A RACE TO THE BOTTOM: CREATING RISK, GENERATING DEBT AND GUARANTEEING ENVIRONMENTAL DESTRUCTION

A Compilation of Export Credit & Investment Insurance Agency Case Studies

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INTRODUCTION

Publicly owned bilateral export credit agencies and investment insurance agencies (ECAs) are an increasingly important class of international finance institutions that support a growing number of privately owned project ventures abroad. Many of these projects present major threats to the environment and people of the affected regions. *A Race to the Bottom: Creating Risk, Generating Debt and Guaranteeing Environmental Destruction* provides a series of case studies exploring a sample of the environmental and social problems caused by these publicly owned institutions.

Bilateral finance agencies provide publicly-backed loans, guarantees and insurance to corporations from their country seeking to do business overseas in developing countries and emerging markets. Most OECD nations have at least one ECA, and investment insurance agency, which are usually an official or quasi-official branch of their government. Because of the inherent risks of controversial projects in the mining, forestry, oil and gas, coal, power and other sectors, many, if not most of these projects in the developing world could not go forward but for the support of some bilateral or multilateral finance institution.

In May 1996, the governments which form OECD's Development Assistance Committee issued a report on *Shaping the 21st Century: The Contribution of Development Co-operation.* In this report they made the following commitment:

"The ramifications and opportunities of policy coherence for development now need to be much more carefully traced and followed through than in the past. We should aim for nothing less than to assure that the entire range of relevant industrialized country policies are consistent with and do not undermine development objectives. (…) We will work to assure that development cooperation and other linkages between industrialized and developing countries are mutually reinforcing."

Despite that strong statement, there are disturbing contradictions within OECD countries regarding the environmental policies of ECAs and those of development assistance agencies and multilateral development banks supported by OECD countries. While OECD country-supported bilateral aid agencies and multilateral development banks, such as the World Bank, have adopted detailed social and environmental procedures, most ECAs and public insurance agencies have few and, at times, no environmental or social standards. The same OECD countries that have approved environmental and social policies for their aid agencies and the World Bank are now subverting them with inadequate ECA policies. Due to a lack of common international standards for ECAs, the OECD governments are prepared to finance individually what they cannot fund collectively.

Bilateral ECAs are also intensely competitive with one another, and they are quick to back projects other multilateral development banks and ECAs have refused on environmental and social grounds, leading to a "race to the bottom" that encourages the absence or lowering of standards. This "race to the bottom" also increases financial and political risks associated with projects, the very risks ECAs supposed to protect against.

Bilateral ECAs are also responsible for an increasing amount of debt, leading to the financial dependency that limits the progress of many less developed countries. According to a recent study by the Environmental Defense Fund, "(a)nnual new commitments of officially supported export credits have increased over four-fold during the past decade, from about $26 billion in 1988 to $105 billion in 1996. In 1996 they accounted for 24 percent of the total indebtedness of all developing countries, and for 56 percent of their official debt." A large portion of ECA

debt is a major concern because a lack of environmental and standards means that many of these projects are not sustainable investments.

In recent years, environmental NGOs and governments have begun to call on all ECAs to adopt and upwardly harmonize their environmental and social policies. In 1997, the G-8 Summit final Communiqué included a section on “Environmental Standards for Export Credit Agencies” encouraging ECAs to adopt “sustainable practices by taking environmental factors into account when providing financing support for investment in infrastructure and equipment.” The 1998 Communiqué of the G-8 Finance Ministers also contained language supporting this goal. So far, however, there has been little real progress on the part of ECAs to improve their performance. Accordingly, NGOs have launched an international grassroots campaign to research and expose environmentally and socially harmful ECA-backed projects and promote international common environmental standards for all bilateral ECAs.

In the coming months, these case studies will be updated and more will be presented as environmental and social organizations around the world continue to closely monitor ECAs.

PART ONE: PROJECT CASE STUDIES

I Case Study: PROPOSED ILISU DAM—TIGRIS, TURKEY

A series of OECD ECAs are considering extending, or have already extended, about $850 million in export credits and guarantees for Ilisu, the largest hydroelectric dam currently planned in Turkey. The project violates five policy guidelines of the World Bank on 18 accounts, and core provisions of the UN Convention on the Non-Navigational Uses of Transboundary Watercourses, which Turkey has opposed.

Damming the Tigris near the Iraqi and Syrian borders, the project will enable Turkey to block flows of the Tigris to Iraq for several months, further exacerbating the current turmoil characterizing the region. Ilisu will flood 52 villages, 15 small towns, and evict the 5500 inhabitants of Hasankeyf, drowning the best preserved medieval town in Anatolia, a legally protected archaeological and cultural site. It will forcibly displace an estimated 15,000 mainly Kurdish refugees (most likely a significant underestimation because numbers are based on helicopter overflights of project consultants). Compensation for Ilisu will only be decided after construction begins, a violation of accepted OECD Development Assistance Committee (DAC) resettlement guidelines. Affected people are not being consulted, and given the state of undeclared war in the Kurdish areas, are not able to voice protest or defend their interests. The Ilisu reservoir will vastly reduce the autopurification capacity of the Tigris: solid waste and wastewater of major cities like Diyarbakir, Siirt and Batman are still being dumped into the Tigris River without treatment. It will also infest the area with Malaria and Leishmaniosis. Rife with social, political, and environmental problems, Ilisu underscores the urgent need for common, harmonized, minimal environmental and social standards for ECAs.

ECA Support

Loan syndication coordinated by Union Bank of Switzerland. External financing depends on coverage by official export credits or guarantees. In summer 1998, the Ilisu contractors submitted applications for coverage to the export credit agencies (ECAs) of Austria, Germany, Italy, Japan, Portugal, Sweden, Switzerland, the UK, and the U.S. The Swiss Export Risk Guarantee has decided to support the project and the U.S. Export-Import Bank has issued a preliminary commitment, which does not necessarily entail final approval. Export Risk Guarantee is presently coordinating a common position among interested ECAs for extending official export credits or guarantees of about $850 million.

Project Description

Located on the Tigris 65 kilometers from the Iraqi border, Ilisu is supposed to have a capacity of 1200 megawatts and will flood an area of 313 square kilometers. Ilisu is part of the South-East Anatolia Project (GAP), a giant hydropower and irrigation scheme in the Kurdish inhabited area of Turkey that to date has forcibly resettled over 100,000 people. Project costs are estimated at $1.52 billion, part of total GAP costs of $32 billion. Construction is planned to start in mid-1999, production of power in mid-2006. The electromechanical contract has been awarded to a consortium led by the Swiss (Swedish) companies Sulzer and ABB. Civil works have been awarded to a consortium led by Balfour Beatty (UK), and including among others, Impregilo (Italy), Skanska (Sweden), Nurol, Kiska, and Tekfen (all Turkey). Sulzer and ABB have commissioned an EIA, but arguing that it has only been done for ECAs, they have withheld it from NGOs and representatives of affected people.

The Convention on the Non-Navigational use of Transboundary Waterways, adopted by the UN General Assembly in 1997 by 103 nations, attempts to prevent international water conflicts caused by unilateral diversion of water resources without negotiation with downstream

countries. Turkey, along with China and Burundi, was one of only three countries which rejected this convention. In late August 1998, the Iraqi government threatened to bring the water issue to an international tribunal, and Syria has supported PKK Kurdish guerillas in the project region, partially in retaliation for Turkish monopolization of transboundary water resources.

The Ilisu reservoir will flood Hasankeyf, a Kurdish town with a rich treasure of Assyrian, Christian, Abassidian-Islamic and Osmanian history. Hasankeyf was awarded complete archeological protection by the Turkish department of culture on April 14, 1978 (decision A-1105). Numerous cultural experts and activists in Turkey have appealed to the national authorities and the foreign companies to save Hasankeyf by changing the design of Ilisu.

The proposed Ilisu project violates numerous important World Bank policy guidelines including the lack of public disclosure of its environmental impact assessment; the failure to consider alternatives (i.e., alternative investments, sites, technologies and designs); project sponsors' failure to consult with affected communities, NGOs and internationally recognized environmental specialists in the development of environmental assessments; failure to conduct cost benefit analyses measuring environmental impacts; failure to consider demand-side management (including energy efficiency projects); failure to provide advance compensation or other assistance for those involuntarily resettled; failure to provide any socio-economic surveys, land compensation or other vital infrastructure and services to assist those involuntarily resettled; failure to resolve potential resulting water disputes with Iraq and Syria; and failure to mitigate against damage to non-replaceable cultural property. The World Bank has refused to support GAP projects, including Ilisu.

At a cost of $ 1,300/kilowatt (plus financing costs), Ilisu is a relatively expensive power project. Project opponents in Turkey believe that power could be saved at a lower cost by modernizing the country's transmission system, which has a reputation of being inefficient. The Swiss Export Risk Guarantee (ERG) is presently coordinating an attempt among interested ECAs to reach a few minimum standards for the project on issues such as resettlement and diversion of waters from downstream users. Because the project is so environmentally and socially unsound on so many counts, any agreement for the project to go forward at all will represent an acceptance of standards much lower than those of the World Bank and the OECD DAC. Hence Ilisu stands for a new variant of the ECAs' race to the bottom, in true lemming style: All together downward at once.

Recommended Action

All ECAs should decline financial assistance to the Ilisu dam project unless, at a minimum, it meets World Bank and OECD DAC standards in all respects.

II CASE STUDY: MAHESHWAR DAM, INDIA

The German government is considering granting export credit insurance and investment guarantees for the Maheshwar dam on the Narmada River in the Indian State of Madhya Pradesh. Maheshwar will submerge lands of 61 villages, and forcibly displace over 20,000 people. In conjunction with other dam projects on the Narmada, Maheshwar poses serious risks, including water pollution, health hazards, loss of fish, increased flooding and earthquakes. Madhya Pradesh state legislation explicitly calls for "land for land" compensation, but already with six completed dams in the greater Narmada scheme, over 100,000 people have been dispossessed, and not a single person has been rehabilitated with land for land. On January 11,1998, over 15,000 angry protesters occupied the Maheshwar Dam site, more than 3000 staying blocking all construction for 21 days, some going on death fasts. The subsequent Madhya Pradesh state review acknowledged the unavailability of land for resettlement. Maheshwar promises to replicate the social, political and environmental disasters of the downstream Sardar Sarovar dam, which is now being backed by an export loan from the Sumitomo Bank of Japan. This case study clearly demonstrates that ECA-support without transparent, common international environmental and social standards results in severe social and environmental upheaval.

