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Ms Patricia Scott
Presiding Commissioner
Export Credit Arrangements
Productivity Commission
LB2 Collins Street East
Melbourne VIC 8003

Dear Ms Scott

National Australia Bank Limited ("NAB") welcomes the opportunity to provide comment on the Productivity Commission's ("Commission") draft report *Australia's Export Credit Arrangements.* NAB was interviewed by members of the Commission to provide input for this draft report in October 2011.

NAB has a history of over 150 years supporting businesses and is a key player in the Australian project finance market. Our Global Specialised Finance team provides project finance funding to projects across a broad range of sectors, including finance solutions specifically for major capital assets. We take seriously the role we play in supporting Australia's economy and nation building through project financing and providing sophisticated funding solutions for businesses.

We are also Australia's leading business bank, and our support for Small and Medium Enterprises ("SMEs") is well proven. We recognise the importance of supporting this vital sector, and as such are supportive of the draft report's recommendation for Australia's Export Finance and Insurance Corporation ("EFIC") to address the impediments faced by exporting SMEs to export finance, in a way which complements EFICs current role. Australia's infrastructure requirements, relating to roads, rails, ports, airports and power, are well understood, and EFIC's ability to continue to fill the financing gap left by the withdrawal of offshore banks is critical.

NAB has worked with EFIC over a number of years and has also worked with other leading international Export Credit Agencies ("ECAs") on specific transactions. As such, NAB is well placed to provide an informed perspective on some of the issues raised in the draft report.

We refer to the Scope of Inquiry for the Commission to "Review the presence or otherwise of market gaps for EFIC's products and services" [1] and to the Report's Key Finding that it "has found no convincing evidence to indicate there are failures in financial markets that impede access to finance for large firms, or for domestic resource

[1] Productivity Commission Draft Report, *Australia's Export Credit Markets*, http://www.pc.gov.au/__data/assets/pdf_file/0005/1385/export-credit-draft.pdf, 2012 p. IV (Accessed March 2012)

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projects. EFIC should not continue to provide finance to large corporate clients or for domestic resource projects on the commercial account".[2] The International Monetary Fund's latest *Global Financial Stability Report*[3] dated January 2012 does not provide support for this assessment.

That report comments on the impairment of credit channels which could be caused by European banks' pull back from cross-border and local lending, particularly in Asia where European banks have provided roughly 30% of trade and project finance.[4] The report further notes that "Constraints on long term funding could severely limit banks' capacity in such areas as shipping and aviation trade finance, as well as project and infrastructure finance".[5]

We observe that the trends noted in the IMF's recent report are indeed taking place in Australia; European banks' contribution to the Australian syndicated loan market has fallen steadily from over 30% in 2007 (of a total $110 billion) [6] to 15% in 2011 (of a total $108 billion) [7]as a number of European banks have reduced or withdrawn their Australian presence. NAB and other Australian banks have stepped up to largely fill this gap, increasing their share of the Australian syndicated loan market from 52% to 64%.[8] This has occurred during a time when funding for the banking sector has become increasingly challenging, in particular for the longer tenors which are necessary to fund long term infrastructure and natural resources projects.

At the same time, companies are undertaking unprecedented levels of investment in Australian minerals and energy projects; the Australian Government's Bureau of Resources and Energy Economics has confirmed in its October 2011 report a record $231.8 billion of planned capital expenditure on 102 advanced stage projects [9]. Of significance, in addition to the record absolute amount, the average $2.27 billion capital cost per project is significantly higher than the average $369 million capital cost of projects recorded between 2003 and 2011.[10] We expect most of these projects will be financed by large corporations, although a number may require separate project debt financings in amounts that are significantly higher than debt financings seen over the past decade.

Prudential lending guidelines of course dictate a finite limit to an individual bank's exposure to single projects and to borrowers generally. As project capital costs have

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[2] Ibid, p. XIV
[3] International Monetary Fund, Global Financial Stability Report, http://www.imf.org/External/Pubs/FT/fmu/eng/2012/01/index.htm, 2012 (Accessed March 2012)
[4] Ibid
[5] Ibid
6 Reuters Loan Pricing Corporation 2007
[7] Ibid, 2011
[8] Reuters Loan Pricing Corporation
[9] Bureau of Resources and Energy Economics, *Mining Industry Major Projects*, *http://bree.gov.au/documents/publications/resources/BREE_MEMP_NOV2011.pdf*, 2011, p.1 (Accessed March 2012)
[10] Ibid

increased, particularly in the infrastructure and natural resources sectors, maximum individual bank exposure amounts are being tested and additional sources of capital have been required. A recent example is the September 2011 $3 billion senior debt financing for construction of the Wiggins Island Coal Export Terminal ("WICET"), referred to in the draft report. Although the draft report correctly stated that EFIC provided $100 million (as a financial guarantee) and was just one of 19 financing parties, [11] we would have liked to see the draft report making the important point that five sovereign-owned financial institutions, including EFIC, (the others being German, Canadian, Chinese, and Korean) provided a total of $780 million i.e. 26% of the financing, almost equivalent to the $794 million total provided by NAB and other Australian lenders.[12]

From this perspective, we do not share the Commission's view that "It is not apparent what impediment to access to private finance or shareholder equity, caused by failures in financial markets, would have stopped the project proceeding". [13] In our opinion, without EFIC and other sovereign-related financing it seems unlikely that private finance alone could have fully funded WICET. More generally, we observe that in the current Australian debt finance market, single project debt requirements in excess of $2 billion to $3 billion will require debt or debt support from sovereign ECA's to cover a financing "market gap".

