INTERNATIONAL FINANCING REVIEW ASIA ROUNDTABLE

DECEMBER 2017
www.ifrasia.com

Sponsored by

IMF/WORLD BANK 2017

Internationalising Asia's Capital Markets

OUR NETWORK CONNECTS YOU TO THE WORLD. IMAGINE THE POSSIBILITIES.

With an extensive global network, opportunity awaits wherever you're looking to take your business.

At HSBC, we have experienced teams on the ground in over 70 countries, where 90% of the world's trade and capital flows originate. This means we have both the expertise and connections to help your business grow in today's most important markets.

Visit GBM.HSBC.com and see how our innovative solutions are ready to help your business.

HSBC

HSBC Bank USA, N.A. is a member of the HSBC Group of affiliates ("HSBC"). Certain products and services may not be offered by the local HSBC affiliate in every country.

HSBC Bank USA, N.A. Member FDIC. Equal Credit Opportunity Lender.

United States persons (including entities) are subject to US taxation on their worldwide income and may be subject to tax and other filing obligations with respect to their US and non-US accounts. US persons and entities should consult a tax advisor for more information. Trade and supply chain transactions may be subject to credit approval. Other restrictions, including specific country regulations may apply. Foreign currency exchange rates may apply to certain trade transactions.

Copyright 2017. ALL RIGHTS RESERVED.

FOREWORD

The IMF/World Bank annual meetings this year provided an ideal backdrop for a discussion on the internationalisation of Asia's capital markets.

With China and India – Asia's two largest emerging economies – opening their currencies and reforming their capital markets, the 2017 meetings offered a timely opportunity to discuss the region's progress, and the challenges that remain.

China this year allowed foreign investors to invest in onshore renminbi bonds without opening a bank account on the mainland, introducing a groundbreaking Bond Connect platform in early July.

That followed a direct access programme giving certain institutional investors a way into the interbank bond market in 2016 and the gradual opening of the Panda bond format, allowing overseas issuers to raise funds onshore.

But China has also restricted currency outflows and squeezed onshore bond yields higher to rein in credit growth, giving global investors pause for thought. It has also been slow to formalise Panda bond rules, and questions around the direction of the currency remain unanswered.

India allowed companies to sell rupee bonds overseas in 2015 and has been refining the rules ever since. Housing finance company HDFC made the breakthrough for the corporate sector in 2016, opening up a promising alternative investor base for Indian borrowers and giving global investors unrestricted, quota-free exposure to rupee securities. The offshore liquidity pool, however, remains limited, and the latest rule changes have added more complications for potential issuers, imposing coupon caps and minimum tenors that were originally designed to prevent weaker companies from taking on foreign exchange liabilities.

Barely a stone's throw from President Trump's White House in Washington DC, the latest IFR Roundtable also took place amid a mounting debate over the resilience of global emerging markets to rising US dollar interest rates.

Emerging markets tend to underperform when the US dollar strengthens, and Asia felt the full force of shifting global capital flows in the 2013 "taper tantrum", when the suggestion of an end to US quantitative easing rocked confidence in India and Indonesia, among others.

Asian borrowers have sold a record amount of US dollar debt in 2017, with issuance already exceeding US$250bn, excluding Japan and Australasia. As countries open their capital markets to the world, are they attracting valuable long-term capital, or are they leaving themselves more exposed to volatile capital flows?

An engaged audience at the IMF headquarters tested the panellists on this and other topics, ranging from infrastructure finance to the use of blockchain technology.

At a time when the US administration is reducing its emphasis on multilateral institutions to focus on stimulating domestic growth, the debate around recent developments in China and India takes on even greater significance.

REUTERS/Yuriko Nakao

Chair: Steve Garton **Participants:** Alexi Chan, Arnab Das, Bill Foster, Monish Mahurkar, Eddy Sternberg
Head of production: Clive George **IFR production manager:** Carole Styles
Senior production executive: Gavin White
Global advertising production manager: Gloria Balbastro +44 (0)20 7542 4348
Global Head – Advertising & Sponsorship Sales: Shahid Hamid
Advertising & Sponsorship Sales Director: Leonie Welss
Client Services: IFR.Clientsupport@tr.com
Printed by Diversified Global Graphics Group © Thomson Reuters 2017 www.ifrasia.com
UNAUTHORISED PHOTOCOPYING IS ILLEGAL

Roundtable participants

ARNAB DAS

Invesco

Arnab Das is head of emerging markets macro research at Invesco Fixed Income. He joined Invesco in 2015, and previously held senior research positions at Roubini Global Economics, Dresdner Kleinwort and JP Morgan. He has also been a private consultant in global and emerging markets, as well as consulting with Trusted Sources, a specialist EM research boutique in London. He has a degree from Princeton University and a doctorate from London School of Economics, and is based in London.

ALEXI CHAN

HSBC

Alexi Chan is the global co-head of debt capital markets at HSBC, overseeing a team of over 300 professionals around the world. He is based in Hong Kong, and previously worked in Singapore and London. Before joining HSBC in 2000, he worked as an economic adviser in HM Treasury, the UK's economics and finance ministry. He is a graduate of the University of Oxford, and completed his master's degree at the London School of Economics.

BILL FOSTER

Moody's Investors Service

Bill Foster is a senior credit officer in the Sovereign Risk Group at Moody's in New York, where he serves as lead analyst on Canada, India, Pakistan, Bangladesh, Sri Lanka and the World Bank Group.

Bill joined Moody's in August 2016, following 10 years at the US Department of the Treasury. He most recently served as senior adviser for international financial markets, where he was the Office of International Affairs' first dedicated liaison to New York's international financial community, and was earlier stationed in India.

MONISH MAHURKAR

International Finance Corp

Monish Mahurkar is the director of treasury market operations at the IFC, responsible for the institution's global debt capital markets and fixed income activities, including IFC's funding strategy and cash management. Previously director of treasury client solutions, Monish joined IFC in June 2012 and has over 25 years of international experience in banking and capital markets, spanning treasury and fixed income roles at Citibank, Merrill Lynch and the Asian Development Bank.

EDDY STERNBERG
Loomis Sayles
Eddy Sternberg is a vice president of Loomis Sayles and co-portfolio manager on emerging markets debt portfolios. Before joining Loomis Sayles in 2005, Eddy was a senior analyst and portfolio manager at Evergreen Investments. He also worked as an investment officer for the Inter-American Investment Corporation and a development program associate at BASF. He began his career as a credit analyst with Banco Ganadero Argentino in Buenos Aires, and has an engineering degree from the Universidad de Buenos Aires and an MBA from the Sloan School of Management at MIT.

STEVE GARTON
IFR

The bigger picture here is that the global monetary policy cycle among the major central banks is converging towards the Fed rather than diverging

IFR ASIA: WELCOME TO THE IFR ROUNDTABLE. WE HAVE FOR YOU A DISCUSSION ON THE INTERNATIONALISATION OF THE ASIAN CAPITAL MARKETS, AND A WIDE RANGE OF VIEWS REPRESENTED ON THE PANEL.

THE FIRST QUESTION TO KICK THINGS OFF IS WHY ARE WE HERE TO TALK ABOUT ASIA? IN MY MIND, IT'S BECAUSE OF A FEW RECENT MAJOR DEVELOPMENTS IN ASIA'S BIGGEST CAPITAL MARKETS, CHINA AND INDIA, BUT I'M GOING TO ASK ALEXI FOR YOUR VIEW ON HOW SIGNIFICANT THE ASIAN EMERGING MARKETS ARE AND WHAT INTERNATIONALISATION REALLY MEANS.

ALEXI CHAN, HSBC: Thank you, Steve, and thank you IFR for sponsoring this important event. I'm delighted to be here with this distinguished group of fellow panellists.

I think it's a very exciting time to be talking about Asia's capital markets. We're more than 20 years now since the Asian financial crisis. At that time, people were talking about Asia's over-dependence on the bank lending market and the importance of developing a capital market that could sustain the needs of corporates – in both local currency as well as other G3 currencies – and take advantage of what the capital markets can offer in terms of scale and tenor.

