OVERSEAS PRIVATE INVESTMENT CORPORATION

WASHINGTON, D.C. 20527-0001, U.S.A.

OFFICE OF THE PRESIDENT

December 19, 2002

Mr. Daniele Nouy
Secretary General-Basel Committee
Centralbahnplatz 2
CH-4002 Basel
Switzerland

Dear Mr. Nouy:

The Overseas Private Investment Corporation (OPIC) is an agency of the U.S. government that offers political risk insurance and financing to private U.S. investors in 150 emerging market economies. Our mission is to mobilize and facilitate private investment by complementing the resources of private financial institutions and insurers.

Having studied the Basel II proposals, we have become concerned that, despite good intentions, the proposed reforms could result in significant harm to developing countries, as they may ultimately discourage private investment in emerging markets. Although the implementation of the Basel II accord will remain the responsibility of national banking regulators, we believe that regulators are unlikely to consistently interpret and apply these regulations across markets.

More specifically, we believe that the Basel II proposal is based upon questionable assumptions that are briefly outlined below:

1. *Foreign investment before and after Basel II will be unaffected.* Basel II excludes credit and investment insured financing from capital relief that could result in additional expense for the banks and more conservative lending practices. Also, smaller banks that do not have sophisticated internal risk management systems will not automatically be able to apply the capital relief previously available for ECA insured financing under the current Basel I accords. Thus it is likely Basel II will discourage certain foreign investment.

2. *Project financing and commercial lending are equivalent and the same approach can be applied to each.* We believe that project financing has had a better track record than corporate lending, given the highly structured nature of project finance. Project financing should be considered separately from corporate

finance, otherwise the new Basel II accords could result in less project finance being available for important overseas infrastructure projects.

3. *Investment guarantees are the only risk mitigants that get relief from capital charges.* Under the new proposals there is capital relief for financing that is guaranteed by third parties, however the proposals do not address capital relief on financing that is insured by a third party. This fails to recognize the broad acceptance of insurance products by banking institutions and could result in excess demand for investment guarantees beyond the capacity and capability of the market. When political risk and export credit insurance products are referenced at all, there is no distinction between the public and private markets and yet the public market has historically been more reliable, predictable, and able to provide what are essentially unconditional guarantees.

4. *Effective communication, understanding and transparency are only necessary within the banking community.* One of OPIC's greatest concerns is that the proposals have not been well communicated, understood or debated outside of the banking community; yet the proposals will have important impact in other sectors. Conversations with officials from foreign countries, as well as the relevant U.S government agencies, have made it clear that there is inadequate knowledge of the proposal and its implications. It is indisputable, however, that the investment climate for project finance supporting economic development will be less available and less affordable. The mere absence of clarity could lead to cross-border investment paralysis.

5. *The rules have established parity between IRB-eligible and ineligible banks.* Banks ineligible for IRB treatment will be at a market disadvantage versus those who are, and such banks are unlikely to be able to compete. As a result, small banks may withdraw from cross-border lending entirely or they may relegate themselves to supporting only those investments in which the large banks have no interest. This could accelerate the trend toward consolidation that may be an unintended consequence of the Basel II accords.

The consequences of this proposal are enormous and will likely have a negative impact on both foreign direct investment and international lending. Rather than facilitating developed nations' goals of combating poverty, providing adequate supplies of water, electricity and housing, and fostering free market private enterprise, this proposal could constrict private lending. This could leave the public developmental agencies as the investor of only resort, rather than the investor of last resort. At a minimum, additional time and opportunity for interested parties across the globe to comment may prove beneficial to achieving the goals of Basel II.

Thank you for the opportunity to comment and we would be happy to elaborate on any of these points.

Best wishes,

Peter S Watson

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President and CEO

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