



German Federal Ministry of Finance

Berlin, October 2007

**Implementation Report**  
on the G8 Action Plan for Developing Local Bond Markets  
in Emerging Market Economies and Developing Countries

In the **Action Plan** G8 Ministers asked their Deputies, the IMF and World Bank for a joint report on how to implement recommended actions on:

- More efficient and robust market infrastructure; strengthened public debt management practices; broader and diversified investor base in local currency bond markets; development of derivative and swap markets; broadening database on local currency bond markets; promotion of regional cooperation where appropriate; build-up bond markets in developing countries, especially Sub-Saharan African countries.
- Improved and better coordinated technical assistance (TA) to promote local bond market development, facilitating an improved dialog between emerging and G8 market participants and emerging market regulators and sovereign issuers.

**The IMF and the World Bank** have now presented their recent and planned activities which are summarised below:

- **Strengthening regulatory and supervisory frameworks and trading, settlement, custody, and delivery mechanisms.** Through the IOSCO principles assessments carried out under the IMF and the World Bank's Financial Sector Assessment Program (FSAP), and as part of individual country and regional TA and advisory programs, reform priorities have been identified in various countries and technical assistance is already being provided. The IMF and the World Bank see further scope in coordination with other IFIs, to speed up the reform agendas.
- **Improving public debt management and debt market development.** The IMF and the World Bank have ongoing program of country assistance in debt management and debt market development. These programs are coordinated across both institutions. A stronger focus is being placed on assisting countries to develop effective debt management strategies that take account of debt market development needs. The World Bank is also promoting a local currency bond fund (GEMLOC) that will provide a new and important channel focusing TA work.
- **Expanding securitization markets.** Asset-backed securities (ABS) markets can help improve access to long-term funding for housing and infrastructure investment, while also providing pension funds and insurance companies long-term instruments for asset-liability management. Although the recent sub-prime crisis highlights that risk dispersion can amplify volatility, the merits of securitization cannot be discounted as it has fostered the development of financial markets. However, it will be critical to ensure that financial innovations are carried out with adequate safeguards and risk management capacities. The IMF has initiated a major project in this area (a paper titled "ABS in Emerging Markets: Recent Trends and Policy Implications for Capital Markets" to be published in the 1<sup>st</sup> quarter of 2008). The World Bank has extensive operations to support individual securitization transactions and assist countries in building domestic securitization markets by providing technical assistance on legal and operating frameworks.
- **Broadening and diversifying the investor base.** The IMF is working as part of the Capital Markets Consultative Group (CMCG) on a study to explore factors driving the changes in investor behaviour in emerging markets, key impediments to development of emerging capital markets and local and foreign institutional investors therein, and remedial measures. Drawing lessons from the experiences of mature market and emerging market countries, the IMF is working on a set of good practices for developing the domestic institutional investor base (including enabling reforms such as pension fund reforms) and for improving regulation and consistency of treatment of institutional, foreign, and other

investors. The World Bank Group provides TA and makes investments that promote the pension and insurance industries. It plans to increase efforts to develop bond products that attract more institutional investment and is building a new database on pension funds. In addition, the GEMLOC project will help diversify the investor base in emerging market countries.

- **Developing emerging repo and derivative markets.** The IMF has been working with several emerging market countries in this area, including on a major project on derivatives markets in emerging markets (a paper titled “Derivatives in Emerging Markets: Recent Trends and Policy Implications for Capital Markets” to be published in the 1<sup>st</sup> quarter of 2008). The IMF, in collaboration with the World Bank, will also be hosting regional workshops with participation from regulators and policy-makers. The World Bank Group offers derivatives to clients as part of its risk management services and is outlining a strategy for assisting countries in strengthening domestic derivatives markets, particularly tied to government bond market operations.
- **Developing bond markets in less developed countries, particularly sub-Saharan Africa.** A joint initiative of the IMF and the World Bank has recently been launched that is aimed at helping Low Income Countries, including those in sub-Saharan Africa, develop effective medium term debt management strategies (MTDS) that are consistent with the goal of maintaining debt sustainability by focusing on the cost and risk characteristics of the debt portfolio. The MTDS will also take account of market development factors and will facilitate a more structured and systematic approach to developing local government debt markets. A World Bank Group’s program, funded by Sweden, will also help build bond markets in selected African countries, with an initial focus on improving bond financing for housing and infrastructure development.
- **Improving securities market data.** The lack of high quality and internationally comparable bond market data is a key impediment to the development of markets in emerging countries. The IMF and the World Bank are working on initiatives that will help address this issue. Of note, the IMF, ECB, BIS, and the World Bank have reconvened the Working Group on Securities Databases (WGSD) to evaluate and implement the recommendation to broaden the database. At a meeting in Washington D.C. on 27/28 September 2007, the WGSD agreed on a sequence of goals to improve data on securities, including the development of a handbook on bond securities. Also of note, an international conference to be held in January 2008 is being organized by Deutsche Bundesbank in close cooperation with the German Federal Ministry of Finance that will deal with a number of issues, especially broadening the database. Furthermore, an international conference focusing on challenges in improving the global comparison of securities statistics, is being organized by the Irving Fisher Committee on Central Bank Statistics and hosted by the IMF in March 2008. In addition, the World Bank is investigating the possibility of creating a bond market indicator and is developing an investibility index for emerging bond markets related to the GEMLOC initiative.
- **Promoting regionalization.** The IMF and the World Bank are increasing efforts to identify how regionalization can best be designed and implemented to bring greater efficiency, scale, and market access for small capital markets. The World Bank is currently studying existing examples which have been successful in this regard to find relevant lessons to be learnt from past experience. A study is being launched concerning regionalization of East African Securities.
- **Facilitating exchange of knowledge and experience.** The IMF and the World Bank plan to continue to work on this front through a series of workshops and seminars (such as the World Bank’s Sovereign Debt Conference, the joint OECD/World Bank/IMF Global Bond Forum, the IMF’s Debt Managers’ Forum and other seminars and workshops) involving debt managers, central bankers, regulators, investors and other market participants.

