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FINANCIAL MARKET DEVELOPMENT ACTIVITIES OF DONORS AND THE UNITED STATES GOVERNMENT

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AND THE UNITED STATES GOVERNMENT

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SECTION I

INTRODUCTION

A. PURPOSE OF THE REPORT

The purpose of this report is to provide an overview of financial market development programs and policies of various economic development and regulatory institutions. Knowledge of these activities will be useful to A.I.D. as it defines its own financial market programming and seeks out areas of cooperation and collaboration with others.

B. SCOPE OF ORGANIZATIONS INCLUDED

This report does not intend to be all-inclusive, but attempts to cover the organizations that have the most extensive activities and those that possess the expertise and skills that are needed to implement financial market programs. These organizations fall into three broad categories: multilateral and regional development organizations, agencies of the United States Government, and international regulatory and research bodies. Other donor countries have programs of their own, but they are not addressed in this report.

Included in this report are the financial market development activities of the World Bank Group (IBRD, IDA, IFC and MIGA,) which are extensive, the IMF, and certain research and program activities of the United Nations. The activities of the United States Government are also covered, including those of The Overseas Private Investment Corporation, The Export Import Bank, The Securities and Exchange Commission, The Department of the Treasury, and The Federal Reserve System.

Two international regulatory bodies are discussed and the International Organization of Securities Commissions (IOSCO), the Basle Committee on Banking Supervision (Basle Group).

C. TYPES OF PROGRAMS REVIEWED

1. Macroeconomic Reform

Macroeconomic reform programs that seek to liberalize interest and exchange rates and those that address debt reduction are mentioned in this report because they are considered to be necessary prerequisites to successful realization of financial market development. Included in this category is a description of the World Bank's structural adjustment lending programs and its accompanying loan conditionality, and various organizations' debt reduction schemes, such as those of the World Bank and the U.S. Treasury.

2. Financial Sector Reform

Extensive structural reforms directed towards the financial sector have been implemented over the last four years or so as a result of banking system collapse. Most of the rescue measures have consisted of World Bank and IMF loans to the financial sector that have been used to recapitalize failing institutions and for technical assistance. An overview of the World Bank's activities in this area is discussed in Section III.

The other important and growing area of Financial Sector Reform addresses the need for prudential regulation, adequate supervision and legal reform. Much of the work in this area consists of technical assistance, advisory work, and training programs. The activities of the IMF, the Federal Reserve System, the World Bank, the IFC, and the SEC are described in Section III.

3. Increasing Domestic Savings and Investment

The core of financial market development consists of strengthening domestic financial markets. Programs in this category consist of the following:

- Financing domestic financial institutions;
- Creating new markets and instruments;
- Creating contractual savings institutions [1];
- Developing and funding on-lending programs;
- Working with the informal sector;
- Promoting and funding venture capital companies.

The IFC, The World Bank, the Asian Development Bank, the United Nations, and to a limited extent, OPIC and the SEC, are involved in this program area. Their activities are described in Section III.

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[1] Contractual savings institutions include pensions funds, national provident funds, life insurance companies and similar institutions that collect long-term savings on a contractual basis.

4. Increasing International Capital Flows

Many of the programs that increase the flow of international capital to developing countries have been designed as a result of the Third World debt crisis, the retrenchment of the commercial banking sector and capital flight. These programs are designed to identify new sources of capital and to increase net capital transfers. Certain programs of the IFC, the World Bank, and the SEC have this objective. A different sub-set included in this category have other primary objectives, such as trade, or foreign direct investment, or the globalization of financial markets; only indirectly do they provide financial market benefits for the developing world. Included in this group are The Export-Import Bank and OPIC, certain policy positions of the Bush Administration, such as GATT, and some of the international objectives of the Securities and Exchange Commission.

D. ORGANIZATION OF THIS REPORT

Section II of the report discusses the United States policy framework as it relates to financial markets, primarily with regard to debt reduction (Brady Plan) and trade (GATT). Section III describes the various program activities. The section is organized by institution. (Annex 1 sets forth a matrix of organizations by program type and objective.) Section III provides a discussion of the relationship and relevance of other entities' activities to A.I.D. and to A.I.D. programming. Suggestions on a niche for A.I.D. are offered.

SECTION II

UNITED STATES GOVERNMENT POLICIES

A. THE BRADY PLAN

One of the most pressing issues facing the international financial community has been the international debt problem. At year end 1987 an estimated $886 billion of external public debt was outstanding and owed to private and official creditors from lower and middle income countries. The U.S. Treasury estimated that approximately $275 billion of the total was owed to commercial banks by 15 highly indebted countries. [2] The table below shows the breakdown of external debt by region.

EXTERNAL DEBT OUTSTANDING AS OF 1987
(In millions of U.S. Dollars)

Latin America	$338,331
Sub-Saharan Africa	$103,874
East Asia	$147,605
South Asia	$ 68,696
Europe, Middle East & North Africa	$227,861
Total	$886,366
17 Highly Indebted Countries	$402,171

Source: World Bank. World Development Report 1989.

Since 1985 the United States Government has been committed to a debt reduction strategy that is based upon four fundamental principles:

- Economic growth is essential to the resolution of debt problems;
- Debtor nations will not achieve sufficient levels of growth without reform;
- Debtor nations have a continuing need for external resources;
- Solutions must be undertaken on a case-by-case basis.

Underlying this strategy is a commitment towards resolving the debt crisis through the support of market-driven voluntary debt reduction techniques between debtor countries and their creditors. Other strategies, that were rejected by both the Reagan and Bush Administrations, proposed that the debt crisis be resolved through U.S. government intervention and wholesale purchase of debts. These strategies were rejected because they would transfer debt repayment

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[2] Includes Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Ivory Coast, Mexico, Morocco, Nigeria, Peru, Philippines, Uruguay, Venezuela, and Yugoslavia.

risks to the public sector and because such actions would disrupt the secondary market for external debts that has been developing.

Debt reduction techniques include debt/equity swaps, other debt conversions, exit bonds, cash buybacks on the secondary market and privately negotiated debt restructuring. Between 1986 and 1988 approximately $24 billion of debts were reduced through market-driven voluntary debt reduction techniques. Nearly half of this amount was from debt/equity swaps. Approximately $7 billion (mostly Mexico) was from private debt restructuring and over $6 billion in other types of swaps.

The existence of a secondary market for Third World debt facilitates debt reduction transactions, although it has been estimated that only 25% of the secondary market transactions actually cause a reduction in debt outstanding. Estimates of the size of the secondary market ranged from $15 to $40 billion in 1988. Prices on such debt can be volatile, and, due to the thinness of the market, the spread between the bid and offer price can be significant. Comparable weighted average prices for the 15 highly indebted countries ranged from a low of 36 cents per one U.S. dollar face value to a high of 68 cents per one U.S. dollar face value.

Demand for debt in the secondary market arises from debt-for-debt swaps, cash purchases and sales, and the purchase of debt for conversions into other financial instruments, such as equity.

- Debt-for-debt swaps usually involve banks exchanging debt from one country for debts of another country. These transactions may account for as much as 75% of secondary market activity. Debt swap transactions may be undertaken by banks for portfolio diversification or strategic business reasons. Debt-for-debt swaps do not provide debt reduction for debtor countries, but they add liquidity to the secondary market.

- Cash sales by banks are used to reduce or exit from Third World debt exposure. Sales can be made to secondary market dealers, to corporations for direct investment through debt/equity swaps, or to charitable or academic institutions for environment, education or development swaps. These transactions will produce debt reduction benefits for the debtor countries only if the debtor country will redeem the debt in local currency and allow the proceeds to be used to acquire equity, other financial instruments, or to be budgeted for other developmental purposes.

- Debtor countries can purchase their own debt on the secondary market as well. These cash buybacks can be used by a debtor country to directly reduce its outstanding debts.