I'm pleased to say that we've reached a position in the last few years where Asia has become the largest capital market among the global emerging markets. In hard currency, we've now got a regional G3 bond market expected to print well north of US$250bn this year. That has provided a very significant source of financing for governments in the region, for financial institutions as well as corporates.

So, the development of an Asian dollar bond market, with a significant number of investors in the region as well as globally, I think has been a pretty unique feature of the international financial system, and one that we've strongly encouraged.

If we look on the local currency side, we've also seen good progress in Asia's local currency markets right across the region. I think the most significant development is how the RMB market is opening up. We've had a number of offshore local currency markets, including the Dim Sum market in RMB, and that has extended to other major markets like India, which has developed the Masala bond market. The offshore markets have given international investors a way to provide financing to Asian and other issuers, while taking on the foreign exchange risk themselves, and that's been an important development.

Clearly, one of the goals that we're working towards is a greater opening up of the domestic markets themselves. Onshore China represents a very major opportunity. We've brought a number of global issuers to the Chinese market in the sovereign space, including European sovereigns like Poland and Hungary, and a number of the supranational issuers have also tapped these markets and helped to develop these markets in terms of both access and the curve.

These are exciting developments in terms of both hard currency and local currency, which really makes the Asian capital markets a pretty exciting place to be right now.

IFR ASIA: THERE IS A GOOD TALKING POINT AROUND ASIA'S EXPOSURE - OR THE EMERGING MARKETS' EXPOSURE - TO WHAT HAPPENS HERE IN THE US AS WELL. ARNAB, WHEN US RATES GO UP, EMERGING MARKETS TEND TO UNDERPERFORM. WHAT'S YOUR TAKE ON WHERE ASIA FITS INTO IN THAT PICTURE?

ARNAB DAS, INVESCO: Yes, it's certainly generally been the case, that when US interest rates go up and the US yield curve rises or steepens, and in particular the dollar strengthens, then you usually have some kind of adjustment in emerging market countries and many other places around the world.

I would suggest, looking forward, the bigger picture here is that the global monetary policy cycle among the major central banks is converging towards the Fed rather than diverging. The ECB is in the process of getting ready to taper and then will probably eventually start to raise rates. The Eurozone is growing above trend. China's major central bank operates behind capital controls, but it's already been tightening. The BOJ faces an economy that's growing well above trend, although like many other places, inflation is still missing in action.

As long as there aren't any surprises, or let's say significant shifts, in fiscal policy in the US, the bigger picture is that the monetary policy differential between the Fed and the other central banks is closing, and the dollar, if anything, is expensive – not cheap.

The dollar tends to behave in multi-year cycles, so we're probably likely to see a weaker dollar rather than a stronger dollar, which should be conducive to continued interest and inflows into emerging markets. Especially in this global macro sweet spot, where growth is reasonably strong, inflation reasonably weak in most places, and financial conditions extremely easy. So, it should be very conducive for more change and more interest in Asian local markets, and other parts of emerging markets as well.

IFR ASIA: DO WE THINK, THEN, THAT OPENING UP ASIAN MARKETS PROVIDES SOME KIND OF PROTECTION FROM GLOBAL CAPITAL FLOWS, OR DOES IT LEAVE ASIAN COUNTRIES MORE EXPOSED? BILL, MAYBE I'LL THROW THAT TO YOU. I KNOW YOU'VE LOOKED AT THESE QUESTIONS IN PARTICULAR REGARD TO INDIA.

BILL FOSTER, MOODY'S: Sure. The Indian market is quite closed when you look at it on a relative basis. Foreigners hold only around 4% or so of outstanding government securities. By 2018, the expectation is it will go up about 5% or so, but foreign investors are very limited in terms of their potential exposure. The corporate bond market in India is very under-developed as well. It's only about 5% of GDP in total. There's really not a lot of opportunity for foreign investors of scale to really participate as much as they would like, I would say.

The Masala bond market in particular, which is an exciting new potential opportunity, is a very nascent market, and we've seen some kind of fits and starts

> The incentives are very much there for the authorities to continue to develop that local market

recently in terms of its development. In particular, very few issuers are eligible for that market - only the highest quality of issuers, like the HDFCs of the world and certain state-owned enterprises. More recently, the government has decided to set more limitations, basically, on who can use that window. They've shifted the restrictions towards the external commercial borrowing window, which places certain tenor and price restrictions on the issuers.

So, when you look at India in particular, it's really in the early stages. The reason that this is happening is, I think, because the domestic market itself is still in the early stages of development. The RBI and SEBI, the securities market regulator, are very much focused now on continuing domestic market development, providing more depth, more liquidity. Still, the majority of corporate issuances, for example, are really private placements. It's going to take time, and some of the analysis behind this is it's a bank-driven lending model still driving the economy. This is what's led to significant issues with regard to infrastructure projects and high NPLs in the banking system, because of the maturity mismatch.

So, the incentives are very much there for the authorities to continue to develop that local market. They'll be focused on that over the next few years, but it will take time for foreigners to be able to participate at scale because of these issues that we're dealing with.

IFR ASIA: MONISH, PERHAPS WE CAN ASK YOU FOR THE OFFICIAL SECTOR VIEW. HOW CRUCIAL IS IT TO OPEN UP AND DEVELOP CAPITAL MARKETS FROM A DEVELOPMENT PERSPECTIVE?

MONISH MAHURKAR, IFC: From IFC's perspective, we have observed over many years that there are recurring lessons from various crises. Certainly the Asian crisis was caused by excessive foreign currency imbalances between assets and liabilities. That was a lesson well-learned in Asia, and that's the time when the development of local bond markets started in all seriousness.

In our own case, while our primary lending currency is the US dollar, which offers the maximum liquidity for us to finance our clients, we have seen a growing demand from many of our clients to finance in their own currency. It is quite logical because, unless a client has export revenues in foreign currency, all others who have domestic revenue streams should be appropriately borrowing in their own currency.

The challenge, of course, is that in many markets where inflation rates are high, nominal interest rates are high as well. When you compare nominal double-digit or high single-digit rates with a very low nominal one in dollars, the temptation is to take the lower one. It's only in hindsight, or after a major currency devaluation or correction that you realise how expensive that tempting low dollar coupon actually was.

Over the years, we've been pushing the development of many domestic markets. Where sometimes domestic markets don't provide the right opportunity, we try and find these bridge products, like the Masala bonds that were created in late 2013, early 2014.

Eventually, these offshore markets are only as good as the domestic markets, because there is an inevitable concern among regulators and policy

The investor base and the amount of savings in the region is enormous

makers that you can never say that money coming from the outside will only be one way. Every time it comes to a sudden halt, it creates a lot of disruption and volatility and has a serious impact on the real economy.

So, while we would like to see one-way growth, less restriction on foreign capital inflows and instruments that allow foreign capital to flow in – including through Masala bonds, for example – there is some understanding among policy makers, and certainly amongst ourselves, that there are some real issues out there. Right now, we are financing about 25% to 30% of our total client financing globally in local currencies.

Asia is, on balance, less challenging than sub-Saharan Africa or other less developed markets. In India, for instance, to pick up on your point on the Masala bonds, since we were able to access that instrument, our India programme literally doubled within the last two years, because that's where the gap and the need was.

To push this forward from here, what we have done recently in the World Bank Group is to establish a group-wide programme called JCAP, short for the Joint Capital Markets Development Programme. Partly this is meant to complement the work that we do from the treasury side to actually then follow through to policy work and regulatory work to make sure that it is embedded in longer term, more stable policies, and that the markets continue to grow.

I think it's an exciting area. It's still growing, as you said, and there are still a lot of challenges ahead.

IFR ASIA: IS THAT PROGRAMME AVAILABLE TO ANY COUNTRY?

MONISH MAHURKAR, IFC: Given, of course, there's always the challenge of resources, the aspiration is to take it to as many markets as possible, but the reality is that we have to begin by focusing on a few select markets. We have picked a mix of the least developed and some semi-developed markets to focus on initially, but eventually we hope to get it across to as many markets as possible.

IFR ASIA: EDDY, LET'S BRING YOU IN ON THIS ONE. WHAT IS IT LIKE FROM A FOREIGN INVESTOR'S POINT OF VIEW WHEN YOU LOOK AT ASIAN EMERGING MARKETS? YOU HAVE TO MAKE A CHOICE BETWEEN HARD CURRENCY, LOCAL CURRENCY, OFFSHORE AND ONSHORE. HOW DO YOU GO ABOUT DOING THAT?

