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Improving Governmental Support for the Export Credit of Foreign Trade in the Eurasian Space*



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Abstract. The development of common approaches to the provision of governmental support to export credit within the Eurasian Economic Space streamlines the entry of national producers into foreign markets and the development of foreign trade. The paper aims to justify the need to harmonize the rules according to which the government provides support to foreign trade within the Eurasian Economic Union (EAEU). We analyze principles for determining the minimum rates on export credits (CIRR, Commercial Interest Reference Rates) in national currencies, describe a methodology for determining the value of CIRR and calculating the minimum premium for credit risks adopted by the OECD, and define basic conditions for the provision of related export financing in the OECD. The novelty of our research consists in the fact that we calculate CIRR for EAEU member states in their national currencies in accordance with the provisions of the OECD Arrangement on Export Credits. The calculation technique that we propose contributes to the establishment of harmonized conditions to support the export of industrial products within the EAEU. We use research methods such as analysis, synthesis, generalization, and comparison. We identify risk zones of the export credit system and measures to reduce the cost of funding for the EAEU member states that do not issue freely convertible (reserve) currencies. We substantiate the expediency of developing and approving CIRR calculation techniques within the EAEU. We point out the advantages of supplementing the state support of export crediting with the mechanism of linked export financing. We reveal the barriers to establishing a unified and standardized system of export support in the Eurasian Space. We substantiate the ways to streamline the mechanisms of export policy at the level of the EAEU. Practical significance of our research consists in the fact that we develop an algorithm for calculating the minimum allowable rates of export credits denominated in the national currencies of EAEU member states (Russian ruble, Belarusian ruble, Kazakhstani tenge, Armenian Dram, and Kyrgyzstani som) on the basis of agreements and practices of state financial support (subsidies) for OECD export credits to stimulate mutual foreign trade within the EAEU.

Key words: international competition, foreign trade, OECD, EAEU, export crediting, CIRR, credit risk, linked export financing.

Introduction. State support for the expansion of national producers to foreign markets is relevant in the context of international competition.

Formation and development of the system of state financial support for exports have been studied since the mid-1980s. According to some research, the provision of a state export subsidy increases export of a subsidy recipient and reduces export of its competitor [1]. Most researchers come to the conclusion that the practice of providing subsidies to national exporters contributes to country's welfare, especially when it comes to the economy of a developing state [1; 2; 3; 4; 5; 6; 7; 8]. State

regulation of export, including imposition of production and export taxes, has a greater effect than neutral state policy, especially if a national producer expects a rise in demand for its products abroad [9].

Nowadays people discuss the need to create an institutional infrastructure for export credit with state support [10; 11; 12; 13]. In particular, the developed system of state support for export credit has been established in all OECD countries, primarily in the United States and Germany. Export quota in the manufacturing sectors of German industry is very significant and often reaches 50–60%. Financing of

foreign traders is carried out through specialized and state-controlled structures – KfW IPEX Bank (export and project financing), as well as KfW Entwicklungsbank and DEG (developing countries), which are part of Kreditanstalt für Wiederaufbau-KfW [14].

China is also one of the three major world trading powers that have created a support system. In the country the Ministry of Commerce of the PRC is the main state body responsible for the development and implementation of foreign economic policy. The Export Support Department and the China Investment Promotion Agency are key organizations in the Chinese national system to promote export of products and investment in foreign assets [15, p. 50]. The China Development Bank is one of the leading financial institutions supporting export. It together with the Export–Import Bank of China has attracted at least 112 billion US dollars of foreign loans to Chinese companies doing business abroad since 2010.

A similar infrastructure to support export credit is currently being developed in the Russian Federation and the EEU countries. State-owned banks that position themselves as financial development institutions (for example, Vnesheconombank of Russia, Development Bank of Kazakhstan, Development Bank of the Republic of Belarus) are key creditors in the Eurasian space [16].

In terms of the stated above we believe that financial and credit incentives through export credit subsidies play an important role in addressing the issue of foreign trade development. In the context of international competition the positive effect of state regulation can go up in case of harmonization

of state financial support within the framework of regional economic associations, in particular the EEU.

In this regard this article is aimed at identifying the problems of state support for export credit of foreign trade and working out the proposals to ensure conditions for advancement of EEU producers to foreign markets.