ECA Support

In 1997, the German Government made an in-principle decision to provide export credit insurance through the Hermes Kreditversicherungs AG. The guarantee would insure 85% of a $257 million loan of the Bayerische Vereinsbank; the loan would go principally for purchase of equipment (turbines, generators) from Siemens. In addition an investment guarantee application has been put forward to C & L Deutsche Revision by two German power utilities, Bayernwerk and VEW, who will together hold 49% of equity in the project. The German Government has put both decisions on hold since June 1998 to more fully investigate the social impacts of the project.

Project Description

The newly privatized 400 Megawatt (MW) Maheshwar dam is being built as part of the controversial Narmada Valley Development Project (NVDP), which consists of 30 large and 135 medium-sized dams. The low lands threatened by submergence are one of the most fertile tracts in India, with abundant crops of cotton and chilies, wheat pulses and sugarcane, rich with irrigation from the river or wells. Maheshwar will also eliminate employment for thousands of people working in sand and stone quarrys along the river. None of these factors have been taken into account in the benefit-cost ratio of the project or in determining the magnitude and nature of displacement.

Environmental clearance for Maheshwar was rejected in 1986 by India's Federal Ministry of Environment and Forests, and received only conditional clearance in 1994. The environmental clearance was granted on the condition of availability of land for rehabilitation, but a recent study by the Tata Institute of Social Sciences shows that the majority of land identified for rehabilitation will be submerged. Madhya Pradesh state legislation explicitly calls for "land for land" compensation for disappropriated land-owners, but with six completed dams, over 100,000 people have been dispossessed and uprooted from lands their ancestors have lived on for centuries, and not a single person has been rehabilitated with land for land.

There have been no studies regarding the impact of the reservoir on health, on downstream effects, on seasonal riverside cultivators, or the cumulative impact of all the proposed dams on the Narmada on floods and seismicity. Through the construction of the dam industrial effluents,

sewage and pesticides runoff will accumulate, causing a serious health hazard. During the last three years, thousands of quintals of fish have perished due to the effluents exuded by the Keida liquor factory in Badwah, upstream of
Maheshwar. Also, the cumulative impact of all the proposed dams will likely be increased heavy floods and seismicity. The devastating earthquake of 1997 at Jabalpur, and of 1998 at Hoshangabad indicate that the Narmada Valley is showing signs of fresh seismic activity.

On January 11, 1998,over 15,000 local villagers occupied the dam-site, more than 3000 sitting in for a 21 day occupation of site, including a death fast by 6 protesters. The Madhya Pradesh Government responded by establishing a Task Force to conduct a project review. The review raised questions of whether efficient and environmentally benign alternatives exist and acknowledged that adequate land area for resettlement has not been identified. Indian NGOs contend that rehabilitation of affected people is impossible and that project planning has overlooked many important economic, environmental and cultural losses.

If internationally accepted environment standards and procedures by the public export credit and investment insurance agencies existed, Maheshwar and the other Narmada Valley projects would clearly not meet such standards. After an independent review in 1992, the World Bank year pulled out of the Sardar Sarovar Project on the Narmada. Over the past four years India's Supreme Court stalled further work on Sardar Sarovar because rehabilitation has not been able to precede submergence. Nonetheless the Sumitomo Bank of Japan has recently announced that it will provide a 26.5 billion Yen export loan for the project. Given the venture is so risky and controversial, Sumitomo Bank of Japan will most probably request export credit insurance through the Japanese government.

Recommended Action

The German government should turn down applications for export credit insurance and investment guarantees for Maheshwar. Due to their immense social impacts, bilateral export credit and investment agencies should not support dam projects in the Narmada Valley.

III CASE STUDY: THREE GORGES DAM, CHINA

Many environmentalists consider the massive Three Gorges Dam as the world's most environmentally and socially destructive infrastructure project. The Three Gorges Dam is touted by the Chinese government as the world's largest hydroelectric project and a symbol of China's development and "superior organizing." The Chinese government remains fixed on hydroelectric gigantism despite its continuing misery from past ill-fated hydro projects. The Three Gorges Dam, which will cost at least US$43 billion (unofficial estimates cite figures upwards of US$72 billion), will be 600 feet high, more than a mile wide and create a reservoir 400 miles long.

ECA Support

Hermes (Germany) loan guarantees of up to $833 million to German engineering giant Siemens AG and turbine manufacturer Voith Hydro. Exportrisikogarantie/ERG (Switzerland) loan guarantees of almost $300 million to Swiss companies ABB and Sulzer Escher-Wyss. EDC provided a US$12.5-million taxpayer-backed loan, enabling Calgary-based Agra Inc. to secure its first contract. Since then, EDC has extended a further $153 million in support of a turbine contract awarded to General Electric Canada.

Project Description

The Export-Import Bank of the United States refused to support the Three Gorges Dam, due to a lack of substantive information provided to the agency on mitigating environmental and social impacts. According to independent reports by the International Rivers Network and Friends of the Earth, budget costs are spiraling out of control and environmental and social issues are not being adequately addressed. According to *Canada Business*, the World Bank officials advised China not to approach them for loans after it became clear "they would become lightning rods for criticism of the project." (*Canada Business*, Feb. 12, 1999). "When the Americans pulled back, Canada very smartly stepped in," says Agra vice-president Peter Mayers. (Id.)

Independent experts note that the project has many significant environmental costs that threaten the financial stability of the project[1]:

- Involuntary dislocation and relocation of up to 1.9 million people.
- Inundation of valuable arable land.
- Three Gorges is not expected to solve the flooding problems of China. Within 50 years, scientists expect the sediment-laden Yangtze will fill much of the dam's reservoir, impairing any power production and impeding navigation with associated environmental costs.
- Heavy silting could compromise the dam's financial operations and increase chances for a catastrophic collapse in a heavy flood.
- The Yangtze River has become the biggest "sewer system" in China. According to the Chinese Academy of Sciences, in the Three Gorges area alone "there are over 3,000 industrial and mining enterprises which release more than one billion tons of wastewater annually, containing more than 50 different pollutants. Presently, there is very little treatment of industrial wastewater flowing into the reservoir area, and no treatment of residential wastewater; everyone relies on the river's capacity to flush pollutants out to sea to keep it clean. But following the construction of the large dam, the river's flow through the reservoir will be significantly and irreversibly reduced and with it any flushing capacity."

International financial institutions that have environmental standards recognize that environmentally destructive projects often have technical and financial risks, and can ultimately and collectively contribute to greater country risks. By integrating environmentally responsible standards into the project loan agreements, ECAs endeavor to lower risks to the project as a

whole. Projects that cannot meet such standards can be rejected by the ECA. However in the Three Gorges example, Exim prudently refused support of the project, while other ECAs such as Hermes and EDC filled that gap of necessary support, thus creating a race to the bottom, where those ECAs with lesser environmental and social standards receive contracts for sensitive projects.

Recommended Actions

A more appropriate approach would be for ECAs internationally to categorically prohibit funding of large dams that disrupt natural ecosystems or the livelihoods of local inhabitants. OPIC has taken a leadership role by adopting this standard. ECAs should start with that common line of prohibition and adopt internationally recognized common environmental standards for acceptable hydroelectric projects.

Sources:
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Christian Science Monitor, August 7, 1998
Export-Import Bank of the United States Transcript, May 30,1996
New York Times, Nov. 15, 1997
"Report on Site Visit to 3 Gorges Dam" by Sklar-Luers & Associates, Oct. 17, 1997
"Sediment Problems at Three Gorges Dam" Luna Leopold, Apr 11, 1996
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IV CASE STUDY: SAN ROQUE HYDROPOWER AND IRRIGATION PROJECT, LUZON, PHILIPPINES

The Japanese Export-Import Bank (JEXIM) plans to provide $702 million in project funding for the San Roque Hydropower and Irrigation Project on Luzon island's Agno River in the Philippines. If built, San Roque would be the tallest dam and largest private hydropower project in Asia. This Build-Own-Transfer (BOT) project will be built and operated by the San Roque Power Corporation, which is owned by Japanese and American corporations. Electricity generated by the 345 MW dam will be sold at fixed rates to the Philippine National Power Corporation (Napocor), and will be primarily used to power industrial activity in northern Luzon. The project is fiercely opposed by thousands of indigenous Ibaloi peoples who stand to lose their homes and land if the dam goes ahead. Over 160 families have already been forcibly displaced and are living in desperate conditions at a temporary site. Napocor has not yet purchased, much less prepared, the fully-equipped resettlement site that it promised. JEXIM's environmental guidelines state that people resettled by projects that it funds must have given their consent. Potential environmental impacts include erosion, siltation, disruption of fisheries, other biodiversity losses, reduced water quality and increased water-borne disease. In October, 1998 a San Roque Power Vice-President publicly admitted that the Environmental Assessment prepared by Napocor failed to address watershed management and did not adequately demarcate the anticipated reservoir level.

ECA Support

JEXIM will provide $702 million toward the total $1-1.5 billion dollar cost of the San Roque Dam. Of this, $302 million has been committed, and an additional $400 million is under consideration.

Project Description

The San Roque Dam is to be located on the lower Agno River of Pangasinan Province, in the Cordillera region of Luzon Island in the Philippines. Project plans call for an earth and rock-filled dam that is 200 meters high and 1,000 meters long, generating 345 MW. Project benefits are said to include irrigation of 87,000 hectares, water quality improvements due to reduced downstream siltation, and 50% reduction of floods, which destroy crops during the rainy season. Preparation of the site began in 1998, and construction is slated for completion in 2004. If built, San Roque would be the tallest dam and largest private hydropower project in Asia.

Finance and Corporate Actors

In October 1998, **JEXIM** approved a $302 million loan to the private sector developers of this project. This funding was approved in apparent contradiction to its guidelines, despite strong local opposition to the project. JEXIM is considering an additional $400 million loan to finance the Philippines' National Power Corporation contribution to the project, but delayed approval of the funds pending endorsement of local governments. Approval of the Itagon provincial government was obtained after the Philippine government offered P50 million (US$1.3 million) in regional development funds. Local groups may challenge the legality of this endorsement, based on the appearance of a payoff and new information regarding an increased number of families to be affected. **San Roque Power Corporation** is owned under a BOT agreement by a Japanese trading company, **Marubeni** (42.45%); a US company, **Sithe Energies** (50.75%), which itself is 29% owned by Marubeni; and a Japanese utility company, **Kansai Electric** (7.5%). The Philippines' **National Power Corporation** (Napocor) has signed a power purchase agreement to purchase electricity from the power station at fixed rates for 25 years, after which it will assume ownership of the dam. Napocor will contribute $400 million toward construction of the dam and spillway. Napocor's financial commitments are being entirely

supported by JEXIM, which will provide political risk cover of its buyout and termination payment obligations after year 10. Sithe received the government contract to build, operate and maintain the dam. In April 1998, US-based **Raytheon Co**. won a $700 million subcontract to design and build the dam. The US subsidiary of Japan's **Toshiba Corporation** won the $51 million supply contract.

