ADB

Technical Assistance Consultant's Report

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Regional: Promoting Remittance for Development Finance

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For Asian Development Bank

Asian Development Bank

ASIAN DEVELOPMENT BANK

Remittances for Development Program

The People's Republic of Bangladesh

Feasibility Study Report

June 2016

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GLOSSARY OF TERMS

ADB	–	Asian Development Bank
BMET	–	Bangladesh Bureau of Manpower, Employment and Training
BOI	–	Bangladesh Board of Investments
BRAC	–	MFI: BRAC Bank Ltd microfinance institution, and NGO tied to the bank
DBBL	–	Dutch Bangla Bank Ltd
GDP	–	Gross Domestic Product
ISL	–	Isla Bank Ltd
MESA	–	Migrant Endowment Savings Account
MFI	–	Microfinance Institutions
MTC	–	Money Transfer Companies
MRA	–	Microfinance Regulatory Authority
PKSF	–	Palli Karma-Sahayak Foundation
TMSS	–	Thengamara Mohila Sabuj Sangha
SEC	–	Bangladesh Securities and Exchange Commission
SME	–	Small and Medium-sized Enterprises
Tk	–	Thaka – Bangladesh national currency
UCL	–	Union Commercial Bank Ltd
USAID	–	United States Agency for International Development

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 Bangladesh for development finance. The study is meant to identify opportunities for policy intervention that would result in efficient leveraging of alternative resources as a reliable source of long term development finance. The study proposes to identify tools, solutions and best practices, and to demonstrate how the mobilization of these alternative sources of capital can be structured. The study took place between February 12th and 18th, 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 (London).

KEY CONTEXTUAL ELEMENTS

At US$13.5 billion, or approximately 8% of GDP, annual remittances play a significant role in underpinning the Bangladesh economy. Key known factors include a large population; adequate literacy rates; and a reliance on two key industries: garment exports and remittances. Microcredit plays a significant role in uplifting the very poor and including them in broad base economic growth. Having fathered the microcredit industry, Bangladesh remains deeply committed to the notion of financial inclusion with a deep focus on facilitating access to capital by low income households. This has led to an explosion of microfinance service providers. In addition, policy makers have focused keenly on facilitating the delivery of remittances to rural areas by encouraging partnerships between banks, money transfer companies (MTC) and Microfinance institutions (MFI). As a result, Bangladesh has an extensive overlapping remittance delivery coverage network with varying degrees of penetration.[1]

Bangladesh has over 10 million migrants who work in low to mid-level jobs, earning wages and remitting between $300 - $600 per month on average. However, Bangladesh also has a wealthy contingent in the United States, in Canada and in the United Kingdom who, by all accounts remit significantly back to Bangladesh: approximately US$10 billion from 250,000 Bangladeshis in the US alone, according to a recent USAID report.[2] The majority of these diaspora show a keen interest in investing “back home” in a structured way. Current offerings directed at them have been underwhelming in scope, in depth and in distribution.

Banks and MFIs provide a broad range of financial products directed at the families of migrant workers. However, the offerings to migrant workers themselves are relatively scant in scope. The emphasis has been less on the migrant worker and more on their families that have remained in Bangladesh. This has caused sustenance issues for returnee migrants who rarely have personal savings they can rely on independently of those the family may have already consumed.

MFI institutions are well developed and are looking to introduce means of increasing self-finance by applying to provide savings products to non-members. The Microcredit Regulatory Authority (MRA), who regulates all MFI in Bangladesh, is not likely to approve such a widening of MFI mandates due to a deep concern about oversight and governance issues within MFI. It should be noted that widening the

[1] Asian Development Bank Country Strategy Partnership 2011 – 2015.
[2] USAID: Bangladesh Diaspora Assessment Project – June 2015

scope of MFI savings to include non-members would in essence turn them into banks which would possibly shift oversight of the MFIs to Bangladesh Bank, the central bank.

MRA tightly oversees the MFI industry. It has deep knowledge of key players and their internal policies. It is looking for new ideas to further push financial inclusion. It has no objection to new "investment accounts" linked to MFI loan portfolio – but would prefer if these linkages come with financial literacy tests. These tests and related financial education would be offered by the Bangladesh Bureau of Manpower, Employment and Training (BMET) and participating partners.

