> <li>● Protection of human rights</li> <li>● Public consent &amp; transparency</li> <li>● Dispute settlement</li> </ul>	<ul style="list-style-type: none"> <li>● National governments</li> <li>● MNEs</li> <li>● SMEs</li> <li>● Public development banks</li> <li>● DFI investee companies</li> <li>● Institutional investors</li> <li>● Private banks</li> </ul>
<b>OECD Guidelines for MNEs</b>	<ul style="list-style-type: none"> <li>● Protection of human rights</li> <li>● Protection of the environment</li> <li>● Tax</li> <li>● Public consent &amp; transparency</li> <li>● Dispute settlement</li> </ul>	<ul style="list-style-type: none"> <li>● National governments</li> <li>● MNEs</li> <li>● Public development banks</li> <li>● DFI investee companies (secondary targets)</li> <li>● Institutional investors</li> <li>● Private banks</li> </ul>
<b>Equator Principles</b>	<ul style="list-style-type: none"> <li>● Protection of human rights</li> <li>● Protection of the environment</li> <li>● Public consent &amp; transparency</li> <li>● Dispute settlement</li> </ul>	<ul style="list-style-type: none"> <li>● MNEs (financial sector)</li> <li>● Public development banks (secondary targets)</li> <li>● Private banks</li> </ul>
<b>IFC Performance Standards</b>	<ul style="list-style-type: none"> <li>● Protection of human rights</li> <li>● Protection of the environment</li> <li>● Public consent &amp; transparency</li> <li>● Dispute settlement</li> </ul>	<ul style="list-style-type: none"> <li>● DFI investee companies</li> </ul>

Source: Authors' summary based on Vervynckt (2016).

Through developing environmental and social risk management practices and policies, IFIs and DFIs were able to raise the bar “on the level of environmental and social review and performance for many international projects” (CBX International, 2015).

**A group of European NGOs and CSOs also developed a ‘A principled approach to public-private finance’** so that governments can apply best practice, international standards and more systemic learning for the benefit of better sustainable development outcomes (CAFOD et al., 2015), as illustrated in Figure 5.

These principles are undoubtedly relevant. However, they seem to be even broader than those currently in place, which raises questions with regard to their operational effectiveness and ability to be implemented in practice. Based on such broad guidelines, more operational and specific sustainable practices should be identified.

Figure 5: A Sustainable Development Traffic Light



Source: CAFOD et al. (2015).

### EDFI principles: additionality, catalytic effect and project sustainability

Investments by the EDFIs are guided by three principles, referred to as 'success criteria for DFI investments': i) additionality, ii) the catalytic effect, and iii) project sustainability (EDFI, 2016). These criteria aim to help DFIs:

- to invest where other investors are not present (**additionality**), i.e. taking a long-term approach, which allows taking higher risk with greater development benefits,
- to mobilise other investments through risk sharing instruments, being first movers, thus, demonstrating to other investors that investments despite higher risks are feasible, and sharing expertise (**catalytic effect**), and
- to reduce the dependency on aid by investing in financially viable projects, which therefore become sustainable sources of jobs and tax income, and at the same time introducing responsible business conduct respecting environmental, social and governance (ESG) standards (**project sustainability**).

In 2009, the EDFIs also adopted the 'EDFI Principles for Responsible Financing: Towards Sustainable Development', which include 'EDFI's Harmonised ESG Standards in relation to the ESG in investment activities'.<sup>15</sup> Those standards on Environment, Social Matters and Governance (ESG) include: (a) Environmental and Social Category Definitions, (b) Requirements for Environmental and Social Due Diligence, Environmental and Social Contractual Requirements and Monitoring and (c) an Exclusion List, all of which will be reviewed regularly. The EDFI principles take as benchmarks the UN Declaration of Human Rights, the ILO Core Conventions and the IFC Performance Standards on Economic and Social Sustainability and associated Environmental and Health & Safety Guidelines.

### IFIs' efforts - development results indicators

In October 2013, 25 DFIs and IFIs - including the EDFIs, ADB, AfDB, EIB, EBRD, IFC, OPIC, and MIGA

<sup>15</sup> [http://www.finnfund.fi/yrittys/sustainability/en\\_GB/edfi\\_responsible\\_financing/](http://www.finnfund.fi/yrittys/sustainability/en_GB/edfi_responsible_financing/)

amongst others - signed a memorandum of understanding (MoU)<sup>16</sup> regarding harmonised indicators for private sector operations (HIPSO), which includes a list of 27 indicators, definitions and units of measurement along a number of cross-cutting issues.<sup>17</sup> Those agreed indicators are meant to help in harmonising results measurement and decrease the reporting burden, but most importantly they aim to facilitate learning across DFIs/IFIs, from each other’s practices. In autumn 2015 the memorandum was amended by an addendum<sup>18</sup> harmonising the definitions of 38 indicators for private sector operations. Tracking and using the harmonised indicators is however no obligation, “if an IFI does not wish to track the development outcomes they capture”.<sup>19</sup> It is though a promising initiative that could contribute to better cross-institutional learning and enhance the ability to compare projects and their success between institutions, which in turn increases the ability to identify investment gaps and funding or project opportunities.

### 3.3. Challenges and opportunities

DFIs have an important role to play with regard to integrating principles and criteria that support the sustainability and development impact of operations. In that regard, the International Trade Union Confederation (ITUC) examined how DFIs applied and integrated development effectiveness criteria, when using aid to leverage additional finance for development (ITUC, 2016). It concluded that the examined DFIs are “ill-equipped to manage aid flows in line with existing best practices”, summarised in Table 3.

Table 3: Summary of DFIs’ performance on selected development effectiveness principles

DFI	Ownership		Development results		Mutual accountability	
	Mandate & eligibility	Participation government & social partners	Standard on worker’s rights and OFC	Monitoring	Transparency	Complaint mechanism
Bio (Belgium)	poor performance	poor performance	average performance or some good features	average performance or some good features	poor performance	poor performance
CDC Group (UK)	average performance or some good features	poor performance	average performance or some good features	poor performance	average performance or some good features	average performance or some good features
Cofides (Spain)	poor performance	poor performance	average performance or some good features	poor performance	poor performance	poor performance
DEG (Germany)	poor performance	poor performance	average performance or some good features	poor performance	poor performance	good performance
FMO (Netherlands)	poor performance	poor performance	average performance or some good features	poor performance	poor performance	good performance
Norfund (Norway)	average performance or some good features	poor performance	good performance	poor performance	poor performance	poor performance
OPIC (US)	poor performance	poor performance	average performance or some good features	average performance or some good features	poor performance	good performance
Proparco (France)	average performance or some good features	poor performance	good performance	average performance or some good features	average performance or some good features	poor performance
Swedfund (Sweden)	average performance or some good features	poor performance	good performance	poor performance	average performance or some good features	poor performance

■ poor performance ■ average performance or some good features ■ good performance

Source: ITUC (2016).

**Based on its own analysis of DFIs’ performance, ITUC makes the following recommendations:**

1. Increase the ownership of development projects: DFIs should review their mandate and overall

<sup>16</sup> Memorandum regarding ‘IFIs harmonised development results indicators for private sector investment operations’, 12 October 2013.

<sup>17</sup> Direct employment and payments to governments, and along the sectors of agribusiness, education, energy, financial intermediation, private equity and investment funds, health, housing, ICT, industry & services, transportation, waste & sanitation, and water.

<sup>18</sup> Addendum No.1 to the MoU regarding IFIs Harmonised Development Results Indicators for Private Sector Investment Operations among IFIs, October 5, 2015.

<sup>19</sup> <https://indicators.ifipartnership.org/about/>

- development policy and compatibility with ownership principles;
2. Focus on delivering and demonstrating development results;
  3. Adopt upward and downward accountability systems that guarantee the right of all project stakeholders to be heard.

**In light of the recent overhaul by the World Bank's social and environmental framework**, multilateral development banks (MDBs) also aim to address criticism related to “ignoring community concerns around development projects” and human rights violations<sup>20</sup>, as “critics view the ongoing revision of the World Bank safeguards with scepticism” (Heinrich Böll Foundation, 2015). Civil society claims that the “refusal of the [World] Bank to finally institutionalise human rights is an abject failure for the people who risk their lives speaking out about development projects or defending their lands” (Gordon, 2016). However, “project proponents are now required to assess potential risks to vulnerable groups”, which the World Bank could take as an opportunity to make sure that such assessments also measure risk for human rights defenders. OPIC and KfW could serve as an example, as they “are legislatively required (...) to ensure [that] projects identify (...) human rights risks”, while this allows to introduce further due diligence measures that could protect human rights defenders (Gordon, 2016).

