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CONGRESSIONAL TESTIMONY

The End of Ex-Im: No Threat to U.S. Exports

**Testimony before
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Chairman Poe, Ranking Member Keating, and Members of the Subcommittee, thank you for inviting me to testify this morning. My name is Diane Katz. I am a Senior Research Fellow in Regulatory Policy at The Heritage Foundation. The views expressed in this testimony are my own, and should not be construed as representing any official position of The Heritage Foundation.

Introduction

My testimony today will address whether the expiration of the Export-Import Bank charter has affected the ability of American companies to conduct global trade. The short answer is "No." As I document here, there is no shortage of private export financing. The primary beneficiaries of Ex-Im financing continue to secure billions of dollars of new orders without it. And, while subsidies inflict more harm than benefit, there are many state and federal programs to assist businesses—small businesses, in particular—with exporting their products and services.

A number of media outlets in recent weeks have reported that thousands of U.S. jobs are being moved overseas because Congress rejected reauthorization the Ex-Im charter. Such claims are unfounded.[1] The real story is that Boeing, General Electric and other top beneficiaries of the government bank are trying to scare Americans into further subsidizing their hugely successful multinational operations.

Bank proponents have spent tens of millions of dollars trying to convince Congress and the public that Ex-Im is a lifeline for American jobs. They also have engaged in a form of political extortion by threatening to withdraw contributions from members who do not act as they prescribe.[2] But it is critically important for Congress and the public to understand that export subsidies do not "create" or "support" jobs—they simply redistribute them from unsubsidized firms to subsidized ones. And the job numbers touted by Ex–Im advocates are dubious, at best. The Government Accountability Office, among others, has roundly criticized them as misleading.

It is likewise important to recognize that Ex-Im finances a meager 2 percent of U.S. exports. That means 98 percent of American exports (and the tens of millions of jobs that produce them) do not depend in any way on Ex-Im subsidies. Compared to other forms of financing, Ex-Im subsidies barely contribute to the growth of U.S. exports, as the chart below illustrates.

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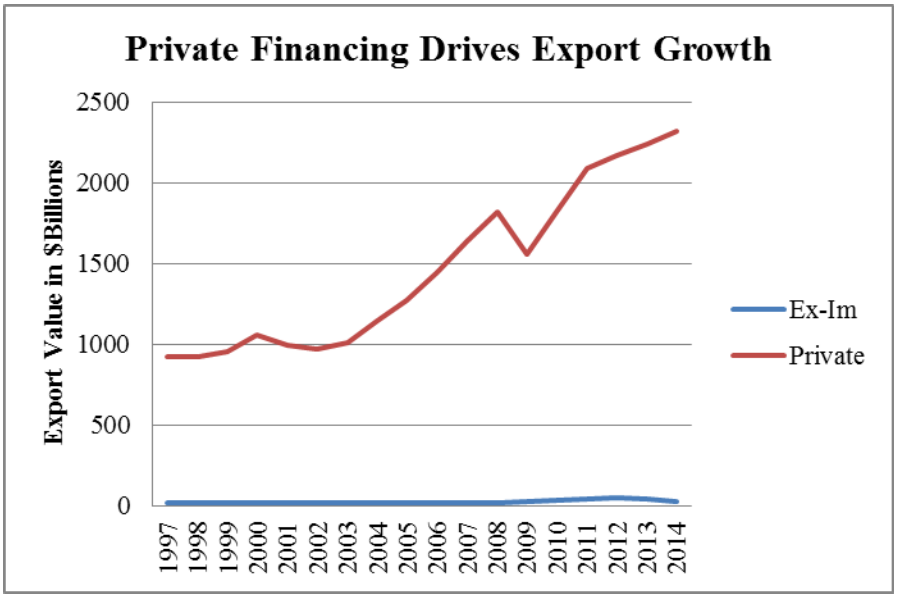
[1] See Diane Katz, GE's Cynical Ruse: Pretending Jobs Are Moving Because of End of Ex-Im Subsidies, Daily Signal, September 30, 2015, http://dailysignal.com/2015/09/30/ges-cynical-ruse-pretending-jobs-are-moving-because-of-end-of-ex-im-subsidies/ and Diane Katz and Veronique de Rugy, Don't buy the pro-Ex-Im hype, The Hill, September 23, 2015,, http://thehill.com/blogs/congress-blog/economy-budget/254536-dont-buy-the-pro-ex-im-hype