EDDY STERNBERG, LOOMIS SAYLES: That's an excellent question, because we do actually invest both in hard currency and in local currency, through different strategies. Sometimes we mix them, but it's seldom. Both markets have had their challenges lately.

On the hard currency market, you mentioned US$250bn in issuance for this year, a lot of it coming from China, with a large investor base in the region. We're about 12 hours apart from most of the Asian region here in the eastern United States. When we go to bed, they wake up, they go to work. Here comes a company that decides to issue a bond with the help of the capital markets people. They find lots of investors who are willing to pay very little for this debt. We wake up, we say, "Oh, they're issuing, we want to participate." They say, "So sorry, but we already placed the bond." So, everyone there is already invested and we're left out.

How do you resolve that? You have local offices. In our case it's great because we have one, but it still requires a lot of coordination between, in our case, Boston and Singapore. So, that has its challenges. The investor base and the amount of savings in the region is enormous, and the willingness to pay very little is very high. I'm an old-fashioned emerging markets person, so I don't like 3%, 4% yields!

On the local markets, they're rather small in some countries. The two largest ones are China and India, and they're both for the time being harder to access for foreign investors. One is rapidly moving to open

> What's very important for international issuers, underwriters and investors, first of all, is the consistency of the regulatory and government framework behind these markets

itself, not without some details to resolve, and that's where the devil appears.

Let's take India, which is the one that's not opening, although it sort of opened a little bit late last year, or early this year. In the past, you had to pay for the privilege of lending, which is sort of awkward. You have to pay to be able to lend to the government. Not everyone was willing to do that.

IFR ASIA: YOU'RE TALKING ABOUT QUOTAS?

EDDY STERNBERG, LOOMIS SAYLES: I'm talking about quotas, yes. You have to pay to use a quota. You also had to use the quota all the time, and if you stopped using it for 45 days you lost it, and then you had to bid again and pay again. More recently, the quota has been increased and the cost came down until it reached zero. We used that opportunity, but then that night that we invested, it closed. Again, it reached the limit. So, that is a problematic market.

The Masala bond market would help us out with that. But, whether it's Masala bonds or whether it's the Brazilian offshore market or any other market, I've personally learned to dislike them because they are not available to local investors. They're only available to foreign investors, and the foreign investors tend to move in a pack. We all buy at the same time, we all sell at the same time, and it doesn't necessarily reflect local dynamics.

This year, for example, we had the privilege of investing in two bonds in India, because the corporate bond market is actually easier to access. By corporate bond market, I mean more the quasi-sovereign bond market. In that case, we had one Masala bond and one local domestic corporate bond. Interest rates were coming down in India, inflation was coming down, so everything was working out.

The local domestic corporate bond behaved the way we expected it to, so yields came down, so that is a capital appreciation for the investor, it was good. The Masala bond initially didn't do anything, and it took quite a while for it to start behaving like the local bond, and it never accomplished the type of return that the domestic bond market had. So, I don't like it.

IFR ASIA: THEY DO PAY YOU MORE THAN 3% OR 4% THOUGH, DON'T THEY?

EDDY STERNBERG, LOOMIS SAYLES: Yes, in India you do get higher interest rates, but then the currency can depreciate. It's not always on an appreciating trend. That happened late last week, I think.

IFR ASIA: ALEXI, MAYBE THIS IS A QUESTION FOR YOU. HOW DO YOU GET AROUND SOME OF THE INVESTOR CONCERNS WHEN YOU WANT TO ENCOURAGE PEOPLE TO GO TO THE INTERNATIONAL MARKETS?

ALEXI CHAN, HSBC: Yes, I think there are some very interesting issues around the challenges of developing these local markets. What's very important for international issuers, underwriters and investors, first of all, is the consistency of the regulatory and government framework behind these markets. It clearly can be challenging if there are different views on withholding tax, different views on whether local investors can or can't participate in the markets, which can make this more challenging.

We would absolutely like to see – and we are seeing, I think, in certain markets – the authorities taking a concerted step to help build international participation in these markets, recognising that perhaps some of the early requirements on things like withholding tax may be needed to be more flexible to build the markets.

We've talked quite a lot about India. With China, we are seeing some very encouraging progress in the opening up of what is already the world's third-largest capital market, the onshore RMB market. There, the authorities have taken a number of steps to facilitate access for international investors. The early steps were very much quota-based, the QFII and RQFII programmes, and we've had a number of further schemes introduced. The CIBM [China interbank market direct access] was, if you like, the third iteration. Most excitingly, in the middle of this year we had a new scheme called Bond Connect.

Bond Connect effectively allows international investors to get access to the onshore market in China through their existing infrastructure in Hong Kong, without the need to use any quotas or have any infrastructure onshore.

The precursor to this, Stock Connect, was set up with a northbound and a southbound element [allowing money to flow into and out of China]. Bond Connect has started with a northbound route, and our experience in the transactions we've been involved in is that we've seen a significant uptick in participation from international investors and we think that's set to continue.

CHINA SQUEEZE

5Y ONSHORE BENCHMARK YIELD (%)

Source: Thomson Reuters Eikon

The offshore instruments are a bridge to a full scale, fully-open, free-flowing market which connects onshore and offshore players

I think there's a lot of cause to be optimistic. Clearly, for any country to have a sustainable capital market, we do need consistency of regulatory and public policy. We need underwriters to be able to provide liquidity to the international markets, and that's something we've worked hard on with Monish and his team, for example, on Masala, and on Dim Sum before that. I think liquidity provided by market makers is another factor that will support the development of these markets. For HSBC, that's something we're committed to across the Asian region.

IFR ASIA: THERE ARE TWO MODELS HERE FOR INTERNATIONALISATION. THERE'S THE OFFSHORE MARKET, WITH MASALA, DIM SUM BONDS AND SO ON. THEN YOU HAVE BOND CONNECT, WHERE INTERNATIONAL INVESTORS GET DIRECT ACCESS INTO THE LOCAL POOL. WHICH ONE MAKES MORE SENSE?

MONISH MAHURKAR, IFC: Like I was saying earlier, I think the domestic market has to be the primary driver. The offshore instruments are a bridge to a full scale, fully-open, free-flowing market which connects onshore and offshore players.

I can see the gentleman on my right is concerned that Masala, from your perspective, may not work, because if you have direct access to the domestic market, why would you not go there? That's where the liquidity is, that's where the major buyers and sellers are. But then, when we launched the Masala bonds in late '13, early '14, to our surprise at that time, there is still a large segment of investors for whom there are certain other criteria.

I'll just name two or three of them. One, many of the global investors still have fairly stringent ratings restrictions, so they won't buy paper below a certain level, so it helped that we were Triple A. It doesn't necessarily help an Indian company looking to go into Masala, but then later on, as things picked up, there was a market for that credit level as well.

A second factor that came to light is that many investors prefer the standard international GMTN format or Euroclear instruments, which may not be available domestically. A third could be simply administrative. There are more sophisticated fund managers, perhaps such as yourselves, who are willing to go through the registration process, understand the local market's peculiarities and work within that. Then there are those who just won't have the appetite to do that and would just like a standard instrument in the international market.

So, there is a place for both, and I think the Dim Sum bond market played a similar role. We were beneficiaries again – working with partners such as HSBC and other banks – where having access to both markets gave us the advantage to see which one worked, from a pricing perspective, better at any given point in time.

We've had, over the years, situations where the Dim Sum market offered better pricing than the domestic market, and now currently there's more favourable pricing in the domestic market. So, I think in the process of developing these markets, we have to keep an open mind. There is no easy, linear, straight-forward process to developing bond markets from our experience. I think one needs to be flexible.

IFR ASIA: I THINK INVESCO HAS A PRESENCE IN THE ONSHORE CHINESE MARKET ALREADY, BUT A LOT OF INVESTORS HAVE BEEN HOLDING BACK. WHERE IS THAT GOING TO END UP, ARNAB? WE'RE GOING TO HAVE TO GET MORE INTERNATIONAL MONEY IN THERE SOMEHOW, AREN'T WE?

