

# MUNICIPAL BORROWING

**Roland White**

GLOBAL LEAD: CITY MANAGEMENT AND FINANCE  
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# PRESENTATION STRUCTURE



MUNICIPAL  
BORROWING

DEBT INSTRUMENTS  
AND IMPACTS



MUNICIPAL  
BORROWING

THE BIG PICTURE

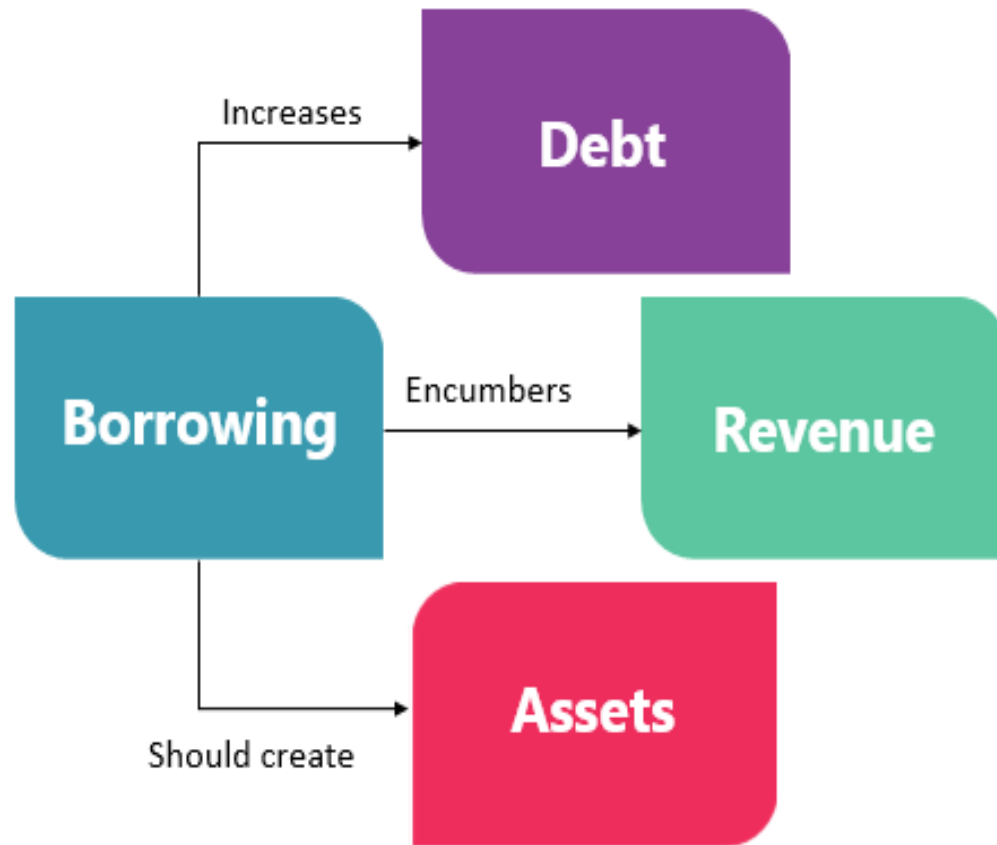


# MUNICIPAL BORROWING

Debt Instruments & Impacts



# Impacts of Municipal Debt



**Effects of borrowing depend on the type and how it is done**

- Borrowing will degrade the financial position of a LG if it used to avoid a hard budget constraint
- The "Golden Rule"



# Characteristics of Municipal Debt

## **Different types of debt have specific issues and risks**

- ✓ Short and long-term borrowing
- ✓ Local and foreign currency denominated borrowing



