



International Monetary Fund

Pros and cons of issuing an international bond

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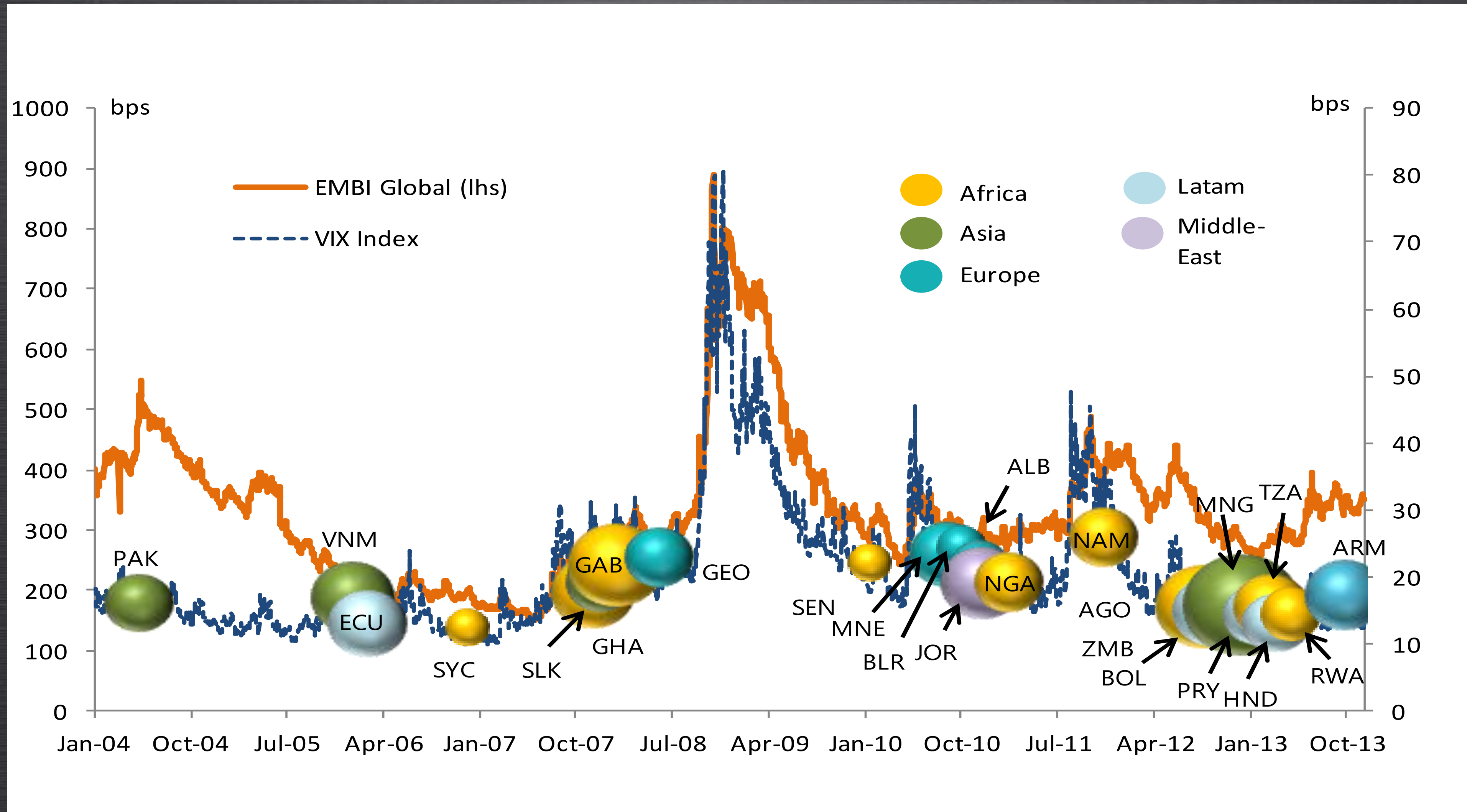
Monetary and Capital Markets Department

