Innovative Financing for Development
New Frontiers in Financing for Development

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Mobilizing the MENA diaspora for Global Integration, Investment, and Knowledge Transfer
Marseille
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Innovative Financing
Outline

• New or under-utilized sources
  – Reducing remittance costs
  – Diaspora bonds
  – Diaspora philanthropy
  – Using remittance channels to facilitate health insurance
  – Reducing recruitment costs for low-skilled migrant workers
  – Monetizing flight capital or art from Africa
  – Performance-indexed bonds

• Financial structuring and credit enhancement
  – Credit rating vs borrowing cost (need for shadow rating)
  – Risk guarantees provided by IFIs and governments
  – Using future-flows as collateral
  – (New research on choice of US vs UK law for bond issuance)
Remittances to developing countries reached $436 billion in 2014
MENA: $53 billion

Source: Development Prospects Group, World Bank
Top recipients of remittances

$ billion, 2014e

Egypt, Arab... 20
Lebanon 9
Morocco 7
Jordan 4
Yemen, Rep. 3
Tunisia 2
West Bank... 2
Algeria 2
Syrian Arab... 2
Iran, Islamic... 1

as % of GDP, 2013

Lebanon 18
Jordan 11
Yemen, Rep. 9
Morocco 7
Egypt, Arab... 7
Tunisia 5
Djibouti 2
Algeria 1
Iran, Islamic... 0
Iraq 0

Borrowing cost rises exponentially as credit rating deteriorates

*Interest spread, basis points*

Launch spreads and S&P ratings for sovereign issues of size $100 million and 7 years tenure. Source: Bondware, S&P, and Ratha, De and Mohapatra (2007)
Diaspora Financial Resources for Development

• Mobilize diaspora saving through diaspora bonds
• Mobilize diaspora giving for fighting disease
• Reduce remittance costs
• Improve credit rating and reduce borrowing costs via future-flow securitization of remittances
• Reduce recruitment costs
Diaspora bonds can be adapted for financing Education, Health, Infrastructure
The wealth of the diaspora can be mobilized through diaspora bonds

<table>
<thead>
<tr>
<th>Developing countries</th>
<th>Estimated savings ($ billions, 2012)</th>
</tr>
</thead>
<tbody>
<tr>
<td>East Asia &amp; Pacific</td>
<td>116</td>
</tr>
<tr>
<td>Europe &amp; Central Asia</td>
<td>93</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>146</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>47</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>37</td>
</tr>
<tr>
<td>South Asia</td>
<td>72</td>
</tr>
</tbody>
</table>

Source: Updated estimates based on De, Ratha and Yousefi 2014, peoplemove.worldbank.org
Top 20: Diaspora Savings

Source: Updated estimates based on De, Ratha and Yousefi 2014, peoplemove.worldbank.org
Rationale

• For issuing countries:
  – Patriotic discount
  – Diaspora investors more loyal than foreign investors
  – Diversification of funding sources
  – Support to sovereign credit rating

• For diaspora investors:
  – Patriotism & desire to do “good” in the country of origin
  – Diaspora investors are less worried about devaluation risk
Retail diaspora bonds often come with “patriotic” discount

Source: Ketkar and Ratha 2011
## Comparison of Diaspora Bonds Issued by Israel and India

<table>
<thead>
<tr>
<th></th>
<th>Israel</th>
<th>India</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purpose</td>
<td>Development-oriented borrowings</td>
<td>Balance-of-payments support</td>
</tr>
<tr>
<td>Discount</td>
<td>Large though declining patriotic discount</td>
<td>Small patriotic discount, if any</td>
</tr>
<tr>
<td>Rates</td>
<td>Fixed, floating-rate bonds and notes</td>
<td>Fixed-rate bonds</td>
</tr>
<tr>
<td>Maturity</td>
<td>Maturities 1-20 years, bullet</td>
<td>Five year, bullet maturity</td>
</tr>
<tr>
<td>Distribution</td>
<td>Direct distribution by DCI</td>
<td>Distn by SBI in conjunction w intl banks</td>
</tr>
<tr>
<td>Target</td>
<td>Targeted, but not limited, to diaspora</td>
<td>Limited to diaspora</td>
</tr>
<tr>
<td>SEC</td>
<td>SEC registered</td>
<td>No SEC registration</td>
</tr>
<tr>
<td>Nonnegotiable</td>
<td>Nonnegotiable</td>
<td>Nonnegotiable</td>
</tr>
</tbody>
</table>
Challenges

• Cost of marketing to retail diaspora investors

• Understanding of diaspora profile

• Appropriate use of bond proceeds – need for credibility and oversight

• Debt management
Future flow securitization can mitigate sovereign risks

Choice of collateral, excess coverage and reputation of issuer mitigate other risks
Future export securitization structure

Foreign buyer

Local exporter

Foreign

Local
Remittance securitization structure

- Remittance senders
  - Correspondent bank
    - Special trustee
- Beneficiary
  - Local bank

Foreign

Local
Remittance securitization structure

- Remittance senders
  - Correspondent bank
  - Special trustee
- Local bank
- Beneficiary

Foreign \| Local
## Improving ratings: FF Securitization

<table>
<thead>
<tr>
<th>Year</th>
<th>Issuer</th>
<th>Amount (US$ mn)</th>
<th>Flow type</th>
<th>Transaction rating</th>
<th>Sovereign rating</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998</td>
<td>Banco Cuscatlan</td>
<td>50</td>
<td>Remit.</td>
<td>BBB</td>
<td>BB</td>
</tr>
<tr>
<td>2004</td>
<td>Banco Salvadoreño</td>
<td>25</td>
<td>DPRs</td>
<td>BBB</td>
<td>BB+</td>
</tr>
<tr>
<td>2002</td>
<td>Banco do Brasil</td>
<td>250</td>
<td>Remit.</td>
<td>BBB+</td>
<td>BB-</td>
</tr>
</tbody>
</table>
Hierarchy in Future-Flow-Backed Transactions

- Heavy crude oil receivables
- Diversified payment rights (DPRs), airline ticket receivables, telephone receivables, credit card receivables, and electronic remittances
- Oil and gas royalties and export receivables
- Paper remittances
- Tax revenue receivables
### Securitization Potential in Sub-Saharan Africa ($ billion)

<table>
<thead>
<tr>
<th>Category</th>
<th>Receivable</th>
<th>Potential</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fuel exports</td>
<td>182</td>
<td>36</td>
</tr>
<tr>
<td>Agrl. raw materials exports</td>
<td>20</td>
<td>3</td>
</tr>
<tr>
<td>Ores and metals exports</td>
<td>63</td>
<td>11</td>
</tr>
<tr>
<td>Travel services</td>
<td>26</td>
<td>2</td>
</tr>
<tr>
<td>Remittances</td>
<td>31</td>
<td>4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>322</strong></td>
<td><strong>56</strong></td>
</tr>
</tbody>
</table>

Source: Authors’ calculations, WDI

Note: Based on average for 2011-13
Constraints to FF securitization

• Paucity of highly rated entities
• Long lead times
• High fixed costs (legal and others), somewhat less relevant now
• Non-transparent legal structure
Performance-indexed bonds for counter-cyclical borrowing