

GENERAL AGREEMENT ON
TARIFFS AND TRADE

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EXPORT INFLATION INSURANCE SCHEMES

Information Submitted by Contracting Parties

Addendum

1. Information submitted by five contracting parties on export inflation insurance schemes, in response to GATT/AIR/1330, was circulated in document L/4467 dated 20 January 1977.
2. The following information has been received from:
 - Burundi
 - European Communities
 - Finland
 - France
 - Italy
 - United Kingdom
 - United States
3. Contracting parties who have not yet submitted information in response to GATT/AIR/1330 are invited to do so without delay. Further notifications will be produced as additional addenda to this document.

BURUNDI

A. EXPORT INFLATION INSURANCE SCHEMES IN BURUNDI

The major part of exports from Burundi still consists of coffee exported by the Burundi Coffee Company (BCC).

The remaining exports are by the Office du Thé du Burundi (OTB) for tea, by COGERCO for cotton, and by certain private enterprises for fruit and vegetables, skins and other products.

None of these Burundi exporters are insured against inflation.

B. MEASURES, DIRECT OR INDIRECT, WHICH ARE USED TO ATTENUATE OR COMPENSATE FOR THE EFFECTS OF COST INFLATION

Let us first analyze where cost inflation affects the Burundi exporter.

Clearly there is no inflation of the cost of labour. Wages are practically never indexed, and but for exceptional cases the Burundi worker receives, year in year out, the same nominal wage.

Similarly, the peasant producing coffee beans, cotton fibre or tea leaves cannot be a source of inflation because the prices of these products are imposed upon him in the light of the good-management requirements of the enterprises buying or exporting those products without any regard whatever for the proportion of the raw product's value in the value of the finished product and without regard to the deterioration of the purchasing power of the peasant producer.

Cost inflation therefore intervenes at the level of imported capital goods (imported inflation) and at the level of transport costs outside of Burundi.

In our opinion the institutional measures relating to the compensation of labour on the one hand and the fixing of the purchasing price paid to the peasants on the other help to attenuate and even partially compensate for cost inflation.

C. TRADE EFFECTS, REAL OR POTENTIAL OF THE MEASURES OUTLINED ABOVE

The measures outlined above of course help to increase the competitiveness of our export products.

This is being seriously affected, however, by imported inflation (i.e. inflation of the cost of capital goods) and by the inflation of transport costs, which is still a growing handicap for Burundi as regards exports.

EUROPEAN COMMUNITIES

Under the terms of reference of the Working Party on Export Inflation Insurance Schemes and in conjunction with "any other measures, direct or indirect, which are used to attenuate or compensate for the effects of cost inflation" (item (b) of document GATT/AIR/1330), the European Communities wish, at this stage, to draw the Working Party's attention to a scheme in Japan involving a fiscal arrangement in favour of large industrial co-operation projects.

This scheme (Article 55 of Japan's Finance Law for the year 1976/77) would enable Japanese undertakings, when concluding industrial contracts for exports in the framework of co-operation agreements, to advance funds from liquid assets up to a certain amount of the obligated expenditure. These earmarked funds are deductible, under certain conditions, from taxable profits for the year in which they are constituted, and the deduction may be made during a certain period of time. This privilege, it would seem, can be used indirectly to stabilize the contract's prices during the period of manufacture.

At this stage in the Working Party's work, the Communities are continuing their study of measures that may fall under the definition given in paragraph (b) of the above-mentioned airgram and, inter alia, in the light of the discussion, reserve the possibility of drawing attention later to other examples of measures having effects similar or comparable to inflation insurance schemes.

FINLAND

1. According to the Finnish Insurance Scheme against Cost Escalation (so called K-guarantees), in force since 1964, a partial cover against exceptionally high rates of inflation during the manufacturing period can be granted in the form of a special guarantee to the Finnish exporters of heavy metal industry products and, in certain exceptional cases, of heavy construction industries. The Act on Export Guarantees of 1962 authorized VTL (Export Guarantee Board), a government agency, to issue these guarantees.

Numerous amendments, especially concerning the exporters' own risk, have been made to this scheme (the latest one in December 1976).

2. Clearly identifiable heavy metal products of Finnish origin are eligible for cover, provided that the delivery time is at least eighteen months. The maximum period of cover is sixty months, running from the signature of the contract to the delivery of the product.

3. At present only the part of the domestic inflation, which exceeds 8 per cent annually, will be partially (50-85 per cent of the guaranteed price) covered by the guarantee. The guarantee covers solely domestic components. The premium to be paid by the exporter in advance is 0.04 per cent per month (0.02 per cent up to November 1975) and calculated from the guaranteed price.

FRANCE1.1 DEFINITION

The purpose of the guarantee against economic risks, a scheme introduced in 1960 following the "guarantee of prices" introduced in 1948, and administered by COFACE (Compagnie française d'assurance pour le commerce extérieur) acting for the account of the State, is to guarantee, under certain conditions, French exporters of capital goods against increases actually suffered in production costs related to fixed-price contracts.

1.2 ELIGIBILITY

The scheme is applicable to contracts for the sale of manufactured capital goods or related performances amounting to more than FF 1 million whose lead time is not shorter than twelve months.