IMF

ROADMAP

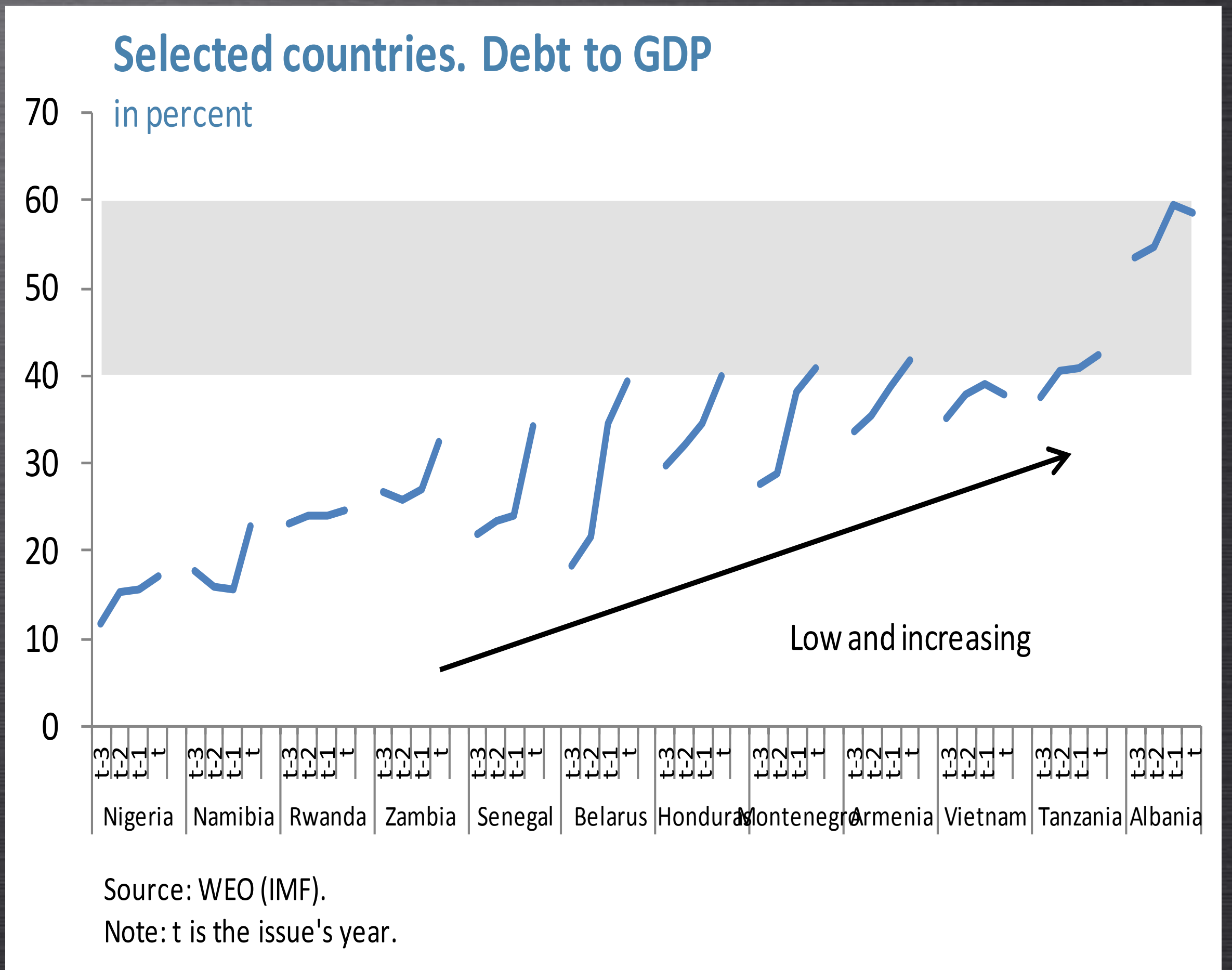
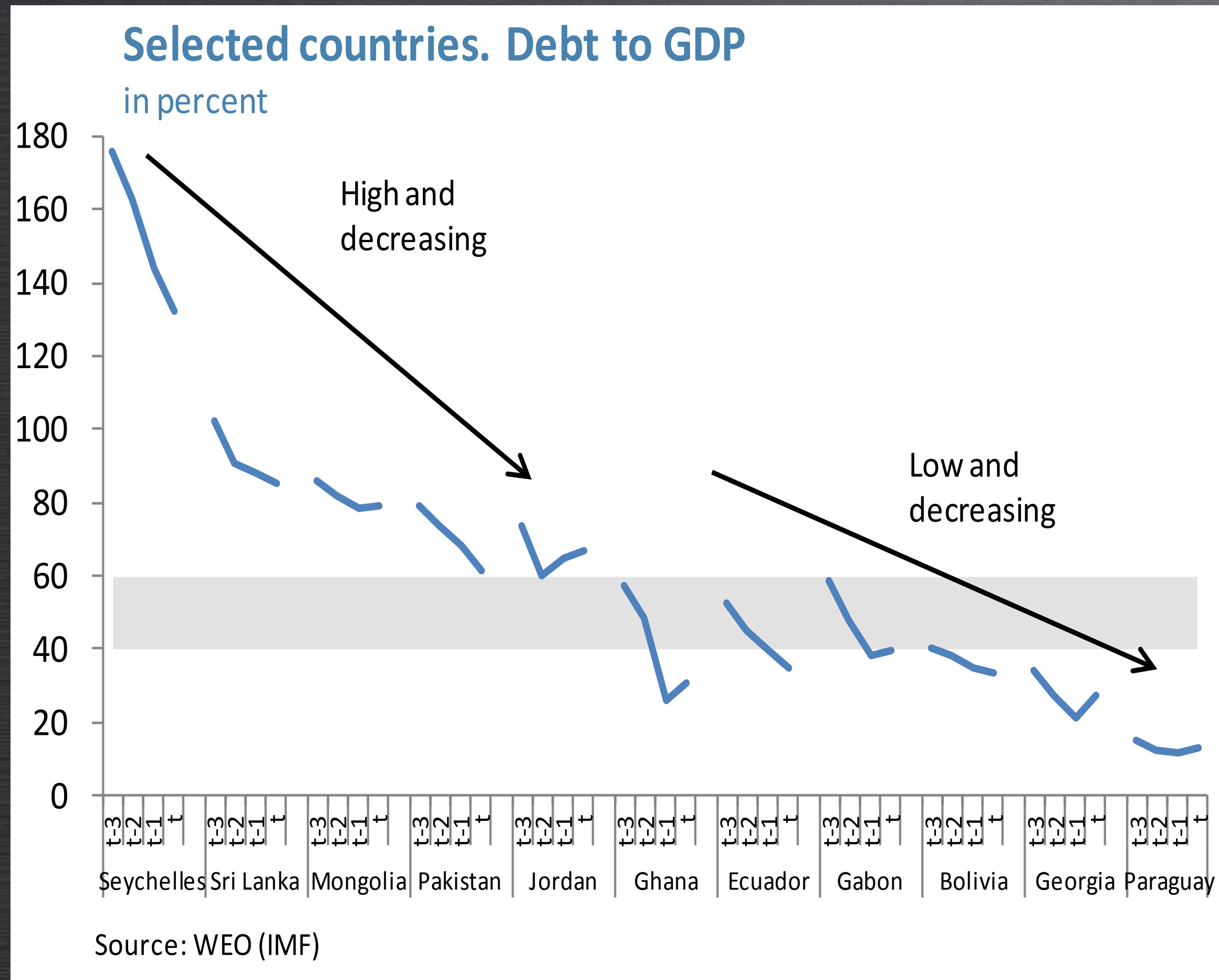
- **Background**
- **Frontier Markets: new opportunities, old risks?**
- **Reasons for issuing in external markets**
- **Benefits and Pitfalls**

A new wave of LICs accessing the international market



Reference: "First-Time International Bond Issuance—New Opportunities and Emerging Risks" by A. Guscina, G. Pedras and G. Presciuttini. IMF WP forthcoming.