Talbot (2015) underlines the increasing role of DFIs in delivering sustainable development, while referring to Canada and Australia both setting up their own DFIs<sup>21</sup>, as well as to the UK scaling up their efforts with CDC through a US\$1 billion capital increase in 2015.<sup>22</sup> However, he identifies a **number of challenges, which relate to both DFI activities and how they affect developing countries**: i) risk transfer to own balance sheets as opposed to risk mitigation; ii) addition is not equal to additionality since they do not account for what would have happened in the DFIs' absence; iii) impact measurement mainly taking place in quantitative terms; and iv) issues of capture and distortion related to adverse selection of companies, tied aid or distorting markets by picking and subsidising winners. Overcoming these challenges is crucial as otherwise it could fall back to taxpayers, as public funding is used to trigger private investments and even worse, it could have more negative effects for developing countries due to market distortion.

Another challenge relates to DFIs providing finance to financial intermediaries, as often DFIs have only limited knowledge about actual results and activities by final beneficiaries that benefit from access to finance. By using financial intermediaries, DFIs and IFIs lose “control over how the money is eventually spent” and in the case of IFC, for instance, despite requiring its clients to comply with its social and environmental safeguard policies, there is uncertainty about whether “those same standards are met in the majority of the projects the client then funds” (Oxfam, 2015). Hence, if IFC and other DFIs do not know where funding is actually spent, and in particular to which final beneficiaries and how they operate (according to DFIs principles or not), how can DFIs ensure that there is no harm being done in terms of environmental or social issues, let alone sustainable development being actively promoted, as laid down in their mandate?

On the other hand, working through financial intermediaries allows DFIs to reach a wider range of (smaller) final beneficiaries (such as SMEs and smallholders). It also allows them to strengthen the management and practice of these financial intermediaries, including in terms of sustainability principles, with trickle down effects on final beneficiaries. In practice, the challenge for DFIs is thus to ensure not only that financial intermediaries are adhering to the DFIs principles, but also the final beneficiaries, while limiting the reporting administrative burden that comprehensive monitoring and transparency requirements could require. A possible yardstick for DFIs should be whether they are contributing to positive dynamics towards

<sup>20</sup> Gordon (2016). See also <http://www.brettonwoodsproject.org/2016/09/world-bank-approves-new-diluted-safeguards/> & <https://www.escri-net.org/resources/information-export-credit-agencies-and-human-rights> & [http://www.thirdworldtraveler.com/IMF\\_WB/Export\\_Credit\\_Agencies.html](http://www.thirdworldtraveler.com/IMF_WB/Export_Credit_Agencies.html)

<sup>21</sup> Canada creates a bilateral Development Finance Institution: will Australia follow suit? April 23, 2015.

<sup>22</sup> DfID to pump £735m into investment arm for private sector projects. The Guardian article 17 July 2015.



more sustainable practices by final beneficiaries (and not turning a blind eye), and whether they have effective monitoring and complaint mechanisms, with the ability to redress meaningful malpractices. In this respect, it is important for DFIs to keep learning from each other's experiences, and keep fostering a constructive engagement with civil society and local private sector and other relevant actors, to identify better and more sustainable practices.

Indeed, while there is an increasing emphasis on the role of DFIs to promote development through sustainable investments, enhancing already existing coordination and cooperation among DFIs and with other concerned stakeholders should be a priority, and could be articulated along three areas:

- more stringent and coherent application of **sustainability standards and criteria**;
- **enhancing reporting practice** related to used indicators for results and impact measurement; and
- **exchange of information, data and knowledge** to improve efficiency, peer learning and the ability to identify investment gaps and opportunities.

While this holds particularly true for development cooperation actors, such as DFIs, the following section tries to better understand how commercial investment promotion could further contribute to more responsible and sustainable practices. To this end, Section 4 focuses on the role of export credit agencies, with a view to identify, in Section 5, synergies and complementarities beyond the development cooperation circles, between DFIs and ECAs.

## 4. The role of ECAs in promoting responsible investments

Building on commercial interests, the development community seeks to stimulate sustainable investment along the SDGs, drawing on the experience and leverage of IFIs and DFIs. But outside the development cooperation framework, there has long been an active support by public entities to private sector investment, for commercial purposes. Such investment and trade promotion must also comply with some sustainability principles, and under the universal 2030 Agenda for Sustainable Development, should also contribute to achieving the SDGs.

### 4.1. Role of investment and trade promotion agencies

Public authorities, including in Europe, have sought to promote domestic and international investment and trade, including by providing support to their domestic private sector. Public entities in Europe, such as Business Sweden, Team Finland, Germany Trade & Invest (GTAI), the Netherlands Enterprise Agency (RVO), or the UK Department for International Trade (DIT)<sup>23</sup>, are dedicated institutions to promote domestic companies abroad while attracting FDI into their countries.

Similarly, export credit agencies (ECAs) provide trade finance and credit loans to enterprises and banks to trigger trade and prosperity. This Section focuses on the role of ECAs, the criteria and guidelines of sustainability they adhere to and the opportunities to become more responsible and sustainable in their activities.

#### Role of ECAs

As defined by the OECD, an ECA is “an agency in a creditor country that provides insurance, guarantees,

<sup>23</sup> Formerly UK Trade & Investment (UKTI) but following the Brexit referendum, renamed and restructured as of July 2016 the UK Department for International Trade <https://www.gov.uk/government/organisations/uk-trade-investment>

or loans [mainly to domestic companies] for the export of goods and services". By doing so, they lower the commercial and political risks<sup>24</sup> for private companies linked with exporting and/or investing overseas, boost international trade, and thus contribute to jobs creation both in ECAs home countries and ideally abroad. Therefore they fill gaps in trade finance for non-marketable risks (OSCE, 2004; Grieger, 2013).<sup>25</sup> In this respect, it can be argued that they do not compete with commercial banks, but rather ensure that adequate insurance cover exists at all times and market situations (Schone, 2015).

**In practical terms, ECAs provide three main instruments to support their domestic private sector:**

- 1) insurances,
- 2) short, medium and long-term export credits, and
- 3) guarantees, often coupled with advisory services (market information).

These respond to the basic financial needs of exporters, from pre-export working capital to short-term export terms extended to importers; medium to long-term financing support to overseas importers; project financing and/or special export structures (Krauss, 2011). Within the EU, most ECAs provide support through insurance (EIC, 2014).

Although the ECAs' share of the aggregate financing of world trade remains relatively small (US\$2 trillions in 2014 according to the Berne Union, accounting for 11% share of global trade), they play an increasingly important role in today's globalised and often uncertain economy.<sup>26</sup> Their capacities to mitigate medium and long-term credit risks and boost trade finance markets, even in times of investment climate deterioration, are amply recognised by the international community (European Banking Federation, 2015; World Bank, 2010), which further acknowledges their decisive role in realising projects and their resulting exports in developing countries<sup>27</sup> (Berne Union, 2013). ECAs are indeed the largest source of public financial support for projects in developing countries (Both Ends, 2016), and have a unique access and set of information regarding countries and millions of buyers in all of the major trading countries (Stephens, 1999). They hence deserve to be better understood in the development context.

**Although the ECAs' mandate and objectives are commercial, they engender significant developmental impacts in developing countries,** such as the creation of more and better jobs or the provision of capital and climate finance in/to developing countries (Klasen, 2015; Mostert et al., 2015). That is also why officially supported export credit may be connected to ODA, through the controversial "tied aid" (see Box 1), which represents today around 4% of total ODA (Fritz and Raza, 2014, 2015).

**Besides ECAs' activities are strictly regulated by hard and soft laws** designed by the World Trade Organization (WTO), the OECD, the Berne Union as well as by the EU for European ECAs, as outlined in Box 2. This is meant to encourage ECAs in their efforts to do more in terms of transparency (through their reporting activities), level the playing field in order to encourage competition among exporters based on the quality and price of their goods and services exported (Drysdale, 2014), and foster responsible and sustainable investment.

<sup>24</sup> "Typically, risks arise from non-payment for political or commercial reasons. Political causes of loss can be the lack of hard currency in the buyer's country or, for example, wars, civil unrest or a payment moratorium imposed by a government. Commercial risks include payment defaults by the customer or insolvency leading to temporarily uncollectible receivables or full write-offs".

<sup>25</sup> ECAs may also complement private-sector coverage for short, medium and long-term marketable risks, provided they comply with EU state aid rules. Besides, ECAs in OECD countries can cover "all political risks, including those relating to contracts with public buyers, borrowers or guarantors; commercial risks relating to contracts with private buyers, borrowers or guarantors in non-OECD-countries and the Czech Republic, Hungary, Mexico, Poland, South Korea and Turkey and; commercial private buyer risks in the remaining OECD-countries with a risk period of two years or more." (<http://www.osce.org/secretariat/32797?download=true>)

<sup>26</sup> As demonstrated by the increase of 35% on average of EU Member States' support to their national ECAs.

<sup>27</sup> As explained in the EBF (2011) report on export finance, "ECA covered export credits are often the only possibility to conduct business in certain emerging and developing countries since private sector companies (i.e. insurance undertakings, banks) do not provide finance in these regions".

## Box 1: Definition and different forms of tied aid

Tied aid is a type of aid that is “in effect (in law or in fact) tied to the procurement of goods and/or services from the donor country and/or a restricted number of countries. It includes loans, grants or associated financing packages with a concessionality level greater than zero percent, provided under a strict set of guidelines”. ECAs shall not provide tied aid that has a concessionality level of less than 35%, or 50% if the beneficiary country is a Least Developed Country (LDC) (unless exception). So it is similar to export credit but it provides better terms (interest rate; repayment; grace period).

