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World faces 'reversal' of global trade as populism wrecks deals

By Elliot Wilson, Lucien Chauvin and Thierry Ogier

Hopes of a jumbo trade partnership to kickstart the misfiring global economy were fading yesterday at the annual meetings of the IMF. A body of experts and officials told *Emerging Markets* that the sudden rise in anti-globalisation and populism were to blame for wrecking the prospects of big, intercontinental deals being

signed this year.

In Asia, the 12-nation Trans-Pacific Partnership (TPP) is lumbering slowly toward an unclear endgame. In Europe, another US-led alliance, the Transatlantic Trade and Investment Partnership (TTIP), is frozen, very possibly for good. Negotiators are facing the real threat of years of work going down the drain.

Continued on page 34



Trump and Clinton: helping to turn the world against trade pacts

Japan fears grow as Mr Yen warns stimulus of Abenomics is wearing off

Exclusive

By Anthony Rowley

The positive impact of Japan's unconventional monetary policy is "tapering off", the country's former vice finance minister for international affairs Eisuke Sakakibara told *Emerging Markets*.

The man known as "Mr Yen" for his ability to influence the exchange rate in the 1990s, said that while Japan's Abenomics policies — the economic strategy of prime minister Shinzo Abe — had had a positive impact they were coming to their "final stage". "People are worried



Sakakibara: defends Kuroda

about what comes next," he said.

In an interview Sakakibara, who was *Continued on page 3*

Meirelles raises prospect of 2017 Brazil recovery

By Thierry Ogier

The beleaguered Brazilian economy will finally post growth by the end of this year, the country's finance minister claimed in an exclusive interview with *Emerging Markets*.

Henrique Meirelles said that Latin America's largest economy had started to "stabilise which means that the economy will start growing at the turn of the year.

"The economy is still going through *Continued on page 3*

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FINAL WORD Mark Carney

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OUT OF THE WOODS

Seen and heard in the corridors of the Annual Meetings

• **Full disclosure** Amber Rudd's plans to make businesses disclose their number of foreign workers have been variously mocked and panned. But one wag padding the halls this week in Washington spotted a silver lining to the British home secretary's cloudy judgement: "This could mean the Conservative party will have to disclose how many of its donors are foreign. As in," he said with a throaty chuckle, "foreign for tax reasons."

• **Dial 'M' for multilateral** These must be tough times for the IMF's internal communications ombudsman. Spotted in the fulcrum of the press office: a giant, old-fashioned beige telephone emblazoned with the mysterious designation of 'Concordia Apartments'. There it sits in splendid isolation, asking users to dial 9 for local calls and zero if the light is flashing. *OOTW* called the 202 number on the handle: Line disconnected!

• **Schäuble gets wiggly** At the landmark seminar of the day, CNN anchor Richard Quest prodded and poked his panel, seeking to elicit a dressing-down of Donald Trump, a man who would be America's first celebrity president. Finally, Germany's finance minister Wolfgang Schäuble succumbed. "I never thought we would see this kind of demagoguery return," he fumed, adding that Hitler was "defeated by a united Europe and a united West." Well, sort of. But kudos all the same.

• **Claws out** At the same panel, Schäuble was also asked whether he was tired of talking about Greece. He was indeed. They should pay their own way, he railed, adding that Europe's sovereign basket case "hadn't paid interest on its debt in years". He trailed off but not before adding, with a rumbly grumble: "And you can tell that to Stiglitz!" Clearly Nobel laureate Joseph S. had riled Wolfgang S. the wrong way by suggesting that Greece's bailout money had been siphoned back to Frankfurt all those years ago, to prop up Germany's lumpen old lenders. Miaow!

• **Take the midnight train** Power ballads, like mullets and pet rocks, may be a thing of the past, but Lord Stewart Wood of Anfield, high on life in the post-Brexit era, was keen to outlining the investability of a free, independent and shrunken UK. "Don't stop believing!" he told a rapt audience. "We're going on a journey!" Much to *OOTW*'s regret, the boisterous Baron refused to burst out into song — or even to bust out a Bonnie Tyler wig. Next time maybe.

• **Avian folly** Madagascar's glotally surnamed finance minister Gervais Rakotoarimanana, clearly keen to be seen to be down with the kids (under 7's), told a bewildered audience at the World Bank's human capital summit that his homeland was "probably best known to them as the home of that famous Pixar cartoon". The subdued ripple of laughter that trickled through the audience was perhaps due to the sinking realisation that the avian-rich movie was produced by DreamWorks. Doh!

• **Exit pursued by hacks** Argentina is clearly taking its fiscal responsibilities painfully seriously. While chatting over a breakfast of stewed coffee and clammy eggs at our down-at-heel hotel, the full *Emerging Markets* editorial team bumped into Buenos Aires' economy minister Alfonso Prat-Gay. Swatting away a flurry of requests for interviews, he settled down for his own clammy eggs. Surely it's time for Argentina to do another bond, with the proceeds to be used to pay for a better hotel so that P-G can escape our pack of hounding hacks and eat his breakfast in peace.

Obor \$1.8tr debt pile raises bad debt fears in China

By Elliot Wilson

Bankers in Beijing are fretting about the sheer quantity of bad loans they may have to absorb as China pushes ahead with its mammoth 'One Belt, One Road' (Obor) policy, which is set to stretch overland from the Pacific Ocean to Europe, taking in Pakistan, Iran, the Middle East, Russia, the Gulf states and Central Asia.

One senior official at a Beijing based state-run commercial bank said the big question was how much of the lender's loans to projects in regions such as Central and South Asia would go sour. "Look at Pakistan," the banker said in an off-the-record interview with *Emerging Markets*.

"[Beijing] is investing \$46bn there" as part of the China-Pakistan Economic Corridor (CPEC), which includes building a slew of new power plants, ports, coal mines and airports, as well as highways stretching from the Indian Ocean overland to western China. "Our big question is simple: should we book all of our loans to Pakistan as non-performing now, or just wait a few years until they do go bad — which they will."

Many in Beijing fear China's desire to economically dominate and de-dollarise Central Asia and many of the economies that border the country, from Pakistan to Myanmar to Mongolia, cloud its ability to think rationally about the value of the capital that domestic policy and commer-

cial banks are putting to work.

The Obor project is set to cost China up to \$1.8tr, including \$46bn pumped into CPEC and \$40bn being injected in tranches into the private equity-style Silk Road Fund. China has asked its biggest commercial banks, including Industrial and Commercial Bank of China and China Construction Bank, to channel \$1tr into Obor-related projects in the years to come, with the remaining \$800bn sluiced into the system from development lenders.

RERUN OF VENEZUELA?

Bankers point to the headaches the country has endured over Venezuela. Since 2007, two policy lenders, China Development Bank and Export-Import Bank of China, have lent \$65bn to the failing Latin American state. CDB, insiders say, is now faced with the challenge of booking more than 90% of its entire lending to Venezuela as "failed" or "special mention" loans, and bankers in Beijing fear the same will happen with Pakistan. "All it takes is a military takeover in Pakistan, a return to the unrest we saw in past years, more problems in Balochistan, and all of our loans to Pakistan could fail."

Kevin Gallagher, co-director of the Global Economic Governance Initiative at Boston University, said China had underestimated the complexity and cost of Obor: "They are stretching themselves too thin," he said. "China is realising it is



The Taldyk Pass: \$14bn coming through

going to have to bear a lot if not all of the risks on its own, as it is finding it all but impossible to convince other governments to help to finance these projects."

The Asian Infrastructure Investment Bank, the new Beijing-based multilateral, will help spread and reduce some of the overall financial risk and stress. But Gallagher said China's investment plans were predicated on the assumption that the world's second largest economy would not suffer a fresh banking crisis or economic hard landing. "If there's another crisis, the central bank would be forced to clean up banks' balance sheets again. And if that happens, you're going to see a lot of this [Obor-related project] financing being repurposed to rescue the homeland."

Call for \$200bn development fund as Kim u-turns on capital increase

By Phil Thornton

Donor countries face the prospect of a multi-billion dollar cash call by the World Bank and its regional development banks yesterday after a report co-authored by former Treasury Secretary Larry Summers called for a fourfold increase in funds.

The report, by the respected Center for Global Development (CGDev), calls for a quadrupling to \$200bn of the \$50bn in infrastructure investment funded by the World Bank and sister regional institutions such as the Asian Development Bank in order to underpin an acceleration in potential economic output.

It called for a focus on what it called a well defined set of global public goods where the multilateral development banks (MDBs) and particularly the World Bank should be contributing given their "sectoral and financial capabilities" — climate change, agriculture, health and development data.

Its recommendations also included \$10bn for research and deployment of new energy and health technologies, to foster the nascent green bonds market, and to issue loans and guarantees on terms that encouraged borrowers to take on the upfront costs of climate mitigation.

It also called on the Bank to maintain its concessional lending — loans to the

world's poorest countries — at recent high levels of \$25bn a year.

However, the current level of lending which hit \$29bn in the latest financial year is prompting speculation that the Bank will need to come to shareholders for a capital increase.

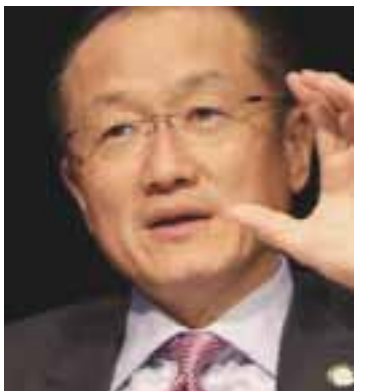
'OPENNESS' TO EXTRA CASH

Bank president Jim Yong Kim yesterday added to speculation when he said that the Bank was "being asked to step up in many areas that we have not traditionally been involved in".

"Climate change was not a traditional area of work for us. Forced displacement was not a traditional area of work for us," he said. "If you expand the agenda like that and then, at the same time also have increasing demands for the traditional things that we've been doing, it's hard to see how we're going to meet all those demands without a capital increase."

He said there was "much more openness" to a capital increase, in a sign that he has approached shareholders. "So we'll make the case and then just as my election was up to the governors the capital increase will be up to the governors," he said.

The move appeared to take Bank insiders by surprise. A year ago Kim told *Emerging Markets* that the lender would have enough resources to cope with a surge in demand for loans in the wake of



Kim: Stepping up

the economic slowdown without going back to its shareholders.

The impact of the CGDev report was partially diluted by a dissenting opinion by panel member Ray Offenheiser, the president of Oxfam America, who criticised the report for tackling the impact of the widening inequality.

"I would continue to argue that the overarching mission and mandate of the World Bank (and other MDBs) must remain the fight to eliminate extreme poverty," he said.

A World Bank spokesperson said: "The report rightly acknowledges the crucial role of multilateral development banks (MDBs) to development. In fact, the World Bank Group is already working in key areas referenced in the report, including stepping up its response to multiple global crises and shocks — including climate change — and leveraging the private sector in development."

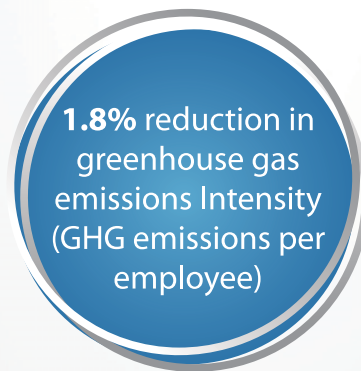
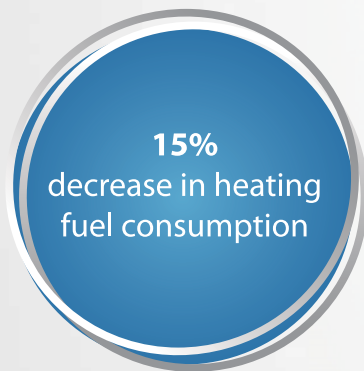
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Success is a journey

'Don't get left behind' says Roome on shift to green

By Elliot Wilson

Commercial banks and institutional investors who fail to switch their investment focus and to prepare for a greener-and-cleaner world risk being left behind by their peers, the World Bank's head of climate change has warned.

John Roome, senior director for climate change at the multilateral, said there has been a "sea-change" over the past year, as a cluster of financial institutions, from Danish and Canadian pension funds to Spanish lenders and even cumbersome Chinese state banks looking to eliminate some of the more carbon-intensive operations and assets from their books. "Banks need to begin to shift the balance of their investment into greener sectors," Roome told *Emerging Markets*. "Banks with greener portfolios are getting better investment rates of return than those without."

He added that the next step-change would happen when banks are forced, under international rules and norms likely to be inculcated in the years ahead, to disclose how much of their assets are invested in 'dirty' or 'non-green' assets. "The G20 group of nations and the Financial Stability Board talk about voluntary disclosure, but the real change will come when we can take the next step, toward mandatory disclosure," he said. "Banks should be revealing how much of their balance sheets are invested in carbon-intensive assets. The savviest banks and investors know they are at risk in the long-term if they don't disclose this kind of detail."

Roome insisted that the push to transform climate change into an asset class in its own right — bringing borrowers together with investors seeking higher returns on clean projects, many in the emerging world — is gaining momentum. "Nigeria and Morocco are both looking to issue sovereign green bonds" in the months ahead," the World Bank's climate change supremo said. "The drive is coming from the highest level of government and state in both those countries. Morocco will host the COP22 climate change conference in Marrakech in early November, the event starting a few days after the Paris climate deal, which has now been ratified by 73 nations accounting for 57% of all global greenhouse gas emissions, is activated.

Roome said the next stage for governments would be to move from the abstract — agreeing to COP21 and COP22 accords — to the practical. That will mean convincing their ministries to work together to generate new 'green' investment bonds, funds, loan and credit facilities, and major infrastructure projects, which will attract and drag in capital from leading institutional investors and lenders. "Some governments, such as Côte d'Ivoire, Ethiopia, and Morocco, are already doing this," he said. "Their finance and planning ministries are working in harmony to bring it all together. The next aim will be to mainstream these processes", ensuring that it becomes common practice at state level.

Capital is coming, says Egypt's finance minister El Garhy

By Virginia Furness

Egypt's ailing economy is on the cusp of a \$12bn IMF programme that could help mobilise \$10bn-\$15bn of much needed foreign investment into the country, the country's finance minister, Amr El Garhy, told *Emerging Markets* on Thursday.

El Garhy, a former investment banker who took office in May this year, is the eighth person to take up the role since the Egyptian revolution in January 2011. He has inherited an unstable regime facing enormous challenges, and diabolical metrics. Egypt has crippling twin deficits and indebtedness has risen to close to 100% of GDP. Low growth of 1.5%-2% and rapid inflation have done little to improve the situation.

But Egypt is on the verge of an agreement with the IMF which would unlock access to not only a \$12bn Extended Fund Facility, but also some \$10bn-\$15bn of foreign direct investment, not including investment from the oil and gas sector. While El Garhy expects this over a period of two to three years he acknowledges that an IMF agreement will not provide instant access to fast cash, nor a solution to all Egypt's problems, though he does see it as an important endorsement of the health of the economy. "These things take time," he said, noting the importance of fiscal and

structural reform.

Egypt is also at the "advanced stages" of Eurobond issuance and is planning to be out with a new deal of \$2.5bn-\$3bn before the end of the month. El Garhy is conscious to avoid a clash with the US elections though is seemingly ambivalent about the result. "I'm open to dealing with any regime, we've had good relations with the US," he said.

El Garhy wants to kickstart the economy into functioning at a "full steam growth rate of 5%-8%". He aims to reduce the budget deficit to 10% in 2016-2017 which he hopes will be revised down to 8% in the next three to five years, and to reduce debt to GDP to 80%. But a consistently high level of government expenditure has weighed on public investment. "We're a very diversified economy and our potential is huge," he said. "But our challenges are enormous. In recent years government spending has been very rigid."

Fiscal reform is coming in the form of a five year plan to gradually increase VAT, reducing wages which currently make up 28% of the budget. While subsidy cuts are on the agenda, El Garhy wants to make sure they are made in the right places and will retain food subsidies for the poor.

TOURISM HIT

Depleted tourist numbers have hit



El-Garhy: not worried about Trump

Egypt's economy hard, but El Garhy thinks that Egypt is being unfairly punished. "What happened was a tragic accident, and other countries have them too," he said. "We don't have security issues, people talk about factions of extremists but they are very small. We will be pushing tourism very hard."

Regardless, El Garhy has work to do to convince those foreign businesses deterred by what they see as elevated security risks.

Along with tourism, El Garhy is focusing on industrial growth, energy, food exports and capital markets development to stimulate growth. He also plans to sell several state owned assets and is in talks about the sale of a bank, and use the capital markets as a catalyst to bring investment.

Caribbean warns of de-risking crisis as Michael wreaks hurricane havoc

By Olly West

Some Caribbean countries fear they could soon be left without correspondent banking relations, with potentially disastrous economic effects.

Despite all 27 Caribbean nations complying with CFATF (Caribbean Financial Action Task Force), international banks are withdrawing their correspondent banking relationships across the region. This is largely due to banks having to comply with more rigorous anti-money laundering (AML) and counter financing terrorism (CFT) regulation.

As the Caribbean deals with the aftermath of Hurricane Matthew, which has killed at least 35 people and destroyed swathes of infrastructure, Haiti's central bank governor said he "did not want to imagine" what would be of his country without correspondent banks.

"In economic terms, Matthew will be worse than the 2010 earthquake (in which at least 100,000 people died)," Jean Baden Dubois, governor of Banque de la République d'Haiti, told *Emerging Markets*. "The destruction of infrastructure and agriculture is terrible, and in the few days there will be shortages of agricultural products.

"Fortunately we still have the correspondent banks. If we did not we would be in deep, deep trouble."

Although the Caribbean is working hard to find solutions, and is working closely with the US Treasury, there is "a real risk" that the remaining correspondent banks will leave, said the governor.

"We are a small country," he said. "The size of business for these banks is too small versus the risk of a million dollar fine should even \$100 of the money they are transmitting be found to be related to terrorism or money-laundering."

Remittances from Haitians living abroad account for around 20% of the country's GDP, but three of the six institutions with correspondent banking relationships in Haiti have withdrawn from the country. Of the remaining three, one has no letters of credit or cheque clearing business, effectively leaving two banks, said the governor.

The situation could have grave consequences for the country's trade balance: it imports around \$4bn of goods per year but exports just \$1bn.

"We have a \$3bn gap to fill, and it is partially filled by \$2.2bn of remittances from abroad," said the governor. "If we cannot receive remittances the macro-economic impact would be huge."

Remittances are playing an increasingly important role in Haiti, as foreign



Destruction in Haiti

aid has dropped from \$1.5bn in 2010 to just \$500m.

"People in Haiti are not receiving money for luxuries; it is for real needs. So they will continue to send money — only outside the banking system."

This could be an "unintended consequence" of AML/CFT regulation, said Therese Turner-Jones, general manager of the Caribbean Country Department at the IADB.

The withdrawal of correspondent banking relationships could gravely set back progress in financial inclusion.

"We cannot lose sight of what is at stake here," said Turner-Jones. "We are concerned about disintermediation, lack of economic growth because of constraints in the financial sector, and savings not being intermediated properly to investment."

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A BANK TO TRUST

Alarm as Britain's May wades in on monetary policy direction

By Jon Hay and Graham Bippart

The UK government has lent its voice to the growing current of international opinion that expansive monetary policy has gone far enough, and may even be harming growth. Britain is set to embark on a fiscal stimulus, likely to be welcomed by financial markets.

The strongest remarks came from Theresa May, UK prime minister, in her key address to the Conservative Party conference on Wednesday. She even appeared to indicate that UK monetary policy was about to change — despite monetary policy being the domain of the Bank of England.

While many financial specialists would welcome a more proactive fiscal policy, most would be alarmed by any suggestion of politicians gaining more influence over monetary policy.

May said “monetary policy — with super-low interest rates and quantitative easing — provided the necessary emergency medicine after the financial crash”. But she added that it had had “bad side effects”.

Rather than reaffirm the Bank of England's right to set monetary policy, she said: “A change has got to come. And we are going to deliver it. Because that's what a Conservative government can do.”

