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GREEN ECB
Lagarde plunges in
PAGES 10-11

LATAM
Lessons in debt restructuring
PAGES 12-13

INDIA
Covid battle
PAGES 16-17

NEWS

Putting the humanity back into capitalism 3

Former Malpass sceptics notice a green tinge 4

Rule of law deal provides a test for the Union 4

Indonesia reaches out to all sources for funding 4

Fiscal recovery at peril in fiery LatAm 5

Legal row puts Ukraine's $5bn in doubt 5

Renminbi finds friends in post-Covid world 5

IMF urges 'early and decisive action' on debt restructuring 21

Best of 2020
GM Awards
The Middle East
Page 14-15

Biden victory to boost Asia but China tensions to remain

By Rashmi Kumar and Oliver West

US presidential candidate Joe Biden's rising lead in the polls is being seen a positive signal for Asian economies outside China that would benefit from a new face in the White House.

Market watchers in Asia are taking stock of the possible ramifications to growth and their economies. According to Shaun Roache, Asia Pacific chief economist at S&P Global Ratings, there can be some good news coming the way of countries in the region.

He predicts a Biden win will bring big capital inflows into Asia, a demand pick-up and easing of financial conditions — all of which will be much needed.

"I think it provides a big tailwind, particularly at a time when a lot of relief measures that we've seen [due to Covid] are going to start tapering, which is when you need some external push to help the economy," said Roache "And at the moment, it looks as though… we might get that from the US."

Steven Cochrane, chief economist for Asia Pacific at Moody's Analytics, added that Biden was likely to "re-engage" with the World Trade Organisation or maybe even join the Trans-Pacific Partnership.

However, China is unlikely to share in the change of fortunes. "No matter who wins the

Continued on page 21

Biden: might bring a more multilateral approach

Exclusive

IADB to roll out hurricane clauses as small state pleas gain traction

By Oliver West

The Inter-American Development Bank could soon become the first multilateral lender to offer its borrowing countries the option to defer debt payments in the event of natural disasters, *GlobalMarkets* has learned.

The move comes amid Caribbean policymakers'

Continued on page 3

IMF will need Bank's help to fulfil climate ambition

By Jon Hay

The International Monetary Fund realises it needs to up its game on climate change and is hiring staff. But specialists say it can only fulfil this new area of its work properly if it restarts a stalled partnership with the World Bank.

"On climate we are trying to step up a lot," said James Roaf, the new co-ordinator of climate change policies in the IMF fiscal affairs department. "It's macro-critical in its effects," meaning critical to macroeconomic performance.

The impacts are varied. Climate-related hurricanes devastated parts of the Caribbean in 2017. Countries need to invest in infrastructure to protect themselves from floods and droughts. Hydrocarbon producers face falling demand and

Continued on page 3

Roaf: stepping up

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Success is a journey

IMF

Continued from page 1

prices. China has committed itself to net zero emissions in 2060, but needs to finance that. European countries have been asking the IMF to advise them on similar issues.

"Climate has been a huge blind spot of the IMF," said Jon Sward, environment project manager at the Bretton Woods Project, an NGO observing the World Bank and IMF. "In many countries it has been promoting export-led growth which is quite carbon-intensive and sometimes leads to deforestation. We've been discussing with IMF shareholders about this and they agree the IMF needs to see climate as macro-critical."

Beginning when Christine Lagarde was managing director, but particularly in the past year under Kristalina Georgieva, the Fund has been trying to rectify its severe shortage of climate experts.

Climate is not an issue where the IMF can just passively analyse the effects. It needs to help countries mitigate climate change and prepare for it.

"The idea is to mainstream climate within our country teams," said Roaf. "We want them to be able to deepen their engagement with central banks and country authorities, to advise and discuss climate issues in all our member countries."

Every year the IMF produces a surveillance report on each member, which includes a Debt Sustainability Analysis (DSA). Climate issues can be factored in, but the framework is not specifically built to encourage that.

More fundamentally, the Fund lacks the necessary skills. Calculating a country's climate needs requires detailed assessment of energy, agriculture, transport, weather and many other issues.

"The more the IMF gets into climate change, the more they will expose themselves, because they need credible access to sector knowledge," said Carter Brandon, a senior fellow at the World Resources Institute who advises the IMF.

The Bank and Fund only work together on three areas: DSAs, Financial Sector Assessment Programmes — another part of surveillance reports — and the Highly Indebted Poor Country programme. On these tasks, they pool complementary skills: the World Bank's sectoral and longer term view, the IMF's knowledge of short term liquidity and debt pressures.

Post-Covid world will demand 'new more humane' capitalism

By Jon Hay

The coronavirus pandemic is emboldening those who call for capitalism to be reformed to make it more responsive to society's needs, and less destructive of the planet. But for that to be more than fine words, investors will have to make difficult choices.

"Covid is bringing everything forward," said Larry Fink, CEO of BlackRock, at the World Bank/IMF annual meetings this week. "Very large macro trends that might have taken 10 years have been truncated into seven to nine months."

The private sector is eager to show it is behind this movement. Deutsche Bank found US companies mentioned inequality 80% more in public communications in the third quarter of 2020 than a year ago.

But words alone do not constitute change. Leonardo Martinez-Diaz, global director of the sustainable finance centre at the World Resources Institute, said the coronavirus had exacerbated "the very clear distinction between those who had assets and could invest and take advantage of lower asset prices and the tech boom, and those left out of it entirely."

He added: "If we're going to have a new, more humane capitalism, we have to figure out how to insulate those who have least ability to cope with shocks. We can't just return to the old safety nets of the 20th century — unemployment insurance, health insurance, pensions."

He pointed to a scheme in Kenya in which people were issued with biometric cards they could use to buy food in times of famine. The government can claim on an insurance policy to provide a surge of money. Schemes like this could build resilience into the system to help people endure shocks without having to wait for politicians to pass support packages.

Leonardo Martinez-Diaz: "We can't just return to the old safety nets of the 20th century"

Courtesy of Center for American Progress

STRONG ECONOMY, STRONG SOCIETY

Meanwhile, the mainstream of the economy will continue to be owned, and therefore governed, by investors. "Can capitalism be retooled? Of course it can," said Wolfgang Kuhn, director of financial sector strategies at ShareAction, an NGO. "Society just needs to be more careful when giving out licences to operate to business. It is all about economic players taking responsibility for their adverse impacts on people and planet."

Bruce Davis, co-founder of Abundance, a UK ethical crowdfunding platform, said finance should not just mean extracting wealth, but creating value, "which needs to be economic and social, because our resilience is a function of the two and they are co-dependent. A strong society needs a strong economy, but vice versa too."

Institutional investors "will have to move money into new places and look at assets and instruments that are not part of" liquid markets.

IADB

Continued from page 1

calls to make debt more resilient to climate events gain traction.

The IADB is planning to roll out a so-called "hurricane clause", which would allow borrowers to defer principal payments on eligible loans for two years after an eligible event, through its Flexible Financing Facility. The option would be available on both new and existing loans.

The IADB confirmed to *GlobalMarkets* it was working on the option, saying that details were "still being worked out". It is aimed at small Caribbean and central American nations, several of which have suffered extreme economic destruction as a result of hurricanes in recent years — and many of which have very high debt levels.

"Finally, our small states which often seem invisible are being heard," Timothy Antoine, governor of the Eastern Caribbean Central Bank, the monetary authority for the members of the Organisation of Eastern Caribbean States, told *GlobalMarkets*.

"I welcome this move by the IADB. It is the right and appropriate thing to do. I applaud the IADB on its leadership as the first multilateral to proceed with this clause."

Moreover, Antoine said that disaster-linked clauses "should be standard in all sovereign debt contracts" in the Caribbean, as policymakers seek to deliver an effective response to the climate crisis and build resilience.

NOT A DEBT REDUCTION

Hurricane clauses first appeared when Grenada restructured its bonds in 2015, with Barbados following in October 2019 with its own bond restructuring. Barbados prime minister Mia Mottley had told *GlobalMarkets* at the time that small island states, especially, needed to make their debt more resilient to climate events, and pledged to take her workings to the IADB and Caribbean Development Bank.

Mottley's prompting seems to have had the desired effect with the IADB.

"We are convinced that the use of such counter-cyclical features will come to be seen as one of the main ways of making debt structures more resilient," said Sebastian Espinosa, managing director at White Oak Advisory, which advised Barbados and Grenada on their restructurings.

However, the option proposed by the IADB would not constitute a debt restructuring, *GlobalMarkets* understands, and is not related to a country's level of debt.

Antoine: "I applaud the IADB on its leadership"

Courtesy of the Caribbean Development Bank

"We would like to emphasise that this offering will imply no change to our financial policy framework and that any option would be offered against a fee and as long as the bank is able to accommodate it while retaining its strong financial footing," said the IADB in a statement provided to *GlobalMarkets*.

Insurance and reinsurance markets are generally too expensive for small Caribbean island nations, while calls for a regional catastrophe bond — such as that used by the Pacific Alliance countries to provide insurance against earthquake risk — have not gained traction.

EU bid to tie recovery fund to rule of law triggers row with Eastern bloc

By Lewis McLellan

Poland and Hungary are preparing to face down the rest of the European Union over the question of imposing rule of law conditions for the allocation of EU recovery funds.

Economists expect that the EU will blink first, but that doing so could lead to a weakening of the EU's power to oversee the use of funds.

The EU Council, currently under a German presidency, submitted a budget proposal making the receipt of recovery funds contingent on adherence to rule of law standards, sparking outrage from Poland and Hungary.

There is strong support in the European parliament to make the funds in the Next Generation EU recovery fund conditional on the rule of law. Jörg Kukies, the German deputy finance minister, said on Tuesday that parliament was seeking a stronger role in the governance of the recovery fund.

Kukies said: "The rule of law is still the most difficult debate facing the EU budget," during an IIF webcast on Tuesday.

Claus Vistesen, chief eurozone economist at Pantheon Macroeconomics, said it was clear that the European parliament had a "genuine desire to go beyond economic oversight and budgetary rules".

Poland's Elzbieta Witek and Hungary's Laszlo Kover (both speakers of their parliaments) met in Poland and, on Wednesday, announced a joint stance that they would not support an EU budget that included clauses to make funds contingent on adherence to the rule of law.