[2] Anna Palmer and Jeremy Herb, Boeing, GE cut off donations to Ex-Im foes, Politico.com, August 5, 2015, http://www.politico.com/story/2015/08/boeing-ge-cut-off-donations-to-ex-im-opponents-121056#ixzz3pJW9HM5i



Sources: U.S. Census Bureau and annual reports of the Export-Import Bank.

Ex-Im subsidies do impose costs on taxpayers and all the American businesses without access to export subsidies. Because Ex-Im financing is effectively discounted, foreign firms that receive it enjoy artificially lower costs when purchasing goods and services. Consequently, all the unsubsidized American companies—those paying higher finance costs—are at a competitive disadvantage in the global market. Ex-Im subsidies also drive investment from unsubsidized projects to subsidized projects—regardless of the merits. That's the essence of "picking winners and losers."

Most economists agree that subsidies yield more harm than benefit. As noted by scholar Matthew Mitchell, "Whatever its guise, government-granted privilege [to private businesses] is an extraordinarily destructive force. It misdirects resources, impedes genuine economic progress, breeds corruption, and undermines the legitimacy of both the government and the private sector."[3]

It may seem understandable that lawmakers regard Ex-Im as helpful to businesses in their district. But "helpfulness" is no justification for the federal government to supersede a fully functioning export-finance market. Every government action undoubtedly helps someone, but a citizenry dependent on government favors inevitably becomes subservient. That's precisely why the Founders restricted government power—and why subsidy schemes like Ex-Im should be eliminated.

<u>Charter Expiration and Employment</u>

In analyzing whether the charter expiration has impeded U.S. trade, it makes sense to first identify the primary beneficiaries of Ex-Im programs. That turns out to be a select few

[3] Matthew Mitchell, The Pathology of Privilege: The Economic Consequences of Government Favoritism (Arlington, VA: Mercatus Center at George Mason University, 2014), 1–2, http://mercatus.org/publication/pathology-privilege-economic-consequences-government-favoritism

multinational conglomerates. Between 2007 and 2014, more than 51 percent of all Ex-Im subsidies benefitted just 10 corporations.[4]

Boeing is the biggest by far, benefitting from $66.7 billion in subsidies during the past seven years.[5] Others in the Top 10 include:

2. $8.3 billion for General Electric (market cap $279 billion)
3. $5.2 billion for Bechtel (annual revenue $32.7 billion)
4. $3.2 billion for CBI Americas Ltd. (market cap $4.4 billion)
5. $3 billion for Exxon-Mobil Corp. (market cap $337 billion)
6. $2.7 billion for Solar Turbines Inc. (a subsidiary of Caterpillar)
7. $2.3 billion for Caterpillar (market cap $42.5 billion)
8. $2.1 billion for Applied Materials Inc. (market cap $19.6 billion)
9. $2 billion for Westinghouse Electric Co. (annual sales $10 billion)
10. $1.4 billion for Noble Drilling (market cap $3.2 billion)

These and all the other deals involving titans of industry belie bank advocates' claims that Ex-Im subsidies are necessary to fill "gaps" in financing. Indeed, in the months since the charter expired, Boeing (as an example) has secured multiple export deals worth billions of dollars, including:

- An $8 billion order from Taiwan-based EVA Airways for 24 Dreamliners (787-10s) and two Extended Range jetliners (777-300ER).