# Terminology and issues

## LOANS

1. Borrower
2. Lender
3. Maturities must match
4. Small-scale borrowers don't have a choice

## BONDS

1. Issuer
2. Bondholder
3. Liquid secondary market brings in more investors
4. For large scale borrowers



# Specific Types of Bond

## **“General obligation” bonds**

### **Revenue bonds**

- TIF bonds

### **Green bonds**

### **Retail bonds**



# Credit enhancements

Guarantees, insurance

Intercepts

Reserve funds

Sinking funds

Covenants





# Debt service

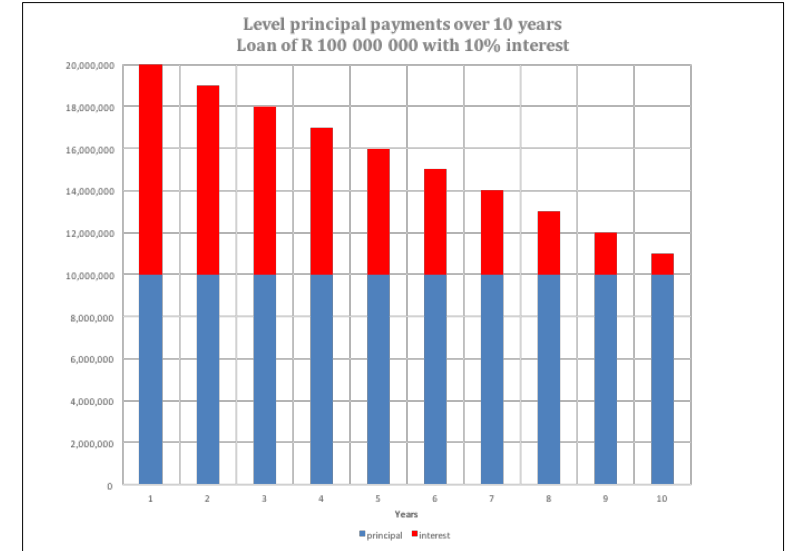
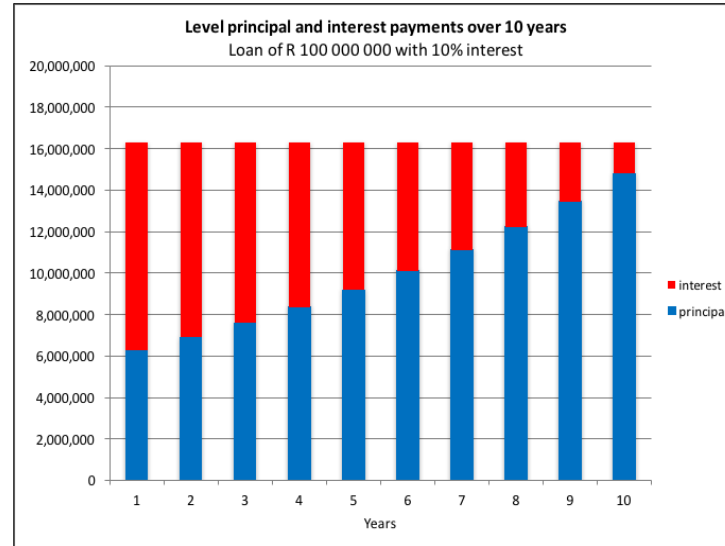
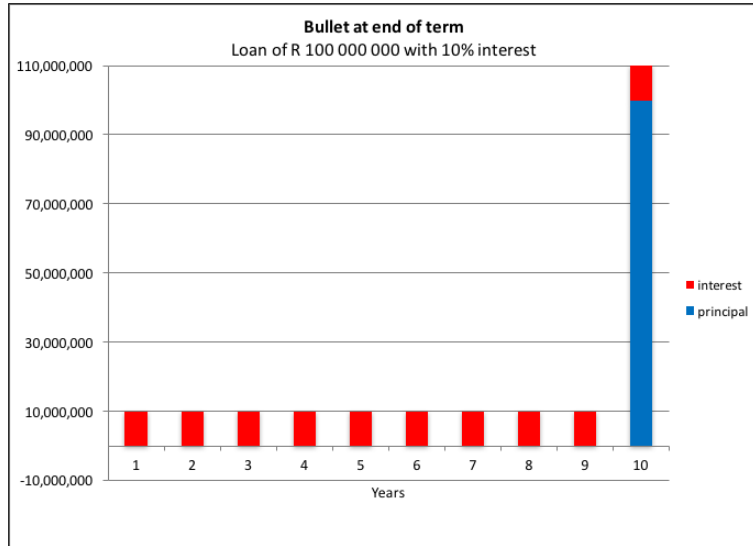
## **Size matters**

- How much total?
- How much each period?