Frontier markets: old risks?



Reasons for Issuing Externally

Strategic Ones

- Diversify financing sources and the investor base
- Create reference for the corporate sector
- Disseminate a positive image for the country to a broader community of investors.
- Foster market discipline

Opportunistic Ones

- Lower cost
- Longer maturity
- Temporary access to specific demand
- Refinance maturing bonds

Significant Potential Benefits

Direct

- Supplements domestic savings and borrowing from official lenders
- Sometimes lower costs versus domestic markets
- Extend maturities farther than possible in domestic markets
- Cash borrowing allows for speedier project implementation

Indirect

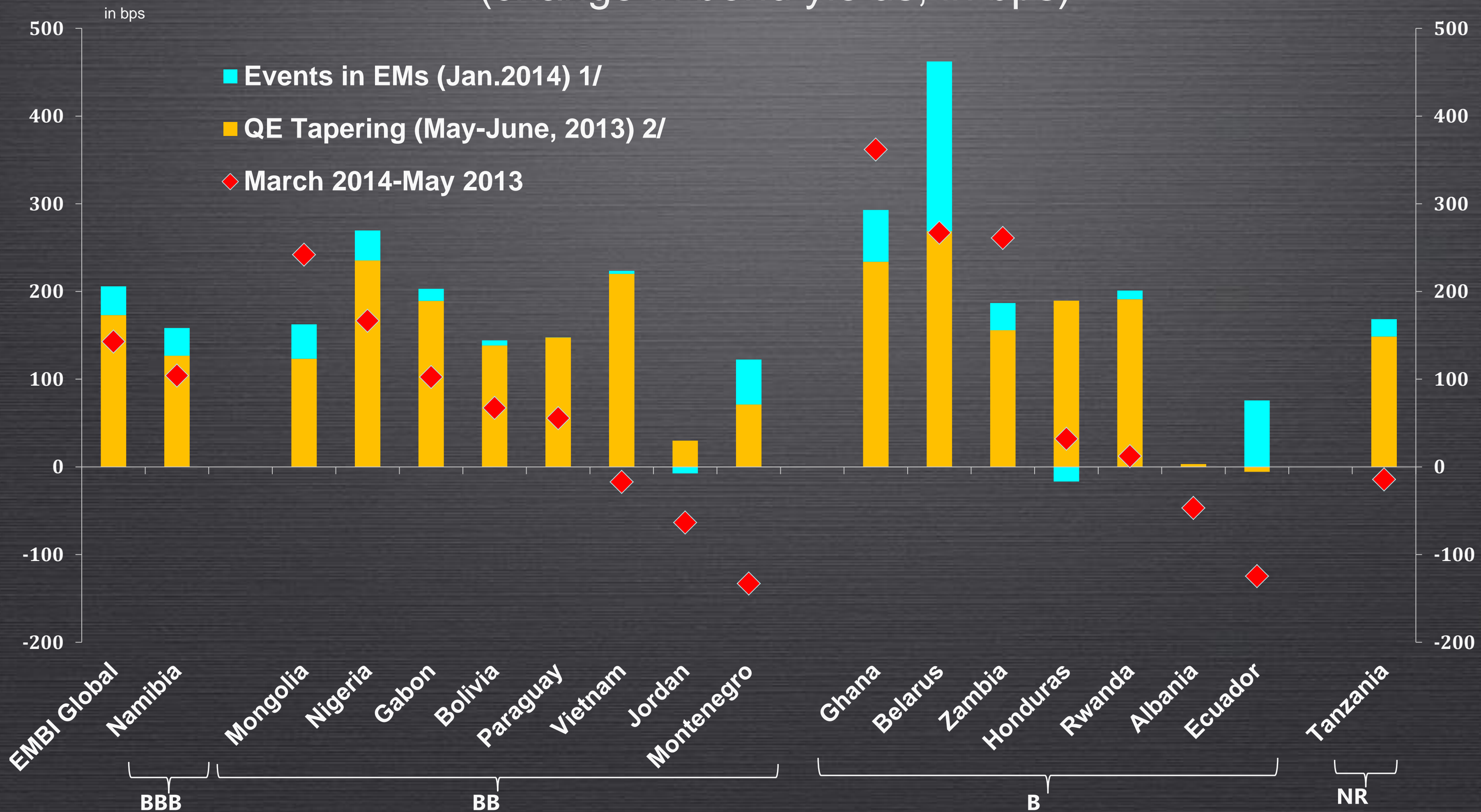
- Establishes a pricing benchmark for private companies
- Broaden sources of capital and reduce reliance on bank financing
- Strengthen incentives for maintaining macroeconomic discipline