At the end of 1988, despite the emergence of some market driven debt reduction programs, serious economic problems remained - capital flight, low growth, stagnating levels of investment and savings, and commercial bank delays - that were perceived as barriers to meaningful levels of debt reduction. In addition the exposure of the multilateral institutions to the debt problems was increasing sharply.

In March 1989 the United States Government issued a revised strategy to cope with the debt problem. At a Brookings Institution and Bretton Woods Committee Conference on Third World Debt the new strategy, dubbed the "The Brady Plan", was announced. Elements of the policy were set forth as follows:

- Debtor nations must focus on policies that encourage new investment flows, strengthen domestic savings, and promote the return of flight capital. The World Bank and the IMF should incorporate conditions in their loans that support these policies.

- Commercial banks need to take a broader and more realistic approach to debt service and debt reduction. Individual banks need to determine their own interests and negotiate debt reductions if they wish to do so. Banks that wish to provide new money should be encouraged to do so. Debtor nations would be expected to maintain debt/equity swap programs and permit nationals of their countries to participate in them.

- The multilateral financial institutions should continue to play a central role. They should be relied upon to promote sound economic policies and to set-aside funding for debt or debt service reduction purposes. The money would be used to support collateralized debt for bond exchanges involving a significant discount on outstanding debt, or to replenish reserves following a cash buyback. Some money could be used for interest relief as well.

- Creditor governments should continue to reschedule or restructure their own exposures through the Paris Club [3], and to maintain export credit cover for countries with sound reform programs. Additional financing should be considered. Creditor governments should also consider how to reduce regulatory accounting, or tax impediments to debt reduction.

- Sound trade policies and open markets within industrial countries are essential. Debtor nations cannot be expected to increase exports without access to industrial country markets.

The Brady Plan has been met with skepticism and resistance from some borrowers, creditors and observers. Disappointment has run highest for Latin American borrowers (those same countries that were initially targeted for assistance). Some skeptics say the money available to address the problem - about $30 billion - will do little to dent Latin America's $300 billion plus of debt outstanding and $24 billion of interest arrearage. Furthermore, the lack of any headway for Argentina and Brazil is another problem.

It took eleven months for the first agreement to be concluded for Mexico. But by October 1990 five more countries had followed suit: Venezuela, Costa Rica, the Philippines, Morocco and Uruguay. In addition in 1990 the United States Government forgave $7 billion owed by Egypt and very recently has announced a debt-forgiveness plan for Poland. (The World Bank's participation

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[3] Paris Club is the group of c ial creditors that convenes to collectively reschedule Third World debt.

in debt reduction is described in Section III.)

The Mexican agreement concluded covered approximately half of the country's debt and provided debt reduction to the Mexican government from commercial banks based upon the following options and terms:

1. Debt Exchange. (a) For medium-term debt at a price of 35 cents, fully collateralized, registered debt reduction bonds with a single payment of principal in 30 years at a rate of LIBOR plus 13/16 were offered, or (b) For medium-term debt at full value, debt reduction bonds at an fixed interest rate of 6.25%. (Commercial banks would also have the option after 1997 to recover some forgone interest income if Mexican oil prices increase), or,

2. New financing. New money over a four year period equal to 25 percent of exposure not exchanged. This could be in the form of new Mexican bonds, on-lending to public sector borrowers, or medium-term credits.

3. World Bank and IMF support. Interest support for one to two years for the debt reduction bonds was provided by the World Bank, the IMF, the Mexican government, and indirectly by the Japanese Government. Credit enhancement support was provided and included purchase of zero-coupon bonds to be used as collateral for the exchanged debt.

4. Debt/equity swaps. Banks participating in the agreement will be allowed to exchange up to $3.5 billion in debt for equity between 1990 and 1993.

In June 1990 President Bush announced new trade, investment and debt initiatives specifically for Latin America. The debt reduction component included a proposal for the Inter-American Development Bank to join the World Bank and the IMF in set-asides and for the United States Government to write-off or sell substantial amounts of its own loan portfolio, the latter designed to encourage debt-for-equity and debt-for-nature swaps.

Similar proposals are likely to emerge for poorer countries whose debts are primarily government-to-government. Countries that embrace economic reform policies that encourage growth can be expected to benefit from the Brady Plan over the next several years.

B. THE GENERAL AGREEMENT ON TARIFF AND TRADE (GATT)

Major U.S. trade policy efforts are the Omnibus Trade and Competitiveness Act of 1988 and the activities undertaken in the current GATT Uruguay Round.

The GATT Uruguay Round was launched in 1986 as the eighth negotiating round held under GATT auspices since its 1948 creation. Issues of services, trade-related investments, and intellectual property rights were introduced for the first time with the Uruguay Round.

Inclusion of services is controversial and distinctive. It includes the insurance, banking, tourism, construction services, communications and other information-related services such as data processing. A draft document, adopted by the Group of Negotiations on Services, has been written to serve as the basis for further negotiations. Negotiations are expected to provide a framework for the progressive liberalization of trade in services as well as for increasing participation in the service sector by developing countries.

The United States, through the U.S Treasury Department, has proposed an Annex to the draft document specifically addressing financial services. The annex proposes the right of establishment, national treatment, provision of free payments and transfers (with exceptions for balance of payments purposes), and provisions for regulators to carry out prudential regulation.

Developing countries have been consulted on the draft annex, but to date none have signed on. Some developing countries have voiced concerns regarding the issue of potential foreign presence in a delicate part of the economy. Other countries have raised concerns that, due to the small size of their financial systems, foreign banks easily could develop near monopoly market share.

The financial services annex is moving along slowly. It is not clear when an agreement will be reached.

Concurrently, the United States Government, through the Securities and Exchange Commission, has removed certain restrictions on the resale of unregistered securities. Since most of the securities issued by foreign borrowers are unregistered, it is expected that these changes could serve to further open U.S. capital markets to foreigners, including borrowers from developing countries.

SECTION III

PROGRAM ACTIVITIES

A. THE WORLD BANK

1. History and Purpose

The World Bank's programs for financial market development are quite extensive and are expected to increase in the 1990's. Program activities encompass multiple objectives and large amounts of funding. The World Bank is active in programs that support macroeconomic adjustment, financial sector reform, strengthening of domestic financial institutions, provision of funds for on-lending, and increasing international capital flows through debt-reduction and co-financing activities. The World Bank also engages in a substantial amount of policy research and training related to financial market development.

Since the early 1980's, the World Bank has supported structural adjustment lending. Its purpose is to improve the functioning and efficiency of the economy as a whole and to allow for the removal of impediments to its long-term development. Structural adjustment lending related to financial markets has focused primarily on exchange rate and interest rate liberalization, and more recently on assisting countries make the transition to a market-oriented system through privatization.

In response to banking failures, The World Bank has increased significantly the number of adjustment loans specifically targeted towards the financial sector. The objective of financial sector adjustment lending is (i) to develop well-functioning, competitive, market-oriented financial systems, (ii) to ensure that supportive legal and regulatory frameworks are in place and that supervisory institutions are strengthened, and (iii) to ward off the likelihood that financial systems insolvencies happen again.

In line with the objectives of financial sector adjustment lending, the World Bank is in the process of implementing major policy changes that will cause its vast on-lending programs to take into consideration the furtherance of the financial sector objectives described above. Such policies were laid out in a Task Force Report on Financial Operations in 1990.

The World Bank is also active in programs that are designed to increase international capital flows. Several of these programs are designed to elicit support from the private sector, such as the Expanded Co-Financing Guaranty Program (ECO). The ECO program is an outgrowth of the World Bank's "B" loan program which was designed to encourage the commercial banks to lend funds to World Bank projects. The dormant "B" loan program was seen as too high risk for the World Bank to continue due to arrearages and reschedulings of the "B" loans. The ECO program was designed to access not only commercial banking money, but also other sources of long term capital such as the bond and private placement markets. The program was started on a pilot basis in 1989 and was recently reauthorized to continue.