Vistesen said that the stand-off was unlikely to lead to a veto from the holdout countries, saying: "The likeliest outcome — the path of least resistance — is that the issue is fudged away."

BUDGET DELAY FEAR

But he laid out another possible outcome. "It's no coincidence the rule of law has become an issue," he said. "Some of the northern European countries want to make rule of law an issue and could push back on any budget without rule of law conditions. If that happens, the situation could become dicey very quickly for any opposing holdouts like Poland and Hungary."

Kukies: parliament wants stronger role in fund governance

If Poland and Hungary do end up holding up the EU budget, Vistesen believes they could become politically ostracised and, in extreme circumstances, be stripped of voting rights by a qualified majority under article seven proceedings.

However, this is the less likely scenario when compared with the possibility of the presidency submitting a budget proposal with a weaker link to the rule of law, acceptable to all nations.

Malpass begins to thaw on climate change

By Jon Hay

World Bank watchers have noticed David Malpass, its president, becoming more vocal on climate change of late. The Bank is not proposing any major change in policy, but if there is a more relaxed attitude at the top, it could free staff to push harder on some climate initiatives.

Some believe Malpass, appointed by President Trump in April 2019 after the abrupt departure of his predecessor Jim Yong Kim, may be repositioning to improve his chances of remaining in office if Joe Biden wins the US presidency.

Other stakeholders are pushing for a greener World Bank, too. On Wednesday ministers from six European countries and the EU wrote an open letter calling on the Bank and IMF to deliver "clear results on a green and inclusive recovery" and phase out oil and gas investments.

As Malpass had advised Trump in his 2016 campaign and been Treasury undersecretary, responsible for the multilateral development banks, insiders feared he would try to revolutionise the Bank.

But Malpass impressed colleagues by not reorganising the Bank or overturning its policies on climate change and fossil fuels, making conciliatory noises to China and being easy to work with.

"The World Bank hasn't been backsliding on its existing commitments," said Jon Sward, environment project manager at the Bretton Woods Project, an NGO monitoring the World Bank and IMF. "But in a sense it has been standing still, while other MDBs have been putting together more ambitious policies on mitigation."

The Bank's communications on climate have been muted under Malpass. Although the World Bank committed in 2015 to align with the Paris Agreement and is part of a joint MDB process working on Paris alignment, it rarely mentions the Paris Agreement publicly. Trump decided in June 2017 to pull the US out of the agreement.

Last year, the World Bank's Action Plan on Climate Change Adaptation and Resilience did not mention Paris. Lifelines, a big report on resilient infrastructure, mentioned it once.

A joint Framework and Principles for Climate Resilience Metrics in Financing Operations, published by all the major MDBs last year, was not endorsed by the World Bank, though staff are understood to have pushed for this.

However, Malpass has tweeted about climate change several times recently, and in a speech last week he said: "I'm happy to say that, in fiscal year 2020, my first full year as president, the World Bank Group made more climate-related investments than at any time in its history." The group is the largest multilateral climate financier, having committed $83bn in the past five years.

Malpass: proud of record green investments

Sward said Malpass's references to a low carbon recovery were the first time he had spoken so explicitly about climate change mitigation.

Sonia Dunlop, senior policy adviser at E3G, the climate change thinktank, said: "It's good to see Malpass starting to pay more attention to this issue — it's something we'd encourage him to do more as part of supporting a green recovery."

Indonesia uses 'all available resources' for Covid response

By Matthew Thomas

Indonesia has taken a creative approach to funding its response to the coronavirus, leaning on the central bank, multilateral lenders and international investors. But the country has stopped just short of officially billing its bonds as pandemic response deals.

Indonesia's government has made drastic changes in response to the coronavirus, abandoning a plan to relocate the capital from Jakarta to East Kalimantan, removing a 3% budget deficit cap for the next three years and committing Rph695tr ($47.17bn) of fiscal stimulus, worth around 4% of the economy. That has led to a sharp rise in funding needs at the sovereign, forcing the country's funding team to think on their feet.

"We have used all available government resources," said Luky Alfirman, director general of budget financing and risk management at Indonesia's ministry of finance. "We have used an excess cash surplus accumulated in previous years. We have sold bonds to the central bank. We have tapped the international markets. We also worked together with our partners, getting bigger loans than we have in previous years."

The move to sell bonds to Bank Indonesia, the central bank, has been the key tactic to increase available funding onshore.

TAPPING THE MARKET

Indonesia has also tapped the offshore bond market multiple times. The country raised around $3bn between dollar and euro tranches in January, before the real impact of the pandemic was apparent. It followed that with a $4.3bn deal in April, a $2.5bn green sukuk in June and a ¥100bn Samurai bond in July.

The April bond was the closest Asia has come to having a proper pandemic response bond from a sovereign, but Indonesian funding officials stopped just short of giving it an official label, which would have meant appointing third-party opinion providers and setting out clearly the use of proceeds.

The country is also expecting a surge in loans from overseas. Indonesia typically obtains around $2bn of loans from a mix of policy lenders, including multilateral institutions.

Fiscal recovery at peril in LatAm amid rising political and social anger

By Oliver West

Increased social tensions and unpredictable politics in Latin America, the region worst-affected by Covid-19, could jeopardise the return to fiscal stability after the pandemic.

More than 45m additional people in Latin America and the Caribbean will fall into poverty as a result of the crisis, according to estimates from the UN. Petar Atanasov, co-head of sovereign research at Gramercy, told *GlobalMarkets* it was impossible to know the full impact of the pandemic on the region, and that governments would have to learn to deal with the poverty increase.

"Latin America was already seeing major social unrest, and it would appear very difficult to avoid political and social upheaval in some countries as we emerge from Covid-19," he said. "Most of the region is susceptible."

Chile, Ecuador and Bolivia — among others — saw mass protests and violence in the final months of 2019 before Covid-19 lockdowns mostly halted them. Yet unrest returned in recent weeks across the continent and could complicate efforts for fiscal consolidation post-crisis.

"[Prospects for] fiscal consolidation are very much on my mind," said Sarah Glendon, senior Latin America analyst at Columbia Threadneedle Investments. "We will be emerging from a huge crisis, some countries face double-digit unemployment rates and the informal sector is large.

"In these circumstances, it's hard to imagine fiscal belt-tightening — especially in election years."

Moody's said on Monday that EM sovereigns would suffer "long-lasting revenue losses" from coronavirus, with governments' ability to implement revenue-raising measures set to be a "key credit driver".

"Countries are going to have to start talking about things like tax reform, and when they do finally get to fiscal consolidation, there is a risk it sparks further unrest," Glendon told *GlobalMarkets*.

POPULISM RISING

Most of Latin America entered the crisis in a weak fiscal position, and Fitch said this week that the median debt-to-GDP ratio in the region would rise by 13.5% this year and 4.6% in 2021. But with a wave of elections in the next two years, governments may not be willing to tackle the problem.

Mukherji:Recovery will be 'more challenging'

Brazil has implemented one of the world's largest stimulus programmes — at around 12% of GDP — despite limited fiscal space and debt fast approaching 100% of GDP.

"Brazil has arguably the most ambitious reform programme of any EM country," Joydeep Mukherji, head of Latin America sovereign ratings at Standard & Poor's, told *GlobalMarkets*. "But pulling back fiscal stimulus will be difficult and my main concern is that the political economy is not going to be conducive to the fiscal framework that they need."

Ukraine hopeful of unblocking $5bn IMF loan amid legal rows

By Lewis McLellan

The next tranche of Ukraine's $5bn IMF support programme has been delayed by a ruling from the country's constitutional court that could threaten the autonomy of the National Anti-Corruption Bureau (NaBu) amid several areas of contention that could cause friction for the deal.

But while the SDR500m ($858m) disbursement scheduled for September has been delayed, hopes are high that a compromise will be found soon.

Artem Shevalev, EBRD's board member for Ukraine, believes that the dialogue with the IMF will be easy to salvage "as long as there is strong and vocal support of NaBu and the rule of law from the highest level politically".

Ukraine's constitutional court in September deemed some of the provisions of the law governing NaBu unconstitutional. These provisions relate primarily to the president's powers to staff the bureau. NaBu believes the decision is "an attempt to block the fight against political corruption and stop the cleansing of the judiciary".

Yuriy Butsa, government commissioner for public debt management, believes that "it will take a few weeks to discuss the best approach.

"On the good side, the constitutional court decision did not undermine the current operations of the National Anti-Corruption Bureau," he said. "We have already agreed with the IMF that together with our international partners there should be piece of legislation developed that should reflect the Constitutional Court ruling."

'ALARMING SIGNAL'

NaBu was set up in 2015 with the backing of the IMF and the international community, and the court's decision "raised the concerns of our international partners, as well as inside Ukraine", said Butsa.

But the judicial challenge to Nabu is only one of the potential stumbling blocks for the IMF's continued support of Ukraine.

IMF experts are in negotiations with Ukrainian authorities to discuss the proposed budget. Sergey Nikolaychuk, head of macroeconomic research at ICU in Kyiv, said: "The deficit of 6% was not popular with the IMF." Nikolaychuk expects the negotiations to result in a new budget with a lower deficit.

Butsa: discussions will take 'a few weeks'

Furthermore, last week the IMF representative in Ukraine criticised the decision by the council of the National Bank of Ukraine to reprimand two of its board members.

The pair were the only two deputy governors on the NBU board who served under Yakov Smoliy, who resigned from the position of governor in early July, causing widespread concern in the international investor community.

Asia's policymakers look for renminbi push

By Rashmi Kumar

A rise in bond yields in China versus a fall in interest rates in the US and other developed economies this year has enticed more foreign investors into the Asian country's domestic fixed income market.

Additionally, the fact the People's Bank of China (PBoC) has not intervened in the foreign exchange market amid the Covid-19 pandemic — in stark contrast to its decision to depreciate the currency in 2015 — has also proven appealing.

"The PBoC is letting the exchange rate move around a little bit against the dollar and intervening less," Shaun Roache, Asia Pacific chief economist at S&P Global Ratings, told *GlobalMarkets*.

"Yet, they are not suffering the same sort of instability as in 2015/2016. In a world where public debt in the advanced economies is rising sharply, rates are at zero and there is a lot of QE, there is increasing appetite in China again to talk about the global role of the renminbi."

