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Optimal Sources of Financing

by

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Outline

I. Introduction

II. Challenges

a. Complexity of financial management

b. Need to further develop local bond market

III. ADB Support

a. Capacity building in financial management

b. Support of development of bonds market

IV. Conclusion



I. Introduction

- Key precipitating factors of Asian financial crisis included:
 - High level of short term, external debt;
 - High current account deficit; and
 - Vulnerability to liquidity crisis



Introduction

- To address some of these issues countries have been focusing on the need to:
 - Build up foreign exchange reserves and manage them well;
 - Set up and/or expand public debt management functions; and
 - Develop local currency bond markets
- Even if ADB noted considerable progress in these areas.





II. Challenges

- A. Complexity of task of debt managers or foreign exchange reserves manager
 - i. Why is it complex?
 - ii. Need to develop capacity of debt and foreign exchange managers.



The task is complex because...

- Debt managers have to ensure financing needs are met at lowest cost over medium to long-term, but subject to prudent level of risk
- They need to be aware of various risks (macro economy, liquidity, market, operational, and other risks)



The task is complex because...

- Debt managers have to trade-off cost vs. risk such as:
 - Domestic vs. external debt : External debt cheaper but liquidity risk, FX risk
 - Short term vs. long term: Short term cheaper but rollover risk
 - Fixed rate vs. floating rate: Floating rate cheaper but interest rate risk
 - Concessional vs. non-concessional debt: Concessional debt cheaper but risk of excessive non-concessional debt
 - Financing of contingent liabilities: Cheaper to finance less but can negatively impact perception of riskiness



The task is complex because...

- Reserve managers have to trade-off safety, liquidity and return
- In recent years, however, many Asian countries have accumulated large amounts of reserves that could be excessive in some cases



Need for Capacity Building

- Consequently, need to develop the capacity of:
 - Public debt managers
 - Reserve portfolio managers
- Also, need for capacity building in asset liability and risk management
 - Critical to financial institutions and, therefore, for financial stability
 - Underlies both debt management and reserve management



II. Challenges

- B. Need to further develop local bond markets
 - i. Local bond market has developed & is more open with increased foreign holdings