ARNAB DAS, INVESCO: Yes. Invesco has a joint venture in China, Invesco Great Wall in Shenzhen, and we also have an operation in India, Invesco India in Mumbai. So, we have domestic operations, domestic clients, and domestic assets, and some amount of international clients flowing through those operations as well. Like Loomis Sayles and others, we also participate with foreign client money in Masala and Dim Sum, and also directly in the domestic market.

I think we have to think about this in the context of the capital control regime. What's happening, I think, is a gradual sequencing in that both countries at are different points in the sequence of developing their domestic capital markets and gradually reducing the barriers to capital flows. When you start from a situation where you have capital controls, you have, in effect, a distorted capital market.

Not to spend too much time on the Indian case, but in India, the equity market is actually quite open, and the bond market, as we've been discussing, is relatively closed. I personally think that makes the equity market more expensive, and the bond market maybe at times more expensive than it would otherwise be, in the sense that yields are lower and the equity risk premium is lower. You have a lot of capital that's trapped in the domestic market, and the portfolio preferences of the rest of the world for exposure to India are diverted from bonds into equities.

So, many people justify the rich valuations of Indian equities on the basis that India is like a growth stock, which probably has some merit, but I think we have to recognise that there are these distortions.

In the Chinese case, it's very different. We have an enormous amount of wealth and financial assets with resident Chinese investors with something close to 100% exposure to China, who probably want a considerable amount of diversification. The rest of the world has relatively little exposure to Chinese issuers – certainly onshore, and to some extent through offshore and hard currency issuance. So, there needs to be a swap of these exposures. One of the critical questions posed by Bond Connect and Stock Connect is how is that going to work? It's a critical issue for the Chinese financial system, it's a critical issue for the Chinese economy, and it's a critical issue by extension for the world economy because China is so big.

I think we're in a gradual process of feeling out the right sequencing and using examples from history, perhaps somewhat adapted for Chinese circumstances and Indian circumstances, because it's fairly clear nobody is going to flip a switch and give up control and roll the dice come what may. It has to be managed in a very careful way.

If you look back through the history of quote-unquote 'emerging markets', you see some very good cases of this kind of opening where it's worked very well. And you see, of course – not just in emerging

Having a deep capital market that's liquid and has a diverse investor base – both from institutional investors domestically and local currency, and potentially offshore as well in both domestic and foreign currency – is very helpful

markets, but pretty much throughout the developed world – where you've had financial deregulation and liberalisation, you typically get a financial crisis, or at least some financial dislocations after that.

I think the sequencing, going gradually, and along the way dealing with all these frustrations, I think we have to live with that.

IFR ASIA: BILL, ON INDIA, WHEN YOU LOOK AT MASALAS THERE AND THE INTERNATIONALISATION OF THE CURRENCY, IT HASN'T BEEN A COMPLETELY LINEAR PROCESS THERE EITHER, HAS IT?

BILL FOSTER, MOODY'S: Not at all. I was saying earlier it has fits and starts. Just this past summer, you saw that happen. Basically, the regulators closed off the market in June, July, and then in September they reopened it but in a different window with more restrictions, and you have to go to the RBI to request access to the market. For people that know India, this isn't really a surprise. Ultimately, it's a controlled market.

The RBI is understandably very concerned about capital flows, volatility, and how that impacts the balance of payments and the exchange rate. They don't want to be caught in a situation where they have to be on the back foot, which is understandable. The bond market domestically is a product of financial repression. It's ultimately held by banks or large government institutions that don't trade regularly and the yield curve is effectively flat.

There are a lot of sequential issues that need to be sorted out before, ultimately, something like the Masala bond market offshore can develop. They'd first have to be prioritised onshore.

IFR ASIA: AT WHAT POINT DOES THAT FEED INTO A SOVEREIGN RATING? YOU'RE BRINGING IN MORE RISKS, AREN'T YOU, INTO A CLOSED ECONOMY?

BILL FOSTER, MOODY'S: Taking a step back, not necessarily in India but in general, you look at the capacity of the economy to absorb flows in a sustainable fashion. Obviously the external vulnerabilities and level of exchange rates, and how much is foreign currency debt relative to domestic currency debt matters quite a bit in terms of the vulnerabilities there, and the levels of debt and the capacity to assume more debt over time, and how sustainable that is at a very basic level.

Obviously, there's a lot more that goes into it, but having a deep capital market that's liquid and has a diverse investor base – both from institutional investors domestically and local currency, and potentially offshore as well in both domestic and foreign currency – is very helpful. But only if the sequencing is right, otherwise it's destabilising and very risky. That's documented very clearly. So those are things that we look at.

IFR ASIA: MONISH, PERHAPS WE CAN GET INTO SOME OF THE SPECIFICS NOW ON YOUR EXPERIENCE IN OPENING UP NEW MARKETS. WE'VE TALKED ABOUT MASALAS, BUT THERE ARE A NUMBER OF PROGRAMMES, AREN'T THERE, ACROSS THIS REGION?

The effort over the years has been to try and create programmes, customised to specific markets and countries

MONISH MAHURKAR, IFC: Yes. The effort over the years has been to try and create programmes, customised to specific markets and countries, because regulatory frameworks do tend to be different.

In most cases, we try and go in and get a framework to be able to issue bonds within the local domestic market. So, for example, we've done this in Nigeria, we've done it in smaller markets like Rwanda or Costa Rica, we've done domestic Panda bonds in the Chinese market. Even in India, we experimented with a small, what we call a Maharaja bond, just to distinguish it from the Masala bond, which was a small issuance because the pricing didn't quite work for us.

What happens in some of the domestic markets is that – and it's not completely surprising – investors do not differentiate an international Triple A from the Triple A that they would associate locally with their own sovereign. In effect, given that in many of the markets we go in may be just about investment grade or even below, we don't get the pricing advantage that we would like to see. It's a real issue for us because, not being a bank, ultimately we're only able to finance clients based on the cost of funding that we can access in the markets. If local banks have access to much cheaper deposits, then we might remain uncompetitive.

That's the kind of challenge that you face. Secondly, there are also, at times, challenges in terms of just setting up regulatory processes, prospectuses, registrations, documentation, a standardised template for these things.

That, we feel, can be a multi-tiered effort, but I think the investment of that time and effort is worthwhile, because it helps to bring these best practices into the markets.

IFR ASIA: WHEN YOU PUT THESE PROGRAMMES IN PLACE, HOW DO YOU GET AROUND SOME OF THE REGULATORS' FEARS THAT ALL THE MONEY IN THE COUNTRY WILL GO TO THE IFC INSTEAD OF THEIR OWN COMPANIES?

MONISH MAHURKAR, IFC: It's a good question, and sometimes we do have those discussions around this potential crowding out. We of course reassure our member country governments that, first of all, scale-wise, we are not talking about large issuances relative to most markets that we go into. Even for a small market like Rwanda, the size that we would issue, it's more of a catalytic transaction.

It's a demonstration, and it of course helps to finance some of our projects, but it's not going to crowd out even a Rwanda sovereign, let alone a Chinese sovereign or an India sovereign, which is in a completely different league in terms of size. So, it's not a concern in most places, but yes, in some markets, people still fear, partly because the discussions are ongoing that they are uncomfortable having a foreign entity coming in and issuing in that market.

ALEXI CHAN, HSBC: If I could just add a couple of thoughts to Monish's comments. First of all, we have seen some interesting transactions where multilaterals or other Triple A or highly-rated organisations have come into a local market like the Masala market and subsequently done, effectively, a back-to-back financing with another issuer who may want to issue a Masala bond themselves, and where the supranational can act as the anchor investor in that financing.

I think those sorts of back-to-back transactions can be very helpful for market development.

MONISH MAHURKAR, IFC: An interesting point to what Alexi just said, is that the way we have deployed proceeds, for example, in the Masala bond, is actually one of the better examples of how, ideally, things should work. The framework for investing that money is under what we call our foreign portfolio investors licence, so all the financing that we do for our clients in India against our Masala proceeds is through asking our clients to issue bonds in turn. They issue domestic, what are called NCDs in India,

It's a question of opening up a little bit more, making it easier

non-convertible debentures – basically domestically listed bonds.