## **Shape matters**



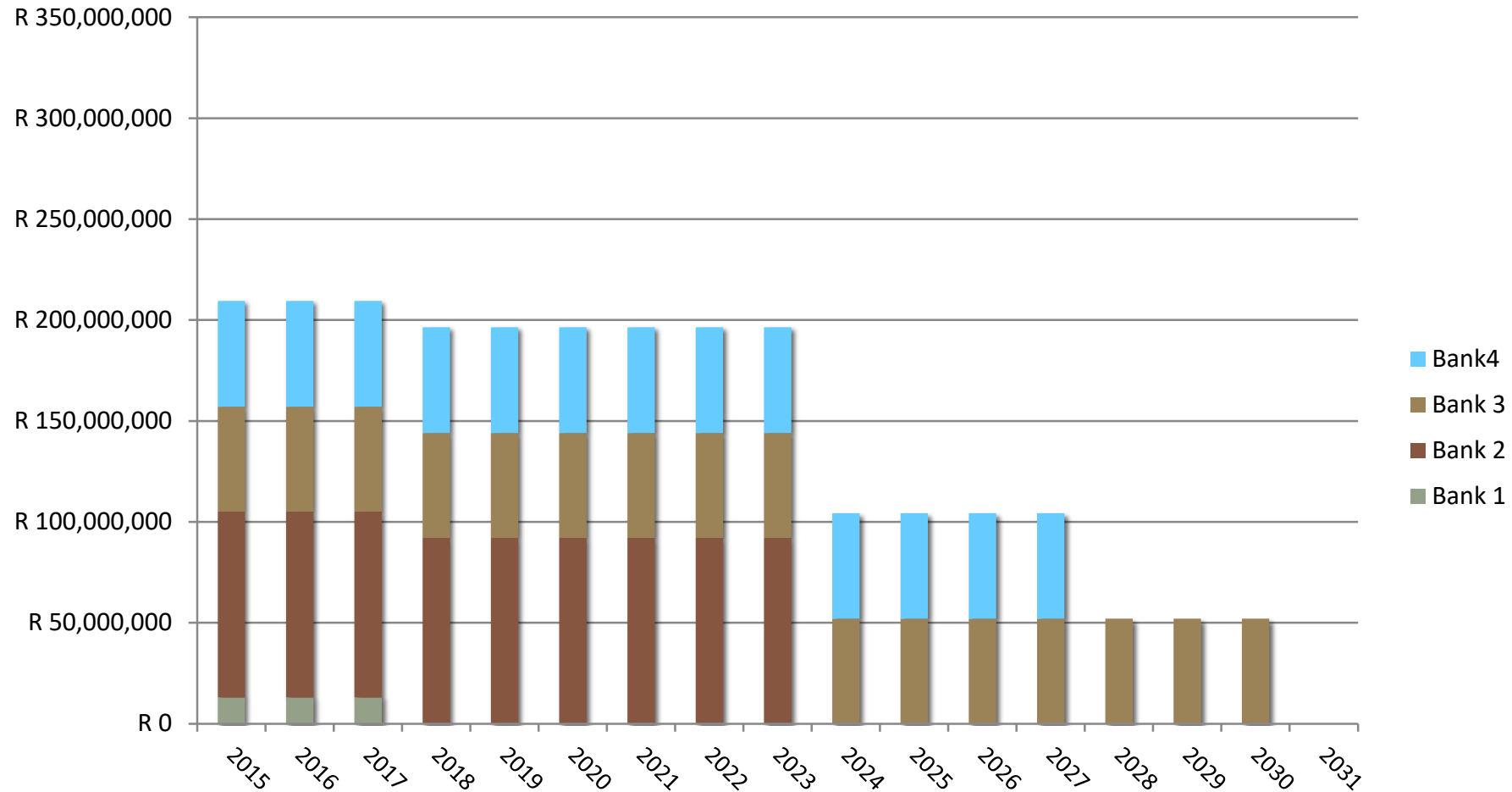
# Different payment structures





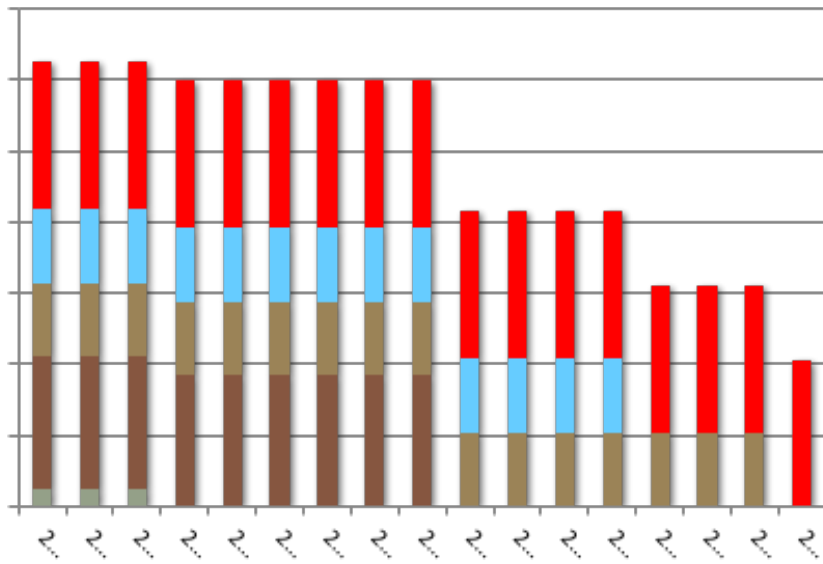
# More on structure – an example

Stacked obligations at level amortization

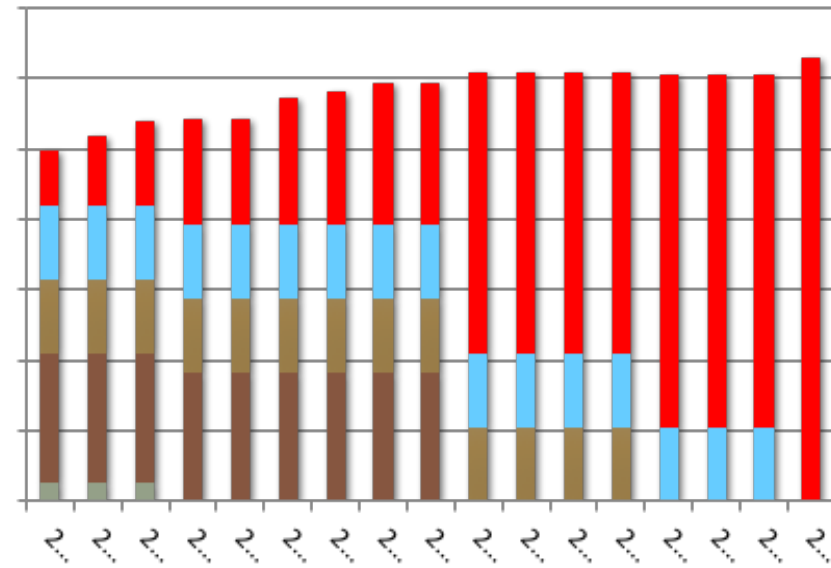




# Which do you prefer, why?



New loan level



New loan custom



# Borrowing Wisely

Knowledge is power

Lenders have knowledge advantage

Municipalities need to be smart



# **MUNICIPAL BORROWING**

The Big Picture



# Municipal Debt Market Ecosystem

## INVESTORS

Bond purchasers  
(pension funds,  
institutional  
investors)

Private/  
Commerical  
Banks

Intermediaries:  
Govt. Dev.  
Banks/MDFs; Bond  
Banks etc.

Int'l Development  
Banks/Donors  
(e.g., IFC, AFD)

## MARKET FACILITATORS

Credit Rating  
Agencies (e.g.,  
Moody's, S&P)

Financial & Other  
Advisors

Project Preparation  
Facilities (e.g., C40  
Cities Finance Facility)

## BORROWERS

MUNICIPALITY

URBAN UTILITY  
(E.G. WATER  
UTILITY)

## RISK BEARERS/ MITIGATORS

Monoline  
insurers

Credit Enhancement  
Facilities (e.g.  
LGUCC, Philippines),  
USAID



# Municipal Debt: An International Perspective

- **Very divergent systems across developed and developing markets:**
  - ✓ US \$3trn vs India \$100m/annum
- **In the developing world, activity tends to be highly constrained**
  - ✓ **Africa:** significant only in South Africa
  - ✓ **South Asia:** limited largely to India, which has a modest market
  - ✓ **East Asia:** mixed and limited experience, e.g., Philippines; Indonesia; China is unique
  - ✓ **LAC and ECA:** some experience (e.g., Colombia, Hungary)





