

# Multilateral development banks local currency lending and cross-border de-dollarization initiatives

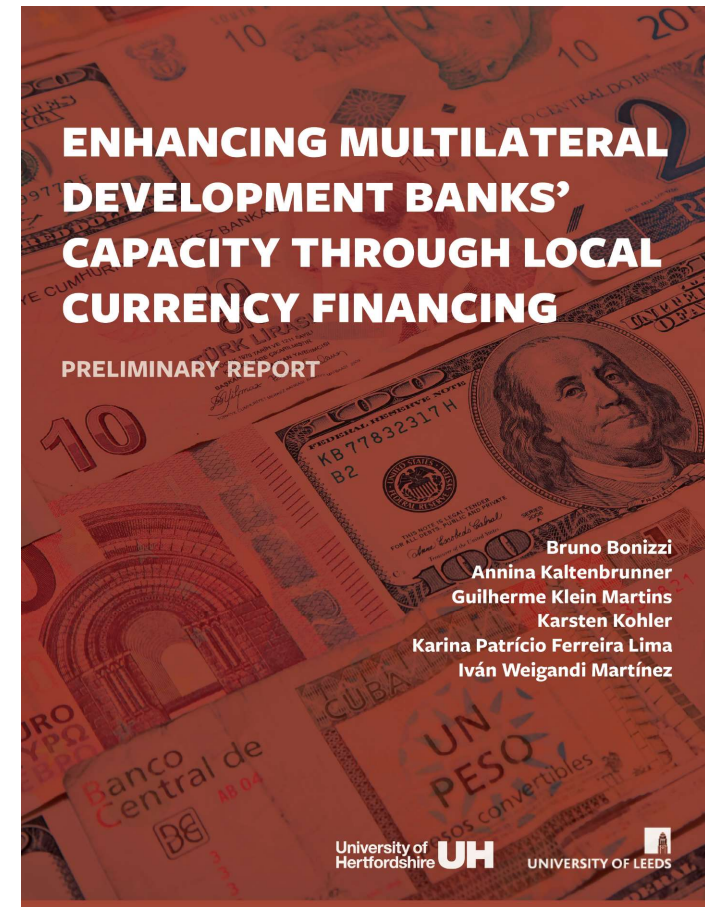
---

**Annina Kaltenbrunner**  
University of Leeds  
[a.kaltenbrunner@leeds.ac.uk](mailto:a.kaltenbrunner@leeds.ac.uk)



# Introduction

- Insights based on extensive research report funded by the Multilateral Development Bank Challenge Fund and ongoing work on cross-border de-dollarization
- Starts from premise that foreign currency dependence and financing is a key driver of financial fragility and debt problems in developing countries – medium to long-term costs!
- Multilateral Development Banks (MDBs) – and Development Finance Institutions (DFIs) more generally – key agents to reduce debt vulnerabilities
- SDGs financing gap is about USD 4 trillion per year – Need sustainable forms of finance!



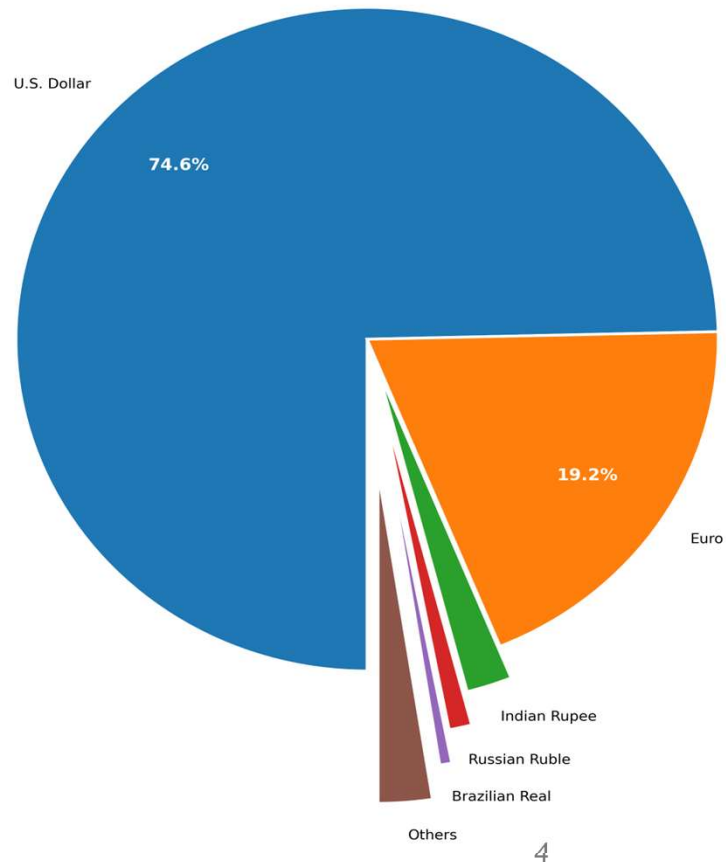
## Our Report (together with Dr Bonizzi - University of Hertfordshire, and Drs Ferreira Lima, Kohler, and Kleins Martin, University of Leeds)