Description of the research method and justification of its choice. As known, commercial interest reference rates (CIRR) are subject to agreement at the interstate level, and certain methods have been developed for this purpose. According to Article 19 of the OECD Arrangement on Officially Supported Export Credits (AOSEC), the parties to the Arrangement providing export credits with state support should use a CIRR as the lowest possible loan rate.

To achieve article purposes, we analyze the principles to determine a CIRR, describe the method to identify a CIRR value and the procedure to calculate a minimum premium for credit risks, as well as reveal the features of tied aid in order to determine the directions of improving state support for foreign trade in the EEU member states.

The principles for establishing a CIRR in national currencies are laid down in Article 19 of the OECD Arrangement on Officially Supported Export Credits:

- 1) CIRRs should represent final commercial lending interest rates in the domestic market of the currency concerned;
- 2) CIRRs should closely correspond to the rate for first class domestic borrowers;
- 3) CIRRs should be based on the funding cost of fixed interest rate finance;

4) CIRR should not distort domestic competitive conditions;

5) CIRR should closely correspond to a rate available to first class foreign borrowers.

The first principle presupposes two major sub-principles. The indication that the CIRR is a final rate implies that the establishment of a CIRR in national currencies should be based on “effective” interest rates, i.e. rates include all possible commissions and additional costs, rather than nominal values. In turn, the statement that the CIRR is a commercial rate implies that it should be based on market values of interest rates rather than concessional, subsidized loans provided to national borrowers by states in order to support them.

The second principle, in our opinion, is of paramount practical application in establishing a CIRR in national currencies. According to this principle, the rates set not only by states, but also by other local borrowers can be used as a basis for establishing CIRR values, provided that they are classified as first class, i.e. having the highest credit rating in national currencies.

The third principle reveals the economic nature of a CIRR. According to it, a CIRR reflects the cost of funding a financial institution that provides an export credit and does not include any margin or premium, such as a risk premium. The provision of export credit at a rate lower than the CIRR would mean granting of a deliberately unprofitable loan, which is contrary to the WTO principles.

In our view, the fourth principle seeks to encourage states to refrain from manipulating the domestic market by artificially undervaluing the funding of individual borrowers in order to establish lower CIRR values.

The fifth principle is similar to the second one, but extends it to first-class foreign borrowers. This extension provides even more opportunities to determine CIRR values in national currencies.

The method to establish a CIRR is stipulated in Article 20 of the OECD AOSIS. The method essence is as follows. In accordance with paragraph a) of Article 20, each participant wishing to establish a CIRR shall initially select one of the following two base rate systems for its national currency: one-tier or three-tier.

Under the one-tier scheme, five-year government bond yields for all maturities is the basis for calculating a CIRR for loans with a maturity of 2–10 years. Some export projects can have longer maturities.

In a three-level scheme, the following algorithm works:

1. Three-year government bond yields for a repayment term of two—up to and including five years.
2. Five-year government bond yields for over five and up to and including eight and a half years.
3. Seven-year government bond yields for over eight and a half years. Some export projects can have longer maturities.

In accordance with paragraph b) of Article 20 of the OECD Arrangement on Officially Supported Export Credits, after determining a base rate, a margin of 100 basis points should be added to it. The economic essence of this paragraph is based on the principle that currency-issuing countries should not support exports at a loss, and this allowance ensures compliance with this principle.

CIRR values are set monthly, fixed from the 15th of each month to the 14th of the following

month and are to be published on the OECD official website. Other participants should use the CIRR, set for establishing a particular national currency in accordance with the above method, in the case of providing financing in this currency. Each participant of the OECD Arrangement on Officially Supported Export Credits may change its base-rate system after giving six months' advance notice and with the counsel of the participants; however, this provision does not apply to the countries which are not OECD AOSEC members, that is, EEU member states.

In addition to the requirement on minimum interest rate on export credits with state support, the participants shall charge no less than the applicable minimum premium rate (MPR) for credit risk. This award is calculated in accordance with the provision of Article 23 of the OECD AOSEC by special authorized organizations. The calculation of the minimum premium for credit risks is based on the credit rating of an importing country and the credit quality of a foreign borrower. At the same time, the minimum premium for credit risks established in the OECD Arrangement on Officially Supported Export Credits does not depend on the credit country rating of an exporting country and the financial condition of an exporter.