# Why Is This?

## Four factors determine access by cities to debt finance

1. Financial sector and investment community
2. City or project revenue sources – the intergovernmental fiscal system
3. The quality of financial data and FM systems of the city
4. The legal and regulatory framework



**SUPPLY**



**COMBINE TO  
PROVIDE DEMAND  
("CREDITWORTHINESS")**



**INTERMEDIATES SUPPLY  
AND DEMAND**



# Why Is This?

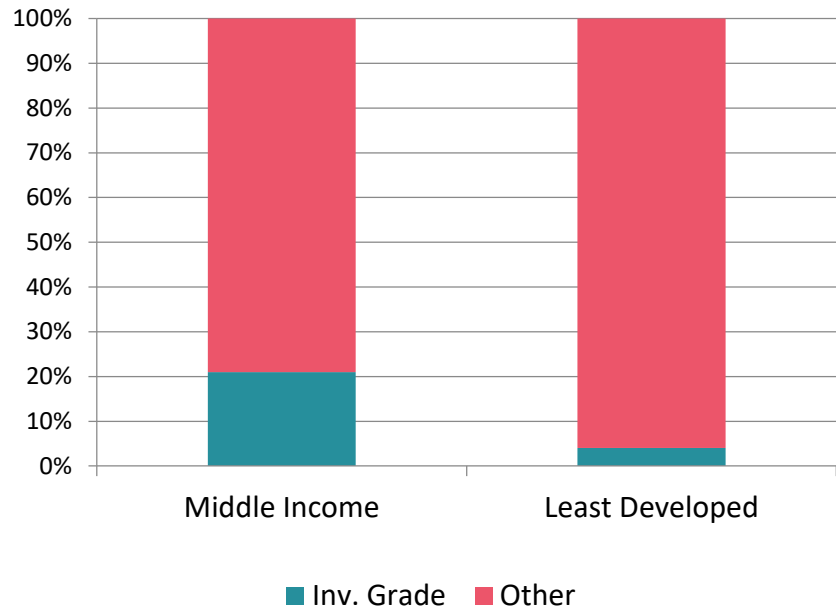
- **In developing countries barriers to all these areas tend to be severe**
  - ✓ Analysis (e.g. India; Vietnam) and experience (e.g. South Africa) shows that the **binding constraints tend to be on the demand and regulatory sides**
  - ✓ **National governments control most of the policy decisions** and levers in these areas, even on issues such as FM (municipal accounting standards; the municipal audit process)
  - ✓ **Cities control many of the demand-side factors**, particularly the quality of FM and data
  - ✓ The reform necessary to expand cities' access to credit markets and PPP and LVC investors often raises **fundamental policy and political issues**, e.g. the degree of autonomy of local governments; management of potential fiscal risks



# The Demand Side: Creditworthiness

Of the 500 largest cities in developing countries, only 95 (19%) are currently rated as investment grade by an international or local rating agency

**Percentage of top 500 cities with Inv. Grade Ratings, by Country Income Category**



Only 32 cities - out of the largest 500 - have issued a bond at the municipal level; these cities are in 12 countries (Argentina, Bolivia, China, Colombia, India, Mexico, Paraguay, Peru, Russia, South Africa, Uruguay, Vietnam)

