ADB

Technical Assistance Consultant's Report

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Regional: Promoting Remittance for Development Finance

(Financed by the Financial Sector Development Partnership Special Fund)

Prepared by Eric Guichard

Homestrings Ltd.

London, United Kingdom

For Asian Development Bank

Asian Development Bank

ASIAN DEVELOPMENT BANK

Remittances for Development Program

The Democratic Socialist Republic of Sri Lanka

Feasibility Study Report

June 2016

Prepared by:

Eric V. Guichard
CEO
Homestrings.com

ACKNOWLEDGEMENTS:

Homestrings Ltd would like to thank the Asian Development Bank for the opportunity to contribute to the policy debate around the wider use of remittances to finance development, as an alternative, sustainable source of development finance capital. We would like to acknowledge the Sri Lanka office of the ADB and its staff who have been instrumental in facilitating meetings and other resources that have made this report possible. We would like to specifically acknowledge Ms. Mayumi Ozaki who was instrumental in making resources available to the consultant that resulted in a deep understanding of the challenges faced by Sri Lankan policy makers. We hope that this aide-memoire contributes valuably to the debate, and results in meaningful understanding of the potential of remittances to finance development sustainably.

GLOSSARY OF TERMS:

ADB – Asian Development Bank

CBSL – Central Bank of Sri Lanka

CSE – Colombo Stock Exchange

BOI – Board of Investments – Sri Lanka

FFS – Future Flow Securitization

GDP – Gross Domestic Product

IMF – International Monetary Fund

MFI – Microfinance Institutions

MESA – Migrant Endowment Savings Account

MTC – Money Transfer Companies

SEC – Sri Lanka Securities and Exchange Commission

SLFEB – Sri Lanka Foreign Bureau of Foreign Employment

SME – Small and Medium-sized Enterprises

SLR – Rupee – Sri Lanka national currency

Purpose of the Feasibility Study:

The Asian Development Bank has retained London-based Homestrings Ltd, a global diaspora investment platform, to conduct a feasibility study focused on actively mobilizing remittances to Sri Lanka for development finance. The study is meant to identify opportunities for policy intervention that would result in efficient leveraging of alternative resources as an accessible and reliable source of long term development finance. The study proposes to identify tools, solutions and best practices, and to demonstrate how such mobilization should be structured and managed. The study took place between February to June, 2016. Key principals were: Ms. Mayumi Ozaki, Finance Specialist (Rural and Microfinance) at the Asian Development Bank; and Mr. Eric V. Guichard, CEO of Homestrings Ltd.

Key Contextual Elements:

Sri Lanka has an estimated 2 million migrant workers who work in key centers around the world with a high concentration in the Middle East, in Italy, in Canada and in the United Kingdom. These migrant workers and the Sri Lankan diaspora remit a total of $7 billion in annual remittances, or 8.75% of Gross Domestic Product.[1]

The majority of current migrant workers is comprised of low skilled housemaids who remit on average between $100 - $300/month through bank branches and transfer houses. Most transfers are cash to cash delivery. Although a growing number is captured through bank accounts, currently estimated at 20% of remittances. Migrant workers set up bank accounts at departure, primarily with state banks, through the Sri Lanka Bureau of Foreign Employment (SLBFE). The SLBFE, working closely with international recruiting agencies, plays the role of migrant worker clearinghouse prior to their departure for foreign shores.

The average migrant worker stay abroad is 3 – 5 years. The SLBFE is currently focused on increasing the number of skilled laborers to be hired for posting abroad. This development comes on the heels of serious domestic socio-economic implications of sending young women abroad. The policy initiative is also intended to impact migrant worker savings as they earn higher wages. This has positive implications for future remittance growth.

Several programs exist to fund bottom of the pyramid households using remittances as collateral, as in the case of housing loans and small and medium-sized enterprise (SME) loans. Very little is being done to insure the financial security of migrant worker returnees who often return to broken homes and with no savings to support themselves.

Microfinance institutions (MFI) have extensive remittances delivery networks in remote areas and are increasingly playing the role of money transfer distribution agents for banks, including facilitating hand to hand delivery of cash at their local branches.

[1] Central Bank of Sri Lanka.

Key Relevant Findings:

1.Sarvodaya Economic Enterprise Development Services (SEEDS) & Sarvodaya Development Finance: Lead MFI in Sri Lanka.

SEEDS and Sarvodaya Development Finance are the leading microfinance institutions with an extensive network of divisional units, district offices and branches, which are in contact with remote areas of the country.[2]

SEEDS recently received a money transfer license with a partner bank to provide money transfer services to remote areas through branches and also door-to-door service to poor households.

SEEDS is seeking to obtain a banking license directly or indirectly to mobilize public savings other than those of their MFI borrowing clients. It is not clear that regulatory authorities will accept this request. However, this does represent the opportunity for the families of migrant workers to easily access savings accounts funded by their migrant relatives. Technology could also be considered for such access if SEEDS were to adopt an SMS interface platform.

SEEDS have a $200 million SME loan portfolio that has a less than 5% default rate. The cost of capital sourced from partner banks to make these SME loans cost between 7% - 10%. SEEDS on-lends and achieves a portfolio yield in excess of 20%, reflecting both the administrative cost of making such loans and their attractive yields. This fact represents a key point when looking at attracting pooled migrant worker savings.