As speculation rose of a radical shift in policy, the government rushed to quell

talk it would remove the bank's independence. George Freeman, chair of the prime minister's policy board said May was expressing unhappiness with previous Chancellor George Osborne's reliance on monetary policy. He said she supported Bank independence on monetary policy.

POTSHOTS AT BANKS

Politicians around the world have become much readier to criticise central banks since the financial crisis, when they moved into unconventional measures that have had profound effects on financial flows, with consequences for the wealth of different economic groups.

In the US Congress, where acts in 1977 and 1978 gave the Federal Reserve de facto control of monetary policy, there have been moves in the past two years to ‘Audit the Fed’. This means imposing closer Congressional scrutiny, which Fed chair Janet Yellen has said would “bring short term political pressures to bear” on the Fed and “politicise monetary policy”.

“I doubt very much that the Bank of England would have its independence taken away by this Conservative government,” said Kallum Pickering, senior UK economist at Berenberg in London. “There is a host of academic research which supports monetary independence. Monetary policy is conducted much better by independent central bankers than by [government] policy



May: ‘bad side effects’ of monetary policy

makers. Among modern, highly developed economies with large financial systems, Britain would certainly be an outlier if it took away the Bank's independence. It would be a real step backwards in terms of taking a modern approach to monetary policy.”

INDEPENDENCE VITAL

Stanley Fischer, vice-chairman of the Fed, used a speech in November 2015 to argue that monetary policy independence “remains of the highest importance” after the financial crisis, when central banks' focus had shifted somewhat from controlling inflation to preserving financial stability. He also emphasised that all major independent central banks are subject to political accountability regimes.

If the Bank of England's independence is safe for now, the UK government clearly believes government action is needed to power growth.

World Bank: Western bond market can learn from China

By Craig McGlashan and Toby Fildes

The World Bank prides itself on bringing best practice to capital markets across the globe, but when it became the first issuer to sell a bond denominated in special drawing rights (SDR) in the onshore Chinese renminbi market it observed an approach to best practice in bond issuance that “others can emulate”, Arunma Oteh, treasurer of the World Bank, told *Emerging Markets*.

“One example is that in Western markets, bookbuilding is essentially done by the bookrunners,” she said. “But China has the Beijing Financial Assets Exchange, which does the bookbuilding. This is an independent entity. I was fascinated when I visited it because the bookbuilding happens in a room that you can see what is going on and you can see as the orders come in. It's a very transparent process.”

“Such approaches can further boost the confidence of investors. For me, it's an example of the role that we play in bringing best practice to a market, but also the role we play in showing that a market is potentially one that people should look at.”

World Bank sold the SDR500m (c. \$700m equivalent) 0.49% three year bond — which makes payments in ren-

minbi — in late August, just one month before the IMF added renminbi to the SDR basket on October 1.

So far, no other borrowers have followed, but Oteh is hopeful that the World Bank's initiative will be picked up by others in the market.

“Since our SDR500m issuance, we've had issuers that are looking at the same market ask us about how did we do it,” she said. “It's also of course an opportunity for the Chinese financial sector to diversify its options in terms of what it invests in.”

BUILDING BLOCKS

But further ahead, the opportunities offered by blockchain — effectively a distributed database of a series of financial transactions — could be adopted in several areas of finance, helping to restore trust in a financial system still viewed with suspicion by many since the crisis of 2008, according to Oteh.

“I'm fascinated by the developments in fintech,” she said. “I've been very anxious that the global financial crisis broke trust in ways that have been difficult for the financial sector to rebuild.”

“My perception is that blockchain could help rebuild that trust. It's a real area of opportunity. It has potential for



Oteh: ‘very transparent process’

managing identity, having an audit trail — it will improve efficiency and broaden opportunities.”

Oteh's view appears to be supported by the government of Dubai, which this week announced plans to become paperless by 2020 — by moving all transactions to a blockchain database.

Aside from the financial benefits, the Dubai government is also hopeful that the cutback in paper usage will have environmental benefits.

Other initiatives to harness the possibilities of blockchain are already underway in a variety of other areas.

In late September, Credit Suisse and technology companies Ipreo, Symbiont and R3 announced they had finished the first stage of a project to showcase how blockchain can improve settlement times for syndicated loans.

Reform while you can, says World Bank's Familiar

By Lucien Chauvin

Slower growth in Latin America could actually have a silver lining, getting countries to move on the reforms they delayed during the commodity boom at the start of the decade, according to the World Bank's vice president for Latin America.

“The good thing about not-so-good times is that it is easier to reform,” Jorge Familiar told *Emerging Markets*.

He said that the region has two primary ways to deal with the economic slowdown, adjusting and borrowing, because the “conditions we are seeing today are not temporary or short term. This is going to be with us for a while, and therefore there is a need to adapt and adjust.”

Nearly all of the countries in the region are forecast to grow in 2017, after two years of recession. The only country that will not grow is Venezuela, which is expected to see a GDP decline of 2.6% in 2017. While bad, it is better than the 10% expected for this year.

Familiar said that unlike the past, countries have room to work through reform. “The other thing that has changed is that unlike the past this is not a situation to call in the firemen,” he said.

LINKING UP REFORMS

He said a critical change in the region was linking up reforms in three major areas, including attracting private investment through public-private partnerships, investment to close the huge infrastructure gap and working on regional integration.

Spain's BBVA estimated in late 2015 that Latin America's infrastructure gap was just shy of \$300bn. The World Bank and other multilaterals are working on new facilities to provide resources, with the focus on the private sector.

The big push is for public-private partnerships (PPPs). Peru is currently reforming its PPP process and Chile is a world leader in crafting mechanisms for working with unsolicited project proposals. Other countries are reducing the need for state-owned firms to have a share in projects, with the Brazil Congress taking the first step on October 6 to eliminate a requirement that its state-owned oil company, Petrobras, have a 30% share in oil/gas blocks.

Familiar said Latin American countries were also looking at infrastructure as it relates to building regional trade integration. “We do not see a region or a world going in the right direction without trade, the conditions that create more opportunities, more jobs and poverty reduction,” he said.

The Inter-American Development stresses the same approach, with its president, Luis Alberto Moreno, highlighting the construction of transport infrastructure connecting Argentina's San Juan province with northern Chile, proving Argentina with another Pacific coast access.

“This physical integration is fundamental. We need to focus on the possibilities of trade that we have not taken advantage of in Latin America,” said Moreno.

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Deutsche Börse clears path for Chinese M&A finance with 'D-Share' market

By Owen Sanderson

Ceinex, Deutsche Börse's joint venture with the Shanghai Stock Exchange and the China Financial Futures Exchange, plans to launch a market in German-listed shares of Chinese companies in 2017, with the first issue planned for the second quarter, and potentially more than 10 listings in the first year. The market is supposed to support Chinese firms funding foreign acquisitions with new equities.

The "D-shares" will be documented in English, listed in Frankfurt and, crucially, match up to German standards of disclosure and transparency — a feature which has slowed down some previous attempts to encourage more Chinese firms to raise equity offshore.

However, they will be governed by Chinese company law. Both German and Chinese regulators will have to approve listings. The share class will support various listing types, according to Deutsche Börse, such as initial public offerings in Frankfurt alone and dual-class simultaneous issuance of A-shares (China-listed onshore RMB) and the new D-shares.

Ceinex is working on a feasibility study for the scheme at the moment, but the results are encouraging, according

to sources within Deutsche Börse.

This year has seen the largest ever Chinese outbound acquisition, the \$43bn bid for Syngenta from ChemChina. But the financing for the deal illustrates why issues of disclosure and security are so crucial. Initially, the deal was structured with an international section, secured by the Syngenta part of the business, and non-recourse to ChemChina, with a China-focused loan alongside it.

At first, international lenders focused their attention on the European non-recourse financing, though many eventually came into Asian syndication as well — but later, on with more intensive credit work.

CAPITAL CONTROLS

Most important to the development of the market is how far China continues easing its capital controls.

In theory, firms are permitted to take funds out of China to pursue foreign acquisitions — it's only investors who are restricted in deploying their capital — but this needs to be approved by foreign exchange regulators, adding another hurdle in arranging finance and bidding for companies.

In practice, this means only the largest



D-share coming soon

firms have ready access to large volumes of foreign exchange, or the kind of banking group that ChemChina has assembled.

Ceinex is therefore targeting mid-sized firms, rather than ChemChina-style megadeals, and plans to source listings through the existing networks and reputation of Deutsche Börse's joint venture partners the Shanghai Stock Exchange and China Financial Futures Exchange. The project also has the support of the Chinese government.

According to Deutsche Börse, there are already 180 "China co-operation products" trading in Frankfurt, though the D-shares have yet to launch. These are 145 China-related bonds and 35 China-related ETFs already listed.

Although the project is launching soon, if China's liberalisation of its capital account proceeds faster than expected, this could also scupper the project — there's no need to raise offshore equity if it's easy to take funds out of the country.

Mozambique on the brink despite IMF agreement

By Virginia Furness

Some donors may never return to Mozambique, according to well-placed sources who warned that investor optimism over last week's landmark deal that saw it finally agree to an independent audit of its debt was misplaced.

The country's sovereign bonds jumped 12 cash points on news of the audit, which was the first positive step in a long story that saw the International Monetary Fund cancel a mission to Mozambique, and *de facto* suspend funding to the embattled country in April after some \$1.4bn of hidden loans, amounting to 11% of GDP, were discovered via a debt exchange programme.

This pushed debt levels up to 86% of GDP. Other international donors such as the World Bank, EU and Canada also suspended funding.

On September 29, the IMF issued a statement confirming that the Government of Mozambique was ready to progress with an international and independent audit of the Ematum, Proindicus, and Mozambique Asset Management (MAM) companies with the objective of strengthening transparency, governance and accountability to avoid recurrence of past debt problems.

The IMF is now choosing a large international firm to carry out the forensic audit, but even after the decision is made, the process will not be a quick or easy one.

In addition, several international donors such as Denmark have made clear their intention not to resume funding to Mozambique under any circumstance. Denmark is understood to be closing its embassy in Maputo.

Progress on the audit would prompt the IMF to resume discussions with, and possibly funding to, Mozambique but there is no telling how long that would take.

OPTIMISM 'UNFOUNDED'

The country's bondholders celebrated "progress at last" by piling into Mozambique's only outstanding Eurobond, a repackaged \$727m Government of Mozambique 2023 bond, the cash price of which jumped some 12 points to 83 from 72 in June. But a source told *Emerging Markets* that the optimism was unfounded, saying that it was too early to tell how the situation would play out.

Mozambique's Eurobond has a \$38m coupon due on January 18 which the coun-



Ematum: boats in dock, Maputo

try's FX reserves could cover, but would make a sizeable dent in those reserves. Mozambique has also reached stalemate over a missed coupon payment on the \$535m loan to MAM. A default could lead to a cross-acceleration default on the country's Eurobond. The original loan was issued by VTB who has since passed on the loan to other creditors.

The UK's Financial Conduct Authority is understood to be investigating VTB and Credit Suisse for their involvement in the loans — both banks worked on the Eurobond exchange earlier this year.

"Overall there is likely to be very little support to Mozambique this year," the source said. "External financing is a key element of the budget. They're going to have to adopt a very tight fiscal position well into 2017." Despite repeated requests by *Emerging Markets*, no one from the government was available for comment.

Paraguay to become a new 'little China' of South America, say ministers

By Thierry Ogier

Paraguay has launched a charm offensive in Washington to present its small but fast growing economy as the "little China" of South America.

"This is exactly what we think, and this is why we see so many large companies moving to Paraguay," Lea Gimenez, deputy economy and integration minister of Paraguay, told *Emerging Markets*.

Paraguay officials have argued that the country could produce 10% of the \$70bn that Brazil imports from China annually. This would in turn help Paraguay diversify its commodity-based economy. "[Paraguay] could be very well a province of China," said Santiago Peña, Paraguay's finance minister, also speaking to *Emerging Markets*.

Companies in Brazil, Paraguay's big neighbour and the largest economy in the region, have started relocating some plants there in search of lower tax and cheap labour. This is also intended to substitute some Chinese imports by goods made in Paraguay. "It almost seems like the Brazilian investors realise what a jewel they have next to them. Paraguay offers them a young labour force, low tax rates and cheap and clean energy. This is an irresistible offer and we are next to them," she said.

Paraguay has experienced growth since Horacio Cartes was elected president in 2013. He appointed a group of young US-trained economists who have implemented orthodox policies.

Car part manufacturers, such as Fujikura, were the first to move some plants from Brazil to Paraguay three years ago. Now, some 80 industries have moved over there, according to Gimenez. In recent weeks, the Brazilian toy company Estrela announced that it was investing in a Paraguayan plant to cut its imports from China. "We are cutting jobs in China and employing Paraguayans instead," said Carlos Tilkian, the CEO of Estrela.

The textile manufacturer Guararapes, which opened a plant last year in Paraguay, now intends to double its capacity. JBS, one of the world's largest meat packers, has recently opened its fourth plant in Paraguay. "You will continue to see those companies moving to Paraguay. This goes beyond the macroeconomic stability that we have been offering in the past 15 years," Gimenez said.

"We have to be a bit more forward looking and show Paraguay as a hub of production for the whole of the southern cone [of South America]," Carlos Fernandez, Paraguay's central bank governor, told *EM*.

Paraguay has been growing steadily in spite of the collapse of commodity prices that affected its soy and meat export revenues, and also in spite of the recession in Brazil and Argentina. The Paraguayan central bank is currently revising its GDP forecast from 3.5% to 4% this year. If this is confirmed, this could be the highest growth rate in South America.

Lagarde looks to use second term to take IMF into new waters

Christine Lagarde took the helm of the IMF as it was facing its toughest challenge in the wake of the global financial crisis and the eurozone debt trauma. In an exclusive interview with *Emerging Markets*, she sets out her agenda for her new five year term and gives her views on everything from Europe's banking problems to Brexit

Exclusive

By Anthony Rowley

In a world of constant turmoil and change for both economic managers and political leaders, Christine Lagarde stands out as a symbol of calm and stability. Earlier this year she was approved unanimously to take on a second five year term after her first tenure expired in July.

She came in after a period of damaging instability for the Fund that saw her predecessor Dominique Strauss-Kahn resign in 2011 after four years following allegations of sexual assault and Rodrigo Rato step down two years early in 2007 for personal reasons.

So what does she regard as the biggest successes during her first term in office, and what does she hope to achieve during her second term? "I think during my first five years we have consolidated the [IMF] financially, we are much more solid than we were with resources that have been increased significantly," she says, in an exclusive interview with *Emerging Markets*.

"I think it is also more representative of the international community and as a result better accepted. What I hope we can achieve in the next five years is certainly building from that strength. I have the ambition to continue working on issues such as inequality, climate change, gender, corruption, the input of technology and its impact on the economy."

The state of the economy has been the primary issue at the annual meetings after the IMF issued a decidedly gloomy World Economic Outlook that forecast growth of close to 3% this year, and 3.4% next.

She says that zero or negative interest rates are "transforming the paradigm in which banks are operating. Monetary policy "is being stretched thin," she warns.

"If [this situation] lasts for a long time it is going to question the current business model not only of banks but also of insurance companies and pension funds. This is a very substantial issue."

BANKING PROBLEMS

She stresses the need for banking problems in Europe especially to be "managed" effectively, urging a more aggressive approach to dealing with European banking problems, which she says have "systemic" implications in one case.

"A lot of good things have been done in the financial sector in terms of improved regulatory environment, improved supervision, better co-operation between regulators and supervisors," Lagarde notes.

"When we look at the banks there is clearly a stronger capital structure and more buffers. We have living wills in place and we have in many instances bailing-in mechanisms that have been framed. Those are the positives since the global financial crisis."

But, she says, "with interest rates at the zero lower bound or less than zero lower bound [that] is clearly transforming the paradigm in which banks are operating." The second factor which has changed is the development of the financial non-banking sector or shadow banking sector.

There are particular concerns in Europe, she notes. "Without disclosing anything, market trepidation around one Italian Bank, one German bank and questions around some of the more southern European countries' banking systems is clear evidence of that.

"This is not to say that all banks are in a difficult situation in Europe but some of them really need to be addressed.

"These institutions need to be managed because one of [them] is of systemic importance, and it is a very large institution — a complex one too. I think the authorities are aware that measures have to be taken. They are disposing of certain assets and considering disposing of further assets and strengthening the structure of the bank [concerned]."

The "big difference between the US and Europe," says Lagarde, "is that the US took very abrupt and heavy duty measures to fix the financial sector, to fix the banks back in 2009 and to deal with the non-performing loans and the lack of capital."

US authorities "went heavy" on reform "whereas the Europeans did not do that and did not deal with non-performing loans as promptly as the US and did not take [such] hard line measures. The financial sector, which was the big weakness of the financial crisis, was addressed head on and very promptly by US authorities whereas it was not the case in Europe. I think the Europeans are dragging things."

EUROPE OVERTAKES U.S.

On overall economic performance, however, there are positive indications, Lagarde observes. She strikes an optimistic note on economic growth prospects in the euro area.

"In our forecast for 2016 the US economy is growing at 1.6% whereas the euro area is forecast to grow at 1.7%. That goes a bit unnoticed because we usually assume that the US economy grows at least one percentage point higher than other advanced economies but in the case of 2016 this is certainly not. The US has slowed down quite significantly."

On the global economy, Lagarde notes that "the world is in an environment where everything that should be high is low — growth, inflation, interest rates and productivity. If we had more growth there would be more space for fiscal policy, debt reduction and reduction of inequality. Low growth is making all these things much more difficult.

"The urgency is for policymakers to actually 'get on



with it' and combine urgently the three policy [tools] that they have available — which are monetary, fiscal and structural reforms.

"My hope is that they would leave this week of annual meetings not thinking that we need global fiscal stimulus, as we did back in 2009 but I would like them to go away thinking 'there's something that I haven't done that I could do. Those who have been talking about structural reforms should not only talk about it but actually do it. If we just drive on, it will be just more difficult to extract ourselves from what I have called the 'new mediocre'."

BREXIT UNCERTAINTY

On globalisation, Ms Lagarde suggests that "what we are seeing at the moment is a reversal" of the process. "It is reversing the relatively free and unencumbered flow of goods and services on the basis of existing or international trade arrangements. There are populist voices around in various countries, and not just in the United States, calling for withdrawing behind borders, limiting the flow of goods and services[and] hindering the flow of people where people could move freely.

"I think it is less so on the movement of capital than it was because monetary policy is more predictable and has not moved violently, and we have not seen as much capital outflows and inflows than we had feared."

How much damage is Brexit likely to do to Britain and to the EU and to other key global economies, *Emerging Markets* asks. "We think it will have negative effects, probably on both — more so on the UK than on the European Union," Ms Lagarde responds.

