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World Bank Devises a New Method to Raise Cash

By Carl Gewirtz
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PARIS — Driven by an expanding appetite for money to lend to developing countries, the World Bank announced in Washington late Tuesday that it plans to step up its borrowing activity and to use new methods to raise cash.

In what may be the institution's most far-reaching innovation, the bank said it would experiment with adapting the structure of the short-term commercial-paper market to the long-term bond market.

Commercial paper are IOUs that are sold daily through dealers for any maturity, usually not longer than one year, and at a price that buyer and seller find mutually acceptable. Bonds are securities bearing a fixed coupon and a stated maturity that are first sold to underwriters who then distribute the paper to investors.

The World Bank's innovation, called Continuously Offered Long-Term Securities, or COLTS, straddles the features of both markets. It has named four dealers to initially market in the U.S. domestic market up to $500 million of 3-to-30-year paper. Investors will be free, as in the commercial-paper market, to chose any maturity within the spectrum that fits their desire.

The interest payment dates on all maturities of paper would be identical, but the rates negotiated. The bank, on a daily basis, will quote yields at which it is willing to offer paper in amounts ranging from $25,000 to $10 million.

The World Bank uses the interest rate on U.S. Treasury securities as the benchmark rate for its own. Through the COLTS method, the bank can direct demand to the maturities it prefers by offering the paper it wants to sell at a higher margin, or spread, over comparably dated Treasury paper.

The World Bank's treasurer, Eugene Rotberg, said that the program will provide "sustained access to the U.S.-dollar borrowings in the domestic market and further diversify the tools available to the bank for managing its liability portfolio." Ultimately, Mr. Rotberg expects to expand the program by including zero-coupon securities and floating-rate paper.

The continuous sale will enable the bank to take advantage of daily rate fluctuations, issuing more paper when rates are deemed attractive, he said.

The method has other cost benefits. Underwriters, because they assume a financial risk in buying bonds from the issuer and then trying to market them, charge much higher fees than do dealers, who simply attempt to put buyer and seller together.

Mr. Rotberg, in a telephone interview, estimated this saving at about ¼ percentage point.

The innovation coincides with a decision by the bank's board to expand this year's borrowing target by $1 billion. The bank had aimed to raise $9.6 billion or its equivalent, as the bank issues paper in all the major currencies, of which $9.2 billion has already been completed.

This reflects both the anticipated increase in the bank's own lending operations this year as well as Mr. Rotberg's view that this is an especially favorable time to be issuing bonds, with yields in all major currency sectors at nearly 10-year lows. Mr. Rotberg commented that "rates in a year are not likely to average as low as they are now."

As the initial borrowing target for the fiscal year ending June 30 is almost completed, the World Bank would have been out of the world's capital markets for about four months — missing the opportunity to lock in current low rates.

The increase, however, is not all opportunity driven. Mr. Rotberg estimated that the bank's borrowings in the fiscal year starting July 1 may total $11.6 billion and said that, "we can expect the increases in borrowing to be repeated in subsequent years" as the bank steps up its own loan disbursements.

Another significant change in the bank's borrowing strategy concerns the swap market. The World Bank has been an innovator in developing swaps. Mr. Rotberg estimated that from mid-1981, when it arranged its first currency swap, to the end of last year, the World Bank has engaged in 182 swap transactions with 49 different counterparties for an amount equal to $6.3 billion.

In a typical swap arrangement, one borrower, who would prefer Swiss francs but is able to raise

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funds more cheaply in dollars, would swap his debt with another borrower, who wants dollars but is able to raise money more cheaply in francs. The two issuers swap their debts, dividing the savings.

The tremendous increase in swap-related transactions, which a Salomon Brothers study recently estimated at $20 billion last year, has ironed out the anomalies that gave rise to this arbitrage, making it ever more difficult to arrange such accords.

As a result, the World Bank announced Tuesday that it will no longer limit its swap counterparties to only triple-A rated entities. By extending the range of acceptable counterparties to single-A and double-A credits, the bank immediately widens the range of arbitrage opportunities.

At the same time, of course, it also widens the risk that the counterparty might fail. Thus, the bank announced that it has arranged with Aetna Casualty & Surety Co., itself a triple-A-rated credit, to insure the swap risk on these lesser-rated counterparties.

Morgan Guaranty Trust, which established Euroclear, the first settlements system for the trading of Eurobonds, has been named by the World Bank as the transfer agent to clear all of its insured swap transactions. Both swap parties will make payments to the bank, which then will disburse the appropriate funds to each party.