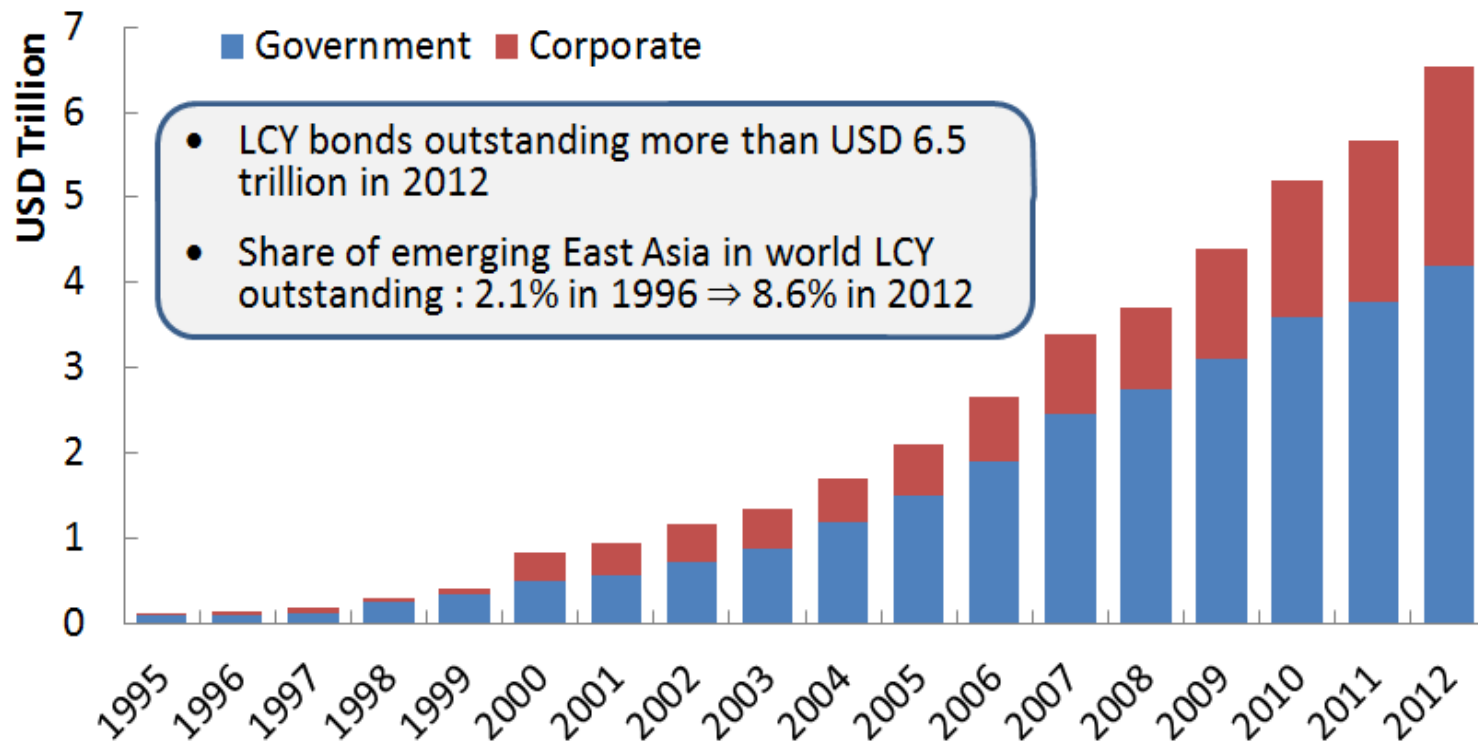
But

- i. There is a need for further develop the local bond market; and
- ii. Challenges remain as:
 - Asian financial system remain bank-dominated; and
 - Need to enhance the role of regional of regional resources.