"The time over which these effects will be produced is to be seen. It is good that there is now a triggering point in time when the Article 50 negotiations will start. When they will finish, we don't know. What will happen in between is uncertain. There are any unknowns." **EM**

EMERGING MARKETS

MANAGING EDITOR

Toby Fildes toby.fildes@globalcapital.com
+44 7580 154 001

ASSOCIATE EDITOR

Phil Thornton +1 469 901 2847

ON-SITE REPORTERS

Lucien Chauvin +1 469 901 2813
Paolo Danese +1 469 996 792
Virginia Furness +1 469 901 2967
Craig McGlashan + 469 901 2857
Thierry Ogier +1 469 901 2863
Anthony Rowley +1 469 901 2832
Owen Sanderson +1 469 901 2849
Oliver West +1 469 901 2860
Elliot Wilson +1 469 901 2868

CONTRIBUTORS

Lucy Fitzgeorge-Parker, Rashmi Kumar

PHOTOGRAPHER

Gerald Hayes +1 469 901 2883

VIDEO

Dave Lamb +1 469 9012 869

HEAD OF OPERATIONS

Sara Posnasky +1 469 954 0122

PRODUCTION EDITOR

Vicki Robinson

HEAD OF SPONSORED PROJECTS

Annabel Nason

SPECIAL PROJECTS EDITOR

Phil Moore

MANAGING DIRECTOR

John Orchard

DIRECTOR

Ruth Beddows ruth.beddows@globalcapital.com
+44 20 7779 7386

PUBLISHER

Oliver Hawkins oliverhawkins@globalcapital.com
+44 20 7779 7304

DEPUTY PUBLISHER

James Andrews james.andrews@globalcapital.com
+44 20 7779 8074

ASSOCIATE PUBLISHER

Henry Krzymuski henrykrzymuski@globalcapital.com
+44 (0)20 7779 7303

ASSOCIATE PUBLISHER

Melissa Roach mroach@globalcapital.com
+44 (0)20 7779 8276

AMERICAS PUBLISHER

Kevin Dougherty +1 646-629-6355

LATIN AMERICA PUBLISHER

Soledad Contreras M: +44 (0) 7408 865 672

CENTRAL ASIA PUBLISHER,

Mine Hekimoglu +90 5324131686

PUBLISHER, MIDDLE EAST & TURKEY:

Adil Jilla of MEIAC ajilla@meiac-uk.com
ASSOC. PUB. MIDDLE EAST & TURKEY
Kaersi Jilla of MEIAC kjilla@meiac-uk.com
(UK: +44 (0) 797 384 310 (Dubai): +971 4 4548690
Shatha Tower, Office No. 1906, Media City PO Box.
502118, Dubai, UAE

FROM THE PUBLISHERS OF

GlobalCapital

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© Euromoney Institutional Investor PLC
GlobalMarkets/Emerging Markets is a
publication of Euromoney Institutional Investor PLC
8 Bouverie Street, London, EC4Y 8AX
Telephone: +44 (0)20 7779 8888

Directors: John Botts (non-executive Chairman),
Andrew Rashbass (CEO), Sir Patrick Sergeant, The
Viscount Rothermere, Colin Jones (Finance Director),
David Pritchard, Andrew Ballingal, Tristan Hillgarth,
Paul Zwillenberg

Washington DC office:

Crescent Room, One Washington Circle Hotel
1 Washington Circle, NW
Washington DC 20037

Hotel Front desk: (202) 872 1680

Printing by:

Stephenson Printing Inc.
5731 General Washington Dr.
Alexandria, VA 22312
Tel: 703 642 9000
stephensonprinting.com

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TRUE VALUE IS ACHIEVED WHEN QUALITY MEETS QUANTITY

BEST MANAGED
ADVISORY SERVICE

BEST BANKING GROUP
LEBANON

BEST INVESTMENT
BANK

BEST CALL CENTER

EXCELLENCE
IN TRADE FINANCE

BEST BROKER

SOCIAL
ECONOMIC AWARD

MOST BANK ADVERTISING
EFFECTIVE **CAMPAIGN**

BEST TRADE FINANCE
BANK AWARD



Best Broker
MedSecurities
2011, 2012, 2013, 2014,
and 2015



Best Investment
Bank Award
2009, 2010, 2011, 2012,
2013, 2015 and 2016



Best Trade Finance
Bank Award
2014, 2015
and 2016

Infrastructure provides right road to cutting poverty, says AIIB's Jin

Exclusive

In a wide ranging interview with *Emerging Markets*, AIIB chairman and president Jin Liqun explains his lending strategy after his first six months of operation and highlights the need for all multilateral institutions to focus more on infrastructure

By Anthony Rowley

With unconventional monetary policy approaching the limits of its effectiveness, fiscal spending on infrastructure is finding favour as a means to stimulate economic growth.

This has lent weight to the arguments of Asian Infrastructure Investment Bank (AIIB) chairman and president Jin Liqun in favour of such spending. "There is empirical evidence showing an undeniable link between infrastructure investment and economic growth," Jin tells *Emerging Markets*.

In a wide ranging interview he defends the AIIB's push to strengthen the focus of

multilateral development banks (MDBs) on infrastructure. The former vice finance minister of China argues that MDBs need to boost infrastructure investment rather than simply talk about a mission to reduce poverty.

There is a need for radical rethinking on this issue, says Jin, citing China's success with infrastructure-linked poverty reduction. The AIIB head notes that "largely owing to the broad benefits of improved infrastructure, China managed to lift over 500 million people out of poverty by World Bank standards, and 600 million by China's standards, in a little over two decades, with the percentage of the population living in poverty falling from 65% in 1981 to just 4% in 2007."

Emerging Markets talked to Jin as the AIIB — which has attracted 58 member countries from within and beyond Asia — entered the second half of its first year of operations and after he had presided over the bank's first annual meeting in Beijing.

A former Asian Development Bank vice-president and alternate governor for China at the World Bank, Jin has shown confidence and skill at the helm of the new Beijing-based bank, many say, raising his profile on the regional and international stage.

The bank has approved just half a dozen loans so far while its business plan for 2016 sees lending of \$1bn with a staff of around 50 people.

“I have a deep conviction that any poverty reduction programme in and of itself will not go very far in making a difference to the livelihood of the poor and the needy”

“There is often a huge gap between what is desired and what is practical”

While the AIIB has made a solid start to its endeavours, it will be a “lean” operation, says Jin, who has demonstrated this principle by dispensing with resident executive directors at the bank. However, he highlights the importance of the oversight exercised by the AIIB board, whose role he says is strong despite the bank’s different approach.

Use of modern technology “can ensure that our non-resident board has no less ready access to information about what is going on in the bank than if its members were here on the premises,” Jin says. “Physically, board members are scattered over the world. Functionally, they remain close to management and staff on a daily basis. This also allows us to save on costs, which ultimately benefits our shareholders.”

He insists that being lean does not stop at the non-residency of the board. “It means that, at its core, the bank will prioritise efficiency in all aspects of its business and operations. We are already seeing this implemented in various ways.

“We have delivered our first four projects barely six months into operation and we have adopted a measured approach to staffing, ensuring there is no [functional] redundancy. The AIIB will strive to remain a small organisation relative to the size of its operations. The lean structure will be institutionalised as part of the corporate culture.”

CORE REQUIREMENTS

It is not just in improved efficiency that the AIIB can make a difference, Jin suggests. China’s economy, he notes, “continues to get bigger and now it is China’s turn to do a bit for the rest of Asia and the world”. China can, for example, demonstrate to others the value of infrastructure investment. “China’s fast growth in virtually all sectors of the economy over the last three decades was preceded by infrastructure investment.”

But such investments can be effective only when they are well co-ordinated, he says. “A power plant once completed should not wait for the transmission lines to be built. Port upgrading and expansion should be supported by road and rail connections. Infrastructure will exert a greater impact if it is part of a regional development strategy. It is important to consider a project’s regional impact to ensure its long term viability.”

In order to ensure this, he says the AIIB sets three core requirements for projects on which it is approached for support. “They must be financially viable, environmentally friendly and socially sustainable.”

The types of infrastructure most likely to contribute to growth, Jin suggests, are “those that can create jobs, pave the path for private sector development and generate

tax revenues through increased economic activity. At the same time, they certainly should be good for the environment.

“If a region lacks transportation infrastructure, then roads, railways or ports are what is needed. If it lacks access to clean drinking water, then water treatment is the most crucial. If a region lacks access to power, then power transmission is the most pressing need.”

Jin challenges the popular orthodoxy that poverty reduction should be the “overarching goal” of development banks. “The real experience in much of Asia is that infrastructure construction has had a meaningful impact on improving the lives of ordinary people,” he emphasises.

“I have a deep conviction that any poverty reduction programme in and of itself will not go very far in making a difference to the livelihood of the poor and the needy. It is certainly necessary for some MDBs to address poverty reduction directly with their concessional funding. In most cases, however, the approach needs to be refined and improved.

“Suppose there is a community in a remote mountainous area, cut off from the outside world and dependent on aid from government and from international donors. Such areas may be rich in natural resources but locals have no way of tapping natural endowments. The only solution, in my view, is connectivity. Resulting economic opportunities will bridge the gap between the livelihood [of poor areas] and that of the outside world.”

For most MDBs, Jin suggests, “division of labour is necessary”. It is, he says, “the duty of some of them to tackle poverty directly and I have noted that their approaches are being adjusted so as to make their interventions more effective and efficient.”

The AIIB should meanwhile “learn from the experience of other MDBs from time to time and we will see if new strategies and new approaches are worth experimenting with.

“While poverty reduction is a laudable cause and a poster child for the virtue of development banks, it does not go very far in and of itself. Broad-based economic and social development is the ultimate solution for poverty reduction. Taking poverty reduction as the overarching objective will do nothing but restrict [development banks] effectiveness.”

Jin says he is “pleased to see that since the AIIB was initiated, with its clarion call for infrastructure investment, more institutions and investors have come to embrace this development approach”.

Some existing MDBs, he adds “have fine-tuned their mandate and have been more explicit about infrastructure investment. It is gratifying too to see that the G20 [Group of 20 emerging and advanced economies]

chaired by China this year has taken infrastructure development as a major theme.”

COLLABORATION AND CO-ORDINATION

The AIIB head says he is very keen on working in collaboration with the World Bank Group, the ADB (Asian Development Bank), the EBRD (European Bank for Reconstruction and Development) and other MDBs in co-financing infrastructure projects, which by their nature are usually very large. “Often, it is not a good idea for one institution to invest in such projects single-handedly,” he says.

The public sector, he says, “naturally has an important role in funding infrastructure investment. However, rising public sector debt and shrinking fiscal space means public sector resources are insufficient to meet demand. We attach great importance to the role of the private sector in infrastructure development and will certainly mobilise resources of the private sector.”

The shortfall of resources for infrastructure investment is, Jin adds, “undisputed, but the exact amount could be controversial. There is often a huge gap between what is desired and what is practical. What is needed does not mean that it is feasible to satisfy the need in one go.

“The onus for infrastructure investment does not fall on any single class of investor, whether it is sovereign governments, MDBs or private investors. But MDBs should work more closely with borrowers to ensure a stable policy environment that can help reduce perceived investment risk for the private sector.”

In Japan, *Emerging Markets* suggests, Abenomics is likely to involve further increases in the Bank of Japan’s purchases of government bonds, with some of this funding being used to finance infrastructure. Could this become a more general pattern in advanced and emerging market economies?

“Traditional monetary policy actions taken by many central banks over the last seven years have yet to bear significant fruit in terms of economic growth,” Jin notes. “If this situation persists, it is reasonable for central banks to consider alternative forms of monetary policy, such as the purchase of infrastructure bonds.”

But such a policy is not without risk, he cautions. “Debt sustainability is one of the factors weighed by investors. A rise in government debt to fund infrastructure investment may actually dissuade other classes of investors if projects are not efficiently implemented. The most critical element is ensuring that infrastructure projects are well designed and properly co-ordinated and that they meet a real need.” **EM**

Project invest

AIIB lending approved since June 2016



^ PROJECT: CENTER SOUTH ROAD CORRIDOR PROJECT, KAZAKHSTAN

Borrower: KazAutoZhol (KAZ)/Kazakhstan

Description: To reconstruct and upgrade 660km of the two-lane road between Karaganda and Burylbaital to a four lane road.

Cost: \$650m (The project is estimated to cost \$1,470m, and is expected to be jointly co-financed by AIIB and the World Bank.

Date announced: September 6, 2016



^ PROJECT: TARBELA 5 HYDROPOWER EXTENSION PROJECT

Borrower: Islamic Republic of Pakistan

Description: Installation of a power house at the fifth tunnel (Tunnel 5) of the Tarbela Dam and construction of a transmission line to connect the power to the national grid.

Cost: \$823.5m (\$390m co-financed by the World Bank); \$133.5m co-financed by the government of Pakistan)

Date announced: July 25, 2016

PROJECT: TRANSMISSION SYSTEM STRENGTHENING PROJECT (TAMIL NADU)

Borrower: India (Power Grid Corporation of India Limited – PGCIL)

Description: Enhancing capability of electricity supply in southern region of India

Cost: \$282.9m. AIIB loan: \$150m

Date announced: July 7, 2016



^ PROJECT: NATIONAL MOTORWAY M-4 (SHORKOT-KHANEWAL SECTION)

Description: Construction of 64 km of the four-lane, access-controlled national motorway M-4 connecting Shorkot and Khanewal in Punjab province.

Cost: \$273m (\$100m – AIIB, \$100m – ADB, \$34m – Dept. for International Development (UK); \$39m – Government of Pakistan)

Date announced: July 6, 2016



^ PROJECT: DISTRIBUTION SYSTEM UPGRADE AND EXPANSION PROJECT

Borrower: The People's Republic of Bangladesh

Description: To enhance distribution capacity and to increase the number of rural and urban electricity consumers in Bangladesh.

Cost: \$262.29m (AIIB loan: \$165m)

Date announced: July 6, 2016



^ PROJECT: DUSHANBE-UZBEKISTAN BORDER ROAD IMPROVEMENT

Borrower: Tajikistan

Description: Rehabilitating the 5 km section of the road connecting Dushanbe to the border with Uzbekistan from the Avicenna Monument to the West Gate in Dushanbe.

Cost: \$105.9m (joint financing from the AIIB and EBRD. EBRD will be the lead co-financer and will administer the project on behalf of AIIB)

Date announced: July 6, 2016



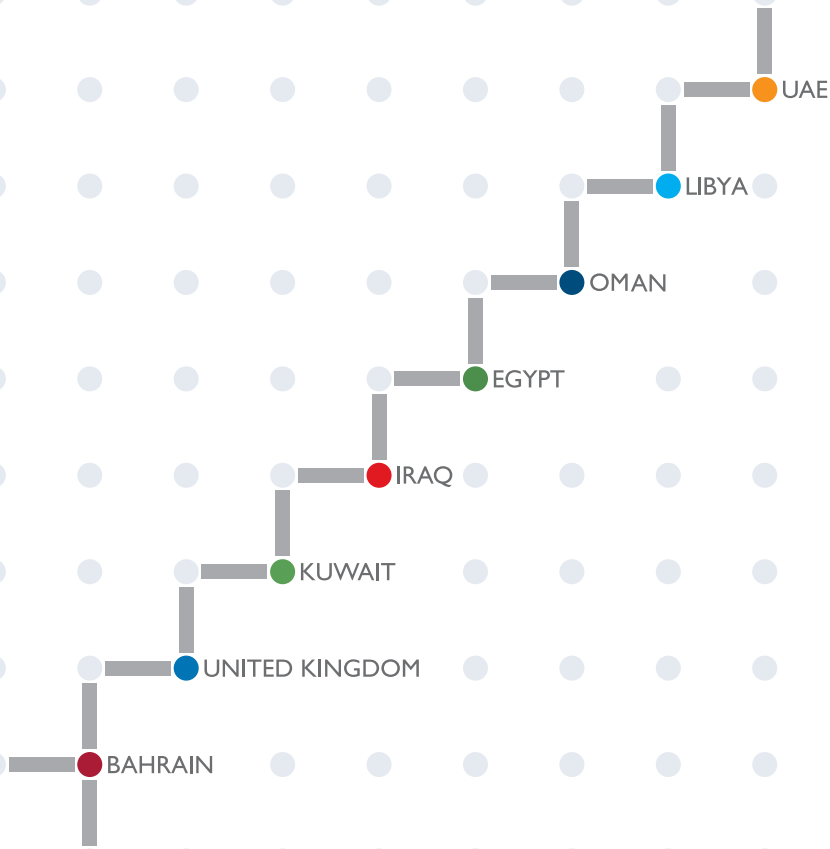
^ PROJECT: NATIONAL SLUM UPGRADING PROJECT

Borrower: Republic of Indonesia

Description: To support the Government of Indonesia's programme of urban slum infrastructure investments for 154 cities in the central and eastern parts of Indonesia.

Cost: \$1743m (sovereign backed AIIB loan of \$216.50m equally co-financed with the World Bank

Date announced: June 1, 2016



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Through our strategy of organic growth and acquisitions, we continue to strengthen our position in the region. Take advantage of our reach and grow with us.





Morocco stands tall amid MENA mayhem

In a region riven by instability, Morocco is rapidly emerging as a star performer thanks to policymakers' commitment to economic reform, cuts to subsidies and industrial expansion

By Lucy Fitzgeorge-Parker



"The country is in a much stronger position today than it has been for some time"

—Jason Tuvey, Capital Economics

It is a truism of emerging markets — and developed ones, for that matter — that structural reform commitments are usually more honoured in the breach than in the observance. Despite urging from domestic and international experts, prudent economic measures tend to be enacted only when unavoidable. It is relatively rare to find a country that follows the IMF playbook without the stimulus of crisis and recession.

Morocco's progress over the past five years is therefore all the more striking. Across a relatively benign economic and political backdrop, policymakers have pushed through a raft of improvements in areas from public spending and welfare support to industrial development and banking regulation.

"In terms of commitment to implementing difficult reforms, Morocco is a standout in the North Africa region," says Amelie Roux, a sovereign analyst at Fitch Ratings.

Easily the most ambitious of these reforms and the one that has generated the most interest has been a drastic reduction in government subsidies. In 2012, Morocco's government spent the equivalent of 6.4% of GDP on keeping the price of commodities including fuel, wheat and sugar artificially low. This year, the figure is expected to come

in at just 1.0% following the phasing out of all subsidies on diesel and gasoline.

Impressively, and unusually, this has been accomplished with minimal domestic push-back, thanks to a combination of effective communication by policymakers and the allocation of a sizeable chunk of the savings to welfare programmes.

Even allowing for increases in social spending, however, the effect on Morocco's public finances has been dramatic. The current account deficit has been reduced from close to 10% to below 2%, allowing for the rebuilding of foreign exchange reserves — to nearly seven months of import cover — and a reduction in net external debt for the first time since the global financial crisis.

Meanwhile the budget deficit, which was hovering around 7% of GDP in 2012, declined to just 4.3% last year and is expected to fall further to 3.7% in the current fiscal year. That in turn should halt the recent rise in public debt levels. Moody's forecasts overall government debt to peak at 65.3% of GDP next year.

Policymakers have also taken steps to ensure that public spending remains at sustainable levels through the introduction of an organic budget law. Passed at the start of this year, the complex legislation includes a golden rule allowing net new borrowing only for purposes of capital spending, as well

as provisions restricting carry-overs between budgets and putting binding ceilings on wage appropriations.

A further reduction in the budget deficit is now targeted to 3% of GDP next year — a level that some analysts see as ambitious given the limited scope for further spending cuts. "Subsidy reform has been the major driver of deficit reduction in Morocco thus far," says Roux. "The question is whether the government will be able to maintain this consolidation going forward."

She notes that the emphasis is now likely to switch to revenue collection, mainly in the form of tax receipts. The government has already announced plans for an overhaul of VAT legislation as well as the introduction of a new system of corporate tax brackets.

Policymakers have also proved surprisingly bold in addressing the thorny issue of public sector pension reform. A key demand of the IMF, which has supported Morocco with a precautionary liquidity line since 2012, plans to curb the pensions bill have nonetheless predictably provoked a domestic backlash.

Despite looming parliamentary elections in October, however, politicians in the ruling Islamic Justice & Development Party (PJD) have faced down opposition and pushed ahead with the first stage of reforms. A new

Gold

Morocco's El Amin Chentouf celebrates after winning the gold medal in the men's T12 Marathon at the Paralympic games in Rio de Janeiro



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law passed in July raised the retirement age for civil servants from 60 to 63 and mandated increased worker contributions.

CURRENCY PEG

Next up on the IMF checklist is the abandonment of Morocco's longstanding currency peg in favour of a flexible exchange rate. Again, policymakers have shown an unusual readiness to tackle the issue. The country's central bank, Bank Al-Maghrib, took the first steps this year with the reweighting of the currency basket used to set the exchange rate for the dirham and a move to a fully floating rate has been promised for next year.

That is due to be followed by the lifting of controls on currency leaving the country — although analysts say this will likely be implemented more gradually. “The authorities are extremely cautious about the process so we are not expecting any major shifts,” says Roux.

Mohamed Abu Basha, an economist at EFG Hermes, agrees. “What we are seeing in Morocco is a structural shift in the economy but one that is happening in a relatively safe macroeconomic environment,” he says. “They are therefore moving slowly but surely.”