Roache added that policymakers in the rest of Asia were also weighing this up. "There is a feeling that some good can come if everybody can reduce their reliance on the dollar," he said. "In large part, that decouples you from the dollar cycle, which really dictates financial conditions across Asia Pacific."

Historically, the direction of the dollar has been important for Asian countries. When the dollar strengthens, the debt burden for sovereigns rises.

The renminbi has gained steam globally in recent years. The International Monetary Fund added the renminbi to its special drawing rights basket in October 2016, with the currency having a weighting of 10.92% versus the dollar's 41.73%.

The IMF's claims in renminbi rose from $212.8bn in the second quarter of 2019 to $230.4bn for the same time this year.

"Unpredictable policies, like the use of sanctions, have at the margin undermined the role of the dollar as an international reserve currency," said Stephen Schwartz, head of Asia Pacific sovereign ratings at Fitch.

"While dollar holdings by global central banks have barely budged, there has been an increase in RMB holdings. But while there is renewed interest in an alternative to the dollar, it's a very market-driven process and quite difficult to dislodge the role of the dollar at this stage."

CONTENTS FEATURES

12

Special sponsored section

8 **EIB REPORT III**
EIB MAKES CLIMATE FINANCE MAINSTREAM AS TAXONOMY UNLOCKS STANDARDS

The European Union's new green grammar book is multiplying the impact of climate finance. From funding to lending to innovation, the EU Taxonomy is helping embed climate throughout the European Investment Bank's activities

Economics & Policy

10 **CLIMATE CHANGE**
CENTRAL BANKERS TAKE THE LEAD

Long used to scanning the horizon for risks, central banks have belatedly woken up to the biggest one of all — climate change. Monetary policy has so far been ignored — but the European Central Bank, until now on the fringes of this issue, is plunging in

Regions & Countries

12 **LATIN AMERICA**
A TALE OF TWO SOVEREIGNS

Though Ecuador provoked admiration and Argentina exasperation as each restructured billions of dollars of bonds this year, the final agreements were not substantially different. However, the contrasting approaches to negotiations could be indicative of each country's chances of success

2020 GM Award Winners

14 **MENA**
THE REGION'S WINNERS

Mohammed al Jadaan, Saudi Arabia, Ziad Fariz, Jordan, and Fahad Al-Saif, Saudi Arabia

Regions & Countries

16 **ASIA**
INDIA'S COVID BATTLE

India's economic future is on shaky ground, after the Covid-19 pandemic dealt a blow to the country's already faltering growth. The impact of the fallout is likely to be felt for years to come — unless the government quickly changes tack

Agenda

20 **WHAT'S HAPPENING**
IN AND AROUND THE VIRTUAL ANNUAL MEETINGS

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European Investment Bank
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EIB makes climate finance mainstream as taxonomy unlocks standards

The European Union's new green grammar book is multiplying the impact of climate finance. From funding to lending to innovation, the EU Taxonomy is helping embed climate throughout the European Investment Bank's activities.

Climate finance and green bonds in particular have taken huge strides in recent years, with the EIB leading the way as the biggest capital markets issuer of the products. Green finance this year took another major legislative step forward, with the European Parliament approving the EU Taxonomy Regulation in June.

The EIB has been a key protagonist in the discussions that led to the taxonomy, and it celebrated the occasion by issuing a new Climate Awareness Bond while announcing the extension of the green funding programme to two new project areas that substantially contribute to climate change mitigation. It meant that lending in the project areas of research, development and deployment of low carbon technologies and to electric public transport can now be allocated from proceeds from the new CABs.

"The taxonomy is the first substantial attempt to define green finance and to lay down some really quite clear criteria that the market can use," says Nancy Saich, the EIB's chief climate change expert. "It doesn't dictate that every green product has to use the taxonomy; what the EU is saying is for every green product being sold you have to say how much aligns with the taxonomy."

Saich points out a huge part of the value of the taxonomy isn't just its clear definitions and language for what is green and sustainable, such as climate goals. It is the insistence of the taxonomy that, to be called green, any project must not cause significant harm to any of the goals, and must meet minimum social safeguards.

"To call something green, you must make sure it is resilient, you must show that you understand the risks of climate change to the project, investment or company and you have a plan for dealing with them," she says. "This is hugely powerful because it closes the door on saying something is green in one way, while undermining green in other ways."

She gives the example of wind farms that might have been built in national parks without proper environmental assessments — for instance, biodiversity assessments — or without meeting the minimum social safeguards — for instance, where land has been appropriated without due process and consent from the people living there.

"This is the really important angle: those kinds of things cannot be called green any more. Investors that want green want to know not just that they are making a substantial improvement but also that no harm is being done to other things."

DON'T BE SHY

The taxonomy that was agreed this year starts with a detailed dictionary and technical criteria for the two climate objectives, while work continues on the definitions under the environmental objectives. The EIB, however, has made sure that the documentation for its Sustainability Awareness Bonds, which it first issued in 2018, is also linked to the evolving EU legislation on sustainable finance and it has anticipated the adoption of the EU Green Bond Standard.

Nancy Saich: "The taxonomy is the first substantial attempt to define green finance and to lay down some quite clear criteria"

It's another example of the EIB taking the lead, as it did in 2007 with the first Climate Awareness Bond. The structure used 13 years ago didn't take off, but that didn't stop the EIB returning with what has evolved into the today's global standards.

"One should not be too shy," says EIB president Werner Hoyer. "You need to have some courage and some good ideas. When we entered the market with the first green bonds ever in 2007, we wouldn't have believed it would be so successful within just a few years."

Being able to reassure investors that what they are buying is indeed going to be put to use for the stated purpose has been central to the success of the EIB's green and sustainable funding programme, he says.

"For us as an institution, we depend on investor support, upon the trust of investors to give €60bn to €100bn every year in bond sales," he says. "When they buy a green bond from us, they must know that what is painted green must contain green — and this is true for the other objectives which we are now pursuing with issuance, in pursuit of the Sustainable Development Goals of the United Nations.

"There will be ample opportunity among investors around the world to put some part of their assets — their wealth — into the objectives we are pursuing with the SDG, but they must be assured that the projects are economically viable and sustainable and that the money is going in the direction in which we have promised to bring it."

MAINSTREAMING CLIMATE

A sign of the commitment to put climate at the centre of everything the bank does was the establishment early in 2020 of a new division in the operations department. Elina Kamenitzer, head of the climate office, explains why it was established.

"We have very strong technical expertise that has been cultivated over the years in the climate space, but in order to enable us to reach

The EIB is supporting electric battery production company Umicore in the construction of a manufacturing plant in Nysa, Poland.

More than 1000 schools and health centres in Gambia will receive clean and reliable electricity for the first time thanks to solar micro-grids.

these ambitious goals we also needed to strengthen climate finance capacities in the front office business function," she says.

The office has two main elements to its mandate: first, to enable strengthening of the operational green financing capacities of the EIB's front office; and second, to facilitate the operationalisation of the EIB's climate policy framework — in other words, to mainstream climate at the operational level.

"The expectation is not that climate is sort of a separate business line, but that climate will be embedded in everything we do," she says. "Each and every banker has to have climate in mind when they are they are originating business and transacting. We are there to facilitate and enable the business development."

Embedding climate and sustainability in the bank's lending operations is, in a way, almost an outcome of the establishment of the green taxonomy and the bank's issuance of Climate Awareness Bonds.

The original eligibilities for CABs were established in 2007, when the hot topic was the EU's Energy Action Plan focused on renewable energy and energy efficiency. "That didn't change for more than a decade, largely because of the absence of an objective institutional and official way to classify and measure contributions to sustainability," says Aldo Romani, head of sustainable funding. "There are areas of controversy as to what is green and what is not, what is contributing and what is not. At the bank, this decision is not made in the finance directorate but in the projects directorate.

"This is the value of the taxonomy. It creates a shared compromise — a consensus that has an authority that no decision could that is made at the level of the individual intermediary, lender, issuer or investor."

The taxonomy, then, ensures that the capital markets' tail wags the front office dog.

"We are aligning our definitions and criteria for green with the EU taxonomy, which also implies some changes in what we count as climate, and what type of projects we are going to focus on in the green space, and how we are going to report and track our contributions," says Kamenitzer.

Saich echoes this view, saying that for many organisations issuing green bonds, what starts out as a capital markets project ends up engaging the entire organisation. "That also happened with the taxonomy. It started with the capital markets but ended up engaging all the different parts of the financial system," she says. "The fascinating thing about a green bond is it brings different parts of an organisation together and you bring together people on the financial side and on the technical side in a way that they never normally would."

INVESTING IN INNOVATION

The taxonomy has other important roles to play — even in the economic recovery from the Covid pandemic. With firms delaying or abandoning investment plans amid uncertainty, anything that reduces that uncertainty is a positive.

"One of the major impediments to climate-related investment by firms is uncertainty on regulation and taxation," says Debora Revoltella, EIB director, economics department. "Now, there is a lot to do around that, but the fact is that at the European level there is a common framework to set standards and provide incentives for firms," she says. "The taxonomy that is being deployed gives clarity on what can be considered for climate change mitigation and adaptation and gives clarity on the kind of instrument that will be incentivised."

Elina Kamenitzer: "Each and every banker has to have climate in mind when they are they are originating business and transacting. We are there to facilitate and enable the business development."

She also points out that the fiscal stimulus being deployed at national and European levels will be used, in part, to invest in decarbonisation and transformation.

For vice-president Ambroise Fayolle, who oversees climate and development at the EIB, this kind of investment is crucial for reaching the bank's climate targets.

"We have seen from studies and we know from experience that innovation has contributed significantly to meeting our climate objectives," he says.

He points to the Northvolt battery factory that the EIB is financing in Sweden and the offshore windfarm park that it is financing in Portugal as examples.

"These are projects that have a huge innovation component, which is also a risky one, and this is the role of the EIB as the EU climate bank to finance them.

"We know that if we want to reach the 2050 target for climate neutrality there will be innovations that we don't yet know, but we do know that they are going to be the types of project that will be extremely important for Europe to reach these targets and we need to finance them from a very early stage."

The kind of finance it is involved in is typified by Breakthrough Energy Ventures-Europe, a fund for very early stage projects, which the EIB has set up with the Gates Foundation.