SEEDS represents an attractive conduit for providing savings vehicles for a new wave of skilled migrant workers being sent abroad. With the SLFEB seeking to export higher skilled workers, this would mean the beginning of a **virtuous circle** in which higher skilled workers would earn higher wages; potentially exhibit a higher propensity to save; become more receptive to financial literacy initiatives focused on savings and investments products which will result in a deep contribution to financial inclusion objectives.

2.Securitization laws exist in Sri Lanka but have yet to be used to mobilize remittances.[3]

Sri Lanka has extensive experience with securitization having facilitated a number of lease transactions as well as asset backed deals. However, there is no evidence that future flow securitizations involving remittances have been attempted or successfully executed in Sri Lanka.

Most, if not all transactions seem to have been executed by private sector players involving overseas interests. Key to our findings is the prospective role of state banks in a pilot remittances securitization project. Separately, the central bank and the SEC are aware that any issuance of diaspora bonds would need to be registered with foreign regulators where they can enjoy certain exemptions if positioned correctly.

[2] http://www.sarvodaya.org/about
[3] http://www.iclg.co.uk/practice-areas/securitisation/securitisation-2015/sri-lanka

3.Central Bank of Sri Lanka (CBSL) hosts a dynamic inclusion program that needs scaling.

The CBSL's **Regional Development Department** (RDD) is an unusual presence in a central bank given its operational mandate of launching and overseeing bottom-of-the-pyramid schemes with partner donors. One particularly successful program – "**Prosperity Loans**" are made to returnee migrants and/or to their families to start small scale businesses or to buy land such that they create wealth stock which can be used as future collateral.[4] The success of this program has led the RDD to seek additional resources to expand the scheme.

The CBSL's **Public Debt Department** (PDB) is the department in charge of issuing government obligations. The PBD staff have the technical expertise in house to pull off a successful offering of a diaspora bond. However, the details of a diaspora bond offering would need to be worked out beforehand. Details such as the use of proceeds; the availability of ADB guarantees, if any; a pre-selected list of projects to be funded; an oversight structure inspiring investor confidence; and a marketing budget to credibly support the distribution of the bonds, would need to be decided upon clearly.

It would be important to include both the Sri Lanka Securities and Exchange Commission (SEC) and the Colombo Stock Exchange (CSE) in the listing and distribution planning discussions. A recurring theme though out this mission is the lack of knowledge among policy makers of the regulatory requirements in target host countries for publicizing and distributing sovereign diaspora bonds. Interestingly, the CSE and the SEC, who are aware of these requirements, have never been consulted on the matter by the central bank or other issuing agencies**.**

5.State banks control over 50% of remittances flow into Sri Lanka – an opportunity.

State banks inspire trust among rural households. People's Bank and Bank of Ceylon control over 50% of remittances flows. Peoples Bank's brand inspires trust among rural households. Peoples Bank seems overwhelmed by the demand for services, and is short staffed in providing services.

No linkages are currently being made between remitter savings, which are less than 20%, and yield generation opportunities – even though foreign exchange rates, yield and transfer costs are key determinants in deciding how to transfer money between bank services, transfer houses or choosing an informal route. Bank of Ceylon is the biggest collector of remittances with in excess of 47% of the market.

The banking system presents a complex web of eligibilities to access various financial products. But most financial products are available domestically. However, only two types of accounts are available to migrant workers: Rupee savings accounts and Foreign Currency accounts which are used for investments. The latter is primarily used by the diaspora who have a higher level of financial literacy.

Mobile banking services are not a key priority for state banks. Banking services are primarily focused on providing physical access to transfer points and to providing competitive exchange rates to attract remittances.

[4] http://www.cbsl.gov.lk/htm/english/07_af_3rd/r_1.html

Because of their dominant position in the remittances market, state banks are likely candidate to pilot a future flow securitization (FFS) project. This will provide the government with alternative sources of capital and direct access to long term funds to finance infrastructure and similar long dated projects.

6.Mobile Banking has great potential in Sri Lanka – if led by the private sector. [5]

Although state banks have not universally promoted mobile banking, the private sector has initiated e-banking with the launch of a domestic platform. Dialog Axiata PLC (Dialog) is the leading Sri Lankan telecom company that is very creative with technology.[6] It has a deep understanding of the needs of the local market. With over 90% of mobile penetration in Sri Lanka households, including in rural areas, domestic uptake of mobile banking has been strong, but still behind countries with similar if not lower macroeconomic standing.[7]

Dialog is currently working on growing "Inbound" flows from migrant workers as another means of transferring funds to local accounts or to a network of merchants and cash points. Dialog claims of growing uptake is being disputed by competitors, especially by state banks.

Dialog is likely to introduce more innovative financial products delivered to rural areas if regulatory authorities allow it.

7.Board of Investments (BOI) is the main source of investment projects in Sri Lanka.

The Board of Investments presents an interesting pipeline of projects ranging from: maritime port development to health care establishment and agriculture projects. However, the promotion of these projects has been somewhat passive. In addition, many of the projects have not been structured to be investment-ready.