---

- **What are the key risks and barriers to scaling up local currency financing by MDBs and how can we address them?**
- **Methodology and core chapters:**
  - Secondary data, semi-structured interviews and survey with MDB treasurers, legal counsel and risk managers to map local currency lending practices and key barriers (Chapter 2)
  - Secondary data and legal analysis to identify legal, credit, and currency risk of local currency lending (Chapters 3-5)
  - Panel-data econometrics of a large sample of low and lower-middle income country currencies to assess risk of large depreciations (tail risk; Chapter 4)
  - Policy recommendations on how to scale up local currency financing (Chapter 6)

# The lack of local currency lending by MDBs

Share of Top Deal Currencies (by amount)

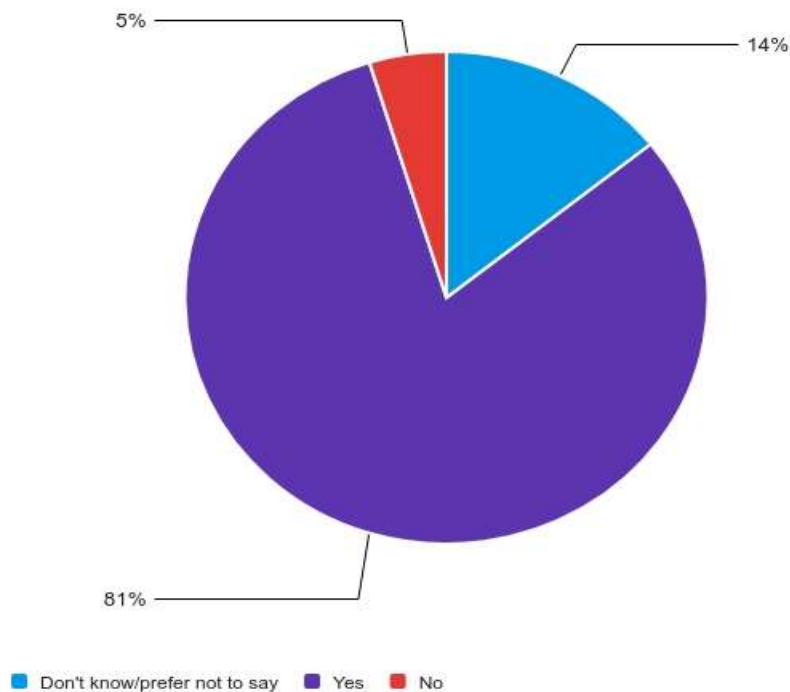


*Note: The graph shows currencies' percentage share in syndicated MDB loans*

*Source: WRDS-Reuters DealScan Database*

# The willingness of local currency lending by MDBs

Do you think your organisation should provide (more) financing in local currency to developing countries?