He notes that a flexible currency, in particular, will be essential if policymakers are to achieve their ambition of developing Morocco into a financial hub linking Europe and sub-Saharan Africa.

Even with a pegged currency, however, significant progress has already been made on this front. Casablanca Financial City, a flagship project launched in 2010, has attracted a raft of international banks and companies including BNP Paribas, Bank of China, Boston Consulting Group and AIG.

Meanwhile, Morocco's leading banks have been on a major acquisition drive outside the country buying assets across North and southern Africa. By June 2015, Banque Marocaine du Commerce Extérieur, Attijariwafa

and Groupe Banque Centrale Populaire had loan exposure to sub-Saharan Africa of 23.5%, 13.1% and 9.4% of total lending respectively, according to Moody's.

This rapid expansion initially raised concerns about the suitability of Morocco's supervisory regime to cope with large cross-border banking exposures. The authorities' response was a wide-ranging banking law, passed in June 2015, which provided for the establishment of a new framework for macroprudential supervision and crisis management as well as the formation of a committee to analyse the financial system and assess systemic risk.

The new legislation also sought to facilitate technological development by broadening the scope of payments to include electronic currency and widening the definition of credit institutions, as well as bringing Morocco into line with international standards in areas such as anti-money laundering, consumer protection and antitrust legislation.

The bill also set the stage for the long-awaited introduction of Islamic banking in Morocco by creating a legal framework for shariah compliant finance. This bore fruit in September, when Credit Agricole du Maroc — no relation of the French house — announced plans to open the country's first Islamic bank early next year. The lender, which will be jointly owned with the Islamic Development Bank, will target rural areas and the unbanked population.

INDUSTRIAL BASE

While finance is seen as an important sector for Morocco, however, policymakers' key focus in recent years has been on leveraging the country's cheap workforce and proximity to Europe to build its industrial base. A wide range of incentives and initiatives has been introduced to attract international manufacturers, with impressive results.

In 2012, Renault began production of its Dacia range at a vast new plant in the Tangiers Free Zone, which was further expanded the following year with the addition of a second assembly line that increased capacity to 400,000 vehicles per year. Peugeot followed suit in June 2015 with the announcement of plans for a €557m plant near Rabat to open in 2019.

Both firms have also backed government efforts to develop supply chains for the auto industry within Morocco, with Renault pledging \$1bn in April to boost local sourcing of components from 32% to 65%. “If Morocco can build on this, it will attract further investment

into the country,” says Jason Tuvey, an economist at Capital Economics.

Other major growth sectors include aerospace — Bombardier is a major investor — and renewable energy. In February, the world's largest concentrated solar power plant began production at Ouarzazate on the edge of the Sahara Desert. When fully operational in 2018, the plant will have a capacity of 580MW and supply electricity to more than one million households, according to the government.

AGRICULTURE DEPENDENCE

Despite these advances, however, Morocco remains heavily dependent on its traditional agricultural base — as is demonstrated by GDP forecasts for this year. While the non-agricultural economy is expected to expand by 3%-3.5%, overall growth is tipped to be as low as 1.8% following a severe drought.

Agriculture still accounts for around 14% of GDP and employs 40% of Morocco's labour force. Here again, as Tuvey notes, the government is making strenuous efforts to reduce the vulnerability of the sector by encouraging farmers to switch from rain-dependent crops such as wheat to more resilient products such as olives and cherries. To date, however, progress has been limited.

Meanwhile, previously key sectors such as construction and real estate have yet to recover from the post-financial crisis crash, and an initial boost to tourism receipts following security troubles in other North African markets such as Tunisia and Egypt also seems to be fading. “For EU tourists, Morocco is increasingly suffering from being associated with the problems of neighbouring countries,” says Roux.

Analysts also note that most of Morocco's key industries remain highly sensitive to the economic performance of Europe, the main source of demand for the country's exports as well as of tourist visitors. “The strongest vulnerability for Morocco is its strong links with Europe,” says Abu Basha.

Nevertheless, the overall mood around Morocco is one of optimism. “We take a positive long-term view of Morocco,” says Tuvey. “Thanks to the government's prudent fiscal policy over the past five years, the country is in a much stronger position today than it has been for some time.”

Abu Basha adds that, while the country missed out on the periods of high growth enjoyed by other MENA countries in the pre-crisis years, it has also avoided any dramatic downturns. “Morocco has been the most consistent performer in the region over the past two decades,” he says.

In a febrile region, this slow but steady approach increasingly looks like a winning strategy. If policymakers can maintain their commitment to reform, Morocco could yet emerge as one of MENA's most prosperous, as well as progressive, economies. **EM**

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Developers look to capital markets to fund India's renewable ambitions



By Richard Metcalf

A new kind of company is set to be floated on the Mumbai Stock Exchange in the next year or so, which it is hoped will help wind and solar project developers to secure the vast amounts of capital required to meet India's ambitious renewable energy targets.

The vehicle, called an infrastructure investment trust, or InvIT, is similar in structure to the real estate investment trusts that exist in many other jurisdictions and is designed to allow public equity investors to hold a stake in a portfolio of cashflow generating infrastructure assets.

At the same time it provides developers with a way to monetise their wind and solar projects once construction is complete, freeing up much needed capital to plough back into projects that are in the earlier stages of development.

The listed investment vehicle is not designed solely for renewable energy—the only company so far to file a draft prospectus for an InvIT with the Securities and Exchange Board of India develops toll roads. But renewable project sponsors and their advisers see it as a potentially useful tool, alongside loans, bonds and direct equity investments, in their quest for fresh sources of capital to fuel India's renewables revolution.

And they will need to tap all the sources of capital they can find if the government's latest targets for renewable energy installations are to be met.

Renewable energy is at the very top of Premier Modi's agenda. Finding the finance to match his ambition will be tough though

In a bold move last year prime minister Narendra Modi's government increased the country's target for renewable power five-fold. From 20GW of installed capacity by 2022, the target for solar was increased to 100GW in the same timeframe. The 2022 target for installed wind power capacity was set at 60GW.

To put those numbers into perspective, as of July 2016 the total installed solar capacity in the country was just 8.1GW, while wind capacity stood at about 27.4GW, meaning that developers need to install about 15GW to 17GW a year of solar for the next six years and about 5GW a year of wind.

Despite the enormity of the task industry insiders are remarkably confident.

"It's not a very big ask," says Vinay Kumar, chief operating officer at Greenko, one of India's largest renewables focused independent power producers. "It's a good target and it's not unrealistic to be hitting 80% to 90% of these targets by the deadline. I'm optimistic."

But if the renewable power industry in India is to develop and construct the solar and wind projects that will be needed to fill the immense gulf between the existing capacity and the target, it will need to deploy

more capital more quickly than ever before.

Greenko and rival renewable IPPs such as ReNew Power and Mytrah Energy have been successful in attracting interest from a wide range of strategic and financial equity investors, from Singapore's sovereign wealth fund, GIC and German development bank KfW to Goldman Sachs and Merrill Lynch.

"We have raised around \$650m of equity and we may need another \$400m to \$450m at most. So maybe at around \$1.1bn we would be fully funded for a business plan of around 9GW to 10GW," says Kailash Vaswani, deputy chief financial officer at ReNew Power, whose majority shareholder is Goldman Sachs.

In addition to the equity provided by its shareholders, the company will recycle the cashflows from its operating portfolio, which is 1.2GW in size and constantly growing. But by far the largest capital requirement will be in the form of debt — about \$270bn for ReNew's business plan.

BRIDGING THE DEBT GAP

Wind and solar projects are typically financed, in India as in other emerging markets, with a combination of sponsor equity



"If you are having external commercial boarding in US dollars, then you need to take the currency risk as well"

—Pallavi Bedi, J. Sagar Associates

"Currently in India you are not really getting the benefit of greenness. There are no green dedicated funds"

—Kailash Vaswani, ReNew Power

and limited recourse project finance loans.

Interest rates on loans provided by domestic banks in India are high — project finance loans are typically priced between 9.5% and 12% — but while some foreign commercial lenders that could in theory offer more attractive rates, including Deutsche Bank, are said to be looking at entering the space, it takes a lot of work for them to be able to get comfortable with the risks involved.

Foremost among those risks is the financial health of the utility companies that are the main offtakers of power. In India those companies, government-owned and known as distribution companies or "discoms", have experienced such serious financial difficulties in recent years that the central government has felt the need to step in and restructure their debts.

Indian commercial banks that have a long history of providing project finance are familiar with the risks — which vary from one state and discom to another — and can price the loans accordingly. But for a foreign bank, assessing the ability of the individual discoms to make payments under their power purchase agreements represents a serious amount of credit work, and some market participants question whether the exercise is worth the effort.

"The other trouble is that if you are having external commercial boarding in US dollars, then you need to take the currency risk as well," notes Pallavi Bedi, a partner in the project finance practice of J. Sagar Associates, a law firm based in New Delhi. "So people were saying if you were doing hedging plus Libor interest rates, you were still coming down to about an 8% or 9% interest rate so it wasn't making that much financial sense."

If foreign commercial bank lending to renewables projects proves unfeasible, sponsors will have to rely as they have in the past on the domestic commercial banks, multilateral institutions and export credit agencies.

However, a slowdown in the development

of conventional, fossil fuel-burning plants is helping to make more capital available for wind and solar. If there are no opportunities to lend to coal-fired and gas-fired power plant projects, the banks' structured finance teams will have to put the cash to work elsewhere.

"There has been no real new investment in conventional power plants in the last two or three years," says L. Viswanathan, a Mumbai-based project finance partner at law firm Cyril Amarchand Mangaldas. "Until existing issues that conventional power plants have around cost recovery have been sorted out, some of the major developers are not going to make any new investment in greenfield conventional power plants and the lenders are also not going to support that, so that adds to the impetus to get the renewable capacity ramped up as well. That is going to be a big contributing factor."

Another development that will free up capacity in the loan market is the growing trend of IPPs tapping the capital markets.

ReNew Power has issued three bonds in the onshore Indian market replacing more expensive project loans.

Last year it also issued a novel bond for an individual 85MW wind project in the Sangli district of southern Maharashtra state. The bond was supported by a credit enhancement feature whereby the AAA-rated government-owned India Infrastructure Finance Company provided a first loss default guarantee on a portion of the debt.

India Ratings & Research, the Indian affiliate of Fitch Ratings, gave the credit enhanced RP4.5bn bond an IND AA+ rating and the deal attracted the participation of Indian insurers, pension funds and infrastructure debt funds.

"It was an attractive transaction for us," says ReNew's Vaswani, who adds that the company is planning to issue two more similar bonds before the end of the year.

Since ReNew only develops renewable energy projects, its bonds have been described

as "green" but they weren't marketed as such, says Vaswani. "Currently in India you are not really getting the benefit of greenness. There are no green dedicated funds in India."

But that did not put off fellow renewable power producer Hero Future Energies from becoming the first Asian issuer of a climate bond certified by the Climate Bonds Initiative in February with a RP3bn multi-tranche transaction.

The green designation could become more important as the credit ratings of the IPPs improve and if they begin to tap the offshore dollar denominated bond market, although for that to be the case the problem of currency hedging would have to be addressed.

In an effort to do just that, the Indian government is exploring the possibility of auctioning power purchase agreements where the tariff is denominated in dollars rather than rupees and hedging the currency risk itself through a pool of funds that it would set up.

INDIA'S YIELDCOS

In the meantime, market participants are interested to see how investors will react when the first renewable infrastructure investment trust is launched. The Securities and Exchange Board of India has issued guidelines on the vehicles and Mytrah Energy is reportedly among those contemplating a listing.

The description of the proposed renewable InvIT will sound familiar to anyone who has been following the fortunes of the so-called "yield companies" in the US, a comparison which could arouse a degree of caution. The model is essentially the same: roll up cashflow-generating renewable projects into a vehicle listed on an exchange.

The yield companies (yieldcos for short) in the US were initially greeted enthusiastically by investors but the companies' share prices dropped precipitously in 2015 amid falling oil and gas prices and a loss of faith in the ability of some of the companies to execute a pipeline of increasingly bold acquisitions.

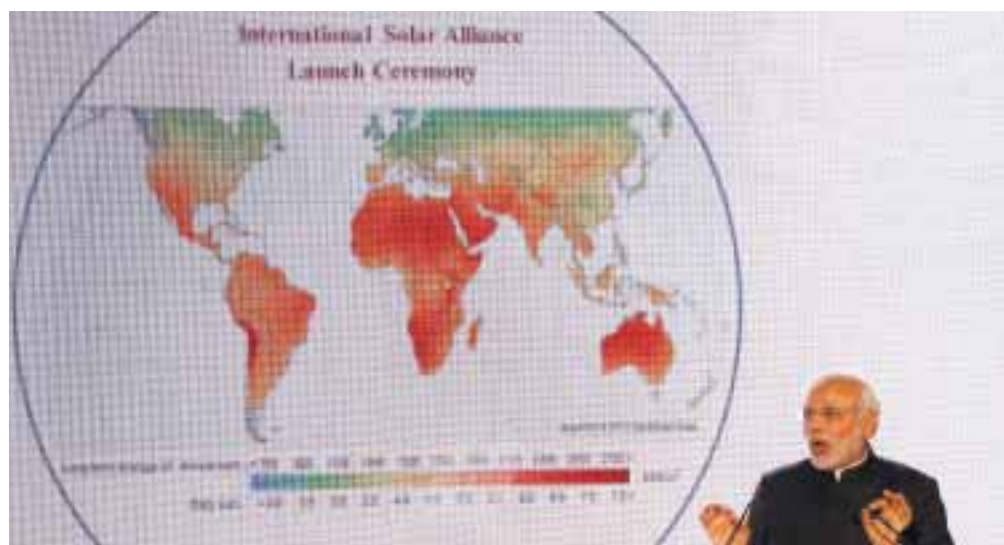
Since then, the Missouri-based renewable energy developer behind two of the yieldcos, SunEdison, has filed for bankruptcy and is now seeking to sell its entire global project portfolio.

Power producers in India and their advisers are well aware of the case, not least because SunEdison had a portfolio of projects totalling about 1.2GW in the country. Several players are making bids for them.

"I think the experience which investors had with the yieldcos... I don't think we need to follow the same track here," says Kumar. **ENI**

Heating up

India's prime minister Narendra Modi delivers a speech during the launching of the International Solar Alliance on the opening day of the World Climate Change Conference 2015 (COP21)





The debit and credit sides of fintech's African bank statement

A \$200,000 fraud at a Ugandan microfinance outfit is a telling parable of the risks that financial technology companies face in seeking to deliver the benefits that its supporters have long claimed for the industry

By **Olivier Holmey**

It happened four years ago but the memory of the fraud hangs heavy on Rupert Scofield, co-founder and president of the Foundation for International Community Assistance (Finca).

"He worked for us for 10 years; we thought we could trust him," Scofield recalls of the accountant at Finca's Ugandan outfit, whom he says embezzled \$200,000 from the group.

The story is one of collusion and poor supervision. The accountant gained access to more of Finca's accounts than he ever should have been able to, Scofield says. The accountant, says Scofield, was colluding with employees at a third-party telecoms provider, South Africa's MTN — an allegation it vehemently denies.

Finca has always faced fraud because of

the places in which it operates — countries where corruption is as endemic as poverty. Last year, some of Finca's own lawyers defrauded the bank's operation in the Democratic Republic of Congo, pocketing \$180,000. A few years earlier in Kosovo, Finca lost \$800,000 to criminals who appropriated the loans of hundreds of customers.

Because the average loan size is only a little over \$800 and because its declared goal is "leveraging every available dollar to maximise impact" on the prospects of the needy the sums lost were, to the group, substantial.

While the cases indicate a concerning vulnerability to embezzlement, neither was enabled by new digital processes but were rather traditional forms of fraud.

Now the risks of embezzlement are even greater, Scofield says, because the introduction of new technology has given fraudsters

additional means of accessing Finca's funds. He says the Ugandan case was made possible by new risks brought about by Finca's hazardous transition to mobile banking in Africa.

To Scofield, there are more reasons to be fearful now than ever before. In an interview published in the September issue of *Euromoney*, Scofield speaks of the new dangers brought about by adopting new technology and partnering with third-party tech players.

"This is something I warned my people about early," Scofield says. "If we're going to move to a new business model, especially one that is digital and involves the use of the internet, being ready for the hackers, being ready for the crooked employees, this is something that we've got to do a whole risk analysis of before we get involved. Even though we did that, obviously we didn't do it thoroughly enough in the case of Uganda."

Mobile money

M-PESA transfer in Kenya

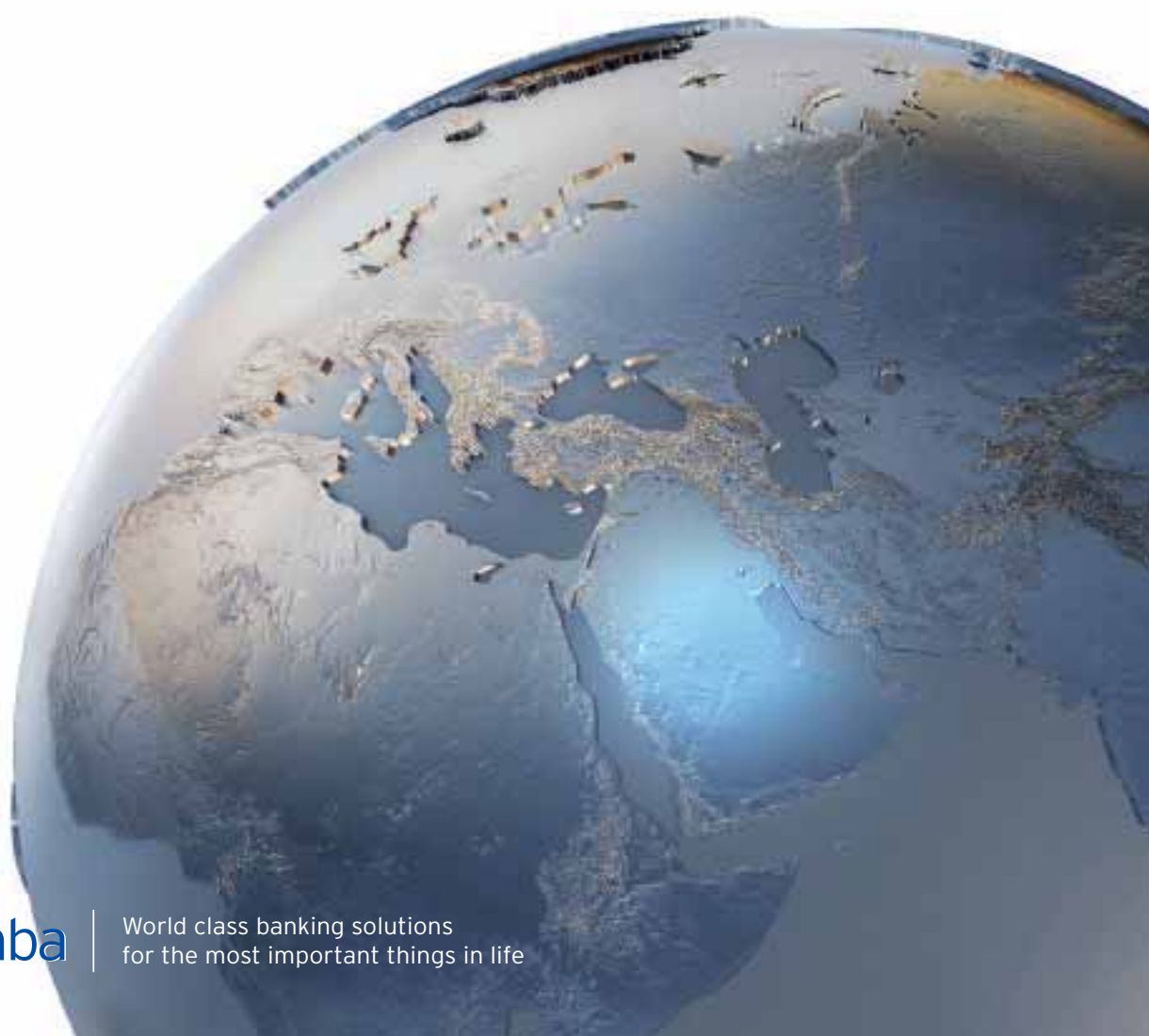
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"If we do not get into tech, we are out of business in the next five years"

—Olaf Becker, COO, Finca Tanzania

SOCIAL AND FINANCIAL COMMITMENT

Finca was founded as a microfinance non-profit in 1984 and focused on what it called "village banking", delivering small, uncollateralised loans to groups in Latin America through a collective guarantee. Each debtor is responsible for every other, making repaying one's loan as much a social commitment as a financial one.

