INTERNATIONAL CAPITAL MARKETS

Peter Montagnon interviews Eugene Rotberg, the World Bank's treasurer.

Moving towards a simpler way of funding

THE WORLD BANK has long been established as the largest single borrower on international bond markets, but now, according to Mr Eugene Rotberg, its treasurer, its paper is becoming scarce.

In its current fiscal year ending June 30, 1987 the bank plans to borrow only $9bn, he said in an interview at last week's annual meeting in Washington. This is down on last year's $10.6bn, and the lowest borrowing total since 1982.

The reasons for this decline are well known. They reflect a parallel slowdown in disbursements by the bank to its developing country clients as well as its record level of liquidity which stands at just over $20bn or 56 per cent of outstanding loan commitments at the end of 1985-86.

This has constrained borrowing at a time ironically when the market can scarcely be more favourable.

"We would like to borrow large sums at the present rate," Mr Rotberg said. The problem is that there is no need to do so, and one aim of the bank at present is to reduce its liquidity to around 50 per cent of loan commitments. Even then it will still be above the basic target level of 40 to 45 per cent.

Temporary decline

Mr Rotberg believes that the decline in the bank's borrowing requirement may be only temporary. Towards the end of the current fiscal year its needs may start to rise again as fresh loan projects are put on its books.

For the time being, however, the World Bank is in a very strong position vis-a-vis the market. It does not need to develop fancy new instruments to titillate the jaded appetite of investors. This year's borrowing programme will concentrate on classic, long-dated plain vanilla instruments. Mr Rotberg says the World Bank was "constantly importuned" with offers of finance during the annual meeting last week, but "we want 20, 30 and 40-year fixed-rate funds. We are rejecting most of everything else."

Meanwhile, the bank's efforts at innovation for which it is well known in financial markets are now being directed to the management of its liquidity. It plans soon to propose to its board a new scheme which will dramatically change the way it's liquid assets are invested.

At present it is not permitted to invest in securities with a life to maturity of more than five years and three months. If the changes go through there will be no such restriction.

This is because the bank would move to a new concept whereby the duration of its liquid assets portfolio would be limited to a range of three months to four years.

Duration is a technical market term. It is basically the weighted average maturity of the investment portfolio calculated on a cash flow basis. It gives, for example, different maturity values to zero-coupon and fixed-rate bonds expiring on the same date because the entire return on the former is concentrated at the end of its life.

Duration concept

Moving to a duration concept will greatly enhance the scope of the bank in managing its liquid assets as it will be able to buy high yielding long-dated instruments provided the purchases are matched with an equivalent amount of short-term paper.

The bank is also to seek permission to use interest rate futures and options in managing its liquidity, though initially only on dollar and sterling instruments. Further down the road it is also looking at using the futures and options market to provide protection for its clients on the currency and interest rate risks they run when borrowing from the bank.

In the long run all this means that its basic approach to financial management can become simpler. Mr Rotberg calls this "unbundling innovation." Instead of lumping all sorts of bells and whistles together in one bond issue, these innovations, which are basically designed as hedging mechanisms, can be separated out and dealt with at a different stage of the process with counter parties to whom they are a natural part of their everyday business.