



Technical Assistance Report

Project Number: 51118-001
Knowledge and Support Technical Assistance (KSTA)
January 2018

Strengthening Asia's Financial Safety Nets and Resolution Mechanisms (Cofinanced by the People's Republic of China Poverty Reduction and Regional Cooperation Fund and the Republic of Korea e-Asia and Knowledge Partnership Fund)

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Asian Development Bank

ABBREVIATIONS

ADB	–	Asian Development Bank
AMC	–	asset management company
DMC	–	developing member country
IPAF	–	International Public Asset Management Company Forum
NPL	–	nonperforming loan
PRC	–	People's Republic of China
RCI	–	regional cooperation and integration
ROK	–	Republic of Korea
TA	–	technical assistance

NOTE

In this report, "\$" refers to United States dollars.

Director General	Yasuyuki Sawada, Economic Research and Regional Cooperation Department (ERCD)
Director	Cyn-Young Park, Regional Cooperation and Integration Division, ERCD
Team leader	Junkyu Lee, Principal Economist, ERCD
Team members	Paulo Rodelio Halili, Senior Economics Officer, ERCD Marilyn Parra, Senior Operations Assistant, ERCD Peter Rosenkranz, Economist, ERCD

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KNOWLEDGE AND SUPPORT TECHNICAL ASSISTANCE AT A GLANCE

1. Basic Data		Project Number: 51118-001	
Project Name	Strengthening Asia's Financial Safety Nets and Resolution Mechanisms	Department /Division	ERCD/ERCI
Country	REG (KAZ, KOR, MAL, PRC, THA, VIE)	Executing Agency	Asian Development Bank
2. Sector	Subsector(s)	Financing (\$ million)	
✓ Finance	Banking systems and nonbank financial institutions		0.15
	Finance sector development		0.10
		Total	0.25
3. Strategic Agenda	Subcomponents	Climate Change Information	
Inclusive economic growth (IEG)	Pillar 1: Economic opportunities, including jobs, created and expanded	Climate Change impact on the Project	Low
Regional integration (RCI)	Pillar 3: Money and finance		
4. Drivers of Change	Components	Gender Equity and Mainstreaming	
Knowledge solutions (KNS)	Knowledge sharing activities	No gender elements (NGE)	✓
Partnerships (PAR)	Implementation		
Private sector development (PSD)	Private Sector Promotion of private sector investment		
5. Poverty and SDG Targeting		Location Impact	
Geographic Targeting	No	Regional	High
Household Targeting	No		
SDG Targeting	Yes		
SDG Goals	SDG8, SDG9		
6. TA Category:	B		
7. Safeguard Categorization	Not Applicable		
8. Financing			
Modality and Sources		Amount (\$ million)	
ADB		0.25	
Knowledge and Support technical assistance: Technical Assistance Special Fund		0.25	
Cofinancing		0.25	
People's Republic of China Poverty Reduction and Regional Cooperation Fund		0.125	
Republic of Korea e-Asia and Knowledge Partnership Fund		0.125	
Counterpart		0.00	
None		0.00	
Total		0.50	
9. Effective Development Cooperation			
Use of country procurement systems		No	
Use of country public financial management systems		No	

I. INTRODUCTION

1. The knowledge and support technical assistance (TA) will address the issue of nonperforming loans (NPLs) in Asia and the Pacific region by supporting the development of a national strategy and a market for NPLs or distressed assets through research and capacity building. This will be coupled with knowledge sharing through Annual Summit Meetings and Conferences of the International Public Asset Management Company Forum (IPAF), as well as training workshops to build the capacity of public asset management companies (AMCs), deposit insurance institutions, and other invited regional participants to manage distressed assets.