Tied aid can take the form of: **a) ODA loans** as defined in the “DAC Guiding Principles for Associated Financing and Tied and Partially Untied Official Development Assistance (1987)”; **b) ODA grants**, as defined in the “DAC Guiding Principles for Associated Financing and Tied and Partially Untied Official Development Assistance (1987)”; and **c) Other Official Flows (OOF)**, which includes grants and loans but excludes officially supported export credits that are in conformity with the Arrangement; **or d) any association**, e.g. mixture, in law or in fact, within the control of the donor, the lender or the borrower involving two or more of the preceding”.

Source: OECD Arrangement, 2016.

That said, these regulations and agreements often came in response to some of the critics addressed to ECAs, such as the nature of their investments (Peperkamp, 2006; ESCR); their environmental, climate and social impacts (ECA-Watch, 2010); and their contributions to debt creation in developing countries (Sundsbo, 2011). The latter issue was particularly important: ECAs’ support for an export includes a counter-guarantee from the government of developing countries, pledging payment in case of default. This mechanism allowed ECAs to shift the original private risk of the company involved to the governments of developing countries, thus contributing to their total external official debt - without contributing to sustainable development (Both Ends, 2004).

By levelling the playing field, these regulations also facilitate ECAs’ “cooperation, co-insurance, and reinsurance agreements [...] in different countries”; between ECAs and also between ECAs and private market players or multinational institutions” (Schone a, p.29, 2015). Such alignment even goes further than OECD countries with for example the Export-Import Bank of Korea following the OECD arrangement, and with the announcement that the United States and China agreed to open talks on setting guidelines for export credit financing, that - “tak[e] into account varying national interest and situations – [and] are consistent with international best practice” (Schöne b, 2015). Importantly however, these negotiations do not include environmental and social issues as well as do not take anti-corruption policies into consideration.

So while regulation is most developed on financial conditions of export finance in the OECD, they are yet to be designed on sustainability criteria, even though “as agencies that operate with taxpayer money under a governmental mandate, there is a strong policy argument that the ECAs should ensure the economic activities they support, at a minimum, do not put people and the environment at risk” (Saldarriaga and Shemberg 2014). This policy argument is further strengthened by the universal nature of the 2030 Agenda - so applying to all countries and supporting other countries in achieving the SDGs - as well as the concept of policy coherence for sustainable development (PCSD).

## Box 2: Regulations framing ECAs' activities

The **OECD "Arrangement"** (legally binding only for EU member states' ECAs - under Art. 1 of Regulation (EU) No. 1233/2011; otherwise non-legally binding). The Arrangement sets the export credit terms and conditions that may be supported by its Participants (e.g. minimum interest rates, risk fees and maximum repayment terms), and is regularly reviewed by its Participants. "In practice, this means providing for a level playing field (whereby competition is based on the price and quality of the exported goods and not the financial terms provided) and working to eliminate subsidies and trade distortions related to officially supported export credits" (OECD, 2013).

**The OECD Principles and Guidelines to Promote Sustainable Lending Practices** (not legally binding): "to ensure that the provision of official export credits to public or publicly-guaranteed buyers in IDA-Only countries (i.e. the poorest countries that are only eligible for interest free loans and grants from the International Development Association of the World Bank) should reflect sustainable lending practices, i.e. lending that supports the buyer country's economic and social progress without endangering its financial future and long-term development prospects." (OECD, 2013)

The **OECD Recommendations or Common Approaches** (not legally binding): these include the OECD Recommendation on Bribery and Officially Supported Export Credits, the Recommendation on Common Approaches for Officially Supported Export Credits and Environmental and Social Due Diligence, the Principles and Guidelines to Promote Sustainable Lending Practices in the provision of Official Export Credits to Low- Income Countries. It also encourages its members to promote the OECD MNE guidelines among appropriate parties involved in applications for officially supported export credits as a tool for responsible business conduct in a global context (OECD, 2012, 2016).

**The WTO's Agreement on Subsidies and Countervailing Measures** (mandatory for signatory countries): The WTO Agreement regulates the use of subsidies and describes the measures countries may take to counter the effect of subsidies. Most export credits are considered to be allowed subsidies as long as they respect conditions set out by the OECD Arrangement.

**Regulation(EU) No 1233/2011** (legally binding for EU ECAs): This regulation stipulates that the guidelines contained in the OECD Arrangement and the specific rules for project finance apply in the Union. It further sets out the transparency and reporting measures to be applied, including how environmental risks, which can carry other relevant risks, are taken into account in member states' ECAs activities.

**Article 21 of the Lisbon Treaty**<sup>28</sup> (legally binding for EU ECAs): "The Union's action on the international scene shall be guided by the principles which have inspired its own creation, development and enlargement, and which it seeks to advance in the wider world: democracy, the rule of law, the universality and indivisibility of human rights and fundamental freedoms, respect for human dignity, the principles of equality and solidarity, and respect for the principles of the United Nations Charter and international law".

Article 21.2(d): "(...) foster the sustainable economic, social and environmental development of developing countries, with the primary aim of eradicating poverty".

The article remains the key benchmark against which the policies applied to export credit transactions are to be evaluated (EU, 2013).

**The Berne Union** is the biggest network of the international credit and investment insurers, which facilitates information exchange, sharing of expertise, and networking among its members. All members follow a set of principles that focuses on sharing implementing and promoting best practices in the export credit industry - including taking into account environmental issues through their activities.

Source: Compiled by the authors.

<sup>28</sup> Consolidated Version of the Treaty on European Union. 26.10.2012. C 326/13

## 4.2. Criteria of sustainability or development

The main criteria for sustainability and development applying to ECAs are the ones of the OECD Recommendations, and Article 21 of the Lisbon Treaty, which ensures that ECAs objectives are in line with EU treaties and policies. All of these apply to the EU ECAs, covered in this paper, focusing on the Belgian Delcredere | Ducroire (DD); the French Compagnie française d'Assurance pour le commerce extérieur (COFACE); the German Euler Hermes Kreditversicherungs-AG (EULER HERMES); the Dutch Atradius NV (ATRADIUS) and the UK Export Finance (UKEF). In 2014, these represented about 73% of the premiums - credit insurance - private market, with Euler Hermes as a leader with 34% market share (Euler Hermes, 2016).

They are all part of the OECD Arrangement and follow the OECD Recommendations (see Box 3), meaning that they need to:

1. Ensure that any projects they finance comply with the environmental and social local legislation in place;
2. Require environmental and social due diligence and post-issue monitoring to ensure these projects are aligned with international standards; most commonly the World Bank Safeguard Policies (especially for non-finance projects) and IFC's Performance Standards on Environmental and Social Sustainability 2012 (for project finance);
3. Apply international standards anywhere where they are more stringent than their local counterparts; and
4. Benchmark against the World Bank Safeguard Policies and/or the standards of other Multilateral Financial Institutions (AfDB, ADB, EIB...) in particular circumstances allowed by the OECD Common Approaches.

Box 3: The OECD recommendations in practice

### The key points of this agreement are:

- the screening of all applications for credit insurance in order to identify the projects that are likely to have a negative environmental or social impact;
- the classification of projects requiring an in-depth analysis into three categories (A, B, C), depending on the scope of the potential environmental and social impact;
- review, which assesses all potential impacts, and must be based on an Environmental and Social Impact Assessment (ESIA) for most sensitive projects (category A);
- internationally recognised environmental standards: in addition to host country standards, international standards drawn up by the World Bank Group must be met. Projects may also meet other relevant standards;
- if necessary, the implementation of specific environmental and social conditions that must be met before a guarantee is issued on a given project, and/or environmental and social monitoring;
- disclosure of environmental and social information before a final commitment to grant support (ex-ante disclosure). The Recommendation implies to make environmental and social information (environmental and social impact assessment, for instance) publicly available at least 30 calendar days before final decision. Potential exceptions to the disclosure procedure, due to commercial confidentiality or to a particularly competitive context will have to be justified;
- disclosure, at both a national and OECD level, of the information related to category A and B projects undertaken (ex-post disclosure);
- common reporting and monitoring procedures for OECD Members, aimed at avoiding unfair competition linked to environmental and social requirements

Source: COFACE Environmental and Social Commitments, 2016.

As shown in the Annex on sustainable criteria for selected ECAs, the ECAs go further than the OECD Recommendations by setting up their own sustainability policies; or by joining certification bodies such as the UN Global Compact (Atradius, COFACE, Euler) or the Equator Principles (UKEF). The ECAs' environmental and social policies are nonetheless rather aligned, which is key as they easily collaborate with one another on a number of projects (for example COFACE has signed cooperation agreement with all four of these ECAs).