But also significant potential macroeconomic risks

- ❑ Higher borrowing cost (when shifting from non-concessional sources)
- ❑ Higher Refinancing risk (maturity hump; private investors are prone to bond sell-off if market conditions suddenly change)
- ❑ Higher exchange rate exposure (when switch from local currency debt)
- ❑ Cost of carry (interest payment during investment period)
- ❑ Terms of trade swings (lower international reserves or ER depreciation)
- ❑ External financing conditions (monetary conditions in G7 countries, risk aversion, etc).
- ❑ Overborrowing can lead to debt sustainability problems.

These countries are not immune to capital outflows...

(change in bond yields, in bps)



Source: Bloomberg and IMF staff calculations.

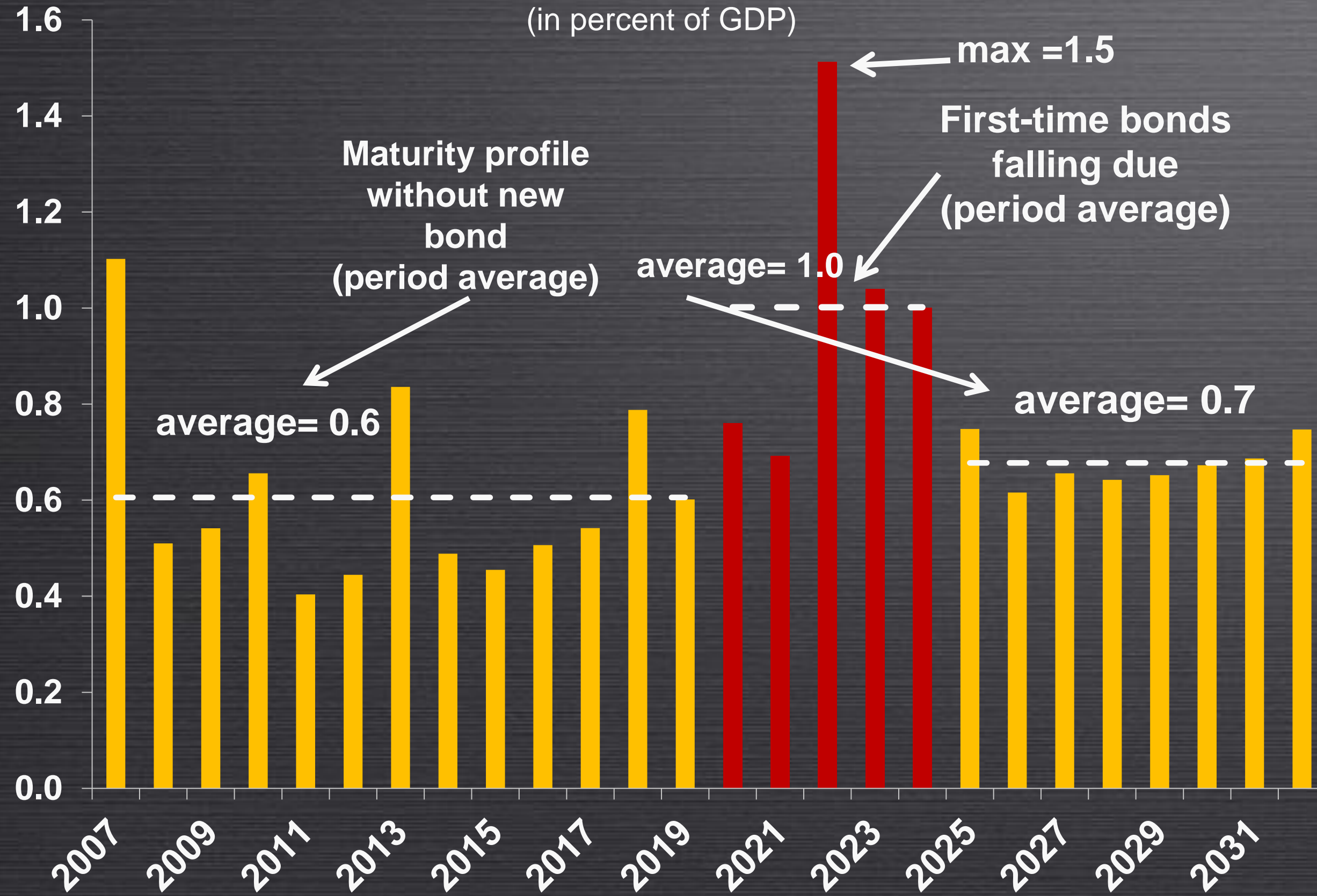
1/ Refers to a series of events in EM economies, which comprises political events in Turkey, lower growth expectation in China and Brazil, devaluation in Argentina, among others.