KEY RELEVANT FINDINGS

1. There is ample evidence that the government is crowding out the private sector from access to financial resources by engaging in significant short-term, expensive borrowing from banks via high yielding savings accounts (interest rate differential between government offerings and private sector deposit rates is in excess of 500 basis points – 6.43% vs. 11.76%.[3]) As a result the government is running a yield curve exposure that is very costly - borrowing short at higher than market rates and investing long at relatively lower rates of return. The maturity mismatch presents a clear and present risk.

2. Foreign Direct Investments (FDI) into the country are at a stagnant $1 billion per year, or less than 1% of GDP. Investments have come primarily from Chinese and Indian interests. One of the biggest impediments to foreign capital investment is the lack of structured projects that are investment-ready.

3. Private banks control in excess of 60% of remittance flows. This is a significant fact as it presents Bangladesh with a unique opportunity to realign long term funding needs for infrastructure investments with long term sources of funding, thereby eliminating the yield curve exposure discussed above. The leveraging of remittance flows using a collateralized loan program with maturities of 10yr-30yrs would enable the government to source permanent capital needed for long-dated investments without resorting to using short-term funding that crowds out the private sector from the banking system.

4. Bangladesh has a myriad of financial instruments that are available to domestic savers as well as to migrant workers. However, only three (3) investments are directly available to diaspora investors, who are classified as foreign investors.[4] The three (3) financing instruments that are available to the diaspora are the USD Premium Bond; the USD Investment Bond; and the USD Development Bond. Neither is listed in foreign markets as the Bank of Bangladesh has not engaged with foreign regulators to register these securities and make distribution arrangements with foreign brokerage houses. Their availability assumes that the diaspora is aware of them and need to make an effort to purchase them from local market brokers. Yet, the central bank and the SEC are members of international regulatory associations that could easily be lobbied to provide favorable and cost efficient treatment of these securities if classified for development

[3] Cf. Star Business Daily: "Sales of savings instruments soar" – by Rejaul Karim Byron – February 18, 2016.
[4] Bangladesh Board of Investments (BOI)

purposes. Such treatment would include, but not be limited to, benefiting from regulatory exemptions in the host countries.

5. Palli Karma-Sahayak Foundation (PKSF) and Thengamara Mohila Sabuj Sangha (TMSS) are significant players in the microfinance market and present key opportunities to achieve significant financial inclusion through a combination of policy decisions**:**

    a. **PKSF as a key financier of MFI**. PKSF has significant regulatory flexibility to raise capital from diaspora and migrant workers to finance MFI such as TMSS. This can be accomplished by the introduction of **PKSF diaspora bonds** (e.g.: PKSF Microfinance diaspora bonds; PKSF SME diaspora bonds; PKSF Agriculture diaspora bonds…) whose yield is tied to returns generated by MFI's SME loan portfolios – currently standing at 20%-25%. ADB could provide bond guarantees that provide downside risk protection to diaspora investors. A pilot program could be introduced to provide proof of concept. This would achieve several objectives: 1. leverage the significant financing flexibility that PKSF has, while taking advantage of its key position as prime financier of a network of MFI; and 2. PKSF diaspora bonds could be sold to diaspora abroad;
    b. **Working with Banks, PKSF can borrow from migrant savings accounts**. Here it would be leveraging its Preferred Borrower Status to provide higher yields to migrant depositors sourced from its MFI loan portfolios. An ADB guarantee could further substantiate existing deposit insurance provided by the banking system. Such a guarantee would need to be structured within the loan portfolio – most likely as matching provision against defaults. Diaspora investors would take advantage of the higher yields and low default rates while enjoying ADB guarantees.