Finca was firmly rooted in paper money and face-to-face interaction with its clients. At first Finca lent primarily to women because women, it found, were less likely to be banked, more likely to be responsible with their money and disproportionately affected by poverty.

Now Finca is one of the world's largest microfinance institutions and serves nearly 2 million clients. It has operations in 23 countries across Latin America, the Caribbean, the former USSR, Africa, the Middle East and South Asia. It operates as a normal bank, insofar as it delivers financial services — deposits, loans, transfers — and its revenues overwhelmingly derive from the return it generates on its services, rather than from charitable donations.

The firm has about 700,000 customers on the African continent, across six countries. In each one of those countries — Uganda, the DRC, Malawi, Nigeria, Zambia and Tanzania — Finca has a banking licence. "The vision for Africa is to be the number one financial service provider for low income individuals," Finca vice-president and regional director for Africa, Mike Gama-Lobo, says.

Sometimes referred to as the World Bank for the poor, Finca has received the support of financial institutions. Credit Suisse, GE Money and MasterCard have been partners with Finca on various projects. The firm has more than 80 lending partners, among them Citi, Deutsche Bank and the World Bank.

Despite all this goodwill, Finca knows banking is changing and that it has to stay on top of developments if it is to survive. To keep delivering on its promise of financial inclusion — bringing the unbanked poor into the financial fold — it has to adopt new tools to reach an ever-larger pool of potential customers, as well as deliver better services to its existing clients.

Finca has been slow to embrace these changes and when it has, their adoption has been fraught with challenges. The Ugandan fraud is a case in point.

COMPETITION IN TANZANIA

Although only its third largest African operation with 100,000 customers, Tanzania represents the forefront of its push to innovate, Finca says. Its hopes for successful change lie here.

At first glance, the Tanzanian outfit does not look much like a modern, digital operation. It nestles between a busy six lane road that runs through miles of central Dar and an open dirt patch.

Overlooking central Dar's only golf course, National Microfinance Bank (NMB), perhaps Finca's most advanced rival in Tanzania, boasts new headquarters, where hundreds of bankers manage the bank's operations around the country.

Ineke Bussemaker, who has been NMB's chief executive since May last year, is aware of the need to constantly update the bank's practices. She says of digital and mobile banking: "That is, to me, where the growth is — where you can actually reach millions of people, where systems are scalable and you can do it at low cost."

NMB has the advantage of being part-owned by Dutch lender Rabobank, which has provided it with the kind of training and technical support available to few microfinance institutions in Africa.

Though microfinance is in the bank's name, NMB has diversified its activities: only about a quarter of its loan book can now be categorised as microfinance and SME lending.

Taking on advanced businesses like NMB is a challenge for Finca. Benoni Katende, based in Kampala, Uganda, is Finca's head of alternative channel delivery for Africa, meaning he is in charge of the provision of services through mobile phones, the internet and physical agencies.

In Tanzania, Finca has 650 full time workers for a balance sheet of \$40m. Of those employees, 240 are loan officers. Their number and role has changed little in recent years. And while they provide valuable face-to-face interaction with customers — a personal touch many at Finca view as essential to what the bank does — they also represent

what some would consider an antiquated form of banking: loan officers spend hours travelling to customers in remote areas rather than serving them through mobile phones or via the internet.

rates on loans. Finca's outfits in the rest of Africa operate on a similar model. It didn't have to be that way. Scofield speaks sadly of an early partnership idea with Grameen to create a mobile phone aimed at providing customers in Uganda with easy access to microfinance. The project, the first of its kind, went ahead as the Grameen-phone (GP) in 1997 — but in Bangladesh and without Finca.

Not only did Finca miss the opportunity to be the first in mobile banking, but the most impressive financial innovation story of recent years, certainly in Africa and perhaps even worldwide, also passed it by: the huge expansion in Kenya of mobile powered financial services, owing largely to the impressive rise of M-Pesa, Vodafone's mobile phone based money transfer and microfinance service. Launched in 2007, M-Pesa has 23m active clients in Kenya — about the size of the country's adult population.

COMPLETE UPHEAVAL

If one man can turn things around for Finca and make it a real force in this challenging new digital environment, it may be Olaf Becker. Becker moved to Dar last year to become Finca's chief operations officer for Tanzania, tasked with dragging the bank's legacy operations there into the 21st century.

Because Tanzania is now where Kenya was a few years ago — huge mobile phone penetration coupled with a large, unbanked population — the bank believes the country is the perfect place to try new things out. If it works, Finca hopes to deploy the tools Becker will have introduced in Tanzania to its other outfits in Africa and eventually around the world.

A young, hard-working German, Becker speaks enthusiastically about his work but he is also keenly aware of the danger Finca faces. "If we do not get into tech," he says, "we are out of business in the next five years."

He is working on three projects that he thinks could revolutionise the way Finca works: digital field automation (DFA), credit scoring and mobile savings.

Under the DFA plan, perhaps the project Becker speaks of with the most enthusiasm, Finca intends to equip all of its loan officers with 3G-connected tablets. On these tablets, the officers will be able to open accounts and deliver loans via electronic forms using fingerprint registration rather than reams and reams of paperwork.

Officers will still be required to travel the country but at least it will make the process of signing up customers less cumbersome, Becker says. "Every loan officer is going to be a small mobile bank," he adds.

On credit scoring, Finca has partnered up with First Access, a US data analytics firm. First Access runs through basic personal information about prospective customers — age, gender, number of dependents, house ownership — to score creditworthiness. It also runs through the individual's repayment

On the ledger

A three-year summary of Finca's key financial indicators

	2013	2014	2015
Total borrowers*	1,146,000	1,203,000	1,166,000
Year-end gross portfolio	\$840,600,000	\$966,900,000	\$818,850,000
Total amount disbursed	\$1,464,727,000	\$1,605,900,000	\$1,282,989,000
Portfolio at risk >30 days**	1.5%	1.9%	3.5%
Total savers*	767,000	1,039,000	1,140,000
Total deposits from clients	\$78,400,000	\$130,200,000	\$168,300,000

Figures include gross loan portfolio, disbursements and savings.

*Includes clients who are both borrowers and savers.

**Percent of loans past due greater than 30 days.



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"The vision for Africa is to be the number one financial service provider for low income individuals"

—Mike Gama-Lobo, vice-president, Finca



history with mobile network operators.

Lastly, changes to Finca's mobile offering will enable clients to get what the bank calls "nano loans" — credit between \$5 and \$50 — without the need to travel to any branch or meet a loan officer. As the credit scoring develops, Finca plans to increase mobile loan amounts continuously to support business investment.

Becker says these changes represent a complete upheaval of how Finca operates: "We're changing everything around this." But he is realistic about the pace at which they will fall into place. "This is a lot of work and it's not going to work from day one."

TECHNOLOGICAL ADVANTAGES

But Becker knows, as Scofield does, that risks exist when going digital. One big challenge comes from the increasing reliance on third parties. To offer mobile banking services, Finca has to partner with mobile network operators across Africa. That exposes the bank to any weaknesses in those operators.

Mobile network operators are not the only businesses Finca cannot do without anymore. Aggregators, firms such as Selcom and Max-Malipo in Tanzania, have carved themselves a central role in the African market for mobile financial services. By forming partnerships with both the payment instrument providers — for instance, the mobile operators — and the groups that want to transfer money, be they businesses needing to pay salaries or utility companies needing to receive payments, aggregators have become key middle men that banks need to cosy up to.

Hacking, too, has been a concern. Though Scofield says there have been no big breaches yet, Finca has been assailed by

online attacks trying to access the bank's customer data. "In our bank in Georgia, in our IT room, we have this big screen which shows all the hackers trying to attack the firewalls around the world," Scofield says. "A lot of them are coming out of Russia, some of them are coming out of Nigeria. It's a new world."

That new world also has its advantages. For example, the introduction of national identity numbers in Tanzania will make it easier for Finca to know its customers — a key part of fighting money laundering and other forms of fraud. By collecting those numbers from prospective clients, Finca will be able to access key information about them from the government database. That information will then feed into First Access's credit scores. Registering clients' fingerprints should also prevent fraudsters from gaining access to the accounts of others.

The use of automated systems via tablets in the field, meanwhile, should enable Finca to keep its many loan officers in check. "The clients used to see the loan officer as Finca, and the loan officer could threaten them and say: 'You know what, if you don't do this and this and this, I'm not going to serve you guys anymore.' He had this huge amount of power and we've taken that power away from the loan officer now."

Becker is convinced default rates will fall as a result. Default rates are already low: only 6% of debtors do not repay on the day their loans mature and that falls to 4% after 30 days. Annual loan write-offs total just 2.5% to 3%. Becker thinks write-offs could fall to 2% or less, thanks to the new credit scoring introduced.

FRAUD AND CHANGE

All banks face these challenges and all are fighting for a place in this shifting market.

"Competition has soared," Becker says. "There are a lot more microfinance institutions. Banks are downscaling to microfinance significantly. The mobile network operators are also entering the microfinance sphere with micro-loans, micro-savings."

In Becker's view, the only way to stand out is to cut operational costs and listen to what clients want. "We need to offer something that our customers really want now. We have to start taking our customers seriously."

Finca is nowhere near giving up the fight. On fingerprint technology and credit scoring, for example, the bank appears to be ahead of many of its competitors. Of all the firms that rely on agency banking in Tanzania, Finca is the only one to have provided fingerprint payment terminals to its agents. Its partnership with First Access, meanwhile, represents one of the largest collaborations between microfinance and financial technology to date. And Finca is far from being the only bank in Africa still to rely on a large contingent of travelling loan officers.

Gama-Lobo does not claim Finca is immune to further losses. To him, fraud and change go hand in hand. "The reality in this business is if you don't have fraud you also don't evolve because no risk manager or person sitting down in a room is going to figure out everything. These guys [fraudsters] figure it out much quicker."

As Finca seeks to leverage technological innovation to reach an ever larger number of the world's poor, to what extent can it mitigate the risks of a Ugandan repeat? And, crucially, how much more will it lose before it gets it right? It's a question facing all banks operating not just in Africa's poorer regions but also those in developing markets around the world. **EM**

Old school

Microfinance companies on the ground, working on promotion of loans for solar home systems in Uganda

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FRANKFURT LAYS OUT ITS FINANCIAL CENTRE CREDENTIALS

Will Frankfurt be the main beneficiary of Brexit? It is certainly working hard to develop its Finanzplatz and polish up its image as a place to live and work. In this roundtable, a who's-who of representatives from the Frankfurt region exchanged their views on the prospects for the city in the post-Brexit era.



HENNER ASCHE,
DEPUTY HEAD,
MARKETS
DEPARTMENT,
DEUTSCHE
BUNDESBANK,
FRANKFURT



ERIC MENGES,
PRESIDENT AND
CEO, FRANKFUR-
TRHEINMAIN
GMBH, FRANKFURT



FRANK SCHEIDIG,
GLOBAL HEAD OF
SENIOR EXECUTIVE
BANKING, DZ
BANK, FRANKFURT



**DR JOACHIM
NAGEL,**
FORMER MEMBER
OF THE BOARD
OF DEUTSCHE
BUNDESBANK,
FRANKFURT



**DR FRANK
CZICHOWSKI,**
SENIOR VICE
PRESIDENT AND
TREASURER, KfW
BANKENGRUPPE,
FRANKFURT



DR STEPHAN BREDT,
DIRECTOR GENERAL
ECONOMIC SECTOR,
FINANCIAL SERVICES,
EXCHANGES, MINISTRY
OF ECONOMICS,
ENERGY, TRANSPORT
AND REGIONAL
DEVELOPMENT, STATE
OF HESSE

EM: Let's start with Brexit. Has Frankfurt been slightly hesitant about using the result of the UK referendum to market the Finanzplatz?

Eric Menges, FrankfurtRheinMain (FRM): You're quite right to say we have not been as aggressive as some people may have expected us to be. However, we are very passionate about promoting Frankfurt and the greater Frankfurt region. We have said very clearly to the UK media that we are not positioning ourselves as competitors to London, but as the best choice for businesses or banks in the UK which may feel they require an alternative to London.

What that means is that we want to build bridges to the financial centre in London. We don't want to tear down the bridges that already exist. London will remain an important player for some time to come and we want to maintain our good working relationship with London. We don't claim to be better or worse than London, just that we are a viable alternative.

EM: Are you implying that you regard your competitors as Paris, Dublin and Luxembourg, rather than London? ?

Menges, FRM: Absolutely. Those are the other alternatives against which we need to position ourselves. One of the reasons we think we are so well-positioned is that people here speak very good English. Some of my friends tell me it's quite hard to learn German if you come to Frankfurt as a native English speaker, because people will automatically switch to English — that applies to the

restaurants, the bars and the shops as well as in the banking industry.

Compared with some of the other European locations, I think we are very international. We have a lot of international schools here and a long heritage of dealing with international businesspeople who come to visit our trade fairs year after year.

Joachim Nagel, Bundesbank: Brexit could affect Frankfurt in a number of different ways. Of course it could be an opportunity for Frankfurt to gain some business from companies relocating from London.

But it could also be a challenge, because if this does not happen, Frankfurt will have to ask itself if it has really done enough to convince companies to come over.

It's an open process but it's definitely a challenging one. It's also a very delicate subject. Frankfurt is an important financial centre which is very pro-Europe. So while I'm not in favour of Brexit at all, if there is a Brexit, we have to ask ourselves how Frankfurt can profit from it.

Frank Scheidig, DZ BANK: I agree that Frankfurt should continue to co-operate with our long term partners in the UK. I fully agree with Eric that London will continue to be a very important hub.

But don't forget that Germany is the largest economy in the European time zone and that the UK is our biggest trading partner.

There will always be competition, which is healthy. The question is: how do you want to play the game? Do you want to build partnerships, or do you go down the French route of aggressively trying to persuade people to pull out of London and

relocate to Paris?

Nagel, Bundesbank: It's still difficult to reach a proper understanding of what Brexit really means. So much is dependent on the outcome of negotiations between the UK and the EU.

Frank Czichowski, KfW: Brexit or not, I agree that Frankfurt has plenty to offer as a financial centre. We need to make sure we tell our story, which is a good one, in order to attract financial services to the city.

If as a consequence of Brexit, some companies or business units relocate to Frankfurt, so be it. But for the time being, nobody really knows how negotiations between the UK and the EU will unfold, or what they will mean for the financial services sector.

Bredt, State of Hesse: It is definitely the German position that politically and economically we would certainly prefer the United Kingdom to remain within the EU. Chancellor Merkel has made it very clear that she is not going to press for a quick Brexit, and that she wants Britain to remain a close trading partner of Germany.

But at the same time we of course have to consider what the implications of Europe's biggest financial centre leaving the EU are. The EU also needs to think about what it needs to provide itself with in terms of financial services to its industry.

This is a fundamental change and we are only at the very beginning of this debate.

EM: Nevertheless, if banks like Goldman Sachs



DR STEPHAN BREDET,
MINISTRY OF ECONOMICS, ENERGY,
TRANSPORT AND REGIONAL DEVELOPMENT

and Morgan Stanley and others should choose to move some of their business from London to Frankfurt, that has to be good news for the Finanzplatz, doesn't it?

Bredt, State of Hesse: Yes, of course. But our stance is that this is not a change that we have chosen. If this change requires readjustments in terms of policy, we will have to have a discussion about that. This will have strong implications for financial regulation, and as a consequence, banks may be forced to reallocate some parts of their businesses. If that happens, we would be happy to be part of the solution.

But because it is in nobody's interest that we have a slowdown in economic growth, it is essential that we find a solution that is quick and effective.

Whether or not major financial services providers choose to move from London to an alternative financial centre depends on two issues. The first is: how will those service providers deal with the uncertainty arising from Brexit? Uncertainty itself can become a driver of a move from London to other cities, because nobody can afford to sit on their hands and not to invest for the next three to five years. And do you choose to invest in a place where you are not sure about what lies ahead, or in one where there is proven stability?

The second, which is much more important, is what will be the outcome of the negotiations between the UK and the EU? We all know what the central topics are in the context of financial services. They are passporting, clearing, and the regulatory regimes. Here, I think the debate is yet to begin — because the EU still needs to develop a clearer picture of the financial services it needs for its own purposes. For example, does the EU want to have control of the clearing of its own currency?

And if you look at the topic of passporting, the eurozone also needs to be clear about the type of services it has and whether they correspond adequately to its industrial strengths.

Third, you need to ask what sort of financial services industry you have under your regulatory control. Is it a very small niche, or should it correspond to the size of your economy?

These are all very central questions. Only when

they have been debated will we be able to find a satisfactory answer.

EM: Leaving Brexit aside, what are Frankfurt's strengths as a financial centre and how has the Finanzplatz evolved over the last 20 or 30 years? Frank, you joined KfW in 1989. How has Frankfurt changed since then? Is it fair to say that at the end of the 1980s Frankfurt was still something of a backwater as far as international finance was concerned?

Czichowski, KfW: I think that is a bit of a British misconception. Frankfurt has been an important trading hub and a financial centre for the last 400 years or so, and it grew very rapidly after the second World War when the Deutsche Bundesbank and KfW were created.

At the end of the 1980s, Frankfurt was already the global headquarters of successful players such as Deutsche Bank, Dresdner Bank, Commerzbank and KfW, as well as the headquarters of the Bundesbank. There were also plenty of international banks located in Frankfurt by the end of the 1980s, so I don't think it is accurate to say it was a backwater.

However, if you look at the historical evolution of Frankfurt — and I think this is equally true for London and all other financial centres — the financial services sector has become progressively more important over the last 25 years. KfW is a good example of this development. When I joined in 1989, it employed about 900 people in Frankfurt. Today, our Frankfurt headquarters hosts well over 3,000. Other banks have grown in a similar way over that period, although there has been a slight decline in recent years.

The growth of the Deutsche Börse is another reflection of this growth. There has been a stock exchange in Frankfurt for several hundred years, but in the last 20 years the Deutsche Börse has developed into a very important market provider and international player in its own right.

But I don't think the role of Frankfurt in the German economy has changed much in the last 25 years. It has always been the financial centre of Germany.

The difference with countries like the UK or France is that we have a federal structure in Germany, which means that there are other smaller financial centres throughout the country.

EM: Yes. When I first came to Germany in the mid-1980s the eight stock exchanges in Germany were all fiercely competing with one another. Even today, Düsseldorf is still an important financial centre, with HSBC Trinkaus based there. Is Germany's decentralised structure a strength or a weakness for the country's financial services industry?

Scheidig, DZ BANK: There is no doubt that over the last decade Frankfurt has rapidly outgrown the smaller former financial hubs like Hamburg, Hannover, Stuttgart and Düsseldorf. Munich still plays an important role in insurance thanks to companies like Allianz and Munich Re, but in commercial and investment banking and capital markets, asset management and financial law, Frankfurt has

now clearly established itself as the German financial hub, which is accepted by the other smaller centres.

Bredt, State of Hesse: Of course, each Land has its own agency that aims to attract capital. That is normal, and we think competition is always healthy because it helps you identify your strengths and weaknesses.

Düsseldorf and Munich both laid a claim to being important financial centres in the past, but I think everyone now agrees that Frankfurt is Germany's financial centre.

Czichowski, KfW: Most of these exchanges still exist, offering niche products. But clearly Deutsche Börse has evolved into by far the largest player, and if the merger with the London Stock Exchange goes ahead it will be a world-scale player.