There has been heavy reliance on foreign private sector players providing project development services. However, it is believed that these services would be better delivered by BOI and paid for by prospective investors.

Channeling Remittances for Development: Sri Lanka Remittances Solutions Toolkit

1. <u>Achieving greater financial Inclusion and security for migrant workers</u> – Case of Returnees

   Migrant worker returnees who typically complete their offshore assignment after 5 years, are currently comprised in majority of woman who leave young families to take up housemaid and other similar jobs abroad. This situation results in several difficult socio-economic realities: a. they typically return to broken homes; and b. they typically have no savings to return to, as all the transfers made by them are typically consumed by their families who no longer have any use for them.

[5] Mobile banking in Sri Lanka: IFC scoping study: http://www.ifc.org/wps/wcm/connect/822beb00407b914e90ed90cdd0ee9c33/Sri+Lanka+Scoping+Report+053013_final+for+publication.pdf?MOD=AJPERES

[6] http://www.dialog.lk/dlg/about/index.jsp

[7] The Economist: Why does Kenya lead the world in mobile money: http://www.economist.com/blogs/economist-explains/2013/05/economist-explains-18

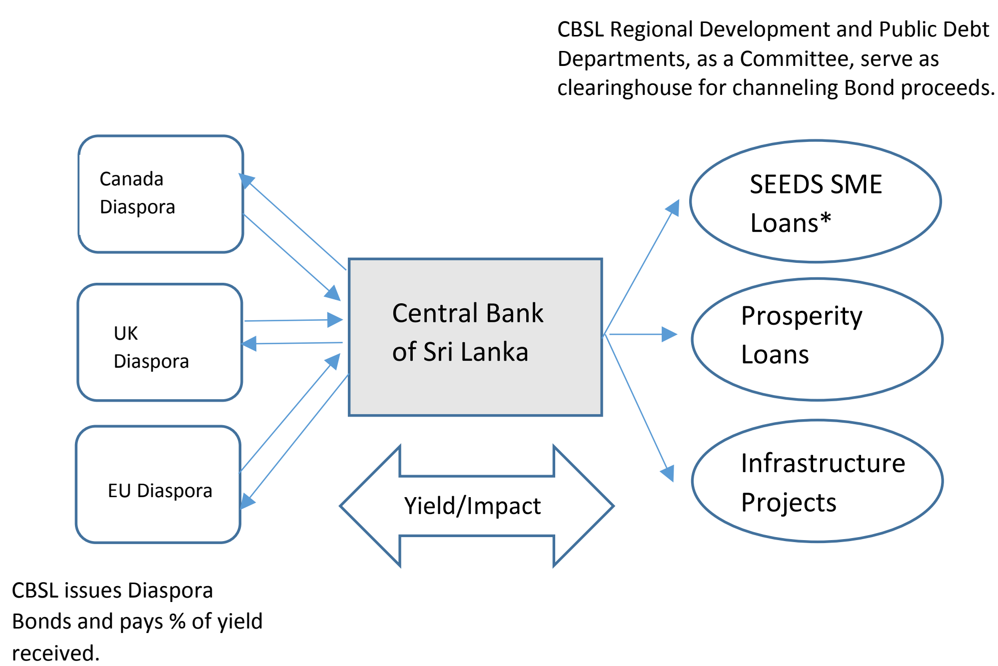
To alleviate this situation, it is recommended that these migrant workers open two savings accounts while exiting through the SLFEB. One account for their families and another for themselves. It is recommended that the latter account be an endowment savings accounts against which they can borrow, if need be. The new **Migrant Endowment Savings Accounts** (MESA) would be tied to MFI loans portfolios and will therefore yield higher returns. The endowment nature of the accounts will help compounding of yields to rapidly generate a wealth stock to which they can return at the completion of their foreign assignment. This wealth stock in their accounts will enable them to begin from a new more secure footing with access to financing based on collateral built with the MRSA.

Financial literacy training will be provided by the SLFEB, the MTC and by state banks while abroad. These can be provided through mobile banking services adopted and promoted by state banks.

2. Leveraging CBSL's Regional Development Department's unique position and experience.

   RDD can oversee the deployment of fundraising proceeds into successful inclusion programs. CBSL can tap into diaspora capital to grow MFI funding – The case of re-introducing **Sri Lanka Diaspora Bonds.**