2/ Refers to the distressed period driven by Bernanke's speech about tapering.

...with potential impact on growth and fiscal balance

Rollover risk

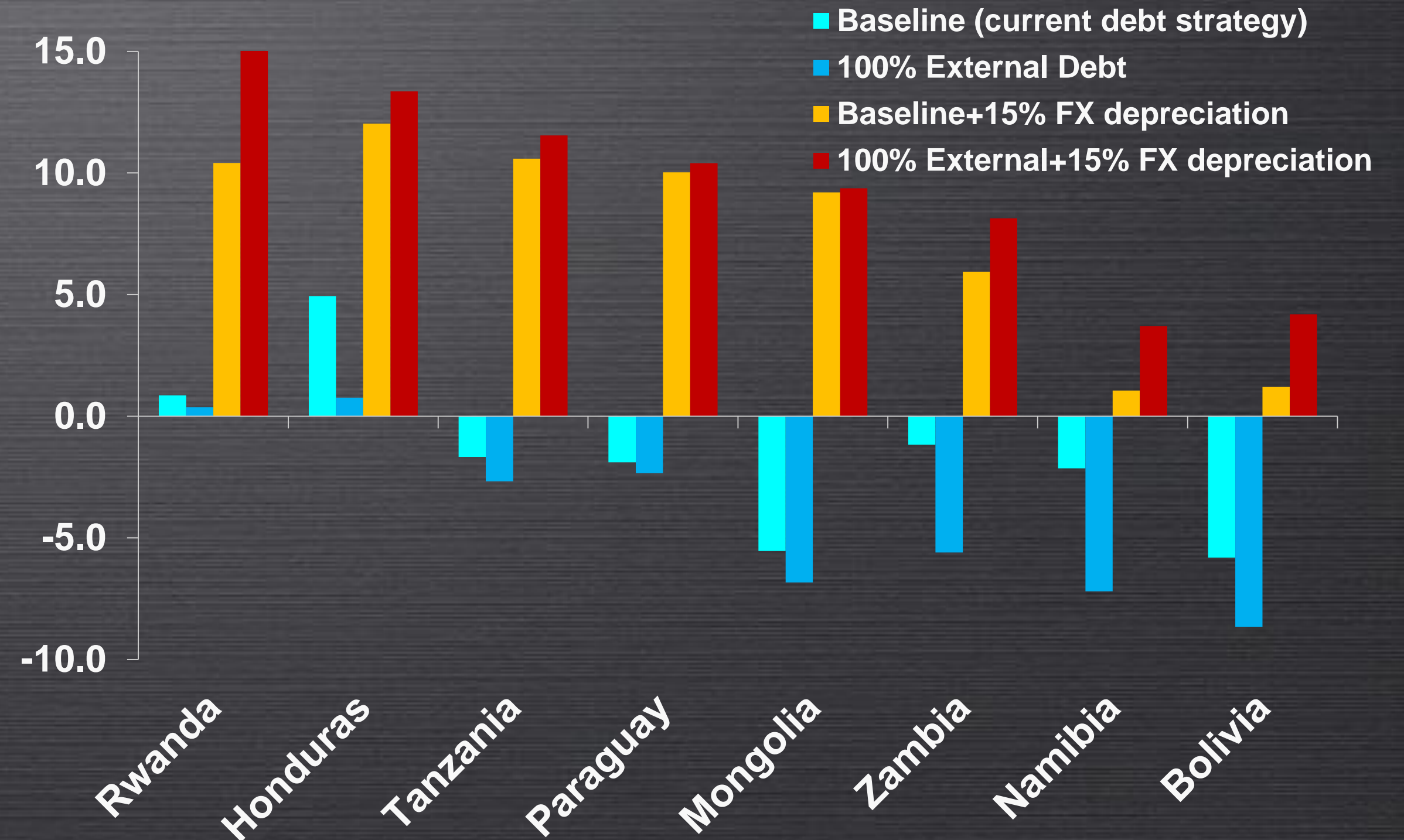
(in percent of GDP)