1.3 FRANCHISE

The franchise is the fraction of the increase which each year is to be borne by the insured. It is currently 6.5 per cent per year.

1.4 COVER AND DETERMINATION OF COST INCREASES

The guarantee does not cover the elements which are not affected by inflation of French origin, namely:

- elements accounted for by local factors
- foreign elements
- profit margins and fixed charges of the French portion (representing 15-25 per cent of the French portion).

The guarantee thus applies only to the variable costs of the French portion, the increases being determined by a revision formula which used official indices (wages, semi-finished goods).

1.5 PREMIUM

The cost of the guarantee is 1 per cent per year of the insured amount.

1.6 BUDGETARY COST

For the last three years the budgetary appropriations have been:

- FF 645 million in 1974
- FF 907 million in 1975
- FF 1,407 million in 1976

Two periods of strong inflationary pressures produced a deficit in the scheme: 1968 and 1974.

ITALY

1. PRELIMINARY OBSERVATIONS

The present insurance scheme covering production-cost risks in Italy was established by Law No. 131 of 28 February 1967, which is the only existing legislative basis for the entire field of export insurance and export credit financing. Unlike the other risks, however, the risk of cost inflation was not immediately covered. Two elements prevented practical introduction of such cover prior to January 1973: (a) the financial difficulties which for years confronted the Italian economy and which naturally had a serious impact on activities in the field of export insurance and export credit financing; (b) the need for detailed elaboration of the procedures and the operational limits of this insurance for covering the risk of cost inflation.

Moreover, it should be noted that, because of the serious deterioration of Italy's financial situation largely due to the repercussions of the energy crisis, the Italian authorities decided, in June 1974, to suspend the cover of this risk, which had become too heavy a burden for State insurance management.

That is why, after the adoption of the principle of such insurance at the legislative level, insurance covering the risk of cost inflation remained in force in Italy for a period of eighteen months as from January 1973, during which 321 applications for insurance were examined and 105 representing an insured amount totalling approximately Lit 47,000 million were accepted.

2. OUTLINE OF THE SCHEME

The risk in question is defined as "the risk of increased production costs" resulting from general circumstances arising during the process of manufacture, provided that the contract entered into with a foreign buyer contains a "fixed price" clause.

The insurance covers variations in the costs of raw materials, energy, labour and other cost elements that might enter into the order in question.

Variations in costs which, as a whole, do not exceed 5 per cent of the price fixed by the contract are borne by the insured; variations greater than that percentage - that is, only the amounts in excess thereof - are covered by the guarantee of insurance to the extent of 10 per cent, and not more than 15 per cent. Any further excess is excluded from the guarantee.

In the first phase of application of the cover in question, which, as has been stated, lasted eighteen months, the only orders considered were those amounting to more than Lit 300 million or those requiring a guarantee of more than six months.

During the period referred to, the level of the premium was determined in accordance with the percentages of the total cost accounted for by the various cost elements and on the basis of the length of the lead time. In general, however, the premium never exceeded 1.25 per cent per year.

UNITED KINGDOM

1. The United Kingdom cost escalation scheme for exports was introduced in 1975 as a temporary insurance facility to give United Kingdom contractors and exporters of major capital goods and overseas projects a limited measure of protection against exceptional and unpredictable cost increases which they might incur as a result of the United Kingdom inflation rate being considerably higher than that in other major exporting countries. This scheme is due to expire in March 1977 unless renewed by Affirmative Resolution of the House of Commons. The United Kingdom Government - as announced by the Chancellor of the Exchequer on 15 December 1976 - have now decided to lay an Order before Parliament seeking extension of the Scheme for a further twelve months.
2. Details of the Scheme are included in the OECD report on cost inflation insurance schemes (TC(76)15 of 16 June 1976).¹
3. Access to the Scheme, which provides very restricted cover, will continue to be strictly controlled; and latest estimates suggest that under 1 per cent of the United Kingdom exports will be covered by it. Experience in its operation shows that under the present detailed operating rules normally no more than half of the contract price is covered. Since cost increases must run at least 7 per cent per annum (plus 1 per cent per annum premium) before benefit begins, the Scheme only provides in effect insurance against annual rates of "inflation" in excess of 12-15 per cent. It does not provide open-ended cover. But its introduction has helped United Kingdom exporters to compete during a period when our rate of inflation has exceeded that of our competitors.
4. To date only two guarantees, covering contracts worth £60 million in all, have been given.
5. In addition there is a separate scheme for both domestic and export sales of ships. To date eight guarantees have been given covering contracts worth about £42 million.
6. No claims have yet been paid under either scheme. It is too early to estimate precisely how much may eventually be paid by way of claims. This will clearly depend largely on the Government's success in bringing United Kingdom inflation down to an acceptable level. Still less is it possible to say yet whether claims paid will cumulatively exceed premium income.
7. These extremely limited schemes provide insurance cover and do not distort international competition: we have yet to see any evidence which suggests the contrary.

¹Reproduced in the Appendix to document L/4464.

UNITED STATES

The United States does not have in effect any programme, such as export inflation insurance, designed to or having the effect of ameliorating, limiting, or compensating for the effects of inflation on the input costs of any exported product.