Schematic of Sri Lanka Diaspora Bond



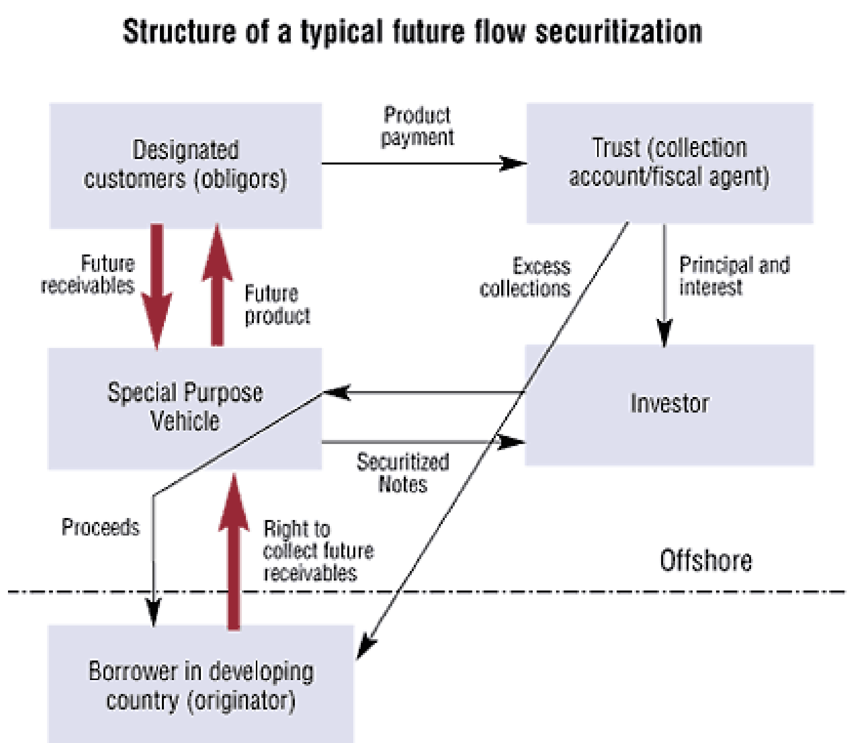
*SEEDS can issue its own Diaspora Bonds independently.

Source: Homestrings

Here, it is proposed that the CBSL's RDD and the PDD form a joint committee to decide on the channeling of bond proceeds among deserving social programs. Key here is that the use of proceeds be reflected in the bond offering – such that investors are aware of the impact they are making. RDD could also enhance the offering by reporting regularly on socio-economic impact metrics of proceeds used. An example of such a reporting framework is that offered by the Global Impact Investment Network.[8]

3. Leveraging Bank of Ceylon's state ownership and dominant position as largest distributor of remittances – Securitizing Future Flows for Infrastructure Finance[9]

   With over 47% of remittance flows going through Bank of Ceylon, it is in an advantageous position to help the government leverage remittances to finance development. The process of taping into remittance-backed long term finance is structured into a single transaction called future flow securitization (FFS). With several related transactions to rely upon, Sri Lanka has a reliable pool of local experts to call on. ADB has the opportunity to facilitate the first FFS involving remittances, under a pilot project with Bank of Ceylon. Below is a typical FFS schematic.



Source: IMF

[8] https://iris.thegiin.org/
[9] Future Flow Securitization primer: http://www.scribd.com/doc/259240248/Leveraging-Remittance-Flows-An-Introduction-to-Future-Flow-Transactions

4. Application of FFS on a sample of Sri Lanka's priority areas of focus: Sea Port Expansion:[10]

The Sri Lankan government has launched an ambitious program of physical infrastructure development to completely upgrade the sea, air, road, power and telecom backbone of the country. The following are the main features of this program:

a. Sea Port and Airport Development

The Sri Lankan government has declared its intention to develop the country as a leading regional aviation, navigation and trading hub in South Asia. Therefore, the development of maritime & aviation transportation is at the forefront of the government's infrastructure development agenda. The focus of these developments is to expand the capacity and improve the efficiency of existing ports through modernization and construction of new ports and airports in strategic locations.

Major Sea Port and Airport development:

- **Colombo South Port Expansion**

The Colombo South Port expansion project with three terminals, each terminal having capacity of 2.4 million TEUs per annum, will increase the capacity of the Colombo Port by 160% upon completion. Construction work of the breakwater has been completed. The first terminal, a joint venture between the Sri Lanka Ports Authority and China Merchant Holdings Ltd, was built under a 35-year build operate and transfer agreement with SLPA. The terminal was opened for commercial operation on 5th August 2013.

- **Hambantota Port Development**

Phase I of the project, the Mahinda Rajapaksa Magampura Port, was inaugurated in November 2010. The port is expected initially to function as a service and industrial port and later be developed to handle transshipment cargo. Phase II of the port is underway at an estimated cost of US$ 800 million. The port is ideally located to serve the main East-West shipping lane connecting Europe and the Middle-east with South East Asia.

The bunkering facilities at the Port of Hambantota, set up at a cost of US$ 76.5 million, and the tank farm has commenced commercial operations. Out of the 14 tanks it has, eight tanks will be used to store marine fuel, three will store aviation fuel and three remaining tanks will be used to store liquid petroleum.

The aviation fuel stored in the Hambantota Port is to be used for the Mattala Airport, the second international airport currently being built in Hambantota.

- **Expansion of Bandaranaike International Airport**

[10] Excerpts from: http://www.investsrilanka.com/why_sri_lanka/developed_infrastructure

A project is under way to expand the island's first international airport at Katunayake, 35 km north of Colombo. The project includes the expansion of the transit area, construction of new baggage-reclaim area, multi storied car park and widening of the existing runway. A feasibility study is being carried out for a second runway.