When calculating a minimum risk premium, commercial risks are classified under the categories (SOV+, SOV / CC0, CC1, CC2, CC3, CC4, CC5), where countries with SOV+ rating have the most stable state according to the criteria of economic and financial stability, countries with CC5 rating – the least stable state, respectively. The commercial risk factor (buyer risk) is linked to a country exporter risk category. At the same time, the most favorable

conditions for supporting lending to producers will be achieved when exporting products to countries with high rates of economic and financial stability.

Government support for export credit can be also supplemented by a mechanism for linked export financing. The provisions of Chapter II of the OECD AOSEC establish requirements for financial parameters of export credits of commercial banks, which use certain measures of state support. At the same time, interstate export credits are provided on the basis of Chapter III of the OECD AOSEC. In accordance with Article 33 of the OECD Arrangement on Officially Supported Export Credits, tied aid policies should provide needed external resources to developing countries in a segment of financing that is not available to the commercial sector. Tied aid can be provided in the form of loans, grants or financial packages on concessional (non-commercial) terms. They are usually given as a combination of grant and loan on commercial terms.

The basic conditions for tied aid provision in the OECD are the following:

- 1) a foreign borrowing country lacks opportunities to attract financing for a project on commercial terms (Article 37 of the OECD AOSEC);

- (2) tied aid can be only provided to the countries determined by the OECD Secretariat on the basis of the World Bank classification (Article 36). To date, more than 90 states are referred as recipient countries [17]; among them there are traditional trade partners of the Russian Federation: EEU member states, Vietnam, Egypt, India, Indonesia, Iraq, Moldova, Mongolia, Pakistan, Tajikistan, Uzbekistan, etc.;

3) depending on the level of gross national income per capita of a recipient country, the OECD AOSSEC sets a minimum concessionality level for provision of tied aid (for least developed countries the concessionality level is 50%, for the rest –35%) (Article 38).

In case of grants the concessionality level is 100%. In case of loans the concessionality level is defined as the difference between a nominal value of a loan and a discounted value of borrower's future debt service payments. This difference is expressed as a percentage of the nominal value of a loan. The calculation of the concessionality level is based on the provisions of Article 40 of the OECD AOSSEC. The concessionality level of tied aid depends on a loan rate, a grace period, an availability period, a plan of repayment of principal amount and interest of a loan, a loan maturity, and a discount rate and does not depend on a loan volume.

Research results. The analysis of the above principles to establish CIRR values in national currencies shows that the calculation of corresponding CIRR levels is based on the yield on participants' state bonds placed on the domestic market of a country and expressed in national currencies. It is obvious that in case of national currencies of the EEU member states, reflecting the corresponding economic potential and market size of a currency, the rates calculated by the OECD AOSSEC method will be higher than in developed countries. As a result, EEU producers are in less competitive conditions due to the WTO rules that determine interests on export credits.

The analysis of the method to establish CIRR values reveals that the rates are set for national currencies of all countries participating

in the OECD Arrangement on Officially Supported Export Credits, for 15 currencies. Thus, for export credits with a repayment period of 8.5 years, a CIRR is set at 3.78% per annum for US dollars and 1.40% for euros. Of the 15 states that take part in establishing CIRR values in their currencies, nine have chosen a three-tier scheme for determining rates, and six – a one-tier scheme [18].

For the ruble and national currencies of Armenia, Belarus, Kazakhstan, Kyrgyzstan, a CIRR rate is not determined, since the EEU member states are not OECD members. At the same time, many OECD member countries are interested in establishing a CIRR in rubles at this stage, despite the sanctions. Such proposals arise due to the fact that a large number of import comes to Russia with financial support of foreign export credit agencies. Quite often Russian contractors require ruble-denominated loans. In particular, export credit agencies of the OECD countries are interested in establishing a CIRR in rubles to reduce the costs associated with foreign currency hedging when issuing export credits with state support to buyers of their products in Russia and the EEU member states, as well as to create a more predictable and favorable system of investment through Russian regional state organizations in joint projects on the territory of the Russian Federation.