Local currency bond markets have grown rapidly...

Growth of developing Asian local currency bond markets, 1995–2012



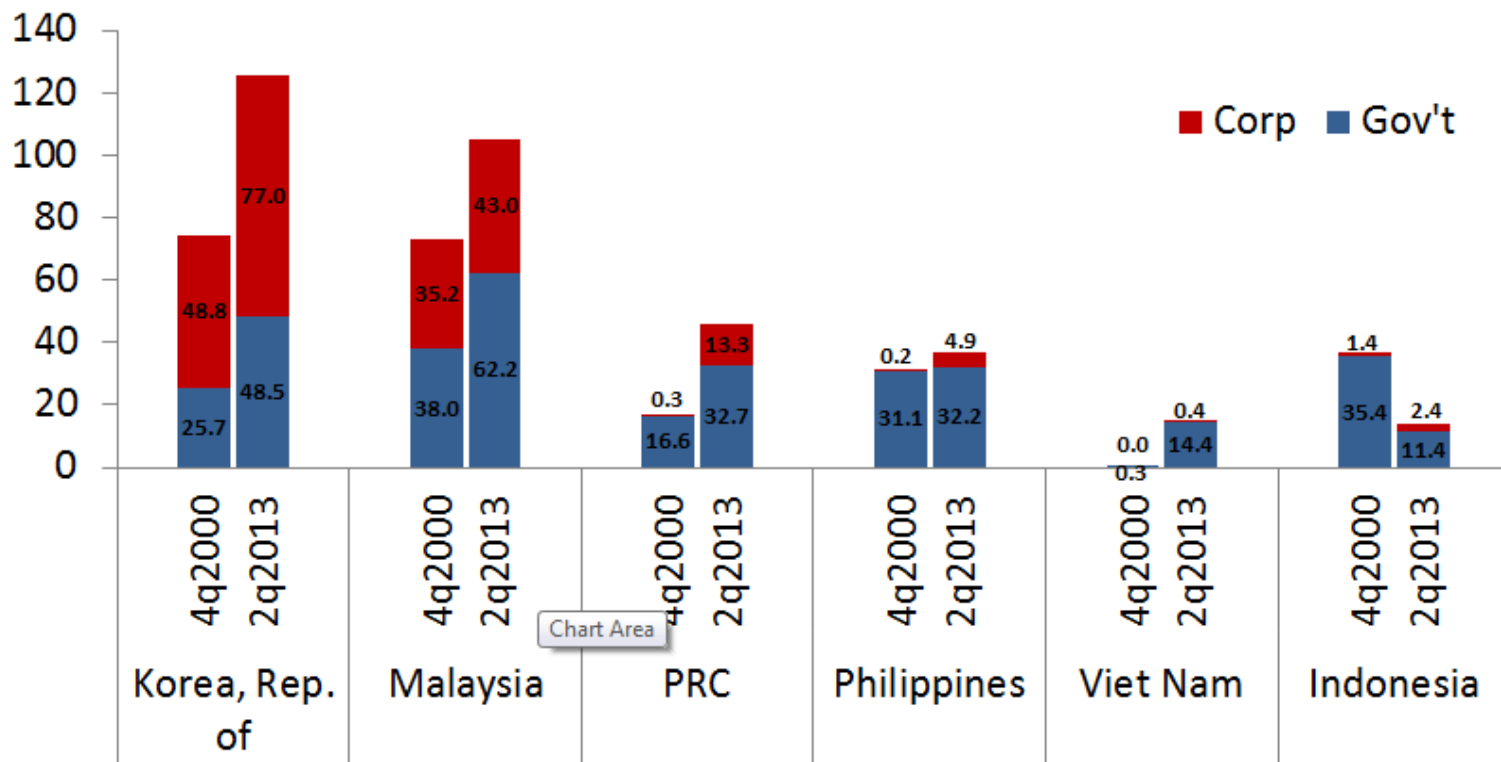
Source: [AsianBondsOnline\(ABO\)](#), ADB