Bredt, State of Hesse: I agree. If you look at the story of the Deutsche Börse over the last 20 years it has been a huge success story. It has grown from being a very small exchange into a global company which has overtaken the other exchanges by far. As Frank said, the others still exist but some are now talking about merging.

EM: The point about the Deutsche Börse is interesting. Maybe I was wrong to call Frankfurt a backwater at the end of the 1990s, but it was certainly very insular. Look at a product like the Pfandbrief, which nobody outside Germany or Austria could spell or pronounce as recently as 1990. Has Frankfurt internationalised more rapidly over the last 20 or 30 years than other financial centres in Europe?

Czichowski, KfW: It is true that Frankfurt has internationalised very quickly, but I think that is also the case for most capital markets around the world. In Germany we had what we used to call the anchoring principle — the Verankerungsprinzip — which dictated that you needed a Germany-based underwriter to issue in Deutschemarks.

You also needed permission from the central bank to do a bond issue. But that was not different from other markets. As late as the mid-1990s I remember very well that whenever we wanted to issue in the Spanish market we had to telephone the Ministry of Finance in Madrid to apply for clearance.

So I don't think the internationalisation of capital markets has been something unique to Frankfurt. Back in the 1980s capital markets were still very localised and the internationalisation of the Eurobond market was something that really only got off the ground in the early 1990s.

EM: Is this something that London maybe underestimates? Do those who argue that London maintained its leadership role in spite of not joining the single currency, and that it can do so again outside the EU, underestimate the speed with which other financial centres have developed in the last 20 years? Is the competition much more formidable than it was?

Czichowski, KfW: London is a big financial centre in its own right and will remain so for quite some time.

But I think the point is that in the late 1980s individual financial centres were trading different products from each other. You mentioned the Pfandbrief, which until the 1990s was very much a locally-traded product. Since then it has made very big inroads internationally, and is traded throughout Europe. So the difference today is that we trade the same products everywhere, which is what is creating more competition among financial centres.

Bredt, State of Hesse: An example of the internationalisation of financial services in Frankfurt is our commitment to establishing an RMB hub here. The rationale for this is that our trade is very closely linked to China, and we would also like to see more Chinese investors coming to the greater Frankfurt region. We always believed that we should provide the best regulatory conditions to allow for the financing of inflows from China as well as outflows to China.

We can offer Chinese companies that come here excellent RMB trading conditions and this is applicable to companies in the financial services industry as well as in manufacturing. For example, the newly-established joint venture, China Europe International Exchange (CEINEX), which went live last year, has established some very successful products, such as RMB-denominated ETFs. From what I understand, the SSE 50 ETF is already one of the most actively traded ETFs in Europe.

Menges, FRM: This is a very important point. We are seeing a very strong rise in the number of Chinese, Japanese, Korean and Indian business coming into the region.

EM: How does Frankfurt's RMB hub compare with — and compete with — London's?

Bredt, State of Hesse: It is our aim to offer the best regulatory environment to do RMB business. We think this is a worthwhile aim for the biggest economy in Europe and for one of its biggest investor markets.

On the question of RMB hubs, of course there will also be RMB business to be done in London. But there will also be plenty of business to be done in Frankfurt.

As we now have to address the very unwelcome question of Brexit, we have to recognise that the UK will no longer be part of the EU. This will pose the question of whether some RMB-euro clearing can take place in London any longer. We don't yet know the answer to this question.

EM: We talked earlier about the Pfandbrief market and the Deutsche Börse. What are the other main success stories in the German financial services sector?

Nagel, Bundesbank: It's not just the Pfandbrief that has been a success story. I think you need to look at the whole package of German banking.

To some outsiders the German financial market may sometimes look a little boring. But boring could be regarded as attractive if the whole package provides support for large as well as Mittelstand companies across the real economy. I



ERIC MENGES,
FRANKFURTRHEINMAIN GMBH

think this package is exceptional compared to many other countries and financial services.

When I travel overseas and people ask me about the strength of our economy, I say that the main driver of this strength is the real economy. This combined with an increasingly vibrant Finanzplatz should be appealing to investors.

Scheidig, DZ BANK: I concur. I think the biggest success story in the German economy is the German Mittelstand, which has been the main driver of the three pillars of the banking industry. In particular, the co-operative banking sector follows the Mittelstand companies throughout the world. They have a very clear understanding of the requirements of SME companies which helps to make the system more robust.

Menges, FRM: The great German success story is that we have preserved our manufacturing base. When people overseas are asked about the German corporate sector they think of the well known brands like BMW and Mercedes, but the real backbone of the German economy is the middle-sized companies which manufacture machine parts, automotive components and so on which they export throughout the world. These are not the major brand names but are often family-owned companies.

The other point I'd make about German success stories is the way in which the eastern part of Germany was brought up to speed with the rest of the country after reunification.

Scheidig, DZ BANK: On the subject of Germany's success stories, there are many other examples within the real economy. Germany is one of the leading hubs for Industry 4.0. We hold more patents per capita than any other country in the world, and we are a global leader in renewable energy which has been driven by our ban on nuclear power. All these examples demonstrate how vibrant and flexible the German economy is as well as the related financial sector.

Also, I don't think you can underestimate the importance of the fact that Germany is so liberal.

EM: Looking at some of Frankfurt's other credentials as a financial centre, people often say

that one of these is the presence of the ECB's headquarters in the city. But some might also say this is a double-edged sword. On the one hand it adds to the credibility of the Finanzplatz. But on the other if it is staffed largely by bureaucrats, it won't do much for the dynamism of the financial centre.

Henner Asche, Bundesbank: I'd like to start by making a short comment about the location of the Bundesbank. Historically, it was assumed that the central bank should be located in the same city as the government. So when Berlin became the capital of Germany some people expected that the Bundesbank might move to Berlin.

But when German lawmakers reconsidered the Bundesbank's location they decided to keep the central bank in Frankfurt. The most important criterion for this decision was the local business environment together with the availability of human capital and the city's top quality infrastructure. The Bundesbank very much welcomed this decision.

Coming back to your question, it is a great advantage for us to be located near to the ECB because the individuals working at both institutions co-operate very closely.

Nagel, Bundesbank: From my experience as a former central banker, I agree that it is an advantage for a central bank to be close to its customers. This is positive both for the central bank itself and for its customers. It is certainly an advantage to have a regular exchange of views on regulatory issues.

Asche, Bundesbank: The location is also an important consideration for attracting talent. We don't just want to have German staff. We have a policy of recruiting staff from all over the world. Sometimes we have to explain them why it is so attractive to work in Frankfurt. The proximity to the ECB as well as the direct contact we have with the broader industry are very helpful in this regard.

Scheidig, DZ BANK: It's clear that people are attracted by the quality of life that Frankfurt has to offer. It has short commuting times, perfect infrastructure, top-quality educational establishments and very low costs.

Frankfurt also provides good access to cities all over Europe. One of the reasons it is so popular with Asian visitors is that Frankfurt is an excellent gate of entry to other parts of Europe.

Menges, FRM: In terms of the attractions of Frankfurt for international banks, I think we have to distinguish between financial institutions that do not yet have a presence in Europe — such as those from China and Korea, for example — and those who already have a strong presence in the UK and are required to look for an alternative. Frankfurt's strength is that it is an established financial centre, rather than something that has to be built from scratch. Even before Brexit there were more than 200 foreign banks in Frankfurt.

Second, it is in the middle of one of the strongest and most consistent economies in the world.

Third, from a political perspective if you looked up 'political stability' in Wikipedia, they'd probably refer you to Germany as an example.



HENNER ASCHE,
DEUTSCHE BUNDESBANK

So if you're an international bank looking for a base at the centre of the new European Union in a post-Brexit world, these are the factors you want to consider.

Asche, Bundesbank: The other thing we shouldn't forget is the quality of financial supervision in Germany.

EM: Eric mentioned political stability. But Germany isn't as stable politically as it was before the migrants' crisis and the growing popularity of Alternative für Deutschland (AFD), is it?

Nagel, Bundesbank: That is true. I think the German election next year is something that could trigger some volatility.

EM: Is the Frankfurt area seeing foreign direct investment in other industries?

Bredt, State of Hesse: Yes. Hesse has a very well-diversified industrial base. In the south there are Merck and Behringer in the pharmaceuticals sector, and there are also several IT and software companies in the south. The northern part of the Land is very strong in the electronics industry, where companies are very internationally oriented. Companies from countries such as Japan, Korea and China, as well as from the US, have all invested in the region. The China Investment Promotion Agency has chosen Frankfurt as its European headquarters, and they have said that they see this as a gateway to Europe.

EM: Allow me to be very provocative and maybe even rather rude. As we speak, there are murmurings about Deutsche Bank going the way of Lehman Brothers, which would be the most severe but by no means the first crisis to befall Germany's financial services industry. Think Herstatt Bank. Think IKB. Think WestLB. Think the Neuer Markt. Germany makes fabulous cars and creates superb engineers. But does it do banking well?

Bredt, State of Hesse: I think Germany does do banking well. We have a stable financial sector in Germany. Of course we suffered during the crisis,

as all European economies did. But in general we have no major problem with providing our industry with financial services.

I don't want to suggest that there are no problems in the German financial services industry, but these seem to me to have their root causes in the past. Maybe those problems have not been overcome as completely as we had hoped. But I'm confident that we have the capacity to overcome these challenges in the future. I think we have a very stable, reliable and consumer-friendly financial services industry. The fact that we have more than 2000 banks is positive for the consumer, through the provision of low-cost financial services.

Asche, Bundesbank: We can't comment on individual banks. But we've learned from the crisis and we've made very good progress on establishing efficient mechanisms for dealing with crisis situations. So we're now in a much better position to respond to challenges than we were five or 10 years ago.

Scheidig, DZ BANK: The examples you mention are largely events that happened many years ago. I'm pretty sure that if you looked at the core financial centres all around the world there would be plenty of examples of equally drastic situations.

I would add that throughout the crisis that started with Lehman, Germany's three-pillar banking system remained very robust. As Henner said, we have a strong regulatory regime in place with very high capital buffers.

So even though we would have preferred for the various disasters you mentioned not to have happened, the crisis management put in place by the Bundesbank in response to events like Lehman Brothers and Hypo Real Estate has been of very high quality. I doubt that any other financial centre would have dealt with these challenges as efficiently as Frankfurt under the guidance of the Bundesbank.

EM: What is the role of financial services in the Hesse economy?

Bredt, State of Hesse: It is a key element of our state policy to foster the growth of financial services in Frankfurt. It is not just that there are about 140,000 people working in the financial services industry here; this sector also plays a key role in supporting local industry going abroad and developing new products here at home. This makes financial services an integral part of our economy, and if anything it might even be too small.

Of course there are other highly successful industries located throughout Germany, all of which need to be financed. Successful export projects don't just depend on the quality of your product, but also on their efficient financing. So there is a strategic commitment to a strong financial services industry here.

EM: We always assume that having a large financial services sector is a good thing, and of course it is very important for everyone around this table. But not everybody in the UK is happy with the size of the country's financial services industry. Former deputy prime minister Nick Clegg, for example, has spoken about the ineq-

uity of propping up a nation of 100,000 square miles on the profits of a single square mile. So people like Clegg may be happy to see some parts of London's financial services industry move to Germany.

But what about Germany itself? How is banking viewed by young people in Germany? Is it regarded as a noble and desirable way of making a living, or is it seen as a grubby, greedy, unprincipled profession? Young Germans want to be engineers or software developers, don't they, rather than bankers?

Nagel, Bundesbank: That's a fair question. What I understand from some surveys is that prior to the financial crisis, young people did want to go into banking. These days, this is not something you hear very often. Banking is no longer one of the things people say they want to do when they leave university.

EM: Isn't this bad news for the ambitions of the Finanzplatz?

Nagel, Bundesbank: You're right. The Finanzplatz does not just need to convince investors. It also needs to convince students that financial services represent a necessary part of our economy and society. But this is also a cyclical process.

Menges, FRM: I wouldn't go as far as saying that young people in Germany admire bankers. But it is a highly respected business in the Greater Frankfurt region.

There is no question of Frankfurt being over-dependent on financial services. The largest taxpayer in the City of Frankfurt is not a bank, but a life science company which manufactures some of its products in this region. So there is plenty of industrial diversification here in areas like life sciences, IT or automotive.

If you look at young people, I think fintech, which is the combination of start-ups and banking, is a very attractive sector in the Frankfurt Rhein-Main region, which benefits from having an established financial sector and one of the biggest German IT clusters around the Darmstadt area.

Czichowski, KfW: In London, and in the UK in general, the financial sector has always been regarded as a large and very important part of the economy. In Germany, that has never been the case. It has never had a dominant share of GDP, nor of the labour market.

To give you some numbers, in the state of Hesse, which has about six million inhabitants, the contribution of finance and insurance to GDP is about 7%. In Germany as a whole, it's significantly smaller. By virtue of that, young people look in a number of different directions, and there is no overwhelming ambition to work in the financial sector. Companies like BMW and Daimler and technology companies like SAP are at the top of the list of the most desirable employers for university graduates.

Perhaps it's a good thing that there is a wide diversity of employment preferences among young people.

EM: Indeed. After all, it wasn't banking that

drove the Wirtschaftswunder. It was engineering. But does it make it more difficult to sell a career at KfW to young graduates?

Czichowski, KfW: Every institution, including KfW, has to create its USP. We're all aware that we need to fight for talent, and KfW is in a privileged situation that it provides responsible banking and appeals to people who are attracted by a career in the financial sector and at the same time care about climate protection, social responsibility and a sustainable world.

Scheidig, DZ BANK: I guess that your question refers back to the mid-1990s when capital markets and investment banking were seen as the hot places to work. Young people saw it as a very creative area of the banking industry. I'm sure it was at the time, although as we all know it probably became too creative in the early 2000s.

Having said that, from what I see in my own bank, and from what I hear from the other two pillars of the German banking industry, there is still a very strong demand for jobs in the sector.

I would also echo what Eric said about demand for jobs in the fintech industry. Berlin is the centre for start-ups and Frankfurt is the centre for fintech, and we're seeing young people from all over the world — from Israel, for example — wanting to play a part in these industries. Don't forget that between them Frankfurt and Berlin raised more money for start-ups than London last year.



FRANK SCHEIDIG,
DZ BANK

Bredt, State of Hesse: I totally agree that attitudes have changed since the 1990s. But if I look at an educational establishment like the House of Finance here in Frankfurt, it is growing rapidly, building its reputation and investing in research and teaching.

The story is the same at the Frankfurt School of Business and Management, which has just opened a new campus, which is three times the size of the old one. It is attracting rising numbers of domestic as well as international students. So we are still seeing a huge influx of talented young people.

Our aim is to build a financial centre here in Frankfurt which relies on a philosophy of stability, responsibility and sustainable growth. That is why as a state government we have set up corresponding programmes at state universities. We think we can and must provide a new philosophy of banking

and finance that fits Continental European industrial and economic models.

EM: What about labour relations? There was an interesting piece in Bloomberg recently which said that part of Frankfurt's pitch to foreign banks is making it easier to fire bankers. Does the financial services industry in Germany still have a problem with labour relations?

Bredt, State of Hesse: I'd answer that with a clear no! We used to have these debates more than 10 years ago. Then we had the major Schroder reforms which did a great job. They created one of the biggest upheavals in social and labour market policy I can remember in my lifetime. Today we're seeing the fruits of those reforms. There is now a very high level of flexibility in the German workforce — so much so that people are sometimes concerned it has become too flexible. But industry has been able to grow but also to contract where necessary.

If you look at the statistics on employment and job creation, they demonstrate that German labour law is at the forefront in Europe.

Nagel, Bundesbank: Frankfurt is certainly not the place to come if you want to make quick money. But in terms of job security it is probably more attractive than many other financial centres.

This may make Frankfurt less attracted, but it is not as return-oriented as some markets.

EM: The UK euro-sceptic MP, John Redwood, wrote in a 1997 book that it is impossible for bankers to work on deals over the weekend in Frankfurt because the unions insisted on offices being closed from 5pm on a Friday to 8am the following Monday. Germany has changed a lot since then, hasn't it?

Scheidig, DZ BANK: Yes. It is completely untrue that German labour laws are a problem for the banking sector. Germany's labour market is as flexible as any other, but it is strongly regulated in a way that safeguards employees. The clearest reflection of that in the banking industry is the lack of volatility of staffing. Germany doesn't have the same hire and fire mentality that there is in London.

EM: But just to bury this John Redwood myth, have you personally worked over the weekend when it has been necessary to get deals done?

Scheidig, DZ BANK: Absolutely! People are very highly motivated to commit themselves to hard work and that includes weekends when necessary. In that respect, there is very little difference between working practices in Frankfurt and London or New York.

Asche, Bundesbank: Just to answer your question from a central banker's perspective, rigid regulation of labour markets in Germany may have been an issue 10 or 15 years ago. But I would agree that this is no longer an issue in this country. Working over the weekend has become much more common since the onset of the crisis, and you don't hear



DR JOACHIM NAGEL,
DEUTSCHE BUNDESBANK

many people complaining about it.

At the same time, we always try to find a fair balance between employers and employees, which is in our genes in Germany.

Menges, FRM: We're asked the question about labour relations all over the world. What we have to explain over and over again is that German labour law is much more flexible than most people think. For example, it is possible to employ people under limited contracts which allows you to terminate the working relationship within a two year time frame without any questions being asked.

The other point I'd like to make is that if labour relations are so difficult in Germany, how come Germany is such a successful player in the global economy and the world champions when it comes to exports? The vast majority of businesses in Germany continue to work very successfully within the labour regulatory environment that we have.

Workers' councils in Germany are not unions. They are there to provide counselling to management, and they co-operate very closely with management with the common aim of securing a better future for their companies.

The major restructuring that the economy went through during Chancellor Schroder's so-called Agenda 2010 reforms was so successful that a number of countries now consider it a model to follow. But the Schroder reforms were only possible because they were implemented hand-in-hand with the unions and the workers' councils. So I'd agree that it's not a hire and fire environment but it's definitely more flexible than most people think.

Scheidig, DZ BANK: If I just look at the sector I work in, which is the co-operative pillar of the German banking industry, people are very dedicated to their jobs. This was reflected in the stability of the sector throughout the crisis.

EM: I understand that Gunter Grass once described Frankfurt as a 'lump of concrete'. Is it fair to say that Frankfurt has traditionally had a reputation as an ugly city?

Bredt, State of Hesse: But when was Gunter Grass writing? In the 1960s and 1970s, when Frankfurt was not the most attractive city in Germany. At the

same time, it was a city of high intellectual spirit. Look at the Horkheimer School of Philosophy. Frankfurt has a rich history in pre- and post-war literature, starting with Goethe. Look at the Darmstadt modern music movement.

But after its destruction during the war, Frankfurt was the only city to really change, and today its skyscrapers give it a very attractive skyline. It has transformed itself into a new, modern city.

Czichowski, KfW: It's true that for many years Frankfurt did not have a very good image even within Germany. One of the reasons for this is that when Frankfurt was rebuilt following its destruction during the War, money was in short supply, as a result of which some of the areas of the city were not very attractive. The railway station at the time was regarded as an area frequented by drug-users.

But much of this has changed in the last 25 years. Today it is one of the greenest cities in Germany. I understand that about 52% of Frankfurt is now green.

EM: That is a subject that interests you personally, isn't it? Do you still cycle to work?

Czichowski, KfW: Yes, I do. Cycling in Frankfurt is much less dangerous than it is in London.

I cycle 16 kilometres to work each morning and I only have to go through two sets of traffic lights. The rest of my commute takes me through the green belt of Frankfurt, which was set up 25 years ago and is about 75 kilometres long.

EM: Eric mentioned the trade fairs earlier. One of the nightmares for foreign visitors coming here during a trade fair is trying to find a reasonably priced hotel. One year I had to stay in a floating hotel on the River Main. Does Frankfurt have enough hotels?