6. BMET who clears migrant workers before they leave to take up posts overseas requires that each migrant worker open a bank account to facilitate the transfer of wages to their families back in the villages. To strengthen migrant worker safety net when they return and further build permanent capital for long term investments, BMET could require that each migrant worker open two (2) accounts: one for themselves; and another for their relatives. This would allow them to grow their savings stock over time and engage in long term investments that generate yield, but also be a direct source of funding for MFIs. This approach is keenly important as Bangladesh looks to increase the number of semi-skilled and skilled workers who are sent abroad. Increased skills translate into higher earning power, which in turn means higher savings back home. Skilled migrant workers are more prone to seek financial literacy to manage long term savings and investments.

    These migrant worker personal savings account could take on the character of Individual Retirement Accounts (IRAs in the USA) that require small allocations from wages over time that are restricted in terms of withdrawals, but against which migrant workers can borrow up to a limit. We shall call these migrant endowment savings accounts (MESA).

7. We've observed a low level of mobile banking penetration compared to countries like Kenya who have leapfrogged Western nations with e-banking services that are convenient, secure and

easily adopted by migrant workers. Our initial analysis suggests that this is caused by key differentiating factors: telecommunication companies were late to the money transfer game in Bangladesh. Banks are well established and yield significant power over access to migrant workers. However, in Kenya, the central bank and the ministry of finance chaperoned the wide use of mobile banking as a challenge to the banking establishment. Bangladesh could easily catch up given the widespread use of mobile devices, by simply mandating that banks, MTC and MFI all introduce mobile banking services and promote adoption.

8. According to a recent USAID study, about 250,000 Bangladeshis reside in the U.S.A. and are responsible for $10 billion in remittances.[5] A significant number are high net worth individuals and families who have set up charities and are actively involved in philanthropic activities in Bangladesh already. They have reportedly helped set up schools, hospitals and other social ventures in their villages or regions. However, the diaspora is also very keen to engage in capital investments into credibly designed, transparent projects of significance that are both impactful and prospectively profitable. This is where Bangladesh falls short in catering to pent up diaspora capital seeking investment opportunities. The diaspora is a separate class of expatriate workers and any outreach policy should be distinctive and apart from those targeted at engaging semi-skilled migrant workers. The capital mobilization tools should be different and should assume very distinct motivations and levels of engagement.

CHANNELING REMITTANCES FOR DEVELOPMENT: A BANGLADESH SOLUTIONS TOOLKIT

1. Achieving Greater Financial Inclusion and Security for Migrant Workers – Case of Returnees

    a. In order to achieve greater financial inclusion, it is important that **returnee migrant workers are given the opportunity to secure their own savings** separate and apart from those for their relatives. As their income grows they can store savings separately, ring-fenced until they return back to Bangladesh, all the while receiving financial literacy training from MTC and MFI while abroad. Key here is to have migrant workers be given the option to set up two separate accounts upon meeting with the BMET before going abroad. They can fund their personal savings account at some suggested sustainable percentage based on their income level or by instructing their employers to send portions of their earnings directly to the accounts set up for this purpose. This structure should be suggested by BMET in order to create permanent savings that become a safety net upon their return, and against which they can borrow from MFI for housing and starting a small business. The alternative, is that they return with no savings and become destitute wards of the government or of their families who would have consumed all the transfers.[6]

       We have explored with BMET the concept of setting up two accounts with one being a MESA similar to an Individual Retirement Account (IRA) which his widely used in the OECD. Similar to IRAs, migrant workers can borrow against the balance in the

[6] IMF Bangladesh Strategy Report: Sixth 5yr Plan 2011 – 2015: Accelerating Growth Reducing Poverty.

endowment savings account up to a limit set by regulators or suggested by BMET. The notion of endowment focuses on creating "**permanent capital**" which is a form of long term capital mobilization. Contributions into the account would be income based or simply a percentage of transfers. It should be noted that Term Deposits are not a good substitute since the holder can break into the account at any time. Therefore, using Term Deposits as an alternative eliminates the engine of the safety net – compounded interest.