In 1990 the World Bank began a program of debt-related structural adjustment lending where the reduction of principal and/or interest payments was a primary objective of the loan. The objective of this type of lending is as a complement to adjustment operations, as a means to increase investor confidence in a country, and as a way to reduce and stem capital flight.

2. Program Description

2a. Adjustment lending for policy and financial sector reform

These loans generally are quick-disbursing loans with accompanying loan conditions based upon targeted levels of macroeconomic performance. Each loan generally will include specific actions that are monitored by the bank over a 12-18 month period. Typical conditions for financial sector policy loans include the elimination of credit allocations, removal of barriers to entry, elimination of restrictions on bank activities, removal of taxes, improvement of information systems, and movement towards a more supportive legal, regulatory and administrative structure.

The use of funds varies from loan to loan, depending on the needs of the sector. A large proportion of the money has been used for financial restructuring of insolvent banks. More recent loans have had larger technical assistance components. For example, a recent $66 million financial system modernization loan for Hungary contained a very large technical assistance component, as follows:

- Technical assistance for changing legislation, regulations and bank supervisory practices. ($1.4 million);
- Technical assistance and training for development of the securities market in collaboration with the IFC ($2.4 million);
- Modernization of accounting and auditing standards ($0.8 million);
- Technical assistance to banks for institutional development and restructuring, if necessary. (Budapest Bank, Commercial and Credit Bank, Hungarian Credit Bank, and National Savings Bank) ($34.9 million).
- Technical assistance for bank infrastructure including a training center, bank clearing house, and a central bank information system ($19.7 million).

2b. Loans to financial intermediaries

Revised World Bank policy for loans to financial intermediaries now seeks to ensure that new loans will serve to strengthen financial institutions and the financial sector. Each loan is supposed to include an assessment of the impact the loan is expected to have on the financial sector. This policy shift is in the process of implementation.

2c. Adjustment lending for debt reduction

In 1990 the World Bank approved for the first time loans to facilitate debt-reduction programs in heavily-indebted countries. These programs provided debt-relief through combinations of new money, conversion of debt into discounted collateralized bonds or other similar securities, and debt buy-backs. In one case, Mexico, funds were also used to support interest payments. (See Section II(A) for a description of the Mexico deal.) The Philippine agreement was less complex, as follows:.

- Philippines The agreement offered banks the choice of selling debt to the government at 50 cents to the dollar or providing new money. In support of this agreement the World Bank approved a $200 million loan for the Philippines to buy-back some its debts. This agreement allowed smaller commercial banks to reduce their Philippine exposure with a one-time loss and for the larger banks to provide new money and maintain the face value of their assets.

2d. Co-financing

The Expanded Cofinancing Guaranty Program, or ECOs, is a credit enhancement program designed to increase developing countries' access to new sources of medium and long term private capital and, also, to leverage the direct lending capabilities of the World Bank.

Currently the program is available for World Bank supported projects only. Also the ECO program is available for countries that have not officially rescheduled their commercial bank debts. Under this program the bank assumes certain contingent obligations that reduce private lenders' risk of repayment. Contingent obligations usually take the form of partial guaranties of principal and/or interest on loans or bonds, but may also include guaranties of other financial instruments such as guaranties of letters of credit, standby lines of credit or puts[4]. Guaranties of project-specific government undertakings may also be issued, particularly in connection with large-capital intensive energy projects. Examples of ways in which this program can be used are as follows:

- The program can be used to partially guarantee commercial bank loans; this would be appropriate in countries where borrowers do not have full access to commercial bank borrowing.

- The ECO program can be used in support of project financing where certain sovereign undertakings are expected from project sponsors, and the ability of the government to back the undertakings is an impediment to obtaining capital.

An example of a completed transaction is as follows:

- Hungary The World Bank issued a partial guarantee of a ten-year bond issue for the State Development Institute of Hungary, an executing agency under an existing World Bank project. The $200 million bond was a ten-year bullet maturity. The World Bank issued a 100% guaranty of the full principal amount due in the tenth year. No interest payments were guaranteed. The bond was priced at 195 basis points over ten year U.S. treasuries. The World Bank will receive a guaranty of repayment from The Government of Hungary. The purchasers of the bond do not make any direct payments for the credit enhancement features. This bond issue was lead by Daiwa Securities Europe.

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[4] A put is a right to sell a financial instrument back to the obligor at a predetermined price.

To date the list of eligible countries numbers 15 and includes: Algeria, China, Colombia, Czechoslovakia, Fiji, Hungary, India, Indonesia, Malaysia, Pakistan, Papua New Guinea, Romania, Thailand, Tunisia and Turkey.

3. Accomplishments to Date

Structural adjustment loans with conditionality tied to the financial sector have been made in Algeria, Morocco, Tunisia, Turkey, Yugoslavia, and Pakistan. In the past two years the World Bank has approved financial sector adjustment loans totalling over $1.695 billion to Mexico, Bangladesh, Morocco, Bolivia, Pakistan, Senegal, Philippines, Venezuela, Kenya,and Hungary.

It is too early to tell how effective conditionality on financial sector adjustment loans will be. The bank is just beginning to conduct its own assessment and many of the reforms are long-term in nature. One important measure will be the effect of these conditions on the reduction in banking failures. To date the bank has made several observations regarding its financial sector operations - that interest rates may still need to be controlled in some countries, that measures to strengthen existing banks require decisive and difficult actions that have been implemented with varying successes, or that direct government action to develop capital markets can be counterproductive; indirect methods including privatization and removal of tax barriers are probably better. The evaluation process also has revealed the complexity of the issues and the challenges the bank is facing in designing and implementing appropriate conditionality.

In 1990 four debt-reduction facilities totalling $1.3 billion were approved - for Mexico, Venezuela, Costa Rica and the Philippines. Each loan contained a different menu of debt-reduction techniques that were negotiated between the borrowers and lenders and approved by the World Bank. The Bank considers these loans as successes, but the true success, measured by the ability of the countries to obtain new loans and the medium-term growth of their economies, can't be determined for several years.

Initially started as a pilot program, the ECO program has demonstrated to the World Bank its usefulness and has recently been reauthorized. It has the authority to issue up to $2 billion of contingent obligations, but to date has completed one $200 million transaction in Hungary. Several other transactions are near completion.

4. Future Plans

Expectations are that the World Bank will continue to make structural adjustment loans to the financial sector for the course of the decade. Countries next in line include India, Sri Lanka, Algeria, Morocco, Tunisia, Turkey, China, Indonesia, and Nepal.

Over the next several years attention will be focused on operational and evaluation issues of these relatively new financial sector lending programs. Issues of review will include analysis of the appropriate size of the loans and the use of the proceeds, what types of policy reforms should be linked to these loans, and how the loans should be disbursed and monitored. It is expected that the bank will move away from quick-disbursing loans towards longer disbursement cycles tied to performance under loan conditions.

For debt-reductions, lending will continue to proceed on a case-by-case basis. New guidelines and funds have been set-aside to offer debt reductions from IDA funds. Bolivia and Mozambique are expected to be the first recipients of these loans.

In the policy and research arena, topics of review will focus on the effect of financial policies and capital market imperfections on private investment, the role of risk capital in private sector development, and a thorough review of the banks' experience with financial sector adjustment operations.

The ECO program staff has been working in Pakistan on the Hab River Project and expects to provide guarantees of the Government of Pakistan's performance under certain of its contracts The staff is also considering participating in projects in India that would provide the Government of India access to the United States private placement market. Also under consideration are ways in which it could enable Latin American countries to access a large and liquid pool of tax-driven funds trapped in Puerto Rico, known as "936" Funds.