It also adds to the flow of product in the domestic market. Right now, we have invested in these bonds, but we can also offload and make them available in the secondary market.

IFR ASIA: EDDY, DO YOU THINK IT BRINGS IN MORE INVESTORS? DOES IT CROWD IN?

EDDY STERNBERG, LOOMIS SAYLES: I was thinking as we were discussing, "Who's come to the Masala market on the domestic company side?" It's very, very few. I don't know if it's because the IFC is crowding out – I don't think that's the case. I think it has to do more with the cost of financing. The domestic issuers can get a certain pricing domestically. Once they come to the Masala market, there are all the issues around withholding taxes, which we would not have to pay as investors, but they would have to make up either in the yield or rebating the cost, or something like that.

All of a sudden, the Masala bond does not seem to be as attractive to issuers who can access the domestic market easily. We haven't seen that many issuers, so I don't know that it's a crowding out, or it's a cost, and that's another reason why I dislike the Masala, or specific offshore investor markets.

I'm also thinking of several things that we said here. One is, if you think of emerging market investors before you think of any other type of investor, there are some indices that we follow, especially when it comes to local currency indices. The most prominent one is the JPMorgan GBI-EM Global Diversified. Neither India nor China is part of that index. Currently, if you think of that index and you think of its market cap, it's about US$1.2trn without those two countries. You bring those two countries and that market value is US$2.2trn. China brings in about US$700bn and India brings about US$300bn – not the exact numbers, but to round it up. It is huge.

We talked about Bond Connect, and we talked about the CIBM access – if I've got that acronym right. CIBM was moving very slowly, so they introduced Bond Connect, which makes things much easier, but China is still not part of the index. So, there is a problem. There are some details that have to be worked out. Going through Hong Kong may be easy, but it's somewhat restricted. You're only able to deal with one counterparty at that point in time. That's great for the counterparty, and not necessarily great for us, so again, not many people are investing, not many people are ready. The index provider has not put China in the benchmark yet, and it's not likely to do it this year – maybe next year if things open up.

I think the authorities there understand that they're making progress, but it's not as great as it sounds, at least today. The case of India, we talked about the equity market being very open. I don't quite understand why the Indian authorities are not concerned about the inflows and outflows of equity investors into India. They say, "No, they are stable." If I'm an emerging market investor and my index has 10% of its benchmark in India, will I not be stable? Will I not want to be there at least with 8% or 12%? Those flows are not huge.

Let's think of it this way, in the investments benchmarked against this US$1.2trn index that I mentioned, the foreign investors only have US$220bn. It's a lot of money, but think of India becoming 10% of that, it's US$22bn. Part of it will be sticky, so I really don't see that many inflows and outflows. Again, it's a question of opening up a little bit more, making it easier. Skip all the steps with Masala, Panda, Dim Sum markets. They're uncomfortable.

IFR ASIA: I THINK A LOT OF PEOPLE ARE EXPECTING, CERTAINLY IN CHINA'S CASE, THAT BONDS WILL BE ADDED TO THOSE INDEXES PRETTY SOON.

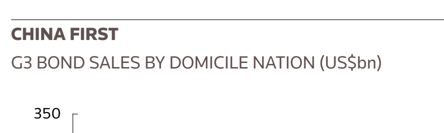
EDDY STERNBERG, LOOMIS SAYLES: Last year, the index providers came around, did a roadshow, and asked, "Who's interested and are you doing anything about it?" And we said, "We're not, but it's going to be 10% of our benchmark." So, immediately after they left, we sent an email and said, "We would like to open accounts in China." This is April of 2016.

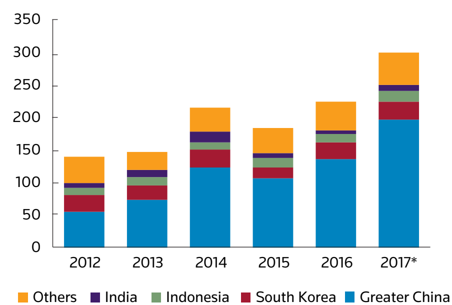
Today, we're having bi-weekly meetings to discuss the opening of the account. We're nowhere close to that yet, so I don't think that's happening any time soon, despite Bond Connect.

IFR ASIA: SO, IT'S NOT FOR LACK OF TRYING? IT'S JUST THE INFRASTRUCTURE IS NOT THERE YET?

CHINA FIRST

G3 BOND SALES BY DOMICILE NATION (US$bn)





*2017 data to Nov 22

Source: Thomson Reuters

I'm an old-style emerging market investor, and low yields are not very attractive to us

EDDY STERNBERG, LOOMIS SAYLES: That's correct.

IFR ASIA: LET'S MAYBE TRY AND TAKE A FEW QUESTIONS FROM THE AUDIENCE, IF WE CAN.

AUDIENCE: I'M BARBARA STALLINGS FROM BROWN UNIVERSITY. THIS PANEL WAS OBVIOUSLY SET UP TO TALK ABOUT DEBT MARKETS, BUT CAPITAL MARKETS DO INCLUDE EQUITY MARKETS. WITH TWO POSSIBLE EXCEPTIONS, MR DAS AND MR STERNBERG WITH CASUAL MENTIONS OF THE INDIAN EQUITY MARKETS, NOTHING.

I WONDER IF ANYONE COULD SAY ANYTHING ABOUT THE EQUITY MARKETS IN ASIA AND HOW THEY LINK TO CORPORATE BOND MARKETS IN THE REGION? THANK YOU.

MONISH MAHURKAR, IFC: I think, partly, the reason why the panel focused so much on fixed income is that most of us are under the impression that, in most of Asia, equity markets are relatively further along in terms of development. They are mostly open. We took the example of India, of Stock Connect in China. It's a bit of a paradox that regulators in general have been much more open and accepting of volatility, inflow and outflows, and openness with equity markets than they have been in the debt markets. Some of that could be because debt markets also get closely linked with monetary policy issues, interest rate issues, FX controls etc., so maybe there is a little bit of regulatory overlap challenges there.

But that's the reason, I think, because equity markets are more open.

ARNAB DAS, INVESCO: If I could just add to that, I would suggest that another very related factor is that, as was said earlier, policy makers prefer stability to instability, for obvious reasons. When the equity market comes under a lot of pressure, equity prices fall, and that's a challenge for the companies, maybe it's for the issuers of equity, it's a challenge for domestic investors. It may not be such a challenge for the entire economy. If the currency falls, while that might be a bit of a problem, it might help with some adjustment to whatever shock is taking place.

But if your bond market is heavily owned by foreign investors, that's different. If you take the case of Indonesia, I believe 40%, or maybe a bit more at the moment, of the Indonesian bond market is held by foreign investors. So it's quite possible that, in the function of Bank Indonesia, keeping that stable is actually quite important.

I suspect that policy makers in a large, politically challenging country like India or possibly even China might have some issues with a lot of volatility in the bond market that transmits directly into the banking system and into the financial system more broadly. That's why I think this whole issue of sequencing is very important, that you get your domestic markets to be as liquid and deep and efficient as you can before you open them up to the vagaries of people like ourselves.

AUDIENCE: HI, MY NAME IS THOMAS PELLERIN FROM IFC WORLD BANK GROUP. UNTIL JUST NOW, ALL WE HEARD IS ABOUT INDIA AND CHINA. OUTSIDE OF THE TWO ELEPHANTS THAT WE MENTIONED, I'D BE REALLY WILLING TO HEAR FROM THE PANEL ABOUT THE TIGERS OF VIETNAM, INDONESIA, PHILIPPINES, MALAYSIA. IT SEEMS TO ME THAT THESE ECONOMIES ARE STILL EXTREMELY PROTECTIVE IN TERMS OF CAPITAL INFLOWS. ARE WE SEEING A LITTLE BIT OF ONE STEP FORWARD, ONE STEP BACKWARDS? OR SOMETIMES TWO STEPS BACKWARDS? I'M HAPPY TO HEAR FROM THE PANELS ON THESE SPECIFIC ECONOMIES.

EDDY STERNBERG, LOOMIS SAYLES: If I may, the one step forward and two steps backwards is very prevalent in the region. Malaysia is a case in point. It's also very important in our emerging market benchmarks. It was quite open. Actually, the ownership of foreigners was much higher than that in Indonesia. It was probably around 60% at some point in time, maybe even higher than that.