- **Development of a second International airport at Mattala**

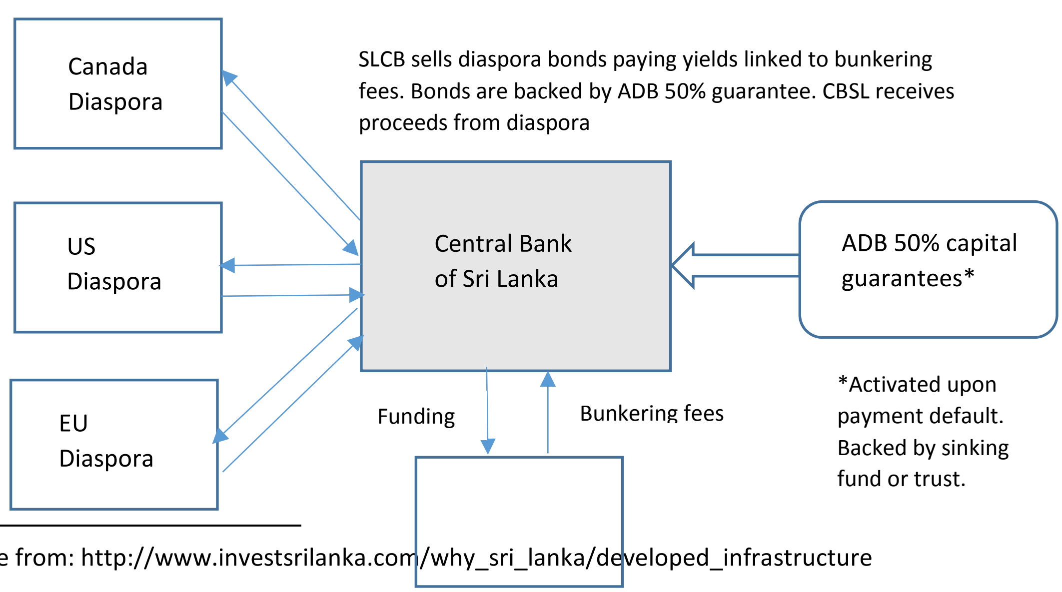
The construction of the new international airport at Mattala in the southern Hambantota district is carried in two phases. The first phase was completed and opened on 18th March 2013. That includes one runway and a taxi way that will be expanded in the second stage to allow for larger planes, including the latest airbus A380, to land. This airport will open up the vast southern and eastern areas of Sri Lanka for development including tourism projects. The airport will be in close proximity to the Hambantota port."[11]

In the context of diaspora and remittances based finance, two financing options exist for the government of Sri Lanka: a. the above projects could be bundled into two separate theme portfolios: Maritime Project Finance and Airport Expansion Finance; or b. each project could be financed individually with a combination of Project-based diaspora bonds and FFS. FFS would be structured in conjunction with Bank of Ceylon.

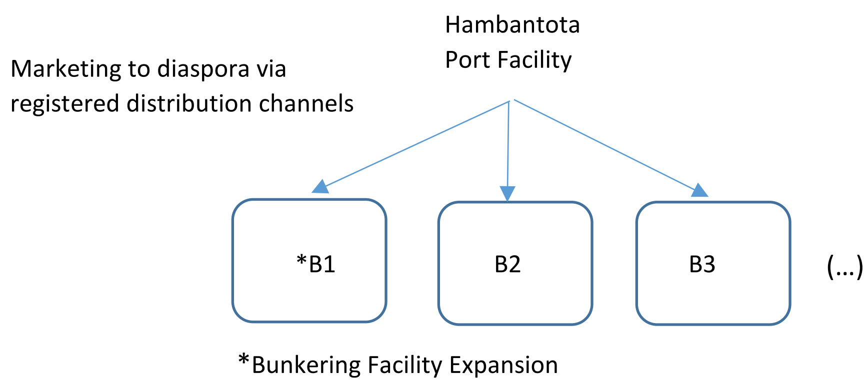
Each of these options presents a unique risk profile that international investors recognize and are willing to take on if the transactions are structured attractively. Below are two illustrations of diaspora and remittances based financing operations:

Diaspora Funding Mechanisms Illustration: Case of Hambantota Port Bunkering Facility Expansion. Estimated cost of $76.5 million:

Hambantota Port is to be expanded to include bunkering facilities. The estimated cost of this expansion is set at $76.5 million. The diagram below illustrates a proposed funding transaction using diaspora bonds:



[11] Quote from: http://www.investsrilanka.com/why_sri_lanka/developed_infrastructure