B. THE INTERNATIONAL MONETARY FUND

1. History and Purpose

The International Monetary Fund's purpose is to promote international monetary cooperation, international trade, and exchange stability. While its primary programs are its lending programs, the IMF also provides technical assistance and training, principally through its Central Banking Department, but also in its Fiscal Affairs Department and Bureau of Statistics. It also operates a training school, the IMF Institute.

The objective of the Central Banking Department's technical assistance programs is to assist countries in strengthening their technical and organizational capabilities in managing monetary policy and in regulating and supervising financial systems. The basic motivation is to ensure that countries have the capacity to implement policies which contribute to a healthy balance of payments position, growth and macroeconomic stability.

In recent years, financial sector reforms and modernization of monetary policy instruments have become key features of many Fund-supported adjustment programs. A significant share of technical assistance (over 20%) is thus related to these financial structural and reform programs.

2. Program Description

Most of the assistance provided by the Central Banking Department takes the form of staff advisory missions, assignment of long-term experts, and provision of information. In 1988/89 staff members undertook 31 advisory missions providing advice on a wide range of assignments. Over 100 long-term experts were in place in 1988/89. IMF Central Banking staff frequently are members of World Bank appraisal missions for financial sector reform loans.

Priority is given to assignments that serve to implement Fund-supported policies and reforms generally take the form of an advisory function rather than executive positions. Generally no more than three advisors can assist a country at any point in time. The training of counterparts is a standard part of most technical assistance and a key factor in the evaluation of the programs.

Representative assignments include the following:

- Indonesia — An advisory mission reviewed the bank supervision system of Bank Indonesia and provided specific recommendations to improve the system. As a result, a six-month technical assistance assignment in the bank supervision area was requested and an expert assigned as Advisor on Bank Supervision.

- Malaysia — Technical assistance through advisory missions was provided to Bank Negara Malaysia to develop the government securities market. Assistance was also provided in the form of a one year expert assignment to train bank inspectors and review sections of a bank inspections manual.

- Nepal — An advisory mission prepared a report on the development of money and government securities markets which prompted the Nepal Rastra Bank to request further technical assistance to implement measures on treasury bill auctions, open market operations, pubic debt management, and develop institutional arrangements for a secondary market in treasury securities. An expert was assigned for six months as Advisor on Market Operations.

- Tunisia — Two advisory missions to review the financial liberalization program were conducted. The first mission reviewed ways to improve the functioning of the money market and advised on the introduction of treasury bills. The second mission focused on ways to improve the regulatory and institutional framework of the banking system in order to stimulate interbank competition.

Other Departments within the IMF such as Fiscal Affairs Department and Bureau of Statistics provide a great deal of technical assistance, a smaller portion of which is related to financial market development. Examples of representative assignments related to money and banking undertaken by the Bureau of Statistics are as follows:

- Bangladesh — To review the implementation of a new reporting system for commercial banks including adding more information on deposits, new credit flows and on the financial position of the banks. To facilitate accurate reporting training was provided.

- Philippines — Technical assistance was provided to reconcile differences in data, to establish a single reporting system in providing data to the IMF, to review the impact on monetary accounts of the transfer of non-performing assets and liabilities of two government-owned banks to the national government.

The IMF institute trains officials of member countries through courses and seminars, arranges briefings for visiting officials, and assists training programs of member countries and other organizations by providing lectures.

IMF also publishes reports, papers and books that may be relevant to financial market development. In 1989 it published a book, International Capital Markets; Development and Prospects. A magazine, Finance and Development is jointly published with the World Bank on a quarterly basis.

3. Organization, Budget and Staffing

Countries requesting technical assistance are expected to pay at least one third of the expert's salary. Some of the IMF's technical assistance programs are funded by World Bank missions. There has been discussion of obtaining UNDP money for IMF technical assistance.

Much of the short-term advisory work is undertaken by IMF staff. Panels of experts are used to supply a reservoir of expert talent and to select experts for assignment. In most areas there is a shortage of available experts.

4. Accomplishments to Date

Judging by the demand for technical assistance, which remains high, the program has been successful. In part this may also be due to careful selection of assignments. Limited success in training local staff due to lack of university graduates, noncompetitive compensation and political changes continues to be a problem.

C. INTERNATIONAL FINANCE CORPORATION

1. History and Purpose

IFC established a Capital Markets Department in 1971 in recognition of the importance of financial markets in economic growth, although the department's activities did not receive any notable market acceptance until the early 1980's. The group's objectives are to increase the size, depth and efficiency of domestic financial markets and to provide increased access for private companies to international financial resources. Emphasis is placed on programs that increase the flow of longer-term financing.

IFC also has a syndications department which raises additional capital for IFC-supported investments. This department also has been working on the creation of several multi-country loan programs that expect to increase international capital flows.

2. Program Description

The Capital Markets Department's programs fall into three broad categories, domestic financial market investments, improving access to international capital markets, and technical assistance. In addition, other financial market activities are also conducted by a new Corporate Finance Services Group and by the Syndications Department. These programs are described below:

2a. Domestic financial market investments

Domestic financial market investments primarily consist of creating new financial institutions and/or expanding the services of existing institutions. IFC's role typically includes project identification, feasibility analysis, investment (through equity, loans or syndications) membership on an institution's Board of Directors (where an equity investment has been made) and project monitoring.

Over the years IFC has invested in a wide variety of institutions; the type of institution or transaction supported depends upon the structure and stage of development of a particular country's financial market, and to a certain extent, on trends in financial market development from year to year. IFC has supported the creation or expansion of money market firms, investment and merchant banks, mutual funds, housing finance companies, leasing companies, commercial banks, development finance companies, venture capital firms, and insurance companies. Also, on-lending programs for small and medium scale enterprises and export projects have been popular.

2b. Improving access to international capital markets

Over the last several years emphasis has been placed on the development of new programs that increase the level and diversify the sources of international financial flows to developing countries. IFC's programs are targeted towards increasing equity flows and longer-term maturities of debt, and towards obtaining investment capital from institutional and other portfolio investors, particularly from the world's largest securities markets in New York, London and Tokyo.

IFC has been a pioneer in the sponsorship and participation of a series of publicly-traded and privately-placed country and regional investment funds, debt/equity conversion funds, and in the underwriting and placement of securities issued by private companies in developing countries. The investment funds have been closed-end mutual funds[5] that purchase securities traded on the stock markets of developing countries. In addition IFC has created The Emerging Markets Data Base, an important source of statistical information for this new group of investors and investment managers.

2c. Technical assistance and advisory services

Technical assistance programs provide advice to governments regarding the legal issues, regulatory and fiscal policies, and institutional development issues relevant to financial market development. Specific financial institutions are offered technical assistance for operational, managerial and training needs.

Sample areas of technical assistance include fiscal policies to promote long-term savings, financial leasing regulations, the role and organization of securities commissions, secondary market mechanisms, particularly stock exchanges, financial market information requirements in general and securities market disclosure in particular, and regulations concerning foreign portfolio investment.

Demand for technical services has always outpaced IFC's ability to provide assistance, and with the inclusion of Eastern European countries, demand has surged. Therefore, IFC tends to take a pragmatic approach to choosing its assignments with the likelihood of success (i.e. will the law get passed) and the receptiveness of the recipient country being the two most important criteria in acceptance of an assignment. Projects that will lead to investment opportunities for IFC are also favored.

Technical assistance is provided by IFC's capital markets staff who have many years of experience as capital markets generalists. Specific technical expertise from outside IFC is sometimes arranged, but is funded from other sources. Most of the assistance is short-term in-country advisory work.

2d. Other financial market activities

A new Corporate Finance Services Group, which works on restructuring and privatization transactions, was formed in 1990. Several of the privatization transactions, especially those in Eastern Europe, will involve new issues of securities on domestic exchanges. For example, in Poland, a public offering of shares in connection with the privatization of a furniture factory is being arranged for a fee. This group will need to deal with financial market issues such as the absorptive capacity of domestic stock markets and the pricing of these shares in a rapidly changing economic environment.