2. Under the TA on the Establishment of the International Public Asset Management Company Forum,¹ the IPAF strengthened the existing knowledge base on the assessment of country-level NPLs and shared resolution experiences unique to each country's development context and economic situation.² The TA team completed four research papers providing policy tools and options by building on empirical analyses of NPL resolution, including individual country experiences in Asia as well as cross-regional experiences. The IPAF was established in 2013, with seven member institutions from five countries. Over time, the IPAF's membership expanded to include deposit insurance institutions. The IPAF currently has 12 member institutions.³

3. The TA supports Regional Cooperation and Integration (RCI), a key strategic agenda under Strategy 2020.⁴ This TA will also contribute to the third strategic pillar of the RCI Strategy, 2006⁵—the development, deepening, and harmonization of regional financial markets—by supporting regional forums and regional macroeconomic and financial stability through research and information dissemination, capacity building, and institutional strengthening and partnership. The TA project's purpose is also aligned with the Financial Sector Operational Plan, 2011⁶ and the plan's mid-term review, 2017⁷ by supporting banks and nonbank financial institutions, and investing in NPL resolution and AMCs. It is also aligned with the RCI Operational Plan, 2016⁸ in helping developing member countries (DMCs) of the Asian Development Bank (ADB) harness increased benefits through improved cooperation and integration and by strengthening ADB's institutional capacity to encourage RCI through a larger, more innovative portfolio.⁹

¹ ADB. 2013. Technical Assistance for the Establishment of the International Public Asset Management Company Forum. Manila (TA 8370-REG).

² Under TA 8370, ADB and IPAF members jointly hosted three IPAF Summit and Conference events, four NPL training seminars, one financial workshop on Asian NPL markets, and one financial stability seminar on managing NPLs in Asia and Europe.

³ The IPAF's 12 member institutions are: the China Cinda Asset Management Company; China Great Wall Asset Management Corporation; China Huarong Asset Management Company; China Orient Asset Management Corporation and Zhejiang Province Zheshang Asset Management Company in the People's Republic of China (PRC); the Joint Stock Company "Fund of Problem Loans" in Kazakhstan; the Korea Asset Management Corporation and Korea Deposit Insurance Corporation in the Republic of Korea (ROK); Perbadanan Insurans Deposit Malaysia in Malaysia; the Sukhumvit Asset Management Company and Deposit Protection Agency in Thailand; and Viet Nam's Debt and Asset Trading Corporation. Eight of these are AMCs, three are deposit insurance institutions, and one is a joint-stock company.

⁴ ADB. 2008. *Strategy 2020: The Long-Term Strategic Framework of the Asian*. Manila.

⁵ ADB. 2006. *Regional Cooperation and Integration Strategy*. Manila.

⁶ ADB. 2011. *Financial Sector Operation Plan*. Manila.

⁷ ADB. 2017. *Review of 2011 Financial Sector Operation Plan*. Manila.

⁸ ADB. 2016. *Operational Plan for Regional Cooperation and Integration, 2016–2020*. Manila.

⁹ The TA first appeared in the business opportunities section of ADB's website on 6 April 2017.

II. ISSUES

4. A sound financial system is crucial to support economic growth and poverty reduction. Therefore, DMCs must safeguard the soundness of their financial systems to ensure that financial markets and systems function well as intermediaries while maintaining financial stability. NPLs threaten financial stability and are often linked to financial crises, as they affect both lenders (by reducing capital resources for lending and increasing the probability of bank failure) and borrowers (by increasing the probability of bankruptcy due to debt default). Financial crises, which are costly and detrimental to growth and poverty reduction, tend to raise NPL volumes, and persistently high NPLs in turn hinder crisis recovery.

5. NPL management remains the focus of discussions on safeguarding financial stability and preventing financial crises effectively and pre-emptively. It is also necessary to consider potential spillover effects. The literature on contagion stresses that financial shocks can spread rapidly through financial linkages and different channels. For example, a shock to one country's financial sector (such as a sharp increase in NPLs or a deposit run) can cause banks in the country to reduce lending to banks in other economies as well. Policy responses to the 1997 Asian Financial Crisis and recent European debt crisis reveal that AMCAs in Asia and Europe play a critical role in facilitating bank restructuring and asset recovery and therefore represent an important layer of national financial safety nets.