Displacement , Resettlement and Opposition

If the dam is built, over 925 families will be displaced, and the livelihoods of tens of thousands of downstream residents will be affected due to erosion and destruction of fisheries. Preparation of the construction site began in early 1998, when 160 families were forced to dismantle their homes and leave the area before a relocation site had been obtained or prepared for them. The Philippine government has not kept its promises to provide affected people with land, housing and social services at a permanent resettlement site. It has also failed to provide the promised compensation for the losses of affected peoples' land, crops and homes. JEXIM's environmental guidelines state that people resettled by projects it funds must give their consent. Given the strident opposition of the populations slated for resettlement, it appears that JEXIM's support for this project violates its own guidelines.

Environmental Impact and Standards

Potential environmental impacts include erosion and siltation; community groups also predict severe disruption of downstream fisheries and other loss of biodiversity, reduced water quality and increased water-borne disease. In October 1998, the San Roque Power Corporation's Vice President, Raymond Cunningham, admitted that the EIA prepared by Napocor was critically flawed. He said it failed to address watershed management issues and adequately demarcate the anticipated reservoir level. Napocor and local officials agreed to alter the EIA, and added 17 conditionalities to the Environmental Compliance Certificate (ECC). This was done without consultation with local people or approval by local government units, as is required by Philippine law. The Ibaloi people continue their strong opposition. JEXIM has been unwilling to provide information to affected peoples or NGOs in Japan regarding the project's social and environmental impact assessments.

Recommended Actions

NGOs have appealed to the Prime Minister of Japan to withdraw JEXIM support, increase transparency and strengthen environmental standards at the agency.

V CASE STUDY: PROPOSED AGINSKOE GOLD MINE KAMCHATKA PENINSULA, RUSSIAN FAR EAST

Potential ECA Investment Insurer support of the destruction of an internationally recognized World Heritage Site. Despite concerns of Russian experts, ECAs with the lowest environmental standards consider supporting a gold mining operation in one of the most pristine areas on earth.

ECA Support

Refused by the Overseas Private Investment Corporation (OPIC), sponsors seek other support including Canada's Export Development Corporation (EDC). EDC's backing of the project and other information related to the current status of the project is not publicly available.

Project Description

Targeting the border zone of the scenic Volcanoes of Kamchatka World Heritage Site in the Russian Far East, the Aginskoe gold mine is a proposed joint venture of Grynberg Resources Inc., Kamgold (both U.S.), and Kinross Gold Co. (Canadian).

The Aginskoe gold mine is proposed to be situated high in the headwaters of mountainous Kamchatka Peninsula's Icha , Bystraya-Khayruzovskaya and Kamchatka rivers. This area is adjacent to the Bystrinsky Nature Park, part of a fragile sub-alpine ecosystem that is recognized by the Russian Government as an "area of the highest biodiversity in the Kamchatka Peninsula."[1] Brown bear, mountain goat, black-capped marmot, lynx, snow ram, elk, sable, otter, as well as the endangered while tailed sea eagle, big horn snow sheep and polar fox reside here amidst numerous hot and mineral springs, and extinct and active volcanoes that tower above aryan fir and larch forests.[2] As a result of international governmental and non-governmental advocacy, in 1996 the Volcanoes of Kamchatka were incorporated into the UNESCO World Heritage system of strictly protected natural areas.

Russian and international conservation authorities and organizations fear that the proposed Aginskoe mine could cause harm or extirpation of some of the species located here, and lead to the degradation of salmon spawning habitat downstream, which is some of the most important salmon habitat in all of Russia. They warn that the development of the mine will also compromise the integrity of UNESCO's World Heritage Site system as an internationally accepted tool for nature conservation- a body to which Russia, Canada and the U.S. are members. Meanwhile, the proposed Aginskoe gold mine has not succeeded in getting the necessary "Positive Expertisa," the environmental due diligence process required under Russian law. In 1991 a Russian Expert Commission of the Kamchatka Academic Environmental Institute recommended against mining development generally in this region of rich biodiversity:

"One can say right away: if we are talking about thousands of tons of potentially toxic ore in a damp area with potential showers; thousands of tons of burned diesel fuel; hundreds of tons of coal and benzene with high content of tetraethyl-lead; chlorate organic flows and uses of explosives...all that in the mouth of a spawning river--then not one hydrobiologist, hyrdochemist, environmentalist or toxicologist will guarantee the preservation not only of the river's spawning qualities, but also of elementary life forms."

Beginning in 1995, Russian and U.S. NGOs vigorously urged OPIC to not support Grynberg Resources' application for financing support for the Aginskoe project. In 1996 OPIC turned down Grynberg Resource's proposal. OPIC went on to categorically prohibit any similar project in the future "in or impacting World Heritage Sites, UN listed National Parks, Habitat/Species Areas" or similarly protected areas.

Project sponsors have repeatedly questioned the interpretation of the World Heritage Site protection of the region, and sought to reverse OPIC's decision, but to no avail. Project sponsors are now rumored to be seeking financing and/or insurance support from ECAs with lesser environmental standards, such as the Canada's Export Development Corporation (EDC).

Recommended Actions

ECAs should internationally agree to categorically prohibit projects in or impacting World Heritage Sites. Russian and U.S. NGOs and intergovernmental conservation bodies remain adamant in their opposition to the Aginskoe mine. Support for Aginskoe by any ECA will be viewed as one of the most flagrant examples of their fueling the "race to the bottom."

VI CASE STUDY: OCENSA PIPELINE, COLOMBIA

Japanese and Italian ECAs support an oil pipeline project that reportedly failed to comply with host country environmental laws resulting in oil spills and forest degradation. The Colombian Army is accused of massive human rights abuses to protect the pipeline from a guerilla insurgency, leading to condemnations by MPs in the British Parliament. Right wing death squads kill 11 people and abduct 40, leading to a strike of oil and pipeline workers that halts all pumping operations in the pipeline. Guerillas blow up the pipeline with dynamite, creating a huge fireball that burns alive 56 people, 28 of them children, and seriously injures over 100--Colombia's worst civil disaster in 34 years. The Ocensa Pipeline project demonstrates that ECA-backed projects lacking attention to social and environmental concerns result in severe political and economic risks.

ECA Support

Japanese Export-Import Bank (JEXIM) approved a direct loan of $121 million for the pipeline, and an untied loan of $300 million to develop the Cusiana and Cupiagua oil fields. SACE (Italy) backed $296 million of loans with a 5 year guarantee. Private Company owners include Ecopetrol (25%), TransCanada Pipelines and IPL Energy (17% each), British Petroleum and Total of France (15.2% each) and Triton Energy (9.6%).

Project Description

The Oleoducto Central, or OCENSA project, used the financing to build the $2.1 billion crude oil pipeline from Cusiana and Cupiagua fields in the eastern foothills of the Andes to the Caribbean port of Covenas.

British Petroleum pumps some 400,000 barrels a day from its Cusiana and Cupiagua fields, in eastern Colombia, through the 800-kilometre Ocensa pipeline

In its short life, the Ocensa pipeline project has been an environmental and social disaster. In August of 1997, Colombia’s Environment Ministry imposed fines and penalties on British Petroleum, Triton Energy and Ecopetrol for damage caused during the construction of Ocensa. The Ministry cited apparently large amounts of crude oil spilled during construction and testing and laying of pipeline in non-approved areas. Besides a cash payment of several thousand dollars, the companies were required to make large investments in the planting and maintenance of 148 acres of trees, due to damage caused during deviations from the plans allowed by Colombian authorities.

In May1998, the main oil workers union in Colombia went on strike to protest the murder of 11 people and the abduction of more than 40 others by army-supported right wing death squads allegedly involved in protecting the pipeline against guerillas. Then in late October of 1998, guerillas attacked the Ocensa pipeline with dynamite, causing a huge explosion that demolished a rural hamlet, killing 56 villagers (28 children), injuring over 100 others and causing severe environmental damage still being assessed. Officials are investigating the explosion and subsequent fires in Machuca, a village 180 miles north of Bogota, but they said evidence pointed to the National Liberation Army, the country's second-largest guerrilla group.

It is evident that the political risks associated with this project warrant the highest environmental standards possible through ECA leverage. Britain's Guardian newspaper recently (October 17, 1998) accused British Petroleum of trying to supply arms to the Colombian army, regularly accused of severe human rights abuses, to protect its oil operations in Colombia. The accusations were repeated by several by several MPs in the British Parliament (Financial Times, October 21, 1998). BP suspended its security chief in Colombia,

Roger Brown, and the company said it had opened an internal inquiry. But BP, one of the main shareholders in the Ocensa consortium whose 500-mile oil pipeline runs from the foothills of the Andes to the Caribbean coast, denied the allegations. (*Washington Times*, 10/20/98).

Recommended Action

The extreme lack of transparency on the part of JEXIM and SACE raises serious questions concerning preparation of environmental documents, including public consultations, related to the project, including any possible emergency response plans meeting international standards that responsible ECAs should have required to mitigate political risk to the project. Without appropriate emergency response plans subject to public accountability, necessary environmental protection in explosion situations is problematic.

VII CASE STUDY: URUCU GAS AND OIL PROJECT, AMAZONAS, BRAZIL

JEXIM is helping to finance with a 7.8 billion yen ($64 million) loan the construction of the Urucu Gas Processing Plant in a remote area of the western Amazon rainforest. The plant will provide gas that is to be transported to Manaus and Porto Velho (mainly to fuel electric power generation) through two rainforest pipelines, 480 and 500 kilometers in length, respectively. The pipelines require a 15-30m-wide construction and service road along their entire length, clearings big enough for helicopters made every 15km; roads and clearings must be kept open for life of project (20-50yrs). The JEXIM financed gas plant is the keystone of a huge scheme which has the potential to repeat the most destructive chapters in Amazon forest destruction since the pipeline construction and roads will act as conduits for loggers, miners, ranchers, and colonists to spread deforestation, and unsustainable resource mining into hitherto pristine areas, in some cases inhabited by isolated, extremely vulnerable indigenous groups. Environmental impact assessments underway, construction in 1999. But in Manaus, the main user of the gas, energy demand is currently met, and NGOs have proposed less costly and risky alternatives. Already construction activities along the pipeline have led to increased prostitution, disease, including rapidly spreading AIDS, violent crimes, robberies, domestic violence and drug use. The Urucu Gas and Oil Project demonstrates that ECA-backed projects lacking attention to associated social and environmental concerns risk catalyzing "development disasters" of the sort tragically familiar in the Amazon.