In our experience in co-financing projects with ECAs, including EFIC, we have not found that the ECAs "crowd out" the private market through below market pricing. Rather, we have found that EFIC in particular has been quite careful to become involved in financings only where a "market gap" is apparent and to be a "price taker" in that they accept pricing already determined by the private lending syndicate.

More importantly, however, we have found that EFIC's qualitative contribution to projects which require ECA financial involvement is substantial. For projects in Australia, EFIC serves as a catalyst for participation of other ECAs which are not as familiar with the country. In addition, EFIC's personnel have great private sector project financing experience and a deep background and understanding of mining and energy finance. In this role, EFIC helps to ensure that lending structures appropriate to the Australian market are applied by foreign ECAs which are now playing a greater role in financing Australian natural resources and infrastructure projects. EFIC involvement also provides a greater level of local and industry knowledge which may assist other ECAs in reaching reasonable, well-informed decisions in responding to future potential borrower requests to restructure financing.

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[11] Productivity Commission Draft Report, Australia's Export Credit Arrangements, http://www.pc.gov.au/__data/assets/pdf_file/0005/115385/export-credit-draft.pdf ,2012, p.148 (Accessed March 2012)
[12] Project Finance International, 5 October 2011, p. 26
[13] Productivity Commission Draft Report, Australia's Export Credit Arrangements, http://www.pc.gov.au/__data/assets/pdf_file/0005/115385/export-credit-draft.pdf , 2012 p.148 (Accessed March 2012)

These benefits also apply to projects outside Australia, where EFIC's potential complementary role as a direct lender is perceived as a helpful catalyst for private sector finance and its "AAA" rated political risk cover is a valuable addition to private sector insurance.

When interviewed by the Commission team, we expressed our view that consideration should be given to expand EFIC's commercial account role to allow it to provide larger amounts to support the financial requirements of increasing project size, particularly in the natural resources and infrastructure sectors. It is useful to consider the actions of other countries that are either establishing or expanding their own ECAs to play a similar role to EFIC. Over the last three years, other ECAs or sovereign lenders from Canada, the United States, Germany, Finland, Japan, and Korea have implemented new flexibility or expansion of their loan or guarantee programs to respond to their concern of a market financing gap for strategically important projects. Last month the Government of Singapore approved the establishment of a "Project Finance Company" to be operational in the second half of 2012, particularly to fund large ticket and long tenor project financings which involve Singaporean companies.[14]

With regards to the short-term trade finance market, we are supportive of the draft report's recommendation that EFIC continues to offer their current suite of "Guarantees" products (as defined in table 3.2 of the draft report),[15] as well as the provision of reinsurance cover for sovereign and country risk. We would also urge the Commission to include "Bonds" (as defined in table 3.2 of the draft report)[16] in EFIC's continued product offering, especially Advance Payment, Performance and Warranty bonds as there are clear connections and synergies between these particular Bonds and the continuing form of Guarantees which are related to export trade transactions.

In our experience, pricing charged by EFIC for short-term trade guarantees is priced on a commercial basis.

We would also comment on two further aspects of the draft report with specific regards to the short-term trade finance market, the SME definition and the cap on the number of transactions per client introduction. If definitions of SME or caps are to be introduced, it is important that consideration be given to ensuring that they are appropriate, clearly defined and commercial.

The turnover figure proposed for SMEs needs to be further examined as there can be different interpretations of SME. Regarding draft recommendation 10.5 and the proposed cap,[17] to three transactions per client will make it critical that the meaning of

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[14] The Straits Times, *New project finance company to fund firms going abroad*, 18 February 2012
[15] Productivity Commission Draft Report, Australia's Export Credit Arrangements, http://www.pc.gov.au/__data/assets/pdf_file/0005/115385/export-credit-draft.pdf ,2012, p.34 (Accessed March 2012)
[16] Ibid
[17] Ibid, p.XLIV

"transaction" is precisely defined. For example, a "transaction" might be considered as a single, one-off deal or conversely a 12-month revolving facility may also be deemed a "transaction", both of which have markedly different attributes.

In conclusion, we recommend the Government and the Commission revisit the draft report's recommendations on EFIC's commercial account role and activities and either support or expand EFIC's current activities. This will complement not crowd out private sector financing for worthy large scale projects which support employment and business for Australians and Australian companies.

In addition, we are supportive of the draft report's recommendation to address the impediments faced by exporting SMEs requiring export finance, in a manner which complements EFICs current role.

NAB looks forward to continuing the dialogue with Government and the Commission about Australia's export credit arrangements. Please do not hesitate to contact me at any stage to discuss further.

Yours sincerely

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cc: EFIC

Bibliography

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