In practice, there seems to be some differences though on how thoroughly these sustainability policies are applied, or at least reported. The Annual Review of Member States' Annual Activity Reports on Export Credits (EU, 2014) shows that: i) all ECAs declare examining applications for export credit from an environmental perspective; ii) DD, COFACE, Euler Hermes and Atradius explicitly refer to social issues, and iii) Euler Hermes and DD go further by applying human rights considerations irrespective of the scope of the Common Approaches, and iv) only Atradius refers to fundamental labour rights; finally v) all ECAs but the UKEF declare applying more ambitious standards sometimes because of their own legislation.

### **Recent development in sustainability applying to ECAs activities**

The OECD Recommendations have been regularly updated, three times during the last decade. The last updates in 2012 and 2016 include a stronger focus on human rights, where the latter explicitly requires ECAs to screen all applications for export credit for severe human-rights risks. Where such risks exist, they should be further assessed if necessary through a human rights due diligence.<sup>29</sup>

This change reflects the growing recognition of international guidelines such as the UN Guiding Principles (UNGPs) (2009) and pushes both development and commercial financial institutions to act more responsibly and integrate these guidelines throughout their activities. As underlined by Apelman & Olming (2015) “[o]ne of the advantages of the UNGPs is that they improve transparency and the ability to discuss human rights risks within and between companies [...] They also make a clear distinction between business and government responsibility. This is particularly helpful and useful for ECAs given their dual role as state bodies, designed to support and interact with the business community in a global context”. As a result, the Norwegian Export Credit Guarantee Agency (GIEK) strengthened its approach in integrating human rights in their due diligence (Shift, 2016); and recently the Thun Group - a group of commercial banks, was created with the purpose of understanding how the UNGPs apply to the banking industry, with a view to integrating these in their activities.

For ECAs, the OECD Multinational Guidelines (2011) are also a key tool in at least two ways: i) ECAs must promote the OECD Guidelines through “consideration of responsible business conduct as a criterion of financing decisions, [but they also have] an obligation to espouse good corporate behaviour themselves” (Nieuwenkamp, 2016); and ii) ECAs, as multinational or even as government-controlled entities companies, and the companies they finance must therefore respect such guidelines.

Therefore, in the context where states committed to implement the OECD Guidelines and the UNGPs, ECAs are increasingly under pressure to integrate these guidelines both across their organisations but also throughout their stream of activities (see Box 4). Such requirements will ultimately ensure that ECAs support more and better trade, which is crucial considering a large part of their activities happen in developing countries.

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<sup>29</sup> <http://www.shiftproject.org/news/oecd-human-rights-due-diligence-export-credit-agencies/>

## Box 4: Cases of the implementation of the OECD MNE Guidelines in the context of ECAs activities

Recently, a case was brought to the OECD National Contact Point (NCP)<sup>30</sup> against a Canadian mining company for its gold activities in China the company refused to participate in the NCP process, which led to the following NCP conclusion “the Company’s non-participation in the NCP process will be taken into consideration in any applications by the Company for enhanced advocacy support from the Trade Commissioner Service and/or Export Development Canada (EDC) financial services, should they be made.” So, more and more, businesses will need to adopt responsible business conduct to get support from export credit finance. In practice they need to have responsible value chains, which may include conducting sustainability due diligence on their customers further down the value chain.

Another case brought to the NCP this time against an ECA (Atradius), was for their failure to comply with the OECD Guidelines in the context of its financing of a dredging project in northeastern Brazil which engendered severe human rights and environmental impacts. The Dutch NCP in its initial assessment considers Atradius to be subject to the OECD guidelines (even though it is an export credit insurance subject to the Dutch government’s policies), and thus a mediation process was engaged with the relevant parties. ECAs are therefore pushed to integrate further sustainability systems in their export finance activities, making these ultimately more developmental.

### 4.3. Challenges and opportunities - need for reforms?

In considering the challenges and opportunities related to the sustainability dimension of ECA activities, it is important to underline the **difficulty of introducing reforms**, “*given the complex range of actors, vested interests, and policy arenas in which official export credit policies are negotiated*” (Harmon et al., 2005).

#### Globalisation of standards

Just as ECAs needed to establish a level playing field in regards to the financial conditions of export finance in the OECD and non-OECD countries - through their International Working Group (IWG) on export credit - to encourage competition among exporters based on quality and price of goods and services exported, thus promoting more and better trade, they will need to undertake the same negotiations and efforts to align their sustainability standards. As demonstrated by the slow progresses within the OECD, and their exclusion from the IWG negotiations, the implementation of sustainability criteria poses serious challenges, which nonetheless need to be overcome to foster trust and confidence in trade, and fair competition among ECAs.

That said, some signs are rather encouraging, for example some non-OECD ECAs have implemented the OECD Recommendations (e.g. the Korean export credit agency), which is also one of the roles of the EU according to Regulation (EU) No. 1233/2011. Besides some trends have emerged that may well support the development of internationally accepted sustainability standards:

- **First, the UNGPs, OECD Guidelines, OECD Recommendations, and IFC Performance Standards (IFC PS) are all recognised by the international community**, including the states which commit to implement the UNGPs and the OECD Recommendations and Guidelines (for OECD member states) through their policies, development and commercial financial institutions and the private sector who are fostering and/or applying the aforementioned guidelines and the IFC PS.
- **Second, the increased cooperation between ECAs, between ECAs and other financial institutions and private sector players should push all these actors to align their**

<sup>30</sup> The Guidelines are supported by a unique implementation mechanism of National Contact Points (NCPs), agencies established by adhering governments to promote and implement the Guidelines. NCPs assist enterprises and their stakeholders to take appropriate measures to further the observance of the Guidelines. They provide a mediation and conciliation platform for resolving practical issues that may arise with the implementation of the Guidelines.

**sustainability standards** with a view to facilitate the implementation of projects, build synergies to reduce costs, and benefits from more business opportunities arising from big projects necessitating the financing of several institutions.

- **Third, ECAs have a bargaining power over businesses aiming to export, and could use it to foster and globalise the UNGPs and OECD guidelines implementation.** A ‘stick and carrot’ approach could punish companies acting irresponsibly by limiting their financing possibilities; and reward companies acting responsibly (following OECD Guidelines and/or UNGPs) by allowing for better financing conditions. For example, Atradius requires its counterparts to “*declare that they are familiar with the OECD Guidelines, and that they will apply these Guidelines in their business operations to the best of their ability.*” (Both Ends, 2007).

Sometimes absent from the sustainability policies and standards as implemented by ECAs, grievance mechanisms should be systematically provided to affected communities who wish to file complaints to an ECA. This ensures that the rights and interests of communities are respected (besides the stakeholder engagement procedures as stipulated in the OECD Arrangement).

### **From the globalisation to the application of sustainability standards**

Although sustainability standards are often well understood, it is often unclear to financial institutions including ECAs how to translate these in practice. Atradius for example notes that the “*OECD Guidelines are too general and vague, which makes it difficult to use them to assess transactions in advance*” (OECD, 2015). In the same vein the EU acknowledges that “[i]t is difficult to define a precise benchmark for measuring ‘compliance’ [of EU ECAs] in EU law” (EU, 2014). This ‘lost in translation’ leads to the following observation: even though “*OECD framework has more recently been enriched by the adoption of additional non-binding policy guidelines and understandings on environmental standards and sustainable lending, these arrangements have generally done little to assuage concerns that ECAs promote harmful forms of exports and investment*” (Sant’Ana, 2013).

Policy-makers, institutional actors, practitioners and civil society organisations should therefore help translate principles and guidelines into practice, in order to facilitate the implementation and operationalisation of sustainability standards by ECAs. They should also focus on ensuring policy coherence between trade policy and other policy areas.

Offering technical assistance or capacity building to EU and non-EU/OECD ECAs in this sense could further be a potential incentive for ECAs to systematically apply sustainability criteria to their organisations and their activities. Monitoring and reporting on the progress of the implementation of sustainability standards, and translating the financial gains of the latter, could contribute to making the business case for ECAs to (better) implementing sustainability standards. Further, and as noted by Apelman & Olming (2015), “[t]he Berne Union is a well-placed institution to support the exchange of good practice on all aspects of trade and export finance including collaboration around voluntary sustainability standards”.

Finally, a closer collaboration could be established between MDBs/DFIs, which have extensive experience in sustainability standards, and ECAs, which are slowly implementing these. This has started under the Berne Union, but should be enhanced. As importantly, it will ensure the spread and use of global sustainability standards on export credit activities. However, only a collaborative, gradual approach and soft transition towards the implementation of global sustainability standards is likely to succeed in the short and middle term.



## 5. Synergies and complementarities

*“ECAs and DFIs have very different purposes, mandates and in the case of multilateral institutions, ownership structures. However, there are many important areas of overlap where the pursuit of different mandates and different policy objectives open up the possibility and often the necessity of active collaboration.”* (Sharma, 2014)

Keeping the above quote in mind, collaboration between ECAs and DFIs, however, in the past mostly took place in developing countries that imported goods and services from ECAs' home countries representing a source of development impact, thus, being eligible for financing support from ECAs. Most of the times, however, such collaboration was opportunistic and happened on a project-by-project basis with a number of challenges attached, relating to for instance the differing roles and documentation approaches, the ability to allow for different types of financing and difficult collaboration on project level, if too many parties are involved (Sharma, 2014).