In countries, such as the Kyrgyz Republic and the Republic of Armenia, various non-profit organizations, as well as information-analytical and training centers financed from abroad, had been operating prior to their accession to the EEU. At the same time, the spread of Russian government bond yields is very significant, and this fact is also

CIRR value in national currencies of the EEU member states with regard to the yield of government bonds, %

	Russia	Belarus	Kazakhstan	Armenia	Kyrgyzstan
Yield of government bonds					
3 years	8.02	8.7	12.68	14.24	16.27
5 years	10.11	10.4	16.47	17.08	18.41
7 years	11.58	12.5	19.2	19.45	-
CIRR value in national currency for export credit					
With maturity of up to 5 years	9.02	9.7	13.68	15.24	17.27
With maturity of 5–8.5 years	11.11	11.4	17.47	18.08	19.41
With a maturity of 8.5 years and over	12.58	13.5	20.2	20.45	-*
<p>* Taking into account that there are no debt securities of the Kyrgyz Republic or Kyrgyz state companies denominated in Kyrgyz som, it is not possible to establish a CIRR value for loans with a maturity of 8.5 years and over. Sources: calculated according to central banks and stock exchanges of the EEU member states: the Bank of the Russian Federation (http://www.cbr.ru/gcurve/GDB.asp; https://smart-lab.ru/q/ofz/), the National Bank of the Republic of Belarus (http://www.nbrb.by/statistics/MonetaryPolicyInstruments/RefinancingRate/), the National Bank of the Republic of Kazakhstan (http://kase.kz/ru/gsecs/; http://cbonds.ru/kazakhstan-bonds/), the Central Bank of Armenia (www.cba.am; http://cbonds.ru/armenia-bonds/), the National Bank of the Kyrgyz Republic (http://www.senti.kg/article/fondoviy_rinok_kirgizctana_itogi_2015_goda) and the information Agency Cbonds.ru (http://ru.cbonds.info/pages/Cbonds), specializing in the field of financial markets (Moscow Exchange, JSC “Belarusian Currency and Stock Exchange”, KASE, defined as a special trading platform of the Almaty regional financial center, the Armenian Stock Exchange, the Kyrgyz Stock Exchange).</p>					

typical for Kazakhstan. In this regard, a possible CIRR in rubles can reach very high values, which is unprofitable for the Russian Federation in terms of expanding the practice of providing export credits using state measures to assist foreign buyers of domestic products in rubles.

According to the OECD AOSSEC provisions, a participant wishing to establish a CIRR value in national currency should first choose a system for determining a basic rate for its national currency. We believe that in order to determine the possibility of establishing CIRR values in national currencies of the EEU countries, it is necessary to establish the presence in circulation of government bonds with a repayment period of 3, 5 and 7 years.

We summarized information on the state of the domestic debt market to calculate CIRR values. We analyzed the EEU government bonds that were denominated in national

currency (Russian rubles, Kazakhstan tenge, Belarusian rubles, Armenian dram, Kyrgyz som) and were in circulation as of March 2018, selected the securities most suitable for the purposes of determining CIRR values, and calculated appropriate rates by countries(*table*).

The corresponding levels of CIRR interest rates are calculated according to the WTO rules and the OECD method on the basis of 3, 5, and 7-year government bond yields, expressed in national currencies. The level of such yield increases by 100 basis points (conditional difference in the cost of funding banks compared to issuers of government bonds, which are sovereign borrowers) and we get a base CIRR value in appropriate currency.

According to the table, the cost of funding and financial conditions of export financing of the EEU member states, taking into account the WTO and OECD standards, is high; it reduces the competitiveness of producers on a

foreign market. To artificially reduce the cost of funding for countries that are not issuers of freely convertible (reserve) currencies is possible to the transition to export lending in currencies of the EEU countries. This effect can also be achieved in case of the use of national currencies in trade within the EEU. For Russia this fact is a top priority under the conditions of sanctions pressure from Western countries.

Funding of national institutions of the EEU countries at the expense of public sources that have assets in reserve currencies is the second possible direction to reduce the cost of funding in freely convertible currencies. In the Russian Federation, for example, the National Wealth Fund can be such a source of funding in foreign currency.