"We see that our competitors in China and in the US are spending more on research and development in climate than we are in Europe and that is a worry — and why this is a target and an ambition for the Bank," he adds. ●

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Central banks and climate change: Lagarde becomes leader

Long used to scanning the horizon for risks, central banks have belatedly woken up to the biggest one of all — climate change. Monetary policy has so far been ignored — but the European Central Bank, until now on the fringes of this issue, is plunging in

By Jon Hay

"Whatever it takes." Those words of Mario Draghi's in 2012 reverberated with power. Politicians might dither, he implied, but the European Central Bank he led would "within our mandate… preserve the euro".

The ECB succeeded absolutely. With limitless monetary firepower, it drove back the bears snarling at the eurozone.

When the coronavirus pandemic struck, no one doubted that central banks would respond with an arsenal of policies to prevent a health and economic crisis becoming a financial one.

In late September Christine Lagarde, Draghi's successor, was able to declare "we have prevented a massive deterioration that would otherwise have been seen".

But behind Covid-19 lurks a far greater threat: climate change. Policymakers of all kinds have known it was coming since the 1980s, but barely lifted a finger. Now, it is inflicting damage on lives and assets that cannot be ignored. Nearly all governments have promised to take some action, and a few — including the EU, the UK and China — have grasped the nettle and set targets to reach zero net greenhouse gas emissions.

Financial specialists have grown used to central banks being the most potent and — from their point of view — rational actors on the scene. They naturally expect them to wield their magic to defeat this evil. But do they have the necessary might? And do they dare to use it?

GETTING TOGETHER

So far, central banks are not keen to talk big about what they can achieve in this field. But they are certainly doing a lot of talking.

Although each central bank has its own national mandate and operations (or, for the ECB, multinational), they are a community that likes to interact. Responding to climate change requires fresh thinking and policies not found in their classical toolboxes, and possibly reinterpreting or stretching their mandates. When venturing into the unknown, central banks feel there is safety in numbers.

The Central Banks' and Supervisors' Network on Greening the Financial System (NGFS), formed as a quiet club of eight central banks in December 2017, has swiftly become one of the most prominent and influential green finance organisations.

Its 72 members come from nearly all major economies. "It's clearly creating momentum in a lot of countries," says Orith Azoulay, global head of green and sustainable finance at Natixis in Paris. "It is one of those initiatives where you start to be remarked when you are not in it, rather than when you are, which is the sign of a successful initiative."

Among G20 members, only Argentina, India, Saudi Arabia and Turkey are not involved. From the US, the Dept of Financial Services of the State of New York has joined.

"Virtually all central banks and supervisors are starting to do something on the climate front, though the level varies very much," says Morgan Després, deputy head of financial stability at the Banque de

> *"One of the things that has made the agenda take off is that it's no longer the preserve of Europeans"*
>
> *—Nick Robins, professor in practice in sustainable finance, London School of Economics.*

> *"Monetary policy and climate change is probably the last frontier. When we started considering it two to three years ago, it was almost unthinkable to address the topic"*
>
> *—Morgan Després, deputy head of financial stability, Banque de France*

France, who heads the NGFS secretariat.

The early involvement of the People's Bank of China and Mexican and Brazilian central banks has been crucial, argues Nick Robins, professor in practice in sustainable finance at the Grantham Institute of the London School of Economics. "One of the things that has made the agenda take off is that it's no longer the preserve of Europeans," he says. "South Africa and China are more carbon-intensive economies than Europe, and emerging economies are the most exposed to physical risks. So the case for thinking it through very seriously is much greater in emerging economies."

The NGFS has produced a wealth of studies and documents to share best practices. Its achievements are particularly impressive in two areas. It has succeeded in making the central banking community accept that climate change is part of its remit, because it threatens financial stability.

But that does not mean central banks know how to tackle the problem — or even talk about it. The NGFS has started to provide a language, by showing how to break the issues down into parts and assess where and how they will impact the financial system.

The pinnacle so far is its detailed guide, published in June, to climate scenario analysis. It lays out three kinds of scenario: orderly transition, disorderly transition and hothouse world, in a total of eight versions.

Having standard scenarios is crucial if central banks, with their supervisory spectacles on, are to steer the banks and insurance companies they regulate away from climate risk.

The Banque de France is using one of the NGFS scenarios for a stress test that concludes in October — the second major one after a study by De Nederlandsche Bank in 2018.

SHOW ME THE MONEY

Central banks' supervisory sway over the whole financial system is probably the most potent way they can help society fight climate change.

But financial market specialists cannot stop eyeing the trillions of dollars central banks have printed in the past decade.

"Monetary policy and climate change is probably the last frontier," says Després. "When we started considering it two to three years ago, it was almost unthinkable to address the topic."

NGFS members at first saw no connection between climate change and monetary policy, and did not want to explore the issue.

Why central banks are so cautious in this area is difficult to explain, Després says: "Certainly it's to do with the fact that central banks are very keen to respect their mandates. They have a mandate on price stability and until recently the link between climate change and price stability did not seem that obvious."

Central banks have accepted that climate change is a risk to financial stability, but not price stability. Yet the idea that a climate-induced shock of financial instability could occur without price instability is almost absurd.

Very gradually, the conversation is moving. In June, after a lot of pushing internally, the NGFS published its first brief report on monetary policy. It covers how climate risks can affect price stability and influence how central banks set monetary policy, but does not explore how they could use monetary policy to drive the economy in a greener direction. Buried on the last page is a single sentence about this.

EMINENCE GRISE

So far, the ECB has kept a low profile on the climate. Oddly, considering that it directly supervises 114 large banks holding 82% of eurozone banking assets, it has left climate risk supervision to national central banks. It is now developing its own stress test.

Observers of the ECB say Draghi was not very supportive of the climate risk agenda — he paid lip service to it, but it was not a core part of his strategy.

However, Després says: "President Lagarde is really keen on doing something — it's now part of the ECB strategy review."

The ECB's first strategy review since 2003 is due to finish in mid-2021. The discussions are confidential, but one very significant fact is clear: the review itself is about monetary policy. This means the ECB is explicitly saying climate change has a bearing on monetary policy — not just prudential policy. The dark horse of the central banking climate race is making a late surge that could put it in the lead.

What form that could take is keenly debated. The best clue comes from Isabel Schnabel, an ECB executive board member, who in September gave possibly the most forthright and determined speech by any central banker about climate change so far.

Addressing monetary policy, she went far beyond the NGFS, arguing that "collective action, by governments, firms, investors, households and central banks, including the European Central Bank, is required to accelerate the transition towards a carbon-neutral economy and correct prevailing market failures".

Securities could be excluded from acceptable repo collateral if the issuer did not properly disclose its climate risks; the ECB could haircut more deeply securities with higher climate risks. The ECB could also reassess how it deploys its bond purchase programmes to better match a sustainable, rather than the present unsustainable, economy.

GREEN HANDOUTS

A proposal for greening the Targeted Longer-Term Refinancing Operation programme, put forward by Positive Money Europe and the Sustainable Finance Lab, will also be considered in the ECB's strategy review. TLTROs are the ECB's handouts of cheap loans to banks, to encourage them to lend.

The plan's authors argue a green TLTRO would encourage lending to sustainable activities, instead of stimulating unsustainable ones, as ECB monetary policy does now — and that this choice is permitted under the ECB's mandate.

Jens van 't Klooster, one of the writers, says a green TLTRO would be "more useful than a green Asset Purchase Programme". Whereas bonds are issued by big companies, "what is so great about a bank-based system is that it's all small things like house refurbishments — activities that wouldn't happen without funding."

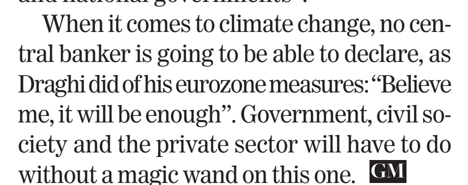
However, van 't Klooster admits that although a green TLTRO would give banks an incentive to make green loans, they would not have to pass on the cost benefit to the underlying borrowers.

At the moment, such ideas still seem too politically controversial for central banks to dare. But considering how far they have already moved — and how uninhibited a few leaders such as Schnabel have become — it is more than likely green monetary policy is on its way.

Robins points out some central banks and regulators, such as the Central Bank of Brazil, Reserve Bank of Australia and US Commodity Futures Trading Commission, are "taking their independence very seriously as they address climate and environmental issues and coming forward with policies that are very robust".

Schnabel sounds eager to get into the fray and "react pre-emptively". But even she argues climate change "requires collective and concerted action by all stakeholders, first and foremost by legislators and national governments".

When it comes to climate change, no central banker is going to be able to declare, as Draghi did of his eurozone measures: "Believe me, it will be enough". Government, civil society and the private sector will have to do without a magic wand on this one. GM



A tale of two sovereigns: negotiation attitudes foretell differing fortunes for LatAm restructurers

Though Ecuador provoked admiration and Argentina exasperation as each restructured billions of dollars of bonds this year, the final agreements were not substantially different. However, the contrasting approaches to negotiations could be indicative of each country's chances of success

By Oliver West

Countries do not usually gain friends when telling creditors they can't pay them back. Yet Ecuador earned serious plaudits as it went about restructuring $17.4bn of bonds this year. The Ad Hoc Bondholder Group that owned more than half of the sovereign's bonds even said that the process "set a precedent" for Covid-19 era restructurings.

Jan Dehn, head of research at Ashmore, part of the Ad Hoc group, explains that on one hand the group was referring to modifications in collective actions clauses that some creditors hope will become standard practice. Second, says Dehn, "Ecuador had one of the most mature approaches ever to a restructuring.

"From the beginning, Ecuador recognised that maintaining access to markets is important. There was a very honest, realistic assessment of the inability to pay owing to the oil price collapse, Covid, and an extraordinary sell-off in external debt."

A VALUABLE PROPOSITION

Richard Martínez, Ecuador's finance minister until he left for a senior role at the IADB in October, says the key to what proved to be a remarkably smooth process was not the economics.

"Negotiations are based on values," Martínez tells *GlobalMarkets*. "The numbers are somewhat secondary.

