

# Консультативные услуги IFC банковскому сектору в Европе и Центральной Азии

# Domestic Local Currency Bonds of IFOs

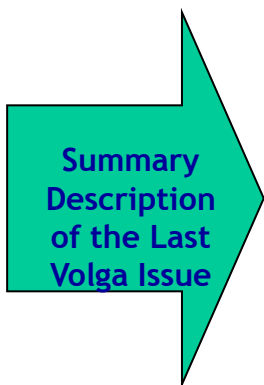
- The last financial crises revealed significant risks associated with foreign-currency denominated debt
- Local currency bonds, issued under local laws and regulations are important risk mitigants for EMs

<b>Advantages</b>	Contributes to capital markets' development; <b>liquid benchmark</b>
	Lengthens maturity of liabilities
	Reduces external vulnerabilities; <b>signal effect</b> to international investors
	Cost-effective means to finance IFOs LC-lending
<b>Drawbacks</b>	Onerous legal and regulatory requirements
	Triple-A rating not valued appropriately
	Exposure to payment and clearing systems

# • Domestic Bonds: IFO's *RUB Bonds*



- Strengthen funding base in the REGIONAL EME markets
- Establish transparent benchmarks for the EME debt markets
- Contribute to further development of that markets
- Allow the development of longer term financing for the real economy



- *Size:* RUB 13 billion issued in Nov. 2012
- *Coupon rate:* Linked to inflation-target index, as **opposed to** MosPrime, commodities, indices (RDX, DJUBS), issued by IFOs
- *Exchange:* MICEX
- *Custody:* National Depositary
- *Repo Eligibility:* A portion of the issue is eligible for swap into the floating-rate USD, available for re-investment in other EMEs

# •Eurobonds

- Means to fund local currency loan where a currency is fully convertible
- IBRD has issued Eurobonds in Korean won, Mexican and Chilean pesos, Brazilian real (fx-linked) and TRY.
- RUB was accepted as a full settlement currency in ICSDs (Euroclear and Clearstream) in 2007

Advantages	Can contribute to capital markets development
	Possible access to longer term funding
	Easy to document in MTN format
Drawbacks	Loan disbursement patterns may give rise to cash management needs, utilising credit lines and potentially increasing costs
	Sporadic international investor interest

# •Local Currency Eurobonds:

*Which Bond Markets had IFOs Accessed?*



- **China**
  - IFC jointly with ADB Renminbi Eurobond issue in 2005
- **Hungary**
  - EBRD Issued two HUF bonds in 2007. Launched first Global bond in 2001 and first domestic issue in 1994
- **Romania**
  - EBRD Issued inaugural domestic/international bond in 2009 followed by two Eurobonds
- **Russia**
  - IFC has been first supranational borrower in RUR (2005); recently (Nov 2012) issued Volga Bond, the Market largest domestic issue by an IFO

# •Capital Markets Development: *IFO's Role in Widening Access to Local Currency Resources*

IFOs were successful in enhancing local currency usage:

- Improving existing and/or helping to develop new money-market indices (KazPrime, KyivPrime, MosPrime) has stimulated activity in local currency;
- Acting as an anchor investor in local currency bonds, including securitisations;
- Establishing the bridge between international clearing and depository systems *Euroclear and Clearstream* (“ICSDs”) and Latvian and Romanian Central Depositories
- Getting currencies accepted by ICSDs (incl. Lat, HUForint and RUR;
- Directing donor funding for technical assistance to stock exchanges, and to the pension and insurance sectors;
- Supporting local investors.

# LC-Bonds: Issuance Environment

## Typical Pre-conditions

- (1) IFI receives the approval of member countries of the **currency and market** of issue;
- (2) Cross-currency swap markets exist (not for IFC, e.g. Ua)
- (3) Suitable projects with LC financing needs

## Minimum Requirements

- (1) WH-Tax exemptions
- (2) Domestic rating exemption
- (3) Broad investor access (ability of PFs and ICs to invest)
- (4) Risk weighting no more than 0% in line with Basel 2
- (5) Eligibility to count against statutory reserves / lombard list

# LC-Bonds in Ukraine: the Last Fortress

- MinFin tries to shield the domestic bond market from crowding out;
- Limited access to UAH-borrowing, as LC lending capped at below the market 10% rate - CabMin Decree, 2011;
- Market of up to USD 400 Mio equivalent annually (30 % of the funded local portfolio, 1:3 between IFC and EBRD);



## IFO's LC-Bonds Bill in Ukraine

- Bill on the LC-bonds submitted to VRU for 2<sup>ND</sup> reading;
- IFO bonds added as the 4<sup>th</sup> type of bonds;
- IFOs, Ukraine is not member to are captured opening doors for EIB and EADB;
- Purpose of the issue **not regulated**

# • Barriers to Local Currency Lending

- Exchange rate policy
  - irrevocable surrender of independent national monetary and exchange rate policy
  - adoption of currency board (Bulgaria, Bosnia and Herzegovina, Montenegro and Lithuania)
  - focus by central bank on exchange rate targeting, rather than monetary policy
  - political rhetoric and/or commitment (incl. ERM II) to replace domestic currency
  - macroeconomic instability and the lack of a transparent and credible policy framework
- Poorly regulated and/or capitalised banking system
  - lack of a lender of last resort (with guaranteed access to central bank repo facility)
  - term deposits that can be withdrawn with little (or no) notice
- Lack of credible market indices and liquid money-markets
- High domestic interest rates
- Inadequate market infrastructure
  - conflicting or unclear legal and regulatory environment, bureaucratic processes
  - imposition of new taxes, currency restrictions and other controls
  - poor payment and settlement systems
  - high domestic costs including listing fees and taxes
  - lack of institutional investor base and credit culture

# ● Credible Money-Market Indices

## *Key to Successful Local Currency Lending*

- IFOs worked with local banks and authorities in Kazakhstan, Romania, Russia and Ukraine to help to create local money market indices and improve their transparency and credibility.
- The development of a credible money-market index allows:
  - greater transparency and consistency in the pricing of all index-linked loans.
  - the pricing of derivatives (including futures and interest rate swaps).
  - the interbank money-market to develop greater liquidity, increasing efficiency, and lengthening the maturity of interbank activity.

# Capital Markets Development:

## *Developing the Local Investor Bases*

IFOs focused on the development of a local investor base through:

- Investing equity in local banks, pension funds and insurance companies;
- Improving the regulatory environment for investors, including through pension reform;
- Channelling donor funding for technical assistance to the banking, pension and insurance sector;
- Providing guidance towards standardising mortgage loans to facilitate the development of secondary mortgage markets;
- Facilitating the restructuring of bank balance sheets through co-investing in facilities to purchase non-performing loans;
- Supporting local brokerage houses' market-making activities in mid-tier corporate bonds.

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