Participation of the EEU state structures in various support programs of international financial institutions, in particular the World Bank, IMF, EBRD, etc. is the third direction to cut costs.

The fourth direction is as such: creation of regional development banks aimed at concessional funding of participants' credit institutions for the purpose of subsequent support of export projects within the framework of integration associations.

The research in the current legislation of EEU member states and the rules to provide national institutions with state-supported target credits indicate a "material advantage" of understanding the rules of the WTO and the EEU Treaty in part of the terms of export credit in accordance with market conditions (for the loans in EEU currencies). Thus, the alternative method of establishing export credit conditions in the national currencies of the EEU countries with state support in

Armenia, Belarus, Kazakhstan, Kyrgyzstan and Russia does not work "de facto". At the same time, when organizing export credit in freely convertible currencies the EEU member states observe certain conditions of the OECD Arrangement on Officially Supported Export Credits, including CIRR rates.

The risk zone of the system of export credit state support in the EEU member states is a lack of legitimate indicators of the minimum level of rates in the provision of funds in Russian and Belarusian rubles, Armenian dram, Kazakhstan tenge. In Kyrgyzstan only pre-export financing is carried out in Kyrgyz som; it is not regulated by the OECD standards. In this connection it is reasonable to develop and adopt common approaches to establishing minimum rates of export credits in national currencies on the basis of the rules and regulations stipulated by the OECD Arrangement on Officially Supported Export Credits and the WTO Agreement on Subsidies and Countervailing Measures (ASCM).

Therefore, in order to comply with the rules of export subsidies within the EEU, it is necessary to work out and approve methods for determining minimum allowable rates of export credit in national currencies on the basis of the described approaches of the OECD AOSSEC and the WTO ASCM.

In addition to this rate, creditors charge a premium for credit risk for each specific credit institution, and the OECD method, similar to a CIRR, provides a certain algorithm for calculating minimum premium rates. This method includes factors, such as attribution of a borrowing country to a risk category, credit terms, amount of state insurance coverage of political and commercial risks of export credit,

quality of structuring of an export transaction and measures to reduce country and corporate risks [19; 20; 21; 22].

To calculate a minimum premium rate for credit risks, it is necessary to consider a country's credit rating by the OECD classification based on a seven-tier scale (1 – the lowest risk, 7 – the highest). The national institutions supporting export of the OECD AOSCE participants set limits on a maximum guarantee or insurance coverage of export credit, depending on the risk category of an importing country according to the OECD classification (the higher the category, the lower the maximum coverage). The decision to raise or maintain the same level of ranking of countries is adopted at regular meetings of the OECD subgroup for identification of country credit risks [23]. The powers of this subgroup include the distribution of countries (both OECD members and non-members) and individual international financial institutions by categories of OECD country credit risks to assess the premium (fee) amount charged for financing of export with state support. At the same time, in accordance with the OECD AOSCE provisions, OECD countries with high per capita income (as well as high-income EU countries) refer to Category 1 under this model. According to the OECD AOSCE participants, Category 7 includes countries with the highest level of credit risk.

Within the OECD classification credit ratings for more than 200 countries have been formed. The Russian Federation is included in Category 4 of the OECD classification, the Republic of Kazakhstan and the Republic of Armenia – Category 6, the Republic of Belarus and the Kyrgyz Republic – Category 7 [24].

We mentioned above the mechanism of tied aid as a way to supplement state support for export credit. The foreign buyer of industrial products (goods, works and services) from a donor country or its creditor can be a recipient of tied export aid. When the volume of tied aid is less than 2 million special drawing rights, which is about 3 million US dollars, there is only one condition to be met: a borrower should be included in the list of recipient countries of tied aid. Tied aid with a grace level of more than 80% can be provided under any conditions.

Throughout the development of the OECD AOSCE, the conditions for tied aid have only been tightened; thus, the minimum concessionality level was 25% in 1985. Since 1987 to the present the grant element has been at least 35%, i.e. it is prohibited to provide tied aid with a lower concessionality level.

Before provision of tied aid a creditor should notify other OECD AOSCE participants about such assistance through the Secretariat. In accordance with Article 41 of the OECD Arrangement on Officially Supported Export Credits, the conditions and procedure for the provision of tied aid should not be fixed for more than two years (due to changes in the economic situation of recipient countries). The main reason for this ban is the OECD countries' conviction that competition with commercial financing and export credits with state support begins at a low concessionary level.