"Our values were clear: transparency, good faith, a strong defence of the state's interests, and being fair and balanced rather than falling into the trap of ideology."

Martínez says Ecuador "did not start by bartering over the numbers", saying that each side first had to agree on objectives.

"It was important for each party to sit in the other's chair for a moment," says Martínez. "It was agreed that Ecuador needed debt relief, but we also made clear that we understood the fiduciary responsibility of investors."

Still, the numbers were not pretty. Ecuador was running out of cash fast as it faced a healthcare crisis amid plummeting oil prices. With a $325m maturity due on March 24, Martínez faced a difficult decision.

To much political outcry, the government paid up — avoiding hard default to ensure continued access to the multilateral funding that would get it through the crisis. However, Martínez said he would not make looming coupon payments, instead entering grace periods and requesting bondholder consent to delay debt payments until August. This bought time for comprehensive restructuring discussions.

Though they faced losses, bondholders appreciated the approach.

"It strikes me as somewhat bizarre that a finance minister should get political heat for respecting a contract, as happened when he made the March payment," says Graham Stock, head of EM sovereign research at BlueBay, also a member of the Ad Hoc group. "This was a strategically sensible decision that helped talks develop more smoothly because Ecuador was not in default."

Indeed, in early July, just weeks after negotiations had begun, Ecuador reached an agreement with the Ad Hoc group. Though smaller creditors protested, and two funds tried and failed to block the deal in court, the swap concluded with the consent of more than 95% of creditors.

Plaudits flooded in. Paul Greer, portfolio manager at Fidelity International, believes Ecuador "did a cracking job".

"We have seen, on many occasions, issuers playing games," says Greer. "Indeed, Argentina did it this year. Ecuador was incredibly pragmatic, with no delaying tactics or crazy deadlines that were endlessly being pushed back."

ARGENTINA'S TOILS

Comparisons with Argentina, a fellow serial defaulter, became commonplace.

A restructuring of Argentina's $65bn external bond stock had been inevitable since long before Covid-19 broke Ecuador's ability to pay. Argentina had initially given itself until a March 31 deadline to complete a deal.

Yet Argentina submitted its first offer only in mid-April, and it was clear the approach would differ from Ecuador's. Finance minister Martín Guzmán called for unity among Argentine politicians against investors who would "play very hard", while creditors rejected the terms, lamenting the absence of "good faith negotiations" and economic proposals.

Conversations with Argentina remained truncated. Hard default arrived in May; Guzmán said it was merely an "anecdote". More than once, Argentina claimed it had made its "final offer", walking away from the table. Finally, the two sides came together in a matter of days in early August.

Nathalie Marshik, head of EM sovereign research at Stifel Nicolaus & Co, saw Argentina's strategy as "to clinch an agreement that left them paying as little as possible until the mid-term elections", due in October 2021.

"A sub-50 NPV [net present value] recov-

Above: courtesy of El Ministerio de Economía y Finanzas Eduador; Right: Juan Mabromata/Pool via REUTERS

ery seemed to be a psychological limit for a long time," she said. "It would have made a nice headline, had Guzmán achieved an NPV with a four-handle."

By the time the agreement came, creditors were fed up of the headlines; the apparent leaking of private discussions to the Argentine press, including the naming of certain people on the creditor committee, was a particular a sore point.

A MERE SNAPSHOT

Yet Stock of BlueBay — which, like Ashmore, was in Argentina's largest creditor group — argues the contrasts between the two processes are "exaggerated".

à table
Above: Economy Minister Martín Guzmán details the agreement to restructure Argentina's sovereign debt at the Casa Rosada, August 31, 2020
Left: Then Ecuador finance minister Richard Martínez (corner right) with President Lenín Moreno in September

"Though it is easy to criticise Argentina for how long negotiations dragged on, in both cases neither side is happy with the outcome — which is the definition of a good negotiation," he says.

Indeed, the numerical substance of the final results — significant upfront payment relief, low coupons, small principal haircuts, and NPV recoveries in the 50s — did not strikingly differ from one country to the other.

Does talk of values and trust romanticise yet another failure by Ecuador to meet its obligations? It is true that Ecuador's extreme reliance on external funding to a certain extent forced its hand. The country needed to reach a deal with bondholders quickly for the government to sign an IMF programme and "access necessary funding, including all the ancillary multilateral support that comes with such a programme", Marshik says.

As Stock says, "If we had reached an agreement with Argentina in April, we would still be asking the same questions about balancing the budget and how the government is going to finance next year's deficit."

Ultimately, a debt swap is just a snapshot in time, and the haircut and maturity extension do not determine whether the country got a good or bad deal, says Dehn.

"The measure of success of a restructuring is whether it allows the issuer to return to markets on a sustainable basis," he says.

Whereas, in Ecuador, Ashmore saw "a confluence of common objectives" between issuer and creditors, "Argentina was a classic case of a government negotiating without any long-term objectives in mind," says Dehn. "It just wanted to drive the toughest deal, so played all the games possible and tried to split all the bondholders."

BEYOND RELIEF

With the restructuring done, the focus moves on to whether the countries can take advantage of debt relief. In both countries, notes Marshik, the low coupons and lack of carry on the restructured bonds mean they "effectively became an equity play".

"This gives governments leeway but fewer incentives to implement the right policies," says Marshik. "It is vital for governments to take advantage of the lower interest payments afforded to them and address macro and fiscal issues."

The nature of negotiations provides clues about each country's chances of making a success of their deals.

One Latin American sovereign that recovered well from restructuring was Uruguay, in 2003. Dehn notes that it has gone "from strength to strength" ever since.

"A key part of this was that Uruguay left a great impression on bondholders," says Dehn.

Argentina's president, Alberto Fernández, had actually suggested in September 2019 that Argentina could carry out a "Uruguay-style" debt reprofiling. But if there was little evidence of this during negotiations, there is even less likelihood Argentina will be able to replicate another key ingredient of Uruguay's transformation: economic and fiscal policy.

"Argentina showed us that restructuring without an economic plan is a bad idea," says Marshik. "You might buy yourself time, but fundamentals will always catch up to you, and a case in point is [the country's] incapacity to stabilise FX reserves, and the pressures on the currency.

"Without confidence in policymaking, Argentina's new bonds will continue to underperform."

Dehn adds that "the government does not view continued access to the markets as an objective in itself. Its focus is very political and short term".

Argentina and Ecuador's restructured bonds went free to trade within a week of each other at the start of September, inviting another comparison that does not reflect favourably on Argentina, which was yielding about 15%. Market access, indeed, looks distant.

"Based on what we saw from Argentina during the negotiations, it is not going to be an improving credit over the next five years," says Dehn.

Yields on Ecuador's new bonds are closing in on 10% — but the outlook depends heavily on presidential elections due in February 2021.

"There is no certainty in Ecuador that an investor-friendly government will be in place after next year's elections, although the odds are slightly better for Guillermo Lasso [considered market-friendly] after PSC's Nebot bowed out of the race [to support Lasso]," says Marshik. "If you think there is going to be a recovery in oil prices, and that the right policy mix will be in place, there is value in Ecuador."

PSYCHOLOGICAL SHIFT

Elections mean prospects for Ecuador's bonds are rather binary. But the country should reap the benefits of its pragmatism during restructuring.

On one hand, the fast deal triggered an IMF agreement that surpassed all expectations and could relieve pressure on the government in the coming months — potentially increasing chances of a market-friendly candidate winning the vote.

Moreover, the new debt structure means the next president cannot argue external debt payments are a burden.

"Regarding the numbers, the most important thing was to obtain the greatest relief possible over the next five years," says Martínez. "We knew the next administration would benefit and wanted to leave little margin for demagoguery or populism.

"We certainly managed to give enough fiscal space for Ecuador to grow and continue with reforms."

On a deeper level, Martínez hopes that Ecuador can shake off its history as a poor debtor. "This negotiation was a message to the country that a good debtor has better options with its creditors. We took great care to prioritise the population and explain what we were doing," he says.

Reforms implemented during Martínez's tenure often sparked protests, but he believes it was easier for citizens to grasp the benefits of the debt restructuring.

"Debt relief is tangible for everyone. We are demonstrating that doing the right thing, as painful as it may be, brings benefits."

Should Martínez's optimism be well placed, it would show that net present values are not always the most important values in a restructuring. GM

Debt Manager
Central Bank Governor
Finance Minister

GlobalMarkets
Middle East & North Africa
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Finance Minister of the Year
Mohammed al Jadaan, Saudi Arabia

Central Bank Governor of the Year
Ziad Fariz, Jordan

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South Asia
Nirmala Sitharaman, India
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East Asia Pacific
Sri Mulyani Indrawati, Indonesia
Yi Gang, China
Luky Alfirman, Indonesia

Latin America
Richard Martínez, Ecuador
Mario Marcel, Chile
Herman Kamil, Uruguay

Sub-Sahara
Tito Mboweni, South Africa
Ernest Kwamina Yedu Addison, Ghana

CEE
Tadeusz Kościński, Poland
Elvira Nabiullina, Russia
Yuriy Butsa, Ukraine

Debt Manager of the Year
Fahad Al-Saif, Saudi Arabia

Debt Management Office of the Year MENA

Fahad Al-Saif, Saudi Arabia

The Gulf state is extending its curve and sourcing new channels of funding to meet its fiscal objectives

Despite enduring unprecedented levels of market and commodity volatility, Saudi Arabia's debt management office has achieved great success this year in capital markets.

The kingdom has raised $12bn in international markets so far this year, in two separate deals: a $7bn triple trancher in April, which included its longest ever bond, of 40 years, and a $5bn triple trancher in January, which was priced inside the borrower's curve. Both of those issues signified to investors Saudi Arabia's fire power.

"The kingdom has extended its dollar curve twice in 2020, from 30 years to 35 years in its January issuance and to 40 years in April, marking the largest EM order book in 2020, which is a testament to KSA's balance sheet strength," says Hani Almedaini, head of portfolio management at Saudi Arabia's National Debt Management Center.

Importantly, the strengthening and enhancing of domestic capital markets through successful local sukuk issues is testament to the NDMC's access to diverse sources of funding.

"The NDMC has developed and introduced new funding channels to support the government's fiscal objectives during the pandemic," Almedaini says.

The NDMC has also instituted measures in the local Islamic market to grow the depth in secondary.