6. While NPLs accounted for less than 3% of total gross loans in most economies in Asia and the Pacific region in 2016, this ratio was greater than 5% in Afghanistan, Bhutan, the Maldives, and Pakistan; and it was 10% in Tajikistan.¹⁰ Due to data reporting limitations in some countries, these figures may underestimate the true level of NPLs. For example, in December 2016, Mongolia's NPL ratio was 8.5%, but this figure is expected to increase, because banks have been allowed to reschedule past due loans and NPLs leniently due to regulatory forbearance by the Bank of Mongolia. Many economies in developing Asia have also recognized loans as normal and performing under practices that differ from international best practice. Moreover, many economies in Asia appear to lack adequate supervision, NPL data tracking, and resolution mechanisms. For example, according to World Bank data, of the 48 Asian regional members, only 28 report banking sector NPL data.

7. Steady increases in NPLs in some regional economies alarm policy makers and market players alike. In this context, during the IPAF Summit in October 2015, IPAF members issued a joint statement calling for (i) the strengthening of IPAF members' operational capacity, (ii) enhanced coordination and cooperation among IPAF members, and (iii) an improved framework for the IPAF platform. IPAF members asked ADB to continue in its role as IPAF Secretariat to build IPAF member capacity to deal with growing NPLs and to conduct a study on developing regional NPL markets. This reaffirms the IPAF's aim to enhance financial stability, financial development, and inclusive growth by addressing financial vulnerabilities, contagion, and systemic risks, as well as by specifically sharing knowledge and policy experience in dealing with distressed assets or NPLs in Asian economies.¹¹

8. In response to the growing demand for ADB assistance on these issues, this TA is proposed to address the issue of NPLs and distressed assets in Asia, support the design of national NPL strategies and resolution mechanisms, and facilitate the development of NPL or

¹⁰ World Bank. World Development Indicators. <http://data.worldbank.org/data-catalog/world-development-indicators>. (accessed 16 March 2017).

¹¹ IPAF members officially conveyed this message to the ADB Vice President for Knowledge Management and Sustainable Development, Bambang Susantono, through a letter dated 15 December 2016.

distressed asset markets. Developing such markets is a challenge that requires policy efforts to build necessary financial market infrastructure, address legal and institutional weaknesses, and review and revise supervisory guidelines and regulatory standards to facilitate NPL write-offs. Each economy faces different conditions that must be considered in developing a distressed asset market—including legal, regulatory, and institutional frameworks; financial market and infrastructure development; and fiscal situation. Hence, each development experience offers valuable lessons applicable to the region.

III. THE TECHNICAL ASSISTANCE

A. Impact and Outcome

9. The TA is aligned with the following impact: regional financial stability and resilience in Asia strengthened through the design of NPL resolution mechanisms and development of NPL or distressed asset markets (as defined by the TA).¹² The TA will have the following outcome: strategies identified and developed for national NPL resolution mechanisms and the development of NPL or distressed asset markets in emerging Asia.¹³

B. Outputs, Methods, and Activities

10. **Output 1: Knowledge shared through annual summit meetings and conferences.**

The IPAF conducts annual summit meetings and conferences among its members, joined by public and private sector experts and policy makers to share knowledge and experiences in NPL resolution and debt restructuring. IPAF members also meet frequently to discuss strategies for NPL resolution and the development of NPL or distressed asset markets as well as concrete action plans. In addition to resolution mechanisms, the members may also identify financial infrastructure conditions that could lead to a surge in NPLs, either to preempt such a situation or to provide solutions when NPLs become a concern. These meetings benefit DMCs by promoting awareness and the adoption of a national strategy and potential mechanisms for NPL resolution appropriate to each country's economic and financial environments. ADB and the IPAF chair will jointly organize and host the annual IPAF summits, at which participants will discuss strategic directions for the IPAF in the succeeding years, and progress will be monitored and evaluated based on the IPAF charter and on this TA's Design and Monitoring Framework.