**Breakdown by Region**

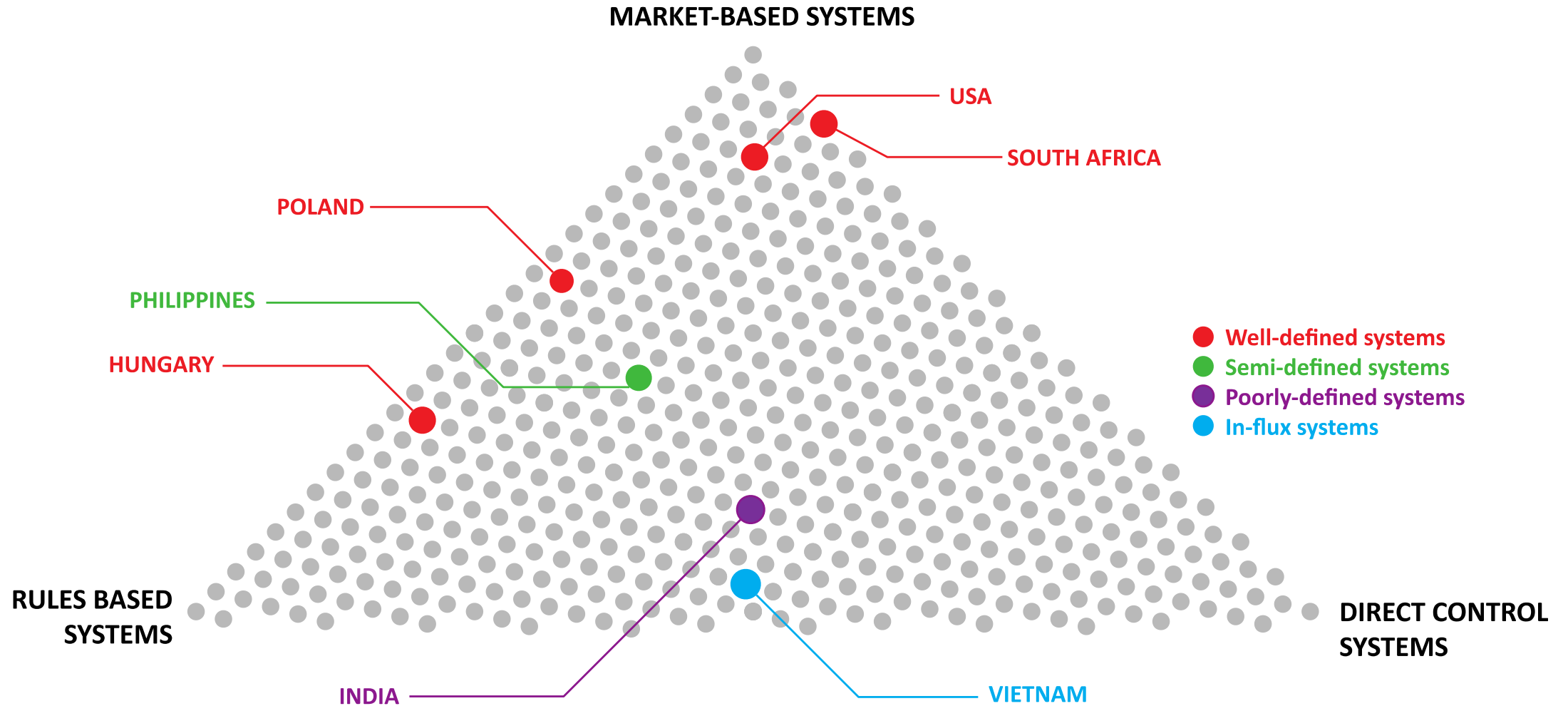
	EAP	ECA	LAC	MNA	SAR	SSA
<b>Cities in top 500</b>	178	44	92	43	82	61
<b>Inv. Grade Rated Cities</b>	12	9	34	0	35	8
<b>Countries in region with rated cities</b>	China*	Armenia	Argentina		India	Côte d'Ivoire
	Indonesia	Belarus	Bolivia			Senegal
	Thailand	Kazakhstan	Brazil			South Africa
	Vietnam**	Russia	Colombia			Uganda
		Serbia	Mexico			
		Ukraine	Paraguay			
			Peru			
			Uruguay			