"This has been reflected by the increase in the secondary market turnover, which reached Sr55bn ($14.7bn) year to date," Almedaini continues.

The NDMC managed to succeed in area of capital markets where no other Gulf sovereign has had success so far. In July, Saudi Arabia signed its inaugural green loan, backed by Germany's export credit agency, Euler Hermes. The loan marked the first sovereign green loan in the Gulf region and has been recognised by the market as a huge triumph for the kingdom. — *MM*

MENA Finance Minister of the year

MOHAMMED AL JADAAN, SAUDI ARABIA

Saudi Arabia's smart, innovative and much-needed fiscal response to Covid-19 has gone down well with investors

While many emerging market countries were crippled under the pressure of Covid-19 and economic slowdown, Saudi Arabia's Ministry of Finance took swift action to consolidate fiscally, while waging its own battle against declining oil prices.

"Since Mohammed al Jadaan became minister of finance, the ministry has embraced more transparency in government finance, allowing the public to access more details on the kingdom's finances. Jadaan also resumed fiscal consolidation in a difficult environment by streamlining expenditure, such as cutting unnecessary allowances to public sector employees and cancelling non-priority government projects," says Garbis Iradian, chief economist MENA at the Institute of International Finance in Washington.

The ministry has made spending cuts of 10% this year, which has left many market-watchers confident about Saudi Arabia's fiscal consolidation efforts. Should the kingdom continue to keep spending at its current rate, it will be on track to balance its budget by 2024 even with oil prices staying below $50/bbl.

In the eyes of investors, the ministry has made smart, innovative and much-needed fiscal decisions, such as tripling VAT from 5% to 15%. That has been critical in increasing revenue at a time when oil prices remain far below Saudi Arabia's fiscal breakeven oil price, which some put at $69/bbl in 2020. Since the start of October, Brent crude has traded at $40-41/bbl.

"The increase in the VAT rate from 5% to 15% was not an easy one, but Jadaan managed it successfully and will be remembered as one of the best finance ministers in the Middle East," Iradian says.

Saudi Arabia has managed to encourage growth in non-oil sectors and has continued on the path to Vision 2030, all the while juggling the presidency of the G20 this year, leaving investors with high expectations for Saudi Arabia's recovery over the next 12 months.

"As a testament to Saudi's commitment to adjust the budget, the government increased VAT from 5% to 15% in July, when most of the world was easing fiscal policies," says Gustavo Medeiros, deputy head of research at Ashmore Group. "Furthermore, there have been notable improvements in procurement rules, expenditure budgeting and execution as well as increased transparency in debt management operations." — *Mariam Meskin*

Central Bank Governor of the Year, MENA

ZIAD FARIZ, JORDAN

Jordan was swift to provide liquidity and bring in a package of stimulus measures when the crisis struck

The Jordanian Central Bank has received hefty praise for the way it has handled the economic response to the coronavirus crisis.

With the economy expected to contract for the first time in many years (by up to 6% this year), the Central Bank stepped up and began making smart decisions to support the economy, which have helped to set it apart from others in the region that are facing the prospect of falling into the grips of a complete crisis.

At the start of the pandemic, in March, authorities cut key benchmark interest rates from 3.5% to 2.5%, which proved to be a critical move in stabilising economic activity.

"The Jordanian Central Bank Governor, Ziad Fariz, was able to swiftly provide liquidity to the banking system, while reducing interest rates to support the economy during the pandemic," says Garbis Iradian, chief economist MENA at the Institute of International Finance in Washington.

A stimulus package targeting banks and small and medium-sized enterprises was released, helping to limit the impacts of the coronavirus.

Those measures included: permitting bank lenders to postpone the loan repayments of clients in affected sectors, providing liquidity of equivalent to $776m by reducing reserve ratios on bank deposits, expanding sectoral coverage and reducing interest rates on its refinancing programme, while simultaneously increasing loan maturities and limits, and reducing the cost and expanding coverage of guarantees provided to small and medium-sized enterprises.

Jordan, which brings in about $5bn of revenue every year through tourism, also benefited from the provision of credit facilities for borrowers in the tourist sector, which was regulated by the central bank.

Alongside decisions from the Ministry of Finance to reduce sales and service taxes in affected sectors, such as hospitality, the central bank provided critical lifelines to the Jordanian economy.

Jordan successfully issued a $1.75bn bond in July in a testament to the country's resilience in difficult times. Market-watchers say that would have been far more difficult without the central bank's leadership and proactive stance towards supporting the economy since the pandemic erupted earlier this year. — *Mariam Meskin*

REUTERS/Alasdair Pal

India's Covid battle: it's only the beginning

India's economic future is on shaky ground, after the Covid-19 pandemic dealt a blow to the country's already faltering growth. The impact of the fallout is likely to be felt for years to come — unless the government quickly changes tack

By Rashmi Kumar

Like many countries around the world, Asia's third-largest economy has suffered a torrid year. By the end of September, India had recorded more than 6m Covid-19 infections, ranking second by number of cases after the US.

This was despite the government hastily implementing one of the world's most stringent lockdowns in March to combat the spread of the virus — a move that not only failed to contain the pandemic but also ended up creating a humanitarian crisis, after hundreds of thousands of migrant workers were stranded.

Growth has taken a beating in the process. For the second quarter of 2020, real GDP growth was minus 23.9% year-on-year — among the sharpest declines seen among Asia's major economies. There is no light at the end of the near-term tunnel either. The International Monetary Fund is predicting a real GDP contraction of 4.5% for India this year, versus growth of 4.2% last year. Growth is, though, expected to rebound in 2021/2022.

The bleak numbers are despite steps taken by the Narendra Modi-led government, as well as the Reserve Bank of India, to shore up confidence in the country.

It began in late March, when finance minister Nirmala Sitharaman announced a $22bn-equivalent relief package to tackle the Covid-19 outbreak, with the funds earmarked for food-related measures, healthcare and agriculture.

The central bank, meanwhile, offered monetary policy support by lowering the repo rate and the liquidity coverage ratio for banks, offering billions in relief for micro, small and medium-sized enterprises, and non-banking financial companies (NBFCs), and offering loan repayment moratoria.

All these measures got the nod of approval from markets.

But efforts have been sorely lacking on greater direct fiscal support to the economy. Fiscal stimulus has been limited at a paltry 1.2% of GDP so far, versus roughly 3% on average in other emerging markets.

"This is the biggest mistake India made: not offering enough fiscal assistance," says Bangalore-based Kunal Kumar Kundu, India economist at Société Générale. "Of course, India doesn't have the fiscal space, but this is not the time to be fiscally conservative — when job losses are rising and spreading from the informal sector to the formal sector, and when there is the real possibility of these job losses becoming permanent."

India's fiscal deficit is likely to rise to about 12.5% of GDP this year, driven mainly by lower revenue generation. But market watchers say fiscal support is critical at this juncture in the world's second most populated country, as it is faced with the triple threat of waning demand, supply concerns and financial sector stress.

Kundu says the "mother of all problems" is lack of demand.

"Unless demand picks up and remains stable, it's very difficult for the economy to recover," he adds. "And this cannot be addressed by monetary policies. When the biggest problem is demand, it has to be tackled with a fiscal response. Other countries have done this, but not India, which is why consumer confidence has hit rock bottom and the economic contraction has been unprecedented."

Prime Minister Modi's government's unwavering stance on limiting fiscal support will come at a steep price, warns Raghuram Rajan, former governor at the RBI and currently a professor of finance at the University

> *"When the biggest problem is demand, it has to be tackled with a fiscal response. Other countries have done this, but not I ndia, which is why consumer confidence has hit rock bottom"*
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> *—Kunal Kumar Kundu, India economist, Société Générale*

> *"Government officials who hold out the possibility of a stimulus when India finally contains the virus are underestimating the damage from a more shrunken and scarred economy"*
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> *—Raghuram Rajan, former governor, RBI*

> *"There were lots of big stimulus measures, after which the overall public sector deficit never managed to get back to the pre-GFC level"*
>
> *—Sreejith Balasubramanian, economist, IDFC Asset Management Company*

of Chicago Booth School of Business. He reckons the strategy of not doing more today to conserve resources for a future stimulus is "self-defeating".

"Government officials who hold out the possibility of a stimulus when India finally contains the virus are underestimating the damage from a more shrunken and scarred economy at that point," Rajan wrote in a LinkedIn post in early September.

Some fiscal space is available for the Indian government if it chooses to use it to bring the economy back on track. But months after the coronavirus reared its head in the south Asian country, that support is still lacking, raising some key questions. Will that fiscal support come? If so, when? And what impact could this have?

PRUDENCE IN THE TIME OF CRISIS

To answer these questions, it's imperative to go back in time to see how India ended up in such dire straits in the first place.

For some, the government's issues go back to around the time of the global financial crisis. In December 2008, the government announced a fiscal stimulus package of about $4bn to spur domestic demand, boost infrastructure spending and give a fillip to exports, through a combination of farm loan waivers and tax cuts. It followed it up with a further $4.1bn relief measure the following year that focused more on setting up alternative financing channels for NBFCs and for more capital expenditure through infrastructure development.

As a result, the country's fiscal deficit shot up from about 2.6% of GDP in 2007/2008 to about 6% the following financial year.

"The story of India's fiscal issues really started there," says Sreejith Balasubramanian, a Mumbai-based economist in the fund management division of IDFC Asset Management Company. "There were lots of big stimulus measures, after which the overall public sector deficit never managed to get back to the pre-GFC level."

Since then, India has witnessed multiple economic woes, he tells *GlobalMarkets*.

In a few years, inflation rose and investment slowed drastically. Companies began to reduce their spending, with the government being forced to plug that hole. Household savings started to dip, eventually leading to a decline in consumption.

Banks then reined back some of their lending, paving the way for India's NBFCs to step in to fill that financing gap. That, however, eventually culminated in rising non-performing loans (NPLs) at India's banks, and the spectacular collapse of aggressive non-bank lender Infrastructure Leasing & Financial Services, whose subsidiaries defaulted onshore in 2018, creating a pall over the country's financial industry.