**The G8 Deputies have discussed the proposals made by the IMF and the World Bank and welcome their work program and underlined its relevance.** In this context, G8 Deputies underscored the importance and relevance of the findings of the **Committee on the Global Financial System (CGFS)** study on local currency bond markets. The Basel-based CGFS, in its June 2007 report on “Financial stability and local currency bond markets”, identified three policy challenges posed by nascent local currency bond markets: providing liquidity, fostering local currency debt issuance by the private sector, and effectively managing risk concentrations. The report noted the shift in the composition of debt from external foreign currency bonds to domestic local currency bonds. While beneficial on bal-

ance, the shift may be associated with increased exposures to interest rate and refinancing risks (from typically shorter maturities of domestic bonds) and increased debt servicing costs (from typically higher interest rates on domestic bonds). The report also highlighted some data issues, together with the need for further analysis on risk exposures, in particular through derivatives markets.

In implementing the Action Plan, the **G8 Deputies** have urged the IMF and the World Bank to consider the following principles:

- **Cooperation with emerging market economies and developing countries.** Discussions with IFIs were taken into account when developing the Action Plan. The G8 have discussed these issues with emerging market economies and developing countries, particularly during a high-level workshop in Frankfurt in May 2007. The public and private sector in emerging market and developing countries should be involved in every stage of implementation, so as to make ongoing and further measures more effective. The G8 strongly encourage the IMF, the World Bank and other international institutions involved in taking this approach to collaborate closely with these countries.
- Within this context, the OECD Working Party on **Debt Management** organises annual meetings tailor-made for emerging market economies and low-income countries - the OECD Global Forum on Debt Management and Emerging Government Securities Markets - and will hold a second forum on African Debt Management later this year. The OECD-Italian Treasury Network for Public Debt Management in emerging markets aims to provide, among others, an electronic platform for continuous information exchange with interactive features that support an intensive and comprehensive electronic policy dialogue. These initiatives complement the IMF / World Bank seminars and workshops, such as IMF Debt Managers' Forum and World Bank's Sovereign Debt Conference.
- **Private sector engagement.** The G8 encourage private sector involvement, particularly in promoting technical expertise and better understanding market dynamics, as a critical complement to official efforts by the IMF, the World Bank, and other multilateral and bilateral organisations.
- **Additional aspects concerning the implementation of the Action Plan.** The G8 believe that supporting the development of securities and derivatives markets in emerging market economies should be put firmly in the context of long term economic development; any changes in this area should be suggested only as appropriate for each country's stage of economic development. Furthermore, the G8 support the efforts of the Working Group on Securities Databases (WGSD) to improve the availability and quality of internationally comparable bond market data. The G8 support the view, that - beyond the mandate of the WGSD - a comprehensive approach for broadening the database needs to be examined by further working groups including stock taking the existing data of bond markets in such countries with the possible aim of integrating it into one data base. In this context, an international conference to be held in late January 2008 is being organized by Deutsche Bundesbank in close cooperation with the German Federal Ministry of Finance. This conference aims to bring different initiatives together and provides a forum for discussing these issues with international experts who deal with financial markets, financial stability and statistics; moreover, market participants are to be invited to ensure that the conference addresses transparency in such markets in addition to statistical requirements. In addition, the G8 also encourage the IMF and the World Bank to look into economic transmission mechanisms in EMEs and study the possible impact that the development of local bond markets might already have had in the current turmoil of financial markets.
- **Time interval of reporting.** In accordance with the Action Plan, the G8 ask the IMF and the World Bank to regularly report on the progress of the implementation. These reports should be presented to the G8 at yearly intervals. Ministers will discuss the reports, when necessary.
- **The G8 recommend that the IMF and the World Bank publish these reports.** Before their publication, the reports could also be discussed by the boards of the IMF and the World Bank. The reports should not limit their scope on enhancing transparency of the steps undertaken and the further work program of the IMF and the World Bank, but should also include an overview of actions taken or planned by other relevant international institutions, the G8 and possibly other countries and market participants. The reports would thus contribute to enhancing the international dissemination of knowledge in this field. In this context, the IMF and the World Bank could organize international

conferences on local capital market development that would provide a valuable platform to discuss the steps already undertaken and future work programs of the parties involved.