### 5.1. Why cooperation?

However, according to Sharma (2014), “both the need and opportunities for collaboration between the ECAs and DFIs are growing rapidly” for various reasons: i) there is an increasing demand for trade and investment flows from emerging and developing markets as growth and consumption rates rise; ii) lower trade and investment barriers with increasing mobility of production and services locations as well as multi-country sourcing of goods and services; iii) project sizes tend to become larger requiring more financial partners to be involved; iv) need for better risk diversification and distribution due to higher project volumes and trade finance risks; v) the Basel III<sup>31</sup> recommendations make commercial banks less engaged in long-term exposures; and vi) market volatility and currency risks demand more local currency financing, thus, involvement of DFIs. Hence, the institutions' differences but also complementing abilities and characteristics make successful collaboration more likely and needed, as illustrated in Table 4.

**Additionally, EIC (2014) lists a number of other reasons for greater collaboration between DFIs and ECAs:**

- The insurance capacity of ECAs could be used for development purposes against the backdrop of decreasing aid budgets or a reallocation of resources to other areas, such as migration;
- Moving from ‘billions-to-trillions’ requires using scarce development aid more efficiently and effectively in line with the Paris Declaration and increasing aid effectiveness;
- Donors could tap into ECAs' (re-)insurance capacity, leading to “substantial amounts of non-developmental capital and risk capital of the development finance community can be freed up and used for other important development purposes”;
- Both ECAs and DFIs are directly or indirectly government-owned and supervised, facilitating better cooperation and coordination.

Particularly the aspects of limited direct lending capacities and fiscal constraints of many of the shareholders make it even more pertinent for MDBs but also IFIs and DFIs to fully perform their catalytic and leveraging role in mobilising financing from various sources that have not yet been (fully) tapped (World Bank, 2013).

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<sup>31</sup> "Basel III" is a comprehensive set of reform measures to strengthen the regulation, supervision and risk management of the banking sector. These measures aim to improve shock absorption, improve risk management and governance, and strengthen banks' transparency and disclosures.

Table 4: Differences, comparative advantages and synergies between DFIs and ECAs

	DFIs	ECAs
<b>Differences:</b>	<ul style="list-style-type: none"> <li>→ wider mandates to promote social and economic development of their member developing countries</li> <li>→ fostering inclusive and sustainable growth</li> <li>→ provision of financing, advisory services and other forms of development support</li> </ul>	<ul style="list-style-type: none"> <li>→ principal focus, a contribution to their domestic economies by promoting and financing exports from the home country</li> </ul>
<p>however, "<b>opportunities for collaboration arise in emerging markets</b>"</p> <ul style="list-style-type: none"> <li>→ both DFIs and ECAs are active there and serving the same clients from their respective mandates</li> <li>→ both are owned directly or indirectly, by the national governments</li> </ul>		
<b>Comparative advantages:</b>	<ul style="list-style-type: none"> <li>→ strong presence in developing/emerging countries</li> <li>→ extensive local networks with local offices and staff on the ground creating local market intelligence</li> <li>→ good local relationships with borrowers, public agencies and local financial institutions</li> <li>→ availability of a diverse range of instruments enables DFIs to intervene at various levels</li> </ul>	<ul style="list-style-type: none"> <li>→ significant risk appetite and high credit ratings</li> <li>→ willingness to provide or guarantee long tenor financing and competitive financing rates</li> <li>→ strong customer base importing from ECAs' home country markets</li> </ul>
<b>Synergies:</b>	<ul style="list-style-type: none"> <li>→ valuable commercial contacts interesting for ECAs that wish to expand their markets (cost saving and more effectiveness)</li> <li>→ keen to mobilise additional sources of financing for their partners, so bringing in ECA finance yet another source of long-term finance</li> </ul>	<ul style="list-style-type: none"> <li>→ enable DFIs access to their domestic client base</li> <li>→ more comprehensive value proposition through partnering with DFIs offering local currency financing, equity finance, small-scale financing and local manufacturing support</li> </ul>
<p><b>Shared ambitions:</b></p> <ul style="list-style-type: none"> <li>→ similar commitments to global best practices: environmental and social standards, anti-money laundering and financing of terrorism safeguards, and due diligence procedures</li> <li>→ goal of diversifying and sharing risks (similar risk profile and asset portfolio in emerging markets)</li> <li>→ risk sharing attractive for both to maintain high credit ratings</li> </ul>		

Source: Compiled from Sharma (2014).

### Challenges to overcome...

**Despite opportunities and potential synergies calling for more collaboration between DFIs and ECAs, various challenges need to be overcome**, as more collaboration seems to be an important chance that should not be missed given today's challenges requiring multi-actor partnership approaches. Sharma (2014) identifies three main challenges: 1) differing mandates with own internal policies and approaches limits possibilities of cooperation, 2) relatively less interaction at business operation level, and 3) differing operating procedures, credit and pricing parameters, tenor and currency preferences, and transaction eligibility criteria.

In practice there are further challenges related to the 'preferred creditor status' of institutions like the EIB<sup>32</sup> and IFC have from host countries, which ECAs do not get. This difference in exposure to risk makes ECAs ultimately more reluctant to jointly engage with DFIs, which are better protected.<sup>33</sup> Additionally, in practice ECAs tend to be more conservative, relying on foreign currency and working mainly with large firms, while

<sup>32</sup> It benefits from *de jure* preferred creditor status (PCS) for loans to sovereigns/guaranteed by sovereigns.

<sup>33</sup> "As a multilateral development institution, IFC enjoys a de facto Preferred Creditor Status. This means that member governments grant IFC loans preferential access to foreign currency in the event of a country foreign exchange crisis. The Preferred Creditor Status therefore mitigates transfer and convertibility risk for IFC and its B Loan participants" (information on IFC's preferred creditor status here). For a discussion, see Perraudin et al. (2016).

IFIs/DFIs, such as EIB or IFC are increasingly seeking to engage SMEs in local currency financing. The cooperation between ECAs and DFIs is also often hampered by the question of ‘who leads whom’: who should be the lead financier in joint projects, which is also an issue in public-private partnerships (Bilal et al., 2014).

Another issue relates to subsidies provided to ECAs by their governments, which allows them to operate at lower than market prices, and on cheaper terms than IFIs that finance themselves on the financial market. This in turn raises questions as to whether IFIs/DFIs are too market-driven, and thus more risk-averse and conservative than would be required to maximise their impact in terms of development outcomes. This is also part of the rationale for blended finance, which provides subsidies in various forms (e.g. grant, technical assistance, interest rate subsidies, risk mitigating mechanisms) to leverage IFIs/DFIs and other private finance, under specific conditions, for more impactful investment (Bilal, S. and S. Große-Puppenthal, 2016a; IFC, 2016b). More fundamentally perhaps, ECAs are thus often perceived, including by some IFIs, as distorting the market and potentially crowding out private finance, a complaint that has also been addressed though to DFIs (Stauffenberg, von D. and Rozas, 2011; Tsuji, 2013) and in particular blended finance (Bilal and Krätke, 2013; Eurodad, 2013).

So, while cooperation remains somewhat difficult and thus limited, it is happening in some instances, as illustrated by the discussion on this issue within the EU Platform for Blending in External Cooperation (EUBEC), summarised in Box 5. Addressing some of these challenges can help open up various opportunities for further cooperation between DFIs and ECAs.

Box 5: EUBEC discussion on collaboration between DFIs and ECAs

“Regarding the potential collaboration between Finance Institutions [“FIs”] and Export Credit Agencies (“ECAs”), participants [to the EUBEC] discussed some of the possible issues of bringing in the ECAs and commercial banks in public sector programmes financed by the EC and the FIs. Some financial institutions pointed out that there is a danger of ECAs crowding out commercial finance that is actually available, thus distorting the market and setting the wrong incentives. FIs also noted that sharing the preferred creditor status would not bring in additional benefits, since ECAs usually are preferred creditors as lenders. FIs expressed their view that sharing the preferred creditor status with commercial banks is not an option for the FIs in public sector projects where the sovereign acts as borrower or guarantor, while in private sector projects this is quite common. As pointed out by the FIs, European Banking Association and the Danish ECA, there are already examples of cooperation between FIs, commercial banks and ECAs in developing countries, such as the mixed credit schemes in Belgium, Denmark and Austria as well as the collaboration between FIs and ECAs in the context of the Berne Union in various areas.

The participants concluded that cooperation with ECAs and commercial banks in the context of blending facilities is already a possible option, and no further sessions will be needed. Participants were invited to propose concrete project ideas involving the ECAs and commercial banks for consideration in the blending frameworks.

Source: European Commission (2016c).

### ...to unlock synergies

**Keeping those challenges in mind, there are a number of areas where collaboration between DFIs and ECAs can unlock synergies**, as both often operate in the same markets, often aiming at the same customers. This means they collect information and data on projects, which potentially are of common interest related to trade, insurance and investment volumes. A more systematic and frequent exchange of such data and information could enhance the effectiveness of market analysis and strategy development keeping in mind that they have to adjust continuously to “changing political, economic and market conditions across many of the emerging markets in which they operate” (Sharma, 2014).