[5] Closed-end mutual funds are funds that purchase and sell securities in a certain market or sector based upon their net cash flow positions. The net cash flow position depends upon the market value of the fund as it trades on an exchange.

In addition, IFC's syndications group raises funds on international capital markets for use in IFC's investment projects. The syndications group has developed several multi-country loan funds that also increase financial flows to developing countries.

3. Accomplishments to Date

The activities of the capital markets group have grown rapidly in recent years. In FY 1990 $423 million of capital markets projects were approved for 33 projects, a substantial increase over FY 1989 approvals of $160 million for 20 projects. In addition to increased levels of investment, the group also has pioneered several innovative programs.

Recent transactions have included an investment to establish the first merchant bank in Pakistan, an investment in a venture capital company in India to promote commercial development of new technologies, investments in six leasing companies, and an investment in a mutual fund management company in Thailand. On-lending activities were expanded to include on-lending facilities in Poland, Indonesia, Mexico and Zimbabwe.

Since its first country fund was established for Korea in 1984, IFC has participated in ten publicly-traded country funds, 11 privately-placed country, regional or global funds, six debt/equity conversion funds and six international corporate securities offerings. IFC's participation has been in traditional investment banking roles as underwriter, lead manager, co-lead manager, and as placement agent. Generally IFC works in partnership with an established investment banking firm that acts as fund manager. IFC also has invested over $85 million of its own money in these funds. IFC has promoted debt/equity conversion funds in Chile, Philippines, Brazil and Argentina and has invested $40 million in them.

It is too early, perhaps, to determine the success of these investment funds since the majority of them have been operating for only one or two years, or are still in formation. Initially, the securities markets in New York and London favored the funds; those that are publicly traded sold at substantial premiums to net asset value. In the last six months, however, the market prices for these funds have declined significantly and many of them are now traded at substantial discounts to net asset value. Investors are realizing the inherent risk of their investments due to foreign currency risks, securities market risks in the target countries and regions, and general business cycles. Over the longer term, however, these investors indeed may realize high returns commensurate with the risks that they are assuming.

In the area of new securities offerings, last year IFC participated in the underwriting and placement of a $100 million dollar issue on the New York Stock Exchange for the Compania de Telfonos de Chile which represented the first time a Latin American equity issue was available on the New York Stock Exchange.

The Emerging Markets Data Base is generally considered a success given the void that previously existed regarding statistical information on developing countries' stock markets. In particular the IFC has developed systems to calculate market indexes and data on returns that are consistent for all reporting countries.

IFC has provided approximately 8 - 10 person-years of technical assistance in 45 countries. Recently, it has provided assistance to Hungary in the development of its stock exchange. Assistance was also provided for this project by the United States Securities and Exchange Commission and the World Bank.

4. Future Plans

Expectations are for continued expansion of activity throughout the 1990's. Emphasis will be placed on creating new types of institutions in countries where they are currently lacking, such as investment banks, venture capital companies, and contractual savings institutions. Regional emphasis may be placed on Africa and Eastern Europe.

Over the next several years IFC expects to do more advising, investing and structuring of international securities offerings and assisting companies gain access to international markets by helping them obtain credit ratings and comply with other regulatory and market requirements. Also, IFC expects to be involved in promoting the securitization[6] of assets. It may be that the international markets' interest in regional and country investment funds has thinned out; the level of new funds is likely to be lower than it was in the last three years.

IFC expects to expand its technical assistance programs, but expansion will be constrained due to the lack of funds and the limited staff available with the requisite technical skills. Future technical assistance assignments will likely focus on countries with nascent stock exchanges and other market-oriented institutions.

D. THE UNITED NATIONS

1. History and Purpose

Two programs operated by the United Nations are expected to assist in financial sector development. One is a new program sponsored by the United Nations Development Programme in its newly-established Division for the Private Sector in Development. The other program, International Programme on Savings and Credit for Development, a policy research and symposium program is operated through the Department of International Economic and Social Affairs of the United Nations Secretariat.

The UNDP program is new. One of its primary objectives is to "create a predictable enabling environment in which entrepreneurs and investors will be encouraged to thrive and to move into the mainstream of development."

The other program, The International Programme on Savings and Credit for Development was established in 1971. From inception it has focused on the importance of domestic savings

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[6] Asset securitization involves the standardization and packaging of untradeable assets to turn such assets into liquid and tradable claims.

mobilization and credit allocation for economic development. Of particular focus has been the mobilization of informal savings and the allocation of credit to small farmers and entrepreneurs.

2. Program Description (UNDP)

UNDP recently established a Division for the Private Sector in Development. The group will be the central point of UNDP on all private sector matters. It will provide support to the field offices on private sector projects.

Relevant areas of focus will include:

- Assistance to governments in a creating suitable environment for private investment and entrepreneurship. Assistance could take the form of advice on legislative and regulatory procedures and fiscal systems.

- Capital market development and investment promotion - which could include creation of stock markets and nurturing of other capital markets.

- Small and medium scale business development. Work here will include project identification, management training, market studies, helping businesses get credit, establishing business incubators and industrial parks and encouraging formation of industrial subcontracting.

- Privatization - Helping governments to privatize economies and specific enterprises. Emphasis will be placed on evaluating the economic and social effect of privatization, especially in Eastern Europe.

- UNISTAR - reservoir of volunteer consultants and technical experts.

Prominent member of local business communities will be appointed Private Sector Advisors in countries.

3. Organization, Budget and Staffing (UNDP)

A budget of $4 million has been allocated to the Division for Private Sector in Development. Funding for UNDP as a whole is based on five year development cooperation cycles and indicative planning figures - formulas based on a country's population and per capita GNP. (1989 UNDP income, including its main programs and trust funds totaled $1.2 billion.) Staff is currently being assembled at headquarters.

4. Accomplishments to Date (UNDP)

Special Private Sector Advisors have been appointed and are already functioning in several countries. A mechanism has been established to work with executing agencies including the World Bank, the IFC, regional development banks and bilateral donor agencies. Assistance has been provided for the privatization plans in Poland, Bulgaria, Czechoslovakia and Morocco. The ground work is being laid for establishment of venture capital funds for Egypt, Tunisia, Indonesia and sub-Saharan Africa.

Assistance with enabling environments has occurred in cooperation with IFC in Guinea, Indonesia, Morocco, Sri Lanka and Tunisia.

UNDP has provided feasibility funding for a venture fund that was established in Zimbabwe and financed by the International Finance Corporation.

5. Future Plans (UNDP)

In Indonesia, a "Fund for Indonesia" is expected to add technical assistance for venture capital projects including work on business plans, managerial and marketing support. Capital (estimated at $50 million) will be provided by UNDP and and raised from an Indonesian private business group. It is expected that funds will be raised in the second half of 1991.

6. Program Description (UN Secretariat)

Under the umbrella of the United Nations Secretariat, Department of Economic and Social Issues, a group of representatives from ministries and central banks, private and public banks, savings bank associations, and non-governmental organizations have been convening to further their financial sector technical assistance projects, and their research and policy agendas. The group also promotes co-operation and co-ordination among its members. The findings of its workshops and symposium have been published by the United Nations as reports titled Savings and Development .

Membership of the steering committee includes the bilateral aid agencies and savings bank associations of Denmark, Germany, France, Norway, Sweden and the United States.

Most recently the group, in cooperation with the Danish Savings Banks Association and the International Savings Banks Institute, organized the International Conference on Savings and Credit for Development. It was held in Denmark in May 1990.

Much of the work of this group is directed towards savings institutions and the participation of the informal sector in savings. The group conducts research on the links between the formal and informal sectors. Another area of focus is financial sector reform and the impact of macroeconomic policies on savings.

7. Organization, Budget and Staffing (UN Secretariat)

The United Nations acts at the group's Secretariat and is a member of its Steering Committee. One staff person handles most of the administrative functions. Over the years, this group has received most of its funding from the Swedish, French and Danish associations of Savings Institutions.

