In each of the past three years, IFC has raised about US$4 billion to US$5 billion to finance operations and aims to raise the same amount this year. IFC has issued bonds in 28 currencies from both established and emerging markets. Currencies in which IFC has borrowed include the South African rand, Polish zloty, Czech koruna, Hong Kong dollar, Singapore dollar, and the Philippine peso. IFC has been the pioneering first issuer in many emerging markets, most recently issuing in the Israeli shekel and Singapore dollar. In Asia, it was the first institution to make a Philippine peso issue.

Many are interested to know how IFC funding promotes development of the local debt market, what benefits accrue to a country when it opens its doors to responsible creditworthy issuers such as the IFC, and how the issuance of bonds by nonresident institutions helps to develop the local debt market. Such bond issues have a huge development impact on local bond markets. An obvious benefit is the demonstration effect by an issuer like IFC. This activity also helps integrate local marketing practice with the best international standards. Although every country has its own ideas about how to develop its debt market, it can learn a great deal from other markets. Even developed nations offer some useful lessons as they are constantly looking for ways to improve market practices, which include the structuring of issues, standardization of documentation, and depository, clearing, and settlement operations.
Introduction of best market practice is by far the most important benefit. There is usually huge resistance the first time a change is made to normal practice because it is difficult to anticipate the advantages of doing things differently. Once a change is implemented, however, it paves the way for subsequent issues. IFC’s counterparts in London, New York, and Hong Kong that are working in the emerging markets have also found it difficult to persuade people in local markets to consider a different approach.

Some regulators claim that nonresident issuers crowd out local issuers, but there are three problems with this argument. First, in IFC experience, issuance in these markets plays a catalytic role in encouraging more activity, both by issuers who are in the market and by new issuers. Second, none of these markets has an oversupply of debt securities. Third, over the long run, the size of the investor pie becomes larger. Both Standard & Poor’s and Moody’s rate IFC bonds AAA, which is several notches higher than the sovereign bond rating in any of these markets. This allows investors to diversify their portfolio risk and hence create an appetite for lower-rated bonds.

Foreign investors who are not keen on taking both the credit risk and the currency risk at the same time are more comfortable with IFC bonds because they do not have to worry about the credit risk. Over time, as they become comfortable with the currency risk, they tend to prefer bonds of the same currency, namely, government bonds and the corporate bonds of the local currency.

IFC uses a standard information memorandum for all its bond issuance in various markets. This prospectus complies with all the requirements of the 28 markets that IFC borrows in and provides good disclosure and total transparency of IFC’s financial statements. Not all jurisdictions require this information in full, but for consistency IFC makes it available across the markets. IFC’s Treasury Department also has a web site at which it posts any significant or material change that may have an impact on its portfolio. IFC makes every effort to be prudent about keeping the various jurisdictions that it borrows in completely informed. For example, when it did the first Singapore dollar bond issue, IFC decided to make a bigger provision in its portfolio for Russia and Brazil. Singapore was having problems at that time. IFC informed its investors and syndicate members of the bond issue. After the changes to the portfolio were
explained, not a single investor or a syndicate member backed out of the investment because of the strong AAA rating of IFC bonds.

Another argument to counter the alleged crowding-out effect is that regulators can always turn off the tap if they do not wish to have further issuance from nonresidents. During the run on the Hong Kong dollar equity market, for instance, the authorities thought there were a lot of speculators in the market. Therefore they asked all the supranationals not to do any borrowing with a maturity of less than three years. IFC does not do any borrowing without government consent.

An additional benefit of IFC bonds is that they help to establish a risk-free benchmark in countries without a benchmark issue. Many markets lack a well-developed yield curve, and swaps are not normally available for longer maturities. As the yield curve and swap market develop over time, however, the maturity of the bonds also increases. After IFC inaugurated the Singapore dollar bond issue in October 1998, which had a three-year maturity, other highly rated nonresident issues followed, with maturities of up to 10 years. In the case of the South African rand, IFC has done 12 issues with maturities ranging from 1 to 25 years. IFC manages its risk exposure to various currencies by swapping them to U.S. dollars, which is the currency of IFC’s balance sheet. Since this is the currency of IFC’s balance sheet, regulators fear that it draws out valuable foreign currency. However, a structure has been worked out to ensure that the currency does not leave the country. Therefore opening markets to the nonresident issuers also fosters the development and deepening of the swap market.

While one issue alone does not give rise to a cross-currency swap market, a series of issues does and over time helps shift the market from one customized back-to-back swap to a system of swap books among key market players, which greatly increases the overall efficiency of the financial markets. This has been demonstrated in many markets, including Hong Kong and South Africa. The importance to local corporates of having deep and liquid stock markets should not be underestimated. Such a market enables them to hedge their foreign exchange exposure on internationally competitive terms and to compete globally on a level playing field. The market structure also needs to be in place.
Such standardization not only provides a great deal of comfort to credit rating agencies when rating a sovereign bond issue, but over a period of time it also reduces the cost of borrowing for all issuers, be it the government or the corporates. It also increases market discipline on the part of issuers as investors hold issuers to global standards of transparency and disclosure. A successful bond issue by an organization such as IFC is a strong validation of a country’s market infrastructure to the international financial community, particularly with respect to depositary, clearing, and settlement operations.

IFC has often been the first issuer doing the spade work, with other issuers subsequently entering the market. IFC has led the way for several reasons. First, it has a very strong AAA rating. IFC received its first rating in 1984 and since then has been rated AAA. Second, IFC is a strategic borrower rather than an opportunistic borrower. It does not pursue the lowest available rate without concern for the market, the investor, or the country image. IFC is risk-averse and intent on maintaining that image in the eyes of all parties, including investors and regulatory authorities. Third, its accounting procedures comply with internationally accepted accounting principles. Fourth, IFC believes in total transparency and the highest standards of disclosure.