...in many economies in both government and corporate bonds

Size of LCY bond outstanding, % of GDP

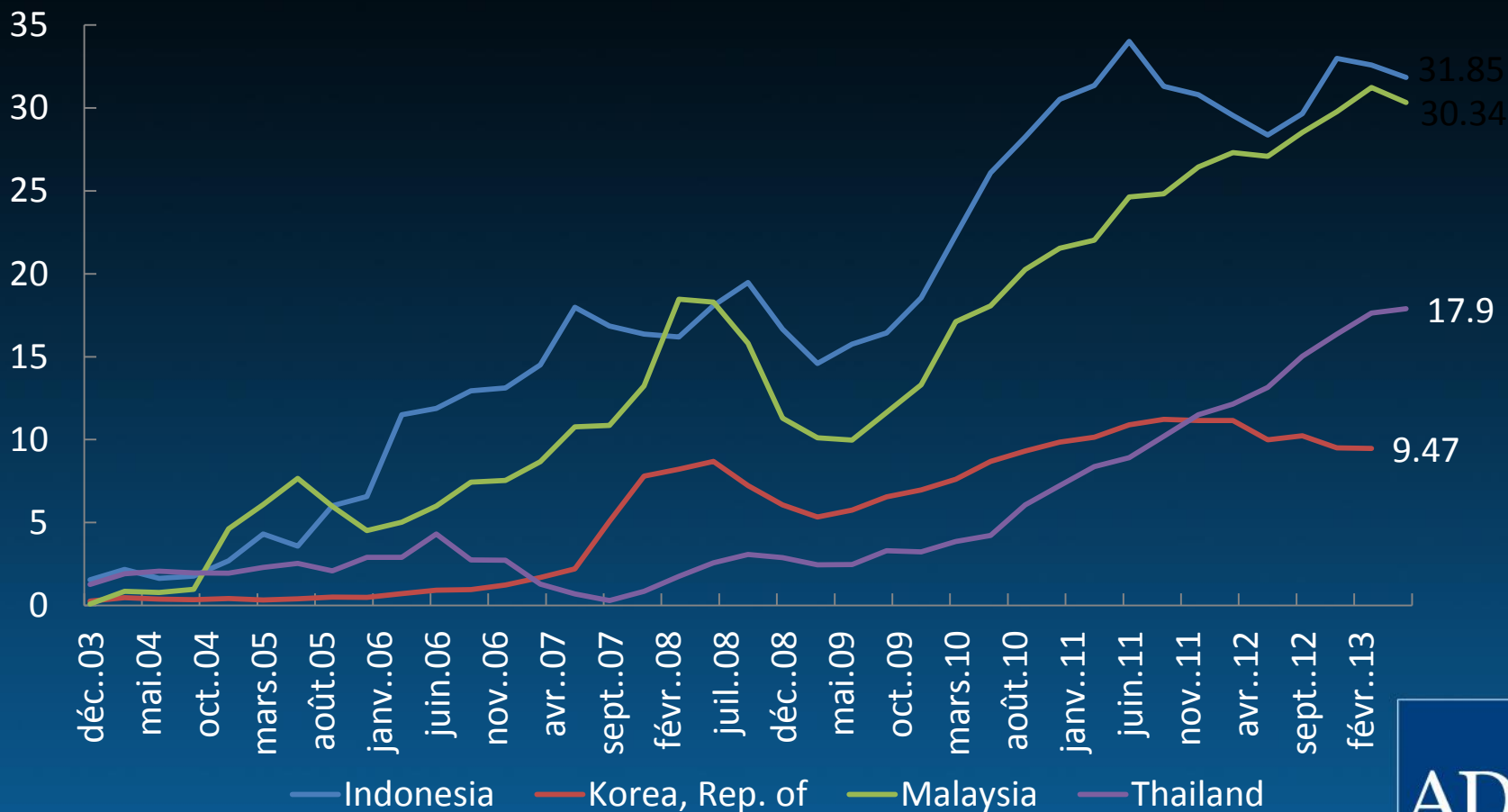


Source: [AsiaBondsOnline \(ABO\)](http://AsiaBondsOnline.com), ADB



The market has become more open with increased foreign holdings

Foreign holdings of local currency government bonds, % of total



Source: AsianBondsOnline(ABO), ADB



But challenges remain: Asian financial systems continue to be bank-dominated.

Size and composition of financial systems (% of GDP)

	Financial sector assets				Total bonds outstanding	
	Deposit-taking financial institutions ¹		Nonbank financial institutions ²			