The fact that DFIs, like ECAs, are owned directly or indirectly by national governments could facilitate greater synergies. This could be further facilitated in countries where ministries of trade and development are merged in the ministry of foreign affairs, as is the case for instance in the Netherlands, Sweden and Finland. Combining these issues under one roof could increase the likelihood to interact, exchange, coordinate and cooperate on a more regular and systemic basis, both at the formal and informal level.

**However, there is a need for a better understanding of the respective business practices and priorities of DFIs and ECAs**, which very much relates also to the lack of cross-institutional communication. Cooperation and synergy between DFIs and ECAs must also be steered by policy-makers, so as to foster a more conducive institutional and political environment and provide the right incentives for each institution to cooperate.

While comparative advantages are mostly relating to commercial and practical operations and practices, both would highly benefit from **collaborating in terms of policy coordination**, as there seem to be similar objectives with regard to global best practices on environmental and social issues, corporate governance, and anti-money laundering and combating the financing of terrorism (Sharma, 2014). **More systematic exchange** of views and agreement on common approaches towards documentation could make transactions involving both types of institutions more efficient. Similarly, knowledge transfer and capacity building of customers and other local actors (local financial institutions or authorities) on trade and investment promotion can yield significant synergies.

Though DFIs have different overall interests than ECAs, **better coordinated knowledge transfer of expertise and service delivery** can enhance market standards and efficiency while avoiding duplication of efforts. Additionally, new initiatives are more likely to kick-off, as resource constraints can be overcome more easily when joining forces and funding. An example of such programmes are DFIs that are selling down risk to trade credit insurers, hence, bringing in ECAs will allow for more business in smaller economies, “where the DFIs can offer greater levels of support” (Sharma, 2014).

## 5.2. Criteria of sustainability

**In the context of trade and investment promotion**, the G20 Trade Ministers recently agreed, after their meeting in Shanghai in July 2016 under the Chinese G20 Presidency, on the *G20 Guiding Principles for Global Investment Policymaking* with the aim to “promote inclusive, robust and sustainable trade and investment growth”.<sup>34</sup> These are nine non-binding principles that shall provide guidance for investment policymaking to achieve three objectives:

- 1) fostering an open, transparent and conducive global policy environment for investment,
- 2) promoting coherence in national and international investment policymaking, and
- 3) promoting inclusive economic growth and sustainable development.

Particularly the last objective seems pertinent when it comes to promoting trade and investment in a way that is both sustainable and conducive for shared prosperity, as those principles can “serve as a reference for national and international investment policymaking, in accordance with respective international commitments, and taking into account national, and broader, sustainable development objectives and priorities”.<sup>35</sup>

While the G20 nine guiding principles are all pertinent, two are of particular relevance in the context of this Section:

<sup>34</sup> <http://www.oecd.org/investment/g20-agrees-principles-for-global-investment-policymaking.htm>

<sup>35</sup> G20 Trade Ministers Meeting Statement, July 2016, Annex III: G20 Guiding Principles for Global Investment Policymaking.

- Principle VII: *Policies for investment promotion should, to maximise economic benefit, be effective and efficient, aimed at attracting and retaining investment, and matched by facilitation efforts that promote transparency and are conducive for investors to establish, conduct and expand their businesses.*
- Principle VIII: *Investment policies should promote and facilitate the observance by investors of international best practices and applicable instruments of responsible business conduct and corporate governance.*

Key guiding dimensions for investment promotion thus include transparency as well as responsible business conducts and corporate governance.

**Table 5 compares sustainable criteria for DFIs and their national ECA counterparts, to identify overlaps and differences.** Both DFIs and ECAs share the adherence to the 2012 IFC Performance Standards on Environmental and Social Sustainability, which require clients to meet those eight Performance Standards throughout the life of an investment. They relate to:<sup>36</sup>

1. assessment and management of environmental and social risks and impacts;
2. labour and working conditions;
3. resource efficiency and pollution prevention;
4. community health, safety, and security;
5. land acquisition and involuntary resettlement;
6. biodiversity conservation and sustainable management of living natural resources;
7. indigenous peoples;
8. cultural heritage.

**It shows that DFIs, which have a development mandate, and ECAs, which have primarily commercial motives, apply very similar sets of sustainability criteria.** This increases the chances to improve the sustainability and responsibility throughout operations regardless of the specific mandate of the concerned institutions.

In the case of the Extractive Industries Transparency Initiative (EITI) for instance, both DFIs (i.e. EIB, IFC, KfW) and ECAs (i.e. France, Germany, UK) commit towards transparency and accountability in the extractives sector, while implementation of EITI itself helps to deliver on other commitments made under the Equator Principles (relating to community consultation and grievance mechanisms) or the UN PRI (Principles 3: disclosure on ESG issues; and 5: working together to enhance effectiveness in implementing the UN PRI) (EITI, 2010).

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<sup>36</sup> IFC Performance Standards on Environmental and Social Sustainability, effective as of 1 January 2012.

Table 5: Overview of sustainability criteria for selected DFIs and their national ECA counterparts

	Belgium		France		Germany		Netherlands		UK	
<i>DFIs and ECAs</i>	BIO	Delcredere - Ducroire	Proparco	Coface	DEG	Euler Hermes	FMO	Atradius <sup>37</sup>	CDC <sup>38</sup>	UKEF
<b>EDFI Principles<sup>39</sup></b> for Responsible Financing, including <ul style="list-style-type: none"> <li>• UN Declaration of HRs</li> <li>• ILO Core Conventions</li> <li>• IFC Performance Standards</li> <li>• IFC EHS Guidelines</li> </ul>	X	IFC PS	X	IFC PS & IFC EHS	X	IFC PS	X	IFC PS	X	IFC PS
OECD Guidelines for MNEs		X	X			X				
UN Guiding Principles		X	X	X		X		X		X
UN Global Compact			X	X		X		X		
World Bank's Safeguard Policies		X		X		X				X
Equator Principles					X		X			X
UN PRI					X		X		X	
Global Reporting Initiative			X		X		X			
EITI										
<p>→ <b>For all ECAs above:</b></p> <ul style="list-style-type: none"> <li>• <b>OECD Recommendations (Common Approaches)</b> <ul style="list-style-type: none"> <li>→ Any project should comply with the legislation of the host country, and with international standards (World Bank Group) when these are more stringent.</li> <li>→ makes explicit reference to the <b>UN Guiding Principles</b>: “business enterprises have the responsibility to respect human rights, as outlined in the ‘Guiding Principles on Business and Human Rights: Implementing the United Nations “Protect, Respect and Remedy” Framework’ endorsed unanimously by the United Nations Human Rights Council on 16 June 2011</li> </ul> </li> <li>• <b>Berne Union Guiding Principles<sup>40</sup></b> → voluntary principles for ECAs to “operate in a professional manner that is financially responsible, respectful of the environment and which demonstrates high ethical values – all in the best interest of the long-term success of our industry”</li> </ul>										

Source: Authors' elaboration.

<sup>37</sup> <https://group.atradius.com/about-us/corporate-responsibility.html>

<sup>38</sup> CDC. 2016. Annual Sustainability Review 2015–2016 - Investing responsibly.

<sup>39</sup> 'all investment activities must have positive impacts for the local community, particularly in the area of social rights and the environment'

<sup>40</sup> <http://www.berneunion.org/about-the-berne-union/our-principles/>

### 5.3. Way forward

Overall, looking at some of the challenges and opportunities for DFIs-ECAs collaboration, it seems that more **systematic effort is needed** both for mutual benefit as much as for emerging market countries and customers who are the common target segment. However, Sharma (2014) rightly stresses that joint operations and projects “will be sustainable only if it results in tangible and demonstrated value-added for all parties”, which requires full commitment by all participants and that the objectives are “realistic and consistent with the business and policy goals of all stakeholders”, which can then ultimately lead to benefits outweighing the efforts.

Others, such as Vassard (2015), argue along similar lines, where public institutions should be more concerned with **alleviating risk and crowding in private investments**, hence ECAs could concentrate on their “home turf”. By referring to the €625 million Lake Turkana Wind Power project in Kenya, where the EIB and AfDB provided the majority of senior debt, besides other Nordic DFIs (from Denmark, Norway and Finland), the Danish ECA EKF covered tranches of approximately €125 million, Vassard (2015) underlines the ECAs’ pertinent role in bridging the gap between national, regional and MDBs *vis-a-vis* private investors, recognising however that successful project design and implementation takes time. In this regard, it is also worth noting the claim that as part of the agreement with the Danish ECA EKF, the Danish turbine supplier Vestas obtain the turbine procurement without tendering, arguably a controversial form of tied aid.<sup>41</sup>

DFIs cooperation with ECAs and more commercial financiers can become even more common in financing infrastructure, through parallel co-financing structures in private sector projects (e.g. greenfield PPPs).