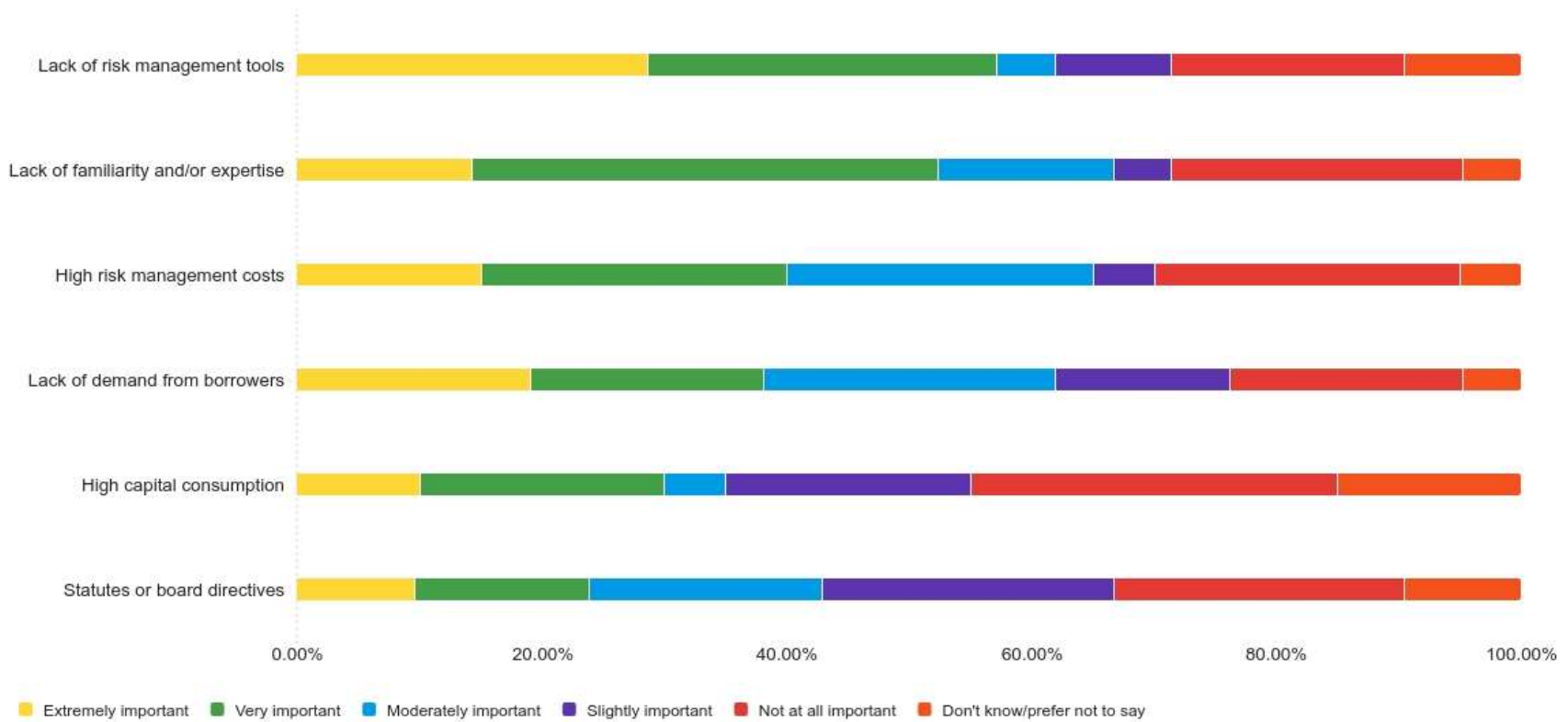
MDBs provide loans, guarantees, equity investments in local currency