ECA Support

Japanese Export-Import Bank (JEXIM) committed about $64 million, 7.8 billion yen in 1997 for the construction of the Urucu Natural Gas Processing plant.

Project Description

This project expands oil and gas production of the Brazilian State oil company, Petrobras, in the Urucu oil field, an area of highly dense tropical forest, among the most remote and least ecologically disturbed of the Amazon basin.. The main use of the gas and oil will be for additional electricity generation in the cities of Manaus and Porto Velho, where energy demand is currently met and for whose energy needs several less economically and environmentally costly alternatives have been proposed. The total project cost is estimated at about $1.5 billion.

Transporting oil and the gas produced by the plant will require a terminal and storage facilities in the town of Coari, as well as two additional pipelines (480km, 500km). The environmental impact analyses for these projects are currently underway and construction is slated to begin in 1999.. The pipelines are to be buried 1-3m underground. Laying and maintaining the lines requires the opening of a 15-30m-wide road along their entire length. Every 15km, clearings large enough for a helicopter to land are made. The road and clearings must be kept open for the life of the project (20-50 years). No other single factor more clearly leads directly to deforestation, uncontrolled migration, and the invasion of existing protected areas in the Amazon, than the opening of new roads.

Various small, rural communities along the Urucu and on the Solimoes Rivers already have suffered from construction of the first stage of the pipelines completed in 1998, from the plant at Urucu to Coari. The pipeline road blocked three streams, formerly used by communities for drinking water, bathing, washing and manioc flour (a principal source of income and subsistence staple) ceased. Drinking water had to be brought from a considerable distance. Various other creeks used by local populations along the Urucu River were silted up or rendered inaccessible by the pipeline. Fish populations are said to have fallen dramatically in the Urucu. Increased traffic on the river aggravated the already existing problem of invasions

by industrial fishing boats. Since fish is a staple food source for the riverine communities, this is an especially serious problem. Brazil nut and fruit trees were cut down in several places. This is a violation of Brazil's forestry code; compensation was in some instances only paid to the "patrons". The project's effect in stimulating rural-to-urban migration has had unforeseen and serious negative consequences.

The town of Coari, where gas from the JEXIM plant is to be stored , has seen an influx of about 7,000 people and is now known as "the whore of the Solimoes" - prostitution, child prostitution, drug traffic, robberies, domestic violence and sexually transmitted diseases including AIDS have increased.

Both pipelines have the potential to repeat the most destructive chapters of the history of Amazon development by acting as conduits for loggers, miners, ranchers, and colonists to spread deforestation and unsustainable resource mining into previously isolated pristine areas, in some cases inhabited by isolated, extremely vulnerable indigenous groups.

Recommended Action

Brazilian NGOs and organizations of the Catholic Church have proposed several less destructive alternatives, including purchasing existing excess capacity from the Guri dam in Venezuela that would meet the projected power needs of Manaus for the next 25 years at less economic and environmental cost. The JEXIM Bank is the financial linchpin for a huge, environmentally risky scheme that already is on track to catalyze a major development disaster of the sort tragically familiar in the Amazon.

VIII CASE STUDY: BHP'S OK TEDI COPPER AND GOLD MINE, PAPUA NEW GUINEA

Australian ECA environmental standards are not "OK." Mining projects supported by Australia's Export Finance and Insurance Corporation (EFIC) in Papua New Guinea leave a river "biologically dead" and fail to consider or address basic concerns of local inhabitants.

ECA Support

EFIC, Ex-Im, Jexim. A $243.8 million line of credit for Australian goods and services was provided by the government owned Export Finance and Insurance Corp. to an international consortium led by Australia's Broken Hill Properties (EFIC) (E&MJ, September, p 9). US Export-Import Bank approved loan of $81.2 Million to an undisclosed U.S. company.

Project Description

Located on Mount Fubilan near the OK Tedi and Fly rivers in the Star Mountains in the Western Province of Papua New Guinea (PNG), the Ok Tedi mine is the third largest open-cut copper mine in the world. This remote region is also home to several thousand indigenous peoples who depend on clean water and the abundance of healthy wildlife in the area to maintain their subsistence economy.

The OK Tedi mine (OK Tedi Mining Limited; OTML) is 52% owned by Broken Hill Proprietary (BHP; Australia's biggest mining company), 30% by the PNG government, and 18% by Mettal Mining Corporation. In 1987 BHP took over control of the entire OTML which it is expected to operate until the year 2010.

According to the Multinational Monitor, the OK Tedi mine dumps 80,000 tons of waste rock tailings containing lead, cadmium, zinc and copper daily into the Fly and Ok Tedi Rivers. The PNG government originally required the mine to maintain a dam to hold back these tailings, however a 1984 landslide destroyed the impoundment, which was then not rebuilt. Original designs for the dam were apparently not approved by the PNG government, and the consulting firm Bechtel stated that a more successfully designed dam could have easily been built nearby.

Subsequent to the dam failure, OTML admitted in internal reports that the upper Ok Tedi fish stocks had declined between 50% and 80% following the mine development and subsequent dam failure. Conservation groups fear the situation is even worse; according to the Australian Conservation Foundation, nearly 70 kilometers of the Ok Tedi river became "almost biologically dead," and 130 kilometers of river bank (including gardens, plantations and forests) had been "severely degraded" following the dam failure. Elevated levels of copper sediments from the mine are reported by the Multinational Monitor to have flowed into the Fly River, causing 30,000 downstream landowners to loose their ability to derive income from fish and garden crops.

The PNG treasury has seen minimal returns from the Ok Tedi mine. For example, while the mine reportedly generated as much as $120 million in earnings in some years, OTML allegedly paid no taxes to the PNG government until October 1995, and even then it reportedly paid only $3.75 million.

In 1994, approximately 30,000 villagers from over 30 clans were represented in a lawsuit against BHP in Australian and PNG courts, seeking damages for the mine's pollution of rivers and consequent damage to these peoples' ability to derive existence and to maintain their traditional way of life. As the case proceeded, BHP drafted and advocated for PNG legislation that would have levied fines of up to $75,000 against anyone who would sue (or assist another

person to sue) the company, or legally challenge the constitutional validity of the company's proposed law.

Meanwhile, judges and human rights activists in the region decried BHP's blatant attempt to control civil society in PNG, arguing that such moves threaten the long-term political stability in a region that has recently experienced armed conflicts connected to controversies over other mines.

Subsequent to the villagers lawsuit a compensation package was passed by a regional legislature, allowing for $82 million to be shared by 30,000 landowners over the course of the mine's remaining 15 years, or about $12 per person per year. Subsequently, an act was passed making it illegal for PNG landowners to take future legal actions for compensation if they are effected by other resource projects in the country.

Following the Ok Tedi debacle, Australian and other environmental activists began to campaign for legislation requiring Australian-based companies operating abroad, as well as the Australian export credit agencies, to uphold the same environmental and social standards that are required domestically. If EFIC and Exim had required this project to uphold World Bank environmental standards, the Ok Tedi disaster, and the subsequent economic, political and social costs may have been avoided. Since this time, Exim has adopted strengthened standards.

Recommended Action

Ok Tedi clearly demonstrates the need for common, internationally recognized environmental and social standards to be stringently applied by ECAs.

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IX CASE STUDY: MANANTALI PROJECT, (MALI, MAURITANIA, SENEGAL)

Supported by the German and Swiss ECAs (Hermes and ERG), the Manantali Project (mixed purpose irrigation, navigation and hydroelectric dam, power plant, transmission lines) on the Bafing River has destroyed 120 km2 of forest, led to the near destruction of flood recession agriculture, forcibly resettled 12,000 people, afflicted surrounding populations with water-borne diseases such as Bilharziosa, and catalyzed regional violent conflict. The project entailed ill-advised legal changes in land tenure rights along the Senegal River which led to massacre of Senegalese farmers by Mauritanians, triggering an ethnic explosion in Senegal. Hundreds were killed and 10,000s of Mauritanian shop-owners deported. The militaries of Senegal and Mauritania engaged in armed skirmishes and nearly went to war. ECAs and European aid donors financed the scheme in the 1980s, despite the World Bank's 1979 refusal to support what it judged to be an economically unsound investment. After huge cost overruns the dam was completed in 1988, but the power plant was not built, and the river was not navigable, making the $500 million investment worthless, entailing major loan defaults. A decade after the dam's completion, donors (including the World Bank, despite the abstentions of the U.S. and Switzerland on the Bank's Board) have negotiated new loans of nearly a half billion dollars to finally build the power plant. The then German minister for development assistance, Carl-Dieter Spranger called Manantali in 1993 an "act of economic and environmental nonsense", and the African Development Bank said that due to Manantali "social disparities and malnutrition" have increased and that the rich Senegal valley has become "the poorest [area] in all three countries." Manantali illustrates that the 'race to the bottom' among ECAs and donors without common standards entails not only environmentally and socially disastrous investments, but results in huge stranded 'sunk costs' which then become the rationale for further loans and the growing indebtedness of some of the poorest countries on earth.

ECA Support

Manantali Dam: the Swiss government Export Risk Guarantee (ERG) provided guarantees of SFrs. 155 million for civil works contract. KfW funding (18% of total) was covered by Hermes guarantee. ECA cover subsidized loans for contracts awarded to Zublin (Germany) and Losinger (Switzerland). Aid donors included the Islamic and African Development Banks, several Arab governments, Italy, the French CFD, the German KfW, the Canadian CIDA and the European Union.

Project Description

In 1972, the governments of Mali, Mauritania and Senegal set up the Organisation pour la Mise en Valeur du Fleuve Senegal (OMVS) in order to promote irrigation, power generation and navigation in the Bafing and Senegal valleys. Under the auspices of the OMVS, construction of the Manantali dam began in1981. The purpose was to irrigate an area of 3,750 km2, to generate hydropower, and to allow navigation between the cities of St. Louis and Kayes. At the same time, the Diama dam was built at the river delta to prevent saltwater intrusion into the lower valley.