According to EIC (2014) “other forms of cooperation, such as insurance of loan exposure of DFIs or reinsurance of guarantee exposure of DFIs, are hardly existent”. This is partly related to the fact that “the risk appetite in the private market remains skewed toward medium tenors and away from longer ones”, while private sector actors recognise that new business could be triggered through co-insuring with ECAs and multilateral agencies, which enables the extension of tenors and increase business in less stable or development markets (MIGA, 2013).

Stephens and Smallridge (2002) underline that IFIs should not “compete either with the ECA in the country concerned (or with ECAs in other countries providing support for imports into the country concerned) or with commercial banks on trade finance in or out of the country concerned”, as IFIs should encourage, help and support ECAs’ development and operation in emerging markets by providing finance as trade and investment flows into the country as well as trade flows out of the country. Hence, they should be taking the role of a catalyst filling gaps both in terms of finance and experience and expertise.

EIC (2014) further suggests that “DFIs could catalyse substantial ECA insurance capacity by insuring DFI loan exposure or DFI guarantee exposure”, so that DFI finance could be used for more pressing development projects. Another way could be to syndicate DFI development loans to commercial banks, as DFIs, such as the EIB and IFC, have a great catalysing potential due to their preferred creditor status.

Annex 2 provides some illustrative cases of cooperation between DFIs and ECAs.

<sup>41</sup> It was reported in *Development Today* (Vol.XXV, no.12, November 2015) that the Lake Turkana project also involved “the Danish export credit agency EKF, which put up a DKK 1 billion guarantee, and the Danish supplier Vestas, which was both an owner in the project and the supplier of the 365 turbines. As part of the agreement, Vestas got the turbine deal without a tender, which was a controversial decision for the DFIs and AfDB.”

## 6. Conclusion

**DFIs and ECAs follow different institutional mandates and objectives to promote investments and exports.** In their operations both types of institutions follow certain principles, criteria and standards, which they need to comply with when operating in developing countries. While DFIs must focus on their development impact, ECAs have also to adhere to a number of principles and criteria, including in terms of sustainability. To a large extent, the sustainability principles required by DFIs and those of ECAs do converge. Besides, both the clients and customers they serve are similar as are the markets where they are active. Therefore, there are various opportunities to join forces across institutions to unlock more private investments that can contribute to the implementation of the 2030 Agenda bringing more and better jobs and prosperity, particularly in developing countries.

**If exports precede investments,** as suggested by recent systematic evidence, **the role of DFIs that promote sustainable investments in developing countries could be to more systematically build on ECA activities, clients and projects** to de-risk potential investment projects and bring in businesses that until that moment have only exported to those markets. By bringing in their capacities and capabilities, including the availability of a diverse range of instruments to intervene at various levels, DFIs can provide solutions, which can nicely complement activities by ECAs, on their side providing long tenor financing and being involved at different investment stages of projects. Doing so can then contribute to better and more impactful investments that allow for greater gains for domestic companies and domestic economy due to positive spillover effects from FDI firms to host country businesses.

**While collaboration until now has been rather limited, there are a number of factors however suggesting that more could be done.** This mainly relates to sharing knowledge and information on potential clients and contacts, so leveraging each other's networks and collected data, as well as to sharing information on project and investment opportunities in a more formalised and frequent manner. A more systematic exchange of views and agreement on common approaches towards documentation could at the same time make transactions involving both types of institutions more efficient.

**Thus, ultimately developing country markets could highly benefit from DFIs and ECAs complementing their instruments,** where:

DFIs...	ECAs...
⇒ could benefit from long-term finance from ECAs	⇒ could extend their value proposition through partnering with DFIs, which in turn offer local currency, equity and small-scale funding as well as local manufacturing support
⇒ play their role of catalysts by bringing in more and diverse investors and sources of funding for sustainable development projects	⇒ rely on a strong customer base importing from ECAs' home country markets
⇒ rely on their strong presence and local networks in developing/emerging countries	

**However, making their roles more complementary, and thus, increasing collaboration between DFIs and ECAs depends mainly on overcoming identified challenges** - both for the respective institutions themselves and cooperation challenges - and building on good practice and lessons in terms of activities, criteria and measurement/reporting. Doing so will allow (development) finance and investments and (commercial) export/internationalisation support to have a sustainable impact on development, if:

- activities are directed in a more sustainable and responsible manner towards countries and regions most in need, which requires balancing risk, return and development impact, and
- FDI and export activities have positive spillovers on domestic companies - both SMEs as much as larger ones - and their ability to sustainably enhance productivity levels and employment creation.



**Failing to do so, though, will be a missed chance** not only for public actors to diversify and better leverage funding sources to implement the 2030 Agenda, but more broadly to effectively achieve sustainability outcomes in promoting investment and trade linkages.

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## Annex 1: Sustainable criteria for selected ECAs

	<b>Delcredere   Ducroire (DD)</b>	<b>Compagnie française d'Assurance pour le commerce extérieur (COFACE)</b>	<b>Euler Hermes Kreditversicherungs-AG (EULER HERMES)</b>	<b>Atradius NV (Dutch State Business) (ATRADIUS)</b>	<b>UK Export Finance (UKEF)</b>
<b>Structure</b>	An autonomous state-owned agency that provides either insurance or lending or both	Private company with an exclusive government charter to administer public funds for export credit and/or investment support to domestic exporters and firms	Private company with an exclusive government charter to administer public funds for export credit and/or investment support to domestic exporters and firms	Private company with an exclusive government charter to administer public funds for export credit and/or investment support to domestic exporters and firms	Specialised government department within the executive branch or reporting to a central authority
<b>Value of transactions insured during the financial year in 2015</b>		€ 1.489 billion	€ 2.638 billion		€ 2,099 billion
<b>Share of activities in developing countries in 2015</b>	Over 49% (among which 16% in Africa)	Over 30% of turnover (of which around 16% in Mediterranean and African countries)	13% in Mediterranean countries, Middle East & Africa		
<b>Net income in 2015</b>	€ 8.9 million	€ 126.2 million	€ 302.5 million		€ 124.2 million
<b>Cooperation with other financial institutions, ECAs or private sector actors</b>  <b>The 5 ECAs are active in several credit insurance working groups:</b> <ul style="list-style-type: none"> <li>• EU</li> <li>• OECD</li> <li>• Berne Union</li> </ul>	Collaborates with other credit insurers, institutions or banks in Belgium and abroad - mainly in the context of foreign incorporation, joint insurance, reinsurance, parallel insurance and general co-operation framework agreements	COFACE has signed 20 MoUs including with Sinasure (China's ECA); Bancomext (Mexico's ECA); SBCE (Brazil)...  They have also signed 18 conventions for joint insurance, 21 conventions for reinsurance, and 6 for coinsurance with mainly ECAs from OECD countries;	Euler Hermes has cooperation agreements with ECAs from 37 countries, predominantly with ECAs in OECD countries	Atradius had previously concluded a MoU with Sinasure; with ECIC, a South African credit insurer; with OPIC, a US government development finance institution; with, ABGF, the Brazilian export credit agency and; with ATI, the pan-African multilateral export credit insurance agency.  Atradius currently collaborates with over 26 other insurers in the context of joint investment insurance, reinsurance	Collaborates with: Commercial finance partners 38 lenders; Commercial insurance partners 39 specialist insurance brokers; Other export credit agencies Reinsurance or cooperation arrangements.  ECGD agreed a partnership arrangement with the Export Guarantee Fund of Iran; a framework with Sinasure; and is a member of the African Trade Insurance Agency



<p><b>Common sustainability policies &amp; reference</b></p>	<p>Any project should comply with the legislation of the host country, and with international standards (World Bank Group) when these are more stringent.                  Apply the OECD Recommendation on Common Approaches on Officially Supported Export Credits and Environmental and Social Due Diligence;                  Apply the OECD Recommendation on Bribery and Officially Supported Export Credits                  Apply the OECD Principles and Guidelines to Promote Sustainable Lending Practices in the Provision of Official Export Credits to Low Income Countries</p>				
<p><b>Specific sustainability policies &amp; reference</b></p>	<p>Delcredere   Ducroire has an environmental and Social Policy, based on the <b>OECD Common Approaches</b>, and also promotes the <b>OECD MNE guidelines</b>; and follows the <b>IFC PS</b></p> <p><b>World Bank Safeguard Policies</b> are the default standards, i.e. when IFC/MFI not involved in project or when more stringent international standards (such as EU standards) not applied</p>	<p>COFACE has made environmental and social commitments, based on the <b>OECD Common Approaches</b>, which follows when appropriate the <b>World Bank's environmental and social safeguard policies for non-finance project</b>, and the <b>IFC PS for finance project</b>. Coface also follows the <b>IFC environmental health safety guidelines</b>. Coface is and is also part of the <b>UN Global Compact</b></p>	<p>EULER HERMES has an Environmental Guidelines, based on the <b>OECD Common Approaches</b> which follows when appropriate the <b>World Bank's environmental and social safeguard policies</b> or the <b>IFC PS</b>. Euler Hermes is also part of the <b>UN Global Compact</b>.</p>	<p>Atradius has a specific environmental and social policy, based on the <b>OECD Common approach</b>, and assess their environmental and social impacts using <b>IFC PS</b>. Atradius is also part of the <b>UN Global Compact</b></p>	<p>The UKEF has a Policy and practice on Environmental, Social and Human Rights due diligence and monitoring, which is based on: <b>OECD Common Approaches</b> and the <b>Equator Principles</b>. UKEF also applies <b>IFC PS</b>, and occasionally the <b>EBRD standards</b> and <b>World Bank Safeguard Policies</b></p>

## Annex 2: Examples of DFI-ECA cooperation

### The case of EIB export promotion

One of such examples, where a DFI or development bank interacts with an ECA is the ‘first-ever EIB facility for buyer credit financing for European SME and Midcap exporters’.<sup>42</sup> Pure trade promotion is mainly done at EU member states level though internationalisation support<sup>43</sup> to European SMEs can also be considered involving trade promotion elements. While national trade and investment promotion agencies, such as export credit agencies, provide credits, loans and guarantees to domestic firms, there is no such formal agency at the European level. However, both the Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs (DG Growth) and the EIB are actively supporting European firms to do investments and trade beyond the EU.