11. **Output 2: Research undertaken.** This TA will produce major research papers and case studies on successes and failures in dealing with distressed assets in the region, and explore ways to strengthen Asia's financial safety nets, including the buttressing of potential roles for AMC's and deposit insurance schemes, thereby addressing the issues raised above (para 6). Key research activities will include the following:

- (i) a study on developing NPL markets, including their prerequisites, strategies, and possible modalities;
- (ii) a study on national and regional approaches or policy recommendations for dealing with distressed assets, focused on developing strategies to develop NPL or distressed asset market; and
- (iii) a study on the legal and regulatory aspects of NPLs, possibly including an analysis of the debt and distressed assets of state-owned enterprises, and Asia's experience in

¹² One measurable performance indicator for this impact would be reduced NPL ratios which indicate a healthier banking sector in the region.

¹³ The design and monitoring framework is in Appendix 1.

dealing with NPLs, including financial supervision and market development compared to other regional approaches.

The research findings will be presented in conferences and seminars, in collaboration with the Finance Sector Group to reach as many finance sector professionals in ADB as possible. These findings will inform country partnership strategies and country operations business plans for DMCs, as well as operations departments' engagements with the public sector and private sector institutions dealing with financial stability. The findings will be published and disseminated through knowledge sharing events.

12. **Output 3: Training workshops conducted.** One training program will be conducted each year during 2018–2020 to build the capacity of financial authorities, public AMCs, deposit insurance institutions, and other invited participants to manage distressed assets. It is critical for AMCs with advanced skills in distressed asset management and financial strength to share their knowledge and experiences with new AMCs in the region. This will help AMCs expand operations outside their home bases, creating win-win value and promoting regional skills transfer.

13. **Output 4: International Public Asset Management Company Forum promotion and expansion effected through website management.** The IPAF will continue to provide members with online access to relevant data and information, research papers, reference materials, training schedules, and networking data through continued management of the IPAF website.

C. Cost and Financing

14. The TA is estimated to cost \$500,000, of which \$250,000 will be financed on a grant basis by ADB's Technical Assistance Special Fund (TASF-6), \$125,000 will be financed on a grant basis by the People's Republic of China Poverty Reduction and Regional Cooperation Fund and administered by ADB, and \$125,000 will be financed on a grant basis by the Republic of Korea (ROK) e-Asia and Knowledge Partnership Fund and administered by ADB.¹⁴ Key expenditure items are listed in Appendix 2.

15. Civil works, the procurement of large-scale equipment, permanent staffing costs, and the hiring of staff consultants are ineligible expenditures under the PRC Poverty Reduction and Regional Cooperation Fund and the ROK e-Asia and Knowledge Partnership Fund.

16. Partner agencies could provide meeting or workshop venues free of charge and assign staff support.

D. Implementation Arrangements

17. ADB will administer the TA. The Economic Research and Regional Cooperation Department will select, supervise, and evaluate consultants and resource persons; procure goods; organize workshops and summits with partner agencies; and provide staff and/or coordinate ADB staff for supporting services and participation in the workshops.

¹⁴ The PRC Ministry of Finance approved the financing of this TA under the PRC Poverty Reduction and Regional Cooperation Fund 2017 on 12 December 2017. On the other hand, the ROK's Ministry of Strategy and Finance approved the financing of this TA under the e-Asia and Knowledge Partnership Fund on 1 June 2017.

Implementation Arrangements

Aspects	Arrangements		
Indicative implementation period	January 2018–December 2020		
Executing agency	ADB		
Implementing agencies	Economic Research and Regional Cooperation Department		
Consultants	To be selected and engaged by ADB		
	Individual (International)	12.0 person-months	\$145,200
	Individual (National)	44.0 person-months	\$145,200
	Individual (Resource Persons)	1.6 person-months	\$36,000
Procurement ^a	To be procured by ADB		
	Shopping	1 contract	\$5,000
Disbursement	The TA resources will be disbursed following ADB's <i>Technical Assistance Disbursement Handbook</i> (2010, as amended from time to time). Disbursement arrangement will be pro-rata.		

ADB = Asian Development Bank.

^a Procurement Plan (accessible from the list of linked documents in Appendix 3).

Source: ADB.