Menges, FRM: I think the cost of doing business — which includes hotel accommodation — is extremely competitive compared with some of the bigger cities in Europe. I agree that hotel capacity can become stretched during the trade fairs, and hotel rooms are at a premium. But it's worth remembering that because of the roads and public transport there is no need for visitors to confine themselves to the centre of Frankfurt. The city itself is a relatively medium-sized area within the greater Rhein-Main region, and you can reach anywhere within that region within 30 minutes or so. During the trade fairs a lot of visitors spill out into the region.

EM: And the transportation infrastructure is excellent, isn't it?

Czichowski, KfW: Yes. We always have to be a bit careful about saying how good the airport connections are, because that invites the joke that it makes it easy to get away from Frankfurt. But the truth of the matter is that when I have an appointment in Berlin, I can go from my house to the airport in 20 minutes, park the car and be on board within another half hour.

Frankfurt is a very big airport with outstanding connections to every destination in the world, especially Asia and the Middle East. The railway system

is also very efficient, so from a transportation perspective Frankfurt is an extremely convenient place to live and work.

Menges, FRM: The airport is also so close to the city that you don't have to get up at 4 o'clock in the morning to catch your morning flight, as you do at many other cities' airports.

Bredt, State of Hesse: It's not just the airport. Motorway and road links are excellent and at the weekend I can be sipping wine in the Rhein Valley within 15 minutes of leaving my home in Wiesbaden. In addition to the excellent roads and motorways is the fact that Frankfurt is the number one railway hub in Europe so there are also excellent train connections.

EM: We spoke earlier about people being prepared to work on Saturdays. At the risk of being highly mischievous, that might be because there's nothing else to do in Frankfurt. You've only got one football team, for example, and it hasn't won anything since 1959. So Frankfurt can't compete with London when it comes to entertainment, can it?

Scheidig, DZ BANK: That's not true. Frankfurt is full of culture. Twenty years ago it may have been true that the city emptied at the weekend, but now people stay on because there is so much to do. Although we may not have as many restaurants as London, the food here is top-notch.

Czichowski, KfW: And don't forget our Apfelwein! It takes some getting used to, but it tastes good and it's a healthy drink. It's good for the digestion and very refreshing — the perfect drink for a sunny Sunday afternoon.

Menges, FRM: Frankfurt was the birthplace of German techno-music, which has made the city's night clubs some of the best in Europe.

As to sport, there are about 30 golf courses in or around Frankfurt. We also have one of the best opera houses in Germany and a good variety of restaurants and bars. So it isn't true that there is nothing to do.

Czichowski, KfW: At my age, I don't think that I can contribute much to the discussion about night-life in Frankfurt. But I've lived in Berlin and visited many big cities throughout the world, and having made Frankfurt my home since 1989 I find it to be a very liveable city. We have a world class opera house, and a number of very good theatres, small as well as large, so there is always something to do.

It's true that we only have one Bundesliga football club in Frankfurt itself but there are several others in cities like Mainz and Darmstadt within easy reach, so if you look at the greater Frankfurt region there is a wide range of sporting and entertainment options.

Bredt, State of Hesse: If you look at the Mercer Quality of Living Survey for 2016, which identifies the cities with the highest personal safety ranking based upon internal stability, crime, effectiveness of law enforcement and relationships with other countries, Frankfurt ranks seventh. By comparison,



DR FRANK CZICHOWSKI,
KFW BANKENGRUPPE

Amsterdam is 11th, Dublin 33rd, Paris 37th and London 39th.

Also, property in Frankfurt is much more affordable than it is in London. But many young families choose to live outside the city centre, close to the Taunus Forest, for example.

Asche, Bundesbank: On a personal note, I should add that I'm originally from Hamburg, not Frankfurt. When I moved here, all my friends felt sorry for me to be posted in Frankfurt. Nowadays, it's completely different. When people hear that I work in Frankfurt they call me a lucky guy.

Scheidig, DZ BANK: I had a similar experience, having moved here from Kiel at the end of the 1980s, and I couldn't agree more with Henner.

Bredt, State of Hesse: I moved here five years ago and I have really come to love the city. It is highly international and very rich in culture. I live in Wiesbaden, which is where the Hesse government offices are located. So it is a five minute walk to the office. But if I need to go to Frankfurt I can drive there in 20 or 30 minutes.

Menges, FRM: If you have a family and kids, this area offers one of the best lifestyles in the world.

EM: At the risk of sounding prudish, would it not be even more suitable for families with young children if the bulldozers did away with that street opposite the central station, with its brothels, sex shops and dodgy bars?

Menges, FRM: I would have thought that any major city in the world which has international connections would have a similar area somewhere within the city's precincts. But if you have visited that particular area over the last few years you will have noticed a great change from the past when it was purely a red-light district. I think Frankfurt is doing a very creditable job of changing that entire area and making it more attractive.

And although it can sometimes look a bit intimidating, it is a perfectly safe part of town to walk through. Many of the bankers in Frankfurt call in there for lunch or a drink after work at one of the many uber-cool new bars and restaurants.



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Safe — efficient — sustainable



GlobalMarkets: Vietcombank's stated ambition is to establish itself as the number one bank in Vietnam and one of the top 300 in the world. Very briefly, can you explain how Vietcombank will achieve this ambition?

First of all, Vietcombank will focus on retail banking, treasury and fee-based services; and at the same time, strive to maintain its leading position and improve its market share in core business areas including international settlement and trade finance, cards and digital banking, and forex. In addition to that, the bank will also continuously refine its customer relationship and customer satisfaction; strengthen its technology infrastructure; and improve its human resources.

Besides, Vietcombank will enhance its financial capacity by controlling its asset quality, increase its profitability ratios and raise capital to fuel its business and ensure its capital adequacy is aligned with international standards. In terms of management, Vietcombank has been implementing a variety of transformation projects in order to

“ VIETCOMBANK HAS DEVELOPED AND IMPLEMENTED A CAPITAL RAISING PLAN (INCLUDING TIER ONE AND TIER TWO CAPITAL). ONCE THE PLAN IS COMPLETED, THE CAPITAL ADEQUACY RATIO (CAR) OF VIETCOMBANK WILL BE AROUND 10% (THE RATIO IS CALCULATED BY USING BASEL II GUIDELINES, HIGHER THAN THE MINIMUM REQUIREMENT OF 8%)

enhance its management capability with the goal of adopting best practice in management especially in risk management. “Safe — Efficient — Sustainable” will be the bank's motto for its development in the upcoming years.

GlobalMarkets:

Vietcombank is committed to diversifying its product and income structure. Which new product areas will the bank be prioritising?

Vietcombank will prioritise products in retail banking, fee-based and digital bank-

ing in order to gradually modify its operating income structure with a higher proportion of income from retail customers (customer dimension) and service activities (product dimension).

GlobalMarkets: Only 35% of the Vietnamese population have bank accounts. What opportunities does this create for a bank like Vietcombank?

Banking penetration in Vietnam is still modest.

According to research, around 35% of the population has bank accounts. Therefore, Vietnam has enormous potential for the development of banking services, especially in retail banking. As the oldest bank in the country with more than 53 years' experience of operating in the market, with unique advantages in management, human resources, technology, brand and competitive funding costs, Vietcombank will continue to penetrate the market. One of Vietcombank's strategic objectives is to become the number one player in retail banking in Vietnam by 2020.

GlobalMarkets: In its most recent analysis, Moody's comments that “Vietcombank's modest capitalization is its key weakness”. Can you give us an update on the bank's capital raising strategy?

The rating of Vietcombank is considered the highest among Vietnamese banks. However, the bank's capital adequacy is modest compared with its peers, given that Vietcombank is expected to be one of the few banks in Vietnam fully adopting Basel II by the end of this year. However, capital is a weakness of many banks in Vietnam. Vietcombank has developed and implemented a capital raising plan (including tier one and tier two capital). Once the plan is completed, the capital adequacy ratio (CAR) of Vietcombank will be around 10% (the ratio is calculated by using Basel II guidelines, higher than the minimum requirement of 8%). ■

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MACRO-ECONOMIC AND BANKING OVERVIEW

Fast-growing Vietnam aims for ASEAN hub status

Vietnam is one of the fastest growing economies in the emerging market universe, and an increasingly popular magnet for investors looking to establish a hub in the ASEAN region. But explosive growth is creating a number of challenges.

In late December 2015, two initiatives were announced within a few days of one another attesting to the range of sectors that are attracting inflows of foreign direct investment (FDI) into Vietnam.

The first was the \$1.1bn acquisition by Thailand's Singha Asia Holding of 25% of Masan Consumer, a leading local branded consumer food group, along with 33.3% of Masan Brewery. This strategic partnership gives the two groups the opportunity to target the inland ASEAN region of Vietnam, Thailand, Cambodia, Laos and Myanmar, which between them have a population of close to 250m.

For Singha, however, the prize is also the greater access the partnership offers to Vietnam's compelling demographics. According to Masan, with 56% of Vietnam's 90m population under the age of 30, the country's expanding and increasingly aspirant workforce is expected to drive rising consumer spending over the next 10-15 years.

Days after the announcement of the Singha/Masan partnership, South Korea's Samsung — Vietnam's biggest foreign investor — announced that it had reached an agreement to increase its investment in Saigon's Hi-Tech Park from \$1.4bn to \$2bn. This investment, which is being channelled into the production of smart televisions and other electronic goods, complements a \$3bn commitment made earlier in 2015 by Samsung.

Landmark deals such as these, targeting the domestic as well as the export markets, have helped FDI inflows into Vietnam to reach record levels over the last 18 months. In 2015, FDI was up 17.4% to \$14bn, and in the first six months of 2016, it rose by 105% year-on-year (yoy) to \$11.2bn, with more than 70% accounted for by manufacturing

and processing. Korea, once again, was the largest investor in Vietnam, accounting for about 35% of the total, followed by Japan and Singapore (each with about 10%).

John Foo, founder and CIO of the Singapore-based Kingsmead Asset Management, points out that this strong rise in FDI is coming from a very low base. "People forget that countries like China and Thailand have been attracting FDI for years," says Foo, whose Indochina and Vietnam Growth Fund was up by about 17% year-to-date by late September. "That means that their cost base is already quite high. In Vietnam it is still very early days for FDI, which means costs and the risk of contagion arising from any sell-off across Asia are both much lower."

STRONG FDI FLOWS

With Vietnam's government forecasting that FDI this year will reach \$15bn, this surge of inward investment shows little sign of slowing down. For example, at the end of August, Singapore's sovereign wealth fund, GIC, reached an agreement to take a 7.7% stake in Vietcombank. As Vietnam's largest lender, with a well-diversified portfolio across a range of sectors, this is an ideal proxy for one of the fastest-growing economies in the emerging market universe.

Impressive streams of FDI into Vietnam have been one of the main motors of continued economic growth, which reached 6.7% last year. "Massive foreign flows into Vietnam, especially in the manufacturing sector, were spurred by the conclusion of a number of major free trade deals, as well as regulatory reform such as the new business law and the new law on foreign ownership," notes the London-listed Vietnam Enterprises Fund (VEIL), in its review of 2015.

Kingsmead's Foo agrees that the deals that Vietnam has signed over the last year or so with a number of trading partners have been pivotal to attracting more FDI. "These free trade agreements are encouraging many companies to move manufacturing facilities to Vietnam from countries such as Japan, China, Taiwan and Korea," he says. "This in turn is allowing Vietnam to become a focal point for manufacturing in the ASEAN region, a community of 700m consumers which is growing at 4% a year."

Vietnam's growth rate of 6.7% last year, which was ahead of the government's own projections of 6.2%, was impressively broad-based. As Moody's comments in its most recent *Credit Opinion*, manufacturing rose by a robust 10.1% in 2015 in line with the strength in Vietnam's exports. "Similarly rapid increases in construction and wholesale and retail trade, as well as services more broadly, indicated the recovery in domestic demand," adds the rating agency. Consumption, which accounts for about 68% of GDP, grew by 9.3% in 2015.

It is not just Vietnam's stellar growth over recent years that has attracted portfolio as well as direct investors and won the approval of external economists and analysts. Moody's adds that imbalances associated with strong growth such as high inflation and sizeable current account deficits have not materialised.

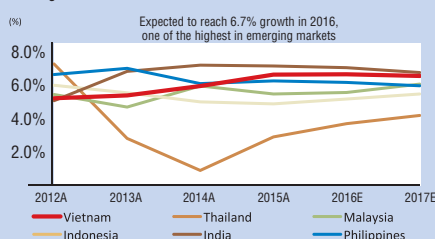
Another positive indicator is Vietnam's fast-growing FX reserves, which are estimated to have expanded at a combined annual growth rate (CAGR) of 19% between 2012 and 2016, doubling from \$25.6bn to \$51.3bn.

While growth is expected to remain robust this year, it faltered slightly in the first quarter, with agricultural production hit by a severe drought. Nevertheless, growth in the first half of 2016 reached 5.5%, which HSBC describes in a recent

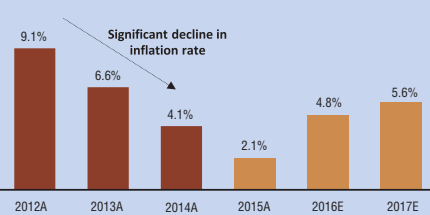
VIETNAM'S FAVOURABLE MACROECONOMIC CLIMATE

Source: Vietcombank; EIU, IMF, General Statistics Office of Vietnam

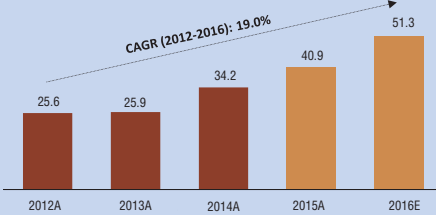
Strong GDP Growth



Stabilizing inflation rate (% of average increase in consumer prices)



Growing FX reserves (US bn)





Compelling demographics and landmark deals

report as “pretty robust by global standards” although it is still slower than the government’s official target for this year of 6.7%. As HSBC adds, however, growth is likely to have accelerated by 3% in the third quarter, which would translate into an annual rate in line with the government’s target. “After two quarters of lower than expected growth, we think that the strength in manufacturing and external sectors helped accelerate GDP growth,” notes HSBC.

MIXED PRODUCTIVITY

Whether these recent growth levels can be sustained over the medium term may depend on how effectively Vietnam can turbocharge its productivity. In a report published in 2012, McKinsey cautioned that after 25 years of steady growth, the country would need to boost its productivity by more than 50% to maintain its momentum.

Since then, the Vietnamese scorecard on productivity has been mixed. On the positive side of the ledger, Vietnam’s position in the World Economic Forum’s Global Competitiveness Index (CGI) has continued to improve, with a rise from 68th out of 144 countries in 2014-15 to 56th out of 140 in 2015-16. While it still ranks below many of its ASEAN peers, Vietnam now stands above Sri Lanka in this index and just one position below India.

On the less positive side, although labour productivity has been rising for the last decade, there is still a yawning gap to be closed with the rest of Asia. According to calculations published recently by the Central Institute for Economic Management

(CIEM), Vietnamese labour productivity in 2014 was 6.41% of the level in Singapore, 13.56% of Korea’s and 40.36% of China’s. With one recent report suggesting that it will take Vietnam half a century to close its productivity gap with Thailand, small wonder that the government has proposed establishing

“[VIETNAM’S] FREE TRADE AGREEMENTS ARE ENCOURAGING MANY COMPANIES TO MOVE MANUFACTURING FACILITIES TO VIETNAM FROM COUNTRIES SUCH AS JAPAN, CHINA, TAIWAN AND KOREA. THIS IN TURN IS ALLOWING VIETNAM TO BECOME A FOCAL POINT FOR MANUFACTURING IN THE ASEAN REGION”

—JOHN FOO, CEO KINGSMEAD ASSET MANAGEMENT

a national committee for labour productivity.

For now, breathless growth is also exposing a number of other vulnerabilities in the Vietnamese economy, especially in the public finances. As VEIL warns, “budget numbers show that Vietnam is resolutely living beyond its means, with annual deficits stuck fast at 5%-plus of GDP.” In 2016, this could rise, with Fitch forecasting that the adjusted budget deficit could reach 6.5% of GDP in 2016.

Allied to worries about the deficit, there are also concerns about public debt in Vietnam. The World Bank has forecast that this

may reach 64% of GDP in 2016, which is well above other ASEAN countries. The good news, as Moody’s points out, is that debt affordability remains high, reflecting the high share of debt owed to official creditors at low-cost or concessional terms. Nevertheless, Moody’s adds that as nearly half of the debt stock is denominated in foreign currency, government finances are rendered “particularly susceptible to exchange rate shocks”.

Kingsmead’s Foo says that this uncomfortably high level of public debt may create opportunities for equity investors such as his Indochina and Vietnam Growth Fund. He says that as part of its commitment to reducing debt to 60% of GDP, the privatisation process will be accelerated, leading to a rising number of IPOs, twinned with higher liquidity and greater diversification. Foo says that these developments, alongside higher foreign ownership limits, improved corporate governance and a more intense focus on shareholder value, will combine to strengthen Vietnam’s case for being upgraded from a frontier to an emerging market in the next 24-36 months.

CROWDED BANKING SECTOR

Another risk identified with the rapid expansion of the Vietnamese economy in recent years is the recent growth in credit within the very overcrowd-

ed banking sector, which is made up of 98 banks. Most of these are tiny, with a handful of state-owned commercial banks (SOCBs) accounting between them for about 50% of industry assets, 46% of lending and 45% of deposits, according to Vietcombank numbers.

Credit growth accelerated to 14.2% in 2014, 17.3% in 2015 and 17.6% in the first five months of 2016 year on year. While this growth is in line with the target of 18%-20% set by the State Bank of Vietnam (SBV), some observers are uneasy that continued acceleration in credit will increase non-performing loans (NPLs), pressurise profitability and weaken capital positions. “In our opinion, rapid credit growth poses a risk to Vietnam’s medium-term financial stability, particularly since the credit/GDP ratio — at 110.3% of GDP in 2015 — is already extremely high by frontier market standards,” notes a recent Fitch bulletin.

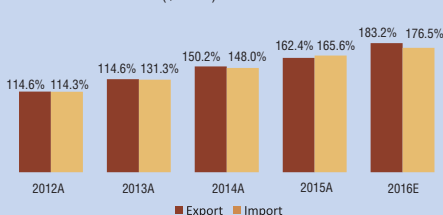
Fitch adds that “Vietnam’s bank ratings are among the lowest in Asia, reflecting a range of structural problems — not least of which is weak capitalisation. Published capital adequacy ratios (CAR) are low, and under-reporting of NPLs suggests that true capitalisation is even weaker.”

The authorities have responded constructively to the problem of asset quality by allowing the Vietnam Asset Management Company (VAMC) to purchase NPLs from banks with cash at market prices rather than by exchanging them for VAMC bonds.

It is hoped that the issue of weak capitalisation, meanwhile, will be addressed by rising foreign investment in the banking sector, with GIC’s acquisition of a share in Vietcombank coming soon after the IFC bought a 5% holding in the much smaller TienPhong Bank. “Banks are likely to need additional capital as they respond to the phasing-in of Basel II capital adequacy standards by end-2018 while trying to meet demand for rapid credit growth,” Fitch notes. It adds that pressures arising from Basel II requirements are likely to have been among the key drivers of the GIC investment in Vietcombank, which had a CAR of just 9.7% under the Basel I regime at the end of June 2016.

Much-needed consolidation across the Vietnamese financial services sector ought to generate compelling opportunities for the leading banks that are likely to drive the process. According to Vietcombank, only 25% of the population has a personal bank account, so the opportunities arising from favourable demographics, increasing urbanization and rising income levels are self-evident. ■

Positive trade balance (\$USbn)





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Global Context

Financial Inclusion

Over a third of the world's adult population still do not have a bank account, despite the rapid growth in global financial services. New digital currencies and the growth in mobility will drive financial inclusion and improve underlying banking processes. There is a continuing role for currency as part of a diverse payments ecosystem, especially for those who remain excluded from the formal banking system. We also believe that effective financial inclusion is linked to personal identity: without an identity it is difficult to access the financial system.