Country sample includes Bolivia, Honduras, Mongolia, Namibia, Rwanda, Tanzania and Zambia.

Growth gap

(in percent)



Source: Country desks and IMF calculations.

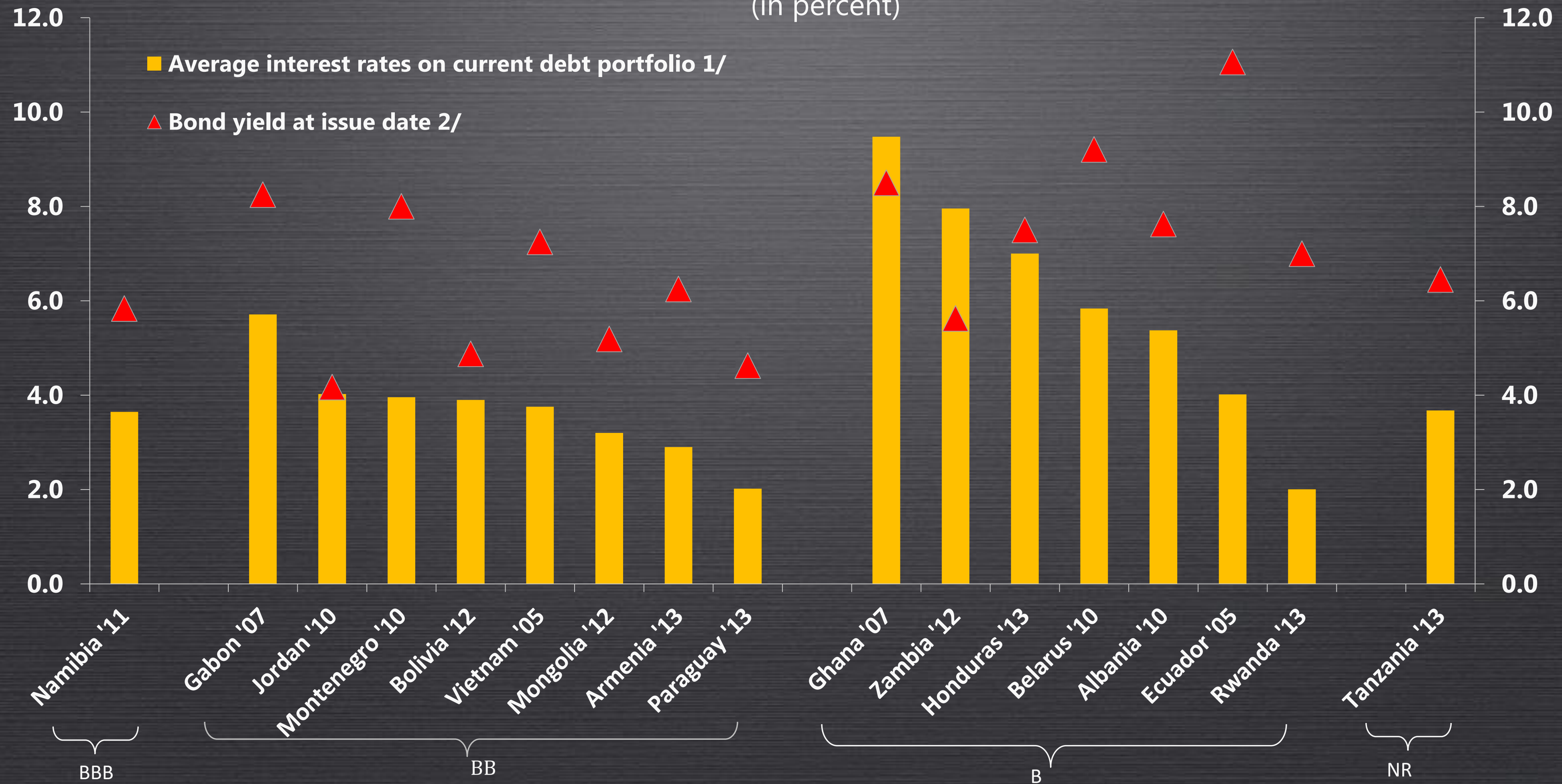
Note: Growth gap is the difference between the required (implied) growth rate that makes the debt stock remains constant at current level and the average expected growth rate over the projection period.