For some reason, Bank Negara decided that that was not convenient. It had a currency which is quite controlled to begin with, and put in steps that make it less attractive for investors to participate in the market. You could hedge if you needed to hedge, then it became a little bit less restrictive but it was not quite clear, to the point where the benchmark or index provider decided to not keep adding new bonds as maturing bonds come out.. They decided not to include new bonds that were coming into the universe, issued by the government, and that's an issue for us.

That's maybe another thing we should have been discussing, but not something that makes investors very happy. We shy away from those markets. The smaller markets are not part of benchmarks and we're still interested. Sri Lanka is a market that we've participated in. On Vietnam, as I said before, I'm an old-style emerging market investor, and low yields are not very attractive to us. Vietnam doesn't pay very high yields in its domestic market.

IFR ASIA: MONISH, WHEN YOU LOOK AT FRONTIER MARKETS IN ASIA AND AROUND THE WORLD, HOW DO YOU DECIDE WHEN THEY READY TO START ENGAGING INTERNATIONAL INVESTORS?

MONISH MAHURKAR, IFC: Again, it's challenging, and we find a whole spectrum of countries out there who are willing to look at this. I already mentioned this example of Rwanda, which is actually surprisingly open-minded, although the market is really undeveloped, very basic. But we have actually managed to issue a Rwandan franc bond in the domestic market and an offshore Rwandan franc-linked instrument. Of course, in these markets, these tend to be isolated and one-offs. It's just a way of starting the process, but it takes time.

There's a discussion ongoing in markets like Nepal, where we have some projects coming up in hydropower and we would be happy to issue a Nepalese rupee bond, and we have some framework of approvals there. We're in discussions around going into Bangladesh and Sri Lanka, it's just that it takes time to make the policy-makers comfortable, and some of those issues around crowding out and finding a balance between different

We're happy to engage, as long as there are projects to finance and there are regulators who are open-minded

priorities acquires a little more profile there, so you have to be a little more careful.

I think we're happy to engage, as long as there are projects to finance and there are regulators who are open-minded.

BILL FOSTER, MOODY'S: I cover several Asian frontier markets, and I would just add that you never have the perfect situation coming to market, but you want to ideally do it from a position of strength, where the policy framework is sound, debt leverages are relatively low, fiscal policy is under control, and ideally you have a flexible exchange rate to absorb shocks. That's not always the case.

You want to at least have the conviction to be able to do the right things and the agreement from a political and economic perspective that, if things get challenging, you'll have policy responses that will be generally prudent. You don't want to be put in a difficult situation moving forward just because you've issued and gone to the market.

If you look at places like Sri Lanka, like Mongolia, like Pakistan, these are very interesting markets, but they also suffered issues over the last few years in terms of accumulating a lot of debt. There have been issues around foreign currency debt because of depreciation. So, these are very important things for governments to consider before going to the market because it will get increasingly difficult for them moving forward if they don't do it in a responsible fashion.

ALEXI CHAN, HSBC: If we think broadly about what we're trying to achieve here, it's quite multi-dimensional. We've talked a lot about how we can bring international investors into the Asian capital markets, and that dimension is similar but not identical to the currency angle we've talked about.

Clearly, the biggest developments we've seen in the last five years have been around a large dollar denominated bond market growing up in Asia with significant participation from international investors – be they in London, in Boston, or closer to home in the region. The third dimension, which we haven't really talked about today, is actually the development of a true credit market in Asia. I think this ties in to the point about equity versus debt.

We've actually seen a lot of international investors want to take a view on the currency via their participation in local government bonds, so the 40% foreign participation that we're talking about in Indonesia is largely a rates and currency position, rather than a credit position. From our perspective, the credit dimension has also progressed pretty well, largely in hard currency, so this year we've seen a range of issuers come to the high-yield international bond market. We've seen infrastructure financings out of Indonesia, in the IPP space, out of India, in the airport space.

I think developing a credit market in Asia is also as worthy a goal as developing a local currency market and as bringing in international investors. Now, how these three dimensions line up at any one time will depend on the progress we make on each of them, but all of them are worthy of pushing forward, and I think it would be a mistake to judge the overall picture by insisting on trying to cover all three of these dimensions in every financing.

The market's view on China today is significantly more positive than perhaps when we were all gathering for these meetings 24 months ago

I think on each parameter we've made significant progress, and as the region opens up and becomes more intertwined, I think there's a lot of cause to be optimistic.

AUDIENCE: I'M FROM CHINA, SO I WOULD LOVE TO KNOW YOUR OPINIONS AND VIEWS TOWARDS THE CHINESE FINANCIAL MARKETS. HOW DO YOU FORESEE THE RISK IN THE HIGH LEVERAGE IN CHINA'S DEBT MARKET?

THE SECOND QUESTION IS ABOUT THE CHINESE EQUITY MARKET. DO YOU UNDERSTAND THE REAL REASON BEHIND THE 2015 STOCK MARKET MELTDOWN? THE THIRD QUESTION IS ABOUT INTERNATIONALISATION OF CHINESE MARKETS. WHAT ARE THE NECESSARY CONDITIONS TO LET THE CHINESE REGULATORS FEEL COMFORTABLE TO LOOSEN THEIR CAPITAL CONTROLS? THANK YOU.

ARNAB DAS, INVESCO: Three very easy questions!. First, on the debt ratios and the leverage problem, it clearly is a challenge. We haven't seen these kinds of rates of credit growth in most countries for some time. What has improved in the last couple of quarters is that the ratio of credit to GDP has stabilised. That seems to be not because credit growth has slowed down sharply, but because nominal GDP growth has accelerated quite a lot because producer price inflation has picked up.

Nominal GDP growth in 2015 – when people were really scared about this – was quite low. There was quite a lot of doubt about the real GDP growth numbers, and PPI was in deflation. So, credit was growing quite rapidly, and the denominator was growing much less rapidly so that debt ratios seemed to be on an explosive trajectory which, among other things, was quite worrying. Since then, like I say, the nominal GDP growth rate has picked up.

People say there's been deleveraging, or at least a slowdown in the growth rate of leverage, and I guess what they really mean is in the total stock of debt. It doesn't appear that TSF – Total Social Financing – has actually slowed down. The problem will probably be contained if China can keep nominal GDP growth up, if it's choosing not to slow down TSF, which it appears not to be willing to do. Assuming growth is a very important target, as it seems to be, I think we can expect that to continue.

Is that going to lead to a credit problem, or some sort of event in the banking system? Well, there's certainly reason for concern, but what I would suggest here is that, unlike many other countries where those kinds of challenges have become a crisis, a lot of this is taking place within the state sector. You have a number of state-owned banks lending to a number of state-owned enterprises and you have a quasi-fiscal guarantee there. I think the Chinese people and Chinese firms and banks understand this.

So, in some sense, that's stabilising. I'm not suggesting that it's ultimately a good thing or the right thing to keep that arrangement. But it will probably allow for much higher ratios of debt to GDP than in many other quote-unquote emerging market countries.

IFR ASIA: JUST TO WRAP UP ON CHINA, BECAUSE WE HAD A LOT OF OTHER HANDS UP THERE, IF CHINA OPENED THE CAPITAL BORDERS TOMORROW, ALL THE MONEY WOULD FLOW OUT, WOULDN'T IT?

ALEXI CHAN, HSBC: Steve, I'm not sure that's really the right question. From our perspective, this is a huge exercise that China is undertaking to reform its economy, to gradually open up the capital market, and to make the transition to more private sector entities and world-beating companies. We're already seeing many successes in technology and other sectors.

From our perspective, the market's view on China today is significantly more positive than perhaps when we were all gathering for these meetings 24 months ago. We're seeing the foreign exchange reserves go up, the currency has appreciated. In terms of the point about liberalisation, really, this needs to be done at the appropriate pace for the Chinese financial system.

I think some of the teething issues that we've talked about in terms of how investors and issuers can get access to the domestic market are inevitable elements of that gradual opening up, which has to be the case for this market to happen in a conducive way for China.