8. Accomplishments To Date (UN Secretariat)

This program is currently in its third funding phase. The first phase (1971-1978) consisted of four workshops and publication of the workshop findings. The second phase (1979 - 1987) the group sponsored several more symposia and published the findings. In 1989 the program was formalized through the establishment of a Steering Committee.

The program has been successful in providing a forum for donors to exchange information and policy research, and as a means of pooling resources.

9. Future Plans (UN Secretariat)

This group plans to hold international conferences on savings and credit biennially. Regional symposia will be organized and held annually.

A regional symposium for Africa is scheduled to be held in Cote D'Ivoire in June 1991. It will be jointly organized by the United Nations and the African Development Bank. It is expected that there will be 90 to 100 participants, consisting of 50 to 60 African experts from central banks, ministries and financial institutions and 30 to 40 representatives of bilateral aid agencies and international organizations. The conference will focus on four themes:

- Creating an enabling environment for financial sector development in Africa;
- Adequacy of the structure of the financial system for economic development;
- Poverty alleviation through innovative approaches to linking the formal and informal financial sectors in Africa.

Another regional symposium is proposed for Latin America or Asia in 1992.

E. THE OVERSEAS PRIVATE INVESTMENT CORPORATION

1. History and Purpose

While the main thrust of OPIC's programs is to increase foreign direct investment, several of its programs serve to increase the business activities of the United States financial sector in developing countries. Two of these programs, political risk insurance coverage for commercial bank loans and coverage for branch bank capital have been in existence since OPIC's inception.

Since 1986 OPIC's finance department has been active in the development of investment funds that provide capital on a regional or global basis. The purpose of these growth funds has been to provide a source of equity capital to markets that have long had only debt to rely upon. Other objectives of the growth funds are to increase the supply of marketable securities, to encourage the creation of an environment for third party ownership and a precedence for minority shareholder rights.

2. Program Description

2a. Political risk insurance for financial transactions

OPIC insurance policies can be purchased to cover specific financial transactions. Insurance is provided to eliminate the political risks of currency inconvertibility, expropriation, or loss due to war or revolution. The existence of such insurance coverage serves as a credit-enhancement feature for banks or financial institutions; it enables banks to take a more active role in Third World markets without assuming unacceptable risks. Also in some instances, OPIC insurance coverage on bank loans eliminates the need to report the loan as cross-border exposure for United States regulatory purposes.

Examples of recent insurance policies for financial transactions are as follows:

- Trinidad and Tobago

  Term bank loans that otherwise may not have been available were provided to finance an industrial project. Funds were obtained by Citibank using Section 936 Funds from Puerto Rico and backed by letters of credit and guarantees. OPIC provided insurance for the project's financing which included protection against loss resulting from rescission by the Government of Trinidad and Tobago of the project's right to hold an off-shore escrow account from which to service the debt. In this way Citibank was protected against perceived political risks and incremental cross-border exposure. The total amount of loan principal insured was $66.5 million.

- Pakistan

Foreign banks in Pakistan are able to increase their domestic lending operations by using a foreign currency deposit program under which the foreign bank accepts US dollar deposits and sells the deposits to the State Bank of Pakistan which guarantees reconversion into dollars upon maturity at the original exchange rate.

Foreign banks can profit from two sources of interest receipts - from the State Bank and from new borrowers in Pakistan. However, the foreign bank must assume the risk that the State Bank will return the deposits, in dollars.

OPIC provided insurance coverage to the Pakistan branch of the Chase Manhattan Bank on one of these deposits. Coverage for Chase provides protection against the State Bank's failure to provide dollars when due. The amount of new capital that flowed to Pakistan under this transaction was $15 million.

- Costa Rica

OPIC insured an investment by a financial institution via a debt/equity swap. The financial institution converted Banco Central de Costa Rica promissory notes into local currency and invested the proceeds in a manufacturing enterprise in exchange for preferred stock. OPIC insured the payment of dividends on the preferred stock and the redemption of the stock at par value on its due date. The investment in equity was for $4 million.

2b. Political risk insurance for branch bank capital

Since its inception OPIC has insured branch bank capital against certain political risks. This coverage encourages banks and other financial institutions to establish banking business in developing countries as well as to expand existing in-country banking operations. Coverage is available for capital investments and for reinvested retained earnings. From a developmental perspective the program transfers U.S. banking technology and increases competition in local financial markets. This program has been popular with banks for twenty years. Citibank and Chase Manhattan Bank have been steady and frequent users of this program.

3. Accomplishments to Date (Insurance)

As mentioned above, the insurance of U.S. branch capital has been an ongoing program that is very popular with money center banks that have extensive branch networks. In the late 1970's and early 1980's insurance on bank transactions was not a popular program because the added cost of insurance reduced margin spreads on loans. Recently, particularly in Latin America, where loan pricing is not as critical as it is in Asia, banks have been more amenable to purchasing political risk cover. In FY 1990 OPIC issued nearly $650 million of bank transaction coverage, an increase of over 50% from previous years levels.

4. Future Plans (Insurance)

The insurance department continues to explore new ways to work closely with banks and other financial institutions. New transactions are likely to be created that stimulate medium-term trade capital flows, that provide insurance cover for loans used in privatization activities, and that provide coverage for debt/equity conversion funds. New programs are being developed to provide political risk insurance for commodity and financial swaps. Existing programs will be continued.

5. Financial Guarantees for Investment Funds

Over the last three years OPIC has sponsored and committed its investment guaranty authority towards the creation of three privately-owned and managed investment funds.

The first to be completed, The Africa Growth Fund, is a $30 million venture capital equity fund for private sector projects in sub-Saharan Africa. The fund is a limited partnership privately-owned by five U.S. corporations and managed by an affiliate of Equator Bank. The Fund can provide up to 20% - 45% of a project's total equity capital and will participate in management of the enterprises in which it invests through membership on boards of directors. An important objective of the Africa Growth Fund will be to sell its equities to third parties within a 3 to 15 year timeframe in order to return capital to its owners and to develop a new source of securities for African markets.

A fund for equities of Eastern European countries and a global fund for environmental projects were approved by OPIC and are currently being formed. The Eastern European fund will be managed by Soloman Brothers out of its London office. The environmental fund will be managed by a partnership between Kidder,Peabody and Booz Allen Hamilton.

OPIC's participation in these funds has been through its investment guaranty authority whereby investors are offered full guaranties of any and all interest and principal when due. In order to structure the investments to be as "equity-like" as possible, most of OPIC's participation will be guarantees of zero-coupon bonds or loans with single bullet maturities.

6. Accomplishments To Date (Investment Funds)

The Africa Growth Fund has chosen its first three portfolio investments and is well on its way towards identifying additional investments. The fund still needs to raise additional capital in order to reach its $30 million target. To date the existing owners of the Fund are pleased with the fund's progress.

The Eastern European Fund and the Environment Fund are expecting to begin raising capital in the near future.

7. Future plans (Investment Funds)

A $100 million investment fund for Asia has recently been approved (OPIC's participation will be an investment guaranty of $50 million.) It will be managed by Hambrecht and Quist, a San Francisco-based investment banking firm with extensive venture capital experience and a presence in several Asian cities.

OPIC expects to continue sponsoring investment funds. Funds for Latin American and the Caribbean and one for Mediterranean countries are on the drawing board. Under consideration is a secondary market fund which would invest in marketable securities and also purchase the securities from other investment funds.

F. THE UNITED STATES EXPORT-IMPORT BANK

1. History and Purpose

The main objective of the Export-Import Bank (EXIM) is to promote exports of United States goods and services. None of its programs have financial market development in developing countries as an objective. However, certain programs, such as insurance for bank letters of credit and leases, have provided indirect benefits for certain country's financial sectors. The benefits of these programs consist of access to new sources of credit, in this case short and medium-term trade credits. The leasing programs also provide an additional source of credit to developing countries. EXIM's letter of credit and leasing insurance programs began in the early 1980's and have been revamped several times during the last ten years.