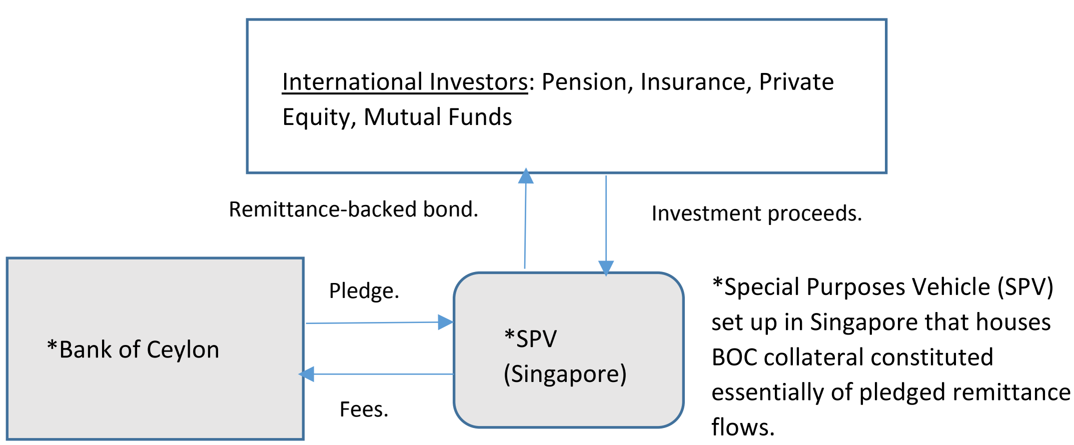


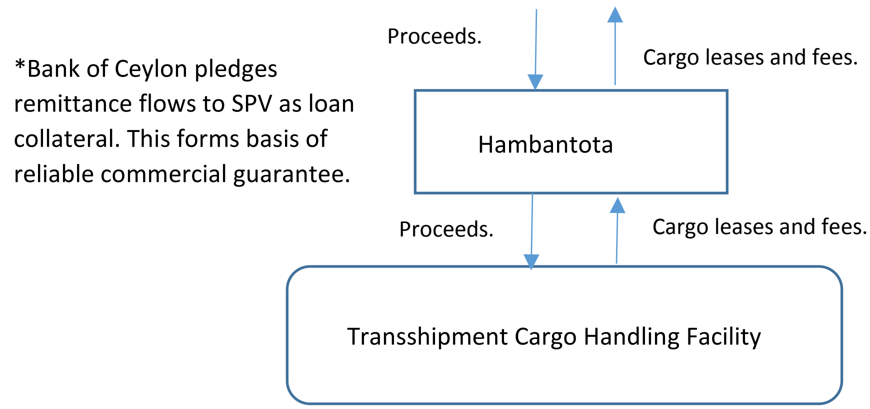
Source: Homestrings Ltd

Here, the government of Sri Lanka would propose to raise $76.5 million through the issuance of project based diaspora bonds. Key features of this transaction are that the diaspora bonds are being issued by Central Bank of Sri Lanka through registered channels in key markets where the diaspora reside (Canada, EU and United Kingdom); the coupon is paid from fees received from the project, in this case usage and other fees paid by bunkering vessels; and an ADB 50% guarantee on capital invested is introduced to address early concerns around credit risk and defaults. The critical element of success is the on-going marketing of the diaspora bonds. This would need to be targeted, sustained, well thought out and executed by a professional marketing and PR firm. The effectiveness of the marketing campaign on the success of the distribution and fundraising exercise is not to be underestimated.

Remittances Backed Funding Mechanism illustration: Case of Hambantota Port Cargo Transshipment Facility Expansion. Estimated cost $800 million.

Hambantota Port is also seeking to expand to include cargo transshipment facilities. The estimated cost of this expansion is set at $800 million. The diagram below illustrates a proposed funding transaction using remittances as collateral or what is known as future flow securitization:





Source: Homestrings Ltd

Here, Bank of Ceylon, a government-owned bank, sets up a separate structure, a special purpose vehicle (SPV), in a jurisdiction recognizable by international institutional investors (Singapore). The SPV's main purpose is to issue collateralized bonds. The collateral, remittance flows controlled by Bank of Ceylon, are pledged to the SPV. The SPV issues a 20-year bond to international investors. The coupon on the bond reflects the credit standing of the SPV and is backed by the revenue stream generated by the new cargo handling facility (assumed here to be cargo transshipment fees). Bank of Ceylon earns a fee for the collateral pledged. Investors are comforted by the quality and stability of the collateral (remittances flows). Bank of Ceylon's SPV can issue as many bonds as are required for infrastructure investment by Sri Lanka. This approach provides an independent source of long term capital. [12]

5. Preparing BOI Project Pipeline for Diaspora and Private Equity Fund Investment

   One of the country's key objectives is to increase international private investment. To achieve this, policy makers have targeted private equity firms as key partners to direct international portfolio flows to the country. To meet these objectives BOI must structure its pipeline of projects such that the equity offerings are directly investable by these targeted funds. Currently, the expectations are that most of the project preparation rests with foreign investor interest.

   If BOI is to be successful in increasing the number of transactions, it needs to take a more engaged promotional approach to marketing the investment opportunities in Sri Lanka and abroad. These promotional activities include, but are not restricted to: holding investment forums in Sri Lanka; presenting BOI's pipeline of projects at global investment forums; and holding private investment meetings with key private equity funds, global investment groups and corporate interests around the world.

[12] Sri Lanka could also envisage selling similar long term bonds in Rupees for local pension and insurance companies who need long-dated investments to hedge their long term liabilities.

Its investment pipeline must have investment-ready status. To achieve investable status, the projects must reflect the following key characteristics, among others:

- Favorable regulatory coverage
- Plausible purchasing agreements that are anchored in equitable recourse rules
- Public Private Partnerships where the local partner provides local distribution, access to local sources of funding; enjoys favorable relations with the government that leads to access to DFI facilities
- Legal documentation and industry due diligence reports conducted by reputable international advisory services – which will be purchased by international partners
- Approved securitization schemes to help mobilize domestic savings and diaspora capital.