- The sale of Boeing Converted Freighters (737-800) to China-based YTO Airlines.

- The sale of 22 Apache attack helicopters (AH-64E) and 15 Chinook heavy-lift helicopters (CH-47F) for the India Ministry of Defense.

- The sale of four Poseidon aircraft (P-8A) for the Royal Australian Air Force (and nine P-8As for the U.S. Navy, for a contract total of $1.49 billion).

General Electric, too, has secured multiple new orders since June 30th, including, among others:

- The sale of two high-efficiency 9HA.01 gas turbines and associated equipment for a combined-cycle power plant in Pakistan.

- The sale of advanced gas turbines for a new 3-gigawatt power plant in Iraq.

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[4] Veronique de Rugy and Diane Katz, Export Jobs Won't Disappear Absent Ex-Im Bank, Mercatus Center at George Mason University, May 21, 2015, http://mercatus.org/publication/export-jobs-won-t-disappear-absent-ex-im-bank

[5] Veronique de Rugy, Diane Katz, and Rizqi Rachmat, "Cumulative Top Ten Ex-Im Beneficiaries, 2007–2014," Mercatus Center at George Mason University, May 20, 2015, http://mercatus.org/sites/default/files/Exim-Cumulative-Backlog-Charts.pdf

- The sale of a high-efficiency 7HA.02 gas turbine and associated clutched steam turbine (as well as a long-term services agreement) for a new combined-cycle power plant in Anyang, Korea.

- The leasing of two Boeing 777-300ER aircraft for Japan's All Nippon Airways Co., Ltd.

- A framework agreement between GE Oil & Gas and Norway's Statoil Petroleum AS for subsea operations services, including offshore installation and intervention, equipment repair and maintenance, studies, upgrades and modifications.

- The purchase of "high-end" turbomachinery for the Trans-Anatolian Natural Gas Pipeline (a partnership between the State Oil Company of Azerbaijan, Turkey's state-owned Petroleum Pipeline Corporation, and British Petroleum.

The biggest Ex-Im beneficiaries also have billions of dollars of backorders that will keep workers busy for years to come. Boeing, for example, has reported a total of 5,656 unfilled orders; General Electric has posted a backlog of $261 billion; Caterpillar Inc.'s backlog is $16.5 million (in the first quarter of 2015); and Bechtel Corp. posted a "strong" backlog of $70.5 billion.

The foreign firms that receive most Ex-Im financing are likewise large corporations that primarily purchase exports from U.S. conglomerates—not from Main Street businesses.[6] All have ready access to a variety of financing to continue their purchases of American goods and services.

[6]Veronique de Rugy and Diane Katz, The Export-Import Bank's Top Foreign Buyers, Mercatus Center at George Mason University, April 2015, http://mercatus.org/sites/default/files/DeRugy-Ex-Im-Foreign-Buyers.pdf

Company	Ex-Im Financing (2007-2013)	Country	Sector
Pemex-Exploracion y Producion	$7,206,653,106	Mexico	Oil & Gas
Ryanair Ltd.	$4,142,677,182	Ireland	Aviation
Emirates Airline	$3,392,703,744	United Arab Emirates	Aviation
Refineria de Cartagena S.A.	$3,215,335,836	Columbia	Oil & Gas
Esso Highlands Limited-Png Lng Project	$3,000,000,000	Papua New Guinea	Oil & Gas
Cathay Pacific Airways Ltd.	$2,952,460,537	Hong Kong	Aviation
Australia Pacific Lng Csg Processing Pty Ltd.	$2,865,507,940	Australia	Gas & Electric
Turk Hava Yotari A.O. (Turkish Airlines)	$2,538,244,371	Turkey	Aviation
Reliance Industries Ltd.	$2,400,000,000	India	Oil & Gas
National Aviation Co. of India	$2,375,441,278	India	Aviation

Five of the top 10 buyers are state-controlled and rake in millions of dollars from their own governments in addition to Ex-Im Bank subsidies. These multiple-subsidy streams offset operating costs, and thus provide a significant competitive advantage over unsubsidized U.S. firms engaged in similar ventures.