Reference: "First-Time International Bond Issuance—New Opportunities and Emerging Risks" by A. Guscina, G. Pedras and G. Presciuttini. IMF WP forthcoming.

...and higher borrowing costs

Changes in the cost of borrowing

(in percent)



Source: WEO, Bloomberg and IMF staff calculations.

1/ Annual interest payments over previous year's debt stock., which includes both local and foreign currency interests.

2/ This yield does not include the expected depreciation rate at issue date,

Take a pragmatic view

- ❑ What is the scale of the infrastructure challenge/foreign funding needs?
- ❑ What is the shortfall compared to other sources of funding?
- ❑ In what time frame can capacity be build?
- ❑ Can complimentary domestic resources be found?
- ❑ Developing domestic markets
- ❑ Engaging new bilateral creditors
- ❑ Tapping external commercial markets

Strategic considerations

□ Conducting debt sustainability is critical in reducing risks of debt distress:

1. Evaluate the future payment capacity under different macroeconomic scenarios (growth, exchange rate, interest rates).
2. The use of the proceeds: finance deficit or investment

□ A comprehensive medium-term debt strategy exercise is important to assess the impacts of the external bond on the cost-risk trade-offs of the debt composition



Thank you



Background slides

Factors affecting spreads at issuance

- ❑ Higher growth prospects, relative low inflation, sustainable current account balance and high foreign reserves.
- ❑ Sustainable levels of debt.
- ❑ Prudent fiscal stance and policy transparency.

Factors affecting spreads at issuance

Supportive external environment “Push factors”

- ❑ Low interest rate environment – “Search for yield”
- ❑ Sufficient risk appetite (low volatility abroad - VIX)
- ❑ Demand for diversification (correlation with either AMs or large EMs is low).

Successful marketing

- ❑ Building investor base
- ❑ Data dissemination
- ❑ Obtaining credit rating prior to issuance
- ❑ Close contact with investors (e.g.: Road shows and active Investor Relation Program)