Linking MESAs to MFI loan portfolios. MFIs are not allowed to take savings from non-members. To increase MFI lending, policy makers essentially have two choices: (a) they can **allow MFIs to take deposits of migrant workers whose parents are already members**, thereby making it easy for MFIs to provide financial products to migrant workers. Here the opportunity is clear – since endowment savings constitute permanent long term capital, MFIs can borrow from these account to make microloans and pay migrant savings accounts attractive returns in the order of 10%-15% (significantly above current savings rates of 6.35%), thereby creating a significant incentive to fund these endowment savings accounts; (b) **MFI's can partner with Banks to offer MFI endowment savings accounts on the Banks' financial services platform. Savings into these accounts can in turn be lent to MFIs by the Banks**.[7] To achieve access to more savings while addressing MRA's concerns, Banks could manage endowment accounts on behalf of MFIs.

b. In either situation, the opportunity is to link endowment savings accounts to MFI lending activity while making sure that they remain safe and protected. Since the default risks are very low (less than 10%) and the rates of returns received by MFI are still relatively high (approx. 20%-25%) these loans can be further protected with ADB guarantees, further reinforcing the incentive to save into these accounts.

This approach empowers migrant workers to control their own destinies via these endowment savings accounts, but also gives them the opportunity to learn and participate in broader financial inclusion. In addition, this approach addresses the problem of remittance consumption and clears the way to directing more remittances towards the productive sector.

2. Leveraging PKSF's unique position to tap into diaspora capital – The case of introducing **PKSF diaspora bonds.**

PKSF enjoys several unique exemptions under Bangladesh law. They have a significant track record and are the premier funder of key MFI in Bangladesh. However, they have been seeking new ways to fund a growing need for financial inclusion through a vast MFI network. We believe

[7] There is a significant regulatory difference between MFI's selling savings accounts to non-members and having partner Banks do it for them under a restricted savings instruments labelled: MFI Savings Account.

that the diaspora, which remits in excess of $10 billion annually, and are looking to invest in excess of $2 billion into projects back in Bangladesh, are ripe for PKSF investment instruments:[8]

a. PKSF could issue **PKSF diaspora bonds** that yield 10%-15% with maturities of 3y – 5yr on a rolling basis where the returns are coming from loans they make to MFI's whose returns are 20%-25%. PKSF can structure these bonds by region, by sectors or by industry and market them as such;

b. These PKSF diaspora bonds can be offered as **listed securities** in various jurisdictions and sold to both high net worth and retail investors via brokerage networks; and/ or PKSF diaspora bonds can be **privately placed** to accredited investors in each region (Asia, EU and Americas). Both these approaches are not mutually exclusive. It should be noted that listed securities are financial instruments that have passed regulatory checks; are available on an exchange to anyone; and are distributed by registered brokers who in turn price the securities and make markets for buyers and sellers. Privately placed bonds, however, are sold only to qualified or accredited investors who are looking to buy and hold securities for the long term and for which a secondary market is not readily available.

c. **PKSF diaspora bonds can carry ADB capital guarantees**, at least initially so that the marketing power of the ADB brand can attract the largest number of participants.

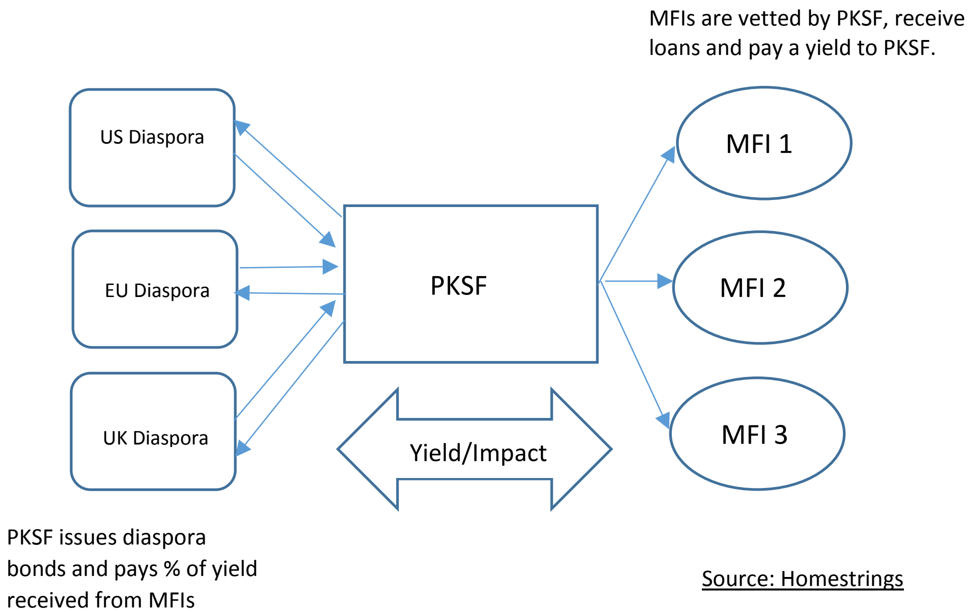
   The ADB guarantee could structure a partial guarantee as a contingent liability. For instance, the US Treasury issues Development Credits under its Development Credit Authority which constitute a claim on the US Government in the event of a default. Alternatively, ADB could set up a fund such as a passively managed Trust Fund, capitalized up to the level of outstanding PKSF loans (50%). Moreover, ADB could simply purchase private insurance and have PKSF defray the premium cost from the yield that is paid to investors.