## Benefits of LC lending:

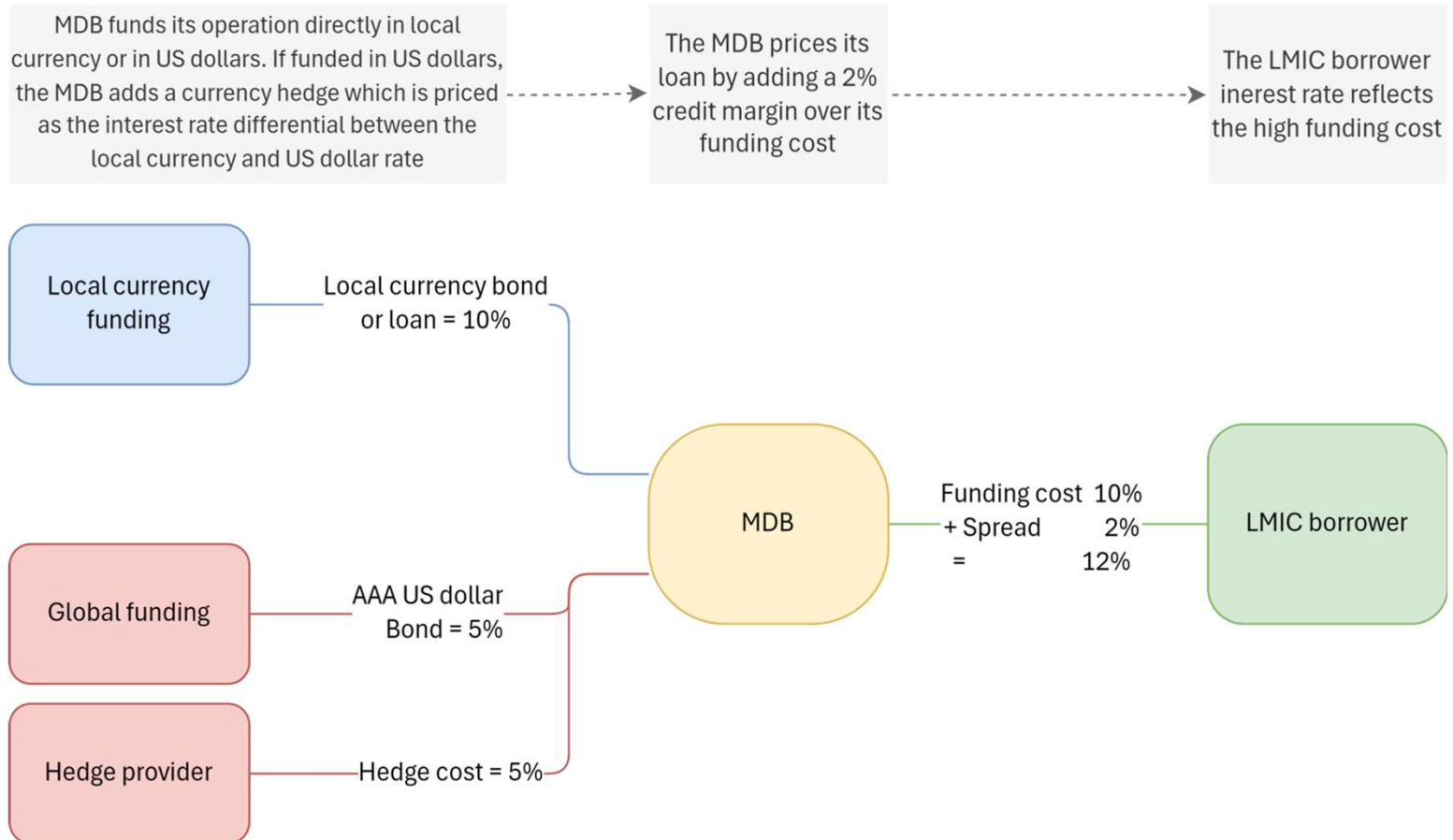
1. Removes currency risk from vulnerable borrowers
2. Cashflows from climate mitigation/adaptation investment is often in local currency (e.g. energy)
3. Higher development impact

# Key Findings: Barriers to local currency financing by MDBs

How important are the following factors as barriers to local currency financing?



# Key Findings: The pricing problem



## Policy Recommendations

---

### **How can multilateral development banks (MDBs) play a transformative role in promoting local currency financing?**

1. Bring local currency lending to the core of the developmental mandate of MDBs
  - Develop capacity in local currency borrowing and lending
  - Enhance the quality and availability of information on MDB local currency lending
  - Reassess back-to-back risk management frameworks and strict counterparty rules
2. Scale up and enhance means of hedging currency risk
  - Scale up and subsidize the currency exchange fund TCX
  - Country-specific hedging mechanisms