Identity security

The SDGs commit governments to ensuring every citizen has a legal and secure identity by 2030. The World Bank says that 1.5 billion people worldwide have no formal identification. This is a huge challenge for many countries as it prevents development assistance reaching the people who need it most. A secure identity allows all citizens receive their state provided benefits, in terms of health, education and social protections. Identity security also leads to solutions to the challenges of mass migration and new forms of terrorism. It creates the foundations for the establishment of e-government services. The critical starting point is effective birth registration – in a world where a million children a week are born without a birth certificate.

Anti-corruption & counterfeiting

Preventing counterfeiting and corruption is key to achieving the SDGs. Funds diverted from the formal economy get diverted into areas of crime and terrorism, when otherwise they can be used by governments to meet their own development needs. The IMF says the money lost to corruption every year is 2% of the global GDP or \$2 trillion per year. Because of this, governments are denied tax revenues on regulated goods and citizen confidence and safety is undermined when counterfeit money or goods enter the supply chain. Moreover, when counterfeit goods enter their supply chain, companies' profits and brands are impacted, reducing their role in leading productive growth. There is a growing global movement to ensure corrupt practices are eliminated so that money can be reinvested in fighting poverty, building infrastructure, creating jobs and protecting the environment.

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Head of Government Relations

duncan.fulton@delarue.com

What's happening Friday, October 7

9.00am - 10.30am

Annual Meetings Plenary

Location: DAR Constitution Hall, 1776 D St NW

11.00am - 12.00pm

Seminar: Financial inclusion not exclusion: managing de-risking

Moderator: **Francine Lacqua**, Anchor, Bloomberg Television

Speakers: **HM Queen Maxima of the Netherlands**, UN Secretary-General's Special Advocate for Inclusive Finance for Development; **Jim Yong Kim**, President, World Bank Group; **Sri Mulyani Indrawati**, Minister of Finance, Indonesia; **Arun Jaitley**, Finance Minister and Minister of Corporate Affairs, India; **Juan Manuel Vega-Serrano**, President, Financial Action Task Force (FATF)
Location: World Bank Group MC Building, Preston Auditorium

11.00am - 12.15pm

Seminar: Inequality: managing the impact of globalisation and technology

Speakers: **Tao Zhang**, Deputy Managing Director, IMF; **Mauricio Cárdenas**, Minister of Finance, Colombia; **David Rubenstein**, Co-Founder and Co-CEO of The Carlyle Group; **Tharman Shanmugaratnam**, Deputy Prime Minister of Singapore; **Laura Tyson**, Professor, Haas School of Business, University of California, Berkeley
Location: George Washington University, Jack Morton Auditorium

12.00pm - 1.30pm

Seminar: Overcoming fragility: why jobs are key

Moderator: **Martin Wolf**, Journalist, *Financial Times*
Speakers: **Stefano Manservigi**, Director-General, International Cooperation and Development, European Commission; **Paul Collier**, Professor, University of Oxford; **Mohamed Omer Arteh**, Deputy Prime Minister, Somalia
Location: World Bank Group MC Building, Jim Wolfensohn Atrium

1.00pm - 2.30pm

Seminar: The shifting global economic and political landscape: fragmentation or integration

Moderator: **Rana Foroohar**, Assistant Managing Editor, *Time*
Speakers: **David Lipton**, First Deputy Managing

Director, IMF; **Ian Bremmer**, Global Research Professor, New York University; **Kevin Rudd**, President, Asia Society Policy Institute; **Lars-Hendrik Röller**, Chief Economic Advisor to the German Chancellor
Location: George Washington University, Jack Morton Auditorium

1.30pm - 3.00pm

Seminar: Toward a more integrated East Asia: economic corridors and infrastructure connectivity

Moderator: **Danny Leipziger**, Managing Director, Growth Dialogue
Speakers: **Sri Mulyani Indrawati**, Minister of Finance, Indonesia; **Quan Zheng**, Director-General, Asian Infrastructure Investment Bank; **Laura Tuck**, Vice-President, Sustainable Development, World Bank; **Victoria Kwakwa**, Vice-President, East Asia and Pacific Region, World Bank
Location: World Bank Group J Building, J B1-080

2.30pm - 4.00pm

Seminar: Fragility and conflict: addressing the causes and consequences

Moderator: **Raj Kumar**, DEVEX
Speakers: **Caroline Heider**, Senior Vice-President, Internal Evaluation Group, World Bank Group; **Mark Malloch-Brown**, Chair, Business and Sustainable Development Council; **Christiaan Rebergen**, Director-General for International Cooperation, Ministry of Foreign Affairs, The Netherlands; **Valerie Amos**, Former UN Under-Secretary-General for Humanitarian Affairs and Emergency Relief Coordinator, and former Secretary of State for International Development, UK; **Christoph Zurcher**, Professor, Graduate School of Public and International Affairs, University of Ottawa; **Laura Frigenti**, Director, Agency for Development Cooperation, Ministry of Foreign Affairs, Italy; **Jian Eliason**, Deputy Secretary General, United Nations; **Alain Bifani**, Director General, Ministry of Finance, Lebanon; **Ustavo Gonzales**, UNDP Sub-regional Development Coordinator for Syria
Location: World Bank Group MC Building, Preston Auditorium

3.00pm - 4.15pm

Seminar: Catalysing private finance for development

Moderator: **Jane Nelson**, Director of Corporate Social Responsibility Initiative, Harvard Kennedy School

Speakers: **Jim Yong Kim**, President, World Bank Group; **Priti Patel**, Secretary of State for International Development, UK; **Kaifala Marah**, Governor, Central Bank, Sierra Leone; **Jose Carlos Ugaz**, Chair of the Board of Directors, Transparency International; **Joaquim Levy**, Managing Director and CFO, World Bank Group; **Philippe le Houerou**, Executive Vice-President and CEO, IFC; **Thierry Deau**, Chairman and CEO, Meridiam
Location: World Bank Group MC Building, Jim Wolfensohn Atrium

4.15pm - 5.30pm

Seminar: Making Trade: an engine of growth for all

Moderator: **Shawn Donnan**, World Trade Editor, *Financial Times*
Opening Remarks: **Christine Lagarde**, Managing Director, IMF; **Roberto Azevedo**, Director-General, World Trade Organisation; **Jim Yong Kim**, President, World Bank
Speakers: **Chrystia Freeland**, Minister of International Trade, Canada; **Doug Irwin**, Professor, Dartmouth College; **Peter**

Mandelson, Former EU Trade Commissioner; **Ernesto Zedillo**, Former President of Mexico
Location: IMF HQ1 Atrium

4.30pm - 6.00pm

Seminar: One year of the SDGs: country action and progress

Moderator: **Mahmoud Mohieldin**, Senior Vice-President for the 2030 Development Agenda UN Relations and Partnerships, World Bank Group
Speakers (Panel one: Global Response, Partnerships and South-South Cooperation): **Peter Thomson**, President, UN General Assembly; **Thomas Silberhorn**, Parliamentary State Secretary to the Federal Minister for Economic Cooperation and Development, Germany; **Mauricio Cárdenas**, Minister of Finance, Republic of Colombia; **Werner Hoyer**, President, European Investment Bank (Panel two: SDGs Implementation: National and Domestic responses); **Sahar Nasr**, Minister of International Cooperation, Arab Republic of Egypt; **Jon Lomoy**, Director-General, Norwegian Agency for Development Cooperation (Norad); **Helen Clark**, Administrator, UN Development Programme
Location: World Bank Group MC Building, Preston Auditorium

OfNote

2016 Brazil Economic Conference

8.00am - 2.30pm

Brazilian/American Chamber of Commerce

In partnership with Brazil/US Business Council; Wilson Center

Speakers: **Henrique Meirelles**, Minister, Ministry of Finance, Brazil; **Ilan Goldfajn**, President, Central Bank of Brazil; **Robson Braga de Andrade**, President, Confederação Nacional da Indústria-CNI; **Monica Baumgarten de Bolle**, Senior Fellow, Peterson

Institute for International Economics; **Dan Bryant**, Senior Vice President for Global Public Policy and Government Affairs, Walmart; **Helio Magalhães**, President, Citigroup Brazil; **Marcelo Neri**, Economist, Fundação Getúlio Vargas; **Paulo Cesar de Souza e Silva**, President and CEO, Embrapa SA; **Paulo Vieira da Cunha**, Partner, Verbank Agriculture and Verbank Consulting, LLC
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Location: Ronald Reagan Building and International Trade Center, 1300 Pennsylvania Ave NW



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Saturday, 8th October

Food and drink will be served
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Finance Minister & Central Bank Governor of the Year

East Asia Pacific | South Asia | Middle East & North Africa | CEE | Sub-Saharan Africa | Latin America | Caribbean

Best Sovereign DMO & Best Government Infrastructure Strategy

DownTime ExtraCurricular

6.00pm – 9.00pm

Reception

Hosts: **The Federation of Egyptian Banks**
Patron: **Tarek Amer**
Location: Crystal Room, Willard Intercontinental Hotel, 1401 Pennsylvania Ave NW

6.30pm – 8.30pm

Reception

Hosts: **Bank of America Merrill Lynch**
Location: National Gallery of Art, East Building, 4th entrance

7.00pm – 10.00pm

Reception

Hosts: **The Banks Association of Turkey**
Location: Andrew W Mellon Auditorium, 1301 Constitution Ave, NW

Institute of International Finance (IIF) 2016 Annual Membership Meeting

Location: Ronald Reagan Building and International Trade Center, Washington, DC

Lead Sponsor: **PwC**; Anchoring Sponsors: **Abu Dhabi Global Market; BNP Paribas; QNB; S&P Global**; Supporting Sponsors: **DBS, IBM, Moody's Investors Service**; Contributing Sponsors: **FitchRatings, Shearman & Sterling, Swift**

Location: Amphitheater

Host: **Ben White**

8.15am – 8.30am

Welcome: **Tim Adams**

8.30am – 9.30am

The Global Outlook from the C-Suite: Mary Callahan Erdoes, Gary Cohn, Sergio Ermotti, Piyush Gupta, Martin Wolf (moderator)

9.30am – 10.30am

Europe: Views from the C-Suite: Ana Botin, Howard Davies, Douglas Flint (moderator), Jean Lemierre, Douglas Peterson, Andreas Treichl

10.30am – 11.15am

In Conversation: **Stanley Fischer, Tim Adams**

11.15am – 12.00pm

Conversation/Keynote

12.00pm – 1.45pm

Lunch: **Bank CEOs: Views from the US:** (Atrium Hall) **Tim Adams (moderator), Michael Corbat, Jamie Dimon, James Gorman**

2.00pm – 2.50pm

Europe Outlook: **Anna Breman, Janet Henry,**

Erik Nielsen, Simon Nixon (moderator), Peter Praet

3.00pm – 3.50pm

In Conversation: **US Economic Outlook:**

Esther George, John Taylor

4.00pm – 4.50pm

Japan Economic Outlook: **Michael Green, Takatoshi Ito, Jacob Schlesinger (moderator), Hajime Takata**

5.00pm – 5.50pm

China Economic Outlook: Assessing the Risks: **Johanna Chua, Brian Coulton, David Dollar, David Loevinger (moderator), Markus Rodlauer**

Location: Atrium Ballroom A

Host: **Ambassador Kristen Silverberg**

2.00pm – 2.50pm

Regulation and Innovation: **Richard Tang, Sopnendu Mohanty, Andrew Bailey, José Manuel González-Páramo, Ian Narev (moderator)**

3.00pm – 3.50pm

Innovation in Payments: **Jim McCarthy, Harry Newman, Braden More, Conan French (moderator), Daniel Marovitz,**

4.00pm – 4.50pm

Blockchain: **Lael Brainard, Caitlin Long, Carolyn Wilkins (moderator)**

5.00pm – 5.50pm

Innovation in Insurance: **Solmaz Altin, Stephen O'Hearn (moderator), Kurt Karl, Zia Zaman**

Location: Atrium Ballroom B

Host: **Host: Andrés Portilla**

2.00pm – 2.50pm

Market Liquidity: **Craig Broderick, Richard Lacaille, Nicholas Silitch, Hung Tran (moderator), Richard Berner**

3.00pm – 3.50pm

Evolving International Insurance Regulation: **George Brady (moderator), John Hele, John Huff, Yoshihiro Kawai, Christian Thimann**

4.00pm – 4.50pm

Bank Capital: A Revised Basel Framework **William Coen, Adam Gilbert, Frédéric Oudéa, David Rule**

5.00pm – 5.50pm

Ensuring Robust Financial Market Infrastructure: **Michael Bodson, Andrew Gracie, Marnie Rosenberg, Barbara Novick, Reena Sahni (moderator)**

6.00pm – 8.00pm

Campaign Cocktails: US Presidential Election (Atrium Hall) **Charlie Cook, Stuart Rothenberg**

NextDoor

10:30am – 11:30am

Roundtable Discussion: **U.S.-India**

Collaboration on Infrastructure

With: **Raghav Chandra, Chairman, National Highways Authority of India**
Location: **USIBC, 1615 H St NW, Washington, DC 20062**

Contact: **Hemal Shah (hshah@usibc.com)**



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Trade

Continued from page 1

Elsewhere, the Regional Comprehensive Economic Partnership, which conjoins 16 Asian nations including China, India, Japan and Indonesia, remains waterlogged, having earlier been slated for completion by early 2016.

“Every major trade agreement is running into obstacles,” said Paul Sheard, chief global economist at Standard & Poor’s. “Look at TTIP and TPP, two trade deals you would think would just sail through. Yet they are struggling, in large part because they embody another facet of the ongoing backlash against globalisation and free trade.”

In an interview with *Emerging Markets*, IMF managing director Christine Lagarde connected the failure of those two deals, which have limped along for years, with the widespread pushback against globalisation, and the rise of populist leaders feeding on the fears of fretful electorates.

“What we are seeing at the moment is a reversal...[of] the relatively free and unencumbered flow of goods and services on the basis of existing or international trade arrangements,” she told *EM*. “There are populist voices around in various countries, and not just in the United States, calling for withdrawing behind borders, limiting the flow of goods and services, hindering the flow of people where people could move freely.”

TRUMP/CLINTON UNITY

Advocates of a free trade deal have been particularly disappointed by the tone of the US presidential campaign where Republican contender Donald Trump has called for the US to withdraw from TTP talks and to renegotiate the North American Free Trade Agreement (Nafta). Democrat candidate Hillary Clinton, once a supporter of TTP, has also called for a US exit.

The same problem bedevils intra-regional economic alliances. In Latin America, Mercosur is as good as dead in the water. And in Europe, until a few years ago a model of economic and social stability and harmony, Britain’s majority decision to leave the union has left the world’s largest trading block in what European Commission president Jean-Claude Juncker terms an “existential crisis”.

However, some global leaders were not willing to give up on the supersized trading block. Brazilian finance minister Henrique Meirelles told *Emerging Markets* that trade partnerships were “still relevant”, and added that while the pushback against them was completely “natural”, given the uncertain nature of the global economy, he believed the public revolt against free trade and globalisation would pass. “At some point, this will be part of the past.”

Others were looking to smaller deals such as the Free-Trade Area of the Asia Pacific (FTAAP) that has been on the drawing board since the previous decade and has been pushed aggressively by China since 2014. Peruvian president Pedro Pablo Kuczynski, host of the upcoming APEC leaders’ summit, said the FTAAP faces headwinds, but he remains optimistic that leaders will see it as an even better idea than the other pacts.

“I think it (FTAAP) is a very good idea. It is better than having bits and pieces like the TPP, which is a huge piece, but not the whole. I told the Chinese that we would welcome this,” he told *EM*.

THE final word

Resolving the climate paradox

By Mark Carney

In addressing the financial stability risks from climate change, financial policymakers face two paradoxes.

First, the future will be past. That is, climate change is the tragedy of the horizon which imposes a cost on future generations that the current one has no direct incentive to fix, with its catastrophic impacts felt beyond the traditional horizons of most actors including businesses and central banks. Once climate change becomes a clear and present danger to financial stability it may already be too late to stabilise the atmosphere at two degrees.

Second, success is failure. That is, too rapid a movement towards a low-carbon economy could materially damage financial stability. A wholesale reassessment of prospects, as climate-related risks are re-evaluated, could destabilise markets, spark a pro-cyclical crystallisation of losses and lead to a persistent tightening of financial conditions: a climate “Minsky moment”.

Building new markets – in climate transition and green finance – can help resolve the tragedy of the horizon. Over the past year, the focus of G20 Leaders and the aegis of the Financial Stability Board (FSB) have spurred important progress. The upcoming German presidency of the G20 now has a historic chance to mainstream climate finance and turn risk into opportunity.

To add impetus, there is a growing macroeconomic case for action. Throughout this decade, global growth has serially disappointed as the combination of huge debt overhangs, profound demographic changes and enormous uncertainties have weighed on activity. Nominal growth in the euro area, the UK and globally is running at half of its pre-crisis rate. Growth has been weak despite significant progress repairing the financial system, recent moves to somewhat expansionary fiscal policies in a number of countries, and years of unprecedented monetary policies.

Growth has been restrained, in part, by risk aversion stemming from elevated geopolitical, economic and policy uncertainty. Business investment across advanced economies has fallen by more than 2.5 percentage points of GDP, creating substantial investment shortfalls relative to pre-crisis trends. Businesses and investors appear to be hedging future disaster risk: equity risk premia are unusually high and government bond yields are consistent with very low growth for a very long time.

In this context, green finance is a major opportunity. By ensuring that capital flows into green and long-term projects, growth can be increased and financial stability promoted. By absorbing excess, global saving, equilibrium interest rates can be raised and macroeconomic stability enhanced.

GREEN FINANCE

For investors, green bond markets offer a stable, rated and liquid investment with long duration. For issuers, green bonds are a way to tap the huge US\$100trn pool of patient private capital managed by global institutional fixed-income investors. For this to happen, however, green finance cannot conceivably remain a niche interest over



the medium term – currently, green bonds account for less than 1% of holdings by global institutional investors.

Encouragingly, the green bond market is gradually gathering speed. Annual issuance rose from just \$3bn in 2012 to \$42bn in 2015. It could double this year with issuers ranging from US regional authorities raising funds domestically to invest in water projects, to Chinese and Indian corporates. Green bonds are being issued in a range of currencies, in major financial centres, including London, to finance a broad range of low carbon projects.

To reach escape velocity, market participants and public authorities must coordinate to deliver common green bond frameworks and definitions, and other

necessary supporting infrastructure for local and cross-border markets. One specific initiative is the development of a ‘term sheet’ of internationally recognised standardised terms and conditions for green bonds. Authorities are now working with the private sector to that end.

FINANCIAL STABILITY

While the transition to a low-carbon economy has many opportunities, an abrupt resolution of the tragedy of the horizons is in itself a financial stability risk. Sudden changes in policy, technology and physical risks could prompt a reassessment of asset values as costs and opportunities become apparent.

An obstacle to a smooth adjustment has been the absence of information to help market participants make a market in climate-related financial risk.

In late 2015, at the request of G20 Leaders, the FSB established an industry-led Task Force, under the leadership of Michael Bloomberg. It is developing recommendations for voluntary, consistent, comparable, reliable and clear disclosures around climate-related financial risks for companies to provide information to lenders, insurers, investors and other stakeholders.

If firms were to make public sufficiently forward-looking and granular information, offering real insight into how climate-related risks and opportunities may impact a firm’s existing and future business lines, including against appropriate transition scenarios, a market in the transition to a two-degree world can be built.

This will help smooth price adjustments as opinions change, rather than concentrating them at a single climate “Minsky moment”. And it would allow feedback between the market and policymaking, making climate policy a bit more like monetary policy, with policymakers learning from markets’ reactions, and markets internalising policymakers’ objectives, strategies and instruments.

By mainstreaming green finance and managing what gets measured, we can help resolve the tragedy of the horizon.

Mark Carney is Chair of the Financial Stability Board and Governor of the Bank of England. This column is based on a speech given by Mr Carney at the Arthur Burns Memorial Lecture, Berlin, on 22 September 2016.

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