Both the Manantali and Diama dams were completed in 1988. Although by then all funding had been eaten up, the power station had not been built, and the river was not fit for navigation. The project has had severe negative impacts on regional ecology, agricultural production, fisheries, public health and political stability of the area. It has destroyed 120 km2 of forest, and caused the involuntary resettlement of 12,000 people. The Manantali and Diama reservoirs have infested the Bafing and Senegal valleys with water-borne diseases, Bilharziosa being most prevalent. The Norwegian government has refused to support the power plant completion because of unresolved further public health impacts.

Due to the expected benefits of the project, land legislation in Mauritania was rewritten. The land rights of the black peasants who had lived along the Mauritanian riverbank for generations were abrogated. In 1989, the killing of Senegalese farmers by Mauritanians triggered an ethnic explosion in Senegal. Hundreds of people were killed and 10,000s of Mauritanian shop-owners were deported. The military of the two countries engaged in armed skirmishes and nearly went to war over the conflict.

At $25,000--$40,000 per hectare, construction costs of irrigation networks from the dam reservoir greatly exceeded estimates, and to date only 100,000 hectares have been irrigated as opposed to original projections of 375,000. Much traditional agricultural production of sorghum, relatively sustainable economically and environmentally, has been replaced by rice production. Local rice has however turned out to be totally uncompetitive with imported rice, driving farmer 'beneficiaries' of the project into indebtedness and destitution. The dam has reduced the annual flood on the Senegal River to an artificial two-week flood, and the long delayed hydropower plant will further compete with water releases for the artificial floods for agriculture. It will also further impair the vital functions of recharging the groundwater table of downstream areas and sustaining remaining fish habitats. The dam has significantly reduced fishing, on which over 100,000 people depend on for protein, as well.

A study financed by USAID in 1994 documents that villagers in Senegal and Mauritania "clearly state that their health has deteriorated in the past few years because of the deterioration in their diet. They are convinced that before the construction of the dams, when they produced traditional food recession crops (...) their diet was more varied and hence more healthy". On September 26, 1997, 250 farmers from the Senegal valley attended a public meeting where public outcry was summarized by a speaker for many of the farmers, Thierno Oumar Sow, who said the Manantali dam had caused "poverty, famine, and indebtedness". The official Appraisal Report of the African Development Bank on the new hydropower project supports this bleak assessment. According to the report, "the absence of or the low flood level induced by the retention of the Bafing waters by the dam (nearly 60 % of the river flow), seriously disturbed the basin's ecosystems and disorganized its traditional economic activities, as a result of which the region became the poorest in all three countries. The appearance and increase of social disparities and malnutrition led to the massive exodus of labor force from the basin."

Recommended Action

The Manantali case clearly exemplifies the need for common social and environmental standards among the ECAs.

X CASE STUDY: PORGERA MINING PROJECT, PAPUA NEW GUINEA

The Porgera gold mine in the Enga Province of Papua New Guinea (PNG) has been operating since 1990. Since then, the mine has brought to this remote part of PNG a record of environmental destruction and social dislocation. The pollution associated with the mine is arguably worse than that of the notorious OK Tedi mine.

Due to the heavy involvement of Australian mining companies, backed by the Australian export credit agency EFIC, environmental and human rights groups are demanding immediate action from the Australian Government to control activities of these companies and to "cease insuring and subsidizing projects which are economic, social and environmental disasters for local landowners and for PNG**."** *(Mineral Policy Institute, Australia).*

ECA Support

Australia's Export Finance & Insurance Company (EFIC) credit line of $120 million to Highlands Gold (65%-owned by MIM Holdings) to assist in that company's 30% share of the financing for the giant Porgera gold mine in Papua New Guinea Porgera Joint Venture.

Project Description

Located above the Srickland-Maiapam River in the Western Province of Papua New Guinea, the Porgera gold mine is one of the world's largest. The mine is operated by the Porgera Joint Venture (PVJ), comprised of three Australian companies, Placer, Renison Goldfields and Highlands Gold.

The mine discharges hazardous and potentially toxic wastes far in excess of the levels permitted under Australian law and, normally, under PNG law. These discharges have been measured at levels up to 3000 times PNG limits. Levels near the discharge point are so high in heavy metals that the area would be declared a contaminated site within Australia and would likely lead to a Government investigation in to the impacts on human health. The levels of contamination are normally only found in the world's most polluted industrial sites. Porgera gold mine has routinely discharged 40,000 cubic meters of tailings per day into the Maiapam-Strickland River. Resultant pollutants discharged into the river system include heavy metal sulfides and hydroxides, including ferro-cyanide complexes and jacosites.

Such discharges are possible because the Porgera mine has no tailings impoundment facility, a practice long ago prohibited in Australia and the US, and by international finance institutions like the World Bank.

Mercury levels immediately below the minesite are at levels that would normally only be found below a mercury mine. This situation poses an extremely high risk to human health, and would not be permitted in Australia, or other developed countries. It occurs because EFIC and other participants have not agreed to put limits on the levels of mercury contamination.

According to the Australian-based Mineral Policy Institute, up to 133 unusual deaths have been reported by local officials between 1991 and 1993, which many link to contaminated water and riverside gardens originating from discharges from the mine. Local villagers' ability to sustain themselves traditionally through the use of riverside gardens has been compromised, and wildlife including fish, turtles and cassowaries are in decline. Villagers say that sediment levels are much higher than projected by the Porgera Joint Venture, causing flooding and preventing fish and crocodile breeding by eliminating windows of clear water for breeding. In addition the river has become shallower, impeding travel.

The Times of PNG reports that Porgera Company officials dispute that toxic materials have been found in the river, and "no connection could be drawn between the reported illness and the existence of the mine."

Drillbits and Tailings reported in 1996 that angry villagers shut down mine, burning seven vehicles. Australian environmental organizations called for an independent inquiry, a demand that was later joined by Australia's minister for overseas development assistance.

Recommended Actions

It is clear that EFIC's lack, in practice, of minimal international environmental standards, such as Australian or World Bank standards, enabled the mine to go forward without perfunctory environmental safety features such as tailings impoundment. Project performance risk is higher due to the lack of internationally accepted standards applied to Porgera.

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PART TWO: COUNTRY AND INSTITUTION CASE STUDIES

I. CASE STUDY: TOGO - POOR GOVERNANCE AND CORRUPTION SUPPORTED BY FOREIGN EXPORT CREDIT AGENCIES

This case study by Richard Gerster, former Director of the Swiss Coalition of Development Organizations, documents how Togo became the victim of mismanagement and corruption in business transactions supported by the Swiss ECA Export Risk Guarantee. Bad governance and corrupt business practices on the part of Togo, an aggressive sales policy by foreign private business and export credits as well as guarantees backed by Northern governments have in their combined effect led to a development debacle. Foreign loans were used to finance investments whose real value corresponds to a fraction of the original volume of credits. The profiteers have not had to bare the burden of Togo's financial crisis because of state guarantees of their own countries. It is the population at large and the farmers who now have to pay for the failed industrialization. Without the government insurance of the Swiss Export Risk Guarantee scheme, these disastrous projects, and the corruption that accompanied them would not have come to be. Governments betray sustainable development by supporting corrupt practices that have disastrous social and economic consequences in host countries.

Project Descriptions

- **ECA Support, Case 1:** Financing of Industrie Togolaise des Plastiques (ITP), was provided in the form of a loan from Credit Suisse. The project was extremely risky - so much so that the companies involved would not have become involved without the insurance of the export deal by the Swiss government via the Export Risk Guarantee (ERG) scheme. Right from its inception, ITP operated in the red. Losses of several millions of US dollars had accumulated, and a high official of the World Bank in Togo confirmed that the cost of building the plant (US $10 million) was significantly greater than the plant's real value of only US $3.7 million. No international invitation of bids occurred. The deal permitted compensation of bribes involved in getting the contract, and to tacitly get ERG coverage via the inflated price for the plant.

- **ECA Support, Case 2:** Rolf Kohlgruber, owner of the Ofenbaugesselshaft Ber & Co. mbH of Cologne (Germany) and of Berg AG of Basel (Switzerland) convinced the government of Togo to guarantee a $5.8 million loan he obtained from the Swiss Bank Corporation to construct a corrugated iron factory. SBC only agreed to the loan on the condition that the delivery of the plant also be secured by the Swiss Export Risk Guarantee. Without the state guarantee by both Switzerland and Togo, the deal would most likely not have been consummated. Because Togo did not invite international bids, it ended up overpaying by SFR 5 million. An internal commission of inquiry submitted a report which stated "The profit is of an order that has to be qualified as immoral and fraudulent" and "One can only regret to [confirm the] Togolese side's imprudence in this affair".

- **ECA Support, Case 3:** Brown Boveri Company (BBC) of Baden (Switzerland) was the leader of the international consortium including Swedish and Austrian suppliers which financed a steel mill valued at US $51 million. ECA cover by the Swiss Export Risk Guarantee was essential for the financing of the deal. The Swiss part of the international consortium comprised supplies of SFR 40 million, shared by BBC (SFR 25 million) and Geilinger (Winterthur/Switzerland, SFR 15 million). The Union Bank of Switzerland (UBs) provided a commercial credit for the Swiss part of SFR 34

million (SFR 40 million less 15% down payment)—which the Swiss ECA Export Risk Guarantee insured for 75%. UBS would not have would not have assumed the financial risks involved without the Swiss state-backed guarantee. Frenchman Francois de Lannurien took over the plant's management and signed, as representative of the government of Togo, the loan contracts in favor of Sototoles that Kohlgruber had set up with Socinvest and Comeda. Thus, foreigners write invoices to be paid by the state of Togo. He also saw to it that there was no international invitation of bids. In 1986, the government of Togo leased the plant for SFR 14 million. Given the initial investment value of SFR 85 million, Togo had to shoulder a massive loss and the steel mill's electric furnace has since been shut down due to bankruptcy.

Recommended Action

ECAs should support sustainable development, not corrupt practices that have disastrous social and economic consequences in host countries. ECA projects should involve financial transparency and competitive bidding, rather than exacerbation of corruption and increased risk.

II CASE STUDY: ECAS IN SIBERIA AND THE RUSSIAN FAR EAST

ECAs leave a legacy of degraded forests and species habitat loss in Russia. NGO criticism of these and other projects leads to higher standards in the United States Overseas Private Investment Corporation (OPIC), which will be ineffective without upward environmental harmonization of all ECAs.