BILL FOSTER, MOODY'S: The other important factor, to add to what you're saying about growth and deleveraging is you also have to see a restructuring of state-owned enterprises so that they become more efficient over time, because this is very credit-intensive growth. If you look at the ICOR ratios, it's very inefficient. For a nominal level of GDP growth to be able to bring down that debt over time, you need to see greater efficiency in the allocation of each dollar of capital.

That would be an important aspect of the reform agenda, as we're all aware, and how that pans out will certainly be a big deciding factor in how the deleveraging story plays out.

AUDIENCE: I'M A PRIVATE EQUITY INVESTOR IN ASSET MANAGEMENT COMPANIES. WHEN YOU THINK OF TIMING, I WOULD LIKE YOUR GUESS IN TERMS OF HOW MANY YEARS UNTIL CHINA'S AND INDIA'S MARKETS ARE LIQUID, OPEN. AND I'M TALKING ABOUT CREDIT MARKETS, NOT THE FX MARKET WE HAVE TODAY. I KNOW I'M ASKING A LOT, BUT IS IT THREE, FIVE, SEVEN, 10 YEARS?

MANY FUND MANAGEMENT COMPANIES ARE THINKING ABOUT BUILDING PRODUCTS FOR THEIR END INVESTORS, AND THEY DON'T KNOW REALLY HOW TO PLAN FOR IT, BECAUSE THEY'VE BEEN TOLD THAT THESE MARKETS WILL OPEN UP FOR YEARS.

EDDY STERNBERG, LOOMIS SAYLES: I won't venture a number, but despite everything I've been saying, we've seen China really moving very, very fast. I wouldn't be surprised if it's a handful of years as opposed to two hands. In the case of India, it's true. We've heard about the opening of their markets for probably 10 years now, and it's always two years down the road.

We're very much alive to how new processes and new technology can help link issuers and investors around the world in the most efficient manner

IFR ASIA: DOES ANYBODY ELSE WANT TO TAKE A STAND WITH A NUMBER?

MONISH MAHURKAR, IFC: I'm not sure if it's the right way to look at emerging markets in general, because it's a long process. In some ways, the opportunity for fund managers, I don't think in these markets is a case of waiting to see when they fall neatly within an index, and you can build simple products to offer investment opportunities in these markets.

I think, for a while to come, you have to look at these more as alpha opportunities, not as index opportunities. That's where I think those who are alive to those opportunities are already exploiting them. I don't think they are waiting to create products when these markets will be fully set up because it's not a linear path.

BILL FOSTER, MOODY'S: I'll say one thing about India. I don't have a number for you, but what you can look at to get a sense as to when they may move is really the fiscal deficit and the debt levels in the system. They need to finance that in an affordable way and, ultimately, they use the banking system to do that.

When they're in a more comfortable fiscal position moving forward, that's when I think you might see more space for reform.

AUDIENCE: I'M WONDERING IF OUR PANELLISTS COULD SAY A LITTLE BIT ABOUT THE STATE OF PLAY OF THE FORWARD MARKETS AND THE ABILITY OF INVESTORS TO HEDGE IN THESE MARKETS, IN TERMS OF SPREADS, SIZE –PARTICULARLY IN SOME OF THE SMALLER MARKETS LIKE PHILIPPINES, MALAYSIA, AND SO ON.

EDDY STERNBERG, LOOMIS SAYLES: It's not great. When I think of an open market, an easy market to do all these things, both to invest and to hedge and use forward markets, think of Mexico. It's outside the region, but it's a good example also of a market that opened up fast with a good, local investor base with growing pension funds and foreign participation. It opened very, very fast from 1996, where it had a three-month T-Bill. By 2006, so not even 10 years later, it had a 30-year bond. Foreign participants helped a lot. They had the ability to invest just the same way as local investors, but also the ability to use all these instruments to hedge. Despite it being so open, it went through a crisis. 2008 was a huge crisis that affected Mexico, not as an internal intrinsic crisis, but as an external one, and it fared quite well. Even in the 2013 taper tantrum, it all worked. It doesn't work that well in most Asian countries.

AUDIENCE: THANK YOU. MY QUESTION IS ACTUALLY IN REGARDS TO DISTRIBUTED LEDGER TECHNOLOGY, THE DLT AND BLOCKCHAIN SPACE. THERE HAVE BEEN RECENT ADVANCEMENTS THAT SHOW IT CAN NOW OFFER SCALE, INVESTOR PROTECTION, AND EASE THE FLOW OF CAPITAL COMPARED TO A LOT OF TRADITIONAL FINANCIAL INSTRUMENTS. CHINA IS NOW TALKING ABOUT LAUNCHING A FEDERAL BLOCK CHAIN CURRENCY IN AS EARLY AS 2019. HOW DO YOU SEE DISTRIBUTED LEDGER TECHNOLOGY IMPACTING GLOBAL FINANCIAL MARKETS AND THE LIQUIDITY OF CAPITAL IN THE NEXT THREE TO FIVE YEARS?

ALEXI CHAN, HSBC: Well, we've seen the use of some of this technology in some of the European markets. Already in the private placement markets we saw one of the large German company issue a Schuldschein instrument using this sort of distributed ledger technology. I think the potential for simpler processes and efficiency to be brought into capital markets is absolutely there, from a technology point of view.

From my perspective, we're very much alive to how new processes and new technology can help link issuers and investors around the world in the most efficient manner. One can't assume that the current approach of bookbuilding, roadshows, distribution of offering memoranda via Bloomberg and other existing technology is going to remain the way that the markets do business.

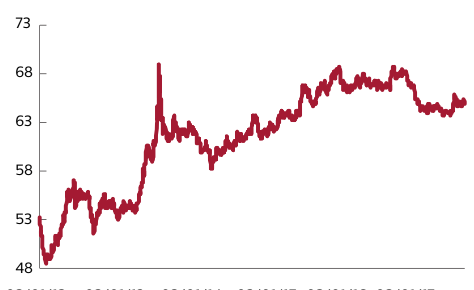
Whether we're talking about changes to the efficiency of how we can connect specific investors to specific financing requirements, or whether we're talking about a fundamental shift in the markets, to me is the critical question. Clearly there are efficiency gains in how we do business.

We've invested, for example, in a platform that gives investors direct access to the bookbuilding process, so we're cutting out a number of stages that, frankly, were not adding significant value to the overall execution of a placement.But it remains to be seen exactly how technology is going to fundamentally change the game.

AUDIENCE: HOW DO YOU GET GLOBAL PENSION FUNDS TO LOOK AT EMERGING MARKETS, BECAUSE

ROCKY RUPEE

INDIA'S CURRENCY HAS STABILISED SINCE THE 2013 'TAPER TANTRUM' (RS/US$)



Source: Thomson Reuters Eikon

Risk mitigation is key for foreign investors looking for a higher rating

THE RATING ITSELF IS A CONSTRAINT? WHAT WE NEED IS LONG-TERM MONEY. HOW DO WE WIDEN THE INVESTOR BASE?

ARNAB DAS, INVESCO: If I could start, my impression is that there's quite a lot of institutional investor interest, from pension funds, sovereign wealth funds, endowments, you name it. I think many of them are quite active. We have significant amounts of institutional client money of those categories that has been very active in emerging markets for quite some time.

Actually, since the GFC, that interest has, if anything, grown quite significantly because we're in a low growth, low inflation world. Maybe we're not talking about old-style emerging market yields, but if you want higher yields than are on offer in the developed world, that's where you're going to go.

MONISH MAHURKAR, IFC: For pension funds and for long-term insurance investors, it plays a bit differently from the kind of discussion we had today about investors looking for a combination of rates and FX, which is more a short- to medium-term play. For pension fund investors, it's about stable, long-term cash flow.

I think the best fit to my mind is the infrastructure investment opportunities in markets like India, China, Brazil, Mexico, or even the next tier of developing markets. That's a less bond-friendly play, but there are again intermediate instruments that can help us get there.

One instrument which we've had some success with in the last couple of years is something we call a managed co-lending portfolio programme. Over the past year, we have signed up about four or five global insurance funds, where they will co-invest with us in a diversified portfolio of infrastructure assets. This is infrastructure loans, so it's not in a bond format.