Five of the top 10 are involved in the exploration, development, and production of oil or natural gas. (These foreign concerns are collecting subsidies from American taxpayers at the same time that the Obama administration is restricting domestic oil and gas operations.[4] Consequently, the federal government has doubly disadvantaged U.S. energy firms—through its excessive regulation and Ex-Im Bank subsidies granted to foreign competitors.)

The other five top buyers are airlines that collectively have received more than $15 billion in Ex-Im subsidies in the past seven years solely to purchase products from Boeing.[5] But as noted in Boeing's latest Aircraft Finance Market Outlook, there now exists "an unprecedented diversity of capital providers."

“An expanding investor base, a rational balance between secured and unsecured funding, innovative financing structures, and a growing private placement market are helping to propel the growth of capital markets in aircraft finance.”[7]

The Small Players

A tremendous amount of media attention has focused on the travails of small businesses that no longer will have access to Ex-Im subsidies. Bank proponents focus on small firms to deflect attention from the fact that the vast majority of Ex–Im beneficiaries are major corporations.

According to bank officials, about 20 percent of Ex-Im subsidies benefit small businesses. But that figure is inflated by the bank’s expansive definition of “small,” which includes firms with as many as 1,500 workers, as well as companies with revenues of up to $21.5 million annually.

In reality, Ex-Im assists only a tiny portion of all small businesses. Using data from the bank and the U.S. Census, economist Veronique de Rugy calculated that Ex-Im subsidies “supported” less than one-half of one percent of all small businesses.[8]

But that figure may be overstated. A recent investigation by the Reuters news agency found that potentially hundreds of the subsidy recipients categorized as “small businesses” by Ex-Im are actually very large enterprises or units of multinational conglomerates. Companies owned by billionaires such as Warren Buffet and Mexico’s Carlos Slim, as well by Japanese and European conglomerates, were listed as small businesses, Reuters reported. So, too, were Austria’s Swarovski jewelers, North Carolina’s Global Nuclear Fuels (owned by General Electric) and Japan’s Toshiba and Hitachi. The bank’s list of small businesses in Texas includes engineering giant Bechtel, which has 53,000 employees.

Even the financing designed for small businesses ends up benefitting the conglomerates. Between 2007 and 2014, large corporations—rather than small businesses—collected between 19.6 and 40.1 percent of the Ex-Im Bank’s working capital loans and guarantees. These included two transactions totaling $711.5 million for Boeing Co. and three transactions totaling $850 million for Ford Motor Co. (with a market cap of $58.5 billion).

The small businesses that have benefitted from Ex-Im subsidies in the past can tap the private financing sources used by the vast majority of their brethren. Given that small and medium-sized businesses account for 98 percent of all exporters, and exports have reached record levels in recent years, financing obviously is not a problem. Indeed, in an annual survey of small businesses by the National Federation of Independent Business

[7] Boeing Capital Corp., Current Aircraft Finance Market Outlook 2015, December 2014, http://www.boeing.com/resources/boeingdotcom/company/key_orgs/pdf/BCC-market-Report-WEB.pdf

[8] Veronique de Rugy, The Export-Import Bank Assists a Tiny Portion of All US Small Business Jobs and Firms, Mercatus Center at George Mason University, July 21, 2014, http://mercatus.org/publication/export-import-bank-assists-tiny-portion-all-us-small-business-jobs-and-firms

Research Foundation, respondents rated "Exporting My Products/Services" as the least problematic of 75 business problems.[9] (The cost of health care ranked as the most severe problem.)