\* Does not include Local Government Financing Vehicles

\*\* 3 Cities in Vietnam have issued bonds, but ratings are not publicized



# The Regulatory Environment: International Examples

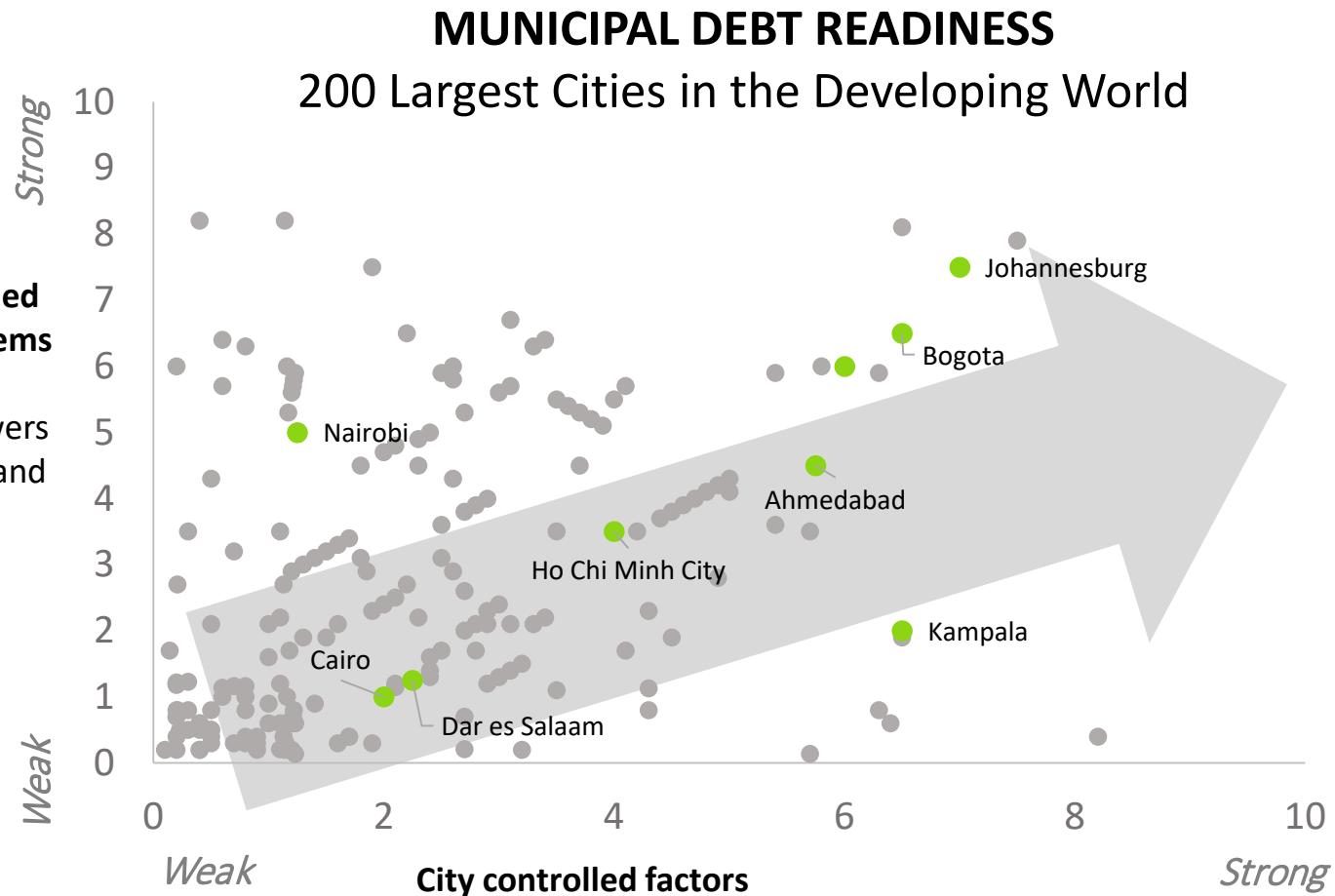




# Addressing the Challenge

## Nationally controlled regulations & systems

- City revenue sources and powers
- City accounting and financial management
- Borrowing regulations