Thus, in case of non-compliance with one of the conditions of Chapter III of the OECD AOSCE on tied aid (a concessionality level is lower than 35%, a recipient country is not included in the list of recipient countries of tied aid, a project can be implemented on

commercial terms), it is possible to provide export credits only if all the requirements of Chapter II of the OECD AOSCE for export credits with state support are met (amount of advance payment, a loan term, a loan repayment procedure, an interest rate, a risk premium, etc.).

Analysis and explanation of the results

The above reasons determine the feasibility of development and approval of the methods to calculate minimum interest rates of export credits with state support in currencies of the EEU member states.

These methods will allow to:

1) protect a domestic market of the EEU member states from unfair competition;

2) contribute to the synchronization of legislation harmonization processes in related areas: export support, financial markets, currency regulation;

3) bring interagency cooperation to a new level, both at the national and supranational level;

4) ensure healthy competition based on the method to calculate interest rates of export credits recognized by the world leading countries, thus helping the EEU member states to boost export in trade with the outside world;

5) take into account the use of methods in trade within the EEU, which allows not to tie the practice of granting export credits to the OECD AOSCE provisions;

(6) consider these methods in terms of a market-based measure to support exports of industrial products, which would be consistent with the provisions of the agreement on subsidies and countervailing measures.

The ongoing harmonization of national export support systems and the adoption of

methodological recommendations will have not only economic, political, but also reputational significance for the EEU, as well as create a favorable regulatory background for enhancing interaction of the EEU member states with the WTO, the OECD and other international organizations.

The role of state structures interaction in the formation of financial elements to support non-commodity exporters in the Eurasian Space is widen due to the activities of the Eurasian Economic Commission (EEC), founded in 2000. It coordinates cooperation in the identification and elimination of barriers, exemptions and restrictions on trade on the EEU domestic market, as well as the development of integration processes. Creation of the international Convention against Cartels and the Toolkit on Combating Restrictive Business Practices of Transnational Corporations and Transborder Violations of Rules on Competition. The Convention had already been approved under the existing effective “5+1” format of interaction between the heads of EEU antimonopoly authorities and the EEC Minister [25, p. 68]. Thus “the financial policy orientation degree on the promotion of economic growth in the region is an indicator of the strengthening of Eurasian integration” [26, p. 109–110].

Dispute about the results. The possibilities to transform the current practice of state financial export support in the EEU member states into a unified and standardized export support system are complicated by the following circumstances:

1) a different level of legal writing of the legislation in the EEU member states, including export legislation;

2) a low development level of the organizational and legal framework and practice of state export support in the Republic of Armenia and the Kyrgyz Republic;

3) states' different perception of OECD AOSEC provisions;

4) a lack of a mechanism to monitor and evaluate the effectiveness of EEC decisions under international treaties.

At the same time, when optimizing the mechanisms to harmonize legislation, converge export policy, and coordinate efforts of the EEC, state bodies and development institutions, at the level of the EEU it is possible to standardize:

- requirements for the minimum institutional structure of national export support systems;

- terminology (establishing uniformity in understanding of terms, such as “export credit”, “interest rate subsidies”, etc.;

- principles of state export support;

- a minimum set and uniform interpretation of government export support measures;

- a list of unfair practices in state export support and enforcement actions against states for their application;

- positioning of the EEU member states in relation to the OECD AOSEC;

- a CIRR analogue calculation method on the basis of EEU national currencies.

The proposed algorithm to calculate minimum allowable interest rates on export credits in national currencies of the EEU countries can be used in various spheres that do not belong to the segments of raw materials and agricultural products and trade and economic relations in order to assess financial and economic results of relevant export operations for their participants.

Recently non-committed financial loans from OECD countries to developing countries have become increasingly important. As a rule, tied export aid is provided on the basis of bilateral interstate agreements between donor and recipient countries, which corresponds to Russian practice and can be actively used within the EEU.

In our opinion, the proposals formulated in this article are aimed at the intensification of industrial and economic cooperation within the EEU, the formation of harmonized conditions of export credit with state support in order to boost integration processes in the Eurasian Economic Space.

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