18. **Consulting services.** Two types of international experts will be hired individually for a total of 12 person-months; an asset resolution research advisor will guide the IPAF's research program for 2 person-months, and the remaining person-months will be allocated to five finance sector experts. Two national consultants will also be recruited on an individual basis for 22 person-months each to support data and research work as well as coordination and implementation of the work program. Resource persons will be engaged for a total of about 1.6 person-months during IPAF training or seminars to deliver lectures on topics concerning public AMCs or to prepare and/or present background papers during the IPAF conferences. Hiring consultants on an individual basis or as resource persons will be more appropriate than engaging a firm, as this will allow greater flexibility and a better fit with the specific technical requirements that will emerge as the TA progresses. ADB will engage the consultants and resource persons in accordance with the Guidelines on the Use of Consultants (2013, as amended from time to time).¹⁵

19. **Website.** After the TA completion date, the IPAF website will be maintained by the emerging IPAF Secretariat to be nominated by IPAF members before the completion of this TA.

20. **Cofinancier requirements.** The PRC Poverty Reduction and Regional Cooperation Fund and the ROK e-Asia and Knowledge Partnership Fund require annual monitoring and progress reports.

IV. THE PRESIDENT'S DECISION

21. The President, acting under the authority delegated by the Board, has approved (i) the Asian Development Bank (ADB) administering a portion of technical assistance not exceeding the equivalent of \$125,000 to be financed on a grant basis by the People's Republic of China Poverty Reduction and Regional Cooperation Fund, (ii) ADB administering a portion of technical assistance not exceeding the equivalent of \$125,000 to be financed on a grant basis by the Republic of Korea e-Asia and Knowledge Partnership Fund, and (iii) ADB providing the balance not exceeding the equivalent of \$250,000 on a grant basis for Strengthening Asia's Financial Safety Nets and Resolution Mechanisms, and hereby reports this action to the Board.

¹⁵ Terms of Reference for Consultants (accessible from the list of linked documents in Appendix 3). Lump-sum payments or output-based contracts for consulting services will be considered in line with Mid-term Review Action Plan Nos. 2.9.2 and 2.10.2.

DESIGN AND MONITORING FRAMEWORK

Impact(s) the TA is Aligned with			
Regional financial stability and resilience strengthened in Asia through the design of NPL resolution mechanisms and development of NPL/distressed asset markets (defined by the TA).			
Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting	Risks
Outcome Strategies identified and developed for national NPL resolution mechanisms and the development of NPL or distressed asset markets in emerging Asia	a. Strategies identified and discussed through conferences and seminars at the national and regional levels b. Cooperation on improving national NPL resolution mechanisms initiated	a. Progress report, plus assessment and feedback from IPAF members b. Dialogue among IPAF members on how to strengthen their NPL resolution mechanisms through the exchange of information and experiences	A lengthy process and political interventions could hinder the discussion and development of strategies to establish a well-developed market for the sale of distressed assets
Outputs 1. Knowledge shared through the annual Summit Meeting and Conference 2. Research undertaken 3. Training workshops conducted 4. IPAF promotion and expansion effected through website management	1. At least three IPAF summits supported and conferences organized and conducted (2016 baseline: one) 2. Three to five research and/or knowledge products produced (2016 baseline: four research papers) 3. At least one training activity for public AMCs and institutions organized and conducted per year for 3 years (2016 baseline: one) 4a. A 10% annual increase in the number of unique visitors to the website 4b. A 50%– 100% increase in the number of IPAF members by the end of 3 years (2016 baseline: 12 members)	1. Back-to-office reports 2. Research papers submitted 3. Feedback from participants through training evaluation forms 4a. Feedback from IPAF members and website statistics 4b. Official list of members	Weakening commitment of current and potential member AMCs and deposit insurance institutions to the IPAF's vision and objectives embodied in its charter Unavailability of top-tier consultants and resource persons for engagement Data limitations Possibly high staff turn-over in AMCs Information technology errors Data limitations