"The balance sheets of various economic agents were under pressure," says Balasubramanian. "The advantage from 2016/17 was that world growth started getting better. But India again couldn't fully use that opportunity because of demonetisation and the introduction of the [goods and services tax], which affected supply chains and the trade balance, and then we had the NBFC crisis soon after. India did not enter Covid in a strong position."

Balasubramanian reckons all this could have played its part in the Modi government not yet using all its fiscal tools to counter the impact of the pandemic. After all, if people were unable or unwilling to spend money, particularly in the initial days, over fears of the health crisis, parking more money in their hands would have only increased savings.

But he also adds that as the government's debt to GDP ratio will definitely rise sharply this year as it combats the pandemic, it needs to be able to sustain this through medium-term growth. "That is where fiscal policy really has to come in to get the wheel moving soon."

What ammunition has the government got? SocGen's Kundu says there have been some talks of boosting investment in infrastructure and using a public-private partnership model to add momentum to the industry. However, no concrete plans have emerged yet.

He adds that another measure the government should focus on is a temporary wage-sharing scheme with micro, small and medium-sized enterprises that have been hit hard by the pandemic, to help tide them over during this difficult time.

"These are two important pillars: wage sharing and immediately starting infrastructure investments. It's something that should have been done earlier, but can still be done now as the impact could be significant in the longer run."

GEARING UP

It's not going to be easy, of course, for several reasons. One of them is simply revenue limitations at both the state and central governments. According to research by Standard Chartered, revenue shortfall at governments in India is estimated to be at 4.6% of GDP, which could possibly rise to 6%.

Anubhuti Sahay, head of south Asia economic research at Standard Chartered in Mumbai, tells *GlobalMarkets* that the revenue shortfall is a "very large constraint on how much the government can spend to drive demand", given two of the international rating agencies have the sovereign on a negative outlook.

S&P Global Ratings affirmed India's BBB- rating with a stable outlook in late September. But in early June, Moody's downgraded the sovereign by one notch to Baa3, while maintaining a negative outlook. Later the same month, Fitch revised its outlook on the nation to negative from stable, while affirming its BBB- rating.

"India is in a tight spot," adds Sahay. "The real economic impact of Covid will emerge only over a period of time; right now, the impact of the shock is still unravelling itself. Hence, the government and the RBI need to use their ammunition in a calibrated manner as the shock will continue to reverberate for some time."

In his LinkedIn post, former RBI chief Rajan suggested India should borrow more "without scaring the bond markets", while also putting in place direct cash transfers to the poorest households to help them deal with the health crisis.

He also recommended establishing a plan to deal with the "financial distress" that will hit the country once the various payment moratoria come to an end, including by setting aside enough resources to recapitalise state-owned banks dealing with bigger losses than expected.

Kundu adds that there were some initial talks in India about selling an international Covid-linked bond — like numerous other sovereigns and multilateral development banks have done globally — but those discussions died down.

Instead, Kundu reckons the RBI, headed by governor Shaktikanta Das, might opt for monetisation of debt, where the central bank will buy government bonds.

Indonesia, for one, opted for a similar approach this year, when Bank Indonesia agreed to a debt monetisation programme of about $40bn to help with the crisis recovery. As part of this, the central bank will buy about $28bn of Indonesian government bonds at zero return.

"Difficult situations call for difficult action," says Kundu. "But if the Indian government really shows adequate commitment to fiscal prudence, then debt monetisation can be the way out."

Whether the government will go down that route — and what other fiscal tools it will deploy — is yet to be seen. But the authorities need to quickly sharpen their tools — the clock is ticking. GM

ENSURING CONTINUITY THROUGH DIFFICULT TIMES

Amid exceptionally challenging global conditions, Egypt's largest private sector bank revealed resilient performance in 2020, delivering top-line growth. With Covid-19 buffeting banking sectors across the world, Commercial International Bank (CIB) has managed to register some robust financials thanks to previous years' efforts to strengthen its balance sheet, with a large number of assets in high-end corporate facilities and with a large concentration in longer-term bonds. These factors helped shield the bank's profitability in the face of a weakening interest rate environment.

First-half 2020 financial results bear out this resilience. The bank's total tier capital in the first half of 2020 was EGP55.7bn ($3.53bn), or 29.5% of risk-weighted assets. The local currency liquidity ratio of 69.0% and foreign currency liquidity ratio of 59.6% were comfortably above CBE requirements of 20% and 25%, respectively. CIB remains well above the 100% requirement in the Basel III net stable funding ratio (NSFR) and liquidity coverage ratio (LCR) ratios. It also has high-quality funding, with customer deposits comprising 92% of total liabilities.

ECONOMIC SUPPORT

CIB has been able to continue supporting the Egyptian economy. Funding to businesses and individuals grew by 2% over first half 2020 to reach EGP134bn, with a loan market share of 6.1% as of June 2020. Deposits grew by 5% over first half 2020 to reach EGP319bn, with a deposit market share of 6.79% as of June 2020.

The bank's gross loan portfolio was EGP134bn, a 2% (or EGP2.39bn) growth in the first half of 2020. This was driven wholly by local currency loans, which grew by 8% or EGP6.36bn. On the deposit side, the first half of 2020 recorded EGP319bn, a 5% or EGP14.5bn growth. Growth was driven mostly by local currency deposits, which increased by 6% or EGP12.4bn, and foreign currency deposits grew by 2% or $98.4m. CIB's deposit market share was 7% as of March 2020, meaning it maintained the highest deposit market share among all private-sector banks.

The bank has maintained its resilient asset quality. Standalone non-performing loans represented 4.03% of the gross loan portfolio, covered 257% by the bank's EGP13.9bn loan loss provision balance as at mid-year 2020. Loan loss provision expenses were EGP2.26bn for first-half 2020, almost three times higher in year-on-year terms.

The bank's management and staff have worked hard to ensure business continuity through difficult times. Management made a gear change in developing its communication infrastructure, while capitalising on its pre-existent digital solutions and online banking platforms, in order to maintain work efficiency without affecting the wellbeing of the bank's staff and clients.

CIB REMAINS WELL ABOVE THE 100% REQUIREMENT IN THE BASEL III NSFR AND LCR RATIOS. IT ALSO HAS HIGH-QUALITY FUNDING, WITH CUSTOMER DEPOSITS COMPRISING 92% OF TOTAL LIABILITIES.

The bank's commitment to supporting the community continues. In 2020, the CIB Foundation assisted in furnishing The Egyptian Naval Forces New Children's Hospital in Alexandria with medical equipment and financed the completion of the medical infrastructure and electro-mechanical works. The CIB Foundation also subsidised Children Cancer Hospital 57357's purchase of 390 infusion pumps and 216 syringe pumps. In addition, the foundation paid the first instalment to Raei Masr Foundation for Development for procuring and equipping two mobile clinics to conduct 192 medical convoys in Minya and Sohag, with an aim to carry out medical check-ups for 96,000 children annually. In collaboration with True Light Society Association for the Visually Impaired, the foundation initiated the implementation of a new project supporting visually-impaired children in their overall life needs and in their integration into the public education system.

Hisham Ezz El-Arab, Chairman, CIB

DIGITAL DEVELOPMENT

The bank has continued investing in digital banking platforms – a sign of its ongoing commitment to innovation and technology. 2019 saw the introduction of Zaki the Bot, the virtual assistant that uses artificial intelligence to help the bank's customers and non-customers learn about CIB's products and also locates the nearest ATM or branch. The chatbot supports both English and colloquial Arabic operating on both Facebook Messenger and CIB's public website, off-loading enquiries from both call-centre agents and social media teams, and creates a new customer touch point. Zaki the Bot's uses will be expanded to serve new customer segments, such as corporate and business banking.

The QR Code is a new payment method which provides a secure and convenient way to process payments through mobile wallets. In 2019, the bank obtained a licence to introduce the QR Code via CIB Smart Wallet as a new payment method which will rapidly expand the bank's merchant network and be a cheaper channel, compared with the traditional PoS terminals that were previously provided to merchants.

The new payment method will encourage a large portion of the mobile wallet users (currently 13.m users) to activate their wallets and follow the new market trend. Smart Pay is a merchant payments service used as an acquiring tool that allows merchants to accept electronic payments from customers through their mobile devices.

CIB's business banking solutions are another core focus, serving SMEs through a comprehensive range of financial products. In 2019, the bank launched the revamped SME lending programmes that offer faster delivery and more flexibility, piloted a special offering to encourage women through its new Women In Business Programme, and launched a dedicated Contact Centre. In 2020, it launched the Supply Chain Finance programme and the Growth Loan for small companies. ●