d. PKSF diaspora bonds would need to be **extensively marketed** via a number of media channels. This marketing would need to be sustained, extensive and broad based.

Here, PKSF would be channeling diaspora capital to the productive sector through its existing network of MFIs and turning itself into a powerful economic funding agent.

[8] The World Bank estimates that estimated diaspora investment flows are typically 25% of global remittances – Sonia Plaza, Senior Economist, World Bank Migration Department. Since $10 billion of remittances come from the US Bangladesh diaspora alone, then 25% of $10 billion = $2.5 billion investment capital to target.

Schematic of PKSF Diaspora Bond



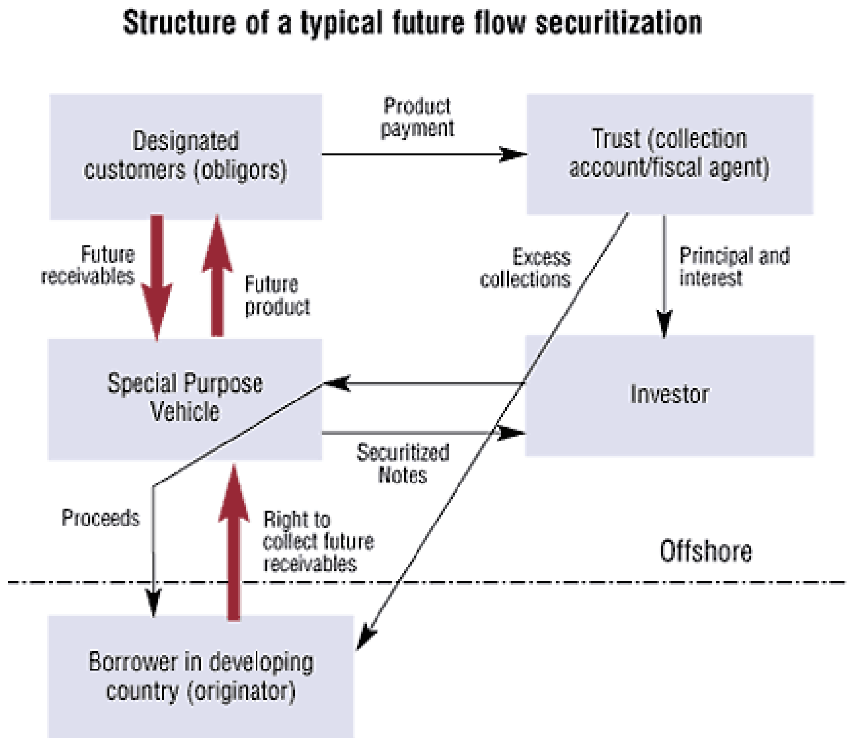
Source: Homestrings

3. Leveraging commercial bank's unique position as largest distributors of remittances – Securitizing Future Flows for Infrastructure Finance[9]