In 1984 Congress established a trade credit insurance programs (TCIP) for Central America under which A.I.D. was authorized to issue guarantees to EXIM for its export credit insurance program. This program continues to operate and has also increased the level of trade credits. A similar program has been established for Poland.

2. Program Description

EXIM bank sells letter of credit insurance to U.S. exporters and banks to cover the risks of trade transactions with foreign banks. Foreign banks apply to EXIM for maximum credit amounts and in effect obtain revolving lines of credit from EXIM for U.S. goods and services. The leasing programs protects U.S. lessors political risk coverage of non-payment on operating and financial cross-border leases.

There are many developing countries where EXIM does not operate, or where its operations open and close depending upon the status of a country's loan repayments and claims. In order to make EXIM programs available in more developing countries, a joint EXIM/A.I.D. trade credit insurance program was developed. In this program, EXIM conducts its programs as usual, but is counter-guaranteed by A.I.D. This has allowed EXIM to operate in countries where it would have normally closed.

Recently, EXIM and FCIA announced a similar trade credit insurance facility for Mexico that is similar to the EXIM/A.I.D. facility, but that will operate without A.I.D. guarantees.

A new process, known as "bundling" has been established for Mexico. Under a bundling facility several local Mexican banks can aggregate a group of trade credits and deliver the notes to EXIM which then funds the aggregated notes in the United States capital markets through the use of its guaranty. This program allows local banks to participate directly with EXIM and at the same time provide them access to the United States capital markets.

3. Organization, Staffing and Budget

EXIM bank's budget for direct lending has been reduced in recent years, but its capacity to issues guarantees and medium and short term credit insurance has not been hampered. The bank has the authority to issue up to $12 billion of guarantees and insurance, a level which has comfortably met the demand for the program. The trade credit insurance facility for Central America and Poland have been renewed, but are likely to be eliminated due to budget cuts in FY 1992. The "bundling" program will be tested next in Chile, Venezuela, and Colombia, and perhaps, Kuwait.

4. Accomplishments to Date

The bank letter of credit insurance programs are well-used programs, particularly for Latin American countries. In FY 1989 EXIM issued over $4 billion of short and medium-term credit insurance.

Over the five years that the EXIM/AID trade credit insurance facility has been operational, it has provided over $800 million of credits to the banking system in Central America. El Salvador and Guatemala were the heaviest users of the facility followed by Honduras and Costa Rica.

Under the recently announced trade facility for Mexico, two Mexican banks have received lines of credit, Bancomext for $75 million and Nafin, for $50 million.

The leasing programs have not been as popular, but are operational.

G. THE FEDERAL RESERVE SYSTEM

1. History and Purpose

The Federal Reserve Board, in joint cooperation with the World Bank offers a three week seminar for senior bank supervisors from developing countries. The seminars were started in June 1987 in recognition that in most countries highly specialized bank supervision and examination skills have been learned on the job, with only the largest and most developed countries having the resources to establish training departments and courses.

The objective of the training seminars is to familiarize participants with the supervisory problems faced by developing countries and the constraints such problems pose to economic growth; to discuss solutions for dealing with bank insolvencies through deposit insurance schemes and bank restructuring and to build basic bank supervision and examination skills.

From time to time staff of the Federal Reserve System (the Board and the various Federal Reserve Banks) also provides adhoc advisory and technical assistance when requested. Such assistance may be at the request of the World Bank or the IMF, and generally is not likely to be of a bilateral nature

The Federal Reserve System also represents the United States Government in meetings of the Basle Group.

The Federal Reserve Bank of San Francisco has formed The Center for Pacific Basin Monetary and Economic Studies. The objective of the center is to promote cooperation among central banks in the region and to enhance public understanding of major economic policy issues. Over the years conferences have been sponsored and research published.

2. Program Description

The Federal Reserve Board training seminar is designed for senior bank supervisors from developing countries, including directors, deputy heads or high level staff involved in bank supervision policy formation. In addition, a limited number of World Bank staff are invited.

The first week of the course focuses on the principal policy issues facing bank supervisors in developing countries. Linkages between financial system health and macroeconomic performance and the World Bank's strategy for financial sector reform are covered. The focus of weeks two and three is skill development. Topic include: loan portfolio management, credit analysis, classification of assets, bank analysis, foreign exchange risk, interest rate risk, the CAMEL rating system, costs of intermediation, and internal and external auditing.

Classes are taught by World Bank staff, experts from U.S. bank regulatory agencies, accounting firms, Federal Reserve, and the Office of the Comptroller of the Currency.

The Center for Pacific Basin Monetary and Economic Studies sponsors programs of staff research, a visiting scholars program (up to three at a time), and an outreach program of affiliated research associates.

3. Organization, Budget and Staffing

The training seminar is funded by the Federal Reserve Board and the World Bank. There is no cost for participants to attend. Most of the course development work is handled by the staff of the Division of Banking Supervision and Regulation which estimates it has a budget of no more than $20,000 for each course.

The Federal Reserve Board has no budget or organizational structure for its adhoc technical assistance programs.

The Center for Pacific Basin Economic Studies has a staff of three professionals.

4. Accomplishments to Date

Demand for the Federal Reserve course for bank supervisors has been high. To date approximately 350 people have attended. The World Bank is responsible for the follow up on the course. The World Bank has stated that in many countries the policies, procedures and skills have been transferred particularly in regard to the closing and restructuring of insolvent financial institutions.

In San Francisco, the Pacific Basin Economic Center has a long history of conferences planned and research published. The center has developed an extensive network of researchers from central banks, international organizations, universities, banks and corporations.

In 1990 center held three conferences. The first was co-sponsored by the Harvard Law School and The Asia Foundation. The topic was "Money Markets and Monetary Policy in the Pacific Basin." The second conference co-sponsored by The 1990 Institute was on China's economic reform. The third conference co-sponsored by the American Committee on Asian Economic Studies was on "Challenges in the 1990's for Banking and Financial Markets: U.S. and Asia."

5. Future Plans

The next session of the bank supervisors training course will be held from October 28 to November 15, 1990 in Washington, D.C. Given the success of the seminar, a new series of advanced seminars for past participants is being considered.

The Pacific Center expects to focus its research activities on the implications of increasing international financial integration for the conduct of monetary and exchange rate policies in the Pacific Basin economies. The center will continue to support research on economic reform in China and other socialist countries in the region.

H. THE SECURITIES AND EXCHANGE COMMISSION

1. History and Purpose

The SEC is involved in international economic issues because of the growing globalization of international financial markets and their effect on the integrity and fairness of United States securities markets. Also, to further market development around the world and in recognition that many countries are restructuring their financial systems to include securities exchanges, the SEC has recently formed a new committee and is offering more training to securities regulators from developing countries.

2. Program Description

In May 1990 the SEC announced the formation of the Emerging Markets Advisory Committee (EMAC). The committee is comprised primarily of private sector representatives from investment banking firms, stock exchanges, clearing houses, law firms, banks, academia, and accounting firms. The United States Government is represented by Commerce and the Federal Reserve Board.

EMAC representatives will be requested by the SEC to respond to technical assistance requests from countries with emerging markets. Requests for assistance may include advice on developing disclosure systems and reporting, how to set up settlement and clearing systems, trading, how to license professionals, how to enforce markets, etc. Many requests are expected to relate to the training of regulatory personnel.

SEC staff also provide technical assistance upon request. Staff may provide short-term advisory assistance or personnel from other countries may do internships on the premises of the SEC for periods from two weeks up to three months.

SEC staff also participate in membership in the International Organization of Securities Commissions (IOSCO) and have observer staus on IOSCO's market development committee.