Developing project offering packages which will be marketed to international investors through a targeted and sustained marketing campaign is critically important. The campaigns need to be aimed at leading private equity funds targeting South East Asia investments; corporate industry leaders and key diaspora clusters in target markets such as Canada, the EU, the Middle East, and the United Kingdom. The targeting exercise should begin with a detailed mapping exercise.[13]

Policy Implications of Key Recommendations:

Sri Lanka's policy makers' keen focus on inclusion drives the focus of this report and its recommendations as to how best to leverage the significant level of remittances the country relies on and which gives it the opportunity for empowerment as it links migrant workers, the diaspora and international investors to the funding of much needed large scale infrastructure projects.

The following lists key policy initiatives that are recommended to further facilitate rural household inclusion; safeguard of migrant worker returnees; long term capital formation for infrastructure investment; proper economic and financial incentives and the establishment of key linkages:

Introducing Migrant Endowment Savings Account (MRSA)

SLFEB should suggest that migrant workers open two savings accounts prior to departure. One account in their own name that are restricted savings akin to retirement savings accounts; and one in the name of their family. Migrant workers should be encouraged to allocate or instruct receiving banks to allocate on their behalf a sustainable percentage of their remittances to these endowment accounts such that this represents a growing stock of long term capital formation and a financial safety net for when they return in typically 5 years' time.

Link Migrant Endowment Savings Accounts to MFI Loan Portfolios

To increase the flow of loans to MFI portfolios that yield about 20% returns with little or no defaults, the capital available in Migrant Endowment Savings Accounts can enjoy higher yields than what is offered by

[13] OECD (2012), "Sri Lanka", in Connecting with Emigrants: A Global Profile of Diasporas, OECD Publishing. http://dx.doi.org/10.1787/9789264177949-20-en

typical bank savings accounts (currently yielding 6.33%). The **compounding effect** of these returns on stable capital would create an important financial safety net and lead to long term capital formation. These loans can be further secured by **ADB savings guarantee scheme**, therefore eliminating completely the risk of loss as a result of default. These loans can be more efficiently channeled through RDD or SEEDS who would play the role of ADB guaranteed loan clearinghouse for various MFIs. RDD can further determine which MFI is deserving based on performance metrics its uses to make its own loans.

For policy makers the comfort of adding an ADB savings guarantee to migrant endowment savings accounts that are invested in MFI loan portfolios would make all the difference. By adding an ADB guarantee to the scheme, policy makers' focus would shift to the socio economic impact of such a scheme rather than focus on the political implications of loan defaults.

It should be noted that financial literacy should always be a key component of the scheme.

Central Bank to issue Sri Lanka Diaspora Bonds

With RDD's successful social inclusion activities and experience working with donors as an implementer and provider of program oversight, it can play an even greater role as overseer of the use of proceeds from the central bank issuance of Sri Lanka diaspora bonds.

PDD exhibits a keen understanding of capital markets and its expertise in arranging the issuance of Sri Lanka Diaspora Bonds will be invaluable. As a result, it is recommended that an internal committee be formed bringing together RDD and PDD to launch and oversee the disbursement of proceeds of diaspora bonds.

It should be noted that these bonds be distributed widely as <u>both listed and privately placed</u> in markets where the diaspora are known to reside.

SEEDS to issue Diaspora Bonds

Because of SEEDS extensive network, deep experience working with the poor and marshalling significant sums of capital – its SME loan portfolio currently standing at $200 million – it should be given the authority to issue diaspora bonds directly to the diaspora, under the supervision of the MFI regulator or the central bank. If this were to be feasible, SEEDS would focus on issuing a diversified range of diaspora bonds such as:

<u>SEEDS SME Microloan Diaspora Bonds</u>: whose proceeds are used to finance microfinance loans for families in rural areas thereby achieving financial inclusion;

<u>SEEDS Housing Loan Diaspora Bonds</u>: whose proceeds are used to finance mortgages for house purchase by families in remote areas – providing capital access and further household capital formation and inclusion;

<u>SEEDS Migrant Skills Development Diaspora Bonds</u>: whose proceeds would be used to provide vocational training and further increase the earning power of migrant workers recruited for jobs

overseas. The result of this is a virtuous circle of higher skills leading to higher earnings, in turn resulting in higher savings into *MRSAs* as described above.

SEEDS could also introduce regional or industry focused diaspora bonds with the same classifications. However, it is recommended that regionalism not be the focus of the motivation to incent diasporans to invest back home. In all cases, SEEDS should report on the impact elements by demonstrating how proceeds have led to better socio-economic outcomes. A reporting framework which SEEDS could adopt is the **Global Impact Investment Network** (GIIN) reporting framework.[14] Key here is that these SEEDS Diaspora Bonds will be marketed widely and sustainably such that they **become the portal of choice for diaspora** seeking to make an impact and access attractive yields by investing "back home".