One such example is the EIB export financing facility, where the EIB partnered with Northstar Europe and Office du Ducroire (‘ODL’), the Luxembourgish ECA, which is the “first ever EIB facility to provide buyer credit financing”. It is a €50 million facility for Northstar Europe S.A. Luxembourg that provides ‘buyer credit financing’ to European SMEs and Midcap exporters, and the first time for the EIB to engage in export financing in support of the internationalisation of European firms.

By providing small buyer credits to importers, EU exporters can improve their working capital management. The Luxembourgish ECA will contribute by providing its securitisation guarantee product to the EIB and the facility as such will then allow Northstar Europe to support “eligible European exporters of capital goods and equipment to increase their exports with the backing of competitive financing for their buyers, in the form of buyer credit loans”.

Normally, ‘small’ ECA-backed structured loans have too high administration costs which undermine their financial viability for the larger credit suppliers”. This approach, however, based on a narrowly focused product suite, enables Northstar to provide such ‘small’ structured loans of this nature. While the “financing is provided by Northstar, from the funding from the EIB, to importers of European goods globally under an Export Purchase Loan Agreement, the scheme has the ODL guarantee with the support of the ECA of the exporter’s country.

### Trade support for development: the case of the Dutch Good Growth Fund<sup>44</sup>

The €700 million Dutch Good Growth Fund (DGGF) has been established by the Ministry of Foreign Affairs and Development Cooperation and provides financing and credit insurance for enterprises and investment funds in both the Netherlands and in low- and middle-income countries that are in support of their development-related export transactions and investments.<sup>45</sup>

While the credit risk needs to be acceptable, there are a number of other conditions relating to the environmental and social impact of the transactions and the overall development impact. Additionally, the DGGF provides technical assistance through advisors assisting with the application or helping the client to ameliorate the development-related or corporate social responsibility aspects of the transaction.

<sup>42</sup> First-ever EIB facility for buyer credit financing for European SME and Midcap exporters. Press release from 23 October 2015.

<sup>43</sup> More information can be found in the EC’s Overview of EU Instruments contributing to the Internationalisation of European Businesses from 3 March 2016 & in Grosse-Puppendahl et al., 2016a/b.

<sup>44</sup> <https://atradiusdutchstatebusiness.nl/en/products/dutch-good-growth-fund.html>

<sup>45</sup> DGGF budget: €100 million in 2014, €150 million in 2015, €150 million in 2016 and €300 million in 2017. <https://www.government.nl/topics/development-cooperation/contents/doing-business-in-developing-countries>

### 1) Local businesses in DGGF countries

Local SMEs as well as local investment funds in designated countries<sup>46</sup> can benefit from financing facilities that aim to develop the SME sector. They can benefit through private investors and financial intermediaries and this part of the DGGF is managed by the Triple Jump and PwC consortium.

#### Dutch businesses

Dutch business that want to benefit from DGGF funding when doing business with eligible countries need to make sure that their export transactions or investments concerned must be development related. Different facilities are available to either do investments or exports, however, for both types of support a number of criteria need to be fulfilled.

**2) The DGGF supports private investments by Dutch SMEs through providing guarantees or co-financing** (loans and equity investments subject to be repaid) of up to a maximum of €10 million while requiring an own contribution of minimum ca. 20%. Those are managed by the Netherlands Enterprise Agency (RVO). Financial support for investments can take three different forms:<sup>47</sup>

1. **Guarantees to EU and local banks**, which can reduce possible losses on a loan or risk capital;
2. **Co-financing with private financiers** by providing an additional loan at market interest rates up to a maximum of 49% (or € 10 million per finance);
3. **Loans to private equity funds** that help the fund to finance its investments with a maximum of 50% and which can stimulate the fund to further invest in local SMEs in investments in DGGF countries conducive to their development.

The eligibility criteria to access support are i) being a Dutch SME (European definition) with substantial economic activities in the Netherlands; ii) adhering to corporate social responsibility (CSR)<sup>48</sup>; iii) having a well-developed business plan with sufficient funding available for future reimbursement; and iv) representing a profitable investment.

### 3) Exports

**Atradius Dutch State Business (DSB), the Dutch ECA, is responsible for those DGGF facilities, which are available specifically for export transactions.** In that regard, Atradius evaluates the impact of the transactions for their social consequences and the environment, such as pollution or occupational health and safety conditions of the buyer. This aims at not only increasing production but also to create jobs and allow for the transfer of knowledge, skills and technology to buyers and their countries.

Atradius provides insurance for transactions worth up to €15 million, while also covering guarantees (such as advance payment bonds or performance bonds) against the risk of the guarantees being called. It further provides up to €2 million in suppliers' credit to customers in one the DGGF-countries. Insurance covers the financial and political risks of Dutch exporters, primarily meant for Dutch SMEs, but also larger companies can be eligible if they are able "to demonstrate that their export will have a positive impact on Dutch SMEs". Both credit insurance and export financing apply to "supply transactions between buyers and principals in the DGGF countries, and Dutch suppliers of capital goods and infrastructure projects (...), where the regular credit insurance of Atradius offers no options".<sup>49</sup>

#### Providing trade finance in the context of development cooperation

With Atradius providing trade support for Dutch businesses to export to DGGF countries, a number of questions arise related to under what criteria and conditions should development cooperation promote own

<sup>46</sup> <http://english.dggf.nl/country-list>

<sup>47</sup> <http://english.dggf.nl/file/download/33030672>

<sup>48</sup> RVO.nl's policy is based on the principles established by the OECD Guidelines and the IFC Performance Standards.

<sup>49</sup> <http://english.dggf.nl/file/download/33030662>

companies' commercial aspirations (issue of tied aid) and how to ensure that such exports have positive development effects (issue of additionality)?

**A group of NGOs (Both Ends et al., 2013) therefore makes four recommendations** related to i) development relevance, ii) the relation of export financing and debt burden, iii) CSR standards, and iv) transparency, involved stakeholders and grievance mechanisms. They argue that “export financing is the most controversial element of the DGGF because the link to development relevance and demand-drivenness is not easy to make”. These are legitimate questions about the role of ECAs using development funds, which primarily aim at supporting domestic companies, and how sustainability criteria and better monitoring could enhance the positive impacts for development. Addressing such issues should be a priority for all stakeholders.

### **About ECDPM**

ECDPM was established in 1986 as an independent foundation to improve European cooperation with the group of African, Caribbean and Pacific countries (ACP). Its main goal today is to broker effective partnerships between the European Union and the developing world, especially Africa. ECDPM promotes inclusive forms of development and cooperates with public and private sector organisations to better manage international relations. It also supports the reform of policies and institutions in both Europe and the developing world. One of ECDPM's key strengths is its extensive network of relations in developing countries, including emerging economies. Among its partners are multilateral institutions, international centres of excellence and a broad range of state and non-state organisations.

### **Thematic priorities**

ECDPM organises its work around four themes:

- Reconciling values and interests in the external action of the EU and other international players
- Promoting economic governance and trade for inclusive and sustainable growth
- Supporting societal dynamics of change related to democracy and governance in developing countries, particularly Africa
- Addressing food security as a global public good through information and support to regional integration, markets and agriculture

### **Approach**

ECDPM is a “think and do tank”. It links policies and practice using a mix of roles and methods. ECDPM organises and facilitates policy dialogues, provides tailor-made analysis and advice, participates in South-North networks and does policy-oriented research with partners from the South.

ECDPM also assists with the implementation of policies and has a strong track record in evaluating policy impact. ECDPM's activities are largely designed to support institutions in the developing world to define their own agendas. ECDPM brings a frank and independent perspective to its activities, entering partnerships with an open mind and a clear focus on results.

For more information please visit [www.ecdpm.org](http://www.ecdpm.org)

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ECDPM Discussion Papers present initial findings of work-in-progress at the Centre to facilitate meaningful and substantive exchange on key policy questions. The aim is to stimulate broader reflection and informed debate on EU external action, with a focus on relations with countries in the South.

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