   Bangladesh has five (5) private banks that control over 60% of all remittances that enter the economy. This presents a unique opportunity to finance infrastructure projects. Under international banking laws, banks can issue debt collateralized by remittances that they control. Remittance backed bonds usually receive high credit ratings. Cost of funds is cheaper than sourcing short term capital in the domestic banking market. There is also the possibly to issue in Thaka (Tk) for local institutional investors such as pensions and insurance companies seeking to hedge their long term liabilities with long dated investments. **These Remittance backed bonds could carry ADB guarantees and be targeted at the diaspora as well as targeted at global institutional investors who are seeking yield and security. In turn, policy makers will have access to a large continuous pools of capital to finance much needed infrastructure projects.**

   Collateralizing remittances for efficient long term sovereign funding falls under the theme of future flow securitization. Although Bangladesh does not have securitization laws, it would be advisable to have a demonstration pilot project with one of the banks. The pilot project conducted under the joint oversight of the Bangladesh SEC and ADB would be followed by technical assistance and training programs for both banking practitioners and banking regulators.

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



Source: IMF

4. Preparing BOI Project Pipeline for diaspora Investment

   BOI has identified a number of key projects that are development priorities and which need investment capital. The January 2016 Bangladesh Investment and Policy Forum yielded interest but very little transactions. The main reason being that very few projects were "investment – ready". Preparing BOI's pipeline entails focusing on project preparation. BOI's focus up to now has been on creating an enabling environment such that global private players can be attracted to working and investing in Bangladesh. In this vein, BOI has focused its efforts on creating eight (8) export zones, two of which have already been established. However, the pipeline of projects remains unstructured. International interest is likely to focus on the attractive proposition of providing products and services to a growing population that stands at over 150 million. Key industries include: pharmaceuticals; power/renewable energy sector; plastics; telecoms; ship building; healthcare; agricultural processing.[10] The transactions would need to be structured and have the following key features among others:

   a. A favorable regulatory coverage
   b. Existence of purchasing agreements that are anchored in equitable recourse rules

[10] A survey of global industry leaders and diaspora investors can be conducted to confirm these choices.

c. Possibility of creating durable Public Private Partnerships where the local partner provides local distribution; provides access to local sources of funding; enjoys favorable relations with the government that leads to access to DFI facilities
d. Availability of legal documentation and industry due diligence reports conducted by reputable international advisory services – which will be purchased by international partners
e. Approved securitization schemes to help mobilize domestic savings and diaspora capital.

Industry offering packages could be marketed to international investors with a targeted, sustained marketing campaign aimed at industry leaders and key diaspora clusters in key markets (US, EU, Middle East, Asia).

Existing investment offerings for international investors such as the USD Premium Bond or the USD Development Bond are not well structured. They provide very little transparency on use of proceeds nor do they provide any sense of the socio-economic impact that these bonds have. However, BOI sourced project bonds would be very interesting to test among the diaspora.

To convert BOI's pipeline into investment-ready projects, BOI would need to retain an advisor to assist with the key tasks such as project identification, project structuring, project documentation, project marketing strategy, securities issuance and provision of oversight on use of proceeds, as well as tracking and reporting on social impact. These can all be achieved with a team of consultants attached to BOI in which it plays the role of lead. The funding instruments could be issued by the central bank as project linked sovereign bonds. The proceeds could be paid directly to the projects - which we suggest be structured as public-private partnerships.

POLICY IMPLICATIONS OF KEY RECOMMENDATIONS

Bangladesh policy makers are keenly focus on inclusion and this is the main focus of this report. The report's recommendations lay out how best to leverage remittances for development by empowering migrant workers and the diaspora, and linking them to the funding of large scale, and much needed, infrastructure projects.

The following lists key policy initiatives recommended to increase rural household inclusion; safeguard migrant returnees; and pool long term capital for infrastructure investment:

Introducing Migrant Endowment Savings Account (MESA)

BMET could suggest that migrant workers open two savings accounts prior to departure. One account in their own name that are endowment savings akin to restricted 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. These savings will represent a growing stock of long term capital. This capital formation will serve as a social financial safety net for when they return in typically 7 to 10 years' time.