<p>Key Activities with Milestones</p> <p>1. Knowledge shared through the annual summit meetings and conferences</p> <p>1.1 Engagement of consultants to be part of the IPAF secretariat (Q1 2018)</p> <p>1.2 Preparatory activities for IPAF conferences (Q1 2018, Q1 2019, Q1 2020)</p> <p>1.3 Conduct of the IPAF conferences (Q2–Q3 2018, Q2–Q3 2019, Q2–Q3 2020)</p> <p>2. Research undertaken</p> <p>2.1 Engagement of consultants (Q1–Q2 2018, Q1–Q2 2019)</p> <p>2.2 Development and publication of research papers (Q3 2018–Q1 2019, Q3 2019–Q1 2020)</p> <p>3. Training workshops conducted</p> <p>3.1 Preparatory activities for training, workshops, and seminars (Q2–Q3 2018, Q2–Q3 2019, Q2 2020)</p> <p>3.2 Conduct of training, workshops, and seminars (Q3–Q4 2018, Q3–Q4 2019, Q3 2020)</p> <p>4. IPAF promotion and expansion effected through website management</p> <p>4.1 Periodic updating and monitoring of the IPAF website (every quarter from January 2018 to December 2020)</p>
<p>Inputs</p> <p>ADB: \$250,000</p> <p>People’s Republic of China Poverty Reduction and Regional Cooperation Fund: \$125,000</p> <p>Republic of Korea e-Asia and Knowledge Partnership Fund: \$125,000</p>
<p>Assumptions for Partner Financing</p> <p>Not applicable</p>

ADB = Asian Development Bank, AMC = asset management company, IPAF = International Public AMC Forum, NPL = nonperforming loan, Q = quarter, TA = technical assistance.
Source: ADB.

COST ESTIMATES AND FINANCING PLAN
(\$'000)

Item	Amount		
	ADB ^a	PRC Poverty Reduction and Regional Cooperation Fund ^{b, c}	ROK e-Asia and Knowledge Partnership Fund ^{b, d}
A. Consultants			
1. Remuneration and per diem			
a. International consultants	48.4	48.4	48.4
b. National consultants	48.4	48.4	48.4
2. Out-of-pocket expenditures			
a. International and local travel	20.0	20.0	20.0
b. Reports and communications	5.0	0.0	0.0
c. Miscellaneous administration and support costs	5.0	0.0	0.0
B. Printed external publications	5.0	0.0	0.0
C. Surveys and/or studies	20.0	0.0	0.0
D. Goods ^e	5.0		
E. Training, seminars, workshops, forums, and conferences			
1. Facilitators	12.0	0.0	0.0
2. Travel costs of ADB staff acting as resource persons	12.0	0.0	0.0
3. Venue rental and related facilities	30.0	0.0	0.0
4. Participants and resource persons	19.6	8.2	8.2
5. Representation	1.0	0.0	0.0
F. Contingencies	18.6	0.0	0.0
Total	250.0	125.0	125.0

ADB = Asian Development Bank, PRC = People's Republic of China, ROK = Republic of Korea.

Note: The technical assistance (TA) is estimated to cost \$500,000, of which contributions from the ADB, the PRC Poverty Reduction and Regional Cooperation Fund, and the ROK e-Asia and Knowledge Partnership Fund are presented in the table above.

^a Financed by ADB's Technical Assistance Special Fund (TASF-6).

^b Administered by ADB.

^c The PRC's Ministry of Finance approved the financing of this TA under the People's Republic of China Poverty Reduction and Regional Cooperation Fund 2017 on 12 December 2017.

^d The ROK's Ministry of Strategy and Finance approved the financing of this TA under the e-Asia and Knowledge Partnership Fund on 1 June 2017.

^e Includes information and communication technology-related equipment and/or supplies and econometric or statistical programs and/or software. ADB will procure the equipment following its Procurement Guidelines (2015, as amended from time to time). Turnover and/or disposal arrangements for the equipment will follow the provisions stated in the Project Administration Instructions on Administering Grant-Financed Technical Assistance Projects (PAI 5.09, para. 68).

Source: ADB estimates.

LIST OF LINKED DOCUMENTS

<http://www.adb.org/Documents/LinkedDocs/?id=51118-001-TARreport>

1. Terms of Reference for Consultants
2. Procurement Plan