ECA Support

OPIC, US Export-Import Bank and Japanese Export-Import Bank

Project Descriptions

After the collapse of the Former Soviet Union (FSU), natural resource-extractive industries from around the world began to turn their interests toward Russia's immense expanses and vast natural resources. Russia's huge and theretofore largely unavailable oil and gas, minerals, forest and fisheries sectors seemed attractive and finally within reach to foreign investors and project developers. But Russia and many former Soviet republics remained politically and economically unstable, and many foreign companies would not do business there but for the leverage and cover of public finance and insurance institutions.

Since 1991, Multilateral Development Bank (MDB) natural resource development projects in Russia have proceeded more slowly when compared to bilateral export credit, finance and insurance agencies. This is especially true in Siberia and the Russian Far East (RFE), where such agencies such as the US Overseas Private Investment Corporation (OPIC) and the Export-Import Bank of Japan raced in to support projects to feed resource-hungry markets on the Pacific Rim.

ECAs in Russia began attracting the attention of NGOs in the early 1990; by 1994 Russian and US forest conservationists exposed that two US joint ventures that had received financing and insurance from OPIC. Located in Khabarovski Krai, the Global Forest Management Group and the Pioneer logging projects were involved in the clearing of primary forests and exporting of raw logs to Japan, while allowing little input of local citizens and avoiding the development of local timber processing jobs these impoverished outposts desperately needs. Neither of these joint timber ventures had obtained a "Positive Expertisa," which is legally required under Russia's environmental due diligence process. Nor would they publicly release Environmental Impact Assessments that were required as a condition of OPIC finance and insurance. In response, in November 1996, one U.S. NGO sued OPIC in Federal Court to obtain EIAs and other public interest documents under the US Freedom Of Information Act (FOIA). Independent site visits later conducted by NGOs and forest scientists at GFMG's logging area revealed seedling regeneration failures due to the stripping of too much of the protective tree canopy in this cold climate, and the elimination of irreplaceable primary forest stand structure and habitat in this once pristine region.

In November 1996, US Ex-Im Bank and the Russian State Timber Industry Company Roslesprom signed a Memorandum of Understanding to facilitate the export of tens of millions of dollars in US forestry and pulp mill equipment to Russia. Some Ex-Im Bank forestry and forest products sector projects may move forward, although perhaps less than otherwise would have if not for the fact that Roslesprom's Director Miron Tatzun was forced to resign amid allegations of corruption. Meanwhile, in 1995, US Trade and Development Administration awarded up to a half million dollars to local Russian officials to conduct a logging feasibility study for several areas including one that the US Agency for International Development was working with other local Russian officials to protect.

ECAs were also found to have expanded their activities into Russia's mining, oil and gas and fisheries sectors. OPIC is one of three international finance institutions (along with the Export-Import Bank of Japan) providing finance to the large Sakhalin II oil and gas project off-shore of Sakhalin Island in the Russian Far East. Inadequate oil spill response preparations threaten endangered grey whale populations, priceless stocks of wild salmon, pristine shorelines and the livelihoods of fisherman in Sakhalin and Northern Japan.

OPIC provided support for the Kubaka gold mine in the Russian Far East, which in 1997 was exposed for having sprung leaks in its toxic tailings retention dam, a facility that was later shown to have been designed differently than what was represented in publicly released environmental impact assessments.

Between 1996 and 1998 these US/Russian NGOs joined forces with other US groups that had worked on other controversial OPIC projects such as the Freeport McMoRan's Grassburg mine in Irian Jaya. This larger campaign challenged OPIC's reauthorization process in Congress, and successfully persuaded the Clinton Administration to pledge OPIC to issue revised and strengthen environmental policies in his United Nations General Assembly Special Session address on June 26, 1997. These new policies include mandatory disclosure of, and public comment period on EIAs, categorical prohibition against projects with untenable environmental problems such as large dams, projects located in primary tropical forests, those in or effecting World Heritage Sites, National Parks and other similarly protected areas. These policies now represent a good example of minimal environmental standards for all ECAs to adopt, and help reduce political and economic risks that these agencies were designed to insure against.

Meanwhile, Russia's current economic crisis poses new risks for ECA-backed projects--and their ability to maintain environmental standards and achieve compliance. Russia's pronouncement in 1998 that it will suspend debt payments to external creditors raises questions about whether project defaults and other destabilizing institutional events could make it difficult for ECAs to enforce environmental conditionalities of loan agreements or manage environmental problems at project sites.

Recommended Action

These projects demonstrate the need for common environmental standards among all ECAs. Other investment insurance and finance agencies should follow OPIC's lead and adopt strong and transparent environmental and social standards.

III CASE STUDY: EXPORT CREDIT AGENCY FINANCE IN INDONESIA

Titi Soentoro, Bioforum and Stephanie Fried, Environmental Defense Fund

Introduction

ECAs have played a major role in financing environmentally and socially unsustainable investments that have depleted Indonesia's extraordinary natural wealth. As a result, the country experienced the rapid depletion of its natural resources. During the Suharto regime, forest degradation reached a rate of two million hectares per year. Investment projects such as factories, plantations, and mines not only destroyed natural resources, but also gave rise to other significant environmental and social impacts including the destruction of the livelihoods of the local peoples who owned, managed, and utilized these resources. Security forces were used to prevent forest-dwelling, rural, and river-side peoples from defending the natural resources upon which their livelihoods and communities depended. In resource rich regions, the violation of human rights was a routine occurrence.

ECAs played a key role in assisting many foreign investors in supporting the Suharto regime system of economic and political monopolies. The regime's military security approach assured low costs for land appropriation and a relatively docile and inexpensive labor force. Foreign investors, often supported by ECA finance, competed to align themselves with the powerful business interests close to the Suharto family – through economic links -- i.e. the offering of cost-free investment shares -- to Suharto's children, other relatives, and business associates. In return, investors were assured of access to lucrative sectors of the Indonesian economy and were able to receive "assistance" from Indonesia's armed forces when it came to clearing people off of land for their projects, stifling labor unrest, or preventing mobs from storming their polluting factories.

The Role of Export Credit Agencies in Indonesia

Between 1992 and 1996, export credit agencies' exposure in Indonesia grew by 25%. By 1996, 24% of Indonesia's total external debt -- approximately $28 billion -- was held by export credit agencies (ECAs) supporting foreign investment in mega-projects linked closely to the Suharto regime.

The longer report on which this case study summary is based provides an overview of thirty-three projects in Indonesia supported by ECAs between 1994 and 1997, valued at total of $15 billion. It explores the relative contributions of the ten ECAs most active in Indonesia, looking in greater detail at the Export-Import Bank of Japan. It then provides a brief overview of the ten largest ECA-supported projects which account for $12.4 billion or 83% of the value of the thirty-three projects surveyed.

Of the 33 projects surveyed, the most significant amount of ECA-leveraged finance was concentrated in four sectors, the largest being the power and paper/pulp sectors, including support for a number of controversial mega-projects such as giant paper and pulp mills in Sumatra valued at a total of $4 billion -- Tanjung Enim Lestari (PT.TEL), Indah Kiat, and Riau Andalan Kertas – and the $4 billion corruption-plagued Paiton coal plants in Java. The third and fourth largest sectors with ECA involvement were mining and state-owned refineries, controlled by Pertamina, Indonesia's notoriously corruption-riddled national petroleum company.

The report examines in greater detail a number of the top ten ECA-supported projects, including the following four, which are representative of the environmental destruction and social repression in which ECAs have been a major accomplice:

Project Descriptions

- **PT. Tanjung Enim Lestari (PT. TEL):** (The following chronology is paraphrased from "Pulping the People" by Down to Earth, 1997.) The Barito Pacific Group, Indonesia's largest logging conglomerate, is the majority shareholder in PT. Tanjung Enim Lestari (PT.TEL) – slated to become Indonesia's largest paper and pulp mill -- and its sister company, PT. Musi Hutan Persada , designated to prepare massive pulp plantations to feed the mill. General Suharto's eldest daughter, Siti Hardiyanti Rukmana ("Tutut"), is also a significant shareholder in the mill. In 1994, the German Hermesbuergschaft, Japanese Export Import Bank (JEXIM), Finnish Export Credit, Swedish Exportkreditnamnden, and the Canadian Export Development Corporation supported a $1.5 billion finance package for PT. TEL. In 1997, Hermes, the Export Development Corporation, Exportkreditnamnden, the Finnish Guarantee Board, and Japan's OECF supported a $1.3 billion finance package for the mill. The signing of this finance package was predicated upon the signing of a pulp supply agreement with PT. Musi Hutan Persada to guarantee sufficient pulp for the mill. The entire output of the mill is destined for export.

  This company, from its pre-construction phase on, has been embroiled in substantial conflicts with surrounding communities. The company's plantation operation has apparently been involved in forced seizures of village lands. Indonesian officials and security forces have also reportedly threatened villagers with subversion charges if they resist the company's land grabs. In the wake of the ouster of Suharto, however, local communities in the area of the plant have begun to call for a halt of construction and are demanding the return of their seized lands. Citing environmental and social concerns, Indonesia's largest environmental organization, Walhi, has called for the cancellation of this project.

- **APRIL: Riau Andalan Paper and Pulp, Tjiwi Kimia**: Riau Andalan's parent conglomerate, Raja Garuda Mas, under its international entity, Asia Pacific Resources International Holdings (APRIL) has financed the expansion of its Riau Andalan mill, through a $750 million investment package supported by the Finnish Guarantee Board and the Swedish Exportkreditnamnden. This expansion allows the mill to convert four million cubic meters of wood into 750,000 tones of pulp each year. The company will be harvesting over 50 species of tropical hardwood from its logging concessions while waiting for its plantations to mature. In October, 1997 conflicts between local communities and the company escalated after Riau Andalan announced that it would no longer honor an earlier land compensation plan and that it planned to build a road directly through ancestral lands owned by the communities. Security forces became involved and the resulting protests led to the hospitalization of several villagers and the arrest of the village's legal representative. In April, 1997, Indonesia's Environmental Impact Assessment Agency, BAPPEDAL, blacklisted Riau Andalan for water and air pollution and for conflicts with local villagers.

