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A Bilateral Strategy For Ex-Im Bank Reform

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Over the next few months, Congressional Republicans will face the critical decision of whether or not to renew authorization for the Export-Import (Ex-Im) Bank, the export credit agency of the United States.

While the issue currently divides Republicans, it's important to recognize the potential adverse economic consequences from reducing subsidies for small businesses that would create increased competition with foreign competitors continuing to receive export credit subsidies, but also find a way to reform an institution that has become synonymous with "crony capitalism". Just this past week, the Miami-based Hencorp Becstone Capital agreed to pay $3.8 million to settle allegations that it received Ex-Im bank funds using false documentation and emails recently uncovered by *The Wall Street Journal* show an extraordinary level of cooperation between Boeing and the Ex-Im bank on crafting policy around the loans Boeing receives.

A case for bilateral reductions in export credit subsidies while reauthorizing the Ex-Im bank

Indeed, subsidizing companies through credit export agencies like Ex-Im create distortions in the global economy. Namely, subsidies artificially inflate a nation's comparative advantage in certain industries. For instance, Ex-Im subsidizes aerospace manufacturing through subsidizing Boeing, which received nearly 70 percent of the Ex-Im bank's long-term loan guarantees last year, according to George Will at *The Washington Post*.

Reflecting this sentiment, Larry Summers last year made a bold observation in the *Financial Times* saying that indeed the Ex-Im bank represents "authoritarian mercantilism". However, he cautions that not reauthorizing the bank would be equivalent to "unilateral disarmament" without extracting any concessions on subsidy reductions from foreign export credit agencies.

This is a key point about the challenge of not reauthorizing Ex-Im. The primary challenge with ending Ex-Im subsidies is that other countries, through their own export credit agencies, will continue to subsidize the competitors of U.S. businesses that would be at a comparative disadvantage without subsidies. For instance, the French aerospace manufacturer Airbus, Boeing's primary global competitor, receives similar subsidies from France's export credit agency, Compagnie Française d'Assurance pour le Commerce Extérieur (COFACE).

The argument for reauthorizing Ex-Im made by some Republicans and business-minded interest groups, including the U.S. Chamber of Commerce, is that companies like Boeing would then be at a competitive disadvantage to companies like Airbus, through being unable to provide the same competitive pricing that government subsidies can afford.

Not reauthorizing Ex-Im could have immediate negative consequences for the economy if for example it resulted in the collapse in Boeing (that employs 165,529 individuals as of December) and other firms including the small businesses that receive $5 billion in financing and insurance subsidies.

The federal dollars lost through interest rate subsidies are very small compared to the overall size of the federal deficit. To put the costs of Ex-Im in perspective, the Ex-Im bank authorized $20.5 billion in financing whereas the 2015 fiscal year federal budget is expected to be roughly $3.9 trillion. As a result, the budgetary impact of not reauthorizing Ex-Im would only marginally improve the federal deficit in the short-run. Without extracting any concessions from foreign countries on export credit subsidies, tax dollars could be lost if Ex-Im supported firms suddenly failed from competition as global competitors continue to receive subsidies.

That's not to say that distortions to the economy don't need to be addressed through reform in the long-run through trade agreements that reduce export credit subsidies. Indeed, a 2014 Cato Institute study by Daniel Ikenson using data from 2007 to 2013 finds that Ex-Im subsidies spur downstream annual costs to industries of roughly $2.8 billion.

Trade agreements as a vehicle for Ex-Im bank reform

Congressional Republicans could avoid the negative economic consequences for businesses but still achieve considerable reform at Ex-Im through reauthorizing the Ex-Im Bank, but with the caveat that President Obama and Michael Froman, the U.S. Trade Representative, should push for international agreements on reductions in export credit agency subsidies in ongoing trade negotiations much like how they are currently negotiating for reductions in tariffs.

Namely, these international reforms could be applied to the Transatlantic Trade and Investment Partnership (T.T.I.P) with European nations and the Trans Pacific Partnership (T.P.P) with Asian nations. Congressional Republicans could negotiate export credit agency subsidy reductions as a condition in giving the President fast-track authority on trade, also known as Trade Promotion Authority (TPA).

Alternatively, the U.S. trade representative could work on bilateral agreements with other singular nations to reduce export credit agency subsidies that affect competition in both countries.

Reducing international export credit agency subsidies in tandem with Ex-Im subsidies would help offset the comparative disadvantage that would be born from asymmetrically only reducing subsidies in only the U.S. by not reauthorizing Ex-Im without any international concessions.

Businesses would then be less negatively affected by competitive burdens with reformed Ex-Im subsidies since global competitors would also lose their subsidies. In the preceding example, competition between Boeing and Airbus would remain unchanged if subsidies from both U.S. and French export credit agency were withdrawn proportionately through a trade agreement like the T.T.I.P.

Lessons from David Ricardo on comparative advantage

David Ricardo's famous theory of competitive advantage, presented in his classic *Principles of Political Economy and Taxation* published in 1817, is an important lesson and teaches us many things particularly about Ex-Im and export credit agencies throughout the world. One of those teachings is that to maximize economic growth in all countries, economic agents in each country should be left to specialize in the industries that they do best in and be free to trade their goods with other nations without the interference of government tariffs or subsidies.

U.S. trade negotiators, President Obama and Congress should take Ricardo's lesson to heart through negotiating reductions in foreign export credit subsidies in tandem with Ex-Im bank subsidies as part of our ongoing trade negotiations.