Summary of Proposed ADB Pilot Projects:

To facilitate ADB follow up we have listed recommended pilot projects to be proposed to ADB:

1. Provide savings guarantees to migrant worker endowment savings accounts that would invest in MFI loan portfolios via state banks;
2. Provide partial capital guarantees to Sri Lanka Diaspora Bonds issued by the CBSL and SEEDS;
3. Provide partial capital guarantees to BOI pipeline of structured projects directed at international and diaspora investors;
4. Assist in demonstrating the effectiveness of Future Flow Securitization with a partner bank;

Conclusion:

Sri Lanka present unique opportunities to effectively leverage remittances, which represent a key pillar of the economy. Policy makers should be commended for the level of effort and the consistent focus on inclusion with the creation of an enabling environment that facilitate to widespread use of known successful tools such as microfinance. However, with remittances representing in excess of 8% of GDP, more can be achieved with effective policy changes to unlock significant resources that would empower Sri Lanka through its migrant workers, its diaspora; foreign investors, and its existing network of economic players to achieve independent sources of finance for much needed infrastructure and other long term projects.

We want to thank the Asian Development Bank, the Sri Lanka office and staff, and specifically Ms. Mayumi Ozaki for the effective guidance of the mission and the timely unlocking of much needed resources that facilitated this study.

[14] Please see: https://iris.thegiin.org/

Attachment I: Model Cash flows for target Securization Project

The basic premise for securitizing remittances is to access lower cost of capital than could be access by going directly into the capital markets. However, to get the attention of investors, yields have to be comparatively attractive on a risk/reward basis, notwithstanding the possibility of a "patriotic discount" which is only achieved following a concerted outreach effort.

The example below showcases how cash flows are structured in a typical infrastructure project securitization. Key issues addressed are: dealing with interest accrued on idle cash; determining coupon levels; mismatched cash flows.

Determining effective interest rate when Cash flows are mismatched:

Issuer pledges $25 million in future flow receivables.
Issuer Issues $25 million in bonds – settled rate is 10% (negotiated and based on comparable and ratings).
Issuer must pay $2.5 million in interest over the next 10 years or $250,000 per year. Plus, principal at Year 10.
Proceeds are invested in building toll roads that will yield $5 million per year in revenues. However, there are construction costs resulting in the need for 3-year grace period, over which interest is accrued, as negotiated:

- Accrued interest over grace period: $250,000*3 = $750,000. Over 10 years +$75,000 each year in additional interest.

Effective interest paid including grace period: $2,500,000 + $750,000 or $3,250,000 or an effective rate of 13%. NB: these rates can be negotiated. For instance, if the issuer receives an ADB guarantee on 50% of the outstanding obligation, this is leverage the issuer could use to lower or eliminate grace period accruing of interest rates. Also, some concessional financing can be obtained by the construction company eager to obtain more construction contracts (builder financing).

Any guarantee that is offered can be deducted from the investor's coupon payment as well as passed on to the underlying project. For instance, a guarantee fee of 2.5% per annum can be paid in full by the investor (13% - 2.5% = net coupon of 10.5%).

For further research please see: http://people.stern.nyu.edu/igiddy/ABS/absasia.pdf

Attachment II: Outreach Plan and Pro Forma Budget

For successful participation by global diaspora into issuance and distribution of diaspora bonds, it is important to develop and implement an effective outreach plan. This plan should begin with the effective mapping of diaspora by geographical location, income levels, professional occupation and level of engagement with the home country. This exercise does not preclude a good understanding of the regulatory regime to which the distribution of diaspora bonds would be subject to in each target host country. This list does not include securities registration requirements and the cost associated.

Below are the steps required for an effective diaspora outreach program, as well as an estimated budget for pre-sales and distribution activities, as well as on-going diaspora engagement. This latter activity will set the stage for successful future diaspora bond placements:

Diaspora Outreach Plan (estimated budget per country):

1. Diaspora mapping exercise ($10,000 - $20,000)
2. Identification and outreach to relevant diaspora associations ($5,000 - $10,000)
3. Socializing databases in compliance with global anti-spam laws ($5,000 - $10,000)
4. Development and roll out of social media campaign – Phase I ($50,000 – $100,000)
5. Targeted Meet-Ups organized through relevant diaspora associations ($100,000)
6. Identification of key distribution partners (listed and private placement) – educating them on offerings, databases and incentives ($250,000)
7. Distribution of summary investment project pipeline details and identification of key spokespersons (social media and live media) ($250,000)
8. Investor Education (how to) module development and roll out via social media and traditional media campaign – Phase II ($500,000 - $1,000,000)
9. Distribution campaign with use of social media content created in (5), (7) and (8) ($250,000)
10. Follow up social media campaign – Phase III: on-going campaign ($100,000 - $250,000 annually)

Estimated total: $1.5 million. This is inclusive of an annual outreach upkeep budget of $250,000.

Attachment III: Future flow Examples in Other Countries

The below links provide insight into past FFS transactions registered in the region whether public or private. Please note that some refer to in-country securitization of FFS. These should be considered as proxies for regulatory sophistication and location of local expertise:

http://corporate.findlaw.com/finance/securitization-in-asia.html

http://www.citigroup.com/transactionservices/home/about_us/press_room/2011/2011_1208b.jsp

http://www.borrowersandinvestorssea.com/speaker/lesi-zuo

http://maalot.co.il/publications/SR20140324134155.pdf