1. Link Migrant Endowment Savings Accounts to MFI Loan Portfolios

There is an opportunity to increase the flow of loans to MFI portfolios by linking migrant endowment savings accounts to MFI loan portfolios. Migrant worker endowment account will enjoy higher yields with little chance of defaults. The **compounding effect** of yields earned in the endowment accounts would create an important financial safety net, and facilitate domestic long term capital formation. These loans can be further secured by an **ADB guarantee scheme**, at the MFI level. This would eliminate completely the risk of loss. These loans can be more efficiently channeled through PKSF. PKSF can further determine which MFI is deserving of additional capital based on performance metrics its uses to make its own loans.

For policy makers the comfort of adding an ADB guarantee to protect migrant endowment savings that are invested in MFI loan portfolios would make all the difference.

2. PKSF to issue diaspora Bonds

PKSF is in a unique position. It enjoys special regulatory status with Bangladeshi authorities. PKSF has a board that is keen on financial innovation that leads to further financial inclusion achievements. PKSF's need for further capital puts it in a unique position to issue its own securities to an audience eager to invest: the Bangladeshi diaspora. PKSF makes it easy for the diaspora to claim having a social impact and having access to attractive returns. Securities issued by PKSF would be medium term notes: 3 years to 5 years in maturity. These note would have coupons that reflect the yields that MFI loan portfolios currently return – adjusted for PKSF's fees. An attractive yield paid to diaspora investors should range between 10% - 25%. These notes could be further reinforced with ADB guarantees on capital invested. The notes could be structured to reflect the actual use of proceeds thereby providing clear transparency and the ability to more easily report on social impact of the loans – a key incentive for diaspora investors.

Therefore, PKSF could issue:

PKSF SME Microloan diaspora bonds: whose proceeds are used to finance microfinance loans for families in rural areas thereby achieving financial inclusion;

PKSF Housing Loan diaspora bonds: 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;

PKSF Migrant Skills Development diaspora bonds: 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 *MESAs* as described above.

PKSF could also introduce regional or industry focused diaspora Bonds with the same classification. However, it is recommended that regionalism not be the focus of the motivation to incent diasporans to invest back home. In all cases, PKSF will report on the impact elements by demonstrating how proceeds have led to better socio-economic outcomes. A reporting framework which PKSF could adopt is the

Global Impact Investment Network (GIIN) reporting framework.[11] Key here is that these PKSF 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".

3. ADB to pilot Future Flow Securitization demonstration

Given the importance of remittance flows to Bangladesh, we recommend a policy initiative demonstrating the use future flow securitization to access permanent long term capital for the financing of long term infrastructure projects. It has been confirmed that Bangladesh has no securitization laws and has not considered this as a policy priority, primarily because of a lack of evidence of its potential. Here, the opportunity exists for ADB to showcase the results of such a policy.

There are five banks which represent in excess of 60% of all remittances that enter the country. The largest recipient of these remittance flows is Islami Bank Ltd (IBL) with over Tk 16,367 million in 2013; followed closely by Dutch-Bangla Bank Ltd (DBBL) at Tk 14,792 million; and rounding out the top 3 is UCBL at Tk 11,856 million.[12] These banks have varying degrees of financial sophistication which in turn would impact the reception of a pilot project around securitization. The bank the consultant visited, BRAC Bank is one of the smallest recipients of remittances, and has falling market share (from 6% to 4% between 2013 and 2015). However, BRAC Bank presents a level of financial sophistication that could be propitious for a demonstration pilot program that could later pull in the other larger banks. It would be important to assess available resources to conduct and follow through with the pilot to insure success and therefore the desired demonstration effect that would not only affect the banks but also policy makers.

It should be noted that unlike Sri Lanka, Bangladesh doesn't present a significant state bank presence in the remittance market. As a result, resource mobilization for infrastructure finance will require private sector participation. The banks would need to be incentivized to finance infrastructure through FFS and on-lending to the government and other infrastructure partners. This relationship is more direct in countries where the state bank is the largest player in the remittances market (cf. Bank of Ceylon).

4. BOI to structure a pipeline of investment-ready projects

BOI presents a unique opportunity to connect Government investment priorities to diaspora demand for investable projects. However, little effort has been made by BOI to package the rich pipeline of projects they have and to market them effectively to international investors. This would include wealthy diasporans who have expressed keen demand for such structured investments. The consultant met with 10 such families in Silicon Valley, California, as part of a separate USAID exercise. The message was clear: they want to invest in professionally structured, impactful projects in Bangladesh. We believe that the feeling is the same for other clusters around the world, such as in Canada and in the United Kingdom.