  In addition, APRIL runs the troubled 240,000 ton per year Indorayon Utama mill, also in Sumatra, which was shut down by angry villagers and students after Suharto's ouster. Over 1,000 members of the security forces were brought into the region to break up a blockade by protestors who had hampered production at the mill since mid-June, 1998. From its earliest stages of development, Indorayon has been

involved in conflicts with local villagers as a result of the forced seizure of their lands for pulp plantations and the heavy-handed use of security forces to silence opposition to the mill through the issuance of threats and bribes.. The mill was the subject of a court case brought by WALHI as a result of its pollution of the Asahan river.

In 1996, Hermes provided a $5.6 million guarantee the shipment of German equipment to APRIL's Tjiwi Kimia paper factory which utilizes the pulp produced by APRIL's troubled Indorayon Utama mill.

- **Sinar Mas: Indah Kiat:** Indonesia's second-largest conglomerate and the world's largest holder of oil palm plantations, Sinar Mas , owns the Indah Kiat pulp mill in Perawang, Sumatra which is financed through a $500 million investment package supported by Swedish Exportkreditnamnden, the Finnish Guarantee Board, Spain's CESCE, Denmark's Exportkreditfonden, and Canada's Export Development Corporation. Hermes and U.S. EXIM have also provided a $5.6 million guarantee, and a $4.5 million loan, respectively, for this mill, under separate financial arrangements. The 790,000 ton per year Indah Kiat mill is slated to consume 200 square kilometers of old growth forest per year until its plantations mature. For years, the mill has been embroiled in conflicts pertaining to the source of its timber for pulping and in 1993 was fined $1.4 million for the utilization of illegally felled timber. To supply land for its pulp plantation program and to obtain an inexpensive pre-plantation timber harvest, Indah Kiat's plantation operation seized and clear-cut over 3,000 hectares of the indigenous Sakai people's forest gardens, leaving the Sakai without cultivable land for their subsistence needs. Indonesia's most prominent environmental coalition, WALHI, documented the terribly polluted conditions of the Siak River downstream from the mill, noting dead fish bobbing by the factory's waste outlet and recording complaints of skin rashes by local villagers bathing and obtaining drinking water from the river downstream from the mill.

- **Paiton Power Project:** Financing for the massive Paiton coal plant complex in Java was provided in 1995 by a $2.5 billion finance package for Paiton One, covered by guarantees and loans from JEXIM, MITI, US EXIM, and OPIC and, in 1996, by a $1.7 billion finance package for Paiton Two provided by US EXIM, Hermes, the German Kreditanstaltfuerwiederaufbau (KFW), and C&L Deutsche Revision (Germany's public investment insurance agency—analogous to the U.S. OPIC). In December, 1998, the Wall Street Journal detailed the staggering corruption involved in the Paiton I deal which had been directly supported, over the years, by former Vice President Dan Quayle, President Clinton, Ron Brown, Robert Rubin, and Warren Christopher and Henry Kissinger, the latter two acting as lobbyists for a Mission Energy-General Electric joint venture which eventually succeeded in winning the project bid. According to the Wall Street Journal, the Mission-GE megaproject, as Indonesia's first private power venture, set the tone for all such investments to follow, including exorbitant power prices leading to private electricity costs, adjusted for local purchasing power, of 60% more than in the Philippines and 20 times as much as in the United States.

  According to Djiteng Marsudi, the head of Indonesia's now-bankrupt state owned electric utility, PLN, "the U.S. power companies dictated terms to us because they had Indonesia's first family behind them." PLN was ordered to utilize coal from a company owned by Hashim Djojohadikusumo, a Suharto relative by marriage, and Agus Kartasasmita, brother of then-Minister of Mines and Energy and current

> Economics Minister -- both partners of Mission-GE. Mr. Hashim's company planned to charge PLN 30% to 40% more than the going rate for coal. According to the Wall Street Journal, Mission-GE insisted that PLN pay an extremely high tariff for the electricity to be produced by the plant and suggested that more debt could be shifted to OPIC to cover the tariff, finally set at 8.6 cents per kilowatt-hour of electricity, 32% higher than comparable tariffs in Indonesia. When a US Exim Bank official visited Jakarta, several government and PLN officials told her that they didn't want and couldn't afford Paiton. 'It was a presidential decision," says Nengah Sudja, a former head of research for PLN. "Everybody knew it was nepotism, but we couldn't do anything about it."

According to the Wall Street Journal, government planners knew PLN was not ready for big private-power initiatives and the utility's "transmission grid leaked like a sieve." Indonesian government power consultants recommended smaller, environmentally and economically more sustainable alternatives such as geothermal and small gas-fired plants, and urged competitive bidding. Instead, Suharto, and then Technology Minister B.J. Habibie, now Indonesia's president, "hand-picked developers to lead the charge into big, high-risk, coal-fired power stations" according to these same consultants.

In the aftermath of the Indonesian economic crisis, PLN has told Mission-GE that it will not buy any electricity at all from the Paiton1,230 megawatt coal-fired plant next year, when it is scheduled to go on-line. ECA finance of over a billion dollars—backed by the taxpayers of the industrialized countries—has abetted a gigantic economic and environmental fiasco.

IV CASE STUDY: CANADA'S EXPORT DEVELOPMENT CORPORATION

"We are insuring Canadian investors against civil war or nationalization… Hypothetically, if the local people were to shut down any mine that we insured because of environmental problems, we would reimburse the company not the local people…We did not ask Monenco Agra, a Canadian company, for environmental assessments when we gave it a $ 12 million loan to supply equipment for the Three Gorges Dam in China, nor did we ask for such as assessment when we insured a $1 billion sale of a CANDU atomic reactor to Romania;" -EDC spokesman Rod Giles (source: *Inter Press Service,* April 3, 1996).

ECA Support
Institutional Case Study

Project Descriptions
Canada's Export Development Corporation (EDC) is a publicly owned export credit and investment insurance agency that finances industrial projects of Canadian corporations worldwide. EDC provides these taxpayer subsidized financial services to corporations without accountability or significant protection of the environment: EDC does not publicly disclose the projects it backs, nor does it require environmental impact statements or otherwise apply Canadian environmental laws to these projects. As a result, many of these projects have resulted in serious impacts on the environment and human health, and have consequently increased financial and political risks incurred abroad by the Canadian government-the kinds of risks that export credit agencies are supposed to insure against. Consequently, EDC is under increasing criticism from environmental organizations, and has been dubbed by Canadian environmental groups as "the wrecking ball of export credit agencies."

- **Kumtor Cyanide Disaster:** On May 20, 1998, high in the mountains of Kyrgystan, a transport truck carrying 20 tons of sodium cyanide crashed through a bridge and plunged into a river, dumping nearly two tons of this potentially lethal chemical into the river. Despite the clear and present danger, company officials apparently decided against informing downstream villagers for approximately five hours. As result, fear and panic ensued, ultimately leading to events which led to four reported dead, hundreds hospitalized, and five thousand evacuated. Soon after the spill, officials applied an application of sodium hypochlorate to the site in an attempt to neutralize the cyanide, which many observers believe to have caused skin rashes and other health ailments long after the spill. Weeks after the spill, women in local villages reportedly induced abortions after being told their fetuses had probably been poisoned. The mining truck was delivering cyanide to the Kumtor mine, which is partially owned and operated by the Cameco Corporation, and supported by $50 million in export credit by EDC.

- **Omai Gold Mine:** The Kumtor mine was not the first EDC-backed mine associated with a tragic cyanide accident: On August 19, 1995, the tailings dam for the enormous Omai gold mine in Guyana broke, spilling some four billion litres of cyanide-laced waste into a tributary of the Essequibo river, endangering human lives and killing thousands of fish. A Dam Review Committee, created to investigate the cause of the accident, found that the dam broke because of "inadequate application and execution of sound practice for design, construction, supervision and inspection that are well understood in current embankment dam and tailings dam technology." Later, The United Nations Development Programme stated that "baseline and continuous monitoring at Omai have largely been inadequate." The Omai mine is a project of Golden Star and Cambior, which faced multiple suits in Guyanese courts, a class action suit filed on behalf of Guyanese citizens in a court in Quebec, and adjudication of the case before the International Peoples' Tribunal on Human

Rights and the Environment. The Omai mine was made possible by $49.8 million in political risk insurance from EDC.

- **Three Gorges Dam:** The Export-Import Bank of the United States refused to support the Three Gorges Dam, recognizing its irreconcilable financial, environmental and social problems. Projected costs are reportedly spiraling out of control for the project. However, EDC and other export credit agencies have announced support for the Three Gorges Dam, "triggering a race to the bottom," where competition for projects by countries and governments is based on winning via the lowest environmental standards.

- **Candu Nuclear Reactor:** In 1998 EDC announced it will back the sale of Canadian Candu nuclear reactors to Korea, Romania and China between the 1997-2004 period, including $1.5 billion worth of loan guarantees for two reactors recently approved for sale to China. EDC will back the sale of these dangerous reactors despite the fact that seven of the outmoded Candu models were regulated and shut down for safety reasons in Ontario because of what one government official described as a "terrific list of mishaps and examples of sloppy mismanagement." Despite the fact these reactors were shut down for safety reasons in Canada, EDC will require no environmental impact assessment for their construction and use abroad. According to Elizabeth May, executive director of the Sierra Club-Canada. "In reality, Canada is showing an appalling contempt for environmental law in its crazed effort to find foreign markets for reactors that it can no longer build at home" (The Boston Globe, June 25, 1998). Sierra Club-Canada is suing the Canadian Government to force the application of Canada's environmental assessment laws to the sale of these reactors. Critics also charge EDC's support for nuclear reactors helped propel nuclear proliferation in a region recently gripped by India's and Pakistan's recent explosion of nuclear bombs.

Recommended Actions

EDC is expected to adopt new environmental guidelines at the end of March 1999. These guidelines should be equal in all respects to those of the Export-Import Bank of the United States and the U.S. Overseas Private Investment Corporation, and EDC should comply with Canada's National Environmental Assessment Act

V CASE STUDY: DEBT CREATING ASPECTS OF EXPORT CREDITS
by Michiel van Voorst, Eurodad, August 1998

Overview
A guaranteed export credit is a loan, usually made to a developing country, to allow that country to be able pay for an export contract. It will be usually made by the exporting company or a commercial bank. Part or all of the scheduled repayments are then guaranteed against the risk of non-payment by the government of the exporting country. These guarantees are issued by the national export credit agency, which will also supply insurance against political risk[3].