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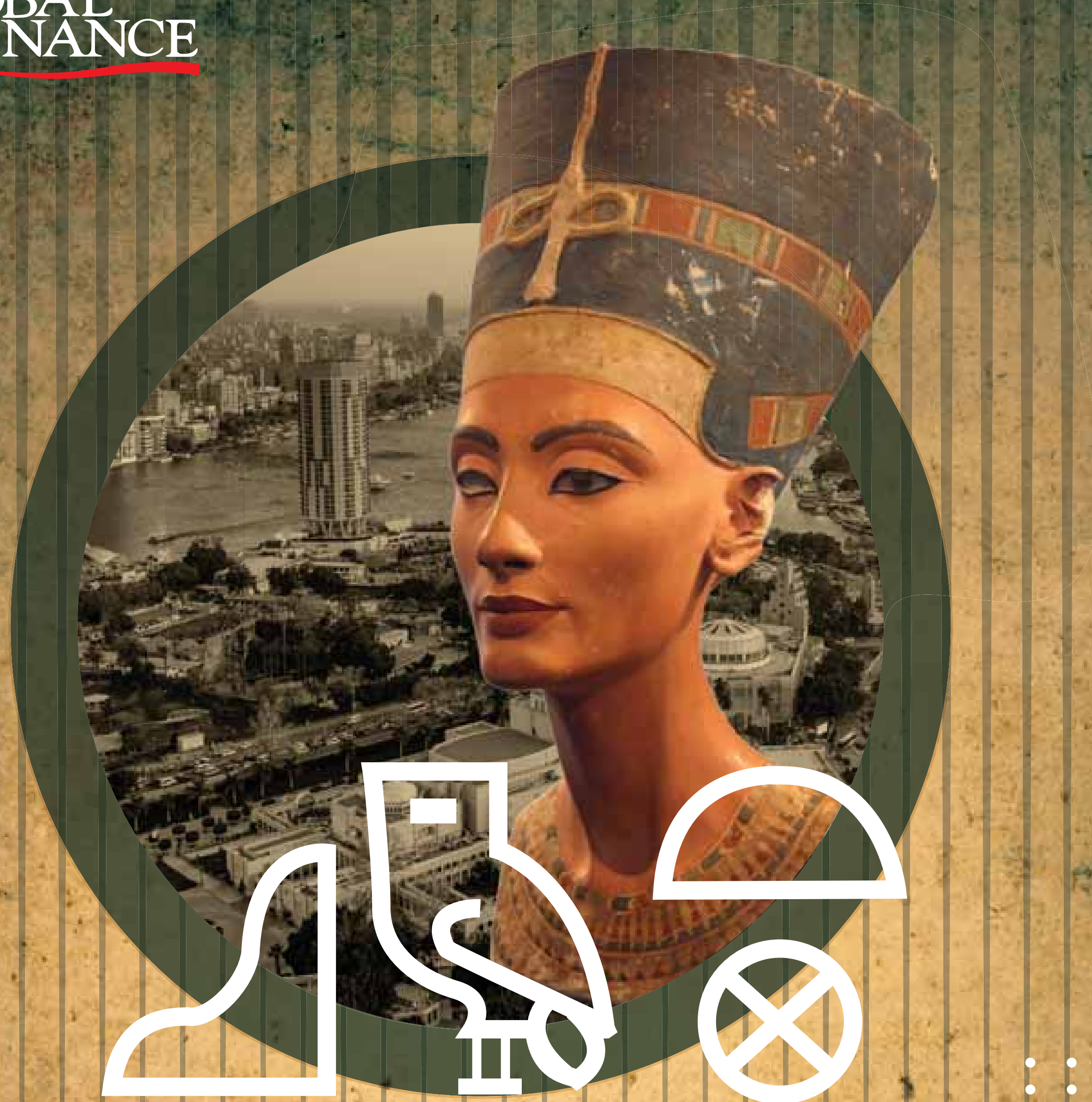

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What's happening Friday, October 16

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8:00 AM – 8:45 AM

CD Talk: Supporting Revenue Administrations to Operate Through the Covid-19 Pandemic

Speakers: **Werner Ovalle**, Director of Customs, Superintendence of Tax Administration of Guatemala
Fathuhulla Jameel, Commissioner General of Taxation, Maldives Inland Revenue Authority; **Susan Betts**, Fiscal Affairs Department, IMF
Azael Perez, Fiscal Affairs Department, IMF

9:00 AM – 10:00 AM

Analytical Corner: Climate Change/Scenario Planning

Session 1: A Green Recovery for Sub-Saharan Africa
Speakers: **Seung Mo Choi**, African Department, IMF; **Genet Zinabou**, Fiscal Affairs Department, IMF

Session 2: Mitigating Climate Change — Growth and Distribution-Friendly Strategies
Speakers: **Marina M. Tavares**, **Simon Voigts**, Research Department, IMF

Session 3: Better Than a Crystal Ball? Scenario Planning & Policy Gaming at the IMF
Speaker: **Alberto Behar**, Strategy, Policy, and Review Department IMF; **Sandile Hlatshwayo**, Strategy, Policy, and Review Department IMF

10:00 AM – 11:00 AM

Seminar: Closing the Digital Divide
Speakers: **Sundar Pichai**, CEO, Google and Alphabet; **Estelle Akofio-Sowah**, West Africa Regional Manager, CSquared; **Sigve Brekke**, President and Chief Executive Officer (CEO), **Telenor**
Pamela Gidi Masías, Vice Minister of Telecommunications, Chile; **Hooi Ling Tan**, Co-Founder of Grab; **Reshma Saujani**, CEO of Girls Who Code; **Mothanna Gharaibeh**, Former Minister of Digital Economy and Entrepreneurship, Jordan
Host: **Lerato Mbele**, Presenter, BBC World News

End Poverty Day 2020

TOMORROW
SATURDAY OCTOBER 17
10:00 AM – 11:00 AM

Seminar: End Poverty Day 2020: Surmounting Setbacks
Speakers: **Lamis Al-Iryani**, Head, Monitoring and Evaluation, Social Fund for Development, Yemen
Sarah Colenbrander, Director, Climate and Sustainability Programme, Overseas Development Institute; **Saleemul Huq**, Director, International Centre for Climate Change & Development, Bangladesh
Strive Masiyiwa, Founder and Executive Chairman, Econet; **Orzala Nemat**, Afghanistan Research & Evaluation Unit; Ngwashi Christabel Apholung, M.D., Medical Doctor; **Dr. Sania Nishtar**, Federal Minister, Poverty Alleviation and Social Safety Ministry, Pakistan
Dominic Raab, United Kingdom Secretary of State for Foreign, Commonwealth and Development Affairs
Axel van Trotsenburg, Managing Director of Operations, World Bank
Host: **Larry Madowo** , BBC North America Correspondent

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Financing a sustainable economy: crisis recovery and drivers of future growth

Biden

Continued from page 1

election, US-China trade and economic relations are expected to remain tense given the degree of bipartisan consensus on [key] issues in the US," said Stephen Schwartz, head of Asia Pacific sovereign ratings at Fitch.

"That said, the Trump administration has been marked by a high degree of policy uncertainty, just by the very nature of how policies have been carried out internationally. Biden might adopt a more predictable and multilateral approach to international issues, which, from the perspective of policymakers in Asia, may be helpful."

CHINA REMAINS IN CROSSHAIRS

The latest figures on trade between the US and China could deal a blow to Trump with the US heading for elections on November 3, given one of his key priorities has been taking down China a peg on trade matters.

China's customs department revealed this week that while its imports from the US jumped nearly 25% last month to $13.2bn — the highest monthly import since mid-2018 — so did exports to the US. Exports soared about 20% to $43.96bn, meaning the country's trade surplus with the US is still nearly 19% higher than a year ago.

Cochrane said: "The trade war is likely to last for the next few years no matter who wins the election. They will go about it in different ways. And there is a good chance tariffs would ultimately fall under Biden."

John Sitilides, a geopolitical strategist at Trilogy Advisors in Washington DC, said that US trade policy would "continue to constrain China's aggressive technology moves, especially in the 5G and semiconductors industries".

A Biden win could prove advantageous for emerging markets overall — albeit with some small caveats. Petar Atanasov, co-head of sovereign research at EM-focused investment manager Gramercy, reckons a Biden victory with a Democratic senate would likely be the "best result" for EM, as it could be positive for globalisation and mutual policymaking.

But he added that if there is a split government, the "potential for policy gridlock is high". "If Biden wins and pushes the green agenda strongly, there is a possibility Mexico and Brazil would feel slightly isolated — especially Brazil as [President Jair] Bolsonaro and Trump have a strong relationship," he added.

EM debt pressures build as IMF calls for 'early' action on restructuring

By Oliver West,

IMF managing director Kristalina Georgieva on Thursday urged highly indebted governments to act "decisively and early" to restructure as investors warned of a wave of negotiations with EM bond issuers.

Although unprecedented public debt levels globally were partly because countries "rightly need to boost spending to fight the crisis", said Georgieva, for many low-income countries urgent action is required immediately to deal with debt burdens. And it is "critical" for all countries to address this in the medium term, she said.

The G20's DSSI debt relief initiative, extended by six months on Wednesday, does not tackle the issue. World Bank president David Malpass said the challenge was to "look beyond DSSI", as it does not reduce payments.

"Interest charges compound quickly on the deferred amounts, leaving countries with even more debt," said Malpass. The DSSI is a stopgap that must be used "while a longer-term solution for the debt crisis can be developed".

Vera Daves, Angola's minister of finance, said in an IMF discussion that the DSSI provided benefits, but that the country also had to "revise and update our medium-term debt strategy", ensuring that dialogue with creditors could ensure a "win-win solution to manage difficult times".

2020 has already been a busy year for EM bond restructuring, with Argentina, Ecuador and Belize having completed negotiations and Lebanon, Suriname and Zambia in the process. Though Covid-19 pushed some of these over the edge, most were already restructuring candidates. But there are more to come.

While even single-B countries have issued in the second half of the year, bond markets indicate the chance of stress.

"EM bond markets are mostly calm because we've been smothered in developed market liquidity but it is constructive to look where the debt is trading," said Jim Barrineau, global head of EM debt strategy at Schroders. "EM investment-grade is close to pre-pandemic levels but sub-investment grade EM spreads remain around 200bp wide of pre-pandemic levels.

"There will be continued concern about potential restructurings and the negative impact of higher debt stocks for already highly indebted countries. Either growth picks up meaningfully or these countries will have to address this."

SEVERAL CANDIDATES LIKELY

Several high yield bond issuers have leaned on the IMF in 2020, and Petar Atanasov, co-head of sovereign research at Gramercy, said he was paying "a lot of attention to the IMF's firepower and whether it can be increased".

"If we see the multilateral response to Covid-19 as a multi-round game rather than a single round, it will be more difficult — economically and politically — to engage in the following rounds," said Atanasov.

"Being able to knock on the door for liquidity relief was a huge help for many EM governments, but the question now is to what extent something deeper is needed, and whether markets will finance the weaker sovereigns."

Atanasov said there were "several candidates" for restructuring in 2021, with sub-Saharan Africa particularly vulnerable as fundamentals and debt-carrying capacity were weak. Some Caribbean countries may have to restructure unless tourism recovers meaningfully, while El Salvador's is also on investors' radars.

Beyond capital markets that are swimming in liquidity, many low-income countries do not have access to bonds. For these countries, multilateral lenders are the only source of finance, said Lesetja Kganyago, governor of the South African Reserve Bank, at the IMF on Thursday.

Georgieva: countries were right to raise spending

"That is why it is important that we make sure that the IMF is not just well-resourced but is also capable of offering concessional facilities to countries that do not have market access," said Kganyago.

Charlie Robertson, global chief economist at Renaissance Capital, offered an alternative view. "There is a big misunderstanding about debt right now," he said. "Debt forgiveness should not be the focus, debt expansion should be. African debtors will be able to refinance their debt at the cheapest rates they have ever borrowed at [and] should be looking at how to refinance their debt over the next two years."

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