To achieve this, BOI would need to invest, with the help of ADB, in project development and legal structuring. This exercise would result in investment-ready projects which BOI and its affiliates could sell to international investors and to diasporans directly through various distribution platforms, including retail brokers, online distribution platforms and privately placed equity and debt interest.

[11] Please see: https://iris.thegiin.org/
[12] Source: UCBL Annual Report – 2013.

The result of such concerted efforts would be a markedly noticeable increase in FDI and diaspora participation. It should be noted that ADB would be called to play a key role in credit enhancement of key projects such as in: agriculture processing, pharmaceuticals, renewable energy, and infrastructure.

5. Mandating increased use of mobile banking platforms

Because of the policy emphasis on banking the poor and on use of MFI's physical penetration to remote areas, little emphasis has been put on the use of technology to achieve similar results. We've seen in countries such as Kenya, where the use of mobile banking has introduced leapfrogging results; where the adoption of easy to understand electronic tools has led to an explosion of e-banking services, thereby outstripping formal banking relationships and introducing more efficient means to provide financial services. These services have included micro-insurance, micro-mortgage loans, cash transfers as well as delivery of medical services.[13]

The Economist's in depth review of Kenya's worldwide lead and the impact on the economy should give Bangladesh policy makers pause about the role that technology could play in achieving their inclusion goals. The important element is that technology can easily complement current "brick-and-mortar" initiatives. In fact, there is clearly a multiplier effect that technology would bring to achieving policy makers' objectives, in a shorter time frame than normally expected.

SUMMARY OF PROPOSED ADB PILOT PROJECTS

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

1. Provide partial capital guarantees to PKSF diaspora bonds;
2. Provide partial capital guarantees to BOI pipeline of structured projects directed at international and diaspora investors;
3. Assist in demonstrating the leveraging power of Future Flow Securitization for long term infrastructure investment, with a partner bank;
4. Feasibility and Impact study of widespread use of mobile banking among migrant workers.

NEXT STEPS

To achieve success, a proper sequencing of events has to be adopted, starting with achievable short term goals to create positive momentum. It is recommended that ADB begin with piloting **PKSF diaspora bonds** since the institutions has significant flexibility to engage without undue regulatory impediments. This would enable PKSF to demonstrate this new source of capital and set itself up to provide support to borrowing from Bank with MESA products. Then we recommend that ADB focus on **assisting BOI in developing a pipeline of investment-ready projects**. This would create an impetus to focus on process and engagement of relevant parties and to meet the already pent up desire to increase FDI over the $1 billion mark it has remained at for some time. Subsequently, ADB would need to prepare a policy paper geared at influencing policy makers to mandate the 2 bank account and the **introduction of MESAs** and its link to PKSF/MFI loans – backed by ADB savings guarantee scheme. This could be piloted with BMET or TMSS, both of who collect remittance. Success from that demonstration would lead to ADB beginning

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

work on **developing and implementing a FFS pilo**t with BRAC Bank or DBBL on a limited basis under the aegis of the SEC. Subsequently, ADB could write a persuasive policy paper such that it results in new securitization laws being passed in Bangladesh and the training of bank officials on its use, as well the training of regulators (SEC) on how to oversee and regulate its use.

The combination of these initiatives will result in substantial capital mobilization for long term infrastructure finance, the increase in FDI and broad positive diaspora and migrant worker engagement in the development of Bangladesh.

CONCLUSION

Bangladesh presents unique opportunities to effectively leverage remittances, which represent one of two pillars 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 facilitates widespread use of known successful tools such as microfinance. However, with remittances representing approximately of 8% of GDP, more can be achieved with limited policy changes to unlock significant resources. This would empower Bangladesh through its migrant workers, its diaspora and its existing network of economic players to achieve independent sources of finance. These funds could then be used for much needed infrastructure investments that in turn lead to accelerating poverty reduction.

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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 comparables 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

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.

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