The rationale behind export credit guarantees is that economic and political uncertainties about developing countries are a disincentive for Foreign Direct Investment (FDI) and trade in general, and project finance in particular. Therefore, export guarantees and investment insurance should help to increase financial flows to developing countries.

However, export guarantees and investment insurance turn out to be primarily trade-promoting instruments for companies in the North rather than development-oriented instruments for the Third World. The economic, social and environmental consequences of the projects supported are dubious, and the 'ambiguous' character of export credits and guarantees only further aggravate the problem. Exporters enjoy the full yields if a project is successful but are also able to transfer the losses to the public sector when confronted with the risks of international finance. This is a clear case of moral hazard: exporters are incentivised to maximize their exports, in the knowledge that they will - at public expense - be bailed out of deals that go bad. This also distorts pricing: the financing terms of deals do not reflect the real level of risks, with the illusion of cheap financing encouraging unnecessary borrowing. Clearly, this leads to inefficient allocation of capital, corruption and waste.

As public entities, export credit agencies are supposed to help bear responsibility for promoting sustainable and equitable development in developing countries, but too often these agencies' actions conflict with domestic priorities.

Recent Developments
Export credits are one of the most important sources of financing for developing countries. Between 1990 and 1995, total export credits grew by 11 percent annually. This strong expansion was driven by more aggressive export promotion and the changing nature of international financing for developing countries, which has shifted to project finance[4] and direct investment projects. About half of the new export credit commitments during this period were related to large infrastructure projects in power generation, telecommunications and transport. In 1996, the total exposure to developing countries amounted to US$463 billion, a two-percent decline compared with 1995 but about 40 percent higher than in 1990. The Japanese, American, German, French and Italian national export credit agencies in particular are large suppliers of guarantees and insurance (Gerster, 1997, pp. 124).

New export credit guarantee commitments have increased strongly during the 1990s, and also private investment insurance is quickly gaining importance. In the period 1990-1996 export

[3] There are three broad categories of investment insurance risk that are usually covered by bilateral and multilateral agencies: currency (in)convertibility and transfer, nationalisation and expropriation (without compensation) and war and civil disturbance

[4] According to the World Bank (1998, pp. 58) project finance is one of the fastest growing forms of external finance in the 1990's, and typically involves a package of financing arrangements that may include export credit guarantees, commercial bank loans, equity debt and different types of contingent liabilities of the host government

agency commitments to developing countries averaged US$110 billion a year and in 1996 new commitments amounted to US$94 billion (World Bank, 1998, pp. 58). The decline in new export credit commitments in 1996 reflected partly growing concerns about the macroeconomic situation and financial sector fragility in emerging markets, especially in Asia. Following the economic collapse of Asia and the subsequent problems in Russia, South Africa and South America, new commitments are likely to fall further in 1997 and 1998.

Export credit agencies exposure is concentrated in only few countries; the ten main recipients accounted for 55 percent of agencies' total exposure. Table 1 lists the ten largest recipients of export credits (Boote & Ross, 1998, pp. 12). This table clearly shows that only a small number of middle-income countries receive the bulk of new export credit commitments.

The multilateral institutions have expanded their guarantee activities during the 1990s. The World Bank Group[5] covered private investment flows worth US$ 4.5 billion in 1997, compared with US$ 1.4 billion in 1991 (World Bank, 1998, pp. 60-61). Also a number of regional development banks, such as the Inter-American Development Bank, the Asian Development Bank and the European Bank for Reconstruction and Development increasingly provide guarantees. The development banks are however supposed to promote development in the Third World and thus have a very different core mission than export credit agencies. According to the World Bank their guarantee activities intend to serve as a catalyst for private sector activities in developing countries and increase their integration with the global economy. Reasonable as this may sound, World Bank - or other development bank - guarantees can be as disruptive as any guarantee issued by an export credit agency.

[5] IFC finances most of the coverage provided by the World Bank Group, but also IBRD and MIGA offer different kinds of guarantees. Currently IDA, the World Bank's soft lending facility for LICs, has also a pilot project for IDA's provision of partial risk guarantees against country risks, see for more details World Bank (1998, pp. 61).

Debt Creating Aspects

If an export guarantee is activated the liability owed to the private sector passes to the public sector, and is added to the total stock of official bilateral debt. Export credits thus bear an ambiguous identity because a private claim can be turned into a public claim. Most national export credit agencies operate however in a secretive manner and on neither the creditor nor the debtor side is the public fully aware of the financial and qualitative consequences. Export guarantees create the illusion of cheaper capital by making funds available at rates below market. It is often claimed that less financing would be made available if official cover were not provided. This is probably true in the present system, as government guarantees are in effect creating subsidies, encouraging corporates to finance trade and exports that would otherwise be economically unviable. Not that less financing is necessarily a bad thing. The current system serves to encourage excessive lending: consistent year-on-year increases in export credit guarantees would seem to reflect an *exporter-driven* drive for business, rather than a *borrower-driven* need for funding.

A rethink of the current system would stem excess and unproductive lending, whilst maintaining an adequate flow of resources to developing countries. A reduction in the amount of government guarantees available would ensure that exporters price their lending to reflect risk levels, or insure themselves against those risks. Mechanisms exist that would enable them to do both of these things. Under the existing set-up, export credit guarantees are at risk of becoming tools to promote one country's exporters at the expense of another's. The original aim of financing important projects and key imports for developing countries risks becoming distorted. The lack of transparency and competition in the current system simply adds to these distortions.

These criticisms are backed up in a study[6] that analyses export credit guarantees and identified five main problems: excess flows, inappropriate projects, design weaknesses, overpriced goods and corruption.

The importance of export credits as a debt-creating vehicle for developing countries is clearly reflected in statistics on the indebtedness of developing countries. Export credit agencies are the largest official creditors of developing countries. The debts related to export credits account for 24 percent of total indebtedness of these countries and for 56 percent of their indebtedness to official creditors in 1996 (Boote & Ross, 1998, pp. 11). A few countries such as Gabon, Algeria, and Nigeria owe more than 50 percent of their total debt to export credit agencies (see table 2).

Although low-income countries (LICs) are not major recipients of export credits, these flows do represent a significant part of the debt stock for a number of LICs. For instance Lesotho, Congo DR, Cameroon and Congo have a relatively large portion of export credit related debt (see table 2). Since export credit related loans are usually less concessional than other official loans, they also figure disproportionately in a country's debt service profile.

Restructuring of Export Credit Debts

The overall debt problem of LICs in particular is very apparent and the export credit related debts constitute a major drain on developing country foreign exchange earnings. Many countries have been unable to fulfil their debt obligations in the past and were forced to enter the seemingly endless cycle of subsequent debt restructurings.

[6] See for more details Fues (1994, pp. 4)

The Paris Club[7] is the key forum for rescheduling guaranteed export credits. The Paris Club distinguishes two groups of debtors according to income and indebtedness. The severely indebted low-income countries[8] can qualify for a debt service or debt stock reduction of 67 percent (Naples terms) provided that the country can boast a satisfactory track record of IMF reform programmes over the past 3 years and has cleared its arrears with the Paris Club. This reduction is also applied to the export credit debt. It is however important to note that the reduction is only applied to *eligible* debt, i.e. all debt incurred before the country's first visit to the Paris Club. Debts contracted after this so-called cut-off date are excluded. Needless to say this significantly reduces the scope of the reduction, especially if the country has an early cut-off date. For instance, in 1995 Uganda (cut-off date 1982) received a 67% percent reduction of its eligible bilateral debt stock. This represented only a 2 percent reduction of its total debt (see for more details Eurodad, 1995). Since 1996 a small group of countries is eligible for an 80 percent reduction under the Highly Indebted Poor Countries Initiative[9]. Lower-middle income countries that do not qualify for Naples terms can qualify for a restructuring of their export credit debts at less generous terms[10]. Other middle-income countries cannot reschedule their export credit debts although some exceptions have been made in the past. Egypt, Poland and Russia have for instance benefited from exceptional relief measures (Martin, 1994, pp. 25).

Finally, because of the *preferred creditor status* of multilateral institutions all debts owed to these institutions need to be repaid in full[11]. This also applies to export guarantee related debts.

Conclusion

Export credits can be an important source of finance for developing countries. When applied in a more development-oriented way, export credits and guarantees can act as a catalyst for private sector activities *and* promote sustainable development in developing countries. However, it is too often the case that exporters' self-interest prevails over developing countries' needs. Protection of Western export sectors or political interest are factors that significantly influence the allocation of these flows. The secretiveness that shrouds the process creates an obstacle for efficient market behavior and the overall costs are high. Too many projects covered by export credits and guarantees do not perform and while exporters are using public funds to cover their losses, developing countries are facing the consequences. A quarter of total external debt[12] is owed to export credit agencies and this represents an enormous drain on these countries' scarce resources. Moreover, the social and environmental cost of projects covered by export credits and guarantees are often high.

Export Credit Guarantees should, as a rule, only be extended for development purposes. Commercial companies and banks are capable of assessing risks by themselves and using the appropriate tools to mitigate those risks. Moreover guarantees should only be extended where there is a specific need for the financing. In the current system, Western governments are

[7] The Paris Club is a forum in which creditors, mainly composed of OECD governments, meet a debtor government to negotiate the rescheduling of its debt. The negotiation process take place at the French Treasury in Paris.

[8] Countries with a GDP per capita below US$500 or a Net Present Value of debts to annual exports of more than 350%

[9] Although to date only six countries have qualified for this exceptional measure, and only one (Uganda) actually received a 80% reduction (see for more information www.oneworld.org/eurodad)

[10] Export credit related debt is restructured at more concessional terms: 8 years grace period and 14-15 years maturity. Conversion up to 10% or US$10-20 million (whichever is higher). Market based interest rates.

[11] The only exception is made for countries that have qualified for the HIPC Initiative, but as was said before this applies only to a small group

[12] For 1997 total external debt of all developing countries is estimated at US$2.17 trillion (World Bank, 1998)

creating moral hazard by underwriting private risk using public funds, which is leading to unnecessary and ill-judged lending and ultimately increasing developing countries' indebtedness.

In view of their development mission, multilateral institutions have in this respect large responsibilities and should set the example. The World Bank, and other development banks, should apply high standards regarding economic feasibility, social impact and environmental impact of projects that are being considered for a guarantee. Furthermore, much more coherence between export promoting policies and development policies in the North is needed. In different international fora, governments have been encouraged to sustainable and equitable development by taking into account human development and environmental factors for all financial assistance to developing countries. The time has come to put these intentions into practice.

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