## Policy Recommendations

---

### How can multilateral development banks (MDBs) play a transformative role in promoting local currency financing?

#### 3. Promote onshore local currency operations

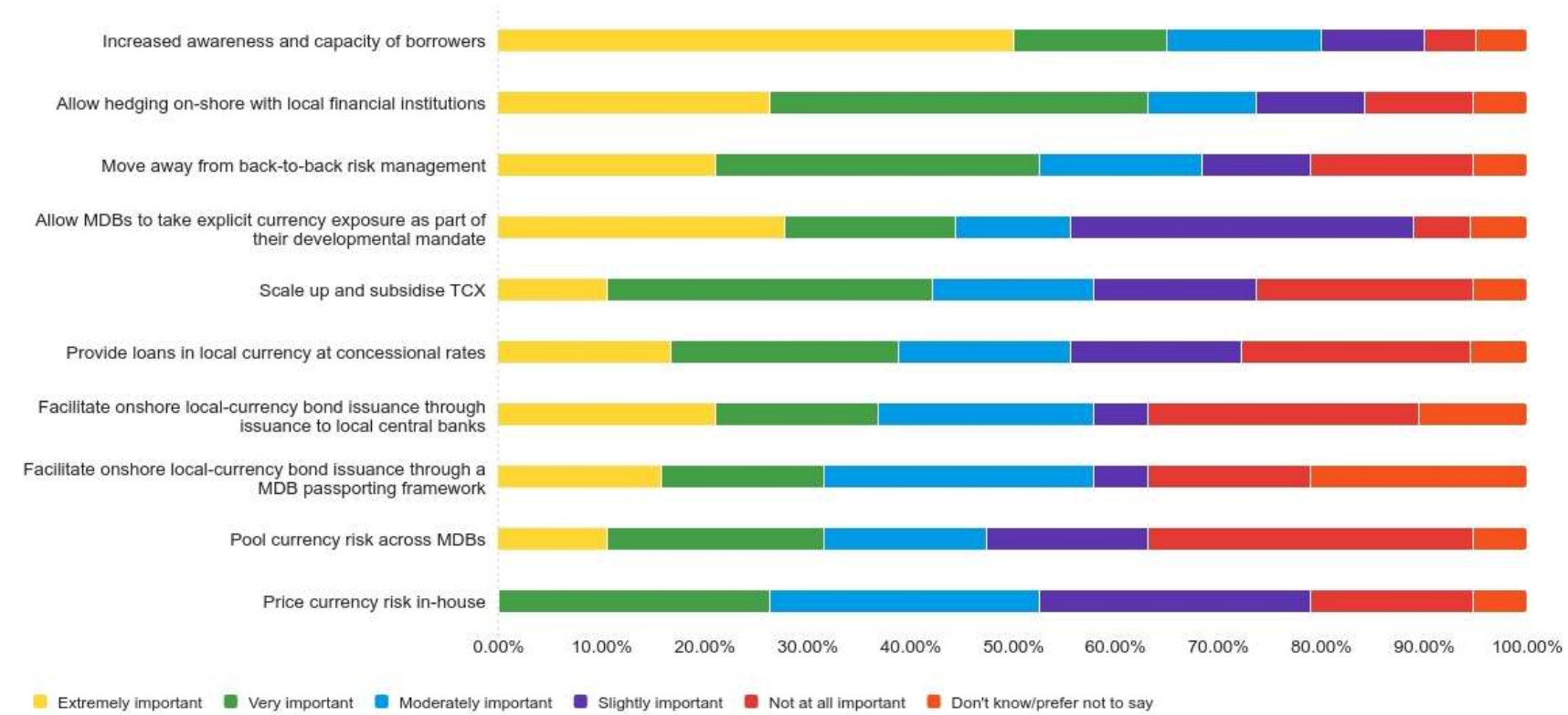
- Onshore liquidity platforms (issue debt to domestic central banks)
- Harmonised transnational legal and regulatory framework for MDB operations

#### 4. Address the pricing problem directly

- Reflect lower credit risk of local currency financing (involve credit rating agencies)
- Provide concessional local currency loans
- Take on some – limited and carefully priced – currency risk
  - off-balance sheet fund (e.g. EIB ACP Investment Facility)
  - risk-sharing scheme to protect MDBs against large depreciations (needs donor capitalization; SDRs)

# Key Policy Recommendations: MDBs View

In your opinion, what would be the most important changes needed to increase local currency financing?



## Cross-border de-dollarization initiatives (together with Prof Fritz, Free University Berlin; Dr Orsi, University of Leeds, Dr Zucker-Marques, Boston University)

---

(Cross-border) de-dollarization attempts that target different money functions:

1. Unit of account and means of payment in trade: Trade invoice and settlement currencies
  - Regional payment systems
  - Payments infrastructures
2. Store of wealth: Stable investment currencies
  - Regional liquidity pools
  - Swap agreements
  - **Local currency lending (e.g. by regional Development Finance Institutions)**
3. Unit of account and means of payment in finance: Funding currency
  - **Development finance institutions** or non-national private and public financial institutions **issue local currency financing**
  - Trade finance in regional currencies

## Regional de-dollarization attempts

- Need of state support and international development finance institutions (new forms of external vulnerability)
- Need of complementary development of money functions
- Hierarchy of money functions (credit vs. non-credit functions)
- Regional and Global South hierarchies