3. Organization, Budget and Staffing

The SEC does not have very much funding for its international programs. Technical assistance provided by SEC staff does not cover any additional expenses beyond staff salaries and limited travel costs. It can not pay for the travel costs of the Institutes participants and the EMAC representatives are all donating their time and services. Organizationally, international issues are handled by an International Division, with technical assistance provided by members of other departments such as Market Regulation and Corporate Finance. The Institute's activities are being coordinated from the Office of Economic Analysis.

4. Accomplishments to Date

In June 1990 a Memorandum of Understanding Between the SEC and the Republic of Hungary State Securities Supervision and Budapest Stock Exchange was signed regarding the provision of technical assistance. The agreement calls for the training of personnel and the provision of information and advice on the development of the Hungarian securities markets. Pursuant to this agreement the SEC staff reviewed the existing Hungarian company act and securities laws and recommended legislative changes. A training program on how to review prospectuses was conducted.

The SEC is in the process of providing technical assistance to Bulgaria. In the past assistance has been provided to the Government of Indonesia, and to Mexico. Internships at the SEC have been provided to regulators from Hungary, Chile, and Israel.

The EMAC as a group has met once for general organizational purposes, and one panel discussion group has been held that dealt with where technical assistance was needed. Four working groups have been assembled: corporate finance, market regulation, financial institutions and intermediaries, and legal.

Several EMAC members have provided technical assistance to Hungary. For example, one member provided assistance on ESOPs (Employee Stock Option Plans.)

5. Future Plans

The SEC has established an International Institute for Securities Market Development which will provide training, internships and technical assistance in the formation and operation of securities markets. The first program of training will be held in Washington D.C. from April 22 to May 3, 1991. The program is designed for officials responsible for securities regulation. The faculty will consist of SEC, World Bank, IFC, U.S.Treasury, Federal Reserve System officials and representatives from the organization comprising the Emerging Markets Advisory Committee.

The SEC is also arranging internships for the course participants following the seminar. Most of the internships will be with the representative organizations of the EMAC, or within the SEC. Between 65 and 70 participants are expected.

Since the demand for internships and technical assistance is high, the SEC will need to determine where to place its limited resources and how to handle the level of technical assistance requested.

I. THE INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS

1. History and Purpose

IOSCO held its first conference in 1974 and has held annual conferences every year. IOSCO is a successor organization to the Interamerican Association of Securities Commissions. The purpose of the group is threefold: to cooperate on regulatory matters both domestically and internationally to maintain just and efficient markets, to establish standards and effective surveillance of international securities transactions, and to provide assistance to ensure the integrity of markets through application of enforcement measures.

2. Program Description

IOSCO is an international regulatory body with membership from major securities regulators. Affiliate members consist of international organizations and several self-regulating exchanges. The organization is comprised of several committees and working groups that meet to study issues and make recommendations. Three regional committees have also been established - the Interamerican Regional Committee, the European Regional Committee and the Asia-Pacific Regional Committee.

The Technical Committee was formed in 1987 and has since set up working groups to review regulatory problems related to international securities transactions. Areas of review include:

- problems with equity offerings on a multinational basis and multiple listings.
- international accounting standards.
- capital adequacy requirements.
- problems between securities and futures regulators
- regulatory problems from off-market trading
- international clearing and settlement problems

The Market Development committee meets twice year and has as its objective the development of emerging securities markets.

Each year workpapers are published on the research results and policy recommendations of the Committees and Working Groups.

3. Organization, Budget and Staffing

IOSCO is headquartered in Montreal, Canada. It has an administrative budget of $65,000 per year (1988). It is run by a Secretary General, Mr. Paul Guy.

4. Accomplishments to Date

The organization held its 15th and most recent conference in Santiago, Chile in November 1990. The increase in membership over the last year attests to the increasing visibility of the organization. Although the organization has achieved a high level of cooperation amongst its members and has delivered a very large volume of studies, one difficulty faced by IOSCO is that is has no authority to implement its recommendations.

J. THE BASLE COMMITTEE ON BANKING SUPERVISION

1. History and Purpose

The Basle Committee was established at the end of 1974 by the central bank Governors of the Group of Ten industrialized countries (Belgium, Canada, France, Germany, Italy, Japan, Netherlands, Sweden, Switzerland, United Kingdom, and Luxembourg) with the objective of strengthening collaboration among national authorities in their prudential supervision of international banking. The Committee's activities are conducted under the auspices of the Bank for International Settlements in Basle, Switzerland. Previously, the committee was known as the Basle Committee on Banking Regulations and Supervisory Practices and known informally as the "Cooke Committee" after its Chairman, Peter Cooke, from the Bank of England.

A continuing theme of the work undertaken by the Committee is the need to strengthen banking supervision in the context of continuing deregulation in financial markets. Also, the financial liberalization of Eastern Europe, and its accompanying needs for regulation are of great interest to the committee.

2. Program Description

The Basle group meets four times a year, normally at the Bank for International Settlements. The committee issues a report twice a year to coincide with the International Conference of Bank Supervisors (ICBS).

Issues under review and discussion relevant to developing countries include the following:

- Assessment of bank credit risk resulting from the Third World Debt Crisis and the development of standards for the provisioning of reserves for losses.

- Closer coordination between banking regulators and securities regulators in order to monitor against risks and to minimize the extent to which regulation distorts the opportunity for fair competition.

- Liaison and relationships with other groups of bank supervisors including the Offshore Group of Banking Supervisors, the GCC Arab States group, the Latin American and Caribbean Commission, the SEANZA group, the Caribbean Supervisors; Group and an initial meeting of African supervisors.

- Close collaboration with the IMF and World Bank on assistance and guidance for Eastern Europe. Consideration of the possibility of setting up a group of supervisors for Eastern European countries.

The Committee offers a one-week course on bank supervision at the Bank for International Settlements.

3. Organization, Budget and Staffing

Mr. Huib Muller, Executive Director of De Nederlandsche Bank N.V. succeeded Mr Peter Cooke as Chairman of the Committee on October 1990. The Secretary of the Committee is Mr. P.C. Hayward, Monetary and Economic Department at the Bank for International Settlements.

The United States Government participates in the Basle Group through the participation of the Federal Reserve Board, the Office of the Comptroller of the Currency, and the United States Treasury Department.

4. Accomplishments to Date

The International Conference of Bank Supervisors has been held six times since 1988. Its most recent meeting was in Frankfurt in October 1990.

To date its major accomplishment has been an accord, reached in July 1988, on international standards for risk-based capital adequacy for banks in its member countries. Target capital levels of an 8% minimum will come into full force at the end of 1992.

Recently officials from IOSCO (International Organization of Securities Commission) were invited to attend the Basle Group meetings and Basle group representatives attended the most recent IOSCO Conference in Santiago, Chile in November 1990.

The group offered its first course in 1987 and its second in November 1989 which was attended by banking authorities from 32 countries.

5. Future Plans

Issues of concern and issues to be reviewed in the future include coping with market risk, issues of bank liquidity, supervision of financial conglomerates, participation in the Joint Task force of the Basle Committee and the International Auditing Practices Committee, and work towards greater compatibility in worldwide accounting standards.

The week long course is expected to be offered annually.

Annex Three LIST OF PERSONS CONTACTED/INTERVIEWED

SEC	Joe Mari, International Division Lise Lustgarten, International Division Susan Nash, International Division Brent Taylor, Int'l Corporate Finance Melissa Guevara, Training Institute
OPIC	Graham Williams, Finance Department Julie Martin, Insurance Department
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IFC	Rudolf van der Bijl, Capital Markets Christopher Goss, Corporate Advisory Services
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Federal Reserve System	Sarkis Yoghourtdjian, Bank Super.& Reg. Charles Siegman, International Finance William Ryback, Bank Supervison & Reg. Don DeSoto,Bank Supervision & Reg. Hang-Shen-Cheng, Fed. Reserve SF Martha Scanlon, Federal Reserve Board
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