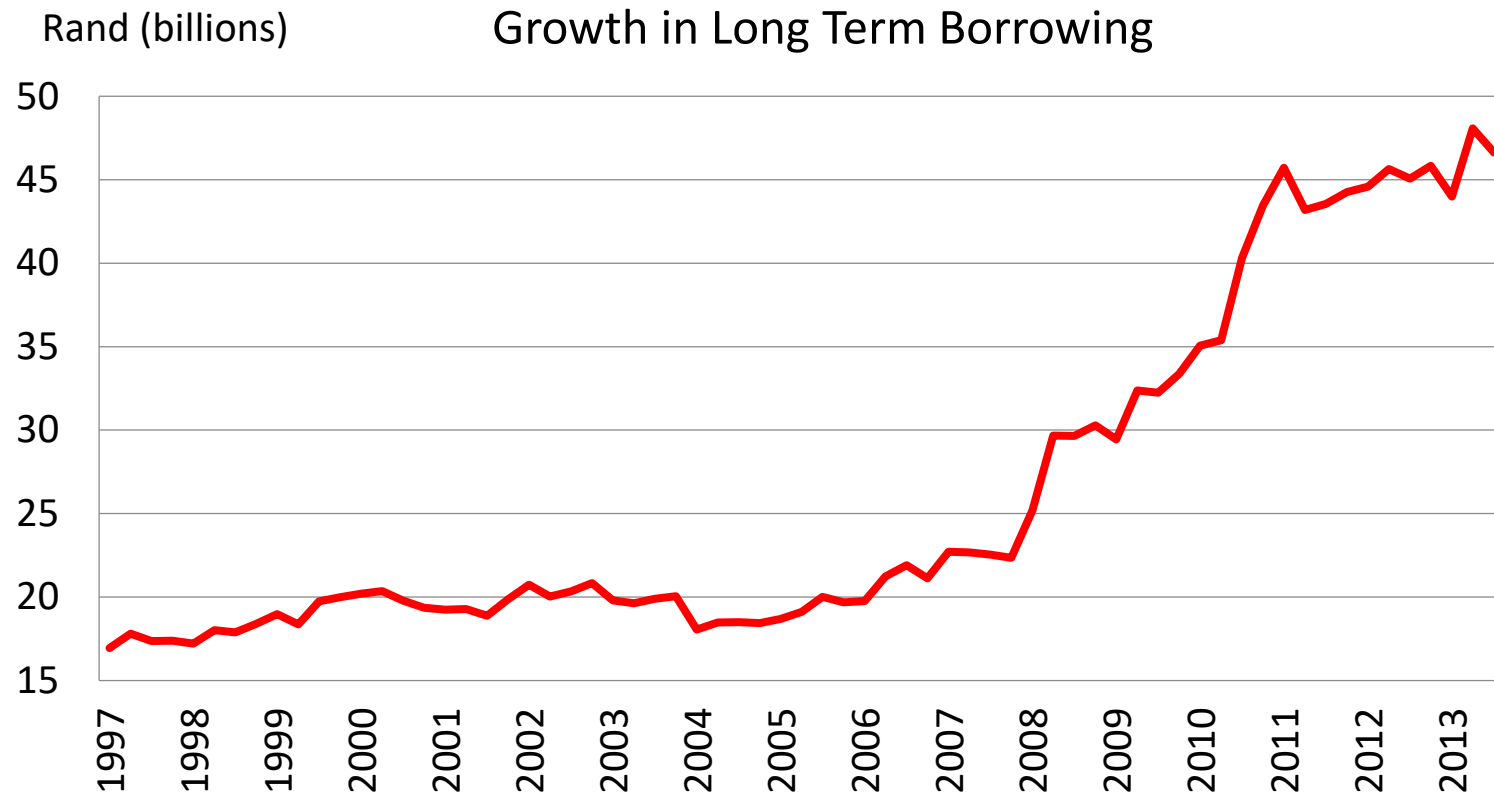
## City controlled factors

- Quality of financial data and reports
- Financial management
- Project bankability



# Addressing the Challenge

## South Africa Municipal Borrowing





# Addressing the Challenge

- **City governments**

- ✓ Maximize revenues, strengthen financial management and improve data to enhance creditworthiness
- ✓ Strengthen project quality
- ✓ Equip themselves to deal with sophisticated lenders
- ✓ Lobby national governments for regulatory reform

- **National governments**

- ✓ Strengthen municipal fiscal systems (e.g. revenue autonomy)
- ✓ Improve regulatory systems for municipal borrowing
- ✓ Support non-distorting interventions to stimulate the market (e.g. advisory services; credit-enhancement facilities)

- **MDBs and Donors (public and private)**

- ✓ Support city and national governments with TA to achieve the above
- ✓ Support targeted credit-enhancement interventions to de-risk transactions in an imperfect environment
- ✓ Facilitate relationships between investors and city borrowers

- **Investors**

- ✓ Pioneer the business drawing from experience in developed markets