	1997	2010	1997	2010	1997	2010
China, People's Rep. of	145	184	1	16	9	52
Hong Kong, China	615	708	76	459	23	29
India	44	90	2	29	18	46
Indonesia	84	36	5	8	2	13
Korea, Rep. of	132	151	23	73	29	110
Malaysia	186	214	28	109	54	101
Philippines	258	147	55	36	20	34
Singapore	762	582	81	79	24	58
Taipei, China	233	294	24	97	7	71
Thailand	156	155	6	37	22	57
Average ³	262	256	30	94	21	57

¹ Data for 1997 refer to 1999 for Rep. of Korea and 2000 for Taipei. Data for 2010 refer to 2009 for PRC.

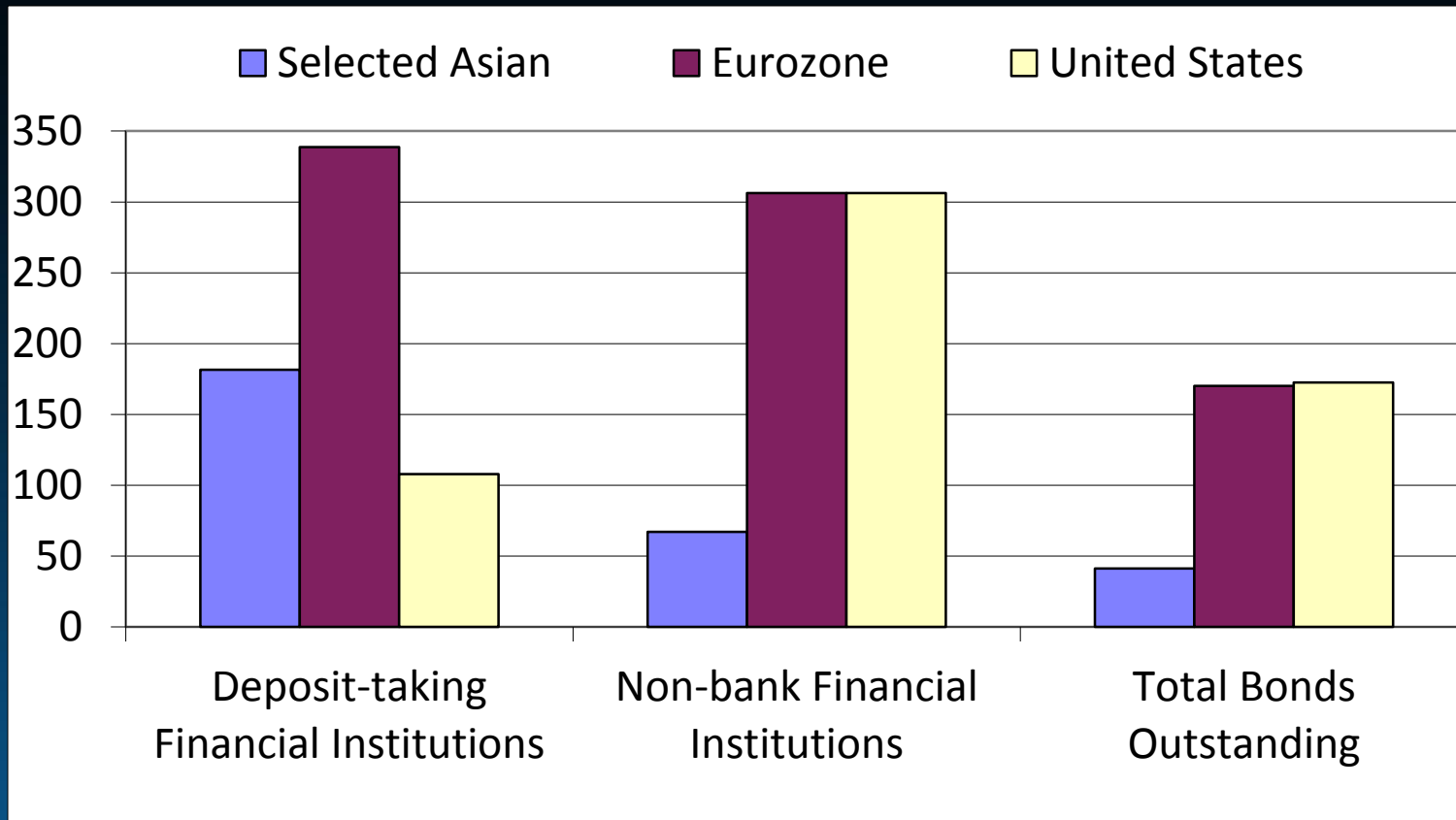
² Data for 1997 refer to 1999 for India and 2000 for Taipei. Data for 2010 refer to 2009 for PRC and Hong Kong and 2008 for India.