Meanwhile, the number of small businesses that export (and the value of their exports) has grown significantly in recent years,[10] which belies the claim of Ex–Im proponents that small firms are unable to compete without Ex–Im financing (since the vast majority of these firms do not get such assistance). Between 1997 and 2007, for example, the value of exports per small and medium-size businesses increased by 80 percent, and the number of these exporting firms grew by 30 percent, according to the U.S. International Trade Commission. (Firms with fewer than 20 employees accounted for 95 percent of the growth.)[11]

Financing Options

Despite the fear-mongering about the outsourcing of American jobs, Congress and the public can rest assured that the consequences of charter expiration are inconsequential. Here's why:

First and foremost, as noted earlier, the vast majority of U.S. exports— 98 percent—do not receive assistance from the bank and thus have access to private financing. For those that no longer have access to Ex-Im subsidies, there is no shortage of private sources of investment. And the companies that benefit most from the subsidies— large and successful corporations such as Boeing, General Electric and Caterpillar—enjoy unparalleled access to private capital.

Second, finance costs are only one among a variety of factors that affect a purchaser's choice of supplier. Availability, reliability and stability all play significant parts in purchase decisions. There should be no question that U.S. firms are capable of competing successfully without corporate welfare.

Third, there is no such thing as a "level playing field" in trade. Every country possesses advantages that others lack. The ingenuity and drive of American enterprise can trump the export subsidies doled out by foreign governments. American companies would be further advantaged if Congress reduced the tax and regulatory barriers that inhibit business growth.

Demand for Ex–Im financing has actually declined in recent years, too. Authorizations dropped by 24 percent between FY 2012 and FY 2013, and decreased by 25 percent between FY 2013 and FY 2014.

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[9] Holly Wade, "Small Business Problems & Priorities," National Federation of Independent Business Research Foundation, August 2012, http://www.nfib.com/Portals/0/PDF/AllUsers/research/studies/small-business-problems-priorities-2012-nfib.pdf

[10] Economic Statistics Administration, "Data Snapshot: How Much Do Small- and Medium-sized Businesses Contribute to U.S. Exports?" January 22, 2015, http://www.esa.doc.gov/under-secretary-blog/data-snapshot-how-much-do-small-and-medium-sized-businesses-contribute-us

[11] U.S. International Trade Commission, "Small and Medium-Sized Enterprises: Overview of Participation in U.S. Exports," January 2010, http://www.usitc.gov/publications/332/pub4125.pdf

Boeing's own assessment of the export finance market for aviation is very positive. According to its 2015 outlook, the company "anticipates an unprecedented diversity of capital providers," and "historically low levels of export credit usage."[12]

The report further states: "While politics are creating some uncertainty around export credit, that should be offset by balanced funding from commercial banks and capital markets. We expect to welcome a number of new commercial bank and capital market participants over the coming year, which should drive continued diversity in these sources."

In the event that a small business cannot access private capital, it can seek to export through wholesalers or associate its business operations with larger firms or with global supply chains.

Small firms can also reduce export risk by requiring upfront payment--a very common strategy among small businesses. In a 2013 survey by the National Small Business Association, 69 percent of exporters said they demand payment in advance of shipping.[13] Only 12 percent utilize any type of "payment enhancement," such as credit insurance. Nor do most small businesses lack access to private capital, as Ex–Im proponents claim: 73 percent of small businesses reported that they access export financing from a bank or credit union.

What most imperils the availability of financing are the tax and regulatory barriers erected by the government. Dodd-Frank, in particular, has increased the costs of credit. The International Chamber of Commerce reports that 70 percent of respondents to its 2015 survey say report declined transactions due to regulatory burden; a total of 91 percent expect compliance requirements to increase over the next year, up from the 81 percent in 2014."[14]

No Need for Reauthorization

It is understandable, of course, that Ex-Im beneficiaries want to keep their subsidies, but the impact on the overall economy should not be overlooked. A review of the academic literature on the topic suggests that in most cases export subsidies reduce the total income of the country paying the subsidies (i.e., the GDP of the country issuing the subsidies is negatively affected). In all cases, export subsidies reduce worldwide income by increasing the wealth of those, and only those, who are subsidized—at the expense of other exporters and taxpayers.[15]