Another instrument, where you've seen some effort but haven't had as much success – at least so far – is this idea of an infrastructure bond. You can get an infrastructure company to issue a bond, but then to meet the ratings threshold, somebody has to step in, either a development institution or another commercial financial institution, to wrap the credit. From what we've experienced, at least during the construction phase of the project when the risk is very high, most pension funds would not take that kind of construction risk at the greenfield stage.

So there are, again, some instruments which are beginning to make an appearance, but it's early days.

AUDIENCE: HI, THIS IS NIPA SHETH FROM TRUST GROUP, INDIA. I HAD A QUESTION AROUND THE INFRASTRUCTURE MARKET. WHEN WE SEE MASALA BONDS, OR EVEN WHEN WE SEE FOREIGN INTEREST IN THE DOMESTIC MARKET, MOST OF IT IS IN AAA, SHORT MATURITIES, OR SOVEREIGN RISK. HOW DO YOU OPEN UP A MARKET FOR FINANCINGS WHICH ARE SLIGHTLY LOWER THAN AAA? INDIA HAS A HUGE NEED FOR INFRASTRUCTURE FINANCING, AND MANY OF THESE PROJECTS MAY NOT BE GREENFIELD – THEY'RE ALREADY MATURE. IS THERE ANY WAY ONE CAN ADDRESS THIS IN EITHER MASALA BONDS OR THROUGH FOREIGN INVESTMENT?

BILL FOSTER, MOODY'S: As you're probably aware, a lot has been done on this front over the last few years, in infrastructure investment funds, IDFs. There's a whole lot the government has done over the last 10 years to focus on ways to bring specifically long-term money into infrastructure in India. You need credit enhancement, you need to have foreign exchange hedging to mitigate the risk there.

Then the question is, who's going to provide sovereign guarantees? Is it going to be the government or is it going to be a tripartite agreement with some kind of government authority? It gets a bit complicated, because ultimately these become more costly, but risk mitigation is key for foreign investors looking for a higher rating.

I know the government has talked in the past to multilaterals about providing guarantees as well. The issue around it, though, is it becomes more expensive for the issuer and for the government to provide the assurances that foreign investors need for it to be deemed safe paper. That's what I've seen, at least.

MONISH MAHURKAR, IFC: On infrastructure, the upside is that it's a classic, ideal asset for long-term investors because once it goes operational, it's steady cash flow. But to get there, the issues around the greenfield, construction stage do create lots of complications.

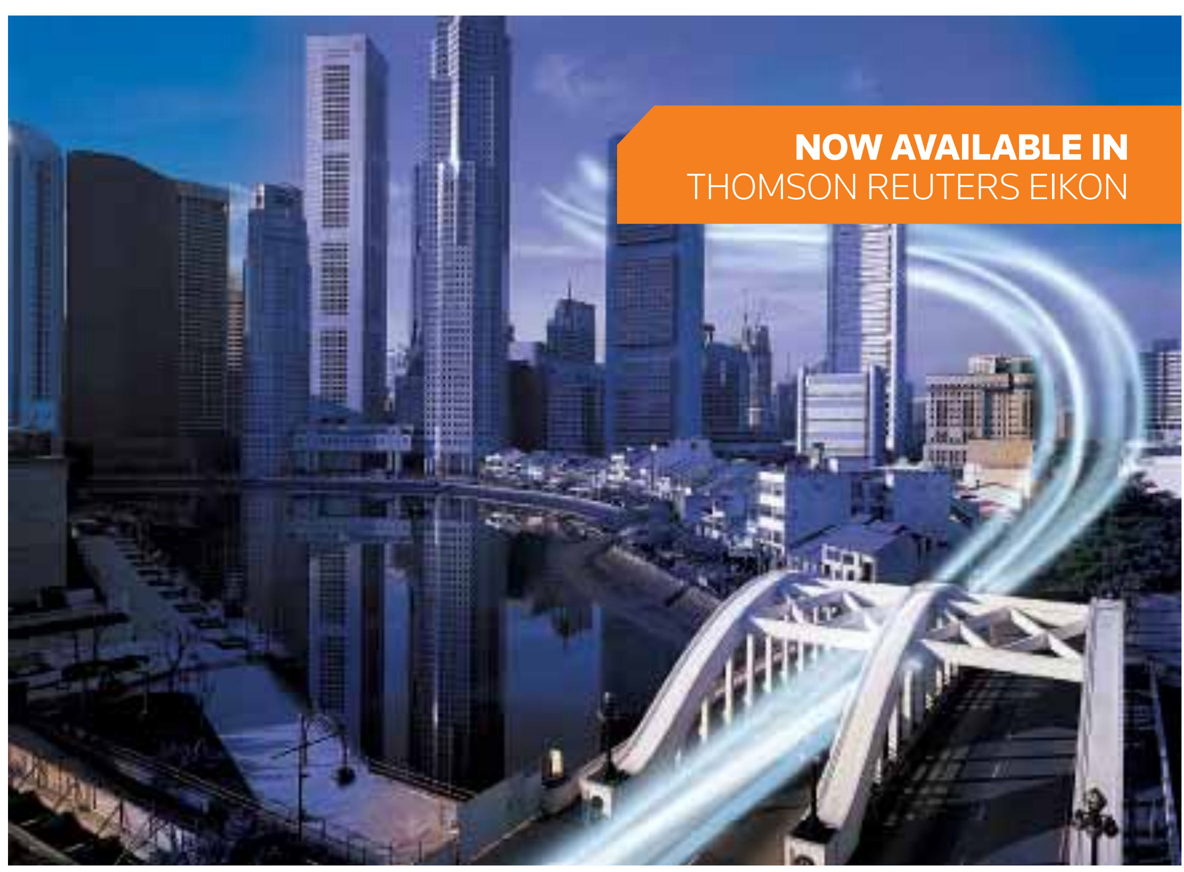
The other aspect is that, to connect it back to the capital markets, there is a certain amount of stabilisation of cash flow that you need to create. A typical infrastructure project follows its own curve, with disbursement over a period of time and then amortisation etc. Those are some challenges that I don't think have been fully overcome yet.

ALEXI CHAN, HSBC: On the hard currency side, we've actually seen some quite interesting transactions this year in the infrastructure space that leave me feeling quite encouraged. So, in airports, we've been involved in a very large financing for the new Mexico City Airport, and this involved a mix of loan and bond financing, and the bond financing had very long tenors out as far as 30 years.

Closer to home, I mentioned earlier in the energy space in Indonesia, we structured an investment-grade financing for PT Paiton Energy, which was really the first large-scale project bond out of Asia. By using project finance techniques to mitigate some of the challenges that Monish has mentioned, we managed to achieve a Triple B rating and access very long-dated money in the international markets.

I think it's important to sometimes distinguish the currency elements and the credit elements, and I think infrastructure is actually an exciting space where there are a range of techniques out there. Whether all of those will play out in the local markets with international investors, we'll see over time, but certainly the space has advanced quite significantly this year.

IFR ASIA: LADIES AND GENTLEMEN, WE ARE OUT OF TIME. THANK YOU VERY MUCH FOR SOME GREAT QUESTIONS, AND PLEASE JOIN ME IN THANKING OUR PANEL. ●



IFR ASIA: AT THE HEART OF ASIA'S CAPITAL MARKETS

IFR Asia is the world's most authoritative source of Asian capital markets intelligence, providing in-depth coverage on every significant issue across all asset classes.

Established in 1997, it draws on IFR's global editorial team – the largest of any capital markets publication with bureaux throughout the region – to provide the most reliable news, data and analysis there is.

IFRAsia.com takes this unrivalled content and combines it with new search functionality, enhanced navigation and intraday updates to create the perfect business development tool for the region's investment banking professionals.

To learn more about how you will benefit from IFR Asia's market-leading intelligence, visit www.IFRAsia.com

A THOMSON REUTERS SERVICE

Best in class? Ask the experts...

Acknowledgement from leading organizations is an honor and these achievements reflect our commitment to high quality expertise in both global and local markets. From in-depth market knowledge to thought leadership and leading customer service, these attributes lie at the heart of everything we do and highlight our dedication to financial markets.

Get more details and see our full collection of awards at moodys.com/awards

© 2017 Moody's Investors Service, Inc. and/or its licensors and affiliates. All rights reserved.