³ Simple average of ratios.

Sources: ADB calculations based on data from national sources, AsianBondsOnline, Bloomberg, IMF (World Economic Outlook Database).

Banking sector relatively small; bond markets even smaller compared to advanced countries

Structure of finance sector (% of GDP, 2009)

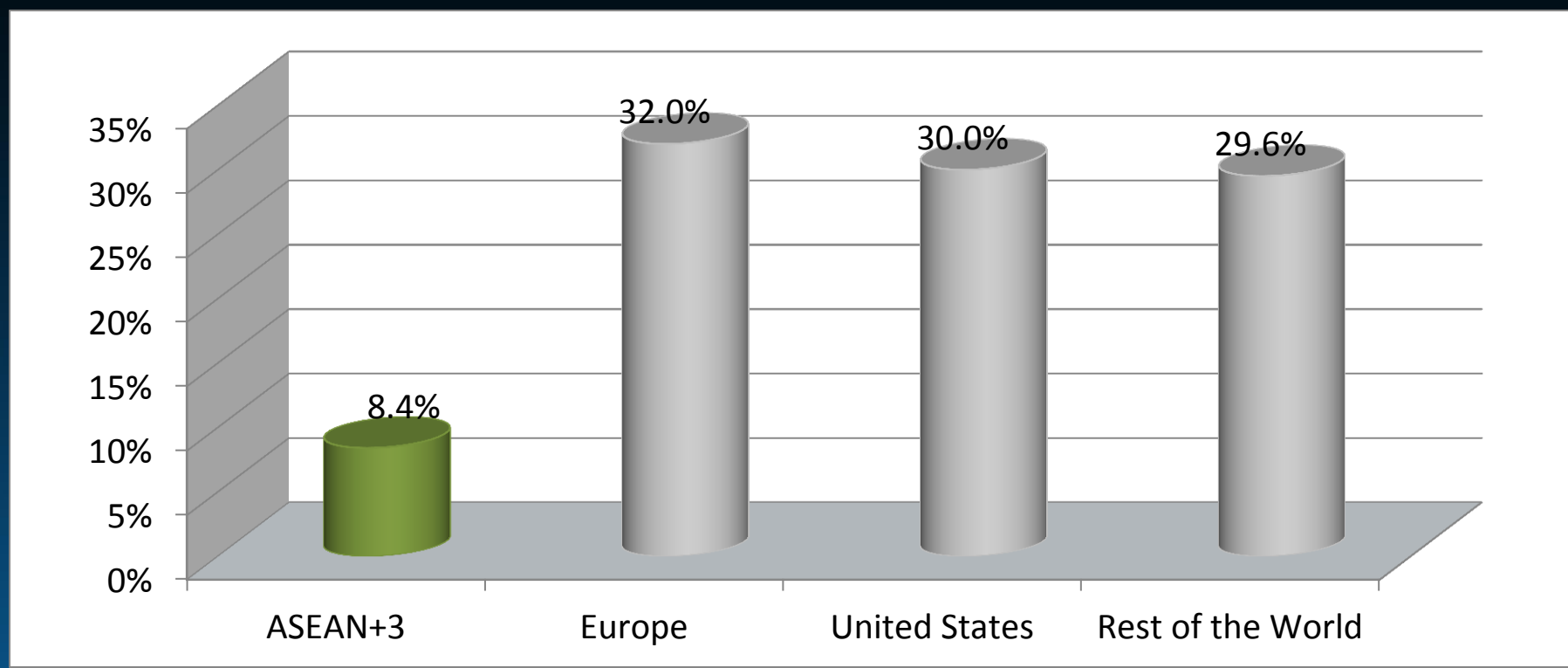


The selected Asian region includes Bangladesh, the People's Republic of China (PRC), India, Indonesia, Kazakhstan, Lao PDR, Malaysia, Nepal, Pakistan, Papua New Guinea, Pakistan, Philippines, Solomon Islands, Sri Lanka, Thailand, and Tonga.
Source: Financial Sector Operational Plan, ADB, 2010



There is a need to enhance the role of regional channeling of regional resources.

Developing Asia's Debt Securities Portfolio Outflows by region (% , 2011)



Source: The International Monetary Fund Coordinated Portfolio Investment Survey;
Note: This refers to the debt securities investments of ASEAN+3 within and outside of the ASEAN+3 region





III. ADB Support

A. Capacity Building





Capacity Building

- ADB also conducts capacity building activities including the following forums, typically held annually on:
 1. Public Debt Management;
 2. Investment Management of Foreign Exchange Reserves; and
 3. Asset Liability and Risk Management.
- In addition, ADB also conducts workshops for individual countries on its financial offerings and, in general, offers customized workshops to meet the client's needs





Capacity Building

- ADB conducts the following annual forums on:
 1. Public Debt Management : For debt management offices
 - Last one held in Jakarta, Indonesia in March 2013, co-hosted with Directorate General of Debt Management, Indonesia
 2. Investment Management of Foreign Exchange Reserves : For central banks
 - Last one held in Seoul, Korea in September 2013, co-hosted with Bank of Korea
 3. Asset Liability and Risk Management: For financial institutions (public and private sector)
 - Next one to be held in Singapore in November 2013
 - ADB also conducts workshops for individual countries on its financial offerings



Capacity Building- Lessons Learned

Through these forums, ADB has learned to:

- Use its financial and treasury expertise and market knowledge to design and organize delivery of the content
- Stress peer learning by organizing opportunities for countries to learn from one another
 - Variation of capacity within member countries
 - Leverage most relevant peer expertise
- Member countries have demonstrated strong support for the forums



II. ADB Support

- B. Support of development of bonds market through:
 - i. Assistance to member countries
 - ii. Local currency bond market development in support
 - iii. Local currency operations
 - iv. Asian Bond Market Initiative



ADB Assistance to Member Countries

- Development of local currency capital markets
 - Asian Bond markets Initiative
 - ADB financing in local currencies



Local Currency Bond Market Development Support

ADB's Role

- ADB has a long history of issuing local currency bonds. Examples of assistance
- ADB has also set up the Asian Currency Note Programme (ACNP)





Local Currency Operations

- ADB currently has local currency financing operations in PRC, India, Philippines, Thailand, Malaysia, Indonesia, Kazakhstan
- In addition, ADB raises local currency through use of swaps
 - Helps promote development of local derivative markets





Asian Bond Market Initiative

- ADB supports the ABMI which was launched by ASEAN+ 3
 - To build efficient and liquid bond markets
 - To mitigate currency and maturity mismatches
- Activities within this initiative include:
 1. Asian Bond Online Website
 2. ASEAN+3 Bond Market Forum
 3. Credit Guarantee & Investment Facility



Conclusion

- Country in Asia are more prepared and significant progress has been made since the financial crisis.
- ADB continue to support market development and capacity building with a regional approach.
- We aim with other IFI to carry on our effort in partnership with developing member countries.



THANK YOU

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