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[12] Boeing Capital Corp., Current Aircraft Finance Market Outlook 2015, December 2014, http://www.boeing.com/resources/boeingdotcom/company/key_orgs/pdf/BCC-market-Report-WEB.pdf

[13] National Small Business Association and Small Business Exporters Association, "2013 Small Business Exporting Survey," http://www.nsba.biz/wp-content/uploads/2013/06/Exporting-Survey-2013.pdf

[14] International Chamber of Commerce, Global Survey on Trade Finance, September 29, 2015, http://www.iccwbo.org/Products-and-Services/Trade-facilitation/ICC-Global-Survey-on-Trade-Finance/

[15] Salim Furth, "The Export Import Bank: What The Scholarship Says," (Backgrounder No. 2934, Heritage Foundation, Washington, DC, August 7, 2014), http://www.heritage.org/research/reports/2014/08/the-export-import-bank-what-the-scholarship-says

This was further documented by economist Dan Ikenson in a 2014 study in which he quantified the industrial "winners" and "victims" of Ex-Im subsidies. Not surprisingly, Ikenson found that Ex-Im policies benefit far fewer industries than they penalize: Out of 236 manufacturing industries studied, 189 are victims, incurring a combined annual net cost of almost $3 billion.

Ikenson's study did not account for the costs imposed on domestic manufacturers who compete with Ex-Im–subsidized domestic exporters, nor did it consider what alternative opportunities might have been otherwise viable in the absence of subsidies. If these indirect costs are factored in, the total true costs of Ex-Im subsidies would likely be greater.[16]

Even if Ex-Im subsidies were actually helpful and less harmful, government interference in business finance has become unsustainable. According to the "Bailout Barometer" developed by the Federal Reserve Bank of Richmond, a whopping 60 percent of all liabilities of the financial system are explicitly or implicitly protected from loss by the federal government—i.e., taxpayers.[17]

This federal "safety net" undermines the financial discipline that is so necessary for the free enterprise system to properly function. Absent government "protection," investors only take risks they are able to manage. But a bailout mechanism encourages excessive risk-taking because investors do not bear the cost of their actions. All of which increases the likelihood of financial crises and bailouts.

Conclusion

Despite overwhelming evidence to the contrary, some members of Congress believe that a few legislative tweaks will remedy all that is wrong with the Export-Import Bank (Ex-Im). But Ex-Im has failed to fully comply with previous reforms mandated by Congress.

Lawmakers would do well to consider the many drawbacks of the subsidies, including distortions in the distribution of labor and capital, higher consumer costs, and the disadvantages to domestic firms that do not receive the subsidies. Moreover, there has been a recent uptick in allegations of serious misconduct by Ex-Im Bank employees. The Office of Inspector General has identified deficiencies in internal controls that reduce the reliability of the bank to ferret out improper payments. There also are weaknesses in the bank's "Character, Reputational, Transactional Integrity" screening of applicants, as well as a pattern of insufficient due diligence by delegated lenders, specifically lenders with a history of defaulted transactions.

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[16] Daniel J. Ikenson, The Export-Import Bank and Its Victims: Which Industries and States Bear the Brunt?, Cato Institute Policy Analysis No. 756, September 10, 2014, http://www.cato.org/publications/policy-analysis/export-import-bank-its-victims-which-industries-states-bear-brunt

[17] Federal Reserve Bank of Richmond, Bailout Barometer: How Large is the Financial Safety Net?, May 13, 2015, https://www.richmondfed.org/safetynet/

In fact, pending legislation is largely a regurgitation of “reforms” previously mandated by Congress—without appreciable effect. The only meaningful way to remedy Ex-Im’s multibillion-dollar risk to taxpayers—and the rampant cronyism the export subsidies perpetrate—is to reject reauthorization of the charter.

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