

## LOCAL CURRENCY FUNDING FOR ADB'S LOAN

1. ADB will borrow local currency (Tenge) from the National Bank of Kazakhstan (NBK) for onlending to Damu (the Borrower), who will relend the funds to participating financial institutions (PFIs). ADB will enter into a TBMA/ISMA Global Master Repurchase Agreement (GMRA) with NBK.<sup>1</sup> Based on this agreement, ADB will contract a number of individual repurchase agreements ('repos') triggered by disbursement requests from Damu (in turn, based on PFIs estimated disbursements to MSMEs). Repo operations conform to Treasury Investment and Risk Management Guidelines and their use in operations are part of the ADB's annual borrowing program as approved by ADB's Board of Directors.<sup>2</sup>
2. Through each repo transaction ADB borrows tenge from the NBK against collateral provided by ADB in the form of USD denominated government securities with a minimum 'AA' rating.<sup>3</sup> NBK lends tenge to ADB and ADB concurrently transfers an equivalent value of securities to NBK's name. The value of USD collateral equivalent to the tenge borrowed will be determined based on the USD/Tenge exchange rate of the day of execution of the repo. At the end of the repo loan term ADB repurchases back the securities. Thus, the ownership of the securities used as collateral is temporarily transferred to NBK.
3. The cost of the tenge received from NBK is half of NBK's policy base rate with a floor of 7% per annum, and will be repriced quarterly to NBK's then prevailing policy base rate. The repos will have one year maturity, which will be rolled over until the end of the term of the overall framework facility, which is three years starting from the execution of the first repo transaction.
4. The transaction uses a third party (Euroclear)<sup>4</sup> that acts as an intermediary between ADB and NBK, and is responsible for administering the transaction, safekeeping the assets, valuating collateral and settling movements of collateral if required.
5. Through the collateral, the credit risk of NBK is mitigated. There is a residual risk related to the change in the market value of the collateral or the exchange rate fluctuation between the repo issuance and the quarterly repricing date. The quarterly revaluation and movement of collateral, called "margining", mitigates this residual risk. In the event that the collateral provided to NBK exceeds the value of the previous valuation due to depreciation of the Tenge, NBK would provide a partial return of collateral to ADB and in the opposite event ADB would provide additional collateral to NBK.

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<sup>1</sup> Published in 2000, this form of repurchase agreement is the current market standard for repos outside of the U.S. ADB and the NBK have reached an in principle agreement on the terms of this facility.

<sup>2</sup> As part of ADB's Borrowing Program for 2016, the Board authorized ADB to source local currency to fund loans through swap transactions and transactions of a similar nature. The GMRA with NBK has been designed to substantially replicate a swap, and therefore is considered in accordance with the Board's authorization.

<sup>3</sup> They could also be denominated in EUR, CHF, BGP or JPY, as agreed between NBK and ADB.

<sup>4</sup> Euroclear, based in Belgium, is the largest international central securities depository.

**Chart 1**

